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PURPOSE OF THIS REPORT

The purpose of this Annual Report is to provide an analysis of the condition and performance of the banking sector in Zimbabwe for the year ended 31 December 2004. The report also provides an overview of the supervisory operations and activities during the period under review. Readers should note that this report is not a statutory requirement, and that it has been prepared solely for the information of the public and the Bank's various stakeholders.

GOVERNOR'S FOREWORD

Dr G Gono
The Governor

1.1 The year 2004 will be remembered as one of the most eventful years in Zimbabwe's financial services history as financial instability reared its ugly head in an unprecedented manner. The turbulent environment presented the Reserve Bank with supervisory and regulatory challenges.

1.2 Uncompromising and decisive measures were therefore taken in order to protect the safety and integrity of the financial system and promote economic turnaround.

1.3 The measures taken by the Reserve Bank of Zimbabwe to restore sanity in the banking sector have yielded immense gains, but not without adverse consequences on some institutions which had deep rooted structural and operational deficiencies. As at 31 December 2004, nine banking institutions had been placed under curatorship, while liquidation proceedings had been instituted against three financial institutions.

1.4 As I highlighted in my maiden Monetary Policy Statement of 18 December 2003, history is yet to record a turnaround case without pain. Indeed, pain and anguish were felt by various stakeholders. Though such pain is undesirable, it has been a necessary and inevitable step towards self-correction and realisation of the noble goals to which we have committed ourselves in ensuring the return of stability to the banking sector.

1.5 Financial institutions occupy a position of special trust in the national economy. As such, corporate discipline is of paramount importance in cultivating and maintaining public confidence in the safety, integrity and stability of the financial services system. Events that unfolded in the year under review served to underscore the importance of sound corporate governance practices and risk management systems in ensuring lasting stability of our financial sector.

GOVERNOR'S FOREWORD

CONTINUED

1.6 The challenges that were witnessed in 2004 as a result of poor corporate governance and the undertaking of non-permissible activities reflect the extent to which corporate indiscipline had taken root in our financial institutions. As regulatory authorities we have committed ourselves to ensuring that such indiscipline is arrested and not allowed to gain any more foothold in our financial institutions going forward.

1.7 As custodians of public funds, financial institutions must exhibit impeccable integrity and professionalism in their conduct so as to instill good corporate culture and governance within the organisation. The challenge therefore falls upon the shoulders of management and directors of financial institutions to prove to the public that they are worthy of the trust reposed in them as custodians of public funds.

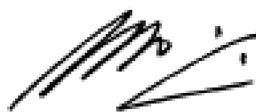
1.8 The Reserve Bank shall continue to discharge its regulatory mandate with commitment and impartiality in safeguarding the soundness of the financial system and the interests of all stakeholders. In order to foster professionalism and adherence to prudent practice by market players the Reserve Bank continues to issue guidance to the market in line with international best practice. As such, where it is not possible to restore soundness, a troubled banking institution shall be allowed to fail.

1.9 As has been the practice, measures shall always be taken to minimise loss of public confidence in the banking system and the impact of institutional failure on the economy as a whole.

1.10 I take this opportunity to thank all stakeholders for the support rendered to the Reserve Bank in the discharge of its statutory mandates. This includes government, directors and management of financial institutions, external auditors and the general public.

1.11 As we prepare to take on the challenges that lie ahead of us, let us all be driven by a sense of collective responsibility for the success of our national objectives.

1.12 As regulatory authorities, we shall also remain resolute in executing our mandate, and as I remarked in my maiden Monetary Policy Statement, failure is not an option.



Dr G Gono
Governor

DEPUTY GOVERNOR'S REMARKS

Dr C L Dhliwayo
Deputy Governor

1.1 Throughout 2004, the Reserve Bank's Bank Licensing, Supervision & Surveillance Division remained resolute and focused in its efforts to instill market discipline, promote financial stability, and bring sanity in the financial sector. The Reserve Bank answered the clarion call to be vigilant against the background of liquidity and corporate governance problems then prevailing in the banking sector.

1.2 In order to expeditiously resolve the challenges in the banking sector the Reserve Bank tailored its supervisory approaches to the developments in the banking sector as well as the wider economy. To this end, a number of prudential measures were instituted in order to correct the risk management and corporate governance flaws that were identified and to guide the industry towards relative stability.

1.3 The prudential measures introduced ranged from allocation of capital for market and operational risks; credit assessment of banks by external credit rating agencies; issuance of guidelines on corporate governance and internal audit standards; annual evaluation of board performance; prescription of new capital levels; enhancement of consolidated supervision; to reinforcement of risk-focused supervision. As part of these measures the Reserve Bank also started to work on refining its early warning systems and macro-prudential indicators.

1.4 We are confident that these measures will facilitate the timely identification of incipient distress in the banking sector. The pro-active measures being taken will go a long way to minimise the contagion effect of bank failures.

1.5 It should, however, be noted that notwithstanding the challenges experienced in 2004, the banking sector continue to grow in sophistication and spectrum of financial services offered. Regardless of the decline in the number of banking institutions in the banking sector over the year, from forty (40) to

DEPUTY GOVERNOR'S REMARKS

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twenty nine (29), the industry has shown considerable resilience. Banking institutions have become more cautious and prudent in the nature and magnitude of the risks they are prepared to assume.

1.6 The general outlook for the sector is moderately positive in view of the adequate capitalisation, sound risk management systems, satisfactory asset quality and earnings positions in most institutions. It is expected that the banking industry will, in the medium to long-term, further benefit from the process of implementing Basel II.

1.7 The Reserve Bank is already putting in place structures and systems to properly manage the gradual adoption of the three pillars of the Basel II framework. The adoption of Basel II will see an improvement in information systems, risk measurement and management, internal risk models, corporate governance, and financial disclosures.

1.8 Finally, on behalf of the Reserve Bank and the Bank Licensing Supervision & Surveillance Division, I wish to express our appreciation for the cooperation from all stakeholders in the banking sector in our turnaround efforts. We also want to acknowledge many banking institutions that have taken measures that go beyond the minimum requirements in order to strengthen their own systems thereby contributing to the overall safety and soundness of the banking sector.

Dr C L Dhliwayo
Deputy Governor

DIVISION CHIEF'S PREVIEW

Mr N Mataruka
Division Chief Bank Licensing, Supervision & Surveillance

1.1 The Bank Licensing Supervision & Surveillance (BLSS) Division executes the Reserve Bank's prudential and regulatory mandate in order to ensure safety, soundness and stability of the financial system. Financial sector stability, regulatory and supervisory issues have become a matter of increasing concern among policy makers, market practitioners and the public at large.

1.2 The year 2004 saw a number of banking institutions facing serious liquidity and solvency challenges, which emanated from, among others, poor risk management systems and weak corporate governance practices. Against this background, and in line with the Division's mission "... to promote and maintain the safety and soundness of the financial system through proactive and rigorous regulation and supervision of financial institutions in line with international best practice", the Reserve Bank instituted a number of measures in order to restore normalcy and stability in the financial sector.

1.3 The major supervisory highlights, during the course of 2004 relate to regulatory reforms, licensing and de-registration of financial institutions, risk-based supervision and the issuance of a number of guidelines on prudential matters.

1.4 The Reserve Bank placed three financial institutions under liquidation while nine other banking institutions were put under curatorship. As a result the number of operating banking institutions declined from 40 as at 31 December 2003 to 29 as at 31 December 2004. By year-end, the banking sector comprised of 11 commercial banks, five (5) merchant banks, five (5) discount houses, four (4) finance houses and four (4) building societies.

1.5 In 2004, the Reserve Bank took over the regulation and supervision of non-bank financial institutions and consolidated the licensing and supervision of banks in terms of the Financial Laws Amendment Act No. 16 of 2004. The new arrangement helps to promote effective supervision of financial institutions and minimise regulatory arbitrage.

1.6 In addition, year 2004 saw the promulgation of the Asset Management Act [Chapter 24:26] and

DIVISION CHIEF'S PREVIEW

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the Troubled Financial Institutions (Resolution) Act [Chapter 24:28]. The Troubled Financial Institutions (Resolution) Act was passed in parliament in December 2004 and became law in January 2005. These statutes provided the legal framework for the prudential supervision of asset management companies as well as the meticulous treatment of troubled financial institutions respectively.

1.7 In a bid to promote good corporate governance practices, instill market discipline, enhance risk management systems and internal controls in banking institutions, the Reserve Bank issued the following guidelines which have been widely adopted by the banking sector: Guideline No. 01-2004/BSD - Corporate Governance, Guideline No. 02-2004/BSD - Internal Audit Standards, and Guideline No. 04-2004/BSD - Accreditation of Rating Agencies.

1.8 As part of these measures the Reserve Bank enhanced its supervision and surveillance over corporate governance systems and structures in the banking sector. In particular, emphasis was placed on separation of ownership and management, appointment of independent non-executive directors, and the appointment of fit and proper persons to positions of responsibility and accountability. Resultantly, a banking institution's board is required to conduct annual peer and self evaluation of the board as a whole, its committees and the contribution of each director including the chairman.

1.9 Furthermore, as part of its efforts to maintain a strong and vibrant banking sector, the Reserve Bank prescribed new minimum capital requirements in January 2004, which became effective on 30 September 2004.

1.10 The Reserve Bank also implemented a new information technology known as Banking Supervision Application (BSA), with effect from October 2004. The BSA system automates the submission of statutory returns and facilities effective assessment of banking institutions' financial condition as well as maintenance of accurate banking supervision data. The system was installed as part of the Southern African Development Community (SADC)/East and Southern Africa Banking Supervisors Group (ESAF) information technology harmonisation project.

1.11 Banking Supervision is increasingly becoming a knowledge based profession. As such BLSS strives to keep its supervisory techniques in line with international best practice. During the year under review, BLSS recruited additional staff members to create a complement with a skills mix spanning various faculties including legal, banking, finance, accounting, economics, financial modelling and IT.

1.12 Going forward, the impending implementation of Basel II capital framework will also uplift the standard of supervision and banking practices in Zimbabwe to internationally accepted norms.

1.13 As the Governor has already remarked, failure is not an option. We remain resolute in our quest for lasting stability in the financial sector.

N Mataruka
Division Chief

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SUPERVISORY APPROACHES

1.1 INTRODUCTION

1.1.1 In fulfilling its regulatory mandate, the Reserve Bank of Zimbabwe has an obligation to ensure the sustained safety, soundness, and stability of the financial system through the effective regulation and supervision of institutions that fall under its jurisdiction.

1.1.2 Pursuant to the objective of ensuring financial stability, the Reserve Bank employs a variety of supervisory approaches in line with international best practice. BLSS has adopted recommendations of the Basel Committee on Banking Supervision such as the 1988 Capital Accord as amended in 1996 and the 25 Core Principles for Effective Bank Supervision.

1.1.3 Banking institutions are on their part expected to muster certain competancies and key success factors to survive competitive pressures on the market.

1.2 KEY SUCCESS FACTORS IN THE BANKING SECTOR

Adequate Capital…

1.2.1 Capital offers banking institutions with protection in two principal ways: absorption of losses and maintenance of confidence in a bank.

1.2.2 The level of capitalisation, apart from indicating a bank's level of solvency, also determines the capacity of the banking institution to underwrite business.

Risk Management…

1.2.3 Banks should be fully committed to sound risk management standards and practices encompassing the following, among others:

a) risk management policies and procedures consistent with the bank's vision and business strategies;
b) bench marks and limits to guide the bank's risk appetite;
c) strong Management Information System (MIS) for reporting, monitoring and controlling risks;
d) independent checks and balances to ensure compliance with internal and external prudential requirements; and
e) enterprise-wide risk management approach.

Corporate Governance…

1.2.4 The board of directors and management of a banking institution need to establish and maintain adequate and effective processes of corporate governance, which are consistent with the nature, complexity and risks inherent in the activities and the business of the banking institution.

1.2.5 The process of corporate governance should be established with the objective of achieving the banking institution's, or bank holding company's strategic and business objectives efficiently, effectively, ethically and equitably.

Information Technology…

1.2.6 Continuing technological developments and innovations have revolutionalised the way banks interact with their customers, suppliers and counter parties, and execute their functions.

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1.2.7 Banking institutions should have robust Information Technology Systems that adequately support the business operations.

Staff training and capacity building…

1.2.8 Human resources issues such as capacity building, staff training and succession planning are critical for effectiveness and continuity.

1.2.9 In terms of the Banking Act [Chapter 24:20] as read with section 5 of the Banking regulations S.I.205/2000, every banking institution is required to appoint suitably qualified and experienced officers to be responsible for:

a) risk management;
b) lending and credit administration;
c) operations and internal controls;
d) investments and asset/liability management;
e) treasury and foreign exchange operations; and
f) trust and fiduciary operations, where a bank proposes to engage in these activities.

Regulatory and ethical compliance…

1.2.10 A financial institution should hold itself to high standards when carrying on business and at all times strives to observe the spirit and the letter of the law. Compliance goes beyond what is legally binding and embraces broader standards of integrity and ethical conduct. Failure to do the right (ethical) thing may give rise to compliance risk and hence attract regulatory sanctions, material financial loss and loss to reputation.

1.2.11 Failures in compliance can be a real threat to the future of any corporate. The adoption of compliance mechanisms (including ethical compliance mechanisms embracing core values of integrity) contributes to stability and growth and thus helps to build corporate image and reputation; gaining loyalty and trust from stakeholders including consumers and employees, hence creating competitive advantage. Commitment to quality objectives such as compliance with the law and high ethical standards results in organisational achievement.

1.2.12 The main supervisory approaches employed by the Reserve Bank include the following:-

1.3 LICENSING OF FINANCIAL INSTITUTIONS

1.3.1 Supervision and regulation of financial institutions commences at the licensing of the institution. In this regard the Reserve Bank has put in place a comprehensive licensing framework aimed at ensuring that only potentially strong institutions are allowed to enter the financial system. This ensures financial stability and minimises the cost of problem bank resolution.

1.3.2 The licensing function entails evaluation of proposals to set up operations by new institutions, mergers and acquisitions as well as the evaluation and approval of cross border investments.

1.3.3 The evaluation includes, among others:

a) viability of the business and potential contribution to the financial system;
b) source and adequacy of capital as well as shareholders' capacity to inject more capital;
c) fit and proper tests on directors, management and significant shareholders;

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d) competence of management;
e) adequacy of the risk management systems; and
f) adequacy of internal control systems and sound corporate governance practices.

1.3.4 Where the proposed owner is a foreign bank, the licensing process requires prior consent of, and information sharing with, the home country supervisor.

1.3.5 Prior to commencement of banking activities, the Reserve Bank conducts a pre-opening inspection to determine the bank's readiness to commence operations. The primary focus of the inspection is to determine the adequacy of risk management systems and infrastructural facilities in place.

1.4 CAMELS RATING SYSTEM

1.4.1 The Reserve Bank has adopted the internationally recognised CAMELS rating system in the evaluation of the performance and condition of banking institutions. CAMELS is an acronym for Capital Adequacy, Asset Quality, Management, Earnings, Liquidity and Sensitivity to market risk.

1.4.2 The standardised rating system also facilitates the identification of those institutions whose financial, operational, managerial or compliance weaknesses require special supervisory attention and/or warrant a higher than normal degree of supervisory concern. The rating system, therefore, is an important tool in promoting financial stability.

1.4.3 The ratings are assigned to each of the six components and then an overall or composite rating is assigned. Ratings are on a scale of 1 to 5 with respect to safety and soundness. The CAMELS components are analysed as follows:

Capital Adequacy…

1.4.4 Financial institutions are expected to maintain capital levels commensurate with their risk profiles and the strength of management.

1.4.5 Capital adequacy is evaluated in relation to:
a) the level and quality of capital and the overall financial condition of the institution;
b) nature, trend and volume of problem assets;
c) volume of risk assets (both on and off balance sheet);
d) bank's growth experience, plans, and prospects;
e) access to capital markets and other sources of capital;
f) quality and strength of earnings; and
g) managements' ability to address the foregoing.

Asset Quality…

1.4.6 Asset quality is a function of the quantity of existing and potential credit risk associated with the loan and investment portfolios, other assets and off-balance sheet transactions.

1.4.7 A financial institution's asset quality is evaluated in relation to:
a) the level, distribution, severity and trend of problem, classified , non-accrual, restructured, delinquent and non-performing assets for both on and off-balance sheet transactions;
b) the adequacy of underwriting standards,

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soundness of credit administration practices and appropriateness of risk identification practices;

c) the adequacy of provisions for bad and doubtful debts;

d) demonstrated ability to administer and collect problem credits;

e) concentration of credit, trend, level of non-performing insider loans;

f) the volume and nature of credit documentation exceptions; and

g) the adequacy of internal controls and management information systems.

Management…

1.4.8 Management's performance is evaluated against virtually all factors considered necessary to operate the bank within accepted banking practices and in a safe and sound manner.

1.4.9 The capability and performance of management and the board of directors is rated based on assessment of, *inter alia:*

a) technical competence, leadership and administrative ability;

b) compliance with banking laws, regulations and supervisory guidelines and directives as well as ethical standards and international best practice;

c) ability to plan and respond to changing circumstances;

d) adequacy of and compliance with internal policies;

e) demonstrated willingness to serve the legitimate banking needs of the community;

f) strong governance between shareholders and management; and

g) staff efficiency and productivity.

Earnings…

1.4.10 Earnings are evaluated in relation to quantity, trend, sustainability and quality of the institution's earnings.

1.4.11 The following factors, among others, are considered in the rating of earnings:

a) ability to cover losses and provide for adequate capital;

b) the level of earnings, including trends and stability;

c) peer group comparisons;

d) the adequacy of budgeting systems, forecasting processes and management information systems in general;

e) the adequacy of provisioning; and

f) exposure of earnings to market risk.

Liquidity and Funds Management…

1.4.12 Liquidity and funds management are evaluated in relation to:

a) the overall effectiveness of asset and liability management;

b) trend , stability and diversity of deposits base;

c) existence and adequacy of contingency funds;

d) reliance on interest sensitive funds and frequency and level of borrowings;

e) volume of off-balance sheet activities;

f) technical competence relative to structure of liabilities;

g) availability of assets readily convertible to cash without undue loss; and

h) access to money markets or other ready sources of cash.

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Sensitivity to Market Risk…

1.4.13 The sensitivity to market risk component reflects the degree to which changes in interest rates, foreign exchange rates, commodity prices, or equity prices can adversely affect a financial institution's earnings or economic capital.

1.4.14 Sensitivity to market risk is evaluated in relation to:

a) management's ability to identify, measure, monitor and control exposures to market risk;
b) the nature and complexity of interest rate risk exposures arising from non-trading positions; and
c) the sensitivity of the financial institution's earnings or the economic value of its capital to adverse changes in market risk.

Composite Rating…

1.4.15 Under the CAMELS system, each financial institution is assigned a composite rating based on an evaluation and rating of six essential components of its financial condition and operations. These component factors address the adequacy of capital, quality of assets, capability of management, quality and level of earnings, adequacy of liquidity, and sensitivity to market risk. Evaluations of the components take into consideration the institution's size and sophistication, the nature and complexity of its activities, and its risk profile.

1.4.16 Composite and component ratings are assigned based on a 1-to-5 numerical scale. A "1" is the highest rating, indicating the strongest performance and risk management practices and the least degree of supervisory concern. A "5" is the lowest rating, indicating the weakest performance, inadequate risk management practices, and the highest degree of supervisory concern.

1.4.17 The composite rating generally bears a close relationship to the component ratings assigned. However, the composite rating is not derived by computing an arithmetic average of the component ratings. Each component rating is based on a qualitative analysis of the factors that make up that component and its interrelationship with the other components. When assigning a composite rating, some components may be given more weight than others depending on the situation at the institution.

1.4.18 In general, assignment of a composite rating may incorporate any factor that bears significantly on the overall condition and soundness of the financial institution. Assigned composite and component ratings are disclosed to the institution's board of directors and senior management. The ability of management to respond to changing circumstances and address the risks that may arise from changing business conditions or the initiation of new activities or products is an important factor in evaluating a financial institution's overall risk profile, as well as the level of supervisory attention warranted. For this reason, the management component is given special consideration when assigning a composite rating.

1.4.19 Financial institutions with a **composite 1 rating** are sound in every respect and generally have

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components rated 1 or 2. Any identified weaknesses are minor and can be handled routinely by the board of directors and management. These financial institutions are the most capable of withstanding fluctuating business conditions and are resistant to outside influences, such as economic instability in their trade area. These institutions are in substantial compliance with laws and regulations. As a result, they exhibit the strongest performance and risk management practices relative to their size, complexity, and risk profile, and give no cause for supervisory concern.

1.4.20 Financial institutions with a **composite 2 rating** are fundamentally sound. For a financial institution to receive this rating, generally none of its component ratings should be more severe than 3. Only moderate weaknesses are present, and the board of directors and management are capable of and willing to correct them. These financial institutions are stable, can withstand business fluctuations, and are in substantial compliance with laws and regulations. Overall risk-management practices are satisfactory relative to the institution's size, complexity, and risk profile. There are no material supervisory concerns and, as a result, the supervisory response is informal and limited.

1.4.21 Financial institutions with a **composite 3 rating** exhibit some degree of supervisory concern in one or more of the component areas. These institutions have a combination of moderate to severe weaknesses; however, the magnitude of the deficiencies generally will not cause a component to be rated more severely than 4. Management may lack the ability or willingness to effectively address weaknesses within appropriate time frames. Financial institutions in this group generally are less capable of withstanding business fluctuations and are more vulnerable to outside influences than those institutions rated a composite 1 or 2. Additionally, these financial institutions may be in significant non-compliance with laws and regulations. Risk management practices may be less than satisfactory relative to the institution's size, complexity, and risk profile. These financial institutions require more than normal supervision, which may include formal or informal enforcement actions. Failure of the institution appears unlikely, however, given its overall strength and financial capacity.

1.4.22 Financial institutions with a **composite 4 rating** generally exhibit unsafe and unsound practices or conditions. They have serious financial or managerial deficiencies that result in unsatisfactory performance. The institution's problems range from severe to critically deficient, and weaknesses and problems are not being satisfactorily addressed or resolved by the board of directors and management. Financial institutions in this group generally are not capable of withstanding business fluctuations. There may be significant non-compliance with laws and regulations. Risk-management practices are generally unacceptable relative to the institution's size, complexity, and risk profile. Close supervisory attention is required, which means formal enforcement action is necessary in most cases to address the problems. Institutions in this

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group pose a risk to the deposit insurance fund. Failure of the institution is a distinct possibility if the problems and weaknesses are not satisfactorily addressed and resolved.

1.4.23 Financial institutions with a **composite 5 rating** exhibit extremely unsafe and unsound practices or conditions. Their performance is critically deficient and risk-management practices are inadequate relative to the institution's size, complexity, and risk profile. These institutions are of the greatest supervisory concern. The volume and severity of problems are beyond management's ability or willingness to control or correct. Immediate outside financial or other assistance is needed for the financial institution to be viable. Ongoing supervisory attention is necessary. Institutions in this group pose a significant risk to the deposit insurance fund and their failure is highly probable.

1.5 RISK-FOCUSED SUPERVISION

1.5.1 The Reserve Bank adopted risk-focused supervision in 2002 to ensure that supervisory resources and time are allocated to banking institutions and areas posing the greatest risk to financial safety and soundness.

1.5.2 Risk-focused supervision is a process that is aimed at assuring a qualitative and quantitative assessment of an institution's risk profile, and thus provides a continuous and dynamic way of supervising banks.

1.5.3 The risk-focused examination supports an analytical framework based on the following six steps:

Understanding the Institution…

1.5.4 This involves collecting information pertaining to the institution's structure and activities, the institution's financial condition, key internal control issues and outstanding past supervisory findings.

1.5.5 The information is gathered from various sources ranging from discussions with bank management, to supervisory early warning systems, offsite/onsite examination reports and market intelligence. The information is used to construct an institutional profile that provides a concise portrait of an institution's structure and activities.

Assessing the Institution's Risk…

1.5.6 The risk assessment process involves the identification of the risk inherent in a financial institution and forms the basis on which the examination may be conducted. The institution's risk assessment is a risk narrative which provides a description of the risks inherent in the bank, the adequacy of risk management controls in place and the trend of the risk. This is further summarised into a tabular risk matrix. The risk matrix identifies the type, level, and direction of risks and forms the basis of the examination.

Planning/Scheduling Supervisory Work…

1.5.7 This process involves holding pre-examination meetings with senior management, external auditors, board chairman and the internal auditor.

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This is meant to gain an understanding of management's business strategy, maximisation on synergies from other parties and obtain an assessment of risk inherent within the institution prior to preparing the Supervisory Plan.

Defining Examination Activities…

1.5.8 This stage is meant to outline specific objectives and activities of the on-site examination and determine staffing needs. This culminates in a document known as the Scope Memorandum which states the type of examination, the rationale of the examination, key areas to be inspected and time and resource allocation.

Performing On-site Examination and Reporting Findings...

1.5.9 This process involves the conduct of the examination including briefing bank management on the focus on high risk areas and risk management processes, holding supervisory meetings to ensure that the examination is proceeding as planned and ensuring that the most important issues are reported and communicated to the bank management. The final examination report is discussed with the financial institution's board of directors.

Conducting On-going Off-site Supervision…

1.5.10 After the on-site examination, examiners update the risk-focused documents such as the institutional profile and conduct ongoing follow-ups on the issues emanating from the onsite examination to ensure supervisory corrective action is being implemented and the conclusive resolution of outstanding issues.

1.6 OFF-SITE SURVEILLANCE

1.6.1 Off-site surveillance entails the analysis of the financial condition of a financial institution, utilising information submitted through periodic prudential returns and any other reliable sources of information. Other sources of information may include the stock market, credit rating agencies and market intelligence.

1.6.2 The Reserve Bank has prescribed the content and format of the prudential returns to ensure a coherent and effective analysis of the performance and condition of the banking institutions.

1.6.3 On a quarterly basis, the Reserve Bank conducts comprehensive analysis to determine the banks' performance, ascertain trends, assess compliance with statutory and regulatory requirements and identify key risk areas. Following such analysis the banks are assigned ratings using the CAMELS rating system.

1.6.4 The ratings provide the basis for the timing and nature of on-site examinations.

1.7 EARLY WARNING SYSTEM

1.7.1 The Reserve Bank, in its efforts to improve the supervision of the financial sector, has developed a comprehensive early warning system comprising financial soundness indicators, stress testing, and back testing.

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1.7.2 The system enables the Reserve Bank to detect economic weaknesses and vulnerabilities and to take pre-emptive steps to reduce the risk of bank failures and financial crises.

1.7.3 Stress tests on the stability of the banking sector and, in particular, the overall vulnerability of the financial system to exogenous and endogenous are conducted on a continuous basis.

1.8 ON-SITE EXAMINATIONS

1.8.1 On-site examinations are a critical component of the supervisory process, and may range from an examination of specific areas (targeted examination) to a comprehensive review (full scope examination) of an institution's operational activities.

1.8.2 The Reserve Bank employs on-site examinations as a means of validating supervisory information received from off-site surveillance. On-site examinations are aimed at evaluating the adequacy of risk management systems and corporate governance practices as well as compliance with regulatory requirements, the on-site examinations are tailored to the risk profile of the institutions, and institutions with higher risks are prioritised.

1.8.3 During the year under review, on-site examinations determined various deficiencies in the operations of some banks as highlighted in Chapter 3. On the basis of those findings appropriate supervisory action were taken to resolve the identified deficiencies.

1.9 CONSOLIDATED SUPERVISION

1.9.1 The Reserve Bank has adopted consolidated supervision in order to effectively supervise banking groups in the wake of financial conglomeration. As at 31 December 2004 there were twenty-two financial conglomerates under the control of bank holding companies.

1.9.2 From a prudential supervision perspective, conglomeration in the financial sector has significant implications on the conditions of banking groups' risk management systems and corporate governance practices.

1.9.3 Consolidated supervision entails a review of both banking and non-banking activities conducted by a bank holding company with a view to determining the extent to which the holding company and its subsidiaries or affiliates comply with prudential regulatory requirements.

1.9.4 Consolidated supervision also involves an evaluation of the activities of a bank holding company both on the domestic scene and international arena. This type of supervision has been instrumental in dealing with the evasion of regulations and engagement in non-permissible activities through group structures.

1.9.5 As financial entities expand their structures it becomes increasingly difficult to oversee their operations on a purely institutional or sectoral basis due to the increased complexity in corporate structures and the diverse inter-linkages therein. Monitoring the

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spillover of risks from one subsidiary to another within a banking group becomes increasingly important, yet increasingly difficult.

1.9.6 Furthermore, intra-group exposures within integrated financial institutions have the potential to aggravate the fragility of their complex structural arrangements. In view of the potential threats posed by consolidated structures to the safety of the entire financial system, it becomes paramount that banking groups have adequate management structures.

1.9.7 As noted above, consolidated supervision transcends national boundaries. As such this approach necessitates information sharing, co-ordination and co-operation among supervisory authorities. To this end, the Reserve Bank has entered into a Memorandum of Understanding with regional supervisors to share information on the condition of banks that have foreign branches.

1.10 BANK HOLDING COMPANY RATING SYSTEM

1.10.1 The Reserve Bank has adopted the Bank Holding Company (BHC) Rating System which is used as an internal rating tool that reinforces the consolidated supervision of financial groups.

1.10.2 The rating system is used to evaluate the condition and performance of banking groups. It forms the basis of supervisory responses and actions to particular issues of concern. Furthermore, the rating system lays the platform for supervisors' discussions of the group's condition with the BHC management.

1.10.3 The BHC rating system is denoted by the abbreviation RFI/C (D). The main components of the rating system represent: Risk Management (R); Financial Condition (F); and potential Impact (I) of the parent company and non-bank subsidiaries on the banking subsidiaries. While the Reserve Bank expects all bank holding companies to act as a source of strength to their banking subsidiaries, the Impact (I) rating focuses on downside risk i.e. on the likelihood of significant negative impact by the non-banking entities on the banking subsidiaries. Another rating component, Depository Institution (D), generally mirrors the regulator's assessment of the banking subsidiaries.

1.10.4 In order to provide a consistent framework for assessing risk management, the "R" component is supported by four sub-components that reflect the effectiveness of the banking organisation's risk management and controls. The sub-components are: board and senior management oversight; policies, procedures, and limits; risk monitoring and management information systems; and internal controls.

1.10.5 The "F" component is similarly supported by four subcomponents reflecting an assessment of the quality of the banking organisation's capital, asset quality, earnings, and liquidity.

1.10.6 Under the rating framework, each BHC is assigned a composite rating (C) based on an evaluation and

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rating of its managerial and financial condition and an assessment of future potential risk to its banking subsidiaries. The BHC rating system is thus an important and effective tool that enhances supervisory functions.

1.11 CORRECTIVE PROGRAMMES

1.11.1 When deficiencies are identified, supervisory response is tailored to the severity of inherent problems, unsafe and unsound practices, non-compliance with applicable laws and regulations. Prompt supervisory action is taken to restore the bank to a safe and sound condition in the shortest time possible.

1.11.2 The Reserve Bank has a comprehensive Troubled and Insolvent Bank Policy that facilitates early identification and prompt responses to banking problems. Among other things, the policy clearly defines what constitutes a "troubled" institution and spells out the regulatory options *'ex ante'*.

1.11.3 Some of the factors to consider in determining the need for and type of corrective action include answers to the following questions:

a) what is the overall condition of the bank with particular emphasis on capital adequacy, asset quality and liquidity?

b) what types of problems has the bank had in the past and was the root cause of the problem addressed? Has the severity of problems progressed?

c) is the ownership and management team the same as in the past? Are decisions made by a dominant individual? Is the board independent, knowledgeable, and informed of the bank's operations?

d) does the management team have the ability, will or expertise to fix the current problem? Is there evidence of inside abuse and/or fraud? Is there concealment or refusal to submit the bank's books, papers, records or affairs or inspection to any examiner?

e) has the bank been placed under an enforcement action before? If yes, how long ago and for what? What is the bank's history of compliance with enforcement action?

1.11.4 The Reserve Bank takes more severe action if management has failed to comply with previous directives to address identified anomalies.

1.11.5 A less severe action may be warranted if management has a proven track record, unless the problems are significant.

1.11.6 The severity of the action chosen is based primarily on the bank's current condition (i.e. composite rating and risk profile) with consideration given to the co-operation, responsiveness, and capability of board and management.

1.11.7 Banking laws provide for progressively harsher responses that may culminate in mandatory closure and liquidation of insolvent or imminently insolvent banks if rehabilitation efforts have failed or proved to be ineffective.

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1.11.8 The full range of potential supervisory tools fall within two broad categories: informal and formal enforcement actions. Formal enforcement actions are generally more severe.

1.11.9 Whatever the course of corrective action the Reserve Bank undertakes, it is in the interests not only of depositors and creditors but also of its owners and managers.

1.12 INFORMAL SUPERVISORY ACTIONS

1.12.1 Informal actions are used in "well-" or "adequately-" capitalised banks, banks with composite ratings of "1" or "2", and 3-rated banks with strong management.

1.12.2 For "1" or "2" rated banks Reserve Bank may obtain affirmative commitments for corrective action from the bank's senior management, the board of directors, and where appropriate, shareholders.

1.12.3 Banks rated "3" with strong management are considered for informal action if other circumstances suggest that the remedial measures necessary to restore the bank to a safe and sound condition are present. In addition, the capability, co-operation, integrity and commitment of the bank's management, board, and ownership are also very important considerations in the selection of appropriate action(s). Some of the informal actions are discussed below:

a) **Board Resolution** is a suggested plan for correction of deficiencies which specifies actions to be taken by board of directors and management. It states who is responsible and sets a time table and/or target levels for achievement.

b) **Commitment Letter** is similar to the above but considered a stronger supervisory response and is used for banks that pose moderate supervisory concerns. It is a formal letter drafted by the Reserve Bank and signed by the board. It outlines specific actions to be taken to address identified deficiencies and a time table for accomplishment.

c) **Memorandum of Understanding** specifies actions written by the Reserve Bank and agreed to by the board. Failure to comply will lead to subsequent enforcement action of a formal nature.

1.13 FORMAL SUPERVISORY ACTION

1.13.1 Formal actions are considered against all "4" or "5" rated banks or "3" rated banks with weak management. As noted above, the capability, co-operation and commitment of the bank's management, board and ownership structure may come into play in choosing the appropriate action.

1.13.2 Regardless of a bank's CAMELS ratings, formal actions are appropriate when significant problems threaten to harm the institution, or when informal actions are insufficient. For instance, failure to

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comply with prior supervisory actions, significant insider abuse, or significant problems in the bank's systems, controls, policies, internal audit or management information systems, may warrant formal corrective actions.

1.13.3 The following are some of the formal corrective programmes that supervisors can implement:

Corrective Orders…

1.13.4 These are formal written directives issued by the Reserve Bank on weak institutions to correct noted deficiencies. The order specifies actions, responsible parties and timetables. Bank Licensing, Supervision & Surveillance monitors compliance with all Corrective Orders and violation of provisions provides a basis for more serious sanctions. Typical Orders issued by Reserve Bank include cease and desist orders, amendment of registration, suspension of officials and banking business among others.

Order of Supervision…

1.13.5 The Reserve Bank may appoint a resident supervisor to oversee corrective actions being taken by the board and management. The board continues to have overall responsibility for supervising the bank's operations.

Capital Demand…

1.13.6 This is an order designed to direct a financial institution to recapitalise the institution to the required levels.

Merger or Consolidation…

1.13.7 This option encourages or facilitates the merger or consolidation of weak institutions with a strong and healthy institution in order to preserve market stability.

Curatorship…

1.13.8 Curatorship places the rights to control the bank in the hands of a curator appointed by the Reserve Bank. A bank may be placed under curatorship due to the following:

a) critical undercapitalisation and capital insolvency;
b) violations of law or unsafe or unsound practices that have had, or are likely to have, a substantial negative effect on the bank or weaken the institution's condition. Severe liquidity problems fall in this category; and/or
c) critical management failures of the bank: e.g. violation of a corrective order, or concealment or refusal to submit the bank's books, papers, records, or assets, or affairs for inspection to any examiner or lawful agent.

1.14 APPOINTMENT OF CURATORS

1.14.1 Curators are appointed by the Reserve Bank to take over the management of distressed institutions, investigate the problems in an institution, take remedial action, and recommend resolution of the problems in an institution.

1.14.2 Qualified and experienced professionals of high calibre and integrity are appointed as curators.

1.14.3 The curatorship period is for an initial period of up to one year, and may be extended depending on the situation.

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Duties and Powers of the Curator…

1.14.4 Placing a bank under management of a curator has the effect of suspending the powers of every director, officer and shareholder of the banking institution.

1.14.5 All legal proceedings and the execution of all writs, summonses and other legal processes are stayed. Operation of any set-off in respect of any amount owing by a creditor to the banking institution is suspended.

1.14.6 The curator takes over and assumes management of the banking institution concerned in a manner he or she deems prudent to protect the institution and its creditors.

1.14.7 Deposits and investments in a banking institution placed under curatorship may be frozen for a period not exceeding one year and no withdrawals can be made notwithstanding the provisions of any other law.

1.14.8 The curator is required to examine the affairs of the institution to ascertain whether past or present directors and employees have committed offences which render them personally liable to pay damages to the institution.

1.14.9 The curator is expected to prepare periodic reports for the Reserve Bank on the condition of the institution and possible way forward.

1.14.10 Any person who is aggrieved by any decision or action taken by the curator may appeal against it to the Reserve Bank.

1.14.11 The Reserve Bank has the right to apply to the High Court for liquidation.

CHAPTER TWO
CONDITION AND PERFORMANCE OF THE BANKING SECTOR

2.1 OVERVIEW

2.1.1 The number of operating banking institutions declined from forty (40) as at 31 December 2003 to twenty-nine (29) as at 31 December 2004, following the liquidation of two discount houses and the placement of nine other institutions under curatorship.

2.1.2 At the end of 2004, the banking sector comprised eleven (11) commercial banks, five (5) merchant banks, five (5) discount houses, four (4) finance houses and four (4) building societies.

2.2 CONSOLIDATED BALANCE SHEET STRUCTURE

2.2.1 Composition of Assets

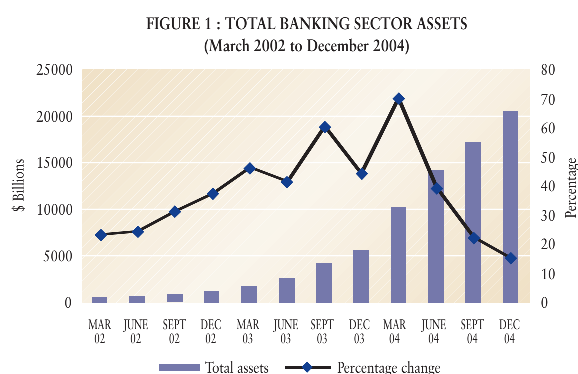
a) Total assets for the banking sector grew by 232% during the year under review from $5.99 trillion to $19.86 trillion as at 31 December 2004. This position is comparatively lower than a growth rate of 389% in banking industry assets between December 2002 and 2003.

b) As at 31 December 2004, on-balance sheet assets amounted to $17.79 trillion representing 90% of total industry assets, down from 90.21% recorded in 2003. Off-balance sheet items accounted for $2.06 trillion, which was 338% higher than the $470 billion recorded as at 31 December 2003.

c) The growth in the banking sector assets is partly reflective of the hyperinflationary environment and utilisation of productive sector facilities, which were granted to the productive sector through commercial and merchant banks.

d) Figure 1 shows total assets of the banking sector on a quarterly basis, from March 2002 to December 2004.

FIGURE 1 : TOTAL BANKING SECTOR ASSETS (March 2002 to December 2004)



e) Total assets for the sector have been on an upward trend since 2002. However, a slowdown in asset growth occurred between March 2004 and December 2004.

f) The asset growth in 2004 was spurred by a large investment in securities. Securities and investments grew by 375% from $1.10 trillion as at 31 December 2003 to $5.23 trillion as at 31 December 2004. The increase is largely attributed to the high money market interest rates that prevailed in the economy that resulted in the shift by financial institutions from loans and advances to securities and investments. The shift also reflected the cautious approach adopted by some banks towards lending in a bid to minimise credit risk against the background of relatively high interest rates during the first half of 2004.

g) Table 1 below illustrates on a comparative basis the composition of assets as at 31 December 2003 and 2004.

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Table 1: Composition of Assets

	Dec-2003	Dec-2004
Assets		
Cash and due from banks	14.61%	6.31%
Balances with RBZ	8.48%	17.98%
Foreign Claims	2.90%	4.45%
Securities & investments	18.42%	26.34%
Net loans and advances	31.40%	24.00%
Fixed assets	3.22%	2.50%
Other assets	13.11%	8.03%
Off-balance sheet items	7.87%	10.40%
Total	100.00%	100.00%

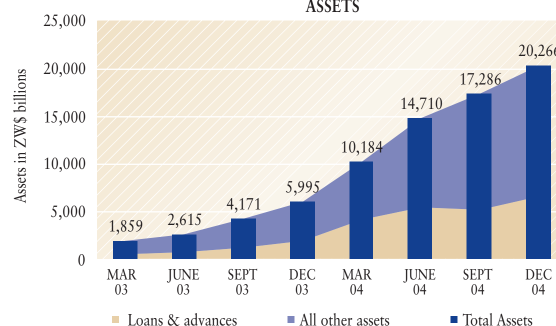
h) Balances with the Reserve Bank increased from 8.48% to 17.98% as a result of higher statutory reserve requirements introduced during the year under review, as well as the new requirement for building societies and discount houses to pay statutory reserves.

i) As at 31 December 2004, total loans and advances for the banking sector amounted to $5.42 trillion, up from $1.91 trillion as at 31 December 2003.

j) The increase in loans and advances between December 2003 and December 2004 was largely attributed to productive sector facilities that were availed at concessional interest rates to commercial and merchant banks (Figure 2 below). A total of $2.06 trillion was disbursed under the facility in 2004.

k) The proportion of loans and advances in relation to total assets, however declined by 7.4 percentage points, from 31.40% to 24.00% during the year ended 31 December 2004. The growth in loans and advances between March 2003 and December 2004 is depicted in Figure 2.

FIGURE 2: PROPORTION OF LOANS TO TOTAL ASSETS



2.2.2 Composition of liabilities

a) Deposits continued to be the major source of funding followed by capital and reserves. A year-on-year comparison of the composition of liabilities is reflected in Table 2.

Table 2: Composition of liabilities

	Dec-2003	Dec-2004
Total Deposits	47.87%	41.44%
Due to RBZ	6.93%	8.17%
Due to Financial Institutions	5.80%	6.04%
Foreign Liabilities	1.83%	2.91%
Capital and Reserves	8.60%	12.04%
Other Liabilities	21.11%	18.92%
Total on-balance sheet liabilities	92.13%	89.60%
Off-balance sheet items	7.87%	10.40%
Total Liabilities	100.00%	100.00%

b) Between December 2003 and December 2004 deposits increased from $2.86 trillion to $8.24 trillion. In percentage terms, total deposits constituted 41.44% of total liabilities, down from 47.87% in 2003.

c) The composition of deposits over the year is illustrated in Figure 3 and Table 3.

d) Demand deposits constituted 49.28 % of total industry deposits, while savings deposits accounted for 12.89%.

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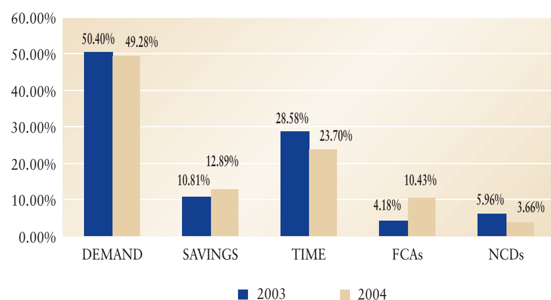
FIGURE 3: DEPOSIT STRUCTURE OF BANKS [2003 & 2004]



e) During the year under review, the proportion of time deposits to total deposits declined from 28.58% as at 31 December 2003 to 23.70% as at 31 December 2004. The decline reflects the shift by investors, from long to short term investments given the inflationary pressures that characterised the economy during the period.

Table 3: Composition of Deposits

	2003		2004	
ITEM	($ billion)	% of Total Deposits	($ billion)	% of Total Deposits
Demand Deposits	1,446.93	50.40	4,063.19	49.28
Savings Deposits	310.71	10.81	1,063.16	12.89
Time Deposits	820.15	28.58	1,954.53	23.70
FCA Deposits	120.17	4.18	860.49	10.43
NCD's	171.80	5.96	302.59	3.66
Total Deposits	**2,869.75**	**100.00**	**8,244.05**	**100.00**

f) The proportion of share capital and reserves to total liabilities increased from 8.60% in 2003 to 12.04% in 2004. The increase was largely attributed to increased capital bases following the rise in minimum capital requirements for banking institutions.

2.3 BANKING SECTOR PERFORMANCE

Capital Adequacy…

2.3.1 In order to ensure maintenance of a strong and vibrant banking sector, the Reserve Bank prescribed new minimum capital requirements on 2 January 2004 and all banking institutions were required to be compliant by 30 September 2004.

2.3.2 A total of twenty nine (29) out of forty (40) banks complied with the new requirements. Eleven (11) banking institutions faced challenges in meeting the new requirements, and had no concrete recapitalisation plans. It must be noted that out of these, seven (7) were under curatorship whilst two (2) were under provisional liquidation and the other two (2) sought and were granted dispensation to regularise their capital positions before 31 December 2004.

2.3.3 An analysis of capital adequacy for the year ended 31 December 2004 revealed that total capital and reserves held by the banking sector amounted to $2.39 trillion, compared to $512.63 billion at the end of December 2003. The average capital adequacy ratio of the banking sector was 54.18%, compared to 20.07% as at 31 December 2003.

2.3.4 The sharp increase in the capital adequacy ratio was attributed to growth in total capital (421.75%) due to capital injections noted above and the shift to securities and investments which have a lower risk weighting. Tier 1 capital remained the major component of regulatory capital as depicted in figure 4 below.

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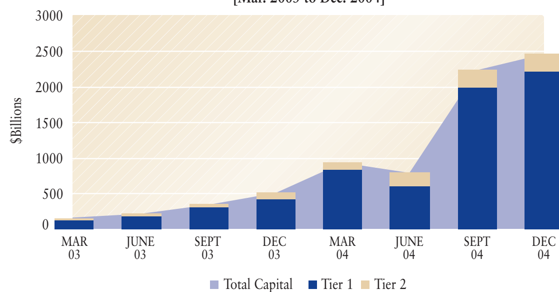

FIGURE 4: CAPITAL LEVELS [Mar. 2003 to Dec. 2004]

Asset Quality...

2.3.5 The overall quality of the loan portfolio in the banking sector deteriorated in 2004 as reflected by a marked increase in the level of adversely classified loans to total loans from 4.43% as at 31 December 2003 to 18.52% as at 31 December 2004. The deterioration in asset quality was a manifestation of the adverse effects of a challenging economic environment characterised by high interest rates and foreign exchange constraints.

2.3.6 Figure 5 below shows the distribution of adversely classified loans (ACL) as a proportion of total loans for each banking class.

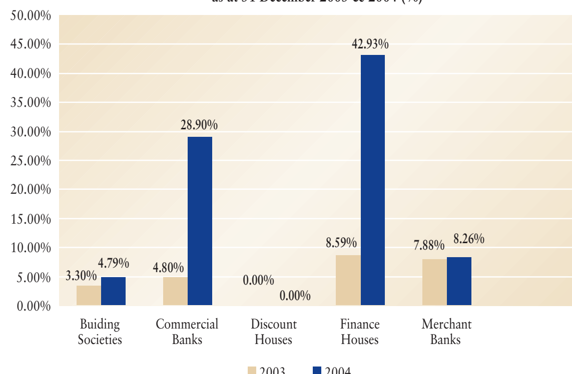

Figure 5: ACL/Total Loans Ratio as at 31 December 2003 & 2004 (%)

2.3.7 The level of overdue loans rose significantly from $77 billion to $1.032 trillion in the twelve months to December 2004. The sharp rise in over-due loans in 2004 is reflective of high lending rates averaging over 200% per annum, which resulted in some borrowers failing to service their loans during 2004. Figure 6 reflects the total banking sector overdue loans from March 2003 to December 2004.

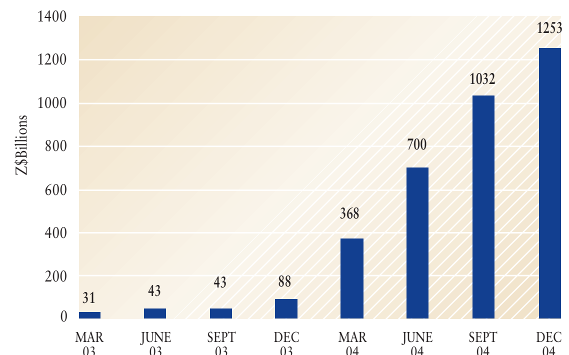

Figure 6: Total Banking Sector Overdue Loans (March 2003-December 2004)

Profitability...

2.3.8 Profitability in the banking sector, as measured by the return on assets, improved marginally during the year ended 31 December 2004, with the ratio increasing from 6.5% to 8.1%. The improvement is largely attributed to improved margins as well as cost containment efforts by banking institutions. The same efforts saw the cost to income ratio declining from 70.7% to 59.4% during the year under review. Figure 7 shows the profitability for banking institutions during the period under review.

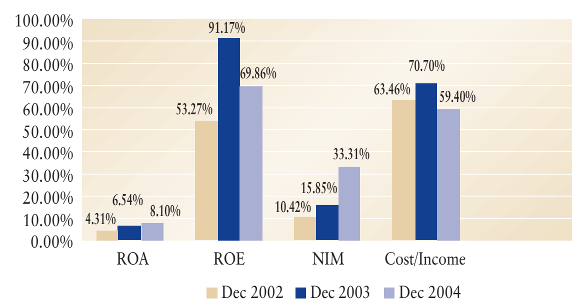

FIGURE 7: PROFITABILITY KEY INDICATORS [2002 - 2004]

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2.3.9 The average net interest margin increased from 16% to 33.3% in the period under review. This was a reflection of the wide spreads between lending rates of over 200% and average deposit rates of below 100% during the year under review.

2.3.10 Total interest income amounted to $5,727 trillion in 2004, a 205% increase from the $1,877 trillion recorded in the previous year. Net interest income increased by 444% from $707 billion in 2003 to $3,846 trillion in 2004.

2.3.11 Interest income constituted 85% of total income for the banking sector in 2004, a marginal increase from 84% recorded in the previous year.

2.3.12 Figure 8 below shows the distribution of the banking sector's revenue streams:

Figure 8(a): Composition of Income (2003)

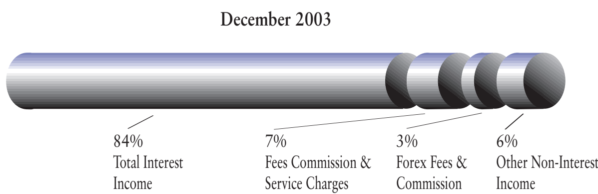
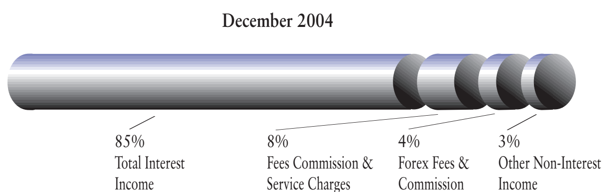


Figure 8(b): Composition of Income (2004)



2.3.13 The bulk of interest income emanated from securities and investments which contributed 48% of the total interest income compared to 37% in December 2003. Figure 9(a): "Composition of Interest Income (2003)". Figure 9(b) below shows the composition of interest income (2004).

Figure 9(a): Composition of Interest Income (2003)

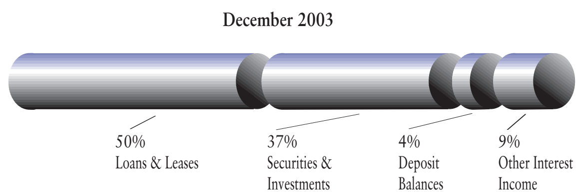
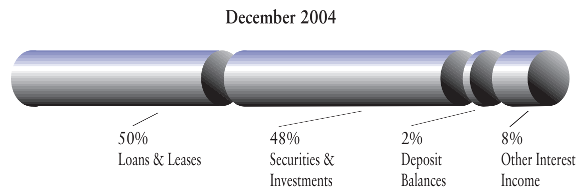


Figure 9(b): Composition of Interest Income (2004)



2.3.14 Total interest expense for 2004 amounted to $2.9 trillion in comparison to $1.17 trillion recorded in 2003. The bulk of this expense was from interest on deposits, which constituted 62% of total expenses in the year under review. Interest expenses from borrowed funds increased from 15% in 2003 to 19% in 2004. Figure 10 below shows the composition of interest expenses over the periods 2003 and 2004.

Figure 10 (a): Composition of Interest expense (2003)

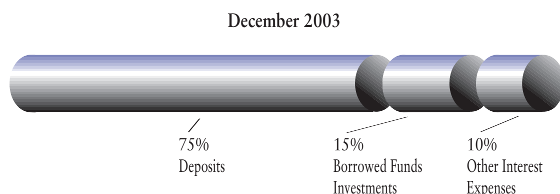


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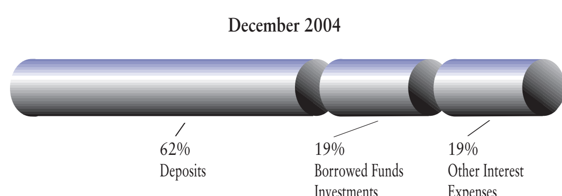
Figure 10 (b): Composition of Interest expense (2004)

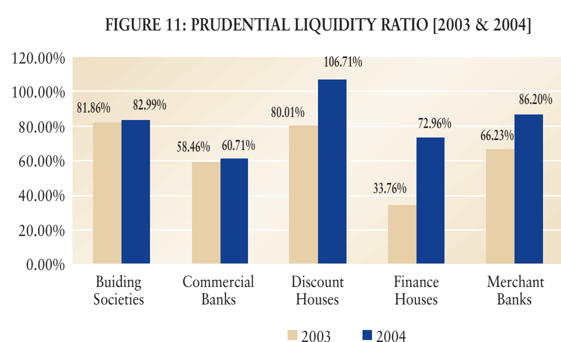


Liquidity and Funds Management…

2.3.15 The banking sector recorded a liquidity ratio of 83.9% as at 31 December 2004 compared to 64.1% achieved in December 2003. This reflected the general shift in focus towards short term investments with a view to matching the funding base, as the investing public was also investing short.

2.3.16 Figure 11 below shows prudential liquidity ratios for the different banking classes:

FIGURE 11: PRUDENTIAL LIQUIDITY RATIO [2003 & 2004]



2.3.17 It is noted, however, that a few institutions faced serious liquidity and solvency challenges during the course of 2004. These challenges were a spill-over from the last quarter of 2003, and reflected poor risk management systems and corporate governance practices on the part of the affected banking institutions. As noted elsewhere in this report, some banking institutions had tied up depositors' funds in speculative investments in real estate, other fixed assets and the stock exchange. The tight monetary policy meant to restore normalcy in the banking sector caught the affected institutions with huge funding gaps.

2.3.18 Discount houses recorded the highest liquidity ratio of 106.7% due to the nature of their core business of trading in liquid short term securities.

2.4 SECTORAL ANALYSIS

2.4.1 Commercial Banks

a) There were eleven commercial banks operating in the sub-sector as at 31 December 2004, following the placement under curatorship of Barbican Bank Limited, CFX Bank Limited, Intermarket Banking Corporation Limited, Royal Bank of Zimbabwe Limited, Time Bank Zimbabwe Limited, and Trust Bank Corporation Limited during the year. The banks that were placed under curatorship collectively had total assets of $671.88 billion as at 31 December 2003, which represented 16.25% of total commercial bank assets.

Total Assets…

b) Total assets in the sector increased by 182% from $5.99 trillion as at 31 December 2003 to $16.87 trillion as at 31 December 2004. The significant growth is a reflection of utilisation of concessional financing under Productive Sector Facilities and a general increase in the loan portfolio due to softening interest rates, in sympathy with declining inflation.

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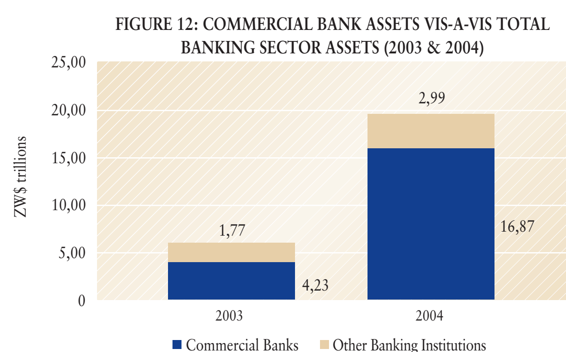
FIGURE 12: COMMERCIAL BANK ASSETS VIS-A-VIS TOTAL BANKING SECTOR ASSETS (2003 & 2004)



c) The major investment items for commercial banks in 2003 comprised securities and investments as well as loans and advances at 56.60% and 24.10% of total assets respectively. In December 2004 the major asset items were balances with the Reserve Bank (20.4%), securities and investments (24.8%) and loans and advances (24.5%).

d) The significant increase in the proportion of balances with the Reserve Bank relative to total commercial bank assets, from 0.20% to 20.4% over the year reflected an increase in statutory reserve requirements from 20% to 50% of liabilities to the public.

Total liabilities…

e) Commercial banks continued to fund their operations mainly through demand and savings deposits. Total deposits accounted for 40.8% of liabilities in 2004, down from 47.87% in 2003 while shareholders' equity funded 8.60% operations in 2003, which increased to 11.3% in 2004. The change was mainly due to capital injections by most institutions following the upward adjustment of minimum capital requirements from $500 million to $10 billion effective 30 September 2004.

f) Commercial bank's foreign liabilities constituted 1.83% and 3.1% of the balance sheet in 2003 and 2004 respectively

Capital Adequacy…

g) The sub-sector was adequately capitalised, as reflected by an average capital adequacy ratio of 34.41%. The capital adequacy ratios ranged from -0.35% to 100.43%. The top four commercial banks accounted for 71.01% of the sub-sector's aggregate capital base of $2.23 trillion while only two institutions had capital adequacy ratios below the 10% minimum requirement.

h) The institutions that registered capital ratios below the minimum requirements had both incurred losses during the year ended 31 December 2004.

Asset Quality…

i) Commercial banks recorded total loans, advances and leases amounting to $4.7 trillion in December 2004 up from $1.63 trillion in December 2003. Asset quality in this sector deteriorated, as shown by the ratio of adversely classified loans to total loans, which went up from 3.9% as at 31 December 2003 to 28.9%, as at 31 December 2004.

Earnings…

j) The sub-sector's profitability, as reflected by average return on assets, increased marginally during the year ended 31 December 2004, from 6.5% to 9%. Net income before tax increased by 450% from $443 billion in 2003 to $2.44 trillion in the year under review. Net interest margins also improved from 16.03% in 2003 to 37.79% in 2004.

k) The return on equity however, declined from

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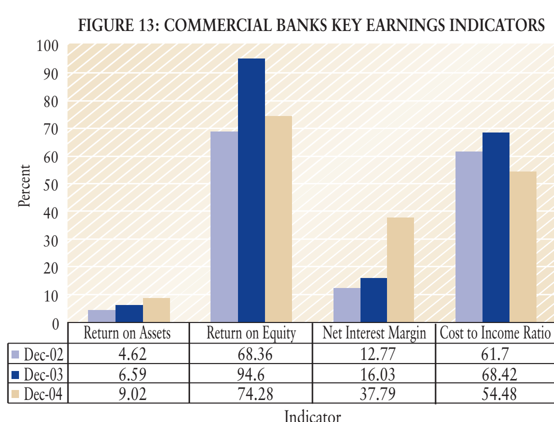
95.2% to 74.3% during the period under review. This was mainly due to the increase in the capital base in line with the new minimum capital requirements which came to effect on 30 September 2004. The earnings position of commercial banks is as shown below.



	Return on Assets	Return on Equity	Net Interest Margin	Cost to Income Ratio
Dec-02	4.62	68.36	12.77	61.7
Dec-03	6.59	94.6	16.03	68.42
Dec-04	9.02	74.28	37.79	54.48

FIGURE 13: COMMERCIAL BANKS KEY EARNINGS INDICATORS

Liquidity and Funds Management…

l. The average liquidity ratio for commercial banks declined from 60.71% to 55.31% during the year under review. A number of institutions experienced liquidity challenges emanating from funding gaps and failure by some borrowers to service their debts owing to generally challenging economic conditions.

2.4.2 Merchant Banks

a) There were five merchant banks operating as at 31 December 2004 after placement of CFX Merchant Bank Limited under the management of a curator on 17 December 2004. Premier Discount House converted to a merchant bank while Merchant Bank of Central Africa Limited (MBCA) converted to a commercial bank. Both institutions commenced the new businesses during the year under review.

Total Assets…

b) The total assets for the sector amounted to $1.5 trillion in 2004, an increase of 90.26% from $788.4 billion in 2003.

c) Securities and investments constituted the main asset component in 2004, being 39.68% of total assets, while loans and advances accounted for 24.53%. This was largely due to a shift by most banks in this sub-sector to money market instruments.

Capital Adequacy…

d) All merchant banks were adequately capitalised as at 31 December 2004, with an average capital adequacy ratio of 33.97%. All the five institutions had capital adequacy ratios that were above the regulatory minimum of 10%.

e) The average capital adequacy ratio increased from 20.2% as at 31 December 2003 to 33.97% as at 31 December 2004 due to additional capital injection in 2004 to meet the prescribed new minimum requirement of $7.5 billion for merchant banks.

Asset Quality...

f) Total loans, advances and leases amounted to $609.7 billion in 2004, an increase of 119.39% from $277.9 billion in 2003.

g) Credit risk in this sub-sector remained fairly stable as the adversely classified loans to total loans ratio marginally increased from 7.88% in 2003 to 8.66% in 2004.

Earnings...

h) The merchant bank sub-sector remained profitable as all institutions in this sub-sector posted positive results in 2004. Profitability, however, marginally declined in 2004, as

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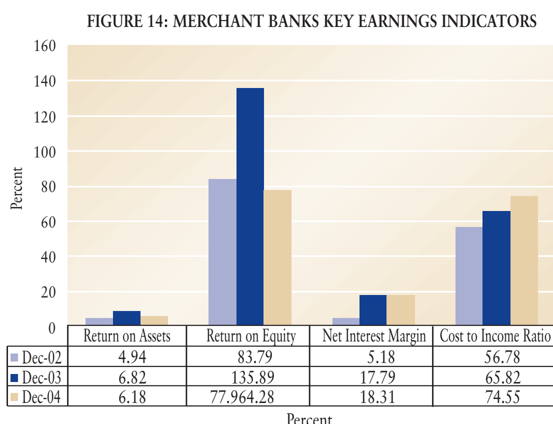
shown by a reduction in return on assets from 8.82% in 2003 to 6.18% in 2004. This was attributed to the increased operational costs, as reflected by the increase in the cost to income ratio, from 65.82% in 2003 to 74.55% in 2004. Income from securities and investments constituted 41.81% of total income during the year under review. The earnings position is as shown in figure 14 below:

FIGURE 14: MERCHANT BANKS KEY EARNINGS INDICATORS



	Return on Assets	Return on Equity	Net Interest Margin	Cost to Income Ratio
Dec-02	4.94	83.79	5.18	56.78
Dec-03	6.82	135.89	17.79	65.82
Dec-04	6.18	77.964.28	18.31	74.55

Percent

i) Net income declined from $69.6 billion in 2003 to $56.9 billion in 2004. The decline in net interest income was attributed to a more than proportionate growth in interest expenses of 191.18% compared to a 135.48% growth in income.

Liquidity and Funds Management...

j) The sub-sector recorded an average liquidity ratio of 86.2% in 2004, which compares favourably with the ratio of 66.23% in the previous year and ratios of the other sub-sectors.

k) The merchant banks managed to mobilise more deposits in 2004 as shown by a 39.74% increase in total deposits from $364.4 billion in 2003 to $509.2 billion in 2004. The bulk of these funds were invested in highly liquid and risk-free government paper on the money market as opposed to loans and advances.

l) Deposits continued to be the major source of funding for merchant banks although the sub-sector's total deposits to total liabilities declined from 46.2% in 2003 to 33.14% in 2004.

m) Other liabilities increased from 22.39% in 2003 to 31.63% in 2004, while capital and reserves amounted to $140.8 billion in 2004, up from $61.9 billion in 2003.

2.4.3 Finance Houses

a) There were four finance houses operating in the sub-sector as at 31 December 2004, down from five in December 2003. This followed divisionalisation of Leasing Company of Zimbabwe in 2004 to become part of CFX Bank Limited (under curatorship).

Total Assets...

b) Total assets increased by 181% from $98.2 billion to $276 billion during the year under review. Securities and investments constituted 26.7% of total assets as at 31 December 2004, down from 35.8% as at 31 December 2003.

c) Balances with the Reserve Bank increased by 7.4% from 0.26% as at 31 December 2003 to 8% as at 31 December 2004, as a result of an increase in statutory reserves from 5% to 15% of liabilities to the public, with effect from 1 January 2004.

Capital Adequacy...

d) All finance houses were adequately capitalised as reflected by an average capital adequacy ratio of 76.44% in 2004, compared to 6.28% in 2003. Total capital in the sub-sector increased by 203.57%, from $10.37 billion to $31.48 billion over the year.

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Asset Quality…

e) Finance houses recorded total loans of $46.90 billion on 31 December 2004, an 8% decrease from $47.3 billion in December 2003.

f) Overall, the quality of the loan portfolio deteriorated over the year under review as reflected by the increase in the ratio of adversely classified loans to total loans, from 8.59% to 42.93%. The deterioration in asset quality is a manifestation of generally challenging conditions which resulted in some borrowers failing to service their loans.

Earnings…

g) The sector's profitability level declined, as evidenced by the decrease in the return on assets ratio, from 5.4% to -2.7% during the year ended 31 December 2004.

h) The sub-sector also experienced a decline in return on equity from 86.57% to -32.73% during the same period. This was mainly due to escalating operational costs incurred in 2004 emanating from increases in salaries and employee benefits.

i) The average net interest margin also declined from 12.55% to 8.26% over the comparative periods. This, effectively, resulted in the sub-sector's retained earnings decreasing from $7.47 billion in December 2003, to a loss of $9.24 billion in December 2004.

Liquidity and funds management...

j) Finance houses funded their operations mainly from time deposits and NCDs, which constituted 72.04% of total liabilities as at 31 December 2003, and 74.36% as at 31 December 2004.

k) The sector's liquidity was, however, affected by an increase in the levels of adversely classified loans from 8.49% to 42.93% during the period under review, which resulted in funding gaps.

2.4.4 Discount Houses

a) There were five operating discount houses as at 31 December 2004, down from nine in December 2003, following the closure of three discount houses and conversion of another to a merchant bank. Total assets for the sub-sector increased by 32% during the year ended 31 December 2004 from $171.47 billion to $226.72 billion Discount houses' assets represented 3.14% of total banking sector assets.

Capital Adequacy…

b) With the exception of one discount house, all discount houses were adequately capitalised as at 31 December 2004. The average capital adequacy ratio for the sub-sector increased from 29% to 87.47% over the year.

Asset quality…

c) Securities and investments continued to dominate the balance sheets of discount houses constituting 52.48% of total sector assets.

Earnings…

d) The sub-sector realised a net loss of $16.9 billion in the year under review up from $14.2 billion in the previous year.

e) The return on equity for the period under review deteriorated from 77.7% for the period to 31 December 2003 to 53.1% for the year to 31 December 2004. The decrease can be attributed to an increase in the funding costs. Figure 15 below summarises the key earning indicators for discount houses.

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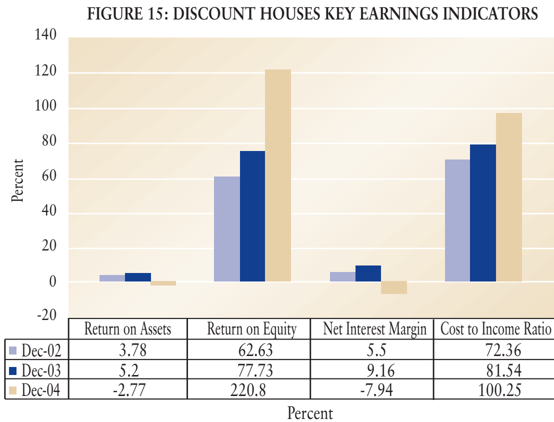


	Return on Assets	Return on Equity	Net Interest Margin	Cost to Income Ratio
Dec-02	3.78	62.63	5.5	72.36
Dec-03	5.2	77.73	9.16	81.54
Dec-04	-2.77	220.8	-7.94	100.25

Liquidity and Funds Management...

f) The total deposits for the sub-sector of $35.76 billion as at 31 December 2004 constituted 4.35% of total industry deposits.

2.4.5 Building Societies

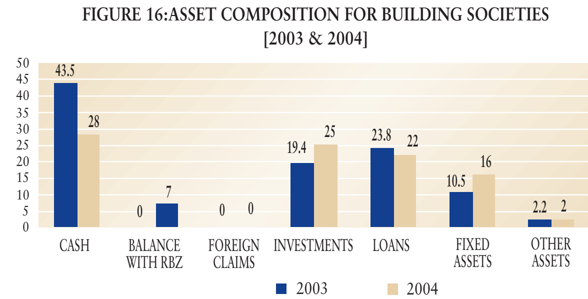
a) There were four building societies in operation as at 31 December 2004. The total assets for building societies constitute 5% of the total banking sector assets.

Total Assets...

b) Total assets for the sector grew by 188% during the period under review, from $171.5 billion as at 31 December 2003 to $948.1 billion as at 31 December 2004.

c) Balances with the Reserve Bank amounted to $62.57 billion following a new requirement for building societies to pay statutory reserves.

d) Total loans grew by 168% from $80.9 billion to $216.9 billion during the period under review. The contribution of securities and investments to total assets increased from 19.4% to 25.5% mainly due to the high money market interest rates that prevailed in 2004. On the other hand, the proportion of loans to total assets fell marginally from 23.7% to 22.3%. The composition of the assets for building societies is reflected in Figure 16 below;



Capital Adequacy...

e) Building societies were adequately capitalised with capital adequacy ratios significantly in excess of the regulatory minima. Capital adequacy ratio was 70.18% as at 31 December 2004, compared to 52.6% recorded as at 31 December 2003. The increase in capital adequacy ratios is indicative of a shift towards short term investments by the societies, partly reflecting constraints such as limited availability of serviced stands, as well as the inhibitive costs of mortgage finance.

Asset Quality...

f) Asset quality for building societies was satisfactory during the period under review. The average ratio of adversely classified loans to total loans for building societies increased from 1.01% as at 31 December 2003 to 4.79% as at 31 December 2004.

g) However, the level of adversely classified loans to total loans ratio for building societies remains low in comparison to the banking sector average of 18.52%. The low level of adversely classified loans for building societies is a reflection of high payment levels by clients

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who fear repossessions of their properties, in view of the escalating replacement costs.

Earnings…

h) The earnings performance of the sub-sector was satisfactory during the period under review. Net income for building societies increased by 135% from $26.51 billion in 2003 to $62.33 billion in 2004.

i) The average return on assets fell from 8.55% in 2003 to 6.57% in 2004. The average return on equity also declined from 45.93% in December 2003 to 32.69% in December 2004. However, net interest margins increased marginally from 19.86% to 21.37% due to high interest rates on the money market. The aggregate cost to income ratio for building societies declined marginally from 73.97% in 2003 to 71.45% in 2004.

j) Income from securities and investments constituted 53% of total building society income as at 31 December 2004, down from 84% as at 31 December 2003. On the other hand, income from loans and leases increased by 20% from 10% of total income to 30% of total income in December 2003 and 2004 respectively.

Liquidity and Funds Management…

k) Building societies recorded an average liquidity ratio of 82.99% during the period under review, compared to 81.5% recorded as at 31 December 2003. The increase in the ratio is a reflection of the shift towards short-term investments, such as Treasury Bills and Bankers' Acceptances, as noted above. In the same vein, concentration on non-core activities partly explains the marginal fall in building societies' total loans to total deposit ratio. The ratio of building societies' total loans to total deposits decreased from 36.5% to 33.3% as at 31 December 2003 and December 2004 respectively.

CHAPTER THREE
MAJOR DEVELOPMENTS AND ACTIVITIES IN BANKING SUPERVISION

3.1 INTRODUCTION

3.1.1 The Reserve Bank conducted a number of activities during the course of 2004 in fulfillment of its mandate of promoting financial stability. The major highlights relate to regulatory reforms, licensing and de-registration of financial institutions, on-site and off-site examinations, investigations, issuance of various guidelines and conducting workshops aimed at educating banking institutions on prudential issues. In line with BLSS's thrust of value added supervision, a number of presentations were conducted on topical issues in order to enlighten the banks and the general public on prudential requirements.

3.2 REGULATORY DEVELOPMENTS

Financial Laws Amendment…

3.2.1 In January 2004, The Presidential Powers (Temporary Measures) (Financial Laws Amendment) Regulations, Statutory Instrument No.14 of 2004 were promulgated to amend the following statutes:

- The Banking Act (Chapter 24:20), (the Banking Act);
- Building Societies Act (Chapter 24:02);
- Money lending and Rates of Interest Act (Chapter 14:14); and
- The Collective Investments Schemes Act (Chapter 24:19).

3.2.2 The said amendments had the effect of bringing the function of licensing and de-licensing of banking institutions, building societies, money lenders and collective investment schemes within the jurisdiction of the Reserve Bank. This function had, prior to the said statutory instrument, been vested in the Ministry of Finance.

3.2.3 The vesting of both the licensing and supervisory functions with the Reserve Bank has strengthened the regulation of the finance sector. To ensure continuity in the licensing function, the said Statutory Instrument also had provisions to transfer employees from the Registrar of Banking Institutions' office under the Ministry of Finance to the Reserve Bank.

3.2.4 Another key provision of the statutory instrument related to the amendment of section 18 of the Banking Act which now requires that at the time a banking institution is licensed or when a director is appointed to a banking institution's board he/she must be fit and proper to sit on such a board, and shall not exercise any of the duties of a director until the Reserve Bank's written approval to that effect is obtained. This was an important provision, against the background of wide-spread poor corporate governance in the banking sector in the pre- 2004 era.

3.2.5 The amendments to banking laws introduced by the said regulations, which were enacted in Parliament in the second half of the year as the Financial Laws Amendment Act No. 16 of 2004, went a long way towards bringing the banking laws in line with the principles outlined in the Basel Committee's 25 Core Principles for Effective Bank Supervision.

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Asset management companies…

3.2.6 In January 2004, the Presidential Powers (Temporary Measures) (Asset Management) Regulations, Statutory Instrument 16 of 2004 was issued. The statutory instrument brought the sub-sector of asset managers within the ambit of the Reserve Bank's regulatory jurisdiction. This development was necessitated by the fact that the year 2003 had seen the mushrooming of asset management companies, which, being unregulated, engaged in speculative and illicit activities.

3.2.7 Statutory Instrument No. 16 of 2004 provided for the licensing, by the Registrar of Asset Managers, of companies which were conducting, or intending to conduct the business of asset management. Upon the expiry of the Statutory Instrument, the Asset Management Act [Chapter 24:26] was passed by Parliament, giving permanence to the provisions of the temporary Presidential Powers Regulations.

3.3 TROUBLED FINANCIAL INSTITUTIONS (RESOLUTION) ACT

3.3.1 Recent bank failures highlighted the need for a long term solution to deal with troubled financial institutions in a manner which safeguards depositors' interests and protects the integrity of, and stabilises the financial sector.

3.3.2 Following the adoption of a comprehensive Troubled Bank Resolution Framework, the Troubled Financial Institutions (Resolutions) Act No. 31 of 2005 was enacted in January 2005. The said Act provides for the declaration and administration of troubled financial institutions and the formulation and implementation of schemes of resolution in respect of such institutions. The main aim of the Act is to provide a legal framework for resolution of problems in the financial sector, the emphasis being to prevent the destabilising effects of systemic risk in the sector.

3.4 PROPOSED AMENDMENTS TO BANKING LAWS

3.4.1 The Reserve Bank is currently working towards amending the Banking Act to reflect market changes and keep abreast with international best practice. The Reserve Bank is committed to the holistic supervision of financial institutions operating within a group structure and as such, provisions for a detailed legal framework in consolidated supervision are becoming increasingly necessary.

3.4.2 The Banking Act is also in the process of being amended to make the provisions on corporate governance more comprehensive. The Act will also take into account issues of auditor and accountants' liability.

3.5 BANKING SUPERVISION APPLICATION

3.5.1 With effect from October 2004, the Reserve Bank implemented a new information technology system, the Banking Supervision Application (BSA). The BSA system was installed as part of the Southern African Development Community

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(SADC)/East and Southern Africa Banking Supervisors' Group (ESAF) information technology harmonisation strategy, with the objective of enhancing the effectiveness of the bank supervision function in the SADC/ESAF countries.

3.5.2 The BSA system has two subcomponents, namely Banking Supervision System (BSS) and Risk Analysis Automated System (RAAS). The BSS component incorporates five supervision applications, namely licensing of banks, supervisory infrastructure and databases, on-site examinations, off-site analysis and enforcement actions.

3.5.3 The RAAS component provides powerful analysis tools (graphs and reports) and facilitates the compilation and maintenance of current and accurate bank supervision data.

3.5.4 BSA, through the Risk Analysis Automation System (RAAS), has the capacity to generate multiple ratios critical for the off-site surveillance of banking institutions, as well as highlighting early warning signals for potential challenges in the supervised institutions.

3.5.5 Following the deployment of the BSA Solution, all banking institutions and building societies are now required to submit statutory returns electronically.

3.5.6 The system can be upgraded to incorporate additional functions. Further, it has the ability to perform preliminary verification and validate returns, thereby enhancing data accuracy and integrity. The validation of returns acts as an early warning signal for challenges that a financial institution may be facing, manifesting in flawed reporting.

3.5.7 This is not only important to the Reserve Bank, but to the supervised financial institutions, policy-makers and the public at large, as decisions will be based on quality information.

3.5.8 This will enhance the effectiveness and efficiency of banking supervision through the automation of supervisory processes and workflows.

3.6 CAPACITY BUILDING

3.6.1 During the year under review, BLSS recruited additional staff members with various skills including legal, banking, finance, accounting, economic and statistical modelling, and IT.

3.6.2 This has enabled the division to constitute examination teams with diverse skills required to undertake various tasks and has facilitated in-depth determination of the condition of banking institutions.

3.6.3 Fourteen supervisors have received specialist training in computer-based auditing. This will go a long way towards preventing some of the challenges that bedevilled the banking sector in 2004, which included creative accounting and manipulation of data by some banking institutions to disguise their true conditions. In that regard,

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twenty-one bank examiners attended regional and international supervisory courses. The trained examiners will impart acquired skills to the other bank supervisors.

3.7 FSI CONNECT

3.7.1 Zimbabwe was the first African country to subscribe to FSI Connect, which was launched by the Bank for International Settlements (BIS) at the end of June 2004. All staff in Bank Licencing, Supervision & Surveillance division have access to this facility.

3.7.2 FSI Connect is an online training and development program and information tool for banking supervisors, developed by the Financial Stability Institute (FSI).

3.7.3 FSI Connect offers tutorials on a wide range of practical banking and bank supervision topics including all aspects of the Basel II framework. The tutorials utilise an appropriate blend of content and interactive exercises and case studies. Key topics covered include Market Risk, Credit Risk and Operational Risk.

3.7.4 The course content is designed to suit experienced supervisors as well as those new to the field. Tutorials are offered at fundamental, intermediate and advanced levels.

3.7.5 The Reserve Bank has also made FSI Connect tutorials a benchmark for the internal accreditation and upgrading of its bank supervisors. Our bank supervisors have, through FSI Connect, been exposed to international standards in bank supervision and international developments pertaining to the profession.

3.7.6 In light of foreign currency shortages, the program has proved to be cost effective in that it enables the simultaneous training of all staff members as opposed to sending a few staff members to attend courses outside the country. It has complemented on the job training for bank supervisors and to date has made a notable positive impact in ongoing efforts to strengthen the central bank's supervisory capacity.

3.7.7 FSI has gone a long way in strengthening supervisory capacity in the division. As a result our supervisory processes are more comprehensive and thus provide greater value addition to supervised institutions.

3.8 COORDINATION WITH OTHER FINANCIAL SYSTEM REGULATORS

3.8.1 BLSS has established working relationships with the Zimbabwe Stock Exchange and the Deposit Protection Board which will be formalised through memoranda of understanding. Co-operation facilitates the sharing of information which is mutually beneficial to all parties.

3.8.2 The memoranda of understanding will go a long way towards reducing supervisory gaps, regulatory arbitrage, and enhance consolidated supervision.

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3.9 BASEL II

3.9.1 In June 2004, the Bank for International Settlements' Basel Committee published the revised version of the Capital Accord under the title "International Convergence of Capital Measurement and Capital Standards, a Revised Framework".

3.9.2 The revised framework (Basel II) represents a major revision of the international bank capital adequacy framework that was first introduced in 1988. Basel II aligns the capital measurement framework with sound contemporary practices in banking, promotes improvements in risk management, and emphasises the importance of market discipline in enhancing financial stability.

3.9.3 The principles enshrined in Basel II ensure that banks' capital adequacy requirements are aligned to their true risk profiles. The capital framework represents bank supervisors' response to changes flowing from the increasing sophistication of risk measurement and management.

3.9.4 The erosion of the Basel I rules through capital arbitrage was one of the motivations for the development of Basel II. One example of such arbitrage is the transfer, off the balance sheet, of certain assets with economic capital allocations below regulatory capital requirements and the retention of those for which regulatory requirements are less than the economic capital burden. Aggregate regulatory capital thus ends up being lower than what the economic risks require. In such instances, it is possible for banks to increase their risks without increasing their required capital. Hence, regulatory capital ratios will not always reflect the banks' true risk profiles.

3.9.5 The 1988 Capital Accord did not sufficiently recognise the different risk profiles of bank clients within the same category. It is noted that the "one-size-fits-all" approach of the 1988 Capital Accord was a major weakness.

3.9.6 The overarching goal of Basel II, which is more risk-sensitive, is to advance the practice of banks' risk management. Management of banking institutions are required and are expected to have an enhanced knowledge of their institutions' activities, risk profiles and risk management processes.

3.9.7 The Internal Ratings Based (IRB) approaches give primacy to internal risk measures in setting regulatory capital requirements. The regulators should however be satisfied that the risk measures are reasonably accurate and consistent. In this regard, the qualification standards under the IRB approaches are a representation of the banking industry best practice.

3.9.8 The three pillars under Basel II detailed below, work in an integrated manner to strengthen the supervision of banking systems.

Highlights of Basel II…

3.9.9 In the new Capital Accord the scope for regulation has considerably increased due to use of advanced risk measurement techniques, internal models,

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supervisory discretion as well as validation of banks' internal models. By way of architecture, the New Capital Accord is made up of three complementary pillars.

3.9.10 The first pillar provides for the determination of regulatory capital requirements; the second pillar is a set of principles for the execution of supervisory oversight; and the third pillar is a set of disclosure requirements intended to enhance market discipline.

3.9.11 The First Pillar: Minimum Capital Requirements

a) The quantitative regulations on minimum capital requirements are the starting point of the New Basel Capital Accord.

b) The calculation of the total capital requirements for credit, market and operational risk are covered in the proposed minimum capital requirements.

c) Pillar I sets out three means for calculating capital requirements:

- The "standardised" approach (SA) provides for the use of predetermined weights for allocation of capital in respect of credit and market risk. A simplified basic indicator approach is also available under the standardised framework for operational risk
- The "internal ratings-based (IRB)" approaches utilise the bank's own internal assessments to allocate capital for credit, market and operational risk. Before a banking institution is authorised to make use of these internal models it is expected to satisfy certain validation standards put in place by the regulatory authorities. The internal ratings based approach can either be at foundation or advanced level.

3.9.12 The Second Pillar: Supervisory Review Process

a) The supervisory review process plays a critical validation role to support both capital regulation (Pillar 1) and market discipline (Pillar 3). The process involves the continuous review of the bank's risk management processes against the risk profile of the institution.

b) Pillar 2 seeks to ensure that a bank's capital position is consistent with its overall risk profile, control environment and strategy, and that early supervisory intervention is possible.

c) The supervision applied must be more risk-focused and concerned with validating systems under Basel II. Supervisors are expected to evaluate the quality of risk management and examine the adequacy of the risk measures such as internal ratings and the probabilities of default.

3.9.13 The Third Pillar: Market Discipline

a) The third pillar encourages market discipline by developing a set of disclosure requirements about a bank's risk profile, enabling other participants in the market to assess its risk position and the adequacy of its capital. This pillar therefore, instills market discipline by imposing strong incentives on banks to conduct their business in a safe, sound and efficient manner.

b) The Basel Committee requires that where possible, disclosures should be reconciled with the accounting principles of the International Accounting Standards (IAS). This pillar

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therefore has significant implications for banks' data quality and system integration, and hence banks' IT landscapes.

c) The availability of informative and comparable disclosures of banks' internal risk measures will certainly enhance the effectiveness of market discipline. The market will be in a position to react quickly and appropriately to material variations in banks' risk postures.

Benefits…

a) Basel II should be seen as an opportunity to put in place new risk management and regulatory reporting standards. The advanced approaches for operational and credit risks encourage banks to embrace best practice in these areas.

b) Further, Basel II provisions will not only ensure that banks maintain levels of capital that are in line with their risk exposure, but also require banks to control risk adequately and to justify the risks they have taken. Thus, over and above the calculation of capital requirements, Basel II creates new opportunities for financial institutions through the transformation of the enhanced regulation into a tool for creating value.

c) The Accord will have an impact on the transparency of published results. Pillar II will provide a strong motivation for sound financial communication and risk management. Financial institutions in Zimbabwe are already subject to disclosure requirements and hence the graduation process to the enhanced disclosure framework is expected to be smooth.

Challenges…

a) Implementation of Basel II brings with it certain challenges which include the suitability of internal and external data sources, determination of the appropriate historical period to use in producing estimates, and the manner in which historical data and loss estimates should be linked to the bank's current exposures.

b) The Basel Committee proposes that where a banking group has operations in at least one country other than the home country, the implementation of the New Accord requires that such a banking group obtains approval for its use of certain approaches from relevant host country supervisors on an individual or sub-consolidated basis, as well as from its home country supervisor in respect of consolidated supervision. Thus closer cooperation between supervisors can assist the implementation efforts of both supervisors and banking groups.

c) Basel II makes significant strides in aligning regulatory capital with true economic risk. The benefits of the new Accord are considerable. It is more than a compliance exercise. It is likely to transform the underlying economics of the financial services markets, leading to significant changes in resource allocation, competitive positioning and the supply of financial services.

3.9.14 Way forward

a) BLSS has conducted a number of workshops on Basel II for the representatives of the banking sector and more are scheduled for 2005 as

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efforts to build capacity and prepare the banking sector for implementation progresses.

b) The Reserve Bank already requires banking institutions to allocate capital for market and operational risks. Further, a number of guidelines have been issued to the banking sector in order to promote prudent risk management practices in line with the provisions in Pillar I and II.

c) Member countries of the Basel Committee on Bank Supervision have agreed on a common implementation date for Basel II of end of 2006 for the standardised and foundation approaches, and end of 2007 for most of the advanced approaches. In these countries, the implementation of Basel II is intended to encompass internationally active and other significant banks as the national supervisors deem appropriate.

d) However, Basel II implementation for the developing world is expected to take longer. It is noted that in many of the developing countries, the priority may be to strengthen the supervisory function and capacity building for both supervisors and the market, among other pertinent considerations before implementation.

e) Although Basel II has been embraced by the developing world, large scale implementation in most African countries is expected from 2010 onwards. Zimbabwe is coordinating efforts with other countries in the region in the implementation program.

f) The region is receiving assistance in building technical assistance and general capacity for Basel II implementation from the Financial Stability Institute (FSI).

g) The implementation of Basel II will be one of BLSS's high-priority strategic focus areas for the forthcoming years.

h) In preparation for Basel II implementation, banking institutions are now required to be rated by external credit rating agencies, which are accredited by the Reserve Bank of Zimbabwe. This enhances the role of market discipline as economic agents have access to additional information from independent sources. Going forward it is expected that banks' borrowers will also be rated, thus facilitating the use of independent external credit ratings in the implementation of the New Capital Accord.

i) The Reserve Bank has also issued guidance to the market that include guidelines on the internal audit function in banks, as well as a framework for cooperation between the supervisors and banks' external auditors. The roles of these stakeholders complement the supervisory function and are important facets of the risk-focused supervision approach.

3.10 CONSOLIDATION OF THE LICENSING AND SUPERVISORY FUNCTIONS

3.10.1 A notable development was the transfer of the licensing function from the Ministry of Finance to the Reserve Bank with effect from 1 January 2004. Consequently, the Reserve Bank assumed the role of both licensing and supervisory authority for banking institutions, microfinance and money lending institutions, and asset management companies.

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3.10.2 The consolidation of the licensing and supervision functions was in recognition that the supervision of a bank starts at inception.

3.10.3 Prior to the transfer of licensing function, the Reserve Bank's involvement in the licensing process only went as far as making recommendations to the Registrar of Banking Institutions. Financial sector developments in the fall of 2003 dictated the need for the licensing and supervisory functions to be consolidated and housed with one authority.

3.11 DEPOSITING START-UP CAPITAL WITH RESERVE BANK

3.11.1 The year 2004 also saw the Reserve Bank requiring promoters of new banking institutions to deposit their start-up capital with the Reserve Bank whilst the evaluation of their project proposal is under way.

3.11.2 The new policy was prompted after a realisation that some promoters were applying for banking licences and misrepresenting to the Reserve Bank on the existence of start-up capital.

3.12 CONVERSIONS OF BANKING LICENCES

3.12.1 Two (2) banking institutions were authorised to commence operations following the conversion of their banking licences. Premier Discount Company Limited's application to convert from a discount house to merchant banking was approved in August 2004. Following a pre-opening inspection the institution was authorised to commence merchant banking operations as Premier Banking Corporation Limited with effect from 10 November 2004.

3.12.2 The Merchant Bank of Central Africa ("MBCA"), whose application for conversion from a merchant bank to a commercial bank had been approved in 2003, commenced commercial banking operations as MBCA Bank Limited on 29 November 2004.

3.12.3 The repositioning of MBCA from a merchant bank to a commercial bank was designed to broaden its product range. The bank wanted to diversify its deposit base by augmenting wholesale deposits with retail deposits.

3.13 CROSS BORDER INVESTMENTS

3.13.1 Two (2) cross border investment applications were received in 2004. The rationale for cross-border investments was to develop a market for niche products and services in the respective jurisdictions.

3.13.2 Kingdom Financial Holdings Limited was authorised to establish a wholly owned commercial bank subsidiary in Zambia, Kingdom Bank Zambia Limited. Renaissance Financial Holdings applied for the establishment of a wholly-owned subsidiary to conduct stock broking and investment advisory services in Uganda. Both applications were approved by Bank Licensing, Supervision & Surveillance and Exchange Control Divisions.

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3.13.3 The Reserve Bank will enter into Memoranda of Understanding with the respective central banks to ensure adequate oversight on the operations of these subsidiaries.

3.14 LICENSING OF NON-BANK FINANCIAL INSTITUTIONS

3.14.1 The year 2004 saw the Reserve Bank developing licensing criteria for asset management companies and microfinance and moneylending institutions. The criteria formed the basis for a transparent review of the applications.

3.14.2 Asset Management Companies

a) Fifty-eight (58) applications for registration of asset management companies were received in 2004 and thirty-one (31) licences were issued, while nine (9) applications were withdrawn and eighteen (18) applications were rejected for the following reasons, among others:
- inadequate capitalisation;
- misrepresentation of information;
- project documents not properly drawn up; and
- some promoters were not fit and proper.

b) The registration of asset management companies was completed by 31 August 2004 with thirty one (31) institutions having been licensed.

c) Following a determination by the Reserve Bank that some asset managers were not conducting proper asset management business and that the sector was facing viability challenges, a policy decision was taken by the Reserve Bank not to register any new asset management companies.

3.14.3 Microfinance institutions

a) As at 31 December 2004, forty-five (45) applications for licensing had been received. Ten (10) licences had been issued, four applications were withdrawn, and two applications were rejected, while the remaining applications were at various stages of processing. The pace of processing the applications was, in most cases, hindered by the late response to information requests by the applicants.

3.14.4 Moneylenders

a) As at 31 December 2004, one hundred and ninety-two (192) applications had been received. A total of thirty-five (35) institutions were licensed, nine (9) rejected, while four (4) applications were withdrawn and the remaining applications were at various stages of evaluation. In most cases, the promoters had not provided the required information and documentation.

b) In the majority of cases, both microfinance and moneylending applications were rejected for the following reasons, among others:
- incomplete documentation;
- inadequate capitalisation;
- deposit taking (microfinance and moneylending institutions are prohibited from taking deposits in this country);
- misrepresentation of information; and
- Unfit and improper promoters.

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3.15 ON-SITE EXAMINATIONS ON BANKING INSTITUTIONS

3.15.1 During the year under review, BLSS carried out ten full scope and nineteen targeted examinations.

3.15.2 The targeted on-site examinations were carried out on various institutions, to determine among other things, their liquidity and solvency status.

3.15.3 In addition, two pre-opening examinations were conducted on Premier Banking Corporation Limited and MBCA Bank Limited following the conversion of their respective licences.

3.15.4 BLSS also commissioned investigations on CFX Bank Limited [formerly Century Bank], CFX Merchant Bank Limited and Time Bank Zimbabwe Limited to determine their solvency and liquidity status as well as to establish the nature of fraudulent activities which were suspected to have taken place in these institutions.

3.16 MAJOR FINDINGS FROM ON-SITE EXAMINATIONS ON BANKING INSTITUTIONS

3.16.1 General Findings

a) Both targeted and on-site examinations determined that some banks were facing serious solvency and liquidity challenges. Liquidity challenges were attributed to non-performing assets and flight of deposits from perceived unsound banks. The resultant refinancing costs, coupled with the required provisions for bad and doubtful debts, translated to solvency challenges.

b) These developments were a crystallisation of the underlying flaws that characterised the banking sector prior to the monetary policy of December 2003. The fundamental flaws related to poor corporate governance practices, rapid expansion without the requisite risk management systems, high volumes of non-performing insider loans, inadequate capitalisation, insider abuse, and inappropriate transactions with associate companies. Faced with these challenges, some banks employed creative accounting in order to mask losses and undercapitalisation.

3.16.2 Poor Corporate Governance

a) Poor corporate governance practices were epitomised by improperly constituted boards of directors, poor board oversight, inexperienced management, and undue influence or domination by owner managers with a high concentration of shareholding influence.

b) Such poor corporate governance practices provided fertile grounds for the abuse of depositors' funds.

c) Some boards of directors of banks were virtually non-functional. Board members of these institutions were not fully conversant with the magnitude of problems in their banks relating to the level of insider lending, the high concentration risks, and the level and nature of non-core activities that had been undertaken by the banking institutions.

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d) There were numerous examples of non-core business activities that were conducted by banks which included investments in commodities, real estate, and equities. In this way, the banks concerned helped fuel the asset price bubble.

e) Excessive management control was manifested by the emergence of owner-run institutions, and through the domination of CEOs in decision making, cronyism and nepotism on boards of directors. Undue influence by CEOs led some banking institutions to catastrophe as such CEOs bypassed their boards or were merely waved-on by rubber-stamping "yes-men" boards to engage in extensive risky and speculative transactions, with disastrous consequences for the institutions concerned.

3.16.3 Inadequate Risk Management Systems

a) The on-site examinations also revealed that in addition to poor corporate governance, most financial institutions were operating without adequate risk management practices and had poor management information systems.

b) Poor risk management practices largely stemmed from failure to timely identify, measure, monitor and control material risks. This exposed certain banks to failure as banks are highly geared and have substantial maturity mismatches on their balance sheets.

c) The examinations, however, also noted that some banking institutions were sound and had prudent risk management systems, an aspect which is commendable.

d) A lack of internal controls in the derivatives departments of some asset management companies made it difficult to establish the validity and completeness of transactions, resulting in fraud by employees.

3.16.4 Abuse of Depositors' Funds

a) There are numerous ways in which some senior executives in the troubled banking institutions abused and manipulated depositors' funds. In some cases, funds were blatantly diverted to the personal use of the CEO or top management in the form of personal loans, or investments falsely accounted for in the company's name.

b) Other less patent abuses of depositor funds exposed through Reserve Bank investigations involved management designing elaborate structures of capitalising the banks using depositor funds. The structures involved advancing funds to a "friendly institution" which in turn would on-lend the funds back to the bank's holding company. The holding company would inject the funds back into the bank which would be accounted for as capital. In other instances, depositor funds had been recklessly invested by management in speculative and risky transactions, such as short-term stock market trades, resulting in huge losses for the institutions concerned.

3.16.5 Abuse of Holding Company Structures

a) There was unprecedented abuse of associate companies and/or related parties to effect elaborate schemes designed to enable banks to venture into non-banking activities such as investments on the stock market and real

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estate, trading of foreign currency on the parallel market, and acquisition of fixed assets for speculative purposes. Such engagements were designed to evade regulation and channel depositors' funds to non-regulated entities such as asset management or investment companies.

b) The Monetary Policy announced in December 2003 which was aimed at bringing sanity in the financial sector, caught the affected banking institutions with illiquid assets that could not be easily liquidated. In some instances, banks abused liquidity support from the Reserve Bank to fund non-banking subsidiaries and associates' requirements.

c) Special purpose vehicles and holding company structures were used in the crafting of structured transactions designed to conceal the diversion of depositors' and borrowed funds into non-permissible activities.

3.16.6 Rapid expansion

a) On-site examinations also determined that some banking institutions were facing liquidity challenges due to rapid and ill-planned expansion drives which tended to overstretch their limited resources.

b) The expansion drive embarked on by most institutions locally and in the region, was not synchronised with the overall strategic initiatives of the institution concerned, hence exposing them to greater risk of loss. In particular, the capital bases of these institutions were placed under undue pressure directed towards reckless expansion drives. In a few cases, the rapid expansion was funded by depositors' funds as opposed to equity.

3.16.7 Misrepresentation and Creative Accounting

a) The examinations unearthed massive misrepresentation of the financial condition of some banking institutions. It was noted that some banking institutions unethically maintained two sets of records; one fabricated set for regulatory convenience, and another set reflecting the correct profile of the institution.

b) In addition to misrepresentation of financial condition, some banking institutions went as far as tampering with the information systems to conceal losses by creating fictitious assets and understating expenses and liabilities. Management of some banking institutions crafted irregular capitalisation schemes involving the use of borrowed funds to fund the purchase of the company's own shares, in violation of the Companies Act.

3.16.8 Capital

a) Onsite examinations established that some banking institutions were overstating their capital positions by under-providing for non-performing loans which were in most instances linked to insiders and associate companies.

b) Cases were also noted of banking institutions which were capitalised using depositors' funds in contravention of the Banking Act. One institution went to the extent of crafting an intricate web of transactions designed to create an impression of adequate capitalisation.

c) Some institutions were also found to have misrepresented the minimum paid up capital

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during the licensing stage, a development which prompted the Reserve Bank to require promoters to deposit start-up capital with the central bank.

3.16.9 Asset Quality

a) As already noted, poor corporate governance practices, weak underwriting and monitoring standards as well as ill-planned growth resulted in high levels of non-performing loans.

b) Some banking institutions were not adhering to prudential lending limits as provided for in the Banking Regulations (S.I/205 of 2005) ("the Banking Regulations"). There was wilful breach of lending limits especially to insiders and related parties. Some institutions went as far as not charging interest on insider loans and eventually writing off these loans without board approval.

c) It was also noted that some boards of directors had limited oversight on the loan portfolio. Some Board Loans Review and Credit Committees were literally rubber stamping the activities of owner managers without taking cognisance of the risk associated with the advances. In a number of cases, some members of these Committees were found to have benefited directly or indirectly from the loans, and therefore, had no moral grounds to challenge management.

3.16.10 Earnings

a) Prior to the financial distress, banking institutions experienced phenomenal growth in their balance sheets and earnings were generally above inflation. The significant growth in earnings and the balance sheets was largely attributed to revaluation of the bank's investments in long term assets which were experiencing an asset price bubble.

b) In the face of increasing competition which resulted in squeezed profit margins, the high salaries and benefits that had been offered by new banks to attract staff from traditional banks could no longer be sustained from core revenue streams; hence the diversion into non-core sources of income. In most cases, the engagement in non-core business was orchestrated through special purpose vehicles designed to circumvent regulations.

c) The crash in equity prices during the first quarter of 2004 resulted in revaluation losses being incurred by banks that had been speculating on the stock market.

3.16.11 Liquidity and Funds Management

a) Some banking institutions experienced liquidity problems in the fall of 2003 and the greater part of 2004. The underlying causes were funding gaps which were occasioned by illiquid assets which were being funded by short-term deposits.

b) The underlying liquidity challenges had been masked by surplus money market conditions, against the background of lax accommodation. With the advent of the tight accommodation, the affected banking institutions were caught with huge funding gaps. The situation was aggravated by the sharp increase in interest rates in line with efforts to curb inflation.

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c) The first quarter of 2004 also saw a decline in equity prices, which in turn presented challenges to the banks which had funds locked up in the stock market. Disposal of these investments would imply automatic loss.

d) These developments not only created liquidity problems, but exposed the affected banks to interest rate risk in view of the upward repricing of short-term liabilities. The situation was exacerbated by the absence of risk management systems to measure and manage market risks.

e) With the placement of nine banking institutions under curatorship during the year, a few of the smaller banks experienced deposit flight to banks that were perceived to be sound, hence aggravating the liquidity crisis.

f) The developments noted above culminated in the Reserve Bank introducing the Troubled Bank Fund to avert a systemic crisis as most banking institutions could not easily liquidate the speculative positions or investments.

g) In addition, the examinations also established that most banking institutions did not have effective board committees to manage the banks' liquidity risk. The management of the bank's balance sheet was relegated to junior staff without adequate strategic direction from senior management.

3.17 SUPERVISORY ACTION

Corrective Orders…

a) Having identified the above weaknesses through on-site and off- site examinations, six banking institutions were issued with corrective orders in line with the Troubled and Insolvent Bank Policy. The corrective orders required the banking institutions, among other issues to:

i) inject additional capital;

ii) enhance corporate governance practices in line with the Banking Act, Banking Regulations and the Corporate Governance Guideline;

iii) enhance board and senior management oversight;

iv) ensure the stepping down of board members and senior management who had been responsible for the problems facing their banks; and

v) put in place risk management systems to measure and manage liquidity, credit and market risks.

Curatorship and Liquidations…

i) Failure to adhere to corrective orders and capital demands left the Reserve Bank with no option but to either place the affected banks under the management of a curator or liquidator. Curatorship is aimed at protecting the interests of depositors and creditors, while the curator determines the full extent of the problems faced by the institutions before recommending the way forward.

ii) During the year 2004, nine (9) banks were placed under curatorship, and three banks were placed under liquidation.

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a) Intermarket Discount House

i) The discount house was placed under curatorship on 12 March 2004 following a determination by the Reserve Bank that the bank was facing serious solvency and liquidity challenges.

ii) It was further determined that the institution had poor corporate governance structures and inadequate risk management systems as evidenced by the significant amount of non-performing loans of $209 billion of which insider loans amounted to $185.59 billion. The required provisions on the loans resulted in a capital deficit of $186 billion.

iii) The insider loans were not granted at arms' length and were not supported by any documentation. The loans had been characterised by continuous roll-overs of both capital and interest.

iv) In addition, the institution was heavily involved in speculative activities on the stock exchange using short-term funds which led to serious asset-liability mismatches.

b) Intermarket Banking Corporation

i) The bank was placed under curatorship on 12 March 2004 after a determination by the Reserve Bank that the bank had insurmountable liquidity and solvency problems. The curator's report dated 31 May 2004 revealed that the bank had a capital deficit of $41.1 billion and funding gaps of around $27.3 billion.

ii) Poor corporate governance structures were at the centre of the liquidity challenges faced by the bank. Most exposures in the Private Banking Division were non-performing intra-group and related party exposures which had been granted without following the institution's own internal policies and procedures. These exposures amounted to $4.47 billion, which constituted 33% of total loans and advances.

iii) The bank was also engaged in speculative non-banking activities such as the purchase of land for $6.4 billion and the acquisition of shares on the Zimbabwe Stock Exchange worth $2.3 billion. The bank employed short-term funds to finance these positions, which culminated in serious liquidity challenges.

c) Intermarket Building Society

i) The building society was placed under curatorship as a result of exposure to an associate company, Intermarket Discount House, emanating from forced placements with the discount house by the Group Chairman.

ii) The breakdown in corporate governance structures enabled the Group Chairman to issue a directive to the effect that 60% of all investments by the Society had to be invested within the Intermarket group on an unsecured basis. This resulted in the building society being exposed to the discount house to the tune of $28 billion.

iii) Apart from the imprudent exposure to related parties, the building society had

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viable operations. In this respect, the society was reopened in April 2004 to offer limited services to the public following a recommendation by the Curator to that effect.

d) Barbican Bank

i) The bank was placed under curatorship on 15 March 2004 after an investigation conducted by the Reserve Bank determined that the institution was insolvent with a capital deficit of $46.6 billion, as at 31 January 2004.

ii) The problems that faced the bank were all linked to poor corporate governance practices. There was no separate and independent board for the subsidiaries and the holding company.

iii) The institution mixed non-banking activities and banking business.

iv) The bank abused the Reserve Bank liquidity support by funding non-banking activities such as the purchase of shares in various counters on the stock exchange.

v) The bank was also engaged in fraudulent foreign exchange activities to fund the operations of its foreign subsidiaries based in South Africa and Botswana.

e) Royal Bank

i) The bank was placed under curatorship on 4 August 2004 after the Reserve Bank determined that it was facing serious solvency and liquidity problems. This was reflected by a capital deficit of $27.6 billion.

ii) The capital deficit was mainly attributed to non-performing loans amounting to $28.3 billion, of which insider loans amounted to $23.1 billion.

iii) The bank failed to inject the required additional capital amounting to $140.1 billion, required to meet maturing liabilities, extinguish the Reserve Bank liquidity assistance facility.

f) Trust Bank

i) The bank was placed under the management of a curator on 23 September 2004 after various attempts to resuscitate the bank failed.

ii) The bank had been facing serious liquidity and solvency challenges emanating from rapid expansion without a corresponding increase in capital, as well as high levels of non-performing loans.

iii) Additional challenges included poor corporate governance structures which resulted in poor asset and liability management. The bank was also engaging in non-banking activities through a special purpose vehicle, TMB Nominees. The bank's capital deficit increased to $1.14 trillion as at 31 July 2004 as a result of huge losses stemming from poor asset quality and the inhibitive cost of refinancing the huge liquidity net mismatches.

g) Time Bank

i) The bank was placed under the management of a curator on 27 October 2004 after a determination by the Reserve

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Bank that the bank was not operating in a safe and sound manner.

ii) It was determined that although the bank's records indicated a capital base of $14.76 billion as at 31 December 2003, the actual capital position, after reversing interest income of $184.58 billion that had been accrued on fictitious assets, was a negative $174.6 billion.

iii) The source of the liquidity and solvency challenges were loan facilities ostensibly availed to various companies connected to shareholders and directors to fund peri-urban agricultural and property development projects.

h) CFX Bank Limited

i) Following a determination by the Reserve Bank that the institution was facing serious liquidity, profitability and solvency challenges, CFX Bank was placed under curatorship on 17 December 2004.

ii) Bank management were manipulating computer generated financial statements in order to conceal accumulated and current monthly losses. Management also resorted to creation of fictitious assets in order to conceal the losses and funding gaps on illegal foreign exchange deals. The utilisation of depositors' funds to acquire fixed assets further exacerbated funding gaps.

iii) The institution was adversely affected by poor corporate governance as evidenced by numerous unauthorised excesses and imprudent write-offs of interest on insider loans.

i) CFX Merchant Bank

i) The bank was placed under curatorship on 17 December 2004 following a determination that the bank was experiencing liquidity problems. The liquidity challenges emanated from exposures to CFX Bank, amounting to $64.7 billion.

ii) The merchant bank was technically insolvent with a capital deficit of $47.7 billion, which was classified as a loss in view of the challenges facing the commercial bank, and after adjusting for a provisioning shortfall of $4.8 billion.

j) Century Discount House Limited (CDH)

i) The discount house was closed on 2 January 2004 after a determination by the Reserve Bank that the institution was facing serious liquidity problems. The financial challenges were occasioned by advancement of funds to ENG Asset Management Private Limited amounting to $32.8 billion. ENG Capital, the holding company of ENG Asset Management Limited, had acquired CDH Limited from Century Holdings Limited without regulatory approval.

ii) The owners of ENG Capital had siphoned depositors' funds from CDH to fund speculative activities, which included investments on the stock exchange and real estate. The required provisions on these exposures, which were non-performing, coupled with unaccounted for assets of $21.6 billion, resulted in a capital deficit of

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$50.3 billion. In view of the serious liquidity and solvency challenges that ensued from the asset–liability mismatches, the discount house was placed under liquidation on 2 January 2004.

k) Rapid Discount House

i) The discount house was placed under curatorship on 26 March 2004 after it was determined that it was facing serious liquidity and solvency problems emanating from non-performing insider loans amounting to $20 billion. Most of these loans were disguised as Negotiable Certificates of Deposit (NCDs) purportedly issued by other banking institutions, in a bid to mislead the regulatory authority.

ii) The discount house had a capital deficit of $24 billion after adjusting for insider loans of $6.92 billion and specific provisions for bad and doubtful debts.

iii) Existing shareholders failed to inject the required capital and various attempts to recapitalise the institution did not materialise. In view of this, the Reserve Bank was left with no option but to pursue the liquidation route. The final liquidation order was granted on 1 December 2004.

3.18 ON-SITE EXAMINATIONS ON ASSET MANAGEMENT COMPANIES

3.18.1 Nine on-site examinations were conducted during 2004. All the institutions, with the exception of one, were found to be carrying out non-permissible activities in the form of lending and taking positions with clients' funds.

3.18.2 Further, on–site examinations on unlicensed asset management companies were conducted during the year under review. The objective was to determine whether institutions whose licensing applications were rejected were winding up as per the Reserve Bank directive.

3.18.3 The examinations revealed that the institutions were winding up except for a few which had filed appeals with the Reserve Bank. These institutions were later followed up after confirmation of their rejections to ensure that they were winding up as directed by the Reserve Bank.

3.19 MAJOR FINDINGS FROM ON-SITE EXAMINATIONS OF ASSET MANAGEMENT COMPANIES

a) Non-permissible Activities

Lending...

i) The on-site examinations conducted on asset management companies revealed that most of these institutions were conducting non-permissible activities. Some of the institutions were found to be issuing out loans in violation of the Banking Act.

ii) Issuing of loans in whatever form is not permitted under the Asset Management Act as asset managers are required to transact as agents for and on behalf of their principal who are their clients. It, therefore, follows that their revenue should be fee-and

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commission-based as is typical of a principal-agent relationship.

iii) In a bid to circumvent supervisory scrutiny of asset management companies sticking to their core business some asset management issued out loans disguised as commercial paper, in order to sustain their operations.

iv) The sector is facing viability challenges as the scope of asset management business in Zimbabwe appears limited. The business is volumes driven and given the size of the market and the number of asset managers, there is limited scope for new business and growth.

Taking positions with clients funds…

i) On-site examinations also revealed that instead of relying on commissions, some asset managers were quoting rates upfront and placing investors' funds in the market for a margin. Such activities are tantamount to conduct of banking business without the requisite license and this is in contravention of the Banking Act.

ii) Asset managers are different from banks in that while both act as financial intermediaries, banks accept deposits and transform the same into loans and investments. The relationship between banks and their customers is that of debtors and creditors, hence credit risk and loss of value in investments lies with the bank.

iii) On the other hand, asset managers and their clients transact on an agent-principal basis and are not permitted to take investors' funds on their balance sheet.

iv) Further, default risk and loss of asset value lies with the investor as asset managers are mere agents of their principal (who are the investors). This is the primary reason why the minimum capital requirements for asset managers are lower than those for banking institutions.

Non-separation of Company and Client reporting…

i) The examinations also noted that there was no separation of company and client reporting as required of asset managers. In a number of cases, the asset managers were found investing funds without clear mandates from the investors and in the process, mixing company funds and investors' funds. Consequently, clients' funds lose identity in the process which could result in abuse of the funds.

b) Corporate Governance

i) The examinations also revealed that a number of asset managers had corporate governance weaknesses which included improperly constituted boards, poor board oversight, inexperienced management and undue influence from owner managers.

3.20 SUPERVISORY ACTION ON ASSET MANAGEMENT COMPANIES

Corrective Orders…

Following identification of the above weaknesses and improper conduct, five asset

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management companies were issued with Corrective Orders during the year 2004, requiring them among other things to:

i) cease and desist from conducting non-permissible activities;
ii) regularise board composition and management in line with provisions of the Corporate Governance Guideline;
iii) recapitalise the institutions to the required minimum capital levels; and
iv) enhance risk management systems and processes

Closures and Winding up…

i) Some asset managers failed to comply with provisions of the corrective orders, while others were found to be critically undercapitalised such that their continued existence in the market was not warranted and the Reserve Bank had no option but to cancel their licences.
ii) As a consequence, in early 2005, five asset managers had their licences cancelled and one was placed under curatorship. The affected institutions were Sunshine Unit Trusts Management Company, GP2 Asset Management, Imperial Management Company and Renaissance Asset Management Company. First Factoring Company of Zimbabwe surrendered their licence citing viability challenges. CFX Asset Management Company was placed under the management of a curator when CFX Bank Limited was placed under curatorship in December 2004.

CHAPTER FOUR
CORPORATE GOVERNANCE AND COMPLIANCE

4.1 OVERVIEW

4.1.1 The Governor's monetary policy of 18 December 2003 set a new tone on corporate governance standards in the financial sector.

4.1.2 The new Corporate Governance regime has had a significant impact on our banking sector as witnessed by a number of changes in board composition.

4.1.3 Corporate governance relates to the manner in which the business of enterprises is directed and controlled, how the corporate objectives are set, and how the corporate activities and expectations of stakeholders are aligned.

4.1.4 The significance of corporate governance is now widely recognised as essential for national prosperity, corporate competitiveness and good corporate citizenship. In fact, the King Report II of 2002 put great emphasis on corporate discipline, transparency, independence of board members and committees, fairness, accountability and social responsibility as essential pillars of good corporate governance.

4.1.5 The state of corporate governance in a country is thus critical for financial and economic development of the nation as a whole.

Maiden Monetary Policy Statement…

4.1.6 In the period prior to this monetary policy, Zimbabwe's financial sector had endured a period of unprecedented challenges as the financial sector grappled with the harsh conditions brought about by the volatility in Zimbabwe's economic environment.

4.1.7 In his maiden Monetary Policy of December 2003, the Governor, Dr. Gideon Gono announced that:

4.1.8 *'As Monetary Authorities, the Bank will not stand by and watch without consequence, malpractices taking place within financial institutions under its jurisdiction. The financial sector is, therefore, forewarned and is expected to uphold sound corporate governance standards. Only by encompassing sound corporate governance practices can we maintain soundness, and the prosperity of the financial sector which in turn will guarantee same to the economy as a whole'.*

4.1.9 The significant changes initiated through the Reserve Bank's introduction of innovative, stringent monetary policy measures, served to unearth a cesspool of corruption, speculative and abusive practices that underpinned the failure of countless players in Zimbabwe's financial sector.

4.1.10 Tough supervisory intervention was not only necessary, but long overdue.

4.2 STEPS TAKEN TO ADDRESS CORPORATE GOVERNANCE FAILURES

Refocus: Tightened Supervision & Surveillance…

4.2.1 In the context of the monetary policy regime ushered in by the Governor, Dr G. Gono, beginning in December 2003, the Reserve Bank

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enhanced the supervision and surveillance over corporate governance systems and structures.

4.2.2 On-site and off-site surveillance was refocused, with the creation of a new unit within Bank Licensing, Supervision and Surveillance, specifically dedicated to Corporate Governance compliance issues.

4.3 CORPORATE GOVERNANCE AND COMPLIANCE UNIT

4.3.1 The Corporate Governance and Compliance Unit was set up in August 2004 to monitor compliance with laws, rules, and regulations, and to promote effective corporate governance systems in financial institutions, in line with international best practice.

4.3.2 The key objectives of the unit include:

a. to instill a culture of strict compliance within the financial sector and internally within BLSS.
b. to enforce compliance both internally and externally, with statutes, rules, regulations, directives, processes, policies and procedures etc, in order to promote market discipline and protect the integrity of the financial sector;
c. to continuously review the regulatory and supervisory framework with a view to ensuring the effective monitoring and supervision of the financial sector; and
d. to increase focus on internal controls and corporate governance systems and structures during onsite examinations.

4.4 INITIATIVES TAKEN TO ENHANCE MARKET DISCIPLINE AND CORPORATE GOVERNANCE

4.4.1 In a bid to further enhance corporate governance practices and instill market discipline the Reserve Bank issued the following guidelines:

- Corporate Governance;
- Minimum Internal Audit Standards in Banking Institutions;
- Framework on the Relationship Between Bank Supervisors and Banks' External Auditors; and
- Accreditation of Credit Rating Agencies.

4.5 CORPORATE GOVERNANCE GUIDELINE

4.5.1 The Guideline on Corporate Governance No. 01 - 2004 BSD was issued in September 2004. The Guideline covers the key corporate governance areas in respect of financial institutions that will be monitored by the Reserve Bank. The following are major highlights of the guideline:

Board Composition and Separation of Owners from Managers…

4.5.2 The Guideline calls for the appointment of independent chairpersons, a balance of power by calling for separation between the chairperson and chief executive officer, with the appointment of independent non-executive directors and boards comprising of technically competent persons of impeccable integrity with a strong sense of professionalism. It was noted in the failed banks that it was the owner managers who abused controls as they had unfettered authority.

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4.5.3 In order to address this cancer, the Reserve Bank stipulated in clause 2 of the Corporate Governance Guideline that no shareholder with a 10% or more shareholding in a banking institution would be appointed Chairperson, Deputy Chairperson, nor form part of management. Further, no individual shareholder who had significant shareholding in a failed institution or anyone previously involved in the running of a failed institution would be allowed to hold a significant shareholding in a banking institution or to hold a position of accountability in a banking institution.

Board Committees…

4.5.4 Boards of directors are required to set up committees to provide assistance in discharging their duties and responsibilities. However, the board remains accountable.

Appointment and Disqualification of Directors and Management…

4.5.5 Financial institutions are required to seek prior written consent of the Reserve Bank on appointment of a chief executive officer or chief accounting officer as stated under section 20 of the Banking Act. The Corporate Governance Guideline calls for the appointment of fit and proper persons. It provides for disqualification of persons who have been involved in the directorship or management of a failed banking institution and or bank holding company, were directors of liquidated institutions, associated with incompetence, lack of integrity and unsoundness of judgment, are on suspension or dismissal or have been adjudged insolvent.

4.5.6 The Division has tightened its vetting structures and procedures. All directors of banking institutions are required to file with the Division affidavits in respect of the fit and proper test.

Practicing Lawyers and Accountants…

4.5.7 Practising lawyers and accountants may be appointed as directors of a financial institution provided that they are not employed by or are not partners in a legal or accounting firm which is engaged to provide the particular financial institution with professional services.

4.5.8 Practising lawyers and accountants who are appointed as directors of financial institutions are expected to exercise the highest degree of integrity and professionalism.

Board and Director Evaluations…

4.5.9 The Board, through an appropriate committee is required to regularly review its mix of skills and experience and other qualities such as demographics and diversity in order to assess the effectiveness of the board.

4.5.10 Such evaluations may be by means of peer and self evaluation of the board as a whole, its committees and the contribution of each and every director, including the Chairman, on an annual basis.

Other directorships…

4.5.11 Directors of banking institutions are prohibited from having interlocking directorships between banking institutions that operate in competition with each other to avoid conflict of interest in the

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management of two or more institutions. This is in line with section 19(1)(b) of the Banking Act.

4.5.12 As part of the vetting process, directors are also required to disclose their directorships and shareholdings in other companies. The Guideline has provided guidance on how the number of other directorships is computed to ensure compliance with section 19(1) of the Banking Act which limits the maximum number of additional directorships to not more than seven.

Board Attendance…

4.5.13 The guideline highlights the requirement for directors to play an active role on their boards by setting a minimum 75% attendance rule, compliance to which must be disclosed in the institution's annual report. The Reserve Bank monitors this requirement and requires institutions to review the suitability of directors that do not treat their duties with the seriousness they deserve.

Financial Disclosure…

4.5.14 The Guideline further highlights the role of comprehensive financial disclosure requirement for corporate and banking institutions to complement sound corporate governance, strengthen accountability and enhance risk management incentives. Proper financial disclosure helps the market and observers to monitor the soundness of their performances and take appropriate action against those that fail to meet prudential expectations.

4.6 GUIDELINE NO.2-2004/BSD: MINIMUM INTERNAL AUDIT STANDARDS IN BANKING INSTITUTIONS

4.6.1 The role of the internal audit function in financial institutions is to provide an independent and objective appraisal of the institution's activities as a service to management. This guideline serves to provide internal auditors with the minimum standards required of the internal audit function in terms of:-

a) **organisation of the function** with emphasis on independence and objectivity;
b) **reporting lines** – the function is required to report administratively to the Chief Executive Officer and functionally to the Audit Committee;
c) **professional proficiency** – cognisance should be given to the internal audit function's requirements in terms of appropriately qualified and skilled resources, training, and continuing professional education;
d) **minimum standards** of ethics and due professional care required;
e) **maintaining proper relationship and communication channels** with management, external auditors and the Reserve Bank, including the monitoring of corrective actions taken by management in response to Reserve Bank examination findings; and
f) **audit governance** – the right set of implementation tools should be in place to assist the function to discharge its functions effectively, including the audit charter, plan, manual, programme and internal control questionnaires.

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4.6.2 Minimum scope of audit work and reports expected, including coverage of the following key areas:
(a) evaluation and appraisal of the Internal Control System;
(b) compliance with policies, procedures, rules, guidelines, directives, laws and regulations;
(c) adequacy and effectiveness of risk management system;
(d) effective and efficient use of resources;
(e) accomplishment of set goals and objectives; and
(f) effectiveness and independence of the Compliance Function.

4.7 FRAMEWORK ON THE RELATIONSHIP BETWEEN BANK SUPERVISORS AND BANKS' EXTERNAL AUDITORS

4.7.1 This Framework sets out the rationale for formal co-operation between bank supervisors and external auditors in that it contributes to enhancing the risk-focused approach to bank supervision. The guideline facilitates mutually beneficial synergies between external auditors and bank supervisors. It covers *inter alia,* the role of external auditors, their independence, their reporting responsibilities in relation to the Reserve Bank, and the framework for on-going dialogue between external auditors and the Reserve Bank.

The Role of External Auditors…

4.7.2 External auditors express an objective opinion on whether the bank's financial statements give a true and fair view of the bank's financial position and make recommendations to the board of directors. They are expected to perform their duties with due care and skill commensurate with the complexity of the engagement.

4.7.3 External auditors shall not be exonerated by disclaimer clauses in the statements they endorse if they contain material errors and gross misrepresentation.

Independence of External Auditors…

4.7.4 External auditors are expected to maintain their objectivity and independence by ensuring they avoid providing non-audit / consulting services to, or borrowing from, banking institutions and bank holding companies that they audit. External auditors are expected to ensure that they are not involved in the management or decision making of the banking institution. Further, the audit firm should diversify its clientele base in order to avoid over-reliance on fees from one banking institution or group of connected institutions. Annual audit fees derived from an audit performed on a banking institution or group of connected institutions are also limited to not more than 10% of the total gross fees of the firm as a whole, or as shall be determined from time to time by the Reserve Bank in consultation with relevant stakeholders.

Reporting…

4.7.5 External auditors are required to report promptly to the Reserve Bank, in terms of section 43 of the Banking Act, irregularities or illegal acts that may have been committed by any director of the financial institution or any person whose activities may significantly damage the financial institution's financial stability.

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Meetings between the Reserve Bank and External Auditors…

4.7.6 The co-operation between the Reserve Bank and external auditors takes various forms:

(a) periodic bi-lateral meetings between the supervisor and external auditors;

(b) tripartite meetings with the auditors and the bank, and bilateral meetings with the auditors are conducted; and

(c) exchange of specific information.

4.8 GUIDELINE NO. 04-2004/BSD: ACCREDITATION OF CREDIT RATING AGENCIES

4.8.1 The Accreditation Guideline provides that no person, other than an accredited credit rating agency, is permitted to conduct or assign a credit rating to a banking institution conducting banking business in Zimbabwe. Each banking institution operating in Zimbabwe is required to be rated by an accredited credit rating agency at least once a year.

4.8.2 The Credit Rating Agent is accredited by the Reserve Bank.

4.8.3 Credit Rating Agencies assess the credit risk of corporate or government borrowers and issuers of fixed income securities. Credit Rating Agencies may provide credit ratings for different types of debts and financial obligations including, for instance, private loans and debt securities that are not publicly traded, zero coupon bonds, preference shares and other securities that offer a fixed rate of return.

4.8.4 The work of rating agencies is complementary to regulatory efforts of promoting financial stability and protecting the interests of investors and creditors.

4.8.5 Credit ratings also instil market discipline which in turn enhances corporate governance and risk management systems for the financial institutions.

4.8.6 Credit Rating Agencies facilitate the realisation of regulatory objectives of protecting investors, maintaining fair, efficient and transparent markets, and reducing systemic risk.

Eligibility criteria for accreditation…

4.8.7 In terms of the guideline the following are the minimum eligibility criteria that must be met by credit rating agencies seeking to be accredited by the Reserve Bank:

(i) registered company;

(ii) proven track record and experience;

(iii) professional competence and integrity;

(iv) adequate infrastructure;

(v) adequate internal practices, policies and procedures, encompassing:

(a) disclosure of rating scales and definition;

(b) quality and integrity of the rating process;

(c) factors considered in rating methodologies;

(d) agreements with clients;

(e) policies on rating actions;

(f) content and depth of rating reports; and

(g) development of sound database and research capacity.

CHAPTER FIVE
TROUBLED BANK RESOLUTION FRAMEWORK

5.1 DUTY TO MAINTAIN FINANCIAL STABILITY

5.1.1 The Reserve Bank has a responsibility to ensure that those troubled banking institutions that can be saved from failure are saved, and those that cannot be saved are allowed to exit in an orderly fashion. This is consistent with the Reserve Bank's statutory mandate to maintain financial stability and promote economic development, underpinned by price and exchange rate stability.

5.1.2 Efficient financial intermediation helps to promote economic prosperity via enhanced mobilisation of savings, asset transformation, allocative efficiency, screening and monitoring projects, risk transfer and sharing, enforcement of contracts and good corporate governance, and improved total factor productivity.

5.1.3 Unsound financial institutions are detrimental to the financial health of any nation and its citizens. Insolvent financial institutions are prone to poor risk management practices, creative accounting, and poor corporate governance practices.

5.2 BANK INSOLVENCY

5.2.1 The insolvency of banks has consequences that go beyond losses for the shareholders and creditors of the banks. Bank insolvency leads to loss of confidence in the financial system, capital flight, and high interest rates. Insolvent banks pay depositors any interest rate to attract deposits and remain liquid. This results in extremely high lending rates and poor asset quality.

5.2.2 Bank insolvency is a problem that should be addressed to avoid systemic insolvency. If regulatory authorities follow a *laissez faire* approach to systemic bank insolvency, all depositors will withdraw their funds from the banking system, resulting in the collapse of the financial system. This is one reason why financial stability is a goal of public policy.

5.2.3 There is no doubt that financial safety is required to unleash positive reactions in the real sector. As such, there is need to resolutely deal with troubled and insolvent banking institutions in order to maximise the contribution of the financial system to economic growth and poverty alleviation.

5.3 TROUBLED BANK FUND

5.3.1 At the height of the problems in the banking sector, the Reserve Bank, created the Troubled Bank Fund (TBF), and through the fund, used public funds (i.e. tax payers' funds) to resolve solvency and liquidity deficiencies in privately-owned banking institutions.

5.3.2 A number of banking institutions that benefited from the Troubled Bank Fund not only failed to repay the loans, but also failed to recapitalise, or to conclude various merger talks that they had gone into. A Capital Verification Exercise undertaken by the Reserve Bank confirmed that these institutions had no capacity to inject the required resources, despite being granted time within which to do so.

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5.3.3 When faced with the imminent collapse of no less than nine banking institutions in the year 2004, it was clear to the Reserve Bank that liquidation of those institutions was not a feasible option as it would have resulted in serious losses to depositors who stood to recover only a few cents for each dollar deposited in the troubled institutions.

5.3.4 At the same time, the resultant erosion of confidence in the banking sector would result in the loss of a vital source of credit, the high cost of deposit insurance, and ultimately destabilise the economy. The Reserve Bank then formulated a comprehensive Troubled Bank Resolution (TBR) framework to address problems in the banking sector in a holistic fashion.

5.4 OBJECTIVES OF TROUBLED BANK RESOLUTION FRAMEWORK

5.4.1 The Troubled Bank Resolution framework was designed to achieve the following key objectives:

a) strengthen the banking system and promote sound banking practices;
b) develop permanent solutions for troubled banking institutions;
c) promote economic development and growth;
d) restore stability of the financial sector; and
e) preserve indigenisation of the financial sector.

5.5 RESOLUTION TECHNIQUES APPLIED

5.5.1 The Reserve Bank adopted a two-pronged approach to deal with problem banks in the banking sector, which involved:

a) restructuring of the troubled institutions which included amalgamation of institutions, as well as mergers and acquisitions; and
b) liquidation.

5.6 FORMATION OF ZIMBABWE ALLIED BANKING GROUP (ZABG)

5.6.1 The Reserve Bank created a Special Purpose Vehicle (SPV), Allied Financial Services (Pvt) Ltd, which facilitated the conversion of debt in troubled banks into equity. Troubled banking institutions that qualified were then consolidated into a single entity known as Zimbabwe Allied Banking Group (ZABG), which was granted a banking licence and commenced business on 31 January 2005.

Cession of Debt to Government…

5.6.2 In terms of the resolution framework adopted, the Troubled Bank Fund debt was converted into equity in the troubled banks. In appreciation of the fact that it is not desirable for the Reserve Bank to own financial institutions which it supervises, and the need for the Reserve Bank to remain separate from the institutions it regulates, monitors and supervises, the Reserve Bank ceded the TBF debt to Government, through Allied Financial Services (Pvt) Ltd.

5.6.3 The result was that the banking sector stabilisation costs were borne by Government, not the central bank, in line with international best practice. This approach has been used in many countries such as Norway, Spain, Malaysia, Indonesia, Chile, Argentina and Brazil, among others.

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Government's Divesture...

5.6.4 Government therefore owns shares in ZABG, through the special purpose vehicle Allied Financial Services (Pvt) Ltd. It is expected that Government will fully divest from ZABG by 2007, by which time full economic turnaround will have been achieved.

5.6.5 Determination of residual shareholding value in troubled banking institutions was being undertaken by independent professionals in the interest of transparency and accountability. The residual value will determine the eventual shareholding of existing shareholders in ZABG.

Mandate and objectives of ZABG...

5.6.6 ZABG was created to resolve the problems of solvency and liquidity experienced by the banking sector in 2003 and 2004, which if left unchecked, could have resulted in a systemic crisis.

Three banks amalgamated...

5.6.7 ZABG, upon licensing in January 2005, amalgamated three troubled banks - Trust Bank, Royal Bank, and Barbican Bank into a single unit, and commenced business on 31 January 2005.

5.6.8 **In this endeavor, Government and the Reserve Bank hope to achieve the following objectives:**

i) to resolve liquidity and solvency challenges in distressed institutions;
ii) to protect creditors and depositors;
iii) to create a platform for indigenous investors to acquire shares in sound banking institutions;
iv) to minimise moral hazard and promote prudent banking practices;
v) to promote strong corporate governance, accountability and shareholder oversight; and
vi) to create strong banking institutions able to withstand competitive challenges in the market.

Financing of ZABG...

5.6.9 ZABG was initially financed through the conversion of the RBZ Troubled Bank Fund and the claims of other creditors and depositors into equity.

Stratification of Deposits...

5.6.10 Deposits in troubled institutions were stratified into three categories to facilitate their conversion into equity: i.e. small deposits (< $5m), medium sized deposits ($5m to $50m), and large deposits (above $50m).

5.6.11 A close analysis of the deposit profiles of troubled banking institutions revealed that there was an inverse relationship between the number of clients per deposit strata and the value.

Majority of Customers Got their Money Back...

5.6.12 All depositors in the three banking institutions were paid cash from their deposits up to a maximum of $5 million per account. These payments were made by the curators of the respective banks from 24 to 29 January 2005.

Shareholder value lost...

5.6.13 In the interests of preserving financial stability, banks warrant special treatment, at registration and in liquidation. After assessment and valuation

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of an institution it may become clear that shareholder value has been lost. This was the case in relation to the three banking institutions, where the extent of negative equity in the institutions amounted to $1.45 trillion.

5.6.14 The liquidation of banking institutions is different from that of a company and requires special rules. A recent study by the IMF determined that international practice supports the usage of a special insolvency regime for banking institutions. The banking laws of the USA, Switzerland, Austria, Germany, and Luxemburg contain special bankruptcy provisions for the reorganisation or liquidation of financially distressed banks.

Conversion to shares…

5.6.15 Balances above $5 million prior to the above payments were converted into shares using a progressive scale as follows:

i) Up to $50 million : 545-day preference shares (Class A);
ii) $50 million to $100 million : 730-day preference shares (Class B); and
iii) above $100 million : Ordinary shares

5.6.16 Upon being called upon to convert their claims to equity, over 70% of depositors in the three troubled institutions elected to convert their deposits as at 31 March 2005.

5.6.17 Investment opportunities will also be available for new investors who wish to hold equity in the new bank. This presents an opportunity for corporate investors who are keen on investing in the banking sector to come on board and take up equity.

Bank insolvency different from commercial bankruptcy…

5.6.18 Company law generally provides creditors with a more active role than is the case under banking law. What distinguishes a bank's insolvency from a commercial bankruptcy is that the former may entail risk to the entire economic system propagated through the insolvent bank's counter-parties. The challenge faced in formulating Troubled Bank Resolution strategies outlined herein was to strike a balance between the differing objectives of banking law and company insolvency law.

5.6.19 Problem bank resolutions often entail the use of public funds in order to minimise systemic risk, rendering Government "the owner of last resort". Such solutions would imply a capital transfer from the government to the bank shareholders without any corresponding input on the part of the shareholders. The situation in Zimbabwe was no different, hence the aim of the bank resolution strategies to save the financial system and not to support the troubled banking institutions' shareholders.

5.6.20 Where public funds are used to provide solvency support to TBIs, international practice requires shareholders of the TBIs to write down their shareholding to a specific figure, which could even be zero, in accordance with the banking institution's losses.

5.6.21 This approach was successfully used in Norway

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(1991), Spain (1980), and Jamaica (1997), to render it possible to restructure banks in an orderly fashion as well as penalise incompetent shareholders.

5.6.22 In the SADC region, Zambia, for instance, has provisions in her banking laws which authorise termination of shareholders' interests in banking institutions taken over by the Central Bank.

5.6.23 Namibian banking laws prohibit persons who are not fit and proper from becoming significant shareholders in banks.

5.6.24 In addition, international best practice proposed by the Basel Committee on Banking Supervision supports this approach, especially where public funds are used to provide solvency support to Troubled Banking Institutions (TBIs). These provisions force shareholders of TBIs to take banking institutions' losses into account before recourse to taxpayers' money.

Basis for writing down shareholding…

5.6.25 In the ordinary course of banking business, losses are written off against the profit and loss account in the first instance. Where this is not enough, losses are then written off against capital. Capital is therefore a cushion against unanticipated losses. Prudence and good accounting practices necessitate the adjustment of financial reports to reflect realised losses.

5.6.26 For instance, if audited financial results of Bank A, with a capital base of $10 billion, show that $7 billion of equity has been lost, its capital should be reduced to $3 billion after writing off the losses, other things being equal. A capital injection of $7 billion will be required to restore the banking institution's capital base to its original position.

5.6.27 However, if Bank B, with an identical capital base of $10 billion, posts losses amounting to $25 billion, it will have a negative capital position once the losses are written off against capital. In fact there is no doubt that substantial losses depreciate the value of shareholders' investment in a corporate entity, banking institutions included.

5.6.28 Conceptually, an insolvent banking institution's liabilities exceed its assets. In practical terms, an insolvent banking institution's net worth position reflects net liabilities to depositors and creditors, rather than assets. Notwithstanding the legal protection available under the "Limited Liability Concept" shareholders of insolvent banking institutions have lost value via diminution of equity, and on aggregate actually have obligations to, rather than claims against, their counter-parties.

5.6.29 It follows that prudential considerations and good accounting practices necessitate the adjustment of financial reports to reflect realised losses and/or diminution in equity. In essence, writing down shareholding to the extent of a banking institution's losses merely follows the need for fair valuation of assets to its logical finality. This was therefore an essential component of the Troubled Bank Resolution Framework adopted.

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5.6.30 In addition, banking laws all over the world preclude individuals who are no longer fit and proper from continuing to direct the affairs of a banking institution. The requirement for banking institutions to have fit and proper shareholders, officers and employees does not only apply at registration stage, but continues to have potency and force on an on-going basis.

5.6.31 Ideally a proposal to write down the share capital (or sum of the primary capital fund organised in a manner other than as in a limited company) against losses shown in audited financial statements should be effected following a resolution passed by simple majority at a general meeting. Some countries, notably Norway, have put in place appropriate banking laws to enable Regulatory Authorities to effect the writing down of shareholding if the general meeting of shareholders fails to pass the required resolution.

Changes in the law...

5.6.32 When the need to formulate a resolution strategy for the troubled banks became apparent, it also became clear that the legal framework in place could not adequately support the Troubled Bank Resolution Framework conceived. It therefore became necessary to formulate legislation to effectively and successfully implement the framework. The Banking Act has limitations in that it was promulgated at a time when the magnitude of banking sector problems experienced in 2004, and the need to find new and different solutions for troubled banking institutions, were not foreseen.

5.6.33 The legal framework that was then proposed had adequate provisions to enable the creation of the Zimbabwe Allied Banking Group (ZABG), in order to resolve the problems of solvency and liquidity being experienced by the banking sector.

Enabling provisions...

5.6.34 The Troubled Financial Institutions (Resolution) Bill, 2004 went through Parliament in December 2004, and became law in January 2005. It is now known as the Troubled Financial Institutions (Resolution) Act, [Chapter 24:28], and enables the Reserve Bank to issue an order declaring a financial institution to be troubled, and to proceed to appoint an administrator and such assistant administrators as may be required.

5.6.35 The powers of the administrator include amalgamating various troubled banking institutions to set up a successor financial institution, the valuation of shareholding and the writing down of liabilities to the extent of losses incurred by a troubled banking institution, the appointment of an interim board etc.

TBRF implementation – ZABG…

5.6.36 A board comprising experienced professionals, led by Mr. Cornelius Sanyanga, provides effective oversight on the bank's operations. ZABG has put in place adequate structures and board committees as required by Corporate Governance guidelines issued by the Reserve Bank during the year under review.

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Infrastructure…

5.6.37 The amalgamations undertaken in ZABG need to be properly managed to minimise integration risk that is associated with merging different corporate cultures, processes and systems. Pertinent issues to focus on include management, infrastructure, deposits and staff.

5.6.38 The infrastructure of ZABG takes into account the existing branch network and geographical distribution of the banking institutions amalgamated as divisions of ZABG.

5.6.39 ZABG has a widely distributed branch network to ensure convenient access to financial resources by the general populace of Zimbabwe.

5.7 OTHER MERGERS AND ACQUISITIONS

5.7.1 Some of the institutions that were placed under curatorship in 2004, as reported elsewhere in this Report, were left out of ZABG due to the fact that merger initiatives with other market operators were in the offing.

5.8 LIQUIDATION

5.8.1 In cases where the cost of resuscitation far outweighs the benefits that will accrue to the economy, the TBRF recognises the need to earmark institutions falling in this category for liquidation.

5.8.2 In the TBRF implementation, Rapid Discount House was identified as one such institution, and was accordingly placed under final liquidation by the High Court in the final quarter of 2004.

5.9 CHALLENGES IN TBRF IMPLEMENTATION

5.9.1 The implementation of the TBRF has not been without its challenges, chief of which is the legal challenge taken to the High Court in the first month of operation of ZABG. Former shareholders in Trust Bank and Royal Bank challenged the amalgamation of the two banks in ZABG, which challenges were dismissed by the High Court.

5.9.2 The High Court's decision was challenged on appeal in the Supreme Court, and judgment of the two matters is still outstanding.

5.10 CONCLUSION

5.10.1 The TBRF is designed to achieve financial stability, preserve indigenisation of the financial sector, and to promote sound banking practices and effective market discipline.

5.10.2 As in all ground-breaking initiatives, there is a great deal of scope for learning "on-the-job", and need to modify blue-prints where necessary in order to ensure the attainment of the main objectives. The TBRF and its implementation continue to present opportunities for us to fine-tune our processes, which, we believe, is a positive thing as it strengthens regulatory and supervisory preparedness and capacity to deal with similar challenges in the future.

APPENDIX 1 - STATISTICAL TABLES

TABLE 1A
COMPOSITION OF THE BALANCE SHEET (As at 31 December, 2004)

COMMERCIAL BANKS																										
ASSETS	**AGRIBANK Z$million**	**%**	**BARCLAYS Z$million**	**%**	**CBZ Z$million**	**%**	**FBC Z$million**	**%**	**KINGDOM Z$million**	**%**	**METROPOLITAN Z$million**	**%**	**MBCA Z$million**	**%**	**NMB Z$million**	**%**	**STANBIC Z$million**	**%**	**STANCHART Z$million**	**%**	**ZIMBANK Z$million**	**%**	**COMPOSITE '2003 Z$million**	**%**	**COMPOSITE '2004 Z$million**	**%**
Cash and Due from Banks	18,503.20	2.5	29,365.60	1.0	168,148.75	6.6	19,103.93	4.3	11,504.80	1.8	10,383.35	4.5	27,833.17	4.5	118,173.77	10.4	137,164.68	7.7	126,529.37	3.1	58,521.69	3.5	875,640.09	1.90	725,232.31	4.3
Balances with RBZ	166,019.09	22.5	774,053.16	25.9	411,442.68	16.1	9,064.23	2.0	62,030.31	9.6	8,703.11	3.8	53,137.50	8.7	73,711.61	6.5	481,253.12	26.9	1,022,622.89	25.2	376,475.09	22.8	508,677.37	0.20	3,438,512.79	20.4
Foreign Claims	(1,114.85)	(0.2)	202,910.80	6.8	107,986.54	4.2	35,886.06	8.1	35,758.24	5.5	1,813.62	0.8	86,041.42	14.1	50,879.36	4.5	178,717.80	10.0	40,202.73	1.0	94,843.43	5.7	173,825.38	1.20	833,925.15	4.9
Securities and Investments	104,193.48	14.1	900,418.12	30.1	490,856.09	19.2	24,834.80	5.6	325,102.70	50.3	36,812.88	16.0	10,500.00	1.7	239,201.29	21.0	469,145.63	26.2	1,086,126.40	26.8	498,658.78	30.2	1,104,318.79	56.60	4,185,850.17	24.8
Loans, advances and leases	463,312.99		732,389.61		1,167,322.95		299,421.88		190,936.34		240,977.68		236,862.26		242,156.06		247,411.30		595,461.45		352,635.36		1,914,452.92		4,768,887.88	
Total Provisions	36,567.3		116,825.95		70,004.31		87,764.50		13,400.90		139,624.00		5,653.71		24,450.66		68,773.21		17,152.99		52,040.11		60,190.85		632,257.64	
Net Loans, advances & leases	426,745.69	57.9	615,563.66	20.6	1,097,318.64	42.9	211,657.38	47.8	177,535.44	27.5	101,353.68	44.0	231,208.56	37.8	217,705.40	19.1	178,638.09	10.0	578,308.46	14.3	300,595.25	18.2	1,882,591.37	24.10	4,136,630.25	24.5
Fixed Assets	15,460.13	2.1	22,311.71	0.7	23,552.06	0.9	27,343.91	6.2	24,890.34	3.9	2,955.26	1.3	9,697.90	1.6	19,876.13	1.7	57,110.33	3.2	15,743.24	0.4	31,532.40	1.9	192,859.84	2.70	250,473.41	1.5
Other Assets	7,829.72	1.1	36,722.78	1.2	224,262.02	8.8	14,523.04	3.3	8,076.42	1.3	6,368.42	2.8	16,179.76	2.6	418,392.81	36.8	286,300.27	16.0	62,052.78	1.5	278,141.96	16.8	785,710.27	5.60	1,358,849.98	8.1
Total Book Assets	**737,636.46**	**100.0**	**2,581,345.83**	**86.3**	**2,523,566.78**	**98.7**	**342,413.35**	**77.4**	**644,898.25**	**99.8**	**168,390.32**	**73.1**	**434,598.30**	**71.0**	**1,137,940.37**	**100.0**	**1,788,329.92**	**100.0**	**2,931,585.87**	**72.3**	**1,638,768.60**	**99.2**	**5,523,623.11**	**92.13**	**14,929,474.05**	**88.5**
Off-balance sheet items	0.00	0.0	410,366.75	13.7	32,960.00	1.3	100,199.72	22.6	1,190.31	0.2	61,998.97	26.9	196,600.76	32.1		0.0		0.0	1,124,029.39	27.7	13,712.07	0.8	471,744.75	7.87	1,941,057.97	11.5
Total Assets	**737,636.46**	**100.0**	**2,991,712.58**	**100.0**	**2,556,526.78**	**100.0**	**442,613.07**	**100.0**	**646,088.56**	**100.0**	**230,389.29**	**100.0**	**612,072.64**	**100.0**	**1,137,940.37**	**100.0**	**1,788,329.92**	**100.0**	**4,055,615.26**	**100.0**	**1,652,480.67**	**100.0**	**5,995,367.86**	**100.00**	**16,870,532.02**	**100.0**

LIABILITIES	**AGRIBANK Z$million**	**%**	**BARCLAYS Z$million**	**%**	**CBZ Z$million**	**%**	**FBC Z$million**	**%**	**KINGDOM Z$million**	**%**	**METROPOLITAN Z$million**	**%**	**MBCA Z$million**	**%**	**NMB Z$million**	**%**	**STANBIC Z$million**	**%**	**STANCHART Z$million**	**%**	**ZIMBANK Z$million**	**%**	**COMPOSITE '2003 Z$million**	**%**	**COMPOSITE '2004 Z$million**	**%**
Total Deposits	285,372.78	38.7	1,375,958.09	46.0	1,189,544.69	46.5	135,746.29	30.7	452,748.30	70.1	79,252.25	34.4	107,951.25	17.6	218,644.09	19.2	694,340.92	38.8	1,577,479.00	38.9	771,551.56	46.7	2,869,753.82	47.87	6,888,589.22	40.8
Of Which: Demand Deposits	85,828.43		914,293.30		468,565.76		69,193.31		81,782.85		12,329.69		19,622.65	3.2	168,171.78		473,115.07		1,209,838.83		509,889.49		1,446,927.95		4,012,631.16	
Savings Deposits	74,124.89		94,791.30		65,480.19		11,343.89		16,118.36		2,252.49		0.00	0.0	6,183.57		38,906.15		183,629.59		120,458.58		310,709.43		613,289.01	
Time Deposits	125,418.78		169,223.34		555,702.33		5,525.74		134,867.15		64,630.40		9,527.74	1.6	18,767.93		35,451.50		128.07		87,682.61		820,152.03		1,206,925.59	
FCA Deposits	-	0.68	197,650.15		99,796.41		8,543.98		32,350.00		39.67		78,800.86	12.9	19,012.84		146,868.20		183,882.51		53,520.88		120,165.05		820,466.18	
NCD's	-	0.00	-		-		41,139.37		187,629.94		-		0.00	0.0	6,507.97		-		-		-		171,799.36		235,277.28	
Due to RBZ	98,107.16	13.3	353,638.03	11.8	354,625.79	13.9	20,000.00	4.5	84,111.14	13.0	62,254.13	27.0	37,056.87	6.1	234,273.32	20.6	117,331.46	6.6	114,577.10	2.8	80,587.52	4.9	415,548.89	6.93	1,556,562.52	9.2
Due to Financial Institutions	96,746.08	13.1	39,706.87	1.3	40,508.71	1.6	17,820.28	4.0	17,820.28	2.8	4,367.77	1.9	538.24	0.1	152,363.72	13.4	405,994.32	22.7	4,378.67	0.1	261,222.87	15.8	347,681.46	5.80	1,041,467.81	6.2
Foreign Liabilities	0.0	0.0	140,616.29	4.7	108,856.42	4.3	3,652.10	0.8	-	0.0	973.22	0.4	95,448.69	15.6	-	0.0	16,020.89	0.9	119,849.19	3.0	30,578.52	1.9	109,523.51	1.83	515,995.32	3.1
Capital and Reserves	246,966.48	33.5	317,418.86	10.6	116,753.02	4.6	97,935.86	22.1	5,967.89	0.9	19,042.95	8.3	91,040.86	14.9	1,263.96	0.1	222,264.65	12.4	603,435.46	14.9	185,816.89	11.2	515,459.30	8.60	1,907,906.88	11.3
Other Liabilities	10,443.96	1.4	354,007.69	11.8	713,278.15	27.9	67,258.82	15.2	84,250.64	13.0	2,500.00	1.1	83,435.97	13.6	531,395.28	46.7	332,377.68	18.6	511,866.45	12.6	309,011.24	18.7	1,265,656.12	21.11	2,999,825.88	17.8
Sub-Total	**737,636.46**	**100.0**	**2,581,345.83**	**86.3**	**2,523,566.78**	**98.7**	**342,413.35**	**77.4**	**644,898.25**	**99.8**	**168,390.32**	**73.1**	**415,471.88**	**67.9**	**1,137,940.37**	**100.0**	**1,788,329.92**	**100.0**	**2,931,585.87**	**72.3**	**1,638,768.60**	**99.2**	**5,523,623.09**	**92.13**	**14,929,474.05**	**88.5**
Off-balance sheet items	0.00	0.0	410,366.75	13.7	32,960.00	1.3	100,199.72	22.6	1,190.31	0.2	61,998.97	26.9	196,600.76	32.1	-	0.0	-	0.0	1,124,029.39	27.7	13,712.07	0.8	471,744.75	7.87	1,941,057.97	11.5
Total Liabilities	**737,636.46**	**100.0**	**2,991,712.58**	**100.0**	**2,556,526.78**	**100.0**	**442,613.07**	**100.0**	**646,088.56**	**100.0**	**230,389.29**	**100.0**	**612,072.64**	**100.0**	**1,137,940.37**	**100.0**	**1,788,329.92**	**100.0**	**4,055,615.26**	**100.0**	**1,652,480.67**	**100.0**	**5,995,367.86**	**100.00**	**16,870,532.02**	**100.0**

A P P E N D I X 1 - S T A T I S T I C A L T A B L E S

C O N T I N U E D

TABLE 1B
COMPOSITION OF THE BALANCE SHEET (As at 31 December, 2004)

MERCHANT BANKS

ASSETS

	ABC		GENESIS		INTERFIN		PREMIER		RENAISSANCE		COMPOSITE '2003		COMPOSITE '2004	
	Z$million	**%**	**Z$million**	**%**	**Z$million**	**%**	**Z$million**		**Z$million**	**%**	**Z$million**	**%**	**Z$million**	**%**
Cash and Due from Banks	37,006.03	7.97	64,791.82	28.51	0.00	0.00	2,229.90	5.03	3,137.29	0.97	72,825.42	6.59	107,165.04	6.98
Balances with RBZ	13,084.88	2.82	4,941.44	2.17	12,912.62	2.70	3,385.65	7.64	4,915.86	1.53	2,553.30	0.23	39,240.45	2.55
Foreign Claims	48,325.22	10.41	866.22	0.38	0.03	0.00		0.00	598.30	0.19	19,980.57	1.81	49,789.77	3.24
Securities and Investments	166,391.28	35.85	17,170.62	7.55	228,063.32	47.65	30,743.25	69.40	167,310.42	51.96	229,871.83	20.80	609,678.89	39.68
Loans, advances and leases	175,299.99	0.0	30,556.09	0.0	138,196.54			0.00	42,849.92		251,360.19		386,902.54	
Total Provisions	7,070.70	0.0	2,283.09	0.0	0.00			0.00	662.14		3,620.10		10,015.93	
Net Loans, advances & leases	168,229.29	36.25	28,273.00	12.44	138,196.54	28.87		0.00	42,187.78	13.10	247,740.09	22.42	376,886.61	24.53
Fixed Assets	8,887.43	1.91	3,707.34	1.63	62,771.51	13.11	1,298.15	2.93	6,962.17	2.16	42,758.18	3.87	83,626.60	5.44
Other Assets	22,195.57	4.78	59,240.04	26.06	36,687.91	7.67	6,640.64	14.99	21,544.02	6.69	488,032.54	44.17	146,308.18	9.52
Total Book Assets	**464,119.70**	**100.00**	**178,990.48**	**78.75**	**478,631.92**	**100.00**	**44,297.59**	**100.00**	**246,655.84**	**76.60**	**1,103,761.93**	**99.89**	**1,412,695.53**	**91.95**
Off-balance sheet items	-	0.00	48,300.41	21.25	0.00	0.00	-		75,333.17	23.40	1,222.18	0.11	123,633.58	8.05
Total Assets	**464,119.70**	**100.00**	**227,290.89**	**100.00**	**478,631.92**	**100.00**	**44,297.59**	**100.00**	**321,989.01**	**100.00**	**1,104,984.10**	**100.00**	**1,536,329.11**	**100.00**

LIABILITIES

	ABC		GENESIS		INTERFIN		PREMIER		RENAISSANCE		COMPOSITE '2003		COMPOSITE '2004	
	Z$million	**%**	**Z$million**	**%**	**Z$million**	**%**	**Z$million**	**%**	**Z$million**	**%**	**Z$million**	**%**	**Z$million**	**%**
Total Deposits	233,284.21	50.26	4,928.50	2.17	233,952.59	48.88	23,445.53	52.93	13,587.75	4.22	558,092.01	69.54	509,198.58	33.14
Of Which: Demand Deposits	11,564.53	0.0	953.96	0.0	13,739.84		1,292.86		1,213.66		119,743.80		28,764.85	
Savings Deposits	0.00	0.0	0.00		0.00		-							
Time Deposits	183,882.82	0.0	3,805.16		220,212.75		22,152.67		10,360.99		428,454.29		440,414.39	
FCA Deposits	37,836.86	0.0	169.38		0.00				2,013.10		9,893.55		40,019.34	
NCD's	0.00	0.0	0.00		0.00									
Due to RBZ	46,033.97	9.92	19,467.00	8.56	0.00	0.00		0.00		0.00	3,610.00	0.45	65,500.97	4.26
Due to Financial Institutions	-	0.00	236.94	0.10	0.00	0.00		0.00	154,235.33	47.90	28,840.61	3.59	154,472.27	10.05
Foreign Liabilities	56,446.96	12.16	17.30	0.01	0.00	0.00		0.00	301.14	0.09	19,192.59	2.39	56,765.40	3.69
Capital and Reserves	48,243.08	10.39	13,032.45	5.73	44,968.56	9.40	14,056.07	31.73	20,510.61	6.37	61,943.22	7.72	140,810.77	9.17
Other Liabilities	80,111.48	17.26	141,308.29	62.17	199,710.77	41.73	6,795.99	15.34	58,021.01	18.02	129,633.24	16.15	485,947.54	31.63
Sub-Total	**464,119.70**	**100.00**	**178,990.48**	**78.75**	**478,631.92**	**100.00**	**44,297.59**	**100.00**	**246,655.84**	**76.60**	**801,311.66**	**99.85**	**1,412,695.53**	**91.95**
Off-balance sheet items	-	0.00	48,300.41	21.25	-	0.00	-	0.00	75,333.17	23.40	1,222.18	0.15	123,633.58	8.05
Total Liabilities	**464,119.70**	**100.00**	**227,290.89**	**100.00**	**478,631.92**	**100.00**	**44,297.59**	**100.00**	**321,989.01**	**100.00**	**802,533.84**	**100.00**	**1,536,329.11**	**100.00**

APPENDIX 1 - STATISTICAL TABLES
CONTINUED

TABLE 1C
COMPOSITION OF THE BALANCE SHEET (As at 31 December, 2004)

FINANCE HOUSE	**ABC**		**ZDB**		**TRUSTFIN**		**SAGIT**		**COMPOSITE '2003**		**COMPOSITE '2004**	
ASSETS	**Z$million**	%	**Z$million**	%	**Z$million**	%	**Z$million**	%	**Z$million**	%	**Z$million**	%
Cash and Due from Banks	100,345.14	56.4	5,946.16	14.5	17,178.68	51.9	4,913.36	20.4	12,355.7	12.6	128,383.34	46.5
Balances with RBZ	14,005.92	7.9	4,980.38	12.2	1,468.31	4.4	1,559.02	6.5	586.9	0.6	22,013.63	8.0
Foreign Claims	-	0.0		0.0		0.0		0.0	-	0.0	-	0.0
Securities and Investments	57,032.42	32.1	793.30	1.9	3,031.34	9.2	12,904.55	53.7	35,127.5	35.8	73,761.61	26.7
Loans, advances and leases	3,728.07		27,716.91		10,755.05		4,699.04		47,302.0		46,899.07	
Total Provisions	1,098.95		3,596.84		610.39		1,346.98		1,536.8		6,653.16	
Net Loans, advances & leases	2,629.12	1.5	24,120.07	59.0	10,144.66	30.6	3,352.06	13.9	33,461.8	34.1	40,245.91	14.6
Fixed Assets	654.30	0.4	840.97	2.1	828.42	2.5	1,136.89	4.7	3,523.2	3.6	3,460.58	1.3
Other Assets	3,150.15	1.8	4,219.12	10.3	468.48	1.4	179.31	0.7	8,727.9	8.9	8,017.06	2.9
Total Book Assets	**177,817.05**	**100.0**	**40,900.00**	**100.0**	**33,119.89**	**100.0**	**24,045.19**	**100.0**	**93,783.0**	**95.5**	**275,882.1**	**100.0**
Off-balance sheet items	-	0.0	-	0.0		0.0		0.0	4,369.10	4.5	-	0.0
Total Assets	**177,817.05**	**100.0**	**40,900.00**	**100.0**	**33,119.89**	**100.0**	**24,045.19**	**100.0**	**98,152.13**	**100.0**	**275,882.13**	**100.0**
LIABILITIES	**ABC**		**ZDB**		**TRUSTFIN**		**SAGIT**		**COMPOSITE '2003**		**COMPOSITE '2004**	
	Z$million	%	**Z$million**	%	**Z$million**	%	**Z$million**	%	**Z$million**	%	**Z$million**	%
Total Deposits	147,383.40	82.9	33,282.90	81.4	18,068.60	54.6	-	0.0	52,330.63	53.3	198,734.90	72.0
Of Which: Demand Deposits	-				1,365.05				-		1,365.05	
Savings Deposits	-								-		-	
Time Deposits	125,447.31		33,282.90		16,703.55				47,044.27		175,433.76	
FCA Deposits	-								-		-	
NCD's	21,936.09		-						5,286.36		21,936.09	
Due to RBZ	-	0.0		0.0		0.0		0.0	-	0.0	-	0.0
Due to Financial Institutions	-	0.0	-	0.0	5.94	0.0	2,697.47	11.2	10,704.98	10.9	2,703.41	1.0
Foreign Liabilities	4,145.00	2.3	-	0.0		0.0		0.0	758.77	0.8	4,145.00	1.5
Capital and Reserves	10,146.82	5.7	2,856.82	7.0	7,580.81	22.9	8,447.12	35.1	9,726.24	9.9	29,031.57	10.5
Other Liabilities	16,141.85	9.1	4,760.55	11.6	7,464.54	22.5	12,900.60	53.7	24,631.52	25.1	41,267.54	15.0
Sub-Total	**177,817.07**	**100.0**	**40,900.27**	**100.0**	**33,119.89**	**100.0**	**24,045.19**	**100.0**	**98,152.13**	**100.0**	**275,882.42**	**100.0**
Off-balance sheet items	-	0.0		0.0	-	0.0		0.0	-	0.0	-	0.0
Total Liabilities	**177,817.07**	**100.0**	**40,900.27**	**100.0**	**33,119.89**	**100.0**	**24,045.19**	**100.0**	**98,152.13**	**100.0**	**275,882.42**	**100.0**

APPENDIX 1 - STATISTICAL TABLES
CONTINUED

TABLE 1D
COMPOSITION OF THE BALANCE SHEET (As at 31 December, 2004)

DISCOUNT HOUSES	ABC		HIGHVELD		DCZ		TETRAD		NDH		COMPOSITE '2003		COMPOSITE '2004	
ASSETS	Z$million	%	Z$million	%	Z$million	%	Z$million	%	Z$million	%	Z$million	%	Z$million	%
Cash and Due from Banks	15,744.08	24.40	220.64	0.84	(63.96)	(0.12)	14,179.07	42.61	76.82	0.16	4,528.96	2.64	30,156.65	13.30
Balances with RBZ	0.00	0.00	2,214.36	8.46	6,312.71	11.67	0.00	0.00	11.80	0.02	(362.54)	(0.21)	8,538.87	3.77
Foreign Claims	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00		0.00	-	0.00
Securities and Investments	47,492.68	73.59	20,745.89	79.24	31,114.68	57.52	11,862.45	35.65	7,764.58	15.96	379,592.19	221.37	118,980.28	52.48
Loans, advances and leases	0.00		0.00	0.0	0.00		0.00		0.00		0.00		-	
Total Provisions	0.00		0.00	0.00	0.00		0.00		0.00		489.30		-	
Net Loans, advances & leases	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.89	0.00	27,839.99	16.24	0.89	0.00
Fixed Assets	479.28	0.74	2,306.38	8.81	511.70	0.95	3,168.83	9.52	361.61	0.74	6,030.17	3.52	6,827.80	3.01
Other Assets	819.09	1.27	694.86	2.65	16,215.79	29.98	4,066.97	12.22	40,422.63	83.11	19,303.01	11.26	62,219.34	27.44
Total Book Assets	**64,535.13**	**100.00**	**26,182.13**	**100.00**	**54,090.92**	**100.00**	**33,277.32**	**100.00**	**48,638.33**	**100.00**	**171,472.03**	**100.00**	**226,723.83**	**100.00**
Off-balance sheet items	0.00	0.00		0.00			0.00	0.00	0.00	0.00	0.00	0.00	-	0.00
Total Assets	**64,535.13**	**100.00**	**26,182.13**	**100.00**	**54,090.92**	**100.00**	**33,277.32**	**100.00**	**48,638.33**	**100.00**	**171,472.03**	**100.00**	**226,723.83**	**100.00**
LIABILITIES														
	ABC		HIGHVELD		DCZ		TETRAD		NDH		COMPOSITE '2003		COMPOSITE '2004	
	Z$million	%	Z$million	%	Z$million	%	Z$million	%	Z$million	%	Z$million	%	Z$million	%
Total Deposits	12,900.10	19.99	16,548.78	63.21	158.39	0.29	6,082.24	18.28	74.51	0.15	341,025.55	198.88	35,689.51	15.74
Of Which: Demand Deposits	12,900.10		0.00		158.39		6,082.24				12,552.18		19,140.73	
Savings Deposits	0.00		1,162.98		0.00		0.00				0.00		1,162.98	
Time Deposits	0.00		15,385.80		0.00		0.00				307,959.08		15,385.80	
FCA Deposits	0.00		0.00		0.00		0.00				0.00		-	
NCD's	0.00		0.00		0.00		0.00				0.00		-	
Due to RBZ	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.90	0.00	19,652.49	11.46	112.00	0.05
Due to Financial Institutions	0.00	0.00	0.00	0.00	27,298.91	50.47	0.00	0.00	81,843.24	168.27	11,322.94	6.60	-	0.00
Foreign Liabilities	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	-	0.00
Capital and Reserves	19,423.46	30.10	7,268.20	27.76	13,445.88	24.86	8,635.27	25.95	(56,423.51)	(116.01)	7,766.52	4.53	(7,650.70)	(3.37)
Other Liabilities	32,211.57	49.91	2,365.15	9.03	13,187.74	24.38	18,559.81	55.77	23,143.20	47.58	30,152.15	17.58	198,573.01	87.58
Sub-Total	**64,535.13**	**100.00**	**26,182.13**	**100.00**	**54,090.92**	**100.00**	**33,277.32**	**100.00**	**48,638.33**	**100.00**	**171,472.03**	**100.00**	**226,723.82**	**100.00**
Off-balance sheet items	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	-	0.00
Total Liabilities	**64,535.13**	**100.00**	**26,182.13**	**100.00**	**54,090.92**	**100.00**	**33,277.32**	**100.00**	**48,638.33**	**100.00**	**171,472.03**	**100.00**	**226,723.82**	**100.00**

APPENDIX 1 - STATISTICAL TABLES
CONTINUED

TABLE 1E
COMPOSITION OF THE BALANCE SHEET (As at 31 December, 2004)

BUILDING SOCIETY												
ASSETS												
	BERVERLY		**CABS**		**INTERMARKET**		**ZBS**		**COMPOSITE '2003**		**COMPOSITE '2004**	
	Z$million	%	**Z$million**	%	**Z$million**	%	**Z$million**	%	**Z$million**	%	**Z$million**	%
Cash and Due from Banks	63,706.38	21.32	144,424.00	30.11	41,115.00	29.14	13,339.00	46.68	145,226.55	43.54	262,584.38	27.70
Balances with RBZ	28,470.00	9.53	30,765.00	6.41	3,341.00	2.37	2.62	0.01	0.00	0.00	62,578.62	6.60
Foreign Claims	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Securities and Investments	83,655.62	27.99	113,151.00	23.59	42,976.00	30.46	1,830.59	6.41	64,643.35	19.38	241,613.21	25.48
Loans, advances and leases	66,189.00		98,024.00		44,577.00		3,973.42		149,405.50		212,763.42	
Total Provisions			1,315.00		0.00		254.24		70,135.00		1,569.24	
Net Loans, advances & leases	66,189.00	22.15	96,709.00	20.16	44,577.00	31.60	3,719.18	13.01	79,270.50	23.77	211,194.18	22.28
Fixed Assets	56,808.00	19.01	80,089.00	16.70	9,073.00	6.43	5,712.48	19.99	35,185.52	10.55	151,682.48	16.00
Other Assets	0.00	0.00	14,481.00	3.02	0.00	0.00	3,972.93	13.90	7,422.40	2.23	18,453.93	1.95
Total Book Assets	**298,829.00**	**100.00**	**479619.00**	**100.00**	**141,082.00**	**100.00**	**28,576.80**	**100.00**	**331,748.32**	**99.46**	**948,106.80**	**100.00**
Off-balance sheet items	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1,793.02	0.54	0.00	0.00
Total Assets	**298,829.40**	**100.00**	**479,619.00**	**100.00**	**141,082.00**	**100.00**	**28,576.80**	**100.00**	**333,541.34**	**100.00**	**948,106.80**	**100.00**
LIABILITIES												
	BERVERLY		**CABS**		**INTERMARKET**		**ZBS**		**COMPOSITE '2003**		**COMPOSITE '2004**	
	Z$million	%	**Z$million**	%	**Z$million**	%	**Z$million**	%	**Z$million**	%	**Z$million**	%
Total Deposits	176,852.48	59.18	317,471.00	66.19	78,937.00	55.95	15,055.60	52.68	254,551.95	76.32	588,316.08	62.05
Of Which: Demand Deposits	0.00		0.00		0.00		0.00		100,001.00		0.00	
Savings Deposits	162,606.00		223,041.00		49,263.00		13,802.96		78,906.09		448,712.96	
Time Deposits	0.00		76,881.00		17,050.00		291.07		21,953.67		94,222.07	
FCA Deposits	0.00		0.00		0.00		0.00		0.00		0.00	
NCD's	14,246.48		17,549.00		12,624.00		961.57		50,131.10		45,381.05	
Due to RBZ	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	135.00	0.04	0.00	0.00
Due to Financial Institutions	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	223.64	0.07	0.00	0.00
Foreign Liabilities	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Capital and Reserves	110,942.00	37.13	145,506.00	30.34	53,294.00	37.78	10,331.10	36.15	56,534.98	16.95	320,073.10	33.76
Other Liabilities	11,034.92	3.69	16642.00	3.47	8,851.00	6.27	3,189.10	11.16	19,986.15	5.99	39,717.02	4.19
Sub-Total	**298,829.40**	**100.00**	**479,619.00**	**100.00**	**141,082.00**	**100.00**	**28,575.80**	**100.00**	**331,748.32**	**99.46**	**948,106.20**	**100.00**
Off-balance sheet items	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1,793.02	0.54	0.00	0.00
Total Liabilities	**298,829.40**	**100.00**	**479,619.00**	**100.00**	**141,082.00**	**100.00**	**28,576.80**	**100.00**	**333,541.34**	**100.00**	**948,106.80**	**100.00**

APPENDIX 1 - STATISTICAL TABLES
CONTINUED

TABLE 1F
COMPOSITION OF THE BALANCE SHEET (As at 31 December, 2004)

CONSOLIDATED BALANCE SHEETS

ASSETS	COMMERCIAL BANKS		FINANCE HOUSES		MERCHANT BANKS		BUILDING SOCIETIES		DISCOUNT HOUSES		COMPOSITE DEC 2004	
	Z$million	%	Z$million	%	Z$million	%	Z$million	%	Z$million	%	Z$million	%
Cash and Due from Banks	725,232.31	4.30	128,383.34	46.54	107,165.04	6.98	262,584.38	27.70	30,156.65	13.30%	1,253,521.72	6.31
Balances with RBZ	3,438,512.79	20.38	22,013.63	7.98	39,240.45	2.55	62,578.62	6.60	8,538.87	3.77%	3,570,884.36	17.98
Foreign Claims	833,925.15	4.94	0.00	0.00	49,789.77	3.24	0.00	0.00	0.00	0.00%	883,714.92	4.45
Securities and Investments	4,185,850.17	24.81	73,761.61	26.74	609,678.89	39.68	241,613.21	25.48	118,980.28	52.48%	5,229,884.16	26.34
Loans, advances and leases	4,768,887.88		46,899.07		386,902.54		212,763.42		0.00		5,415,452.91	
Total Provisions	632,257.64		6,653.16		10,015.93		1,569.24		0.00		650,495.97	
Net Loans, advances & leases	4,136,630.25	24.52	40,245.91	14.59	376,886.61	24.53	211,194.18	22.28	0.89	0.00%	4,764,957.84	24.00
Fixed Assets	250,473.41	1.48	3,460.58	1.25	83,626.60	5.44	151,682.48	16.00	6,827.80	3.01%	496,070.86	2.50
Other Assets	1,358,849.98	8.05	8,017.06	2.91	146,308.18	9.52	18,453.93	1.95	62,219.34	27.44%	1,593,848.49	8.03
Total Book Assets	**14,929,474.05**	**88.49**	**275,882.13**	**100.00**	**1,412,695.53**	**91.95**	**948,106.80**	**100.00**	**226,723.83**	**100.00%**	**17,792,882.34**	**89.60**
Off-balance sheet items	1,941,057.97	11.51	0.00	0.00	123,633.58	8.05	0.00	0.00	0.00	0.00%	2,064,691.56	10.40
Total Assets	**16,870,532.02**	**100.00**	**275,882.13**	**100.00**	**1,536,329.11**	**100.00**	**948,106.80**	**100.00**	**226,723.83**	**100.00%**	**19,857,573.90**	**100.00**

LIABILITIES	COMMERCIAL BANKS		FINANCE HOUSES		MERCHANT BANKS		BUILDING SOCIETIES		DISCOUNT HOUSES		COMPOSITE DEC 2004	
	Z$million	%	Z$million	%	Z$million	%	Z$million	%	Z$million	%	Z$million	%
Total Deposits	6,888,589.22	40.83	206,512.86	74.86	509,198.58	33.14	588,316.08	62.05	35,689.51	15.74%	8,228,306.25	41.44
Of Which: Demand Deposits	4,012,631.16		1,365.05		28,764.85		0.00		19,140.73		4,061,901.79	
Savings Deposits	613,289.01		0.00		0.00		448,712.96		1,162.98		1,063,164.95	
Time Deposits	1,206,925.59		183,211.72		440,414.39		94,222.07		15,385.80		1,940,159.57	
FCA Deposits	820,466.18		0.00		40,019.34		0.00		0.00		860,485.52	
NCD's	235,277.28		21,936.09		0.00		45,381.05		0.00		302,594.42	
Due to RBZ	1,556,562.52	9.23	0.00	0.00	65,500.97	4.26	0.00	0.00	112.00	0.05%	1,622,175.49	8.17
Due to Financial Institutions	1,041,467.81	6.17	2,703.41	0.98	154,472.27	10.05	0.00	0.00	-	0.00%	1,198,643.49	6.04
Foreign Liabilities	515,995.32	3.06	4,145.00	1.50	56,765.40	3.69	0.00	0.00	0.00	0.00%	576,905.72	2.91
Capital and Reserves	1,907,906.88	11.31	29,031.57	10.52	140,810.77	9.17	320,073.10	33.76	(7,650.70)	-3.37%	2,390,171.62	12.04
Other Liabilities	2,999,825.88	17.78	33,489.58	12.14	485,947.54	31.63	39,717.02	4.19	198,573.01	87.58%	3,757,553.02	18.92
Sub-Total	**14,929,474.05**	**88.49**	**275,882.42**	**100.00**	**1,412,695.53**	**91.95**	**948,106.20**	**100.00**	**226,723.82**	**100.00%**	**17,792,882.33**	**89.60**
Off-balance sheet items	1,941,057.97	11.51	0.00	0.00	123,633.58	8.05	0.00	0.00	0.00	0.00%	2,064,691.56	10.40
Total Liabilities	**16,870,532.02**	**100.00**	**275,882.42**	**100.00**	**1,536,329.11**	**100.00**	**948,106.80**	**100.00**	**226,723.82**	**100.00%**	**19,857,573.89**	**100.00**

APPENDIX 2 - STATISTICAL TABLES

TABLE 2A
COMPOSITION OF INCOME STATEMENTS (31 DECEMBER 2004)

COMMERCIAL BANKS (Figures in ZW$ millions)

ITEM	BARCLAYS	MBCA BANK	AGRIBANK	CBZ	STANBIC	ZIMBANK	FIRST BANK	KINGDOM	NMB	STANCHART	METROPOLITAN	TOTAL
Total interest income	**969,363.95**	**140,248.42**	**167,908.62**	**1,027,077.39**	**575,088.02**	**315,437.80**	**362,526.69**	**354,162.28**	**455,571.52**	**982,833.10**	**214,691.82**	**5,564,909.62**
Loans and Leases	93,246.96	78,243.79	79,618.59	788,928.16	207,675.85	41,289.19	260,901.73	143,821.35	189,776.58	240,730.74	103,859.26	2,528,092.20
Securities and investments	575,077.73	58,098.50	11,780.16	238,149.23	233,513.72	257,913.75	97,777.30	179,318.38	202,589.62	560,404.44	110,300.73	2,524,923.55
Deposit balances	1,039.26	3,901.81	38,799.51	0.00	7,986.23	1,711.72	3,847.67	20,215.35	0.06	21,846.97	531.83	99,880.39
Other interest income	0.00	4.33	37,710.36	0.00	125,912.22	14,523.14	0.00	10,807.20	63,205.27	159,850.97	0.00	412,013.48
Total interest expenses	**192,217.81**	**9,566.46**	**41,809.19**	**448,136.59**	**106,060.22**	**241,110.88**	**107,401.48**	**285,554.74**	**373,505.44**	**80,501.51**	**126,166.76**	**2,012,031.07**
Deposits	70,402.00	7,439.63	25,601.86	379,553.88	21,641.47	13,714.17	1,708.51	285,554.74	207,569.84	16,036.10	60,486.85	1,089,709.03
Borrowed funds	121,815.49	1,563.73	16,206.62	64,354.80	84,203.07	76,083.58	23,812.35	0.00	0.00	64,465.41	53,070.99	505,576.04
Other interest expenses	0.32	563.10	0.72	4,227.90	215.69	151,313.13	81,880.62	0.00	165,935.60	0.00	12,608.92	416,746.00
Net interest income	**777,146.14**	**130,681.97**	**126,099.43**	**578,940.80**	**469,027.80**	**74,326.92**	**255,125.21**	**68,607.54**	**82,066.08**	**902,331.60**	**88,525.06**	**3,552,878.55**
Provisions for loans and lease losses	113,949.07	5,195.47	31,544.54	58,913.02	59,293.44	868.03	62,370.60	10,744.47	21,263.65	14,232.18	59,653.63	438,028.10
Total non-interest income	**143,417.76**	**49,424.29**	**13,595.95**	**136,293.35**	**96,740.85**	**29,402.64**	**38,791.59**	**35,150.91**	**(11,605.90)**	**211,933.88**	**4,681.47**	**747,826.78**
Fees commission and service charges	91,163.52	20,673.49	11,668.11	113,348.49	35,019.43	23,931.09	0.00	22,503.60	13,158.33	98,866.07	4,338.08	434,670.21
Forex fees and commission	38,060.36	26,687.50	0.00	8,183.24	0.00	5,470.09	16,810.78	8,865.24	0.00	112,559.42	303.05	216,939.68
Other non-interest income	14,193.88	2,063.30	1,927.84	14,761.62	32,797.77	1.46	21,980.81	3,782.07	(204.61	)508.38	40.35	91,852.87
Total non-interest expenses	**373,816.01**	**43,579.06**	**69,852.83**	**197,561.24**	**142,233.96**	**88,285.39**	**93,166.33**	**104,732.12**	**72,232.50**	**208,765.06**	**30,414.80**	**1,424,639.30**
Salaries and employee benefits	171,237.59	23,868.07	48,802.68	149,040.90	68,223.98	66,096.11	49,693.66	68,525.96	36,947.20	138,088.37	12,388.38	832,912.88
Premises equipment and depreciation	10,695.12	1,727.57	2,711.62	3,591.72	2,580.07	5,124.05	5,483.80	4,944.72	7,275.74	11,779.50	893.23	56,807.13
Administrative and other expenses	191,883.30	17,983.42	18,338.54	44,928.62	71,429.92	17,065.24	37,988.87	31,261.44	28,009.56	58,897.19	17,133.20	534,919.29
Net income before taxes and extraordinary items	**432,798.83**	**131,331.73**	**38,298.00**	**458,759.90**	**364,241.25**	**14,576.14**	**138,379.88**	**(11,718.14)**	**(23,035.98)**	**891,268.24**	**3,138.09**	**2,438,037.93**
Taxes	161,766.60	47,148.09	0.00	174,627.15	131,395.72	5,232.83	48,349.93	(2,043.26)	3,094.03	319,965.30	0.00	889,536.39
Net income after taxes before extraordinary items	**271,032.23**	**84,183.64**	**38,298.00**	**284,132.74**	**232,845.53**	**9,343.30**	**90,029.95**	**(9,674.88)**	**(19,941.95)**	**571,302.94**	**3,138.09**	**1,554,689.60**
Extraordinary items	0.00	0.00	0.00	108.35	0.00	0.00	0.00	0.00	0.00	0.00	0.00	108.35
Net income/(Loss)	**271,032.23**	**84,183.64**	**38,298.00**	**284,241.09**	**232,845.53**	**9,343.30**	**90,029.95**	**(9,674.88)**	**(19,941.95)**	**571,302.94**	**3,138.09**	**1,554,797.95**
Dividends	18,762.28	15,200.00	0.00	0.00	57,285.44	0.00	10,000.00	0.00	0.00	9,000.00	0.00	110,247.72
Retained Earnings	**252,269.95**	**68,983.64**	**38,298.00**	**284,241.09**	**175,560.09**	**9,343.30**	**80,029.95**	**(9,674.88)**	**(19,941.95)**	**562,302.94**	**3,138.09**	**1,444,550.23**

APPENDIX 2 - STATISTICAL TABLES
CONTINUED

TABLE 2B
COMPOSITION OF INCOME STATEMENTS (31 DECEMBER 2004)

MERCHANT BANKS (Figures in ZW$ millions)

ITEM	ABC	PREMIER	GENESIS	INTERFIN	RENAISSANCE	TOTAL
Total interest income	**174,949.03**	**39,445.75**	**120,805.44**	**296,542.24**	**41,754.09**	**673,496.54**
Loans and Leases	48,721.95	730.24	5,329.91	76,118.92	18,793.60	149,694.62
Securities and investments	125,875.11	24,119.66	115,475.53	65,246.02	(6,002.86)	324,713.46
Deposit balances	351.97	0.00	0.00	24,052.71	28,963.35	53,368.03
Other interest income	0.00	14,595.85	0.00	131,124.59	0.00	145,720.44
Total interest expenses	**107,402.63**	**39,786.34**	**101,352.31**	**266,774.71**	**14,047.38**	**529,363.36**
Deposits	100,974.74	36,874.39	1,869.29	249,819.45	14,047.38	403,585.25
Borrowed funds	0.00	1,173.42	0.00	0.00	0.00	1,173.42
Other interest expenses	6,427.88	1,738.54	99,483.02	16,955.26	0.00	124,604.70
Net interest income	67,546.40	(340.59)	19,453.13	29,767.53	27,706.71	144,133.18
Provisions for loans and lease losses	1,183.69	226.22	2,246.16	16,539.89	517.88	20,713.84
Total non-interest income	**36,879.96**	**11,818.96**	**4,951.59**	**33,195.67**	**16,319.27**	**103,165.44**
Fees commission and service charges	8,214.13	2,055.24	4,466.86	12,542.37	15,066.39	42,344.99
Forex fees and commission	17,586.34	0.00	268.97	9,762.49	0.00	27,617.80
Other non-interest income	11,079.49	9,763.72	215.76	10,890.80	1,252.88	33,202.65
Total non-interest expenses	**54,387.26**	**7,118.46**	**11,461.17**	**42,945.42**	**22,216.96**	**138,129.27**
Salaries and employee benefits	27,599.98	3,048.93	6,794.05	24,425.07	10,309.97	72,178.01
Premises equipment and depreciation	4,651.03	576.71	1,085.56	4,303.66	3,925.22	14,542.18
Administrative and other expenses	22,136.25	3,492.82	3,581.57	14,216.68	7,981.77	51,409.08
Net income before taxes and extraordinary items	**48,855.40**	**4,133.70**	**10,697.38**	**3,477.89**	**21,291.14**	**88,455.51**
Taxes	16,539.09	564.06	3,010.24	723.49	9,436.57	30,273.44
Net income after taxes before extraordinary items	**32,316.31**	**3,569.64**	**7,687.14**	**2,754.40**	**11,854.57**	**58,182.07**
Extraordinary items	0.00	0.00	167.06	0.00	1,046.59	1,213.65
Net income/(Loss)	32,316.31	3,569.64	7,520.08	2,754.40	10,807.98	56,968.42
Dividends	0.00	0.00	0.00	0.00	0.00	0.00
Retained Earnings	**32,316.31**	**3,569.64**	**7,520.08**	**2,754.40**	**10,807.98**	**56,968.42**

APPENDIX 2 - STATISTICAL TABLES

CONTINUED

TABLE 2C
COMPOSITION OF INCOME STATEMENTS (31 DECEMBER 2004)

BUILDING SOCIETIES (Figures in ZW$ millions)

ITEM	CABS	BEVERLEY	INTERMARKET	ZBS	TOTAL
Total interest income	**87,548.29**	**65,012.24**	**22,534.80**	**10,167.26**	**185,262.59**
Loans and Leases	31,002.85	27,365.13	7,547.14	1,438.18	67,353.30
Securities and investments	56,545.44	37,647.11	14,875.74	8,729.08	117,797.37
Deposit balances	0.00	0.00	0.00	0.00	0.00
Other interest income	0.00	0.00	111.92	0.00	111.92
Total interest expenses	**20,512.14**	**17,410.16**	**7,321.95**	**6,434.50**	**51,678.75**
Deposits	20,512.14	17,410.16	7,321.95	6,434.50	51,678.75
Borrowed funds	0.00	0.00	0.00	0.00	0.00
Other interest expenses	0.00	0.00	0.00	0.00	0.00
NET INTEREST INCOME	**67,036.14**	**47,602.08**	**15,212.85**	**3,732.76**	**133,583.83**
Provisions for loans and lease losses	1,315.00	0.00	0.00	91.90	1,406.90
Total non-interest income	**22,731.71**	**7,258.41**	**5,469.63**	**1,394.16**	**36,853.92**
Fees commission and service charges	18,188.62	227.12	3,204.94	1,325.49	22,946.16
Forex fees and commission	0.00	0.00	0.00	0.00	0.00
Other non-interest income	4,543.09	7,031.30	2,264.70	68.67	13,907.76
Total non-interest expenses	**42,818.03**	**36,814.39**	**20,164.28**	**7,222.75**	**107,019.43**
Salaries and employee benefits	23,543.69	23,053.07	8,418.23	3,547.54	58,562.53
Premises equipment and depreciation	2,993.23	2,982.95	1,111.58	640.82	7,728.58
Administrative and other expenses	16,281.10	10,778.37	10,634.47	3,034.38	40,728.33
Net income before taxes and extraordinary items	**45,634.82**	**18,046.11**	**518.21**	**(2,187.72)**	**62,011.42**
Taxes	0.00	0.00	0.00	0.00	0.00
Net income after taxes before extraordinary items	**45,634.82**	**18,046.11**	**518.21**	**(2,187.72)**	**62,011.42**
Extraordinary items	0.00	0.00	0.00	(317.60)	(317.60)
Net income/(Loss)	**45,634.82**	**18,046.11**	**518.21**	**(1,870.13)**	**62,329.02**
Dividends	0.00	1,710.66	0.00	0.00	1,710.66
Retained Earnings	**45,634.82**	**16,335.45**	**518.21**	**(1,870.13)**	**60,618.36**

APPENDIX 2 - STATISTICAL TABLES
CONTINUED

TABLE 2D
COMPOSITION OF INCOME STATEMENTS (31 DECEMBER 2004)

FINANCE HOUSES (Figures in ZW$ millions)

ITEM	ABC ASSET	TRUSTFIN	SAGIT	ZDBFS	TOTAL
Total interest income	**96,420.73**	**47,905.55**	**12,712.46**	**35,026.53**	**192,065.27**
Loans and Leases	19,867.92	24,583.31	1,167.84	29,672.20	75,291.26
Securities and investments	76,548.07	23,322.25	11,229.09	5,354.33	116,453.74
Deposit balances	0.00	0.00	0.00	0.00	0.00
Other interest income	4.74	0.00	315.54	0.00	320.27
Total interest expenses	**87,070.18**	**34,063.08**	**16,685.60**	**29,513.91**	**167,332.77**
Deposits	86,644.71	30,722.19	16,685.60	29,227.08	163,279.58
Borrowed funds	0.00	0.00	0.00	0.00	0.00
Other interest expenses	425.47	3,340.89	0.00	286.83	4,053.19
Net interest income	**9,350.55**	**13,842.47**	**(3,973.14)**	**5,512.62**	**24,732.50**
	0.00	0.00	0.00	0.00	0.00
Provisions for loans and lease losses	727.55	446.00	1,346.98	9,610.70	12,131.24
Total non-interest income	**8,584.43**	**90.63**	**569.17**	**538.14**	**9,782.37**
Fees commission and service charges	178.35	151.08	569.17	446.05	1,344.65
Forex fees and commission	1,212.03	0.00	0.00	0.00	1,212.03
Other non-interest income	7,194.04	(60.45)	0.00	92.09	7,225.69
Total non-interest expenses	**4,494.33**	**7,177.18**	**2,736.03**	**4,459.54**	**18,867.09**
Salaries and employee benefits	2,532.29	4,391.81	1,049.55	2,026.68	10,000.33
Premises equipment and depreciation	76.31	429.14	242.05	303.74	1,051.23
Administrative and other expenses	1,885.73	2,356.23	1,444.44	2,129.12	7,815.53
Net income before taxes and extraordinary items	**12,713.09**	**6,309.92**	**(7,353.45)**	**(8,019.48)**	**3,650.08**
Taxes	(4,616.70)	2,251.95	0.00	0.00	(2,364.75)
Net income after taxes before extraordinary items	**8,096.39**	**4,057.97**	**(7,353.45)**	**(8,019.48)**	**(3,218.57)**
Extraordinary items	6,030.83	0.00	0.00	0.00	6,030.83
Net income/(Loss)	**2,065.56**	**4,057.97**	**(7,353.45)**	**(8,019.48)**	**(9,249.40)**
Dividends	0.00	0.00	0.00	0.00	0.00
Retained Earnings	**2,065.56**	**4,057.97**	**(7,353.45)**	**(8,019.48)**	**(9,249.40)**

APPENDIX 2 - STATISTICAL TABLES
CONTINUED

TABLE 2E
COMPOSITION OF INCOME STATEMENTS (31 DECEMBER 2004)

DISCOUNT HOUSES (Figures in ZW$ millions)

ITEM	ABC SEC	DCZ	HIGHVELD	NDH	TETRAD	TOTAL
Total interest income	**76,805.33**	**13,414.27**	**24,748.80**	**16,774.83**	**5,788.05**	**137,531.27**
Loans and Leases	0.00	0.00	0.00	0.00	0.00	0.00
Securities and investments	76,766.48	13,414.27	24,748.80	16,729.97	5,770.10	137,429.62
Deposit balances	0.00	0.00	0.00	0.00	0.00	0.00
Other interest income	38.85	0.00	0.00	44.85	17.95	101.65
Total interest expenses	**60,059.84**	**7,224.98**	**17,833.37**	**60,301.20**	**1,119.29**	**146,538.68**
Deposits	59,927.47	7,224.98	17,833.37	0.00	1,119.29	86,105.11
Borrowed funds	0.00	0.00	0.00	44,717.23	0.00	44,717.23
Other interest expenses	132.37	0.00	0.00	15,583.97	0.00	15,716.34
Net interest income	**16,745.48**	**6,189.29**	**6,915.43**	**(43,526.37)**	**4,668.76**	**(9,007.41)**
Provisions for loans and lease losses	0.00	0.00	0.00	0.00	0.00	0.00
Total non-interest income	**6,813.47**	**23,672.52**	**4,643.15**	**821.48**	**850.64**	**36,801.26**
Fees commission and service charges	0.00	551.02	0.00	297.74	0.00	848.76
Forex fees and commission	0.00	0.00	0.00	0.00	0.00	0.00
Other non-interest income	6,813.47	23,121.50	4,643.15	523.74	850.64	35,952.50
Total non-interest expenses	**1,856.42**	**14,204.66**	**3,166.10**	**6,071.59**	**2,936.70**	**28,235.48**
Salaries and employee benefits	838.59	2,653.12	2,018.13	2,391.44	1,260.14	9,161.42
Premises equipment and depreciation	137.64	0.00	1,032.27	396.33	327.17	1,893.40
Administrative and other expenses	880.20	11,437.28	115.71	3,283.83	1,349.39	17,066.40
Net income before taxes and extraordinary items	**21,702.53**	**15,657.15**	**8,392.47**	**(48,776.48)**	**2,582.70**	**(441.64)**
Taxes	7,791.21	5,561.05	2,359.48	0.00	0.00	15,711.73
Net income after taxes before extraordinary items	**13,911.32**	**10,096.10**	**6,032.99**	**(48,776.48)**	**2,582.70**	**(16,153.37)**
Extraordinary items	0.00	0.00	0.00	0.00	0.00	0.00
Net income/(Loss)	**13,911.32**	**10,096.10**	**6,032.99**	**(48,776.48)**	**2,582.70**	**(16,153.37)**
Dividends	0.00	740.00	0.00	0.00	0.00	740.00
Retained Earnings	**13,911.32**	**9,356.10**	**6,032.99**	**(48,776.48)**	**2,582.70**	**(16,893.37)**

APPENDIX 2 - STATISTICAL TABLES
CONTINUED

TABLE 2F
CONSOLIDATED INCOME STATEMENTS (31 DECEMBER 2004)

(Figures in ZW$ millions)

ITEM	BUILDING SOCIETIES	DISCOUNT HOUSES	COMMERCIAL BANKS	MERCHANT BANKS	FINANCE HOUSES	TOTAL
Total interest income	**185,262.59**	**137,531.27**	**4,538,859.31**	**673,496.54**	**192,065.27**	**5,727,214.98**
Loans and Leases	67,353.30	0.00	2,528,092.20	149,694.62	75,291.26	2,820,431.38
Securities and investments	117,797.37	137,429.62	2,524,923.55	324,713.46	116,453.74	3,221,317.73
Deposit balances	0.00	0.00	99,880.39	53,368.03	0.00	153,248.41
Other interest income	111.92	101.65	412,013.48	145,720.44	320.27	558,267.76
Total interest expenses	**51,678.75**	**146,538.68**	**2,012,031.07**	**29,363.36**	**167,332.77**	**2,906,944.64**
Deposits	51,678.75	86,105.11	1,089,709.03	403,585.25	163,279.58	1,794,357.72
Borrowed funds	0.00	44,717.23	505,576.04	1,173.42	0.00	551,466.68
Other interest expenses	0.00	15,716.34	416,746.00	124,604.70	4,053.19	561,120.23
Net interest income	**133,583.83**	**(9,007.41)**	**3,552,878.55**	**144,133.18**	**24,732.50**	**3,846,320.65**
	0.00	0.00	0.00	0.00	0.00	0.00
Provisions for loans and lease losses	1,406.90	0.00	438,028.10	20,713.84	12,131.24	472,280.09
Total non-interest income	**36,853.92**	**36,801.26**	**747,826.78**	**103,165.44**	**9,782.37**	**934,429.76**
Fees commission and service charges	22,946.16	848.76	434,670.21	42,344.99	1,344.65	502,154.76
Forex fees and commission	0.00	0.00	216,939.68	27,617.80	1,212.03	245,769.51
Other non-interest income	13,907.76	35,952.50	91,852.87	33,202.65	7,225.69	182,141.46
Total non-interest expenses	**107,019.43**	**28,235.48**	**1,424,639.30**	**138,129.27**	**18,867.09**	**1,716,890.58**
Salaries and employee benefits	58,562.53	9,161.42	832,912.88	72,178.01	10,000.33	982,815.17
Premises equipment and depreciation	7,728.58	1,893.40	56,807.13	14,542.18	1,051.23	82,022.51
Administrative and other expenses	40,728.33	17,066.40	534,919.29	51,409.08	7,815.53	651,938.63
Net income before taxes and extraordinary items	**62,011.42**	**(441.64)**	**2,438,037.93**	**88,455.51**	**3,650.08**	**2,591,713.29**
Taxes	0.00	15,711.73	889,536.39	30,273.44	(2,364.75)	933,156.80
Net income after taxes before extraordinary items	**62,011.42**	**(16,153.37)**	**1,554,689.60**	**58,182.07**	**(3,218.57)**	**1,655,511.15**
Extraordinary items	(317.60)	0.00	108.35	1,213.65	6,030.83	7,035.23
Net income/(Loss)	**62,329.02**	**(16,153.37)**	**1,554,797.95**	**56,968.42**	**(9,249.40)**	**1,648,692.62**
Dividends	1,710.66	740.00	110,247.72	0.00	0.00	112,698.37
Retained Earnings	**60,618.36**	**(16,893.37)**	**1,444,550.23**	**56,968.42**	**(9,249.40)**	**1,535,994.24**

APPENDIX 3
REGISTERED AND OPERATING BANKING INSTITUTIONS AS AT 31 DECEMBER 2004

COMMERCIAL BANKS		Total Assets: ZW$ millions		
Banking Institution	**Address and Website**	**2003**	**2004**	**% Annual Growth**
Agricultural Bank of Zimbabwe	15th Floor, Hurudza House 14-16 Nelson Mandela Avenue Harare Phone: 774429 or 773704/5 or 774554 Fax: 774554 http://www.agribank.co.zw	145,397.67	737,636.41	407%
Barclays Bank of Zimbabwe Ltd	1st Street/Jason Moyo Avenue Harare Phone: 758280/99 or 758324 http://www.africa.barclays.com	747,026.09	2,991,712.58	300%
Commercial Bank of Zimbabwe	60 Kwame Nkrumah Avenue Harare Phone: 749714 or 748050/79/ 759110 Fax: 758077 http://www.cbz.co.zw	496,917.34	2,556,526.78	414%
First Banking Corporation Limited	Old Reserve Bank Building 76 Samora Machel Avenue Harare Phone: 700312/703529 (704165 D/L) Fax: 704995 http://www.firstbank.co.zw	197,844.44	442,613.07	124%
Kingdom Bank Limited	12th Floor, Karigamombe Centre 53 Samora Machel Avenue Harare Phone: 749400 or 758469/70 or 749407 or 091 235 315 Fax: 755201 http://www.kingdom.co.zw	252,965.37	646,088.56	155%

APPENDIX 3
REGISTERED AND OPERATING BANKING INSTITUTIONS AS AT 31 DECEMBER 2004 CONTINUED

COMMERCIAL BANKS		Total Assets: ZW$ millions		
Banking Institution	**Address and Website**	**2003**	**2004**	**% Annual Growth**
Metropolitan Bank of Zimbabwe Limited	Metropolitan House 3 Central Avenue Harare Phone: 706091/706128 (701970 – Direct) Fax: 733014 http://www.metbank.co.zw	83,356.45	230,389.29	176%
NMB Bank Limited	1st Floor, Unity Court Kwame Nkrumah Avenue Harare Phone: 759651/9 or 754933/5 or 70912268 or 70912409 http://www.nmbz.co.zw	289,521.96	1,137,940.37	293%
Stanbic Bank Zimbabwe Limited	Stanbic Centre Samora Machel Avenue Harare Phone: 759471 Fax: 772126 http://www.stanbic.co.zw	220,735.38	1,788,329.92	710%
Standard Chartered Bank Zimbabwe Limited	2nd Floor, Old Mutual Centre Cnr. Third Street/Jason Moyo Avenue Harare Phone: 253801-7 or 252289 Fax: 252288 http://www.stanchart.co.zw	584,201.87	4,055,615.26	594%
Zimbabwe Banking Corporation Limited	Zimbank House Cnr.1st Street/Speke Avenue Harare Phone: 751168/75 or 78662590/2576 or 757471-9 781693-7 http://www.finhold.co.zw	442,640.56	1,652,480.67	273%
MBCA Bank Limited	Old Mutual Centre 3rd Street/J Moyo Harare Phone: 701636/52 (739089-DL) Fax: 727330 http://www.mbca.co.zw	43,446.88	612,072.64	1309%

APPENDIX 3
REGISTERED AND OPERATING BANKING INSTITUTIONS AS AT 31 DECEMBER 2004 CONTINUED

MERCHANT BANKS		Total Assets: ZW$ millions		
Banking Institution	**Address and Website**	**2003**	**2004**	**% Annual Growth**
African Banking Corporation Limited	1 Endevour Crescent Mt. Pleasant Business Park Mt Pleasant Harare Phone: 727294/9 or 703071 369260-99 Fax: 338102 http://www.africanbankingcorp.com	206,293.33	464,119.70	125%
Genesis Investment Bank Limited	10th Floor, CABS Centre Jason Moyo Avenue Harare Phone: 703791/6 or 703551/3 Fax: 705491 http://www.genesis-zim.com	17,403.47	227,290.89	1206%
Interfin Merchant Bank	3rd Floor, Social Security Centre Cnr. Julius Nyerere Way/Sam Nujoma Street Harare Phone: 790824, 790901, 790791 Fax: 799492/252155 http://www.interfin.co.zw	302,446.59	478,631.92	58%
Renaissance Merchant Bank	7th Floor, Karigamombe Centre 53 Samora Machel Avenue Harare Phone: 773458/774686 Fax: 798910 http://www.renaissance.co.zw	110,529.87	321,989.01	191%
Premier Banking Corporation	137 Samora Machel Avenue Harare Phone: 706036/7 or 701350/3 or 703011/2/4/851642 or 851639/7 (Borrowdale) Fax: 794993 http://www.premierfinance.co.zw	14,439.29	44,297.59	207%

APPENDIX 3
REGISTERED AND OPERATING BANKING INSTITUTIONS AS AT 31 DECEMBER 2004 CONTINUED

BUILDING SOCIETIES		Total Assets: ZW$ millions		
Banking Institution	**Address and Website**	**2003**	**2004**	**% Annual Growth**
Beverley Building Society	Beverley Place Selous Avenue Harare Phone: 792631/5/705001 Fax: 705999 http://www.bbs.co.zw	117,850.54	298,829.00	154%
Central African Building Society	Northridge Park Northend Close Borrowdale Harare Phone: 883823-59 Fax: 883804 http://www.cabsonline.co.zw	131,251.86	479,619.00	265%
Zimbabwe Building Society	ZBS House 113 Leopold Takawira Street Harare Phone: 756811/6 or 772721/24/30/48 Web page not available	19,990.97	28,576.80	43%
Intermarket Building Society	1st Floor, Travel Centre, South Wing 95 Jason Moyo Avenue Harare Phone: 702571 or 705833/705 http://www.intermarket.co.zw	64,447.97	141,082.00	119%

APPENDIX 3
REGISTERED AND OPERATING BANKING INSTITUTIONS AS AT 31 DECEMBER 2004 CONTINUED

FINANCE HOUSES		Total Assets: ZW$ millions		
Banking Institution	**Address and Website**	**2003**	**2004**	**% Annual Growth**
African Banking Corporation Asset Finance (Ltd)	1 Endevour Crescent Mt. Pleasant Business Park Mt Pleasant Harare Phone: 727294/9 or 703071 369260-99 Fax: 338102 http://www.africanbankingcorp.com	17,265.70	177,817.05	930%
Sagit Finance House Limited	14th Floor, Intermarket Life Towers 77 Jason Moyo Avenue Harare Phone: 794053/794486 or 774294/790616/794986 Fax: 792017/792570 http://www.sagit.co.zw	4,955.02	24,045.19	385%
ZDB Financial Services Limited	ZDB House, 99 Rotten Row Harare Phone: 774226/7, 750171/8, 751341 Fax: 720724/774225 http://www.zdb.co.zw	24,124.92	40,900.00	70%
Trustfin Finance House	First Floor, Building 1 Arundel Office Park Mt Pleasant Phone: 338235/52, 338254 Fax: 338253	34,341.92	33,119.89	-4%

APPENDIX 3
REGISTERED AND OPERATING BANKING INSTITUTIONS AS AT 31 DECEMBER 2004 CONTINUED

DISCOUNT HOUSES		Total Assets: ZW$ millions		
Banking Institution	**Address and Website**	**2003**	**2004**	**% Annual Growth**
African Banking Corporation Securities (Ltd)	1 Endevour Crescent Mt. Pleasant Business Park Mount Pleasant Harare Phone: 727294/9 or 703071 369260-99 Fax: 338102 http://www.africanbankingcorp.com	70,972.3	64,553.13	-9.06%
Discount Company of Zimbabwe Limited	70 Park Lane Harare Phone: 708945/6 or 705414 Fax: 731670 http://www.kingdom.co.zw	25,044.6	54,090.92	115.98%
Highveld Financial Services	12th Floor, Pearl House 61 Samora Machel Avenue Harare Phone: 700462/3, 700471, 700533/ 851642 Fax: 700565 Web page not available	13,623.79	26,182.13	92.18%
National Discount House Limited	5th Floor, MIPF House 5 Central Avenue Harare Phone: 700771/5 or 705596/8 Fax: 705118/251402 http://www.ndh.co.zw	12,477.84	48,638.33	289.80%
Tetrad Securities Limited	9th Floor, Pegasus House Samora Machel Avenue Harare Phone: 704271/5, 302625 Fax: 704149 http://www.tetrad.co.zw	13,719.75	32,277.32	135.26%

APPENDIX 4
BANKING INSTITUTIONS UNDER CURATORSHIP & LIQUIDATION

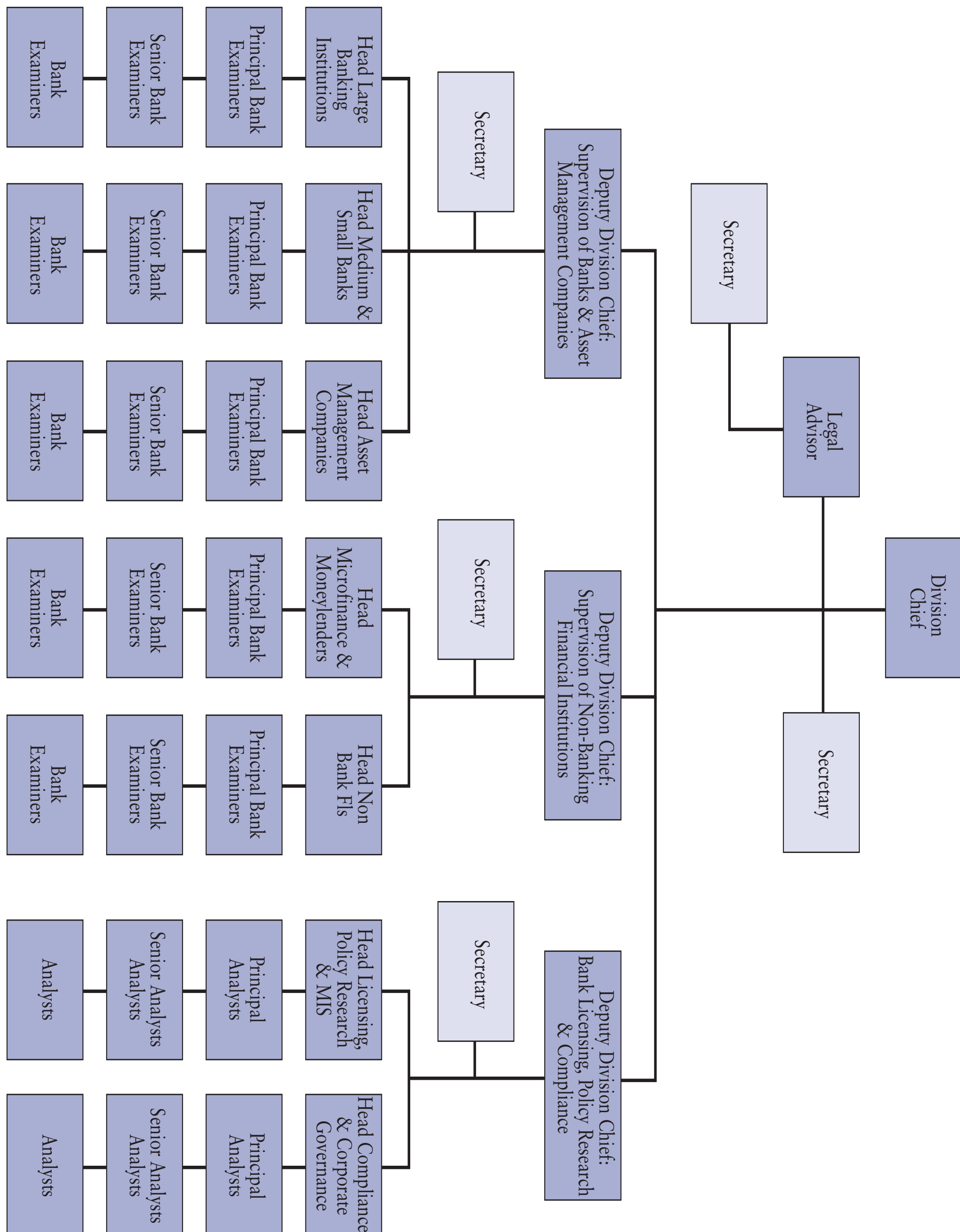
TABLE 4A: BANKING INSTITUTIONS UNDER CURATORSHIP

Banking Institution	Curator	Date of order
1. Barbican Bank	Mr. T. Matavire, KPMG	15 March 2004
2. Royal Bank Zimbabwe Limited	Mr. M. Moyo, KPMG	4 August 2004
3. Intermarket Discount House	Mr. N. Kudenga, Kudenga & Company	12 March 2004
4. Intermarket Banking Corporation	Mr. N. Kudenga, Kudenga & Company	12 March 2004
5. Intermarket Building Society	Mr. N. Kudenga, Kudenga & Company	12 March 2004
6. CFX Bank Limited	Mr. F. Kuipa, Ernst & Young	17 December 2004
7. CFX Merchant Bank	Mr. F. Kuipa, Ernst & Young	17 December 2004
8. CFX Asset Management	Mr. F. Kuipa, Ernst & Young	17 December 2004
9. Trust Bank Corporation Limited	Mr. P. Bailey, KPMG	23 September 2004
10. Time Bank of Zimbabwe Limited	Mr. T. Rwodzi, PriceWaterhouseCoopers	27 October 2004

TABLE 4B: BANKING INSTITUTIONS UNDER LIQUIDATION

Institution	Liquidator
1. Century Discount Houses	Mr. C. Madondo
2. Rapid Discount House	Mr. M. Mubaiwa
3. First National Building Society	Mr. D. Scott

APPENDIX 5
BANK LICENSING SUPERVISION AND SURVEILLANCE DIVISIONAL STRUCTURE



PROFILE OF BANK LICENSING, SUPERVISION & SURVEILLANCE (BLSS)

The Division comprises three departments, namely:

a) Supervision of Banks & Asset Management Companies;
b) Supervision of Non-Banking Financial Institutions; and
c) Bank Licensing, Policy, Research & Compliance.

1.1 Supervision of Banks & Asset Management Companies

a) This department is responsible for conducting the following functions:

- on-site examinations, both full-scope and targeted, to determine the financial condition of banking institutions and asset management companies;
- off-site supervision, which involves the analysis and evaluation of statutory returns submitted to the Reserve Bank, both on a solo and consolidated basis, utilising predetermined performance indicators. The off-site supervision function acts as early warning system to identify emerging problems at banks and asset management companies;
- investigations on banking institutions and asset management companies. Where peculiar problems are noted investigations are conducted in liaison with other divisions.
- consolidated supervision, which involves the evaluation of the strength of an entire banking group, taking into account all the risks which may affect a bank, regardless of whether these risks are carried in the books of the bank or related entities; and
- where problems are identified at the financial institutions and asset management companies, BLSS recommends prompt enforcement of corrective action based on applicable laws and legislation. The corrective action taken ranges from moral suasion to curatorship and/or liquidation.

1.2 Supervision of Non-Banking Financial Institutions

a) This department is responsible for the oversight of non-banking financial institutions, which include the microfinance institutions, money lending institutions, People's Own Savings Bank (POSB), Zimbabwe Development Bank (ZDB), Small Enterprises Development Corporation (SEDCO) and venture capital companies.

b) As in the case of banks and asset management companies, the ongoing supervision of non-banking financial institutions is conducted through on-site examinations and off-site analyses.

1.3 Bank Licensing, Policy, Research & Compliance

a) The department is responsible for the following:

- licensing of banking and non-banking financial institutions;
- evaluation of local mergers and acquisitions, restructuring proposals, and cross border investments by banks, including opening of subsidiaries, branches, and representative offices;
- accreditation of rating agencies to complement prudential regulatory efforts in promoting financial stability through enforcement of market discipline, transparency and bridging the information gap;
- drafting of regulations, guidelines and amendments to statutes administered and applicable to the Reserve Bank;
- developing prudential benchmarks for guidance of bank examiners and the financial sector;
- provision of information, internally and externally, on the status of the financial sector through reports and posting of the status reports on the Reserve Bank website; and
- facilitating discussions on policies and regulations with internal and external stakeholders.

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