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Foreword

On behalf of Government, I have the pleasure once again of presenting the Green paper, 2006-2008 in the spirit of Government's continued commitment to engage in dialogue with all stakeholders on major economic development issues. The Green Paper is being issued at a time when the country is preparing the Fifth National Development Plan (FNDP), which will succeed the Transitional National Development Plan (TNDP). The TNDP comes to the end in December 2005. This Green paper therefore, reflects a transitional phase between TNDP and FNDP.

The process of preparing the FNDP has involved extensive consultations with stakeholders on the policies and priorities to be included in the plan. These consultations which are continuing included visits to all 72 districts to discuss local development concerns. The Sector Advisory Groups (SAGs) have also prepared drafts of their respective chapters of the FNDP. Overwhelming policy recommendations have been received from these consultations. From preliminary indications the priorities of the FNDP include rural infrastructure, agricultural development, and fighting HIV/AIDS pandemic and malaria.

The current Green Paper reflects the phasing out of the issues that were being tackled in the TNDP while anticipating those being put forwards in the on-going consultations for the FNDP. In many instances, of course, it is expected that issues from the TNDP will continue under the FNDP.

To meet these priorities, macroeconomic objectives over the period 2006 to 2008 are aimed at sustaining, accelerating and broadening the economic gains that have been achieved in the last four years so as to reduce poverty. Strong growth over the medium term is expected to come from mining, construction, tourism, agriculture and manufacturing. Although growth will be driven by mining and construction, investment in rural infrastructure and pro-poor labour intensive sectors such as agriculture and manufacturing processing will be the key priorities over the medium term.

Government intends to re-orient expenditures towards the outlined priorities in the FNDP. Through the harmonisation of aid effort with the development partners, Government is also working with the donors to ensure that their financial assistance comes in only to support the priorities that the country has identified. Government will also deepen the implementation of structural reforms such as the public expenditure management and financial sector development reforms including the private sector development action plan.

The key challenges that Government faces over the medium term are to prioritise the recommendations from the districts and SAGs and realign expenditures to the outlined priority areas including mobilising revenues to meet the demands coming from the districts.

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1.0 INTRODUCTION

1.1 This Green paper is divided in six sections. Section one is the introduction while section two outlines Government's macroeconomic intentions for the period 2006-2008. These proposed intentions will be a major input into the preparation of the 2006 budget and the 2006-2008 MTEF. Section three proposes how Government resources will be allocated by type of expenditure. Section four, which is a new section presents expenditures by function. It is hoped that this new section will give the public more insight into the government's spending planning in various sectors. Section five provides indicative expenditure ceilings for Ministries, Provinces and Spending Agencies (MPSAs). Section six concludes.

2.0 MACROECONOMIC FRAMEWORK, 2006-2008

2.1 Policy Objectives

2.1.1 Government's macroeconomic goal over the period 2006 to 2008 is to sustain, and build on the economic gains that have been achieved in the recent past. The specific objectives include the following:

- i accelerate pro-poor growth;
- ii reducing the rate of inflation to single digits;
- iii safeguarding the economy against domestic and external shocks; and
- iv maintaining the external current account deficit and external debt position at a sustainable level.

2.2 Macroeconomic Targets and Strategies, 2006-2008

2.2.1 Targets

4. In line with the broad objectives outlined above, Government's specific macroeconomic targets for the period 2006-2008 are to:

- i. Achieve real GDP growth rates of 6 percent per year;
- ii. Bring down end-year inflation to 10 percent in 2006 and 5 percent in 2007 and 2008;
- iii. Reduce domestic borrowing to 1.6 percent of GDP in 2006, 0.7 percent in 2007 and 0.5 percent in 2008;
- iv. Increase the official Gross International Reserves (GIR) to 1.5 months of imports cover in 2006, 1.8 months of imports in 2007 and 2.2 months of imports in 2008; and

- v. Remain current with foreign debt service which has significantly reduced after reaching the HIPC Completion Point. Foreign debt service amounts to K130.0 billion or 0.3 percent of GDP in 2006, K184.0 billion or 0.4 percent of GDP in 2007 and K171.0 billion or 0.4 percent of GDP in 2008.

Table 1: Key Macroeconomic Targets: 2003-2008

	2003	2004	2005 Proj	2006 Proj	2007 Proj	2008 Proj
Real GDP Growth Rate	5.1	5.4	4.3	6.0	6.0	6.0
Inflation Rate (end period)	17.2	17.5	19.0	10.0	5.0	5.0
Inflation (period average)	21.4	18.0	18.8	14.4	6.3	4.9
Nominal GDP (K' Billions)	20,479	25,916	32,141	38,036	42,184	46,581
Current Account Deficit Incl. grants (% of GDP)	(7.5)	(4.8)	(4.6)	(4.7)	(3.1)	(4.2)
Domestic Borrowing (% of GDP)	5.2	2.2	1.9	1.6	0.7	0.5
GIR months of Import Cover	1.3	1.2	1.4	1.5	1.8	2.2

Source: Ministry of Finance and National Planning

2.2.2 Strategies

5. The broad strategy for this MTEF period is to achieve accelerated, high and diversified economic growth. This strategy will be supported by implementation of appropriate monetary and fiscal policies and deepening structural reforms including improving the environment for private sector development. Government's strategy is also to re-orient expenditures towards the NDP priorities, including social sector priorities.

Accelerating Economic Growth

6. **Economic growth is expected to accelerate over the MTEF period.** Real GDP growth is expected to average 6.0 percent. Mining and construction will continue to dominate the growth process during the period 2006 to 2008, especially as the result of coming on stream of the new mines at Kansanshi and Lumwana. Other sectors that will contribute to growth are manufacturing, tourism, and transport, storage and communication (see Table 2). Although growth will be driven by mining and construction, Government's focus over the medium term is to stimulate pro-poor labour intensive sectors such as agriculture and manufacturing processing. In this regard particular attention will be on expanding rural infrastructure such as feeder roads, bridges and dams, among others.

7. Growth in the construction sector is premised on increased public and private construction activities, especially in residential housing around the main urban centres and facilitating mining sector investments at Kansanshi and Lumwana mining areas.

8. In the mining and quarrying sector, higher production of copper is expected as a result of opening up of the new mining at Kansanshi and Lumwana mines. The rising world metal prices will provide the impetus for the mining companies to produce more. Despite significant contribution of large scale mining to the overall mining sector, Government strategic focus in the next three years will be on promoting small-scale mining and the gemstone sector. This is in view of the potential that small-scale mining and gemstone sector has in creating employment

especially in rural areas where jobs are scarce. Programmes to be implemented during the MTEF period will focus on the following:

- strengthening the institutional framework support by way of the geological survey department providing affordable geological services;
- strengthening regional mining bureaus and decentralising the functions and strengthening the department of mines safety;
- increasing exploration and geological mapping of Zambia;
- improving access to capital and equipment;
- setting up a skills training centre in order to provide skills and knowledge in mine safety, valuation and grading, business management and entrepreneurship skills and down stream processing of gemstones and other minerals; and
- facilitating linkages for marketing of processed and rough gemstones and other minerals.

9. Other priority programmes in agricultural marketing, trade and agribusiness development, irrigation development and support, agricultural infrastructure and land development, agriculture research and technology development, agriculture extension, animal health and livestock production and extension, among others. Priority will also be on fisheries development and the key programmes will be aquaculture development, capture fisheries management and development and fish processing and marketing.

10. In the energy sector, key programmes over the MTEF period will focus on the following:

- increasing supply of energy and access for rural income generation and activities for households;
- improving accessibility and service delivery to agriculture, manufacturing, tourism, mining and other commercial activities;
- promoting investment in the electricity industry;
- integrating electrification programmes within national development plans;
- increasing generation and transmission capacity for local and regional markets;
- enhancing security and cost-effectiveness of supply of petroleum;
- improving efficiency in the petroleum sector;
- ensuring prompt response to and minimisation of possible emergencies and disasters;
- ensuring better management of woodlands and forests as a sustainable source of wood fuel; and
- Improving the technology of charcoal production and utilisation, among others.

Table 2: Real Gross Domestic Product Growth

	Annual Percentage Change			
	2005	2006	2007	2008
GDP (market prices)	4.3	6.0	6.0	6.0
Primary sector	2.7	9.4	8.2	6.4
Agriculture, forestry & fishing	3.0	5.0	4.0	4.0
Mining and quarrying	2.2	17.5	15.0	10.0
Secondary sector	6.4	5.9	6.6	8.0
Manufacturing	2.6	5.0	6.0	7.0
Electricity, gas & water	3.6	2.3	5.5	14.0
Construction	12.5	8.0	7.5	7.5
Tertiary sector	4.1	4.6	4.8	5.0
Wholesale and retail trade	5.1	5.0	5.2	5.4
Restaurants and hotels	10.9	7.0	6.0	6.0
Transport, storage & communication	2.2	7.0	8.0	8.5
Financial intermediation & insurance	3.5	3.5	4.0	4.5
Real estate and business	5.0	5.0	5.0	5.0
Community, social and personal services	1.8	3.0	3.0	3.0
Other	1.4	1.4	1.4	1.4

Source: Ministry of Finance and National Planning.

11. Manufacturing will continue to be dominated by food processing and textiles. However, in line with Private Sector Development (PSD) action plan, the intention of Government is to broaden the manufacturing base by removing bottlenecks across all manufacturing sub-sectors. Additionally, attention will also be paid on attracting investment, improving product quality and standards.

12. In Tourism, growth will continue to be driven by public and private sector investments. Key programmes will include:

- developing and rehabilitating tourism and support infrastructure in the Kafue National Park and surrounding Game Management Areas, Lower Zambezi (Siavonga to Feira), Luangwa Regional Programme and Sioma Ngwezi and West Lunga National Parks;
- promoting investment in the tourism sector by among other things, enhancing tourism development credit facility and developing policies targeted towards tourism development;
- diversifying the tourism products through museums development programme, heritage development programme and cultural/ethno tourism development programme, among others; and
- promoting local community participation and ownership in tourism.
- Streamlining the licensing framework in the sector.

Monetary and Financial Sector Policies

13. **Monetary and financial sector policies will build on the gains made in the recent years** in reducing inflation and interest rates. Monetary policy will, therefore, principally be focused on achieving price stability. To improve monetary policy management, coordination between Bank of Zambia and the Ministry of Finance and National Planning will be improved with regard to cash management so as to make monetary policy more effective through the control over monetary growth.

14. Other measures will include improving the payments systems so as to reduce the use of cash as the dominant means of payments in the economy. This will entail among others, enacting the Payments Systems Bill so as to provide legal backing to the development of the payments system. The scope of financial instruments will also be expanded through the establishment of primary dealers. This should result into a wide distribution of government securities and increased liquidity in the secondary market. In addition, market making in the government securities and equities markets will also be introduced. The operational autonomy of the Bank of Zambia in formulating monetary and supervisory policy will also be reinforced.

15. Financial sector policies will primarily be focused on expanding financial intermediation and access to financial services both in urban and rural areas so as to contribute to the achievement of rapid pro-poor growth. To achieve this vision, a Financial Sector Development Plan (FSDP) was prepared in 2004 and implementation commenced in 2005. The FSDP is a master plan for the development of the financial sector and its main focus is on developing the capital markets, enhance the role of micro financing in the economy and rural financing, and strengthen the banking and non banking financial institutions. It also seeks to enhance the role of pensions and insurance in the financial sector.

16. To develop the capital market, attention will be devoted to activating secondary market activity on the stock exchange by developing broad and deep primary and secondary bonds market. Corporate entities and local authorities will, therefore, be encouraged to issue corporate and municipal bonds through the LuSE. To facilitate this, bond listing rules on the LuSE will be finalised and implemented by 2006. The Government will also introduce long term bonds partly to encourage the development and emergence of privately issued longer dated capital market instruments as well as for raising funds for targeted development projects.

17. In the light of the focus on rural led development under the FNDP, one of the key strategies in the MTEF period will be to develop a well functioning micro and rural financing system. The first step will be the preparation of a comprehensive rural financing policy and strategy which has been absent. The policy and strategy will provide a framework for the provision of rural financing. Efforts towards the preparation of the rural financing policy and strategy already commenced in 2005 and it is expected to be in place in 2006. Apart from developing and implementing a rural financing policy and strategy, the National Savings and Credit Bank (NSCB) will be jointly capitalized with the International Fund for Agricultural Development (IFAD) and its rural branch network expanded further. This will be after the Bank has been transformed into a viable institution within the context of the FSDP.

18. In the area of Non-Bank Financial Institutions (NBFIs), the focus in 2006 will be on incorporating the Development Bank of Zambia (DBZ), Zambia National Building Society (ZNBS) and National Savings and Credit Bank (NSCB) as limited liability companies under the Companies Act. This is in line with the FSDP implementation plan. In 2005, the focus was on harmonisation of the Banking and Financial Services Act (BFSA) with the DBZ Act, the Building Societies Act and the NSCB Act, which were in conflict with the Banking and Financial Services Act.

19. Reforms in the pension system will involve: (i) amending the Pensions Scheme Regulation Act, 1996 and harmonizing all legislation affecting pensions; (ii) streamlining taxation with regard to pension funds incentives for pension funds; (iii) effecting of consumer education programmes; (iv) conducting a study on viability of personal pension plans; (v) reviewing the need for an independent supervisory authority for National Pension Scheme Authority (NAPSA); (vi) establishment of investment guidelines; (vii) creation of a supervisory authority for the NAPSA; and (viii) implementation of a comprehensive financial reform programme for Public Service Pensions Fund (PSPF) and Local Authorities Superannuation Fund (LASF).

External Sector Policies

20. The external sector objectives are to maintain a sustainable and viable current account balance, improving the external competitiveness of the economy and maintaining a sustainable external debt position. To sustain a viable current account balance, the main strategy remains that of promoting export growth. Although the mining sector will still continue to play an important role in Zambia's external sector position especially with the opening up of new mines in the North Western province and the reinvestments on the existing mines on the Copperbelt, Zambia's export development strategy will remain focused on diversification away from copper.

21. Export development policies will continue to be centred on maintaining a liberal trade policy while ensuring a competitive, expanded and diversified export production base. In this regard, Government will continue to push for improved market access while addressing the supply side constraints and enhancing the competitiveness of the domestic industry through the implementation of the PSD action plan.

22. Apart from the implementation of the PSDP, Government will continue with : (i) the establishment of an accessible and affordable export financing facility; (ii) strengthening and decentralizing the administration of sanitary and phytosanitary as well as the standards testing and certification services; and (iii) strengthening the export-oriented investment promotion and the export promotion functions.

23. Following the country reaching the Enhanced HIPC Initiative Completion Point in April 2005, which has resulted in the easing of the external debt burden, the prime goal in the medium to long term is to avoid a return to the unsustainable position of the last three decades. In this regard, a debt reform and capacity building programme has been prepared and its implementation started in 2005 which will among other things result in development of a debt policy and strategy by 2006 that will see the laws that govern public borrowing be revised and a new law put in place.

24. In the area of aid management, attention will be devoted to maximizing the impact of aid on growth and poverty reduction. This will be achieved through the provision of aid in a more predictable manner, which is aligned to the development priorities. Predictability of aid is expected to be enhanced through implementation of the Harmonisation in Practice (HIP) principles whose design has reached an advanced stage. In April 2005, a Memorandum of Understanding on Poverty Reduction Budget Support (PRBS) was signed by four cooperating partners. It is expected that other cooperating partners will come on board.

Structural reforms

25. **Implementation of structural reforms will continue.** The reform agenda is in the area of public service reform, private sector development and parastatal reform and privatisation. The pace of implementation of reforms will be accelerated and will be aimed at improving the business and investment climate in the provision of basic infrastructure, delivery of basic services, expenditure and financial accountability, and strengthening the financial system.

Public Service Reform Programme

26. The overall goal of the Public Service Reform Programme (PSRP) is to improve the quality, efficiency, cost effectiveness and delivery of public services to the people of Zambia. It focuses on Public Expenditure Management and Financial Accountability Reforms (PEMFA), Public Service Management (PSM) and Decentralization.

27. The key activities under PEMFA to be implemented are the rolling out of the Commitment Control System (CCS) and Financial Management System (FMS) to all spending agencies, overhauling of the legal and regulatory framework, implementation of the new financial management system (through IFMIS) and reform of the public procurement system. Another important reform milestone under the PEMFA will be the development and implementation of a debt management strategy for Zambia. A new public debt strategy and policy will be developed and as part of that process, the laws that govern public borrowing will be revised and new law put in place.

28. With regard to public service management, the focus is on rightsizing and pay reforms. Under right sizing, the main actions to be undertaken will be the completion of the restructuring of the remaining ministries and all provinces and enforcing the policy on hiring and firing.

29. As for pay reforms, the main objectives are to (i) ensure that employee remuneration is related to the job responsibilities and performance (ii) attract and retain essential technical, professional and managerial staff in the Public Service through clear pay policy and strategy; (iii) pay arrangements support and reinforce improved service delivery; (iv) increases in pay levels are consistent with the resource envelope (i.e. MTEF provisions). The key milestones to be undertaken will be the development and implementation of a pay policy. The pay policy and strategy should also help reduce discrepancies in remuneration to the different categories of public officers/officials. The Pay policy is expected to be developed and implemented in 2006/2007.

30. With regard to decentralization, the goal is to empower local governance structures to effectively participate in the formulation and implementation of development programmes. There are three phases in the implementation of the decentralization policy: (i) Phase I (2002 – 2005) was devoted to preparation of the decentralisation policy and implementation plan. (ii) Phase II (2006 – 2010) will be devoted to implementation of the policy through ten key components. Among these will be development of legal and institutional frameworks, execution of “bottom-up” development process, sector devolution that will entail transfer of functions and fiscal resources to lower level governance structures; (iii) Phase III (2010 -2011) will be review period of progress made over the nine-year period.

Private Sector Development

31. The key milestones to be achieved under the PSD program include will be the creation of a “One-Stop-Shop” for business investment as a solution to the problems of red tape barriers to business entry and streamlining procedures in issuance of licenses and permits. Other important milestones will be the liberalisation of the International Telecommunication Gateway.

Parastatal Reform

32. The main objectives of Government’s parastatal reform programme are to: (i) scale down on Governments’ direct involvement in commercial activities by disposing off entities that could be better run by the private sector; (ii) reduce any budgetary outlays to state-owned enterprises; (iii) promote competition and improve the efficiency of state owned enterprises; and (iv) encourage wider share ownership and minimise the involvement of Government bureaucracy in the operations of enterprises.

33. During the period 2006-2008, the main attention will be devoted to improving the operations of the utility companies in the energy and telecommunications sectors, namely ZESCO and ZAMTEL. The strategy being pursued is that of commercialisation. The process of commercialising ZESCO started in 2004 and is expected to be completed in 2006. A framework to ensure effective management and regulation of ZAMTEL operations to prevent anti-competitive behavior will also be developed. Still in the energy sector, the possibility of leasing out of the operations of Indeni Oil Refineries will be considered. This is aimed at encouraging new private investment in the refinery so as to improve efficiency. Government will instead focus on managing fuel strategic reserves. In this regard, Government will build infrastructure for strategic reserves.

34. The reform process in a number of sectors will also continue to be undertaken. In the financial sector, the 49 percent Government shareholding in the Zambia National Commercial Bank (ZNCB) will be disposed off. Additionally, 25 percent shares in ZNCB will be floated on the Lusaka Stock Exchange. Other notable parastatals that require attention include the Nitrogen Chemicals of Zambia (NCZ). In the event that no private investor acquires the company, Government will undertake a due diligence of the plant to determine which operations can be commercially sustained. This is because although fertilizer is an important commodity for agriculture purposes, importing the commodity at the moment is a much more cost

effective option than operating the NCZ which has obsolete equipment and outdated technology.

Social Sector Policies

35. Besides the need to accelerate growth and reduce poverty, Zambia is faced with formidable social sector challenges especially in health and education which require to be effectively addressed if the goal of accelerating growth and rapidly reducing poverty is to be attained.

36. In the health sector, the key challenges where attention will continue to be focused are in the fight against HIV/AIDS, tuberculosis and malaria, the high infant, under five and maternal mortality and resolving the general human resource deficiencies in the sector. Addressing these concerns will remain the major focus of the health policy which will also enhance the chances of Zambia attaining the Millenium Development Goals (MDGs) related to these areas.

37. In the education sector, the goal over the MTEF period is to strive to bring the teacher pupil ratio, which currently stands at 52 to internationally accepted levels of 35-40. In this regard, more attention will be paid to the recruitment of teachers and mitigating the impact of HIV/AIDS which has been one of the factors in teacher staffing levels.

Cross-cutting Issues

38. To accelerate pro-poor growth which is being advocated in the FNDP, cross-cutting issues of gender and environment will be a major focus in this MTEF. In this regard, mainstreaming gender in all the sectors will continue to be one of the key programmes. In environment, aforestation and waste management will be among the key programmes.

3.0 FISCAL FRAMEWORK, 2006-2008

3.1 Objectives

Promoting Macroeconomic Stability and Fiscal Sustainability

39. The medium-term fiscal policy stance for the period 2006-2008 is consolidation so as to promote macroeconomic stability. This is in the light of a huge domestic debt and high inflation and interest rates. The fiscal programme therefore envisages to keep the overall deficit below 3.0 percent of GDP over the medium term. This is expected to be achieved by expenditure restraint. In line with the overall deficit, domestic borrowing will be maintained at the 2005 level of 1.6 percent of GDP in 2006, and reduce it to 0.7 percent in 2007 and 0.5 percent in 2008. Apart from reducing domestic borrowing, Government will also pay particular attention to the payment of domestic arrears.

Re-Orienting Expenditures to Developmental Programmes

40. Although Government's stance is to run a non-expansionary fiscal policy over the medium term, more attention will be devoted to reorienting expenditures towards identified pro-poor growth programmes. These are in the areas of infrastructure development in agriculture, education and health.

41. In addition to re-orienting expenditures to pro-poor growth programmes, Government's focus will be on gradual deconcentration of government functions and resources to the district level and tracking the effectiveness of the public expenditures. In this regard, Public Expenditure Tracking Surveys (PETS) will be developed and implemented.

Improving Efficiency, Revenue Productivity and Equity of the Tax System

42. In the area of taxation, Government's objective in the medium term is to reform the entire tax system so as to improve its efficiency, revenue productivity and equity. The reform will focus on improving tax administration and widening the tax base by further bringing in the informal sector into the tax net. This is aimed at increasing domestic revenues from the current 18 percent of GDP. These efforts will generally shift the burden of taxation from production to consumption and reducing high tax incidence especially with regard to Pay As You Earn (PAYE).

3.2 Resource Envelope

43. The resource envelope, that is financial resources available for expenditure, comprises domestic revenues from taxes, non-tax revenues and exceptional revenue; grants from cooperating partners and loans (financing) from both domestic and external sources. For the 2006-2008 fiscal frame, the resource envelope available to Government will be determined by the following factors:

- (a) The collection levels of taxes by the Zambia Revenue Authority, non-tax revenues through other appointed public sector institutions, exceptional revenues such as dividends from the remaining state owned and quasi government enterprises and other miscellaneous revenues that may come;

- (b) The level of assistance from cooperating partners in form of programme and project support through general budget support, the Sector Wide Approaches (SWAPs) and direct project grants; and
- (c) The level of financing expected to be raised from both domestic and external sources. Domestic financing is usually raised from the banking and non-banking sector while external borrowing primarily comes in the form of programme and project loans.

Domestic Revenues

44. In the 2006-2008 MTEF period, the amount of domestic revenue expected is K6,835.0 billion, K7, 674.96 billion and K8, 591.0 billion in 2006, 2007 and 2008 respectively. These translate into domestic revenue to GDP ratios of 18.0 percent in 2006, 18.2 percent in 2007 and 18.4 percent in 2008.

Table 3: Projected 2006- 2008 Resource Envelope in K' Billions

	2005 Projection Outturn	2006 Projection	2007 Projection	2008 Projection
Total Resources	9,316.39	10,140.11	10,643.41	11,466.22
Domestic Revenue	5,757.68	6,835.00	7,674.96	8,591.02
Taxes	5,546.93	6,660.60	7,489.00	8,377.10
Non-taxes (fees & fines)	135.83	75.58	135.96	138.92
Exceptional Revenue	74.92	78.82	50.00	75.00
Total Grants	2,130.79	2,314.37	2,284.60	2,413.91
Programme Grants	740.37	867.71	1,002.83	1,036.18
o/w General Budget support	367.06	482.29	654.21	636.37
SWAPs	373.31	385.42	348.62	399.81
Project Grants	1,390.42	1,446.66	1,281.77	1,377.73
Total Financing	1,427.92	990.74	683.85	634.42
Domestic Financing	499.96	592.00	295.29	231.19
Net External Financing	837.06	398.74	388.56	230.10

Source: Ministry of Finance and National Planning

Grants

45. Total grants over the medium term are estimated at K2,314.4 billion in 2006, K2, 284.6 billion in 2007 and K 2, 413.9 billion in 2008. Total grants will comprise mainly project and programmes grants.

46. Project grants during the MTEF period are anticipated at K1,446.7 billion for the year 2006, K1,281.8 billion for the year 2007 and K1,377.7 billion for the year 2008 (see table 2.1.1) . Project grants will also be forthcoming for as long as Government disburses counterpart funds where applicable.

47. Support under *Programme* grants is expected to increase in nominal terms from the projected outturn of K740.4 billion (2.3 percent of GDP) in 2005 to K867.7 billion (2.3 percent of GDP) in 2006, K1, 002.8 billion (2.4 percent of GDP) in 2007 and slightly increase to K1, 036.2 (2.3 percent of GDP) in 2008. The enhanced programme grants are expected to come mostly as general budget support and partly

as SWAPs. These funds are expected to be directed mostly to the health and education sectors of the economy. The release of most of these programme grants will be linked to prudent expenditure management and effective programme implementation.

Domestic and Net External Financing

48. Domestic borrowing for 2006 will be maintained at 2005 level of 1.6 percent of GDP. In 2007 and 2008 domestic borrowing is expected to drop to 0.7 percent and 0.5 percent of GDP, respectively. This is expected to contribute to enhancement of macroeconomic stability especially reduction of interest rates.

Net external financing is expected to be K398.7 billion, K388.6 billion and K230.1 billion in 2006, 2007 and 2008, respectively.

Total Expected Resources for the MTEF Period 2006-2008

49. The total expected resources for the MTEF period are K10,140.1 billion for 2006, K10,643.4 billion in 2007 and K11,466.2 billion in 2008.

3.3 Expenditure by Type

50. Total expenditures over the medium term is estimated at K10, 140.1 billion in 2006, K10, 643.4 billion in 2007 and K11, 639.4 billion in 2008. As a percentage of GDP the expenditures are estimated at 26.7 percent, 25.2 percent and 25.0 percent in 2006, 2007 and 2008 respectively.

Personal Emoluments

51. Government's intention is to continue to cap on the national resources going to pay civil servants in order to leave reasonable amounts to spend on developmental expenditures. In the past five years approximately an average of eighty-five percent of the capital expenditures have been largely been financed by foreign grants and loans and hence, the need to increase the share of government funding for development projects. In this regard, Government's wage bill has been projected to be 7.9 percent of GDP in 2006, 7.9 percent in 2007 of GDP and 8.0 percent of GDP in 2008. This is still above the sub-Saharan average of 7.5 percent.

52. The medium term pay reform allocation in the three year period stands at K298.5 billion, K196.6 billion and K164.7 billion in 2006, 2007 and 2008 respectively. This is the amount of resources available for any increments in salaries of civil servants in the medium term.

53. Government has also made provision for the civil servants housing allowance amounting to K121.0 billion, K126.3 billion and K131.2 billion in 2006, 2007 and 2008, respectively. This is an increase compared to the 2005 levels and is premised on increased number of staff due to the net recruitment done in 2005 in the ministries of education and health.

Public Service Reform Programme (PSRP)

54. Total allocation towards the PSRP in the medium term is projected at K232.8 billion and broken down into the following instalments, K75.0 billion in 2006, K80.0 billion in 2007 and K77.8 billion in 2008. This is supposed to cater for retrenchments that are going on in the ministries and departments being restructured.

Recurrent Department Charges (RDCs)

55. By the end of 2005 the projected outturn of RDCs is K1, 448.3 billion. Over the medium term Government projects to spend K1,437.9 billion in 2006, K1,661.9 billion in 2007 and K2, 508.6 billion in 2008. As a ratio of GDP, RDCs are estimated at 3.8 percent in 2006, 3.9 percent in 2007 and 5.4 percent in 2008, respectively.

56. To accommodate general elections in the year 2006, ordinary RDCs have been projected at lower levels of 2.6 percent of GDP compared to 3.2 percent in 2005. In 2007 and 2008 ordinary RDCs are projected at 3.2 percent and 3.6 percent of GDP, respectively.

57. In 2006, a total of K240.2 billion has been allocated to general elections and this translates to 0.6 percent of GDP. In 2007 the country is expected to continue with the constitutional review process. It is expected that the census will be conducted by the Central Statistics Office (for purposes of Article 79 of the constitution) at an estimated cost of K95.1 billion. In 2008, it is expected that a referendum process will be undertaken to comply with the alteration of Article 79 Part III of the constitution at an estimated cost of K500.0 billion.

58. To clear domestic arrears of goods and services, K100.0 billion, K114.4 billion and K250.0 billion has been allocated in 2006, 2007 and 2008, respectively. This is an effort to release locked-in resources to the private sector. An additional total amount of K76.3 billion has been allocated in the three year period to clear the 2003 housing allowance arrears owed to civil servants. The provision has been broken into two instalments of K38.2 billion each in 2006 and 2007.

59. To honour judgments made against Government in the courts of law, a provision of K60 billion per year over the medium period has been made.

Transfers and Pensions (Grants and Other Payments)

60. For the period 2006, 2007 and 2008 transfers and pensions are projected to stand at K1, 582.2 billion, K1, 614.9 billion and K 1, 574.9 billion respectively. As percent of GDP, these allocations are at 4.2 percent, 3.8 percent and 3.4 percent in 2006, 2007 and 2008 respectively.

61. Transfers to Zambia Revenue Authority (ZRA) are projected at K130.0 billion in 2006, K139.4 billion in 2007 and K146.4 billion in 2008. Apart from covering salaries and wages these resources are meant for operational and capital expenses for the institution so as to enhance tax revenue collection.

62. In order to facilitate the early retirements Pensions Fund has been allocated K254.0 billion in 2006, K266.00 billion in 2007 and K174.3 billion in 2008. This is in addition to the 7.25 percent employer's contribution in the Personal Emoluments.

Other Current Expenditure

63. In a continued effort of ensuring food security in the nation, Government will subsidise agricultural inputs such as fertiliser to medium and small-scale farmers. As such Government has made provisions towards the Fertilizer Support Programme amounting to K150.0 billion per year over the medium term.

64. The Food Strategic Reserve is another programme that Government continues to pursue to ensure food security for the country. Total allocation of K100.0 billion has been provided for this purpose, and broken down in two instalments of K50.0 billion and K50.0 billion in 2006 and 2007 respectively. In the year 2008, Food Reserve Agency (FRA) is expected to be self sustained.

65. Government has also allocated resources for contingency amounting to K10.0 billion in 2006, K12.0 billion and K20.billion in 2008. This vote is meant to cover unforeseen events.

66. A provision of K240.0 billion provision has been made for financial restructuring and contingent liabilities over the three year period and broken down to three instalments of K80.0 billion. This will be used to restructure remaining parastatals, which will only be done once a bankable restructuring plan is produced and approved by Government. Contingent liabilities include bad loans that have been guaranteed by Government on behalf of some parastatals.

Capital Expenditure

67. Capital expenditures continue to be largely financed from the external resources through grants and loans, although at lower levels compared to the previous MTEF period. Approximately an average of 69.6 percent of the capital expenditures will be financed from external resources compared to the 85 percent in 2005-2007 period. In this vein Government has allocated K2, 766.6 billion or 7.3 percent in 2006, K2, 935.7 billion or 7.0 percent in 2007 and K2, 841.3 billion or 6.1 percent in 2008.

68. The estimates for foreign financed capital expenditures are projected to be falling in the medium term from K2, 178.25 billion in 2005 to K2, 000.7 billion in 2006, K1, 791.3 billion in 2007 and K1, 794.8 billion in 2008. Reflected as a percentage of GDP these capital expenditures will fall from the level of 6.8 percent of GDP in 2005, to 5.3 percent of GDP in 2006, and reducing further to 4.2 percent and 3.8 percent of GDP in 2007 and 2008 respectively. Programmes to be covered under these funds will be directed towards road projects, road repairs, water development projects, among others.

69. In contrast, capital expenditure financed from the domestic resources and general budget support¹ is projected to increase from the 2005 levels of 1.8 percent of

¹ General budget Support include grants from our cooperating partners that are not tied to any particular expenditure programme and are at the discretion of Government.

GDP to 2.0 percent in 2006. This is expected to further increase to 2.7 percent of GDP in 2007 and reduce to 2.2 percent of GDP in 2008 respectively. These funds are expected to cover counterpart-funding provision to support foreign financed projects, road rehabilitation projects and road repairs, rural electrification projects, and land development as well as purchase of movable assets.

70. Government has continued to make provisions for on-going and new road projects and these are projected to increase from expected outturn of K100.0 billion in 2005, to K261.5 billion in 2006, K242.0 billion per year 2007 and 2008. As a ratio of GDP this is significantly increasing to 0.7 percent of GDP in 2006 compared to 0.3 percent projected for 2005. In 2007 and 2008 allocations slightly reduce to 0.6 percent and 0.5 percent of GDP.

71. Further, allocations have been made to cover the maintenance of existing road infrastructure under the Road Fund, which is financed from the Fuel Levy and other road taxes and these stand at K194.8 billion, K220.7 billion and K245.0 billion in 2006, 2007 and 2008 respectively.

72. Land development Fund, is one of the ear-marked expenditure items which will be financed from the land rent. Government's objective is to develop land for agricultural use, among others. Over the medium term a total allocation of K11.5 billion has been made annual allocations of K3.6 billion, K3.8 billion and K4.1 billion in 2006, 2007 and 2008 respectively.

73. Government has made provision of a total allocation of K3.0 billion over the medium term period for construction of access roads and other site requirements for stadia expected to be financed through bilateral cooperation and partnership with the private sector under Build, Operate and Transfer (BOT) scheme.

Constitutional and Statutory Expenditure

74. Constitutional and Statutory expenditures are obligatory in nature and primarily include expenditure related to domestic and foreign debt service obligations. They also include the cost of the salaries and conditions of service of constitutional office holders.

75. With regard to foreign debt service obligations, Government policies were principally tailored to preserving the gains made in the 2004 fiscal year, which saw the country reach the Completion Point under the enhanced HIPC Initiative. This attracted cancellation of the foreign debt that Zambia owes to its creditors such as the Paris Club. As a result of this Government realised savings of K161.0 billion in 2005 and envisages more savings in the medium term. As such, the projections of servicing foreign debt have reduced from the expected outturn of K151.7 billion in 2005 to K130.0 billion in 2006, however the debt figures are expected to increase to K184.0 billion in 2007 and K171.0 billion in 2008.

76. Due to the reduced cost of domestic borrowing attributed to the continued fall in interest rates on Government Securities in 2005, the projected cost of servicing the domestic debt in 2006 stands at K777.6 billion, and then drops to K491.0 billion and K463.0 billion in 2007 and 2008 respectively. As share of GDP, the cost of servicing

domestic debt is projected at 2.0 percent in 2006, 1.2 percent and 1.0 percent in 2007 and 2008 respectively

78. The upward adjustment of salaries for Members of Parliament (MPs) and other constitutional office holders done in 2005, but to be implemented in 2006, implies an increase in the allocation. Thus the projected costs of the constitutional posts over the medium term are K23.7 billion in 2006, K25.6 billion in 2007 and K25.6 billion in 2008.

3.4 Summary of Central Government Budget for 2006-2008

79. In summary the central government budget for the period 2006-2008 is expected to be as follows:

- Total revenue and grants in 2006 are projected to mount to K9, 149.4 billion, K9, 959.6 billion in 2007 and K11, 004.9 billion in 2008;
- Total central government expenditure (excluding amortisation) in 2006 are estimated to amount to K10, 140.1 billion, K10, 643.4 billion in 2007 and K11,639.4 billion in 2008; and
- Thus from the projected total revenues and the proposed expenditures for the period 2006-2008, the overall financing requirement is estimated to stand at K990.7 billion in 2006, K683.8 billion in 2007 and K634.4 billion in 2008 or 2.6 percent, 1.6 percent and 1.4 percent of GDP respectively

Table 4: Summary Central Government Operations in K'-billion, 2006-2008

	2005 Proj Outturn	2006 Proj	2007 Proj	2008 Proj
Revenue and Grants	7,888.47	9,149.37	9,959.56	11,004.93
Total expenditure	9,316.39	10,140.11	10,643.41	11,639.35
Current Expenditures	4,353.33	6,442.15	6,135.06	6,283.84
Of which: Personnel Emoluments (PEs)	2,542.37	3,018.80	3,320.14	3,727.24
Other PE Related Expenses	130.57	113.17	118.17	77.76
RDCs	1,448.32	1,437.92	1,661.87	2,508.57
Grants and Other Payments	1,311.39	1,582.21	1,614.90	1,574.89
Other Current Expenditure	308.78	290.05	292.00	250.00
Interest payments	815.70	931.34	700.61	659.61
Domestic	651.00	777.60	491.00	463.00
Foreign	151.70	130.00	184.00	171.00
Constitutional Posts	13.00	23.74	25.61	25.61
Capital Expenditure	2,759.26	2,766.62	2,935.71	2,841.28
Overall Balance	(1,427.92)	(990.74)	(683.85)	(634.42)
Financing	1,337.02	990.74	683.85	461.29
Domestic	499.96	592.00	295.29	231.19
Foreign	837.06	398.74	388.56	230.10
Financing Gap	90.90			173.13

Source: Ministry of Finance and National Planning

4.0 EXPENDITURES BY FUNCTION

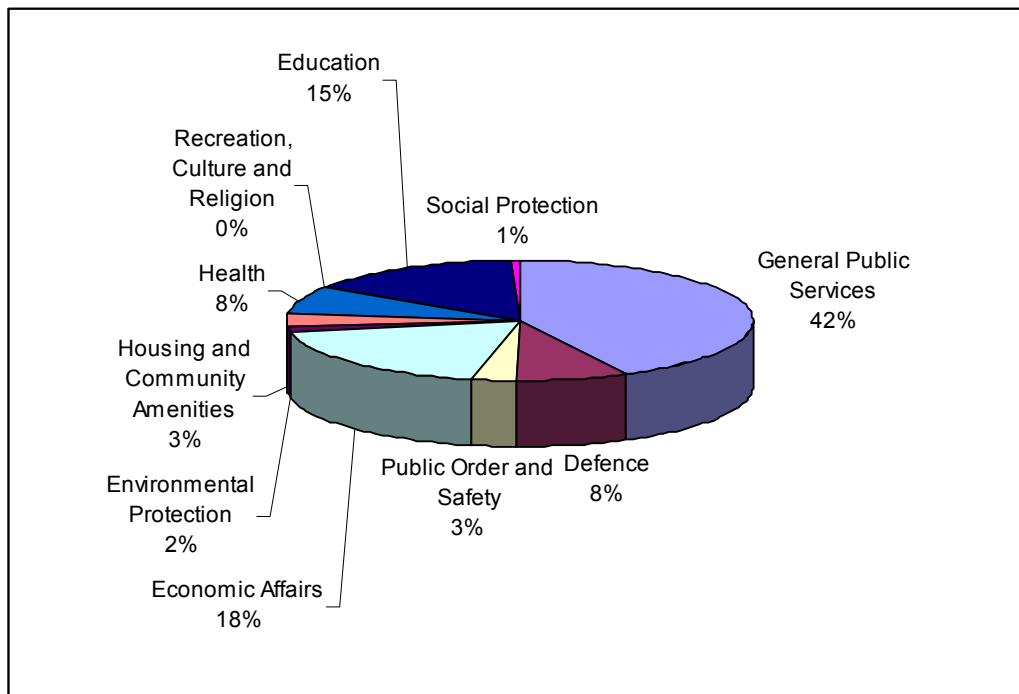
80. The Green Paper 2006-2008 has a new chapter introduced to provide information on government spending plans. These projections are based on the 2005-2007 forecast as provided by the Ministries, Provinces and Spending agencies (MPSAs) last year. This also takes into account all firm decisions that Government has undertaken in its effort in pursuing economic development and poverty reduction goals.

General Public Services

81. General Public Services include functions such as administration and operation of /or support to the executive and legislative arms of government, administration of financial and fiscal affairs and services. It also includes Research and Development (R&D) related to General Public Services, administration of the government agencies involved in applied research and transfers to Local Authorities and other quasi government institutions such as Zambia Revenue Authority.

82. In 2006 Government proposes to spend 42 percent of the projected total expenditure on General Public Services, however, in the years 2007 and 2008, the share of total expenditures is anticipated to reduce to 30.1 percent per year due to the projected fall in the domestic and external debt payments.

Figure 1: Proposed Spending by Function in 2006 , as Percentage of Total Expenditure



Source: Ministry of Finance and National Planning

Table 5: Government Proposed Spending By Function, K' Billions 2006-2008

Function	2005	2006	2007	2008
General Public Services	3,863.34	4,305.55	3,203.43	3,503.19
Defence	569.05	789.63	939.05	1,026.92
Public Order and Safety	273.60	318.79	303.63	332.04
Economic Affairs	1,785.36	1,841.21	1,602.81	1,752.79
Environmental Protection	133.50	221.79	202.86	221.84
Housing and Community Amenities	625.95	293.24	1,622.83	1,774.68
Health	897.31	766.68	758.47	829.44
Recreation, Culture and Religion	15.88	18.14	17.77	19.43
Education	1,061.38	1,530.33	1,937.57	2,118.87
Social Protection	91.02	54.45	55.00	60.15
Total	9,316.39	10,140.11	10,643.41	10,966.02

As Percentage of Total Expenditures

Function	2005	2006	2007	2008
General Public Services	41.47	42.46	30.10	30.10
Defence	6.11	7.79	8.82	8.82
Public Order and Safety	2.94	3.14	2.85	2.85
Economic Affairs	19.16	18.16	15.06	15.06
Environmental Protection	1.43	2.19	1.91	1.91
Housing and Community Amenities	6.72	2.89	15.25	15.25
Health	9.63	7.56	7.13	7.13
Recreation, Culture and Religion	0.17	0.18	0.17	0.17
Education	11.39	15.09	18.20	18.20
Social Protection	0.98	0.54	0.52	0.52
Total	100.00	100.00	100.00	100.00

Source : Ministry of Finance and National Planning

Defence

83. The Defence function includes administration of the military and civil defence affairs and services. It also includes administration and operational military aid, basic R & D related to defence. Over the medium term the proposed spending is projected at 7.8 percent of the total expenditures in 2006 and will increase to 8.8 percent per year in 2007 and 2008.

Public Order and Safety

84. Public Order and Safety function includes administration of police affairs and services and fire protection services, administration and operation of courts of law, administration and operation of prisons. It also includes basic research and formulation of policy related to the public order and safety sector. Government proposes to spend 3.1 percent of the total expenditures in 2006 in this area. In 2007 and 2008 the amount reduces to 2.8 percent each.

Economic Affairs

85. This includes general economic, commercial and labour affairs, agriculture forestry, fishing and hunting affairs and services, fuel and energy affairs and services, mining, manufacturing and Construction affairs and services, transport sector including road, water, railway, air and oil pipeline and other transport, Communication, other industries such as hotels and restraints, tourism administration multi purpose projects. This also includes R&D and policy formulation related to economic affairs. As a percentage of total expenditure the economic affairs is projected to absorb 18.2 percent in 2006 and 15. 1 percent per year in 2007 and 2008.

Environmental Protection

86. This covers waste management which includes collection, treatment and disposal of waste. Waste water management is another sub-function of the environmental protection and covers sewerage system. Other sub functions include pollution abatement and protection of biodiversity and landscape, R&D in environmental protection, administration and regulation supervision to support these activities.

87. The main function undertaken by central government is that of regulatory and supervision of these activities. In 2006, 2.2 percent of the total expenditures will be directed to environmental protection, while 1.9 percent will be expended in 2007 and 2008.

Housing and Community Amenities

88. This includes administration of community development services, administration of water supply, street lighting, R & D for housing and community amenities and formulation and monitoring of overall policies and plans programs and budgets relating to housing and community affairs.

89. The Central Government functions mainly relate to peri- urban and rural water supply. Urban water supply affairs has been commercialised and is mostly in private hands. Formulation and monitoring of overall policies relating to the sector are also a function of the central government.

90. In 2006 the projected expenditures towards this function will stand at 2.9 percent and increase to 15.3 percent for each year in 2007 and 2008.

Health

91. Government outlays on health include expenditures on services provided to individual persons and on collective basis. Expenditure on individual services are concerned with medical products, appliances and equipment, outpatient services, hospital services and public health services. Services on collective basis include R& D in health sector and formulation, administration, coordination and monitoring of overall health policies, plans, programmes and budgets.

92. Government intends to spend 7.6 percent of the total expenditures in 2006 and 7.1 percent each in the years 2007 and 2008.

Religious, Culture and Religion

93. Government spending relating to this function are on recreation and sporting services, cultural services, broadcasting and publishing services and religious and other community services.

94. Over the medium-term, Government intends to spend an average of 0.2 percent of the total expenditures.

Education

95. Outlays on education include expenditure on services provided to individual pupils and students and expenditures provided on collective basis. Expenditure on individual pupil services are pre-primary and primary education, secondary education, post-secondary non-tertiary education, tertiary education, education not definable by level (vocational training and cultural development) and provision of subsidiary services to education. Services on collective basis include R& D in education sector and formulation, administration, coordination and monitoring of overall educational policies, plans, programmes and budgets.

96. In the medium term, Government envisages to spend 15.1 percent in of the total expenditures in the year 2006. This is projected to increase to an average of 18.2 percent in 2007-2008.

Social Protection

97. This includes expenditures on services and transfers provided to individual persons and households and expenditure services provided on collective basis. Expenditures on individual services include provision of social protection on the sick and disabled, old social protection schemes, survivors of the deceased, family and children, unemployment, housing, provision of social protection to immigrants, refugees and victims of criminal violence. Services done on a collective basis include R& D of the social protection function and formulation, administration, coordination and monitoring of policies, plans, programmes, budgets relating to the function.

98. On average, Government envisages to spend 0.5 percent of the total expenditures towards this function.

5.0 Indicative Expenditures Ceilings For Institutions, 2006 - 2008

99. The key factors that have been used to set the expenditure ceilings for institutions during the period 2006-2008, are the transitional or carry over programmes from the TNDP and the indicative priorities from the FNPD which include rural infrastructure, agriculture development, fighting HIV/AIDS pandemic and malaria. Historical cost structure of running the public services are also taken into account. (see table 5).

6.0 CONCLUSION

100. Government faces key challenges over the medium-term which include accelerating growth and reducing poverty as well as fighting HIV/AIDS, tuberculosis and malaria, infant mortality rate and maternal mortality rate and resolving the human resource constraints in the health and education sectors. These challenges have been outlined during the FNDP consultations and form the basis for the priority issues to be resolved during the FNDP period. The key challenge for this MTEF is therefore to re-orient expenditures towards these identified priority areas and execute the budget as approved by Parliament to meet these demands.