

AFRICA RISK CONSULTING

Zambia Monthly Briefing September 2015

Zambia Summary 23 September 2015

Switzerland-based Glencore suspends operations at its Mopani mine for 18 months. The move cuts 3,800 jobs and decreases Zambia's copper output by 26%. The closure threatens government revenues as well as the economy of the Copperbelt region which relies on large mining operations. The kwacha falls to a six year low of K10.56 to the dollar; the Bank of Zambia and the treasury are unable to halt the slide and agree not to intervene further to stabilise the currency. Zambia's power deficit increases to 985MW from 560MW in March as demand increases during the hot and dry months of September to November.

Glencore's Mopani suspension threatens Copperbelt and economy

Switzerland-based **Glencore** suspended operations at its **Mopani Copper Mine (MCM)** in **Copperbelt** province on 8 September.¹ This reduces Zambia's copper output and therefore government revenues. The mine is one of the largest employers in the sector and produces 200,000 tonnes of copper per annum, around 26% of the country's total output.² The company claims the move is due to external factors such as the falling price of copper but company sources say that the continuing power crisis was a key factor (see below).³ The government and unions have criticised Glencore for putting 4,300 jobs at risk. However after weeks of talks, the government accepted 3,800 job cuts on 23 September.⁴

Glencore is suspending operations at MCM for 18 months.⁵ The company will redevelop its processing facilities at the site in order to reduce the cost of processing copper and says that it plans to re-open the mine in 2017.⁶ The move is part of a wider \$10 billion debt reduction plan Glencore announced on 7 September.⁷ However, local issues also contributed to the decision. A senior source at MCM said that the decision of the **Copperbelt Energy Corporation (CEC)** to require copper mines to purchase 20% of their power at import prices in August (see *ARC Briefing Zambia August 2015*) was a factor behind Glencore suspending operations:

*"The load shedding (power outage) is one of the factors that has forced that decision on us. As you may be aware, CEC wrote to us indicating to us that they were going to restrict power supply to this mine by 30%. [The electricity] we are receiving currently is not something that is readily available at the current price. It is at the imported premium price and if you look at the imported premium price, it is something that we can't sustain if you look at the current copper price."*⁸

President **Edgar Lungu** (2015-present) called MCM executives for crisis talks with him, mines minister **Christopher Yaluma** and labour minister **Fackson Shamenda** on 10 September.⁹ Lungu

¹ Lusaka Times, 8 Sep 2015.

² Glencore website, 2015

³ Source, MCM executive, Kitwe

⁴ Bloomberg, 23 Sep 2015.

⁵ FT, 8 Sep 2015.

⁶ FT, 8 Sep 2015.

⁷ Lusaka Times, 8 Sep 2015.

⁸ Source, MCM executive, Kitwe

⁹ Zambia Reports, 10 Sep 2015.

originally said that the government would not accept any “illegal retrenchments”.¹⁰ The ministers met representatives from MCM and Glencore on 18 September, and reached an agreement to allow the suspension to go ahead.¹¹ Lungu’s spokesperson **Amos Chanda** told the media on 23 September that the president would allow job cuts “that were legal”.¹² This implies that the suspension of activity will go ahead but on a reduced scale. Sources within the government told the media that MCM would now lay off 3,800 people – reducing the number of jobs lost by 500.¹³ Glencore also promised investment of up to \$1 billion in the mine to build its more efficient copper processing plant.¹⁴

Union leaders are unhappy at the prospect of large job losses at the mine, but are realistic about the prospects for compromise. **Mine Workers Union of Zambia (MUZ)** and **Zambia Congress of Trade Union (ZCTU)** president **Chishimba Nkole** said the situation is gloomy for the sector.¹⁵ Nkole lobbied the government to intervene to reduce the job losses and resolve the situation.¹⁶ He will attend a 28 September meeting with the government, unions and mining companies to discuss how to keep as much of the workforce intact as possible.¹⁷ Zambia’s other major mining union, the **National Union of Miners and Allied Workers (NUMAW)**, will also attend the meeting.¹⁸

However, even a compromise agreement will have a serious impact on the Copperbelt regional capital **Kitwe**:

“This will bring untold misery to this town [Kitwe]; you know this town depends on the mines running. If the mines are not running, this town is going to die and become just like a ghost town. Even all these businesses and the subsequent satellite businesses that are associated with the mines are going to go down. So, I would have thought that this is the time that government should quickly intervene and solve the situation here.”¹⁹

There has been an uncharacteristic lack of communication about the suspension. According to the NUMAW source, MCM assured union leaders in August that it would not suspend operations despite the increased cost of power and decreasing price of copper.²⁰ However, the MCM source said the local company had to comply with Glencore’s plans, and the 18-month suspension “was the best we can do for the moment...we are talking to the unions to try and resolve the situation”.²¹

Union leaders and the government are concerned about further job losses as a result of other mine closures. The **Baluba Mine**, which **China Non-Ferrous Metal Mining Corporation (CNMC)** subsidiary **Luanshya Copper Mines** owns, went under care and maintenance on 8 September, putting 1,600 workers on forced leave.²² The government is currently trying to prevent the mine closure. It claims that Luanshya did not follow proper procedure when suspending operations.²³ Government spokesperson **Chishimba Kambwili** said that if the company did not follow proper procedure, the mines ministry would suspend its licence to operate.²⁴

¹⁰ Zambia Reports, 10 Sep 2015.

¹¹ Reuters, 19 Sep 2015.

¹² Bloomberg, 23 Sep 2015.

¹³ Bloomberg, 23 Sep 2015.

¹⁴ Reuters, 23 Sep 2015.

¹⁵ Post Newspaper, 14 Sep 2015.

¹⁶ Zambia Reports, 9 Sep 2015.

¹⁷ Zambia Watchdog, 23 Sep 2015.

¹⁸ Bloomberg, 23 Sep 2015.

¹⁹ Source, NUMAW leader, Kitwe

²⁰ Source, NUMAW leader, Kitwe

²¹ Source, MCM executive, Kitwe

²² Post Newspaper, 14 Sep 2015.

²³ Tumfweko, 21 Sep 2015.

²⁴ Tumfweko, 21 Sep 2015.

Kwacha devaluation defies government intervention

The kwacha continues to devalue against the dollar, increasing pressure on business operations and government revenues.²⁵ The currency fell to an all-time low against the dollar of K10.56 on 23 September.²⁶ It has had wide fluctuations across the past few months, depreciating 30% against the dollar to K9.83 from K7.87 across August.²⁷ The currency first passed K10 to the dollar on 4 September, its lowest point since 2009. However, it appreciated across the middle of the month to K9.57 on 13 September. It then fell back to K10.03 on 17 September and has gradually depreciated since.²⁸ It has now depreciated 35% against the dollar in 2015, and 69% year-on-year.²⁹

The **Bank of Zambia (BoZ)** did not intervene in August when the currency started an accelerated depreciation against the dollar. It stated on 3 September that it would not intervene on the foreign exchange markets and would maintain its foreign exchange reserves and a flexible exchange rate.³⁰ The BoZ's rationale is that external factors, notably the price of copper, were behind the currency collapse and the temporary buying of foreign currency would not affect the overall trend of depreciation.³¹ Following the announcement there was widespread panic buying of exported goods across the country and the currency continued to fall.³² Lungu intervened and injected \$120m into the market in an effort to save the currency from further collapse on 5 September.³³ BoZ governor **Den Kalyalya** supported the move as a way to stabilise the currency without trading on the foreign exchange markets.³⁴ According to Kalyalya the finance ministry converted part of the \$120m into kwacha in order to pay kwacha-based invoices (such as the public wage bill) but the bulk of the money went into the BoZ to boost foreign currency reserves.³⁵

Lungu attributed the currency collapse to global economic developments that have had adverse effects on many emerging and developing economies, including Zambia.³⁶ He says the treasury and the BoZ have closely monitored international developments to assess the impact on the domestic economy and the kwacha.³⁷

*"Both traditional and non-traditional exports have declined significantly this year while imports have declined at a slower pace. As a result, the kwacha has been on a depreciating trend. The Treasury has been authorised to make all necessary assessments and recommend interventions that include release of money into the market."*³⁸

The deteriorating balance of payments has compounded this. Zambia's revenues are due to fall below the \$202m revised projection of finance minister **Alexander Chikwanda** in June 2015.³⁹ In a letter to President Lungu, Kalyalya stated:

*"Zambia remains vulnerable to developments in the global economy. In particular, the balance of payments position has deteriorated, reflecting a widening current account deficit as both traditional and non-traditional exports have declined significantly this year."*⁴⁰

²⁵ XE.com

²⁶ XE.com

²⁷ XE.com

²⁸ XE.com

²⁹ XE.com

³⁰ BoZ press statement, 3 Sep 2015.

³¹ BoZ press statement, 3 Sep 2015.

³² Zambia Reports, 4 Sep 2015.

³³ State House Press Statement, 5 Sep 2015.

³⁴ Times of Zambia, 6 Sep 2015.

³⁵ Bank of Zambia Governor Press Briefing, 10 Sep 2015.

³⁶ State House Press Statement, 5 Sep 2015.

³⁷ State House Press Statement, 5 Sep 2015.

³⁸ State House Press Statement, 5 Sep 2015.

³⁹ Reuters, 9 Sep 2015.

⁴⁰ Post Newspapers, 21 Sep 2015.

Both agree that if more dollars return to the economy, primarily through increased export revenues, the currency will gain value.⁴¹ However, given the closure of at least one major copper mining operation (see above), exports are projected to decrease in 2015. There are also internal factors dragging down the value of the kwacha such as the power deficit (see below) which the government has not addressed in statements about the value of the currency. For the moment there will be no further centralised action. A source within the finance ministry confirms that:

"The kwacha is so dependent on copper and the international markets that we cannot do anything to stop the slide...every time the central bank buys kwacha with dollars the currency falls to the same level two days later...there are no short-term intervention plans."⁴²

While the currency may be able to recover some of its position in the long term, the short-term economic effect is damaging, particularly on small import/export companies. The owner and director of a small company that buys goods in **South Africa** for resale in Zambia said:

"My volume of sales has drastically reduced...I have temporarily suspended the purchase of some of my goods and monitor the money market to see when the currency improves and I can restart that part of my business."⁴³

Power deficit increases to 985MW

Mines and energy minister Christopher Yaluma said that Zambia's power deficit increased from 560MW to 985MW between March and September.⁴⁴ This is in line with government predictions that the September-November hot season would drive up demand prior to the start of the rainy season in November (see *ARC Briefing Zambia August 2015*). The **Zambia Electricity Supply Corp (Zesco)** will reach the total of its allocated water capacity for 2015 in mid-October. This does not mean that reservoirs will run dry, but that hydro generation will tap into Zambia's emergency water reserves.⁴⁵ When water drops in key reservoirs below minimum operating levels, Zesco is supposed to cease generation entirely. Current Zesco projects for 2015 show levels at the key **Kariba Dam** falling to 477 metres, 1.5m above the minimum level.⁴⁶

Zambians who are able to afford it, have invested in diesel generators. Much of the continued business across the country is due to the relative cheapness of the fuel.⁴⁷ Most households experience load shedding power cuts at least once a day, often in the early evenings when demand peaks.⁴⁸ On the macro-economic level the reduction of power to copper mines has already contributed to Glencore's decision to close the Mopani mine (see above). If generation levels fall further, \$140m of government revenue (out of a projected \$202m) from the copper sector is at risk.⁴⁹

The government has implemented a fast-tracked power development programme involving coal and solar generation projects (see *ARC Briefing Zambia July and August 2015*). However, underlying the crisis are decades of poor investment in the power sector. According to **Chrispin Mphuka**, president of the **Economic Association of Zambia**:

*"Organisations like the **World Bank** have been advising for a long time that there would be a potential power deficit and it was important to start investing in this area...from two or three decades ago, this has been on the agenda but there has been a lack of political will."⁵⁰*

⁴¹ State House Press Statement, 5 Sep 2015 and Bank of Zambia Governor Press Briefing, 10 Sep 2015.

⁴² Source, finance ministry, Lusaka

⁴³ Source, small business owner, Lusaka

⁴⁴ Lusaka Voice, 22 Sep 2015.

⁴⁵ Lusaka Times, 7 Sep 2015.

⁴⁶ Lusaka Voice, 22 Sep 2015.

⁴⁷ Business Day, 21 Sep 2015.

⁴⁸ Business Day, 21 Sep 2015.

⁴⁹ Lusaka Times, 7 Sep 2015.

⁵⁰ Mphuka quoted in Guardian, 18 Sep 2015.

Lack of spending affects not only generation but also maintenance. The 600MW Kariba Dam is in urgent need of repairs. The **Zambezi River Authority (ZRA)**, which operates the dam, signed a \$300m repair contract in February but has put it on hold to keep the dam running at capacity.⁵¹ The dam risks collapse, which could unleash a tidal wave through the **Zambezi Valley** up to the **Mozambique** border.⁵² The poor maintenance of Kariba and other hydro facilities reduces their generation capacity and efficiency, leaching up to an estimated 100MW of power from the grid in leaks and damaged turbines.⁵³

Implications

Zambia's copper mines are victims of a global downturn in commodities prices, but the complexities of doing business in the country ensured that international companies cut operations there and not elsewhere. There is little the government can do about this as the actions needed to stop the power crisis should have started decades ago. The willingness of Lungu's government to bring union leaders and mining companies around the table has not only reduced job losses (if only by 500) but has also negated any threat of widespread industrial action which could further harm the sector. Rumours that Glencore will close Mopani for good are unfounded – demand for copper may be down for now but as long as electrical wiring is made of copper, it will bounce back.

The BoZ and the presidency are partly correct – intervention in the foreign exchange markets by central banks across Africa has not halted currency slides. However, blaming the problem solely on external factors and failing to act does not increase market confidence – another key factor in currency value. Keeping the deficit under control, and addressing the power crisis (see below) could help mitigate the slide. Unfortunately the wider forces pushing down currencies across the continent remain dominant – the kwacha is likely to devalue further across the final quarter of 2015.

The power crisis underlies much of Zambia's economic difficulty and the government is only beginning to take the requisite action to resolve it. Rushing independent power projects onto the grid will not prevent the problem from repeating next year. The transmission and distribution infrastructure of the country requires a comprehensive overhaul. When work begins on Kariba, it will be partly out of commission for three years – leaving a 200MW generation gap that the new power stations will have to cover. It is also unlikely that the government will increase its allocation of domestic price electricity to copper mines until it has stabilised supply. Electricity supply will pose an economic challenge to companies operating in Zambia for the medium term.

⁵¹ Lusaka Times, 7 Sep 2015.

⁵² Lusaka Times, 7 Sep 2015.

⁵³ Lusaka Times, 7 Sep 2015.

About Africa Risk Consulting:

Africa Risk Consulting (ARC) is a pan-African consulting company that provides timely, relevant information and advice that enables its clients to take informed investment decisions and to safeguard their reputations.

ARC's core consulting services include integrity due diligence and corporate investigations, political advisory and country assessments, opportunity monitoring and reputation risk management. Most relevant to private equity firms is ARC's integrity due diligence and corporate investigations capability. Specifically, ARC offers pre-deal integrity checks to highlight red flags before negotiations start; full detailed multi-jurisdictional reputation due diligence; and supplier and senior hire vetting and repeat due diligence for compliance programmes. ARC is unique in that it offers a 10-day delivery for a routine integrity due diligence. ARC also offers a suite of corporate investigations services from immediate investigation, evidence gathering, e-discovery, forensic accounting and whistleblower support on one end to crisis media management and regular monitoring on the other.

www.africariskconsulting.com

About ARC Briefing:

ARC Briefing is ARC's essential online business information service.

Companies at any stage in their Africa expansion, whether building or communicating an Africa strategy, investing directly, expanding current operations, financing other investors, doing the legal leg-work or researching the Africa growth trend, need ARC Briefing.

ARC Briefing is an online information service keeping you:

- Up to date with Country Chronologies of business-critical events
- In the know via Country Briefings on political, economic, business and operating trends. Written in-country, ARC experts analyse and comment
- Ahead with Country Planner which details future elections, budgets, regulatory changes etc.

www.briefing.africariskconsulting.com

Getting in touch

Please contact us by email info@africariskconsulting.com or call + 44 (0) 20 7078 4080

Follow us on Twitter: [@ARCBriefing](https://twitter.com/ARCBriefing)