

AFRICA RISK CONSULTING

Zambia Monthly Briefing November 2015

Zambia Summary 30 November 2015

An International Monetary Fund (IMF) team finds that the Zambian economy is under considerable stress, however the government pushes back any intervention until after a second IMF visit in March 2016. The kwacha rallies 12% against the dollar across November breaking a four-month trend of depreciation. It remains 70% lower against the dollar across 2015. The Bank of Zambia raises interest rates to 15.5% from 12.5% in order to curb increasing inflation which reached 7.7% in September. Mopani Copper Mine and Konkola Copper Mine begin lay-offs of 4,300 and 2,500 employees respectively after a year of low copper prices and a difficult operating environment.

Zambia pushes back IMF intervention...

A team from the **International Monetary Fund (IMF)** visited Zambia between 11 to 20 November to review the economic situation and to assess the government's response to the faltering economic situation.¹ The government invited the IMF team to the country in September following a year of falling copper prices and the collapse of the Zambian kwacha. However, President **Edgar Lungu** (2015-present) has decided not to take the IMF up on its offer of aid and has pushed back any intervention until March 2016.² The IMF found the economic situation to be poor in its report on 26 November:

"The Zambian economy is under stress. Low copper prices and a severe electricity shortage are straining the economic activity. The Zambian kwacha has lost half of its value since the beginning of the year, causing difficulties for many segments of the economy and population and putting upward pressure on inflation. Moreover, domestic and external financing conditions have tightened markedly, with increased interest rates on the Zambian government debt."³

The president held a joint press conference with members of the IMF team at **State House** the same day, and admitted that the economy is facing severe challenges due to a combination of external and internal factors. It is the first time a president has held a press conference with IMF representatives on fiscal matters. According to Lungu:

*"On the external side, a slowdown in economic activities mainly in **China** and the **Eurozone**, coupled with the strengthening of the **United States** dollar, has led to a drop in commodity prices and a fall in investment inflows...as a result, copper prices have slumped by 26% since the beginning of this year leading to a fall in production and scaling back of some mining operations...On the domestic side, the poor rainfall pattern particularly in the 2014/15 agricultural season has led to a fall in crop production and a severe decline in electricity generation. Non-traditional export earnings have declined by 36.6%."⁴*

The IMF has said it has reached an understanding with the Zambian government on the current economic challenges and implication of alternative policy choices. The IMF and the Zambian

¹ Times of Zambia, 19 Nov 2015.

² Presidential Speech during the Press Conference, 26 Nov, 2015.

³ IMF press statement, 20 Nov 2015.

⁴ Presidential Speech during the Press Conference, 26 Nov, 2015.

government will continue to discuss the forms and timing of engagements.⁵ The IMF mission team met with President Lungu, finance minister **Alexander Chikwanda, Bank of Zambia (BoZ)** (central bank) governor **Denny Kalyalya**, the private sector, labour unions, civil society organisations and other development partners for Zambia. The IMF team is scheduled to visit Zambia again in March 2016 and Lungu told the press that the government will decide whether or not it will go with the IMF assistance at that time.⁶ According to deputy finance minister **Christopher Mvunga** the government is playing for time to carry out its own internal fiscal measures to try to resolve the economic situation:

“Government is looking at different options...we’re not averse to an IMF package. We’ve put our own measures in place, so let’s see how these measures work out, if we’re able to correct the issues that are around. We’ll look at any possible means that are best for the country.”⁷

But opposition figures have criticised the government for not taking the IMF’s assistance immediately. Former finance minister **Situmbeko Musokotwane** wrote an article in the **Lusaka Times** saying that Zambia should access the emergency funding from the IMF.⁸ Musokotwane said the government should quickly restore investor confidence and re-kindle faster economic growth.⁹ He also said that the government did not want to take the IMF aid for political reasons, and would damage the economy as a result.¹⁰ Musokotwane was finance minister from 2008-2011 under the last administration of the now opposition party **Movement for Multiparty Democracy (MMD)**.¹¹ Figures close to the government say that the popularity issue is a factor in the decision:

“The administration would not hold out on the IMF if the country needed it urgently but as the situation might stabilise soon then senior guys in the finance ministry would like to try and avoid it if possible. After all there is an election coming [in September 2016].”¹²

...as the kwacha rallies across November and BoZ increases interest rates

The kwacha appreciated 12% against the dollar across November, reversing a four-month trend of net losses. The currency fluctuated across the month reaching a new low of K14.27 to the dollar on 10 November.¹³ However, it appreciated 23% to K10.98 to the dollar from 10 to 23 November and remains at K10.98 at time of writing.¹⁴ The kwacha is now back at values it last hit in late September but this still represents at 72% depreciation across 2015 from its January value of K6.38.¹⁵

The reasons for the appreciation are unclear. The copper price has not increased across the month. It fell to a new low of \$4,444 per tonne on 23 November, and has recovered slightly to \$4,530 at time of writing.¹⁶ The slump represents a 12% decrease across the month from \$5,150 per tonne on 1 November.¹⁷ When Lungu committed to helping the mining sector and cut spending on 26 November there was a slight appreciation in the currency.¹⁸ The BoZ reports that foreign currency inflows increased across November 9.2%, however it did not suggest an explanation given the current poor state of the mining industry (see below).¹⁹

⁵ IMF press statement, 20 Nov 2015.

⁶ Press Conference, 26 Nov 2015.

⁷ Mvunga in Bloomberg, 27 Nov 2015.

⁸ Lusaka Times, 26 Nov 2015.

⁹ Lusaka Times, 26 Nov 2015.

¹⁰ Bloomberg, 27 Nov 2015.

¹¹ Bloomberg, 27 Nov 2015.

¹² Source, journalist with PF connections, Lusaka

¹³ XE.com

¹⁴ XE.com

¹⁵ XE.com

¹⁶ Infomine.com

¹⁷ Infomine.com

¹⁸ Lusaka Times, 27 Nov 2015.

¹⁹ Bank of Zambia Press Statement, 5 Nov 2015.

The appreciation also appears to be unrelated to the BoZ's monetary policy efforts. The BoZ increased the central lending rate 300 basis points to 15.5% from 12.5% on 2 November.²⁰ The rate raise was an effort both to slow the fall of the kwacha and to keep consumer price index (CPI) inflation under control. According to the BoZ, annualised CPI inflation was 7.4% in the third quarter of 2015, 0.3% higher than the second quarter average of 7.1%. Inflation rose to 7.7% in September up from 7.1% in June.²¹

Copper mines begin lay-offs after difficult year

The copper industry started laying off thousands of employees after a year of record low copper prices hit profitability. **Switzerland**-based **Glencore** subsidiary **Mopani Copper Mine (MCM)** has started laying off over 4,300 employees as part of its debt reduction strategy.²² In September, Glencore announced a reduction of its over \$30 billion net debt by \$10 billion at the end of next year by suspending operations at MCM for 18 months (see *ARC Briefing Zambia September 2015*). A source at MCM said that the job losses were a painful but necessary compromise:

*"Of course it's a painful decision to send people home but as a company, we also need to continue in existence. For now, we had no choice but to make this decision, though it's a painful one."*²³

Of the total number of workers affected, 3,051 were laid off while 1,249 opted for voluntary separation. The lay-offs proceeded after negotiations with the **Mine Workers Union (MWU)** that represents MCM workers. MWU president **Chishimba Nkole** said after months of negotiations, the union had agreed with MCM that the retrenchments were the only viable option available.²⁴ Lungu told a press conference on 26 November that his government had tried to save the jobs of miners but eventually they agreed that some workers needed to be laid off.

*"In fact, over 7,000 jobs were at stake, but through the negotiations, Mopani can only do so much and over 4,000 workers have been affected. I take this issue very seriously and that is why I had to involve myself in the negotiation process and I monitored all the discussions that took place on this issue."*²⁵

London Stock Exchange (LSE)-listed **Vedanta Resources** owned **Konkola Copper Mine** has also started laying off workers in November after declaring the mine is not sustainable anymore.²⁶ Konkola say that it will lose between \$30m and \$40m if they continue to operate loss-making **Nchanga** underground mine during the year.²⁷ The closure of the mine, one of several that Konkola operates, will lead to the lay-offs of 2,500 workers.²⁸ A source within Konkola confirmed that the company has already started laying off workers and that the process will continue until they reach a point where the production will pick up and copper prices stabilise.²⁹ The company will then carry out a technical review of the site until it works out how to ensure it can be profitable:

*"We are not pulling back from the site, we are just trying to make sure we can continue to be a profitable business that can provide jobs for the local community."*³⁰

²⁰ Bank of Zambia Press Statement, 5 Nov 2015.

²¹ Bank of Zambia Press Statement, 5 Nov 2015.

²² Zambia Daily Mail, 21 Nov 2015.

²³ Source, MCM, Copperbelt

²⁴ Zambia Reports, 17th November 2015.

²⁵ Presidential Speech during the Press Conference, 26 Nov, 2015.

²⁶ Mining Technology, 27 Nov 2015.

²⁷ Mining Technology, 27 Nov 2015.

²⁸ Mining Technology, 27 Nov 2015.

²⁹ Source, Konkola, Copperbelt

³⁰ Source, Konkola, Copperbelt

Implications

Zambia's economic situation is poor; however, much of the problem rests on factors beyond government control. The heavy reliance on a single commodity – copper – has left the economy highly exposed to fluctuations in China's demand. Two bond auctions have also exposed the government to the international capital markets. Traders invested in Zambia sovereign debt who are hesitant about the country's economic performance can undermine on foreign exchange markets any action that the BoZ or the finance ministry takes to shore up the kwacha. The government has committed to tightening spending since Lungu became president in January 2015, and it will take time to implement any programme of fiscal responsibility. However, the decision to delay direct IMF intervention cannot be taken outside of the context of the 2016 elections, which Lungu needs to win to prove he has a real mandate to govern. Lungu and Chikwanda are banking on further currency stabilisation and that the worse of the copper slump is now over. This is a risky bet to take when the country's economic stability is on the line.

The appreciation of the kwacha across November will ease inflationary pressure on Zambia's citizens and businesses. They have had to fight the rising cost of imported goods and the risk of multiple companies shedding staff to survive. It may be that a positive cycle of good news – starting with the IMF visit, and continuing with Lungu's pro-business and fiscally cautious speech – has helped keep the currency up in the latter weeks of the month. It is also good news that the currency has held its new value of K10.98/\$ for over a week, a level of stability not seen since March this year. However, the last few years of currency fluctuations show that the kwacha is highly exposed to external factors and the markets could easily lose confidence in the currency in the future.

The relationship between the Lungu administration, copper miners and unions is a model for countries across the region. Despite enormously difficult economic circumstances for both the government and copper companies, President Lungu has personally made sure that all sides sit around the table rather than risking damaging strike action. The result is a structured programme of retrenchments with a number of voluntary redundancies focused on contract workers rather than longer term employees. This keeps the political risk of redundancies low. However the influx of labour onto the market will have a poor short to medium term impact on the economy, particularly in the **Copperbelt** region.

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