International Monetary Fund
African Department

“Where is Zimbabwe heading”?

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The views expressed do not necessarily reflect the views of the IMF or the Executive Board of the IMF.

Outlook

- Zimbabwe Economic outlook
- Reengagement: what are the challenges
- Way forward

ECONOMIC OUTLOOK

Genesis of the Problem

- After a period of stability in 2010-2014, largely reflecting fiscal prudence and dollarization in the aftermath of hyperinflation, the country again finds itself in crisis.
- Several years of unsustainable fiscal deficits that were financed via central bank creation of quasi-money instruments have led to an inflation-wage-exchange rate depreciation spiral.
- Unsustainable fiscal deficits in 2017 and 2018, financed by RBZ money creation, have fueled an ever-growing parallel market for the quasi-currency (RTGS).
- Maintenance of official parity of the RTGS with the US dollar, provided opportunities for rent seeking as exchange rate distortions crushed exporters to the benefit of well-connected importers.

Staff Monitored Program

- **The SMP is anchored on the policies laid out in the authorities' TSP and supports the reform agenda:**
  - Assist the authorities to implement and monitor the key policies outlined in their TSP
  - 2019 budget halts central bank financing of the budget
  - The program would help Zimbabwe build a track record of sound economic policies towards normalizing relations with external creditors
  - Safeguard and protect the most vulnerable

SMP main objectives:

(i) **reduce the fiscal deficit** to restore macroeconomic stability, while maintaining investment in infrastructure and priority social spending;

(ii) **stop monetary accommodation** of the fiscal deficit to stabilize inflation and the exchange rate;

(iii) **increase financial sector stability** by implementing financial sector reforms and tightening the regulatory framework;

(iv) **address governance and corruption vulnerabilities**; and

(v) **advance the structural reform agenda**, including in Public Financial Management (PFM) and revenue administration, as well as State-Owned Enterprise Reform.

SMP main objectives (Con't)

- *Substantial fiscal consolidation* . From a deficit of 10 percent of GDP in 2017 to 4 percent of GDP in 2019 (the authorities are currently running a fiscal surplus, so fiscal effort greater than envisaged).
- *Stabilizing the new currency* While initially stable around 3.5:1, the currency slid to 13:1 due to delays in introducing monetary/FX market reforms and a lack of confidence in policy implementation
- *Address macroeconomic imbalances and remove distortions* , including multiple currency practices. The CA deficit has been eliminated, largely due to import compression and FX restrictions.
- On June 24th, *the RBZ converted the RTGS$ into a resurrected Zimbabwe* dollar and made it the sole legal tender of the country. At the same time, RBZ raised interest rates to 50% (from 15 %) and allowed a larger portion of FX surrender requirements to flow directly into the interbank market. Subsequent to these reforms, the currency has stabilized at about 10:1 -- a much more depreciated level than was anticipated at the time of the February reform

Quantitative Targets

Table 1. Zimbabwe: Proposed Quantitative Targets[1]

(in units as indicated)

	2018	2019		
	Dec.	Jun.	Sep.	Dec.
	Actual	Prog.	Prog.	Prog.
1. Floor on the primary budget balance of the central government (RTGS$ million) [2]	…	-1,203	-1,604	-2,005
2. Floor on protected social spending (RTGS$ million) [2]	…	225	500	750
3. Floor on the stock of net official international reserves (in US$ million)	-1,267	-1,267	-1,267	-1,267
4. Continuous ceiling on the stock of new non-concessional external debt contracted or guaranteed by the public sector with original maturity of one year or more (in US$ million) [3]	…	0	0	0
5. Ceiling on changes in net domestic assets of the RBZ (RTGS$ million) [4]	…	300	350	400
6. Ceiling on credit to the nonfinancial public sector from the RBZ (RTGS$ million) [4]	…	0	0	0

[1] Program performance will be monitored based on the quantitative targets for June, September, and December 2019.

[2] Value of cumulative flows since December 31 of the previous year.

for priority infrastructure projects.

[3] Cumulative from April 30, 2019.

[4] Cumulative from March 1st 2019. For the NDA target, excludes foreign exchange valuation changes.

SMP Structural Benchmarks

Table 2. Zimbabwe: SMP Structural Benchmarks

Benchmark	Objective	Completion Date
Cabinet to approve a revised 2019 budget consistent with a deficit of RTGS$2.9 billion (¶9 and ¶10)	Restore macroeconomic stability	Prior Action
Issue instructions to ensure that no payments shall by made by the RBZ on behalf of Government without explicit and case-by-case authorization by the MoFED (¶13)	Improve PFM, budget execution, and fiscal discipline	Prior Action
Adopt regulations implementing the Public Financial Management (PFM) Act., including to ensure all expenditure commitments are recorded in IFMIS (¶13)	Improve governance, PFM, and budget monitoring/execution	June 2019
Complete a comprehensive stock-take of domestic expenditure arrears across the central government as of end-2018 (¶17)	Improve PFM, budget execution, and fiscal discipline	September 2019
Complete a review of agricultural support programs and develop an action plan based on its findings (¶10)	Improve targeting and efficiency of agricultural support programs	September 2019
Extend the coverage of IFMIS to 37 Districts by establishing 31 additional kiosks (¶13)	Improve governance, PFM, and budget monitoring/execution	September 2019
Submit to Parliament draft amendments to the Banking Law to address gaps identified by the FSSR (¶22)	Maintain financial stability	December 2019
Complete with assistance from the IMF and publish the report of a diagnostic assessment of Zimbabwe's governance vulnerabilities (¶24)	Strengthen governance and combat corruption	December 2019

Zimbabwe: Economic outlook

- **Economic outcomes in 2019 are worse than anticipated**
- **Twin external shocks:** have significantly impacted the macroeconomic adjustment, worsening the humanitarian crisis.
- **No external support:** Zimbabwe continues to have external arrears to IFIs and bilateral official creditors. It is effectively blocked from traditional external support to address its balance of payments crisis.
- **No domestic buffers:** The central bank has no reserves, leaving little policy ammunition to defend the new currency in a context of very weak confidence.
- Growth projected to contract by at least -5 percent in 2019, compared to -2.1 percent under the SMP

Zimbabwe: Economic outlook (Con't)

- The deep effects of multiple shocks due to:
  - The impact of deep fiscal adjustment
  - A general lack of confidence from past economic mis-management
  - The authorities' inability to access external financing
  - Impact of Cyclone Idai (leaving 270,000 people in need of emergency humanitarian assistance, and caused infrastructure damages estimated to exceed US$600 million, and recovery-cost financing needs of over $1bn (5 percent of GDP).
  - and the drought affecting Southern Africa (has severely impacted agricultural production and radically reduced electricity production, resulting in a significant contraction in the mining/gold sector, key sources of foreign exchange). So far, the financing need for cyclone recovery and drought impact mitigation is largely unmet—at end-July, Zimbabwe had received pledges of only $138 million, including a US$72 million grant spread over 4 years approved by the World Bank in July.

Projections …

Macroeconomic Indicators	2018		2019	2019
(Annual % change, unless otherwise indicated)			SMP	**Proj.**
Real GDP Growth	3.4		-2.1	**-5.4**
CPI (end of period)	42.1		49.6	**119.1**
CPI (annual average)	10.6		80.8	**129.4**
Nominal GDP (RTGS billions)	42.8		70.3	**82.5**

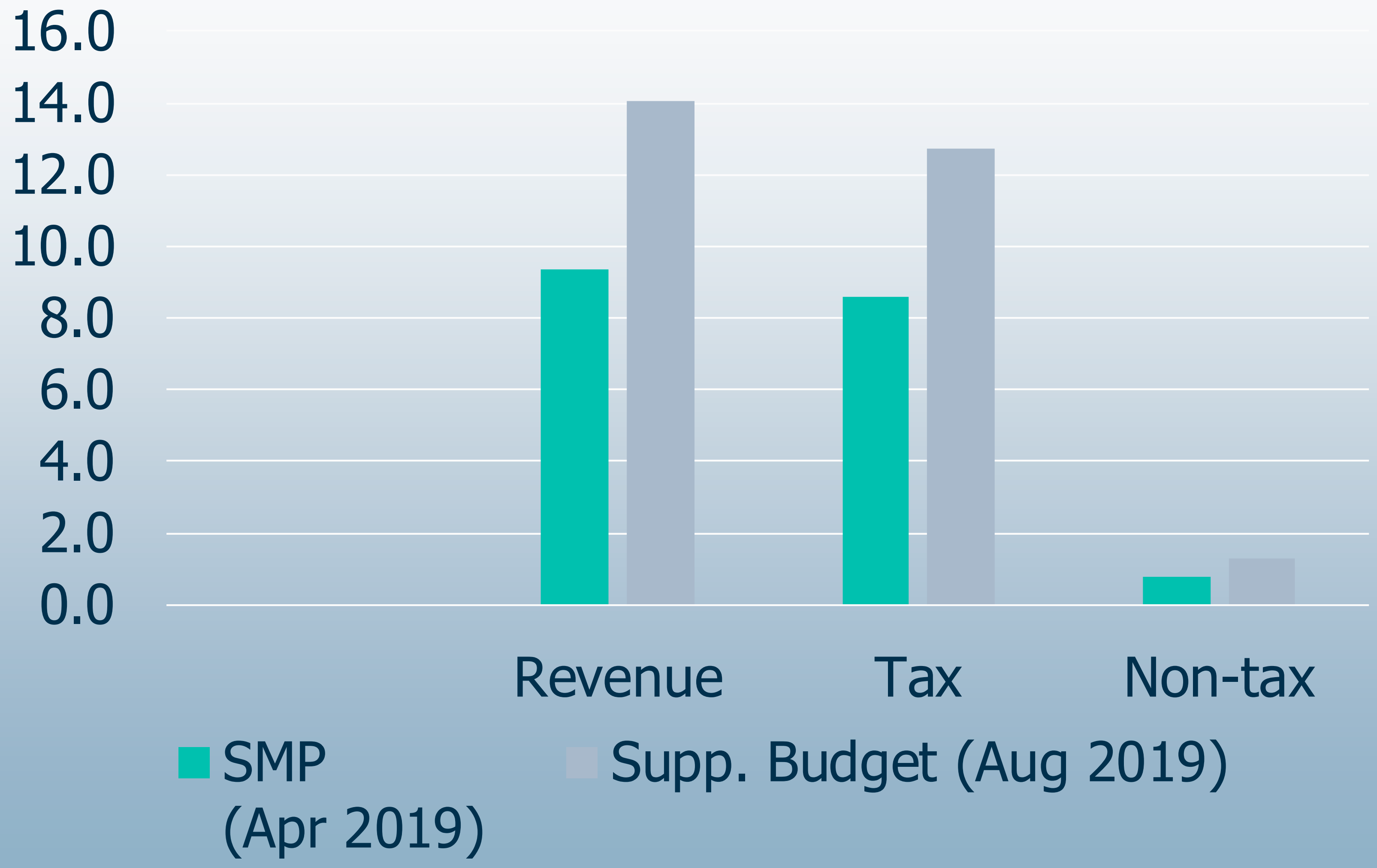
Negative growth shock

- Agriculture sector is expected to contract by at least 15 percent
  - drought has crippled agriculture, with maize production—cut by about a half
  - tobacco underperformed
- Mining is expected to contract by 10 percent
  - as FX shortages, pricing anomalies from the issuance of the new currency, and electricity outages affect output
- Low rainfall has curtailed hydroelectricity generation
  - Power rationed nationwide, with outages reaching 18 hours a day in Harare
  - Importation of electricity from South Africa and Mozambique has stalled due to a lack of FX/access to external financing
  - Equipment is outdated at most power stations

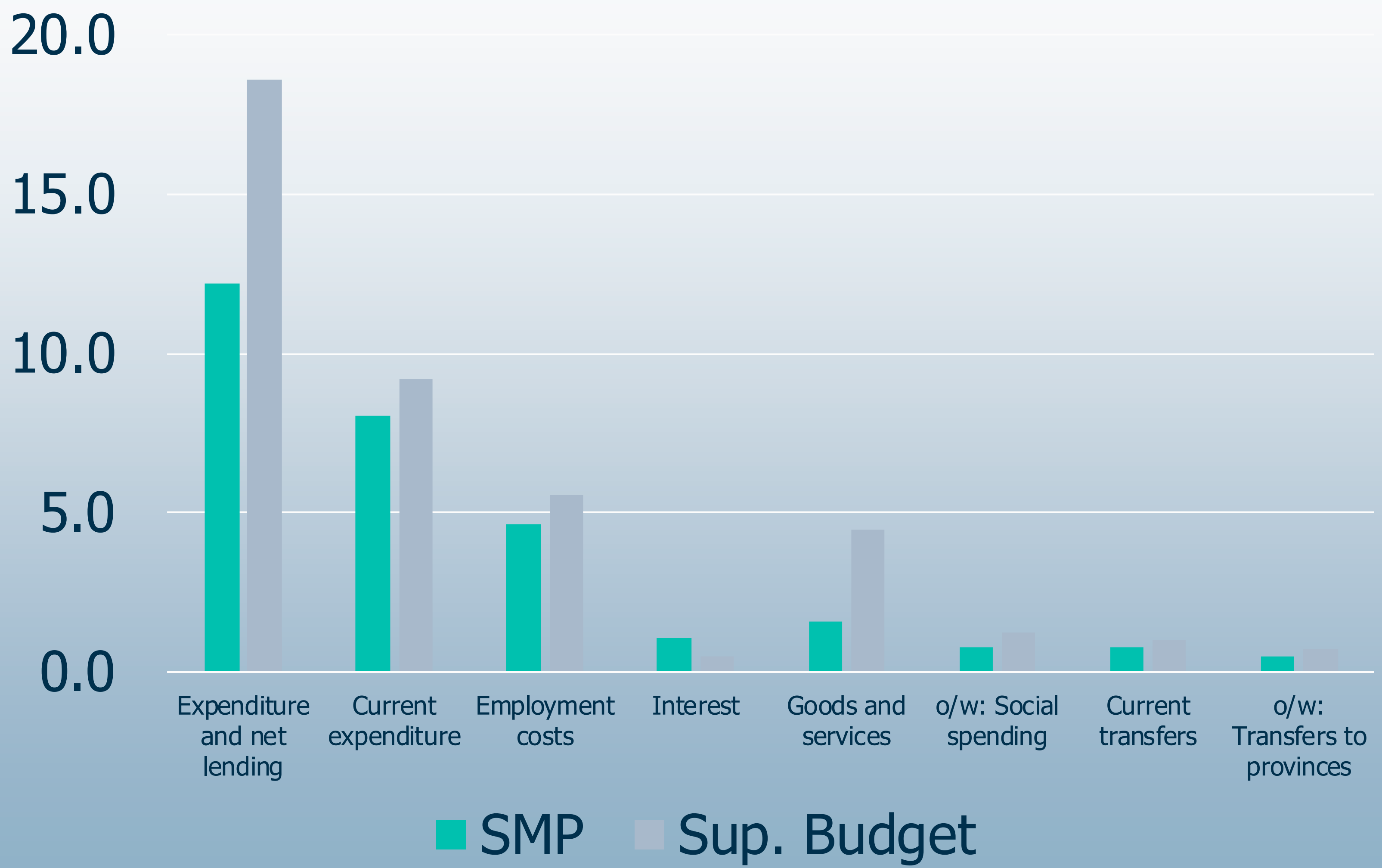
Lack of confidence

- a weak communication strategy
- haphazard implementation of policies,
- opaque transactions,
- distortions caused by multiple exchange rates, and a refusal to move quickly to a market determined exchange rate have exhausted all the country's external buffers
- initial hesitancy in moving to a market-determined exchange rate, has fueled inflation.
- Inflation reached 230 percent (y-o-y) in July, from 5 percent a year ago, reflecting the continued depreciation of the exchange rate
- The elongated impasse - major stakeholders remain in a 'wait and see' mode

Yes, fiscal adjustment is proceeding: SMP vs. Supplementary Budget



SMP vs. Supplementary Budget



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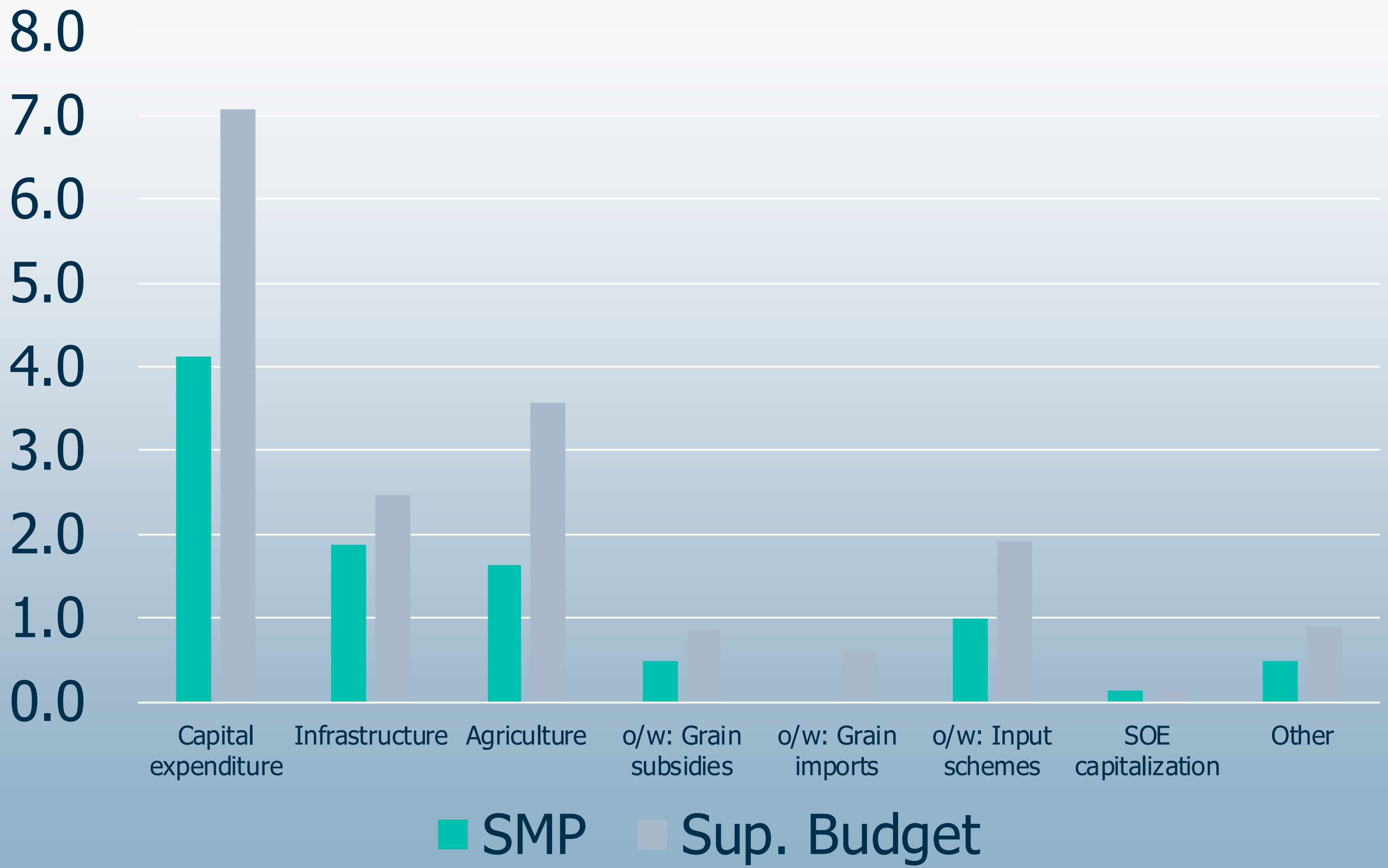
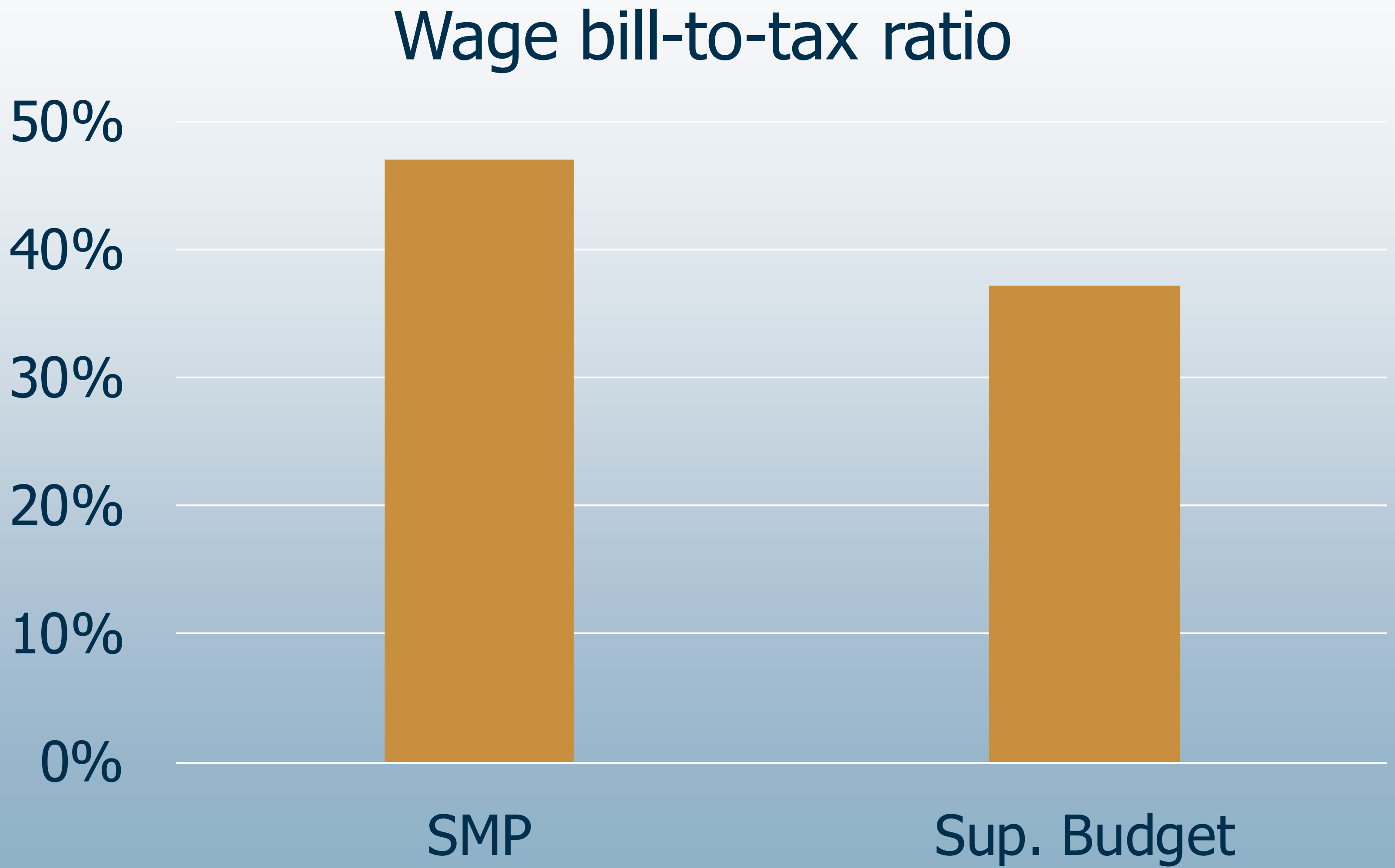
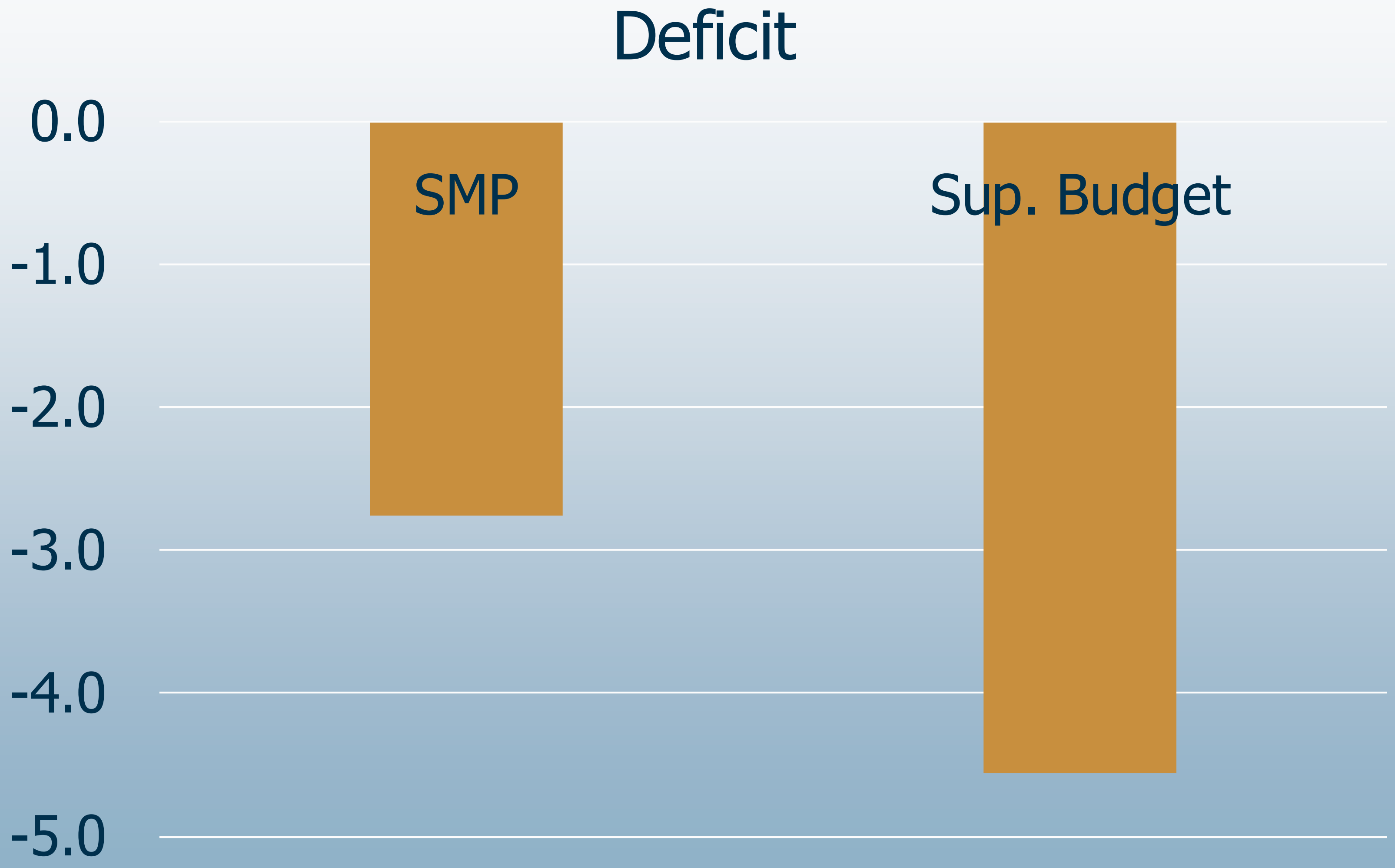


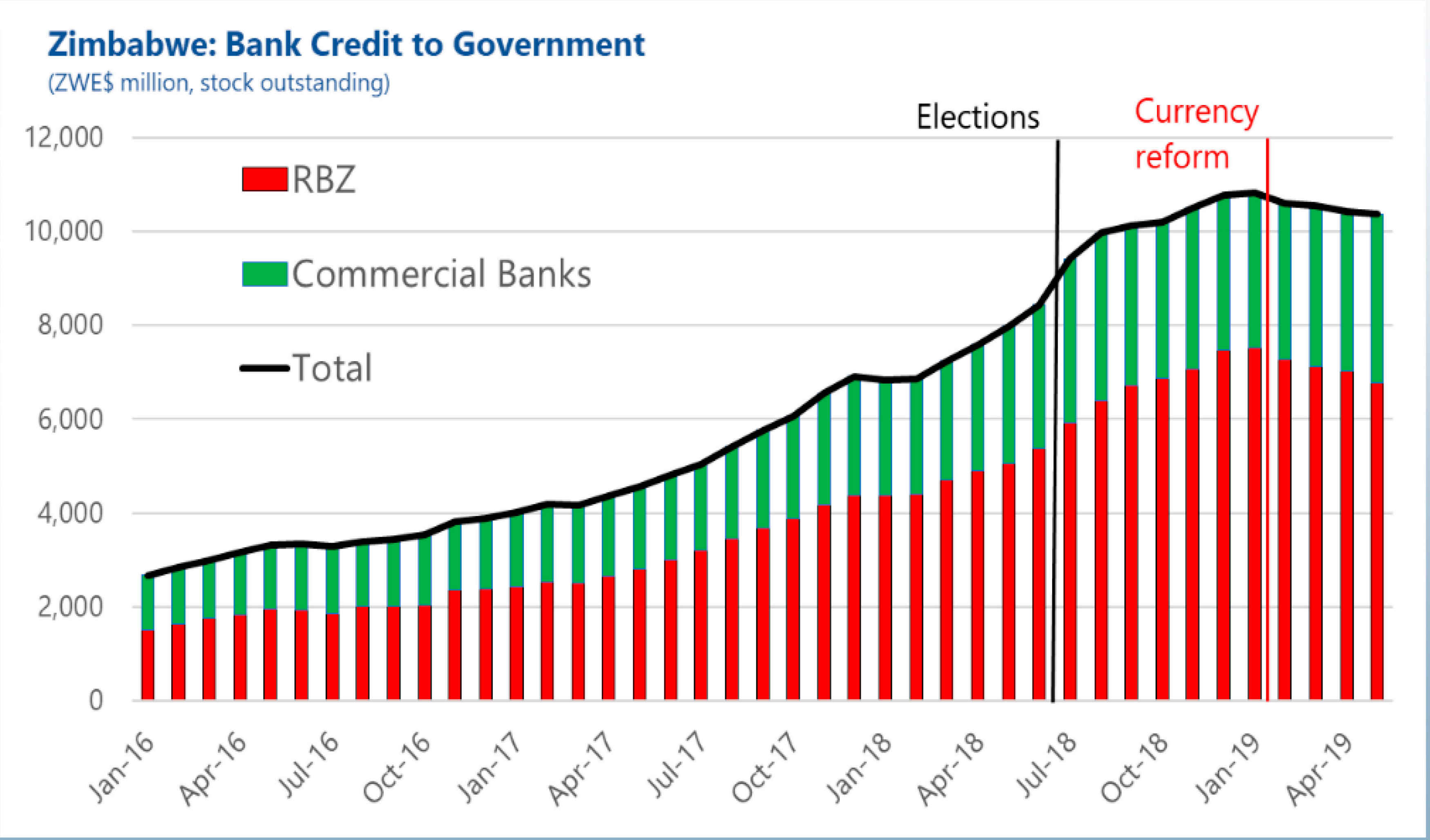
SMP vs. Sup. Budget



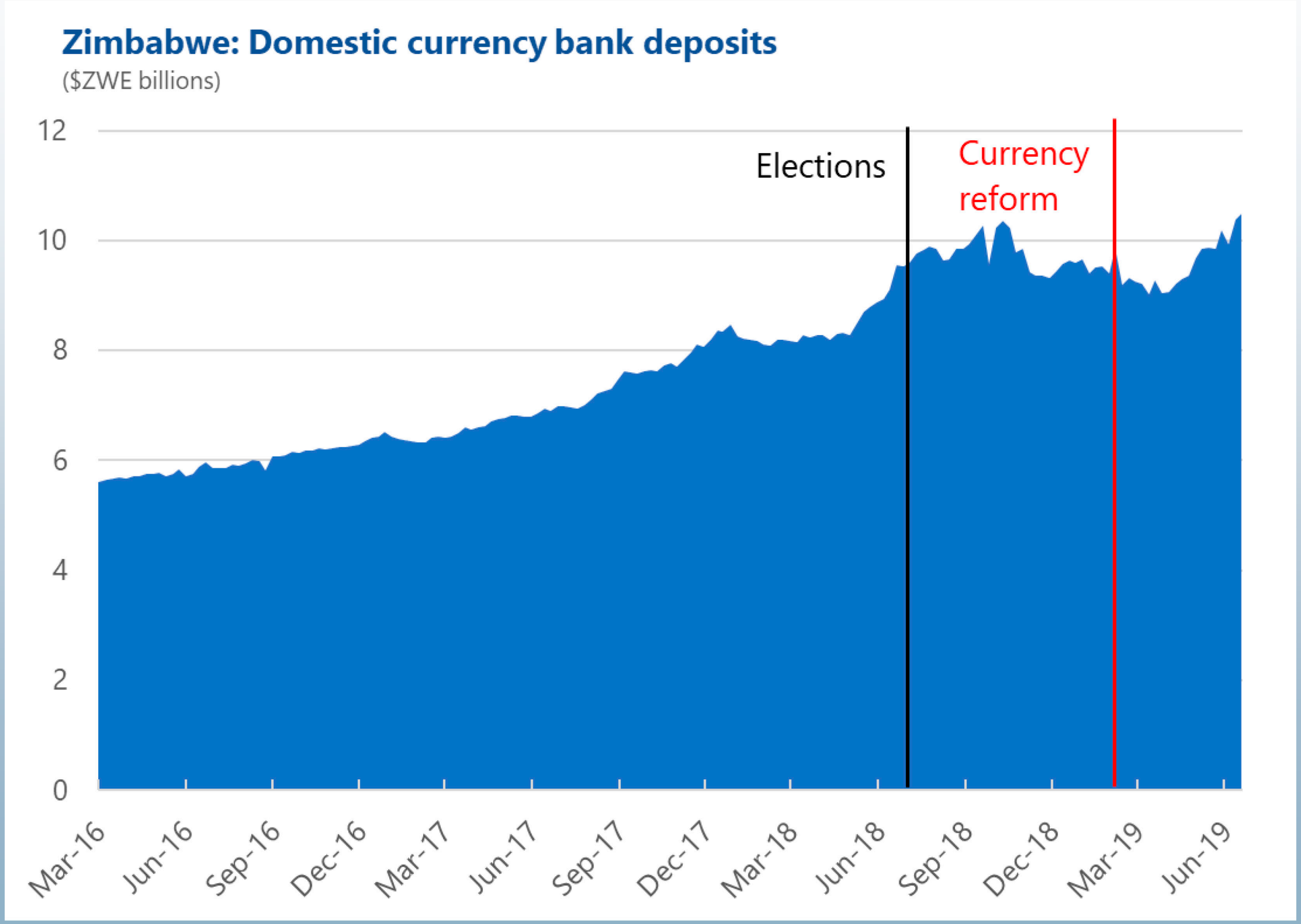
SMP vs. Sup. Budget



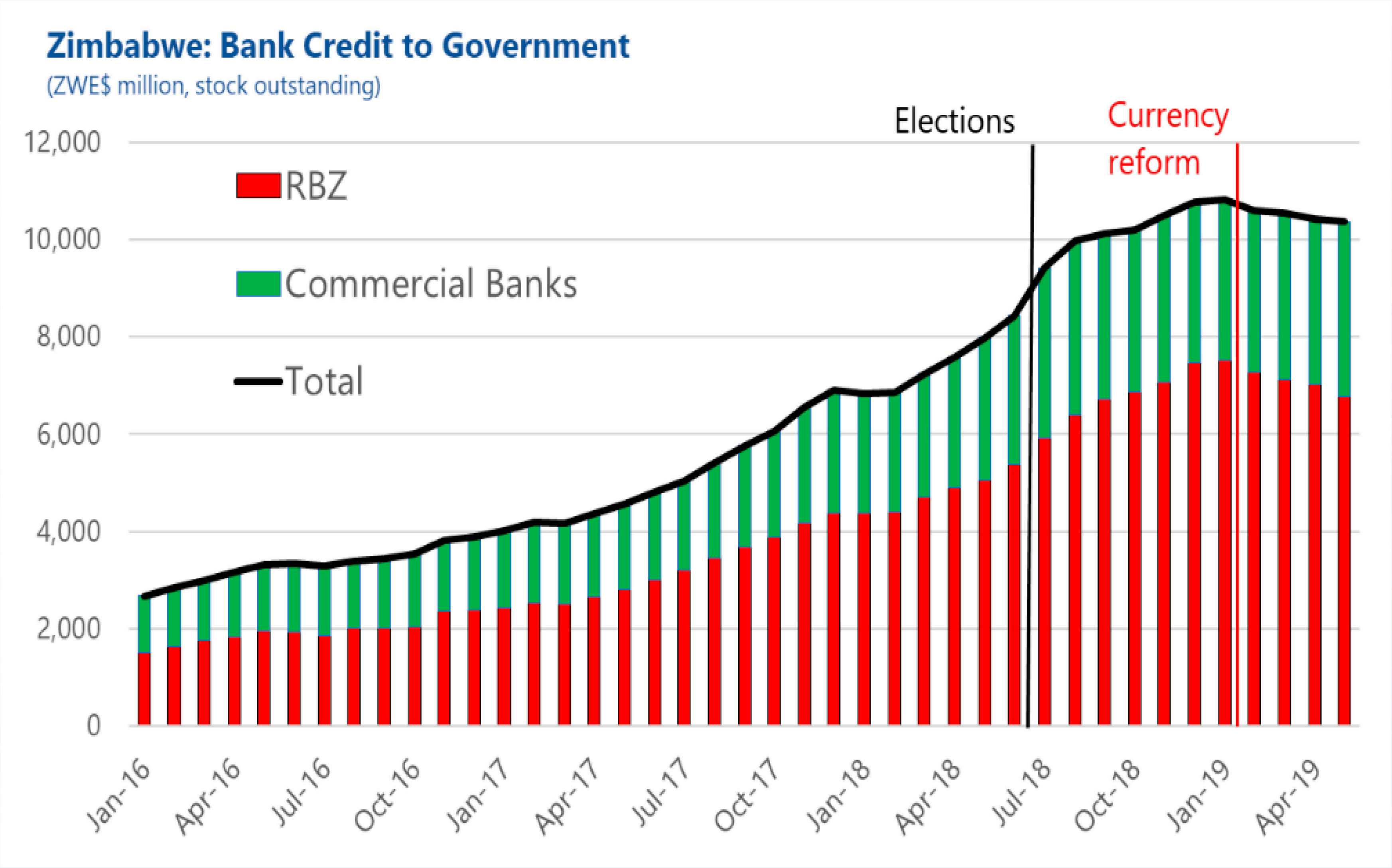
Public domestic debt is declining, and central bank financing stopped…



Local currency money supply remains stable

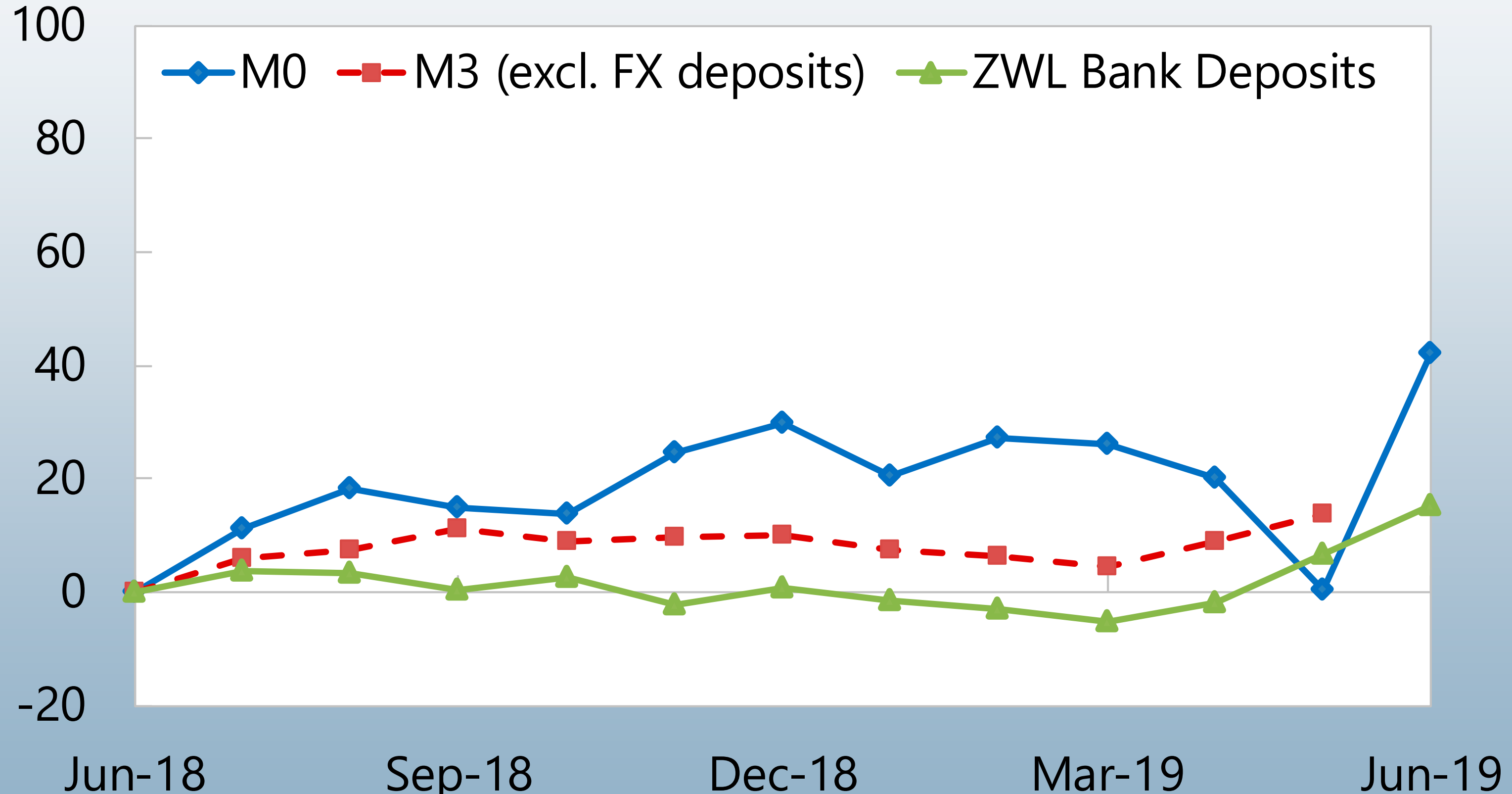


Local currency money supply remains stable (Cont.)



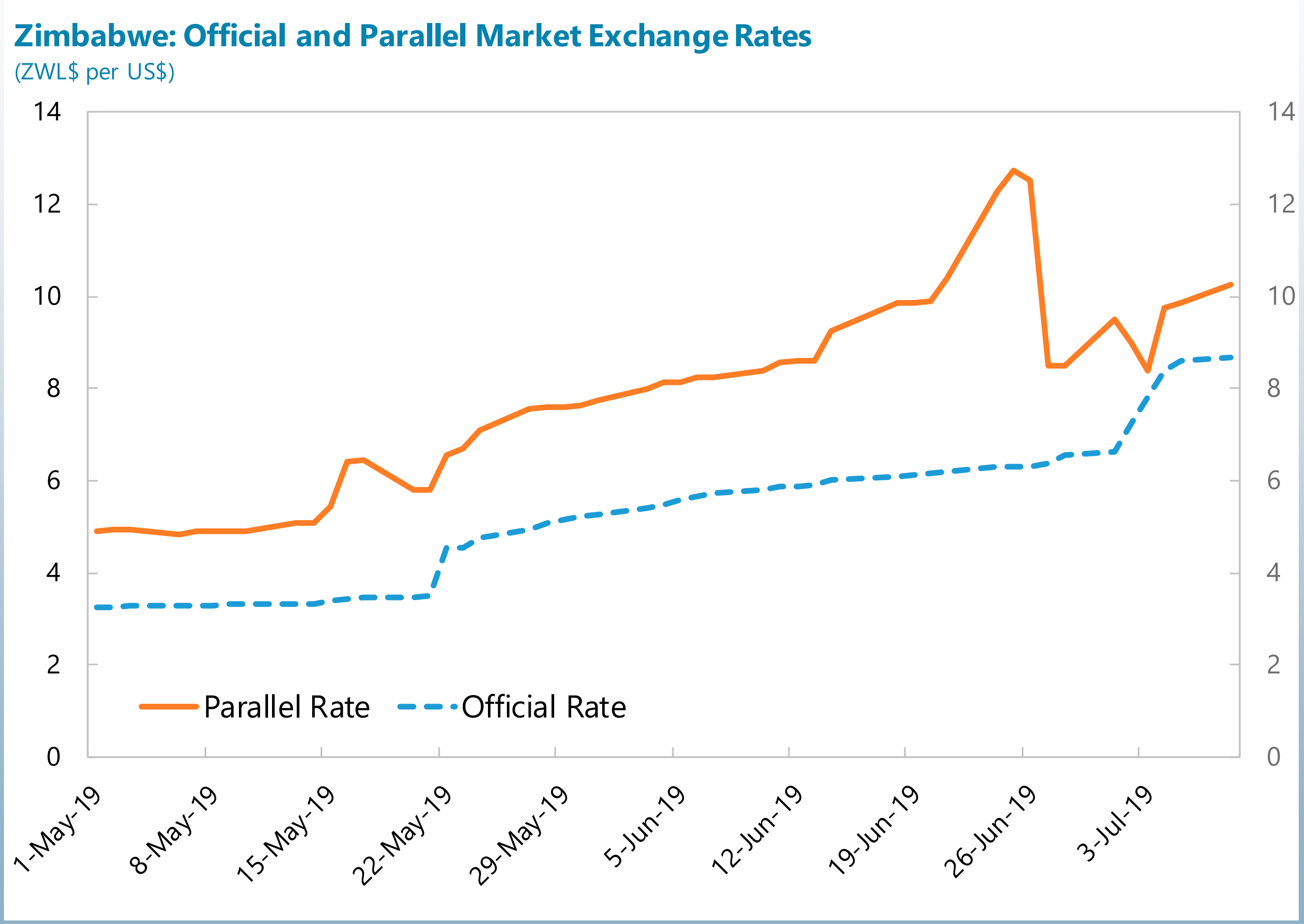
Recent Developments in Money Supply

(Cumulative percent change since June 2018)

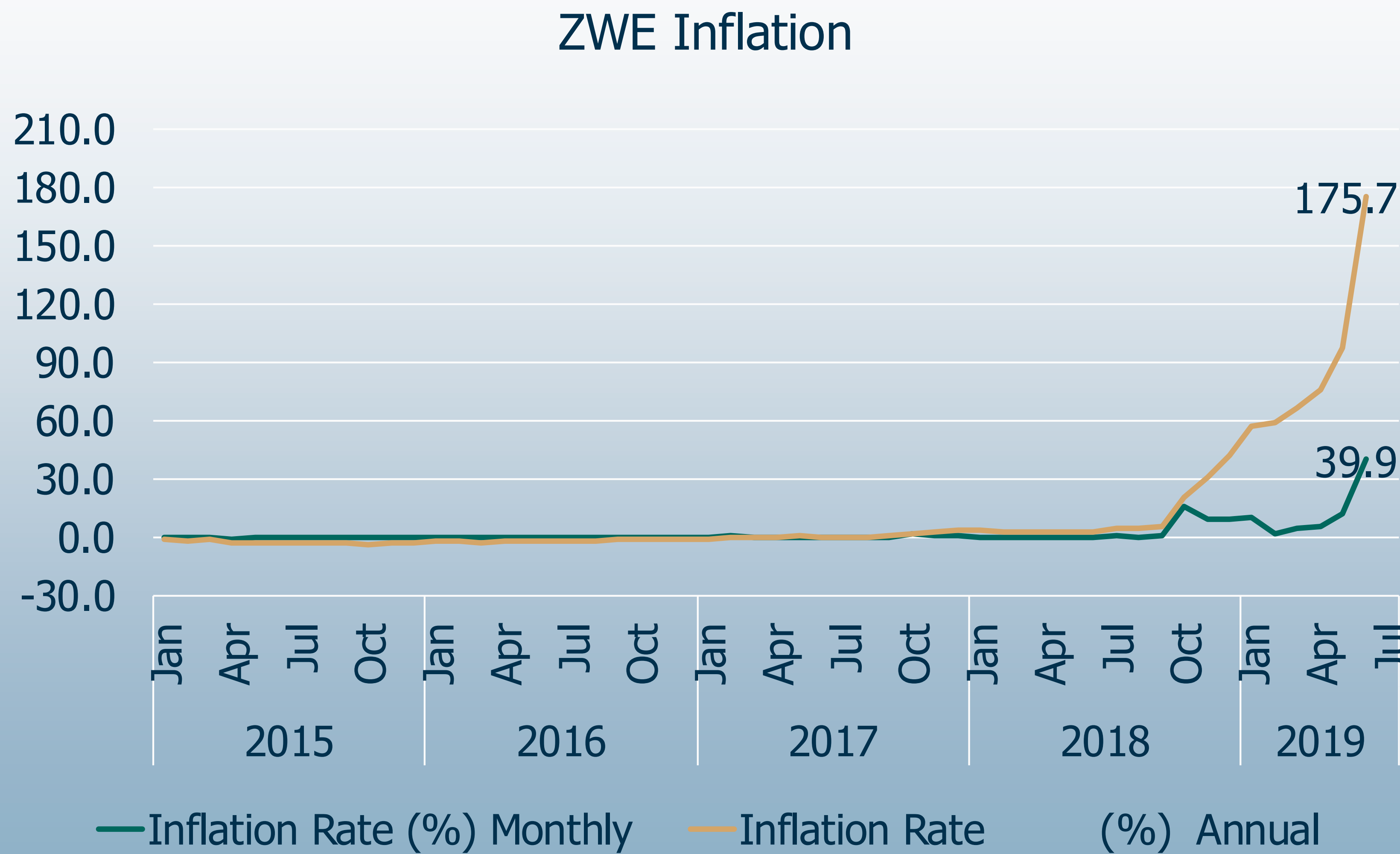


Sources: Zimbabwe authorities and IMF staff calculations.

After a rapid depreciation, the exchange rate has largely stabilized over the past months …



… but inflation is still rising…



External Sector Adjustment

Current Account

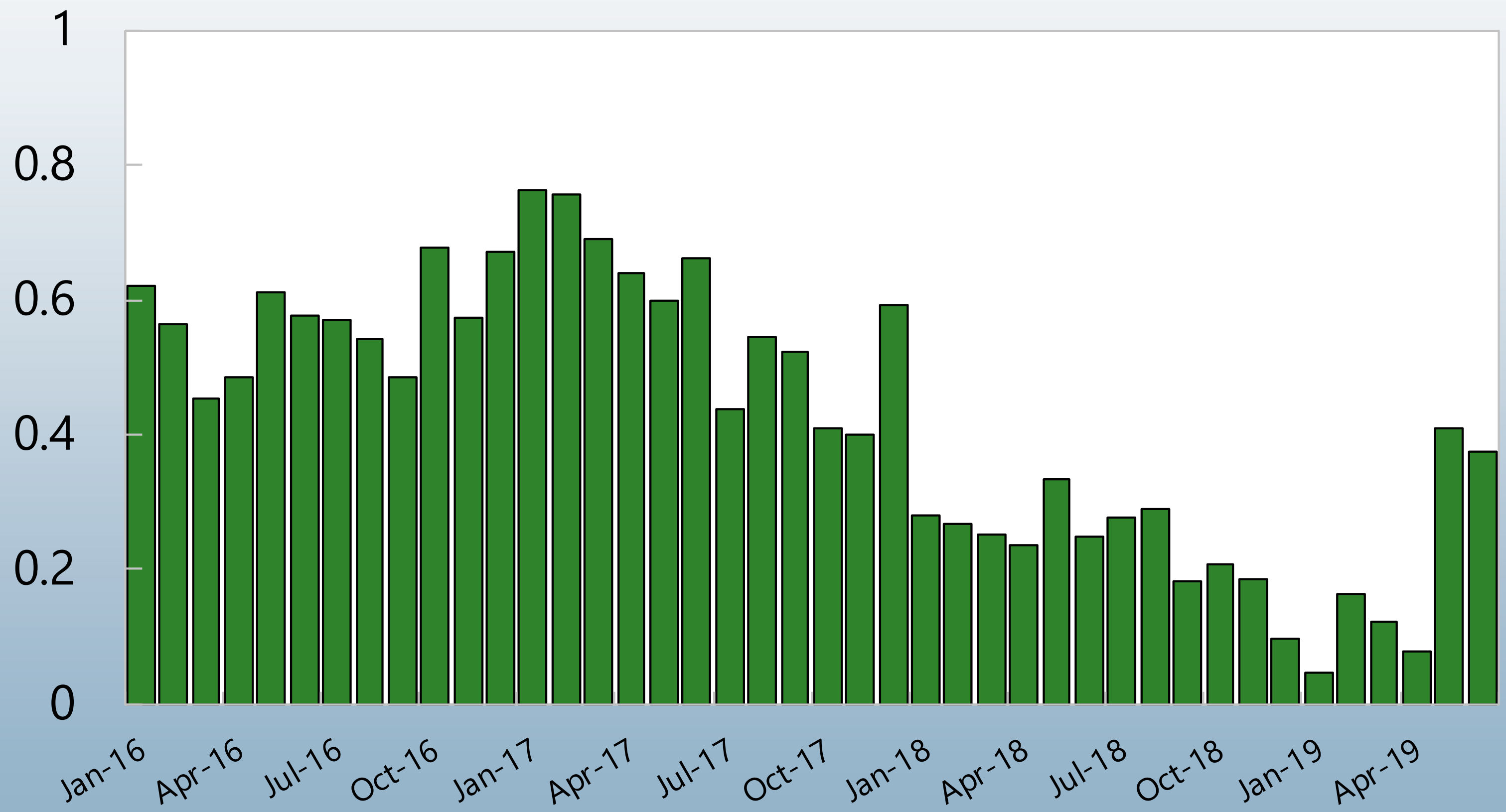
- Terms of trade have been declining since 2016 with tobacco prices falling and oil prices rising, increasing foreign exchange shortages in the face of limited foreign financial flows
- Current account turned to a surplus in 2019Q1.
- Surplus of US$196 million so far, compared to a deficit of over US$1 billion in 2018 reflects
  - import compression from the fuel price adjustment in January 2019 that reduced incentives for arbitrage,
  - FX shortages
  - a sharp decline in real disposable income
  - Sharp decline in investment due to weak investor confidence

External Sector Adjustment (Cont.)

- Reserves remain at critically low levels
- Export diversification is declining and Zimbabwe is vulnerable to external shocks from its dependence on a few commodity exports and on a single destination
  - During 2009-18, gold, platinum, and tobacco accounted for about 60 percent of total export earnings
  - During 2015-18, about 66 percent of the exports were to South Africa
- Foreign direct investment inflows have been low. Annual FDI was 1.6 percent of GDP during 2004- 2017, compared to the SSA average of 2.6 percent and well below its similarly endowed peers (Zambia attracted 6 percent of GDP during 2004-2017).

Reserves

Zimbabwe: Net International Reserves



Sources: Zimbabwe authorities and IMF staff calculations.

Policy implementation under the SMP

- Policy implementation under the SMP has been largely satisfactory, albeit with costly delays in implementing measures supporting the new domestic currency

- But economic outcomes are much worse than expected as adverse weather shocks (drought and cyclone Idai) crippled agriculture, mining, and electricity generation

- The authorities have maintained the key fiscal anchor of halting central bank lending to the government, resulting in a budget surplus in 2019H1,

- But poor communication and hesitancy in key steps in the currency reform, weakened confidence resulting in
  - a large exchange rate depreciation
  - inflation spike (230 percent y-o-y in July)

Worsening humanitarian crisis

- Cyclone idai
- Drought
- Erratic fuel and electricity supply
- Erosion of real wages and savings
- Authorities’ inability to respond to the climatic shocks
- Limited support from the international community

Worsening humanitarian crisis (Con't)

- Cyclone Idai has left 270,000 people in need of emergency humanitarian assistance
- Drought and cyclone combined has affected 5.3 million people
- Urban and rural poverty is rising
  - the introduction of the new currency and sharp acceleration in inflow implies a substantial cut in real incomes and in the real value of savings

RISKS

Risks to the outlook

- **Risks remain tilted to the downside and include factors both within and outside the authorities' control:**
  - social and political resistance to reform
  - policy slippages (e.g. currency reform), or interference by vested interests,
  - spending pressures, particularly on wages, social support, subsidies to SOEs and agriculture, and financial sector bailouts could jeopardize fiscal goals.
  - the envisaged deep fiscal adjustment needs to be carefully implemented to avoid a too a heavy toll on vulnerable portions of the population

Risks to the outlook (Cont.)

- **Factors beyond the authorities control include:**
  - a worse-than-envisaged agricultural season,
  - exacerbating risks of poverty and social discontent, and
  - a slow recovery in confidence that delays a resumption of economic activity, particularly in export industries like mining.
  - the outlook also does not factor in a significant macroeconomic impact from Cyclone Idai, and the power cuts going forward

Fund relations

- The Fund continues to support Zimbabwe's capacity building in:
  - Debt management, public financial management, and government financial statistics
  - Monetary policy frameworks and operations
  - Revenue mobilization and administration
  - Financial oversight and bank supervision

Full cooperation – Reengagement

- Reengagement with the international community and restoring debt sustainability are important priorities of the Zimbabwean authorities, which the IMF supports
- These priorities require strong economic reforms that address existing imbalances, as outlined in the SMP

Conditions for IMF financial engagement

Arrears clearance to the IFIs

+

Financing assurances from bilateral creditors

+

Comprehensive, consistent package of policies for sustainable, inclusive growth

→ Reengagement

Conclusion

Imbalances are being addressed

- Continued tight fiscal and monetary policies - necessary to support the new currency and stabilize the economy
  - Fiscal adjustment - contain growth in monetary aggregates - stopping monetary financing - stabilize the exchange rate - removing exchange restrictions- orderly operation of payment systems
- build credibility - improve communication and policy consistency
- bring inflation under control
- restart investment and growth
- continue to address the untargeted subsidies– maize, urban water supply, toll fees
- Press for continued FX market reforms - monetary policy be tightened to stabilize the exchange rate.

Thank you