

AFRICA RISK CONSULTING

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President Edgar Lungu (2015-present) clashes with the opposition United Party for National Development (UPND) and members of his own Patriotic Front (PF) after pushing through a constitutional amendment which allows ministers to remain in office when parliament is dissolved. Lungu passed the amendment on the day when parliament closed for three months of campaigning before the general election on 11 August. The economic outlook remains poor: the Bank of Zambia (BoZ) (central bank) has retained its landmark high 15.5% interbank interest rate to try to reduce inflation which was at 21.3% in May, while the kwacha fell 7% against the dollar. However, better than expected rainfall increases the maize harvest to a record 2.78m tonnes, will mitigate the effects of the falling kwacha. Lungu reveals that the power crisis, which knocked 0.5% off GDP growth in 2015, will continue for another three years.

President and opposition row over constitutional reforms

President **Edgar Lungu** (2015-present) and opposition figures clashed on 11 May over constitutional reforms that would allow ministers to continue in office after parliament dissolved prior to the August elections.¹ The government originally tabled an amendment that would allow it to appoint ministers that were not elected members of parliament.² However, the government faced criticism from within its own **Patriotic Front (PF)** party as well as from the primary opposition, the **United Party for National Development (UPND)**.³ The Lungu administration therefore proposed a changed amendment which would allow the existing ministers to continue in office during the campaigning period.⁴ The government tabled the amendment on 11 May, the day parliament dissolved.⁵ Opposition figures say this was a deliberate move to ensure that the PF can continue to run the country with less accountability:

*"The PF waited until the last minute to table this amendment, they have governed the country so poorly and have run out of time to fix things...they are trying to cheat the electoral rules and undermine the constitution."*⁶

The opposition and law groups also argued that the government should have shelved the entire amendment when parliament rejected it in its original form.⁷ According to a member of the pro-constitutional reform think-tank, the **Foundation for Democratic Process (FODEP)**:

*"This is a simple matter of parliamentary process, if the legislature rejects a constitutional amendment the government does not have a mandate to impose half of it. The process is unconstitutional."*⁸

¹ Lusaka Times, 11 May 2016.

² Lusaka Times, 11 May 2016.

³ Zambia Daily Mail, 8 May 2016.

⁴ Lusaka Times, 11 May 2016.

⁵ Lusaka Times, 11 May 2016.

⁶ Source, opposition MP, Lusaka

⁷ Zambia Daily Mail, 8 May 2016.

⁸ Source, FODEP, Lusaka

Lungu defended his decision on 13 May to implement the amendment, arguing that the government received legal advice saying that it was within its power to implement it.⁹ He also addressed concerns that ministers would use government resources to help the PF campaign for the election:

*"I am not insisting that ministers remain in office so that we can use government resources."*¹⁰

However, the **Law Association of Zambia (LAZ)** lodged a formal legal complaint against the government on 11 May.¹¹ The professional body has referred the matter to the **Constitutional Court**,¹² but the Court has yet to release a statement on when it will rule on the issue. Zambia's general elections, and a referendum on broader constitutional reform, will take place on 11 August.¹³

Increased rainfall mitigates poor economic outlook

The economic picture has continued to be poor across May: the kwacha fell against the **United States (US)** dollar; the **Bank of Zambia (BoZ)** (central bank) has retained record high interest rates to try to keep consumer price inflation (CPI) low; and the government is still negotiating a structured loan facility from the **International Monetary Fund (IMF)**.¹⁴ However, better rainfall has helped to increase the size of the crucial maize harvest.

The kwacha fell 7.2% from K9.7 on 1 May to K10.4/\$ at time of writing.¹⁵ The fall is linked to a dip in the price of copper which fell 9.5% from \$5,050/tonne to \$4,570/tonne over the same period.¹⁶ This affirms the long-standing trend that the kwacha tracks the price of copper.¹⁷ When the copper price stabilised on 30 May the kwacha gained 1% against the dollar overnight.¹⁸ This is partly due to copper producers, who are responsible for roughly 90% of export receipts, holding onto foreign capital supplies as they anticipate further drops in the currency.¹⁹

Inflation has begun to fall, from 22.2% in March, 21.8% in April to 21.3% in May.²⁰ However, the BoZ opted to keep its benchmark interbank lending rate at a record high of 15.5%.²¹ The bank's monetary policy committee (MPC) took the decision on 17 May.²² BoZ governor **Denny Kalyalya** told the media that the bank would retain the high interest rates until inflation fell below 10%.²³

*"Inflation is trending downwards and our projections are that by the fourth quarter of this year we should be in single digit inflation."*²⁴

The poor economic performance has hit public finances. The finance ministry is in the process of preparing a deficit reduction plan for the IMF, which is expected to announce the terms of a structured loan facility later this year (see *ARC Briefing Zambia April 2016*).²⁵ The finance ministry released figures that showed that the budget deficit averaged 4.8% of gross domestic product (GDP) from 2014-2016.²⁶ However, it forecasts this to fall to 3% of GDP in the medium term starting from

⁹ Reuters, 13 May 2016.

¹⁰ Lungu, in Reuters, 13 May 2016.

¹¹ Lusaka Times, 11 May 2016.

¹² Lusaka Times, 11 May 2016.

¹³ Lusaka Times, 11 May 2016.

¹⁴ Times of Zambia, 17 May 2016.

¹⁵ www.XE.com

¹⁶ www.infomine.com

¹⁷ www.XE.com

¹⁸ www.XE.com ; www.infomine.com

¹⁹ Reuters, 19 May 2016.

²⁰ Zambia Daily Mail, 18 May 2016.

²¹ Lusaka Times, 17 May 2016.

²² Lusaka Times, 17 May 2016.

²³ Lusaka Times, 17 May 2016.

²⁴ Kalyalya in Lusaka Times, 17 May 2016.

²⁵ Reuters, 13 May 2016.

²⁶ Reuters, 13 May 2016.

the second half of 2017.²⁷ It also released figures showing that GDP growth will improve in 2016 to 3.7%, in line with the IMF's predictions released in April, which is up from 3.5% growth in 2015.²⁸ Lungu gave a media address where he said that the government would be able to address the infrastructure backlog within the year and drive higher growth and a lower deficit.²⁹ According to Lungu:

*"This performance will largely be driven by agriculture, construction and tourism."*³⁰

The primary driver of economic recovery will be a better than expected rainfall. This has changed the outlook for the crucial maize harvest to a record 2.87m tonnes, up from 2.6m tonnes in 2015.³¹ The agriculture ministry had forecast that the harvest would be 2.4m tonnes in March (see *ARC Briefing Zambia March 2016*) and the government had considered introducing capital controls on grain exporters in order to ensure local producers sold to the local market at lower costs (see *ARC Briefing Zambia April 2016*).³² Maize prices, however, remain high at over \$9/2.5kg bag due to the continuing region-wide drought which has kept production down in neighbouring **Zimbabwe** and **South Africa**.³³ Lungu told the media on 17 May that the government had received advice not to bring in the price controls, but did not specify who it was from.³⁴

Power problems due to continue for the next three years

Lungu told a meeting of the **African Development Bank (AfDB)** on 24 May that Zambia's power shortages during its dry season are due to continue for at least three years.³⁵ Poor power generation due to low rainfall caused electricity generation to drop by 33% in 2015.³⁶ It has had a severe impact on Zambia's economic development, reducing growth to an estimated 0.6% in 2015.³⁷ The energy ministry said in January that the government intended to solve the power crisis by the start of the dry season in August 2016 by commissioning independent power producers to add an extra 500MW of generation potential to the power pool.³⁸ This will start with a new 300MW coal-fired plant currently in development that is expected to come online in June.³⁹ However, the government has not commented on four further power generation contracts it was due to sign in January (see *ARC Briefing Zambia January 2016*). In 2015 Zambia generated only 65% of its total generation capacity of 2150MW. This was primarily due to the **Kariba Power Plant**, a hydro generation plant that produces 50% of Zambia's power, running at just 25% of capacity from August 2015 to January 2016.⁴⁰ According to an experienced power investor, the process of adding to the grid will take time:

*"The idea that Zambia could solve its power deficit in a year was always highly unrealistic, just getting the finance structuring for a small power plant can take over a year and this is before you have factored in any potential delays in the development stage."*⁴¹

However, Zambia remains highly exposed to decreased rainfall, as hydroelectricity accounts for 75% of its power generation.⁴² Lungu revealed that the government expects generation to fall by 38.9% in

²⁷ Reuters, 13 May 2016.

²⁸ Reuters, 13 May 2016.

²⁹ Zambia Report, 17 May 2016.

³⁰ Lungu in Zambia Reports, 17 May 2016.

³¹ Lusaka Times, 4 May 2016.

³² Lusaka Times, 4 May 2016.

³³ Lusaka Times, 4 May 2016.

³⁴ Zambia Report, 17 May 2016.

³⁵ Lusaka Times, 24 May 2016.

³⁶ Lusaka Times, 24 May 2016.

³⁷ Lusaka Times, 24 May 2016.

³⁸ Reuters, 22 Jan 2016.

³⁹ Reuters, 22 Jan 2016.

⁴⁰ Reuters, 22 Jan 2016.

⁴¹ Source, power investor, London

⁴² Lusaka Times, 24 May 2016.

2016 due to continuing repairs at power plants as well as the current drought.⁴³ The recent higher rainfall has increased the maize crop (see above) and will have an impact on these figures; however, it will not be enough to replenish the reserves in **Lake Kariba**, which dropped to 12% in January 2016, the end of the last dry season.⁴⁴ According to Lungu:

"The effects of these developments are expected to take long to moderate with power generation in countries such as Zambia and Zimbabwe expected to return to normal only in three years."⁴⁵

Implications

Lungu and the PF agreed to a blended constitutional reform programme in March 2015 which gives the government power to pass minor reforms on parliamentary vote. The amendment Lungu pushed through is likely to fall within this remit, which will allow PF ministers to continue to access government resources during campaigning. Opposition fears that this might impact the campaign are well founded; however it is less likely that Lungu passed it in order to advantage the PF. The current economic situation and the need to continue negotiating with the IMF are good reasons to keep key ministers in post despite the upcoming elections.

The economy remains exposed to both fluctuations in the price of copper and rainfall. Currently good rainfall is balancing out poor prices of copper. However, the government has no way of preventing both from applying negative pressure on the economy in the future, as they did in 2015. The gains in the kwacha will take some of the pressure off businesses that rely on imported goods, but the high interest rates will apply some downwards pressure to growth. The government claims that it is implementing an economic diversification plan, though it has yet to release any details. This may come with the IMF loan facility after the elections.

Sources within the private power generation sector have repeatedly said that the government's claim that it could turn the power crisis around within a year was unrealistic. Lungu's statement to the AfDB shows the government coming to the same realisation. Zambia's economic situation makes it a less attractive investment for power generation than other countries in the region. The power crisis will continue to apply downwards pressure on the economy in the medium term.

⁴³ Lusaka Times, 24 May 2016.

⁴⁴ Reuters, 22 Jan 2016.

⁴⁵ Lungu, Lusaka Times, 24 May 2016.

About Africa Risk Consulting:

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