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July 1, 1992

To: Members of the Executive Board

From: The Acting Secretary

Subject: Zambia - Staff Report for the 1992 Article IV Consultation and Request for Accumulation of Rights

Attached for consideration by the Executive Directors is the staff report for the 1992 Article IV consultation with Zambia and its request for a rights accumulation program, which is tentatively scheduled for discussion on Friday, July 17, 1992. Draft decisions appear on pages 32 and 33.

Ms. Dillon (ext. 38313) or Mr. Katz (ext. 37465) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

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ZAMBIA

Staff Report for the 1992 Article IV Consultation and Request for Accumulation of Rights

Prepared by the African Department and
the Policy Development and Review Department

(In consultation with the Fiscal Affairs,
Legal, and Treasurer's Departments)

Approved by E.L. Bornemann and Thomas Leddy

July 1, 1992

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I. Introduction and Background

Discussions relating to the 1992 Article IV consultation and a new rights accumulation program (RAP) were held in Lusaka between February and June 1992. 1/ The staff met with the Minister of Finance, Honorable E. Kasonde; the outgoing Governor of the Bank of Zambia, Mr. J. Bussières, and the new Governor, Mr. D. Mulaisho; and other senior officials and representatives of the private sector.

The last Article IV consultation with Zambia was concluded by the Executive Board on April 17, 1991, when it also endorsed Zambia's economic program and approved the accumulation of rights for Zambia. Welcoming the Government's determination to bring the reform effort back on track, Directors underscored the importance of strict adherence to the fiscal targets if the program's monetary and inflation objectives were to be met. Directors urged the Government to achieve positive real interest rates at an early stage. While expressing satisfaction with the progress in reforming the exchange and trade system, Directors indicated their strong concern regarding the postponement of taxation of housing allowances and emphasized the need to broaden the tax base. Directors called on the Government to move rapidly and decisively to increase private sector participation in the economy.

On October 31, 1991, Zambia held its first multiparty democratic elections in more than 20 years and a new government headed by President F.J.T. Chiluba assumed office. The macroeconomic situation that the new Government had inherited was very difficult. In early 1992, understandings were reached on a shadow program through the first half of the year to be monitored informally by the Fund staff (EBS/92/49; 3/3/92). In March 1992, a revised policy framework paper (PFP) for 1992-94 that had been prepared by the new Government was discussed by the Executive Boards of the World Bank and of the Fund (EBD/92/32; 2/27/92). Shortly thereafter, it became evident that a devastating drought had hit Zambia and all of southern Africa.

In a letter to the Managing Director dated June 26, 1992, (Appendix I) the Minister of Finance has requested that the Fund: (i) endorse Zambia's program, agree to monitor it during the period ending March 31, 1995, and approve the accumulation of rights during that period, in accordance with the guidelines on Operational Modalities of the Rights Approach, and (ii) cancel the previous decision on rights accumulation (EBS/91/59; 4/3/91). The rights accumulation on the basis of the new monitored program would be for a maximum amount of SDR 836.9 million, or 309.6 percent of quota, (i.e., the July 1990 level of arrears to the Fund, which would be the same amount as under the decision on rights accumulation approved in April 1991), of

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1/ Details regarding the dates of these contacts and the staff members are contained in Appendix III. This report was prepared by a staff team comprising Ms. Dillon (head-AFR), Messrs. Nowak (AFR), Katz (AFR), Brown (ETR), McCarten (FAD), and Gordon (AFR).

which SDR 251.1 million (92.9 percent of quota) could be accumulated on the basis of program performance during 1992 (Table 1).

Zambia was declared ineligible to use the general resources of the Fund on September 30, 1987. The Fund has since reviewed the matter of Zambia's overdue obligations to the Fund on a number of occasions, the most recent being February 19, 1992. At that time, Directors welcomed the adoption by Zambia of a macroeconomic program for 1992. Noting the recent payments by Zambia and acquisitions of SDRs to meet forthcoming obligations to the Fund, Directors stressed that the full and prompt settlement of Zambia's arrears to the Fund should be given the highest priority. Zambia has met all obligations falling due to the Fund so far this year, and as of June 30, 1992, its arrears to the Fund were SDR 920.7 million. Zambia intends to reduce its arrears to the Fund by SDR 22 million during the second half of 1992 and by a further SDR 62 million during 1993 to reach the July 1, 1990 level. To facilitate timely payments of both arrears and amounts currently falling due, Zambia will acquire SDRs in advance of established payment dates. On June 30, 1992 Zambia's outstanding use of Fund resources stood at SDR 632.8 million (234.1 percent of quota) from the General Resources Account (GRA) and SDR 6.7 million under the Trust Fund.

The staffs of the Fund and the World Bank worked closely together during the preparation of the PFP and the rights program. Zambia eliminated arrears to the World Bank on January 31, 1992, and has met its obligations to the Bank since that time. Bank disbursements under its Economic Recovery Credit totaled US$90 million during the first half of 1992. Bank staff recently concluded negotiations for Zambia's Privatization and Industrial Reform Credit totaling US$200 million, which was approved by the Bank's Board on June 30, 1992; the first two tranches of US$100 million and US$50 million would be disbursed during 1992.

Zambia still avails itself of the transitional arrangements of Article XIV.

Long-term balance of payments scenarios are presented in Appendix II; Appendices III and IV provide summaries of Zambia's relations with the Fund and the World Bank Group, respectively; and basic economic and financial data and social and demographic indicators are presented in Appendices V and VI, respectively.

Table 1. Zambia: Schedule of Rights Accumulation, 1991-95

Amount (Cumulative)	Availability date	Conditions necessary for accumulation
SDR 83.69 million (SDR 83.69 million)	On Board approval of decision on the accumulation of rights.	
SDR 83.69 million (SDR 167.38 million)	November 15, 1992	Observance of performance criteria for September 30, 1992 and completion of the program review.
SDR 83.69 million (SDR 251.07 million)	February 15, 1993	Observance of performance criteria for December 31, 1992
SDR 334.76 million (SDR 585.83 million)	1993/94	Observance of performance criteria and completion of applicable reviews.
SDR 251.07 million (SDR 836.90 million)	1994/95	(Same as above)

II. Performance Under the 1991 Program and Developments in Early 1992

1. Performance under the 1991 program

Overall economic performance under the 1991 program was poor and Zambia failed to accumulate any rights. 1/ Policies went substantially off track in the second half of the year under the previous Government, especially in the run-up to the election. While some progress was made in the implementation of structural reform measures, particularly in the exchange and trade area, substantial slippages occurred on the macroeconomic stabilization front. Real GDP is estimated to have declined by 2 percent, mainly reflecting a sharp fall in copper and manufacturing output (Table 2). 2/ Inflation declined to an annual rate of 46 percent in the third quarter of 1991, but then picked up sharply again to reach 111 percent for the year as a whole, compared with a program target of 40 percent.

Fueled by a highly expansionary fiscal stance, broad money also rose by nearly 100 percent. The overall budget deficit (accrual basis, including grants) swelled to 7.1 percent of GDP, compared with the program target of 4.0 percent of GDP, with the primary deficit (cash basis, excluding grants) increasing to 7.9 percent of GDP (as against 0.7 percent of GDP under the program). Major weaknesses were evident in both the tax and expenditure areas. The decision to tax cash allowances and fringe benefits was withdrawn for a second time, and mining income tax payments fell short of projections. Mealie meal subsidies rose sharply when consumer prices were not adjusted after a tripling of producer prices, and substantial budgetary funds had to be lent to the agricultural cooperatives to purchase maize. Finally, large pay awards were granted to the public sector. Under the circumstances, efforts to contain liquidity growth through the introduction of a new liquid assets requirement had a very limited effect.

The external current account (excluding official transfers and interest obligations) recorded a deficit of US$93 million (2.5 percent of GDP), slightly below the program target of US$101 million, largely because of a compression of imports in the second half of the year when most donor support was suspended. With favorable copper prices, copper export revenues were US$25 million above the programmed level, but these were more than offset by a 26 percent decline from 1990 in the surrender of foreign exchange earnings from nontraditional exports, apparently in anticipation of exchange rate movements. Gross foreign reserves declined slightly in 1991, with uncommitted reserves virtually exhausted; at end-1991, Zambia's arrears

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1/ A description of developments in 1991 is presented in an appendix to "Zambia - Economic and Financial Policy Framework, 1992-94" (EBD/92/32).

2/ As noted in the PFP, technical assistance is being sought on both national income accounts and the consumer price indices. Neither series is considered to be a very reliable indicator of developments and both are subject to substantial revisions on a continuous basis.

Table 2. Zambia: Selected Economic and Financial Indicators, 1986-94

	1986	1987	1988	1989	1990	1991	1992 PFP	1992 Revised program	1993 Revised program	1994 Revised program
	(Annual percentage changes, unless otherwise indicated)									
National income and prices										
GDP 1/	0.7	2.7	6.3	-1.0	-0.5	-1.8	2.0	-9.0	13.2	4.0
GDP deflator	82.0	48.6	46.4	118.4	113.3	97.3	76.4	141.3	26.2	5.3
Consumer prices										
Period average	54.8	47.1	54.0	128.3	109.6	93.4	81.6	152.7	25.0	8.0
End-period	34.6	50.4	64.1	158.0	105.0	111.0	45.0	101.1	15.0	5.0
Copper prices 2/	0.63	0.74	1.16	1.33	1.21	1.06	0.90	0.93	0.94	0.90
External sector (in SDRs)										
Exports, f.o.b.	-30.6	12.7	28.1	27.7	-15.2	-14.9	-24.1	-9.4	5.2	0.6
Of which: copper	(-26.7)	(16.3)	(28.4)	(31.4)	(-19.1)	(-15.7)	(-9.3)	(-21.2)	(4.8)	(-2.3)
Imports, c.i.f.	-29.3	2.8	10.7	20.5	0.3	-12.9	10.7	24.8	-10.9	4.6
Real effective exchange rate (depreciation, -)	-51.8	5.4	55.6	32.3	-7.5	0.7	...	...	...	...
Gross reserves (weeks of nonmaize imports)	5.2	5.2	8.1	8.5	8.1	8.8	9.8	10.0	11.4	11.9
Government budget										
Revenue and grants	103.0	36.3	28.7	105.0	142.1	108.0	94.3	202.1	37.9	-2.7
Expenditure and net lending	165.6	-5.6	43.6	90.3	115.9	102.8	47.8	93.4	28.2	6.8
Money and credit										
Broad money	93.1	54.3	61.6	65.3	45.8	98.1	25.0	35.0	10.0	5.0
Domestic credit 3/	64.9	22.2	47.2	56.4	27.0	146.7	15.3	31.4	...	...
Interest rate (bank lending rate: end of year)	33.5	18.4	25.0	35.0	40.0	46.0	...	...	...	...
	(As a percentage of GDP, unless otherwise indicated)									
Gross domestic savings	22.6	18.0	18.7	14.4	14.7	12.0	12.6	-1.2	10.2	11.3
Gross national savings 4/	3.3	6.1	6.6	7.6	12.3	13.5	18.2	6.2	13.9	12.5
Gross domestic investment	23.8	13.9	11.4	9.9	15.4	13.5	19.5	14.5	18.5	19.0
Consumption	77.4	82.0	81.3	85.6	85.3	88.0	87.4	101.2	89.8	88.7
Government budget										
Revenue and grants	24.7	22.1	18.7	19.2	21.9	23.5	25.7	32.4	31.3	27.8
Foreign interest	12.9	5.5	3.8	3.4	5.7	5.7	4.8	5.3	5.2	4.9
Other expenditures and net lending	38.8	26.5	26.5	25.4	23.6	25.0	20.6	21.7	19.1	18.7
Balance										
Overall (accrual basis)	-26.9	-9.9	-11.5	-9.6	-7.4	-7.1	0.3	5.4	7.0	4.1
Excluding grants and interest (cash basis)	-14.1	-2.1	-7.3	-6.5	-4.1	-7.9	-1.9	-2.6	--	0.5
External current account										
Overall balance	-20.5	-7.8	-4.8	-2.3	-3.1	--	-1.3	-8.3	-4.6	-6.5
Balance excluding official transfers and interest	-3.7	3.2	6.6	4.4	-1.1	-2.5	-7.8	-16.9	-9.4	-8.6
External debt service 5/	111.1	101.5	80.9	58.0	59.2	67.9	66.2	61.0	56.5	54.8

Sources: Data provided by the Zambian authorities; and staff estimates.

1/ At constant 1977 prices.
2/ Average export prices. c.i.f., in U.S. dollars per pound.
3/ Change as a percent of beginning of period money.
4/ Including unrequited transfers.
5/ Scheduled payments, as a percent of receipts from exports of goods and nonfinancial services.

to the Fund exceeded program levels by SDR 85 million, new arrears to the World Bank had reached US$40 million, and new arrears had also arisen to other multilateral creditors (about US$70 million) and to Paris Club creditors (about US$30 million).

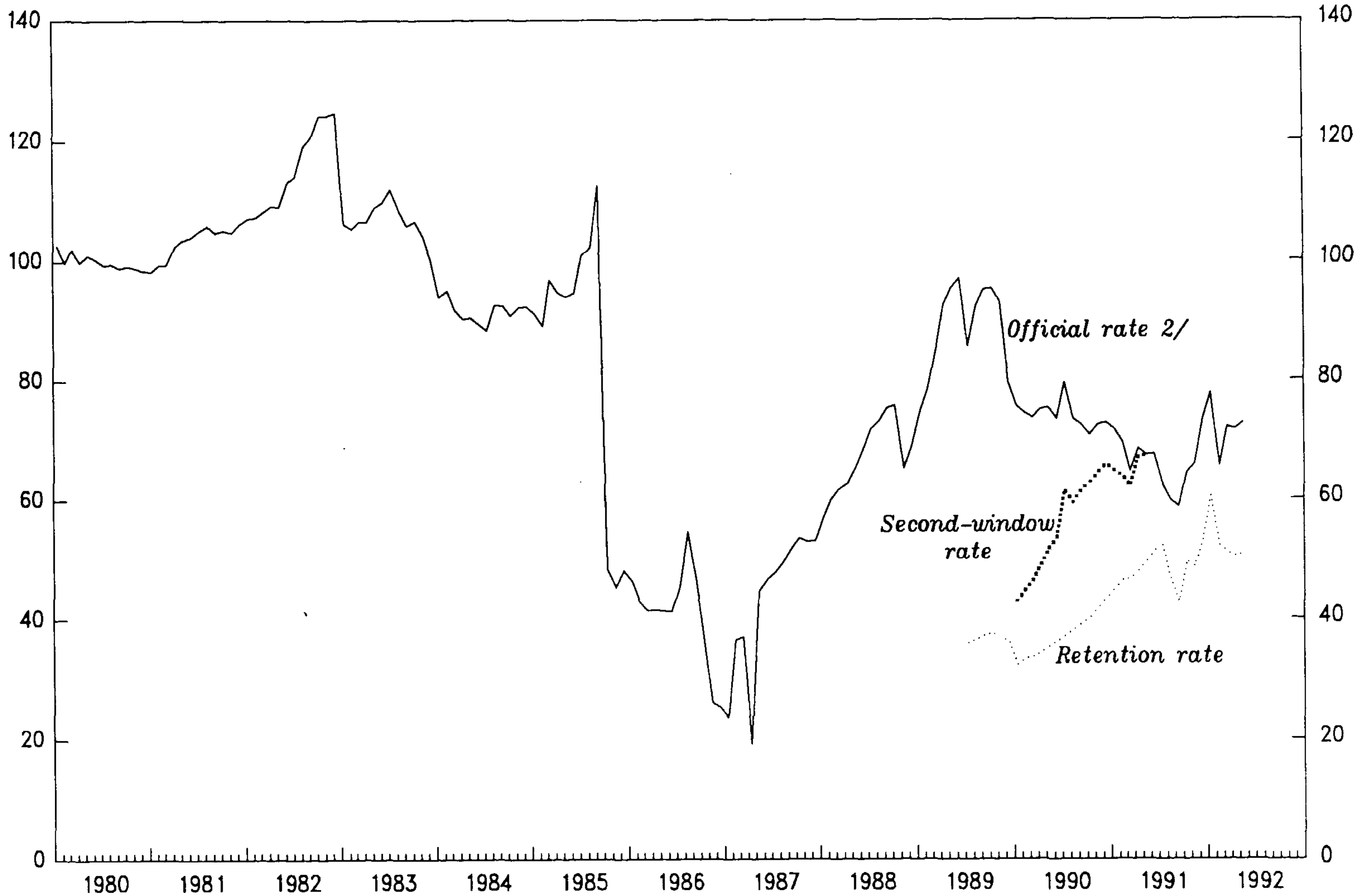
In contrast to the record in most policy areas, progress continued in the liberalization of the exchange and trade system. The open general license (OGL) system was expanded; the first and second window exchange rates were unified well ahead of schedule; and the number of controlled or prohibited exports was reduced from 48 to 4. Throughout most of 1991, adjustments in the official exchange rate were sufficient to generate a gradual depreciation in real effective terms; however, these much-needed gains in international competitiveness were eroded toward the end of the year, as inflation accelerated (Chart 1).

2. <u>Developments in early 1992</u>

The new Government has moved quickly to implement its economic program. In its first seven months in office the Government has put in place a number of fundamental and politically difficult policy reforms aimed at restoring macroeconomic stability and transforming Zambia into a market economy. In a move to cut subsidies, maize meal prices were increased by more than 100 percent in December 1991; this and subsequent adjustments in the first half of 1992 have resulted in a fivefold increase in the consumer price of maize meal. In early January 1992, domestic prices for petroleum products, which had been frozen since late 1990, were raised to cover costs plus excise duty. The 1992 budget, introduced on January 31, 1992, aimed at largely reversing the fiscal slippages of 1991; the overall deficit (accrual basis, including grants) was to be reduced from 7.1 percent of GDP to a surplus of 0.3 percent in 1991, with the primary deficit (cash basis, excluding grants) to be cut by 6 percentage points to less than 2 percent of GDP. The overall deficit would imply no need for recourse to inflationary borrowing from the domestic banking system. Key budgetary actions included the following: (i) a reduction in maize- and fertilizer-related expenditure from 6.0 percent of GDP in 1991 to 2.7 percent of GDP in 1992 as the result of action on maize meal pricing, the elimination of fertilizer subsidies, and a reduced need to finance cooperatives, because of increased agricultural liberalization; and (ii) a fundamental reform of the personal income tax, including bringing cash allowances and fringe benefits fully within the tax net while cutting tax rates--the top marginal tax rate was lowered from 50 percent to 35 percent, and the former personal allowance was replaced by a tax credit sufficient to remove a large number of low-income taxpayers from the tax roll.

In the monetary area, the maximum commercial bank lending rate was increased in February to an annual effective rate of 70 percent, consistent with the objective of achieving positive real interest rates under the inflation profile then projected for the first quarter of 1992. As for external sector policies, the official exchange rate was devalued by 30 percent on February 1, and was subsequently adjusted at weekly intervals

CHART 1
ZAMBIA
REAL EFFECTIVE EXCHANGE RATE INDICES [1], JANUARY 1980 - MAY 1992
(Period average, 1980=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.

beginning in early March. In mid-March the Government increased from 50 percent to 100 percent the share of foreign exchange earnings from exports of goods and services that exporters (other than the copper company) may retain for their own use or sell in the export retention market at a freely determined exchange rate. At the same time, the Bank of Zambia ceased to provide official foreign exchange for a range of transactions, primarily services, and shifted them to the retention market. In the weeks following this change the exchange rate in the retention market depreciated rapidly and the spread between the official and the retention rates widened from 20 percent to 30 percent, at which level it remained as of mid-June.

The informal benchmarks for end-March on net bank claims on Government, external arrears, short-term debt, and external borrowing were all met (Table 3). 1/ The satisfactory fiscal performance in the first quarter contributed to a marked deceleration in the growth of liquidity. The benchmark on reserve money and the target for broad money were missed by a small margin (1 percent) because of a short delay into early April of first quarter tax payments by the copper company (ZCCM). M2 rose by 14 percent in the first quarter of 1992 (seasonally adjusted), compared with a 33 percent increase in the final quarter of 1991 (72 percent and 214 percent, respectively, on an annual basis). Net international reserves fell short of the benchmark by SDR 5 million, as a result of a larger-than-anticipated net reduction of short-term trade credit lines intermediated through the Bank of Zambia (which are not included as an external liability in the program definition of net international reserves).

While money and credit developments were broadly on track, the consumer price index rose by 50 percent in the first quarter (an average monthly rate of about 15 percent). This adverse development reflected the confluence of the inflationary momentum carried over from late 1991, as well as the direct and apparently very strong announcement effects of the administered and parastatal price adjustments and the February 1 devaluation, all of which were validated by the substantial liquidity overhang created in late 1991.

Difficulties were encountered in the implementation of financial policies in the second quarter of 1992. Partial information indicates that fiscal performance slipped significantly, primarily as a result of a very sizable increase in wages. Effective April 1, a pay award that resulted in an increase of 130 percent in the wage bill was granted to the civil service. The program had been based on an increase in civil service pay and benefits of 50 percent as from July 1. This increase is expected to raise the wage bill to K 7 billion (1.3 percent of GDP) more than the PFP level, although the net increase is estimated at K 5 billion, in view of the broader tax base following the income tax reform. Accordingly, the Government is estimated to require net recourse to the domestic banking

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1/ A description of the quantitative and structural benchmarks for the first half of 1992 appears in EBS/92/49 (3/13/92).

Table 3. Zambia: Quantitative Benchmarks Under Informal Program, First Half 1992

	1991	1992		
	Dec.	March		June
		Prog.	Act.	Prog.
		(In millions of kwacha)		
Reserve money 1/	21,962	22,768	22,899	23,771
Net claims on Government by banking system 1/ 2/				
Unadjusted	30,938	27,760	...	28,293
Adjusted	...	27,274	25,944	...
Debt swaps 1/ 3/	...	330	307	1,000
Net reduction in domestic arrears of Government 3/ 4/	...	500	492	1,000
		(In millions of SDRs)		
Net international reserves 4/ 5/				
Unadjusted	-811.2	-799.5	...	-799.5
Adjusted	...	-800.1	-804.9	-799.0
New external loan commitments 1/ 6/		142.9	--	142.9
1- to 5-year subceiling	...	71.4	--	71.4
Stock of short-term debt 1/ 7/				
Unadjusted	278.5	319.8	...	319.8
Adjusted	274.7	315.9	238.6	315.9
Minimum reduction in external payments arrears 8/ 9/	1,027.5	30.9	30.9	34.7
Minimum reduction in arrears to IMF 8/	921.8	--	--	--

1/ Ceiling. The indicative limit on debt swaps and the external loan commitment ceilings are cumulative from January 1, 1992.

2/ Limits adjusted downward (a) if, and to the extent that, net nonproject external financing to the budget exceeds the amounts envisaged in the program, i.e. K 4,558 million through end-March 1992 and K 5,955 million through end-June 1992; (b) by the amount that total nonbank holdings of government debt exceeds the level at end-December 1991; (c) by the amount of any receipts from the mineral resource levy and company income tax payments from ZCCM in excess of K 500 million through end-March 1992 or K 1,000 million through end-June 1992, up to the amount through the corresponding date of any cumulative excess copper earnings (ECE) that have not been sterilized by other means; and (d) by the amount of any proceeds received from the sale of parastatals.

3/ Indicative targets only.

4/ Floor.

5/ Net international reserves are defined as gross reserves minus outstanding Fund credit (including Trust Fund loans) and Fund charges in arrears. Floor is adjustable upward, as provided for under the copper contingency mechanism. The floor is adjustable downward by the amount of any cash payments by the Bank of Zambia for emergency maize imports during January-March 1992, up to a maximum of US$10 million.

6/ Commitments on external loans (other than debt rescheduling) with an original maturity of more than one year contracted or guaranteed by the Government, Bank of Zambia, and parastatals, except borrowing on concessional terms according to the DAC definition and borrowing from multilateral institutions. This ceiling, and the subceiling for debt with a maturity of 1-5 years, is increased and the ceiling on short-term debt decreased to the extent that the Bank of Zambia is able to refinance its existing short-term liabilities as medium-term liabilities.

7/ Disbursed debt of Government, Bank of Zambia, and parastatals, excluding normal trade credit for imports and interest arrears. See also adjustment described in Footnote 6.

8/ Data for December 1991 are stocks. Targets for March and June 1992 are cumulative reductions from January 1, 1992.

9/ Excludes overdue payments to bilateral or commercial creditors that may arise pending consideration of requests for rescheduling of these payments.

system of K 6 billion in the second quarter, after a net repayment of K 5 billion in the first quarter. Monetary policy management was further complicated in the second quarter by strong foreign exchange earnings of the copper company (ZCCM), as not only copper prices but also production were higher than expected. 1/ Consequently, it is anticipated that the end-June numbers will show reserve money and broad money at or near the PFP targets for end-December. Inflation decelerated to about 6 percent a month in April and May.

The authorities began preparations and payments for emergency maize imports in late March in order to ensure that adequate supplies would begin to arrive by late June, when domestic inventories were projected to be exhausted. By mid-June, cash payments totaling about US$40 million had been made to open letters of credit and pay shipping costs on the earliest orders. It is anticipated that these costs will be covered retroactively by donor disbursements.

During the second quarter of 1992 the authorities continued the policy of frequent small devaluations of the official exchange rate, increasing the pace of devaluation in June. In real effective terms the official exchange rate remained at roughly its end-1991 level through May, and has since begun to depreciate gradually. On June 19, a number of steps were taken to liberalize quantitative limits and administrative requirements on transactions in the retention market, including eliminating the requirement of prior Bank of Zambia approval of the provision of foreign exchange for small transactions and for business travel, and permitting nongovernmental organizations and foreign investors to sell the foreign exchange they bring into the country in the retention market.

1/ Under the contingency mechanism described in Section IV.1, the international reserve target is adjustable upward if actual copper prices exceed program projections. In order to ensure that the program's monetary objectives are met, the kwacha counterpart of such excess copper earnings has to be sterilized, either through the budget or directly through the placement of copper company receipts at the Bank of Zambia. To that end, the program provides that the ceiling on net bank credit to the Government is adjustable downward for any budgetary receipts from the mineral resource levy or of company tax payments by ZCCM in excess of K 500 million per quarter in the first half of 1992 and K 800 million per quarter in the second half, up to the amount of excess copper earnings not sterilized by the Bank of Zambia. In both the tables and text, company tax receipts from ZCCM are assumed to be at the baseline amounts. In the first five months of 1992 actual receipts of company tax from ZCCM were K 3.8 billion above the baseline amounts and actual borrowing from the banking system was less by that amount.

III. Rights Accumulation Program and Policies for the Second Half of 1992

The economic program of the new Zambian Government involves prompt action to address slippages in macroeconomic policies that took place during 1991 and to accelerate structural reforms. The objectives and targets for 1993-94 for growth, inflation, and monetary and fiscal policies remain essentially those described in the PFP for 1992-94 which, in turn, entailed a return to the policy stance set out in the rights program endorsed by the Executive Board in April 1991. Thus, for 1993 the proposed new rights program continues to target a balanced primary fiscal position (excluding grants), a reduction in the banking system's claims on the Government, money supply growth of 10 percent, and the maintenance of international competitiveness, as under the 1991 rights program. Although growth and inflation objectives are fully restored by 1994, external prospects for the immediate future are now weaker than envisaged earlier, even after allowance for the direct impact of the drought; this weakening is attributable mainly to a decline in copper export volume, lower projected world copper prices, and slower expansion of nontraditional exports in 1991-92 (owing to policy slippages in 1991 and the drought). Over the somewhat longer term, as described in Section V, the external outlook appears essentially the same as envisaged a year ago--achieving external viability will require further sustained and substantial adjustment efforts by Zambia and extraordinary support from the international financial community.

The immediate tasks facing the Government are to manage the drought relief effort and to bring about a rapid deceleration of inflation. In view of the effects of the drought and developments in the first half of 1992, several macroeconomic policies and targets for 1992 have been revised since the preparation of the PFP for 1992-94. Real GDP is now projected to drop by 9 percent in 1992, compared with an earlier projection of an increase of 2 percent. A return to normal crop conditions in 1993 should reverse the real decline being experienced in 1992. Although the profile of inflation in the second half of the year is targeted to be the same as in the original program (30 percent on an annual basis), for the year as a whole inflation is likely to again reach 100 percent, considering price developments in early 1992. Due to the expected impact of the drought on import requirements and export earnings, estimated at US$270 million, the external current account deficit (excluding interest payments and official transfers) is projected to widen to US$550 million, or 16.9 percent of GDP. In view of the minimal level of usable reserves, the targeted increase in gross international reserves has been kept at US$35 million.

To meet these objectives, the program will seek to bring money supply growth in the second half of 1992 fully back to the profiles targeted in the original program. To this end and to permit adequate bank credit to the private sector, fiscal policy will aim at a substantial net repayment of government debt to the banking system, compared with the original program target of zero net borrowing. To facilitate the transformation of the economy, the Government is proceeding with the liberalization of the exchange and trade system and of maize and fertilizer marketing and, assisted by the World Bank and donors, has embarked on structural reform initiatives in the parastatal sector and the civil service, and on an expanded social action program.

1. Fiscal policy

For 1992, the PFP targeted a reduction in the Government's primary deficit (cash basis, excluding grants) to 1.9 percent of GDP, down from 7.9 percent in 1991 (Table 4), and zero use of inflationary domestic bank financing. The revised program aims at a net reduction of K 10 billion (2 percent of GDP) in the Government's indebtedness to the banking system, a performance criterion under the program. This will permit the availability of bank credit to the nongovernment sectors to be maintained in real terms, taking into account the higher-than-anticipated level of prices now prevailing in the economy.

As noted above, as a result of the government wage increase and other developments, fiscal performance slipped significantly in the second quarter. In addition, various unprogrammed expenditures related to the drought will be necessary in the third and fourth quarters. While the Government is taking action to both increase revenues and contain expenditures over the remainder of the year, for the year as a whole the primary deficit (excluding grants) is expected to be 2.6 percent of GDP, or 0.7 percent of GDP higher than anticipated in the original program. Nevertheless, in comparison with 1991, the revised primary deficit target still represents an improvement of more than 5 percent of GDP. Despite the drought, the main factor contributing to the better overall budgetary result is reduced expenditure relating to maize and fertilizer, reflecting the Government's actions to raise prices and cut subsidies. Given an upward revision to projected external financing of over 2.5 percent of GDP, primarily as the result of expected grant receipts from donor-financed maize, the revised deficit target is sufficient to permit the desired net repayment to the banking system and scope for adequate growth in credit to the nongovernment sector.

a. The 1992 budget

On the revenue side, in addition to the far-reaching reform of the personal income tax system described earlier, the 1992 budget introduced important changes to the company income and sales taxes. Effective April 1, the company income tax base was broadened by disallowing as deductible expenses noncash fringe benefits provided to employees, and the company income tax rate was reduced from 45 percent to 40 percent. Effective with the presentation of the budget, the domestic and import sales tax systems were harmonized at a common rate of 20 percent; this was intended both to raise revenues and to set the stage for the later introduction of a value added tax (VAT). Nontax revenues were also programmed to increase sharply in 1992, reflecting a more aggressive stance regarding the payment of dividends by parastatals and the charging of user fees by the Government.

Table 4. Zambia: Central Government Operations, 1986-92

(In percent of GDP)

	1986	1987	1988	1989	1990	1991	1992 PFP	1992 Revised
Revenue and grants	24.7	22.1	18.7	19.2	21.9	23.5	25.7	32.4
Tax revenue	21.2	19.7	15.5	16.4	17.7	16.2	16.3	17.2
Mineral sector 1/	3.1	2.4	1.8	2.7	2.8	1.4	0.5	0.5
Import taxes	6.9	7.6	5.2	5.6	6.5	5.4	5.9	5.9
Domestic goods and services	4.6	4.0	3.7	4.0	4.3	5.0	5.4	5.2
Income taxes (nonmining)	6.5	5.7	4.9	4.1	4.2	4.5	4.5	5.6
Nontax revenue	2.2	1.9	1.6	0.7	0.3	0.3	1.2	0.7
Exceptional revenue	--	--	--	--	--	0.3	--	--
Grants	1.3	0.5	1.6	2.1	3.9	6.7	8.2	14.4
Expenditure and net lending	51.7	32.0	30.3	28.8	29.3	30.7	25.4	27.0
Current expenditure	40.1	28.6	25.2	21.1	22.9	23.0	20.5	21.5
Personal emoluments	5.1	5.1	3.8	3.1	3.5	4.2	4.2	4.7
Severance pay	--	--	--	--	--	--	0.4	0.3
Recurrent departmental charges	4.4	5.5	4.7	4.2	3.7	3.3	3.5	3.9
Subsidies 2/	4.4	3.4	4.7	3.1	3.2	3.5	1.7	1.4
Interest: domestic 3/	3.6	2.2	2.0	1.7	1.2	1.5	1.7	1.4
Interest: foreign	12.9	5.5	3.8	3.4	5.7	5.7	4.8	5.3
Transfers and pensions	3.1	2.1	2.0	1.8	2.3	2.5	1.9	2.0
Other	6.7	4.8	4.2	3.9	3.3	2.3	2.4	2.4
Capital expenditure and net lending 4/	7.5	3.3	4.5	4.7	5.5	4.8	3.9	4.0
Net agricultural lending 5/	--	--	--	--	--	2.5	1.0	0.5
Exceptional expenditure 2/	4.1	0.1	0.5	3.0	0.9	0.4	--	1.0
Overall balance (accrual basis)	-26.9	-9.9	-11.5	-9.6	-7.4	-7.1	0.3	5.4
Change in domestic arrears	-2.3	0.6	--	0.1	0.2	-1.3	-0.4	-0.4
External interest arrears (increase +)	4.0	4.3	2.9	2.6	-12.3	-2.5	-2.6	-2.5
Debt relief: interest 6/	6.3	--	--	--	16.7	3.8	1.0	-0.8
Overall balance after interest relief and arrears (cash basis)	-19.0	-5.0	-8.7	-6.9	-2.8	-7.2	-1.7	1.7
Financing	19.0	5.0	8.7	6.9	2.8	7.2	1.7	-1.7
External (net)	10.1	-0.3	4.1	1.0	1.3	1.9	1.5	0.2
Domestic (net)	8.9	5.2	4.6	5.9	1.5	5.2	0.2	-1.9
Banking system	5.0	0.8	4.3	5.7	2.1	5.0	0.2	-1.9
Other	3.9	4.4	0.3	0.3	-0.6	0.2	--	--
Memorandum items:								
Primary balance excluding grants (cash)	-14.1	-2.1	-7.3	-6.5	-4.1	-7.9	-1.9	-2.6
Primary balance excluding grants, maize, fertilizer, and drought-related expenditure (cash)	-9.7	1.4	-2.7	-3.4	-0.9	-2.2	0.8	-0.1

Sources: Data provided by the Zambian authorities; and staff estimates.

1/ Excludes excess copper earnings sterilized through budget.
2/ Includes drought-related expenditures in 1992.
3/ Excludes interest paid to Bank of Zambia.
4/ Includes only nonagricultural net lending.
5/ Includes transactions relating to financing of 1991/92 imports.
6/ Assumes that US$64 million in moratorium interest deferred in 1991 is paid in 1992.

While these measures were expected to increase revenues by the equivalent of one percent of GDP in 1992, mining taxes were expected to fall by about the same amount; hence, the targeted reduction in the deficit was to occur on the expenditure side, and in particular with regard to outlays relating to maize and fertilizer. As part of the medium-term objective of eliminating subsidies altogether, the program called for maize and fertilizer subsidies to be cut in half in 1992, while net agricultural lending coming from the budget was to decline in line with the private sector's increased role in maize and fertilizer handling. Also, the largest local councils were to become financially independent, with no transfers being provided after midyear. Given these measures, in conjunction with a programmed reduction in capital expenditure, the PFP targeted an overall decline in noninterest expenditure of about 4.5 percent of GDP.

b. Recent developments and revised projections

Developments in 1992 to date have led to a slight upward revision to projected revenue. 1/ The main factor buoying revenues is a substantial increase relative to GDP in personal income tax collections. While one of the main purposes of the income tax reform was to improve the buoyancy of the tax system, the short-run revenue elasticity is exceptionally high; recent large wage awards throughout the economy have eroded what had been intended to be a generous tax credit and brought a significant number of workers back into the tax net at a bottom marginal rate of 25 percent. Also, in order to increase revenue collections in the second half of the year, the Government is reintroducing the sales tax on clear beer, soft drinks, and cigarettes; these excisable items were exempted from the domestic and import sales tax when the systems were unified with the 1992 budget. This measure is estimated to contribute at least one half a percent of GDP at an annual rate. On the other hand, projections of nontax revenues have been revised downward, reflecting the experience to date in actually collecting from the local level the higher fees and charges announced with the budget, and trade taxes are now projected to rise less rapidly than the kwacha value of imports, given poor collections in the first quarter and in view of duty exemptions on capital goods that have been granted recently under the new Investment Act.

On the expenditure side, the drought and its financing have resulted in substantial revisions to the fiscal program. Under the pricing strategy being adopted for both donor-financed imports and domestically produced maize (see Section III.4 below), the Government sets only into-mill prices; the previous system of controlling maize meal prices and providing direct subsidies to the mills to enable them to sell below cost has been ended. While the into-mill pricing strategy still entails subsidies--including on the domestic transport and handling of donor-provided maize--the total cost

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1/ Company tax receipts from ZCCM are projected at baseline amounts. See Footnote 1, page 9.

of subsidies is expected to be slightly below the PFP target. 1/ In addition, although the drought has necessitated a large budgetary provision (K 6.3 billion) for the financing of inputs for small-scale farmers, net agricultural lending is now projected to be half that originally programmed since little finance is required to purchase the small 1991/92 crop and such loans will be repaid fully within the current calendar year. As a result of these lower subsidy and net lending figures, total expenditure with regard to maize and fertilizer is now expected to be marginally below the original program, even after account is taken of various additional drought-related expenditures--such as the cost of upgrading roads and water supplies. 2/

A number of revisions have also been made to the PFP targets for core expenditures (i.e., noninterest expenditures excluding expenditures related to maize and fertilizer). The wage increase granted from April 1 has led to personal emoluments being revised upward to 4.7 percent of GDP (compared with 4.2 percent in the PFP). Recurrent departmental charges (RDCs, i.e., nonwage operating costs) have also been running ahead of program; to address this and establish more effective cash control, the Budget Office has now established monthly funding trajectories for the rest of the year, which will limit such expenditures to 3.9 percent of GDP in 1992. 3/ Finally, while unprofitable long-haul routes have been cut as planned, Zambia Airways has again had to seek budgetary support to meet its operating costs. More radical restructuring plans are now under consideration, but the airline is expected to require further support this year, resulting in total unprogrammed subventions equal to 0.3 percent of GDP. As a result of the combined effect of the above factors, total expenditures have now been revised upward by 1.2 percent of GDP, or 0.7 percent of GDP more than the upward revision to revenues; hence the primary deficit (cash basis, excluding grants) is now targeted at 2.6 percent of GDP rather than 1.9 percent in the PFP.

Further fiscal improvement over the medium term was called for in the PFP, with a primary surplus (excluding grants) of 0.5 percent of GDP to be achieved by 1994, at which time the Government would have begun to make net repayments to the banking system. In 1993, some unprogrammed

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1/ It should be noted that the fiscal discussion and fiscal tables value donor-financed maize and maize grants at the price at which the maize is sold to mills. If these transactions were valued instead at the c.i.f. cost of delivered maize in Lusaka, the difference between this cost and the sales price to mills would be reflected in the tables as another source of subsidy, financed entirely by additional donor assistance, amounting to about 3 percent of GDP.

2/ Total expenditure on maize and fertilizer excludes cash payments made by the Government for maize in advance of the receipt of donor support, since it is expected that such lags will unwind by the end of the year.

3/ A reporting system for expenditure control monitoring on a commitment basis was introduced on an experimental basis in 1991, but proved to be overly complex; the Budget Office is now trying to simplify the system.

drought-related expenditures will remain and, in comparison with a normal year, there will be less debt from the previous crop year to be repaid; nevertheless, these factors will be more than offset by the continuing receipt of counterpart funds from the sale of donated maize in the first half of the year. This augurs well for additional fiscal improvement in 1993 and the medium-term fiscal targets of the PFP have been retained.

2. Money and credit policies

Monetary policy will aim at a sharp reduction in the growth of the money supply in the second half of 1992 so as to bring about a rapid deceleration of inflation. The annualized rates of growth of M2 for the third and fourth quarters (seasonally adjusted) are targeted at 11 percent and 5 percent, respectively, consistent with maintaining the money supply growth in the second half as in the PFP. In view of monetary developments in the first half of 1992, the targeted growth rate of M2 for the year has been revised upward from 25 percent to 35 percent (Table 5). Given the program objective on net international reserves and the fiscal stance, this should allow bank credit to the nongovernment sector to be maintained in real terms.

To meet the targeted growth in the money supply, quarterly limits on reserve money have been established as a performance criterion under the program. Critical to meeting these limits will be a strict adherence to the fiscal program. Active use will also be made of available monetary policy instruments, which include changes in the liquid asset ratio requirement and adjustments in interest rates on government debt. In addition, deposits that two government ministries were holding with commercial banks (K 2 billion) have recently been transferred to the Bank of Zambia (BOZ), and all ministries are now required to hold their cash balances with the Central Bank. Understandings are being sought with ZCCM to hold a large part of its sizable and volatile cash resources in the form of treasury bills. Furthermore, the kwacha counterpart of additional ZCCM receipts that result from any excess of copper earnings will be sterilized directly at the Bank of Zambia or by the budget, as provided for under the contingency mechanism (see Footnote, page 9 above, and Section IV.1 below). Also, direct new lending by the BOZ to the parastatal sector--a prevalent practice in recent years--has ceased. Finally, reductions in Zambia's external commercial arrears through debt swaps have in the past been an important factor in undermining the effectiveness of monetary policy. Therefore, a limit equivalent to 6 percent of reserve money has been imposed on the amount of local currency created as a result of debt-swap arrangements (indicative target under the program); any debt-swap operations entered into effect after March 1, 1992, are to be undertaken at a market-related discount. These actions should enable the Central Bank to establish firmer control of the monetary aggregates.

In support of the effort to enhance the flow of savings to the banking system, the Government remains committed to achieving positive real rates of interest. To this end, the interest rate structure was increased on

Table 5. Zambia: Monetary Survey, 1991-92 1/

	1991	1992			
	Dec.	March	June	Sept.	Dec.
	Act.	Act.	Est.	Program	
	(In millions of kwacha)				
Net foreign assets	-4,182	683	1,948	5,939	9,739
Monetary authorities	-13,173	-8,797	-7,532	-4,753	-2,155
Commercial banks	8,991	9,480	9,480	10,693	11,895
Domestic credit	55,229	59,872	66,726	68,047	70,463
Net claims on Government 2/	30,938	33,058	39,266	36,332	27,699
Monetary authorities	(19,887)	(16,118)	(21,071)	(22,047)	(23,049
Commercial banks	(11,051)	(16,940)	(18,195)	(14,285)	(4,650
Claims on nongovernment sector	24,291	26,814	27,460	31,716	42,764
Other items (net)	2,596	8,833	10,653	12,829	14,792
Monetary authorities	-13,170	-17,492	-11,684	-9,509	-7,572
Revaluation account 3/	(-23,243)	(-23,562)	(-23,562)	(-23,562)	(-23,562
Other	(10,073)	(10,070)	(11,878)	(14,053)	(15,991
Commercial banks	17,265	23,471	23,484	23,484	23,510
Transit items	-1,499	-1,146	-1,146	-1,146	-1,146
Broad money (M2)	48,451	51,720	58,019	61,157	65,409
	(In percent)				
Memorandum items:					
M2 growth	98.7	74.4	90.0	77.4	35.0
Change in domestic credit 4/	146.7	122.5	118.4	80.3	31.4

Sources: Zambian authorities; and staff estimates.

1/ Program data exclude the revaluation effects of exchange rate changes on the stock of net foreign assets. These revaluation effects are included in the actual data.

2/ Flows differ from fiscal tables because of the inclusion of receipts from mineral resource levy and of parastatal counterpart deposits to external debt payments.

3/ Includes adjustment to net foreign assets.

4/ As a percentage of M2 at the beginning of the period.

June 15, 1992 by 2 percentage points, in addition to the 5 percentage point increase of February. The maximum bank lending rate, after compounding and including up-front fees, which are not covered by the ceiling, now amounts to 73 percent. Although below recent inflation rates, this effective lending rate is well above the targeted rate of inflation for the third quarter of 1992; should inflation turn out to be higher than targeted, the Government is prepared to raise the maximum bank lending rate further as necessary to ensure that by the completion of the 1992 program review that lending rate exceeds the annualized rate of inflation in the preceding three months. Moreover, the maximum bank lending rate will not be lowered as inflation comes down and interest rates will, thereby, become market determined. Over the medium term, the Government intends to develop a financial 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. This should allow for a substantial reduction in statutory reserve requirements which, in turn, would facilitate a narrowing of the differential between deposit and lending rates.

3. External policies

In view of Zambia's extremely heavy external debt-servicing burden and the expected longer-term downturn in copper production, the new Government regards the diversification of sources of foreign exchange earnings and increased efficiency in the utilization of those earnings, including reduced dependence on imports, as crucial to the adjustment effort. Policies that are expected to contribute to these objectives include further liberalization of exchange and trade policies; the establishment of a unified exchange system with a market-determined exchange rate; and, more generally, the creation of an environment conducive to domestic and foreign private investment in both mining and nontraditional export industries.

With the changes in the exchange system announced in March and June 1992, virtually all foreign exchange transactions other than imports under the OGL system and transactions of the Government, ZCCM, Zambia Airways, and the state oil company (ZIMOIL) have been moved into the retention market, where the exchange rate is freely determined. (However, the transactions remaining in the official market account for about 80 percent of total foreign exchange transactions.) The Government intends to move rapidly toward a unified exchange system, with all transactions at a market-determined rate, and further steps to liberalize the system are planned for the coming months. The Government will use the retention rate as the primary guide to movements in the official exchange rate during the remainder of this year, and will seek to narrow the spread between the official and retention rates, which stood at 30 percent in early June, to 20 percent by no later than September 1992. To help make rapid progress toward this goal, the rate of devaluation of the official exchange rate was raised from 1.75 percent per week to 2.0 percent per week on June 17, 1992.

The pace of the crawl will be adjusted as necessary to take into account movements in the retention rate and the balance between supply and demand in the OGL system.

To increase the transparency and automaticity of the OGL system, the Government will shift it from a positive to a negative list basis not later than September 1992. The OGL was widened in May 1992 to include fertilizer imports and the timing of further expansion of its coverage to include all import categories that can now make use of the retention market (i.e., from the current 90 percent to about 95 percent of base-period imports) will be determined in the context of the first program review.

The PFP describes the Government's general strategy for simplifying the trade system and moving toward lower and more uniform tariff rates. As a step in this process, in the context of the 1993 budget and drawing on a study of the tariff system that is now under preparation, the Government will further reduce the maximum tariff rate, which is currently 50 percent.

4. Maize and fertilizer policies

The achievement of the Government's objective of liberalizing both maize and fertilizer--which was spelled out in the PFP--has been complicated by the current drought. Whereas fertilizer prices were decontrolled on schedule in March 1992, the Government--through its management of the maize importation exercise--is inevitably the dominant player in the 1992 maize marketing season. In this drought year, the Government, as custodian of donor-financed yellow maize imports equal to approximately three fourths of consumption needs for the 12-month period beginning July 1, 1992, will provide free or heavily discounted maize to the most vulnerable sections of the population, but will set into-mill prices for the bulk of maize imports so as to phase in border pricing by the end of 1992.

Consistent with understandings reached with donors, some 1.7 million bags of imported yellow maize (out of total donor-financed imports of 11 million bags) will be distributed free or at a 50 percent discount through hospitals and nongovernmental organizations (NGOs), primarily in rural areas. A further 3.9 million bags of imports will be sold at a 15 percent discount and self-targeted at lower-income groups in the form of straight run or hammer-milled meal. The rest of the donor-financed yellow maize imports will be sold to the mills at about US$130 per metric ton until September. The into-mill price will rise thereafter according to a schedule agreed with the World Bank, so that by end-December maize meal prices will be consistent with the border prices that would prevail in an ordinary year. Thus, by the beginning of 1993, within 14 months of taking office and despite the drought, the Government should be in a position to eliminate subsidies without having to make further large corrective adjustments to consumer prices.

With regard to the pricing of the approximately 2 million bags that have been produced domestically, the objective is to prevent these supplies from being illegally exported while also encouraging farmers to plant next year. To this end, a minimum producer price of about US$220 per metric ton has been set, which will be paid at designated delivery points by registered buyers. Initially, white maize will be acquired by mills at the same price as the donor-financed yellow maize; the Government will pay for its transportation to the mills and pay an into-mill subsidy. Such transport and into-mill subsidies are temporary measures and will end within a few months once all the white maize has been acquired by the mills. Since white maize meal is the preferred product and the mills are now free to set their own prices, it is expected that white meal will sell at a premium.

The Government intends to complement its decision to end fertilizer subsidies by reducing the monopoly powers of the parastatal fertilizer company (NCZ). To this end, fertilizer was placed on OGL in April and NCZ has been instructed to purchase no more than two thirds of this year's fertilizer import requirement (i.e., an amount approximately equal to the fertilizer usage of small-scale farmers); the residual is expected to be imported by the private sector.

5. <u>Parastatal reform</u>

The parastatal reform program is a two-pronged effort, involving the liquidation and privatization of most parastatals (some 140 enterprises) over the next five years and the restructuring and strengthening of the few parastatals that are to be retained in the public sector (mostly public utilities).

The legal and institutional infrastructure to manage the privatization program is being prepared. The Government's privatization strategy has been formulated and Parliament passed the Privatization Act in June. Under the Privatization Act, a new Zambian Privatization Agency will be fully responsible for undertaking all activities related to the privatization process. ZIMCO, the parastatal holding company, is to be transformed into an investment holding company and its subholding subsidiaries (e.g., INDECO) are to be dismantled; its staff is to be reduced by 75 percent and its role in the privatization process will be limited to preparing the companies for sale. Ten parastatals (initially offered in 1991) are to be completely privatized by year-end, and ten additional enterprises (mainly milling companies) are to be prepared for offer for sale by the end of 1992.

Regarding the parastatals that are to be retained in the public sector, studies for the restructuring are under way or about to commence, with financial and technical support from IDA and other donors. Also, a separate new secretariat responsible for the public utilities will be set up, and a public utilities regulatory commission and systems of automatic price adjustment for the utilities are to be established by mid-1993.

6. Civil service reform

The Government's program of civil service reform is intended to motivate and retain key personnel while reducing the size of the service. First, reform of the civil service pay structure was initiated with the April wage award, which allows for greater pay differentiation in favor of the upper staff echelons. Second, the formulation of appropriate retrenchment procedures, including compensation and early retirement packages, is under way with financial support expected from donors. The retrenchment program targets a net reduction in the size of the public service of 10,000 central government workers (or 7 percent) by early 1993, and of a further 11,000 by end-1993.

7. Social policies

The implementation of growth-oriented macroeconomic and structural policies described above can be expected to have a positive impact in the coming years on employment and income generation by increasing overall economic activity, labor intensity, nontraditional exports, and the role of the private sector. In the short run, however, the drought and some of the recent price adjustment measures will have negative consequences on the poor, in both rural and in urban areas. To address both such short-term problems and longer-run concerns, the Government has devised a five-pronged approach. First, with the assistance of donors, ways are being devised to lower the cost of maize to the poor (as discussed in section III.4 above). Second, K 1 billion of the savings from the abolition of the consumer subsidies on maize meal is being channeled into welfare programs to the poorest of the poor. Third, units will be established by the Government to advise and train retrenched civil servants. Fourth, the Government, with World Bank and donor assistance, is implementing a program of small-scale, labor-intensive public works programs in water, sanitation, health, and education. Fifth, as part of the restructuring of budgetary expenditures, the share of health and education will be increased over the medium term as described in the PFP.

IV. Balance of Payments and External Financing

1. Balance of payments and financing strategy for 1992

The balance of payments outlook for 1992 has changed significantly since the scenario presented in the PFP for 1992-94 (EBD/92/32, 2/27/92), as a result of the impacts of the drought, the proposed schedule for the reduction of arrears to the Fund, and revised estimates of debt service obligations to other creditors. As described in the memorandum of economic and financial policies of the Zambian authorities, the net impact of these changes has been to increase the financing requirement for 1992 from US$1.4 billion to US$1.5 billion (Table 6).

Table 6. Zambia: External Financing Requirements, 1992-94

(In millions of U.S. dollars)

	PFP projections			Revised projections		
	1992	1993	1994	1992	1993	1994
1. Current account, excluding interest and official transfers	-287	-267	-274	-550	-296	-272
(Drought impact)				(-270)	(-48)	(...)
2. Debt service obligations	-761	-707	-610	-739	-652	-641
Nonmultilateral organizations	-504	-444	-374	-514	-437	-424
Scheduled obligations	-413	-365	-290	-491	-402	-380
Paris Club creditors	-236	-214	-180	-404	-307	-268
Pre-cutoff	-49	-48	-45	-73	-63	-60
Previously rescheduled	-172	-152	-121	-253	-177	-156
Post-cutoff	-15	-14	-14	-78	-67	-52
Other	-176	-151	-110	-87	-95	-112
Interest on arrears and service of rescheduled obligations	-91	-79	-84	-23	-34	-44
Paris Club creditors	-50	-31	-32	-7	-11	-17
Other 1/	-41	-48	-53	-16	-23	-27
Multilateral organizations	-258	-263	-235	-225	-215	-217
World Bank	-82	-87	-78	-63	-53	-54
IMF	-109	-104	-92	-95	-93	-97
Other	-67	-72	-66	-67	-69	-66
3. Targeted reduction of arrears	-293	--	--	-170	-88	--
Nonmultilateral organizations	-66	...	...	-30	...	...
Paris Club creditors	-66	...	...	-30	...	...
Post-cutoff	-66	...	...	-23	...	...
Moratorium interest on 1990-91 rescheduling	--	...	...	-7	...	...
Other	...	...	...	...	...	...
Multilateral organizations	-228	...	...	-140	-88	...
World Bank	-40	...	...	-40	...	...
IMF	-119	...	...	-31	-88	...
Other	-69	...	...	-69	...	...
4. Change in gross official reserves (increase -)	-35	-30	-30	-35	-30	-30
5. Gross financing requirement (= 1+2+3+4)	-1,376	-1,004	-913	-1,494	-1,066	-943
6. Identified disbursements	374	294	276	1,024	731	670
World Bank (nonproject)	...	...	...	240	150	150
Balance of payments support from other donors	...	...	...	396	270	220
Commodity assistance	49	50	52	105	52	53
Project assistance	229	214	198	264	240	225
Suppliers, private and short-term capital, net	96	30	26	20	19	22
7. Financing requirement, after identified disbursements	-1,003	-710	-637	-470	-335	-273

Sources: Bank of Zambia, and staff estimates.

1/ Includes imputed interest on residual financing gap.
2/ Includes deferral and temporary accumulation of arrears to nonmultilateral organizations pending conclusion of rescheduling discussions.

The program for 1992 incorporates a substantial widening of the external current account deficit, excluding interest obligations and official transfers, from US$93 million in 1991 to about US$550 million in 1992 (Table 7). This reflects primarily the following factors: (i) a decline of US$170 million in copper export receipts, given an assumed world copper price of US$0.90 per pound in the remaining months of 1992, compared with an average of US$1.06 per pound in 1991; (ii) a US$65 million recovery in imports of petroleum products, fertilizer, and mining sector inputs to more normal levels; and (iii) payments of US$240 million for emergency maize imports and associated transportation and handling charges. The program also envisages a sharp increase in other metal export receipts, owing to the impact of supply disruptions in Zaire on the world market price of cobalt; a recovery of 25-30 percent in nonmetal export receipts, mainly reflecting a return of export surrenders to formal channels; and an increase of about 6.5 percent in other imports, as a result of to more regular availability of foreign exchange through the OGL system and export retention market.

Excluding the impacts of the drought, the current account deficit excluding interest obligations and official transfers is projected to increase by US$190 million, reflecting a US$130 million reduction in the surplus of the metal sector and a US$60 million widening of the deficit of the nonmetal sector. Based on current indications of the firm availability of official transfers, which as noted below is still uncertain, the overall current account is projected to swing from approximate balance in 1991 to a deficit of US$270 million (8.3 percent of GDP).

The program envisages the timely payment of debt service obligations falling due to multilateral creditors, a reduction of SDR 22 million (US$31 million) in overdue obligations to the Fund during the second half of 1992, and the elimination of arrears to other multilateral creditors (including the US$40 million of arrears to the World Bank that were paid in January 1992 and US$69 million of other multilateral arrears). Understandings have been reached on a schedule of SDR acquisitions designed to facilitate timely payment of obligations falling due to the Fund and the programmed reduction of overdue obligations; these payments are a performance criterion under the program. The authorities intend to make payments in 1993 sufficient to reduce arrears to the Fund by a further SDR 62 million (US$88 million), to SDR 836.9 million (the level as of July 1990).

Gross international reserves are targeted to increase by US$35 million. In addition, as a buffer against uncertainties about conditions in world metal markets and possible delays in donor assistance, the program includes a contingency mechanism under which copper export receipts resulting from a world market price in excess of the program's assumed price for the remainder of the year would be added to Zambia's international reserves. Under this mechanism, the international reserve target will be raised by the amount of any such excess copper earnings, after deducting any shortfall in net nonproject external assistance. In no event will the reserve target be reduced below the program's baseline. Once the reserve target has been

Table 7. Zambia: Balance of Payments, 1987-94

(In millions of U.S. dollars)

	1987	1988	1989	1990	1991	1992	1993	1994
						Projections		
Trade balance	96	267	387	179	133	-211	-21	-63
Exports, f.o.b.	868	1,156	1,407	1,263	1,082	1,004	1,056	1,062
Copper	736	982	1,231	1,055	895	723	757	740
Other metals	66	91	106	95	103	177	169	176
Nonmetals	66	82	70	113	84	105	135	153
Imports, f.o.b.	-772	-888	-1,020	-1,084	-949	-1,215	-1,082	-1,132
Metal sector	-233	-278	-372	-346	-285	-320	-338	-358
Fertilizer	-45	-47	-73	-49	-29	-40	-38	-41
Petroleum	-67	-62	-103	-119	-73	-93	-104	-110
Maize 1/	...	...	...	...	-16	-181	...	...
Other	-427	-501	-473	-570	-545	-581	-602	-623
Services (net)	-412	-496	-579	-538	-579	-625	-565	-522
Interest 2/	-341	-409	-401	-332	-378	-313	-314	-333
Other factor	-3	-3	--	--	-13	-13	-20	-21
Nonfactor	-69	-85	-178	-206	-188	-299	-231	-168
Of which: maize handling	(...)	(...)	(...)	(...)	(...)	(-95)	(-48)	(--)
Unrequited transfers	75	65	44	253	448	566	451	390
Private	-30	-35	-28	-43	-40	-40	-41	-43
Official	105	99	72	296	488	606	492	433
Current account	-242	-164	-149	-106	1	-269	-135	-195
Metal sector	480	710	875	671	584	456	451	407
Nonmetal sector	-722	-874	-1,024	-778	-582	-725	-586	-602
Nonmonetary capital	-213	-198	-105	-323	-80	100	-79	-48
Medium- and long-term	-211	-147	-112	-149	-20	75	-89	-50
Disbursements	130	196	192	169	317	418	240	240
Amortization	-341	-343	-304	-318	-337	-343	-329	-290
Short-term	-2	-51	7	-174	-59	25	10	2
Overall balance	-456	-362	-255	-430	-79	-169	-214	-243
Financing	456	362	255	430	79	169	214	243
IMF (net)	66	76	77	89	-39	-37	-91	--
Purchases	...	...	...	...	...	...	...	...
Repurchases (scheduled)	-243	-216	-135	-122	-59	-6	-3	--
Overdue obligations	308	291	213	212	20	-31	-88	--
Gross official reserves	-13	-54	-33	-7	11	-35	-30	-30
Other foreign assets (net)	-12	-56	-65	17	20	-26	--	--
Valuation adjustment	-5	5	6	-3	--	...	...	...
Debt relief	--	--	--	799	1,158	-64	...	...
Arrears (excluding IMF)	419	391	270	-465	-1,070	-139	--	--
Financing gap	--	--	--	--	--	470	335	273
Memorandum items:								
Current account, excluding interest obligations and official transfers	2	160	205	-48	-93	-550	-296	-272
Drought impact	...	...	...	...	...	-270	-48	...
Metal sector	519	746	910	745	655	529	534	501
Nonmetal sector, excluding drought impact	-517	-586	-705	-793	-748	-809	-782	-773
Copper export volume ('000 metric tons)	475	398	432	440	375	380	390	400
Copper price (US$/lb)	0.74	1.16	1.33	1.21	1.06	0.93	0.94	0.90

Sources: Bank of Zambia; and staff estimates.

1/ Figure shown reflects timing of payment, rather than date of importation.
2/ Assumes half of residual financing gaps are filled on grant terms.

adjusted upward by US$40 million, 50 percent of any further excess copper earnings will be used to increase international reserves through the accumulation of additional balances in Zambia's SDR account, and 50 percent would be available for the discretionary use of Zambia. The use of any such balances accumulated in the SDR account, including possible accelerated reduction in arrears to the Fund, would be determined in the context of discussions on Zambia's program for 1993.

Some US$1.0 billion of Zambia's US$1.5 billion financing requirement for 1992 is expected to be met through private capital flows and firm indications of external assistance already received from external donors. The latter include roughly US$260 million of project assistance, US$100 million of commodity assistance, US$240 million of adjustment lending by the World Bank, and US$400 million of balance of payments assistance from other donors. The Zambian authorities, with the assistance of the staffs of the World Bank and Fund, are seeking to meet the remaining financing requirement of US$0.5 billion through firm commitments of additional commodity (maize) and balance of payments assistance and comprehensive debt relief from nonmultilateral creditors.

On current estimates, it would appear that debt relief on the terms available to low-income countries from bilateral official creditors would reduce the financing gap by about US$0.3 billion. This would leave cash payments of about US$230 million to Paris Club creditors (comprising US$30 million of arrears on post-cutoff-date obligations, US$78 million of post-cutoff obligations falling due in 1992, US$6 million of moratorium interest on amounts expected to be rescheduled in 1992, and US$120 million of moratorium interest on amounts rescheduled under the terms of the July 1990 Agreed Minute--including US$65 million of deferred moratorium interest); and cash payments of US$30-40 million to other nonmultilateral creditors (including interest payments on short-term debt). 1/ A larger contribution to meeting Zambia's financing requirements from this source would require exceptional cash-flow relief. There are indications that additional commodity and balance of payments assistance will be firmly committed in the coming weeks for disbursement during 1992. The staff will report to Executive Directors at the time of Board consideration of Zambia's rights accumulation program on the progress in mobilizing external financing, and the first review of the program will include a financing assurances review.

1/ The program provides for payments to non-Paris Club nonmultilateral creditors, including repayment of short-term debt, and net of new disbursements from such creditors, of no more than US$72 million during 1992. To help ensure that net payments are thus consistent with the program's objectives and Zambia's external financing constraints, the Government has approached such creditors for rescheduling on terms comparable to those of the Paris Club and ZCCM has also initiated discussions with its external creditors.

2. Long-term balance of payments prospects and Fund obligations

The conclusions of the analysis of Zambia's long-term balance of payments prospects provided at the time of Executive Board consideration of Zambia's previous rights accumulation program (EBS/91/59, 4/3/91) are still basically valid: that is, given the likelihood of a decline in copper exports, the prospects for external viability depend on substantial further efforts by both Zambia and its external creditors and donors to build on the base provided by Zambia's rights accumulation program. Zambia will need to continue and deepen the adjustment effort in order to mobilize domestic savings, promote the growth of noncopper exports, and reduce import dependence. Progress toward a sustainable balance of payments position will also depend on the willingness of Zambia's external creditors to provide very substantial debt forgiveness, debt relief on highly favorable terms, and/or an increase in the real level of grant assistance.

The results of three updated long-term balance of payments scenarios are presented in Appendix II. In all three scenarios, copper export volume is assumed to recover from 375,000 metric tons in 1991 to 400,000 metric tons a year in 1994-97; thereafter volume declines steadily to about 200,000 metric tons per year by 2002. Zambia is projected to meet all current debt service obligations to multilateral creditors, to reduce its arrears to the Fund to SDR 836.9 million by end-1993, and to clear these arrears in early 1995 with the assistance of use of Fund resources equivalent to the accumulated rights.

Scenario A (which envisages debt relief from Paris Club creditors in 1992-94 with the "enhanced concessions" currently provided in reschedulings for low-income countries, and thereafter through the continuous rescheduling of all obligations on pre-cutoff-date debt, with comparable debt relief from other nonmultilateral creditors) shows a residual financing gap of US$4.1 billion in 1993-2006, concentrated in the period 1999-2005, the period of repurchases of the encashed rights. The ratio of debt service obligations (excluding arrears) to receipts from exports of goods and nonfactor services falls from 61 percent in 1992 to 33 percent in 1997. The debt service ratio then rises to an average of 55 percent in 1999-2004 before falling again to 31 percent by 2006. Zambia's financial obligations to the Fund are projected to average 14 percent of receipts from exports of goods and nonfactor services, 50 percent of quota, and 51 percent of gross international reserves over the period 1999-2004, which is also the peak period of Zambia's possible external financing gap. These figures suggest that continued extraordinary financial support from the international community and continuing involvement of the Fund through successor arrangements may be necessary in future years.

Scenario B shows the impact of 10 percent higher world copper prices during the period 1994-2006. In this scenario, the residual financing gap for 1993-2006 is reduced to US$3.0 billion and the debt service ratio is roughly 3 percentage points lower, on average, than in Scenario A.

Scenario C provides an illustrative mix of additional efforts that could eliminate the residual financing requirement (along the lines of Scenario F in EBS/91/59). These include: (i) a 1 percentage point increase in the annual growth rate of nonmetal export volume over the period 1995-2006, which would reduce the cumulative financing requirement by US$500 million from the level implied by Scenario A; (ii) a reduction of 1 percentage point a year in the growth rate of imports by the nonmining sector after 1994, which would reduce the cumulative gap by US$1.0 billion; (iii) the provision of all Fund resources under a successor arrangement on ESAF terms, with continued Fund financial support following the encashment of accumulated rights, which would lower the cumulative gap by US$400 million; and (iv) complete forgiveness of pre-cutoff-date debt by nonmultilateral creditors, which would reduce the cumulative gap by US$2.2 billion. The debt service ratio would fall to 13-14 percent in 1998-99, rise temporarily to 32 percent in 2000-2005, and fall again to 15 percent by 2006.

These results are similar to those noted in the staff report for the previous rights accumulation program. As indicated in that report, the composition of financing and the mix between financing and adjustment would need to be reviewed continuously during and after the period of rights accumulation; these scenarios do not take into account the possibility that balance of payments assistance by the donor community might be maintained at levels nearer that expected for 1992, or the possibility of a more favorable outcome for world copper prices or Zambia's copper production.

It is clear that, on any reasonable assumptions, Zambia's external financing situation will be extremely difficult in the coming years. Successful implementation of the rights accumulation program would provide a basis for further efforts by Zambia and the international community, to ensure more rapid progress toward a sustainable balance of payments position. At the same time, the experience under the preceding Fund-monitored programs underscores the risks in the current adjustment effort and financing strategy, as the uneven record of policy implementation in turn has contributed to shortfalls in donor assistance. Finally, with its still-limited production and export base, Zambia remains highly vulnerable to developments in world copper markets and climatic conditions.

Both policy implementation and donor support have been encouraging in the early months of 1992. The new Government has shown determination to make rapid progress in crucial, and long-delayed, economic reforms, as well as a strong desire to normalize financial relations with the international community. In addition, the program provides a modest buffer against adverse external shocks through the programmed increases in international reserves, the schedule of advance acquisition of SDRs to meet Fund obligations, and the external contingency mechanism.

V. Summary of Performance Criteria and Reviews

The proposed quarterly quantitative performance criteria and structural performance criteria are set out in Table 8. The program for 1992 will provide for one review, to be completed by the Fund's Executive Board no later than December 31, 1992. The review will assess progress and developments under the program and reach understandings, if and as necessary, on actions to bring performance in line with program objectives. Particular focus will be placed on: (a) budgetary developments, including the impact of the drought on the budget; (b) interest rate policy; (c) exchange rate policy and further steps to liberalize the exchange and trade system, including reduction in the list of goods ineligible for import under OGL; (d) external financing assurances; and (e) monetary and fiscal aspects of privatization policies.

VI. Staff Appraisal

The new Government has during its short time in office taken and successfully implemented a number of key decisions which, while in some cases politically difficult, were essential to reestablishing macroeconomic stability and setting the stage for economic recovery.

First, the Government has moved rapidly to ensure that subsidies will no longer place a major burden on the budget. Fertilizer subsidies have been eliminated and maize meal prices have increased fivefold. Although assessment of the budgetary impact for 1992 is complicated by the drought, the actions the Government has taken to date, together with proportionately smaller increases in maize meal prices slated for the remainder of the year, should in themselves be sufficient to ensure that subsidies--other than targeted assistance to the poor--will not be required in 1993.

Second, the Government has implemented a fundamental reform of the personal income tax, bringing cash allowances and other fringe benefits within the tax net. This reform, from which the previous Government twice backed off, was essential to establishing a viable income tax system that could provide a buoyant source of revenue as copper earnings decline.

Third, with the shift of virtually all private sector transactions to the export retention market, the Government has taken an important step toward liberalizing the exchange system and improving the near-term incentives and longer-term outlook for noncopper exports.

The one major area where performance has fallen short of the Government's intentions is public sector wage policy, which was also an important element in the slippages under the programs of the previous Government. It was recognized from the outset of the recent series of adjustment efforts that the public service in Zambia was underpaid and overstaffed, and the strategy has consistently called for increases in real

Table 8. Zambia: Performance Criteria Under Rights Program, Second Half 1992

	1991	1992		
	Dec.	June Est.	Sept. Performance criteria	Dec.
		(In millions of kwacha)		
Reserve money 1/	21,962	27,310	28,889	30,551
Net claims on Government by banking system 1/ 2/	30,938	32,152	29,217	20,584
Debt swaps 1/ 3/	...	1,000	1,250	1,250
Net reduction in domestic arrears of Government 3/ 4/	...			
		(In millions of SDRs)		
Net international reserves 4/ 5/	-811.2	-799.0	-783.7	-756.8
New external loan commitments 1/ 6/	...	142.9	142.9	142.9
1- to 5-year subceiling	...	71.4	71.4	71.4
Stock of short-term debt 1/ 7/	274.7	315.9	315.9	315.9
Minimum reduction in external payments arrears 8/ 9/	1,027.5	-35.8	-91.7	-125.9
Minimum reduction in arrears to IMF 8/	921.8	-1.1	-7.8	-23.1

Structural Performance Criteria, Second Half 1992

Shift OGL from a positive list to a negative list.	By end-September 1992
Continue to ensure that any debt-swap operations entered into after March 1, 1992 are at a market-related discount.	From March 1, 1992
Lodge cash balances of all ministries at the Bank of Zambia.	From June 26, 1992
Ensure that the maximum bank lending rate exceeds the annualized rate of inflation in the preceding three months	Before completion of review

1/ Ceiling. The indicative limit on debt swaps and the external loan commitments ceilings are cumulative from January 1, 1992.

2/ Limits to be adjusted downward (a) if, and to the extent that, net nonproject external financing to the budget exceeds the amounts envisaged in the program, i.e., K 9,160 million between end-December 1991 and end-September 1992, and K 8,400 million between end-December 1991 and end-December 1992; (b) by the amount that total nonbank holdings of government debt exceeds the level at end-December 1991; (c) by the amount of any receipts from the mineral resource levy and company income tax payments from ZCCM in excess of K 1,800 million between end-December 1991 and end-September 1992 or K 2,600 million between end-December 1991 and end-December 1992, up to the amount through the corresponding date of any cumulative excess copper earnings (ECE) that have not been sterilized by other means; and (d) by the amount of any proceeds received from the sale of parastatals.

3/ Indicative targets only.

4/ Floor.

5/ Net international reserves are defined as gross reserves minus outstanding Fund credit (including Trust Fund loans) and Fund charges in arrears. Floor is adjustable upward, as provided for under the copper contingency mechanism.

6/ Commitments on external loans (other than debt rescheduling) with an original maturity of more than one year contracted or guaranteed by the Government, Bank of Zambia, and parastatals, except borrowing on concessional terms according to the DAC definition and borrowing from multilateral institutions. This ceiling, and the subceiling for debt with a maturity of 1-5 years, will be increased and the ceiling on short-term debt decreased to the extent that the Bank of Zambia is able to refinance its existing short-term liabilities as medium-term liabilities.

7/ Disbursed debt of Government, Bank of Zambia, and parastatals, excluding normal trade credit for imports and interest arrears. See also adjustment described in Footnote 6.

8/ Data for December 1991 are stocks. Targets are cumulative reductions from January 1, 1992.

9/ Excludes overdue payments to bilateral or commercial creditors that may arise pending consideration of requests for rescheduling of these payments.

wages, particularly in the upper grades, to be financed through prior reductions in the work force. In the event, government wages have risen sharply since 1988--both in real terms and relative to GDP (although they are still well below the levels prevailing in the early 1980s), while the civil service reform effort has yet to get off the ground. Regardless of its achievements on other fronts, the new Government will most likely fail in its effort to continue to reduce the budget deficit and bring down inflation unless it succeeds in integrating public service wage decisions fully into the budget process.

Looking forward, both the Government's stated positions and its overall record to date in taking tough policy decisions give grounds for confidence in Zambia's longer-term prospects. The Government is determined to move as rapidly as possible to dismantle the system of state intervention and ownership and let private initiative and market forces come to the fore. Privatization will most likely be a long and difficult process, but the authorities have taken early action to get that process under way.

On the exchange system, the Government has acted earlier and more decisively than originally anticipated and indications are that it will move quickly toward a liberal, unified exchange system with a market-determined exchange rate. The staff welcomes in particular the Government's decision to use the retention market exchange rate as a guide for adjustments in the official rate and to progressively narrow the spread between the two rates, as well as the Government's intention to put the OGL system on a negative list basis and to broaden further the coverage of the system.

While the informal benchmarks for March were generally met, there are areas of concern with respect to near-term macroeconomic policies, and developments will need to be monitored carefully. The overall budgetary outturn projected for 1992 depends crucially on the Government's implementing its stated policies with respect to maize pricing and the official exchange rate; while this Government's record is good in these areas, there is no room for slippage or delays. To help attain the fiscal objectives for 1992 and to lay the groundwork for further improvements in 1993, the authorities need to ensure that both Zambia Airways and the largest local councils are taking measures necessary to end their reliance on budgetary support and that the parastatal sector is setting prices and controlling costs with a view to providing the Government with a reasonable return on its investment. More generally, the authorities need to devise and implement a workable system of budgetary control and oversight at the commitment level. A cause for concern on the revenue side is what appears to be a very large number of import duty exemptions granted under the Investment Act since early this year. The staff urges the Government to re-examine these provisions of the Act with a view both to preserving government revenues and to ensuring that Zambia's course of development is not inappropriately capital intensive.

Regarding monetary policy, the Bank of Zambia will have to work closely with ZCCM and the Budget Office to ensure that any kwacha counterpart of excess copper earnings is sterilized quickly and fully. It will also be important that debt-swap offers not be responded to on an ad hoc basis but, rather, that an overall strategy be developed consistent with the intended limit on monetary creation through this channel. Although the new Government has raised interest rates twice since taking office, the maximum bank lending rate remains significantly negative in real terms, as measured against actual inflation in recent months. The staff welcomes the authorities' intention to raise that maximum rate if and as necessary to ensure that, before the completion of the program review, it is at least equal to the actual rate of inflation, and then, as inflation comes down, to let interest rates become market determined.

The international donor community has responded generously to Zambia's request for assistance both to support its program and to meet the additional requirements resulting from the drought. Not all of this financing is firm, however, as important amounts still require final decisions in capitals or budgetary authorization. Taking into account only firm commitments, in addition to the baseline financing assumptions laid out in the PFP, some US$690 million in commodity and balance of payments has been mobilized, including US$240 million in balance of payments assistance from the World Bank. While firm commitments to date do not fully cover the program's financing requirement, substantial additional amounts of assistance are still under consideration or awaiting final approval. The staff considers that the gap can be closed if donors act quickly to firm up commitments or provide additional assistance and if Zambia's creditors respond, as they have in the past, imaginatively and flexibly taking into account the very exceptional circumstances Zambia faces in this drought year.

Developments will need to be monitored closely and policies implemented firmly if Zambia is to accumulate rights and normalize its relations with the Fund according to the proposed timetable. In particular, it will be essential that Zambia meet its obligations falling due to the Fund on a timely basis and reduce its arrears to the Fund by at least SDR 22 million in 1992 and by at least a further SDR 62 million, or to the July 1, 1990 level, during 1993, as called for under the proposed program. The staff regrets that it has not proved feasible, in the context of the drought and the resultant extremely difficult external situation, to reduce overdue obligations to the Fund to the July 1, 1990 level at the outset of the program. The staff notes, however, the record of the new Government in meeting obligations falling due to the Fund in the first half of 1992 and considers that, in the circumstances, the proposed schedule for reduction of arrears to the Fund will require a determined effort by Zambia underpinned by strong donor support.

Over the medium term, the viability of Zambia's balance of payments and its ability to repay the Fund will depend importantly on additional efforts by all parties concerned--by Zambia to increase nontraditional export growth and reduce dependence on imports and by the international community to provide the necessary assistance, including comprehensive debt relief, on the most concessional terms possible.

In the present situation there are risks with respect to both policies and financing. The staff notes, however, that the proposed program includes substantial up-front action in crucial policy areas and considers that and on balance the performance during the first half of 1992 provides evidence of the commitment of the authorities. Also, the program seeks to address near-term uncertainties with regard to external financing through the contingency mechanism and the advance acquisition of SDRs and incorporates a financing assurances review before the next accumulation of rights.

The staff considers that Zambia's program for 1992 meets the standards for programs supported by upper credit tranche arrangements from the Fund. The staff therefore recommends that the Fund agree to monitor Zambia's program through March 31, 1995, and decide that Zambia will accumulate rights for potential access to Fund resources under a successor arrangement up to a maximum of SDR 836.9 million.

Zambia still maintains exchange restrictions in accordance with the transitional arrangements of Article XIV of the Fund's Articles of Agreement, except that the following exchange measures maintained by Zambia are subject to Fund approval under Article VIII: limitations on the availability of foreign exchange for certain current transactions, including limitations on personal remittances and the nonavailability of foreign exchange for tourism; a limitation on the availability of foreign exchange for the servicing of external debt, which has given rise to the accumulation of external payments arrears; and a multiple currency practice arising from the operation of the export retention market. The staff notes that the authorities have stated their intention to unify the official and retention exchange markets during the period of the rights program and recommends approval of this multiple currency practice until March 31, 1993. However, as there is not yet a clear timetable for the elimination of the other restrictions, the staff does not recommend approval of their retention by Zambia.

It is recommended that the next Article IV consultation with Zambia be held on the standard 12-month cycle.

VII. Proposed Decisions

The following draft decisions are proposed for adoption by the Executive Board:

I. 1992 Consultation

1. The Fund takes this decision relating to Zambia's exchange measures subject to Article VIII, Sections 2(a) and 3, and in concluding the 1992 Article XIV consultation with Zambia, in the light of the 1992 Article IV consultation with Zambia conducted under Decision No. 5392-(77/63), adopted April 29, 1977, as amended (Surveillance over Exchange Rate Policies).

2. Zambia continues to maintain restrictions on the making of payments and transfers for current international transactions as described in EBS/92/114, in accordance with Article XIV, except that the multiple currency practice arising from the spread between the official exchange rate and the rates for foreign exchange in the export retention market are subject to Fund approval under Article VIII, Sections 2(a) and 3, and that the limitations on the availability of foreign exchange for certain current transactions, including limitations on personal remittances and the nonavailability of foreign exchange for tourism, and the restrictions evidenced by some external payments arrears are subject to Fund approval under Article VIII, Sections 2(a). The Fund approves the retention by Zambia of the multiple currency practice arising from the spread between the official rate for foreign exchange and the rates in the export retention market until March 31, 1993 or the conclusion of the 1993 Article IV consultation with Zambia, whichever is first. The Fund encourages the authorities to remove the other exchange restrictions as soon as possible.

II. Accumulation of Rights

1. The Fund notes that, in accordance with the authorities' request, the accumulation of rights for Zambia in the amount equivalent to SDR 836.9 million approved on April 17, 1991 (EBS/91/59, Supplement 2) has been canceled as of the date of this Decision.

2. The Fund approves the accumulation of rights for Zambia as set forth in EBS/92/114.

Zambia - Accumulation of Rights

Attached herewith is a letter, with an annexed Memorandum on the Economic and Financial Policies of Zambia, dated June 26, 1992, from the Minister of Finance and the Governor of the Bank of Zambia, requesting the endorsement of a rights accumulation program (the "program") in accordance with the guidelines on Operational Modalities of the Rights Approach and its monitoring by the Fund and setting forth:

a. the objectives and policies the authorities of Zambia intend to pursue during the period of the program;

b. the policies and measures that the authorities of Zambia intend to pursue during the first year of the program; and

c. understandings of Zambia with the Fund regarding reviews that will be made of progress in realizing the program objectives and of the policies and measures that the authorities of Zambia will pursue for the second and third years of the program.

On the basis of these objectives and policies, the Fund, having found that the program of Zambia meets the Fund's standards associated with programs supported by arrangements under the extended Fund facility and the enhanced structural adjustment facility of the Fund, endorses the program of Zambia and decides to monitor it in accordance with the following provisions:

1. During the period from July --, 1992 to March 31, 1995, Zambia will accumulate rights for a maximum amount equivalent to SDR 836.9 million subject to paragraphs 2, 3, 4 and 5 below.

2. a. For the period until March 31, 1993 Zambia will accumulate rights for up to an amount equivalent to SDR 251.05 million, provided that such rights shall not exceed the equivalent of SDR 83.69 million until November 15, 1992, and the equivalent of SDR 167.38 million until February 15, 1993.

b. The accumulation of rights during the remaining period of the program shall be subject to such phasing as shall be determined.

3. a. The amounts of rights that can be accumulated in accordance with paragraphs 1 and 2 above:

(i) shall be reduced pro tanto by any reduction of Zambia's outstanding financial obligations to the Fund resulting from refunds under the burden-sharing decision or from a retroactive reduction of the rate of charge, and

(ii) may be reduced pro tanto by any amount paid by Zambia to the Fund that lowers the amount of overdue financial obligations to the Fund below SDR 836.9 million.

b. Any reduction under this paragraph shall only be taken into account in determining the amounts that may be accumulated subsequently.

4. The accumulation of rights shall be suspended:

a. throughout the first year of the program, during any period in which the data at the end of the preceding period indicate that:

(i) the ceiling on reserve money specified in Table 2 of the attached memorandum; or

(ii) the limit on net claims on government by the banking system specified in Table 2 of the attached memorandum; or

(iii) the floor on net international reserves specified in Table 2 of the attached memorandum; or

(iv) the limits on new external loan commitments specified in Table 2 of the attached memorandum; or

(v) the limit on the stock of short-term debt specified in Table 2 of the attached memorandum; or

(vi) the minimum reduction in external payments arrears specified in Table 2 of the attached memorandum; or

(vii) the minimum reduction in overdue financial obligations to the Fund specified in Table 2 of the attached memorandum; or

(viii) any of the structural performance criteria, as set out in Section V of the attached memorandum, are not observed; or

b. after November 14, 1992 until the review with the Fund contemplated in paragraph 6 of the attached letter has been completed; or

c. after March 31, 1993 and March 31, 1994, until suitable performance criteria for the second and third years of the program, respectively, have been established in consultation with the Fund as contemplated in paragraph 6 of attached letter, or after such performance criteria have been established, while they are not being observed, or

d. throughout the entire duration of the program, if Zambia:

(i) imposes or intensifies restrictions on payments and transfers for current international transactions; or

(ii) introduces or modifies multiple currency practices; or

(iii) concludes bilateral payments agreements which are inconsistent with Article VIII; or

(iv) imposes or intensifies import restrictions for balance of payments reasons; or

(v) if Zambia fails to make payments equivalent to obligations falling due to the Fund after July --, 1992.

Whenever the accumulation of rights is suspended because of this paragraph 4, it will be resumed only after consultation has taken place between the Fund and Zambia and understandings have been reached regarding the circumstances--including possible rephasing of rights to be accumulated and extension of the period of the program --in which such accumulation of rights will resume. Whenever the accumulation of rights has been suspended for a period of six months, the Fund may reduce the accumulated rights by an amount not to exceed twenty five percent of the total accumulated and by up to a further twenty five percent of the same total, every three months thereafter for as long as the suspension continues, until all previously accumulated rights have been reduced to zero.

5. An amount equivalent to the accumulated rights will be made available to Zambia as the first disbursement under a subsequent arrangement or arrangements approved by the Fund for the use of its general resources, or of resources under the SAF or ESAF, or any combination thereof, as decided by the Fund at the time of the approval of such arrangements. Such subsequent arrangement or arrangements may be approved only if Zambia has settled its overdue financial obligations to the Fund and if all the other requirements for the use of such resources are met.

6. In accordance with paragraph 6 of the attached letter, Zambia will consult with the Fund on the adoption of any measures that may be appropriate at the initiative of the government or at the request of the Managing Director because he considers that consultation on the program is desirable.

Lusaka, Zambia
June 26, 1992

Mr. Michel Camdessus
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. Camdessus:

1. At the beginning of this year the newly elected Government of Zambia set out in a Policy Framework Paper its economic strategy to stabilize the Zambian economy, to promote sustainable growth through a fundamental restructuring relying on market forces, and to make substantial progress over the medium term toward balance of payments viability. That document also contained the Government's broad quantitative macroeconomic objectives for 1992-94. Subsequently, Zambia and most of the rest of southern Africa have experienced a devastating drought. The attached memorandum describes the economic program that the Government of the Republic of Zambia intends to pursue during the remainder of 1992, and revisits the objectives for 1993-94, in light of these new circumstances.

2. The Government expects that its program will continue to be supported by external assistance to facilitate the transformation of the economy and the normalization of relations with external creditors. Substantial additional assistance also is required in 1992 to cope with the impact of the drought. The Government requests the Managing Director of the Fund, in collaboration with the President of the World Bank, to continue to assist in mobilizing the necessary support.

3. Following the breakdown of Zambia's rights accumulation program under the previous Government, new arrears were accumulated to the Fund and the World Bank. At the end of January 1992, Zambia cleared its arrears to the World Bank and reduced its arrears to the Fund to the end-1991 level. Since then, Zambia has met fully all obligations falling due to the Fund and the World Bank and will continue to do so. As of June 19, 1992, Zambia's arrears to the Fund were equivalent to SDR 920.7 million. Zambia will make additional payments to the Fund sufficient to reduce its arrears to SDR 898.7 million by December 31, 1992 according to a schedule that has been established, and to SDR 836.9 million (their level as of July 1, 1990) by December 31, 1993. Within the framework of its program, Zambia expects to settle all remaining overdue obligations to the Fund no later than March 31, 1995 and to request access to the use of Fund resources under a subsequent arrangement or arrangements.

4. We request that the Executive Board of the Fund:

(i) cancel the decision on accumulation of rights for Zambia that was approved on April 17, 1991;

(ii) find that the program of Zambia, described in the attached memorandum, is consistent with the standards for programs supported by Fund arrangements in the upper credit tranches;

(iii) endorse the program of Zambia and decide to monitor it during the period ending March 31, 1995;

(iv) decide that, in accordance with the guidelines on Operational Modalities of the Rights Approach, Zambia will accumulate "rights" during the period July 17, 1992 to March 31, 1995 up to an amount equivalent to SDR 836.9 million, minus any amount that may be payable to the Fund during the same period of the program in accordance with the contingency mechanism for 1992 as described in the attached memorandum or similar mechanisms that may be established for the remaining period, and also minus any further amount by which Zambia reduces its arrears below this level during the period ending March 31, 1995. We understand that accumulations of rights after the initial amount upon approval, equivalent to SDR 83.69 million, will be made available on a quarterly basis in nine equal installments of SDR 83.69 million each, contingent on observance of the corresponding quarterly performance criteria and completion of the applicable reviews by the Fund.

(v) endorse the intention of the Managing Director of the Fund, following full clearance of arrears to the Fund, to recommend to the Executive Board that it:

(a) terminate the declaration of Zambia's ineligibility to use the general resources of the Fund; and

(b) at the request of Zambia, approve an arrangement or arrangements from the Fund, under which an amount equivalent to the accumulated "rights" would be made available as part of the first disbursement.

We understand that the recommendation by the Managing Director referred to above would be made on the basis of satisfactory performance under the endorsed program, that the policies pursued under this program remained appropriate, and that understandings had been reached on a program for the subsequent period that would qualify for access to the Fund's resources.

5. *During the period of the monitored program, the Government of* Zambia does not intend to impose new or intensify existing restrictions on payments and transfers for current international transactions, introduce or modify multiple currency practices, conclude any bilateral agreements that are inconsistent with Article VIII of the Fund's Articles of Agreement, or impose new or intensify existing import restrictions for balance of payments reasons.

6. *The Government* believes that the policies and measures set forth in the attached memorandum are adequate to achieve the objectives of the program, but will take further measures that may become necessary for this

purpose. Zambia will remain in close consultation with the Fund during the period of the program and will consult with the Fund on the adoption of any measures that may be appropriate in accordance with the Fund's policies on such consultations. A review of the program will be completed by the Fund not later than December 31, 1992. The performance criteria and the timing of reviews for the program in 1993 and 1994 shall be established not later than March 31, 1993 and March 31, 1994, respectively. For the purposes of monitoring the program, Zambia will provide the Fund with such information as the Fund requests at regular intervals or dates requested by the Fund.

Sincerely,

Emmanuel Kasonde
Minister of Finance

Attachments

Memorandum on the Economic and Financial Policies of Zambia

I. Introduction

Since mid-1989, Zambia has been implementing a series of structural economic reforms, with technical support from the International Monetary Fund and the World Bank and the assistance of bilateral donors (and, more recently, also with Bank financial support). In July 1990, Zambia's economic and financial program was endorsed as a Fund-monitored program, and in April 1991 the Fund's Executive Board approved the accumulation of rights up to a maximum of SDR 836.9 million (the level of arrears to the Fund as of July 1, 1990). However, policies went substantially off track in the second half of 1991 under the previous Government, program performance criteria were not observed, and no rights were accumulated.

In February of this year the newly elected Government set out its economic strategy and objectives in a Policy Framework Paper (PFP). 1/ The cornerstone of that strategy was a radical reorientation of the Zambian economy from one dominated by government ownership, control, and intervention to a system in which private initiative and market forces would come to the fore to motivate and guide the mobilization and efficient allocation of resources necessary for the restructuring of the economy. At the same time, that strategy recognized that this effort could not succeed without prompt action to reduce the government budget deficit, bring down the rate of inflation, and restore macroeconomic stability. This two-pronged approach is considered essential to provide the basis for the resumption of economic growth necessary to raise over time the living standards of the Zambian people. However, the transformation of the economy, after years of economic decline, will come neither easily nor quickly. In the meantime, the Government attaches high priority to addressing the needs of the poorest and most vulnerable groups in the society.

The macroeconomic program set out in the PFP targeted real GDP growth rising from 2 percent in 1992 to 4 percent in 1994. Primarily as the result of strong fiscal measures to curtail rapidly the Government's recourse to inflationary bank financing, money supply growth was to decline from about 100 percent in 1991 to 25 percent in 1992, and to 5 percent by 1994. Reflecting inflationary momentum and the large liquidity overhang from late 1991, inflation was targeted to decline more slowly initially--falling from 100 percent in 1991 to 45 percent in 1992--with prices thereafter moving closely in line with money. For the first half of 1992, specific targets and benchmarks were established against which Zambia's progress in implementing its program is to be assessed. 2/

1/ Developments under the previous programs during 1990-91 are summarized in an appendix to the Policy Framework Paper (EBS/92/32, 2/27/92).

2/ Zambia - Report on Staff Visit (EBS/92/49, 3/13/92).

Since the time the Government's macroeconomic program was formulated, and subsequent to the presentation of the budget on January 31, there have been two major unanticipated developments that have substantially changed the outlook for 1992 and made necessary a review of the objectives for this year. First, Zambia and most other countries of southern Africa have suffered a drought of unprecedented severity that has had a devastating impact on the production of the staple food crop, maize, and has also seriously affected other sectors of the economy. As a result of the drought, real GDP is expected to fall by 9 percent this year and Zambia's external financing needs for 1992 have been increased by US$300 million, primarily for maize imports. Second, the inflationary momentum inherited from the policies of the previous Government appears to have been much stronger than anticipated. This, together with certain adjustments in administered prices, resulted in an increase in consumer prices of 50 percent in the first quarter alone, despite the fact that performance on the budget and money was broadly on track. The surge in prices that began in late 1991 and carried over into early 1992 has resulted in substantial wage pressures and large wage awards, in both the public and the private sectors.

The Government remains determined to proceed as planned with its agenda for structural reform and to take the measures necessary to bring its macroeconomic program quickly back on track. The following sections of this memorandum review developments in the first half of this year, lay out in specific terms the Government's policy agenda and macroeconomic objectives for the remainder of this year, and outline the revised balance of payments outlook and financing requirements for 1992. Certain targets and projections for 1993-94 have also been revised in light of the drought and of expected developments with respect to the balance of payments and financing.

II. Developments in the First Half of 1992

1. Structural policies

The new Government has moved rapidly to implement certain structural reforms considered essential to the success of its program. Action in most of these had been promised, but never delivered, by the previous Government.

Subsidies had become a major drain on budget resources in recent years, and the Government reduced subsidies sharply shortly after taking office, leading to an increase in maize meal prices of more than 100 percent. Subsequently, the direct consumer subsidy on breakfast meal was eliminated in January 1992 and that on roller meal eliminated in June 1992; maize meal prices consequently are now market determined, a year ahead of the timetable indicated in the PFP. The Government's objective of liberalizing other aspects of maize marketing has been complicated by the drought, as the market will be dominated by government provision of donor-funded maize, and policies in this situation are outlined below. With respect to fertilizer, the Government ended all subsidies as from March 1992, and in April fertilizer imports were made eligible for importation under the open general license system (OGL). The parastatal fertilizer company has been instructed to purchase no more than two thirds of the national requirement (approximately the fertilizer usage of small-scale farmers) this year; the balance is expected to be imported by the private sector.

The Government also has successfully implemented a long-overdue reform of the income tax system essential to restoring the income tax as an important and buoyant source of government revenue. Previously all fringe benefits, even cash allowances, were exempt from income tax, and in recent years pay awards in both the public service and the private sector have increasingly been granted in the form of such tax-free benefits. Effective April 1, 1992, all cash fringe benefits became taxable as income to the employee, and fringe benefits given in kind can no longer be considered as an expense in calculating company tax liability. At the same time, tax rates were cut (the top marginal personal tax rate falling from 50 percent to 35 percent) and the former personal allowance was replaced with a tax credit intended to remove a large number of low-income taxpayers from the tax rolls. These measures, taken together, were designed to be revenue neutral in aggregate, but they inevitably produced sharp cuts in after-tax pay for some and increases for others. This exacerbated wage demands and has rendered near-term macroeconomic management more difficult. We believe, however, that the long-term gains of broadening the tax base and increasing buoyancy outweigh that short-term cost.

The Government attaches priority to establishing a liberal exchange system with a unified, market-determined exchange rate. At end-January the kwacha was devalued by 30 percent to make up for competitiveness lost as inflation accelerated in late 1991 and, after a hiatus of several weeks, the system of small, frequent adjustments to the official exchange rate was resumed. On March 11, 1992, the share of foreign exchange proceeds that exporters of goods and services (other than the copper company, ZCCM) are allowed to retain for their own use or to sell freely in the export retention market was increased from 50 percent to 100 percent; at the same time, the provision of foreign exchange for most service payments and for the debt service of exporters was shifted to the export retention market. In the weeks following this change the exchange rate in the export retention market depreciated rapidly and the spread between the official and the retention exchange rates widened from 20 percent to about 30 percent, at which level it remained at the end of May. These measures are expected to provide an important incentive to nontraditional exporters, not only by improving competitiveness in the short run, but also by ensuring that the rate exporters receive in the future will be market determined.

2. Macroeconomic policies

Substantial progress was made through the first quarter of 1992 in implementing the economic policies and reforms that are embodied in the PFP. The 1992 budget provided for a range of revenue and expenditure measures that were intended to reduce the budget deficit to the level envisaged in the program. In general, tight control was maintained over expenditures during the first quarter and, despite a shortfall in trade taxes, the benchmark on bank financing of the budget deficit for end-March was observed.

The satisfactory fiscal performance in the first quarter of 1992 contributed to a marked deceleration in money growth. Broad money rose by 71 percent at an annual rate (seasonally adjusted), compared with over 200 percent in the final quarter of 1991. The target for broad money (and reserve money, which is a program benchmark) was exceeded by 1 percent, primarily as a result of a short delay in receipt of a large tax payment from ZCCM. However, despite these favorable monetary trends in the first quarter of this year and an increase in the maximum bank lending rate of 5 percentage points in February, high rates of inflation have persisted. Consumer prices rose by an average of 15 percent a month in the first quarter, which is roughly three times higher than had been envisaged in the program. This rate of increase in the consumer price index can in part be explained by large adjustments in administered prices, including maize, oil, and the official exchange rate, but the price advance was widespread as the sharp expansion in liquidity recorded in the latter part of 1991 worked its way rapidly through the economy.

During the second quarter of 1992, serious difficulties were encountered in the implementation of financial policies. The program had been based on an increase in civil service pay and benefits of 50 percent as from July 1. However, in view of the high prevailing rates of inflation and in an effort to assist those groups most adversely affected by the income tax reform, a civil service pay award which resulted in an increase of 130 percent in payroll costs was granted effective April 1. This increase is expected to raise the wage and benefits bill to K 7 billion above the programmed amount, but if account is taken of the broader tax base, the net increase would amount to some K 5 billion. In addition, recourse to bank financing was made necessary by a larger pay-down of domestic arrears than had been envisaged in the program. Monetary management was further undermined in May by the fact that large foreign exchange earnings were not fully sterilized at the Bank of Zambia. By the end of May, reserve money growth for the year to date reached 25 percent, which is the program target for the year as a whole. There were, nonetheless, clear signs in the second quarter of an abatement in inflation, with the increase in consumer prices dropping in April and May to about 6 percent a month.

Applications for imports under the open general license (OGL) system moderated during the first five months of 1992, with approved applications running about US$4.5 million a week, compared with the program target of just over US$5 million a week. In addition, copper export receipts were buoyed by continued higher-than-programmed world copper prices and higher production. Net external financing was in line with expectations, and Zambia observed the benchmarks on external payments arrears, including those to the Fund. However, Zambia failed to meet the net international reserves target (which is a benchmark under the program) by a small margin of US$8 million, owing mainly to an unexpectedly large contraction of short-term lines of trade credit intermediated through the Bank of Zambia. 1/

1/ The definition of net international reserves for program monitoring purposes does not include Bank of Zambia short-term debt.

III. Macroeconomic and Structural Policies for the Second Half of 1992

The Government intends to bring its macroeconomic program rapidly back on course during the second half of 1992 and to proceed as scheduled with its agenda of structural reform.

1. Macroeconomic policy

The Government considers it essential to rapidly curtail the recent surge in reserve money growth while providing adequate scope for the extension of bank credit to the nongovernment sectors, and fiscal and monetary policies will be geared to those objectives. The original program for 1992 had envisaged zero net recourse to inflationary bank financing of the Government and money growth for the year of 25 percent; this would have permitted credit to the nongovernment sectors to increase roughly in line with the targeted inflation of 45 percent. Under its revised program, the Government intends to bring the pace of money supply growth and inflation during the second half of 1992 back in line with original program objectives for the same period. However, given developments during the first half of the year, this will imply money supply growth of 35 percent, and inflation of about 100 percent, for 1992 as a whole. In order to provide adequate resources to the nongovernment sectors in this new situation, the Government now intends to reduce its net indebtedness to the banking system by K 10 billion, or 2 percent of GDP, over the course of 1992.

a. Fiscal policy and maize pricing

After repaying K 5 billion to the domestic banking system in the first quarter of 1992 and borrowing K 6 billion in the second, the Government intends to reduce its domestic bank debt by about K 3.0 billion and K 8.5 billion during the third and fourth quarters, respectively. To some extent these movements in bank borrowing reflect the volatility of net external financing. Net nonproject external financing (defined as gross disbursements of donor assistance other than maize provided in kind, minus government external debt service payments and cash payments for maize imports) moved from a net inflow of K 5 billion in the first quarter to a projected net outflow of almost K 2 billion in the second, and is expected to show a net inflow of K 6 billion in the third quarter and a small outflow in the fourth. These shifts in net external financing reflect the timing of certain large transactions, such as World Bank disbursements, as well as the fact that a substantial part of maize imports is being purchased early in the year by the Government, to be reimbursed subsequently by donors. Reflecting both higher U.S. dollar amounts and exchange rate developments, net nonproject external financing going through the budget is now expected to reach K 8.4 billion, compared with K 4.7 billion assumed in the original program.

In the present circumstances, expected budgetary developments can be best understood by looking at transactions related to maize, fertilizer, and other drought-related expenditures separately from the other accounts. The costs of maize imports are expected to be met entirely through additional donor assistance. While part of maize imports will be distributed free or at a substantially reduced price to vulnerable groups (see Section III.4), most will be sold to the mills on commercial terms with the counterpart funds going to the budget. Maize pricing policies will therefore have a critical impact on budgetary resources.

Given the objective of eliminating subsidies, the Government has decided that by the end of this year donor-provided maize should be selling at a price that approximates the expected border price in a normal crop year. To that end, a schedule of the prices at which the Government will sell maize to the mills and others over the remainder of the year has been developed in conjunction with World Bank staff. Consumer prices for maize meal will be market determined. The small amount of maize expected to be produced domestically this year will be sold to the mills at the same price as imported maize and most of it will be marketed early in the year, before prices reach border equivalents. Producer prices have recently been increased substantially to ensure that the small domestic maize harvest is retained in the country. Given the into-mill pricing policy, transport and into-mill subsidies on domestic maize are now in effect on a temporary basis.

The Government expects to receive about K 12 billion in counterpart funds from the sale of donor-financed maize in 1992 and a further K 19 billion in the first half of 1993. Most of the counterpart funds received this year will be spent on drought-related items, including the domestic transport and handling of imported maize. The largest expenditure will be K 6.3 billion to provide input credits to small-scale farmers for the next planting season. Other drought-related expenditures include the improvement of rural water supplies, assistance to the livestock sector, and the upgrading of roads in remote subsistence farming areas to which maize will need to be delivered. Total transactions related to maize, fertilizer, and other drought-related expenditures, after recording a deficit of K 2.3 billion in the first half of 1992, are expected to show a further deficit of K 3.4 billion in the third quarter of this year and a surplus of K 4.3 billion in the fourth.

The (cash) primary budget deficit, excluding grants as well as maize, fertilizer, and drought-related expenditures, is expected to improve steadily over the remainder of the year, moving from a deficit of K 2.6 billion in the second quarter to a surplus of K 2.1 billion in the fourth. For the year as a whole the budget on this definition is expected to be approximately in balance, compared with a surplus of less than 1 percent of GDP envisaged in the original program. The improvement during the remainder of the year will result from rising revenue collections combined with expenditure restraint.

Revenues are expected to be buoyed by the strong performance of the personal income tax, which has already started to show up in sharply increased pay-as-you-earn (PAYE) receipts. The tax reform implemented in April was designed to be revenue neutral, other things being equal; however, the new system has a high short-run elasticity and recent rounds of wage adjustments have led to a significantly faster rate of increase in tax revenues. As a result, PAYE collections are now projected at 2.6 percent of GDP for the year as a whole, compared with the 1.5 percent of GDP envisaged in the original program for 1992. Also, in order to help improve the overall fiscal position after the weak performance of the second quarter, the Government will apply the 20 percent general sales tax to clear beer, soft drinks, and cigarettes effective July 1, 1992; these items are subject to excise tax but were previously exempt from sales tax. This measure is expected to raise K 1.5 billion during the second half of the year, or 0.6 percent of GDP on a full-year basis. Another factor that will improve domestic revenues in the second half of 1992 is the payment of dividends from parastatals after the close of their tax years under the Government's mandatory dividend policy. A negative factor in the revenue outlook is that, despite the substantial further depreciation of the kwacha, receipts from import duties and sales tax on imports are now projected to be no higher relative to GDP than envisaged in the PFP; in part this reflects a conservative projection based on poor tax collections in the early months of the year, but it also reflects the expected impact of duty exemptions granted this year under the new Investment Act. Total nongrant revenues are expected to reach 18.0 percent of GDP this year, compared with the original target of 17.5 percent of GDP and the 1991 outturn of 17.0 percent of GDP.

On the expenditure side, the major development is the recent wage adjustment that raised civil service payroll costs by 130 percent, which will increase expenditure on this item to 4.7 percent of GDP compared with the programmed 4.2 percent. Total core expenditure--excluding outlays on maize, fertilizer, and drought-related expenditure--is now targeted at 17.7 percent of GDP, the same as in 1991 but about 1.5 percent of GDP above the PFP figure. In addition to increased payroll costs, this reflects higher outlays for RDCs (recurrent departmental charges, i.e., primarily government recurrent expenditure for goods and services); RDCs were running above program during the first half of the year, but monthly funding trajectories have now been established to contain this category of expenditure to 3.9 percent of GDP for the year as a whole. The increase in core expenditure also reflects unprogrammed subventions to Zambia Airways; a major review of Zambia Airways operations is under way.

b. Monetary policy

The targeted rate of money growth for 1992 has been revised upward from 25 percent to 35 percent. However, the annualized rates of growth for the third and fourth quarters are the same as in the original program, that is, about 10 percent and 5 percent, respectively, seasonally adjusted. To meet this objective, quarterly limits on reserve money have been established as a performance criterion under the program. Given program objectives for the budget and net international reserves, the targeted expansion in the money supply is expected to be consistent with an increase of 100 percent in credit to the nongovernment sectors over the course of 1992. In addition, the Government and ZCCM have each effected already in 1992 a substantial net repayment of arrears to domestic suppliers, and for the year as a whole such repayments are expected to provide additional resources to the nongovernment sectors equivalent to an increase in bank credit of about 20 percent.

While strict adherence by the Government to its fiscal objectives will be critical to meeting the monetary targets, active use will also be made of available monetary policy instruments, such as changes in liquid assets requirements and adjustments in interest rates on government debt. In order to help mop up excess liquidity in the economy, two measures were taken late in the second quarter. First, all ministries are now required to hold their cash balances with the central bank rather than commercial banks; previously two ministries had held balances of more than K 2 billion with the commercial banks. Also, the Government is seeking to reach understandings with ZCCM whereby that company will shift a large part of its volatile, and at times substantial, cash resources from the commercial banks into treasury bills. Finally, as provided for under the contingency mechanism (see below), the kwacha counterpart of additional ZCCM receipts that result from any excess of world copper prices above US$0.90 per pound will be sterilized, either through the mineral resource levy, directly at the Bank of Zambia, or by the budget.

With respect to interest rate policy, the Government seeks t achieve positive levels in real terms and, subsequently, to eliminate the ceiling on bank lending rates. Interest rates will thus become market determined. To that end the maximum bank lending rate was increased by a further 2 percentage points in June, after the 5 percentage point rise in February. At present the effective maximum bank lending rate is 73 percent, well above the targeted rate of inflation for the second half of 1992. If inflation comes down as targeted, the Government will not reduce the maximum bank lending rate but rather allow it to become inoperative prior to eliminating it entirely. If, however, inflation does not come down as targeted, the Government still firmly intends to achieve positive real interest rates before the completion of the review under the program; accordingly, the maximum lending rate will be reviewed monthly against the recent inflation experience and adjusted if necessary.

In order to help meet the monetary targets, a limit of K 1,250 million (equivalent to 6 percent of reserve money) has been imposed on the amount of kwacha created as a result of debt-swap arrangements, and procedures are in place to ensure that debt is swapped at a market-related discount. Moreover, to conserve scarce foreign exchange resources, no direct debt discounting involving the use of the Bank of Zambia's reserves will be undertaken unless donor assistance is made available specifically for this purpose.

2. External policies

The decision in March 1992 to shift to the retention market 100 percent of the receipts from exports of goods and services (except those of ZCCM), as well as nongovernment payments for services and the debt service payments of exporters, was a major step toward the Government's objective of achieving a unified exchange system with a market-determined exchange rate. An Exchange Market Liberalization Committee has been established to help plan and oversee future steps and an orderly transition to that new system. On June --, 1992 a number of further steps were taken. Foreign investors and nongovernmental organizations can now sell the foreign exchange they bring into the country in the retention market. (The major categories of transactions now effected at the official rate are those of the Government and ZCCM and certain transactions of other parastatals, as well as imports of oil and imports under the OGL system, including fertilizer.) Ownership of retention accounts has been shifted from the Bank of Zambia to the commercial banks. Banks can now sell foreign exchange without prior Bank of Zambia approval for transactions up to US$500 and for business travel abroad, and the maximum amount of kwacha a traveler can take out of the country was changed from K 2,000 (about US$10) to the equivalent of US$100 at the retention rate. The Exchange Market Liberalization Committee has been asked to prepare a proposed schedule for further liberalization.

A decision has also been taken to replace by no later than September 1992 the present positive list of goods eligible for importation under OGL with a negative list system of goods not eligible for OGL. The initial negative list will include goods constituting no more than 10 percent of base-period imports, excluding oil. Thereafter, the Government intends to reduce the OGL negative list to the same short negative list (about 5 percent of base-period imports) that now applies to the retention market; understandings on a timetable for reduction of the negative list are to be reached in the context of the review of the program.

As an increasing proportion of Zambia's foreign exchange transactions have been shifted to the retention market, the exchange rate in that market has become the primary indicator of exchange market conditions in the country. The Government intends to use the retention rate as a guide in adjusting the official rate and to reduce the spread between the two markets progressively during 1992.

3. Other structural reforms

The Government believes that in order to improve economic efficiency and achieve sustainable economic growth over the medium and long run, macroeconomic stabilization will have to be accompanied by structural reform. To this end, the Government, with the assistance of the World Bank and donors, has embarked on structural reform initiatives in the parastatal sector, the civil service, the health and education sectors, as well as in the agricultural and international trade sectors, as discussed above.

a. Parastatal reform

The parastatal reform program is being carried out as a two-pronged effort. The few parastatals that are to be retained in the public sector, will be restructured and given more independence, and will agree performance standards with a new public utility regulatory commission. Most other parastatals (some 140 enterprises) are to be privatized over the next five years. As a first step in establishing financial discipline in the parastatal sector, a strict mandatory dividend policy for parastatals was introduced with the 1992 budget, and their dividend-generating potential is expected to be boosted by their newly granted autonomy to adjust prices in line with costs.

Regarding the public utilities, studies for the restructuring of the Post and Telecommunications Corporation, Zambia Airways, Zambia Electricity Supply Corporation, Zambia Railways, the water companies, and ZIMOIL, financed by IDA and other donors, are to commence by mid-1992. In addition, a separate new secretariat will be responsible for the six utilities, and a public utilities regulatory commission and systems of automatic price adjustment for the utilities will be established by mid-1993.

To manage the privatization program, the legal and institutional infrastructure is being prepared. The Government's privatization strategy has been formulated and a privatization bill has already been presented to Parliament. A new organizational setup will be provided through the Privatization Act which was presented to parliament in June 1992. The Act provides for the Zambian Privatization Agency, which would replace the interim Privatization Steering Committee and would be fully responsible for undertaking all activities related to the privatization process. ZIMCO, the parastatal holding company, is to be transformed into an investment holding company and its role in the privatization process will be limited to preparing the companies for sale. Ten parastatals (initially offered in 1991) are to be completely privatized by year-end, and ten additional enterprises (mainly milling companies) are to be prepared for offer for sale by the end of this year.

b. Civil service reform

The public service has become too large, beyond the means available for it to operate productively and efficiently. The Government has therefore embarked on a program of civil service reform designed to motivate and retain key personnel while reducing the size of the service. Together with the recent wage award, the pay structure has been reformed to allow for greater pay differentiation in favor of the higher levels of the civil service. An exercise to identify areas of retrenchment has been completed. The formulation of appropriate compensation, early retirement packages, and retrenchment procedures is under way with expected financial support from donors. The budgetary cost of this retrenchment, net of associated wage savings, will not exceed K 1.8 billion in 1992. The target of the retrenchment program is a reduction in the size of the public service of at least 10,000 central government workers by early 1993, and by a further 11,000 by end-1993. (There are at present 140,000 central government workers.) In line with this policy, the Government has already abolished the Prices and Incomes Commission, the Department of National Guidance, and the Price Control Department. The abolition of additional regulatory bodies is planned for the period ahead.

4. Social action program

The program is expected to have a positive impact on the most disadvantaged groups in Zambia in the coming years. In the short run, however, some of the recent price adjustment measures will have negative consequences on the poor, especially in urban areas. To deal with this, as well as with longer-term problems, the Government has devised a five-pronged approach. First, with the assistance of donors, ways are being devised to lower the cost of maize to the poor. Consistent with understandings reached with donors, some 1.7 million bags of imported yellow maize will be distributed free or at a 50 percent discount through hospitals and NGOs, and a further 3.9 million bags targeted at lower-income groups will be sold in the form of straight run or hammer-milled meal at a 15 percent discount. Second, K 1 billion of the saving from the abolition of the consumer subsidies on maize meal is being channeled through welfare programs to the poorest of the poor. Third, the Government will establish units in the Cabinet Office and ZIMCO to assist retrenched employees in adjusting to new opportunities outside the public sector. Fourth, the Government, with World Bank and donor assistance, is implementing a program of small-scale, labor-intensive public works programs in water, sanitation, health, and education. Fifth, as part of the rationalization of expenditures in the budget, the share of health and education will be increased.

To improve the quality and quantity of health services, the Government will channel resources to rehabilitate the health infrastructure and on-service delivery mechanisms, including the provision of essential drugs to hospitals, and will implement better budgeting, decentralize management, and introduce cost recovery measures. The Government has initiated a national population policy aimed at reducing the high rate of population growth, including improved family and maternal health care programs and expanded public education on family planning methods. The Government will step up its efforts in general education on AIDS prevention, with particular focus on the targeting of special high-risk groups.

To improve access to quality education, emphasis in expenditure is being placed on primary education, particularly in the very poor urban and rural areas. In an effort to strengthen the financial resource base for education, the Government has introduced user fees on secondary and higher education.

IV. Balance of Payments and External Financing

The medium-term outlook and objectives for Zambia's balance of payments were described in the PFP for 1992-94. The drought has since caused severe losses in agricultural production and hydroelectric generating capacity. Discussions have proceeded with multilateral and bilateral donors, in the Consultative Group for Zambia and other fora, to identify external financing for the adjustment program and to offset the impacts of the drought.

Prior to the drought, the current account deficit, excluding interest payments and official transfers, was projected to widen from US$90 million in 1991 to US$287 million in 1992. This widening of the current account deficit was due largely to a projected decline in copper export prices from US$1.06 per pound in 1991 to US$0.90 per pound in 1992, with copper export volume remaining at the historically low level of 375,000 metric tons to which it had fallen in 1991. In addition, the program provided for a partial recovery in imports, particularly of mining sector inputs and petroleum. For 1993-94, the noninterest current account deficit was projected to narrow only slightly, to US$270 million a year, owing to continued low copper output and weakness in world copper prices, in response to growing world copper output and depressed demand. Against this background, success in achieving the Government's goal of increasing nontraditional exports by 10-15 percent a year over the next decade was viewed as essential to support even modest further growth in imports.

In the wake of the drought, Zambia's maize import requirements are projected to widen by US$290 million for the current crop season (June 1992-May 1993), representing the cost of purchasing and transporting into this landlocked country roughly 1.0 million metric tons (11 million bags) of maize. About US$240 million of this cost will be incurred in 1992. In addition, the drought is expected to result in losses in agricultural export receipts and a shift from net exports to net imports of electricity, whose total impact may be on the order of US$30 million. These drought impacts have been offset partially by higher-than-expected copper production and export volume in the early months of 1992, which is assumed to result in a modest upward shift in the production profile for 1993-94 as well. Nevertheless, the noninterest current deficit is now projected to reach US$550 million in 1992 and US$300 million in 1993, before declining to US$270 million in 1994.

The external financing requirement for 1992, taking into account Zambia's debt service obligations and the targeted reserve increase and reduction in external arrears, is currently estimated at US$1.5 billion, compared with US$1.4 billion at the time of the PFP. This increase in the financing requirement reflects the net impact of four factors: (i) the US$260 million widening of the noninterest current account deficit described above; (ii) a US$12 million reduction in obligations falling due to the Fund stemming from the elimination of special charges during the second half of 1992; (iii) a reduction of US$31 million, rather than US$119 million, in arrears to the Fund during 1992, with the remaining US$88 million needed to reduce arrears to their July 1990 level to be paid in 1993; and (iv) a small net reduction in Zambia's debt service obligations to other creditors based on more complete information on stocks of debt, rescheduling, and interest terms.

Roughly US$300 million of the 1992 financing requirement is expected to be met through commitments of project and commodity assistance that were outstanding at the time of the PFP. Disbursements by the World Bank and the African Development Bank (ADB), mainly in the form of adjustment lending, are expected to total another US$300 million. From the World Bank, this would include the US$80 million already disbursed under the second tranche of the Economic Recovery Credit, US$150 million from the first two tranches of the Privatization and Industrial Reform Adjustment Credit, and US$10 million of supplementary "Fifth Dimension" financing through IDA reflows.

The Government is seeking to meet the remaining US$0.9 billion financing need through additional support from bilateral and multilateral donors in the forms of balance of payments assistance, donations of maize, and debt relief. Firm indications of balance of payments and additional maize assistance totaling about US$450 million have been received from a number of donors, including Canada, Denmark, the EEC, Finland, France, Germany, Japan, the Netherlands, Norway, Sweden, Switzerland, the United Kingdom, and the United States. Additional pledges under consideration could narrow the financing gap quite substantially.

Even with the expected further progress in this regard, however, meeting the program's external financing requirement for 1992 will probably also require exceptionally generous and comprehensive debt relief from nonmultilateral creditors. Obligations falling due on medium- and long-term debt to nonmultilateral creditors in 1992 total about US$530 million. 1/ Of this amount, some US$440 million is owed to bilateral creditors participating in the Paris Club, including an estimated US$200 million of obligations on pre-cutoff and previously rescheduled debt, US$80 million on post-cutoff maturities, US$30 million of arrears on post-cutoff maturities and moratorium interest, US$120 million of moratorium interest on amounts consolidated in 1990-91 (including moratorium interest deferred from 1991) and US$7 million of moratorium interest on amounts assumed to be consolidated in 1992.

1/ This figure excludes US$600 million of arrears to private creditors and official bilateral creditors that do not participate in the Paris Club, on which discussions toward possible rescheduling are continuing.

The Government is also continuing discussions, with its private external creditors and those bilateral official creditors who have not participated in the Paris Club, for a rescheduling or refinancing of arrears and amounts falling due. The program for 1992 provides for US$72 million of payments to such creditors, inclusive of any net repayment of short-term lines of credit and net of any new financing from them. Procedures to monitor such payments were established in the context of the program for 1991 and, in order not to jeopardize the achievement of the program's objectives, a plan to ensure that these payments are limited to no more than US$72 million is being elaborated in the context of discussions with creditors.

The response of the donor community to Zambia's extremely large external financing requirements, particularly in the wake of the drought, has been most generous. Disbursements of balance of payments assistance totaling US$200 million were received in January-May (including the US$80 million World Bank disbursement), and substantial further disbursements are anticipated in June-July. However, Zambia's external financing requirements are also large in the second and third quarters of 1992, particularly because avoiding shortages of maize will require that arrangements for the purchase of virtually the entire 1.0 million metric ton import requirement be completed early in the third quarter. Thus, there is no room for slippage in the expected timetable for already committed amounts and there is an urgent need to identify firm sources of additional balance of payments and maize assistance in order to provide greater confidence that the external financing needs can be met fully and on time.

During 1992, the Government intends to achieve an increase in gross international reserves of US$35 million, as well as reduction in Zambia's overdue obligations to the Fund by SDR 22 million from the level outstanding at end-June 1992. These targets are reflected in the performance criteria for net international reserves and for the minimum reduction in arrears to the Fund. Zambia intends to make monthly acquisitions of SDRs in amounts sufficient to meet repurchases and charges falling due and to meet its targets for the reduction of arrears to the Fund. The Government intends to make further payments to the Fund in 1993 sufficient to meet obligations falling due and to reduce arrears to the Fund to SDR 836.9 million, the level as of July 1990. The performance criteria for the minimum reduction in total external arrears provide for the elimination of all arrears to other multilateral institutions by the end of 1992.

The program for 1992 incorporates a contingency mechanism to address certain important uncertainties in the balance of payments outlook, in a form similar to the programs for 1990 and 1991. The balance of payments projections underlying the 1992 program are based on an average copper price of US$0.90 per pound during the last three quarters of the year. The contingency mechanism provides that the program target for net international reserves will be adjusted upward for the excess earnings derived from world copper prices above that level. This adjustment will be reduced by the amount of any shortfall in net nonproject external assistance from the programmed amounts, with the caveat that in no case will the reserve target be reduced below the baseline increase of US$35 million. Once the cumulative upward adjustment of the reserve target has reached US$40 million, 50 percent of any further net excess copper earnings will be used to accumulate additional reserve balances in Zambia's SDR account, and the utilization of the remaining 50 percent will be determined by the Government at that time.

V. Summary of Performance Criteria and Reviews

Quarterly performance criteria for the second half of 1992 have been established for the following and are set out in the attached table: (a) reserve money; (b) net claims on Government by the banking system; (c) net international reserves; (d) the contracting or guaranteeing of nonconcessional medium- and long-term public and publicly guaranteed loans from nonmultilateral creditors; (e) the stock of short-term external debt; and (f) the change in external arrears, with a subceiling on arrears to the Fund. An indicative ceiling has been set for debt swaps and an indicative floor for the pay-down of the Government's domestic arrears.

The structural performance criteria are as follows: (a) that the OGL will be shifted from a positive to a negative list system by September 30, 1992; (b) that any debt-swap operations entered into after March 1, 1992 are at a market-related discount; (c) that from June 26, 1992, cash balances of all ministries will be lodged with the Bank of Zambia, rather than commercial banks; and (d) that before the completion of the 1992 program review, the effective maximum lending rate will equal or exceed the annualized rate of inflation in the three preceding months.

The 1992 program will provide for one review to be completed by the Fund's Executive Board no later than December 31, 1992. The review will assess progress and developments under the program and reach understandings, if and as necessary, on actions to bring performance in line with program objectives. Particular focus will be placed on: (a) budgetary developments, including the impact of the drought on the budget; (b) interest rate policy; (c) exchange rate policy and further steps to liberalize the exchange and trade system, including reduction in the list of goods ineligible for import under OGL; (d) external financing assurances; and (e) monetary and fiscal aspects of privatization policies. Reviews and phasing for the subsequent program years (1994 and 1995) will be established in the context of future reviews to be completed not later than end-March 1993 and 1994, respectively.

Table 1. Zambia: Quantitative Benchmarks Under Informal Program, First Half 1992

	1991	1992		
	Dec.	March		June
		Prog.	Act.	Prog.
		(In millions of kwacha)		
Reserve money 1/	21,962	22,768	22,899	23,771
Net claims on Government by banking system 1/ 2/				
Unadjusted	30,938	27,760	...	28,293
Adjusted	...	27,274	25,944	...
Debt swaps 1/ 3/	...	330	307	1,000
Net reduction in domestic arrears of Government 3/ 4/	...	500	492	1,000
		(In millions of SDRs)		
Net international reserves 4/ 5/				
Unadjusted	-811.2	-799.5	...	-799.5
Adjusted	...	-800.1	-804.9	-799.0
New external loan commitments 1/ 6/		142.9	--	142.9
1- to 5-year subceiling	...	71.4	--	71.4
Stock of short-term debt 1/ 7/				
Unadjusted	278.5	319.8	...	319.8
Adjusted	274.7	315.9	238.6	315.9
Minimum reduction in external payments arrears 8/ 9/	1,027.5	30.9	30.9	34.7
Minimum reduction in arrears to IMF 8/	921.8	--	--	--

1/ Ceiling. The indicative limit on debt swaps and the external loan commitment ceilings are cumulative from January 1, 1992.

2/ Limits adjusted downward (a) if, and to the extent that, net nonproject external financing to the budget exceeds the amounts envisaged in the program, i.e. K 4,558 million through end-March 1992 and K 5,955 million through end-June 1992; (b) by the amount that total nonbank holdings of government debt exceeds the level at end-December 1991; (c) by the amount of any receipts from the mineral resource levy and company income tax payments from ZCCM in excess of K 500 million through end-March 1992 or K 1,000 million through end-June 1992, up to the amount through the corresponding date of any cumulative excess copper earnings (ECE) that have not been sterilized by other means; and (d) by the amount of any proceeds received from the sale of parastatals.

3/ Indicative targets only.

4/ Floor.

5/ Net international reserves are defined as gross reserves minus outstanding Fund credit (including Trust Fund loans) and Fund charges in arrears. Floor is adjustable upward, as provided for under the copper contingency mechanism. The floor is adjustable downward by the amount of any cash payments by the Bank of Zambia for emergency maize imports during January-March 1992, up to a maximum of US$10 million.

6/ Commitments on external loans (other than debt rescheduling) with an original maturity of more than one year contracted or guaranteed by the Government, Bank of Zambia, and parastatals, except borrowing on concessional terms according to the DAC definition and borrowing from multilateral institutions. This ceiling, and the subceiling for debt with a maturity of 1-5 years, is increased and the ceiling on short-term debt decreased to the extent that the Bank of Zambia is able to refinance its existing short-term liabilities as medium-term liabilities.

7/ Disbursed debt of Government, Bank of Zambia, and parastatals, excluding normal trade credit for imports and interest arrears. See also adjustment described in Footnote 6.

8/ Data for December 1991 are stocks. Targets for March and June 1992 are cumulative reductions from January 1, 1992.

9/ Excludes overdue payments to bilateral or commercial creditors that may arise pending consideration of requests for rescheduling of these payments.

Table 2. Zambia: Performance Criteria Under Rights Program, Second Half 1992

	1991	1992		
	Dec.	June	Sept.	Dec.
		Est.	Performance criteria	
		(In millions of kwacha)		
Reserve money 1/	21,962	27,310	28,889	30,551
Net claims on Government by banking system 1/ 2/	30,938	32,152	29,217	20,584
Debt swaps 1/ 3/	...	1,000	1,250	1,250
Net reduction in domestic arrears of Government 3/ 4/	...			
		(In millions of SDRs)		
Net international reserves 4/ 5/	-811.2	-799.0	-783.7	-756.8
New external loan commitments 1/ 6/	...	142.9	142.9	142.9
1- to 5-year subceiling	...	71.4	71.4	71.4
Stock of short-term debt 1/ 7/	274.7	315.9	315.9	315.9
Minimum reduction in external payments arrears 8/ 9/	1,027.5	-35.8	-91.7	-125.9
Minimum reduction in arrears to IMF 8/	921.8	-1.1	-7.8	-23.1

Structural Performance Criteria, Second Half 1992

Shift OGL from a positive list to a negative list.	By end-September 1992
Continue to ensure that any debt-swap operations entered into after March 1, 1992 are at a market-related discount.	From March 1, 1992
Lodge cash balances of all ministries at the Bank of Zambia.	From June 26, 1992
Ensure that the maximum bank lending rate exceeds the annualized rate of inflation in the preceding three months	Before completion of review

1/ Ceiling. The indicative limit on debt swaps and the external loan commitments ceilings are cumulative from January 1, 1992.

2/ Limits to be adjusted downward (a) if, and to the extent that, net nonproject external financing to the budget exceeds the amounts envisaged in the program, i.e., K 9,160 million between end-December 1991 and end-September 1992, and K 8,400 million between end-December 1991 and end-December 1992; (b) by the amount that total nonbank holdings of government debt exceeds the level at end-December 1991; (c) by the amount of any receipts from the mineral resource levy and company income tax payments from ZCCM in excess of K 1,800 million between end-December 1991 and end-September 1992 or K 2,600 million between end-December 1991 and end-December 1992, up to the amount through the corresponding date of any cumulative excess copper earnings (ECE) that have not been sterilized by other means; and (d) by the amount of any proceeds received from the sale of parastatals.

3/ Indicative targets only.

4/ Floor.

5/ Net international reserves are defined as gross reserves minus outstanding Fund credit (including Trust Fund loans) and Fund charges in arrears. Floor is adjustable upward, as provided for under the copper contingency mechanism.

6/ Commitments on external loans (other than debt rescheduling) with an original maturity of more than one year contracted or guaranteed by the Government, Bank of Zambia, and parastatals, except borrowing on concessional terms according to the DAC definition and borrowing from multilateral institutions. This ceiling, and the subceiling for debt with a maturity of 1-5 years, will be increased and the ceiling on short-term debt decreased to the extent that the Bank of Zambia is able to refinance its existing short-term liabilities as medium-term liabilities.

7/ Disbursed debt of Government, Bank of Zambia, and parastatals, excluding normal trade credit for imports and interest arrears. See also adjustment described in Footnote 6.

8/ Data for December 1991 are stocks. Targets are cumulative reductions from January 1, 1992.

9/ Excludes overdue payments to bilateral or commercial creditors that may arise pending consideration of requests for rescheduling of these payments.

Long-Term Balance of Payments Scenarios

This appendix presents three long-term balance of payments scenarios, updating the analysis of Zambia's long-term balance of payments prospects that was provided at the time of Executive Board consideration of Zambia's previous rights accumulation program (EBS/91/59, 4/3/91). The results are summarized in Table 1.

In all three scenarios, copper export volume is assumed to recover from 375,000 metric tons in 1991 to 400,000 metric tons per year in 1994-97; thereafter volume declines steadily to about 200,000 metric tons per year by 2002. Reflecting expected increases in global supply and weak demand conditions, world copper prices are assumed to fall to US$0.86 per pound by 1995 before recovering to US$0.96 per pound in 1997, and subsequently to remain constant in real terms relative to world inflation of 3 percent per year. Petroleum import volume grows in line with real GDP (4.5 percent a year in 1995-2006) and petroleum price assumptions are consistent with the WEO scenario at the time of program negotiations. Other export and import prices are assumed to grow by 3 percent a year. The import requirements of the metal sector are assumed to vary with copper output. Zambia is projected to meet all current debt service obligations to multilateral creditors, to reduce its arrears to the Fund to SDR 836.9 million by end-1993, and to clear these arrears in early 1995 in conjunction with the use of Fund resources equivalent to the accumulated rights. As was the case for the scenarios presented with the 1991 rights program, Fund resources are assumed to be allocated between ESAF and GRA resources in a ratio of 2:1. Disbursements from the World Bank are assumed to fall slightly in 1993-94 from their 1992 level, and thereafter to shift increasingly toward project assistance. Disbursements of balance of payments assistance from other donors are assumed to fall gradually by 1997 to about one-fourth of their 1992 level, while project and commodity assistance (all grants) is assumed to remain constant in real terms at the levels of 1994. Gross international reserves are targeted to reach the equivalent of three months' imports by end-1994 and to grow sufficiently to maintain that relationship in subsequent years.

In Scenario A, the volume of nonmetal exports is assumed to grow by 10 percent per year in 1993-94 (with some allowance also for a recovery in electricity exports in 1993) and by 9 percent a year thereafter. Import requirements of the nonmining sector are assumed to grow in line with real GDP, with an elasticity of 0.8. The scenario envisages debt relief from Paris Club creditors in 1992-94 with the "enhanced concessions" currently provided in reschedulings for low-income countries, and thereafter through the continuous rescheduling of all obligations on pre-cutoff-date debt, with comparable debt relief from other nonmultilateral creditors. On this basis, Scenario A shows a residual financing gap of US$4.1 billion in 1993-2006, concentrated in the period 1999-2005, the period of repurchases of the encashed rights. The ratio of debt service obligations (excluding arrears) to receipts from exports of goods and nonfactor services falls from 61 percent in 1992 to 33 percent in 1997. The debt service ratio then rises to an average of 55 percent in 1999-2004 before falling again to 31 percent by 2006. During the period of peak financing requirements, Zambia's financial obligations to the Fund are projected to average 14 percent of receipts from exports of goods and nonfactor services, 50 percent of quota, and 51 percent of gross international reserves.

Scenario B shows the impact of 10 percent higher world copper prices during the period 1994-2006. In this scenario, the residual financing gap for 1993-2006 is reduced to US$3.0 billion and the debt service ratio is roughly 3 percentage points lower, on average, than in Scenario A.

Scenario C demonstrates an illustrative mix of additional efforts required to eliminate the residual financing requirement (along the lines of Scenario F presented in EBS/91/59). These include: (i) a 1 percentage point increase in the annual growth rate of nonmetal export volume over the period 1995-2006, which would reduce the cumulative financing requirement for 1993-2006 by US$500 million from the level implied by Scenario A; (ii) a reduction of percentage point a year in the growth rate of imports by the nonmining sector, which would reduce the cumulative gap by US$1.0 billion; (iii) the provision of all Fund resources under a successor arrangement on ESAF terms, with continued Fund financial support following the encashment of accumulated rights, which would lower the cumulative gap by US$400 million; and (iv) complete forgiveness of pre-cutoff-date debt by nonmultilateral creditors, which would reduce the cumulative gap by US$2.2 billion. The debt service ratio would fall to 13-14 percent in 1998-99, rise temporarily to 32 percent in 2000-2005, and fall again to 15 percent by 2006.

Table 1. Zambia: Long-Term Balance of Payments Scenarios, 1993-2006

(In millions of U.S. dollars)

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	1993-2006 Total
Current account balance 1/															
Scenario A	-296	-272	-345	-327	-322	-358	-414	-473	-533	-573	-591	-606	-619	-630	-6,359
Scenario B	-296	-209	-274	-253	-243	-281	-346	-413	-483	-527	-544	-558	-569	-578	-5,574
Scenario C	-296	-272	-336	-309	-291	-314	-355	-396	-437	-454	-446	-432	-411	-383	-5,132
Scheduled debt service obligations 2/															
Scenario A	-652	-641	-570	-494	-438	-492	-584	-713	-801	-770	-735	-752	-641	-534	-8,817
Scenario B	-652	-640	-565	-486	-427	-478	-566	-692	-777	-743	-705	-719	-605	-494	-8,549
Scenario C	-346	-348	-260	-230	-203	-200	-188	-302	-448	-487	-488	-502	-385	-247	-4,634
Gross reserve accumulation															
Scenario A	-30	-30	-15	-16	-17	-12	-7	-8	-8	-15	-23	-25	-27	-28	-261
Scenario B	-30	-30	-15	-16	-17	-12	-7	-8	-8	-15	-23	-25	-27	-28	-261
Scenario C	-30	-30	-13	-15	-15	-10	-5	-5	-5	-12	-20	-21	-22	-23	-226
Reduction of Fund arrears	-88	--	-1,172	--	--	--	--	--	--	--	--	--	--	--	-1,260
Assumed new disbursements	731	670	640	581	595	609	653	677	702	728	755	783	812	842	9,778
Use of Fund resources															
Scenarios A and B		----	1,172	--	--	--	--	--	--	--	--	--	--	--	1,172
Scenario C		----	1,172	151	151	--	--	--	--	--	--	--	--	--	1,474
Debt relief															
Scenario A	246	226	190	131	97	100	93	86	85	85	85	79	80	78	1,661
Scenario B	246	226	190	131	97	100	93	86	85	85	85	79	80	78	1,661
Scenario C	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--
Residual balance (gap -)															
Scenario A	-89	-47	-100	-125	-85	-153	-259	-431	-555	-545	-509	-521	-395	-272	-4,086
Scenario B	-89	17	-24	-43	5	-62	-173	-350	-481	-472	-432	-440	-309	-180	-3,033
Scenario C	-29	20	31	178	237	85	105	-26	-188	-225	-199	-172	-6	189	--
Memorandum items:															
Debt service ratio 3/															
Scenario A	57	55	49	40	33	36	44	55	64	60	53	51	41	31	48
Scenario B	57	52	46	37	30	34	41	51	59	56	50	47	37	28	45
Scenario C	32	32	24	19	15	14	13	22	35	38	36	34	25	15	25
Fund obligations															
Percent of exports 4/	8	9	6	4	3	7	10	16	21	16	12	11	5	--	9
Percent of reserves 5/	39	39	23	15	14	27	39	58	76	57	40	38	18	--	35
Percent of quota	25	28	17	12	12	24	35	53	71	56	42	42	21	--	31
Copper export volume ('000 metric tons)	390	400	400	400	400	375	325	275	225	200	200	200	200	200	299
Copper price (US$/lb)															
Scenarios A and C	0.94	0.90	0.86	0.91	0.96	0.99	1.02	1.05	1.08	1.12	1.15	1.18	1.22	1.26	1.05
Scenario B	0.94	0.90	0.94	1.00	1.06	1.09	1.12	1.16	1.19	1.23	1.26	1.30	1.34	1.38	1.14

Source: Staff estimates.

1/ Including obligations to Fund, but excluding payment of arrears. Assumes half of residual financing gaps are met on grant terms.
2/ Excluding interest obligations and official transfers.
3/ As percentage of receipts from exports of goods and nonfactor services.
4/ Scenario A; as percentage of receipts from exports of goods and nonfactor services.
5/ Scenarios A and B; as percentage of gross international reserves.

Zambia: Fund Relations

(As of June 30, 1992)

I. Membership Status: Joined September 23, 1965/Article XIV

A. Financial Relations

II. General Resources Account:

	SDR Million	% Quota
Quota	270.3	100.0
Fund holdings of currency	903.1	334.1
Reserve position in Fund	--	--
Operational budget transfers (net)	--	--

III. SDR Department:

	SDR Million	% Allocation
Net cumulative allocation	68.3	100.0
Holdings	2.6	3.8
Designation plan amount	--	--

IV. Outstanding Purchases and Loans:

	SDR Million	% Quota
Total	632.8	234.1
Stand-by arrangements	120.9	44.7
Extended arrangements	64.7	23.9
EAR	253.9	93.9
CCFF	193.4	71.5
SAF arrangements	--	--
ESAF arrangements	--	--

V. Financial Arrangements:

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
1. Stand-by	2/21/86	2/29/88	229.8	35.0
2. CFF	2/21/86	--	68.8	68.8

VI. Projected Obligations to Fund (SDR Million; Based on Existing Use of Resources Only):

	Overdue 6/30/92	Forthcoming 7/1/92-12/31/92	1993	1994	1995	1996
Principal	635.1	2.2	2.2	--	--	--
Charges/interest	285.6	25.8	51.2	51.1	50.7	49.8
Total	920.7	28.0	53.4	51.1	50.7	49.8

VII. Exchange Rate Arrangement

The exchange system consists of a dual exchange rate arrangement. The official exchange is determined by the Bank of Zambia with adjustments at weekly intervals. It covers imports under the OGL system, government transactions, ZCCM, Zambia Airways, and the state oil company. Virtually all other foreign exchange transactions are under the retention market, where the exchange rate is market determined. On June 30, 1992 the official exchange rate was K 160.0 = US$1 and at the average retention rate, K 210 = US$1.

VIII. a. The dates and composition of missions to discuss the 1992 Article IV consultation and the rights accumulation program for 1992 were:

1. February 15-24, 1992. Ms. Dillon (head-AFR), Messrs. Nowak (AFR), Brown (ETR), Gordon (AFR), and Mrs. Saunders (assistant-STA). Ms. Kirmani, the Fund's resident representative in Lusaka, also participated in the discussions.

2. May 22-June 11, 1992. Ms. Dillon (head-AFR), Messrs. Nowak, Katz (AFR), Mr. Brown (ETR), Mr. McCarten (FAD), Mr. Gordon (AFR), and Ms. Duane (assistant-AFR). Mr. Hill, the resident representative in Lusaka, participated in the discussions, as did Mr. Mwananshiku.

b. Zambia is on a 12-month Article IV consultation cycle; the last Article IV consultation was concluded by the Executive Board on April 17, 1991. The following decisions were adopted:

1. The Fund takes this decision relating to Zambia's exchange measures subject to Article VIII, Section 2(a) and 3, in concluding the 1991 Article XIV consultation with Zambia conducted under Decision No. 5392-(77/63), adopted April 29, 1977, as amended (Surveillance over Exchange Rate Policies).

2. As described in EBS/91/59, Zambia continues to maintain restrictions on the making of payments and transfers for current international transactions in accordance with Article XIV, except that the following exchange measures maintained by Zambia are subject to Fund approval under Article VIII; multiple currency practices arising from the operation of the dual exchange market and from the sale of retained export proceeds; limitations on the availability of foreign exchange for certain current transactions, including limitations on personal remittances and the nonavailability of foreign exchange for tourism; and the limitation on the availability of foreign exchange for the servicing of external debt evidenced by payments

arrears. The Fund approves the retention of the multiple currency practice arising from the operation of the dual exchange market until December 31, 1991. The Fund encourages the authorities to remove as soon as possible the other exchange restrictions and the other multiple currency practice.

IX. Technical Assistance

The Central Banking Department has furnished the Bank of Zambia with a research advisor (February 1983-February 1984), an external debt advisor (November 1983-November 1984), an economic advisor to the Governor (appointed October 1983), and, since late 1990, a head of the Banking Supervision, an advisor in the Banking Department, and an advisor in the Research Department.

Technical assistance missions from the Fiscal Affairs Department visited Zambia March 25-April 9, 1984, May 13-20, 1986, april 25-May 16, 1989, and May 14-June 1, 1990. Missions from the Bureau of Statistics visited Lusaka twice in 1985, once in 1986, and most recently in December 1989 to review government and banking data.

X. Resident Representative

A Fund resident representative took up position in Lusaka in June 1990. Since May 1992 the Fund resident representative is John Hill. Previously, the Fund had a resident representative stationed in Lusaka between November 1983 and July 1987.

World Bank Group Relations with Zambia

1. The World Bank Group has provided over 55 loans and credits to Zambia since 1956, with total commitments amounting to over US$1,100 million. These commitments have financed operations in several areas, including energy, transportation, communications, rural water supply, secondary and higher education, teacher training and technical education, commercial and small-holder agriculture (commercial crops, family farming, coffee production, dairying, integrated rural development), industrial forestry, and fisheries. Other loans and credits have supported the country's mining and manufacturing sectors and the urban sector. Two program loans were approved in the early 1970s, and three adjustment credits were approved in the period 1985-86. Disbursements were suspended in May 1987 when Zambia abandoned the reform program and stopped paying debt service. Adjustment lending resumed after clearance of arrears in early 1991, and the latest adjustment operations was approved in June 1992. A free-standing technical assistance (TA) credit was approved in 1978 to help the Government improve its planning and project preparation; a second TA credit was approved in 1986 to support improvements in economic management; and a third was just recently approved to assist in parastatal reform and privatization. The International Finance Corporation (IFC) has provided nine loans and six equity participations in support of private enterprise activities, including food production and processing, shoe manufacturing, packaging and plastic wrap, textiles, tourism, mining, and development finance.

2. The main elements of the Bank's strategy are to support efforts to:

- achieve macroeconomic stability and initiate a path of sustainable and equitable growth through elimination of the budget deficit, attaining a competitive exchange rate, and increasing the allocation of resources to economic and social sectors by restructuring the composition of public expenditure;

- ensure sufficient access to imports, and an adequate reserve cushion, through maintenance of an appropriate exchange rate and other measures to encourage exports and to use imports wisely, and through coordination of donor assistance and efforts to secure needed debt elimination and rescheduling;

- improve the climate for private sector development through deregulation, provision of infrastructure, and privatization of parastatals;

- strengthen human resource capacity by rehabilitating the education and health infrastructure and improving the quality of education and health services; and

- implement an effective environmental strategy.

World Bank Group Relations with Zambia (continued)

3. In the context of this strategy, the Bank is providing urgent support to mitigate the effects of this year's drought. Thus, the allocation for the most recent policy adjustment credit was increased from $100 million to US$200 million, and some existing operations are being revised to provide funding for drought-related activities. The Bank is also actively coordinating donor support for Zambia. The most recent Consultative Group meeting was held in Paris in March 1992.

4. Zambia's withdrawal rights under Bank loans and IDA credits were suspended on May 1, 1987 because of arrears on obligations owed to the Bank. On March 5, 1991, the Bank approved, subject to the clearance of arrears, an Economic Recovery Credit (and suplemental IDA Reflows) in the amount of SDR 169 million (US$237 million). On March 13, 1991 Zambia cleared all its arrears to the World Bank and IDA, and disbursements resumed. Policy slippage in mid-1991, particularly on maize pricing, led to a withdrawal of donor support, nonpayment of debt service, and a second suspension of disbursements in September. Following the elections in October, agreement was reached with the new government, the new arrears were cleared, and disbursements resumed in late January 1992. Accordingly, the Bank's loans to Zambia are no longer in nonaccrual status, and the Bank has ended its suspension of new lending and of disbursements of previously approved IBRD loans and IDA credits. A summary of Bank Group financial relations with Zambia is presented below.

World Bank Group Relations with Zambia (concluded)

Zambia: Status of Bank Group Operations

(In millions of U.S. dollars; as of March 28, 1991)

Loan or Credit No.	Fiscal Year	Borrower	Purpose	Bank	IDA	Undis-bursed	Closing Date
				(Amount in US$ million, less cancellations)			
Credits							
12 Credits closed					467.76		
C14370-ZAM	1984	Zambia	Forestry III		22.40	7.79	09/30/92(R)
C15290-ZAM	1985	Zambia	Fisheries		7.10	7.73	12/31/91(R)
C15750-ZAM	1985	Zambia	Railways IV		20.00	23.85	06/30/92(R)
C16790-ZAM	1986	Zambia	Technical Assistance II		8.00	6.96	12/31/92
C17430-ZAM	1987	Zambia	Coffee II		20.40	22.48	06/30/95
C17460-ZAM	1987	Zambia	Agriculture		13.00	13.29	12/31/95
C17530-ZAM	1987	Zambia	DBZ III		10.00	11.37	06/30/92
C22690-ZAM	1991	Zambia	Mining Technical Assistance II		21.00	20.37	06/30/97
C22730-ZAM	1991	Zambia	Social Recovery Project		20.00	16.16	07/31/97
Total number Credit = 9					141.90	130.00	
Loans							
28 Loans(S) closed				582.13			
All closed for Zambia							
Total number loans = 0							
	Total*			582.13	609.66		
	Of which: repaid			355.58	1.06		
	Total held by Bank and IDA			226.55	608.60		
	Amount sold		28.58				
	Of which: repaid		28.58				
	Total undisbursed					130.00	

Notes:

* Total approved, repayments, and outstanding balance represent both active and inactive loans and credits.
(R) Indicates formally revised closing date.
(S) Indicates SAL/SECAL loans and credits.
The net approved and bank repayments are historical value, all others are market value.

The signing, effective, and closing dates are based upon the Loan Department official data and are not taken from the Task Budget file.

ZAMBIA - Basic Data

Area, population, and GDP per capita

Area	752,600 square miles
Population	
Total (1990 estimate)	8.1 million
Growth rate	3.7 percent
GDP per capita (1990)	SDR 310

	1986	1987	1988	1989	1990 Est.	1991 Est.
Gross domestic product and expenditure (at current market prices) 1/			(In millions of kwacha)			
Gross domestic product	12,963	19,778	30,021	60,025	127,400	246,778
Agriculture	(1,578)	(2,180)	(5,056)	(10,562)	(...)	(...)
Mining	(2,355)	(2,689)	(3,155)	(7,720)	(...)	(...)
Manufacturing	(2,936)	(5,547)	(9,496)	(2,705)	(...)	(...)
Government services 2/	(1,169)	(1,488)	(2,171)	(2,705)	(...)	(...)
Other sectors	(4,925)	(7,874)	(10,143)	(17,105)	(...)	(...)
Gross domestic expenditure	13,120	18,961	27,820	57,310	128,290	250,482
Consumption	(10,033)	(16,219)	(24,407)	(51,372)	(108,707)	(217,211)
Investment	(3,087)	(2,742)	(3,413)	(5,964)	(19,583)	(33,270)
External resource gap (-) or surplus (+) at market prices	-156	818	2,201	2,689	-891	-3,704
			(In percent of GDP)			
Consumption	77.4	82.0	81.3	85.6	85.3	88.0
Investment	23.8	13.9	11.4	9.9	15.4	13.5
External resource gap (-) or surplus	-1.2	4.1	7.3	4.5	-0.7	-1.5
Prices (period averages)			(In percent)			
GDP deflator	82.0	48.6	46.4	118.4	113.3	97.3
CPI (low-income)	54.0	45.7	54.7	128.8	111.0	92.6
CPI (high-income)	60.1	56.4	50.2	125.4	100.2	98.6
CPI (composite)	54.8	47.1	54.0	128.3	109.6	93.4
Government finance			(In millions of kwacha)			
Revenue and grants	3,206	4,371	5,628	11,535	27,926	58,087
Expenditure and net lending	6,699	6,327	9,087	17,294	37,340	75,708
Current	5,198	5,661	7,560	12,687	29,181	56,840
Capital and net lending	973	653	1,365	2,801	7,059	17,857
Overall deficit (accrual basis) (-)	-3,493	-1,955	-3,459	-5,759	-9,414	-17,620
Overall deficit (cash basis) (-) 3/	-2,468	-983	-2,601	-4,169	-3,580	-17,700
Financing	2,468	983	2,601	4,169	3,580	17,700
External	1,310	-54	1,220	621	1,617	4,812
Domestic	1,159	1,038	1,381	3,548	1,963	12,888
Banking system (net)	(594)	(125)	(1,253)	(2,099)	(2,270)	(11,179)
Other 4/	(565)	(913)	(128)	(1,449)	(-307)	(1,709)
Overall accrual deficit/GDP (%)	-26.9	-9.9	-11.5	-9.6	-7.4	-7.1
Money and credit (end of period)						
Foreign assets (net)	-9,348	-8,242	-7,259	-5,527	-544	-4,182
Net domestic credit (net)	5,374	6,274	9,658	15,338	19,783	55,229
Claims on the Government (net)	(3,487)	(3,778)	(5,201)	(6,489)	(5,584)	(30,938)
Claims on the private sector	(1,888)	(2,497)	(4,457)	(9,049)	(14,199)	(24,291)
Money and quasi-money (M2)	4,062	6,266	10,126	16,729	24,390	48,451
Money (M1)	(2,304)	(3,225)	(5,245)	(7,950)	(12,548)	(22,468)
Balance of payments			(In millions of SDRs)			
Exports, f.o.b.	596	671	859	1,098	931	792
Of which: copper	(489)	(569)	(731)	(960)	(777)	(656)
Imports, c.i.f.	-581	-597	-661	-796	-799	-695
Trade balance	15	74	199	301	132	97
Services (net)	-301	-319	-369	-451	-397	-424
Transfers (net)	85	58	48	34	177	328
Current account balance	-201	-187	-122	-116	-88	1
Capital account (net)	-201	-165	-147	-82	-238	-40
Medium- and long-term flows	(-33)	(-163)	(-109)	(-87)	(-110)	(-15)
Short-term and errors and omissions	(-168)	(-1)	(-38)	(5)	(-128)	(-26)
Overall surplus or deficit (-)	-402	-351	-270	-198	-326	-40

Sources: Central Statistical Office; Bank of Zambia; and staff estimates.

1/ Central Statistical Office estimates up to 1989 and staff estimates thereafter.
2/ Includes public administration, defense, and economic and social services.
3/ Overall deficit after interest relief and arrears.
4/ Includes nonbank holdings of treasury bills, float items, and other misclassified items.

Social and Demographic Indicators - Zambia

Area

752,600 square kilometers

Population characteristics (1990)

Population density:	11 per sq. km.
Urban population (percent of total)	50
Proportion in capital city as a percentage of urban population	24
Population age structure (percent):	
0-14 years	49
15-64 years	49
65 and above	2

Income distribution (1973)

Percent of national income,	
highest quintile	63
lowest quintile	4

Access to safe water (1987)

Percent of population - urban	76
- rural	41

Nutrition (1989)

Per capita calorie intake per day	2,077

Population (1990)

8.1 million
Annual rate of growth: 3.7 percent

Health

Life expectancy at birth (1990)	50
Infant mortality (aged under 1, percent) (1990)	8.2
Population per physician (1984)	7,150
Population per nursing person (1984)	740

GDP per capita (1990)

In SDRs	310

Labor force (1987)

Female (percent)	29
Agriculture (percent)	73
Industry (percent)	10

Education (1989)

Percent of age group:	
Primary school enrollment	95
Secondary school enrollment	20
Enrollment in tertiary educaiton	2

Source: World Bank, World Development Report, 1992.