KPMG

Economic Snapshot H1, 2017

Zambia

Inflation overview – Headline inflation decreased from 6.8% year-on-year (y-o-y) in February 2017 to 6.7% y-o-y in March. Single-digit inflation is expected for the next few years - remaining well within the central bank's target of 6%-8%. The Bank of Zambia (BoZ) is expected to continue cutting its key policy rate during 2017, after having reduced rates for the first time in five years in February 2017.

Growth summary – Real GDP growth is forecast on an upward trajectory during 2017-2018 following a weaker trend in 2015-2016. However, growth will remain below the pre-2014 commodity boom years due to copper production that remains structurally lower than before. In order to ensure greater economic stability and growth, the country needs to develop a sustainable, diversified and competitive agriculture sector.

Economic policy – The government launched its 'Zambia Plus' economic recovery programme in October 2016, aimed at boosting economic growth to the 7% level deemed sufficient to reduce poverty. The scheme focusses on strengthening tax policy and administration, increasing budgetary allocation to social protection, improving economic and fiscal governance, and improving the country's economic stability.

Trade & Investment SWOT

Strengths	Weaknesses
The Zambian Development Agency (ZDA) has provided a clearer framework and a variety of incentives for foreign direct investment.	Portfolio investment is limited due to the lack of secondary trading in equities.
Lusaka Stock Exchange (LuSE) is well established, with reasonable liquidity and good connections to international financial markets.	Investments under $10 million are not eligible for certain tax breaks and incentives.
Zambia has one of the most open trade environments in Africa and is a member of the Southern Africa Development Community (SADC) and the Common Markets for Eastern and Southern Africa (COMESA).	Fitch Ratings downgraded Zambia's national credit rating in 2013 due to weakness in public finances and government expenditure acts as a barrier to investment.
Businesses in Zambia benefit from among the lowest profit taxes in the region.	High levels of trade bureaucracy add significantly to shipping lead times to and from Zambia, which undermine trade competitiveness.
Opportunities	**Threats**
The streamlining of some bureaucratic procedures which has already taken place suggests that further improvements are possible.	Amendments to the Companies Act could see minimum quotas for domestic investment imposed in some industries.
Developing ICT legislation and e-government readiness will improve the security and ease of business activity in Zambia.	Corruption continues to be a serious issue.
Mining continues to attract FDI, while the manufacturing, energy, agriculture, tourism and infrastructure sectors provide alternative opportunities for FDI.	Rising capital outflows to overseas markets have created a deficit in the financial account, which drags on balance of payments and economic openness in Zambia.
Increasing regional cooperation through multilateral organisations, including SADC and the African Union should continue to reduce the likelihood of interstate conflict.	Rising commercial activity driven by GDP growth, coupled with a rapidly increasing population will place mounting pressure on utilities and transport infrastructure which already struggle to meet demand.

Source: Business Monitor International (BMI)

Mega trends

Population	2017	Total: 17.24 million; female: 8.63 million; male: 8.61 million; age 0-14: 45.53% of total; age 15 +: 54.47% of total; age 65+: 2.88% of total
Population growth rate	2015	3.07%
Life expectancy at birth	2014	Total: 60.05 years; female: 61.96 years; male: 58.23 years
HIV/AIDS	2015	Total number of people living with HIV: 1.2 million; total adult prevalence: 12.9%; HIV/AIDS orphans (age 0-17): 0.38 million
Adult literacy rate	2015	Total population: 85.12%; female: 80.57%; male: 58.23%
Urbanisation	2015	Urban population: 40.92% of total; annual urban population growth: 4.18%; rural population: 59.08% of total
Population below $1.90 per day poverty line	2010	31.59%
Unemployment rate	2017	Total: 7.4%; female: 7.5%; male: 7.3%; youth (15 - 24): 13.6%
Employment	2012	Agriculture: 52.2% of total; industry: 9.5% of total ; services: 38.3% of total
Labour participation rate	2017	Total (ages 15+): 75.33% of total population
Business languages	n/a	Bemba, Nyanja, Tonga, Lozi, Lunda, Kaonde, Luvale, English
Telephone & Internet users	2013	Fixed telephone subscriptions: 0.12 million; wired internet subscriptions: 0.02 million; cell phone subscriptions: 11.56 million (2015)

Sources: UNESCO Institute for Statistics, World Telecommunication/ICT indicator database, World Development Indicators, UNAIDS, International Labour Organisation

Human Development Index (HDI) 2015		Index of Economic Freedom 2016		Global Competitiveness Index (GCI) 2016		Doing Business 2017		Corruption Perceptions Index 2016	
139th	out of 188 countries	106th	out of 179 countries	118th	out of 148 countries	98th	out of 189 countries	87th	out of 177 countries

Source: Transparency International, Doing Business, World Economic Forum, UN Human Development Report, The Heritage Foundation

Sovereign Risk Ratings		
S&P Global Ratings	**Fitch Ratings**	**Moody's Investors Service**
B/Negative	B/Negative	B3/Negative

S&P Global Ratings affirmed Zambia's long-term foreign sovereign credit ratings at "B" in February 2017, with a negative outlook. S&P is concerned about the fiscal financing pressures that will increase further due to high debt service in 2017 and weaker economic growth momentum. This prompted its analysts to keep the rating on a negative outlook. Overall, Zambia has limited fiscal financing options at its disposal. "*The increase in copper prices could provide an important boost to government revenues and support foreign currency inflows into Zambia. However, the government's fiscal position remains difficult,*" commented the agency. S&P could lower the ratings over the near future if plans to put public finances on a sustainable path is further delayed or if the levels of investment remains low or worsen, which would increase external financing needs and further worsening economic growth. The ratings could be affirmed at their current levels if sustainable fiscal and economic policies are in fact implemented efficiently, which will assure financing conditions and an acceleration of economic growth.

Fitch Ratings affirmed Zambia's long-term foreign Issuer Default Ratings (IDR) at "B" with a negative outlook in February 2017. Zambia's persistent fiscal deficits and structural constraints has kept economic growth below potential and constrained the country's rating. From a ratings perspective, these weaknesses are balanced against an "*improving fiscal and external outlook, enhanced monetary policy credibility and the potential implementation of a fiscal and economic adjustment agenda*". The main factors that could lead to the ratings of Zambia being downgraded include: not being able to access external sources of financing (leading to liquidity and funding shortfalls), failing to stabilise the government debt ratio, and a further deterioration in external balances, for example through a significant fall in copper prices (Zambia's largest export product). The main factors that could lead to the negative outlook being revised by Fitch to a stable include: an economic reform programme that leads to sustained higher growth, effective fiscal consolidation that narrows the fiscal deficit and stabilises the general government debt ratio and a rise in international reserve coverage, which will effectively reduce Zambia's vulnerability to external shocks.

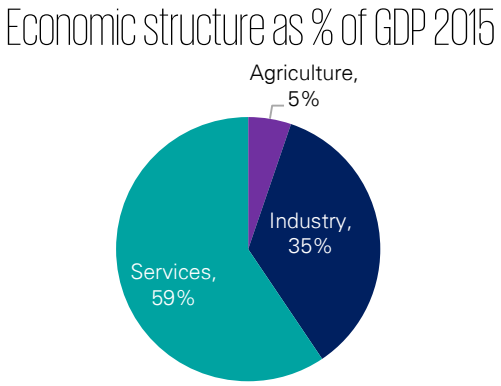
Moody's Investors Services rated Zambia with a "B3" government bond rating with a negative outlook in March 2017. The prospects for the country's economy are positive, according to the rating agency, as copper prices are rising gradually and there is extra mining capacity and reduced electricity shortages in the country. The outlook on Zambia's rating could change to stable if the trends behind the negative outlook disappears or reverses over the next 12-18 months. Stabilising the rating would occur in the event of Zambia containing the fiscal deficit and if there is increased certainty surrounding government fiscal policies and funding sources. The country is "*vulnerable to external factors, particularly copper price shocks and a slowdown in China's growth, a major trading partner*".

Quality of infrastructure	Economic diversity	Banking sector	Continuity of economic policy	GDP growth	Fiscal / current account balances	Foreign investment	Socio-economic development	Forex reserves
Low quality but improving	Dominated by the copper sector	Dominated by subsidiaries of foreign banks	Recovery plan launched in October 2016	Recent decline, projected slow recovery	Twin deficits	Healthy inflows	Low	Sufficient

Stock market	Listed companies	Liquidity	Market capitalisation	Largest sector	Weekly trading volume
Lusaka Stock Exchange (LuSE)	25	Moderate	$2.7 billion Source: African Alliance	Retail	$857 000 Source: African Alliance
Capital market	**Level of development**	**Liquidity**	**Maturity range**	**Municipal bonds**	**Corporate bonds**
Yes	Developed in an African context	Low	91 days to 15 years	No	Yes

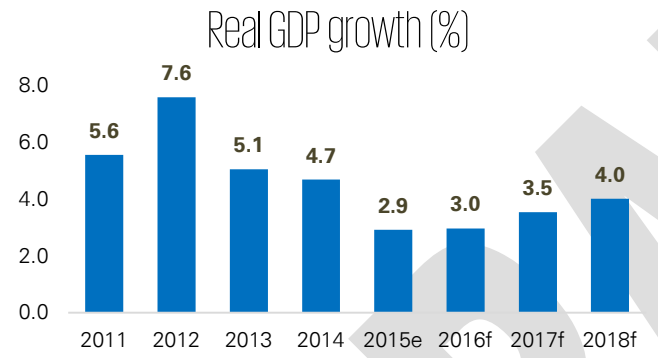
Macroeconomic overview

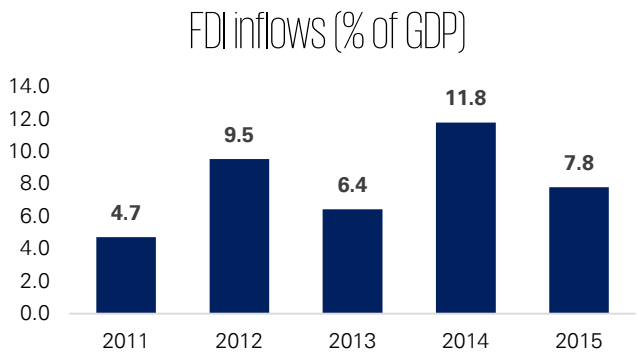
Economic structure – The primary sector in Zambia comprises of crop farming, livestock rearing and fisheries, and the staple crop in the country is corn. The agricultural sector is the backbone of the Zambian economy as it contributes to the growth of the economy and also to exports, even though it contributes the least to GDP. Mining, construction and manufacturing together make up the majority of the secondary sector. Growth in the manufacturing industry is largely driven by the agro processing of food and beverages as well as the textiles and leather subsectors. Manufacturing absorbs much of the output from other sectors such as agriculture, and also supplies inputs into the other secondary sectors such as mining and construction. The Zambia Development Agency (ZDA) Act provides various incentives for companies investing in the mining sector in the country. Zambia is a large producer of copper and the commodity is the country's largest export product. The tertiary sector includes a large wholesale and retail trade industry. Tourism in the country is also growing and has a positive knock-on effect on transport and accommodation providers.



Source: World Bank: World Development Indicators

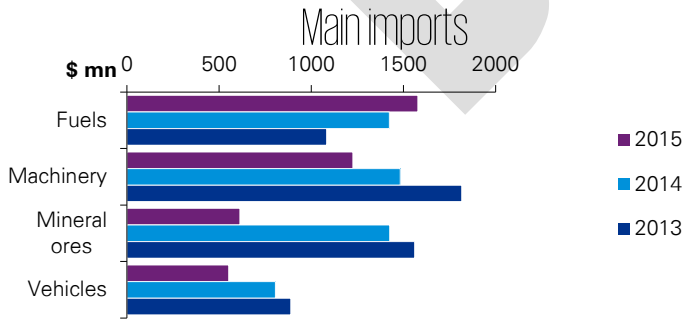
Economic growth – Real GDP growth is forecasted on an upward trajectory during 2017-2018 following a weaker trend in 2015-2016. Growth is predominantly driven by domestic copper production and associated exports. The economy will also benefit from rising investment as investor's appetite to enter Zambia returns after a period of rigid tax policies in 2015. However, going ahead, data from the International Monetary Fund (IMF) shows that GDP growth will remain below the pre-2014 commodity boom years. This is due to copper production that remains structurally lower than before as a result of the electricity crisis. Zambia's 2017 national budget revealed that in order to ensure greater economic stability and growth, the country needs to develop a sustainable, diversified and competitive agriculture sector. To ensure a competitive agricultural sector, and to reduce risks related to drought, the government has committed to promote diversification to cash crops such as cotton, cashew nuts, soya beans, cassava and rice.

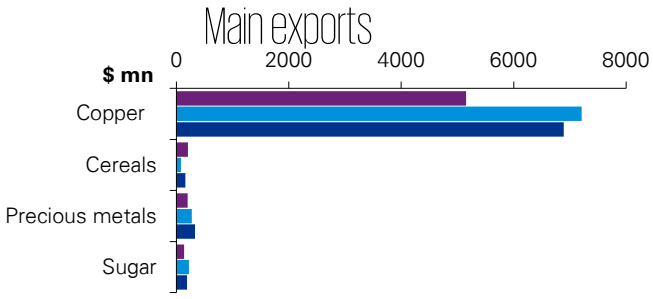




Sources: IMF, United Nations Congress on Trade and Development (UNCTAD)

Foreign investment – Overall openness to investment in Zambia is better than most of its Southern African peers. The Zambian government has outlined a clear foreign direct investment (FDI) framework in the country and there are various Special Economic Zones (SEZs) and incentives on offer for foreign investors. There are also no restrictions imposed on which sectors foreign business are allowed to participate in. In 2015, Zambia's inward FDI stock amounted to $16.5 billion, which is equal to 75.6% of GDP. This reflects that Zambia is open to foreign investment in terms of policy and that FDI is intrinsic to the Zambian economy. From 2014, FDI growth slowed down to an extent due to the slump in global copper prices, while in 2015 there was policy uncertainty with regards to Zambia's mining tax regime. Even though the Zambian government is open to FDI and the investment environment comes with various incentives for foreign investors, there are still some structural barriers which presents risks for future FDI.





Main Imports: % share of total	2013	2014	2015
Fuels	10.7%	14.9%	18.7%
Machinery	17.9%	15.5%	14.6%
Mineral ores	15.4%	14.9%	7.3%
Vehicles	8.8%	8.4%	6.6%

Main Exports: % share of total	2013	2014	2015
Copper	65.0%	74.4%	73.8%
Cereals	1.5%	0.8%	2.9%
Precious metals	3.1%	2.8%	2.9%
Sugar	1.8%	2.3%	1.9%

Source: Trade Map

External trade –Zambia's current account deficit is expected to narrow towards the end of the forecast period in 2018. The country's exports will receive a boost from the recovery in the country's copper sector as well as rising global prices – the country's trade dynamics remain highly dependent on this commodity. In February, the finance Minister Felix Mutati said that production is set to exceed 800 000 metric tonnes in 2017, higher than the 2013 record of 790 000 tonnes. Additionally, increasing foreign exchange earnings, a stable kwacha and fiscal consolidation will temper external financing needs, resulting in less pressure on Zambia's external accounts

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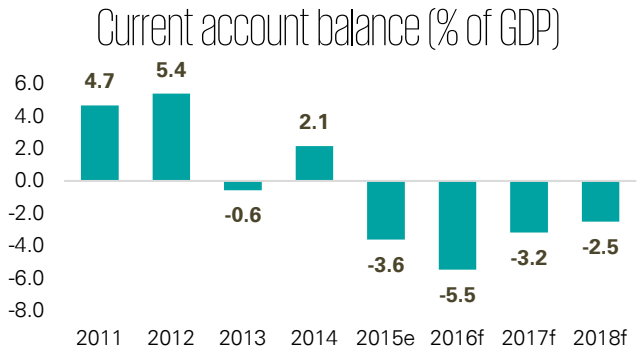
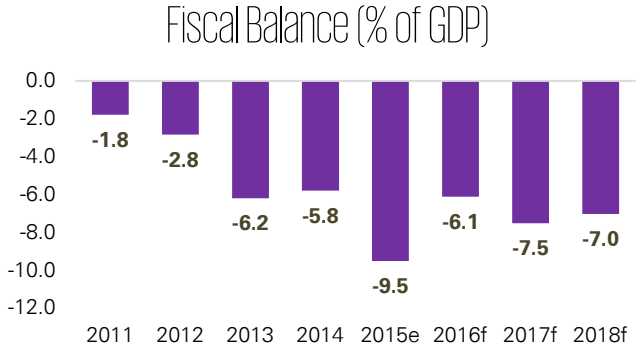
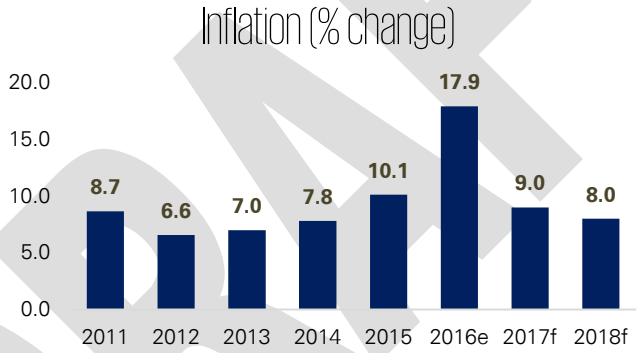




Source: IMF

Fiscal policy – Zambia's fiscal position is set to improve this year due to improvements on both the revenue and expenditure side of the budget. Falling copper prices led to a sharp slowdown in revenue growth from 2014 to 2016, while the government kept expenditure growth elevated. Fiscal pressures should, however, ease in 2017 as the copper sector recovers. BMI forecasts Zambia's copper production to grow in 2017 for the first time in three years. Furthermore, government revenue will receive a boost as consumer's purchasing power increases – leading to higher private consumption. The government will likely continue to limit fuel and electricity subsidies as well as additional employment in the public sector in an effort to narrow the fiscal deficit. With regards to the public sector, capital spending will slow as the government limits new capital projects until ongoing projects are completed. This slowdown in large projects, mainly financed through high-cost borrowing, will have a positive effect on the fiscal balance and reduce the fiscal shortfall. .



Source: IMF

Monetary policy - Headline inflation decreased from 6.8% y-o-y in February 2017 to 6.7% y-o-y in March, associated with favourable developments in the food basket. The Bank of Zambia (BoZ) is expected to continue cutting its key policy rate during 2017, after having reduced rates for the first time in five years in February 2017. Single-digit inflation is expected for the next few years - remaining well within the central bank's target of 6%-8%. The central bank also uses the sale or purchase of foreign exchange in the market as an instrument in monetary policy – since 2015, the supply of US dollars has helped stabilise the kwacha. This contributed to the Zambian currency recovering from almost ZMK14/$ in November 2015 to below ZMK10/$ in April 2017. Furthermore, auctioning of government securities also help regulate the stock of money and control inflationary pressures in Zambia.

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