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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 20/20-1

10:00 a.m., February 24, 2020

1. Zimbabwe—2019 Article IV Consultation

Documents: SM/20/43 and Correction 1; and Correction 2; and Supplement 1; and Supplement 2; SM/20/44

Staff: Leon, AFR; Zettelmeyer, SPR

Length: 1 hour, 21 minutes

Executive Board Attendance

T. Zhang, Acting Chair

Executive Directors	**Alternate Executive Directors**
D. Mahlinza (AE)	
	F. Sylla (AF)
	B. Lischinsky (AG)
N. Ray (AP)	
	P. Fachada (BR)
	Y. Liu (CC), Temporary
	J. Rojas (CE), Temporary
L. Levonian (CO)	
	S. Benk (EC)
	P. Rozan (FF)
R. von Kleist (GR)	
	B.Singh (IN), Temporary
D. Fanizza (IT)	
	K. Chikada (JA)
	C. Sassanpour (MD), Temporary
	P. Al-Riffai (MI), Temporary
	R. Doornbosch (NE)
	J. Sigurgeirsson (NO)
	S. Potapov (RU), Temporary
	R. Alkhareif (SA)
	K.Tan (ST)
	P. Trabinski (SZ)
S. Riach (UK)	
M. Rosen (US)	

H. Al-Atrash, Acting Secretary
E. Tsounta, Summing Up Officer
D. Al-Jarbou / D. Alcantara, Board Operations Officers
L. Nagy-Baker, Verbatim Reporting Officer

Also Present
African Department: N. Hobdari, H. Leon, T. Lessard, F. Queiro Pedroso de Lima, D. Robinson, A. Selassie. Communications Department: A. Kanyegirire. Fiscal Affairs Department: O. Akanbi, R. Allen. Finance Department: N. Westelius. Legal Department: H. Pham. Strategy, Policy, and Review Department: D. Kim, J. Yu, J. Zettelmeyer. World Bank Group: W. Battaile. Executive Director: A. Mozhin (RU). Alternate Executive

Director: A. Guerra (CE), I. Mannathoko (AE). Senior Advisors to Executive Directors: M. Maidi (AE), W. Nakunyada (AE), R. N'Sonde (AF), L. Smith (CO), L. Voinea (NE). Advisors to Executive Directors: A. Abdullahi (AE), A. Arevalo Arroyo (CE), S. Bah (AF), M. Bernatavicius (NO), X. Cai (CC), D. Crane (US), J. Garang (AE), T. Iona (AP), M. Ismail (AE), B. Jappah (AE), R. Makhammadiev (SZ), A. Nainda (AE), K. Nelson (UK), K. Osei-Yeboah (MD), T. Persico (IT), A. Ribeiro Mateus (IT), M. Shimada (JA), D. Susiandri (ST), D. Vogel (AG), A. Zaborovskiy (EC), J. Al Saud (SA), F. Antunes (BR), T. Herold (GR), E. Comolet (FF).

1. ZIMBABWE—2019 ARTICLE IV CONSULTATION

Mr. Mahlinza and Mr. Nakunyada submitted the following statement:

Introduction

Our Zimbabwean authorities appreciate the constructive Fund engagement during the recent Article IV consultations. They broadly share staff's assessment of key policy challenges and priorities.

Macroeconomic conditions in Zimbabwe have continued to deteriorate over the past year, exacerbated by the twin shocks of the severe drought and tropical cyclones experienced in 2019. As a result, economic activity has contracted, and social indicators have deteriorated, with an estimated 8.5 million people (more than half the population) expected to be food insecure in 2020. Meanwhile, subdued exports and limited access to affordable offshore credit lines have compounded the foreign exchange situation, with persistent pressures on the exchange rate and inflation. Against this background, the new government, which assumed power in September 2018, launched Vision 2030 to guide medium term policies aimed to create a competitive and open economy. Consistent with the overarching Vision, they adopted the short-term Transitional Stabilization Program (TSP 2018-2020), to address structural rigidities, restore macroeconomic stability, and accelerate growth.

To support the TSP, the authorities requested a Staff Monitored Program (SMP) which was approved in May 2019. The SMP largely focused on establishing a track record of coherent policies to restore macroeconomic stability and facilitate reengagement with the international community. Despite implementation challenges with the SMP, the authorities remain committed to continued reforms supported by a new SMP, which is currently under negotiation.

Recent Economic Developments

Economic growth declined from 3.5 percent in 2018 to an estimated -8.3 percent in 2019 due to adverse weather conditions which undermined agricultural production and hydro-power supply with downstream effects on manufacturing and mining activity. Concurrently, persistent foreign exchange shortages constrained critical imports required to support productive sectors. Looking ahead, the authorities are optimistic that economic activity will rebound faster, subject to the moderation of weather-related shocks, as well as improved prospects in mining and tourism. Meanwhile, inflation has increased significantly from 42 percent in December 2018 to an estimated 521 percent by end 2019, amplified by the depreciation of the exchange rate, broad money supply growth, and the recent removal of fuel and electricity subsidies.

On the external front, the current account balance is projected to improve from -4.5 percent of GDP in 2018 to -2.5 percent of GDP in 2019 underpinned by a faster decline in imports and growth in remittance inflows. That said, reserve buffers remain below 1 month of import cover, reflecting the cumulative effects of persistent external imbalances over the years.

Fiscal Policy and Debt Management

Since September 2018, the authorities have pursued strict cash budgeting practices, realizing a large fiscal adjustment in 2019. Sustained fiscal consolidation achieved through a combination of revenue enhancing and expenditure containment measures, delivered cash surpluses for the greater part of 2019. At the same time, domestic revenue performance remained impressive on the back of several tax administration measures adopted by the Zimbabwe Revenue Authority (ZIMRA). Other measures being implemented by ZIMRA include an enhanced compliance program focusing on improvements in data matching and integrity, upgrading ICT systems, and strengthening controls. Additional efforts to recover tax arrears and simplify and modernize business processes, are also expected to improve tax compliance, plug leakages, and generate efficiency gains.

On the expenditure front, the authorities' frontloaded fiscal adjustment program has largely focused on containing the public wage bill through restrained wage adjustments. As a result, savings were generated from a 5 percent pay cut in the salaries of senior government officials, rationalization of the civil service, and the limiting of the civil servants 13th cheque to the basic salary. The authorities also introduced biometric verification of civil servants, which is expected to help further contain the wage bill. They also halted expenditure overruns to rein-in the budget deficit and scaled back central bank borrowing.

To further curtail expenditures, the authorities successfully re-set the agricultural financing model in 2019, away from direct government budget allocations, towards lending by private banks. Under the new arrangement, banks are lending to farmers in line with their normal due diligence and creditor scrutiny to minimize NPLs. Further, in the last quarter of 2019, subsidies on fuel and electricity were removed. The authorities are also reviewing the maize meal subsidy for better targeting and prudent management. Furthermore, they have terminated the gold export incentive scheme and replaced it with the Gold Fund, established by the Treasury. This will enhance transparency and minimize the effects of the gold incentives on reserve money and inflation, as the Gold Fund has been established at a much lower cost.

To address the worsening debt dynamics, the authorities are also considering non-debt creating sources of finance for major capital projects. At the same time, government has reduced central bank borrowing from the 20 percent statutory limit to 5 percent of the previous year's revenue, with advances only confined to smoothening short-term cashflow mismatches. Going forward, the resumption of the Treasury Bill (TB) auction system is expected to promote competitive bidding and market pricing of government securities and the eventual reduction of the interest burden.

The authorities view the settlement of exchange losses stemming from the currency conversion implemented in February 2019, as essential to retain the private sector's access to critical off-shore facilities. In this respect, they plan to compensate banks' net operating positions to enhance financial stability. Already, the central bank has completed verification of the external obligations and plans to firm up on repayment modalities. Nevertheless, the authorities concur with staff that the obligations to be assumed by government, remain subject to resource availability and Parliamentary approval.

Monetary and Financial Sector Policies

To anchor inflation expectations and stabilize the exchange rate, the authorities concur that adoption of reserve money targeting (RMT) would be critical. In this regard, the new Monetary Policy Committee is planning to establish monthly reserve money targets consistent with low inflation. Concurrently, the Reserve Bank of Zimbabwe (RBZ) is planning to operationalize the RMT framework through deployment of open market operations tools including Treasury Bills, Savings Bonds, Corporate Bonds, and reserve requirements to support active liquidity management. Consistent with Fund advice, the authorities introduced the interbank market for foreign exchange in February 2019 which allows for the greater role of market forces. They also launched the Reuters Electronic Trading Platform (RETP) to enhance the efficiency of the interbank market. The RETP is expected to promote realistic price discovery and help remove distortions while the market determined exchange rate is expected to help eliminate the need for the gold export incentive.

The banking sector remains generally stable with sustained earnings performance, fairly liquid positions, and reasonably good asset quality. In light of emerging vulnerabilities faced by banks, the authorities recently directed banks to increase their minimum capital requirements. In addition, the RBZ is developing guidance on the implementation of the Basel III capital and liquidity framework to support ongoing measures to enhance the stability and resilience of the financial system. Relatedly, the central bank is in the process of operationalizing the macro-prudential policy framework to improve identification of financial vulnerabilities.

The authorities have also advanced work to implement recommendations of the 2019 Financial Sector Stability Review (FSSR). In this regard, they have made steady progress in strengthening off-site examinations, capacitating the financial stability unit of the RBZ, and revamping the supervisory toolkit. Further, the authorities are currently reviewing the regulatory and supervisory framework to strengthen consolidated supervision, cross-border cooperation, and crisis management.

Satisfactory progress has been made in improving the coverage and usage of the web-based Credit Registry. In parallel, work is advancing to establish a collateral registry for movable assets, which is expected to promote access to credit including by SMEs. The RBZ has also directed banks to appropriately review their risk management systems to mitigate financial stability risks stemming from adverse climate events. The authorities are also pressing ahead with the implementation of the National Financial Inclusion Strategy (NFIS) which was launched in 2016. Under the NFIS, efforts are being made to promote product diversification, innovation and human centered design of financial services and delivery channels, financial literacy, consumer protection, micro-insurance, and support for SMEs. As a result, access to financial services has more than doubled between 2016 and 2019, underpinned by increased access by women, the youth, and SMEs, as well as the opening of low-cost accounts.

Structural Reforms

The authorities are making determined efforts to implement comprehensive structural reforms to promote private sector development and improve the business environment. In this vein, they are advancing work to identify, evaluate, and determine appropriate restructuring models that are suitable for various state-owned enterprises (SOEs). Already, work has commenced to restructure the Grain Marketing Board, re-bundle the power utility company (ZESA), and review government's shareholding in the telephone and mobile phone SOEs. Further, government has earmarked 43 out of 107 enterprises for privatization, liquidation, or merger. At the same time, the Public Entities Corporate Governance (PECG) Act was approved in November 2018, while the Corporate Governance Unit was established in the President's office.

The authorities are at an advanced stage to establish the Zimbabwe Investment Development Authority (ZIDA) which is expected to integrate the various investment-supporting institutions into a one-stop investment shop. In addition, work is advancing to review about 40 pieces of legislation aimed to improve the business climate and enhance the country's investment appeal. On AML/CFT, the authorities are currently addressing deficiencies identified in the 2016 Mutual Evaluation Report, to safeguard the integrity of the financial system.

The authorities are planning to develop a roadmap for the implementation of recommendations of the recent Governance and Vulnerabilities Assessment conducted jointly by the IMF and the World Bank. Meanwhile, progress has been made on governance reforms targeting improvements in individual and media freedoms. In this context, the Public Order and Security Act (POSA) has been repealed and replaced with the Maintenance of Peace and Order Act (MOPA). On the other hand, work to review the Access to Information and Privacy Protection Act (AIPPA) has advanced. Furthermore, the Zimbabwe Anti-Corruption Commission (ZACC) has been reconfigured and capacitated to intensify the fight against corruption.

The authorities attach great importance to ensuring adequate social spending to cushion vulnerable households and creating fiscal space for growth-enhancing public investment. External support, however, remains essential to complement government's efforts to strengthen social safety nets and mitigate the pain of adjustment on vulnerable households. The compression of real wages over the recent past, extreme poverty levels, and the adverse impact of weather shocks, underline the need for stronger social safety nets to avert the humanitarian crisis. Although government has increased budgetary allocations for social assistance, the remaining financing requirements are significant, thereby, underlining the need for donor support to avoid further impoverishment of vulnerable segments of the population. This is particularly important given that the drought conditions are expected to persist into 2020.

Conclusion

The authorities acknowledge the pressures exerted by high money supply growth on inflation and the exchange rate in the past year. Going forward, they are determined to rein-in monetary expansion while pursuing further fiscal consolidation. At the same time, they remain committed to reforms under a Fund supported SMP, which remains a critical step towards amicable resolution of the country's debt arrears and re-engagement with the international community. They are determined to implement corrective measures including through sustained fiscal consolidation and supportive monetary and structural reforms. They however, require support from the international community to sustain reforms, alleviate poverty, and ensure food security. That said, the authorities remain optimistic that the Fund can help explore more innovative ways to assist them overcome attendant challenges. They look forward to continued Fund engagement and technical support to sustain the reform momentum.

Mr. Rosen, Ms. Pollard and Ms. Crane submitted the following statement:

We thank staff for the reports and Mr. Mahlinza and Mr. Nakunyada for the buff statement. We welcome this overdue opportunity to discuss Zimbabwe's Article IV review. Tentative initial progress on fiscal consolidation under the Staff Monitored Program has unraveled from the second half of 2019, with partial implementation of reforms that required full discipline, massive quasi-fiscal operations and a newly-revealed gold incentive scheme. We urge the authorities to implement transparent, market-based economic reforms with social protections, underpinned by the political reforms necessary to restore the confidence of the international community. We regret the devastating impacts on the people of Zimbabwe resulting from a combination of failed economic policies and partial reforms, continued corruption, and natural disasters. We view staff's baseline scenario, which assumes steady implementation of reforms, as optimistic. We are not convinced that the authorities are committed to take the coordinated fiscal, FX and monetary policy measures necessary to stabilize the economy. We agree with staff on the imperative of addressing rising food insecurity, which will require the authorities' effective cooperation with international humanitarian donors and effective agricultural sector reforms.

Monetary and Exchange Rate. The authorities' gradual approach to reforms is unlikely to stem the inflationary spiral. The authorities do not seem to have a timeline or sense of urgency about moving to restrict reserve money in order to arrest the collapse of the Zimbabwe dollar. Similarly, the current gradualist path on FX market liberalization appears to be resulting in FX scarcity and opportunities for corruption rather than supporting liquid FX markets to facilitate critical imports. Immediate action to publish the daily RBZ balance sheet with a one-week lag and full monthly monetary statistics with a four-week lag, the minimum called for by staff, would be a good start.

Fiscal. We underscore staff's call for more decisive reforms of agricultural support programs, elimination of RBZ quasi-fiscal activities, and limits on the assumption of private losses related to currency reform. While the agricultural support system, which has been costly and produced scant results, is now financed through a public-private partnership with banks, government guarantees remain troubling. As the SIP points out, government support schemes have encouraged rent-seeking rather than agricultural productivity. Furthermore, while staff has called for an end to quasi-fiscal activities by the RBZ, including lending to its subsidiaries, we did not see a commitment in this regard in the "Authorities Views." We are also concerned by the scale of private losses from the currency reform — on the order of 10 percent of GDP — and news reports of the RBZ approving payments of legacy debt. The staff report notes that the authorities have been taking on debt collateralized against future gold and platinum exports and we join staff in calling for its full transparency. Can staff comment on how confident they are in the comprehensiveness of the debt figures in the DSA and where the potential blind spots may be?

Governance. We welcome the annex on priority governance and corruption challenges and call on the authorities to publish the full governance report. Endemic, high-level corruption is an important driver of economic mismanagement, from the highly unusual RBZ loan discount that derailed the SMP to the untold millions lost under costly, ineffective Command Agriculture schemes. A robust set of governance and anti-corruption measures is essential to the success of any reform program.

Financial Sector and AML/CFT. Financial sector risks, including banks' exposure to untraded government debt, should not be ignored. We echo staff in calling for close monitoring of weakly capitalized banks and elevated NPLs, an asset quality review, and a strategy to address capital shortfalls. On AML/CFT, we note the authorities' progress in addressing technical deficiencies, notably with respect to customer due diligence. However, implementation lags far behind legislative progress. The authorities should redouble efforts to effectively implement FATF standards, in particular: 1) improving risk understanding among supervisors and reporting entities; 2) enforcing reporting and monitoring standards of reporting entities; and 3) fully implementing UN Security Council Resolutions on terrorism and proliferation financing.

Mr. Bhalla and Mr. Singh submitted the following statement:

We thank the staff for their informative reports and issue papers and Mr. Mahlinza and Mr. Nakunyada for their helpful buff statement.

Notwithstanding severe climate-related shocks, crippling growth and consequent humanitarian crisis and economic distress, we truly appreciate the authorities' efforts in undertaking structural reforms, including a beginning towards reforming the exchange rate regime, containing fiscal deficit and institution of a Monetary Policy Committee.

We understand that government deficits, financed predominantly by the central bank have led to a rapid expansion in base money and thus fueled inflation. This adverse feedback loop of higher inflation and greater exchange rate depreciation seems to have entrenched. Responding to these challenges, the authorities have undertaken substantial fiscal adjustment which has significantly brought down fiscal deficit in 2019 over the level of 2017. The concern, nevertheless, arises from predominant monetary financing of deficits in the absence of adequate tax revenues and external official support. We agree that restraining deficit financing from the central bank becomes a precondition for stabilization of hyper-inflation and sharp erosion of the external value of currency. We concur with the Staff that given Zimbabwe's large external arrears and ineligibility for traditional debt relief mechanisms like HIPC, there is a need to build and reach consensus on affordable solutions to debt overhang. Since the sizeable outstanding arrears are seriously hampering the eligibility for traditional debt relief schemes and discouraging private creditors and the donors, we would like to know the strategy to deal with such arrears.

As an interim arrangement to tackle high inflation, we support the staff advice on switching to reserve money targeting as the possible nominal anchor. We appreciate that the central bank and the newly established Monetary Policy Committee expressed determination to establish monthly reserve money targets consistent with low inflation with a moderate (10-15 percent) targeted increase in reserve money planned in 2020. Alongside, we support the Staff suggestion for FX reforms and greater exchange rate flexibility. On the financial sector, it seems that loan performance has improved helped by the sale of nonperforming loans to the

Zimbabwe Asset Management Corporation (ZAMCO) during 2015-2018 and declining debt payments in real terms in 2019. Despite this, the past dues of the banking system have remained significantly high since 2014. We would like to invite the staff comment on the success of the AMC and the improvement in the repayment climate.

Any macroeconomic adjustment during a cyclical downturn is likely to impose disproportionately higher adjustment cost on an economy in the near term. More so in fragile and conflict affected states as the large part of population is displaced and economically vulnerable, the Fund advice on major structural adjustments should be cognizant of the potential social backlash, which may ultimately compromise the credibility of the reform process with public at large. Given that the social assistance spending in Zimbabwe is way below its Sub-Sahara African peers and the LICs, we believe that strong adjustment programmes should be preceded by well-designed and targeted social safety net in order to protect the vulnerable population.

We wish the authorities all the success in bringing the economy back to a sustainable growth path and in their endeavor to overcome the humanitarian crisis.

Mr. Beblawi and Ms. Al-Riffai submitted the following statement:

We thank staff for their detailed report and Mr. Mahlinza and Mr. Nakunyada for their informative buff statement. Zimbabwe is facing a humanitarian and economic crisis, exacerbated by policy missteps. The current administration has adopted an agenda focused on macro stabilization and reforms. We welcome staff's engagement with the authorities and concur that coordinated fiscal, exchange rate, and monetary policies are a near term imperative to stabilize the economy, whilst addressing food insecurity. We agree with staff appraisal and have the following issues to highlight.

In the presence of significant financing constraints, the authorities have made notable efforts to tighten the fiscal stance, contain the monetization of the deficit, and help stabilize the economy. Though we welcome that the 2020 budget approved by Parliament is anchored around eliminating central bank financing, we note that in staff's view, the ambitious revenue targets may not be met. We are reassured by the authorities' commitment to delay execution of some allocations in the 2020 budget (whilst protecting social spending), until there is greater clarity on revenue outcomes and the availability of domestic financing. We would appreciate staff's comments on which potential revenue items the authorities expect may fall short of their targets. However, we are concerned that staff estimates of the financing needs do not include the additional funding needed to close the humanitarian funding gap. Zimbabwe's critical humanitarian and economic situation restricts revenue mobilization through tax policy reforms. We urge the authorities to eliminate the Reserve Bank of Zimbabwe's (RBZ) monetization of the budget, contain the fiscal implications related to the currency reform losses, and refrain from engaging in collateralized external borrowing.

We take positive note of the authorities' efforts to address weaknesses in the monetary framework and the exchange rate market, including by introducing a new domestic currency, creating an interbank foreign exchange market, establishing a new monetary policy committee, and increasing transparency of the RBZ. Nonetheless, we note that progress has been uneven and confidence in the new currency has not been restored, despite the tightening in fiscal policy. We concur with staff's advice that reserve money targeting would be the optimal anchor, at this time, for the new currency and see merit in the introduction of short-term instruments to allow the RBZ to conduct open market operations to facilitate the process. We also see a need to proceed with currency reforms to establish a well-functioning market, including by continuing the liberalization of foreign exchange controls and enhancing measures to de-dollarize the economy.

The banking sector's resilience has been aided by administrative measures and the government's commitment to compensate banks for foreign exchange losses. However, the capacity of the banking sector to support growth has been reduced, since private sector credit as a share of GDP shrank for the fifth consecutive year. Though we sympathize with the authorities' motivation to support bank credit to the productive sectors, we concur with staff that it raises contingent liabilities for the government and de-incentivizes banks to effectively manage credit risk. We welcome the authorities' stated commitment to addressing the gaps in financial sector supervision and financial stability frameworks based on the recommendations of the Financial Sector Stability Review. We see merit in conducting an asset quality review and strengthening the AML/CFT framework. Zimbabwe has achieved one of the highest usage levels of innovative payment products (mobile payments) in the region and we welcome the positive impacts that has had on financial inclusion. Can staff shed light on the efficacy of the underlying regulatory infrastructure required to minimize associated cybersecurity risks?

Climate shocks have had severe humanitarian and economic impacts on Zimbabwe, as a result of drought and Cyclone Idai. The agriculture, energy, and mining sectors, along with associated livelihoods, are adversely affected, making 60 percent of the population food insecure. The authorities' lack of financing severely limits their ability to respond to the humanitarian crisis and meet reconstruction and development spending needs. We see a crucial role for the international community to help close this financing gap. Can staff comment on whether there is a national integrated plan to address climate risks in Zimbabwe?

The Zimbabwean authorities have stated and shown their commitment to stabilization. However, in addition to financing, they will need the necessary expertise from IFIs and development partners to build national capacity. We, therefore, welcome the joint World Bank and IMF technical assistance program for 2020-21 that aims to provide the necessary expertise and help the authorities in their efforts to stabilize the economy.

Mr. Tan and Ms. Susiandri submitted the following statement:

We thank staff for the comprehensive set of reports and Mr. Mahlinza and Mr. Nakunyada for their insightful buff statement. The authorities have embarked on an ambitious package of economic reforms to address macroeconomic instability, but progress has been mixed and hampered by climatic shocks. This has placed Zimbabwe in an economic and humanitarian crisis that will require difficult policy choices from the authorities, and support from the international community, to navigate the significant challenges ahead. Against this backdrop, we are encouraged that the authorities remain committed to reforms under a Fund-supported SMP. We agree with the broad thrust of staff's assessment and offer the following points for emphasis.

Urgent fiscal adjustment is imperative to restore macroeconomic stability. We note with concern the expected financing gap in the 2020 budget and the humanitarian funding gap for social protection needs, as well as the apparent lack of credible measures to close these gaps realistically. While we welcome the authorities' commitment to anchor the budget on zero RBZ financing, we agree with staff on the need to further explore decisive expenditure measures and coordinated outreach to the international community in anticipation of the revenue shortfall. We also welcome the authorities' commitment to delay some budget execution until there is greater clarity on revenue outcomes and availability of domestic financing, while protecting social spending. On the elimination of quasi-fiscal activities by the central bank, we note from the buff statement that the authorities have terminated the gold incentive and replaced it with the Gold Fund. We welcome staff’s view on the new scheme and the likely fiscal implications. We also share staff’s recommendations on debt management reforms and to avoid continued recourse to collateralized external borrowing on commercial terms. Could staff elaborate the magnitude of such borrowing for Zimbabwe?

We concur with staff that reserve money targeting (RMT) is the most appropriate anchor at this current juncture. We also agree on the need to step up efforts in establishing adequate instruments to operationalize the RMT and welcome staff’s elaboration in the Selected Issues Paper (SIP). Efforts to enhance open market operations (OMO) should be carefully undertaken, particularly in determining the true price for OMO, with due consideration for potential adverse effects on exchange rate and interest rate volatility. With respect to the importance of eliminating central bank financing, including direct lending to its subsidiaries, we note the authorities’ intent to continue limiting the amount of fiscal financing in the domestic market. On the exchange rate policies, we welcome staff’s recommendation to continue to liberalize the FX market. At the same time, we acknowledge the authorities’ preference for a gradual and deliberate approach to limit the pass-through effects to inflation.

Financial sector reforms should be the top agenda to preserve financial sector stability. Although the banking sector has shown resilience, this is supported by administrative measures and government support rather than underlying fundamentals. On the overstatement of banks’ ability to provide credit and meet deposit withdrawals, we welcome staff’s comments on the potential impact and mitigating measures if the administrative measures were removed. We share staff’s view on the urgency for reforms and welcome the authorities’ commitment and progress to address gaps consistent with the recommendations of the 2019 Financial Sector Stability Review.

The authorities should accelerate governance and structural reforms to improve the business environment and support sustained and inclusive growth. We welcome the steps taken to address governance vulnerabilities and encourage the authorities to step up their efforts in close collaboration with the Fund and the World Bank. Given that agriculture is the main driver of the economy, we also support the staff recommendation to conduct reorientation and rationalization of fiscal agricultural support program, along with legal and policy reforms as laid out in the SIP.

Mr. Mojarrad and Mr. Osei Yeboah submitted the following statement:

We thank staff for the well-written set of papers and Mr. Mahlinza and Mr. Nakunyada for their insightful buff statement. We broadly concur with staff appraisal and offer the following comments for emphasis.

In a fragile environment and despite climate shocks, the new government has made notable progress to restore macroeconomic stability and reduce distortions. The authorities have launched the ambitious Transitional Stabilization Programme (TSP) aimed at correcting macroeconomic imbalances, boosting growth, and enhancing human development. However, economic growth remains subdued, fiscal deficit has declined, but still high, and the hyperinflation is still protracted. While noting the significant downside risks to the outlook, appropriately balanced policy mix and strengthened cooperation with the Fund will improve macroeconomic prospects, boost the business climate, and enhance the recovery. Noting that Zimbabwe lags regional peers in attracting FDIs, the private sector channel presents a viable option to bolster export diversification for inclusive growth.

The fiscal position is still a work-in-progress after some tightening effort by authorities. This is underscored by the continuing high debt and deficit, diminished buffers, and financing by monetization. Policy should therefore focus on further consolidation to restore macroeconomic stability and create buffers for pro-poor and pro-growth spending, while at the same time being alert and reactive to the adjustment cost on vulnerable groups. We welcome the recently introduced financial intermediary tax and the increase in fuel excises and encourage the authorities to explore further revenue measures to preserve fiscal sustainability. We agree with staff that spending rationalization holds better prospect for closing the deficit gap in the context of the significant humanitarian situation and economic contraction. That said, strengthening public financial management (PFM) by enhancing fiscal governance transparency while eliminating non-priority subsidies will help to restore fiscal discipline.

Monetary policy should strengthen the disinflationary path and support exchange rate stabilization. To this end, we support the recommendation on reserve money targeting framework for monetary policy implementation, which must be underpinned by a market-based instrument for the conduct of open market operation. Monetary reforms must also eliminate deficit financing, bolster central bank independence, credibility and communication to help the transmission of policy objectives. We encourage the authorities to pursue a path of FX flexibility, which will hopefully remove policy restrictions on interbank transactions and contribute to de-dollarize the economy.

A strong, stable, and resilient banking sector is pivotal to anchor increased private sector participation in economic development. In this context, we welcome the authorities' administrative directives and commitment to compensate banks for FX losses. While this has fostered a stable low-cost funding, transitioning to a more market-oriented FX trading will bode well for the longer-term sustainability of the sector. Ensuring that banks have healthy balance sheet will also help ensure better transmission of confidence and improve intermediation. We take positive note of the authorities' commitment to align reforms to the recommendations of the 2018 financial sector stability review, notably upgrade the legal framework, the supervisory toolkit, and the payment system to enhance financial sector stability and resilience. Developing a new bank liquidation framework with appropriate triggers to guide RBZ in the event of bank resolution will strengthen the financial system further.

Improving governance, transparency, and investor friendly environment should remain the centerpiece of structural reforms which will help strengthen Zimbabwe's external position. To this end, Zimbabwe's stated commitment and close collaboration with the IMF and the World Bank to address governance vulnerabilities and improve the business environment is commendable. Steps to reduce SOEs financial burden on the budget and implement an effective agricultural support system that is aimed at improved infrastructure and land reforms will promote inclusive growth and poverty reduction. We take positive note of the authorities ongoing steps to address AML/CFT deficiencies identified in the 2016 mutual evaluation report as indicated by Mr. Mahlinza and Mr. Nakunyada.

With these comments, we wish the authorities all the success in their endeavor.

Mr. Benk and Mr. Zaborovskiy submitted the following statement:

We thank staff for the informative papers, and Messrs. Mahlinza and Nakunyada for their helpful buff statement. Unsustainable economic policies, on the backdrop of severe climate shocks, have led to a dire economic and humanitarian situation in Zimbabwe. We regret that the staff-monitored program, adopted in May 2019, went off-track as the authorities failed to deliver on their commitments, resorting to the monetary financing of the fiscal deficit. We agree with the thrust of the staff appraisal and call on the authorities to return the much-needed macroeconomic adjustment on track, and accelerate the structural and governance reforms, as well as the fight against corruption.

Restoring macroeconomic stability through coordinated fiscal and monetary tightening remains vital. The critical first step in this direction is the adoption of a realistic budget. We are concerned about the fiscal gap of 3.8 percent of GDP, or ¼ of spending in the 2020 budget, according to staff's estimates. We caution the authorities against monetizing this deficit and urge them to develop a robust macroeconomic policy package which can be potentially supported by external donors and unlock the resources of domestic stakeholders. The budget rebalancing should be based on broadening targeted social assistance, while reducing inefficient subsidies and non-priority current expenditures. Like staff, we encourage the authorities to accelerate the debt reconciliation, avoid non-concessional borrowing, and increase debt and budget transparency. These measures are vital to start finding a mutually agreeable resolution to Zimbabwe's debt overhang with external creditors. The continued recourse to collateralized external borrowing on commercial terms may potentially complicate any future arrears clearance operations for Zimbabwe, so it should be avoided. We call on the authorities to carefully and transparently assess private sector losses related to the currency reform before assuming any obligations. Could staff further elaborate on these losses and the legal provisions justifying their compensation?

The monetary financing of the budget deficit and the central bank's quasi-fiscal operations should be discontinued to combat hyperinflation. Due to the uncontrolled increase of the money supply, inflation has rocketed to 521 percent at end-2019. The continued monetization of the deficit would further damage the growth potential and depress the economic recovery. To rebuild the monetary system, reserve money targeting should be introduced, consistently applied, and supported by the fiscal policy. We urge the authorities to speed up the introduction of short-term, market-rate-determined monetary policy instruments to advance open market operations. We welcome staff's comments whether there are any capacity constraints to do so. We stress the importance of enhanced central bank transparency, as well as the disclosure of the information critical for market participants in the first place: monetary statistics. Regarding the financial sector, we echo staff's call to speed up the reforms which are essential to preserve financial stability, including strengthening banking supervision, conducting an asset quality review, advancing the bank resolution and contingency planning, and bringing the national payment system regulation in line with international standards.

Substantial progress is urgently required in firming up Zimbabwe's AML/CFT framework.

On the structural front, we urge the authorities to accelerate reforms to address weaknesses, including in the judicial system, the fight against corruption, and the protection of property rights in line with best practice. We also support the emphasis on reforms in the agricultural sector. Gradually giving agricultural land to private hands has a potential to spur investment and productivity, while improving the regulatory environment will help create a level playing field.

From the buff statement, we learned that the authorities are determined to implement corrective measures, including through sustained fiscal consolidation and supportive monetary and structural reforms. In this regard, we encourage them to proceed steadfastly with this agenda. We would also welcome staff's comments on the next steps in the Fund's further engagement with Zimbabwe.

Mr. Alkhareif, Mr. Chikada, Mr. Keshava and Mr. Shimada submitted the following joint statement:

We thank staff for their comprehensive report and Mr. Mahlinza and Mr. Nakunyada for their informative buff statement. Zimbabwe is experiencing an economic and humanitarian crisis. It is regrettable that the authorities' fiscal consolidation efforts are overshadowed by their uneven implementation of policy reforms, especially the delays and missteps in FX and monetary reforms, which has put the Fund's Staff Monitored Program off-track. In this regard, a harmonized mix of fiscal, monetary and FX policies as well as re-engagement with the donor community are paramount to break the vicious cycle and hopefully be a good starting point for Vision 2030. As we broadly concur with the thrust of the staff appraisal, we would like to offer the following comments for emphasis.

Fiscal consolidation needs to continue to avoid further central bank quasi-fiscal activities while preserving social spending for the most vulnerable segments of the population. In this context, we welcome the authorities' consolidation efforts in 2019, but regret base money has been increasing due to central bank's quasi-fiscal activities. At the same time, we note with concern staff estimates of a fiscal financing gap of about 3.8 percent of GDP in 2020, and agree with staff that reprioritization of spending should be considered to close the gap without central bank's finance. In this regard, could staff elaborate more on how the authorities could avoid central bank financing while maintaining social spending to support the vulnerable, considering the funding gap on required social spending?

The RZB's autonomy is warranted as a precondition for effective monetary policy, given Zimbabwe's unfortunate history of monetary finance and hyper-inflation. As for monetary policy framework, we welcome the staff's detailed analysis in the Selected Issues paper and concur with the recommendation that quantitative monetary targeting is a feasible option to stabilize inflation at the current juncture. Noting that mobile payments have been significantly increasing in the country, could staff elaborate on the potential ramifications to inflation dynamics?

FX reforms need to be promoted in a determined manner. We understand the authorities' preference for a gradual approach for the FX liberalization, considering the spillover effect to inflation. At the same time, we see merit in staff's recommendation that any subsidies should be through the budget and not through preferential FX rates to ensure transparency.

Financial sector vulnerabilities warrant closer attention. We note with concern staff's evaluation that reported prudential ratios overstate banks' ability due to holdings of illiquid long-term government bonds. We encourage the authorities to conduct an Asset Quality Review of the banking sector to comprehend each bank's situation in detail, as well as finalizing legal and regulatory framework. We also emphasize the importance of improving the effectiveness of the AML/CFT framework to exit from the FATF list and help mitigate pressures on correspondent banking relationships.

In the medium- to long-term, structural reforms to improve business environment are important to enhance potential growth and needs to be promoted. We welcome staff's analysis of the agricultural sector in the Selected Issues paper and encourage the authorities to advance agricultural reforms to support growth and poverty reduction. Efforts to address governance vulnerabilities should continue.

Last but not least, re-engagement with international community is indispensable. While we welcome the Fund engagement in the country through the well-targeted TAs shown in the country's capacity development strategy, the re-engagement with other international institutions and donor countries are critical for the country's sustainable development. In this regard, we have concern regarding the continued recourse to collateralized borrowing and the authorities' assumption of the liabilities from losses associated with the currency reform, both of which would make debt negotiation, which is the precondition of the re-engagement, further complicated. We urge the authorities to accelerate their efforts to resolve the prolonged external arrears. Considering that Zimbabwe is not eligible for traditional debt relief mechanisms such as HIPC and MDRI, could staff elaborate on the potential Fund role to coordinate debt relief discussions with donor countries, when the authorities show a strong commitment?

Mr. Ray and Mr. Iona submitted the following statement:

We thank staff for the set of reports and Mr. Mahlinza and Mr. Nakunyada for the useful buff statement. We broadly concur with staff's appraisal and recommendations and will limit our comments to the following.

While we acknowledge some efforts by the authorities in implementing certain policy interventions, we are concerned with the costly missteps and slippages in the SMP on fiscal and monetary policy and on FX market reforms. Against a backdrop of multifaceted economic challenges, climate shocks in 2019 amplified the fiscal adjustment costs, leaving more than half the population food insecure. Going forward, the authorities are faced with the daunting task of tightening monetary policy, to ease hyperinflation pressures, and contain the fiscal policy to address the macroeconomic imbalances, while making sure the disruptive impacts are mitigated. In this regard, we welcome the authorities' intention to engage in a new SMP as mentioned in the buff statement. This would be an opportunity for the authorities to renew its commitment to the implementation of the Vision 2030 and advance reengagement efforts with the international community.

Staff's proposed near-term macroeconomic policy mix to stabilize the exchange rate and inflation seems sensible. These policies have the added potential advantage of supporting the normalization of external arrears with official creditors. In that regard, we encourage the authorities to take decisive measures to contain expenditures, including careful judgment on the assumption of private losses related to the currency reform. In the current circumstances, we are convinced that fiscal consolidation is a critical precondition to avoid further monetization of the deficit, lessen the pressure to recourse to collateralized external borrowing, and boost debt sustainability restoration efforts. On monetary policy, we concur that money targeting is currently the preferred anchor given the high inflation situation, facilitated through open market operations. We strongly support staff's recommendation to further liberalize the FX market and eliminate multiple currency practices to support the monetary targeting framework.

Despite the good progress made on structural reforms under the SMP, the business climate remains challenging. This underscores the need to urgently address governance bottlenecks and improve the business environment. While new legislation is in place to tackle corruption, more efforts are needed on consistent enforcement. We welcome the recommended shift of fiscal resources in the agricultural sector from the provision of private goods to the provision of public goods. Can staff comment on the political appetite for such a paradigm shift in policy and how would transitory costs be mitigated?

We acknowledge the well-thought-out CD strategy for 2020 which is grounded on the FSSR findings and current SMP objectives. We are fully supportive of this continued heavy CD engagement. While we note that Zimbabwe's fragility could complicate CD delivery, we stress the need for strong ownership by the authorities to ensure traction and successful implementation of CD. Staff comments regarding CD ownership in Zimbabwe are welcome. Noting the significant gaps in reforms and previous AIV advice, what were the key lessons learned from past engagement that would improve traction of future CD delivery?

Ms. Liu and Ms. Cai submitted the following statement:

We thank staff for the comprehensive reports and Mr. Mahlinza and Mr. Nakunyada for their helpful buff statement. Zimbabwe has faced hard times since the early 2000s, with only a brief period of recovery between 2009 and 2012. Food shortages, high inflation and power outages have reached critical levels. Even though various measures have been taken during the past year or so to enable macroeconomic stabilization, the country is yet to turn the corner. This is in part because Zimbabwe has been hit by multiple shocks such as droughts, foreign exchange shortages and the Cyclone Idai. More efforts are needed to push forward with reforms and strengthen the cooperation with the Fund. We broadly agree with the thrust of the staff appraisal and would limit our comments as follows.

Strengthening public finance management framework and improving domestic revenue mobilization are crucial to maintain macroeconomic stability. We share staff's concern that the 2020 budget approved by Parliament is based on ambitious revenue and financing assumption. We take note in Table 3a that non-tax revenue and grants in the 2020 budget would be ZWL$2.18 billion, which significantly increases from the previous year. Of the ZWL$2.18 billion, how much is grant money and have the grants been fully confirmed? Do the authorities have any remedial measure in case of grant shortfalls? It is encouraging to see that the authorities are implementing expenditure controls. At the same time, more efforts are needed to broaden the tax base and reduce non-priority spending. But spending on education, health and infrastructure should increase as fiscal space is enhanced. Zimbabwe is in debt distress with large and longstanding external arrears to IFIs, official and commercial creditors. We encourage the authorities to double their efforts to find an agreeable debt restructuring plan with external creditors and begin to clear the arrears at the IFIs.

Tight monetary policy is crucial to contain high inflation and FX reforms should be pushed forward. Reserve money rose sharply in the second half of 2019 owing to the resumption of quasi-fiscal operations by the Reserve Bank of Zimbabwe (RBZ) and distortions in the FX market that remain significant. We see merit in reserve money targeting a regime and associate ourselves with staff that the framework should be implemented flexibly to incorporate other factors, including expected inflation and exchange rate developments. Could staff elaborate to what extent the high inflation reflects the pass through from the higher-than-expected depreciation of the ZWL$?

More needs to be done to maintain financial stability and enhance financial intermediation. Zimbabwe has achieved one of the highest usage levels of innovative payment products, including mobile payments in the region, which significantly increase the financial inclusion of underserved communities. Relevant regulatory requirements should also be stepped up to prevent potential risks rising from this area. We join staff to encourage the authorities to conduct an asset quality review to gauge banks' capital positions and prepare contingency plans should capital shortfalls be detected in the review. Further measures to enhance financial infrastructure and improve the business climate are also needed to address remaining gaps in the financial sector and improve compliance of the AML/CFT frameworks.

Eliminating bottlenecks to growth is essential to sustained economic recovery and social inclusion. Structural reforms should be pushed forward in the agricultural sector, including a reorientation and rationalization of fiscal agricultural support programs. We take positive note that the authorities are committed to publish their final assessment of governance vulnerabilities and their high-level anti-corruption plan which will feed into a comprehensive anti-corruption strategy for Zimbabwe. We encourage staff to continue providing technical assistance in this respect in collaboration with the World Bank.

We are glad to see that despite implementation challenges with the SMP, the authorities remain committed to continued reforms supported by a new SMP, which is currently under negotiation. Could staff elaborate more on the experiences and lessons learned from previous SMP?

With these remarks, we wish the authorities every success in their policy endeavors.

Mr. Sigurgeirsson and Mr. Bernatavicius submitted the following statement:

We thank staff for the informative set of reports and Mr. Mahlinza and Mr. Nakunyada for their helpful buff statement. Zimbabwe is experiencing an acute humanitarian crisis, as more than half of the population is food insecure after policy missteps and major climate shocks. Addressing severe macroeconomic imbalances and re-engaging with the international community to gain access to financial support should be guiding policy priorities going forward. We generally concur with the staff appraisal and would like to provide a few additional points for emphasis.

Monetary reforms should be key items on the reform agenda. After significant monetary policy missteps, inflation has jumped sharply to 521 percent at end-2019. We agree on the need for determined measures on currency reform through steps to liberalize FX controls, including elimination of the priority list. In addition, we encourage the authorities to enhance disclosure of monetary statistics and strengthen the autonomy and the mandate of the central bank (RBZ). We welcome the progress achieved in containing monetary financing of the deficit, but note with concern, that quasi-fiscal operations by the RBZ continued during 2019. We support staff's view, that reserve money targeting (RMT) is the best feasible monetary anchor considering current circumstances.

We note the fiscal consolidation that has taken place in recent years, which has brought the government wage bill back towards an improved position. We support staff's recommendation on the need to further scale back low-priority spending and strengthen the social safety net, as social outcomes lag significantly behind peers. The 2020 budget is based on very ambitious assumptions, which could result in a fiscal financing gap of about 25 percent of planned spending, according to staff estimates. In the context of the humanitarian crisis and economic contraction there are no obvious tax policy reforms that could generate the additional revenue needed to close the gap. Therefore, we support staff's recommendation to contain spending on inefficient subsidies and transfers in order to avoid resorting to RBZ monetary financing.

Zimbabwe remains in debt distress according to the staff's debt sustainability analysis. There is an urgent need to re-engage with the international community to pave the way for arrears clearance and restore access to markets. We encourage the authorities to find an agreeable debt restructuring plan with external creditors, beginning with the clearance of arrears at the IFIs.

Weak public institutions, corruption, fiscal and monetary policy missteps have eroded investors' confidence. There appears to be plenty of room to reduce the footprint of the government in the economy, improve the business environment and increase the role of the private sector. We encourage the authorities to develop a comprehensive and ambitious anti-corruption strategy, underpinned by the robust asset declaration regime and strengthened AML/CFT framework.

Mr. Doornbosch and Mr. Manchev submitted the following statement:

We thank staff for the comprehensive set of papers and Messrs. Mahlinza and Nakunyada for their informative buff statement. Staff's efforts to provide comprehensive analyses is a good example of pro-active engagement with a fragile country. The authorities' commitment to reforms and fiscal adjustments in the last two years under the SMP have been important steps in the right direction. Unfortunately, the SMP is off-track since September and Zimbabwe is experiencing an economic and humanitarian crisis due to a combination of climate shocks and policy slippages, which have magnified the social impacts of the fiscal retrenchment and currency reform. Since we broadly agree with the thrust of the staff appraisal, the following comments are provided for emphasis:

Clear priorities are needed for staff's continuous engagement. Zimbabwe's macro-balances have been deteriorating in the last twelve months, the risk of debt distress remains high, and the overall socio-political situation has been deteriorating. Protracted external arrears constrain access to external official support, while additional commercial borrowing has worsened the debt overhang and likely complicated the discussions on debt resolution. A fragile equilibrium is maintained through exchange controls and other restrictions on access to foreign exchange, creating a deep distortion for domestic economic activity. Against this background, we support the monitoring role of the IMF to be expanded to all areas mentioned in paragraph

47 of the staff appraisal. The authorities progress in implementing critical political and economic reforms will be key to restore confidence of the international community.

The authorities should also address several other very important issues beyond the scope of the SMP to mitigate the risk of a wide-spread popular uprising prior to the forthcoming election. Staff rightly observed that human development indicators in Zimbabwe have barely changed since the independence, while most countries in Sub-Saharan Africa made steady and significant improvements. For example, the NGOs and human rights organizations report a further deteriorating security situation in the country and injustice in the form of human rights abuses during the January 2019 protests. We also believe that compensation for disowned farmers should be part of a debt agreement to alleviate the socio-political tension.

Given the critical humanitarian situation, benchmarks for social spending would be beneficial to enhance the potential new SMP. Low coverage of Zimbabwe's social protection programs is worrisome and poses a significant challenge to responding to the current humanitarian crisis. We believe that coordinated efforts from the international community to help the government of Zimbabwe better prioritize scarce budgetary resources to the social sector should continue throughout 2020. Pushing for further reprioritization of budgetary resources will close the gap to ensure a minimal level of social protection and a decrease in food insecurity. Further reprioritization will also help the government of Zimbabwe to build credibility with the international community and increase the willingness by both sides to close the gap to fight a full-fledged humanitarian crisis.

We welcome the approved 2020 budget, which is anchored on zero Reserve Bank of Zimbabwe (RBZ) financing and envisages very ambitious revenue mobilization efforts. Nevertheless, even without including estimates of additional funding needed to close the humanitarian funding gap, the updated staff projections of budget revenue and financing reveal a sizable gap of about 3.8 percent of GDP or one fourth of what is needed to support the full spending envelope in the 2020 budget. Furthermore, the impact on the budget of the authorities' recent decision to terminate so called "gold incentives" and replace them with a credit support by the government funded scheme is unclear at this stage. In the current juncture, staff rightly focused their discussions with the authorities on fiscal measures to close the identified gap, since the alternative of resorting to RBZ money creation to fully close it would nearly triple reserve money and further stoke hyperinflation pressures.

We stress the importance of restoring debt sustainability. We underline the importance of fiscal consolidation and reengagement with the international community. We are concerned by the reliance on collateralized future borrowing. Securitization of future mineral exports may potentially complicate future arrears clearance and may reduce and may reduce the availability of budgetary resources. These efforts should be accompanied by a clearer and well-coordinated approach to tackle the existing arrears and cessation of quasi-fiscal activities that lead to debt increases. Staff's further elaboration on their commitments with the authorities and progress in these areas would be welcome.

We agree with staff that reducing governance and corruption vulnerabilities is not only of paramount importance to effectively address the current economic and humanitarian crisis but for improving the business environment and ensuring sustained and inclusive growth. The recent IMF TA report on governance, presented to the authorities in January, should serve as a benchmark to transform their strong anti-corruption commitment into an effective strategy in many areas, including public financial management, revenue administration, oversight of state-owned enterprises, the extractive industries, public procurement, RBZ operations, financial sector oversight, the rule of law, and AML/CFT. Based on this assistance, the authorities should adopt and publish in the next few months a high-level anti-corruption plan which will feed into a comprehensive anti-corruption strategy for Zimbabwe.

Finally, Zimbabwe's extreme vulnerability to climate-adverse events and low investment in human capital constitutes a key challenge to achieve inclusive and sustainable growth in the long-term. We encourage staff and the authorities to work closely under the SMP and develop a clear long-term strategy to properly address climate change and capacity development issues through preparing the risk reduction plan in the prospective Fund-supported programs.

Mr. Fanizza, Ms. Mateus and Mr. Persico submitted the following statement:

We thank staff for the informative set of reports, the pertinent choice of Selected Issues, and Mr. Mahlinza and Mr. Nakunyada for their buff statement. Zimbabwe is facing a humanitarian crisis and an economic meltdown. Without reengagement with the international community, the country cannot overcome its challenges. We encourage staff to explore innovative solutions and to build the necessary consensus among development partners to provide support to the country. For this purpose, we believe the following to be the immediate top priorities:

The Zimbabwean authorities must end hyperinflation and establish a credible nominal anchor. Monetary financing of fiscal deficits has fueled hyperinflation, contributing to bring economic activity to a halt and hurting the poorest the most. We agree with staff that strict reserve money targeting can be a feasible way to reduce inflation. Tightening the limit to monetary financing is a welcome first step in this direction. However, the central bank RBZ should be endowed with the necessary framework and tools to achieve that goal.

Zimbabwean authorities should redouble their efforts to enforce the rule of law and improve governance. The authorities need to commit themselves to the rule of law and need to deliver steadfast progress in reducing corruption, both in terms of devising the necessary legal frameworks and guaranteeing its enforcement. These actions would be instrumental to mobilize the needed support from developing partners.

The Fund should provide the Zimbabwean authorities with technical assistance. Fund staff should help the Zimbabwean authorities develop capacity to improve their frameworks, both on policy decision-making, as well as on operational implementation. We look forward to further staff engagement also considering the Recommendations of the IEO Report on Fragile States.

Ms. Levonian, Ms. McKiernan and Ms. Smith submitted the following statement:

We thank staff for their comprehensive reports, and Mr. Mahlinza and Mr. Nakunyada for their useful buff statement. It is evident that Zimbabwe continues to face significant economic and humanitarian headwinds, owing to both structural and external factors. In this context, a strategic and balanced approach to fiscal, monetary and exchange rate policy will be crucial for stabilizing the economy.

We agree with the staff's assessment that fiscal restraint will be necessary to restore macro-economic stability. We acknowledge, however, that this is difficult against a backdrop of severe humanitarian challenges and capital development needs. The authorities' recent tax reforms are welcomed, but additional taxes will likely be counterproductive and insufficient to close fiscal gaps given the high poverty levels. In this vein, we support staff's recommendations to sustain efforts to improve revenue administration and reduce subsidization in the agriculture sector. Further, we note the authorities' decision to terminate gold incentives in favor of a government-funded credit scheme but advise them to ensure that appropriate measures are in place to enforce repayment. We also encourage the authorities to identify additional avenues to prioritize and curtail spending. Does staff have any estimates on the amount of revenue leakages that are due to poor administration? Further, we note the reduction in the gap between private sector and public sector wages. Is there any data on the gender wage gap?

In addition, we would caution on the continued use of collateralized borrowing and support staff's call for debt transparency supported by debt reconciliation, particularly in light of recent borrowing.

Staff's debt sustainability Selected Issues Paper (SIP) provided useful insight into the extent of Zimbabwe's debt distress. With the government overleveraged, due to both internal and external financing, a commitment to the Fund's TSP should lead to an appreciable improvement in debt indicators. We also agree that the authorities would benefit from international support and debt relief. Moreover, we recall the commencement of a staff Monitored Program (SMP) in May of last year and note that it is due to expire next month, even though significant macro-economic imbalances remain present. Can staff please provide an update on the progress of the program, next steps, as well as comment on how the TA approach would evolve in this context?

There is an urgent need for a climate change resilience strategy, and external assistance would be useful. The severe impact of drought on the basic human needs of food and water, as well as its impact on the productive sectors due to electricity outages, highlights Zimbabwe's need for a formalized and mobilized strategy to make its agriculture and energy sectors more resilient. This also highlights the need for the Fund be a source of meaningful assistance — through capacity building, concessional financing, or a combination of these measures — to poor countries that are battling the consequences of climate change. Have the authorities investigated new technologies or processes that have the potential to mitigate the impact of climate change on the agriculture sector? There may also be scope to increase productivity with the use of technology.

We agree that reserve money targeting (RMT) may be the best monetary policy route at this time. We thank staff for the thorough analysis provided in the SIP, as it offers useful historical context on the developments leading up to hyperinflation and the collapse of previous exchange rate regimes. Further, we commend the authorities on the establishment of a Monetary Policy Committee to facilitate open market operations in order to meet reserve targets. We note the authorities' introduction of treasury bills and corporate bonds. We hope that they are effective in absorbing excess liquidity within the system.

In terms of the financial sector, we applaud the steps the authorities have taken toward compliance with the Basel III capital and liquidity frameworks, as well as their work to strengthen supervision of the sector. These enhancements should increase financial stability and help to improve monetary policy transmission.

Strengthened structural reforms should have a positive impact on private sector investment and inclusive growth. Given the current debt crisis, the authorities do not have leeway to support their major industries through subsidies, incentives, and capital investment at this time. However, if significant progress is made with policy reforms in major industries, improving the ease of doing business and addressing governance and corruption issues, this should help to create an environment conducive for domestic and foreign direct investment. It should also assist in improving their governance indicators relative to their peers. Nonetheless, we acknowledge the authorities' efforts thus far — including their progress on establishing the Zimbabwe Investment Development Authority, addressing AML/CFT deficiencies, as well as several governance reforms — and encourage them to continue.

Mr. Lischinsky and Mr. Vogel submitted the following statement:

We thank staff for the reports and Mr. Mahlinza and Mr. Nakunyada for their helpful buff statement.

First, we recognize the Zimbabwean authorities and population for their efforts aimed at addressing the impressive challenges and risks the country has been facing. The staff clearly depicts these substantial efforts, which include significant fiscal consolidation and the introduction of the new domestic currency, among many other policies and reforms. One of the biggest issues that Zimbabwe is tackling is its long history of economic mismanagement, extremely low confidence, and unavoidable bad results. Over the past few years, substantial efforts have been made, but evidently it has not been enough due to the tremendous adverse strength that the country is facing. In addition, Zimbabwe is vulnerable to climate change and environmental shocks, which, as noted in the staff report, are key factors to understand the deep contraction the country suffered in 2019 as the adverse impact of a severe drought on agriculture and electricity generation, all of which reinforce the contractionary effects of fiscal consolidation.

Clearly, Zimbabwe will not be able to address of all the substantial challenges without essential help from the international community. We note from the staff report that donors continue to provide significant humanitarian support, but as of January 2020 only US$ 240 million, or roughly half of the US$ 468 million requested under the UN Flash Appeal for Zimbabwe, has been committed. In this regard, we would appreciate a further elaboration from staff on the reasons for this delay in delivering commitments.

As underscored, efforts in the fiscal area have been relevant, including policies and reforms, but they should be accompanied by other measures. As staff clearly states in the report, without a resolution of the country's unsustainable external debt, the economy will not be able to grow and the probability of reaching its target under the sustainable development goals (SDGs) is low. Economic stability is not viable if it is not accompanied by social stability. In this regard, we found the poverty indicators in Zimbabwe a little unnerving: as underlined by Mr. Mahlinza and Mr. Nakunyada, an estimated 8.5 million people (more than half the population) are expected to be food insecure in 2020 and the risks of a deep humanitarian crisis are high. Once again, Zimbabwe's international re-engagement is imperious and must advance quickly. The international community needs to be more actively involved in confronting and finding solutions to these issues.

We agree with the authorities that the Fund should help explore more innovative ways to assist the country to overcome these challenges. Staff's feedback is welcome.

With these comments, we wish Zimbabwe and its people every success in their future endeavors.

Mr. Guerra and Mr. Rojas Ramirez submitted the following statement:

We thank staff for its set of well-written reports and Mr. Mahlinza and Mr. Nakunyada for their helpful buff statement. We support staff's assessment and highlight the following points for emphasis.

Zimbabwe's economy is experiencing an economic and humanitarian crisis. Looking forward, the degrees for policy implementation are very limited for a successful stabilization of the economy given the high risk of debt distress. The authorities should be strongly committed to a comprehensive reform program thru sound macroeconomic policies, fiscal consolidation, and a business-friendly open economy.

Restoring fiscal balance and attaining debt sustainability are essential for Zimbabwe's macro stability. Notwithstanding the authorities' significant efforts in 2019 for tightening the fiscal stance and containing quasi-fiscal operations by the RBZ, pervasive deficits and debt distress risks remain. We note that for the 2020 budget, staff estimates a fiscal financing gap of about 3.8 percent of GDP or ¼ of spending in the 2020 budget. In addition, further funding is required to deal with the humanitarian needs that the Zimbabwean economy is facing. Against this backdrop and with limited possibilities for advancing tax reforms and improving revenue mobilization, we concur with staff's recommendation for implementing measures aiming at spending reduction and for immediate halting of monetary financing.

Reserve money targeting and FX reforms will be instrumental to lower inflation. The monetary authorities should focus their efforts in recovering credibility in inflation management and implementing a money targeting framework for conducting open market operations. Also, FX reforms, measures to de-dollarize the economy, and the elimination of Multiple Currency Practices (MCP) are necessary for correcting market distortions, underpin reserve building and attain price stability. In this regard, we urge the authorities to eliminate the exchange restrictions and MCPs, which should be done as soon as possible or at the very least there should be a clear compromise by the authorities on a specific timeline to phase out these measures.

We concur with staff on the need for implementing financial sector reforms by conducting comprehensive banks' balance sheets soundness assessments, and to immediately put in place a strategy to address capital shortfalls. We note with concern the increase in government contingent liabilities by the collateralization of corporate loans by RBZ, as an additional drawback to an effective monetary policy implementation.

Although the authorities are taking some steps to address governance vulnerabilities, much more needs to be done. In particular, the authorities should significantly increase their efforts to effectively implement FATF standards. This will mitigate pressures on correspondent banking relationships.

Finally, we agree with staff on the urgency of closing the gap of resources necessary to attend the humanitarian crisis. This will require both the further reprioritization of budgetary resources and the authorities' effective cooperation with international humanitarian donors. Also, looking forward, given the large capacity development needs in Zimbabwe, the IMF in coordination with the World Bank and other organizations should continue to provide an effective and comprehensive technical assistance agenda. In this regard, we commend staff for reporting the capacity development strategy for 2020 in Annex V. This should become a standard annex in future Art. IV consultations.

Mr. Trabinski, Mr. Makhammadiev and Ms. Wehrle submitted the following statement:

We thank staff for the good set of papers and Mr. Mahlinza and Mr. Nakunyada for their helpful buff statement.

We note with regret that Zimbabwe is experiencing its worst economic downturn in a decade. Steadfast macroeconomic stabilization is key to prevent further aggravation of the crisis. It is also unfortunate that the SMP went off-track despite initially promising progress on the fiscal front. We support staff's policy recommendations and encourage the authorities to implement them in a timely manner. We also urge the authorities to decisively address governance weaknesses and strengthen the rule of law in an effort to improve the business environment. Such steps will be critical to garner the support of the international community and move closer towards arrears clearance.

We encourage the authorities to contain non-essential spending and better prioritize investments, given the large fiscal financing gap. We welcome the discontinuation of gold incentives and urge the authorities to phase out costly agriculture subsidies and transfers. This would release much-needed resources for priority social spending, especially to protect the most vulnerable. Better expenditure controls, as illustrated in Annex IV, could prevent leakages and the accumulation of arrears going forward.

We encourage the authorities to enhance debt management. We caution against building up external debt through collateralized borrowing on commercial terms. These loans add to debt vulnerabilities and complicate any arrears clearance or debt operation, owing to their opacity. We urge the authorities to undertake a comprehensive debt reconciliation exercise with creditors to get a full picture of the debt stock, and to work towards enhancing transparency on borrowing activities more broadly. Moreover, compiling and publishing debt statistics regularly would be a necessary step towards strengthening debt management.

On the monetary policy side, stabilizing reserve money and enhancing central bank governance should be key priorities. We concur with staff that reserve money targeting is currently the most feasible monetary policy regime and should help reduce inflation relatively quickly. We also urge the authorities to continue liberalizing the FX market. A market-based exchange rate would remove significant distortions in the economy. Monetary and FX reforms should be supported by efforts to strengthen the governance framework of the RBZ. We welcome the establishment of a monetary policy committee, which has helped enhance transparency. We nonetheless encourage the authorities to put an end to the RBZ's quasi-fiscal activities and to further enhance central bank independence. Greater timeliness in the publication of key monetary statistics would also be helpful. Further, we take note of the unusual practices in the allocation of foreign exchange and in the transfer of liabilities to the RBZ and believe that these should be abolished immediately.

We urge the authorities to reconsider their approach to supporting the agricultural sector. The SIP on Zimbabwe's agricultural potential clearly illustrates the unsustainability and inefficiency of current agricultural support programs. We note the high risks to the budget arising from fully guaranteeing farmer loan defaults. These risks should be shared with borrowers to eliminate moral hazard and misuse. We agree that input subsidies and price controls should be replaced with the provision of public goods.

Finally, we look forward to the publication of the authorities' final assessment of governance vulnerabilities and the development of a comprehensive anti-corruption strategy with the help of the Fund and World Bank. Addressing governance and corruption vulnerabilities as well as providing greater transparency is critical to restoring trust in the public institutions and succeeding with the stabilization of the economy.

Mr. Buisse, Ms. Riach, Mr. Rozan, Mr. Bouvet and Ms. Nelson submitted the following joint statement:

We thank staff for a detailed set of papers and Mr Mahlinza and Mr Nakunyada for their informative buff statement.

We note with concern staff's assessment of Zimbabwe's macroeconomic situation and outlook. Zimbabwe is again facing an economic and humanitarian crisis, exacerbated by climate shocks. The Staff Monitored Program (SMP) agreed in May was an opportunity for the authorities to establish a track record of reform and the failure to maintain that effort is enormously disappointing. We are grateful for staff's efforts to continue to support and engage with the authorities and we encourage continued efforts, working with the broader international community. While acknowledging the challenges posed by the limited access to external financing, we encourage the authorities to urgently take steps to re-establish macroeconomic stability.

We note that the authorities have made progress in implementing economic reforms in some areas. In particular, the authorities significantly reduced the fiscal deficit in 2019 from 7.5 percent to 3.5 percent of GDP and have brought the public wage bill to a sustainable level. We also welcome the introduction of a new domestic currency, adoption of an official foreign exchange market, removal of fuel subsidies, and merging of investment-promoting institutions into a single agency.

We recognize that these reforms have been made in a challenging environment. Climate shocks have had a significant impact on agriculture and electricity generation. A further poor harvest is predicted in 2020, and climate vulnerabilities remain.

We are concerned by the inconsistency of reform implementation to date. The initial reform progress under the SMP was not sustained through 2019. Monetary policy, in particular the large quasi-fiscal operations by the Reserve Bank of Zimbabwe, has not been compatible with restoring economic stability and growth. Continued restrictions on the exchange rate are driving distortions across the economy and creating opportunities for corruption. The 2020 budget has over-ambitious revenue and financing assumptions, particularly considering the social spending required to cope with the humanitarian crisis. A holistic reform effort remains needed, bringing together fiscal, foreign exchange, and monetary levers alongside a political effort to help ensure Zimbabwe's return to sustainable and inclusive growth while addressing food insecurity.

The authorities' failure to fully engage with the SMP is a missed opportunity for them to begin to demonstrate the track record of economic reforms, necessary for re-engagement with the international financial institutions and bilateral debt relief. We note with concern the DSA finding that Zimbabwe's already unsustainable debt burden continues to rise. Progress towards a solution for Zimbabwe's debt position will be dependent on the authorities' ongoing reform implementation. We support staff's assessment that the authorities should avoid further complicating their debt position through opaque, non-concessional financing arrangements, particularly when these obligations are collateralized. The authorities should enhance public debt transparency, to include all public and publicly guaranteed exposure. Can staff comment on the authorities' engagement with creditors and plans for moving towards a solution for their debt position in the medium-term? Can staff provide further information on the authorities' position on the potential assumption of losses related to currency reforms which could affect future normalization of Zimbabwe's external arrears with official creditors?

Given the challenges under the SMP, we agree with staff that improved governance is a crucial element of the reform agenda. Zimbabwe scores significantly below the regional average on governance, transparency, and corruption indicators. We welcome staff's work with the authorities on a governance vulnerabilities assessment and anti-corruption plan as an essential step towards combatting these issues. Increasing transparency should be at the heart of these reforms. We note with disappointment that the Government has failed to take significant steps to reduce corruption.

We support staff's assessment that there is a high risk of a prolonged humanitarian crisis in Zimbabwe. Rising inflation is already negatively impacting on the poor through higher prices for food, especially maize, and fuel and electricity. On the back of growing risks of social unrest, we welcome the planned increase in social spending under the 2020 budget but note staff's assessment that the true needs for social spending are significantly higher. Given the broader fiscal position, and lack of access to external financing, this will be challenging. The international community has contributed significant development funding and is also supporting the humanitarian response. Further engagement with development partners is essential and will require a demonstrated commitment by the authorities to address elite capture and corruption.

In this extremely challenging environment, we welcome Staff's ongoing engagement with the authorities. We appreciate the proactive approach taken by the IMF in responding to the authorities' request for an SMP in May last year. Given the authorities' stated commitment to continue the reform process, we encourage staff to continue to engage to support this and mitigate risks of a worst-case economic scenario for the people of Zimbabwe. Capacity building, technical advice, and surveillance will remain essential. Given the significant reform inconsistencies and future challenges noted above, how can staff best continue to engage and support reform efforts?

Mr. Mozhin and Mr. Potapov submitted the following statement:

We thank staff for a set of insightful reports and Mr. Mahlinza and Mr. Nakunyada for their informative buff statement. Zimbabwe is a fragile state with GDP per capita remaining stagnant since the 1990s. Against the backdrop of macroeconomic imbalances and the climate-related shocks, Zimbabwe is facing an economic and humanitarian crisis. The authorities have embarked on an ambitious package of economic reforms to restore macroeconomic stability, but progress has been mixed, which has put the Fund's Staff Monitored Program off-track. At the same time, protracted external arrears constrain access to external official support. We broadly agree with staff's analysis and recommendations.

Zimbabwe's outlook is challenging. Sharp economic contraction in 2019 makes it more difficult for the authorities to improve the fiscal position, reduce poverty, and increase living standards. The medium-term outlook remains fragile with the 2020 growth rate projected to be essentially zero. Inflation has increased significantly from 42 percent in December 2018 to an estimated 521 percent by the end of 2019, amplified by the depreciation of the exchange rate, broad money supply growth, and the removal of fuel and electricity subsidies. At the same time, Zimbabwe's economy is exposed to substantial external and internal downside risks, outlined by staff in the Risk Assessment Matrix (RAM). In this context, we welcome the authorities' efforts to engage in a new SMP as mentioned in the buff statement. This would be instrumental for the country's reengagement with the international community.

Sustained fiscal consolidation through enhancing revenue performance and improving spending quality is required to reduce the fiscal gap and contain pressures for monetary financing of the budget. The authorities have made important progress in their fiscal adjustment efforts, with the cash deficit expected to have declined to 3.5 percent of GDP in 2019 from 7.5 percent of GDP in 2018. At the same time, we share the concerns about the expected financing gap in the 2020 budget and staff's estimates for additional social spending needs. Could staff elaborate on an existing scope for reprioritizing capital expenditure and containing inefficient subsidies? Could staff also elaborate on the authorities' decision to replace the gold incentives scheme with the Gold Fund and potential fiscal implications?

We agree with staff that reserve money targeting (RMT) is the most feasible anchor at this juncture for the new currency. The authorities are well advised to introduce short-term market rate-determined instruments in order to operationalize the RMT. On the exchange rate policy, we welcome staff's recommendations to continue to liberalize the FX market and de-dollarize the economy. At the same time, it is paramount to monitor and limit the pass-through effects from exchange rate depreciation to inflation, which may require a more gradual approach going forward. We also support staff's recommendations to improve the publication by the RZB of monetary statistics.

Implementation of structural reforms is critical to improve the business environment and boost potential output. We welcome staff's analysis of the agricultural sector in the Selected Issues paper and encourage the authorities to advance agricultural reforms to support growth and poverty reduction. We also welcome the authorities' efforts to address governance vulnerabilities, as well as the AML/CFT deficiencies identified in the 2016 mutual evaluation report.

According to staff's DSA, Zimbabwe remains in debt distress. We would highlight the importance of clearing arrears to the international financial institutions (IFIs) and reengaging with bilateral creditors. Comprehensive and integrated technical assistance from the IFIs to Zimbabwe is also crucial for supporting the socio-economic transformation of the country. Could staff elaborate on the prospects for debt relief discussions?

Mr. Fachada and Mr. Antunes submitted the following statement:

We thank staff for the insightful reports and Mr. Mahlinza and Mr. Nakunyada for the candid statement.

Zimbabwe faces numerous macroeconomic and social challenges, including high inflation, debt distress, sluggish growth perspectives, governance weaknesses and rising levels of poverty and malnutrition. Policy slippages, coupled with the twin shocks of tropical cyclones and a severe drought, led to a drastic contraction of economic activity in 2019 and deteriorating social indicators. The current macroeconomic outlook is alarming. Coordinated reforms on the fiscal, monetary and exchange rate policy fronts are urgent. At the same time, a looming humanitarian crisis calls for a renewed engagement of the international community in support of the country.

Implementing a credible and stable monetary policy framework is key to avoid a new hyperinflation episode. We concur with staff and the authorities that, in the impossibility of adopting an alternative anchor, reserve money targeting is the best feasible solution to contain high inflation and avoid the return of hyperinflation in the short run. Designing the appropriate set of policy tools, including open market operations and repo instruments, will be crucial to allow the Reserve Bank of Zimbabwe (RBZ) to perform its institutional mission. Nevertheless, no monetary policy strategy will succeed in bringing inflation down in a sustained manner if the monetary financing of the budget is not interrupted. We are encouraged to learn that the new Monetary Policy Committee is planning to establish monthly reserve money targets consistent with low inflation. Effectively meeting those targets over a long period of time is a necessary condition to gradually rebuild monetary policy credibility.

Despite recent fiscal restraint, budget imbalances continue. We recognize the authorities’ recent efforts regarding fiscal consolidation. After growing for more than a decade, the government wage bill was substantially reduced in 2019, together with public employment ratios. Going forward, strengthening fiscal discipline will be crucial. Improving budget credibility through more realistic expenditure targets and enhanced domestic revenue mobilization should be the pillars of budget sustainability and macroeconomic stability at large. At the same time, all efforts should be done to save some fiscal space for much needed poverty- and malnutrition-alleviation programs, targeted at the most vulnerable households.

The Fund must continue to support Zimbabwe in a pragmatic basis. Zimbabwe’s current macroeconomic and social challenges are the result of policy missteps and recent climate-related shocks, but also reflect long-lasting structural issues. The international community should support Zimbabwe’s development endeavors, and the IMF must continue to play a constructive role in the country. The authorities’ commitment to reengage in the reform path should be met with a new Staff Monitored Program (SMP)— or at least some sort of “intensive” surveillance—as soon as macroeconomic and political economy conditions allow for it. Furthermore, the Fund must continue to work hand in hand with the World Bank, playing a catalytic role in Zimbabwe. To fully unleash international support, however, the Zimbabwean authorities must decidedly show consistency and ownership of their macroeconomic policies and move towards addressing the country’s official arrears.

Mr. Raghani, Mr. N’Sonde and Ms. Nankunda submitted the following statement:

We thank staff for the comprehensive set of papers and Mr. Mahlinza and Mr. Nakunyada for their insightful buff statement.

Zimbabwe's economic situation and outlook remain challenging despite the implementation of noteworthy economic reforms. We commend the authorities for their policy efforts to tackle the country's large macroeconomic imbalances. However, in spite of these efforts, economic activity has sharply contracted due to low commodity prices, adverse weather conditions and continued liquidity constraints, amid a humanitarian crisis and high inflation. External sector performance is hampered by import dependence, commodity price shocks, subdued capital inflows, and reserve inadequacy. In addition, significant downside risks weigh on the outlook and are related to delay in implementing key reforms, tighter global financial conditions and the fiscal impact of their currency reform on foreign denominated debt. Against this backdrop, sustained commitment to reforms is of the essence. The authorities should pursue their fiscal consolidation efforts while avoiding RBZ overdraft financing. On the monetary and exchange rate side, efforts should be geared at gradually streamlining current and capital account controls with the view to reducing distortions. Efforts are also needed to alleviate structural constraints to growth, including by improving the weak business climate, intensifying the fight against corruption and streamlining the large public sector.

The authorities should sustain their fiscal consolidation efforts. We commend the authorities for the significant fiscal adjustment made to date. We agree that further adjustment is needed to achieve fiscal and debt sustainability consistent with SADC commitments. We welcome the measures adopted in the budget in this regard and the contingency plans to reduce expenditures in case revenues underperform, while protecting social spending. Efforts to further improve investment spending efficiency and strengthen debt management should be pursued. While we encourage the authorities to follow through on their commitment to avoid monetary financing of the budget and continue seeking concessional resources, the lack of external financial support will strongly complicate the attainment of those objectives. Furthermore, the absorption of losses following the currency reform and the need to respond to the humanitarian crisis would add to the challenges facing the authorities to achieve fiscal and debt sustainability in the near term. We therefore call on the international community to support the authorities' reform efforts through adequate external funding.

On monetary policy, we welcome the RBZ's commitment to substantially reduce inflation particularly through the establishment of monthly reserve money targets and urge them to liberalize progressively foreign exchange controls. This should help move towards a market-determined foreign exchange rate. The authorities' gradual approach is warranted given the large fuel and food import needs. The pace of liberalization should also take into consideration the impact of the relaxation efforts on foreign exchange conditions and market confidence. We would inquire whether the authorities have requested technical assistance (TA) from the Fund to help them navigate such important reforms?

More efforts are needed to ensure financial sector stability. We welcome the measures undertaken by the authorities to mitigate operational and market risks. Nevertheless, we note with concern rising financial sector vulnerabilities and disintermediation stemming from liquidity shortages as a result of fiscal deficit financing. This re-emphasize the need to avoid monetary financing of the fiscal deficit. The withdrawal of correspondent banking relationships (CBRs) also constitutes a major source of vulnerability to the banking system. We encourage the authorities to align the country’s AML/CFT framework with international best standards. Can staff also elaborate on the technical assistance provided to the country on those fronts if any?

Additional structural measures are needed to reinforce private sector development and foster more inclusive growth. We press on the authorities to strengthen the anti-corruption framework and align it to international best standards, with a view to raising fiscal revenues, improving the business climate, and creating policy space to tackle poverty and inequalities. Enhancing human capital, notably through increased investment in education and training, and closing the infrastructure gaps in rural areas are critical to raise productivity and boost potential growth.

We support efforts to clear debt arrears and strengthen the country’s ties with the international community. Low foreign reserves, tight domestic liquidity and restricted access to international financial markets and official sector assistance are aching the ability of Zimbabwe’s economy to develop. We urge the authorities to take further steps to reengage with international financial organizations and official bilateral creditors to resolve the arrears, thus ceasing international isolation and facilitating much-needed financial support for stabilization and economic recovery.

With these remarks, we wish the Zimbabwean authorities, success in their reform efforts.

Mr. von Kleist and Mr. Herold submitted the following statement:[1]

We thank staff for their candid report, the Debt Sustainability Analysis and Selected Issues. We concur with their assessment to a large extent. We thank also Mr. Mahlinza and Mr. Nakunyada for their buff statement.

The economic and social situation in Zimbabwe poses major challenges: The economy has shrunk significantly in 2019; the newly introduced currency ZWL$ has devalued considerably while inflation is high and foreign exchange reserves are low. In accordance with staff's recommendations during the last Article IV Consultation, the government has introduced an ambitious reform program. However, its implementation has been uneven and its unavoidable social impact has been magnified by two major natural disasters, leaving more than half the population in food insecurity. We note that with the exception of the impact from two natural disasters, the authorities' fiscal consolidation efforts were largely in line with staff's recommendations. Could staff provide additional information on how the (social) adjustment costs were taken into account in the projections under the SMP?

Firm implementation of the reform strategy outlined in the authorities' stability program is crucial for Zimbabwe to overcome its economic and humanitarian crisis. Therefore, we support staff's call for simultaneous and consistent fiscal, foreign exchange and monetary policies to stabilize exchange rates and lower inflation while combating food insecurity. Concerning the latter, the planned increases in social benefits in the 2020 budget will likely not be sufficient to contain the humanitarian crisis. Therefore, if no additional donor support is forthcoming in the first half of 2020, we note with concern that the pressure for substantial central bank financing of the budget will continue to intensify. Ensuring a minimum level of social protection will require further reprioritization of spending and engagement with the international community.

We thus welcome the efforts of the authorities to tighten the fiscal stance further in order to contain the monetary financing of the deficit and contribute to economic stabilization. However, since the approved expenditures in the 2020 budget, which do not yet include additional resources to close the humanitarian funding gap, exceed the realistic mobilization of revenues and available financing by commercial banks, additional measures to reduce expenditures are necessary. Furthermore, we agree with staff's call to

[1] The gray statement by Messrs. von Kleist and Herold (OEDGR) was not circulated to Executive Directors until after the Board meeting had taken place.

increase fiscal transparency and abolish quasi-fiscal activities of the central bank (e.g. the gold incentive introduced in September 2019) and to minimize the absorption of private losses in connection with the currency reform.

Zimbabwe is still in debt distress, with longstanding arrears to IFIs, official and commercial creditors, while the real value of domestic debt has fallen significantly in the face of high inflation. Building on sustained reform implementation, we encourage the authorities to continue to explore possible modalities and financing options to clear arrears to the World Bank and other multilateral institutions in order to restore Zimbabwe's full access to external public support. In this context, we share staff's concerns that continued recourse to collateralized external borrowing on commercial terms may potentially complicate arrears clearance and should be avoided.

Sustained rapid money supply growth through continued quasi-fiscal operations by the central bank has led to a substantial depreciation of the exchange rate and very high inflation. Against this background, we agree with staff that reserve money targeting (RMT) through the introduction of short-term, market-price-driven repo instruments is currently the most appropriate monetary policy regime for the new currency. Given the very low level of FX reserves and the poor track record on inflation, alternatives such as a fixed exchange rate regime or inflation targeting are unlikely to be viable at the current juncture. We therefore welcome the explicit determination of the central bank and the newly established Monetary Policy Committee to set monthly reserve targets consistent with low inflation and to introduce instruments and procedures to achieve these targets at market rates. In the foreign exchange market, the introduction of the new Zimbabwean dollar and interbank foreign exchange trading have significantly reduced distortions. However, due to the existence of capital controls, there is still a spread of almost 30 percent between the parallel market and the interbank market. We therefore support staff's call for continued liberalization of the foreign exchange market. Most importantly, a timetable should be developed for the lifting of the foreign exchange allocation via the priority list. Furthermore, measures to further de-dollarize the economy by increasing incentives to hold local currency are essential, in particular the requirement that all domestic government transactions be conducted in ZWL$.

By providing collateral for corporate loans, the authorities have transferred credit risk to the central bank and reduced banks' incentives to manage credit risk effectively. For example, 99 percent of loans to the agriculture sector are classified as overdue. We therefore agree with staff that timely reforms in the financial sector, including improving the legal framework, strengthening banking supervision and introducing asset quality reviews are of the essence.

We second staff's assessment that structural reforms in the agricultural sector are key to promoting medium-term growth and reducing poverty in Zimbabwe. A reorientation and rationalization of fiscal support programs for agriculture, complemented by legal and policy reforms, could revitalize the sector and help re-establish Zimbabwe as an agricultural exporter. Other key reform priorities include strengthening governance, especially of the SOE sector, tackling corruption and the broadening of the rule of law (securing the rights for land use and property in the fields of agriculture). Accordingly, we welcome the authorities' commitment to publish a final assessment of governance weaknesses and a high-level anti-corruption plan in the coming months.

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

The previous Article IV on Zimbabwe was done in July 2017. Since then, there has been a change in administration, followed by efforts by the new government to try to implement fiscal consolidation and a new currency. Afterward, there were massive climate shocks that have devastated livelihoods, contraction in growth and decline in social indicators.

In the meantime, there was a 2019 staff monitored program (SMP), and the program as of now is off track, and the international reengagement has not advanced, even though the authorities have indicated strong interest in continuing reforms supported by this new SMP. However, we have to recognize that there is a binding constraint to support Zimbabwe – as the country has large external arrears, including those to international financial institutions (IFIs), it is ineligible for the traditional debt relief mechanism and has limited access to external financing.

I noted in your grays that you recognize that there is a need to facilitate reengagement with the international community in a coordinated approach, and we have to encourage or support the authorities' continuing those measures envisaged in the SMP.

Your grays covered a wide range of issues, and I would like this morning's discussion among others to include particularly three policy areas. One is how to address the fiscal challenges, including how to address the fiscal vulnerabilities with increasing social spending needs, particularly concerning the humanitarian crisis. Second, what is the Fund's role in the reengagement efforts by the international community, particularly in the context of a new SMP; and, third, the extent and pace of the foreign exchange reforms and the fiscal cost of compensating the private losses from the foreign exchange reforms.

Mr. Mahlinza made the following statement:

Zimbabwe faces deep macroeconomic challenges. The authorities have had to implement an ambitious reform agenda without balance of payments support. Progress in the implementation of the reforms was, however, complicated by severe weather-related shocks. Under the circumstances, the government had to continue to deliver social service obligations on an even larger scale than initially anticipated. At the same time, they implemented currency reforms to liberalize the foreign exchange market. These key reforms were undertaken at a time when the economy was in a downturn. The resulting pressures exerted undue stress to the economy. The authorities admit that under the circumstances, there were policy missteps and these were discussed with staff. My authorities would like to appeal that these policy missteps should not be viewed as lack of commitment to reform. In this respect, I would like to reiterate my authorities' commitment to implement reforms.

Following the elections in 2018, the Zimbabwean authorities articulated Vision 2030, which outlines a broad economic reform agenda. They also launched the short-term Transitional Stabilization Program (TSP) 2018-2020 to address structural rigidities and restore macroeconomic stability. To complement the reforms, they requested a Staff Monitored Program (SMP), which was approved in May 2019 when reforms were already being implemented, in particular the fiscal consolidation efforts. In this respect, they have owned the reform agenda from the beginning and remain committed to its implementation.

The authorities continue to remain in reform mode. They are pressing ahead with the implementation of corrective measures previously discussed with staff to get the reform agenda back on track. To this end, they are sustaining fiscal consolidation measures while working on complementary measures to establish a credible nominal anchor and improve the operations of the foreign exchange market.

As further demonstration of their commitment to reform, they have invited representatives of former commercial farmers to high-level negotiations on compensation for land development. These negotiations, which started today, will establish the amount of compensation due to the farmers and reinforce government's commitment to property rights. Follow-up technical meetings are scheduled for next week, and the negotiations are expected to be concluded within three months.

I would like to underscore the need for international support to provide humanitarian assistance and strengthen social safety nets to ease the pain of adjustment on vulnerable households. In this year's budget, the authorities have allocated an amount for social spending. However, this remains inadequate.

I would like to end by restating that my authorities value Fund advice and look forward to a renegotiated SMP to guide policy implementation. At the same time, they are hopeful that the Fund will continue to explore innovative ways to address the challenges facing Zimbabwe.

The staff representative from the African Department (Mr. Leon), in response to questions and comments from Executive Directors, made the following statement:[2]

As noted in the staff report, the central government fiscal actions were very encouraging on revenue mobilization and expenditure containment. The implementation of a reserve money targeting framework and liberalization of the foreign exchange market did not live up to expectations. Confidence in the government's ability to implement reform never took off, aided in part by poor communication, lack of transparency on data, and quasi-fiscal operations in the second half of 2019 that derailed green shoots of the tight fiscal effort.

Moreover, the political reform agenda moved too slowly to give impetus to the reengagement agenda. As the economic situation deteriorated, the social plight of citizens intensified, including from the drought and escalating price increases. Although the authorities met most of the quantitative benchmarks for June 2019—that is the first test date under the SMP—the adverse impact from policy slippages, including on governance, climate shocks, deteriorating social environment, and the absence of external finance, would have required much more adjustment than could be expected under a continuation of the May 2019 SMP. Thus, the scheduled reviews were not completed. The SMP was declared off track and discussions finalized for the 2019 Article IV consultation.

[2] Prior to the Board meeting, SEC circulated the staff's additional responses by email. For information, these are included in an annex to these meetings.

The economy remains in dire stress, and confidence has not been restored. The premium on the parallel market has widened recently to almost 70 percent, about 30 ZW dollars to 1 U.S., versus 18 on the official market. Over half of the population is deemed food insecure, and risks of another poor harvest are high. In staff's view, there is an urgent need to rally a two-stage approach to the evolving crisis. One would be to stabilize the currency and consumer price inflation while containing the humanitarian crisis, and the second track, to boost efforts at structural reform to lay the foundation for sustainable, inclusive, and resilient growth.

Directors have asked about how staff see engagement going forward. Zimbabwe needs a way out of the impasse, and staff would welcome Director's views on possibilities. From a macroeconomic stabilization perspective, the authorities will need to commit to and implement the necessary fiscal and monetary tightening, including eliminating all quasi- fiscal activities and financing by the central bank, and significantly improve the functioning and transparency in the FX market.

From a broader economic transformation perspective, the authorities should announce and start advancing a consistent and high-impact package of reforms that can support confidence and growth potential, including on agricultural transformation, governance vulnerabilities, social development, political detente, and international reengagement.

There is an equally urgent need to address the humanitarian crisis. Staff is aware of the significant contributions being made by the donor community and consideration for scaling up that assistance. Directors inquired about the delay in delivering commitments to the United Nations Flash Appeal. Our understanding is that the main reasons for delays in receiving financial commitments include an underestimation initially of the magnitude of the damage of the cyclone and the severity of the drought, tight fiscal constraints in many donor countries' aid budgets, and challenges in executing existing humanitarian support programs.

One option going forward would be for discussion on a new SMP. We are ready to engage, but the SMP would need to include all of the above aspects; namely, credible policy package to address macro imbalances, and at least an adequate social protection package potentially funded outside the budget to address at least the pressing humanitarian needs.

Turning to external debt and arrears, Directors inquired about the strategy for arrears clearance, prospects for debt relief, and the role for the

Fund in that process. Let me reiterate that the large external debt on arrears is a critical bottleneck to reengagement and Zimbabwe's economic recovery. Staff has encouraged the authorities to work with its external creditors to resume discussion on modalities to restore debt sustainability in Zimbabwe.

Progress on arrears clearance and a normalization of Zimbabwe's external financial relationship has stalled recently, as the authorities focus their attention on the immediate humanitarian and economic crisis but also as external creditors await a track record of economic and political reforms, as well as macro stability, before reengaging.

The Fund, along with the World Bank, when the time is appropriate, can assist the authorities with a comprehensive debt reconciliation exercise, an essential first step to any discussion with creditors on debt. In the event that the reengagement process accelerates and a comprehensive debt reconciliation exercise takes place, the Fund can also play its traditional role of providing analysis on various scenarios to advance discussions between Zimbabwe and its external creditors.

Finally, on the question of CD ownership, our recent experience shows that the authorities have had a very good track record on implementing technical assistance (TA) advice on statistical issues, mostly prices and national accounts, and on public financial management (PFM) and tax administration reforms. On the other hand, TA implementation has been unsatisfactory on the monetary effects and debt management issues, which require a fundamental change in policy. If we could draw a takeaway from this, it would be that traction in TA is likely highest when the policies to be implemented, especially those requiring fundamental change, are fully accepted by policymakers, thereby insuring commitment for implementation.

Mr. Von Kleist made the following statement:

The governing ZANU-PF party has been in power for over 40 years. So, what is wrong in the country is ingrained within the political structure of the country and there is nobody else to blame. That is an important point to remember if we talk about new governments.

Secondly, even the new government, there are some positive signs, the introduction of the new currency, for instance, is a hugely important step. You do it once and you try to get people trusting that new currency, and if you mess that up, you cannot do it again in two years. So, it is a lost opportunity that the introduction of the new currency was botched.

Also, Zimbabwe also went off track and the country had the opportunity to build trust with a Fund-supported SMP.Fund. So, I think we are not yet ready to announce that we would welcome a new SMP. We need some more steps by Zimbabwe before going forward.

The next point, which makes it for the donor community very difficult to engage above what they have done in Zimbabwe, is the way the brutal crackdown seems led by the army and security forces on the widespread protests over the mounting currency crisis. On the one hand, Zimbabwe is in a situation where it will need donor support. But the way the government treats its people makes it very difficult for the donor community to step up its support, and that is just something which the authorities need to recognize and change.

On the other hand, there seem to be small groups of reform-minded people in the government. We welcome that strongly, and I think the IMF should support these groups going forward, and they have done well in some areas; but more is needed in other areas, for instance, at the fact that 99 percent of loans to the agricultural sector are classified as overdue. You cannot work in an economy like that. I think the Fund can and should support Zimbabwe strongly, but without a new program at the moment.

We all want to do more climate, and we had this very interesting discussion on climate and Australia; but in this report, what we used to call natural disasters are now called climate shocks. I am not sure what that means. Why do we call things we always used to call natural disasters, suddenly call it climate shocks? Shocks tend to be unexpected, but if it is part of climate change, then it is not unexpected because we know it is coming. In that sense, I would prefer that we do not introduce new words which really do not have very much additional meaning regarding what the IMF does in countries, but rather describe things as natural disasters or weather-related events until we really know what we mean by climate shocks.

Mr. Rosen made the following statement:

I think staff set out very well what needs to happen in Zimbabwe and set out a comprehensive plan that I hope Zimbabwe will now finally follow.

First, political and governance reforms are essential to restoring confidence of the international community in Zimbabwe. International isolation is a result of its long record of poor governance, including entrenched corruption, and its disregard for property rights and the rule of law. Progress on the reforms as identified by the international community remains disappointing, and though we have heard positive remarks from Mr. Mahlinza on some of this today, the Summing Up for this Board needs to call out the entrenched vested interests and endemic corruption that is still standing in the way of reform and reengagement with the international community. For it to include any vague references to governance challenges would be a disservice to the people of Zimbabwe.

Second, we urge the authorities to move forward with coordinated fiscal foreign exchange and monetary policy measures, as staff recommended this morning. A gradualist approach to reform is not likely to stem the inflationary spiral. It is not clear to us that the authorities are committed to taking actions needed. For example, there is no apparent timeline or sense of urgency by the authorities on establishing reserve money normal anchor. Staff says the delay in introducing a monetary targeting framework appears related to pressures to continue large fiscal quasi-operations by the Reserve Bank of Zimbabwe (RBZ) at the same time the authorities are considering an assumption of large scale private losses related to currency reform. The authorities' actions to shift agricultural support schemes to the banking sector are likely to simply create new contingent liabilities rather than promote productivity. They are also collateralizing future mineral exports, which does not give us confidence in the direction of economic policies.

Finally, we agree with staff on the importance of addressing the urgent humanitarian needs of Zimbabwe's people, but we would stress that this is a role for humanitarian donors rather than the Fund. We would also call attention to recent reporting in Zimbabwe's own press that officials at Zimbabwe's state grain company are allegedly involved in diverting subsidized corn, exporting it to the DR Congo, even as food insecurity is plaguing Zimbabwe itself.

The United States remains the largest bilateral donor to Zimbabwe, and we are committed to continuing humanitarian assistance to the people of Zimbabwe, but we will not do so through government channels.

Ms. Riach made the following statement:

The case of Zimbabwe is one of the most difficult ones we deal with in the Board. The economic situation and the humanitarian situation are dire, and their need for support from the international community is very clear; but nonetheless, engagement with the authorities has proved to be challenging.

When the SMP was agreed in May 2019, the U.K. was a strong supporter of that. We always knew that it was challenging. We always knew that it was risky, but I really feel that staff did the right thing by taking those risks and trying to engage with the authorities and giving them a path to establish a track record which could help with the reengagement that we would all like to see. So, seeing the SMP going off track in the way that it has is not surprising, but it is enormously disappointing.

Mr. Von Kleist said that it was very clear that he is not ready to see a new SMP with Zimbabwe, and I have a lot of sympathy with that given where we are, but we cannot just walk away from Zimbabwe, given the humanitarian situation and the challenges that are being faced on the ground. That leaves us with some really difficult questions about how the Fund can engage going forward, and we very much encourage staff to continue the good work and the constant dialogue that they have been having with the authorities.

I agree with Mr. Rosen that the humanitarian community has a big part to play in providing immediate support. The U.K. is an important part of that effort, but it is difficult, and it is difficult for all of us as bilateral donors to step up the effort in the way that is evidently needed when the government continues to behave in the way that it does. Mr. Von Kleist mentioned the treatment of their people. I think that is a really important part of it; and if we are going to really make progress, we also need to see a crackdown in corruption and the authorities themselves doing more to provide the much-needed social safety nets.

We very much encourage the Fund to continue to engage. I think the steps that Mr. Leon set out that they will be looking for from the authorities are the right ones. We would like to see a new SMP, and until we are at a point where we can agree, we do find ways to continue that engagement. A new SMP is an important part of providing the track record, which ultimately provides a path to multilateral arrears clearance, which has to be part of the long-term solution.

Mr. Sylla made the following statement:

First of all, I would like to express this chair’s sympathy with the Zimbabwean people, which have been hit by serious climate change effects. But, maybe for lack of communication or governance, they have not been communicating. All the focus was on Mozambique, but not on Zimbabwe, and these two countries were similarly hit by natural disasters. There is no surprise that we will not have any pickup on the GDP for the next years because of the continuing drought and the impact of climate change. However, the CPI annual average data is projected to 3.7 in 2021, from 221.1 percent in 2020, so I wonder how is that projection realistic.

To end my intervention, this Board has always called staff to have imagination and to remain engaged for fragile states, and we have a case here. It is not the time for the Fund to withdraw when these people are struggling. This is why we strongly support the SMP program for Zimbabwe. We should stay and remain engaged. It is a fragile state and we cannot expect any quick result from that.

Mr. Trabinski made the following statement:

I would like to encourage the authorities to step up with a more comprehensive set of reforms, and I agree here with points raised by Mr. Von Kleist and Mr. Rosen on governance, as well as on the policy side and political side.

The situation in Zimbabwe is critical, thus, full commitment on the authorities' side would be necessary to address longstanding impediments to economic growth. It also seems that the sense of urgency is needed to introduce transparent economic reforms with social protection that should be aimed at restoring internal and external confidence. That includes focus on governance issues in the first place.

On the fiscal policy, we support staff's call for a more pronounced reform of the agricultural sector, including by eliminating or limiting existing support programs, which hamper overall productivity. More broadly, we also encourage the authorities to enhance the overall debt management. In this regard, we support the establishment of a full-spectrum debt management function in order to ensure a holistic view of debt management and its relationship with both fiscal and monetary policies. Here, I would like to ask staff on what are the authorities' plans with regard to enhancing debt management function and whether staff also factors supporting the Zimbabwean government in this regard in the 2020 capacity development.

Mr. Fanizza made the following statement:

I tend to agree with Ms. Riach that we cannot stay put. We cannot say let's wait for political change and then we start. I have seen this happen before. Before, it was always 'let's wait until the old man goes away, and then you will see things will change'. I am convinced that the failure to address the issue before Mugabe left was the reason things completely went astray. Had we got a clear macroeconomic setup and solved the issue, the country would have been able to stay together and have different political results. So, we shouldn't wait for the bad guys to leave and then we can work. It never happens like that. The two things have to go together.

We need to be innovative and think before moving, which does not mean that everything should be good there and solve this. But, we should think how to develop a credible plan for normalized relations with the international community, hoping that that will also help the political change.

On the SMP, I am actually agnostic. I do not think it is useful to repeat an SMP after what has happened. I would rather propose an approach that focuses on stabilizing the macroeconomic situation, which means tight monetary policy and completely cash-based budget. So, avoid big reforms for now, and just try to stabilize the macroeconomic situation. Inflation is 500 percent—that's hyperinflation. There is no way that you can build a credible reform program with structural issues in such an environment. You must tackle the main things and then start to work. If that works, then one could still start to think about an engagement plan. Then, a Staff Monitored Program could become helpful. I am agnostic in the sense that, if we do another SMP without a significant change in the situation, it is going to be exactly like before with no change to the situation. So, more thought should be given and not rush into a Staff Monitored Program.

We should convince the authorities to act immediately to fight the hyperinflation and implement a cash-based budget, without any illusions that we are going to change things and have a comprehensive reform program. If authorities manage to do that, then they can start reengaging with the international community, showing as a fact that they are in the process of also improving the political situation and the rule of law. Then, we can do a Staff Monitored Program to build the track record needed for engagement.

What I am against doing business as usual, as we have done until now. Therefore, we need to try to be imaginative and I would support humanitarian assistance.

Mr. Alkhareif made the following statement:

We welcome the authorities' fiscal consolidation efforts in 2019, including through improving domestic revenue mobilization and increase in efficiency of spending. We also take positive note of the increase in social spending envisaged in the Budget 2020. Like Mr. Sylla, we think the humanitarian crisis put pressure not only on the authorities, but also on the Fund and the World Bank, to help the country weather this extreme crisis.

We note with concern the uneven implementation of structural reforms, including in the foreign exchange and monetary reforms. We encourage the authorities to do all what is needed to restore the independence of the central bank. I think Mr. Von Kleist and Mr. Fanizza raised two good words, credibility and trust, and these are very good components for an independent central bank, and we encourage the authorities to emphasize the role of independence of the central bank to restore macroeconomic stability.

I welcome the selected issues paper's analysis on monetary policy. The staff used a good analysis in terms of giving the pros and cons of the different monetary policy regimes, and we tend to agree with staff that the monetary targeting is the most feasible regime. However, we encourage staff to discuss with the authorities the lessons learned from other recent Fund-supported programs that did not succeed in the monetary targeting. I think that will be a more enriching discussion, as the authorities formulate their plans on bringing down inflation and inflation expectations.

We welcome the structural reform agenda under the Vision 2030. However, like Mr. Rosen, we ask the authorities to pay clear attention to the governance and anti-corruption measures as essential for a successful reform agenda, to restore the governance, and build credibility and trust.

On the agriculture sector, we agree that improving the productivity and avoiding any rent-seeking activities will be important. It is also important to improve the AML/CFT framework—specially to exit from the FATF list—to restore the correspondent banking relationships (CBRs).

With these remarks we wish the authorities well in their future endeavors.

Mr. Rozan made the following statement:

We agree that the environment in Zimbabwe is very challenging. We recognize that natural disasters faced by the country last year have put a strain on reforms and triggered a humanitarian crisis of a very significant scale. However, these vulnerabilities have been compounded by a range of policy actions that have contributed to increasing the country's already significant imbalances, resulting in a high level of money creation. This calls for urgent and coordinated action with the country, and we encourage the authorities, both monetary and fiscal, to take all necessary actions to stabilize the economy and free more fiscal space to tackle the humanitarian crisis. It is clear there is a need for holistic reform of economic policies, but I will not go too much into details on this.

Regarding the SMP, the failure of the past SMP is a missed opportunity for the authorities to demonstrate their commitment to reform and set an important milestone for the HIPC process. However, I encourage staff to maintain a close engagement with the authorities, and agree with the comments made this morning by Ms. Riach. So, this close relationship and engagement should take the form of advice on reforms, as well as technical assistance, as highlighted this morning. This would be instrumental to help the authorities build the conditions for a potential successor SMP in the coming months. This will also ensure buy-in from potential donors given the huge humanitarian needs.

Mr. Doornbosch made the following statement:

I would very much like to support the intervention this morning by Ms. Riach. We do think the Fund should do everything it can and work hard towards a new Staff Monitored Program. I think there is no way around this. It is very much needed, and this will also be very helpful for the international community to further engage. Whether this will be sooner or later will depend on the authorities taking the required corrective measures that the Fund staff is rightly asking.

I agree with Mr. Rosen that anticorruption measures need to be part of the corrective action, and we need to be clear about that up front. Of course, Mr. Fanizza points out that this might not help immediate macroeconomic stabilization, but it gives a clear signal of the intentions of the authorities of Zimbabwe. I also believe that macro and structural in this kind of situation should go hand in hand. We have seen that, without credibility of the government, you try to introduce new currency and it does not help, because you need to take the structural measures to get the credibility to take these measures that would help the macro stabilization. So, there is no way around it, we need to do both and we need to do it in the context of a Staff Monitored Program, and whether that is going to be successful, it will depend on the authorities of Zimbabwe.

Mr. Ray made the following statement:

I just had a quick look at the 2012 Article IV report: “The authorities remain interested in a Staff Monitored Program. Zimbabwe’s debt overhang remains a serious impediment. Addressing it will require a comprehensive arrears clearance framework underpinned by strong macro policy framework in what would likely be a protracted process.” I think that judgment was correct. Record of implementation or recommendations from previous consultations is mixed. I do wonder how long we keep kicking the can down the road, whether or not there might be a different approach, and how we wrestle with a situation where clearly it is a humanitarian case.

In 2012, things were a little bit rosier than they are now. There is a strong humanitarian case for the international community to be involved. Also, the external debt issue needs to be addressed. However, just how to go about it is the question. I thought Mr. Leon put his finger on it. He was talking about TA, and he said traction in TA is likely highest when policies to be implemented are fully accepted by policymakers. I think you could take out the TA and say traction is likely to be highest when policies to be implemented are fully accepted by policymakers.

I tend to agree with Mr. Fanizza. Given the dire circumstances, we should be thinking about stripping back to the core essential strengths to try to solve something, to demonstrate to the authorities that by working with the Fund on an appropriate set of policies, they can solve something and that is in their interests rather than having a whole huge reform agenda attached to what is a macroeconomic problem.

I am not necessarily going to be that optimistic given the track record, but if the authorities are interested, an SMP is a way as it is the vehicle that we have when we are not providing any balance of payments support. How to get traction in a situation like this? That is really the question that we need to think about. It is worthwhile trying to be a bit innovative, because just looking back over the history, the way we have been approaching it does not seem to get us far.

Mr. Chikada made the following statement:

I agree with all Directors about the daunting challenges Zimbabwe faces regarding transparency, governance, and the need to regain the confidence.

Specifically, I want to comment on the monetary policy following Mr. Alkhareif's comments, that is the importance to secure RBZ autonomy or independence, given the unfortunate history of Zimbabwe's monetary finance and consequent hyperinflation with the political pressure. We think that safeguarding the central bank autonomy, both legally and in practice, is essential to recover confidence in the monetary policy. Without central bank autonomy, the monetary targeting regime will not work. Giving RBZ the autonomy is a good starting point since it does not cost that much in fiscal resources, shows credibility, and should pave the way for international donor support.

On the second point, we are concerned about the fast-growing and collateralized borrowing and lack of transparency, this should be tackled.

Ms. Levonian made the following statement:

Zimbabwe is facing significant challenges and the authorities have difficult decisions to make to improve the humanitarian crisis and the fundamentals of the economy. The question is whether they will, given the context we have just discussed; and I agree with colleagues who have talked about corruption and governance being fundamental in being able to mobilize change, and without it, there is going to be a serious lack of credibility.

I tend to agree with Mr. Fanizza's approach in that we really need to strip this down to its fundamentals. Part of that is achieving the central bank autonomy. The central bank has to significantly reduce financing to the government and shift the focus to conducting monetary policy, promoting financial stability, and managing the exchange rate. The central bank authorities have to move towards increasing transparency and credibility in order to maximize monetary policy effectiveness. This is a foundational change necessary to achieve what needs to be done. And there has to be buy-in from the authorities, and to do that, the Fund advice needs to be tailored in that respect.

Finally, combining two of the points that have been raised. A large part of the humanitarian crisis is a result of climate change. How you provide assistance is going to be tricky, but there is clearly a requirement to assist. Building resilience to natural disasters is part of that, and this chair has often raised that as an issue. We should work towards a Staff Monitored Program but only in the sense that as we go forward, we see progress in doing so. With that I would wish the authorities well.

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

First, on the inflation issue, the way in which inflation goes down that rapidly, end point to end point, is because of the adjustment that we are building into the program for 2020. The average is high because it ended last year, 2019, at 520. The target is to get it down to 50 at the end of 2021. So, the average is already of 200; but then, starting from 50, going down towards 3 percent in 2021, the average will drop precipitously at that point. The real issues are if there is a risk that the inflation will not fall that rapidly, and that is a question on whether the adjustment that staff is looking for in terms of monetary consolidation, fiscal, are going to be executed. If they are, then it can be realized. If they are not, then you will have an issue.

The second question I want to address was from Mr. Trabinski on the issue of debt management functions. Both the Fund and the World Bank have been providing technical assistance on building the debt management capacity in Zimbabwe. They are looking specifically at improving the reporting timeliness, improving and consolidating a debt template, and even expanding the overall debt perimeter in terms of how debt is managed within that particular system. This is an ongoing work and there is still a long way to go, but there has been a start.

One further comment I would like to make is looking at the issue of an SMP. The hard reality is that the macro stabilization adjustment that we can conceive of in an SMP, even if it is brute force focused purely on inflation, has a significant social cost— the cost of adjustment. Given the situation where we are now, during the initial condition, it is vital that there has to be some type of support from the international community to help that process along. That is probably up for debate and maybe requires further discussion, but the SMP on its own carries too-huge a cost to give it any reasonable chance of success without some support. I would like to put this on the table.

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

Just to support that and also to say that the Catch-22 situation that you might think is implied by the strategy, namely, that we think a successful SMP requires financial support while the potential donors may think that financial support requires a track record first. With the right set of conditional commitments and prior actions, that could be sorted out, so the fundamental problem is one of essentially political will.

Ms. Riach made the following statement:

I just wanted to come in briefly on a couple of points, one responding to the points that staff have just made about the SMP and the humanitarian assistance. This is a real issue and there are a number of countries who are already providing bilateral support, including the U.K. It is difficult to conceive of a significant step-up in that support without the prior actions and clear demonstration from the authorities that staff have outlined. That said, I do think that this is really the only way forward, and there is also a job for us to do in terms of coordinating between the Fund and potential donors to try and put together a package that could work.

Finally, slightly off the subject of Zimbabwe, I wanted to pick up on the point about climate shocks and the language used and to say that actually we really like this language. I think the debate has moved on somewhat, and it is useful to be clear that we are talking here about natural disasters, which specifically relate to climate.

Mr. Mahlinza made the following concluding statement:

On behalf of my Zimbabwean authorities, I wish to thank Executive Directors for their constructive views and policy recommendations. We have listened very carefully to the comments by Directors, and we just want to stress that we are dealing with a difficult case where the political reforms are moving at a slow pace, however, with severe macroeconomic challenges at the background that could get worse if not properly addressed. We cannot give up, and I believe that this is really challenging the role of the Fund. The authorities are ready to move, and we want to just encourage continued engagement by the Fund with the authorities. We like the discussions that are emerging also in terms of really being innovative and maybe also looking at an SMP-lite.

Despite some setbacks, the authorities have continued to implement macroeconomic reforms. They view the successful implementation of reforms under a renegotiated SMP as instrumental to entrench macroeconomic stability and anchor the broader reform agenda. I think for us it is important that we have support to anchor the broader reform agenda.

The authorities concur on the need to reinforce fiscal discipline. They have steadfastly implemented frontloaded fiscal consolidation measures over the past 16 months. In this vein, they have continued to exercise expenditure restraint and remove fuel and electricity subsidies.

They have also transferred the financing of agriculture to private banks and terminated the gold export incentives to contain growth in reserve money and inflation. The interim gold incentive scheme, which has been transferred to the budget at a much lower cost, was previously financed through the Reserve Bank of Zimbabwe subsidiary.

In line with Fund advice, the authorities have agreed to adopt a reserve money targeting framework to anchor inflation and stabilize the exchange rate. To achieve the Monetary Policy Committee's monetary reserve targets, the central bank is working on modalities to introduce short-term liquidity management tools. At the same time, the central bank advances to government have been reduced and now limited to smoothing short-term cash flow mismatches.

To complement these monetary policy measures, the central bank introduced a foreign exchange electronic training platform that is expected to improve the efficiency of the foreign exchange market. Against the background of these recent measures, month-on-month inflation has significantly declined from 3.8 percent in October 2019, to 2.23 percent in January 2020, and the authorities are optimistic that this disinflationary trend will persist into the future.

The authorities want to reiterate their commitment to undertake structural reforms aimed at promoting private-sector development, improving the business environment, and strengthening competitiveness. They are implementing longstanding structural reform measures aimed at reforming state-owned enterprises, while addressing corruption in procurement and revenue administration. Concurrently, they are advancing political reforms subject to the unavoidable yet important consultative processes. The authorities are planning to develop and publish a roadmap for the implementation of reforms, as recommended in the recent Governance and Vulnerabilities Assessment.

Finally, I wish to thank staff, the staff team lead by Mr. Leon, for their tireless effort and constructive engagement with my authorities and responding to the questions and issues raised by Executive Directors this morning.

The Acting Chair (Mr. Zhang) noted that Zimbabwe is an Article VIII member and maintains several exchange restrictions and multiple currency practices subject to Fund approval under the Article VIII Section 2(a) and Section 3. Staff is not recommending approval of these measures at this time. Therefore, no decision is proposed.

The following summing up was issued:

Executive Directors agreed with the thrust of the staff appraisal. They noted with concern that Zimbabwe is facing an economic and humanitarian crisis exacerbated by policy missteps and climate-related shocks. These would require difficult policy choices from the authorities and support from the international community. Directors urged the authorities to make a concerted effort to ensure economic and social stability through the adoption of coordinated fiscal, monetary and foreign exchange policies, alongside with efforts to address food insecurity and serious governance challenges. They emphasized the importance of reengagement with the international community to support efforts to achieve economic sustainability and address the humanitarian crisis.

Notwithstanding efforts in 2019 to tighten the fiscal stance and contain quasi-fiscal operations by the central bank, Directors noted that pervasive deficits remain and could be exacerbated by the need to respond to the humanitarian crisis. Directors called for non-essential spending cuts, including decisive reforms to agricultural support programs, to allow for social spending needs. They underscored the importance of public financial management and enhanced domestic revenue mobilization efforts.

Directors stressed that eliminating deficit monetization would not only be crucial for fiscal sustainability, but it would also serve as a precondition for the stabilization of hyper-inflation and the preservation of the external value of the currency.

Directors noted that Zimbabwe remains in debt distress, with large external arrears to official creditors, and encouraged the authorities to give impetus to reengagement efforts and debt management and transparency. In particular, they cautioned against continued recourse to collateralized external borrowing on commercial terms as this may potentially complicate any future arrears clearance operation.

Directors underscored the need to establish credibility in the new currency. They encouraged the authorities to press forward with the establishment of a functional foreign exchange market and to remove distortions that could lead to rent-seeking behavior in the economy. Directors agreed that given low reserves and hyper-inflation, limited credibility, and a lack of access to traditional forms of external financing, a monetary targeting regime is appropriate to conduct monetary policy. Enhancing central bank independence and transparency, including by timely publication of monetary statistics, would be important.

Directors welcomed the progress on financial innovation, supervision and inclusiveness indicators. They noted, however, the need for continued vigilance to ensure financial stability. They encouraged the authorities to conduct asset quality reviews of the banking sector, develop a new framework for managing weak banks, and increase the effectiveness of the AML/CFT framework, including by effectively implementing FAFT standards.

Directors stressed the need to address governance and corruption challenges, entrenched vested interests, and enforcement of the rule of law to improve the business climate and support private-sector-led inclusive growth. Such efforts would be instrumental to advance reengagement efforts with the international community and mobilize the needed support. They noted with regret that the staff-monitored program was off-track and underscored the importance of continued engagement between the Fund and the authorities, including through technical assistance, policy advice and other innovative ways, to help immediately stabilize the economy and address the humanitarian crisis.

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

APPROVAL: January 20, 2022

CEDA OGADA
Secretary

Annex

The staff circulated the following written answers, in response to technical and factual questions from Executive Directors, prior to the Executive Board meeting:

Fiscal policy

1. Can staff comment on which potential revenue items the authorities expect may fall short of their targets?

- For the 2020 budget, the authorities had used a baseline that included a higher inflation projection for the year, which was reasonable at the time given available information. Subsequent announcements on monetary policy, which used updated data, incorporated a lower forecast for inflation. The most likely categories of revenue to be affected by the lower inflation forecast are VAT, the 2 percent financial intermediation tax, and income taxes (as lower inflation leads to a lower projection for nominal wages in the economy).

2. Can staff elaborate on how the authorities could avoid central bank financing while maintaining social spending to support the vulnerable, considering the funding gap on required social spending?

- In the absence of additional, non-inflationary, and affordable financing (e.g. grants or concessional financing) the authorities are left with two major avenues to bolster social spending while avoiding central bank financing. First, the authorities can eliminate inefficient subsidy schemes and use the proceeds for additional targeted social spending. Second, the authorities could delay further planed capital expenditure for 2020 into later years to finance social support schemes. The latter, while alleviating short-term acute needs, would worsen the growth outlook and timelines for cyclone and drought recovery.

3. Can staff comment on the scope for reprioritizing capital expenditure and containing inefficient subsidies, and the political appetite for a paradigm shift in agriculture policy and how could transitory costs be mitigated?

- The authorities share the view that further reforms to Command Agriculture are necessary, and many support the paradigm shift from the provision of private good to investment in public capital for the agricultural sector.

- Nevertheless, there are significant vested interests who benefit from the current system that remain skeptical of reforms. Moreover, a paradigm shift in agriculture would have to be accompanied by a similar revolution in the rural social safety net, for example by expanding the harmonized-cash transfer, to maintain the living standards (and support) of small-scale farmers during the transition to more private-sector led business model.

4. Of the ZWL$2.18 billion in non-tax revenue and grants in the 2020 budget, how much is grant money and have the grants been fully confirmed? Do the authorities have any remedial measure in case of grant shortfalls?

- The 2020 budget projects non-tax revenue and grants to reach ZWL$2.18 billion, versus an expected ZWL$ 0.4 billion in 2019. The increase is attributable to two factors: first, inflation, which has increased significantly the nominal value of non-tax revenue to a projected ZWL$985 million; and second, the remainder is the authorities' forecast of disbursements from donors in response to the international appeals. A shortfall in grants would have to be mitigated in a similar manner to the existing financing gap.

5. Does staff have any estimates on the amount of revenue leakages that are due to poor administration? Further, we note the reduction in the gap between private sector and public sector wages. Is there any data on the gender wage gap?

- Revenue administration capacity at ZIMRA is relatively strong and ZIMRA has shown consistent traction in implementing TA advice and strategic goals for domestic revenue mobilization. With the assistance of Fund and World Bank TA, ZIMRA is in the midst of modernizing its entire IT system as part of a larger strategic plan adopted in 2019.

- Leakages in revenue relate to macroeconomic idiosyncrasies that make it challenging for revenue authorities to keep up. Rapid movements in prices and the exchange rate make it difficult to sustain the real value of tax collections for important tax bases (e.g. fees, customs duties expressed in ZWL$, etc.).

- Wage rigidities in Zimbabwe's very high inflation environment have created significant volatility and dispersion in real wages as different sectors have different wage negotiating timelines. The public sector in particular has taken a particularly severe real wage cut, as wage negotiation and agreements have not kept pace with inflation. The slightly more flexible private sector, and in particular the informal economy, seem to have been able to adjust wages more quickly, but still not fast enough to keep up with inflation.

- There is not at present any strong data on the trend in the gender wage gap.

6. Can staff elaborate on the fiscal implications of the new Gold Fund and the termination of quasi-fiscal activities by the central bank for gold incentives?

- Staff's preliminary view of the new Gold Fund is that its fiscal costs will be higher than the authorities expect. Staff analysis is based on the parallel market spread and its effects on gold deliveries to Fidelity (see Text Figure 14 of the staff report), which are essential for the RBZ to meet its loan obligations, and the assumption that gold deliveries will only normalize if the price paid to gold miners is near to the international spot price (otherwise smuggling and diversion will undercut Fidelity). In the absence of price liberalization in the gold sector, subsidies of some form will be necessary to incentive the sales to Fidelity.

Debt sustainability

7. Can staff elaborate the magnitude of collateralized external borrowing on commercial terms by Zimbabwe and on the authorities' position for assuming losses related to currency reform, both of which could affect future normalization of Zimbabwe's external arrears with official creditors?

- Collateralized borrowing still makes up a relatively small percentage of Zimbabwe's total external debt, but it has been growing fast since 2016. Measurement of Zimbabwe's collateralized debt is severely hampered by the lack of full disclosure in the contracting of these debt obligations, as well as the use of proceeds. A combination of loans (and loan guarantees) that have been renegotiated on several occasions clouds the picture of the net exposure of the RBZ and what it means for encumbering future gold production.

- On losses from the currency reform, the latest information points to at least US$1.2 billion in losses. As discussed in ¶27 of the staff report, the authorities are concerned that failing to honor the obligations of foreign investors and creditors affected by these losses would harm Zimbabwe's reputation and undermine access to critical goods and services (e.g., fuel and international air travel).

- Staff has stressed to the authorities the risks that both collateralized borrowing and assumption of losses from the currency reform have the potential to complicate solving Zimbabwe's debt overhang with the creditors.

8. ***Can staff comment on how confident they are in the comprehensiveness of the debt figures in the DSA and where the potential blind spots may be?***

- There are significant risks to an upside surprise to Zimbabwe's public debt. The most obvious are the future settlement of compensation to displaced farmers and the RBZ's commitment to compensate the private sector for various losses, including exchange losses stemming from the currency conversion.

- There are other risks to the debt level, including potential contingent liabilities from SOEs. The risk of another debt shock relating to agriculture is also very high.

- Fundamentally, the risks stem from the lack of establishing front, middle, and back office debt management functions. While the back-office function within the DMO has strong capacity, it is severely hampered by a lack of real time data and the issuance of debt outside its authorization. Moreover, with no functional middle- or front- office debt management, there is little ability to take a holistic view of debt management and its interrelation with the budget and monetary policy.

Monetary and exchange rate policy

9. Could staff further elaborate on losses from the currency reform and the legal provisions justifying their compensation?

- These losses have arisen from the currency mismatch of assets and liabilities of banks and non-financial firms at the time of the currency reform. When the new domestic currency was introduced in February 2019, all assets and liabilities under the Zimbabwe jurisdiction, which were previously denominated in US$, were converted at 1:1 into the new domestic currency. This created losses for bank and non-financial firms for obligations to foreign residents that remained denominated in US$.

- Staff is not aware of any legal requirement to compensate for all of these losses from the currency reform. However, as discussed in ¶27 of the staff report, the authorities are concerned that failing to honor the obligations of foreign investors and creditors affected by these losses would harm Zimbabwe's reputation and undermine access to critical goods and services (e.g., fuel and international air travel).

10. Can staff elaborate on the capacity constraints for introducing short-term, market-rate-determined monetary policy instruments to advance open market operations?

- The RBZ has the technical capacity to introduce a money targeting framework. The delay in implementation appears related to pressures to continue large quasi-fiscal operations by the RBZ and concerns that high interest rates would have a negative impact on public debt service and economic activity.

11. Could staff elaborate on the potential ramifications to inflation dynamics of the significant increase in mobile payments?

- In staff's view, mobile payments do not have a material impact on inflation dynamics. The very high inflation is due to the very high increase in reserve money and lack of confidence in the new currency.

12. Could staff elaborate to what extent the high inflation reflects the pass through from the higher-than-expected depreciation of the ZWL$?

- Staff believes that, as shown in Text Figure 15 of the staff report, the high exchange rate depreciation is the primary factor behind the rapid increase in inflation since September 2018.

13. Have the authorities requested technical assistance (TA) from the Fund to help them implement in a gradual manner the monetary and FX reforms?

- The new Monetary Policy Committee has requested TA on the monetary and FX reforms, beyond the TA provided to the RBZ in April 2019. Staff is currently discussing the appropriate timing and sequencing of such TA. Ultimately the pace of implementation of the reforms is a decision of the authorities.

Financial sector

14. Can staff comment on the success of the Asset Management Corporation (ZAMCO) during 2015- 2018 and the improvement in the repayment climate?

- The takeover of non-performing assets by ZAMCO during 2015-18 indeed improved the affected banks' performance. However, in staff's view, such takeover was not accompanied by reforms to address the underlying problem of weak credit culture at affected banks. Since the new government came into office in October 2018, the amount of assets held by ZAMCO was capped at ZWL$1.1 billion, and efforts intensified to increase asset recovery. The observed improvement in repayments reflect to a large extent the high inflation that has reduced the real value of outstanding bank credit.

15. ***Can staff shed light on the efficacy of the underlying regulatory infrastructure required to minimize associated cybersecurity risks?***

- The current regulatory infrastructure seems generally effective as there has not been any significant cybersecurity breach. Moreover, in cooperation with the Government, the country's near-monopoly for electronic money (ECONET) has recently updated its know-your-client policies to include improved documentation and biomarkers.

16. Can staff elaborate on mitigating measures if the administrative measures on deposits and FX controls were removed?

- The staff and authorities agree that the removal of existing deposit and FX controls should be done gradually to mitigate any adverse effect on financial stability.

17. ***Can staff elaborate on the technical assistance provided to Zimbabwe on AML/CFT to bring the framework with international best standards?***

- The Fund has provided TA on AML/CFT, but stands ready to extend its capacity development effort to strengthen the AML/CFT framework if the authorities request it. Such capacity development could focus on addressing the key items in the authorities' action plan with the FATF. Strengthening the effectiveness of the

AML/CFT framework would facilitate Zimbabwe's exit from the FATF list and mitigate potential CBR pressures.

Structural reforms

18. ***Have the authorities investigated new technologies or processes that have the potential to mitigate the impact of climate change on the agriculture sector?***

- The authorities adopted a climate mitigation strategy in 2016, which has been updated with various policies in 2018. However, implementation of this policy has been slow due to financial constraints and an agricultural support model that prioritized income support over sustainable development and building climate resilience.

19. ***Can staff comment on whether there is a national integrated plan to address climate risks in Zimbabwe?***

- Zimbabwe has a national climate mitigation strategy and Vision 2030 has explicit sections for safeguarding the environment.