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Zambia 1991-92
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Zambia - Subject Files - Country Files - Correspondence - Volume 1

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WBG ARCHIVES

SecM92-1581

FROM: Vice President and Secretary

December 23, 1992

CONSULTATIVE GROUP MEETINGS FOR ZIMBABWE AND MOZAMBIQUE

INFORMAL DONORS MEETING ON ZAMBIA

Written Statements

Attached are written statements on the meetings of the Consultative Group for Zimbabwe held December 2-3, the Consultative Group for Mozambique held December 9-10; and on the meeting of the Informal Donors for Zambia held on December 11, 1992, circulated in lieu of oral statements.

Distribution:

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MOZAMBIQUE CONSULTATIVE GROUP MEETING

1. The Consultative Group for Mozambique held its sixth meeting in Paris on December 9 and 10, under the chairmanship of Mr. Stephen Denning, Director of the Southern Africa Department of the World Bank. The Mozambican Delegation was led by His Excellency Mario da Graca Machungo, the Prime Minister, and included His Excellency Eneas da Conceicao Comiche, Minister of Finance, His Excellency Daniel Tembe, Minister of Trade, and His Excellency Adriano Maleiane, Governor of the Central Bank.
2. The Consultative Group meeting took place just two months after the signing of the peace agreement and the implementation of a cease fire, which ended 17 years of war. Participants agreed that peace offers the country the possibility of accelerating economic growth over the medium term and thus reducing the severe poverty in which the majority of the Mozambican people live, and moving towards democracy. The Consultative Group focused on the Economic and Social Rehabilitation Program, ESRP, particularly the regular balance of payments support. The peace conference which took place in Rome the following week dealt with the assistance necessary to sustain the peace process, including demobilization, elections, reintegration of returning refugees, displaced persons and demobilized soldiers, and emergency non-food aid. Participants at the CG stressed that it is critical that both the peace process and the ESRP be adequately funded.
3. The donors commended the Government for its determination in achieving peace and for progress made in carrying out its reform program, despite extremely difficult security conditions, exacerbated this year by the severe drought that has devastated the region. In the past year a number of measures have been taken to improve the incentive structure for production, provide for greater financial discipline in fiscal management and public enterprises, and improve efforts to reduce poverty. These include unification of the foreign exchange markets; shifting expenditures to high priority areas including health and education; establishment of more transparent procedures for the management of counterpart funds; advances in the financial sector reform, including establishment of the Bank of Mozambique as a separate Central Bank, and authorization for the establishment of new banks and insurance companies; progress in establishing the autonomy of public utilities; and steps towards the revitalization of the regional transport network.
4. There was broad agreement that to realize the potential benefits of peace, the most immediate challenge confronting the Government is to secure full political and economic integration of the country, including the resettlement of one third of population and the reconstruction of up to half the infrastructure. Another major challenge is to continue building and to extend the reach of the market-oriented economy. While some donors were concerned that extending market based reforms at present would conflict with securing a supply response of the economy, several commented that market-based reforms need to be supportive of domestic productive capacity. Others questioned whether a liberalized import regime and credit allocation system would ensure that sufficient resources flow to productive investments to generate the supply response for long-term growth. As administrative solutions have been tried and failed, participants said, other policies such as taxes on luxury goods and restructuring of uncreditworthy enterprises were needed to address the problem. Overall, there was general agreement on the main elements of reform needed: a more stable macro-economic framework to reduce inflation, further liberalization of trade and exchange rate policy, continuing the financial sector reform, and restructuring or privatization of public enterprises.

5. Another main theme of the discussion was the need for a more effective collaboration among donors. Harmonization of policies—of both Government and donors—is needed to enable Mozambique to exploit the opportunities and meet the challenges of peace. Due to conditions of war and drought, support has been given to Mozambique in the form of separate emergency and economic programs, which has made external resource management complex and resulted in confusion and inefficiency. Donors suggested that, in the CG meeting of 1993, the Government present a program that unifies the emergency and reconstruction programs in a coherent and transparent framework that will serve as a reference point for all donor assistance. Participants noted that continued improvements in accounting and transparency in the management of external aid would enable donors to provide funds in a more flexible manner including untying of aid, thereby facilitating the implementation of the ESRP. Donors agreed to work closely with Government to harmonize their procedures on procurement and assure more timely disbursement.

6. The meeting suggested that the National Reconstruction Plan, now under preparation, should serve as the common reference point for programming donor support. Donors stressed that it is important to ensure the consistency of the Plan with macro-economic objectives, as well as to link investments to growth and poverty reduction. In this regard the Bank indicated its willingness to assist the Government in looking at how the macroeconomic framework might evolve under peace, and what the shorter term implications of such a scenario would be in order to ensure sustained economic development.

7. The full amount of external financing for credits and grants (including food aid) of about US\$ 760 million was committed at the meeting. Of this amount, 18 % was food aid, 51 % was for other grants, and 28 % for concessional loans; of the total, 34 % was import support. At the Rome peace conference additional pledges amounting to about US\$300 million were announced by participants for demobilization, elections, reintegration of refugees, displaced persons and demobilized soldiers, and non-food emergency aid. The assumption of reasonable external debt relief, Mozambique's overall financing needs for 1993 have good prospects of being met.

8. Members of the Consultative Group attending the meeting were Austria, Australia, Brazil, Canada, Denmark, Finland, France, Germany, Italy, Japan, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, the United Kingdom and the United States. Also represented were the African Development Bank, Commission of the European Communities, European Investment Bank, International Monetary Fund, Kuwait Fund for Arab Economic Development, and the United Nations Development Programme. Ireland and the Organization for Economic Cooperation and Development participated as an observers.

**1992 CONSULTATIVE GROUP MEETING
MOZAMBIQUE
(US\$ Million)**

	<i>1992 Estimated</i>	<i>1993 Required</i>
GRANTS	512.2	500.3
Commercial Food	99.2	85.0
Emergency Food	95.5	55.0
Non-Food Emergency	27.5	1/
Import Support Funds	82.0	146.3
Investment Projects	208.0	214.0
CREDITS	206.0	210.7
Import Support	104.0	112.0
Investment Projects	53.0	53.1
Services	49.0	45.6
External Debt Relief	528.4	419.2
ESAF	63.1	21.0
External Investment	30.0	30.0
TOTAL ESRP	1339.7	1181.2
SPECIAL PROGRAMS		
Demobilization		61.0
Elections	0.0	76.0
Non-Food Emergency and Resettlement	2/	265.0
TOTAL	1339.7	1522.2

1/ Included in "Special Programs".

2/ Included in Grants.

ZIMBABWE CONSULTATIVE GROUP MEETING

1. The second Consultative Group Meeting for Zimbabwe was held on December 2 and 3 in Paris. The meeting was successful in raising the funds that Zimbabwe will need to continue implementing its adjustment program, despite the worst drought of this century, and in allowing for a full and frank discussion of the program and the issues confronting the country. The Zimbabwe delegation was led by the Honorable Dr. Bernard Chidzero, Senior Minister of Finance. The meeting was held almost ten months after the first Consultative Group Meeting in Paris in February 1992.
2. Donors especially praised the Government's handling of drought relief: procurement and distribution of food to a large part of the country's population, as well as efforts to deal with shortages of water and electricity, have been major undertakings of the last year and have heavily taxed the country's fiscal and human resources.
3. The Donors commended the Government of Zimbabwe for its continued implementation of its adjustment program in the face of the severe drought and especially its efforts at restraining the budgetary deficit, the steps taken in liberalizing trade, reducing the civil service and decontrolling prices. They emphasized the need for persistence in the adjustment efforts and the importance of Government's efforts to disseminate the details of the adjustment program to ensure popular appreciation and support of the reform measures.
4. However, key elements of the program were judged to have fallen behind the pace needed to elicit a strong supply response from the economy and to keep the program sustainable. Donors expressed the view that civil service rationalization and parastatal restructuring should be accelerated. Similarly, accelerated domestic deregulation, especially relating to private investment, and continued trade liberalization and export promotion, complemented by continued fiscal adjustment and monetary restraint, are vital to increase the competitiveness of exports and domestic producers. The donors urged the Government to accelerate the implementation of elements in the program designed to protect the poor from transitional hardships, including the Social Development Fund that the Government has established. Moreover, donors urged that budgetary provisions for basic social needs in education and health be maintained, including provisions for the management of the AIDS pandemic.
5. Donors expressed support for the overall adjustment strategy and stressed the importance of timely implementation and management of the program. The Government agreed with this view and announced that technical assistance for implementation of various components of the program has already started or soon would be under way. Although the drought has occupied many of the staff expected to deal with the Social Dimensions of Adjustment component, the Government has recently organized and staffed the units that would implement this vital component. Both donors and the Government agreed that rates of disbursement of financial assistance, especially balance of payments support, needed to be improved. Discussions were continued from the last CG meeting on improved modalities of procurement and disbursement to facilitate untying of aid and to reduce procedural delays by both Government and donors. Regular consultations will be held in Harare to review progress and ensure increased flexibility by all parties.

.../...

6. The Donors emphasized the importance of creating an environment that encourages increased private sector activity in the economy and recognized the need to make special provisions to encourage small and medium enterprise development, particularly the informal sector. This was seen as a key to dealing with the vital need to increase employment opportunities in the economy. Privatization of those public sector institutions whose functions could be better carried out by the private sector was urged, along with improved performance of parastatals that would remain in the public sector. The Government reconfirmed its intention to assure a greater role for the private sector in the economy and strengthen the partnership between Government and the private sector. Donors also urged the Government to continue to look at its program in a regional context and assist efforts now under way to increase regional cooperation and integration. Zimbabwe should benefit financially from the recent peace accord in Mozambique. Given the need for greater budgetary flexibility, it is important for this peace dividend to be secured as early as possible.

7. Total additional external resources of about US\$1.4 billion will be needed in 1993 for Zimbabwe to accelerate economic growth, continue its drought recovery efforts and implement successfully its structural reform program. About two-thirds of this amount was expected from commitments already signed. Pledges given at the meeting indicated that the remaining amount had been essentially met, with about 57% of this in the form of quick-disbursing balance of payments support.

8. The meeting was attended by delegates from Australia, Austria, Canada, Denmark, France, Germany, Italy, Japan, the Netherlands, Norway, Spain, Sweden, Switzerland, the United Kingdom, the United States, the African Development Bank, the Arab Bank for Economic Development in Africa, the Commission of the European Communities, the European Investment Bank, the International Finance Corporation, the International Fund for Agricultural Development, the International Monetary Fund, the Kuwait Fund for Arab Economic Development, the United Nations Children's Fund, and the United Nations Development Programme. Observers from the Organisation for Economic Co-operation and Development were also present.

TABLE A. ZIMBABWE: EXTERNAL FINANCING PLAN
(US\$ million)

	1993	1994	1995	1993-95
TOTAL DISBURSEMENTS NEEDED BY SOURCE OF FINANCE				
LOANS	1126	772	540	2438
Multilateral	744	517	400	1661
Bilateral	191	158	58	407
Commercial	191	97	82	370
GRANTS	280	258	200	738
TOTAL FINANCE	1406	1030	740	3176
EXPECTED DISBURSEMENTS FROM COMMITMENTS EXISTING AT THE END OF OCTOBER 1992				
LOANS	755	347	183	1285
IDA	90	0	0	90
IBRD	88	31	22	141
IMF	144	122	51	317
ADB	213	19	25	257
Other multilateral	56	53	42	151
Bilateral	91	93	28	212
Commercial	73	29	15	117
GRANTS	155	58	30	243
TOTAL	910	405	213	1528
ADDITIONAL DISBURSEMENTS NEEDED				
LOANS	371	425	357	1153
Multilateral	153	292	260	705
Bilateral	100	65	30	195
Commercial	118	68	67	253
GRANTS	125	200	170	495
TOTAL	496	625	527	1648

TABLE B. ZIMBABWE: ADDITIONAL COMMITMENTS NEEDED TO MEET
FINANCING REQUIREMENTS
(US\$ million)

	1993	1994	1995	1993-95
LOANS	575	475	470	1520
Multilateral	300	300	300	900
Bilateral	150	100	100	350
Commercial	125	75	70	270
GRANTS	200	250	200	650
TOTAL	775	725	670	2170

INFORMAL DONORS MEETING FOR ZAMBIA

1. A donor's meeting on Zambia took place at the World Bank Office in Paris on December 11, 1992. It was chaired by Mr. Stephen Denning, Director of the World Bank's Southern Africa Department. Honorable Emmanuel Kasonde, Minister of Finance, led the Zambia Government delegation. The delegation included Honorable R.D.S. Penza, Minister of Commerce, Trade and Industry, Honorable Guy Scott, Minister of Agriculture, Food and Fisheries, Honorable Dean Mung'omba, Deputy Minister for Planning and Development Cooperation in the Office of the President, Mr. Dominic Mulaisho, Governor of the Bank of Zambia, and senior Government Officials.
2. The purpose of the meeting was to review progress under Zambia's economic recovery program and to discuss its financing requirements for 1993. Donors congratulated the Government of Zambia on the manner in which it had managed the effects of the devastating drought gripping the country in 1992 and for democratizing its political system. Zambia had been able to cope with the drought largely because of the timely and effective administrative and logistical arrangements the Government put in place early in the year and the efforts of the international community in mobilizing resources to finance food imports. As a result, famine had been averted and no one had died of starvation.
3. Donors commended the Government for the bold measures it had implemented since taking office in November 1991 to reform and restructure the economy. Despite the drought, the Government increased sharply the price of maize and decontrolled consumer prices of mealie meal. The Government also eliminated subsidies on fertilizer. With the introduction of foreign exchange bureaus in October this year and movement of the OGL system to a negative list covering only about 5 percent of the country's imports, the foreign exchange system has been liberalized further. In September this year, lending interest rates were decontrolled, with the result that these rates have risen substantially. The budget deficit (excluding grants and interest) is reported to have declined from 7.5 percent of GDP in 1991 to 2.5 percent. Progress has also been made on civil service reform, with retrenchment of 12,000 workers in 1992. And finally, implementation of the privatization program is on track with 19 parastatals offered for sale.
4. Donors expressed concern about the high rate of inflation, estimated at over 170 percent in 1992. While it was recognized that this was due in part to unavoidable structural factors, including the current drought, but the meeting agreed that greater restraint in Government spending would be critical to bringing inflation under control in 1993. Specific mention was made of the need to contain spending on wage increases, Zambia Airways, and the military. Control of inflation would also be critical in alleviating poverty. Donors stressed the importance of the provision of essential social services including a social safety net and the Government's Civil Service Reform Program. They urged accelerated action to deal with the structural aspects of poverty reduction.
5. Donors noted the progress so far in establishing transparency and accountability of governance in Zambia and urged that further progress be made. They are seen as critical elements in assuring the sustainability of the economic recovery program.

6. For its part, the Government delegation expressed its appreciation to the international donor and creditor community for having made available in 1992 an extraordinary level of external assistance and generous external debt relief to Zambia. The Government hoped that a similar level of support would be provided in 1993.

7. Regarding donor commitments for 1993, all donors expressed their continued support for the program. As it was an informal donor meeting, no formal pledging was requested. Donors indicated that they expected to be in a position to pledge their commitments at the next Consultative Group Meeting in Paris in March 1993. The two tables attached were circulated at the meeting. They show the external financing requirements assuming a baseline World Bank program and balance of payments support already announced by the EEC and Japan. Some donors were able to make at least partial pledges for 1993, but these are not included in the attached tables. While the pledges that were given were of encouraging amounts, considerable additional effort will be needed to meet the 1993 financing requirements. Donors agreed to consider these substantial financing needs when setting their programs for next year.

8. The meeting was attended by delegations from Canada, Denmark, Finland, France, Germany, Ireland, Italy, Japan, Netherlands, Norway, Sweden, Switzerland, the United Kingdom and the United States. Also represented were the African Development Bank, Commission of the European Communities, European Investment Bank, International Finance Corporation, International Fund for Agricultural Development, International Monetary Fund, Kuwait Fund for Arab Economic Development, United Nations Development Programme and the World Food Program. The Organization for Economic Cooperation and Development participated as an observer.

Table 1. Zambia -- Updated Balance of Payments Projection, 1992-94
(In millions of U.S. dollars)

	1991 revised	Rights program projections			Update of November 1992		
		1992	1993	1994	1992	1993	1994
Trade balance	129	-306	-69	-63	-222	-193	-107
Exports, f.o.b.	1082	1004	1061	1069	1064	947	1016
Copper	895	723	757	740	852	738	736
Other metals	103	177	169	176	112	79	129
Nonmetal	84	105	135	153	100	130	150
Imports, c.i.f.	-952	-1310	-1130	-1132	-1286	-1140	-1123
Metal sector	-285	-320	-338	-358	-317	-338	-357
Fertilizer	-34	-40	-38	-41	-44	-45	-47
Petroleum	-83	-93	-104	-110	-83	-82	-87
Maize 1/	0	-276	-48	...	-269	-72	...
Other	-550	-581	-602	-623	-573	-603	-631
Services (net)	-593	-530	-517	-522	-519	-536	-550
Interest 2/	-378	-313	-314	-333	-313	-314	-333
Other factor	-13	-13	-20	-21	-13	-20	-21
Nonfactor	-202	-204	-183	-168	-194	-202	-196
Unrequited transfers	468	566	451	390	631	750	453
Private	-40	-40	-41	-43	-38	-38	-38
Official	508	606	492	433	669	788	491
Current account balance	4	-269	-135	-195	-110	21	-204
Metal sector	584	456	451	407	525	346	362
Nonmetal sector	-579	-725	-586	-602	-635	-325	-566
Memorandum items:							
Current account, excluding interest obligations and official transfers	-90	-550	-296	-272	-454	-440	-345
Drought impacts	...	-276	-48	...	-289	-72	...
Metal sector	655	529	534	501	596	426	451
Nonmetal sector, excluding drought impacts	-745	-803	-782	-773	-761	-794	-796
Copper export volume ('000 MT)	375	380	390	400	400	390	390
Copper price (US\$/lb)	\$1.06	\$0.93	\$0.94	\$0.90	\$1.026	\$0.920	\$0.920

Source: Bank of Zambia, and Fund staff estimates

1/ Figure shown reflects timing of payment, rather than date of importation.

2/ Assumes financing gaps are filled on highly concessional terms.

07-Dec-92

Table 2. Zambia: External Financing Requirements, 1992-94
(In millions of U.S. dollars)

	est. 1991	Rights 1992	program 1993	projection 1994	Update of 1992	November 1992 1993	1994
1. Current account, excluding interest and official transfers (Drought impact)	-90	-550 (-270)	-296 (-50)	-272 (...)	-454 5/ (-289)	-440 (-72)	-345 (...)
2. Debt service obligations	-791	-739	-651	-641	-771	-677	-648
Nonmultilaterals	-462	-514	-436	-424	-536	-453	-431
Scheduled obligations	-334	-447	-352	-316	-464	-372	-338
Paris Club creditors	-212	-404	-307	-268	-404	-307	-268
Other 1/	-122	-43	-45	-49	-60	-65	-70
Interest on arrears and service of rescheduled obligations	-128	-67	-84	-107	-72	-81	-93
Paris Club creditors	-78	-7	-11	-17	-7	-11	-17
Other	-50	-60	-73	-90	-65	-70	-76
Multilaterals	-329	-225	-215	-217	-235	-223	-217
World Bank	-88	-63	-53	-54	-73	-77	-77
IMF	-172	-95	-93	-97	-95	-77	-74
Other multilaterals	-69	-67	-69	-66	-67	-69	-66
3. Targeted reduction of arrears 2/	-1050	-170	-88	0	-186	-100	0
Nonmultilaterals	-833	-30	...	...	-91	...	...
Paris Club creditors	-76	-30	...	...	-91	...	...
Other	-757	...	...	...	...	...	...
Multilaterals	-217	-140	-88	0	-95	-100	0
World Bank	-253	-40	...	...	-39	...	...
IMF	20	-31	-88	...	-32	-90	0
Other multilaterals	16	-69	...	...	-24	-10	...
4. Change in gross official reserves (increase -)	11	-35	-30	-30	-15 5/	-30	-30
5. Gross financing requirement (= 1+2+3+4)	-1920	-1494	-1065	-942	-1426	-1247	-1023
6. Debt relief 3/	1158	0	0	0	526	337	282
Paris Club creditors	295	...	...	...	451	262	212
Other	863	...	...	...	75	75	70
7. Financing requirement after debt relief (= 5+6)	-762	-1494	-1065	-942	-900	-910	-741
8. Identified possible disbursements	762	1025	731	670	850-900	638	445
World Bank (nonproject)	202	240	150	150	190-240	125	125
BOP support from other donors	264	396	270	220	325	156	...
Commodity assistance (Maize)	76 (--)	105 (18)	52 (--)	53 (--)	224 (106)	118 (68)	60 (--)
Commodity assistance (Non-maize)	(76)	(87)	(52)	(53)	(118)	(50)	(60)
Project assistance	244	264	240	225	200	247	260
Suppliers, private and short-term capital, net 4/	-23	20	19	22	-87	-8	0
9. Financing requirement, after identified disbursements and debt relief	0	-470	-335	-273	-50-0	-272	-296
Memo: Copper volume ('000 MT)	375	380	390	400	400	390	390
Copper price (US\$/lb)	1.06	0.93	0.94	0.90	\$1.026 5/	\$0.920	\$0.920

Source: Bank of Zambia, and Fund staff estimates.

- 1/ Includes interest on short-term lines of credit.
- 2/ Excludes temporary further accumulation of arrears to nonmultilaterals pending conclusion of rescheduling discussions.
- 3/ Includes deferral, and temporary accumulation of arrears to nonmultilaterals pending conclusion of rescheduling discussions.
- 4/ Also includes changes in reserve liabilities, other than to IMF.
- 5/ Assumes a copper price of US\$0.963/pound in the fourth quarter of 1992.



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Document Date 10 September, 1992	Document Type Board Record			
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Exception(s)				
Additional Comments Declassification review of this record may be initiated upon request.		The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group. <table border="1"><tr><td>Withdrawn by Salma Berrada</td><td>Date June 13, 2025</td></tr></table>	Withdrawn by Salma Berrada	Date June 13, 2025
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THE WORLD BANK
Washington, D.C. 20433
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LEWIS T. PRESTON
President

May 15, 1992

His Excellency
Sigbjorn Johnsen
Minister of Finance
Oslo NORWAY

Her Excellency
Grete Faremo
Minister of Development Cooperation
Oslo NORWAY

Dear Mr. Minister and Madam Minister:

May I take this opportunity to acknowledge with thanks receipt of your letter of April 30, 1992, addressed to me and Mr. Camdessus. Norway has been an important source of assistance for Zambia. I am conscious of this contribution and I look forward to Norway's continued support for Zambia's development efforts.

I share the sentiments that you expressed in your letter regarding the peaceful and democratic change of Government in Zambia after last year's elections. It was a proud moment for Zambia and, indeed, for Africa. The new Government moved quickly to take charge and to implement its economic reforms with the support of the World Bank and the IMF. I personally visited the country in February this year, and gained first-hand impressions of the Government's commitment to the program. The Government's credibility depends, to a large extent, on the speed with which it can deliver the benefits of reform and economic recovery to the people of Zambia. This, in turn, depends critically on the quantity and quality of assistance the country can get from the international donor community. As you correctly observed in your letter, the existing financing gap has been exacerbated by the need to import large quantities of food on account of the drought.

We in the World Bank recognize the imperative of making extraordinary efforts to provide emergency assistance to Zambia. To this end, we are collaborating with the United Nations in mobilizing emergency support for Zambia. In addition, we have doubled our allocation for an IDA adjustment credit scheduled for Board presentation in June of this year, from US\$100 million to US\$200 million. The increase is intended, in part, to provide balance of payments support related to Zambia's food import requirements.

His Excellency Sigbjorn Johnsen and
Her Excellency Grete Faremo

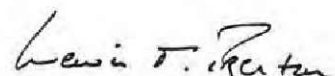
- 2 -

May 15, 1992

The country's high debt service is a major constraint on Zambia's development efforts. We are urging donors to extend debt relief to Zambia through conversion of debt into outright grants. Furthermore, in our aid coordination efforts, we are urging Zambia's creditors and donors to consider rescheduling their debt. I am confident that the concerted efforts of Zambia's creditors and the international donor community can help the country overcome its debt overhang and generate sufficient economic growth and development to improve the living conditions of its people.

I look forward to collaborating with Norway in these efforts.

Sincerely,

A handwritten signature in dark ink, appearing to read "Lewis T. Preston". The signature is fluid and cursive, with the first name "Lewis" and last name "Preston" clearly distinguishable.

Lewis T. Preston
President

WORLD BANK OFFICE TRACKING SYSTEM
OFFICE OF THE PRESIDENT
Routing and Action Transmittal Sheet



TO: Mr. Jaycox (J-5073) DATE: 5/04/92

SUBJECT:

Document From: Sigbjorn Johnsen & Grete Faremo

To: ltp

Dated: 4/30/92

Reference No.: EXC920504001

Topic: ZAMBIA: writing about the difficult economic situation & the worst drought in the region, etc.

ACTION INSTRUCTIONS:

DUE DATE:

HANDLE

REVIEW AND RECOMMEND

FOR YOUR INFORMATION

DISCUSS WITH

AS WE DISCUSSED

XXX PREPARE RESPONSE FOR LTP'S SIGNATURE

5/15/92

FOR YOUR FILES

RETURN TO

OTHER:

Remarks: cc: Messrs. Karaosmanoglu, Stern and Sandstrom

PLEASE HAVE RESPONSE READY FOR LTP'S SIGN. BY DUE DATE.

OFFICE MEMORANDUM

DATE: April 30, 1992

TO: President Lewis T. Preston

FROM: Einar Magnussen, ED

EXTENSION: 81081

SUBJECT: Zambia

Dear Mr. Preston,

I have today received by fax the attached copy of a letter from the Norwegian Minister of Finance, Mr. Sigbjørn Johnsen and from the Minister of Development Cooperation, Ms. Grete Faremo, respective Governor and Alternate Governor for the World Bank and was asked to forward this to you.

The original will follow by mail.



DET KONGELIGE FINANS- OG TOLLDEPARTEMENT

KONTOR: AKERSGT. 42 - TELEFON: (02) 34 90 90
TELEFAX: 34 95 05 - TELETEX: 21 444 FDEP N. TIL FINANSDEPARTEMENTET
POSTADRESSE: POSTBOKS 8008 DEP., 0030 OSLO 1

Michel Camdessus, Managing Director
IMF

Lewis Preston, President
The World Bank

Deres ref.

Vår ref. (bes oppgitt ved svar)

Dato

92/3745/Ø

30.04.1992

Dear Mr. Camdessus and Mr. Preston,

We are writing to you on the issue of Zambia, a country with a newly elected democratic regime, an extremely difficult economic situation and now hard-hit by the worst drought in the region for decades.

As you probably know, Zambia is one of Norway's main partner countries in development cooperation. A substantial part of our development assistance has over the years been directed towards this country. Furthermore, we have been most pleased to witness the recent positive political developments in Zambia, with last year's elections and the subsequent democratic change of Government.

On the economic scene we have been impressed by the new Government's demonstrated commitment towards strong economic reforms. Norway, together with other members of the donor community, has expressed strong willingness to support these efforts by the Zambian Government.

However, it is discouraging to observe that even after the joint efforts at the Consultative Group meeting last month, a large financing gap still remains for Zambia for which no immediate solution can be foreseen. It is furthermore a fact that a substantial part of the financing gap is a direct consequence of Zambia's multilateral debt burden.

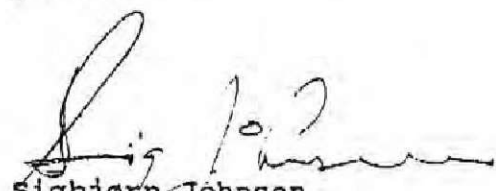
In order to stimulate a joint effort to reduce Zambia's financing gap, we would strongly urge the Bretton Woods Institutions to use their influence to put pressure on major bilateral creditors and donors, and at the same time consider possibilities for further easing Zambia's acute multilateral debt service problem. Only through such a joint effort can a comprehensive and satisfactory package with a fair burden sharing be put together.

We would like to use this opportunity to thank you personally for the assistance your institutions already have given over the years to support Zambia in its adjustment efforts, and the creativity your institutions have shown in order to ease Zambia's debt burden in general, and its multilateral debt burden in particular. We would also like to use this opportunity to repeat our satisfaction with the Bank's efforts through the establishment of mechanisms such as the 5th and the 6th Dimension, and with the Fund's "Rights Approach". Particularly in the case of Zambia, both institutions have shown great flexibility to ease its debt service burden.

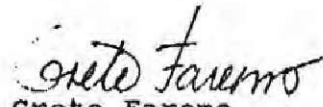
However, given Zambia's serious situation, the existing mechanisms are not sufficient to assure the required financing and create the basis for sustainable growth. We would therefore appreciate if you could seriously consider ways to further ease the debt burden to IBRD and IMF in order to facilitate the difficult reform process Zambia has committed herself to.

As you understand, we are deeply concerned about Zambia's situation which now has been further exasperated by the drought. Norway is therefore prepared to make a special effort to assist Zambia, provided that complementary efforts are being made by the rest of Zambia's bilateral creditors and donors with strong support from your institutions. This concerted effort must aim at closing Zambia's financing gap and should reflect principles of fair burden sharing.

Counting on your ability to be innovative and creative, we are confident that the donor community will be able to help Zambia through this crucial and very difficult transition period.



Sigbjørn Johnsen
Minister of Finance



Grete Faremo
Minister of Development
Cooperation

OFFICE MEMORANDUM

DATE: May 14, 1992

TO: Mr. Ernest Stern, EXC *sec*

THROUGH: Mr. Francis X. Colaço, Acting Regional Vice President, AFR

FROM: David Cook, Acting Director, AF6 *AF6 Cook*

EXTENSION: 33321

SUBJECT: ZAMBIA - IMF Contribution
to External Financing Gap

1. As explained in the attached papers, the IMF Board was given an informal briefing on Zambia on May 13. The principal matter discussed was the possible deferral of payments due to the Fund in 1992 amounting to US\$100 million, as a contribution to meeting Zambia's exceptional drought related, external financing requirements. The discussion was positive and our sense of the meeting (shared by Mr. Erb) was that EDs considered that such a deferral would be needed and could be expected to be endorsed formally when a new rights arrangement program is considered by the Fund Board in July, 1992.

2. May we have your confirmation that the action taken by Fund Management in presenting the deferral issue and the generally positive reception of the Board, constitute a sufficient basis for distributing the Privatization and Industrial Reform Credit (PIRC) documents to the Bank's Executive Directors, once the Credit negotiations with the Zambian authorities have been successfully completed.

cc: Messrs. Karaosmanoglu (EXC); Husain (AFRCE); Denning o/r (AF6DR);
Patel, Todd (AF6CO); Daffern (AF6IE)

DCOOK:baf

Yes. we can go ahead. But, as noted earlier, the existence of a satisfactory financing plan should be a condition of effectiveness — just to make sure that the Fund in fact acts as anticipated.

5/16/92

OFFICE MEMORANDUM

DATE: May 14, 1992

TO: Mr. D. Cook, Acting Director, AF6

FROM: John Todd, AF6CO

EXTENSION: 3-5056

SUBJECT: ZAMBIA: IMF Contributions to External Financing Gap

1. The Deputy Managing Director of the IMF gave an informal briefing on Zambia this morning to the Fund Board. His speaking notes are attached. Note in particular the bottom half of page 8 where he says, "I believe it will be necessary for the Fund to spread out over 1992 and 1993 the targeted reduction of arrears". The particular schedule he mentions is to reduce these payments by \$88 million in 1992. When added to the Board's decision of last month to reduce Zambia's special charges by \$12 million, this deferral would contribute \$100 million to meeting the 1992 external financing requirements identified at the recent Consultative Group Meeting.

2. The discussion that followed was positive. Even the French, who had strongly opposed conceding this point at the CG, offered only some general concerns that the Fund should be careful not to set precedents and that every effort should be made to raise enough money to avoid such a deferral. My sense of the meeting was that everyone recognized that such a deferral would be needed and would be formally endorsed as part of a new rights arrangement program.

3. Mr. Erb was pleased with the discussion. He believes his remarks and the ensuing discussion represent as much of a commitment by the Fund as can be given at this time. He trusts it will be sufficient for the Bank to proceed with our operation. If Senior Management require further clarification, they may want to talk to him directly.

cc: Messrs. Patel (o/r), Imam, Kisa (AF6CO); Daffern (AF6IE)

JTodd:lim



Record Removal Notice

File Title Zambia - Subject Files - Country Files - Correspondence - Volume 1		Barcode No. 1328884		
Document Date 13 May, 1992	Document Type Notes			
Correspondents / Participants				
Subject / Title Informal Meeting of Executive Directors on Zambia - May 13 1992 - Speaking Notes for Acting Managing Director				
Exception(s) Communications of Executive Directors' Offices				
Additional Comments		The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group. <table border="1"><tr><td>Withdrawn by Salma Berrada</td><td>Date June 13, 2025</td></tr></table>	Withdrawn by Salma Berrada	Date June 13, 2025
Withdrawn by Salma Berrada	Date June 13, 2025			



Record Removal Notice

File Title Zambia - Subject Files - Country Files - Correspondence - Volume 1		Barcode No. 1328884		
Document Date 08 April, 1992	Document Type Board Record			
Correspondents / Participants From: Vice President and Secretary To: Executive Directors and Alternates				
Subject / Title Executive Directors' Meeting - April 7, 1992 - Consultative Group Meeting for Zambia March 23-24, 1992				
Exception(s)				
Additional Comments Declassification review of this record may be initiated upon request.		The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group. <table border="1"><tr><td>Withdrawn by Salma Berrada</td><td>Date June 13, 2025</td></tr></table>	Withdrawn by Salma Berrada	Date June 13, 2025
Withdrawn by Salma Berrada	Date June 13, 2025			

OFFICE MEMORANDUM

4/8



DATE: April 7, 1992

TO: Mr. Dirk T. Mattheisen, SECGE

FROM: Stephen M. Denning, Director, Southern Africa Department

EXTENSION: 34035

SUBJECT: ZAMBIA: CG Meeting, Report to the Executive Directors

At the conclusion of the oral report on the Zambia CG meeting this morning, Mr. Langley commended the Bank for its efforts on behalf of Zambia, and asked that my statement be circulated to the EDs. I am attaching the statement for circulation.

cc: Messrs. E.V.K. Jaycox (o/r), E. Lim, A. Karaosmanoglu, P. Patel (o/r), J. Kisa, J. Todd, C. Helman, D. Cook (o/r), I. Sam, R. Grawe, A. Aksoy
Mmes J. Armitage, J. Edstrom, P. Pomerantz

CONSULTATIVE GROUP MEETING ON ZAMBIA

PARIS, MARCH 23-24, 1992

REPORT TO THE EXECUTIVE DIRECTORS

STEPHEN DENNING

DIRECTOR, SOUTHERN AFRICA DEPARTMENT

Mr. Chairman,

The Zambia Consultative Group meeting took place in Paris on March 23-24, 1992. The mood was frank and optimistic.

The strong commitment of Zambian authorities to implementing the adjustment program was recognized. In the four-and-a-half months since coming to office, the new Government has established a short but distinguished track record. Donors welcomed Government indications of commitment to deepening and vigorously pursuing structural reforms, and its emphasis on implementation, particularly in privatization, civil service reform, public sector wage restraint, improvements in fiscal management, liberalization of agricultural marketing, and foreign exchange management. In some areas, an acceleration of implementation is envisaged.

Despite the encouraging tone of the meeting, the effects of the drought threaten to jeopardize continued implementation of the program. The Government estimated that Zambia would need to import about 900,000 metric tons of cereals (primarily maize) at an estimated cost of around US\$300 million. Donors recognized that the macroeconomic targets specified in the PFP would inevitably be affected by the shortfall in agricultural production, the likely contraction in domestic demand, and the associated fall in Government revenue. Unless full funding of drought requirements was secured, investment levels and economic growth prospects would be in jeopardy.

Many donors expressed concern that the policy framework might be too ambitious under the prevailing circumstances. They welcomed the approach of the IMF in setting only six-month interim benchmarks and planning to agree on targets for the second half of the year only after the maize situation and its financing were clearer. Supply constraints in the economy would limit the possibilities for real growth and restructuring. The need for effective macroeconomic stabilization focussing on demand management, especially expenditure restraint, was greatly increased under drought conditions. Restraint on aggregate expenditure, in the face of high inflation, could result in increased hardship, as the purchasing power of the incomes of the poor got eroded.

Recognizing these risks, donors acknowledged the imperative of making extraordinary efforts to support Government actions.

Zambia's 1992 external financing requirements are large -- around US\$1.4 billion, excluding the drought. This is around US\$300 million larger than a year ago, owing to declining copper receipts, and the debt service arrears carried over from 1991. With the additional drought requirement of US\$300 million, the overall requirements are US\$1.7 billion, i.e. US\$600 million larger than they were a year ago.

Despite this large need, pledges did meet the non-drought requirements of the program. This in itself was quite an extraordinary accomplishment, and reflects the unusual effort that the donor community has been willing to make in support of Zambia's economic reform and restructuring.

However, when taking into the additional drought requirements, there was still a remaining financial gap of some US\$300 million. Moreover, there is a problem in the second quarter of 1992, where pledges were inadequate to meet the extraordinary requirements flowing from the drought.

At the meeting it was agreed that donors would within three weeks consult with their respective headquarters and determine the magnitude of additional resources that they could bring to the table, and the extent to which disbursements can be brought forward to the second quarter. These results are to be communicated to the World Bank, by Friday, April 10.

Although it is still too early to say precisely how this process will conclude, I can say that preliminary indications are encouraging and progress is being made towards closing the remaining financial gap.

Thank you.

April 7, 1992 2:10pm

OFFICE MEMORANDUM

DATE: March 20, 1992

TO: Mr. Michel Camdessus, Managing Director, IMF

FROM: Lewis T. Preston, President, World Bank

EXTENSION: 3-4858

SUBJECT: ZAMBIA PFP

The Committee of the Executive Directors of the Bank and IDA discussed the paper entitled "Zambia Policy Framework Paper, 1992-1994" on March 17, 1992. Attached for your information is a summary of the main points of that discussion.

Attachment

lim

ZAMBIA: Policy Framework Paper, 1992-1994

Summary of Discussions by the Committee of the Whole March 17, 1992

1. The COW commended the Government's prompt actions in its first four months of implementing the economic restructuring program. Several speakers welcomed the increased reliance on the private sector.
2. Some speakers noted the poor track record of the previous Government and pointed to the risks that this had for the implementation of the current program. It was noted that early and aggressive action in implementing the program would be important to warrant credibility for the program.
3. Concern was expressed as to whether some of the macroeconomic projections were realistic.
4. The Directors expressed concern about the serious drought affecting the region that is likely to add \$200-300 million in food imports to the estimate of Zambia's external financing gap described in the PFP.
5. The speakers commended the managements of the Bank and the IMF for their flexibility in considering extraordinary assistance to Zambia at this time, though it was noted that additional assistance should be accorded only when a longer track record of implementation is established.
6. The Executive Directors expressed concern over the Government's commitment to the privatization program and urged that concrete goals be set and monitored and that significant progress be demonstrated soon.
7. The Executive Directors emphasized the critical importance of the Government holding to a firm line on fiscal policy in general and on wage negotiations in particular because controlling inflation will be essential to a resumption of economic growth. Directors noted with satisfaction the progress made towards phasing out maize and fertilizer subsidies.
8. The Executive Directors noted that rapidly increasing food prices and decreasing public sector employment will add considerably to individual hardships. The Government's policies in the social action program area will be essential for ensuring the political sustainability of the program.
9. Clarifications were asked for the timing and scope of the parastatal and civil service reforms.



Record Removal Notice

File Title Zambia - Subject Files - Country Files - Correspondence - Volume 1		Barcode No. 1328884		
Document Date 23 March, 1992	Document Type Board Record			
Correspondents / Participants From: The Deputy Secretary To: Executive Directors and Alternates				
Subject / Title Committee of the Whole March 17, 1992 - Summary of Discussions on Zambia				
Exception(s)				
Additional Comments Declassification review of this record may be initiated upon request.		The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group. <table border="1"><tr><td>Withdrawn by Salma Berrada</td><td>Date June 13, 2025</td></tr></table>	Withdrawn by Salma Berrada	Date June 13, 2025
Withdrawn by Salma Berrada	Date June 13, 2025			

ALL - I N - 1 N O T E

DATE: 19-Mar-1992 01:12pm

TO: Edwin Lim

FROM: Stephen Denning, AF6DR

EXT.: 34035

SUBJECT: Zambia PFP: summary of discussions

AKK
Are it we getting confused between minutes and summary? The summary is ours; and a composite of ED views. Unless the substance is wrong there should be nothing to argue about.
ES & SS
KYI
3/19

This EM is intended to clarify the status of the Summary of Discussions of the CoW on the Zambia PFP.

The CoW discussion lasted almost two hours and was generally very supportive, with only the French ED raising questions as to the level of IDA assistance (an issue not covered in the PFP itself) and noting that actual approval of the assistance would require a longer track record -- a point we agree with, in that we will only be proposing the assistance in some three months time.

We were ready with a draft summary of discussions at the close of the CoW meeting which I or Mr. Preston could have read out to the EDs. It was prepared rapidly in the midst of the discussions. Mr. Preston however announced that the summary would be circulated later in writing.

We sent forward a slightly modified version of our original summary which we believe to be a reasonable capturing of the flavor of the discussion, although obviously given the time constraints not every nuance was reflected.

Mr. Karaosmanoglu thought that the first paragraph might be too positive, and we changed that in the second draft that you signed yesterday.

In the meantime, the French Alternate obtained a copy of the second draft from our staff. This was a breach of procedure and our staff should not have given him the draft. I have asked the staff to ensure that this does not happen again.

Nevertheless the sharing of the draft also revealed a further concern that some nuances of the French position were not fully captured in paragraph 5. Thus he urged that EDs had commended the "flexibility" but not necessarily the "initiative" of the Bank and Fund managements. He also urged that his point, which was emphasized by the fact that the minutes mention "one speaker", was not the scope of the measures supported by adjustment but rather that there be a track record of implementation at the time of decision. I said that we would take care of these points in the oral presentation to the IMF

Board this afternoon. He said that on this basis he was satisfied, and regarded the matter as closed. He said he felt that it would be more helpful in future if the minutes could be read out to the CoW at the time so that any corrections of nuances could be done on the spot, but that this was a process point for the future.

We have also amended the written version of the Summary which are being sent forward for signature and in due course submission to the IMF Board.

Please let me know if there any further questions on this matter.

CC: Attila Karaosmanoglu
CC: TIMOTHY THAHANE

(ATTILA KARAOSMANOGLU)
(TIMOTHY THAHANE @A1@EDSEL)

✓
A L L - I N - 1 N O T E

DATE: 17-Mar-1992 04:36pm

TO: Attila Karaosmanoglu (ATTILA KARAOSMANOGLU)

FROM: Stephen Denning, AF6DR (STEPHEN DENNING)

EXT.: 34035

SUBJECT: Zambia PFP

My apologies again for not attending the pre-Board meeting this morning for the Zambia PFP, owing to a communications mix-up. We will make sure that this doesn't happen again.

No questions had been received from EDs on the Zambia PFP prior to the meeting.

The discussion of the PFP at the Committee of the Whole was very supportive, with a number of the major shareholders including UK, US, Netherlands and Canada strongly endorsing the extraordinary support announced by the Bank and IMF managements in preparation for the CG.

Most of the interventions suggested that the PFP objectives were already rather ambitious, and that care should be taken not to push the new government too fast, particularly in the middle of a devastating drought. (The PFP had been prepared before the drought.) Only the French representative cautioned about ensuring that the policy actions by Zambia warranted the extraordinary financial support envisaged by Bank management.

CC: Edward V.K. Jaycox o/r
CC: Edwin Lim

(EDWARD V.K. JAYCOX)
(EDWIN LIM)

The World Bank/IFC/MIGA
O F F I C E M E M O R A N D U M

DATE: March 19, 1992 09:12pm

TO: Attila Karaosmanoglu

(ATTILA KARAOSMANOGLU)

FROM: Stephen Denning, AF6DR

(STEPHEN DENNING)

EXT.: 34035

SUBJECT: Zambia: developments in the IMF

A serious problem has come up: the deal with the IMF management aimed at filling the Zambia gap seems to have come unstuck as a result of the IMF Board discussion of the PFP this afternoon. If it is convenient, I would appreciate if I could meet with you tomorrow (Friday) morning to figure out what to do. (The CG starts in Paris on Sunday night, and I am scheduled to leave the Bank for Paris lunchtime tomorrow.)

1. What happened at the IMF Board

As part of the opening, Mr. Erb shared with the EDs the same position he had shared with the shadow support group on March 13, i.e. that Fund management was considering a proposal to reduce Zambia's payments in CY 1992 by \$100 million provided that the Bank would add \$100 million in disbursements, that the program stays on track, and that the donor effort would suffice to fill the remaining gap. This would, of course, be subject to Board approval at the appropriate time. He was sharing it informally so that they could react if they wanted to and so that they would be aware of the position that Fund staff would be taking at the CG.

The PFP itself was uncontroversial.

However the \$100m deferment, which had been unveiled last Friday, generated opposition:

- Against were the French, Italian, Belgian, and German chairs who did not want the Fund to stake out any such specific position. They could not endorse any specific proposal at this time, and they did not want to be presented with a fait accompli later.

- In favor were the British and Canadian chairs who strongly supported the Erb proposal. The US also supported but with misgivings. The Japan chair did not address the question directly. Most of the others were generally supportive of the proposal.

The second point concerned the \$12 million in special charges which was to be part of the \$100 million deferment. This was more strongly opposed as premature since there was a discussion on this point scheduled for April 17, and no interim commitments should be made by IMF management.

Mr. Erb said all the right things in terms of why this indication of flexibility on the Fund part was essential to the success of the CG and why it was the best way to ensure that they received as much as they could in the short-term while protecting their longer term position. Otherwise there would be pressures for the Fund to do even more, and if the CG was a failure, the Fund might get nothing. The opposition nevertheless remained strong.

IMF staff believe, after talking to Mr. Erb after the meeting, that the IMF management intention is to change their tables to put the full \$119 million of debt service arrears back in and raise the gap, i.e. an unconstructive wait-and-see approach.

2. Suggested Bank action vis a vis the IMF

While the IMF management obviously has a problem, it still has options as to how to present its position. Since the sequence of events and positions of all players are known to all participants, the question is how the IMF management presents the situation. Our recommendation is that senior Bank management call Mr. Erb and try to obtain the best possible presentation of the situation.

The best presentation will be for the IMF management to continue to show its tables and intentions unchanged, though perhaps making clearer that the result is contingent on eventual Board approval.

The worst presentation will be for the IMF management to back down and adopt the position of the vocal but influential minority, with no indication of any intention to waive any charges, with the implicit but futile hope that the donors fill a huge gap.

We should make clear that the latter tack will have serious adverse consequences at the CG, with many donors conditioning their pledges on a more responsive stance by the IMF. More importantly, it risks donors sliding into a wait-and-see mode in terms of disbursements, with disastrous consequences for the cash-strapped Zambian economy in the grip of the worst drought in a century, and may well prevent Zambia staying current with 1992 IMF charges or ever getting back into the Rights Approach. At best, it will win the unanimous opprobrium of the donor community, for acting so egocentrically in respect of one of the few democratically elected governments in Africa, that has done everything right in its admittedly short tenure in terms of macro

management.

The donors will be aware of all of the discussion at the Fund Board. No one at the IMF Board suggested that the imports number be reduced, and no one suggested that the Fund say they are unwilling to consider such reductions. They just didn't want to appear to be negotiating their contribution to the gapfill exercise as if they were just another donor. I expect all of this has much to do with Fund policies to countries other than Zambia.

A possible backup position to mitigate a difficult situation would be to get the Fund to prepare a separate set of tables with \$100 million each from the Bank and Fund (the composition of which for the Fund would be undefined). It could be arranged for a donor to ask question of the staff from the floor suggesting that for the benefit of the donors' considerations, such tables be prepared on the clear understanding that they are only being presented as a computational aid with no commitment by the Bank and Fund to produce these amounts. This would help, but not much.

3. What should the Bank stance be?

Our recommendation is to stick firmly with our position that our additional \$100 million is contingent on the IMF deferring an equivalent \$100 million.

Since all participants know that this is the Bank management position, and that there is support from our Board for it (with the possible exception of the French), there seems no reason to conceal it. If we withdraw even our conditional pledge of an additional \$100 million, this will give the impression that we are falling in lockstep with the conservative minority of the IMF Board, which is hardly a public posture we want to be caught in.

Hence our recommendation is to stick with our existing stance, and continue to present our conditional offer of an increment. This will not jeopardize our maneuvering room, since in any event, the IDA adjustment operation is not planned for Board presentation till June, and we can continue to condition Board presentation on IMF action.

Maintenance of the Bank stance may encourage some donors to step into the breach, but there remains an extremely serious risk that there will be sufficient discouragement to the bilaterals to cause the CG to abort, with either a significant shortfall in pledges or a cash flow problem for Zambia or both.

The main effort in our view should be to persuade the IMF management to put the best possible face on its position to encourage a strong enough bilateral response to help Zambia get

through the next few months, until the IMF management can sort out its problems with its Board.

I would appreciate the opportunity to discuss these issues tomorrow morning, if that is compatible with your schedule.

CC: Ernest Stern
CC: Edward V.K. Jaycox o/r
CC: Edwin Lim
CC: Gisu Mohadjer
CC: Jane Armitage

(ERNEST STERN)
(EDWARD V.K. JAYCOX)
(EDWIN LIM)
(GISU MOHADJER)
(JANE ARMITAGE)

FORM NO. 75
(6-83)

THE WORLD BANK/IFC

ROUTING SLIP		DATE: 3/18/92	
NAME		ROOM NO.	
Mr. Lewis T. Preston, EXC			
Through Mr. A. Karaosmanoglu <i>AK</i>			
Managing Director			
APPROPRIATE DISPOSITION		NOTE AND RETURN	
APPROVAL		NOTE AND SEND ON	
CLEARANCE		PER OUR CONVERSATION	
COMMENT		PER YOUR REQUEST	
FOR ACTION		PREPARE REPLY	
INFORMATION		RECOMMENDATION	
INITIAL		SIGNATURE	
NOTE AND FILE		URGENT	
REMARKS: Re: ZAMBIA PFP - Summary of Discussions by the Committee of the Whole - March 17, 1992.			
FROM: E. Lim, Acting, VP, AFR <i>EL</i>		ROOM NO.: J6-157	EXTENSION: 3-4848

OFFICE MEMORANDUM

DATE: March 20, 1992

TO: Mr. Michel Camdessus, Managing Director, IMF

FROM: Lewis T. Preston, President, World Bank

EXTENSION: 3-4858

SUBJECT: ZAMBIA PFP

The Committee of the Executive Directors of the Bank and IDA discussed the paper entitled "Zambia Policy Framework Paper, 1992-1994" on March 17, 1992. Attached for your information is a summary of the main points of that discussion.

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lim

ZAMBIA: Policy Framework Paper, 1992-1994

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2. Some speakers noted the poor track record of the previous Government and pointed to the risks that this had for the implementation of the current program. It was noted that early and aggressive action in implementing the program would be important to warrant credibility for the program.
3. Concern was expressed as to whether some of the macroeconomic projections were realistic.
4. The Directors expressed concern about the serious drought affecting the region that is likely to add \$200-300 million in food imports to the estimate of Zambia's external financing gap described in the PFP.
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9. Clarifications were asked for the timing and scope of the parastatal and civil service reforms.

ZAMBIA: Policy Framework Paper, 1992-1994

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5. The speakers commended the managements of the Bank and the IMF for their initiative and flexibility in making extraordinary assistance to Zambia at this time, though one speaker urged that care be taken to ensure that the extent of the assistance be reflected in the scope of the policy measures that were being supported.
6. The Executive Directors expressed concern over the Government's commitment to the privatization program and urged that concrete goals be set and monitored and that significant progress be demonstrated soon.
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2/28
✓
Hob.

International Bank for Reconstruction and Development
FOR OFFICIAL USE ONLY

DECLASSIFIED

JUN 04 2025

SecM92-246

FROM: Vice President and Secretary

WBG ARCHIVES

February 27, 1992

ZAMBIA: Economic and Financial Policy Framework, 1992-94

1. Attached is a Policy Framework Paper for Zambia. It was prepared jointly by the Government of Zambia and the staffs of the Fund and the Bank. The policy framework outlines the Government's objectives for the medium term; it reflects agreements reached between the Government and the Fund and the Bank on the adjustment program.
2. The paper also indicates the estimated external financing requirements for 1992-1994. A part of this requirement is expected to be met by future IDA lending. The volume and timing of such lending, both project and adjustment related, will continue to be dealt with in the usual manner under the Bank's normal procedures.
3. This document will be considered by the Executive Directors meeting as the Committee of the Whole on March 17, 1992.

Distribution:

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be referred to Mr. Todd (Ext.35056)

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ZAMBIA

Economic and Financial Policy Framework, 1992-94

Prepared by the Zambian authorities in collaboration with the
staffs of the Fund and the World Bank

February 26, 1992

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I. Introduction

1. The people of Zambia inaugurated a new economic and political era when they went to the polls on October 31, 1991. By an overwhelming majority, they voted into power a party--the Movement for Multiparty Democracy--committed to an open political system in which human rights would be protected and to an open market economy in which private initiative would be encouraged and rewarded.

2. This document describes the strategy and specific courses of action the MMD Government intends to follow in stabilizing and restructuring the economy. The economic strategy recognizes the importance of market forces and reflects the conviction that Government should not undertake what the private sector can do at least as well. It is grounded in the view that individual initiative and freedom in the market place and in the political arena are essential for a thriving economy and a responsive political system. These beliefs are fortified by the conviction that free markets reinforce political freedoms, and vice versa.

3. The present administration intends to enter into policy commitments only if it is convinced that they can be fulfilled. The decision to reduce mealie meal subsidies substantially after only six weeks in office is a clear and early manifestation of the determination to turn the economy around.

4. The Government also attaches a high priority to relieving the social problems that have accompanied the economic decline and to ameliorating the impact on the most vulnerable of the disruptions that will accompany economic restructuring. The primary goal will be to reduce unemployment, expand resources to improve health, education, and other basic social services, and meet the income and other needs of the most vulnerable members of society. In addition, to alleviate the most pressing social problems in the immediate future, the Government will undertake a range of targeted support activities to protect the most vulnerable groups.

5. The reasons for Zambia's economic decline over the past two decades have been well documented. The deterioration stemmed in part from the country's heavy dependence on copper, which in 1989 accounted for 87 percent of total exports and contributed about 10 percent to GDP. Although Zambia has considerable potential in noncopper activities, notably agriculture, this potential has never been adequately exploited.

6. The vulnerability of the Zambian economy to developments in the international copper market was evident during the 1970s and much of the 1980s when a protracted decline in metal prices, in conjunction with a decline in copper output, contributed to a fall of one third in per capita

GDP. Rather than take steps to halt the decline by diversifying production through market-oriented investments and pricing structures, policies were geared toward maintaining consumption in anticipation of an eventual upturn in the copper market. As low copper prices persisted, however, large and unsustainable external and internal imbalances developed, savings and investment ratios fell, and external debt rose sharply. Effective use of existing productive capacity was hampered by extensive government involvement in the form of price regulation, subsidies, and exchange and trade controls, and by the presence of a large parastatal sector that dominated all areas of the economy with the exception of agriculture and banking. Several attempts at economic reform were made during this period, but--because of poor policy implementation, weaker-than-anticipated copper prices and, in some instances, shortfalls in donor assistance--none met with lasting success.

7. By late 1988, Zambia was facing a rapidly deteriorating fiscal position, accelerating inflation, chronic shortages of foreign exchange, and a proliferation of black market activities. Severe difficulties were also encountered in servicing external debt obligations, much of which had been contracted on commercial terms. It was against this background that the previous Government launched the adjustment program described in the first annual policy framework paper (PFP), which was prepared in mid-1989.

8. Implementation of the first PFP is described in the Appendix. An updated PFP was prepared in February 1991, and this formed the basis for an Economic Recovery Credit from the World Bank, the first tranche of which was disbursed in March 1991, and a rights accumulation program (the first of its kind), which the Fund Board endorsed in April 1991. Performance under the rights program is also described in the Appendix.

II. Overview of Policy Strategy

9. While the adjustment strategy for 1992-94 calls for a wide range of policy and institutional changes, a prerequisite for success is establishing macroeconomic stability. The fiscal and monetary restraint that the situation demands will not come easily, since copper prices now appear to be falling and copper production is expected to continue to decline. The resulting contraction in foreign exchange earnings and mineral taxes will have to be offset by a combination of economizing on imports, increasing nontraditional exports, and achieving budgetary savings.

10. Zambia must reverse its long economic decline and restore the momentum of growth. This will require fostering saving and investment and promoting diversification. The program will scale down government intervention, stabilize financial and fiscal conditions, encourage foreign investment, and create an overall environment in which the private sector can prosper. The objective is to achieve positive real per capita growth as quickly as possible while bringing inflation down to an acceptable level and to set the stage for rapid growth in the nonmetal sectors during the second half of the

decade. At the same time, resources are expected to shift to more labor-intensive activities, including smallholder agriculture and small-scale industry and services, so that employment expands faster than GDP.

11. Past attempts to regulate prices--including interest rates and the exchange rate--led to resources being allocated to activities in which Zambia does not necessarily have a comparative advantage, thus impeding the diversification process. Moreover, the existing capital stock and infrastructure remain poorly utilized and seriously run down. Through liberalizing markets, removing impediments to resource mobility, and encouraging greater private sector involvement, the adjustment strategy seeks to promote those activities in which Zambia can compete effectively in international and domestic markets. The Public Investment Program (PIP) will accordingly give priority to rehabilitating the components of existing capacity and infrastructure that are integral to this effort.

12. Zambia is, and will remain for some time, heavily dependent on external assistance. The Government is aware that ensuring an adequate net flow of assistance depends on its own efforts, including steadfast implementation of the economic reform program and normalization of relations with external creditors. But Zambia cannot rely indefinitely on exceptional levels of foreign aid. Investment and growth can be sustained in the long run only by mobilizing sufficient domestic savings. The Government is therefore determined to take measures to cut fiscal deficits, achieve positive real interest rates, and reduce the import intensity of production and consumption.

13. Even the best adjustment policies, however, will not restore vigorous growth without a reduction in the burden of Zambia's enormous external debt. As the Government demonstrates its commitment to economic reform, external creditors will be asked to provide early debt relief on extraordinary terms. Success on this front is a key to securing a prosperous and stable future for Zambia.

III. Macroeconomic Framework, 1992-94

1. Objectives

14. The program objective is to achieve real GDP growth rates of 2 percent in 1992, 3 percent in 1993, and 4 percent in 1994 (Table 1). These growth rates will not permit per capita consumption to increase until 1994, in part because of the anticipated deterioration in Zambia's terms of trade and in part because of the needed increase in investment. However, even these modest rates of GDP growth represent a marked departure from the decline in previous years. This reversal should be possible because Zambia will have both the resources and the policies for renewed growth. There is ample agricultural land of good quality available. There will also be adequate amounts of both skilled and unskilled labor, and significant portions of the industrial sector have unused capacity. The availability of both credit and

foreign exchange is expected to increase in real terms to the nongovernment sector. Add to these factors the anticipated improvements in the allocation and efficiency of public spending, the liberalization of markets, and the reduction in government regulation, and the opportunities for growth should be considerable. In order for this growth to be sustainable in the medium and longer term, the program aims for an increase in gross investment from an estimated 13.5 percent of GDP in 1991 to 20.5 percent of GDP by 1994. This will be facilitated by the stance of both fiscal policy, which will seek to increase public savings and shift financial resources to the private sector, and monetary policy, which will seek more attractive returns to savers by offering positive real interest rates. To meet the investment and growth targets, domestic savings mobilization will need to be supplemented by substantial net inflows of foreign assistance.

15. The most immediate problem of macroeconomic policy is the unfinished business of conquering inflation. The objective is to bring the December-to-December inflation rate down from about 100 percent in 1991 to 45 percent in 1992, 15 percent in 1993, and 5 percent in 1994. The Government will maintain strict fiscal and monetary discipline to achieve these targets. In doing so, it will demonstrate its determination to reduce inflation.

2. Fiscal policy

16. As a cardinal principle of its macroeconomic stabilization program, the Government is committed to ending recourse to inflationary domestic borrowing to finance public spending. To achieve this, the primary budget balance (excluding grants) is targeted to show a deficit of no more than 2 percent of GDP in 1992 (Table 2). The budget is expected to be balanced in 1993 and [and to show a surplus of 0.5 percent in 1994.]

a. Revenue measures

17. Comprehensive tax reform will be a cornerstone of the fiscal program. The objective is to establish a revenue-generating mechanism that is simultaneously more buoyant, more fair, and more efficient than the present system. The income tax reforms introduced in the 1992 budget and planned for the rest of the program period (see paragraphs 41 and 42) are expected to be revenue-neutral, with rate reduction being offset by an expansion in the base. By contrast, the reform of the indirect tax system (see paragraph 43) is expected to raise revenue by about one-half percent of GDP, primarily through measures designed to harmonize and unify import and domestic sales taxation.

18. Nontax revenues have failed to keep pace with inflation in recent years, falling from 1.6 percent of GDP in 1988 to 0.4 percent of GDP in 1991. The Government intends to redress this decline over the program period and restore the ratio to its level in 1988. Accordingly, the level of fees and charges will be adjusted so as to raise 0.4 percent of GDP from this source in 1992. The policy on parastatal dividends outlined in paragraph 38 is also expected to increase revenue. As a result, nontax

revenues are expected to increase to 1.2 percent of GDP in 1992. Despite the continuing slump in mining taxes, total domestic revenue will rise from 17.0 percent of GDP in 1991 to 17.5 percent of GDP in 1992. A concerted effort will also be made to boost revenue from the mining sector through improved management and rapid divestiture of loss-making operations.

b. Expenditures

19. The brunt of fiscal adjustment for 1992 will be borne on the expenditure side. The objective is to cut current noninterest expenditure as a percent of GDP from 16 percent in 1991 to 14 percent in 1992, even as recurrent departmental charges (RDCs, i.e., operating costs other than personnel) rise in real terms. In 1993 and 1994 the compression and restructuring will continue, though at a slower pace. This fiscal plan requires major changes including reform of the public and parastatal sectors, devolution of authority to local governments, determined control of commitments and expenditures, and, above all, the phased elimination of subsidies.

20. The Government's aim is to have a smaller, more efficient, and better paid civil service. To achieve this, the Government will proceed with the civil service reform (described in paragraphs 45 and 46). The Government intends to use the savings realized from personnel reductions to improve the conditions of service, especially for skilled and professional personnel. Personal emoluments will be limited to 4.2 percent of GDP in 1992 and beyond. This does not include the cost of the severance package under the civil service reform, which would be limited to K 1.8 billion (0.4 percent of GDP) in 1992. With regard to RDCs, the program provides for a reversal of the trend of deteriorating public services, with expenditure specifically targeted at agriculture, health, and education. The decline in roller meal subsidies and the elimination of breakfast meal subsidies, combined with the termination of the mealie meal coupon scheme at the end of 1991 and the ending of fertilizer and maize handling subsidies, should limit total maize and fertilizer subsidies to 1.7 percent of GDP in 1992 (compared with 3.4 percent in 1991) and eliminate them entirely over the program period (see paragraph 52).

21. With regard to transfers to district councils, the Government's intention remains to realize savings by granting the councils more autonomy. District councils are now free to set charges for most local activities (excluding health and education) at levels they think appropriate. The Government intends to continue to provide grants only to the smaller councils beginning in mid-1992. In time, it is expected that ways will be found to reduce the dependency of the smaller councils as well. A further source of budgetary savings is expected to result from the delinking of political parties from the Government's budget. These factors, combined with wage policies, are expected to reduce outlays on transfers and pensions to 1.9 percent of GDP in 1992 from 2.5 percent in 1991.

22. The Government intends to establish budget headings for each of the defense and security wings so as to introduce greater transparency to military expenditure. Besides permitting closer scrutiny and control of these expenditures, such action will facilitate the extension of the program of civil service reform to the military; as a result, military expenditure is expected to decline in real terms over the program period.

23. Capital expenditure, excluding donor funds on-lent to parastatals, will be further contained in 1992 at 3.9 percent of GDP, with resources concentrated on a core program of rehabilitating infrastructure and completing ongoing projects. (See discussion of the PIP in paragraphs 47 to 49). New projects have been subject to strict cost-benefit criteria. In line with the Government's objective of reducing the subsidization of parastatals, domestically financed net lending to these bodies will be less than 0.5 percent of GDP in 1992.

3. Monetary policy and interest rates

24. Structural reform and durable growth can only proceed once inflation has been brought firmly under control. The inflation target of 45 percent for 1992 therefore represents a significant reduction in inflation compared with the previous year. To meet this, the Bank of Zambia has established a target for broad money growth of 25 percent for 1992. Particularly in view of the carry-over effect of rapid monetary expansion that occurred in the second half of 1991, the money target is lower than the inflation objective since it is anticipated that it will take some time for inflation to decelerate as monetary policy is tightened. The Government believes that both targets are feasible based on the rate of inflation through the third quarter of 1991. Fiscal discipline will be crucial in achieving the monetary target and ensuring that sufficient funds are available to fuel the economic recovery of the nongovernment sector. The Government will also make active use of available monetary policy instruments, such as changes in liquid asset requirements and adjustments in interest rates on government debt. Over the longer term, the Government intends to develop a capital market that will enable monetary control to be effected indirectly through the purchase and sale of government debt rather than through reliance on reserve and liquid asset requirements.

25. So long as interest rates remain negative in real terms, inflation cannot be effectively overcome, sufficient investment will not take place, and investment will not be allocated efficiently. To raise the real return on holding money and other financial assets, the interest rate structure was increased recently by 5 percentage points, and the Government remains committed to achieving positive real rates of interest. The maximum bank lending rate, including up-front fees, now corresponds to the rate of inflation targeted for the first quarter of 1992. Further increases may be necessary should inflation turn out to be higher than targeted. To encourage savings, efforts will also continue to be directed at raising bank deposit rates relative to lending rates. To this end, in the second half of 1991 reductions in statutory reserve requirements (which legally are

non-interest-bearing) were matched by increases in liquid asset requirements (which are interest-bearing). Further such adjustments will be undertaken during the course of 1992.

26. The policy of imposing a strict limit on the kwacha created as a result of debt swaps will remain in effect in 1992. In addition, the Bank of Zambia will continue to operate the mechanism established in 1992 whereby it levies an administrative charge on debt swaps to ensure that they take place at market-related rates of discount and that Zambia's external debt is reduced by the maximum amount possible. Debt buy-backs will be undertaken only to the extent that foreign exchange is made available from donors or creditors for this specific purpose.

4. External sector policies

27. The Government has made major strides in liberalizing the exchange and trade system and will continue to make active use of external sector policies to help achieve the stabilization and structural transformation of the economy. The authorities are confident that as peace and prosperity return to Southern Africa, Zambia can compete in foreign markets-- particularly in manufacturing, agriculture, gemstones, and tourism. In addition to providing an environment that is conducive to private initiative, the centerpiece of the strategy for expanding nontraditional exports by at least 10-15 percent a year over the next decade is an exchange rate policy that provides adequate profit opportunities for exporters, while also helping to rationalize the demand for imports, promote the efficient allocation of scarce foreign exchange, and improve incentives for private capital inflows. To that end, the kwacha was devalued by 30 percent on January 31, 1992. The Government's objective is to complete the process of moving the official exchange rate to a level that would permit the open general license system (OGL) to be shifted to a negative list system as soon as possible, and coverage of the OGL to widen from about 90 percent to at least 95 percent of base period imports by mid-1992, provided Zambia receives adequate external assistance. The Government will manage the exchange rate to maintain a balance between supply and demand and, over the next year, will increasingly move toward a market-determined rate. In addition, the duty drawback system will be streamlined to make it more effective, and a bonded warehouse scheme will be developed.

28. An active exchange rate policy will be supported by disciplined financial policies and complemented by structural measures--including tariff reform, elimination of barriers to exports, rebuilding infrastructure for trade and tourism, and promoting foreign investment. The normalization of relations with external creditors, in ways consistent with Zambia's balance of payments situation and prospects, also will help to improve the investment climate and restore access to trade credit.

IV. Structural Reform

29. Macroeconomic stabilization is essential for restoring self-sustaining growth, but it is not sufficient. The Government believes that restoring long-term growth will also require raising saving and investment, improving efficiency, stimulating nontraditional exports, and fundamentally restructuring the economy to end its dependence on copper. The engine of growth must be private initiative, guided by market incentives. Government policy will be redirected at creating an environment in which initiative, entrepreneurship, and effort can thrive. Considerable progress has already been made in liberalizing the economy and improving incentives for restructuring and growth. The Government will consolidate the gains from measures taken earlier, while broadening and deepening the program of reforms.

1. Role of the private sector: Competition and investment policies

30. Economic growth and efficiency in Zambia will require a vital private sector. Private entrepreneurs will be encouraged to participate freely in economic activity, and Government will not pre-empt or inhibit business opportunities. Investor confidence has been poor because of excessive regulation and on-again, off-again macroeconomic policies. In order to create an improved climate for private investment and private sector activity, the Government is committed to setting a more consistent path for macroeconomic policy. The Investment Act of 1991 is being implemented immediately with the establishment of an Investment Center and Board. Provisions of that act are being put into effect to assure private entrepreneurs that their activities and assets are safe from government interference and expropriation.

31. Too often, the Government has placed legal and administrative obstacles in the path of business and commerce. This red tape must be cut. In addition to opening the one-stop Investment Center, the Government will identify during 1992 all formal and informal requirements faced by business in the process of gaining approval for new investment or other business decisions in order to streamline the process.

32. Foreign assistance programs are largely conducted on a government-to-government basis and have so far not provided direct support of the private sector, except for balance of payments support, which directly provides foreign exchange for imported intermediate goods and spare parts. The Government is encouraging donors to provide project aid and technical assistance in ways that will contribute more directly to growth of the private sector.

33. The Government intends to strengthen the privatization program by providing a legal status, a policy statement, and a plan of action. The Government will present a privatization bill to Parliament in April 1992. The Government plans to proceed rapidly with privatization once Parliamentary approval is obtained. It will proceed with the sale of the

ten firms offered last year as soon as the legal basis is established, and additional and much larger companies will be available for bidding later this year. The Government expects that most parastatals will be privatized in the next five years. Priority will be given to the maize mills taken over by Government in 1986. The privatization program will distinguish between simple commercial and trading parastatals and more complex manufacturing entities whose valuation will require great care. The former can be disposed of without lengthy preparation; the latter will take more time. Responsibility for the privatization process has been transferred from the parastatal holding company (ZIMCO) to the Ministry of Commerce and Industry. In order to facilitate trading in shares, legislation will be proposed to Parliament. In order to encourage further investment in a highly productive sector, a new Mining Code will be developed and presented to Parliament in 1992. Finally, district councils will be urged to divest themselves of the commercial enterprises they operate.

34. The Government will encourage greater competition in the provision of those financial services, such as insurance, pensions, and building society funds, that are presently controlled by state monopolies. This will be accomplished by removing monopoly rights from the state enterprises, and in some cases by privatizing the enterprises themselves. In view of this privatization, the Government will introduce antimonopoly legislation to guarantee competition and avoid cartels.

35. Public utilities not immediately on the privatization list will have their services commercialized. In the past, rates of the electricity company (ZESCO), Zambia Railways, and other utilities were restrained by Government without regard to the financial viability of the enterprises. This will no longer be the case. Utilities will be free of day-to-day interference in their management and will no longer receive governmental subventions to offset operating losses. Because they will not be subject to competitive forces that serve to restrain prices and contain costs, however, there will need to be some oversight mechanism for approving prices. During the coming year, the Government will examine alternative mechanisms for setting public utility prices at levels that will provide a fair return on capital and facilitate a sound level of performance, efficiency, and investment.

2. Parastatal reform

36. A parastatal reform program is being undertaken to facilitate the privatization effort. Until parastatals are divested, they must remain financially viable. The Government will no longer subsidize any parastatal. The aims are to eliminate any special advantages for parastatals that may inhibit private competition, to increase parastatals' contribution to government revenues, and to strengthen their ability to compete in domestic and foreign markets.

37. To improve the ability of parastatals to compete, the Government will take steps to shore up their financial and economic performance. On the

basis of financial studies being undertaken on a number of major enterprises, investment and restructuring programs will be evaluated and ways to strengthen managerial and technical capabilities identified. For most parastatals, restructuring investments will be left to the new buyers, but on a very exceptional basis, candidates for privatization may have to be made more attractive through careful investment decisions, particularly emergency rehabilitation measures.

38. To increase parastatal contributions to government revenues, two approaches will be followed. First, beginning with reported income from the 1991/92 financial year, all parastatals will be required to pay dividends directly to the Government; previously, the losses of firms within the ZIMCO group could be offset against the profits of others, thus providing cross-subsidies between ZIMCO parastatals and reducing total tax liabilities. All parastatals will be required to revalue their assets and to determine a realistic value of shareholder funds. On the basis of such revaluations, parastatals will be required to remit a 10 percent dividend to the Government. The result should be a substantial increase in dividend receipts to the Government, compared with prior years.

39. As an additional measure to increase revenue, and one that will also reduce any special advantages they may have been given relative to the private sector, the Government will enforce penalties and interest charges on overdue tax and customs payments by the parastatals. It will not provide transfers or subsidies to parastatals, except in connection with financial restructuring programs for public utilities whose financial viability is at risk. Other parastatals in financial trouble will have to cope by mortgaging assets to qualify for commercial loans, reducing or ceasing operations, selling off assets, or reducing costs. The Government will normally not guarantee commercial debt for such institutions.

40. If parastatals are to make an adequate return on capital and meet tax and dividend obligations, they must, and will, be allowed to set prices as market conditions dictate, irrespective of the product involved. For example, Zimoil raised petroleum prices by 25 percent in January 1992 to cover cost increases arising from the depreciation of the kwacha, and can be expected to make further adjustments as required.

3. Public finances

a. Tax reform

41. Nonwage cash payments, such as the housing allowance, remained untaxed and continued to proliferate in 1991, thereby distorting wage structures and eroding the personal income tax base. Taxing cash allowances forms part of a revenue-neutral reform of the personal income tax introduced in the 1992 budget, with the revenue gained from the base expansion used to reduce marginal rates and substantially increase the threshold level of income escaping taxation altogether. The new personal income tax has broader tax

brackets, a top marginal rate of 35 percent, and a personal tax credit rather than a primary allowance.

42. The Government buttressed the reform of the personal income tax described above by ceasing to allow noncash fringe benefits as deductible business expenses. The associated widening of the company tax base will be offset by a cut in the basic company tax rate from 45 percent to 40 percent beginning April 1, 1992. The Government is undertaking a detailed examination of the structure of the company tax with the intention of implementing a major restructuring in 1993.

43. The sales tax was harmonized and unified in the 1992 budget with a uniform rate of 20 percent now applying to a single schedule of goods and services, whether imported or produced domestically. This implies an increase in the average level of domestic sales tax and is a prelude to introducing a broader based value-added tax in 1993, which will eliminate any rationale for the "uplift factor" for import sales tax. Excise taxes are also being amended in 1992 to apply equally to imports and domestic goods. There will be additional revenue gains over the program period from eliminating the tax- and duty-free status of foreign exchange shops and from limiting sales tax and import duty exemptions.

44. Structural changes in the tax system will also be reinforced by administrative reform. The Government is committed to completing implementation of the Revenue Board in 1992, work on which began in 1991. Even before the Revenue Board becomes operational, the Government will significantly increase tax department budgets, improve conditions of service for tax officers, and tighten enforcement provisions in the tax law. In addition, tax administration will be computerized in 1992. The introduction of master tax files based on taxpayer identification numbers will permit extensive cross-tabulation of taxpayer data, eliminate assessment backlogs and enable administrative resources to be redirected toward collecting current taxes. A donor-funded technical assistance project to achieve these objectives began in early 1992.

b. Civil service reform

45. The effectiveness of Zambia's public service has suffered from the loss of skilled personnel as a result of an erosion of pay in real terms at upper staff echelons. Thus, even after the recent increases, the average salary of the most senior civil servants in real terms is still no more than 50 percent of what it was in 1980 and is now only four times higher than that of lowest paid civil servants, as opposed to over seven times in 1985. At the same time, the size of the public service has grown excessively large--not only surpassing the number of established positions, but also outstripping the capacity of Government to provide a sufficient operating budget to make the public service productive and efficient.

46. To address these public service issues, the Government has embarked on a concerted program of public service reform. The centerpiece of this

program will be the enhancement of incentives to motivate and retain key personnel in technical and managerial positions while reducing the size of the public service. This would include a careful assessment of government implementation capacity, and formulation of appropriate early retirement and retrenchment procedures and compensation packages. The Government will progressively address the restructuring of the public service in the higher priority subsectors to enhance efficiency and performance. In low priority subsectors and for nonessential functions of the Government, the emphasis will be on a reduction in the size of the public service. The Government is also in the process of considering the hiving-off from the government budget of certain departments, commissions, and other bodies that have either become defunct or could survive on their own on a commercial basis. Announcements about these will be made as decisions are made.

c. Structure of public investment

47. The Government has completed the second annual update of the PIP, covering 1992-94. As with earlier PIPs, the new document will serve as a guide to ministerial capital budgets, parastatal investment activities, and mobilization of donor project assistance. The government investment program will be consistent with the fiscal policy targets. Ongoing capital projects will be scrutinized systematically with an eye to terminating low-priority or low-productivity investments, and no new capital projects will be budgeted without strong economic justification.

48. Parastatal investments will also be governed by the PIP and will be based strictly on financial and economic viability. As a condition of Government guaranteeing the necessary foreign loans, the public utilities will have to demonstrate how each of these proposed investments will add to their profitability. For the other parastatals, the new investment will be kept to a minimum and will normally be appropriate only for emergency rehabilitation expenditures or other investment that will pay for itself prior to divestiture. Our firm intention is to reduce government involvement in business activities as quickly and smoothly as possible. Under the new policy, dividend payments will have first claim on profits.

49. Within the government budget, investment decision making in the economic sector will continue to emphasize the following priorities. In agriculture, priority will be given to promoting development of smallholder agriculture through enhancing government capacities to deliver research and extension services, and to provide adequate maize storage facilities for buffer-stock operations. Rapid expansion of cash crops such as tobacco will be emphasized. In transport, investments will focus on restoring and repairing the road and railway network, including feeder roads to outlying agricultural districts. In education and health, the Government will give priority to repairing and rehabilitating existing primary education facilities and primary and preventive health care service facilities.

d. Expenditure control and monitoring

50. Efforts to restructure the public service and improve budgeting will be of little avail if the recording of public expenditure is untimely and inaccurate and the mechanism of expenditure control ineffective. Current reporting requirements cover commitments and expenditures, and the Government will improve implementation of these procedures through training, computerization, and withholding monthly allocations until the use of previous allocations has been satisfactorily reported. In addition, all decisions related to wage and benefits packages for government employees now require the prior consent of the Minister of Finance.

4. Maize and fertilizer

51. The liberalization of maize and fertilizer prices is important not only to reduce the burden of subsidies on the budget but also to improve the structure of incentives to farmers and consumers. The improved geographical pattern of production and the increased efficiency in the growing, transporting, and processing of agricultural crops that will accompany the liberalization of maize and fertilizer markets should help offset the impact on consumers of the phasing out of subsidies.

52. The first PFP set a goal of attaining by 1993 market-based prices for fertilizer, maize, and mealie meal. Although there was limited progress in this area through most of 1991, the new Government took major steps late in the year to adjust producer and into-mill prices for the 1992/93 crop year and to reduce substantially the subsidies on mealie meal. The Government is committed to achieving market-based prices for these products in 1992 (except for a small subsidy on the consumer price of roller meal). The farm-gate floor price for maize will be increased sharply for the next crop year, and will vary inversely with transport costs so as to eliminate subsidies on maize transport. These prices should be sufficient to compete with export demand in all but the most remote areas. Millers will be free to set their into-mill prices according to market conditions. Also late in 1991, roller meal subsidies were reduced by 50 percent and breakfast meal subsidies were cut by 90 percent, leading to price increases of over 100 percent. The Government has since eliminated all subsidies on breakfast meal and will gradually reduce the subsidy on roller meal to 20 percent by December 1992 and phase out that subsidy completely in 1993. The Government will also eliminate all fertilizer subsidies by March 1992.

53. Private traders are now allowed to participate in all phases of maize and fertilizer marketing. Into-mill prices and consumer prices will vary by mill, reflecting such factors as transportation and production cost differences. The Government has also continued to promote more widespread use of hammermills, to increase competition in the milling industry, and to cut down on the need for long distance transportation. The combined effect of all these actions should be to increase competition and efficiency in maize production. In the longer run, improved efficiency and increased production are the best way to stabilize maize prices.

54. Given the vagaries of weather, Zambia's landlocked position, and the scarcity of foreign exchange, however, interruptions in the supply of maize will continue, in the short term, to be a concern of the Government. During 1992, a follow-up to last year's survey of maize stocks and storage facilities will be conducted. Rules for the operation and financing of a maize strategic reserve will be developed in 1992 for implementation in 1993.

5. Land policies

55. It is essential that more land become available for development. To this end, the Government will ensure that the current leasehold system continues. However, in order to maximize security of tenure, the Government will ensure that subject to conditions and covenants of the lease being complied with by the lessee, the lease shall be deemed to have been extended for a further 99-year period upon the expiration of the initial 99-year lease period. The Ministry of Lands will also accelerate the land survey program in order to reduce the backlog in the issuance of title deeds and will overhaul the land titling system to speed the access to land by new investors.

6. External trade

56. Excessive trade protection diverts resources toward high-cost, uncompetitive producers, at the expense of more efficient and more outward-looking development. The Government intends to move to a more uniform, lower-rate tariff regime. Given the importance of import duties as a source of budgetary revenue, and to ease the transition, tariffs will be reduced in careful steps that do not jeopardize macroeconomic targets. The Government will continue the policy begun in 1990 to reduce the dispersion of tariff rates and the effective rate of protection on high-duty products. In addition, it will reduce average tariff rates as the higher nontariff revenues expected from the tax reform program materialize.

57. The Government intends to reduce sharply discretionary waivers and exemptions from import taxes during 1992. Existing preferences will be revoked, and the statutory discretion of the Minister of Finance to grant new exemptions will be used only in exceptional circumstances.

58. As market-oriented pricing is established for maize, fertilizer, and petroleum during 1992, export control on these products will be eliminated. Access to support services and credit for exporters will be improved, beginning with the reform of the EXIM Bank, Export Board of Zambia, and Development Bank of Zambia. In addition, as part of the 1992 Budget, the duty drawback system for all duties and taxes paid on imports used in the production of nonmetal exports is to be streamlined.

V. Sectoral Policies

1. Agriculture

59. Agricultural development in the past has been inhibited by excessive government intervention in pricing and marketing, especially with respect to maize. Price controls and subsidies on maize and fertilizer, the system of uniform national pricing, and the cooperatives' monopoly in maize marketing have operated as disincentives to efficient production and optimal land utilization, while encouraging consumption, stimulating smuggling, and nurturing a bloated and inefficient structure of agricultural cooperatives.

60. The Government intends to promote efficient production, ensure food security, and augment exports. Major steps have been taken recently toward elimination of subsidies and liberalization of pricing policies (Section IV.4). The agricultural terms of trade, which had deteriorated over the past five years, are expected to improve with the decontrol of producer prices, and this should enhance the sector's contribution to economic growth. Efficiency gains are expected as a result of increasing private participation in the milling, distribution, and marketing of maize over the period as the handling cost subsidy is ended. In order to complement the liberalization in maize pricing and marketing and to ensure that the resulting increased efficiency benefits consumers, it is intended to privatize the operations of the INDECO Maize Mills and to move toward elimination of the Government's support and control of the cooperatives. Private traders will also play the major role in fertilizer distribution and importation. The restructuring of maize production will be facilitated by the adoption of regionally differentiated floor producer prices, and by the removal of all restraints on exports of agricultural commodities. The pricing of other crops is already market-based, subject only to floor producer prices.

61. Zambia's agricultural development strategy will focus on promoting smallholder production by redirecting and augmenting research and extension services, strengthening agricultural credit, and improving rural infrastructure--especially roads, storage, and agro-processing facilities. Specific programs will be developed to enhance the private sector's involvement in agricultural marketing, processing, and export, including the introduction in 1992 of an Agricultural Market Information Center to improve the flow of information on crop developments and prices.

62. The farm credit system has not worked well in recent years. This is manifested by inadequate access to credit by small farmers (e.g., to satisfy demand for fertilizer), high administrative costs in relation to interest charges, deteriorating performance on loan repayments, and generally poor management and financial accounting of the agricultural lending institutions. The Government will look into ways of addressing these problems and promoting a viable credit system with reduced dependence on government funding. Where such funding is considered necessary, it will

be conditional on strengthening of financial management of the lending institutions and improving their collection and repayment record.

2. Mining, industry, and energy

63. Notwithstanding the Government's efforts to diversify the country's economic base, the copper industry will remain the mainstay of the Zambian economy in the medium term as a major source of foreign exchange and employment. In the past the sector's performance was overshadowed by the inefficiencies and high production expenditure, making the copper company (ZCCM) increasingly uncompetitive on world markets. Declining copper prices over the current decade will also affect the company's operations. The new Government has begun to put in place policies that will enable the company to operate profitably, primarily by reducing spending on personnel and by improving procurement and inventory management procedures. ZCCM will be restructured and nonmining activities will be divested. Expenditures that are not essential to maintain mining production will be eliminated. Mobilization of both local and foreign financial resources will enhance the company's creditworthiness. In the light of this program, it is vital that the expenditure reduction measures be complemented by private investment in ZCCM's undeveloped copper resources. In order to sustain copper production in the medium and long term, the potential ore sources (Konkola, Nkana, and Chambeshi) must be brought into production. They will require considerable and foreign investment. ZCCM is currently preparing a long-term strategy for its operations covering divestiture, joint ventures, and privatization.

64. The Government has expanded incentives and improved the marketing arrangements in the noncopper mining sector, including small-scale mining. In the gemstone sector, mining and marketing of gemstones have been streamlined with a view to developing viable mining operations and obtaining market value prices for the products. The local communities in the gemstone mining areas will be encouraged to set up cottage type industries in the cutting and polishing of the products. A 100 percent foreign exchange retention scheme has been introduced for gemstone and other nontraditional exports. The private sector will play the major role in gemstone development.

65. Sustainable growth in the nonmining industrial sector will be promoted by decreasing the role of the public sector over time and by the pursuit of policies for macroeconomic stability, liberalization, deregulation, and privatization described in earlier sections. Public investments will focus on areas complementary to private sector growth. Unnecessary barriers will be identified and removed as quickly as possible. The Investment Center will be operational early in 1992. It will provide a one-stop center for new investors and offer other services to investors and to the Government, in its quest to identify barriers to and needed incentives for investment. In tourism, emphasis will be on the rehabilitation of the tourist attraction centers as well as the road network leading to these places.

3. Transport

66. Creation of new transport infrastructure in Zambia has not been matched by sufficient expenditures on maintenance and repair, and the sector's infrastructure has deteriorated badly, causing high transport costs and serious delays. The Government recognizes this problem and is determined to give high priority in its medium-term expenditure program to rehabilitation and maintenance of roads and railways.

67. Zambia's roads are important national assets, with an estimated replacement cost of over US\$2.3 billion. Unfortunately, more than US\$500 million in value has been lost in recent years through inadequate maintenance. Annual expenditures of only about US\$38 million would be required to avoid more such losses. Unfortunately actual spending has been far less. Clearly this would be money well spent to avoid further such losses, but additional public spending of this amount will be difficult without new sources of revenue clearly designated for this purpose. Accordingly, the Government will develop a road financing plan to meet these pressing needs, with new revenue from a combination of increased transit fees, license fees, fuel charges, and district council contributions. In addition, Government policies will promote better control of road expenditures and place road maintenance on a more commercial basis, in particular by doing as much as possible through the private sector.

68. To reduce and revamp the regulatory framework, government regulations for surface transport will focus on safety and reliability, leaving the other characteristics of transport services, e.g., price, to be determined by the marketplace. Parastatals in this area--particularly trucking, bus service, and ports--will be privatized as quickly as possible.

69. In the railway sector, a comprehensive strategy and action plan will be developed for ensuring Zambia Railways' (ZR) commercial viability. ZR's poor operating and financial performance has been due primarily to the deteriorated condition of physical assets caused by deferred maintenance and inadequate procedures to ensure efficient utilization of its assets. To reverse this trend, ZR will be restructured to focus on its core business as a freight railway, and in so doing, to streamline operations, stem the deterioration of its assets, and introduce a system of accountability and financial control.

70. Zambia Airways (ZA) is in critical financial condition and, given its considerable net absorption of foreign exchange, is a high priority for improvement. A preliminary economic analysis has been completed as part of a broader study of the airline industry in the SADCC countries, and a further restructuring plan is included in the second phase of the parastatal reform program. This study will address the operational efficiency of the airline, as well as more fundamental issues such as full or partial privatization. In the short run, however, it will be necessary to eliminate the airline's heavy losses through prompt action to eliminate routes that

are heavy loss-makers, improve crew and aircraft utilization, reduce costs, and sell assets.

71. Zambia is largely self-sufficient in energy, the major exception being petroleum. The Government's objectives in the energy sector are to utilize available power-generating capacity by expanding power exports, to arrest the localized depletion of woodfuel resources, to ensure access to and efficient supply of household energy, and to protect the environment. The Government has adopted an expenditure program that gives priority to the rehabilitation of the sector's infrastructure and to more efficient utilization of existing capacity. Pricing policy in the sector will ensure that energy prices reflect economic costs to promote energy conservation and to ensure the financial viability of sector organizations.

4. Environment

72. The Government is paying greater attention to environmental concerns within the framework of environmentally sound sustainable development. This is evidenced by the existence of several pieces of legislation which culminated in the enactment of a consolidated Act, namely, the Environmental Protection and Pollution Control Act 1990 that came into operation on 1st February, 1992. The creation within the new Government of a Ministry of Environment and Natural Resources is a further manifestation of the priority the Government is giving to environmental issues.

73. The most pressing environmental concerns include: the declining quality of water in Zambia's streams and rivers, especially in urban areas with heavy concentrations of population; declining quality of air in localities affected by industrial emissions; declining quality of urban life due to inadequate facilities for the efficient disposal of solid waste; potential dangers posed by inadequate facilities for the disposal of hazardous wastes; decline in wildlife population as a result of heavy poaching; and deforestation due to an overgrowing demand for fuelwood and inappropriate agricultural practices.

74. Under the National Energy Strategy developed with the assistance of the World Bank and UNDP, the Government will improve woodland management and promote use of energy-efficient charcoal stoves and kilns. With the establishment of the National Environmental Council the Government will work closely with the private sector to encourage the latter to adopt adequate environmental control measures and sound environmental practices. Increased support from the international community will be essential to reinforce the Government's own programs.

VI. Social Dimensions

75. The program will have long-run positive impacts on the poor in Zambia. The increased spending on primary health care and primary education, increased emphasis on extension and training for small farmers, the

liberalization of the small-enterprise sector (especially the removal of obstacles for small traders), and the general improvement in economic growth, will all lead to improvements for the poor. In the short run however, some measures, especially the necessary increases in prices of maize and fuel may have negative consequences on the poor, especially in urban areas.

76. The Government has devised a four-pronged strategy to deal with such short-term problems. First, the Government is working with donors to devise ways of using food-aid in the most efficient way to lower the cost of maize-meal to the poor, perhaps by offering a blended yellow maize product at lower cost. Second, a substantial amount (1 billion K) of the savings from the abandoned maize subsidy is being channeled through the Ministry of Community Development and Welfare for welfare programs for the poorest of the poor. This program is being implemented by local governmental and nongovernmental groups in the poorest areas of Zambia. Third, the Government is continuing the Social Action Program, which provides funding for small-scale social development activities through the Provincial Permanent Secretaries.

77. Fourth, the Government--with assistance from the European Community and the World Bank--is implementing a program of small-scale, community-based, labor-intensive public works programs, focusing on the rehabilitation and upgrading of infrastructure and programs in water, sanitation, health, and education. This work is being carried out by the Social Recovery Fund and the Microprojects Programme in the office of the President, National Commission for Development Planning. The Government is actively seeking more donor support for these programs, and several donors have already expressed an interest in further support to the Social Recovery Fund.

78. In the health sector, the Government believes that people have a right of access to affordable health care of good quality. To improve the quantity and quality of health services, the Government will channel resources to rehabilitate and consolidate the infrastructure, plant, and medical equipment. This will be achieved by implementing better planning, accountability, program budgeting, decentralized management, and introducing collective financing mechanisms at the community, provincial, and national levels. This will include cost-recovery measures, integrating private sector services and resources by offering attractive incentives, and enhancing the role and responsibilities of health consumers. The Government is also studying the possible role for health insurance. The Government will allocate increased budgetary resources to provide drugs and medical supplies and their distribution, and for manpower training and retention. The Government will also develop a longer run nutrition policy to supplement the short-run activities supported by the Social Action Program and the MCDSW.

79. The Government has initiated a national population policy aimed at reducing the high rate of population growth, including family and maternal health care programs and public education on family planning methods. The

Government will step up its efforts in general education on AIDS prevention. With estimates of HIV seropositive prevalence rates of around 20 percent in major urban areas of Zambia, medium- to long-term development plans must take the impact of the threatening AIDS epidemic into account. The Government plans to review the ongoing AIDS program with a view to enlarging and strengthening the implementation of various aspects of the program. Subject to the outcome of this review, the Government plans to propose an increase in the information, education, and communication activities, especially targeted at urban populations below the age of 40. Furthermore, special high-risk groups will be targeted with intensive prevention training and information. The Ministry of Health will also focus its attention on cholera and dysentery epidemics through improvement of water and sanitation programs and projects.

80. To improve access to quality education, emphasis in education expenditures is being placed on primary education, particularly in the very poor urban and rural areas. Increased resources for education within the expenditure program will be channeled to rehabilitating existing facilities, while recurrent expenditures will be focused on providing adequate teaching materials and equipment, on improving educational quality (curriculum development, upgrading of teachers), and on strengthening management and supervision in the sector. In order to strengthen the financial resource base for education, Zambia has introduced user fees for the beneficiaries of secondary and higher education and instituted cost-effective measures. The Government intends to use the resultant savings to finance the additional recurrent expenditures that will result from the limited increase in primary education. These policies are expected to reduce the current wide disparities of expenditure levels between primary and higher education in Zambia. To further enhance educational quality at the primary level, the Government will concentrate resources on the first seven years. Primary education will have priority over the development of basic schools until such time as the Government can mobilize adequate resources to provide nine years of high-quality basic education.

VII. Program Monitoring and Technical Assistance

81. A two-tiered mechanism will be established to monitor the stabilization and structural adjustment program. An interministerial coordinating committee, chaired by the Minister of Finance, will meet monthly to review implementation of all elements of the recovery program and more frequently as necessary to review individual economic policy issues. A small technical staff housed in the Ministry of Finance, headed by the Senior Economic Adviser to the Government, will coordinate all staff presentations to the committee, maintain a current data base relating to the progress of the program and the economy, and act as the secretariat for the committee.

82. Progress has been made in strengthening administrative capacity to implement economic policy effectively, although in certain areas-- particularly with respect to economic statistics--further efforts and

support are required. Technical assistance is being provided in the form of advisory support in the Ministry of Finance and in aid coordination and debt management, and help in improving tax administration is expected to be in place shortly. Problems have been encountered in the compilation of price statistics and national accounts data, and Zambia is requesting assistance from the international community in this area. In support of its restructuring program, the Bank of Zambia is receiving technical assistance in the areas of bank supervision, monetary policy, banking administration, and accounting. The Government intends to strengthen coordination of technical cooperation to minimize duplication and to improve its effectiveness. In this regard, the Government is working closely with the United Nations Development Program and the World Bank to achieve these goals.

VIII. Balance of Payments and External Financing. 1992-94

83. The ongoing decline in copper export revenues and large external debt service burden are the central realities of Zambia's balance of payments outlook. Copper export volume has already fallen from 430,000 metric tons in 1990 to under 400,000 metric tons in 1991; while it is expected to stabilize around that level until the late 1990s, thereafter it is expected to decline rapidly to about 200,000 metric tons a year as ore reserves are depleted (Table 3). Compounding this, copper prices have dropped from US\$1.20 a pound in 1990 to under US\$1.00 per pound at present, and are expected to fall further during 1992-94 in response to growing world copper output and stagnating demand. By the end of this decade, the real purchasing power of copper export proceeds is expected to be about 25 percent of its 1990 level.

84. Zambia's external debt service payments falling due (excluding payment of arrears) in 1991 were equivalent to about 65 percent of exports of goods and services; its external debt of US\$6.5 billion was equal to 560 percent of exports of goods and services, and implied that per capita indebtedness was more than twice per capita income. Roughly 45 percent of Zambia's total debt is owed to multilateral creditors, 35 percent to bilateral official creditors, and 20 percent to commercial banks and nonguaranteed suppliers.

85. In view of the very poor outlook for copper exports, the Government's objective of 10-15 percent annual growth for nontraditional export volumes over the next decade, though it may appear ambitious, is the minimum necessary if there is to be any hope for sustained growth and balance of payments viability. The Government also expects to realize the potential for rapid growth in service receipts, particularly from tourism. Even with such an expansion, however, total receipts from exports of goods and services are projected to increase by only about 2 percent a year during the remainder of this decade, limiting the scope for rapid import growth. The import requirements of the metal sector will decline over time with the winding down of production; average annual growth in the volume of other imports is projected at 3.5 percent in 1992-94, implying a modest reduction

in the import intensity of production in response to changes in relative prices and increased efficiency.

86. The program for 1992 is based on a copper price of US\$0.90 a pound and an export volume of 375,000 metric tons. It also provides for US\$38 million of maize imports in the first quarter, and targets a reserve increase of US\$35 million. As in 1991, the program incorporates an integrated contingency mechanism under which the reserve target will be adjusted upward for any additional copper export revenues that result from world prices above US\$0.90 a pound. In addition, the reserve target will be adjusted downward for any shortfall in nonproject assistance from external donors. In no event will the reserve target be reduced below the baseline increase of US\$35 million. Once the adjusted reserve target has reached US\$75 million, half of any further excess in 1992 will be used to reduce arrears to the Fund below the programmed level and the disposition of the remainder will be determined by the Government.

87. Reflecting the expected decline in copper prices and some recovery in imports, the external current account deficit (excluding interest and official transfers) is expected to widen from US\$90 million in 1991 to about US\$285 million or 7.8 percent of GDP in 1992, and to decline only slightly in 1993-94 (Table 4). Zambia recently paid its outstanding arrears to the World Bank, and the Government also intends to reduce its arrears to the Fund to the level outstanding as of July 1, 1990, which is equivalent to the maximum amount (SDR 836.9 million) that Zambia can accumulate under the Fund decision on the accumulation of rights for Zambia. Including arrears of about US\$70 million to other multilateral creditors and new arrears of US\$60 million to Paris Club creditors, plus all other debt service obligations falling due, Zambia faces a gross financing requirement of about US\$1.4 billion in 1992 and US\$1.0 billion a year in 1993-94.

88. After deducting normal flows of project-related and commodity assistance (about US\$280 million) and private capital flows, the residual financing requirement for 1992 is about US\$1.0 billion. The Government is seeking to fill this gap through balance of payments assistance from donors, the World Bank, and the African Development Bank, and through debt relief, including debt relief on concessional terms from official bilateral creditors. In addition, it will seek through debt restructuring and new lending to limit net payments to private creditors and non-Paris Club bilateral creditors to no more than US\$72 million. In general, the Government is asking donors to be as flexible as possible in providing assistance in forms that can facilitate private sector activity, particularly through OGL imports. With the assistance of the World Bank and Fund, the Government is reaching out to the international community for generous support for Zambia's new beginning.

Implementation of the PFP in 1989-91

I. Macroeconomic and Structural Policies

1. The adjustment strategy as set out in the original PFP (September 1989) and in the updated document (February 1991) sought through fiscal and monetary restraint to achieve a sound and stable financial environment. Within this environment, structural reforms were to be taken to liberalize the economy and to remove impediments to diversification and sustained growth.
2. In the event, the effort to bring down the rate of inflation and reduce macroeconomic imbalances was disappointing. During the second half of 1989 and the first half of 1990, some progress was made in bringing the public finances under control and achieving slower monetary growth and reduced inflation. Around the middle of 1990, however, serious problems were encountered in implementation of the budget. Significant increases in housing allowances and reversal of a decision to tax fringe benefits, which in Zambia primarily take the form of cash allowances and are a large proportion of total remuneration, led to serious budgetary slippages. Although the primary budget deficit (excluding grants) in 1990 declined to 4.2 percent of GDP from 6.6 percent in 1989, it was still well above the PFP target of 0.4 percent. This poor fiscal performance was reflected in greater-than-expected monetary expansion, and while inflation fell from 158 percent in 1989 to 105 percent in 1990, this was very much higher than the PFP objective of 55 percent.
3. In early 1991, the adjustment effort again moved forward. Extraordinary efforts by the donor community and heavy frontloading of aid disbursements enabled Zambia to clear its arrears to the World Bank and to reduce its arrears to the IMF. In March 1991, Zambia became eligible for disbursements from the World Bank under an Economic Recovery Credit, and in April the Executive Board of the Fund endorsed Zambia's rights accumulation program and approved the accumulation of rights over a period of three years. The rights program, which was based on the updated PFP of February 1991, targeted economic growth for 1991 at 3 percent and inflation at 40 percent.
4. Macroeconomic performance under the rights program, however, was poor and Zambia failed to accumulate any rights in 1991. Problems in meeting the fiscal and monetary targets emerged in the first half of the year. The decision to tax fringe benefits was again withdrawn, and ZCCM fell well behind in meeting its income tax and mineral resource levy obligations. During the second half of 1991, policy implementation worsened further. Fiscal subsidies for mealie meal rose sharply as a result of a decision not to adjust consumer prices after a tripling of producer prices. In addition, substantial funds had to be lent to the agricultural cooperatives to purchase the maize crop, and large pay awards were granted to the public sector. A range of tax and spending measures were taken, but they were insufficient to offset these expenditure overruns. The primary fiscal deficit (excluding grants) increased to 6.5 percent of GDP in 1991, compared

with the rights program target of 0.7 percent. To contain the monetary impact of the enlarged budget deficit and encourage savings, the Bank of Zambia introduced a new liquid assets requirement and increased interest rates, but broad money still grew by nearly 100 percent. Consumer prices are estimated to have risen by about 100 percent in 1991, compared with a target of 40 percent in the rights program.

5. Prior to June 1989, price regulation was widespread in the Zambian economy, either in the form of statutory controls or informally through the requirement of prior approval of price increases. In June 1989, all formal price controls except those on maize, mealie meal, and fertilizer were abolished, and black marketeering virtually disappeared. However, informal regulation of some pricing decisions by parastatals (e.g., cooking oil) continued intermittently. This undermined the profitability of the parastatals and badly distorted the pattern of resource allocation.

6. There has been a progressive liberalization of the exchange and trade system since mid-1989 in the context of efforts to strengthen Zambia's international competitiveness. In February 1990, an OGL system was introduced for most merchandise imports. At the same time, a second, more competitive official exchange rate was introduced at a level of K 40 per U.S. dollar (compared with K 22 per U.S. dollar in the first window), for use in conjunction with all foreign exchange surrenders other than exports and all imports covered by the OGL system. The OGL system was gradually expanded, and the difference between the first and second window rates was narrowed until the two official exchange rates were unified on April 23, 1991. Subsequently, the official rate continued to be adjusted on a weekly basis. The real effective depreciation of the kwacha from June 1989 to December 1991 is estimated at about 45 percent in local currency terms (see Chart 1).

7. The comprehensive system of foreign exchange licensing and allocation was abolished in November 1990. In addition, limits on remittances of profits and dividends were eased and procedures were established for the clearance of post-1986 dividend arrears.

8. Exporters of nontraditional products may retain 50 percent of the foreign exchange proceeds for use in eligible import transactions, for certain service payments, and for arrears pipeline clearance. These funds may be sold to third parties at freely determined rates. As of end-December 1991, the exchange rate in the export retention market was about K 25 per U.S. dollar (about 28 percent) above the official rate.

9. Under reforms of the import tariff system initiated in November 1990, the maximum tariff rate was reduced from 100 percent to 50 percent for all but a small number of luxury goods, a minimum rate of 15 percent was established, and duty exemptions were reduced. Export licensing was streamlined and shifted to the banking system in September 1990, and in March 1991 the list of controlled or prohibited exports was reduced from 48 to 4.

II. Balance of Payments and External Financing

10. The program for 1991 was based on a decline in the world price of copper to US\$0.96 per pound and an export volume of 430,000 metric tons, compared with a price of US\$1.20 per pound and over 440,000 metric tons of exports in 1990. World crude oil prices were projected to average US\$22 per barrel, and Zambia's gross international reserves were targeted to increase by US\$35 million. Zambia undertook to meet obligations falling due to multilateral creditors and under the July 1990 Paris Club agreement; to reduce arrears to the Fund to their July 1, 1990 level; and to pay all arrears to other multilateral creditors. In addition, the Government sought comprehensive debt service relief from other creditors.

11. On this basis, Zambia faced an external financing gap, after rescheduling, of US\$1.1 billion. The gap was expected to be met through normal project aid disbursements of about US\$200 million, World Bank lending of over US\$400 million, US\$40 million of private capital inflows, and about US\$450 million of other balance of payments assistance from bilateral and multilateral donors.

12. Actual copper prices averaged about US\$1.06 per pound in 1991, and consequently, despite lower-than-expected production, copper export revenues were about US\$25 million above the programmed level. However, nontraditional export receipts declined by 26 percent from their 1990 levels, rather than rising substantially as had been expected. Because of the suspension of most donor disbursements after mid-1991, net external financing was also well below projections. Donor disbursements fell short of the programmed level by US\$240 million; the suspension of disbursements by the World Bank prevented the release of some US\$175 million of IDA financing plus associated bilateral assistance. In addition, the proportion of commodity and project assistance in total inflows was greater than had been hoped for. As a result, gross liquid foreign reserves declined slightly (and uncommitted reserves were virtually exhausted), Zambia's arrears to the IMF grew by some US\$85 million--instead of the programmed US\$35 million decline--and Zambia built up new arrears of US\$40 million to the World Bank, about \$70 million to the other multilateral creditors, and about US\$60 million to Paris Club creditors. In addition, the shortage of foreign exchange complicated further expansion of the list of items eligible for the OGL (or a movement to a negative list) and contributed to a backlog in providing foreign exchange for OGL imports.

Table 1. Zambia: Key Indicators, 1989-94

	1989	1990	1991	1992	1993	1994
				Projected		
(In percent change)						
Real GDP	-1.0	-0.5	-1.8	2.0	3.0	4.0
Real nonmining GDP	-1.7	-0.7	-0.7	2.1	3.1	4.1
Real per capita GDP	-4.4	-3.9	-5.1	-1.4	-0.5	0.5
Real consumption per capita	-10.1	-3.0	-2.8	-4.9	-5.6	0.2
Terms of trade ^{1/}	9.4	-1.1	-7.3	-8.8	-6.9	-3.8
Consumer prices (end period)	158.0	105.0	95.0	45.0	15.0	5.0
Export volume	3.1	6.8	-17.4	7.6	4.8	3.5
Copper	8.4	2.0	-14.8	-0.1	2.2	2.3
Noncopper	-14.9	27.9	-27.1	39.2	12.5	6.6
Import volume ^{2/}	8.4	15.9	-11.5	11.3	-3.1	1.5
Real exchange rate (depreciation -)	32.3	-16.4	-9.9	...	...	...
Money supply (M2)	65.3	45.8	98.1	25.0	10.0	5.0
(In percent of GDP)						
Gross domestic savings	13.7	16.6	12.0	12.6	14.0	14.5
Gross national savings ^{3/}	6.0	13.8	15.3	18.2	16.9	15.2
Central Government	-4.9	-1.8	1.2	5.2	3.1	3.8
Nongovernment	10.9	15.6	14.1	13.0	13.9	11.4
Unrequited transfers and net factor income ^{3/}	-7.7	-2.8	3.3	5.6	2.9	0.7
Gross domestic investment	9.9	17.3	13.5	19.5	20.0	20.5
Central Government	4.7	5.4	7.3	4.9	4.5	4.7
Nongovernment	5.3	11.9	6.2	14.6	15.5	15.8
Consumption	86.3	83.4	88.0	87.4	86.0	85.5
Central Government	14.1	11.1	10.3	10.5	10.8	10.9
Nongovernment	72.2	72.3	77.7	77.0	75.2	74.7
External current account ^{3/}	-4.0	-3.5	1.8	-1.3	-3.1	-5.3
Metal sector	18.0	16.9	15.7	11.8	9.9	9.1
Nonmetal sector	-22.0	-20.4	-14.0	-13.1	-13.0	-14.4
Government domestic revenues	17.1	17.6	17.0	17.5	17.7	18.0
Government grants ^{3/}	2.1	3.8	6.8	8.2	3.3	2.3
Government expenditure	29.5	29.1	30.9	27.7	23.4	21.4
Government deficit						
Accrual basis	-10.3	-7.7	-7.1	-2.0	-2.3	-1.1
Accrual excluding grants and interest	-6.6	-4.2	-6.5	-1.4	--	0.5
Domestic financing of government deficit (net)	6.4	2.6	6.1	2.5	-0.3	-1.0
(In percent of exports of goods and services)						
Debt service (accrual) ^{4/}	58.0	60.2	65.2	66.2	61.7	51.5
External interest (accrual)	28.9	28.3	30.8	32.1	29.3	26.2
(In percent)						
Commercial bank lending rate (end of period)	35.0	40.0	46.0	...	...	...

Sources: Zambian authorities; and staff estimates.

^{1/} Copper price (US\$/lb): 1.29 1.21 1.06 0.90 0.90 0.88

^{2/} Import volume growth in 1992 is inflated by emergency maize imports and restocking of fertilizer and petroleum; these factors serve to depress import volume growth in 1993.

^{3/} Assuming that bulk of external financing gap is filled with grants.

^{4/} Excludes payment of arrears.

Table 2. Zambia: Central Government Operations, 1991-92

	1991		1992
	Prog. 1/	Prel.	Proj.
(In percent of GDP)			
Revenue and grants	25.9	23.8	25.7
Tax revenue	18.9	16.3	16.3
Mineral revenue	3.0	1.4	0.5
Import taxes	6.6	5.4	5.9
Domestic goods and services	5.2	5.1	5.4
Income taxes	4.0	4.5	4.5
Nontax revenue	0.8	0.4	1.2
Exceptional revenue	0.4	0.3	--
Grants	5.9	6.8	8.2
Expenditure and net lending	29.9	30.9	27.7
Current expenditure	24.2	23.2	22.8
Personal emoluments	3.7	4.3	4.2
Civil service reform	--	--	0.4
Recurrent departmental charges	3.6	3.3	3.5
Subsidies	2.7	3.4	1.7
Domestic interest	1.9	2.5	4.0
Foreign interest	7.3	4.8	4.8
Transfers and pensions	2.4	2.5	1.9
Other	2.6	2.3	2.4
Capital expenditure and net lending	5.7	4.8	3.9
Crop financing and maize imports	--	2.5	1.0
Exceptional expenditure	--	0.4	--
Overall deficit (accrual)	-4.0	-7.1	-2.0
Payment of domestic arrears	0.9	1.0	0.4
Overall deficit (cash)	-4.9	-8.1	-2.4
External financing (net) 2/	4.7	2.3	-0.1
Domestic financing (net)	0.2	6.1	2.5
Residual	--	-0.3	--
<u>Memorandum items:</u>			
Primary deficit excluding grants (accrual)	-0.7	-6.5	-1.4
Primary deficit excluding grants (cash)	-1.6	-7.5	-1.9

Sources: Zambian authorities; and staff estimates.

1/ Rights Accumulation Program.

2/ Includes debt relief, and change in debt arrears, with respect to both principal and interest.

Table 3. Zambia: Balance of Payments, 1987-94
(In millions of U.S. dollars)

	1987	1988	1989	1990	1991 Prog.	1991 Est.	1992 Projections	1993 Projections	1994
Trade balance	96	267	387	179	-21	133	-72	-70	-95
Exports, f.o.b.	868	1,156	1,407	1,263	1,098	1,082	1,006	1,000	1,025
Copper	736	982	1,231	1,055	852	895	697	712	710
Other metals	66	91	106	95	128	103	177	131	135
Nonmetal	66	82	70	113	118	84	133	158	179
Imports, c.i.f.	-772	-888	-1,020	-1,084	-1,118	-949	-1,078	-1,071	-1,119
Metal sector	-233	-278	-372	-346	-350	-285	-319	-335	-353
Fertilizer	-45	-47	-73	-49	-56	-29	-40	-38	-41
Petroleum	-67	-62	-103	-119	-130	-73	-100	-96	-102
Maize	...	...	...	...	...	-16	-38	...	...
Other	-427	-501	-473	-570	-583	-545	-581	-602	-623
Services (net)	-412	-496	-579	-571	-528	-548	-535	-489	-445
Interest ^{1/}	-341	-409	-401	-365	-408	-347	-340	-310	-283
Other factor	-3	-3	--	--	--	-13	-13	-20	-21
Nonfactor	-69	-85	-178	-206	-120	-188	-182	-159	-141
Unrequited transfers	75	65	44	253	398	481	232	220	210
Private	-30	-35	-28	-43	-28	-40	-40	-41	-43
Official	105	99	72	296	426	521	272	262	253
Current Account	-242	-164	-149	-139	-150	65	-374	-339	-330
Metal sector	480	710	875	671	531	584	471	378	357
Nonmetal sector	-722	-874	-1,024	-810	-682	-519	-845	-717	-686
Nonmonetary capital	-221	-206	-126	-217	273	-293	-274	-338	-277
Medium- and long-term flows	-211	-147	-208	-143	263	-31	-332	-329	-267
Disbursements	130	196	96	169	644	317	44	36	29
Amortization	-341	-343	-304	-312	-382	-348	-376	-365	-297
Short-term (includes errors and omissions)	-10	-59	82	-74	10	-262	58	-9	-10
Overall balance	-463	-370	-275	-356	122	-228	-648	-677	-607
Financing	463	370	275	356	-122	228	648	677	607
IMF (net)	74	86	87	89	-158	-39	-125	-3	--
Purchases	...	...	...	...	...	...	...	...	...
Repurchases (scheduled)	-234	-206	-126	-122	-60	-59	-6	-3	...
Overdue obligations	308	291	213	212	-98	20	-119	0	...
Other foreign assets (net)	-50	-101	-94	-1	-35	20	-34	-30	-30
Central Bank	-16	-63	-63	-1	-35	20	-34	-30	-30
Official assets	-1	-58	-35	--	-35	--	-35	-30	-30
Official liabilities	-14	-5	-28	-1	--	20	1	...	...
Commercial banks	-35	-38	-31	...	...	...	...	...	...
Valuation adjustment	21	-4	1	...	...	...	...	...	...
Debt relief ^{2/}	--	--	--	771	2,031	1,176	-20	--	--
Scheduled obligations	...	...	...	189	468	371	--	...	...
Arrears	...	...	...	582	1,563	805	--	...	...
Arrears (excluding IMF)	419	389	280	-503	-1,961	-928	-175	--	--
Financing gap	--	--	--	--	--	--	1,003	710	637
Memorandum items:									
Current account, excluding interest obligations and official transfers	2	160	205	-48	-140	-92	-287	-267	-274
Copper export volume (in thousands of metric tons)	475	398	432	440	430	375	375	383	392
Copper price (US\$/lb)	0.74	1.16	1.33	1.21	0.96	1.06	0.90	0.90	0.88

Sources: Bank of Zambia; and Fund staff estimates.

^{1/} Assumes financing gaps are filled on highly concessional terms.

^{2/} Includes deferral, and temporary accumulation of arrears to nonmultilaterals pending conclusion of rescheduling discussions.

Table 4. Zambia: External Financing Requirements, 1991-94

(In millions of U.S. dollars)

	1991 Prog.	1991 Est.	1992	1993 Projections	1994
1. Current account, excluding interest and official transfers	-140	-92	-287	-267	-274
2. Debt service obligations	-898	-828	-761	-707	-610
Nonmultilaterals	-569	-505	-504	-444	-374
Scheduled obligations	-366	-396	-413	-365	-290
Paris Club creditors	-201	-201	-236	-214	-180
Other	-165	-195	-176	-151	-110
Interest on arrears and service of rescheduled obligations	-203	-109	-91	-79	-84
Paris Club creditors	-93	-82	-50	-31	-32
Other	-111	-27	-41	-48	-53
Multilaterals	-329	-322	-258	-263	-235
World Bank	-88	-85	-82	-87	-78
IMF	-181	-172	-109	-104	-92
Other multilaterals	-60	-66	-67	-72	-66
3. Targeted reduction of arrears	-2,053	-1,050	-293	--	--
Nonmultilaterals	-1,618	-757	-66	...	...
Multilaterals	-435	-293	-228	--	--
World Bank	-312	-293	-40	...	...
IMF	-92	...	-119	--	...
Other multilaterals	-31	...	-69	...	...
4. Change in gross official reserves (increase -)	-35	...	-35	-30	-30
5. Gross financing requirement (= 1+2+3+4)	-3,126	-1,970	-1,376	-1,004	-913
6. Increases in arrears 1/	--	142	--	--	--
Nonmultilaterals	--	76	--	--	--
Multilaterals	--	40	...	...	...
World Bank	...	20	...	...	...
IMF	...	16	...	...	...
Other multilaterals	...	...	...	...	...
7. Debt relief 2/	2,031	1,176	--	--	--
Paris Club creditors	208	208	...	...	...
Other	1,823	968	...	...	...
8. Financing requirement after arrears accumulation and debt relief (= 5+6+7)	-1,095	-652	-1,376	-1,004	-913
9. Identified possible disbursements	1,095	653	374	294	276
World Bank	414	202	...	...	...
African Development Bank	70	57	...	...	...
Other project assistance	138	236	229	214	198
BOP support from other donors	412	244	...	...	...
Commodity assistance	23	76	49	50	52
Suppliers, private, and short-term capital, net 3/	38	-163	96	30	26
10. Financing requirement, after identified disbursements	--	--	-1,003	-710	-637

Sources: Bank of Zambia; and Fund staff estimates.

1/ Excludes temporary further accumulation of arrears to nonmultilaterals pending conclusion of rescheduling discussions.

2/ Includes deferral, and temporary accumulation of arrears to nonmultilaterals pending conclusion of rescheduling discussions.

3/ Includes changes in reserve liabilities, other than to IMF.

Table 5. Zambia: Summary and Timetable of Adjustment and Structural Measures, 1991-94

(Asterisks indicate areas for priority action)

	Objectives and Targets	Strategy and Measures	Timing of Measures
I. External Policies			
1. Exchange rate	Increase earnings from nontraditional exports, reduce import dependence, and improve allocative efficiency.	Unify official and second-window exchange rates.	April 1991
		* Step devaluation of 30 percent.	From January 31, 1992
		* Manage the exchange rate so as to satisfy the 1992 balance of payments objectives and move increasingly toward a market-determined rate.	During 1992
2. Exchange and trade system	Liberalize import regime.	* Shift OGL system to a negative list.	Mid-1992
		Widen OGL coverage from 90 percent to at least 95 percent of base period imports.	Mid-1992
	Remove impediments to exports.	Further reduce list of controlled exports from 4 to 1 (ivory).	End-1992
3. Tariff reform	Achieve a more uniform and lower-level tariff regime.	Continue to rationalize and reform tariff structure.	1992-93
4. External debt and aid	Take steps to normalize relations with external creditors.	* Reduce arrears to the Fund to their July 1, 1990 level.	During 1992
		* Eliminate arrears to other multilateral creditors and meet payments falling due to all multilateral creditors.	From January 1992
		* Clear recent arrears to Paris Club and other bilateral creditors in the context of arrangements for debt relief and new external disbursements.	1992
		* Discuss with commercial banks and other private creditors means of addressing debt service problems.	1992

Table 5 (continued). Zambia: Summary and Timetable of Adjustment and Structural Measures, 1991-94

(Asterisks indicate areas for priority action)

	Objectives and Targets	Strategy and Measures	Timing of Measures
	Improve aid/debt management.	Continue efforts to strengthen monitoring of aid/debt flows.	1992
II. Fiscal Policy			
1. Revenue mobilization	Increase buoyancy, fairness, and efficiency of tax system.	Expand income tax base to include fringe benefits and reduce tax rates.	Announced in 1992 budget
		Harmonize domestic and import sales tax at a uniform rate.	Announced in 1992 budget
		Convert sales tax to VAT.	1993
	Reverse decline in real value of nontax revenue.	Restore real value of nontax revenue to 1988 level.	1992-94
2. Expenditure restructuring	Eliminate subsidies while containing the growth, and restructuring the composition, of other noninterest expenditure.	* Eliminate transport subsidies for maize.	1992
		Eliminate subsidies for breakfast meal.	Implemented January 1992
		* Reduce subsidy on roller meal to 20 percent.	December 1992
		Eliminate subsidy on roller meal.	Mid-1993
		* Eliminate subsidy on fertilizer.	March 1992
		Increase share of recurrent budget allocated to supplies and maintenance.	1992-94
		* Improve targeting of current expenditure toward priority sectors and vulnerable groups.	1992-94
3. Fiscal management	Strengthen management of public finances.	* Strengthen monitoring and control of expenditures.	1992-94
	Improve tax administration.	Increase tax department budgets and computerize.	1992
4. Civil service reform	Improve efficiency without raising cost.	Improve incentives for technical and managerial positions, while reducing size of public service.	1992-94

Table 5 (continued). Zambia: Summary and Timetable of Adjustment and Structural Measures, 1991-94

(Asterisks indicate areas for priority action)

	Objectives and Targets	Strategy and Measures	Timing of Measures
III. <u>Monetary Policy</u>			
1. Money supply	Bring monetary growth under control; M2 to increase by no more than 25 percent in 1992.	* Introduce, and make active use of, new liquid asset requirements.	1991-92
		Continue to impose limits on kwacha created through debt swaps in consistency with monetary objectives.	1991-92
2. Credit	Ensure adequate credit availability to nongovernment sector.	* Limit net borrowing by Government from banking system.	1992-94
3. Interest rates	Achieve positive real rates to encourage saving, discourage capital flight, and achieve a more efficient allocation of credit.	Increase interest rates by 5 points to bring lending rates in line with targeted inflation for Q1, 1992.	Implemented February 3
		* Raise rates further if warranted by inflation performance.	1992
IV. <u>Parastatal Reform</u>	Remove Government interference through granting substantial autonomy.	Grant managerial autonomy and eliminate subsidies.	Mid-1992
		Institute regulatory system for public utilities and agree price adjustment mechanism.	1993
	Reform of parastatal holding companies.	Implementation of agreed action plan for ZIMCO/INDECO.	1992-93
	Strengthen public utilities.	Review managerial and institutional reform measures and adopt action plan.	1993
V. <u>Privatization</u>	Enhance efficiency by privatizing most state-owned enterprises.	Overall plan.	July 1992
		Sale of first group and offer of next ten.	Early 1993
VI. <u>Agriculture</u>			
	Eliminate maize and fertilizer subsidies.	See under II.2	

Table 5 (continued). Zambia: Summary and Timetable of Adjustment and Structural Measures, 1991-94

(Asterisks indicate areas for priority action)

	Objectives and Targets	Strategy and Measures	Timing of Measures
	Increase efficiency of maize and fertilizer marketing.	Establish floor price for maize with variations based on transport costs so as to eliminate transport subsidies.	Mid-1992
		Develop rules for operation and financing of maize strategic reserve.	Developed 1992 Implemented 1993
		Take other steps as necessary to encourage private sector participation in maize and fertilizer marketing.	1992-94
VII. <u>Mining</u>	Improve competitiveness of ZCCM.	Formulate a detailed medium-term investment and production program.	1992
		Improve operating efficiency of ZCCM.	1992-94
		Begin process of divesting ZCCM of non-mining activities.	1992
VIII. <u>Industry</u>			
1. Role of sector	Reaffirm Zambia's commitment to a market-based free enterprise system.	Issue a major policy statement on the role of the private sector and issue Investment Guidelines.	1992
2. Legislative reform	Encourage investment.	Implement recently enacted investment code to streamline procedures and liberalize treatment of foreign investment.	1992

Table 5 (continued). Zambia: Summary and Timetable of Adjustment and Structural Measures, 1991-94

(Asterisks indicate areas for priority action)

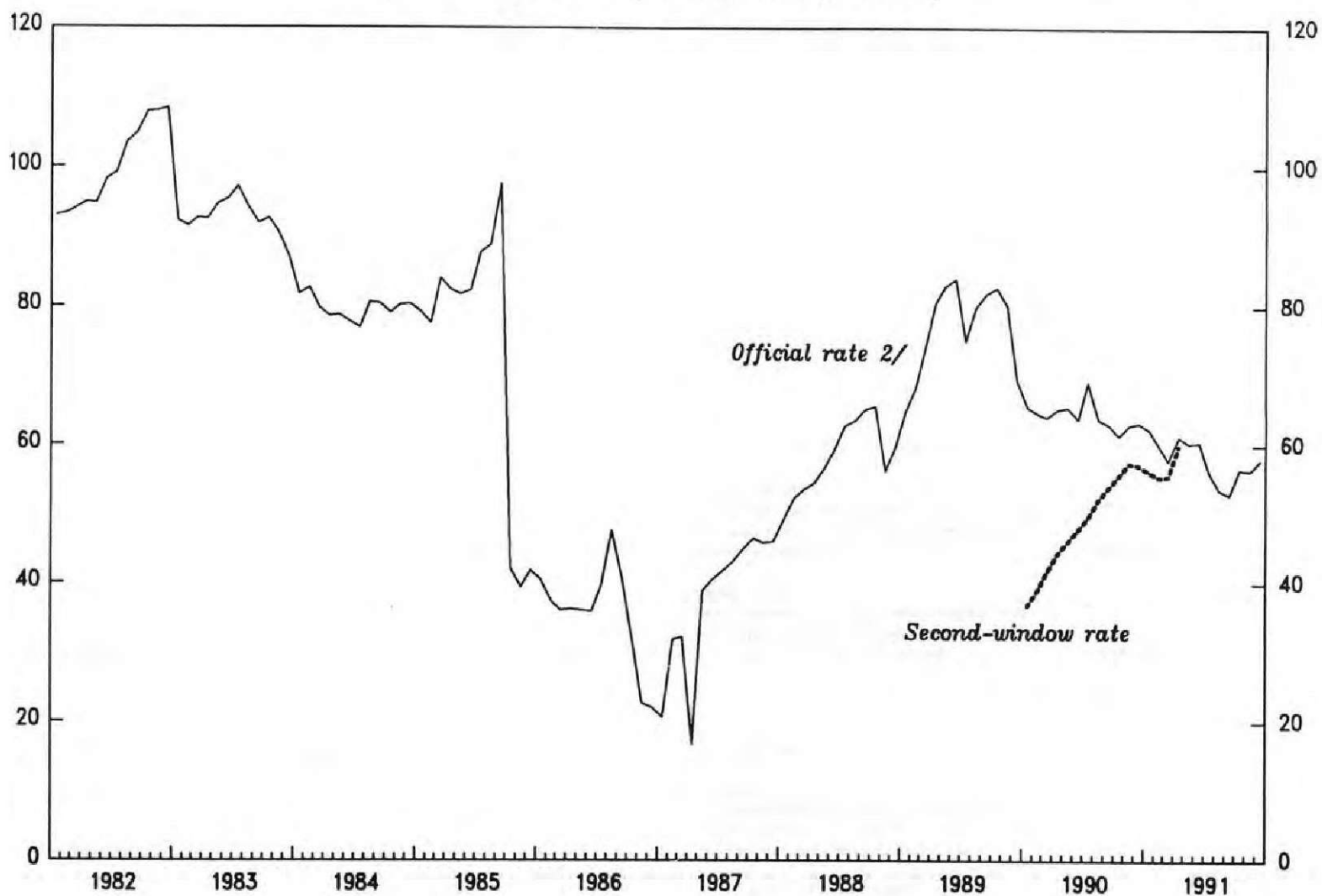
	Objectives and Targets	Strategy and Measures	Timing of Measures
IX. <u>Transport</u>			
Expenditure reforms	Raise efficiency of transport services and reduce budgetary burden of operating subsidies.	Give high priority to maintenance, rehabilitation, and repair of existing road transport systems.	Announced in 1992 budget
		Develop and implement restructuring plans for Zambia Railways and Zambia Airways.	1992-94
		Implement short-term measures to stem losses incurred by Zambia Airways.	1992
		Improve maintenance of feeder roads through institutional reform and increased resource mobilization.	1992-94
X. <u>Energy</u>			
1. Price Reforms		Increase petroleum prices.	Implemented January 1992
		* Maintain petroleum product and electricity prices at economic levels.	1992-94
2. Expenditure	Supply adequate and economically priced energy to industrial and household users.	Allocate expenditures in power and petroleum sectors to maintenance, repair and rehabilitation of existing infrastructure rather than to creation of new capacity.	1992-94
XI. <u>Health and Population</u>			
1. Expenditure reforms	Improve delivery of health services.	Adequately fund health sector activities and give priority to maintenance and repair of existing primary health facilities.	1992-94
		Shift emphasis to preventive health care from curative care.	1992-94
		Increase real funding for nonsalary recurrent costs.	1992-94
2. Revenue Reform		Continue and expand cost recovery program on ability-to-pay basis.	1992-94

Table 5 (concluded). Zambia: Summary and Timetable of Adjustment and Structural Measures, 1991-94

(Asterisks indicate areas for priority action)

Objectives and Targets		Strategy and Measures	Timing of Measures
3. Population growth		Implement national population policy aimed at significantly reducing the rate of population growth.	1992-94
4. Nutrition	Improve nutritional status of population.	Develop medium-term National Nutrition Strategy.	1993
XII. <u>Education</u>			
Expenditure reforms	Improve access to and quality of education.	Give priority in education expenditures to primary education, particularly in the poor urban and rural areas.	1992-94
		Focus expenditures on rehabilitation and maintenance of existing facilities as well as teaching materials.	1992-94
		Increase share of education in budget.	1994

CHART 1
ZAMBIA
REAL EFFECTIVE EXCHANGE RATE INDICES¹, JANUARY 1982 - DECEMBER 1991
(Period average, 1982=100; foreign currency per kwacha)



Sources: IMF Information Notice System; and staff estimates.

1/ Weighted by total trade.

2/ First-window rate from February 1990 to April 1991.

A L L - I N - 1 N O T E

DATE: 12-Mar-1992 04:59pm

TO: Edward V.K. Jaycox

(EDWARD V.K. JAYCOX)

FROM: Stephen Denning, AF6DR

(STEPHEN DENNING)

EXT.: 34035

SUBJECT: Zambia: Discussion with IMF

Ms. Dillon (IMF) called to let me know that she had met with Mr. Erb today (Thursday) who confirmed that IMF management would be willing to provide \$100 million in relief to Zambia at the outset, on the understanding that IDA also envisaged increasing its PIRC Credit by \$100 million, and on the understanding the Bank would join with the Fund in presenting this as a final position, and not a "going in" position which we were expecting to increase as part of a bargaining session at the CG.

In Mr. Stern's absence from Washington, Mr. Erb asked Ms. Dillon to confirm with me orally that this was the correct understanding of what was being proposed. I confirmed to Ms. Dillon that this was my understanding of our proposal.

Ms. Dillon said that on this basis Mr. Erb would brief the IMF EDs tomorrow (Friday) at 2.30 p.m. that the IMF management was planning to proceed on this basis. In the absence of objection from the IMF EDs, this would then become the IMF position for the CG.

At the request of the Nordic ED, we are also holding a briefing session for Bank donor EDs tomorrow (Friday) at 4 p.m.. Unless I receive a contrary indication, I will reflect these developments in our presentation to our EDs, as this will help to ensure a positive result at the CG.

CC: Attila Karaosmanoglu
CC: Ernest Stern
CC: Gisu Mohadjer

(ATTILA KARAOSMANOGLU)
(ERNEST STERN)
(GISU MOHADJER)

International Bank for Reconstruction and Development

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R92-6

FROM: Vice President and Secretary

January 21, 1992

*File
Zambia*

Zambia: Economic Recovery Credit - Release of Second Tranche Waiver of Condition

1. Attached is a memorandum from the President entitled "Zambia: Economic Recovery Credit (3087-ZAM) - Release of Second Tranche" dated January 21, 1992.
2. In the absence of objection (to be communicated to the Vice President and Secretary or the Deputy Secretary by the close of business on January 30, 1992), the waiver of the condition in paragraph 3(b) of Schedule 3 (Annex A to the memorandum) will be deemed approved, and so recorded in the minutes of a subsequent meeting of the Executive Directors.
3. Questions on this memorandum should be referred to Mr. Todd (X35056).

Distribution:

Executive Directors and Alternates
Office of the President
Executive Vice Presidents, IFC and MIGA
Vice Presidents, Bank, IFC and MIGA
Directors and Department Heads,
Bank, IFC and MIGA

January 21, 1992

From: The President

ZAMBIA: Economic Recovery Credit (3087-ZAM)
Release of Second Tranche*

I. Introduction

1. Zambia is currently under suspension because the Government owes US\$51 million in debt service arrears to the Bank dating back to July 15. As discussed with the Joint Audit Committee on December 18, 1991, we are issuing this second tranche release memorandum prior to our arrears being cleared because this indication of Bank management support of the policies and actions of the new government will be critical in securing the donor support necessary for Zambia to clear its arrears with the Bank. We will not disburse any funds until our arrears are cleared and the suspension lifted.

II. Background

2. Credit 3087-ZAM, in the amount of US\$210 million equivalent, was approved by the Board on March 5, 1991, and was declared effective on March 13, 1991, at which time the first tranche of US\$130 million was disbursed. This credit is designed to provide import financing in support of Zambia's economic adjustment program, and, in particular, to assist Zambia with the foreign exchange cash flow during the year in which the arrears to the World Bank were being paid.

3. As outlined in the Policy Framework Paper (PFP) 1991-93, the overall aims of the adjustment program are to stabilize the economy through fiscal and monetary restraint and to restore sustainable growth

in the medium term through policies of structural realignment and improved incentives. The main structural objectives are to reduce the dependence on copper by encouraging non-traditional export growth, to lower the capital and import intensity of production and consumption, to increase savings and investment levels, and to help reduce poverty by expanding employment and income opportunities. Since achieving these objectives will mean substantial restructuring of the economy, a complementary goal is to protect vulnerable groups from the adverse impact of the adjustments.

4. The requirements for release of the second tranche were discussed frequently over this past summer. While policy performance in most structural areas remained good, serious policy slippage was occurring in the reduction of maize subsidies in particular and in budget deficit control in general. The previous Government could not take the remedial actions in these areas which we considered necessary because they felt the public reaction could threaten the process of transition to multi-party democracy. Other donors also refused to disburse balance of payments assistance, and arrears on external debt worsened. Zambia was declared in suspension by the Bank on September 13, 1991. Elections were held on October 31, 1991. They were considered fair. The opposition party won over 80 percent of the vote and captured the Presidency and over 80 percent of Parliament. A new Government was appointed and moved quickly to restore confidence and political stability. The new Government is also eager to restore good relations with the donors, as well as the Bank and Fund, and is strongly committed to the policy agenda of the ERC and the PFP.

5. The staff have continuously reviewed progress under the adjustment program since the ERC was first approved. Supervision missions visited Zambia in April, June, September, and December, and donor consultations were held in Paris in March and July, with informal briefings in June and December. This memorandum summarizes progress under the program. It concludes that progress in most areas of the program has been satisfactory. Seven of the eight conditions for release of the second tranche have been met. The condition relating to maize meal pricing can no longer be achieved because it was written in terms of containing the 1991 cost of maize-related subsidies below a specific figure long since exceeded. However, the new Government has moved quickly and decisively in this area. It has already increased consumer prices by over 100 percent and has agreed to monthly increases in 1992 that will eliminate all subsidies on breakfast meal by the end of the year and will reduce subsidies on roller meal to 20 percent of production cost. The subsidy on breakfast meal (the higher-cost product) has been reduced from 405 Kwacha per 25Kg bag to 50 Kwacha as a result of the recent price increases. Subsidies on the transport of maize and the sale of fertilizer will also be eliminated by mid-1992. This memorandum concludes that policies now adopted are a reasonable adaptation to current circumstances and, given the overall progress of the program, the condition on maize subsidies should be waived and the second tranche released. Finishing the agenda on maize market liberalization should be included as a specific component of the next structural adjustment credit, scheduled to be appraised in February and presented to the Board later this fiscal year.

6. Other donors have also maintained an interest in monitoring progress on this program. Germany and Japan (through OECF) are committed to co-financing the ERC. The German co-financing has been approved by their Parliament and is expected to be disbursed once we have indicated we are prepared to recommend release of this second tranche, subject to the arrears being cleared. The Japanese co-financing is less well advanced, in part because of the broader concerns OECF has had over the applicability of "Trinidad Terms" to their debt. Many other donors have provided balance of payments assistance to Zambia in support of the adjustment program,

including the UK, Sweden, Norway, the USA, the Netherlands, Canada, the EC, Finland and the African Development Bank.

III. Progress Under the Program

7. The current reform effort began in late 1988/early 1989. The policies are described in two PFPs, the first of which was reviewed by the Committee of the Whole in September 1989 and the second in March 1991. Because of the high level of arrears to the Bank and the Fund and the continually shifting external environment, an external financing plan was not agreed until early in 1991. With the considerable assistance of the donor community and from Zambia's own resources, the Bank arrears were completely cleared and the Fund arrears were reduced to the agreed level in March of that year. This allowed the Economic Recovery Credit (ERC) to be approved by the Board on March 5, 1991. An innovative "rights accumulation program" was approved by the Fund Board in April.

8. In general, progress under the program has been good in most structural areas, but there have been serious slippages in fiscal policy, which are being corrected in the 1992 budget, and difficulties were experienced in adjusting maize meal and fertilizer prices fast enough to contain the cost of Government subsidies. Progress in this area has resumed, but the target for total subsidy cost in 1991 will not be reached.

9. The overall program will not succeed unless macroeconomic stability is established and maintained. The original program called for a reduction in the fiscal deficit (on an accrual basis, excluding grants and interest) from 4.3% of GDP in 1990 to 0.7% in 1991. Performance in the first quarter was good, and the IMF target for bank financing of the deficit was met. Fiscal performance deteriorated in the second quarter, however, in part because of the increasing cost of subsidies but also because of lower than expected tax payments from ZCCM. Fiscal performance continued to deteriorate in the second half of 1991 primarily because of continued low ZCCM tax payments, crop financing to the cooperatives, and escalating maize subsidy costs. The final primary deficit (excluding grants) is likely to exceed 6 percent of GDP for 1991. The recent IMF mission worked with the Government on a 1992 budget that would reduce the deficit to 2 percent of GDP. The primary reductions in spending are in maize and fertilizer subsidies and crop financing. The budget will also contain some tax increases; in particular, all fringe benefits, including the housing allowance, will be subject to income tax. As a result of their satisfaction that macro-economic balance is being restored, IMF management has notified Bank management that they have no objections to the Bank releasing the second tranche of the ERC.

10. The liberalization of foreign trade through ending of restrictive import licensing, the closing of FEMAC, and the establishment of the second window on an open general license (OGL) basis has been one of the major accomplishments of the reform program. In April of this year (8 months ahead of schedule), the first and second windows were merged. The percentage of imports available on an OGL basis has been steadily increased to its current level of about 90 percent. We had hoped they would achieve 95 percent by mid-year, but this has not been possible because of the shortage of donor disbursements and consequently the very low level of reserves. The pent-up demand for the still excluded categories would not be sustainable at this time. It was also hoped that the OGL system could be shifted from a positive to a negative list for administrative ease. Clearly this could be done at any level of coverage. However, the Government has decided to wait until they reach the 95-96% level currently available in the export retention market which already uses a negative list system. Then the OGL system can adopt the same negative list as the export retention market. This is now expected in 1992, provided donor flows resume. One other consequence of the nearly non-existent balance of

payments assistance over the last eight months of 1991 has been the periodic accumulation of unsatisfied foreign exchange applications in the OGL. These delays have been the direct result of a shortage of foreign exchange due to lower than expected copper receipts and donor flows. With the anticipated resumption of donor support, the OGL should be able to resume timely clearance of these letters of credit.

11. The trade regime has been liberalized in other ways as well. No-funds import applications can now be processed by commercial banks. A number of exemptions from import tariffs and sales taxes were announced with the 1991 Budget, and the structure of tariffs has been compressed by raising the minimum and lowering the maximum rates. Progress in this area has been steady and on schedule.

12. Good progress has been made in the areas of parastatal reform and privatization. The contract for the study of ZIMCO (the parastatal holding company) has been signed, and work has started. Terms of reference for the study of the major parastatals (e.g. PTC, ZESCO, Zambia Airways, and Zambia Railways) have been agreed and funding arranged. Funding has also been secured for the follow-up study of 13 of the ZIMCO parastatals once the preliminary report of the ZIMCO study itself is completed late this year. The announcement of sale of the first seven parastatals appeared in the papers in late July, and 42 requests to bid have been received. The first sales are expected in early 1992. Strategy documents on the medium term privatization plan are being prepared for cabinet review. This is clearly an area that the new Government will emphasize strongly. The 1992 budget will contain a major commitment of local resources to staff the effort. We expect rapid progress in 1992.

13. Early emphasis in the civil service reform program has been on eliminating "ghost workers." After a slow start in getting the personnel inventory questionnaires completed and the necessary consultants in place, progress has been good. The computerization of the payroll records and pay system for certified daily employees has already produced considerable savings in many ministries where payments had been done largely in cash. Physical pay parades for the disbursement of checks to employees with proper identification have begun, and early savings are encouraging. Programs to reduce redundancies have not yet borne fruit and will probably not do so until the 1992 budget when the Government hopes to achieve an initial reduction of 10,000 employees through the elimination of redundancies.

14. After a slow start, good progress is also being made in implementing the Social Action Program. Six working groups have been set up with donor involvement to review proposals and to formulate medium-term policy, including budget priorities for 1992. The first implementation report has been prepared. The study of the maize coupon system was completed, and action was taken on some of the recommendations. However, the new Government has decided that the problems of inefficient targeting are endemic to the coupon program, which has therefore been discontinued. In its place, the Government is increasing budget allocations for purchase of medical and educational materials, strengthening the administration of the existing social action program, and providing a block grant of 1 billion Kwacha (compared to a total cost of the coupon program in 1991 of 1.2 billion Kwacha) in 1992 to augment the resources of the social welfare program for aid to the indigent. The micro-projects unit has been expanded and is now being supported by the Social Recovery Credit approved by the Board of Directors in June. This Unit will provide support to smaller projects with significant community involvement. A household survey was recently undertaken to establish a baseline for key social indicators and has submitted a preliminary report.

15. The most serious problems have arisen in the area of maize meal subsidies. All prices were decontrolled in 1989, except maize meal and fertilizer prices. The previous Government periodically tried to phase out these remaining price controls, but political pressures prevented this. The program for 1991 called for full decontrol of maize meal prices by mid-year unless available supplies fell short of projected demand, in which case, we were worried that a panic could push the market clearing price well above that needed by suppliers. In the event, supplies have fallen short, and therefore full decontrol was not expected. In that eventuality, however, the program called for increasing the controlled price so as to keep maize-related subsidies to the level agreed with the Fund in the 1991 budget. When that goal was set, the expectation was that the producer price would be 500 Kwacha per 90 Kg bag, and domestic inflation would be 40%. In fact, the producer price was raised to 800 Kwacha, a move we supported given the rapidly increasing price in contiguous countries and the rise in (illegal) maize exports from Zambia. In addition, domestic inflation is now expected to be nearer 100 percent in 1991. Thus the price increases necessary to contain the subsidy bill turned out to be much larger than expected.

16. However, the previous Government found itself unable to increase prices at all. As a result, the new Government inherited a rapidly escalating subsidy bill and consumer prices that were still 20 percent below the levels of June 1990 in nominal terms. After an intensive review of the options, the Cabinet adopted a plan which has increased consumer prices immediately (by 100 percent for roller meal and 165 percent for breakfast meal) and which will increase prices monthly in 1992 in order to end the subsidy on breakfast meal by end-1992 and to bring the subsidy on roller meal to 20 percent of production cost. This final subsidy will be phased out by mid-1993. Although these increases cannot restore the 1991 subsidy cost to the previously agreed level, it does return prices and subsidy amounts to levels previously agreed upon and will contain the total subsidy bill to the original PFP target of 1.9 percent of GDP in 1992.

IV. Summary of Second Tranche Release Conditions

17. All of the conditions have been met in substance, except for the limitation on maize subsidies. A listing of those conditions is attached as Annex A. The present status of those conditions is as follows:

(a) The first quarter fiscal performance was satisfactory although problems developed in the rest of the year that have required extensive corrective measures for 1992. The actual figure used in the release condition was taken from the IMF draft memorandum of February 1. When the program was approved by the IMF Board, the benchmark for increase of net banking credit in the first quarter had been changed. It was stated clearly in the minutes of negotiations that the intent of our condition was to reflect the fiscal benchmark of the IMF program (although we would interpret their fulfillment for our purposes). The revised benchmark was met and in fact was well exceeded if we count the ZCCM tax check for March which was not deposited until April 1. Met (see para. 9).

(b) The Borrower has made satisfactory progress in expanding the use of the OGL system, covering over 90 percent of imports, other than petroleum and fertilizer. The postponement in adopting a negative list until OGL coverage matches that in the no-funds market is primarily an administrative matter. Given the shortage of donor funds and hence the absence of a reserve cushion, they have expanded this list as quickly as has been prudent. Met (see para. 10).

(c) All export bans have been removed except white maize and maize products, petroleum, fertilizer, and ivory, and no new import duty exemptions have been added since January 1, 1991. Met

(d) The Borrower has adopted a satisfactory Public Investment program and has not undertaken any significant public investment projects outside that program. Met

(e) The Borrower has carried out a physical survey of public employees to eliminate "ghost workers" and has also computerized payroll records and completed the initial phase of a physical check pick-up system. Met (see para. 13).

(f) The Borrower has offered for sale to the private sector seven parastatals and has done preliminary work to offer five more soon. The first sales are expected in early 1992. Met (see para. 12).

(g) The Borrower has completed, under agreed terms of reference, an evaluation of the efficiency of the maize meal coupon system. Met (see para. 14).

(h) The maize condition was in two parts. Complete decontrol was not achieved, but the side letter clearly exempts the Borrower from achieving full decontrol if supplies are not adequate, which they were not. However, the Borrower did not contain maize subsidies within the 1991 budget which was the second part of the condition. (Technically, the condition refers only to maize handling subsidies. The overrun on maize subsidies will come from a new subsidy given directly to the mills. Renaming the subsidy does not change the logic, however, since the condition refers to adjusting the price of maize and maize meal to contain these subsidies.) Maize meal prices have recently been increased and are scheduled to continue increasing in 1992, but maize subsidies in 1991 will still be well above the level specified in the 1991 budget. Not met (see paras. 15-16).

Conclusion

18. The second tranche of the ERC should be released once arrears are cleared even though one condition has not been fully met, because the program is making good progress and because recent actions have brought the subsidy removal operation back on track. The new Government has shown strong commitment to the policies supported by the ERC and described in the PFP and has demonstrated this by implementing early actions. We are scheduled to bring to the Board a second adjustment credit later this year. The completion of maize price decontrol will be handled in that operation.

SCHEDULE 3

Actions Referred to in Paragraph 4 (b)
of Schedule 1 to this Agreement

1. The Borrower has implemented measures, satisfactory to the Association, for expanding the use of the Open General License (OGL) system to include all imports other than petroleum, petroleum products and other items specified in a short negative list.

2. The Borrower has furnished evidence, satisfactory to the Association, that the increase of net banking credit to the Borrower in the first quarter of 1991 did not exceed Kwacha 4,725,000,000.

3. (a) The Borrower has furnished to the Association evidence, satisfactory to the Association, that it has decontrolled the into-mill price of maize and the consumer price of maize meal products unless the Borrower has furnished to the Association evidence, satisfactory to the Association, that maize supplies (including imports) are not adequate.

(b) Notwithstanding the provisions of paragraph (a) above, the Borrower shall take all necessary measures, including adjusting the price of maize and maize meal, so as to hold the cost of maize handling subsidies not to exceed the amount (of Kwacha 2,478,000,000) specified in the 1991 budget.

4. The Borrower has furnished evidence, satisfactory to the Association that (a) it has removed all restrictions/prohibitions on exports with the exception of exports of maize, maize products, petroleum, petroleum products fertilizers and ivory; and (b) exemption from import duties and sales taxes continue to apply only to those imports benefitting from such exemptions as of January 1, 1991.

5. The Borrower has furnished to the Association a Public Investment Program (PIP) for 1991-1993, satisfactory to the Association and consistent with the Program, and has not undertaken any investment Project outside the PIP.

6. The Borrower has carried out a physical survey of public employees to ensure that only bona fide employees are being paid salaries.

7. The Borrower has furnished to the Association evidence, satisfactory to the Association, that it has offered for sale to the private sector at least six parastatals.

8. The Borrower has completed, under terms of reference satisfactory to the Association, an evaluation of the efficiency of the maize meal coupon system in assisting vulnerable groups.

International Bank for Reconstruction and Development

FOR OFFICIAL USE ONLY

SecM92-73

FROM: Vice President and Secretary

January 17, 1992

DECLASSIFIED

ZAMBIA

JUN 04 2025

Nonaccrual Status

WBG ARCHIVES

In view of nonpayment of outstanding debt service payment obligations, Zambia's loans and credits were placed in nonaccrual status as of January 16, 1992. This means that interest and charges on Zambia's loans/credits will be included in income only when received in cash, and that interest and charges accrued but not yet paid will be deducted from net income for the current quarter. As of January 15, 1992, US\$50.51 million equivalent was overdue to the IBRD. This amount consists of US\$32.92 million equivalent of principal and US\$17.59 million equivalent of interest and charges. Arrears to IDA totaled US\$1.21 million equivalent.

As of December 31, 1991, loans disbursed and outstanding to Zambia totaled US\$373.16 million equivalent, equal to .37 percent of all loans outstanding as of that date. IDA credits outstanding totaled US\$493.01 million equivalent.

Distribution:

Executive Directors and Alternates
Office of the President
Executive Vice Presidents, IFC and MIGA
Vice Presidents, Bank, IFC and MIGA
Directors and Departmental Heads, Bank, IFC, and MIGA

OFFICE MEMORANDUM

DATE: January 16, 1992

TO: Mr. Attila Karaosmanoglu, Managing Director, EXC

FROM: Edwin R. Lim, Acting AFRVP *EL*

EXTENSION: 34380

SUBJECT: ZAMBIA - Board Notification of Nonaccrual Status

Attached for your approval and subsequent transmittal to the Secretary's Department for distribution is the Notification to the Board regarding nonaccrual status.

The Notification to the Board has been cleared by the Legal and Loan Departments.

Attachments

Ms. Lim
Ed
Please go ahead.
AK.
1/16.



SecM

January 1992

FROM: Vice President and Secretary

ZAMBIA

Nonaccrual Status

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Distribution:

Executive Directors and Alternates
 President
 Managing Directors
 Vice Presidents
 Vice Presidents, IFC
 Directors and Department Heads, Bank and IFC

SecM

January 1992

FROM: Vice President and Secretary

ZAMBIA

Nonaccrual Status

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Executive Directors and Alternates
Office of the President
Executive Vice Presidents, IFC and MIGA
Vice Presidents, Bank, IFC and MIGA
Directors and Departmental Heads, Bank, IFC, and MIGA

NEWS RELEASE NO.

WORLD BANK PLACES LOANS TO ZAMBIA IN NONACCRUAL STATUS

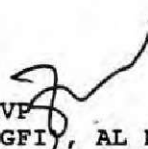
WASHINGTON, January , 1992. The World Bank has placed all loans to, or guaranteed by, Zambia in nonaccrual status, effective January 16, 1992. This action was in accordance with the Bank's standing policy of placing all its loans to, or guaranteed by, a country in nonaccrual status if a payment on any loan is overdue by more than six months. At December 31, 1991, the principal amount outstanding on Bank loans to Zambia was \$373.2 million equivalent or 0.37 percent of the Bank's total outstanding loans. Overdues totaling \$50.5 million equivalent consisted of \$32.9 million of principal and \$17.6 million in interest and other charges.

Zambia previously entered nonaccrual status in August 1987. It fully paid arrears of \$309 million on World Bank loans in March 1991. Zambia's subsequent failure to implement agreed adjustment programs resulted in reduced donor funding and Zambia's again becoming delinquent in making its debt service payments to the Bank. That delinquency, in turn, led the Bank to suspend disbursements to Zambia in September 1991. Since then Zambia has held democratic elections and has begun to implement many of the important reforms it has committed to undertaking.

The World Bank is currently negotiating with Zambia for the clearance of its arrears and the resumption of disbursements.

THE WORLD BANK/IFC/M.I.G.A.
WASHINGTON, D.C. 20433
U.S.A.
TELEX TRANSMITTAL

WDIAL
.AF6CO
OINFO

-SUBJECT: NOTICE OF NON-ACCRUAL STATUS
-DOCUMENT NAME: NACCRUAL.TLX
-DRAFTED BY: J.KISA:CA
-EXTENSION: 34413
-AUTHORIZED BY: EDWIN R. LIM, ACTING AFRVP 
-CW AND CC: MS. MULETA (LOALA), WHITE (LEGFI), AL HABSY (LEGAF),
-REEDY (LOAAF)
-CC: MESSRS./MMES. KARAOSMANOGLU (EXC); JAYCOX (AFRVP), SHIHATA
-(LEGVP); ECCLES (CTRVP); KASHIWAYA (CFSVP), WYSS (CODDR), THAHANE
-(SECGE), LINN (FPRVP), NISHIMIZU (FRSDR), GOLDBERG (LEGOP), ROTH
-(TREV), HUSAIN, MARTINEZ, OHRI, ARMSTRONG (AFRVP); DENNING, SINGH
-(AF6DR), PATEL, TODD, YANG, BRACHER, MACHADO, DI GIROLAMO (AF6CO);
-COOK (AF6IE); HELMAN (AF6AG), DE FERRANTI (AF6PH), SAM (AF6IN),
-WIJESINGHE (LOALA)

965 42221 =
-MINISTRY OF FINANCE
-LUSAKA, ZAMBIA
-ATT: HON. EMMANUEL G. KASONDE, MINISTER OF FINANCE
965 42999 =
-BANK OF ZAMBIA
-LUSAKA, ZAMBIA
-ATT: GOV. JACQUES BUSSIÈRES
IBRDLUS
-INTBAFRAD
-LUSAKA, ZAMBIA
-ATT: MR. JOHN INNES, RESIDENT REPRESENTATIVE
BT
WASHINGTON DC January 16, 1992

TO: HON. EMMANUEL G. KASONDE
MINISTER OF FINANCE

SUBJECT: NOTICE OF NONACCRUAL STATUS

AAA I REGRET TO INFORM YOU THAT AS OF JANUARY 15, 1992, THE IBRD HAS NOT RECEIVED PAYMENTS OF US DOLLARS 10.10 MILLION EQUIVALENT DUE ON JULY 15, 1991 UNDER LOAN NUMBERS 562-0, 563-0, 592-0, 645-0, 911-0 AND 919-0 TO ZAMBIA OR GUARANTEED BY ZAMBIA. THEREFORE, THE IBRD AND IDA HAVE BEEN OBLIGED TO PLACE ALL LOANS AND CREDITS TO ZAMBIA OR GUARANTEED BY ZAMBIA IN NONACCRUAL STATUS, AND HAVE SO INFORMED THE EXECUTIVE DIRECTORS. THE IBRD WILL ALSO INFORM ITS UNDERWRITERS AND RATING AGENCIES.

BBB IN ACCORDANCE WITH OUR POLICY TO STOP ACCRUING INTEREST AND CHARGES ON ALL LOANS/CREDITS TO OR GUARANTEED BY A BORROWER WHEN TWO CONSECUTIVE PAYMENTS HAVE BEEN MISSED, THE IBRD AND IDA FINANCIAL STATEMENTS WILL REFLECT INTEREST AND CHARGES ON LOANS AND CREDITS TO OR GUARANTEED BY ZAMBIA ONLY TO THE EXTENT THAT SUCH INTEREST AND CHARGES ARE ACTUALLY RECEIVED. WHEN ZAMBIA CLEARS ALL ITS OVERDUE SERVICE PAYMENTS, THE IBRD AND IDA FINANCIAL STATEMENTS WILL ONCE AGAIN REFLECT INTEREST AND CHARGES ON AN ACCRUAL BASIS.

CCC WHILE ZAMBIA IS IN NONACCRUAL STATUS, THE IBRD AND IDA WILL CONTINUE TO CALCULATE AND BILL INTEREST AND CHARGES TO ZAMBIA IN THE NORMAL MANNER.

DDD UNTIL ZAMBIA CLEARS ALL ARREARS TO THE IBRD AND IDA, IT WILL BE NECESSARY FOR THE RESPECTIVE FINANCIAL STATEMENTS TO DISCLOSE THAT ZAMBIA IS IN NONACCRUAL STATUS. IN ORDER FOR IBRD AND IDA TO RESUME ACCRUING INTEREST AND CHARGES ON LOANS AND CREDITS TO OR GUARANTEED BY ZAMBIA, IT WOULD BE NECESSARY FOR ZAMBIA TO CLEAR ALL ARREARS ON IBRD AND IDA LOANS AND CREDITS, WHICH AS OF JANUARY 15, 1992, TOTALLED US\$51.72 MILLION EQUIVALENT.

EEE WE AT THE BANK ARE ANXIOUS TO RESUME OPERATIONS IN ZAMBIA AND TO CONTINUE WORKING ACTIVELY WITH YOU FOR ZAMBIA'S ECONOMIC DEVELOPMENT. WE TRUST, THEREFORE, THAT YOUR GOVERNMENT WILL MAKE EVERY EFFORT TO CLEAR ALL ARREARS AS SOON AS POSSIBLE.

BEST REGARDS, EDWARD V.K. JAYCOX, VICE PRESIDENT, AFRICA REGION, THE WORLD BANK.

A L L - I N - 1 N O T E

DATE: 26-Dec-1991 07:14am

TO: Francis X. Colaco (FRANCIS X. COLACO)
TO: Edward V.K. Jaycox o/r (EDWARD V.K. JAYCOX)

FROM: Stephen Denning, AF6DR (STEPHEN DENNING)

EXT.: 34035

SUBJECT: Zambia: current status and next steps

Before I depart on home leave, I thought it might be useful if I report briefly on the current status of Zambia and lay out the next steps. No action is needed at this stage.

1. Game plan: The idea is to get bilateral flows started soonest on the understanding that the program is back on track, with the blessing of the Bank and the Fund, and that this will enable Zambia to pay its arrears (\$37 million), upon which we would release the second tranche of the Economic Recovery Credit (ERC). A new PFP and CG would be organized by the middle of the year.
2. JAC briefing: I made a brief presentation to the JAC on December 18. I indicated that we were very likely to be issuing the memorandum to the EDs proposing release of the second tranche before arrears are cleared. There were no questions and the chairman expressed the JAC's appreciation of "these positive developments".
3. Need to seek the Board's approval: One footnote on the reason for needing to seek the Board's approval: seven of the eight conditions for release of the second tranche have been fully met, while the eighth condition has been met "in substance" but not technically. The eighth condition concerned an obligation to limit maize subsidies to a certain amount in 1991. Subsidies have exceeded the agreed amount, hence technically the condition has not been met and cannot now be met, given the way the condition was drafted. However the Government has taken decisive action increasing maize prices by more than a 100%, thus getting back on to the track that had been originally envisaged, and going considerably beyond what we had been discussing with the former Government as being sufficient for release. Therefore we believe that that the condition has been met in substance, but technically it is a waiver of the terms of the original condition, and thereby requires Board approval on a "no objection" basis.
3. Memorandum to the EDs: the draft memorandum to the EDs proposing release of the second tranche is currently being worked on in the Region and is expected to be ready for RVP and MD

clearance late December or early January.

4. IMF "no objection" letter: Agreement was reached on Tuesday (December 23) at the staff level in the IMF to give its "no objection" letter to the release of the second tranche, once Zambia takes some upfront actions i.e. (i) maize price increases (already done); (ii) increases on oil prices (agreed, and expected any day); and (iii) increase in interest rates. The good news here is that the IMF are not seeking immediate payment of any part of the \$120 million arrears in 1991, as the quid pro quo for the "no objection" letter. Instead, they have deferred this discussion till later in the year, when the PFP is negotiated, and the Rights Approach is renegotiated. This staff recommendation still needs IMF management approval, which if not forthcoming might need a high-level intervention with Mr. Camdessus or Mr. Erb. As of now, we don't expect the need for any such intervention.

5. Informal briefing of donor EDs: It has been the practice to hold regular briefings of donor EDs on developments in Zambia. We plan to hold another such briefing early in January, just prior to issuing the memorandum proposing the release of the second tranche, to make sure that there are no surprises with the Board. The memorandum would be distributed on a "no objection" basis, and, with this preparatory work, we would not expect any request for a discussion.

6. Donor flows: We are counting on five donors to get flows going: UK, Germany, and US, and in smaller amounts, Canada and Norway. Each of these agencies are in various stages of processing their funding. Our best estimate now is mid to late January for clearance of the arrears.

7. Praful Patel will be acting for me most of January. The task manager, John Todd, and the country officer, Jack Kisa, will be on hand to deal with questions arising from these various steps.

CC: Praful Patel
CC: Attila Karaosmanoglu
CC: Arnold Clift
CC: John Todd
CC: Jack Kisa

(PRAFUL PATEL)
(ATTILA KARAOSSMANOGLU)
(ARNOLD CLIFT)
(JOHN TODD)
(JACK KISA)

Presentation to the Joint Audit Committee

December 18, 1991

Statement of Mr. Stephen Denning, Director AF6

Mr. Chairman,

When I presented the Zambia situation to this committee last February, it was just before a complicated set of transactions involving very substantial bilateral donors support, and Bank Board approval of the Economic Recovery Credit (US\$235 million), Bank arrears of \$330 million were cleared, and the IMF put in place the "rights approach" to regularize some US\$1.1 billion in IMF arrears.

Performance in many areas of the economic reform program have gone well, and all but one of the conditions for the release of the second tranche of the Economic Recovery Credit were met. However fiscal discipline disintegrated in the midst of a hard-fought election campaign, and in May 1991, the Government reneged on its commitments to reduce subsidies on the consumption of maize.

In the Zambian economy, consumer maize prices are a central issue, and on the Bank/IMF recommendation, the bilaterals stopped quick-disbursing support for the program. The Government was unable to meet its debt service obligations to the Bank and the IMF. On September 13, 1991, there was a general suspension of disbursements to Zambia for non-payment of arrears. Arrears will be around US\$37 million around the end of the year.

At the time of entering these transactions last February and March, we had flagged the risk entailed in lending to a government that was entering an election campaign -- a risk that has in fact materialized. We had also underlined that there was in our judgement a broad consensus on adjustment and the direction of economic reform that would survive the election result. This prediction also looks as though it will be borne out.

On October 31, 1991, in one of the few genuinely democratic elections in Africa, President Chiluba won a decisive victory, and has appointed an impressive Cabinet. The Bank/IMF mission which returned Friday has confirmed that the Government is moving aggressively to restore fiscal discipline and to mobilize the energies of the private sector.

The new government has inherited a very difficult fiscal situation, and a crushing debt burden, from its

predecessor.

On consumer maize prices, the Government took on December 13 the tough decision that its predecessor refused to take.

We are now working very closely with IMF and the donor community to regularize the situation.

An informal donor meeting held in Paris on December 11, 1991, confirmed widespread donor willingness to support the new Government, combined however with a strong reluctance to make disbursements before the Bank/IMF had formally endorsed the new Government's program. All substantive conditions for the release of the second tranche of the Economic Recovery Credit have now been met.

We are now moving to prepare a memorandum to the EDs proposing to release the second tranche of an adjustment credit, subject to reducing arrears to zero, and removing the general suspension now in effect.

We would obviously like to get the arrears cleared before issuing the memo to the EDs.

The Government however does not have sufficient cash on hand to clear the arrears. Clearing the arrears depends on donor flows starting.

While a group of five donors are willing to disburse enough funds to enable Zambia to clear the arrears, they are unlikely to do so until they get an unambiguous signal to proceed, such as the distribution to the Executive Directors of the Bank's memorandum proposing release of the second tranche.

Other alternatives to solve the chicken-and-egg problem are being reviewed. However the negotiation of a bridge loan from a commercial bank would be costly and time consuming. Similarly, if all donors would pay funds directly into trust funds into the Bank, this would solve the problem, but it seems unlikely that this will happen.

It seems more probable that donors will insist on receiving an unambiguous signal before disbursing. We believe that we have to find a way to give such a signal. We believe that it is important that international financial support for the new Government materialize relatively quickly, and in such a situation, we expect that the management will be issuing the memorandum to the Executive Directors proposing release of the second tranche, even before the arrears are cleared. We would underline that it

would be fundamental to any such arrangements that the
second tranche would not be released until arrears are
reduced to zero.

In this process, we are working very collaboratively with the Fund. I should also note that before issuing the memorandum to the Executive Directors, we will also need to obtain a "no-objection" letter from the IMF, to which Zambia has arrears in service payments of some \$US120 million. There are reasonable prospects of obtaining such a letter quickly, provided that IMF management accepts a two-stage approach to resolving its arrears problem, involving agreement for the release of the Bank's second tranche in order to trigger new bilateral flows to Zambia, followed by more comprehensive set of understandings to be developed over the coming months, laying the basis for a reformulated "rights approach" to be concluded some time around the middle of 1992.

I am therefore hopeful that the arrears will be cleared in January 1992 and that full normalization of relations with the IMF will take place by the middle of the year. This full regularization will require strong bilateral port, and a vigorous "solution-mindedness" on the part of the Bank and Fund management. I think that the first indications of the international community in Paris on December 11 were extremely positive, and that although there is a long and difficult road in front of us, we do see a way to resolve the issues.

Thank you.

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The World Bank/IFC/MIGA
O F F I C E M E M O R A N D U M

DATE: December 17, 1991 07:24am

TO: Edward V.K. Jaycox (EDWARD V.K. JAYCOX)

FROM: Stephen Denning, AF6DR (STEPHEN DENNING)

EXT.: 34035

SUBJECT: Zambia: clearing the arrears; and Mr. Preston's visit

Kim,

One further piece of good news: we learned yesterday that the U.S. has decided to contribute some \$10 million for Zambia to help clear the Bank arrears. As the U.S. had taken the toughest and most drastic stance when the program went off track in mid-year, this is strong evidence that the donor coalition is coming back together again. This will offer some encouragement to other bilaterals who are expected to be willing to assist the Zambia program in the near future, i.e. U.K., Germany, Norway and Canada. (As was done last March, the U.S. money would be made available directly to a trust fund in the Bank and would be contingent on the whole amount of the arrears being cleared.)

Based on the positive developments, we are proposing to confirm the Zambia leg of Mr. Preston's visit to the Zambia Government. Discussions with the other three Governments -- Tanzania, Zimbabwe and South Africa -- are already under way and are proceeding well.

Steve

CC: Attila Karaosmanoglu	(ATTILA KARAOSMANOGLU)
CC: Praful Patel	(PRAFUL PATEL)
CC: John Todd	(JOHN TODD)
CC: Jack Kisa	(JACK KISA)
CC: Patricia O'Hara	(PATRICIA OHARA)
CC: Africa ISC Files	(AFRICA ISC FILES)

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The World Bank/IFC/MIGA
O F F I C E M E M O R A N D U M

DATE: December 15, 1991 09:29am

TO: Edward V.K. Jaycox (EDWARD V.K. JAYCOX)
TO: Attila Karaosmanoglu (ATTILA KARAOSMANOGLU)

FROM: Stephen Denning, AF6DR (STEPHEN DENNING)

EXT.: 34035

SUBJECT: Zambia: release of the ERC second tranche

Last Friday (December 13), the Zambia Government announced the decision to increase consumer maize prices by well over 100%, effective immediately. All conditions for the release of the second tranche (US\$77 million) of the Economic Recovery Credit have now been met in substance. We are now preparing a memorandum to the Executive Directors proposing release of the second tranche. While the second tranche cannot be released until Zambia's debt service arrears with the Bank Group (US\$37 million by end December) are cleared, we would like to have approval to brief the Joint Audit Committee that we plan to circulate a memorandum to the Executive Directors proposing to release the second tranche prior to the clearance of arrears and conditional on payment of the arrears.

Background

On October 31, 1991, in one of the few genuinely democratic elections in Africa, President Chiluba won a decisive victory, and has appointed an impressive Cabinet. The Bank/IMF mission which returned Friday has confirmed that the Government is moving aggressively to restore fiscal discipline and to mobilize the energies of the private sector. On consumer maize prices, the Government has taken the tough decision that its predecessor refused to take. An informal donor meeting held in Paris on December 11, 1991, confirmed widespread donor willingness to support the new Government, combined however with a strong reluctance to make disbursements before the Bank/IMF had formally endorsed the new Government's program, for instance, by a decision to release the second tranche (US\$77 million) of the Bank's Economic Recovery Credit, for which all substantive conditions have now been met.

It is normal Bank practice to insist on clearance of arrears before issuing a proposal to our Executive Directors to release the second tranche of an adjustment credit. The Government however does not have sufficient cash on hand to clear the arrears. While the UK, many, and in smaller amounts, Canada and Norway, are willing to disburse enough funds to enable Zambia to clear the arrears, they are unlikely do so until the Bank's memorandum proposing release of the second tranche has been distributed to our Executive Directors, thus signifying an unambiguous decision on our part to proceed.

We are thus faced with a chicken-and-egg situation. If we follow standard Bank practice, we cannot issue the memorandum to the Executive Directors until Zambia clears the arrears. However Zambia cannot clear the arrears until it gets funds from the bilaterals who will probably not move until we issue the memorandum to the Executive Directors. Other alternatives like the negotiation of a bridge loan from a commercial bank would be costly and time consuming. We believe that it is important for international financial support for the new Government to materialize relatively quickly

It would not be the first occasion for such an exception. A similar exception was made in Zambia in March 1991 when the arrears to be cleared were much larger (\$330 million compared to the \$37 million that will be due by end December). We believe that a similar exception Bank practice is warranted.

We are making a presentation on Zambia to the Joint Audit Committee this coming Wednesday (December 18) and we could use this occasion to inform the Board of our intention to proceed in this fashion and ensure that there is a consensus to make the necessary exception.

I should also note that before issuing the memorandum to the Executive Directors, we will also need to obtain a "no-objection" letter from the IMF, to which Zambia now has arrears in service payments of some \$US120 million. There are reasonable prospects of obtaining such a letter quickly, provided that IMF management accepts a two-stage approach to resolving its arrears problem, involving agreement for the release of the Bank's second tranche in order to trigger new bilateral flows to Zambia, followed by a more comprehensive set of understandings to be developed over the coming months, laying the basis for a reformulated "rights approach" to be concluded some time around the middle of 1992.

May we have your approval to brief the Joint Audit Committee that we plan, once we have the IMF no-objection letter, to issue to the Executive Directors the memorandum recommending release of the second tranche of the Economic Recovery Credit?

CC: Ishrat Husain
CC: Praful Patel
CC: John Todd
CC: Dunstan Wai

(ISHRAT HUSAIN)
(PRAFUL PATEL)
(JOHN TODD)
(DUNSTAN WAI)

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The World Bank/IFC/MIGA
O F F I C E M E M O R A N D U M

DATE: December 5, 1991 05:30pm

TO: Edwin Lim (EDWIN LIM)

FROM: Stephen Denning, AF6DR (STEPHEN DENNING)

EXT.: 34035

SUBJECT: Zimbabwe Structural Adjustment Loan/Credit

This is to update you on the status of the Zimbabwe Structural Adjustment Loan (SAL) which falls between the arrangements for the approval of adjustment operations before and after December 1, 1991, and inform you of our intention to issue an intention to negotiate.

The appraisal of the Zimbabwe SAL of US\$ 125 million was authorized by the Operations Committee in March 1991. As stated in the memorandum from Mr. Jaycox to Mr. Wapenhans, Acting SVP, of November 22, the appraisal of the loan was consistent with the IM presented to the OC in March. However, two points were highlighted: the amount of the operation had been increased in view of higher than expected financial needs, and the opening up of the economy was proceeding through a combination of OGIL and export retention schemes (originally, only OGIL was envisaged). In view of a deteriorating balance of payments situation, Zimbabwe requested an Extended Fund Facility from the IMF.

A proposed Structural Adjustment Loan for US\$ 125 million and a Structural Adjustment Credit for US\$ 50 million equivalent was circulated to the Operations Committee for review on a no-objection basis on November 25, 1991. A memorandum to that effect from Mr. Enzo Grilli, indicated that comments should be directed to the RVP by c.o.b. December 5, 1991.

No objections have been received to date, and in the absence of objections by the deadline, we intend to issue an invitation tomorrow to the Government of Zimbabwe to negotiate the Loan/Credit next week, in Washington.

Policy measures to be taken before negotiations, as agreed with the Appraisal mission in September, have been implemented. A draft of the Letter of Development Policy has been agreed and will be finalized during negotiations; however, no fundamental changes are envisaged.

The IMF has already negotiated an EFF for SDR 343.8 million that will be partially converted into an ESAF should Zimbabwe be declared eligible for such financing. The IMF staff is sending the EFF program to management for formal approval, contingent on

getting assurances on two financial issues are clarified (elimination of "caps" on lending rates and additional increase in rediscount rates). Given the substantial progress that has taken place and the expectation that the two mentioned issues will be resolved in the very near future, we propose to go ahead with the negotiations. The Zimbabweans will be informed again on the need to resolve the pending issues with the IMF before we send the Loan/Credit documentation to our Board.

There is a fairly tight sequence of steps involved in the completion of Bank/IMF processing of the SAL and EFF documents in early December, the presentation of those operations to the respective Boards in January, Mr. Preston's proposed trip to Zimbabwe in early February, and a planned CG in Paris on February 17-18.

If you have any guidance on this, please let me know, particularly whether there is any need for further discussion needed prior to issuing the invitation to negotiate.

CC: Attila Karaosmanoglu
CC: Edward V.K. Jaycox
CC: Ishrat Husain
CC: Praful Patel
CC: Carlos Elbirt
CC: Roger Grawe
CC: Fred King
CC: Enzo Grilli
CC: Aberra Zerabruk

(ATTILA KARAOSMANOGLU)
(EDWARD V.K. JAYCOX)
(ISHRAT HUSAIN)
(PRAFUL PATEL)
(CARLOS ELBIRT)
(ROGER GRAWE)
(FRED KING)
(ENZO GRILLI)
(ABERRA ZERABRUK)