



## MONETARY POLICY COMMITTEE STATEMENT

---

### ***Monetary Policy Rate adjusted upwards by 50 basis points to 8.5%***

*At its February 15 - 16, 2021 Meeting, the Monetary Policy Committee (MPC) decided to adjust the Monetary Policy Rate upwards by 50 basis points to 8.50%. This has been necessitated by the escalation in inflationary pressures, which are pushing inflation further away from the upper bound of the 6-8% target range<sup>1</sup>. The decision balances the need to contain rising inflation and anchor inflation expectations against the efforts made to support financial system stability and growth. Ensuring that inflation remains well anchored in the medium-term is essential to moderate fragilities in the financial sector and support economic recovery. In addition, the implementation of a strong fiscal policy adjustment, whose key parameters are clearly outlined in the Government's Economic Recovery Programme, is critical in restoring macroeconomic stability.*

### ***A strong recovery in the global economy expected in 2021***

As anticipated, the global economy contracted in 2020 on the back of lockdown measures to contain the COVID-19 pandemic. The lockdown measures caused severe disruptions to global supply chains and resulted in a slump in consumption and investment spending. Consequently, global real GDP is estimated to have shrunk by 3.5%. However, a strong rebound to 5.5% in 2021 is projected. This recovery is on the back of policy support and the gradual easing of restrictive measures owing to the anticipated widespread COVID-19 vaccination. In the medium-term, growth is projected to be uneven and highly uncertain contingent on the extent of economic damages, effectiveness of policy support and severity of the current health shock. ***Indicators of domestic economic activity point to a less severe contraction, but weak recovery projected in the medium-term***

High frequency indicators of domestic economic activity point to a less severe contraction in real GDP in the last half of 2020 following the partial relaxation of COVID-19 restrictions. Nearly all the monitored indicators in the [\*Bank of Zambia Survey of Business Opinions and Expectations\*](#) improved over the third quarter readings. In addition, the [\*Stanbic Bank Zambia Purchasing Manager's Index\*](#) also signalled a softer deterioration in the private sector business environment.

---

<sup>1</sup> The forecast period or horizon is eight quarters ahead, that is, the first quarter of 2021 to the fourth quarter of 2022.



In 2021 and the medium-term, domestic real GDP is projected to recover supported by positive growth in mining, electricity, gas and water as well as information and communication sectors. However, uncertainty surrounding the resurgence of COVID-19 infections and the narrow fiscal space pose significant downside risks to this growth outlook. This is consistent with the weaker [\*January 2021 Stanbic Bank Zambia Purchasing Manager's Index\*](#).

### ***Inflation accelerates and deviates further away from target***

Annual overall inflation accelerated to a four-year high in the fourth quarter of 2020. This was largely driven by the sustained depreciation of the Kwacha, reduced seasonal supply of some vegetables and the fish ban. Inflation rose to a quarterly average of 17.6% from 15.7% in the preceding quarter. Food inflation averaged 17.2%, up from 15.2% while non-food inflation rose to 18.0% from 16.2%. Inflation increased further to 21.5% in January 2021 from 19.2% in December 2020.

Over the next eight quarters, inflation is projected to deviate further away from the upper bound of the 6-8% target range due to the lagged pass-through from the depreciation of the Kwacha and sustained high fiscal deficits. The risks to the inflation outlook are assessed to be tilted to the upside. Inflation is bound to accelerate further if crude oil price increases persist, fiscal deficits turn out to be higher than projected and the exchange rate depreciates further. Inflation may be moderated by improved supply of food and subdued aggregate demand as economic growth is likely to remain modest.

### ***Overnight interbank rate held within the Corridor***

The overnight interbank rate declined further to a quarterly average of 8.06% in the fourth quarter of 2020 from 8.57% and was contained within the Policy Rate Corridor of 7.0% to 9.0% throughout the period. This was largely attributed to the accommodative monetary policy measures implemented earlier in the year.

### ***Demand for Government securities weakens***

Demand for Government securities weakened as investor appetite reduced. Both Treasury bills and Government bond auctions were undersubscribed with the bid amounts falling short of amounts on offer by 20.0% and 70.0%, respectively. However, funds raised from the

auctions were adequate to cover maturities resulting in a marginal surplus of K0.3 billion. Additional securities were issued through private placements mostly to finance the Farmer Input



Support Programme (FISP) and partially clear fuel arrears to suppliers. Consequently, the stock of Government securities rose by 9.7% to K130.2 billion.

At end-December 2020, Government securities held by non-residents increased by 30.9% to K18.4 billion, representing 14.1% of the total securities. Ninety-three percent of these holdings were in Government bonds.

### ***Interest rates continue to decline***

Market interest rates continued to trend downwards, influenced largely by the accommodative monetary policy stance. The commercial banks' average lending rate declined to 25.1% in December from 25.7% in September. The savings rate for 180-day deposits also reduced to 9.8% from 10.3%. Similarly, the composite yield rate on Treasury bills declined to 21.2% from 22.7%. The composite Government bond yield rate, however, rose to 32.9% from 32.3%, reflecting weaker demand for longer-dated instruments.

### ***Credit to the private sector moderates further, but money supply continues to expand***

Credit to the private sector moderated to 8.5% in December, year-on-year, from 13.8% in September due to strict lending conditions as banks sought to curb elevated credit default risk. However, credit to Government continued to grow at a strong pace underpinned by issuance of Government securities, particularly for procurement of agricultural inputs under FISP and clearance of fuel arrears to suppliers. This continued to contribute to the sustained strong annual growth in money supply (M3)<sup>2</sup>, at 46.4%, in December 2020.

### ***Fiscal pressures persist***

Fiscal pressures remained high as revenue fell due to the COVID-19 shock amidst rising expenditures especially on agricultural inputs, health and clearance of arrears. Fiscal consolidation remains challenging given the significant uncertainty about the evolution of escalating COVID-19 infections and the debt restructuring process. Narrowing the fiscal deficit by ramping up revenue whilst rationalising expenditure, and restructuring of

Government debt remain critical to restoring fiscal and macroeconomic stability. Securing external sector support will be central to this effort.

---

<sup>2</sup> M3 comprises currency in circulation, Kwacha deposits, and foreign currency deposits.



### ***Current account surplus narrows***

Preliminary data indicate that the current account surplus was sustained in the fourth quarter, supported by strong balance on goods performance. The current account surplus, however, narrowed to US\$0.6 billion (3.3% of GDP) from US\$0.7 billion (3.7% of GDP) in the third quarter. This was largely explained by the widening of the primary income account deficit due to the pay-out of earnings to non-resident shareholders, particularly in the mining sector.

The balance on goods surplus edged higher by 5.2% to US\$1.1 billion as the growth in exports outpaced imports. Exports rose by 2.7% to US\$2.4 billion supported by copper export earnings that rose on account of higher average realised prices and volumes. However, earnings from non-traditional exports, gold and cobalt declined. Merchandise imports rose by 0.5% to US\$1.4 billion following an increase in consumer and capital goods which more than offset reductions in raw materials and intermediate goods.

### ***Depreciation of the Kwacha accelerates***

Rising excess demand continued to characterise the foreign exchange market due to higher import requirements for petroleum products and agricultural inputs under FISP. Consequently, the Kwacha weakened against the US dollar by 9.4% to an average of K20.71/US\$ in the fourth quarter compared with 3.3% depreciation in the third quarter.

In response, the Bank of Zambia scaled-up interventions to moderate pressure on the exchange rate. The Bank sold US\$339.8 million compared to US\$148.5 million in the third quarter on a net basis. This included receipts of all statutory tax obligations by the mining companies.

Gross international reserves declined by US\$117.7 million to US\$1.2 billion (equivalent to 2.4 months of import cover) at end-December 2020 from US\$1.3 billion at end-September (equivalent to 2.3 months)<sup>3</sup>. The decline was largely on account of foreign exchange interventions and debt service.

---

<sup>3</sup> Despite the reduction in the level of reserves, the months of import cover remained broadly unchanged, explained by a further reduction in imports of goods and services following the weakening of the Kwacha.



### ***The MPC Decision***

The MPC noted the escalation in inflationary pressures which are pushing inflation further away from the upper bound of the 6-8% target range. This is despite aggregate demand remaining

subdued. In the medium-term, growth is expected to recover albeit at a weak pace given the uncertainty surrounding the resurgence of COVID-19 infections and the narrow fiscal space.

The risks to the inflation outlook are assessed to be tilted to the upside. These include persistent increases in crude oil prices, higher than programmed fiscal deficits and a further weakening of the Kwacha against the US dollar.

In view of this, the MPC **decided to raise the Monetary Policy Rate by 50 basis points to 8.50%**. The decision balances the need to contain rising inflation and anchor inflation expectations against the efforts made to support financial system stability and growth. Ensuring that inflation remains well anchored in the medium-term is essential to moderate fragilities in the financial sector and support economic recovery. In addition, the implementation of a strong fiscal policy adjustment, whose key parameters are clearly outlined in the Government's Economic Recovery Programme, is critical in restoring macroeconomic stability.

The Bank stands ready to adjust the policy rate upwards further should inflationary pressures persist.

**Decisions on the Policy Rate will be guided by inflation forecasts, outcomes, and identified risks, including those associated with financial stability and the COVID-19 pandemic.**

The next MPC Meeting is scheduled for May 17 - 18, 2021.

Issued by

Christopher M. Myunga  
**GOVERNOR**