RESERVE BANK OF MALAWI

SPEECH BY

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INSTITUTE OF BANKERS IN MALAWI
2019 ANNUAL LAKE CONFERENCE

THEME: FINANCIAL SYNERGIES, A CATALYST FOR FINANCIAL INCLUSION

NKOPOLA LODGE, MANGOCH

30 AUGUST, 2019

- **The Director of Ceremonies, Ms Maria Bauleni;**
- **The Guest of Honour, Mrs Natalie Morris, Chief Executive Officer of EcoCash, Zimbabwe;**
- **The President of the Bankers Association of Malawi, Mr Kwanele Ngwenya who is also the Chief Executive Officer of NBS Bank;**
- **The 2nd Vice President of the Bankers Association of Malawi; Mr McFussy Kawawa;**

- **Institute of Bankers in Malawi Board Members;**
- **All Chief Executive Officers here present;**
- **The Chief Executive Officer of the Institute of Bankers in Malawi, Mrs Lyness Nkungula;**
- **Panelists and Speakers to this Conference;**
- **Sponsors to this Conference;**
- **Distinguished Delegates;**
- **Ladies and gentlemen.**

Good Morning

As usual, **Mr. President,** I am delighted to once again join you in this year's Institute of Bankers Conference. To begin with, let me join other Speakers before me to welcome the Guest of Honour, Mrs. Natalie Morris, Chief Executive Officer of EcoCash to Malawi and to this Conference and indeed all other participants. Let me also applaud the choice of this year's theme; **Financial Synergies, a Catalyst for Financial Inclusion**. It could not have come at a better time than this and I will explain why shortly.

Distinguished Delegates, Ladies and Gentlemen, we are gathered at a time the global economy has lost momentum and slowed down following a decade and half of extraordinary economic performance. In 2019, global growth is projected at a mere 3.2 percent down from 3.6 percent in 2018 and 3.7 percent in 2017. The drag in economic growth is due to a number of headwinds, key among them is the rise in trade tensions and tighter financial conditions. We live at a time the United States of America is reviewing its trading arrangements with partners, the United Kingdom is reviewing its relationship with its sister European Union nations and the global multilateral trading system under the auspices of the World Trade Organisation (WTO) is undergoing great uncertainty.

The second headwind is the monetary policy normalization in advanced economies aimed at addressing the prevailing negative interest rates. This is also complemented by unwinding of Central Banks balance sheets. Both these developments are leading to global monetary policy uncertainty and tightening of financial conditions. The third headwind is coming from China where the authorities are introducing necessary deleveraging reforms for rebalancing their economy and making growth more sustainable.

The last headwind is arising from the current unprecedented levels of stockpiles of debt. The global economy is currently sitting on catastrophic debts which have never been seen before at an all-time record of US$247 trillion in nominal terms which is equivalent to 305 percent of global GDP in 2018. Top among the list of borrowers are the United States of America, China and Japan and together, they account for two thirds of the global debt, exceeding their share of global output. On average, global debt now exceeds US$114,000 in per capital terms and is weighing heavily on the global economy.

Specifically, growth in advanced economies, is projected at 1.9 percent in 2019 and 1.7 percent in 2020. The 2019 projection is 0.1 percentage point higher than the April projection, mostly reflecting an upward revision for the United States. In the United States, 2019 growth is expected to be 2.6 percent and that is, 0.3 percentage point higher than the April WEO, moderating to 1.9 percent in 2020 as the fiscal stimulus unwinds. The revision in the growth reflects stronger-than-anticipated first quarter performance.

The emerging market and developing economy group is expected to grow at 4.1 percent and 4.7 percent in 2019 and 2020, respectively. Emerging and developing Asia is expected to grow at 6.2 percent in 2019–20. In China, negative effects of escalating tariffs and weakening external demand have added pressure to the economy in the midst of a structural slowdown and high dependence on debt.

Closer to home, in the Sub-Saharan Africa region, growth is projected at 3.4 percent in 2019 and 3.6 percent in 2020, 0.1 percentage point lower for both years than in the April WEO, as strong growth in many non-resource-intensive countries partially offsets the lacklustre performance of the region's largest economies. Higher, albeit volatile, oil prices have supported the outlook for Angola, Nigeria, and other oil-exporting countries in the region. But growth in South Africa is expected to be muted in 2019 than projected in the April WEO following a very weak first quarter performance, reflecting a larger-than-anticipated impact of strike activity and energy supply issues in the mining and weak agricultural production.

With regard to international oil prices, the IMF projects that Brent crude oil prices are expected to be lower in 2019 and 2020, averaging $66.0 and $65.0 a barrel, respectively. As of 29th August 2019, Brent crude oil price stood at US$60.3 per barrel from US$64.8 per barrel as at end June 2019. The lower prices are on account of weaker-than-expected global demand and greater-than-anticipated U.S. oil production. However, geopolitical events in Middle East, civil unrest in Venezuela, and slower-than-expected US production growth pose an upward risk to oil prices.

Here in Malawi, growth is projected at 5 percent up from 4 percent in 2018 and is expected to rise further to 6-7 percent in 2020 and beyond. This is a matter of paramount importance, and I would suggest non-negotiable. The economy needs to take a new upward norm. As we are all already aware, in the past 55 years of our independence, the economy has suffered 7 major recessions all arising out of weather shocks in 1968, 1970, 1981, 1986, 1992, 1994 and 2001. The country has also witnessed 2 significant economic rebounds and understandably so, arising out of economic recessions as the agriculture sector recovered in 1971, when we grew by 16.2% and in 1995 when we grew by 16.7%, which is our record growth year in post-colonial era. While the current growth between 2003 and 2019 can be applauded for being in a range 2.1 percent and 9.8 percent and devoid of any recession as compared to the period 1964 to 2002 when there were huge volatilities ranging from the worst ever recession of -10.2 percent in 1994 to the record growth of 16.7 percent in 1995, the trend has generally been below par as weather shocks have weighed heavily on the economy, as their frequency and intensity have persisted.

The problem has also been compounded by the fact that unlike in other countries, where economies are more balanced, the economy in Malawi is overly dependent on one sector, agriculture, and once hit, all other sectors have retreated as well.

As a result, while all other countries have progressed in terms of total GDP and per capita GDP, from around US$100 per capita per person is the early 1960s to somewhere around US$30,000 to US$60,000 per capita per person in countries such as South Korea, Singapore, Malaysia, China and others. Per capita incomes in Malawi have only edged up from the same $100 per capita per person at our independence to around US$400 per capita per person to date. More therefore needs to be done to invest in the energy sector, Agriculture and value addition, mining, tourism and manufacturing to come to the new normal of upward GDP growth trajectory which will help create jobs and improve the living standards of people in this country. It is on this basis that I support the choice of this year’s theme which is focusing on building synergies and financial inclusion. We all need to work together as an economy and support productive sectors of the economy so that we are able to move on.

On inflation, **Mr. President,** which is the preoccupation of the Central Bank, we have come back to a new and desirable norm of low and declining inflation. We are currently at 9.3 percent having come back down from an all-time worst ever performance of 95 percent in 1995 and the trend is downward which is the most promising trend since independence as the first 30 years of our independence was generally characterized by steady pick-up in inflation from 2 percent in

1967 to 95 percent in 1995. While we appreciate though that the current success in bringing down inflation to single digit and sustaining it there, we know that in other economies, these trends and target is around 2 percent and that we need to aim for that in the medium to long term. Currently, our medium-term objective is to get our inflation to 5 percent target by 2021.

With regard to the exchange rate, as you all know, the Malawi Kwacha attained its current equilibrium in

August 2016. Since then, it has generally remained stable. However, in the second quarter of 2019, we experienced a slight pick-up as a result of demand and supply dynamics during elections. The trend has since been re-established and re-restored and we expect it to continue.

Regarding interest rates, due to an improved macroeconomic outlook, the policy rate has been revised downwards by about 1,050 basis points from 24.0 percent in 2017 to the current 13.5 percent, with 350 basis points cuts effected in the first two MPC meetings of 2019. At the current level, the policy rate has established a new downward trend compared to a gradual pickup of 1964 to 1995 when the policy rate had gone up from 5 percent in 1964 to 50 percent in 1995.

Consistent with the decline in policy rates, base lending rates for Commercial Banks have also followed suit. At 13.9 percent, base lending rates are the lowest since 1980s and they have come down from an all-time peak of 56.2 in 2001. This is also a new norm compared to the period 1964 to 1999 when base lending rates had risen from 9 percent in 1964 to 53.4 percent in 1999. Going forward, with medium term inflation objective of 5 percent by 2021, we wish to bring down the policy rate to 11 percent and at that level, base lending rates will also follow. I must also report that to improve the transmission of monetary policy further, the Reserve Bank of Malawi in conjunction with the Bankers Association of Malawi, has introduced the Reference Interest Rate. The Reference Interest Rate is a weighted average of the Lombard rate, the Interbank rate (IBR), the 91-day Treasury bill rate, and the Savings rate and at the moment, the weights are 64.8 percent, 25.0 percent, 10.0 percent and 0.2 percent, respectively. The Reference Rate will come into effect on 3rd September 2019 and will be the new base lending rate for Commercial Banks.

Mr. President, the pick-up in economy, coupled with the aforementioned decline in interest rates has resulted in the rebound of private sector credit. I am pleased to report that Real Private Sector Credit Growth is now positive and was recorded at 10.9 percent in July 2019, after mostly being negative since 2012. In nominal terms, the outstanding stock of credit to the private sector was recorded at K531.0 billion in July 2019. Compared to the 55 years of our independence, one would argue that private sector credit is re-establishing its trend it enjoyed between 1964 and 1983 and 2004 to 2011. We will need to stay this course for some years to see businesses expanding, jobs created, more output realised and more wealth created which will reduce poverty.

With respect to public debt, which currently stands at 62 percent of GDP is a substantial pick up from the trough of 30 percent in 2004 at HIPC, and a much more improvement from the gradual pick-up in public debt from 50 percent in 1970 to a peak of 180 percent in 1995. At 33 percent, Domestic Debt is outside the debt sustainability threshold of 20 percent while foreign debt is within the debt sustainability threshold of 30 percent, at 27.9 percent. We will therefore need to do more to bring down domestic debt to sustainable levels in the coming months and years.

Turning of the financial system, Ladies and Gentlemen, our prudential analysis reveals that the Malawi financial system continues to exude strength and resilience. In the Banking sector, whereas our main preoccupation in 2017 was to address capital issues which we successfully dealt with, our main preoccupation in 2018 and 2019 was to deal with non-performing loans (NPL's). I am absolutely delighted that since June this year, our NPL ratios have reverted back to their prudentially regulated levels of below 5 percent as they are now at 4.5 percent as at end July 2019.

This is quite commendable and is the first time since 2012 that our NPL's have dropped to levels below the minimum regulatory requirements. The banking sector is now well capitalized with capital ratios above regulatory benchmarks. Core and total capital ratios stand at 16.4 percent and 20.4 percent and are above the regulatory minimum benchmarks of 10.0 and 15.0 percent, respectively.

Furthermore, the sector remains liquid as evidenced by a liquidity ratio of 59.1 percent, which is above the regulatory benchmark of 25.0 percent. What this means is that we now have a Banking System which is well capitalized, with low NPL ratios, proper liquidity conditions and profitable. This is extremely important for the well-being of our economy. As the saying goes that the health of an economic system is measured by the health of its financial system. Moving forward, we wish to see the financial system seriously investing in the growth of the economy so that we all benefit from the growth of our economy, hence the support of the theme of the Conference, building synergies with the private sector. Similar successes and achievements can also be made of all other sub sectors of the financial system in particular, the insurance, pensions, stock market, microfinance and others.

To strengthen the legal and regulatory environment of our financial system, **Distinguished Delegates, Ladies and Gentlemen,** let me update you on some of the steps the Reserve Bank of Malawi has recently undertaken:

(i) We have issued a Development Bank Licence to NBM Development Bank. The Development Bank will focus on lending small and medium scale enterprises. The issuance of the licence follows the coming into effect of the development finance institutions regulatory framework in 2018;

(ii) We have drafted a Licensing Directive on Community Banks and the same has been submitted to stakeholders for comments. The policy rationale for formulating a regulatory framework for community banks is to promote financial inclusion and empowerment of local entrepreneurs;

(iii) In collaboration with relevant stakeholders, we have drafted a Mortgage Finance Bill, which is at an advanced stage. The Bill seeks to create a separate legislation and prudential requirements that explicitly promotes mortgage financing in Malawi. The Bill will provide for the licensing of mortgage finance institutions and also encourage existing financial institutions to participate in mortgage financing;

(iv) In order to enhance financial stability and confidence and protect smaller depositors, we have finalized the design and development of the Deposit Insurance Bill which is awaiting Cabinet approval;

(v) Considering that Cyber Security Risk is pervasive and an ever-expanding threat to the banking industry and may have adverse impact on financial stability when crystallised; we have finalised drafting of the Cyber Security Risk Management Guidelines for banks. The Guidelines seek to prescribe minimum requirements to be adhered to by banks as they manage cyber risks and are issued pursuant to Section 96 of Financial Services Act 2010. The draft Guidelines have been submitted to stakeholders for review;

(vi) With the aim of assessing quality of service delivery, we conducted a mystery surveillance of banking outlets in the Southern Region, to assess treatment accorded to financial consumers at the banking outlets including banking halls and auto teller machines; the extent of transparency and disclosure of information to customers; and overall compliance with market conduct. Results were quite satisfactory, although there is still room for improvement;

(vii) In a bid to have a robust Credit Reference Bureau regime that is pivotal to financial stability, we have finalised the review of Credit Reference Bureau (CRB) Regulations for the better carrying out of the CRB Act and its administration. In collaboration with the

International Finance Corporation (IFC), a member of the World Bank Group, and the country's two Credit Reference Bureaux, we conducted capacity building workshops on credit reporting awareness;

(viii) In terms of financial literacy, together with other key stakeholders, we continued to conduct and monitor financial literacy initiatives aimed at empowering the general public to make informed financial decisions.

With these remarks, which I regard to be long quite frankly, I wish to sincerely thank you all for your perseverance in listening in silence.

I thank you all for your kind attention.