

WHAT ZAMBIA'S RECLASSIFICATION AS A LOW-INCOME COUNTRY MEANS

In the early 2000s, Zambia underwent robust economic growth and this led to the World Bank classifying it as a lower-middle income country (LMIC) in 2011 (due to a healthy macroeconomic position in 2011, resulting from high economic growth since 2002 averaging between 6 and 7 percent and a sound government budget). This was after it had spent many years being classified as a low-income country (LIC). In spite of the 2011 classification of Zambia as a LMIC, it still belonged to the group of least developed countries in the world and its classification as a LMIC by the World Bank only covered up its high levels of economic and social vulnerabilities. Some of the economic and social vulnerabilities which were covered up by the classification of Zambia as a lower-middle income country include: its excessive reliance on copper exports which account for more than 70% of Zambia's exports and this makes it prone to the volatile global commodity price movements; vulnerability to external shocks; high poverty levels and food insecurity. With regards to the poverty situation, more than 50% of Zambia's population live below the poverty line. In 2018, Zambia was ranked as the fifth hungriest country in the world by the Global Hunger Index and the hunger situation in Zambia is provisionally categorized as serious.

The classification of Zambia as a lower-middle income country (LMIC) presented Zambia with an opportunity to tap into the private capital markets and it did. It also gained access to other financing options such as Chinese loans and other commercial debt. From 2012, the Zambian government issued three Eurobonds amounting to almost \$3 billion (in 2012 the Zambian Government issued a \$750 million Eurobond at a coupon rate of 5.375%, in 2014 the Zambian Government issued a \$1 billion Eurobond at a coupon rate of 8.5% and in 2015 the Zambian Government issued a \$1.125 billion Eurobond at a coupon rate of 8.97%) which at the time was more than 40% of public external debt. It should also be noted that each of Zambia's Eurobond issuances was more expensive than the last in both principal and interest rate. The Eurobonds issued by the Zambian government were low quality bonds and such bonds attract higher yields than investment-grade bonds. The higher yields on low quality bonds are associated with increased risk and this increased risk is due to the possibility of default by the issuer (in this case the Zambian Government). This is due to the increased risk of paying back each successive loan. In 2016, Chinese loans accounted for a quarter of Zambia's total external debt and concessional financing from the development assistance committee (DAC) decreased significantly. Despite the fact that debt levels in countries across the world increased, Zambia's debt levels grew at a much higher rate. This has led to Zambia experiencing high debt servicing costs due to the high concentration of maturities and borrowing at varying interest rates.

Every year on July 1, the World Bank classifies the world's economies into four income groups — low-income, lower-middle income, upper-middle income, and high income. The classifications are based on the gross national income (GNI) per capita of the previous year (so for 2022, the year used was 2021) and are expressed in United States dollars (USD), and determined using conversion factors derived according to the Atlas method. The Atlas conversion factor for any year is the average of a country's exchange rate for that year and its exchange rates for the two preceding years, adjusted for the difference between the rate of inflation in the country and international inflation. The Atlas method reduces the impact of exchange rate fluctuations in the cross-country comparison of national incomes.

This year's World Bank classifications saw Zambia reclassified as a low-income country after it recorded a GNI per capita of US\$1040 in 2021 and this was a downgrade from its

previous classification of lower-middle income country (a classification it enjoyed for about a decade). While a rebound in the price of copper boosted Zambia's gross domestic product (GDP) in 2021, a sharp deterioration in exchange rates led to a large decrease in the Atlas GNI per capita expressed in US dollars, reclassifying Zambia to the low-income group. For the 2023 fiscal year, low income countries are defined as those with a GNI per capita of USD\$1,085 or less in 2021. On the other hand, lower-middle income economies, upper-middle income economies and high-income economies are those with a GNI per capita between: US\$1, 086 and US\$4, 255; US\$4, 256 and US\$13, 205 and US\$13, 205 or more in 2021 respectfully.

Zambia is not the only country that saw itself being reclassified to a lower income group after the July 1 World Bank classification. Lebanon's GDP per capita fell in 2021 for the eleventh consecutive year and its exchange rate experienced a sharp depreciation. As a result, Lebanon, which enjoyed an upper-middle income status for almost 25 years was reclassified as a lower-middle income country. Palau, a tourism dependent country will now move to the upper-middle income group after it saw its tourism industry and other industries severely impacted the Covid-19 pandemic.

Zambia's economy has been performing poorly over the past few years with inflation rate as high as 24.6% in June and July 2021, poverty rate above 50%, GDP as low as -2.8 % in 2020, unemployment rate as high as 13.8% in 2020, persistent depreciation of the Zambian Kwacha, Balance of Payment deficits as high as 2.2% of GDP in 2020 and high debt burden leading to a default in 2020.

Given Zambia's many challenges this reclassification comes with opportunities such as increased access to funding on concessional terms and financial aid as wealthier countries and/or international aid organizations often give low-income countries financial aid to help boost and support their economic, political, social, and environmental development. This may come in the form of bilateral aid, which is given directly from the donor country to another, or multilateral aid, which is given by international organizations such as World Bank, Africa Development Bank and the International Monetary Fund IMF, which distribute aid to developing countries. This also increases the chances of Zambia having its debt restructured under the G20 common framework.

The World Bank's reclassification of Zambia as a low-income country should give the government time to reflect on how to best move our economy in the right direction and out of this debt trap that we are currently in. The potential for the Zambian economy to grow and be classified as a lower-middle income country (LMIC) again by the World Bank is quite high. When this happens, the government ought to be very careful to learn valuable lessons from the post HIPC extravagant borrowing and be very prudent at managing the financial resources of our country. The risk of not learning from our past could lead us into a similar mess that we are currently facing as a country or even worse. Going forward the government should watch the debt to GDP ratio and pay very close attention to it. The suspension of certain projects which were being funded by the borrowed funds is commendable and has the possibility of enhancing the Zambian government's fiscal responsibility.