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October 1, 1985

To: Members of the Executive Board

From: The Acting Secretary

Subject: Zambia - Staff Report for the 1985 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1985 Article IV consultation with Zambia. A draft decision appears on page 26.

This subject will be brought to the agenda for discussion on a date to be announced.

Mr. Muzonda (ext. 8969) or Mr. Greene (ext. 8754) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

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INTERNATIONAL MONETARY FUND

ZAMBIA

Staff Report for the 1985 Article IV Consultation

Prepared by the Staff Representatives for the 1985 Article IV Consultation with Zambia

Approved by A.D. Ouattara and S. Kanesa-Thasan

October 1, 1985

I. Introduction

The 1985 Article IV consultation discussions with Zambia were begun in Lusaka during April 15-May 2, 1985. The Zambian representatives included the Minister of Finance, Mr. L. Mwananshiku; the Governor of the Bank of Zambia, Mr. D. Phiri; and other senior officials concerned with economic and financial matters. The staff representatives were Messrs. A.C. Woodward (head), T. Muzondo, J. Greene (all AFR), J. Diamond (FAD), E. Zervoudakis (ETR), and Ms. D. Heflin (secretary-AFR). Mr. J. Paljarvi, the Fund resident representative in Zambia, also participated in the discussions. The Article IV consultation discussions were concluded in Washington, D.C., during June 12-14, with a Zambian delegation consisting of the Minister of Finance, the Governor of the Bank of Zambia, and other senior officials. 1/

The last Article IV consultation with Zambia was concluded by the Executive Board on July 18, 1984. Zambia continues to avail itself of the transitional arrangements of Article XIV.

A summary of Zambia's relations with the Fund is provided in Appendix I. Statistical issues are discussed in Appendix III, and basic economic and financial data are presented in Appendix IV.

On July 18, 1984 the Executive Board approved in principle a 21-month stand-by arrangement for Zambia in the amount of SDR 225 million (equivalent to 47.5 percent of quota on an annual basis). The arrangement was activated on July 26, 1984 after a Paris Club debt rescheduling agreement assured adequate financing to meet Zambia's balance of payments gap. Three purchases totaling SDR 80 million were made under the arrangement, the last of which was on December 3, 1984, following the

1/ Subsequently, a joint Fund-Bank team visited Lusaka for technical discussions with the authorities on the technical aspects of the exchange rate and trade policy reforms considered in this report. The team comprised Messrs. Acquah (head-AFR), De Zoysa (FAD), Muzondo (AFR), Fisher (ETR), and Hansen and Kaufman (from the World Bank), with Miss Nepomuceno (secretary-AFR).

first review by the Executive Board on November 26 (EBS/84/229). Further purchases under the arrangement were subject to completion of the second review (before end-February 1985) and the reaching of understandings on an adjustment program for 1985. The review was not completed because understandings could not be reached on details and timing of needed economic policy adjustments. Moreover, the performance criterion relating to net bank credit to the Government for end-December 1984 was also not observed, and further purchases under the stand-by arrangement were interrupted.

There have been delays in the discharge by Zambia of its financial obligations to the Fund, which have prompted a report and complaints to the Board under Rule K-1 and Rule S-1 (EBS/85/80). As of August 31, 1985, Zambia's overdue obligations to the Fund were SDR 78.1 million, with additional payments of SDR 44.6 million due for the remainder of 1985. 1/ As of the end of August 1985, the Fund's holdings of Zambian kwacha subject to repurchase were SDR 693.3 million (the equivalent of 256.6 percent of quota), including the overdue repurchases and SDR 183.1 million (67.7 percent of quota) under the compensatory financing facility.

Zambia is one of the countries in Africa singled out for "enhanced collaboration" between the Fund and the World Bank to ensure that both institutions have the same aims and priorities. The staff of both institutions have been in regular consultation in seeking solutions to Zambia's extremely difficult economic problems. Following a period of relatively low Bank activity and divergences of views between Zambia and the Bank on investment priorities in the late 1970s, there has been a significant increase in Bank project lending and regular economic policy dialogue between the Bank staff and the Zambian authorities. The Bank Board has approved a series of agricultural development projects for Zambia since 1980, and in early 1984 it approved an export rehabilitation loan for the mining sector in an amount of US$75 million. The Bank also collaborated closely with the Zambian authorities in preparing an investment program that was submitted to a Consultative Group meeting in May 1984 and the follow-up package on outlines of economic policy reforms submitted to a Consultative Group meeting in June 1985. In January 1985 the Bank approved an agricultural sector credit amounting to US$25 million, and it is also discussing a possible industrial sector credit for an amount of SDR 75 million to be financed mainly from the Special Facility for Sub-Saharan Africa (the African Facility). As of end-December 1984 total outstanding disbursements of the World Bank Group to Zambia amounted to US$390.7 million; there have been delays by Zambia in making payments on these obligations. Zambia's relations with the World Bank Group are summarized in Appendix II.

1/ On September 12, 1985 a payment of SDR 2.0 million was made, fully settling the overdue net SDR charges, and the complaint under Rule S-1 was withdrawn; on September 20, 1985 a further payment of SDR 1.8 million was made.

II. Economic Background

Since the mid-1970s Zambia's economic performance has sharply deteriorated, largely because of declining prices of copper, which accounts for over 90 percent of exports. Over the past decade, the real purchasing power of Zambia's exports has fallen steadily by about 70 percent, and real per capita income has declined markedly. In the face of this large deterioration in the external terms of trade, the policies adopted by the authorities have not been adequate to sufficiently reduce domestic absorption or to diversify the export base of the economy. The resulting external payments gaps have been financed by the very substantial increase in external debt and the accumulation of external payments arrears. Between 1980 and 1984 the net increase in medium- and long-term debt amounted to SDR 1.7 million. As a result, the scheduled debt service obligations have risen sharply, and were estimated to have been equivalent to some 69 percent of exports of goods and services in 1984. Since 1978 there have been periodic adjustment efforts, supported by the use of Fund resources. However, these efforts have not been sustained enough to counter the pressures emanating from the continued downward trend in copper prices. The deterioration in the economic and financial situation was particularly marked in 1982, when a period of lax financial management followed cancellation of an extended arrangement from the Fund.

In 1983 the Government initiated a more far-reaching adjustment program supported by a one-year stand-by arrangement in the amount of SDR 211.5 million (equivalent to 100 percent of quota at that time). The program aimed at diversifying the Zambian economy and reducing its overdependence on imports. Between the last quarter of 1978 and the fourth quarter of 1982 the real effective exchange rate of the kwacha appreciated by 21.8 percent. Under the program, the kwacha was devalued in January 1983 by 20 percent against the SDR to which it was pegged until July 1983 when the peg was switched to a basket of currencies. After this, the authorities followed a policy of flexible exchange rate management. Between January and December 1983 the kwacha was thus depreciated by 15.4 percent in nominal effective terms, but with comparatively high domestic inflation, however, the depreciation amounted to only 4.2 percent in real effective terms (Chart). Despite these adjustments, by the end of 1983 the real exchange rate had returned to broadly the same level as the last quarter of 1978. In 1983 there was a general decontrol of wholesale and consumer prices, a significant reduction of budgetary subsidies on basic foodstuffs and fertilizer through sharp price increases (ranging from 30 percent to 60 percent), and adjustments in agricultural producer prices. Public enterprises were allowed greater freedom in the exercise of their corporate responsibilities, with a view to improving efficiency and allocation of resources. Fiscal policy was also tightened through a combination of a virtual freeze on total expenditure and an increased tax effort. The central government budget deficit, measured on a commitment basis, was reduced to K 319.7 million (about 7.6 percent of GDP) in 1983, from K 521.5 million (14.6 percent of GDP) in 1982 (Table 1). Accordingly,

Table 1. Zambia: Selected Economic and Financial Indicators, 1982-85

	1982	1983		1984			1985
		Rev. prog. 1/	Actual	Orig. prog. 1/	Rev. prog. 1/	Est.	Proj.
		(Annual percent changes, unless otherwise specified)					
National income and prices							
GDP at constant prices	-2.8	--	-2.0	--	--	-1.3	...
GDP deflator	6.1	25-30	18.7	25	25	14.7	...
Consumer prices	12.5	25-30	19.6	25	25	20.0	44.3 2/
External sector (on the basis of SDRs)							
Exports, f.o.b.	-2.8	14.5	6.4	-10.3	-14.7	-6.8	8.8
Imports, c.i.f.	3.2	-19.8	-25.2	-11.2	-12.3	-10.0	6.1
Non-project imports, c.i.f.	20.2	...	-25.3	-25.0	-25.6	-7.7	1.7
Export volume	9.3	1.8	-6.5	-4.0	-4.0	-2.8	1.3
Import volume	-4.0	-17.0	-27.6	-9.5	-9.7	-13.5	4.2
Terms of trade (deterioration, -)	-14.5	9.0	10.2	-7.4	-11.9	-12.9	6.6
Nominal effective exchange rate (depreciation, -) 3/	-6.4	...	-18.1	...	...	-23.7	...
Real effective exchange rate (depreciation, -) 3/	9.9	...	-9.0	...	...	-14.4	...
Government budget							
Revenue and grants	4.2	22.3	23.1	15.5	15.0	8.6	24.2 4/
Total expenditure	8.8	-6.7	-0.7	7.3	12.8	11.4	17.9 4/
Money and credit							
Net domestic assets 5/	75.3	23.7	22.8	23.9	23.9	13.4	5.0 2/
Government 5/	49.9	11.4	8.8	12.0	12.0	13.1	10.1 2/
Money and quasi-money (M2)	33.8	12.5	10.2	15.4	15.4	18.0	16.1 2/
Velocity (GDP relative to M2)	2.5	2.7	2.9	3.1	3.1	2.8	...
Interest rates:							
Treasury bill rate	6.0	7.5	7.5	...	...	10.0	9.5 6/
Discount rate	7.5	...	10.0	...	...	14.5	14.5 6/
Maximum lending rate	9.5	...	13.0	15.0	17.5	17.5	17.5 6/
		(In percent of GDP)					
Central government budget deficit							
Including official transfers (commitment basis)	14.6	5.6	7.6	4.5	5.2	8.1	...
Including official transfers (cash basis)	18.9	5.6	7.4	4.5	5.2	7.3	...
Excluding official transfers (cash basis)	19.7	6.3	8.7	5.3	6.8	8.8	...
Domestic bank financing	13.7	4.2	2.7	3.3	3.3	4.0	...
Foreign financing	3.1	0.3	2.4	-0.3	0.4	1.3	...
Gross domestic investment	16.8	...	13.8	15.5	15.5	14.0	...
Current account deficit							
Excluding official transfers	18.4	8.0	9.0	11.6	13.0	11.6	...
External debt 7/	88.8	...	109.2	...	...	150.8	...
Debt service ratio 8/							
Before debt relief	56.4	60.9	59.4	91.6	83.5	68.7	...
After debt relief	56.4	50.8	49.6	42.1	47.8	41.8	...
Actual payments	34.3	...	29.1	...	...	34.1	...
		(In millions of SDRs, unless otherwise specified)					
Overall balance of payments							
Before debt relief	-546	...	-390	-761	-727	-671	-699
After debt relief	-546	...	-293	-394	-410	-427	...
Gross official reserves (weeks of imports)	6.3	7.8	7.3	7.5	7.5	4.1	...
External payments arrears 9/	725	657	597	597	620	568	...
External arrears on debt service	197	--	310	-38	--	150	...

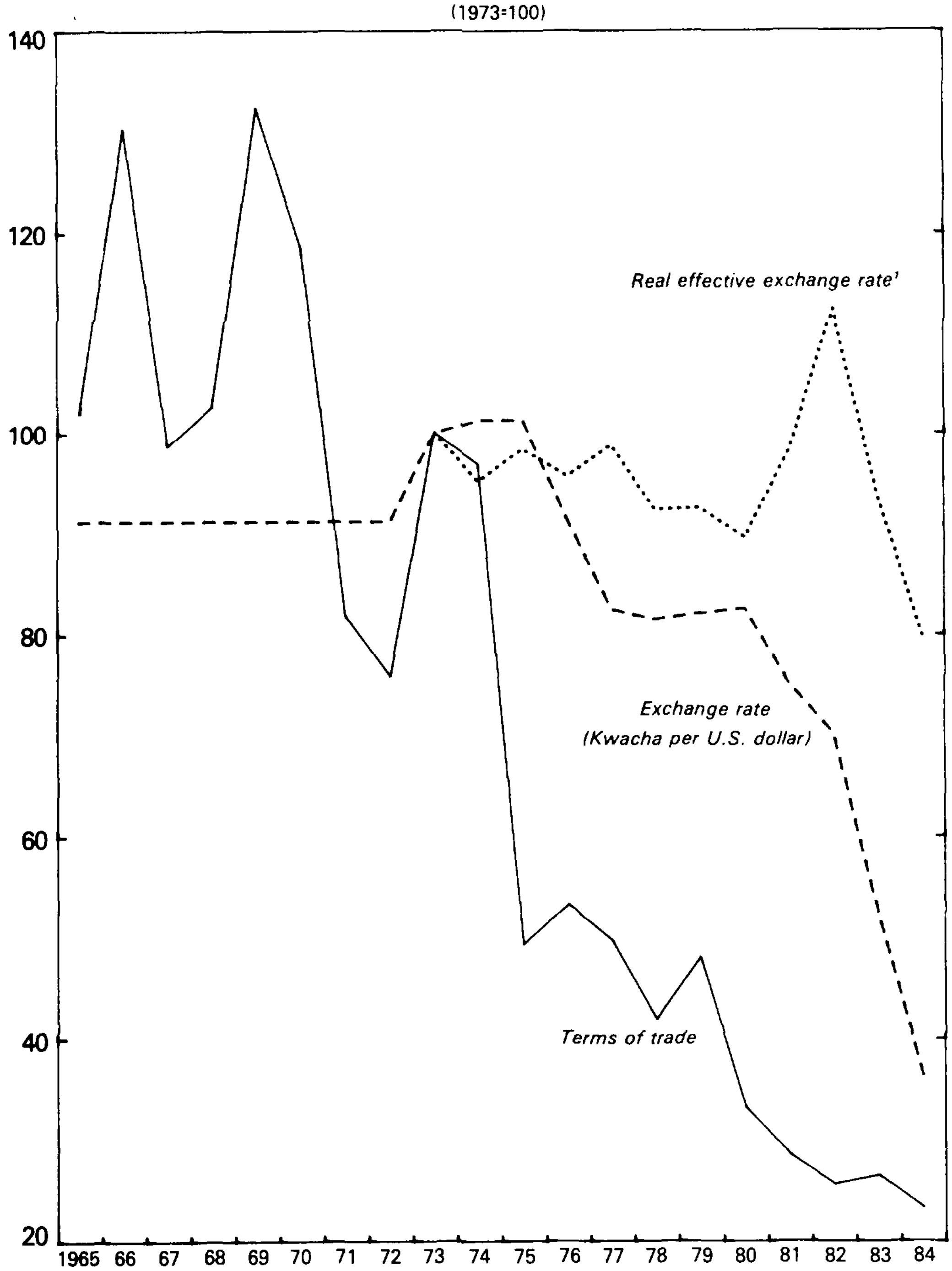
Sources: Data provided by the Zambian authorities; and staff projections.

1/ Basic ratios and indicators are those specified in EBS/83/67, EBS/84/135, and EBS/84/229.
2/ End-June annual percent changes.
3/ Annual average; Information Notice Systems index.
4/ Budget estimates.
5/ As a percentage of money and quasi-money at the beginning of the period.
6/ End-June percent per annum.
7/ Inclusive of use of Fund credit but excluding all external payments arrears.
8/ Scheduled debt service payments in percent of exports of goods and nonfactor services; including interest on short-term debt.
9/ Consists of commercial payments arrears, including arrears of the mining company.

ZAMBIA

TERMS OF TRADE AND EXCHANGE RATE, 1965-84

(1973=100)



Sources: International Financial Statistics; Zambia– Recent Economic Developments (June 1984), and staff estimates
[1]Series begins in 1973.

the net domestic bank borrowing requirement of the Government was sharply curtailed in 1983 to the equivalent of about 9 percent of the beginning money stock of the year, from the equivalent of 50 percent in 1982. This contributed to a sharp slowdown in the expansion of domestic liquidity, with broad money growth easing downward to 10 percent.

External sector developments proved relatively more unfavorable than had been anticipated early in the year. A sharp and unexpected decline in copper prices during the second half of 1983 caused a large shortfall of SDR 110 million in export earnings relative to earlier projections for the year. Although a cutback in the volume of imports (by some 9 percentage points more sharply than was programmed) led to a compression of the current account deficit from the equivalent of 18.4 percent of GDP in 1982 to 9 percent, the imbalance still turned out to be larger (by SDR 20 million, or 1 percentage point of GDP) than was programmed. The combination of this development in the current account and unanticipated lower inflows of capital and official transfers produced another large overall balance of payments deficit (SDR 294 million) and intensified the pressures on Zambia's already precarious foreign exchange situation. Zambia accumulated arrears on external debt service obligations including payments arising from Paris Club rescheduling agreements, as well as additional external commercial payments arrears during 1983. Consequently, Zambia could not make the final purchase under the stand-by arrangement of SDR 67.5 million, which was scheduled for February-March 1984.

III. Performance and Developments in 1984 Under the Stand-By Arrangement

In July 1984 another stand-by arrangement was approved in support of a new program which aimed to build on the adjustment efforts initiated in 1983. For the period covering 1984, the program had as its main objective the consolidation of progress begun in 1983. It continued measures to correct domestic cost-price distortions, improve efficiency in the mining sector, and increase incentives for the diversification of economic activity.

During 1984, the Zambian authorities maintained the policy of steadily depreciating the kwacha against a basket of currencies. Between December 1983 and December 1984 the nominal effective exchange rate was depreciated by 21.6 percent, which was sufficiently rapid to bring about a further real effective depreciation of 8.9 percent. This depreciation was sufficient to return the mining industry to profitability, but still left substantial unsatisfied demand for foreign exchange.

Agricultural producer prices were increased by amounts ranging from 12 percent to 42 percent, and price controls were further liberalized, involving significant price increases (ranging from 15 percent to 83 percent) for a number of items, including petroleum products. Meanwhile, Zambia continued to work closely with the World Bank in the mining, agricultural, and industrial sectors, in efforts to reduce costs and increase efficiency in parastatal enterprises. These measures, together with continued wage restraint throughout the economy, were expected to improve the financial position of the nonfinancial public enterprises. However, the severe foreign exchange shortage, coupled with inadequacies in the import allocation system, adversely affected economic performance throughout the economy, and capacity utilization in industry remained well below efficient levels.

Preliminary data on developments in the real sector of the economy during the year indicated that real GDP declined in 1984 again, by 1.3 percent, for the third consecutive year, and that the economic recession was broad-based. The exception was in the agricultural sector, where real value added rose by nearly 10 percent, mainly because weather conditions improved and additional acreage was brought under cultivation in response to the higher producer price levels. The domestic rate of inflation as measured by the rise in the GDP deflator remained high at 14.7 percent, although modest in relation to the projected inflation rate (25 percent) for 1984 and the rate recorded in 1983 (18.7 percent), due to the increases in administered prices and the continued depreciation of the kwacha. However, the consumer prices rose only slightly faster in 1984 than in 1983 largely because of the improvement that occurred in the overall food supply situation, and the policy of strict wage restraint applied under the program. The rise of the index for low-income families remained stable at about 20 percent (19.6 percent in 1983), while the index for higher-income households rose somewhat faster by 20.8 percent in 1984 as against 17.7 percent in 1983.

Demand management in 1984 continued to focus on the central government budget with the emphasis on expenditure restraint while providing for an adequate level of productive expenditure. In the original program, the overall budget deficit (measured on a commitment basis and including official transfers) was to be reduced from 7.6 percent of GDP in 1983 to 4.5 percent of GDP in 1984, and to be financed mainly by net domestic bank credit of K 174.4 million (equivalent to some 12 percent of beginning broad money stock). With revenue and grants programmed to increase by 15.5 percent (or significantly below the rate of inflation), expenditure growth was to be limited to some 7.3 percent, with strict restraint to be applied on outlays on personal emoluments, recurrent departmental charges, and budgetary subsidies on maize and fertilizer along with a less ambitious capital expenditure program. However, the provisional budgetary outturn for 1984 indicates that revenue and grants increased by only 8.6 percent (as against the programmed 15.5 percent) in part because of significant shortfalls in collections from excise duties (mainly due to production difficulties at the domestic breweries) and the mineral export tax, and because of the lack of implementation of proposed adjustments in import duties, including the introduction of a minimum import duty of 10 percent on certain exempt items and a delay in changing the basis for taxation of imports from an f.o.b. to a c.i.f. valuation (Table 2). Meanwhile, total expenditure exceeded the budgetary appropriations by a wide margin because of overruns on capital

Table 2. Zambia: Central Government Operations, 1980-85

	1980	1981	1982	1983	1984 Budget	1984 Original program 1/	1984 Revised program 1/	1984 Prov. outturn	1985 Budget
	(In millions of kwacha)								
Revenue and grants	791.3	833.4	868.2	1,069.0	1,217.1	1,222.8	1,231.7	1,161.1	1,442.2
Tax revenue	684.5	727.8	744.3	940.9	1,062.5	1,071.2	1,026.4	991.1	1,262.5
Nontax revenue	83.1	83.1	96.1	75.2	112.7	109.7	125.2	100.9	103.9
Grants	23.7	22.5	27.8	52.9	41.9	41.9	80.1	69.1	75.7
Total expenditure and net lending	1,168.0	1,277.7	1,389.7	1,388.7	1,408.6	1,461.8	1,510.4	1,546.7	1,824.2
Current expenditure	1,045.3	1,148.6	1,162.1	1,190.8	1,238.6	1,311.5	1,338.5	1,280.3	1,571.8
Personal emoluments	247.2	320.4	356.3	403.0	433.4	437.4	438.3	456.6	460.8
Recurrent departmental charges	159.9	182.2	236.2	202.6	228.3	228.3	232.1	220.4	228.0
Subsidies	213.7	110.4	125.5	82.2	56.6	91.6	111.2	88.6	150.0
Constitutional and statutory payments	337.1	444.2	302.6	367.9	376.9	411.1	413.5	379.1	595.2
of which:									
External interest	(62.6)	(47.1)	(75.2)	(46.3)	(109.7)	(127.7)	(102.0)	(71.8)	(...)
Domestic interest	(64.2)	(70.6)	(74.4)	(147.5)	(103.8)	(120.0)	(145.0)	(144.3)	(...)
Other	(210.3)	(326.5)	(153.0)	(174.1)	(163.4)	(163.4)	(166.5)	(163.0)	(...)
Other payments	87.4	90.4	141.4	135.1	143.4	143.4	143.4	135.6	137.5
Capital expenditure	161.3	119.3	100.9	153.9	150.0	140.0	142.9	215.4	204.5
Net lending	-38.6	9.8	126.7	44.0	20.0	10.0	29.0	51.0	47.9
Overall deficit (commitments basis)	-376.6	-444.3	-521.5	-319.7	-191.5	-239.0	-278.7	-385.6	-382
Change in arrears (increase +)	33.0	-19	-153	9.4	--	--	—	39.9	--
Overall deficit (cash basis)	-343.6	-463.3	-674.5	-310.3	-191.5	-239.0	-278.7	-345.7	-382
Financing	343.6	463.3	674.5	310.3	191.5	239.0	278.7	345.7	382
External (net)	141.9	247.4	111.6	100.8	-13.3	-13.3	19.4	59.5	...
Gross borrowing	(178.1)	(278.6)	(193.0)	(154.0)	(57.9)	(57.9)	(71.9)	(127.6)	(70.2)
Amortization paid 2/	(36.2)	(31.2)	(81.4)	(53.2)	(71.2)	(71.2)	(52.5)	(68.5)	(...)
Domestic nonbank (net)	*41.7*	*52.0*	*38.9*	*81.0*	*64.9*	*77.9*	*84.9*	*97.5*	*70.0*
Domestic bank (net)	232.8	163.8	488.9	115.1	139.9	174.4	174.4	188.7	160.0
Other items (net)	-72.8	0.1	35.1	13.4	...	...	...	...	...
Memorandum items	(In percent)								
Annual growth rate of revenue and grants	27.5	5.4	4.1	23.1	13.9	15.5	15.2	8.6	24.2
Annual growth rate of expenditure	26.6	9.4	8.8	--	1.4	7.3	8.8	11.4	17.9
Overall deficit (commitment basis)/GDP	12.5	12.9	14.6	7.6	4.0	4.5	5.2	8.1	...
Overall deficit (cash basis)/GDP	11.4	13.4	18.9	7.4	4.0	4.5	5.2	7.3	...
Total expenditure/GDP	38.8	37.0	39.0	33.0	29.4	30.6	32.0	32.5	...
Bank financing/GDP	7.7	4.7	13.7	2.8	2.9	3.6	3.7	4.0	...
Bank financing/Total financing	67.7	35.4	74.5	37.1	73.1	73.0	62.7	54.6	20.9
Bank financing as percent of beginning broad money	28.0	18.1	50.0	8.8	9.7	12.1	12.1	13.1	9.4

Sources: Ministry of Finance, Financial Reports (Annual), 1979-84; Estimates of Revenue and Expenditure, 1985; and data provided by the Zambian authorities.

1/ The basic ratios and indicators are those specified in the programs in EBS/84/135 and EBS/84/229.
2/ Identified arrears on external amortization payments were K 58.7 million in 1984.

expenditure and net lending, although much of the additional capital spending was financed by external project aid and grants. Consequently, in 1984 the overall central government budget deficit (on a commitment basis) turned out to be an estimated K 385.6 million (or 8.1 percent in relation to GDP). Included in this deficit was an identified budgetary accumulation of external interest arrears of K 40 million; additional arrears of K 59 million was incurred as amortization payments on external debt obligations. Thus, although the deficit was financed on a much larger scale by external resources than was envisaged under the program and by accumulation of arrears, the Government's net use of domestic bank credit (K 189 million) still exceeded the ceiling by K 14 million established under the program, even before taking account of the drawdown of deposits made from the blocked account established for external debt service payments under the program.

In parallel with the above budgetary developments net domestic assets of the banking system rose by 11.1 percent in 1984 (only marginally exceeding the 10.8 percent target envisaged at the inception of the program, and the 7.7 percent ceiling established under the revised program), 1/ as private sector credit expansion remained broadly within the target range (Table 3). There was some acceleration in monetary growth (measured on a year-end basis) during 1984, with broad money increasing by 18 percent, as against a program target of just over 15 percent and a rise of 10 percent recorded in 1983. In May 1984, the authorities increased interest rates by an average of 2 percentage points, and in December, by a further 2.5 percentage points, thereby moving the maximum lending rate to 17.5 percent and the short-term deposit rates and the Treasury bill rate to 11 percent and 9.5 percent, respectively. Short-term lending rates were more than doubled from 7 percent to 15 percent. However, when these adjustments are viewed against the background of increasing inflation they fall far short of the authorities' objective of achieving positive real interest rates.

Zambia's external position remained very difficult during 1984. The original external sector objective established early in the year was to contain the overall balance of payments deficit (before debt relief) to SDR 394 million in 1984. Exports were projected to amount to SDR 765 million, while the target import level was set at SDR 688 million, implying a decline of more than 12 percent in value and a much larger reduction in real terms in relation to the previous year (Table 4). This target took into consideration the minimum requirements of the mining sector critically necessary to avoid a downward spiral of falling output and export earnings. On this basis, a current account deficit of SDR 334 million (equivalent to 11.5 percent of the projected GDP) was projected for 1984. This gave rise to a financing gap of SDR 489 million (allowing for a programmed reduction of arrears) to be covered by a financing package including debt relief by Paris Club

1/ The program was revised during the first review in September 1984 (EBS/84/229)

Table 3. Zambia: Monetary Survey, 1983-85

	1983	1984							1985	
		March	June	Sept.	Sept.	Dec.	Dec.	Dec.	March	June
		Actual		Revised prog. 1/	Actual	Orig. 1/ prog.	Revised prog. 1/	Actual	Actual	
	(In millions of kwacha; end of period)									
Net foreign assets	-1,744.8	-1,872.5	-1,986.6	-2,006.8	-1,956.7	-2,181	-2,082.6	-2,142.3	-2,146.9	-2,150.8
Monetary authorities 2/	-1,166.2	-1,146.3	-1,226.3	--	-1,251.8	--	--	-1,397.3	-1,366.4	-1,354.7
Commercial banks	-13.1	-68.7	-80.3	--	-48.0	--	--	-55.6	-75.7	-113.4
Payments arrears 3/	-565.5	-657.5	-680.0	--	-656.9	--	--	-689.4	-704.8	-682.7
Net domestic assets	3,089.4	3,148.0	3,257.7	3,402.3	3,258.3	3,579.0	3,480.6	3,431.5	3,378.7	3,419.7
Claims on Government (net)	2,098.5	2,164.7	2,267.4	2,238.5	2,228.2	2,273.5	2,273.3	2,287.2	2,343.8	2,495.7
Claims on private sector	1,032.6	1,040.4	1,078.6	1,161.9	1,146.7	1,205.4	1,205.4	1,201.7	1,198.1	1,243.7
Of which: BOZ	(165.5)	(165.5)	(165.5	(165.5)	(165.5)	(165.5)	(165.5)	(165.5)	(165.5)	(160.5)
Other assets (net)	-41.7	-57.1	-88.3	1.9	-116.6	100.1	1.9	-57.4	-163.2	-319.7
Assets = Liabilities	1,344.6	1,275.5	1,271.1	1,395.5	1,301.6	1,398.0	1,398.0	1,289.2	1,231.8	1,268.9
Broad money	1,443.5	1,393.7	1,483.5	1,630.5	1,637.5	1,678.0	1,678.0	1,703.4	1,680.8	1,730.4
Money	782.6	696.1	732.8	--	890.3	--	--	866.8	857.8	941.4
Quasi-money	660.9	697.6	750.7	--	747.2	--	--	836.6	823.0	789.0
SDR allocation	87.4	97.4	97.4	87.4	97.4	97.4	97.4	120.7	120.7	120.7
Revaluation of official gold holdings	107.1	107.1	108.6	108.6	2.3	2.3	2.3	1.6	1.6	1.6
Revaluation gains/Losses on net foreign assets 4/	-293.4	322.7	-418.4	-431.0	-435.6	-379.7	-379.7	-536.5	-571.3	-583.8
Memorandum items:	(Percentage changes)									
Net domestic assets	5.3	7.0	9.9	9.2	4.6	10.8	7.7	11.1	7.3	5.0
Claims on government (net)	5.8	4.9	25.5	5.8	5.3	8.3	8.3	9.0	8.3	10.1
Credit to private sector	14.1	16.9	22.2	17.9	16.4	16.7	16.7	16.4	15.2	15.3
Net domestic assets (as percentage of broad money outstanding at beginning of period)	22.8	16.2	22.1	20.5	10.2	12.3	12.3	13.8	16.6	10.9
Claims on Government (net)	8.8	7.8	10.7	8.8	8.0	12.5	12.5	13.1	12.9	15.4
Credit to private sector	9.7	11.7	14.8	12.6	11.5	10.2	10.2	9.9	11.3	11.1
Broad money	10.2	9.1	12.0	16.6	17.1	15.4	15.4	18.0	20.5	16.6
Money	14.3	10.2	12.0	...	21.8	...	...	10.8	24.1	28.5
Quasi-money	5.4	8.0	12.0	...	12.0	...	...	25.6	18.0	-5.6
	(In percent)									
Broad money/GDP	41.4	...	...	...	...	35.5	35.5	36.0	...	...
Discount rate	10.0	10.0	12.0	...	12.0	...	...	14.5	14.5	14.5
Treasury bill rate	7.5	7.5	7.5	...	7.5	...	...	9.5	9.5	9.5
Maximum lending rate	13.0	13.0	14.5	...	14.5	...	...	17.5	17.5	17.5

Sources: Bank of Zambia; Quarterly Financial and Statistical Review; and staff estimates.

1/ Data have been revised to eliminate revaluation changes attributable to external commercial payments arrears. The absolute increase in net domestic assets during the program period as specified in EBS/84/135 has been preserved. Basic ratios and indicators are those specified in EBS/84/135 and EBS/84/229.

2/ Official gold holdings and other assets and liabilities (except IMF liabilities) are revalued at market-related prices on December 31 each year. The exchange rates used to convert foreign assets and liabilities into kwacha equivalents do not always reflect market valuation when the exchange rate is adjusted frequently. Liabilities to the IMF are converted at the rate ruling at the end of the Fund's financial year, while other liabilities and assets are revalued at the rate ruling at the relevant dates of transactions.

3/ These reflect the domestic counterpart on external payments arrears deposited by commercial banks with the Bank of Zambia. Local currency totals may not match the foreign exchange liabilities, as changes due to exchange rate movements are generally recorded only when the payments of external liabilities are made.

4/ Includes valuation losses on net foreign assets, and payments arrears. Data beginning in March 1983 are cumulative totals for Bank of Zambia foreign assets and liabilities thus far revalued, including Fund accounts and losses in respect of payments arrears as provided by the authorities.

Table 4. Zambia: Balance of Payments, 1982-89

	1982	1983	1984 Original prog. 1/	1984 Revised prog. 1/	1984 Revised estimate	1985	1986	1987	1988	1989
							Projection			
					(In millions of SDRs)					
Trade balance	-225	92	77	48	111	127	227	229	215	236
Exports, f.o.b.	824	877	765	728	817	876	1,021	1,099	1,129	1,195
Of which: copper	(722)	(778)	(638)	(599)	(668)	(702)	(798)	(830)	(863)	(897)
Imports, c.i.f.	-1,049	-785	-688	-680	-706	-749	-804	-870	-914	-959
Project-related and commodity aid	-353	-265	-293	-293	-226	-261	-289	-328	-341	-356
Petroleum	-193	-171	-141	-141	-138	-128	-134	-134	-134	-134
Other	-503	-349	-249	-246	-342	-360	-380	-408	-438	-469
Services (net)	-338	-333	-390	-402	-357	-445	-447	-508	-540	-566
Interest payments	-226	-236	-290	-302	-253	-350	-360	-419	-444	-466
Other (net)	-112	-97	-100	-100	-104	-95	-88	-89	-96	-100
Receipts	110	94	84	80	90	95	112	120	124	131
Payments	-222	-191	-184	-180	-194	-190	-200	-209	-220	-231
Unrequited transfers	-46	-17	-21	14	2	21	23	24	25	26
Private	-82	-51	-50	-50	-50	-50	-53	-53	-58	-61
Official	36	34	29	64	52	71	75	79	83	87
Current account	-609	-258	-334	-340	-244	-297	-197	-255	-300	-304
Nonmonetary capital	102	-57	-60	-70	-122	-143	-76	-47	-10	-21
Public sector (net)	59	5	-82	-78	-136	-208	-116	-87	-50	-61
Mining company (net)	43	-62	22	8	15	65	40	40	40	40
Other capital 2/	-60	29	--	--	-61	-50	--	--	--	--
SDR alloc./Gold reval.	21	-8	--	--	--	--	--	--	--	--
Overall balance	-546	-294	-394	-410	-427	-489	-273	-302	-310	-325
Financing	546	294	394	410	427	-245	-148	-181	-154	-64
IMF (net)	-52	60	74	74	74	-95	-148	-181	-154	-64
Purchases	34	174	148	148	148	--	--	--	--	--
Repurchases										
Other foreign assets (net) (increase -)	166	-11	-9	-1	15	--	--	--	--	--
Total debt relief	--	293	569	556	470	...	...	...	...	...
Scheduled obligations	--	96	367	317	244	...	...	...	...	...
Arrears	--	197	202	239	226	...	...	...	...	...
Arrears	432	-48	-240	-219	-132	-150	...	...	...	...
Incurrence/cash reduction (-)	432	149	-38	20	94	-30	...	...	...	...
Commercial payments	225	-50	--	58	25	-30	...	...	...	...
Rescheduled debt	--	38	-38	-38	8	...	...	...	...	...
Other external debt	207	161	--	--	61	...	...	...	...	...
Rescheduled	--	-197	-202	-239	-226	-120	...	...	...	...
Financing gap						734	421	483	464	389
Memorandum items:										
External payments arrears 3/	725	597	597	620	568	...	...	...	...	...
Nonmonetary capital (net)	102	-57	-60	-70	-122	-143	-76	-47	-10	-21
Disbursements	317	170	269	229	174	230	239	249	259	269
Amortization	-215	-227	-329	-299	-295	-373	-315	-296	-269	-291
Cumulative new disb.						230	469	718	977	1,246
							103	157	212	263
Interest on new disbs.			5.0%			33	17	30	42	56
Interest on financing gap			9.0%			33	86	127	169	208
Cumulative financing gap						734	1,167	1,651	2,115	2,504
Copper										
Volume (MT/000)	604	570	530	530	541	520	570	590	590	590
Price (SDR/lb)	0.61	0.68	0.65	0.61	0.61	0.66	0.69	0.71	0.74	0.77
					(In percent of exports of goods and services)					
Current account/GDP (percent)	-17.4	-10.2	-14.6	-14.8	-10.6	...	...	...	...	...
Scheduled debt service	56.4	59.3	91.6	83.5	68.7	83.1	71.6	72.2	61.0	60.5
Debt service after debt relief	56.4	49.4	38.4	44.3	41.8	...	...	...	...	...

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

1/ The basic ratios and indicators are those specified in the programs in EBS/84/135 and EBS/84/229.
2/ Including errors and omissions.
3/ Consists of commercial payments arrears, including arrears of the mining company.

creditors granted in July 1984 and an expected rescheduling of other eligible debt by other creditors.

The preliminary balance of payments results for 1984 show that total merchandise exports reached SDR 817 million, exceeding by 6.8 percent the initial export target of SDR 765 million, but remaining 7 percent below the 1983 level; it also was the lowest export level recorded in six years. Copper sales (SDR 668 million) surpassed (by more than 4 percent) the level assumed under the program; but this level of sales was achieved because of a rundown of existing copper stocks, as copper production declined. The price of copper continued to drop by about 10 percent in SDR terms from an average of SDR 0.7 per pound to SDR 0.61 per pound, and was 4 percent below the implicit U.S. dollar price assumed under the program. Export receipts for cobalt more than doubled in 1984 to SDR 73 million, while other exports rose by one third to SDR 46 million, a strong response to the improvement in export incentives offered by the kwacha depreciation and the export retention scheme introduced early in January 1984. 1/ However, imports exceeded the programmed level by nearly 4 percent, although the amount was some 10 percent lower than in 1983 and, in real terms, some 40 percent below the level attained in 1980. Combined with a slight improvement in the services account (mainly due to a downward revision of accrued interest payments), the trade developments contributed to an external current account deficit (before debt relief) of SDR 244 million (equivalent to 10.6 percent of the estimated GDP in 1984), which was significantly lower than programmed. However, whereas project-related imports financed almost exclusively from external resources did not reach the targeted level, other imports exceeded the programmed amount by some SDR 93 million, putting severe pressure on the external liquidity position. Moreover, there was relatively large unanticipated net capital outflow during the year, causing the overall balance of payments deficit (SDR 427 million) to exceed slightly the level programmed for 1984. Despite the rescheduling of a large amount of external debt obligations falling due in 1984, there was a further accumulation of external payments arrears.

Zambia's medium- and long-term external public debt amounted to an estimated SDR 3.5 billion at the end of 1984. Of this amount, about 48 percent was owed to bilateral official creditors, and 36 percent to multilateral institutions; the remainder represented commercial loans. In addition, Zambia had short-term debt estimated at SDR 175 million, and it had accumulated external payments arrears in an amount of SDR 920 million, of which SDR 568 million were commercial arrears. Thus, Zambia's total external indebtedness, including obligations to the Fund and the arrears, amounted to an estimated SDR 4.4 billion at the end of 1984. Zambia's scheduled debt service payments in 1984 were estimated at SDR 623 million, or equivalent to 69 percent of exports of

1/ The scheme allows exports of nontraditional goods to retain 50 percent of their export earnings for import payments related to their economic activity.

goods and services; amortization payments alone were estimated at SDR 370 million. In addition, there were some SDR 310 million of arrears on debt service payments at end-1983. Of the scheduled debt service payments, some SDR 201 million was owed to multilateral institutions, and SDR 226 million to Paris and London Club creditors. Actual debt service payments, including Fund repurchases and charges in 1984 amounted to SDR 310 million, or 34 percent of exports of goods and services.

Zambia reached an agreement on multilateral debt rescheduling under the auspices of the Paris Club in July 1984. The agreed minute provided for rescheduling of 100 percent of 1984 maturities, including interest falling due as a result of the previous year's Paris Club rescheduling; these were to be repaid over a period of ten years, with a five-year grace period. Arrears under the 1983 rescheduling agreement were, however, to be repaid over a shorter period--during the 12 months to end-July 1985. To meet these payments on schedule, the Government of Zambia undertook to make quarterly deposits of at least SDR 20 million (in monthly installments of at least SDR 5.7 million) in a special account established at the Federal Reserve Bank of New York. These deposits were intended to cover repayment of the arrears as well as for moratorium interest. Zambia's deposits into that account have so far amounted to less than SDR 10 million, of which less than half has been utilized for payments to creditors. By end-February 1985, the agreed deadline for concluding the rescheduling exercise with the Paris Club creditors, agreement had been reached with only seven out of the thirteen Paris Club participants. 1/ In 1984, Zambia also reached rescheduling agreements with three non-Paris Club official creditors--Yugoslavia, the German Democratic Republic, the U.S.S.R., and the London Club. The London Club agreement was signed in December 1984, after a long period of negotiations. It covered arrears of principal payments falling due during the period March 1983 to February 1985 and 90 percent of principal payments due during the remainder of 1985. The terms were broadly comparable to those accorded by countries participating in the Paris Club. As a result of these rescheduling agreements, estimated debt relief received by Zambia in 1984 totaled SDR 244 million, of which about one half represented obligations due to the Paris Club; and about a quarter was due to the London Club, the remainder being accounted for by the U.S.S.R., and certain other commercial creditors. In addition, an estimated SDR 226 million, representing about four fifth of the debt service arrears outstanding at end-1983, was rescheduled during 1984.

1/ Bilateral agreements were concluded with Austria, Belgium, France, the Netherlands, South Africa, Switzerland, and the United Kingdom. Agreements with the remaining countries--Canada, the Federal Republic of Germany, Italy, Japan, Sweden, and the United States--are in the process of being finalized after a protracted period of data collection and confirmation.

IV. Report on the Discussions

The policy discussions with the Zambian representatives took place against the background of an extremely difficult external liquidity situation for Zambia. Toward the end of 1984, it had become increasingly apparent that while the authorities had continued to implement adjustment policies broadly in line with the policy package supported by the 21-month arrangement from the Fund, even more fundamental adjustment was needed in view of the further deterioration of Zambia's medium-term balance of payments prospects. Market developments had led to significant downward revisions of the projected price per pound of copper for 1985 and 1986 to US$0.75 and US$0.91, respectively. Even these assumptions appeared no longer tenable, in view of market expectations and the drop of the copper price to around US$0.60-US$0.65 per pound which had occurred early in the year. The implications of this price revision for export earnings was a potential cumulative shortfall of some SDR 258 million during 1985-86 in relation to the program target, and of SDR 1.2 billion over the five year period through 1989.

Already, Zambia's economic situation had deteriorated rapidly during the first four months of 1985. Zambia was experiencing delays in making payments to the Fund. As noted above, Zambia had not met its obligations to the Paris Club, to its non-Paris Club official creditors, or to the London Club. As of the end of April 1985, Zambia was more than US$40 million in arrears on the oil facility with commercial banks used to procure imported petroleum, and it was with great reluctance that the consortium of the banks involved agreed to issue a new letter of credit in return for the halving of these arrears. The tight foreign exchange situation had caused a sharp curtailment of the foreign exchange allocations to the Zambia Consolidated Copper Mines (ZCCM), which was allowed to retain only 20-24 percent of its foreign exchange earnings during the first three months, and only 19 percent during April, as against the 25 percent retention in effect during much of 1984, and 35 percent which the company requires to maintain production and undertake essential mine development and maintenance. As a result, ZCCM had accumulated significant arrears to its foreign suppliers and was finding it increasingly difficult to secure inputs and spare parts for essential mining operations, as well as maintenance and development. Mineral output consequently fell, further reducing export receipts.

In view of continuing shortages of imported goods and spare parts, the Zambian authorities indicated that they expected no improvement in industrial production or activity in related sectors in 1985. However, a record performance was predicted for the agricultural sector. Production of maize during 1985 was expected to increase by more than 35 percent with even larger increases forecast for sunflower seeds, paddy rice, and groundnuts, and a growth in seed cotton production of nearly 20 percent. Even so, there was considerable uncertainty about marketing this output because the tight foreign exchange situation had created difficulties in procuring sufficient quantities of grain bags and spare parts for vehicles needed for the transportation and storage of the harvest. Meanwhile, the early indications on domestic price developments were pointing to a definite acceleration in the rate of inflation. The consumer price index for low-income households rose by 32.0 percent between end-June 1984 and end-June 1985, while the rise in the index for high-income households rose by 31.2 percent. The Zambian representatives also reported that wage increases negotiated during the first six months of 1985 were averaging more than 20 percent at an annual rate, far higher than the estimated 10 percent achieved during 1984. For lower-paid civil servants, the Government agreed to a general wage increase equivalent to 18 percent on an annual basis, retroactive to November 1984. The movements in the domestic banking system's net claims on the Government during the fourth quarter signaled a further weakening of the fiscal position.

In the external sector, the balance of payments outlook signaled a major weakening in the external current account, with a prospective deficit of some SDR 296 million for 1985 (or 21 percent larger than the 1984 deficit). The volume of copper exports was expected to drop by some 20,000 tons to 520,000 tons, although at an average copper price of SDR 0.66 per pound, earnings were projected to reach SDR 702 million and to raise total exports to SDR 876 million for 1985. Meanwhile, scheduled debt service payments in 1985 (excluding debt service arrears of SDR 120 million outstanding at the end of December 1984) were estimated to amount to SDR 818 million (equivalent to about 83 percent of exports of goods and services). Thus, even with imports rising by 6 percent from their relatively compressed level and assuming a successful debt rescheduling and implementation of strong adjustment policies, the Zambian authorities were confronted as in previous years, with a prospective large overall balance of payments deficit in 1985 and very severe liquidity problems.

Faced with this revised assessment, the staff underscored during the consultation discussions the need for a radical change in domestic and external policies designed to encourage significant structural change in the economy in the medium term and to promote the growth of nontraditional exports. This would focus on the adoption of a market-oriented exchange rate and domestic pricing policies, accompanied by substantial liberalization of the import licensing and foreign exchange allocation systems, and of exchange controls. These changes would aim to provide adequate incentives for export diversification and import substitution and to improve the efficiency of the allocation of foreign exchange.

1. The economic policy reform

The Zambian authorities noted that the deterioration in economic conditions had led to a basic reconsideration of economic policies by the Government. They referred to the Third National Convention in August 1984, where the President had noted in his address that, although enormous strides had been made in developing the country during the past decade, serious problems also had emerged associated with declining copper prices, increased import costs, and high foreign interest rates. The Zambian representatives noted that there were already signs that some of the progress made in the past was being reversed: delays in making foreign payments were raising import costs and impairing Zambia's credibility with its trading partners and creditors; factories viable in themselves were unable to operate for lack of imported inputs; and the imbalance between the demand for, and the availability of, foreign exchange was leading to an increasing reliance on administrative controls, a serious misallocation of resources, and the emergence of a growing parallel market for foreign exchange. The President had thus concluded that it was necessary to re-examine current economic policies, if Zambia were to avoid slipping into a situation of increasing economic difficulty.

The Zambian representatives noted that a number of measures had been implemented in recent years in the external sector which were aimed at alleviating some of the problems. In particular, the continued downward movement of the kwacha under the flexible exchange rate policy initiated in 1983 had improved the profitability of the export sector. In addition, retention schemes permitting exporters to keep part of their export earnings rather than surrender them to the Bank of Zambia had been successful in stimulating nontraditional exports. The authorities, however, concurred with the mission's assessment that these policies were inadequate to resolve Zambia's serious economic problems, which require a radical departure from current policies.

2. Exchange rate and trade policy reforms

The authorities stated that after lengthy deliberations, they had decided to proceed with a major reform of the exchange and trade system. The most fundamental change would be a move away from the crawling peg exchange rate regime and toward a market-related system for the determination of the exchange value of the kwacha. In this connection, they were actively considering a system of weekly or biweekly foreign exchange auctions by the Bank of Zambia. In that event, the exchange rate would be determined by the marginal bid that would exhaust the supply of foreign exchange to the market. The Government and the mining and oil-importing companies would not participate in such an auction; their foreign exchange requirements would be determined administratively and provided for in the context of a foreign exchange budget along with those for external debt service, and certain essential imports (such as oil, maize, and fertilizer); but the auction-determined exchange rate would be applied to all their transactions.

The staff welcomed the planned introduction of a market-related exchange rate system (such as the auction system) and offered technical assistance in this area, adding that it would be desirable to liberalize the import-licensing system concurrently. With the exception of certain goods that would continue to be controlled for reasons of public policy, import licenses should be used only for facilitating import procedures and customs documentation. Furthermore, in view of the improvement in the competitiveness of the import-substituting sector, which would result from the expected substantial depreciation of the kwacha in the auction market, import restrictions for the purpose of protecting local producers should be generally discontinued; continued protection, where deemed necessary, should be achieved through an appropriate tariff structure. In addition, in line with the policy of import liberalization, the staff advised that the import monopoly enjoyed by several state agencies or enterprises should be abolished, with the possible exception of the monopoly for the importation of oil. Restrictions on current invisible payments should also be liberalized.

The Zambian authorities were in general agreement with the staff representatives on the need to liberalize the trade and payments system. They stated that they intended to simplify the existing import-licensing system as part of the exchange rate reform. They also indicated that import prohibition for protective purposes, which now covered about 50 items, would be replaced in two stages by appropriate tariffs. The first stage would involve introduction of a minimum tariff of 10 percent on all imports, together with the reduction of the maximum tariff to 100 percent. In the second stage, a tariff commission would be established before the end of 1985, which, in collaboration with the World Bank, would review the protection system and recommend changes in the structure of tariffs and indirect taxes with a view to reducing the high level and wide dispersion of effective protection to the manufacturing sector.

The staff representatives noted Zambia's debt servicing problems, and underscored the need to be current on its external debt obligations. In this connection, the staff pointed out the rapid buildup of arrears by Zambia to the Fund beginning in the first quarter of the year, and urged the authorities to give priority to the prompt settlement of these overdue obligations, and to ensure that Zambia remains current thereafter.

While noting that the precarious external liquidity situation could only be eased through appropriate adjustment policies, the staff stressed the need for effective foreign exchange budgeting and cash flow management to ensure that adequate provision is made for essential transactions, including meeting financial obligations to the Fund. The Zambian authorities stated that they attached great importance to honoring their financial obligations to the Fund, and stressed their Government's determination to seek ways to settle the overdue payments as soon as possible.

As regards commercial arrears, the staff representatives stressed that the problem requires an early settlement as part of process of the normalization of Zambia's relations with foreign exporters and the encouragement of foreign investment. The Zambian representatives were cognizant of the need to address urgently the problem of commercial arrears, and indicated that they had engaged consultants to propose several options to deal with this problem.

3. Fiscal policy

The budget adopted early in the year by the authorities for 1985 envisaged an overall deficit of K 382 million (equivalent to 9.4 percent of the beginning money stock). This was to be achieved by a combination of revenue measures and expenditure restraint, with revenues increasing by 24 percent over the 1984 level, while total expenditures were budgeted to increase by 18 percent, somewhat higher than the overall rate of inflation of about 15 percent at that time. The budgeted deficit, however, considerably understates the subsidy payments for maize and fertilizer by about K 105 million and to some extent scheduled interest payments and charges on the external debt. As budgeted, the domestic bank financing requirement of the budget was set at K 160 million, or 9 percent of the end-1984 broad money supply. However, the data for the first four months of 1985 suggested that serious slippages from the fiscal targets may already have occurred.

The staff considered that, if the new exchange rate and trade system were introduced during the year, the budget aggregates would be inflated by the expected substantial depreciation of the kwacha. The authorities recognized that a number of expenditure items on the budget would be substantially increased as a result of the depreciation of the exchange rate, most notably, foreign debt service obligations. Unfortunately, the impact of the depreciation of the exchange rate on revenues was unlikely to be quite as direct or as substantial, and, in 1985, this was likely to result in an overall deficit much in excess of that originally budgeted, especially considering the underbudgeting for certain items noted above. The staff urged the authorities to introduce the significant adjustment measures to reduce the prospective fiscal deficit so as to limit recourse to domestic bank financing to no more than the equivalent of 15 percent of the beginning broad money stock, under the new exchange rate and trade system.

The Zambian authorities agreed with the staff that measures would have to be taken to reduce the size of the budget deficit. They indicated, however, that the Government planned expenditure cuts in a number of areas, most notably reducing employment in the public service. Over a three-year period, they said that the Government intended to reduce the number of temporary workers (presently accounting for 26 percent of government employment and 23 percent of the total wage bill) by 50 percent, although the dismissed workers would be provided with appropriate compensation. In addition, the Government planned to institute an accelerated voluntary retirement scheme (with full benefits being provided as lump sum payments) for perhaps 2,400 employees, as well as retiring all those employees due for retirement (an estimated 6,400 employees). In addition, the Government envisaged a reduction of fringe benefits (including use of cars) presently provided to a wide range of public officials. Recognizing the importance of expenditure cuts in areas with a high direct foreign exchange component, the Zambian authorities said that about one third of the diplomatic missions abroad would be closed as soon as possible and estimated the saving on this item at around K 10 million at current rates of exchange.

The staff commended the authorities for their decision to contain expenditures, but pointed out that while the measures held potential for substantial savings in the medium term, they were unlikely to have a significant effect on expenditure in the short run. The staff also stressed that the authorities should, in addition to constraining current expenditure while ensuring adequate outlays for maintenance, also consider cuts in capital expenditure, particularly in areas not expected to contribute to output expansion in the short term. The authorities agreed to bear this in mind. Regarding incomes policy, the staff agreed with the authorities that the best policy course would be to leave income determination to free collective bargaining. However, with respect to government employees, the staff pointed to an increase of 18 percent that had already been granted to the lower paid employees, and cautioned the authorities on the need for wage restraint. The authorities concurred, but also indicated that, in view of the expected depreciation of the kwacha and in the context of the reforms, it would be difficult for them not to grant at least some modest pay award, especially to those grades of civil servants who had not benefitted from the last round of wage increases.

The staff also stressed that, to minimize budgetary subsidies and transfers, adjustment measures needed to be directed toward Zambia's large parastatal sector, which accounts for nearly 40 percent of total value added in the economy and more than one third of all wage employment. Performance in this sector, and particularly in the large Zambia Industrial and Mining Corporation (ZIMCO) holding company, 1/ has been weak because of inefficiency and government policies that, even after the introduction of price decontrol in late 1982, have inhibited economic pricing. The staff stressed that the Government strengthen its commitment to allowing full economic pricing throughout the economy, including the parastatal sector, with cost increases (resulting from exchange rate depreciation and other sources) fully and quickly passed through to consumer prices for all commodities, including petroleum and fertilizer. In particular, the staff recommended that the prices of mealie meal and fertilizer be increased substantially to keep subsidy payments for those items within acceptable limits. The authorities indicated that they were contemplating an increase in the price of mealie meal but they felt that no increase in fertilizer prices was required because the National Agricultural Marketing Board (NAMBOARD), the parastatal enterprise which handles fertilizers, had ample stocks purchased at the earlier exchange rates. The staff advised that the increases in the price of mealie meal should at least be sufficient to keep mealie meal subsidies at the 1985 budgetary provision. The staff pointed out that there was a need to increase fertilizer prices as well, because NAMBOARD incurred arrears when it imported the current fertilizer stocks and, in any case, pricing needed to be on a replacement rather than historic cost basis.

1/ ZIMCO owns or controls more than 60 enterprises representing the bulk of all domestic industry and commercial activity.

On the revenue side, the authorities proposed that additional revenues would be obtained from increases in customs or excise duties on luxury items and improved tax administration including recovery of tax arrears. The staff cautioned against excessively high tariffs that would further distort the effective protection system, and expressed some doubts as to the magnitude of the revenues which could be expected from such measures. In the staff's view, the principal source of potential revenue increase would be appropriate taxation of the increased profits of the mining company following the depreciation of the kwacha. The authorities agreed that there was room for increased revenues from this source, but cautioned the need to safeguard the adequacy of the cash-flow of the ZCCM given its critical role as the nation's main foreign exchange earner.

4. Monetary policy

The staff stressed that, under a system of market determination of exchange rates, monetary policy would assume a central and crucial role, and the monetary authorities would need to have tools that would enable them to respond promptly and flexibly to developments in the financial markets. The staff recommended that under the new system the practice of setting ceilings on commercial banks' lending should be supplemented by Bank of Zambia operations designed to limit the growth in reserve money (currency plus deposits with the Bank of Zambia). In addition, in order to finance its deficit, the Government should offer paper to banks and nonbanks at market-determined prices rather than the current practice of automatic financing of government deficits through an overdraft with the Bank of Zambia. This would entail the decontrol of interest rates, which would help the process of efficient financial intermediation and allocation of resources. It would also strengthen the leverage of the monetary authorities over the growth of credit and money supply, and help them counter speculative pressures on the exchange rate.

The Zambian representatives said that they agreed with the staff recommendation to discontinue controls on interest rates. They stressed, however, that they would wish to maintain some controls on interest rates to the agricultural sector with a view to according credit to the sector at preferential rates. While agreeing with the authorities as to the importance of the agricultural sector, particularly in view of the need to broaden Zambia's export base, the staff, nevertheless, recommended that appropriate agricultural producer pricing following the depreciation of the exchange rate as being a more efficient way for promoting growth of the sector than subsidizing the cost of credit.

On September 2 the authorities introduced a daily auction for Treasury bills and removed controls on the structure of banks' interest rates. At the first auction the Treasury bill rate rose to 13 percent from 9.5 percent. However, at subsequent auctions the authorities have adjusted the quantity of bills they offered to the market in order to hold the interest rate at 13 percent. At that rate the demand for Treasury bills does not appear to be sufficient to prevent a substantial expansion in the monetary base.

V. The Medium-Term and External Payments Outlook

The outlook for 1986-89 is extremely difficult and will depend critically on the authorities' pursuit of strong adjustment policies, including the immediate implementation of major policy changes and on the economy's response to these policies over the medium term. Mineral exports are expected to rise at an annual average rate of 5.3 percent in SDR terms (unchanged in real terms) during the period 1986-89 and are likely to be largely invariant to the policies pursued (provided, of course, that the achievement of output targets is not prevented by shortages of foreign exchange and imported inputs). In accordance with projections by the mining company, the volume of copper output, assuming adequate maintenance of development work in the mines, is expected to rise by 50,000 tons in 1986, and a further 20,000 tons in 1987, because of the coming into operation of the Tailings Leach project during the first half of 1986. In these projections, the price of copper is assumed to rise by 4 percent a year in SDR terms and remain constant in real terms. The export volume of cobalt, the second most important export item, is projected to show a slight increase in 1986, and remain constant in subsequent years in the absence of the discovery of new reserves; its price is assumed to remain constant in real terms in accordance with estimates by company officials. On the other hand, exports of zinc and lead are expected to show a steady decline, reflecting a gradual depletion of existing reserves.

It is difficult to estimate with any reasonable accuracy the effects of the new policies on nonmineral exports, although the supply response can be expected to be substantial. Zambia's low level of manufacturing exports reflects the orientation of its large manufacturing sector predominantly toward the domestic market. Nevertheless, there could be a strong increase in manufacturing exports over the next few years if the manufacturing sector were reoriented toward external markets and marketing difficulties quickly overcome. Similarly, Zambia has a large agricultural potential, and appropriate price incentives could provide a strong impetus to agricultural exports. Thus, the increase in nonmineral exports assumed in the medium-term projections (24 percent in real terms on an annual basis), though by no means small, may not be unrealistic in view of the low recorded levels of such exports compared with the economy's agricultural and manufacturing potential. Imports are projected to rise by some 6 percent or more in SDR terms, implying a small volume increase during the period. The sharp depreciation of the kwacha likely to result from the implementation of a floating exchange rate system will probably result in significant import substitution and decreased dependence on imported inputs. However, the overall effects of gains in the trade balance would probably remain relatively small in relation to the projected stream of external claims on Zambia's resources. The debt service ratio before debt relief 1/ is expected to remain at very high levels during the entire projection period, but to decline somewhat from 83 percent in 1985 to 61 percent in 1989, largely reflecting the expected recovery of exports (Table 5).

Even assuming that the economy will respond so favorably to the adjustment measures currently under consideration, Zambia will still be faced with very large, though diminishing, financing gaps over the medium term. The gap would amount to SDR 421 million in 1986 and SDR 389 million in 1989. The sustainability of these external payments gaps will depend on continued debt relief and exceptional assistance on concessional terms. The projected financing gaps, however, are very sensitive to economic assumptions, particularly assumed developments in copper prices. For instance, at the projected volumes of copper exports and levels of other transactions, the resource gap at the outer years could widen by as much as SDR 520 million by 1989, if the average copper price were to remain unchanged at SDR 0.66 per pound; it would decline to SDR 240 million by 1989 assuming the copper price were to rise steadily at an annual rate of 4 percent to SDR 0.77 by 1989.

1/ Including debt service on the projected financing gaps.

Table 5. Zambia: Debt Service Payments, 1982-89

	1982	1983	1984 Original prog.	1984 Revised prog.	1984 Revised est.	1985	1986	1987	1988	1989
						Projections				
					(In millions of SDRs)					
Scheduled debt service	527	577	693	675	623	818	822	853	735	688
Interest	226	236	290	302	253	350	358	377	400	422
Amortization	301	341	403	373	370	468	463	477	335	267
Rescheduled commercial arrears	--	--	--	--	--	--	--	39	39	124
Interest	--	--	--	--	--	--	--	39	39	36
Amortization	--	--	--	--	--	--	--	--	--	88
Total	527	577	693	675	623	818	822	792	774	812
Actual debt service										
After debt relief	527	481	326	358	379	...	...	...	...	...
After debt relief and arrears	320	282	364	396	310	...	...	...	...	...
					(In percent of exports of goods and services)					
Scheduled debt service	56.4	59.3	81.6	83.5	68.7	88.1	71.6	69.1	57.9	51.2
Interest	24.2	24.2	34.2	37.4	27.9	35.5	31.2	30.5	31.5	31.4
Amortization	32.2	35.0	47.5	46.2	40.8	47.6	40.4	38.6	26.4	19.8
Rescheduled commercial arrears	--	--	--	--	--	--	--	3.1	3.0	9.2
Interest	--	--	--	--	--	--	--	3.1	3.0	2.7
Amortization	--	--	--	--	--	--	--	--	--	6.5
Total	--	--	--	--	--	83.1	71.6	72.2	61.0	60.5
Actual debt service										
After debt relief	56.4	49.4	38.4	44.3	41.8	...	...	...	...	...
After debt relief and arrears	34.3	29.0	42.9	49.0	34.2	...	...	...	...	...
Memorandum:										
Exports of goods and services	934	973	849	808	906	984	1,148	1,235	1,269	1,343

Sources: Bank of Zambia; Central Statistical Office; EBS/84/135 and EBS/84/229; and staff estimates.

VI. Staff Appraisal

The Zambian economy has been in a prolonged state of contraction since 1975. Zambia relies on a single primary product (copper) for the bulk of its export earnings, and its industrial sector is heavily dependent on imported inputs. The economy has thus been extremely vulnerable to the combination of declining copper prices (which no longer can be viewed as a cyclical phenomenon) and the increasing costs for imported goods and services. Since 1973, the purchasing power of Zambia's exports has fallen by more than 70 percent. Faced with this situation the authorities resorted to heavy external borrowing from the Fund and on commercial terms, and also incurred large commercial arrears. As a result, the burden of debt service has risen sharply. In retrospect, it is clear that the authorities' adjustment efforts, which have been supported by a number of Fund arrangements, were delayed and not adequate or sustained enough to cope with the strong external payments and other economic pressures stemming from such a massive deterioration in the terms of trade. This was in part the result of failure to recognize the long-term nature of the decline in the copper price. Equally important was the authorities' failure to implement the major policy changes that were required, as evidenced by the interruptions of many of the arrangements with the Fund.

The economic and financial situation, especially the external liquidity position, has become extremely precarious since the beginning of 1985. Imports are severely compressed, and foreign exchange allocations to the mining company are now below what is considered necessary to maintain current levels of production and exports. Inputs for other industrial firms are in such short supply that output is running greatly below capacity throughout the economy, while inflation is accelerating partly as a result of the constrained supply situation.

Since April 1985 there have been serious delays in the discharge by Zambia of its financial obligations to the Fund, prompting a report and complaints to the Executive Board under Rule K-1 and Rule S-1 (the latter has recently been withdrawn). Zambia has also not been meeting payments to the Paris and London Clubs, including those arising from the 1984 debt rescheduling agreements, and has incurred considerable arrears in respect of debt service to multilateral organizations.

It is thus to be welcomed that the Zambian authorities have decided to implement radical changes in their exchange and trade system, and to consider, inter alia, the introduction of an auction system for the determination of the exchange rate, and a general liberalization of the highly restrictive trade system. This is essential if Zambia is to begin to make progress to deal with its problems. One consequence of the adoption of a market-determined exchange rate system would be the removal of the existing multiple currency practice arising from the 10 percent levy on the sale of foreign exchange for private overseas travel. The new exchange rate system should be allowed to reflect to the maximum extent possible the influence of market forces. Moreover, rigidities such as administered prices now present in the domestic pricing system should be rapidly reduced to allow room for economic pricing throughout the economy, including the parastatal sector. It would be particularly important for the corrective effects of the movements in the kwacha rate to be transmitted fully and quickly through to domestic cost-price relations, including the pricing of petroleum products and fertilizer.

The staff has stressed the need to tighten demand management policies to support the exchange rate and trade policy measures and has urged the authorities to put in place as quickly as possible appropriate measures in the areas of fiscal, monetary, and pricing systems and adhere to such policies resolutely. This would be even more important if confidence is to be developed in the new exchange and trade arrangements. The authorities have indicated clearly their intention to reduce the fiscal deficit sufficiently to bring monetary growth down within a low target range. In the staff's view this requires in the short run firm and decisive restraint on the growth of personal emoluments through a combination of a restrictive wage and recruitment policy, phased reductions of administrative staff and daily labor, and strict containment on the budgetary subsidies on maize and fertilizer through realistic pricing of these products. Slippages in the execution of recent budgets also underscore the need to introduce and strictly apply improved expenditure control procedures and practices and to limit the capital program to projects with the greatest potential for contributing to growth and diversification of the production base. To mobilize additional resources and increase the elasticity of the tax system, the basis of certain important domestic taxes, notably the excise tax, should be shifted from specific to ad valorem valuation. This change should be combined with selective increases in taxes, especially taxes on the mining industry to recoup some of the exchange profits in excess of what is necessary to ensure the liquidity and smooth operations of the company.

The staff has also stressed that under a market-determined exchange rate regime as envisaged by the authorities, an active monetary policy will be crucially important as an adjunct to the much needed tightening of fiscal policy, and of overall demand management. It is, therefore, welcome that the authorities have accepted the principle of introducing a financial market, initially for government debt instruments, and a freeing of interest rates, as a framework for such an active monetary policy in the period ahead. They have, in fact, already taken the initial step of introducing an auction for Treasury bills. The staff would urge the authorities to permit that market to operate freely and to use it effectively as a means of controlling bank liquidity and allowing appropriate market-related interest rate structure to evolve.

It cannot be overemphasized, however, that even with such fundamental economic policy reforms and comprehensive adjustment, Zambia will still be faced with large external financing gaps in 1985-86 and over the medium term. The extremely large external debt servicing burden, coupled with the substantial external payments arrears accumulated in recent years, poses serious problems for external viability, even with successive debt rescheduling on very generous terms. Thus, Zambia will continue to need very substantial donor support in the form of quick-disbursing concessional aid and grants. In these circumstances, adjustment can no longer be delayed; it is imperative for the authorities to put in place as soon as possible a credible adjustment program worthy of such support, and to implement it consistently with the greatest possible determination.

Zambia's exchange system involves restrictions on payments and transfers for current international transactions subject to approval under Article VIII, including those related to imports, travel, medical and educational expenditures, and dividends and profits, as well as restrictions evidenced by external payment arrears. All of these restrictions are subject to approval under Article VIII. Two multiple currency practices arising from (1) the 10 percent levy on sales of foreign exchange for private overseas travel, and (2) the counterpart deposit requirement against commercial payments arrears are also subject to approval under Article VIII. The staff welcomes the authorities' intention to liberalize the exchange system as the balance of payments position permits, and progressively reduce the level of outstanding external payments arrears, and encourages the authorities to take the adjustment steps that would make this possible. In the meantime, the staff is not recommending the approval of the restrictions on current payments and the multiple currency practices.

It is proposed that Zambia remain on the 12-month consultation cycle.

VII. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board:

1. The Fund takes this decision relating to Zambia's exchange measures subject to Article VIII, Sections 2 and 3, in concluding the 1985 Article XIV consultation with Zambia and in the light of the 1985 Article IV consultation with Zambia conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Zambia continues to maintain restrictions on payments and transfers for current international transactions, including those evidenced by external payments arrears, and multiple currency practices arising from the tax imposed on purchase of foreign exchange for certain foreign travel and the maintenance of counterpart deposit scheme for external payments arrears as described in SM/85/ , which are subject to approval of the Fund under Article VIII, Sections 2(a) and 3. The Fund encourages the authorities to remove these restrictions and practices as soon as possible.

ZAMBIA - Relations with the Fund
(As of July 31, 1985)

I. Membership Status

(a) Date of membership: September 23, 1965
(b) Status: Article XIV

II. General Department (General Resources Account)

(a) Quota: SDR 270.3 million
(b) Total Fund holdings of currency:
SDR 963.6 million (356.5 percent of quota)
(c) Fund credit: SDR 693.33 million (256.5 percent of quota)
Credit tranche--SDR 109.^ million (40.3 percent)
EFF--SDR 77.0 million (28.5 percent)
Enlarged access--SDR 324.2 million (119.4 percent)
CFF--SDR 183.1 million (67.7 percent)
(d) Reserve tranche position: 0.01 million
(e) Current operational budget: Not included
(f) Lending to the Fund: None

III. Current Stand-by or Extended Arrangement and Special Facilities

(a) Current stand-by
(i) Duration: July 16, 1984-April 30, 1986
(ii) Amount: SDR 225.0 million
(iii) Utilization: SDR 80.0 million
(iv) Undrawn balance: SDR 145.0 million
(b) Stand-by and extended arrangements during last 10 years:
(i) First credit tranche purchase - one-year stand-by for 25 percent of quota, approved in May 1973;
(ii) One-year stand-by for 82 percent of quota, approved in July 1976;
(iii) Two-year stand-by for 177 percent of quota, approved in April 1978;
(iv) Three-year extended arrangement for 378 percent of quota, approved in May 1981 and canceled in July 1982;
(v) One-year stand-by for 100 percent of quota, approved in April 1983;
(c) Special facilities in the past two years:
(i) Compensatory financing facility purchase for 16 percent of quota (SDR 34 million), approved in December 1982.
(ii) Compensatory financing facility purchase for 46 percent of quota (SDR 97.2 million), approved in principle April 18, 1983 and authorized May 18, 1983.

ZAMBIA - Relations with the Fund (continued)
(As of July 31, 1985)

IV. SDR Department

(a) Net cumulative allocation: SDR 68.3 million
(b) Holdings: None
(c) Current Designation Plan: Not included

V. Administered Accounts

(a) Trust Fund Loans
  (i) Disbursed SDR 42.8 million
  (ii) Outstanding SDR 40.0 million
(b) SFF Subsidy Account: None

VI. Overdue Obligations to the Fund: SDR 70.1 million

Nonfinancial Relations

VII. Exchange rate arrangement

The Zambian kwacha is pegged to an unannounced basket of currencies. The U.S. dollar is the intervention currency, and the Bank of Zambia's rates for the U.S. dollar are based on the U.S. dollar/SDR rate calculated by the Fund for the preceding day. As of July 31, 1985, the rate was K 1 = US$0.4470.

VIII. Last Article IV consultation and stand-by review

The last Article IV consultation discussions were held in Lusaka during February 7-22, 1984 with Board discussion on July 16, 1984. The first review under the current arrangement was discussed by the Executive Board on November 26. Discussions for the second review were begun in Lusaka, December 2-13 and continued during a staff visit to London on January 9-11.

IX. Technical Assistance

The Central Banking Department has furnished the Bank of Zambia with a Research Adviser (February 1983-February 1984), an external debt adviser (November 1983-November 1984), and an economic adviser to the Governor (appointed October 1983).

A technical assistance mission from the Fiscal Affairs Department visited Zambia March 25-April 9, 1984, and a mission from the Bureau of Statistics visited Lusaka during late February 1985.

ZAMBIA - Relations with the Fund (concluded)
(As of June 30, 1985)

X. Adequacy of Statistics

The provision of statistics by Zambia is generally adequate.

XI. Resident Representative

A Fund resident representative has been stationed in Lusaka since November 1983.

World Bank Group Relations with Zambia

The World Bank Group has made 28 loans and 14 credits to Zambia amounting to about US$780 million since 1956. The IFC has invested about US$85 million in 11 projects in Zambia since 1972. Energy, transportation, communications, and rural water supply projects have received half the loans and five of the credits; secondary and higher education, teacher training, and commercial, agricultural, and technical education have received four loans and one credit; in agriculture, six loans and four credits have assisted industrial forest plantations, livestock, commercial crops, integrated family farming, coffee production, and smallholder dairy development; other loans have assisted Zambia's development program in the mining and manufacturing sectors as well as urban development. A technical assistance credit is helping the Government improve its planning and project preparation.

The Bank Group's present strategy in Zambia is to support economic diversification away from overdependence on copper and to improve economic efficiency. In March 1984 the Bank extended an Export Rehabilitation and Diversification loan to Zambia for an amount of US$75 million to improve economic efficiency in the mining industry. In January 1985 an Agricultural Rehabilitation credit of US$25 million was approved, and another credit for an Industrial Reorientation Project is under active consideration. A primary focus for these credits is improving the policy and institutional environment for agriculture and manufacturing, the sectors with the greatest potential for production and export growth. The Agricultural Rehabilitation Project is cofinanced by credits totaling approximately US$40 million from the African Development Bank, the United States Agency for International Development, the CIDA, and the Government of Switzerland. The project will complement policy and institutional reforms designed to provide greater incentives to producers of agricultural products; phase out subsidies resulting from the current structure of marketing and consumer pricing of maize and fertilizers; and allow competition among NAMBOARD and the cooperative unions, the official marketing organizations, and private traders. The credit is to finance purchases of farm inputs, including machinery and implements, spare parts, agrochemicals, improved seeds, etc., with the foreign exchange to be provided at market-determined exchange rates.

The Industrial Reorientation Project is expected to be financed through a credit in an amount of US$75 million (of which US$72.8 million is for industrial imports) drawn mostly from the African Facility, and is expected to be disbursed over nine months. The project's objective is to increase the output of efficient industrial firms and reorient manufacturing activity toward exports and greater reliance on labor and domestic raw materials. The project has been closely interfaced with the proposal for introducing a market-determined exchange rate system, trade liberalization, reform of the external tariff structure, adoption of a new Investment Act, and agreement on the size and composition of the Industrial Development Corporations (INDECO) 1986/87 investment program. The financial relations of the World Bank Group with Zambia are summarized below.

ZAMBIA: Disbursed and Undisbursed Loans and Credits by the World Bank Group

(July 31, 1985)

IBRD/IDA loans and credits (In millions of U.S. dollars)

	Disbursed			Undisbursed		
	IBRD	IDA	Total	IBRD	IDA	Total
Agriculture (incl. industrial forestry)	39.57	10.84	50.41	7.51	40.76	48.27
Education	63.56	6.99	70.55	--	15.97	15.97
Export sector rehabilitation	13.85	--	13.85	61.15	--	61.15
Industrial and development finance	30.85	1.11	31.96	3.82	--	3.82
Power, energy, and water supply	193.02	3.23	196.25	--	15.09	15.09
Program lending	42.50	--	42.50	--	--	--
Petroleum exploration	4.00	--	4.00	2.60	--	2.60
Technical assistance	--	3.57	3.57	--	1.43	1.43
Telecommunications	31.85	--	31.85	--	--	--
Transportation	65.53	20.83	86.36	17.92	5.46	23.38
Urban	20.00	--	20.00	--	--	--
Total	504.73	46.57	551.30	93.00	78.71 1/	171.71
Of which:						
Repaid	(160.58)	(--)	(160.58)			
Outstainding	(344.16)	(46.57)	(390.72)			

IFC investments

Disbursed	Undisbursed
55.2	17.9

Sources: IBRD; and IFC.

1/ Excludes credits totaling US$52.1 million not yet effective.

Zambia--Statistical Issues

1. Outstanding Statistical Issues

The main sources of statistics in Zambia are the Central Statistical Office, the Bank of Zambia, the Ministry of Finance, and the National Commission for Development Planning.

a. Real sector

A one-week technical assistance mission (February 1985) in the area of general economic data reviewed the methodologies underlying the compilation of trade, production, and price statistics. The report of the mission was sent to the authorities in May 1985.

During 1984, the Zambian authorities improved the timeliness of statistical reporting in the real sector. They were able to provide national accounts estimates for 1984 in early April 1985.

Data on consumer prices are based on a 1972/73 expenditure survey and are normally available with a one-to-two month lag. The industrial production index is based on the 1973 Annual Census and needs to be rebased. Data on employment and earnings are typically available only with a oneto two-year lag and only for the estimated 10 percent of the labor force working in the formal sector of the economy. The Central Statistical Office is now conducting a comprehensive employment survey, the first to be made in many years. The results should be available sometime in 1986.

b. Government finance

Quarterly data on the Central Government are available in IFS through the third quarter of 1984 (September 1985 issue). Data on government expenditure by function (particularly capital expenditure) are available only after a substantial lag, and there have been problems in recording and reporting data on foreign grants. The coverage in the 1984 Government Finance Statistics Yearbook is limited to the central government, for which data on revenue, expenditure, and financing are available through 1982, and local governments, for which data on revenue and expenditure end in 1980. Comprehensive data on government debt are available for the years 1977 and 1978 only. No additional data have been received for the 1985 Yearbook.

c. Monetary accounts

Data on money and banking are generally available with a lag of 3-4 months. Differences exist between the data provided by the authorities and IFS. These arise because of (i) different valuation adjustments relating to liabilities to the Fund, (ii) the authorities' exclusion of commercial payments arrears from the liabilities of the banking system and their different methods of valuation of these liabilities, and (iii) the authorities' exclusion of the mining company's deposits at the Bank of Zambia from reserve money.

The Bureau of Statistics has requested balance sheet data relating to some other financial institutions, so that Section 40 on the country page for Zambia in IFS may be made more comprehensive.

d. External sector

In November 1984, a Bureau of Statistics staff member visited Zambia on a balance of payments technical assistance mission. The final report of the mission was sent to the authorities in June 1985. This mission observed that a great deal of data for estimating balance of payments are already available in Zambia, but noted that improvements are needed to ensure the flow of information to compilers in a coordinated fashion.

2. Coverage, Currentness, and Reporting of Data in IFS

The table below shows the currentness and coverage of data published in the country page for Zambia in the September 1985 issue of IFS. The data are based on reports sent to the Fund's Bureau of Statistics by the Bank of Zambia, which during the past year have been provided on a timely basis.

	Status of IFS Data	Latest Data in September 1985 IFS
Real Sector	- National Accounts	1984
	- Prices: WPI	Q3 1984
	CPI	March 1985
	- Production: Industrial	Dec. 1984
	Mining	Dec. 1984
	- Employment	n.a.
	- Earnings	n.a.
Government Finance	- Deficit/Surplus	Q3 1984
	- Financing	Q3 1984
	- Debt	n.a.
Monetary Accounts	- Monetary Authorities	March 1985
	- Deposit Money Banks	May 1985
	- Other Financial Institutions	Dec. 1984

		Status of IFS Data	Latest Data in September 1985 IFS
External Sector	-	Merchandise Trade:	
		Values	Dec. 1984 1/
		Unit Values (Exports)	1980 2/
		(Imports)	1981
	-	Balance of Payments	1984
	-	International Reserves	July 1985
	-	Exchange Rates	July 1985

1/ The latest data for copper are for February 1985.
2/ The latest data for unit value of copper exports are for December 1984.

ZAMBIA - Basic Data

Area, population, and GDP per capita

Area	290,410 square miles
Population	
Total (1983 estimate) 1/	6.2 million
Growth rate	3.0 percent
GDP per capita (1983)	SDR 523

	1980	1981	1982	1983	1984 2/
		(In millions of kwacha)			
Gross domestic product and expenditure (at current market prices)					
Gross domestic product	3,063	3,486	3,595	4,181	4,733
Agriculture	(435)	(554)	(492)	(594)	(698)
Mining	(501)	(488)	(397)	(642)	(664)
Manufacturing	(566)	(684)	(740)	(830)	(988)
Government services	(468)	(586)	(665)	(709)	(800)
Other sectors	(1,093)	(1,174)	(1,301)	(1,406)	(1,583)
Gross domestic expenditure	3,207	3,922	3,911	4,240	4,669
Consumption	(2,494)	(3,248)	(3,308)	(3,665)	(4,005)
Investment	(713)	(673)	(603)	(575)	(664)
External resource gap (-) or surplus at market prices	-144	-436	-316	-59	64
		(In percent of GDP)			
Consumption	81.4	93.2	92.0	87.7	84.6
Investment	23.3	19.3	16.8	13.8	14.0
External Resource gap(-) or surplus	-4.7	-12.5	-18.8	-1.4	1.4
		(In percent)			
Prices					
GDP deflator	11.7	7.2	6.1	18.6	14.7
CPI (low income)	11.7	14.0	12.5	19.6	20.0
CPI (high income)	11.5	10.4	13.2	17.7	20.8
CPI (composite)	11.6	12.2	12.9	18.7	20.4

1/ Mid-year estimates.
2/ Preliminary estimates.

ZAMBIA - Basic Data (continued)

	1980	1981	1982	1983	1984 1/
		(In millions of kwacha)			
Government finance (cash basis)					
Revenue and grants	791	833	868	1,069	1,161
Expenditure and net lending	1,168	1,278	1,390	1,389	1,507
Current	1,045	1,149	1,162	1,191	1,241
Capital and net lending	123	129	228	198	266
Overall deficit(-)	-344	-463	-675	-310	-346
Financing	344	463	675	310	346
External	142	247	112	101	60
Domestic	275	216	528	196	286
Banking system	(233)	(164)	(489)	(115)	(189)
Other	(42)	(52)	(39)	(81)	(98)
Other	-73	--	35	13	--
Overall deficit (as percentage of GDP)	11	13	19	7	7
		(In millions of kwacha)			
Money and credit					
Foreign assets (net)	-860	-1195	-1484	-1745	-2143
Domestic assets (net)	1,515	1,823	2,291	2,933	3,432
Claims on government (net)	(1,331)	(1,495)	(1,983)	(2,099)	(2,287)
Claims on the private sector (incl. mining)	(500)	(760)	(906)	(1,037)	(1,199)
Money and quasi money	907	979	1,309	1,444	1,703
Money	509	561	682	787	867
Balance of payments		(In millions of SDRs)			
Exports, f.o.b.	1,023	833	824	877	817
Of which: copper	(865)	(734)	(722)	(778)	(668)
Imports, c.i.f.	1,017	-1,050	-1,049	-785	-706
Trade balance	6	-217	-225	92	111
Services and transfers (net)	-360	-421	-338	-333	-357

1/ Preliminary estimates.

ZAMBIA - Basic Data (Concluded)

	1980	1981	1982	1983	1984 1/
			(In millions of SDRs)		
Balance of payments (concluded)					
Current account balance	-354	-638	-609	-258	-244
Capital account (net)	126	249	42	-28	-183
Government	(139)	(242)	(59)	(5)	(-153)
Mining companies	(26)	(111)	(43)	(-62)	(31)
Other (incl. errors and omissions)	(-39)	(-104)	(-60)	(29)	(-61)
SDR allocation	15	15	21	--	--
Valuation adjustment	--	47	--	-8	--
Overall surplus or deficit(-)	-213	-327	-546	-294	-427
Current account balance (as percent of GDP)	-12	-19	-17	-10	-11

1/ Preliminary estimates.