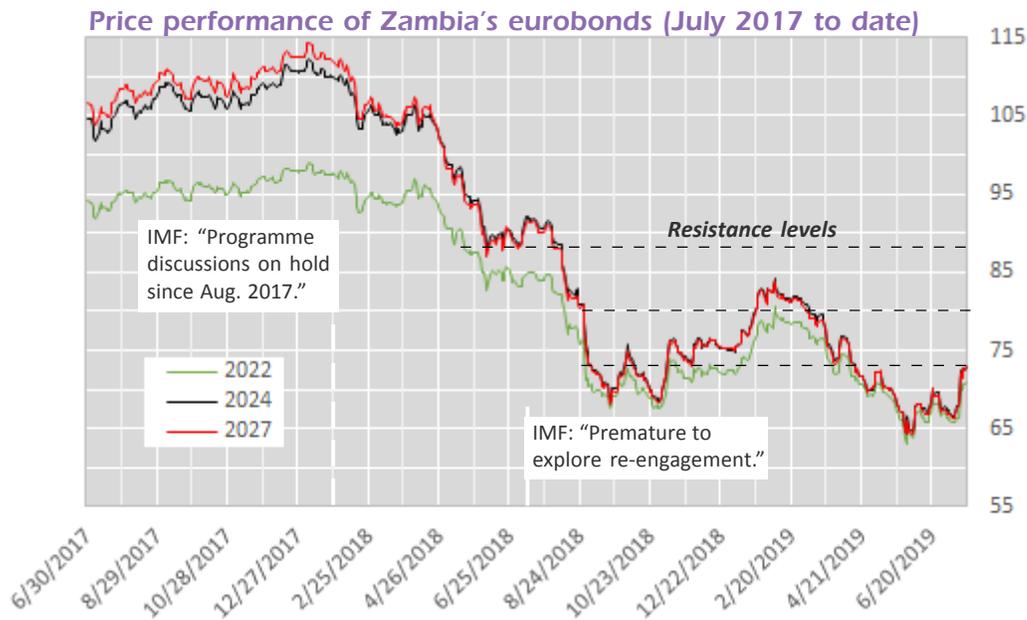


July 19, 2019

ZAMBIA RESEARCH NOTE

Enjoy the honeymoon, but ...

Professional honeymoons don't get much better than Dr. Bwalya Ng'andu's first week as finance minister¹, with bond prices up by an average of 7% and indications that this rally might have another leg or two to run. **But the assumptions on which it rests are decidedly speculative and unlikely to survive a confrontation with Zambia's dire fundamentals. As such, it would be wise to keep an eye on the exit.**



1) The former BoZ deputy governor is, admittedly, replacing a somewhat discredited predecessor². But, what triggered the market's exuberance was the following, uttered during his maiden press conference: **"I will be quite keen to get us talking and see whether we can get the program."**³

Perhaps understandably, the consensus expectation now is that **the Republic will shortly re-engage with the IMF, and that an ECF programme⁴ will materialize in short order.**

2) However it is worth noting that, in his own remarks upon administering the oath of office, **President Lungu made absolutely no mention of approaching the IMF⁵** - notionally one of the new minister's most important briefs. Similarly, when Dr. Ng'andu presented the *Update of Economic Developments* for Q2/2019 two days later, his introductory remarks – which included a vision statement⁶ - studiously avoided any mention of the Fund.

¹ As it happens, Dr. Bwalya Ng'andu was sworn in as finance minister more than 24 hours before his nomination as a Member of Parliament became effective - a clear breach of the Constitution. Section 116.(1) provides that, **"The President shall appoint a prescribed number of Members of Parliament as Ministers"**, while clause 116.(3)(c) stipulates that a Minister's office be declared vacant if, **"in the case of a nominated Member of Parliament, the nomination is revoked."**

² Her frequently incoherent arguments were as memorable as the embarrassing footage of [her semi-comatose 'performance'](#) during the proceedings of the so-called National Democratic Forum two months ago.

³ As quoted in *"Zambia's New Finance Minister Wants to Restart Talks With IMF"*, by [Bloomberg](#), Jul. 15, 2019.

⁴ Designed to **"provide assistance to countries with protracted balance-of-payment problems"**, these support programmes are viewed by many market participants as *de facto* credit guarantees.

⁶ Viz.: **"President Edgar Lungu has tasked newly appointed Finance Minister [Dr Bwalya Ng'andu to fix the economy](#). Speaking during the swearing in ceremony of Dr. Ng'andu, President Lungu has challenged the [Minister to settle Zambia's mounting debt obligation](#). He has encouraged Dr. Ngandu to work with relevant stakeholders to achieve meaningful results."** See *"Lungu tasks New Finance Minister to Fix the economy"*, [Facebook](#) post by Patriotic Front, Jul. 15, 2015.

The implication is that **the new minister's enthusiasm for an IMF programme is not shared by his principal** and is thus doomed to remain unfulfilled. Regrettably, we have been here before - during the incumbency of Felix Mutati⁷, who preceded Mrs. Mwanakatwe in the position.

3) In the short run, technical conditions suggest that **the Zambian rally has additional headroom**. With the Fed back in accommodative mode, and the Republic's 2027 bond offering 733 b.p. in incremental credit spread over its defaulted Mozambican counterpart⁸, we could see as much as **another 5 points in price appreciation**.

4) But **the market's exuberance is fated to collide with the grim reality** of Zambia's macro-economic - and increasingly political instability. Our baseline expectation is that the rubber meets the road in **early October, when the draft budget for 2019 is due to be presented** and the creative fiscal arithmetic put on display.

5) However, the day of reckoning could come much sooner. **Potential precipitating events** could include any of the following:

- a steep drop in **copper prices**;
- a crisis in the grain-marketing sector, where the **government still owes farmers for maize delivered 12 months ago**⁹;
- an **injunction** from the High Court in Johannesburg¹⁰, **halting the attempt to resell the 79.4% stake in KCM** that his government has expropriated from Vedanta;
- further **internecine strife within the Patriotic Front**, where a broad Cabinet reshuffle was announced this morning¹¹.

6) In the interim, the IMF Staff, who are currently working on the Article IV report¹², are unlikely to volunteer any comments on Zambia's prospects¹³. However, given **the litany of unfulfilled promises by successive finance ministers**¹⁴, the Fund's indulgence should not to be taken for granted.

⁶ E.g. **'Our vision, therefore, is to attain fiscal fitness, increase tax and non-tax revenue collections, sustainable debt levels, reduced arrears, a healthy financial system, reduced lending rates, and increased provisions for the social sector.'** See **Introductory Remarks in, "Update of Economic Developments for 2nd Quarter, 2019"**, published by **Ministry of Finance** on Jul. 17, 2019.

⁷ A well-known IMF enthusiast, Mutati was named finance minister in September 2016, to replace Alex Chikwanda – an inveterate opponent of engagement with the Fund. Predictably, the market saw in his appointment the promise of an early agreement but these hopes soon foundered on the rocks of Mr. Lungu's refusal to countenance any of the required austerity measures. It did not help that Mutati was not a member of the ruling party – another handicap that Ng'unda the technocrat shares with him.

⁸ Meanwhile, the corresponding premium over the Congo sovereign stands, which experienced and then cured a payment default in 2017 – stands at 633 b.p.

⁹ As it happens, this was the very first item on the National Assembly's agenda for Thurs. July 18th, viz.: **"When will when the Food Reserve Agency (FRA) will pay farmers for the maize supplied during the 2017/2018 marketing season, countrywide; how much money the FRA owes the farmers, province by province; and what has caused the delay in paying the farmers."** See Item #469(a) – Mr. Lufuma (Kabompo constituency), as listed in National Assembly Order Paper – Thursday, 18th July 2019 at 2.30 p.m.

¹⁰ Vedanta has petitioned the court under the terms of the KCM shareholder agreement which stipulates that any disputes between shareholders are to be submitted for arbitration by the S. African tribunal. The Lungu administration has attempted to do an end-run around this procedure by instituting a liquidation action against the company.

¹¹ In total, nine ministers are affected. However, this figure does not include the battered justice minister Given Lubinda who, at the National Assembly yesterday, chose to sit with the back-benchers rather than in his customary seat.

¹² I.e. the first such exercise since the one concluded in Sept. 2017, that mainly covered the period through Dec. 2016.

¹³ Indeed, the next press statement is almost certain to recycle the words spokesman Gary Rice employed in July 2018: **"Therefore, it's premature to discuss the appropriateness, the fitness, for any potential reengagement regarding a program discussion."**

¹⁴ They will also have been struck by how many of Mrs. Mwanakatwe's tired clichés were audible in her successor's introductory remarks this week: e.g. **"achieve fiscal sustainability by reducing the deficit over the medium term"**; **"increase our capacity to mobilize resources"**; **"ensuring debt sustainability"**.

This Report has been prepared purely for the purposes of information and neither constitutes, nor is intended to constitute an offer to sell or the solicitation of an offer to purchase securities. Although the statements of fact in this Report have been obtained from, and are based upon sources that Rhombus Advisors LLC believes to be reliable, the Firm does not guarantee their accuracy, and any such information may be incomplete or condensed. All opinions and forecasts included in this Report represent the Firm's judgement as of the date of the Report and are subject to change without notice.