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DP/ZAM/85/007/11- 54

MISSION AT THE NATIONAL COMMISSION FOR DEVELOPMENT PLANNING LUSAKA - ZAMBIA

AUGUST 2 - NOVEMBER 2, 1990

FINAL REPORT

WOJCIECH HUBNER
UNIDO CONSULTANT

LUSAKA, ZAMBIA, NOVEMBER 1990.

1. The project was aimed at strengthening of the Investment Planning and Research Department (IPR) of the National Commission for Development Planning (NCDP).

The mission covered the period from August 2 to November 2, 1990. During the mission the UNIDO consultant was attached to the IPR Department of the NCDP and was working in close cooperation with professional staff of the Department.

2. Main objective of the mission, in line with the terms of reference, was to collect materials and prepare two opening chapters of the NCDP Economic Report 1990 which is to be submitted to the Parliament of the Republic of Zambia in November 1990. During my mission I have been working under the direct supervision of Mr.G.Chivunga, Director of the IPR, and Mr. W. Kawana, Permanent Secretary of the NCDP. Both chapters ("Recent Developments in the Global Economy and their Impact on the National Economy of Zambia" and "State of the Domestic Economy") play a leading role in the Economic Report and are considered as an introduction to more detailed, part of the Report, dealing with sectoral issues. The chapters were submitted to the Editing Committee of the Economic Report and thoroughly discussed during its meetings. Edited version of both chapters is attached to this report. The contents of particular chapters is the following:

Chapter I: Recent developments in the Global Economy and their impact on the National Economy of Zambia.

1.1. Introduction

1.2 World Economy

1.3 Developed Market Economies

1.4. Developing Countries

1.5. Impact on the National Economy

Chapter II: State of the Domestic Economy

2.1. Introduction

2.2. Trends and structure of GDP

2.3. Price System

2.4. Wages and Income Policy

2.5. Foreign Trade and the Balance of Payments

2.6. Monetary Policy

2.7. Financial Policy

Materials submitted to the Editorial Committee were based on information from Central Statistical Office, Bank of Zambia, Ministry of Commerce and Industry, Ministry of Finance, Zambia Consolidated Copper Mines and various international sources.

During the meetings with the Editorial Committee, we have had long, substantive discussions with the top management of the NCDP on various issues referring to the present position of developing countries in the world economy and to domestic economic policies of Zambia (inflation and price reform, devaluation, Balance of Payments and indebtedness, restructuring, etc).

Economic and political developments of 1989 and 1990 are extremely important from the point of view of Zambia' attempts to gain in future more competitive position in the world economy and improve standard of living of the society. Zambia has embarked upon a package of radical economic reforms announced in June/July 1989. These reforms have been endorsed by leading international organizations and received considerable moral and financial support from international community.

Zambia has entered the new decade with new hopes and facing new challenges as the transition period to already restructured economy is exposing numerous deep-seated weaknesses of the economic system.

Despite a difficult economic situation and hardships of the transition period the country has proved, so far, its strong commitment to a successful implementation of the idea of the basic economic change.

At the same time, as discussions at the NCDP proved, the dialogue is still open about the ways, means and the pace of economic reforms.

The number of countries in the African continent experimenting with economic reforms is unprecedented. Zambia's national case provides us with valuable experience about existing alternatives in the economic policy, as well as exposes the role of the Government in cushioning negative impact of economic reforms on the standard of living of low-income groups.

While preparing materials for the Economic Report and during the discussions I was widely referring to positive and negative experience in introducing radical economic reforms and adjustment policies by Eastern European economies.
I have found very helpful, as well, my own experience from last years' assignments connected with preparation of the Economic Report 1989.

3. Analysis of potential improvements in preparation of the new Public Investment Program (PIP) for 1990 - 1993 and, in general, of the public expenditure management system, was another specific area of my research during the mission.

At the end of 1989 the Public Investment Programme (PIP) 1989 - 1993 was developed in Zambia. This document was drawn out of the Fourth National Development Plan (FNDP) and was complementary to the Policy Framework Paper prepared jointly by the Government of Zambia and the staffs of the World Bank and the International Monetary Fund.

Since the introduction of economic reforms in 1989 a considerable effort has been made in Zambia to strengthen the budget expenditure control and, in general to create an efficient public expenditure management system. The PIP was an important element of this system.

The PIP was the expression of the most recent Government's priorities and was constrained by the verified, actual funding available. Under the PIP, highest priority was given to rehabilitation and maintenance of already existing facilities. Particular emphasis was on completion of on-going projects in order to avoid losses in already frozen expenditure.

It was generally agreed that there should be no public investment projects (both by the Government, as well as by parastatals) outside the framework of the PIP.

However, some isolated cases of Government and parastatals projects, continued from the past, could be identified outside the framework of PIP in 1990.

I took part in meetings with representatives of the World Bank (headed by Mr. J. E. Todd) and the NCDP (with Mr. Kawana, the Secretary and Mr. G. Chivunga, Director of IPR) discussing these issues. It was agreed that in the future the NCDP together with the Budget Office would screen and carefully monitor implementation of particular projects, block not authorized ones and check on allocation of funding. A specialized computer system designed within the IPR Department of the NCDP (Dr. P. Nkanza's team) will be used for monitoring purposes.

As a result of my studies and the discussions held, I have prepared and submitted to the head of the IPR Department Mr. Chivunga a working paper "Guidelines for Preparation of the New Updated Public Investment Programme 1990 - 1993" which is also attached to this report.

4. Following a request by INDECO, as agreed between Mr. Wiedemann from UNIDO and Mr. R.L. Bwalya, Executive Director of INDECO, I participated in re-evaluation of the Kasama Maize Mill project. Original feasibility study of this project was done in the Economic Evaluation Unit of INDECO with application of the specialized UNIDO computer software COMFAR. Discussion during meetings chaired by Mr. Bwalya were based on my written expertise which is endorsed in this report. With the background of very dynamic current systemic reforms in the Zambian economy, repeated price changes of mealie-meal and deregulation of marketing arrangements in this area, proper assessment of project's viability in commercial terms poses serious intellectual problems. On the basis of discussions held, two updated and corrected versions of project appraisal (with application of COMFAR) were prepared. Under this assignment I cooperated with Mr. K.C. Mubita (Manager, Economic Evaluation Unit) and his staff, as well as discussed particular issues with Mr. J.E. Chulu, General Manager of the National Milling Company Limited, and financial directors of INDECO.

5. On invitation from the Secretariat of the Preferential Trade Area (PTA) I participated in the First Meeting of Prospective Investors of the PTA Multinational Triple Super-phosphate Fertilizer Project held in Kampala on 3 - 4 September, 1990.

   This was a follow-up of a UNIDO mission of 1988 under which, together with another UNIDO consultant Mr. P. C. Stone (technical expert) we have submitted a feasibility study on utilization of Uganda phosphate rock deposits in Tororo.

   There is a chance that this project, financially supported by the African Development Bank, various Government institutions and private investors from Kenya, may become the first multinational PTA industrial project integrating markets of Uganda, Kenya and Tanzania.

   During the meeting in Uganda I took part in financial negotiations between the representatives of the PTA Secretariat, Governments of Uganda, Tanzania and Kenya, as well as private investors and the African Development Bank. At the end of the conference I participated in preparation of the final document of the meeting (the Agreed Minute) by a committee chaired by Mr. Mwencha, Head of the PTA Industrial Division.

6. In conclusion, based on my work with the IPR department, I wish to make some recommendations to strengthen the work of the department.

The department should consider increasing the number of professionals to tackle the increasing demands for macroeconomic analysis both the national and global economic trends).

The collection of data and analytical work should be a constant and systematic activity of the department. It was observed that data collection was done in a rather short period proceeding the preparation of the Economic Report.

Professionals of the department, who are basically qualified economists, will still require support to strengthen their analytical capabilities in order to enable the department provide considered advice in strategic decision making at the national level, especially in the period of rapid systemic changes.

In my opinion above observations should be taken into consideration by UNIDO while preparing long-term strategy of cooperation with NCDP.

7. During my mission I have received considerable support from NCDP and various other Zambian Government institutions, as well as from the UNDP office. I am especially grateful to Mr. W. Kawana, Mr. G. Chivunga and Dr. P. Nkanza for helping me establish necessary contacts and create friendly environment conducive to my research.

Enclosures:

1. Economic Report 1990

   - Chapter I

   - Chapter II

2. Guidelines for preparation of the updated PIP (1990 - 93)

3. Expertise and comments the appraisal of the Kasama Maize Mill Project.

CHAPTER I

RECENT DEVELOPMENTS IN THE GLOBAL ECONOMY AND THEIR IMPACT ON THE ZAMBIAN ECONOMY

1.0 INTRODUCTION

1. As we enter the new decade of the 1990s and look back into the past quarter-century we can clearly see how complex and multidimensional the developments in the world economy were. Considerable changes have taken place; some of them favourable, some not. These exogenous developments will continue to exert even stronger influence on individual national economies, as particular elements of the world economy become more and more interrelated, and the world, as a whole, more integrated.

2.0. WORLD ECONOMY

2. After rapid expansion in 1988 the world economy generally slowed its pace of growth in 1989. This process, however, remained largely diversified. (Table 1.1). The most economically dynamic region - developing countries of East Asia - expanded slightly slower in 1989, but still at an impressive rate of 6 percent, despite economic setbacks in China. The developed market economies continued their long-term expansion and grew by 3.5 percent, above some pessimistic earlier predictions. In contrast, most countries in Africa, Latin America and South Asia were stagnating or even declining. Stagnation was also a predominant feature of East/Central European economies and the Soviet Union. All this [illegible] contributed to a slow-down in the total world output which grew by 3.1 percent in 1989, compared to 4.4 percent in 1988.

TABLE 1.1 Performance indicators in the world economy, 1989

Group and region	Real growth of GDP 1980-89	Real growth of GDP 1989	Growth of export Volume 1980-89	Growth of export Volume 1989	Gross domestic investment/GDP (a) 1980-89	Gross domestic investment/GDP (a) 1989
Industrial countries	3.0	3.6	4.8	7.6	20.9	21.5
Developing countries	4.3	3.3	6.1	8.1	24.3	24.6
Sub-Saharan Africa	1.0	3.5	0.0	10.1	16.1	15.2
East Asia	8.4	5.1	14.7	8.1	30.8	30.7
South Asia	5.5	4.8	6.1	9.6	22.3	21.4
Eastern Europe(b)	1.4	0.0	3.8	2.0	27.4	24.8
Middle East, North Africa and other Europe	2.9	2.5	6.4(b)	1.4(b)	25.9	24.1
Latin America and the Caribbean	1.6	1.5	4.9	4.4	20.1	20.6

a: Data for 1989 are preliminary
b: Estimates

Source: World Bank.

3. Despite some unfavorable trends in the world output, world trade remained relatively vigorous, though less dynamic than the year before. In 1989 the volume of world trade increased by some 6.7 percent, compared to a record high of 8 percent in 1988.

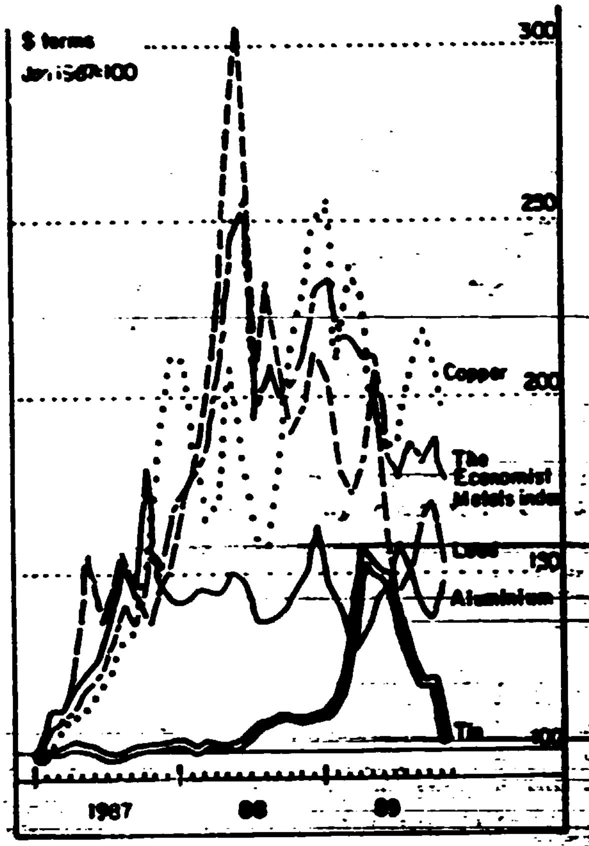
4. With only one exception of the East/Central Europe, structure and patterns of functioning of the world economy, remained the same and in most cases were an extension of trends started earlier. This was evidenced especially in the patterns of the regional diversity and regional pattern of resource flows among countries,leading to further increase of account imbalances among major economies and an aggravation of problems arising from indebtedness of the developing world.

5. In 1989 the movements of world prices were largely diversified and it is difficult to find one general pattern. Some key international prices remained practically unchanged or continued their previous trends; movements of some others changed dramatically. In 1989, on average, non-fuel commodity prices were rather stable. Fuel prices on the other hand, rose considerably during the year. The upward trend of crude oil prices prevailing at the end of the 1980s was reversed in January 1990. Spot prices of West Texas Intermediate Crude fell from the level of approximately $ 24 a barrel (end of 1989) to approximately $ 16 a barrel in June 1990. Due to the growing tensions in the Persian Gulf region, crude oil prices resumed accelerated growth in July and by August 2nd (Iraq's invasion of Kuwait) reached the level of nearly $ 25 a barrel. Afterwards, they skyrocketed approaching the psychological barrier of of $ 4[illegible] a barrel in September/October 1990.

6.The above changes in crude oil prices created serious challenges for small and medium size countries dependant on external oil sources and posed new problems for the world economy (including the possibility of recession in major world economic centers).

7. At the end of the decade there were many symptoms indicating that a long-term decline of metal prices was reversed (Figure 1.1A). Since January 1987 until mid-1988 metal prices rose on average by about 250 percent. The rate of growth of aluminum prices was the lowest, but still close to approximately 150 percent in the same period. During 1988 movements of metal prices were mixed, but in 1989 declining tendency resumed. By the end of 1989 prices fell on an average by approximately 80 percentage points, as compared to the highest 1988 levels.

Figure 1.1A METAL PRICES 1987-89



Source: The Economist

8. World copper prices grew considerably in the second half of the 1980s. Within this period the lowest yearly average was in 1986 ie. 934 British pounds per tonne, at the London Metal Exchange. The average yearly copper price grew in the second half of the 1980s by 157 percent, climbing up to the level of 1734 British pounds per tonne in 1989. Parallel to other metal prices some declining tendencies emerged in copper prices in the second half of 1989. Thus copper prices in the beginning of this year were considerably below 1989 average. During the year copper prices resumed their growth, stabilizing in the third quarter at 1530 - 1550 British pounds per tonne level.

9. The financial situation of the world in 1989 was rather unstable and not favourable for the developing countries. International interest rates rose, primarily in response to inflationary tendencies in developed market economies.

10. Exchange rates of major currencies were volatile and the American dollar appreciated significantly. This trend was reversed in mid-1990, improving the United States competitive position, yet again increasing uncertainty in world trade business.

11. Inflation became a greater concern to policy makers around the world, although both the magnitude and the tolerance of the problem varied widely :from approaching sensitive levels of over 5 percent in some of the developed market economies, to 5,000 percent in some countries of Latin America, where hyperinflation was rampant. In many developing countries economic adjustment and reforms have been contributing to inflationary pressures. The removal of subsidies and price controls (particularly on essentials) and devaluations of local currencies, inevitably raised domestic price levels in the short term - before expected supply side effects could come into the picture.

12. Despite serious problems surrounding the Persian Gulf crisis, long-term progress in relaxation of political and military tensions in the world is still widely expected. Thus, convertion of a fraction of huge military expenditures of industrialized countries into the debt-relief aid to developing countries may become finally more and more viable alternative in the near future.

13. At the same time, recent changes in East European region have increased a number of countries which compete to receive external financial support from international sources. There is some anxiety among developing countries, that Eastern Europe with developed infrastructure, cheap and skilled labour may appear more attractive for international business and financial institutions, diverting a considerable portion of financial aid, which might have been allocated to developing countries.

14. However, existing potential in reducing military budgets is enormous. In the 1980s world military expenditures grew to unprecedented peacetime levels estimated at US $ 1 trillion a year (half of this - NATO expenditures), accounting for approximately 5 percent of total world income. Estimates by international organizations prepared before the Persian Gulf crisis provided us with new experience indicate, that by the end of this decade defence outlays could be brought to half of their current levels without jeopardizing the military balance between the superpowers.

3.0 DEVELOPED MARKET ECONOMIES

15. In 1989, the long-term expansion of the developed market economies still continued, albeit, at a slower pace. Within the group of major industrial countries only the Federal Republic of Germany performed much better than the year before. In general, at the end of the decade some major trends prevailing at the beginning of the 1980s were reversed. Western Europe accelerated its growth, while Japan and North America experienced a slow-down of their expansion.

16. In 1988 and 1989, in almost all the major industrial economies, capacity utilization reached its highest level and unemployment decreased to the lowest level in the decade. In anticipation of potentially accelerated inflation monetary policy was tightened in most of these countries. Short term interest rates resumed a steady climb; in some countries the increase in nominal interest rates in 1989 was greater than the rise in inflation, further increasing already high real interest rates. There was an evidence of a slowing down of the United States economy in 1989, partly as a result of restrictive monetary measures introduced earlier. Anxiety about recession in the USA grew considerably in mid-1990, as the Persian Gulf Crisis triggered a dramatic fuel price increase, influencing directly and indirectly the overall cost structure.

17. External imbalances among different groups of countries, and within particular groups of countries remained large or increased during 1989. The Japanese current account surplus fell by more than 25 percent in dollar terms and came close to that of the Federal Republic of Germany which experienced at the same time a slight upward tendency. Simultaneously, serious external imbalances appeared in a number of other countries (e.g Canada, Australia, United Kingdom). The trade deficit of the United States decreased in 1989 by roughly the same amount as the Japanese surplus.

18. In view of the German reunification process, the further integration of the European Community in 1992, as well as the dramatic systemic changes in Eastern/Central Europe, the whole European continent is emerging as a key driving force in the world economy in the 1990s. Some analysts have already declared the decade of the 1990s as the European decade. However, the pivotal points of the world economy are likely to be determined by the triangle: Europe - Pacific Rim - the United States, with the leading role of Germany and Japan in the first two regions.

4.0. DEVELOPING ECONOMIES

19. Distribution of income among particular groups of developing countries has changed considerably over the past quarter-century (Figure 1.2). The East Asian region, increased its share in developing countries' real income from 22 to 37 percent. Sub-Saharan Africa's share dropped from 12 percent in the 1960s to only 7 percent at the end of the past decade. At the same time the Sub-Sahara African fertility rates were well above average, leading to rising population share and declining results in per capita terms.

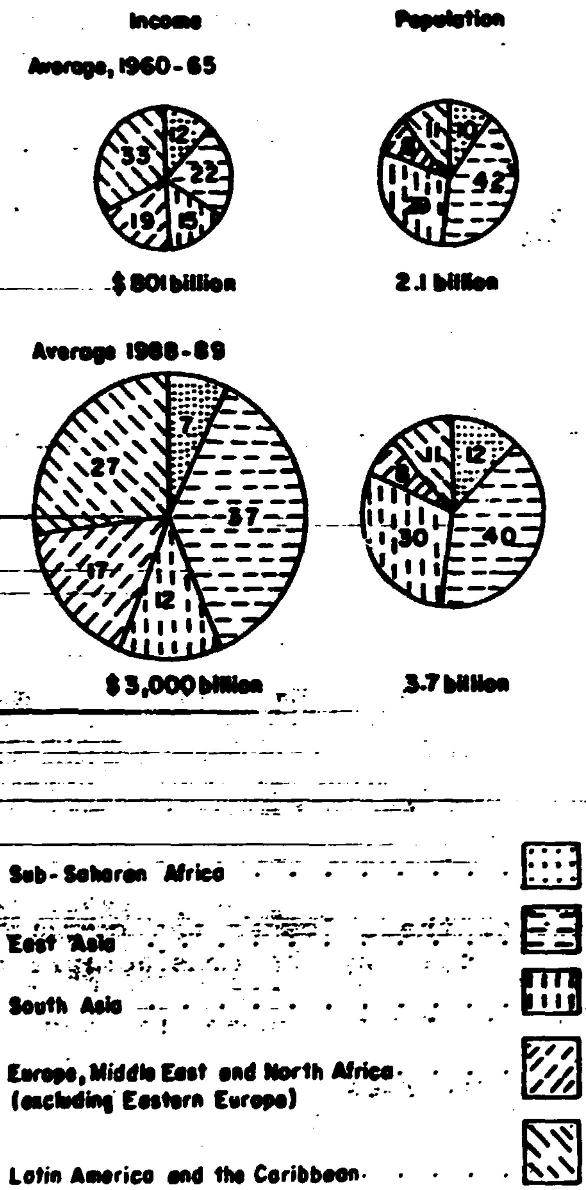
20. In 1989, regional differences in economic performance among various groups of developing countries further deepened (Table 1.2). The East Asian developing countries managed to diversify their economies and achieved in some sectors very advanced standards of production, even challenging traditional producers from developed market economies. On the other hand, for the majority of countries in Africa, the dominant link with the world ~~economy remained via~~ traditional, undiversified exports of primary commodities.

In line with a predominant tendency to decrease the primary commodity-intensity of the global output, this led, to a relative deterioration of the continent's position in the world economy. These unfavourable developments have been further exacerbated by the fact that during the 1980s the prices of many commodities - traditional export items of African countries, fell down to their lowest levels (in real terms) in many decades. It was only during the dynamic expansion experienced in 1988 that prices of some minerals, metals (including copper) and agricultural raw materials moved upwards; in most cases, however, this trend has decelerated (Figures 1.1A, 1.1B).

21. A comparison of the 1970s and the 1980s reveals unfavourable long-term tendencies constraining the growth of the developing countries. The rate of growth in Latin American countries went down from 5.5 percent to about 1 percent. In the 1980s African countries expanded at a rate of merely 0.5 percent, compared to 4.9 percent in the 1970s. GDP per capita in these two groups of countries fell dramatically, as well. The same tendencies prevailed in West Asian and Mediterranean countries. Only China and South and East Asian countries significantly improved their performance in the last decade.

CHANGES IN THE DISTRIBUTION OF INCOME AND POPULATION IN THE DEVELOPING WORLD

(Percentage Share)



Source: World Bank

Note: Income is in 1980 dollar.

Figure 1-2

22. Both domestic and external factors have to be taken into consideration while analysing divergences in the rates of growth of particular groups of countries. In particular, it is widely admitted that the dramatic fall in commodity prices and terms of trade largely contributed to the worsening of the economic situation in the African countries. Between 1980 and 1988, the real prices of non-fuel commodity exports from developing countries declined by about 40 per cent. In the same period African and Latin American terms of trade fell by 40 and 25 percent, respectively.

TABLE 1.2 Performance indicators, by developing region, selected periods

Region	Growth of real per capita GDP (percent) 1965-73	1973-80	1980-89	Gross domestic investment/GDP 1965-73	1973-80	1980-89(a)
Sub-Saharan Africa	3.2	0.1	-2.2	16.2	20.8	16.1
East Asia	5.1	4.7	6.7	24.2	29.7	30.8
South Asia	1.2	1.7	3.2	17.1	19.9	22.3
Eastern Europe(b)	4.8	5.3	0.8	28.3	33.8	29.4
Middle East, North Africa and other Europe	5.5	2.1	0.8	23.4	29.2	25.9
Latin America and the Caribbean	3.7	2.6	-0.6	20.7	23.9	20.1

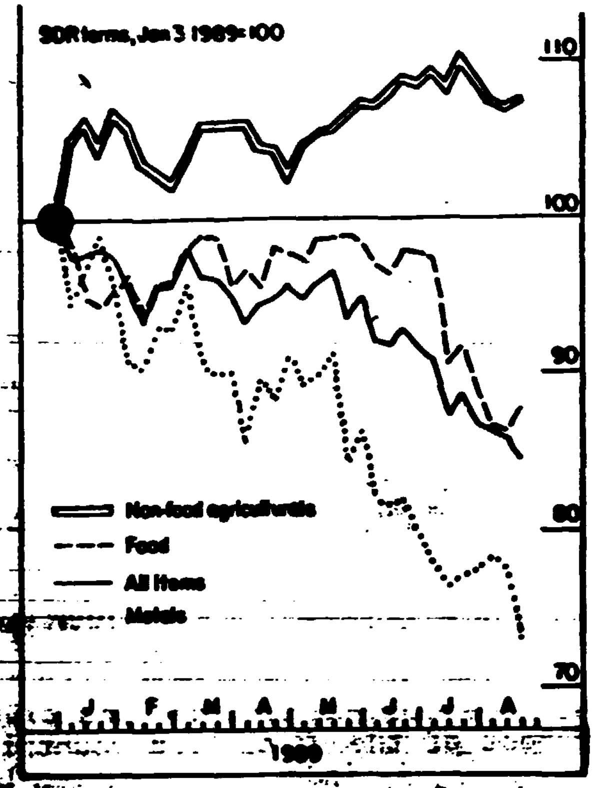
a: Data for 1989 are preliminary

Source: World Bank

23. The impact of these losses was compounded by the debt crisis and exacerbated by the considerable rise of interest rates in the 1980s. The combination of external shocks reduced real disposable income in most of the African economies. In view of this situation many African countries were looking for new ideas and ways out of the crises. They adopted austerity measures, various stabilization and adjustment programmes, most of which led to very difficult transition periods with new consumption constraints and yet to be achieved supply side targets.

24. On the whole, exports in value terms of the developing countries increased by 12 percent in 1989. The rates of growth of particular regions were, however, highly varied, with energy exporters clearly in the lead (Figure 1.3). At the same time imports of developing countries grew by about 11 percent in value terms.

Figure 1.1B THE ECONOMIST COMMODITY
PRICE INDEX



Source: The Economist

However, the trade balance improved only in the group of oil exporters, while a relative deterioration took place in some of the newly industrialized economies, as well as in the group of oil importers, as a whole. The Persian Gulf Crisis may still exacerbate these tendencies. The structure of developing countries' trade flows in the second half of the 1980s changed only marginally, indicating difficulties which these countries have been facing in trying to promote export diversification. The rate of growth of developing countries' exports indicates a strong, long-term dependance on the rate of growth of industrial production in the developed countries (Figure 1.4).

Figure 1.3 Real export performance of developing countries, 1980 to 1989

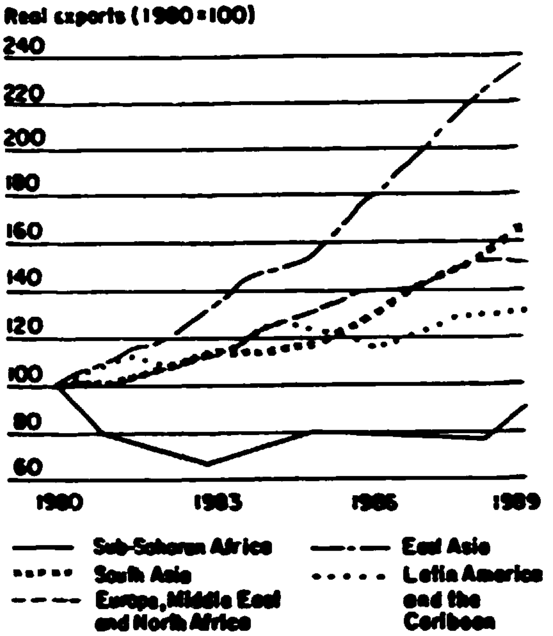
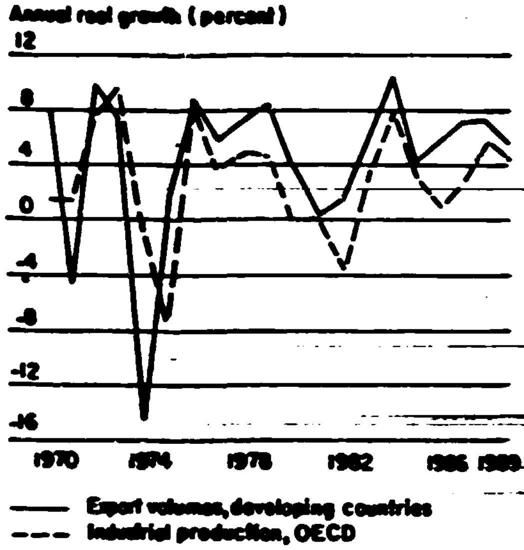


Figure 1.4 Growth of OECD industrial production and developing country exports, 1970 to 1989

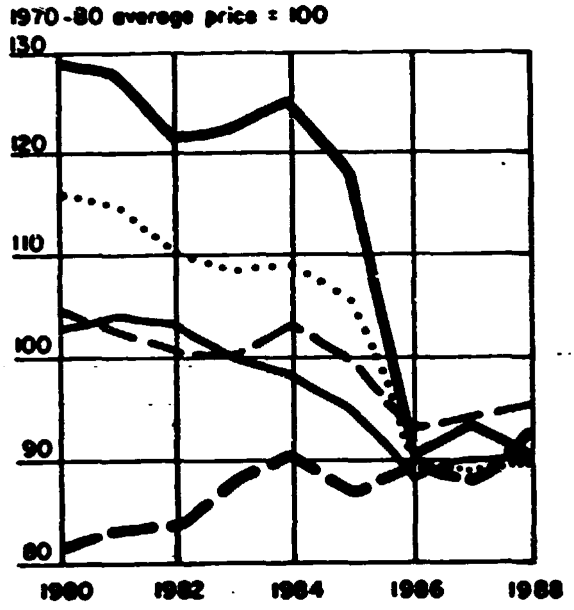


Source: World Bank

25. External indebtedness remained one of the major growth barriers for most of the developing countries, particularly in Africa. Many highly indebted countries have been using a substantial portion of export earnings and restricting imports largely because of their need to service debt. Sub-Saharan Africa, followed by Latin America, were the regions which suffered most as a result of unfavourable developments in international trade in the 1980s. A general decline in the terms of trade of developing countries in the past decade (Figure 1.5) affected foreign trade of these two regions most adversely. The fall in prices during the 1980s cost Sub-Saharan Africa 15 percent of its exports' real import purchasing power relative to the 1970s. Despite the persistence of the debt problem, at the end of the decade some positive phenomena were emerging. Among them, the concept of commercial debt reduction began to be applied in some, selected countries. For the first time, the developing countries debt stock (measured in terms of dollars) declined.

CHANGES IN THE TERMS OF TRADE

BY DEVELOPING REGION, 1980 TO 1988



Sub-Saharan Africa

South Asia

Europe, Middle East & North Africa

East Asia

Latin America & the Caribbean

Source: World Bank

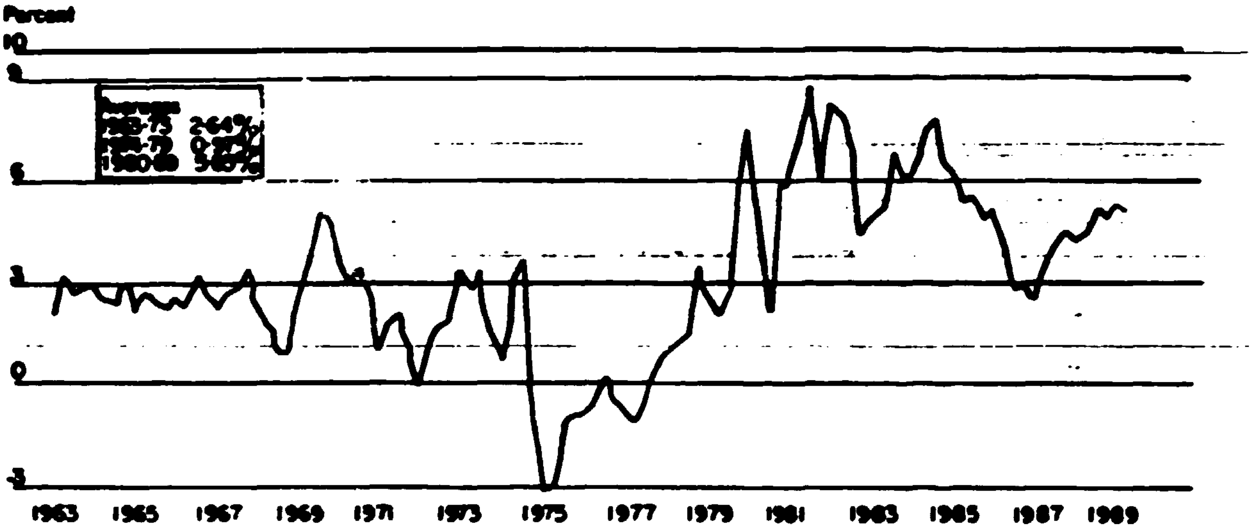
Figure 1.5

26. Real interest rates were exceptionally high during the 1980s (Figure 1.6). The major reasons for this unfavourable development included a decline in industrial countries' savings, large swings in the major currencies and uncertainty regarding future exchange rate movements, as well as global current account imbalances. It has been established that the additional burden of high interest rates is affecting first of all the Latin American region, followed by Sub-Saharan Africa and South Asia.

In 1989, international interest rates rose for the second consecutive year, making efforts to service the debt even more difficult. This unfavourable trend continued in 1990.

27. The combination of domestic policies pursued in the past decades and external factors influencing growth have largely determined the present position of particular groups of developing countries in the world economy.
The performance of developing countries in the 1980s varied according to their sensitivity to particular types of unfavourable world economic events and their ability to adjust to shocks over the decade. Countries where the domestic policies were not supportive to maintaining adequate levels of national savings, investment, balanced budgets, curbing inflationary pressures or facilitating active exchange rate policies, entered the decade with greater underlying imbalances and structural problems. This was the case for most of the Sub-Saharan countries. As already existing imbalances were often hidden behind heavy borrowing and protection of local markets, these countries found it very hard to adjust to the shocks of the 1980s.

Figure 1.6 Real interest rates, 1963 to 1989



Note: The real interest rate is calculated as the London interbank offered rate (LIBOR) minus the U.S. GDP deflator.

Source: World Bank

28. Towards the end of the decade many developing countries embarked upon decisive institutional reforms and consolidated efforts to reallocate resources. This process, however, is sometimes slow and response of foreign partners and local private investors is weak.

In Sub-Saharan Africa the problems are still aggravated by the lack of developed infrastructure, heavy dependence on exports of primary commodities and, in some cases, underdeveloped entrepreneurial and managerial skills. Thus, under these circumstances the adjustment of African developing countries is likely to be a long and difficult process. Even assuming considerable progress in domestic reforms, it is expected that the performance of African countries will depend heavily in the short and medium-term on exogenous factors such as weather and the trends of world commodity prices.

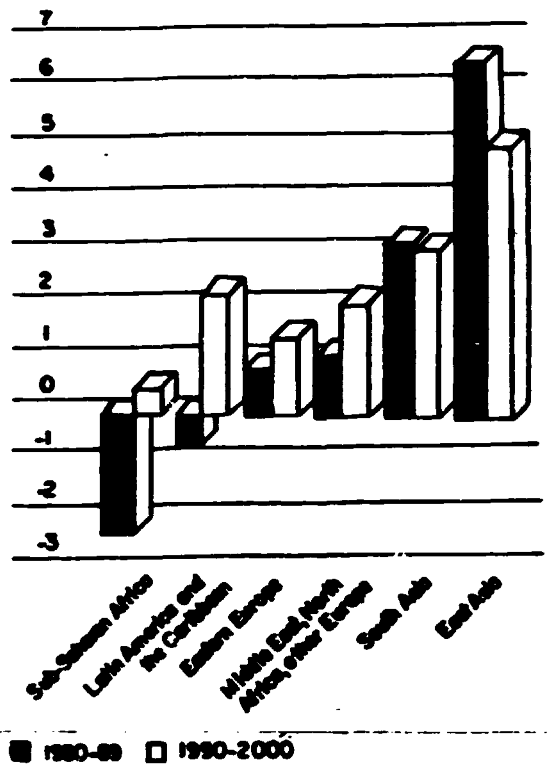
TABLE 1.3 Prospects for the 1990s

	Real GDP growth rates			Gross domestic investment/GDP		
	Trend	Recent experience	Forecast	Trend	Recent experience	Forecast
Group and region	1965-80	1980-89	1989-2000	1965-73	1973-80	1980-89(a)
Industrial countries	3.7	3.0	3.0	2.8	2.5	2.6
Developing countries	5.9	4.3	5.1	3.4	2.3	3.2
Sub-Saharan Africa	5.2	1.0	3.7	2.0	-2.2	0.5
East Asia	7.3	8.4	6.6	4.8	6.7	5.1
China	6.4	10.1	6.8	4.1	8.7	5.4
Other	8.1	6.4	6.3	5.5	4.2	4.6
South Asia	3.6	5.5	5.1	1.2	3.2	3.2
India	3.6	5.6	5.2	1.2	3.5	3.3
Other	3.0	5.0	4.8	1.2	2.2	2.4
Eastern Europe	5.3(a)	1.4(a)	1.9	4.5(a)	0.8(a)	1.5
Middle East North Africa, and other Europe	6.5	2.9	4.3	3.9	-0.8	-2.1
Latin America and the Caribbean	6.0	1.6	4.2	3.6	-0.6	2.3

a) Preliminary
Source: World Bank

29. Short-term prospects for developing countries are not very optimistic (Table 1.3). Despite the fact that the rate of growth of these countries in 1989 was the lowest in the past six years, its further decline in the nearest future can be foreseen. Some acceleration of economic growth is possible only in the long run. Even without major external shocks the rates of growth of African countries were not likely to improve in 1990. There were some hopes for moderate improvement in 1991 and later during the decade (Figure 1.7), but the Persian Gulf Crisis and the rapidly rising crude oil prices in mid-1990 make it very difficult to adhere to this scenario. What is worse, the initial positive results of ongoing economic reforms, which were expected to appear across the continent in the beginning of the decade of the 1990s, might be largely endangered by these unfavourable events.

Figure 1.7 Real per capita growth in developing countries in the 1980s and World Bank forecast values, 1980 to 2000
(percent)



Source: World Bank

5.0. <u>IMPACT ON THE NATIONAL ECONOMY</u>

30. In Africa, the growth of output during 1989 is estimated at 2.8 percent. Thus, for the third consecutive year the whole continent was improving its performance. However, this increase in output fell short of population growth (3.1 percent). In per capita terms it was another year of relative decline. Most of the forecast assume, that the overall performance of developing countries in the 1990s might be slightly stronger than in the past decade, as a result of improvements in domestic policies and greater external assistance. Yet, Sub-Saharan Africa per capita incomes are not likely to rise in the first half of the decade and the World Bank predicts a moderate growth of about 1 percent a year in 1995-2000.

31. Within the African continent Eastern and Western sub-regions witnessed the best economic performance in the past decade. The most dynamically growing sector in African countries was agriculture; considered as the main driving force for economic expansion in most of the countries. Favourable weather conditions and improved government policies were conducive to the growth of this sector. This growth however, could barely match that of the population.

While oil-exporting countries benefited from higher oil prices, most of the mineral-producing countries, like Zambia, were unable to scoop potential benefits offered by relatively improved prices in international markets due to long-term production barriers coupled with current foreign exchange constraints.

32. Generally favourable weather conditions in the last two years were an important exogenous factor contributing to a visible expansion of the agricultural sector in many African countries. Other positive developments included improved availability of domestic and imported agricultural inputs.

33. The year 1989 witnessed some positive changes in the manufacturing sector. An overall capacity utilization was clearly on an increase, though below the world standards.

34. Exports of Sub-Saharan Africa, in real terms, did not increase at all during the 1980s (Table 1.1), however, they considerably accelerated at the end of the decade. Export volume of the region surged by 10 percent in 1989, moving up the GDP growth to 3.5 percent, much above the average level of GDP growth for the whole decade (only 1.0 percent).

35. Supported by favourable tendencies in prices of oil and minerals, export earnings of the whole continent went up in 1989 by approximately 16 percent and reached the level of 67 billion US dollars. At the same time the cost of African imports increased by 10 percent and rose to approximately 76 billion US dollars. Imports from Asia tend to play more and more significant role in the African trade. Apart from this recent development the pattern of trade in the continent is still very traditional: trade flows actually have not changed much since the pre-independence times. Another observation is, that there is still a very limited scope of the inter-African trade. It accounted for less than 5 percent of total exports in 1989 and indicates serious difficulties in implementing of the idea of the regional cooperation.

36. African external debt continued to grow, despite positive tendencies in export earnings. In 1989 African debt exceeded the level of 250 billion US dollars.

The stock of debt is already equivalent to approximately 40 percent of the continent's GDP. Recent inflows of official development assistance to African countries are below the level of their current debt service obligations.

37. Official creditors account for the bulk of the total debt of highly indebted, low-income countries. The principal creditors are trying to reduce the debt burden of this group through the mechanisms agreed to at the 1988 Toronto summit. The debt of sixteen Sub-Saharan African countries has been rescheduled under the new protocol. The Special Programme for Africa, which provides concessional balance of payments assistance to low-income countries that are undertaking significant reforms, is expected to be extended beyond 1990, when the current programme ends. These, together with the IMF's Enhanced Structural Adjustment Facility, are the main sources of multilateral concessional assistance.

38. Investment remained strongly depressed in the Sub-Saharan region (Table 1.1). Average Gross Domestic Investment/GDP ratio for the whole decade was only 16.1 percent, considerably below the average level for all developing countries (24.3 percent), and indicating a decline in 1989.

39. It is widely admitted that if the patterns of regional income growth of the 1980s were to be repeated in the present decade, the results could be especially challenging for Sub-Saharan Africa. If the present trends were to be continued, the estimated population of the region of 450 million would increase by approximately 165 million, decreasing todays' per capita incomes by 20 percent. In view of this, in most of the African countries there is a wide recognition of the need for structural reforms, institutional change and explicit population policies. As a result, the number of countries experimenting with domestic economic reforms is unprecedented.

40. The changes in South Africa, as well as serious economic and political efforts in the field of systemic reforms of many developing African countries may create a conducive environment to promote economic development. However, in most of the countries, including Zambia, the discussion is still open about the nature of the changes required and about the ways of their introduction.

41. In short and mid-term horizon, Zambia and other African countries will have to pursue their development policies under generally unfavorable external conditions, facing numerous barriers and constraints. In view of various phenomena on world markets (e.g.: skyrocketing oil prices, danger of recession in leading economic centers, high interest rates, uncertain future growth of world demand for primary export goods, mounting protectionism, huge payment imbalances), the

prospects of rapid acceleration of Zambia's economic growth are clouded and achievement of ambitious socio-economic goals has to be considered a difficult task.

42. Zambia and other severely indebted, low-income economies, are expected to encounter the worst conditions for economic growth in the present decade. Among other things, these countries suffer from deeply rooted, structural weaknesses (Table 1.4).

43. Zambia belongs to the group of African developing countries which depend on a narrow range of primary commodities for exports and have a weak financial and infrastructural base. High population growth still aggravates their situation. In light of these problems intensification of international initiatives to ease the debt burdens and lower the barriers to world trade is becoming of utmost importance.

Table 1.4 Comparative indicators for severely indebted low and middle-income countries
(percent unless otherwise)

Indicator	Low-income	Middle-income
Average population growth (1988)	3.1	2.0
GNP per capita (1988 dollars)	276.0	1782.0
Gross domestic investment as a share of GDP (current prices, 1987-88)	14.4	22.4
Exports as a share of GDP (1987-88)	17.4	16.3
Imports as a share of GDP (1987-88)	23.3	13.7
Share of manufacturing in exports (1987-88)	6.2	45.0
Share of nonfuel commodities in exports (1987-88)	52.5	30.3
Official development assistance as a share of GNP (1987)	3.2	0.5
Under 5 mortality rate (per thousand, 1985)	191	86
Primary net enrollment rate (1985)	50	89

Source : World Bank

44. Africa's Priority Programme for Economic Recovery of the Organization of African Unity (OAU) has announced a change in the general economic policy profile in the region. A shift has been made from the post-industrialization strategy stressing import substitution objectives, to be achieved via establishing new industries requiring considerable investment imports. The new strategy outline points out and gives priority to agriculture and resource-based industrial projects, with particular emphasis on small and medium-scale enterprises.

Despite recent slow-down in agriculture in Zambia this sector has a great potential and is considered to be one of the major driving forces for economic growth in the country in the 1990s.

45. Only drastic changes in economic policies within particular groups of countries can reverse the unfavourable tendencies in the future. With present policies, prices and exchange rates, global disequilibria are likely to be maintained, if not increased in the 1990s. Therefore, further reconsiderating and strengthening of adjustment policies are called for in both developed and developing economies. Zambia's attempt to introduce an ambitious and radical adjustment programme is an example of understanding of such necessity, despite all difficulties. Zambia's example is exposing at the same time the complexity of such a task, and is indicating potential social challenges to radical economic reforms.

46. Despite all the difficulties and challenges stemming from the developments in the Zambia's external environment, there is no alternative to the policy of openness and active participation in the global economy. Policy of isolation should be rejected as leading in the long-term to inefficient solutions. Zambia should use its links with the external economic environment to derive relative and absolute advantages from the foreign trade. This environment may provide the country with the information required to restructure and adjust the economy to the long-term trends in the world. Therefore, a modern foreign trade management system is needed with an active exchange rate policy, as the focal point.

47. The exchange rate policy should generate sufficient motivation to promote export expansion and its diversification, and, at the same time, should indicate the real cost of import expenditures. Zambia has already embarked upon a package of important reforms within the system of foreign trade management and has introduced incentives for export development through repeated devaluation of the local currency. In order to improve the international competitiveness of the national economy, this orientation of the economic policy will be continued in the future.

48. Given the present situation in Zambia's balance of payments, the mounting debt and deep-seated disproportions in the foreign trade, the country will remain very sensitive to future developments in the external environment. From the point of view of a country of the Zambia's size and potential, most of these developments have to be considered as strictly exogenous and independent from the country's influence.

However, the domestic policies in the field of the foreign trade management system may play an active role in adjusting the national economy to the recent trends in the technical progress in the world and promoting development of non-traditional exports. In 1989 Zambia has made a considerable progress in creating a modern system of foreign trade regulation. Further changes, in line with the targets pointed out in the Policy Framework Paper 1989 - 1993, are required to meet all the challenges of highly competitive situation in the global economy.

49. As the progress in diversification of the Zambia's production and export structure is advancing slowly, in the short-and medium-term the country's foreign trade balance will largely depend on developments on world copper markets, as well as country's ability to reduce emerging production barriers in the copper industry. Recent favourable trends on the world copper markets have been reversed and the future is rather uncertain.

50. World consumption of copper grew steadily from 1982 onwards supported by continuous expansion in the developed economies. In addition to this, consumption of base metals increased significantly in some developing countries (e.g. South-East Asian countries, Latin America, China). In the absence of substantial excess capacity, the demand pressure led to considerable increases in metal prices, after the producers' stock were drawn down.

This comfortable situation from the producers' point of view, caused mainly by the tightness on the supply side, continued, however, only into the first half of 1989. World production levels were gradually increased and a slow-down in some important industrial centers (including the USA) followed. Metal prices including copper, were already on a decline in the first half of 1990 (Table 1.5). In the long run prospects of copper industry are vague, but the developments in this sector may heavily depend on the pace and directions of the technical progress in the world. It is expected that new and advanced materials will be soon developed which may replace metals in their traditional application. These could be mineral substitutes, such as plastics, or new alloys using various exotic components - all cheaper, more efficient and more corrosion resistant. Even if the moderately declining demand from developed economies could be counterbalanced by the growing consumption in the developing countries, Zambia's copper earnings are likely to be depressed by falling copper prices, as predicted in the international forecasts.

51. On the import side, dramatically growing oil prices already are, and may rerain in the short-and medium, a considerable burden for the national economy, adversely affecting the domestic cost structure. Future trends of oil prices are difficult to predict, but are not likely to rapidly decline to the low levels of the beginning of 1990. On the other hand, a wider application of alternative fuel sources in Zambia may be difficult even in the medium-term and is constrained by the financial factor.

52. In the 1980s the developed economies significantly improved their terms of trade, especially in the second half of the decade. Within the group of the developing economies, only the Newly Industrialized Countries (NICs) of South-East Asia experienced favourable terms of trade in the same period. Economic development of Zambia and other countries - primary commodities exporters has been slowed-down by deteriorating relations of exchange in the foreign trade. Declining Zambia's terms of trade are likely to continue in the 1990's unless the structure of exports is changed to include a larger share of processed goods.

Table 1.5
THE ECONOMIST Commodity Price Index
June - October 1990.

1985=100	June19 1990	June26 1990	Oct2 1990	Oct9 1990	% change on one month	one year
Dollar index						
All items	126.7	126.3	128.7	132.7	-2.6	1.1
Food	98.5	97.9	94.6	100.5	2.5	-3.7
Industrials						
All	154.6	154.5	162.5	164.7	-5.4	[illegible]
*NFA	139.9	141.7	131.6	132.9	-1.3	-2.9
Metals	165.0	163.5	184.6	187.3	-7.4	0.9
Sterling index						
All items	94.4	93.4	87.4	86.3	-8.5	-20.0
Food	73.4	72.4	64.2	65.4	-3.7	-18.0
Industrials						
All	115.2	114.2	110.3	107.1	-11.2	-21.2
*NFA	104.2	104.7	89.3	86.4	-7.4	-23.2
Metals	122.9	120.9	125.2	121.8	-13.0	-20.2
SDR index						
All items	97.6	97.3	93.5	94.3	-6.2	-10.6
Food	75.9	75.4	68.7	71.4	-1.2	-8.3
Industrials						
All	119.1	119.0	118.0	117.0	-9.0	-11.9
*NFA	107.8	109.1	95.6	94.4	-5.0	-14.1
Metals	127.1	126.0	133.9	133.0	-10.8	-10.7
GOLD $ per OZ	349.75	[illegible]	396.50	396.00	+3.9	+9.4

*NFA = Non-food agriculturals
Source: The Economist

53. In mid-1990 there were no signs that the recent upward trend of international interest rates might be reversed soon, easing the Zambia's debt service burden. At the same time volatility of exchange rates of the major world currencies continued to increase uncertainty in the world trade, with the German mark and the Japanese yen significantly appreciated in relation to the weakening American dollar, as well as the British pound on an increase after Great Britain decided to join the European Monetary System.

CHAPTER II

STATE OF THE DOMESTIC ECONOMY

1.0 INTRODUCTION

1. The year 1989 may be considered as an important turning point in the recent economic strategy of Zambia. Zambia has entered the 1990s with new hopes and facing new challenges, as the country embarked upon a package of radical reforms announced in June/July 1989. These reforms have been endorsed by the World Bank and the International Monetary Fund and have received considerable financial support from international community. Despite a difficult economic situation and hardships of the transition period the country has proved its commitment to a successful implementation of basic economic reforms.

2. The challenges of the transition period originate from both the internal, as well as the external factors. The reforms introduced since mid-1989 (eg. deregulation of prices, repeated devaluations of the local currency, new monetary policy) have created new, dynamically changing conditions for conducting economic activities in Zambia. At the same time Zambia remained strongly affected by continued unfavourable exogenous trends of the world economy pertaining to highly indebted African countries. In the second half of 1990 these long-term trends and the usual uncertainties of world markets were exacerbated by the global oil crisis resulting from the political and military events in the Persian Gulf.

3. As the problems within the Zambian economy are deep-rooted, and the efforts to bring about radical reforms have just started it is foreseen that the difficult economic situation prevailing in Zambia cannot be reversed rapidly. Rather, it is expected that some positive results of the reforms and the adjustment programme may appear only in the medium and long-term. During the transition period a wide understanding of economic challenges is needed, as well as a broad social support for the new programme.

4. Among numerous economic problems which the Zambian economy is facing now, two seem to be critical. Firstly internal imbalances evidenced by the high rate of inflation could undermine the country's adjustment efforts. Stabilization of economic environment is therefore as a major precondition to successfully continue economic reforms and the adjustment programme.

The other one is connected with a long-term challenge to diversify the structure of the economy. Zambia's attempts in this respect have not been successful so far and the country is still vulnerable to exogenous changes in the price of a single commodity, copper, which remains the backbone of the economy.

5. In order to address above mentioned issues the Government prepared two major economic policy documents: the Economic and Financial Policy Framework 1989-1993 and the Public Investment Programme 1989-1993. The Financial and Economic Policy Framework is drawn out of the Fourth National Development Plan (FNDP) 1989-1993 and formulates the economic policy framework required to achieve identified objectives of highest priority:

- increasing growth in non-metal sectors and promoting non-traditional exports;
- reducing inflation by combined fiscal and monetary measures.

Financial and Economic Policy Framework includes the timetable of adjustment and structural measures until 1993 and is the major guideline for development of economic policy in the short and medium-term.

6. At the end of 1989 the Public Investment Programme (PIP) 1989 - 1993 was developed. This document is complementary to the Policy Framework and is also drawn out of the FNDP. The PIP is the expression of the most recent Government's priorities and is constrained by the verified, actual funding available. Under the PIP, highest priority has been given to rehabilitation and maintenance of already existing facilities. Particular emphasis is on completion of on-going projects in order to avoid losses in already frozen expenditure.

2.0 TRENDS AND STRUCTURE OF GDP

7. The initial basis for economic development in 1989 was very demanding. In 1988 Zambia's Gross Domestic Product (GDP) expanded at an exceptionally high rate of 6.3 per cent (in real terms) largely due to favourable movements in copper prices and good weather conditions contributing to high performance of the agriculture and agro-based industries. In 1989, the rate of growth of the national economy dropped resulting in the lowering of the GDP by 1 percentage point (in real terms), as compared to the previous year's level. A further deceleration of growth by about 2 percentage points is foreseen for 1990 (Table 2.1 and 2.2.).

TABLE 2.1

GROSS DOMESTIC PRODUCT BY KIND OF ECONOMIC ACTIVITY
IN PRODUCER'S VALUE AT CURRENT PRICES (Kwacha million).
1985 - 1990

Kind of economic activity	1985	1986	1987	1988	1989	1990
Agriculture, Forestry and Fishing	925.2	1577.8	2180.4	5505.5	10562.1	17955.6
Agriculture	788.1	1303.3	1707.8	4048.4	8126.4	13814.9
Forestry	59.5	125.6	179.0	435.8	1006.7	1711.4
Fishing	77.6	148.9	293.6	571.3	1429.0	2429.3
Mining & Quarrying	1101.9	2354.9	2689.0	3155.2	7719.8	8808.3
Metal mining	1056.8	2280.4	2584.5	3009.2	7519.8	8368.7
Other mining & Quarrying	45.1	74.5	104.5	146.0	200.0	439.6
Manufacturing	1616.5	2936.3	5547.0	9495.6	21933.0	45913.9
Food, Beverage & Tobacco	600.2	843.3	1283.9	2584.5	5170.4	15988.1
Textile & leather Industries	212.6	289.8	459.5	609.8	6231.9	2802.6
Wood & Wood Products	43.8	88.4	74.0	146.8	510.2	999.7
Paper and Paper Products	95.4	166.4	344.9	658.2	1287.8	4808.9
Chemical, Rubber and Plastic Products	194.8	370.5	592.1	751.0	1156.5	3134.5
Non-Metallic Mineral Products	129.7	153.7	200.5	1730.0	1888.5	4381.6
Basic Metal Products	13.2	23.9	59.3	82.3	107.5	348.7
Fabricated metal Products	309.0	960.7	2448.7	2200.9	3240.7	12521.3
Other manufacturing n.e.c	17.8	38.6	85.0	203.0	322.2	928.4
Electricity, Gas & Water	71.0	166.2	238.5	283.2	398.1	493.7
Construction	183.2	292.2	393.8	618.4	884.0	3739.4
Wholesale and Retail Trade	763.0	1638.2	2778.3	3440.4	5109.0	7724.1
Restaurants and Hotels	181.1	261.7	427.4	735.5	1363.3	2151.2
Transport, Storage and Communications	342.3	594.3	839.6	1206.8	2880.6	4304.6
Rail Transport	103.3	181.7	244.1	342.1	779.4	1105.1
Road transport	95.5	166.5	249.3	358.8	881.0	1362.1
Other Transport & Services Allied to Transport	63.1	110.5	155.6	221.0	523.7	778.6
Communication	80.4	135.6	190.6	284.9	696.5	1058.8
Financial Institutions	228.9	445.2	735.1	1083.8	1781.1	2514.7
Real Estates and Business Service	454.6	751.8	1155.9	1483.0	2072.0	3586.4
Community, Social & Personal Services	934.3	1169.2	1487.6	2170.5	2704.6	5598.2
Public Admin. (& Defence)						
Public Sanitary Services	391.7	472.8	623.8	879.6	1155.9	2822.7
Education	292.1	384.1	436.2	690.0	776.4	1416.0
Health	112.6	124.6	149.2	272.9	338.3	603.2
Other Community & Personal Services	137.9	187.7	278.4	328.2	434.0	756.3
Import duties	334.1	900.2	1506.4	1558.1	3105.3	5502.0
Less: Imputed Banking Service Charges	64.2	124.9	201.0	297.2	488.4	689.5
TOTAL GDP	7071.9	12963.1	19778.9	30020.9	60024.5	107602.0

* Provisional; estimates are based on partially available data
Source: CSO

TABLE 2.2 GROSS DOMESTIC PRODUCT BY KIND OF ECONOMIC ACTIVITY IN PRODUCER'S VALUE AT CONSTANT 1977 PRICES. (Kwacha million) 1985 - 1990

Kind of economic activity	1985	1986	1987	1988	1989	1990
Agriculture, Forestry and Fishing	343.8	373.8	365.6	436.2	424.5	393.4
Agriculture	303.6	331.7	326.7	389.6	379.0	351.2
Forestry	15.9	14.4	14.2	16.8	16.4	15.2
Fishing	24.3	27.7	25.2	29.8	29.1	27.0
Mining & Quarrying	185.8	176.5	184.2	160.4	175.6	180.7
Metal mining	179.3	169.9	178.7	154.2	169.4	174.4
Other mining & Quarrying	6.5	6.6	5.5	6.2	6.2	6.3
Manufacturing	421.6	425.3	462.9	547.0	544.1	524.9
Food, Beverage & Tobacco	176.9	179.8	189.2	249.6	241.1	266.4
Textile & leather Industries	74.3	63.5	68.1	76.4	79.2	69.9
Wood & Wood Products	9.3	9.1	8.1	8.0	9.4	8.2
Paper and Paper Products	15.3	19.3	29.9	34.7	36.3	36.4
Chemical, Rubber and Plastic Products	42.9	41.7	39.0	39.5	36.4	37.0
Non-Metallic Mineral Products	26.1	19.1	21.2	25.2	25.2	27.0
Basic Metal Products	3.6	3.3	2.6	2.8	2.8	1.9
Fabricated metal Products	68.9	85.1	100.2	100.2	100.2	70.7
Other man. n.e.c.	4.3	4.4	4.6	10.6	12.9	7.2
Electricity, Gas & Water	72.7	71.1	62.2	61.3	49.9	51.0
Construction	77.1	81.1	77.3	70.3	63.3	57.1
Wholesale and Retail Trade	174.7	174.4	181.5	185.3	186.8	179.3
Restaurant and Hotels	51.3	46.8	46.5	48.6	46.2	47.6
Transport, Storage and Communications	109.2	110.1	114.5	113.3	110.2	108.9
Rail Transport	32.9	33.4	33.3	31.7	30.0	28.2
Road transport	30.5	31.2	34.0	34.4	33.9	34.6
Other Transport & Services Allied to Transport	20.1	20.5	21.2	20.8	20.2	19.8
Communication	25.1	25.0	26.0	26.4	26.1	26.3
Financial Institutions	60.6	56.8	50.8	60.0	52.9	55.9
Real Estates & Business Services	179.0	178.6	189.2	191.1	192.7	198.4
Community, Social & Personal Services	365.6	358.1	370.6	373.5	375.6	385.5
Public Admn. (& Defence) Public Sanitary Services	141.3	137.3	142.2	143.2	144.2	148.7
Education	119.0	115.7	120.0	120.7	121.5	125.3
Health	44.1	42.9	44.4	44.7	45.0	46.5
Other Community & Personal Services	61.2	62.2	64.0	64.9	64.9	65.0
Import duties	19.9	22.5	23.1	16.7	17.0	19.6
Less: Imputed Banking Service Charges	16.9	15.8	14.1	16.6	14.6	15.5
	2044.5	2059.3	2114.3	2247.1	2224.2	2186.8

* Provisional; estimates are based on partially available data
Source: CSO

8. Current tendencies in the GDP growth indicate that it may be difficult to achieve the target rates of growth (close to 5 percent in 1993-94) envisaged in the Economic and Financial Policy Framework Paper (PFP) without a strong support of positive results of the applied new economic policy measures. Acceleration of economic growth within a mid-term horizon, is largely based on an assumption that the non-mining sector can develop faster than the average GDP expansion, (4.5 percent in 1992 and 5.5 percent in 1993). So far, its relatively slow pace of growth only aggravated stagnating tendencies in the economy.

9. Deeper analysis, based on long-term trends of the GDP growth reveals some traditional barriers impeding economic growth and leading to a stagnation. Between 1975-1990 GDP at constant prices is expected to grow by 8.6 percent which gives an average annual rate of growth considerably below 1 percent over a period of 15 years (Table 2.3).

10. The stagnating tendencies in Zambia's economic growth correspond to a dramatic, long-term deterioration of the country's terms of trade and are reflecting unfavourable developments in the external environment, which with some time-lag adversely affected Zambian foreign trade and largely curbed possibilities of economic expansion.

11. Despite difficult external situation, in the second half of the 1980s Zambia's economy managed to overcome overall downward trend, but still experienced a considerable slow-down at the end of the decade. Between 1986-1988 Zambia experienced a positive rate of growth. The rate of growth of GDP has been rising steadily from 0.7 percent (1986/1985) to 2.2 percent (1987/1986), 6.3 percent (1988/1987) and dropped by 1 percentage point in 1989. A further decline by is expected in 1990. During the same period the GDP per capita at constant prices has been revealing almost permanent long-term declining tendencies (Table 2.3) mainly due to an extremely high rate of population growth. In 1989 GDP per capita dropped by 5 percentage points,as compared with the previous year and a similar decrease is expected in 1990.

12. Given the present trend of population growth, it will be extremely difficult to reverse this unfavourable tendency. However, according to the IMF and World Bank projections positive rates of real, per capita GDP may be expected already in 1992-1993 (0.2-1.2 per cent).

13. The negative rates of growth encountered last year and expected in 1990 confirm an existence of serious long-term development barriers in Zambia, resulting in general stagnating tendencies in the economy and reflected in the progressing deterioration of the quality of life.

TABLE 2.3 LONG-TERM TRENDS OF GROSS DOMESTIC PRODUCT (1970 - 1990)

	1970	1975	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
1. GDP at constant (1977) prices (A) Kwacha Million.	1775	2013	1986	1998	1937	1996	2119	2059	2019	2012	2245	2059	2114	2247	2224	2187
(B) 1975 = 100	88.2	100	98.7	99.3	96.2	99.2	105.3	102.3	100.3	99.9	111.5	102.3	105.0	111.6	110.5	108.6
(C) Previous year = 100	-	97.5		100.6	96.9	103	106.2	97.2	98.1	99.7	111.6	91.2	102.7	106.3	99.0	98.3
2. GDP at current market prices (Kwacha Million).	1279	1583	1986	2251	2560	3064	3485	3595	4181	4931	7072	12963	19778.9	30020.9	60024.5	107602.0
3. GDP per capita (A) at constant(1977) prices	427	412	382	373	351	351	361	340	325	313	334	294	290	300	285	270
B) 1975 = 100	103.6	100	92.7	90.5	85.2	85.2	87.6	82.5	78.9	80	81.1	71.4	70.4	72.8	69.2	65.6
C) Previous year = 100		93.8		97.6	94.1	100	102.8	94.2	95.6	96.3	106.7	88.4	98.6	103.5	95.0	94.7

Source: CSO, National Accounts Statistics

14. In the second half of the past decade the structure of the Zambia' economy remained relatively stable. General proportions between particular sectors did not undergo major changes. Despite some setbacks or stagnating tendencies witnessed last year and a expected in 1990 (Table 2.7), the agricultural and manufacturing sectors were the most dynamic ones in the second half of the 1980s and they could be considered as the potentially strongest driving forces for the economic growth in the mid-term.

TABLE 2.4

GROSS DOMESTIC PRODUCT BY TYPE OF EXPENDITURE
AT CURRENT PURCHASERS' VALUES (Kwacha Million)
1985 - 1990

	1985	1986	1987	1988	1989	1990 *
1. Government Final Consumption Expenditure	1686.7	3481.2	4399.0	4582.4	7574.3	16647.1
2. Private Final Consumption Expenditure	4294.6	6551.7	11820.3	19824.8	50360.0	72699.3
3. Increase in Stock	328.5	1701.0	810.6	1031.8	2321.0	2318.0
4. Gross Fixed Capital Format	724.5	1385.6	1931.0	2381.2	3642.7	13117.8
5. Final Consumption and Capital Formation (1+2+3+4)	7034.3	13119.5	18960.9	27820.2	63898.0	104782.2
6. Exports of goods and Services	2740.2	5759.3	8512.4	10266.2	14791.6	34816.7
7. Less: Imports of goods and Services	2702.6	5915.6	7694.9	8065.6	18665.1	31996.9
TOTAL GDP	7071.9	12963.1	19778.4	30020.9	60024.5	107602.0

* Provisional: estimates are based on partially available data.
Source: CSO

TABLE 2.5

Gross National Product By Type of Expenditure
at constant (1977) prices (Kwacha million)
1985 - 1990

	1985	1986	1987	1988	1989	1990 *
1. Goverment Final Consumption Expenditure	460.1	464.4	377.6	331.3	438.7	402.8
2. Private Final Consumption Expenditure	1236.9	1224.6	1498.5	1660.9	1505.5	1556.9
3. Increase in Stock	62.4	216.7	75.0	66.9	105.0	150.5
4. Gross Fixed Capital Formation	198.8	168.6	158.9	178.1	123.2	153.9
5. Final Consumption and Gross Capital Formation (1+2+3+4)	1958.2	2074.3	2110.0	2237.2	2172.4	2264.1
6. Exports of Goods and Services	527.8	537.8	505.9	476.3	469.6	476.2
7. Less: Imports of Goods and Services	465.2	526.9	541.4	540.4	452.7	523.0
8. Statistical Discrepancy	23.7	-25.9	39.8	74.0	34.9	-30.5
Total G.D.P	2044.5	2059.3	2114.3	2247.1	2224.2	2186.8

* Provisional; estimates are based on partially available data
Source: CSO

TABLE 2.6 COST STRUCTURE OF THE GDP
(at current purchasers values)
1985-1989

	1985	1986	1987	1988	1989
Compensation of employees	2818.6	4207.2	5922.8	8306.6	17549.2
Operating of surplus	2582.0	5177.2	8089.0	16139.1	32489.2
Consumption of fixed capital	932.8	2233.1	3429.3	4264.4	8152.5
Indirect taxes	926.9	1915.5	3014.7	2706.7	3336.4
Less: subsidies	188.4	569.9	677.4	1396.0	1502.8
Total GDP	7071.9	12963.1	19778.4	30020.8	60024.5

Source: CSO

15. After a strong decline in 1988, mining and quarrying improved its performance last year, but the prevailing long-term tendency is rather unfavourable. Copper industry remains the mainstay of the Zambian economy, but this sector is encountering serious development barriers: diminishing ore reserves with more difficult access and rising production cost.

This situation, as well as unfavourable long-term tendencies in world copper prices, strongly justify the Government's efforts to diversify the country's economic base. However, the results of these efforts are still to be seen.

16. In addition to this, in 1989 same unfavourable tendencies could be noticed in some other important sectors of the economy like: construction (the third consecutive year of rapid decline), transport, storage and communication (the second consecutive year of a mild decline) and electricity, gas and water (the fourth consecutive year of decline exacerbated by the Kafue Gorge accident in 1989).
In 1990, further considerable declines (leading to the overall negative rate of growth of GDP of -1.7 percent) are foreseen in agriculture (-7.3 percent) and construction (-9.8); milder unfavourable developments are expected in manufaturing and trade. At the same time mining and quarrying is supposed to expand at a positive rate of approximately 3 percent (Table 2.7).

3.0 PRICE SYSTEM

17. Until June 1989 market regulation had a very limited influence on the structure of commodity prices. Instead, prices were subject to two types of regulatory activities:

- administrative price monitoring and screening,
- direct price control.

The institution designated to carry out these activities was the Prices and Incomes Commission (PIC). Until the economic reform package was launched in mid-1989 there were twenty-three commodities whose prices were set by the statute and enforced by the PIC and the Department of Price Control of the Ministry of Commerce and Industry.

18. Administrative direct control over prices was rather costly and never sufficiently effective, despite considerable efforts of the institutions involved. The pressure on PIC was constantly growing and large number of key companies filed applications requesting exemption from the price freeze. Such permissions were granted in a number of cases. In the period of administrative price control numerous cases of black market operations emerged and could not be put under control. It is generally believed that the scope of parallel market transactions expanded during this period.

19. In recent years the rise in prices has accelerated (Tables 2.8, 2.9). Various problems may be identified, which were brought about by the direct price control in the past. It was, however, finally recognized, that a better administrative control or improved legal discipline could not change the essence of the problem. The roots of unfavorable developments in the price policy have to be seen in the context of structural issues like: losses in export revenues, cummulative loan repayments, low capacity utilization, etc. and they refer to objective discrepancies between demand and supply. Under direct control, prices were not reflecting relative scarcities of products and resources and were not sending the right signals to both producers and consumers.

TABLE 2.7

Dynamics of G.D.P Components
(percentage change over previous year)
at constant (1977) prices
1986 - 1990

	1986	1987	1988	1989	1990	Average rate 1987-89
1. Agriculture, Forestry and Fishing	8.7	-2.2	19.3	-2.7	-7.3	4.8
2. Mining and Quarring	-5.0	4.4	-12.9	9.5	2.9	0.3
3. Manufacturing	0.9	8.8	18.2	-0.5	-3.5	9.4
4. Electricity, Gas and Water	-2.2	-12.5	-1.5	-18.6	2.2	-10.9
5. Construction	5.2	-4.7	-9.1	-10.0	-9.8	-4.8
6. Wholesale and Retail trade	-0.2	4.1	2.1	0.8	-4.0	2.7
7. Restaurants, Bars, Hotels	8.8	-0.6	4.5	-4.9	3.0	5.5
8. Transport, Storage Communications	0.8	4.0	-1.1	-2.6	-1.2	0.1
9. Financial Institutions	-6.3	-10.6	18.1	-11.8	5.7	3.3
10. Real Estate and Business Service	-0.2	5.9	1.0	0.8	3.0	2.2
11. Community, Social and Personal Services	-2.1	3.5	0.8	0.6	2.6	1.6
12. Import Duties	13.1	2.7	-27.7	1.8	15.3	8.7
13. Less: Imputed Banking Service Charges	-5.9	-10.8	17.7	-12.1	6.2	3.2
Total G.D.P	0.7	2.7	6.3	-1.0	-1.7	3.0

Source: CSO

TABLE 2.8

Dynamics of Prices
(average annual % change)
1980 - 1990

	1980	1984	1985	1986	1987	1988	1989	1990 JUNE
GDP Deflator		18.3	41.1	82.1	41.5	46.4	105.6	
Consumer Price Index								
a) Low Income	11.7	20.0	37.4	51.6	43.0	55.6	124.7	124.6*
b) High Income	11.5	20.7	32.8	58.3	54.5	45.1	106.2	107.5*
Wholesale Prices								
a) All Goods	9.2	28.0	47.2	115.9	84.4	11.5	84.2	
b) Consumer Goods	15.0	15.4	41.0	62.0	70.9	29.0	118.7	
c) Export Goods	5.3	37.7	73.2	138.5	50.2	29.2	67.9	

Source : NCDP/CSO : Consumer Price Statistics, National Accounts Statistics.
* As compared with June 1989.

TABLE 2.9

GDP Deflator by Sector of Activity
(percentage change over previous year)
1980 - 1990

	1980	1984	1985	1986	1987	1988	1989	1990*
1. Agriculture, Forestry and Fishing	116.9	14.4	24.6	56.9	41.2	111.7	97.2	83.4
2. Mining and Quarrying	1.6	16.4	76.0	125.2	9.4	34.7	123.5	10.9
3. Manufacturing	19.2	20.3	48.0	80.1	73.6	44.9	131.0	118.2
4. Electricity, Gas, Water	-1.9	0.8	-0.6	139.3	64.0	30.3	59.6	21.3
5. Construction	16.8	15.2	37.3	51.6	41.4	72.7	58.8	368.9
6. Wholesale/Retail trade	-8.4	32.7	40.8	115.1	63.0	21.3	47.3	57.5
7. Hotel, Bars, Restaurants	21.6	16.3	37.3	58.4	64.4	64.6	95.0	53.2
8. Transport/Communication	14.6	13.5	44.9	72.2	35.8	45.3	145.5	51.2
9. Finance/Insurance	17.7	16.9	36.6	107.5	84.6	24.8	86.4	33.6
10. Real Estate and Business Services	7.5	30.7	32.4	65.7	45.1	27.0	38.5	68.1
11. Community, Social and Personal Services	10.6	13.1	13.3	27.8	22.9	44.9	23.9	101.7
12. Import Duties	26.0	55.6	115.2	138.3	63.0	43.1	95.8	53.7

Source: CSO
* Estimates

20. In recognition of the necessity of the need to change above price control system the decision was made in June 1989 to deregulate all prices, except for maize meal (a strategic consumption item especially for the low-income group). A rapid price increase which followed was the result of a natural adjustment process as the previously surpressed inflation emerged and prices went up towards their market clearing levels.

It is a pure economic necessity that this portion of inflation has to be absorbed, but from the point of view of the society this is usually a very difficult and painful process. To this end, during 1989 the Government prepared a social programme containing a wide range of projects aimed at cushioning the impact of adjustment policies on the most vulnerable social groups.

21. Proper implementation of the new price policy becomes one of the major challenges in the period after launching of radical economic reforms, as the society tends very often to interprete the economic situation from the sole perspective of price movements. However, long-term effects should lead to general stabilization of the economy.

22. In order to reduce the budgetary cost of maize subsidies and discourage smuggling, maize prices were increased almost threefold in January 1989. This allowed to cut maize subsidies by one half. At the same time, in order to protect the low-income groups, a coupon scheme was introduced.

23. Despite Government's efforts to protect the most vulnerable groups, the Zambian population still remains very sensitive to changes in maize meal prices. Increase of these prices by approximately 100% in June 1990 is widely considered as the immediate cause sparking social tensions and riots.
24. Recent efforts of the Government are oriented towards decreasing the price of mealie meal through liberalization of maize sales and decontrol of marketing arrangements. Under the new regulations introduced in September 1990 farmers are allowed to sell maize directly to millers. At the same time the retail prices of maize meal were reduced by 20 percent.

25. The recent structure of price increase has been unfavourable from the point of view of the low-income group. Consumer Price Index for the low-income group registered an increase of 56.6 percent in 1988 and was over 10 percentage points higher than that for the high income group.
This unfavourable disproportion still increased in 1989 resulting in the index for the low-income group higher by roughly 18 percentage points (Table 2.8).

26. Given the momentum of the price increases already gained, it might be difficult to adhere to the targeted, maximum inflation rates assumed in the Policy Framework paper (1990 - not more than 55 percent, 1991 - 40 percent, 1992 - 25 percent and 1993-15 percent). In the first half of 1990, consumer Price Index for the low income group grew to 124.7 percent, but the rate of growth of consumer prices was indicating some deceleration.

4.0 EMPLOYMENT AND INCOME POLICIES

27. Despite improvements in quality of available labour force, employment has been declining for a number of years (Table 2.10). Parallel to that, incomes in real terms have been decreasing. During the past decade employment in mining and quarrying has fallen by some 13 percent, partly as a result of cost-reduction measures pursued by ZCCM. This tendency is likely be continue, given the gradual decrease in copper reserves.

TABLE 2.10

POPULATION AND LABOUR FORCE

	1980	1985	1986	1987	1988	1989	1990 *
1. Total Population (million)	5.68	6.72	6.95	7.15	7.35	7.57	7.79
2. Rate of Crowth (previous year = 100)		103.30	103.4	102.8	102.9	102.9	102.9
3. Urban Population (million)	2.26	3.00	3.20	3.4	3.6	3.8	4
4. Labour Force (million)	1.65	1.99	2.70	3.74	3.78	3.82	3.86
5. Formal Sector Employment	0.382	0.361	0.361	0.361	0.362	0.370	0.377
6. Urban Population as percentage of total population (%)	40.0	44.6	46.0	48.0	49	50.2	51.3
7. Formal Sector Employment as percentage of Labour Force	23.2	18.1	13.10	9.40	9.6	9.7	9.8

* Provisional

Source: estimates based on information provided by CSO

28. The unfavorable tendency in real incomes over the past decade could not be counterbalanced by an increasing practice of granting employees extra bonuses in form of various fringe benefits.

Real average annual cash earnings in the formal sector have fallen sharply below their 1980 level, accompanied by a downward tendency in output per worker.

29. There is an urgent need to increase employment by reducing excessive reliance on capital-intensive techniques pursued in the past. Adjustment processes, including promotion of agriculture and non-traditional exports, should increase the importance of labour-intensive methods of production generating considerable amount of new job opportunities.

5.0 FOREIGN TRADE AND THE BALANCE OF PAYMENTS BASED ON COPPER EXPORTS

30. In the past, foreign trade was one of the major driving forces in economic development in Zambia. However, after the global economic shocks of the 1970s and and the 1980s resulted in dramatic decline of world copper prices and coupled with emerging production barriers in the Zambian copper industry, lack of diversification in foreign trade became one of the major development barriers.

Structural disproportions between export revenues and import demand, lack of imported inputs, inability to further develop non-traditional exports, led to a widening of Zambia's balance of payments disequilibria and to a very high national debt, as related to population, GDP or export earnings.

31. Supported by favourable tendencies in world copper prices, improved control over import expenditures, and stronger motivation through devalued local currency, Zambia's economy maintained and even considerably improved (by approximately 30 percent in dollar terms) the positive Trade Balance in merchandise last year.

On the other hand, the Current Account Balance deteriorated, as the export surplus in goods of $561.8 million was negatively adjusted by strongly unfavourable balances of Investment Income, as well as transportation, insurance, travel and other services. Negative balance on the Current Account worsened to $189.2 million (Table 2.11) in 1989.

32. In addition to deteriorating Current Account Balance, external disequilibrium was widened by recently prevailing negative trends in capital movements. As a result of these cummulative processes a large external debt was generated which, in per capita terms approached the level of US $950, which is among to the highest in the world.

33. Balance of payments estimates for 1990 were prepared in sets of alternative scenarios depending mainly on different assumptions concerning cost of imported crude oil ($22 and $27 per barrel, respectively). In the second scenario, as a result of more expensive crude oil imports, the positive Trade Balance drops to $209.5 million and negative Current Balance increases to minus $136.8 million (Table 2.12).

In view of the rapidly deteriorating situation on world crude oil markets in August - September 1990, with oil prices going above $35 a barrel, still more pessimistic developments in Trade and Current Account may be expected. At the same time, the United Nations embargo imposed on Iraqi and Kuwaiti trade, created a necessity to find alternative sources of oil supplies. Crude oil purchases (amounting to over $ 106 million, on CIF basis, in 1989) clearly dominated Zambia's imports in 1989 and 1990 (Tables 2.13, 2.14, 2.15).

34. Among the factors causing long-term unfavourable trends, of the overall balance of payments, one can identify the following can be identified:

TABLE 2.11

1989 BALANCE OF PAYMENTS ESTIMATES

	CREDIT		DEBIT	
A. Goods and Services	(K'Million)	($'Million)	(K'Million)	($'Million
1. Merchandise	18434.0	1335.8	10680.8	773.9
Trade Balance	7753.2	561.8		
2. Freight & Insurance on Merchandise	553.0	40.1	2778.4	201.3
3. Other Transportation	344.0	24.9	1376.9	99.8
4. Travel	172.0	12.4	1359.5	98.5
5. Investment Income	17.2	1.2	6503.0	471.2
Government			5300.8	384.1
Public corp.			550.4	32.0
Other			651.8	47.2
6. Other Goods, Services & Income	103.2	7.4	618.0	44.7
Government	103.2	7.4	494.5	35.8
Private			123.5	8.9
B. Unrequited Transfers	1567.9	113.6	485.2	35.2
7. Government	1562.9	113.2	65.9	4.5
8. Private	5.0	0.4	422.3	30.6
9. Current Account	-2610.5	-189.2		
C. Capital Account Net Plus Errors & Ommission	873.1	63.3		
10. SDR Allocations				
Overall Balance			-3484.7	-252.5
D. Monetary	7029.8	509.4	-3545.1	-256.9
11. Monetary Authority	2239.6	162.3	-1173.6	-85.0
(a) Assets			-1173.6	-85.0
(b) Liabilities	2239.6	162.3		
12. Commercial Banks	685.1	49.7	-2371.5	-171.8
(a) Assets			-2371.5	-171.8
(b) Liabilities	686.1	49.7		
13. Payments Arrears	4060.6	294.2		
(a) Commercial	439.5	31.8		
(b) Debt Service	3621.1	262.4		
14. Currency Re-aligrment	43.5	3.1		

Exchange Rate: K13.8 per US Dollar

Source: Bank of Zambia

TABLE 2.12

1990 BALANCE OF PAYMENTS ESTIMATES

	1ST SCENARIO		2ND SCENARIO	
	(K'Million)	($'Million)	(K'Million)	($'Million
1. Exports (F.O.B)	33802.6	1090.4	33802.6	1090.4
of Which Copper	29118.5	939.3	29118.5	939.3
2. Imports (F.O.B)	27001.0	871.0	27307.9	880.9
3. Trade Balance	6801.6	219.4	6494.7	209.5
4. Non-Factor Services (net)	-9077.6	-292.8	-9089.1	-293.2
5. Investment Income (net)	-12806.1	-413.1	-12806.1	-413.1
6. Unrequited Transfers (net)	11160.0	360.0	11160.0	360.0
7. Current Account	-3922.1	-126.5	-4240.5	-136.8

Assumptions : average Kwacha/$ rate assumed to be 31.00
Scenario 1: price of Crude Oil assumed to be $22 per barrel
Scenario 2: price of Crude Oil assumed to be $27 per barrel

Source: Bank of Zambia

Table 2.13

1989 IMPORTS (C.I.F.)

MONTH	CRUDE OIL K'000	FERTILIZER K'000	MAIZE K'000	WHEAT K'000	ELECTRICITY K'000	OTHER K'000	TOTAL K'000
JANUARY	139,376	-	7,248	-	-	513,422	660,046
FEBRUARY	113,894	83	-	3,846		545,765	663,588
MARCH	-	3,080	28,553	-		553,337	584,970
APRIL	147,352	-	-	-	2,207	512,327	661,886
MAY	-	-	-	-	25,818	602,007	627,825
JUNE	140,327	560	-	-	22,718	1,353,349	1,516,954
JULY	219,671	-	-	-	19,823	638,790	878,284
AUGUST	240,357	518	-	6,299	25,905	959,619	1,232,698
SEPTEMBER	293,700	9,107	-	-	21,934	887,123	1,211,864
OCTOBER	-	1,380	7,071	339	24,525	1,239,637	1,272,952
NOVEMBER	284,203	41,334	20,245	20,566	22,853	1,565,211	1,954,412
DECEMBER	321,975	7,168	44	13,840	8,619	983,412	1,335,058
TOTAL	1,900,855	63,230	63,161	44,890	174,402	10,353,999	12,600,537

Table 2.14

CRUDE OIL IMPORTS 1989

MONTH	TONNNE	US $ C.I.F	C.I.F (K'000)	US $ F.O.B.	F.O.B. (K'000)
JANUARY	95,164	13,273,891	139,376	12,955,023	136,027
FEBRUARY	77,540	10,847,041	113,894	10,586,975	111,163
MARCH	-	-	-	-	-
APRIL	89,313	13,347,083	147,352	13,024,532	143,790
MAY	-	-	-	-	-
JUNE	88,317	12,757,564	140,327	12,438,638	136,700
JULY	98,953	13,511,951	219,671	13,155,893	213,783
AUGUST	-	-	-	-	-
SEPTEMBER	89,814	12,992,278	240,357	12,641,487	233,867
OCTOBER	-	-	-	-	-
NOVEMBER	90,647	14,210,137	293,700	13,826,463	285,654
DECEMBER	90,893	15,332,176	321,975	14,918,207	313,282
TOTAL	720,641	106,272,121	1,616,652	103,547,218	1,574,266

Source: Bank of Zambia, CSO.

Table 2.15

1990 IMPORTS (C.I.F.)

MONTH	CRUDE OIL K'000	FERTILIZER K'000	MAIZE K'000	WHEAT K'000	OTHER K'000	TOTAL K'000
JANUARY	278,822	10,011	-	-	1,780,573	2,069,406
FEBRUARY	-	5,452	-	20,642	1,722,969	1,749,063
MARCH	278,526	171,081	-	-	2,224,503	2,674,110
APRIL	328,140	23,472	-	-	2,847,827	3,199,439
MAY	-					
JUNE	316,603					

Source: Bank of Zambia, CSO.

- burden of yearly operational expenditures payable in foreign exchange. This constraint will be valid in the foreseeable future, as well. It is estimated, in the PFP that only to sustain copper production ZCCM will require SDR 250 - 280 million of imports a year until 1993;
- high burden of freight and insurance;
- still low level of receipts from tourism vis a vis foreign travel expenditures;
- largely negative balance of Investment Income;
- low level of foreign direct investment in Zambia consisting mainly of reinvested earnings, with very limited amounts of new equity;
- high burden of the principal component in loan repayment.

35. Among export items, copper is still by far the most important one, with the recent share in export earnings of above 85 percent. Cobalt is ranking second, with the share of approximately 6 percent (Tables 2.16, 2.17, 2.18).

TABLE 2.16

1988 - 1990 EXPORTS (F.O.B)

	1988		1989		1990 *	
	K,(MIL)	$,(MIL)	K,(MIL)	$,(MIL)	K,(MIL)	$,(MIL)
COPPER	8339.6	834.0	16353.1	1185	29118.5	939.3
ZINK	161.9	16.2	301.9	21.9	291.6	9.4
LEAD	19.0	1.9	8.5	0.6	1.9	0.1
COBALT	598.2	59.8	1101.2	79.8	2118.7	68.3
BY-PRODUCTS	44.0	4.4	40.5	2.9	83.8	2.7
ELECTRICITY	96.7	9.7	70.8	5.1	329.9	10.6
OTHER PRODUCTS	460.5	46.1	460.4	33.4	1806	58.3
RE-EXPORTS	66.3	6.6	97.6	7.1	52.2	1.7
TOTAL	9786.2	978.7	18434	1335.8	33802.6	1090.4

Exchange Rate: Kwacha/US Dollar = 10.00, 13.8, 31.00
* Provisional estimates
Source: CSO, BANK OF ZAMBIA

TABLE 2.17

JANUARY-APRIL 1990 EXPORTS (F.O.B)

MONTH	DOMESTIC TOBACCO K'000	EXPORTS ELECTRICITY K'000	MINERALS K'000	OTHER K'000	RE-EXPORT K'000	TOTAL K'000
JANUARY	-	12,553	1,398,904	58,073	1,111	1,470,641
FEBRUARY	-	16,333	2,081,241	83,635	3,239	2,184,448
MARCH	-	23,709	3,903,211	188,356	5,366	4,120,642
APRIL	-	17,114	3,073,439	271,923	7,659	3,370,135

Source: Bank of Zambia

TABLE 2.18

1990 METAL SALES (F.O.B)

	COPPER		ZINC		LEAD		COBALT		BY PRODUCT	TOTAL
	TONNE	K'000	TONNE	K'000	TONNE	K'000	TONNE	K'000	K'000	K'000
JANUARY	31,369	1,196,017	105	6,911	30	420	443	184,574	10,982	1,398,904
FEBRUARY	41,773	1,930,276	968	29,015	-	-	281	116,692	5,258	2,081,241
MARCH	50,344	3,684,797	1,270	49,965	10	398	373	159,201	8,850	3,903,211
APRIL	39,463	2,838,776	609	27,133	-	-	475	205,037	2,493	3,073,439
MAY	29,944	2,482,867	240	8,490	-	-	469	217,310	7,350	2,716,017

Source: Bank of Zambia

It might be expected that export revenues will be subject to gradual, structural change over time. Volume of copper exports may gradually decline as access to ore deposit is becoming more and more difficult and is evidenced by decreasing ZCCM finished copper production in the 1980s (Table 2.19).

TABLE 2.19

ZCCM FINISHED COPPER PRODUCTION (1982 - 1990)

YEAR	PRODUCTION (TONNES)	YEAR	MONTH	PRODUCTION
1982	583,967	1990	JANUARY	37,368
1983	574,772		FEBRUARY	32,306
1984	521,691		MARCH	38,799
1985	479,446		APRIL	34,532
1986	459,172		MAY	33,189
1987	483,039		JUNE	27,038
1988	422,221		JULY	30,194
1989	450,707		AUGUST	40,335
			SEPTEMBER	40,928 *

* Provisional
Source : ZCCM

Despite recent mixed developments in copper prices, most of the international, mid-term predictions are pessimistic, so the problem may be exacerbated in early 1990s by decreasing unit values.

36. The only compensating development for the declining traditional copper exports may come from export diversification. This problem creates one of the major challenges for the country in medium and long-term.
Despite expected progress in 1990, non-traditional exports both in absolute and relative terms still play only marginal role in the foreign trade.

37. Systemic changes in foreign trade aimed at export promotion and its diversification include new active exchange rate policy launched at the end of 1988 and continued until the present time. After devaluations of November 1988 and June 1989, a dual exchange rate system was introduced in February 1990.

This system was aimed at promoting the growth of non-traditional exports, attracting foreign private investments and reducing the scope of parallel market operations. The dual exchange rate system has two types of exchange rates: the official rate and the market rate. Within the Official Exchange Rate the Kwacha remained pegged to the SDR. At the same time, the Market Exchange Rate was fixed on the basis of the US dollar/Kwacha par rate of US $1 = K40. In October 1990 the market rate was also made to crawl, as was the case of the official exchange rate.

38. The market exchange rate is applied to the following foreign exchange operations:

- -Non-traditional (non-metal) export receipts and foreign exchange earnings from hotel and other services which are eligible for the retention facility under the Export Retention Scheme;
- -foreign private investment;
- -donor balance of payments support (with some exceptions);
- -foreign exchange sold by tourists and any one else wishing to sell it on a "no questions asked" basis.

As foreseen in the PFP the process of exchange rate adjustment will be continued until this parameter reaches the market clearing level (not later than mid-1992).

39. After the dual exchange rate system was introduced in February 1990, total Kwacha earnings from non-traditional (non-mineral) exports were increased considerably (Table 2.16), due to depreciation of the local currency.
The share of non-traditional exports in the total value of exports was only 5.3 percent at the end of the first quarter of 1990. In dollar terms, non-traditional exports fell from $62.4 million in 1988, to 45.6 million (only 3.4 percent of total exports) in 1989. It is estimated that the non-mineral exports will ammount to $70.6 million by the end of 1990 contributing to 6.5 percent of the total export earnings.

40. In order to supply economic entities with additional export incentives a liberalized foreign currency retention quota system was introduced. This system allows to move a greater share of export hard currency earnings directly to producers and exporters creating conditions for their less constrained business initiative.

41. In addition to this, export licencing system has been streamlined with the objective to abolish bureaucratic barriers hindering export development. An Export Promotion Board and Export Revolving Fund were established. The objective, according to the PFP, is to achieve an annual rate of growth of non-traditional export volumes of 10 percent.

42. In the beginning of 1989 regulations governing "no-funds" imports scheme were further liberalized. This facility allows imports scheme to be purchased with foreign exchange from sources other than Bank of Zambia and items to be purchased are subject only to few restrictions.

43. To improve efficiency of the national economy new tariff policy in foreign trade is being introduced. The main objective will be to keep protective tariffs to a minimum and reduce the dispersion of protection.In the future, minimum tariff rates for each import category will be levied on all items presently zerorated, or subject to discretionary exemptions and rebates.

44. In 1989, SDR 644 million of debt service payments (principal and interest) were scheduled to fall due. Even with this years' exceptionally high copper prices this represented 80 percent of export earnings (after deducting fixed import requirements of ZCCM).

45. In view of the weakening copper prices in the mid-1990s, as projected by experts, it is widely agreed that Zambia will not be in a position to service its debt fully on a current basis at any time in the foreseeable future. Thus, special arrangements will have to be made and the dialogue with both bilateral and multilateral creditors will need to be intensified.

46. The bulk of Zambia's outstanding stock of debt is owed to bilateral creditors (approximately 42 percent) and to multilateral creditors (approximately 36 percent). The rest of the debt stock is owed to other financial institutions (10 percent) and to various non-guaranteed private creditors.

47. According to the PFP, approximately SDR 281 million are needed in 1990 to meet Zambia's debt service payments to multilateral institutions. At the same time, due to unprecedented oil price increases, the negative current account deficit may reach, or even exceed SDR 136.8 million level assumed in the second scenario of the Balance of Payments for 1990.

48. Arrears to the International Monetary Fund and the World Bank at the end of 1989 amounted to SDR 919 million.
An agreement to clear the arrears to the multilateral institutions and permitting resumption of financial support from these institutions is expected to be reached at the end of 1990. Zambia's bilateral debt was rescheduled in 1990 under a Paris Club agreement covering the period from January 1987 to December 1991.

6.0. MONETARY POLICY

49. The new monetary policy introduced in the reform package of June 1989 has been targeted at reducing the inflation rate and stabilizing the economy.

50. Both the rate of inflation and the rate of growth of money supply were sharply accelerated in the period preceeding the introduction of the economic reform package last year. The rate of growth of "broad money" for the whole 1988 was 61.6 percent, however, it grew by 83 percent in the final quarter of the same year, at a seasonaly adjusted annual rate. The momentum money supply already gained indicated major difficulties in bringing last year's inflation rate down below 80 - 90 percent level, as initially targeted.

51. In 1989 a major effort was done to impose monetary restraint and thus decisively help reduce inflation in the medium term. The immediate target set for 1989 was to reduce the rate of growth of "broad money" to 50 percent, assuming continuation of this policy, it would allow for cutting inflation rate by half in the beginning of the 1990s, as envisaged in the PFP. The actual rate of growth of broad money in 1989 was higher by approximately 15 percentage points from the target level. This allowed for higher than expected increase of prices. Consumer price index averaged 124.7 percent, but went up to 154.3 percent at the end of the year.

52. The integrated action plan introduced by the Bank of Zambia in July 1989 was the major tool in implementation of the concept of enforcing monetary restraint. It included the following decisions:
- an increase in minimum reserve requirements;
- payment into the Bank of Zambia of the Kwacha counterpart to overdue parastatal external debt obligations;
- an introduction of a non-rediscountable government bond aimed at absorbing excess liquidity in the banking system and reducing credit expansion;
- increase of interest rates by approximately 10 percentage points.

Moreover, in order to decrease money supply the Bank of Zambia decided to limit its approval of debt - equity swaps only to those cases, where an investment in productive activities was undertaken.

53. New levels of interest rates introduced in July 1989, as an element of adopted monetary policy, were the following:
- the basic interest rate of the Bank of Zambia was raised from 19 percent to 29 percent;
- the maximum lending rate for commercial banks went up from 25 percent to 35 percent;
- the upper limit on the rate of interest on loans to peasants and small-scale farmers for agricultural purposes charged by commercial banks was set not to exceed 33 percent;
- the interest rates of treasury bills were increased from

18.5 to 28.5 percent;
- saving rates of banks went up from 13 to 23 percent.

The term structure of nominal average interest rates in the first half of 1990 is indicated in Table 2.20. In October 1990 the Bank of Zambia basic lending rate for commercial banks was further increased by 5 percentage points.

TABLE 2.20
TERM STRUCTURE OF NOMINAL AVERAGE INTEREST RATES
(FIRST HALF OF 1990)

Savings	23.0 %
Fixed 30 days	25.0 %
Fixed 60 days	25.7 %
Fixed 120 days	28.1 %
Amounts over Kwacha 1 million	
60 days	28.7 %
120 days	29.6 %
Treasury bill rate	25.0 %
Long-term bond rate	31.0 %

Source: Bank of Zambia

54. Despite 1989 considerable increases of nominal interest rates, due to a high inflation rate, their real values were still on the negative side in 1990.

This situation requires concerted actions in order to bring inflation fully under control and further adjust interest rates until they reach positive values. The latter may be very difficult given the present momentum of the inflation rate. Current interest rates are already considered in some parts of the business community as a disincentive to invest and develop economic activity.

55. Due to growing inflationary pressures, overall propensity to save in Zambia has declined in recent years. The negative tendencies in savings and as a result in investments, were strongly supported by highly negative real interest rates, large budget deficits and fall in foreign assistance. In 1989 Gross Fixed Capital Formation (Table 2.4) accounted only for 5.5 percent of GDP and, according to estimates, it was too low to ensure even simple replacement of capital stock. However, the Fixed Capital/GDP ratio is foreseen to increase by 2.5 percentage points, as compared to the last year's level.

56. As a result of implementation of the new monetary policy

the rate of growth of broad money supply is expected to drop drastically to 25.4 percent in 1990. After eight months of 1990 the actual rate of growth of broad money was 17.3 percent.

7.0 FISCAL POLICY

57. The major objective of the fiscal policy was to reduce the inflation rate and create a more stable internal economic environment through balanced budget.

58. Among the factors influencing rapid escalation of the budget deficit since 1986 were the following:
- continued subsidies in food and agriculture:
- growing burden of debt service cost on foreign loans;
- rise in domestic interest charges on Government debt following liberalization of domestic interest rates;

- decreasing discipline in budget expenditures and various other deficiencies in the public expenditure management system.

The growing budget deficit was financed mainly by increased money supply, which had an adverse effect on maintaining internal balances.

59. Fiscal performance improved in 1989 as compared with the previous year. The overall deficit on a commitment basis was recorded at 9.5 percent of GDP. The deficit on a cash basis dropped to 7.1 percent. Government Revenue and grants decreased from 18.3 percent of GDP in 1988 to 17.7 percent of GDP in 1989.

Expenditure and net leading (excluding foreign interest) decreased from 26.7 percent in 1988 to 24.1 percent of GDP in 1989. A further decrease of expenditures to 22.8 percent of GDP is foreseen for 1990, with revenue and grants growing to 24.5 percent.

60. Improved fiscal performance in 1989 may be largely attributed to the measures taken in conjunction with the economic reforms package launched during the year, aimed at achieving of the following objectives:
- -creating a socially and economically justifiable, modern tax system;
- -orienting the tax system towards stimulation of structural changes and export expansion;
- -broadening and clearly defining the tax base;
- -increasing efficiency of tax collection.

62. Among measures taken in 1989 and 1990 to fulfill long term objectives specified in PFP were the following:
- -a review of the structure of tax exemptions and tax

relief;
-widening the sales tax base;
-imposition of ad valorem duties on import items previously zerorated;
-levying of partial cost recovery charges and fees in the education and health sectors.

63. Since the introduction of economic reforms in 1989 a considerable effort has been made to strengthen the budget expenditure control and, in general, to create an efficient public expenditure management system. The Public Investment Programme (PIP) adopted at the end of 1989 is an important element of this system. The PIP drawn out of the Fourth National Development Programme, is the expression of the most recent Government priorities. It has been generally agreed that there should be no public investment projects outside the framework of the PIP.

64. However, some isolated cases of Government and parastatal's projects, continued from the past, could be identified outside the framework of the PIP in 1990. In the future no new public projects can be undertaken (both by the Government and the parastatals) outside of the framework of the PIP. National Commission for Development Plannning (NCDP) in conjunction with the Budget Office will screen and carefully monitor implementation of particular projects and check on allocation of funding.

65. There is a great need to maintain the momentum of reforms in the area of fiscal policy.
The following issues can be identified as urgent tasks to further improve the fiscal policy:

- all major fringe benefits should be brought under the tax bracket and personal allowances and should be eliminated.
- the tendency should be abolished to submit end-of-year request for supplementary appropriations which distort the fiscal discipline and impede adequate expenditure planning, should be abolished;
- the amount of budget subsidies should be further decreased and at the same time a review of the structure and levels of recurrent departmental charges (RDCs) is necessary to improve efficiency of important sectors of the economy;
- company income tax relief structure should be adjusted to efficiently promote non-traditional exports.
  In medium-term, a value added tax is recommended for Zambia, in line with universally accepted tendency to avoid cummulative effects of the sales base.

W. HUBNER

Guidelines for Preparation of the new, updated Public Investment Program 1990 - 1993

A) <u>Present Status</u>

Documents existing and currently in use:

1. Fourth National Development Plan (FNDP) launched: January 1989

2. Estimates of Revenue and Expenditures for the year 1990, prepared on the basis of FNDP, published January 1990.

3. Economic and Financial Policy by GRZ in collaboration with the staffs of the International Monetary Fund and the World Bank. Published August/September 1989.

4. Public Investment Programme, prepared by GRZ in collaboration with the Fund and the World Bank.

B) <u>Some problems identified in connection with documents (A):</u>

1. Analysis of the documents in question allows to formulate a general observation that they are, so far, not fully consistent with each other

   One can rather identify two groups of corresponding documents:

   - first: FNDP and the Budget
   - second: Policy Framework and PIP

   First and second group do not always correspond with each other.

2/.....

2. PIP drawn out of the Fourth National Development Plan is supposed to be an expression of the most recent priorities and is constrained by the verified, actual funding available. It has been generally agreed that there should be no investment projects accepted outside the framework of the PIP.

   However, some important on-going projects can be identified which are still being implemented outside the agreed framework of PIP (eg. Sports Stadium, Party Headquarters etc). They are isolated cases, but they do exist.

3. Awareness about the PIP concept and logic behind it is still rather limited in some sectoral ministries. There are reported cases that the ministries are working on project preparation not bothering to comply with the PIP constraints.

4. Not only some marginal, isolated government on-going projects are not included in the PIP; in addition to this some parastatals' investment activity has not yet been captured in this document. The newly prepared PIP should include both: all government and all parastatal investment projects to be implemented.

C) <u>General Orientation</u>: of future investment strategy (according to the Fourth National Development Plan and the Policy Framework Paper):

- investment strategy has to be strictly consistent with resource availability and priorities identified by the Government and indicated by PIP;

- highest priority has been given to rehabilitation and maintenance of already existing facilities. Particular emphasis is on completion of on-going projects, to avoid losses in already frozen expenditures;

- In 1991 no new projects can be undertaken (both by the Government and the parastatals) outside of the framework of the PIP;

- NCDP in conjunction with the Budget Office of the Ministry of Finance will screen and carefully monitor (on quarterly basis) implementation of particular projects and check on allocation of funding. For this purpose special computer based system will be used. In order to increase expenditure discipline and improve implementation efficiency of the investment program as outlined in the PIP both NCDP and Ministry of Finance will use all their authority to block implementation of "wild" projects, from outside of the framework of the PIP, even in case they do not require outside financing.

Specific Profiles of Investments:

a) Agriculture: highest priority has been given to projects promoting smallholder agriculture (including improved research marketing and extension services);

b) Transportation: highest priority to repairing and restoring of road and railway network.

c) <u>Energy</u>: priority on rehabilitation and maintenance of already existing facilities.

d) <u>Health and Education</u>: in order to stop the deterioration of the social infrastructure, better funding will be offered via increased recurrent departmental charges.

Attention will be paid to protect the most vulnerable social groups during the adjustment process.

D) <u>Tasks to be completed</u> in the process of preparation of the new PIP.

1. Identify existing projects being implemented outside of the old PIP. (Only those considered as major ones, decisive from the point of view of the national economy) The new PIP should cover all actually implemented projects, as Zambia is looking for untied funding to finance the whole package of projects of the highest priority. Otherwise, if PIP covers only selected projects and the financial and investment discipline cannot be maintained, the donors will tend to offer funding for specific projects only, leaving Zambia with a serious financial gap.

2. The existing inconsistencies between Budget Expenditure document and the old PIP, which could have been justified to some extent in 1990 (there was no timely coordination, and some old procedures were still applied)

5/....

- cannot be maintained in 1991.

3. As:

   a) no major priority shift can be identified by the Government of Zambia;

   b) the old PIP is generally considered (apart from some critical remarks specified above) as a good document in substantive terms and is using an adequate format;

   The new PIP may not be prepared from scratch as a completely new document, but rather should be created as an adjustment to already existing programme.

4. Adjustments in the new PIP should include the following problems:

   - the list of major on-going projects should be completed;
   - all leading investment projects by parastatals should be captured;
   - if within particular sectors, or in the economy as the whole there has been a shift of priorities; or the circumstances and conditions of project implementation have considerably changed - the new PIP should be adjusted accordingly to reflect the actual situation.
   - the new PIP should take into consideration most recent changes in the rate of exchange, adjusting the Kwacha equivalent of imported

inputs accordingly. The new PIP should be based on the most recent estimates concerning the inflation rate.

- the new PIP should take into consideration recent dramatic increase of fuel prices and thus all transportation cost.

5. In general - in order to minimize organizational efforts and concentrate on substantive decision making process - the old format of PIP should be used, with only minor improvements.

6. In order to maintain compatibility with other national and external documents, the new PIP should cover the same period (1990-93) as before, however, should include all substantive adjustments mentioned earlier.

7. Summary tables for particular sectors should indicate separately:

   a) the investment programme by the government and

   b) investment programme of the parastatals.

8. A note on Project Registration and Monitoring System (prepared by the team of Dr. P. Nkanza) should be included in the Policy Framework Paper and this system should be actually used for project identification and quarterly monitoring as a very important tool in increasing efficiency of the Government's investment procedures.

9. The same system should be used for identification and monitoring of the parastatals' projects. However, all relevant forms should not be presented

to the parastatals as "open ended", triggering a process of submitting "wishful lists" of project proposals.

The over-riding objective should be maintained: identification, monitoring and disciplining of investment activities in accordance with national priorities and targets assumed by PIP.

10. Without prior clear consent, no deviation from accepted priorities and limits should be accepted. NCDP and Ministry of Finance should use all the authority to control the implementation of the investment programme. This should be done by screening all project proposals, precise monitoring and strengthening of expenditure control.

All projects outside of the PIP framework should be effectively blocked, even those based solely on parastatal internal financing.

W. HUBNER

Ad hoc expertise and comments to the appraisal of the Kasama Maize Mill project.

I GENERAL REMARKS

1.1. All comments that follow have been prepared on the basis of information provided by INDECO (Appraisal Report at 19/1/90, COMFAR print-outs of 11/7/90 with updated final product prices, minutes of the Board meetings and additional written remarks to the project). There was no possibility to verify input data used in the appraisal report, like required investment cost, or particular components of operational cost, including admin. overheads. Neither was it possible to verify estimates covered by the Market Analysis (demand gaps, structure of consumption, etc). It has been assured that all data presented in the documents are adequate and reflect realistic estimates of both cost and revenues of the project.

1.2. In order to formulate a balanced opinion about the project in question, one has to distinguish at least three separate issues emerging during the on-going debate on project implementation:

A) Logic behind project implementation from the point of view of the Zambian economy.

B) Appraisal done so far with application of the UNIDO soft ware COMFAR.

C) Apparent unwillingness on behalf of the representatives of shareholders "B" to participate and support the idea of project implementation.

Below some comments have been presented which refer to these three groups of problems.

II SPECIFIC COMMENTS:

2.1 Project idea from the point of view of the Zambian economy.

There is no doubt that the need of project implementation is strongly justified from the point of view of the national economy as a whole Economic impact on socioeconomic cost -

benefit analysis would clearly support project idea exposing socio-economic merits which are less relevant while assessing the project in purely financial or commercial terms. Amended version (with up-dated prices) of the project appraisal (from 11/7/90) proves that the project idea may be supported not only by the socio-economic, national considerations but may be viable in commercial terms, too. This statement has to be taken, however, with some reservations - probably :. deceisive - as couple of details in project appraisal documents require clarification and some issues should be rectified. Under next paragraph 2.2 one may find some suggestions in this respect.

2.2. "COMFAR" System and "COMFAR" Application

A. Despite some rigidities in initial system's design (first version was created almost a decade ago), UNIDO's experience with application of COMFAR has been generally positive. Today's version (2.1) allows for much more flexible and multidimensional approach to project's appraisal. Very powerful tools (eg. sensitivity of IRR examination, comparative type of analysis etc) have been included in the currently used software package. COMFAR as a specialized system for investment project appraisal is permanently being developed and improved and the most recent versions are automatically being supplied to COMFAR users all over the world. COMFAR meets most of international standards required while preparing project appraisal, however, it has to be used by highly qualified specialist. By the same token the results obtained in COMFAR schedule should be interpreted with understanding of all characteristic features of this software.

B. Application of COMFAR for Appraisal of the Project in Question

First impression is positive, the system has been used by thoroughly trained personnel and there are clear marks of understanding of software specifics.

Precise evaluation of the work done is not possible without discussing particular issues with the specialists involved or looking into the Data [illegible] It seems, however, that several issues need to be clarified, explained or even corrected to supply the fin[illegible] decision-making body with more precise picture of the project. The following are, in opinion the most important issues:

- more attention should be paid to the assumptions concerning the build-up of working capital. There is no provision for n initial build-up and later a decrease in W.C. takes place mainly due to questionable assumptions on current liabilities vs. Current assets. There is no provision for spare parts build-up over two first years of production.

- There are no investments during production period whatsoever. Maintaining target capacity over the period of 15 years without replacement of some elements of especially rotating machinery might occur very difficult in the reality;

- Attention should be paid to the fact, that though the liquidity position of the project is never endangered (as may be seen from COMFAR Cash-Flow tables), the actual, disagregated structure of the cash balance is unfavourable. The project generates highly positive stream of local currency, but at the same time each year of operation is closed with a negative balance in foreign exchange.

- There are no assumptions concerning future inflation which might affect the .project. I understand that a standard assumption has been made about "neutral impact of price changes both at the cost, as well as, on the revenue side. However, under dynamically changing prices and various cost components, as is the case of Zambia now, some analysis of this issue should be carried out. Synthetic answers might be, of course, found in the IRR sensitivity analysis.

- Similar remarks refer to exchange rate and devaluation issues. Cost of imported fixed capital, all foreign operational expenses, foreign debt service expressed in terms of Kwacha might change dramatically due to potential devaluations in the future. At which rates of exchange were both appraisal versions done?

- Grade period on local loan should be two years (according to assumptions p. 21 of Memo of 19/1/1990); as shown in the COMFAR schedules it actually is only 1 year;

In general, in a country of a high rate of inflation, repeated devaluations of local currency and possible structural changes of inflation rate for various groups of cost items on the one hand, and final product prices - on the other, it is very difficult to carry out a convincing commercial evaluation of an industrial project.

After introducing some improvements to the second (11/7/90) version of the appraisal - commercial viability of the project might be proved.

The most sensitive issue seems to be however financing of the project. This is probably the weakest link and the vaguest issue in the whole set of documents.

Proposed structure of the sources of finance needs some clarification. As it is presented now in the documents, this issue may leave considerable doubts (e.g. relation between local and foreign loan, structure of equity, terms like "NMC internal generation"). From which funds is the interest during production covered?
From equity contribution?

III. ATTITUDE OF SHAREHOLDERS "B"

Apparent unwillingness of shareholders "B" to support the project and participate in its financing has to be probably seen on a wider background.

Even though the project might seem relatively attractive in commercial terms, as later appraisal proves - the actual reason for lack of enthusiasm are deeply rooted in private investors' opinion about poor performance and low efficiency of NMC in general.

They might see, as well, alternative, more attractive - from their point of view - ways of capital allocation. They might be relatively more interested in doing good business in general and not necessarily providing the region with staple food, which the local point of the Government's approach.