ZAMBIA

Table 1	2020
Population, million	18.4
GDP, current US$ billion	19.4
GDP per capita, current US$	1055.9
International poverty rate ($1.9)[a]	58.7
Lower middle-income poverty rate ($3.2)[a]	75.4
Upper middle-income poverty rate ($5.5)[a]	88.1
Gini index[a]	57.1
School enrollment, primary (% gross)[b]	98.7
Life expectancy at birth, years[b]	63.5

Source: WDI, Macro Poverty Outlook, and official data.
Notes:
(a) Most recent value (2015), 2011PPPs.
(b) WDI for school enrollment (2017); life expectancy (2018).

The COVID-19 crisis exacerbated Zambia's fragile macroeconomic situation in 2020. The economy contracted by 1.2 percent, reflecting the impact of lockdown measures and external shocks due to the pandemic. Poverty is estimated to have increased by just over 1 percentage point to 59.7 percent. A weak rebound is expected in 2021, but prospects for a stronger and sustainable recovery hinge on progress on debt restructuring and fiscal consolidation, the COVID-19 pandemic outlook, and reforming the current growth model.

Key conditions and challenges

Zambia's economic challenges in recent years have highlighted the need to diversify away from a mining-led development model. Zambia experienced a period of unprecedented growth averaging at 7.4 percent per annum over 2004-2014. This raised GDP per capita levels by nearly 53 percent, with the country becoming a lower middle-income country in 2011. These successes followed debt relief under HIPC in 2005, increased production in agriculture and mining along with rising global copper prices and investment in the social sectors. However, delays to unwind expansionary fiscal policies over the past decade in the face of copper price fluctuations and weather vagaries led to increasing macroeconomic and debt vulnerabilities. Debt to GDP increased from 23.8 percent in 2014 to 141.3 percent by 2020.

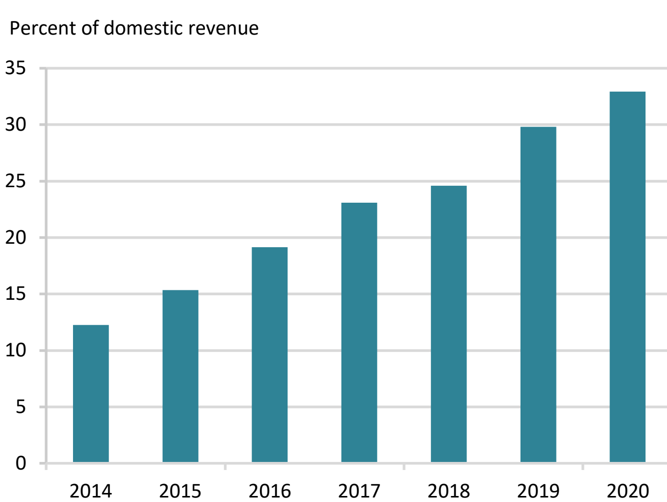
The Zambian economy was already at its weakest point at the onset of the COVID-19 pandemic. Growth in 2019 slumped to the lowest in two decades (1.4 percent), with drought conditions impacting agriculture, electricity and copper production. Expansionary fiscal outturn in 2019– an overall deficit of 11.4 percent of GDP, further constricted the country's fiscal space. Inflation started rising above the authorities' target band of 6-8 percent beginning June 2019 and the Kwacha depreciated by 18.3 for the year, leading to a tightening of monetary policy. By 2019, Zambia's debt was assessed to be at high risk of debt distress and unsustainable. Combined, these macroeconomic pressures led to a liquidity crisis by the end of 2019 and underlined the need for significant fiscal consolidation and diversification beyond mining.

Recent developments

The COVID-19 pandemic pushed into contraction an economy that was already weakened by recent persistent droughts, falling copper prices and unsustainable fiscal policies. Economic activity through Q3 of 2020 contracted by 1.7 percent, as declines in industry and services outweighed growth in agriculture. Mining and services suffered from lower global demand and social distancing measures earlier in the year, respectively. However, relaxation of the lockdown measures in second half and a global pick-up of copper prices helped activity to recover. Overall, the economy is estimated to have contracted by 1.2 percent in 2020 - the first recession for Zambia since 1998. Inflation remained in double digits throughout 2020--averaging 15.7 percent --and reached a high of 21.5 percent in January 2021.

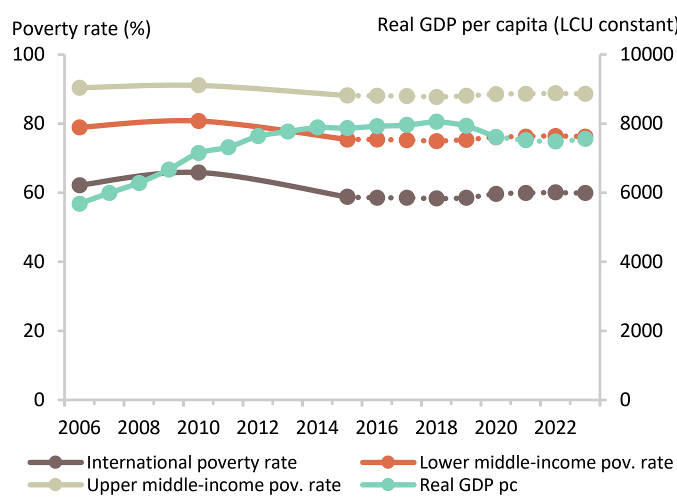
The COVID-19 pandemic has also deepened Zambia's fiscal and debt vulnerabilities. Falling revenues and COVID-related expenditures saw the fiscal deficit increase to 10.3 percent of GDP compared to an approved budget of 6.5 percent. The Kwacha depreciated by over 50 percent while reserves declined to $1.2bn even as the

FIGURE 1 Zambia / Interest payments on debt as a share of domestic revenues



Sources: Zambian authorities and World Bank Staff estimates and projections.

FIGURE 2 Zambia / Actual and projected poverty rates and real GDP per capita



Source: World Bank. Notes: see Table 2.

government accumulated over US$840mn in external arrears through December 2020—a clear reflection of increasing debt service pressures (figure 1). By September 2020, the government stopped servicing all external debt except for multilaterals and some priority projects; this was followed by a default on the Eurobond repayments in November. As debt became unsustainable, the authorities embarked on a debt restructuring process in early 2020 and in May hired legal and financial advisors to help them with the negotiations. The country's participation in the Debt Service Suspension Initiative (DSSI) has helped free up resources for the COVID-19 response. The government has also requested debt treatment under the G -20 Common Framework, agreement of which could help frame and support the debt restructuring process with all creditors. Restoring Zambia's external debt to sustainable levels will require significant debt restructuring, including debt reduction to reduce the present value of debt, and fiscal consolidation.

Poverty and vulnerability have increased due to the pandemic. The national poverty headcount rate is expected to increase by around 1.1 percentage points from 58.6 percent in 2019 to 59.9 percent by 2021. This is largely driven by increases in poverty in urban areas, and among those relying on employment income from the informal sector. A World Bank Household Monitoring phone survey found that 4 in 5 households reported a drop-in income from nonfarm business, and that 1 in 3 reported a reduction or disappearance of wages. Core recurrent spending, including social benefits, has suffered in recent years, with only about one third percent of the government's budget on social cash transfers (SCT) disbursed in FY20. While the government has budgeted for a higher amount in SCT in FY21, this could be further affected by the increasing fiscal pressures due to the crisis, with a substantial impact on the most vulnerable households in the population.

Outlook

A gradual recovery is expected, with GDP growth projected at 1.8 percent in 2021 and averaging 2.8 percent over 2021-23. Higher copper prices, the commissioning of a new hydro power station, and a return to normal rainfall patterns are expected to support growth in agriculture and electricity production, key contributors to Zambia's industry and service sectors. However, the impact of COVID-19 will continue to dampen activity, especially in tourism (about 7 percent of GDP) and retail and wholesale trade (20 percent of GDP). While the recent uptick in copper prices could help in ramping up mining activity in the short-term, a stable fiscal regime and clarity on the role of the state will be critical for regaining and increasing investment in the sector for longer-term benefits. Absent decisive policy interventions and in the face of fiscal pressures, poverty is expected to peak in 2022 at 60.0 percent.

The risks to this outlook are balanced. Timely achievement of macroeconomic stability will largely depend on progress on debt restructuring and to fiscal consolidation and the availability of the COVID-19 vaccines. However, a prolonged fallout from COVID-19 could amplify fiscal and domestic liquidity challenges, deepen exchange rate pressures, further weaken the base on which the Zambian economy is expected to recover, and lengthen the time for Zambia to embark on key macroeconomic and structural reforms. Rainfall variability remains a key structural risk to Zambia's sustainable growth, affecting key sectors like agriculture and electricity, and highlights the need to incorporate climate-smart solutions in the country's long-term growth strategy.

TABLE 2 Zambia / Macro poverty outlook indicators (annual percent change unless indicated otherwise)

	2018	2019	2020 e	2021 f	2022 f	2023 f
Real GDP growth, at constant market prices	4.2	1.4	-1.2	1.8	2.9	3.8
Private Consumption	1.2	2.3	3.1	3.6	4.5	4.5
Government Consumption	-14.9	-10.1	10.8	-15.8	-11.4	-4.4
Gross Fixed Capital Investment	9.9	-14.3	-29.9	8.9	6.1	12.6
Exports, Goods and Services	8.7	-7.2	10.8	8.6	9.8	6.9
Imports, Goods and Services	4.9	-13.7	-9.8	16.1	14.3	13.1
Real GDP growth, at constant factor prices	4.0	1.5	-1.2	1.8	2.9	3.8
Agriculture	-21.2	7.7	18.2	4.5	4.0	4.0
Industry	4.6	-3.3	-1.5	1.0	1.8	3.6
Services	7.3	3.5	-3.1	1.8	3.3	3.9
Inflation (Consumer Price Index)	7.5	9.1	15.7	21.0	19.0	10.0
Current Account Balance (% of GDP)	-1.3	1.1	8.4	6.5	5.9	3.5
Net Foreign Direct Investment (% of GDP)	1.4	-1.0	2.0	2.0	3.1	3.0
Fiscal Balance (% of GDP)	-10.1	-9.5	-10.1	-8.1	-5.6	-2.2
Debt (% of GDP)	77.8	88.4	84.2	76.0	73.1	100.3
Primary Balance (% of GDP)	-5.5	-5.6	-7.0	-3.7	-2.2	0.4
International poverty rate ($1.9 in 2011 PPP)[a,b]	58.3	58.6	59.7	59.9	60.0	59.9
Lower middle-income poverty rate ($3.2 in 2011 PPP)[a,b]	74.9	75.3	76.0	76.2	76.4	76.2
Upper middle-income poverty rate ($5.5 in 2011 PPP)[a,b]	87.7	88.0	88.5	88.6	88.8	88.6

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices.
Notes: e = estimate. f = forecast.

(a) Calculations based on 2015-LCMS-VII. Actual data: 2015. Nowcast: 2016-2020. Forecast are from 2021 to 2023.
(b) Projection using neutral distribution (2015) with pass-through = 0.7 based on GDP per capita in constant LCU.