# WHY ZAMBIA DESPERATELY NEEDS THE IMF BAILOUT

The Zambian Government recently reached a staff-level agreement with the International Monetary Fund (IMF) team on a new arrangement under the Extended Credit Facility (ECF) for 2022-2025 to help it restore its macroeconomic stability and provide the foundation for an inclusive economic recovery. The Staff-Level Agreement between the IMF and the Government of Zambia stipulates the economic policies, financial policies and reforms which the Government will take up over time. This three-year extended credit facility is worth about SDR 980 million or $1.4 billion and it brings Zambia one step closer to a comprehensive debt overhaul. We should all bear in mind that this ECF is yet to be approved by the IMF's management and Executive Board.

Even though the staff-level agreement is yet to be approved, it is already bearing fruits for Zambia and this can be seen in the Zambian kwacha (ZMW) appreciating against the United States (US) dollar. Following the announcement of the staff-level agreement, the Zambian kwacha appreciated to K16.0000 per dollar on 9th December, 2021, from a close of K17.8078 on 2nd December, 2021. Entities or individuals holding foreign exchange are likely to start converting to the Zambian Kwacha to avoid further foreign exchange losses. The current high US dollar supply and sudden inflows into Zambia of US dollars is coming from off-shore market players and corporations closing off their dollar positions. The Zambian kwacha (ZMW) is expected to continue making further gains against the US dollar due to positive sentiment from the staff-level agreement reached between the IMF and the Zambian Government for a bailout. Market fundamentals have remained largely unchanged and this means that the current appreciation in the Zambian kwacha against the dollar is only being driven by investor sentiment.

As long as the Zambian kwacha's appreciation is sustained, it could contribute to fighting current high inflation levels and compliment the Bank of Zambia's Monetary Policy Rate adjustment by 50 basis points to 9%. This means that fewer Zambian kwachas will be needed to buy US dollars.

Zambia is a highly indebted country and most of the debt was accumulated in the last decade by the previous Patriotic Front (PF) Government. It was the previous PF Government's expansionary fiscal policies that contributed to Zambia's debt problems. The PF Government's expansionary fiscal policies for public investments, despite falling revenues, contributed to widening fiscal deficits (8.3% of GDP in 2019 and 11% of GDP in 2020). The PF Government's expansionary fiscal policies, which were mainly financed by external and local borrowing, led to Zambia's public and publicly guaranteed debt to rise to 91.6% of GDP in 2019 and 104% of GDP in 2020. In the medium term, Zambia's debt to GDP ratio is expected to remain high. On 3rd November 2020, Zambia became the first African country to default on its international debt since the outbreak of Covid-19, as it couldn't make the $42.5 million in interest payments on its three Eurobonds in mid-October and it also couldn't honour payments at the end of the grace period given by the investors.

One of the fiscal adjustments in the economic reforms the Government is currently pursuing is the removal of subsidies. With the pending removal of fuel and electricity subsidies, the Zambian people especially the poor and vulnerable in society would really appreciate if the Zambian Kwacha continues its rally and stabilizes below K10 per US dollar and the cost of oil remains below a $100 per barrel. Increasing the prices of these two items in the energy sector which are non-discretionary and impossible to substitute will have a significant impact on inflation in Zambia and the poor and vulnerable would be negatively impacted by this potential rise in inflation once the subsidies are removed. This could mean higher fuel prices for Zambians and higher inflation as removal of fuel and electricity subsidies alone has the potential to drive inflation up.

The Zambian Government intends to invest more resources in its people, particularly youth and women empowerment. This is why the removal of subsidies on fuel and electricity is crucial. It is unsustainable to keep subsidizing the energy sector especially with the ambitious 2022 budget in which the Zambian Government is offering free education up to Grade 12, intends to hire 30,000 teachers and also intends to hire about 11,000 medical personnel in the health sector. Money that is currently being used to finance subsidies in the energy sector and any other inefficient public investment will be redirected to finance greater investment in healthcare, education and the delivery of more social benefits to the Zambian people. Apart from rationalizing expenditure, the government also seeks to enhance revenue mobilization through policy and administrative changes. These are some of the economic reforms in the IMF deal.

In 2017, the PF Government started talks with the IMF on a $1.3 billion bailout and their requests were turned down several times. Once Zambia's application for an Extended Credit Facility from the IMF is approved by the IMF management and Executive Board, it is going to allow Zambia to start debt restructuring engagements with its creditors. The Debt Sustainability Analysis (DSA) exercise, undertaken during technical discussions with the IMF provides the basis for the Zambian Government's engagement with creditors. Debt restructuring means that Zambia is going to have an opportunity to refinance its external debt. **Debt refinancing** is when you replace your existing debt with new debt that has more favourable terms such as lower and less frequent coupon payments. Debt refinancing is going to allow the Zambian Government to consolidate all external debt to a single lender and this helps with cash flow management as payments are due just once a month, rather than across multiple days and this also makes budgeting and payment processing much less time consuming. Debt restructuring will also give the Zambian Government a chance to reduce its interest rate with the IMF and take advantage of special rates. Debt restructuring could also allow the Zambian Government to restructure to a more suitable loan facility.

The Zambian Government stands to benefit through budget support from multilateral development banks and bilateral aid once talks with its creditors result into an agreement and once the ECF is approved by the IMF management and Executive Board. Multilateral development banks provide funds in the form of loans and grants for projects that support social and economic development, e.g., funds to build new roads or funds to support clean water projects. An approved ECF from the IMF management and Executive Board is going to prop up macroeconomic conditions and boost investor confidence in Zambia.

The staff-level agreement between Zambian Government and the IMF team on a new arrangement under the Extended Credit Facility (ECF), will contribute to the fiscal reforms that Dr. Kalyalya stressed would complement the central bank's monetary policies on low and stable inflation. The IMF deal compliments the Monetary Policy Committee's policy rate adjustment by increasing investor confidence in Zambia and this could lead to economic growth through business investments. Business investments will create opportunities for more employees to be hired and this would mitigate the loss of employment through the MPC's contractionary monetary policy rate adjustment.

Advantages of the IMF's ECF for Zambia include:

- It will help enhance the local economy through the boosting of investor confidence which could lead to more investment and reduced unemployment in the country
- It will help the Zambian kwacha appreciate against the US dollar and other currencies
- It will help restore price stability through promotion of efficient and long-term growth
- It will help bring the debt management problem under control by allowing Zambia to refinance its debt
- It will help Zambia achieve higher inclusive growth
- The deal will provide fiscal space for the Government to hire 30,000 teachers, eliminate tuition fees up to grade twelve and also allow the Government to employ more healthcare workers
- It will help Government administer reforms aimed at increasing checks and balances required for Government to acquire new debt. It will also help the Government enhance revenue mobilization

Without the IMF deal, Zambia risks:

- The exchange rate getting worse due to the current economic status
- Prices will escalate due to low production in the country and low production due to less investment in production due to high interest rates following the Monetary Policy Rate adjustment by the Bank of Zambia
- Poverty will get out of hand due to lack of jobs in the economy
- The credibility of government plans such as the national budget and its commitment to debt restructuring will be low. Government policies are prone to the time inconsistency problem which could mean Government trading long-term debt sustainability with short-term appeasement policies.

In his press statement during the joint media briefing with the Zambia IMF mission chief on 6th December, 2021, Zambia's Minister of Finance and National Planning, Dr. Situmbeko Musokotwane, emphasized that the staff level agreement which the Zambian Government reached with the IMF is based on the economic reform programme that the Zambian Government is currently pursuing. The economic programme which the Ministry of Finance presented to the IMF is therefore a Zambian economic programme **developed by Zambians for Zambia** and it aims to restore macroeconomic stability and promote higher, more resilient, and inclusive growth and the IMF is only going to support its implementation. Therefore, it is very critical for the Zambian people to understand that this is **NOT** the IMF's programme for Zambia. The Zambian people should not be afraid of the staff-level agreement reached between the IMF and the Government of Zambia because the benefits of having this deal outweighs the risk of Zambia not having this deal.

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