

Caleb M Fundanga: Winning with leasing

Speech by Dr Caleb M Fundanga, Governor of the Bank of Zambia, at the “Winning with Leasing” seminar, Lusaka, 21-23 February 2007.

* * *

- Mr Chairman
- Chief Executives and representatives of Banks and Leasing Companies
- Representatives of businesses organizations;
- Distinguished ladies and gentlemen

Let me first express my sincere gratitude for being invited to officiate at this important regional Leasing Seminar. It is my hope that this interaction will give us a better understanding and appreciation of the important contributions that the Leasing sector has made and continues to make to the economic growth of this country. As the title of the seminar “Winning with Leasing” suggests, it is only by winning in all our efforts that we will provide meaningful contributions to the development of this country.

Mr Chairman, before I talk about your role in the growth of the economy, allow me to first give a brief account of the macroeconomic developments in Zambia in the recent past. I know that many of you have been following the economic developments in the country. The economy has performed relatively well in recent years, with positive real Gross Domestic Product (GDP) growth and inflation as well as interest rates coming down.

During the period 2001-2005, growth in real GDP averaged around 5% per annum. More recently, in 2006, it is estimated that the economy grew by close to 6%, marking the eighth consecutive year of positive real growth in output. This positive economic growth has been broad-based, extending beyond the recovery of the mining sector and has withstood adverse shocks, such as, droughts and increases in oil prices. For example in 2006, real GDP growth was largely driven by the mining, construction, and transport sectors. Other sectors that registered positive growth were agriculture, tourism, manufacturing, wholesale and retail trade and the services sectors.

Ladies and Gentlemen, bringing inflation down to single digits has been Government’s goal for a long time. Therefore, it is pleasing to note that last year inflation fell to its lowest level in 30 years. At end December 2006, the annual rate of inflation had fallen to 8.2 % compared to the annual target of 10% and the 15.9% outturn in 2005. In January 2007, it remained in single digit level of 9.8%.

These unprecedented developments in inflation have been due to continued implementation of prudent monetary and fiscal policies, coupled with increased food supply.

In line with lower inflation and yields on Government securities, the average commercial banks’ lending rate declined further to around 28 % in December 2006 from about 34 % in December 2005. In January 2007, it slightly declined to about 27 %.

Mr Chairman, clearly, there is a need for commercial banks to do more to reduce lending rates in order to influence a substantial expansion of private sector credit. Lower lending rates will contribute to the reduction in the cost of doing business in Zambia. The current environment of low inflation and relatively stable exchange rate offer a good opportunity for lowering commercial banks lending interest rates.

Distinguished Guests, Ladies and Gentlemen, Zambia’s external position continues to score remarkable improvements as reflected in the build-up of gross international reserves to 2 months of import cover in 2006 from 1.6 months of import cover in 2005. Furthermore, the preliminary assessment is that Zambia’s surplus trade balance increased to US \$1,176.0 million in 2006 from a trade surplus of US \$10 million in 2005. Similarly, the current account deficit as a percentage of GDP, excluding grants, reduced from 11.8% in 2005 to 2.3% in 2006. This improvement has been due to increased export receipts arising from record high copper prices and increased export volumes.

In addition, the historic debt relief received in 2006 and the increased budget support from our co-operating partners has helped to strengthen the external position. Preliminary information indicates that the country’s external debt position stood at US \$635 million as at end of December 2006 , a reduction of about 87% from the end-2005 debt stock of US \$4.5 billion.

In 2006, the foreign exchange market was characterized by general depreciation of the Kwacha against major currencies. In order to moderate exchange rate volatility and maintain stability in the external value of the Kwacha, the Bank of Zambia intervened by way of purchasing and selling foreign exchange.

In the banking sector, there have been no bank failures in the recent past, reflecting stability in the financial sector

Mr Chairman, the Government has shown commitment to continuing the economic reform programme. To this end, measures are being taken to ensure that the macroeconomic gains attained so far will be consolidated in 2007. Accordingly, Government is targeting Real GDP growth of 7.0% and inflation of 5.0%. Pursuit of these objectives is within the context of the long-term development objectives well articulated in the national long term vision, 2030. Part of this vision is enshrined in the Fifth National Development Plan (FNDP) from 2006-2010 whose broad macroeconomic objectives for the plan period are as follows:

- to accelerate pro-poor economic growth;
- to reduce and stabilise inflation; and
- to sustain a viable balance of payments and external and domestic debt position.

At this juncture, **Ladies and Gentlemen**, allow me to share with you my understanding of the role of the leasing sector in economic growth. Clearly, the remarkable economic gains that I have outlined above would not have been possible without the leasing sector's contribution. Leasing companies are specialized lenders that provide asset-backed finance. The assets financed by leasing companies include plant and machinery and motor vehicles. Traditionally, these assets have excluded chattels or personal moveable assets.

Though the leasing sector has existed in Zambia since independence, the formal supervision of the leasing sector by the Bank of Zambia only began in the 1990s. It is pleasing to note that the leasing sector has a bright future in Zambia as evidenced by its growth. Since the liberalisation of Zambia's financial sector, the contribution to private sector credit of leasing companies has increased. In the period December 2001 to December 2006, total leases increased from K67,161 million to K206,972 million, representing an average annual growth rate of about 25.2 %. At the same time, the performance of the leasing sector was satisfactory as on average, leasing companies maintained adequate capital and reserves relative to their risk profiles and the sector has been consistently profitable.

Notwithstanding this improved performance of the leasing sector, I am aware of a number of constraints the financial sector in general is facing, including the low financial intermediation, limited access to financial services for the rural population and low-to-middle income earners, high cost of funds, lack of product diversity and underdeveloped money and capital markets. To redress these impediments to economic growth and as an integral part of the pro-poor growth strategy, the Government's objective is to enhance financial intermediation and improve access to financial services both in urban and rural areas. To this end, a five year Financial Sector Development Plan (FSDP) was prepared in 2004. This Plan aims at promoting the development of a financial system that is stable, sound and market-based to support efficient resource mobilization, which is necessary for economic diversification, sustainable growth and poverty reduction. Currently, the key recommendations of the FSDP are under implementation.

Mr Chairman, learning from others, some of the obstacles facing the leasing companies, include inability to attract funding and lack of adequate leasing expertise, can be overcome through formation of synergies and partnership with other industry players. I understand in the USA, for example, over 70% of leases are actually written through lease intermediary companies or brokers, who use their specialised skills to structure lease transactions in the best way possible for the benefit of both the lessee and the lease underwriter. Lease syndications and funding partnerships with bigger players should also be encouraged as these help to spread risk and reduce pressures on balance sheets of individual leasing companies.

Ladies and Gentlemen, you will agree with me that there is vast untapped potential of leasing activities in this country. There is need to develop this line of business further. A developed leasing sector is characterized by a diverse range of financial services that include factoring and trade finance, term lending, corporate finance and investment advisory services, and corporate restructuring, treasury management as well as traditional leasing activities. But this is not the case in Zambia at

present. Currently, the leasing sector is restricted primarily to the traditional leasing activities. This seminar has thus come at the right time, as the lessons learnt are vital to complement the Government's efforts not only to develop the leasing sector, but the financial sector as a whole. I am particularly delighted that this seminar will address the need to "match products to user needs". This is indeed key to the success of any service oriented industry and therefore inevitable in meeting the needs of a growing economy such as ours. Without overemphasizing this point, I would like to implore you to ensure that you develop products suitable to your clients as a good and useful product is only one that meets the needs of the market.

As I have already noted, on its part the Government is committed to resolving the various constraints identified in the country's financial system through implementation of the FSDP and related initiatives. Key among the strategies includes the development of appropriate regulations and improving the capital adequacy base for the leasing and finance companies. Adequate capitalization of commercial banks and financial institutions is important if there is to be stability in the financial sector. It is for this reason that the Bank of Zambia, effective January 2007, increased the minimum paid-up capital for commercial banks from K2 billion to K12 billion. In the same vein, the start-up capital for the deposit taking leasing institutions was increased to K1.5 billion from K250 million. I wish to urge all leasing companies to make sure that they take steps to meet the required minimum capital.

Let me conclude by paying tribute to the organisers of this seminar, Sapitwa Finance. Mr Sudhir Amembal the principal resource person is a renowned authority in leasing, having undertaken various leasing consultancies and training worldwide and being an author of various leasing publications and books. I am very grateful that he has found time to come to Zambia and share his vast experiences with us.

I am glad to note that this seminar has brought together key players in the economy and other stakeholders.

I thank you for your attention.