Zambia's Debt Restructuring Experience

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Introduction

- The meetings' theme *Addressing the cost of development finance to achieve the Sustainable Development Goals* could not be more timely, in light of the recent global public health crisis (notably the COVID–19 pandemic), natural disasters, etc., coupled with developments in the global economic market have exacerbated fiscal challenges which have the potential to hinder the attainment of the Sustainable Development Goals. In the recent past, many countries experienced downgrades of their sovereign credit ratings, higher borrowing costs, and intensified risks of debt distress, the majority being developing countries.
- The topic of this session "***The elements that impact sovereign credit ratings and their role in development financing***", provides the opportunity to gain useful insights on navigating the dynamic terrain from various stakeholders. My address will provide a snapshot of Zambia's experience in debt restructuring, reviewing the trajectory of credit ratings. and proposing recommendations that may be of benefit to countries looking into the Common Framework process, especially concerning credit ratings.

Zambia's Debt Restructuring under the G20 Common Framework

- Zambia as one of the frontier countries to use the Common Framework, has been providing insights into how similar cases may be addressed in future and possibly form the basis of reforms to international financial architecture. The external debt restructuring journey commenced with Zambia officially defaulting in the year 2020, followed by a successful application to undertake the restructuring under the G20 Common Framework in 2021. Earlier notable milestones were the formation of the Official Creditor Committee (OCC) in July of 2022 whose financing assurances paved the way for the approval of the USD 1.3 billion International Monetary Fund Extended Credit Facility program.
- During the 2023/ 2024 farming season, Zambia experienced the most severe drought recorded to date. Despite the impact of the drought, the country continued to record significant milestones under the external debt restructuring in 2024 illustrated below:

Recent milestones in the Process

2024 Feb
Signing of the Memorandum of Understanding with all members of the country's OCC

2024 Mar
Agreement in Principle (AIP) with Adhoc Committee of Eurobond Holders

2024 Jun
Successful Consent solicitation

2024 Jun
IMF Board approval of 3rd Review & SDR (293.46 million (~ US$385.7 million) augmentation

2024 Jul
Exchange & Trading of New Bonds (Bond A – USD 1.75 billion and Bond B – USD 1.35 billion) on LSE

2024 Sep
Agreement in Principle (AIP) with selected commercial creditors ~ US$ 1.5 billion

2024 Nov
IMF Staff Level Agreement for the Fourth Review

The Role of Credit Ratings Agencies

The country's ratings pre and post-default are summarised below:

Table 1: Zambia's credit rating trajectory

Agency	Rating	Outlook	Date
Fitch	RD	N/A	June 7 2024
Moody's	Caa2	Stable	Jun 14 2024
S & P	SD	N/A	June 17 2024
Fitch	RD	N/A	Nov 18 2020
S&P	SD	N/A	Oct 21 2020
S&P	CCC-	Negative	Sep 25 2020
Moody's	Ca	Stable	Apr 03 2020
Fitch	CC	Stable	Apr 17 2020
S&P	CCC	Negative	Feb 21 2020

Source: "Zambia Credit Rating," World Government Bonds, https://www.worldgovernmentbonds.com/credit-rating/zambia/

Key
RD : Restricted Default
SD: Selective Default
Ca, CC, CCC: Very high level of default risk
Caa2: highly speculative – risk of default

The Role of Credit Ratings Agencies

- From the table, we observe that the downgrade in the rating was triggered by the announcement of the official default. Although the 2020 ratings of CC by Fitch, Ca by Moody's and CCC by S& P, respectively, already denoted a very high level of risk of default. As of June 2024, Zambia's long-term foreign currency rating remains as Selective Default (SD) according to S & P and at Restricted Default (RD) according to Fitch, this is expected to remain so until the restructuring especially with commercial creditors is concluded. Moody's applied a more favourable rating upgrading the country to Caa2 from Ca with stable outlook as a result of the bond exchange as well as expected concessional financing inflows.
- With regard to the New Bonds, both Fitch and S & P issued a rating of 'CCC+', which is anticipated to be the rating the country will receive on completion of the restructuring. Moody's rated the bonds at Caa2 on the basis that the extended maturity payments and reduced coupon payments provided significant relief in alleviating immediate liquidity pressures on the fiscal.
- In the recent past, Zambia participated in the Debt Service Suspension Initiative as well as the G20 Common Framework and has also undertaken significant policy reforms such as the introduction of Public Investments Planning guidelines, amendment of the Public Procurement Act, and the enactment of the Public Debt Management Act of 2022. However, the significant strides that the country has made, do not appear to have contributed to significant adjustments in the rating or outlook.

The Role of Credit Ratings Agencies

- Additionally, the impact of climate change which materialized through drought in Zambia, led to a downward adjustment in GDP growth assumptions at a country level and also by the ratings agencies averaging 2 percent from an earlier expectation of 4 percent. The adjustment in the GDP assumption is expected to carry an impact on the fiscal deficit despite mitigation factors such as the IMF augmented support as well as intervention measures from other cooperating partners.
- With regard to borrowing, Zambia has committed to a moratorium on the acquisition of non – concessional financing over the medium term, as part of the efforts to consolidate the fiscal position. In light of the foregoing, one would assume that with the current ratings and the ongoing default, financing from sources other than the multilateral development banks would be extended to Zambia at a very high premium.
- Allow me to cite the UNDESA (2022) policy brief which outlined the following three key challenges related to developing country sovereign credit ratings:

(i) the impact of downgrades on countries' cost of borrowing and on financial market stability, including whether there is perceived bias, increased volatility, and "cliff effects".
(ii) how official actions, including official debt restructurings such as DSSI, are incorporated into ratings analysis; and
(iii) the integration of climate change and other non-economic factors into rating methodologies.

A review of the credit ratings for Zambia pre and post-default shows that the findings of the report to, an extent ring true for Zambia.

Lessons for other countries

01 Public Investments Planning is essential to maximise the gains from borrowing as it will ensure that the type of borrowing (commercial or concessional) relates to the type of investment. Zambia has published a Public Investments Management Strategy, Guidelines, Public Investment Plans as well as Public Investment Project Prioritisation & Financing Option Mapping Criteria.

02 Countries should regularly review and update legislation and regulations relating to public debt management. Zambia repealed and replaced the Loans and Guarantees (Authorisation) Act of 1969 with the Public Debt Management Act No.15 of 2022. The act among others: established the Debt Management Office; mandates parliamentary approval of public borrowing improving oversight and accountability; and promotes transparency through mandated timely reporting

03 Aside from increased revenue mobilization efforts, countries should proactively take fiscal adjustment measures when faced with economic downturns. This will require sufficient early warning systems and prompt reactions to slow the adverse impacts and avoid situations of debt distress.

03 Regularly undertake necessary institutional reforms and continued capacity building in the relevant stakeholders within the Ministry responsible for Finance and Central Bank.

Recommendations & Conclusion

01 Reform to financial architecture, particularly for sovereign debt restructuring such as publication of guidelines would prescribe timelines as well as provide definitions for key terminologies such as comparability of treatment.

02 Development of more inclusive platforms to account for the evolution of the creditor landscape and to facilitate consensus building on debt treatments.

03 Adjustment in rating agencies' policies in order to accommodate circumstantial ratings to reflect efforts made by respective countries.

04 Establishment of regional rating agencies which may benchmark peculiarities common among respective regions.

It is necessary for countries undergoing debt restructuring or fighting natural phenomena to have access to sustainable financing resources to ensure that the basic needs of the people - which are well outlined in the Sustainable Development Goals are met. Credit Rating Agencies have a critical role to play as advocates for vulnerable countries that are demonstrating the necessary commitments to reform.

Thank you for your Attention