DEVELOPMENT FINANCE ASSESSMENT FOR ZAMBIA

by the Zambia Institute for Policy Analysis and Research

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Acronyms and Abbreviations

8NDP	Eight National Development Plan
AAAA	Addis Ababa Action Agenda
ACC	Anti-Corruption Commission
ACFTA	Africa Continental Free Trade Area
ADFC	African Diaspora Finance Cooperation
AfDB	African Development Bank
ADB	Asian Development Bank
ADF	African Development Fund
ASYCUDA	Automated System for Customs Data
BAZ	Bankers Association of Zambia
BIDA	Bulk Intelligence Data Analysis
BioFin	Biodiversity Finance Initiative
BoZ	Bank of Zambia
CAG	Cluster Advisory Group
CDC	Centre for Disease Control
CDF	Constituency Development Fund
CIT	Corporate Income Tax
CP	Cooperating Partner
CSO	Civil Society Organisation
COMESA	Common Market for Eastern and Southern Africa
DDCC	District Development Coordinating Committee
DEC	Drug Enforcement Commission
DMFAS	Debt Management and Financial Management System
DRM	Domestic Revenue Mobilization
DRM	Development Bank of Zambia
DFA	Development Finance Assessment
DSA	Development Finance Assessment
EFD	Electronic Fiscal Devices
ERP	Economic Recovery Programme
ECF	Extended Credit Facility
EGP	Electronic – Government Procurement
EU	European Union
FDI	Foreign Direct Investment
FIC	Financial Intelligence Centre
FISP	Farmer Input Support Programme
FGP	Focus Group Discussion
FNDP	Fifth National Development Plan
FRA	Food Reserve Agency
FSP	Financial Service Provider
SNDP	Sixth National Development Plan
SNDP	Green Climate Fund
GDP	Gross Domestic Product
GFCF	Gross Fixed Capital Formation
GNI	Gross National Income
GRZ	Government of Zambia
GW-MMS	Government-Wide Management Monitoring System
GWP	Gross Written Premiums
GSB	Government Service Bus
IBRD	International Bank for Reconstruction and Development
ICT	Information and Communications Technology
IDA	International Development Association
IDC	Industrial Development Co-operation
IDP	Integrated Development Plan
IFAD	International Fund for Agricultural Development
IMF	International Monetary Fund
IFF	Illicit Financial Flows
IFMIS	Integrated Financial Management Information System
INDC	Intended Nationally Determined Contribution
INFF	Integrated National Financing Framework
KII	Key Informant Interview
KGS	Keeping Girls in School
LA	Local Authority
LEA	Law Enforcement Agency
LCC	Lusaka City Council
LGAA	Loans and Guarantees Authorisation Act
LGEF	Local Government Equalisation Fund
LME	London Metal Exchange
LuSE	Lusaka Securities Exchange
MCTI	Ministry of Commerce, Trade and Industry
MoFNP	Ministry of Finance and National Planning
MLGRD	Ministry of Local Government and Rural Development
MNO	Mobile Network Operator
MOSES	Mineral Output Statistical Evaluation System
MRT	Mineral Royalty Tax
MSME	Micro and Small and Medium Enterprise
MTDS	Medium-Term Debt Strategy
MTEF	Medium Term Expenditure Framework
MTBP	Medium Term Budget Plan
NAPA	National Adaptation Plan of Action
NCCF	National Climate Change Fund
NDC	Nationally Determined Contribution
NDCC	National Development Coordinating Committee

Acronyms and Abbreviations

NDA	National Designated Authority
NDP	National Development Plans
NGO	Non-Governmental Organisation
NFIS	National Financial Inclusion Strategy
NPCC	National Policy on Climate Change
NRFA	National Road Fund Agency
NHIMA	National Health Insurance Management Authority
NSDS	National Strategy for the Development of Statistics
NSS	National Statistical System
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
OOF	Other Official Flows
OPEC	Organization of the Petroleum Exporting Countries
PAYE	Pay As You Earn
PAC	Public Accounts Committee
PDCC	Provincial Development Coordinating Committee
PDM	Public Debt Management
PFM	Public Finance Management
PIA	Pensions and Insurance Authority
PPDF	Public Private Dialogue Forum
PPPU	Public Private Partnership Unit
RTSA	Road Transport and Safety Agency
REFiT	Renewable Energy Feed-in Tariff
SADC	Southern African Development Community
SBR	Sector Budget Support
SDR	Special Drawing Rights
SDG	Sustainable Development Goal
SEC	Securities and Exchange Commission
SIDA	Swedish International Development Cooperation Agency
SOE	State Owned Enterprise
SSA	Sub-Saharan Africa
TIMS	Tax Invoice Management System
TPIN	Taxpayer’s Identification Number
TSA	Treasury Single Account
TWG	Technical Working Group
TRALARD	Transforming Landscapes for Resilience and Development
UK	United Kingdom
USAID	United States Agency for International Development
UN	United Nations
UNIDO	United Nations Industrial Development Organization
UNICEF	United Nations Children's Fund
UNDP	United Nations Development Program
UNFCCC	United Nations Framework Convention on Climate Change
UNOPS	United Nations Office for Project Services
USSD	Unstructured Supplementary Service Data
US$	United States Dollar
VAT	Value Added Tax
WDC	Ward Development Committee
WFP	World Food Program
WWF	World-Wide Fund for Nature
ZACCI	Zambia Chamber of Commerce and Industry
ZAM	Zambia Association of Manufacturers
ZAMeT	Zambia Mobile Electronic Taxation
ZamStats	Zambia Statistics Agency
ZCCG	Zambia Credit Guarantee Scheme
ZDA	Zambia Development Agency
ZEEP	Zambia Education Enhancement Project
ZIFLP	Zambia Integrated Forest Landscape Project
ZICTA	Zambia Information and Communications Technology Authority
ZIPAR	Zambia Institute for Policy Analysis and Research
ZANACO	Zambia National Commercial Bank
ZPPA	Zambia Public Procurement Authority
ZRA	Zambia Revenue Authority
ZMW	Zambian Kwacha
ZTA	Zambia Tourism Agency

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Foreword

I have the pleasure to present Zambia´s first ever Development Finance Assessment (DFA). This Assessment has been carried out by the Zambia Institute for Policy Analysis and Research (ZIPAR) and the United Nations Development Program (UNDP) at the request of the Government of Zambia through the Ministry of Finance and National Planning. This pioneering study follows a UNDP developed methodology that employs a unique country-level, government-led process of aggregation, analysis, dialogue, and collaboration that helps countries determine ways forward to strengthen sustainable development financing. In so doing, the DFA enables effective resource allocation, necessary to spur economic growth, manages risks, ensures accountability, and fulfils international commitments. Moreover, it empowers the government to make informed decisions, maximize project impact, and contribute to Zambia's sustainable development. In so doing, this DFA provides necessary foundations for the development of the country's development finance strategy, which will aid resource mobilisation for the Eight National Development Plan (8NDP) and the Sustainable Development Goals (SDGs).

I wish to express my heartfelt gratitude to all those who contributed to the consultations and various stages of the DFA process. I extend my sincere appreciation to the Zambian authorities, particularly the Ministry of Finance and National Planning, for their unwavering cooperation and support throughout the assessment. Their engagement and collaboration have been instrumental in the successful completion of this assessment.

I would like to acknowledge the Zambia Institute for Policy Analysis and Research (ZIPAR) for preparing this report in collaboration with UNDP. Their expertise and rigorous research approaches and experience have played a pivotal role in producing this assessment. Their commitment to evidence-based policy analysis has ensured the quality and reliability of the findings presented herein. I am grateful to the ZIPAR team under the guidance of Dr. Herrick Mpuku, Executive Director and technical leadership of Dr Sylvia Mwamba.

I also wish to extend my profound gratitude to the UNDP senior management team led by my immediate predecessor, Mr. Lionel Laurens, and Deputy Resident Representative, Mr. Roland Seri for having initiated and supported the process. The technical team at the Strategy and Policy Analysis Unit led by Mr. Domingos Mazivila, UNDP Senior Economic Advisor, were exceptionally stellar. I also extend appreciation to the UNDP's Financial Sector Hub, the Regional Bureau of Africa, the UN Resident Coordinator's Office in Zambia, the UN Joint Program participating agencies, namely UNICEF, ILO, UNECA, and UNFPA, for their valuable inputs on Zambia´s DFA. Their expertise and contributions have added significant value to the report. Furthermore, I would like to acknowledge the Cooperating Partners´ Public Finance Management (PFM) working group, and all other stakeholders who provided valuable inputs, insights and perspectives that have significantly enriched the analysis and recommendations presented in this report.

We are grateful for the generous support of the Joint SDG Fund, whose financial contributions and collaborative efforts have played a vital role in enabling the completion of this assessment. The findings and recommendations outlined in this report will contribute to the government's determination to transform the Zambian economy and improve the livelihoods of its people. Thank you all for your contributions and unwavering commitment to sustainable development in Zambia.

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UNDP Resident Representative
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Executive Summary

Zambia aspires to become a middle-income country by 2030 (Vision 2030). This long-term vision is expected to be attained by effectively implementing five-year National Development Plans (NDPs) while staying committed to regional and global aspirations such as the African Union (AU) Agenda 2023. However, despite implementing seven development plans over a good period of the country's post-independence economic history and with only even more years (less than a decade) to go before 2030[1], Zambia has little to show as NDP-based socioeconomic development. Indeed, some socioeconomic indicators have deteriorated, severe fiscal imbalances have emerged, prolonged episodes of macroeconomic instability have been experienced, and ultimately, economic growth remains subdued.

One of the main reasons for limited progress toward Vision 2030 is the weak linkage between national planning and budgeting, reflected in uncosted plans, resulting in poor implementation of the NDPs. This Development Finance Assessment (DFA) provides a systematic mapping of Zambia's development finance, including the outlook up to 2030, while assessing the policy, institutional and legal environments for an Integrated National Financing Framework (INFF). By assessing the development financing landscape and reviewing the key frameworks, this Development Finance Assessment (DFA) presents key observations and recommendations, which provide Zambia with an opportunity to "right" the policy, regulatory and institutional wrongs of the past, and accelerate its attainment of Vision 2030. The summary findings and conclusions of the DFA are organized into four building blocks, namley: (i) Assessments and diagnostics; (ii) Financing strategy; (iii) Monitoring and review; and (iv) Governance and coordination. These are considered in turn below.

Assessments and Diagnostics

A review of the macroeconomic and fiscal environment of Zambia indicates that as of 2022 the country continued to grapple with financing gaps. This was reflected in widening budget deficits and an ensuing debt crisis in 2020. For instance, fiscal deficits increased from 1.8 percent in 2010 to 9.1 percent in 2019, 14.4 percent in 2020 (the worst outturn) during the COVID-19 pandemic and 9.0 and 7.8 percent, respectively, in 2021 and 2022, while debt accounted for over 100 percent of the economy. Thus, even as aggressive reforms are anticipated through the IMF-backed home-grown recovery program, which could help to restore macroeconomic stability and attain fiscal sustainability, significant risks remain. The main risks include protracted debt restructuring, weak and lethargic public institutions, a thin private sector, and lacklustre economic growth.

Zambia relies on a blend of public and private resources from domestic and external sources to finance its development objectives. The domestic sources comprise of tax revenue and non-revenues while external finance mainly includes grants, aid, Foreign Direct Investment (FDI) and loans.

Given the limited data and information on development finance flows to Zambia, this DFA only analyses flows for which data were available for the reference period. Despite the gaps, this DFA provides general guidance for the future mobilization of Zambia's domestic and external resources from public and private sources.

Based on the available data, Zambia's development finance landscape has mostly stayed the same over time, as international sources continue to dominate the landscape, concerns remain over prospects for achieving fiscal sustainability and overall sustainable development. Recent shocks such as the COVID-19 pandemic, the Russia-Ukraine war, and uncertainties induced by Zambia's on-going debt distress have laid bare the vulnerability of external flows.

1. Zambia is currently implementing its Eighth National Development Plan, 2022-2026 and is, by law – the Planning and Budgeting Act, 2020 – anticipated to formulate and implement a 9th NDP over the period 2027-2031, which will take the country across the finish line of the Vision 2030

The rapid accumulation of public debt, a symptom of fundamental gaps in the country's financing strategy, has also been worrying given its potential to crowd out private investment. The gaps include a lack of an integrated revenue mobilization strategy and monolithic private sources, including the failure to fully exploit the capital markets and innovative sources such as green finance and carbon markets.

Domestic public finance accounts for the second largest proportion of Zambia's development finance, with tax revenues contributing the most; On the other hand, non-tax revenues have stagnated over the years. It is worth noting that following the COVID-19 and debt default shocks in 2020, domestic public finance overtook international public finance, becoming the dominant source of financing. Nonetheless, domestic revenue mobilization remains subdued, as reflected in rising domestic debt. Weak legislative frameworks, leaked through illicit financial flows, and unstable fiscal regimes have contributed to the narrow revenue bases and low revenue collections. The mining sector has the potential to contribute to revenue mobilization. However, operational challenges and politically inclined government interferences, volatile global mineral prices, and unstable mining fiscal regimes limit the sector's ability to contribute to national coffers and economic growth.

Internally, Zambia also raises significant resources from the private sector. Pensions and Insurance investments have seen a consistent surge over the review period, with the most prominent investments from these funds directed towards Government bonds and property. Additionally, the capital markets have seen significant growth over the review period, as evidenced by the upward trend in the Lusaka Securities Exchange (LuSE) market capitalization. Nonetheless, there is hope on the private domestic sources front, especially with the creation of the Ministry for a Green Economy and Environment and Ministry of Small and Medium Enterprise Development (MSMEs), which are expected to boost innovative financing and draw resources to the private sector.

Public Private Partnerships (PPPs) have emerged as an additional mechanism for the sourcing of financing for infrastructure development. However, PPPs have performed poorly since the enactment of the PPP Act in 2009. At the time of writing this report, only five PPP projects had been successfully completed in Zambia. Impediments to using PPPs include a lack of political will, weak legal framework, and capacity challenges. The Government has made some headway in securing potential PPPs in the infrastructure sector. However, the outlook for PPPs is positive as the Government has initiated PPP legislative reforms and also earmarked some infrastructure projects as PPPs.

Due to insufficient revenue mobilization, the Government engaged in debt financing to bridge the development finance gaps. However, the heavy reliance on debt left the economy in tatters, triggering a debt crisis. To repair its fiscus and restore macroeconomic stability, Zambia has embarked on an IMF-supported debt restructuring and economic recovery program. This entails a shift towards concessional loans, with implications on the development finance landscape. At the same time, grants have taken a back seat, stagnating over the review period. It is also worth noting that should Zambia's economic recovery efforts yield positive results and the country graduates to high economic status (developing country or middle income), the external flows could decline significantly.

Zambia is yet to fully explore innovative and emerging sources of financing such as philanthropy, venture capital, green financing grants, endowment funding pension funds, PPPs, venture capital, green financing, and local capital markets that could contribute to the mobilization of development finance. However, given the treacherous global financial environment exacerbated by the ongoing geopolitical tensions and the resurgent and emerging pandemics, these alternative financing sources provide the bulwark Zambia needs. Additionally, with concerns over fiscal slippages and dwindling external support, Zambia has shifted its focus towards domestic sources and innovative modes of financing, such as PPPs, climate finance, green bonds, domestic capital markets, and thematic bonds, among others, to finance infrastructure, agriculture,

2. **Following the August 2021 elections, Zambia made a turn towards addressing the macroeconomic instabilities, including strengthening the policy environment.**

and empowerment programs. However, underdeveloped capital markets, including carbon markets and weak frameworks, impede the realization of the potential of these largely unexplored sources.

Zambia's macroeconomic and institutional environments were unstable for most of the review period, culminating in a debt crisis in 2020 and other fiscal imbalances. Granted, following the August 2021 elections, the country took a turn towards addressing the macroeconomic instabilities, including strengthening the policy environment. However, the instabilities coupled with climate change related shocks continue to call for investments in risk assessment systems to safeguard development finance.

Financing Strategy

While the Government has made some strides in devising strategies and implementing reforms to boost domestic public finance, more must be done to bolster international and private sources of finance. As this DFA reveals, most policies and frameworks focus on domestic sources with little or no details on international sources. The weak institutional and policy frameworks, reflected in the absence of an integrated financing framework, partially explain the resource gaps that Zambia has been grappling with over the years. These continue to pose a severe threat to fiscal sustainability, macroeconomic stability, and a stable resource pool, all of which are crucial for the attainment of sustainable development. The weak public institutional environment, ineffective planning emanating from misalignments between development planning and financing, poor governance institutions, and inadequate development finance are all also partially responsible for Zambia's struggle its graduation to higher income economic status.

The frequent ministerial and institutional realignments that tend to accompany changes in political regimes also exacerbate the public institutional weaknesses and gaps. Coordination among key stakeholders in the development finance space also needs to be enhanced, particularly within the public sector.

Recent legal reforms, such as the Public Debt Management Act of 2022, are pivotal for enhancing the development finance architecture as they have the potential to improve debt management, significantly altering the development finance landscape. In addition, various institutional innovations are also on the horizon, such as the establishment of the mineral regulatory body and analytics department at ZRA, which will have a bearing on the development finance landscape.

Until recently, Zambia's frameworks for subnational financing had mainly remained undeveloped. However, some progress has been recently made in strengthening the policy, legal and institutional frameworks. These include the ongoing review of the National Decentralization Policy, and the Constituency Development Fund (CDF) Act and guidelines, among others. The Government's unprecedented increase of the CDF by 1,500 percent in 2022 and a further 10 percent in 2023 also demonstrates its resolve to catalyze the decentralization process. The elevation of decentralization is expected to birth other subnational reforms that will spur the broadening of the revenue base at the subnational levels.

It is worth noting that Zambia's record of seven national development plans towards the country's Vision 2030 places it in an advantageous position to establish or enhance prerequisite frameworks for an INFF. However, timely and comprehensive costings of these plans have been few and far between, negatively affecting implementation of the plans.

Overall, this DFA concludes that gaps in policy, institutional and legislative arrangements and data limitations are the main binding constraints for developing an INFF. The weak regulatory environment and policy gaps manifest themselves in terms of weak institutional capacities, policy fragmentation, weak governance systems, and poor policy implementation. In addition, quality data, which is crucial for evidence-based policymaking, is sparse in the case of Zambia. This DFA revealed glaring data gaps, underpinned by inadequate information management systems, which impede effective policy formulation.

From the foregoing, this DFA urges the Government to take concrete steps to address the gaps in the existing frameworks and to develop additional ones where appropriate. The Government must also make strategic public expenditure investments in improving data and information management systems, including establishing database for development finance.

Monitoring and Review

Robust governance, accountability and transparency systems are crucial for sustainable development and for achieving fiscal sustainability. However, this DFA reveals that Zambia needs more reliable monitoring and evaluating (M&E) systems and processes to deliver results. The current lack therefore poses challenges for the effective mobilization and management of development resources. The earlier mentioned inadequate data gathering and management systems further compound the development financial resource mobilization problem. Further, some government institutions do not have established M&E departments, contributing to the overall weaknesses in public sector M&E systems. Where the systems exist, they are fragmented across several institutions and actors, further undermining their usefulness and effectiveness. Zambia also lacks practical reporting tools, including for M&E, which would be essential for effective planning and implementation, contributing to the weak linkage between financing and outcomes. The lack of M&E systems also contributes to the undermining of the public financial management (PFM) framework, which constraints Zambia's ability to attract external development financing.

To strengthen the M&E systems, Government must devote significant resources toward data management, and institutional capacity enhancements. It must also explore ways to integrate and synchronize existing systems or develop and apply an integrated M&E systems approach. A number of specific actions towards strengthening the M&E systems are provided in the main DFA report (see Chapter 8).

Governance and Coordination

A strong governance system is critical for the effective implementation of an INFF. Zambia already has the institutional arrangements and coordination tools that can be adapted to host the INFF. These include Zambia National SDGs Coordination Framework Mechanisms and the governance arrangements for the NDP (in particular, the Public Financial Management Act 2018 and the Planning and Budgeting Act 2020). In addition, the INFF governance structure should also encompass decentralization frameworks. The available governance systems possess the necessary State authority and convening power to bring together various actors across government (Judiciary, Legislature and Executive) cooperating partners, and private sector and other non-State actors, to ensure buy-in, ownership and collaboration.

Going forward, the Government must constitute a team to assess the governance system for the INFF and provide evidence and instance for developing or enhancing the system. This includes benchmarking exercises that should be used to take a leaf from countries that are at more advanced stages in the development and application of development financing strategies. Chapter 8 in the main DFA report elaborates on the key steps toward strengthening Zambia's governance structures.

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Chapter 1: Introduction

1.1 Background

Development finance is an important basis for leveraging resources towards addressing the developmental needs of households, communities, businesses, industries, investors and other economic actors in any given economy. It generally refers to the domestic and external resources or funds, both public and private, that are directed towards achieving sustainable development national objectives, towards improving economic conditions and fostering inclusive growth in a country.

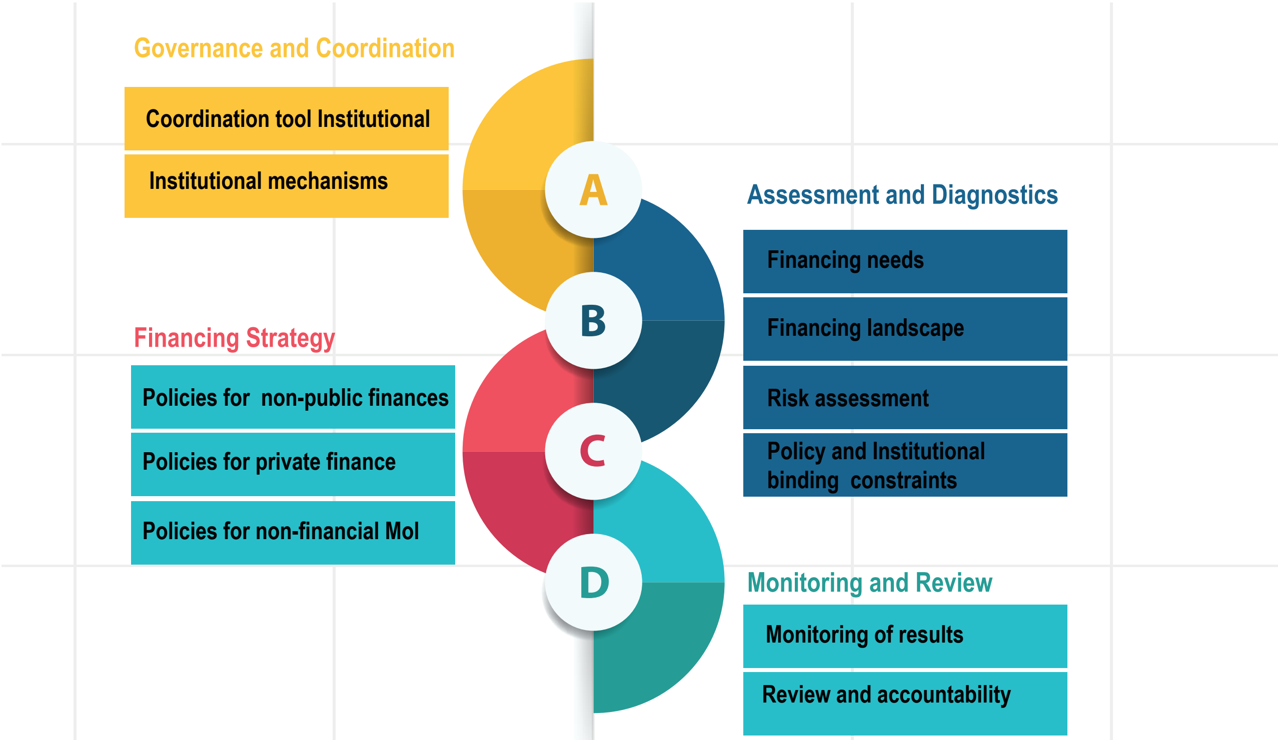
In that regard, Development Finance Assessment (DFA) is gauging and optimizing financial resources from various sources to support national development plans and strategies. In Zambia, where economic challenges such as subdued growth, high inflation, fiscal deficits, and unsustainable debt levels have persisted even before the COVID-19 pandemic, the concept of DFA holds crucial significance, serving as a vital tool to comprehensively analyze the country's development finance landscape, and policy, regulatory and institutional frameworks. In particular, prior to COVID-19, Zambia was already grappling with macroeconomic and fiscal instabilities, culminating in subdued economic growth, a weakening local currency (the Kwacha), rising inflation, widening fiscal deficits, and unsustainable debt levels. Notably, real GDP growth markedly decreased from an average of 6 percent between 2010 and 2015 2.2 percent from 2016 to 2021 while the commodity price situation deteriorated from a single-digit annual average inflation rate of 7.7 percent to a double-digit inflation (annually averaging 13.2 percent) over the same respective reference periods. Additionally, years of fiscal mismanagement pushed the country into debt distress, with public debt accounting for 117 percent of the economy by 2020. The main factors contributing to these woes included enervated institutions, reflected in the weak linkage between planning and budgeting and the lack of an integrated approach to development financing, among others.

Following the change of government in August 2021, Zambia ramped up macroeconomic and fiscal stabilization efforts, setting out on an arduous recovery path. Additionally, the securing of an International Monetary Fund (IMF) Extended Credit Facility (ECF) of US$1.3 billion in August 2022 as well as a deal to restructure US$6.3 billion in loans from official creditors in June 2023 provided Zambia with the desperately needed financial and technical support to reestablish the path to economic recovery. However, despite these external deals, Zambia's ability to fully establish and sustain its economic recovery agenda and attain prospecous middle-income status by 2030 will viscerally depend on how effectively it implements its National Development Plans (NDPs). The resource requirements for attaining the 2030 Agenda and implementing the NDPs are severely constrained, requiring a robust strategy for financing development.

The financing strategies and potential sources are well articulated in the Addis Ababa Action Agenda (AAAA). Specifically, the AAAA recommends that countries establish the Integrated National Financing Framework (INFF) within their jurisdictions to guide their development finance resource mobilization. The INFF includes four building blocks, namely: (i) Assessments and diagnostics; (ii) Financing strategy; (iii) Monitoring and review; and (iv) Governance and coordination. The DFA is a crucial instrument in operationalizing the INFF, an integral component in effective planning and implementation for sustainable development.

The DFA is a tool designed and developed by the United Nations Development Program (UNDP) to help countries identify and pursue opportunities for mobilizing and efficiently utilizing available and additional financial resources, towards achieving the Sustainable Development Goals (SDGs). Further, the DFA is also designed to support governments and their development partners to develop an integrated financing approach.

Figure 1.1 Building Blocks for an INFF



Source: UNDP, 2022, DFA Guidebook

The economic vulnerabilities highlighted above and the need to accelerate sustainable economic recovery necessitated the undertaking of a DFA for Zambia, to provide the Zambian Government with a deeper policy-relevant insight and understanding of the country's development finance landscape and needs as well as the state of play of the associated institutional, regulatory, and policy frameworks. Further, the DFA will be vital in responding to the calls of the 8NDP, the Vision 2030 and the Sustainable Development Goals (SDGs) for adoption of sustainable and inclusive financing strategies.

In the Zambian case, the DFA aims to provide a holistic analysis of public and private finance across domestic and international sources, for sustainable development financing. In addition, the DFA will inform development financing options for the country's NDPs and, more broadly, the country's long-term developmental aspiration, the Vision 2030, which aims to transform Zambia into a prosperous middle-income nation by 2030.

Over time, Zambia has put in place a host of planning, budgeting, and financing frameworks whose effectiveness can be enhanced by the completion of a DFA for the country. This financing assessment will help address the issues of inadequate resources, underpinned by unreliable forecasts and fragmented planning and budgeting processes.

The national planning framework in Zambia revolves around the formulation of five-year strategic plans called NDPs. These plans are cumulatively financed through annual National Budgets which contain a single year expenditure plan. However, these can be constrained in their formulation by their short-term nature at the expense of longer-term strategic financing. To avoid a disconnect between National Budgets and NDPs, a rolling three-year budgetary framework called the Medium-Term Budget Plan (MTBP) (previously the Medium-Term Expenditure Framework (MTEF)) was developed. The MTBP helps to ensure that the National Budget is aligned with the medium-term strategic development aspirations of the nation.

In the past, weaknesses in development planning, suboptimal financing mechanisms and inadequate financing contributed to Zambia's failure to attain its development objectives. Some observed weaknesses in development planning include poor implementation resulting from unreliable resource forecasts, weak institutional arrangements, and inadequate monitoring and evaluation (M&E) mechanisms. These issues persist to date. In addition, existing national development planning tools are often primarily focused on government finances and do not fully explore how government can harness diverse forms of financing, from both public and private sources, either emanating domestically and/or internationally.

Furthermore, the DFA will help improve the alignment of available financing with national strategies and policies. The current national development planning cycle (2022 to 2026) is governed by the 8th National Development Plan (8NDP). The formulation of the 8NDP included a costed implementation plan, whose successful execution could greatly benefit from a clear understanding of the current and future financing landscape and resource forecasts for the country during the plan period. As such, conducting a DFA for Zambia at the outset of the 8NDP is not only timely, but also essential as it would help devise and refine strategies necessary to optimise financing for the development plan.

The financing strategy, which is to be informed by the DFA, will in turn aid the alignment of development financing beyond the NDPs, towards ultimate realization of the Vision 2030 aspirations. In addition, the INFF will ultimately strengthen public resource management and build institutional capacity for the accelerated delivery of Sustainable National Development Goals.

Purpose, Objectives and Rationale

The main purpose of this assignment is to support the Government of Zambia, through the Ministry of Finance and National Planning (MoFNP), to undertake an assessment of the country's development finance landscape as an important first step towards the establishment of an Integrated National Financing Framework (INFF).

The study focuses on the following specific objectives:

i. Review the policy, institutional and regulatory frameworks for public finance management and development finance in Zambia;
ii. Undertake an exhaustive mapping of sources of development finance and relevant financing streams (i.e., private, public, domestic, and external sources);
iii. Conduct a disaggregated trend analysis of financial flows from 2010 to 2020;
iv. Conduct a prospective analysis of major financing flows from 2022 to 2030;
v. Analyse factors influencing the flow of financial resources to and from the country;
vi. Review financing innovations, reforms, and systems in place for enhancing resource mobilization and efficient allocations of these resources across different sectors;
vii. Assess the alignment of financing sources of national development plans and strategies; and
viii. Propose actionable recommendations, and a roadmap for the INFF.

Zambia aspires to achieve broad developmental and economic objectives as espoused in the national development plans (the 5th, 6th, 7th and more recently the 8th NDP) and the Vision 2030. In order to meet these objectives, the plans set out therein must be adequately supported, financed and effectively implemented. This will require a deeper understanding and appreciation of the development finance landscape and the development of a robust strategy for maximization of available finances. Indeed, financing can be a key constraint to a country's achievement of its developmental and economic objectives. As such, adequate financing is essential to improving the quality of national economic development in terms of its depth, inclusiveness, and long-term sustainability.

Moreover, given Zambia's current economic challenges and tight fiscal space, it is important to establish an INFF to support the attainment of sustainable economic development. Therefore, this DFA provides a starting point for the country to develop its INFF. The findings of this assessment also add to the knowledge base, towards building a sustainable and resilient financing system. it also contributes to dialogue and debate on enhancing development finance resource mobilization in Zambia.

1.2 Methodology

A multipronged analytical approach was utilized in undertaking the DFA. The ensured the collection and analysis of adequate authentic information and data on critical aspects of the four INFF building blocks, namely Assessment and Diagnostics, Financing Strategy, Monitoring and Review, and Governance and Coordination. Given that a robust multifaced methodology was essential for analyzing private and public finance by origin (domestic and international), this DFA follows and adapts the analytical approach developed by UNDP to meet the set objectives[3]. Consequently, a multifaceted analytical approach including institutional and stakeholder mapping, desk reviews, and stakeholder engagements in the form of key informant interviews (KIIs) and focus group discussions was employed to accomplish the study tasks. The analytical framework is outlined below;

1.2.1 Major Flows and Sources

The following major sources and flows were explored (see, Table 1.3.1) and can be summarized as follows:

Domestic Public Finance: This encompasses government revenue (tax and non-tax revenues; revenues from state owned enterprises [SOEs]) and government borrowing (government securities) from domestic sources. The data was sourced from the Ministry of Finance and National Planning (MoFNP), Bank of Zambia (BOZ), Zambia Revenue Authority (ZRA), and other sources.

Domestic Private Finance: This comprises commercial bank loans, non-bank credit, private investment; microfinance, corporate bonds; institutional investments (insurance, pensions), foundations, flows from non-governmental organisations (NGOs), civil society organisations (CSOs), and corporate social responsibility, among others. The data sources included MoFNP, BOZ, Zambia Development Agency (ZDA), and other relevant institutions.

International Public Finance: This includes official development assistance (ODA), other official flows (OOFs), and government borrowing from international sources. Government borrowing refers to lending received or guaranteed by GRZ from bilateral and multilateral institutions and private entities. The data sources included MoFNP and line ministries, the IMF, World Bank, Development Banks, Cooperating Partners (CPs) and other donors.

International Private Finance: Major flows include foreign direct investment (FDI), portfolio equity, private borrowing from international sources, remittances, and financing from private funds, foundations and other philanthropical entities. A combination of data sources, included BOZ, MoFNP, ZDA, World Bank, and other relevant authentic sources.

1.2.2 Data Collection

The following data collection methods were used:

Institutional Mapping and Stakeholder Consultations

The aim of the stakeholder and institutional mapping exercise was to identify key stakeholders to be engaged during the DFA and to orient the Consultant to the Zambian development finance terrain. The comprehensive mapping was done in consultation with MoFNP, as the primary custodian of national financial data, and other key stakeholders. Additionally, the mapping process also informed an engagement plan for the DFA process. The main stakeholders and data sources include:

- Government ministries and agencies: MoFNP, Ministry of Green Economy and Environment, ZRA, BOZ, Zambia Statistical Agency (ZamStats), ZDA, and Development Bank of Zambia (DBZ), and Financial Intelligence Centre (FIC), among others;
- State-owned enterprises (SOEs),
- Industrial Development Corporation (IDC);
- Subnational entities;

3. UNDP (2021). Development Finance Assessment Guidebook 3.0. https://inff.org/resource/development-finance-assessment-guide-book

- Private sector players and associations: Zambia Chamber of Commerce and Industry (ZACCI), and Zambia Association of Manufacturers (ZAM);
- CSOs and NGOs;
- Cooperating partner institutions and organisations: World Bank, IMF, OECD and UN system;
- Financial sector institutions;
- Regional body organisations: the Southern Africa Development Community (SADC) and the Common Market for Eastern and Southern Africa (COMESA).

The consultation engagement plan laid out which institutions were engaged at different consultation stages of the DFA. Stakeholders were grouped differently according to their influence and interests in resource mobilisation and policy planning frameworks, with special focus on institutions which were deemed to be very important to the consultation process like the MoFNP. As a lead stakeholder in the DFA development process and custodian of the final output, MoFNP was instrumental in the consultation process and also provided overall project oversight and facilitated access to other key stakeholders and organisations where data was required to be sourced. MoFNP also provided technical input on some sections of the report such as planning frameworks and prospective analysis of the financing flows.

Other government institutions and ministries such as the Ministry of Green Economy and Environment (MoGEE) also provided assistance in the consultation process, especially regarding climate financing, planning and policy issues. Similarly, NGOs and CSOs also provided much needed information in the consultation process such as the review of the adequacy of different policy planning frameworks.

Desk Review

The desk review encompassed several activities including literature review, exploration of international best practices regarding DFA (review of case studies), and secondary data collection and review. During this process, key national documents were examined including national development plans and their financing strategies, MoFNP reports such as Annual Economic Reports and National Budgets, MTBP, Yellow books, and other financing policies and strategies. In addition, other sector thematic plans and policies related to specific types of finance were also reviewed. Further, national publications such as national reviews and progress reports, as well as reports produced by international monitoring agencies and cooperating partners were reviewed.

By design, the DFA exercise was heavy on the quantitative data aspects. Thus, quantitative data was collected from secondary sources, including MoFNP, BOZ, ZamStats, ZRA, and other government reports. As highlighted above, international data sources included the World Bank, IMF, African Development Bank (AfDB), OECD, and United Nation's Agencies. These sources were particularly important for sourcing comparable and reliable data for Zambia on international financing flows and sources (Table 1.3.1). Finally, the desk review process also provided a basis from where subsequent consultation processes such data collection instruments — key informant interview guides and focus group discussion guides— were prepared as discussed below.

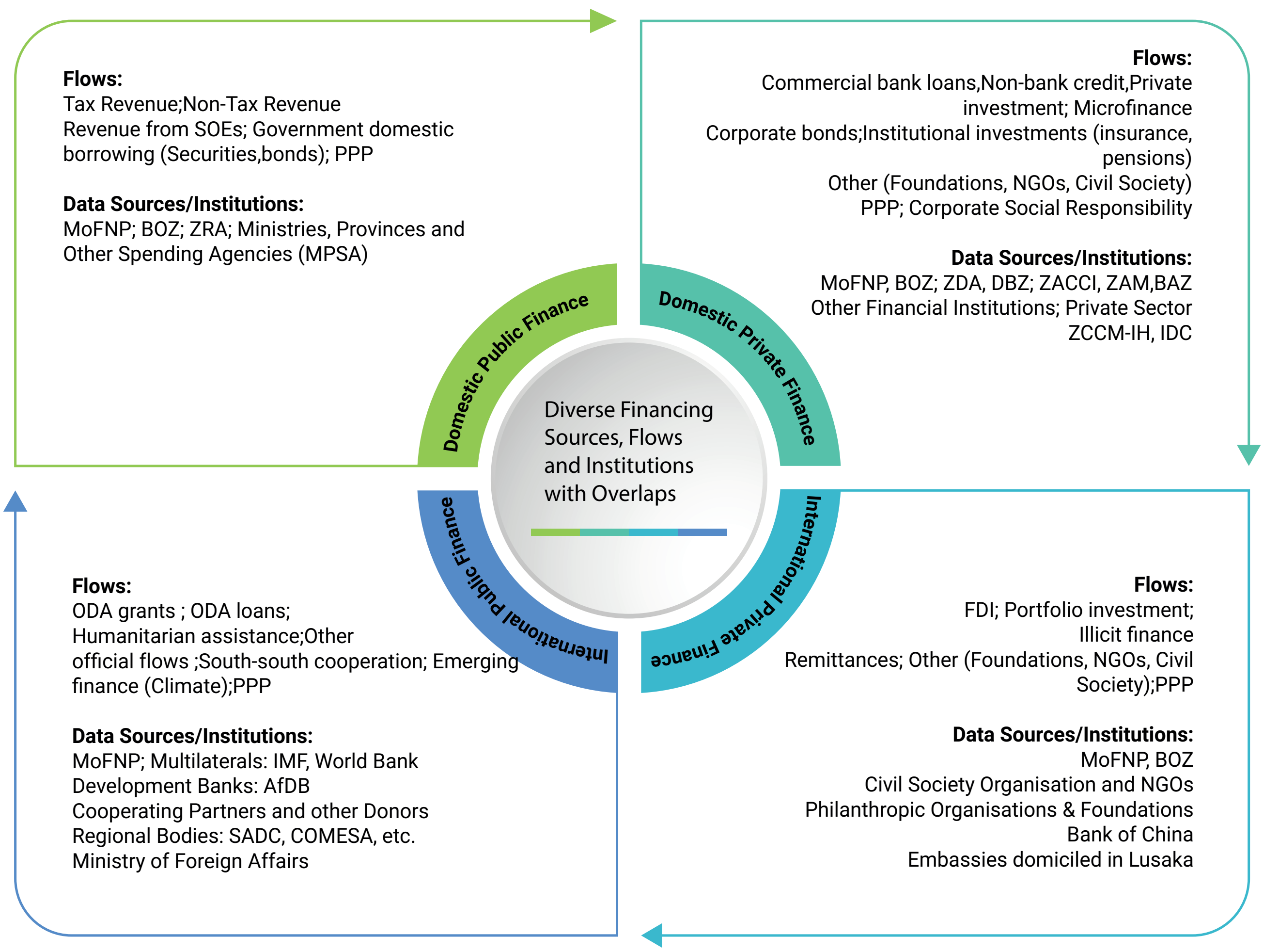
Key Informant Interviews

Using semi-structured interview guides, key informant interviews (KIIs) were conducted with key stakeholders such as MoFNP, Ministry of Green Economy and Environment, BOZ, ZRA, FIC, and CSOs. The KIIs provided an efficient and effective way to consult and engage stakeholders on relevant specific issues that could not be discussed in an open discussion workshop. KIIs also provided a platform to fill in the data gaps on Zambia's different financing sources and flows such as FDIs, remittances, and received government grants and assistance from cooperating partners. Further, some of the stakeholders consulted also directed the consulting team to specific data and information sources. This process also acted as a validation process for the desk review by shading light on observed literature trends from secondary sources.

Workshops and Focus Group Discussions

In addition to KIIs, focus group discussions (FGDs) were part of the consultation process for developing the DFA. Using the mode of open workshop discussion forums and sometimes small breakaway groups, FGDs provided an opportunity to consult different stakeholder institutions and elicit their input, views, and clarifications on common issues of development finance for Zambia that could be discussed openly. Having different stakeholders sitting in one discussion forum provided an opportunity to review and discuss issues that were not part of the discussion guides as opposed to KIIs that usually involve the consultation of a single stakeholder at a time. To that end, vital policy and strategic issues were unearthed and clarification was obtained from relevant stakeholders such as MoFNP, BOZ, ZRA, and FIC. Similar to the KIIs, follow-ups with specific stakeholder were done after the discussions to obtain official data, documents and other information that could not be collected during the discussions.

Table 1.3.1 Financing Flows and Data Sources



Source: Adapted from UNDP Development Finance Assessment Guidebook Volume 3

1.2.3 Data Analysis

The mixed research methods of the DFA yielded a wealth of quantitative and qualitative data and information on development finance and related issues in Zambia. Inherently, the large volumes of data and information required further review and reorganization before the analysis and report writing were conducted. Thus, the data was collated, synthesized, and cleaned in preparation for analysis while the qualitative information was manager in serialized MS Word files for ease of reference. During this process, any emerging data inconsistencies and overlaps emanating from the diverse range of data sources were properly identified and reconciled. Furthermore, quantitative data was subjected to trend, pattern, and other descriptive statistical analyses. Projections to 2030 were also done, mostly based on Zambia's past, present and policy-based future economic conditions, past and present global economic and geopolitical shifts, and key on-going multilateral, regional, bilateral and unilateral programs such as the IMF deal and Official Creditor Committee (OCC) debt restructuring arrangement. Most projections were based on MoFNP models while others used simple time-series forecasting methods, as elaborated in Chapter 4.

Similarly, qualitative data analysis methods such as content analysis, and literature and case study reviews were conducted to enhance and compliment the quantitative data analysis. Finally, as part of the data analysis and report writing process, the DFA report was also subjected to an iterative review process at each stage to ensure robustness of the findings.

1.4 Report Structure

The rest of the report is structured as follows. Chapter 2 highlights the country context of development in Zambia while Chapter 3 provides an assessment of the development financing landscape. Chapter 4 offers a prospective analysis of major financial flows. Chapter 5 analyzes the frameworks of financing strategy. Chapter 6 assesses the monitoring and review for the INFF while Chapter 7 give a review of the governance and coordination structures for the INFF. Finally, the proposed INFF roadmap is presented in Chapter 8.

02

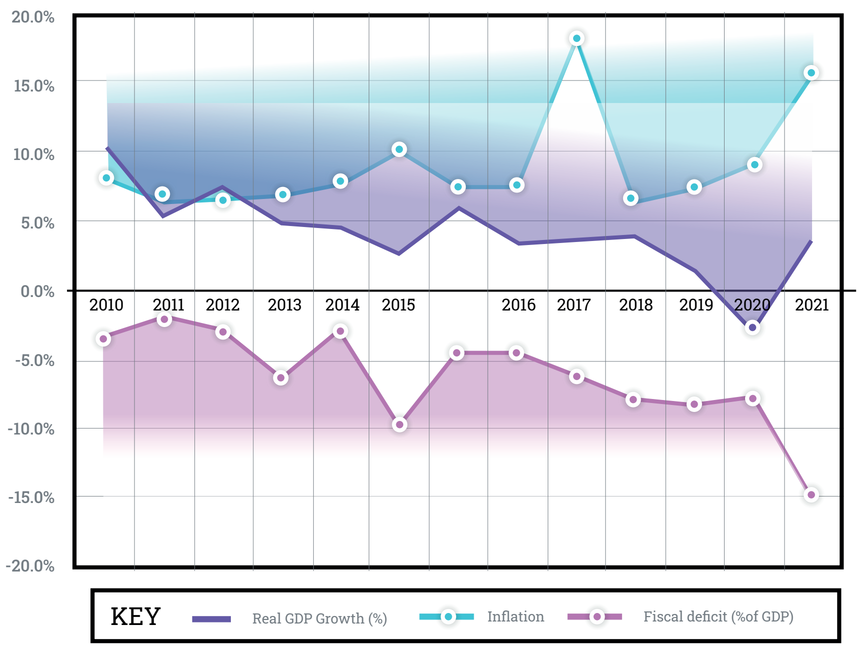
Chapter 2: Country Context

2.1 Macroeconomic Context

Over the last decade, the Zambian economy has been characterized by a deteriorating macroeconomic environment and increasing fiscal constraints. For instance, real GDP growth declined from an annual average of 6 percent over the period 2010-2015 to 2.3 percent from 2016-2021 (Figure 2.1). Also noteworthy is the fact that the Zambian economy contracted by 2.8 percent in 2020, pushing the country into a recession in that year. The contraction was driven by an unprecedented deterioration in all key sectors of the economy largely due to the COVID-19 pandemic and its social and economic effects.

The decline in real GDP growth coincided with the widening and perpetual fiscal deficit, which doubled from an average of 4.4 percent over 2010 to 2015 to 8.1 percent from 2016 to 2021. The combination of fiscal and policy missteps, and economic decline triggered a debt crisis, as debt accounted for 117 percent of GDP in 2020. The sharp deterioration in macroeconomic indicators, especially from 2016 to 2021 suggests that even before the COVID-19 pandemic, the country was already confronted by severe economic headwinds, manifested in deteriorating macroeconomic indicators as shown in Figure 2.1.

Figure 2.1 Selected Macroeconomic Indicators



Source: Ministry Finance and National Planning; Annual Economic Reports

In relation to commodity prices, average annual inflation remained stable and in single digits over most of the reference period (2010 to 2021), except in 2015, 2018, and 2021. In addition, consistent with the marked deterioration in the macroeconomic environment over the recent past, inflation switched from a single-digit annual average of 7.7 percent between 2010 to 2015 to a double-digit annual average of 10.8 percent from 2016 to 2021. The raising inflation was attributed to persistent fiscal slippages reflected in huge Government expenditures.

The weak macroeconomic fundamentals also pose severe threats to development finance mobilization and implementation of sustainable economic development, notably as the Country continued to recover from the economic strain brought about by the COVID-19 pandemic and years of policy implementation challenges. However, the recovery plan that was put in place to restore macroeconomic stability, attain fiscal sustainability and spur economic recovery is beginning to bear some fruit, as shown by the rebound in real GDP growth in 2021 (to 3.6 percent) and projected growth of 3.1 percent in 2022. The recovery is mainly on account of global copper prices remain bullish post-COVID-19, improved post-election market confidence, and aggressive macroeconomic stabilization efforts. However, concerns remained over macroeconomic indicators such as exchange rate, inflation, and fiscal deficits that had continued deteriorating over the reference period.

2.2 Demographic Profile

With about 45 percent of its population aged below 15, Zambia is one of Africa's and the world's youngest countries. The country's population is expected to grow rapidly at 2.8 percent per annum, which will translate into a doubling of the population every 25 years, roughly. From 2011 to 2035, young dependents (0–14 year olds) are projected to account for an average of 45 percent of the population. These demographic shifts are anticipated to put significant pressure on Zambia's already tight fiscal space, posing tremendous challenges to the country's attainment of the SDGs. The socioeconomic consequences of the young population and changing demographics are reflected in high poverty levels and rising youth unemployment. The International Labour Organization (ILO) (2022) estimates youth unemployment at 26.1 percent whereas Zamstats (2021) places this at 17.4 percent. Poverty is expected to increase by 0.2 percentage points to 60.3 percent in 2021, in part reflecting COVID-19 impacts. With the demographic profile being dominated by children and youths and bearing in mind the youth unemployment challenge, brunt of the burden of increased poverty in Zambia will be borne by young people.

With targeted investments in social and economic sectors and effective policy implementation, Zambia will have a fighting chance to turn the demographic challenges around and reap the benefits or dividends – not costs or debts – of the demographic transition. Getting ahead of the demographic transition and harnessing it will require aggressive, steadfast and sustained financing of NDPs.

2.3 Evolution of Economic Planning

Zambia, in its quest to reduce poverty and attain economic prosperity, articulated its long-term development goals in the National Vision 2030. The Vision 2030 reflects the collective understanding, aspirations, and determination of the Zambian people to be a 'prosperous middle-income country'. The Vision sets the horizon for developing the medium-term plans and provides the 'gravitational pull' to achieve long-term objectives. It outlines in broad terms, plausible courses of action to be undertaken towards the achievement of the country's long-term objectives and targets.

The Vision is operationalized through five-year medium term planning instruments, which contain specific policies, programs, and projects, predominantly targeted at wealth creation and poverty reduction. Prior to 2002, Zambia had fragmented national development planning. For instance, the Fourth Development Plan was abruptly abandoned in 1999. However, the re-introduction of national planning in 2002 and the creation of Sector Advisory Groups (SAGs) and the strengthening of the district and provincial planning units enhanced the planning and implementation processes. As a result, there was a Transitional National Development Plan (TNDP) between 2002 and 2005.

The Fifth National Development Plan (FNDP), implemented from 2006 to 2010, heralded the return to more consistent national development planning. The FNDP placed emphasis on diversifying and accelerating economic growth beyond the 6 percent annual average real GDP growth of the 2000s, rural development, and human capital development. The strategic focus of the Plan was "Economic infrastructural and human resources development". The Plan focused on building productive infrastructure for the economy and enhancing social service delivery. The plan identified seven priority public investment areas to accelerate development to better the lives of the people of Zambia whose population was then estimated at 12 million. These priority areas were: agriculture, energy, infrastructure, health, education and skills development, water and sanitation, and public order and safety.

After the expiry of the FNDP came the Sixth National Development Plan (SNDP), themed "Sustained economic growth and poverty reduction", which was to run for the period 2011 to 2015. The SNDP focused on achieving accelerated infrastructure and human development, enhanced economic growth and diversification, and promotion of rural development. However, the Plan was soon revised, following a change of Government in September 2011 and replaced with the Revised Sixth National Development Plan (R-SNDP) for the period 2012 to 2016. This shift was important as it aligned the five-year planning cycles to Zambia's electoral cycles, providing greater buy-in from economic philosophy of the political party in Executive office. The R-SNDP theme was "People Centred Economic Growth and Development". This Plan focused on public capital investments that had a bias to rural development and job creation so as to achieve inclusive growth. The main investment areas were in Skills Development, Science and Technology, Agriculture, Livestock and Fisheries, Energy, and Infrastructure Development particularly transport infrastructure while enhancing human development related Sectors of Water and Sanitation, Education and Health.

The Seventh National Development Plan 7NDP (2017 to 2021) aimed at "Accelerating development efforts towards Vision 2030 without leaving anyone behind". The goal of the Plan was to create a diversified and resilient economy for sustained growth and socio-economic transformation driven, among others, by agriculture. It identified five key strategic development outcomes or pillars, including: Economic Diversification and Job Creation; Poverty and Vulnerability Reduction; Reduced Developmental Inequalities; Enhanced Human Development; and Enhanced Governance Environment for a Diversified and Inclusive Economy.

All these development plans faced similar implementation challenges, ranging from inadequate financing, to delay in costing the plans, poorly costed plans, failure to fully implement the decentralization policy, poor uptake of results, inadequate project appraisal system and weak inter-sectoral coordination and program linkages. In terms of financing, the previous plans were mostly supported through the annual budgets. However, the poor disbursement of funds adversely affected the performance of the plans in relation to implementation.

The current national development plan cycle (2022 to 2026) is governed by the 8NDP and legally, by the Planning and Budgeting Act No.1 of 2020. The implementation timeframe implies that Zambia is one NDP away from the year 2030 when the Vision 2030 ought to have been achieved. The 8NDP was developed in accordance with the National Planning and Budgeting Act No.1 of 2020, which earlier plans did not have the opportunity to refer to. The Act is elaborated on in Chapter 5 of this report.

The 8NDP sets out Zambia's strategic direction, development priorities and implementation strategies for the period 2022-2026. The major thrust of the 8NDP is macroeconomic stability, and fiscal and debt sustainability, to improve the livelihoods of the Zambian people. To achieve this, the Plan outlines a number of reforms including strengthening public finance management (PFM), establishing a fiscal risk management framework and strengthening the legal framework for public private partnerships (PPPs), among others. The policy focus over the Plan period is to improve living standards as well as reduce poverty and inequality by creating conditions for strong and inclusive growth. This is expected to anchored on economic transformation and job creation through the implementation of interventions that foresee enhanced production and productivity in the agriculture, tourism, mining and manufacturing sectors.

Unlike the 7NDP, the 8NDP pre-and-implementation periods are characterized by heightened macroeconomic and fiscal vulnerabilities. The economic challenges have been highlighted in earlier subsections. To adequately respond to these challenges and attain Vision 2030, the Plan is anchored on economic transformation and job creation, human and social development, environmental sustainability, and a good governance environment. The 8NDP also supports Zambia's attainment of several international and regional commitments, including the SDGs. The 8NDP, like the 7NDP, takes cognizance of the SDGs, especially those related to gender equality, decent work and economic growth, and peace, justice, and strong institutions that are seen as key for creating a good governance environment.

The development of the 8NDP is envisaged to be accompanied by a costed implementation plan, the successful execution of which would be supported by a clear understanding of the current and future financing landscape and resource forecasts for the 8NDP. Therefore, by providing a detailed assessment of the development finance and policy landscape, this DFA should be a reliable basis to foster the enhancement of the existing planning, budgeting and financing architecture, including the 8NDP. Ultimately this should result in effective clearing of the path to the Vision 2030.

Strengthening Linkage between Planning and Budgeting

Zambia's national planning framework revolves around the formulation of a five-year strategic plans called NDPs. These Plans are cumulatively financed through annual National Budgets which contain a single year expenditure plan. However, these can be constrained in their formulation by their short-term nature at the expense of longer-term strategic financing. To resolve the disconnect between the National Budgets and the NDPs, a rolling three-year budgetary framework called the MTEF was developed. In 2021, Zambia renamed MTEF to MTBP,[4] broadening the perspective from an expenditure focus to a general budgeting (fiscal revenue, fiscal expenditure and fiscal balances).

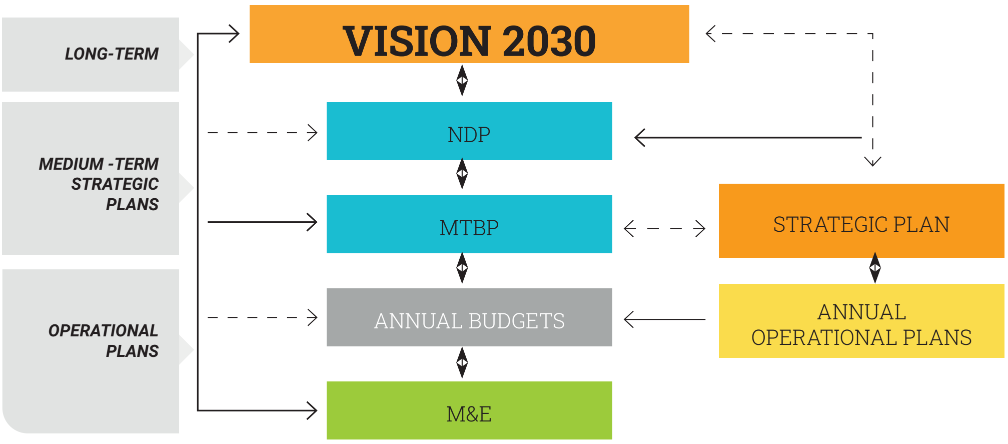
The MTBP, also known as the "Green Paper", sets out the Government's three-year fiscal or budget plans. It includes and guides on the country's medium term revenue mobilization strategy, and synchronizing with a legally prescribed Annual Budgeting Plan. In essence, the MTBP links the country's National Budgets to its social and economic development goals as outlined in its NDPs (Figure 2.2). According to ZIPAR (2022), the MTBP is intended to address the well-known shortcomings of annual budgeting, not least short-sightedness, conservatism and parochialism. In most cases, public programs require multi-year funding

4. Prior to 2021, the MTBP was referred to as the Medium-Term Expenditure Framework (MTEF).

and tend to yield benefits over a period of years, however, annual budgeting largely ignores future costs and benefits. The MTBP resolves these shortcomings by providing multiyear budget planning.

Typically, the approval of the MTBP initiates the annual budgeting cycle. The National Budget, particularly the accompanying Ministerial speech to Parliament by the Finance Minister, is a central policy document that reflects the Government's vision on economic and social development. The National Budget broadly communicates to the public, how the Government intends to utilise public resources to meet its developmental goals. Further, it reflects the Government's ideological commitment and political philosophy, among other things. It also broadly shapes the country's economic priorities. Above all, the National Budget is also subject to constitutional requirements; for example, the Constitution prescribes that the Government can only spend money after it has been authorised to do so by parliament. Figure 2.2 depicts the planning process in Zambia, highlighting the policy frameworks, and their linkages.

Figure 2.2 Planning and Implementation Framework



Source: Ministry of Finance and National Planning

While gains have been recorded in integrating the country's planning frameworks, challenges remain in the overall mobilisation of resources and tracking their utilization, reflecting weaknesses in the existing policy frameworks for resource mobilisation and management. Despite some CSO's acknowledging ZRA's above-target performance in domestic resource mobilisation, a number of them still point to the many challenges the country as a whole continues to face in its efforts to increase domestic resource mobilisation.

2.4 Impediments to Successful Implementation of National Development Plans

Misalignment between NDPs and budgets is a critical factor behind the slow economic growth, persistent and entrenched poverty levels, and overall dismal progress on sustainable development in Zambia. Therefore, examining how well the alignment of development finance flows to NDPs forms an essential ingredient for ensuring successful implementation of the plans. The importance of this cannot be over-emphasized; assessing alignment ensures that: plan priorities are implemented as planned; there is improved transparency in resource allocation; spending agencies are held accountable for their performance; and, reporting procedures to decision makers, Parliament and other stakeholders are followed to raise overall accountability.

Zambia's previous development plans all faced similar implementation challenges. The challenges range from inadequate financing, failure to fully implement the decentralization policy, poor uptake of results, lack of a project appraisal system as well as weak inter-sectoral coordination and program linkages. In terms of financing, the previous plans were mostly supported through the annual budgets however, the poor disbursement of funds adversely affected the performance of these plans. The implementation failures can be partially attributed to misalignment between planning and budgeting.

Additionally, the literature[5] attributes the weak linkages between plans, resources and monitoring in underdeveloped countries to the following factors:

- Numerous plans with separate M&E provisions.
- Insufficient capacity to coordinate and monitor plan implementation..
- Data/statistics gaps for effective monitoring.
- Inappropriate and insufficient indicators for measuring performance; and
- Processes do not have sufficient ownership at all levels.

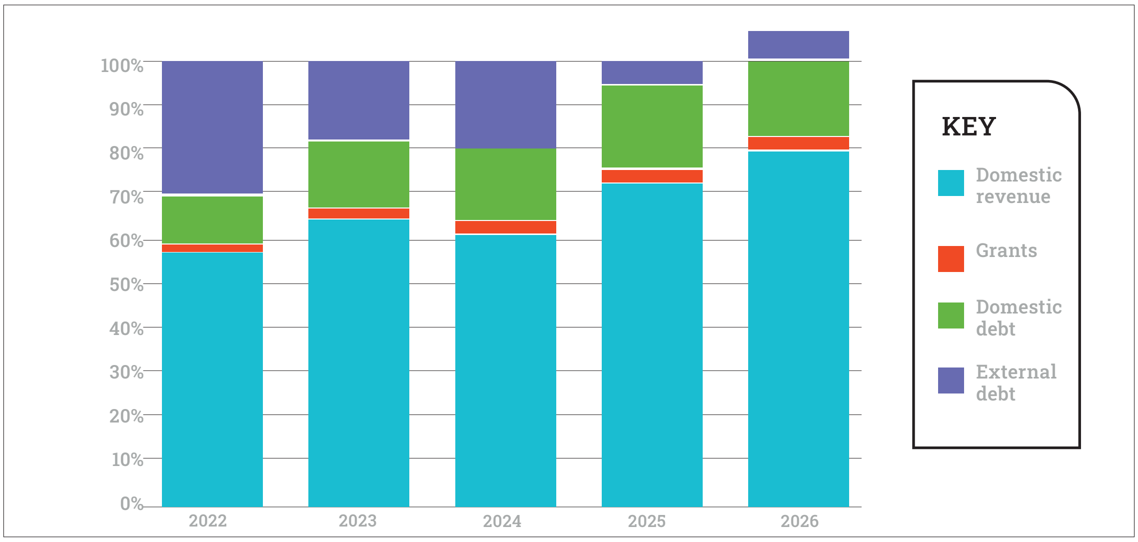
Several of these factors are applicable to Zambia. Specifically, stakeholders bemoaned the lack of complete and timely sectoral and local level plans (Integrated Development Plans (NDPs)), posing serious hindrance to integrated planning and financing.

2.5 Resource Requirements for the 8NDP

Zambia recognizes that implementing the 8NDP and achieving its development goals will require enormous financial resources. As such, a mix of traditional and non-traditional financing sources has been identified to ensure effective and fiscally sustainable implementation of the Plan. Traditional sources of finance include domestic revenues, grants, donations, and concessional loans while alternative sources with low or no interest payments or guarantee commitments from the Government, such as PPPs and impact capital comprise the non-traditional sources. The Government also intends to partner with the private sector and other cooperating partners to finance and implement the 8NDP.

Overall, the Plan will cost an estimated total of K 997.1 billion (approximately US$58.6 billion, at 2022 annual average exchange rate) to be fully implemented, primarily drawing on domestic sources, including revenues (67.3 percent) and domestic borrowing (16.4 percent) (Figure 2.3). The increased reliance on domestic financing flows is in line with Government's commitment to attaining sustainable development while ensuring fiscal sustainability and macroeconomic stability.

Figure 2.3 : Resource Requirements for the 8NDP



Source: Authors' Adaptations from the 8NDP

5. Sanjesh Naidu (2018): Alignment of National Planning and Government Expenditure (Budgets) Linkages to Support Implementation of Sustainable Development Agenda & Support Monitoring and Reporting.

03

Chapter 3: Assessment of the Development Financing Landscape

This section analyzes trends in Zambia's resource envelope, overall development finance and major development finance flows by category: domestic public finance, domestic private finance, international public finance, and international private finance.

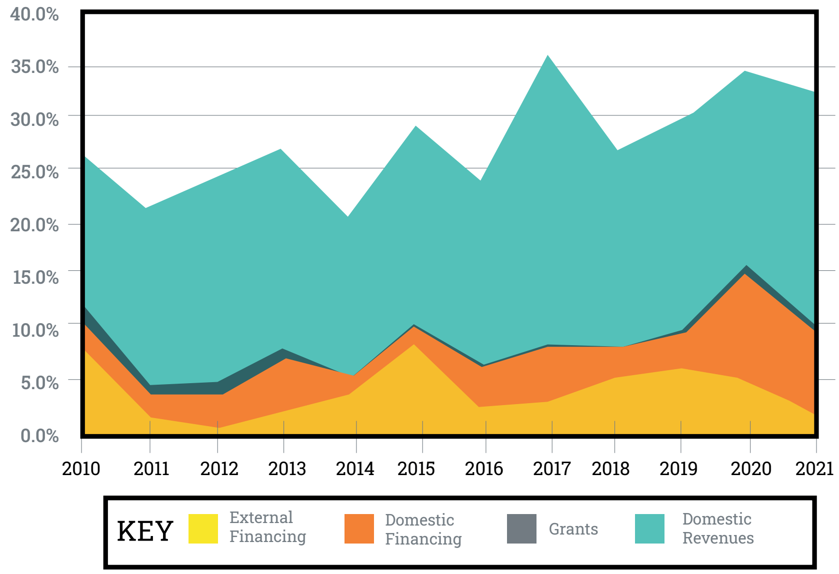
3.1 Assessing Zambia's Resource Pool

3.1.1 Overall Resource Pool for Zambia

As earlier alluded to, Zambia draws its financing from a combination of sources, which include: domestic revenues (tax revenues; non-tax revenues); borrowing from the domestic securities market; borrowing from external markets; and foreign grants. Successful implementation of the Government's priorities under the NDPs, which ultimately lead to the Vision 2030, crucially depends on the efficient mobilization of the sources and prudent expenditure. In relation to this DFA, development finance for Zambia comprises domestic and external finance. The domestic sources are further split between public and private finance. Similarly, external financing includes private and public sources. (See figure 3.1: Zambia's resource envelope).

Over the period 2010 to 2021, domestic revenues (tax and non-tax) had hovered around 19.2 percent of GDP. On the other hand, due to Government's expansionary fiscal stance, expenditures had continued to outstrip revenues, resulting in widening and persistent fiscal deficits. In order to finance the deficit, the Government was forced to continue borrowing from the domestic and foreign markets. Consequently, domestic financing almost doubled from 2.6 percent of GDP over 2010 to 2015 to 5.1 percent over from 2016 to 2021. The rise in domestic debt was largely on account of declined external financing that reduced from 8 percent of GDP in 2010 to 1.3 percent of GDP in 2021. This sharp decline in external financing was mainly on account of the IMF and World Bank classifying Zambia's debt as unsustainable and ensuing negative sentiments from the international community, including foreign investors. Exacerbated by the Covid-19 pandemic, the nation had to rely more on domestic sources. There have also been concerted Government efforts to promote fiscal sustainability through enhanced domestic revenue mobilization. Grants had also stagnated, accounting for a paltry average of 0.6 percent of GDP over the period, more so declining from 1.8 percent of GDP in 2010 to 0.6 percent of GDP in 2021.

Figure 3.1: Zambia's resource envelope



Source: MoFNP Fiscal Tables & Economic Reports

3.1.2 Overall Trends in Development Finance Flows

As a share of the total resource envelope, domestic public finance declined from 41.7 percent for 2010-2014 to an average of 33.2 percent over 2015-2019. Over the same period, international public finance increased from 37.6 percent to 54.9 percent, suggesting that Zambia has been heavily dependent on external financing to bridge its funding gaps.

International private finance (mostly FDI) on the other hand has been on a downward streak since 2010, with its share in total financing dropping to 5.1 percent over 2015-2019 from 16.1 percent during the period 2010 to 2014. Overall, FDI accounted for 7.6 percent of development finance on average.The slow FDI inflows can be attributed to the instabilities in policies predominantly surrounding the tax regime in the mining sector, and the weaker macroeconomic environment that characterized Zambia over the past decade.

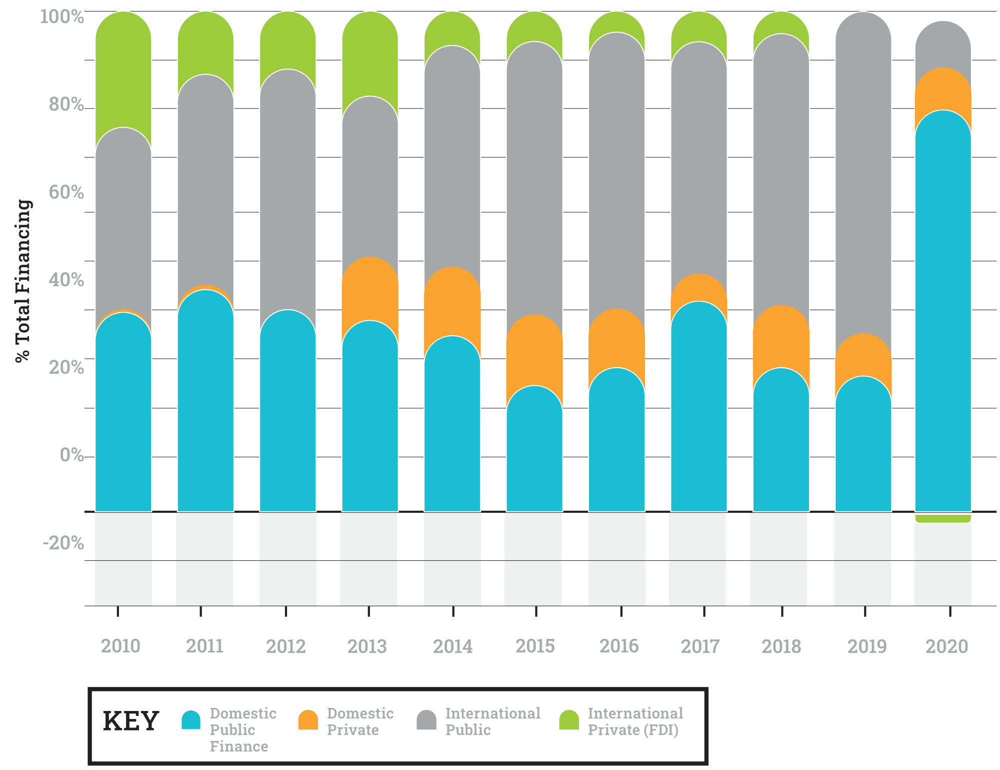
Zambia has also increasingly sought domestic private sources to mobilize development finance. However, domestic private finance (proxied by private investment), has stagnated for the most part, averaging 3.7 percent of GDP between 2010 and 2020.

Moreover, the debt crisis and COVID-19 pandemic effects significantly altered the development finance landscape, making domestic sources (public and private) dominate the financing landscape (Figure 3.1). Consequently, in 2020, the share of domestic public finance in the total resource pool drastically increased to 78.6 percent from 30.9 percent in 2019. During the same period, international public finance plummeted to 13.2 percent in 2020 from 59.2 percent in 2019. Despite this, international public finance edged domestic public finance, accounting for an average of 47.7 percent of the total development finance envelope compared to 43.2 percent domestic public finance. These results suggest that Government must do more to enhance domestic resource mobilization and explore cheaper and innovative financing sources.

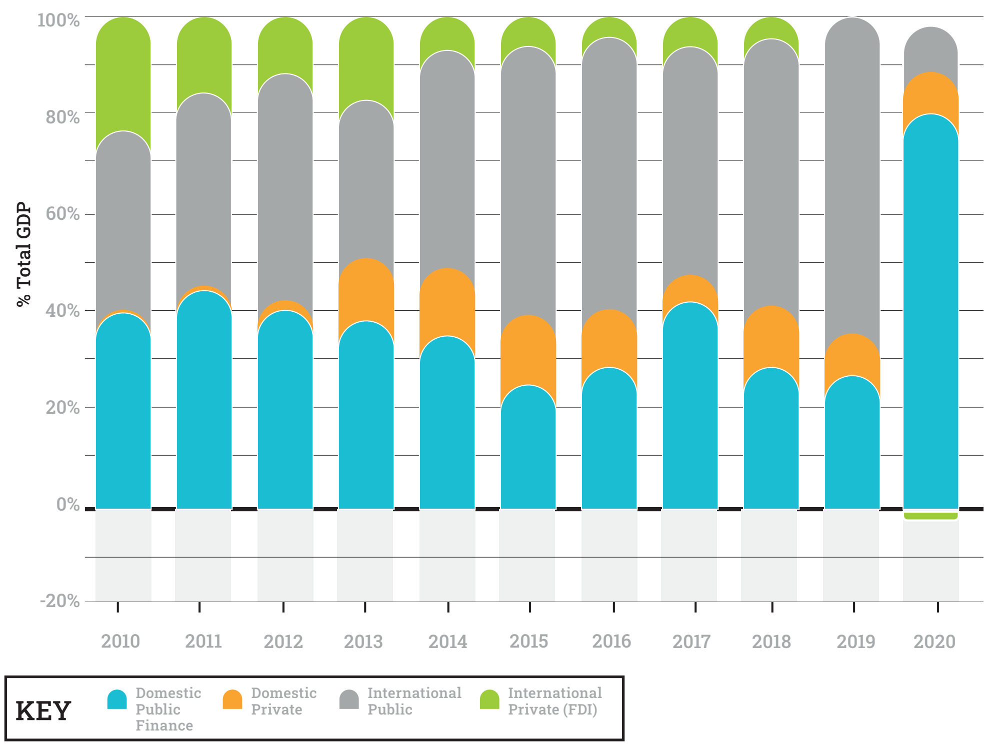
A similar pattern is observed when these flows are expressed as shares of GDP (Panel B). While the share of domestic public finance in GDP has been steadily increasing over the years, it still trailed international public finance which accounted for 26.5 percent of GDP (on average) from 2010 to 2020. Public finance followed in second place, accounting for 22.4 percent of GDP, while international private finance and domestic private kept a distant third and fourth slots, respectively. These observations suggest that public sources of finance dominate the development finance landscape for Zambia, and that the country has been running significant financing gaps.

Figure 3.2 Composition of Development Finance

Panel A: Composition of Development Finance (Share in Total Development Finance)



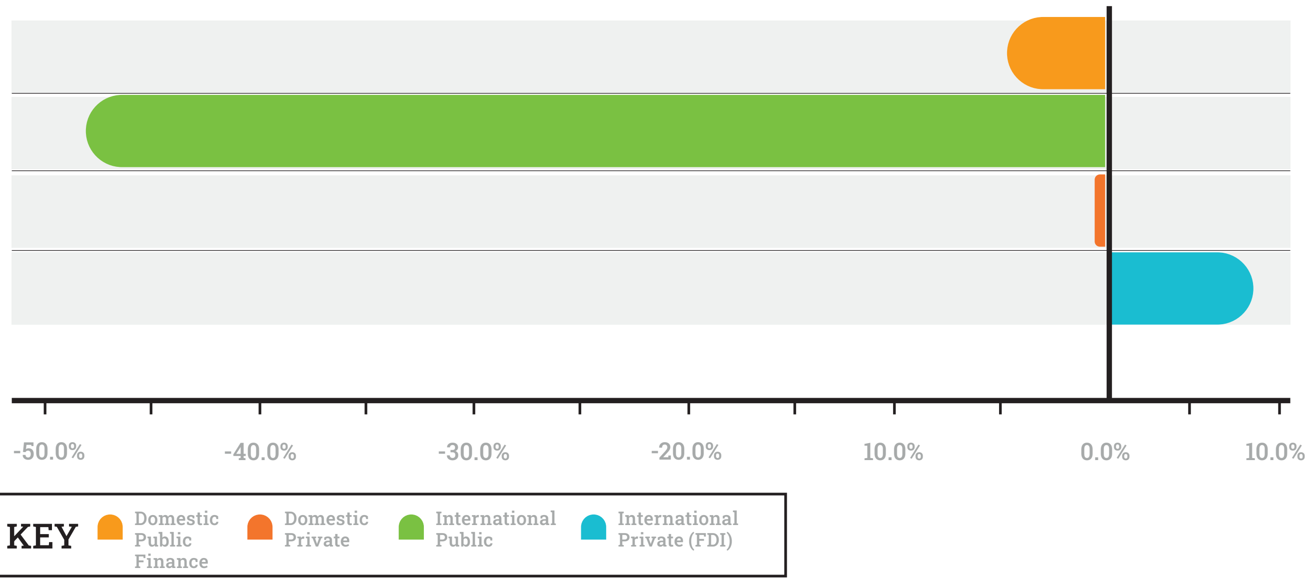
Panel B: Share in GDP



Source: Authors construction from MoFNP Annual reports and other sources

Zambia suffered significant reductions in international finance due to COVID-19 and the consequences of debt distress (Figure 3.2). This suggests that international flows are highly susceptible to global shocks and sentiments, making them an unsustainable source of development finance.

Figure 3.3: Change in Development Finance between (2019 and 2020)



Source: MoFNP (Fiscal Tables, Annual Economic Reports)

3.1.3 Key Takeaways

The following are the main takeaway points from the foregoing

- While Zambia's domestic revenues and grants have only averaged 19 percent of GDP between 2016 and 2021, the country seeks to increase it's domestic revenues and grants to 22 percent of GDP by 2025.
- Zambia has heavily relied on domestic financing and external financing to bridge the financing gaps, triggering a fiscal crisis.
- The stagnation in grants in part contributed to the reliance on expensive sources of development finance, including debt.
- International public finance accounts for the bulk of development financing, but shocks such as the COVID-19 pandemic and fiscal crisis have exposed its vulnerability.
- Domestic public finance increased in importance especially during the global shocks (COVID-19 pandemic)
- The share of domestic private finance remained largely unexplored, indicating possible constraints in harnessing private domestic sources.
- Data gaps limited this DFA analysis to flows for which data is available.

3.2 Domestic Public Finance

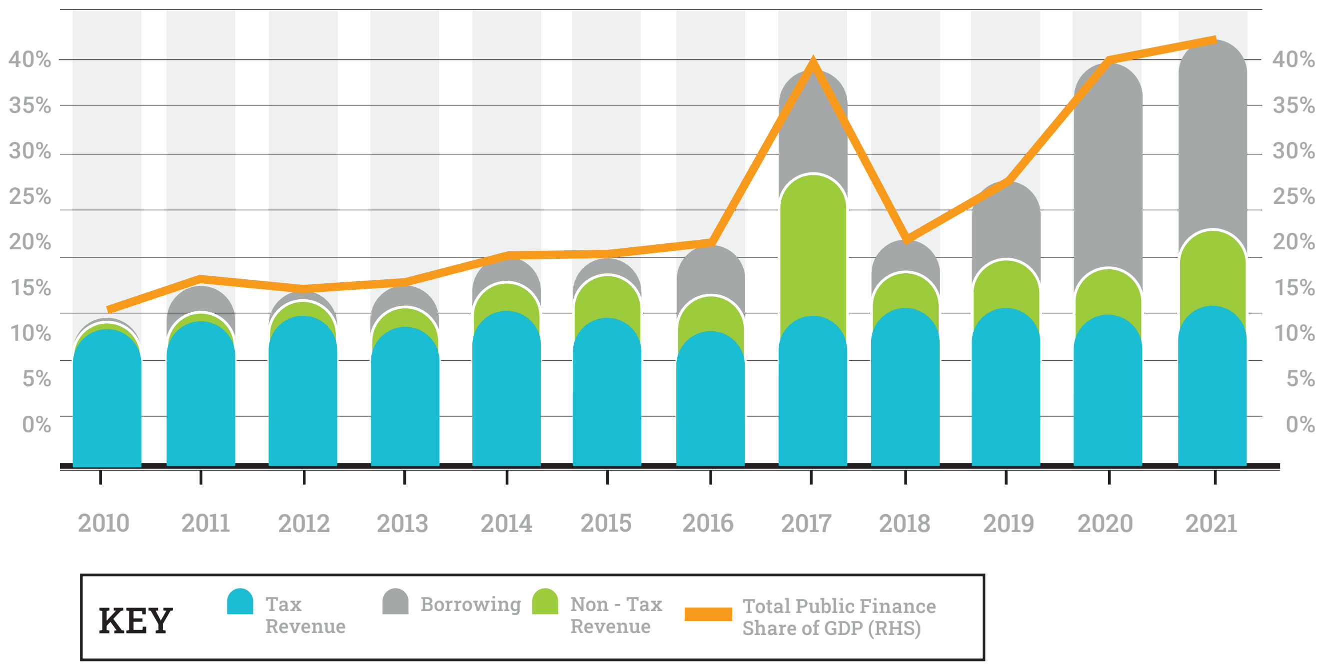
3.2.1 Composition of Domestic Public Finance

Domestic public finance comprises of government revenue (tax and non-tax revenues including revenues from SOEs and government borrowing (government securities) from domestic sources. As a share of GDP, domestic public finance stagnated over the period 2010 to 2021, averaging 23.7 percent.

A decomposition of domestic public finance by type reveals that although tax revenue has stagnated over the years, it still constitutes the largest share of domestic public finance (14.8 percent). However, public debt took up an increasingly crucial role after 2019 when the country embarked on an expansionary fiscal stance, culminating in the rapid accumulation of debt (Figure 3.4). The resulting increased reliance on debt, including expensive private commercial loans could explain why Zambia has been underperforming, compared its peers, in tax revenue mobilization.

Further non-tax revenues had remained sluggish over the period (2010 to 2021), reflecting narrow base and weak policy frameworks.

Figure 3.4: Main Sources of Revenue (% GDP)



Source: BoZ and MoFNP Annual Reports

Tax Revenues

The Zambia tax system consists of three major tax categories: Income taxes; Value Added Tax (VAT); and Customs and Excise taxes. Other taxes include insurance premiums and export duties. Income tax comprises Company Income Tax (CIT), Pay-As-You-Earn (PAYE), and Withholding tax.

Although Zambia has made several reforms aimed at boosting its tax revenues, its tax collections lag its peers in the SADC region. Between 2010 and 2019, Zambia's tax-GDP ratio averaged 14.9 percent, way below the SADC average of 20.2 percent (Figure 3.4). A combination of factors, including lackluster economic growth, high informal sector, revenue leakages, weak governance systems, and external shocks, could explain the underperformance in revenue mobilization. For instance, tax revenues declined from an average of 16 percent over 2018-2019 to less than 15 percent in 2020 when the COVID-19 pandemic struck.

Additionally, poorly designed tax incentives and illicit financial flows (IFFs) are a drain on domestic revenues. In the 2022 Budget for example, tax incentives reduced total revenues by 5.9 percent while losses through IFFs accounted for about 14 percent of tax revenue in 2018. A detailed discussion of impediments to effective revenue mobilization, including IFFs, is provided in Chapter 5.

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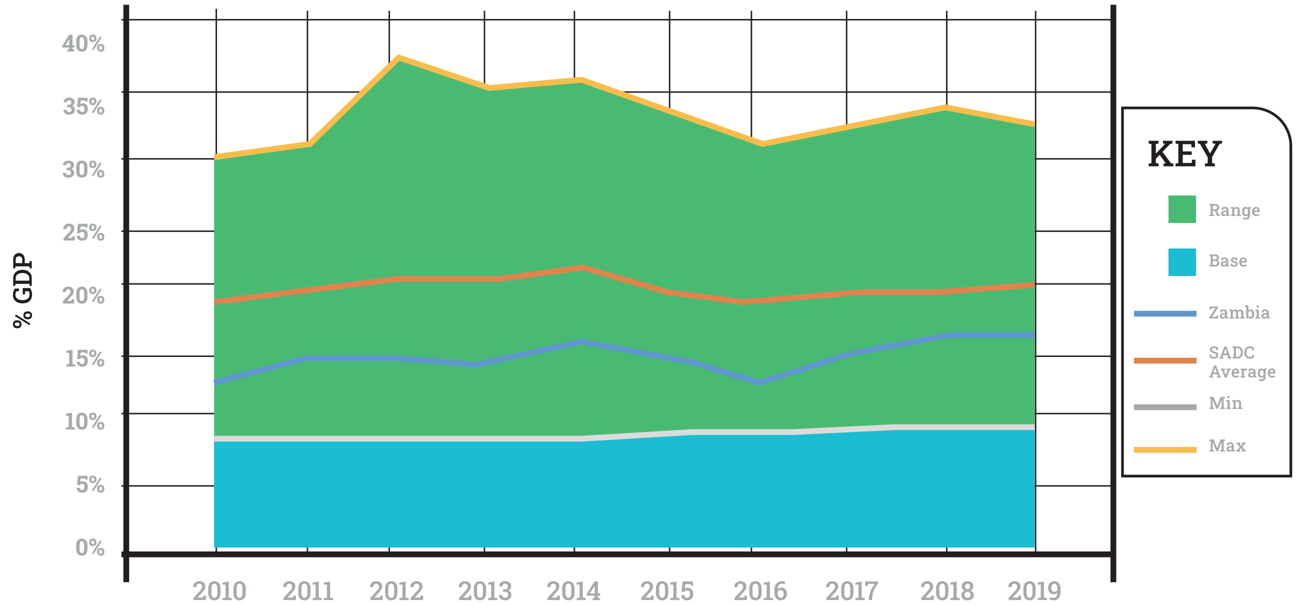
Figure 3.5: Zambia's Tax Collections Relative to SADC

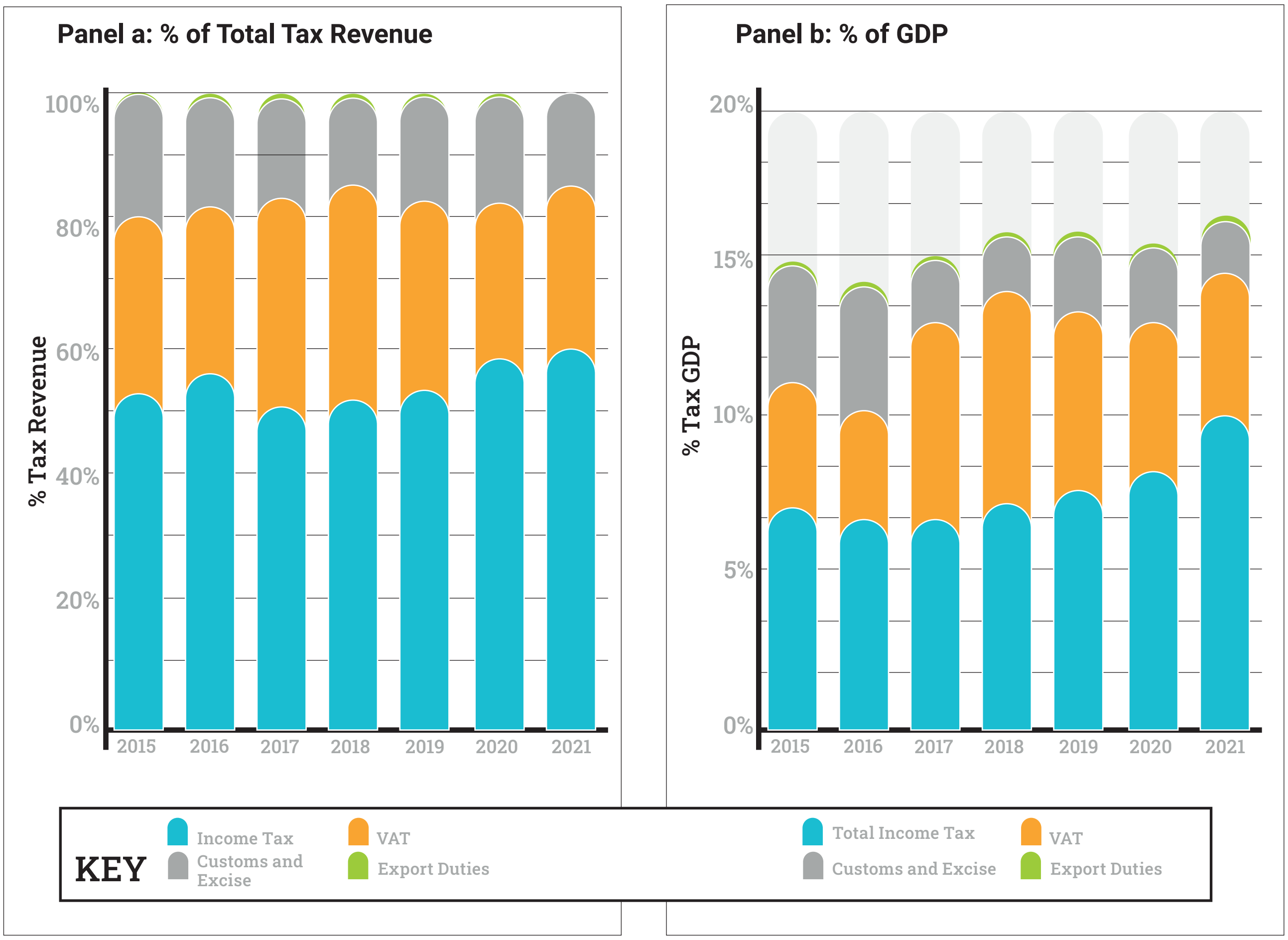


Source: World Development Indicators

Income taxes dominate the Zambian tax mix, accounting for slightly over half (51 percent) of tax revenues and 7.7 percent of GDP from 2015 to 2021 (Figure 3.5). The main drivers of income taxes are CIT and PAYE, which have benefited from the aggressive compliance measures and reforms instituted by Government and ZRA over the years. Key reforms include the expanded use of Information, Communications and Telecommunications (ICT), and moves toward a competitive mining fiscal regime by introducing non-deductibility of mineral royalties, among others. It is worth noting that the mining sector is a pivotal contributor to tax revenues. For instance, extractive royalties contributed about 1.7 percent to GDP. The reliance on extractive revenues poses severe risks to fiscal sustainability due to the exposure to global shocks. Thus, fluctuations in mining productivity and mineral prices on the international market significantly impact Zambia's fiscal health.

Value Added Tax is the second largest contributor to tax revenues. From 2015 to 2021, the share of VAT in total tax revenue and GDP averaged 32.5 percent and 4.9 percent, respectively. Additionally, reforms such as the appointment of withholding agents and the introduction of electronic fiscal devices for VAT-registered suppliers contributed to the growth in VAT.

Figure 3.6: Composition of Tax Revenue (Share in total tax revenue & GDP)



Source: Constructed from MoFNP Annual reports

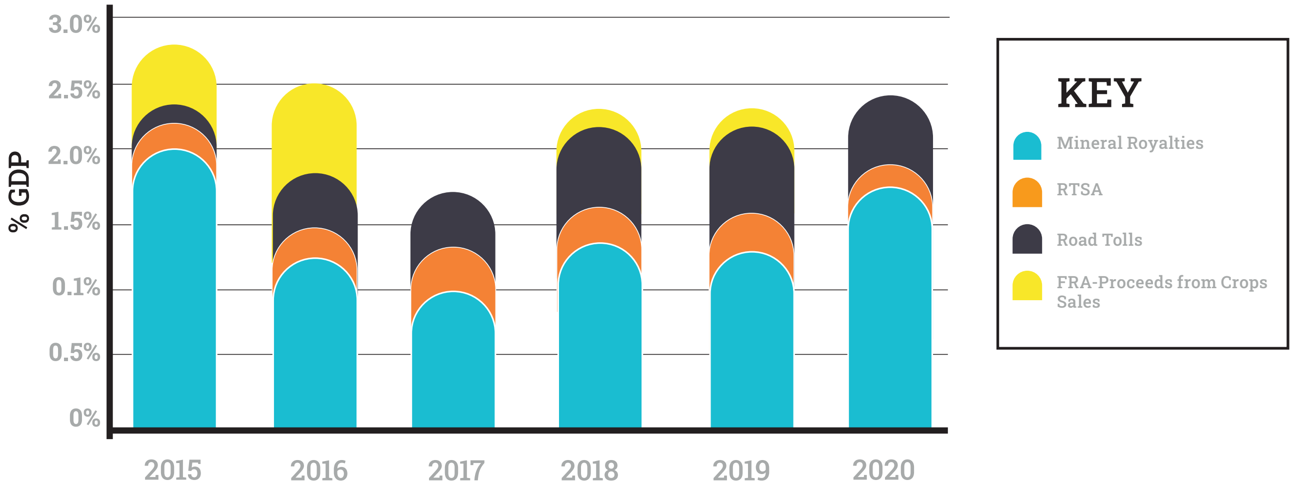
Non-Tax Revenues

In Zambia, non-tax revenues are collected from various sources, and such include Mineral Royalty Tax (MRT), fees and charges in exchange for various services or benefits provided by Government, fines and penalties on offences. Non-tax revenues stagnated at 3.8 percent of GDP per year (on average) over the period 2015 to 2020.

Mineral royalty has commanded the lion's share of the non-tax revenues, despite the instability in the mining tax regime. Over the period 2015 – 2020, mineral royalty collections averaged 1.5 percent of GDP. Mineral royalty performance peaked at 1.6 percent of GDP in 2020, and this was on account of an increase in the copper price on the London Metal Exchange (LME) from US$6,049 per metric ton in January 2020 to US$7,755 per metric ton in December 2020.

Road Tolls followed in distant second place averaging 0.4 percent of GDP over the same period. The rest of the components remained stagnant over the reference period, hovering around 0.2 percent of GDP.

Figure 3.7: Non-Tax Revenue Collection as a percent of GDP, (2015 - 2020)



Source: MoF Fiscal Tables

The stagnation in total non-tax revenues over the reference period is mainly on account of the lower collections from the Road Transport and Safety Agency (RTSA), poor recoveries from the Farmer Input Support Program (FISP), and low proceeds from crop sales (Table 3.2.1).

However, MRT collections bolstered non-tax revenues due to high international copper prices over most of the reference period (2015 to 2021). For instance, the copper price on the London Metal Exchange (LME) increased from US$6,049 per metric tonne in January 2020 to US$ 7,755 in December 2020. This copper price boom explains the over-collection of MRT by 8.7 percent in 2020. Road toll collections had also contributed to non-tax revenues, notably in 2018 and 2019, when they over performed by 91 percent and 83 percent, respectively. According to the National Road Fund Agency (NRFA), tolls revenue increased by 25 percent to K1.5 billion in 2020 from K1.2 billion in 2019. This growth in tolls revenue was despite the challenges caused by the COVID-19 pandemic.

Table 3.2.1 Budget variances of specific Non-tax Revenues, (2015 - 2021)

	2015	2016	2017	2018	2019	2020	2021
RTSA	-14%	-14%	-49%	-53%	-27%	-	-4%
FISP Recoveries	-78%	-98%	-91%	-100%	-	-	
FRA – Proceeds from Crop sales	45%	66%	-92%	230%	-15%	-85%	-88%
Mineral Royalties	-37%	6%	29%	12%	-12.6%	8.7%	118%
Road Tolls	2%	27%	61%	91%	83.1%	-5.1%	37%

Source: Constructed from MoFNP Fiscal Tables

Domestic Borrowing

Treasury bills (T-bills)—which was short term borrowings of less than a year and issued at a discount— and Government bonds that span from 2 years to 15 years with semi-annual coupon payments are the primary domestic financing sources for the Government. In cases where domestic financing is insufficient, domestic arrears arise to ease the financing constraint.[6]

During the period 2015-2021, Government bonds dominated the domestic debt profile, accounting for approximately half of the portfolio as shown Table 3.2.2. In view of limited external financing, the fiscal authorities increased the issuance of government securities by increasing the size of T-bills and frequency

6. These relate to amounts owed to suppliers of goods and services, unremitted pension contributions, and payments towards litigations and compensations.

of auctions for Government Bonds from quarterly to every two months. Consequently, domestic debt stood at K203.4 billion by the end of December 2021[7]. Further, total government securities grew at 42.8 percent per annum over 2015 to 2021 from K24.09 million to K203.34 million, reflecting government's increased reliance on domestic financing (Table 3.2.2).

Table 3.2.2: Domestic Debt, 2015 – 2021(K'000)

	2015	2016	2017	2018	2019	2020	2021
Treasury Bills	12,090.10	13,174.21	20,193.51	18,468.06	20,883.23	33,009.33	37,800.23
Government Bonds	12,612.79	19,809.36	28,165.70	39,792.91	59,371.44	97,205.36	165,500.56
Total Government Securities	24,702.89	32,983.57	48,359.21	58,260.97	80,234.73	130,214.69	203,356.88

Source: MoFNP Annual Economic Reports

The rise in domestic debt stock has translated into colossal debt service costs, contributing to the fiscal crisis Zambia has been experiencing in the recent past. For instance, domestic debt service increased from K4.1 billion in 2015 to K25.4 billion in 2021, representing an average annual growth rate of 43.8 percent. Additionally, the share of domestic debt service in domestic revenues more than doubled between 2015 and 2021, increasing from 12.2 percent to 26.3 percent. This means that in 2021, the Government was spending K26 towards debt service for every K100 it collected from domestic sources.

Table 3.2.3 Domestic Debt Service, 2015 – 2021 (K'Million)

	2015	2016	2017	2018	2019	2020	2021
Interest Payments	3,264.60	4,024.90	5,045.20	7,414.10	9,025.80	14,496.10	24,929.50
Amortisation	879.30	4,696.70	476.90	2,082.60	3,016.10	2,791.00	463.10
Total Domestic Debt Service	4,143.90	8,721.60	5,522.10	9,496.70	12,041.90	17,287.10	25,392.60

Source: MoFNP Fiscal Tables

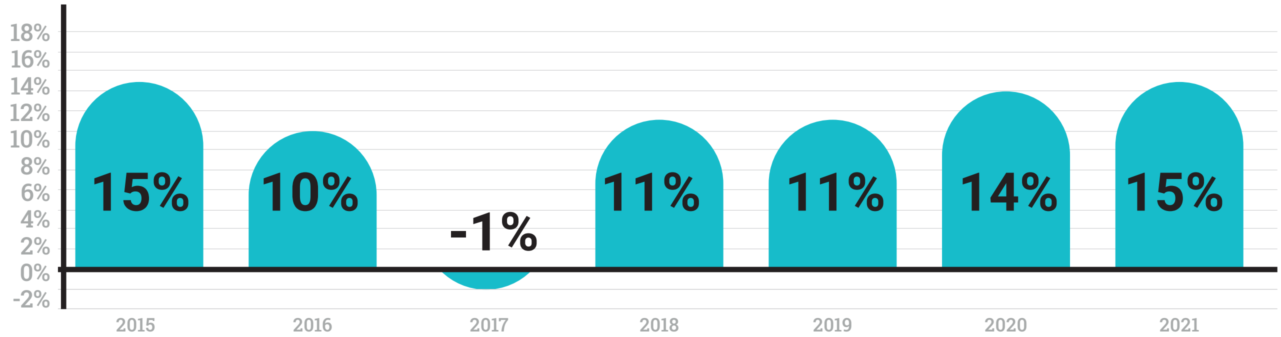
3.2.2 Public Expenditure

Since 2010, Zambia's expenditure patterns have been characterized by higher than planned expenditures. This has been largely on account of capital spending. As a result, social and other critical spending were crowded out as a disproportionate amount of the budget was spent on debt servicing. The fiscal mismanagement explains why fiscal deficits continued widening despite the improved revenue performance.

Figure 3.8 shows that over the period 2015 to 2021, expenditure patterns fell by one percent in 2017, and the other years of over expenditure in 2015 (15 percent), 2016 (10 percent), 2018 (11 percent), 2019 (11 percent), 2020 (14 percent) and 2021 (15 percent). The largest expenditures occurred in 2015 and 2021, fueling fiscal and macroeconomic instabilities. In 2015, the country experienced a mini economic crisis that was caused by the fall in copper prices, electricity deficits, and macroeconomic instability. In addition, the issuance of the US$1.25 billion Eurobond in 2015 and other borrowings, significantly increased debt servicing costs from US$185.3 million in 2014 to US$309.4 million in 2015. It's worth noting that the high expenditures in 2021, were driven by general elections, and fiscal slippages from programs such as the Farmer Input Support Programmes (FISP) which was above budget by 80 percent.

7. MOF. (2022). 2022 -2024 Medium Term Budget Plan. Lusaka : MOF

Figure 3.8: Variance between planned and actual budget, (2015 - 2021)

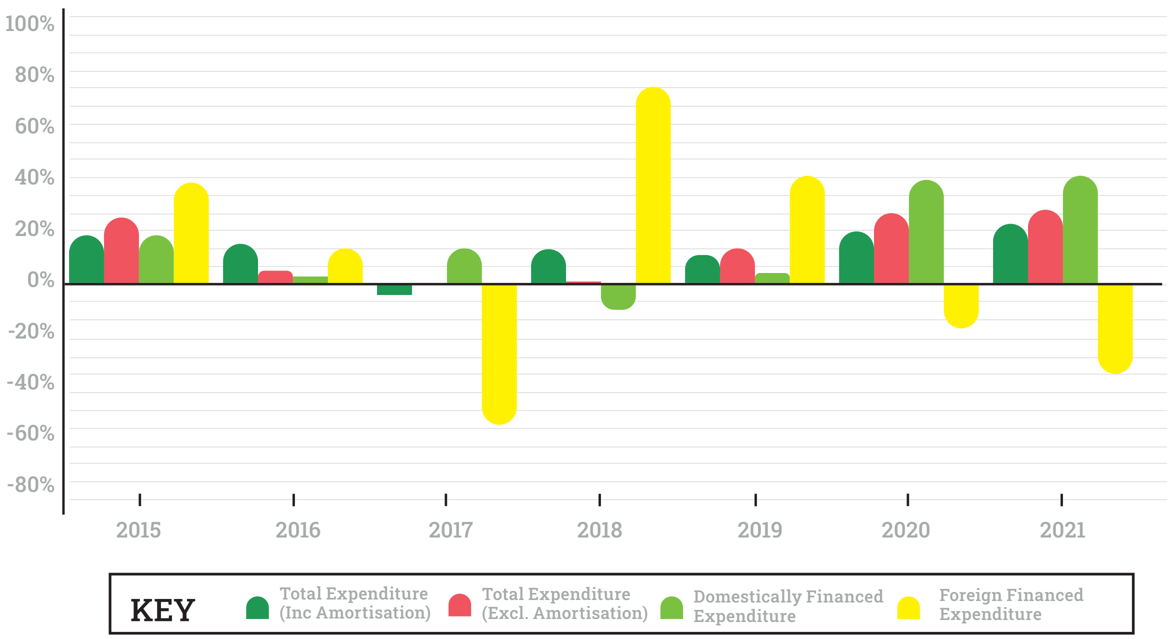


Source: MoFNP Fiscal Tables

In fiscal frameworks total expenditure is typically measured or presented with or without amortization[8]. The MoFNP Fiscal Tables, categorize total expenditure without amortization by source of expenditure (domestic or foreign financed) and or by operational classification (recurrent vs capital expenditure).

During the period 2015 – 2021, foreign-financed expenditure was more volatile than domestic-financed expenditure, suggestive of unsustainability of external sources. The high volatility on foreign financed expenditure was largely on account of huge project disbursements in 2018, which were above target by 83 percent (Figure 3.9).

Figure 3.9: Variance between Planned and Actual Domestically and Foreign-Financed Expenditure, (2015 - 2021)



Source: MOFNP Fiscal Tables

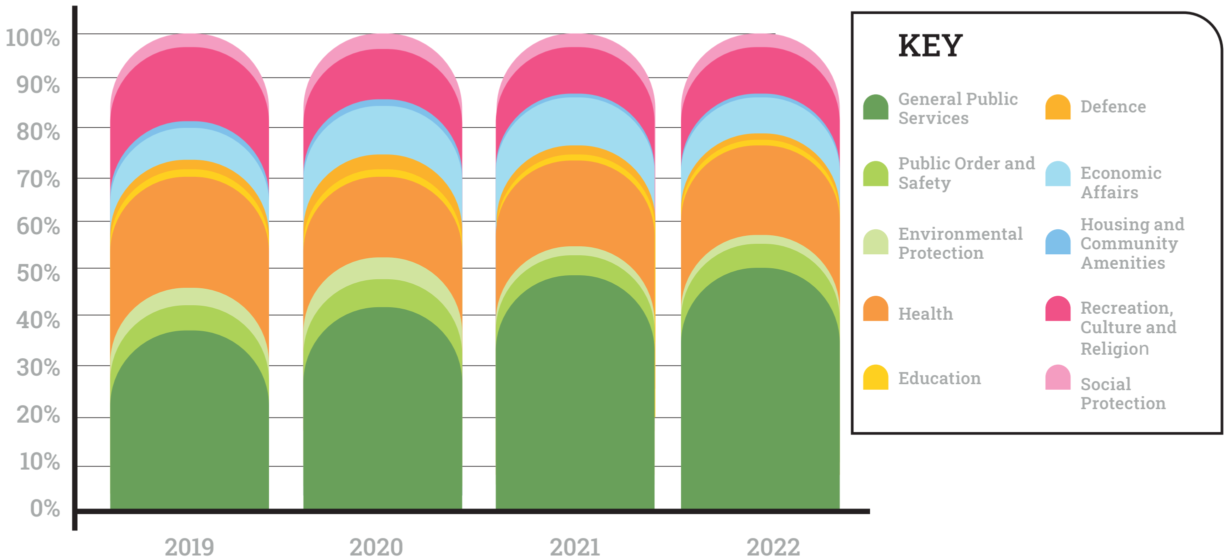
Regarding functional classification, general public services accounted for the largest share of the budget, averaging 43.9 percent (Figure 3.10). General public services have also been on an upward trajectory, increasing by 40.5 percent per annum, from K31.3 billion in 2019 to K86.4 billion in 2022. The growth in allocations towards general public services was primarily because of increased debt servicing costs stemming from the large debt stock.

8. Amortisation is the payment on principal debt

The fiscal authorities have also made deliberate moves to direct resources towards growth sectors such as agriculture, as shown by the steady increase in allocations to economic affairs, which accounted for 20.4 percent of the budget (on average).

Allocations to social sectors have also been on an upward trajectory. For example, the budgetary allocation to the health sector increased by 44.8 percent between 2021 and 2022, mainly due to the Government commitment to procuring vaccines and the recruitment of 11,200 health workers. Similarly, the budgetary allocation to the education sector increased by 31.2 percent, from K13.8 billion in 2021 to K18.1 billion in 2022, mainly on account of the planned recruitment of 30,000 teachers. However, when analysed as shares of total budget, social sector spending has stagnated for most of the reference sub-period 2019 to 2021.

Figure 3.10: Budget allocation in relation to other functional spending (% of Budget)



Source: MoFNP Annual Budget Speeches

From an operational classification perspective, total expenditure excluding amortization is classified into recurrent and capital expenditure. Recurrent expenditure which was above budget during 2014-2016, was within budget in 2017 and under budget in 2018. This was primarily due to reductions in spending in all recurrent expenditure other than interest payments on debt. However, during the period 2019-2021, recurrent expenditure was above target by 15 percent on average, and this was on account of increased spending in recurrent expenditure as shown in Table 3.2.4.

Interest payments were above target in 2015 (52 percent), 2016 (5 percent), 2017 (17 percent), 2018 (24 percent) and 2019 (27 percent), and this was attributed to huge disbursements on external debt to finance costly capital projects as reflected by the positive variances under non-financial assets. However, in 2020 and 2021 interest payments were below budget by 5 percent and 6 percent respectively, and this was primarily due to the default on Zambia's Eurobond and the Debt Service Suspension Initiative (DSSI) under the G20 Common Framework.

Table 3.2.4 Variance between planned and actual decomposed expenditure, (2015 - 2021)

	2015	2016	2017	2018	2019	2020	2021
Recurrent Expenditure	5%	7%	-2%	-5%	4%	20%	21%
Personal Emoluments	-3%	-8%	0%	-5%	-9%	5%	12%
Use Of Goods And Services	-18 %	-4 %	-14 %	-23 %	-13 %	43 %	113 %
Interest Payments	52 %	5 %	17 %	24 %	27 %	-5 %	-6 %
Grants And Other Payments	79 %	78 %	-10 %	-8 %	50 %	113 %	49 %
Social Benefits	-17 %	-53 %	-20 %	-46 %	-87 %	24 %	34 %
Non-Financial Assets	21 %	-7 %	9 %	63 %	39 %	2 %	6 %
Financial Assets	-31 %	-78%	54%	-86%	-99%	231%	454%
Liabilities	17%	-2%	-6%	-67%	51%	216%	71%

Source: MoFNP Fiscal Tables

3.2.3 Key Takeaways

The following were the key takeaway points from the foregoing:

- Fiscal space has been constricted by huge debt servicing costs, narrowing Zambia's financing options, and adversely impacting social sector spending and investment in growth sectors.
- Zambia's tax performance is far behind the SADC tax-GDP ratio. Between 2016 and 2020, the tax-to-GDP ratio averaged 15 percent, below the country's own target of 18 percent. However, non-tax revenues have stagnated for the most part.
- Non-tax revenue has stagnated over the years. Although mineral royalties performed relatively well in the recent past, other components such as FRA proceeds from crop sales have been a drag on the revenue collections.
- Mining sector performance is crucial to revenue mobilization. Zambia continues to heavily rely on extractive taxes for its revenue, posing threats to attainment of fiscal sustainability as mining tends to be susceptible to shocks.

3.3 Domestic Private Finance

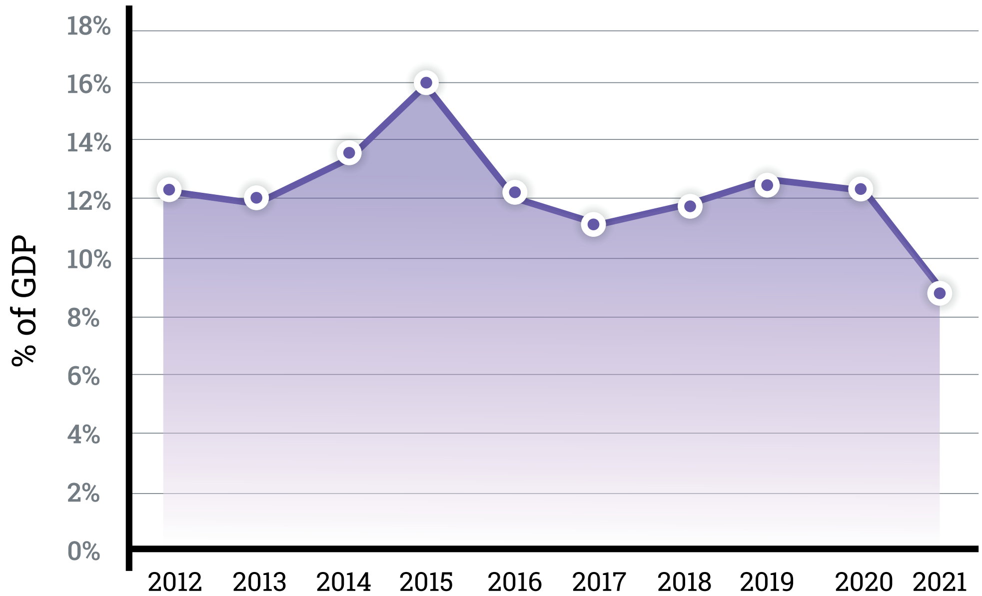
Domestic private finance includes commercial bank loans, non-bank credit, private investment; microfinance, corporate bonds; institutional investments (insurance, pensions), foundations, flows from NGOs, CSOs, and private firms' corporate social responsibility activities.

3.3.1 Private Investment

Private Sector Credit

Adequate and affordable financing is critical for the private sector to actively and effectively participate in Zambia's economic development. However, the flow of financial resources to the private sector has remained relatively stagnant and has been in decline since 2015. For instance, the share of private sector credit in GDP declined from 15.7 percent in 2015 to 12.1 percent in 2016. Since then, the private sector-to-GDP ratio has stagnated, averaging 11.5 percent of GDP between 2016 and 2021. Additionally, the sharp drop in private sector credit between 2020 and 2021 can be attributed to the exacerbating effects of the COVID-19 pandemic. The trends in private sector credit are suggestive of the crowding out effects from excessive government borrowing spurred by excessive public spending.

Figure 3.11 Domestic Private Sector Credit (2012 – 2021; % of GDP)

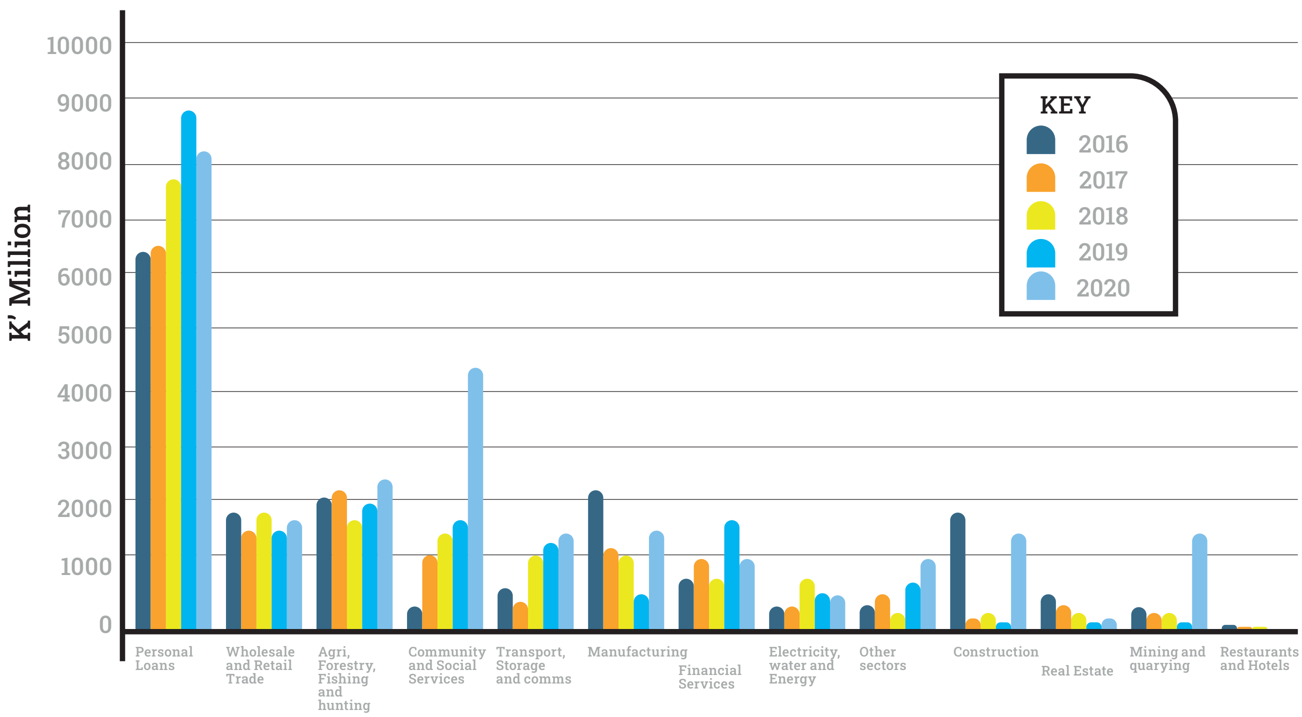


Source: Authors' construction using Bank of Zambia data

Private Sector Investment

Private investment proxied by domestic credit has not seen much growth since 2016. Personal loans remain the most dominant form of credit. However, in terms of the actual sectors that received credit, the wholesale and retail trade sector, agriculture, fishing and hunting, community and social services and transport, storage and communications were the most dominant sectors in terms of domestic credit (Figure 3.12).

Figure 3.12 Domestic Credit to the Private sector



Source: Authors' construction using BoZ Annual reports

The sectors highlighted in Figure 3.12 are partially aligned to Zambia's priority sectors as espoused in the 8NDP. Under the pillar on Economic Transformation and job creation, the 8NDP outlines four priority sectors and seeks to increase agricultural production and productivity, promote mining of traditional and non-traditional minerals, and promote value addition in manufacturing as well as stimulating tourism growth.

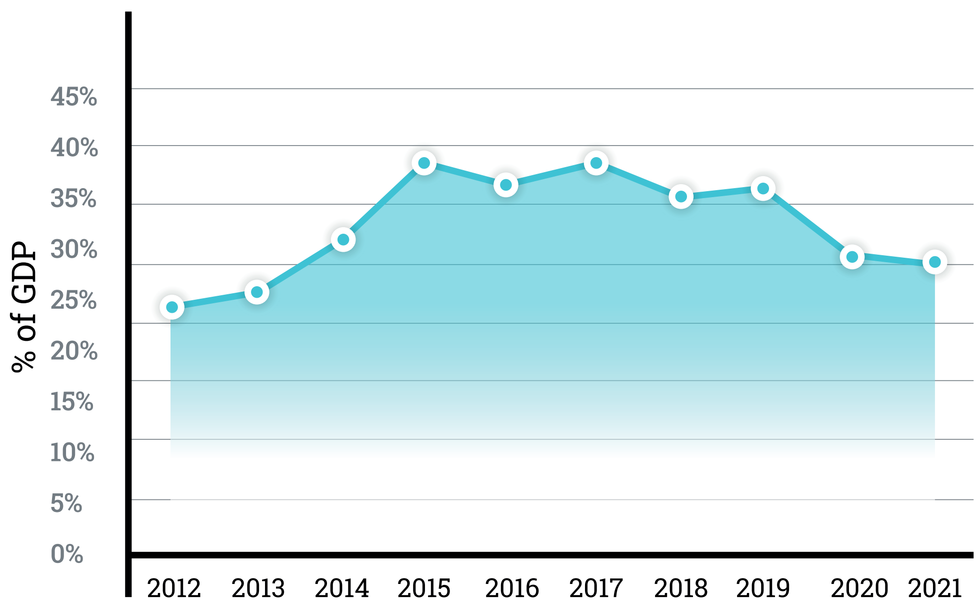
From the foregoing analysis on the profile of domestic credit to the private sector which is dominated by personal loans, the prospects for attaining the country's goals in the 8NDP will remain weak considering the low levels of credit to priority sectors such as manufacturing and tourism. While the Agriculture sector averaged almost the same level of credit as the wholesale and retail sector, this remains low when compared to the share of personal loans. For a country that seeks to transform its economy and create jobs, one would expect a higher share of credit allocated to the growth sectors as opposed to personal loans which, from anecdotal data, are mostly used for consumption as opposed to supporting real sector growth. This raises further concerns on the country's prospects to attain the SDGs 8 and 9 which speak to decent work and economic growth as well as industry innovation and infrastructure. To this end, most of the progress with respect to these two goals has been spearheaded by the public sector with significant investments in infrastructure specifically roads, airports, energy, health and education facilities. However, these investments (some inefficient) have led to a debt burden for the country. The banking sector would therefore be an alternative form of finance specifically to support the growth of the real sector through provision of credit thereby increasing Zambia's prospects for attaining the SDGs relating to economic growth, job creation and infrastructure development.

Investment in Capital Goods

Gross fixed capital formation (GFCF) refers to the acquisition of produced assets (plus purchases of second-hand assets), including the production of such assets by producers for their own use, minus disposals. The relevant assets relate to assets that are intended for use in the production of other goods and services for a period of more than a year. This variable is important because it is indicative of the level of investment in fixed assets taking place in the country. By extension, it gives us an idea of the amount of credit to the private sector specifically for investment in productive assets.

Evidently, GFCF has been on a downward trend from 2015 and this is in line with the overall trend in credit to the private sector shown earlier. This also entails that credit to the private sector has not extended to investment in capital goods which is crucial for economic growth.

Figure 3.13: Investment in Capital Goods



Source: Authors' Construction using World Bank data

3.3.2 Institutional Investments

In this DFA, institutional investments include funds from pensions and insurance companies. The Pensions and Insurance sector plays a significant role in Zambia's financial system. It provides a source of finance for the Government through investment in government securities among others.

Performance of the Pensions Industry

In recent years, the COVID-19 pandemic had a negative impact on the Pensions Industry, specifically pension schemes in the tourism, mining, education, and transport sectors. Nonetheless, the Pensions Industry in general was resilient both in terms of the number of pension scheme members and industry net assets. The pension industry's net assets grew by 14.1 percent to K10.84 billion as at end December 2021 from K9.45 billion as at end-December 2020. This was premised on the increase in investment income and contributions. Pensions Contributions increased by 22.1 percent to K1.60 billion in 2021 from K1.31 billion in 2020 (Table 3.3.1). This was attributed to new enrolments of members in the existing schemes, registration of new schemes and an increase in the base salaries for computing the contributions (MoFNP, 2022).

Table 3.3.1 Pensions Contributions (K'000)

Description	2021	2020	Percent Change
Regular Contributions	1,397,146.94	1,177,151.84	18.69
Special Deficit Funding	110,279.82	94,445.08	16.77
Transfer from Other Funds	92,714.68	39,156.43	136.78
Totals	**1,600,141.44**	**1,310,753.35**	**22.08**

Source: Authors' construction using 2021 Annual Economic Report

However, total investment income reduced by 4.92 percent to K1.78 billion in 2021 from K1.86 billion in 2020 Table 3.3.2). This reduction was mainly attributed to losses in property valuations amounting to K7.93 million. The reduced total investment income was also attributed to foreign exchange losses experienced in the last two quarters of the year 2021 due to appreciation in the local currency against major foreign currencies. Return on Average Net Assets reduced to 17.5 percent as of 31 December 2021 from 21.4 percent as of 31 December 2020. Notable also is that the gap between the industry return and inflation rate reduced to 1.1 percent as compared to 2.2 percent in 2020. This demonstrates the resilience of the pensions industry amidst the effects of the COVID-19 pandemic (MoFNP, 2022).

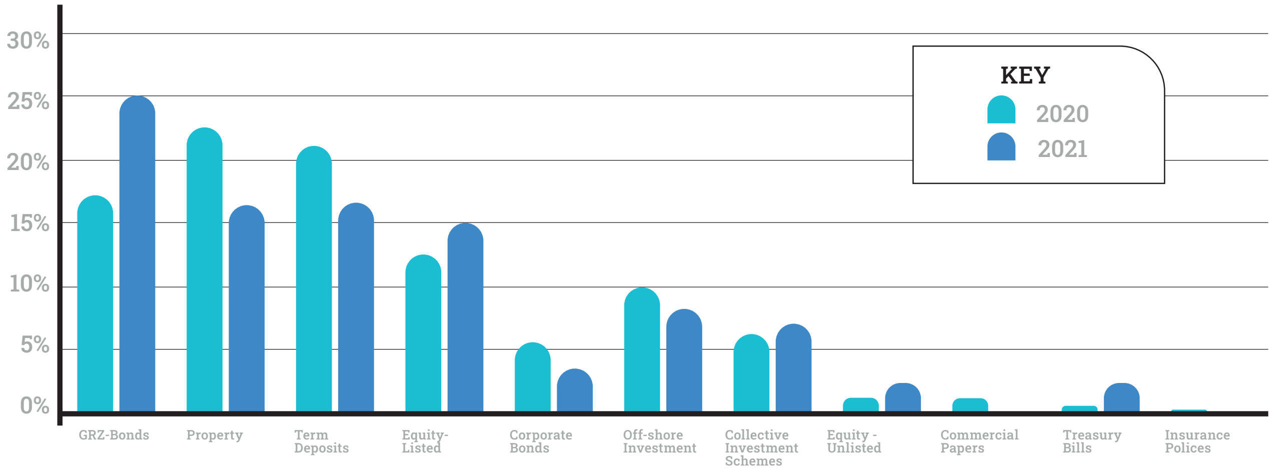
Table 3.3.2 Key Performance Indicators of the Pensions Industry, (K'000)

Description (K '000)	2021*	2020**	Percent Change
Total Investment Income	1,867,956	1,775,988	-4.9
Net Assets	9,499,008	10,841,317	14.1
Gross Domestic Product	332,223,233	408,914,789	23.1
Net Assets to GDP	2.86	2.67	-6.6
Return on Average Net assets (Annual)	**21.4**	**17.46**	**-18.4**

Source: Authors' construction using 2021 Annual Economic Report

In 2021, the Investment holdings of pension houses by category was dominated by Government bonds as shown in Figure 3.13. This demonstrated the financing role that Pensions funds play in supporting Government. Previously, property and term deposits were the most dominant investment portfolios.

Figure 3.14: Investment categories, (2020 - 2021)



Source: Authors' construction using 2021 Annual Economic Report

The total number of active registered pension schemes decreased by 1.6 percent to 244 pension schemes in 2021 from 248 in 2020. Nonetheless, participants in these pension schemes increased by 4.4 percent to 118,131 in 2021 from 113,175 in 2020. The increase in membership was due to the registration of new schemes and enrolment of new members in the existing pension schemes.

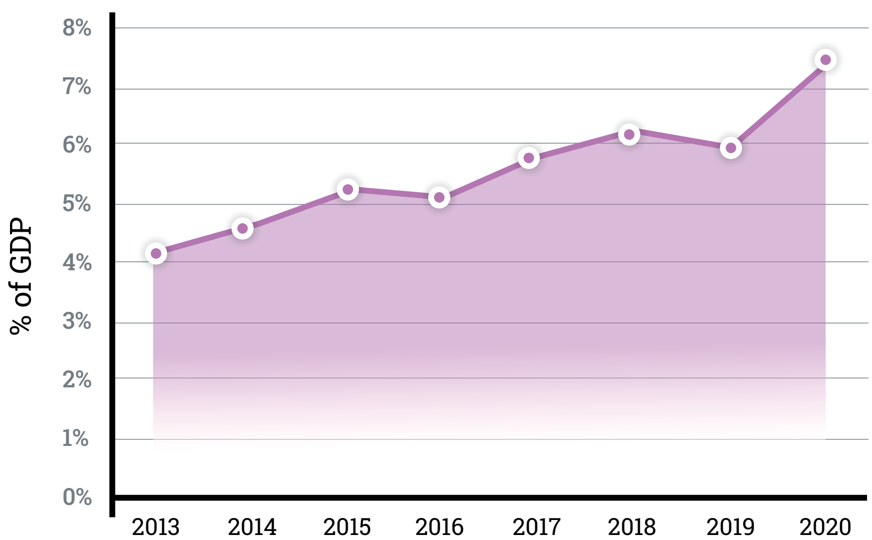
3.3.3 Insurance

The insurance industry recorded steady growth in 2021 with increased demand in the wakeof the COVID-19 Pandemic. This was reflected in a 22 percent rise in Gross Written Premiums (GWP) estimated at K5.4 billion in 2021 compared to K4.5 billion in 2020. This growth was supported by foreign exchange denominated premiums which cushioned the gross premium income.

3.3.4 Overall Performance of Pensions and Insurance

Over the recent decade, institutional investments (from Zambia's Pensions and Insurance Industry) have been on an upward trajectory. This is evidenced by Figure 3.15 which shows that institutional investments from pensions and insurance funds have been increasing since 2013. At the time of writing, data was available from 2013, and the institutional investments were not decomposed by type (insurance and pensions).

Figure 3.15: Institutional Investment from Pensions and Insurance Funds, (% of GDP; 2013 - 2020)



Source: Authors' Construction using PIA Annual Reports (2013 – 2020)

3.3.5 Capital markets

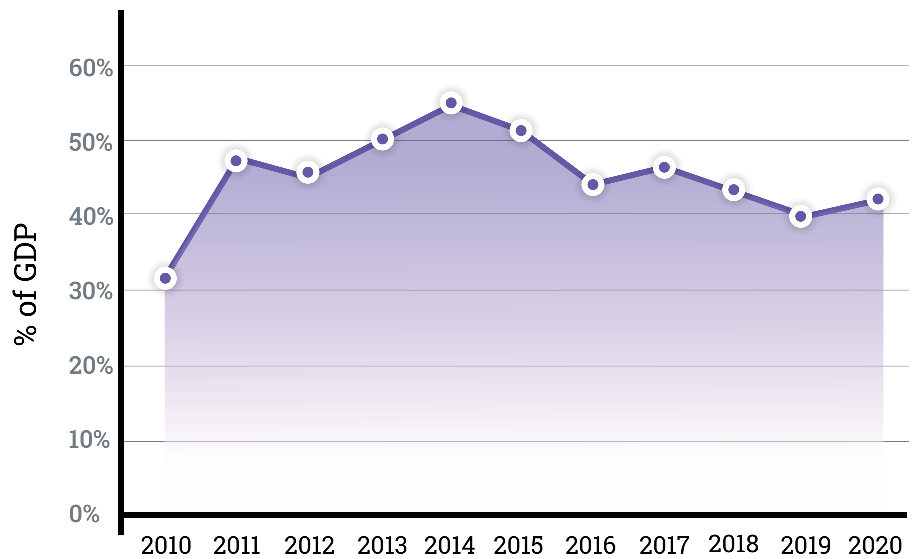
Capital markets comprise stock and bond markets. The roles of these markets in development finance, including their performance, are discussed below.

Stock Market

The players that operate in Zambia's Capital Markets industry consist of brokers/dealers, investment advisers, securities exchanges, central securities depositories, issuers, fund managers, credit rating agencies, investment banks, transfer agents among others. The Zambian Capital Markets have been gaining momentum and systemic importance over the years. For the year ending 31st December 2018 the Securities and Exchange Commission had issued 252 licenses and a total of 33 firms held dealers' licences.[9]

The Lusaka Securities Exchange (LuSE) recorded some growth in Market capitalisation from 2010 to 2014, before embarking on a downward trajectory lasting up to 2019 (Figure 3.16). The drop in market capitalization can be attributed to the deterioration in the macroeconomic environment over the reference period. Overall, market capitalization averaged 45.1 percent over the past decade (2010-2020). This suggests that Zambia has not fully exploited the stock exchange's revenue potential.

Figure 3.16: LuSE Market Capitalisation, (% of GDP; 2010 - 2020)



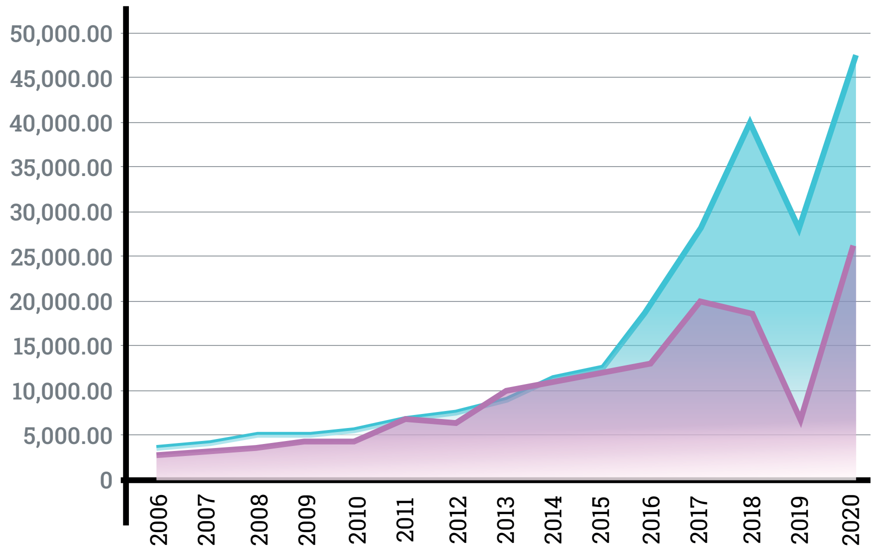
Source: Authors' construction using Annual Economic Reports

Bond Market

Zambia's Treasury bills and bond Market has seen growth since 2006. The biggest spike in the two variables was between 2015 and 2018. This was followed by a drop in 2019 although another leap was experienced in 2020 – (See Figure 3.17.) The giant leap since 2015 is indicative of Government's excessive borrowing from the domestic financial markets.

9. 2018 is the most recent year in terms of Annual reports available from the Securities and Exchange Commission

Figure 3.17: Trends in Zambia's Treasury Bill and Bond Markets, (K'Million)



Source: Authors' Construction using BoZ data

Corporate bonds

The corporate bonds market remains underdeveloped in Zambia. Currently, only a handful of issues are available on the market and these are all from financial service companies. This thin bond market is partly due to low liquidity and activity on the secondary market for Government bonds. This highlights the need for a liquid and well-developed government bond market in order to underpin the corporate bond market. Further, the corporate market development market landscape is held back by the harsh macroeconomic environment, characterized by high interest rates.

The most recent data from the Securities and Exchange Commission (SEC) shows recent corporate bonds activity (Figure 3.18).

Table 3.18: Corporate Bond Activity

Issuer	Tenor (years)	Rate	Par Value (ZK)	Year of Maturity
Madison Finance	5	-	10,000,000	2020
Stanbic	5	182-day T-bill + 400 bps	32,275,000	2021
Atlas Mara	6	22%	150,000,000	2024
Bayport Financial Services	3	182-day T-bill + 300 bps	19,000,000	2021
Bayport Financial Services	5	364-day T-bill + 300 bps	88,370,000	2023
ZNBS	5	364-day T-bill + 320 bps	20,050,000	2023

Source: Securities and Exchange Commission Zambia, 2018

3.3.6 Key Takeaways

The foregoing imply the following key takeaway messages:

- A surge in government borrowing has led to a crowding out of private investment. Domestic credit to the private sector (as share of GDP) has been a downward trajectory during the review period.
- The profile of credit is not entirely aligned to the country's priority sectors. While the 8NDP has a focus on value addition activities in the manufacturing and mining sectors as well as development

of the tourism sector, personal loans remained the most prominent class of lending to the private sector. Other sectors which received the highest proportion of loans are the wholesale and retail sector and the agriculture sector.

- Most private sector flows funds are going toward consumption as opposed to supporting growth sectors through investment. Since 2016, domestic private investment has been on slow and on a downward trajectory.
- Institutional investment (Pensions and Insurance) have seen a consistent surge over the review period with the most prominent investments from these funds directed towards Government bonds and property. This suggests a limited use of pensions and insurance investments to support the Government's socio-economic development agenda.
- Zambia is not fully exploiting the capital market's potential to contribute to resource mobilization. This is evidenced by the downward trend in the LuSE market capitalization.
- During the review period, the bond markets have seen significant growth more especially the period between 2015 and 2020 given Government's appetite for domestic borrowing. However, there is a dearth of information on corporate bond activity.

3.4 International Public Finance

To bridge financing gaps, many developing countries, including Zambia rely on external support to finance their development agendas. This subsection analyses international public finance flows for Zambia with a view to appreciate its structure and trends. International public finance includes the following components that are elaborated on in the ensuing subsections:

- Government borrowings from International Sources (External debt)
- Official Development Assistance (ODA)
- International Grants
- Other official flows (OOFs)

Due to paucity of data, other categories such as South-to-South, and OOFs are not analyzed in this DFA.

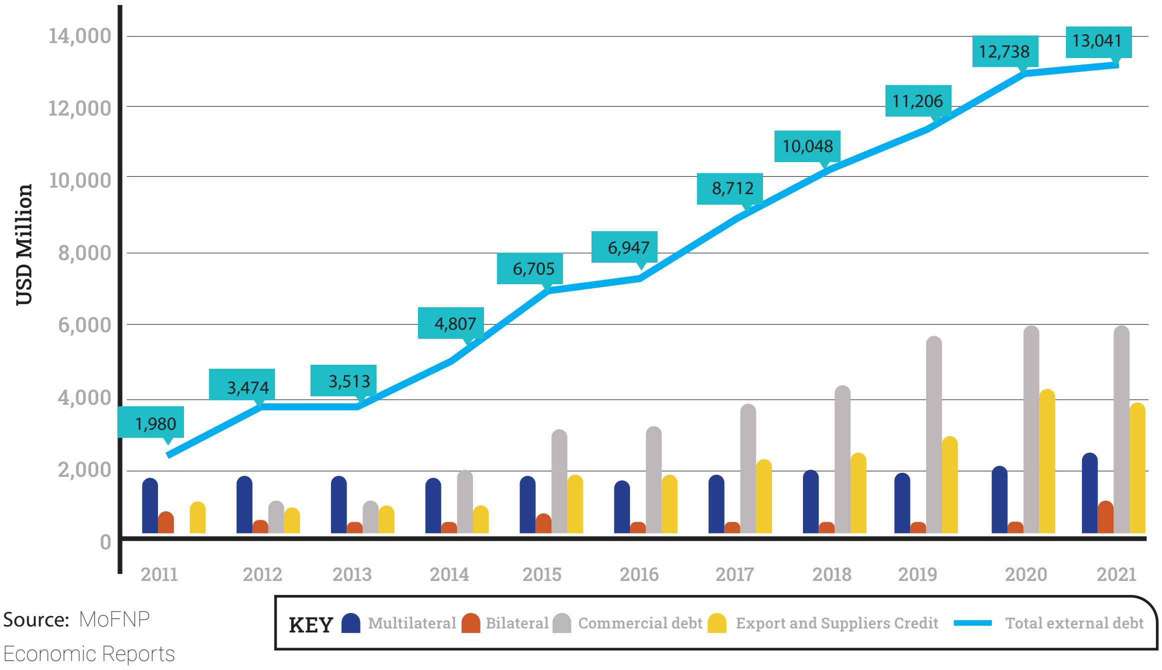
3.4.1 External debt

Post 2011, Zambia's external debt, comprising mostly of multilateral; bilateral; commercial debt as well as export and supplier credit, took an upward trajectory, specifically resulting from the country's increased access to the international capital markets. The aggressive infrastructure drive amidst ballooning fiscal deficits pushed the Government towards debt. As a result, total external debt grew from about US$ 2 billion in 2011 to US$ 13 billion in 2021 as depicted in Figure 3.18, representing a 550 percent increase in the period under review. Overall, total external debt grew at 22.5 percent per annum over the reference period.

The transition from a low-income to a lower middle-income country in 2011 opened-up the Country's borrowing options, resulting in increased participation in the commercial debt markets. In 2012, 2014 and 2015, the country borrowed US$750 million, US$1.0 billion and US$1.25 billion, respectively, rapidly raking up Eurobond debt of US$3.0 billion in less than 5 years. Other types of commercial loans also came on board. However, the terms and conditions of the commercial loans and Eurobonds were not as favorable as loans from bilateral and multilateral lenders, triggering debt and fiscal crises. As the proportion of commercial debt in the total debt profile grew, so too did the debt service costs.

Prior to 2015, multilateral loans accounted for most of the country's debt stock, the World Bank, IDA and SIDA being the major sources of multilateral loans. The loans were mainly in the form of project and program loans. However, after 2015, the structure of public borrowing changed drastically with Commercial debt accounting for the largest share of total external debt. The commercial debt surge was also fueled by the Zambia's reclassification from lower income to lower middle-income status. Other factors that triggered this change in debt composition include the economic slowdown, political cycles and reduced ODA inflows to the country. The loans were mainly used to finance infrastructure programs such as transport, ICTs and energy. While some infrastructure projects had significant socio-economic benefits, others generated minimal benefits, contributing to the deterioration in the economic environment. A thorough Public Expenditure and Institutional Review (PEIR) would be essential to assess the utilization of debt funds, particularly in infrastructure development.

Figure 3.19 Zambia's Central Government External debt by type, (2011-2021)



Source: MoFNP Economic Reports

Another growing category of external debt has been export and supplier credit, which has been the second largest source of external debt. This is followed by multilateral and lastly bilateral debt. Exports and suppliers' credit is made up of loans extended to facilitate the purchase of goods and services from within the creditor's country and this has been increasing, averaging US$1.6 billion between 2011 and 2021. The major creditor in this category has been the Exim Bank of China, accounting for an average of 87 percent while CATIC and others accounted for 13 percent of this finance.

Similarly, bilateral debt was on an upward trajectory over the reference period, albeit some fluctuations averaging US$331million. Between 2011 and 2013, Paris club flows dominated bilateral flows, accounting for about 68 percent, but this was reversed post 2013 with Non-Paris club flows accounting for an average of 63 percent over the same period.

In August 2019, with the massive debt accumulation overtime, the IMF and World Bank, based on a joint Debt Sustainability Assessment (DSA), announced that Zambia's debt was no longer sustainable. Many factors preceded the heightened debt contraction by the country and key among them included the ease with which borrowing could be acquired mainly due to weak legislation, reduced transparency, infrastructure drive and the weak linkage between national development planning and budgets.

Further, in November 2020, the country became the first African country to default on its debt during the COVID-19 pandemic, opting out of a US$ 42.5 million coupon payment. This debt crisis has since prompted Zambia to implement home-grown economic reforms supported by an IMF Extended Credit Facility as well as debt restructuring under the G-20 Paris Club Common Framework. The country has committed to an ambitious economic reform which includes attainment of fiscal sustainability. This will entail narrowing the budget deficit by curtailing wasteful expenditure especially towards poorly targeted public investments and programs such as the agricultural and energy subsidies. To cushion the poor, the Government is expected to increase allocations to the social sectors of the economy such as health and education. Successful and speedy conclusion of debt restructuring will also free up resources for investment in priority growth sectors.

In 2021, US$1.3 billion worth of Special Drawing Rights (SDRs) was allocated to Zambia by the IMF as part of a general allocation to the Fund's members. This resulted in significant increase in the country's international reserves. Further, as part of the restructuring program, the MoFNP has since cancelled US$2 billion worth of commercial debt-financed projects in July 2022. These fiscal adjustments are aimed at restoring fiscal and debt sustainability. The project cancellations are also in a bid to reduce the risk of further accumulating non-concessional loans and curtailing accumulation of arrears. At the same time, greater investments in education and health are emphasized to mitigate the impact of the adjustment programs and global shocks on the vulnerable members of society.

There are also efforts to restore budget credibility, enhance public finance management (PFM) and halt the accumulation of arrears to promote private sector led growth. The strengthening of legal framework around debt management in 2022 is testament to Government's commitment to fiscal sustainability. The major reform includes enactment of the Public Debt Management Act, 2022, which is discussed in Chapter 5. Further, the MoFNP seeks to improve interface with other ministries in need of financing by enabling them to present their financing needs which would later be addressed in the coming fiscal year.

Future flows in the next 3 to 5 years will be made up of more concessional and less of commercial debt as the country implements its economic recovery and debt restructuring and IMF programs. Further, a financing mix that the country can adopt without triggering another debt crisis is the Public Private Partnerships (PPPs). This is elaborated in Chapter 6 of this report. The government is also adopting a 60:40 strategy with the aim of contracting 60 percent domestic debt and 40 percent foreign debt. Out of this foreign debt, 15 percent should be PPP- bankable projects. These reforms will alter the development finance landscape, steering the country away from international sources.

3.4.2 Official Development Assistance (ODA)

Official Development Assistance (ODA) comprises Government aid that promotes and specifically targets the economic development and welfare of developing countries. ODA remains the main source of development aid for developing countries.[10] ODA constitutes disbursement of loans made on concessional terms (that is with a grant element of 25 percent or more), grants, technical cooperation, humanitarian assistance as well as debt relief to promote economic development. This finance is disbursed to countries through off budget support and direct budget support. ODA is categorized into bilateral and multilateral assistance depending on its source.

All low-and-middle income countries, with the exception of EU and G8 members, are eligible to receive ODA. The income status is determined by the country's Gross National Income (GNI) per capita as published by the World Bank. This also includes Least Developed Countries as defined by the United Nations. For a country to access ODA finance, its developmental goals must align with the relevant sectors or thematic areas that will contribute to the achievement of broader level goals such as climate change, poverty reduction among others. Further, this financing is sector specific and requires that a country meets the minimum standards on various indicators such as country ratings, level of fiscal discipline and percentage allocations to key sectors of the economy.

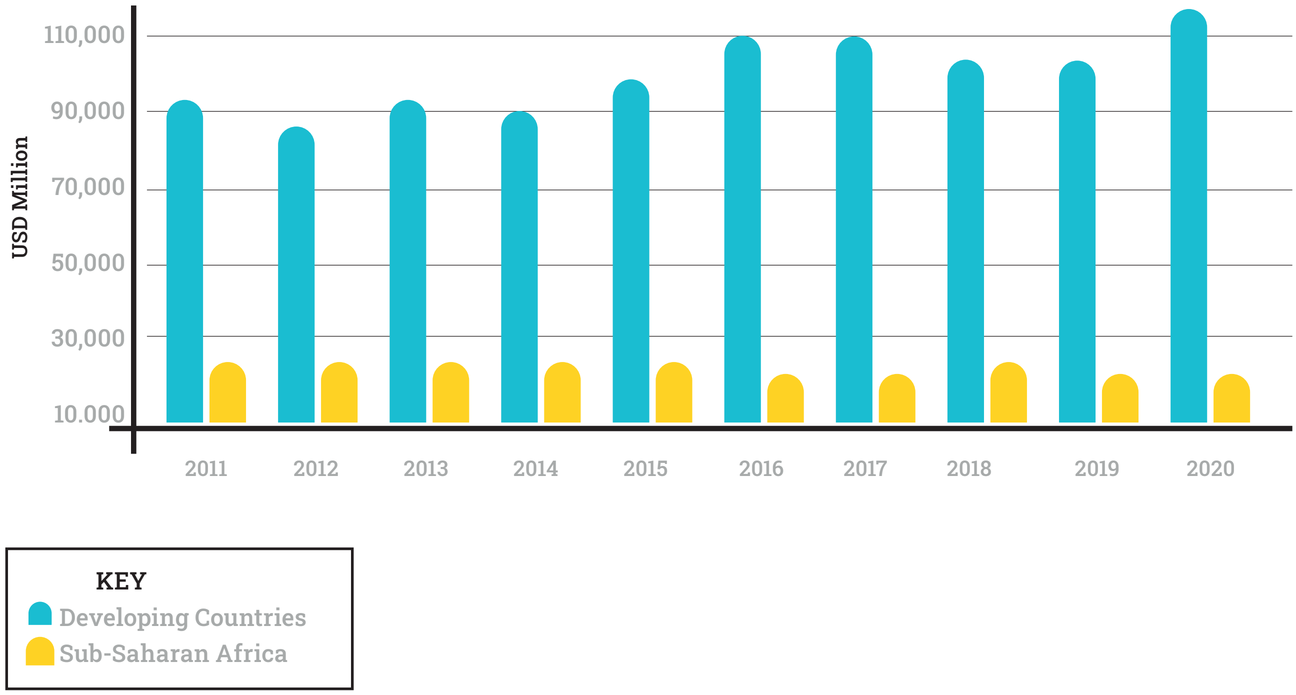
Post-independence, many developing countries relied on aid as a tool for boosting economic growth through economic, financial and technical assistance in form of grants and loans with favorable terms.[11] Challenges surrounding domestic revenue mobilization along with difficulties in attracting investments further reinforced many developing countries' reliance on ODA to finance development programs.

The general trend of ODA in developing countries and particularly SSA between 2010 and 2021 was upward. Majority of this finance was in form of grants, mainly debt relief, whilst a smaller proportion involves loans and equity investments.

The reliance on ODA saw disbursements to developing countries by Development Assistance Committee (DAC) countries increase from US$90 billion in 2011 to US$114 billion in 2020 as depicted in Figure 3.20, signifying a 26 percent increase in the period under review. Narrowing it to Sub-Saharan Africa (SSA), ODA inflows remained relatively constant averaging US$26 billion annually in the last decade, with significant bilateral sources being Germany, USA, UK and Japan while the World Bank, EU and the UN were among the major multilateral sources of this finance.

10. OECD. 2021
11. Japan Trade Organisation. (2010). The Role of Foreign Aid in Developing Countries

Figure 3.20: ODA Disbursements by DAC countries, (2011-2020)



Source: Authors' compilation using figures from OECD database

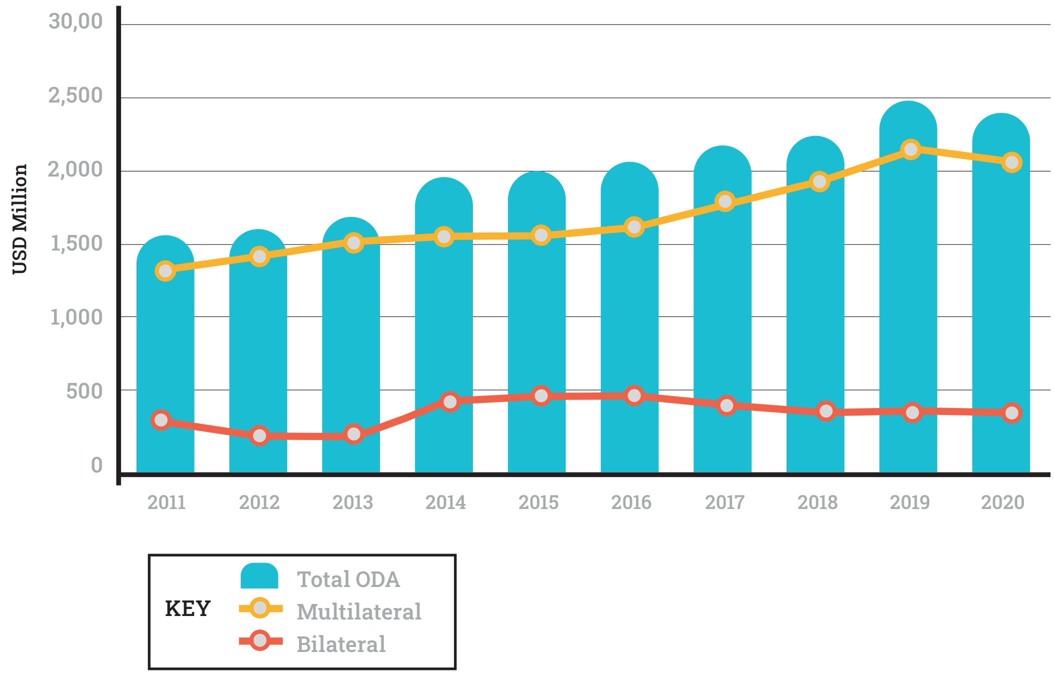
Globally, total ODA from DAC countries increased from US$ 133 billion in 2011 to an all-time high of US$179 billion in 2021[12]. On the other hand, net ODA to SSA countries on a cash basis increased to US$33 billion in 2021 representing an average increase of 2 percent from 2020, partly owing to development assistance for COVID-19 activities particularly in form of vaccine donations. The major sources remained the USA (US$ 42.3 billion), Germany (US$32.3 billion), Japan (US$17.6 billion), UK (US$15.8 billion) and France (US$15.5 billion). Of the total ODA in 2021, 97 percent was in form of grants, loans to sovereign entities, debt relief and contributions to multilateral institutions while 3 percent went towards development oriented private sector instrument vehicles, net loans and equities to private companies[13].

ODA to Zambia is received through sector wide approach (SWAP), sector budget support (SBS), project support) and direct budget support. Despite the Government having a preference for receiving ODA through direct budget support, cooperating partners preferred to channel these funds through project approaches that is, off-budget. This is so because funders prefer to channel resources to programs that are aligned to their priority strategies, thus retaining direct control on the utilization of funds.[14]

Except for 2020, Zambia's ODA receipts had generally been on the rise overtime. Except for commercial creditors, all other components of ODA such as bilateral and multilateral have been on an upward trajectory. The increase in ODA flows over the 7NDP period (2017-2021) was, in part driven by increased trust between Government and cooperating partners Government and cooperating partners.

12. Based on preliminary OECD data
13. OECD ODA summary 2021
14. Republic of Zambia (2020) Review of the Implementation of the Istanbul Program of Action Least Developed Countries (2011-2020).

Figure 3.21: Bilateral and Multilateral ODA to Zambia (2011-2020)



Source: Authors compilation using figures from Economic reports

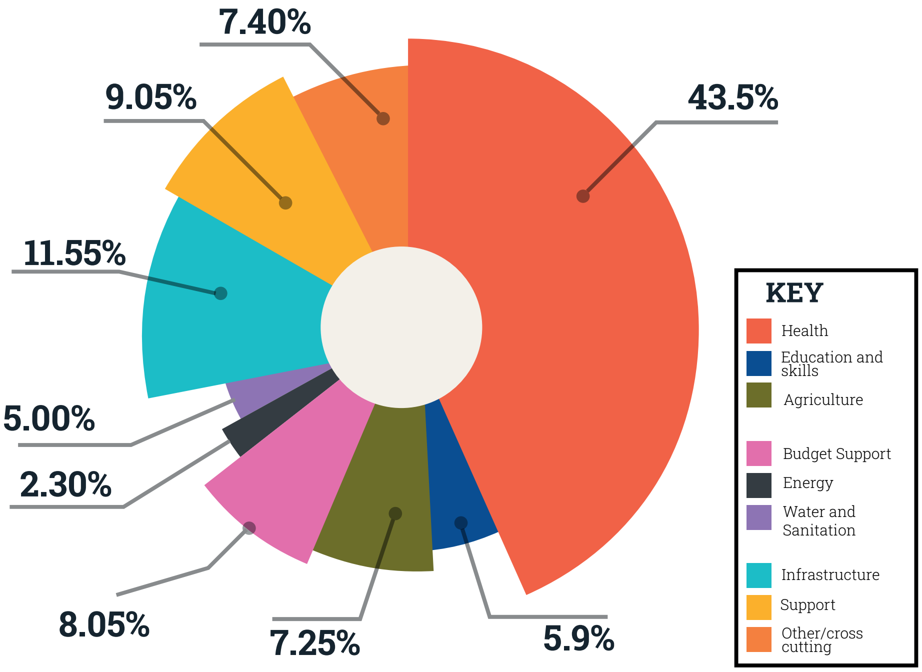
Between 2011 and 2020, Zambia had on average received US$ 1.9 billion in total ODA flows (Figure 3.21). ODA finance on average contributed 26 percent to Zambia's National Budget in the recent past and this was in form of projects, loans and program grants. Overall, ODA received from multilateral sources increased by 85 percent and was 5-times higher than that from bilateral sources. The main multilateral sources include the ADB, World Bank and the IMF; the World Bank being the largest source, accounting for more than half of all multilateral flows.

On the other hand, bilateral ODA flows were mainly from the Paris and non-Paris club members. Until 2014, the Paris club accounted for a larger proportion of bilateral ODA. However, this changed in the period after 2014 with non-Paris club dominating this category of flows. Between 2011 and 2020, Zambia received an average of US$ 331 million in bilateral ODA compared to US$ 1.6 billion in multilateral ODA. Although multilateral ODA was on an upward trajectory, a notable decline of 27 percent in bilateral ODA was recorded between 2011 and 2013 as well as between 2015 and 2020.

Recent drive toward fiscal sustainability and debt restructuring efforts entail a move away from non-concessional expensive debt to cheaper financing such as ODA. Further, for more ODA to flow to Zambia, Government must have clear development strategies, strengthen implementation of national plans and leverage from finance windows that promote global developmental goals as well as initiate pilot projects especially under climate change.

Regarding the composition of Zambia's ODA by sector, the health, infrastructure, agriculture and education sectors were among the top recipient sectors between 2011 and 2016 (Figure 3.22). This indicates that the ODA flows were closely aligned with the 6th and 7th National Development Plans.

Figure 3.22: Average percentage of ODA disbursements by Sector, (2011-2016)



Source: MoF Cooperating Partners Report

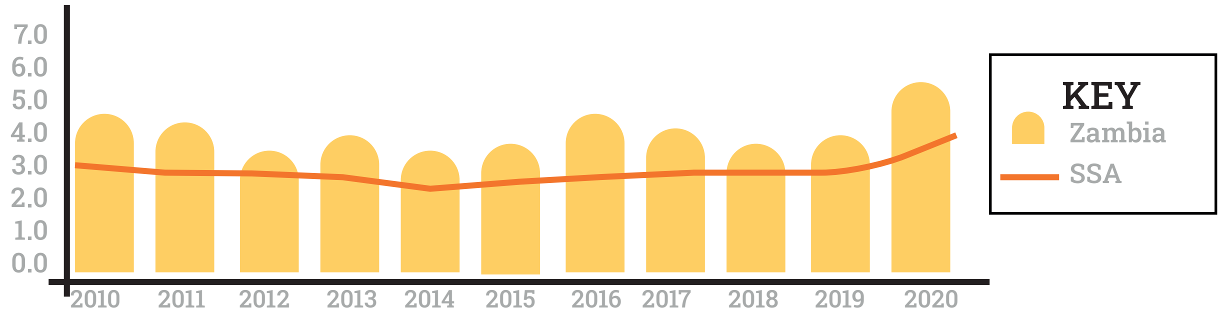
According to Figure 3.22, the top 3 sectors that received ODA in the period 2011 and 2016 included: the health sector receiving almost half of the total ODA at an average of 43.5 percent. This was followed by infrastructure at 11.5 percent and other support (capacity building, in-kind) at 9 percent.

ODA has since evolved toward growth sectors such as energy and agriculture. For instance, in the recent years, Zambia's ODA has mostly been channeled towards the Energy sector, particularly the Rural Electrification Authority (REA), followed by the agricultural sector. Primarily, these funds were channeled towards technical and operational capability enhancement, promotion of sustainable practices against climate change as well as the promotion of energy saving and renewable energies.

Zambia's ODA as a percentage of GNI surpassed the SSA average increasing by 18 percent overall in the period under review (Figure 3.23). Overall, the SSA ODA averaged 3 percent while Zambia recorded an average of 4.3 percent. This suggests that Zambia is aid dependent, posing threats to sustainable implementation of development programs. Overreliance on donor driven projects tends to pose risks to the country's implementation of development plans. This is especially true if there is weak alignment between priority and donor priority sectors.

Zambia's reliance on ODA waned between 2012 and 2015, as reflected declining ODA-to-GNI ratio (Figure 3.23). This is because the country switched to non-concessional (including commercial debt) funding from the international market and other alternative financing sources following a re-classification to a lower middle-income country which opened access to international capital markets.

Figure 3.23: ODA as a percentage of GNI: Zambia and SSA, (2010-2020)



Source: Authors' Own Construction Using OECD Database

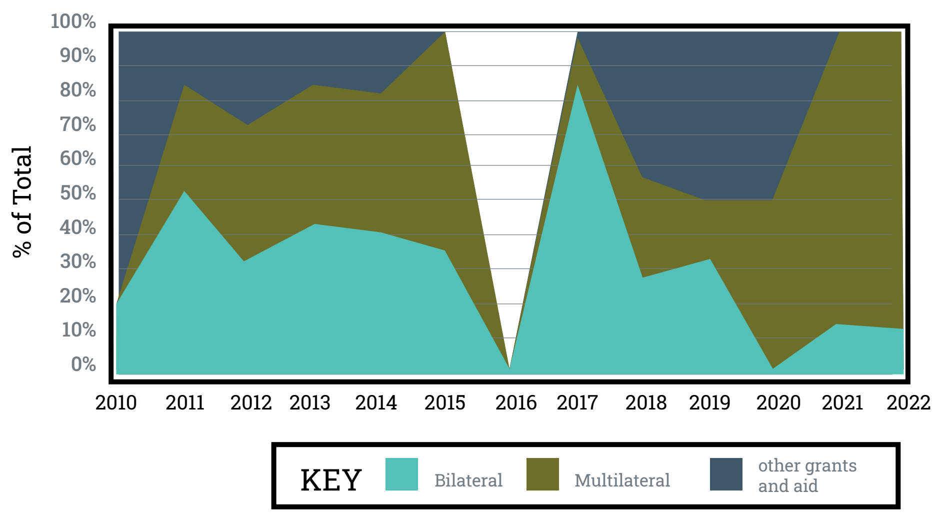
After 2015, however, ODA picked up before falling in the 2017 and 2018. The major reason for the dip in ODA was that the country did not fully align its developmental objectives with that of the ODA window objectives. However, the trend was reversed in 2019 and 2020 when Zambia saw a significant increase in ODA. This increase was driven by resource injections toward containment of the COVID-19 pandemic.

3.4.3 International Grants

Grants are legally binding obligations for disbursement of a specified value of funds for which repayment is not required. These include noncompulsory current or capital receipts that are received by government from another government or international organization.[15] Total international grants to Zambia constitute multilateral, bilateral and other grants and aid. Generally, grants to Zambia have been fluctuating and ultimately decreasing overtime most of these have been attached to ODA. Between 2011 and 2022, total grants averaged K2.8 billion. However, during the period, grants decreased from K4 billion to K1.8 billion representing an average decrease of 55 percent. This decline was mainly driven by the fall in bilateral grants, resulting from weak governance systems.

A decomposition of grants by major categories indicates that multilateral grants dominated the international grants, accounting for 41.9 percent of the grants over 2010 to 2022 (Figure 3.24). Bilateral grants follow in second place, averaging 33.4 percent over the same reference period. Evidently, bilateral grants have declined in importance over time, falling from an average of 37.7 percent (of total grants) from 2010 to 2015 to 29.2 percent over the past six years (2017 to 2022).

Figure 3.24: International Public Grants to Zambia, (2011-2022)



Note: 2016 data is missing; 2021 and 2022 are based on estimates.

Source: Authors' contruction using figures from Yellow and Blue books[16].

15. Ministry of Finance (2010). Financial Report
16. 2016 has missing data on international grants

Bilateral grants averaged K1 billion overtime accounting for the largest portion of total grants in the period 2011 to 2017 (with an exception of 2015). Most of the bilateral grants were from Germany, Sweden and USA, among others (Table 3.4.1). Additionally, the highest amount received of total international grants to Zambia between 2011 and 2022 was K7.1 billion in 2017. From this, a large portion of it was bilateral aid totaling K6 billion. The significant bilateral donors in 2017 were USA (USAID) (with a grant amount of K4 billion) and Germany (K1.4 billion).

Table 3.4.1 Zambia's Bilateral grants sources, (2017-2020)

	2017 (K)	2018 (K)	2019 (K)	2020 (K)
Japan	94,069,138.00	-	330,577,235	3,407,464
United Kingdom	202,072,348.00	36,922,283	-	-
Germany	1,144,814,008.00	188,980,262	497,495,779	-
SIDA-Sweden	119,409,689.00	277,270,914	93,249,847	36,043,297
Ireland	69,439,655.00	-		-
Finland	46,121,198.00	56,436,968	12,726,980	-
AFD	183,602.00	-	5,859,267	-
USAID - Various Projects	4,454,082,091.00	361,150	63,763,750	-
Saudi Arabia	95,593,264.00	-	-	-
Danish Institute for Human Rights	-	135,357	118,372,319	-
China	-	227,204,886	-	-
Denmark	-	-	-	4,191,750
Other Grants	-	-	118,372,319	
Total	**6,225,784,993.00**	**787,311,820**	**1, 122, 000, 177**	**43,642,511**

Source: Authors contruction from Financial Reports

On the other hand, multilateral grants to Zambia have averaged around K1 billion annually making up 86.5 percent of total international grants in 2021 and 2022. The increase is in part due to the COVID-19 response efforts from various agencies. Major sources of multilateral grants include the AfDB, World Bank, IFAD and the Global Fund (Table 3.4.2).

Table 3.4.2 Zambia's Multilateral grant sources, (2017 - 2020)

	2017 (K)	2018 (K)	2019 (K)	2020 (K)
UN	1,999,962	-	-	22,761,221
World Bank	540,937,193	512,290,388	599,757,420	-
African Development Fund	138,381,649	-	-	-
European Union	184,153,490	9,049,654	-	-
SADC	5,279,107	-	-	2,688,762
IFAD	101,732,094	-	-	133,724,077
EU/SADC	-	5,418,360	-	-
Donor General	-	277,694	-	-
African development Bank	-	1,060,158	-	244,793,815
Gavi The Vaccine Alliance	-	24,984,784	-	-
FAO	-	93,816	-	-
UNIDO	-	190,642	-	-
United Nations Office for Project Services-UNOPS	-	1,652,652	-	-
Hope of Homes for Children	-	153,433	-	-
Development Aid	-	124,261	-	-
Clinton Health Access Initiative	-	7,214,414	-	-

ICF	-	22,514,033	-	-
Liverpool School of Tropical Medicine	-	10,452,485	-	-
UNFPA	-	3,840,136	-	-
Centre for Diseases Control	-	16,092,080	-	-
UNICEF	-	9,495,131	-	-
Global Fund	-	209,050,550	-	-
OPEC	-	-	-	51,036,171
CCARDESA	-	-	-	745,200
IBRD	-	-	-	769,295,657
Global Water Partnership Southern Africa	-	-	-	248,442
WHO	-	-	-	1,897,838
Total	**972,483,495**	**833,954,671**	**599,757,420**	**2,757,486,082**

Source: Authorscontruction from Financial Reports

Overall, grants to Zambia have been channeled towards social sector projects such as education, community development, health, water and sanitation while others come in form of relief programes. These funds are also channeled towards capacity building to enhance skills training, promoting value chains and entrepreneurship.

The education sector in Zambia receives significant resources from cooperating partners both through direct budget support and project financing. The main partners include the World Bank, UNICEF, USAID, and World Food Program (WFP). The financing has been channeled to different programes including the Keeping Girls in School (KGS) project, Zambia Education Enhancement Project (ZEEP) and the Support to Early Childhood Development.

In the health sector, most grants are for the enhancement of the primary health services, and these are mainly funded by USAID and International Development Association (IDA) among others. The water and sanitation sector also continues to be heavily donor financed with 73 percent of its budget coming from external finance in 2022. This is for financing projects such as water supply, sanitation and drainages.

3.4.4 Key Takeaways

The key takeaway points from the foregoing are:

- Zambia has been relying on external debt to finance its development programs. Total external debt has grown by about 22.5 percent per annum between 2011 and 2021.
- External debt is dominated by commercial debt, posing threats to attainment of fiscal and debt sustainability.
- Some of the debt was not economically profitable, contributing to deterioration in the macroeconomic environment, and deepening fiscal imbalances.
- Zambia's ODA as a percentage of GNI is generally above the SSA average. This suggests a heavy reliance development assistance to finance development plans.
- A significant part of Zambia's budget is financed through grants. However, multilateral sources have been fluctuating over the recent past.
- Social sectors are the largest recipients of ODA, raising questions about sustainability of such programs.
- Zambia is not adequately leveraging the financing windows to optimize the international public resources.

3.5 International Private Finance

Since the initiation of economic reforms in the early 1990s, the Zambian Government has made major strides in supporting private sector led growth by implementing reforms aimed at enhancing a competitive business and investment climate. In general, these reforms are critical in making the investment climate in Zambia conducive for both local and foreign investment. The landscape of development finance has changed substantially over the past decade. Private finance has replaced aid at the centre of global and national development initiatives, for both governments and international bodies. This reflects both the growing need to mobilise all types of resources to lift people out of poverty, as well as growing pressure among donors to link their commercial interests with development policy. While domestic private financial resources are far larger and, most would argue, more important for investment in developing countries, much attention has instead focused on international private finance. International private finance includes foreign direct investment (FDI), portfolio equity, remittances, and private borrowing from international sources. The Addis Ababa Action Agenda of 2015 on financing for development emphasizes that private business activity, investment and innovation are major drivers of productivity, inclusive economic growth and job creation. Long-term private investment is critical to support growth, employment and structural transformation, and needs to be aligned with social inclusion and environmental sustainability.

3.5.1 Foreign Direct and Portfolio Investments

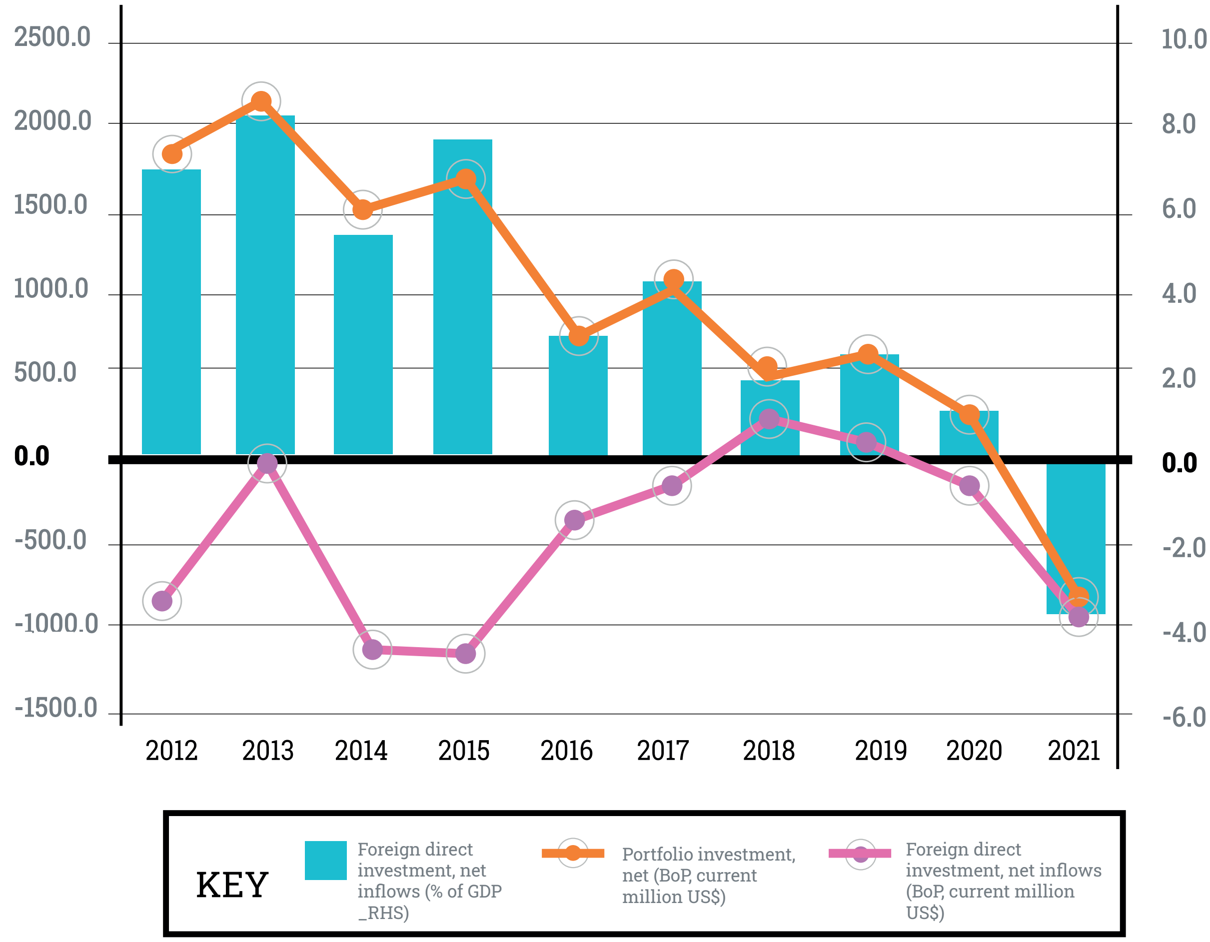
Foreign Direct Investment (FDI) has a key role to play in the development trajectory of any economy. This is particularly true for developing countries like Zambia where there is a strong relationship between foreign investment and economic growth. FDI boosts international trade through increased export earnings, promotes global best practices, is non-debt creating, provides growth through gross capital formation, creates employment and stimulates inflows of foreign currency. To add to this, FDI facilitates technology transfer, increases and accelerates opportunities for the domestic market. The government's major obligation is to ensure that FDI contributes to the economic well-being of citizens in their respective communities by channeling investments into zones that have the most potential to create decent jobs and reduce poverty.

Figure 3.25 shows that since 2013, international private flows, including FDI net inflows have been generally declining. This downward trend can be attributed to the instabilities in the macroeconomic and policy environments which the COVID-19 pandemic exacerbated. However, even before the COVID-19 pandemic, private international flows were already in a declining trajectory. Specifically, the mining sector suffered major disinvestments, dampening FDI.[17] The poor performance of FDI to the mining sector can in turn, be attributed to the unpredictable fiscal regime for the sector manifested in frequent policy reversals.

With regards to the distribution of FDI liability inflows by sector, mining and quarrying contributed the largest share of 56.6 percent mainly in form of debt, a decrease from 62.8 percent in 2019. Manufacturing was second, at 20.1 percent, following a growth of 4.4 percent due to debt and equity capital inflows. The remaining sectors collectively accounted for 23.2 percent of the total stock. The FDI liability flows continued to be dominated by large mining investments from Canada, Switzerland, Australia, China and the United Kingdom.

17. 2022 Survey on Private Sector Foreign Investment in Zambia (Bank of Zambia)

Figure 3.25: Zambia's FDI and Portfolio Investments net in-flows (US$)

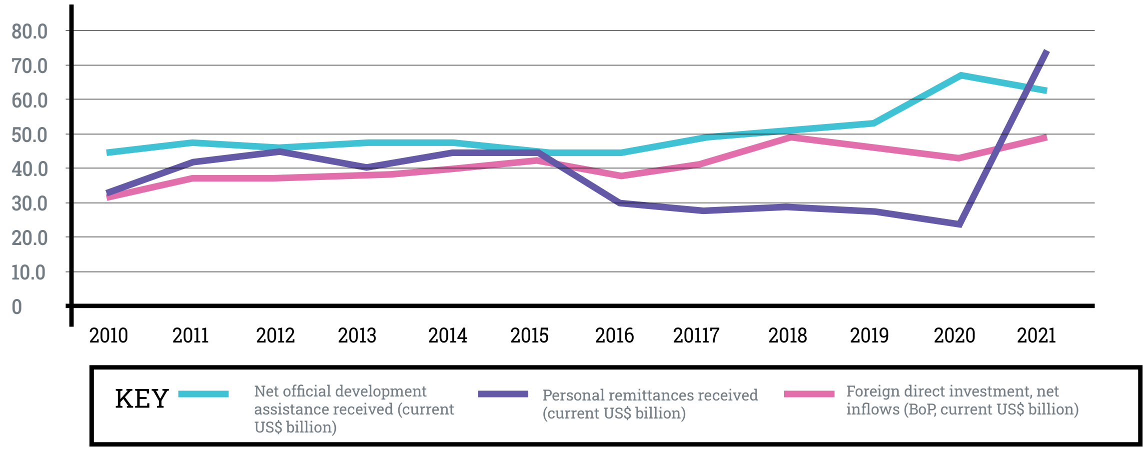


Source: MoFNP and the World Bank

3.5.2 Remittances

Remittances can be broadly defined as transfers, cash or in-kind goods that developing countries receive from their diaspora communities. Over the years, remittances have become an important component of development finance in developing countries, competing with FDI and ODA (Figure 3.26). In fact, remittances averaged US$41.1 billion from 2010 to 2021, compared to US$ 38.3 billion flows from FDI. Additionally, considered to be more stable and evenly distributed across developing countries than private capital and FDI, remittances form the lifeline of most developing countries' economies, including Zambia (Ratha, 2015) (UNCTAD, 2013). As of August 2022, the United States and United Kingdom remained as the top originating countries accounting for 44 percent of international inbound remittances to the country (BoZ, 2022).

Figure 3.26: Remittances, FDI and ODA Flows to Sub-Sahara Africa, (Billions of USD)

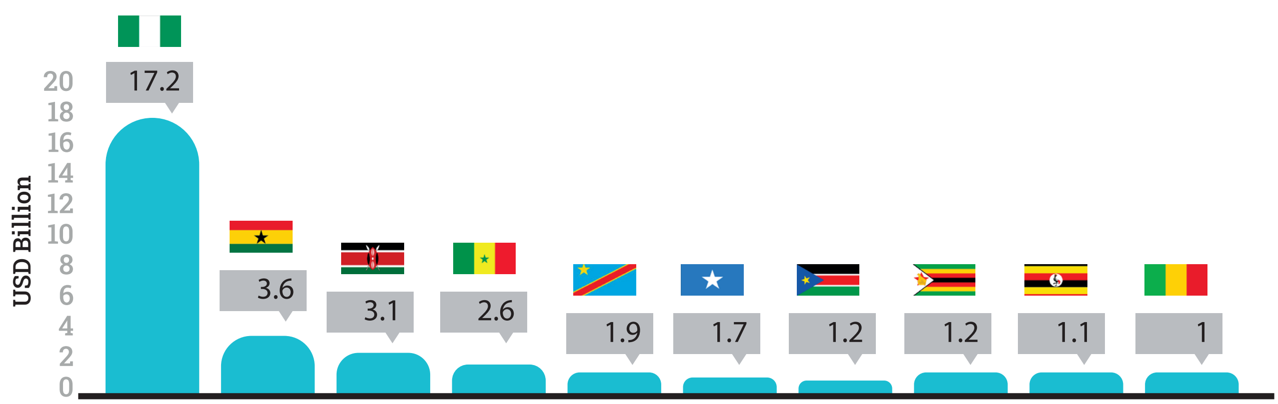


Source: Adopted from the World Bank 2023

More importantly, unlike other flows such as FDI and private capital, remittances have proved to be countercyclical, increasing during economic downturns or global crisis such as the financial crisis of 2008/9 and the COVID-19 pandemic, as migrants working in developed countries intensify their support to their relatives back home during such crisis (World Bank-KNOMAD, 2021) (Ratha, 2015). This resilience makes remittances an important factor in combating poverty and increasing income levels in developing countries, especially during 'tough times'.

According to the World Bank (Figure 3.27), major recipients of remittances in Sub-Saharan Africa (SSA) include Nigeria (US$ 17.2 billion), Ghana (US$ 3.6 billion) and Kenya (US$ 3.1 billion), respectively (World Bank-KNOMAD, 2021). Being the most populous country in SSA, Nigeria's high receipts of remittances largely owes to its large diaspora community. However, as a percentage of GDP, smaller economies like Lesotho, Gambia and Cape Verde boast of receiving more remittances, accounting for 20.6 percent, 15.6 percent and 13.9 percent, respectively, in 2020 (World Bank-KNOMAD, 2021).

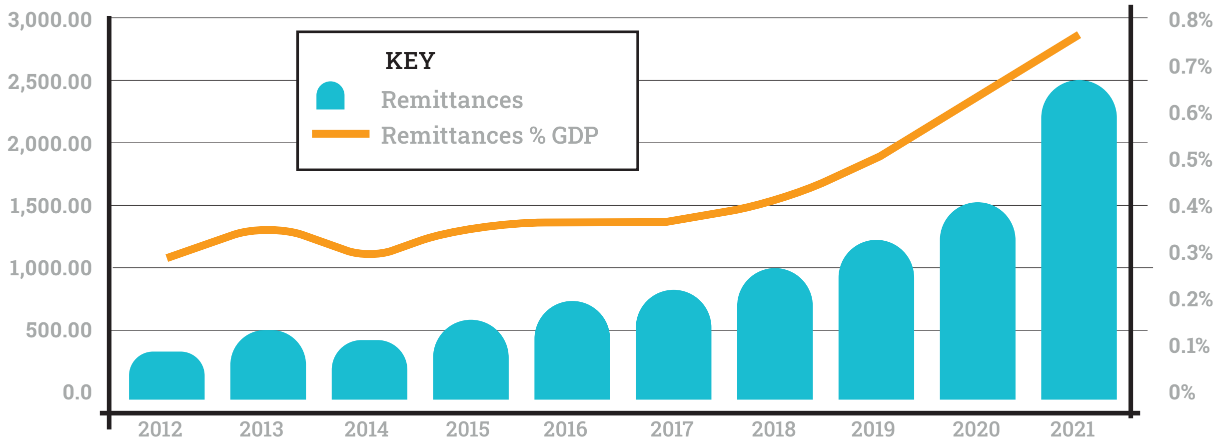
Figure 3.27: Top Remittance Recipients in Sub-Saharan Africa, ($ billion, 2020)



Source: Source: Adopted from the World Bank-KNOMAD Policy Brief Report (p.34), 2021

Like other developing countries, Zambia's inflow of remittances has been growing over the years; almost tripling in size between 2012 and 2018 – more than doubling from K369 million to K914 million (Figure 3.28). From 2017 to 2021 remittances inflows to Zambia grew about fivefold, from about K800 million to almost K4.6 billion (World Bank, 2022). While the entire SSA region recorded a significant reduction in remittances inflows of about 12.5 percent in 2020, Zambia on the other hand recorded a marked increase in remittances inflows (37.5 percent), distantly followed by Mozambique (16 percent) and Kenya (9 percent) (World Bank-KNOMAD, 2021).

Figure 3.28: Zambia's Inflow of Remittances (K'million), (2017-2021)



Source: Authors' contruction from the World Development Indicators Data, 2022

Engagements with stakeholders such as BoZ and MoFNP revealed that improvement in the system of recording remittances in 2020 explains the larger volume of transactions captured. However, whether this spike in remittances supposedly from a system upgrade and/or expansion will be sustained beyond the COVID-19 era remains to be seen. Despite this impressive growth, remittances still make up less than 1 percent of Zambia's GDP, only estimated at 0.7 percent of the country's GDP in 2020 (World Bank, 2022). This is by far behind other countries in the region like Zimbabwe whose receipt of remittances in 2020 was estimated at almost 6 percent of its GDP (World Bank-KNOMAD, 2021). Key informants attributed the stagnation in remittances small diaspora population and a relatively unskilled workforce. In addition, inadequate money transfer mechanisms (lengthy bank transfer periods), weak frameworks for diaspora financing and high transaction costs also contribute to the slow growth of remittances.

3.5.3 Key Takeaways

The following are the main takeaway points from the forgoing:

- During the period 2012 -2014, most of Zambia's FDI inflows originated from the United Kingdom followed by Switzerland, Canada, China, India and Nigeria;
- Since 2014, Zambia's international private flows such as FDI and portfolio investments have been declining mainly due to poor investor perceptions and unconducive policy and macroeconomic environment.
- In the medium-term, sectors that are expected to receive most FDI include, mining and quarrying, energy, agriculture, and tourism. However, this is premised on the implementation of the industrialization and export diversification strategy under the Economic Recovery Program (ERP); and
- Further, the continued promotion of Public Private Partnerships (PPPs), particularly in infrastructure development is also expected to enhance private investments.

In terms of remittances:

- Although Zambia's inflow of remittances has been growing over the years they only make up less than 1 percent of Zambia's GDP, estimated at 0.7 of GDP in 2020;
- While the Sub-Saharan Africa (SSA) region recorded a significant reduction in remittances inflows of about 12.5 percent in 2020 because of the effects of the COVID-19 pandemic, Zambia recorded a momentous increase in the inflow of remittances estimated at 37.5 percent; and
- Remittances are more resilient to external shocks as evidenced by their ability to with stand the COVID-19 shocks; and
- Reforms and innovations aimed at reducing transaction costs for diaspora population (for example, through system upgrades) proved effective in increasing inflows.

04

Chapter 4: Prospective Analysis of Major Financial Flows

Zambia seeks to attain prospeous middle-income status by 2030, an ambitious aspiration that requires colossal financing. This chapter provides a prospective analysis of the major financial flows from 2022-2030 mostly based on Government forecasts. Given the crucial role of financing in development planning and implementation, the importance of conducting a prospective analysis cannot be over-stressed.

4.1 Key Assumptions

The preceding sections have painted a picture of Zambia's development finance landscape, highlighting the unexploited routes, and unviable sources. Aside from providing a historical analysis of development finance flows, this DFA also seeks to bring out areas where new sources of finance can be mobilized. This section takes a forward-looking approach by assessing development finance outlook for the next six-eight years (from 2022 to 2030).

Projections for domestic finance flows were heavily informed and drawn from the MoFNP extrapolations. This DFA also relied on the historical global trends, IMF World Economic Outlook (WEO) to make projection for select flows. In a few cases, simple assumptions such as averages and growth rates for the series were used to inform the forecasts.

The projections in this study take into account two main factors:

- Country-specific factors: Factors such policy reforms including the IMF deal, macroeconomic trends, the downgrade to low-income status and investment climate form a major component of the assumptions. The forecasts from the Government that this DFA mostly relied on already incorporate most of these factors. However, the forecasts do not adequately account for the debt restructuring process and its uncertainties as the country is still undergoing negotiations with its creditors to restructure its external debt.
- Global economic trends and factors: External factors including the geopolitical forces, effects of global catastrophes (Ukraine war; COVID-19 pandemic), frameworks for international cooperation are critical drivers of external sources. Thus, these factors are critical inputs into the projections of ODAs, FDIs and remittances. By drawing from the IMF WEO, the projections for the relevant flows incorporate most of these factors.

4.2 Outlook for Major Flows

4.2.1 Domestic Public Sources

Prospective analysis of development finance flows is crucial for fiscal sustainability and effective long-term planning. Knowledge of the development finance outlook is particularly vital for Zambia as it works to restore macroeconomic stability, attain economic recovery, and fortify fiscal fitness. The forecasts for revenues and grants are drawn from MoFNP estimates and models.[18] For these flows, the analysis starts with a review of the projected resource pool for the 8NDP (2022-2026). According to MoFNP, the projections for 2022-2026 are more accurate than those for 2027-2030.

For this reason, the prospective analysis focuses more on the 8NDP period, with extensions to 2030 for selected flows. The idea is to provide a forward-looking finance mobilization perspective that furnishes Zambia with sufficient policy wiggle room, positioning it to adequately respond to resource mobilization-related shocks.

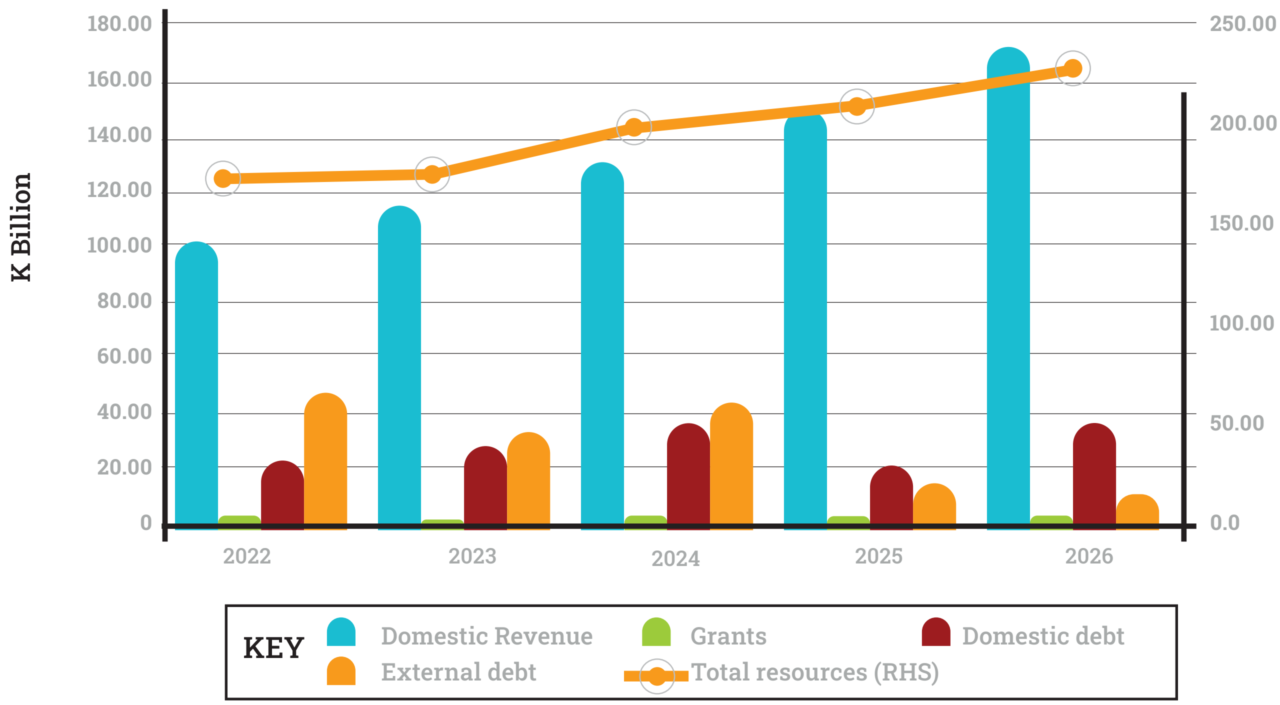
Implementation of the 8NDP will require a significant resource as shown in Chapter 2. MoFNP (2022) estimates that the 8NDP will gobble a total of K997.1 billion, corresponding to K199.4 billion per year on average as depicted in figure 4.1 below. Revenues and grants will account for 68.4 percent of the total plan

18. MoFNP did not provide details on the models

budget. The bulk of this is from domestic revenues (67.3 percent), while grants take a distant place at 1 percent of the total resource envelope. Over the plan period (2022-2026), domestic revenues are projected to maintain an upward trajectory, picking up momentum after 2024 and averaging K134.2 billion from 2022 to 2026. Predictably, grants are expected to remain flat, averaging K2.2 billion over the reference period (Figure 4.1). These resources estimates are in line with Government's fiscal aspirations of attaining fiscal sustainability through boosting domestic revenue collections. The Government is banking on bridging the financing gap of about 31.6 percent from domestic and external sources (16.4 percent).

Taken together with the analysis in Chapter 3, a closer look at the 8NDP indicates that Zambia's development finance landscape has evolved, with domestic finance occupying more room in the national resource envelope. The 8NDP projects a total resource envelope of K997.1 billion over a five-year period, dominated by domestic revenue. The yearly resource envelope is projected to increase from K172 billion in 2022 to K198 billion in 2026. While domestic revenue and grants are projected to increase over the medium term, external debt (program and project loans) is projected to decline over the period as depicted in figure 4.1 below. This evolution towards domestic revenue mobilization (DRM) is critical for Zambia's fiscal recovery and sustainability as it has implications on debt accumulation and fiscal prudence. These trends are also in line with Government's commitment to attain fiscal sustainability through enhanced DRM and switch to cheaper sources of financing such as concessional loans.

Figure 4.1: Projected Resource Envelope for 8NDP, (2022-2026)

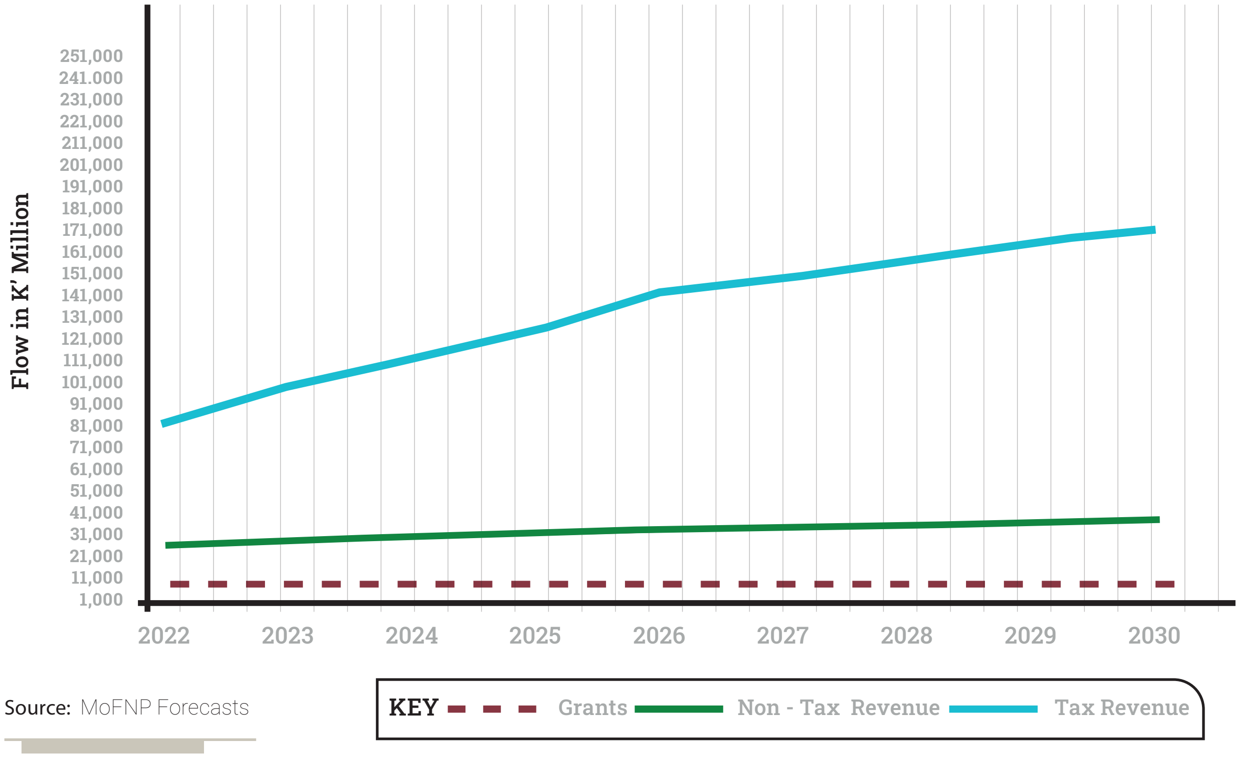


Source: MoFNP Eighth National Development Plan

The following charts (Figure 4.2 and Table 4.2.1) provide an extended forecast of revenues from 2022-2030. The trends in financing flows remain the same even when the forecast period is extended to 2030, with tax revenues maintaining prominence in the development finance portfolio and grants maintaining the lowest level on the finance ladder. As Table 4.2.1 shows, domestic revenues will account for 21.1 percent of GDP, while its constituents, tax revenue and non-tax revenue, take up 17.4 percent and 3.7 percent of GDP, respectively. This domestic revenue outlook is premised on the ongoing aggressive macroeconomic and fiscal reforms along with innovations from ZRA. While tax revenues are forecasted to improve over the period, non-tax revenues and grants are projected to stagnate over the same period. The policy and legislative gaps highlighted in Chapter 5 that are more pronounced for non-tax revenues could explain the stagnation in non-tax revenues. The projected stagnation in non-tax revenues raises concerns over Zambia's ability to attain fiscal sustainability through improved DRM.

It is also worthy pointing out that global shocks and policy gaps and instabilities, particularly in the mining sector, a key driver of domestic revenues could pose threats to the DRM outlook. Other areas of concern include the failure to broaden the non-tax revenue base and effectively tax the informal sector.

Figure 4.2: Extended Projections by type



Source: MoFNP Forecasts

Table 4.2.1 Extended Projection by Type (percent of GDP)

	2022	2023	2024	2025	2026	2027	2028	2029	2030	Average
Revenue and Grants	21.2%	22.3%	22.6%	22.8%	23.1%	22.1%	20.9%	19.6%	18.2%	21.4%
Domestic Revenue	20.9%	22.0%	22.2%	22.4%	22.8%	21.8%	20.7%	19.4%	18.0%	21.1%
Tax Revenue	16.4%	17.9%	18.2%	18.5%	18.9%	18.2%	17.3%	16.3%	15.1%	17.4%
Non-Tax	4.4%	4.1%	4.0%	3.9%	3.8%	3.6%	3.3%	3.1%	2.9%	3.7%
Grants	0.4%	0.3%	0.3%	0.3%	0.3%	0.3%	0.3%	0.3%	0.2%	0.3%

Source: MoFNP Forecasts

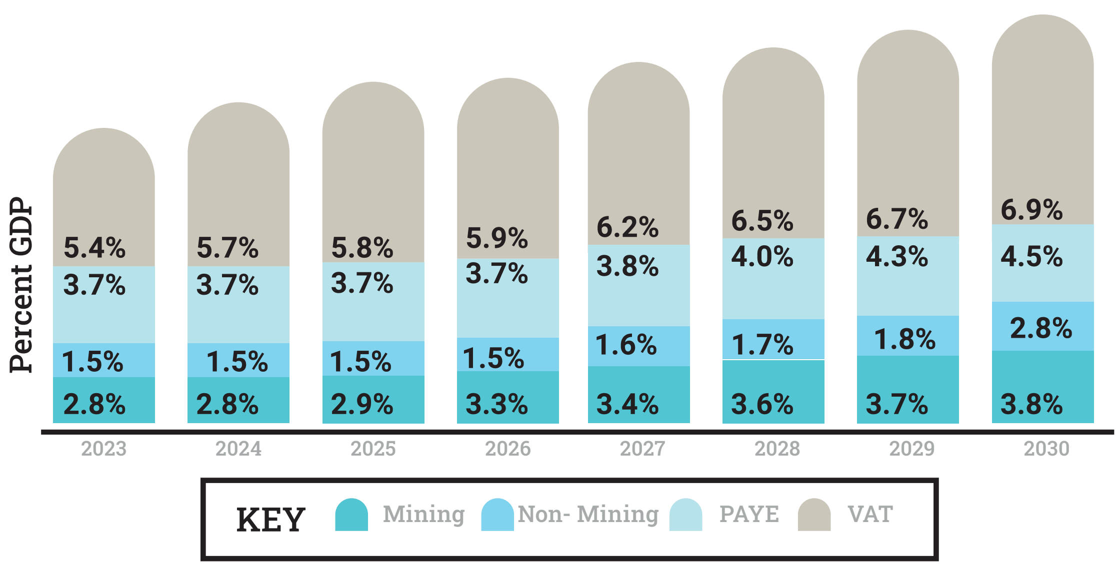
Effective planning and resource mobilization require some understanding of the resource outlook by type. Given that tax revenues command the lion's share of the domestic revenues, analysis of its main components is vital. In line with prior analysis, Zambia will continue to rely on income tax and VAT for its development financing over the next eight years (2022-2030). Income taxes account for 10.9 percent of GDP, compared to 6.1 percent for VAT. Since the mining sector is a significant contributor to these taxes, realizing these revenues will hinge on the performance of the sector. Thus, the stability of the mining fiscal regime and assurance of enabling business climate will be crucial for securing fiscal sustainability. Zambia's private sector-led development crusade offers an opportunity to broaden the corporate income tax base, with the potential to provide the much-needed insurance from the volatile mining revenue. As already pointed out in earlier sections, the mining sector is susceptible to external shocks, and this is increasingly becoming an issue with unfolding global economic events. Although Zambia has committed to trade liberalization, the analysis indicates a continued reliance on Customs and Excise Duties.

Figure 4.3: Projections for Select Tax Revenue Types, (percent of GDP)

Source: MoFNP projections

Predictive analysis indicates that Zambia continues to rely on the mining sector for its economic development agenda, revenue and fiscal sustainability. However, the country has not maximized the sector's potential to contribute to economic development and resource mobilization. The projections in Figure 4.3 present a dismal outlook, with the mining tax revenues hovering around 3 percent of GDP and averaging 3.3 percent over 2022-2030. However, VAT is projected to become a significant contributor to the tax revenue over the next eight years, averaging 6.9 percent of GDP from 2022-2030. The ongoing fiscal consolidation measures, domestic arrears dismantling efforts and IMF-backed fiscal reforms are expected to result in reduction in VAT exemptions, contributing to increased VAT collections. It is worth noting that the contribution of VAT to Zambia's fiscal envelope depends on the effectiveness of the institutions and frameworks guiding VAT tax collections. It is worth noting that the mining sector is a major play in the VAT tax collections. Further, Zambia's VAT system has faced various challenges culminating in delayed refunds and accumulation of arrears. These issues make VAT a less reliable source of revenue.

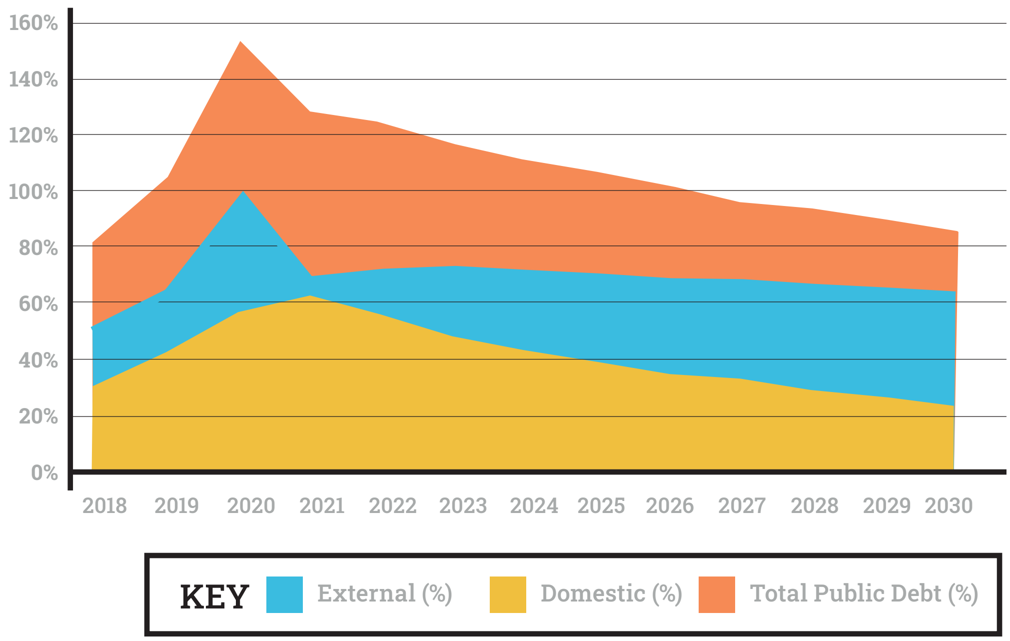
Figure 4.4: Projections for Select Taxes, (2022-2030)



Source: Authors' contruction using MoFNP Projections

In line with Zambia's renewed commitment to attaining fiscal and debt sustainability, Zambia's debt is projected to decrease steadily over the forecast horizon (Figure 4.5). While this declining trend is crucial for preventing a recurrence of debt distress, it also requires the Government to implement aggressive measures to boost domestic revenues. However, the bleak growth prospects limit how far Government revenue mobilization policies can go. Additionally, while debt accumulation is predicted to reduce significantly, the projected total public debt is still higher than the IMF's sustainability threshold of 35 percent of GDP for weak policy performers.

Figure 4.5: Zambia's Debt trajectory, (% GDP)



Source: IMF Country Report 2022 (from 2018 to 2025); Authors' estimates[19] (from 2026-2030)

4.2.2 Select International Sources

The outlook for external flows such as FDI and ODA is bleak in the medium term. This assessment is based on the recent IMF global outlook indicating global economic slowdown and the ongoing monetary tightening in major advanced economies such as the US. Further, Zambia's graduation to higher income status could further reduce some of these flows. When asked about the outlook for external financing, MoFNP officials argued that it is difficult to pinpoint the outlook given the unfolding policy shifts in advanced economies.

This DFA uses simple time series forecasting methods to project the ODA and FDI. For ODA, exponential smoothing is used to make projections up to 2030, while an autoregressive integrated moving average (ARIMA) is used to predict FDI. It is worth noting that these models do not factor in the ongoing debt restructuring and some aspects of the IMF deal.

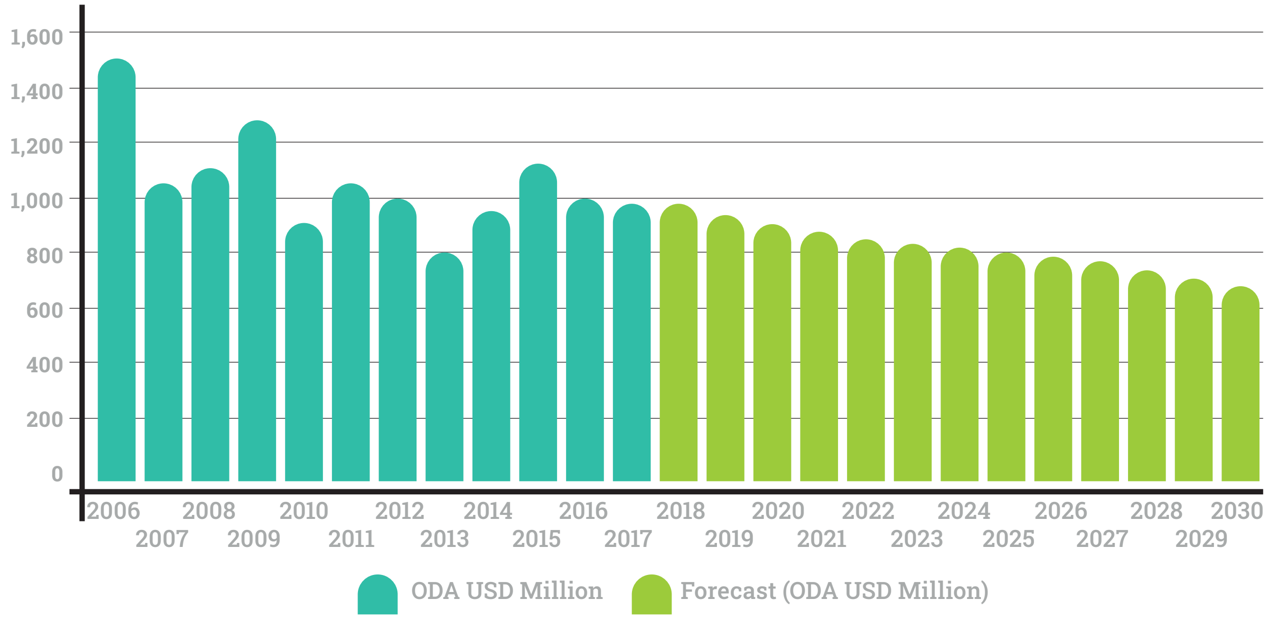
Figure 4.6 shows that ODA is expected to stabilise and taper off over the next eight years (from 2022 to 2030). The slow growth in ODA is partially attributed to the harsh global economic conditions mainly arising from the tightening financial conditions, lingering COVID-19 effects, and geopolitical tensions. However, this picture could change with successful debt restructuring and implementation of the IMF-backed program.

The prospects look much better for FDI, which has been on a sharp declining trajectory since 2013 (Figure 4.6). The slightly brighter FDI prospects can be ascribed to the recent economic recovery and macroeconomic stabilization reforms. Nonetheless, Zambia is predicted to experience FDI inflows over the next eight years. The ongoing reforms, successful implementation of the home-grown economic recovery program, and conclusion of the debt restructuring process could brighten the outlook for FDI.

19. For 2026-2030, Authors assume growth stays constant at a compunded annual growth rate

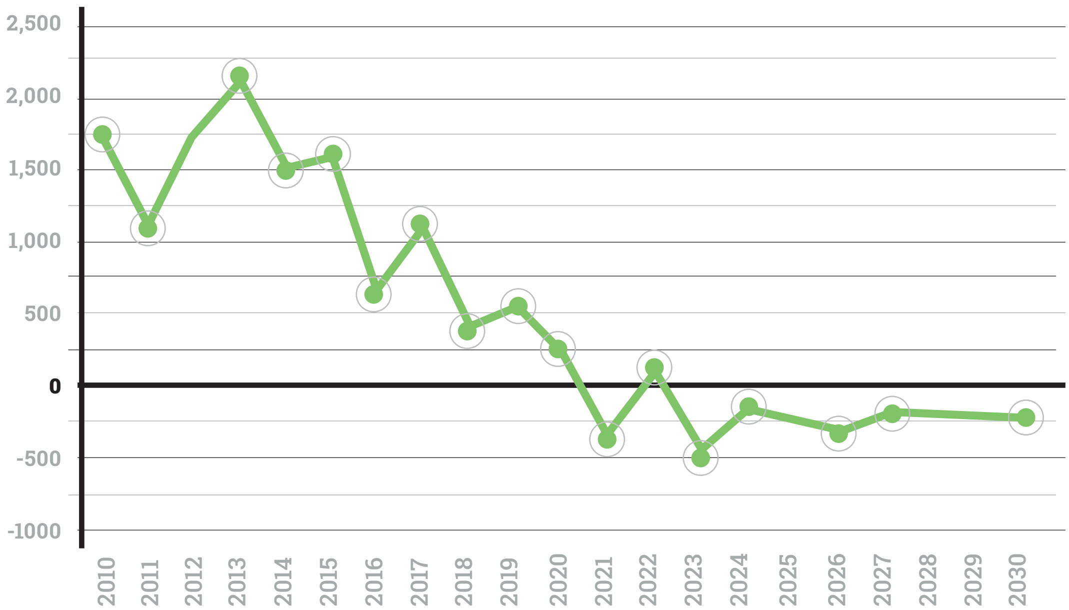
Figure 4.6: ODA and FDI Projections

Panel A: ODA



Source: Authors' estimations using simple exponential smoothing methods

Panel B: FDI (US$ Million)



Source: Authors' Computations Using the ARIMA (1,1,5) Model

Box 4.2: How does the IMF impact the development finance landscape?

Over the years, Zambia's external debt and debt servicing burdens have soared, putting the country at high risk of debt distress. The borrowing appetite was driven by an ambitious infrastructure-led development agenda, resulting in a shift from a conservative fiscal policy stance to an expansionary fiscal policy position that set Zambia on a path of excessive overspending and borrowing, which ultimately became unsustainable. **The sharp rise in debt service payments led to crowding out of other critical economic and social sectors. The COVID-19 pandemic exacerbated the acute economic and social challenges facing the country, as a result, Zambia is in debt distress, defaulting on its Eurobonds since November 2020 while also accumulating arrears to other creditors.**

Despite Zambia having hired financial advisors Lazard Frères and legal advisor White & Case, debt restructuring talks with Eurobond holders stalled in 2020, with the Bondholders citing, among other things, the agreement of a deal between Zambia and the IMF as a pre-condition for negotiating with creditors. In other words, the Eurobond creditors suspended negotiations on debt restructuring until Zambia secures an IMF deal.

Against this backdrop, an IMF program became inevitable as a catalyst to get the country on the path to recovery.

T**he 38-month, USD$ 1.3 billion IMF-supported program is based on the Zambian authorities' homegrown economic reform plan. The proposed program aims to restore macroeconomic stability and foster higher, more resilient, and more inclusive growth. With a resolution to the debt crisis, economic recovery is anticipated to continue in 2022.** Amongst other things, and in line with the nations 8NDP, the Funds program aims at (i) restoring sustainability through fiscal adjustment and debt restructuring; (ii) creating fiscal space for social spending to cushion the burden of adjustment; and (iii) strengthening governance and reducing corruption vulnerabilities, including by improving public financial management. The programs fiscal adjustments will be anchored on cutting back inefficient public investment, eliminating regressive fuel subsidies, and reforming the agricultural subsidy program by reducing procurement costs.

The IMF program provides additional benefits including technical support, expanded fiscal room and enhanced credibility **on the international stage, all of which are crucial for safeguarding macroeconomic stability, and achieving sustainable economic growth. The program will also anchor the country's debt restructuring program, freeing up resources for both social and economic spending. During the Funds program, Zambia cannot raise loans from other creditors except the multilaterals (ODA). Therefore, the country expects to record an increase in ODA in the next coming years, coupled with** increased investor confidence, ultimately increased domestic and foreign investments.

4.3 Key Takeaways

The foregoing offers the following main takeaway points:

- Tax revenues will become a more prominent source of development for Zambia for the next eight years. Grants and non-tax revenues will remain sluggish in line with recent trends.
- Zambia will continue to rely on income tax and VAT for its development financing over the next eight years (2022-2030). Income taxes account for 10.9 percent of GDP, compared to 6.1 percent for VAT.
- In general, domestic financing is predicted to take a front row in Zambia's development finance, while external financing will generally embark on a steady declining trajectory.
- ODA is predicted to be stable but subdued over 2022 to 2030. However, successful implementation of IMF-backed economic recovery program, global economic stability and attainment of fiscal and debt sustainability could brighten the prospects for ODA
- Though preliminary forecasts indicate a downward trajectory for FDI, recent economic reforms, IMF deal and renewed focus on private sector led growth could reignite FDI inflows. FDI could come from the region, as Zambia deepens ties with other countries and settles in the African Continental Free Trade Area.
- The protracted debt restructuring process, and bleak outlook for international flows could negatively impact the resource mobilization for the 8NDP.
- Going forward, the Government must interrogate its policies especially for international flows to assess their effectiveness.

05

Chapter 5: Frameworks of Financing Strategy

As with several other countries in the world, the Zambian government has a strong desire to ensure that the country's economic prosperity and recovery from the country's debt crisis, COVID-19 pandemic, climate related impacts and geopolitical tensions is characterised by greater resilience, inclusivity and sustainability. To achieve this, the country requires a clear and comprehensive financing strategy for both private and public sector players, to underpin its development agenda. This chapter examines the overall policy landscape for the main private and public financing flows in Zambia. It also describes the institutional and regulatory framework for resource mobilisation in Zambia.

5.1 Frameworks for Mobilising Public Finance

5.1.1 Institutional Arrangements

Key institutions in Zambia's PFM and revenue mobilization include MoFNP, Ministry of Local Government and Rural Development (MLGRD), National Assembly, Auditor General's Office, other line ministries, NRFA, government agencies and statutory bodies, civil society, research institutions, academia, cooperating partners (CPs), and NGOs. The MoFNP—along with its statutory bodies— plays a central role in PFM (Table 5.1.1).

Table 5.1.1 Institutional Arrangements for PFM

Agency	PFM Role
MoFNP	Overall coordination, planning, policy formulation, implementation, and financial management
BoZ	Monetary policy and financial system stability
ZRA	Tax administration
ZPPA	Regulation of public procurement
Pensions and Insurance Companies	Mobilising resources
SEC	Regulator of the Capital Markets in Zambia
MoLGRD	Mobilising resources at local authority level
National Assembly	Provides fiscal oversight
Non-Tax collecting Govt. Agencies (MPSA)	Ministries, Provinces and Spending Agencies develop plans and budgets at various levels and collects revenues at various levels
Auditor General	Auditing use of public resources
NRFA	Administer and manage the road fund

Source: Authors' adaptations based on the 2017 Public Finance Management Handbook & MoFNP Reports

5.1.2 Legal and Policy Framework

Frameworks for PFM

Resource mobilization is a crucial component of PFM. Hence, it is important to highlight key pieces of legislation for PFM. Zambia has a number of legislations that provide for the management and mobilization of its public finances. Some of the legislation also touch on key aspects of development finance in general.

Of all legislation, the National Planning and Budgeting Act No.1 of 2020 and the Public Debt Management Act of 2022 are amongst the most consequential for development finance as they touch on critical elements of public finance, such as debt management and integrated planning and budgeting. Other policies that speak to various aspects of revenue mobilization and PFM issues are the National Financial Sector Development Policy 2017, and the National Payment System Vision and Strategy 2018–2022, among others. The pieces of legislation are summarized in Table 5.1.2.

Table 5.1.2 PFM Legislation

LEGISLATION	OBJECTIVE
1. The Constitution of Zambia (Amendment), Act No. 2 of 2016	The Constitution is the supreme law of the Republic of Zambia and any other written law, customary law and customary practice.
2. Public Audit Act, 2016	Makes certain provisions relating to the duties and powers of the Auditor-General in auditing public institutions.
3. National Planning and Budgeting Act, 2020	Provides a framework for an integrated planning and budgeting process which espouses a participatory and decentralized approach to national planning and budgeting.
4. Public Debt Management Act, 2022	Primary legislation on debt management authority for the Minister of Finance. The Act provides for the raising of loans, the establishment of sinking funds, the giving of guarantees and indemnities and the granting of loans by or on behalf of the Government.
5. Public Finance Management Act, 2018	Provides for the control and management of public finances, as well as audit of all public accounts.
6. Public-Private Partnership Act, 2009	Currently under review but it provides for public-private partnerships for the construction and operation of infrastructure facilities and systems and for the development of general principles of transparency, economy, and fairness in the awarding of contracts by public authorities. The Act also provides for rules governing procurement, contracting and management of public-private partnerships.
7. National Road Fund Act, 2003	This law established the National Road Fund Agency (NRFA) for use in the construction, maintenance, and care of public roads as well as to manage traffic and safety in the road transport sector.
8. The Rating Act, 2018	Provide for the levying of rates; provide for the assessment of ratable property, plant and machinery; provide for the appointment and powers of valuation surveyors; provide for the continuation of the Rating Valuation Tribunal and revise its composition, jurisdiction and powers.
9. Public Procurement Act No.8, 2020	This law regulates and controls practices relating to public procurement in order to promotethe integrity, fairness and public confidence in the procurement processes.

Source: Author's contruction from various sources

Legal Frameworks for Tax Revenues

Central Government Taxes are collected by ZRA, a corporate body mandated to collect all national taxes. The tax types are governed by primary tax legislation, subsidiary legislation and annual practice notes which detail the ZRA's interpretation of changes in tax laws. The Direct Taxes Division of the ZRA is mandated to administer and collect income taxes as provided for under the Income Tax Act, Chapter 323; and the Property Transfer Tax Act, Chapter 340. The Division also administers Mineral Royalty, as provided for under the Mines and Minerals Development Act No. 11 of 2015, Tourism Levy pursuant to the Tourism and Hospitality Act No. 13 of 2015 and Skills Development Levy pursuant to the Skills Development Levy Act No. 46 of 2016.

The Indirect Taxes and Excise Division of the ZRA is responsible for administering inland consumption taxes as provided for under the Value Added Tax Act Chapter 331; the Insurance Premium Levy Act No. 21 of 2015; and the Customs and Excise Act Chapter 322 to administer Local Excise. The Customs Services Division is responsible for administering trade taxes, fees and charges as mandated under the Customs and Excise Act Chapter 322.

The Local Government Act No.2 of 2019 provides for an integrated local government system; decentralisation of functions, responsibilities and services at all levels of local government; and provides for the review of tariffs, charges and fees within the area of a local authority among other things.

Although the frameworks highlighted above mainly cover public finances, some aspects also touch on private finance. For instance, the BoZ also presides over domestic and international private finance, and these include, the Securities Act CAP 354 of the Laws of Zambia where all securities that are issued and traded are regulated; the Banking and Financial Services Act CAP 387 of the Laws of Zambia gives the Bank of Zambia the mandate to act as the fiscal agent for the Government; and the Pension Scheme Regulation Act CAP 255 of the Laws of Zambia.

Legal Frameworks for Non-Tax Revenues

Non-tax revenues are much more varied than tax instruments. They include royalties for fees for mining rights, dividends on Government investments in State-Owned Enterprises (SOEs) and in stock portfolios. Other sources include user fees and fines, construction permits among others.

User fees are charges levied against individual consumers of publicly produced services and commodities and publicly granted privileges on a cost per unit basis (Giacoma, 1990). In the Zambian context, user fees, fines and charges are governed by the Fees and Fines Act No.11 of 2013, which provides for the amount of fees and fines to be expressed in terms of the fee units and penalty units; to provide for the amounts of existing fees and fines to be converted into fee units and penalty units; and to provide for matters connected with or incidental to the foregoing.

Table 5.1.3 gives the broad tax and non-tax categories in Zambia, the laws underpinning revenue collections and the types of taxes/non-taxes under each category. The list, however, is not exhaustive of all the Acts governing non-tax revenues in Zambia, but merely highlights on a few critical ones.

Table 5.1.3 Tax Category, Legal Framework and Tax type

Broad Category	Category	Primary Legislation	Subsidiary Legislation	Type
Direct Taxes	Income taxes	Income Tax Act Chapter 323 of the Laws of Zambia		▪ Company Income Tax ▪ Personal Income Tax ▪ Pay As You Earn ▪ Withholding tax ▪ Presumptive Tax ▪ Turnover Tax ▪ Base Tax
	Property Taxes	Property Transfer Tax Chapter 340 of the Laws of Zambia		Property Transfer Tax
Indirect Taxes	Value Added Tax	Value Added Tax Act Chapter 331 of the Laws of Zambia		Domestic VAT Import VAT
	Customs, excises, and other duties	Customs and Excise Act Chapter 322 of the Laws of Zambia		▪ Customs Duty ▪ Excise Duty ▪ Export Duty ▪ Carbon Emissions Surtax
Non-tax Revenue	Mineral Royalties	Mines and Minerals Development Act, 2015	Income Tax Act Chapter 323 of the Laws of Zambia	Mineral Royalties
Other Non-Tax	Fees, fines, charges and dividends from SOE	The Rating No. 21 of 2018 among other Acts; Toll Act No.14 of 2011; Road Traffic Act No.11 of 2002		▪ Land rate ▪ Toll fees ▪ Fees and fines ▪ Dividends from SOE

Source: Author's contruction from various sources

Gaps in the Frameworks

The weakness in the institutional framework mainly emanates from the multiplicity of actors in revenue mobilization, creating coordination challenges. The fragmentation is more pronounced in nontax revenues where various institutions are involved in revenue administration and management. Additionally, there is lack of clarity on the role of Local Authorities (LAs) in-revenue collection, contributing to depressed non-tax revenues and LA own source revenues.

Further, inadequate capacities in various institutions tasked with revenue administration such as ZRA, and NRFA, aggravate the institutional weaknesses.

5.1.3 Main Impediments to Resource Mobilisation

Domestic resource mobilisation in Zambia faces several challenges and these can be categorised into macroeconomic factors, government and taxpayers' behaviours, policy frameworks, and institutional capacity. These challenges are compounded by demographic factors, low-income levels and the structure of financial markets. The very fact that Zambia has a young population who are mostly unemployed makes the revenue base even narrower and therefore affects the domestic resource mobilisation efforts. We group the impediments into the following subcategories.

Weak Policy Frameworks

Zambia's current policy landscape requires enhancement in order to support an integrated approach to revenue mobilization. The closest Zambia comes to integrating public resource management is the MTBP, which includes aspects of revenue mobilization strategies. The policy gaps are reflected in the multiplicity of actors in the public finance space, contributing to inefficiencies in revenue collections.

Hard-to-tax Informal Sector

Zambia as with other African countries is characterised by a hard-to-tax informal sector. Particularly, the sectors and activities characterized by high levels of informality include the agriculture, forestry and fishing, and the wholesale and retail trade industries as depicted in Table 5.1.4 below. In the past few years there has been a search for economic opportunities, and this led to a rural-urban drift, as most people are abandoning the low-productivity subsistence agriculture in rural areas to urban areas. According to the 2020 Labour Force Survey, 73.8 percent of the Total Labour Force in Zambia are in informal employment not far from the African share of 85.8 percent. Of this, 94 percent of those employed in the wholesale and retail trade were informally employed- other service activities accounted for 87 percent while domestic workers accounted for 85 percent. The informal sector is generally characterised by low compliance, contributing to the stagnation in revenues highlighted in Chapter 3.

Table 5.1.4 Labour Force Sectoral composition

	Formal		Informal		Total	
	Number	Percent	Number	Percent	Number	Percent
Total	776,160	23.7	2,496,963	76.3	3,273,123	100
Agriculture, forestry and fishing	70,728	9.8	650,718	90.2	721,446	100
Mining and quarrying	41,118	69.3	18,253	30.7	59,371	100
Electricity, gas, steam and air conditioning	4,576	90.1	503	9.9	5,079	100
Construction	18,427	11.6	140,504	88.4	158,931	100
Wholesale and retail trade	55,557	6.1	858,410	93.9	913,967	100
Real estate activities	0	0.0	18,469	100	18,469	100
Education	139,807	87.4	20,145	12.6	159,952	100
Arts, entertainment & recreation	5,349	28.9	13,137	71.1	18,486	100
Other service activities	7,636	6.0	120,245	94.1	127,881	100
Activities of households as employers	16,942	16.0	88,877	84.0	107,819	100
Activities of extraterritorial organizations and bodies	1,822	100	0	0.0	1,822	100

Source: 2022 Zambia Labour Force Survey

Fiscal incentives

The Zambian government has over the years introduced tax incentives to stimulate economic growth and attract FDI. The mining sector has been a major beneficiary of these incentives. However, there is inadequate information on the detailed design and duration of the incentives. The lack of transparency has the potential to adversely impact tax compliance, contributing to slowed revenue growth.

Additionally, while the revenue losses from the tax incentives are well documented in national documents (National Budgets), there is no system to monitor effectiveness of these incentives in spurring economic growth.

Further, the fiscal incentives are a huge drain on revenues. According to ZIPAR (2021), tax concessions in the 2022 Budget reduced total revenues by 5.9 percent.

Complex tax codes

Complex tax systems contribute to low compliance levels and low revenues. For instance, the CIT rate schedule has a multiplicity of tax rates which generate distortions and are prone to arbitrage, avoidance, and revenue leakage. Complex tax schedules also present administration challenges, further compounding compliance issues.

Policy inconsistency

Unstable fiscal regimes have been a characteristic of the mining sector, resulting in low tax collections. Zambia has one of the most volatile mining tax regimes in Africa. The country changes it's mining tax, on average, every eighteen months, which is above the African average and only second to Ghana (Siwale & Chibuye, 2019). These mining tax instabilities are costly to the country of which. 300,000 MT of copper or USD$300 million annually has been estimated to be lost due to mining tax policies that are tied to copper prices and political cycles.[20]

Inadequate infrastructure

Infrastructure is crucial for revenue mobilization. However, Zambia's infrastructure is inadequate and in a need of upgrading, contributing to revenue underperformance. Being land-linked, Zambia is uniquely positioned to raise revenue through trade and road fees. By improving trade infrastructure, Zambia could broaden its revenue base and boost revenue mobilization.

Capacity constraints

Although ZRA has made progress in enhancing its capacities, along with making various institutional innovations, other institutions involved in revenue mobilization face capacity constraints. For instance, the Ministry responsible for mines, a crucial player in mobilization of revenues from the extractive industry has concerning capacity issues in areas such as mineral content valuation, data analytics and generally difficult in keeping up with innovations in the sector. Other key players in revenue mobilization such as law enforcement agencies are also ill-capacitated to monitor and prosecute Illicit Financial Flows.

Illicit Financial Flows

Illicit Financial Flows (IFFs) refer to illegal, unrecorded or wrongly recorded transfer of capital from an economy[21]. IFFs result in a loss of what are often desperately needed resources to fund public initiatives or critical investments, and this undermines the efforts of countries to mobilize more domestic resources in order to meet the internationally-agreed Sustainable Development Goals (SDGs) by the target date of 2030.[22]

Over the years, IFFs continue to be a serious concern in Zambia. In order to track IFFs in Zambia, the Zambian authorities set up the Financial Intelligence Centre (FIC). FIC was constituted to complement and support the work of the Law Enforcement Agencies such as the Financial Crimes Court which is under the Judiciary) and the Drug Enforcement Commission (DEC) and the Anti-Corruption Commission (ACC) which are commonly known as the investigative wings. FIC tracks IFFs and produces a trends report which covers matters that have been referred to and may be under active investigation by the investigative wings. For instance, there was an increase in IFFs from K4.5 billion in 2017 to K6.1 billion in 2018 as shown in Table 5.1.5. In 2019, IFFs reduced to K984 million in 2019, and this was on account of having more individuals than corporates which usually have higher values. However, IFFs increased in 2020 to K3.1 billion due to an increase in corruption and illegal mining in precious metals and stones.

20. Mwaba & Kayizzi-Mugerwa (2021). Boosting Mineral Revenues in Zambia
21. https://www.imf.org/en/About/Factsheets/Sheets/2023/Fight-against-illicit-financial-flows
22. https://gfintegrity.org/issue/illicit-financial-flows/

Table 5.1.5 Losses due to IFFs in Zambia, 2017 - 2020 (K' Millions)

	2017	2018	2019	2020	2021	2022
Tax Evasion	3,900	1,000	1,889	719	1,067	1,342
Corruption	500	4,795	332	2,232	1,287	1,664
Fraud	3	110	1,113	26	302	21
Money Laundering	91	195	450	466	1,628	3,031
Illegal mining in precious metals and stones	0	0	0	165	0	0
Others	0	0	3	53	91	1
Total	4,494	6,100	3,787	3,142	3,474	6,059

Source: FIC Annual Reports

Legal Framework for IFFs

Zambia has made progress in strengthening the regulatory framework to curb IFFs addressing revenue leakages. The main pieces of legislation guiding IFFs and Anti-Money Laundering and Counter Financing of Terrorism (AML/CFT) include:

a) Public Procurement Act No 8 of 2020
b) Public Finance Management Act No 1 of 2018
c) Prohibition and Prevention of Money Laundering Act No 14 of 2001, amended by Act No. 44 of 2010:
d) Anti-Terrorism Act No 21 of 2007
e) Forfeiture of Proceeds of Crime Act No 19 of 2010
f) Financial Intelligence Centre Act No 46 of 2010
g) The Public Interest Disclosure Act No. 4 of 2010
h) Mutual Legal Assistance in Criminal Matters Act No. 19 of 1993;
i) The Plea Negotiations and Agreements Act No. 20 of 2010; and
j) The Anti-Corruption Act, No. 3 of 2012 (replacing the Anti-Corruption Act, No. 38 of 2010).

Anti-Money Laundering and Counter Financing of Terrorism Institutional Framework

Some of the key policy AML/CFT institutions in Zambia include the following:[23]

Table 5.1.6 Institutional Arrangements for AML/CFT

Institution	Legislation	Role
Anti-Money Laundering Authority (AMLA)	Prohibition and Prevention of Money Laundering Act, No. 14 of 2001	Policy guidance and advise Government on measures required to prevent and detect money laundering
The National Task Force of Senior Officials on AML/CFT Matters	Prohibition and Prevention of Money Laundering Act, No. 14 of 2001	To coordinate AML/CFT matters among key stakeholders with a view to improving the effectiveness of existing policies to combat money laundering, financing of terrorism and other serious offences
Financial Intelligence Centre (FIC)	Financial Intelligence Centre Act No 46 of 2010	Coordinates the receipt, analysis and dissemination of suspicious transaction reports to Law Enforcement Agencies (LEAs) and other foreign designated authorities
The National Prosecution Authority (NPA)	Section 82 of the Criminal Procedure Code, Chapter 88 of the Laws of Zambia	Main mandate for all prosecutions in the Country. Also hosts the Office of the Director of Public Prosecutions (DPP)

Source: Authors illustrations based on Stakeholder Consultations

23. https://www.fic.gov.zm/aml-cft-framework

Other key institutions playing crucial roles in curbing IFFs include:

a) **Law Enforcement Agency (LEAs)** which comprise the following institutions (with accompanying legislations):
   - The Zambia Police Service (the Constitution);
   - The Zambia Security Intelligence Service (Zambia Security Intelligence Act);
   - The Immigration Department (Immigration and Deportation Act of 2010);
   - The Drug Enforcement Commission (the Narcotic Drugs and Psychotropic Subsistence Act);
   - The Anti-Money Laundering Investigations Unit (the Prohibition and Prevention of Money Laundering Act, 2001);
   - The Anti-Corruption Commission (the Anti-Corruption Act, 2010); and
   - The Zambia Revenue Authority (Zambia Revenue Authority Act).

b) **The Judiciary:** Plays critical role in the prosecution of cases and recovery of stolen assets and funds.

5.1.4 Innovations and Reforms for Domestic Revenue Mobilization

So far, this report has demonstrated that there are still several constraints to the Government's revenue mobilisation efforts. The report also shows that in a bid to supplement domestic resources which have historically been inadequate to finance the country's development agenda, Zambia has hard to turn to external sources to finance development and social programs. However, the Government recognises that there is still scope for enhancing domestic resource mobilisation more innovatively and sustainably. In this regard, the country continues to explore different innovations, reforms and strategies for revenue mobilisation.

In recent years, the Government sought to improve tax administration by streamlining the tax system and creating a stable and predictable tax environment. In particular, the Government has continued to rely on ICT including innovations such as the ZamServices Portal and the adoption of online and e-services at the Zambian Revenue Authority. The main innovations and strategies are detailed below.

The ZamServices Portal

The Government, through MOFNP and in collaboration with Smart Zambia introduced an online payment solution under an integrated system called the Government Service Bus (GSB). The system was designed to be accessed across the country and improve service delivery and provision to the general public. Within this system is the ZamServices Portal, which is an electronic catalogue of public electronic services provided by authorities to the citizens, the business environment and to the visitors of Zambia. The portal provides for the use of on-line payments for services requested on-line, and therefore increases digitization, contributing increased efficiency in revenue collection.

GSB has a potential revenue impact through integrated data sharing. However, delayed integration and implementation of data sharing among institutions that have been loaded on the GSB is adversely impacting its potential to boost revenue collection.

Innovations at ZRA

In recent years, ZRA has embarked on using ICT and e-services to enhance revenue collection in the country. This has included the adoption of the Bulk Intelligence Data Analysis (BIDA) system, the use of Electronic Fiscal Devices, TaxOnphone, TaxOnApp and payment via WhatsApp to ease tax administration and tax compliance. The Authority is also looking to replace the Automated System for Customs Data (ASYCUDAWorld system) and has had to develop a customs module on the TaxOnline system. ZRA has noted that this has seen more taxpayers come on board, in addition to an increase in returns being filed. The Authority further noted that there is need for further enforcement and education of taxpayers to realise the full benefits of these systems.

ZRA has also undertaken various innovations, including capacitating staff in data analytics and auditing. The innovations are aimed at enhancing their capacity to curb revenue leakages, especially the IFFs. Key innovations include the creation of the Mining Tax and the Transfer Pricing Units, and the Mineral Output Statistical Evaluation Strategy (MOSES). These innovations are generally aimed at enhancing tax compliance among mining companies.

a. TaxOnline, TaxOnPhone and TaxOnApp

In 2020, ZRA implemented the TaxOnline system that enables taxpayers to process their registrations, filing and payments online. It also launched the TaxOnApp system which provided an internet based mobile application designed for small and medium taxpayers. It was designed to improve compliance for both customs and domestic taxes. It includes services such as registration for a Taxpayer's Identification Number (TPIN) and tax type registration or deregistration, returns filing, tax payments, tax education and search for a Customs bill of entry. There was also the introduction of payment of taxes through the WhatsApp online application.

b. Electronic Fiscal Devices

ZRA also procured and distributed electronic fiscal devices (EFDs) in 2018 meant to enhance compliance in the administration of Value Added Tax (VAT). These are meant to replace the use of manual cash registers for business transactions for registered taxpayers, and to provide an enhanced level of security in the recording sales transactions. In addition, the Authority introduced the Tax Invoice Management System (TIMS) making it mandatory for every taxpayer registered for insurance premium levy, tourism levy and VAT to install and use Electronic Fiscal Devices (EFDs) as provided for in the VAT Act, Cap 331 of the Laws of Zambia.

c. Advances in tax collection in the Mining Sector

In 2018, the Authority commenced the roll out of an export permit module under the Mineral Output Statistical Evaluation System (MOSES) that would allow for reduced processing time for export permits and the elimination of costs associated with the manual processing.

d. Advances in Taxing Small and Medium Taxpayers

A number of efforts are being made to improve taxpayer services and therefore tax compliance among Small and Medium Taxpayers. In 2017, for instance, the Authority working with GIZ procured and installed automated modern queue management systems at the Kitwe and Ndola offices, and also commenced the development of a mobile phone-based e-tax solution for SMEs called Zambia Mobile Electronic Taxation (ZAMeT) Project. This was done to help reduce costs in tax compliance by increasing the range, quality, and uptake of e-services.

The Authority has also used TaxOnphone to allow taxpayers to access ZRA services such as registration, filing of tax returns and reviewing of their tax compliance status on a mobile phone or other similar devices without using the internet. The system utilises an Unstructured Supplementary Service Data (USSD) platform.

5.1.5 Frameworks for Government Borrowing

Zambia's economic recovery efforts will greatly benefit from a strengthened institutional and regulatory framework for debt contraction and management. The MoFNP has the main mandate for debt contraction, while the Ministry of Justice and BoZ offer institutional support by ensuring transparency in the financing process and enhancing the impact of various monetary instruments on the economy, respectively. Another key player is the National Assembly which provides oversight on budgets and budget execution rates, and approval of the annual borrowing plan.

The key pieces of legislation guiding debt management over the study period include Constitution (Amendment) Act No. 2 of 2016, and the Public Debt Management (PDM) Act No. 15 of 2022.

The PDM Act No. 15 of 2022 which repealed the Loans and Guarantees Authorisation Act addresses the gaps in the regulatory and institutional frameworks around debt management by strengthening parliamentary oversight in the debt contraction process, and setting debt ceilings. The Act provides for resource mobilization through loans and grants, issuing of guarantees, approval of loans, establishment of sinking funds and Debt Management Office, among others. Specifically, Article 4 of the Act specifically states that "The Minster shall, not later than ninety days before the commencement of the next financial year, lay the annual borrowing plans before the National Assembly". Further, Article 6 states that "The National Assembly shall, by resolution of the Members of Parliament, approve the annual borrowing plan for the next financial year". The legislation also mandates the ministry of finance to publish very specific information on debt and also present it before the National Assembly. In addition, the PDM Act No.15 of 2022 prescribes for the preparation of a Medium-Term Debt Strategy (MTDS), which was missing in the Loans and Guarantees Authorisation Act. According to PART III Section 4 (1) of the PDM Act states that ***"The Minister shall cause the preparation of a Medium-Term Debt Strategy for the management of Government debt, in accordance with section 3, for Cabinet consideration and approval".*** The preparation of the Debt Sustainability Analysis (DSA) is carted for under PART IX of the Act. These provisions are crucial for promoting accountability and transparency in debt contraction, contributing to fiscal prudence.

Therefore, the PDM Act plugs the main gaps in the frameworks for debt management, providing guardrails against debt distress and fiscal crisis. However, challenges remain with regards to specifics on subnational debt contraction, and the enforcement of the legal provisions. Other risks include fragile macroeconomic environment and other economic vulnerabilities that have fiscal implications. In times of economic slowdown, fiscal gaps, and weaker supporting legislations and governance systems, the existing laws may not withstand the pressure from multiple fronts.

The Government has also taken concrete steps to improve debt governance systems through promoting transparency and accountability. This includes publishing debt information and reports such as Medium-Term Debt Strategy, Debt Reports, Debt Sustainability Analysis Reports, Annual Borrowing Plans, and statistics.

Going forward, a developmental vision protected by law should be put in place that will ensure that the country is always on the right developmental course irrespective of political cycles and this will ensure borrowed funds are rightly channelled in the future.[24]

5.1.6 Key Takeaways

The key takeaways include the following:

- Zambia has requisite frameworks for mobilization and management of public finances, However, the multiplicity of actors present coordination challenges.
- There have been aggressive reforms and innovations toward enhancing domestic revenue mobilization with most efforts have centred on tax revenues.
- A large and hard-to-tax informal sector is major challenge that contributes to narrow tax base and low domestic revenues.
- Widespread use of tax incentives contribute to low revenue collections.
- Gaps in frameworks including fragmentation are more pronounced in the non-tax revenues
- Although still underperforming, SOEs are behind the subdued non-tax revenues, the frameworks around management of SOEs are inadequate.
- Revenue leakages from tax avoidance and IFFs are a huge threat to fiscal sustainability.
- Fragmentation and capacity gaps in relevant institutions such as the ministry of mines contribute to revenue leakages and low tax collections.
- Zambia has strengthened its framework for debt contraction by repealing the Loans and Guarantees Authorisation Act and enacting the Public Debt Management (PDM) Act No. 15 of 2022 which ensures the restoration of debt sustainability, enhanced transparency and accountability.

24. Ministry of Finance stakeholder engagement

- Zambia's debt markets are underdeveloped, and there is no clarity on sophisticated debt arrangements such as debt swaps.

5.1.7 Recommendations

The following recommendations are put forth:

- Strengthen the frameworks for mobilization and management of public finance to address coordination challenges by taking the following actions:
  - Capacitate revenue collection institutions in information management.
  - Improve data and information sharing among institutions involved in revenue collection.
  - Strengthen coordination between MoFNP and other institutions involved in revenue collection.
  - Review the existing legislation on revenue collection with a view to strengthen coordination amongst the various players involved in the revenue collection.
  - Leverage existing systems such as the GSB to improve service delivery in order to maximise revenue collection.
- **Devise measures to boost domestic revenues, focusing more on non-tax revenues:**
  - Establish an institution to coordinate the administration of non-tax revenues.
  - Leverage ICTs, business groups/associations and CDF to bring the informal sector into the tax net
  - Review of the performance of SOEs to get a better understanding of the reasons for their underperformance.
  - Review IDC's capacity to promote growth of SOEs.
  - Expedite the rollout and integration of ZRA systems on the GSB to sharpen the effectiveness of the GSB.
  - Rationalise the use of fiscal incentives, and increase transparency in their applications.
- **Curb IFFs:**
  - Develop a policy and legal framework to compel LEAs to integrate and share information.
  - Invest in automation and information sharing among LEAs for easier tracking and monitoring illicit financial flows.
  - Enhance the capacity of LEAs through increased resource allocation and provision of technical support to sharpen their investigation, prosecution, and asset recovery capabilities.
  - Capacitate relevant institutions in product/service evaluations and analysis to curb IFFs.
- **Enhance the management of debt:**
  - Government must deepen debt markets to exploit sustainable debt management options such as debt swaps (e.g., debt-for-climate swaps)
  - Further strengthen accountability and transparency in debt management, focusing on the utilization of debt funds. This can be done by expanding the publication of debt statistics, publishing financing gaps by sector, and sensitizing the public on debt management.
  - Review existing frameworks to clarify provisions for debt management at subnational level.

5.2 Frameworks for Development Cooperation

Given Zambia's fragile macro-fiscal environment, ODA is poised to remain a critical source of financing for social and economic programs. This section highlights the institutional and legislative frameworks governing Zambia's development cooperation and mobilization of international flows.

5.2.1 Policies, Institutional and Legislative Frameworks for Development Cooperation

The Ministry responsible for Finance oversees the coordination of development cooperation through implementation of development cooperation policies and strategies so as to ensure effective targeting of development assistance. The Ministry is also responsible for developing, coordinating and managing official development assistance (ODA) flows to the country, mobilizing and allocating external resources as it enters into loan and grant agreements with various development partners.[25] Other institutions that play crucial roles in mobilising international flows include BoZ and the Ministry responsible for foreign affairs among others.

Zambia's policy framework for development cooperation is outdated and weak. To the authors' knowledge, the Aid Policy and Strategy drafted in 2005, and finally approved in 2007 is the only framework guiding development cooperation for Zambia. The Policy was formulated with a focus of reorienting the states administration, particularly the financial system, so as to meet prerequisites for improving efficiency and effectiveness of development cooperation. It offers guiding principles for aid policy, thereby providing a framework for interactions between government and its CPs.[26] The Policy makes commitment to strengthening Governments planning, budgeting and financial management systems so as to maximise the country's capacity to optimally utilize domestically and externally acquired resources.

In line with Zambia's Aid Policy, the Ministry of Finance's responsibilities include: mobilization of resources from development partners, maintain a database on all funded projects and programs, and monitoring financial and operational performance of all existing multilateral and bilateral agreements[27]. Furthermore, the Policy mandates domestic and external development efforts to be treated in the same manner and to be based on priorities that are set by national development planning and budgeting processes.[28] Thus, the assistance must be demand driven and integrated into government's national capacity building strategies.

However, weaknesses were noted regarding policy implementation, which included deficit political will, especially around leadership of aid management, inadequate dialogue, coordination and information sharing as well as capacity building and retention. This was in part because the Aid Policy of 2005 did not include an implementation as well as coordination framework.[29]

In order to strengthen relations between Zambia and cooperating partners, the Joint Assistance Strategy for Zambia (JASZ) was formulated and this ran from 2007 to 2010. The Strategy provided for a substitute for all separate strategies of various cooperation partners. The JASZ signatories included 12 bilateral donors, the UN, World Bank, African Development Bank and the European Union. The JASZ like the Paris Declaration that emphasizes local ownership of developmental processes and the enhancement of aid effectiveness. It also represented CPs joint response to Zambia's Vision 2030, its 5NDP and Aid Policy and Strategy which altogether made up a national framework for poverty reduction and sustainable development promotion.[30] In line with the Zambia Aid Policy, JASZ mandated Government to align external assistance with well-established and functioning governance system while requiring CPs to improve funding predictability and alignment to the Country's development plans.

An update from the JASZ was the JASZ II, which was formulated to support Zambia's 6NDP for the period 2011-2015. This was to provide a medium-term framework to realise principles and align development assistance to Zambia's Aid Policy and Strategy. The JASZ II built on the first JASZ aimed at supporting efforts to address rural poverty and inclusive growth, support Zambia's longer-term transition from ODA, improve the flow and quality of information and dialogue between Government and cooperating partners.

25. Ministry of Finance and National Planning
26. Saasa and Wohlgemuth (2008) Changing Aid Relations in Zambia
27. Thomson et.al (2010). Evaluation of the Joint Assistance Strategy for Zambia 2007-2010
28. Ibid.
29. Thomson et.al (2010). Evaluation of the Joint Assistance Strategy for Zambia 2007-2010
30. Saasa and Wohlgemuth (2008) Changing Aid Relations in Zambia
31. Stakeholder Consultation- Ministry of Finance

Currently, Zambia is in the process of drafting the National Policy on Development Cooperation. This Policy would outline the country's focus in terms of development cooperation and how ODA is envisaged to support the attainment of Zambia's development plans. The drafting of the Policy will be done through the integration of wider mechanisms of development assistance that are implemented in a coordinated manner. This is in order to enhance efficiencies in managing aid to achieve broad based greener growth and wealth creation.[31]

5.2.2 Key Takeaways

- The policy, legislative and institutional frameworks for development cooperation and international resource mobilization are weak and outdated.
- The gaps in the frameworks, manifesting in fragmentation present challenges for effective mobilization of international resources, including ODA.

5.2.3 Recommendations

- Government must review and update frameworks to safeguard and attract concessional financing. This entails expediting the finalization of the National Policy on Development Cooperation.
- Strengthen coordination and information sharing between government and CPs to optimize international flows. One way is to enhance the capacities of the MoFNP Development Cooperation department, and line relevant ministries (responsible for foreign affairs, trade and investment, social sectors).
- Enhance transparency in utilization of development finance by availing information on financing gaps by sector.

5.3 The Frameworks for Private Finance

Most of the frameworks highlighted in this subsection pertain to domestic private finance, albeit with indirect consequences for international private finance. The frameworks are detailed in the ensuing subsections.

5.3.1 Overall Frameworks for Domestic Private Finance

The overall strategic guidance and coordination of the financial sector in Zambia is done by the MoFNP through the National Financial Sector Development Policy (2017) and the National Financial Inclusion Strategy (2017 - 2022).

In terms of regulation, there are three main regulators of the financial sector as follows:

i. The Bank of Zambia (BoZ): Responsible for monetary and supervisory policy, regulates banks and other financial service institutions registered under the Banking and Financial Services Act, Chapter 387 of the Laws of Zambia.

ii. The Securities and Exchange Commission (SEC): Responsible for the supervision and development of the Zambian Capital Markets; Licensing, registration and authorization for financial intermediaries, issuers of debt and equity instruments and collective investment schemes. This role is prescribed under the Securities Act no. 41 of 2016.

iii. The Pensions and Insurance Authority (PIA): Regulates the conduct of the pension and insurance industry through prudential supervision in order to protect the interest of pension scheme members and insurance policyholders. This is done under the provisions of the Pension Scheme Regulation Act No. 28 of 1996.

iv. Other recent/ongoing reforms include:

    - Trade and Investment Bill: Provide market access in export markets for Zambian businesses and the much-needed financing for MSMEs.

- The new Small and Medium Enterprises Ministry: created in August 2021 to provide conducive environment for existing SMEs to grow and catalyze private sector led growth.
- Revised SME Policy to accelerate the development of MSMEs.

5.3.2 Frameworks for Pensions and Insurance

The Pensions and Insurance sector play a key role in Zambia's financial system. It provides a source of finance for the private sector and the Government through investment in government securities among others. The industry is regulated by the Pensions and Insurance Authority (PIA), a body for the pensions and insurance industries in Zambia. The PIA falls under the MoFNP and derives its mandate from the Pension Scheme Regulation Act No 28 of 1996. NAPSA (an independent body) is the biggest player in this space. Other key players include the National Health Insurance Management Authority (NHIMA), established under the National Health Insurance Act No. 2 of 2018, and Public Service Pension Fund Board.

In recent years, the COVID-19 pandemic had a negative effect on the performance of the sector. Notwithstanding this, the sector has been resilient and performed relatively well. Notably, the uptake of pension services increased from 3.8 percent in 2015 to 8.2 percent in 2020 (BoZ, 2020). In similar vein, the uptake of insurance services increased from 2.8 percent in 2015 to 6.3 percent in 2020.

However, several barriers on the use of pensions and insurance still persist. For instance, the most prominent barriers to the use of pension services include high unemployment levels and low incomes, limiting pension contributions. Major impediments to growth of insurance services include inadequate information. About 40.9 percent of the 2020 FinScope survey respondents indicated that they had never heard of insurance reflecting, limited awareness and knowledge of insurance services. Further, some respondents indicated that they could not afford insurance services.

Generally, the pensions and insurance sector has been plagued by the poor performance of the economy which has affected accessibility to these services. In addition, the lack of information continues to hinder growth of the sector. Therefore, policy actions to support increased awareness of these services are a necessity and should be accompanied by wholesale actions necessary to stabilise the economy and make it possible for the majority of the citizens to access pensions and insurance services.

The Role of Capital Markets in Promoting Private Finance and enhancing Institutional Investments

The capital market in Zambia remains largely underdeveloped to enable sufficient domestic resource mobilisation. The development of capital markets will allow the government to easily tap finances from local investors in the economy. Developing the Zambian capital markets will also be enormously beneficial to the government's ability to internally finance development.

Further, there is scope for the stock and bond markets to channel finance towards SDGs and national priorities. In that regard, given the growth in institutional investments from pensions and market capitalisation in the Zambian stock market, finances are clearly available within these two sectors to support economic transformation. However, these investments, particularly from the pension funds have been directed towards Government bonds and infrastructure development (property).

To help attain the country's priorities as espoused in the 8NDP, policy reforms are essential to shift the focus from investment in financial instruments to more social investments such as those involving education, health, climate change among others. Such investments are mutually beneficial to the Government and pension funds as they contribute to the development of human capital, a crucial ingredient in economic development and growth of institutions. However, the current legal framework is restrictive on the thresholds for these investments, inhibiting the contribution of pension funds to resource mobilization and economic development. Therefore, a clear policy direction for pension and insurance funds toward providing an alternative form of financing such as green bonds for the Government's social economic development agenda is worth pursuing.

5.3.3 Frameworks for Public Private Partnerships

Public Private Partnerships (PPPs) still remain one of the options for sustainable financing in Zambia. Currently, the Public Private Partnership Act No. 14 of 2009 (GRZ, 2009) regulates PPPs in Zambia. It defines a PPP as an investment through private sector participation in an infrastructure project or an infrastructure facility. The PPP Act created a framework that allows the private sector to invest and participate in various public sector sponsored projects and infrastructure. The PPP Act establishes three institutional bodies to handle the management of PPPs: 1) a PPP Unit, 2) a Council, and 3) a Technical Committee, each with specifically delineated responsibilities in the lifecycle of the PPP process. The PPP Unit, established under the Ministry of Finance and National Planning is responsible for coordinating PPP activities in the country. The Act also describes how projects are identified and how feasibility studies for projects are conducted.

PPP's can provide an alternative means of unlocking private finances for public infrastructure. PPP's also provide other benefits such as efficiency advantages from using private sector skills and mitigation of inherent risks; increased transparency and enlargement of focus from only creating an asset to deliver a service, including maintenance of the infrastructure asset during its operating lifetime. As such, Zambia's PPP Act is aimed at promoting and facilitating the implementation of privately financed infrastructure projects and effective delivery of social services by enhancing transparency, fairness, and sustainability.

Additionally, various stakeholders interviewed were in concord that PPPs are a crucial avenue for sustainable resource mobilization. The stakeholders pointed out that the push is now on actualizing the use of PPPs as a financing mechanism. It was also noted that the MoFNP has an understanding of how PPPs work and that they are usually applied as long-term concessional agreements.

The Government of Zambia intends to leverage on the PPP financing model, resulting in the provision of services to the public and creation of more fiscal space for social sector and growth spending. Some of the recognized PPP arrangements under the Act include Built and Transfer (BT), Build Lease and Transfer (BLT), Build Operate and Transfer (BOT), Build Own and Operate (BOO), Build Own Operate and Transfer (BOOT), Build Transfer and Operate (BTO), Contract Add and Operate (CAO), Develop Operate and Transfer (DOT), Rehabilitate Operate and Transfer (ROT), Rehabilitate Own and Operate (ROO), Management Contract and Supply Operate and Transfer (SOT) and others.

Some of the successful PPP projects in Zambia are documented in Table 5.3.1. It is also noteworthy that there are many other PPP projects currently in the pipeline as well as others that have fallen off along the way due to various reasons. At the time of writing, the values of these PPPs were not provided. Recently, the Government flagged off two notable PPPs related to road infrastructure namely the Lusaka – Ndola Dual carriage way and the Chingola- Kasumbalesa road projects. The rehabilitation of the Lusaka – Ndola Dual carriage way is valued at about USD$ 577 million and is expected to be completed within 36 months. Further, the Government also signed the Concession Agreement for the Design, Financing, Building, Operation, Maintenance and Transfer of 35km of the mining transportation channel of the Chingola-Kasumbalesa using the PPP financing model.

Table 5.3.1: Select PPP Projects in Zambia

Project	Contracting Authority
Kasumbalesa One Stop Border Post	ZRA
East Park Shopping Mall	UNZA
Luburma Market Development	Lusaka City Council
Town Centre Project	Lusaka City Council
Mwembeshi Correctional facilities	Ministry of Home Affairs

Source: Authors' construction using Ministry of Finance data

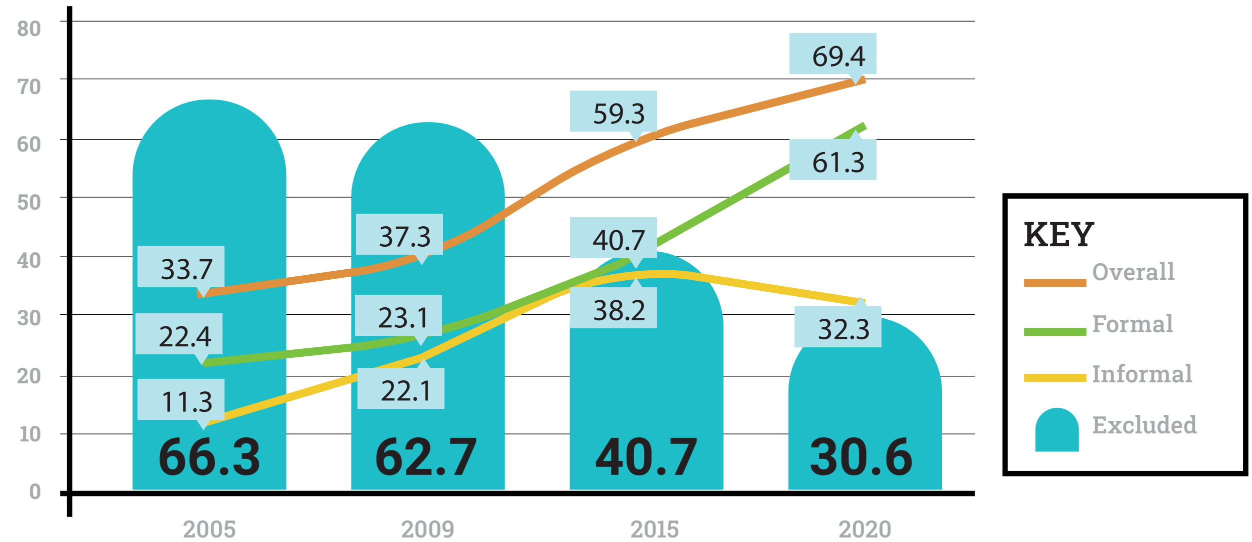
In April 2022, the Zambian Government launched the Public Private Dialogue Forum (PPDF) aimed at promoting economic growth and development through PPPs. The PPDF, while not entirely a new structure with the Public Private Dialogue spectrum in Zambia, provides an opportunity for much needed interaction between Government and the Private Sector to promote economic growth and development through PPPs.

5.3.4 Frameworks for Financial Inclusion

Attempts at ensuring the availability of financial services trace as far back as the 1990s, coinciding with a time when the country embarked on its first effort at actualising financial sector deepening and liberalization. The banking sector was small and underdeveloped such that only 8 percent of the population was captured in the banking system by 2005 (Lwanga 2021; Martínez, 2006). To address this challenge, the BoZ developed a Financial Sector Development Plan (FSDP). The FSDP was aimed at tackling the lack of financial services especially in rural and peri-urban areas; high bank charges and account requirements; poor credit culture, and low levels of financial literacy and education.

Other reforms aimed at promoting financial inclusion include the formulation of the National Financial Inclusion Strategy (NFIS) (2017-2022) and the Rural Finance Policy and Strategy (2012). Generally, Zambia has made impressive strides in reducing the share of unbanked individuals across the adult population. Between 2005 and 2020, financial exclusion significantly reduced by approximately 50 percent. Formal financial inclusion has also increased by three times its share in the reference period. Further, the level of informality in terms of accessing financial services initially trended upwards between 2005 and 2015. However, between 2015 and 2020, informal channels of financial inclusion have been on the steady decline (Figure 5.1). Implicitly, more individuals in Zambia are utilizing various channels of funds transfer, remittances, bill settlement and saving, among others that are less costly than what would obtain in the financial exclusion bracket.

Figure 5.1: Financial Access Trends



Source: Author's construction based on Finscope Surveys, 2005-2020

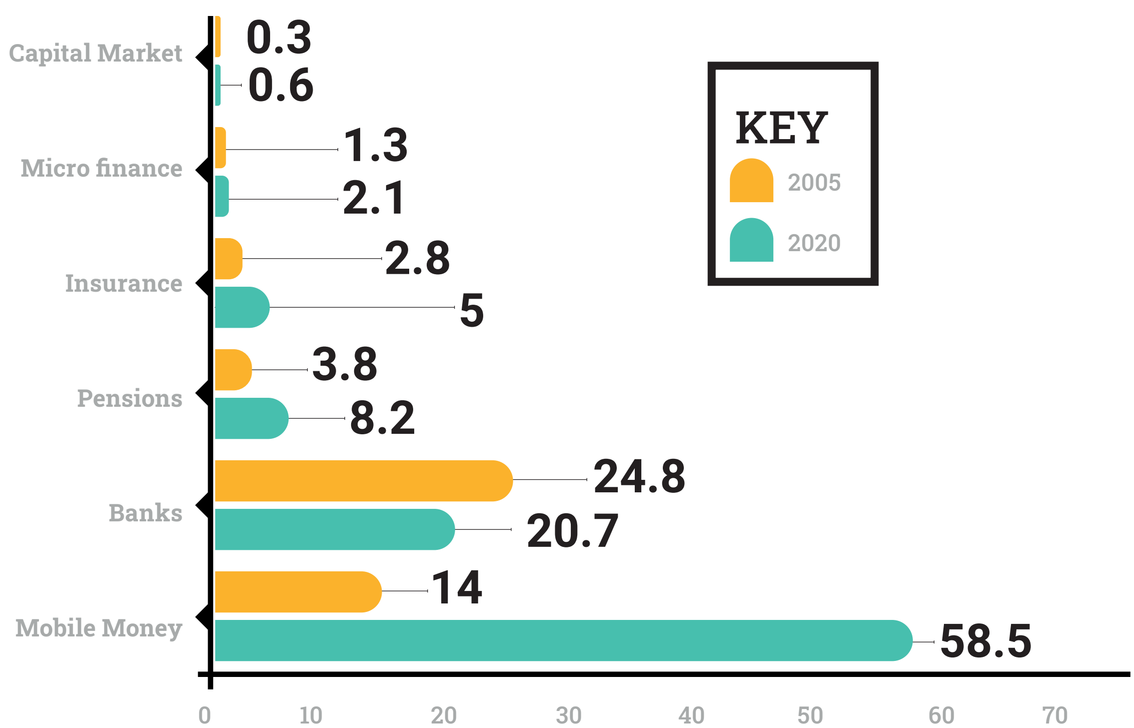
Enhanced access to financial services in most parts of Zambia has been through the emergence of new banks, microfinance branches and most recently, mobile money. The number of commercial banks in Zambia rose by 46.15 percent, from 13 in 2004 to 19 in 2020. Further, the nationwide distribution of automated teller machines (ATMs) rose to 1032 in 2020.

32. https://data.imf.org/?sk=E5DCAB7E-A5CA-4892-A6EA-598B5463A34C
33. https://www.fsdzambia.org/wp-content/uploads/2019/03/Zazu-Financial-Education-Pilot-Report-FINAL-9818.pdf

Most significantly, however, the popularity of mobile money has contributed the most to the upscale of financial inclusion in Zambia (Figure 5.2). Spreading financial services through mobile money to the financially underserved areas in the country has been considerably easy with growth in ICTs. Mobile money also only requires the use of mobile phones and so far, the country has over 90 percent of the population with mobile phone access (ZICTA, 2020). Moreover, based on profit maximising decisions, banks are unable or unwilling to invest money into building branches in remote areas. Implicitly, the most cost-efficient methods to get people in rural areas to participate in the formal financial system is through the use of mobile money.[32] Mobile money has equally been recognised as a tool that has allowed more women to be financially included and expanded socio-economic opportunities for many people in recent times.

Although financial inclusion outcomes in the nation seem promising, there are still evident gaps in areas such as gender biases and low rural and urban absorption rates, among others. For instance, the share of women using financial services increased from 57.4 percent to 61.2 percent in 2020. This is compared to 67.9 percent of men in 2015 and 71.2 percent in 2020 (FSD, 2020). Furthermore, while financial inclusion has increased in both rural and urban areas, the rural areas still lag behind urban areas. According to the 2020 Finscope study, usage of both formal and informal financial services is higher in urban areas than rural areas. Particularly, adults that used formal financial products and services in urban areas were about 49.7 percent compared to rural areas at 26.3 percent. Likewise, the proportion of the adult population that used both formal and informal financial products and services in urban areas was approximately 31.2 percent relative to 17.9 percent in rural areas. Similarly, the use of informal financial services was observed to be higher in the rural areas (12.7 percent) than in urban areas (2.9 percent).

Figure 5.2: Financial Sector players and contribution to financial Inclusion (percent)



Source: Author's construction based on Finscope (2020)

The gaps in the financial inclusion ecosystem are a key consideration given that digital and mobile money adoption have contributed to increased financial inclusion outcomes in Zambia. The use of digital platforms to broaden financial services to stakeholders such as MSMEs and women can induce economic activity and recovery post the pandemic era. Policy responses should ride on digital technologies and the extension of financial services and support to these marginalized groups. This will help tackle the pursuit for sustainable

34. Oz-Yalaman, G. (2019). "Financial inclusion and tax revenue", http://www.journals.elsevier.com/central-bank-review/

growth and development. Identifying and dealing with the barriers to adoption of digital financial services is a matter of urgency for sustained increase in financial inclusion.

Financial inclusion has the potential to contribute to revenue mobilization through growth in incomes of the financially included and higher investments from the beneficiary firms. For example, investment in government paper (bonds and treasury bills) made possible by the increased financial inclusion, can also target the majority of individuals and firms from microfinance and on mobile money platforms. This would allow the government to have access to funds that may sit idle in people's accounts.

Despite the merits of financial inclusion, sustaining current gains and ensuring deeper levels of financial inclusion is much dependent on how the country responds to deficiencies in the national financial inclusion strategy. Most importantly, financial inclusion targets people who are left out of the financial inclusion bracket. These individuals typically reside off the line of rail in rural locations, are uneducated, illiterate and are usually faced with digital exclusion. Nevertheless, communication of various channels of financial inclusion and related processes are not socially and culturally inclusive. For instance, the national financial inclusion strategy is in English and not translated in local languages for the rural and illiterate individuals to internalise and use. This leaves many behind and stands in the way of ensuring the gain of the country has so far made in financial inclusion are sustained or increased.

Most popular channels of financial inclusion such as village banking remain largely informal, limiting contributions of the general public to resource mobilization and economic development. While some channels are formal, others operate informally with huge amounts of money that could potentially be a source of government financing through bonds and treasury bills. Educational awareness on the information about the criteria for investing in government paper should however be well disseminated by BoZ. Financial literacy should not only emphasise the need for individuals to use affordable financial services, but also raise awareness of businesses and individuals to invest in the economy, and make resources available for national development. Financial literacy efforts should address communication barriers that currently only accommodate English, leaving out the local languages that target individuals often use in day-to-day transactions.

Sustaining the gains in financial inclusion is cardinal as the Government looks to bring on board the 'unbanked' populace. Increased financial inclusion can provide a pool of resources in the financial system thereby enabling private sector investment and freeing the Government from its public investment burden.

5.3.5 Addressing SME Finance Challenges

Access to affordable finance is one of the major challenges faced by SMEs in Zambia. These challenges became even more pronounced during the 2020/2021 COVID-19 pandemic. The COVID-19 crisis placed negative territorial impacts that were mostly evidenced among the MSMEs in Zambia as financial inclusion players. This was especially observed between March 2020 when the first case in the country was recorded and September 2021 when infections were more severe. Although Zambia never experienced a full lockdown, the effect of the COVID-19 Pandemic on incomes of MSME owners was profound. The pandemic inflicted devastating consequences characterised by disruption in supply chains, productivity and output of these entities. Zambian business owners often reported having to withdraw cash out of their business for personal use to cope with the pandemic, limiting liquidity of their firms. About 70 percent of MSMEs faced even deeper limitations with access to funding for recovery of productive units even when COVID-19 restrictions were eased off to pave way for full scale operations.[35] This amplifies the vulnerability of the MSME sector to financial and policy exclusion. The susceptibility of MSMEs was exacerbated by their physical-service based business models that were unmatched with abandoned customer and workspaces that since transitioned to virtual operations with the pandemic.[36]

35. Ibid
36. https://www.fsdzambia.org/how-micro-and-small-enterprises-mses-leveraged-informal-financing-and-digital-technology-during-the-COVID-19-pandemic-in-zambia/

While the BoZ delivered the Targeted Medium Term Refinancing Facility (K10 billion) to support the recovery of MSMEs, only an estimated 4,200 firms were supported through this facility. It is worth noting that Zambia's macroeconomic instabilities and Government arrears to MSMEs were also impediments to substantial financial support to MSMEs. Thus, most MSMES, especially women led MSMEs, resorted to microfinance institutions as the preferred source of financing despite the high interest rates.

To unlock finance for SMEs, the Government established the Zambia Credit Guarantee Scheme (ZCGS) in 2017. ZCGS provides a platform for financial institutions to lend to SMEs, promoting the flow of finance to the segment. The Government also launched the PPDF to expand affordable finance opportunities for the private sector. Further, following the change of Government in 2021, and the creation of a dedicated ministry for SMEs, Zambia has witnessed an increased interest in support towards SMEs, with some commercial banks developing financial packages for SMEs. In addition, the CPs such as the donors, World Bank, EU, and AfDB have also been providing financial and technical support to promote the SME segment.

5.3.6 Key Takeaways

- More can be done to leverage on Public Private Partnerships (PPPs) as a source of finance as its uptake has been irregular since the enactment of the PPP Act in 2009. To date, only 5 PPP projects have been successfully completed in Zambia.
- The major challenges faced include capacity challenges as well as lack of political will, weak legal framework among others. Further, the documented success stories relating to PPPs have mostly been in the services sector further highlighting the limited success of the model in supporting other socio-economic priorities of the country.
- Zambia has made strides with respect to financial inclusion. Banking the unbanked remains a key priority for gathering resources from which the private and public sectors can borrow.
- Zambia has inadequate frameworks to address financial challenges for the private sector and support the channelling of resources toward priority sectors. The economic challenges including unstable macroeconomic environment further compound the challenges for private sector growth and participation in the economic agenda
- Current frameworks are not adequate enough to limit purchase of public debt by commercial banks
- Though institutional on pensions have investments have potential to contribute to development finance and economic development, the limited public awareness on the associated investment opportunities remains a major impediment to their effectiveness.
- Although financial inclusion has increased in both rural and urban areas, the rural areas still lag behind urban areas. Additionally, gender gaps persist with most women still financially excluded.

5.3.7 Recommendations

- Government must safeguard the macro-fiscal gains to create an enabling environment for private sector led growth and economic participation.
- There is need to promote increased sensitization and public awareness of the roles and available investment opportunities at insurance and pension to stimulate institutional investments and public participation.
- Government must further strengthen the PDM Act to limit the purchase of commercial bank debt.
- Government should continue to promote public-private dialogue by expanding the reach of the PPDF and expanding its reach.
- To improve financial inclusion, Government must ramp up financial literacy efforts through the use of local languages and braille in financial transactions and packages.
- There is need to review and further strengthen the regulatory framework for PPPs to maximise their economic benefits

- Government should continue to promote the use of FinTechs to increase financial inclusion.
- Providers and regulators need to collectively address limited ICT infrastructure (especially in remote areas of the country), lack of guarantees on safety of identifying user information, data security and, most recently, fraud and physical abuse of women using digital platforms.

5.4 Frameworks for International Private Finance

5.4.1 Frameworks for Investment

The Ministry of Commerce, Trade and Industry (MCTI) is the lead institution mandated to promote investment (foreign and domestic) in the Country through the creation of an enabling investment climate. MCTI executes this mandate through the ZDA (ZDA Act 2006), its statutory body, and in collaboration with other relevant line ministries and government agencies. Other key players in the investment promotion space include Zambia Tourism Agency (ZTA), Public Private Partnership Unit (PPPU), and Industrial Development Corporation (IDC).

Given the multiple actors in the investment space, coordination challenges persist, usually manifesting in policy inconsistencies and bureaucracy. For instance, FDI to the mining sector has been adversely impacted by policy inconsistencies fiscal regimes, and policy fragmentation among relevant institutions.

Policies and legislation guiding investment promotion include Vision 2030, NDPs, the National Investment Promotion Strategy 2018-2022, the ZDA Act, the Investment, Trade and Business Development Act No.18 of 2022, and the PPP Act.

The Vision 2030 and 8NDP articulate the investment promotion strategies for Zambia, providing strategic direction for inflows to Zambia. Regarding policies, the National Investment Promotion Strategy 2018-2022 and the National Industrial Policy (2018) are the main documents guiding investment flows in Zambia, including addressing gaps in the existing regulatory frameworks.

The main weaknesses in the investment policy frameworks include poorly designed investment incentives, weak M&E systems, weak governance systems, low human capital, and inadequate infrastructure. Additionally, most policies and frameworks are in need of review.

Overall, macroeconomic instabilities, unstable fiscal regimes, global shocks, climate change, and a weak governance environment are the main impediments and threats to the effective promotion of investment, especially FDI. Significant declines in FDI that Zambia has experienced recently have been attributed to instabilities in the mining fiscal regime and resulting operational challenges.

The ongoing IMF-backed home-grown economic recovery program aimed at stabilizing the macroeconomic environment and restoring fiscal and debt sustainability is expected to lead to increased FDI inflows to Zambia. Key areas of reform focus include improving PFM, curbing corruption, containing accumulation of debt and strengthening governance systems. These reforms have a bearing on FDI inflows and investment in general.

5.4.2 Policies and Reforms to Increase Remittances

As highlighted in Chapter 3, growth in remittances are necessary to spur economic growth and development. On a macro-level, remittances are a great source of capital inflows and foreign exchange earnings and thus have a multiplier effect on the economy (UNCTAD, 2013). In addition, remittance funds partly support MSMEs, largely contributing to resolving issues of access to affordable finance these small businesses face. At the household level, remittances support basic consumption, including healthcare and education expenditures (Ratha, 2015).

Globalization and advancements in communication technologies have greatly expanded the avenues for the Diaspora to remain actively involved in their respective countries' cultural, economic, social, and political life. Unfortunately, Zambia has been lagging behind other countries in the region in mobilizing resources from the Diaspora. Factors contributing to the under exploitation of diaspora resources include inadequate frameworks (regulatory, policy), harsh macroeconomic conditions and poor ICT infrastructure.

However, Zambia has made great strides in strengthening the policy frameworks for remittances, as evidenced by the development of the Diaspora Policy in 2019. The Policy is based on the realization that the Diaspora has enormous potential to contribute positively to the Country's economic development. The Policy, therefore, aims to provide a framework for effective mobilization and engagement of Zambia's Diaspora to identify and implement mechanisms for harnessing the developmental potential of the Diaspora. Wide dissemination of the Diaspora policy and integration of various diaspora groupings are crucial for the effectiveness of the Policy in increasing remittances and maximizing its contribution to economic growth.

To enhance monitoring and tracking of remittances and other capital flows, BoZ developed a Balance of Payments Monitoring Guide in 2019. The guide included an electronic monthly return called Money Remittance and Receipt Return (MRRR), a monitoring tool that all registered Financial Service Providers (FSPs) in Zambia are required to complete and submit to the Bank. It is mandatory for FSPs (involved in cross-border financial transaction) to complete and correctly fill in all the fields. All FSPs are required to report all cross-border foreign exchange transactions to residents and from non-residents using this in return. This innovation is expected to enhance the monitoring and tracking of diaspora economic contributions resulting in remittance growth and diaspora investments. Additionally, in 2020, BoZ in an effort to encourage increased use of digital financial services in the Country revised the transaction balance and transaction limits for individuals, agents, small businesses and corporates.

Further, the Mobile Network Operators such as Zamtel Mobile Money, MTN MOMO and Airtel Mobile Money and other Payment Service Providers entered into partnerships with big international remittances players such as World Remit and Ria Money Transfer, thereby introducing new products and facilitating the inflow of remittances across boarders at a relatively lower cost. This also contributed to increased adoption of formal transaction channels, contributing to additional revenue collection through charges and fees.

At the continental level, there are discussions to establish the African Diaspora Finance Cooperation (ADFC). In February 2022, the 40th Session of the African Union Executive Council formally adopted the framework developed by Professor Gibril Faal, for the creation of an African Diaspora Finance Corporation (ADFC) focussed on RemitAid™, Diaspora Bonds, Diaspora Mutual Funds, Perpetual Endowment Legacy Fund, and a Trust Fund that finances diverse development activities in Africa and within the diaspora. ADFC will be set up as an independent, non-AU continental finance institution, operating as a social enterprise and working together with other African and global finance, development, and diaspora institutions.

To the authors' knowledge, Zambia has made limited progress in attracting diaspora investments, partly due to weak institutional and regulatory arrangements and limited financial innovations such as diaspora bonds.

5.4.3 Key Takeaways

- Zambia has made strides in addressing gaps in the policy and regulatory frameworks for investment and FDI. However, gaps remain mostly reflected in fragmentation, and policy inconsistencies .
- Given the multiple actors in the investment space, coordination challenges persist. For instance, FDI inflows to the mining sector has been adversely impacted by policy inconsistencies especially unstable fiscal regimes, and policy fragmentation among relevant institutions.
- Limited FDI to non-mining priority sectors (tourism, manufacturing and agriculture) is indicative of weak investment policies and frameworks.
- Zambia has instituted key reforms and innovations aimed at harnessing diaspora finance and investments. The main reforms include developing a Diaspora Policy, establishing a monitoring and tracking system, and leveraging ICTs.
- Limited information on investment opportunities for the diaspora, and lack of diaspora targeted investment options could explain the slow growth of remittances and diaspora investments in Zambia.
- Underdeveloped capital markets manifest in limited diaspora targeted investment products impede growth in diaspora investments .

5.4.4 Recommendations

- Government must develop an integrated approach to FDI promotion by strengthening coordination and information among key players such as MoFNP, ZDA, BoZ, relevant line ministries, and the private sector .
- There is need to strengthen capacity of key institutions such as ZDA, and BoZ in promoting and tracking FDI.
- More efforts must be directed at diversifying FDI by attracting investments to other priority sectors such as tourism, mining, manufacturing and agriculture.
- To increase and stabilize FDI, Government must stay the course and restore macroeconomic stability and attain fiscal sustainability.
- Given the contribution of mining sector policy inconsistencies to fluctuations in FDI, Government must prioritize the stabilization of the mining fiscal regime and policies.
- There is need to strengthen the policy and regulatory frameworks for the diaspora activities. One way is to establish a desk or department for the diaspora affairs at ZDA. Additionally, there is need to strengthen coordination, between embassies and the relevant line ministries (foreign affairs, MCTI).
- There is need to improve information flow between the Government and diasporans especially on available investment opportunities.
- There is need to incentivise financial institutions and capital market players to develop diaspora-tailored financial products and instruments to attract diaspora finance. These can take the form of diaspora bank accounts, and diaspora bonds.

5.5 Climate Finance

The 8NDP recognizes environmental sustainability as being key to enhancing mitigation and adaptation to climate change. This is critical to facilitate innovative sources of climate change, carbon markets, and green bonds to increase resource mobilization prospects.

5.5.1 Historical Analysis of Climate Financing

Over the last decade, the impact of climate change has been recognised as an impediment to development and in need of resources to apply adaptation and mitigation measures. The impacts of this impediment have been projected to slow development and costed Zambia approximately US$$ 13.8 billion loss in GDP.[37]

Zambia first acknowledged climate change in its National Budget in 2014, with the Government looking to complement efforts at the global level to mitigate climate change through the establishment of large-scale forestry nurseries across the country. In 2015, it was then recognised as a threat to development, making the country's developmental challenges even more formidable. Thus, the Government pledged to upscale support to conservation farming involving a total of 84,000 farmers in 31 districts during the 2014/15 season.

In 2016, climate change was then recognised as a reality affecting the day-to-day lives of citizens. It was said to have affected the timing, distribution and amounts of rainfall in the previous season which adversely affected the agricultural sector and weakened the country's capacity to generate sufficient electric power.

Government ramped up its response efforts to mitigate climate change. In 2017, the Government sought to mitigate the effects of climate change by continuing with the construction of multipurpose dams and promotion of irrigation schemes. It also committed to setting up 20 irrigation schemes and scaling-up of the sustainable utilisation of wetlands. Additionally, irrigation projects would be undertaken using the PPP model, particularly in farming blocks. The government also sought to engage with the private sector in delivering new generation facilities to increase on-grid and off-grid access to electricity, given the risks

37. Zambia's Nationally Determined Contribution of 2021.

associated with climate change. The projects included the Scaling-Up of Solar Project and the development of the Kafue Gorge, Batoka Gorge and Kalungwishi projects. Government's commitment to mitigate efforts is reflected in a specific sub-allocation to climate resilience of K347.99 million.

In 2018, climate change was seen as having the potential to reverse the country's economic gains. Thus, the Government sought to implement strategies to mitigate and adapt to the adverse effects of climate change. These measures included a Pilot Project for Climate Change Resilience that was being implemented in Western, Southern and Central provinces, with a plan to extend it to Northern, Muchinga and Luapula Provinces. The Government also sought to address deforestation by undertaking a US$32.8 million Integrated Forestry Landscape project in Eastern province with the support of cooperating partners. It further looked to strengthen the national disaster response system. In continuing with the trend of the previous year, the Government increased its sub-allocation from K347.99 million in 2017 to K457.5 million, translating into an increase of 31.5 percent.

With climate change firmly recognised as a budgetary issue, in 2019 Government rolled out the climate change adaptation projects. This included the Pilot Program on Climate Resilience in Western, Southern, Central and Lusaka Provinces, and the development of the 237 kilometre climate resilient road from Kalomo to Dundumwezi up to Itezhi-Tezhi. More adaptation projects were scheduled to be rolled out to Northern, Muchinga and Luapula Provinces under the Transforming Landscapes for Resilience and Development Program. Their preparation was estimated to cost USD$150 million, which would be secured from CPs. The Government had also submitted a USD$100 million project to the Green Climate Fund aimed at creating a creditworthy intermediary off-take for renewable energy as part of its climate change mitigation efforts. The Government further acknowledged that in 2018 it had mobilised a total of USD$84.5 million from the Green Climate Fund to finance projects in agriculture and energy sectors. The projects were estimated to cost USD$278 million. However, allocations to climate resilience declined by 53.4 percent, to K213.0 million from K457.5 million in 2018.

In 2020, the Government stated that it would support the adoption of climate smart agricultural technologies through increased allocations and fiscal incentives. Consequently, Government proposed to allocate K97.9 million for extension services for crop, livestock, and fish production. The Government zero rated the supply of gas stoves, other gas cookers and gas boilers. Additionally, the Government moved to suspend import duty, for three years, on the importation of machinery for processing of solid waste to generate electricity and produce organic fertilizers as a way of encouraging sustainable industrialisation while mitigating the effects of climate change. Further, the Government also increased the carbon tax on all motor vehicles entering Zambia by 20 percent. However, during this time Government did not allocate any funds to climate resilience.

Despite suspending allocations to climate resilience in its 2020 and 2021 budgets, the Government stated that it would accelerate the implementation of climate change programs, with one such being the US$100 Million Transforming Landscapes for Resilience and Development (TRALARD) Program. Government also initiated reforms to strengthen legislation on climate change to provide a legal framework for the implementation of the 2016 National Climate Change Policy. However, Government did not declare any sub-allocation of its funds to climate change.

5.5.2 International Efforts: Initiatives of Multilateral Climate Finance for Zambia

Despite grappling with existing and emerging climate change impacts, there are major opportunities through multilateral institutions, bilateral partners and other international organisations for Zambia to tap in and resolve some of the constraints related to climate finance. The initiatives are highlighted below.

The Green Climate Fund

The Green Climate Fund (GCF) was developed to support the Paris Agreement. As the world's largest climate fund, it has the mandate of supporting developing countries in their goals of raising and realizing their ambitions in creating low-emissions, climate-resilient pathways as outlined in their Nationally Determined Contributions (NDC). It does this through National Designated Authorities (NDAs) who serve the role of an interface between each country and the GCF.

38. See Zambia's Nationally Determined Contribution of 2021

Zambia's NDA was established to provide an efficient and fairly independent office, and to balance mainstreaming functions of the NDA into the Government, while providing for its necessary identity and visibility. This is intended to ensure that activities supported by the GCF align with the strategic national objectives and priorities and assist Zambia advance towards ambitious climate action goals on adaptation and mitigation as espoused in its NDC. This has been estimated at USD$15 billion with limited international support, and an added USD$35 billion with substantial international support.[38]

AfDB has been playing a critical role in unlocking green financing. In 2019, the Bank in conjunction with the GCF worked together to support a US$ 154.0 million renewable energy financing framework in the country. The framework sought to address Zambia's dependence on hydropower generation (about 90 percent) of its energy needs and shift towards alternative energy sources by financing 100 MW renewable energy projects, primarily small-scale solar projects. Of the total financing requirement for the framework, GCF provided US$ 50 million in debt financing and a grant of US$ 2.5 million to support the technical assistance component of the project. The proposal included co-financing of US$ 51.5 million from AfDB, as well as US$ 50 million from banks and private sector investors.

In July 2021, the DBZ was awarded accreditation to receive and submit proposals on behalf of developers of green projects to be funded by the GCF. Under this arrangement, DBZ will be able to fund green projects up to a tune of USD$250 million. The legal and other requirements of the accreditation are yet to be finalised.

In October 2022, the Zambia National Commercial Bank (ZANACO) was also awarded accreditation to access capital for onward lending to green projects, including smart agriculture, agro-forestry and renewable energy.

Zambia received USD$91.2 million of the GCF funding to support various green projects aimed at enhancing mitigation and adaptation measures. For example, the Zambian Government received assistance to catalyse private investment in the renewable energy sector in order help the country shift from dependence on hydropower generation. This initiative supported the Renewable Energy Feed-in Tariff (REFiT) policy to facilitate the development of 100MW of renewable energy projects, mainly through solar power.

Zambia has also had access to internationally sourced finance for green projects, particularly for Agriculture, Forestry and Other Land Use (AFOLU). The Government, in partnership with the GCF and other stakeholders is implementing the US$137.3 million Strengthening Climate Resilience of Agricultural Livelihoods in Agro-ecological Regions I and II (SCRALA). The project aims to promote climate resilient agricultural practices, thereby improving food security and income at household level.

Other Supported Projects

Another project is the World Bank funded Transforming Landscapes for Resilience and Development in Zambia (TRALARD) at the cost of USD$100 million. The project, which is being implemented in Northern, Luapula and Muchinga Provinces, is a highly relevant initiative that has potential to support people, reduce the vulnerabilities to climate change derived from unsustainable livelihoods and a deteriorating natural resource base.

The TRALARD project has shown that a synergetic, integrated approach may deliver more tangible results on the ground especially if it pays particular attention to community and stakeholder concerns, and identifying ways of bolstering and augmenting the intervention for impact. The focus of the project is to ensure sustainability of poor rural community livelihoods in an environment already highly stressed by climate change and expected to undergo further important changes in the next decades. By improving agricultural and forestry practices, the project will simultaneously yield climate mitigation benefits and complement the USD$32.8 million Zambia Integrated Forest Landscape Project (ZIFLP), another World Bank funded project, which is helping to create an enabling environment for emissions reductions in the Eastern Province. These projects align with key national strategies and the country's Intended Nationally Determined Contribution (INDC).

39. Capital Markets Master Plan as launched on 23rd February 2023: http://www.seczambia.org.zm/wp-content/uploads/2023/02/Capital-Markets-Master-Plan-Approved-Document.pdf
40. See Securities (bond) guidelines available at http://www.seczambia.org.zm/wp-content/uploads/2020/01/The-Securities-Green-Bonds-Guidelines-2019.pdf

Climate Financing Innovations

Green Bonds

Green bonds are debt instruments used to finance projects, assets or businesses with specific environmental benefits. They are usually targeted at reducing greenhouse gas emissions and mitigating the effects of climate change through initiatives like renewable energy, sustainable agriculture and forestry. Green bonds have a high potential to attract private investors provided associated barriers are overcomed. Some of the barriers include lack of knowledge about existing international practices, and inadequate information from potential beneficiaries.

Zambia has a green bond initiative within the Capital Markets Development Master Plan[39] and spearheaded by the Ministry of Finance, the Security Exchanges Commission (SEC), and Biodiversity Finance Initiative (BioFin). As the nation transitions into a green economy, the green bond is intended to help address for instance, biodiversity loss and investment in green projects that will bring long-term benefits both to investors and the environment. The SEC and its partners have been working to shape the development of a green bond market for the country. The drafting and approval of the rules and guidelines for securities (green) bonds issued in a government gazette in 2020 and the development of the CMDP in 2023 are the notable developments from this process.[40]

Zambia has not had any issuance yet, either sovereign or corporate green bond. On the sovereign front, the debt situation and the macroeconomic environment have not permitted Government to issue a green bond. But in an ideal scenario, the sovereign bond takes precedence over the corporate or private bond to catalyse the market and then allow the private sector to follow. However, Zambia's situation is unique given the debt sustainability concerns. Until debt sustainability and macroeconomic stability are attained, sovereign bonds cannot be issued.

The SEC and its partners are redirecting their efforts towards private sector engagement to accelerate the issuance of a green bond. On the other hand, the SEC is also actively engaging the Government through the Ministry of Finance and National Planning (MoFNP) to establish fiscal incentives to entice various market players. In the 2023 National Budget address to parliament, the Minister of Finance and National Planning announced an 'exempt from withholding tax interest income earned on green bonds listed on the securities exchange in Zambia with maturity of at least 3 years' in order to promote investments with environmental benefits. This measure, if applied appropriately, could help crystalize the green bond market in Zambia particularly aimed at promoting private sector participation while the Government works on improving the general macroeconomic environment and resolving the debt issue with support from the International Monetary Fund (IMF).[41]

Green Fund

The country has made strides with respect to other climate financing initiatives. Notable is the "Green Outcomes Fund" established by ZANACO, Kukula Capital, and the World-Wide Fund for Nature (WWF) Zambia valued at K 1 billion (about US$59 million). The Fund forms a pool from which small and medium-sized enterprises can source funding for green business initiatives that create environmental outcomes such as climate, water, waste and green jobs. The fund was started in 2020 with support from the World Bank Climate Technology Program, with WWF-SA, University of Cape Town's Bertha Centre and Green Cape as the main design partners.[42]

Additionally, WWF Zambia manages the "Dutch Fund for Climate and Development". This fund renders support to businesses that have been impacted by climate change by providing assistance towards the adoption of more sustainable production methods.

Notwithstanding the already existing climate finance initiatives, sensitisation and awareness of the climate

41. On 31st August, 2022, The IMF approved a $1.3 billion Extended Credit Facility (ECF) for the Zambian government to help restore macroeconomic stability and resolve the debt impasse. See more here https://www.imf.org/en/News/Articles/2022/08/31/pr22297-imf-executive-board-approves-new-extended-credit-facility-arrangement-for-zambia
42. See https://africa.panda.org/?31543/Green-Outcomes-Fund-call-to-small-green-businesses-and-fund-managers
43. See https://theconversation.com/how-debt-for-climate-swaps-can-help-solve-low-income-countries-crushing-debt-and-environmental-challenges-at-the-same-time-191161
44. See https://www.imf.org/en/Blogs/Articles/2022/12/14/swapping-debt-for-climate-or-nature-pledges-can-help-fund-resilience

change impacts on climate-sensitive sectors is cardinal. Stakeholders observed that low knowledge and awareness on climate change including capacity constraints can be a challenge to ensure development and uptake of climate financing initiatives in the country.

Debt-for-Climate (Debt-for-Nature) Swaps

Debt-for-Climate or Debt-for-Nature Swaps are an instrument designed to free up public resources by exchanging debt obligations with commitments to finance domestic climate or nature projects[43]. To be effective they would require a significant amount of the debt to be relieved in favour of investments to new or additional climate adaptation or mitigation efforts. However, the swaps should not be treated as a universal solution to solving debt burdens, but as a complementary instrument that can help strengthen resilience to climate change and biodiversity loss where funding is limited.[44]

Zambia's National Climate Change Fund

Zambia places significant importance and priority on mitigation and adaptation to the effects of climate change in order to reduce GHG emissions and enhance the resilience of its population, ecosystems, infrastructure, productive and health systems. This entails promoting sustainable natural resources management across all sectors. To enhance local resource mobilization, the government is in the process of establishing a National Climate Change Fund. This will be one of the innovative ways of raising funds to use for different climate change programs.

A National Climate Change Fund can take many forms and include many types of instruments. However, the aim is to promote investment in climate change adaptation and mitigation programs and projects. It could also include funding for innovation through research and development. The fund could be used to administer either grants or loans, with interest acquired from loans used to grow the fund. It could also be used to receive climate funding from bilateral, multilateral, donor, philanthropic and other credible sources, or returns from carbon transactions.

5.5.3 Looking Ahead

Despite all efforts, domestic climate financing from government has remained low over the years. For instance, the budgetary allocations to climate change marginally increased to K972 million (0.6 percent of the budget) in the 2022 fiscal year from K956 million (or 0.8 percent of the 2021 National Budget).

This inadequate funding for climate change programs contributes to the implementation challenges the country faces in championing for a sustainable environment. It should be noted that increased funding from locally generated funds will help strengthening the capacities of local enterprises and other stakeholders thereby contribute to building a resilient and sustainable economy.

To complement government efforts towards climate action, the private sector has an enormous role in providing localised solutions including financing to tackle climate change. Stakeholders noted that most traditional commercial banks are less willing to lend to sectors such as agriculture. The financial sector should be encouraged to reach a number of sectors and borrowers with innovative business models that have the potential to address climate-related development challenges.

5.5.4 Frameworks for Climate Finance

Zambia is making every effort possible in taking action on climate change. Environmental sustainability has been identified as one of the pillars in the 8NDP as the government strives to mitigate against the negative effects of climate change. Accordingly, the country has developed dedicated national policies such as the National Policy on Climate Change (NPCC), the Nationally Determined Contribution (NDC), and has embarked on preparing the National Adaptation Plan (NAP). While the National Adaptation Plan of Action (NAPA) of 2007 focused on urgent and immediate adaptation needs, NAP will focus on medium to long-term adaptation. Further, it will help to integrate adaptation in the development planning process. Similarly, the Government intends to review the NPCC as it has been in effect for more than 5 years. It is anticipated that this review will incorporate aspects of what green economy means for Zambia and further strengthen institutional frameworks.

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45. See Zambia's full NDC available at https://www.greengrowthknowledge.org/sites/default/files/downloads/policy-database//Zambia_Provisional_Updated_NDC_2020.pdf

On the international level, Zambia has assented to several commitments including the Paris Agreement on Climate Change, the United Nations Framework Convention on Climate Change (UNFCCC) and the Sendai Framework for Disaster Risk Reduction. However, climate change financing is still a huge impediment in Zambia, hence, the need for further collaborations with international organizations. According to Zambia's INDC, for the country to successfully achieve a reduction of 38,000 Gg CO2 eq by 2030, the international community will have to play a huge role in form of finances, technology and capacity building. For instance, to implement adaptation and mitigation programs in Zambia, 70 percent of the estimated USD$50 billion will have to be externally sourced if the objectives of the INDC are to be achieved by the year 2030.[45]

5.5.5 Key Takeaways

The main takeaways are:

- Climate finance has the potential to contribute to Zambia's finance envelope. However, its potential remains largely unexploited. The situation is likely to change given the strengthened frameworks, including the creation of the Ministry of Green Economy and Environment in 2021.
- Government's budgetary allocations to climate change have been low and inconsistent. For instance, Government halted allocations to climate resilience in 2020.
- To date Zambia has not issued any green bonds despite their potential to contribute to resource mobilization.
- Zambia has been accessing internationally sourced finance for green projects, particularly for energy and agriculture.
- Private sector participation in climate finance is limited, contributing to the exclusion of sectors.
- Zambia has not optimised the available green financing initiatives and innovations.
- Zambia is yet to establish National Climate Change Fund, a game changer in mobilizing green resources.
- With better realignment of climate finance and financing processes, prospects for climate finance could improve.

5.5.6 Recommendations

- Government must increase budgetary allocations to climate change to enhance mitigatory measures
- There is need to create an enabling environment for green finance by reviewing frameworks and devising incentives to promote green financial products
- Government must promote and incentivise development of financial instruments such as climate-for-debt swaps
- The Government must also provide incentives to encourage private sector investments in green Projects such as renewable energy, low carbon waste management systems, smart agriculture and low carbon industry processes.
- Establishment of dedicated reporting mechanisms such as climate risk disclosure and reporting will also strengthen frameworks for climate change mitigation and adaption, and promote fiscal sustainability
- Government must expedite the establishment of the National Climate Change Fund to promote resiliency to climate change and green recovery
- CPs must work with Government to improve the alignment between development plans, financing processes, and climate finance so as to boost prospects for climate finance

5.6 Financing Arrangements for Local Government

5.6.1 Overview of Key Developments

Zambia's quest to attain inclusive growth crucially depends on its demonstrated commitment to the decentralization process, reflected in adequate legislative and institutional frameworks, and robust financing arrangements for subnational government. However, despite having a long history with decentralization, dating back to 1964, Zambia has not made significant progress in devolving functions and resources to subnational governments. It worth noting that the recent push to promote grass root-driven growth through increased intergovernmental fiscal transfers, following the change of government in 2021 has put decentralization at the forefront of the Country's inclusive and sustainable development agenda.

Zambia's commitment to the attainment of inclusive economic growth is evidenced by the inclusion of decentralization in the Country's national plans, i.e., 7NDP and 8NDP. However, the fact that the country did not have the Policy till 2013 to guide the decentralization process processes partly explains why not so much progress has been made in decentralizing authority and resources to subnational levels. The 2013 National Decentralization Policy, currently under revision indicates Government's resolve to actualize the decentralization agenda.

Other key developments in the decentralization space are contained in the Cabinet Circular No.10 of 2014, which sets out various milestones; the approval of a revised Decentralization Implementation Plan (DIP) covering 2015 to 2017, endorsement of new structures for local government, harmonization, and improvement of the conditions of service through the re-creation of Local Government Service Commissions (LGSCs).

While these efforts are promising, they cannot go far without robust financing arrangements for subnational governments. Adequate financing at all levels, including the Local Authority's ability to accountably raise and disburse funds for developmental purposes are crucial catalysts for the decentralization agenda. In its quest to accelerate decentralization and promote equitable development, the Government of Zambia has put in place an intergovernmental fiscal system that is discussed below.

5.6.2 Zambia's Intergovernmental Fiscal Decentralisation

Intergovernmental fiscal decentralisation focuses on the financial component of the larger decentralisation program. In order to successfully implement fiscal decentralisation, the Zambian government had set up an intergovernmental fiscal system. This included creating the Intergovernmental Fiscal Relations Unit in 2018 in the Budget Office of the MoFNP, whose primary role is to facilitate fiscal decentralisation.

5.6.3 The Pillars of Fiscal Decentralisation

Zambia's public expenditure arrangements and revenue assignments are highly centralised, weakening the local authorities' accountability for delivering local public services. The fiscal architecture of a decentralised system in Zambia stands on four pillars (Government of the Republic of Zambia, 2017).

Pillar 1: Expenditure assignment and autonomy

The first pillar, expenditure assignment and autonomy, is the cornerstone because it defines the service delivery responsibilities of local governments and their autonomy in making decisions about the level and mix of expenditures. However, the Government has recorded limited progress in devolving expenditure functions. According to a study conducted by ZIPAR in 2018 it was revealed that only agriculture extension services, primary health care and in some districts, social welfare and community development seemed to be in high gear of being devolved. According to the revised National Decentralisation Policy of 2013, the devolved functions would be followed by the transfer of their respective sector resources from the Public Service Commission to the Local Government Service Commission.

Pillar 2: Revenue assignment and autonomy

Actualization of fiscal autonomy entails granting subnational control over their own sources of revenue. By making LAs more accountable to the locals, fiscal autonomy promotes good governance among LAs. However, care must be taken to decide the appropriate assignment of revenue functions to ensure optimal revenues and fiscal stability.

Government must provide an enabling environment to empower LAs to mobilise own-source revenues. Some of the necessary reforms include the amendment of the Rating Act in order to carry out the property rate reform and update rating valuation rolls, and rationalising of fees, charges and levies, among others.

Pillar 3: Intergovernmental transfers: Vertical and horizontal imbalances

Matching tax and revenue assignments is a daunting task for central governments in their quest to implement decentralization. This is due to administrative considerations, economies of scale in tax administration, access to and sharing of information, tax competition and other factors that must be factored in the decision-making process. These difficulties give rise to vertical (fiscal disparities between different levels of government) and horizontal imbalances (variances between same levels of government), necessitating the need for a robust intergovernmental fiscal transfer system.

Zambia's fiscal transfer system includes the following:

a) Local Government Equalisation Fund (LGEF-General Purpose Grant);

b) Grants in lieu of rates (General Purpose Grant);

c) Local Authorities Development Fund (Mineral Royalties Sharing); and

d) Constituency Development Fund (CDF).

Of the above transfer mechanisms, the CDF has received more policy attention (See Box 1). Despite this increase, the CDF is seen by many to have many bottlenecks and this has led to low abortion and low execution rates. By Government's own admission, the Minister of Finance during his 2023 National Budget Address, stated that one of the major bottlenecks in the implementation of the CDF process, was that the process was not fully decentralised.

Box 5.1: The Constituency Development Fund: A game changer for local development and subnational financing

The CDF Act of 2018 is the main piece of legislation guiding the administration of CDF. The CDF is a tool for attaining inclusive growth through involvement of communities in decision making. The Government elevated the potential role of the CDF in the decentralization process by increasing it to K25.7 million in the 2022 National Budget from K1.6 million per constituency in previous fiscal years. This translates into an unprecedented increase of about 1,506%. Prior to 2022, the CDF had stagnated at K1.6 million for some time and was much smaller than the LGEF. Between 2015 and 2019, the LGEF averaged K896.8 million, while the CDF stood at K245.2 million.

According to the 2022 CDF guidelines, the following are the components of the CDF with their respective weights. The enhanced 2022 CDF includes the following components:

- Community Projects (60 percent);
- Youth, Women and Community Empowerment (20 percent); and
- Secondary Boarding School and Skills Development Bursaries (20 percent).

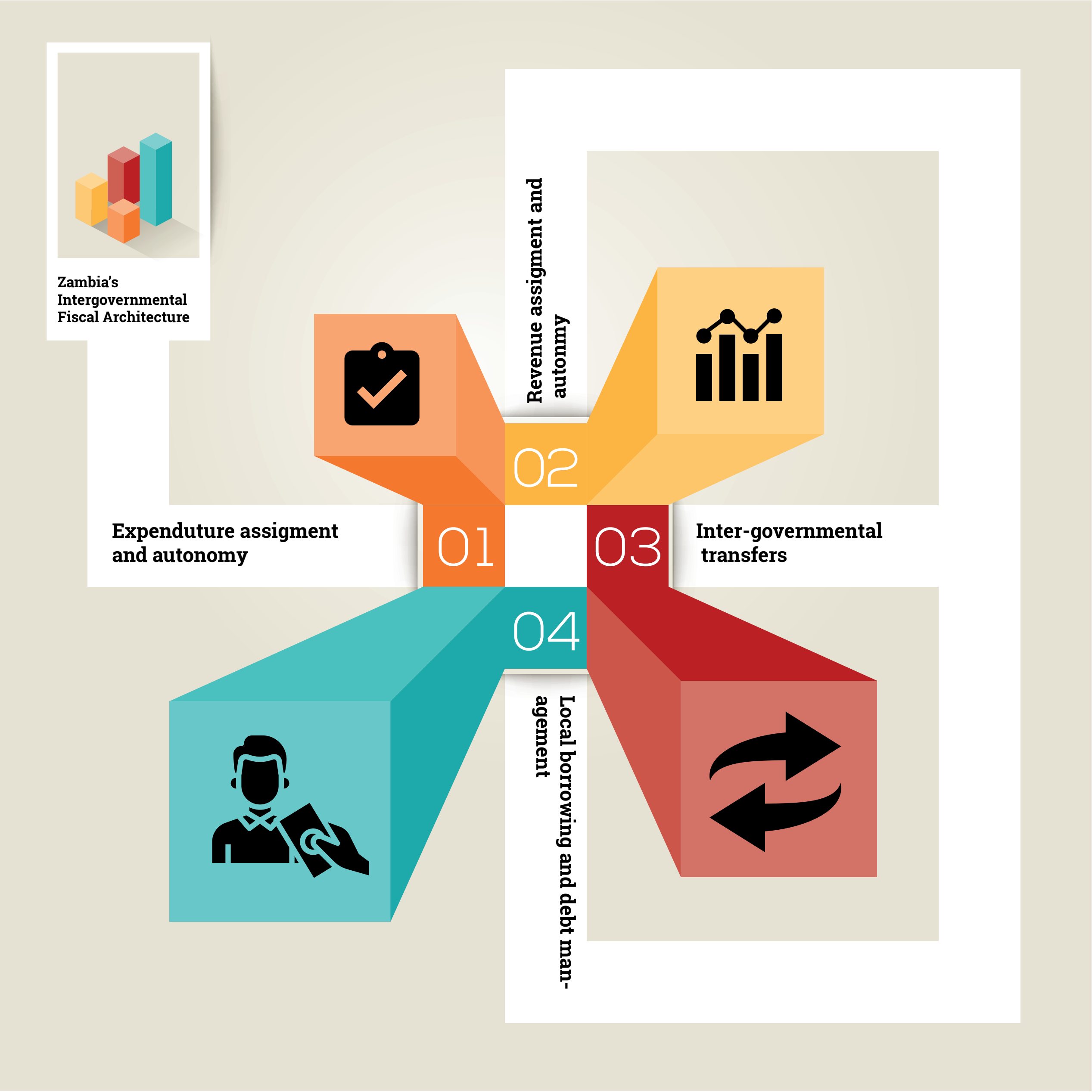
If well implemented the CDF has the potential to reduce inequalities, alleviate poverty, lower unemployment, and improve local governance structures. The CDF also has potential to be used as tool for facilitating mobilization of additional investment and unlocking alternative financing such as climate finance and grants.

Pillar 4: Local borrowing and debt management

Governments, including local governments, need to borrow for short term cash management and to fund longer term capital investments. The fourth pillar, local borrowing and debt management, caters for this.

Despite these various funding arrangements, Local Authorities (LAs) remain underfunded, negatively impacting their ability to deliver services to the communities. The funding deficiencies are compounded by the gradual removal by central government of certain financing and service provision functions of councils, such as housing and water, including inability by local authorities to collect taxes and levy in various sectors, e.g., transport, exacerbated this situation. The erosion of the local authority's capacities to raise their own resources has negatively impacted service delivery resulting in public discontent.

Figure 5.3: Zambia's Intergovernmental Fiscal Architecture (IFA)



Source: Intergovernmental Fiscal Architecture Report.

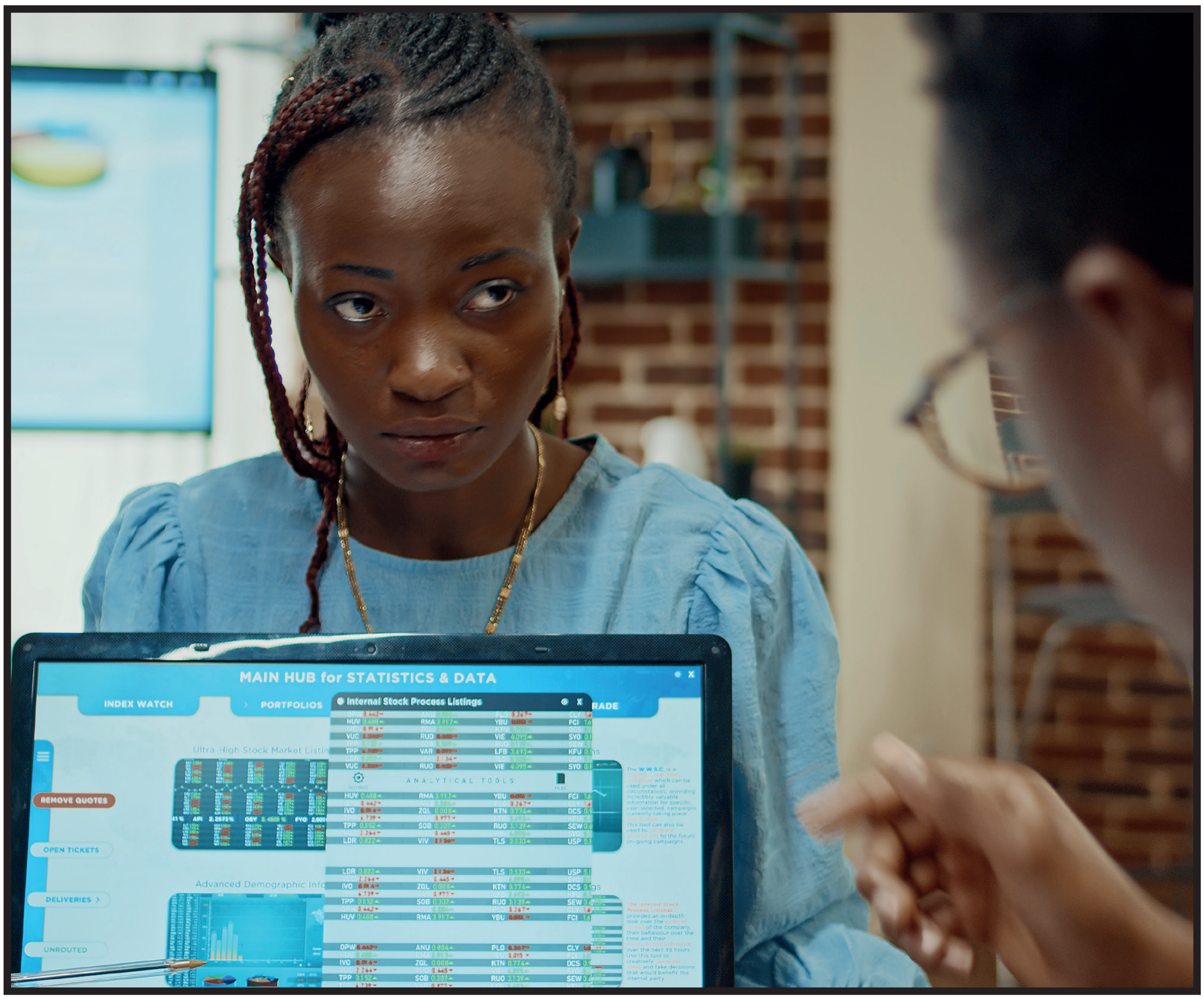
5.6.4 Key Takeaways

- Zambia has an elaborate intergovernmental fiscal architecture, albeit weakly implemented.
- Despite making strides toward actualizing decentralization, Zambia still remains highly fiscally centralized, with main functions pending full devolution.
- The recent (since 2021) increase in allocations to CDF is expected to catalyse the fiscal decentralization, provided the remaining implementation bottlenecks are addressed.
- Low own source revenue collections by LAs is a threat to fiscal sustainability and attainment of grassroot-driven economic growth.

5.6.5 Recommendations

- Government must expedite implementation of the Decentralization Policy (latest version) to address identified gaps in the regulatory frameworks.
- There is need to capacitate LAs to increase collection of own-source (local) revenues. This also calls for expanding the LA revenue bases by exploring diaspora resources (diaspora municipal bonds), local PPPs, among others.
- Government must quickly address the remaining bottlenecks in the CDF process by further decentralizing the approval processes down to the district level, and strengthening the institutional arrangements by allocating more funding to key CDF structures such as Ward Development Committees (WDCs) and Constituency Development Fund Committees (CDFCs).
- There is need to commission research to assess the development finance landscape at subnational level.
- More efforts must be directed at strengthening systems to improve coordination between central and local governments. One way is through ensuring all LAs develop IDPs.

06


MAIN HUB for STATISTICS & DATA
INDEX WATCH
PORTFOLIOS
Internal Stock Process Listings
REMOVE QUOTES
OPEN TICKETS
DELIVERIES
UNROUTED

Chapter 6 : Monitoring and Review

Robust Monitoring and Evaluation (M&E) systems are crucial for effective planning and efficient implementation of development programs and projects. The role of M&E in development planning is particularly crucial for countries like Zambia that face acute fiscal constraints. Without strong M&E systems in budgeting, financing, planning, procurement, development project implementation, a country cannot attain sustainable development. Zambia's recent fiscal woes and macroeconomic instabilities can be linked to its weak M&E systems, opening doors for resource wastage and misappropriation. Government stakeholders consulted bemoaned the absence of dedicated M&E systems in government departments, arguing that weak systems contribute to resource waste and revenue leakages.

6.1 Monitoring Systems for Public Resources

6.1.1 Overall Systems for Public Resources

To enhance transparency and accountability in the management and utilization of public resources, the Government established the Integrated Financial Management Information System (IFMIS), a computerized system for real-time monitoring of public sector spending. IFMIS is an innovation aimed at enhancing transparency and accountability in the management and utilization of public resources. The tool achieves this by facilitating a consistent recording and reporting of financial information for MPSAs onto a centralized system. However, IFMIS is mainly focused on the spending aspects of the fiscal framework, leaving out the revenue side.

While ZRA has internal systems and tools (Annual Reports, Tax Statistics Bulletins) for monitoring the tax revenue, it remains unclear how the non-tax revenues are monitored. Additionally, the fact that revenue collection in Zambia involves multiple actors including ZRA, MoFNP, BoZ, and other line ministries presents a stronger case for establishing an integrated M&E system for revenues.

To further reinforce PFM systems, the MoFNP set up a Treasury Single Account (TSA), a central system to facilitate consolidated public spending. The TSA also facilitates the tracking and monitoring of public spending across government departments.

Other innovations aimed at enhancing the monitoring and tracking of public resources include the Government Service Bus (GSB), an online platform for all government services that is designed to reduce revenue leakages.

Other notable monitoring and tracking tools include MRRR, an electronic monitoring tool established by the Bank of Zambia Amendment Act No, 1 of 2013.[46] The system requires all FSPs to develop electronic monitoring systems interlinked to the BoZ electronic balance of payment (eBOP) system. The monitoring system enables BoZ to track the following transactions:

- Foreign Exchange inflows and outflows
- The value of imports and exports of goods and their related outflows and inflows;
- International Transactions in Services;
- International transfers to or from non-residents;
- Profits or dividends received in respect of investments abroad;
- Borrowings and lending from and to non-residents;
- Investments in the form of equity and debt securities abroad;
- Receipts of both principal and interest on loans extended to non-residents; and
- Remittances of both principal and interest on loans from non-residents.

46. https://boz.zm/Guidelines_-_Electronic_BoP_Monitoring_Project_2019.pdf

Despite these reforms and innovations, tracking systems remain weak in Zambia and there is no system that interlinks the various ICT platforms and management information systems. There was also limited awareness of the existing tracking systems, even among Government officials. For instance, the MRRR did not come up during the Stakeholder consultations.

6.1.2 The Role of the MoFNP in Monitoring and Tracking of Public Resources

The MoFNP is responsible for fiscal policy, including budgeting and debt management. The Budget Office at MoFNP coordinates with institutions such as BoZ to track inflows, both domestic and international. The Budget Office receives daily inflows statements from BoZ that include tax, and non-tax revenues, international flows, and debt schedules. The MoFNP uses these inputs from BoZ to undertake analytical assessments and build budget tracking and monitoring tools.

The analytical budget assessments include the quarterly Budget Execution reports, Estimates of Revenue and Expenditure (Yellow Books), and tools such as Fiscal Tables. The reports from BoZ also form the materials for tracking expenditures over time. The Ministry also publishes the following reports:

- Monthly Economic Indicators: information on macroeconomic indicators, domestic revenues, grants, and expenditures.
- Annual Economic Report and, the Quarterly and Midyear Economic Reviews: information on budget performance, debt, and sectoral developments (Real, external, monetary, and financial sectors)

However, most of .these monitoring and reporting tools remain largely paper-based, and uncoordinated, creating inefficiencies in the M&E chain. As one MoFNP official aptly put it “the lack of an automated system to track revenue inflows presents challenges for real-time analysis and reconciliation, creating a day lag”. Additionally, despite having several tools to track expenditures and revenues, such as IT platforms, documents, and spreadsheets to monitor revenues and expenditures, Zambia lacks an integrated system for tracking inflows of resources from domestic and international sources.

6.1.3 Monitoring Debt

Zambia has been entangled in debt issues over the years, culminating in default in 2021, a debilitating debt crisis, and a contentious debate on the authenticity of Government reported debt statistics. The inconsistent debt statistics are a symptom of deeper problems, including inadequate statistical systems and a lack of management information and M&E systems for debt management. Recent reforms such as the enactment of the PDM Act in 2022 are an attempt at rectifying issues around the management of public debt. Prior to the enactment of the PDM Bill in 2022, debt contraction and management were governed by the Constitution and the Loans and Guarantees Authorisation Act (LGAA) which contradicted the Constitution on certain aspects around debt contraction. By providing for loan and debt contractual processes including the preparation of annual borrowing plans, establishment of a Debt Management Office, and setting up of debt ceilings, the PDM Act helps to strengthen systems for tracking and monitoring debt and its usage.

The MOFNP uses the Debt Management and Financial Management System (DMFAS) to track its debt. The DMFAS, which is aimed at enhancing transparency in debt data and management through improved tracking and reporting contains a wealth of information on loans, repayment terms, funded projects, and projected debt servicing. Through this system, MoFNP is able to generate analytical reports such as the Debt Statistical Bulletin (Quarterly), Debt Summary reports, and the recently mandated Debt Sustainability Reports (annual).[47] The recently approved PDM Act is expected to improve debt tracking and the production and publication of statistics. There are also plans to link the DMFAs to the BoZ system, and other budget and accounting systems such as the IFMIS, ensuring an integrated approach to monitoring and tracking of spending and resource flows.

The MoFNP also produces a Medium-Term Debt Management (MTDM), a three-year debt management plan, similar to the MTEF. However, the MTDM has not been produced consistently, creating gaps in monitoring and potential room for debt mismanagement. These M&E gaps could in part explain why Zambia’s debt reached unsustainable levels, triggering fiscal and macroeconomic imbalances.

47. The recently enacted Public Debt Management Bill of 2022 requires the MOFNP to produce debt sustainability reports.

6.1.4 Monitoring Public Procurement

Like other developing countries, Zambia has a poor PFM record, manifesting in resource wastage and mismanagement. Weak procurement systems have created an enabling environment for this mismanagement of public resources. The Public Procurement Act No.8 of 2020 is the main legislation guiding the procurement system in Zambia. The Act also provides for the establishment of the Zambia Public Procurement Authority (ZPPA), an institution mandated to formulate procurement policy, regulate aspects of procurement, set standards for procurement, enforce compliance and performance, and information dissemination on procurement issues.

However, recent revelations of corruption and abuses in the procurement system suggest that the available frameworks are too inadequate to respond to procurement issues. Weak M&E in procurement processes results in failure to adhere to procurement processes, contributing to inflated costs and delays in the completion of projects, and sheer abandonment of certain projects. The weaknesses in M&E systems are also reflected in widespread mismanagement in other government departments including human resources where reports of ghost workers are not a new phenomenon.

Zambia has been leveraging ICT to curb corruption and abuse of the procurement system. To this effect, Zambia introduced the Electronic – Government Procurement (E-GP) in 2015 to enhance accountability and transparency in the procurement system. This system also allows for the monitoring of procurement processes in the public. However, the E-GP has not been completely rolled out, limiting its effectiveness in combatting abuse of public resources.

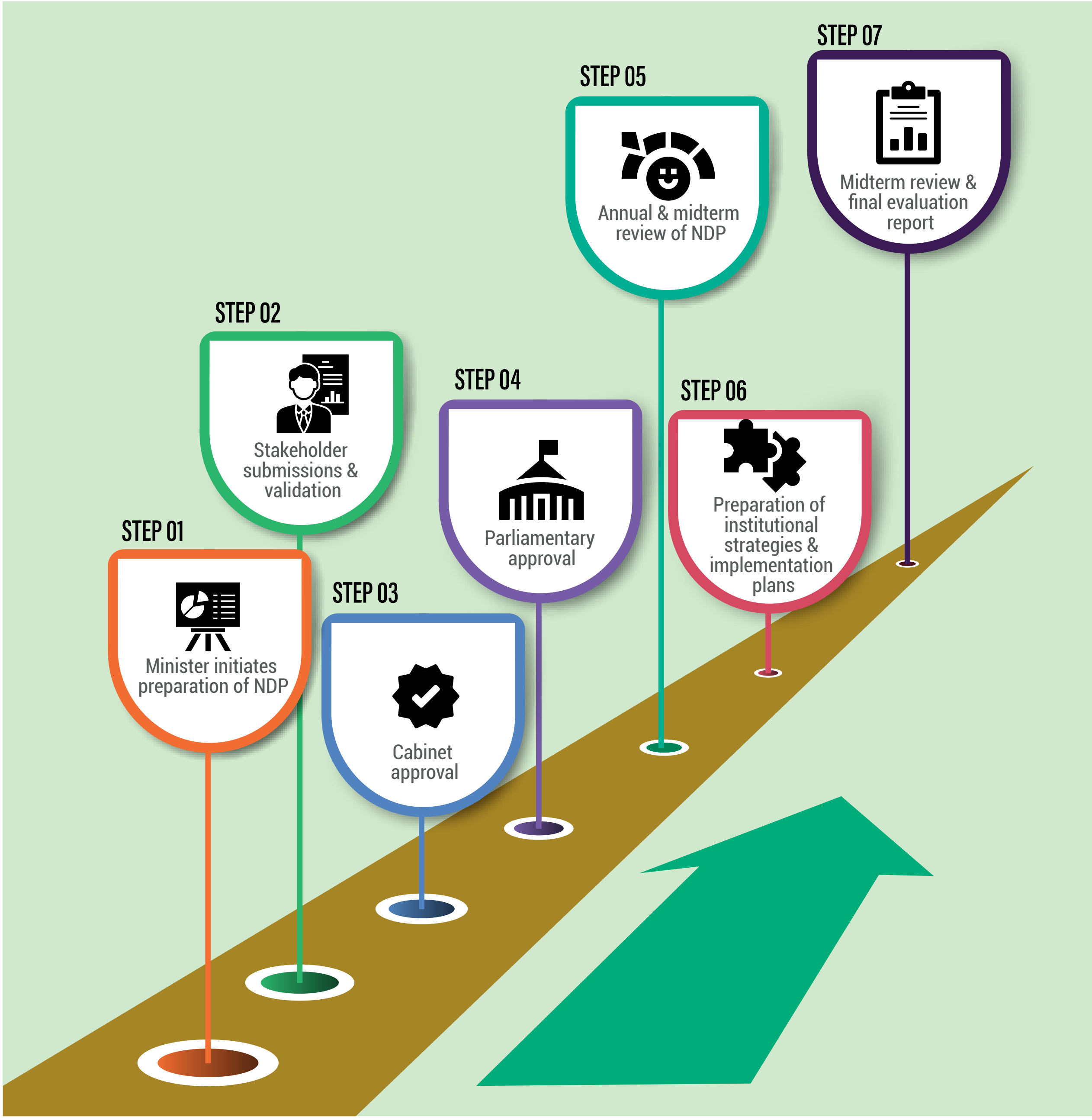
6.2 Monitoring Systems in National Plans

The National Planning and Budgeting Act of 2020 guides national development planning and budgeting in Zambia. Zambia's national development planning cycle has some inbuilt M&E mechanisms, including quarterly[48] and annual midterm reviews, and annual M&E plans (Figure 6.1). The recent move to a cluster planning approach entails a refocus on cluster-based M&E systems, and the need for an integrated approach to M&E as provided in the national development plans.

Parliament undertakes some form of M&E of the plan as the Minister responsible for finance is required to present an annual review of the NDP and a mid-term review three years into the Plan to parliament. Further, within two years of the NDP's expiration, a final evaluation report, providing more opportunities for parliamentary oversight and M&E. Clusters that are an integral part of the planning and implementation governance structure are active at the second stage (stakeholder submissions and validation).

48. In the 7NDP quarterly reviews were done against the set annual targets. However, in the 8NDP quarterly targets have since been set to facilitate quarterly reviews.

Figure 6.1 National Development Planning Process



Source: Adapted from ZIPAR Budget Analysis Toolkit and National Planning and Budgeting Act, 2020

6.3 Monitoring of National Budgets

Although the MoFNP has the mandate to formulate and implement the National Budget, the whole process involves several key stakeholders including Cabinet, the National Assembly, MPSAs, the Attorney General, non-state actors such as the private sector, civil society, and the general public. The National Planning and Budgeting Act No. 1 of 2020 is the main law guiding the budgeting process in Zambia. Another key piece of legislation is the PFM Act No. 1 of 2018 which provides for the management of public funds including mechanisms for strengthening accountability and oversight in the PFM framework. As already alluded to in earlier sections, the budget process includes four distinct stages, namely budget formulation; legislative approval stage; implementation; and post-implementation/budget accountability.

The budgeting cycle in Zambia includes some aspects of M&E, albeit weak, and limited. Some institutions performing M&E systems in the budgeting process include parliament and the Auditor General's Office. The M&E processes are conducted a bit late in the budget cycle, mostly intensifying in the last stage: post-implementation/budget accountability. Ideally, these processes should start much earlier because reporting is provided for in the law, including the call circulars. The obtaining situation where the reports are done in quarter 4 contributes to the weakening of M&E systems. The processes are there and clearly spelt but MPSAs lack prioritization of M&E and the attention it deserves.

The OBB is an attempt to strengthen the tracking processes and guides the monitoring by providing parameters (and specifics on the items budgeted for monitoring of the budget). But all these systems need to be integrated to facilitate effective tracking of resource mobilization and utilization. The Public Finance Management (PFM) Act No. 1 of 2018 provides for some form of M&E by requiring the Minister responsible for Finance to submit several reports to the National Assembly, including a Treasury Minute on the implementation of recommendations of the PAC and the annual report and financial statements. Parliamentary oversight and monitoring functions are mostly limited to the legislative approval (Second stage) of the budgeting cycle. The last stage (Post-implementation/Budget Accountability) includes some aspects of evaluation, mainly through the Auditor General's Office. The Public Accounts Committee (PAC) also undertakes M&E functions on public expenditure based on the report of the Auditor General, and other accounts.

Further, the Auditor General's M&E role is limited by the fact that the report is only due in September of the following year (too late to inform subsequent stages of the budgeting cycle). This makes it difficult to incorporate the report findings in subsequent budgets. Additionally, the in-year M&E budgetary processes are limited especially on the part of the line ministries. It is, therefore, not surprising that the Auditor General's reports continue to expose various forms of financial mismanagement and misapplication of public resources.

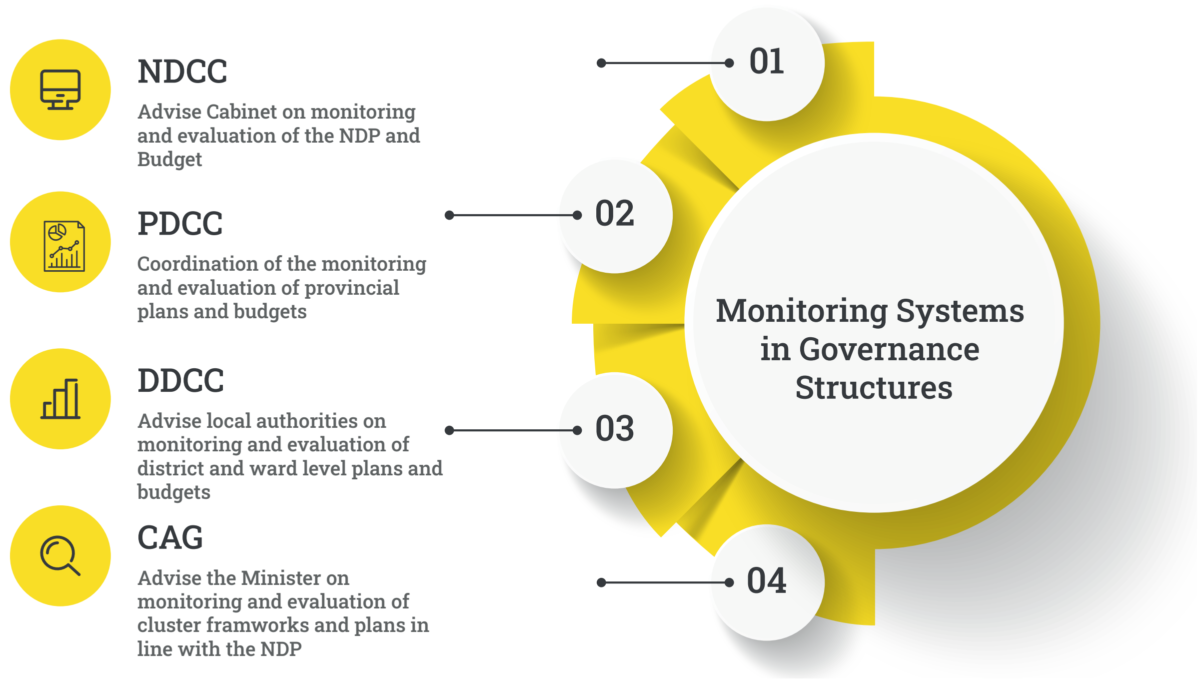
6.4 An Integrated Approach to Monitoring of National Plans and Budgets

Zambia's budgets are backdropped by the MTEF while aligning with its NDPs. The National Planning and Budgeting Act No. 1 of 2020 is the main piece of legislation guiding integrated national planning and budgeting, good governance, and M&E systems, among other provisions. The Act also establishes four crucial governance structures, namely the National Development Coordinating Committee (NDCC), Provincial Development Coordinating Committee (PDCC), District Development Coordinating Committee (DDCC), and the Cluster Advisory Group (CAG), all of which incorporate aspects of M&E (Figure 6.2). Despite these provisions in the Act and Policy, implementation remains a challenge. The policy gaps are reflected in non-adherence to the provisions in the available frameworks, contributing to the slow uptake of M&E programs and implementation failures.

In line with its commitment to improving the implementation of the 8NDP to achieve its developmental targets, the 8NDP is accompanied by an M&E framework that is anchored on the National Performance Framework for Vision 2030. The key actors in the M&E framework include Government, the private sector, civil society, faith-based organizations, cooperating partners, local authorities, traditional authorities, and the general citizenry. The M&E framework takes an integrated approach encompassing institutions at national, provincial, district, and ward levels. The alignment between OBB and the 8NDP is testament to the enhanced integration.

Further, inadequate M&E structures across government institutions, along with weak data and statistical systems to capture relevant data presents a daunting challenge for effecting monitoring and tracking of budgets, NDPs, and their integration.

Figure 6.2: Monitoring Systems in Governance Structures



Source: Adapted from the Planning and Budgeting Act of 2020

6.5 Gaps in Monitoring Systems

Like other countries, Zambia recognizes the crucial role of evidence-informed planning and reporting in national development. However, despite Zambia's commitment to long- and medium-term planning as demonstrated through Vision 2030 and successive NDPs, not much progress has been made in building effective systems for monitoring and evaluating development programs. As already highlighted in prior sections, effective implementation of development plans requires enhanced mobilization of financial resources, prudent utilization of the resources, and robust monitoring and tracking systems. Zambia's recent fiscal and macroeconomic challenges are in part a symptom of weak fiscal frameworks and inadequate M&E systems.

Despite recognizing the importance of effective tracking of development programs, Zambia has made limited progress with strengthening M&E systems. To date, M&E systems and capabilities remain weak and fragmented across Ministries, Provinces, and Other Spending Agencies (MPSAs). Additionally, development partners have set up their own parallel M&E systems, further weakening the monitoring systems. These weak M&E systems are a major hindrance to the attainment of development objectives including SDGs and establishing integrated planning and financing frameworks that are vital for sustainable development.

Further, the weak and at most non-existent M&E systems also contribute to the weedy linkage between annual budgeting and NDPs. The misalignment in planning and budgetary processes could explain the limited successes in implementing NDPs. For instance, an analysis of the performance of the 7NDP over 2017-2021 indicates that only 29 percent of the output targets were met.

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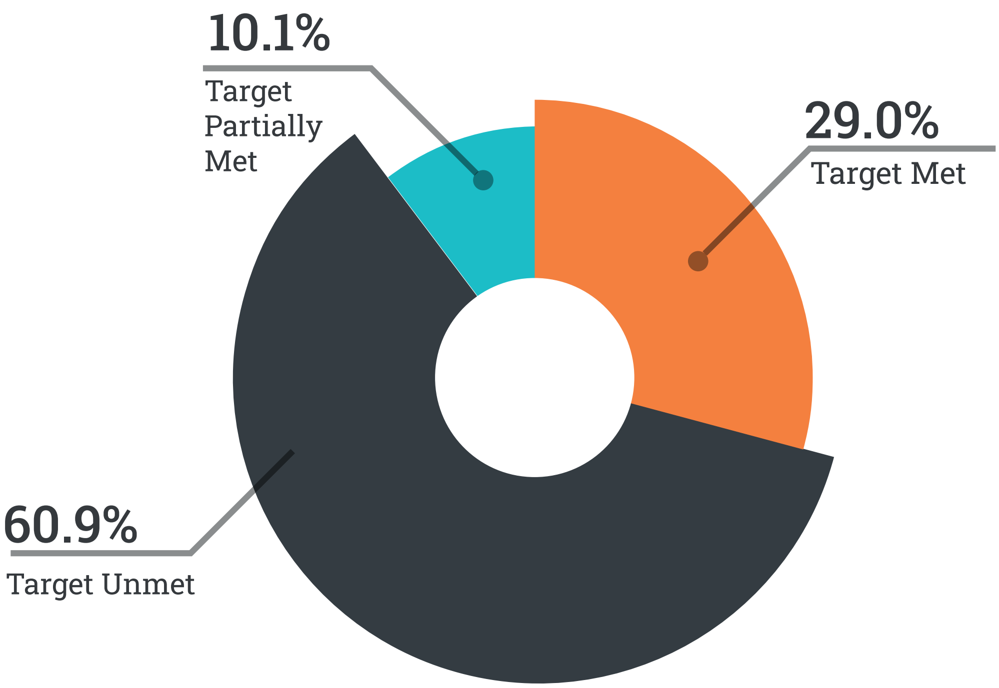


Source: Adapted from the 2021 MoFNP APR Report

The fragile M&E systems can be attributed to weak legislative and institutional frameworks for M&E.[49] For instance, the MPSAs do not have dedicated M&E units nor staff establishments, resulting in strained national M&E systems. Consequently, M&E has not been adequately planned and budgeted for in prior budgets, contributing to low M&E capabilities in key institutions. This explains the fragmented and at most absent across government units and established governance structures.

Additionally, inadequate, uncoordinated, and mostly manual Management and Information Systems (MIS) in government contribute to weakened M&E systems in Zambia. To bolster MIS functions and enhance National Statistical System (NSS), the Government crafted the National Strategy for the Development of Statistics (NSDS). The goal of the NSDS is to create a Planning, Monitoring & Evaluation, and Statistics unit in all MPSAs so as to strengthen and decentralize M&E functions.

Further, the Zambian ICT sector is characterized by unstructured, uncoordinated, and inadequate frameworks for the interface. This presents challenges for the integrated collection and reporting of M&E statistics. To counter fragmentation in ICT systems, the government established the Electronic Government Division (SMART Zambia) to coordinate and implement electronic government (E-Government) in the country.

The Government recognizes the weaknesses in the current M&E system and experts spoken to provided suggestions on how to enhance the existing systems (Box 6.1).

49. The National Strategy for the Development of Statistics (NSDS)) Development of Statistics (NSDS) 2014 – 2018).

Box 6.1: Government Views on the Current M&E System

Government recognizes the critical role of strong M&E in national development. Following consultations from Government Ministries, the following recommendations were made:

"Government needs to expedite the roll-out of the Government-Wide Management Information System that will enhance monitoring of data completeness by sectors rather than just leaving it to sectors alone". "Sector information systems should be strengthened to capture more disaggregated data".

"There is need to allocate adequate resources towards the development and finalization of the new National Strategy for Development of Statistics (NSDS 2020 – 2022) and align it to the 8NDP". "Development partners should align themselves to the national measurement framework other than creating parallel frameworks for monitoring".

Source: Author's contruction

To respond to the observed weaknesses in the existing M&E systems, the Government, with support from CPs, the government introduced and rolled out the Government-Wide Management Monitoring System (GW-MMS) to select line ministries in 2022. While IFMIS focuses on financial accountability, GW-MMS is an attempt at filling the gaps in the monitoring system by concentrating on development accountability. The GW-MMS tracks progress on the following:

- Targeted annual outputs in the annual budgets & work plans;
- Projects and programs under implementation.
- Targeted results (outcomes and impacts) in NDPs, and other regional and international frameworks
- Budget performance for developmental works during implementation.

The Government must enhance its capacity to monitor and report flows to national priority areas by sharpening existing processes and tools and introducing new ones. At the same time, it must incorporate aspects of existing systems while enhancing integration. Some of the actions that need to be undertaken to strengthen M&E systems include:

- Enhancing the capacity of the MoFNP Budget office to undertake analytical assessments.
- Capacitating MoFNP to produce budget execution reports regularly, and expand its scope to include a section on flows to the private priority areas.
- Conduct regular public expenditure reviews, with a cluster focus.
- Expand the coverage for M&E and related tools to include reporting on private (domestic and international) flows such as FDI .
- Integrate the reporting processes between MoFNP, BOZ, ZRA, and other relevant institutions to make it easier to track the flows.
- Establish tools for monitoring and improving the alignment between fiscal policies and national priorities.
- Conduct detailed review of existing M&E systems across institutions (state and non-state).
- Mobilize financial and technical resources to enhance reporting and monitoring capabilities for MPSAs and other key institutions such as ZamStats, BOZ, and MoFNP, among others.
- Enhance the capacity of SMART Zambia to address the fragmentation in E-Government, accelerating integration in M&E systems.
- Leverage ICTs to automate tracking systems and digitize reporting processes.
- Strengthen M&E frameworks by establishing M&E departments in all Government institutions, including subnational government.

- Devote resources toward embedding M&E processes at all levels of planning and budgeting and ensuring timely monitoring.
- Review existing systems and explore potential areas of possible interface.

Following the above actions, the GW-MMS can be further improved to monitor the INFF process. Modifications to the GW-MMS must take an integrated monitoring approach by incorporating valuable aspects of the existing M&E systems. This calls for a detailed review of existing M&E frameworks to appreciate their strengths and gaps.

6.6 Key Takeaways

- ICT systems for supporting M&E processes remain highly fragmented and inadequate across government levels, sectors, and actors in the development space. For instance, some Government institutions, especially in rural areas mostly use manual MIS systems.
- M&E systems and capabilities remain weak and fragmented across MPSAs, and development partners. This problem is more pronounced when it comes to tracking of financial flows and progress on the implementation of development programs.
- Systems for tracking the alignment of budgetary processes with NDPs and other national development priorities are grossly inadequate.
- Lack of capacity in planning at sectoral and subnational levels contribute to weak M&E systems
- M&E has not been adequately planned and budgeted for in prior budgets, contributing to low M&E capabilities in key institutions.
- Paucity of disaggregated data for M&E processes, contributing to weak monitoring systems.

6.7 Recommendations

- Government must capacitate relevant institutions such as SMART Zambia, ZICTA and the ministry responsible for information to address fragmentation in the ICTs.
- Government also needs to leverage ICTs to automate reporting systems and digitize records.
- Government must strengthen M&E systems by incorporating it in tertiary education systems to enhance M&E capacities.
- Government must to establish M&E units in all government ministries and key government institutions. This also calls for creating a budget line for M&E and devoting more resources toward it.
- IT systems such as IFMIS should be activated to support tracking of all types of flows going to support the NDPs. This will ensure coordinated and harmonized monitoring and tracking flows in terms of their sources and disbursements by sector and national priorities.
- Reporting and tracking of all key flows should also be institutionalized to ensure consistent and timely reporting.
- Explore alternative monitoring and reporting tools for tracking the alignment of budgetary processes with NDPs and other national development priorities.
- M&E systems will need to be extended beyond development programs to include tracking financial flows and progress on the implementation of development programs.
- Accelerate the roll-out of the GW-MMS to address fragmentation in M&E systems. The GW-MMS could be enhanced to monitor the INFF process.
- Enhance the capture of financing from NGOs and development partners.
- Capacitate government institution and LAs in planning.
- Address knowledge and data gaps to improve M&E systems. This entails investing in review of existing monitoring systems, enhancing ZamStat's capacity to collect M&E-related statistics and routine data collection in relevant institutions.

07

Chapter 7: Governance and Coordination

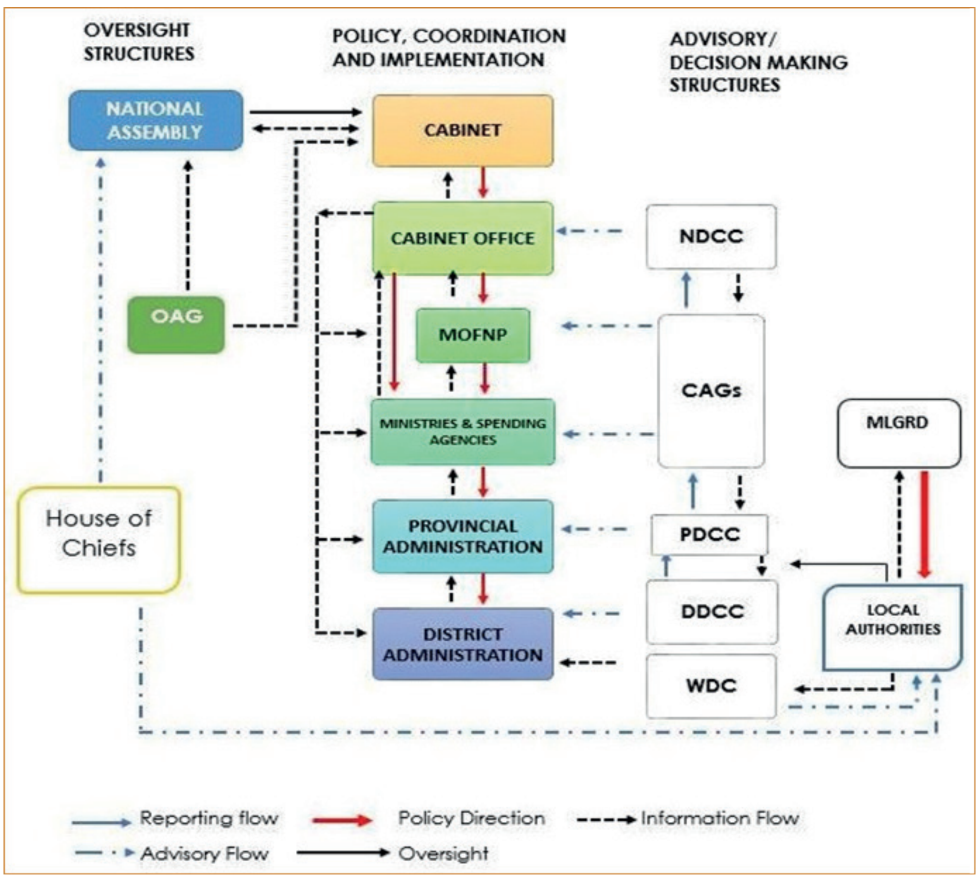
In this Chapter, we outline the existing governance structures, which could form the basis for the implementation of the Intergrated National Financing Framework. National and subnational coordination and implementation structures for the 8NDP are also discussed with a view to situate the INFF implementation structures into the existing governance structures at both the national and subnational levels.

7.1 Institutional Arrangements for the 8NDP

Solid governance structures, including robust institutional arrangements are crucial for successful implementation of the development plans. As a result, the Government has put in place the necessary regulatory framework to inform the institutional arrangements, in line with the National Planning and Budgeting Act No. 1 of 2020. The INFF should be implemented within the existing governance structures to ensure effective implementation and mobilization of resources. The key governance structures are divided into three main categories, namely oversight, policy and coordination, and advisory (Figure 7.1). The NDCC, CAGs, PDCCs and DDCCs are responsible for coordination and provision of oversight during the implementation of the 8NDP at national level, while WDCs cater for subnational implementation (MoFNP, 2022). At the district level, the DDCCs coordinate the work in constituencies, wards, and zones. The constituencies, wards, and zones are essential in coordination and governance at the district level. Some constituencies have relatively more wards than others. Similarly, there is variation in the zones within the wards. Given this complex governance structure, it is crucial to ensure that there is wider stakeholder involvement and improved governance outcomes for the development processes.

Policy and coordination will be provided by MoFNP, Cabinet, MPSAs, provincial and district administrations. Advisory structures include NDCC, CAGs, PDCC, DDC, MLGRD, WDCs and local authorities.

Figure 7.1: Overall Institutional Arrangements for the 8NDP



Source: MoFNP 2022, 8NDP

The overall instructional framework for the 8NDP includes a combination of oversight, implementing and advisory structures (Table 7.1.1). These governance structures for the 8NDP can also be strengthened to facilitate operationalization of the INFF.

Table 7.1.1 Institutional Arrangements for development planning in Zambia

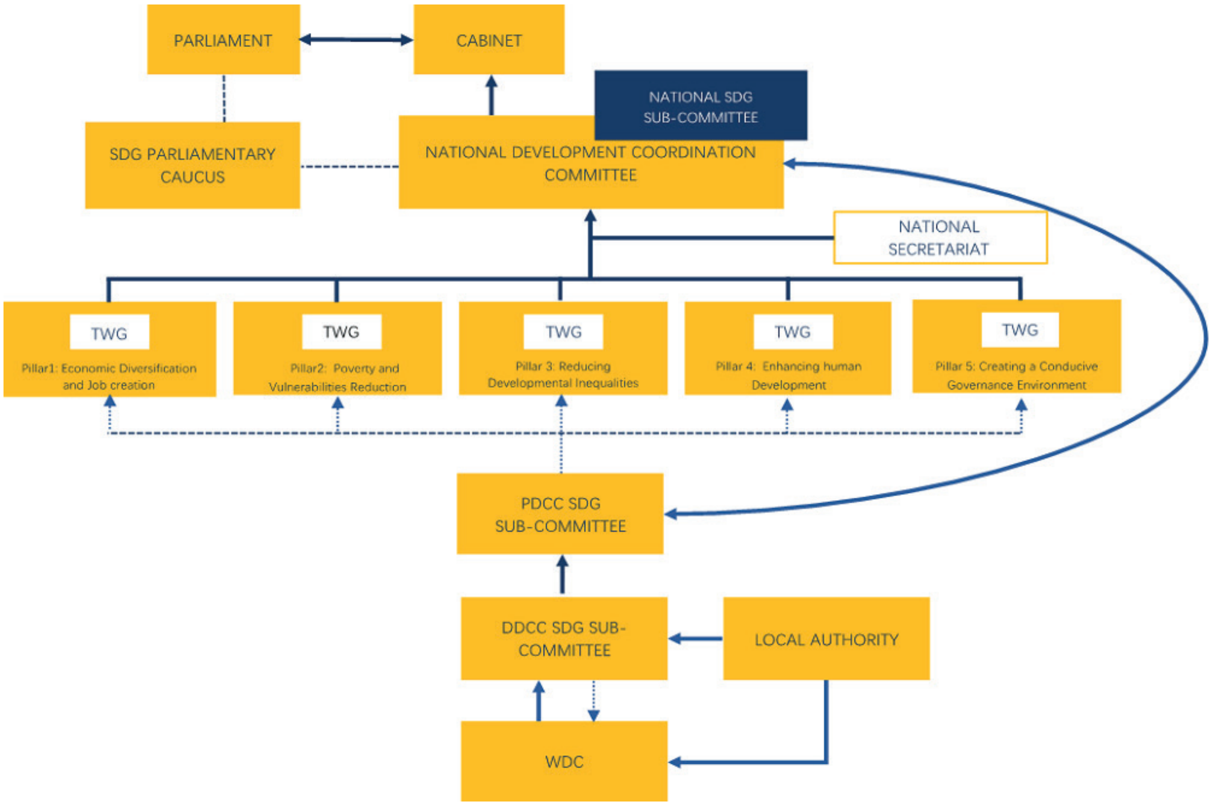
Institution	Role
National Assembly	Makes laws, approves the budget and plays an oversight role over the executive.
Cabinet Office	Coordinates implementation of government policies, systems and procedures, including monitoring and evaluation of the performance of the public service.
Office of the Auditor-General	Audits government institutions, parastatal organisations, statutory organisations, donor funded agencies, including any other institution in which public resources have been invested.
Cabinet	Comprised of ministers and the President who take responsibility for government policy direction and ensure the required environment for policy implementation.
Ministry of Finance and National Planning	National planning, budgeting, approval of public projects and investments, including the facilitation of resource mobilization for various development initiatives.
Ministry of Local Government and Rural Development	Implementation of decentralization process, NDPs through local authorities. Ensures Ward Development Plans are compiled, including Integrated Development Plans, aligned with NDPs
House of Chiefs	Making recommendations to the National Assembly and Local Authorities on socio-economic development matters. Also plays advisory role to the government.
Institution	Role
Ministries, Provinces and other Spending Agencies	Coordinate the implementation of NDPs, develop institutional Strategic and Implementation Plans that are used to achieve development targets.
State-Owned Enterprises	Perform various commercial activities to supplement private sector investments, and generate additional government revenues.
Private Sector	Plays a crucial role in job creation, economic transformation and resource mobilization.
Civil Society Organisations	Implementing community-based projects, especially those aimed at poverty reduction, youth unemployment, including gender inequality. Complement government efforts to assist the vulnerable in society. Perform advocacy role, including the provision of checks and balances in the governing of the country.
Cooperating Partners	Provide different sources of financing mechanisms and technical assistance.

Source: Adapted from the MoFNP 8NDP Report and other sources

7.2 Leveraging Existing Governance Structures

The Government remains strongly committed to the implementation of the Vision 2030. Attainment of the targets in the Vision will require significant and efficiently mobilized resources, and an effective governance system to guide their mobilization. To be effective, integrated national financing frameworks (INFFs) should be driven by strong political will and wider ownership and stakeholder involvement. For this reason, governance structures and coordination mechanisms should be located at high level government body, such as the NDCC which is tasked with implementation of the NDP and or implementation of the SDGs, and mainstreamed into national development frameworks (Figure 7.2).

Figure 7.2: Zambia National SDGs Coordination Framework



Source: Ministry of National Development Planning 2019

Zambia already has established governance structure to spearhead implementation of its national development programs as shown in the Figure above and preceding subsection. However, the institutional arrangements remain highly fragmented and centralized. Additionally, there is limited information on the existence of structures to spearhead the operationalization of the INFF.

This DFA recommends tweaking the structure presented in Figure 7.2 to establish an INFF Oversight Committee. Further consultations with MoFNP and key stakeholders are needed to arrive at a preferred INFF governance structure. Nonetheless, this DFA proposes the following starting-point membership composition for the INFF Oversight Committee:

- MoFNP (as chair)
- Line ministries/Cabinet
- Members of Parliament
- ZRA
- BoZ
- Private sector (representative institutions
- UN Agencies
- Donor Agencies and CPs
- CSOs

Further, due to the slow and incomplete devolution of functions to Local authorities, there are no clear institutional arrangements for an integrated financing framework at local government level. With the enhancement of the CDF, along with expansion of its coverage, integrating local government resource mobilization and spending into national level resource mobilization frameworks will be key. The revival of the inclusive development agenda through the enhanced CDF and emerging reforms will also help strengthen the governance structures for the INFF.

7.3 Key Takeaways

The main takeaways are

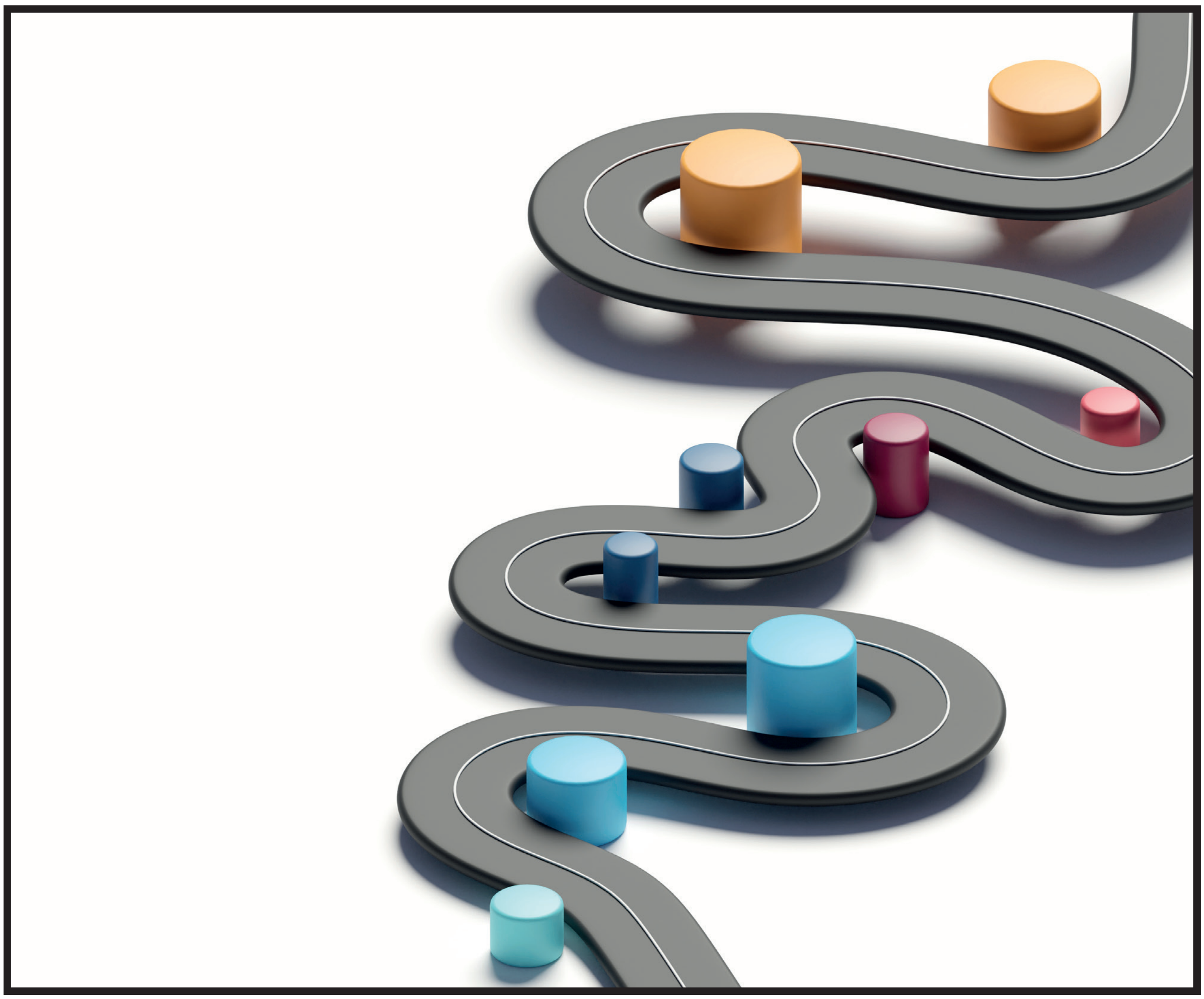
- Zambia has the regulatory and institutional arrangements for coordination of development planning and budgeting, albeit weak.
- The available governance structures and coordination mechanisms for national development planning can be strengthened and adapted to host the INFF.
- Information on specific governance structures for the INFF is scanty and, at most unavailable.
- Slow actualization of decentralization could pose challenges for establishment of a robust INFF governance structure.

7.4 Recommendations

The following are the main recommendations:

- Government must constitute an Oversight Committee for the INFF in consultation with key stakeholders
- Governance and coordination systems need to be strengthened further to facilitate effective mobilization of resources and establishment of an INFF.
- Set up appropriate inter-institutional steering committees (Ministerial, Agency, development partners) to oversee the operations of the INFF.
- Enhance coordination among existing governance structures and actors in the development finance space.
- Mobilize resources to support the operations of the INFF governance organs, including at subnational level.
- Sensitize Government institutions and key stakeholders on the INFF process.
- There is need to accelerate the decentralization process to create a workable environment for the INFF.

08



Chapter 8: INFF Road Map

The study makes the following broad recommendations grouped by type of flow and building blocks 2-4 (Financing, Monitoring and Review, and Governance and Coordination).

Overall Actions to Improve Financing Frameworks

The road map for building blocks 2-4 is presented in the table below.

Table 8.1.1 INFF Road Map

A. Overall Actions to Improve Financing Frameworks

Actions	Time Frame	Agencies
Conduct/Expedite detailed costing of 8NDP, subnational plans	Short-term (2023)	MoFNP, UN, ZamStats, other CPs
Assess the resource requirements for the Vision 2030	Medium term (2023-2025)	MoFNP, Line ministries, UN, Private sector, CPs
Review current policies, frameworks, including PFM to identify gaps	Short-term Term (2023-2024)	MoFNP, CPs
Strengthen capacities in OBB among MPSAs	Short-term (2023-2024)	MoFNP
Strengthen strategic planning, PFM systems and enhance budget coherence	Medium term (2023-2026)	MoFNP, line ministries, National Assembly

B. Actions for Domestic Public Finance

Actions	Time Frame	Agencies
Strengthen the frameworks for mobilization and management of public finance: ▪ Capacitate revenue collection institutions in information management ▪ Improve data and information sharing among institutions involved in revenue collection such as ZRA, NRFA, FRA ▪ Develop a system to strengthen coordination between MoFNP and other institutions involved in revenue collection ▪ Review the existing legislation on revenue collection with a view to strengthen coordination ▪ Leverage existing systems such as the GSB to strengthen coordination among key institutions, boosting revenue mobilization.	Medium-term (2023-2026)	MoFNP, ZRA, Line Ministries, CPs,ZAMSTATS
Devise measures to boost domestic revenues, focusing more on non-tax revenues: ▪ Establish an institution to coordinate the administration of non-tax revenues. ▪ Leverage ICTs, business groups/associations, the CDF to bring the informal sector into the tax net. ▪ Conduct a public expenditure reviews, especially on the performance of SOEs to get a better understanding of the reasons for their underperformance. ▪ Enhance IDC's capacity to promote growth of SOEs ▪ Scale back on the use of fiscal incentives, and increase transparency in their applications.	Medium term (2023-2025)	MoFNP, Line ministries, UN, Private sector, CPs,CSOs

Curb IFFs: ▪ Invest in automation and information sharing among LEAs for easier tracking and monitoring of illicit financial flows. ▪ Enhance the capacity of LEAs through increased resource allocation and provision of technical support to sharpen their investigation, prosecution, and asset recovery capabilities. ▪ Capacitate relevant institutions such as the ministry responsible for mines in product evaluations and analysis to curb IFFs.	Short-term Term (2023-2024)	MoFNP, Line Ministries, ZRA, LEAs, CPs, regional groupings (COMESA, SADC), UN, CSOs
Enhance the frameworks for debt management to avoid the recurrence of the debt crisis: ▪ Deepen debt markets to exploit sustainable debt management options such as debt swaps (e.g., debt-for-climate swaps). ▪ Further enhance transparency around debt contraction and utilization of debt funds by publishing detailed debt statistics. ▪ Review existing frameworks to clarify provisions for debt management at sub-national government. ▪ Explore alternative and sustainable financing sources such as PPPs and climate finance.	Medium-term (2023-2026)	MoFNP, Line Ministries, Judiciary, CPs,
Promote efficiency and effectiveness of public expenditure: ▪ Conducting public expenditure reviews, focusing on SOEs and public investment.		

C. Actions for Domestic Private Sources

Actions	Time Frame	Agencies
Promote increased sensitization and public awareness of the roles and available investment opportunities at insurance and pension to stimulate institutional investments and public participation	Short-term (2023-2024)	Government, CSOs, CPs, Private sector
Further strengthen the PDM Act to limit purchase commercial bank purchase of debt .	Medium term (2023-2026)	MoFNP, Line ministries, National Assembly
Incentivise private sector investments in priority sectors such as agriculture, tourism and manufacturing.	Short-term Term (2023-2024)	MoFNP, CPs, Private sector
Improve financial inclusion: ▪ Ramping up financial literacy efforts (e.g., by promoting the use of local languages in financial transactions and packages). ▪ Promoting the use of FinTechs. ▪ Address ICT infrastructure gaps and user safety.	Short-term (2023-2024)	MoFNP; relevant line ministries, Private Sector, CSOs, CPs
Strengthen frameworks for PPPs: ▪ Review and further strengthen the regulatory framework for PPPs to maximise their economic benefits. ▪ Strengthen capacity of key PPP institutions focussing on appraisals, risk management and assessment. ▪ Enhance transparency and accountability (e.g creating a data base for PPPs, and public projects)	Medium term (2023-2026)	MoFNP, line ministries, National Assembly
Strengthen frameworks for public-private dialogue: ▪ Review the institutional arrangements for public-private dialogue. ▪ Enhancing coordination between PPDF, and other dialogue for a, think tanks and CSOs.	Medium-term (2023-2024)	Government, CSOs

D. Actions for International Sources

Actions to enhance Development Cooperation & Boosting ODA

Actions	Time Frame	Agencies
Strengthen frameworks for development cooperation to safeguard and attract concessional financing: ▪ By expediting the finalization of the National Policy on Development Cooperation	Short-term (2023-2024)	MoFNP, UN, Line Ministries, other CPs
Strengthen coordination and information sharing between government and CPs to optimize international flows: ▪ by enhancing the capacities of the MoFNP Development Cooperation department, and line relevant ministries (responsible for foreign affairs, trade and investment, social sectors), ZAMSTATS to manage information	Medium term (2023-2026)	MoFNP, Line ministries, UN, Private sector, CPs
Strengthen frameworks for international public finance ▪ Enhance transparency in utilization of development finance by availing information on financing gaps by sector ▪ Develop a robust and comprehensive ODA management system (e.g database for development finance)	Medium-term (2023-2026)	MoFNP, Line Ministries, CPs

International Private Sources

Actions	Time Frame	Agencies
Strengthen coordination through enhancing information sharing among key players such as MoFNP, ZDA, BoZ, relevant line ministries, and private sector to promote investment	Short-term (2023-2024)	MoFNP, UN, MCTI,ZDA, other line Ministries, CPs
Enhance the capacity of key institutions such as ZDA, and BoZ in promoting and tracking FDI	Medium term (2023-2026)	MoFNP, Line ministries, UN, Private sector, CPs
Prioritize the stabilization fiscal regimes and policies, especially in the mining sector	Short-term Term (2023-2024)	MoFNP, Line Ministries, CSOs
Strengthen coordination between ZDA and relevant ministries to lure investment to priority sectors (manufacturing, tourism, manufacturing, agriculture)	Short-term Term (2023-2024)	MCTI, line ministries
Take drastic steps to arrest the declining FDI trajectory: ▪ Leverage the trade agreements such as COMESA, SADC, AfCFTA ▪ Promote diaspora FDI by incentivizing them to invest home	Short-term Term (2023-2024)	

Strengthen the policy and regulatory frameworks to promote diaspora investments and boost remittances: ▪ Establish a desk or department for the diaspora affairs at ZDA. ▪ Strengthen coordination among embassies, the relevant MPSAs (foreign affairs, MCTI), and academia. ▪ Improve information flow between the Government and diasporans especially on available investment opportunities ▪ Incentivise financial institutions and capital market players to develop diaspora-tailored financial products and instruments to attract diaspora finance. These can take the form of diaspora bank accounts, and bonds	Medium term (2023-2026)	MoFNP, UN, MCTI, ZDA, other line Ministries, CPs

E. **Monitoring and Review**

Actions	Time Frame	Agencies
Monitor the finalization and approval of the M&E Framework for the 8NDP	Short-term (2023)	MoFNP, UN, ZamStats, other CPs
Collaborate with ZamStats to identify key indicators that will be used to track progress, the data collection methodology, and resources (financial and technical)	Short-term (2023)	MoFNP, ZamStats, Line ministries, UN, Private sector, other CPs
Integrate ICT systems and tracking of private flows and monitoring of development programs into existing electronic systems	Short-term Term 2023)	MoFNP, Government, Private Sector, CPs
Disseminate to all key stakeholders (Government, private sector) identified indicators and methodology employed to collect them	Ongoing (2023-2026)	MoFNP, ZamStats, private sector, National Assembly
Create a dashboard to harmonize and centralize data collection for financing flows for the 8NDP	Ongoing (2023-2026)	MoFNP, ZamStats, UN, private sector, CPs

F. **Governance & Coordination**

Actions	Time Frame	Responsible
Enhance Coordination among key stakeholders	Ongoing (2022-2026)	MoFNP; Private Sector; CPs, CSOs
Setup an INFF Steering Committees (Oversight, technical)	Short-term (2023)	MoFNP; Line Ministries; CPs, CSOs, Private Sector
Mobilize resources to support INFF governance structures	Short-Medium term (2023-2024)	MoFNP, CPs
Work with other key stakeholders to establish TORs for the committees	Short term (2023)	MoFNP; CPs, Line Ministries

09

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