

Central Role of the Central Bank Governor

'State performance is enhanced when politicians are able to mobilize support for clear policy preferences and when they can utilize a high-quality bureaucracy (a core element of state capacity) to see these policies transformed into real outcomes' ¹

Zambia's central bank, the Bank of Zambia (BOZ), is widely regarded as one of the most professional economic institutions in the country, generally successful in fulfilling its primary mandate of maintaining price and financial system stability. Since 2018, we have studied the effectiveness of BOZ in delivering on its mandate, focusing on the post-liberalization banking reforms in the early 1990s. We explore some of the main factors behind the sustained success of the central bank as an effectiveness outfit relative to other apex economic institutions in Zambia. BOZ's steadiness is especially striking when compared to other economic institutions, like the Ministry of Finance and Zambia Revenue Authority whose functioning was notably undermined.² BOZ performance relies significantly on the legal autonomy, which insulates the institutions from undue interference.

In our forthcoming paper, we coincidentally delve into the role of the Governor in fostering and sustaining the success of BOZ. This is a coincidence because the BOZ Governor was fired by the Republican President during the weekend, on 22nd August 2020.

Generally, we note that occasional political pressures on the central bank arose quite often between the mid-1990s and 2019, emanating out of competitive clientelist democracy, especially around elections. During those episodes of external political pressure, BOZ was generally able to deliver on its mandate and from a study perspective, was ultimately regarded as a 'Pocket of Effectiveness.' We view a Pocket of Effectiveness as a '...public organisation that is relatively effective in providing the public goods and services the organisation is officially mandated to provide, despite operating in an environment in which effective public [policy and] service delivery is not the norm.'³The prospects for an institution to emerge as a Pocket of Effectiveness are shaped by organizational factors, namely the scope and clarity of its mandate; the strength and political linkages of its leadership; and its internal culture and cohesiveness.

Zambia's political settlement is based on highly centralised executive powers, which has resulted in the importance of personality and quality of the leader and his chosen coalition. This at times has produced a positive outcome for Zambia's technocracy, as we have seen during the Mwanawasa years, but can also produce rather unproductive ones, in which the

¹ Centeno, M., Kohli A. and Yashar, D. J. (eds.) (2017). *Unpacking States in the Developing World: Capacity, Performance, and Politics*. Cambridge: Cambridge University Press, p. 27

² Hinfelaar, M., and Sichone, J. (2019) The challenge of sustaining a professional civil service amidst shifting political coalitions: The case of the Ministry of Finance in Zambia, 1991-2018. ESID Working Paper No. 122. Manchester, UK: The University of Manchester, http://www.effective-states.org/wp-content/uploads/working_papers/final-pdfs/esid_wp_122_hinfelaar_sichone_POE.pdf. The ZRA and BOZ studies are forthcoming.

³ Michael Roll (2014), (ed.) *The Politics of Public Sector Performance: Pockets of Effectiveness in Developing Countries*, London and New York: Routledge

function and capabilities of the institutions are undermined.⁴ The Zambian Central Bank's relatively independent position in the ever changing political coalitions from the mid-1990s to 2019 was significantly attributed to conscious efforts of its top echelon, particularly the Governor, to entrench BOZ's autonomous position and work towards legislative independence in 2016. Besides changes in the legislative framework, BOZ's countervailing powers were strengthened by the acknowledgement by political leaders that the central bank acts as an important 'signaller' to international financial markets.

Historically, the BOZ Governor has played an important role in defending BOZ's mandate vis-à-vis the Executive, with the ability to withstand political pressures and prevail over the Executive regarding the necessity for BOZ to abide by international and regional central banking standards. From the 1990s, BOZ maintained a long tradition of internal mentoring and grooming of would-be future Governors and senior management. However, BOZ's autonomy and effectiveness were briefly under threat during December 2011 – January 2015. This intermittent observation coincided with a major political and ideological shift, which saw a short-lived attempt by the ruling party to change conventional central banking policies.

In the context of the independence, professionalism and thus effectiveness of public institutions in recent years, including BOZ, Dr. Grieve Chelwa, a senior lecturer at the University of Cape Town noted that:

There was a general sense of armageddon in the dark days of late 2015 and early 2016 and the heroic efforts by Dr. Kalyalya and his team brought the country back from the brink. Knowing that the origination of the crisis was in the Ministry of Finance, Dr. Kalyalya has openly castigated government on their reckless and uncoordinated borrowing and spending policies, showing unusual independence of thought by a public servant in Zambia⁵

The recent firing of the Governor may well be a turning point for BOZ's independence and possibly, for its effectiveness as well. Granted, the decision of the Head of State to fire the Governor was a Constitutional prerogative of the Presidency as was the decision to appoint a new Governor, subject to Parliamentary ratification.

The real underlying challenge of this recent turn of events at BOZ for central bank independence and effectiveness is at least threefold:

Firstly, there appears to have been a glaring lack of due process in taking the firing decisions. The reportedly lack of internal consultations in the Executive before making the changes is very disquieting, particularly considering the critical point in the country's economic trajectory. State House takes its cue – or should take its cue – on the macroeconomic growth and stabilization swings of the economy and therefore the required countercyclical monetary, fiscal and external policy measures to take from the heads of the Executive's apex economic institutions, notably the Minister of Finance, Minister of National Development Planning,

⁴ For a recent study on the important of institutions in Zambia, see The Developmental State in Zambia: Plausibility, Challenges, and Lessons from South Korea <https://ecommons.cornell.edu/handle/1813/69927>

⁵ <http://gchelwa.blogspot.com/2018/05/in-praise-of-denny-kalyalya.html>

BOZ Governor, and Commissioner General of the Revenue Authority, among others. Again, the lack of due consultation in decision-making is very worrying.

Secondly, the firing of a highflier Governor with credentials aplenty, extensive accolades of accomplishment and a long track-record of monetary policy success during a precarious economic period was always bound to have a strong social and political backlash locally and general apprehensive reaction internationally. The negative local and international sentiments were possibly significantly worsened by the fact that no reasons were fronted, not even flimsy ones for the firing of the Governor, which has created space for speculation.⁶ Meanwhile, as we understand it, according to the law, the recently fired Governor will continue to receive his full contractual package, salary and all, until May 2023 when his contract would have ended. This essentially means BOZ will pay for two Governors while deriving the services of only one. This is clearly an unnecessary cost resulting from a rush, un-consulted and irrational decision.

Finally, the appointment of a possibly politically inclined and motivated individual as BOZ Governor has the potential to undermine the independence, credibility and particularly, effectiveness of the central bank; the risks of further capital flight from Zambia have just escalated. And given the hasty nature of movements at BOZ, in the interim, the Governor position will remain vacant as the new appointee cannot take up office, pending ratification by the Parliament after it reopens on 11th September.

Typically, one might have argued for the Zambian society and indeed the world to give the new Governor the benefit of the doubt. However, Zambia is facing a unique quadruple threat, namely: a general slump in real GDP growth even before Covid-19 hit; headwinds from a full-blown Covid-19 pandemic; a huge and problematic pre-Covid-19 debt overhang with massive debt service pay-out demands; and pressure of escalating fiscal slippages – including money printing by BOZ – during the 2021 elections just around the corner.

Experimentation during a macroeconomic crisis is never a good idea, least of all when the economy already had a tried and tested winning formula for macroeconomic and financial stabilization. But since the decision has already been taken and is unlikely to be reversed, we would bid the new Governor and Zambia Godspeed. We can only hope the new Governor will learn quickly and will muster the fortitude to withstand the competitive clientelist political pressures that have so often come to bear on BOZ's political economy around election time during the country's post-liberalization history.

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⁶ For the possible motivation of the firing of the BOZ governor, see <https://www.bloomberg.com/news/articles/2020-08-23/zambian-leader-criticized-for-firing-central-bank-governor>