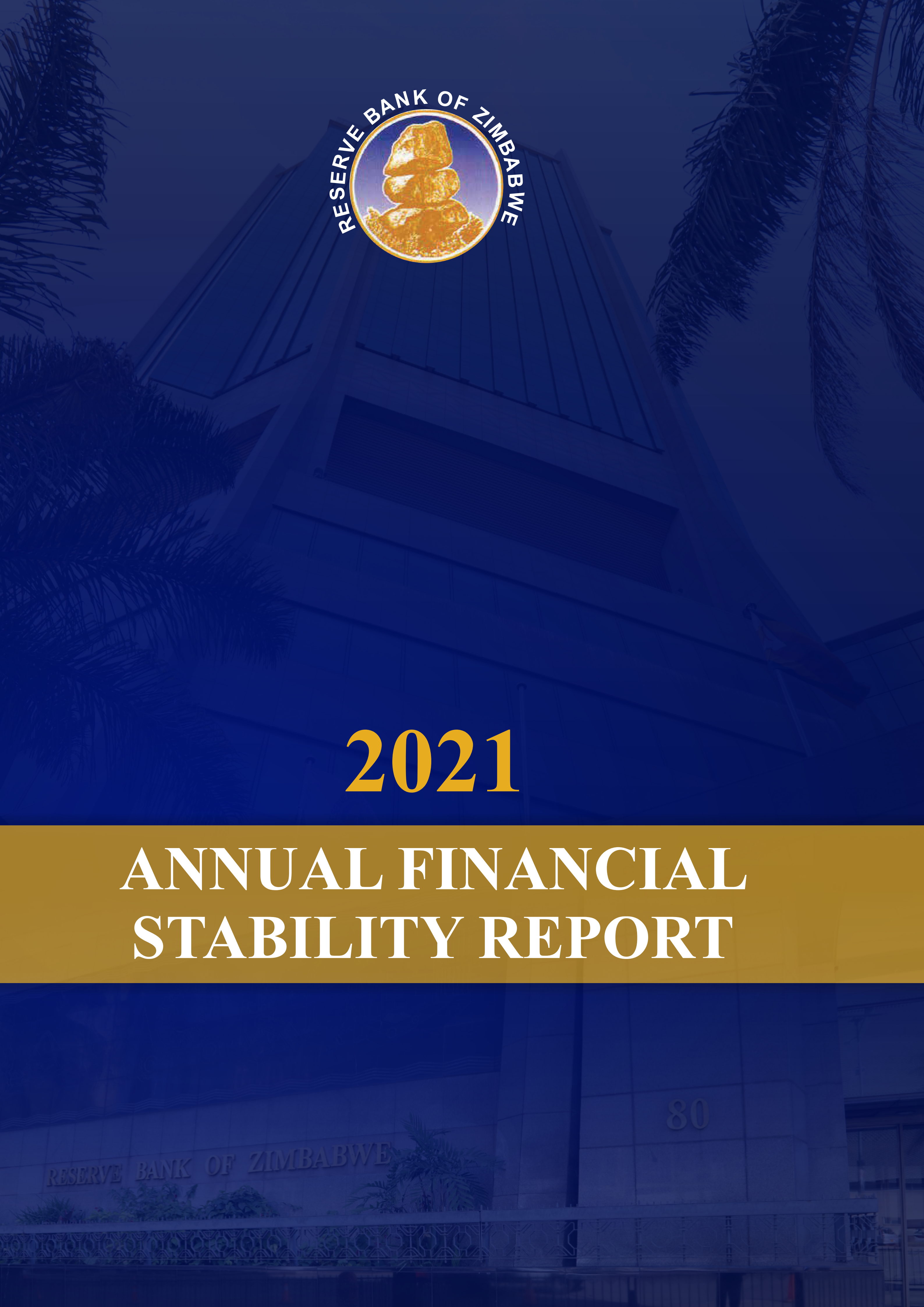
RESERVE BANK OF ZIMBABWE



2021

ANNUAL FINANCIAL STABILITY REPORT

Table of Contents

List of Tables

List of Figures

Acronyms

AML	Anti-Money Laundering
ALSI	All Share Index
ATP	Alternative Trading Platform
AUC	Assets Under Custody
BIC	Bank Identifier Code
CFT	Combating the financing of terrorism
CAR	Capital Adequacy Ratios
CBDC	Central Bank Digital Currency
CBI	Contributory Financial Institutions
CDD	Customer Due Diligence
CSCF	Customer Security Controls Framework
DPC	Deposit Protection Corporation
D-SIB	Domestic Systemically Important Bank
DTMFI	Deposit-taking Microfinance Institutions
EMDE	Emerging Markets and Developing Economies
EWMA	Exponentially Weighted Moving Average
FATF	Financial Action Task Force
FCA	Foreign Currency Account
FINSEC	Financial Securities Exchange
FMIs	Financial Market Infrastructures
FUM	Funds Under Management
FSI	Financial Soundness Indicators
GDP	Real Gross Domestic Product
IMF	International Monetary Fund
IPEC	Insurance and Pensions Commission
MDFSC	Multidisciplinary Financial Stability Committee
NPL	Nonperforming Loan
OFAC	Office of Foreign Assets Control
PMFI	Principles for Financial Market Infrastructures

RBZ	Reserve Bank of Zimbabwe
RTGS	Real Time Gross Settlement System
SADC	Southern African Development Community
SECZ	Securities and Exchange Commission of Zimbabwe
SWIFT	Society for Worldwide Interbank Financial Telecommunication
TCIB	Transactions Cleared on an Immediate Basis
ZICARP	Zimbabwe Integrated Capital and Risk Programme
ZSE	Zimbabwe Stock Exchange

Purpose of the Report

The Annual Financial Stability Report provides an overall assessment of financial stability in 2021 and also provides an analysis of potential risks to financial stability. The report also serves to promote the mitigation of systemic risks by stimulating market participants' evaluation of the wide range of risk factors in the financial sector in the context of developments in domestic, regional and global environments.

This report is a product of collaborative efforts by the Multidisciplinary Financial Stability Committee, constituted by the Reserve Bank of Zimbabwe, Insurance & Pensions Commission of Zimbabwe, Securities & Exchange Commission of Zimbabwe, and the Deposit Protection Corporation. The report is published annually and selected developments up to the time of finalisation of the report that have an impact on financial stability are incorporated.

Multidisciplinary Financial Stability Committee

GOVERNOR'S FOREWORD

1. The global financial sector has continued to register resilience to the ongoing Covid-19 pandemic. Expansionary policy measures that were implemented at the beginning of 2020 supported the global economy to contain global financial stability risks during the year ended 31 December 2021.
2. In 2021, a number of Central banks reversed the accommodative monetary policies by increasing interest rates in order to restrain the rising inflationary pressures. Under these circumstances, global economic activity is estimated to have increased by 6.1% in 2021 and is projected to moderate to 3.6% in 2022 (World Economic Outlook, April 2022).
3. Sub-Saharan Africa is estimated to have grown by 4.5% in 2021 and will likely moderate to 3.8% in 2022 in line with the rest of the global economy.
4. Despite the potential risks arising from the Covid-19 pandemic and external socio-economic factors, the Zimbabwean banking sector remained resilient as reflected by adequate capitalisation, liquidity buffers and strong asset quality.
5. Inflationary pressures in the review period were contained through an adjustment in the overnight accommodation rate to 60% by the end of the year. The Bank also revised downwards the quarterly reserve money growth target for 2021 from 22.5% during the first two quarters of 2021 to 20% in the third quarter, and further down to 10% in the fourth quarter of the year.
6. The inflation containment measures during the year 2021 promoted stability in the operating environment and financial stability in the country, which is key for the banking sector to support the productive sectors of the economy. The economy is estimated to have grown by 7.8% in 2021.
7. The insurance and pensions sector remained largely sound and stable during the period under review despite the dynamic operating environment, characterised by increasing Covid-19 cases, inflation pressures and outstanding compensation payments to insurance policy holders emanating from the Justice Smith Commission of Inquiry recommendations of 2015.
8. The capital market sector remained stable in 2021 and continued to play its role as a source of long-term funding and investment. The economic stabilisation

measures initiatives during the year positively impacted on investment returns for both Securities Market Intermediaries (SMIs) and investors.

9. The geo-political conflict in Ukraine has, however, generated downside risks to the global economic outlook. The supply chain disruptions in the global energy sector and associated rise in oil prices have resulted in a knock-on effect on inflation, especially in oil importing countries such as Zimbabwe. Such developments raise uncertainties which will provide a real stress test to the resilience of the financial sector in the outlook period.
10. Increased adoption of digital financial services on the back of the ongoing technological revolution has amplified operational and strategic risks while generating new risks, notably cyber risk. Heightened cyber risk underscore the need to ensure operational resiliency within the financial sector.
11. In line with regional and international developments, the Bank has created a conducive environment that promotes responsible innovation while minimising potential risks to financial stability. A Fintech Regulatory Sandbox (the Sandbox) was launched in March 2021.
12. The Bank is continuing to enhance financial infrastructure in order to promote inclusive access to credit while strengthening credit risk management, with positive impact on financial stability.
13. Financial sector regulatory authorities will continue to monitor and implement timely policy interventions to ensure that financial stability is maintained, and this is an imperative for attaining and sustaining economic growth in the outlook period.
14. Finally, I would like to thank the Ministry of Finance and Economic Development, fellow financial sector regulators and other key stakeholders for their unwavering efforts in promoting financial stability.

Dr. J.P. Mangudya
Governor

1. RISKS TO FINANCIAL STABILITY ARISING FROM THE MACROECONOMIC ENVIRONMENT

Global Economic Environment

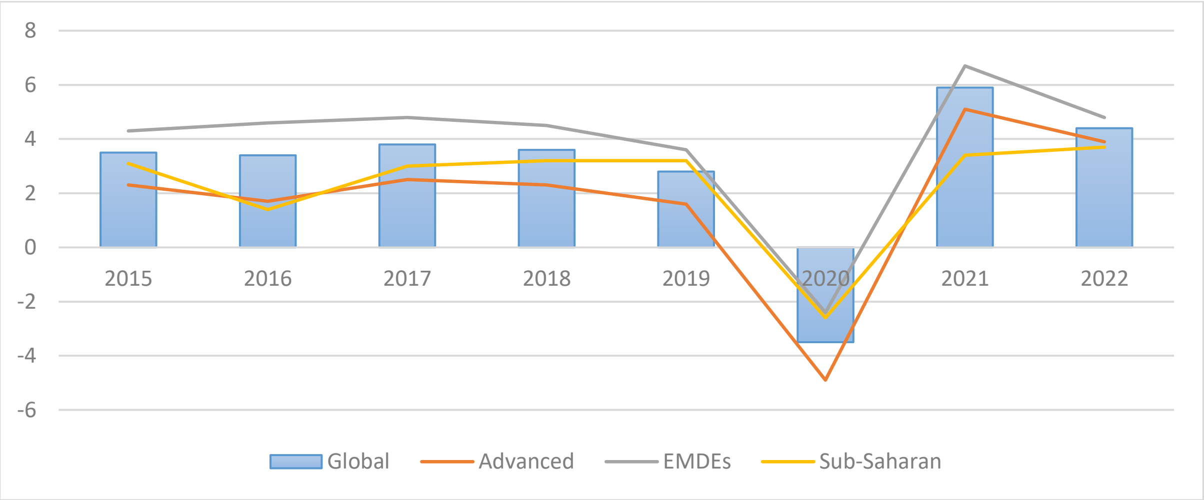
1.1 The reduction in interest rates in 2020 eased financial conditions and supported the global economy. This contributed to the estimated global economy growth of 6.1% in 2021. Growth is, however, expected to moderate to 3.6% in 2022. The forecasted slowdown is partly attributed to the geo-political tension in Ukraine and rising global inflation.

1.2 Economic contraction in both Ukraine, Russia and the rest of Europe is expected in 2022 due to the energy supply chain disruptions arising from the geo-political tension and the lingering effects of covid-19. The knock-on effect of the geo-political tensions is expected to negatively impact other countries through trade, and marginally through financial interlinkages.

1.3 In 2021, in an effort to contain inflationary pressures and risks to financial stability arising therefrom, advanced economies' central banks tightened monetary policies.

1.4 The policy changes, coupled with supply chain disruptions, have contributed to lower growth forecasts in both the developed and developing countries. In the euro area, prolonged supply constraints and the geo-political conflict in Ukraine are expected to reduce economic growth from 5.3% in 2021 to 2.8% in 2022.

Figure 1: Global Economic Growth (%)



Source: World Economic Outlook (January 2022)

1.5 In China, disruption in the housing sector largely due to some of the largest property developers accumulating debt amidst falling sales, contributed to the economy's lower than anticipated growth during the review period. With a strict zero-Covid-19 strategy leading to recurrent mobility restrictions and deteriorating prospects for construction sector employment, private consumption is projected to be lower than anticipated.

1.6 The likely impact of these developments on the world's largest economy, has potential negative implications for trading partners' prospects.

Elevated Inflation Expectations

1.7 Inflation is expected to remain elevated in the near term, averaging 3.9% in advanced economies and 5.9% in emerging market and developing economies in 2022. The geo-political conflict in Ukraine has led to a rapid increase in fuel prices. The potential spill over effects of rising fuel prices will increase local inflationary pressures.

1.8 Despite rapid and effective rollout of vaccination programs in most advanced economies, vaccination programs in many emerging market and developing economies are slow. This sluggish progress has been a contributing factor weighing on the recovery prospects in under-vaccinated countries.

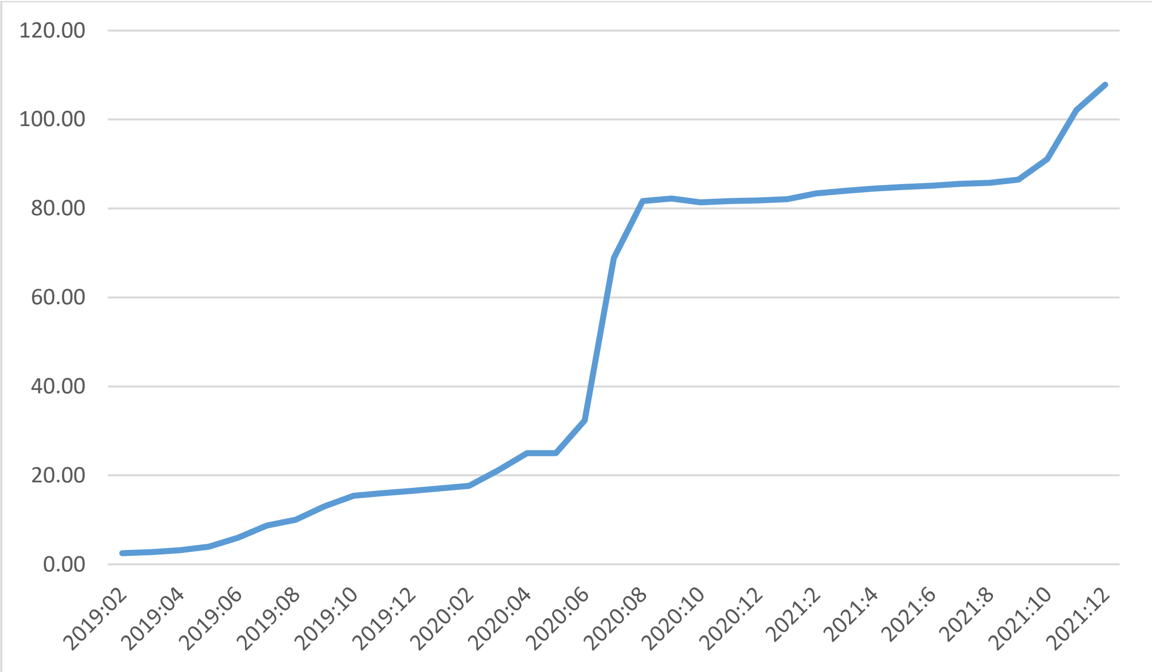
Domestic Macroeconomic Environment

1.9 The local economy is estimated to have grown by 7.8%[1] in 2021 and is expected to grow by 5.5% in 2022. The significant growth was mainly spurred by fiscal relief measures that supported agriculture, industry and other sectors of the economy in a bid to mitigate downside effects of the Covid-19 pandemic.

1.10 The local currency depreciated from an average of ZW$82.07/US$1 in January 2021 to an average of ZW$107.83/US$1 in December 2021. The monetary targeting framework, aimed at restricting money supply and inflation is expected to reduce risks to financial stability arising from exchange rate volatility in the absence of significant negative impact from exogenous factors.

[1] 2022 National Budget

Figure 2 : Exchange Rate Developments (ZW$/US$)

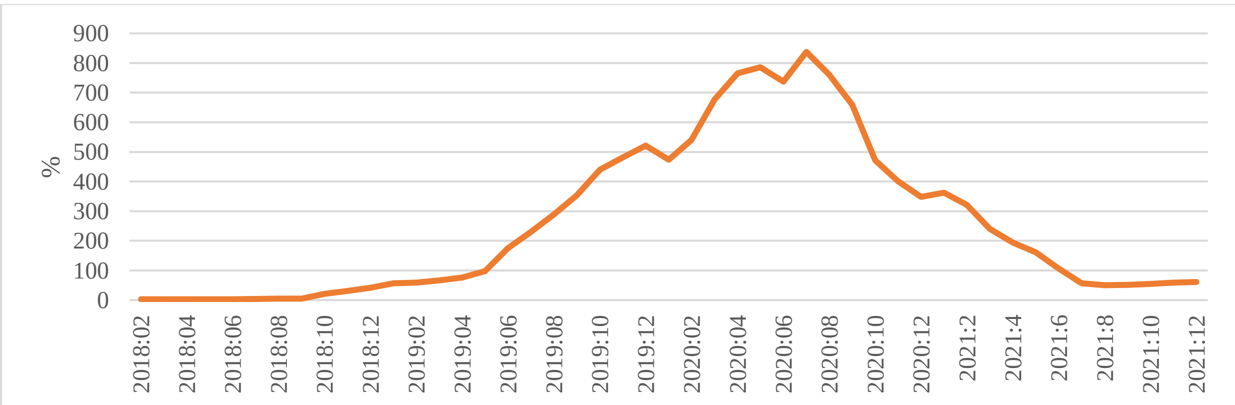


Source: RBZ (2022)

Inflation Risk

1.11 Annual inflation was on a downward path during the greater part of the review period to end at 60.74% in December 2021 compared to 379.26% recorded at the end of 2020. This was mainly a result of fiscal consolidation and the implementation of the monetary targeting framework by the central bank. Transitory shocks arising from increases in fuel prices due to the geo-political conflict in Ukraine will contribute to inflation dynamics in the local economy in the outlook period.

Figure 3: Annual Inflation (%)



Source: ZIMSTAT (2022)

Monetary Developments

1.12 The monetary targeting framework has ensured that reserve money growth remained within the set targets and, therefore, reduced pressure on the exchange rate, supporting macroeconomic and financial stability.

1.13 The quarter on quarter reserve money growth target for 2021 was progressively reduced from 22.5% during the first two quarters of 2021 to 20% in the third quarter, and further down to 10% in the fourth quarter of the year. The downward revision was a response to resurgence of inflationary and exchange rate pressures in the economy.

1.14 These revisions in the reserve money growth target reduced reserve money to ZW$25.49 billion at the end of December 2021, compared to the fourth quarter target of ZW$28.9 billion.

1.15 In an effort to curb inflationary speculative borrowing, the Bank increased the overnight accommodation rate from 35% at the beginning of 2021, to 60% by the end of the year.

Summary of Major Risks to Financial Stability

1.16 The table below shows potential risks to financial stability and possible mitigants.

Table 1: Risks to Financial Stability

Type of Risk	Likely Impact	Risk Mitigants	Residual Risk	Direction of Risk
Macroeconomic Risk emanating from • Inflationary pressures. • Low aggregate demand. • Weak Global economic growth. • Inflation in western economies	**High** • Disruption in business operations through Covid-19 induced lockdowns • Decreased trade amongst nations	• Continued vaccination to achieve herd immunity. • Restrict reserve money growth to 5% • Increased local production	**Moderate**	**Stable**
Foreign Exchange Risk Emanating from • Significant disparity between official & parallel market rates • Increasing demand for forex as astore of value	**High** • Inflationary pressure	• Restrict reserve money growth to 5% • Raise cost of speculative borrowing • Improve foreign currency inflows through exports, remittances etc.	**Moderate**	**Stable**
Covid-19 Pandemic (Health Risk)	**High** • Supply chain disruptions • Reallocation of resources from development programmes • Disruption of economic activities. • Disruptions to loan repayments • Increased Government allocation of funds to vulnerable groups (Increased Government expenditure)	• Promotion of use of digital platforms by banking institutions • Encouragement of telecommuting at work places. • Pursuit of herd immunity via vaccination of at least 60% of the population. • Increased uptake of vaccination by population.	**Moderate**	**Stable**

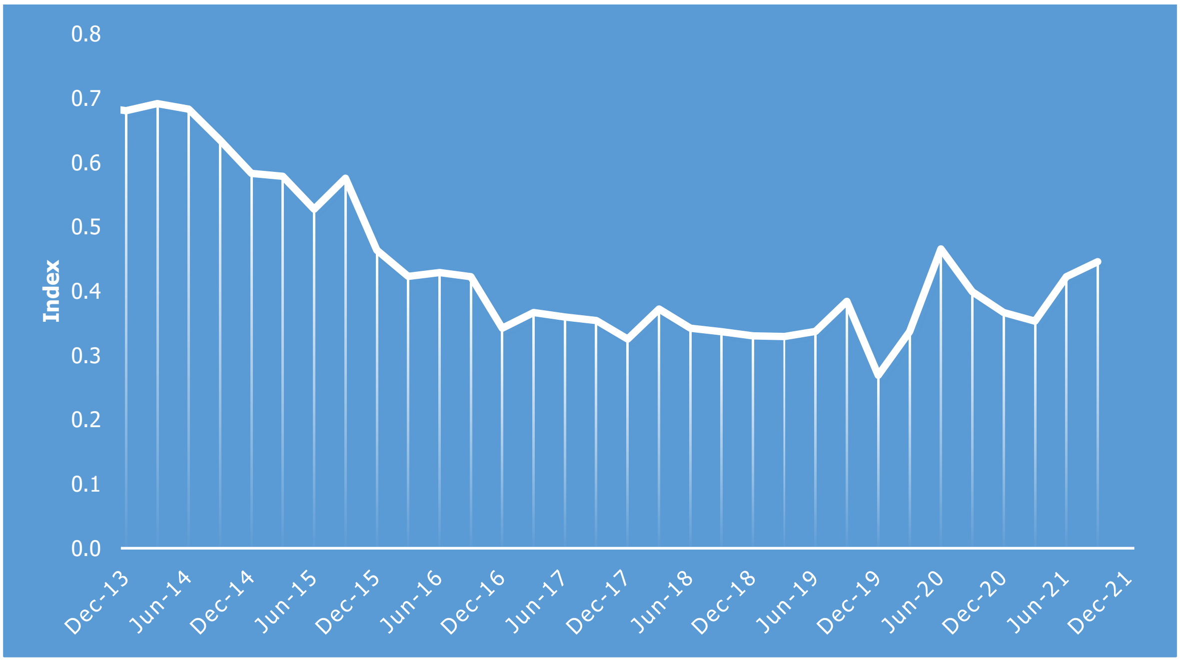
Inflation Risk emanating from • Preference for use of USD. • ZW$ prices indexed to USD at parallel market rates • High service charges, utility and energy prices	**High** • Decrease in disposable income & consumer purchasing power. • Increases in prices of goods and services. • Increasing cost of borrowing	• Restriction of money supply growth to below 10% per quarter. • Allocation of FX on the auction system to maintain price and monetary stability. • Government not borrowing from the RBZ. • SDRs allocated by IMF for productive purposes • Increase in bank policy rate	**High**	**Stable**
Climate risks As a result of • Climate Change & Global Warming • Cyclones, earthquakes, Hurricanes & droughts	**Moderate** • Destroys infrastructure and businesses, including Financial Institutions • Hazards raise credit, operational & sustainability risks to financial institutions. • Strain fiscal space as Government attempts to fund Civil Protection Units. • Lowers production in agriculture	• Promotion of Green economy • Promotion of Sustainable banking practices, spearheaded by Central Bank • Decentralization of Civil Disaster Response units	Moderate	increasing
Operational Risk from • Increasing digitisation • Impact of telecommuting on risk managemen**t** • Power supply bottlenecks • ICT failures. • High cost of living against depressed wages	**Moderate** • Disruptions to business processes • Increased downtime in digital platforms • Increased bank robberies & cash heists • People Risks in form of frauds	• Telecommuting policies and procedures. • Importation of power and installation of solar based power systems • Continuous review of wages and salaries and offering of non-financial benefits.	**Moderate**	**Stable**
Cyber Risk from • Accelerated Digitisation for financial services.	**High** • Digital platforms prone to cyber-crimes e.g. card cloning, pin hacking, & sophisticated viruses • Confidential Data snooping by hackers • Costly upgrade of Systems	• Promulgation of Cyber Security & Data Protection Act • Upgrade of cyber security systems • Public or client education campaigns • Client electronic notifications or messaging warning of cyber-attacks.	**High**	**Stable**
Sovereign Risk as a result of • **Legacy Debt Arrears** • **Western Political & economic sanctions.**	**High** • Lack of multilateral support from Global Financial Institutions. • High cost of funds from offshore lenders	• Payment of external debt obligations. • International reengagement efforts by Government • New sources of development finance e.g. China, AfDB • Financing from domestic resources	**High**	**Stable**

2. BANKING SECTOR RISKS AND RESILIENCE

Overview

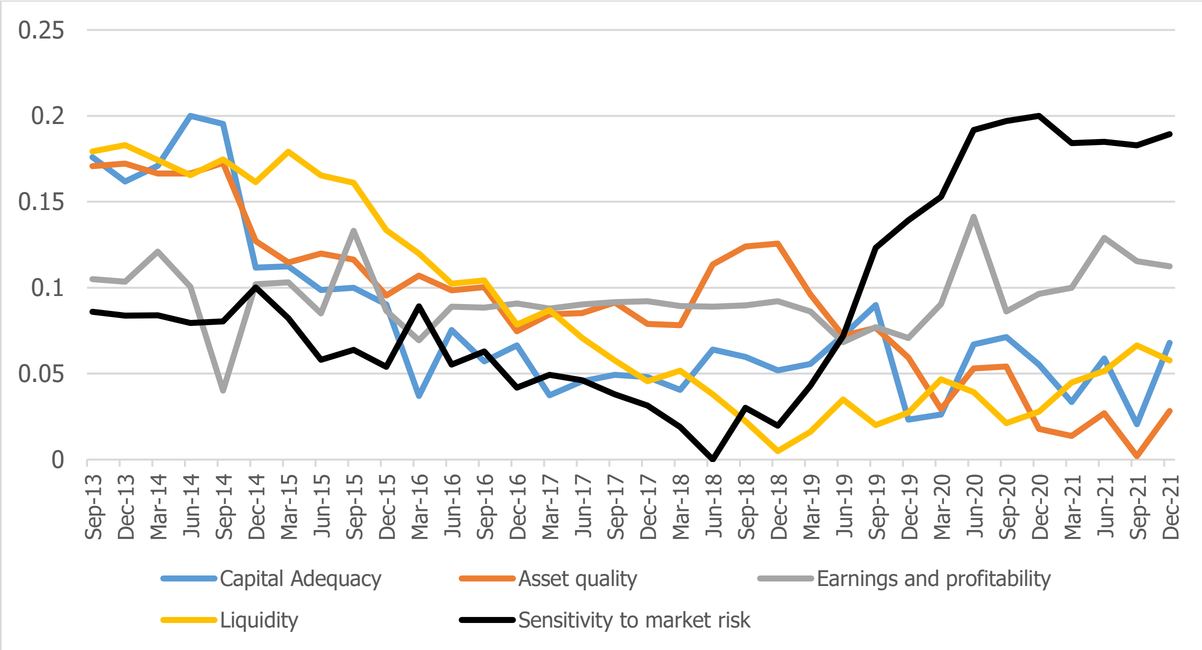
2.1 The stabilisation of the macroeconomic environment has provided a conducive environment for the financial sector to continue supporting the growth of the economy. Banking institutions generally had sufficient capital and liquidity buffers before the onset of the Covid-19 pandemic which helped to cushion the banking sector from the pandemic's impact as evidenced by the solvency metrics and other financial sector indicators.

Figure 4: Banking Sector Soundness Index[2]



[2] See Box 1 for the derivation of the index.

Figure 5: Banking Sector Soundness Index: Sub-Indices



Source: RBZ (2022)

2.2 All five Domestic Systemically Important Banks (DSIBs) were well capitalised throughout 2021, with their capital adequacy ratios averaging 22.88% at the end of 2021. Aggregate net income for the five DSIBs was ZW$33.63 billion in 2021. DSIBs held 66% of the total banking sector assets and stress test results showed that all the DSIBs were resilient to unforeseen shocks.

2.3 The figure above shows that asset quality remained satisfactory while the sector remained adequately capitalised.

BOX 1: BANKING SECTOR SOUNDNESS INDEX (BSI)

In the aftermath of the Global Financial Crisis of 2007-2009, which provided ample evidence of the consequences of financial instability, policymakers and academics have devoted resources to develop composite measures of financial stability and bank soundness. The aim of these measures is to enable informed assessment of financial stability and banking system soundness, and adoption of appropriate policies to mitigate the risks. In this regard, the Reserve Bank constructed a Banking Sector Soundness Index (BSI) as a single measure of banking system soundness which gives an overall picture of the state of the banking system. The BSI is mainly based on five CAMELS components, namely:

1. Capital Adequacy;
2. Asset Quality;
3. Earnings and Profitability;
4. Liquidity; and
5. Sensitivity to Market risk.

The data used in the BSI for Zimbabwe is compiled from Financial Soundness Indicators (FSIs) that are available on a quarterly basis. These are then transformed using empirical normalization to fit the data within the range of 0 to 1. The following equation is used to normalize the ratios:

$$I_i = \frac{X_i - X_{min}}{X_{max} - X_{min}}$$

Where:

I_i is the sub-index value at point i

X_i is each data point i

X_{Min} is the minima among all the data points

X_{Max} is the maxima among all the data points

$X_{i,\,0\text{ to }1}$ is the data point i normalized between 0 and 1

After the normalization of each ratio, a sub-index is computed using a simple average of the normalized ratios. The formula for this step is given below, using the capital adequacy sub-index as an example:

$$\overline{X}_{tc} = \frac{\sum_{i=1}^{n} X_{tci}}{n}$$

The overall BSI is then computed as the sum of the equally weighted sub-indices and calculated using the following equation:

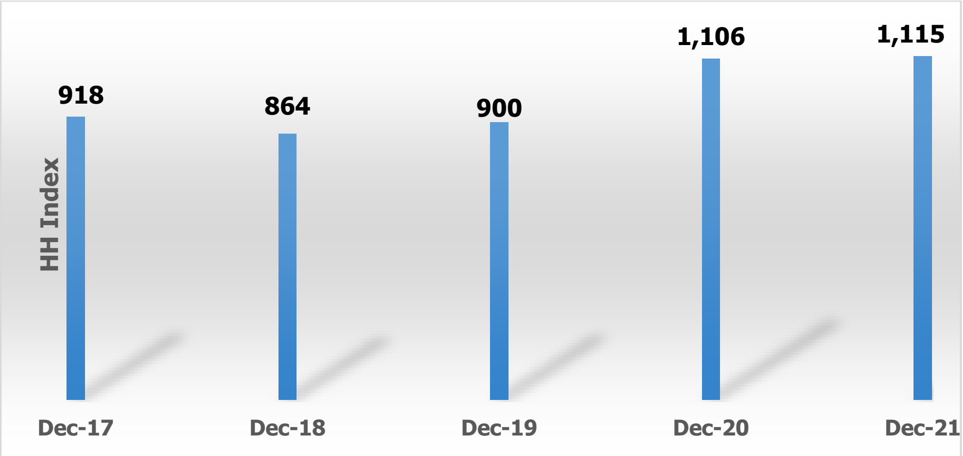
$$BSI_t = w_c\overline{X_{tc}} + w_a\overline{X_{ta}} + w_e\overline{X_{te}} + w_q\overline{X_{tq}} + w_s\overline{X_{ts}}$$

Where BSI_t is the value of the BSI at time t and $\sum_{r=c,a,e,q,s} w_r = 1$

Banking Sector Concentration

2.4 The Zimbabwean banking sector has generally exhibited low levels of concentration as shown by the Herfindahl-Hirschman indices in the figure below (*Refer to Box 2*).

Figure 6: Herfindahl-Hirschman Index



2.5 Notwithstanding the depicted low levels, the figure above shows that the level of concentration in the banking sector has been on an upward trend since 2017. The Bank implemented **Prudential Standard No: 1-2020/BSD: Framework for Dealing with Domestic Systemically Important Banking Institutions** with the objective of ensuring that systemically important banking institutions are subjected to more stringent prudential requirements.

BOX 2: THE HERFINDAHL-HIRSCHMAN INDEX

The Herfindahl-Hirschman Index is an index that measures the market concentration. It is computed as follows

$$HHI = s_1^2 + s_2^2 + \cdots + s_n^2 = \sum_{i=1}^{n} s_i^2$$

Where s_i is a banking institution's share of total banking sector assets.

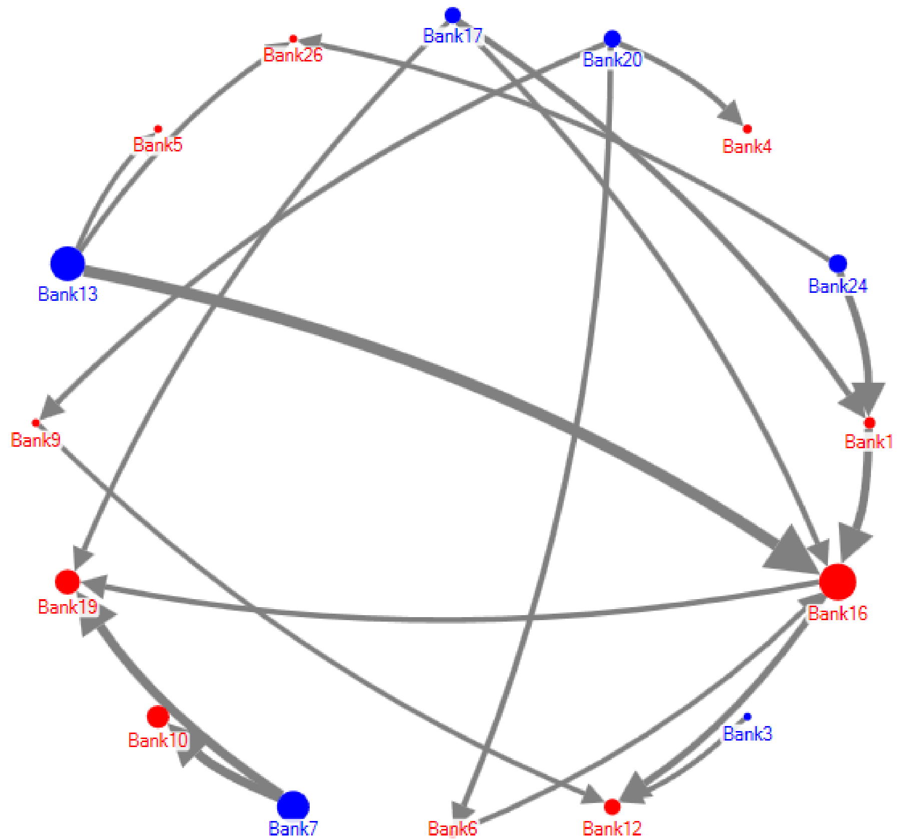
HHI of between 1 500 and 2 500 points to moderate concentration, while HHI greater than 2 500 points to high concentration.

The Interbank Network Analysis

2.6 An analysis of the Zimbabwean interbank network as at 31 December 2021 revealed moderate interconnectedness with some banking institutions not having any deposits from other banks or lending to other banks.

2.7 The interbank network is presented in the figure below with arrows showing the direction of the flow of credit, from the lending bank to the borrowing bank.

Figure 7: Interbank Network as at 31 December 2021



2.8 The above shows that 16 institutions had either direct or indirect connections with other institutions. This means that shocks in one institution can be transmitted to other banking institutions within the network. There was one significant borrower in the network (Bank 16) as at 31 December 2021 which had borrowings / placements from four other banking institutions.

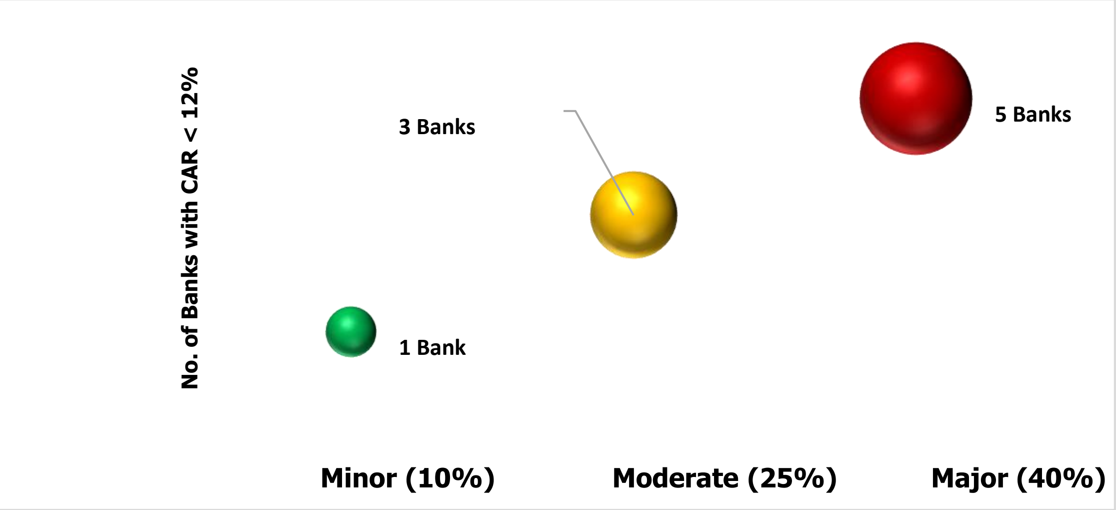
Credit Risk

2.9 Inherent credit risk remained moderate during the year under review against the backdrop of the disruptive effects of Covid-19 on the level of economic activity. A combination of fiscal interventions designed to contain the covid 19 shock, as well credit risk management enhancements by banking institutions, however, mitigated potential shocks on asset quality.

2.10 Against this background, the banking sector depicted resilience as reflected by a low NPL ratio of 0.94% as at 31 December 2021 against the internationally recommended level of 5%.

2.11 Banking sector resilience to credit risk shocks was also demonstrated by stress test results as at 31 December 2021 which showed that a minor credit shock, of a 10% increase in nonperforming loans, would result in one bank having a capital adequacy ratio (CAR) below the regulatory minimum of 12%. An additional two banking institutions were vulnerable to a moderate shock of 25% increase in nonperforming loans whilst an additional two banks were vulnerable to a major credit shock of 40% of performing loans becoming nonperforming loans, with their CARs falling below the regulatory minimum of 12%. Given the mitigants outlined above and the quality of the current credit portfolios, the likelihood of significant shocks materialising is considered low.

Figure 8: Credit Stress Test: Increase in NPLs



Source: RBZ (2022)

2.12 A sectoral analysis of the banking sector's loan portfolio showed that most of the loans were to agriculture (29%) and individuals (21%). The lower-than-expected rainfall during the 2021/2022 agriculture season may impact the performance of some agriculture loans. The banking sector level of capitalisation is however, considered adequate to absorb the potential losses from distressed agricultural loans.

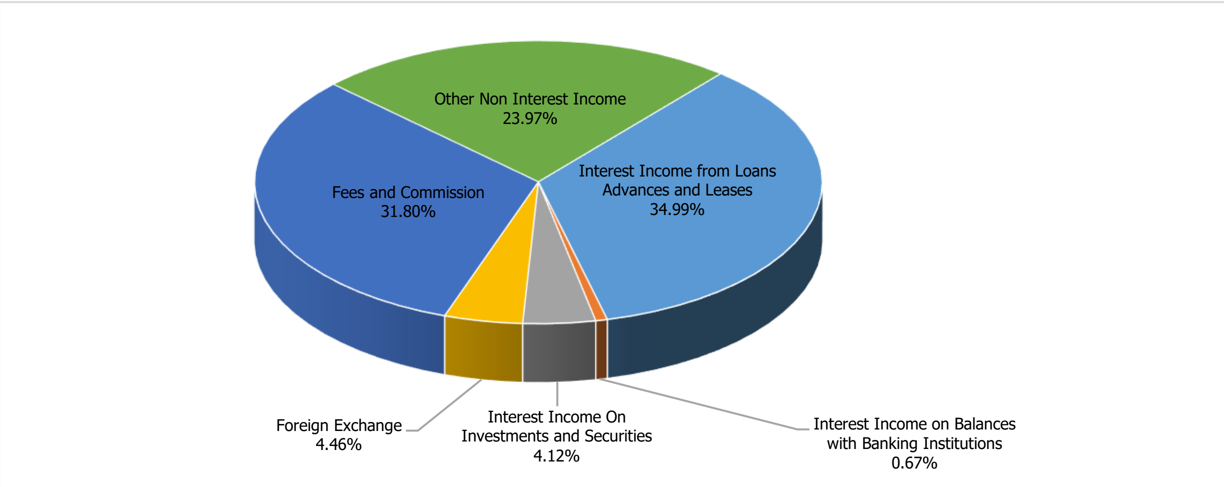
Income Generation Risk

2.13 In an environment characterised by Covid-19 related disruptions, inflationary pressures, as well as cautious approach to lending as banks tightened credit risk management, inherent income generation risk was moderate during the year ended 31 December 2021.

2.14 The banking sector however demonstrated resilience as reflected by net aggregate profit of ZW$59.29 billion for the year ended 31 December 2021, compared to ZW$34.24 billion recorded in December 2020. The growth was mainly spurred by a combination of fees from increased digital financial services and lending activities, and revaluation gains on investment properties and foreign currency denominated assets.

2.15 The proportion of interest income from loans and advances significantly increased from 17.82% of total income in 2020, to 34.99% as at 31 December 2021, largely a reflection of enhanced financial the relaxation of Covid-19 restrictions.

Figure 9: Banking Sector Income Mix as at 31 December 2021



Source: RBZ (2022)

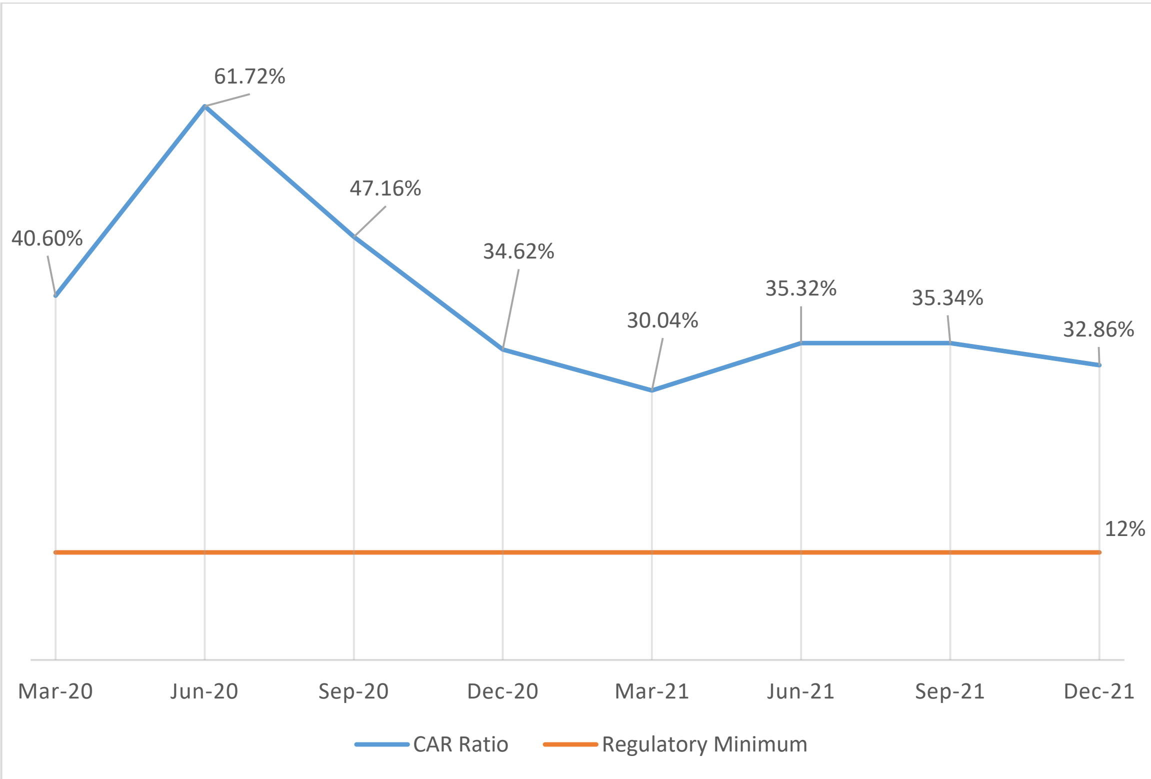
The banking sector is expected to remain profitable in the outlook period underpinned by sustainable sources of funding as shown in Figure 9 above.

Capital/Solvency Risk

2.16 Against the background of minimal shocks from credit risk as well as strong earnings position, banking institutions had adequate capital buffers to support banking operations and to enable the sector to continue playing its role of providing credit to the real economy.

2.17 The figure below shows the trend in the banking sector's capital adequacy ratio from March 2020 to December 2021.

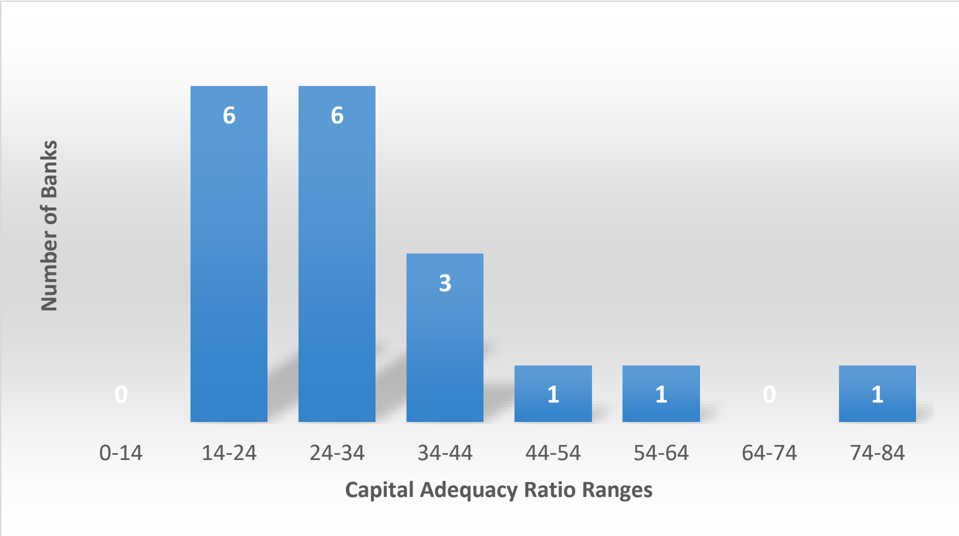
Figure 10: Capital Adequacy Ratio Trend: March 2020 to December 2021



Source: RBZ (2022)

2.18 The figure below shows an analysis of the distribution of banks' CARs as at 31 December 2021.

Figure 11: Distribution of Banks' CARs (%)



Source: RBZ (2022)

2.19 Due to the pandemic induced challenging operating environment, which the banking sector was facing, the Bank extended the deadline for compliance with the requirement for meeting the new minimum capital levels from 31 December 2020 to 31 December 2021. The extension gave banking institutions more time to raise the required minimum capital meant to enhance the banks' ability to absorb unforeseen risks and to strengthen their balance sheets.

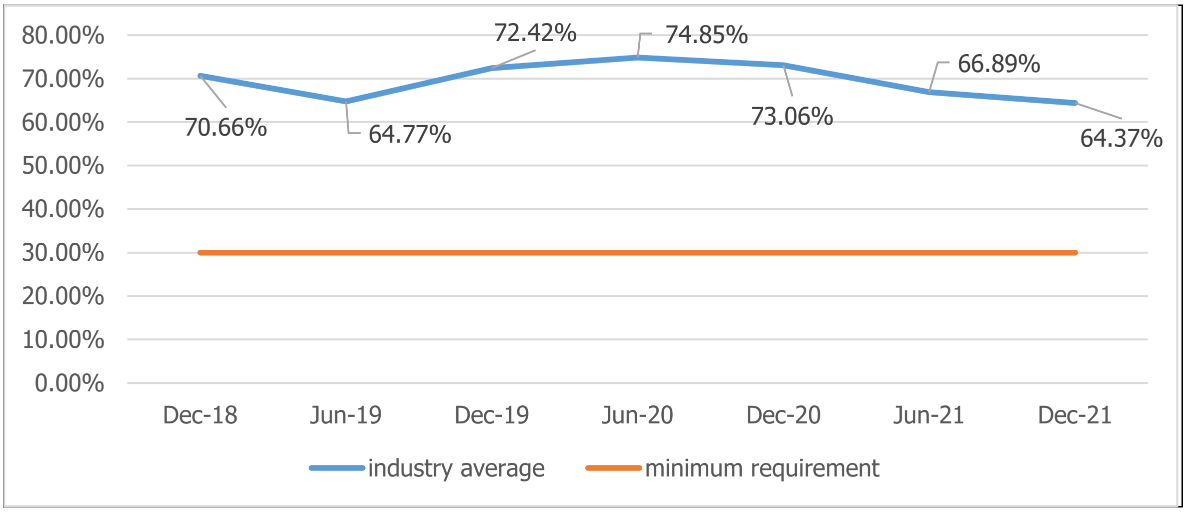
2.20 As at 31 December 2021, most banking institutions were in compliance with the new minimum capital requirements effective 31 December 2021. The remaining few banking institutions were granted up to 31 December 2022 to comply with the minimum capital requirements. As such these institutions were not permitted to pay dividends without prior approval of the Bank until such a time that they have met the new minimum capital requirement.

Liquidity Risk

2.21 The banking sector had adequate liquidity holdings as reflected by the average prudential liquidity ratio of 64.37% as at 31 December 2021, against the minimum regulatory requirement of 30%, largely reflecting high stock of liquid assets in the sector.

2.22 The trend in the liquidity ratio from 31 December 2018 to 31 December 2021 is shown in the figure below.

Figure 12 : Prudential Liquidity Ratio Trend



Source: RBZ (2022)

2.23 All banking institutions remained resilient to both minor and moderate liquidity risk shocks as at 30 December 2021, as their cash flows remained positive before or on the fifth day of the stressful period. Only four banks were susceptible to a major liquidity stress test as their cash flows became negative within five days of the stressful period.

2.24 Liquidity risk is expected remain low in the outlook in light of excess reserve holdings at most banking institutions on the backdrop of the absence of a well-developed bond market and hence limited availability of investment options to deploy the excess liquidity.

Market Risk

2.25 Under the current operating environment, the banking sector's exposure to interest rate risk is mainly in the banking book in view of limited trading activities. In addition, sources of funds for banks are predominantly retail deposits which are relatively less interest rate sensitive, while re-pricing assets are mainly loans and advances and treasury bills. Prevailing high interest rate spreads cushion banking institutions' balance sheets from capital erosion.

2.26 As at 31 December 2021 the banking sector had an overall asset sensitive book, with a cumulative re-pricing gap of ZW$68.34 billion in the 1-365 days' time bucket meaning that assets re-price or reset faster than liabilities.

2.27 The banking sector was resilient to interest rate shocks as revealed by stress test results which showed that a minor shock of a 10-percentage point increase in interest rates would result in only one (1) bank having a CAR less than the minimum regulatory threshold. A moderate shock of a 20-percentage point increase and a major shock representing a 30-percentage point increase in interest rates, may result in additional three (3) banking institutions having CAR of less than 12%. The total asset base of the vulnerable banks account for only 9.53% of the total banking sector assets.

2.28 Both monthly food and non-food inflation, which had been falling in the first half of the year, assumed an upward trend in line with the exchange rate developments in the second half of 2021. In this regard, the Bank increased the policy rate to end the year at 60%, in order to curb speculative borrowing.

2.29 The banking sector's reported net open position deteriorated from deficit of ZW$78.71 billion in December 2020 to a deficit ZW$166.95 billion in December 2021 largely due to the depreciation of the local currency from an average of ZW$81.81/US$1 in December 2020 to an average of ZW$107.83/US$1 in December 2021. Stress test results, however, indicate that the banking sector is largely resilient to potential future exchange rate shocks.

Strategic Risk

2.30 The dynamic operating landscape in 2021, exposed banking institutions to amplified strategic and business model risks. Banking institutions reconfigured their business models and instituted revenue enhancement and cost rationalisation measures. Strategic risk is expected to remain moderate due to uncertainties in the operating environment.

Operational Risk

2.31 Adoption of new technologies such as Digital payments and E-money, Big Data Analytics, Artificial Intelligence, and Cloud Computing have been associated with amplified operational risks as well as generation of new risks such as cyber risk. Increasing incidences of fraud and card cloning were registered during the review period. Banking institutions continued to enhance their information management frameworks including adoption of EMV compliant electronic payment cards.

2.32 Operational risk remains inherently high due to the increase in volume of online transactions which has heightened cyber–risk. Emergence of new Covid-19 variants also remains a possibility in the outlook. Heightened operational and cyber risks have the potential to disrupt the smooth functioning and efficiency of the payments system with negative consequences on financial stability.

2.33 Banking institutions are continuing to develop core competences and requisite frameworks in managing emerging risks, including cyber risk.

2.34 Banking institutions are also required to comply with the Society for Worldwide Interbank Financial Telecommunication (SWIFT) Customer Security Controls Framework for Cybersecurity management.

2.35 Table 2 below presents the banking sector's major risks at an aggregate level and assessment of the adequacy of risk management systems across the market as at 31 December 2021.

Table 2: Banking Sector Risk Matrix as at 31 December 2021

Type of Risk	**Level of Inherent Risk**	**Adequacy of Risk Management Systems**	**Overall Composite Risk**	**Direction of Overall Composite Risk**
Credit	Low	Acceptable	Low	Stable
Liquidity	Low	Acceptable	Low	Stable
Foreign Exchange	Moderate	Acceptable	Moderate	Stable
Interest Rate	Moderate	Acceptable	Moderate	Stable
Strategic Risk	Moderate	Acceptable	Moderate	Stable
Operational Risk	High	Acceptable	High	Increasing
Legal & Compliance Risk	Moderate	Acceptable	Moderate	Stable
Reputational Risk	Moderate	Acceptable	Moderate	Stable
Overall	**Moderate**	**Acceptable**	**Moderate**	**Stable**

3. CAPITAL MARKETS PERFORMANCE

3.1 The capital market sector remained stable in 2021 and was able to play its role as a source of long-term funding and investment. The economic stabilisation efforts such as the foreign exchange auction system introduced in June 2020 to stabilise the exchange rate, have impacted positively on the capital markets' returns on investments for both Securities Market Intermediaries (SMIs) and investors.

Capital Market Structure

3.2 A summary of the total number of licensed and registered institutions in the capital market as at 31 December 2021 (Securities Market Intermediaries) is shown in the table below.

Table 3: Number of SECZ Licensed Entities

Type of institution	2021	2020
Securities Exchanges	3	3
Central Securities Depositories	2	1
Securities Dealing (Stockbroking) firms	20	18
Securities Investment (Asset) Management firms	24	22
Securities Custodial firms	5	5
Securities Transfer Secretaries firms	3	3
Securities Trustee firms	3	3
Securities Advisory firms	50	44

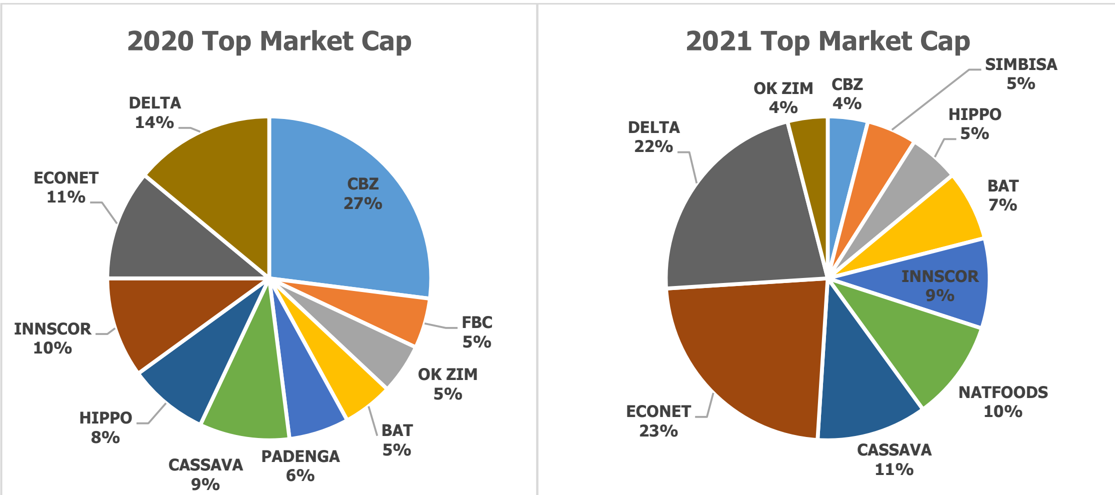
Source: Zimbabwe Stock Exchange

3.3 The Securities and Exchanges Commission of Zimbabwe assessment of the capital markets reflects notable resilience based on the key financial soundness indicators including Capital, Liquidity, Earnings, Solvency, Funds under management/ Assets under custody, Management Quality and Turnover. There was an improvement in the capital adequacy of investment management firms as there were 20 out of 21 firms which were adequately capitalised compared to 16 reported during the previous period. One asset manager reported operating losses. The sector's profitability and capital adequacy compliance stood at 81% and 95.2%, respectively, as at December 2021. The industry losses reported were mainly linked to new entrants into the asset management industry who are still to gain critical mass. The adoption of a risk adjusted capital framework by Securities and Exchange Commission has stabilized the solvency of both individual institutions and the sector.

3.4 The Zimbabwe Stock Exchange (ZSE) market capitalisation gained 314.37% during the year to close the period on 31 December 2021 at ZW$1.32 trillion from ZW$317.88 billion reported in 2020.

3.5 The All Share and Top Ten indices grew by 311% and 191%, respectively, during the period under review. The top ten contribution to the total market capitalisation increased from 68.5% in December 2020 to 73.59% as at 31 December 2021. The figure below summarized the composition of the top ten counters on the ZSE.

Figure 13: Top Ten Counters to Market Capitalization



Source: Zimbabwe Stock Exchange

3.6 The value of trades (turnover) for the period ended 31 December 2021 increased by 276.80% to ZW$65.27 billion from ZW$17.32 billion that was reported in 2020.

Table 4: Equity Markets Performance Summary

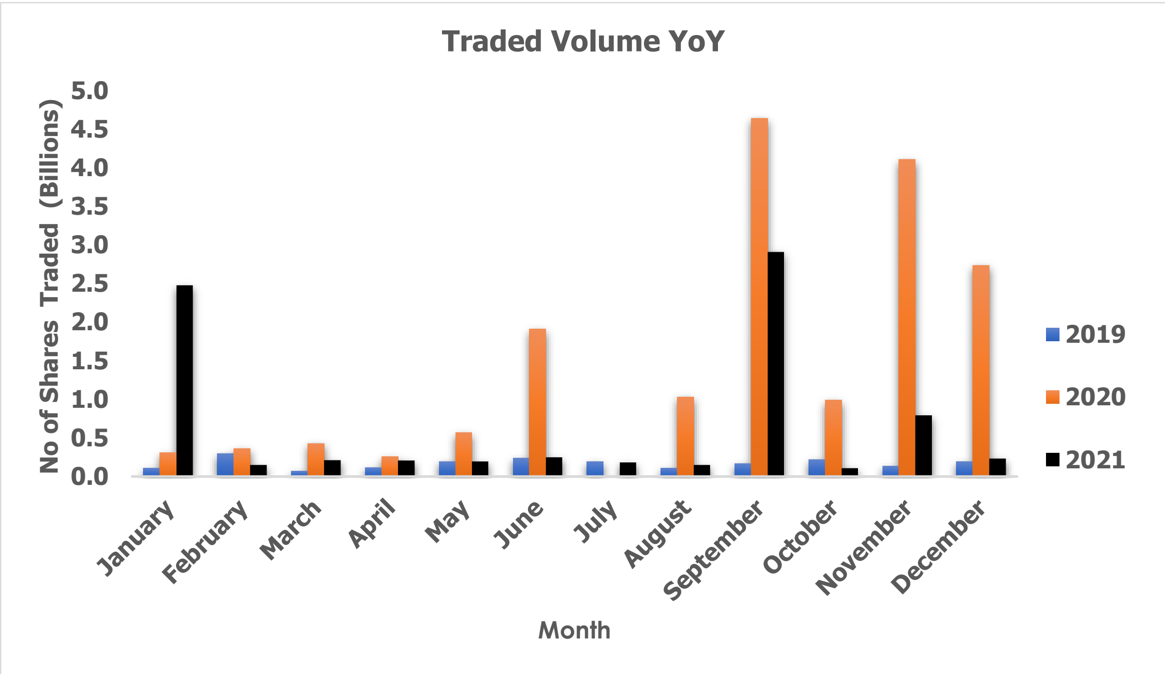
	2019	2020	2021	% Change
ZSE Turnover	ZW$2,028,580,517	ZW$17,321,473,923	ZW$65,266,783,511	277%
Traded Volume	2,283,747,926	3,735,809,255	7,851,770,473	110%
Market Capitalisation	ZW$29,767,094,449	ZW$317,879,307,047	ZW$1,317,205,109,565	314%
All Share Index	230.08	2,636.34	10,822.36	311%
Top 10 Index	200.56	1,671.47	4,857.20	191%
No of Listed Companies	60	51	50	-2%

Source: Zimbabwe Stock Exchange

3.7 Foreign investors registered a net sell-off of ZW$9.73 billion, during the year accounting for 14.91% of total trades for the year.

3.8 The performance of the equity markets is summarized in the figure below.

Figure 14: Volume of Shares Traded Year on Year (2019- 2021)



Source: Zimbabwe Stock Exchange

3.9 Victoria Falls Stock Exchange (VFEX) recorded US$619,549 worth of trades during the year and market capitalization grew to US$254 million. As at the end of 2021, four companies were listed on VFEX namely Padenga Holdings, SEEDCO, Bindura Nickel Corporation and Caledonia Mining.

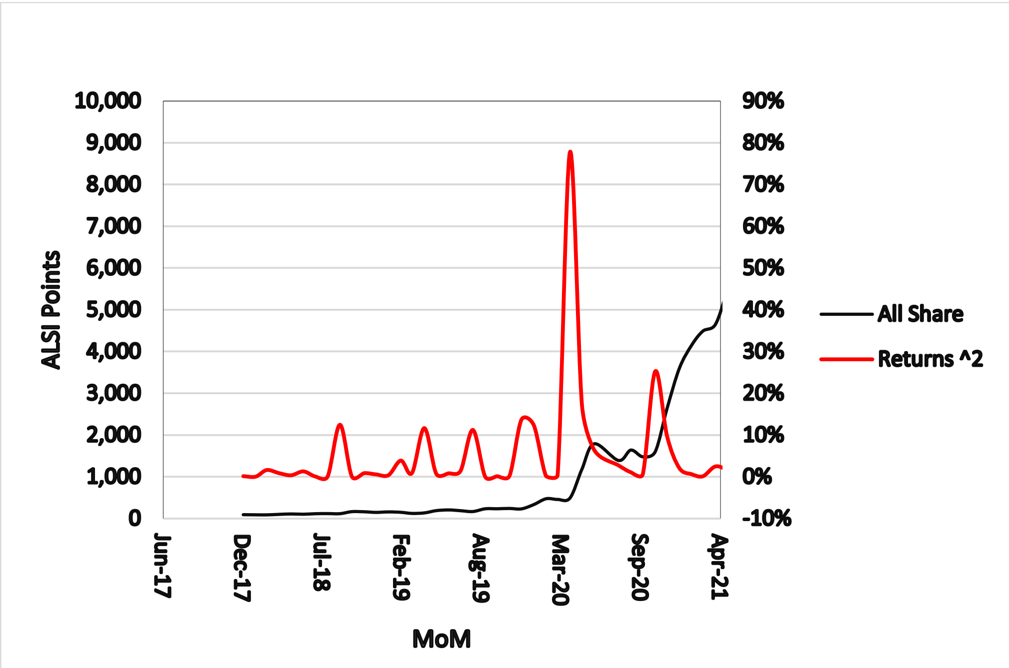
3.10 The low stock price volatility on the VFEX market stabilised the profitability and returns on investments for both Securities Market Intermediaries (SMIs) and investors.

3.11 As at 31 December 2021, Assets under Custody (AUC) amounted to ZW$533.26 billion which was a 257.30% increase from ZW$149.25 billion reported as at 31 December 2020.

ZSE All Share Index (ALSI) Volatility

3.12 The ALSI volatility was calculated using industrial indices from January 2018 to December 2021. The ALSI Index Monthly Exponentially Weighted Moving Average (EWMA) relative volatility is shown below.

Figure 15: All Share Index EWMA Relative Volatility (January 2018–December 2021)



Source: Zimbabwe Stock Exchange

3.13 The ALSI volatility was estimated at 4.17% as of 31 December 2021 (Q32021-4.31%), using a smoothing constant of 0.97. The increased retail investors' activity, and the widening gap between interbank exchange rate and parallel market rates continued to shock the market and smoothen equity prices volatility. The ZSE equities presented a viable and rewarding alternative for investors which include institutional investors such as pension funds, insurance companies and corporate sector.

3.14 The FINSEC Alternative Trading Platform's market capitalisation closed at ZW$8.30 billion in December 2021 from ZW$5.89 billion in September 2021, a 41% quarterly increment and a significant increase of 277% from $2.2 billion in December 2020. The turnover grew by 439% while the volume of shares traded rose by 99% to 3.2 million from previous 1.6 million shares. The table below summarises the overall performance of the FINSEC ATP.

Table 5: FINSEC ATP Performance Summary

Financial Securities Exchange	2019	2020	2021	% Change
ATP Turnover	49,907,564	57,251,889	308,667,813	439%
ATP Traded Volume	ZW$9,886,188	ZW$1,595,785	ZW$3,175,393	99%
ATP Market Cap	ZW$996,140,616	ZW$2,199,810,527	ZW$8,301,171,900	277%
Number of listed Companies	1	1	1	

Source: Zimbabwe Stock Exchange

Investment Management

3.15 Funds under Management (FUM) for the industry as at 31 December 2021 stood at ZW$534 billion [Q3-2021-ZW$396.8 billion] representing an increase of 241.2% from ZW$156.5 billion reported as at 31 December 2020. The increase was mainly attributed to price valuations and the conversion of United States Dollar (US$) denominated property assets as at 31 December 2021.

Table 6: Asset Management Summary (December 2021)

Asset Management	2018	2019	2020	2021	*Change*
Total FUM)	ZW$7,159,044,293	ZW$15,050,708,208	ZW$156,539,539,068	ZW$534,071,318,090	241.2%
Collective Investments Schemes	ZW$168,176,773	ZW$167,023,446	ZW$730,246,168	ZW$5,668,692,465	676.3%
CIS / Total Market FUM	2.3%	1.1%	0.5%	1.1%	127.5%
Number of Players	16	19	22	24	9.1%
**Capital Adequacy Compliance (%)*	93.8%	77.8%	72.2%	95.2%	31.9%
**Firms' Positive Earnings (%)*	62.5%	100.0%	89.5%	81.0%	-9.5%

3.16 A significant increment in retail investors was registered as reflected by the 6.8 times increase of collective investment schemes composition of FUM from 0.5% to 1.1% of the total funds under management.

Figure 16: Distribution of Funds Under Management as at 31 December 2021

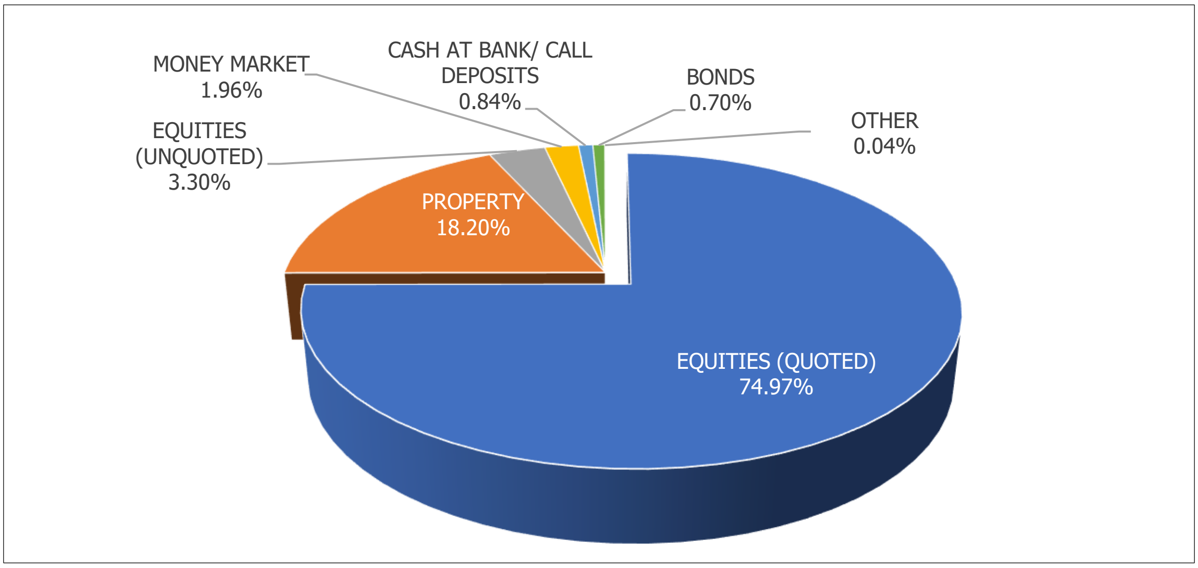
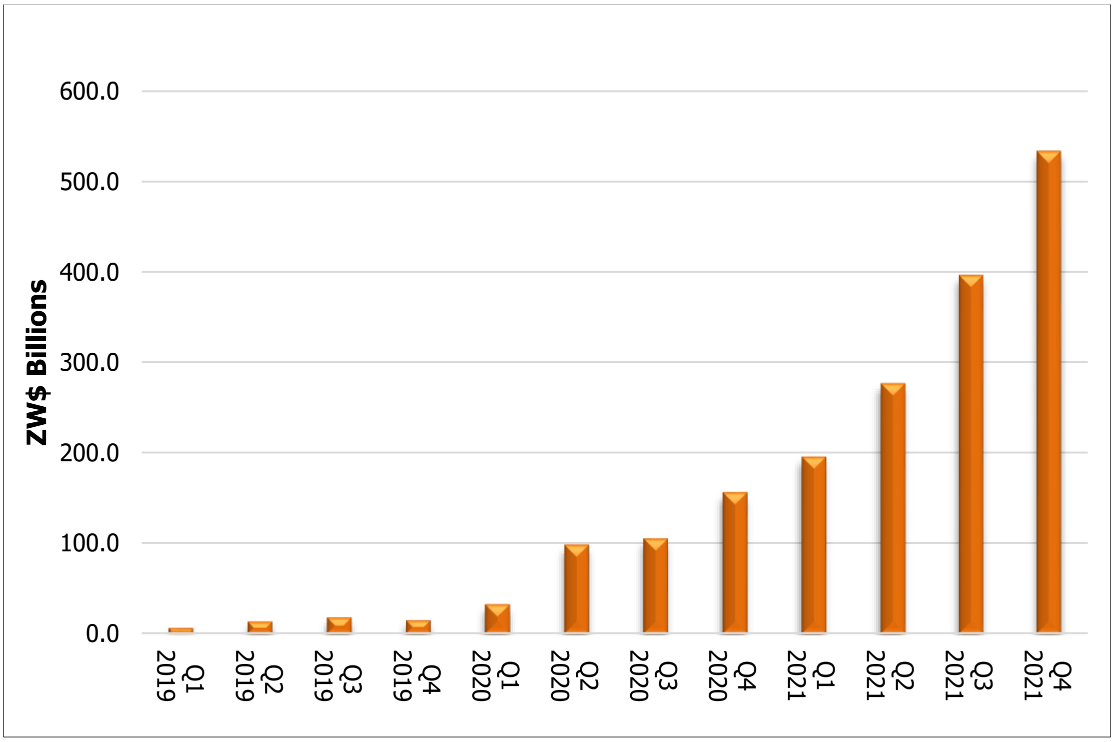


Figure 17: Funds Under Management as at 31 December 2021



Capital Markets Risk Management and Developments

3.17 The Securities and Exchange Commission of Zimbabwe (SECZ) became an associate member of the International Organization of Securities Commissions (IOSCO) in January 2022. The development provides opportunities for the Commission to collaborate with other world regulators and enhance its regulation and supervision techniques to promote stability of the capital markets.

3.18 Securities Market Institutions (SMIs) continued to adopt the practices necessary to fight the spread of Covid-19 and ensure availability of uninterrupted financial services. SECZ encouraged SMIs to invest in basic technology for customer data retention and historical company information.

3.19 In addition, SECZ set up a dedicated team on the assessment of the fintech ideas from both the market players and individuals to harness technology in capital markets sector.

4. CONDITION AND PERFORMANCE OF THE INSURANCE AND PENSIONS INDUSTRY

4.1 The insurance and pensions sector remained largely sound and stable during the period under review in spite of the challenging operating environment characterised by increasing Covid-19 cases, inflation pressures and some unresolved legacy issues.

Risks to the Insurance and Pensions Industry

Reputational Risk

4.2 In line with the Justice Smith Commission of Inquiry recommendations of 2015, the Commission initiated the compensation of policy holders and pensioners for the loss of value suffered due to hyperinflation in 2007 and 2008 and the adoption of a multi-currency system in 2009. The development is expected to reinforce confidence in the insurance sector.

4.3 Pension benefit arrears grew by 85% from ZW$327.55 million in 2020 to ZW$606.70 million in 2021. The arrears include those of non-resident pensioners whose pension pay-outs have remained outstanding for years owing to foreign currency challenges.

Economic Risk

4.4 Inflation risk arising from exchange rate volatility affected performance of some insurance companies during the review period. In response the sector undertook regular premium reviews to match inflation developments. Meanwhile compensation packages generally lagged behind inflation, thereby reducing disposable incomes and affecting the demand for insurance products. The mismatch between inflation developments and salary reviews was evidenced by the increase in the lapse rate as policyholders failed to keep pace with premium reviews.

4.5 The structure of Gross Premium Written by the industry was skewed towards short-term products, thus indicating the negative impact of inflation on the industry. Life products were largely driven by defined benefit products such as funeral services, group life (Group Life Assurance) and group funeral. Inflation also worsened the purchasing power of pensioners who were already getting low pension pay-outs.

Operational Risk

4.6 Inherent operational risk was rated high for the review period on account of the increased number of applications for dissolutions, potential cyber security risk and uncertainty about the Covid-19 pandemic, which threatened business continuity. It was, however, noted that the Covid-19 impact on claims was not as high as anticipated as the increase was 109.7% from ZW$135 million in 2020 to ZW$282 million as at 31 December 2021.

4.7 There were, however, no reported cases of cyber risk in the industry during the review period. To enhance awareness and mitigation of cyber security risk, SECZ is in the process of developing a framework which will be issued to the industry.

Liquidity Risk

4.8 Liquidity risk was considered medium in 2021 on account of the growth in premium debtors and contribution arrears attributed to challenging macroeconomic conditions.

Regulatory Risk

4.9 Regulatory risk was rated low. Average compliance levels with Minimum Capital Requirements (MCR) improved from 87% in 2020 to 93% in 2021. Compliance levels for the funeral assurers were the lowest at 63% from 38% in 2020.

4.10 Compliance with prescribed asset minimum requirement continued to be low, at an average of 1.1% for short-term insurers, 3.49% for life assurers and 4.08 % for pension funds against compliance thresholds of 10%, 15% and 20%, respectively. The low compliance rates were mainly attributed to the quest for balance between compliance and preservation of value. This was reflected in the concentration of investments in two (2) asset classes, namely investment property and listed equities which were 70% for pensions, 55% for short term insurance and 90.70% for life companies.

Solvency Risk

4.11 IPEC implemented the Zimbabwe Integrated Capital and Risk Programme (ZICARP) Framework in June 2021, which aims to, among other objectives, improve consumer protection and assurance to policyholders and beneficiaries. ZICARP provides incentives to insurers to measure and properly manage their risks, which enables them to absorb significant unforeseen losses. The framework introduced a principle-based approach to regulation, moving away from a rules-based approach, to ensure better allocation of capital resources in insurance firms, align supervision of all insurance entities and make the sector more attractive to investors.

4.12 To minimise compliance risk, the Commission encouraged entities to align their capital with the outcomes of the ZICARP dry runs in order to avoid last minute efforts to raise additional capital.

Market Risk

4.13 Market risk was considered moderate to high during the review period. Insurance and pensions liabilities are generally of a long-term nature and the unavailability of a variety of matching assets exposes the industry to market risk. This is exacerbated by the dominance of the market by a few asset classes namely equities and properties. Listed equities were 36% of the assets, showing that a substantial amount has been channelled to the Victoria Falls Stock Exchange. The widening of Victoria Falls Stock Exchange and the granting of prescribed asset status on foreign currency denominated instruments is expected to reduce market risk going forward.

5. DEPOSIT PROTECTION SCHEME

5.1 The roles and functions of the Deposit Corporation of Zimbabwe (DPC) facilitate the maintenance of financial stability by guaranteeing protection to depositors in the banking sector, whereby depositors are compensated the insured portion of their deposits in the event of failure of a contributory institution.

5.2 The existence of deposit protection is of paramount importance in minimizing the risk of bank runs, which involves panic withdrawals due to failure of one bank or rumours of fragility in the banking sector.

Risks to the Deposit Protection Corporation Fund

5.3 The DPC Fund, in fulfilment of its mandate of protecting depositors, is exposed to three main risks as shown in the Table below.

Table 7: DPC Risks and Mitigation

Type of Risk	Impact	Risk Mitigants Quality rating	Residual Risk	Direction of Risk
Investment Risk • **Investing the main source of income i.e. premiums on money market where returns are low.**	**High** • Low returns than inflation rate. • Value of Deposit Protection Fund growth is stunted. • Continued depreciation of local currency diminishes value of Fund	• Diversification of investment portfolio into properties and special instruments like prescribed bonds to hedge against inflationary pressures as well as improve the rate of return on investments.	**Moderate**	**Stable**
Fund Adequacy Risk • **The combined fund size against watchlist exposures**	**High** • Limited capacity to fulfil its mandate of paying depositors in the event of a material compensation event.	• Restoration of ZW$ premium rate to 0.3% per annum. • Gradual increase in FCA premium rate effective January 2022	**High**	**Stable**
Insurance Assessment Risk • **Safety and soundness of Contributory Banking institutions**	**Low** • Wrong determination of insurance exposure in the event of a compensation event	• CBIs' and DPC's external auditors verify the deposits yearly • RBZ regular on-site examinations • MOU with RBZ on sharing information. • Monthly meetings between RBZ and DPC	**Low**	**Stable**

Deposit Protection Corporation Cover Level

5.4 As at 31 December 2021, 92.3% of the contributory banking institutions' (CBI's) depositor accounts were fully covered at the cover level of ZW$10,000 per depositor per bank. This is in line with the public policy objectives of covering at least 90% of the depositors.

5.5 At the cover level of US$1000.00 per individual FCA deposit class, 96.3% of the depositors were fully covered in compliance with the public policy objectives of covering at least 90% of the depositors.

5.6 The coverage levels for the banking institutions is reflected in Tables 9 and 10.

Table 8: Deposit Insurance Coverage for Banking Institutions (Local Currency Accounts)

Item	December 2021	Percentage
Total Number of Deposit Accounts	5,871,908	100%
Total Number of Deposit Accounts Fully Covered	5,419,591	92.3%
Total Number of Deposit Accounts Partially Covered	452,317	7.7%
Value of Deposits in Fully Covered Accounts	ZW$2.9 billion	1.3%
Value of Deposits in Partially Covered Accounts	ZW$225.2 billion	98.7%
Total Value of Insured Deposits	ZW$7.4 billion	3.2%
Total Value of Deposits	**ZW$228.1 billion**	**100%**

Table 9: Deposit Insurance Coverage for Banking Institutions (Foreign Currency Accounts)

Item	December 2021	Percentage
Total Number of Deposit Accounts	920,708	100%
Total Number of Deposit Accounts Fully Covered	886,153	96.3%
Total Number of Deposit Accounts Partially Covered	34,555	3.7%
Value of Deposits in Fully Covered Accounts	US$38.6 million	2.5%
Value of Deposits in Partially Covered Accounts	US$1,520.1 million	97.5%
Total Value of Insured Deposits	US$72.5 million	4.7%
Total Value of Deposits	**US$1,558.7 million**	**100%**

5.7 At the maximum deposit insurance cover level of US$500 per individual deposit class, 92.3% of the FCA deposit accounts in the deposit-taking microfinance institutions (DTMFIs) sector were covered in full.

5.8 At the cover level of ZW$500 per depositor per institution, 91.3% of the DTMFI depositors were fully covered as shown in Table 11 and 12.

Table 10: Deposit Protection Cover for DTMFIs as at 31 December 2021 *(Local Currency Accounts)*

Item	December 2021	Percentage
Total Number of Deposit Accounts	201,828	100%
Total Number of Deposit Accounts Fully Covered	184,253	91.3%
Total Number of Deposit Accounts Partially Covered	17,575	8.7%
Value of Deposits in Fully Covered Accounts	ZW$5.8 million	1.1%
Value of Deposits in Partially Covered Accounts	ZW$505.7 million	98.9%
Total Value of Insured Deposits	ZW$14.6 million	2.9%
Total Value of Deposits	**ZW$511.5 million**	**100%**

Table 11: Deposit Protection Cover for DTMFIs as at 31 December 2021 *(Foreign Currency Accounts)*

Item	December 2021	Percentage
Total Number of Deposit Accounts	1,276	100%
Total Number of Deposit Accounts Fully Covered	1,178	92.3%
Total Number of Deposit Accounts Partially Covered	98	7.7%
Value of Deposits in Fully Covered Accounts	US$25,825	0.7%
Value of Deposits in Partially Covered Accounts	US$3,848,545	99.3%
Total Value of Insured Deposits	US$74,825	1.9%
Total Value of Deposits	**US$3,874,370**	**100%**

5.9 As at 31 December 2021, membership to the DPC Scheme was comprised of 27 contributory financial institutions (CBIs) as shown in the Table below:

Table 12: Membership to the DPC Scheme as at 31 December 2021

Type of Institution	Number
Commercial Banks	13
Building Societies	5
Merchant Banks	1
Savings Bank	1
Infrastructure Development Bank	1
Deposit-Taking Micro-finance Institutions (DTMFIs)	6
Total	**27**

Future Regulatory Developments

5.10 Deposit Protection Corporation undertook a review of the **DPC Act, [*Chapter 24:29*].** This was occasioned by the liquidation provisions, in the new **Insolvency Act, [*Chapter 6:07*]**, which was revised in 2018, precluding the application of the Act to banking institutions and insurance companies. Proposed amendments had been submitted to the Attorney General for input as at the end of 2021.

5.11 DPC is also proposing changes to the Problem Bank Resolution laws providing for, *inter alia*, writing down of shareholding, to instil finality & speedy CBIs resolution.

5.12 The smooth resolution of failed banks is a prerequisite for a stable financial system.

6. FINANCIAL MARKETS INFRASTRUCTURE

6.1 A strong and well-functioning national payment systems fortifies the foundations of economic growth and development. In this regard, the Bank takes quick and decisive steps to ease any payment, clearing and settlement constraints in the value chain, at the same time strengthening the regulatory and supervisory framework to proactively identify, assess and deal with vulnerabilities in the ecosystem.

6.2 The national payment services sector remained robust, notwithstanding the disruptive effects of the Covid-19 pandemic during the period under review.

Major Highlights and Developments

6.3 The key highlights of the national payment systems sector's activities in 2021 were:

i. the payment systems comprising of 13 payment system providers and 25 participant banks continued to register upward trend in values in the various payment streams during 2021;

ii. transaction values grew by 192% percent to ZW$1,160 billion, whilst the volumes increased by 19.5% percent to 130.78 million in 2021 compared to 2020 period. The Tables below show the monthly transactional values and volumes respectively;

iii. a total of 28 products from different financial institutions were approved in 2021 compared with a total of 16 in the previous period;

iv. the Cybersecurity Risk Based Guideline on Payment Systems and the Risk Based Anti-Money Laundering Guideline were issued during the review period;

v. the Reserve Bank evaluated self-assessments for compliance from seven institutions against the 24 Principles of Financial Market Infrastructures [PFMIs] (core payment systems standards under the Bank for International Settlement (BIS));

vi. two anti-money laundering inspections were conducted on high-risk institutions as informed by the sectorial risk assessment and risk-based approach; and

vii. the local banking community continued to participate in the SADC Real-Time Gross Settlement System (SADC-RTGS) and maintained a progressive share of transaction values processed in the SADC-RTGS.

Table 13: National Payment Systems Transactional Activities January - December 2021

TRANSACTION VALUES IN BILLIONS (ZW$)							
MONTH	**RTGS**	**ATM**	**POS**	**Mobile**	**Internet**	**Values Total**	**Total Change**
Jan-21	255.55	2.30	21.04	35.35	66.62	380.87	-15%
Feb-21	226.34	2.29	22.88	36.43	63.60	351.54	-8%
Mar-21	320.42	3.32	28.57	44.52	86.46	483.30	37%
Apr-21	288.96	2.81	30.07	44.13	90.58	456.55	-6%
May-21	361.43	3.19	36.77	49.75	89.47	540.60	18%
Jun-21	388.76	3.20	38.54	51.44	115.15	597.08	10%
Jul-21	379.66	2.49	45.81	57.57	145.03	630.55	6%
Aug-21	397.54	4.09	52.85	60.91	159.21	674.59	7%
Sep-21	477.93	4.18	52.26	64.14	181.19	779.71	16%
Oct-21	481.18	3.84	53.17	65.33	197.97	801.49	3%
Nov-21	621.90	4.88	56.03	63.44	252.41	998.65	25%
Dec-21	747.04	4.71	67.90	76.51	264.75	1,160.91	16%
TOTAL YTD	**4,946.70**	**41.28**	**505.89**	**649.52**	**1,712.44**	**7,855.83**	
Proportion	**63.0%**	**0.5%**	**6.4%**	**8.3%**	**21.8%**	**100.0%**	

Table 14: National Payment Systems Transactional Activities January - December 2021

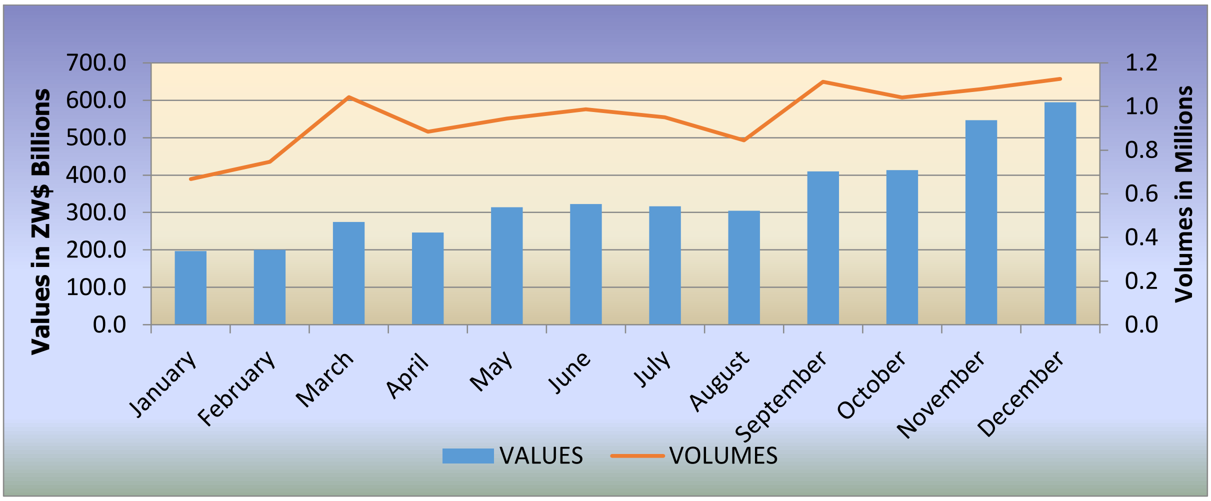
TRANSACTION VOLUMES IN MILLIONS							
MONTH	RTGS	ATM	POS	Mobile	Internet	Total Volumes	Total Change
Jan-21	0.72	0.35	12.02	95.46	0.87	109.41	-21%
Feb-21	0.81	0.53	12.31	90.08	0.75	104.47	-5%
Mar-21	1.11	0.75	15.18	105.27	1.00	123.32	18%
Apr-21	0.95	0.61	15.18	97.25	1.04	115.04	-7%
May-21	1.03	0.66	16.51	103.71	0.99	122.91	7%
Jun-21	1.08	0.58	14.80	99.35	0.98	116.79	-5%
Jul-21	1.03	0.55	15.22	102.59	0.98	120.37	3%
Aug-21	1.05	0.48	14.39	105.30	0.96	122.17	1%
Sep-21	1.19	0.49	15.40	105.81	2.09	124.99	2%
Oct-21	1.11	0.43	18.21	107.29	2.34	129.39	4%
Nov-21	1.14	0.48	17.44	99.31	2.32	120.69	-7%

TRANSACTION VOLUMES IN MILLIONS							
MONTH	RTGS	ATM	POS	Mobile	Internet	Total Volumes	Total Change
Dec-21	1.22	0.52	20.03	106.43	2.58	130.78	8%
TOTAL YTD	**12.44**	**6.43**	**186.68**	**1,217.85**	**16.91**	**1,440.32**	
Proportion	**0.9%**	**0.4%**	**13.0%**	**84.6%**	**1.2%**	**100.0%**	

Real Time Gross Settlement System (RTGS)

6.4 Real Time Gross Settlement (RTGS) system cumulative total transactions of 12 million were valued at ZW$4.95 trillion in 2021.

Figure 18: RTGS Values and Volumes for the Year 2021



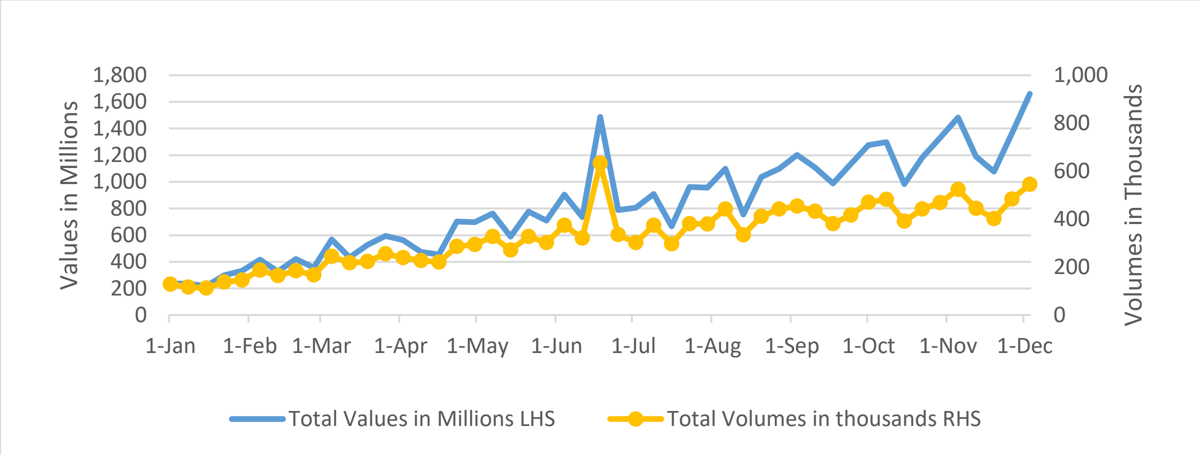
Interoperability

6.5 The implementation of Statutory Instrument 80 of 2020 on interoperability brought convenience to the transacting public in the movement of funds across players in the face of the coronavirus pandemic. This continued to be underpinned by sustained growth in the volume and value of electronic payment transactions (see Figure 17).

6.6 The interoperability transaction values processed increased significantly from ZW$105 million in 2020 to ZW$1.48 billion as at the end of 2021.

6.7 The Figure below provides monthly graphical comparison of the interoperability transactional activities for the year, from January to December 2021.

Figure 19: Mobile Money Interoperability Volumes and Values from January to December 2021



Payment Systems Risk Analysis

6.8 Risks from the payment systems pertaining to clearing, securities and settlement in the period under review, remained unchanged with medium probability of occurrence and impact in 2021.

6.9 The inherent security risk of retail payments increased in the advent of digitisation and emerging cyber security risks during the period under review. The probability and impact of the risk heightening in 2022 is, however, medium.

6.10 The Bank will continue to monitor risks to the national payment system. Specifically, cyber security and money laundering, will be monitored accordingly under the risk-based framework in place. To ensure sustained stability, the authorities will continue to identify and monitor market developments as well as any other pertinent risks.

Oversight

6.11 During the period under review, the Bank evaluated self-assessments for compliance of seven payment systems providers against the 24 Principles of Financial Market Infrastructures [PFMIs] (core payment systems standards under the Bank for International Settlements (BIS)).

6.12 Positive technical compliance with the standards has been registered by the majority of the institutions over the past six years of implementation. There is need, however, for improvement in the application of some key standards such as the stress testing for participant banks and participant default procedures.

Anti-Money Laundering and Counter Financing of Terrorism (AML-CFT)

6.13 The supervisory efforts over the year, applying the risk-based approach, covering off site analysis and onsite examinations, had a positive effect on compliance and hence promoted awareness of AML/CFT obligations and ML/TF risks among the market players. This is expected to contribute significantly to the financial stability discourse through mitigating against adverse effects of criminal economic activity which have the potential of destabilising the financial sector.

6.14 Recommendations to players were made to enhance structural governance arrangements and application of the risk-based approach across the financial institutions' products.

SADC-RTGS System[3]

6.15 The Region through the SADC Bankers Association embarked on the implementation of a number of key initiatives pertaining to the regional payment, clearing and settlement systems including the Mobile Initiated Low Value Credit Transactions Cleared on an Immediate Basis (TCIB). The TCIB output will settle in the SADC-RTGS.

6.16 The TCIB retail payments initiative aims at creating an efficient, safe, harmonised and integrated payments system in the SADC region, to further reduce cross-border remittance costs across the SADC region as well as to enhance financial inclusion.

6.17 The soft launch and testing of TCIB were successfully completed between Zambian and Zimbabwean banks. The results will help the project to be replicated across the regional member states.

6.18 The regional payment systems and integration project is expected to enhance the current national efforts to formalise cross border small payments, and hence

---

[3] SADC-RTGS (formerly known as SIRESS) is the regional cross-border interbank settlement system in the SADC region.

improving on the accountability and monitoring of international remittances. The project is also critical for both regional and domestic financial stability.

SWIFT Customer Security Controls Framework[4]

6.19 In view of the heightened digitalisation, leading to increased interconnectivity between systems and institutions, the rise of cyber risk is another potential threat to domestic financial stability. Cognisant of that, the SWIFT Customer Security Controls Framework (CSCF) is being implemented with mandatory and advisory security controls for SWIFT users.

6.20 The CSCF Assessment status for Zimbabwean banks is shown in the Table below.

Table 15: CSCF Assessment Status as at 31 December 2021

Zimbabwean Banks	No of Bank Identifier Codes	Proportion
Compliant	19	68%
No valid attestation	6	21%
Not compliant	3	11%
Total	28	100%

6.21 The Bank will continue to monitor the implementation process and ensure full compliance with the SWIFT-CSCF by the banking community on the agreed timelines.

ISO 20022

6.22 The adoption of ISO 20022, an international standard for payments messaging being driven by SWIFT alongside major central banks worldwide, is equally receiving due attention within the local banking community.

6.23 The banking sector is expected to migrate by third quarter of 2022 well ahead of the globally set deadline of October 2023. This will assist in achieving the following core objectives:

i. greater interoperability;

ii. elimination of barriers impeding seamless automation capabilities; and

[4] The SWIFT Customer Security Controls Framework (CSCF) is a set of mandatory and advisory security controls for SWIFT users. The mandatory security controls establish a security baseline for the entire community. They must be implemented by all users on their local SWIFT infrastructure.

iii. end-to-end transportation of richer data eliminating the need for translation or truncation.

6.24 This will also enable compliance with latest international best practices and standards, such as those related to AML/CFT, subsequently easing automated processing and improving the speed and efficiency of cross-border payments.

7. AML/CFT SURVEILLANCE INITIATIVES

7.1 Measures implemented by the country since being "grey-listed" resulted in a provisional determination by the FATF, at its October 2021 plenary, that Zimbabwe had addressed all the key deficiencies as required.

7.2 In line with its procedures, the FATF undertook an onsite assessment in January 2022 and confirmed the progress made by the country in implementation of AML/CFT recommended measures. In March 2022 the country was removed from the "grey-list".

7.3 The development is expected to enhance confidence in Zimbabwe's financial system and contribute positively to financial stability. The development is also expected to improve local banks' ability to establish new correspondent banking relationships and to maintain existing ones. Some Zimbabwean companies, however, remain on the USA OFAC[5] sanctions list and this may still continue to hamper correspondent banking relationships.

7.4 As part of addressing the deficiencies listed by the FATF, Zimbabwe has put in place a robust Risk Based Supervision framework to ensure that financial institutions comply with AML/CFT standards as prescribed by the country's laws and the FATF Forty Recommendations.

[5] The Office of Foreign Assets Control is a financial intelligence and enforcement agency of the U.S. Treasury Department. It administers and enforces economic and trade sanctions in support of U.S. national security and foreign policy objectives.

8. OUTLOOK AND FINANCIAL STABILITY ENHANCEMENTS

8.1 Foreign exchange, inflation, and cyber risks are expected to remain elevated in the next 12 months given the high foreign currency demand, the global and domestic inflationary pressures as well as increased migration to digital banking models by financial institutions.

8.2 Shocks arising from the spill over effects of the Russia-Ukraine conflict have the potential of negatively affecting the operating environment through supply chain disruptions which may lead to further increases in energy and food prices.

8.3 The vaccination momentum to contain the Covid-19 pandemic and restoration of normal business activities through easing of restrictions is expected to mitigate risks to financial stability through an improving macroeconomic environment.

8.4 Meanwhile, financial sector regulators are pursuing various policy initiatives to promote and maintain financial stability in the outlook period.

Banking Sector

8.5 The Bank is developing a Macro-prudential Policy aimed at facilitating containment of systemic vulnerabilities in the economy. Effective assessment of systemic risk, and deployment of the macro-prudential toolkit will be key success factors, while strong institutional and governance frameworks will be essential for the effective conduct of macro-prudential policy.

8.6 To achieve its goals, the Macro-prudential Policy will be supported by strong supervision and enforcement.

8.7 The Bank will also broaden its stress testing framework to cover macro-stress testing aspects incorporating linkages between the banking sector, macroeconomic developments or other external shocks, and financial market prices or real estate prices.

8.8 Further, the operationalisation of an enhanced Contingency Planning and Systemic Crisis Management Framework is expected to boost financial stability institutional arrangements, strategies, and processes necessary for the management and containment of a financial crisis.

8.9 Globally, sustainable banking practices are increasingly becoming the future in banking as highlighted by the shift towards adoption of sustainable banking practices aimed at contributing to the development of, as well as mobilising mainstream finance to support the transition towards a sustainable economy.

8.10 In an effort to drive the adoption of sustainability in the banking sector, the Bank adopted a central bank led model in the adoption and implementation of sustainability standards. As part of the efforts to promote the implementation of sustainability standards in banking sector processes, banks have been requested to integrate sustainability principles, covering environment and climate related issues, into their corporate governance and risk management frameworks and practices.

8.11 Cognizant of the impact of climate related physical and transitional risks on the banking sector through macro and microeconomic transmission channels, and in pursuance of its mandate to promote financial stability, the Bank has initiated a process of collaboration with various stakeholders responsible for climate risk management.

8.12 To combat the rising risk of cyber-attacks in the increasingly digital environment, the Bank is conducting a structured assessment of the banking sector's readiness to prevent, detect and respond to cyber-attacks. The results of the cybersecurity maturity assessments will inform policy going forward.

8.13 Further, the Bank is in the process of rolling out the implementation of the Basel III liquidity framework, which will promote banking institutions' resilience to severe liquidity stress. The Bank is also in the process of recalibrating its early warning and failure prediction models to take into account current economic developments. The models will be used to identify banking institutions that are likely to be in distress in the next twelve months.

8.14 The Bank will continue to support Fintech innovations through the Regulatory Sandbox (the Sandbox) which was launched in March 2021. The growing interest in the Fintech space is expected to continue with more registrations on the Sandbox expected in 2022.

Capital Markets Initiatives

8.15 The Securities and Exchange Commission of Zimbabwe will be undertaking the following initiatives in the outlook period, as part of efforts to promote financial stability:

i. development of a framework for the determination of Systemically Important Financial Institutions in the capital markets and requisite regulatory requirements;

ii. development and refinement of the risk-based capital adequacy framework to promote proactive monitoring and identification of cases of financial insolvency and other risks to Financial Market Infrastructures;

iii. adoption of the IOSCO Principles for Financial Market Infrastructures (PFMI): The standards require Financial Market Infrastructures to maintain sufficient financial resources to cover their exposures arising from the default of one or two clearing members; and

iv. development of a stress testing methodology for the capital markets sector.

Insurance and Pensions Industry

8.16 The Insurance and Pensions Commission issued the following guidance to members:

i. directive on Dissolutions to facilitate orderly exit of dormant and unviable funds from the industry for the protection of members; and

ii. Investment Guidelines to facilitate diversification of pension fund investments by allowing the pensions industry to invest 15% of their assets offshore as a way of managing risk.

Financial Markets Infrastructure

8.17 The national payment systems sector is projected to remain robust in the outlook period.

8.18 The Reserve Bank has commenced a process to review the **National Payment System Act [*Chapter: 24:23*]** with the view to enhance safety and security of digital transactional activities on the various payment platforms. Other planned initiatives in the sector include:

i. continuous review of the regulatory framework to embrace new developments and innovations;
ii. capacity building through upskilling staff competencies in anti-money laundering and counter financing of terrorism; and
iii. ensure effective cyber security measures are implemented and enforced to reduce inherent risks.

APPENDICES

Appendix 1: Macroeconomic Indicators for Zimbabwe

	2016	2017	2018	2019	2020	2021(Est)
REAL SECTOR						
Real GDP at 2012 Market prices (ZW$' m)	181,923.9	190,491.6	199,681.3	187,412.4	177,519.8	191,297.5
Nominal GDP at Market (US$'m up to 2016)	20,548.7	22,040.9	36,921.3	187,412.4	1,157,099.9	2,987,130.5
GDP at Market Prices % changes	0.8	4.7	4.8	-6.1	-5.3	7.8
GDP per capita	12,400.9	12,681.2		11,890.6	71,649.8	180,476.7
PRICES						
Month-on-Month (end period) %	-0.11	0.06	0.53	9.03	16.55	4.22
Annual Inflation (end period) %	-2.50	-0.93	3.46	42.10	521.15	348.59
Annual Inflation (period average) %	-2.41	-1.56	0.90	10.60	255.29	557.21
EXTERNAL SECTOR						
Trade Balance (US$m)	-2113.5	-1262.6	-927.0	-1938.4	174.4	-139.0
Current a/c balance (US$m)	-1596.7	-697.5	-271.2	-1379.6	920.5	678.4
Current a/c balance (% of GDP)	-1.2	-7.5	5.5	4.8	1.4	0.9
MONETARY SECTOR*						
Broad Money M3 (ZW$ '000)	6,200,282.3	7,817,278.6	10,009,905.3	34,983,470.7	204,924,855.9	475,361,517.9
Domestic Credit (ZW$ '000)	8,451,438	10,697,156	14,982,345	21,168,772.4	101,159,726.3	340,286,879.8
Credit to Private Sector (ZW$ '000)	3,495,107	3,719,426	4,058,651	6,875,497.3	74,660,404.6	222,930,132.7
Credit to Parastatals (ZW$ '000)	356,235	591,301	737,587	1,048,058.5	2,578,274.2	23,865,846.5
Credit to Government (net)(ZW$ '000)	4,466,829	6,277,468	9,992,337	16,410,748.9	23,276,846.7	83,610,072.3
Nominal Minimum Lending Rate (%)	4.0	4.5	4.0	5.0	6.0	6.0
Nominal Maximum Lending Rate (%)	18.0	18.0	18.0	65.0	65.0	65.0

PUBLIC FINANCES						
Revenue excluding grants	3,502.2	4,336.5	5,533.5	22,970.7	183,039.1	3,502.2
Revenue including grants	3,502.2	4,336.5	5,533.5	22,970.7	183,039.1	3,502.2
Capital expenditure and net lending	967.5	1,826.8	2,548.0	8,710.7	54,277.1	967.5
Recurrent Expenditure	3,934.8	4,741.3	5,196.8	13,823.0	108,648.2	3,934.8
Total expenditure and net lending	4,902.2	6,568.1	7,744.8	22,533.7	162,925.3	4,902.2
Balance excluding grants	-1,400.0	-2,231.6	-2,211.3	437.0	20,113.8	-1,400.0
Balance including grants	-1,400.0	-2,231.6	-2,211.3	437.0	20,113.8	-1,400.0
POPULATION (millions)	14.7	15.0	15.4	15.8	16.1	16.6

Source: RBZ (2022)

Appendix 2: Selected Banking Sector Indicators, 2016 – 2021

	2016	2017	2018	2019	2020	2021
Capital Adequacy Ratio	24.55%	27.64%	28.22%	33.41%	34.62%	32.89%
Nonperforming Loans Ratio	7.88%	7.05%	6.92%	1.75%	0.31%	0.94%
Large Exposures to Capital	93.03%	94.78%	97.60%	35.47%	32.61%	30.88%
Return on Equity	13.36%	15.50%	26.28%	58.77%	45.54%	41.93%
Return on Assets	2.49%	2.61%	4.57%	8.99%	13.55%	11.38%
Prudential Liquidity Ratio	97.07%	98.58%	100.97%	98.31%	73.06%	64.41%

Source: RBZ (2022)