

Jesuit Centre for Theological Reflection (JCTR)

Submission to the Estimate Committee on

**The Status of Zambia's Domestic and External Debt and the Citizens' Participation in
Economic Development**

13th January 2012

A. The Status of Zambia's Domestic and External Debt

i. The Policy Framework on debt management

A strong legal and institutional and policy framework is an essential component of an efficient debt management system for any country. Two important aspects of debt management are reviewed here – the legal framework and institutional framework for debt management and coordination purposes.

Legal Framework:

The contraction and management of public debt in Zambia is governed by several legislations and regulation. The principle laws and regulations that provide the legal framework for public debt contraction and management are contained in Part X of the Constitution of Zambia and Volume 20 of the Laws of Zambia covering chapters 347 to 379 with the following particularly being noteworthy:

- CAP 348; Treasury Bills,
- CAP 350; General Loan and Stock Act,
- CAP 353; Local Loans (Registered Stock and Securities) Act,
- CAP 355; Loan (Authorization) Act;
- CAP 358; General Loans (Guarantee) Act,
- CAP 366; Loans and Guarantees (Authorization) Act.

Prominent among these Acts is the Loans and Guarantees (Authorization) Act which specifically provides for the raising of loans, the establishment of sinking funds, issuance of guarantees and indemnities and the granting of loans by or on behalf of the Government. CAP 366 also provides for the limits of the amounts of loans raised both within and outside the country. Section 3 states that the Minister of Finance may raise from time to time, loans not exceeding an amount outstanding at any one time such amounts as he shall from time to time be authorized by resolution of the National Assembly to prescribe by statutory instrument. The Act further in section 15 authorises the Minister to guarantee the repayment

to any person ordinarily resident in and outside Zambia of any loan or any portion of the loan. From 1988, the Minister's limit for foreign loans has been at K20 trillion (approximately US\$5 billion) per year and at K5 trillion (US\$1 billion) per year for domestic loans.

Institutional Framework:

The Act further provides for the establishment of institutional structures to carry out the day-to-day functions of borrowing and repayment of loans thereafter contracted. Under this provision, the country has two sites from where debt management is conducted, the Ministry of Finance and National Planning (MoFNP) and the Bank of Zambia (BOZ). The Ministry manages the country's external debt as it relates to public and publicly guaranteed debt. It is in charge for negotiating, contracting, guaranteeing, record keeping and debt servicing of external debt. In the area of domestic debt, the ministry is mainly in-charge of servicing of interest on government securities. It also maintains data on internal suppliers' credit, contingent liabilities of local government entities and state enterprises. The Bank of Zambia is charged with the responsibility of monitoring, recording its own and private sector contracted short-term external debt, management of domestic debt, in particular government securities and effecting external debt service.

Observations on the Legal and Institutional Framework

It is true that Zambia has many laws and regulations that govern public debt management. For example CAP 366 and other laws define functions and responsibilities of the Ministry of Finance and National Planning and the Bank of Zambia that determines the level of indebtedness and guarantees that the country can undertake. But while legal and administrative framework for the management of national debt exists, they are fraught with very serious weaknesses. These include:

- ***Lack of high-level coordination*** – it is important that the legal framework of debt management defines clearly the responsibilities and functions of the various agencies involved in debt management so as to avoid duplication of functions. For example, while the Loan (stock, Bonds and Treasury Bills) regulations and the Bank of Zambia Act gives power to the central bank to undertake and manage government securities that are publicly issued, the law also assigns the responsibility of registering securities to the Ministry of Finance and National Planning
- ***Lack of guidelines in terms of borrowing*** – while the law has imposed limits of indebtedness to the Government, it has not done so to the public sector nor for local governments, except when requesting guarantees. Furthermore, there is no legislation that details the process that need to be followed to obtain the approval of guarantees from the Ministry, nor do regulations establish any requirements that the public sector need to provide to MOFNP to obtain it.
- ***Absence of basic permanent negotiation teams;***
- ***Lack of public accountability;*** and
- ***Centralization of borrowing powers in one office*** which is also not adequately overseen by parliament.

There is therefore overall lack of a debt strategy and policy in Zambia to guide the country in the areas of borrowing, terms of borrowing and the purpose of borrowing. This coupled with significant political involvement and poor data management can easily result in uncontrolled debt and litigations. Emerging best practice is to have in place a comprehensive debt strategy and policy that stipulates when to borrow, at what terms and for what purpose. Such practices ensure that government financing needs and its payment obligations are met at the lowest possible cost while debt levels remain at sustainable levels.

ii. Current External Debt Stock

Type of External Debt	US\$' billion	K' trillion
Public	1.3 billion	*6.5 trillion
Publicly Guaranteed	1.7 billion	*8.5 trillion
Total External Debt	3.0 billion	*15 trillion

2010 Economic Report

iii. External Debt Trends

Year	Public Debt US\$'	Debt Stock US\$	GDP US\$	% of GDP	Debt Service US\$'	% of Budget
2005	4.1 billion	4.5 billion	7.2 billion	*63	384.1 million	*22
2006	696.7 million	1.5 billion	10.7 billion	*14	65.18 million	*4
2007	\$1.0 billion	2.0 billion	11.5 billion	*17	60.9 million	*3
2008	1.2 billion	2.3 billion	14.6 billion	*16	60.1 million	*3
2009	1.5 billion	3.5 billion	12.8 billion	*27	53.7 million	*2
2010	1.3 billion	3.0 billion	16.1 billion	*19	48.90 million	*2

*Based on calculations based on approved budget figures/GDP Statistics Source: World Bank, World Development Indicators

iv. Zambia's Creditors

Year	Creditor	Purpose	Amount US\$
2005	<ul style="list-style-type: none"> Data un-available 		
2006	<ul style="list-style-type: none"> International Development Association (IDA) 	<ul style="list-style-type: none"> Public Service Management Support 	<ul style="list-style-type: none"> 29,754,760
	<ul style="list-style-type: none"> International Development Association (IDA) 	<ul style="list-style-type: none"> Water Sector Performance Improvement 	<ul style="list-style-type: none"> 22,567,620
	<ul style="list-style-type: none"> International Fund for Agriculture Development (IFAD) 	<ul style="list-style-type: none"> Smallholder Livestock Investment 	<ul style="list-style-type: none"> 10,310,934
	<ul style="list-style-type: none"> People's Republic of China (P.R. China) 	<ul style="list-style-type: none"> TAZARA Protocol 	<ul style="list-style-type: none"> 6,250,774
	<ul style="list-style-type: none"> Arab Bank for Economic Development in Africa (BADEA) 	<ul style="list-style-type: none"> Water Supply to Six Towns 	<ul style="list-style-type: none"> 6,800,000
	<ul style="list-style-type: none"> Opec Fund for International Development (OFID) 	<ul style="list-style-type: none"> Water Supply to Six Towns 	<ul style="list-style-type: none"> 4,000,000
2007	<ul style="list-style-type: none"> International Development Association (IDA) 	<ul style="list-style-type: none"> Road rehabilitation and Maintenance Project 	<ul style="list-style-type: none"> 24,746,240
	<ul style="list-style-type: none"> African Development Foundation (ADF) 	<ul style="list-style-type: none"> Poverty Reduction Poverty Support 	<ul style="list-style-type: none"> 30,000,000
	<ul style="list-style-type: none"> ADF 	<ul style="list-style-type: none"> Water Supply and Sanitation 	<ul style="list-style-type: none"> 22,425,000
	<ul style="list-style-type: none"> IDA 	<ul style="list-style-type: none"> Regional Trade Facilitation Project 	<ul style="list-style-type: none"> 17,086,690

	<ul style="list-style-type: none"> • Exim Bank-China 	<ul style="list-style-type: none"> • Earth-Moving Equipment 	<ul style="list-style-type: none"> • 39,899,000
	<ul style="list-style-type: none"> • OFID 	<ul style="list-style-type: none"> • Copperbelt Feeder Road Rehabilitation Project 	<ul style="list-style-type: none"> • 6,000,000
2008	<ul style="list-style-type: none"> • BADEA 	<ul style="list-style-type: none"> • Copperbelt Feeder Roads Project 	<ul style="list-style-type: none"> • 8,000,000
	<ul style="list-style-type: none"> • IDA 	<ul style="list-style-type: none"> • Economic Management and Growth Facility Credit 	<ul style="list-style-type: none"> • 10,000,000
	<ul style="list-style-type: none"> • IDA 	<ul style="list-style-type: none"> • Increased Access to Electricity 	<ul style="list-style-type: none"> • 33,000,000
	<ul style="list-style-type: none"> • African Development Bank (ADB) 	<ul style="list-style-type: none"> • Poverty Reduction Budget Support II 	<ul style="list-style-type: none"> • 24,000,000
	<ul style="list-style-type: none"> • ADB 	<ul style="list-style-type: none"> • Nkana Water and Sanitation Project 	<ul style="list-style-type: none"> • 57,000,000
2009	<ul style="list-style-type: none"> • IDA 	<ul style="list-style-type: none"> • Road Rehabilitation Project 	<ul style="list-style-type: none"> • 75,700,000
	<ul style="list-style-type: none"> • OFID 	<ul style="list-style-type: none"> • Kalabo-Sikongo Angola Border Project 	<ul style="list-style-type: none"> • 10,000,000
	<ul style="list-style-type: none"> • Exim-China 	<ul style="list-style-type: none"> • Procurement of non-intrusive scanners 	<ul style="list-style-type: none"> • 45,800,000
	<ul style="list-style-type: none"> • Exim-China 	<ul style="list-style-type: none"> • Rehabilitation and Maintenance of storage sheds 	<ul style="list-style-type: none"> • 11,600,000
	<ul style="list-style-type: none"> • Exim-China 	<ul style="list-style-type: none"> • Completion of Government Complex Project 	<ul style="list-style-type: none"> • 25,000,000
	<ul style="list-style-type: none"> • OFID 	<ul style="list-style-type: none"> • Cancer Diseases Hospital Project-II 	<ul style="list-style-type: none"> • 6,000,000
	<ul style="list-style-type: none"> • Japanese International Cooperation Agency 	<ul style="list-style-type: none"> • Increased Access to 	<ul style="list-style-type: none"> • 59,200,000

	(JICA)	Electricity	
2010	<ul style="list-style-type: none"> Data un-available 	<ul style="list-style-type: none"> 	<ul style="list-style-type: none">

Zambia Economic Reports 2005-2010

v. Purpose and Utilization of External Loans

There are a lot of questions raised as regards the purpose of loans that the country contracts as well as the usage of loan funds. This is because both policy and legal framework does not guarantee transparency, accountability and parliamentary participation and approval to ensure government justifies why they are contracting a particular loan and what the cost would be to the country in terms of conditionalities. This will help ensure loans being contracted are in line with identified priority areas in the National Development Plan. There is need for the government to strengthen monitoring and evaluation of loan projects to ensure implementation is in line of set objectives, timely implementation and that impact is great and results in improved living conditions of the citizens.

To ensure that loan funds are used for the benefit of citizens, the Jesuit Centre for Theological Reflection (JCTR) conducts Debt Resource Monitoring and as such has monitored some loan projects which include the following:

- a. OFID/BADEA US\$14 million Copper belt Feeder Roads Project- Despite the government contracting these loans in 2007 and 2008 respectively, our report reveals the following;
 - The loan was necessary given the need to promote agriculture development and economy diversification and the poor feeder road infrastructure in the province;
 - works had not commenced as late as December 2010 with implementation being expected to commence in 2009;
 - Instead of the initial 768km, only 210km will now be covered by the project at the same loan amount and interest;
 - The road network in the targeted roads in Mpongwe has worsened;
 - This has lead to continued difficulties and increased cost of farmers transporting farm inputs and produce for which the project was aimed at.
- b. AfDB US\$36.9 million Central Province Water and Sanitation Project:
 - Given the fact that access to clean and safe water and sanitation is now recognised as a Human Right and that a great majority of citizens in Central Province and Kapiri Mposhi in particular had no access, to clean and safe water and sanitation, the loan was necessary;

- At the time of reporting, the project was in completion stage with only the sanitation part remaining;
- setting up of a commercial utility company had been completed;
- 99.38% of the loan and about 80% of the grant had been disbursed;
- The project generally lacked impact as most of the residents had not connected to the water and sewerage lines as the cost of connection by Lukanga Water and Sewerage was very high;
- Sanitation still remains poor in the district as majority of residents were still found to use self-made pit latrines near un protected wells, while others still use the bush or their back yards in the night;
- The construction of pit latrines from the project was slow and against the set criterion for beneficiaries;
- However, in areas such as East Park where majority of residents had connected to water and sanitation, the benefits were felt in terms of 24 hour access to water and gardening;
- A good number of kiosks have no running water while some are rarely open. True to this, some kiosks were found to be closed at the time of monitoring;
- The kiosks were also found to be inadequate and in some areas not evenly distributed.

c. IDA US\$ 33 million Increased Access to Electricity Supply Project:

- The loan agreement for this project was signed in 2008 and is currently under implementation;
- Preliminary findings from project areas (Rural Electrification) monitored in Mwinilunga and Ikelenge districts show that the loan project is a necessary one as a great majority of citizens and government institutions such as schools and Rural Health Centres in the area have no access to power and thus rely on firewood, charcoal, lamps, etc which affects productivity and the quality of life and public services;
- This has also resulted in poor retention of civil servants who leave the institutions in the area for those with access to electricity;
- It is also noted that, the government intends to set up mini hydro stations and solar packages in Zengamina and Salujinga respectively even though there is already a private hydro station in operation with sufficient capacity to meet power demand for the areas.

vi. 2005-2010 Trend

Year	Debt Stock K' billion	Debt Stock US\$'	GDP US\$'	% of GDP
2005	6,189.4	1,237,880,000	7.2 billion	*17.2
2006	8,798.24	1,759,648,000	10.7 billion	*16.4
2007	8,279.05	1,655,810,000	11.5 billion	*14.4
2008	8,517.7	1,703,540,000	14.6 billion	*11.6
2009	10,520.6	2,104,120,000	12.8 billion	16.4
2010	10,591.96	2,118,392,000	16.1 billion	*13.2

Sources: 2005 to 2010 Economic Reports and World Bank Statistics

*Based on calculations/ Debt Stock in US\$ calculated @K5, 000 per US\$

vii. Local Creditor Institutions

Table 1: Domestic Debt Position, 2008-2010

Debt Category	Dec-10 (K' Billion)
Treasury bills	
Sub Total	4,501.5
Bonds	
Sub Total	5,439.4
Total Securities	9,941.0
Domestic Arrears	
Various Creditors	242.8
Sub Total	242.8
Public Service Pension Fund	
Sub Total	58.0
Awards and Compensation	
Sub Total	350.0
Grand Total	10,591.7

Source: Ministry of Finance and National Planning and Bank of Zambia

NB: Specific data on institutions owed by government not available.

ix. Measures in place to ensure that the external and domestic debt remains sustainable

Government's capacity to manage external and domestic debt within sustainable levels is relatively low. Even though Zambia participates in the joint IMF/World Bank Debt Reform and Capacity Building Program and due for an IMF debt sustainability assessment programme later this year, much remains to be done to ensure that domestic and external debt remains sustainable.

Efforts to strengthen debt management have been made by Government. As a first step, Government prepared *a debt management strategy* in 2008 that describes the existing institutional framework and procedures, and highlights the need to consolidate the legal framework. However, its implementation has stalled and thus Government is still working under old legislation with regard to loan contraction and management.

Government further announces its borrowing ceilings in the annual budget for both domestic and external debt as a way of limiting its liability but it rarely sticks to these limits. There have also been promises by government to access more of grants than commercial loans but often we have seen government borrow commercial loans.

x. Suggested way forward

Zambia's public debt is currently sustainable as the ratio of public debt to GDP at 19% is below the generally accepted threshold of 40%. However, the current legal framework regarding debt contraction and debt management are neither adequate nor appropriate enough to prevent Zambia from slipping back into another debt trap. While some notable progress has been made in enhancing debt management much remains to be done to effectively address the danger of slipping into another debt crisis.

- **Legal and Institutional Framework** - enhance the legislative framework of external and domestic debt management by regulating the borrowing procedures and responsibilities of the various agencies involved in the process. Currently, the law is not very clear about the role of Ministry of Finance and Bank of Zambia and other government agencies. The review of legal and institutional framework should guarantee further lead to the following:
 - **Enhance Parliamentary and Citizen Participation** – the legal and institutional reforms must ensure that the loan contraction process is transparent and participatory, i.e. parliament and/or citizens and affected communities in the borrowing nation must be given adequate time and information to debate the taking-on of the loan, including purpose, terms and conditions of the loan in accordance with the national constitution. Currently, Parliament only approves the budget including the loan financing component of the budget but has no say on the determination of the terms and conditions of the loan. Legal reforms should therefore be implemented concerning loan

contraction and management that will enhance parliamentary oversight. The JCTR have tabled a proposal for this legal framework before the National Constitutional Conference, NCC.

- **Promote Public disclosure of information** – the loan contract must be available to the public (e.g. transmitted to parliament, available for consultation on request, published on the web, announced in the national press, radio and/or television as appropriate). Currently, it is almost impossible to access debt information from Ministry of Finance even though it is public information. Government should therefore move towards full information disclosure on public debt to make monitoring by stakeholders much easier. Government makes debt contraction public usually at the point of signing contract with the lender country/ institution.
- **Clarify Purpose of the Loan** - The Government should use debt resources to invest in projects with significant social and economic impacts. This can only be achieved if Government can appraise projects before they are implemented. Government should desist from borrowing money for unknown projects. Even though the current government has promised to depart from this trend (2012 budget speech, Page 5, Paragraph 36; we have already seen government borrowing from China US\$10 million in the name of fighting poverty for projects yet to be agreed upon.
- **Grants against Loans** - Government should go for grants instead of loans and put a stop to contracting new commercial loans and guaranteeing private loans. There should be a publicly determined ceiling for the amount for which the government of Zambia can publicly guarantee external debt for private investments. In the meantime, Government should desist from contracting foreign loans without a clear exit strategy and without the consent of Parliament.
- **Enhance Government Fiscal Policy** (i.e. its macro-economic policy, tax policies and spending priorities) - Government's fiscal policy remains a very important tool in debt sustainability management. A stable macroeconomic environment will guarantee continued economic growth that will generate sufficient tax revenue and ultimately reduce on borrowing. Additionally, government needs effective tax system that will capture more tax revenue and thereby reduce external financing component of the budget. Government should complement these measures with effective spending where resources will be directed to priorities areas and avoid wastage. Previously, the Auditor's Generals reports have highlighted significant abuse of public resources by Government which has lead to poor execution of budgets in the country but little had been done to redress the situation.

- **Enhance Loan Project Monitoring and Evaluation-** It is very cardinal that government enhances monitoring and evaluation of loan projects to ensure project objectives and targets are met by way of identifying problem areas during implementation and thus put up corrective measures to keep the project on course and thus focus on impact rather than just outputs and outcomes.

It is the hope of JCTR that both debt and fiscal policies will be used soon to address the danger of another debt crisis. All the past budgets since 2006 have acknowledged the urgency of enhancing debt legal framework but it has remained a pipedream. Ministry of Finance should therefore quickly provide a time frame under which this will be undertaken. Since the current Minister of Finance has also showed willingness to implement debt legal reforms, there is need for Parliament to request a specific timeframe in which this process will be concluded. Both external and domestic debts have continued on the stead increase and if left unchecked may result in unsustainable levels.