

**FIGHT
INEQUALITY**



FIGHT INEQUALITY ALLIANCE ZAMBIA



OPTIONS FOR EQUITABLE ECONOMIC GROWTH AND DEVELOPMENT IN ZAMBIA

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ECONOMIC GROWTH AND
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#IMFAlternatives, #BeyondTheIMF, #IMFZambia, #FightInequality, #TimeToTaxTheRich
#PeoplesEconomicRecovery, #Peoplesbudget, #DebtCancellation

EXECUTIVE SUMMARY

This paper is an analysis of the Zambian government's fiscal situation with an emphasis on the recently concluded Staff Level Agreement with the International Monetary Fund (IMF) with a view to establish the ramifications of this strategy on economic recovery, poverty and inequality. The paper also considers alternative financing options that could have been/can be pursued other than the route of the IMF. The paper was prepared for the Fight Inequality Alliance Zambia in their effort to bring about a Zambia without inequality.

In 2011 Zambia achieved the World Bank's middle-income country status. This new status, along with austerity measures in high income countries, made Zambia less able to access multilateral and bilateral concessional loans. The government of the day, to fulfil campaign promises, embarked on ambitious infrastructure projects and utilized Zambia's newfound creditworthiness to access external loans. These external loans largely came from the international bond market (Eurobonds) and from non-Paris club nations, particularly China. By June 2021, Zambia's total public debt had grown to USD26.96 billion dollars with an external component of USD14.4 billion. These numbers, and other indicators, suggest that Zambia has been in the throes of a Balance of Payments (BOP) crisis since about 2015. In other words, the country needs to source foreign exchange to forestall a dire economic situation in the present decade.

Different financing options are available to the government including, but not limited to, pursuing the IMF. These include rolling-over, restructuring, reprofiling, refinancing and repurchasing of debt. Any financing option has trade-offs, and the circumstances that led to Zambia's present debt situation and the accompanying loss of credibility with international creditors leave little room for manoeuvre. However, the assessment of options needs to weigh both the need to restore credibility and demonstrate fiscal discipline, against maintaining sufficient policy options to enable inclusive and inequality reducing growth and poverty reduction. On the back of strong and widespread support for the United Party for National Development (UPND) government in the August 2021 election, there may be a case for parallel consideration of non-IMF financing options premised on the opportunity to demonstrate fiscal discipline and credibility whilst maintaining policy autonomy.

However, the Zambian government has opted to go for a financing route that relies quite significantly on the IMF. The IMF and Zambia have had a long relationship with IMF BOP support rising to prominence during the economic crisis of the late 1980s and 1990s. There is ample evidence that IMF support to Zambia, particularly in the 1980s and 1990s, has been disastrous for the country's growth and development aspirations. In the current moment, the Zambian government and the IMF have reached a Staff Level Agreement (SLA) with a promise of accessing up to USD1.4 billion in a three-year Extended Credit Facility (ECF). The process resulting in the SLA took place behind

a veil of secrecy and the Zambian public is yet to know what conditions have been agreed to in exchange for the ECF. It is without doubt, however, that the agreement will result in widescale increases in poverty and inequality. The drastic reductions in government expenditure over the next five years (i.e. austerity), which we estimate at USD4 billion, will impact the poor and marginalized more than any other group. The subsidies that are targeted for removal (energy and agriculture) have the poor and marginalized as the biggest beneficiaries. The claim made by government and the IMF that savings from subsidy removal will be spent on the poor does not survive careful scrutiny. Pro-poor expenditure is projected to be small and unimaginative. In certain instances, as is the case with the education sector, promises of free service delivery appear to be laden with hidden fees. Conversely, reducing taxes on the corporate and mining sectors will serve to enhance the earnings accruing to the small cadre of Zambians engaged in these sectors at the expense of millions in the country.

Our report concludes by recommending:

- The Fight Inequality Alliance Zambia should develop an advocacy strategy that will seek to counter the avalanche of neoliberal economic policymaking that will dominate the Zambian policy space over the next five years.
- As the analysis in this report demonstrably proves, there were many alternative options to getting on an IMF programme. For example, our analysis reveals that the best pathway forward would have been a non-IMF financing option implemented with increased fiscal discipline in order to achieve the desired credibility. Unfortunately, the Zambian government did not proactively engage with diverse voices at the very early stage in the process. A strong recommendation emanating from this is that going forward, a mechanism for broad-based consultations be put in place in such a way that decisions arrived at by the Zambian government are based on widescale consultations and are based on broad public support.
- A close analysis of the policy process that led to the IMF agreement shows that it lacked transparency. Even though the Staff Level Agreement was announced with much fanfare on 3rd December 2021, we are yet to know the exact wording of the agreements between the government and the IMF at the time of writing this report. It would be in the best interests of the nation to devise economic policy, especially one as seismic as this, in the open.
- Finally, the report calls for a reversal of the generous incentives given to the corporate sector especially the mining industry. Reducing inequality and poverty will require the marshalling of all of the country's resources especially revenue from our God-given mineral resource.

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1. OVERVIEW

This paper is an analysis of the Zambian government's fiscal situation with an emphasis on the recently concluded Staff Level Agreement with the International Monetary Fund (IMF) with a view to establish the ramifications of this strategy on recovery, poverty and inequality. The paper begins with a brief history of Zambia's debt contraction between 2011 and 2018 in order to demonstrate what led to the country's current debt sustainability concerns. This is followed by an analysis of the various financing and policy options (aside from an IMF facility) that the government could or should explore to achieve debt relief and steer the country towards economic growth. The paper continues with a discussion on the IMF, its institutional policies as well as the application of those policies when contracting with member countries. The discussion further examines the implications of an IMF facility on social programmes in the context of addressing inequality drawing largely from Zambia's own history with the IMF. Finally, the paper concludes with policy recommendations to ensure that the economic recovery and desired growth is inclusive.



2. EMERGENCE OF THE CURRENT DEBT CRISIS

In 2011 Zambia achieved the World Bank's middle-income country status. This new status, along with austerity measures in high income countries, made Zambia less able to access multilateral and bilateral concessional loans. The government of the day, to fulfil campaign promises, embarked on ambitious infrastructure projects and utilized Zambia's newfound creditworthiness to access external loans. These external loans largely came from the international bond market (Eurobonds) and from non-Paris club nations, particularly China.¹

Zambia has had three issuances of Eurobonds issued between 2012 and 2015 to the value of USD3 billion and at interest rates of 5.75 percent, 8.5 percent and 8.97 percent respectively. Bonds in this context are fixed income debt instruments that represent a loan advanced by an investor facilitated by the purchase (or "subscription") of these instruments from a borrower such as a government or corporation, which issues them. Eurobonds are simply instruments that are issued in a currency other than the local currency of the issuing country.

Another significant source of Zambia's external debt is China. The Chinese loans are typically provided by state owned commercial lenders which include the Industrial and Commercial Bank of China, the Chinese Development Bank and Export Import Bank of China. The Chinese loans are attractive due to their below market interest rates and flexible repayment options. Additionally, unlike most multilateral loans, Chinese loans are not conditional on meeting conditionalities or international standards. Between 2012 and 2017, the external debt from China grew by almost 300 percent. By 2018, Chinese Loans accounted for 27 percent of Zambia's external debt load and 31 percent of Zambia's external debt service (Barclays, 2019). Although it is important to note that there has been much debate about the actual quantity of Chinese debt due to the complex ways in which such debt is contracted.

According to the Public Debt Summary (PDS)² issued by the Ministry of Finance & National Planning (MOFNP) in October 2021, the total amount of debt attributable to Zambia's public sector including interest arrears stood at USD26.96 billion as of 30 June 2021. However, it is important to note that this is a total amount representing both domestic and external debt. The external debt alone was USD14.4 billion.

¹Joshua Charles and Lev Lascu. A Barometer for a Perfect Storm: The Causes of the Zambian Debt Crisis and Indicators for Tracking Public Debt Management Progress. AFRODAD. 2019

²https://www.mof.gov.zm/?wpfb_dl=378

The World Bank and IMF periodically conduct a joint Debt Sustainability Analysis (DSA) framework for Low Income Countries (LICs) (together the “LIC-DSA”) which classifies countries according to their ability to access international financial markets on the one hand, and their capacity to service debt on the other, which in-part determines the proportion of debt as a portion of the Gross Domestic Product (GDP) that an assessed country can take on sustainably. In short, debt sustainability is a measure of how much debt a country can sustain relative to the size of its economy.

In the IMF's DSA for Zambia conducted in 2017, Zambia was considered to have “medium capacity”³, but was re-evaluated to have “weak capacity” in 2019 based on low levels of foreign exchange reserves, thereby reducing the amount of implied total external debt that the country could sustain relative to the size of its economy, or that it could service relative to fiscal revenue. Although it is important to point out that there is some debate as to whether the methodologies employed in the DSA analyses are robust enough. For example, some have argued that the DSA framework exaggerates debt concerns in developing countries.⁴

In the wake of the Covid-19 pandemic, Zambia's debt levels rose to the point that the country defaulted not less than twice on its Eurobond coupon repayments, the fiscal deficit rose well above the 5.5 percent target, standing at 11.7 percent in 2020 and the national currency, the Kwacha depreciated by almost 100 percent in 2020. In addition, the cost of living in Zambia has been rising, with year-on-year inflation peaking in January 2021 with a recorded excess of 21 percent.⁵

A breakdown of the total debt stock as of June 2021 is as follows:

- a. USD16.86 billion (including USD520 million in arrears) denominated in foreign currency, representing 62.5 percent of the total debt stock, comprising:
 - i. Central government loans, totalling USD13.38 billion including arrears
 - ii. State-owned enterprises totalling USD3.48 billion including arrears
- b. USD10.10 billion, representing 37.5 percent of the total debt stock, comprising:
 - i. Treasury bills and bonds, equivalent to USD7.96 billion
 - ii. Domestic arrears, equivalent to USD2.07 billion
 - iii. Government and SOE loans in local currency, equivalent to USD0.06 billion.

This section has demonstrated that the Zambian economy has unsustainably contracted debt over the last decade. The next section considers different options that maybe available to the authorities as sustainable financing options.

³Broadly implying that Zambia could sustain a public debt stock of up to 55 percent of GDP, and service external long-term public and publicly guaranteed debt of up to 18 percent of government revenue.

⁴Hannah Ryder, How multilaterals exaggerate Africa Risk. <https://african.business/2021/09/trade-investment/how-multilaterals-exaggerate-africa-risk/>

⁵Gabriel Pollen. An analysis of the Economic Recovery Plan. Centre for Trade Policy and Development. 2020



3. FINANCING OPTIONS FOR ZAMBIA

This section considers the various financing options available to Zambia. The section starts with a (technical) discussion of financing options in general. Thereafter, the specific case of Zambia is considered in some detail.

3.1. Overview of Sovereign Financing Options⁶

There are various commercial and concessional sources of sovereign funding, including debt and non-debt options, that Zambia may consider⁷. Broadly, financing involves getting cash today (or over time) by either one or a combination of:

a. Committing to repaying the cash over time on agreed terms (Type A Options)

This best aligns with debt financing, where the provider of cash (the “creditor”) is compensated for time, inflation and risk (typically through a “coupon rate”⁸ or “premium”) on the cash provided (the “principal”). More detail is provided below.

b. Ceding the receipt of cash from a given source over time on agreed terms (Type B Options)

This is where the receiver of cash agrees to give-up cash or benefits that are due to them in the future. A good example of this is equity or shares in a company, which entitle the shareholder to receive a dividend in the future, when the company makes profits. More detail is provided below.

3.2. Overview of Debt Financing Options

This section provides an overview of Type A Options described above, with selected debt options available to Zambia. Debt may be classified in various ways:

a. Concessional or Commercial

- Concessional debt is contracted on terms considered to be more favourable (or generally cheaper) than would ordinarily be the case in the general market, and usually with broader strategic objectives or conditions that justify the below-market

⁶See Appendix 1 for more detail

⁷Excludes grant or Official Development Assistance

⁸Typically a fixed percentage of the amount received

rates (e.g the IMF Extended Credit Facility, infrastructure loans from Chinese lenders, loans from development banks, etc).

- Commercial debt is contracted on terms that are based on how the lending market perceives the risk of the lender (e.g Eurobonds, loans from commercial banks, etc...).

b. Who is the lender?

- Official lenders are those that are state-related, including:
 - » Bilateral lenders, which are individual or state-sponsored financial institutions (SSIs) (e.g China, or the China EXIM bank);
 - » Plurilateral lenders, which are closed groups of individual or SSIs (e.g Scandinavian countries); and
 - » Multilateral lenders, which comprise and represent the interests of multiple states (e.g the IMF and World Bank).
- Commercial or private lenders are non-official lenders that provide debt on an arms-length basis either directly, through projects or via the international capital market (e.g commercial banks, Eurobond holders).

c. Is the debt in the form of a “loan” or a “bond”?

- Loans generally involve a contract with one party lending to the other (the “borrower”).
- Bonds generally involve the recipient of funds creating financial instruments (the “issuer”) which are purchased by investors. Once purchased, investors are typically free to sell or buy these in a secondary market.

d. Can the lenders go after the borrower's assets if they fail to pay?

- Secured debt allows the creditor to pursue identified assets of borrower, which may be tangible (such as property, a port etc) or intangible (such as a guarantee, shares, funds receivable from third parties, revenue etc).
- Unsecured debt does not allow the creditor to pursue the borrowers assets, as set out above. Therefore, unsecured creditors lend on the basis of the borrower's ability to pay.
- Guarantees involve a credible third-party providing assurance to creditors of meeting all or part of the obligations of the borrower if they fail to repay the loan (or breaches their contract). In this way, it serves as a form of security.

e. Does the financing have conditions attached?

- Debt with Conditionality requires the borrower to commit to performing some condition or meeting some defined outcome. Conditionality is typically attributable

to financing from official lenders such as the IMF or the provision of aid but may also apply to “outcome based” financing such as Social Impact or Green Bonds.

- Debt without Conditionality generally has little or no strings attached. This may still require the borrower to clarify how the funds will be used. For example, Zambia's first Eurobond did not have conditionality, but specified that the proceeds were targeted for specific infrastructure development projects.

f. Is the debt simple or complex in structure?

- Plain vanilla describes the simplest form of debt. This is in the form of a coupon rate payable at a fixed percentage⁹ of the principal amount, and the principal is repaid in a defined manner. The payment obligations from plain vanilla debt are easy to predict for the borrower.
- Exotic debt has additional features, including some discussed above, that may change the interest or principal payable based specified outcomes or events. This adds complexity to the debt, making it harder to predict for lenders.



⁹This may also be 0 percent, for “zero-coupon” debt, but typically involves a compensatory payment at the end of the term

3.3. Overview of Other Financing Options¹⁰

This section focuses on the Type A Options, with a focus on equity and royalty financing, though may loosely be applied to exotic debt:

a. *Equity*

- Equity is effectively an ownership interest in an asset such as property, infrastructure or a company. Equity-holders (or “shareholders”) generally benefit from the asset when it is profitable and pays a dividend, or when they sell it at a higher price than they bought it for.
- In the context of a government shareholder, there may be additional considerations or objectives for shareholding, such as job creation, economic competitiveness or strategic positioning, that may supersede a profit objective.
- Equity financing is generally achievable by selling shares in the asset at an attractive value. This “value” depends on the future prospects of the asset, and its ability to generate cash (after expenses) for its owners.
- The proceeds from the sale of the Zambian Government's interests in previous SOEs via privatisation in the early 1990's and 2000's represents a form of equity financing. Privatisation has both benefits and drawbacks, but altogether needs to be managed effectively and need not always result in complete government withdrawal, a bad deal value for the country, or not be conducted transparently.

b. *Royalties*

Royalty financing is usually based on cash receivable from the sale of some globally tradeable commodity such as copper, gold or oil. For the Zambian Government, an example is cash received from mineral royalties.

3.4. Key Considerations for Zambia¹¹

a. *Zambia's debt obligations are not sustainable, in the short-term*

When referring to Zambia's “debt-sustainability” or of the country being at “high risk of debt distress”, most refer to the Zambia's debt as a portion of GDP, usually in the context of the LIC-DSA presented in section 2. The key liquidity and solvency requirements¹² under the DSA are presented in appendix 4.

Our analysis of Zambia's debt profile reveals the following information¹³:

- Approximately 70 percent of Zambia's debt obligations over the next 13 years are due within five years, between 2022 and 2026
- Most (approximately 40 percent) of this debt is attributable to repayment of the principal on maturing Eurobonds in 2022, and between 2024 and 2027

¹¹See Appendix 4 for more detail

¹²<https://www.undp.org/sites/g/files/zskgke326/files/publications/54241%20-%20UNDP%20WP%20Debt%20Vulnerability-web.pdf>

¹³See Appendix 4

- Beyond five years, total debt service reduces from just over USD500 million to under USD250 million by 2034, suggesting that a debt reprofiling may be achievable depending on long-term Government revenue
- Based on Government fiscal revenue projections over the next five years, Zambia's projected interest obligations are within the solvency limit for Weak Capacity LICs

The last two points assume no new debt is contracted and that DSOs are met per contractual obligation, which has been superseded by Zambia's default in 2020 and initiatives such as the DSSI.

b. Possible actions regarding existing debt stock

Sections 3.1 to 3.3 have focussed on new fundraising, some of which may be applied towards settling or refinancing the current debt stock. The table below shows possible actions on existing debt:

Action	Description
Rollover	This generally involves extending the period of repayment of the principal (sum borrowed) when the loan becomes due.
Reprofile	A limited adjustment of the terms of the debt obligation, usually resulting in: • Period for repaying being extended • Principal staying the same • Coupon staying the same
Restructure	A material adjustment of the terms of the debt obligation, usually resulting in: • Principal may be adjusted up or down • Coupon may be adjusted up or down • Repayment may be extended • Numerous possible outcomes
Refinance	Repayment of an Existing Debt Obligation usually financed by incurring a New Debt Obligation (or borrowing to pay back debt). The New Debt Obligation may be provided by a new or existing creditor.
Repurchase	This involves an Issuer of bonds (or borrower) repurchasing or buying back their own bonds, directly or indirectly, from bondholders

It is hoped that the Zambian Government has considered some of the above interventions in pursuing a restructuring of its existing debt obligations, which may include some of the above options where appropriate. Some of the actions pursued by the government to date include:

- Lazard Freres, a French investment bank that has advised various countries on debt default issues, is the Zambian Government's financial advisor regarding its debt
- Two important themes when resolving debt issues with multiple creditors and contractual obligations are equality of treatment and transparency
- Zambia participated¹⁴ in the G20's Debt Service Suspension Initiative (DSSI), initiated in May 2020, which facilitated the temporal suspension of debt-service payments for 73 eligible countries
- Zambia is one of three countries¹⁵ that has applied for debt relief under the G20's Common Framework, which was created to provide relief beyond the DSSI – it has been fraught with delay¹⁶.
- In a presentation¹⁷ to creditors by Zambia's Minister of Finance and National Planning, Dr. Situmbeko Musokotwane, Zambia expects to reach an agreement with creditors in April 2022

c. Zambia's credibility as a bond issuer or borrower

Credibility is a major consideration in what determines the cost of debt for a borrower or issuer. For Zambia, a concern raised by some holders of its Eurobonds¹⁸ in their rejection of a request for a payment holiday by the Government in 2020 was the lack of a "credible medium-term framework for restoring fiscal sustainability". In this context, an IMF program was viewed as a means of "chaperoning" a government that was not credible in its fiscal management.

The sharp increase in the value of Zambian Eurobonds following the August 2021 elections and gains in the Kwacha in part reflect positive investor expectations from the United Party for National Development (UPND), viewed as more credible from a policy perspective, but also viewed as more likely to join an IMF program. With a strong mandate through the August 2021 elections and positive investor sentiment, the newly elected government may arguably leverage some of this goodwill.

d. Leveraging outcome-based financing with aligned conditions

Outcome based financing, which is increasingly aligned with Sustainable Development Goals, offers potential new financing that may be structured to align with Zambia's

¹⁴According to the World Bank's estimates as of 23 November 2021, Zambia potentially saved over USD500 million on DSSI debt obligations between January and November 2021

¹⁵The others being Ethiopia and Chad. <https://blogs.imf.org/2021/12/02/the-g20-common-framework-for-debt-treatments-must-be-stepped-up/>

¹⁶<https://blogs.imf.org/2021/12/02/the-g20-common-framework-for-debt-treatments-must-be-stepped-up/>

¹⁷<https://www.mof.gov.zm/?p=6448> | ¹⁸<https://www.reuters.com/article/zambia-debt-idUSL1N2HZ0R1>

environmental, social and governance goals. Outcomes may include wealth inequality, climate transition and mitigation, gender equality and women empowerment, health access, education or poverty eradication.

Outcome-based financing may offer opportunities for diversifying Zambia's creditor pool whilst allowing Zambia to be proactive in aligning desired socioeconomic outcomes with the terms and conditions of financing. However, as with any financing initiative, it is pertinent that the relative value proposition be evaluated.

e. Equity and royalty financing considerations

A key consideration for equity or royalty financing is valuation. Currently, the Zambian Government's dividends from equity interests are nominal, with many of the large SOEs in financial distress and thus, only bankable with government guarantees.

In terms of royalties, the most valuable of these are likely to be Mineral Royalty Taxes, though the attractiveness of a royalty-backed instrument must be considered in the context of the future taxes that would be ceded to the investor (and the resultant reduction in fiscal revenue) to ensure that it is not unreasonably onerous, but also offers relative value to other alternatives. A key matter here, is how the lump-sum proceeds are deployed.

f. A brief note on IMF Financing

Zambia has been in discussion with the IMF over an Extended Credit Facility (ECF) for some time¹⁹. This is separate from the USD1.3 billion received in August 2021 as part of the IMF's wider USD650 billion allocation to member countries to provide fiscal support due to Covid-19²⁰.

In his presentation to creditors and stakeholders conducted on 2 November 2021, the Zambian Minister of Finance and National Planning indicated that the Government intends to secure ECF funding by the second half of 2022. The funding that Zambia is able to access under the ECF is discretionary, but even under extraordinary conditions may not exceed 1.3 times annually (about USD2.5 billion) or 4 times in total (about USD7.8 billion) of Zambia's allocation of Special Drawing Rights²¹. The ECF is extended²²:

- On a concessional basis – the interest rate is reviewed every two-years, but is currently nil
- With a long grace period – currently five and a half years with repayment over the following 10 years
- With conditionalities, which are a key consideration of this study

¹⁹<https://www.imf.org/en/News/Articles/2021/05/10/pr21126-zambia-imf-staff-update-on-discussions-with-the-authorities-on-a-new-ecf>

²⁰<https://www.imf.org/en/Topics/special-drawing-right/2021-SDR-Allocation>

²¹Via Special Drawing Rights, a type of reserve allocated to IMF lenders that may be exchanged for hard currency – Zambia currently has 1,406,698,221 cumulative SDRs equivalent to USD1.97 billion as at 2 November 2021

²²<https://www.imf.org/en/About/Factsheets/Sheets/2016/08/02/21/04/Extended-Credit-Facility>

- In the case of Zambia, would require the support of private creditors to ensure, for the IMF, that proceeds are not simply a mechanism for refinancing selected debt obligations

On the basis of cash towards servicing debt, the IMF ECF is amongst the cheapest sources of funding available for Zambia. However, the overall financial and non-financial costs of conditionalities are equally important given the historical context of IMF-lending, and must be considered in Zambia's overall economic and financial modelling in the context of ambitions to achieve debt sustainability whilst reducing poverty and achieving inclusive economic growth.

On 3 December 2021, the IMF announced that it had reached a Staff Level Agreement with the Government on a USD1.4 billion IMF program, over three years. It is still unclear how the funds will be disbursed, or the conditionalities that will be tied to this financing option.



3.5 Conclusion on Financing Options

Any financing option has trade-offs, and the circumstances that led to Zambia's present debt situation and the accompanying loss of credibility with international creditors leave little room for manoeuvre. However, the assessment of options needs to weigh both the need to restore credibility²³ and demonstrate fiscal discipline, against maintaining sufficient policy options to enable inclusive growth and poverty reduction. Table 3 below shows a summary of the options discussed in this paper.

On the back of strong and widespread support for the UPND government in the August 2021 election, there may be a case for parallel consideration of non-IMF financing options premised on the opportunity to demonstrate fiscal discipline and credibility whilst maintaining policy autonomy. Section 4 considers the history and implications of IMF financing.

²³Some Eurobond holders, for example, cited fiscal indiscipline and the lack of transparency around Chinese loans (many of which are bound by confidentiality agreements) as a basis for why Zambia needs IMF as a "chaperon" – <https://www.reuters.com/article/uk-zambia-debt-imf-idUSKBN28I2OB>

Table 3: Overview of Selected Financing Options

Type of Financing	Sub-type	Main Sources									Potential New Options
		Concessional			Commercial						
		Bilateral Lenders	Multilateral Lenders	Plurilateral Lenders	Commercial Lenders	Mainstream Investors	Alternative Investors	Strategic Investors	Other Investors		
Debt	Loans	X	X	X		X		X			• Apply via new cash, refinancing, restructuring or enhancement • Consider mutually-beneficial strategic financing arrangements • Sustainability-linked financing
	Guarantees	X	X					X			
	Bonds			X		X	X	X	X	X	• Municipal bonds • Sustainability (ESG) Bonds (repeated below)
Equity	Private								X		• Full or partial sale of non-core assets to private investors • Curbing inefficiencies at State-Owned Operations
	Public					X	X	X	X	X	• Full or partial sale of valuable non-core assets • Sale through the Lusaka Securities Exchange or internationally
Other	Outcome Based			X					X	X	• Climate Bonds • Debt-for climate swaps • Social Impact Bonds
	Commodity Based								X		
	Revenue Based							X	X		• Copper-cobalt-gold linked bonds or royalties • Monetising other receivables (including royalties)



4. IMPLICATIONS OF AN IMF PROGRAM

4.1. History of the IMF

The idea for the IMF was formulated at the United Nations Monetary and Financial Conference held at Bretton Woods, New Hampshire in the United States in 1944. The entity itself came into existence in December of 1945, making this year its 77th year of existence. The Articles of Agreement agreed to at the Bretton Woods conference stipulate that the IMF's role is to foster "international monetary cooperation through a permanent institution which provides the machinery for consultation and collaboration on international monetary problems"²⁴. Practically speaking, the Articles of Agreement required the establishment of an international body that would ensure the smooth functioning of the international payments system.

The IMF is headquartered in Washington, DC alongside its "sister" organization the World Bank which was also conceived at the same Bretton Woods conference of 1944. Organizationally, the IMF, sometimes referred to as "the Fund", is headed by a Managing Director who is assisted by an Executive Board. Since its inception, managing directors of the IMF have come from Europe whereas presidents of the World Bank have come from the United States – part of a "gentleman's agreement" struck at the Bretton Woods conference²⁵.

Between 1945 and the late 1960s, much of the IMF's functions were limited to the provision of technical expertise especially towards the newly independent states following the decolonization wave of the post-war world. However, from the 1970s, the IMF's role took on a different turn following the collapse of the Bretton Woods System of Monetary Management in 1971. Between 1945 and 1970, and as agreed at the Bretton Woods conference of 1944, the major powers of the world agreed to fix their exchange rates and link them to the price of gold. Revaluing or devaluing one's currency, under this system, required respectively a build-up or draw-down of one's gold reserves. The Bretton Woods System, however, broke down in 1971 when the Richard Nixon administration in the United States announced the unilateral delinking of the value of the US dollar to that of gold²⁶. This then gave way to the current global system of flexible of exchange rates where the value of currencies (currency convertibility) is determined by so-called market fundamentals of supply and demand.

²⁴<https://www.imf.org/external/pubs/ft/aa/index.htm>

²⁵See the Battle of Bretton Woods by Benn Steil for an account of the compromises struck at the Bretton Woods conference

²⁶<https://www.federalreservehistory.org/essays/bretton-woods-created>

The breakdown of the Bretton Woods System of monetary management and the dawn of flexible exchange rates introduced an element of instability in the international payments system. Nowhere was this instability more acute than in small developing countries. With the breakdown of the Bretton Woods system, small countries were now frequently prone to Balance of Payments (BOP) problems, that is the inability to meet international payments requirements owing to a shortage of foreign currency.

With the collapse of the Bretton Woods System, the IMF took on a new role of providing BOP support to countries that found themselves in BOP problems. The provision of BOP support has arguably become the IMF's most important and potent function in the post-Bretton Woods System era.

4.2 Balance of Payments Support

At each time, countries are involved in the export and import of goods and services. In addition, residents of a country might undertake investments abroad while foreign nationals might make investments into the domestic economy. All the inflows and outflows related to these transactions are recorded in accounts known as the Balance of Payments Accounts of a country. As the name suggests, ordinarily outflows should be matched exactly by inflows in such a way that the two balance out. Sometimes, the two components do not balance, often with outflows outstripping inflows. When this happens, it is referred to as a Balance of Payments problem. In ordinary situations, the imbalance may correct itself in such a way that it does not persist. However, the imbalance may persist over several years giving rise to what is known as a BOP crisis – a persistence shortage of foreign exchange. Often, persistent depreciation in the domestic currency vis-à-vis the United States dollar is the smoking gun evidence that a country is in the throes of a BOP crisis.

The IMF has traditionally provided BOP support, that is providing bridging loans to address the BOP crisis. The IMF's bridging loans are not free per se but come with strings attached formally known as conditionalities. That is, countries are required to meet certain conditions before the BOP support or parts of it can be rendered.

4.3 Conditionalities and BOP Support

IMF conditionalities that come with BOP support in essence require austerity. That is, they require that the recipient countries engage in expenditure reductions and/or tax hikes. Traditionally, recipient countries have opted to cut expenditure on social spending and/or to hike income taxes on the lower and middle classes. In terms of social spending, often cuts have been made to health and education budgets.²⁷ In addition, reductions in subsidy expenditures which benefit the poor have been advocated for.²⁸

²⁷http://www.kentikelenis.net/uploads/3/1/8/9/31894609/stubbs2016-the_impact_of_imf_conditionality_on_government_health_expenditure_a_cross-national_analysis_of_16_west_african_nations.pdf

²⁸<https://www.reuters.com/article/us-egypt-economy-imf-idUSKCN1Rl032>

²⁹<https://www.bu.edu/gdp/2021/04/05/imf-austerity-is-alive-and-impacting-poverty-and-inequality/>

³⁰<https://www.oxfam.org/en/press-releases/imf-paves-way-new-era-austerity-post-covid-19> and <https://www.project-syndicate.org/commentary/doing-business-scandal-highlights-deep-imf-problems-by-jayati-ghosh-2021-10>

There has been talk that the IMF no longer requires conditionalities that require fiscal austerity. However, a series of recent studies show that IMF austerity is alive and well²⁹ and even more so in the current era of the COVID pandemic.³⁰

4.4 Lessons from Zambia's history with the Bretton Woods institutions

In 1992, the Zambian government then lead by the Movement for Multiparty Democracy (MMD) pushed neoliberal policies supported by the IMF and World Bank's Structural Adjustment Programmes (SAPs), to foster a private sector led economy. During its first decade in power, the MMD government consistently and rather aggressively adopted these policies under the SAPs.

The state's role was to maintain the creation of an enabling environment for private business and also act as regulator. Trade, exchange rates and interest rates were liberalised, subsidies removed, agricultural marketing liberalised. Within the first year of implementation more than 126 state-owned enterprises and parastatals had been privatised. The state also implemented measures to reduce the civil service to a so-called efficient and manageable size, through retrenchment and voluntary separation. In short, the "forces" of the market were to determine prices for goods and services with minimal to zero state intervention.

By the year 2000, the results of the adjustment process were in and Zambia was now among one of the poorest nations in the world. The World Bank classified Zambia as a Least Developed Country and the United Nations Development Programme Human Development Report 1999 ranked Zambia 156 out of 174 countries, having fallen consistently over the past years, from 136 in 1996, to 142 in 1997, to 146 in 1998. The social indicators revealed declining trends over time and worsening living conditions for most Zambians. Life expectancy dropped to an estimated 37 years, compared to 42 years at the time of independence (1964) and 54 years at the end of the 1980s. Mortality rates were among the highest in the world with an increase in the number of orphans. National household surveys revealed that the percentage of people living in poverty increased from 70 percent of the population in 1991 to about 74 percent in 1993, decreased to 69 percent in 1996 and then rose again to 73 percent in 1998. These estimates only showed the proportions of the population that were income poor, without considering the other dimensions of poverty.

In December 2000, Zambia qualified to the Highly Indebted Poor Countries (HIPC) Initiative, which gave the country some breathing room in terms of debt service. The inequality and poverty generated by the SAPs, however, persisted through the first decade of the new millennium.

It should be noted that this experience is not unique to Zambia. As lender of last resort, the IMF provides countries in economic turmoil with financial support and in return borrowing countries are required to commit to policy reforms or conditionalities. These conditionalities have mostly resulted in adverse social implications.³¹

³¹Timon Forster, Bernard Reinsberg, Thomas Stubbs. The Conversation. July 17, 2019. <https://theconversation.com/imf-says-it-cares-about-inequality-but-will-it-change-its-ways-120105>

4.5 The IMF and Zambia in the present moment

The IMF and Zambia have had a long relationship with IMF BOP support rising to prominence during the economic crisis of the late 1980s and 1990s. There is ample evidence that IMF support to Zambia, particularly in the 1980s and 1990s, has been disastrous for the country's growth and development aspirations.³²

In the current moment and given the unsustainable external debt situation and attendant BOP crisis, the new government of the UPND indicated from the moment they were elected that they would seek BOP support from the IMF. Confirmation of this came in the 2022 National Budget presented on 29th October 2021 to parliament³³. In that presentation, the Minister of Finance confirmed that the Zambian government would be seeking considerable amounts of external financing from co-operating partners over the medium term. Subsequent to the budget presentation, the Ministry of Finance issued a press statement confirming that talks were underway with the IMF and the goal was to conclude negotiations on an agreement by the end of November 2021.

On Friday, December 3rd 2021 official confirmation came from the IMF that a Staff Level Agreement had been reached with the Zambian government for an ECF over three Years.³⁴

4.6 The IMF Agreement with Zambia

The specifics of the agreement entered between the IMF and the Zambian government are not yet known nor has there been transparency around the process. The various press statements issued by both the IMF and the Zambian government in the wake of the agreement have both signalled the fact that "bold structural reforms" will have to be implemented as a key condition of accessing the ECF. Different pieces of evidence taken together signal that the agreement, like those of the past and like those with different countries, have austerity as the bedrock.

Projections contained in the IMF's flagship World Economic Outlook (WEO) for Zambia show trends that suggest that austerity is to be expected over the medium term.³⁵ Figure 3 below taken from the IMF's WEO shows how steep and rapid austerity will be over the next five years. The IMF expects that the fiscal deficit will move from about 13 percent of GDP in 2020 to 1 percent of GDP in 2026. Further, Figure 4 shows trends in government expenditure over the next five years. The figure shows that government expenditure will decline from 31 percent of GDP in 2020 to 21 percent of GDP in 2026. Both graphs suggest that we are going to see a contraction of government expenditure over the medium term totalling about USD4 billion. An incredible amount of austerity to impose on a country whose population is generally poor.

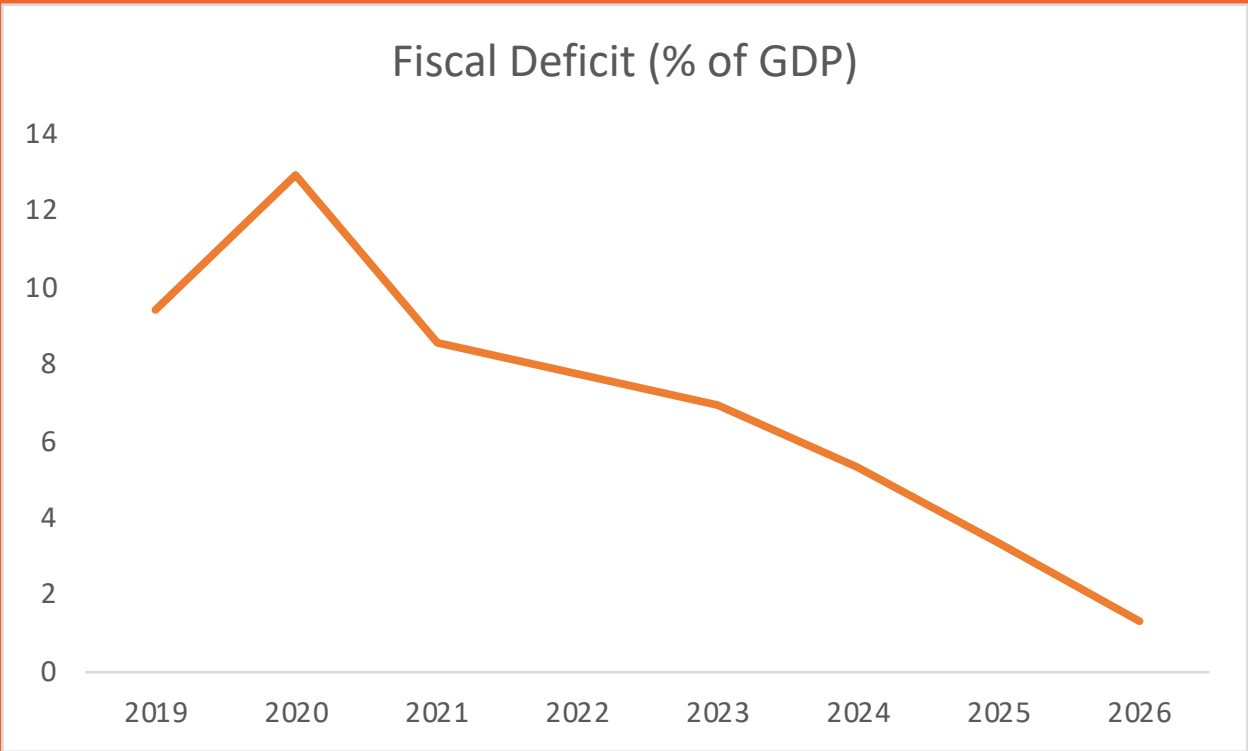
³²<https://www.sciencedirect.com/science/article/abs/pii/S0305750X91901377> and <https://library.fes.de/libalt/journals/swets-fulltext/11220673.pdf>

³³https://www.parliament.gov.zm/sites/default/files/images/publication_docs/BUDGET%20SPEECH%20_%202022.pdf

³⁴<https://www.imf.org/en/News/Articles/2021/12/03/pr21356-IMF-Staff-Reaches-Staff-Level-Agreement-on-Extended-Credit-Facility-Arrangement-with-Zambia?cid=em-COM-123-43976>

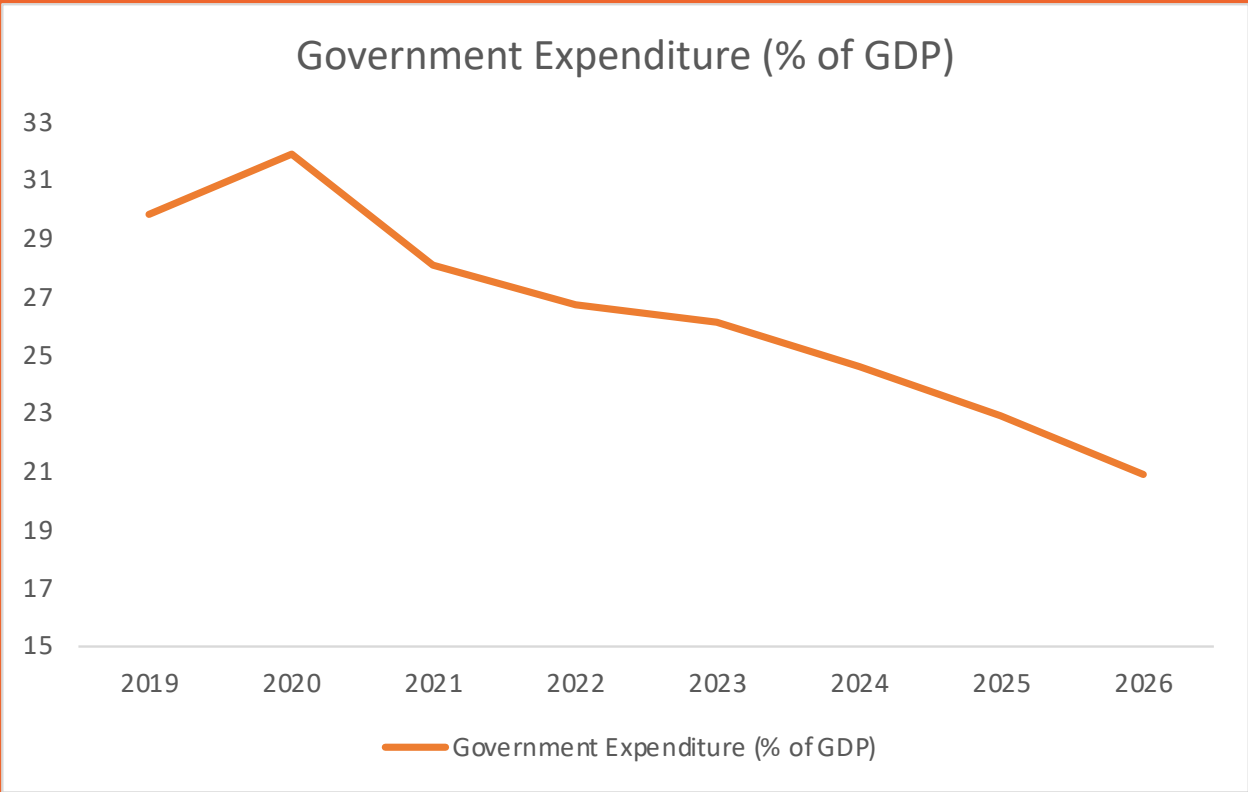
³⁵<https://twitter.com/danielmunevar/status/1467126280789594116>

Figure 3: Trends in Fiscal Deficit Zambia, 2019 to 2026



Source: IMF World Economic Outlook, October 2021

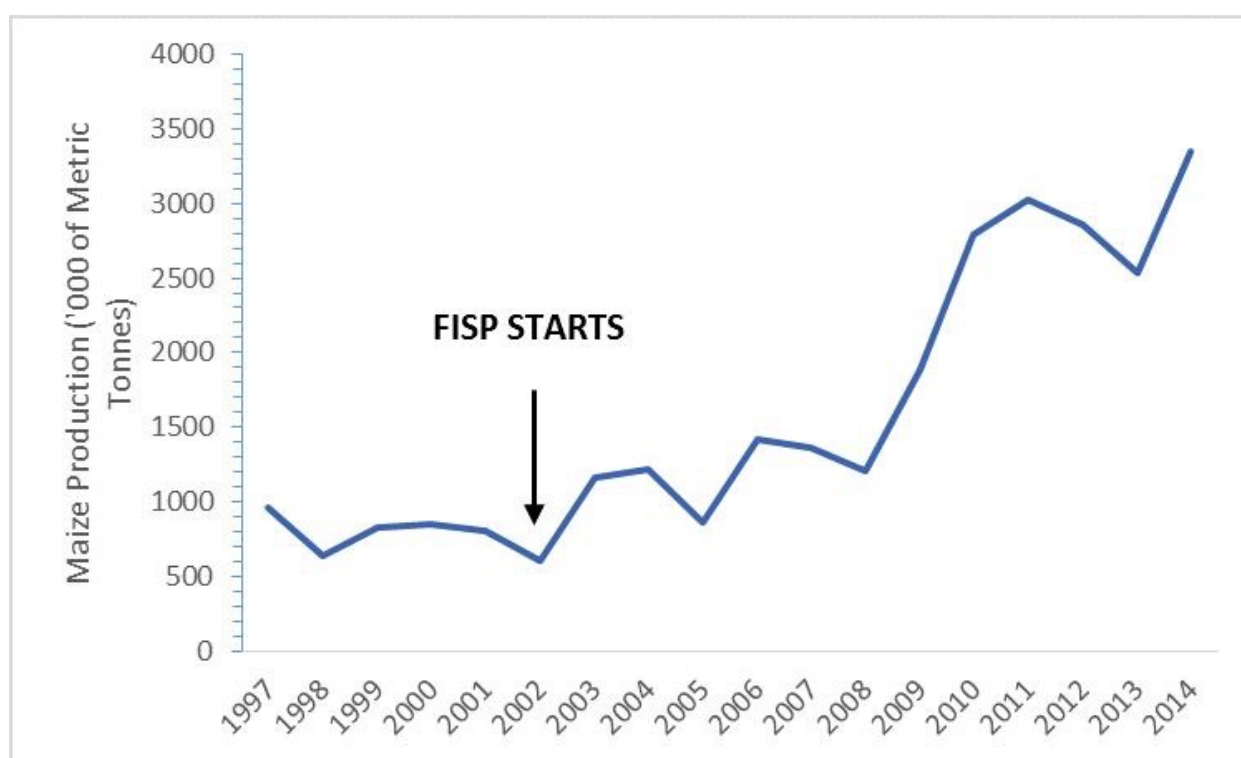
Figure 4: Trends in Government Expenditure (% of GDP)



Source: World Economic Outlook, October 2021

Where will these cuts come from? As alluded to earlier, several government officials have confirmed that subsidies to electricity and fuel will have to go. Given the primary importance of energy as an input into the economy's production process, it is very clear that the wide-ranging economic impacts of this policy shift will be seismic. A scholarly paper published in *Energy Policy* in 2019 found that the removal of subsidies had a significant impact on the welfare of the poor in Zambia. Further, the government has made it clear that the widely successful Farmer Input Support Programme (FISP) will have to be "reformed" into a Comprehensive Agriculture Support Programme that also includes support to commercial farmers. As is well known, FISP which targets about 1 million peasant farmers as primary beneficiaries has been successful in converting Zambia from a net-importer of maize in the early 2000s to a position now where it is a net-exporter of maize (see figure 5). FISP was introduced in the 2002/03 farming season. Between 2002/03 and 2013/14 farming season, maize output grew by about 500 percent! The government, as a likely condition of the IMF Agreement, wants to reform FISP by reducing support to peasant farmers and rather granting support to already established and resource-rich commercial farmers.

Figure 5: Farmer Input Support Programme (FISP) and Trends in Maize Production



Source: Zambia Statistical Agency

The government and the IMF have continued to make the argument that savings from subsidy removals will instead be channelled towards more expenditure on education, health and social cash transfer programmes. For example, the IMF and the government have repeatedly argued that the key elements of their agreement are the following:

i. re-establishing fiscal sustainability while channelling public resources towards investment in people, particularly the youth;

- ii. removing expenditure towards inefficient public investment and poorly targeted subsidies;***
- iii. channelling resources towards greater investment in health and education and the delivery of more social benefits.***

However, how will the Zambian government meet such an ambitious expenditure programme when all the evidence gathered so far suggests drastic cuts in government expenditure? In other words, how will the points in (i) to (iii) be satisfied given that government expenditure is expected to contract by about USD4 billion dollars over the next five years?

Already, there are early signs suggesting that promises of increases in allocation to social sectors are largely a chimera. The Minister of Finance in his budget address announced a policy of free education from primary to secondary school. However, it appears that this policy announcement does not guarantee universal free education but contains "hidden fees" for parents. Several news outlets are reporting that parents with children attending boarding schools will be required to pay non-negligible sums of money during this year's school calendar.

Further, the so-called social cash transfer programme leaves a lot to be desired. Beneficiaries receive paltry amounts of ZMW180, bi-monthly (approximately USD11). This type of assistance can hardly be called transformative and is certainly a sore on our conscious given the largesse the country is dishing to the corporate and mining sectors (see below).³⁷

Further, the IMF and government are hoping to enhance government revenues by "developing a medium-term agenda to enhance revenue mobilization through policy changes and administrative changes". However, how is this to be effectively achieved given that the government has reduced corporate income taxes and made Mineral Royalty Tax (MRT) tax deductible in addition to providing very generous tax concessions to the mining industry? In sum, the Staff agreement between the Zambian government and the IMF does not make sound economics let alone balance arithmetically.

4.7 Impact of IMF facility on inequality

As is clear from the discussion in the previous section, it is without doubt that the latest agreement between the Zambian government and IMF will result in widescale increases in poverty and inequality. The drastic reductions in government expenditure over the next five years, which we estimate at USD4 billion, will impact the poor and marginalized more than any other group. The subsidies that are targeted for removal (energy and agriculture) have the poor and marginalized as the biggest beneficiaries. As we have argued above, the claim made by government and the IMF that savings from subsidy removal will be spent on the poor does not survive careful scrutiny. Pro-poor expenditure is projected to be small and unimaginative. In certain instances, as is the case with the education sector, promises of free service delivery appear to be laden with hidden fees. Conversely, reducing taxes on the

³⁷Rather social policy should be transformational. See the literature on transformational social policy.

corporate and mining sectors will serve to enhance the earnings accruing to the small cadre of Zambians engaged in these sectors at the expense of millions in the country.

More formally, many studies have investigated the likely impacts on inequality of IMF programmes. Unsurprisingly, these find that such programmes only serve to enhance inequality. For example, a study of a panel of 135 countries for the period 1980 to 2014, examined income inequality using multivariate regression analysis correcting for non-random selection into both IMF programs and associated policy reforms. The study found that overall, policy reforms mandated by the IMF increased income inequality in borrowing countries. An analysis of specific pathways linking IMF programs to inequality by disaggregating conditionality by issue area revealed adverse distributional consequences for four policy areas: fiscal policy reforms that restrain government expenditure, external sector reforms stipulating trade and capital account liberalization, financial sector reforms entailing inflation-control measures, and reforms that restrict external debt. In most instances these effects occurred one year after the incidence of an IMF program, and persisted in the medium term. The findings suggest that the IMF's attention to inequality neglects the multiple ways through which the organization's own policy advice has contributed to inequality in the developing world.³⁸

Research by the University of Glasgow³⁹ revealed that policy reforms prescribed in IMF lending programmes affected income inequality for developing countries between 1980 and 2014 by an average 6.5 percent a year once the programme commenced. For example, a lending programme with Togo mandated such reforms between 2008 and 2011. During this period, income inequality rose by 3.7 percent.

Guatemala and Papua New Guinea recorded an increase in GINI coefficients up to 0.8 percent higher than prior to the IMF program implementation. Indonesia which is Southeast Asia's largest economy consented to IMF reforms that limited its external debt and recorded an increase in inequality of 1.6 percent within 6 years of implementation.

In addition, the IMF has generally repeatedly mandated the removal of restrictions to trade and financial flows and although promoting international economic openness can increase demand for skilled labour in developing countries, income inequality increase as low-skilled labour is excluded from these opportunities. Financial development and capital account liberalisation also favours individuals with access to financial capital and services further widening the gap between rich and poor. In Sri Lanka for example, the GINI coefficient⁴⁰ increased by almost 5.6 percent under an IMF program implemented between 2000 and 2006.

Existing evidence therefore indicates that it is, without doubt that the Zambian government's latest engagement of the IMF will result in widescale increases in poverty and inequality.

³⁸Timon Forster et al. How structural adjustment programs affect inequality: A disaggregated analysis of IMF conditionality 1980 -2014. Science Direct Journal. Volume 8, May 2019. Pages 83 -113

³⁹Timon Forster, Bernard Reinsberg, Thomas Stubbs. The Conversation. July 17, 2019. <https://theconversation.com/imf-says-it-cares-about-inequality-but-will-it-change-its-ways-120105>

⁴⁰The GINI coefficient is statistical measure of the degree of variation used in analysing income inequality.



5. RECOMMENDATIONS

As is clear from the analysis provided in this report, the next couple of years in Zambia will be very difficult for the majority of the country's population. The burden of these neoliberal economic policies will fall on the poor and disposed. The benefits will accrue to a small elite that is well positioned with capital and connections to lobby for favourable economic policies. The puzzling reductions in corporate income tax and favourable tax treatment provided to the mining houses in light of the need to “tighten our belts” is a prelude of things to come. All things considered, this will result in an increase in poverty and inequality in the country.

The following are the recommendations emanating from the analysis in this report:

- The Fight Inequality Alliance Zambia should develop an advocacy strategy that will seek to counter the avalanche of neoliberal economic policymaking that will dominate the Zambian policy space over the next five years. Such an advocacy strategy should look towards growing a broad-based movement and coalition of different progressive constituencies in Zambia. Such a movement and coalition should cut-across gender and be led by the working class and other progressive elements in Zambia. The next five years will be a battle of ideologies and ideas and FIA Zambia should be at the ready to respond and engage. With luck, this movement will succeed, and the country may overturn some if not most of the anti-poor and inequality enhancing policies that have already been implemented thus far. In addition, it may offer an opportunity to influence the final conditionalities of the IMF program should there still be room to do so.
- As the analysis in this report demonstrably proves, there were many alternative options to getting on an IMF programme. For example, our analysis reveals that the best pathway forward would have been a non-IMF financing option implemented with increased fiscal discipline in order to achieve the desired credibility. Unfortunately, the Zambian government was not interested in engaging with diverse voices at the very early stage in the process. A strong recommendation emanating from this is that going forward, a mechanism for broad-based consultations be put in place in such a way that decisions arrived at by the Zambian government are based on widescale consultations and are based on broad public support. It is very disappointing to see that the process of negotiating towards an IMF programme was restricted to officials at the Ministry of Finance, the Central Bank and the IMF itself. This is unacceptable as the implications of the agreement will have

wide-ranging impacts beyond these narrow set of technocrats. The policy consultation space should have been left wide open. For example, the new government should have called for an Economic Indaba very early on to debate alternatives before committing to a single policy position.

- A close analysis of the policy process that led to the IMF agreement shows that it lacked transparency. Even though the Staff Level Agreement was announced with much fanfare on 3rd December 2021, we are yet to know the exact wording of the agreements between the government and the IMF at the timing of writing this report. The negotiations took place behind a veil of secrecy involving only a small clique of technocrats. Further, it appears that parliament, the ultimate representative of the people's aspirations, had very little oversight of the entire process. The new government promised transparency and sadly such transparency was missing from this process. It would be in their best interests and in the interests of the people going forward to devise economic policy, especially one as seismic as this, in the open.
- Finally, the report calls for a reversal of the generous incentives given to the corporate sector especially the mining industry. The Minister of Finance in his budget speech announced the reduction of the corporate income tax (CIT) from 35 percent to 30 percent. Further, he announced that the Mineral Royalty Tax (MRT) had been made tax deductible, meaning that mining houses can now expense MRT from their revenues when calculating profit. Both policy shifts are going to cost the Zambian fiscus hundreds of millions of dollars at a time when the IMF and the Zambian government are calling for anti-poor austerity policies. It is common knowledge that Zambia's corporate sector has been a major culprit in tax dodging schemes, a scenario explaining the low effective CIT rate in the country. The mining sector has not performed any better in this regard. Many credible reports have documented largescale tax avoidance and evasion on the part of the mines that has likely cost the treasury billions of dollars over the years. Reducing inequality and poverty will require the marshalling of all of the country's resources especially revenue from our God-given mineral resource.

APPENDICES

Appendix 1 – Further Notes on 3.1. Overview of Sovereign Financing Options

c. *Committing to repaying the cash over time on agreed terms (Type A Options)*

Type A Options are typically debt or quasi-debt structures, which are typically viewed as less-risky than equity (see below) and other forms of financing that are less predictable cashflow in the future:

- recipients of debt financing (“borrowers” for loans, “issuers” for bonds) are obligated to meet their repayment obligations as and when they fall due
- creditor claims are typically a *priority*⁴¹ over those of other capital providers
- the repayments are relatively *predictable*⁴² for the provider of cash

d. *Giving up the receipt of cash over time on agreed terms (Type B Options)*

Under Type B Options, the cash received today is typically calculated as the sum of the future cash that the provider of cash expects to receive, adjusted for time, inflation and risk via a discount rate⁴³ or some other adjustment (the “present value”).

Equity and royalty financing structures involve the cession or sale of a series of future cashflows (whether a dividend, rental, management fee, royalty etc) or asset (which may be productive land, physical commodities etc) in exchange for cash today:

- equity financing may be achieved through the sale of a “share” of an asset, where the seller receives the cash, or through the dilution of a share of an asset (via a “subscription”), where the funds go towards the asset or its collective owners.
- shareholders typically expect some future cash (or a “return”) from their investment in the form of a dividend or in the increase in the value of their shareholding – dividends are typically only paid after meeting debt obligations and from profits⁴⁴.
- unlike equity or debt, royalties are typically payable from or as a percentage of gross income or revenue (not profits, like equity, or after expenses, like debt) and so are paid ahead of other obligations.

like equity, royalties are typically activity-dependent, therefore may be unpredictable based on the changes in the gross income attributable to the royalty.

⁴¹<https://corporatefinanceinstitute.com/resources/knowledge/finance/senior-and-subordinated-debt/>

⁴²In the case of bonds, where investors “subscribe” or purchase financial instruments that trade on a stock exchange, the price and implied interest rate of the bonds may fluctuate, even if the coupon rate being paid by the issuer fluctuates

⁴³A discount rate may be thought of as a means of describing a figure in the future (or “future value”) in today’s terms (or “present value”). It is the opposite of a growth rate (such as an interest or inflation rate), which is used to describe a figure today (present value) in future terms (future value).

⁴⁵When the assets combined income exceeds its combined expenses

Appendix 2 – Further Notes on 3.2. Overview of Debt Financing Options

Debt may be classified in various ways, including by the terms of repayment, creditor type and the mode of provision or security amongst others⁴⁵:

i. By the terms of repayment

- Concessional debt is contracted on terms considered to be more favourable (or generally cheaper) than would ordinarily be the case in the general market, and usually with broader strategic objectives or conditions that justify the below-market rates (e.g the IMF Extended Credit Facility, infrastructure loans from Chinese lenders, loans from development banks).
- Commercial debt contracted on terms considered to be commensurate to the risk profile of the borrower given prevailing market conditions (e.g Eurobonds, loans from commercial banks). For borrowers or issuers that are deemed risky or have a history of default, this results in a higher cost of debt, all things equal.

ii. By lender or creditor type

- Official lenders are state related and can be bilateral, plurilateral, multilateral or commercial.
- Bilateral lenders are individual or state-sponsored financial institutions (SSIs) with individual strategic objectives (e.g China, or the China EXIM bank). Plurilateral lenders are closed groups of individual or SSIs, usually with aligned strategic objectives (e.g Scandinavian countries). Multilateral lenders comprise and represent the interests of multiple states, usually with a specific mandate (e.g the IMF and World Bank).
- Commercial or private lenders are non-official lenders that provide debt on an arms-length basis either directly, through projects or via the international capital market (e.g commercial banks, Eurobond holders). Amongst these, debt may be provided through a loan or via the subscription or purchase of financial instruments (see "By the mode of provision" below).

iii. By the mode of provision

- Loans generally involve a contractual agreement between two or more parties with one party lending to the other (the "borrower").

⁴⁵This list is not exhaustive and a single loan or bond may comprise various combinations of these factors

- Bonds generally involve the issue of financial instruments by the recipient of funds that are usually tradeable or transferrable (the “issuer”), to investors who purchase or “subscribe” for the bonds, notes or other financial instruments and may freely trade them thereafter.

iv. By the protections provided

- Secured debt gives the creditor a full or partial claim against an identified asset, which may be tangible (such as property, a port etc) or intangible (such as a guarantee, shares, funds receivable from third parties, revenue etc). Secured creditors may be ranked which determines the order in which the creditors are paid in the event of default (with senior debt ranked higher, and subordinated debt lower). In addition, the debt may be “non-recourse”, limiting the creditor’s claim to the security provided, or “recourse”, allowing the creditor to pursue other assets in excess of the value of the security if there is a shortfall.
- Unsecured debt does not give the creditor a claim against identified assets, as set out above. However, unsecured creditors are typically paid ahead of claims by share or equity-holders in the event of default. For unsecured debt, creditors lend on the basis of the creditworthiness of the borrower or issuer, which may result in a higher compensation for risk through a higher coupon rate, or adjustment. Commercial unsecured debt will, all things equal, be the most expensive cost of debt for a sovereign issuer.
- Guarantees are a form of credit-enhancement that involve a credible third-party providing assurance to creditors of meeting all or part of the obligations of the borrower or issuer in the event of default. This usually results in more attractive terms for the borrower if the provider of the guarantee (or the “guarantor”) is credible and is less-risky, thereby resulting in better credit terms for the borrower.

v. By the absence or presence of conditions

- Debt with Conditionality involves the recipient of cash along with committing to performing some condition or meeting some defined outcome⁴⁶. Conditionality is typically attributable to financing from official lenders such as the IMF or the provision of aid but may also apply to “outcome based” financing such as Social Impact or Green Bonds. In addition, there may be restrictions on how the proceeds for debt are applied and the requirement of reporting or independent evaluation of whether conditions have been met.
- Debt without Conditionality generally has little or no strings attached. This may not negate the need for the recipient of funds to clarify how the funds are to be utilised, or how the debt is to be settled. For example, Zambia’s first Eurobond specified the use of proceeds, which were targeted infrastructure, whilst subsequent issuances were comparatively generic.

⁴⁶That is, has “strings attached”

vi. *By whether they have traditional or hybrid features*

- Plain vanilla describes the simplest form of an asset or financial instrument. For debt, as described in the Overview of Sovereign Financing Options section above, this is typically in the form of a coupon rate payable at a fixed percentage⁴⁷ of the principal amount, and the principal repaid in a defined manner. The payment obligations from plain vanilla debt are relatively easy to predict for the borrower or issuer.
- Exotic debt has additional features, including some discussed above, that may change the interest or principal payable based on the fulfilment (or lack thereof) of an outcome, a change in the price of another asset (such as the price of a commodity⁴⁸), economic variable (such as inflation⁴⁹) or give the creditor some other right or benefit such as the option to convert some or all of the debt into ownership of a specified asset (such as shares in a company⁵⁰). This adds a measure of complexity to the debt and is typically targeted for strategic or sophisticated institutional investors or lenders.

⁴⁷This may also be 0 percent, for "zero-coupon" debt, but typically involves a compensatory payment at the end of the term

⁴⁸Commodity-linked bonds | ⁴⁹Inflation-linked bonds | ⁵⁰Convertible bonds

⁵¹Many of the companies listed on the Lusaka Securities Exchange were sold by the Zambian government, with preferential allocation to locals, under the Zambia Privatisation Trust Fund

Appendix 3 – Further Notes on 3.3. Overview of Other Financing Options

This section focuses on the Type B Options, with a focus on equity and royalty financing, though may loosely be applied to exotic debt:

c. *Equity*

- Equity is effectively an ownership interest in an asset such as property, infrastructure or a company. This ownership claim is typically “residual”, with equity-holders (or “shareholders”) benefiting from the asset when it operates sustainably and generates cash for its owners.
- In the context of a government shareholder, there may be additional considerations or objectives for shareholding, such as job creation, economic competitiveness or strategic positioning, that may supersede a profit objective. Where this is the case, it is pertinent that the government be clear on its priorities and consider sustainability, prioritization and net impact.
- Regarding company equity, shares may be publicly held (and would then be tradeable on a securities exchange) or be privately held. An Initial Public Offer is one way through which equity may be sold to the public⁵¹.
- Equity financing is generally achievable by selling all or a part of an ownership claim in an asset, which in turn should be of value to the buyer. Usually “value” is determined by the present value of future cashflow⁵² receivable by the equity-holder, though unlike for debt, these cashflows may be less certain.
- The proceeds from the sale of Government interests in previous SOEs via privatisation in the early 1990's and 2000's represents a form of equity financing. Privatisation has both benefits and drawbacks, but altogether needs to be managed effectively and need not always result in complete government withdrawal, suboptimal value for the country nor lack transparency. It is also cardinal to evaluate the overall nature of the asset and clarify whether it better suited for commercial alignment for profit⁵³ versus alignment on a not-for profit or strategic basis⁵⁴.

d. *Royalties*

- Royalty financing is typically linked to some globally tradeable commodity (usually a mineral such as copper or gold) but may relate to any claim proportionate to the gross cash receivable.

⁵²This includes dividends, preference share interest or the proceeds from the sale of the asset in the future

⁵³Prioritizing efficiency with a view to profitability, which profits would benefit the government and the public, and in the absence of sustainable operations should be wound down

⁵⁴Prioritize strategy and may be operated with a view to some aspiration or quantifiable benefit, which notwithstanding, should be sustainably financed by the government

- There are specialised royalty investors and in the context of the Government in relation to tax receivables, this may include the taxable parties themselves. For example, the Government may agree to cede a portion of future mineral royalties in exchange for upfront cash targeting specialised royalty investors or may be sell them to mining companies as an effective partial prepayment of mineral royalty tax.
- A related arrangement to royalties called “streaming” is effectively an agreement to pre-sell a physical commodity (such as copper or cobalt) from an owned asset (usually a mine), based on assumed production levels and commodity price projections.

Appendix 4 – Further Notes on Key Considerations for Zambia

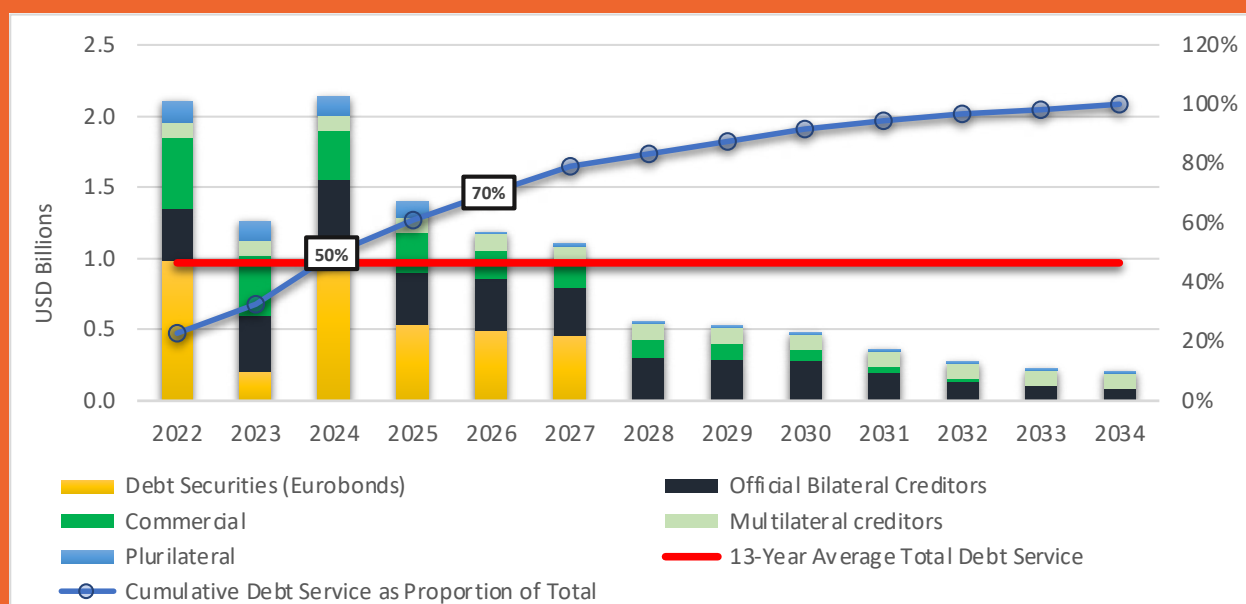
g. Zambia's debt obligations are not sustainable, in the short-term

Common citations of Zambia's "debt-sustainability" or of the country being at "high risk of debt distress", refer to the assessment of how much debt that Zambia can sustainably incur as a portion of GDP according to the LIC-DSA, as highlighted in section 2 above. It is pertinent, as part of any consideration of options to resolve Zambia's debt crisis, that the parameters of the country's debt sustainability reflect both Zambia's current and near-term status and acknowledge any levers or scenarios that may impact Zambia's standing under the LIC-DSA framework. We summarise the key liquidity and solvency requirements⁵⁵ under the DSA in the table below:

Figure 1 on page 35 shows Zambia's debt profile and the Authors' estimates of Zambia's cumulative debt obligations over 13 years, whilst figure 2 shows the Authors' estimates of Zambia's debt service obligation limits based on the IMF DSA limits for weak and medium capacity countries. Notably, based on the underlying information:

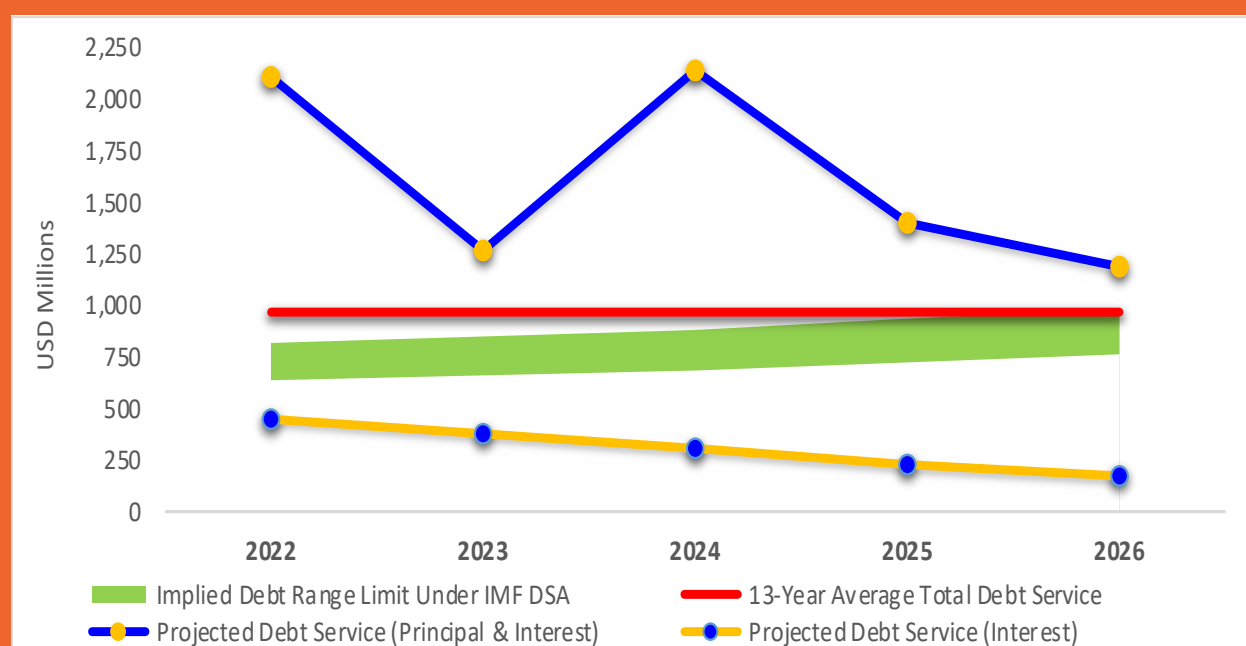
- Approximately 70 percent of Zambia's debt service obligations (DSOs) over the next 13 years are payable within five years, between 2022 and 2026
- Most of this debt is attributable to repayment of the principal on maturing Eurobonds in 2022, and between 2024 and 2027, accounting for approximately 40 percent of projected total debt service obligations over the next five years
- The 13-year average debt service is just under USD1 billion, whereas payments in 2022 and 2024 exceed USD2 billion
- Beyond five years, total debt service taper off and reduce from just over USD500 million to under USD250 million by 2034, suggesting that a debt reprofiling may be achievable depending on long-term Government revenue
- Based on Government fiscal revenue projections over the next five years, Zambia's projected interest obligations are within the solvency limit for Weak Capacity LICs over the period and below the 13-year average total debt service
- Further to the above, the total DSOs are much higher than the limit for Medium Capacity LICs and above the 13-year average total debt service
- The estimates below assume no new debt is contracted and that DSOs are met per contractual obligation, which in part has been superseded by Zambia's default and initiatives such as the DSSI.

Figure 1: Zambia's Debt Profile – 2022 to 2034



Source: Ministry of Finance and National Planning, Author's estimates

Figure 2: Zambia's Debt Service Limit based on Projected Government Revenue – 2022 to 2026



Source: Ministry of Finance and National Planning, IMF October 2022 WEO

h. Possible actions regarding existing debt stock

Sections 3.1 to 3.3 have focussed on new fundraising, some of which may be applied towards settling or refinancing the current debt stock. The table below shows possible actions that may mitigate or facilitate progression of a defaulting borrower or debt issuer:

Action	Description
Rollover	This generally involves extending the period of repayment of the principal (sum borrowed) when the loan becomes due.
Reprofile	A limited adjustment of the terms of the debt obligation, usually resulting in:-Repayment period being extended-Principal staying the same-Coupon staying the same
Restructure	A material adjustment of the terms of the debt obligation, usually resulting in:-Principal may be adjusted up or down-Coupon may be adjusted up or down-Repayment may be extended-Numerous possible outcomes
Refinance	Repayment of an Existing Debt Obligation usually financed by incurring a New Debt Obligation (or borrowing to pay back debt). The New Debt Obligation may be provided by a new or existing creditor.
Repurchase	This involves an Issuer of bonds (or borrower) repurchasing or buying back their own bonds, directly or indirectly, from bondholders.

The Zambian Government has likely considered many of the above interventions and is expected to pursue a restructuring of its existing debt obligations, which may include some of the above options where appropriate:

- Lazard Freres, a French investment bank that has advised various countries on debt default issues, is the Zambian Government's financial advisor regarding its debt
- Two important themes when resolving debt issues with multiple creditors and contractual obligations are equality of treatment and transparency
- Zambia participated⁵⁶ in the G20's Debt Service Suspension Initiative (DSSI), initiated in May 2020 and extended to December 2021, which facilitated the temporal suspension of debt-service payments for 73 eligible countries
- Zambia is one of three countries⁵⁷ that has applied for debt relief under the G20's Common Framework, which was created to provide relief beyond the DSSI and importantly, note the increasing role of China as a dominant bilateral lender – the Common Framework has been fraught with delay⁵⁸
- In a presentation⁵⁹ to creditors by Zambia's Minister of Finance and National Planning, Dr. Situmbeko Musokotwane, Zambia expects to reach an agreement with creditors in April 2022

⁵⁶According to the World Bank's estimates as of 23 November 2021, Zambia potentially saved over USD500 million on DSSI debt obligations between January and November 2021

⁵⁷The others being Ethiopia and Chad. <https://blogs.imf.org/2021/12/02/the-g20-common-framework-for-debt-treatments-must-be-stepped-up/>

⁵⁸<https://blogs.imf.org/2021/12/02/the-g20-common-framework-for-debt-treatments-must-be-stepped-up/>

i. Zambia's credibility as a bond issuer or borrower

Credibility is a core consideration in what determines the cost of debt for a borrower. For Zambia, a concern raised by some holders of its Eurobonds⁶⁰ in their rejection of a request for a payment holiday by the Government in 2020 was the lack of a “credible medium-term framework for restoring fiscal sustainability”. In this context, an IMF program was viewed as a means of “chaperoning” a government that otherwise lacked credibility in its fiscal management.

The sharp increase in the value of Zambian Eurobonds following the August 2021 elections and gains in the Kwacha in part reflect positive investor expectations from the United Party for National Development (UPND), viewed as more credible from a policy perspective, but also viewed as more likely to join an IMF program. With a strong social mandate through the August 2021 elections and positive investor sentiment, the newly elected government may arguably leverage some of this goodwill to its benefit when engaging with both new and existing creditors.

j. Leveraging outcome-based financing with aligned conditions

Outcome based financing, which is increasingly aligned with Sustainable Development Goals, offers potential new financing that may be structured to align with Zambia's environmental, social and governance goals. Outcomes may include wealth inequality, climate transition and mitigation, gender equality and women empowerment, health access, education or poverty eradication. Sustainability bonds, for example, allow issuers to access financing for investment targeting a combination of social and climate outcomes. It may also support infrastructure development and economic activity that otherwise may not be possible or be relatively more expensive.

Notably, outcome-based financing may offer opportunities for diversifying Zambia's creditor pool whilst allowing Zambia to be proactive in aligning desired socioeconomic outcomes with the terms and conditions of the financing. However, as with any financing initiative, it is pertinent that the relative value proposition be evaluated.

k. Equity and royalty financing considerations

A key consideration for equity or royalty financing is valuation. Currently, the Zambian Government's dividends from equity interests are inconsequential, with many of the large SOEs in financial distress and thus, only bankable with government guarantees. An equity financing strategy would need to consider government's pool of assets and determine:

- Which should be commercially or socially inclined
- For those that are commercially inclined, which are sustainable or strategically critical for the country, and which are not

⁵⁹<https://www.mof.gov.zm/?p=6448>

⁶⁰<https://www.reuters.com/article/zambia-debt-idUSL1N2HZoR1>

- Whether the Government would be able to unlock value; by a partial or full sale, a turnaround process, or mutually beneficial investment partnerships that limit the extent of Government's financial support, doing so in a transparent manner.

In terms of royalties, the most valuable of these are likely to be Mineral Royalty Taxes, though the attractiveness of a royalty-backed instrument must be considered in the context of the future taxes that would be ceded to the investor (and the resultant reduction in fiscal revenue) to ensure that it is not unreasonably onerous, but also offers relative value to other alternatives.

L. A brief note on IMF Financing

Zambia has been in discussion with the IMF over an Extended Credit Facility (ECF) for some time⁶¹. This is separate from the USD1.3 billion received in August 2021 as part of the IMF's wider USD650 billion allocation to member countries to provide fiscal support due to Covid-19⁶², which is notably free from conditionality. In his presentation to creditors and stakeholders conducted on 2 November 2021, the Zambian Minister of Finance and National Planning indicated that the Government intends to secure ECF funding by the second half of 2022.

The funding that Zambia is able to access under the ECF is discretionary, but even under extraordinary conditions may not exceed 1.3 times annually (about USD2.5 billion) or 4 times in total (about USD7.8 billion) of Zambia's allocation of Special Drawing Rights⁶³. The ECF is extended⁶⁴:

- On a concessional basis – the interest rate is reviewed biannually, but is currently nil
- On an extended grace period – currently five and a half years with repayment over the following 10 years
- With conditionalities, which are a key consideration of this study
- In the case of Zambia, would require the support of private creditors

On the basis of cash payments for debt service obligations, the IMF ECF is amongst the lowest sources of funding available for Zambia. However, the overall cost of conditionalities are equally important given the historical context of IMF-lending, and as such must be considered in the overall economic and financial modelling of Zambia's ambitions to achieve debt sustainability whilst reducing poverty and achieving inclusive economic growth.

On 3 December 2021, the IMF announced that it had reached a Staff Level Agreement with the Government on a USD1.4 billion IMF program, over three years. It is still unclear how the funds will be disbursed, or the conditionalities imposed.

⁶¹<https://www.imf.org/en/News/Articles/2021/05/10/pr21126-zambia-imf-staff-update-on-discussions-with-the-authorities-on-a-new-ecf>

⁶²<https://www.imf.org/en/Topics/special-drawing-right/2021-SDR-Allocation>

⁶³Via Special Drawing Rights, a type of reserve allocated to IMF lenders that may be exchanged for hard currency – Zambia currently has 1,406,698,221 cumulative SDRs equivalent to USD1.97 billion as at 2 November 2021

⁶⁴<https://www.imf.org/en/About/Factsheets/Sheets/2016/08/02/21/04/Extended-Credit-Facility>

Appendix 5 – About The Researchers



Grieve Chelwa, PhD

Dr. Grieve Chelwa is the Director of Research at the Institute on Race, Power and Political Economy at The New School, where he leads the institute's work on inclusive economic rights.

Before joining the New School, Grieve was a senior lecturer in economics and MBA Program Director at the University of Cape Town's Graduate School of Business, prior to which he was the Inaugural Postdoctoral Fellow at the Center for African Studies at Harvard University. He was previously a visiting postdoctoral fellow at the Wits Institute for Social and Economic Research (WISER) at the University of the Witwatersrand. Before taking up a career in academia, Dr. Chelwa was a banker with Citi and completed postings in Congo (DR), Kenya, Nigeria, and South Africa.

Dr. Chelwa holds a BA in Economics from the University of Zambia and advanced degrees in economics, including a PhD, from the University of Cape Town. He can be reached at grievechelwa@gmail.com.



Chileshe G. Mange

Ms. Chileshe Mange is a qualified legal practitioner and practiced corporate law with Corpus Legal Practitioners advising a wide range of public and private corporate clients on mining, energy and infrastructure as well as banking and finance related transactions. Some notable clients include the Industrial Commercial Bank of China, the Bank of China, Bank of Zambia, Tullow Oil Plc and First Quantum Minerals.

Prior to a career in law, Chileshe worked extensively in Public Health and contributed to the development of health policies in Namibia for over five years during which time she consulted for organisations such as the United Nations Development Programme, the Global Fund and USAID. She also consulted

with UN Women and the Vienna Institute for Democracy on governance processes, and previously consulted for the Centre for Trade Policy and Development (CTPD), Market Access Africa and the Association for Progressive Communications.

She is an Advocate of the High Court for Zambia, a member of the Zambia Society for Public Administration and until recently, a part time tutor with the University of Zambia School of Law. Her email address is: cgmange@gmail.com



Mr. Jimmy Mwambazi

Mr. Jimmy Mwambazi is a co-founder and Managing Director for Kalene Hill Partners (Zambia). He has over twelve years of combined experience in financial services, financial research and investment management and has executed transactions in excess of USD300 million across a broad spectrum of sectors. In addition, Jimmy has completed or pursued transactions in six countries, advised clients ranging from Zambian entrepreneurs to Fortune 500 companies, led various "first-time" transactions on the Zambian capital market, and has recently consulted on sustainability (climate, gender, sovereign) financing, policy and advocacy in Africa.

Prior to Kalene Hill Partners, Jimmy worked in senior roles at Imara Corporate Finance (South Africa), the Industrial Development Corporation (Zambia), Stockbrokers Zambia (Zambia) and ZCCM Investments Holdings (Zambia).

Jimmy holds a BCom in Finance and Economics and a BCom (Honours) in Finance from the University of Kwa-Zulu Natal. His email address is: jimmy@kalenehill.com.

Notes

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#IMFAlternatives, #BeyondTheIMF, #IMFZambia, #FightInequality, #TimeToTaxTheRich
#PeoplesEconomicRecovery, #Peoplesbudget, #DebtCancellation



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