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July 2017

2017 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR ZIMBABWE

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2017 Article IV consultation with Zimbabwe, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its July 5, 2017 consideration of the staff report that concluded the Article IV consultation with Zimbabwe.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on July 5, 2017, following discussions that ended on May 13, 2017, with the officials of Zimbabwe on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on June 19, 2017.
- An **Informational Annex** prepared by the IMF staff.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and the International Development Association (IDA).
- A **Statement by the Executive Director** for Zimbabwe.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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IMF Executive Board Concludes 2017 Article IV Consultation with Zimbabwe

On July 5, 2017, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Zimbabwe.

Zimbabwe's economy is facing difficulties. A severe drought and slow reform momentum have led to high expenditure levels since late 2015 despite subdued revenues. With limited access to foreign inflows, the ensuing fiscal imbalances have become unsustainable, and are being financed by rising domestic borrowing. The expansionary fiscal stance, curtailed net capital flows, and declining investor confidence have resulted in cash shortages. In response the government has introduced capital and current account controls and quasi-currency instruments in the dollarized economy. An overvalued real exchange rate is hurting external competitiveness.

Budgetary operations are crowding out the private sector, and the expenditure profile tilted towards employment costs and unsustainable agricultural support is inhibiting investments in other priority sectors, particularly infrastructure and social outlays. On the financial side, credit to the private sector remains subdued, and some domestic banks face increasing risks emanating from fiscal imbalances.

Some progress on advancing structural reforms, notably to improve the business climate, has been made. However, progress on implementation of laws applicable to non-indigenous investors, improvements in the functioning of state-owned enterprises, and upgrades in public financial management, governance and accountability remain limited.

The envisaged reengagement with the international community is facing delays. The Zimbabwean government has settled all overdue obligations to the PRGT. However, it is yet to reach agreement with the World Bank and other multilateral institutions on the settlement of arrears, and undertake reforms that would facilitate resolution of arrears with bilateral creditors.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

Growth this year is expected to be supported by a strong performance in agriculture mainly due to exceptional rains. However, economic activity in the medium term is projected to remain subdued, pending adjustment and reform that tackle the structural challenges and enable the economy to restore fiscal and external sustainability and achieve its growth potential.

Executive Board Assessment[2]

Directors stressed the urgency of fiscal consolidation to restore policy credibility and economic stability. They noted that public sector employment costs remain at an unsustainable level, constraining social and infrastructure spending. Directors encouraged the authorities to engage only in well-targeted, cost effective, and properly budgeted support to the agricultural and other productive sectors. They noted the potential to enhance tax revenues, and highlighted the need to strengthen public financial management and reform state-owned enterprises.

Directors stressed the need to contain broader, adverse spillovers from the fiscal imbalances. The ongoing deficit financing modalities, particularly the credit from the central bank, are unsustainable and have significant potential for generating inflationary pressures. The marked increase in public debt is crowding out private sector activity, aggravating liquidity shortages, and exacerbating debt distress. The dollar scarcity has led to administrative controls on current and capital account transactions. Directors noted that unless adjustment and reforms are forthcoming, these conditions would further undermine economic performance and weaken confidence.

Directors underscored the need to restore credibility of the currency regime and safeguard the financial sector. Even as private sector credit growth remains subdued, bank asset concentration on non-liquid central bank deposits and treasury bills has increased financial sector fragility. The extensive use of quasi-currency instruments exacerbates this fragility. Directors encouraged a proactive approach to managing these risks, including by bolstering the regulatory and supervisory framework, and closing loopholes in the AML/CFT framework. Directors also encouraged the authorities to roll back exchange controls.

Directors stressed the urgency of structural reforms and the need to create a conducive environment for private-sector-led growth. They welcomed efforts to improve the business climate, but called for comprehensive actions to provide a level playing field for investors through consistent and transparent implementation of laws, and measures to combat corruption.

Directors welcomed Zimbabwe’s clearance of arrears to the IMF and encouraged an early resolution of arrears to other IFIs and bilateral creditors. Determined reform implementation and

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

reengagement with the international community are key to unlocking external financing, fostering investment, and resolving the debt overhang. Directors cautioned against clearing arrears using modalities which exacerbate debt problems. They emphasized that Zimbabwe needs the support of the international community to achieve sustainability.

Table 1. Zimbabwe: Selected Economic Indicators, 2013–16

	2013	2014	2015	2016 Est.
Output				
Real GDP Growth (annual percentage change)	5.3	2.8	1.4	0.7
Nominal GDP (US$ millions)	15,224	15,834	16,072	16,124
GDP deflator (annual percentage change)	2.9	1.2	0.1	-0.3
Inflation (annual percentage change)				
Consumer price index (annual average)	1.6	-0.2	-2.4	-1.6
Consumer price index (end-of-period)	0.3	-0.8	-2.5	-0.9
Central government (percent of GDP)				
Revenue and grants	24.6	23.8	23.3	21.7
Expenditure and net lending	26.7	25.4	25.9	30.8
Overall balance (cash basis)	-1.9	-0.9	-2.4	-8.8
Money and credit (US$ millions)				
Broad money (M3)	3,888	4,377	4,736	5,638
Net foreign assets	-730	-693	-628	-556
Net domestic assets	5,100	5,367	5,611	6,292
Money and credit (annual percentage change)				
Domestic credit (net)	6.2	4.2	8.8	19.8
Of which: Credit to the private sector	3.7	4.7	-2.3	-3.6
Balance of payments (US$ millions)				
Current account balance	-2,375	-2,395	-1,495	-662
(percent of GDP)	-15.6	-15.1	-9.3	-4.1
Official reserves (end-of-period)				
Gross international reserves (US$ millions)	284	303	339	310
(months of imports of goods and services)	0.4	0.5	0.6	0.6
Debt (end-of-period)				
Domestic debt (US$ millions)	479	1,764	2,281	4,006
(percent of GDP)	3.1	11.1	14.2	24.8
PPG external debt (US$ millions)	5,389	6,407	6,613	7,231
(percent of GDP)	35.4	40.5	41.1	44.8

Sources: Zimbabwean authorities and IMF staff estimates.

INTERNATIONAL MONETARY FUND

ZIMBABWE

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION

June 19, 2017

KEY ISSUES

Context. In the 1990s, Zimbabwe was one of the most developed economies in Africa. While many of the country's underlying strengths remain, some of its industrial and agricultural base has since eroded. The nominally dollarized economy now faces difficulties as diminishing net capital flows and an expansionary fiscal stance have generated an acute cash shortage that has prompted the use of quasi-currency instruments amid imposition of controls over capital and current account transactions. With reengagement with creditors delayed, access to external financing is limited, and the fiscal deficit is being financed by domestic borrowing at an unsustainable pace.

Outlook and Risks. The fiscal impulse and a recovery in agriculture following favorable rainfall after last year's drought will support moderate growth in 2017. However, financing constraints and declining confidence are likely to result in stagnant economic activity in the medium term. Inflation will likely increase as monetary financing of the deficit raises the premium on U.S. dollars against the quasi-currency instruments. Political polarization is undermining the prospects for fiscal consolidation and reform, imperiling financial sector and external stability. Debt-financed government interventions to ramp up production are exacerbating vulnerabilities.

Key Policies. The authorities are encouraged to urgently build consensus around a comprehensive package of reforms. Fiscal consolidation—notably, a rationalization of the high employment costs and the expensive agricultural initiatives—must be at the center of this package. Deep structural reforms—including measures to increase transparency in the mining sector, support property rights, and reduce fears of expropriation—are necessary to boost growth amid the fiscal contraction. Early success in reform could in turn allow for a gradual removal of the exchange controls and repair of bank balance sheets. Strong policies would also pave the way for a successful reengagement with the international community.

Approved By
Anne-Marie Gulde-Wolf (AFR) and Zeine Zeidane (SPR)

Discussions took place in Zimbabwe from May 3–12, 2017. The staff team comprised Ms. Coronel (head), Mr. Thornton and Mr. Thakoor (all AFR), and Ms. Jung (SPR). Mr. Beddies (Resident Representative) and Ms. Chishawa (local economist) assisted the mission. Mr. Nakunyada (Advisor to Executive Director) attended key discussions. The mission met with the Chief Secretary to the President, Mr. Sibanda, the Minister of Finance and Economic Development, Mr. Chinamasa, the Governor of the Reserve Bank, Dr. Mangudya, other senior government officials, members of parliament, representatives of the private sector, civil society and development partners.

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CONTEXT AND RECENT ECONOMIC DEVELOPMENTS

A. Background

1. **The Zimbabwean economy, once among the most advanced in sub-Saharan Africa, has become one of its most vulnerable, but some pillars of its strong foundation remain**. In 1980, GDP per capita in Zimbabwe was higher than in most of its neighbors; manufacturing accounted for a large share of GDP; and the quality of health and education services was high. However, the country was also characterized by social and economic inequalities. While Zimbabwe has made some progress on social indicators, much of the economic base has eroded (Figure 1). The land reform since the late 1990s saw agricultural production plummet and productivity decline, while excessive fiscal deficits led to external payment arrears. Following the economic downturn, a substantial part of the skilled workforce emigrated. Despite the challenges, a vibrant private sector and a growing informal economy have demonstrated surprising resilience—a testament to Zimbabwe's solid infrastructure and human capital.

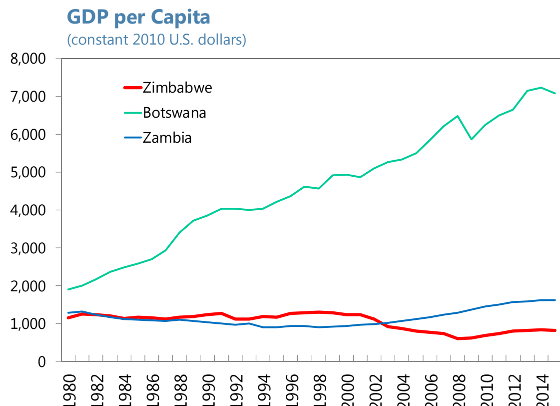
2. **The 2008–09 hyperinflation led to the abandonment of the Zimbabwean dollar.** As the domestic currency lost value following one of the worst inflation episodes in modern history, Zimbabwe moved to a multi-currency system in early 2009, with the U.S. dollar, the rand, and other international currencies becoming legal tender. As the U.S. dollar strengthened against the rand in the mid-2010s, it came to dominate. The absence of a domestic currency anchored prices and helped improve policy credibility, but the regime was imperfect from the start, as the net external and fiscal positions were negative, the Reserve Bank of Zimbabwe (RBZ) was not adequately capitalized, the financial sector was weak, and liquid assets were scarce.

3. **Insufficient policy adjustment, structural rigidities, and exogenous shocks drove an overvaluation of the real exchange rate and the consequent decline in competitiveness.** In the absence of monetary policy, wage policy was not sufficiently flexible to respond to shocks, driving an expansionary fiscal stance. High public-sector wages, in turn, were reflected in other wages and prices, which became sticky downwards. Structural and governance weaknesses made provision of public goods expensive. With weather-related shocks and nominal exchange rate depreciations in key trading partners, the current account deficit remained high, reserves were nearly depleted, and external competitiveness suffered. Subsequently, the multi-currency system became unsustainable, resulting in the introduction of three quasi-currency instruments to meet the demand for transactions: small denomination currency notes, electronic balances, and T-bills.

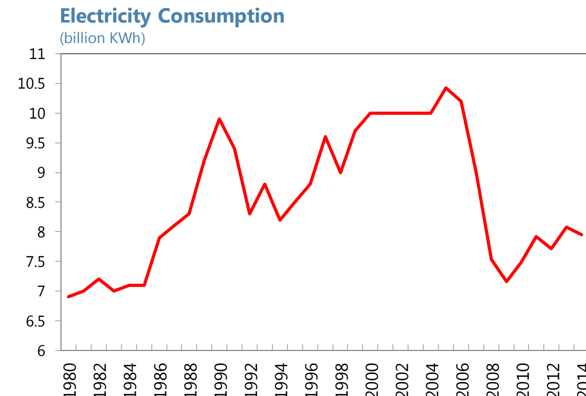
4. **With economic imbalances not fully addressed and creditor concerns over political issues and human rights, Zimbabwe has remained isolated.** Zimbabwe's large external arrears, including to multilateral institutions, have limited access to financing and increased the country's international isolation. Attempts to reengage with the international community culminated in the Lima process—a strategy to repay and refinance arrears—but progress on moving this plan forward has been slower than anticipated. Some countries have maintained sanctions over issues related to democracy and human rights. Concerns about governance and corruption have not dissipated.

Figure 1. Evolution of Selected Indicators

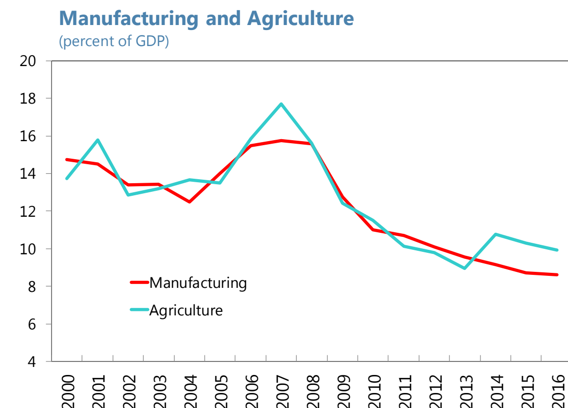
GDP per capita has shrunk by a third since the 1980s.



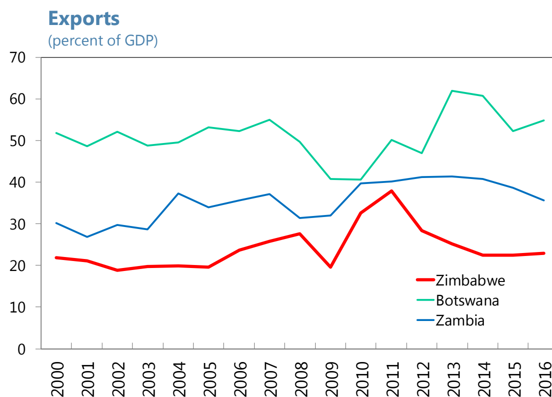
Electricity consumption is only recovering gradually.



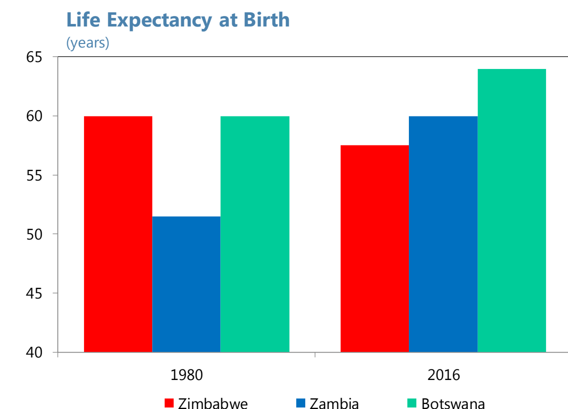
The contribution of agriculture and manufacturing to GDP has declined.



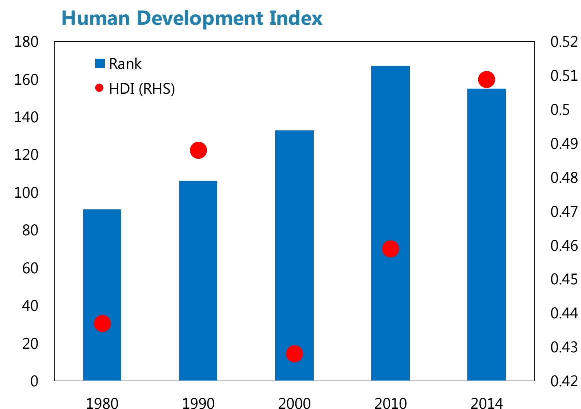
Exports have stagnated at low levels.



Life expectancy has declined in contrast to neighboring countries.



Notwithstanding the improvement in human development, Zimbabwe's ranking has deteriorated.



Sources: Zimbabwean authorities, International Energy Agency, and IMF staff calculations.

B. Recent Developments

5. The reform agenda, underpinned by two successive IMF staff monitored programs, aimed at addressing the imbalances, but was constrained by political circumstances. Prospects for reengaging with the international community initially gave the economic team leverage to contain spending pressures and articulate a reform strategy. However, implementation of the reforms described in the last Article IV consultation report—aimed at fostering expenditure discipline, strengthening transparency in the mining sector, improving the business environment, restoring confidence in the financial sector, and clarifying the indigenization policy to encourage investment—was delayed (Box 1). Investor confidence, already dented by economic policies, has been further undermined by the country's uncertain political prospects.

Box 1. Implementation of IMF Policy Advice

Fiscal policy. While there was technical support for the measures recommended by the Fund to achieve fiscal discipline, particularly by reducing employment costs, improving tax administration, and accelerating reforms of state-owned enterprises (SOEs), the advice to target a broadly balanced fiscal position was missed by a large margin due to expenditure overruns only partly explained by exogenous shocks.

Financial soundness. The swelling fiscal deficit also undermined implementation of Fund advice on financial sector soundness (strengthening bank risk management), as the issuance of large amounts of public debt reduced the availability of credit to the private sector, and undid the progress made in strengthening confidence. While Fund advice on the resolution of non-performing loans (NPLs) was carried out, the implementation resulted in higher debt than anticipated.

Structural reforms. Progress was made in clarifying the indigenization policy (aimed at increasing the participation of indigenous Zimbabweans in the economy); improving the use of land leases to support lending; and establishing a one-stop shop window for investors. However, the reform program was not fully implemented, with a perception among stakeholders that much progress is needed to tackle corruption and improve the business climate.

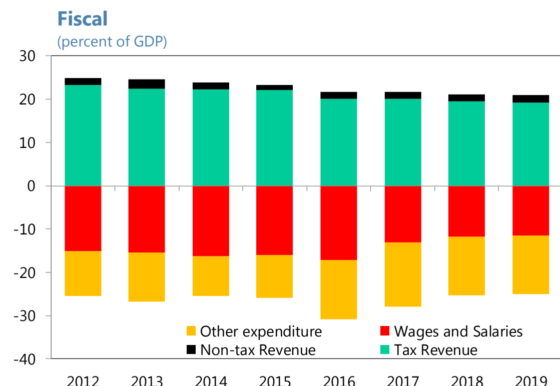
6. A large domestically-financed fiscal deficit left the private sector with scarce resources to operate. With weak economic activity in 2016, annual revenues fell by 6 percent in nominal terms, but government spending increased, exacerbating emerging liquidity shortages. Payment of the (unbudgeted) 13th month salary raised employment costs (including pensions and the portion of transfers relating to salaries) to over 90 percent of total revenues, and the overall deficit reached 9 percent of GDP (Figure 2). About 4 percent of GDP was spent on agricultural support.[1] While this intervention included drought-related grain purchases to ensure food security, it also involved costly provision of inputs to farmers and assistance to the agricultural marketing board. As financing needs exceeded the private sector's T-bill absorption capacity, the government used an overdraft from the RBZ, exerting additional pressure on the balance of payments.[2] At end-2016, domestic debt was almost 25 percent of GDP (14 percent in 2015).

[1] The authorities classify agricultural support as capital spending, though the bulk of it might be considered transfers.

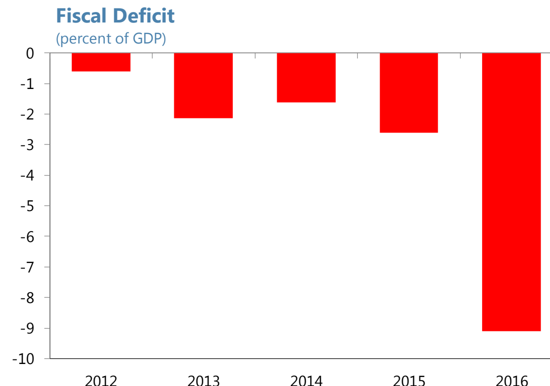
[2] The overdraft, legally limited to 20 percent of the previous year's revenue, exceeded 25 percent in 2016. It reached a level equivalent to 7 percent of GDP, notwithstanding the dollarized economy.

Figure 2. Fiscal Challenges

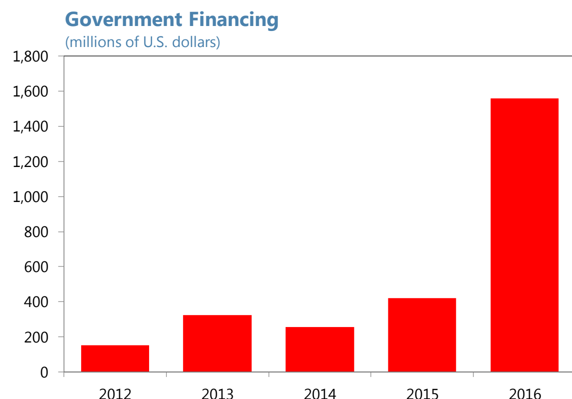
An increasing wage bill and declining revenues…



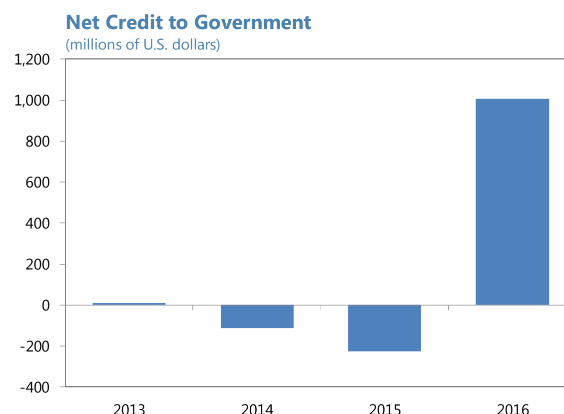
…are contributing to a worsening fiscal position…



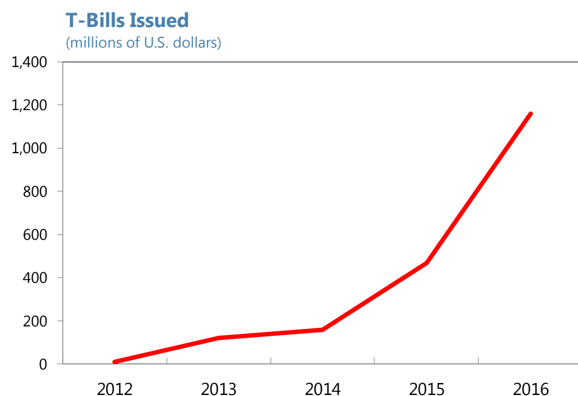
…and increasing government financing needs.



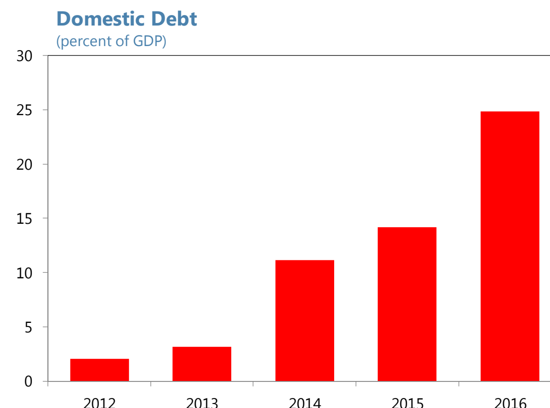
Financing needs are met by an overdraft from the RBZ…



…and increased issuance of T-Bills…



…resulting in higher domestic debt.



Sources: Zimbabwean authorities and IMF staff calculations.

7. Exogenous factors also contributed to the deterioration of economic and social conditions. With key export prices depressed, falling FDI, and rand-based remittances declining in U.S. dollar terms, the external position weakened. The diminishing interest in doing business with Zimbabwe and the withdrawal of correspondent banking relationships further compounded the situation, by jeopardizing companies' foreign payments and increasing their transaction costs. Moreover, the El-Niño induced drought resulted in the lowest maize harvest in 25 years, contributing to worsening food insecurity and social indicators.[3] With limited private or official external financing forcing a compression of trade, the external position remains precarious. International reserves cover only two weeks of imports.

8. The reengagement process is facing severe headwinds (Box 2). In late 2016, Zimbabwe cleared its arrears to the Poverty Reduction and Growth Trust (PRGT), and the IMF Executive Board removed the remedial measures applied to Zimbabwe resulting from the overdue obligations. However, the expected bilateral loan to clear arrears to the World Bank Group did not materialize, and led the authorities to seek an alternative package from commercial lenders. Inadequate progress on reforms is undermining the prospects for new external financing, while insufficient assurances of new financing is weakening the incentives for reform. In the absence of debt relief, Zimbabwe is in debt distress (see accompanying Debt Sustainability Analysis).

Box 2. Reengagement with the International Community

Planned simultaneous repayment modalities. The 2015 Lima process, which received support from creditors and development partners, envisaged clearing arrears to the IMF using the SDR holdings, to the IBRD with a bridge loan from a bilateral creditor, to IDA drawing on a turnaround facility, and to the AfDB with the AfDB Pillar II Trust Fund set up for countries' arrears clearance.[1]

Payment to the PRGT. After the bilateral loan to clear the World Bank arrears and the IDA turnaround facility failed to materialize, Zimbabwe proposed a sequential approach. It fully settled overdue obligations to the IMF's PRGT in October 2016. This allowed the IMF's Executive Board to lift the declaration of noncooperation, ineligibility to access PRGT, and restriction on technical assistance, in November 2016. Access to IMF resources, however, requires that Zimbabwe comply with other applicable IMF policies, including having a credible plan to: (i) resolve arrears with official creditors, and engage with external private creditors (if any); and (ii) implement strong fiscal adjustment and structural reforms to restore fiscal and debt sustainability and foster private sector development.

Clearing the World Bank arrears. The authorities view market resources, an option with costlier financial terms, as the only alternative to clear World Bank arrears in the absence of official support. They are willing to collateralize gold proceeds to settle these obligations, and pave the way for regularization of arrears with other creditors.

The road ahead. There are concerns over the sustainability of relying on market resources to repay the World Bank obligations, which are currently not being serviced. Additionally, collateralizing gold proceeds could complicate future debt relief. The key question is the timing and quantity of new financing that the arrears clearance could unlock. Assessing this matter has proved challenging amid uncertainties over the strength of policies to restore sustainability and the appetite for support at the Paris Club.

[1] See "Strategy for Clearing External Arrears and Supportive Economic Reform Measures" at www.rbz.co.zw.

[3] The number of Zimbabweans in extreme poverty increased by 200,000 to 2.8 million in 2016 (World Bank).

C. Managing the Dollar Shortages

9. Delayed fiscal adjustment led to RBZ financing of the budget deficit and prompted the use of quasi-currency instruments. The RBZ's overdraft facility, in the absence of sufficient cash reserves, set in motion the creation of money in the nominally dollarized economy. Government entities spend the borrowed funds by crediting bank accounts of the payment recipients (employees, suppliers, contractors) through the real time gross settlements (RTGS) electronic system. These transactions increase deposits in the banking system, but without a concomitant increase in the quantity of U.S. dollars available in cash or external (nostro) accounts. To finance the remainder of the deficit, the government issued T-bills, mainly acquired by commercial banks but also used as payment for services. Moreover, to provide cash for small transactions, in November 2016 the RBZ started issuing $2 and $5 denominated "bond notes" at parity with the U.S. dollar—nominally in the form of incentives of up to 5 percent of exports deposited in exporters' accounts.

10. An increase in the demand for cash, in the context of U.S. dollar shortages, prompted the authorities to adopt current and capital account controls. To curb imports and deposit withdrawals, the authorities have imposed administrative measures since May 2016 to allocate foreign exchange on the basis of import priorities, and implemented new limits and controls on imports (Statutory Instrument 64). They concurrently introduced total or partial export repatriation, which in practice meant the exchange of U.S. dollars for RTGS electronic balances. The authorities also encouraged the use of credit and debit cards for transactions, and imposed deposit withdrawal ceilings, which have been gradually lowered and now left to banks' discretion (in some cases as low as $20 per day). These withdrawals are mainly occurring in the form of bond notes. By end-May, around $140 million (20 percent of currency in circulation), out of a planned $200 million had been issued.[4] Finally, the authorities imposed lending rate ceilings to cap the cost of credit.

11. The implementation of the priority list for allocating foreign exchange gives rise to an exchange restriction subject to Fund approval under Article VIII, Section 2(a). In May 2016, the RBZ released a foreign exchange priority list to direct the allocation of foreign exchange by commercial banks to certain domestic import substitution industries, exporters, and strategic imports. Market participants not on the priority list face significant challenges and long waiting times to access foreign exchange for current international transactions, and private sector external payment arrears have emerged.[5]

12. The use of bond notes and RTGS electronic balances, officially at par with the U.S. dollar amid capital flow controls, is giving rise to a parallel market. The administrative measures reduced the pace of economic transactions (real GDP growth is estimated at 0.7 percent in 2016)[6], at the cost of driving US dollars out of circulation. With bond notes and electronic balances utilized for the bulk of

[4] While no official survey has been undertaken, US dollars in circulation is estimated at around $600–800 million.

[5] Staff is monitoring the authorities' imposition of other measures to assess whether they give rise to any exchange restriction or multiple currency practice subject to Article VIII, Section 2(a) and Section 3.

[6] The GDP series were revised upwards in early 2017 as national accounts coverage was expanded.

payments, and T-bills for a few others, U.S. dollars are used for international operations and hoarded as a store of value outside the formal banking system. The expanding informal sector functions using cash to finance imports that reportedly evade government controls and customs. In the parallel market, bond notes are trading at a 5 to 7 percent discount *vis-à-vis* the U.S. dollar, and electronic balances reportedly exchange at a 15 to 20 percent discount.[7] Combined with the trade controls, the discounts have led to an uptick in inflation, which has increased to a quarterly annualized rate of 3.4 percent in March 2017 (compared to 0.7 percent in December 2016).

ECONOMIC OUTLOOK AND RISKS

A. Short-Term Outlook

13. Aided by the rebound in agriculture, growth is expected to pick up in 2017 in an environment of rising inflation and a narrowing current account deficit (Figure 3). Following the drought in 2015–16, staff estimates that the strong harvest on the back of a good rainfall season, favorable prospects for gold, chrome and tobacco exports, and lower demand for imported food, could allow real GDP to grow by 2.5–3.0 percent in 2017. The authorities are more optimistic in their projections (3.7 percent) as they expect higher growth in manufacturing and services. Staff argued that insufficient liquidity will continue to hamper imports and affordable financing, encumbering growth prospects. Inflation and inflation expectations will rise in line with money creation and increasing import prices due to the controls. Annual average inflation is set to be 2–3 percent, which implies an increase to about 7 percent by year-end. The external current account deficit is projected to continue to narrow to about 3¾ percent of GDP (from an average of 13¼ percent in 2012–15), still affected by diminished imports.

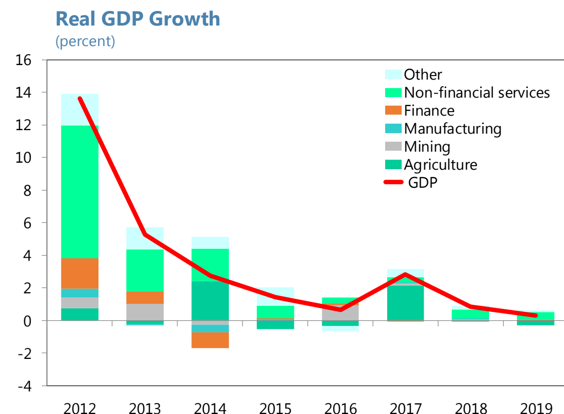
B. Medium-Term Outlook

14. Reform and reengagement constitute the optimal scenario, but require strong efforts by the authorities and reciprocal support by the international community. There is widespread understanding among policymakers of the benefits of fiscal consolidation and structural reform. Should these proceed along the lines presented in Fund policy advice, the economy's potential is huge (Scenario A, Table 5). Physical infrastructure is adequate; human capital is high; and agriculture, mining, and industry have substantial underutilized capacity and offer significant opportunities for domestic value addition. Structural reforms to attract investment could support growth, notwithstanding the necessary fiscal contraction. Moreover, political and governance reforms, including on human and property rights, could support the reengagement objective, thereby facilitating debt treatment and unlocking financial support, both essential lubricants of economic recovery.

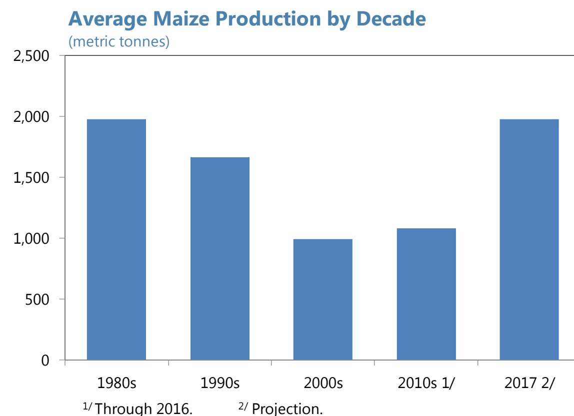
[7] There are no official statistics on these discounts. The Old Mutual Implied Rate, which compares prices between the LSE share price in sterling to the ZSE share price in (Zimbabwe) U.S. dollars estimates that the intrinsic value of the dollar in Zimbabwe is 50 percent lower than the US dollar.

Figure 3. Economic Prospects

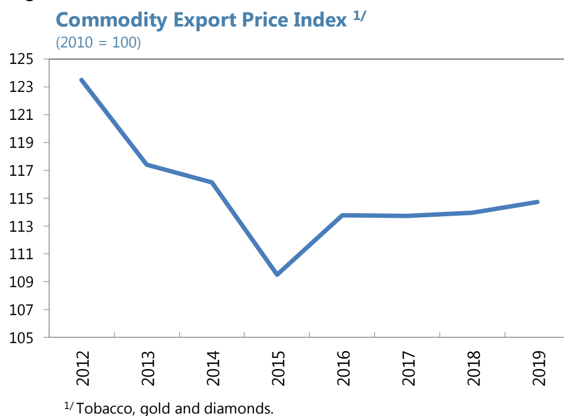
Absent reforms and reengagement, growth prospects remain subdued…



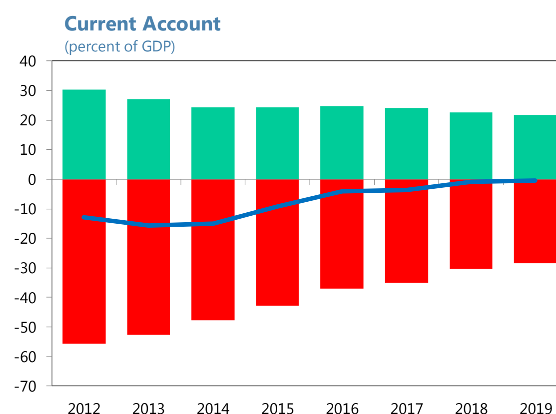
…notwithstanding the boost from a bumper maize crop in 2017.



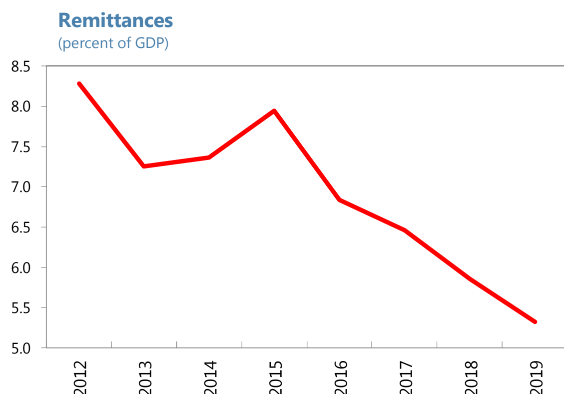
With export prices expected to remain below previous highs…



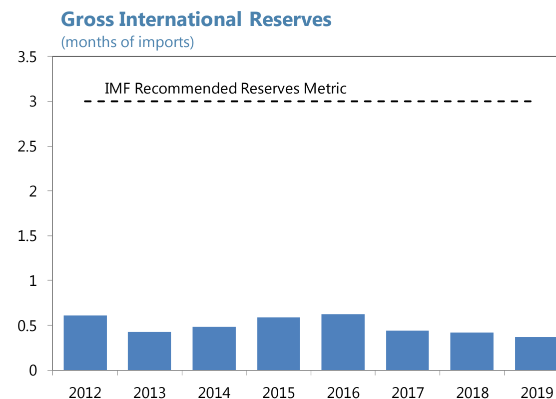
…import compression will contribute to a narrowing of the current account deficit.



Official remittances are expected to decline reflecting the weak rand and increasing informalization.



International reserves are projected to remain low.



Sources: Zimbabwean authorities and IMF staff calculations.

15. The downside risks are substantial and their negative impact is high, particularly for inflation. Should the authorities prove unable to restrain fiscal spending, or additional exogenous shocks arise, the *status quo* could prove very fragile (Scenario B, Table 5). With its link to the U.S. dollar increasingly tenuous and lacking a strong anchor, confidence in the domestic monetary system could weaken rapidly. The government would have to finance the deficits by expanding the RBZ overdraft, issuing T-bills, and supplying bond notes at an increasingly high cost. This would lead to rapidly rising inflation, growing shortages of foreign exchange and imported goods, and increasing discounts of the quasi-currency instruments. The deteriorating situation would exert a heavier toll on the most vulnerable, and the resulting growth slowdown and collapse in confidence could lead to financial sector distress and social tensions.

16. A baseline scenario based on current policies would involve a delayed fiscal consolidation. This scenario assumes some expenditure restraint—including by continuing the current wage and hiring freeze, and cutting capital spending over the medium term—but insufficient consolidation to address macroeconomic imbalances and generate growth. Fiscal deficits would continue at a higher than optimal level, which will still force some monetary financing, but the authorities, conscious of the risks of hyperinflation, will restrain the issuance of bond notes. The consequent rise in inflation would have an impact on real wages, thereby restraining the deficit-to-GDP ratio. With an overappreciated real exchange rate, U.S. dollars would become increasingly scarce or only be available at a premium. The RBZ would likely intensify administrative controls to try to enforce parity and ensure that the banking system continues to contribute to deficit financing. Even if such a scenario avoids rapidly accelerating inflation, it would result in accentuated economic distortions, deteriorating macro-financial and external imbalances, and growth stagnation over the medium term. Nonetheless, the informal economy could continue to find ways of dealing with the cash scarcity and the controls.

Zimbabwe: Baseline Economic Indicators, 2017–22

	Prel.	Projections					
	2016	2017	2018	2019	2020	2021	2022
Real GDP growth (annual percentage change)	0.7	2.8	0.8	0.3	-0.3	-0.7	-0.9
Nominal GDP (US$ millions)	16,124	17,105	18,904	20,601	21,434	22,218	22,877
Consumer price inflation (annual average)	-1.6	2.5	9.5	8.3	4.0	4.0	4.0
Central government (percent of GDP)							
Revenue and grants	21.7	21.7	21.1	20.9	20.7	20.6	20.5
Expenditure and net lending	30.8	28.0	25.4	25.0	24.7	24.7	24.7
Overall balance (cash basis)	-8.8	-5.9	-4.3	-4.1	-4.1	-4.1	-4.0
Financing		5.9	4.3	4.1	4.1	4.1	4.0
Of which RBZ overdraft		1.2	1.6	0.5	0.5	0.5	0.4
Current account balance (excluding official transfers)	-662	-617	-159	-79	-211	-370	-439
Gross international reserve (months of imports of G&S)	0.6	0.4	0.4	0.4	0.3	0.3	0.3
Domestic debt (percent of GDP)	24.8	28.2	30.1	32.0	34.9	37.7	40.6
External debt (percent of GDP)	44.8	42.4	38.3	35.0	33.5	32.2	31.3

17. The authorities concurred with staff's assessment of the potential risks. However, they stressed the constraints under which they were operating—including high country risk premium and intense political polarization. They argued that the country's isolation calls for a gradual pace of reform. In response, staff stressed Zimbabwe's vulnerabilities to external shocks despite its isolation—including further dollar appreciation, the slowdown in China, and possible protectionist policies in advanced economies (Annex I). Recent climate-induced shocks have also emphasized the need for policy buffers and adaptation/mitigation measures (Annex II).

POLICY DISCUSSIONS

18. Policy discussions centered on the need for strong fiscal and structural reforms that could restore domestic and external equilibria. Staff argued that sound policies could unleash the potential of the Zimbabwean economy, thereby attaining the optimal scenario (Scenario A, Table 5). In the absence of policy buffers, there is an urgent need to transform the current productive structure—oriented to the domestic market and dependent on government spending—into one that encourages private investment and exports.

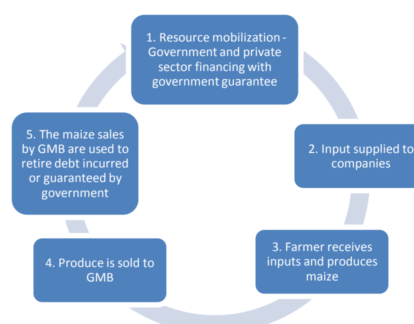
A. Achieving Fiscal Restraint

19. The 2017 budget target—an overall deficit of around $2^{1}/_{3}$ percent of GDP—proved overly optimistic. Envisaged revenue measures extending VAT to food items were partially reversed, and expenditure cuts proved impossible to implement. A Finance Ministry proposal to restrain the wage bill was rejected by cabinet.[8] A further suggestion to pay the 13th salary in land rather than currency failed following a strike by teachers and health care workers. The authorities are also expanding their agricultural support programs at a high cost (Box 3). Additional pressures stem from the need to capitalize the asset management company, ZAMCO, and other failing SOEs. With the need for food imports reduced, the deficit is expected to be around 6 percent of GDP, financed by the issuance of a bond by the social security agency, and a potential loan from commercial lenders at market terms.

Box 3. Command Agriculture Program

Public resources to encourage production. Production of maize, the main staple, has been on a declining trend because of insufficient investment mainly due to unresolved land tenure, reduced productivity, and a shift to cash crops. The situation was exacerbated by the 2015/16 drought, which forced the authorities to import $250 million worth of maize. In the absence of other sources of financing, the government felt the need to borrow domestically to support production of maize and other products.

Loans in exchange of production. Under the scheme, farmers are provided with loans to purchase inputs, which they are expected to repay in the form of grain supplied to the Grain Marketing Board (GMB). In addition, the GMB purchases grain from farmers at a fixed price, storing some in the strategic reserve, and selling the surplus at market prices.



Large costs and considerable risk. The government has set the buying price for the GMB at $390 per ton of maize, more than double the current world price, and significantly above the import parity price at which millers have agreed to purchase maize from the GMB. Depending on the loan recovery rates and the prevailing market prices, the cost of the command programs for maize and wheat are likely to be in the range of 2 to 3 percent of GDP by the end of 2017.

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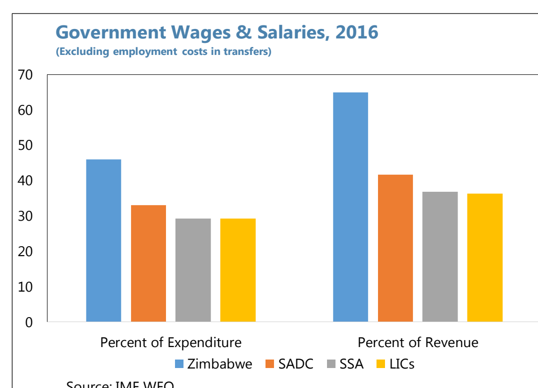
[8] In September 2016, cabinet rejected measures announced by the Finance Minister to reduce employment numbers by 25,000, cut salaries and allowances, and forego bonuses for two years.

20. Fiscal consolidation is the most urgent and critical element for stabilizing the economy. Staff proposed a series of measures aimed at restoring a fiscal surplus over the medium term, noting that persistent large deficits will crowd out private sector investment, exacerbate the external imbalance, and further undermine confidence in the currency regime. Failure to curtail monetary deficit financing could have a rapid and escalating impact on the price level. The authorities agreed that deficits at current levels cannot be sustained, but stressed that the recent increases must be seen in the context of one-off shocks and the country's international isolation. Moreover, they are confident that their efforts to increase production will result in higher revenues, thus alleviating the situation.

21. Given the magnitude of public sector employment costs, fiscal consolidation must encompass ambitious action on wages. Staff noted that a public sector wage bill of around 19 percent of GDP cannot be sustained.[9] The authorities stressed that efforts to freeze salaries and hiring (with exceptions for key priorities) as well as to reduce overlaps and rationalize benefits as suggested by the Public Service Commission audit —are already underway. Staff acknowledged this progress, but suggested bolder measures, such as suspending the 13th salary (1 percent of GDP); and downsizing the civil service, including through eliminating ghost workers, reducing nonessential positions, and compressing the remuneration package, while protecting social priorities (1 to 2 percent of GDP). Viewing these as medium-term measures, the authorities pointed to the political constraints on sharp adjustments in remuneration or employment, given the limited scope for the economy to absorb labor, and the potential need for civil servants to support extended families. Staff acknowledged that civil service reform would require consensus-building, and that technical and—ideally—financial support could make the adjustment easier (Annex III).



22. While supporting the goal of ensuring food security, staff questioned the design and financing of the command agriculture program. The commitment to buy large quantities of grain at above-market prices is not cost-efficient. Staff argued that future agricultural interventions could limit fiscal risks, while meeting the food security and poverty alleviation objectives, and realize savings of around 1–2 percent of GDP lower per year. Preventing the programs becoming a drag on the budget is essential, notably if the government needs to borrow to finance them. Staff referred to other country experiences, which show that private sector participation—for example, by financing the plantation season in return for a guaranteed access to output during the harvest—has been successful, leaving the authorities' interventions to areas such as irrigation, educational programs, and infrastructure. The authorities indicated that they had no choice but to intervene strongly to ensure production and avoid a recurrence of the food shortages. They noted that the support would be reduced over time as production increases.

[9] Including the employment-related component of grants and transfers.

23. Staff and authorities agreed on the potential for increasing government revenues. The authorities indicated that their enforcement actions and measures to reduce zero-rating under VAT appear to be bearing fruit. Staff recommended further measures to buttress revenues by phasing out income tax and capital gains exemptions, and restricting VAT exemptions to those critical to low-income households. Additional action should seek to reduce the administration gaps in transit, export controls and excise taxes, and improve fiscal governance in the mining sector. Staff pointed out that Zimbabwe's revenue-to-GDP ratio is already high for a LIC and by regional standards, suggesting that the potential for further increases may be limited, particularly if the trend toward increasing informalization is not reversed. However, staff estimates that administrative and policy measures, together with broader economic reforms to reduce informalization of the economy, could result in the revenue-to-GDP ratio 3 percentage points higher than in the baseline scenario over the medium-term.

24. Staff also suggested to use the room for efficiencies in other areas. Given that preserving foreign currency is a priority, there are potential savings from foreign travel expenses and nonessential procurement of goods and services, in such areas as the provision of government vehicles. Staff thus recommended a careful review of expenditure outlays.

B. Dealing with Adverse Macro-Financial Linkages

25. The overvaluation of the real exchange rate adversely affected the stability of the dollarized regime. The formal economy uses bond notes, electronic balances, and T-bills as media of exchange; administrative measures as vehicles for liquidity allocation; and U.S. dollars as units of account and store of value. This system coexists with an informal market continuously searching for equilibrium pricing of the quasi-currency instruments. The authorities consider that this is the result of an excessive liberalization of the economy that has driven the foreign exchange "externalization". Staff argued that the expansionary fiscal policy and deteriorating confidence have been at the core of capital outflows and diminished interest in investing in Zimbabwe, and therefore have played a key role in the external position being weaker than implied by fundamentals (Annex IV). While full dollarization has been a mixed experience (Box 4), no currency regime would have gone unscathed without the accompanying international reserves and supporting policies.

26. Fiscal imbalances are raising financial sector vulnerabilities (Figure 4, Annex V). Staff noted that given the heightened sovereign risk and insufficient RBZ reserves to honor its obligations with banks, bank assets in the form of RTGS electronic balances and T-bills pose liquidity and solvency risks. While foreign-owned banks' appetite for T-bills is on the wane, these banks hold a large share of their assets in RTGS electronic balances, as they deal with exporters subject to repatriation. Domestically-owned banks hold the bulk of T-bills, in some cases as part of their capital. Against this backdrop, the upcoming reforms to bank regulations requiring the valuation of assets at market prices would create recapitalization needs for several banks. Based on the official indicators (Table 6), the authorities are less concerned about bank liquidity and solvency. They argued that high deposits (due to the RBZ credit to the government and to the withdrawal limits) boost bank liquidity, and large holdings of T-bills raise bank profitability. They are hopeful that discounts on the quasi-currency instruments will disappear once dollar liquidity returns to normal levels. Staff argued that reliance on financial indicators that do not fully factor in emerging pricing and liquidity risks could imperil bank soundness analysis.

Box 4. Experience with the Dollarized Regime

Dollarization brought benefits to the economy at a critical moment.

- It halted hyperinflation. Inflation declined from 79.6 billion percent at end-2008 to 3.2 percent by end-2010.
- It helped restore business confidence. Real GDP had declined by 15 percent in 2008 and grew by 15.4 percent in 2010.
- It supported re-monetization of the economy and eliminated the exchange rate risk involved in investment decisions.

However, the basic conditions for the system to function smoothly were not in place.

- High employment costs raised the fiscal deficit and obstructed the downward adjustment of private sector wages and prices in response to changing economic conditions.
- With limited external inflows, the RBZ financing of the deficit was higher than its readily available reserves (those that do not back liabilities), resulting in money creation and undermining banks' ability to finance private sector's activities.
- Economic policies led to an overvalued real exchange rate that hurt competitiveness and growth. Increasing foreign exchange outflows compounded the liquidity crisis.
- The banking sector has not been performing its intermediation role. More recently, banks' main function has been to finance the fiscal deficit, undermining its ability to finance development.

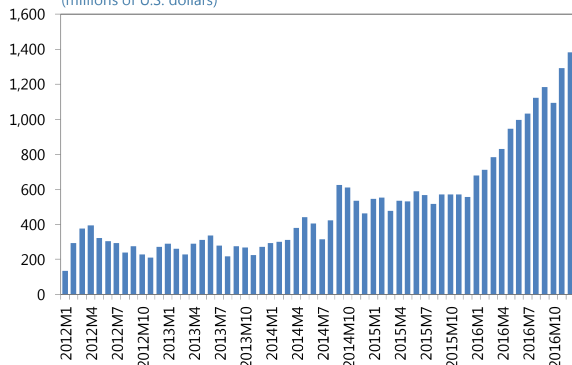
27. Refraining from further monetary financing of the deficit and containing domestic debt is critical. The RBZ's ability to honor its obligations to banks depends on the government's capacity to pay back the overdraft, which would require it to move to fiscal surpluses, and/or obtain significant external financing. Fiscal consolidation would help ensure that the bond notes issued remain within the agreed limit and do not widen the emerging discounts. The authorities concurred with the need to minimize monetary financing of the deficit.

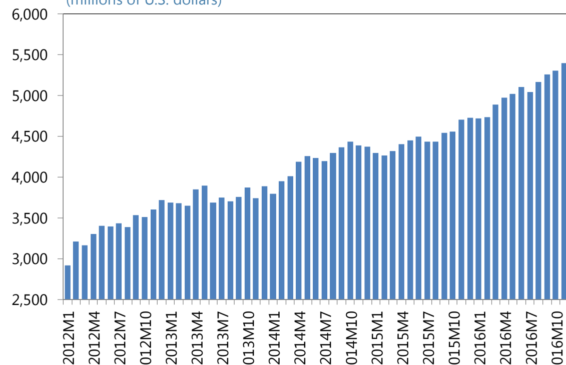
28. Financial sector soundness is jeopardized by declining external financing and increased credit risk. Related to the country's high risk perception, 50 correspondent relationships with banks based in Zimbabwe were lost since 2014, though alternative arrangements have been secured in most cases. In this context, domestically-owned banks indicate having less access to external financing, facing payment delays, and being subject to additional transaction costs. In response, the authorities noted that they have ramped up their AML/CFT framework. They also pointed to the introduction of ceilings to domestic lending rates to contain the cost of financing. Staff encouraged the authorities to reinforce efforts to restore banking relations and argued against interest rate caps, which constitute an additional economic distortion. Banks, which already face high credit risk, are finding it hard to adhere to regulated interest rates. Bank impaired portfolio continues to increase as the payment capacity of borrowers is affected by import delays and liquidity shortages.

Figure 4. Banking Sector Fragility

Commercial banks have increasingly illiquid deposits at the RBZ…

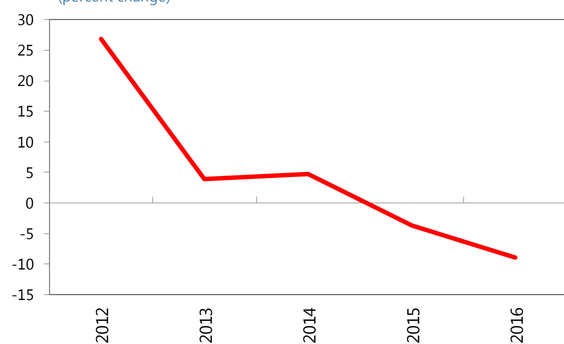
…as do private depositors with commercial banks.

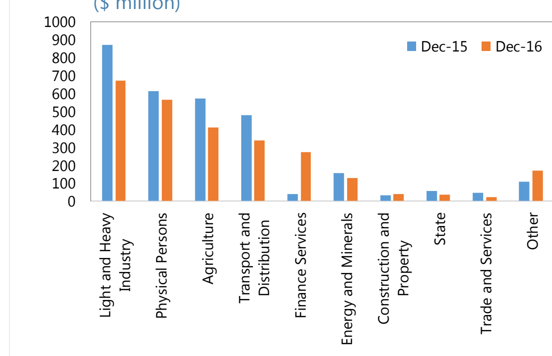




The private sector is being crowded out.

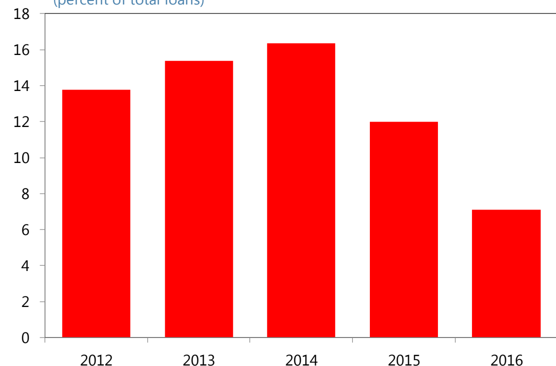
Industry, agriculture, and distribution account for over 50 percent of credit.

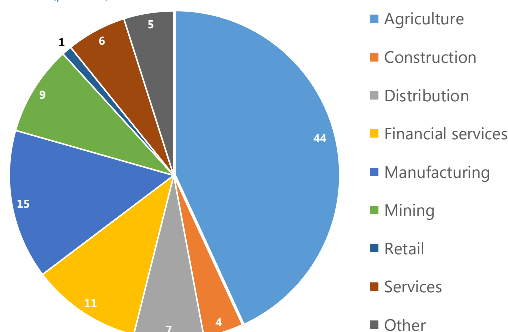




Non-performing loans peaked in 2014.

Agriculture accounts for the bulk of ZAMCO's portfolio.





Sources: Zimbabwean authorities and IMF staff calculations.

29. Dealing with NPLs has proven more challenging than anticipated. While ZAMCO's purchases of bad loans brought down NPLs in bank balance sheets, the fiscal cost has been higher than expected, both because the assumed portfolio was twice the amount initially intended and because the recovery of bad loans has been lower than expected. With the fiscal position in deficit, ZAMCO's NPL assumption implies that the government is bearing the cost of socializing private losses through additional borrowing. Banks' business models are also affected by firms' decision to downsize their operations or to recourse to the informal market in procurement of U.S. dollars for purchases abroad. Staff noted that these developments are impairing the ability of corporates and individuals to meet bank obligations, and putting upward pressure on NPLs. While acknowledging the likely difficulties in resolving consequent funding needs, staff urged the authorities to work with banks in developing contingency planning to tackle these risks. Bolstering the AML/CFT framework, including by addressing the deficiencies identified in Zimbabwe's 2016 AML/CFT Mutual Evaluation Report, could help to reduce the pressure on correspondent banking relationships.

C. Boosting Structural Reforms

30. The government's large footprint in the economy continues to impede private sector development. Businesses are deterred by the uncertain policy environment, a relatively heavy tax burden, economic imbalances that complicate investment decisions, and a high degree of perceived corruption.[10] Agricultural land is owned by the state, and there are no market-based mechanisms in place to have truly bankable land leases. This situation has affected meaningful investment in the sector, much needed also in the wake of climate change. SOEs cover key areas of the economy (airline, electricity, water, railways, and mining); are inefficient in their service provision; and constitute a drain on the budget.[11] Under such circumstances, informalization has become increasingly widespread, with only a small percentage of the working population in formal employment.

31. Against this backdrop, there is a clear need to speed up implementation of key structural reforms. The authorities pointed to the progress on reforms to improve the business environment achieved through the Special Economic Zones Act and the Rapid Results Reform Initiative with support from the World Bank. They indicated they have examined the bottlenecks to doing business, and commenced work on needed institutional, legislative, and regulatory reforms targeted at promoting tourism and manufacturing, and bringing land back into productive use.[12] Staff acknowledged this progress, but called for effective implementation of reforms to provide a level playing field for domestic and foreign actors. In mining, for example, this would entail making all leases public, and avoiding

[10] Corruption was identified as one of the most problematic factors in doing business by the World Economic Forum's Global Competitiveness Index. See also Zimbabwe's low score in Transparency International's Corruption Perception Index.

[11] In 2016, the government consolidated all diamond-mining operations into an SOE, the Zimbabwe Consolidated Diamond Company (ZCDC). However, it has yet to begin substantial mining operations and has significant capitalization requirements.

[12] Some of the legislative reforms that have been approved by cabinet and have gone through first readings in parliament are (i) Movable Property Security Interest Bill, (ii) Insolvency Bill, (iii) Estate Administrators Act Amendment Bill, (iv) Ease of Settling Commercial and Other Disputes Bill, and, (v) A Deeds Act Amendment Bill.

contract negotiations on a case-by-case basis that depart from the established legal principles. On the agricultural front, fully bankable leases are critical to restore access to credit and finance investment. Uncertainties about non-indigenous investors' options need to be eliminated by implementing the indigenization policy in a fair and measured way. To complement efforts to improve governance, steps should be taken to criminalize acts of corruption in line with the United Nations Convention against Corruption, strengthen the Zimbabwe Anti-Corruption Commission, and publish comprehensive asset declarations of high-level officials.

32. Improving the management of SOEs will reduce the drain on the budget and improve the supply of public goods. The authorities acknowledged the need to reduce losses, but highlighted the difficulties of finding international partners to assist in running companies in the context of the country's isolation and the SOEs' huge debt overhang. With the assistance of the World Bank, they have drafted a new law, the National Code of Corporate Governance Bill, to improve SOEs corporate governance and reporting requirements. Political obstacles, however, appear to have hampered more direct central control of SOEs, which will continue to be largely overseen by the line ministries. Stronger monitoring of the financial operations of SOEs will be essential to reduce future recapitalization needs.

33. Further improvements in public financial management could promote good governance, budget credibility, and effectiveness of government expenditure. Budgetary processes need to be brought into line with fiscal objectives and available resources. ZIMASSET, the national development strategy, for example, provides project proposals for budget preparation, but investment expenditure, squeezed out by current outlays, is well under one-tenth of the levels foreseen in the strategy. Although a joint venture law could potentially provide a way for PPPs to fill some of the infrastructure gap, there is a need for strengthened transparency and accountability. On procurement, a new legal framework with an independent regulatory authority overseeing decentralized procurement entities has been introduced. The framework incorporates new inspection and evaluation arrangements, including possible sanctions for offending procurement officers and service providers. Staff also supported the authorities' efforts to improve the comprehensiveness of fiscal reporting and auditing processes.

STAFF APPRAISAL

34. The severe challenges faced by the Zimbabwean economy require an immediate and commensurate response from the authorities. Zimbabwe's international isolation imposes constraints on the economy, and makes attracting external financing and investment difficult. However, such constraints make sound domestic policies even more essential. Efforts to restore economic stability and improve the business climate to attract investment have not been sufficient to unleash the economy's enormous potential. A concerted political consensus on the need for further adjustment and reform is therefore essential.

35. Fiscal consolidation is urgent and inescapable. The unsustainable modalities of deficit financing are undermining policy credibility, reducing the resources available for private sector development, and hampering international transactions. Public sector employment costs are at the heart of the current economic difficulties, and need to be dealt with to halt the unsustainable increase of public debt. This would require taking advantage of external expertise and seeking to mitigate the

negative social consequences. Similarly, while the authorities' desire to expand production is understandable, it must be done in a measured way to avoid creating distortions and inefficiencies that could undermine growth and increase income inequality. Measures to enhance revenue collection and cut discretionary spending can also help support consolidation.

36. Achieving a sustainable fiscal stance is also a *sine qua non* for stabilizing the monetary regime and restoring confidence. To restore credibility, the authorities must reduce the fiscal deficit and reestablish private sector confidence. It is important to refrain from monetary financing of the deficit, contain the issuance of T-bills to prevent an accelerating discount of domestic paper to the U.S. dollar and a further worsening of a dire liquidity situation, and refrain from borrowing at unsustainable terms or by collateralizing future export proceeds.

37. Financial sector supervision should be more proactive and focus on emerging risks. Restoring confidence in the financial sector and allowing it to perform its financial intermediation role effectively is a main priority. Bolstering the AML/CFT framework is another critical component for facilitating international transactions. As the situation stabilizes, the authorities can also rollback the exchange controls. With respect to the measures giving rise to the exchange restriction described in paragraph 11, staff does not recommend the Executive Board approval of the retention of the measures since there is no clear plan and timetable for their elimination.

38. The authorities are encouraged to build on the efforts underway to ensure full and deep implementation of the structural reform agenda. The efforts to contain wages, establish a one-stop shop for investors, create Special Economic Zones with more liberal economic policies, and ease the difficulties of doing business demonstrate technical and institutional willingness to attract investment and support growth. In addition to tackling the current macroeconomic imbalances, success in these endeavors will require consistent and transparent implementation of policies, laws, and regulations. Combating corruption and improving governance will also contribute to reducing the cost of doing business.

39. While the risks on the downside are clear and immediate, there are also significant opportunities on the upside. Zimbabwe has a strong endowment of natural resources and human capital. The formal economy is facing severe difficulties, but the resilience of the informal sector is suggestive of the speed with which the economy could recover given the right policy framework. A strong reform agenda, including to make progress on human rights and property issues, could also pave the way for reengagement with the international community, thereby unlocking possibilities for financing, investment and debt relief that are essential to unlock Zimbabwe's enormous potential.

40. Staff recommends that the next Article IV consultation with Zimbabwe be held on the standard 12-month consultation cycle.

Table 1. Zimbabwe: Selected Economic Indicators, 2012–22

	Actual				Est.	Projections					
	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Real GDP growth (annual percentage change) [1/]	13.6	5.3	2.8	1.4	0.7	2.8	0.8	0.3	-0.3	-0.7	-0.9
Nominal GDP (US$ millions)	14,058	15,224	15,834	16,072	16,124	17,105	18,904	20,601	21,434	22,218	22,877
GDP deflator (annual percentage change)	2.5	2.9	1.2	0.1	-0.3	3.2	9.6	8.7	4.3	4.4	4.0
Inflation (annual percentage change)											
Consumer price inflation (annual average)	3.7	1.6	-0.2	-2.4	-1.6	2.5	9.5	8.3	4.0	4.0	4.0
Consumer price inflation (end-of-period)	2.9	0.3	-0.8	-2.5	-0.9	7.0	10.0	7.0	4.0	3.5	3.5
Central government (percent of GDP)											
Revenue and grants	24.9	24.6	23.8	23.3	21.7	21.7	21.1	20.9	20.7	20.6	20.5
Expenditure and net lending	25.5	26.7	25.4	25.9	30.8	28.0	25.4	25.0	24.7	24.7	24.7
Of which: Employment costs (incl. grants & transfers)	17.8	18.2	19.2	18.9	20.0	18.5	16.8	16.2	15.9	15.5	15.3
Of which: Capital expenditure and net lending [2/]	2.5	3.2	2.3	3.1	6.0	4.5	3.8	3.6	3.5	3.4	3.3
Overall balance (cash basis)	-0.5	-1.9	-0.9	-2.4	-8.8	-5.9	-4.3	-4.1	-4.1	-4.1	-4.0
Primary balance (cash basis)	-0.4	-1.7	-0.6	-1.8	-8.1	-4.8	-3.1	-2.5	-2.3	-2.2	-2.1
Money and credit (annual percentage change)											
Domestic credit (net) [3/]	91.6	6.2	4.9	14.1	25.6	3.1	6.8	8.0	7.4	7.5	6.3
Of which: Credit to the private sector [3/]	27.1	3.7	5.8	6.0	8.2	-10.0	-6.7	-3.7	-3.4	-2.2	-1.9
Bond notes + commercial bank deposits with central bank	46.6	-0.4	70.9	21.3	161.3	29.3	15.9	4.6	4.4	4.2	4.1
Balance of payments (US$ millions; unless otherwise indicated)											
Merchandise exports	3,990	3,835	3,570	3,614	3,701	3,821	3,984	4,185	4,159	4,208	4,259
Value growth (annual percentage change)	-12.7	-3.9	-6.9	1.2	2.4	3.2	4.3	5.1	-0.6	1.2	1.2
Merchandise imports	-6,710	-6,809	-6,306	-6,062	-5,236	-5,349	-5,076	-5,190	-5,213	-5,290	-5,361
Value growth (annual percentage change)	-11.3	1.5	-7.4	-3.9	-13.6	2.2	-5.1	2.2	0.4	1.5	1.3
Current account balance (excluding official transfers)	-1,818	-2,375	-2,395	-1,495	-662	-617	-159	-79	-211	-370	-439
(percent of GDP)	-12.9	-15.6	-15.1	-9.3	-4.1	-3.6	-0.8	-0.4	-1.0	-1.7	-1.9
Overall balance [3/]	-33	-179	-333	-165	133	-253	92	60	51	32	47
Official reserves (end-of-period)											
Gross international reserves (US$ millions)	398	284	303	339	310	221	201	181	161	141	141
(months of imports of goods and services)	0.6	0.4	0.5	0.6	0.6	0.4	0.4	0.4	0.3	0.3	0.3
Net international reserves (US$ millions)	260	149	178	222	303	213	193	173	153	133	133
Debt (end-of-period)											
Domestic debt (US$ millions, e.o.p.) [4/]	287	479	1,764	2,281	4,006	4830	5699	6595	7480	8377	9285
(percent of GDP)	2.0	3.1	11.1	14.2	24.8	28.2	30.1	32.0	34.9	37.7	40.6
Public and publicly guaranteed external debt (US$ millions, e.o.p.) [5/ 6/]	5,169	5,389	6,407	6,613	7,231	7,259	7,245	7,216	7,187	7,164	7,152
(percent of GDP)	36.8	35.4	40.5	41.1	44.8	42.4	38.3	35.0	33.5	32.2	31.3
Of which: Arrears	4,439	4,576	4,718	4,864	5,014	5,042	5,028	4,999	4,970	4,947	4,935
(percent of GDP)	31.6	30.1	29.8	30.3	31.1	29.5	26.6	24.3	23.2	22.3	21.6

Sources: Zimbabwean authorities; IMF staff estimates and projections.

1/ At constant 2009 prices.

2/ About 70 percent of 2016 spending is attributable to the build-up of grain reserves and the distribution of agricultural inputs under the command agriculture program.

3/ Credit to the private sector revised up for NPL purchase of $38 mn. (2014), $315 mn. (2015), $458 mn. (2016) and $100 mn. (2017, proj) by ZAMCO.

4/ Domestic debt includes government overdraft with the RBZ, recapitalization of RBZ and other entitities, recognition of debt incurred during the hyperinflation era, and TBs issued for buget financing and clearance of domestic arrears.

5/ Includes valuation adjustment.

6/ Debt stocks are based on preliminary results of the authorities' external debt reconciliation exercise. Includes valuation adjustment.

Table 2. Zimbabwe: Balance of Payments, 2012–22
(Millions of U.S. dollars; unless otherwise indicated)

	Actual				Est.	Projections					
	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Current account (excluding official transfers)	-1,818	-2,375	-2,395	-1,495	-662	-617	-159	-79	-211	-370	-439
Trade balance	-2,720	-2,974	-2,736	-2,448	-1,535	-1,528	-1,091	-1,004	-1,053	-1,082	-1,101
Exports, f.o.b.	3,990	3,835	3,570	3,614	3,701	3,821	3,984	4,185	4,159	4,208	4,259
Imports, f.o.b.	-6,710	-6,809	-6,306	-6,062	-5,236	-5,349	-5,076	-5,190	-5,213	-5,290	-5,361
Nonfactor services (net)	-856	-919	-963	-541	-455	-368	-357	-361	-364	-369	-373
Investment income (net)	-339	-458	-686	-667	-622	-640	-633	-624	-671	-767	-805
Interest and dividends	143	88	-147	-162	-180	-169	-143	-119	-154	-239	-270
Receipts	294	179	187	196	205	205	205	205	185	148	134
Payments	-152	-91	-333	-358	-385	-375	-348	-325	-339	-388	-403
Other	-482	-546	-540	-505	-442	-470	-490	-505	-518	-527	-535
Current transfers (net)	2,097	1,975	1,992	2,161	1,950	1,918	1,922	1,911	1,877	1,847	1,840
Remittances	1,164	1,104	1,166	1,277	1,103	1,105	1,107	1,096	1,041	989	960
Capital account (including official transfers)	1,721	1,721	2,034	1,529	795	365	251	139	262	402	486
Official transfers	738	251	369	398	242	230	219	208	212	216	220
Direct investment	351	373	473	399	343	132	130	104	115	124	134
Portfolio investment	99	114	130	123	-80	-150	-24	-18	17	17	20
Long-term capital	32	750	178	434	244	202	-188	-164	-108	46	66
Other short-term capital	0	0	0	0	0	0	0	0	0	0	0
Change in NFA of DMBs	266	1	63	57	22	114	-97	-51	-42	-29	-34
Change in assets	-2	62	-171	-174	-62	64	-69	-12	-17	-4	-9
Change in liabilities	-376	-702	108	231	84	50	-28	-39	-25	-25	-25
Errors and omissions[2]	64	474	27	-198	0	0	0	0	0	0	0
Overall balance	-33	-179	-333	-165	133	-253	92	60	51	32	47
Financing[1]	33	179	333	165	-133	253	-92	-60	-51	-32	-47
Central bank (net) (- denotes increase)	-98	91	-102	-8	-73	111	20	20	20	20	0
Change in gross foreign assets	-34	108	18	85	-24	-92	-20	-20	-20	-20	0
Change in gross official reserves	-32	114	19	36	29	-90	-20	-20	-20	-20	0
Of which : Change in SDR holdings	109	0	0	0	17	0	0	0	0	0	0
Monetary authorities operations (non-reserve)	-2	-5	-1	49	5	-2	0	0	0	0	0
Change in gross foreign liabilities	34	-108	18	85	-24	-92	-20	-20	-20	-20	0
Change in short-term official liabilities	8	3	10	8	110	0	0	0	0	0	0
Change in net international reserves	-40	111	9	28	-81	-90	-20	-20	-20	-20	0
Change in arrears (– denotes decrease)	130	174	167	134	142	140	146	148	142	141	120
Memorandum items:											
Current account balance (percent of GDP)	-12.9	-15.6	-15.1	-9.3	-4.1	-3.6	-0.8	-0.4	-1.0	-1.7	-1.9
Gross international reserves (US$ millions, e.o.p.)	398	284	303	339	310	221	201	181	161	141	141
Months of imports of goods and services	0.6	0.4	0.5	0.6	0.6	0.4	0.4	0.4	0.3	0.3	0.3
SDR holdings (US$ millions, e.o.p.)[4]	143	143	134	128	108	109	109	109	109	109	109
PPG external debt (US$ millions, e.o.p.)[3, 5]	5,169	5,389	6,407	6,613	7,231	7,259	7,245	7,216	7,187	7,164	7,152
Percent of GDP	36.8	35.4	40.5	41.1	44.8	42.4	38.3	35.0	33.5	32.2	31.3
Of which: Arrears	4,439	4,576	4,718	4,864	5,014	5,042	5,028	4,999	4,970	4,947	4,935
Percent of GDP	31.6	30.1	29.8	30.3	31.1	29.5	26.6	24.3	23.2	22.3	21.6
Nominal GDP (US$ millions)	14,058	15,224	15,834	16,072	16,124	17,105	18,904	20,601	21,434	22,218	22,877
Percentage change	16.5	8.3	4.0	1.5	0.3	6.1	10.5	9.0	4.0	3.7	3.0
Exports of goods and services	4,258	4,113	3,854	3,903	3,996	4,115	4,278	4,479	4,451	4,497	4,548
Percentage change	-12.1	-3.4	-6.3	1.3	2.4	3.0	4.0	4.7	-0.6	1.0	1.1
Imports of goods and services	-7,834	-8,005	-7,553	-6,893	-5,986	-6,010	-5,726	-5,844	-5,868	-5,948	-6,022
Percentage change	-10.1	2.2	-5.6	-8.7	-13.2	0.4	-4.7	2.1	0.4	1.4	1.2
Terms of trade (percentage change)	2.5	-1.6	-2.0	0.6	4.7	4.3	3.2	2.6	3.5	3.1	0.7

Sources: Zimbabwean authorities; IMF staff estimates and projections.

[1] May not match data for government external financing in the fiscal table because this line is on an accrual basis.
[2] Large errors and omissions are likely generated by under-recording of exports, remittances, and FDI.
[3] Debt stocks are estimates based on preliminary results of the authorities' external debt reconciliation exercise initiated in 2013. Includes valuation adjustment.
[4] Excludes amounts in SDR escrow account.
[5] Includes valuation adjustment.

Table 3. Zimbabwe: Central Government Operations, 2012–22

(Millions of U.S. dollars)

	Actual				Est.	Projections					
	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total revenue & on-budget grants	**3,496**	**3,741**	**3,770**	**3,737**	**3,502**	**3,714**	**3,981**	**4,302**	**4,427**	**4,575**	**4,697**
Tax revenue	3,279	3,414	3,519	3,548	3,237	3,439	3,676	3,961	4,071	4,207	4,318
Personal income tax	661	744	900	770	736	761	824	890	889	912	929
Corporate income tax	445	404	365	422	338	350	383	409	413	423	432
Other direct taxes	287	227	284	204	187	192	211	227	236	245	252
Customs	354	361	351	345	273	280	264	266	277	287	296
Excise	394	510	517	714	642	665	665	758	789	818	842
VAT	1,086	1,068	972	985	963	1088	1218	1292	1344	1393	1435
Other indirect taxes	52	98	129	108	98	102	112	119	124	129	132
Non-tax revenue	217	327	251	189	265	275	304	342	355	368	379
Total expenditure & net lending	**3,581**	**4,065**	**4,024**	**4,156**	**4,970**	**4,783**	**4,793**	**5,146**	**5,300**	**5,486**	**5,641**
Of which: Cash expenditure	3,568	4,027	3,912	4,117	4,923	4,719	4,797	5,149	*5,304*	*5,477*	*5,620*
Current expenditure	3,226	3,583	3,655	3,666	4,004	4,013	4,076	4,405	4,545	4,738	4,883
Employment costs	2,134	2,344	2,583	2,579	2,756	2,709	2,709	2,848	2,908	3,015	3,078
Wages & salaries	1,732	1,926	2,106	2,142	2,278	2,231	2,227	2,354	2,425	2,514	2,562
Pensions	402	418	477	438	478	478	482	494	483	501	516
Interest payments	40	116	136	177	127	191	225	332	373	414	456
Foreign	38	110	110	102	20	30	22	33	32	31	29
Of which: Paid	18	17	17	10	13	30	26	36	36	22	8
Domestic	3	6	26	75	107	161	203	299	341	383	426
Of which: Paid	3	6	26	75	107	161	203	299	341	383	426
Goods & services	505	359	322	319	370	446	464	500	510	529	545
Grants & transfers	548	763	613	590	751	667	678	724	754	781	804
Capital expenditure and net lending	355	483	370	490	966	771	717	742	755	747	759
Capital expenditure [1/]	266	411	333	399	859	582	541	566	583	580	591
Net lending	89	71	36	91	107	189	176	176	172	167	167
Overall balance (commitment basis)	**-85**	**-324**	**-254**	**-419**	**-1,468**	**-1,070**	**-813**	**-844**	**-873**	**-911**	**-944**
Primary balance (commitment basis) [2/]	-45	-208	-118	-242	-1,341	-879	-588	-512	-501	-497	-488
Overall balance (cash basis)	**-72**	**-286**	**-142**	**-380**	**-1,421**	**-1,005**	**-817**	**-847**	**-878**	**-902**	**-923**
Primary balance (cash basis) [2/]	-51	-262	-98	-295	-1,301	-814	-588	-512	-501	-497	-488
Financing	**85**	**324**	**254**	**419**	**1,468**	**1,070**	**813**	**844**	**873**	**911**	**944**
Domestic financing (net)	13	282	197	449	1,244	759	869	896	885	897	908
Bank	105	41	544	479	1,163	759	869	896	885	897	908
Of which: RBZ overdraft	n.a.	n.a.	n.a.	152	663	200	300	100	100	100	100
Non-bank [3/]	-36	72	-347	-29	81	-100	0	0	0	0	0
Foreign financing (net)	6	-127	-151	-187	77	182	-41	-23	18	36	49
Disbursements	0	72	0	8	210	400	120	120	160	170	181
Amortization due	102	199	151	187	133	218	161	143	142	134	132
Of which: Paid	49	68	55	69	32	154	173	169	167	165	166
Change in arrears	66	169	209	157	147	128	-15	-28	-29	-23	-12
Domestic	-6	-55	20	-53	40	65	0	0	0	0	0
Foreign	72	224	189	210	107	63	-15	-28	-29	-23	-12
Interest	20	93	93	92	7	-1	-4	-3	-4	8	21
Principal [4/]	53	130	97	118	101	64	-11	-25	-25	-31	-34

Sources: Zimbabwean authorities; and IMF staff estimates and projections.

[1/] Approximately 70 percent of 2016 expenditure is related to grain imports and agricultural support programs.

[2/] The difference between the primary balance on a commitment and cash basis is the change in domestic arrears.

[3/] Including statistical discrepancy.

[4/] Accumulated arrears on foreign debt do not include valuation adjustment. The stock of arrears could differ from that in the balance of payments table.

Table 3. Zimbabwe: Central Government Operations, 2012–22 (concluded)

(Millions of U.S. dollars)

	Actual				Est.	Projections					
	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total revenue & on-budget grants	**24.9**	**24.6**	**23.8**	**23.3**	**21.7**	**21.7**	**21.1**	**20.9**	**20.7**	**20.6**	**20.5**
Tax revenue	23.3	22.4	22.2	22.1	20.1	20.1	19.4	19.2	19.0	18.9	18.9
Personal income tax	4.7	4.9	5.7	4.8	4.6	4.5	4.4	4.3	4.1	4.1	4.1
Corporate income tax	3.2	2.7	2.3	2.6	2.1	2.0	2.0	2.0	1.9	1.9	1.9
Other direct taxes	2.0	1.5	1.8	1.3	1.2	1.1	1.1	1.1	1.1	1.1	1.1
Customs	2.5	2.4	2.2	2.1	1.7	1.6	1.4	1.3	1.3	1.3	1.3
Excise	2.8	3.4	3.3	4.4	4.0	3.9	3.5	3.7	3.7	3.7	3.7
VAT	7.7	7.0	6.1	6.1	6.0	6.4	6.4	6.3	6.3	6.3	6.3
Other indirect taxes	0.4	0.6	0.8	0.7	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Non-tax revenue	1.5	2.1	1.6	1.2	1.6	1.6	1.6	1.7	1.7	1.7	1.7
Total expenditure & net lending	**25.5**	**26.7**	**25.4**	**25.9**	**30.8**	**28.0**	**25.4**	**25.0**	**24.7**	**24.7**	**24.7**
Of which: Cash expenditure	25.4	26.5	24.7	25.6	30.5	27.6	25.4	25.0	24.7	24.7	24.6
Current expenditure	22.9	23.5	23.1	22.8	24.8	23.5	21.6	21.4	21.2	21.3	21.3
Employment costs	15.2	15.4	16.3	16.0	17.1	15.8	14.3	13.8	13.6	13.6	13.5
Wages & salaries	12.3	12.6	13.3	13.3	14.1	13.0	11.8	11.4	11.3	11.3	11.2
Pensions	2.9	2.7	3.0	2.7	3.0	2.8	2.6	2.4	2.3	2.3	2.3
Interest payments	0.3	0.8	0.9	1.1	0.8	1.1	1.2	1.6	1.7	1.9	2.0
Foreign	0.3	0.7	0.7	0.6	0.1	0.2	0.1	0.2	0.1	0.1	0.1
Of which: Paid	0.1	0.1	0.1	0.1	0.1	0.2	0.1	0.2	0.2	0.1	0.0
Domestic	0.0	0.0	0.2	0.5	0.7	0.9	1.1	1.4	1.6	1.7	1.9
Of which: Paid	0.0	0.0	0.2	0.5	0.7	0.9	1.1	1.4	1.6	1.7	1.9
Goods & services	3.6	2.4	2.0	2.0	2.3	2.6	2.5	2.4	2.4	2.4	2.4
Grants & transfers	3.9	5.0	3.9	3.7	4.7	3.9	3.6	3.5	3.5	3.5	3.5
Of which: Employment costs	2.6	2.8	2.9	2.8	2.9	2.7	2.4	2.4	2.4	1.9	1.9
Capital expenditure and net lending	2.5	3.2	2.3	3.1	6.0	4.5	3.8	3.6	3.5	3.4	3.3
Capital expenditure 1/	1.9	2.7	2.1	2.5	5.3	3.4	2.9	2.7	2.7	2.6	2.6
Net lending	0.6	0.5	0.2	0.6	0.7	1.1	0.9	0.9	0.8	0.8	0.7
Overall balance (commitment basis)	**-0.6**	**-2.1**	**-1.6**	**-2.6**	**-9.1**	**-6.3**	**-4.3**	**-4.1**	**-4.1**	**-4.1**	**-4.1**
Primary balance (commitment basis) 2/	-0.3	-1.4	-0.7	-1.5	-8.3	-5.1	-3.1	-2.5	-2.3	-2.2	-2.1
Overall balance (cash basis)	**-0.5**	**-1.9**	**-0.9**	**-2.4**	**-8.8**	**-5.9**	**-4.3**	**-4.1**	**-4.1**	**-4.1**	**-4.0**
Primary balance (cash basis) 2/	-0.4	-1.7	-0.6	-1.8	-8.1	-4.8	-3.1	-2.5	-2.3	-2.2	-2.1
Financing	**0.6**	**2.1**	**1.6**	**2.6**	**9.1**	**6.3**	**4.3**	**4.1**	**4.1**	**4.1**	**4.1**
Domestic financing (net)	0.1	1.9	1.2	2.8	7.7	4.4	4.6	4.3	4.1	4.0	4.0
Bank	0.7	0.3	3.4	3.0	7.2	4.4	4.6	4.3	4.1	4.0	4.0
Of which: RBZ overdraft	0.0	0.0	0.0	0.9	4.1	1.2	1.6	0.5	0.5	0.5	0.4
Non-bank 3/	-0.3	0.5	-2.2	-0.2	0.5	-0.6	0.0	0.0	0.0	0.0	0.0
Foreign financing (net)	0.0	-0.8	-1.0	-1.2	0.5	1.1	-0.2	-0.1	0.1	0.2	0.2
Disbursements	0.0	0.5	0.0	0.0	1.3	2.3	0.6	0.6	0.7	0.8	0.8
Of which: SDRs	0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Amortization due	0.7	1.3	1.0	1.2	0.8	1.3	0.9	0.7	0.7	0.6	0.6
Of which: Paid	0.4	0.4	0.3	0.4	0.2	0.9	0.9	0.8	0.8	0.7	0.7
Change in arrears	0.5	1.1	1.3	1.0	0.9	0.7	-0.1	-0.1	-0.1	-0.1	-0.1
Domestic	0.0	-0.4	0.1	-0.3	0.2	0.4	0.0	0.0	0.0	0.0	0.0
Foreign	0.5	1.5	1.2	1.3	0.7	0.4	-0.1	-0.1	-0.1	-0.1	-0.1
Interest	0.1	0.6	0.6	0.6	0.0	0.0	0.0	0.0	0.0	0.0	0.1
Principal	0.4	0.9	0.6	0.7	0.6	0.4	-0.1	-0.1	-0.1	-0.1	-0.1

Sources: Zimbabwean authorities; and IMF staff estimates and projections.

1/ Approximately 70 percent of 2016 expenditure is related to grain imports and agricultural support programs.

2/ The difference between the primary balance on a commitment and cash basis is the change in domestic arrears.

3/ Including statistical discrepancy.

Table 4. Zimbabwe: Monetary Survey, 2012–18
(Millions of U.S. dollars; unless otherwise indicated)

	Actual					Projections	
	2012	2013	2014	2015	2016	2017	2018
CENTRAL BANK							
Net Foreign Assets	**-641**	**-731**	**-631**	**-624**	**-574**	**-685**	**-705**
Foreign Assets	441	332	350	435	412	320	300
Foreign Liabilities	1,082	1,064	981	1,060	986	1,005	1,005
Net Domestic Assets	**1,489**	**1,485**	**1,392**	**1,434**	**2,145**	**2,592**	**2,913**
Net Domestic Credit	1,644	1,575	1,474	1,481	2,285	2,562	2,847
Net Credit to Non Financial Public Sector	1,680	1,621	1,515	1,356	2,372	2,762	3,072
of which: Net Credit to Central Government	1,660	1,660	1,524	1,269	2,219	2,512	2,812
Credit to Private Sector	10	4	5	56	31	25	25
Net Credit to Financial Corporations	-46	-50	-46	70	-118	-224	-249
Other Items Net	-155	-90	-81	-47	-140	30	66
Monetary Base	**273**	**272**	**464**	**563**	**1,473**	**1,907**	**2,208**
Non Liquid Liabilities [1/]	**575**	**482**	**298**	**247**	**98**	**0**	**0**
OTHER DEPOSITORY CORPORATIONS							
Net Foreign Assets	**266**	**1**	**-62**	**-4**	**18**	**132**	**34**
Foreign Assets	642	704	533	359	298	361	292
Foreign Liabilities	376	702	595	364	280	230	258
Net Domestic Assets	**3,453**	**3,886**	**4,438**	**4,733**	**5,549**	**5,892**	**6,457**
Net Domestic Credit	3,980	4,374	4,789	5,548	6,635	6,895	7,506
Net Credit to Non Financial Public Sector	96	394	594	1,311	1,650	2,211	2,776
of which: Net Credit to Central Government	23	315	515	1,204	1,529	2,088	2,653
Credit to Private Sector	3,437	3,573	3,741	3,602	3,497	2,980	2,726
Net Credit to Financial Corporations	447	408	455	635	1,488	1,705	2,005
Other Items Net	-527	-488	-351	-815	-1,086	-1,003	-1,050
Liquid Liabilities	**3,719**	**3,888**	**4,377**	**4,729**	**5,567**	**6,024**	**6,491**
DEPOSITORY CORPORATIONS							
Net Foreign Assets	**-376**	**-730**	**-693**	**-628**	**-556**	**-554**	**-671**
Net Domestic Assets	**4,669**	**5,100**	**5,367**	**5,611**	**6,292**	**6,800**	**7,385**
Net Domestic Credit	5,278	5,606	5,843	6,356	7,614	8,008	8,629
Net Credit to Non Financial Public Sector	1,776	2,015	2,108	2,666	4,022	4,972	5,848
Credit to Private Sector	3,447	3,576	3,745	3,658	3,528	3,004	2,750
Net Credit to Other Financial Corporations	56	14	-11	31	64	31	31
Other Items (Net)	-609	-506	-476	-745	-1,321	-1,208	-1,244
Broad Money (M3)	**3,719**	**3,888**	**4,377**	**4,736**	**5,638**	**6,245**	**6,714**
Money (M2)	3,663	3,805	4,257	4,691	5,575	6,177	6,641
Narrow Money (M1)	2,431	2,478	2,724	3,059	4,104	4,585	4,925
Non Liquid Liabilities	**575**	**482**	**298**	**247**	**98**	**0**	**0**

Sources: Zimbabwean authorities; and IMF staff estimates and projections.

[1/] Non liquid liabilities represent nonmonetary liabilities to the private sector.

Table 5. Zimbabwe: Alternative Scenarios

Alternative Scenario A. Absence of Adjustment

	Projections					
	2017	2018	2019	2020	2021	2022
Real GDP growth (annual percentage change)	1.7	-1.3	-3.6	-4.0	-3.7	-3.7
Nominal GDP ($ millions) at parity	17,291	22,221	32,744	63,718	190,770	826,700
Nominal GDP ($ millions) at parallel market rate	13,927	13,960	13,642	13,227	12,820	12,401
Consumer price inflation (annual average)	5.7	30.2	52.8	102.7	210.9	350.0
Implicit parallel market rate to US$	1.2	1.6	2.4	4.8	14.9	66.7
Central government (percent of GDP)						
Revenue and grants	20.4	19.5	19.2	19.0	18.8	18.6
Expenditure and net lending	29.9	29.6	29.3	29.3	29.3	29.3
Overall balance (cash basis)	-9.1	-10.4	-10.4	-10.4	-10.5	-10.7
Primary balance (cash basis)	-8.1	-9.3	-9.6	-9.5	-9.3	-8.9
Of which: RBZ overdraft	6.1	7.0	7.0	6.9	7.0	7.1
Current account balance (percent of GDP)	-0.9	-0.9	-0.5	-0.5	-0.1	0.2
Gross international reserves (US$ millions)	185	167	149	137	116	92
Domestic debt (percent of GDP)	31.1	34.7	33.9	27.7	19.6	15.1
External debt (percent of GDP, parallel market rate)	52.2	51.9	52.9	54.4	55.9	57.7

Alternative Scenario B. Strong Adjustment

	Projections					
	2017	2018	2019	2020	2021	2022
Real GDP growth (annual percentage change)	3.1	4.6	6.0	5.9	5.8	5.7
Nominal GDP ($ millions)	17,038	18,252	19,748	21,338	23,062	24,902
Consumer price inflation (annual average)	2.7	2.4	2.1	2.0	2.2	2.2
Central government (percent of GDP)						
Revenue and grants	21.7	22.0	22.4	22.7	23.1	23.4
Expenditure and net lending	26.6	23.7	22.6	22.2	21.7	21.6
Overall balance (cash basis)	-4.5	-1.7	-0.2	0.5	1.4	1.9
Of which: RBZ overdraft	0.0	-1.1	-2.0	-1.0	0.0	0.0
Current account balance (percent of GDP)	-0.6	-4.3	-7.9	-8.1	-7.9	-7.9
Gross international reserves (Months of Imports)	0.7	1.5	2.4	3.1	3.3	3.9
Domestic debt (percent of GDP)	27.0	25.7	23.9	21.5	18.4	15.1
External debt (percent of GDP)	42.6	41.9	39.1	36.5	34.1	31.9

Table 6. Zimbabwe: Financial Soundness Indicators, 2012–16

	2012	2013	2014	2015	2016
Capital Adequacy					
Regulatory capital to risk-weighted assets	11	12	17	20	24
Percentage of banks greater or equal to 10 percent	89	88	86	100	100
Percentage of banks below 10 and above 6 percent minimum	11	0	7	0	0
Percentage of banks below 6 percent minimum	0	13	7	0	0
Capital to assets	7	7	10	11	12
Asset quality					
Foreign exchange loans to total loans	6	5	1	3	0
Past-due loans to gross loans	30	32	46	43	41
Nonperforming loans	14	15	16	12	8
Watch-listed loans	16	16	29	31	33
Provisions as percent of past-due loans	26	27	16	13	13
Earnings and profitability					
Return on assets	1	0	1	2	2
Return on equity	5	-3	5	9	13
Expenses/ income	90	99	93	82	75
Liquidity					
Liquid assets/total assets	25	28	27	36	47
Liquid assets/short-term liabilities	30	35	36	47	59
Loans/deposits	93	104	77	85	65
Liquid assets/total deposits	40	51	49	64	78
Foreign exchange liabilities/total liabilities	1	0	4	2	5

Source: Zimbabwean authorities.
Note: Numbers are in percent, unless otherwise indicated. These numbers are not adjusted for liquidity and pricing risks.

Annex I. Risk Assessment Matrix[1]

Sources of Risks	Relative Likelihood	Impact if Realized	Policy Response
Significant further strengthening of the U.S. dollar and/or higher international rates	High	**High**. Continued appreciation of the U.S. dollar would undermine already weak competitiveness and exacerbate pressures on the external current account and the fiscal deficit. Higher interest rates will impact the cost at which Zimbabwe sources funding, including for the arrears clearance plan.	Increase labor market flexibility, and implement structural reforms to improve the business climate, achieve productivity and competitiveness. Ensure that interest rate risks are factored in the sourcing of funds, and build fiscal buffers to restore imbalances and meet financing obligations.
Reduced external funding, including financial services by correspondent banks	High	**High**. Further loss of correspondent banking relationships would impact the ability of banks, particularly the domestic ones, to intermediate effectively, including by increasing their costs and reducing their access to liquidity. It would also worsen the existing market segmentation.	Strengthen banks' regulatory frameworks, including for AML/CFT to ensure financial soundness, integrity, and good governance. Improve the business environment to allow banks to function in line with international best practices.
Structurally weak growth in key advanced and emerging economies	High/ Medium	**Medium to High**. Zimbabwe would be impacted through the trade channel, particularly from South Africa, reflecting both weaker demand and prices. Financing and remittances would also suffer, increasing the BOP pressures and worsening the liquidity situation.	Reduce the budget deficit to create policy buffers and improve policy credibility; advance structural reforms to boost productivity and competitiveness; and re-engage with the international community to access much needed financial support.
Failure to advance fiscal reforms	Medium/ High	**High**. Absent expenditure rationalization, particularly on the wage bill, fiscal borrowing requirements would remain high in a context of declining tax revenue. The crowding out of the private sector would continue, and domestic financing of the budget would further weaken the financial sector and threaten price stability as the supply of bond notes increases.	Create the domestic political consensus needed to advance fiscal reforms. Improve revenue collection by strengthening tax administration and broadening the base. Improve the efficiency of public spending by reallocating resources to social and capital spending. Reduce the footprint of the government in the economy by leveraging the private sector.
Stalled reengagement and structural reforms until after 2018 elections	High	**High.** A failure to advance reforms and garner the support of the international community would result in incomplete *ad hoc* adjustments that could exacerbate economic imbalances and further worsening policy confidence.	Advance structural reforms both to improve the external position and to garner support of the international community. Take the needed action so that the arrears clearance process unleashes external financing from IFIs to contain the balance of payments pressures and restore access to international financial markets.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term" and "medium term" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

Annex II. Climate Change: Risks and Policy Options for Zimbabwe[1]

1. The 2015/16 El-Niño induced drought and the heavy rains of early-2017 exposed Zimbabwe's vulnerability to climatic variations (Figure A2.1). The disasters damaged output and production capacity, resulting in significant deterioration of social conditions. The drought hurt the agricultural sector, which employs nearly 70 percent of the population, directly or indirectly. It also led to a marked spike in malnutrition and reduced employment opportunities. The floods somewhat dampened the projected rebound in agriculture by damaging crops, contributing to an infestation of climatic-induced armyworms, causing significant infrastructure damage, and leading to outbreaks of typhoid and malaria.

2. The drought brought to the fore the economy's cyclical and structural vulnerabilities:

- ***Output and employment in agriculture.*** After an already poor 2014/15 season, land under cultivation declined sharply as irrigation capacity was strained; livestock farmers had to destock; and migration by pastoral farmers increased.

- ***Electricity supply.*** Hydro-generation capacity was disrupted, impacting industrial production, particularly in the energy intensive mining industries.

- ***External trade.*** The trade balance deteriorated as electricity and grain imports increased markedly, and agricultural exports declined.

- ***Fiscal deficit.*** Expenditure picked up and domestic debt rocketed as the government expanded the command agriculture program and distributed free grains to those affected.

3. The recent floods have further revealed the social implications of these disasters. The poor are being disproportionately hit as they settle in the most vulnerable areas with weak housing standards. With deteriorating infrastructure, water quality has worsened, and waterborne diseases have increased. The stretched healthcare system has been unable to cope with the outbreaks of malaria and typhoid, resulting in a rise in fatalities.

4. The frequency and severity of climatic events is likely to increase due to climate change, resulting in longer-term economic and social costs. As elsewhere, sub-Saharan Africa has already seen temperature increases and average rainfall declines, and is likely to face accentuated climate change effects. Global warming by 1.5°–2°C could lead to a 40–80 percent reduction in present maize, millet, and sorghum cropping areas in Africa (World Bank 2013), affecting subsistence agriculture households disproportionately more. Zimbabwe is highly vulnerable to losses in agricultural productivity, infrastructure, and food security. Moreover, hydroelectric power generation (which supplies about 40 percent of electricity needs) could drop drastically; and declines in wildlife stock could affect tourism arrivals. Finally, changing weather patterns could disrupt traditional

[1] Prepared by Vimal Thakoor and reviewed by Ana Lucía Coronel.

business models, lead to dislocation of economic activities, and result in stranded assets, such as roads, bridges, and dams. For instance, the increasing reliance on hydropower—through the construction of the $4 billion Batoka project (shared with Zambia)—will increase risks arising from fluctuations in water levels. Changing water quality could also affect fishing.

5. The economy's structure and limited adaptation capacity renders Zimbabwe highly vulnerable to climate change. The strained fiscal position and limited access to external financing inhibit investment in adaptation and mitigation measures. The economy is highly dependent on rain-fed agriculture and weather-sensitive activities, such as herding. While the country has the second highest number of waterbodies in the region, lack of maintenance has affected their storage capacity due to silting. Given that an increasing share of the population lives just above the poverty line, a small climatic shock often results in a significant increase in the number of people falling into poverty and unable to meet their basic needs. Finally, low access to credit and insurance reduces the scope for risk transfer and for financing for post-disaster relief and reconstruction.

6. Zimbabwe needs to overcome its limited adaptive capacity, existing structural amplifiers, and restricted policy space and international support. While some initiatives have been implemented at the grassroots levels, they are yet to make a significant dent. It is imperative to integrate climate change in development planning to mitigate the challenges for economic management through a mix of risk reduction and risk transfer, with private sector taking the lead in many areas.

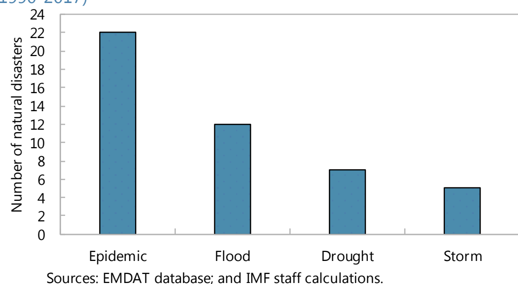
- ***Risk reduction*** entails diversification away from agriculture, which is prone to floods and droughts, and toward private sector-led manufacturing and services; investments in irrigation and water infrastructure in line with a targeted program integrated with the budget process; strategies to increase agricultural productivity and food security, including focusing on crops more resilient to water shortages, and ensuring better preparedness and spatial planning; restoration of access to financing through a well-functioning payment system and developed debt markets; implementation of financial inclusion initiatives to support pastoral farmers; and development of well-targeted social safety nets and cost-effective primary healthcare systems to contain the cascading impact of disasters (e.g., rain leading to floods, diseases and epidemics).
- ***Risk transfer*** toward households involves increasing access to cost-effective financial instruments (such as the mobile-driven initiatives in East Africa) to address the disproportionally higher inability of poor households to adapt to and hedge against climate-related shocks. Risk transfer toward aid providers would require Zimbabwe's reengagement with the international community to become eligible for quicker and better-targeted disaster relief, including from international financial institutions.

7. Unfortunately, given Zimbabwe's constraints, the country has little alternative but to retain a higher than optimal level of risk in the near-term. Zimbabwe can self-insure against natural disasters and climate change by creating policy buffers. Dealing with climate change is yet another important reason to rebalance the expenditure profile making room for infrastructure and healthcare investment; raise revenues, including through a potential carbon tax; redouble efforts to restore access to credit; and accelerate reengagement with the international community.

Figure A2.1. Impact of Climate-Induced Disasters

Zimbabwe is more prone to epidemics…

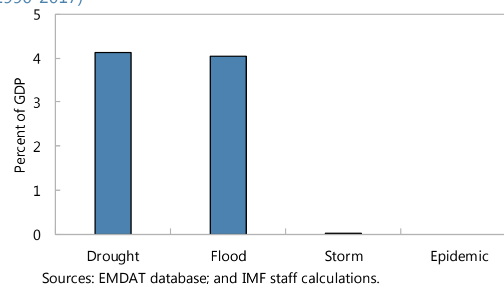
Natural Disasters in Zimbabwe
(1990-2017)



Sources: EMDAT database; and IMF staff calculations.

…but droughts and floods generate a high economic cost.

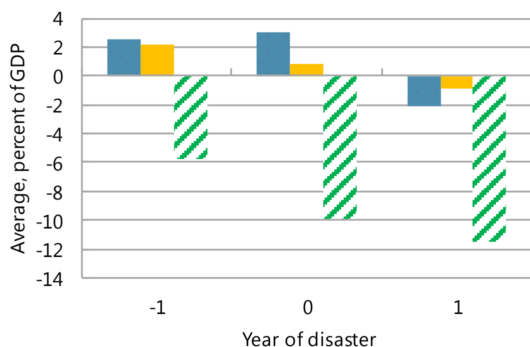
Total Reported Cost by Type of Disaster
(1990-2017)



Sources: EMDAT database; and IMF staff calculations.

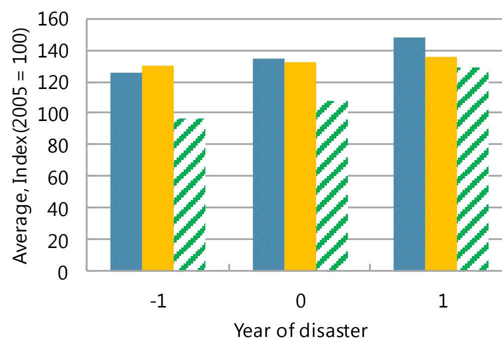
Disasters are associated with lower growth…

Real GDP Growth (1990-2014)



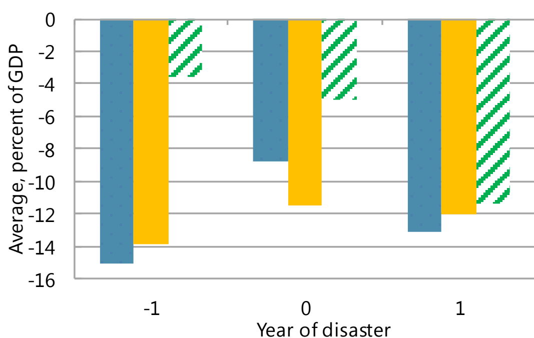
…and increased food vulnerability…

Food Price Index (1990-2014)



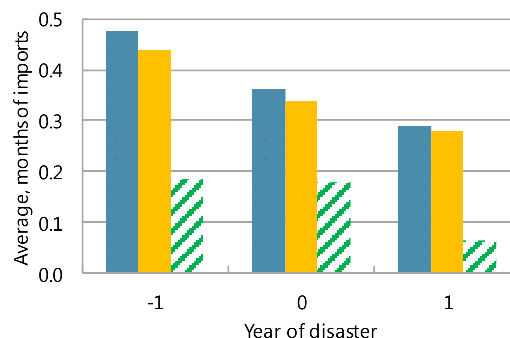
…as well as weaker external balances…

Current Account Balance (1990-2014)



…and generally declining reserves.

International Reserves (1990-2014)



Droughts Floods Storms

Sources: EM-DAT database, Zimbabwean authorities, and IMF staff calculations.

Annex III. Fiscal Consolidation in Fragile States: Comparisons with Zimbabwe[1]

How do countries overcome fragility?

1. **IMF studies[2] suggest that on average it takes around a decade for fragile countries to overcome fragility.** The fiscal situation of fragile states tends to be characterized by a poor revenue base, large expenditure pressures, poor public financial governance, and a long list of reform needs in a context of generalized capacity challenges, which can undermine efforts to build well-functioning states. Yet several countries—many with far worse initial conditions than Zimbabwe—could overcome these constraints, and employ fiscal policy as a driving force in building more resilient and responsive states.

2. **While transitioning out of fragility, countries experienced improvements in rule of law and political stability.** Lower inflation and higher growth was usually accomplished through efforts to build and maintain fiscal space in these countries. Mobilization of domestic revenue was key in creating the demand for accountable government, and reducing reliance on aid and borrowing. Equally important was maintaining tight control of current expenditure, and notably wages. This required high-level political commitment and consensus building, for example in Uganda in the early 1990s when the number of ministries and civil servants was reduced by almost half. In other instances, exchange rate depreciations facilitated the adjustment without the need to cut nominal wages (e.g. Cameroon in 1994). With current expenditures contained, countries could increase investment: capital spending—on infrastructure and provision of public goods—doubled to 30 percent of total spending over the decade in which countries built resilience.[3] At the same time, PFM improvements sought to ensure a higher return from these investments. The international community played a supportive role: in seven African states that successfully built resilience, aid and debt relief averaged 10 percent of GDP in the decade they overcame fragility.[4]

Comparisons with Zimbabwe

3. **While the experience of formerly fragile countries demonstrates that reestablishing resilience is possible, the context of Zimbabwe imposes some unique challenges.** Zimbabwe's current position differs from those states that overcame fragility in three key ways:

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[1] Prepared by Joe Thornton and reviewed by Ana Lucía Coronel.

[2] "Exiting from Fragility in sub-Saharan Africa: The Role of Fiscal Policies and Fiscal Institutions", Delechat, Fuli, Mulaj, Ramirez, Xu, IMF WP/15/268, and "Building Resilience in sub-Saharan Africa's Fragile States", IMF 2015.

[3] Building Resilience in sub-Saharan Africa's Fragile States", IMF 2015, found a strong positive relationship between public investment and growth performance in fragile states, suggesting that their large infrastructure needs can result in high returns.

[4] Cameroon, Ethiopia, Mozambique, Níger, Nigeria, Rwanda and Uganda.

- **A relatively high revenue-to-GDP ratio**. At 22 percent, Zimbabwe's revenue-to-GDP ratio is five times higher than the average for the fragile states at the start of their transition. Moreover, Zimbabwe also boasts significant non-tax revenues from minerals and licensing fees. Furthermore, the widespread adoption of fees for services in such areas as health and education suggests that the income base is even greater.

- **An extremely high public-sector wage bill.** At 20 percent of GDP, 100 percent of tax revenues, and two-thirds of government spending, the public-sector wage bill is several times higher than the average for the seven formerly-fragile countries. Relative to Zimbabwe's income level, its public administration is both large and well compensated.[5]

- **A difficult international context.** Aid and debt relief were essential elements to restoring stability for all the formerly fragile countries. Zimbabwe's prospects for assistance on a similar scale appear bleak at present.

4. While the high tax ratio reflects the economy's resilience, it also suggests the capacity to implement additional tax measures is likely to be more limited than in other countries. Attempts in February 2017 to broaden the base by extending the VAT to formerly exempt foodstuffs, for example, had to be quickly revised. While the government is encouraged to consider measures to reduce loopholes, improve efficiency, and decrease evasion, maintaining tax rates at a level that encourages entrepreneurial activity is also important.

5. International comparisons would suggest that measures to reduce the public sector wage bill would be more productive in terms of generating fiscal space. In the case of Zimbabwe, a nominal depreciation, such as that used by many countries in the CFA franc zone to reduce real wages, is not an option. Furthermore, the U.S. dollar's appreciation against the South African rand is creating a deflationary context that exacerbates the current high wage bill. Absent much stronger growth in the real economy, significant nominal cuts in employment costs may be necessary under a dollarized system. While the government has implemented a general freeze on recruitment and wages since 2014, and began implementing the findings of the Public Service Commission Audit in 2016, stronger measures are required to reduce the current macroeconomic imbalances. Such measures could include extension of the wage bill audits to other sectors (e.g. judiciary and health), rationalization of benefits, allowances and the 13th salary, and revisions to the wage bill structure. Going forward, a more fundamental reevaluation of the role of the state in the economy might suggest possibilities for a deeper rationalization of the public sector, with the aim or producing a smaller yet more effective government.

6. Given the social and economic costs involved, successful reform of the public sector will require strong support at the highest level. Other countries have found that challenging moments can serve to generate consensus behind long-needed reforms. The international political context will be vital in Zimbabwe too. External financing could greatly ease the costs of transition, providing funding for retrenchment of public sector workers, and helping to generate the growth

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[5] Government of Zimbabwe and World Bank (2017), Public Expenditure Review, forthcoming]

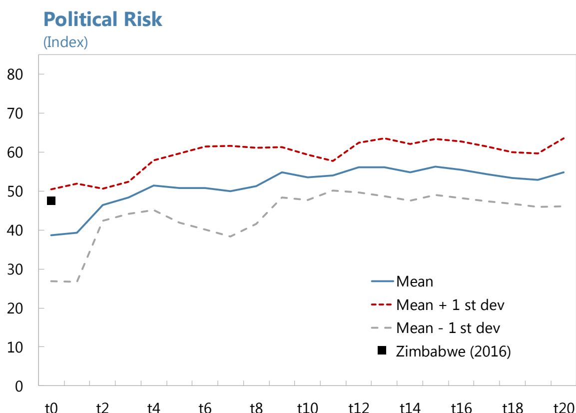
necessary to open broader economic opportunities. Indeed, it is doubtful whether many of the other formerly fragile countries could have grown as strongly without the aid and debt relief they received in recent decades. Even if external financial assistance is not available, technical assistance from the international institutions such as the IMF and World Bank could help the authorities develop a roadmap to implement difficult civil service reforms. Yet in the final analysis, the state's own willingness and ability to provide public goods is most vital to demonstrate its competence and commitment, and thereby strengthen the resilience of the country.

7. **While the short-term costs would be high, over the medium term reducing and redirecting government expenditures will support growth and poverty reduction.** At present, the macroeconomic imbalances generated by the large fiscal deficit undermine confidence in the economy, deterring investment and putting the financial system at risk. The country's large infrastructure needs go unaddressed, further inhibiting growth. The experience of other countries in sub-Saharan Africa suggests that once a coherent framework is in place, both domestic and external resources could be generated to address the country's investment needs and, given the high potential rates of return, place the country on a greatly improved growth trajectory.

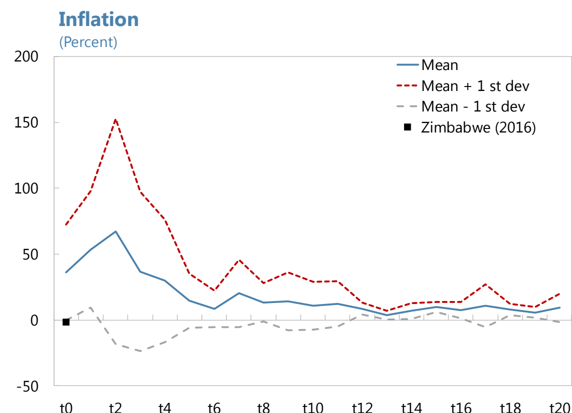
8. **Ensuring high rates of return from government spending will also require further measures to improve public financial management.** While much diagnostic work has been carried out on PFM issues, and efforts are underway to strengthen expenditure controls and internal audit functions, transparency, accountability and efficiency all need to be improved. Many of the issues are technical and can be solved with sufficient technical assistance and effort from the authorities, but others relate to the political dynamics. The deficit targeted by the 2017 budget, for example, is unlikely to be realized, as both its expenditure and revenue measures have proved difficult to implement in the current context. Issues, such as budget credibility and forecasting public debt management needs, have proved to be potential building blocks of resilient states, but they need to be complemented by some degree of political consensus and stability.

Figure A3.1. Overcoming Fragility

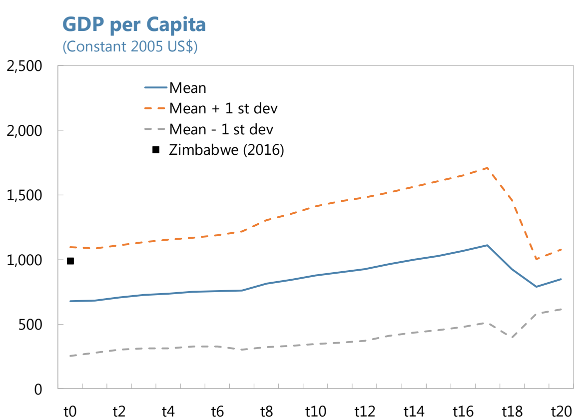
Stabilization of the political situation....



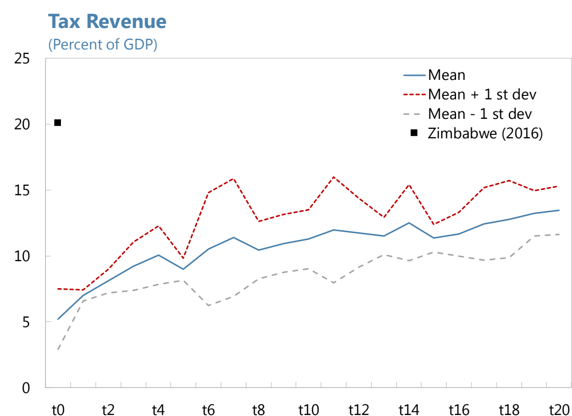
...and the economy...



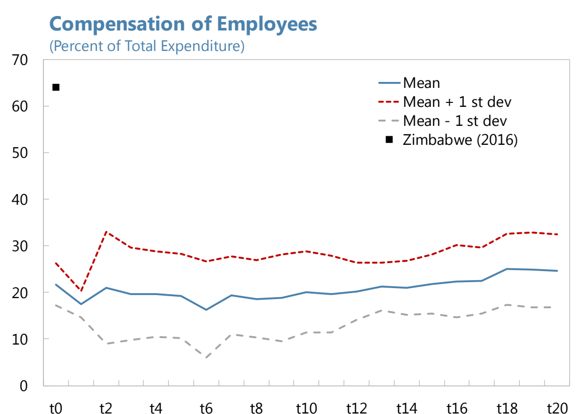
...supported the resumption of economic growth.



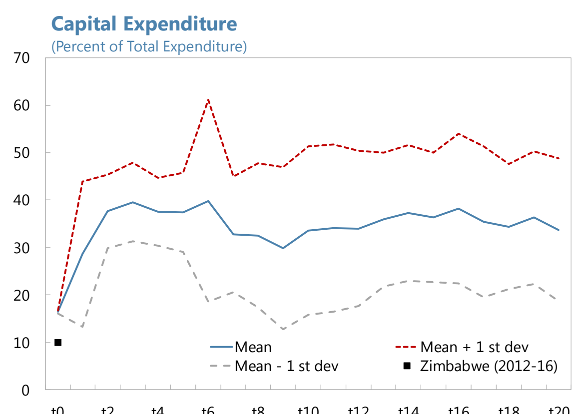
The restoration of state capacity was seen in growing government tax revenues....



...but with tight control of current spending, and in particular the wage bill ...



...allowed for a large increase in capital expenditures.



Source: "Exiting from Fragility in sub-Saharan Africa: The Role of Fiscal Policies and Fiscal Institutions", Delechat, Fuli, Mulaj, Ramirez, Xu, IMF WP/15/268

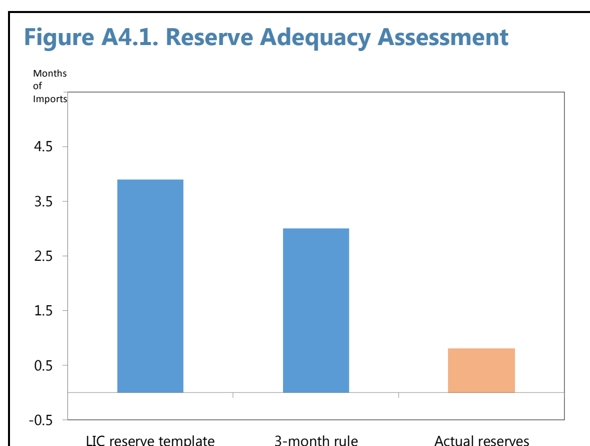
Annex IV. External Stability Assessment[1]

Zimbabwe's external position is significantly weaker than implied by fundamentals. Structural weaknesses, fiscal slippages, and exogenous factors worsened an external position already weakened by years of economic isolation and reduced external competitiveness. International reserves are inadequate by all metrics, and the current account balance presents continuous deficits, albeit narrowing due to the administrative measures in place. Restoring external stability would require real exchange rate adjustment through fiscal consolidation and structural reforms aimed at improving the business environment. The authorities concurred with staff's assessment and pointed to the various reforms they are implementing to improve the economy's competitiveness.

A. International Reserves and Current Account Balance

1. Zimbabwe is experiencing serious foreign exchange shortages and international reserves are inadequate under all metrics.[2] Gross international reserves as of end-2016 stood at $310 million, down from $339 million in 2015, covering only about two weeks of imports of goods and services. Based on the IMF's template for LICs, which considers both cross-border transactions and fundamentals such as FDI, trade, terms of trade, and the government balances, the adequate reserve level for Zimbabwe is about 3.9 months of imports. However, in light of the fragility of the Zimbabwean economy, an even higher reserve level than the one suggested by the metrics may be needed to provide buffers against price shocks. As a resource-rich economy,[3] export revenues can be very volatile. Furthermore, as a dollarized economy Zimbabwe needs to provide adequate backup for money in circulation and RTGS electronic balances in order restore confidence in the monetary regime.

Figure A4.1. Reserve Adequacy Assessment



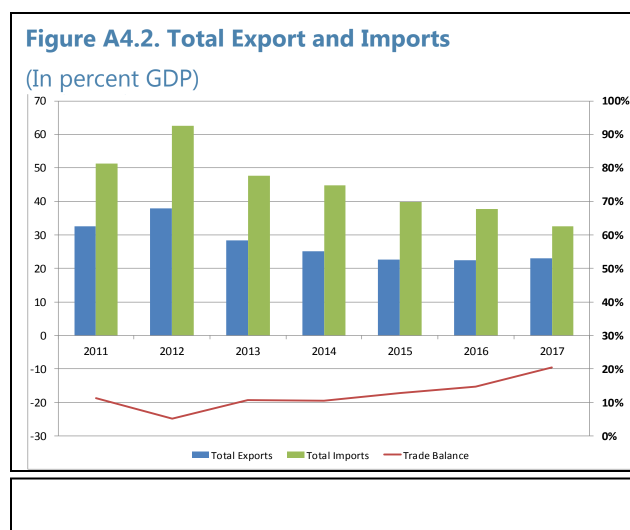
2. The current account balance, which had been characterized by acute deficits, has recently contracted sharply due to import compression. The export-to-GDP ratio has remained subdued since 2013 as depressed commodity prices and weak industry competitiveness have curbed export growth. Foreign exchange shortages have compressed capital imports and thus further weakened the domestic production capacity. While the deficit fell sharply to 4.1 percent of GDP in 2016 from 15.1 percent of GDP in 2014, this was driven by a sharp import compression rather than a

[1] Prepared by Yeu Jin Jung and reviewed by Ana Lucía Coronel and Joe Thornton.

[2] See Guidance Note on The Assessment of Reserve Adequacy and Related Considerations (June, 2016), and Assessing Reserve Adequacy – Specific Proposals (April, 2015).

[3] A country is considered resource-rich if it depends on natural resources for at least 20 percent of export or fiscal revenue using average data for 2006–10.

recovery in exports. Total imports declined by about 17½ percent in these two years mainly due to foreign exchange shortages and more recently in the context of the government's import and exchange controls.[4]



3. Owing to weak economic activity and the restrictive measures in place, overall trade is expected to remain subdued. Staff projects the current account deficit to further contract to 3.6 percent of GDP in 2017. Improved prices for minerals and tobacco are expected to boost production, resulting in export growth of about 3.2 percent, but manufacturing exports will remain constrained by outdated equipment. Imports are projected to increase by 2.2 percent, at a slower pace than export growth. While foreign exchange shortages are anticipated to continue to constrain imports, domestic manufacturers may benefit from the de facto discount of electronic balances to the U.S. dollar, which may reduce their cost base.

B. Exchange Rate and Capital Flows

4. A significantly overvalued real effective exchange rate (REER) suggests challenges for external stability. Quantitative estimates using the Fund's EBA-lite methodology for 2015 suggest that Zimbabwe's external position is substantially weaker than implied by its medium-term fundamentals and desirable policy settings.[6] The current account gap is 7.5 percent of GDP, and the real exchange rate gap varies between 26 and 48 percent. The fiscal policy gap (0.8 percent) and the international reserves shortage (1.2 percent) have contributed to 26 percent of the gap, while further structural reforms could address the factors responsible for the remainder. Zimbabwe's REER depreciated somewhat after 2010, as the depreciation of the rand against the U.S. dollar was outweighed by South Africa's higher inflation. However, low productivity, limited trade openness, and foreign exchange shortages signal a large overvaluation of the real exchange rate and the consequent need for a significant depreciation.

[4] The "Exchange Control Directive RR86 (ECOGAD8/2016)" implemented in May 2016 prioritizes 1) net exporters who import raw materials or machinery to generate exports, 2) importers of raw materials and machinery for local production that substitute imports, and 3) imports of critical and strategic goods, for the allocation of foreign exchange. The authorities also introduced repatriation requirements on export proceeds ranging from 50 to 100 percent.

[6] 2015 is used as the baseline for the assessment since the economic variables in 2016 were affected by the administrative measures introduced on current and capital account transactions.

Table A4.1. Zimbabwe: Real Exchange Rate Assessment Results

EBA-lite Current Account Regression		**EBA-lite Equilibrium RER Regression**	
CA-Actual	-8.3%	ln(REER)-Actual	4.67
CA-Norm	-0.8%	ln(REER)-Norm	4.41
CA-Gap	**-7.5%**		
REER-Gap	**47.6%**	**REER-Gap**	**23%**

Source: IMF staff estimates.

1/ Data of year 2015 used for regression.

2/ Positive numbers indicate overvaluation. Elasticity of current account to real exchange rate gap is -0.17.

Figure A4.3. CA: Actual, Fitted, and Norm

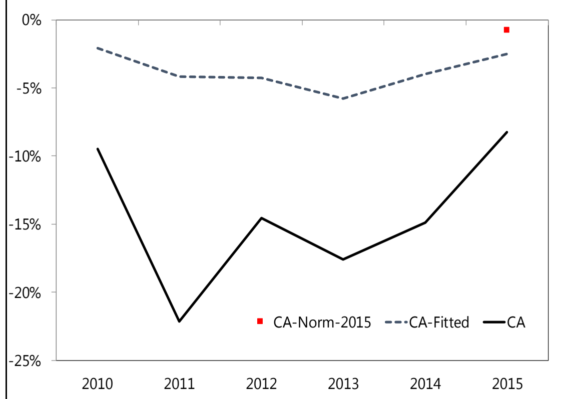
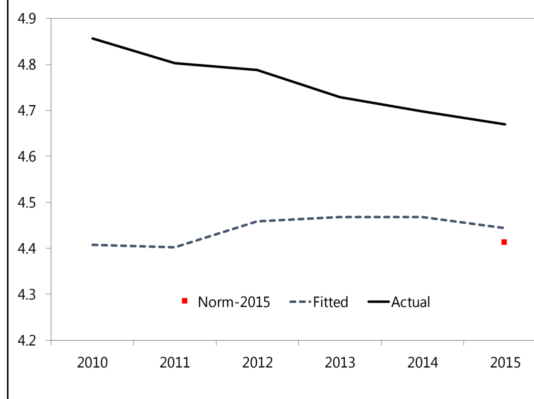


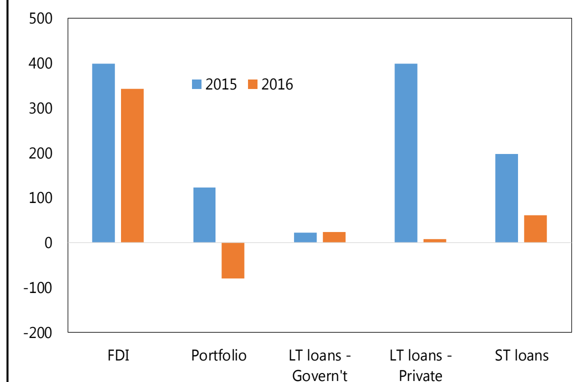
Figure A4.4. Ln(REER): Actual, Fitted, and Norm



5. **Reduced net foreign capital flows have made the problem of weak external position more challenging.** The deterioration of net capital flows in 2016 shows that foreign investors' confidence has already fallen significantly. Both foreign direct investment and portfolio investment shrunk (14 percent and 78 percent, respectively). Public sector access to credit has largely dried up due to the arrears situation, and private sector access to long-term external credit is almost non-existent. While some interest to invest remains, particularly in the mining and energy sectors,[7] structural reforms are necessary to translate this interest into real investment.

Figure A4.5. External Capital Flows (net)

(Million U.S. dollars)



[7] In 2016, the Zimbabwe Investment Authority (ZIA) approved projects worth $2.3 billion.

C. Policies to Achieve External Stability

6. Intensive structural reforms to strengthen competitiveness are essential. The business environment continues to pose challenges for investment. The World Bank's Doing Business indicators show a drop of four positions for Zimbabwe. The Country Policy and Institutional Assessment (CPIA) reflects improvements across most criteria, but the index remains at a low level, pointing to the need to intensify fiscal and structural reforms. Zimbabwe's wages are also higher than in most peer countries. Zimbabwe's minimum wage for general workers range from $200 to $300, significantly higher than in neighboring Botswana, Mozambique, and Zambia where it tends to be around $100, although broadly in line with the proposed wages that South Africa is considering introducing next year. Uncertainty over human rights and security of property also deters foreign investors.

Figure A4.6. Doing Business Index

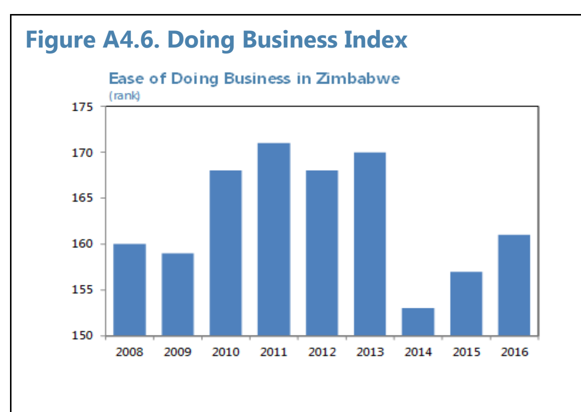
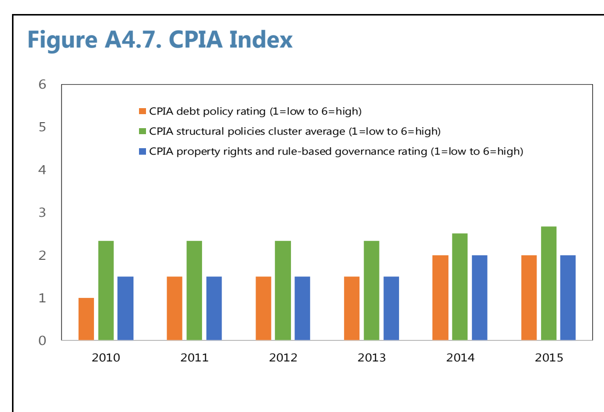


Figure A4.7. CPIA Index



7. A key indicator suggests that international investors perceive the intrinsic value of the dollar in Zimbabwe to be lower than the U.S. dollar The Old Mutual Implied Rate (OMIR) is an unorthodox but effective indicator to proxy the market's most recent perception on the economy.[8] The OMIR has been lower than the market exchange rate (between the pound sterling and the U.S. dollar) since August 2016, and increasingly diverged thereafter (Figure A4.9). This divergence reflects a perceived 50 percent premium for investing in the country. This perception might have translated into a nominal depreciation of the exchange rate, but given the dollarized system, the outcome is a *de facto* real overvaluation of the currency.

[8] The Old Mutual is an international investment, savings, insurance, and banking group. Established in 1845 in South Africa, it had more than 16 million customers and £303.8 billion in assets under management in end-2015. In Zimbabwe, 49 percent of Old Mutual shares are fungible, meaning that shareholders who bought shares on the Zimbabwe Stock Exchange (ZSE) can dispose them in other markets for better returns. This mechanism allows full arbitrage between London Stock Exchange (LSE) and ZSE. The OMIR is constructed as the ratio of the prices of Old Mutual shares traded in the LSE in sterling and ZSE in dollars. Since the shares of the Old Mutual Company are fungible and command the same claim on the company's earnings and assets, the price ratio should equal to the market exchange rate between sterling and US dollar, on the basis that the premise of purchasing power parity holds.

Figure A4.8. London Stock Exchange vs Zimbabwe Stock Exchange
(Prices divided by 100)

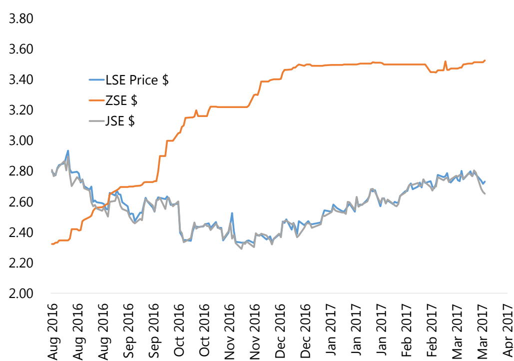


Figure A4.9. OMIR vs Market Rate Sterling/USD

8. The external position is likely to deteriorate further in the absence of adjustment. A further strengthening of the U.S. dollar would pose additional risks to the economy's external competitiveness. Increased inflation pressures from monetary financing of the deficit and bond notes could potentially result in increased REER appreciation in the near term.

Annex V. Financial Sector Health and the Fiscal Imbalance in Zimbabwe[1]

1. Zimbabwe's financial sector is largely bank-based. Total assets held by the 13 commercial banks are equivalent to almost 50 percent of GDP, of which nearly 24 percent are held by the 6 foreign-owned banks. Foreign-owned banks account for 42 percent of the market share, while one domestically-owned bank has more than 30 percent. On average, 50 percent of banks' income is interest based, while around 40 percent originates from fees and commissions.

2. The need to finance the fiscal deficit is compounding liquidity shortages and worsening confidence, thus boosting financial sector vulnerabilities and market segmentation. The banking sector, once affected by the hyperinflation episode, is now being pressured by the elevated fiscal financing needs, which are crowding out private sector credit and raising operational risks of banks and corporates. Notwithstanding the strength shown by core financial soundness indicators, the system faces weaknesses posed by an increase in RTGS electronic balances and T-bill holdings in the asset part of the balance sheets at the expense of loans to the economy. Domestically-owned banks hold an increasing part of their assets in the form of T-bills, while foreign-owned banks hold a higher share in RTGS electronic balances. The increasing mismatch between these balances and the RBZ's available foreign exchange to meet them render the bulk of these obligations inaccessible and illiquid. Additionally, the aggregated indicators mask the banking system's segmentation, with heightened risk for a few domestically-owned banks.

3. The asset/liability composition has raised risks, potentially jeopardizing the solvency of some banks (Figure A5.1). T-bills are no longer risk-free and liquid as they are subject to varying degrees of discounting in the market. With anecdotal evidence pointing to discounts of up to 45 percent, the solvency of many banks could be at risk. On average, the industry could lose up to 15 percent of its capital base (about 1 percent of GDP) for every 10 percent discounting of T-bills, with domestically-owned banks at higher risk. Additional losses could arise from the discounting of RTGS balances. Staff estimates that for every 10 percent discount in these balances, bank capital would decline by the equivalent of 0.9 percent of GDP, based on end-March numbers. Moreover, the prospective issuance of NSSA bonds to finance the central government deficit raises further concerns about the asset quality of the banks that acquire such bonds. Changes in accounting rules requiring the valuation of assets to market could bring forward the realization of these losses.

4. The economic slowdown and liquidity crisis are worsening credit risk, reducing profitability, and contributing to financial disintermediation. Many firms are unable to finance their imports due to the liquidity shortages, and the pipeline for import awaiting payments is increasing by the day. These delays are affecting the capacity of firms to produce and export, thus worsening the liquidity crisis. Private sector credit as a share of GDP is contracting as well. Reflecting both the increased risk aversion and the operations of ZAMCO, banks' credit portfolio shrunk in 2016, with four sectors (industry, individuals, agriculture, and transport and distribution) accounting

[1] Prepared by Vimal Thakoor and reviewed by Ana Lucía Coronel.

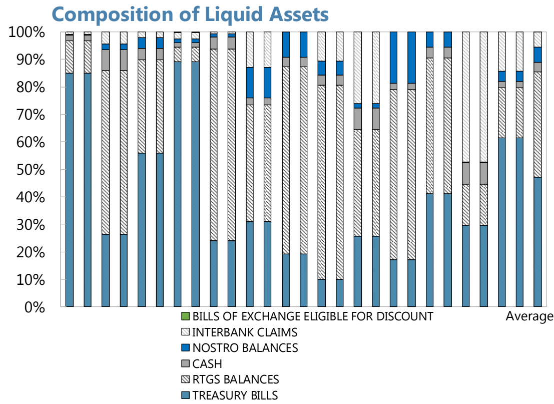
for nearly 75 percent of all credit to the economy. The segmentation also extends to credit allocation, with foreign-owned banks less willing to increase their exposure to domestic firms. In turn, this is increasing the pressure on domestic-owned banks to fill part of the void created by the foreign-owned banks. Banks' return on assets of around 2 percent in 2016 is low by international standards, reflecting high operational costs, including for procuring liquidity.

5. The expansion in the mandate of the Asset Management Company (ZAMCO) increases the risks on the public-sector balance sheet. ZAMCO was set up in 2014 with a three-year mandate to address the legacy of high NPLs from the hyperinflation episode thus complementing the overall restructuring of the banking sector. The initial strategy, aimed at purchasing viable NPLs from commercial banks and moving them to resolution, resulted in a decline of bad loans from 21 percent of total loans in 2014 to 10 percent by 2016 for the system, but several banks remain saddled with high NPLs. A further deterioration of banks' asset quality following the economic slowdown prompted ZAMCO to double the amount of purchased NPLs to over $800 million (5 percent of GDP). While ZAMCO expects to recoup about 60–65 percent of its NPL holdings, the recovery rate has so far been slower than anticipated. Moreover, when NPLs are purchased by ZAMCO, banks T-bill holdings increase, thus releasing little liquidity that can be used as fresh credit to the economy.

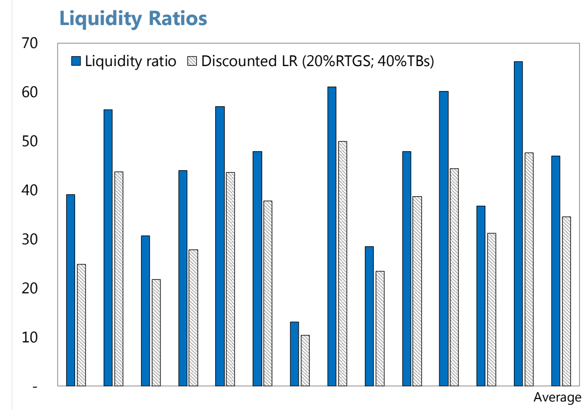
6. Recent fiscal developments are impairing banks' financial intermediation function. With the bulk of bank credit directed to the government, banks' balance sheets have weakened and they are no longer able to direct credit to the private sector on a commercial basis. The ability of banks to intermediate effectively can only be restored as the fiscal position strengthens and confidence improves.

Figure A5.1. Financial Sector Developments

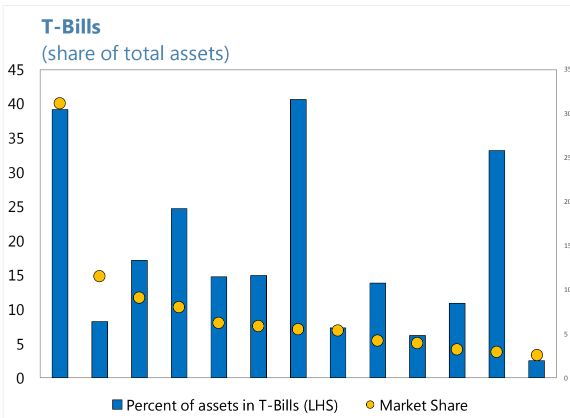
T-bills and RTGS electronic balances account for the bulk of liquid assets.



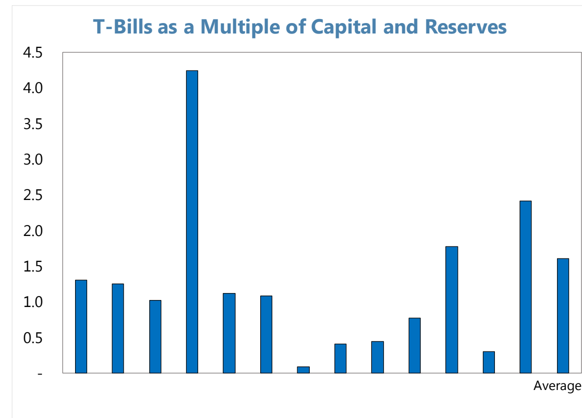
Discounts on these instruments could lead several banks to fall short of the 30 percent liquidity requirement.



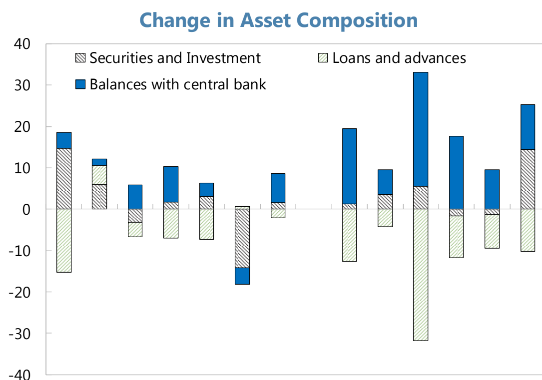
While the exposure of banks to T-Bills varies…



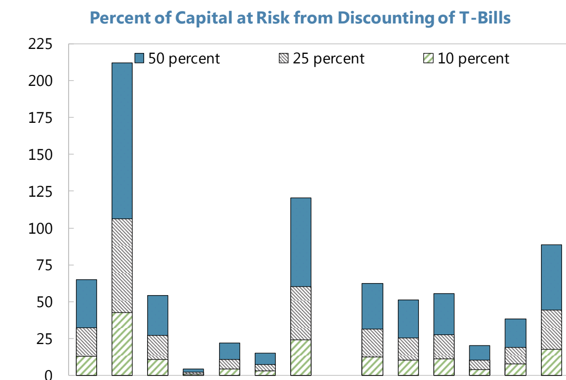
…some hold a multiple of their capital and reserves in these instruments.



Foreign-owned banks hold more unremunerated RTGS electronic balances with the central bank.



Some banks could face a significant reduction in their capital base if T-bills are discounted.



Sources: Zimbabwean authorities and IMF staff calculations.

INTERNATIONAL MONETARY FUND

ZIMBABWE

June 19, 2017

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By

The IMF's African Department
(in collaboration with other Departments, the World Bank, and the African Development Bank)

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RELATIONS WITH THE FUND

A. Financial Relations

(As of March 31, 2017)

Membership Status

Joined: September 29, 1980; Article VIII

General Resources Account:	SDR Million	%Quota
Quota	706.80	100.00
Fund holdings of currency	706.47	99.95
Reserve position	0.33	0.05
SDR Department:	**SDR Million**	**%Allocation**
Net cumulative allocation	338.58	100.00
Holdings	80.42	23.75

Outstanding Purchases and Loans: None

Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-by	Aug 02, 1999	Oct 01, 2000	141.36	24.74
Stand-by	Jun 01, 1998	Jun 30, 1999	130.65	39.20
ECF[1]	Sep 11, 1992	Sep 10, 1995	200.60	151.90

[1] Formerly PRGF

Projected Payments to Fund

(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2017	2018	2019	2020	2021
Principal					
Charges/interest	0.77	1.07	1.07	1.07	1.07
Total	0.77	1.07	1.07	1.07	1.07

Implementation of HIPC Initiative: Not Applicable

Implementation of Multilateral Debt Relief Initiative (MDRI): Not Applicable

Lifting of Remedial Measures following clearance of arrears to the PRGT:

On October 20, 2016, Zimbabwe fully settled its overdue financial obligations to the Poverty Reduction and Growth Trust (PRGT) using its SDR holdings. Zimbabwe had been in continuous arrears to the PRGT since February 2001. As of the day of repayment, Zimbabwe's arrears to the PRGT amounted to SDR 78.3 million, which comprised overdue PRGT principal of SDR 61.7 million, and total interest obligations of SDR 16.6 million (covering overdue interest and interest accrued through October 20, 2016 on overdue principal and interest amounts). The repayment of SDR 78.3 million has been applied towards the PRGT's Reserve Account.

Effective November 14, 2016, the Executive Board of the International Monetary Fund (IMF) approved the removal of the remedial measures applied to Zimbabwe. These measures had been in place because of Zimbabwe's overdue financial obligations to the Poverty Reduction and Growth Trust (PRGT). These remedial measures related to: (i) the declaration of noncooperation with the IMF (see Press Release No. 02/28); (ii) the suspension of technical assistance (which had already been partially lifted, see Press Release No. 09/152 and Press Release No. 12/405); and (iii) the removal of Zimbabwe from the list of PRGT-eligible countries (see Press Release No. 01/40).

Zimbabwe is now current on all its financial obligations to the IMF. Its eligibility to the PRGT has also been restored.

B. Nonfinancial Relations

Exchange Arrangement

In 2009, Zimbabwe adopted a multi-currency regime, including the U.S. dollar, the South African rand, the British pound, the euro, and the Botswana pula—with the U.S. dollar as principal currency and unit of account. The Australian dollar, the Chinese yuan, the Indian rupee, and the Japanese yen were added to the list in February 2014. The use of the Zimbabwean dollar as domestic currency was discontinued.

Faced with increasing balance of payments and US dollar liquidity pressures that intensified since end-2015, the authorities put in effect a range of measures to limit current and capital account transactions in May 2016. Among others, the RBZ released a foreign exchange priority list to direct the allocation of foreign exchange by commercial banks to certain domestic import substitution industries, exporters, and strategic imports. This measure gives rise to an exchange restriction subject to Fund approval under Article VIII, Section 2(a). Staff is also monitoring the authorities' imposition of other measures to assess whether they give rise to any exchange restriction or multiple currency practice subject to Article VIII, Section 2(a) and Section 3. The authorities proposed to remove these measures gradually, as the economic situation stabilized.

A new law was promulgated in October 2016 through Statutory Instrument 133 of 2016, Presidential Powers (Temporary Measures) Amendment of the Reserve Bank of Zimbabwe Act, empowering the RBZ to issue bond notes and bond coins. The statutory instrument prescribes that a tender of payment of bond notes and coins issued by the RBZ are exchangeable at par value with any specified currency prescribed as legal tender in Zimbabwe and shall be legal tender in all transactions in Zimbabwe. The authorities started the issuance of bond notes as from November 28, 2016.

Zimbabwe has also a longstanding exchange restriction subject to IMF jurisdiction arising from unsettled balances under an inoperative bilateral payments agreement with Malaysia.

The *de facto* exchange rate arrangement has been classified to the residual category *"other managed"* from an *"arrangement with no separate legal tender"*, effective October 31, 2016.

Article IV Consultations

Zimbabwe is on the standard 12–month consultation cycle. The Executive Board discussed the staff report for the 2016 Article IV consultation on May 2, 2016.

WORLD BANK—IMF COLLABORATION

1. The IMF Zimbabwe team led by Ms. Ana Lucía Coronel (mission chief) met with the World Bank Zimbabwe team, led by Ms. Camille Nuamah (country manager) on May 11, 2017.

2. The teams concurred on the analysis of the challenging economic situation, the policy response, and the corrective needed actions. There was agreement that Zimbabwe needed urgent fiscal adjustment, deep-seated structural reforms, and external financing to address the fundamental economic imbalances. In the short term, it is critical to reduce public sector employment costs and reverse central bank financing of the budget. Reforms are also needed to restore the health of the financial sector, improve public financial management and governance, and rebalance the economy away from the public sector to the private sector. In this regard, measures are critical to reduce the cost of doing business by tackling infrastructure bottlenecks and implementing reforms to attract investment once regulatory and legal frameworks have been upgraded. These measures are also critical to regain creditor support for reengagement and unlock external financing.

3. Based on this assessment, the teams agreed to support the authorities' efforts with the following division of labor:

- **PFM reform:** The Fund will continue its engagement with the Zimbabwean authorities in their efforts to advance the fiscal reform agenda and restore fiscal sustainability. The Fund will offer TA on containing fiscal risks from SOEs and improving budget monitoring and reporting. The Bank will continue supporting the gradual rollout of program-based budgeting in line ministries, the modernization of public procurement (including new legislation), financial management and reporting, enhancing internal controls and internal auditing. The Bank will also help enhance the external audit oversight and the oversight of Parliament to ensure increased transparency and accountability, the gradual expansion of the IFMIS system to public authorities (especially local

governments) currently not covered, and is working towards stronger enforcement of government rules in SOEs. As part of a joint World Bank – Ministry of Finance and Economic Development effort to review public expenditures, oversight and transparency of extra-budgetary funds is gradually being expanded.

- **Fiscal policy:** The Fund will continue to help the authorities make progress on tax reform. Technical assistance will continue to build on previous TA on tax policy, debt management and budget preparation, while AFRITAC South will support revenue administration.

- **Mining regulatory framework, fiscal policy and tax administration support.** The Bank will continue to oversee the unified mining fiscal model, which the authorities have been working to populate with data from mining companies; and monitor progress on the "options note" on mining fiscal policy.

- **Business environment reform:** The Bank will support the reforms related to improving the ease of doing business, as per the World Bank's *Doing Business* indicators; the preparation of a new Companies Code; and the formulation of a road map to an omnibus investment policy framework, both led by the Office of the President and Cabinet.

- **Financial sector reform:** The Bank will support the RBZ in the areas of banking supervision and crisis resolution, credit infrastructure, financial inclusion, and anti-money laundering and combating of financing of terrorism. The Bank is also preparing a diagnostic on SME and microfinancing. The Fund will focus on contingency planning.

- **Reform of the statistical system:** The World Bank is supporting the design and implementation of the ongoing Poverty Income and Consumption Expenditure Survey (PICES) 2016/17. The Fund will continue to offer TA in national accounts, monetary statistics, balance of payments, and government finance statistics.

- **Debt and arrears strategy:** Bank and Fund staffs will continue to support the authorities in producing the debt sustainability analysis.

- **Poverty Analysis and Poverty Reduction Strategy:** The Bank is providing TA to support Zimbabwe in the preparation of a poverty reduction strategy for the period 2018–23 following the delivery of the interim poverty reduction strategy paper covering 2016–18.

4. The teams agreed to the following sharing of information:

- The Fund team will be kept informed about the analysis and conclusions of Bank missions and about progress in all macro-critical structural reform areas. The Fund will receive the Bank's output on these topics.

- The Bank team will be kept informed of progress in the above cited areas where the Fund takes the lead. The Bank will receive the Fund's outputs, as requested.

5. The appendix lists the teams' work programs over the period April 2017–April 2018. Fund TA will continue to build on the areas of fiscal management and financial crisis management. The Bank's engagement in 2017/18 will strongly be influenced by programs under the new Zimbabwe Economic Reconstruction Fund Trust Fund (ZIMREF).

Joint Bank-Fund Work Program May 2017–April 2018			
Title	**Products**	**Provisional Timing of Missions**	**Expected Delivery Dates**
A. Mutual Information on Relevant Work Programs			
Bank work program in next 12 months	**Investment Projects** • PFM Enhancement Project; • National Water Project • Public Procurement Modernization Project • Health Sector Development Project **Technical Assistance** • SOE Reform • Doing Business and Investment Policy, including SMEs; • Financial Sector Reform • Mineral Sector Reform • Climate Change • Energy Sector • Transport Sector • Program-based budgeting • Health and Nutrition Sector • Education Sector • Social Protection and Safety Nets • Land Policy and Administration • Transport Sector • Poverty Monitoring and Analysis **Studies and Lending** • Public Expenditure Review	Ongoing, all	All beyond mid-2017, except where indicated otherwise. May 2018

IMF work program in next 12 months	**Macroeconomic Policy Analysis and Policy Advice** • Article IV 2017 **Technical Assistance** • Macro-fiscal forecasting and budget preparation and execution • Customs and tax administrations • Comprehensive, timely, and accurate accounting and financial reporting • Financial crisis management • Strengthening data compilation and dissemination	 Q2 2017 Ongoing Ongoing Ongoing Ongoing Ongoing	
B. Requests for Work Program Inputs			
Bank provides to Fund	• Updates on policy reform work: increasing mining sector transparency, strengthening human resource and payroll management, PFM reform, improving the business climate, I-PRSP • Macro framework • Timing, scope, and conclusions of Bank's missions • Update on arrears clearance	Ongoing Ongoing Ongoing Ongoing	
Fund provides to Bank	• Updates on program discussions • Updates on policy reform work: PFM, tax and financial sector reforms • Timing, scope, and conclusions of missions	Ongoing Ongoing Ongoing	
C. Agreements on Joint Products and Missions			
Joint products and missions in next 12 months	• Debt Sustainability Analysis	Q2:2017	

RELATIONS WITH THE AFRICAN DEVELOPMENT BANK GROUP

(As of May 19, 2017)

A. Overall Engagement and Strategy

1. The African Development Bank (AfDB) Group has maintained a physical presence in Zimbabwe since 2009. The AfDB seeks to assist the country transition out of fragility, build resilience, accelerate re-engagement with international financial institutions (IFIs) and promote socio-economic transformation. To this end, the AfDB has focused on the following areas: (i) rehabilitation of basic infrastructure, (ii) governance and institutional capacity strengthening, and (iii) supporting private sector development. The engagement in these areas emphasized gender and youth empowerment, climate resilience, green growth, and provision of knowledge solutions and advisory services to hasten the recovery process.

2. The Zimbabwe Country Office, with support from the Southern Africa Regional Development and Business Delivery Office (RDGS), has played a critical role in delivering the Bank's mandate. The Bank's presence has facilitated program and project implementation, aid coordination, policy advisory services, policy formulation and implementation, country policy dialogue, re-engagement efforts, as well as enhanced overall development impact of the Bank's support in the country.

3. Despite the arrears situation, the current active portfolio in Zimbabwe is composed of sixteen (16) operations with a total commitment of UA 159 million (US$ 217 million). This includes one regional and two private sector operations. The portfolio is composed of African Development Fund Grants (59.9 percent), AfDB loan for Private Sector (15.0 percent) and trust funds administered by the Multi-Donor Trust Fund for Zimbabwe (23.7 percent) and other trust funds (1.4 percent). The water supply and sanitation sector accounts for 32.8 percent of the portfolio, followed by power (30.3 percent), governance and institutional support (16.6 percent), financial (11.3 percent), agriculture (4.6 percent), social (3.9 percent), and transport (0.5 percent).

B. Key Interventions by the AFDB Group in Zimbabwe

4. The main interventions will focus in the following areas:

- **Infrastructure rehabilitation and development.** In 2010, the AfDB was requested by a group of donors to establish and administer a Multi-Donor Trust Fund for Zimbabwe (MTDF or ZimFund). The purpose of ZimFund is to contribute to early recovery and development efforts in Zimbabwe by mobilizing donor resources, promoting donor coordination, and channeling financial assistance to such efforts. Since its inception, ZimFund has played a key role in rehabilitating targeted social infrastructure in water and sanitation, and energy sectors to ensure

the country delivers basic services, builds resilience against shocks, and overcomes fragility in the face of serious socio-economic challenges.

Donors' current commitments to the ZimFund, which have been fully honored, amount to US$145 million. Under the ZimFund Phase 1 water project (US$43.61 million), physical works as well as consultancy works were completed in all the beneficiary municipalities of Harare, Chitungwiza, Chegutu, Mutare, Masvingo, and Kwekwe. Under the Phase 1 power project (US$39.6 million), there have been three work contracts focusing on distribution and sub-transmission system reinforcements and the Hwange Power Station Ash Plant Rehabilitation. ZimFund is now focusing on implementation of Phase 2 water supply and sanitation project (US$36 million) targeted at Harare, Chitungwiza, Redcliff and Ruwa as well as the energy project (partly funded to the tune of US$15.4 million).

Over and above ZimFund-financed projects in emergency infrastructure rehabilitation, the Bank Group has been able to leverage resources, including through partnerships, to support the rehabilitation of Kariba Dam, Bulawayo water and sanitation, and Alaska-Karoi energy security interventions. In addition, the Bank Group, through the Africa Water Facility (AWF) Trust Fund, is implementing a project to support the preparation of planning and technical studies for an Integrated Urban Water Management to rehabilitate the water supply and sanitation system in Marondera Municipality. The Bank also continues to assist the country in operationalizing the infrastructure study it prepared in 2011, supporting the preparation of the Energy and Transport Sector Master Plans and helping develop a pool of investment specialists to prepare feasibility studies for bankable projects. The Bank Group's intervention in basic infrastructure rehabilitation is aimed at arresting fragility and building resilience through sustainable provision of service delivery.

- **Economic and financial governance.** The AfDB Group supports Zimbabwe's economic governance and private sector development initiatives aimed at promoting inclusive growth. Support in this area consists of technical assistance, capacity building, and other types of assistance not affected by the debt arrears situation. Support has been targeted at improving economic governance and enhancing the effectiveness of public service delivery in PFM, statistics, debt management, revenue management, procurement reforms, and mining sector governance. Support has also focused on enhancing the RBZ's supervisory role, and reforming SOEs, among other topics. The Bank Group's engagement in private sector development in Zimbabwe has been both direct and indirect. Beyond its direct investment in Lake Harvest (aquaculture expansion project on Lake Kariba and trade finance line of credit to Central Africa Building Society), the AfDB Group has supported Zimbabwe's private sector through regional financial institutions that operate and invest in Zimbabwe. Also, the presence of the AfDB Group in Zimbabwe, together with the Southern Africa Regional Development and Business Delivery Office, has facilitated the close follow-up of project implementation and support to enhance the overall development impact of the Bank Group's support.

- **The re-engagement process.** The Bank Group is playing a key role in the country's debt arrears clearance and reengagement process, collaborating with other development partners. As part of the re-engagement process, the Bank Group co-hosted a series of forums with the IMF and

World Bank aimed at accelerating re-engagement. To date, the government has cleared its debt arrears with the IMF. The government is also expected to clear its debt arrears with the African Development Bank and the World Bank, in line with its debt arrears clearance strategy.

STATISTICAL ISSUES

As of May 19, 2017

I. Assessment of Data Adequacy for Surveillance
General: Despite the resource constraints, ZIMSTAT provides sufficient data to users and largely complies with international standards.
National Accounts: ZIMSTAT has made progress in following the 2008 *System of National Accounts (SNA)* guidelines. The scope of national accounts statistics is being expanded, including through the compilation of quarterly national accounts. Staff resources remain insufficient to achieve these objectives. ZIMSTAT revised GDP data from 2009 to incorporate grant-in aid items which were erroneously left out. This led to an upward revision in the GDP series. The authorities are now working on rebasing the GDP numbers. In 2017, Zimbabwe amended its laws, to allow ZIMSTAT to share anonymized micro data with data users. However, there has been no progress with regards to amending the law to allow the Zimbabwe Revenue Authority to share tax data which is a basis for quarterly national accounts compilation. The authorities are undertaking the Poverty, Income, Consumption and Expenditure Survey (PICES) 2017. The survey will provide data on income distribution, consumption level, private consumption, and living conditions of the population, CPI weights, production account of agriculture and poverty mapping.
Price Statistics: ZIMSTAT compiles and disseminates a monthly CPI, with weights based on data from the 2011/12 PICES with a December 2012 base. In the new CPI, compiled since January 2013, ZIMSTAT has also expanded the geographical coverage to include price developments in both urban and rural areas, and increase the number of items in the basket. ZIMSTAT also compiles and disseminates a quarterly producer price index (PPI), based on December 2009 with December 2008 weights. ZIMSTAT is yet to adopt a 2013 STA TA mission recommendation to make improvements to the CPI basket by replacing outdated products, increasing the frequency of data collection for perishable items from monthly to weekly, and expanding PPI coverage to include exports ZIMSTAT also compiles monthly building material index, civil engineering index and producer price index.
Government Finance Statistics: The Ministry of Finance and Economic Development (MoFED) collects data on revenue and expenditure for the budgetary central government. These are published on its website on a quarterly basis, along with the annual and mid-term budget statements. Data on government financing have improved. The MoFED is in the process of moving to Government Finance Statistics Manual (GFSM) 2001.
Monetary Statistics: The RBZ migrated to MFS reporting to the Fund in late 2015. The MFS data is based on the Standardized Reporting Forms (SRFs). Consultations are ongoing with STA on classifications of certain line items, particularly the distinction between national currency and foreign currency denominated assets and liabilities in a dollarized/multi-currency monetary regime.

External Sector Statistics: The RBZ migrated from Balance of Payments and International Investment Position Manual (BPM4) to BPM6 in December 2016 and has since submitted data to STA in accordance to BPM6. There remain gaps particularly on the financial accounts, especially reinvested earnings and trade credit. These can only be maintained through surveys. The latest survey was done in 2016 before migration to BPM6 and the data is not consistent with BPM6. Compilation of quarterly BOP statistics on BPM6 is envisaged by December 2017. The RBZ is receiving technical assistance from IMF and DfID under the Enhanced Data Dissemination Initiative II (EDDI-II) Project for Balance of Payments Module 1 aimed at strengthening compilation of external sector statistics.
International Investment Position (IIP): The RBZ has made progress on the compilation of IIP with the assistance of the IMF under EEDI II. There is however missing stock data on FDI and portfolio investments which will be obtained from the planned Foreign Private Sector Survey.
II. Data Standards and Quality
Zimbabwe participates in the Enhanced General Data Dissemination System (e-GDDS) from November 2002. The e-GDDS metadata on the IMF DSBB site were last updated in April 2013. No data ROSC is available.
III. Reporting to STA
Zimbabwe is reporting external sector statistics mainly BOP, and currency composition of foreign reserves to STA. However, Zimbabwe does not report national accounts and price statistics to STA for dissemination in the International Financial Statistics and the BOP Statistics Yearbook. Reporting of GFS to STA needs to be improved, and no sub-annual data are reported.

Table 1. Zimbabwe: Common Indicators Required for Surveillance

	Date of latest observation	Date received	Frequency of data[1]	Frequency of reporting[1]	Frequency of publication[1]
Exchange rates[2]	NA	NA	NA	NA	NA
International reserve assets and reserve liabilities of the monetary authorities[3]	Mar. 2017	May 2017	W	W	M
Reserve/base money	Mar. 2017	May 2017	W	W	M
Broad money	Mar. 2017	May 2017	M	M	M
Central bank balance sheet	Mar. 2017	May 2017	W	M	M
Consolidated balance sheet of the banking system	Dec. 2016	May 2017	Q	Q	NA
Interest rates[4]	Feb. 2017	May 2017	M	M	M
Consumer price index	Mar. 2017	May 2017	M	M	M
Revenue, expenditure, balance and composition of financing[5]— General government[6]	NA	NA	NA	NA	NA
Revenue, expenditure, balance and composition of financing[5]—Central government	Mar. 2017	May 2017	M	M	M
Stocks of central government and central government-guaranteed debt[7]	2016	May 2017	Q	I	A
External current account balance	2016	May 2017	A	I	I
External capital and financial account	2016	May 2017	Q	I	I
Exports and imports of goods	Dec. 2016	May 2017	M	I	I
GDP/GNP	2015	May 2017	A	A	A
Gross external debt	2016	May 2017	A	I	I
International investment position[8]	NA	NA	NA	NA	NA

[1] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).
[2] The Zimbabwe dollar is no longer traded against foreign currencies on the exchange market.
[3] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.
[4] Both market-based and officially-determined, including discounts rates, money market rates, rates on treasury bills, notes and bonds.
[5] Foreign, domestic bank, and domestic nonbank financing.
[6] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[7] Including currency and maturity composition.
[8] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

Note: This table reflects data submission as of May 19, 2017.

INTERNATIONAL MONETARY FUND

ZIMBABWE

June 19, 2017

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION – DEBT SUSTAINABILITY ANALYSIS

Approved by
Anne-Marie Gulde-Wolf, Zeine Zeidane (IMF) and Paloma Anós Casero (IDA)

Prepared by the staffs of the International Monetary Fund and the International Development Association

Zimbabwe is in debt distress, and its total public and external debt is unsustainable. With longstanding external arrears, foreign financing has been scarce, and large fiscal deficits are lately being financed through domestic borrowing. Domestic debt, which was negligible five years ago, has increased sharply to more than 25 percent of GDP, and is on an unsustainable trajectory. External debt indicators, notably those related to solvency, continue to breach their thresholds under the baseline scenario, while those measuring liquidity (debt service) are deteriorating over time. Attaining debt sustainability would require sharp fiscal consolidation and external support from the international community.[1] The authorities broadly concurred with the staff's assessment, and were confident that the envisaged reengagement with the international community will help restore debt sustainability.

[1] This DSA was prepared jointly by IMF and World Bank staff under the joint Fund-Bank Low-Income Country Debt Sustainability Framework (LIC DSF, 2013). Zimbabwe's Country Policy and Institutional Assessment (CPIA) Rating was 2.9 in 2015, and categorized as weak policy performance. Zimbabwe's fiscal year runs from January 1 to December 31. The result of this DSA were discussed with the authorities and they are in broad agreement with its conclusions.

BACKGROUND AND RECENT DEVELOPMENTS

1. **The economic environment has experienced a major deterioration, further eroding Zimbabwe's already precarious fiscal status.** Real GDP growth in 2016 decreased to 0.7 percent from 1.4 percent in 2015. A severe drought resulted in the lowest maize harvest in 25 years, and foreign exchange inflows declined as key export prices remained depressed and country risk increased. Reforms aiming at fostering fiscal discipline were constrained by political difficulties. As a result, annual fiscal expenditures increased by 5 percent of GDP in 2016, while revenues fell by 2 percent of GDP. Public debt reached almost 70 percent of GDP.

2. **The process of reengagement with external creditors has been slower than anticipated.** Arrears to the IMF-administered Poverty Reduction and Growth Trust were cleared in October 2016, allowing Zimbabwe's PRGT eligibility to be restored and the declaration of noncooperation to be lifted. However, discussions are still ongoing over financing and modalities to clear the arrears to the World Bank and the African Development Bank. As reengagement with international institutions is delayed, and reforms on governance, and human and property rights have not proceeded at the expected pace, debt treatment from bilateral creditors also remains constrained. External obligations are being serviced selectively, and with a view to unlocking additional financing.

3. **With limited access to external resources, large fiscal deficits are being financed domestically through central bank advances and T-bill issuance.** Public domestic debt almost doubled to 25 percent of GDP in 2016. The expansionary fiscal stance led to the government's absorption of domestic capital, exacerbating the dollar scarcity in the economy, and crowding out the private sector. A series of administrative measures on capital and current account transactions was introduced in May 2016.

Figure 1. PPG Debt Development
(U.S. dollars millions)

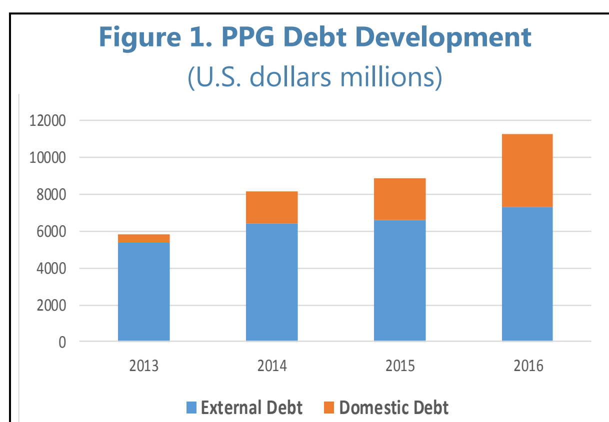
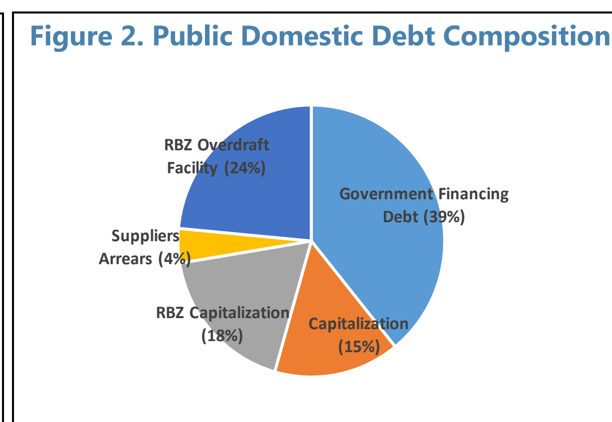


Figure 2. Public Domestic Debt Composition



MACROECONOMIC ASSUMPTIONS

4. The macroeconomic assumptions underlying the previous DSA have been revised to reflect recent developments. The long-term growth outlook has been moderated, reflecting the current challenges, including the crowding out of private sector borrowing, the continued external payment arrears and delays in addressing them, and the perceived difficulties in the investment climate. The fiscal deficit is anticipated to narrow only slowly as the wage and hiring freezes from this year take effect. Equally, the external current account deficit is expected to continue to decline, as import compression persists, and sources of financing remain limited. The private sector is likely to find it hard to attract lines of credit in a context of dollar scarcity. Similarly, a continuation of the country's arrears situation would result in the maintenance of the *status quo* regarding sources of official financing from traditional creditors.

5. Key assumptions: The macroeconomic assumptions that underpin the baseline scenario are as follows:

- **Annual real GDP growth** is projected to be just under 3 percent in 2017, mainly reflecting the rebound in agriculture from a low base last year and some recovery in manufacturing. Over the medium term, however, prospects are weak, with near zero growth (a range of 0.3 to -0.3 percent) through 2022, reflecting subdued private sector activity, a difficult business environment, declining policy credibility, and a likely limited impact of government-led efforts to increase production. Thereafter, the DSA assumes an increase of growth to around 2 percent a year, far lower than its potential under the right policies.

- **Average inflation** is projected to pick up in the short term to 8–9 percent, reflecting sustained monetary financing of the deficit, which in combination with the foreign exchange controls in place would drive up prices of domestically produced and imported goods, before stabilizing at 2 percent over the longer term.

- **Exports** in nominal terms are anticipated to grow at about 3 percent per year over the projection period, reflecting an anticipated production increase in the mining sector, particularly in chrome ore and diamonds.

- **Import** growth is envisaged to be constrained in the near term by the foreign exchange controls, and subsequently reach 3 percent annually in the medium and longer terms.

- **The non-interest current account deficit** is expected to stabilize at around 1 percent of GDP, reflecting limited inward investment and low private sector's capacity to borrow.

- **Government revenues** are projected to reach 21 percent of GDP by 2018, while primary expenditure would fall gradually from 29.8 percent in 2016 to 21 percent by the end of the projection period.

- **A forced fiscal adjustment** is assumed over the medium term. Amid the financing constraint, a continued policy of salary freezes could generate an adjustment in the wage-to-GDP ratio over the medium term. However, the baseline scenario assumes that such an adjustment would be insufficient to restore macroeconomic stability, and thus the persisting deficits, while lower than the current one, would continue to hamper private investment and growth.

- **New external borrowing** is assumed to average just 1½ percent of GDP, with a grant element close to zero, in line with recent trends. Staff assumes that Zimbabwe will continue to receive limited financing from non-traditional creditors only as repayments unlock new credit, especially in the near term. Private sector external borrowing would remain subdued.

- **External arrears** are expected to remain in place, and accumulation of arrears is assumed to be only related to debt currently not being serviced.

- **International reserves** are projected to remain around the current low level, reflecting the difficulties in building buffers under current policies.

DEBT SUSTAINABILITY INDICATORS

A. External DSA

6. Zimbabwe's Public and Publicly Guaranteed (PPG) external debt burden indicators remain elevated, and the external debt overhang is large.[2] PPG external debt is estimated at 44.8 percent of GDP as of end-2016, of which 70 percent stands in arrears (Table 1). Private external debt is estimated at 13 percent of GDP.[3]

7. Zimbabwe remains in external debt distress. As of end-2016, with a present value (PV) of PPG external debt-to-GDP ratio of 41.8 percent, a PV of debt-to-revenue ratio of 192.3 percent, and a PV of debt-to-export ratio of 168.6 percent, Zimbabwe's PPG external debt breached most indicative thresholds. Moreover, per the assumptions in the baseline scenario, external debt in relation to exports remains above the threshold throughout the 20-year projection period by a substantial margin of around 70 percent. (Table 4 and Figure 3). The results suggest that absent much stronger growth or more concessional financing and debt relief, Zimbabwe has little chance of emerging from its debt problems even in the long term. These outturns, together with the existence of substantial arrears and ongoing negotiations on debt restructuring, support the determination that Zimbabwe is in external debt distress.

[2] The external DSA is based on official statistics on the debt contracted and/or guaranteed by the central government, and on estimates for the private sector.

[3] The data on private sector external debt is based on available data and staff estimates; therefore, it might not cover the entirety of the debt stock.

Table 1. Zimbabwe: External Debt Stock as of end-2016
(U.S. dollars million)

	Principal Outstanding	Arrears	Total	Percent of GDP (%)
Public and Publicly Guaranteed	**2,217**	**5,014**	**7,231**	**44.8**
Bilateral Creditors	1,198	2,985	4,183	25.9
Paris Club	223	2,818	3,041	18.9
Non Paris Club	975	167	1,142	7.1
Mutilteral Creditors	448	2,070	2,518	15.6
World Bank	253	1,149	1,402	8.7
AfDB	37	605	642	4.0
EIB	22	228	250	1.6
Others	137	65	202	1.2
RBZ External Debt	530		530	3.3
Private Debtors			**2,117**	**13.1**
Total External Debt			**9,348**	**58.0**

Source: Zimbabwe authorities and IMF staff estimates

Table 2. Zimbabwe: External Debt, 2013–2016
(U.S. dollars million)

	2013	2014	2015	2016
Public and Publicly Guaranteed External Debt	5,389	6,407	6,613	7,231
Medium and Long Term	5,389	6,407	6,613	7,231
Private Sector External Debt	1,862	2,465	2,115	2,117
Medium and Long Term	547	1,404	1,602	1,662
Short Term	1,315	1,061	513	455
Total External Debt Outstanding	**7,251**	**8,872**	**8,728**	**9,348**
Percent of GDP	**47.6**	**56.0**	**54.3**	**58.0**

8. **Declining foreign exchange inflows are a major cause of the weakening external position.** The increase in the stock of external debt has been modest not because of a lower financing need, but due to Zimbabwe's limited access to financing. Nonetheless, weak export competitiveness and the withdrawal of foreign investment have hampered the country's debt service capability. While Zimbabwe may receive some financing from non-traditional creditors, the external financing gaps are projected to widen.

B. Public DSA

9. **Driven by government's rising spending, the stock of domestic debt has increased rapidly.** Central government domestic debt has reached almost 25 percent of GDP, driven mainly by the issuance of T-bills and the use of an overdraft from the Reserve Bank of Zimbabwe (RBZ).

Recapitalization of the RBZ and other public enterprises has also led to an increase in domestic debt, as has the issuance of government paper to commercial banks through the Asset Management Company, ZAMCO, in an effort to reduce the stock of non-performing loans held by the banking system.

Table 3. Zimbabwe: Domestic Debt of Central Government as of end-2016
(U.S. dollars million)

	2013	2014	2015	2016
Government Financing Debt [1/]	226	363	748	1,569
Capitalization [2/]	-	240	286	611
RBZ Capitalization and Debt [3/]	-	801	801	720
Suppliers Arrears	216	233	168	164
RBZ Overdraft Facility	-	126	279	942
Total Domestic Debt	442	1,764	2,282	4,006

Source: Zimbabwean authorities and IMF staff estimates

[1/] Includes T-bills issued for budgetary financing, government debt, and statutory reserves.

[2/] Includes T-bills and T-bonds issued to recapitalize institutions such as Agribank, ZAMCO, etc.

[3/] Includes paper issued to recapitalize RBZ and debts assumed under the RBZ (Debt Assumption Act) of 2015.

10. The projected total public debt (external plus domestic) indicates that the fiscal consolidation assumed in the baseline scenario will prove insufficient. The PV of public-sector debt-to-GDP ratio is projected to increase from 67 percent in 2016 to 80 percent in 2027, a level almost twice as high as the benchmark. The PV of debt-to-revenue ratio and debt service ratios show a similar increasing profile (Table 6 and Figure 4).

STRESS TESTS AND ALTERNATIVE SCENARIOS

11. Stress tests highlight the possibility of an even more challenging debt outlook. Figure 3 presents the results of various stress tests to the baseline scenario, suggesting a worsening of all debt burden indicators. Any scenario based on historical key variables leads to explosive debt levels and unsustainability. Stress tests featuring the use of historic averages of key variables suggest that the PV of external debt-to-GDP ratio could reach 125 percent and the PV of external debt-to-exports ratio could be 654 percent by 2027 (Table 5a). These results suggest the economy is particularly vulnerable to lower-than-anticipated real GDP growth and export growth.

12. An alternative scenario demonstrates the adverse effects of adding to the debt potential liabilities of the broader public sector. While sufficient data is not available to present a full DSA based on the broader public sector, the liabilities of both the local authorities and the

State-Owned Enterprises (SOEs) are high and growing.[4] The debt stock of local governments reached an estimated $555 million in 2015 (3.4 percent of GDP)[5], while the debt of nonfinancial public corporations stood at around $440 million as of end-2016 (2.7 percent of GDP). Contingent liabilities stemming from transport projects are estimated at just under $1 billion (6.2 percent of GDP). For illustrative purposes, if these obligations were to be added to the central government's stock of debt in 2017, the PV of public debt-to-GDP ratio would increase by 12 percentage points to 82 percent. Assuming no adjustment, the gap with the baseline scenario would continue to widen to 22 percent over the projection period, as additional debt service would have to be paid with new borrowing (were the government able to contract such new loans) (Table 7).

CONCLUSION

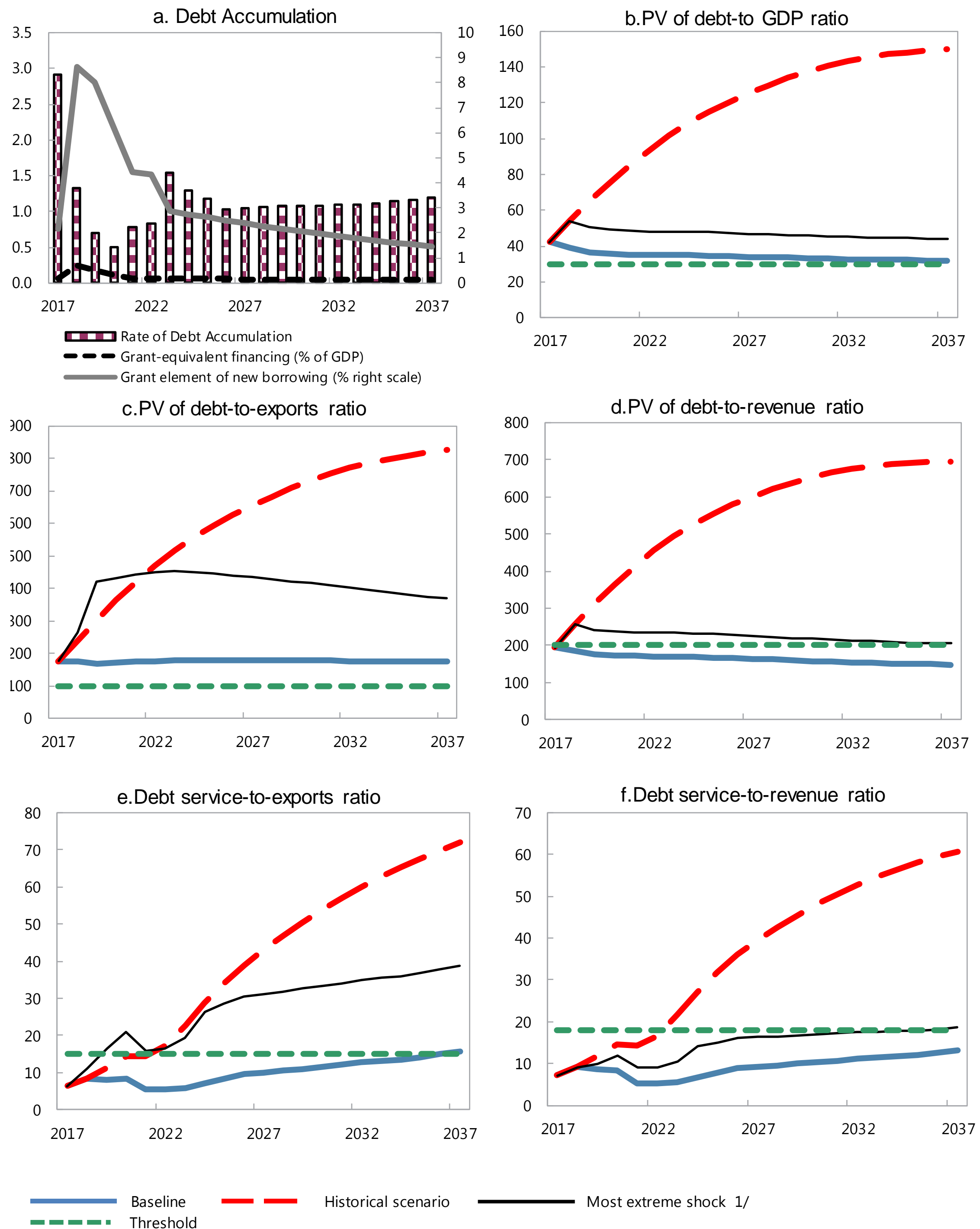
13. Zimbabwe is in debt distress. In addition to the already excessive external debt burden that led the country to incur arrears, Zimbabwe has now accumulated significant domestic debt, to the point where domestic financing of the deficit has begun to undermine the competitiveness of the private sector. Furthermore, the debt indicators are not projected to improve much on current policies, and are estimated to worsen under the various shock scenarios.

14. The adoption of an ambitious set of policies is essential if Zimbabwe is to emerge from its current difficulties. Sharp fiscal adjustment and bold structural reforms to restore growth and attract investment are necessary to this end. Furthermore, external support and debt relief from the international community must be part of the strategy. Supported by a robust reform program, the envisaged reengagement process could bear fruit and restore growth and sustainability.

[4] See Government of Zimbabwe and World Bank (2017), Public Expenditure Review, forthcoming, for a fuller discussion.

[5] ibid.

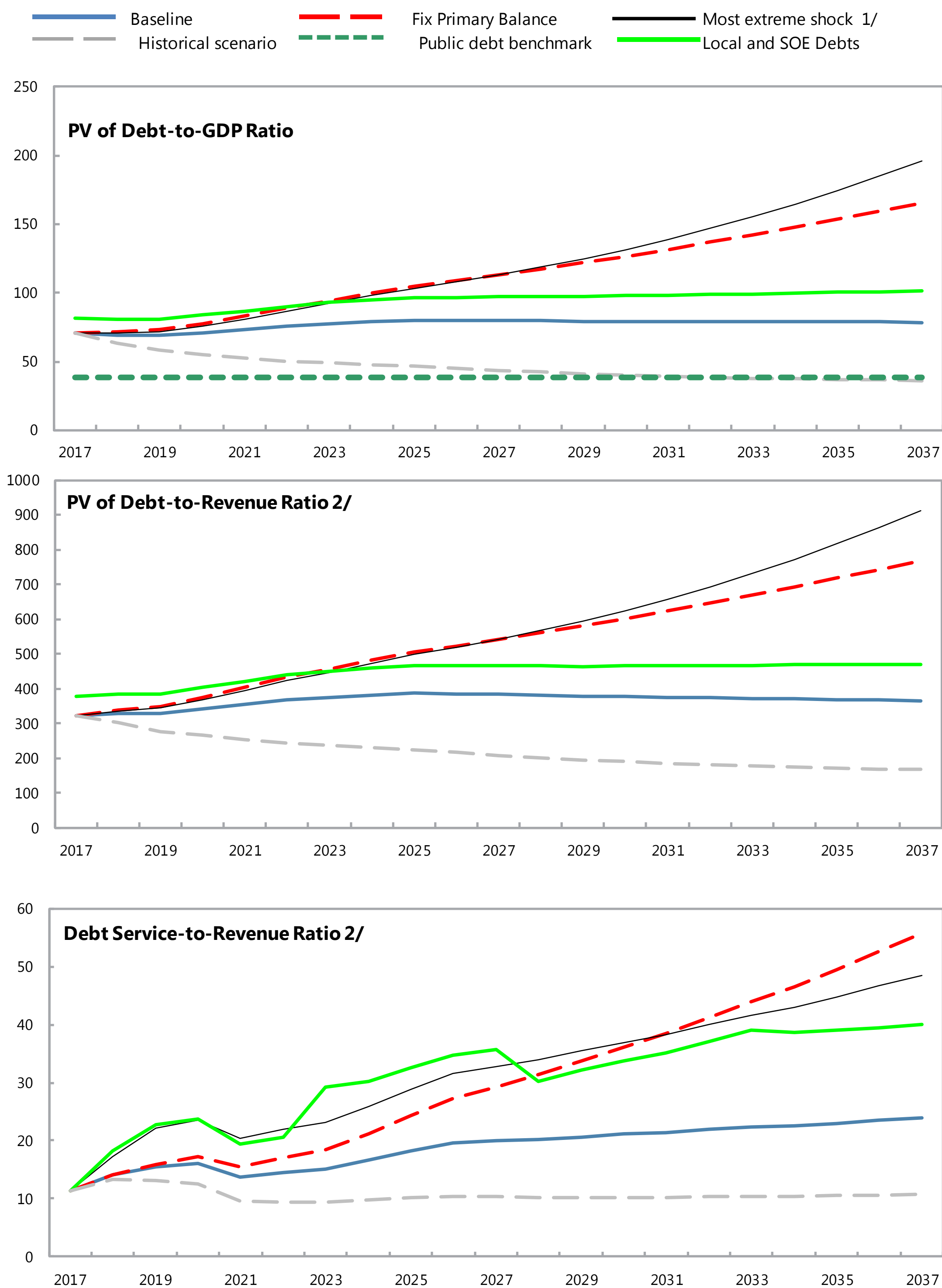
Figure 3. Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2017–2037[1]



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2027. In figure b. it corresponds to a One-time depreciation shock; in c. to a Exports shock; in d. to a One-time depreciation shock; in e. to a Exports shock and in figure f. to a Exports shock.

Figure 4. Indicators of Public Debt Under Alternative Scenarios, 2017–2037



Sources: Country authorities, and staff estimates and projections.
1/ The most extreme stress test is the tes that yields the highest ratio on or before 2027.
2/ Revenues are defined inclusive of grants.

Table 4. Zimbabwe: External Debt Sustainability Framework, Baseline Scenario, 2014–2037

(In percent of GDP, unless otherwise indicated)

	Actual			Historical Average 6/	Standard Deviation 6/	Projections									
	2014	2015	2016			2017	2018	2019	2020	2021	2022	2017-2022 Average	2027	2037	2023-2037 Average
External debt (nominal) 1/	**56.0**	**54.3**	**58.0**			**55.3**	**51.2**	**47.9**	**46.6**	**45.7**	**45.2**	**48.7**	**43.2**	**43.0**	
of which: public and publicly guaranteed (PPG)	40.5	41.1	44.8			44.7	41.6	38.9	37.8	37.2	36.9		35.8	34.6	
Change in external debt	8.4	-1.7	3.7			-2.7	-4.1	-3.3	-1.3	-0.9	-0.5		-0.4	0.3	
Identified net debt-creating flows	10.3	6.0	1.8			1.3	-0.3	-0.3	0.6	1.4	1.8		0.9	1.6	
Non-interest current account deficit	**13.6**	**8.0**	**2.8**	**15.4**	**11.7**	**2.4**	**-0.4**	**-0.9**	**-0.3**	**0.4**	**0.6**		**0.8**	**0.9**	0.8
Deficit in balance of goods and services	23.4	18.6	12.3			11.1	7.7	6.6	6.6	6.5	6.4		6.1	5.7	
Exports	24.3	24.3	24.8			24.1	22.6	21.7	20.8	20.2	19.9		19.1	18.2	
Imports	47.7	42.9	37.1			35.1	30.3	28.4	27.4	26.8	26.3		25.3	23.9	
Net current transfers (negative = inflow)	-12.6	-13.4	-12.1	-14.1	1.5	-11.2	-10.2	-9.3	-8.8	-8.3	-8.0		-6.8	-5.2	-6.4
of which: official	-4.6	-4.9	-4.7			-4.2	-3.8	-3.5	-3.4	-3.4	-3.4		-3.2	-2.9	
Other current account flows (negative = net inflow)	2.8	2.9	2.6			2.5	2.1	1.8	1.9	2.2	2.2		1.5	0.4	
Net FDI (negative = inflow)	**-3.0**	**-2.5**	**-2.1**	**-2.3**	**0.7**	**-0.8**	**-0.7**	**-0.5**	**-0.5**	**-0.6**	**-0.6**		**-0.6**	**-0.5**	-0.5
Endogenous debt dynamics 2/	**-0.3**	**0.4**	**1.1**			**-0.3**	**0.8**	**1.1**	**1.4**	**1.6**	**1.7**		**0.6**	**1.1**	
Contribution from nominal interest rate	1.5	1.3	1.3			1.2	1.2	1.2	1.2	1.3	1.3		1.5	2.0	
Contribution from real GDP growth	-1.3	-0.8	-0.4			-1.5	-0.4	-0.1	0.1	0.3	0.4		-0.8	-0.8	
Contribution from price and exchange rate changes	-0.6	0.0	0.2			...	...	...	...	...	...		...	...	
Residual (3-4) 3/	**-1.9**	**-7.7**	**1.9**			**-4.0**	**-3.8**	**-3.0**	**-1.9**	**-2.3**	**-2.3**		**-1.3**	**-1.2**	
of which: exceptional financing	-1.7	-0.7	1.0			-0.8	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 4/	...	...	54.9			52.7	48.9	45.8	44.6	43.8	43.4		41.6	40.5	
In percent of exports	...	...	221.6			219.2	215.9	210.5	214.7	216.5	218.3		217.2	222.8	
PV of PPG external debt	**...**	**...**	**41.8**			**42.1**	**39.3**	**36.7**	**35.8**	**35.3**	**35.1**		**34.1**	**32.0**	
In percent of exports	**...**	**...**	**168.6**			**175.1**	**173.7**	**168.9**	**172.2**	**174.2**	**176.3**		**178.1**	**176.4**	
In percent of government revenues	**...**	**...**	**192.3**			**194.0**	**186.7**	**175.8**	**173.2**	**171.2**	**170.7**		**163.5**	**148.7**	
Debt service-to-exports ratio (in percent)	**10.1**	**9.4**	**11.3**			**11.5**	**13.0**	**12.6**	**12.9**	**9.8**	**10.0**		**14.0**	**20.0**	
PPG debt service-to-exports ratio (in percent)	**3.7**	**3.7**	**5.4**			**6.4**	**8.4**	**8.2**	**8.4**	**5.4**	**5.5**		**10.0**	**15.6**	
PPG debt service-to-revenue ratio (in percent)	**3.7**	**3.7**	**6.1**			**7.1**	**9.1**	**8.5**	**8.4**	**5.3**	**5.4**		**9.2**	**13.2**	
Total gross financing need (Millions of U.S. dollars)	3390.6	2317.7	1076.3			1203.9	630.5	541.8	689.2	692.9	738.7		1082.7	1932.3	
Non-interest current account deficit that stabilizes debt ratio	5.2	9.7	-0.9			5.1	3.7	2.4	1.0	1.3	1.2		1.3	0.5	
Key macroeconomic assumptions															
Real GDP growth (in percent)	2.8	1.4	0.7	7.9	6.9	2.8	0.8	0.3	-0.3	-0.7	-0.9	0.3	2.0	2.0	2.0
GDP deflator in US dollar terms (change in percent)	1.2	0.1	-0.3	1.9	1.7	3.2	9.6	8.7	4.3	4.4	4.0	5.7	2.0	2.0	2.0
Effective interest rate (percent) 5/	3.3	2.3	2.4	2.5	0.5	2.2	2.4	2.6	2.7	2.8	2.9	2.6	3.5	4.8	3.9
Growth of exports of G&S (US dollar terms, in percent)	-6.3	1.3	2.4	16.1	37.4	3.0	4.0	4.7	-0.6	1.0	1.1	2.2	3.4	3.5	3.4
Growth of imports of G&S (US dollar terms, in percent)	-5.6	-8.7	-13.2	0.9	20.2	0.4	-4.7	2.1	0.4	1.4	1.2	0.1	3.3	3.5	3.4
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	2.2	8.6	8.0	6.2	4.4	4.3	5.6	2.4	1.5	2.1
Government revenues (excluding grants, in percent of GDP)	23.8	24.3	21.7			21.7	21.1	20.9	20.7	20.6	20.5		20.9	21.5	21.1
Aid flows (in Millions of US dollars) 7/	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
of which: Grants	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
of which: Concessional loans	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			0.1	0.2	0.2	0.1	0.1	0.1		0.1	0.0	0.1
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			2.2	8.6	8.0	6.2	4.4	4.3		2.4	1.5	2.1
Memorandum items:															
Nominal GDP (Millions of US dollars)	15834	16072	16124			17105	18904	20601	21434	22218	22877		27930	41425	
Nominal dollar GDP growth	4.0	1.5	0.3			6.1	10.5	9.0	4.0	3.7	3.0	6.0	4.0	4.0	4.0
PV of PPG external debt (in Millions of US dollars)			6735.6			7206.0	7431.7	7563.0	7665.1	7832.7	8018.9		9521.9	13265.8	
(PVt-PVt-1)/GDPt-1 (in percent)						2.9	1.3	0.7	0.5	0.8	0.8	1.2	1.0	1.2	1.1
Gross workers' remittances (Millions of US dollars)	1166.0	1277.2	1102.8			1105.0	1107.2	1096.1	1041.3	989.3	959.6		881.9	827.2	
PV of PPG external debt (in percent of GDP + remittances)	...	...	39.1			39.6	37.1	34.9	34.1	33.8	33.6		33.0	31.4	
PV of PPG external debt (in percent of exports + remittances)	...	...	132.1			138.1	138.0	135.7	139.6	142.8	145.6		152.9	158.9	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	4.2			5.0	6.7	6.5	6.8	4.4	4.6		8.6	14.1	

Sources: Country authorities and IMF staff estimates and projections

1/ Includes both public and private sector external debt.

2/ Derived as $[r - g - \rho(1+g)]/(1+g+\rho+g\rho)$ times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Assumes that PV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

7/ Defined as grants, concessional loans, and debt relief.

8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 5a. Zimbabwe: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2017–2037

(In percent)

	Projections							
	2017	2018	2019	2020	2021	2022	**2027**	2037
PV of debt-to GDP ratio								
Baseline	42	39	37	36	35	35	**34**	32
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	42	54	65	75	85	93	**125**	150
A2. New public sector loans on less favorable terms in 2017-2037 2/	42	40	38	37	37	37	**38**	43
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	42	39	36	35	35	35	**34**	32
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	42	45	52	51	51	51	**47**	38
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	42	43	43	42	42	42	**40**	38
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	42	36	29	28	27	27	**27**	29
B5. Combination of B1-B4 using one-half standard deviation shocks	42	39	36	34	34	34	**33**	33
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	42	54	51	49	49	48	**47**	44
PV of debt-to-exports ratio								
Baseline	175	174	169	172	174	176	**178**	176
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	175	239	300	363	418	470	**654**	826
A2. New public sector loans on less favorable terms in 2017-2037 2/	175	176	173	178	182	186	**200**	236
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	175	174	169	172	174	176	**178**	176
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	175	262	419	432	440	449	**434**	368
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	175	174	169	172	174	176	**178**	176
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	175	159	134	135	136	136	**144**	160
B5. Combination of B1-B4 using one-half standard deviation shocks	175	175	174	176	178	179	**185**	193
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	175	174	169	172	174	176	**178**	176
PV of debt-to-revenue ratio								
Baseline	194	187	176	173	171	171	**163**	149
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	194	257	313	365	411	455	**601**	696
A2. New public sector loans on less favorable terms in 2017-2037 2/	194	190	180	179	179	180	**183**	199
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	194	186	174	172	170	169	**162**	147
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	194	213	248	247	246	247	**226**	176
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	194	204	208	205	203	202	**194**	176
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	194	171	139	136	133	132	**132**	135
B5. Combination of B1-B4 using one-half standard deviation shocks	194	184	170	167	164	163	**160**	153
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	194	257	242	238	236	235	**225**	205

Table 5b. Zimbabwe: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2017–2037 (concluded)

(In percent)

Baseline	6	8	8	8	5	6	**10**	16
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	6	8	11	14	14	17	**43**	72
A2. New public sector loans on less favorable terms in 2017-2037 2/	6	8	5	5	5	5	**10**	19
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	6	8	8	8	5	6	**10**	16
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	6	11	16	21	16	17	**31**	39
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	6	8	8	8	5	6	**10**	16
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	6	8	7	7	3	4	**6**	12
B5. Combination of B1-B4 using one-half standard deviation shocks	6	9	9	9	5	5	**9**	16
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	6	8	8	8	5	6	**10**	16
Debt service-to-revenue ratio								
Baseline	7	9	8	8	5	5	**9**	13
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	7	9	12	14	14	17	**39**	61
A2. New public sector loans on less favorable terms in 2017-2037 2/	7	9	5	5	5	5	**9**	16
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	7	9	8	8	5	5	**9**	13
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	7	9	10	12	9	9	**16**	19
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	7	10	10	10	6	6	**11**	16
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	7	9	8	7	3	3	**6**	10
B5. Combination of B1-B4 using one-half standard deviation shocks	7	9	9	8	5	5	**8**	13
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	7	12	12	12	7	7	**13**	18
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	-2	-2	-2	-2	-2	-2	**-2**	-2

Sources: Country authorities, and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).
4/ Includes official and private transfers and FDI.
5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.
6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Table 6. Zimbabwe: Public Sector Debt Sustainability Framework, Baseline Scenario, 2014–2037

(In percent of GDP, unless otherwise indicated)

	Actual			Average 5/	Standard Deviation 5/	Estimate	Projections								
	2014	2015	2016			2017	2018	2019	2020	2021	2022	2017-22 Average	2027	2037	2023-37 Average
Public sector debt 1/	51.6	55.3	69.7			72.9	71.8	70.9	72.7	74.9	77.4		81.6	81.1	
of which: foreign-currency denominated	51.6	55.3	69.7			72.9	71.8	70.9	72.7	74.9	77.4		81.6	81.1	
Change in public sector debt	13.1	3.7	14.4			3.2	-1.1	-0.9	1.8	2.2	2.6		-0.2	-0.1	
Identified debt-creating flows	-0.6	0.6	8.6			1.9	-2.6	-1.8	1.3	1.5	1.9		0.6	-0.1	
Primary deficit	0.6	0.8	8.1	1.4	2.8	4.7	2.9	2.2	2.1	1.9	1.6	2.6	0.7	-0.5	0.4
Revenue and grants	23.8	24.3	21.7			21.7	21.1	20.9	20.7	20.6	20.5		20.9	21.5	
of which: grants	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Primary (noninterest) expenditure	24.4	25.1	29.8			26.4	24.0	23.1	22.7	22.4	22.2		21.5	21.1	
Automatic debt dynamics	-1.2	-0.2	0.6			-2.8	-5.5	-4.0	-0.7	-0.4	0.2		-0.1	0.4	
Contribution from interest rate/growth differential	-1.2	-0.2	0.6			-2.8	-5.5	-4.0	-0.7	-0.4	0.2		-0.1	0.4	
of which: contribution from average real interest rate	-0.2	0.5	0.9			-0.9	-4.9	-3.8	-0.9	-0.9	-0.5		1.5	2.0	
of which: contribution from real GDP growth	-1.0	-0.7	-0.4			-1.9	-0.6	-0.2	0.2	0.5	0.7		-1.6	-1.6	
Contribution from real exchange rate depreciation	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		...	...	
Other identified debt-creating flows	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	13.6	3.2	5.7			1.3	1.5	0.9	0.5	0.7	0.7		-0.8	0.0	
Other Sustainability Indicators															
PV of public sector debt	...	...	66.6			70.4	69.5	68.7	70.7	73.0	75.6		79.9	78.5	
of which: foreign-currency denominated	...	...	66.6			70.4	69.5	68.7	70.7	73.0	75.6		79.9	78.5	
of which: external	...	...	41.8			42.1	39.3	36.7	35.8	35.3	35.1		34.1	32.0	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	3.4	4.2	13.7			13.2	12.5	12.6	13.4	13.4	14.1		16.3	16.4	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	306.7			324.1	329.9	329.1	342.1	354.3	368.4		383.2	364.5	
PV of public sector debt-to-revenue ratio (in percent)	...	...	306.7			324.1	329.9	329.1	342.1	354.3	368.4		383.2	364.5	
of which: external 3/	...	...	192.3			194.0	186.7	175.8	173.2	171.2	170.7		163.5	148.7	
Debt service-to-revenue and grants ratio (in percent) 4/	4.4	5.6	9.2			11.4	14.2	15.4	16.1	13.6	14.4		19.9	24.0	
Debt service-to-revenue ratio (in percent) 4/	4.4	5.6	9.2			11.4	14.2	15.4	16.1	13.6	14.4		19.9	24.0	
Primary deficit that stabilizes the debt-to-GDP ratio	-12.4	-2.9	-6.3			1.4	4.0	3.1	0.2	-0.3	-0.9		0.9	-0.4	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	2.8	1.4	0.7	7.9	6.9	2.8	0.8	0.3	-0.3	-0.7	-0.9	0.3	2.0	2.0	2.0
Average nominal interest rate on forex debt (in percent)	0.7	1.1	1.4	0.7	0.4	1.8	2.2	2.9	3.0	3.1	3.3	2.7	3.9	4.5	4.1
Real exchange rate depreciation (in percent, + indicates depreciation)	0.0	0.0	0.0	0.0	0.0	0.0	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	1.2	0.1	-0.3	1.9	1.7	3.2	9.6	8.7	4.3	4.4	4.0	5.7	2.0	2.0	2.0
Growth of real primary spending (deflated by GDP deflator, in percent)	-4.5	4.0	19.6	3.0	7.7	-8.9	-8.5	-3.2	-2.0	-1.9	-2.1	-4.4	1.7	1.8	1.7
Grant element of new external borrowing (in percent)	...	...	...	...	...	2.2	8.6	8.0	6.2	4.4	4.3	5.6	2.4	1.5	...

Sources: Country authorities and IMF staff estimates and projections

1/ [Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also, whether net or gross debt is used.]
2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.
3/ Revenues excluding grants.
4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.
5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 7. Zimbabwe: Sensitivity Analysis for Key Indicators of Public Debt 2017–2037

	Projections							
	2017	2018	2019	2020	2021	2022	2027	2037
PV of Debt-to-GDP Ratio								
Baseline	70	69	69	71	73	76	80	79
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	70	64	58	55	52	50	44	36
A2. Primary balance is unchanged from 2017	70	71	73	78	83	89	113	165
A3. Permanently lower GDP growth 1/	70	71	72	76	81	87	113	196
A4. Including Local and SOE Debts	82	81	81	84	87	90	97	101
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2018-2019	70	69	68	70	72	74	78	74
B2. Primary balance is at historical average minus one standard deviations in 2018-2019	70	71	72	74	76	79	84	83
B3. Combination of B1-B2 using one half standard deviation shocks	70	67	64	65	65	66	62	43
B4. One-time 30 percent real depreciation in 2018	70	98	96	98	100	103	111	122
B5. 10 percent of GDP increase in other debt-creating flows in 2018	70	80	79	81	83	86	91	91
PV of Debt-to-Revenue Ratio 2/								
Baseline	324	330	329	342	354	368	383	364
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	324	302	277	265	253	243	209	168
A2. Primary balance is unchanged from 2017	324	339	349	376	403	433	542	768
A3. Permanently lower GDP growth 1/	324	336	344	368	393	423	543	911
A4. Including Local and SOE Debts	377	384	386	405	421	439	465	470
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2018-2019	324	329	325	337	349	362	372	344
B2. Primary balance is at historical average minus one standard deviations in 2018-2019	324	336	345	358	371	385	401	383
B3. Combination of B1-B2 using one half standard deviation shocks	324	318	309	313	317	322	297	197
B4. One-time 30 percent real depreciation in 2018	324	464	458	472	486	503	530	566
B5. 10 percent of GDP increase in other debt-creating flows in 2018	324	379	376	391	404	419	436	422
Debt Service-to-Revenue Ratio 2/								
Baseline	11	14	15	16	14	14	20	24
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	11	13	13	12	10	9	10	11
A2. Primary balance is unchanged from 2017	11	14	16	17	15	17	29	56
A3. Permanently lower GDP growth 1/	11	14	16	17	15	16	28	62
A4. Including Local and SOE Debts	11	18	23	24	19	21	36	40
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2018-2019	11	14	15	16	13	14	19	22
B2. Primary balance is at historical average minus one standard deviations in 2018-2019	11	14	16	17	15	15	22	26
B3. Combination of B1-B2 using one half standard deviation shocks	11	14	14	15	12	13	15	11
B4. One-time 30 percent real depreciation in 2018	11	17	22	24	20	22	33	48
B5. 10 percent of GDP increase in other debt-creating flows in 2018	11	14	18	19	16	17	25	30

Sources: Country authorities; and staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

Statement by Mr. Mkwezalamba, Executive Director and Mr. Nakunyada Advisor to the Executive Director, on Zimbabwe
July 5, 2017

Introduction

1. Our Zimbabwean authorities appreciate the candid and constructive engagement with staff during the recent Article IV Consultation mission. Broadly, they concur with the staff's assessment of economic developments and the underlying policy challenges.

2. **Over the recent past, economic growth in Zimbabwe has decelerated, against the backdrop of low commodity prices, adverse weather conditions, and subdued capital inflows.** To correct the underlying macroeconomic imbalances and boost growth prospects, the authorities are taking steps to improve fiscal performance, implement structural reforms, and safeguard financial stability.

Recent Economic Developments and Outlook

3. **Economic growth slowed down from 1.1 percent in 2015 to 0.7 percent in 2016 due to low commodity prices, tight liquidity conditions, limited offshore financing, and successive droughts.** This notwithstanding, the authorities are optimistic that real GDP growth will rebound to 3.7 percent in 2017, underpinned by a favourable agricultural season and positive spill-over effects on the agro-processing industry. The partial recovery in commodity prices is expected to enhance viability of mining operations, and culminate in improved output. Looking ahead, growth prospects are subject to downside risks emanating from fiscal imbalances, persistent liquidity constraints, and susceptibility to weather-related shocks.

4. **Inflation turned positive in 2017 following a prolonged episode of negative inflation.** Renewed inflationary pressures emerged, stemming from premiums in the informal foreign exchange market. Consequently, year on year inflation rose from -0.7% in January 2017 to 0.75% in May 2017. Restraint by the Reserve Bank of Zimbabwe (RBZ) in issuing bond notes and accompanying liquidity constraints have moderated the exchange rate pass-through effects and stabilized inflation within single digit levels.

5. **Export recovery and import compression resulted in an improved external sector position.** The firming of commodity prices, as well as increased artisanal gold mining, and chrome and tobacco production spurred export recovery in 2016. At the same time, the compression effects of import controls introduced in 2016 further improved external current account performance. This notwithstanding, external sector performance remains subject to risks emanating from import dependence, commodity price shocks, subdued capital inflows, and reserve inadequacy.

Fiscal Policy and Public Financial Management Reforms

6. **The country's fiscal position has deteriorated largely due to depressed revenues and elevated expenditures.** The deterioration in terms of trade coupled with the economic slowdown amplified fiscal revenue shortfalls. On the other hand, extra- budgetary expenditures related to grain imports necessitated by drought conditions, as well as elevated employment costs, shored-up government expenditures in 2015 and 2016.

7. **To place the fiscal deficit on a sustainable trajectory, the authorities are prioritizing expenditure rationalization and revenue enhancing measures.** Towards this end, they instituted measures to contain expenditures through the freezing and abolishment of non-essential posts while protecting critical hiring in education and health. Moreover, they have successfully eliminated duplications and redundancies in the civil service, and tightened employment controls.

8. **The authorities are aware of the budgetary implications of the support extended to the agriculture sector.** This notwithstanding, they view, as warranted, targeted support provided to maize farmers to ensure food self-sufficiency, and avoid unbudgeted expenditures related to drought-induced food imports, as has happened in the past. In view of inadequate lending by the banking sector to maize producers, the government intervened to promote the production of maize as the staple crop. This interim financing arrangement is envisaged to gradually decline going forward, as private sector participation is expected to complement government efforts in maize and wheat production. Accordingly, the fiscal position is expected to improve as government intervention in the agricultural sector declines.

9. **Improved tax efficiency and administration measures are beginning to bear fruit.** The introduction of the VAT system of recording taxable transactions has effectively closed loopholes, improved effectiveness and efficiency, and enhanced revenue collection, particularly from the retail sector. In addition, the Zimbabwe Revenue Authority (ZIMRA) introduced the electronic cargo tracking system in early 2017, which is expected to enhance efficiency in clearance and management of transit cargo, and significantly reduce transit fraud. Against this background, revenue collections exceeded targeted levels in the first quarter of 2017.

10. **Progress has been made in Public Financial Management (PFM) reforms aimed to strengthen the regulatory framework that supports government's financial oversight role over public entities.** In this vein, the authorities are working in close collaboration with key stakeholders to further improve the effectiveness of public resource use and

accountability. Further, they are taking steps to roll-out the PFM system from provincial to district level for all ministries by the end of 2017.

Debt Management

11. **Limited progress has been made towards clearance of arrears to multilateral creditors.** In line with the country's arrears clearance plan presented to creditors in Lima in October 2015, the authorities cleared their PRGT obligations in October 2016, resulting in the subsequent lifting of remedial measures by the Fund. In this respect, the authorities have continued discussions with the World Bank and the African Development Bank to settle debt arrears and advance the re-engagement agenda. The World Bank conducted a TA mission to Zimbabwe earlier in 2017 to assess the competitiveness of the country's sources of finance. In view of the favourable assessment by the World Bank, the authorities are keenly awaiting feedback on potential reflows that would be unlocked once arrears have been cleared. The resolution of these outstanding issues is expected to provide substantial impetus to the authorities' efforts to amicably resolve debt obligations, and set the economic reform agenda on a sound footing.

Financial Sector Policy Measures

12. **The financial sector is characterised by well capitalized and profitable banks**. Non-performing loans (NPLs) declined from 20.5 percent in 2015 to 7.9 percent in 2016 following the establishment of a special purpose vehicle, the Zimbabwe Asset Management Company (ZAMCO), to acquire collateralized NPLs from banks. Further, the operationalisation of a credit reference system in January 2017 is expected to nurture a credit culture among borrowers, and improve credit risk management. Moreover, the authorities are at an advanced stage to establish a collateral registry that would allow for acceptance of movable assets as collateral, and promote access to credit by households, large corporates, and small to medium scale enterprises (SMEs).

13. **Consistent with Basel II requirements, the authorities have taken measures to mitigate operational and market risks, and strengthen management and governance.** The RBZ has also made significant progress in enhancing macro-prudential tools within the context of the Basel III framework. In this vein, the authorities expect to finalize the macro-prudential framework by the end of 2017. The framework will improve the assessment of the stability of the financial system. In addition, the Banking Amendment Act of May 2016 provides for the establishment of a comprehensive regulatory framework on corporate governance and risk management within institutions, consumer protection, and problem bank resolution.

14. **The RBZ established the Multi-Disciplinary Financial Stability Committee in 2016, comprising all financial regulators**. The Committee focuses on identifying emerging financial sector vulnerabilities and recommending pro-active policy measures required to maintain financial sector stability. Moreover, the authorities are in the process of implementing various initiatives to improve access to financial services by all citizens, under the National Financial Inclusion Strategy launched in 2016. The strategy aims to mainstream financially excluded segments of the population through the provision of tailored financing packages to meet the needs of SMEs, women, small holder farmers, and the youth.

15. **The authorities are vigilantly monitoring developments in the financial sector in view of potential vulnerabilities emanating from fiscal imbalances.** Notwithstanding the risks associated with the discounting of treasury bills (T-Bills), banks are strategically investing in these short-term instruments as a measure to convert NPLs into assets that generate returns. The authorities also view ample capital buffers as important to cushion banks from unrealized losses associated with the discounting of government T-Bills.

Import Management Measures

16. **The regulation of selected commercial imports is a temporary measure geared to help resuscitate domestic industrial production.** Under the import management measures, the authorities imposed restrictions on selected products to protect the domestic industry from stiff competition posed by low cost producers. These measures are aimed to reverse the de-industrialization effects of the hyperinflationary era. Once the domestic industries have completed the recapitalization and retooling phase, they envisage the lifting of these temporary measures and adhere to regional trade commitments. Relatedly, banks have increased the allocation of scarce foreign exchange to all sectors, following improved foreign exchange inflows realized from the first quarter of 2017.

Structural Reform Measures

17. **Subject to resource constraints, the authorities are pressing ahead with structural reforms aimed at enhancing the country's investment appeal.** In this regard, their policy efforts are currently directed towards the ease of doing business reforms. In the absence of full monetary autonomy, policy actions to reduce the cost of doing business are aimed to reduce the real exchange rate overvaluation, and improve competitiveness. Reflecting the positive outcomes stemming from the ease of doing business reforms, turnaround times have been reduced for: starting a business from 90 to 15 days; approval of construction permits from 448 to 120 days; and property registration from 36 to 14 days.

18. **The attraction of foreign direct investment ranks high on the authorities' development agenda**. In this respect, the authorities are finalizing the establishment of the One Stop Investment Shop to streamline routine investment procedures and expedite approval processes. Completion of on-going projects to expand hydropower generation capacity and improve the road network to support cross-border trade are also expected to reduce the cost of doing business. Further, the government passed into law the Special Economic Zones Bill in 2016 to help boost foreign direct investment and promote diversification. These enclaves offer flexible labor laws, and simplified processes related to the granting of residence and work permits.

19. **Government is also reviewing the legal and regulatory framework to support structural reform efforts**. To this end, the authorities recently gazetted 13 Bills that seek to guide the liquidation of unviable firms; ensure the amicable resolution of commercial disputes; modernize procurement processes; allow for electronic management of the Deeds registry; and streamline and simplify licensing procedures.

20. **Finally, the authorities are finalizing turnaround, growth, and transformation strategies for state owned enterprises (SOEs) to set them on a viable footing, lessen their burden on the budget, improve accountability, and enhance service delivery**. Further**,** Cabinet recently approved the draft Public Sector Governance Bill that seeks to promote sound corporate governance, ethical leadership, professionalism, and accountability in public institutions. Technical support provided by the World Bank is expected to help the authorities develop accompanying regulations for the proposed Act.

Conclusion

21. **Our Zimbabwean authorities value Fund advice and agree with staff on the need to accelerate the implementation of reforms**. This notwithstanding, lack of access to external financing has constrained the pace of reforms. In this context, they continue to prioritize initiatives to clear debt arrears and advance their re-engagement with development partners, to support the reform agenda. More importantly, the authorities look forward to continued close collaboration with the Fund to help strengthen policies and unlock external support.