



Republic of Zambia

**2007 - 2009 MEDIUM TERM
EXPENDITURE FRAMEWORK AND THE 2007
BUDGET**

GREEN PAPER

Ministry of Finance and National Planning

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FOREWORD

On behalf of Government, I wish to present the Green Paper for the 2007-2009 Medium Term Expenditure Framework (MTEF) as a consultation document. Government, through this process, would like to reaffirm its commitment to preparing an MTEF based on the principles of transparency, accountability and responsibility. This Green Paper has been prepared based on the Fifth National Development Plan (FNDP) for the period 2006-2010. The strategic focus of the FNDP is socio-economic infrastructure and human resource development aimed at promoting wealth creation through sustained broad-based economic growth and poverty reduction.

In the medium-term, Government's macroeconomic objectives are aimed at preserving and consolidating the macroeconomic stability achieved in the last few years. In this regard implementation of prudent fiscal and monetary policies will continue, particularly by limiting government borrowing. Other efforts will focus on strengthening tax administration and resource mobilisation as well as reducing and realigning expenditures on non-priority areas while stepping up poverty-related expenditures.

Further, Government will continue with its structural reform programme in the area of Private Sector Development (PSD), public expenditure and financial management, and financial sector development.

This Green Paper also recognises the Decentralisation Policy which aims at devolving some functions, authority and control of resource allocation and utilisation from Central Government to Local Authorities. In this vein, Government will accelerate the implementation of reforms in an effort to improve public service delivery by placing greater responsibility on local authorities who are closer to the people.

Lastly, I urge all stakeholders to fully participate in the process by providing valuable comments that will be considered for incorporation in the 2007-2009 MTEF and 2007 Budget.

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MINISTRY OF FINANCE AND NATIONAL PLANNING

1.0 INTRODUCTION

1 This document is divided into five parts. The first part outlines Government's macroeconomic objectives for the medium-term. The second part contains Government's proposals on the allocation of resources by expenditure type; and the third part shows expenditures by functional classification. Summary of the Central Government Operations is contained in part four. The last part contains the conclusion.

2.0 THE MACROECONOMIC FRAMEWORK, 2007-2009

2.1 Macroeconomic Objectives

2 In the medium term, Government shall focus on consolidating past macroeconomic gains by maintaining macroeconomic stability. In this regard, the broad macroeconomic objectives, which are also in line with the Fifth National Development Plan (FNDP), are to:

- (a) accelerate pro-poor economic growth;
- (b) stabilise inflation at single digit;
- (c) achieve financial and exchange rate stability; and
- (d) sustain a viable balance of payments and external and domestic debt position.

2.2 Macroeconomic Targets and Strategies

2.2.1 Targets

3 During the period 2007-2009, Government aims to:

- (a) Achieve real GDP growth of at least 6 percent a year;
- (b) Bring down end-year inflation to no more than 5 percent;
- (c) Limit domestic borrowing to 1.0 percent of GDP in 2007, and 0.5 percent of GDP in 2008 and 2009; and
- (d) Increase the coverage of official Gross international reserves to at least 2.0 months of imports in 2007 and 2.4 months in 2008 and 2009.

Table 1: Key Macroeconomic Targets, 2006-2009

	2006	2007	2008	2009
Real Sector				
Real GDP	6.0	6.0	6.0	6.0
Inflation rate (e.o.p)	5.0	5.0	5.0	5.0
Inflation rate (annual average)	8.6	8.6	5.0	5.0
Nominal GDP (K' Billions)	39,299	45,283	49,555	53,116
Government Sector				
Primary balance (% of GDP)	(0.9)	(1.2)	0.07	0.52
Overall balance (% of GDP)	(2.9)	(2.3)	(1.0)	(0.5)
Domestic borrowing (% of GDP)	1.6	1.0	0.5	0.5
External Sector				
Current account balance, incl. grants (% of GDP)	(4.7)	(3.1)	(4.2)	(4.5)
Overall balance (% of GDP)	(3.3)	(3.3)	(4.6)	(4.5)
Gross International Reserves (months of import cover)	1.5	2.2	2.2	2.5

Source: Ministry of Finance and National Planning

Strategies

4. Broadly, Government's intention is to target key and potential growth sectors by diversifying from the traditional copper sector in line with strategies contained in the FNDP while relying on the private sector as a key partner in national development. In addition, prudent fiscal policies will be pursued to maintain a stable economic environment. Structural reforms especially in the financial sector will be accelerated and deepened in order to support private sector development.

Economic Growth and Poverty Reduction Measures

5. In the medium term, Government will focus on accelerating pro-poor growth by emphasising the implementation of appropriate policies. In this regard, Government will continue encouraging traditional growth areas such as mining, construction, wholesale and retail trade with a deliberate policy to targeting new growth opportunities that can significantly reduce poverty. As outlined in the FNDP, the growth strategies in the medium term shall therefore include supporting rural development, especially in the agriculture sector; encouraging stronger linkages between agriculture and manufacturing through agro processing; stimulating stronger tourism growth; and supporting the expansion of a strong and diversified economy.

6. In mining, the growth is mainly going to emanate from large-scale mining due to the opening of new mines and anticipated relative high metal prices in the medium term. The development of Lumwana mine in North Western province is particularly expected to spur growth by increasing output in the mining sector.

7. At institutional level, capacity shall be built in the Ministry of Mines and Minerals Development to undertake detailed geological mapping and extensive mineral exploration and to offer the much needed laboratory services to the mining and exploring companies. Government will also make efforts to integrating the copper sub-sector into the Zambian economy by encouraging value addition. On the regulatory and legal front, reforms shall be undertaken particularly in reviewing mining related legislation and particularly the Mines and Minerals Act (1995). Overall, the focus of Government shall be under-pinned by the diversification programme that Government has committed itself to.

8. With regard to tourism, Government shall prioritise development by concentrating on the Kafue National Park and surrounding game management areas; the Northern Circuit Development and Lower Zambezi National Park and surrounding areas. Other areas shall include Lusaka Region and surrounding areas as well as the Livingstone Regional Development Programme. Promotional and marketing strategies will be employed in order to increase the sector's contribution to GDP and employment.

9. In agriculture, the emphasis in the medium term will focus on promoting high agricultural productivity and competitiveness in order to ensure food security, income generation, creation of employment opportunities and reduction in poverty levels. Government will increase investment in irrigation development and support, agricultural infrastructure & land development; animal health and livestock research, production and marketing. Other programmes will be agricultural extension, farm power and mechanisation as well as aquaculture development.

10. In Manufacturing, the focus shall be investment promotion; technology and skills development and Micro Small and Medium Enterprises development and economic empowerment. Further, product quality improvement; support to private sector development and; export development will be prioritised in the medium term. In this respect, amongst the key strategies, Government shall prioritise the establishment of the Zambia Development Agency as a one stop shop which will amalgamate the Export Board of Zambia, Zambia Privatisation Agency, the Zambia Investment Centre and the Zambia Export Processing Zone Authority.

Monetary and Financial Sector Policies

11. Monetary policy will be geared to keeping end-year inflation to no more than 5 percent during the period.

12. In the Financial Sector, the primary objective will be to entrench and enhance financial system stability. In this regard, Government will continue to implement the Financial Sector Development Plan (FSDP). Some of the milestones to be achieved over the medium term will be obtaining a country sovereign rating from a reputable international rating agency and establishing an enabling environment for the broader access to financial services. These developments are expected to further improve transparency in macroeconomic management of the economy and lead to better borrowing terms and conditions by local entrepreneurs on international markets as well as improve access to financing by Zambians.

13. With regard to the exchange rate, Government will continue to maintain the flexible exchange rate regime in harmony with other macroeconomic objectives. Where there will be undesirable fluctuations, the Central Bank will endeavour to smoothen the movements so as to maintain stability in the market.

External Sector Policies

14. The primary objective in the external sector will be to sustain a viable current account balance, improve the external competitiveness of the economy and maintain a sustainable external debt position. To sustain a viable current account, the main strategy remains that of promoting export growth.

15. The medium focus on external loans is to avoid a return to the high indebtedness of the past. External financing will still be sourced but foreign loans will be contracted for specific projects and for general budget or balance of payments support. Therefore, any new borrowings

over the period 2007-2009 will be procured in a manner that does not affect the debt sustainability negatively. The country shall also continue to rely on highly concessional loans.

16. Other measures will focus on trade expansion and facilitation. In this regard a pilot programme that will attempt to integrate the operations of all institutions involved in trade facilitation at two points of entry (Chirundu Border Post and Lusaka International Airport) will be undertaken in the next two years.

Structural Reforms

17. Sustained economic growth requires the implementation of structural changes in the economy, so as to increase productivity in both the public and private sectors. The structural reform agenda during the medium term will focus on: private sector development by improving the business and investment climate; enhancement of efficient public service delivery system and decentralisation, particularly fiscal decentralisation.

Private Sector Development

18. Government, in collaboration with cooperating partners, will augment efforts in the implementation of the PSD Action Plan through complementary projects aimed at enhancing the participation of private sector in economic development. Further, implementation of the FSDP will also continue, so as to enhance financial intermediation and contribute to private sector development.

19. The PSD seeks to enhance the efficiency of the institutions that serve the private sector. It is expected that successful implementation of this programme will result in faster access to services, quicker and less cumbersome procedures, and greater customer satisfaction with the targeted institutions. Improvements to the regulatory frameworks will focus on tackling administrative barriers to investment.

20. Other key focus areas will be the improvement of the regulatory framework in the key area of telecommunications. Attention will be devoted to addressing the barriers to entry by among others improving the regulatory framework so as to enhance competition in the sector. The key reforms will therefore include the revision of the appropriate legislation together with the licensing framework in the sector.

Public Sector Reform

21. Government will continue with its reform programme based on the following three pillars of the public sector reform programme: (i) Public Expenditure Management and Financial Accountability (PEMFA); (ii) Public Service Management (PSM); and (iii) Decentralisation process.

22. Under PEMFA, the key milestone will be the piloting of Integrated Financial Management Information Systems (IFMIS) in a few Ministries, Provinces and Spending Agencies (MSPAs). It is envisaged that IFMIS will be rolled out to all MPSAs by 2009. With regard to the PSM, the main focus will be the right-sizing of Government and the completion of the restructuring of the remaining institutions.

Fiscal Decentralisation

23. Under decentralisation, Government intends to speed up the implementation process as stipulated in the Decentralisation Implementation Plan (DIP). One of the processes is Fiscal decentralization which is the allocation of revenue responsibilities and the rationalisation of expenditures between and among the various tiers of government. In the case of Zambia, this is between the central and local governments. Fiscal decentralisation is one of the modalities of implementing the Fifth National Development Plan 2006 – 2010 (FNDP). It is envisaged that fiscal decentralisation will improve programme implementation and service delivery at the local level.

24. The method of fiscal decentralization as explained in the Decentralisation Policy is devolution whose implementation is planned to start in 2007. Underlying this process is the recognition that successful decentralization and fiscal decentralisation in particular depends upon local governments that have capacity to carry out their service delivery assignments and that when local governments do not have delivery capacity, transferring additional capital resources and/or recurrent responsibilities will not produce desirable results/outcomes. Based on this understanding, three steps have been identified as key towards the establishment of sustainable intergovernmental transfer system in Zambia. These are as follows:

- i. That local governments are appropriately structured with adequate human resources and systems to carry out their core business;
- ii. That local governments have adequate recurrent financial resources to retain the capacity to deliver services; and
- iii. That local governments optimize the generation of own resources, rationalize and reassign sectoral responsibilities and resources, and conditionally fund capital requirements through predictable and transparent mechanisms.

25. Against the above background, three modalities of fiscal transfers to local authorities are currently being developed. These are:

- i. **Restructuring Grant.** This is meant to facilitate the restructuring of local authorities by clearing retrenchment/retirement costs and other debts.
- ii. **Recurrent Grant.** This grant is meant to support recurrent costs of running local governments in addition to own revenue sources such as property tax, personal levy and user charges and thereby address both vertical and horizontal imbalances. It is envisaged that the recurrent grant would replace the ad hoc general purpose grant currently being given to local government.
- iii. **Capital Grant.** This is meant to serve as a mode through which resources for development will be channelled to local authorities.

Social Sector Policies

26. During the period 2007-2009, the fiscal policy direction shall have greater attention to ensuring that the composition of public spending is not only growth -oriented but also pro-poor. One of the public spending priorities shall be social sector spending particularly on health, education, and water and sanitation.

27. The health sector continues to be faced with the problems related to inadequate drug supplies, poor infrastructure and equipment and declining number of frontline medical personnel. During the MTEF period, significant levels of resources will be directed towards addressing these problems especially provision of essential drugs and recruitment of frontline medical personnel.

28. Government will also make a deliberate attempt to build at least one first level district hospital in each of the remaining 19 districts which would operate as referral hospital to the satellite health centres. This is intended to improve accessibility to health centres in outlying areas, especially in the rural districts and also reduce congestion at the existing few first level referral hospitals.

29. In the education sector, the focus will be to continue with the recruitment and retention of teachers; provision of education materials; and improvement of infrastructure in the sector, including construction of classrooms and teachers' houses. These programmes will be undertaken with a view of expanding education in a manner that improves the overall education standards.

30. With regard to water and sanitation, Government will strive to improve access to safe drinking water and basic sanitation. Investments will therefore be scaled up in order to increase access to safe and adequate water in most of the peri-urban and rural areas. This will be done through capital investment programmes consisting of projects for construction of new facilities and rehabilitation of facilities to secure or safeguard existing coverage.

Public Order and Safety

31. The public order and safety sector has continued to be faced with constraints such as inadequate housing, poor conditions of service and working environment. In this regard it is Government's intention to provide more resources to the law enforcement wings in order to address these deficiencies. In particular more investments are being earmarked to provide infrastructure in the area of housing by rehabilitating existing infrastructure especially in the police camps and building new ones.

3.0 FISCAL FRAMEWORK 2007-2009

3.1 Objectives

32. In the medium term, the fiscal policy objectives will continue to focus on fostering macroeconomic stability, directing public resources to priority areas in line with the FNDP and enhance the capacity to generate domestic resources. In this regard, the overall deficit will be contained to around 2.3 percent of GDP while domestic borrowing will be constrained to 1.0 percent of GDP. The containment of domestic borrowing is partly aimed at curtailing the rise in the domestic debt thereby contributing to the reduction of inflation and interest rates.

33. In order to achieve the projected 2 percent overall deficit over the period, Government will continue exercising strong control on its expenditures by reducing non-priority expenditures while increasing poverty related expenditures. The resources from debt relief provided under the Multilateral Debt Relief Initiative (MDRI) as well as the HIPC Initiative will be directed, to priority areas such as agriculture, health, education and infrastructure in line with the FNDP.

Resource Mobilisation

34. In order to consolidate the fiscal objectives in the medium term, Government recognises the need to generate more revenues to finance its programmes. Although Zambia's tax effort has been favourable in the region, the share of revenue to GDP has declined from over 19 percent in the early 2000s' to about 16.3 percent by 2006. This decline has prompted Government to undertake reforms in both tax policy and administration. With regard to the tax policy reform, the objective will be to make the Zambian tax system, more robust, simpler and economically efficient, thereby contributing to buoyant revenue. The reform will also aim at improving the effectiveness of the tax system and eliminating tax inequalities that may distort resource allocation. In the area of tax administration, focus will be on enhancing efficiency. This will include client or taxpayer segmentation.

35. With regard to non-tax revenue, Government will undertake a comprehensive audit and strengthen all revenue points to enhance collections. This will include: providing adequate logistics for non-tax revenue collecting agencies; reviewing current legislation; and adjusting fees and fines to cost-effective and appropriate levels.

36. The collection of non-tax revenues is also expected to be enhanced as a result of the introduction of the IFMIS under the PEMFA reforms. The IFMIS will, among other things, allow for easier and automated tracking of revenue collections by government agencies.

37. As for external grants, it is expected that support from the co-operating partners during the period 2007-2009, will continue to increase due to Government's prudence in fiscal and financial management. Fundamentally, additional support is expected to enable the country accelerate progress towards meeting the Millennium Development Goals (MDGs).

3.2 Revenues and Grants

38. For the 2007-2009 MTEF period, Government projects to raise revenue and grants of resources of K9, 985.20 billion in 2007, K10,822.41 billion in 2008 and K11,704.44 billion in 2009. This translates to 22.62 percent of GDP in 2007, 22.41 percent of GDP in 2008 and 22.0 percent of GDP in 2009. (See Table 2.0 below)

Table 2.0: REVENUE AND GRANTS in K' MILLIONS, 2006 TO 2009

	2006	2007	2008	2009
TOTAL REVENUE AND GRANTS	8,225.90	9,985.20	10,822.41	11,704.44
Domestic Revenue	6,622.00	7,958.20	8,581.00	9,624.14
Tax revenue	6,381.90	7,693.00	8,306.40	9,322.00
Income taxes	2,953.00	3,547.00	3,718.70	4,173.20
Excise taxes	936.00	998.70	1,207.30	1,354.90
Value-added tax (VAT)	1,812.00	2,352.00	2,414.60	2,709.90
Domestic VAT	805.00	633.00	1,014.10	1,138.20
Import VAT	1,007.00	1,719.00	1,400.50	1,571.70
Customs duty	640.90	795.30	965.80	1,084.00
Non-tax revenue	240.10	265.20	274.60	302.14
Grants	1,603.90	2,027.00	2,241.40	2,080.29
Programme	310.00	518.20	662.70	577.79
Sector Wide Approaches (SWAPs)	283.63	319.90	398.37	401.94
Project Grants	1,010.27	1,188.90	1,180.34	1,100.56

Source: Ministry of Finance and National Planning

39. The revenue forecasts adopted for 2007-2009 are based on relatively conservative assumptions and takes into account projections of key macroeconomic variables and recent revenue trends.

Domestic Revenues

40. Domestic revenues include local taxes collected by the Zambia Revenue Authority (ZRA), non-tax revenue collected by mandated Government departments throughout the country, exceptional revenues such as dividends from State owned and quasi-government enterprises and other miscellaneous revenues. For the MTEF period, Government has projected to generate about K7,958.20 billion in 2007, K8,581.00 billion in 2008 and K9,624.14 billion in 2009 from local (domestic) sources. As a share of total revenue and grants this represents 79.7 percent in 2007, 79.3 percent in 2008 and 82.2 percent in 2009.

Tax Revenue

41. In the medium term, tax revenue as a proportion of GDP, is expected to increase from 16.24 percent in 2006 to 17.55 percent by 2009. Thus, Government projects to raise K7, 693.00 billion in 2007, K8,306.40 billion in 2008 and K9,322.0 billion in 2009.

Non-tax Revenue

42. Non-tax revenues are projected to increase from K265.20 billion in 2007 to K302.14 billion by 2009. With the re-introduction of Appropriation-in-Aid, revenue generating activities will receive adequate funding thereby easing operational problems of institutions mandated to collect these revenues.

External Grants

43. External grants include project and programme grants provided to Zambia by Cooperating Partners/Donors as development assistance (aid). Current commitments show that total aid inflows (excluding loans) will increase to US \$683 million in 2007 from US \$641.1 million in 2006. However, in 2008 they are projected to decline to US \$638 million and further to US \$588.5 million in 2009. (See table 3.0 below) In kwacha terms, this translates to K2,401.26 billion in 2007, K2,241.40 billion in 2008 and K2,080.29 billion in 2009.

44. The decline in external grants is mainly explained by the fact that a number of donors have not yet finalised their country assistance strategies for the period 2007-2010. It is most likely that actual support would be much higher than what is projected.

Table 3.0: External Grant Flows Projections, 2005-2009

	2005	2006	2007	2008	2009
	Actual	Proj	Proj	Proj	Proj
In US \$ Millions					
General Budget Support	131.1	93.3	153.9	160.2	137.0
MDRI Assistance		3.0	51.6	-	-
Sector Wide Approaches (Pool Funding)	91.3	88.0	95.2	96.3	95.3
O/w Education	55.3	54.9	58.1	56.6	55.6
Health	36.0	33.1	37.1	39.7	39.7
Project Assistance	272.2	358.4	302.5	285.2	260.9
Total	585.9	641.1	683	638	588.5
In % of GDP					
General Budget Support	1.8	0.8	1.7	1.4	1.1
MDRI Assistance	0.0	0.0	0.3	0.0	0.0
Sector Wide Approaches	1.2	0.8	0.9	0.8	0.8
O/w Education	0.8	0.5	0.5	0.5	0.4
Health	0.5	0.3	0.3	0.3	0.3
Project Assistance	3.7	3.2	2.8	2.2	1.8
Total	6.8	4.9	5.3	4.4	3.6

Source: Ministry of Finance and National Planning

3.3 Expenditures

45. Total expenditures (excluding amortisation) are projected to be at K11, 012.67 billion, K11,378.18 billion and K12, 088.10 billion in 2007, 2008 and 2009 respectively. As a percentage of GDP, the expenditures are estimated at 24.32 percent in 2007, 22.96 percent in 2008 and 22.76 percent in 2009. Recurrent expenditure is projected to stand at K8, 016.69 billion, K8, 466.33 billion, K9, 106.82 billion, while capital expenditure is projected at K2, 995.97 billion, K2, 911.84 billion and K2, 981.28 billion in 2007, 2008 and 2009 respectively.

3.3.1 Expenditure by Type

Personal Emoluments

46. Government's policy on personal emoluments for the civil service continues to be that of containing the wage bill within 8.0 percent of GDP. This is to enable Government direct more resources to other priority areas, especially those of a developmental nature. As such, the salaries and wages bill is projected to be at an average of 7.9 percent of GDP.

47. Notwithstanding the above, Government will continue with its effort to increase staffing levels in the education and health sectors. In this regard, net recruitment of the teachers and medical personnel has therefore been allocated K89 .0 billion, K120.0 billion and K132.0 billion in 2007, 2008 and 2009 respectively. From these allocations approximately 15,000 teachers and 5,715 medical personnel will be recruited over the medium term.

48. Government has also set aside K246.62 billion in 2007, K169.06 billion in 2008 and K178.0 billion in 2009 for the Medium Term Pay Reforms. In addition, Government will continue to implement the on-going restructuring programme in line with the Public Sector Reform Programme (PSRP). In this regard, allocations amounting to K102.03 billion, K85.6 billion and K91.9 billion have been set aside for the years 2007, 2008 and 2009 respectively.

Expenditure on Goods and Services (Recurrent Departmental Charges (RDCs))

49. In the medium term, spending on goods and services to sustain Government operations is expected to decline as percentage of GDP. General spending on goods and services in the medium term is estimated at 3.94 percent of GDP in 2007, 3.71 percent of GDP in 2008 and 3.70 percent of GDP in 2009. This is in line with Government's policy to reduce consumption spending while increasing expenditure on developmental programmes.

50. Government is concerned with the current level of outstanding bills owed to road contractors, food suppliers and other suppliers of goods and services. In an effort to dismantle these outstanding bills, provisions amounting to K114.83 billion, K95.5 billion and K105.0 billion in 2007, 2008 and 2009 respectively, have been made.

51. Government is also expected to continue with the constitutional review process which will include undertaking a census as a pre-requisite for administering a national referendum in accordance with Article 79 of the Constitution. Government has, therefore, made allocations of K182.51 billion, K186.5 billion and K20.9 billion in 2007, 2008 and 2009 respectively.

52. For Awards and Compensations for court cases decided against Government, provisions made over the three year period are K80.0 billion, K78 billion and K70 billion in 2007, 2008 and 2009 respectively.

Grants and Other Payments

53. Government proposes to spend a total of K1, 587.15 billion in 2007, K1, 693.87 billion in 2008 and K2, 001.93 billion in 2009 on Grants and Other Payments. As share of GDP, these are projected at 3.50 percent, 3.42 percent and 3.77 percent in 2007, 2008 and 2009 respectively. The major components in this category of expenditure are sector-wide Approaches (SWAPs) and transfers to institutions such as Zambia Revenue Authority (ZRA) and local governments.

54. With regard to SWAPs, support from cooperating partners to sectors of education and health are projected to be K319.90 billion, K398.37 billion and K401.94 billion in 2007, 2008 and 2009 respectively. This is meant to support the basic health care and basic education programmes, particularly for the purchase of essential drugs under health and school requisites under education.

55. As for transfers to local governments, provisions have been made to aid the decentralisation process. As a first step to the process, Government has provided a recurrent grant amounting to K50.1 billion per year for the 54 district councils. This is in addition to the K25 billion, restructuring grant that Government is currently providing. In addition, Government has provided an average of K17.7 billion for grants in lieu of rates for all councils and K2.3 billion per year to support the fiscal decentralisation and devolution processes.

56. With regard to pensions, Government proposes to transfer K266.0 billion, K279.69 billion and K389.54 billion in 2007, 2008 and 2009 respectively to the Pension fund to cater for the grant and liquidation of arrears that Government owes the institution. The grant is meant to pay civil servants retired in national interest, early retirements and the deceased estates.

57. The allocations to the Zambia Revenue Authority, in the medium term, are proposed at K135 billion, K141.6 billion and K148.70 billion in 2007, 2008 and 2009 respectively to support the operations of the institution.

Constitutional and Statutory Expenditure

58. Constitutional and Statutory Expenditure largely made up of domestic and external debt payments as a share of GDP, is projected to decline, over the medium term period from 1.18 percent in 2007 to 1.03 percent by 2009. This is mainly due to the attainment of the HIPC Completion Point and the Multilateral Debt Relief Initiative (MDRI) which has resulted in a large portion of the external debt being cancelled by bilateral and multilateral cooperating partners. As such, external debt interest payments, as a percentage of GDP, are expected to decline from 0.15 percent in 2007 to 0.07 percent by 2009.

59. Similarly, domestic debt interest payments are also expected to decline over the medium term reflecting Government's continued policy of reduced domestic borrowing. Government proposes to spend K491.2 billion (1.08 percent of GDP) in 2007, K463.0 billion (0.93 percent of GDP) in 2008 and K480.5 billion (0.90 percent of GDP) in 2009.

Other Current Expenditures

60. Government intends to continue implementing the Fertilizer Support and Food Strategic Reserve programmes but only up to 2008. This is in line with the initial plans to run these programmes for a limited period of time.

61. The Fertilizer Support Programme has, therefore, been allocated amounts of K150.0 billion each in 2007 and 2008. The Food Strategic Reserve is expected to be self sustaining and as such allocations of K50.0 billion and K30 billion have been provided in 2007 and 2008, respectively.

62. In order to restructure the remaining Parastatals and meet contingent liabilities, Government has provided K180.15 billion in 2007, 178.65 billion in 2008 and K158.72 billion in 2009.

Capital Expenditure

63. Capital expenditures are projected to increase from 4.80 percent in 2006 to 6.62 percent of GDP by 2007. Foreign financed capital expenditures are projected to average 3.15 percent over the medium term while domestically financed and direct budget supported capital expenditures are projected to average 2.88 percent of GDP.

64. Foreign financed capital expenditures are projected at K1, 679.80 billion, K1, 622.34 billion and K1, 322.65 billion in 2007, 2008 and 2009 respectively. Domestically financed capital expenditures are projected to be at K1, 316.17 billion, K1,289.50 billion and K1,658.63 billion in 2007, 2008 and 2009 respectively. From these allocations, some of the programmes that Government proposes to undertake are tabulated in the table below:

Table 4.0: Some Proposed Capital Expenditure in K' Billions, 2007-2009

	2007	2008	2009
National Stadium	30.00	73.00	90.00
GRZ Road Projects	489.23	571.93	700.53
o/w Road Projects funded from fuel levy	220.75	245.03	257.28
Rural Electrification	13.21	14.66	15.39
Youth Empowerment	30.00	30.00	30.00
Ordinary Capital	554.99	599.91	822.71

Source: Ministry of Finance and National Planning

Multilateral Debt Relief Initiative (MDRI) Poverty-Related Expenditures

65. Zambia's external debt has significantly reduced from over 7.0 billion US Dollars as at 31st December 2003 to less than a billion US dollars as at 31st October 2006 due to the attainment of the HIPC completion point and consequently qualifying for debt relief under the MDRI. Most multilateral cooperating partners such as the IMF and the World Bank have cancelled 100 percent of Zambia's debt. From savings arising from debt cancellation, Government intends to scale up expenditure on poverty reducing programmes such as agriculture (irrigation and animal health), water and sanitation, skills training and infrastructure (roads). As such, Government intends to spend a total of K198.74 billion from the MDRI savings in 2007.

Financing Requirement (Overall Balance)

66. From the revenues and expenditures discussed Government projects to incur budget deficit (when revenues are less than expenditures) of 2.27 percent in 2007 and is expected to narrow down to 0.72 by 2009. These deficits will be financed from domestic and external borrowing. The level of financing (including MDRI) is projected to stand at K1,027.47 billion, K555.77 billion and K383.67 billion in 2007, 2008 and 2009 respectively.

Domestic Financing

67. In line with Government policy to contain inflation and reduce interest rates, domestic financing (including MDRI) during the period 2007-2009 will be limited to 1.44 percent of GDP in 2007 and maintained at 0.5 percent in 2008 and 2009 respectively.

Net External Financing

68. Net external financing is projected at K375.90 billion (0.85 percent of GDP), K308.00 billion (0.62 percent of GDP) and a repayment of K118.09 billion (0.22 percent of GDP) in 2007, 2008 and 2009 respectively.

3.3.2 Expenditure by Function

69. Expenditure by function indicates central government expenditures in line with Government's development objectives. These objectives are embedded in the following functional classification: General Public Services; Defence; Public Order and Safety; Economic Affairs; Housing and Community Amenities; Environmental Protection; Education; Health; Recreation, Religion and Culture; and Social Protection.

70. The allocation of resources by expenditure functions has been done in line with the strategic focus of the FNDP which is to increase budgetary outlays to health, education and economic sectors. On this basis, the proposed spending on economic and social sectors is progressively increasing in the medium term as a share of total expenditure. Thus, expenditure on economic sectors is projected to increase to 18.16 percent in 2007, 18.77 percent in 2008, and 19.14 percent in 2009. Similarly, spending on social sectors is projected to increase to 33.44 percent, 34.77 percent and 35.55 percent of total expenditure in 2007, 2008 and 2009 respectively (See table 5.0 and table 6.0 below).

Table 5.0: Expenditure by Function of Government, 2006-2009

	2006	2007	2008	2009
	K'million	K'million	K'million	K'million
Budget	10,236.80	11,012.67	11,378.18	12,088.10
General Public Services	4,188.90	4,100.02	3,923.20	3,963.69
Defence	654.9	794.01	894.32	998.48
Public Order and Safety	391.7	433.90	465.37	505.28
Economic Affairs	1,844.80	1,999.90	2,135.68	2,313.66
Environmental Protection	43.3	37.44	47.79	58.02
Housing and Community Amenities	292	309.46	344.76	381.98
Health	1,098.40	1,398.61	1,484.85	1,602.88
Recreation, Culture and Religion	29.7	22.03	33.00	44.73
Education	1,647.40	1,857.84	1,974.11	2,137.18
Social Protection	45.7	59.47	75.10	82.20

Source: Ministry of Finance and National Planning

Table 6.0: Expenditure by Function in Percent of Total Budget, 2006-2009

Functions	2006	2007	2008	2009
General Public Services	40.68	37.23	34.48	32.79
Defence	6.43	7.21	7.86	8.26
Public Order and Safety	3.85	3.94	4.09	4.18
Economic Affairs	18.12	18.16	18.77	19.14
Environmental Protection	0.43	0.34	0.42	0.48
Housing and Community Amenities	2.87	2.81	3.03	3.16
Health	10.71	12.70	13.05	13.26
Recreation, Culture and Religion	0.29	0.20	0.29	0.37
Education	16.18	16.87	17.35	17.68
Social Protection	0.45	0.54	0.66	0.68

Source: Ministry of Finance and National Planning

General Public Services

71. In 2007 Government proposes to spend approximately 37 percent of the projected total expenditure on General Public Services. This function encompasses several items that require substantial public financing such as:

- (a) Debt (both domestic and foreign) and Investment Management
- (b) Transfers to local authorities and other quasi government institutions such as ZRA
- (c) Administration and operation of/or support to the executive and legislative arms of government

72. However, the proportion is anticipated to decline in the outer years. See Table 6.0 above. The reduction is due to the projected fall in the domestic and external debt payments and the reduction in Government administrative costs.

Defence

73. Expenditure on this function is expected to increase from 6.43 percent of the budget in 2006 to an average of 7.79 percent over the medium term. Within this category, a deliberate effort has been made to provide resources for the construction and rehabilitation of infrastructure especially housing. In this regard, an allocation of K60.0 billion has been earmarked for this purpose over the three year period.

Public Order and Safety

74. Public order and Safety function includes administration of police affairs and services and fire protection services, administration and operation of courts of law and prisons. The focus over the medium term will be on improving infrastructure in police camps and construction of new ones. It is in this vein that K58.1 billion has been set aside for the same over the MTEF period.

Economic Affairs

75. In line with proposed expenditure priorities outlined in the FNDP, it is envisaged that expenditure will be biased towards re-investment in agriculture, fisheries, and livestock. Government will also strengthen other relevant economic and social infrastructure such as roads. In this regard, Government proposes to spend 18.16 percent, 18.77 percent and 19.14 percent of the total central government budget in 2007, 2008 and 2009 respectively. Some of the key programmes that Government intends to channel resources to are shown in the Table below:-

Table 7.0: Proposed allocations for Selected Programmes in the Agriculture Sector in K ‘Billions, 2007-2009

	2007	2008	2009
Agriculture and Infrastructure and Development	20.00	20.8	80.80
Livestock Development	47.50	35.70	143.30
Agriculture Services and Technological Development	40.00	23.80	81.40
Fisheries Development	26.70	24.40	31.60
Irrigation Development	22.00	34.90	86.90

Source: Ministry of Finance and National Planning

Environmental Protection

76. Expenditure in this function will focus on problems of natural resource management especially in “open areas” (land under traditional laws) where there are often ill-defined property rights. The major issues will involve the strengthening of current instruments for policy implementation such as licensing and the provision of a broad legal framework for the sector. To this effect, Government proposes to spend 0.34 percent, 0.42 percent and 0.48 percent out of total expenditure in 2007, 2008 and 2009 respectively.

Housing and Community Amenities

77. This function will absorb 2.81 percent of total expenditure in 2007 with the percentage increasing to 3.03 percent in 2008 and 3.16 percent in 2009. Of the total allocation on this function, Government intends to spend 65 percent on water supply and sanitation. Government's focus is on the peri-urban and rural water supply.

Recreation, Culture and Religion

78. Government spending in relation to this function is on recreation and sporting services, promotion and preservation of culture and religious affairs. It is anticipated that this function will absorb 0.20 percent, 0.29 percent and 0.37 percent of total expenditure in 2007, 2008 and 2009 respectively.

Health

79. The health sector is one of the priority sectors and as such, Government proposes to spend 12.70 percent of total expenditure on this function in 2007. This allocation will cater for the recruitment of front line health personnel and the related costs associated with providing improved health care service. Government intends to spend 13.05 percent of total expenditure in 2008 and 13.26 percent in 2009.

Education

80. Government proposes to spend approximately 16.87 percent of total expenditure in 2007 on this function. Outlays on education include expenditure on services provided to individual pupils and students. The primary objective is the enhancement of education at all levels (i.e. primary, secondary and tertiary). In this regard, Government proposes to spend an additional K84 billion on infrastructure development and K74 billion on curriculum development. In 2008, 17.35 percent of total expenditure will be directed towards education and this will increase to 17.68 percent in 2009.

Social Protection

81. Outlays on social protection include social security welfare and other related social programmes. It is anticipated that Government will spend 0.54 percent of total expenditure on this function in 2007. Over the medium term, Government intends to spend 0.66 percent of total expenditures in 2008 and 0.68 percent in 2009 towards this function.

4.0 SUMMARY OF THE CENTRAL GOVERNMENT BUDGET 2007-2009

82. In summary, the central government budget for 2007-2009 is projected to be as follows:

- Total revenues and grants in 2007 are projected to amount to K9, 985.20 billion, K10, 822.41 billion in 2008 and K11, 704.44 billion in 2009. As a share of GDP, revenues and grants are projected at 22.05 percent, 21.84 percent and 22.04 percent in 2007, 2008 and 2009 respectively;

- Total central government expenditures (excluding amortization) in 2007 is expected to amount to K11,012.26 billion in 2007, K11,378.18 billion in 2008 and K12,088.10 billion in 2009. As a share of GDP expenditures are projected at 24.32 percent, 22.96 percent and 22.76 percent in 2007, 2008 and 2009 respectively;
- From the projected total revenues and grants and proposed expenditures for the period 2007-2009 the overall deficit is projected to stand at K1,027.47 billion, K555.77 billion and K383.676 billion in 2007, 2008 and 2009 respectively. This deficit will be financed as follows:
 - i. Domestic financing (including MDRI) is projected at K651.57 billion, K 247.78 billion, and K 265.58 billion or 1.44 percent, 0.5 percent and 0.5 percent of GDP in 2007, 2008 and 2009 respectively.
 - ii. Net External financing is projected to stand at K375.90 billion, K308.00 billion and minus K118.09 billion or 0.83 percent, 0.62 percent and minus 0.22 percent of GDP in 2007, 2008 and 2009 respectively.

5.0 CONCLUSION

83. The proposed macroeconomic framework and fiscal framework discussed in this paper set a solid platform for consultations on the resource allocation over the medium term. Government is committed to strengthening the linkage between agreed priorities and the expenditure plan in order to improve service delivery and ultimately the quality of life of the Zambian people. In that regard, a deliberate attempt has been made to realign expenditures to accommodate the core FNDP programmes and as such MPSAs, in preparing their estimates for 2007 – 2009, should take this into account.

84. Further, this document is one of the first steps used to kick start the 2007 budgeting process. Therefore, this Green Paper gives an opportunity for all stakeholders to comment and submit their recommendations to the Ministry of Finance and National Planning for consideration and possible inclusion in the 2007 budget.

APPENDICES

1. 2007 – 2009 Draft Fiscal Framework.
 2. 2006 Domestic Budget and Aggregated 2007 - 2009 Indicative Expenditure Allocations:
 - (i) Personal Emoluments and Other Related Expenses
 - (ii) Non-Personal Emoluments (Programme Ceilings)
 - (iii) Constitutional and Statutory Expenditure
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