

AFRICA RISK CONSULTING

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Zambia Summary 24 September 2018

The United Kingdom (UK) suspends aid payments to Zambia over alleged government fraud and corruption. President Edgar Lungu (2015-present) fires community development and social services minister Emerine Kabanshi and Zampost postmaster General McPherson Chanda in response. Finance minister Margaret Mwanakatwe denies the government offered state-owned enterprises to China as collateral for further borrowing following an Africa Confidential report that claimed the government offered power utility Zesco as security against a loan. United States-based ratings agency Standard & Poor's (S&P) downgrades Zambia's long-term foreign and local currency sovereign credit ratings from 'B' to 'B-', but keeps the outlook stable.

UK and other countries suspend aid over fraud allegations

The **United Kingdom (UK)** confirmed it suspended aid payments to **Zambia** on 17 September over alleged government fraud and corruption.¹ Online media source **Africa Confidential** noted on 14 September that officials fraudulently diverted aid payments from the health, education, and local communities departments.² The UK has reportedly been aware of issues since a 2016 Zambian auditor-general report noted several red flags in funding for the education department. This led the UK's **Department for International Development** to ask for restitution of \$4.7m in aid payments that were diverted from the **Social Protection and Expansion Programme (Social Cash Transfer)** to officials of the state-owned postal company, **Zampost**, which administers the programme.³ The UK high commissioner to Zambia, **Fergus Cochrane-Dyett**, confirmed the reports of the freezing of aid:

"[It is] correct that the UK has frozen all bilateral funding to the Zambian government in light of potential concerns until audit results are known."⁴

The UK pledged \$62.2m in aid to Zambia for 2017-2018. It is not known how much of that has already been disbursed and how much has been suspended.⁵ However, in a speech to the national assembly on 20 September, finance minister **Margaret Mwanakatwe** stated that the UK withheld aid only to the Social Cash Transfer programme and that other areas have not been affected.⁶

The UK is not the only country to freeze funding to Zambia. **Finland, Sweden, Ireland** and **United Nations** aid agency **Unicef** have also suspended aid payments over these concerns, as well over reports that medical supplies and drugs were stolen with high-level involvement.⁷ According to Mwanakatwe, a total of \$20m in funding for the Social Cash Transfer programme is frozen, as well as \$13.9m for the education sector.⁸

In response, President **Edgar Lungu** (2015-present) fired community development and social services minister **Emerine Kabanshi** and Zampost post master **General McPherson Chanda** on 19

¹ Times Live, 18 Sep 2018

² Africa Confidential, 14 Sep 2018

³ Africa Confidential, 14 Sep 2018

⁴ Times Live, 18 Sep 2018

⁵ Times Live, 18 Sep 2018

⁶ Zambia Reports, 20 Sep 2018

⁷ Africa Confidential, 14 Sep 2018

⁸ Zambia Reports, 20 Sep 2018

September.⁹ Mwanakatwe also said that the government will re-evaluate its payment and identification systems to make sure the right beneficiaries are paid and to make sure all unpaid beneficiaries are paid by the end of 2018.¹⁰

The freezing of aid will further hurt Zambia's economy as the government struggles to continue to meet debt repayments as well as other expenditure. According to government sources, the government is partly funding current account expenditure with the government pension scheme, which has caused delays in disbursements to pensioners.¹¹ The government's debt repayment and its failure to collect enough revenue has caused the liquidity issue and forced the government to look to other areas for funds.¹² There is no indication if or when the UK and other countries plan on unfreezing the aid. It is more likely they will look into other departments for similar corruption issues, which may result in a further freezing of aid.

Officials deny government offered state-owned enterprises to China as debt collateral

Finance minister Margaret Mwanakatwe has denied that the government offered state-owned enterprises to **China** as collateral for further borrowing.¹³ An **Africa Confidential** report on 3 September stated that the government offered power utility **Zesco** as security against a loan.¹⁴ The Africa Confidential report covered China's strategy of 'debt diplomacy' in **Africa**, in which it offers cheap debt in return for overpriced infrastructure projects as part of its **Belt and Road Initiative (BRI)**.¹⁵ According to Africa Confidential,

*"A major worry of the **International Monetary Fund (IMF)** and the **United States (US)** is that China's BRI strategy is first to encourage indebtedness, and then to take over strategic national assets when debtors default on repayments. The state electric company, Zesco, is already in talks about a takeover by a Chinese company... The state TV and radio news channel [**Zambian National Broadcasting Corporation (ZNBC)**] is already partly Chinese-owned. The long-term outcome could be effective Chinese ownership of the commanding heights of the economy and potentially the biggest loss of national sovereignty since independence."¹⁶*

China's ambassador to Zambia, **Li Jie**, has also denied the allegations and stated that China does not own any part of Zesco or ZNBC.¹⁷ However, media reported in February that ZNBC entered into a 25-year agreement with China-based television provider **StarTimes** to distribute decoders for digital television.¹⁸ Media reported that a StarTimes subsidiary, **TopStar Communications Ltd**, owns 60% of ZNBC as part of the deal. However, information minister **Dora Siliya** states that TopStar is a joint venture in which StarTimes owns 60% while ZNBC owns 40%.¹⁹ So while ZNBC is still 100% government-owned, TopStar will collect all ZNBC advertising revenue and broadcast tower rental fees which will be used to service a \$273m loan from the **Export-Import Bank of China** to ZNBC for infrastructure upgrades.²⁰

The accusations of state-owned enterprises offered as collateral, while not proven, have resulted in anger against Chinese companies in Zambia.²¹ Zambia's debt, which stood at \$9.3 billion at the end of March, is up from \$8.7 billion at the end of 2017 and is at a high risk of debt distress, according to the

⁹ Lusaka Times, 19 Sep 2018

¹⁰ Zambia Reports, 20 Sep 2018

¹¹ Africa Confidential, 14 Sep 2018

¹² Africa Confidential, 14 Sep 2018

¹³ Reuters, 13 Sep 2018

¹⁴ Reuters, 13 Sep 2018

¹⁵ Africa Confidential, 3 Sep 2018

¹⁶ Africa Confidential, 3 Sep 2018

¹⁷ Lusaka Times, 14 Sep 2018

¹⁸ Public Media Alliance, 24 Feb 2018

¹⁹ Zambian Watchdog, 13 Sep 2018

²⁰ Public Media Alliance, 24 Feb 2018

²¹ Times Live, 23 Sep 2018

IMF.²² The opposition **United Party for National Development** described the rate of Chinese investment, and particularly the policy of using Chinese workers on projects, as “*a time bomb*”.²³ Regardless, the government continues to look for further funding. President Lungu reportedly received a \$30m interest-free loan and a \$30m grant agreement at the **Forum on China-Africa Cooperation** in September.²⁴ A Zambia-based source notes that

“...Lungu is likely looking for further funding from China considering an IMF bailout is basically off the table. There is no proof that Lungu or other government officials offered up state companies as collateral, but I would imagine it was at least discussed, as any lender would need some sort of security to extend further loans to Zambia considering its current economic condition.”²⁵

With this political fallout, any plans to offer state-owned enterprises will be off the table. However, the government will still need to find financing to fund expenditure and re-service debt, which totalled \$342m in the first half of 2018.²⁶ The government will struggle to do this, which may result in a default of its debt and a pause in debt re-service, placing Zambia in even deeper financial crisis.

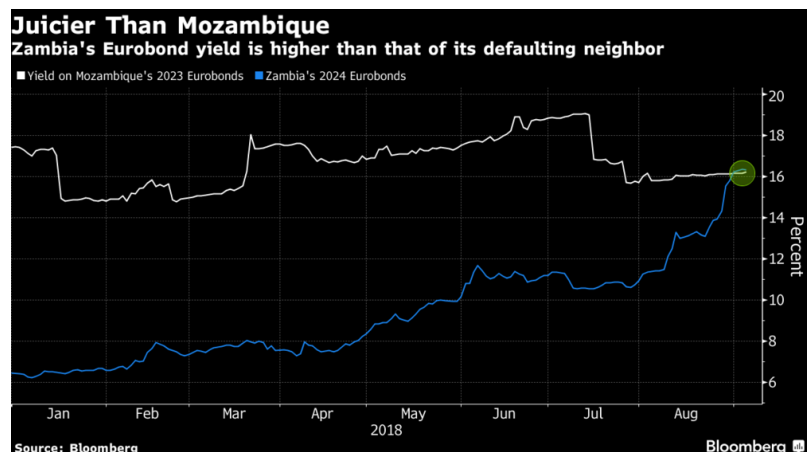
Standard & Poor’s downgrades Zambia’s long-term debt

US-based ratings agency **Standard & Poor’s (S&P)** downgraded Zambia’s long-term foreign and local currency sovereign credit ratings on 24 August from ‘B’ to ‘B-’, though it kept the outlook as “*stable*”.²⁷ The reason for the downgrade is expected higher deficits and faster debt accumulation than previously forecast, though S&P does not expect to raise the ratings over the next year.²⁸

The government has attempted to reign in its spending. The finance ministry announced on 6 September that it plans to limit its fiscal deficit to 5.1% by 2021, down from 7.8% in 2018.²⁹ The finance ministry expects economic growth to remain around 4% between 2019 and 2021, while inflation would be between 6-8%.³⁰ Almost ironically, Zambian bonds are yielding more than **Mozambique**, which has

completely defaulted on its debt and has stopped re-servicing its debt. Investors are thus still more confident that Mozambique will eventually pay off its debt than Zambia.

While the forecast is positive, the IMF will expect to see more government action to achieve these goals before a proposed \$1.3 billion loan is granted. The IMF stated on 25 August that negotiations are still frozen and no discussions will occur until major changes are made to Zambia’s borrowing plans.³¹



²² Reuters, 13 Sep 2018

²³ Times Live, 23 Sep 2018

²⁴ VOA, 16 Sep 2018

²⁵ Source, economic analyst, Zambia

²⁶ Times Live, 23 Sep 2018

²⁷ S&P, 24 Aug 2018

²⁸ S&P, 24 Aug 2018

²⁹ Reuters, 6 Sep 2018

³⁰ Reuters, 6 Sep 2018

³¹ africanews, 25 Aug 2018

Contradictory to the IMF's forecast, the **World Bank's** country economist, **Zivanemoyo Chinzara**, is adamant that Zambia is not in a debt crisis and that there are only 10 African countries in actual debt distress, which is mainly due to external shocks.³² Chinzara noted that

"...If you are in high risk of debt distress, it doesn't mean you are in debt distress; it doesn't mean you are in a debt crisis. It means you need to take action because if you don't take action, the consequences can be dire. And the consequences can include macroeconomic instability and more spending going towards debt service, but less going to other sectors of the economy."³³

However, World Bank country manager **Ina-Marlene Ruthenberg** noted that the lending rate remains too high for the private sector to borrow, which would create jobs, and that gross domestic product is forecast to decrease (by World Bank measures) to just 3.3%, down from 4.3%.³⁴ President Lungu appears to be facing a perfect storm of issues – economic and political – and will need to pull out all the stops to contain it. Lungu's **Patriotic Front** party will need to use more resources to contain these issues rather than pushing Zambia's economy forward. Zambia can probably expect more political drama, such as arbitrary arrests of opposition leaders.

Planner

19-20 Nov 2018 **Lusaka (Zambia) Bank of Zambia** (central bank) Monetary Policy Committee meeting;

2021 **(Zambia)** Scheduled presidential elections;

Chronology

21 Sep 2018 **Lusaka (Zambia) Lusaka Times**. **World Bank** country economist **Ziv Chinzara** says that **Zambia** is not in a debt crisis, despite media reports;

19 Sep 2018 **Lusaka (Zambia) IOL**. **Sweden** freezes all funds to **Zambia** over a reported misuse of funds, joining the **United Kingdom (UK), Finland** and **Ireland**;

19 Sep 2018 **Lusaka (Zambia) News24**. President **Edgar Lungu** dismisses development minister **Emerine Kabanshi** after reports of abuse of funds which led to the UK and others to freeze all bilateral funding;

18 Sep 2018 **Lusaka (Zambia) Times Live**. The **United Kingdom (UK)** high commissioner to **Zambia, Fergus Cochrane-Dyett**, confirms that the UK has suspended aid payments to Zambia over alleged fraud and corruption;

14 Sep 2018 **Lusaka (Zambia) Zambia Reports**. The **Chinese** ambassador to **Zambia, Li Jie**, denies claims that Zambia offered state-owned companies as collateral for new loans;

13 Sep 2018 **Lusaka (Zambia) EWN**. Finance minister **Margaret Mwanakatwe** denies that **Zambia** offered its power utility to China as security for a loan;

11 Sep 2018 **Lusaka (Zambia) VOA**. Presidential spokesman **Amos Chanda** denies that **China** is taking over any state-owned assets after several blogs and newspaper stated that China was in control of the state-owned TV and radio station, **ZNBC**;

10 Sep 2018 **Lusaka (Zambia) Lusaka Times**. Energy minister **Mathew Nkhuwa** states that the memorandum of understanding to establish an oil pipeline between **Zambia** and **Angola** will be signed 12 October;

³² Lusaka Times, 21 Sep 2018

³³ News Diggers, 24 Sep 2018

³⁴ News Diggers, 24 Sep 2018

6 Sep 2018 **Lusaka (Zambia)** *Reuters*. The finance ministry states it plans to limit the fiscal deficit to 5.1% by 2021, from 7.8% in 2018;

27 Aug 2018 **Lusaka (Zambia)** *NewsDiggers*. **United States**-based ratings agency **Standard & Poors** downgrades **Zambia's** long-term foreign and local currency sovereign credit rating to B-, but maintains a stable outlook for the economy;

25 Aug 2018 **Lusaka (Zambia)** *africanews*. The **International Monetary Fund** states that talks with **Zambia** for a \$1.3 billion bailout are still on hold;

22 Aug 2018 **Lusaka (Zambia)** *Mining Weekly*. **Bank of Zambia** (central bank) governor **Denny Kalyalya** states that copper output rose 10.6% year-on-year to 402,222 tonnes in the first half of 2018;

22 Aug 2018 **Lusaka (Zambia)** *The Herald*. China-based **China Non-Ferrous Metals Company Ltd**, launches the **Chambishi South-East mine**, in addition to its **Chambishi main mine** and **Chambishi west mine**;

21 Aug 2018 **Lusaka (Zambia)** *Press Release* The **Bank of Zambia** (central bank) holds the policy rate unchanged at 9.75%;

22 Aug 2018 **Lusaka (Zambia)** *Bloomberg*. **Italy**-based electricity and gas company, **Enel SpA**, starts construction of the 34 megawatt **Ngonye** solar plant, which should be operational by 2019;

20 Aug 2018 **Addis Ababa (Ethiopia)** *Reuters*. State-owned **Ethiopian Airlines** signs a shareholding agreement with **Zambia's Industrial Development Corporation** to revive **Zambia Airways**;