April 6, 2001
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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 00/120

12:30 p.m., December 6, 2000

Contents

Executive Board Attendance

H. Köhler, Chairman
S. Fischer, First Deputy Managing Director
E. Aninat, Deputy Managing Director
S. Sugisaki, Acting Chairman

Executive Directors	**Alternate Executive Directors**
S.M. Al-Turki	A.S. Alosaimi
A. Barro Chambrier	D. Ondo Mañe
T.A. Bernes	P. Charleton
	M.S. Hililan, Temporary
R.F. Cippà	S. Bonomo, Temporary
	W.-D. Donecker
	R. von Kleist, Temporary
	H. Vittas
	G. Schlitzer, Temporary
D.I. Djojosubroto	Low K.M.
K.-T. Hetrakul, Post Designate	P. Lathouly, Temporary
V.L. Kelkar	
W. Kiekens	J. Prader
	C. Josz, Temporary
O.-P. Lehmussaari	A. Fidjestøl, Temporary
K. Lissakers	P.A. Brukoff, Temporary
J.-C. Milleron	G. Bauche
A. Mirakhor	
A.V. Mozhin	A. Lushin
	S. Vtyurina, Temporary
H. Oyarzábal	F. Varela
S. Pickford	S.P. Collins
	H. Mori, Temporary
C.D.R. Rustomjee	I. Usman
A.S. Shaalan	K. Sakr, Temporary
	Jin Qi
	Liu F., Temporary
J. de Beaufort Wijnholds	
Y. Yoshimura	H. Toyama
	G.R. Le Fort
	D. Vogel, Temporary

S.J. Anjaria, Secretary
A. Mountford, Acting Secretary
P. Cirillo, Assistant
S.T. Djumena, Assistant

Also Present

M. Camdessus, former Managing Director; Mrs. Camdessus, A. Kafka, Mrs. Köhler, P. Narvekar, J.J. Polak, L. van Houtven. IBRD: Y. Ansu and F. Yagci, Africa Regional Office. African Department: G.E. Gondwe, Director; E. Hernández-Catá, Associate Director; P.A. Acquah, Deputy Director; J. Fajgenbaum, Deputy Director; L. Erasmus, T. Harjes, G.G. Johnson, M. Katz, A. Kovanen, P. Neuhaus, N. Pillay. Asia and Pacific Department: A. Singh, Deputy Director. European I Department: J.R. Artus, Deputy Director. European II Department: J. Odling-Smee, Director. External Relations Department: T.C. Dawson, Director; G. Hacche, Deputy Director; M. Fouda. Fiscal Affairs Department: G.T. Abed. IMF Institute: S.M. Nsouli, Deputy Director. Legal Department: F.P. Gianviti, General Counsel. Middle Eastern Department: P. Chabrier, Director. Monetary and Exchange Affairs Department: V Sundararajan, Deputy Director. Policy Development and Review Department: J.T. Boorman, Director; L.P. Ebrill, G.R. Kincaid, L.Y.M. Leigh. Research Department: M. Mussa, Economic Counsellor and Director. Secretary's Department: A.S. Linde, Deputy Director; S. Bhatia, J. Prust, T. Turner-Huggins. Statistics Department: C.A. Enoch. Technology and General Services Department: I.E. Prebensen, Deputy Director. Treasurer's Department: M.G. Kuhn, Deputy Treasurer. Western Hemisphere Department: D. Goldsbrough, Deputy Director. Office of the Managing Director: A.A.E. Bertuch-Samuels, Special Advisor; S.B. Brown, Advisor, C. Salmon, Personal Assistant; E.L. Archer, A. Bauer, D.A. Citrin, D. Elie-Goodall, K.S. Moses, S. Tiwari; Office of Budget and Planning: E.-A. Conrad, Director; Office of Internal Audit and Inspection: R Muñoz, Director. Office in Europe: S.P. Leite. Advisors to Executive Directors: J.M. Abbott, M.P. Bhatta, J.A. Costa, S.S. Farid, O.A Hendrick, N. Jadhav, J.M. Jones, M. Lundsager, I. Mateos y Lago, J. Ntamatungiro, L. Palei, S. Thiam, M. Yanase, F. Zurbrügg. Assistants to Executive Directors: A.S. Al Azzaz, N. Budina, I.- K. Cho, V. Dhanpaul, E. González-Sánchez, K. Harada, F. Haupt, S.K. Keshava, T. Koranchelian, D.H. Kranen, J. Kwakye, Liu Z., J. Mafararikwa, W.C. Mañalac, D. Merotto, D. Nardelli, E. Nyambal, K. Ongley, C.A.E. Sdralevich, B. Siegenthaler, T. Skurzewski, Sugeng.

1. MANAGING DIRECTOR—PORTRAIT

The Chairman unveiled the official portrait of the former Managing Director, Mr. Michel Camdessus.

The Chairman made the following statement:

> Michel, it is an honor for me to welcome you back to this Boardroom. It is also a pleasure to see our distinguished former colleagues, Alexandre Kafka, P.R. Narvekar, Jacques Pollack, and Leo Van Houtven here with us today.
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> Before I took this job, Michel, we discussed various measures, but I forgot to ask you what it is like to be seated here as Chairman of the Executive Board. I must tell you that I have discovered that it is a humbling experience—not only because of all these difficult issues and crises, but because sitting here in this chair I am aware of the history of the Fund, especially of all those illustrious people, our predecessors, to whom we owe so much.
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> Michel, this occasion provides us—staff, management, and the Executive Board—an opportunity to recognize and honor your tremendous contributions to this institution from 1987 to 2000, a remarkable 13 years. During this period, the international community faced many challenges, and each time the Fund, under your stewardship, rose to the occasion. Let me mention a few instances.
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> One of the first issues that Michel Camdessus confronted as Managing Director was how to deal with the worsening poverty in sub-Saharan Africa and other regions, and from the beginning of his tenure he was committed to this issue. He had a deep conviction that the international community had to find better ways to help low-income countries, to achieve sustainable growth and reduce poverty. This led to the creation of the Enhanced Structural Adjustment Facility, and later the Poverty Reduction and Growth Facility. In the same vein, during the 1990s, to deal with the special problems of low-income countries with unsustainable debt burdens, Michel, together with Jim Wolfensohn, was able to bring together the multilateral institutions and bilateral donors to put in place the HIPC Initiative, which is now of so great interest to us and which I am sure we will make a success. I hope the success will also be seen, Michel, as being contributed particularly by your initiative and management.
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> In all of this, Michel, combined a central banker's impulse for sound policies with a strong human instinct to do the right thing. These same traits led him to press for increased attention to issues of excessive military spending and weak governance.

Another milestone that the Fund faced during Michel's tenure was the fall of the Berlin wall and the collapse of the Soviet Union. Dealing with the political, economic, and social consequences of this historic event was a daunting task, and I remember because I was involved in this closely at the German finance ministry and in hindsight not always to the best of the Fund's task.

In those circumstances, we all marveled at the Fund's swift response to come to the aid of these countries, so that they could be integrated into the international monetary system.

Michel guided the Fund as it became a truly global institution with near universal membership and he was personally involved with putting in place the first Fund-supported programs with these countries. While we may differ in our judgment about the transition countries, clearly, there is success and particularly a development beyond the point of no return toward democracy and market economy.

A recurring theme of Michel's work and one that was accentuated toward the end of his tenure was helping members adapt to a globalized world. In his various conversations with authorities, civil society, and academics, Michel spoke at length about what countries could do to position themselves so as to maximize the benefits of globalization, while minimizing the risks and avoiding marginalization. We must continue this effort in the ongoing work of the IMF.

With the crisis in 1994, the opportunity was confronted with what Michel termed the first financial crisis of the 21st century and at that time you also predicted that next crisis would be a banking-financial sector crisis. How right you were.

In response to the crisis in Asia and later in other regions, the Fund was able to quickly put together programs to begin restoring financial market confidence and help members to restore macroeconomic stability. Under your leadership, the international community could count on an IMF that delivered. You also realized that fundamental reform was needed and out of this were born the various initiatives to strengthen the architecture of the international financial system.

Michel, you made the Fund a different place. A better one, and one better able to adapt to the fast-changing global environment.

I have spoken about Michel Camdessus as Managing Director. But, let us not forget his many qualities as an individual which we admire.

He is a tough negotiator, but at the same time a deeply compassionate and spiritual human being. A man with insatiable energy and vitality, a kind spirit, with a flair for wit and charm, and I took very much to my heart that he himself said in an interview, "To survive in this job, you need to have a sense of humor." While it may not always remain true for a German to have a particular kind of sense of humor, I take it as a very important direction.

For these and many other reasons, Michel, your colleagues will always hold you in deep affection.

And our gratitude has to go also to Brigitte Camdessus. She stood by her husband with patience and I am, sure, often personal sacrifice. Brigitte helped Michel maintain the necessary strength and perseverance, to do the demanding job in the public interest. So, as part of our gratitude to you, I would like to present you with these lovely flowers we have prepared for this occasion.

After presenting a bouquet of flowers to Mrs. Camdessus, the Chairman then unveiled the official portrait of Mr. Michel Camdessus.

The Chairman then reiterated the Fund's gratitude for all his contributions to the institution. The portrait, which would maintain Mr. Camdessus permanently in the annals of the Fund, would, together with those of his predecessors, be a reminder to maintain the high standards that he had set.

The Chairman then invited the Dean of the Executive Board, Mr. Mirakhor, to deliver some brief remarks.

The Dean of the Executive Board of Directors, Mr. Mirakhor, made the following statement:

I would like to say that it is a pleasure for us to see Michel here, and I would welcome, also, Mrs. Camdessus and Mrs. Köhler. The unveiling of your portrait is a symbol of honor that this institution and this Board is bestowing on you for your dedicated and distinguished service to the institution and its membership.

The end of the artist's work is hanging on this wall, but the historian's work—trying to capture the essence of the Camdessus era—is just beginning. It was a vital and unique era, characterized by one of our colleagues in the Board some time ago as an era when talent, tenacity, and temperament met tempestuous times with grace and a sense of high purpose.

On behalf of my Board colleagues, Michel, I take this opportunity to extend to you and Madame Camdessus our best wishes.

Mr. Camdessus made the following statement:

Well, Mr. Chairman, I must tell you that I am overwhelmed. It is not the first time I am overwhelmed by the kindest of words I hear in this room. But, I can tell you that not only am I overwhelmed, but I am as intimidated as the first time I took this gavel here and I said, "The meeting is called to order."

Of course, I saw frequently the faces of my predecessors in this room, but I did not imagine that the day would come when I would be attending the unveiling of my own portrait. You have with kind words reminded me of 13 years of history, 13 years of work together in this Executive Boardroom. When you were talking, I was reading in the faces of several of our colleagues here this very history. You have in the Board, still, people who were here before me, including Mr. Polack, Mr. Kafka, Mr. Narvekar, Mr. Van Houtven, Mr. Wijnholds (who was an Alternate Executive Director when I arrived here), and Mr. Shaalan (who was a member of the staff). There were several others, and of course there were those who joined when the history was unfolding, and all that you have so generously attributed to my own activity. In my view, all this must be attributed to the contribution of the Board, and of individual members of the Board.

I am proud to say, and I repeat it in my speeches in Europe and other parts of the world, that there is something unique here. It is the way in which people are able to come from so different backgrounds and cultures, to work together constantly and to reach a consensus on the most tricky and controversial issues of the time. The fact that we unanimously agreed on so many difficult issues is a testimony to the quality of the relationship among the members of the Board, and between the Board and management and staff. As a matter of fact, I must tell you that I am now changing a little bit my speech, because two weeks ago, I was again making this point about the ability of the IMF to reach a consensus on issues of the most extreme difficulty, and then somebody, a very distinguished theologian, told me, "Well, I do not like your story about consensus. When there is such unanimous consensus, something must be wrong, there must be some underlying forces there, bringing to this consensus." Well, he was wrong, and I told him that. I tried to explain, but he gave me food for thought, and I will try to adapt that part of my description of the Board's work. But what is true, is that there is something unique about this quality of trust among all these people. It is the source of the strength of this institution and the quality of its contributions to the world.

Thank you also for inviting Brigitte to this meeting. Now, she will understand better why I did enjoy so much to spend so many hours here. She will also understand why every evening I returned home in a very high spirit and good humor; but, of course, this was also due to her contribution, which you have so well characterized.

Let me also take advantage of this occasion to thank our colleagues for the many demonstrations of their affection and friendship on the occasion of my departure from the Fund, including, the large and extraordinary leather-bound book I received a few weeks ago in Paris. It is a huge book, containing many letters from your authorities, former members of the Board, ministers, and presidents, and the speeches from the members of the Board when I left, telling me so excessively kind things. I will have that there with me, so that from time to time I can show it to my children, and from time to time, if I will be depressed, I can open it to get a better image of myself. You know, from time to time one needs that!

So, let me thank you very much for it, and for all those who called and stopped by in Paris. And I hope that those who have not yet done so, will remember their promises they made to me.

About the portrait, well, I must tell you that I had, from time to time while working here in the Board, asked myself whether it was better to be hanging here, or to be sitting here. Now, I can tell you that both are fine, in the right order.

I must express my thanks to the Board for placing my portrait there. For someone who had a problem with his image for 13 years, seeing an unveiling of a portrait is a high-stakes occasion. However, thanks to Mr. Zoccali, the choice of the artist was superb, and you could be sure that, the artist being better than the model, the painting would be a good painting. Now, you will possibly have the impression that I am a little bit stiff, but it is quite a test to spend six hours sitting still and trying to look statesman-like, especially when you are used to gesticulating and moving around. So, perhaps this stiffness reflects the effort I made to have a dignified attitude that would fit well with this Executive Board.

I am especially grateful to you all for this occasion to meet together. Let me tell you that these past few months have demonstrated that there is life after the Fund. They have only strengthened my very strong feeling that this institution does its work well, and one can be proud to have been part of it.

My best wishes to you, Horst, and to Eva for your time here in Washington, D.C. Many years will pass before your portrait is hanging there, but, you will enjoy these years. You have an extraordinary task, but you will have the formidable support of the Board and the staff. You told me already that you are enjoying this work thoroughly. As you are a man who likes challenges and working hard, you will be more satisfied every day in the job, and you will have more success in doing it.

Finally, thanks to all who have made these 13 years so beautiful and so rewarding for me, and best wishes to all your families.

2. ZIMBABWE—2000 ARTICLE IV CONSULTATION

The Executive Directors considered the staff report for the 2000 Article IV consultation with Zimbabwe (SM/00/254, 11/15/00; and Sup. 1, 12/1/00). They also had before them a background paper on recent economic developments and selected issues in Zimbabwe, and a statistical appendix (SM/00/262, 11/27/00).

Mr. Rustomjee made the following statement:

At the outset, the Zimbabwean authorities are very grateful for the constructive role which the Fund, the Bank and the donor community continue to play in helping the country move forward with its economic development process. They thank the Fund staff for their fair, accurate and candid assessment of recent and current economic developments in the country.

The immediate picture illustrates that Zimbabwe's short-term outlook is challenging; there is need to stabilize the macroeconomic environment, pursue a viable land reform, restore investor confidence, fight against HIV/AIDS and reduce unemployment in order to enable the economy to turn around. Against the background of these considerable short-term difficulties, it is also important to recognize that the upside potential for Zimbabwe, once the range of short-term policy issues are addressed, is significant. The country is endowed with natural resources, a highly educated labor force, well developed infrastructure, one of the highest productivity growth rates in the region and represents an important trading partner to several other economies in the region.

The authorities appreciate the difficulties facing the economy and the urgency with which they have to act. The new economic team that was appointed after the June 2000 parliamentary elections, in which the opposition gained a substantial number of seats, moved quickly to adjust the exchange rate in order to ease the foreign exchange shortages, increased fuel and electricity tariffs to improve the financial situation of these utility companies and disclosed the costs associated with Zimbabwe's involvement in the Democratic Republic of Congo (DRC).

The real test of the authorities' resolve to turn the economy around is contained in the 2001 Budget which was announced on December 16 and is under discussion in parliament. This Budget projects a major improvement in the primary fiscal balance from a deficit of 6 percent of GDP in 2000 to a surplus of 4.3 percent of GDP in 2001. The Budget was formulated against the background of high inflation, a declining economy and the realization by the new economic team that failure to stabilize the economy in the past was due in substantial part, to fiscal lapses.

The budget now faces a structural problem where 81 percent of total expenditures are non-discretionary and little is left for social sectors and infrastructure. The new budget, elaborated in the staff supplement (SM/00/254), targets a drastic reduction in the public sector wage bill and military expenditures. To realize these cuts, wage negotiations and the civil service retrenchment exercise have been decentralized to line ministries while peace is being pursued in the DRC within the context of SADC and the UN. To ensure that line ministries live within their allocations, a cash budgeting system has been introduced and a computerized Public Finance Management System is being made applicable to all ministries. Professional finance managers are being appointed and will be supplemented by private accounting firms who will undertake special audits. The new budget also sets an important new trend in the allocation of expenditures where by more resources will be earmarked for health, education, infrastructure, fighting against HIV/AIDS and other poverty reduction activities. These efforts are consistent with the approach of the new economic team, which is to progressively shift the composition of budgetary expenditures towards poverty alleviation and infrastructure development.

On the revenue side, Zimbabwe portrays an over-taxed economy with total revenue collections close to 30 percent of GDP, despite significant exemptions. The 2001 budget contains revenue measures aimed at simplifying the tax system and reducing the tax burden while enhancing revenue collections. To strengthen tax administration and collection, the National Revenue Authority will become operational in the first quarter of 2001 and preparations are being expedited to introduce VAT in 2002. It is intended that fiscal consolidation will rely more on expenditure reduction.

The authorities have also presented a medium-term fiscal framework which aims at reducing the fiscal deficit to 3 percent of GDP by 2003 from about 23 percent in 2000. In this connection, the 2001 budget has set a target to accelerate privatization with a view to retire domestic debt and reduce the borrowing requirements of Government. The authorities have also authorized local authorities to charge economic tariffs for their services beginning January 2001.

To reduce inflation, a number of measures were taken recently to tighten monetary policy, including linking interest rates to inflation and interest rates are positive in real terms. In support of the 2001 Budget, the stance of monetary policy will remain sufficiently tight until inflation is brought under control. The role of the central bank has also been strengthened in its oversight of the financial sector, capital adequacy ratios for the banking system are being enforced and measures are being taken to reduce non-performing loans. The central bank has benefited from a number of MAE missions and some of the advice has been fully implemented.

On the external sector, the authorities are concerned about the poor export response to recent exchange rate devaluations and are undertaking a study on the issue. In addition, the fallout of the emerging market crisis, the sharp increase in oil prices and general terms of trade loses are weighing heavily on external sector performance and Zimbabwe is currently facing serious shortages of foreign currency. Against this background, the authorities have committed themselves to adjusting the exchange rate in line with the need to maintain competitiveness. Nevertheless, they are also of the opinion that given the current situation prevailing in the country, exchange rate devaluation is not the panacea, and they are giving the highest priority to reducing the fiscal deficit, bringing inflation under control and restoring investor confidence.

As a result of the shortage of foreign exchange, the authorities could not discharge their external obligations on time and external payments arrears have accumulated. They have made a commitment to clear these arrears once the foreign exchange situation improves. In this connection, the authorities are close to clearing their arrears to the World Bank and they remain current with regards to payments to the Fund.

Zimbabwe has been making steady progress towards the liberalization of trade. More recently, the number of tariff lines have been reduced by 1180, the maximum tariff has been scaled down and the average tariff including surcharges has been reduced from 39 to 36 percent. The authorities are engaged in regional free trade initiatives within the SADC and COMESA. A trade agreement with South Africa, the major trading partner in the region, is also being negotiated.

Turning to the land issue, it is important to underscore that land reform represents a pressing and historical challenge which is deeply rooted in the economic legacy of the pre-independence era. World Bank studies have conclusively shown that land reform in Zimbabwe is a central issue in enhancing Zimbabwe's long-term growth potential and is capable of improving the productive capacity of labor and capital in agriculture, increasing employment, stabilizing the rural economy and reducing poverty. This reality was also acknowledged by the UNDP administrator in his press statement of December 1, 2000 after he visited Zimbabwe. It is the intention of the authorities to pursue a land reform strategy that reduces imbalances in the ownership of fertile land while improving productivity in agriculture and reducing poverty among the 75 percent of the population that lives in the rural areas. The UNDP are actively engaged with the authorities in working out the modalities for providing technical assistance for the exercise and this mobilizing donor support for land reform.

> The authorities are also aware of the need to improve governance. Cases of corruption are being pursued by the police and the courts and measures are being put in place to recover public funds from cases that have been concluded, as announced in the 2001 Budget. Parliament has also strengthened its oversight role in the management of public resources and has formed the Budget and Portfolio committees. The Minister of Finance is required to submit quarterly reports on the economy and the budget to Parliament. The new Finance Minister is also on record as having set about enhancing transparency and public disclosures from the start of his term and in that same spirit, he has authorized the publication of the staff papers.
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> In conclusion, Zimbabwe faces a difficult and complex set of economic, social and other challenges. It is authorities' hope that they will be able to conclude negotiations soon with the Fund on a program that could help catalyze external assistance. The 2001 Budget offers important proposals to enable Zimbabwe to begin benefiting from its resource potential. In this regard, there is evidence that technical assistance provided to Zimbabwe has benefited the country and it would be of great value to the new economic team if this assistance could be redoubled, particularly at a time when improvements in the statistical data and the management of fiscal policy are initially needed.

Extending his remarks, Mr. Rustomjee stated that the authorities had consented to publishing the staff report. However, they requested the deletion of market-sensitive information, including the level of reserves and some specific aspects of the exchange rate policy. The authorities had also prepared additional comments which they suggest to be annexed to the their comments to the published report.

The authorities were of the view that the report generally presented a candid, fair, and balanced assessment of Zimbabwe's current macroeconomic position. They were hopeful that their decision to publish the report, which presented a difficult picture of Zimbabwe's current condition, could be viewed as an expression of the determination of the new economic team, which had come into office since the parliamentary elections this year, to conduct economic policy formulation in a transparent and open manner, and in close dialogue with the Fund and other international financial partners.

The conduct of economic policy since the new team took office would hopefully be recognized by the Board as being worthy of further encouragement. Some movement on the exchange rate issue existed, although, as staff had noted in the supplementary paper, there had been no further change in the exchange rate since October 20. Also, the new Minister had been candid in disclosing the costs of war in the Democratic Republic of the Congo, an issue which had been kept largely secret until the new economic team took office. The new Minister had also shown himself to be determined to shift the orientation of the budget toward poverty alleviation and social spending.

At the time of the last informal Board meeting on November 8, the Board had noted that considerable emphasis should be placed on the outcome of the budget speech, which took place on November 16. The 2001 budget presented scope for encouragement. The Minister had indicated his determination to reduce the fiscal deficit to 15.5 percent of GDP next year, currently at 23 percent, and to 8 percent and 3 percent in the subsequent two years. A systematic rather than a large one-off reduction in the deficit was the more sustainable approach. The approach taken by the Minister, which tried to lock in deficit reductions progressively, was the right one and should be supported. In addition, the national revenue authority was set to become operational in the first quarter of 2001. Work had also commenced, although at a preparatory stage, on implementing the VAT in 2002.

The Minister had weighed whether to visit Washington to speak with management and staff as well as Board members prior to the passage of the 2001 budget, but had opted to wait until the budget had passed through parliament. He hoped to visit the Fund in January of next year. The budget would again provide further opportunity for encouragement and for obtaining further detailed advice from management, staff, and the Board.

It was important that the Board considered nurturing and encouraging the new team. Other examples existed, where early engagement by other institutions had locked in the promise of sustainable economic reform over a longer period. That would be the case in Zimbabwe as well.

Mr. Barro Chambrier made the following statement:

> We commend the staff for this well written report and Mr. Rustomjee for his helpful and comprehensive Buff which clearly outlines the challenges facing the Zimbabwean economy. Continued weaknesses in macroeconomic policies, especially in the fiscal area, combined with governance problems and the political turmoil have undermined investor confidence and curtailed international assistance. Zimbabwe is in the midst of a serious economic and financial crisis, and vigorous efforts are needed to address the problems that have developed and to stabilize the economy. In this regard, we welcome the courageous measures taken by the new economic team that was appointed in June 2000, but these need to be fully supported by a comprehensive set of policies, which do not appear to be the case. The political situation is also difficult and it will be very important that the authorities gather the necessary consensus to design a package of policy measures along the lines recommended by the staff. These should encompass both financial as well as structural reforms. Land reform, governance issues, the fight against poverty and against HIV/AIDS which threaten the economic fabric of the Zimbabwe society are issues that should receive the full attention of the authorities. Overall, it is of crucial importance that the authorities embark quickly on such a reform program which can receive both domestic as well as international support.

Recent Economic Development

The Stand-By Arrangement of 1999 went off-track. Several performance criteria were missed. As a result, the economic crisis deepened in 2000, fuelled by mounting fiscal imbalances, further deterioration of competitiveness and election-related violence. Real GDP contracted markedly in 1999 and 2000. Inflation accelerated to about 61 percent and could reach 80 percent by year-end. The budget deficit increased due to wage, defense overruns and high interest payments. The tightening of monetary policy failed to curve inflation, reflecting continued fiscal imbalances and supply constraints. Government domestic borrowing pushed high interest rates and crowded out the private sector. Although some progress was made on trade liberalization and fuel pricing, structural reforms stalled. On the external front, the combination of lax domestic policies, investor skepticism, the pegging of the currency since January 1999 and the unstable neighboring environment led to the erosion of competitiveness, shortages of foreign exchange, and the building-up of arrears. On the social front, the rapid spread of HIV/AIDS in recent years and a deterioration of living conditions are becoming key challenges to Zimbabwe's socio-economic development. In the absence of fundamental changes aimed at stabilizing the economy, improving governance and restoring domestic and donor confidence, Zimbabwe could fall into an economic and financial collapse.

Medium Term Prospects

Against this background, medium term economic prospects remain given the unused production capacity. GDP growth could rebound in 2002 and rise to 4.5-5 percent in the outer years, provided that the authorities gather a broad consensus to implement an adjustment package aimed at stabilizing the economy and paving the way for the resumption of sustained growth. We are encouraged by the first steps taken by the new economic team to address the country's problems and increase transparency, as evidenced by the devaluation of the currency and increased information to the civil society regarding defense outlays. However, the reform package will only bear fruit if the authorities are committed to restoring confidence through prudent and more predictable macroeconomic policies, improving governance and restoring the rule of law, especially as regards land reform. Implementation of measures taken in these key areas would help ease domestic tensions and improve relations with the international community.

Fiscal Policy

Fiscal consolidation will play a critical role in Government strategy to revive the economy because it will reduce Government borrowing and thus help release resources for the recovery of private sector activity. It will also reduce inflation and balance of payments pressures. We welcome the

Government's commitment to reduce the fiscal deficit from 23 percent of GDP in 2000 to 3 percent in 2003. Fiscal adjustment should heavily rely on expenditure restraint given the depressed economic activity and, the high level of taxation. In order to reach the fiscal targets without jeopardizing efforts in social sectors and infrastructure, the authorities are encouraged to reduce expenditure in non priority areas and improve their composition. To this end, we see merit in substantially curtailing the unsustainable wage bill and defense outlays. Fostering structural reforms such as civil service reform and restructuring/privatization of public enterprises could also help reduce the budget deficit. These measures would free resources for protecting the most vulnerable social groups and maintaining investment in basic infrastructure for the resumption of growth. On the revenue side, given the depressed economic activity the high level of taxation which is already around 30 percent of GDP, we encourage the authorities to broaden the tax base, and improve tax administration, especially through the setting up of the autonomous National Revenue Authority. Moreover, utility companies which are currently subsidized and whose prices are still below cost recovery levels should be given more flexibility for periodic adjustments in fuel and electricity prices, which could help improve the fiscal situation.

Monetary Policy

Monetary policy faces the challenge of curving inflation while avoiding a generalized weakening of the economy that could adversely affect the financial sector. We therefore encourage the authorities to speed up a strong fiscal adjustment so as to ease the heavy burden on monetary policy. Also, a greater exchange rate flexibility could help bring inflation down and to avoid a prolonged overvaluation of the currency. As regards the soundness of the financial system, we welcome the Government's commitment to strengthening bank supervision and encourage the authorities to finalize guidelines for dealing with troubled banks.

External Sector

On the external front, we encourage the authorities to pursue efforts to liberalize the trade regime in order to spur competition and improve resource efficiency. We also advise the authorities to normalize their relations with external creditors and formulate a timetable for the elimination of arrears in order to pave the way for renewed international assistance and possibly debt rescheduling. Given the counter-productive economic impact of foreign exchange control, we urge the authorities to unify the exchange rate system, to liberalize access to foreign exchange for current transactions and to simplify the export surrender requirements.

Governance issues

The reform program may not succeed unless the Government reduces the political tensions, and uncertainties, and improves transparency in public sector management. In this regard, we welcome the steps taken by the authorities to curb corruption and improve budget management and control through the establishment of Oversight Committees in the parliament. However, sending strong signals to the international community and domestic stakeholders regarding the prevalence of the rule of law will be critical. We recognize the challenge facing the authorities in resolving the contentious issue of land reform and the related inequalities. However, we concur with the staff that the reform process must be conducted in a lawful manner so as to dispel uncertainties regarding property rights and the availability of crop financing in an economy which is already depressed. Given the potential adverse impact of any abrupt disruptions of farm output on the rest of the economy, we encourage the authorities to work closely with the donor community and spell out a careful phasing of reform in line with available resources. As regards transparency, we encourage the authorities to improve the reporting of economic statistics and request technical assistance if needed. These efforts would help Zimbabwe restore its image as a credible investment location and have spillover effects in the sub-region.

Social Sector

The rapid spread of HIV/AIDS and the related pandemics in recent years together with a decline in living standards are the most daunting challenges facing Zimbabwean decision-makers as the country enters a sustained adjustment period. On the one hand, a weakening in the fiscal stance is putting serious strains on the public health system and eroding earlier gains in social indicators. On the other hand, the human burden of HIV/AIDS hampers economic development through lowering the supply of skilled labor. We commend the commitment of the authorities, the Fund and the Bank to working together in future adjustment programs to help improve the conditions of living of the poor and give special attention to fighting HIV/AIDS.

Conclusion

In conclusion, we share the staff assessment and encourage the authorities to take the necessary measures that could pave the way for a Fund-supported program.

Mr. Kelkar made the following statement:

Our chair would like to support the thrust of the staff appraisal which underscores the need for developing a broad political consensus for designing and implementing a stabilization policy package to emerge from the present serious crisis. Though we are encouraged by the positive steps taken by the new economic team, a number of measures are still required for stabilizing the economy and achieving sustainable growth over the medium term. We are happy to note from the helpful buff statement of Mr. Rustomjee that the authorities are determined to overcome the challenges to achieve the true growth potential of Zimbabwe.

The reasons for the predicament that the Zimbabwe economy finds itself in at present are not hard to identify if one is to read the chronology of the events since the last consultation. Performance under the 1998 SBA and its successor approved in August 1999 remained very weak and the economic situation continued to decline. While the factors for decline in economic activity are both external as well as internal what is striking is the breakdown of underlying social consensus which has made the macroeconomic measures rather ineffective. Any indecisiveness in the policy framework or weak governance would not only jeopardize the stabilization process but also would allow the crisis to continue unabated. Zimbabwe urgently needs to take corrective actions to emerge from the weakening in economic activity, high inflation, and a looming financial crisis. The spread of HIV/AIDS has eroded earlier gains in social indicators. There seems to be an urgent need to bring down inflation to moderate levels and rebuild foreign exchange reserves which presently are at an extremely low level. The authorities also need to resolve the land reform issue in a fair and transparent way at the earliest.

The authorities face the difficult task of exercising expenditure restraint and achieving fiscal consolidation, while improving the composition of public spending. Given the enormous needs to address the problem stemming from HIV/AIDS and other social needs, the move of the authorities to start the operations of the autonomous revenue authority early next year should result in improved tax administration and collection. We endorse the recommendation of the staff for broadening the tax base, and eliminating preferential tax regimes, exemptions and loopholes. Also periodic adjustments in fuel and electricity tariffs will reduce the need for budgetary support to the utility companies. The authorities are encouraged to continue with their efforts to accelerate the privatization process in 2001. Given the structural problem in the budget with a substantial proportion of expenditure being non-discretionary, the authorities are moving in the right direction by targeting a drastic reduction in the public sector wage bill and non-priority expenditures.

We welcome tightening of the monetary policy stance to bring inflation under control. It is also encouraging to know that the role of the central bank has been strengthened in its oversight of the financial sector; efforts are being made to reduce non-performing loans; and capital adequacy ratios for the banks are being enforced. The staff has argued for greater exchange rate flexibility preferably by floating the currency or effective discrete adjustments under the crawling peg. Our chair sympathizes with the stand of the authorities that, given the current prevailing situation in the country, an appropriate course of action at this stage would be reduce fiscal deficit, bring down inflation, and restore investor confidence in the Zimbabwean economy. The authorities are also encouraged to clear the external payments arrears once the external position strengthens.

It is true that Zimbabwe has been going through an economically tumultuous period but it is evident that the authorities are keen on establishing policy credibility. This would require refocusing efforts on macroeconomic stabilization. But given the external and internal vulnerabilities at this juncture, it would be desirable to consider the request of the authorities to arrive at an agreement on a program that could help in catalyzing external assistance. If this is not done, the more fundamental agenda of structural reforms will be unreasonably delayed and the economy may in fact become more vulnerable both from the macroeconomic as well as social point of view. Our chair also endorses the request of the authorities for additional technical assistance.

In conclusion, we wish the authorities continued success in their policy endeavors.

Ms. Vtyurina made the following statement:

If anything, it is rather sad to read about the recent developments in Zimbabwe not only from the staff report but also from the abundant discussion in the media about the country's deteriorating situation. A lack of a strong response from the authorities to address macroeconomic imbalances denies the Zimbabwean population of a hope for recovery. To make things worse there has been a further decline of heath and social indicators, and Box 4 presents a gruesome picture of the state of the HIV/AIDS pandemic. I have to admit though that Mr. Rustomjee's statement brought a bit of assurance that the authorities are trying to aid the present situation, but measures being undertaken by them still do not seem to be sufficient.

I share most of the staff analysis. It is quite obvious what needs to be done to stop the economic and social corrosion. However, judging from the analysis in the paper the response from the authorities to the staff advice so far has been weak. Neither do the markets see the government's policies as adequate which is evident from a significant deterioration of the market sentiment over the past year. Allow me to comment on some of the issues being debated.

The Confederation of the Zimbabwe Industries last week released a survey on the market's perception of the state of the economy. The results are rather troublesome. It has been identified that at least one quarter of the manufacturing companies operating in the country are going to divest from the country in the next few months. The main reasons sited are: extremely high level of inflation, shortage of foreign exchange, low effective demand, exchange rate regime rigidity, erratic fuel supply, and disruption of agriculture. There are basically the same concerns the staff have voiced in the papers. Now the question is what the authorities can and should do to address the aforementioned deficiencies.

On the fiscal side, consolidation is absolutely necessary, I am glad to see that the authorities have agreed with the staff on this issue. While the staff's proposed budget deficit is 10.5 percent of the GDP, the authorities have indicated that the budget needs to be more realistic so to avoid repeated expenditure overruns of the past. I tend to agree with this and will come to this point later. Therefore, the authorities' target for the budget deficit is 15.5 percent of the GDP for the next year. However, even this number is considered by the analysts to be too optimistic given the magnitude of problems, and especially lack of coordination between the fiscal and monetary policy management.

To see how much contraction is realistic, it is important to look at the reasons behind a dramatic deficit increase of recent years. As I understand, the rise in the deficit from only 4.8 percent in 1998 to whopping 22.8 percent estimated for this year is a result of sharply higher government borrowing due to a shortfall in foreign financing and subsequent significantly higher interest payments. Of course, a drastic increase in the wage bill and a projected two-fold increase in military expenditures have exacerbated the situation further. On the other hand though, education outlays are also projected to have increased significantly this year. Health outlays appear to be higher than budgeted as well. The last too, while being positive developments, are still not considered to be adequate.

Given the fact that corporate and personal tax collections are going to be much less because of businesses closings and subsequent layoffs, and that numerous tax deductions are going to take place, and that improvements in the tax administration will take time, it seems that expenditure cuts are the authorities' only alternative. I note that both, the authorities and the staff, agree that major cuts have to come out of military and wage expenditure. However, given the country's circumstances and the pressure coming from the affected groups, it appears doubtful that a 12 percent deficit contraction proposed by the staff can be achieved. I think at this point it would be important for the government to stick to their budgeted deficit target and try to stay on a path of a proposed three-year rolling framework for deficit reduction.

In any event, the deficit will remain high and so will the interest rates. This leads me to the monetary policy conduct. It is said that markets are awaiting for the Reserve Bank to come out with a statement in the next few weeks on new measures on how to deal with the persistently high inflation and punitive interest rates. The recent measures taken by the Bank on the exchange rate regime are not considered to be adequate since the shortage of foreign exchange continue to be extremely large and the inflation is soaring. More fundamental measures have to take place for the situation to improve. A market determined exchange rate, and monetary and fiscal tightness are warranted to stop further deterioration of social and investment conditions.

On the structural front, I have noted that the government has stepped up its efforts on the privatization and that it has identified an initial list of assets for disposal and privatization over the next three years. It is said that the successful implementation of the program is expected to raise at least Z$23 billion and that the proceeds will be used to clear the external arrears, retire part of the domestic debt and capitalize a revolving fund for SMEs. This initiative is commendable and, if the results are as hoped for, they will give the government some breathing space. However, as are the staff, we are rather doubtful that given the worsening of the economic conditions and sagging rule of law there will be much investor interest.

Finally, a comment on the deteriorating health situation. It is indeed devastating to see the projections on HIV/AIDS. It is rather unfortunate that the efforts that have been put into the prevention of this disease are not generating better results. But there is a belief that the AIDS awareness campaign in Zimbabwe has largely failed because of poor funding, lack of government direction and increasing poverty. This is highly regretful. We do, however, commend the government for their recent steps to increase spending on AIDS prevention through disbursement of moneys from the National AIDS Fund. We also welcome the announcement of plans to set up a National HIV/AIDS Endowment Fund to the tune of $20 million to take over the responsibility from the existing fund. We wish the authorities determination in this difficult battle.

Mr. Lathouly made the following statement:

The situation in Zimbabwe at this stage needs urgently prudent economic measures to stabilize the economy. We appreciate the comprehensive staff report and the clear statement made by Mr. Rustomjee. With this in mind we would like to emphasize some of the staff's recommendations on the following issues.

Without strong and consistent policy measures, it would be difficult for the authorities to achieve its economic reform program launched in 1991 and to recover from its economic crisis that they have faced presently. Therefore, we encourage the authorities to take urgent steps to restore fiscal discipline particularly by trimming defense budget, restraining wage increase, reducing unproductive expenditures and encouraging the private sector wherever possible.

On the monetary front, although we are encouraged by the initial performance of the newly appointed economic team of the government, we urge the authorities to further tighten the money supply by restraining rapidly rising government borrowings from the banking sector. Also, interest rate should be liberalized in a gradual manner and exchange rate policy should be more flexible and realistic.

We urge the authorities to intensify the structural reforms, particularly the resumption of privatization program, civil service reform and trade liberalization to improve the resource allocation, to increase competitiveness and to avoid monopolistic practices. The authorities should also pay special attention towards good governance and the law and order should be restored as soon as possible especially regarding the land reform in order to create confidence internally as well as internationally.

We agree with the staff that the authorities should normalize relationship with its external creditors and formulate a timely plan for elimination of the public sector's external payment arrears in order to increase creditworthiness of the authorities in the international community.

Finally, in order to help the authorities to improve the economic situation, we support the Fund's continuation of technical assistance to Zimbabwe.

We wish the authorities well in their future endeavors.

Mr. Collins made the following statement:

Let me begin by saying that we strongly endorse the very candid staff report, which gets to the core of Zimbabwe's regrettable decline in recent years. This decline is regrettable not only for the hardship it has inflicted on Zimbabweans, but for the risk that it could precipitate a financial crisis, which would have serious repercussions for neighbouring countries.

In pointing this out clearly, this staff report is one of the most direct, honest, and--as Mr Rustomjee notes—fair, that I have seen. I thank staff for their efforts under trying circumstances, and I particularly welcome the new Finance Minister's agreement to publish the report. I regard that as a positive signpost in an otherwise dismal landscape.

It is worth reiterating the main points which staff bring out. Over the past 12 months the Zimbabwe economy has contracted significantly. Government has contributed to this decline through poor governance and lax economic policies. At the heart of this lies unsustainable fiscal policy. This has led to the build-up of a precarious level of domestic debt of short maturity, and led Government to resort to 'printing money', which has fuelled inflation.

In addition, the slow movement towards a market-determined exchange rate and the existence of a parallel market has exacerbated the shortage of foreign exchange, hurt exporters and harmed investor confidence.

I join staff in urging Zimbabwe's authorities to tighten fiscal policy and maintain monetary control to help bring inflation down. And to restore external balance and assist exporters, I also join staff in urging the authorities to introduce flexibility in the exchange rate to narrow the gap with the parallel market.

As staff note in paragraph 9, the decline in law and order, the handling of the fast-track land resettlement process, the emergence of serious governance problems and breaches in property rights--all have created serious uncertainty. This has damaged the important agricultural sector, decimated tourism, and undermined investor confidence throughout the whole economy. These effects will linger. Agricultural production is expected to decline again in 2001 by around 10 percent, and manufacturing output is expected to fall by 5 percent.

Poverty is rising sharply as formal employment is lost from the tourism, mining and manufacturing industries, farm workers are displaced, and as 60% inflation erodes the value of incomes. Against this background, and taking into account the impact of the HIV/AIDS pandemic, medium term prospects for Zimbabwe look bleak unless positive steps are taken.

I therefore join staff in urging the government to muster a broad political consensus to turn this situation around. The new economic team appointed in July, spearheaded by Mr. Makoni, have taken a step in the right direction with signs of an intent to make some of the necessary hard choices in the 2001 Budget. However, I share the implication of the staff's supplement that, when one looks closely at the assumptions, and at Zimbabwe's past performance, there must be doubts as to whether the 2001 budget can be achieved. I welcome the intention to withdraw Zimbabwean troops from DRC, to reduce the real wage bill of the public service, and to accelerate privatisation. However, it will require broad political support to achieve these outcomes. My authorities urge the Government to demonstrate their commitment to the measures announced by following through with the early implementation of key reforms.

Simply addressing the economic policy failings alone will not suffice in securing a turnaround in the Zimbabwean economy. Governance problems have destroyed confidence – both domestic and international. This confidence will only be restored when the Government of Zimbabwe takes action to restore law and order and to ensure a fair and transparent land redistribution process.

If the Government does not demonstrate a commitment to both economic and governance measures in 2001 we are likely to see a widening of the fiscal deficit, hyperinflation, more dramatic declines in the domestic economy, and a likely introduction of price and interest rate controls.

This would result in even greater shortages of goods and further increases in poverty. And as staff note, the likely financial crisis which would ensue would have repercussions in neighbouring countries. My authorities urge Zimbabwe to act responsibly to forestall such a crisis. Strong political endorsement from the highest level is imperative if there is to be any chance of turning the situation around, and I hope that the opportunity which the new economic team embodies will be seized.

Mr. Josz made the following statement:

Zimbabwe's economic performance has steadily deteriorated since the government abandoned the stabilization and market reform policies being supported by the international community, sent soldiers to the Democratic Republic of Congo, and sped up its arbitrary confiscation and redistribution of land. Mr. Rustomjee reminds us in his excellent buff statement that Zimbabwe possesses abundant natural resources, a highly educated workforce, a well developed infrastructure, and fast growing productivity. But the pursuit of imprudent policies has led Zimbabwe to the brink of economic and financial destruction and has made it third on the Economist's list of riskiest investment destinations worldwide.

This self-inflicted disaster is now compounded by a sharp deterioration of Zimbabwe's terms of trade, due to the rise in oil prices and a high and growing incidence of HIV/AIDS.

To halt and reverse this downward spiral, Zimbabwe's authorities must renew their pursuit of macroeconomic stability and sustainable growth, and regain their respect for the rule of law. Reducing public spending will be the key to macroeconomic stability. The government wage bill, much higher than that of comparable countries, is a primary target for spending restraint. Zimbabwe's defense expenditures of 5 percent of GDP are more than double the average for Africa as a whole in 1998 (October 1999 WEO). Cutting unproductive public expenditures would free enough resources to both slow the swelling budget deficit and increase spending for health care, education and infrastructure. And based on their recurrent losses during the 1990s, privatizing loss-making public enterprises would cut a further 3 percent of GDP from the budget deficit each year. The 2001 budget is a step in the right direction but is much less ambitious than the staff would llike. It grossly underfunds the land resettlement program.

Last August's currency devaluation and the crawling peg adopted then have not succeeded in restoring Zimbabwe's external competitiveness of the economy, as shown by the scarcity of foreign exchange, the 25 to 30 percent spread between the official and parallel exchange rates, and the staff's own calculations. Could the staff comment on the authorities' puzzlement, reported in Mr. Rustomjee's buff, that exports have not responded to the recent devaluation? Given the anxieties and uncertainties created by the violent land expropriations of the past year, we do not wonder that exports have not yet responded to the currency devaluation.

The staff's recommendations provide the framework of an adjustment program that the authorities must urgently implement. But before we can support such a program with additional technical assistance and new Fund resources, we need strong assurances that its ownership goes beyond Mr. Rustomjee, who demonstrates his commitment to it in his excellent buff statement. The Fund-supported programs of 1998 and 1999 went off track almost immediately because they were instantly rejected by the President. Approving the use of Fund resources for programs that are not endorsed by a country's highest authorities is a mistake that this Board should not make again. For Zimbabwe, a successful Staff Monitored Program following the restoration of the rule of law and the clearance of external arrears should be a prerequisite for a new Stand-By Arrangement with the Fund.

Ms. Brukoff made the following statement:

The staff report tells a grim story of an economy in imminent danger of collapse. While exogenous shocks have figured in this deterioration, the authorities have been the authors of this crisis to a significant degree, particularly given the continued absence of commitment to a comprehensive economic reform strategy at the highest levels. We agree with the staff analysis that current policies run the risk of bringing about total economic collapse, hyperinflation, implosion in the financial sector, as well as damage to the regional economy. The authorities' willingness to publish this candid and negative assessment is a welcome step, and we hope it will promote public understanding and support for the very difficult policies needed to improve the situation.

Interest payments on government debt alone are expected to be nearly 17 percent of GDP, putting the authorities in danger of finding themselves in a debtor's trap, where interest payments consume such a large share of fiscal expenditures that the government must accumulate new debt in order to make debt service payments. Clearly, great damage is being done to the economy by continuing to borrow as opposed to tightening fiscal policy. Plans for progressive fiscal consolidation are encouraging, but implementation will be the key here.

We recognize the authorities recent steps to improve expenditure management and control through the introduction of cash budgeting and extension of the computerized Public Finance Management System. This effort to improve control, oversight, and transparency of public finances is the first key step toward addressing Zimbabwe's structural fiscal problems, and it remains to be seen how well it will be implemented.

The second key to improving public finances is making the right choices about how to spend scarce resources. Although military expenditures are slated to decrease, they will still be close to 10 percent that we are aware of, as there has still been no full accounting of the costs incurred by Zimbabwe's involvement in DRC. Spending on health is slated to rise but will still be less than 7 percent of expenditures. The authorities should continue the process of re-aligning expenditure priorities to reflect Zimbabwe's critical social needs, especially in connection with the HIV/AIDS crisis, where the social statistics are truly alarming, and where a firm government commitment to fight the spread of the disease is Zimbabwe's only hope to reduce poverty.

On monetary policy, I associate myself with those Directors calling for a tightening of the monetary stance to rein in inflation, and on exchange rate policy, with those supporting a flexible, market-determined exchange rate.

We cannot state in strong enough terms our concern over the authorities' current fast-track land resettlement program. Official plans to divide the commercial farms into single-family plots provide no clear indication whether the current residents on the commercial farms would receive the land or whether the land would be given to other families. This raises the real possibility that as many people will be displaced as resettled. There are also no clear plans for maintaining viability of the resettled farms (e.g., agricultural extension services) or to help those who would lose their jobs and their homes. While we appreciate Mr. Rustomjee's discussion of the acute difficulties posed by land reform, it would seem that the approach in Zimbabwe would have to be regarded as an example of how not to tackle this challenging issue. This institution and its membership cannot support a program that is inimical to redistributing land in an orderly manner and that does not attempt to minimize either displacement of the current commercial farm workers who depend on the commercial farms for their homes and their income or disruption to a key sector of the country's economy.

The authorities will have to move immediately to take the measures needed to reduce fiscal spending, tighten monetary policy, loosen capital controls, and introduce an orderly plan of land reform that minimizes the negative impact not only to current land-owners but to the commercial farm workers and to the economy as a whole. Finally, a serious commitment and strategic plan to stop the spread of HIV/AIDS is needed urgently. Without taking these steps expeditiously, Zimbabwe runs the risk of social collapse and severe civil disorder.

Mr. Fidjestol made the following statement:

The well written staff report clearly shows the dramatic deterioration in Zimbabwe's economic performance in recent years. This weak economic performance is largely due to inappropriate domestic policies. The weak performance is also illustrated by the failure of the Stand-By Programs of 1998 and 1999.

Since I share the assessment of the staff, and can broadly associate myself with the views expressed by Mr. Collins and other previous speakers, I can be brief and concentrate on four major points.

First, in order to rectify the situation, very strong measures are necessary on several fronts. Additionally, a very strong commitment from the authorities to implement the measures and to build domestic consensus supporting the measures is paramount.

Second, fiscal consolidation on the expenditure side in order to roll back the massive increase in the deficit is necessary. In particular military expenditures have to be reduced. In addition, the government wage bill in terms of GDP, which by far exceeds that of other sub-Saharan African countries, must be reduced sharply. These reductions are also needed to provide room for necessary social expenditure. The proposed budget for 2001 implies considerable progress on the fiscal front. However, serious doubts remain concerning the authorities' ability and commitment to implement the necessary measures.

Third, I agree with staff that monetary authorities need to tighten liquidity and move toward greater exchange rate flexibility.

Finally, but by no means least importantly, restoring the rule of law will be of critical importance. More generally, improved governance will be a necessary ingredient in any program to restore the Zimbabwean economy.

The staff representative from the African Department made the following statement:

Evidence suggests that there is some lagged export response to devaluation, and staff plan to deepen their study in the next several months. However, the devaluation has not had a major supply response, because of supply bottlenecks. There is nearly no fuel in the country, scarcities of key imported inputs exist, in addition to a wholesale disruption in the farming sector, which is the mainstay of export activity, as well as a tourism sector where bookings are sharply down. While staff do not subscribe to a view of pessimism, there is room for improving competitiveness. The current rate is still overvalued.

In terms of comparing staff's proposal in its normative projections and the authorities numbers, the primary balance that staff had recommended at the time is similar to the authorities' version now. The authorities target is marginally higher than staff's proposal. A major difference is that the authorities are now, several months after our discussions in Harare, assuming little foreign financing and few grants. Consequently, a larger domestic borrowing requirement exists, which drives up the interest bill. That is why the authorities came up with an overall higher budget deficit. Staff broadly sympathize with what the authorities are trying to achieve in terms of the primary balance. The issues are, as staff indicate in the supplement paper, the uncertainties attached to the government's wage bill, where the government has mentioned a cap of about 12 percent of GDP.

On the status of the DRC, today's wire services note a limited step in terms of the parties in the Congo conflict on agreeing to move troops by 15 kilometers away from front lines.

Uncertainties exist also in terms of the privatization proceeds. The authorities are using optimistic assumptions in their projections. They are counting on the divestiture of a promising mobile phone company which, is a subsidiary of the post office, and could earn upwards of $320 million. If the authorities can secure that amount, that would be helpful in alleviating the need for expensive domestic borrowing. Whether any major international investor or consortium of investors will be interested in such a large acquisition at the time of uncertainties in Zimbabwe remains to be seen. The other privatization proceeds are miscellaneous government holdings in companies that have already been partially privatized. However, the privatization list of companies has remained the same for about two years, and therefore it is a question of willingness now. At the end of the day, staff tend to look at 2000 as an outlier. Looking at 1998, with a budget deficit of about 4 1/2 percent of GDP, in 1999 of about 11 1/2 percent of GDP, it is 2000 that is the outlier, primarily because of the unsustainable wage increase that was granted and, to some extent, because of the intensification of the conflict in the DRC. I am not dismissing the political difficulties that the government will have in curtailing expenditures, but the issue is what alternatives exist. If no foreign financing is available, the alternative is hyperinflation. The choice is between an orderly adjustment, politically and socially agreed ex ante, or a forced adjustment ex post that comes through hyperinflation. At the same time, as staff stressed in the paper, the process hinges on securing a broad and strong political consensus with civil society about the need to reduce the wage outlays, and on leaving the DRC as soon as possible.

On the composition of social and military expenditures, the first caveat is the deficient quality of fiscal statistics in Zimbabwe. Particularly, the question of the functional distribution of spending is an area where the authorities need to carry out considerable work. As many of the social ministries have large wage bills, especially the health and education ministries, that means that a drift exists when giving large and unsustainable wage increases, as was the case this year. But, that does not mean that the delivery of social services or quality of social services is rising. Teachers and health professionals, received a windfall which, to some extent, will be reduced next year. Staff have been trying to work with the authorities and encouraging them to have a finer breakdown of social spending and to look at the wage and nonwage component. However, that element requires caution when analyzing the trends in social spending, as the wage component of the social ministries is high.

Mr. Rustomjee made the following further statement:

On the issue of land reform, it is accurate that the issue needs to be addressed if there is to be a sustainable exit from the decline that we have seen in growth and confidence in the economy. The issue of land reform is a hangover from the pre-independence era and a source of frustration from every quarter, from those that are affected who are landowners, to those who are not land owners, e.g. donors and interested stakeholders. The UNDP is serving as facilitator in the process of trying to achieve some accommodation among all the stakeholders on the land reform issue. The UNDP fielded a mission recently, and last week the administrator of the UNDP visited Zimbabwe to meet all the stakeholders and came back with a statement on how he saw a way forward with the land reform issue. I want to summarize some of the comments that were made by the administrator, who is understood by all parties to be impartial in trying to facilitate this process.

This is an emotive issue, at least 25 years old and was the source of the liberation war and an issue that was not addressed once political settlement was reached. The first comment made is that a consensus exists in all quarters that land reform in Zimbabwe is a pressing social and economic priority for the government, the people of Zimbabwe, for the sovereign African region, and also for the wider international community. The administrator said that this is not an issue that should simply be left to resolve itself in Zimbabwe. The wider international community needs to have active involvement.

The second issue raised was that a series of constructive proposals were put forward as part of the report, which was released last week. The first was the recognition that, to move forward with land reform, there needs to be enhanced capacity building within the line ministries that are involved in this process. That is a recognition of the fact that, even if the political will existed, support is going to be needed on the ground, in the government departments, in trying to make this process move forward. It is not clear where the resources will come from. Some will come from the 2001 budget; there is a line item allocation in the budget of about $25 million. But, it is clear that more financial resources will be needed in the line departments.

The second point that the administrator reported was that it was clear that concerns with the issues of law and order in rural areas are of the utmost importance to donors, and need to be addressed in order to secure donor support.

The third point that was raised by the facilitator was that a need existed for a trust fund to be established to finance infrastructure and services for three categories of people: the landowners who may be displaced in this process, the new settlers, and the farm workers who are already on the land. A consensus was reached by all parties, including the government, that the finance to provide the infrastructure for this land reform needs to be put in place.

The UNDP administrator also noted that the land reform program will need to take place in a sequenced way in order not to overwhelm Zimbabwe's implementation capacity. I raise this particular aspect because, if we see movement forward on land reform, it will be important to recognize that this is going to be a long-term process; and will not happen in one year or 18 months. It is going to take a long time to address and to finance properly.

The final point that was raised by the administrator was a recognition of the anger and frustration of the government on the time it has taken for land reform to occur in Zimbabwe. Looking back, one can apportion the blame to many different quarters, however the issue is to look forward. If we are going to move forward on land reform in Zimbabwe, it is going to take political will, donor participation, considerable resources, and a long- term commitment to finance and technical assistance. It is important to recognize that it is going to be a long-term process. I appeal to colleagues in the donor community to consider the outcome of the UNDP report. It contains all the ingredients of a successful move forward on this issue, and makes a clear case that, if there is to be a move forward, one key element is going to be sizable financial resources and technical resources commitment.

Zimbabwe is in arrears to the World Bank, of approximately $50 million. However, recently $20 million has been repaid, and the Minister has said that every effort is being made to clear these arrears by year end. To the World Bank representative, I communicate the request of the authorities that the resources be released as soon as the arrears are cleared, to help efforts to provide social protection, particularly to avert the collapse in the health system, to provide resources for HIV/AIDS, and specifically to provide resources for the large and growing number of orphans in Zimbabwe as a consequence of AIDS.

Technical assistance to Zimbabwe is crucial. This is not a country that takes technical assistance and does not use it. There is a balanced picture, even if some technical assistance has not been effectively used, but the table at the end of the staff report indicates that, where technical assistance has been provided, a reasonable amount of that has been used.

Zimbabwe has tremendous potential. It is demonstrating a determination to establish policy credibility. The new economic team is serious. They will generate some positive surprises with the budget, which in Zimbabwe's circumstances is a tough budget that has been presented.

On the issue of the DRC, I share the staff's comment that the precise position is not clear. However, a meeting took place in Harare during the last few days, where a large number of participants in the war signed, at the level of the Defense Ministers, an agreement to cease hostilities and to withdraw, but I do not know how accurate that report is.

Mr. Charleton noted that the UNDP report and the idea of a trust fund was constructive, however, President Mugabe's recent speech included phrases such as "I urge farmers to drop this nonsense of land issue in courts. That will make us even more angry. If this nonsense continues, if farmers cannot be harmonious, then we will take more farms. If they are prepared I ask them to leave the country harmoniously. They are not bosses among us." That was not a response that encouraged donors to help Zimbabwe.

Mr. Rustomjee replied that land reform was the most emotive issue in Zimbabwe, and went to the heart of productivity and stability of the economy, and the President took a particular view of that issue. However, the UNDP report embedded institutional proposals which, if put in place, could shift away from the emotive to a substantive progress, e.g. the trust fund, and technical assistance to line ministries. Part of the ingredients was to try to buttress progress with strong institutional mechanisms, and to try to move forward, because that was a way out of the intractable situation. In South Africa, for example, on the apartheid system, positions were diametrically opposed that it became impossible to imagine how to reconcile them. The way forward was to ring fence an issue, and find areas of commonality, where progress could be built slowly, steadily, and institutionally, away from the emotiveness.

Mr. Liu made the following statement:

First of all, I would like to thank staff for their well-prepared paper and Mr. Rustomjee for his insightful buff.

Recent data show that Zimbabwe faces a difficult and complex set of economic, and social challenges. Continued weaknesses in macroeconomic policies, especially in the fiscal area, combined with governance problems and the political turmoil, have undermined investor confidence and curtailed international assistance. However, as Mr. Rustomjee mentions in his helpful statement, the authorities recognize the difficulties facing the economy and the urgency with which they have to act. It is very important that the authorities obtain the necessary consensus in designing a package of policy measures. We are happy to note that the authorities are determined to overcome these challenges to achieve Zimbabwe's true growth potential. Given the natural resources, a highly educated labor force, well developed infrastructure, the progress with economic reforms, especially the authorities' firm commitment to pursue their reform agenda in the Budget, together with assistance from the international community, I am confident that Zimbabwe could regain its rightful status as an anchor of stability and prosperity in southern Africa .

Since we are in broad agreement with staff and other speakers on various issues, I will make a few comments for emphasis.

First, on fiscal policy, we are pleased to note that the new budget targets a drastic reduction in the public sector wage bill and military expenditures. We endorse staff's recommendation for broadening the tax base, and eliminating preferential tax regimes, exemptions, and loopholes. We also welcome the authorities shift in budgetary expenditure towards poverty alleviation and infrastructure development. They are encouraged to continue their efforts to accelerate the privatization process in 2001. We are happy to note that Parliament has strengthened its supervisory role in the management of public resources and has formed the Budget and Portfolio Committee.

Second, on monetary policy and banking supervision, we welcome tightening the monetary policy stance to bring inflation under control. It is encouraging to note the central bank's strengthened role in overseeing the financial sector—capital adequacy ratios for the banking system are being enforced and measures are being taken to reduce non-performing loans. As for exchange reform, we join Mr. Kelkar in sympathizing with the authorities' stand that, given the current prevailing situation, the appropriate course of action at this stage is to reduce the fiscal deficit, bring down inflation, and restore investor confidence in the Zimbabwean economy.

With these remarks, we agree that the next Article IV consultation be held on the standard 12-month cycle, and we wish the authorities every success in the future.

Mr. Charleton made the following statement:

First, I endorse Mr. Collins's comments on the quality and frankness of this report. I can endorse all of Mr. Collins's comments.

Let me thank staff for a well-written and frank assessment of the situation in Zimbabwe. I also wish to thank Mr. Rustomjee for his very helpful preliminary statement.

When one compares the tremendous efforts made by many very poor African countries to persevere with reform in the face of overwhelming problems with the performance of Zimbabwe, it is extremely disappointing. In referring to Zimbabwe, staff use the phrase—its rightful status as an anchor of stability and prosperity in Southern Africa. This certainly was true but I fear that, without a fundamental change of attitude, the prospects of it being regained are fast diminishing.

Some things are being done and the level of awareness of the challenge is increasing but I do not sense the required sea-change in attitude. At this stage, reform is still more aspirational than practical.

I would not often start a statement with a comment on statistics but paragraph 26 makes it clear that official statistics are so non-transparent and inconsistent that one wonders how staff can adequately conduct surveillance. More importantly how can the authorities frame a coherent economic policy? My fear is that the actual economic and social situation is worse than we can see.

One of the major problems facing Zimbabwe is that it has frittered away its credibility in the international community and seems perfectly capable of continuing to do so. Those who are both willing and able to help have lost faith and the onus is on Zimbabwe to rebuild it. Perhaps since the June 2000 elections, the quality of the dialogue has improved but there is certainly a long way to go. Fundamental issues such as the rule of law are still very worrying and this goes beyond the tactics being used in the land redistribution issue—it includes aspects such as the treatment of opposition voices in general and the promotion/tolerance of violence.

On the land issue itself, it is disappointing that 20 years after independence this colonial legacy has not been resolved. It may well be that land redistribution is the key to a stable and prosperous rural economy and society but it is far from clear that the government's approach will ensure a favorable outcome. Is there any element of transparency in the redistribution process and what criteria are being used? Even in favorable circumstances, there must be a distinct danger that the initial impact of redistribution will be a loss of commercial farm output and exports in the early years.

It is difficult to describe Zimbabwe as having a fiscal policy in 2000. A initial planned budget deficit of 3.8 percent of GDP deteriorated into an outturn of 23 percent. This is total abdication of fiscal responsibility. Even though the authorities seem receptive to the need for fiscal consolidation, their ability to regain control is doubtful. The required cuts in civil service numbers and wages and in essential services seem unattainable. As Mr. Rustomjee notes, 81 percent of expenditure is non-discretionary—this makes effective retrenchment very difficult. This is also an economy which is already overtaxed. Even if some modest progress could be made in 2001, what are the prospects for further consolidation with a presidential election in 2002?

On the fiscal side, it would appear that privatization is looked upon as a potential revenue source. But para. 6 estimates the net worth of the 9 major parastatals at -2 percent of GDP.

There at least seems to be a realistic hope that the war in the DRC is drawing to a close. The resources wasted by Zimbabwe in this war—in the face of pressing domestic needs—is incomprehensible to me. A previous Zimbabwean Finance Minister assured me that the war was not costing Zimbabwe anything.

One can have great sympathy with the central bank of Zimbabwe. Faced with an abdication of fiscal policy, it has somehow managed. It is to their credit that positive real interest rates have been maintained. The exchange rate peg was clearly unsustainable and a float is necessary but, of course, a float is not a substitute for sound macro policies.

The poor output response to the exchange rate depreciation is a worry. General terms of trade losses are part of the problem but my concern would be that the general environment for economic activity has deteriorated to the extent of seriously impairing the supply capacity. The country had a fine industrial sector and infrastructure but the chronic foreign exchange shortage, deteriorating electricity supply, etc. are serious impediments to output.

At the end of the day, we can only offer advice to members: it is entirely their prerogative to follow it or disregard it. Zimbabwe, however, cannot expect the support of the international community until it takes convincing steps to halt the deterioration. Staff still see the possibility of relatively quick recovery if the situation is addressed forthwith: let's hope they are right.

Mr. Sakr made the following statement:

Since the economic reform program of 1991, Zimbabwe's economic performance has been weakening at a pace which has been accelerating. This weak performance was mainly owing to large fiscal imbalances and a decline in investor confidence which is fuelled in part by political uncertainties. More recently, the situation deteriorated further due to a sharp increase in the fiscal deficit and worsening security situation. Low commodity prices and reduced access to foreign financing added to the country's economic woes.

Zimbabwe is clearly in the middle of an economic crisis with usable official reserves remaining negligible, external arrears accumulating, inflation escalating, and GDP contracting. To address this difficult situation, the authorities need to urgently tighten fiscal policy and rebuild confidence by accelerating structural reforms and improving security and law enforcement. Our comments will therefore focus on these priorities as well as on the exchange rate regime.

The fiscal deficit for 2000 is projected at some 23 percent of GDP, compared to a target of 3.8 percent. This sharp deviation was mainly due to large overruns in non-priority expenditures, including the wage bill which is extremely large as a result of the sharp wage increase granted before the elections. This unsustainable situation is not only raising the risk of a total financial collapse, but is also contributing to the decline in economic activity through the excessive burden on monetary policy and the upward pressure on the real exchange rate. These unfavorable developments contain the ingredients of a potential financial collapse, which would be unfortunate in a country that has the potential to be an anchor of stability in this part of the world.

The Staff's recommendation of targeting a primary fiscal surplus in 2001 is well placed. To achieve this target, it is essential to limit nominal wage increases and to strengthen expenditure control. It is also important to increase revenue by improving tax administration, broadening the tax base, and raising user fees and utility tariffs.

In response to intensified pressures in the foreign exchange market the authorities' allowed a devaluation in the exchange rate. While staff recommend a move to a floating exchange rate regime, they seem to accept the retention of the crawling peg regime as long as the gap with the parallel market is narrowed. We have sympathy for this last option in view of the current economic instability, political tension, and the need to reign in expansionary financial policies. However, the crawling peg regime would benefit from timely adjustments of the parity and a widening of the band around it. Here, it should be noted that unless financial policies are brought under control and the banking sector problems are forcefully addressed, no exchange regime can be successful.

On structural reforms, the authorities are to be commended for the progress achieved in simplifying the import tariff structure and reducing the average tariff rate, as well as the establishment of a competition commission and a privatization agency. Progress in other structural reforms is also needed to improve growth prospects and regain confidence. Immediate priorities include liberalizing remaining price controls, reforming or liquidating loss-making parastatals, and finalizing the guidelines on dealing with troubled banks. Furthermore, while it is important to make progress in land reform in order to address the serious inequality in land ownership and to ease political tension, it is crucial to conduct this process in a way that ensures full respect of law in order to minimize uncertainty and reduce the negative effect on investor confidence and Zimbabwe's image abroad.

Finally, we encourage the authorities to urgently and decisively move forward on these fronts in order to pave the way for negotiations on a Fund-supported program.

Mr. Schlitzer made the following statement:

The staff report is very balanced and provides a candid assessment of Zimbabwe's difficult economic situation. It is very regrettable to see that the economic outlook remains so dismal, and that the economic crisis has deepened during 2000. This involves human suffering on a large scale. Also, the negative repercussions on the neighboring economies are not negligible. On top of all this, there is the AIDS epidemic, which besides the immediate loss of human lives leads to further hampering of economic growth prospects.

The urgency of the situation requires immediate and thorough action to avoid that economic diseases become chronic. As recalled by Mr. Rustomjee, the country's productive potential is significant, due to its high stock of human capital and natural resources. These are assets that Zimbabwe cannot afford to waste. It is therefore imperative to restore confidence in the economy and to do so as soon as possible.

To this aim, it is quite clear that implementing the right economic policies is necessary, but not sufficient. If the rule of law is established, if human rights are observed, if governance problems are resolved, and if the land reform is carried out according to the principles agreed upon with donors and stakeholders in 1998, only then can the confidence of the international community resume. In this context it is not reassuring to hear that the land reform is being treated so inconsistently by the authorities and that farm invasions have continued. As recognized by Mr. Rustomjee as well, land reform is key to enhance Zimbabwe's long-term growth potential.

We are encouraged by the new economic team that was appointed in July, which is to be praised for implementing some badly needed measures and for increasing transparency with civil society, especially on defense outlays. We also very much welcome the authorities' decision to publish the staff report, which is an important piece of evidence of the more transparent approach that the new economic team intends to pursue. The RBZ has also been very skillful, considering that it has to operate in a very adverse monetary environment and a difficult exchange rate situation. We also welcome the measures to strengthen banking supervision. But these actions are bound to prove largely insufficient as well as ineffective to reverse the situation unless a comprehensive radical change in policies is embraced at the highest level of government.

Let me mention three areas that appear especially problematic due to the lack of a comprehensive adjustment framework.

First, on exchange rate policy, even after the allowed devaluation, the currency remains overvalued to a large extent. Hence, either the current exchange rate level must be supported by appropriate macroeconomic policies, which is clearly not the case for now, or it is better to go for a float.

Second, on fiscal policy, the budget law that is now in Parliament is encouraging. The correction, at least "on paper," is significant. But how likely is it that the government will succeed in containing wage increases to only a tenth of those called for by government employees? Is it realistic to believe in military spending cuts and the withdrawal of troops from the Democratic Republic of Congo in early 2001?

Third, in the monetary area, the action of the RBZ is clearly hampered by the rising government's borrowing requirement. The staff calls for a tightening of monetary policy until inflation is brought under control. However, in a situation in which there is no coordination with fiscal policy, to what extent would monetary tightening be possible without fully crowding out the private sector?

There are obviously a number of other areas where there is also need for intervention –taxation, trade and exchange rate restrictions, financial sector stability—but I cited these three examples to prove the need for an adjustment and reform program that is at the same time comprehensive and owned at the highest level. Staff has outlined clearly what the main elements of such a package should be, which I do not need to repeat here.

While the international community has certainly an important role to play in helping Zimbabwe in such difficult circumstances, it should be clear that the Zimbabwean authorities have most of the responsibility for accomplishing this task. I would like to conclude by wishing them all the best and by encouraging them to work as close as possible with the staffs of the Fund and the World Bank in this very challenging endeavor.

Ms. Bonomo made the following statement:

I agree with much what has been said today and with the thrust of staff's appraisal. I would just like to make some points for emphasis. It was mismanagement that has brought about the severe economic crisis with continued GDP contraction and high inflation. While the way out of these difficulties is far from easy, staff has outlined the course to be taken in its paper. It will be crucial to have fiscal consolidation, prudent wage and monetary policy, land reform in a fair and transparent manner with restored rule of law and improved governance.

While the new economic team has undertaken some positive steps, they are far from sufficient. On the proposed budget, while it is a step in the right direction, it is now important that the targeted limit of wage increases as well as the reduction in defense outlays can actually be achieved. Moreover, the budget depends also on an ambitious acceleration of the privatization program, which we, of course, support.

Furthermore, like Mr. Josz (Belgium), I believe that strong assurances are needed before a program could be supported. That means that substantial prior actions would need to be implemented, particularly in the area of fiscal discipline, but also with respect to greater transparency in fiscal reporting, to governance in general, to foreign exchange rate adjustment and to an agreement on a land reform program that could garner domestic and international support.

In addition, it would, of course, be very important that a broad political consensus can be mustered. After two SBAs that went off-track before the first review, I think that we should only approve a new program if the LOI is signed by the president, because otherwise there is a lack of commitment, especially in light of the presidential elections in 2002.

Finally, I wonder whether the provision of the Fund's technical assistance should not also depend on comprehensive progress with policy implementation. If the overall picture remains so bad, I doubt that another technical assistance mission would be of much use, particularly given that the advice from the last MAE missions have only been partly implemented. Staff comments on this issue would be welcome.

To conclude, I welcome the publication of the staff report and wish the new economic team success with their challenging task.

Mr. von Kleist made the following statement:

At the outset, I commend the staff for a well written and candid report. Since I generally concur with the gist of other speakers' comments, I shall keep my own comments to the minimum.

Zimbabwe's economy is currently in a bad shape, and I cannot join those who optimistically assume that it will soon take a turn for the better. Fiscal profligacy, with defense and wage expenditures spiraling out of control, is one side of the coin of what has been going wrong in Zimbabwe. I share the staff comments and advice. The other side of the coin, as other speakers have mentioned, is the blatant disregard for the rule of law, especially in connection with the so-called "land reform." I use this expression in inverted commas since the current situation has little in common with what was agreed in the international conference on land reform in September 1998.

Disregard for the rule of law will harrow Zimbabwe for many years to come, since it is much easier to break down institutions than to rebuild them. The fallout from this political crisis shapes the current economic picture in Zimbabwe on three fronts: 1) domestic and foreign investor confidence has been severely shaken, curtailing the access to foreign financing and resulting in pressures on the foreign exchange market; 2) agricultural output, especially of exportable cash crops, has declined, further straining the balance of payments situation; and 3) from a wider perspective, developments in Zimbabwe have had a negative impact on the whole region, hampering economic recovery in all of southern Africa, reducing trade flows, and steering investors away to other regions. The staff rightly emphasized this in the document, and points to Zimbabwe's wider responsibility toward its neighbors.

Mr. Chairman, when I compare the assessment of the staff with that of Mr. Rustomjee in his buff, I was struck by the difference concerning the future impact of the so-called land reform. Mr. Rustomjee expects that land reform will enhance Zimbabwe's long-term growth potential and improve the productive capacity of labor and capital in agriculture, thereby increasing employment, stabilizing the rural economy, and reducing poverty. Staff, on the other hand, expects the land reform to result in sizable losses in output, employment and export earnings, not only in the agricultural sector but also in the rest of the economy, and a rise in relative foodstuff prices. If I had to place a bet, I would put my money on the staff.

Please excuse my choice, Mr. Rustomjee; I know that you are in a difficult situation yourself. However, I also cannot share your optimism concerning the UNDP report. It is truly the least common denominator to agree that someone else has to put up money to solve an issue of property ownership, especially in a country where reports connecting Cabinet members to corruption charges are widespread.

Mr. Vogel made the following statement:

The economic situation of Zimbabwe is not satisfactory, presenting severe imbalances in the fiscal accounts, and an extremely illiquid foreign position. Zimbabwe's economy is in a deep recession, that reflects lack of confidence. However, we welcome the initial measures developed by the new economic team, and, for example, we value that Mr. Rustomjee stated in his helpful buff about the progress towards the liberalization of trade, even though, as reported by staff, Zimbabwe's trade regime continues to be quite restrictive.

We agree with the staff assessment on the condition presented by this economy and their recommendations on the need of prudent macroeconomic policies, more efficient channeling of public expenses (there are some costs associated with military expenditure), improvement in the structure of the debt, acceleration of the privatization program, and a improvement in the property rights (viable land reform would be vital in the future). Also, and fundamentally, we agree with Mr. Kelkar and staff on the need for developing a broad political consensus for designing and implementing a stabilization policy package.

Finally, we wish the Zimbabwe's authorities success in their future challenges.

Mr. Mirakhor made the following statement:

I join other Directors in their appreciation of the staff report, and thank Mr. Rustomjee for his lucid and sobering statements. At this point of discussion, I do not have technical points to add. And, even if I had, I would not want to reveal it at this time because I feel that we are in an unrealistic, bizarre world when we talk about marginal technical points for a country where something like 20 percent of the population over 15 years of age would die of AIDS within the next ten years, or where there are about 600,000 orphans, or it is estimated that 60,000 children may have lost one parent. To discuss monetary or fiscal policy under such circumstances appears somewhat out of place.

After having listened to others and having read the staff report, I think that the authorities are taking a very courageous step in publishing their Article IV consultation, and it should not be taken lightly. We have just been through one of my constituencies where the staff report was not that positive, and yet the authorities had the courage to agree to its publication. In this case, as Ms. Brukoff indicated, this is a very negative staff report. So, why would the authorities agree to publish a very negative staff report when they do not have to? Of course, it could be interpreted, as some colleagues have indicated, as a sign of transparency or a signal of the intention of the authorities. But I believe that the decision to publish Article IV consultation reports should be considered as a downpayment on ownership and commitment.

I think if I were a minister who knew that he had some support from a higher authority and I wanted to move forward, I would want to emphasize that I am taking a big chance with this highly negative report, and that I am doing it to demonstrate ownership and commitment. I do not think that one needs to know rational expectation theory to know what would happen, nor does one need to talk about public choice to know that, once this staff report is published, there would be some negative feedback. So, why would you want to do it? Basically, because you want to note that you expect improvements and that here is the baseline against which you will try to do better. So, I would take it as a sign of ownership and a commitment to do better. I also strongly support Mr. Rustomjee's call for encouragement and nurturing of this new economic team. Frankly, this is a very positive opening we have with Zimbabwe, and we ought to try to engage the authorities in a very constructive dialogue.

The magnitude of human suffering is enormous in Zimbabwe; let us exploit all positive opportunities to move forward. I endorse Mr. Rustomjee's call for keeping a positive attitude toward Zimbabwe at this stage.

Mr. Alosaimi made the following statement:

Zimbabwe's worsening economic situation underscores the need for strong and sustained policy correction. Real GDP is falling, inflation is accelerating, and the fiscal and external positions are deteriorating. The unsettled domestic situation is further aggravating the daunting challenges facing the economy. These developments are, as staff rightly notes, a serious concern not only for Zimbabwe but also for neighboring countries. In this connection, the measures taken by the new economic team are a first step that needs to be broadened and strengthened within the context of a comprehensive economic reform plan. Delays in formulating and implementing such a plan will further increase the costs of adjustment.

As I am in broad agreement with the staff appraisal, I will only make a few brief comments.

In the fiscal area, improving revenue collection and tax administration remains a priority. Without a measurable improvement in these areas, efforts to raise revenue by increasing taxes will likely be frustrated. On the expenditure side, it is clear that curtailing wage outlays is critical. Indeed, there is room to reduce these outlays given the substantial rise in real wages over the past year. In this regard, the budget bill, if fully implemented, will be a major step forward,

Turning to monetary and exchange rate policies, the measures taken by the Reserve Bank of Zimbabwe to devalue the currency and move to a crawling peg are useful first steps in improving competitiveness. Staff argues that despite this depreciation, the currency remains substantially overvalued and encourages the authorities to move to a floating regime or accelerate the adjustment in the crawling peg. Success of this strategy will depend in large part on tightening monetary policy in order to contain inflationary pressures. In this connection, I am encouraged by Mr. Rustomjee's assurances that monetary policy will remain sufficiently tight until inflationis brought under control.

Tightening macroeconomic policies needs to be completed by ambitious structural reform and increased efforts to regain investors' confidence. In this regard, while recognizing the difficulties facing the authorities as pointed out by Mr. Rustomjee, I agree wth other speakers that implementing land reform in an orderly fashion and in compliance with the law is a priority. Completing the reforms detailed in Box 1, especially those related to strengthening the banking sector and reforming the civil service is also critical. Furthermore, I agree with staff that a "well-designed program of public asset sales" would improve the fiscal position and enhance the role of the private sector. Here, could staff elaborate on investors' demand for public enterprises given the weak financial situation of these companies and the unsettled domestic situation.

With these remarks, I wish the authorities success in meeting the very difficult challenges ahead.

On publishing the staff report and deleting market sensitive information, Mr. Rustomjee explained that the authorities would like to take the references regarding external reserves in paragraph 6 of the supplementary paper out.

The staff representative from the African Department made the following further statement:

Firs on technical assistance, I endorse the position taken by Mr. Rustomjee, and also by Mr. Mirakhor. We owe it to the new economic team which is trying hard to strengthen their hands in terms of the capacity to change matters and to deliver results. The Fund is asking for much in terms of improved transparency and filling gaps in fiscal information. While the record is mixed, by and large the authorities have been receptive and there is a good payoff to investing in technical assistance. I propose that in conjunction with the authorities, and in anticipation of a visit by the Minister and some of his associates to Washington early next year, we try to identify the priorities for technical assistance, and talk to the functional departments about availability and the phasing.

On the DRC, the Reuters report states that Defense Chiefs from six African countries, as well as rebel groups fighting in the DRC signed an agreement today, to begin withdrawing troops from front line positions later this month. The agreement is expected to take effect December 15. All parties have agreed to cooperate in pulling their forces back at least 15 kilometers from the frontline.

On the sequencing of exchange rate policy, the authorities contend to first carry out fiscal consolidation and then take care of the exchange rate. Staff have discussed this issue and have noted to the authorities that we do not consider the exchange rate to be a panacea. However, it is an important component of a concerted and broad-based package of adjustment. Because, the price relativities are off-line, the market rate being 75 Zimbabwe dollars to the U.S. dollar, vis-à-vis an exchange rate of 55 Zimbabwe dollars to the U.S. dollar. Most glaringly, the virtual absence of fuel, the scarcity of imported inputs, and the decline in tourism, have to be supported by fiscal policies, by confidence, and by governance issues being addressed. Staff have no illusions that only addressing the exchange rate would be a meaningful response. However, in the virtuous cycle where the authorities receive the political support to address the issue of fiscal consolidation, the exchange rate is a central pillar.

On land reform issues, staff talked about the immediate effects, which will be extremely disruptive. For the medium and longer term, staff pointed out that there will be a change in the composition of output in the farm sector between subsistence agriculture and tradable crops. This is potentially a source of friction that has to be handled well. However, if the support system rises to the occasion, there is potential for an increase in farm output. Yet, I draw attention to the expensive price tag of this type of ambitious land reform. A revealing statistic is the fact that in the 20 years since independence only 3.3 million hectares have been resettled, and the goal originally was to settle an additional 5 million hectares in the second half of this year. The complexity and the amount of resources needed is daunting. Some estimates, including from the authorities, suggest that the price tag for the land reform would be about $500 to $800 million. For a country that has virtually no foreign exchange reserves, and a large fiscal deficit, this is an expensive proposition. Therefore, the debate has to be focused on the question of the phasing of the land reform. This is a crucial part of the debate, and the authorities realize that the phasing has to be carried out more gradual, that donors have to be brought on board to pay some of the costs, but also that the political leadership has a more ambitious agenda to resettle fast because of its political constituency. How to bring a meeting of the minds between those different constituencies is the crux of the problem.

On the prospects for privatization, the centerpiece of this proposal is the sale of the telecommunications company. The issue is whether due diligence and other steps associated with the process can be carried out quickly. However, for the last two or three years, the government has been talking about privatization of some of the smaller enterprises, and the results have been negligible. At the same time, the fiscal situation is stringent and the government appreciates that it has to do something to survive.

There is also a question of the portfolio demand of investors. When the government introduced the new monetary policy in August, rapidly bringing down the returns on financial instruments, and effectively capping the interest rates, there was euphoria in the stock market, because the investments in stocks appeared to be a relatively more attractive investment. Some institutional investors and households could consider buying shares in some of those companies. However, the other parastatals pose a challenge that the authorities have yet to address. The statistic that staff mentioned show a negative net worth of about 2 percent of GDP of the nine major parastatals and did not include the promising telecom company. The steel company and other large companies, however, have been a source of uncertainty for a long time. They are economically not feasible, and need to be restructured. They will not be privatized in the immediate future, although the authorities have been discussing this issue with the World Bank, and with the Fund for some years.

Mr. Rustomjee made the following concluding remarks:

On land reform my comments are not addressed at the short term, but at a medium-term framework rather than the long-term. In any land reform a promise should exist that at the end, the objectives of stabilizing an agrarian economy, hopefully shifting output away from agriculture into the manufacturing sector, should be striven for. This is a possibility in a more stabilized environment in Zimbabwe. Staff make a valuable point about phasing, about the time frame and about the costs of land reform. These are important considerations in the land reform process, which I will take back to my authorities.

On the UNDP report, the comment that, not to expect anyone to come and help is a short-term response. I urge the Board not to move in that direction. I have seen irreconcilable conflicts resolved by ring-fencing problems and trying to address them. That is what the UNDP mission is trying to do, and I strongly urge that colleagues look at those efforts, because those stakeholders have to buy into the relevant issues. It is important that in the process, part of the solution is the authorities coming to the table with the political commitment, and another big part of the solution is substantial additional resources.

I thank Directors for their detailed comments. As is always the case, I will reflect all of these in detail to the authorities. My authorities welcome the ongoing engagement of Fund staff with Zimbabwe. It may not be apparent, but it is bearing fruit, and is a vital element of the encouragement that is being given by the Fund to the new economic team. I hope that that will continue, and will be strengthened. I also hope that technical assistance can be escalated to Zimbabwe at this time.

The clear message came on tightened fiscal policy. Mr. Collins, captured that by saying it is the heart of what is needed in the short term. Clear comments on the tightening of monetary policy and on structural policy will also be forwarded to the authorities.

In a study of 29 African countries, the ILO reported, that in Zimbabwe's case, 29.4 percent of the population will die of HIV/AIDS by 2020. 20 percent in ten years is probably the number in the staff paper, but the ILO has taken a longer view. Mr. Charleton's comment that we are not sure about the exact nature of poverty and the depth of the depression in the Zimbabwe economy is valid. That applies to the HIV/AIDS issue as well.

I ask colleagues not to prejudge the new Minister and the new economic team and to hold your views in abeyance until you have seen the quality of the 2001 budget, which he hopes to have shepherded through parliament shortly.

I believe it will be an important signal of determination of the authorities to bring about elements of the changes that have been suggested by colleagues here.

On the issue of pace of recovery, even if major steps are taken adequately, recovery is going to take a long time. However, the recovery could be swift if the political will exists and if the requisite elements of reform are pursued. I ask colleagues to keep an open mind about this aspect as we move forward.

I welcome the comments that have been made on the publication of the staff report. It is not an easy decision, by the authorities, to publish a report almost all of which paints a difficult picture. I hope the gesture is taken in the spirit it was intended and I will communicate the comments that have been made by colleagues.

Mr. von Kleist said that the harshness of his comments were dictated by despair, that almost a third of the population was dying, while at the same time, the highest levels of government were pursuing policies that went in the wrong direction.

Mr. Rustomjee said that the meeting should not end on a note of despair. He had seen worse, and the situation would turn around, even if it took some time.

The Acting Chairman made the following summing up:

Executive Directors agreed with the thrust of the staff appraisal. They expressed deep concern about the decline in per capita income and the deterioration in social conditions of the past several years as a result of Zimbabwe's weak macroeconomic policies, the rapid spread of the HIV/AIDS pandemic, poor governance, and escalating tension and uncertainty related to the government's land reform program.

Directors stressed that the slump in economic performance in 1999-2000 was due mainly to the pursuit of an unsustainable fiscal policy driven by large wage and defense overruns, and by governance problems that have undermined investor confidence. Economic activity has contracted, inflation has accelerated, and the balance of payments position has weakened significantly, as evidenced by the depletion of usable foreign reserves and the emergence of external payment arrears. Directors also noted the worrisome fallout from Zimbabwe's problems on neighboring countries and they urged the authorities to be mindful of the repercussions on their neighbors when framing domestic policies.

Directors considered that Zimbabwe needs to take corrective measures urgently in order to forestall a deepening of the current economic crisis. Despite the severe deterioration in recent years, Directors noted that Zimbabwe has the potential to resume vigorous and sustained economic growth, provided the authorities implement a strong economic program with determination. They were encouraged by the new economic team's commitment to reform, and hoped that it would attract the national consensus and broad ownership necessary for success. Directors agreed that a restoration of macroeconomic stability—which is a prerequisite for recovery—would hinge on the design and implementation of a credible adjustment program, anchored by a return to a sustainable fiscal path and restoration of external competitiveness. Rebuilding investor confidence will require determined efforts to improve the economic environment, including by taking decisive steps to strengthen governance and ensure a speedy return to the rule of law, and by implementing an orderly and transparent land reform program that garners domestic and international support. Directors also urged the authorities to normalize relations with foreign creditors and eliminate external payment arrears.

Directors considered that the brunt of the fiscal adjustment will have to come from savings in wage and defense outlays. They welcomed the government's plan to curtail these outlays so as to reduce the fiscal deficit substantially, and to realign spending priorities, especially to make room for increased spending to address the HIV/AIDS problem. They underscored that the establishment of strong expenditure control mechanisms will be essential to underpin fiscal discipline, and endorsed the government's statement that fiscal consolidation must be further deepened during 2002-03.

Directors also observed that the 2001 budget bill features a number of tax cuts, and they encouraged the authorities to adopt offsetting measures to bolster tax revenue, particularly by broadening the tax base and improving tax administration. In this regard, they welcomed the imminent establishment of an autonomous revenue authority. Directors welcomed the decision to strengthen the position of the state oil and power companies through periodic adjustments in fuel and electricity tariffs. They also encouraged the authorities to take steps to improve the finances of the other major parastatals. Directors noted that structural initiatives such as civil service reform and restructuring or privatization of public enterprises would also help reduce the fiscal deficit and promote efficiency.

Directors urged the authorities to tighten monetary policy until inflation is brought firmly under control, while noting that fiscal adjustment should ease the burden on monetary policy and avoid a crowding out of the private sector. They recommended elimination of interest rate caps and a return to market determination of treasury bill yields. Directors welcomed the steps that have been taken to strengthen banking supervision. In view of current dislocations in economic activity and strains on the financial sector, however, they urged the authorities to be vigilant in identifying weaknesses in the banking system, and to promptly issue the guidelines for dealing with troubled banks.

Directors welcomed Zimbabwe's decision to exit from the fixed exchange rate regime, and underlined the need for further steps to restore competitiveness in conjunction with a tightening of macroeconomic policies. In this connection, they stressed that a flexible and market-determined exchange rate would be appropriate.

Directors encouraged the authorities to deepen trade liberalization, and recommended the elimination as soon as possible of the multiple currency practice and the exchange restriction subject to approval under Article VIII of the Fund's Articles of Agreement.

Directors expressed considerable concern about the impact on Zimbabwe's economy of the government's policy on land reform. They noted that it was important to conduct the process in a lawful manner, and to dispel uncertainties that could entail further large output and employment losses. They urged the authorities to work closely with donors, and recommended, in particular, a close examination of the economic and legal aspects of the land reform program, as well as a careful phasing of the program, commensurate with available financial resources and implementation capacity.

Directors expressed deep concern over the decline in social indicators, and the rapid spread of HIV/AIDS and related diseases. They strongly urged the authorities to formulate appropriate measures to address the social and economic consequences of the health crisis.

Directors underlined the importance of transparency in government operations. Zimbabwe's database continues to suffer from numerous deficiencies in coverage and timeliness, and they urged the authorities to address these shortcomings as soon as possible, including with Fund technical assistance. Directors stressed that timely statistics and full disclosure will be essential to guide the authorities in the implementation of economic policy, and to facilitate the discharge by the Fund of its surveillance responsibilities.

Directors welcomed the authorities' decision to publish the staff report for the 2000 Article IV consultation.

It is expected that the next Article IV consultation with Zimbabwe will be held on the standard 12-month cycle.

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/00/119 (12/4/00) and EBM/00/120 (12/6/00).

3. FINANCIAL TRANSACTIONS PLAN FOR DECEMBER 2000-FEBRUARY 2001—AMENDMENT

The Executive Board approves the amendment to the financial transactions plan for the quarterly period December 2000-February 2001 (EBS/00/226, 11/14/00) set out in Table 1 of EBS/00/226, Supplement 1 (11/30/00).

Decision No. 12351-(00/120), adopted
December 4, 2000

4. EXTERNAL AUDIT COMMITTEE, FY 2001—COMPOSITION

Pursuant to Section 20(c) of the Fund's By-Laws, the Managing Director is authorized to appoint Mrs. Fang Ai Lian to serve as a member of the external audit committee for a term of three years from the beginning of FY 2001. (EBAP/00/136, 11/28/00)

Adopted December 4, 2000

5. INDEPENDENT EVALUATION OFFICE—RECRUITMENT SEARCH FIRM

The Executive Board approves the recommendation set forth in EBAP/00/138 (12/01/00) regarding the selection of a recruitment firm.

Adopted December 5, 2000

6. EXECUTIVE BOARD TRAVEL

Travel by Executive Director and by Assistants to Executive Directors as set forth in EBAM/00/163 (12/01/00) and EBAM/00/124, Supplement 2 (12/01/00) is approved.

APPROVAL: April 13, 2001

SHAILENDRA J. ANJARIA
Secretary