August 21, 2009
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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 09/44-3

2:30 p.m., May 4, 2009

3. Zimbabwe—2009 Article IV Consultation; Targeted Lifting of the Suspension of Fund Technical Assistance

Documents: EBS/09/55; SM/09/102 and Supplement 1

Staff: Kramarenko, AFR; Desruelle, SPR

Length: 1 hour, 19 minutes

Executive Board Attendance

T. Kato, Acting Chair

Executive Directors	**Alternate Executive Directors**
S. Itam (AE)	M. Majoro (AE)
	D. Sembene (AF), Temporary
	B. Lischinsky (AG), Temporary
	S. Duggan (AU), Temporary
	S. Rottier (BE), Temporary
P. Nogueira Batista, Jr. (BR)	M. Agudelo (BR)
	J. He (CC)
	A. Guerra (CE)
	M. Morgan (CO), Temporary
	B. Claveranne (FF)
	S. von Stenglin (GR)
	N. Choudhary (IN), Temporary
	N. Giammarioli (IT), Temporary
	N. Imamura (JA), Temporary
	M. Daïri (MD)
	S. El-Khouri (MI)
	W. Schilperoort (NE), Temporary
	J. Bergo (NO)
	Y. Ustyugova (Ru), Temporary
	A. Al Nassar (SA)
	S. Nget (ST), Temporary
T. Moser (SZ)	
	M. Kaplan (UA), Temporary
	J. Talbot (UK)

G. R. Kincaid, Acting Secretary
I. Teodoru, Assistant

Also Present

IBRD: P. Kumar, P. Nicholas. African Department: M. Atingi-Ego, S. Coorey, L. Engstrom, V. Kramarenko, M. Takebe, G. Verdier. External Relations Department: I. Dieng. Fiscal Affairs Department: R. Hughes. Finance Department: Y. Bal Gunduz, J. Grochalska, P. Njoroge. Legal Department: I. Mouysset. Monetary and Capital Markets Department: S. Erik Oppers, S. Erik Oppers. Office of the Managing Director: C. McDonald. Secretary's Department: P. Cirillo, P. Martin. Strategy, Policy, and Review Department: D. Desruelle, B. McDonald. Statistics Department: A. Burgi-Schmelz, C. Enoch. Senior Advisors to Executive Directors: G. Aboobaker (AE), H. Djoufelkit (FF), A. Ndyeshobola (AE), B. Ólafsson (NO), R. Perez (BR), S. Rouai (MD), G. Ukpong (AE), R. Weber (SZ), Z. Zhang (CC). Advisors to Executive Directors: S. Alnefaee (SA), J. Estrella (BR), E. Haryono (ST), J. Kwakye (MD), L. Lephoto (AE), V. Pillai (UK), A. Rieck (GR), G. Tesfamichael (AE).

3. ZIMBABWE—2009 ARTICLE IV CONSULTATION; TARGETED LIFTING OF THE SUSPENSION OF FUND TECHNICAL ASSISTANCE

Mr. Itam submitted the following statement:

Introduction

The Zimbabwean authorities appreciate the encouragement and support of the Fund. They thank staff for their constructive dialogue during the 2009 Article IV consultation and for the lucid set of reports, and broadly agree with the analyses and recommendations.

Background

In the ten years prior to the emergence of a government of national unity in February 2009, economic and social conditions in Zimbabwe deteriorated significantly and reached crisis proportions. In that period, GDP growth declined by about 40 percent; unprecedented hyperinflation, fueled largely by excessive money growth, resulted in macroeconomic instability and the demise of the national currency; and the debt position became very precarious, with external debt estimated at US$6 billion (189 percent of GDP) at end-2008. The central government's spending capacity collapsed in 2008 as economic decline and rapid erosion of the real value of accrued tax liabilities contributed to a drastic drop in revenues. At the same time, the Reserve Bank of Zimbabwe's (RBZ's) quasi-fiscal activities increased. Furthermore, the tightening of price controls and exchange restrictions exacerbated the deterioration in business climate, exacerbating the economic decline. These factors, coupled with the collapse in the public sector capacity to provide basic services, accentuated unemployment, poverty, and the incidence of infectious diseases.

Economic Developments and Policy Responses by the New Government

Against the background of the economic and humanitarian crisis, the new administration has rapidly taken several macroeconomic and supply-side policy actions in the fiscal, monetary, financial, and structural areas aimed at maintaining low inflation, halting and reversing the economic decline, and improving social conditions. These actions are articulated in the Short-Term Emergency Recovery Program (STERP) of the new administration. Specifically, macroeconomic stability is to be restored and inflation contained through strict fiscal discipline and appropriate monetary policy.

Fiscal Policy

The authorities have made considerable progress in implementing prudent fiscal policy. They introduced a cash budgeting system in 2009. In order to implement the cash budgeting system realistically while addressing critical social needs, the authorities have revised the 2009 budget and have targeted a balanced fiscal position. They project hard currency revenue to increase to US$ 1 billion in 2009 (29 percent of GDP). In this regard, they are stepping up the collection of customs and excise duties as well as value-added tax (VAT), which are expected to account for 60 percent of budget revenue. Expenditure is also budgeted at US$ 1 billion, representing a cut of 15 percentage points of GDP relative to the 2008 outturn. As a contingency plan in case of a shortfall in revenue, the authorities will consider measures to raise additional revenue in July 2009—including increasing royalties on mineral resources and broadening the VAT and customs tax bases—to ensure the provision of critical public services (including food relief, education and health).

The authorities are under intense political pressure to increase public sector wages, cognizant that maintaining the current flat civil service allowance of US$ 100 per month would weaken morale. However, any reasonable pay raise may lead to an unaffordable increase in the wage bill. Thus, the authorities and staff, agree that some decompression of the wage scale would be justified in 2009 to improve motivation and retention of skilled civil servants. This should be preceded by a payroll audit to remove "ghost workers". Regarding any unfilled financing gap in 2009, the government is vigorously seeking donor financing support to help forestall the prospect of drastically reducing expenditures on social programs and incurring payments arrears that could worsen economic and social conditions.

Monetary Policy

The new administration's timely adoption of the use of hard currencies (especially the US dollar and the South African Rand), with the Rand as the reference currency, has assisted Zimbabwe in addressing the acute problem of hyperinflation. In addition, the abolition of exchange controls and liberalization of trade and payments (for all transactions in foreign currency) is helping to restore confidence. Furthermore, the RBZ has been directed to stop quasi-fiscal activities, which hitherto included subsidized direct lending and allocation of foreign exchange, below-cost provision of equipment and fertilizers to farmers, and transfers to parastatals. The expenses arising from the quasi-fiscal activities were mainly financed by surrender requirements on export proceeds, the retention of foreign exchange earnings of the gold and agricultural sectors in excess of mandatory surrender requirements, the confiscation of most foreign exchange deposits, external borrowing, and purchases of foreign exchange at the parallel market exchange rate. These unconventional practices have also been abolished.

The authorities have agreed with the staff recommendation to urgently enable the domestic payments system to process payments in foreign exchange and attune banking system supervision to the needs of the multi-currency system. In addition, ways to improve liquidity management in the new multi-currency system, including through limited lender-of-last-resort operations, are being examined. Also, the authorities are considering measures for strengthening the RBZ's governance and accountability framework, including the appointment of five non-Executive Board members. The authorities plan to explore the merits of possible re-introduction of a national currency at end-2009, taking into account all requisite conditions.

Structural Reforms to Enhance Growth and Competitiveness

The authorities have been pressing ahead with structural reforms since the inception of the new government. Reforms in this area include price liberalization, discontinuation of the foreign exchange surrender requirements and restrictions, abolition of the Grain Marketing Board, and imposition of hard budget constraints on parastatal enterprises. The government is seeking technical advice from the World Bank on other aspects of the reform agenda, including privatization.

The STERP recognizes the urgency of dealing with the general concern regarding property rights and the rule of law. However, staff call for drafting, adopting and implementing necessary legislative acts to deal with these governance issues needs to bear in mind that enacting such legislations requires strong political consensus among the coalition partners. The government intends to continue working hard on confidence boosting measures to elicit the necessary political consensus in the period ahead.

Challenges and Risks Ahead

Notwithstanding the laudable policy and reform measures already taken by the authorities to improve economic and social conditions, there remain many challenges and risks. The authorities are, however, unwavering in their commitment to devote all efforts and available resources to address the challenges and mitigate the risks—which include possible strain in political cohesion; shortfalls in budget revenue and foreign financing; issues related to wage, productivity, employment and competitiveness; capacity constraint; data limitations; debt burden; and, importantly, normalization of relations with the Fund.

However, these challenges and risks are not insurmountable. Indeed, the authorities have addressed several of them through a series of policy actions and reforms, while remaining strongly committed to finding appropriate solutions to the others. But for complete success, the authorities are counting on firm support from the Fund, other IFIs and development partners to complement their efforts. As staff indicated, "economic turnaround would not be possible without foreign assistance and private capital flows, even assuming sound policy implementation". The authorities are, therefore, looking forward to the Fund being favorably disposed to their request for targeted provision of TA in the critical areas highlighted in the "Proposed Decision". It stands to reason that no meaningful economic analysis and decision-making can take place, especially in the fiscal and monetary-financial areas, without properly collated, reliable and timely data. Going forward, therefore, the provision of Fund TA to strengthen statistics should be an integral component of the TA package which should not require a formal listing or 'Decision'.

The authorities acknowledge, with appreciation, policy advice by the World Bank. They thank the governments and peoples of Botswana, the Republic of South Africa and other members of SADC for commitments of financial support, which demonstrate the region's aspiration to see Zimbabwe's economy recover quickly. At the same time, the authorities call on other IFIs and donors to come to the aid of Zimbabwe at this critical juncture when the emergence of a new administration has created an opening for consultation and cooperation. Zimbabwe stands ready to strengthen its cooperation with the Fund and other relevant partners by continuing to build and establish a credible record of strong policy implementation to ensure macroeconomic stability, entrench reforms, collaborate on debt sustainability work, and meet financial obligations to the Fund and other creditors under mutually agreed terms. The authorities look forward to Zimbabwe's full integration into the Fund, with all rights restored in the not too distant future.

Conclusion

The authorities have established an encouraging record of economic policy implementation and reform during the short period of the new government's existence. They are committed to continued implementation of necessary policies and structural reforms to maintain macroeconomic stability essential for reversing the deterioration in economic conditions and tackling poverty. They value the Fund's policy advice and engagement, and look forward to continued strong support for the country by the international community, including the Fund. This new approach reflects the desire of Zimbabwe to cooperate fully.

Mr. Legg and Mr. Duggan submitted the following statement:

The Staff Report makes for sobering—and sad—reading. The people of Zimbabwe have suffered over the last decade under a regime of atrocious governance and appalling policies. According to staff estimates, real GDP has fallen more than 50 percent since 2000 due to the political elite's abrogation of its responsibilities to the Zimbabwean people through extreme corruption, the fuelling of hyperinflation, abandonment of private property rights and abuse of the rule of law. The human toll is catastrophic.

Substantial improvements in political and economic governance are critical to Zimbabwe's future prospects. The formation of the transition government, while less than ideal, is an important step on a long and difficult road. We have enormous respect for Prime Minister Tsvangari's determination and commend him and his Ministers for the substantial progress made by the transition government in a relatively short period of time.

We strongly support the Short-Term Emergency Recovery Program (STERP), which captures the key planks for restoring macroeconomic stability, and agree that broad political buy-in and the support of the international community are key to successful implementation. We recognize the substantial contribution that IMF staff have already made by helping to shape the STERP through the Article IV process and broader policy dialogue.

Policy Directions

We support the authorities' decision to dollarize and their selection of the South African Rand as the official unit of account. A currency board arrangement—and through this, effective elimination of the RBZ's monetary powers—is the only credible nominal anchor in the circumstances. We agree with staff that future changes to the exchange rate regime should only be considered once a strong track record of macroeconomic stability, economic growth, and central bank credibility and accountability have been firmly established. This will take considerable time and therefore any discussion on restoring a national currency should be placed in a longer term context.

We welcome the authorities' stated commitment to prudent fiscal policy and the stringent constraints imposed under the cash budgeting framework. In the context of a significant budget financing gap, public sector wage restraint and improved revenue performance (through both tax reforms and strengthened revenue administration) are essential. Pressures to increase public sector wages should be weighed against the implied opportunity costs, namely the government's capacity to provide humanitarian assistance, provision of basic services and building of critical infrastructure. Strengthened public financial management is also critical for unlocking increased donor support.

We caution the authorities against targeted assistance to so-called 'priority sectors', whether through tax incentives, subsidies, trade protection measures or other forms of preferential treatment. These measures would sit at odds with the authorities' revenue objectives. More fundamentally, targeted industry assistance would detract from the central priority of putting in place the macro and micro foundations for efficient resource allocation in support of sustained growth and development.

Restoration of private property rights and the rule of law are essential for reviving investment and restoring economic growth. We agree with staff on the importance of the commitments to land reform and enforcement of private property rights stated in the STERP being swiftly translated to the adoption—and determined implementation—of well-framed legislation.

Nevertheless, we should not discount the downside risks highlighted in paragraph 31. Questions regarding the sustainability of the current political arrangements pose the biggest threat. And this is inextricably linked to issues of capacity. Key institutions such as RBZ are not just short of technical capacity, but have experienced an erosion of their understanding of, and commitment to, basic principles of good governance.

Proposed Technical Assistance

We support the targeted lifting of the suspension of Fund technical assistance in the specific areas identified by staff (tax policy and administration, payments systems, lender of last resort operations and banking supervision, and central bank governance and accounting) on the basis of recent improvements in policy cooperation with the Fund, the government's stated commitment to regular repayment of its arrears to the PRGF-ESF Trust, and as part of the international community's support for the transition government's reform platform.

Providing technical assistance in an environment where institutional governance has broken down carries enormous risks. This is particularly true in those areas that fall within the mandate of RBZ. Our support for the proposed IMF technical assistance is on the basis that it will be carefully attuned to these risks and that staff will update the Board regularly (at least quarterly) on developments, including progress in repaying arrears to the Fund.

Our approach to any future requests for the targeted lifting of the suspension of Fund TA will rest on the success of this first TA program and the interim government demonstrating further progress towards the objectives of the STERP.

Donor Support

In a statement released at the end of March, our Australian and New Zealand authorities joined the US, UK, France and other donors in agreeing to maintain and, to the extent possible, increase current levels of humanitarian assistance based on identified needs.

These donors also urged the transition government to take additional steps to demonstrate its commitment to reform, such as the immediate release of all political prisoners, the end of farm seizures, the cessation of politically-motivated violence, the establishment of a credible and transparent Central Bank team, an end to harassment and intimidation of the media, and a commitment to credible elections in a timely manner. They signaled that they are ready to support Zimbabwe's rebuilding with development assistance provided there are positive developments in these areas.

Finally, we encourage the authorities to publish the Article IV staff report. Access to the Fund's assessment of Zimbabwe's economic outlook and policies is an important input to international assistance efforts and would signal a new commitment to transparency.

Mr. von Stenglin and Mr. Denk submitted the following statement:

We thank the staff for their excellent report on Zimbabwe's deeply saddening economic collapse which led to a humanitarian disaster in a once blossoming country. We are also grateful for Mr. Itam's very helpful buff statement.

Finally, there are some rays of light. The authorities' short term emergency recovery program (STERP) contains many sensible policy measures, notably establishing the rand as reference currency, ending the central bank's quasi-fiscal activities, and introducing cash budgeting. We welcome these measures. Yet, as the staff rightly points out, the list of risks to the outlook is long and is dominated by domestic political risks.

We agree with the thrust of the staff's assessment and policy advice. We are also ready to support the proposed decision to allow for focused technical assistance (TA), trusting that staff and management will clearly target TA to where it promises to succeed and will closely monitor implementation. In addition, we would like to highlight the following points:

The rand appears to be an adequate nominal anchor in the current situation. However, the near-depletion of currency reserves poses significant additional risks to external and financial stability. We therefore welcome the authorities' intention to conduct a thorough review of the financial conditions of individual banks and to address identified vulnerabilities. In addition, we see merit in discussing appropriate measures to mitigate liquidity risks in the context of Fund technical assistance as well as strengthened collaboration with the South African authorities.

We urge the authorities to spare no effort to strengthen the credibility and accountability of the central bank. We encourage the authorities to fully implement the staff's recommendations with regard to central bank governance and accounting. In addition, we agree that rebuilding an effective and credible institutional framework for monetary policy will take some time. We thus caution against a premature discussion about the revival of the national currency which could potentially scare off potential donors and investors.

Restoring property rights and the rule of law is indispensable to attract private investors for an economic recovery. We therefore welcome the recognition of these aspects in the STERP and encourage the authorities to seek timely implementation of adequate reforms. With regard to tax incentives, subsidies and preferential treatment, we share the staff's concerns and would like to highlight the need to improve the overall business climate.

Finally, both a sustained policy turnaround and external assistance will be necessary to restore stability and growth. The former will also be a precondition for the latter.

Mr. Daïri and Mr. Kwakye submitted the following statement:

We thank staff for the concise report and Mr. Itam for his helpful statement. Welcome progress on the political front that has led to formation of a unity government provides a unique opportunity to turn the situation in Zimbabwe around. Reestablishing macroeconomic stability and addressing acute humanitarian problems while placing the economy on a path of growth represent the key challenges facing the new government. The Short-Term Emergency Recovery Program is well-tailored to addressing these challenges. Given the severe domestic resource and capacity limitations, external financial and technical assistance are critical to helping the country achieve its socio-economic revival.

As intended, fiscal discipline—underpinned by cash budgeting—will offer strong support to macroeconomic stabilization. Incorporation in the Budget of RBZ quasi-fiscal activities and imposition of hard budget constraints on parastatals will bolster fiscal policy transparency and credibility. It is pleasing to see the progressive return of budget revenue and expenditure to normalcy in 2009, after their virtual collapse in 2008. However, there are downside risks to the budgeted revenue target, and we welcome the authorities' intention to take further measures as needed. We agree with the authorities and staff that budgetary expenditure limits are clearly insufficient in the face of large humanitarian and public service needs, and it will be essential to mobilize additional donor budget support for their financing. The intent to address weaknesses in PFM should be carried through to improve expenditure control and efficiency.

The multi-currency system would appear for now to represent the most credible monetary framework and will help provide a credible nominal anchor to deliver rapid disinflation. The system provides new challenges for liquidity management, which will benefit from technical assistance. Also, banking system vulnerabilities, including in terms of capital erosion, currency mismatches, and illiquidity, need to be addressed, and we welcome the RBZ's plans to review financial conditions of individual banks. As agreed, RBZ governance needs to be strengthened in line with best practices to enhance transparency and policy credibility. As noted by Mr. Itam, successful reintroduction of the national currency to replace the multi-currency system would hinge on several key conditions being in place.

Due attention is being given to reforms to strengthen the economy's competitiveness and productive potential. To attract much-needed private investment, the business climate needs to be improved, and to this end, the legal and regulatory framework is being reinforced along with reestablishing market signals. The intent to impose hard budget constraints on parastatals will engender efficiency in the public sector and reduce fiscal costs. While some tax incentives, subsidies, and other protective measures may be needed initially to bolster the real economy, it is reassuring to note that the authorities intend to apply them on a limited basis, targeted to critical sectors.

The DSA shows Zimbabwe to be in debt distress, with key debt indicators far exceeding sustainability thresholds. This highlights the importance of prudent macroeconomic and debt policies, supported by strong concessional financial assistance.

To mitigate the several risks to the economic outlook, steadfast implementation of the intended macroeconomic and structural policies, based on broad political and public support, will be critical, but challenging. Mr. Itam assures of the authorities' unwavering commitment to devote all their efforts to this end. The importance of sizable donor support, including debt relief, to the achievement of the socio-economic objectives cannot be over-emphasized.

In view of Zimbabwe's severe capacity constraints and its cooperation on and commitment to policies to address its Fund arrears problems, we support the proposed decision to partially lift the suspension of Fund TA and expect that full lifting would follow in due course. Economic and social data compilation will need to be improved to enhance surveillance and policy formulation. This will require financial resources and improved capacities, which will benefit from donor assistance.

We wish the authorities success in meeting the challenges ahead.

Mr. Kishore and Mr. Choudhary submitted the following statement:

Zimbabwe had one of the most diversified economies in Sub-Saharan Africa, with a prosperous agrarian sector. As a result of collapse of the commercial agricultural sector on account of the disastrous land reform program and subsequent flawed economic policies, Zimbabwe is today faced with a severe economic and humanitarian crisis marked by deepening poverty and rising unemployment. The economy is in shambles and turning things around would be a mammoth task for the authorities, even with substantial donor assistance.

Prospects of Cooperation

After the power sharing negotiations, the opposition has been co-opted in the government and after a long time, there is hope for movement towards political rapprochement and reestablishing rule of law. However, to what extent, the economic policies are driven by political considerations with the struggle for influence between two main parties is yet to be seen. One of the key test could be the end of forcible displacement of farmers and rule based land reforms. Staff comments are welcome on the direction of economic policies and likelihood of cooperation between the two main parties.

Reforms: The Crucial Requirement

We welcome the authorities' commitment to stop quasi fiscal activities of the Central Bank and implement cash budgeting. We note the difference between staff and authorities on the approach to public sector wage increase and would urge authorities to exercise caution keeping in mind the resource availability. We are looking forward to structural reforms measures like public sector reforms, price liberalization, removal of trade restrictions and legislation to protect property rights in order to enhance competitiveness and boost growth potential. We also agree that adoption of hard currencies for transactions has provided a strong nominal anchor and moving forward, urge authorities to implement staff recommendations to enable domestic payments system to process payments in foreign exchange and attune banking supervision to the needs of the multi currency system.

Restoration of International Community Confidence

We note the strong emphasis of authorities on improving relations with external creditors and sincere effort made to address its arrears problems in the recent past. We also understand the very limited capacity of Zimbabwe to repay Fund arrears at this juncture, but what is important is the strong intent and effort in that direction, clearly visible now. Going forward, keeping in view the authorities forward movement on policies, we support the staff proposal for lifting of the partial suspension of Fund TA to Zimbabwe which will definitely help authorities in their getting a better picture of options available to formulate better policies. We are looking forward to Zimbabwe's full integration into the Fund, with all rights restored soon.

With these observations, we wish the authorities well in their future policy endeavors and efforts to reconstruct economy. We also thank staff for well written papers and Mr. Itam for his informative buff statement.

Mr. Yamaoka and Mr. Imamura submitted the following statement:

We thank the staff for their report and Mr. Itam for his helpful statement. Considering the new administration's commitment and the cooperative nature of the Fund, we support the proposed partial lifting of the suspension of technical assistance.

We welcome the authorities' commitment to overhauling Zimbabwe's economic institutions and stabilizing the social conditions that collapsed due to the authorities' past economic policies. Having said that, the tasks ahead are enormous given that the starting point is to ensure the protection of property rights and the rule of law, without which economic activities never work well. We also note the significant risks stemming from the country's political instability and capacity constraints in the context of an economic and humanitarian crisis.

Moreover, the stabilization obtained through the official adoption of hard currencies should be regarded as a fragile equilibrium, and it should be followed by the implementation of strong policies. Indeed, Zimbabwe's adoption of hard currencies was taken as an only option amidst the complete destruction of confidence in both the nation's own currency and its macroeconomic policies. Since the adoption of hard currencies brings neither an independent monetary policy nor an exchange rate policy, the authorities will have to re-issue their own currency in order to regain their policy maneuvers so as to stabilize the economy over the medium term. Whether this new currency can maintain credibility will warrant close monitoring, especially because people have once lost credibility in the nation's currency control. In addition, many difficult tasks remain, such as the task of determining an appropriate exchange rate between the old currency and the new currency.

Since the Fund has not expressed a favorable view regarding other member countries' move to dollarization following periods of inflation, it is important that the Fund maintain sufficient vigilance against risks related to the future course of the country's policies, and such vigilance should not be biased by any wishful thinking, or by a willingness to re-open a window between Zimbabwe and the Fund. In particular, we look forward to seeing, in the next Board arrear review, a credible track record particularly in terms of the central bank's governance and progress toward clearance of arrears to the PRGF-ESF Trust.

With this, we wish the authorities success in their future endeavors.

Mr. Bakker and Mr. Schilperoort submitted the following statement:

Devastating macroeconomic policies over the past years have resulted in a decline of the economy to the detriment of the Zimbabwean people. We welcome the authorities' resumption of cooperation with the IMF and their coherent policy plans. A forceful implementation of these plans is crucial to lay a basis for sustained recovery.

We would welcome staff's latest insights on the size of the budget financing gap. As we understand it, South Africa is likely to give budget support which will help to fill the gap of $200 million. At the same time, the additional humanitarian assistance of $300 million already provided in 2009 should remain outside of the current budget, and, as we understand it, the recent announcement of $400 million in credit lines from African states relates to the commercial sector and hence will not benefit the budget.

We would like to emphasize the importance of credible independent audits of the financial statements of the RBZ. We much welcome that budget financing by the RBZ seems to have been halted and that the authorities agree that the corporate governance of the RBZ needs to be strengthened.

We would welcome more attention for the financial sector in future staff papers. In its selected issues paper of two years ago staff questioned whether the banking sector continued to be of systemic importance, and the shrinkage of the banks in real terms has continued since. Nevertheless, this is no reason for neglect since a functioning financial system can be of great value in fostering the reversal of economic decline. We hope that upcoming technical assistance should help to paint a better picture of the financial sector.

We support the resumption of technical assistance, while considering the improvement of statistics to be among the key priorities. The informational annex outlines serious concerns regarding the adequacy of statistics, to which we would like to add the need to grasp more reliably the size of the informal sector and the importance of data on micro finance. However, we notice that statistics are not mentioned among the four areas of technical assistance resumption.

Mr. Prader and Mr. Rottier submitted the following statement:

We thank the staff for their report. We agree with their appraisal and their assessment of the economy, the concerns about the humanitarian drama in Zimbabwe and the necessary policy response. No recovery is possible without major efforts from the international community. The IMF should step in as soon as possible. However, it is up to the authorities to ensure that the social and political climate remains conducive to restoring confidence in the country's governance. We thank Mr. Itam for his very insightful and candid buff statement.

We support the proposal that the suspension of technical assistance should be lifted. However, we wonder why there is no technical assistance allowed in the area of statistics. Zimbabwe's data have major shortcomings that limit proper surveillance of its economy.

We welcome the government's STERP program. It is an important first step to improving the economic outlook. More progress in political stability will also be necessary to attract donors. Respect of property rights and a transparent implementation of the rules of law are also needed to rally foreign investors.

We support the use of the South African rand as reference currency. Anchoring expectations is a precondition to restoring the needed credibility of the monetary framework. The randization should also benefit the fiscal revenue collection.

We welcome the authorities' commitment to exercising restraint from the central bank undertaking quasi-fiscal activities.

Strict implementation of a cash budget on a month-by-month basis is critical for curtailing the deterioration of the macroeconomic outlook. Therefore, major efforts will be urgently needed so that fiscal discipline can be introduced. The authorities should abolish the large tax exemptions and increase royalties on mining receipts. Some expenditures will have to be contingent on donor financing.

A responsible response to wage increase demands will be necessary. We understand the social concerns. However, the authorities should seriously respect the limits of their cash budget. The authorities should also consider the spillover effects of major public wage increases on the private sector.

Lastly, we agree with the staff that Zimbabwe's public debt is unsustainable. Could the staff tell us whether Zimbabwe would be HIPC-eligible once arrears are cleared and what amount of debt relief the country could get?

Mr. He and Mr. Zhang submitted the following statement:

We thank staff for their informative reports. We welcome the recent progress the Zimbabwean authorities have made in social and economic stabilization, including price stabilization, improvement in the availability of basic goods, and a gradual restoration of market signals. These achievements are attributable to the implementation of many of the policy recommendations by staff early this year, including a fiscal adjustment, adoption of a strong nominal anchor, price liberalization, imposition of hard budget constraints on parastatal enterprises, and elimination of most restrictions on current account transactions. Further more, they reflect a significant improvement in Zimbabwe's cooperation on economic policies with the Fund. We are pleased to note that broad agreement on policies was reached during the consultation. However, the authorities face severe capacity constraints in implementing these policies. At this juncture, we urge the Fund to fully lift the suspension of its technical assistance to Zimbabwe.

We commend the authorities' strong commitment to implement sound and forward-looking policies and improve cooperation with the Fund and its developmental partners. The top priority should be achieving low inflation by a mix of fiscal and monetary measures, including maintaining official dollarization as the nominal anchor, the elimination of the Reserve Bank of Zimbabwe's quasi-fiscal activities, and strictly implementing cash budgeting. The authorities also need to immediately implement the supply-side measures as set out in their Short-Term Emergency Recovery Program (STERP) for 2009 to restore production and improve social conditions. We encourage the authorities to contain public sector wages.

It is regrettable that progress in resolving Zimbabwe's arrears to the PRGF-ESF Trust has been limited and in light of Zimbabwe's very limited payment capacity, it would be difficult for the country to make significant payments to the Fund under the current circumstances. We reiterate that the satisfactory solution to this problem largely depends on rejuvenating the economy, thereby generating adequate repayment capacity. As staff pointed out in their report, Zimbabwe is at a critical juncture and faces a historic opportunity to improve prospects for economic growth and poverty reduction which requires broad support from the international community. In our view, it is also an opportunity for the Fund to show responsibility and leadership in this regard. We call for consideration of restoring Zimbabwe's voting rights in the Fund and its eligibility to use the Fund's general resources.

With these remarks, we wish the authorities all the success in their future endeavors.

Ms. Lundsager and Mr. Kaplan submitted the following statement:

We thank the staff for its informative report. Mr. Itam's comprehensive statement catalogues Zimbabwe's self-inflicted collapse over the past ten years. The emergence of a government of national unity in February 2009 now offers a chance for a turning point. Political risks to the sustainability of the power sharing agreement are serious, however, and the Zimbabwean people's pent up expectations for recovery would be unrealistic, even in the best of global economic conditions.

We are ready to support the provision of targeted Fund technical assistance to the Ministry of Finance to help it implement its reform agenda, and support the proposed Decision.

There are reasons for cautious optimism about the economy—first and foremost the spontaneous collapse of hyperinflation. Elements within the new government appear ready to press forward with much needed reform. Many of these reforms—price liberalization, elimination of surrender requirements, and cessation of quasi-fiscal activities at the Reserve Bank—were measures that had been advocated for by the staff for years.

Fiscal Policy

We recognize the challenges that confront the fiscal authorities as they attempt to rebuild their revenue collection capacity and meet important expenditures, including wage payments, rehabilitation of basic water and power infrastructure, and health supplies. We understand the political difficulties that surround the flat civil service allowance of $100 a month. However, we agree with the staff that changes to the wage scale must be approached with extreme caution, given the already tenuous fiscal situation and the competitiveness implications of such a move. We support the authorities' plans to carry out a government payroll audit as an appropriate first step.

We support the efforts of the authorities to strengthen their public financial management systems with the assistance of the World Bank. Significant reform in this area will be critical to unlocking donor support.

Monetary Policy

Many of the economic problems that Zimbabwe has faced in recent years can be traced to misguided policy decisions at the Reserve Bank. Bluntly stated, concerns with the management of the RBZ remain a key source of political and operational risk for Zimbabwe's recovery. The proposed appointment of five non-Executive Board members to oversee RBZ operations is an appropriate step.

Completion and publication of the legally-mandated annual audit of the RBZ's financial statements by a credible audit firm is a critical step in identifying vulnerabilities on the balance sheet and will also be a first step toward improving the accountability and transparency of the Bank's operations. We also support the staff's suggestion for a thorough review of bank balance sheets to identify vulnerabilities. Recalibrating the payments systems to handle multiple currency transactions is also a clear near-term priority in order to get the economy moving again.

Arrears Clearance

Zimbabwe owes SDR 73.83 million to the PRGF, and the Reserve Account has been reduced to cover these arrears, which reduces the amount of subsidies that the Reserve Account can provide for new lending to the rest of the Fund's low-income members. Even on the best assumptions for strong policy cooperation with the Fund from the Zimbabwean authorities, arrears clearance and possible debt reduction for Zimbabwe promises to be complicated.

If the Fund's Governors approve a general allocation of SDR amounting to some $250 billion, Zimbabwe will receive an allocation in the range of SDR 272 million. We see great merit in Zimbabwe repaying its arrears in the PRGF, which will remove a serious roadblock on the path to normalization of relations with the international financial community.

Mr. Talbot and Mr. Pillai submitted the following statement:

We thank staff for the useful set of papers and Mr. Itam for his candid buff statement. We concur with most of the analysis in the staff papers.

The Staff report clearly highlights the degree of appalling economic mismanagement that has led to a severe economic and humanitarian crisis in Zimbabwe. An extended episode of destructive policy-making will necessitate radical institutional reform as a pre-requisite for Zimbabwe to begin establishing a new and credible track-record of sound economic management.

The formation of the Government of National Unity (GNU), has led to substantive and commendable change in the area of economic policy-making. We also commend the authorities for engaging with Fund staff on substantive policy dialogue for the first time in a number of years, and we hope the cooperation will be strengthened further going forward.

In addition to the measures enforced by dollarization, the new government has implemented a range of welcome measures in the area of fiscal and economic governance, including, critically, measures to reverse the previous funding of quasi-fiscal activities through massive money creation and confiscation of foreign exchange. We congratulate the authorities for abolishing foreign exchange retention by RBZ and preparing a more realistic budget for 2009. There have also been some important corrections in the functional roles of the Ministry of Finance and RBZ although, as highlighted in the staff report, much remains to be done to enhance the governance of the RBZ in order to reduce the risk of policy slippage or even reversal.

The key challenge going forward will be to sustain and deepen reform and to avoid policy reversals in areas where there has been welcome movement in recent weeks. We strongly encourage the authorities to implement critical policy measures and institutional reforms identified by staff, including:

- avoiding policy reversals, e.g. on price liberalization and restoring market signals; and setting hard budget constraints for parastatals and maintaining fiscal discipline;

- working within agreed ceilings for wages and avoiding unaffordable wage demands as acknowledged in Mr. Itam's statement, linking wages to productivity, and conducting a payroll audit;

- establishing a Board of non-executive Directors to ensure that the RBZ operates within an appropriate mandate; publishing audits of RBZ and its subsidiaries; and imposing strict limits and procedures on international borrowing by the RBZ;

- establishing the RBZ's role as lender of last resort and operating the payments system in hard currency;

- signaling and demonstrating commitment to ensuring protection of property rights and to maintain the rule of law; and

- Zimbabwe should defer planning to reintroduce a local currency until strong institutional and legal requirements for credible monetary policy management are established. In the interim, it should seek to implement the policy of using rand as the reference currency.

As staff note, there are fiscal uncertainties in 2009, especially over the pick-up of revenue. Staff projections rise steeply towards the end of the year, with average last quarter revenue projected to be over $100 million. Could staff comment on what revenue policies and administrative measures are necessary to achieve these rates? And what are the main downside risks to this pick-up in revenue? What are staff views on the comprehensiveness of revenue collections, and are there significant sources of potential revenue that are currently not collected, including in extractive industries?

We concur with staff that there is likely to be a significant financing gap in 2009—although there exists significant scope for error in forecasting revenues and capacity for absorbing expenditure. We look forward to the outcome of donor consideration of possible time-bound targeted assistance to help deliver the 2009 budget. Such consideration will no doubt look at measures to safeguard donor funds while ensuring resources achieve macroeconomic and fiscal objectives. It is helpful that the Fund has analyzed the extent of donor assistance to Zimbabwe over the last few years. The Fund's estimate of $500 million donor support in 2008 shows that the international community has been effective in providing life saving support on a large-scale. This has been despite appalling economic management and governance, and despite specific obstacles designed to impede donor and NGO access to provide humanitarian aid.

We support the recommendation for targeted lifting of the suspension of Fund TA. This significant step by the Fund would recognize the turnaround in economic policies since the establishment of the GNU, and re-engagement of serious policy dialogue with the Fund. TA will provide the authorities with an opportunity to build upon their reform efforts in addressing the considerable set of challenges that lie ahead. We join Mr. Legg and Mr. Duggan in asking staff to keep the Board regularly updated on progress in delivering this TA.

Mr. Horgan and Mr. Ladd submitted the following statement:

We thank the staff for their extraordinary efforts in Zimbabwe and for a clearly-written staff report. We appreciate Mr. Itam's informative buff. Zimbabwe has, at last, taken strong measures to halt the deterioration of its economy, a deterioration which has had serious consequences for the health and prosperity of its people and for the stability of the region. The Fund's considerable experience in rescuing hyperinflation cases will be invaluable at this time. We agree with the staff's appraisal and support the request for a targeted lifting of the suspension of Fund technical assistance.

Monetary Policy

By adopting hard currencies for transactions and the rand as the numeraire, the authorities have taken a radical but necessary step. We support maintaining official dollarization ("randization?") as the nominal anchor for the foreseeable future. The staff report indicates that the authorities will consider the merits of reviving the national currency in late-2009, but they should be in no rush. There is a daunting agenda of reforms (para. 24 and throughout the staff report) before Zimbabwe has a trustworthy central bank that can implement a credible monetary policy framework. In the meantime, we applaud the decision to put a halt to quasi-fiscal activities of the central bank (para. 14) and can support, with some trepidation, the provision of the limited technical assistance required to support implementation of the new currency regime. We welcome the measures to strengthen governance of the central bank (para. 23) but note that they fall short of an independent audit of the RBZ. Such an audit will be required, sooner or later.

Fiscal Policy

Zimbabwe's fiscal policy, and fiscal accounts, are clearly in chaos (para. 10). Their debt, as best it can be ascertained, is unsustainable (Appendix 1). Under these circumstances, the adoption of month-by-month cash-balance-based budgeting is appropriate. Short-term rolling budgeting, alongside dollarization, will help to break inflationary expectations, as the staff points out (para. 38). We agree that the authorities must follow through on their plans to mobilize revenues, to contain expenditures (especially disciplining parastatals) and to mobilize donor support for critical humanitarian needs. Any eventual move to "restructure, privatize or liquidate" state-owned enterprises should be undertaken transparently and in a manner consistent with best practice. Mr. Itam's buff suggests that the authorities may have found a way to finesse the pressure for across-the-board wage increases with a decompression of the wage scale.

Structural and Other Issues

We agree with the measures that the staff recommends for re-establishing Zimbabwe's environment for direct investment, indigenous and foreign (paras. 42 and 43). It was not so long ago that Zimbabwe was an economic bright spot in Africa, and a renaissance is feasible. Of course, there is a litany of serious risks that could derail progress (political disagreement, social unrest, inflation or deflation, bank collapse and capacity constraints). There will be opposition, on ideological and self-interested grounds, to the restoration of economic normality in Zimbabwe, as Mr. Itam's buff alludes (para. 8).

We must also remember that Zimbabwe has been in continuous arrears to the PRGF-ESF Trust since February 2001 and that these arrears stood at SDR 89 million as of December 2008. While recognizing that Zimbabwe has limited resources, we attach the highest importance to the authorities accepting and keeping to an agreed schedule of payments on their overdue financial obligations to the Fund and other official creditors.

Like Mr. Legg and Mr. Duggan, we urge the authorities to consent to the publication of the staff report. This gesture of transparency will be a helpful backstop to the emergency reform program.

With this, we wish the Zimbabwean authorities all the best with their emergency recovery program and urge them to continue their improved cooperation with the Fund.

Mr. Rutayisire submitted the following statement:

We thank Mr. Itam for a helpful buff statement and the staff for an informative report.

Since the last Article IV consultation, Zimbabwe has continued to face fierce economic challenges. Consumer price index inflation peaked in September 2008, fueled by unprecedented money growth. Partly as a result, GDP contracted significantly over recent years and the external position continued to deteriorate sharply. Against this backdrop, we welcome the Short-Term Emergency Recovery Program (STEMP) put in place by the new administration with a view to ensuring macroeconomic stabilization and a prompt economic recovery and improving social conditions.

We take good note that a number of policy measures recently implemented by the authorities are in line with Fund advice, including the recommendations formulated at the time of the Board review of Zimbabwe's overdue obligations to the PRGF-ESF Trust which was held last January. These include the steps taken to carry out a sizable fiscal adjustment, establish a strong nominal anchor, remove price controls and most restrictions on current account transactions, and impose budget constraints on parastatal enterprises. We welcome the recent introduction of the cash budgeting system, as reported in Mr. Itam's statement.

The recent transition to a multi-currency system has been instrumental in helping achieve macroeconomic stabilization and strengthen the monetary framework. We are encouraged by staff's projection that such a system will contribute to containing CPI inflation to one-digit levels in 2009 notably by supporting fiscal discipline.

We are encouraged to note from Mr. Itam's statement that the Zimbabwean authorities stand ready to enhance cooperation with the country's partners, including the Fund, by pursuing notably a credible record of strong policy implementation and meeting financial obligations to the Fund and other creditors under mutually agreed terms. We encourage the authorities to secure the political consensus needed for a sustained and successful implementation of the STEMP.

Given the demonstrated performances, we support the staff's proposal for a partial lifting of the suspension of Fund technical assistance to Zimbabwe.

Mr. Al Nassar submitted the following statement:

I thank the staff for a candid and well-written report and Mr. Itam for his helpful buff statement. It is most unfortunate that the deterioration in Zimbabwe's economic performance has accelerated since the last Article IV consultation. Indeed, over the past two years, GDP shrank substantially and inflation spiraled out of control. That said, the formation of a national unity government in February and the formulation of a Short-Term Emergency Recovery Program (STERP) are welcome first steps toward addressing the pressing economic and social needs of the country.

Turning to the details of the STERP, the adoption of multi-currency system is the most appropriate monetary framework at this stage, given the unprecedented hyperinflation and the demise of the local currency. I also agree with the authorities' choice of the rand as the reference currency in view of the potential significant benefits of closer regional integration. Turning to the financial sector, I share the views of the authorities and the staff that there is an urgent need to enable the domestic payments system to process payments in foreign exchange and attune banking system supervision to the needs of the multi-currency system. I also welcome the plans of the Reserve Bank of Zimbabwe (RBZ) to conduct a thorough review of the financial conditions of individual banks.

On the fiscal front, I welcome the introduction of a cash budgeting system and am encouraged by the substantial increase in hard currency budget revenue in February 2009 and by the government's expectations that revenues would steadily increase to total US$1 billion for the year. However, the substantial expenditure needs and staff's estimates of lower budgetary revenues underscore the need to strengthen public financial management. Here I would appreciate staff's comments on the budgetary developments during the first 4 months of the year.

Turning to structural reform, while welcoming the measures that have already been implemented, I share the view that respect of property rights and the rule of law are essential for a recovery in investment and growth. In this regard, I endorse the staff's recommendation to draft, adopt, and implement the needed legislation to ensure property rights. I also welcome the ongoing efforts to enhance the functioning of the parastatal enterprises.

Against this background of significant improvement in Zimbabwe's cooperation on economic policies and the commitment to improve cooperation on payments to the Fund, I support the proposed targeted lifting of the suspension of Fund technical assistance to Zimbabwe.

Mr. Mozhin and Ms. Ustyugova submitted the following statement:

At the outset, we would like to express our deepest sympathies to the Zimbabwean people for having to endure the severe humanitarian crisis resulted from destructive economic policies that have been pursued for many years. Unfortunately, even with the most decisive steps going forward, it will take much more time to rebuild the economy and the social conditions than it took to ruin them.

The 2009 Article IV Consultation

We thank the staff for the excellent report which candidly describes the economic situation in Zimbabwe and elaborates on measures that are absolutely necessary for preventing further economic and social corrosion. We agree with the staff's recommendations and encourage the authorities to fully implement them. We will emphasize the following points.

We welcome the government's Short-Term Emergency Recovery Plan. It contains a comprehensive package of policy and structural measures that are economically feasible and can stabilize the economic situation in Zimbabwe. Among them, we place the top priority on enforcing property rights and the rule of law. We urge the authorities to undertake urgent steps in this area.

Multi-currency system is indeed the essential element of the stabilization strategy. It automatically eliminates the bad practice of monetizing the budget deficit and imposes the budget constraints. From this perspective, the credibility of such a monetary framework is largely automatic and does not require special commitment from the authorities' side. With much work needed to rebuild accountability and credibility of the central bank and to establish track record of sound fiscal policy implementation, any discussions in the near future on reviving the national currency seem to be meaningless if not harmful.

Fiscal discipline is indispensable for economic stabilization. Targeting a balanced fiscal position on a month-by-month basis is an appropriate approach to fiscal management in case of Zimbabwe. It also hedges against the risks from fiscal slippages when budget revenue estimates are either overly optimistic or subject to serious downside risks. In particular, the assumption that budget revenue would rise from 4.2 percent of GDP in 2008 to 29 percent of GDP in 2009 looks somewhat unrealistic, as it would require a dramatic pick up in economic activity. To address downside risks to revenue, the authorities also intend to consider increasing royalties and broadening the tax base. We would appreciate the staff's comments on the effectiveness of such measures.

We note that even with all possible spending cuts, budget revenue would still be insufficient to cover all the critical expenditures. In order to count on donor support to finance the gap, the authorities should put forward sound principles of public financial management.

Technical Assistance

We support a partial lifting of the suspension of technical assistance (TA) to Zimbabwe to allow for the resumption of TA in the areas proposed by the staff. The staff is right to emphasize that technical capacity constraints may undermine the implementation of the emergency recovery program. Indeed, maintaining a multi-currency system, which is a pillar of viability for this program, is technically demanding, as it requires reorganizing the payments system, banking supervision practices and lender-of-last-resort operations. Consequently, TA in these areas is absolutely necessary, but, unfortunately, not sufficient for having Zimbabwe's arrears to the PRGF-ESF Trust to be resolved. It is the authorities' willingness to sustain their commitment to improving the cooperation with the Fund both on economic policies and payments which is crucial. Therefore, while supporting the request for TA, we expect the authorities to exhibit the discernible efforts in both areas, confirmed by regular payments to the Fund, as indicated in para 3.

We also believe that TA in the area of statistics should be made an integral component of the TA package, as emphasized by Mr. Itam in his buff statement. According to the informational annex, there are serious shortcomings in all major datasets. In our view, the bad quality of economic statistics constraints policy formulation and monitoring not less then the lack of expertise in economic policies in the dollarized environment.

Mr. Claveranne submitted the following statement:

We thank staff for their very informative report and Mr. Itam for his insightful buff statement.

We welcome the actions already taken by the new government to address the most pressing short-term economic recovery needs and the preparation of a Short-Term Emergency Recovery Program (STERP) for 2009.

We support the three axes of the discussion with the authorities: (i) transition to sound fiscal management while addressing critical social needs; (ii) the appropriate nominal anchor and banking supervision, (iii) structural reforms to enhance growth potential and competitiveness.

On the fiscal management side, we welcome the implementation of cash budgeting and the targeting of a balanced fiscal position on a month-by-month basis. We also welcome the transfer of quasi-fiscal operations to the treasury. Amidst the expected rise in hard currency budget revenue, the 2009 budget financing gap is likely to reach $200 million, which can only be financed through donor budget support. Without such a financing, the government would be bound to reduce expenditures on social programs, postpone public investment projects and incur payment arrears. In order to incite donors to provide budget support, we encourage the Fund and the World Bank to make technical assistance (TA) available with a view to help the authorities to improve public financial management.

Unprecedented hyperinflation led to the demise of the local currency and almost complete dollarization in late 2008. We welcome the multi-currency system with the rand as the reference currency and concur with staff and the authorities to consider it as the essential element of the stabilization strategy, because under such a system it is impossible to monetize the budget deficit. We encourage Fund to provide TA to help banks to cope with this new multi-currency system and to improve the RBZ governance. A reliable and credible central bank is critical to economic recovery and to donor budget support. Furthermore, the adoption of a new central bank legislation is a key prerequisite for a revival of the national currency.

We encourage the authorities to move forward with fundamental structural reforms. In particular, the respect of property rights and the rule of law are essential for reviving investment and economic growth. We urge the authorities to implement shortly the necessary legislative acts for that purpose, as envisaged in the STERP. It is also important to initiate a comprehensive review of parastatal enterprises and then impose hard budget constraints by eliminating quasi-fiscal subsidies. We encourage the authorities to implement STERP commitments to restructure, privatize or liquidate nonviable parastatals in the medium term.

The DSA exercise is subject to major caveats due to the lack of reliable data, but we take note of staff's assessment that Zimbabwe is in debt distress. In that regard, we concur with staff that, in any case, establishing a track record of sound policy implementation is a critical first step to resolving overdue financial obligations to official creditors, including the IMF, and ultimately securing donor financial support.

Mr. Sadun and Mr. Giammarioli submitted the following statement:

We thank staff for the comprehensive analysis and clear report as well as for their effort to remain engaged with the authorities. We also thank Mr. Itam for his helpful buff statement.

After having suffered large cumulative GDP losses and high inflation for a decade, the Zimbabwe's economy deteriorated further in 2008, culminating in a humanitarian crisis with almost 70 percent of the population in need of food assistance and with high rates of child and maternal mortality. Political instability and hyperinflation have led economic activity to a standstill and a sharp fall in fiscal revenue and expenditure. The resulting disruption of public service provisions exacerbated the effect of the crisis on the population. In addition, the external position deteriorated severely. The large current account deficit was mainly financed by depleting international reserves and increasing external debt, a large part of which is represented by arrears, including overdue financial obligations to the IMF.

We concur with the staff that these disastrous outcomes derive from poor policies and weak governance. In particular, the massive Reserve Bank of Zimbabwe's (RBZ) quasi-fiscal activities, and their monetization, seem to be at the root of hyperinflation. Poor governance and accountability of RBZ are also contributing to the financial chaos. Tightening of price controls and exchange rate restrictions, widespread land invasions, and the confiscation of foreign currency deposits as well as frequent changes in business regulations are just a few examples of misguided policies that are harming the country.

Against this background, a new government of national unity, devoted to tackling the difficult economic and humanitarian crises, was formed last February. The government has immediately started to work on short-term economic recovery measures and much needed structural reforms. The Short-Term Emergency Recovery Plan (STERP) for 2009 includes a number of measures aimed at curbing inflation, arresting the economic decline, and improving social conditions. In this respect, the decisions to maintain strict fiscal discipline (stopping the RBZ's quasi-fiscal activities and cash budgeting) as well to adopt a strong nominal anchor (multi-currency system with the Rand as the reference currency) are much appreciated. Further efforts are needed to strengthening the RBZ governance, guaranteeing property rights and the rule of law, liberalizing prices, and removing exchange rate restrictions.

Radically different policies and greater cooperation with the international community are necessary to tackle the economic and social problems in Zimbabwe. Sound policies without massive foreign assistance and private capital flow could be however insufficient. Furthermore, a long list of downside risks, including possible policy reversals, add uncertainty to the economic perspectives. The results of the Debt Sustainability Analysis, confirming that Zimbabwe is in debt distress, is particularly worrisome. In this respect, we agree with the staff's appraisal that establishing a track record of sound policy implementation is key in resolving overdue financial obligations to official creditors, including the IMF, and in regaining donor's financial support to help reconstruct Zimbabwe's economy.

In the context of Zimbabwe's overdue obligations review, the Executive Board identified four major recommendations last January: i) substantial fiscal adjustment; ii) liberalization of price controls and impositions of hard budget constraints on public enterprises; and iii) exchange rate unification and removal of all restrictions on making payments and transfers for current international transactions; and iv) establishment of a strong nominal anchor for monetary policy. Taking into consideration that such recommendations have been accepted and that the authorities have expressed their commitment to improving their cooperation on payments to the Fund, we can support the decision of a partial lifting of the suspension of the Fund's technical assistance to Zimbabwe. Nevertheless, we urge staff to closely monitor the situation and report promptly to the Board, should this attitude change in the future.

Mr. Moser and Mr. Weber submitted the following statement:

The population of Zimbabwe continues to suffer from a decade of public economic mismanagement that culminated in out-of control hyperinflation and the collapse of domestic production and public services in 2008. This home-grown crisis is now being exacerbated by the impact of the global recession on the region. We are concerned that staff expects the agricultural sector to decline further, for the ninth year in a row. Only the revitalization of this sector will allow a broad-based economic recovery, increased export earnings and improved socio-economic indicators. Given the dire humanitarian situation in the country, economic stabilization is but one of the necessary conditions to restore some degree of normalcy to daily lives. Misguided and weak governance has been at the cause of Zimbabwe's crisis and will remain a major obstacle to a recovery, if not remedied.

We note that, thanks to a complicated political agreement, the government is attempting to reverse the decade-long economic slide. The official adoption of hard currencies for transaction has provided a much needed nominal anchor for monetary policy. We are encouraged by the commitment to stop quasi-fiscal activities by the central bank and to address weaknesses in public financial management. The adoption of cash budgeting will help adapt to the new constraints but may amplify the volatility of public services delivery. It should eventually be replaced by an annual budgeting process that is transparent and based on realistic assumptions and projections.

Even if the authorities adhere to significant fiscal restraint going forward, the financing needs remain daunting in their magnitude, as does an unsustainable burden of external debt and arrears. We note with great concern that neither the fiscal nor the external positions are sustainable without massive foreign aid injection. A sound economic reform strategy that clearly breaks with the past and the restoration of good relations with donors are key preconditions for mobilizing the necessary financial flows. It is also important that the authorities affirm their intention to resolve overdue financial obligations, including to the Fund, so that they can regain access to international support programs.

We consider staff's medium-term baseline predicated on achieving 6 percent real GDP growth a best case scenario, and would have liked staff to be more explicit on the amount of financing (and possibly debt restructuring) needed. We note the SADC's promise to help Zimbabwe raise financial aid worth USD 8.5 billion. Could staff inform about the amounts already raised or pledged and whether the large amount targeted can be absorbed?

Budgeting is particularly precarious in the current transition period to a new currency arrangement. We concur with staff that the authorities should be conservative regarding tax and customs revenues, given that these will be payable in foreign exchange. In this context, we would welcome comments on the tax cut on gold export revenues and how this fits into a royalty and taxation framework for the mining industry. Financing the current wage bill will already be a challenge and we concur with staff that pressure for exceeding the current envelope should be resisted. We welcome the authorities' plan to audit the public sector payroll, which should allow to eliminate ghost workers.

The newly introduced multi-currency system, with the rand as the reference currency, gives rise to ambiguities. We wonder why this system is deemed superior to a peg (to one currency or a mix of hard currencies) for anchoring monetary policy. Were South Africa and Botswana consulted on Zimbabwe's move and will it impact their monetary operations? What is the status of the various foreign currencies in use? In our view, the reintroduction of a new local currency at this stage would clearly not be credible and must not be rushed.

We regret that Zimbabwe continues to accumulating arrears to the PRGF-ESF Trust, imposing a financial burden on the Fund's membership and reducing the resources available to support other members. Given signs of improved cooperation on policies, however, and the authorities' commitment to resume regular payments to the Fund, we are ready to support the proposed targeted lifting of the suspension of Fund TA to Zimbabwe. We call upon the authorities to strengthen cooperation with the Fund and to adopt a comprehensive recovery program, including the restoration of property rights and the rule of law.

Regarding the remaining sanctions that are in place against Zimbabwe with regard to the voting and related rights, at the time of the 2006 Article IV consultation the Executive Board could not agree on further actions that are required of Zimbabwe in order for the sanctions to be lifted, and the Board has not returned to this issue, as it would be required under Rules K-4 and K-7. Could the Chair inform the Board on how management intends to proceed on this issue?

We welcome the authorities intention to improve the timeliness of data reporting and transparency of government and RBZ operations. Zimbabwe's statistics remain poor for surveillance purposes and are also likely to hamper the effective use of potentially increased foreign aid. We wonder to what extent improvements in statistics are due to capacity constraints and, if so, whether they are accommodated by other donors. The staff's comments would be appreciated.

Ms. Agudelo and Mr. Estrella submitted the following statement:

We thank staff for the set of documents and Mr. Itam for his informative buff statement.

We are pleased to note that after a significant deterioration of macroeconomic and social indicators, the Zimbabwean authorities are willing to take corrective policies to reverse trend. Real GDP declined (cumulative) by about 21 percent in 2007/08, due to economic disruptions, hyperinflation (500 billion percent by September 2008), and a significant deterioration in the business climate. No doubt, poverty, unemployment, the cholera epidemic and child mortality have risen to catastrophic levels. In 2008, the central government's revenue and expenditure effectively collapsed and quasi-fiscal activities undertaken by the Reserve Bank of Zimbabwe (RBZ) increased to 36 percent of GDP. In order to finance part of its activities the government undertook surrender requirements on export proceeds, the retention of higher than mandatory foreign exchange earnings of the gold and agricultural, a freeze of most foreign currency deposits, external borrowing, and purchases of foreign exchange at the parallel market exchange rates. All of which inflicted great damage to the economic activity.

The macroeconomic outlook is extremely uncertain, however, there should be light at the end of the tunnel. Following the signing of the Global Political Agreement and the subsequent constitution of an Inclusive Government in February 2009, the authorities launched the Short-Term Emergency Recovery Program (STERP) in March 2009. Although we understand that this program will only cover the period until December 2009, the intention of the Inclusive Government to work on a more comprehensive medium to long-term development plan is rightly placed.

We welcome that the short-term key priority areas of the STERP are related to political and governance issues, provision of social safety nets and support for capacity building in key areas of the economy, that is, agriculture, mining, manufacturing, construction and tourism among others. The STERP also prioritizes provision of adequate basic social services, including access to health care, education and humanitarian assistance.

Successful implementation of the STERP will require financial resources. However, as the staff have emphasized, private capital inflows and donor support may not pick up as expected by the authorities, and even if policies were improved and private sector inflows increased, large external financing gaps would persist and external debt would remain unsustainable over the medium term. Therefore, it is extremely important to establish a track record of sound policies to attract donors and international support.

The key monetary element of the STERP is the multi-currency system with the rand as the reference currency. With the widespread use of foreign currency and the lack of an institutional framework to ensure the central bank's credibility and accountability, this was the only credible monetary framework to show results in the short term. We welcome the authorities' decision to present the next budget in rands, and adopt this currency as the sole unit of account for the public and private sectors in the near future. Having a strong nominal anchor is key to begin rebuilding economic confidence.

On the positive side, following the adoption of the multicurrency system and the subsequent pricing of goods and services in foreign currency, the country recorded a decline in month-to-month inflation for the first three months of 2009. We welcome the authorities' (unity government) recent decision to maintain the current US$100 current flat civil service allowance (payment of civil servants). However, we understand that at some point the authorities would need to deal with a revision of the public sector wages, which should be addressed in the context of a reformed civil service.

For the medium term, and the earlier the better, we encourage the authorities to pursue their enormous agenda of needed structural reforms. Among the most important ones are price liberalization, the discontinuation of the foreign exchange surrender requirements and restrictions, the abolition of the Grain Marketing Board, and the imposition of hard budget constraints on parastatal enterprises.

All in all, for the STERP to succeed, commitment to the economic agenda is fundamental. We support the proposed decision to partially lift the suspension of the Fund's technical assistance to Zimbabwe in the areas of tax policy; payments systems; lender-of-last-resort operations, as well as banking supervision and central banking governance and accounting. We would like to know about World Bank's involvement with the country at this stage.

Mr. Chua and Mr. Haryono submitted the following statement:

We welcome with the improvements in Zimbabwe's cooperation with the Fund. It is important for the dialogue between the authorities and the Fund to continue in order to bring the macroeconomic conditions of the country back on track. The economic outlook is challenging given the sharp decline in economic activity and worsening humanitarian situation in Zimbabwe during the last decade. We support the thrust of staff's assessment and the request for targeted lifting the suspension of technical assistance.

Combating hyperinflation should be a top priority at this juncture. In this regard, we urge the authorities to learn from the Fund's experiences in dealing with this challenging macroeconomic issue. In the same vein, we welcome the Short-Term Emergency Recovery Program (STERP) of the authorities. However, we should bear in mind that the economic program alone is not enough to solve acute economic and humanitarian problems of the country. Political and social stability are prerequisites for any economic program to work.

On macroeconomic management, the official adoption of hard currencies for transactions has provided a much needed anchor for monetary policy. We urge the authorities to move expeditiously to restore macroeconomic stability coupled with a credible institutional framework. A well-sequenced liberalization of price and exchange rates would be a welcome step to enhance competitiveness and growth. Banking supervision needs to be strengthened following the introduction of foreign currencies in payment and banking systems.

We welcome the authorities' stated commitment to prudent fiscal policy and the rules under the cash budgeting framework. We urge the authorities to improve relations with the donor community to mobilize external financing for social and infrastructures. Zimbabwe also needs to pursue structural reforms, including improving private property rights and strengthening the rule of law. These steps are essential for much needed private investment to take place.

With these remarks, we wish the authorities the success in their challenging endeavours.

Mr. Henriksson and Mr. Ólafsson submitted the following statement:

Economic growth in Zimbabwe has contracted by more than 40 percent 1999-2008. Growth is projected to turn positive in 2009. Domestic macroeconomic policies were the main contributing factor in creating this outcome. The new government of national unity is faced with the difficult task of restoring confidence and putting the economy on a constructive path after years of extreme mismanagement which inflicted severe suffering on the population. We are encouraged to read that the government has expressed to staff a clear commitment to maintain critical policies that have already been implemented. We support staff's assessment and the proposal to partially lift the suspension of the Fund's technical assistance to Zimbabwe. However, staff should move cautiously as not enough time has elapsed since the new government took power to fully assess whether a new era of progress has begun.

Given Zimbabwe's capacity constraints, close coordination among international partners is crucial as they prepare for strengthened engagement as warranted by developments in the field. We encourage the Fund to participate actively in existing donor coordination fora and, in particular, to work very closely with the World Bank and the African Bank to avoid overlaps. This applies also to the suggested technical assistance.

Fiscal Policy

The 2009 revised budget contains useful measures to control expenses and to strengthen private sector activity. However, there are downside risks as there is a large potential financing gap that has to be filled, including with revenue measures, capital inflows and donor support, as staff points out. In these circumstances, wage increases should be kept to a minimum. The emphasis must be on restoring public services, utilities, health provision and education. The cash budgeting, targeting a balanced fiscal position on a month-by month basis, supports discipline in difficult circumstances. More flexible budget planning and execution with some medium-term elements should be adopted as soon as possible.

Monetary Policy

A modern economy cannot function without money. Total disregard for the price system and the value of money has resulted in hyperinflation and the collapse of the currency. We share the concerns of Ms. Lundsager and Mr. Kaplan with respect to the management of the RBZ and the need to promptly improve governance in the institution. In the present circumstances some form of dollarization was inevitable. The government's decision to maintain the multicurrency system with the rand as the reference currency seems to be appropriate. Strengthening the accountability and transparency of the RBZ's operations is an essential part of monetary reform. Reintroducing the national currency already at the end of 2009 seems somewhat optimistic.

Structural Reforms

We find the structural reform agenda as described in Mr. Itam's useful Gray, very constructive. These include price liberalization, abolition of the Grain Marketing Board and imposition of hard budget constraints on parastatal enterprises. The need to strengthen the rule of law and to protect property rights, as well as other legislative reforms should be seen as a prerequisite for further progress. Any doubts on political commitment in this area would be detrimental to confidence building and donor support. We urge the authorities to resume payments to the Fund as soon as conditions permit and otherwise to normalize relations with official creditors. Zimbabwe has huge growth potential and rapid economic and social progress will be ensured with improved governance.

Mr. Guerra made the following statement:

We want to thank Mr. Itam for his clear and comprehensive buff statement and the staff for a set of papers. We support the staff's assessment and policy recommendations. Like other Directors, we regard the present circumstances as a turning point in Zimbabwe's institutional and economic prospects. We all concur that the IMF should be present in supporting Zimbabwe to hopefully turn the page and embrace the future. We should continue to follow developments in Zimbabwe closely and increase cooperation with the authorities further. At this critical juncture, as expressed in Mr. Itam's statement, we believe that the government's short-term emergency recovery plan will be instrumental in restoring macroeconomic stability and contain inflation through fiscal discipline and appropriate monetary policy.

Given the expansion of the quasi-fiscal activities that took place in the context of the weak governance of the RBZ, it is important to have a major overhaul of the RBZ's institutional framework before evaluating the option of the return to the use of a domestic currency. In the meantime, the adopted hard currency system, with the rand as the reference currency, will serve the country well. That is why we see the planned annual independent audit as instrumental. The proposed technical assistance engagement should also cover the management and accountability of public enterprises.

We support the request for targeted lifting of the suspension of the Fund's technical assistance. In this regard, we agree with Mr. Prader and Mr. Rottier, and with Mr. Mozhin and Ms. Ustyugova that technical assistance in the area of statistics should be made an integral component of the activities, as highlighted also by Mr. Itam in his statement. We would also like to ask the staff how this technical assistance is going to be coordinated with other IFIs, a point already made by Ms. Agudelo and Mr. Estrella.

Finally, we are certain that the new approach of the government and the strengthened cooperation with the IMF are putting Zimbabwe on the right track to a full integration with the Fund and restoration of all its rights.

Mr. El-Khouri made the following statement:

We thank the staff for the concise papers, and Mr. Itam for a very helpful buff statement. We are pleased that Zimbabwe has now started a new chapter on its economic policy, by taking some very welcome adjustment measures that mark a sharp departure from past policies.

First the monetary reform, without which it would have been impossible to tackle the problem of hyperinflation, is welcome. Second, is the related need for fiscal discipline, because the budget deficit could no longer be monetized. Here, we welcome the commitment to eliminate quasi-fiscal activities and implement cash budgeting. Third, we also welcome the price liberalization measures and elimination of some of the foreign exchange restrictions, which are essential to the recovery of the private sector.

Going forward, we encourage the authorities to reinforce and sustain these reform policies. Such an adjustment effort constitutes the first building block, which the Fund needs to build upon in order to play its catalytic role in mobilizing donor assistance for Zimbabwe.

Finally, we support the targeted lifting of the suspension of Fund technical assistance to Zimbabwe. Like other Directors, we believe that statistics should be included in the technical assistance offered by the Fund, especially because the staff mentioned that there is a direct need for substantial improvement in this area.

With these remarks, we wish the authorities success in meeting the significant challenges lying ahead.

Extending his remarks, Mr. Rottier associated himself with those Directors who stressed the need for improvements in the governance of the central bank. Like Mr. He and Mr. Zhang and Mr. Moser and Mr. Weber, the Board should consider restoring voting and related rights to Zimbabwe as soon as possible.

Mr. Moser pointed out that he had issued a revision to his statement. Instead of asking for an update from the staff on the conditions that the Board had set two years ago to restore Zimbabwe's voting and related rights, as the draft letter had never gone out because the Board had not agreed on those measures, the paragraph was revised to ask instead where management stood on that issue, and how the issue was going to be taken forward.

Mr. Nogueira Batista made the following statement:

I would like to add a few brief comments to what we had in our gray concerning monetary conditions in Zimbabwe. First, we welcome the decision taken by the government in this difficult situation to use the South African rand as a reference currency at this moment. The reasons were given by the staff on paragraph 21, page 13. The authorities' choice is based on optimal currency area considerations and potential significant benefits from regional integration. I would add the fact that, if the government does want to retain the option of reintroducing a sound national currency going forward, this is tactically a better move, because the adoption of the dollar as a reference currency would introduce an element of irreversibility, as in the case of the rand.

I would suggest that the staff does not use dollarization as a shorthand for the use of any foreign currency transactions among residents, because this gives a wrong impression. Before the meeting, the staff told me that about 60 percent of transactions are in dollars, and 40 percent in rand. Moreover, the rand is the reference currency and this is increasing. At first sight, the term "dollarization" gives a wrong impression and I would caution against using that as a shorthand.

The other point that I would like to make is that Zimbabwe is not a small country. It is larger than Poland in terms of geographical area and it has 11 million inhabitants. It is probably a country that can look forward to having its own national currency. I hope that the Fund will be ready to support Zimbabwe, if that is the wish of the authorities. Maybe Mr. Itam will throw some light on that. They have gone through a horrendous monetary experience, maybe it is the highest hyperinflation ever in monetary history, including that of Germany. They need to recover from that. But, the Fund should be supportive if the authorities wish to reinstate a national currency. The preconditions for that are well summarized in the staff report.

Mr. Kaplan made the following statement:

We have a substantial affinity with the tone and substance in the statement of Mr. Legg and Mr. Duggan. When I read their statement, I wish we had also called for the publication of the staff report, and hopefully the authorities will see fit to do that.

On the question of technical assistance for statistics that many Directors have quoted in their statements, Mr. Legg and Mr. Duggan noted that "providing technical assistance in an environment where institutional governance has broken down carries enormous risks. This is particularly true in those areas that fall within the mandate of RBZ. Our support for the proposed IMF technical assistance is on the basis that it will be carefully attuned to these risks and that the staff will update the Board regularly (at least quarterly) on developments. Before we join the consensus to support additional technical assistance for statistics, we would like to hear from the staff where that technical assistance will be directed.

Mr. von Stenglin made the following statement:

> Like other Directors, I welcome that the authorities have implemented many of the staff's recommendations made over the years and in particular during the last review of Zimbabwe's overdue obligations in January. However, for the time being, it seems to me to be at least premature to discuss or consider the restoration of Zimbabwe's voting and related rights as some other Directors have indicated. And the same is true for the question of whether the country would be eligible for HIPC debt relief once arrears are cleared. As Mr. Henriksson stated in his gray, not enough time has elapsed since the unity government was installed to fully assess whether a new era of progress has begun.
>
> Before the Board discusses further steps, we would like to see a credible track record of coherent policy implementation, and continued cooperation with the Fund as well as visible progress toward clearance of arrears to the PRGF/ESF Trust. Given the country's mixed recent history with the Fund and the significant political uncertainty that still remains, it is Zimbabwe's turn to deliver.
>
> Finally, like Mr. Legg, Mr. Horgan, and others, we would see the authorities' consent to the publication of the staff report as a helpful gesture of transparency, which could strengthen the government's commitment to the emergency reform program.

Mr. Daïri joined Mr. El-Khouri and other Directors in their call for the lifting of the restrictions on technical assistance in the area of statistics.

The staff representative from the African Department (Mr. Kramarenko), in response to questions and comments from Executive Directors, made the following statement:

> I would like to answer the questions relating to the macroeconomic outlook and the political context. There was a question on the direction of economic policies and the likelihood of cooperation between the coalition partners. The Movement for Democratic Change managed to get approval of very important pieces of legislation, which shaped the macroeconomic policies for 2009. These include the abolition of the surrender requirement on foreign exchange proceeds, the revised 2009 budget, as well as the recognition of the issues related to the rule of law and the enforcement of property rights. However, forging political consensus on RBZ governance issues, the restoration of the rule of law, and the enforcement of property rights are

challenging tasks, and the prospects for rapid resolution of these issues remain uncertain.

On fiscal policy, some Directors asked about recent developments in revenues and expenditures. Revenues continued to increase in March. As noted in the staff report, revenue amounted to about US$30 million in February, and increased to over US$40 million in March. This is somewhat below the staff's forecast, but it is difficult to make month-by-month projections in the current unsettled environment. On the expenditure side, because revenue was limited to just US$30-40 million per month, the government was only able to pay civil service wages, US$23 million a month, and pension, US$6 million a month, and to make some small payments on current expenses. This means that the accumulation of payments arrears may have increased over the reporting period, which is not good news.

There were a number of questions on assumptions underlying the staff assessment of the revenue forecasts, risks to the staff forecast of the revenue, and potential revenue measures. Staff estimates of the revenue are based on the tax policy decisions, which are reflected in the revised 2009 budget. They do not incorporate any additional measures. We assume that there would be a gradual pickup in economic activity, in particular in the second half of 2009. We also assume that there would be a progressive formalization of economic activity following price liberalization and elimination of most restrictions on current account transactions, which would facilitate tax collection. We also assume a strengthening in revenue administration by the Zimbabwe Revenue Authority, as the authorities are still acquiring experience in collecting revenue in foreign exchange. We also take into account that the schedule for the collection of personal income tax and social security tax is back-loaded, meaning that more is collected by the end of the year than at the beginning of the year. All these factors account for the staff's projection of a gradual pick up in revenue by the fourth quarter of 2009.

It is also worth mentioning that the revenue-to-GDP ratio projected at 25 percent of GDP for 2009 is about the same as it was in 2005 when inflation was around 200 percent, and the revenue base did not erode as fast as it happened in 2007 and 2008.

It is clear that the risks to our forecasts of the revenue are weighted to the downside. The economic recovery is subject to significant downside risks mainly because of political factors. Moreover, the recovery could be undermined or delayed in the absence of external financing and capital inflows early in 2009 and as a result of the fiscal contraction and liquidity squeeze because money creation is generated from abroad. There is also continued uncertainty regarding property rights and the rule of law, and if these uncertainties persist, the ongoing process of formalization of economic activity could be undermined and revenue could be negatively affected. Also, a weaker pace of capacity improvement in the revenue authority may undermine revenue collection. To mitigate these downside risks, the authorities requested Fund technical assistance in the areas of tax policy and administration, and hopefully with the Board approval of technical assistance in this area, the authorities would be able to address the downside risks in a timely manner.

In light of the significant risks to the revenue outlook, the staff encouraged the authorities to implement a number of revenue measures. In light of the abolition of the 7.5 percent surrender requirement of foreign exchange proceeds, the staff advised the authorities to consider raising the royalty on mining companies. In the past, there was an implicit tax, which was collected by the RBZ through the surrender requirement. This implicit tax is not in place currently and the authorities have to rethink the taxation of mineral resources and mining companies. The forthcoming Fund technical assistance will address these issues. We also advised the authorities to broaden the VAT tax base and eliminate the existing exemptions. The Fund's technical assistance will help quantify the revenue impact of these proposed measures.

Several Directors asked about the size of the budget financing gap, and prospects for external financing. The staff identified a budget financing gap of at least US$200 million. For the time being, only South Africa is expected to provide US$33 million for the period of May to July to cover part of the financing gap. No additional resources to cover the budget financing gap have been identified. Regional external financing, in the form of guaranteed credit lines to Zimbabwe's private companies—US$55 million from South Africa and US$70 million from Botswana—is still under discussion. These are very important credit lines, which will help finance the balance of payments need.

In the medium term, the estimated reconstruction needs and the financing gap would require an assessment by many international financial institutions, including the African Development Bank and the World Bank. However, it is evident that US$8.5 billion, which was mentioned in the government economic recovery program, can only be absorbed in the medium to long term because it is a relatively large number compared to the size of Zimbabwe's GDP.

Some Directors asked why the multicurrency system is superior to a peg, and whether South Africa and Botswana were consulted on Zimbabwe's move to the system and how the system will impact monetary operations in these countries. Regarding the advantages of the current system relative to the peg, serious governance problems at the RBZ, the refusal of the public to use the local currency, and the lack of an institutional framework that ensures the credibility of monetary policy and focus on price stability preclude a quick introduction of a national currency. Also, there is no equipment to print high-quality bank notes, which is also an important technical consideration. The Zimbabwean authorities maintain close policy dialogue with SADC countries, including South Africa and Botswana. They presented their short-term economic recovery program to SADC countries, which are fully aware of Zimbabwe's stabilization plans. Regarding the impact of the circulation of the rand on the South African monetary system, Zimbabwe represents only 1 percent of GDP of South Africa, so the impact of the circulation of the South African rand in Zimbabwe is very small, and it is nothing new because the South African rand already circulates in Zimbabwe and in neighboring countries.

There were a number of questions related to technical assistance, and some Directors asked to what extent other donors accommodate technical assistance needs in the area of statistics. There was a capacity building mission of the African Development Bank visiting Harare in April and this mission decided to recommend a capacity-building project in the area of national accounts. So, the African Development Bank is expected to provide technical assistance in the area of national accounts. On the role of the World Bank, and how the Fund cooperates with the World Bank on technical assistance issues and on other aspects of macroeconomic management, the World Bank had a parallel mission with the Article IV mission, and they participated in many meetings with the IMF staff. During their mission, the World Bank staff conducted a rapid review of the public financial management systems and they are expected to provide more technical assistance in this area to ensure that rapid progress is achieved, which is essential for unlocking donor support. The World Bank also plans technical assistance in the areas of public enterprise restructuring and advisory service across certain ministries. More information on Bank-Fund cooperation is provided in the informational Annex.

The staff representative from the Strategy, Policy, and Review Department (Mr. Desruelle), in response to questions and comments from Executive Directors, made the following statement:

> On HIPC eligibility, there are two qualification criteria and one policy requirement in order to benefit from the HIPC Initiative. The qualification criteria are that the country needs to be PRGF-eligible and have a debt level based on end-2004 data that exceeds certain thresholds after full application of traditional debt relief. The policy requirement is that the country adopts a program that is supported by an appropriate arrangement that meets the upper credit tranche standard.
>
> What does this imply for Zimbabwe? It implies that the country goes through a sequence of events to become HIPC eligible. First, the Board will have to restore PRGF eligibility. Then, the staff would have to assess whether the criterion pertaining to the debt threshold is met. Policy progress would also have to be made so that the country can adopt a program that meets the upper credit tranche conditionality standard. The World Bank will have to go essentially through a parallel process.

The Acting Chair (Mr. Kato) made the following statement:

> As regards the point raised by Mr. Moser, the Board will judge the issue of restoration of Zimbabwe's voting rights on the basis of an assessment of policy cooperation on the part of the authorities, and also of the authorities' commitment to reduce arrears to the Fund. Mr. Moser is right that, previously, the letter was not sent out because the required 70 percent of the total voting power majority could not be achieved.
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> So, we will make an assessment whether there is a basis for us to bring the issue of restoration of voting rights to the Board, and at that time we need to have a sense that the 70 percent majority Board support can be counted upon. I reassure Directors that we will assess subsequent developments very carefully, always having in mind the issue of restoration of voting rights.

Mr. Rottier said that he did not understand why Zimbabwe was not eligible for technical assistance in the area of statistics, given that other institutions were offering it. The issue was relevant given that the question was on whether Zimbabwe's external debt would be above the threshold such that the country would be eligible for HIPC debt relief.

Mr. Kaplan noted that, on the question of whether Zimbabwe was eligible for HIPC debt relief, if the Board of Governors passed a resolution on a general allocation of SDRs, Zimbabwe would still receive a portion of SDRs, regardless of its eligibility to use GRA resources or of the restoration of its voting rights. While there were tremendous demands on the ministry of finance for budgetary spending, and total arrears outstanding were more than a question of arrears to the PRGF Trust, Zimbabwe would stand to receive an SDR allocation that was far above their arrears in the PRGF. That would represent one unexpectedly positive benefit that Zimbabwe could take from its relationship with the Fund.

Mr. Moser made the following further statement:

> First, again, on the multicurrency system, I have to admit that I still do not fully understand why the staff would not recommend a full "randization," to not use the term "dollarization," but rather recommend a multicurrency system. Randization would seem to make things much simpler and there is not necessarily a need for the central bank in Zimbabwe, which would, again, solve other problems that are related to governance. Maybe the staff could elaborate on that.
>
> On the issue of the voting rights, I fully agree with Mr. von Stenglin that we all want to see a certain track record, and we all think that it is up to the authorities to deliver. But, we need to be clear about what we expect from them. I think that the Board should tell exactly what it expected from the authorities in order for the voting rights to be restored. So, the concern is that the process is not very transparent, because we do not say exactly what we expect from the authorities, leaving it open and watching the performance of the authorities at one stage and only afterwards deciding to return to this issue. This is the reason why we have raised this issue. We also believe that the best way to promote the rule of law is to adhere to the rule of law ourselves.
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> So, I am still uncomfortable with the suggestion that we just watch developments and then at one point decide that we have now seen enough track record. It seems to me that it would be preferable to have a clear road map and clear expectations as to what we would like to see before we reconsider this issue.

Mr. Daïri sought the staff's comments on the potential cost from the loss of seigniorage associated with the adoption of the rand or other currencies as opposed to the adoption of a national currency. As stressed by Mr. Moser, the road to reestablishment of voting rights should be made clear. It was important to strengthen the hands of the pro-reform faction of the government instead of waiting until the point that the other nonreformist factions would take over, if there was not enough support.

The staff representative from the African Department (Mr. Kramarenko), in response to additional questions and comments from Executive Directors, made the following further statement:

> On the provision of Fund technical assistance in the area of statistics, at this time, the staff has proposed four areas where we believe there is an urgent need for it, taking into account the problems facing the country. We do not envisage the participation of the Statistics Department in these four missions at this stage.
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> That issue could be revisited later in the context of the review of the decision if needed. We believe that the priority now is to ensure the proper functioning of key institutional elements of the government and the central bank before addressing the issue of statistics. The issue of national accounts, which is somewhat different from that of financial statistics, monetary statistics, or fiscal statistics, is handled by other institutions.

Mr. Daïri remarked that the first way to follow developments and assess progress in Zimbabwe was to ensure the reliability of the statistical data, which called for a strengthening of technical capacity.

Mr. El-Khouri supported Mr. Daïri's view and asked how the staff arrived at the indicators in Table 1, what kinds of data were provided by the authorities and whether the staff compiled the data itself.

Mr. Guerra supported Mr. Daïri's and Mr. El-Khouri's views on the staff's need to improve Zimbabwe's technical capacity, if the Fund were to follow developments in Zimbabwe.

The Acting Chair (Mr. Kato) explained that the immediate priorities were to recover from a decline in production, to establish confidence in the macroeconomic system, and to address hyperinflation. Those were the priority areas of technical assistance where the Fund had core competence. They were identified on the basis of consultation with the authorities. The overdue obligations of Zimbabwe would be reviewed by the Board in mid-July. At that time, the issue of technical assistance in the area of statistics could also be discussed, bearing in mind Executive Directors' views and further consultation with the authorities.

Mr. Itam stated that he could not envisage providing effective technical assistance in the four areas mentioned by the staff without the associated assistance for improving the statistics in those four areas. If technical assistance in statistics would be necessary to provide effective technical assistance, it would have to be provided by the Fund. Those four areas fell under the core competence of the Fund, and any other interpretation would be invalid.

The Acting Chair (Mr. Kato) agreed with Mr. Itam that, with respect to the four areas identified for technical assistance provision, to the extent necessary, streamlining statistics was part of the technical assistance provided by the Fund.

The staff representative from the African Department (Mr. Kramarenko) confirmed that that was how it was envisaged. The four areas mentioned in the proposed decision did not necessarily exclude technical assistance pertaining to statistics in any of those particular areas. First, the staff would need to have a diagnostic mission, which would look at the compilation of data at the operational level. If the operational data were of good quality, the staff could move to the next stage.

Mr. Daïri asked whether the Board could modify the decision to include statistics as well.

The Acting Chair (Mr. Kato) asked the Board members to react to Mr. Daïri's suggestion.

Mr. El-Khouri asked whether provision of technical assistance in statistics was excluded because there were not enough resources to devote to Zimbabwe.

The Acting Chair (Mr. Kato) explained that there were vast areas that statistics covered, but the staff needed to have a dialogue with the authorities to identify the areas of immediate and greatest priority, including where technical assistance in statistics was urgently needed.

Mr. Daïri said that the issue was not whether the staff should consult the authorities on the priorities, but rather whether the Board should decide to lift the restrictions on technical assistance in the area of statistics. It would then be up to the staff to consult and discuss with the authorities how the decision could be implemented, and what the priorities were. The Board should at least lift the current restrictions.

Mr. Rottier supported Mr. Daïri's point.

Mr. Itam informed the Board that, during the Spring Meetings, his authorities had discussed the issue with the staff, and they had emphasized the importance of providing technical assistance in the four areas. Zimbabwe welcomed technical assistance in those four areas, provided that the interpretation was clear that statistics would be made an integral part of the technical assistance. If that was not the case, the provision of technical assistance would be useless. If the staff insisted on receiving very clear guidance from the Board in terms of technical assistance in statistics, the authorities would agree with Mr. Daïri taht statistics be made part of the decision explicitly.

The Acting Chair (Mr. Kato) explained that the Board was not asked to take a decision on full restoration of technical assistance provision. The decision for the Board was the resumption of targeted provision of technical assistance. If a majority of the Board wished to include statistics as an area that should be included in the partial resumption of technical assistance to Zimbabwe, that would be up to Board members to decide. In that case, the authorities had to specify what areas of statistics they targeted for technical assistance.

Mr. Itam made the following statement:

> My authorities saw the four areas identified as the starting point, fully realizing that this is opening a window to go ahead. But their understanding is that any technical assistance in the area of statistics associated with these four areas comes automatically. They had a long discussion with the Statistics Department at the Fund and expect the Statistics Department to be an integral part of this exercise. So, we are willing to go along with this arrangement for the time being, as we work toward restoration of the full voting rights of Zimbabwe.
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> But, the answer we have received from the staff did not come out clearly—that technical assistance in statistics required in these four areas will be provided as an integral part of the policy advice. If that is not so, we should consider including statistics generally as part of the decision.

Mr. Daïri stressed that the Board was not going to decide on any technical assistance mission or draw any terms of reference to any mission, but rather to decide on the removal of the restrictions, which should cover technical assistance in statistics in the areas where needed. The Board would send the wrong message to the authorities if it did not underscore the importance of reliable data for monitoring and surveillance purposes.

The Acting Chair (Mr. Kato) proposed to suspend the meeting briefly so that the staff could incorporate Mr. Itam's point into the draft decision.

Mr. Moser asked whether Mr. Itam's understanding was shared by the staff, in which case there would not be a need to make any amendments to the decision. If the staff had a different understanding, an explanation would be useful.

The staff representative from the African Department (Mr. Kramarenko) responded that the proposed decision as drafted did not preclude the possibility of the Fund providing technical assistance in the four areas mentioned in the decision. That was the staff's understanding.

Mr. Itam reiterated his understanding that technical assistance in statistics was included as an integral part of the decision for it to be effective.

Mr. Talbot asked whether, if the Board redrafted the decision on technical assistance, statistics would be specifically included in the decision, or whether the current decision made it implicit that in those four areas all aspects of technical assistance were involved, including statistics.

The Acting Chair (Mr. Kato) replied that, to the extent that statistical assistance was needed for effective, meaningful technical assistance covering those four areas of priority from the authorities' point of view, providing technical assistance in statistics related to those four areas was an integral part of the partial lifting of the restrictions.

The staff representative from the African Department (Mr. Kramarenko) confirmed that the Acting Chair's understanding of the issue was accurate.

Mr. Schilperoort recalled that in the discussion on access limits for low-income countries, a similar issue had arisen where some Directors asked that debt sustainability concerns be included in the decision. In the end, Directors had agreed on having the summing up clearly stating that the Board felt that debt sustainability concerns included the areas mentioned. In the present case, a similar approach could be adopted—the decision would not be changed, but the summing up would make it clear that Directors expected technical assistance in statistics in those four areas.

The Acting Chair (Mr. Kato) expressed hope that Mr. Itam's suggestion could be adopted. On the basis of consultation with the authorities, four areas of immediate priority for Fund technical assistance were identified, and to the extent that providing technical assistance on statistics was deemed necessary to make the provision of technical assistance effective in those four areas, such assistance would be included.

Mr. Daïri noted that the Board was often accused of micro management, but that was not its intention. The Board could just lift the restrictions on technical assistance, and let management and the authorities decide what the priority areas of technical assistance provision should be.

Mr. Kaplan said that he was rather partial to the way the decision was currently drafted.

Mr. Duggan, like Mr. Kaplan, preferred the decision as currently drafted. To the extent that technical assistance in statistics was necessary to make technical assistance in the four areas effective, it should be part of the technical assistance provided to Zimbabwe.

Mr. Bergo shared the same view, preferring the decision as it was drafted, but with the understanding that the Acting Chair had stated. The Fund should move cautiously with restoring its relations with Zimbabwe. Technical assistance should be provided to priority areas and the four areas identified were appropriate. At the same time, decisions on technical assistance were left to the authorities, the Board would be faced with serious capacity constraints, as reflected in the documentation.

Mr. Talbot shared the views of the previous three speakers.

Mr. von Stenglin also supported the decision as it was drafted, accepting the pragmatic interpretation.

Mr. Claveranne noted that he could not see how statistics could be left out of the four areas of technical assistance, supporting the decision as it stood. Mr. Itam should convey to his authorities that there was a clear sense that the Board was trying to help the authorities, by not precluding legally technical assistance on statistics.

Ms. Agudelo endorsed Mr. Claveranne's remarks and further stressed that the summing up should reflect that legal interpretation, if that was the case.

Mr. Itam accepted that interpretation, with the clear understanding that technical assistance in statistics associated with those four areas was part of the package. The summing up should reflect that particular message. If there was no support for lifting the restrictions on general technical assistance, including in statistics, Zimbabwe could accept that for the time being.

Mr. El-Khouri also endorsed that interpretation. The staff report, in paragraph 44, mentioned the areas of statistics where technical assistance would be needed, including the reconciliation of debt data with external creditors. The staff was asked whether the current decision stipulated that the Fund could not help Zimbabwe in that area.

The staff representative from the African Department (Mr. Kramarenko) explained that debt reconciliation issues fell under the framework for the debt sustainability analysis. Therefore, the area department, in cooperation with the Strategy, Policy, and Review Department, would help the authorities in that area.

Mr. El-Khouri wondered whether, under the current decision, Zimbabwe needed technical assistance in the area of statistics to address debt reconciliation issues.

The staff representative from the African Department (Mr. Kramarenko) responded that the efforts of the area department and Strategy, Policy, and Review Department would be sufficient for that specific exercise. Going forward, the Fund would have to improve the compilation of the international investment position and external debt data, and disseminate those data in accordance with the established international best practice. At that point, the Fund would consider technical assistance in the area of statistics.

Mr. Daïri endorsed Mr. El-Khouri's statement, and commented that the provision of technical assistance by area department and Strategy, Policy, and Review Department might be less productive than the more dedicated Statistics Department. It could incur losses in terms of efficiency, staff resources, and optimal advice.

The staff representative from the Strategy, Policy, and Review Department (Mr. Desruelle), in response to additional questions and comments from Executive Directors, made the following further statement:

> I can provide a clarification in regard to the question of whether the staff had already undertaken work to determine whether Zimbabwe would meet the HIPC debt threshold. The short answer to the question is no. The reason is that it is an intensive technical exercise that indeed requires work on reconciliation of external debt data between debtors and creditors. The staff would not want to speculate on numbers before having completed that work.
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> The second part of the answer is that that work is typically performed as part of normal working arrangements between the area department and the Strategy, Policy, and Review Department in the context of debt work, which falls under the mandate of Strategy, Policy, and Review Department, as defined by management.

Mr. Itam made the following concluding statement:

> I would like to thank Directors and the staff for trying to interpret the decision in a pragmatic way. We hope we will be going forward. This is important for Zimbabwe. It is also important for us, the Board, to understand in a reliable way what is going on in Zimbabwe. A few issues were raised. First, on the introduction of a national currency, what my authorities have said is that the present situation of using the U.S. dollar and other currencies, including the South African rand, is viewed very much as an interim arrangement. My authorities have said that they will reconsider this situation by the end of this year, taking into consideration the need to not jeopardize stability that would have been reestablished. They need to provide a very predictable economic environment in order to enhance development and reduce poverty. Therefore, at this point, we cannot say clearly which way Zimbabwe is likely to go in terms of national currency, or whether it will remain under the current regime of using other currencies. So, I would like us

to leave that subject open for the time being. Toward the end of the year, we can look at the pros and cons, establish the benefits and the costs, and then decide the way forward.

On publication of the documents, let me inform the Board that my authorities have given consent to the publication of all the staff papers. I will communicate this to the Secretary's Department.

On the arrears to the Fund, my authorities take this issue very seriously. We have taken note of the suggestions made by Mr. Kaplan in terms of possible use of the SDR allocation that may be forthcoming. We have also taken note of the advice expressed in the grays encouraging Zimbabwe to do its best to at least establish a pattern of paying what has been agreed to. I have indicated in my buff very clearly that the intention of the authorities is to meet the obligations. However, we cannot foresee now how the SDR allocation could be used, especially since it is not clear when that will become effective. In the meantime, we look forward to receiving support from countries that are in a position to help Zimbabwe. It would be useful to examine how we could overcome this serious obstacle, remaining in communication and cooperation with the Fund as well as with the individual member countries.

Governance is a very important item on the agenda of this government. The authorities would like to establish a very transparent system that would be able to evaluate the position and actions of the government, but also one that will clearly reestablish the rule of law, and start reinforcing property rights. These are very important prerequisites for moving forward as some of you may have indicated in your statements. We recognize that.

At the same time, please let us not underestimate the political challenges on the ground in Zimbabwe. Let us not be in such a rush as to dismantle the little progress made so far. So, our appeal is for the Board's patience. We know where we want to go. We cannot disagree with Directors' advice. We ask for Directors' support in moving forward. But, be patient so that we do not lose our footing.

Finally, I am very much encouraged today by the discussion on the voting rights for Zimbabwe. But, I cannot agree more with Mr. Moser who noted that we needed a yardstick to measure Zimbabwe's performance. We will have to consider this. In my view, cooperation with the Fund is the most important yardstick, and I hope today that, after this discussion and after reading the staff report, we all come to the same view that Zimbabwe is fully cooperating with the Fund. Fully cooperating with the Fund in meeting all its obligations, in listening to the Fund's advice, and in achieving the mutual objective of establishing stability and reducing poverty should be the major yardstick by which we judge Zimbabwe in terms of voting rights.

The Acting Chair (Mr. Kato) noted that it was encouraging to hear that the authorities agreed to make the staff report publicly available, which had been suggested by many Directors.

The Acting Chair (Mr. Kato) made the following summing up:

Executive Directors agreed with the thrust of the staff appraisal. A decade of high inflation, severe economic decline, and rising poverty has culminated in an acute, ongoing humanitarian crisis. Directors considered that Zimbabwe is now at a critical juncture. They welcomed the efforts by the recently formed government of national unity to seize the historic opportunity to improve prospects for economic growth and poverty reduction by forging the necessary political consensus among all stakeholders for ambitious reforms.

Directors welcomed the authorities' Short-Term Emergency Recovery Program (STERP) that is based on sound principles of macroeconomic management. They underscored that following through with the STERP's commitment to establish fiscal discipline, eliminate quasi-fiscal activities, maintain a multi-currency monetary framework, and accelerate structural reforms would be essential for an economic turnaround in a low-inflation environment. However, Directors cautioned that downside risks were significant. Potential political instability and limited implementation capacity may undermine reform and stabilization efforts, weakening the prospects for mobilizing donor financial support and attracting private capital inflows.

Directors underscored the importance of establishing fiscal discipline while ensuring the delivery of essential public services. They were encouraged by the authorities' intentions to improve tax administration and review the tax regime to increase budget revenues. Directors emphasized that the budgeted wage bill needs to be maintained and spending pressures from parastatals to finance nonessential activities should be resisted to leave sufficient resources for critical social needs and infrastructure. They also called for rapid progress in strengthening the public financial management system. Given the sizable unfilled financing gap and the necessity to cover critical humanitarian expenses, Directors encouraged the authorities to intensify their efforts to establish workable budget aid delivery mechanisms in close cooperation with the donor community. Directors noted that Zimbabwe is in debt distress and large financing gaps would persist over the medium term even if policies were improved.

Given the circumstances, Directors supported the authorities' decision to anchor inflation expectations by introducing a multi-currency system with the rand as the reference currency. They also emphasized that a significant strengthening of governance and transparency, including through an independent audit, at the Reserve Bank of Zimbabwe is urgently needed to enhance the credibility and durability of recent macroeconomic policies. Directors concurred that reintroduction of the national currency should await the establishment of a credible institutional framework that would underpin central bank operations with a focus on price stability.

Directors noted that banking system issues need to be addressed to improve payment services and access to credit. They underscored that the payments system, banking supervision, and liquidity management would need to be attuned to the requirements of the multi-currency monetary framework.

Directors underscored that the revival of the economy depends critically on quickly attracting private domestic and foreign investors and improving competitiveness. It is essential that the government ensures the protection of property rights, maintains the rule of law, guards against protectionism, and pursues prudent wage and income policies. Directors emphasized that recent commendable efforts to liberalize prices and exchange restrictions for current account transactions needed to be sustained. They also stressed the importance of improving the quality and timeliness of data.

Directors observed that a track record of sound policy implementation, supported by targeted technical assistance, including related statistics, from the Fund and other international financial institutions, is a critical first step to securing donor financial support for the reconstruction of Zimbabwe's economy and regularizing its arrears to official creditors.

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

The Executive Board took the following decision:

Zimbabwe—Request for Targeted Lifting of the Suspension of Fund Technical Assistance

The Fund decides that a partial lifting of the suspension of Fund technical assistance to Zimbabwe is appropriate. Effective from the date of this decision, Fund technical assistance may be provided to Zimbabwe in the areas of (i) tax policy and administration; (ii) payments systems; (iii) lender-of-last-resort operations and banking supervision; and (iv) central banking governance and accounting. This decision shall be reviewed at the time of the next review of Zimbabwe's overdue financial obligations to the PRGF-ESF Trust, and at subsequent reviews as long as Zimbabwe has overdue financial obligations to the PRGF-ESF Trust. (EBS/09/55, 4/22/09)

Decision No. 14327-(09/44), adopted
May 4, 2009

APPROVAL: August 28, 2009

G. RUSSELL KINCAID
Acting Secretary