UNCTAD's Seventh Debt Management Conference

9-11 November 2009

Economic Recession and Risk of Debt Distress

by

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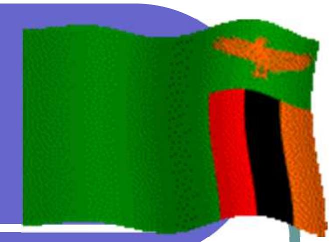
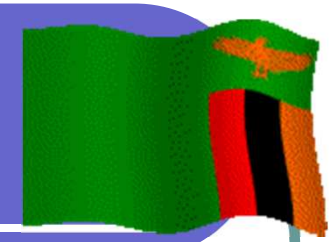
INTRODUCTION



- The world has undergone tremendous economic and financial shock as a result of the global financial crisis.
- Globally trade and output contracted sharply particularly in the fourth quarter of 2008 and first quarter of 2009.
- Projections suggest global growth contraction of 1.4% in 2009 and recovery to 2.5% in 2010.
- Growth in Sub-Saharan Africa is projected to decelerate to 1.5% in 2009 from 5.5% recorded in 2008.

INTRODUCTION (cont.)



- However there is evidence that the worst may be over with the United States and Europe showing signs of growth in output and other leading indicators.
- Important Euro Area economies such as Germany and France have posted positive GDP growth in the second quarter of 2009.
- Increase in production output and broad based recovery in commodity prices suggests that the global economy is on a recovery path.

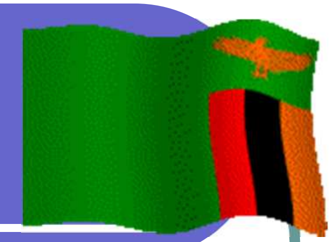
Impact of the Global Financial Crisis on Africa

- Reduction of fiscal space leading to challenges in implementation of critical investment expenditures.

- IMF estimates a drop of budget surpluses from 2.8% of GDP in 2008 to deficits of 5.4% of GDP in 2009 across both oil and non-oil commodity exporters.

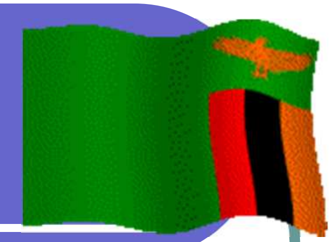
- There has been a marked slow-down in real GDP from an estimated 5.5% in 2008 to a projected 1.5% in 2009 and the projected growth of 4.1% in 2010 is less than the minimum 7% growth required to achieve the MDGs by 2015

Impact of the Global Financial Crisis on Africa (cont.)



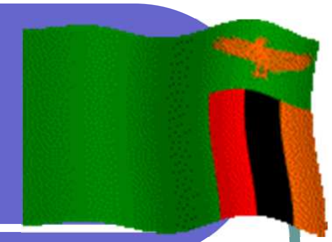
- Foreign Direct Investment Flows and commercial lines of credit have been negatively impacted.
- For example FDI inflows to Africa are projected to fall by 18% in 2009 from the 2008 inflows.
- African countries have had difficulties in raising long term financing in international markets. An example is the Ghana telecom bond issue of US $300 m which did not materialize.
- Eurobond issues for Kenya, Nigeria, Tanzania and Uganda have also been delayed.

Impact of the Global Financial Crisis on Africa (cont.)



- Overall effect on Africa has been a drop in budget balance from a surplus of 2.8% of GDP in 2008 to a deficit of 5.4% of GDP in 2009ecline in government revenues.
- Deterioration in current account balance. Foreign Direct Investment Flows and commercial lines of credit have been negatively impacted.
- For example FDI inflows to Africa are projected to fall by 18% in 2009 from the 2008 inflows.

Impact of the Global Recession on Zambia



- With regard to Zambia, Government revenues during the first half of 2009 were 25% below projections in the 2009 budget as a result of reduced tax revenues from the major export (copper).

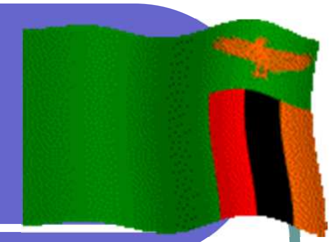
- Non resident holdings of Treasury Bills declined from 16% of outstanding bills in September 2008 to almost nil by end March 2009 due to the negative portfolio inflows resulting from the financial crisis.

- Foreign Direct Investment Flows and commercial lines of credit have been negatively impacted.

Impact of the Global Recession on Zambia (cont.)

- Slow down in domestic credit growth during the first half of 2009 to 2.4% compared to an increase of 36% in the second half of 2008.
- In the external sector, total export receipts for the first half of 2009 declined by 37.8% compared with the same period in 2008.
- There was a sharp contraction of the trade balance mainly on account of reduced metal prices on the international market.
- Job losses in especially in the mining industry.
- Depreciation of the domestic currency by 60%.

Impact of the Global Recession on Zambia (cont.)

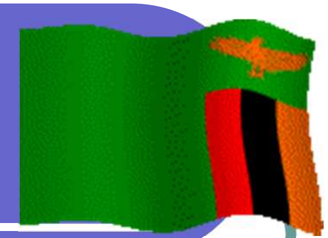


- The response from the G20 in mobilising resources to address liquidity and fiscal challenges for developing countries and Africa in particular is commendable.
- A significant amount of these funds have been channeled through multilateral institutions such as IMF.
- Zambia for example has taken advantage of these resources and has received US $627 million SDR allocation from the IMF in August 2009.
- Further, Zambia has been able to draw on its PRGF resources to compensate for revenue shortfalls.
- Confidence in the banking system with registration of 5 new banks

Possibility of Debt Distress

- The risk of debt distress has greatly reduced for countries such as Zambia following the post HIPC/MDRI as the debt to GDP ratio dropped to below 30% in 2006 and was 24% in 2008.
- However, this perspective had created borrowing space in many low income countries with the potential for re-accumulation of unsustainable debt
- This is because development challenges remain since there is need to fund large investment projects.
- However, countries face macroeconomic vulnerabilities due to a variety of shocks as a result of the global crisis.

Possibility of Debt Distress (cont.)



- The global crisis has negatively affected the availability of resources to service public debt as revenues have declined.
- Kwacha depreciation has also affected the burden of debt servicing.
- Cost of borrowing has increased as witnessed by higher interest rates.

Possibility of Debt Distress (cont.)

- Zambia's interest rate risk is related to the short term maturity structure of the domestic debt.

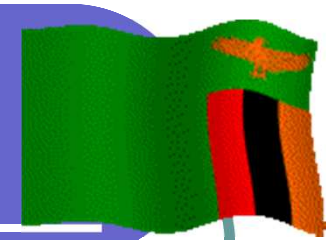
- Meanwhile the currency risk is on the external debt as it could lead to an increase in the debt to GDP ratio following depreciation of the Kwacha.

- Use of the Medium Term Debt Strategy (MTDS) tool for cost/risk analysis.

Possibility of Debt Distress (cont.)

- Zambia ‘s debt management policy and strategy is to ensure debt sustainability.
- Improve risk management (interest rate and currency risks).
- Support development and deepening of financial markets.
- Facilitate effective coordination between monetary, fiscal and debt policies.

Conclusion



- In conclusion, there is need for countries like Zambia to pursue and sustain sound macroeconomic and prudent fiscal policies which will quickly reverse the negative effects of the global economic recession.
- This would improve the debt servicing abilities since resources are still needed by countries for investment expenditures.
- High growth rates are necessary for poverty reduction.
- Need to promote regional integration in order to provide a wider market.

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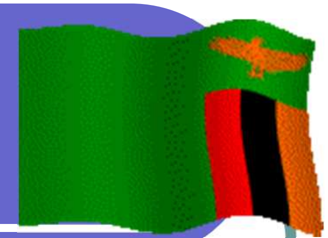

Lastly, do visit Zambia and enjoy one of the seven natural wonders of the world, the Victoria Falls.

Thank you!