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ZICA PRESIDENT'S 2020 FOURTH QUARTER MEDIA BRIEF ON VARIOUS NATIONAL MATTERS

21st DECEMBER 2020

Good Morning

Ladies and Gentlemen,

Welcome to the ZICA 2020 fourth quarter media briefing to discuss matters that affect the accountancy profession and the nation at large. In line with the Accountants Act of 2008, apart from our mandate of regulating the education and practice of the accountancy profession in Zambia, we have a statutory mandate to advise the Government of Zambia on matters relating to the economic development of the Country. In this media briefing, we will reflect on developments related to the following key matters:

1. ZICAs comments on the Country's Debt Distress and subsequent default;
2. Inflation and exchange rate performance and economic implications;
3. Energy Sector reforms;
4. ZICAs comments on the Auditor General's report including the Auditor General's COVID19 report;
5. Public Financial Management issues;
6. The Africa Continental Free Trade Area (ACFTA) and the implications on the profession;
7. National Electoral registration process & citizen participation; and
8. Caution on COVID19.

(i) ZICAS COMMENTS ON THE COUNTRY'S DEBT DISTRESS AND SUBSEQUENT DEFAULT

During the Budget presentation the Minister of Finance Hon. Dr. Bwalya Ngandu, MP announced that Government's External debt increased by 4.3% to US $11.97 billion from U$11.48 billion at end-December 2019. This was mainly on account of new disbursements on existing loans which were used to finance various projects in the energy, education, road and health sectors. The largest growth in debt of 9.9% was recorded under multilateral creditors. This was followed by Exports and Suppliers Credit at 6.73%, and private credit with an increase of 1.1%.

A detailed look at the domestic debt stock shows that Government securities increased to K114.3 billion as at end of August 2020 from K80.2 billion as end of December 2019 inclusive of the K8billion COVID-19 bond.

The Institute urges the Government to ensure they urgently come up with a plan on how they will dismantle the VAT refunds arrears as this is very key to smoothening the operations of the Mining Companies and give a policy statement on what is happening in the Mining Sector particularly with the uncertainties around KCM and Mopani Copper Mines.

Additionally, the Government recently announced a suspension of $120 million in interest payments to its Eurobond holders for the next six months. However, this request was rejected by a group of financial institutions holding 40% of Zambian Eurobonds which resulted in the country defaulting. A default on private debt is damaging in the eyes of investors, and credit rating agency Fitch downgraded Zambia to almost junk status after the Government sought to delay interest payments to Euro bondholders in September 2020. The Government needs to take this outcome with utmost caution as the country may risk facing a financial crisis which could result in flight of foreign direct investments and economic decline.

We commend His Excellency the President Dr. Edgar Chagwa Lungu and Government on the launch of the Economic Recovery Plan 2020 to 2023. Achieving the intended goal of the plan will require full coordination across all Government wings and total dedication by implementing agencies. A plan is only as good as its implementation and execution efforts. ZICA is still studying the report and will provide its comments and input in due course.

(ii) INFLATION AND EXCHANGE RATE

Inflation

The annual inflation rate in Zambia quickened for the third straight month to 17.4 percent in November 2020, reaching its highest level since September 2016. Prices increased faster for both food (16.8 percent vs 14.6 percent in October 2020) and non-food products (18.2 percent vs 17.7 percent in October 2020). On average inflation has increased by about **28 percent** this year from January 2020 when inflation was around **12.5 percent** and inflation is forecast to average 16.7 percent in the fourth quarter of 2020. In 2021, it is expected to decline to 13.5 percent and in 2022 to 10 percent on an annual average basis.

Inflation has been persistently above the central bank's target band of 6-8% for almost a year & a half and may accelerate due to the continued depreciation of the Kwacha against major convertible currencies. Government needs to take all necessary measures to rein-in inflation by implementing measures to restructure debt and implement key structural reforms on public expenditure.

Exchange Rate

The Kwacha depreciated against major convertible currencies, albeit at a slower pace mainly on account of increased foreign exchange market interventions by the Bank of Zambia. Against the US dollar, the kwacha weakened by 3.3 percent to an average of K18.94/US$ in the third quarter of 2020 and closed the quarter at K20.02/US$.

In September 2020, the Zambian Kwacha hit the K20 to the US Dollar mark and the Kwacha has depreciated by about 48% from January this year. The fall in the value of the Kwacha has been gradual with an accelerating trend since 2015.

The first and most significant factor affecting the Kwacha is that Zambia's' sovereign debt (foreign debt) is almost 90% to its Gross Domestic Product (GDP). The high percentage of debt to GDP is inconsistent with international standards, requiring that debt does not exceed 60% percent of a country's GDP. Zambia's' euro bond payment in terms of yields was due in the third week of November 2020 but this was not honoured resulting in a debt default.

The demand in foreign currency partly for debt servicing needs is driving the pressure on the exchange rate. This trend can also be traced from the last time Zambia's' payment was due in March 2020. There was so much pressure for the country to find foreign currency to cover the Eurobond interest payments during that period, resulting in the Kwacha's depreciation.

The second key factor is that the Country has not been generating enough revenue from Zambia's' minerals' exports, as most mining firms have cut down on production which has reduced the foreign currency needed to cover country's' needs. Additional pressure on Zambia's' reserves comes from the fact that the Country is importing more than it's exporting. This imbalance is adversely affecting the performance of the exchange rate.

The third factor relates to international perceptions around investment in Zambia's' capital market. Investors in Zambia's treasury bills and bonds have been liquidating their assets and taking these resources out of the country, resulting in capital flight and further putting pressure on the exchange rate.

(iii) ENERGY SECTOR REFORMS IN ZAMBIA

For historical reasons, most electricity infrastructure across the world has been State-owned, having been considered to be security strategic assets. Over the past decades, however, most countries have embarked on reforms to ensure increased investment and efficiency in the provision of electricity services. The key drivers for power sector reforms in Africa and other parts of the world have included:

- Inefficiencies in investment and operations (poor governance, few incentives for cost reduction, deterioration or collapse of services, etc);
- Insufficient public financing for capacity expansion;
- Part of overall economic restructuring (macro-economic constraints);
- Technological innovation (changing economies of scale and scope, new possibilities for competition; and
- Slow pace of investments in the power sector and resultant low levels of access to power.

The electricity industry in Zambia has been undergoing restructuring since 1994. The main thrust of the reforms has been to liberalise and promote private investment in the industry, particularly in the area of generation. The amendment of the Electricity Act in 1995 abolished the statutory monopoly of

ZESCO while the Energy Regulation Act of the same year established the ERB as an independent regulator of the energy sector.

Currently, Government's power sector reform strategy has focused on the Commercialisation of ZESCO, opening up to private investment and establishment of an independent regulator. The ERB and the Government continue to explore further means to promote investment and remove existing impediments to power sector investment in Zambia.

With load-shedding still a reality for Zambians, and national electricity consumption continuing to rise, it has never been more urgent to reform the country’s energy sector for a sustainable future.

The need for a reformed energy sector has been part of the budget speech from 2016 to date. In the budget speech for 2016 the Minister of Finance informed the nation that the Government would “consider options to improve both the technical and commercial efficiency in the electricity supply industry”, and spoke of the need to move towards cost-reflective tariffs to attract more private-sector participation in the industry. The Government would also review “the overall structure, governance and operations of the sector, including generation, transmission and distribution”.

That was arguably the clearest indication that Government was intending on producing an efficient, internationally competitive energy sector that is attractive to Independent Power Producers (IPPs), attractive to both industrial and domestic users, so as to make the sector a key driver of economic growth.

It is very clear that power utilities in Zambia need to be reformed to ensure high levels of efficiency and to drive investment in new power generation capacity. The persistent underperformance of the power sector in Zambia justifies calls for reform. The reforms should not just be aimed at achieving financial efficiency of utilities they must target such outcomes as affordable tariffs, increased access to electricity and improved quality of service.

For these reforms to have a satisfactory outcome they should focus on the long-term sustainability of the industry, strong competition in the industry, need for effective and independent regulator, policy stability, availability of skills, guaranteed property rights and predictable and stable tax laws.

Energy is a critical enabler to national economic development. Therefore, the sector's contribution to poverty reduction and wealth creation as outlined in the Seventh National Development Plan (7NDP) cannot be over emphasized. As you may be aware, Zambia is endowed with a wide range of energy resources, however investment in electricity generation has been undesirably low.

Currently, the electricity industry in Zambia is facing various challenges some of which include:

i. Low electricity tariffs resulting to non-cost reflective tariffs;
ii. Power generation deficit as a result of over reliance on hydro power which is susceptible to climate change; and,
iii. Little private sector participation to invest in the sector due to low tariffs etc.

These challenges have had a negative impact on the smooth functioning of the sector and as a result, they have led to poor service delivery and hampered the electricity sector's ability to drive economic growth and contribute fully to improved quality of life for all Zambians. Therefore, Government, has a task of resolving these challenges, while also considering:

i. Economic growth projections;
ii. Required investments in new generation capacity; and,
iii. Required investments for expansion of the transmission and distribution networks.

The Institute is aware that in early 2019 Cabinet approved a road-map on the reform programme and directed the Ministry of Energy to:

1) Develop a comprehensive reform program for the entire energy sector, with the transformation of ZESCO Limited as one of the components of the reform programme; and,

2) The Ministry was also directed to expedite the completion of the cost of service study in order to establish the true cost of supplying electricity.

The Institute calls on the Government to update the nation on the status of these steps. The Institute is convinced that the electricity reform programme once implemented will bring the following benefits to the nation:

i. Strengthen the Policy, Legislative and Regulatory Framework;
ii. Promote Integrated Resource Planning (IRP);
iii. Establish a framework to guide investment in power generation, transmission and distribution;
iv. Expedite implementation of the Cost of Service Study;
v. Transform ZESCO Limited with the view to improve its operations and capitalization;
vi. Balance the electricity supply-demand gap through Energy Efficiency and Demand Supply Management; and,
vii. Establish a framework multi-buyer multi-seller power trading.

We therefore urge the Government to commit to create a platform that will remove barriers and promote effectiveness in processes relating to investment in the energy sector in order to spur private sector participation in power generation;

In order to address the liquidity challenges that ZESCO is facing, the Ministry has to seriously priorities the sector reform agenda. Long-term financing need to be sought in order to restructure payables to Independent Power Producers (IPPs) and suppliers, although, this will be a challenge in view of the company's weak financial position, tariff adjustment also needs to be considered in order to avert further losses and allow the utility to recover some of its current operating and maintenance costs. Lastly, priority should be given to revision of the Electricity Act, the Energy Regulation Act and the National Energy Policy which will further contribute to the sectors responsiveness to the country's energy needs and unlock the sector for increased private sector participation.

(iv) ZICA COMMENTS ON THE AUDITOR GENERAL'S REPORT

We are very concerned on the revelations by the Auditor General on the Interim Audit Report released on the utilisation of COVID-19 resources for the period February 1st to July 31st 2020. That report has revealed that a total of over K1.3 billion was mismanaged in various transactions, which included questionable transfers from GRZ accounts amounting to K60 million and up to K3 million in cash withdrawals.

The report highlighted financial irregularities in the utilisation of COVID-19 resources with the highest being an over-commitment of K652 million, which entailed that procurements made for various medical supplies were not adequately supported by an approved budget and exceeded the entire budget.

The report also highlighted problematic awarding of contracts amounting to K384 million as the second highest irregularity. Under this irregularity, some suppliers supplied medical supplies before signing procurement contracts. This was followed by procurement contracts awarded without competition in amounts totaling K194 million. The Ministry of Health also engaged in uncompetitive procurement through cover bidding in respect of four contracts amounting to K10 million. Cover bidding occurs when a competitor submits bids that are intended to be unsuccessful so that another conspirator can win the contract, thereby, giving an unfair advantage to a specific supplier.

The irregularities identified in the COVID-19 report of the Auditor General need to be fully investigated by Government to their full conclusion. Relevant sanctions on any erring officers must be swiftly imposed to ensure that impunity does not take root especially during such a difficult period as is the ongoing COVID-19 pandemic era.

We wish to indicate that the Institute is concerned that the audit findings mentioned in the Report for the financial year ended 31st December 2019 still show concerns that keep on repeating year on year.

Some of the findings raised in this Report are:

i. Weaknesses in the implementation of Information and Communications Technology (ICT) systems,
ii. Failure and delays in the collection of Government revenue,
iii. Failure to maintain books of accounts and accounting records,
iv. Weaknesses in procurement and contract management,
v. Failure to update and reconcile the Establishment Register and the Staff Assignment,
vi. Failure to deduct and remit statutory contributions,
vii. Failure to secure properties with title deeds, and
viii. Failure to insure Government assets.

We are looking forward to a more robust financial management to safeguard national assets. We are hopeful that with qualified men and women in strategic positions of Accountant General, Auditor General and Controller of Internal Audit most of these queries will no longer continue to appear.

(v) AFRICA CONTINENTAL FREE TRADE AREA (ACFTA)

The African Union Heads of State and Government at an Extra Ordinary Summit on 21st March 2018 in Kigali, Rwanda signed the African Continental Free Trade Area (ACFTA) Agreement and its Protocols including the protocol on Trade in Services. Further the AU Heads of State and Government approved five priority services sectors for the first round of negotiations: accountancy, business, communication, financial and tourism.

The Zambia Institute of Chartered Accountants (ZICA) has been participating in the trade in services working group to specifically negotiate on the movement and mutual recognition or otherwise of finance professionals within Countries in Africa. These meetings are aimed at defending the position of countries amidst the free movement of various professionals being advocated for by ACFTA. Even if full market access by professionals is the ideal under ACFTA, countries still need to retain some form of regulation to safeguard their markets and local qualifications against infiltration. The idea is to have a fully integrated African Union and help the continent harmonise reciprocal treatment of professionals who move from one country to the other in Africa. The latest guideline indicates that the ACFTA is effective 1st January, 2021. As an Institute we will continue to participate in further engagements being coordinated by the Ministry of Commerce, Trade and Industry to safeguard the integrity of the Accountancy profession in Zambia. The Institute would like to emphasise the need for the professionals & the Country at large to prepare for a wider market but also competition.

(vi) NATIONAL ELECTORAL REGISTRATION PROCESS & CITIZEN PARTICIPATION.

Since the Government commenced the voter registration process, the Institute has observed the long queues across the country for citizens acquiring voter's cards. This happening during a period when we must see social distancing and near zero crowding. The Institute proposes a reform in the electoral process to allow for voting without voter cards and at any place in the country a qualifying citizen would find themselves at during the national elections. Additionally, the reform should allow for all citizens that possess a National Registration Card to be able to vote as opposed to having a second card, the voters card, as is the case at present.

(vii) CAUTION ON COVID19 AND VACCINE DISTRIBUTION

As we draw closer to the festive season, the Institute would like to urge the public to exercise utmost care during the festivities by practicing social distancing, hand sanitizing, washing hands regularly with soap and avoiding handshaking.

As you may be aware, there has been a major breakthroughs regarding the development of COVID-19 vaccines which have reached advanced stages. In view of the foregoing, the Institute would like to implore the Government to come up with the national vaccine distribution strategy and plan that will speak to the protection of front line staff as soon as the most vulnerable. The vaccine distribution strategy should ensure that all persons in the Republic would be able to receive the vaccine within the shortest period possible. It should utilize the existing vaccine delivery infrastructure while leveraging innovative distribution approaches, new public-private partnerships, and robust engagement of faith groups, tribal authorities, and non-governmental partners to ensure efficient, effective, and equitable access to COVID-19 vaccines.

Lastly, it will be imperative that strategic communications and public messaging are developed in various local languages through the national media as this is critical to ensure maximum acceptance of vaccines across the country. The work must begin now to prepare for a vaccine administration period.

(viii) CONCLUSION

In conclusion, we wish to commend Government for giving professional Institutions like ZICA an opportunity to give professional advice on economic and national matters. We look forward to more engagements and cooperation with both the public and private sectors in the year 2021.

I wish to thank you members of the press for coming and your dedication to the duty of informing the public of developments happening at the Institute and the nation at large.

The Institute would like to take this opportunity to wish all its members and cooperating partners a merry Christmas and a prosperous new year.

I am happy to clarify any aspect of our statement, otherwise we look forward to seeing you at our next quarterly briefing.

Cecilia Zimba
PRESIDENT
ZAMBIA INSTITUTE OF CHARTERED ACCOUNTANTS