Analysis of Zambia's current fiscal deficit and its effects on the performance of the economy

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1 Introduction and background

Zambia's fiscal policy is anchored on expenditure rationalisation and revenue mobilisation measures in order to create more room to finance public infrastructure and reduce the overall fiscal deficit. However, the fiscal deficit has been on the increase, peaking at 6.7 percent of GDP in 2013, sparking debate about fiscal indiscipline and growing concerns over the effects of the fiscal deficit on the performance of the economy.

A fiscal surplus/deficit, often expressed as a percentage of Gross Domestic Product (GDP), is the difference between government expenditure and revenue. When the government collects more than it spends, a budget surplus exists; and when the government spends more than it collects, a budget deficit exists.

The fiscal deficit which was just 1.8 percent of GDP in 2011 soared to 3.2 percent of GDP in 2012 and peaked to 6.7 percent of GDP by 2013, the highest deficit the country has experienced in the last few years, before reducing to 5.2 percent in 2014. The fiscal deficit is expected to further reduce to 4.1 percent of GDP in 2015. Government's objective is to reduce the overall fiscal deficit in the medium term to 3.2 percent of GDP by 2017.

The deficit has been financed by both external and domestic borrowing. With both the external and domestic debt on the rise, this has sparked debate about the increased stock of public debt and high debt servicing. The stock of domestic debt rose from 12.3 percent of GDP in 2011 to 14.6 percent of GDP in 2014, while the stock of external debt equally rose from 8.3 percent in 2011 to 17.8 percent of GDP in 2014. Interest payments on debt have increased from 0.9 percent of GDP in 2011 to 1.9 percent of GDP in 2014 and are expected to rise further to 2.2 percent of GDP in 2015.

How high a fiscal budget can we sustain? The Protocol on Finance and Investment set out deficit targets for SADC Member States. Member States were to achieve ratios of budget deficit to GDP of less than 5 percent by 2008, decreasing to less than 3 percent by 2012 and maintaining that ratio through 2018. This means that Zambia's deficits have been within the thresholds until 2012 when the deficit reached 3.2 percent of GDP and has been above this threshold ever since. The 2013 fiscal deficit was the highest deficit recorded in the last decade.

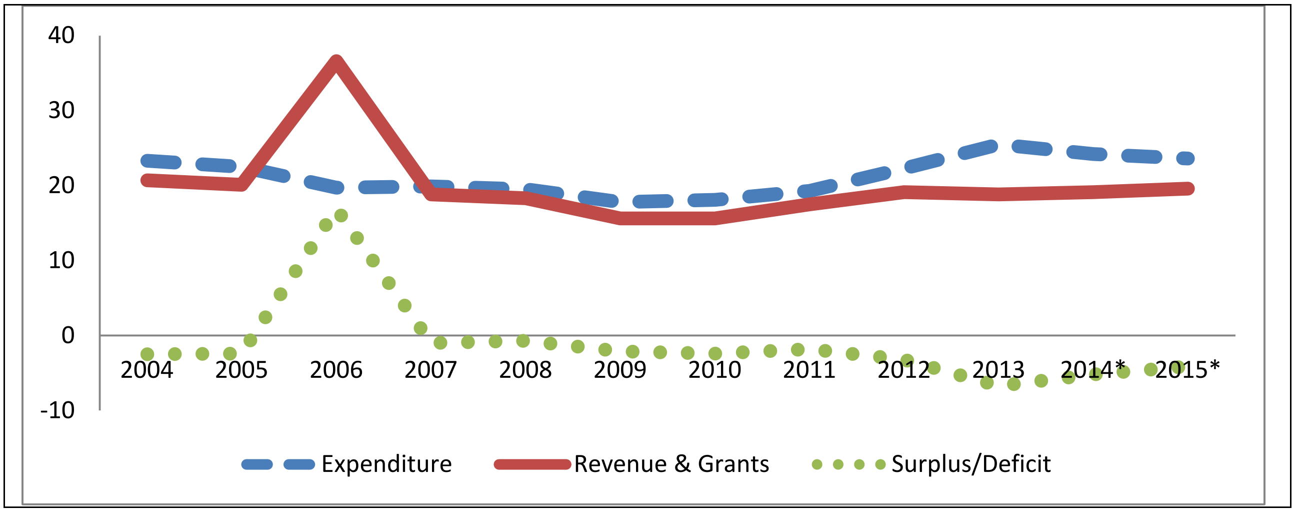
This note examines the trend and causes of fiscal deficits in Zambia. It also seeks to determine the effect of the fiscal deficit on Zambia's economic growth and assesses the consequences of the fiscal deficit on the Zambian economy.

2 The Nature and Causes of Fiscal Deficits in 2013

In 2013, the Government set out to limit the overall fiscal deficit to 4.3 percent of GDP, but the outturn was 6.7 percent of GDP. We examine the causes of this by looking at both the expenditure and revenue side. Government expenditure to GDP ratio experienced a sharp rise beginning 2011, peaking at 25.5 percent of GDP in 2013, before reducing to 24.2 percent of GDP in 2014. It is projected to further reduce to 23.6 percent in 2015.

In the wake of debt cancellation through the Highly Indebted Poor Country (HIPC) and Multilateral Debt Relief (MDR) initiatives which freed up resources in terms of debt servicing, coupled with high copper prices, the country recorded exceptionally high revenues and grants in 2006 amounting to 36.6 percent of GDP leading to a fiscal surplus. By 2011, revenues and grants had fallen to 17.5 percent of GDP. They increased to 19.1 percent in 2012 before reducing to 18.8 percent in 2013. Revenues and Grants are projected to increase to 19.1 percent of GDP in 2014 and increase further to 19.6 percent of GDP in 2015.

Figure 1: Expenditure, revenue and fiscal deficit/surplus, 2004-2015



*Source: International Monetary Fund, Regional economic outlook. Sub-Saharan Africa, October 2014; *projected*

A number of factors were responsible for the record high fiscal deficit recorded in the last two years. These included the unprecedented increase in wages of public sector workers and other recurrent expenditures, higher than programmed expenditures on road and other infrastructure, as well as lower revenues.

2.1 Unplanned expenditures

Personal emoluments as a share of GDP breached the 8 percent barrier in 2013 and reached 8.2 percent of GDP, and jumped to 11.1 percent of GDP in 2014 following the unprecedented wage adjustments for public sector workers. The recent inclusion of 3,100 public sector workers on the government payroll has further increased the wage bill. Government’s planned recruitment of teachers, health personnel and agriculture extension workers in the short to medium term will further put pressure on the wage bill.

In its quest to prioritise public infrastructure and rehabilitation, Government’s spending on non-financial assets – mainly investments in road infrastructure - doubled to 6.7 percent of GDP in 2013 from 3.4 percent of GDP in 2011. While Government planned to spend K2.5 billion in 2013, the budget overrun to K3.6 billion.

Despite not budgeting for fuel subsidies, Government spent K1.6 billion on the subsidies in 2013. Government continued to spend more than the allocated budget on the Farmer Input Support

Programme and the Food Reserve Agency's strategic food reserves. During the 2013/2014 agricultural season, Government purchased more maize than the planned 500,000 strategic food reserves thereby putting more pressure on the treasury.

2.2 Lower than planned revenues

Domestic revenues in 2013 amounted to K24.5 billion, and were below target by 1.0 percent largely on account of lower collections on Income Tax. Company Income Tax underperformed by 40 percent on account of lower mining tax revenues. Mineral royalties, customs and excise duties and grants were also lower than programmed.

Table 1: Revenue performance, 2013 and 2014 (K' thousands)

	2013				2014 (Jan-Oct)			
	Budget	Prelim. outturn	Variance	% Variance	Budget	Prelim. outturn	Variance	% Variance
I Revenue and Grants	**26,271,430**	**24,949,234**	**-1,322,196**	-5.0%	**25,811,393**	**25,996,050**	**184,658**	0.7%
II Revenue and Direct Budget Support	**25,344,959**	**24,798,314**	**-546,645**	-2.2%	**24,502,272**	**25,922,324**	**1,420,052**	5.8%
III Domestic Revenue	**24,745,891**	**24,497,279**	**-248,612**	-1.0%	**24,161,302**	**25,888,521**	**1,727,219**	7.1%
Tax Revenue	**23,535,894**	**23,082,572**	**-453,322**	-1.9%	**19,855,297**	**22,197,558**	**2,342,261**	11.8%
Income Tax	**12,809,445**	**11,574,501**	**-1,234,944**	-9.6%	**9,815,475**	**10,084,742**	**269,268**	2.7%
Company Tax	4,788,590	2,853,760	-1,934,830	-40.4%	3,664,945	3,391,279	**(273,665)**	-7.5%
o/w Mining	2,946,823	1,082,894	-1,863,929	-63.3%	1,687,618	1,502,960	**(184,658)**	-10.9%
Pay As You Earn (PAYE)	5,018,655	5,682,243	663,587	13.2%	4,874,928	5,380,852	**505,924**	10.4%
Other Income tax - Withholding Tax	1,080,170	1,277,771	197,601	18.3%	1,275,601	1,312,610	**37,009**	2.9%
Value Added Tax (VAT)	**6,016,419**	**7,347,964**	**1,331,545**	22.1%	**5,583,807**	**8,089,396**	**2,505,588**	44.9%
Customs and Excise Duty	**4,710,030**	**4,160,107**	**-549,923**	-11.7%	**4,410,902**	**4,001,222**	**(409,680)**	-9.3%
Non Tax Revenue	**1,209,997**	**1,414,707**	**204,710**	16.9%	**4,306,004**	**3,690,962**	**(615,042)**	-14.3%
IV Grants	**1,525,539**	**451,955**	**-1,073,584**	-70.4%	**1,650,091**	**107,530**	**(1,542,561)**	-93.5%

Source: Ministry of Finance, 2014

However, based on preliminary data up to October 2014, there has been a turnaround in the revenue performance compared to 2013. Domestic revenue was 7.1 percent higher than projected during the period January to October, 2014. The improved performance in domestic revenue and reduced expenditure has led to the lower budget deficit expected in 2014.

3 Implications of Fiscal Deficits on the Economy

Theoretically, there are three competing schools of thought that explain the impact of the fiscal deficit on the economy. These are the Neo-Classical, Keynesian and Ricardian Equivalence. The Neoclassical school argues that deficits are harmful to the economy via the mechanism of raising interest rates which causes crowding out. This view is countered by Keynesians who argue that as long as the economy has excess capacity and is operating below full employment, deficits will stimulate economic activity via aggregate demand. The Ricardian Equivalence, however, opines that deficits are at best neutral. This is due to the fact that rational agents interpret a deficit rise as merely implying an equivalent future tax hence they will increase their present savings to offset the impact of the deficit increase and therefore neutralising it. Thus the question of the effects of the fiscal deficit on an economy is an empirical one.

Notwithstanding that no empirical study has been conducted to make meaningful conclusions, it can be argued that fiscal deficits results in a higher stock of debt and may have led to the reduced current account surplus, and the crowding out of the non-financial private sector, among other things.

3.1 Deficit and Debt

Each year the deficit adds to a country's debt stock. Zambia’s public debt stock increased from 20.6 percent of GDP in 2011 to 32.4 percent in 2014. As the debt grows, it increases the interest on the debt which must be paid each year. Interest payments increased from 0.9% of GDP in 2011 to 1.9% of GDP in 2014. The payments are expected to increase further to 2.2% of GDP in 2015. This increases spending without providing any benefits. The interest payments for both the domestic and external debt in the 2014 national budget are higher than the entire social protection budget.

Table 2: *Debt servicing (K’ millions)*

Interest Payments	2011	2012	2013	2014*	2015*
Domestic	1,013	1,636	1,870	2,270	2,893
Foreign	69	101	361	878	1,397
Total	1,082	1,737	2,231	3,148	4,289
% of GDP	0.9	1.4	1.5	1.9	2.2

Source: Ministry of Finance, 2014; *projected

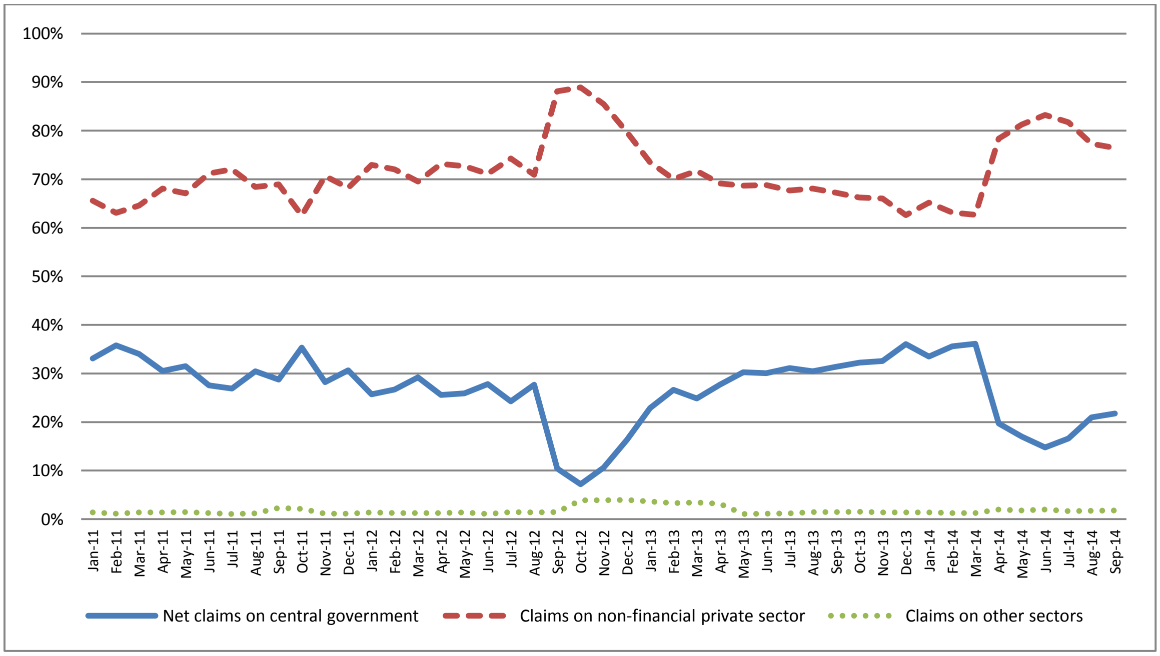
3.2 Deficit and Current Account

The increase in the fiscal deficit in the last few years may have in part led to the reduction in the current account surplus which decreased from 5.9 percent of GDP in 2010 to 0.7 percent of GDP in 2013 when the fiscal deficit reached a record high.

3.3 Deficits and the crowding out of the private sector

When Government increases domestic borrowing to finance the fiscal deficit, it uses up domestic private savings that would otherwise have been available for private sector lending. In turn, the smaller residual pool of loanable funds in the market raises the cost of capital for private borrowers, reducing private investment demand, and hence capital accumulation, growth and welfare. With relatively shallow financial markets, and with most firms being in the small and medium enterprise category who have limited access to international finance, domestic debt issuance can lead to both swift and severe crowding out of private lending. During the last three years, the country has experienced several episodes of crowding out of the non-financial private sector. Figure 2 shows the somewhat symmetric relationship between net claims on central government and the non-financial private sector. There was a steady increase in the lending to the private sector from 2011 until October 2012 when it peaked at 89 percent of domestic claims. After October 2012 until March 2014, lending to the government steadily increased, therefore reducing the lending to the private sector. Thereafter up to mid-2014, Government borrowing from commercial banks declined. However, it has been on the increase since then, effectively reducing the lending to the private sector.

Figure 2: Percentage share of domestic credit – commercial banks' claims on central government, non-financial private sector and other sectors, Jan 2011 – Sep 2014



Source: Bank of Zambia Fortnightly Bulletin, 2014

4 Financing the Fiscal Deficit

Until recently, Government has been relying on concessional and non-concessional loans from multilateral and bilateral institutions such as the World Bank, IMF and donor countries to finance the fiscal deficit. However in 2010, the World Bank reclassified Zambia as a lower Middle income country implying that Zambia has now become richer than before. As a consequence, bilateral and multilateral financiers shifted concessional and non-concessional loans from Zambia to needy countries in the lower income bracket hence we became victims of our own success. With the unpredictability and dwindling of traditional sources of income over the years, Government has had to diversify its financing sources by resorting to commercial borrowing both from domestic and external markets particularly the issuance of sovereign bonds.

Zambia is not alone in the issuance of sovereign bonds, a number of other African governments, that include Ghana, Gabon, the Democratic Republic of the Congo, Côte d'Ivoire, Senegal, Angola, Nigeria, Namibia, Rwanda and Tanzania – have been able to raise funds in international debt markets (Moody's Investor Service, 2014).

To this effect, Zambia has so far successfully issued two Eurobonds amounting to US$1.750 billion in total. The country issued its debut 10-year US$750 million international sovereign bond on 13th September 2012. The Eurobond issuance, which had a coupon rate[1] of 5.625%, was oversubscribed by more than 15 times. This led the country to increase the initially planned amount of US$500 million to US$750 million, with the excess funding allocated to additional investment projects. In order to

[1] The interest rate stated on a bond when it is issued.

augment funding to the selected investment projects under the first Eurobond, Government again successfully issued a second Eurobond amounting to US$1 billion in 2014 at a coupon rate of 8.5% which was oversubscribed by only US$ 4.5 billion. While the former shows high level of investor confidence at relatively lower interest rates, the latter shows some degree of waning investor confidence. In total $128million will be paid in annual interest to service these debts up until 2022 when the first bond will be due for pay back.

Sovereign bonds carry significantly higher borrowing costs than concessional debt does. By February 2013, the 10 African economies mentioned earlier had collectively raised $8.1bn from their maiden sovereign-bond issues, with an average maturity of 11.2 years and an average coupon rate of 6.2%. These countries' existing foreign debt, by contrast, carried an average interest rate of 1.6% with an average maturity of 28.7 years (Stiglitz, 2013). The average maturity on new external debt commitments in Zambia was last reported at 23.48 years in 2010, with an average interest rate of 1.72% (Trading Economics, 2013). So, what is the lure of sovereign bonds?

4.1 Benefits of Sovereign bond issuance

Issuance of sovereign bonds on the international market offers a number of benefits for Zambia. According to the International Monetary Fund (IMF), the following are the benefits of issuing sovereign bonds in the international capital market (International Monetary Fund, 2014).

i. Allow access to a much wider pool of capital than available from concessional financing and domestic savings, and thus help finance desired infrastructure projects more rapidly;
ii. Provide a source of foreign exchange, to help finance import-intensive expenditure (such as major infrastructure projects) without the need to tap into existing reserves or risk weakening of the Kwacha;
iii. Mitigate domestic debt issuance requirements, and thus potential pressures on domestic interest rates and private sector credit growth;
iv. Provide a benchmark for potential private sector dollar-denominated bond issuance;
v. In principle, it can help strengthen incentives to maintain prudent macroeconomic policies and continue reform efforts;
vi. International sovereign bond issuance can provide a benchmark for pricing corporate bonds in international markets, over time expanding the yield curve, and help increase access for the private sector and parastatal companies;
vii. In some cases, sovereign bond issuance can help lower debt servicing costs by substituting outstanding public external debt instruments (also denominated in foreign currency) contracted at higher interest rates with sovereign bonds with lower coupon rates, longer maturities, and no amortization for a significant time.

4.2 Risks of issuing Sovereign Bonds

i. Excessive fiscal expansion and public debt management challenges could negatively affect macroeconomic stability;
ii. Limited administrative capacity, weak fiscal institutions, low efficiency of public investment expenditure, poses a risk that increased public spending or investment projects financed by

bond issuance may be poorly selected or executed and therefore would not render value for money. Increased public investment spending may also be accompanied by a rise in recurrent primary spending, which may be hard to reverse;

iii. Interest rate and exchange rate risks could threaten macroeconomic stability of Zambia. Although issuing sovereign bonds at still relatively low interest rates for longer maturities is generally advisable and could reduce rollover risks, Zambia needs to factor in risks arising from changes in macro financial environments over time. Bonds, in particular those with a bullet repayment structure as is the case with the two Eurobonds, may have to be repaid at a time of higher interest rates, or when the currency may be weaker. As a copper dependent economy, payment of principal could be due at the time when the copper prices are low. Already the copper prices on the international market are trending downward. A strong public debt management office would help mitigate the risks associated with public external debt. This would also entail the establishment of a sinking fund to repay the $750 million and $1 billion bullet payments due in 2022 and 2024 for two bonds respectively;

iv. Although sovereign bond issues could help increase private sector and parastatal entities' access to international capital markets, sometimes corporate governance structures and debt monitoring capacity may not be in place to contain macroeconomic and structural vulnerabilities arising from increased private sector and parastatal external debt and currency risk exposure. Both the Asian crisis and the financial turmoil in Europe are reminders of the drawbacks of excessive private foreign debt;

v. Similar to other forms of capital flows, international bond financing has potential repercussions for the conduct of monetary and exchange rate policy. A shift to larger foreign financing potentially implies appreciation pressure for the domestic currency (depending on the import content of the associated spending). This may harm export competitiveness and if addressed via the issuance of sterilization bills, may cause an interest burden to the monetary authority , in this case Bank of Zambia or the treasury

4.3 Other financing options

Zambia needs to carefully assess its capacity and financing constraints in weighing the weaknesses and strengths of various sources of funding. Wide options exist and should be explored in filling the expenditure gap particularly that of infrastructure. The funding options include local currency bonds, international bonds, Public Private Partnerships, syndicated loans, collateralized loans, and donor financing. From the cost and risks point of view the concessional loans remain the most attractive and cheapest source of financing. However, being a middle income country, Zambia is finding it harder to access the concessional loans. Therefore, in addition to Eurobonds, the country should diversify its funding options such as PPPs, domestic bonds and syndicated loans.

4.3.1 Domestic debt

Domestic debt securities, which amounted to 2.4 percent of GDP in 2011 rose to 3.0 percent of GDP in 2013. This is projected to decrease to 1.7 percent of GDP in 2014 and 2015. Issuing of domestic debt could have a number of benefits and costs as a source of financing and also carries some significant risks.

Benefits of domestic bond issuance

i. Yields on government securities provide pricing benchmarks that underpin the development of private bond markets and other long-term lending
ii. Treasury securities act as collateral for inter-bank lending – enabling commercial banks to better-manage their liquidity needs and thus the efficiency with which they can transform deposits in to credit, and giving central banks more scope to use market-based monetary policy tools
iii. As a high-quality savings instrument, government securities can provide an attractive alternative to capital flight; and by increasing government's reliability on its citizenry, it is argued that Domestic debt issuance can promote political accountability and thus pressure to improve policy and institutions
iv. Domestic debt issuance will also help deepen and diversify governments' financing sources – expanding potential resources available for infrastructure and other expenditure, and providing a means to manage shocks to other financing sources – as well as building a track record that can help to access international capital markets.

Risks of domestic debt financing

i. Availability of domestic financing can delay revenue effort mobilization raising fiscal concerns;
ii. Domestic debt crowds out private sector borrowing;
iii. High Domestic debt stock can also raise inflation expectations, if monetary policy credibility is low, by raising the perceived risk of the government seeking to reduce the real debt burden through higher inflation.

4.3.2 Public- Private Partnerships (PPP)

According to the Organisation for Economic Co-operation and Development (OECD) (2011b), PPPs are a way of delivering and funding public services using a capital asset where project risks are shared between the public and the private sector. There is increasing interest in this financing modality, which features prominently in several national development strategies. However, in Zambia the PPP concept is still being developed and nurtured.

PPPs are perceived as a financing modality to leverage private sector resources to contribute to large-scale infrastructure projects that the government may not otherwise be able to finance and/or implement. However, PPPs do not come without fiscal cost, and they can entail risks for debt sustainability (Caliari, 2014).

PPPs usually require upfront fiscal incentives and transfers from the host government. Although the debt to pay for the infrastructure in PPPs is officially taken on by the private sector and does not appear in the government's books, PPPs give rise to obligations on the part of the government to purchase services from a private operator and to honour calls on guarantees. In the same vein, services provided by private operators have implicit opportunity costs in terms of foregone revenues from levying tariffs or user fees. PPPs may also appear less fiscally onerous by pulling expenses off the balance sheets, bypassing controls and taking advantage of loopholes in accounting conventions with a lower level of transparency and accountability than on-budget public liabilities.

4.3.3 Lending from Re/Emerging Sovereign Donors

Financial resources from non-traditional donors to developing countries have surged in recent years, especially from countries such as Brazil, China and India. They view their financing as based primarily on the principles of South–South cooperation, focusing on mutual benefits and in many a case without policy conditionality (Greenhill and Prizzon, 2012). However, most of these new resources are not ODA-equivalent (i.e. grants or concessional loans), but they could be assimilated to other official flows (OOFs), which, among other criteria, may fail to meet the minimum 25% grant element for ODA eligibility.

Furthermore, according to the latest World Bank International Debt Statistics (2014), most bilateral debt inflows are coming from non-traditional developing country creditors, notably China, and to a lesser extent Brazil and India. The bulk of these flows (not necessarily concessional) have been directed to large-scale infrastructure projects. It is generally argued that there is little transparency on the exact terms of Chinese loans and on which countries what loans are given to, so it is difficult to know if Chinese lending is a threat to the debt sustainability of poor countries, and if so how big a problem.

Table 3: Comparison of Financing Sources

Financing source	Strengths	Weaknesses
Bonds	Usually fixed coupon rate/Easy enforcement of accountability of governments in financing/Establish yield curve for corporate issuers	Rollover risk and potential carry-cost (due to bullet structure)
Local Currency Bonds	No foreign currency risk/Improve intermediation of savings/Facilitate monetary policy implementation	Potential crowding out private sector /Higher interest compared to international bonds
International bonds	Diversification of lender base/ Access to competitive markets enhances the efficient pricing of bonds; market discipline from bond covenants, investors' due diligence, and market scrutiny	Foreign currency risk/High transaction costs owing to capital market access (underwriting and credit-rating agencies)/Long preparation period
PPP (if linked to investment)	Potential for cost savings through bundling the financing, design, construction, operation, and maintenance of infrastructure/Contingent liabilities may be transferred to private sector	High financing costs reflecting the shift of project risks to private sector equity sponsors/Requires solid legal framework and project skills/Lower transparency and accountability
Loans	Low rollover risk and carry-cost (due to flexible amortization)/Crowd-in private sector investment	Variable rate (usually priced over London Interbank Offered Rate)/Limited competition on financing terms
Syndicated loans	Access to multiple lenders	
Collateralized loans	Lower interest compared to ordinary loans	Risk of mortgaging future export Proceeds. Inconsistency with negative pledge clauses of multilateral lenders
Concessional (Donor financing) loans	Low debt servicing cost/Transparency of financial arrangements for public scrutiny	Limited contribution to financial sector development/Scarce resources, long gestation period

Source: IMF; Issuing International Sovereign Bonds, 2014

5 Containing the fiscal deficit

Government expects to bring down the fiscal deficit to 5.2 per cent of GDP this year and achieve a fiscal deficit of 3.2 per cent of GDP by 2017. Although reducing the fiscal deficit is an economic imperative, the measures that need to be taken for its realisation are not politically expedient. Following the death of the fifth Republican President, Michael Sata, Government has had to spend on an election which was not planned for. The total cost of the presidential by-election is estimated at K344 million.[2] As part of the presidential election campaigns, potential candidates have promised to reverse the wage freeze, a move likely to slow down efforts to contain the deficit. The Government's decision to purchase maize beyond the strategic food reserve requirements is also part of the measures that are likely to derail the programme of reducing the deficit in the medium term. Furthermore, the need to hire more teachers, health care personnel and agriculture extension workers makes the containment of the fiscal deficit nearly impossible. Bringing down the fiscal deficit therefore requires a strong resolve on the part of the Government to undertake reforms on the revenue side and on public expenditure.

a) Revenue mobilisation measures

Government revenue, excluding grants, of about 17 percent of GDP in 2013 and 2014 is below its middle income peers in Sub-Saharan Africa. Increasing government revenue is certainly important to reduce the deficit, but it is not sufficient. The low tax revenue is due to tax exemptions, inefficiencies in the tax administration, tax avoidance and tax evasion.

There is need for comprehensive tax reforms that will improve efficiency in tax administration and thereby increase compliance by the tax payers. This will increase revenue collection especially from tax types such as PAYE, withholding tax on rentals that are withheld at source. The recent rolling out of the *TaxOnline* payment system by the Zambia Revenue Authority (ZRA) is expected to improve efficiency in administration of consumption taxes such as VAT through early filing of returns and e-payment of taxes. The Zambia Revenue Authority is commended for this innovation in improving tax compliance but more needs to be done to improve tax revenue collections.

b) **Expenditure rationalisation**

Reducing public expenditure through more prudent public expenditure on the basis of economic and social prioritisation is also necessary. Public expenditure on salaries, new recruitments and pensions is likely to increase in the coming months if the wage freeze and the retirement age issues are reversed. Notably, in the 2015 National Budget, Government has proposed measures to contain the fiscal deficit by limiting the public sector wage bill and streamlining expenditures towards priority programmes. Specifically, Government will control recurrent expenditures of the budget, limit expenditure on maize marketing, ensure cost reflective fuel pricing and rationalise capital expenditure.

Mindful of the fact that a total of $128 million in interest has to be paid annually on the Eurobonds issued with principal to be repaid at maturity in 2022 and 2024 for the $750million and $ 1billion Eurobonds respectively, selection of projects has to be skillfully and carefully done and as much as possible devoid of political expedience. This should be coupled with continuous monitoring and evaluation on the utilisation of borrowed funds from international capital markets to ensure that the selected projects generate resources commensurate with servicing the respective debt obligations.

[2] So far, the Electoral Commission of Zambia has received grants from the United States amounting to US$1.6 million, the Japanese donated US$ 642, 000, while the Swedish Government has donated €600, 000. These grants amount to just under K20 million.

c) Widening of creditor sources

In order to reduce risk associated with one source of funding; Government should widen its creditor sources. The creditors should include a mix of concessional loans (bilateral and multilateral), commercial debt (banks and international capital markets) and domestic debt.

d) Establishment of a sinking fund

Given market risks such as interest rate and exchange rate volatility inherent with borrowing from the international capital markets, debt servicing could be expensive and unsustainable making default more likely. The Government should consider establishing a sinking fund. Through a sinking fund, Government will systematically set aside resources to pay against the principal, along with each interest payment. This will reduce the bullet principal payments that would have to be paid in 2022 and 2024 for the two sovereign bonds, and therefore reduce the risk of default.

e) Parliament to enhance oversight role over loan contraction and management

Parliament must play the critical role of ensuring accountability and transparency in loan contraction and debt management processes. They should mitigate against the risks of excessive borrowing by reinforcing the countervailing mechanisms of government accountability and legislative scrutiny, and exert pressure on the executive to improve fiscal and budgetary performance.

All public loan contraction and debt management rules and regulations must be anchored on constitutional provisions defining how public loans must be obtained, used and serviced in addition to other precise pieces of legislation. The Legislature should by law approve loans before contracts are signed. This will enable and ensure that the loan contraction process is done within the established guidelines and laws, and can be serviced within the national budget. The legal framework should explicitly mention adherence to a debt strategy consistent with broad macroeconomic policy

6 Conclusion

To ensure that Zambia's sovereign-bond issues does not turn into a financial disaster, the country would do well to put in place a sound, forward-looking, and comprehensive debt-management structure. Despite the diversification 'song' away from copper, most of our export earnings are still from copper. Therefore, dependence on copper export earnings and the volatility of prices on the London Metal Exchange makes us vulnerable. A collapse of copper prices will have adverse impact on our ability to repay loans. A deterioration of other macroeconomic fundamentals may lead to the credit rating agencies downgrading the country's rating, thereby increasing the cost of borrowing. We need not only borrow to invest the proceeds in the right type of high-return projects, but we also need to ensure that we do not have to borrow further just to service the debt.

The containment of the fiscal deficits is undoubtedly difficult to achieve due to the limited revenue base, large interest payments, huge expenditure on public service salaries and pensions. Bringing down the fiscal deficit to 3 percent of GDP in the near future requires a strong resolve on the part of the Government to undertake reforms and to spend public money carefully. This is especially unlikely in the months ahead until after the 2016 elections.

Lastly, there is need to improve data management by having fiscal data based on what is actually spent rather than what is released. It is always a challenge to analyse the fiscal performance of government due to the ever changing numbers.

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