Caleb M Fundanga: The history and experiences of the financial sector and regulatory framework in Zambia

Address by Dr Caleb M Fundanga, Governor of the Bank of Zambia, at the Co-operative Bank Capitalisation Consultative Forum "The history and experiences of the financial sector and regulatory framework in Zambia", Lusaka, 3 March 2011.

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- ***The Honourable Minister of Agriculture and Co-operatives, Hon Eustarkio Kazonga, M.P;***
- ***The Board Chairman of the Co-operative Bank Zambia Limited, Mr Mulilo Kabesha;***
- ***Members of the Diplomatic Corps;***
- ***Distinguished Invited Guests;***
- ***Ladies and Gentlemen***

It is with great pleasure and privilege to speak to you at this very important Consultative Forum. I have been requested to speak briefly on the history and some of the experiences of the financial sector in Zambia.

Ladies and Gentlemen, as you are aware, considerable developments have been recorded in the Zambia economy in general and the financial sector in particular, following the liberalization of the economy in the early 1990's. These developments include the proliferation of banks and non-bank financial institutions, which have necessitated the review of supervisory policies as well as the legal and regulatory frameworks in order re-align them to the liberalised environment.

A significant development relating to the Zambian financial sector was the decision to relocate the function of the Registrar of Banks and Financial Institutions to the Bank of Zambia from the Ministry of Finance and National Planning where it was previously located. This decision was taken in an effort to enhance regulatory oversight of banks and financial institutions starting from the licensing stage. Currently, all applicants have to be evaluated in line with relevant provisions of the Banking and Financial Services Act (BFSA) and international best practice such as the Basel Core Principles on Effective Banking Supervision. The intention is to ensure that only applicants who meet these stringent criteria enter the financial system in Zambia. This is crucial for fostering confidence and stability in the financial system.

Mr Chairman, you may be aware that in the early stages of the reforms, a number of commercial banks faced serious problems and were subsequently liquidated. The closures were in part a consequence of the reforms. The reforms also highlighted some weaknesses in corporate governance arrangements at most failed banks.

However, following improvements in the regulatory and supervisory frameworks, no bank closure has been recorded since 2002 and the banking sector has recorded significant growth. The growth in the sector can also be attributed to prudent fiscal and monetary policies aimed at achieving sustainable macroeconomic stability. This has been accomplished under a stable political environment and liberalised market conditions.

Furthermore, in 2002, the International Monetary Fund and the World Bank undertook a comprehensive assessment of the Zambian financial sector through the Financial Sector Assessment Program (FSAP). In response to the weaknesses noted in the FSAP, Cabinet approved the Financial Sector Development Plan (FSDP) covering the period 2004 – 2009. Apart from addressing the weaknesses identified in the FSAP, the FSDP sought to further strengthen the Zambian financial sector as well as to guide efforts for realizing the vision of a stable, sound and market based financial system that would support the efficient mobilisation and allocation of financial resources necessary for economic diversification and sustainable growth. To this end, the Bank of Zambia in conjunction with the Government has been undertaken reforms in the financial sector under the FSDP, which is now in the second phase.

Through the FSDP, the Bank of Zambia promoting competition among banks. Competition in the banking sector while desirable can have both negative and positive effects. In this regard, competition can be viewed in terms of being a public good which can significantly contribute towards access to better quality and cheaper financial services. The challenge, therefore, is to ensure that supervisory effort is adequately able to change and effectively respond to innovations and events in the financial system. It is expected that this would consequently promote confidence in the financial system which is necessary for insulating the economy from adverse internal and external shocks.

The Bank of Zambia has attempted to develop supervisory and regulatory approaches which answer to these challenges. For instance, Bank of Zambia has adopted a risk-based approach to supervision. This approach entails closer interaction with banks and allows early identification of risk as well as close monitoring of the nature and direction of risks as they emerge. This paradigm shift in supervisory approaches requires a permissive legal and regulatory framework.

Chairperson, currently, the legal and regulatory frameworks in Zambia comprise of the Banking and Financial Services Act, Chapter 387 of the Laws of Zambia; the Bank of Zambia Act, Chapter 360 of the Laws of Zambia; the Prohibition and Prevention of Money Laundering Act; the Bank of Zambia Anti-Money Laundering Directives; and the Bank of Zambia Corporate Governance Guidelines. In addition, the Bank of Zambia also issued Risk Management Guidelines to provide minimum standards to be observed by commercial banks in the area of risk management. The Bank has continued to revise these frameworks on an on-going basis to ensure that they address current challenges in the sector. However, the major challenge in this regard remains the extent and speed at which changes to these regulatory frameworks can be made in order to improve policy responsiveness.

Ladies and Gentlemen, the Bank of Zambia has always strived to strike a balance between having a robust supervisory and regulatory framework and the need to promote investments in the sector. The entry of new players in the market is testimony of the confident that Bank's supervisory oversight of the sector has instilled in both the general and investing public. We remain committed to executing our mandate and in ensuring that the financial system is properly regulated in order for economic agents to undertake their activities in a safe and sound environment.

Distinguished guests, we note that financial intermediation is still very low in our economy and as such a lot of work still remains in this area. The Bank of Zambia encourages and supports market initiatives aimed at the financially excluded in order to achieve the objective on financial inclusion. It is therefore my view that promoting the initiative of reviving the operations of a Co-operative bank is important. As you are all aware, in a co-operative bank, shareholders and customers are the same group of people whose dominant purpose is to provide customer value by offering tailored-made products and services cost-effectively and close to home.

Through their membership structures, Co-operatives are known to have a firm foothold in local communities and a sound knowledge of people's overall financial situation. This enables accurate decision making and risk control which in turn, fosters regional development and social cohesion. Co-operative banks are also known for pioneering sustainable development and corporate social responsibility, through continuous engagement to fight unemployment and eradicate social exclusion. In fact, if properly managed, Co-operative banks can make the financial system more competitive. This can be done through proper organization, meaningful investment in technology and proper pricing of products.

Lastly, let me remind all of us here that like any player seeking entry in the market, the co-operative bank which we wish to revive will be bound by the same legal, fiscal and prudential regulations as other players. It is therefore important for those who will be entrusted to manage the affairs of the institution to prudently provide leadership that seeks to promote the well being of all stakeholders. As such the aspect of good corporate governance practices in the banking and financial services sector cannot be over-emphasized.

I thank you all for your attention!