

The Loan Contraction Process in Africa

Making loans work for the poor



The Case of Zambia



**AFRODAD AND
CHRISTIAN AID**

**MAKING LOANS WORK FOR
THE POOR IN ZAMBIA**

STUDY REPORT

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LIST OF ACRONYMS

AfDB	African Development Bank
AIDS	Acquired Immune Deficiency Syndrome
CSO	Civil Society Organisation
EDT	Total Debt Stock
ESSD	Environmentally and Socially Sustainable Development
EU	European Union
FDI	Foreign Direct Investment
GNI	Gross National Income
GRZ	Government of the Republic of Zambia
IFI	International Financial Institution
IMF	International Monetary Fund
IDA	International Development Association
MDG	Millennium Development Goal
MGS	Import of Goods and Services
MMD	Movement for Multiparty Democracy
MoFNP	Ministry of Finance and National Planning
PSI	Private Sector Infrastructure
TDS	Total Debt Service Paid
UN	United Nations
UNDP	United Nations Development Programme
UNIP	United National Independence Party
WB	World Bank
XGS	Exports of Goods and Services

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Introduction

The causes of Africa's debt crisis are varied and complex. A lot of emphasis has been put on external factors to the negation or belittling of internal factors. Notwithstanding the external factors, it is clear that the causes of the debt crisis in many African countries are also attributable to poor borrowing, debt policy and debt management factors. This problem is also a symptom of poor governance in which the underlying premises should be consensus oriented approval mechanisms, equity and inclusiveness in the use of scarce financial resources, effectiveness and efficiency in the use of financial resources, and accountability.

The burden of external debt on Zambia is extremely high. The amount borrowed (the principal), and the interest on debt to be repaid is a significant barrier to economic growth and development. When compared with the level of exports the true impact of the debt becomes more apparent. Zambia has borrowed money from a number of different sources. The bulk of debt is mainly made up from middle and long-term debt. Less than 5% of the total debt is short-term debt having a maturation date of less than one year. Unfortunately Zambia cannot pay these in its own currency, the kwacha. Foreign creditors require payment in their own currency or in a convertible hard currency. Hence, using foreign exchange must pay both of these off.

It is in the light of the foregoing that AFRODAD plans commissioned studies in five selected African countries, including Zambia to critically analyse the role of internal factors in Africa's debt crisis. These studies seek to shed light on the link and contribution of debt management mechanisms to the mounting external debt. AFRODAD believes that if appropriate external borrowing strategies and good internal management of external loan resources were put in place, Africa's external debt would become sustainable. Key to this is the putting up of administrative, institutional and legal reforms to ensure proper management of external loans and project design, implementation and evaluation.

1.2 Objectives of the Study

The overall objective of this study is to ensure that the loans taken by the poor countries are legitimate and serve the basic functions of poverty reduction and development. By this objective the study intends to realign the support rendered by international financial institutions to poor countries with the basic needs of those countries.

The specific objectives as well as the terms of reference for this study are to:

- Summarise the external loan agreements still being serviced by the government or recently contracted by the government, noting any relationship between loans and grants, the existing and estimated future level of debt service as percentage of total expenditure, and the sectoral allocation of loan resources. Outline the legal framework regulating the government's lending practices;
- Discuss the adequacy of existing regulatory frameworks for debt management;
- Examine the role of the IMF and World Bank, and other major creditors/lenders' in the loan contraction process;
- Examine the role of civil society in the loan contraction and monitoring process;
- Give an example and assessment of a specific loan process in the country being studied;
- Use the human rights based approach to assess the performance of government in its responsibilities as a duty bearer to its citizens with particular regard to the attainment of the MDGs in the country; and

7 Draw a conclusion and make recommendations.

1.3. Rationale for the Study

The study is premised on the understanding that the procurement, utilisation and management of public loans and debts are a national and global issue and, therefore, should be seen to be transparent, accountable, participatory and inclusive. The processes of loan procurement and debt management require legitimacy and systematic planning to be sustainable. By making loans sustainable, governments will have extra revenue to support their social services and goods for development and enhance their people's welfare and reduce poverty. This study constructs a framework for rationalisation of the loan contraction and debt management process in these terms.

1.4 Study Methodology

This study employed two types of research tool. The first and most extensively used is literature review. This consisted of a detailed examination of documents from the IFIs, Jubilee-Zambia, AFRODAD and GRZ, the Bank of Zambia and other sources. The second method consisted of interviews with key informants and other stakeholders. The main informants and stakeholders interviewed were staff from Jubilee-Zambia and the University of Zambia.

1.5 Study Limitations

In reading and interpreting this report, it is imperative to bear in mind certain limitations. The main ones were:

- Obtaining debt statistics from the government is a daunting task at the best of times. The situation in Zambia has been made particularly difficult by the governments 'failure' to reach the HIPC completion point by December 2003. Officials at the Ministry of Finance and cooperating partners are in defensive mood and not willing to even talk about the debt. Data from the 2004 budget was unavailable as controversy over the document persisted.
- The civil society organisations in Zambia all discuss the debt problem through Jubilee-Zambia. It was thus difficult to get different opinions on the debt as the respondents quickly referred the researcher to Jubilee-Zambia when questions of debt were posed.
- The World Bank referred all queries to the Ministry of Finance. Issues regarding the Bank's policies and practice are thus inadequately addressed.

2 Economic Background to the Debt Situation in Zambia

At independence in 1964, Zambia was one of the most prosperous nations in Africa. With a rich endowment of arable land, water and mineral resources, it held great potential for sustainable economic development.¹ Having inherited very poor or inadequate infrastructure, including human capital from the colonial regime, The new government of the United National Independence Party (UNIP) set about building schools, a university, roads and hospitals. The inherited copper sales revenue was utilised for this purpose.

A booming copper industry, Zambia's economic mainstay, and the prevailing socialist orientation of the day encouraged state interventionist policies. In the first ten years after independence, the nation experienced growth averaging 2.4 percent a year, significantly lower than population growth, thereby leading to declining per capita incomes.

Starting in 1975, Zambia faced falling copper prices. Government and multilateral donor agencies initially thought this development was a temporary phenomenon but political turmoil in neighbouring countries and the severe effects of the first oil shock added to the economic problems the country faced. Still anticipating a rise in copper prices, the government borrowed heavily to sustain the economy. By the early 1980s, however, it was becoming clear that the Mulungushi economic reforms had failed.

In the period between 1983 and 1985 the government attempted an IMF/World Bank Structural Adjustment Programme (SAP) that had stringent conditions attached. This was abandoned in May 1987, after massive food riots on the Copperbelt. The SAP was replaced by another, local programme that re-imposed the controls of the 1970s. The economy, however, continued to decline; poverty levels were rose and debt had swelled to US\$ 7.1 billion by 1991.

In October 1991 the people of Zambia, discontented with the performance of the reforms thus far, elected the Movement for Multi-party Democracy (MMD) government. The new government introduced and pushed neoliberal economic policies supported by the IMF, World Bank and other donor agencies. At the heart of the reforms was the anticipation that the private sector would be a more efficient engine for economic growth. The state's role remained the creation of an enabling environment for private business.

In December 2000, Zambia qualified for the Heavily Indebted Poor Countries (HIPC) Initiative. In December 2003, Zambia was supposed to reach the HIPC completion point but, due to commitments the government had made to the civil service trade unions, especially over improved housing allowances, the government overspent its budget and failed to reach the completion point.

In the 2004 budget, provision has been made to resolve the problem by putting a wage freeze on civil service salaries and increasing taxes for high income groups. As can be expected, the labour movement is up in arms and fighting for the rewriting of the 2004 budget so as to remove the wage freeze and to reduce tax.

2.1 Zambia's External Debt Stock

There are differing figures for Zambia's debt stock. This is due to a number of factors, such as reliability of data sources, definitions and data management problems.² Under the circumstances, it is advisable to use the official Zambian Government statistics.

Table 1, below, shows the different types of external debt. The table reveals that private debt as a percentage of total debt increased steadily from 1999 to 2001. The table also shows multilateral debt in the years 1999 to 2001.

Table 1 Zambia's External Debt Stock (US \$ Million)

	1999	2000	2001	% Change 2000/ 2001	
Bilateral	2 676.40	2 390.20	3 091.76	26.4	
Paris Club	2 405.00	2 131.40	2 713.85	27.3	
Non Paris Club	271.40	258.80	377.9	46.0	
Multilateral	3 375.10	3 446.82	3 346.04	-2.9	
AfDB/ADF	370.70	316.66	318.66	0.6	
World Bank	1 668.30	1 736.43	1 837.06	5.8	
IMF	1 219.20	1 245.40	992	-20.3	
Others	166.90	148.33	198.32	33.7	
Total Govt. Debt	6 051.50	5 837.02	6 437.8	9.5	
Private debt	455.90	473.49	832.3	75.8	
Total Debt	6 507.40	6 310.51	7 270.06	Average	15.2

Source: Adapted from Jubilee-Zambia/Debt Project/Mphuka C. (2002). HIPC Study: The Case for Zambia page 4.

2.1.1 The structure of bilateral external debt

As indicated in Table 2, below, Zambia owes both Paris Club and Non Paris Club bilateral creditors. The four largest bilateral creditors as at the end of December 2001 were Japan (US\$ 705.8 million), Russia (US\$ 545.7 million), Germany (US\$ 438.2 million) and the United Kingdom (US\$ 359.9 million). These four accounted for 77.2 percent of Paris Club debt and 28.9 percent of total external debt. Apart from these four and the USA, France and Italy, there are also key Paris Club creditors with debt owed to each of them coming over US\$ 100 million.

Table 2 Zambia's Bilateral Debt Creditors (US\$ million)

PARIS CLUB CREDITORS			NON PARIS CLUB CREDITORS		
Country	Amount	% of total	Country	Amount	% of total
Japan	705.8	26.0	China	132.4	35.0
Russia	545.7	20.1	Kuwait	119.7	31.7
Germany	483.2	17.8	Iraq	62.8	16.6
UK	359.9	13.3	Yugoslavia	26.8	7.1
USA	274.3	10.1	Romania	16.4	4.3
France	110.3	4.1	India	14.9	3.9
Italy	104.9	3.9	Bulgaria	5.0	1.3
Brazil	70.5	2.6			
Canada	49.5	1.8			
Austria	9.8	0.4			
Total	2 713.9	100.0		377.9	100.0

Source: Adapted from Jubilee-Zambia/Debt Project/Mphuka C. (2002). HIPC Study: page 5.

Where as most of Zambia's bilateral debt is owed to Paris Club countries, debt owed to Non Paris Club is also significant. Total Non Paris club debt stood at US\$ 378 million in 2001. As a percentage of total bilateral debt, Non Paris Club debt has been falling steadily since 1997. China and Kuwait are among the key Non Paris Club creditors with amounts owed in excess of US\$ 100 million.

2.2 Debt Indicators

Internationally, a number of debt indicators are used to assess the level of indebtedness of a given country. Table 3, below, shows a number of indicators ranging from total debt stock/total export earnings, total debt stock/gross national income and many others. For Zambia, the indicators show an alarming level of indebtedness.

Table 3 Selected Debt Indicators for 1970 to 2001

	1970	1980	1990	1995	1996	1997	1998	1999	2000	2001
EDT/XGS (%)	508.0	199.7	507.8	482.2	576.3	513.4	713.4	636.0	624.6	512.9
EDT/GNI (%)	46.7	90.3	229.9	215.8	230.6	179.9	227.6	197.2	185.2	162.0
TDS/XGS (%)	-	25.2	14.9	180.9	20.4	18.9	21.0	16.1	20.2	11.7
INT/XGS (%)	-	8.7	5.6	37.8	7.7	6.3	7.2	9.8	9.6	4.4
INT/XGS (%)	1.8	3.9	2.5	16.9	3.1	2.2	2.3	3.0	2.8	1.4
RES/EDT (%)	62.4	2.4	2.8	3.2	3.2	3.6	1.0	0.8	4.3	3.2
RES/MGS (months)	-	0.5	1.0	1.4	1.6	1.8	0.6	0.4	2.0	1.2
Short term/EDT (%)	19.7	18.1	20.4	6.0	6.8	3.9	4.8	1.9	1.4	3.1
Concessional/EDT (%)	6.3	24.6	29.9	37.3	49.5	52.3	53.0	60.2	62.4	62.7
Multilateral/EDT (%)	7.6	12.1	20.2	30.5	30.7	32.5	32.6	39.7	42.0	42.9

Source: World Bank (2003). Global Financial Development, page 584.

Table 4 Terms and Conditions for Selected World Bank Loans to Zambia (US\$ million)

Country/Project Name	Network	Approval Date	Mature	Principal Amount	
				SDR	US\$
IDA Second Economic Recovery and Investment Promotion Technical Assistance Supplements. Credit will support the government in completing the restructuring of Konkola Copper Mines and will provide technical assistance, equipment, and training for the privatisation programme. Total cost: US \$10m	PSI	17/6/03	2013/2043	7.3	10.0
IDA Copperbelt Environment Specific Investment Credit/Grant aims to address environmental liabilities associated with the mining sector following its privatisation by financing priority environmental measures and strengthening existing regulatory institutions. Total cost: US \$41.8m	ESSD	20/3/03	2013/2043	14.1c	19.0
IDA Zambia National Response to HIV/AIDS (ZANARA) Adaptable Programme Grant will target high risk groups, aiming to significantly increase access to and use of HIV/AIDS prevention, care and impact mitigation programmes through education and community initiatives. Total cost: US \$46m	HDN	30/12/02	n.a	33.7	42.0

Country/Project Name	Network	Approval Date	Mature	Principal Amount	
				SDR	US\$
IDA Emergency Drought Recovery Credit/Grant will respond to the recent drought crisis by providing support to prevent starvation and malnutrition; providing water, transportation, health and sanitation services, and logistics to keep children in school; and to support threatened livestock. Total cost: US\$ 50m	ESSD	19/11/02	2013/2042	22.8c	30.0
IDA Economic Recovery and Investment Promotion Technical Assistance Supplemental Credit, by providing advisory services, will assist the government in completing the privatisation of the main utilities and parastatals in the power, energy, and telecommunications sectors. Total cost: US\$7.5m	PSI	19/9/02	2012/2042	5.6	7.5

Source: World Bank (2003) Annual Report page 149.

2.3 Terms and Conditions of Selected Loans

It is difficult to obtain conditions on all loans in Zambia. In an effort to show the nature, conditions and purposes of loans, we show below a list of loans from the World Bank for the year 2003. Table 4 shows that the loans approved were for the private sector, environment and HIV/AIDS and human development. The maturities range from ten to twenty years.

2.4 Contractual Obligations on Long Term Debt

Table 5, below, shows Zambia's long-term debt obligations. These projections are for the period 2004 to 2011. It is evident that the long-term obligations on disbursements and interest are falling over time while the principal obligations are rising. It is crucial to note that these projections by the World Bank are based on Zambia reaching the HIPC completion point by December 2003. To the extent that this has not materialised, Zambia's debt obligations are less favourable than the table indicates.

Table 5 Contractual Obligations on Zambia's Long Term Debt

	2004	2005	2006	2007	2008	2009	2010	2011
Disbursements	75	61	44	30	18	9	4	1
Principal	169	143	134	138	134	141	144	148
Interest	104	98	93	89	85	81	77	72

Source: World Bank (2003): Global Development Finance, page 587.

2.5 Domestic Debt

Many analysts feel that the state of domestic debt is a source of worry. 3 The structure of domestic debt is such that the bulk of the debt is owed to the Central Bank. Table 6, below, shows the structure of Zambia's domestic debt in 2000 and 2001. The table shows that the Bank of Zambia is the largest domestic creditor to government followed by the public debt which is in the form of treasury bills and government bonds. What worries observers is that some of the domestic debt is meant to pay off external debt. In addition to this, it is a stated fact that government borrowing crowds out the private sector and hence slows down the pace of economic development.

Table 6 Structure of Domestic Debt (K' billions*)

	Year and Percent of Total				Percentage Increase
	2000	%	2001	%	
Bank of Zambia	1 657.4	49.9	2 177.8	55.3	31.4
Financial Sector	264.3	8.0	239.2	6.1	-0.1
Transport and Communication	43.2	1.3	46.8	1.2	0.1
General Public	1 437.9	43.3	1 598.5	40.6	0.1
Total	3 319.9		3 941.4		18.7

* One US \$ is equivalent to 5 000 Zambian Kwacha

Source: Jubilee- Zambia/ Mphuka C. HIPC Study page 6.

3 The Legal loan contraction process⁴

3.1 The Current Legal Framework

In this section of the report, we examine the legal framework governing public external debt. We begin by setting out what may be termed the ideal loan process. This will provide a basic standard against which the process in Zambia can be measured. It can be stressed from the outset that the United Nations Institute for Training and Research (UNITAR) framework is used as the basis.

There are a number of laws that work together to authorise and regulate public external borrowing. The legal framework changed substantially in 1969 from what it had been at Independence. It is significant that the current law was enacted at around the time when a referendum was held to usher in the one party state. The political domination of the then ruling party, UNIP, and its government was clearly intended to extend to public borrowing. Law reforms had the effect of ending parliamentary control over the borrowing process and legalising undemocratic contraction and management of loans.

Under the current legal framework, the most important piece of legislation is the Loans and Guarantees (Authorisation) Act, Cap 366 of the Laws of Zambia. This Act is primarily intended to give blanket authority to the Government to borrow. Once this authority is given, the loan contraction process tends to follow international principles and rules.

There are a number of Acts that authorise the application of international law in Zambia. These are the:

- International Development Association, Cap. 361;
- Bretton Woods Agreements Act, Cap. 367; and
- International Finance Corporation, Cap. 368.

These Acts enable Zambia to be a member of, and therefore eligible to borrow from, the respective institutions.

The key provisions of the Loans and Guarantees (Authorisation) Act are as follows:

- Loans may be raised through the issue of bonds and stock, issue of treasury bills and by agreement in writing. The Minister of Finance determines the terms and conditions applicable. It is important to note that this expectation is unrealistic in view of the fact that the Minister is expected to negotiate terms that are favourable to Zambia in circumstances where the lenders clearly have the upper hand.
- Section 3 of the Act gives the Minister of Finance a general power to borrow both within and outside Zambia, as she or he may deem desirable. This gives the Minister too much discretion to commit the country to debt. The ceiling on borrowing is contained in a statutory instrument authorised by resolution of the National Assembly. (Under Article 80 of the Constitution, a statutory instrument is to be published in the Gazette within 28 days after it is approved by Parliament). When the National Assembly is not sitting, the Minister is authorised in the public interest and with the approval of the President, under section 26, to vary the ceiling on borrowing to the extent necessary to raise an urgent loan or guarantee. This creates a loophole. Under the current law, external loans are not subjected to the scrutiny of Parliament before they are obtained nor is the Auditor General supplied with all loan documentation. The present borrowing ceiling was set under Cap 366, by Statutory Instrument No. 53 of 1998, at a maximum of K20 trillion. This is the maximum allowed to be outstanding at any one time on loans raised from outside the Republic. In addition, the Government can guarantee up to two hundred thousand, million, Kwacha. It is not clear whether these figures were determined on the basis of the country's ability to absorb and service such debt or simply to accommodate the existing debt obligations and their multiplication due to a failure to

pay back or service them adequately. There is some concern that if twenty trillion Kwacha amounted to US\$ 4 billion at the 1998 exchange rate, and the actual outstanding debt at the time was US\$ 7 billion, then the ceiling is not properly defined and realistic.

- Loans for a period of not more than one year are payable into a special depository account but those for more than a year are payable into the general revenues of the Republic. These loans then become difficult to monitor. It is desirable that loans raised for a specific purpose be applied only to that purpose.
- All debt charges are paid out of the general revenues of the Republic and details are included in the financial report to Parliament. We need to take note that this report thus comes after the fact and serves little useful purpose.
- Although a sinking fund maybe established in the public interest where a loan is obtained through the issue of bonds or stock, it is mandatory to establish a sinking fund for the redemption of not less than 75 percent of the loan only where bonds and stock issued in respect thereof exceed ten years. Currently, sinking funds are not used in practice.⁵
- Under the Loans (Stock, Bonds and Treasury Bills) Regulations appended to the Act, in the case of any loan raised by the issue of stock and bonds the Bank of Zambia shall keep a register of each issue of stock and bonds. The holders of the stock and bonds are also registered. Questions arise as to whether this has been done consistently.
- Under Parts V and VI of the Act, the Minister can guarantee or grant loans to persons and on such conditions as stated under the same provisions of the Act. For instance, upon the issue of a warrant by the President, the Minister can, on written agreement and whatever conditions he deems fit, grant loans out of the general revenues of the Republic to any person or body specified in the warrant. The Minister thus has wide and dangerous discretionary powers to lend public resources.
- Although loans contracted under prior Acts remain valid, all new loans must be raised under the Loans and Guarantees (Authorisation) Act or other written law enacted in future. This section rules out the use of a previous Act, which placed more stringent measures on Government, including the passing of an Act of Parliament to authorise a public loan. (namely, the General Loan and Stock Act of 1931).

Clearly, the Loans and Guarantees (Authorisation) Act does not provide adequate guidance with regard to the procedure to be followed by the Ministry of Finance in negotiating and monitoring loans. It should offer better protection from the risks of borrowing internationally.

In addition to the Loans and Guarantees (Authorisation) Act, the Republic of Zambia can also obtain funds from foreign sources through several means. The Government may issue treasury bills through the “Treasury Bills Act, Cap. 348”. It can also issue stock and bonds or execute loan agreements under a number of Acts, both current and moribund. The General Loans (Guarantee) Act is a general guarantee by the Government.

Under the General Loan and Stock Act, 1931, Cap. 350, money may be obtained through the issue of debentures. This Act is no longer used but it offers much better protection to the Republic than Cap 366, particularly because:

- An Act of Parliament is required to authorise borrowing;
- There are ceilings on the life of a loan;
- A trustee administered sinking fund must be established;
- The date for redemption of stock should not exceed 60 years from the date of issue;

- If the sinking fund is insufficient to cover the principal money borrowed then and only then, are they chargeable to the general revenues of the Republic.

3.2 Constitutional and Statutory Controls on Borrowing

The authority to borrow is controlled and limited through a number of laws, including the Constitution. Thus certain Acts provide mechanisms to monitor and control the power to borrow. However, such laws are either inadequate or ignored by the Minister of Finance because the regulatory mechanisms they create are weak and ineffectual. Below, we outline the key controlling mechanisms.

3.2.1 The Attorney General

The specific functions of the Attorney General are to cause the drafting of and sign all Government bills to be presented to Parliament, and to draw and peruse agreements, contracts, treaties, conventions and any other documents to which the Government is a party or has an interest. An agreement, contract, treaty, convention or other document in which the Government has an interest should not be concluded without the legal advice of the Attorney General unless the law provides otherwise. It must be noted that the Attorney General is an integral part of Government and, therefore, not well placed to give independent advice. His or her independence was further undermined by the fusion of the offices of Minister of Legal Affairs and Attorney General in 2002.

3.2.2 The Auditor General

The Auditor General is the watchdog of the nation's finances and his or her office is set up in such a way as to ensure independence in the performance of these functions. This officer's appointment is ratified by Parliament, the salary is a direct debit on the general revenues and the officer cannot be removed from office without complying with lengthy constitutional requirements. However, it must be noted that the office itself is inadequately funded and dependent upon the Ministry of Finance for regular grants. All staff members other than the Auditor General are seconded by the Ministry of Finance.⁶ The functions of the Auditor General are set out in an Act of Parliament - the Public Audit Act, Cap. 378 of the Laws of Zambia.

The Auditor General's function is to audit the accounts relating to the general revenues of the Republic. This includes auditing any expenditure charged by the Constitution or any other law on the general revenues and making a report thereon to the President within twelve months after each financial year. In practice this report is usually late, sometimes by as long as two or three years.

3.2.3 Parliament and Budgetary Controls

Parliament does not have direct control over the extent to which the nation can be exposed to external debt since such power is the prerogative of the Minister of Finance. Parliament's powers are exercised through more general budgetary controls. Parliament's Committee of Ways and Means, which also doubles as the Committee of Supply and Demand, examines the Government budget under various heads of expenditure and approves certain amounts to be spent under each head.

Such general controls in expenditure may help to limit Government expenditure of external loan funds and begin with the President's good sense in authorising expenditure.

3.2.4 Public Reporting and the Public Accounts Committee of Parliament

The Public Accounts Committee is the Parliamentary institution mandated to scrutinise Government expenditure by verifying and commenting on the Auditor General's report. The Committee's findings and recommendations for disciplinary action in the event of mismanagement of public resources are presented to Parliament as a whole and

published. The Committee can request any information other than ministerial files and minutes. It can also summon any controlling officers, including the Minister of Finance, to appear before it. However, its recommendations are generally ignored as they come in the form of a post-mortem, when the damage is already done and cannot be reversed. The Government's 'action taken' reports invariably say nothing more than 'noted'.

3.2.5 The Central Bank of Zambia's role

The Bank of Zambia is not independent but operates and acts under the Minister of Finance and Economic Development. The Central Bank of Zambia is responsible for determining the exchange rate policy in conjunction with the Ministry of Finance and Economic Development. It is also mandated to manage Government's external debt. The Bank of Zambia handles maintenance of debt records and debt servicing. The Bank also advises the Government on the debt strategy that should apply in such negotiations as Heavily Indebted Poor Countries (HIPC). The Bank is also the official depository of Government funds and is mandated to issue and manage Government loans on terms and conditions determined by the Minister of Finance.

The Government through its Loans and Investments Department is responsible for contracting external loans. The external loans are also repaid by Government through this department which gives instructions to the Bank of Zambia to effect payments. Usually, the Bank of Zambia extends a foreign exchange bridging loan and recovers this from Government accounts later.

3.2.6 The Loan Contraction Process in Zambia in Practice

The External Resource Mobilisation (ERM) department of the Ministry of Finance is responsible for borrowing from external sources. It has three sections. The Bilateral and Multilateral Units are responsible for non debt-creating transactions. Borrowing is confined to a Debt Unit. The Unit is responsible for contracting and managing external loans. The process of contracting loans is not written down, hence there is no standard procedure to guide loan negotiators. Clearly, this violates the UNITAR model mentioned earlier.

Once the department of investments and debt management receives a request for funding from a line ministry, it approaches creditors likely to favour that particular type of project. If the creditors are agreeable to the project, they send a 'standard' draft loan agreement for review by the Ministry of Finance. It is very important at this time to assess the financial implications of the various clauses and conditions in the agreements in order to avoid committing the country to impossible obligations. In practice, not enough attention is given to the study of the draft loan agreement because of the assumption that it is not negotiable. It may not even be submitted to the Treasury Consul or the Attorney General for their comments. And yet, as a contractual agreement, every part of the document ought to be negotiable to ensure true agreement and to justify enforcement of the obligations created.

Although loan agreements may vary, they normally include the following:

- A preamble that includes definitions, the names of the parties and the purpose of the loan. Borrowers need to analyse the definitions of the key concepts carefully and appreciate their implications before agreeing to sign.
- A section on terms and conditions in the loan agreement spells out the borrower's financial obligations including the interest rate, commitment fees, legal and out of pocket expenses, penalties and amortisation. The interest rate is very hard to renegotiate once it is established and the penalties for late payment may be onerous. Creditors usually push for what they claim are standard terms in loan agreements. But it is very important to ensure that the country can comply with the terms and conditions

in the agreement. The loan agreement must be seen as a contract and, therefore, subject to the rules of contract.

- The borrower must make certain representations of fact relating to their financial and legal status. For instance that the legal requirements under the national law have been complied with.⁷ They must also equate the ranking of new debt to any other existing, unsecured indebtedness.
- A section under Covenants and Undertakings deals with promises by the borrower to perform or refrain from doing anything (such as changing domestic law) that would affect its financial condition and integrity. Covenants generally project into the future so the borrower must be careful not to unduly restrict its financial and operational activities.⁸
- A section on Preconditions to Disbursement sets forth a number of conditions that the borrower must meet before the loan is disbursed. These conditions may be excessive and irrelevant, unduly delaying draw down on money that is already incurring commitment fees. They should be negotiated to a minimum.
- A section on Default generally identifies events that give the lender the right to accelerate the maturity of the debt and terminate its commitment. These events must be few and clear, not subject to arbitrary determination by the creditor. For instance, they should not include factors beyond the control of the borrower. In the case of technical default (violation of covenants), as opposed to blatant default, (non payment), the borrower should ensure a reasonable grace period in which to effect compliance before penalties become applicable. Borrowers should also avoid cross-default clauses under which default on one loan triggers default on other loans.
- In case of disagreement or default, the loan agreement also contains the law that will determine any dispute. Currently the creditor determines the law that is applicable. (This position is due to a reversal of the traditional position under which, the law of the borrower state was applicable in cases where the lender was not a nation state.) The applicable law and dispute resolution institution - whether international or in a creditor state - is heavily dominated by jurists from the north. For instance, loan agreements generally include a waiver of sovereign immunity placing the borrower at the same level as the creditor, be it a bank or multilateral financing institution.

Zambia has generally performed very badly with regard to loan negotiation. The initiation, negotiation and conclusion of loan agreements has tended to be carried out as though the lender is doing the country a favour and should not be asked too many questions lest the loan be withdrawn. The fact of the matter, however, is that the lender is keen to lend because that is their business. It is thus incumbent upon the Zambian Government to negotiate favourable loan conditions and preferably opt for grants, especially for social sectors such as health and education.

As it is now in Zambia, once the draft loan agreement is approved, having undergone minimal negotiation or examination of the contractual obligations, a signing ceremony will take place either locally or abroad. At this point, access to the proceeds of the loan will be dependent on the fulfilment of certain preconditions, such as setting up a project unit to implement the project, opening bank accounts etc.

The project accountant draws on the funds using a withdrawal application form. Funds not yet disbursed remain in the custody of the creditor but are committed to the project. It may take years to fully disburse a loan or not all monies may be disbursed due to failure to comply with conditionalities along the way. Yet commitment fees are due and payable throughout. Sometimes creditors cancel loans because disbursement has gone beyond the contracted period. All these obstacles carry financial costs in addition to fees and charges such as interest on disbursed funds.

The same problems also arise with regard to balance of payments support. Where the Government fails to comply with conditionalities such as privatisation the promised support can be withheld, throwing the budget into disarray. In 2003, the IMF withheld US\$ 1 million budgetary support to the Zambian Government because the government overspent its budget by US\$ 125 million and was dragging its feet over the privatisation of the Zambia National Commercial Bank. Over the same period, the EU withheld aid to Zambia because of the projected budget overrun and the US government deferred its promise to cancel US\$ 600 million in bilateral debts because Zambia failed to reach the HIPC completion point.

The process of monitoring loans begins once the loan agreement has been signed. The Director of Investments keeps one copy of the agreement and loans while other copies are sent to the Ministry of Legal affairs and Treasury Consul. The officers in the Debt Unit open a folder on the loan containing the creditor reference number, the date when the loan was signed, the date it takes effect, the period during which draw down should take place, amount and currency of loan, economic sector, repayment dates, interest rates, penalties and applicability. All this information goes into a database used to manage debt. Once the loan becomes effective and disbursement begins, disbursement records are also maintained. The database is used to project debt service due for purposes of budgeting. Each year the budget indicates, in Kwacha terms, what amounts to the equivalent in dollars of debt service on a month-by-month basis. This figure is agreed with the IMF.

4 International Financial Institutions

The two major financial institutions, the World Bank and the International Monetary Fund (IMF), were conceived in July 1944 at a United Nations Conference held in Bretton Woods, New Hampshire, USA.⁹ The Charters of the two IFIs do not provide for interaction with civil society organisations but, due to the growing power of CSOs, they have made some modest efforts to engage with civil society.

During the Donor consultations dubbed the Paris Club meetings, Zambian civil society representatives are sometimes invited and exchange views with the representatives of the two IFIs. Some of the CSO representatives, however, complain that the IFIs are more interested in 'selling' themselves to CSOs than in genuine dialogue. The IFIs, on the other hand, feel that the hostility they see from CSOs is due to lack of appreciation on the part of the CSOs of their role in economic development. It is evident that CSOs want a change in the orientation of the IFIs so that social and poverty issues are taken more seriously than the purely economic aggregates of interest rates, inflation and exchange rates.

It is, however, imperative to mention that most CSOs in Zambia are relatively new and in most cases reflect the social and political situation in the country in the sense that they deal mostly with political and social issues and not so much with economic issues. This means that, while very high competencies have been gained in lobbying and advocacy on good governance, corruption and election monitoring, the same cannot be said regarding economic issues such as trade, the budget process and debt. There is thus a case for capacity building of CSOs in economic literacy and advocacy.

There is also an observation made that the IFIs can play the Zambian government agencies against each other. The HIV and AIDS case is very instructive. In 2002, the Ministry of Finance and National Planning (MoFNP) in Zambia was offered a loan to fight the HIV/AIDS scourge. Many CSO representatives felt uncomfortable and voiced their concerns over the loan. The MoFNP refused to accept the loan on account that it would be difficult to repay. The World Bank later offered the same loan to the Ministry of Health and this ministry accepted it.

Another interesting and possibly more dangerous link is that between loans and grants. A country in good books with the IFIs (implying it is receiving and servicing their loans religiously) can receive grants from the IFIs and other donors. Immediately a country fails the conditionalities of the IFIs and is 'blacklisted' by them, and they and other donors stop offering grants to that country. This means that a country cannot escape the debt trap and opt for grants very easily.

4.1 The International Monetary Fund

According to information released by the Zambia office of the IMF, the main functions and vision of the International Monetary Fund are to:

- Promote international monetary cooperation;
- Facilitate the expansion and balanced growth of international trade;
- Promote exchange rate stability;
- Assist in the establishment of a multilateral system of payments;
- Be a lender for balance of payments problems; and
- Provide technical assistance.

It is important to note that the above mentioned roles of poverty reduction and economic growth were not the original mandate of the IMF. These have been added in response to pressure from the developing countries. It is imperative to prod the IMF

further towards orientating its activities to economic development and poverty eradication. However, this task is difficult because:

- The IMF, just like the World Bank, is controlled by the major economic powers, especially the United States and Europe, whose interests are not necessarily in poverty eradication but expansion of markets for their companies; and
- The IMF is a business entity whose main interests are value for money and profit.

The IMF Zambia office does not appear to have a focal person to deal with civil society organisations. CSOs occasionally make requests for meetings with the IMF representative but access is not easy and often depends on the personality of the officer in charge and not on any laid down procedures.

4.2.1 The World Bank

The World Bank was set up to promote long term economic development, especially the financing of large scale infrastructure projects. The World Bank group is made up of the International Bank for Reconstruction and Development (IBRD), the International Finance Corporation (IFC) and the International Development Association (IDA).

The World Bank group is one of the world's largest sources of development financing. The IDA, in particular, is the main source of lending to developing countries and least developed countries. Like the IMF, the World Bank is largely controlled by the US and Europe and is centred on profit maximisation.

The role of the World Bank's Zambia office, as is the case with the IMF, is advisory to the Government. In official statements and public speeches, both the Zambian Government and the World Bank emphasise their politically neutral position. But, considering the immense financial resources that they command and the debt crisis that afflicts Zambia, it is reasonable to assume that the World Bank carries far more weight than they are willing to admit in public.¹⁰

The World Bank is considered a lead agency for creditors in Zambia. It is also more accessible to CSOs than the IMF.¹¹ The Jubilee-Zambia/Debt Project deals more with the World Bank but urges other donor agencies to bring their influence to bear on both the World Bank and the IMF to help relieve the debt burden for Zambia.

Jubilee-Zambia has further observed that if one wants access to World Bank staff, it is easier to approach the institution regarding the PRSP¹² than debt issues. The Jubilee-Zambia/Debt Project has used this space to interact effectively with both the World Bank and the IMF.

Jubilee-Zambia has also observed that there is more information disclosure at the donor agencies than at the World Bank and the IMF, despite the fact that the major donors are the same ones influencing the two IFIs. It is thus strategically important to keep the major donors well informed.

In 2003, CSOs, through the Civil Society for Poverty Reduction (CSPR), organised a workshop to discuss the role of the IFIs in the loan contraction process in Zambia. A World Bank representative came to the workshop and made a presentation on the role of the World Bank in Zambia. It was clear from her presentation that the Bank would like to state the official role and mandate of the organisation and not look at the practical situation obtaining in Zambia.

5 Civil Society Participation in Loan Contracting Process

The legal loan contraction process described in Section 3 above does not allow room for civil society participation in Zambia. Despite this, civil Society organisations have set themselves up as Jubilee-Zambia and established a debt project hosted by the Jesuit Centre for Theological Reflection. The main reasons for the Jubilee-Zambia Debt Project are briefly outlined below.

5.1 Total Debt Cancellation

Even after the Jubilee Year 2000 and after qualifying in December 2001 for some debt relief under the HIPC initiative the debt crisis still exists in Zambia. At the start of 2003, total debt stock for Zambia was around US\$ 6.5 billion. In a country of ten million people, this is a per capita debt burden of about US\$ 650, or double the per capita GNP. The debt service in 2003 was over US\$ 160 million, or twice the national budget for education and health services. The watchword for the Jubilee Zambia/ Debt Project is:

Zambia's total debt is clearly unpayable. Zambia cannot pay back because the debt burden is economically exhausting. It blocks future development. Zambia will not pay back because the debt is politically destabilising. It threatens social harmony. Zambia should not pay back because the debt burden is ethically unacceptable. It hurts the poorest in our midst.¹³

Because of these challenges, Jubilee-Zambia continues to urge all Zambians and external supporters to continue demanding total cancellation of Zambia's foreign debt for purposes of eradicating poverty.

5.2 The HIPC Initiative in Zambia

Jubilee-Zambia is greatly concerned with the real implications of the HIPC initiative in Zambia, especially for the 80 percent of the population that live below the poverty line. The results of studies done show that HIPC, in its current form, will not benefit Zambia either economically or socially. HIPC is primarily a creditor's plan to assure sustainable debt servicing and not a debtor's plan to assure sustainable development. Its presuppositions are unrealistic (exaggerated estimates of future export earnings), unacceptable (money first to go to debt servicing, before meeting the social needs of the people), and unsuitable (conditionalities continue a discredited SAP). For these reasons, Jubilee-Zambia, while primarily calling for total debt cancellation, will engage in the debate and decisions over HIPC for Zambia by lobbying for a better package and by monitoring the expenditures of any resources freed up under HIPC. This has involved advocating for a more efficient and equitable Poverty Reduction Strategy Paper (PRSP), the implementation of which is one of the conditions for qualifying for HIPC relief.

5.3 The Debt Mechanism

In addition to demanding total debt cancellation, Jubilee-Zambia is keenly aware of the opinion of Zambians as well as outsiders that no debt should be cancelled unless guaranteed that the resources released will be directed to benefiting the poor. Even while some HIPC relief comes to the country, there is serious concern that it should not be diverted to ordinary budget expenditures that are not pro-poor (e.g. expensive vehicles for high government officials). For this reason, Jubilee-Zambia has been lobbying for several years for the establishment of a legal mechanism that requires that debt relief resources be managed in a transparent, accountable and participatory fashion. The proposed 'debt mechanism' would be governed by a tripartite committee, composed of representatives of civil society (e.g., churches, NGOs, trade unions), Members of Parliament, and relevant government officials. Funds would be clearly designed only for poverty eradication purposes, either social services (e.g. health,

education, housing, water), or production programmes (e.g. agricultural, employment generation).

In an effort to promote the legal adoption of the debt mechanism, Jubilee-Zambia conducts popular education programmes using the media and community drama. Jubilee-Zambia/Debt Project also carries out a campaign to gather signatures on a national petition demanding this debt mechanism. These petitions, with signatures now numbering in the thousands, are periodically presented to Members of Parliament, government officials and even the president.

5.4 The Loan Contraction Procedure

Zambia will still continue borrowing and will be expected to service debts even after debt relief is attained but Jubilee-Zambia questions the suitability of the existing loan contraction process in the country. Legally, the Minister of Finance and National Planning is empowered to sign loans worth billions, of US dollars. The Minister does not have to consult Parliament. Lack of transparency, openness, public involvement and information dissemination are the main problems that Jubilee-Zambia recognises in this issue of loan contraction.

Jubilee-Zambia has; therefore, made constitutional recommendations to the Constitution Review Commission (CRC) that contracts for loans beyond a certain level must be submitted to Parliament for full review to determine whether they are in accordance with the best interests of the country.¹⁴ Clear policies and regulations must be put in place so that Zambia can avoid future debt traps.

6 A Case Study: World Bank Enterprise Development Loan

6.1 Introductions and Background

The World Bank extended a concessionary loan under a credit line called the Multipurpose Credit Facility. This credit line was worth US\$ 45 million. The loan was disbursed under the auspices of the Enterprise Development Fund (EDF). Disbursement was through a number of Participating Financial Institution (PFIs) (Anglo Leasing, Barclays Bank Zambia Limited, Cavmont Merchant Bank, First Alliance Bank Ltd and Indo Zambia Bank) to the private sector.

The EDF, launched on 22 June 1998, was under the management of Citibank as Apex Contractor but was later transferred to the Bank of Zambia, still as Apex Contractor. Price Waterhouse Coopers was the Matching Grant Scheme (MGS) contractor. All management contractors were recruited in accordance with international procurement procedures. Negotiations for this loan started as early as 1995 and were finalised in 1998.

The Ministry of Finance and National Planning initiated the loan, supported by the Ministry of Commerce, Trade and Industry. The two ministries had discussions with the World Bank. This was at a time when there was industrial decline and the loan was meant to kick start the Zambian manufacturing and export sectors.

Both government and the private sector contributed to the negotiations for the loan. A technical committee, consisting of government and private sector associations was set up to evaluate and select technical and financial proposals for companies that had applied to become either Apex or Matching Grant Scheme Contractors.

Citibank, among other commercial banks, was selected as the apex institution to wholesale funds to participating financial institutions in the enterprise development loan. The Bank of Zambia was later selected as the apex institution after Citibank served as the apex for over six months.

6.2 Enterprise Development Fund Beneficiaries.

The beneficiaries were basically those in the private sector, through the Zambia Association of Manufacturers (ZAM) and the Zambia Association Chambers of Commerce and Industry (ZACCI), participated in the project design and formulation with the World Bank.

The loan was obtained to complement and support the ongoing economic reform programme by aiding and facilitating investment in internationally competitive economic activities. The loan supported the restructuring and reorientation efforts at the enterprise level.

The loan catered for short, medium and long-term credit. The short-term credit line provided loans for working capital for those companies in exports. The other types of medium and long-term loans were given for capital items.

The assumption made for this loan was that the financial constraints to the private sector would be alleviated and that this would enable companies to grow and create employment.

The loans were divided in three categories, namely the Investment Credit Facility, the Matching Grant Scheme and Technical Assistance to Financial Institutions.

6.3 The Multipurpose Investment Facility

The Multipurpose Investment Facility consisted of an Investment Credit Facility that was worth US\$ 30 million. All Zambian Enterprises were eligible to borrow, provided they satisfied the PFI requirements. The maturity period of the loans was 3 to 7 years.

The financial institutions that were giving out the loans determined interest rates

charged on the loans. The Central Bank, which was the apex institution, provided the funds at 12 months London Inter-Bank Offer Rate (LIBOR) plus 1 percent interest to the participating financial institutions. This was a foreign currency denominated loan. PFIs could access the loans for on lending in either US Dollar or Euros.

The unique feature of the EDF loans was that they allowed for participation by the private sector. The World Bank only facilitated the transfer of funds to the apex institutions. The Commercial banks evaluated the proposals from enterprises and these were sent to the apex institution, which later released funds equivalent to the amounts applied for.

The maximum amount an enterprise would apply for was US\$ 3 million. A group of companies or an enterprise could borrow for different purposes provided that their outstanding loan balance was not more than US\$ 3 million. The grace period is 6 to 17 months but limited to one fifth of the total duration of the sub-loan. The interest paid was left to the discretion of the PFI.

However the multipurpose credit facility was not implemented without any problems. The funds were not accessed as was envisaged because of the general economic decline experienced in Zambia. Most of the banks, even those that qualified, were reluctant to participate in the disbursement of the funds citing the non risk-sharing element as the major stumbling block. However, most of these banks, after being told that this element was not negotiable were willing to reconsider their stand and examine the revised contract.

Other banks cited the poor applications they received as a major reason for not taking part in disbursement of the funds. However, as time went on, there were some improvements in disbursements. The increase in disbursements was also greatly influenced by the sale of the mines in the Copperbelt Province of Zambia (Anglo America PLC bought shares in Konkola Copper Mines), which brought back investor confidence in the banking sector and, indeed, in the whole economy.¹⁵

Since this loan was not the only loan facility that was on the market, it had to be made simple and affordable. It also had to conform to other loan facilities on the market for it to be attractive. In this regard, a number of things had to be changed, which included the reduction in the interest from the original LIBOR plus 2 percent interest under the Investment line of credit to LIBOR plus 1 percent interest.

6.5 The Matching Grant Scheme

As noted, another component of the loan was the Matching Grant Scheme (MGS). This was a facility that provided money for the purposes of helping enterprises build their capacity. Worth US\$ 2.5 million, the MGS was meant to stimulate the use of support services to assist firms in their reorientation. Price Waterhouse Coopers hosted the MGS, which was given as a grant to companies that showed the ability to build capacity in their already existing plants.

The MGS also had its own problems, including slow disbursement of the grant. This was mainly due to the general economic decline in the country, the low liquidity in firms, a declining manufacturing base, inadequate in-firm capacity to produce business plans, coupled with unwillingness or inability to pay for such a plan, and a limited culture of using technical assistance.

The problem of MGS was compounded by certain regulations of the scheme which required that applicants meet 100 percent up front payment for projects before accessing 50 percent reimbursement of their expenditure from the MGS. This requirement was difficult for most enterprises because they did not have enough money to pay up front. Other problems the MGS faced from their clients were their inability to prepare detailed applications, which had to include a business development plan. The MGS dealt with applications up to the grant amount of US\$ 75 000 and a

facility to cater for the small and medium enterprises (SME) application process of up to US\$ 5 000 was also designed.

6.6 The Export Pre-Shipment Facility

The other component of the loan was the Export Pre-Shipment facility. This was equivalent to US\$ 10 million. The Export Credit facility aimed at providing short-term credit to be used as working capital to expand the production base to meet a firm's export orders.

Initially this loan facility was limited to manufacturing companies but it was later extended to companies supplying the mines. The World Bank, due to the very high confidence in the mining sector arising from Anglo American PLC buying shares in Konkola Copper Mines (KCM), facilitated this change. The mining sector was seen as a sector that would put Zambia back on the track of economic recovery. The maturity period of the loan under the export pre-shipment facility was 3 to 9 months.

Once again, the beneficiaries of the loan were through their associations, such as the Zambia Chambers of Commerce and Industry (ZACCI) and the Zambia Association of Manufacturers (ZAM).

6.7 Institutional Development Support

The other component of the EDF was the technical assistance facility that supported the restructuring of the Zambia National Commercial Bank and the computerisation of the Export Board of Zambia.

Technical assistance was given to the Zambia Institute of Bankers (ZIB) to run courses in Investment Evaluation and Export Finance for its members. Additional assistance went to build capacity at the Export Board of Zambia (EBZ) in Information Brokerage. The Bank of Zambia also benefited from the facility under the Bank Supervision department. The funds were finally exhausted in 2002 and Zambia is yet to repay them. This just adds on to the many loans the government has to pay back.

6.8 The Role of Parliament

There was very little role for Parliament in this loan contraction process. Government and the private sector representatives did all the design, negotiation, and implementation. The only time Parliament was involved was when a question on the utilisation of the loan was asked in Parliament. Parliamentarians wanted to know how the loan was being utilised and whether it would benefit the small scale sectors. This is not surprising because parliament does not have direct control over the extent to which the nation can be exposed to external debt. Such powers are the prerogative of the Minister of Finance and National Planning. Thus, it is little wonder that members of Parliament are excluded from the loan contraction process.

6.9 Involvement of the Civil Society.

Traditionally in Zambia, the loan contracting process has been the domain of Government only. The civil society, especially the NGOs, is never consulted on the loan agreements government is entering into. This is despite the fact that these loans affect everybody in the country. For the EDF, a few consultations were held with private sector representatives because they were the main beneficiaries but it was not discussed with the rest of the civil society. Civil societies in general, and Jubilee-Zambia in particular, have built capacity over the years to meaningfully engage with the loan contraction process.

Actually getting Jubilee-Zambia involved with the loan negotiations as part of government teams could be highly beneficial to the government, Jubilee-Zambia and the general public¹⁶. There were no protests about the loan although some quarters of society still felt that Government was forever borrowing, despite Zambia's external debt

overhang of US\$ 7 billion. This loan only added on to Zambia's debt burden.

Like all other World Bank loans, it is difficult to quantify the real impact of the loan. This is because, during the time when the loan was contracted, a number of macroeconomic targets were revised due to the economic shock experienced in the mining sector when Anglo American PLC pulled out of Konkola Copper Mines. Most of the Assumptions of economic growth were dependent on the performance of the copper mines.

7 The Rights Based Approach to Debt and the Millennium Development Goals

The United Nations system in general and the United Nations Development Programme (UNDP) have come up with the concept of a rights based approach to development. This entails looking at the many needs of a person and identifying those which are critical to attainment of a decent life. Shelter, clothing, food and health have been identified as critical to human survival. Arising from this, it is incumbent upon each government to ensure that these basic necessities are made available to the people. The Zambian Constitution does not provide for guarantees pertaining to social and economic rights, such as housing and employment of its citizens. The Constitution has thus absolved Government of this responsibility, leaving Zambian citizens unprotected.

In the run up to the year 2000, world leaders met at the United Nations Headquarters in New York and agreed that concerted efforts needed to be made to meet the basic needs of their people within stated timeframes. These 'Millennium Development Goals' (MDGs) centered on the following themes:

- Eradicating poverty and hunger;
- Achieving universal primary education;
- Promoting gender equality and empowering women;
- Reducing child mortality;
- Improving maternal health;
- Combating HIV/AIDS, malaria and other diseases;
- Ensuring environmental sustainability; and
- Developing a global partnership for development.

From the arguments of this paper, it should be clear that external debt is a stumbling block to Zambia's sustainable development and must be effectively and equitably dealt with if Zambia is ever to meet the MDGs. The fact that debt repayments are considered as mandatory budgetary allocations, and not education, health, and water and sanitation, negates the very essence of the rights based approach to development. Table 7, below, shows Zambia's prospects of meeting the MDGs. The picture is not encouraging at all.

The principal problems blocking Government's ability to address the MDGs are as follows:

- The government lacks ownership of the anti-poverty drive with most initiatives coming from donor agencies and civil society organisations rather than from Government's own desire to fight poverty, hunger, HIV and AIDS etc.;
- There has been a serious problem of corruption and abuse of national resources to the extent that the second republican president (former President Fredrick Chiluba) and some of his senior advisors are now appearing in the Zambian courts answering charges of stealing government money and property; and
- In the face of the heavy debt burden that the country is carrying, resources meant to help in the achievement of the MDGs are being utilised to service the debt.

Table 7 Zambia and the Millennium Development Goals

Targets	Will the target be met?	National Support
Extreme Poverty Halve, between 1990 and 2015, the proportion of people living in extreme poverty	Unlikely	Weak
Hunger Halve, between 1990 and 2015, the proportion of people who suffer from hunger	Unlikely	Weak but improving
Universal Primary Education Ensure that, by 2015, children everywhere, boys and girls alike, will be able to complete a full course of primary schooling	Potentially	Strong
Gender Equality Eliminate gender disparity in primary and secondary education, preferably by 2005, and to all levels of education no later than 2015	Potentially	Fair
Child Mortality Reduce, by two thirds, between 1990 and 2015, the under five mortality rate	Potentially	Fair
Maternal Health Reduce by three quarters, between 1990 and 2015, the maternal mortality ratio	Unlikely	Weak but improving
HIV/AIDS Have halted by 2015, and begun to reverse, the spread of HIV/AIDS	Potentially	Fair
Malaria and Other Major Diseases Have halted by 2015, and begun reversing, the incidence of malaria and other major diseases	Potentially	Fair
Environmental Sustainability Integrate the principles of sustainable development into country policies and programmes and reverse the loss of environmental resources	Unlikely	Weak but improving
Water and Sanitation Halve, by 2015, the proportion of people without sustainable access to safe drinking water and basic sanitation	Potentially	Weak but improving

8 Conclusion and recommendations

National and international efforts need to be put in place to get the country out of the current debt trap. Central to such efforts is ensuring that the debt contracting process is transparent, inclusive and participatory, and that development priorities reflect the aspirations of the Zambian people.

The legal framework for the debt contracting process is weak. Parliament is only marginally involved in the process. The Attorney General and the Auditor General are weak in the sense that they are part and parcel of the executive arm of government and cannot be expected to offer real checks and balances. Civil society organizations need to have meaningful participation in the loan contraction process if loans are to benefit the ordinary Zambians.

8.1 Recommendations

Arising from the above discussion, a set of practical and action-oriented recommendations can be made for both the Government of Zambia and its creditors. Recommendations for Government are that it should:

- 1 Make the process of contracting, processing and monitoring loans part of the constitutional reform process so that the public has an input to the debt situation in the country.
- 2 Along with civil society and the private sector, put in place open, accountable and transparent mechanisms that ensure that all debt relief resources are channeled to the poverty reducing programmes in the country.
- 3 Overhaul its loan contraction process, which is currently legally weak and, therefore, susceptible to manipulation by a few government officials. The process must be made all embracing to include the involvement and participation of Parliament in the contraction of new loans, especially those that tie the country to long periods of repayment.
- 4 Build the relevant capacities of all loan-negotiating officers in Government and some members of civil society and the private sector.
- 5 In the interim period, negotiate for grants only in order to avoid the piling up of future debts.
- 6 Fix and maintain debt service ceiling that is a certain amount (say 10 percent) of its revenues to foreign debt service. Foreign debt service should be met from residual revenues i.e. after the social needs in education, health, water and sanitation have been met.

The international financial institutions and other creditors should do the following:

- 1 Grant full debt cancellation in order to augment domestic resources, while the Zambian Government, together with civil society, should strengthen checks and balances, i.e. strengthen the monitoring mechanisms to ensure that all debt relief resources reach the intended targets.
- 2 Remove strict conditionalities that demand wholesale privatisation of public utilities thus impinging on people's social and economic rights.
- 3 Increase grant funding while, at the same time, honouring their pledge of 0.7 percent of their Gross National Product (GNP) as official development assistance (ODA) to the needy countries.
- 4 Broaden debt sustainability calculations away from export earnings to include the social dimensions of life, such as health, education and poverty.
- 5 Share the risk of a loan with the debtor, i.e. if a project funded by a loan fails both the creditor and the debtor should bear the loss.

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Annex 1

Loan Contraction Process In Zambia

Recommendations For Constitutional Reform

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By: Jesuit Centre for Theological Reflection - hosts for the Jubilee Zambia Debt Project

The Zambian public should be the prime beneficiaries of any loans contracted in their name. Therefore they should have the power to determine the need to borrow and to monitor the effectiveness of the loan. Jubilee-Zambia believes that this calls for constitutional guarantees that enable people to effectively participate in and control the debt contraction process.

Introduction

Zambia's external debt today stands at approximately US\$ 7.0 billion. In a nation of ten million people, this is a tremendous per-capita debt of over US\$ 700, or twice the per capita GDP. This means that a lot of resources are being directed at debt service as opposed to contributing to development. For example, in the 1990s, about 20% of Zambia's GDP in nominal terms was spent on debt servicing, but only 2% to 3% went towards health and education expenditures.

Jubilee-Zambia, a national campaign hosted by the Debt Project of the Jesuit Centre for Theological Reflection (JCTR) has been vigorously calling for the cancellation of this huge external debt, with the freed-up resources from debt relief to be directed toward poverty eradication and integral development. In order to assure that cancellation would really benefit the poor, we have been lobbying for a "Debt Mechanism" to legally be put in place that would oversee the utilization of debt relief resources in a transparent, accountable and participative fashion.

But it is also clear that something must be done to assure that any *future* loans are contracted in a fashion that is more open to public scrutiny and approval – lest the country simply fall back into unsustainable debt! For this reason, Jubilee-Zambia is also lobbying for an effective legal framework governing the Government's power to borrow.

On the basis of a major study commissioned by Jubilee-Zambia, the background and current legal framework for the Government's power has been critically analysed and major recommendations made for improving the process of loan contraction. This summary outlines the findings of the study and presents the recommendations – especially as these recommendations are particularly relevant to the current constitutional review in Zambia.

Background of Loan Contraction

By law, public external debt is a monetary obligation that a country incurs by taking money from outside the country, normally in foreign currency. Some loans are obtained directly by the Government, but others may be obtained by quasi-government institutions provided the Government guarantees repayment. The Government of a debtor country assumes a legal obligation to pay back the loans. In order to do so, the country has to raise revenue from taxes.

It is therefore the people who are ultimately liable for the repayment of public debts. This is true regardless of whether the people were aware of the debts or not, or indeed whether they benefited from the debts or not. The debt must be repaid even if the loan was misused by the Government or individuals and did not benefit the country.

A review of Zambia's external debt portfolio shows that the country has generally borrowed excessively and imprudently, and has managed the debt ineffectively. That this is the case can be seen from the fact that there is not more visible development in place today even after such huge amounts of money has flowed into the country over the years by way of loan contractions.

The reasons for these problems with debt are at least partly attributable to the fact that the legal framework governing the loan contraction process in Zambia is inadequate.

Generally the legal framework relating to debt is made up of national laws that are intended to protect the country and authorize the Government to borrow. These laws are affected by international practice and procedures, which regulate the relationship between the Government and foreign creditors. But international law is heavily biased in favour of the interests of creditors. As a result, Zambia does not benefit from the minimal protection that its domestic laws have to offer.

Another big problem is a failure by Government ministries and parastatals to actually and faithfully comply with the existing law, resulting in *unauthorized* persons contracting loans on terms that are not favourable to Zambia. Furthermore there are no proper records kept of those loans in the appropriate Government offices.

Most importantly, the present system of borrowing lacks legitimacy because the loan contraction process does not include consultation with the people or their representatives before loans are contracted, nor does it result in real benefit to the people. Rather, the present system actually undermines the process of sustainable and integral development.

Recommendations for law reform in the loan contraction process therefore focus on greater public involvement, a clear and detailed debt legal framework and enforcement of legal procedures. They also call for a general education campaign on debt law.

Constitutional Reform Recommendations

Because of these serious problems relating to the loan contraction process, Jubilee-Zambia offers the following specific recommendations to be included in the new Republican Constitution.

1. A Debt Commission or oversight body should be set up as one of the Commissions under the Constitution. This will ensure that the body enjoys the highest level of authority.
2. Parliament should have among its Constitutional powers the clear power to approve all loans prior to actual contraction. This will mean that bills relating to loans will be gazetted and available for public scrutiny before they are passed.
3. Debt service should not take priority over basic human rights. The Constitution should make debt service subject to availability of resources and limit it to a specified percentage of the budget.
4. Borrowing should be treated as a Constitutional issue because of its impact on national interests and on development as a whole. Provisions in the Constitution should indicate that debt should only be incurred for legitimate public investment or as a last resort.
5. Watchdog institutions such as the Auditor-General and the Attorney General must have clear mandatory authority over the borrowing process.
6. The Public should have a right to know about and question all borrowing before loan agreements are signed. This right should be incorporated in the Bill of Rights.
7. All law relating to borrowing should be detailed in one Act of Parliament and authorized by the Constitution.