Poverty Reduction Forum Trust

ANALYSIS OF THE 2022 MONETARY POLICY STATEMENT-SHOULD WE STAY THE COURSE?

Introduction

The Governor of the Reserve Bank of Zimbabwe (RBZ) announced the Monetary Policy Statement (MPS) on the 7th of February 2022 in terms of Section 46 of the Reserve Bank Act (Chapter 22:15). Section 46 requires the Governor of the Reserve Bank of Zimbabwe (RBZ) to issue a statement outlining the monetary policy stance for the subsequent six months, the reasons for the policies and an evaluation of the previous period monetary policy measures. The February 2022 MPS has the theme “Stay the Course” indicating a continuation of the tightening monetary policy to curb inflation. Following the announcement of the MPS we look at its possible impact to the ordinary citizens and the areas that may require further refinement.

Assessment of the 2022 Monetary Policy

Inflation

Year-on year inflation went down from a peak of 837.5% in July 2020 to 60.7% in December 2021. This is partly as a result of a tight monetary policy introduced by the RBZ with reserve money ending the year 2021 at ZW$25.9 billion, compared to a maximum threshold of ZW$29 billion for the last quarter of 2021. The annual growth in broad money (M3) also fell from a peak of 507.9% in January 2021 to 131.8% by December 2021.

Containing broad money supply growth is important because if the money supply grows at a faster rate than the economy's ability to produce goods and services, then inflation will result. This is often known as the problem of too much money chasing few goods. As such the RBZ has set a tight monetary targeting framework. This according to the RBZ is expected to see month-on-month inflation reduced to below 4% in the first quarter of the year and to average below 3% in the second half of 2022. In the end the country’s annual inflation rate is expected to end the year in the range of 25-35%.

The inflation targets seem to be highly optimistic judging by the wage pressures emanating from the civil servants and developments in the parallel exchange rate market. While civil servants salary demands to have salaries restored to 2018 levels of US$540 for the lowest paid appear to be justified especially by the high rising cost of living, it is important that these concerns are addressed in a manner that does not affect the fiscal consolidation measures.

Dealing with the parallel exchange rate will be crucial in addressing the pass-through effect on domestic inflation.

Exchange Rate and Foreign Exchange Auction System

According to the MPS, the exchange rate depreciated from ZW$85 per US$1 for much of 2021 to close the year at ZW$108 per US$1. RBZ estimates that the parallel market premiums rose to between 40% and 90% while our observation is that this was higher and as much as 100% in some instances. The MPS also notes that the banking sector is financially sound and in compliance with banking sector capitalisation requirements.

There is no major policy shift with respect to the Auction System with the MPS promising to fine tune the exchange rate policy. This is despite representations to refine the auction system from stakeholders including mining companies represented by the Chamber of Mines, Industry represented by the Confederation of Zimbabwe Industries and the Zimbabwe National Chamber of Commerce. The fact that both exporters, importers and the general public are agreeing on the need for a review of the system is evidence enough that more should be done beyond the proposed interventions to ensure that the exchange rate is reflective of the market as possible. This will help to deal with the arbitrage opportunities created by the widening official and parallel market exchange rate.

While the Governor of the RBZ is right to say that the RBZ will not be chasing the parallel market as this is akin to "chasing one's tail", that does not take away the need to relook the current exchange rate policy. We also agree that the RBZ may not have direct control of the happenings in the parallel market exchange rate but there is still value in building stakeholders confidence in the official exchange rate. This is possible if the RBZ goes back to the Dutch Foreign Currency Auction principles envisioned at the formation of the Auction System that allow for efficient price discovery taking into consideration the inputs from all key stakeholders. History has shown that when there is confidence as like what happened in the first 6 or so months of the Auction System from June to around November 2020 stakeholders prefer the official channels which are safer. The parallel market also stabilises as what happened during the same period where the rate was around US$1 to ZWL$100. The pressures only started when signs that the foreign currency allocation system was no longer market based began to emerge.

The wide spread between the parallel foreign exchange and the official exchange rate is leading to huge arbitrage opportunities with the poor carrying the burden of the high inflation. While the auction system is meant to stabilise prices this has not been the case as profiteering took route. For example, we have a situation where you have fuel players benefitting from the auction system yet there is not much Zimbabwe dollar fuel available on the market. The PRFT's observation through our Basic Needs Basket surveys undertaken during the period September 2021, is that while formal businesses are the main beneficiaries of the auction system, the pricing in the shops reflect the parallel market exchange rate defying the whole purpose of having the system in the first place. For example, a 2 litre cooking oil which is one of the products prominent on the foreign currency list was priced at ZWL$558.99 or US$6.21 at the interbank rate or US$3.49 using the parallel rate in September

2021. The same 2 litres cooking oil is now priced at ZWL$809, or US$6.80 using the interbank rate and about US$3.67 using the parallel market rate. That is a 44.7% increase in ZWL$ terms, 9.5% using the interbank and 5.2% using the parallel exchange rate over the period September 2021 to February 2022.

Promoting the Use of Domestic Currency

The MPS seeks to promote the use of domestic currency riding on the fact that the financial system is largely constituted of local currency, with around 56% of total deposits being local currency and the balance of 44% being foreign currency deposits. One of the initiatives done to improve the use of local currency include the decision taken by Government to allow payment of 50% of royalties by exporters in local currency and part-payment of duties and taxes in local currency for imported vehicles as well as levying taxes in foreign and local currency proportionately to the export retention levels. Whilst Government has allowed the payment of royalties in local currency it still demands payment of some goods and services exclusively in the US$ such as the passports and number plates contradicting its policies. Government has also gone on to increase the forex retention for a number of exporters including 100% for tourism, 75% for tobacco and 100% of the incremental portion of the export receipts for manufacturing, horticulture and cross boarder transport. Despite these increments there is still a push for increased forex retention which points to minimal demand for local currency. Therefore one way of reducing the push for increased forex retention is ensuring that the forex allocation system is market driven giving fair value to exporters.

Mobile banking transactions limit

The MPS increased limits including from person to business from ZW$20 000 to ZW$25 000 per transaction with a maximum limit of ZW$100 000 per week; Person to person from ZW$5 000 to ZW$10 000 per transaction with a limit of ZW$70 000 per week; Increasing the cash withdrawal limit for the banking public from ZW$2000 to ZW$5000 per week. While this is welcome, this falls short of expectations considering the increased inflation.

Refinement of the US$50 Facility Accessed through Bureaux de Change

According to the MPS, the Government proposes to refine the US$50 Facility, with immediate effect, to limit it to the vulnerable members of the society, that is, pensioners, senior citizens, people with disability and those requiring forex for medical purposes. While ensuring that vulnerable groups are catered for, there is still need for mechanisms that ensure the general public can also access the foreign currency through the formal system. There is also need to deal with the errant players that abused the facility rather than closing the facility to the general public.

Credit Registry System

According to the MPS, as at 31 December 2021, the Credit Registry had 558 272 active loan contracts, with individuals' records accounting for 98.29% of the records in the Credit Registry. In terms of gender distribution, male and female borrowers constituted 68.36% and 31.64% of loan contracts in the Credit Registry, respectively. The borrowing is highly skewed against female borrowers despite the fact that they perform better when it comes to timely repayments. This is reflected in the fact that 5.81% of loans granted to female borrowers were delinquent contracts which were 90 days past due within 12 months from the date of issuance, compared to male borrowers who had 6.16% of their loans in arrears.

Conclusion and Recommendations

We agree that the RBZ has done well in terms of reducing inflation from the peak of 837.5% in July 2020 to 60.7% in December 2021. However the inflation is still very high and equally of concern is the inefficiency of the foreign currency auction system which is evident in the widening gap between the official and parallel market. As such from the above discussion we agree that "staying the course" with the tight monetary targeting framework is the right decision. However there is need to also consider the following in refining the monetary policy;

- That the RBZ should review the foreign currency auction system taking into considerations stakeholder's views and conforming to the Dutch Foreign Currency Auction principles which allows for price discovery. This will build confidence in the official foreign exchange market and help bridge the gap between the official and parallel foreign exchange market.
- Government should allow payment in local currency for all government goods and services to promote the use of the domestic currency.
- The limit on mobile banking transactions should be increased further in line with the inflation developments.
- More emphasis should be put on improving access to credit to disadvantaged groups such as women and persons with disabilities.
- RBZ and the relevant authorities (Police, Zimbabwe Anticorruption Commission etc.) must deal with abusers of the US$50 facility. On the other hand RBZ must put in place a mechanism for all citizens with genuine foreign currency requirements to be able to access the forex through official channels.

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