

ZIMCodd Position Paper on Zimbabwe Accelerated Arrears Clearance, Debt and Development Strategy (ZAADDS)

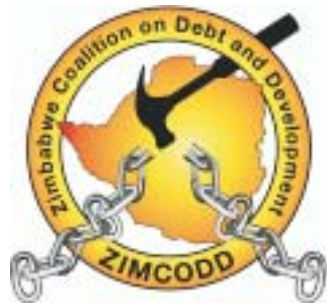
Investing in People for Social and Economic Justice

Introduction

While welcome and progressive in some respects, the strategy by the Zimbabwe government to deal with the country's debt overhang skips one critical and necessary precondition. It is only logical that a comprehensive debt audit be the starting point of a debt strategy. A debt audit that is as prognostic as it is diagnostic will not only establish the extent of Zimbabwe's indebtedness, but comprehensively review and reform the policies and systems of managing debt. This is crucial if Zimbabwe is to avoid falling into the debt crisis again. Moreover government of Zimbabwe needs to provide more details on the mechanics of its strategy. In its current form, the document is thin on detail.

Zimbabwe's external debt grew gradually in the 1980s and ballooned in the 1990s and 2000s. The ballooning of debt in the 1990s is attributable to the economic structural adjustment program (ESAP) prescribed by the international financial institutions namely the (IFIs) International Monitoring Fund (IMF) and World Bank. A direct consequence of ESAP is that Zimbabwe's economy deteriorated such that by 1999 the country could hardly service its debts. To the extent that ESAP contributed to Zimbabwe's indebtedness, some creditors, in particular the IFIs must bear some responsibility. The strategy is silent in this regard and instead prioritizes repayment, even at the expense of other pressing national priorities such as service delivery, poverty reduction, education, health, infrastructure development, remuneration of civil servants among other things.

It is imperative that any attempt to deal with Zimbabwe's debt starts with revisiting factors underlying the growth of this debt, types of debts accrued and why these debts did not lead to better capacity to repay. A basic principle of loan contraction and management is that contracted loans should grow the economy, improve social wellbeing and enhance capacity to repay. ESAP loans clearly failed in this regard. The Report indicated that questionable loans have also been contracted since 2000 mostly related to the military. There has also been massive growth of domestic public debt post 2000 linked mostly to the Reserve Bank of Zimbabwe (RBZ). These need also to be investigated. In the context of social economic justice and the ongoing political transition such an investigation is warranted to ensure accountability and institute the necessary reforms. A blind approach that does not question the legitimacy of



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loans contracted hitherto nor seeks to establish the purpose and utility of these debts cannot be right.

A Summary of ZAADS

Challenges faced by the Zimbabwean economy and society since the late 1990s are expressed in many ways. One clear way has been a public debt overhang growing since 2000. Basing on government's 2010 estimates external public debt stood at US\$6, 9 billion; 118% of GDP. While indicative of a problem, the sum of Zimbabwe's debt or its extent relative to GDP¹ is in itself not the most worrisome aspect. Rather, it is the total breakdown of capacity to repay that should be of bigger concern. Zimbabwe's deteriorating economic and political situation has seen the country defaulting on most of its debt repayments since 2000. According to the ministry of finance, in 2010, US\$4, 8 billion or about 70% of this external debt was in accumulated arrears. As long as Zimbabwe is unable to service its debts, growth in arrears will continue unrestrained. By 2012 Zimbabwe's external debt stood at more than US\$9 billion owing largely to accumulated arrears. Some sort of solution is thus required urgently to rescue the situation.

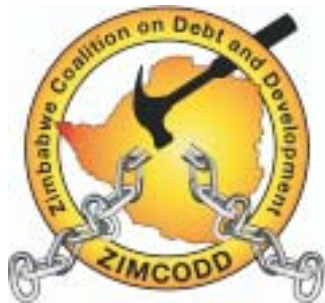
On the 16th of March 2012, the Zimbabwe government announced a strategy to deal with the country's debt overhang. The strategy referred to as the Zimbabwe Accelerated Arrears Clearance, Debt and Development Strategy (ZAADS) has six elements (or steps) namely;

- (1) establishment of a debt management office;
- (2) reconciling of debt figures to establish the correct amounts owed;
- (3) reengagement with all external creditors on arrears clearance;
- (4) adoption of a comprehensive debt relief program;
- (5) mobilizing new financing² (by implication contracting new loans) and;
- (6) Leveraging Zimbabwe's natural resources in pursuit of (debt relief and) economic development.

¹Other countries with higher total public debt and higher debt GDP ratio have fared better than Zimbabwe when it comes to debt service and general socio-economic condition.

²Ministry of Finance, website, 21-09-2012





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Comment on specific aspects of ZAADDS

1. Establishment of a debt management office (ZADMO);

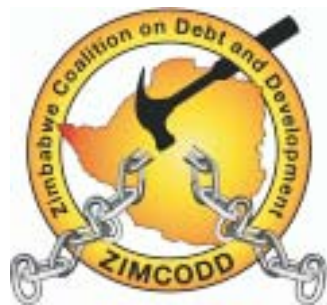
The establishment of an office to deal specifically with issues relating to public debt is a positive development and in accordance with emerging international best practice. It is pleasing to note that this office has been functional since 2010 and that the Zimbabwe government is moving to fully capacitate this office with requisite staff. ZAADS proposals such as a law to support ZADMO and a review of the External Loans Coordinating Committee (ELCC) so as to mandate it to come up with “an explicit Debt Management Policy” (ZAADS) constitute some of the strategy’s most progressive aspects.

Indeed the Zimbabwe government should be encouraged to legislate for the functions of this office so as to clearly define its mandate, terms of reference and accountability to the public. Its relationship to other bodies such as the ELCC, parliament, comptroller’s office and public accounts committee inter alia must be clearly defined. However such change proposals could be better informed by an official debt audit process of the scope suggested in this paper.

2. Reconciling debt figures to establish the correct amounts owed;

Government undertook to verify the actual amounts owed by “undertaking a validation and reconciliation exercise of the external debt data-base”. Such an exercise is warranted as it forms the basis for engagement with creditors. According to the 2012 budget statement, this exercise was completed in 2011. But this process appears limited to making sure everyone agrees with the figures on how much is owed. It is important that a thorough investigation of the circumstances under which the debt was accrued, terms thereof, status, costs, use of the loan (whether it was used for intended purpose) and if objectives were met among other things. The 2012 budget statement admits that the debt overhang can be a result of fiscal indiscipline (15). There is therefore need for an exercise that ensures that Zimbabwe will not in the future find itself in a similar situation. This can be achieved by having a comprehensive debt audit which will recommend changes to the country’s loan contraction and debt management systems.





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3. (and 4) reengagement with all external creditors on arrears clearance and the adoption of a comprehensive debt relief program;

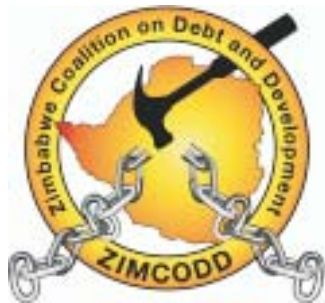
This is perhaps the most crucial part of ZAADS and thus warrants a more detailed analysis. After ascertaining the exact extent of the country's outstanding obligations, the government plans to engage with all its creditors so as to negotiate a suitable way to clear arrears and come up with a debt relief program. This would include "...a request for debt relief under the traditional debt resolution initiatives". Though ZAADS shies away from explicitly mentioning it, (traditional) debt relief usually happens under the Highly Indebted Poor Country Debt Relief initiative (HIPC)³. Under HIPC a country obtains debt relief after fulfilling a prescribed eligibility criterion. The shortcomings of HIPC are well documented.

Three approaches towards re-engagement and arrears clearance are proposed for International financial institutions (IFIs), Paris club and other creditors respectively. These are;

- a) Bridging loans
- b) Applying the Naples Terms
- c) Negotiating for comparable debt relief

Bridging loans for IFIs arrears clearance: Full clearance of arrears to international financial community namely International Monetary Fund (IMF), International Bank for Reconstruction and Development (IBRD), International Development Association (IDA) and the African Development Bank (AfDB) appears central to ZAADS. This will be done through bridging loans from cooperating partners (likely to be a western government). According to IMF rules a country in arrears cannot get new loans. Clearing arrears is thus seen as critical in order to pave way for new financing. But the new loans will in turn be used to repay the bridging loans (ZAADS, 18) with a risk of creating a debt trap vicious cycle. This clearly does not engender a sustainable solution to the current debt problem. If anything, the country is likely to end up in a worse debt situation.

³Parties to Zimbabwe's inclusive government could not agree on the usage of the term HIPC with some arguing that Zimbabwe is too rich to be referred to as HIPC.



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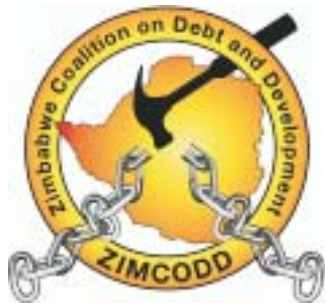
Technically, some of the arrears could be paid off with grants and concessional loans leading to a genuine reduction in the debt. For this to happen certain conditions would need to be fulfilled and this could be a stepping stone to joining HIPC. On the 24 of September, AfDB was reported to have availed a US\$500 million facility for Zimbabwe to go towards arrears clearance⁴. But this is not even enough to cover for arrears in lieu of debt service to AfDB. Though concessional this will only serve to increase Zimbabwe's long term outstanding obligations to the institutions. It also does not resolve that country's incapacity to service its debt, which by implication means the country's debt overhang is likely to grow further.

While ZAADS claims itself to be a hybrid strategy combining the best aspects of HIPC and Zimbabwe specific aspects, the country debt repayment obligations are likely to be worse off than under normal HIPC. The strategy is proposing anything but cancellation of Zimbabwe's debt. On the whole, the debt strategy like HIPC appears to be creditor led and too focused on fulfilling repayment obligation at the expense of sustainable economic development and debt resolution.

Applying the Naples Terms: This is with regards to debt and arrears due to the Paris Club (European creditors). ZAADS proposes relief under the Naples Rule as a minimum. This would be composed of consolidating existing arrears, rescheduling of payments by about 3 years, and a 67% reduction in repayment obligations and rescheduling of the balance over several years. To get this to happen, the Paris Club currently insists that a country meets IMF conditions and the IMF must certify that the debt is not payable. Going through HIPC would require the same criterion, but lead to 90%-100% of the debt to the Paris Club being written-off in the end. Some debt activists have warned that quite often,

"For Paris Club debts, cancelling some or all of them could be a way for western governments to save money. They are allowed to count debt cancellation as aid. Therefore, cancelling debts which are not being paid, like Zimbabwe's, can be counted as 'aid' without spending any money, but used to meet

⁴The Standard, 24 September 2012.



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budgeted targets for aid spending. This would reduce the amount of money the western government would actually have to spend on real aid, so saving them money”⁵.

The other unmentioned thing is that western governments will only consider these steps once there has been more political reform in Zimbabwe.

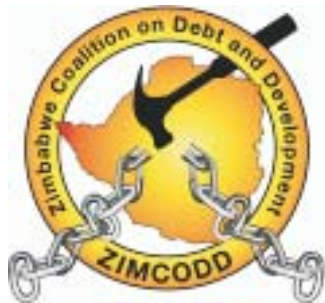
Negotiating debt relief with other creditors: Resolution of debt owed to non-Paris club and commercial creditors will depend on negotiations with individual creditors. Since ZAADS suggests that these will be comparable to that of the Paris Club, observations made above can apply. It is notable that steps to debt relief mentioned for both debts owed to IFIs and Paris club mimics HIPC. There is therefore probability that Zimbabwe might suffer same constrains that have been associated with applying HIPC to non-Paris Club creditors and commercial creditors⁶.

5. mobilizing new financing (by implication contracting new loans) and;

The current debt strategy’s main aim is to unlock new lines of credit. The pitfall of this approach is that it overlooks sustainability as seen by the endeavor to use bridging loans only to access IFIs loans to repay the bridging loans. While new loans are justified as necessary in order to finance “infrastructure reconstruction and improving the quality of life of ordinary Zimbabweans” this is unlikely to be achieved without a clear debt sustainability strategy. The strategy’s elevation of debt repayment above sustainability, poverty reduction and social welfare obligations, fair remuneration for government employees among other things is in conflict with its purported aim of improving the quality of life of Zimbabweans. In any case recent experiences where loans have been contracted to finance things like a defense college put to doubt that new finance will be in line with developmental priorities. In the absence of proper, transparent and accountable loan contraction and public debt management systems new finance is unlikely to result in meaningful improvements in people’s lives.

⁵Tim Jones, UK Jubilee Debt Campaign, ZAADDS discussion notes, 12 September 2012

⁶For HIPC challenges, see ZIMCODD Policy Brief No. 4 of 2010, *2011 National Budget Statement and Zimbabwe’s Indebtness*.



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6. “Leveraging Zimbabwe’s natural resources in pursuit of economic development”.

This is probably the most confusing part of ZAADS. The main text mentions the “leveraging of natural resources in pursuit of economic development”. No link is made between this and resolving Zimbabwe’s debt situation. The President’s foreword is the only part that makes a link, referring to “leveraging of natural resources in pursuit of debt relief and economic development”. The document proposes new mining legislation, a geological survey, proper management of the country’s mineral wealth and boosting investment in the mining sector but it is unclear why this forms part of ZAADS. Specifically, there is no explanation as to what “leveraging” of natural resource would mean.

It is known that in the recent years the Zimbabwe government has used future returns mineral extraction as security for certain loans. The most prominent one is the Chinese loan in 2011 towards construction of a defense college. Future diamond revenue was used as security. If true, the US Department of Interior’s 2006 Minerals year book shows that this was not the only example;

In May (2006), the Reserve Bank pledged future nickel exports to European and South American banks in exchange for their setting up a \$50 million fund that would pay for refined petroleum imports. In June, the Government agreed to a \$1.3 billion deal to send chromite to China in return for the Chinese-funded development of additional coal-fuelled electricity-generation plants, and cemented an agreement, which was valued at \$60 million, to send chromite to China in exchange for radio and television transmission equipment⁷.

Given the lack of clarity on what ZAADS means by leveraging mineral resources one would hope that what is being proposed is dissimilar to the deals mentioned above. Perhaps the document intended to imply that proper management of natural resources to optimize benefits through a sovereign wealth fund, geological survey, community development fund among other things would serve to reduce debt and aid dependency. Such a link could be explicitly made.

ZIMCODD Position

⁷ Phillips Mobbs, “The Mineral Industry of Zimbabwe”, *2006 Minerals Yearbook*, US Department of the Interior, US Geological Survey, April 2009, 42



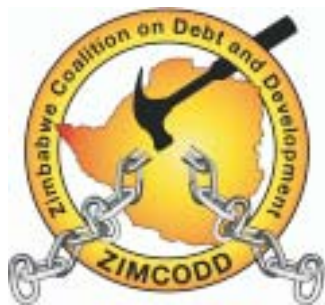
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In the short to medium term, Zimbabwe lacks the capacity to service its debts. Not only is the country unable to service debts, it also can barely manage to meet internal social and developmental obligations. Under the current context expecting and insisting on repayments in one form or the other is immoral and impractical. It is however unfortunate that the current strategy places internal human and economic priorities secondary to satisfying creditor preconditions for new financing. For instance, between January and June 2010 the government of Zimbabwe paid US\$1. 3 million in debt repayment to IMF at a time the ARV requirements were estimated to cost as much, civil servants are still earning below the poverty datum line, approximately 8 women are dying every day due to pregnancy related complications, more than 90% of the country's working age population is formally unemployed, certain districts are facing starvation, health delivery is still pathetic and physical infrastructure is in a state of decay among other things.

At the moment the opportunity cost of debt servicing is very high. Based on a principle that accepts debt responsibility but esteeming human welfare above all else ZIMCODD reaffirms the following.

1. The Zimbabwe government must conduct an official debt audit to not only establish what is owed, the purpose and condition under which loans were given, disbursement methods, whether objectives were met, charges other than interest and benefits and if any benefits accrued to citizens. A debt audit process would strengthen the power of a future Zimbabwean government in negotiations with creditors on the debt, because it would democratise the process and reveal the reckless lending of creditors. This will help to avoid past mistakes. The audit must cover both external and domestic public debt.
2. To pave way for the audit and the interest of social and in the interest of economic justice it is necessary for creditors to immediately institute a moratorium on principal and interest payments. A moratorium is not unrealistic to ask for. In fact paying old debts to the western world is a waste since these have effectively already been written-off due to Zimbabwe's inability to repay.



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3. Loan contraction and debt management legislation must be reviewed and reformed to ensure transparency, accountability and inclusiveness. These reforms will be informed by a comprehensive debt audit.
4. Zimbabwe needs transparent institutions and transparent investment agreements among others which can guarantee efficient utilization of resources and revenue
5. The government of Zimbabwe must not rush into borrowing new money without being clear what the role of foreign lending is. There is need to examine the appropriateness of loans rather than assume an unquestioning assumption that loans are always necessary.
6. It is fair to say that to the extent that ESAP contributed to Zimbabwe's indebtedness, some creditors, in particular the IFIs must bear some responsibility. A debt audit may be able to make this fact more apparent.
7. Resources from natural resources must be used to provide development finance and invest in domestic infrastructure. The optimum use of wealth from natural resource must be supported by legislation that ensures a transparent tax system, open mining contracts and avoidance of resource pledging for loans.

Strategies for debt management must be located within a broader developmental vision that balances growth, obligations to repay and human development. Of all these, poverty eradication, human development and social and economic justice must take centre stage. Sound debt management entails keeping the cost of repayment at minimal while the very debt is employed to build repayment capacity and develop domestic funding mechanisms. Building internal and citizens based revenue capacity is crucial since the link between taxation, state building and democratization is now commonly accepted.



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About ZIMCODD

The Zimbabwe Coalition on Debt and Development, ZIMCODD, is a socio-economic justice coalition established in February 2000 to facilitate citizens' involvement in making public policy and practice pro-people and sustainable. ZIMCODD views Zimbabwe's indebtedness, the unfair global trade regime and lack of democratic people-centered economic governance as root causes of the socio-economic crises in Zimbabwe and the world at large. Drawing from community-based livelihood experiences of its membership, ZIMCODD implements programmes targeted at;

- Educating the citizen
- Facilitating policy dialogue among stakeholders
- Engaging and acting on socio-economic governance at local, regional and global levels

ZIMCODD's headquarters are in Harare with regional offices in Bulawayo, Chitungwiza and Mutare.

Vision

Sustainable socio-economic justice in Zimbabwe through a vibrant people based movement.

Mission

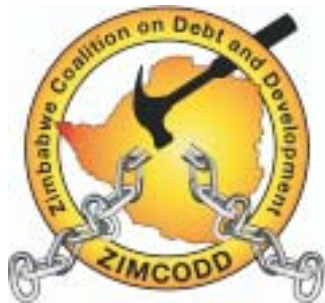
To take action in redressing the Debt burden and Social & Economic Injustices through formulation and promotion of alternative policies to the neo-liberal agenda.

Objectives

To raise the level of economic literacy among ZIMCODD members to include views and participation of grassroots and marginalised communities;

- To facilitate research, lobbying and advocacy in order to raise the level of economic literacy on issues of debt, trade and sustainable development;
- To formulate credible sustainable economic and social policy alternatives;
- To develop a national coalition, and facilitate the building of a vibrant movement for social and economic justice.





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ZIMCODD is a member of the Southern Africa Peoples' Network and currently hosts the SAPSN secretariat since 2003.

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