FOR IMMEDIATE RELEASE

JULY 2014

MONETARY POLICY STATEMENT

BACK TO BASICS
Setting the tone for Zimbabwe's Economic Recovery

BY

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INTRODUCTION

1. My maiden Monetary Policy Statement is issued, in terms of the Reserve Bank of Zimbabwe Act [Chapter 22.15] Section 46, at a time the nation is seeking for solutions to deal with the challenges besetting the economy. I feel greatly honoured to have been given the opportunity to serve the country as Governor at this juncture in the history of Zimbabwe. At a time the nation needs to work as a team to confront the challenges facing the economy. We are in it together as a nation. We cannot be bystanders. We need to put in place bold and pragmatic measures for the recovery of the economy. This is our motherland where no one else is going do to it for us. We are by ourselves. **We are the people whom we have been waiting for.**

2. It is undeniably clear that the indisputable panacea to the challenges that the economy is facing is to stimulate **PRODUCTION** for economic recovery through pursuing consistent, transparent and predictable economic policy measures. This compels the nation to go **BACK TO BASICS** in order to effectively tackle the challenges.

3. We need to increase production of goods and services in this economy in order to increase economic growth, employment, exports, tax revenue, tax base and liquidity. Economic growth is key to economic prosperity and poverty reduction. Zimbabwe has come a long way and too many things have happened and said about this country, good and bad ones. **We now need to move forward without looking backwards.** Whatever made us to be where we are today should now be treated as history. The time to move forward to achieve the goal of economic prosperity is now. **It's doable. We can do it. We must do it.**

4. It is against this backdrop that this Monetary Policy Statement, which takes into account the objectives enunciated in the economic blueprint, Zimbabwe Agenda for Sustainable Socio-Economic Transformation (ZimAsset), is being presented to give impetus to economic recovery as was recently proclaimed by His Excellency, the President, Cde R. G. Mugabe.

5. The solutions being proffered in this Statement require **a TEAM ZIMBABWE Approach** and **BACK TO BASICS values/principles** to pursue the ZimAsset shared vision of **"Sustained Growth of the Economy for the betterment of Zimbabweans" and to become a middle income country by 2020.** The BACK TO BASICS values include;

    Respect of the rule of law;
    Respect and love of each other as patriotic Zimbabweans;
    Respect the environment;
    Policy clarity, consistency, transparency and predictability;
    Nurture positive business culture;
    Nurture productive work ethics and culture to take responsibilities;
    Visible fight against corruption, smuggling and profiteering;
    Inculcate a culture of paying (bills, loans, duties, etc); and
    Good citizenship.

6. As Monetary Authorities, we are confident and optimistic that the above back-to-basics and discipline principles are achievable. We have, as Zimbabweans, done it before and there is no reason to think otherwise. We need to be positive and minimize negativity in order to turn around the fortunes of this economy. The challenges we are facing as a nation are not insurmountable.

CONTEXT OF THE ECONOMIC CHALLENGES

7. The current challenges facing the economy are so intertwined that sometimes it is not so easy to separate the causes from the effects of the challenges. It is however important that the challenges are properly contextualised and diagnosed in order to come up with solutions that are appropriate and relevant to underpin economic recovery.

8. The interwoven economic challenges include the following:

   Tight liquidity conditions;
   Company closures;
   Rising formal unemployment;
   Low production levels;
   Non-performing loans; and
   Disproportionate trade balance.

9. An analysis or diagnosis of these economic challenges shows that the economy failed to hold on to the strong positive economic growth trajectory stimulated by the liberalization of the foreign exchange system in 2009 because of the nation's failure to attract significant foreign financial inflows (both foreign direct investment [FDI] and long term lines of credit) into the economy to sustain and replace the short term expensive loans that were granted by the local financial institutions at the commencement of the multiple currency system.

10. **The above phenomenon is compounded by the shortermism syndrome that has crept into the economy coupled by the glaring lack of discipline across the economy to do things in the right manner, high**

gearing (high debts), the general laissez-faire attitude, the concomitant crisis of expectation bedevilling the nation and the quick buck syndrome that has its origin from the hyper-inflationary era of the Z$/US$ arbitrage opportunities, the "burning period" when getting rid of the Zimbabwe dollar, or burning, became the key to survival.

11. This unfavourable scenario is depicted in Figure 1 which is split into two phases.

12. **Phase I is the euphoria phase, 2009-2011, the growth phase,** ushered in by the introduction of the multiple currency system in 2009. During this phase, businesses and individuals rushed to obtain bank credit to expand (restocking, retooling, etc) their businesses which had been starved of cash during the hyper-inflationary era and the period, 2000 – 2008, of economic decline (shown in Figure 2). Indeed banks responded by extending credit and the economy grew rapidly between 2009 and 2011 by an average of 10 % per annum. Unfortunately the expansion in credit to support the needs of business and individuals was done by utilizing highly priced short term funding to purchase long term assets, thereby creating unsustainable funding mismatches. The funding mismatches were done on the assumption or expectation that this phase was going to continue or that it was sustainable leading to many businesses going to the extent of adjusting salaries and wages to higher levels than what the economy could absorb. **The rapid economic growth was, to the contrary, short lived as shown by the plateau in 2011 in Figure 1.**

13. **Phase II, 2012 to date, is the reality check or a self-adjustment phase,** wherein the **economy is being chocked** with businesses now saddled with

high debts, high cost of doing business characterized by high finance charges, high labour costs, antiquated or obsolete plant and equipment and the scarcity of long term international financial inflows. This adjustment phase or process has resulted in company closures, thus necessitating retrenchments, low production, high imports, narrowing tax base/revenues and the deceleration in economic growth.

14. **It is this current phase that needs urgent attention for the recovery of the economy which is the bedrock of this Monetary Policy Statement.**

Figure 1

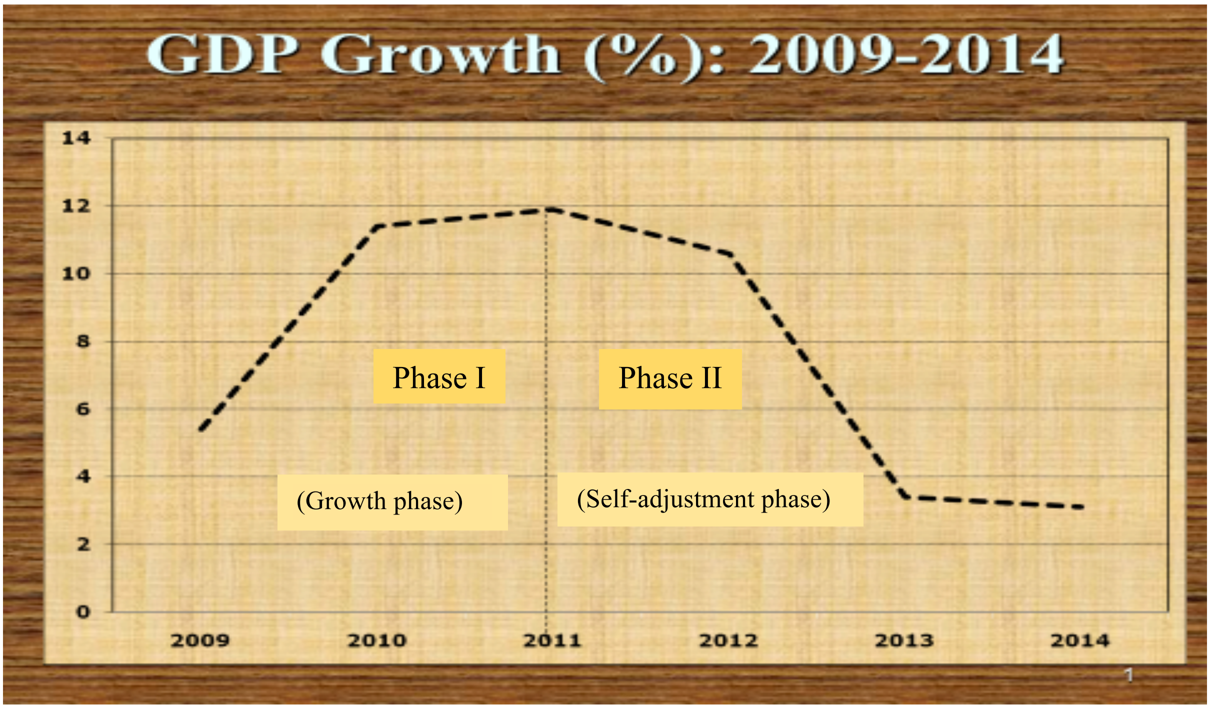
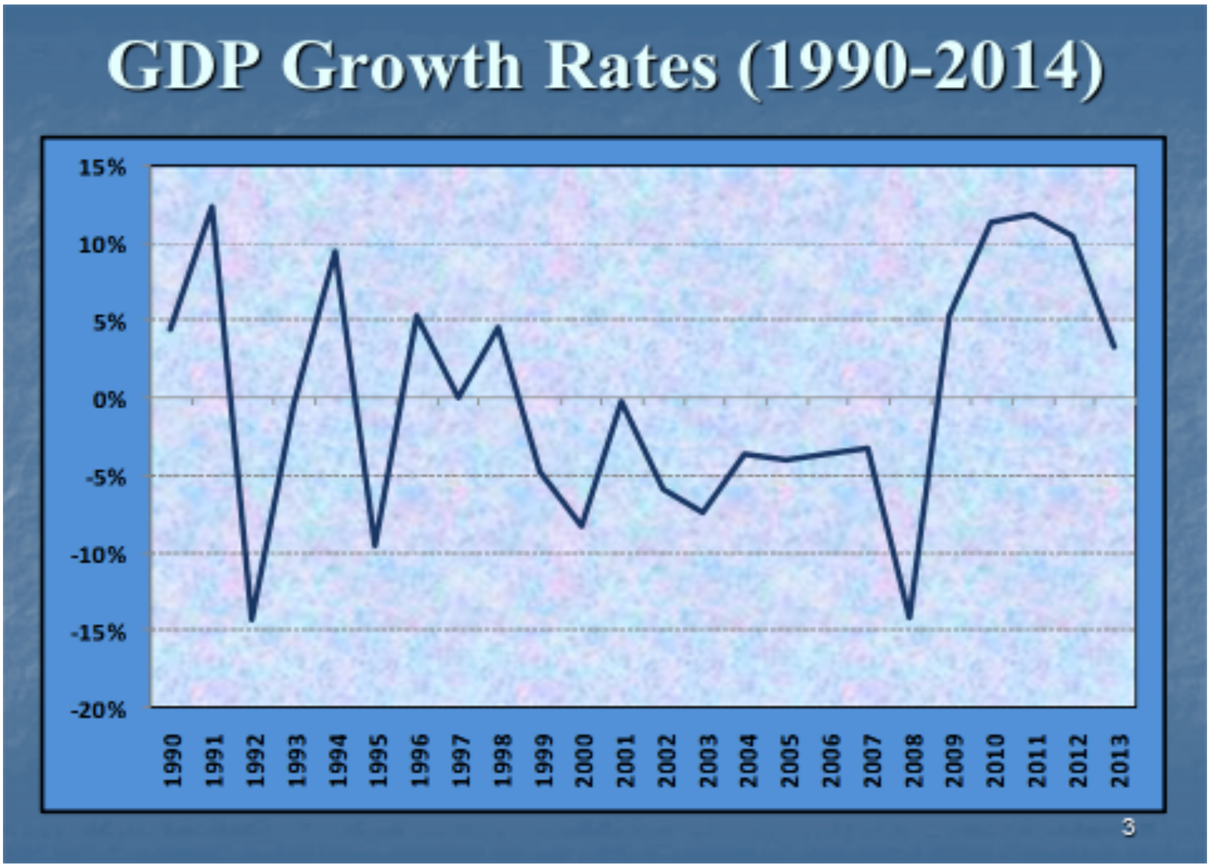


Figure 2



SALIENT SOLUTIONS TO THE CHALLENGES

15. Having graphically analysed the causes and effects of the current economic challenges, it is evident that the solutions to the challenges that the economy is facing are **to putting in place credible, consistent and predictable investment polices to stimulate growth.** This would need to be complemented **by dealing with the high debts or non-performing loans saddling the economy, mobilization of financial resources, inculcating self- discipline,** transparency and accountability across the board.

16. This Statement is, therefore, intended to spell out the necessary bold, robust and pragmatic monetary policy measures that we believe are needed

to pull the economy from the situation it is now, guided by the philosophy that **when a Central Bank wins or loses a fight, it is the wider society which wins or loses.**

ROLE OF RBZ UNDER THE MULTIPLE CURRENCY SYSTEM

17. Our ambition is to make the Central Bank return to its glory and help to stimulate economic activity in an increasing integrated world economy. In doing so we shall only be looking backwards for lessons and looking forward for solutions.

18. We are repositioning ourselves by going back to the **core principles or functions of central banking, which are basically to be banker to Government, administrator of the national payment system, regulator of financial institutions, manager of Exchange Control, supervisor of bank use promotion & suppression of money laundering, lender of last resort and policy advisor to Government.**

Banker and Financial Advisor to Government

19. With effect from 7 July 2014, the role of the Bank as the banker to Government was restored by moving the exchequer account from CBZ Bank to RBZ. The process was done smoothly.

20. As the agent for the State in terms of issuance of Government securities (bonds and Treasury Bills [TBs]) RBZ has issued a cumulative total of US$406 million TBs since the beginning of the year with the bulk of the TBs pertaining to the RBZ debt takeover program by Government. It is pleasing to note that Government has been able to settle all TBs (US$213

million since 2013) timeously on maturity including capital and interest on TBs that were issued in 2012 in lieu of statutory reserves.

Regulator of Financial Institutions

21. The Bank supervises banking institutions and promotes the smooth operation of the payment system in Zimbabwe through on-site and off-site surveillance. From time to time the Bank issues various guidelines to financial institutions to promote discipline and compliance within the sector. Under this function, RBZ through the Registrar of Banks issues and revokes banking licences.

Administrator of the National Payment System

22. The Bank also promotes the smooth operation of the payment system through administering the National Payment System (NPS). The Bank is the administrator of the Real Time Gross Settlement System (RTGS) known as the Zimbabwe Electronic Transfer and Settlement System (ZETSS) and the Central Securities Depository System (CSD). NPS approves all new products relating to the payment system **including mobile banking products.**

Manager of Exchange Control

23. As the steward of the Exchange Control function, the Reserve Bank is responsible for managing and regulating all foreign exchange receipts and payments for the country. The Bank supervises Authorised Dealers (banks) in the implementation of exchange control rules and regulations. The Bank also promotes foreign investments into Zimbabwe and ensures that such investments are sufficiently protected.

Supervisor of Bank Use Promotion & Suppression of Money Laundering

24. As the supervisor of the national bank use promotion and suppression of money laundering function, the bank promotes the use by the public of financial institutions for the purposes of mediating, facilitating or obviating cash transactions and to discharge the functions of supressing money laundering. Under this function, the Bank is currently conducting, with relevant stakeholders, a suppression of money laundering National Risk Assessment exercise to identify, analyse and measure money laundering risks in the country.

Lender of Last Resort

25. The Bank's current challenge here is to be pragmatic enough to find alternative tools to stimulate the economy within the given operating environment of the multiple currency system. To this end, RBZ is earnestly working on mobilizing financial resources to enhance liquidity within the economy. As one of the Bank's key objectives under the back to basics strategy, the **resources being mobilized would be utilised transparently and productively for the establishment and promotion of the lender of last resort function to assist solvent banks to stimulate economic development in the economy. Such funds would not be available for use by errant banks to finance their nefarious activities.**

RBZ UNDER ZIM ASSET

26. The objective under ZimAsset of a continuous economic growth of 7.3% on average per annum is commendable and achievable if we, as a nation, put concerted effort to attract investment, both local and foreign, in order to stimulate production. As alluded to in the blue print, the attainment of the objectives in ZimAsset requires **"robust and prudent fiscal and**

monetary policy measures to buttress and boost the implementation of ZimAsset".

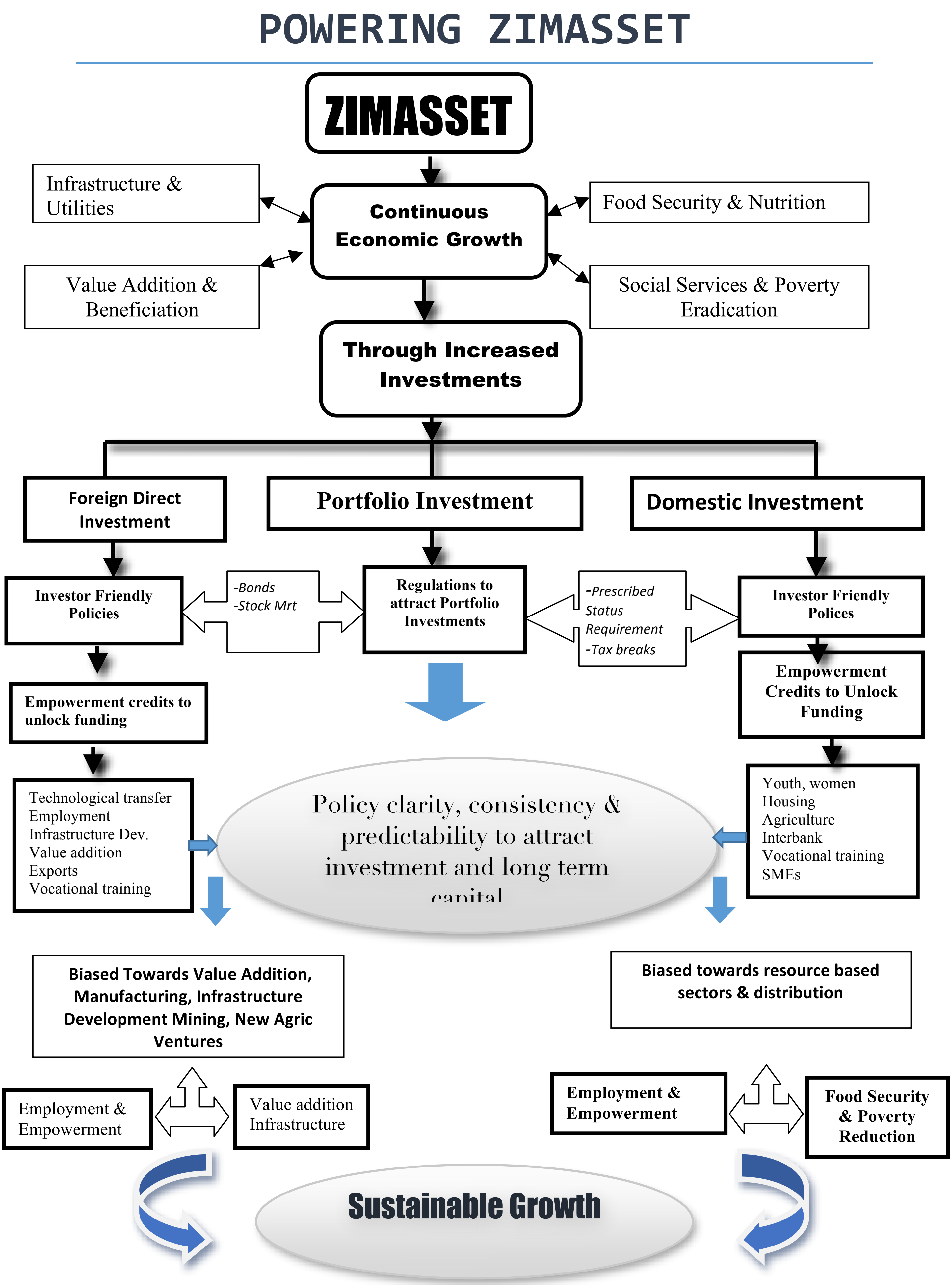
27. As Monetary Authorities, we shall continue to come up with robust and prudent monetary policy measures to address the needs of the economy and compliment fiscal policy as envisaged in ZimAsset. This Statement is being presented with that objective in mind as we envisage **ZimAsset as a national plan for Call to Action by Zimbabweans for Zimbabweans.**

28. The Reserve Bank believes that identification and **working around the Quick Wins or Low Hanging Fruits spelt out in the blue print is the way to fast economic recovery.** Enhancement of production through quick wins would need the nation to **embrace the philosophy of building around the operating companies and not mending what is not broken.** This is necessary for the quick recovery of the economy.

29. It is also necessary to note that the total funding requirement under ZimAsset of US$27 billion **is a snap shot. The $27 billion is ex-post and not ex-ante.** We believe that this distinction is critical in order not to demotivate the nation and/or possible financiers in the mobilisation of resources needed under ZimAsset. As highlighted in Figure 3 below, ZimAsset would need to be propelled or powered from both domestic and international financing resources.

30. As Banker to Government, the Reserve Bank shall do **its part to vigorously work on the mobilization of financial resources needed under ZimAsset and we therefore hope and pray that the ZimAsset blue print will be implemented, by the nation at large, consistently to the letter and spirit for the public good of the nation**

Figure 3


POWERING ZIMASSET
ZIMASSET
Continuous Economic Growth
Infrastructure & Utilities
Value Addition & Beneficiation
Food Security & Nutrition
Social Services & Poverty Eradication
Through Increased Investments
Foreign Direct Investment
Portfolio Investment
Domestic Investment
Investor Friendly Policies
-Bonds
-Stock Mrt
Regulations to attract Portfolio Investments
-Prescribed Status Requirement
-Tax breaks
Investor Friendly Polices
Empowerment credits to unlock funding
Empowerment Credits to Unlock Funding
Technological transfer
Employment
Infrastructure Dev.
Value addition
Exports
Vocational training
Policy clarity, consistency & predictability to attract investment and long term capital
Youth, women
Housing
Agriculture
Interbank
Vocational training
SMEs
Biased Towards Value Addition, Manufacturing, Infrastructure Development Mining, New Agric Ventures
Biased towards resource based sectors & distribution
Employment & Empowerment
Value addition Infrastructure
Employment & Empowerment
Food Security & Poverty Reduction
Sustainable Growth

ECONOMIC AND FINANCIAL REVIEW

GLOBAL ECONOMIC DEVELOPMENTS

31. The Zimbabwe economy is intricately connected to what happens in the region and globally. The country is a member of regional and international organisations such as the Southern African Development Community (SADC), Common Market for Eastern and Southern Africa (COMESA) and World Trade Organisation (WTO).

32. Global economic activity is expected to re-accelerate in 2014 spurred by recovery in advanced and developing economies. The adverse effects of a severe winter in the US and the Euro-Area in the first quarter of 2014, coupled with financial market perturbations and political instability in the Ukraine, however, moderated global economic activity in the first half of 2014.

33. This notwithstanding, economic activity in advanced economies is expected to improve from 1.3% in 2013 to 2.2% in 2014 on the back of moderated effects of fiscal consolidation, improved labour market conditions and supportive monetary conditions.

34. Despite accompanying expansion in import demand from advanced economies, growth in emerging market economies is projected to remain subdued at 4.9% in 2014. This largely reflects the negative repercussions of adverse investor perception with regards to policy weaknesses and vulnerabilities.

35. Political tension the Middle East coupled with a slowdown in economic activity in China is expected to pose significant downside risks to recovery prospects in emerging market economies.

36. The deceleration of economic activity in China is expected to result in a concomitant decline in the demand for commodities, as well as accompanying effects on commodity prices. These adverse developments are likely to spill over to commodity producing countries in Sub-Saharan Africa such as Zimbabwe, in the form of reduced export revenues, and deterioration in current account balances.

Table 1: Global Economic Growth (%)

	2012	2013	2014	2015
World Output	**3.2**	**3.0**	**3.6**	**3.9**
Advanced Economies	1.4	1.3	2.2	2.3
US	2.8	1.9	2.8	3.0
Japan	1.4	1.5	1.4	1.0
Emerging Market & Developing Economies	5.0	4.7	4.9	5.9
China	7.7	7.7	7.5	7.3
India	4.7	4.4	5.4	6.4
Sub-Saharan Africa	4.9	4.9	5.4	5.5
Latin America & the Caribbean	3.1	2.7	2.5	3.0

Source: International Monetary Fund, World Economic Outlook (April 2014)

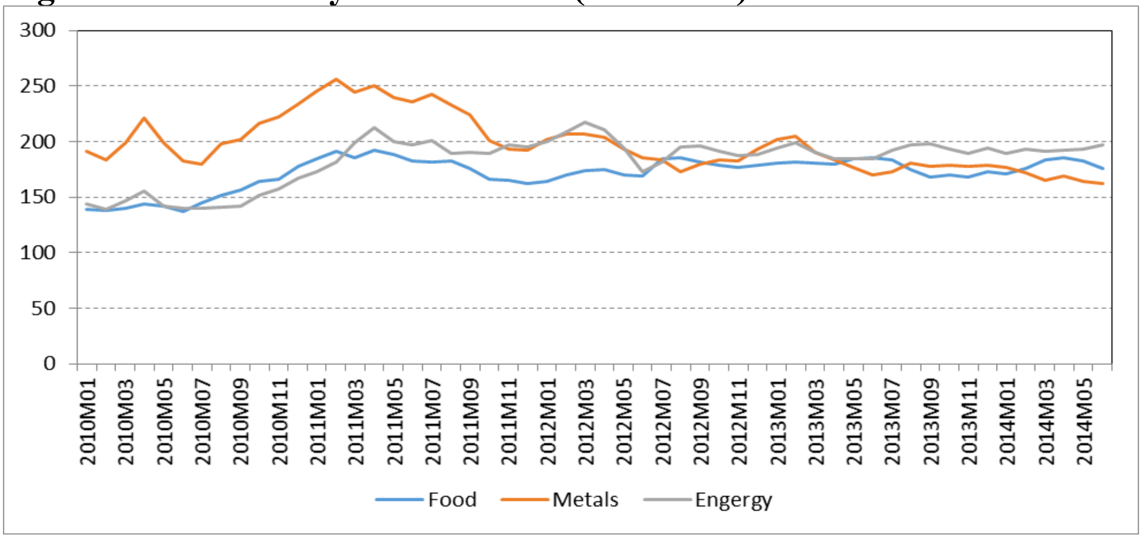
37. Nonetheless, growth in Sub-Saharan Africa is expected to increase from 4.9% in 2013 to 5.4% in 2014 (as shown in Table 1 above) on the back of increased investments in extractive industries, and infrastructure development.

Commodity Price Developments

38. On account of the country's commodity dependence, balance of payments developments, are intricately bound to global economic developments.

39. Since the fourth quarter of 2013, international energy prices have remained fairly stable, notwithstanding the upward pressures from increasing prices for natural gas and coal.

Figure 4: Commodity Price Indices (2005=100)



Source: IMF Commodity Price System, 2014

40. Crude oil prices, however, rose by 4% from US$107.44/barrel in January 2014 to US$111.77/barrel in June 2014 amid geopolitical tensions in the Ukraine and supply disruptions in Libya, Syria, Nigeria, Yemen and Iran (please refer to Table 2). The surge in oil supplies from North America, however, moderated the firming of oil prices.

41. The rise in crude oil prices is, however, expected to exert considerable pressure on the country's fuel import bill, thus worsening the country's balance of payments position.

42. In world food markets, favourable supply conditions for major crops are projected to result in surpluses and downward pressure on prices. As such, inventories for wheat and maize are expected to rise. This notwithstanding, concerns of adverse weather conditions in South

America may weigh down on expected yields and exert upward pressure on food prices.

43. On the back of recovery in global economic activity, precious metal prices have remained firm during the first half of 2014, although they remain relatively low compared to levels attained over the same period in 2013. On the other hand, base metal prices were broadly subdued due to concerns of weaker demand from China, the world's largest consumer of metals.

Table 2: International Commodity Prices

2014	Gold	Platinum	Copper	Nickel	Crude Oil
	US$/oz	*US$/oz*	*US$/tonne*	*US$/tonne*	*US$/barrel*
January	1,241.82	1,420.43	7,294.77	14,096.36	107.44
February	1,299.83	1,409.51	7,149.38	14,158.50	108.69
March	1,336.71	1,451.11	6,668.90	15,673.10	107.79
April	1,298.80	1,431.40	6,665.78	17,346.10	107.99
May	1,289.06	1,451.79	6,880.58	19,396.25	109.20
June	1,278.49	1,452.60	6,797.20	18,575.83	111.77
% Change	*3.0*	*2.3*	*-6.8*	*31.8*	*4.0*

Source: BBC and KITCO

DOMESTIC ECONOMIC DEVELOPMENT

GDP AND INFLATION

44. As stated above, the Zimbabwean economy continues to face challenges which reflect some structural rigidities, inadequate domestic and foreign investments and lack of long term funding.

45. Economic activity decelerated from 10.6% in 2012 to an estimated 4.5% in 2013, in real terms. It is expected that a further slowdown in GDP growth is expected in 2014 to the revised 3.1%.

46. Inflation, however, has remained low and was in the negative territory from February to June 2014. The rate of inflation reached deflationary levels during the 5 months mainly **due to low aggregate demand coupled with a price correcting process since Zimbabwean prices are generally higher than those obtaining in neighbouring countries.**

47. In July 2014, inflation increased to 0.3% from the June level of -0.08%. It is anticipated that inflation would remain below the 1% level for the rest of 2014.

FINANCIAL SECTOR DEVELOPMENTS

48. The general slowdown in the performance of the domestic economy continues to pose challenges to the banking sector. **However, the banking sector has demonstrated resilience under the current macroeconomic environment and the sector has remained safe and sound.**

Architecture of the Banking Sector

49. Currently there are 19 operating banking institutions, comprising 15 commercial banks, one (1) merchant bank and three (3) building societies as well as one (1) savings bank and 156 microfinance institutions.

50. Capital Bank voluntarily surrendered its licence, which was subsequently cancelled by the Registrar of Banking Institutions on 4 June 2014.

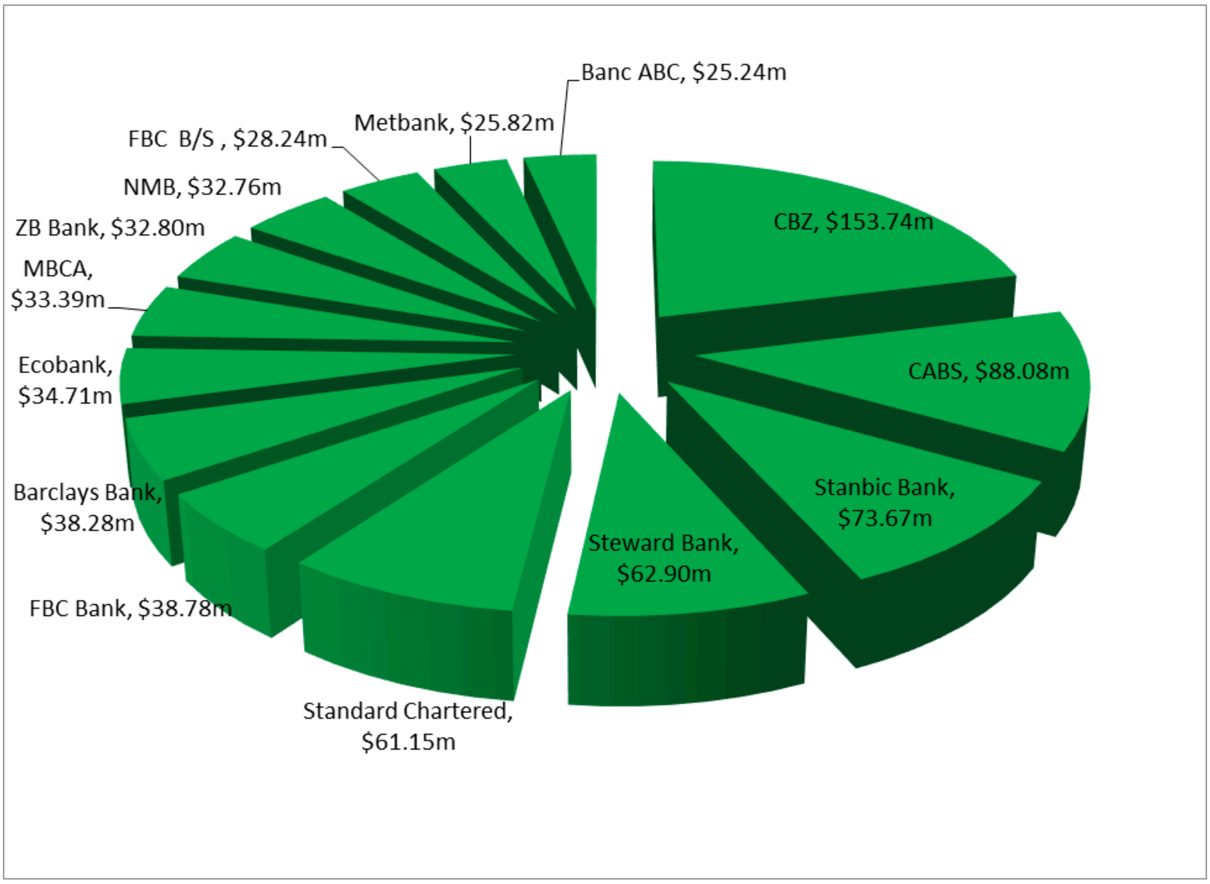
Performance of the Banking Sector

Capitalisation

51. As at 30 June 2014, a total of 14 out of 19 operating banking institutions (excluding POSB) were in compliance with the prescribed minimum capital requirements as shown in Figure 5 below.

52. On aggregate, core capital for the banking sector amounted to $753.09 million as at 30 June 2014 (excluding Interfin Bank which is under curatorship), compared to $790.35 million as at 31 December 2013**.** The reduction in the total core capital is largely attributed to loan loss provisions and subdued earnings performance by some banking institutions.

Figure 5: Capitalisation of Banking Institutions



53. Meanwhile, banking institutions have submitted recapitalization plans which are hinged on organic growth, injection by shareholders, rights issues and mergers and acquisitions for compliance with the minimum capitalisation requirements.

54. The efforts by banks to increase their capital positions have been constrained by a number of challenges including the macroeconomic environment and subdued foreign direct investment.

Banking Sector Profitability

55. The banking sector remained generally profitable as at 30 June 2014, with an aggregate net profit of $13.84 million for the half year ended 30 June 2014, up from $4.90 million during the corresponding period in 2013.

56. A total of 12 banks recorded profits for the period ended 30 June 2014. The losses recorded by the few banking institutions are attributed to high levels of non-performing loans, lack of critical mass in terms of revenue to cover high operating expenses and deliberate strategy by some banks to clean up bad loan books through provisioning.

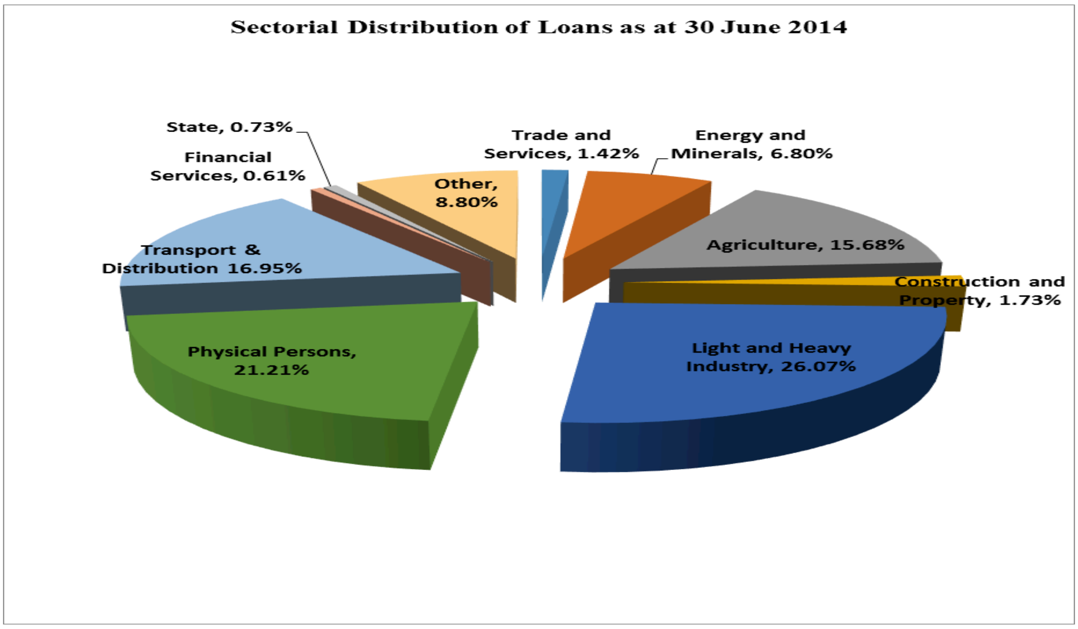
Deposits and Loans & Advances

57. Total banking sector deposits increased by 4.86% from $4.73 billion as at 31 December 2013 to $4.96 billion as at 30 June 2014, while loans & advances marginally increased from $3.70 billion to $3.81 billion, during the same period.

Sectorial Distribution of Loans

58. Loans granted by the banking sector to the various sectors of the economy as at 30 June 2014 were distributed as follows:

Figure 6



59. The banking sector loan portfolio is dominated by the industrial sector, household, transport and agriculture, constituting 26.07%, 21.21%, 16.95% and 15.68 of total credit, respectively. The remaining sectors contributed less than 10% each.

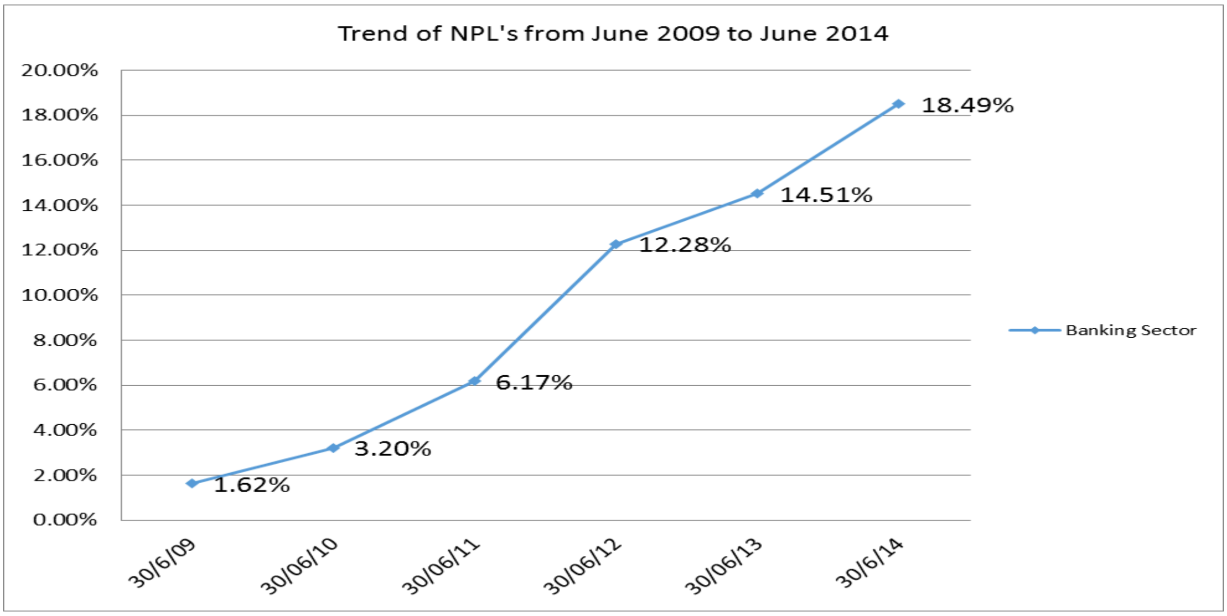
Non-Performing Loans

60. In the face of challenging economic conditions and increasing cost of doing business, the debt repayment capacity of the borrowers remained

under stress. Credit risk remains a key component in the risk profile of the banking sector.

61. As a result, the level of non- performing loans has risen from 15.9% as at 31 December 2013 to 18.5% as at 30 June 2014.

Figure 7



Source: RBZ

62. The surge in delinquencies and loan losses has dampened banks' risk appetite. Resultantly, banks have increasingly adopted a risk averse approach to lending.

Distressed Banks

63. Across the globe, the existence and continued presence of weak banks is a matter of concern to supervisory authorities.

64. There are four banking institutions, namely Metbank, Allied Bank, AfrAsia and Tetrad facing liquidity and solvency challenges due to macro

and institution specific factors. These banks command low market shares in terms of loans (8.8%), assets (7.2%) and deposits (6.7%) as at 30 June 2014.

65. Cognisant of the need to protect the interest of depositors and promote banking sector confidence, the Reserve Bank has been engaging these institutions to come up with credible plans to turnaround their waning financial condition.

66. In this regard, shareholders and boards of the distressed banks have been directed to finalise implementation of their turn around plans, failure of which the Reserve Bank will be left with no option but to intervene and institute appropriate supervisory action in terms of the Banking Act.

67. The Reserve Bank is on record that institutions should seriously consider consolidations/mergers and voluntary surrender of licences when deemed necessary.

Metbank

68. Although Metbank's capital is compliant with the minimum capital threshold of $25 million, the institution has been facing severe liquidity challenges. The bank has embarked on capital raising initiatives and other turnaround strategies to address its current liquidity challenges. The bank remains under close monitoring by the Reserve Bank.

Tetrad Investment Bank

69. Tetrad Investment Bank is facing liquidity challenges resulting in the

institution failing to meet some outstanding payments.

70. The bank has entered into a scheme of arrangement with its creditors to put a stay on litigations. The scheme of arrangement is for three (3) months up to 31 October 2014 and is envisaged to protect the institution's assets for the benefit of all depositors and creditors.

71. In an endeavour to address its solvency status, the bank is in discussion with a potential investor for the injection of capital. The scheme of arrangement is also expected to provide ample time for the potential investor to finalise the recapitalisation initiatives.

AfrAsia

72. The bank is facing liquidity challenges and is instituting various measures to ameliorate the liquidity situation. The institution is seeking liquidity support from the major shareholder and concomitantly pursuing a private placement transaction, whose successful consummation will bolster the bank's capital level.

73. The Reserve Bank is satisfied with the current efforts by the major shareholder to strengthen the bank's financial condition as evidenced by an injection of $10 million which improved the bank's capital to $19.20 million as at 30 June 2014.

74. The Reserve Bank will continue to work closely with the board and senior management of the bank regarding their various initiatives to strengthen the institution.

Allied Bank

75. The bank is facing both solvency and liquidity challenges and consequently has been failing to pay maturing obligations. The board and senior management are working on various capital raising initiatives including engaging the major shareholder to raise funds to bolster the institution's capital and liquidity position.

76. The Reserve Bank will continue to closely monitor the situation at the bank.

Financial Inclusion and Mobile Banking

77. The subject of financial inclusion is continuing to receive increasing focus internationally and is particularly important for developing economies where a large proportion of the population has been traditionally excluded from the mainstream economy.

78. Accordingly, we continue to urge financial institutions to consciously support micro, small and medium enterprises and individuals to facilitate their participation in economic activities thus promoting inclusive growth and development of the economy.

79. The Reserve Bank is supportive of the efforts being undertaken by banking institutions in furthering the objectives of financial inclusion in the country by embracing mobile technologies to reach out to the unbanked population at lower costs. In addition banking institutions are pursuing other initiatives such as agent banking thus enhancing access to financial services.

80. The partnership between banking institutions and mobile network operators has enabled banks to offer their customers mobile banking services such as payments facilities, funds transfers, loan disbursements and repayments.

81. **In this regard, we urge banking institutions and mobile network operations to work towards infrastructure sharing while competing on service delivery.**

Consumer protection

82. Consumer protection is critical as we seek to build an inclusive financial system as well as public confidence in the system.

83. Government has embarked on initiatives towards the development of consumer protection laws. The Reserve Bank and other stakeholders are also working towards the development of a robust consumer protection framework in the financial sector.

84. The Reserve Bank through its supervisory activities have noted that the banking sector has generally not taken the initiative to ensure that consumers of financial services are adequately protected.

85. The Reserve Bank continues to receive complaints from some consumers who enter into borrowing contracts without fully understanding the extent of their obligations.

86. Going forward, the Bankers Association of Zimbabwe is expected to attune the Code of Banking Practice to the obtaining environment and enforce the Code on its members.

Microfinance Act

87. The new Microfinance Act [*Chapter 24:29*], which was gazetted in 2013, provides for the regulation and supervision of both credit-only and deposit-taking microfinance institutions.

88. The new Act has strengthened the consumer protection framework for microfinance clients through mandatory full disclosure by microfinance institutions of the terms and conditions of their services, adequate pre-lending assessment to avoid over-indebtedness of clients and ethical business conduct among other requirements.

EXTERNAL SECTOR DEVELOPMENTS

89. Against the background of commodity price volatility and growing import demand, the country's external sector position remains under considerable pressure. Lack of export competitiveness, coupled with subdued capital inflows, continue to adversely affect the country's external sector position, as evidenced by the low foreign exchange reserves.

90. On the other hand, the continued decline in industrial capacity utilisation, currently estimated at levels below 40%, due to lack of production and competitiveness, continue to widen supply gaps in the domestic economy thereby creating growing demand for imported goods, which further jeopardize the country's external financial position.

Merchandise Trade Developments

91. Export receipts realized over the period January to June 2014 amounted to US$1.23 billion, which compares unfavourably with imports, which amounted to US$2.99 billion realized over the comparative period in 2014.

92. Mining continues to make a significant contribution to the country's export earnings, accounting for **52%.** Agriculture including tobacco and horticulture accounts for **21%,** followed by manufacturing **(13%)** and services, which include transport and tourism **(11%).**

93. The level of exports realised by June 2014 were 21% lower than what was realised for the same period in 2013. This reflects the slowdown in economic activity mainly due to company closures. As such, this subdued level of exports further compound the liquidity situation and deceleration in economic activity.

94. Foreign payments for merchandise imports (excluding fuel & electricity) and services account for approximately 60% of the country's cumulative total cross border payments, indicating the country's heavy reliance on imported goods and services. The merchandise import bill for 2014 has a large proportion of consumption goods (51%), some of which can easily be produced locally.

95. The huge volume of merchandise imports and service payments continues to be a cause for concern to Monetary Authorities, especially in an environment characterised by limited foreign exchange resources. We,

therefore, urge market participants to exercise **discipline** in the use of the limited foreign exchange resources, thus limiting the export of jobs and income.

96. The disproportionate gap between the country's exports and imports has inevitably culminated in a deficit of US$1.77 billion on the trade account, for the first half of 2014, as shown in Table 3 below.

Table 3: Merchandise Trade US$ Million

	2013			2014		
	Exports	Imports	Trade Balance	Exports	Imports	Trade Balance
January	279.6	606.7	(327.2)	**278.2**	**487.9**	(209.7)
February	279.0	499.2	(220.1)	**192.5**	**478.8**	(286.3)
March	253.9	532.8	(278.9)	**156.4**	**499.9**	(343.5)
April	209.9	963.6	(753.7)	**179.0**	**491.5**	(312.5)
May	278.3	580.0	(301.7)	**184.3**	**510.1**	(325.8)
June	244.9	714.1	(469.2)	**238.0**	**528.2**	(290.2)
Total	1,545.6	3,896.5	(2,350.8)	**1,228.4**	**2,996.3**	(1,767.9)

Source: Zimstat

Current and Capital Account Developments

97. This trade deficit is projected to combine with net service payments to result in a sizeable current account deficit of over US$3.5 billion in 2014 or over 25% of GDP. This current account deficit is unsustainably high, compared to the SADC and COMESA macroeconomic convergence target of not more than 9% of GDP.

98. Despite previously recording surpluses on the capital account, the current account has largely been financed by debt creating and volatile short term and long term offshore lines of credit to the private sector, compared to the more stable non-debt creating foreign direct investment flows, which have remained relatively depressed.

Overall Balance of Payments

99. Total declared foreign currency receipts which include exports, loan, transfers, income, and investment receipts, for the period January to June 2014 amounted to **USD3.2 billion** compared to **USD3.8 billion** received during the same period in 2013. The **17%** decline in foreign receipts was mainly attributable to low production and to some extent, the decline in mineral prices.

100. For the period January to June 2014, total cross border payments (including merchandised imports, energy, capital remittances, income and service payments) processed through Authorized Dealers amounted to **USD4.3 billion** compared to **USD4.4 billion** for the same period in 2013 representing a **4%** decrease.

101. Against the backdrop of a huge current account deficit and subdued capital and financial inflows, the overall balance of payments, after taking into account errors and omissions recorded a deficit of US$366 million in 2013 and is expected to deteriorate further in 2014.

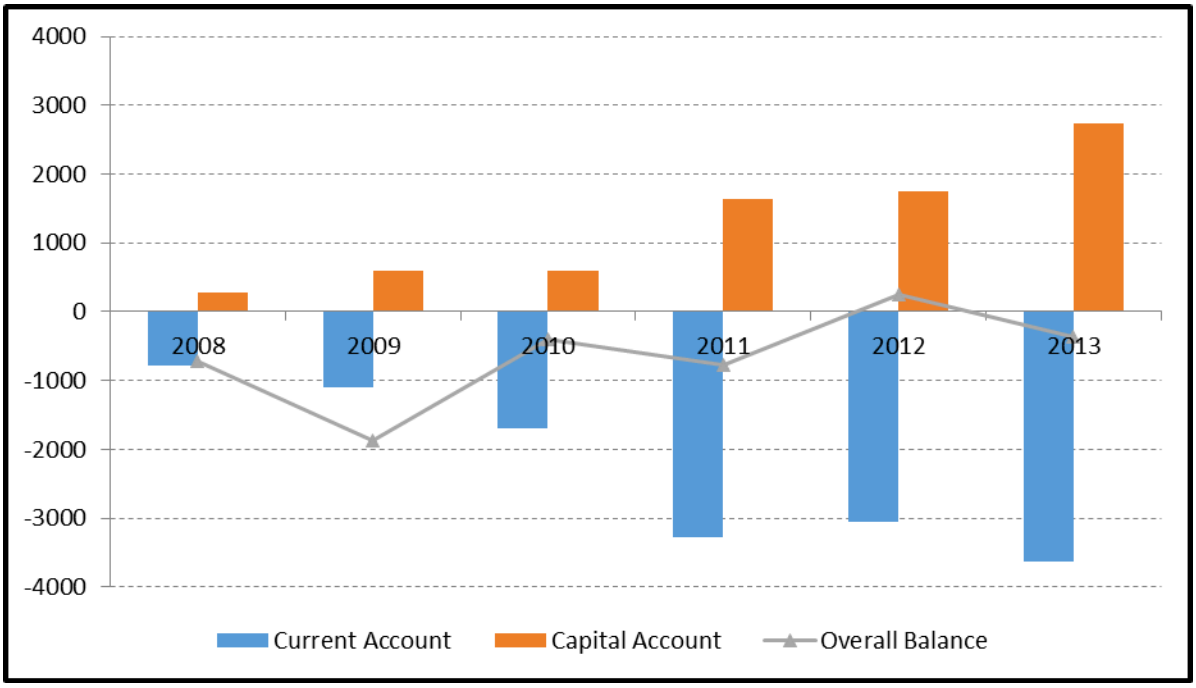
Table 4: Balance of Payments Summary (US$M)

	2008 Actual	2009 Actual	2010 Actual	2011 Actual	2012 Actual	2013 Estimate
Current Account Balance	-775.3	-1092.0	-1701.4	-3273.1	-3048.1	-3639.3
Trade Balance	-969.1	-1599.8	-1918.1	-3145.7	-2902.0	-3315.7
Exports F.O.B	1660.4	1613.3	3243.7	4416.3	3808.2	3636.1
Agric	367.3	413.3	519.3	*893.8*	979.6	1047.5
Mining	*736.4*	*659.6*	*1568.8*	*2126.8*	2189.1	1997.6
Manufacturing	*443.8*	*421.8*	*1026.9*	*1259.4*	549.2	487.0
Imports F.O.B	2629.5	3213.1	5161.8	7562.0	6710.2	6951.7
Food	340.7	741.2	554.0	512.5	730.6	658.1
Fuel	530.1	568.2	945.4	1571.4	1365.7	1495.3
Capital Account Balance	272.7	586.9	586.7	1633.4	1740.2	2734.3
Errors And Omissions	-222.6	-1361.8	707.2	857.2	1558.5	602.3
Overall Balance	*-725.2*	-1867.0	-407.5	-782.6	250.7	-366.4

Source: Reserve Bank of Zimbabwe

102. Against this background, the country's official reserves have remained low. Figure 8 below further amplifies the negative trend in the balance of payments position.

Figure 8: Balance of Payments Summary (US$M)



Source: Reserve Bank of Zimbabwe

Diaspora Remittances

103. For the period January to June 2014, international money transfers amounted to USD845.6 million, of which Diaspora remittances were USD412.4 million and international organisations, such as NGOs, USD433.2 million.

104. Diaspora remittances remain a critical source of liquidity in the market and the Reserve Bank will continue to put in place effective systems to encourage use of formal channels by our kith and kin outside Zimbabwe.

Foreign Investment Inflows

105. Under the multi-currency environment, foreign investment is expected to have a significant and positive impact on market liquidity. Foreign

investment inflows into Zimbabwe have remained subdued due to the perceived country risk. For the first six months of 2014, the country received a paltry USD67 million compared to USD165 million during the same period in 2013.

106. On a cumulative basis, and compared to other countries in the region, Zimbabwe's foreign direct investment inflows amounted to USD1.7 billion over the period 1980 to 2013, whereas, Zambia and Mozambique received USD7.7 billion and USD15.8 billion, respectively. Of the total of USD25.2 billion received between the 3 countries since 1980, Zimbabwe has accounted for a mere 7%.

107. There is therefore need for the country to create an investor-friendly environment so as to tap into these external capital resources to boost employment, production and exports as enunciated in the country's blueprint, ZimAsset.

FINANCIAL SECTOR POLICY MEASURES

Enhancing Legal environment

108. Amendments of the Banking Act [Chapter 24:20] were approved by Cabinet to strengthen the regulatory environment and the Bill is about to be gazetted.

109. In terms of the proposed amendments to the Banking Act, provision will be made for licensing of credit reference bureaus and supervision of the Infrastructure Development Bank of Zimbabwe (IDBZ) and the Small & Medium Enterprises Development Corporation (SEDCO).

110. The Bank is in agreement with Government on parameters to be used by foreign banks to comply with the Indigenisation and Economic Empowerment Policy. The parameters also take into account of the fact that bank deposits are public funds.

New Minimum Capital Requirements for Banks

111. In the Monetary Policy Statement of January 2014, the Reserve Bank reviewed the deadline for compliance with capital requirements to 31 December 2020.

112. The Reserve Bank has observed that the current operating environment still presents numerous challenges in banks' ability to grow capital organically or raise capital from investors.

113. Most local shareholders lack financial capacity to inject the much needed capital into their respective banking institutions. As a result, the local shareholders have failed to follow up on their rights during capital calls.

114. In light of the macroeconomic challenges constraining the capitalization initiatives, the Reserve Bank has taken measures to promote strategic groups based on current banking classes, in line with Section 6 of the Banking Act.

115. Accordingly, the Reserve Bank has come with three segments, namely **Tier I, Tier II and Tier III** for banks' compliance with minimum capital requirements. The strategic groups, the applicable minimum capital requirements and the respective activities are shown in Table 5 below:

116. **Tier I segment comprises of large indigenous commercial banks and all foreign banks. These will conduct their core banking activities, and in addition, offer other activities such as mortgage lending, leasing and hire purchase that have longer term maturities as well as other sophisticated products.**

117. **Banks in the Tier I strategic segment will be required to have minimum core capital requirements of $100 million by 2020 as previously announced. The capital will enable the Tier I banks to absorb the risk associated with the scope and complexity of their activities.**

Table 5 New Capital Requirements of Banks

Segments	**Type of Institution**	**Capital requirements**		**Activities**
		Current	**2020**	
Tier I	Large Indigenous Commercial banks & all foreign banks	$25 million	$100 million	Core banking activities plus additional services such as mortgage lending, leasing & hire purchase
Tier II	Commercial banks, Merchant banks, Building societies, Development banks, Finance & Discount houses	$25 million	$25 million	Core banking activities only
Tier III	Deposit Taking Microfinance banks	$5 million	$7.5 million	Deposit Taking Microfinance activities

118. **The Tier II segment comprises of commercial banks, merchants banks, building societies, development banks, finance houses and discount houses that will only conduct their core banking activities. The Tier II banking institutions should maintain minimum capital requirements of $25 million.**

119. Banks, other than foreign banks, that elect not to increase their capital to $100 million threshold will automatically fall in the Tier II category offering the limited product range.

120. Banking institutions **in Tier II can migrate to the Tier 1 strategic group provided they meet the capital requirements and the risk management systems that are commensurate with the nature and scope of the activities.**

121. **The Tier III segment which has a current minimum capital requirements of US$5 million comprises of deposit taking microfinance institutions. The minimum capital requirements of $7.5 million by 2020 for Tier III take into account start-up costs such as acquisition of an IT system and establishment of branches. It is envisaged that the institutions in Tier III will further bolster the current financial inclusion initiatives.**

122. **Banking institutions will be required to submit revised capital plans for December 2020 based on their chosen strategic group by 31 December 2014.**

123. The Zimbabwean economy requires strong banks that can adequately support the funding requirements of industries. Banks should therefore

ensure they build capital bases to levels that provide critical mass necessary to make significant contribution to the economy.

124. The above strategic segmentation allows the existence of smaller, **profitable banks with strong governance** and risk management systems that play a **meaningful role in the economy.**

Resolution on NPLs

125. Globally, non-performing loans (NPLs) have been a hindrance to economic stability and growth of economies. The Reserve Bank is cognisant that the problem of high levels of NPLs which exceed the international benchmark of up to 5% can be a threat to financial stability and economic growth.

126. As such, addressing the problem of NPLs is essential in order to invigorate the Zimbabwean economy. **The resolution on non-performing loans is therefore a necessary condition to improve the economic status of the country and to address the vicious circle of low economic growth, company closures and banks vulnerability.**

127. As already indicated in Figure 4, NPLs have been rising from 1.6% in 2009 to 18.5% (US$705 million) as at June 2014.

128. **Apart from being a source of concern for financial stability, there is strong evidence that NPLs have led to a decrease in credit growth which is undermining current economic recovery efforts.**

129. Unfortunately the NPLs are now continuously growing even without new lending by banks because of interest accruing on the unpaid loan

balances. **To make matters worse, NPLs are traditionally charged penalty rates of interest which means that they are now growing at a much faster pace.**

130. The rising NPLs in the banking sector since 2009 can be attributed to the operating environment that has characterized the post multi-currency period when businesses and individuals rushed to obtain bank credit to expand their businesses which had been starved of cash during the hyper-inflationary era. Indeed banks extended credit and economic activity expanded. Unfortunately this was done by **utilizing short term funding to purchase long term assets (thereby creating funding mismatches) on the expectation that this phase was going to continue or that it was sustainable.** The other fundamental causes of rising NPLs **include institution specific factors such as weak corporate governance practices and risk management systems.**

131. High cost structures, obsolete equipment, and intense competition from relatively cheap imports have compounded the problem resulting in borrowers failing to service their loans in terms of contractual agreements.

132. The situation in which banks are saddled with high NPLs that do not decrease and remain at high levels for a long period would **result in the prolonged stagnation of the economy.**

133. Across the globe, it has been noted that the problem of non-performing loans has a **mechanism to drag on the economy** in a number of ways including the following:

a) lowering banks' intermediary function due to erosion of bank profits;

b) deterioration of bank assets and erosion of their capital;

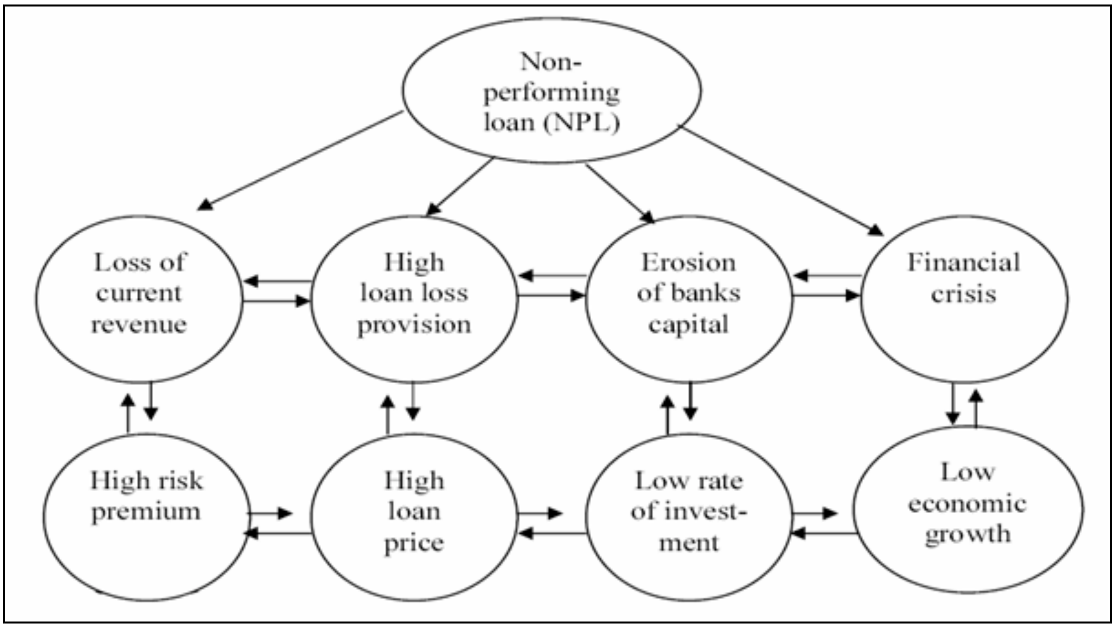
c) stagnation of economic resources, such as labour and capital, in areas with low productivity; and

d) Decline in bank lending, as banks with high level of non-performing loans in their portfolio may become **increasingly reluctant to take up new risks and commit new loans; and pose serious challenges to the pursuit of macroeconomic stability and growth objectives by government.**

134. Increase in NPLs in **Zimbabwe is causing banks to cut on lending to business at a time companies require working capital and funds for retooling.** This is now having a huge bearing on the economy **as reduced credit is leading to a decline in economic growth, private consumption, job losses and decrease in government revenue i.e. taxes.**

135. Figure 9 and 10 summarize the economic and financial implications of NPLs and the associated vicious cycle of low economic growth, NPLs and banks' vulnerability.

Figure 9: Economic and Financial Implications of NPLs



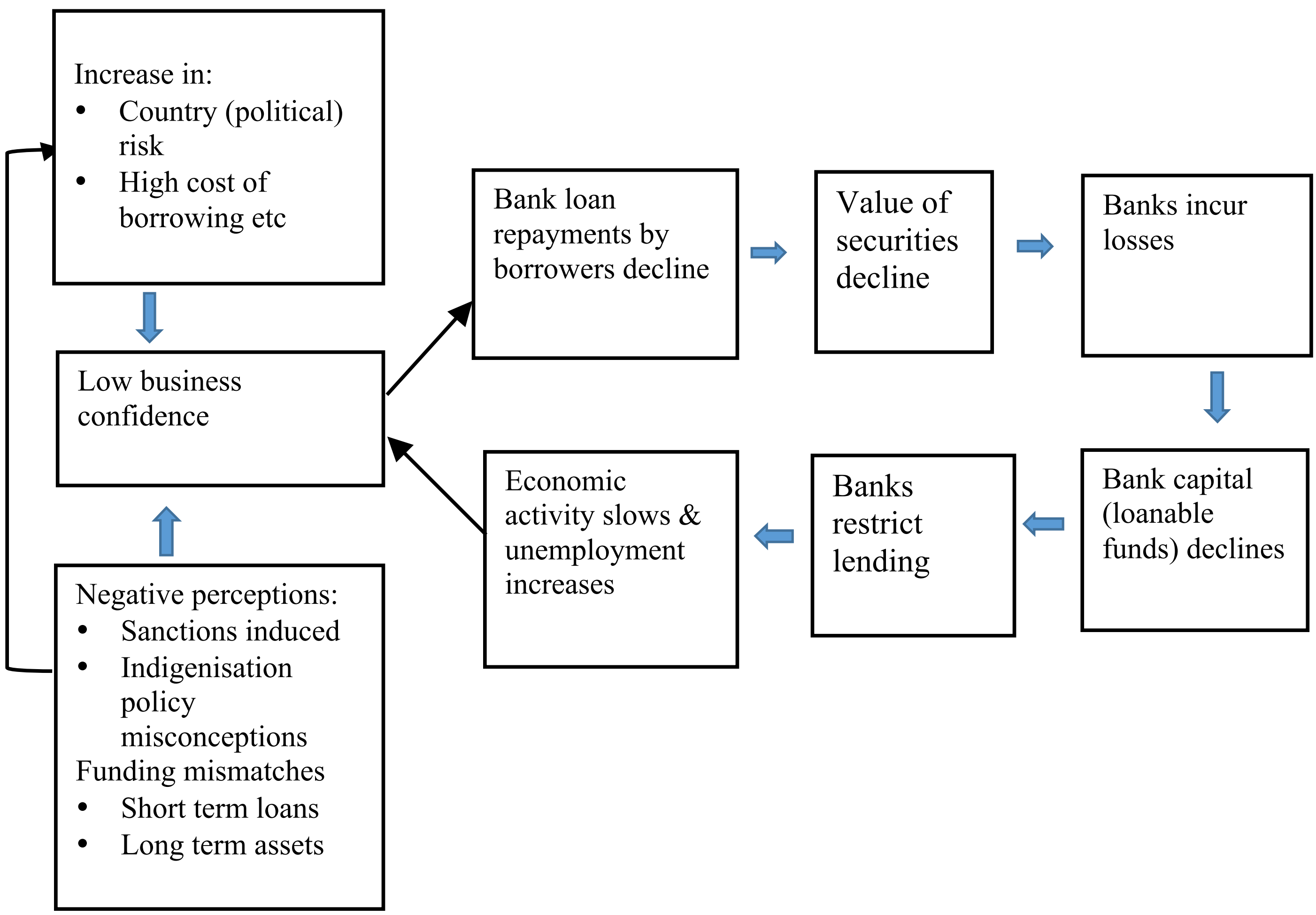
Source: NPL in the Banking Sector of Bangladesh: Challenges & Realities, Bishu Kumar Adhikary

136. To this end, **the Reserve Bank is pleased to advise that Cabinet has approved the establishment of a National Special Purpose Vehicle (SPV)** known as **Zimbabwe Asset Management Corporation (Pvt) Ltd (ZAMCO) to acquire NPLs from Banks in order to clean up and strengthen banks' balance sheets and provide them with the liquidity to fund valuable projects for the economy to rebound and to mitigate loss of confidence**

Figure 10

LOW BUSINESS CONFIDENCE CHALLENGES

VICIOUS CYCLE OF LOW GROWTH, NON-PERFORMING LOANS (NPLS) AND BANK VULNERABILITY



Source: Reserve Bank of Zimbabwe

137. Banks would sell NPLs to ZAMCO under commercial terms, assigning collateral and all other rights attached to the loans.

138. ZAMCO will be funded by a combination of non-funded lines of credit, new inflows, long term bonds and treasury bills.

139. ZAMCO would manage the loan portfolio professionally in order to obtain maximum recoveries over time.

140. Once restructured, the troubled assets will be sold and the proceeds will be used to retire the borrowing, treasury bills or the bonds.

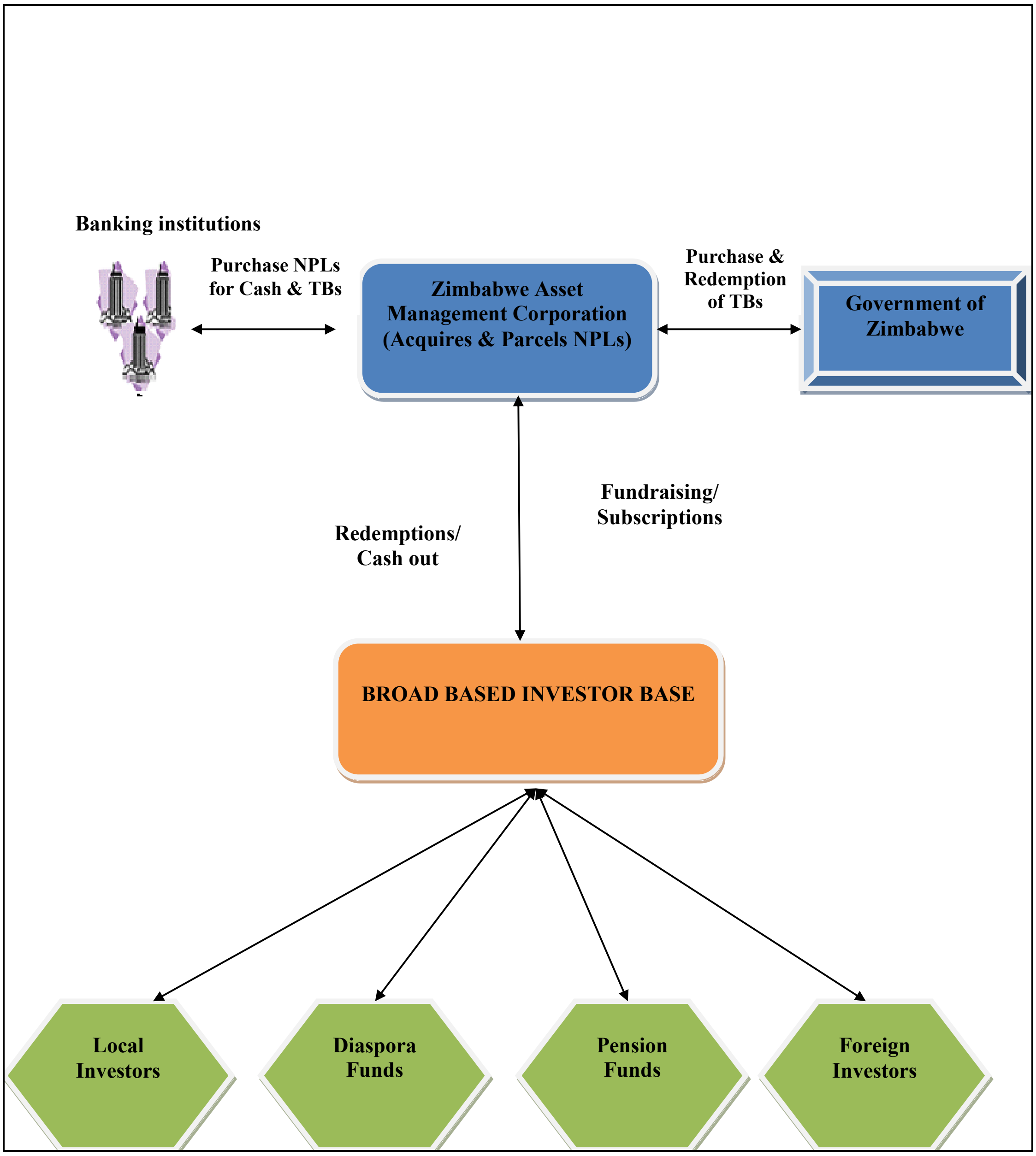
141. NPLs in an amount of US$45 million have already been acquired by ZAMCO from three banks as at 15 August 2014.

142. ZAMCO will be supervised by RBZ.

Structure of NPLs SPV

143. Generically, the SPV structure involves sourcing of funds to purchase NPLs from banking institutions. The SPV will restructure, rehabilitate and recover funds under the non performing portfolio. The schematic representation of the SPV is outlined in Figure 11 below:

Figure 11: Structure of SPV Operations



Benefits

144. The Reserve Bank envisages that these measures will provide a holistic solution to the issue of non-performing loans in the banking sector. The restructuring of non-performing loans will provide relief to borrowers whose fundamentals remain strong but require reasonable funding costs and a tenure that can be accommodated in their cash-flows.

145. The reduction of NPLs will therefore, help revive credit growth, spur activity of previously over borrowed clients and free up resources trapped in unproductive uses. This will bolster the supply side of the economy.

146. A number of countries adopted similar strategies for resolving NPLs as discussed hereunder.

Other Countries' Experience With NPLs

Nigeria

147. Nigeria experienced an excessively high level of non-performing loans in 2009 with the percentage of non-performing loans to total loans ranging from 19% to 34%. The high levels of NPLs were attributable to poor corporate governance practices, lax credit administration processes and the absence or non-adherence to the bank's credit risk management practices.

148. In response, the Central Bank of Nigeria formed an Asset Management Company of Nigeria ("AMCON") in 2010 with a specific mandate to do the following:

a) Acquire the non-performing loans of banks;
b) Put capital into the intervened banks to shore up their capital which had become inadequate; and
c) Manage the acquired assets and recover the debt.

149. In line with its mandate, AMCON acquired the non-performing risk assets of some banks worth over N1.7 trillion, which boosted the banks' liquidity as well as enhance their safety and soundness.

150. With the intervention of AMCON, the banking industry ratio of non-performing loans to total credit was significantly reduced from 34.4% in November 2010 to 4.95% in December 2011. Within 4 years Nigerian banks were cleaned up and were able to meaningfully participate in economic development.

Malaysia

151. The measures taken by the Malaysian government in the advent of NPLs were swift and effective. The Government of Malaysia established an Asset Management Company (AMC), Danaharta, in June 1998 to re-energise the Malaysian financial sector by buying non performing loans from financial institutions and maximizing their recovery value.

152. The AMC was formed in terms of the Pengurusan Danaharta Nasional Berhad Act which gave it the power to acquire, manage, finance and dispose the assets.

153. Danamodal, the organization for the infusion of public funds, pumped an initial amount of 6.4 billion ringgit (equivalent to US$2 billion) into 10 banks.

China

154. China's huge NPL burden amounting to **$500 billion as at 31 December 2004** was largely attributable to non-performing loans at four large State Owned Commercial Banks (SOCBs) largely emanating from sustained losses at state-owned enterprises (SOEs).

155. The Chinese government transformed its four state-owned banks to private entities, by creating four asset management companies (AMCs) to

handle the SOE-backed NPLs, and invited foreign investors to inject capital and financial expertise into its banking system.

156. The purpose of the AMCs, established by the government with predetermined ten year life spans, was to relieve Chinese banks of their NPLs, thereby freeing up capital for new lending to commercial loans.

157. The AMCs were funded by bonds issued under the guarantee of the Ministry of Finance, which then purchased bad loans directly at book value from designated banks.

158. The Chinese AMCs primarily adopted the following recovery methods:

a) debt-for-equity swap;
b) restructuring of debt terms;
c) debt collection;
d) sale or lease of real estate property;
e) direct sales of packaged or individual NPLs; and
f) Securitizations - the securitized receivables from NPLs were the expected stream of cash flows to be generated from the NPLs.

South Korea

159. The South Korean government resolved the problem of NPLs by setting up an asset management company, the Korea Asset Management Corporation, in December 1997. The asset management company immediately purchased NPLs worth 35 trillion won (US$32.1 billion) and recovered 18 trillion (US$16.2 billion).

160. The above country experiences indicate ways in which Zimbabwe can resolve the NPL problem and inject some liquidity into the banking sector.

161. In order not to incur new bad loans, banks require adequate knowledge about the borrowers and the establishment of a Credit Reference Bureau will assist in this regard.

Credit Reference Bureau (CRB)

162. Financial institutions in Zimbabwe are generally exposed to heightened credit risk owing to high levels of information asymmetry and the lack of an effective credit information sharing mechanism.

163. There are limited avenues for banking institutions and other credit providers to check and/or share information on the credit history of borrowers.

164. As a result, some multi-banked clients have also become serial defaulters with non-performing loans at several banking institutions.

165. Cognisant of these challenges the Reserve Bank is working on bridging the information asymmetry gap in the banking sector through establishing a central credit registry system within its structures.

Features of the Proposed Credit Reference System

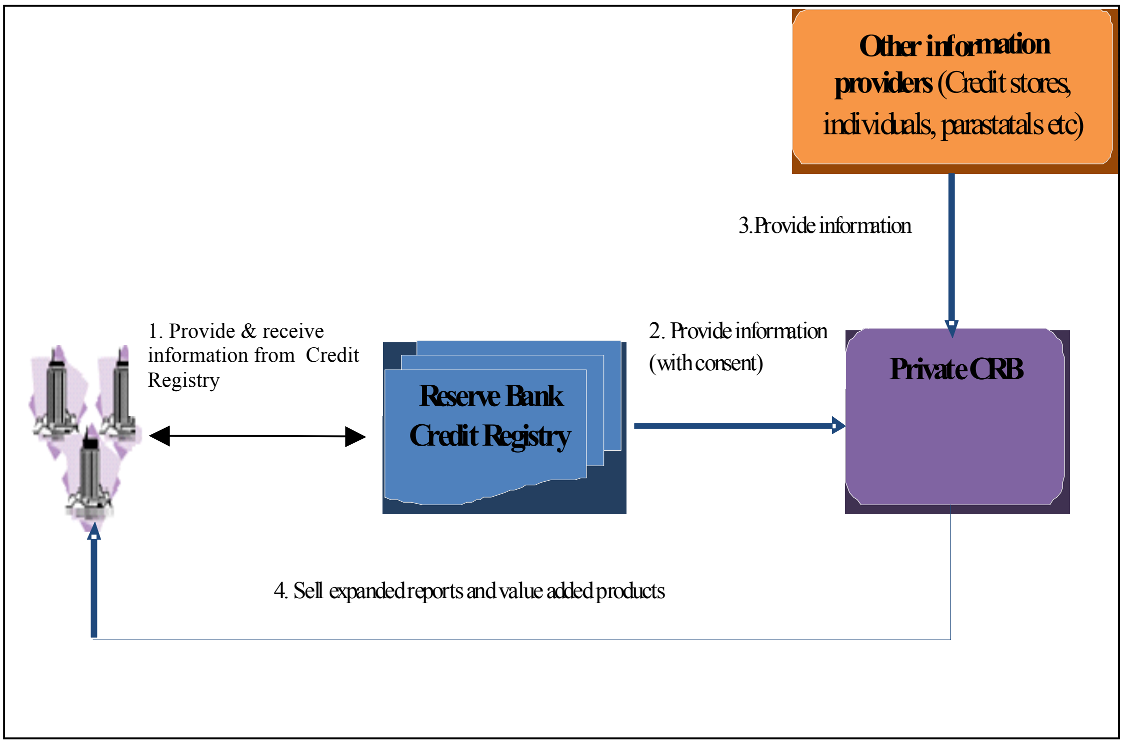
166. The credit reference system shall comprise a credit registry and private credit reference bureaus.

167. The credit registry will be based in the Reserve Bank and will collect credit information from all banking institutions and microfinance institutions.

168. The credit registry will serve as a databank for licensed private CRBs. The private CRBs will access the credit information from the credit registry and provide reports to their subscribers.

169. The proposed structure of the credit reference bureau system is indicated below:

Figure 12: Structure of CRB



170. In order to provide for the implementation of a credit reference system, the Banking Amendment Bill shall be gazetted to provide for the issuance of regulations governing the licensing and supervision of credit reference bureaus and establishment of a credit information data bank. In addition,

the amendments will also address sharing of credit information between banking institutions, Reserve Bank and private credit reference bureaus.

171. The Banking Regulations will also spell out statutory obligations of credit reference bureaus and the rights of borrowers.

Benefits of the Credit Bureau System

172. A credit information bureau serves as an information broker and is thus a key component in promoting financial sector stability.

173. Some of the benefits which will be realised from the credit reference system are as follows:

a) reduce credit information asymmetry and potentially bring down average interest rates;

b) contribute to more robust credit risk management practices which will help promote the safety and soundness of the banking system;

c) assist the microfinance sector where lenders do not ordinarily have savings history of borrowers;

d) limit indebtedness of borrowers which is currently rampant in the economy;

e) reduction of credit risk will increase the supply of credit to businesses to fuel growth and lower lending rates; and

f) promote elaborate analysis, monitoring and oversight of individual indebtedness in the banking sector; and provide input essential for effective implementation of Basel II.

Lending Rates

174. The Reserve Bank noted that soon after the adoption of the multi-currency system in 2009, a number of banking institutions charged

penalty interest rates averaging from 30% to 60% per annum imposing a huge debt overhang on default borrowers

175. Dollarisation brought about reduced business margins compared to the hyperinflation period. Borrowers could not therefore afford the loan repayments inclusive of lending rates of above 15%, let alone the penalty rates. Consequently, the borrowers could not repay the loans resulting in the growth of NPLs

176. **Consequently, a number of borrowers have been caught in situations where they are now finding it extremely difficult to extinguish their debts, despite having made significant repayments, as the bulk of the payments constitute the interest portion.**

177. The Reserve Bank noted that, in general, borrowers risk premium which is factored in the determination of interest rates is high due to information asymmetry on their credit history.

178. The establishment of a credit reference system and the resolution of NPLs through ZAMCO will have a positive impact on interest rates.

179. The credit reference system will enhance **'reputational collateral' of borrowers which should translate to lowering their risk premium which** in turn is expected to promote a reduction in lending rates. Additionally, resolution of NPLs will clean up banks' balance sheets making them attractive to access cheaper sources of funding. This is expected to reduce the cost of funding concomitantly translating into reduced lending rates.

180. In consultation and agreement with the Bankers Association of Zimbabwe (BAZ), the Reserve Bank has formed a forum with BAZ to review, on a quarterly basis, bank charges, interest rates and the credit reference system for the betterment of the economy.

181. In addition, the Reserve Bank has also established a Banks CEO Forum that also meets quarterly to share ideas on the efficacy of the financial sector.

Bank Charges

182. It has been noted that some banks are struggling to manage costs against the backdrop of declining margins hence the tendency to compensate incomes with higher interest rates and bank charges.

183. The Reserve Bank has noted significant restructuring programs that have been adopted by many banks to cut costs and improve profitability, though with mixed success. Some banking institutions have instituted various cost cutting measures including leveraging on technology to improve operational efficiency.

184. Fees and other charges levied by financial institutions should be reasonable, having regard to the actual costs incurred by financial institutions in providing products and services to consumers.

185. The Reserve Bank urges banking institutions to continuously re-examine their business models, interrogate their cost structures and improve on efficiency.

Market Conduct

186. The Reserve Bank noted with concern a number of unethical practices and indiscipline in the sector. The **malpractices range from falsification of records, deliberate misclassification of loans, camouflaging the level of NPLs resulting in under provision and control overrides to imprudent** lending practices.

187. The malpractices cast doubt **on the fitness and probity** of the banking officials involved. The business of banking is about trust and this calls for high levels of honesty and integrity on the part of bankers.

188. The Reserve Bank calls upon banking institutions to uphold ethical conduct in their dealings with members of the public in order to maintain confidence in the financial sector.

Basel II

189. Basel II is a set of banking regulations which regulates finance and banking internationally. Basel II attempts to integrate Basel capital standards with national regulations by setting the minimum capital requirements of financial institutions with the goal of ensuring institution liquidity.

190. The Reserve Bank of Zimbabwe has adopted a gradual approach to Basel II implementation in order to allow for a smooth transition from the current system to the new approaches.

191. Basel II promotes the safety and soundness of banks and fosters sound risk management through:

(i) Improved risk sensitivity of capital requirements.

(ii) Convergence of regulatory and economic capital.

(iii) A menu of approaches which can be varied across institutions to reflect differing risk profiles.

(iv) Encouraging banks to improve further their internal risk management systems

192. Banking institutions have made progress in implementing the revised capital framework. Observations made during on-going on-site examinations are that internal systems for banking institutions are showing greater stability as banks continue to upgrade their systems.

193. However, the Reserve Bank noted the need for banks to involve independent review units such as internal auditors as well as external auditors in the validation of the Basel II related systems and processes.

194. In this regard it is expected that Basel II processes should now be part of Internal and External Auditors' work plans.

195. The Reserve Bank will conduct a final survey on the implementation progress during the quarter ending 30 September 2014 before banks go live using the Basel II compliant statutory returns beginning the first quarter of 2015.

Supervision of IDBZ and SEDCO

196. The Reserve Bank in conjunction with the Ministry of Finance and Economic Development and relevant stakeholders, are working on bringing the Infrastructure Development Bank of Zimbabwe (IDBZ) and

the Small Enterprise Development Corporation (SEDCO) to be under the supervision of RBZ. These two entities are set up in terms of the Infrastructure Development Bank of Zimbabwe Act [*Chapter 24:14*] and the Small and Medium Enterprises Act [*Chapter 24:12*], respectively.

197. These measures will promote financial sector stability through ensuring adherence, by all players in the financial services sector, to sound risk management practices and the protection of depositors through oversight by a supervisory authority.

Fitness & Probity Assessment Criteria

198. The Reserve Bank conducts fitness and probity assessments in respect of proposed directors, shareholders and senior managers of regulated entities in terms of the Banking Act [*Chapter 24:20*] and the Banking Regulations S. I. 205 of 2000.

199. In order to provide transparency in the vetting process and guidance to regulated entities, a set of prudential standards has been issued with this Monetary Policy Statement.

EXTERNAL SECTOR POLICY MEASURES

Amnesty to non-compliant market participants

200. The Reserve Bank as an Exchange Control Authority, is inundated with cases of non-compliance, which emanated from different economic environments, particularly the switch from the Zimbabwe dollar era to the multi-currency system. **While it is the Reserve Bank's obligation to ensure that market participants fully adhere to the country's**

Exchange Control laws, the authorities are also desirous to trade market discipline and self regulation with an official amnesty (pardon) to deserving cases.

201. The Reserve Bank recognises this initiative as a critical platform for **forging renewed relations with market participants**, **a necessary step towards attainment of effective collaboration in the execution of various initiatives aimed at economic reconstruction. This new thrust will manifest in the re-orientation of the Exchange Control framework to compliment its role of administration, accounting and monitoring of foreign currency transactions in the market with that of facilitating investment and business transactions.**

202. Pursuant to this objective **of boosting market confidence and enhancing relationship management,** the Reserve Bank has identified two categories deserving to be granted official amnesty.

Absolute Amnesty

203. The first category is for those cases granted **absolute** amnesty, which result in the complete exceptional reprieve of their pending cases. The pardon is permanent in that it completely strikes off the violation from the Exchange Control register. The following cases have been identified under this category:

(i) Exporters with non-recoverable overdue export proceeds; and

(ii) Machinery exported under repair and return and declared obsolete.

Conditional Amnesty

204. The second category is for cases granted **conditional** amnesty, which gives the affected party a temporary reprieve (time-period) within which to regularise and make good the violation. The following cases have been identified under this category:

(i) Exporters with recoverable overdue export proceeds;

(ii) Unauthorised external loans;

(iii) Unauthorised cross-border investments;

(iv) Non-repatriation of investment income; and

(v) Importers with outstanding Bills of Entry (Imports).

205. The Reserve Bank is concerned with increasing **incidences of capital flight** which are largely attributed to lack of confidence and the negative perception of the business environment by local domestic investors. It is also disheartening that this lack of confidence in the economy manifests itself in the externalisation of capital. The Reserve Bank is, therefore, desirous to give non-compliant market participants **a reprieve to allow them to self-introspect and exercise discipline in the conduct of foreign currency transactions.**

Absolute Amnesty to Exporters with Non-Recoverable Overdue Export Proceeds

206. In terms of Exchange Control policy, all export receipts should be repatriated into the country **within 90 days** from the date of export or when contractually due, and within any other period approved by Exchange Control.

207. As at 30 June 2014, the total overdue export proceeds (Forms CD1/CD3/PTS1) amounted to **USD303.2 million.** Of this amount, **USD108.4 million** accumulated before January 2010 is **not recoverable** owing to the following reasons:

(i) Some exporters engaged in **unauthorised set offs** of export proceeds against value of imported goods;

(ii) Some companies declared external receivables as **bad debts** without seeking approval from the Reserve Bank;

(iii) Some consignees faced operational challenges and ended up being **closed or were liquidated;**

(iv) Some exporters **relocated outside the country** without notifying the Reserve Bank; and

(v) Some exporters who have been under sanctions had their **export proceeds seized** by the US Department of the Treasury through the Office of Foreign Assets Control (OFAC).

208. Table 6 illustrates the total non-recoverable overdue export receipts for the period 2003 to 2009. Prior to the adoption of the multi-currency system in February 2009, there was a high incident of exporters repatriating their export earnings through unofficial channels. Some exporters were trading on the parallel market to evade the statutory requirements prevailing then. It is these exporters who are finding it difficult to account for these proceeds to formally acquit their export documentation with the Reserve Bank.[1]

[1] In terms of the Exchange Control Act [Chapter 22:05] Section 5, any person who contravenes the provisions of the Act other than observance of secrecy under the Act, should be convicted and made liable to such a fine and/or imprisonment as the court deems fit.

Table 6: Overdue Export Receipts declared Non-recoverable

Year	Declared Overdue Values on Forms CD1 (USD)	Declared Overdue Values on Forms CD3 (USD)	Declared Overdue Values on Forms PTS1 (USD)	Total (USD)
2003	1,109,872	1,288,908	-	**2,400,783**
2004	19,957,798	6,363,643	-	**26,323,444**
2005	13,666,304	4,470,320	1,535,057	**19,673,686**
2006	12,865,650	3,428,957	1,963,394	**18,260,007**
2007	8,417,620	7,370,203	917,371	**16,707,201**
2008	12,358,408	5,728,605	-	**18,089,021**
2009	3,544,859	3,452,454	-	**6,999,322**
Total	**71,920,511**	**32,103,089**	**4,415,821**	**108,439,422**

Source: Computerized Export Payments Exchange Control System (CEPECS)

209. In this regard, Exchange Control has developed transparent eligibility criteria to write off these **non-recoverable** overdue export proceeds amounting to **USD108.4 million** through an official pardon, **effective 1 September 2014.** Exchange Control shall in due course issue detailed operational modalities to Authorised Dealers.

Absolute Amnesty on Unreturned Exported Machinery and Equipment

210. Companies raise Forms CD1s for export of machinery and equipment for repair and return. These Forms CD1s are normally acquitted upon submission of Bills of Entry (Imports) as evidence of being returned into the country after repair.

211. However, the Reserve Bank has on record a number of cases of non-compliance where such exported machinery and equipment has not been returned long after the expected repair period. In some cases, exported

machinery and equipment is **genuinely declared obsolete**, whilst in some cases **there are false declarations**.

212. **Absolute amnesty will be granted to deserving cases.** In the same manner, **a transparent eligibility criteria has been developed** and shall be communicated by Exchange Control through Authorised Dealers in due course.

Conditional Amnesty to Exporters with Recoverable Overdue Export Proceeds

213. As at 30 June 2014, recoverable export proceeds amounted to **USD194.8 million** of the declared Forms CD1/CD3/PTS1 raised after 1st January 2010.

214. Under this category, exporters whose export receipts are overdue and categorised by Exchange Control as recoverable shall be granted **conditional amnesty to regularise their overdue positions within 90 days (1 September - 31 November 2014).** The applicable temporary reprieve on such exporters will be in the form of a graduated relief on administrative penalties currently being imposed on non-acquittals using the flagging criterion.

215. Table 7 below illustrates the total recoverable overdue export receipts for the period January 2010 to date.

Table 7: Overdue Recoverable Export Receipts (2010-2014)

Year	Overdue Forms CD1 (USD)	Overdue Forms CD3 (USD)	Overdue Forms PTS1 (USD)	Total (USD)
2010	18,485,874	2,851,096	3,229,640	**24,566,609**
2011	59,924,676	914,265	365,788	**61,204,725**
2012	21,645,279	411,475	6,657,521	**28,714,276**
2013	11,629,882	294,781	5,110,902	**17,035,564**
2014*	52,755,057	2,243,607	8,327,237	**63,325,901**
Total	**164,440,768**	**6,715,224**	**23,691,088**	**194,847,075**

Source: Computerized Export Payments Exchange Control System (CEPECS)

* As at 30 June 2014

216. As at 30 June 2014, all exporters with Forms CD1/CD3/PTS1 that became overdue during the period 1 January 2010 to 31 December 2012 shall be granted a three month (90-day) reprieve to benefit from the reduced graduated export documentation access fee.

217. Exporters are expected to fully acquit their overdue export earnings within the 90-day amnesty period after which, those exporters having overdue positions after the expiry date shall continue to be subjected to the normal administrative penalty fees, currently in force. The applicable graduated Exchange Control flagging framework shall be communicated to Authorised Dealers in due course.

218. Exporters with overdue positions from 1 January 2013 to date will continue to access export documentation using the current flagging framework.

Conditional Amnesty on Unauthorised External Loans

219. The Reserve Bank is fully aware that some companies have contracted unauthorized offshore loans in an effort to sustain their local operations. Exchange Control policy requires that all external loans should be registered with the Reserve Bank.

220. In order to allow for the full accounting through formal regularization of the unauthorised offshore loans, the Reserve Bank **shall grant a three month (90-day) conditional amnesty to such companies to register their external loans with Exchange Control.**

221. The 90-day temporary reprieve should allow Authorised Dealers and their affected clients to exercise discipline and make good **these unwarranted cases of Exchange Control violations.**

Conditional Amnesty on Unauthorised Cross Border Investments

222. The Reserve Bank has on record cases under investigation where some Zimbabwean corporates established cross border investments without the requisite Exchange Control approvals. Such unauthorised cross border investments earn profits and dividends which are not repatriated back into the country to benefit the domestic economy.

223. Similarly, **Zimbabwean investors with unauthorised cross border investments shall be granted a 90-day conditional amnesty to give them** sufficient time to regularise their offshore businesses with Exchange Control.

224. The temporary reprieve on these delinquent cases, **means that the Reserve Bank will during that 90-day period, suspend its investigations and referrals for possible prosecution.**

Conditional Amnesty on Non-Remittance of Investment Income

225. Cross border investments authorised by Exchange Control are required to make regular quarterly submissions to the Reserve Bank on their performance offshore and repatriate investment income back into the country to recoup the initial capital outlay.

226. The Reserve Bank is concerned that most of these cross-border investments have not complied with Exchange Control provisions. In fact, **Exchange Control is inundated with requests for re-capitalisation on the same non-performing unauthorised offshore investments.**

227. In some cases, offshore investors have falsely attributed the non-repatriation of dividends to the need to recapitalise their failing investments. The Reserve Bank is fully aware that some investors continue to externalise foreign currency earned from these offshore investments.

228. In the same vein, **the Reserve Bank shall give such investors a temporary reprieve of 90 days to comply with the Exchange Control requirements of quarterly declaration of financial reports and repatriation of investment income in the form of declared dividends.**

Importers with Outstanding Bills of Entry

229. Following the introduction of the multi-currency system, the Reserve Bank further liberalised the Current Account transactions. In this case, the

requirement for seeking prior Exchange Control approval for all import payments was removed. However, the **removal of import restrictions has resulted in increased cases of capital flight through payment of non-existent imports and rampant transfer pricing.**

230. In order to account for imported goods, the Reserve Bank introduced an administrative requirement for importers to acquit their Bills of Entry (Imports) with Authorised Dealers as proof of receipt of imported goods into the country.

231. The Reserve Bank is concerned **that Exchange Control audits conducted have shown that there is a significant amount of import payments not matched with acquitted Bills of Entry (Imports). This implies that some importers are making false payments** which have no corresponding value of imports coming into the country.

232. As at 30 June 2014, outstanding Bills of Entry (Imports) amounted to **USD5.8 billion**, for advance import payments for the period January 2009 to June 2014.

233. Importers have not been acquitting their Bills of Entry (Imports) taking advantage of the liberalised current account framework. This development is worrisome as it demonstrates possible cases of illegal externalisation of foreign currency by some importers **and the general lack of discipline in the economy.**

Table 8: Overdue Bills of Entry (Imports) (USD million)

Year	Total Merchandise Imports Incl. fuel	Overdue Bills of Entry (Imports)	% Non-Compliance
2009	934	412	44%
2010	1,257	455	36%
2011	3,791	1,461	39%
2012	5,182	1,474	28%
2013	5,295	1,448	27%
2014*	2,467	540	22%
TOTAL	**18,925**	**5,790**	**31%**

Source: CEBAS System, Exchange Control

234. In order to curb externalisation and ensure that the **country receives true and fair value from its import payments, importers shall be granted a conditional amnesty of 90 days (1 September – 30 November 2014)** to acquit their Bills of Entry with Authorized Dealers for advance payments for all imported goods.

235. **In instances where there were no imports being sourced the funds externalised should be repatriated back to Zimbabwe during this amnesty period.**

236. **After the expiry of this temporary reprieve period, the Reserve Bank shall introduce an importers' flagging criterion with high administrative penalties similar to those currently being applied on exporters with overdue export receipts.** Exchange Control shall issue the applicable flagging framework for importers to be effected on delinquent importers with effect from **1 December 2014.**

Review of Nostro Account Balances Threshold

237. As part of the Reserve Bank's broad measures to improve market liquidity, Authorised Dealers are currently required to maintain a maximum of **30%** of their **Foreign Currency Account (FCA) balances which exclude domestic FCA balances** in Nostro Accounts to meet their day to day international payment obligations.

238. It should be noted that keeping large balances in Nostro Accounts is **tantamount to providing liquidity to those offshore jurisdictions where accounts for Authorised Dealers are domiciled. The boosting of liquidity in those countries is at the expense of Zimbabwe's liquidity situation.**

239. As at 30 June 2014, total FCA balances excluding domestic FCA balances held with Authorised Dealers amounted to **USD1.7 billion, of which USD276.6 million were balances** held in Nostro Accounts, representing an average **of 16.5%** or **5.7%** of total bank deposits of US$4.8 billion. This shows that the historical bank holdings in Nostro Accounts have **been more than sufficient to meet Authorised Dealers' international payment obligations.** These developments undoubtedly create more room for the downward review of the Nostro Account balances threshold to allow for further injection of cash resources from Nostro Accounts into the domestic economy.

240. In order to sustain the gains achieved by the policy on improving market liquidity and to simplify the method of calculating the compliance threshold, **with immediate effect, the maximum Nostro Account compliance threshold shall be reviewed from the current 30% of FCA balances excluding domestic FCAs to a simplified threshold of 5% of total FCA balances.** There will be no need to split banks'

deposits between domestic and non-domestic FCAs for the purpose of complying with this new threshold of 5% on the basis of **going back to basics.**

241. Authorised Dealers shall continue to be allowed the normal 48-hour adjustment period in the event account movements result in them exceeding the maximum threshold.

242. Exchange Control shall issue the applicable penalties to be levied for non-compliance.

243. Furthermore, the implementation of the first phase of the Computerised Exchange Control Nostro Account Monitoring System (CENAMS) has improved compliance levels by Authorised Dealers. In this regard, the second phase of CENAMS to enhance the declaration and performance of Authorised Dealers' Nostro Accounts has been developed and will be rolled out in due course.

Compliance with International Anti-Money Laundering Measures

244. Zimbabwe is a member of the **Eastern, Southern African Anti-Money Laundering Group (ESAAMLG),** and is committed to fight against money laundering and the financing of terrorism. As part of its commitment to fight against money laundering, the country is expected to closely monitor the movement of cash across its international borders.

245. The Financial Action Task Force (FATF) experts have concluded that most criminal and terrorist groups launder their funds mainly through:
(a) Cash exports by individuals;
(b) Cash deposits to or withdrawals from bank accounts; and

(c) Wire transfers.

246. Money laundering has adverse effects, both in economic and social terms. If left un-checked it can erode a nation's economy through changing the demand for cash and the country can be black-listed and will be barred from conducting any international transactions.

247. **In complying with the international anti-money laundering measures, most countries have imposed restrictions on movement of cash across their borders as shown in Table 9 below:**

Table 9: Limits on Foreign Currency Exports by Individuals

COUNTRY	LIMITS ON CASH EXPORTS (US$ EQUIVALENT)	(GDP NOMINAL) 2013 US$
Angola	5,000 per year	124 billion
China	5,000 per exit	9.3 trillion
India	5,000 per exit	1.7 trillion
Kenya	4,999 per exit	45 billion
Russia	10,000 per exit	2.1 trillion
South Africa	500 per exit	354 billion
USA	10,000 per exit	16.7 trillion
Zimbabwe	10,000 per exit	13.2 billion

Source: International Air Transport Association (IATA)

248. As part of anti-money laundering measures and consistent with similar countries' limits on export of cash and the need to promote the use of plastic money, the limit on export of cash has, **with effect from 26 August 2014**, been reduced from **US$10,000 per exit to US$5 000 per exit.**

249. Similarly, importation of goods and services above US$ 5 000 should ordinarily be processed through normal banking channels.

250. The Reserve Bank and ZIMRA are working on ways and means on strengthening the use of the **Form 47 in order to avoid its abuse by using Zimbabwe as an arbitrage economy.**

Removal of Prior Exchange Control Approval on Importation of Foreign Currency Notes by Banks

251. Importation of foreign currency notes currently requires specific prior Exchange Control approval. Given the improved compliance status of banks following the implementation of EXCORS, there is need to remove this approval requirement and allow banks to freely import cash under the delegated Exchange Control authority.

252. **Therefore with immediate effect Authorised dealers shall be allowed to import foreign currency notes from their Nostro Accounts without prior approval from the Reserve Bank.**

253. **Total cash holdings of each bank shall, however, not exceed 15% of total FCA balances with effect from 1st September 2014. This policy measure is intended to avoid abuse by market players and to comply with anti-money laundering measures.**

Imports of Non-Essential Merchandise Goods

254. In recent years, the Zimbabwean economy has experienced a widening trade deficit as a result of the country's continued reliance on imported goods.

255. An in-depth analysis of merchandise imports shows that the country is importing non-essential goods as well as goods that can be produced locally. Over and above worsening the liquidity situation, the increased

appetite for non-essential imports has added to the collapse of domestic **production to the detriment of both employment and tax collections.**

256. The Reserve Bank, therefore, **urges market participants to exercise restraint and use limited foreign currency resources responsibly to avoid the collapse of domestic economy and the exportation of jobs and incomes.**

257. The Reserve **Bank also calls upon all the relevant arms of Government that are responsible for issuance of import permits to exercise restraint by ensuring that the country does not continue to incur a huge import bill from non-essentials or goods that can be produced locally and to levy appropriate duties to encourage domestic production.**

258. **Effective collection of duty is also very essential to avoid the current porosity at border posts wherein goods are finding their way into the country duty free much to the detriment of the local economy.**

259. The productive sector should work towards improving production efficiency and lower costs of production in order to be competitive.

Foreign Investment Promotion and Facilitation

260. The country's funding requirements underscore the need for an enhanced approach towards the mobilization of increased cross-border financial inflows, to provide liquidity.

261. As part of measures to boost and sustain market liquidity, the Reserve Bank is expected to play a facilitative role through the provision of an investor-friendly regulatory framework. **There is need, therefore, to**

create conducive conditions that allow the free and unfettered inflow of foreign investment.

262. Pursuant to this, the Reserve Bank has considered the removal of selected Exchange Control capital restrictions, notwithstanding that the capital account has not been liberalised.

Removal of Restrictions on Capital Remittances

263. In terms of the current Exchange Control policy on capital remittances, all disinvestment proceeds arising from **pre-May 1993 investments require prior Exchange Control approval** and are eligible for re-investment on the domestic market for a period of **5 years** prior to remittance.

264. **With immediate effect, all disinvestment proceeds arising from both pre-May 1993 and post-May 1993 shall be fully remittable.** In this regard, investors may remit offshore any capital plus appreciation to any destination of their choice, after Exchange Control approval has been granted.

Review of the External Loans Threshold

265. Current policy states that all loans of USD1 million and above require ELCC approval, whilst external loans below USD1 million are approved at the Authorised Dealers' level. The requirement for a limit on loans approved at bank level is necessitated by the need to curb externalisation through fictitious loans and enable full accounting of the country's external liabilities.

266. Given the need to streamline the approval processes so as to enhance timeous accessing of offshore loans, **the threshold for approval of offshore loans by Authorised Dealers without need for prior Reserve Bank approval is hereby increased from the current USD1 million to USD7.5 million.**

267. This relaxation of Exchange Controls is necessitated by improved compliance levels by Authorised Dealers following the implementation of the Exchange Control Compliance Rating System (EXCORS) by the Reserve Bank. In this regard, the Reserve Bank has noted that EXCORS has improved Authorised Dealers' operational efficiency and effectiveness.

Consolidated Framework for Review of External Loans and Foreign Investments

268. Currently, applications for foreign equity and for contracting external debt are processed separately by the **Exchange Control Review Committee (ECRC) and External Loans Coordinating Committee**, respectively. However, all external debt and foreign equity proposals are subject to Exchange Control rules and regulations.

269. The current set-up is bureaucratic and negates the **back to basics** principle as it prolongs the approval process for investors wishing to bring their capital into Zimbabwe. In some cases, a foreign investor's application for equity participation comes with an external loan component which is then split for consideration by another committee.

270. **In order to streamline and expedite the approval process, the processing of external loans and foreign investment applications shall**

with immediate effect be done under a consolidated and synchronised External Loans and Exchange Control Review Committee.

Promotion of Offshore Investments

271. The Reserve Bank has approved a number of investments by local corporates venturing into the region and internationally. At a time when the country is faced with liquidity challenges, such investments lead to the creation of long term foreign assets, which have the potential to earn the country foreign currency in investment income.

272. Furthermore, these investments have the potential to unlock debt and equity capital which is currently, evasive owing to the country's perceived risk. The success of such investments will undoubtedly result in Zimbabwe being ranked highly as an investment destination of choice.

273. **The Reserve Bank supports such investments which create Zimbabwean offshore companies and have a potential to yield quick and long-term gains to the country. However, key to the success of the offshore investments is the promotion of discipline by local investors in ensuring remittance of investment income in the form of profits, dividends and other income back into the country.**

274. The Reserve Bank shall continue to objectively consider such proposals with the aim of promoting Zimbabwean offshore companies. The investments should **clearly outline the benefits which the country will accrue** to ensure the investments payback, the initial capital outlay and provide further income to the economy. Exchange Control will enhance its **monitoring of these approved investments** for periodic reporting

requirements, and on-site audits/visits to monitor and verify reported performance of the offshore investments.

Removal of restrictions on the participation of foreign investors on the Bond Market

275. The Reserve Bank takes a keen interest in efforts by various stakeholders in developing money and capital markets given their criticality in enhancing financial deepening. It is therefore, necessary to align policies to ensure the successful mobilisation of external finance to boost market liquidity.

276. In terms of current policy on investment, in the bond market, foreign investors may subscribe for up to 35% of primary issues of bonds provided the purchase is financed by inward transfer of foreign currency through normal banking channels. The same policy also prohibits foreign investors from making purchases from the secondary market.

277. **In order to encourage foreign investment inflows and further develop the country's bond market, exchange control restrictions on the level of foreign participation on primary issuance of bonds and participation by foreign investors in the secondary market are removed, with immediate effect.** The purchase of bonds shall be financed by confirmed inward transfer of foreign funds through normal banking channels.

278. The Reserve Bank shall put in place enhanced reporting and monitoring structures to ensure the full accounting of these foreign capital inflows.

Increased participation by Diasporans on the ZSE

279. In 2004, as part of opening up the capital account to allow the participation of Zimbabweans in the Diaspora on the Zimbabwe Stock Exchange, the Exchange Control limit of such participation was increased from 40% to the current 70%.

280. **The Bank continues to recognise the important role that international remittances play in the development of emerging economies. As such, Diasporans play a critical role in economic development of their home economies. In order to allow Zimbabweans in the Diaspora to fully participate in the economic development of their country, all non-resident Zimbabweans shall be permitted to invest in any listed counter on the Zimbabwe Stock Exchange without any limit, i.e. up to 100%.**

281. The Reserve Bank will re-orient Homelink Pvt Ltd to provide a facilitative platform through which Zimbabweans in the Diaspora can be assisted to invest back home. Homelink will collaborate effectively with the Zimbabwe Stock Exchange, Zimbabwe Investment Authority and other financial institutions to develop various investment instruments, such as high yielding Diaspora Bonds. The Bank will also put in place appropriate risk management measures to assure Zimbabweans in the Diaspora **safety on the value of their investments.**

Promotion of Securities Trading Efficiencies and Enhanced Risk Management

282. The Reserve Bank, in its effort to create a monetary regime supportive of the country's overall foreign investment promotion activities, stands ready to support initiatives that are meant to attract all forms of foreign investment into the country.

283. One such area involves the institutionalization of the Central Securities Depository (CSD), which is meant to usher in the electronic trading of securities on the Zimbabwe Stock Exchange (ZSE). Chengetedzai Depository Company Limited has been mandated by the Securities Exchange Commission to establish the depository.

284. The establishment of the depository will bring in efficiency gains which will facilitate trading with enhanced risk management and an increase in the attractiveness of the capital market to external investors.

285. As Monetary Authorities, we are supportive of these efforts given the underlying need for reducing the settlement cycle from the current (T+7) to (T+3) which is the norm obtaining on other external exchanges, and meets international best practice.

286. **To facilitate the attainment of this noble objective, the Reserve Bank shall collaborate closely with the Zimbabwe Stock Exchange, Securities Exchange Commission and the Depository Company to align its Exchange Control regulatory framework to accommodate the electronic trading of securities in the country.**

Disposal and Remittance of Immovable Property Proceeds

287. Current Exchange Control regulations require specific applications to be made to Exchange Control for the remittance of proceeds arising from disposal of immoveable property.

288. **In order to have clarity, as well as allow property owners to make use of their sale proceeds in a manner that enhances liquidity in the market, the following shall apply:-**

Immoveable Properties Acquired Using Offshore Funds

289. The disposal of immovable property and remittance of the proceeds by **foreign individuals shall be handled by Authorised Dealers after the client has provided documentary evidence** confirming inward transfer of funds to purchase the property.

290. The disposal of such immoveable property by foreigners shall be eligible for **100%** remittance upon request.

Renewal of Authorised Dealership Licence and Exchange Control Compliance Rating System (EXCORS)

291. In June 2013, Exchange Control introduced a Compliance Rating System to systematically and effectively monitor all Authorised Dealers by classifying them according to their compliance levels with Exchange Control Rules and Regulations.

292. The Compliance Rating System assigns ratings to all banks on a scale of 1 to 5, depicting a bank's level of compliance. Successful renewal is predicated upon attainment of a minimum compliance level of a rating of three (3). The scale is applied as in table 10.

Table 10

OVERALL RATING	RATING
Excellent	5
Very Good	4
Good	3
Unsatisfactory	2
Poor	1

293. Authorized Dealers have displayed increased levels of compliance with Exchange Control Rules and Regulations since the introduction of EXCORS.

294. Table 11 below shows the statistical analysis of compliance ratings that were awarded to Authorised Dealers in 2013 and 2014.

Table11: Statistical Analysis of Compliance Levels

NO	STATISTICAL DISCRIPTION	RATINGS IN 2014	RATINGS IN 2013
1	HIGHEST RATING	4.500	4.300
2	LOWEST RATING	3.510	3.000
3	MEAN	4.203	3.790
4	MEDIAN	4.273	3.770
5	STANDARD DEVIATION	0.230	0.320

295. The liberisation of the current account has seen an increase in Exchange Control transactions at branch level and the compliance framework requires renewal of Authorised Dealership licence on an annual basis. The new compliance monitoring framework is also being automated to apply best practices and Exchange Control's capacity building programme will be intensified to build the necessary competencies in Exchange Control operations.

296. In this regard, and pursuant to the new Authorised Dealers licencing framework, the licensing fees have been reviewed from the current $400, as follows;

- **Head Office USD 1, 000 per annum**
- **Branch USD 500 per branch per annum**

297. The Reserve Bank **urges banks to exercise extreme caution in the conduct of cross border transactions, and apply as much as possible the KYC principle, in ensuring adherence to the existing Exchange Control framework.**

MEASURES TO BUTTRESS THE MULTIPLE CURRENCY SYSTEM

Upholding the Multiple Currency System

298. A lot of debate has been going on about the longevity of the multiple currency system in Zimbabwe. **Government's consistent and official position is that the country is using the multiple currency system. This position has been well articulated by the Minister of Finance and Economic Development, Hon Patrick Chinamasa, and is the bedrock under ZimAsset. The local currency would only be resuscitated when the country's foreign exchange reserves and domestic production levels are significant enough to sustain its rebirth.**

299. **The current low levels of production within the economy concomitant with the high levels of imports are not conducive for the return of the local currency. It would therefore be economic suicide for**

Government to do so without foreign exchange reserves to anchor the local currency.

Deflation under the Multiple Currency System

300. Again a lot has been said and written on this subject matter. Our considered view is that deflation which is defined as the reduction in the general level of prices in an economy was inevitable in the Zimbabwean economy. The prices of goods and services that are being charged in Zimbabwe continue to be higher than those charged within the region and international markets, **thus the reduction in prices was an unavoidable price correction process or a self-adjustment process for companies and individuals to remain in business in a tight liquidity economy.** The high domestic prices also contribute to the incidence of high propensity to import within the economy. Table 12 provides a comparison of prices of selected products in Zimbabwe and the region.

Table 12

Regional average price comparisons of selected goods (US$)

Commodity	**Zimbabwe**	**S. Africa**	**Botswana**	**Mozambique**	**Zambia**
Milk (1 litre)	1.40	1.01	1.17	1.95	1.53
White bread (loaf)	1.00	0.94	0.70	1.29	1.13
White rice (1kg)	2.29	1.45	1.61	1.67	1.80
Eggs (12)	2.21	1.83	1.93	2.07	1.98
Cheese (1kg)	10.12	6.45	5.02	8.46	13.13
Apples (1 kg)	3.67	1.52	1.99	3.05	3.13
Oranges (1kg)	3.00	1.37	1.78	1.57	2.44
Tomatoes (1kg)	1.96	1.45	1.80	1.34	1.36
Potatoes (1kg)	2.12	1.18	1.94	1.30	2.49
Local transport(1 way)	1.00	1.03	0.40	0.25	0.79
Apartment (85 m2)	177.33	92.41	49.06	82.00	66.70
Petrol (1 litre)	1.52	1.25	1.07	1.62	1.88
Newspapers	1.00	0.50	0.50	0.50	0.50

Importation of coins

301. The most plausible reason given by the Retail Association of Zimbabwe, businesses and individuals across the nation for the discrepancy of prices as indicated in Table 12 in Zimbabwe and the rest of the world **is lack of change within the economy to the extent that sweets and tokens/vouchers are issued as change to the general public. Barter trade is also in use especially in the rural areas. In order to ameliorate this problem of change and it's unintended consequences on the price levels in the economy, the Reserve Bank shall be importing special coins of 1c, 5c, 10c, 20c, and 50c whose values would be at par with the US cents. Rand coins of 10c, 20c, 50c, R1, R2 and R5 are also being imported to buttress the multiple currency system which is dominated by US$s and Rands.** These coins would be distributed to business through normal banking channels from the Reserve Bank.

302. The Bank through its Bank Use Promotion Unit shall monitor that the coins are utilised as change to bring decency in the economy.

Mobilisation of Financial Resources

303. As already indicated, **RBZ is in the process of arranging medium to long term offshore funding to shore up liquidity in the economy for enhancing gold production and the lender of last resort function. This is in line with Cabinet approval for the restoration of the Bank's role to arrange and negotiate financing facilities for the economy at large. The Bill will be gazetted in due course.**

Interbank Market

304. The African Export Import Bank (Afreximbank) guaranteed interbank market facility (or Aftrades facility) of US$100 million is **earmarked to be operational between end of August and mid-September 2014.** This facility would go a long way to augment the current bilateral like-minded intermarket trades taking place in the financial sector. The Aftrades facility is a sector-wide facility that shall also complement the lender of last resort function of RBZ. **The delay in the launch of this facility was attributable to the need to make the instruments under Aftrades tradable in the secondary market. This has been completed.**

Demonetization

305. As Monetary Authorities we are convinced that demonetization of the Z$ currency is a necessary process that Government should do to compensate the banking public. **Consistent with the 2014 Budget Statement, Government should therefore come up with a permanent solution to this matter to restore confidence and good will.** The old local currency should be retired since it was replaced by the multiple currency system.

POLICY ON RESERVE BANK SUBSIDIARIES

306. The Reserve Bank has four subsidiaries, namely, Fidelity Printers and Refiners, Aurex (Pvt) Ltd, Export Credit Guarantee Corporation of Zimbabwe (ECGC) and Homelink (Pvt) Ltd. The Reserve Bank is in the process of ensuring the operations of these companies are enhanced so that they play a meaningful role in the economy.

Aurex

307. Zimbabwe has a diversity of precious and semi-precious minerals, namely, gold, emeralds, platinum, diamonds, silver and many others. In line with ZimAsset, leveraging own resources is critical for sustainable growth and development of the economy. Value addition and beneficiation to the country's natural resources is one of the key pillars of ZimAsset.

308. Against this background, the Reserve Bank is working towards reviving Aurex, whose capacity utilization had declined due to the harsh economic environment, to promote beneficiation of the country's minerals.

309. **Aurex adds value to the locally available gold, diamonds and silver, which benefits the economy through local sales and exports, as well as job creation.**

310. Once the company has been adequately capitalized, obsolete equipment will be replaced to enhance production efficiency and product quality. This will enable the company to take a leading role in the beneficiation of the country's precious minerals.

Export Credit Guarantee Corporation of Zimbabwe

311. In view of subdued export performance that has undermined the country's foreign exchange generative capacity, with negative repercussions on liquidity conditions, there is need to promote the country's productive and export sectors.

312. Against this background, the Reserve Bank is in the process of recapitalising ECGC, with a view to enable it to guarantee credit exports.

This is particularly important, as a well-capitalized ECGC would provide guarantees against exports and trade related losses. Importantly, this is envisaged to support export growth and unlock export earnings.

313. In addition, ECGC will assume an additional role to guarantee domestic loans accessed by small to medium scale enterprises (SMEs). This coupled with the simultaneous establishment of the Credit Reference Bureau is envisaged to promote lending by banks to SMEs and businesses requiring micro financing.

314. This added function of ECGC is expected to help in mainstreaming informal sector SMEs, pull their savings and enable them to access formal banking services.

315. **These measures are envisaged to provide strong impetus to formalizing the informal sector and promote the production of domestic and export commodities.**

Fidelity Printers & Refiners

316. As stated in our January 2014 Monetary Policy Statement, Fidelity Printers and Refiners (FPR) is now the sole buyer and exporter of gold in the country. This position is critical to ensure transparency in the accounting and marketing of gold.

317. As at 31 July 2014, **7.3 tonnes** had been purchased and processed for export by FPR. This is quite remarkable given that gold output had declined to **3 tonnes** in 2008. FPR are projecting an output of 13 tonnes by year end and to continue with the application for accreditation to the London Bullion Marketers Association that needs a threshold of 10 tonnes per year for admittance.

318. The Bank is working closely with the Ministries of Finance and Economic Development and Mines and Mining Development to establish **Gold Service Centres** to harness gold from artisanal miners and SMEs **and to put in place supportive measures to enhance gold production in the country.** The Gold Service Centres are over and above the **existing gold buying centres** that FPR is using at ZB Bank branches around the country.

Gold Bonds

319. Government has commenced to redeem, through Treasury Bills, the previous debt owed by RBZ to creditors. **RBZ and/or FPR do not have liabilities from the current purchases of gold. Artisanal miners and SMEs are paid upon delivery whilst the large scale producers are paid within 48 hours.**

Homelink

320. The Bank is quite **appreciative of the contribution of the Diasporans** to economic development in Zimbabwe with remittances from the Diaspora of **US$412 million** for the first six months of this year far exceeding the **US$67 million** from FDI for the same period. It is against this background that Homelink shall be revamping its operations to provide tailor made products and services that meet the needs of the Diasporans.

POLICY ADVICE

Promotion of Foreign Direct Investment

321. The growing import dependence that has typified the negative trade developments over the past few years, has largely been occasioned by

attendant supply gaps in the economy. A significant number of manufacturing companies have either closed shop or relocated to other countries which has resulted in output gaps widening in the economy.

322. It is against this background that the country has increasingly relied on imported finished goods from South Africa and the Far East, to bridge the domestic supply gaps. Additionally, the country has persistently experienced a net outflow of liquidity through absorption of disproportionately high levels of imports.

323. Attempts to regain lost export and domestic markets have remained constrained by **lack of competitiveness, largely emanating from high production costs. This reflects the country's costly production models on the back of outdated and antiquated machinery. On the other hand, the country's regional and international competitors have adopted low cost, efficient and advanced technology.**

324. As such, imports have taken over the domestic market as they attract lower prices, while exports have **lacked the competitiveness** required to capture new and previously lost markets.

325. On the back of these developments the need to invest in the latest technology to regain the much-needed competitive edge in the domestic market and international export destinations should be prioritized.

326. In this regard, there is need for Government to implement deliberate policies that attract foreign direct investment and exploit the liberalised exchange control policies on capital and dividends for the benefit of the economy. This is largely so, **as non-debt creating investments, create employment, effectively plug supply gaps, reduce import dependence**

and moderate the haemorrhaging effect of imported finished products. The Bank is therefore pleased by the call of His Excellency, the President, Cde R. G. Mugabe at last week's Southern African Development Community (SADC) Summit for South Africa **to empower the region through value addition investments in SADC.**

Clarity of Investment Regulations

327. Whilst the Reserve Bank is clear on the topical subject on the Indigenisation and Economic Empowerment Policy, the Policy is unfortunately misunderstood or misinterpreted by both local and foreign investors. Zimbabwe has a clear Indigenisation and Empowerment Policy which has been clearly articulated over time by his Excellency, the President, Cde. R G Mugabe and the Minister of Youth Development, Indigenisation and Empowerment, Hon Francis Nhema.

328. The Indigenisation and Economic Empowerment Regulations, especially **Section 5 paragraph 4, shows that the Policy is not ambiguous**. **It takes into account flexibility in terms of time and scope (joint ventures, build own operate and transfers projects, land use agreements and contract farming etc) for compliance, use of empowerment credits for compliance purposes and that it is not a one size fits all Policy. The Policy as captured in the Act and Regulations is clear but its publicity is not.**

329. In view of the above, it is essential that Government consider guiding **investors in a clear manner through the gazetting of sector-specific investment regulations and guidelines. Additionally, defining and gazetting clear empowerment credits for compliance with the Indigenisation and Economic Empowerment Policy in line with the**

regulations is critical to promote investment and to ensure that the Policy is consistent and compatible with ZimAsset. The Policy should also ensures that local investors feel at home so that they become good ambassadors for the attraction of more investment into the country.

330. **Such clear regulations when put in black and white would put to rest most of the current misunderstandings and misconceptions surrounding the country's noble objectives** under the Indigenization and Economic Empowerment Policy.

Dealing with the Negative Effects of Sanctions

331. The country's investments drive would need to be complimented by dealing with the negative perception and adverse effects of the **sanctions albatross on foreign financial flows, including FDI on the Zimbabwean economy. Thus apart from blocking funds under the Office of Foreign Assets Control (OFAC) rules as part and parcel of the restrictive measures, the collateral damage of the sanctions is quite high and severe as sanctions have a direct effect of increasing political and/or country risk premium of doing business in Zimbabwe.** The net effect is that FDI is discouraged from coming into Zimbabwe, whilst lines of credit dwindle and foreign banks shunning Zimbabwe.

332. **The sanctions risk is not insurable. Other undesirable and unintended consequences like corruption, smuggling of goods, etc have as a result manifested under the guise of fighting sanctions**

much to the detriment of the economy and peace loving Zimbabweans.

333. We therefore genuinely welcome the positive initiatives by the European Union on this matter and we would like to urge the United States of America to continue to review the OFAC rules to assist this small economy to attract the much needed capital for recovery.

Debt Resolution

334. The country's outstanding debt, which is largely in arrears, has grown to be a constraint on the country's growth and development aspirations. Essentially, a country in arrears attracts offshore loans at unfavourable conditions, on account of the risk premium attached to it. Notably, interest rates are high and conditions precedent on offshore credit facilities become difficult for domestic potential borrowers, even before making any draw-downs.

335. Against this background, the expeditious resolution of the country's debt burden remains critical in efforts geared at unlocking medium to long-term offshore credit lines, required by industry to recapitalize and re-tool.

336. In this regard, the amicable resolution of the country's external debt in a timely manner should rank high on Government's policy agenda, as this would help ease the country's tight liquidity situation, while at the same time rejuvenating industrial activity.

337. It is against the above that the country would need to continue to engage the multilateral and donor community in order to attract international capital inflows.

IMF Staff Monitored Program

338. Government is implementing an International Monetary Fund (IMF) supported Staff Monitored Program (SMP) to help the country establish a track record of sound macroeconomic policies and pave way for effective debt restructuring and resolution. The Fund, in its first and second reviews of the SMP, has expressed satisfaction with the progress made by the country this far.

339. This notwithstanding, **there is need for the country to continue implementing prudent policies, so as to remain within structural benchmarks and quantitative targets agreed with the IMF.** As such, great prominence must be attached to the successful implementation of the SMP in order to consolidate the gains achieved so far from a fiscal and monetary standpoint.

340. The country's successful performance under the SMP would provide **strong impetus to the commencement of an effective debt resolution program and open new options for increased foreign exchange** and investment inflows into the country.

Infrastructural Development & Management of Recurrent Expenditure

341. Infrastructure rehabilitation and development is critical in promoting the country's economic growth. Developing reliable and robust infrastructure enhances productivity, improves competitiveness of firms and makes the country an attractive destination for foreign direct investment.

342. Over the last three years the proportion of capital budget to total budget was relatively low at 14%, 10% and 12% in 2012, 2013 and 2014, respectively.

343. Government would need to find **appropriate and well-structured mechanisms for reducing recurrent expenditure to create space to increase the capital budget allocation** in order to establish a strong foundation for growth and development. Banking institutions are also called upon to support or complement Government initiatives through raising offshore funding for infrastructure projects.

Security of Land Tenure

344. It is noted that the majority of farmers have offer letters which are considered by banking institutions as a weak form of security. There is therefore need to expedite the issuance of **bankable and transferable** 99 year leases to qualifying farmers. Leases with such features are considered better forms of security than offer letters or leases which are not transferrable.

345. It is also advisable for Government to acknowledge the **responsibility to compensate farmers for improvements on farms** that were acquired under the Land Reform Programme and to come up with a validated quantum of the compensation. This position is consistent with His Excellency, the President, Cde R. G. Mugabe's stance that compensation for improvements would be done when financial resources become available. In this regard, the Bank is pleased to note that Government has since 2011 paid compensation in an amount of around US$5 million.

Information Communication Technology

346. A robust Information Communication Technology (ICT) system is one of the major driving forces for economic recovery and sustainable growth. ICT promotes improvements in innovation and productivity which are central to the economic performance of many countries.

347. **In an endeavour to promote a cashless society, utility service providers should adopt measures to promote use of plastic cards and mobile payments in the payment of utility services.**

348. Concomitantly, there is need for a deliberate government policy for investment in telecommunications systems such as fibre optic which are critical in enhancing connectivity. In addition policies that promote the **revamping of point of sale systems in retail outlets** and ensure the interoperability of payment platforms is also critical in that regard.

349. **As such, banking institutions are urged to invest in technology that will allow expansive provision of point of sale systems that can be shared among banking institutions.**

CONCLUSION

350. The theme of this Monetary Policy Statement, **BACK TO BASICS, implies returning to the basic principles of economics, banking and business and the pursuit of consistent and pragmatic policy measures necessary to stimulate production for economic recovery that is needed for economic prosperity and poverty reduction enunciated under ZimAsset.**

351. **These policies would need to be buttressed by a vigorous promotion of FDI to augment local investment. This policy stance is critical because what this country needs most at this juncture is the fishing rod (FDI) much more than the fish (imports) for sustainable development.**

352. **As Monetary Authorities, we have a critical role to play in this process and this Statement presents policy measures that I believe are robust and prudent to reinforce and boost the earnest implementation of ZimAsset and thus setting the tone for Zimbabwe's Economic Recovery.**

353. **The measures also require the nation, at all levels, to adhere to good corporate governance, transparency, integrity and above all the spirit of love and respect for each other as patriotic Zimbabweans united in our resolve.**

354. **The measures in this Monetary Policy Statement also need significant support from the international community towards the normalisation of relations with Zimbabwe through the removal of sanctions as the restrictive measures continue to have a debilitating effect on the economy. The sanctions are quite disproportionate given the small size of the Zimbabwean economy with a GDP of around US$13 billion and total banking deposits of around US$5 billion.**

355. The nation needs to fight the negative perception that Zimbabweans continue to create, knowingly or unknowingly, for ourselves. The negative perception towards the country by foreigners is mainly emanating from within Zimbabwe. **Charity begins at home.** We need to position ourselves in line with the African proverb that says "Until

lions start writing down their own stories, the hunters will always be the heroes.” [Simoen Messan Adagba]

356. We need to minimise self-condemnation and self-hatred. There is need for self-introspection, be proud and thank God for where He has taken us thus far.

357. It is so deep rooted in my heart and I have faith and optimism that Zimbabwe’s economic recovery is in sight.

358. May God bless Zimbabwe.

I THANK YOU

DR. J. P. MANGUDYA
GOVERNOR
AUGUST 2014