

FOCUSING ON COMPETING NEEDS IN AN ECONOMY UNDER PRESSURE: THE CASE OF ZAMBIA

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Introduction

The government of Zambia, like many other countries, has tried its best to provide resources, but it has so many competing needs that there is only so much that can be done given those resources. The government has therefore had to rationalise the available resources to meet these competing needs. The responsibility of government is derived from the fact that the private sector is unlikely to address issues of societal needs and the promotion of equity. Since the 1990s, however, expenditure cuts have been experienced in all areas of the budget, including military expenditure. Today, that decline is evident in many areas receiving financial support from government.

This paper discusses Zambia's efforts at focusing on competing needs amidst pressure. The paper explains that in order to provide for competing needs, Zambia's efforts have focused on promoting economic growth and achieving a stable macroeconomic environment. This requires a single-digit inflation rate, low and stable interest rates, and a stable exchange rate. In this regard, the Bank of Zambia (BoZ) has attempted to influence movements in these variables, as will be noted in later sections.

Improved economic growth constitutes the most significant variable of government intervention in the provision of competing needs. From the onset, it is acknowledged that little can be achieved to meet all competing needs unless policy measures are taken to achieve and sustain high economic growth rates over a long period of time.

Indeed, a growing economy that creates jobs and tax revenues for the state is a sustainable, powerful tool for addressing the population's competing needs such as better education, health, social safety nets as well as better security, both internally and externally. Over the past five years, total resources (that is, revenue and grants) available to the state for distribution to these competing needs have averaged at about 25.4%. This is far below the amount required to meet expenditure on competing needs, which has averaged at about 31.1% of gross domestic product (GDP). Clearly, choices have to be made on which needs to meet at any given time.

The paper begins with a discussion of the macroeconomic conditions in Zambia by reviewing selected macroeconomic indicators. This is followed by a review of the country's economic policy, a review of the national output and inflation and a discussion on interest rates and foreign exchange market developments. The final section highlights the challenges facing the Zambian government and provides some concluding remarks.

Economic policy

At independence in 1964, the Zambian economy was one of the fastest growing economies in the Southern African region. Government expenditure during this period expanded considerably to meet the developmental and social requirements of the economy. Conditions, however, began to deteriorate in the mid-1970s following the 1973 world market oil price increase and the sharp decline in world copper prices in 1974. In line with this, the country's terms of trade declined significantly and economic growth consequently stagnated. This marked the turning point in the government's capacity to deliver developmental and social services.

Unfortunately, the economy did not make the necessary adjustments in response to its declining economic fortunes. The economy continued to provide for competing needs, which included basic requirements such as food, water, clothing and shelter, as well as social requirements such as education, health and security, in the midst of pressure arising from decreased domestic resources available to the government. The government resorted to foreign financing in order to sustain the high levels of expenditure that were in place. As a result, foreign debt increased sharply.

Realising that economic growth was a necessary condition to increase resources and to provide for competing needs, the government embarked on far-reaching economic reforms in 1991. These included the removal of exchange and price controls, and the deregulation of interest rates. Some of the objectives of these reforms were to increase investment, modernise industry and to put the economy back on track.

To bring expenditure under control, subsidies were abolished while the government disengaged from marketing and active involvement in the primary production of agricultural commodities by allowing the private sector to take over these functions. Overall, the government refocused its role in the economy to that of facilitator through the provision of appropriate services and infrastructure such as marketing information, communication and improved access roads.

A key part of the reforms was the privatisation of state-owned enterprises. This began in 1992 following the establishment of the Zambia Privatisation Agency, which was established under the Privatisation Act of 1992 and mandated to privatise all state-owned enterprises. By October 2003, a total of

258 units had been privatised from a working portfolio of 282 state-owned enterprises. In addition, the Zambia Investment Centre was established as a one-stop investment window.

These efforts were all aimed at attracting both local and foreign investment – necessary ingredients for achieving sustained high economic growth which had suffered from stagnation since the mid-1970s.

With regard to macroeconomic policy reforms, the country adopted appropriate monetary and fiscal policies. The objective of the monetary policy was to reduce and contain levels of inflation and to maintain money supply at levels consistent with the desired economic growth. Similarly, the fiscal policy objective was aimed at lowering the budget deficit and ensuring that expenditures were focused on growth-supporting infrastructure, consistent with lowering annual inflation and achieving economic growth. Additionally, enhancing government revenue was also important to government's fiscal policy objectives.

The policy and structural reforms Zambia embarked on in the early 1990s are continuing, and government remains committed to the economic reform programme as part of a strategy for ensuring the realisation of sustained economic growth and providing for people's needs. These goals, objectives and policy actions are well articulated in the Poverty Reduction Strategy Paper (PRSP) for 2002–2006 and in the Transitional National Development Plan (TNDP) covering the period 2002–2005.

Under the economic reform programme, the performance of key macroeconomic indicators has broadly been favourable. Growth in real GDP has generally been positive, with inflation falling from three-digit to two-digit levels; the details of which are given in the ensuing sections.

National output

Although over the past decade Zambia has recorded positive economic growth, the performance has generally been sluggish. The average low economic growth has been attributed mainly to the country's heavy dependence on copper, which prices plummeted in the early 1970s and have stayed depressed. Recently, however, some price recovery has been observed. Compounding the unfavourable copper sector performance was the weak manufacturing sector, coupled with increased oil prices since the 1970s and neglect of agriculture over the years. This resulted in subdued growth in national output, loss of gainful employment and low per capita income. Manufacturing was dominated by inefficient and loss-making state-owned enterprises, while inappropriate agricultural policies with recurring drought characterised the agricultural sector. The low economic growth has constrained the country's ability to effectively mobilise adequate resources and thereby focus on delivering on acceptable competing needs.

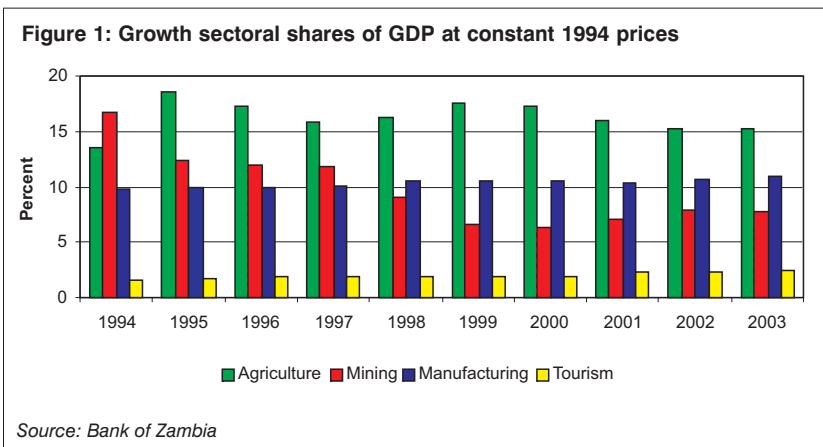
Structure

Between 1994 and 2003, the Zambian economy was largely driven by agriculture, manufacturing and mining, whose shares in real GDP averaged 16.3%, 10.3% and 10.0% respectively during this period. Trade, financial institutions and insurance, real estates, and transport and communications have been the key secondary sectors, with their shares averaging 17.2%, 8.5%, 7.5% and 6.0%, respectively. On the lower end of the shares are construction, energy and water, and tourism, which averaged 5.0%, 3.0% and 1.9%, respectively, during the review period.

In order to accelerate growth, the government, through the PRSP consultative process identified four sectors – namely: mining; agriculture; manufacturing; and tourism – to spearhead growth. Of the growth sectors mining, in particular the extraction and processing of copper, has dominated the country's economic activities. Despite a fall in its share of GDP to 7.9% in 2002 from 16.7% in 1994, the mining sector continues to be an important source of foreign exchange earnings and economic growth (see Figure 1).

Agriculture has exhibited much potential as the rightful successor to mining in leading the country's economic growth. This is reflected in its share of GDP, which has risen from 13.5% in 1994 to 15.2% in 2002. The agricultural sector share has generally been high despite adverse external shocks, such as the frequent occurrence of unfavourable weather during most growing seasons. Nevertheless, the government targets agricultural development as the engine of income expansion for the poor. In this regard, particular effort is directed at agricultural growth stimulation.

Manufacturing has also exhibited steady growth over the years, rising from 9.8% in 1994 to 10.9% in 2003, as shown in Figure 3. However, with trade liberalisation most of the privatised companies face stiff competition from



imported goods. Notwithstanding, the government intends to develop a sustainable export-led manufacturing sector, which will lead to an increase in job opportunities, sustainable export earnings and the growth of manufacturing, GDP and employment. Tourism (measured by the value added in restaurants, bars and hotels) has grown from 1.6% of GDP in 1994 to 2.4% of GDP in 2003. To maintain the growth momentum in tourism, the government will place the private sector in the lead in the development of tourism initiatives and in the implementation of investment plans, with assistance from government.

Performance

During 2003, national output increased for the fifth consecutive year, with real GDP growing by 4.3% compared to 3.0% (see Table 1). This was broadly in line with the target of 4.2%, but much higher than the 3.3% growth registered in 2002. This growth was mainly attributed to favourable developments in both the domestic and global economy. In the domestic market, a recovery in agriculture from the effects of the 2001/2002 season drought coupled with government's support in the area of input supply to the small but viable small-scale farmers through the Fertiliser Support Programme, largely contributed to the positive growth. Other key sectors that contributed to the growth were manufacturing, construction as well as wholesale and retail trade.

In addition, the recovery of the world economy pushed up prices of non-fuel commodities, which assisted in the growth of non-traditional and metal exports. The growth in metal prices led to an expansion in the mining and quarrying sector, as well as to an increase in the country's export earnings.

Table 1: Developments in real GDP, 1999–2003 (in constant 1994 prices) [%]

	1998	1999	2000	2001	2002	2003*
Growth in real GDP	(1.9)	2.2	3.6	4.9	3.0	4.3
Agriculture, forestry and fisheries	1.2	10.1	1.6	(2.6)	(1.7)	5.0
Mining and quarrying	25.1	24.8	0.1	14.0	16.4	3.3
Manufacturing	1.8	2.8	3.6	4.2	5.7	6.3
Energy, gas and water	0.6	2.5	1.2	12.6	(5.2)	0.6
Construction	(9.1)	3.2	6.5	11.5	17.4	13.9
Wholesale and retail trade	3.5	4.4	2.3	5.4	5.0	4.9
Restaurants, bars and hotels	3.8	(6.2)	12.3	24.4	4.9	5.9
Transport, storage and communications	8.5	5.7	2.4	2.8	1.8	5.1
Financial intermediaries and insurance	0.4	2.5	(0.6)	0.1	3.5	3.5
Real estate and business services	12.7	13.8	17.0	3.5	4.4	4.0
Community, social and personal services	(2.3)	8.4	(0.5)	5.8	1.6	2.4
Taxes on products	(5.4)	(4.5)	5.2	7.0	(6.8)	(3.0)
FISIM	0.4	2.5	2.5	2.5	2.5	2.5

Source: Central Statistical Office, and Ministry of Finance and National Planning

*Preliminary data

Inflation

In recognition of the fact that inflation erodes the purchasing power of expenditure, the government aimed at reducing its fiscal deficit as a proportion of GDP through, among other initiatives, the privatisation of nearly all state-owned enterprises – formerly a major drain on government financial resources through subsidies. Furthermore, appropriate monetary policy complemented the fiscal policy efforts in reducing liquidity pressures in the banking system, thereby subduing inflationary pressures. Over the past 10 years, inflation developments have generally been favourable, declining to the lower end of two-digit figures from the three-digit figures in the early 1990s.

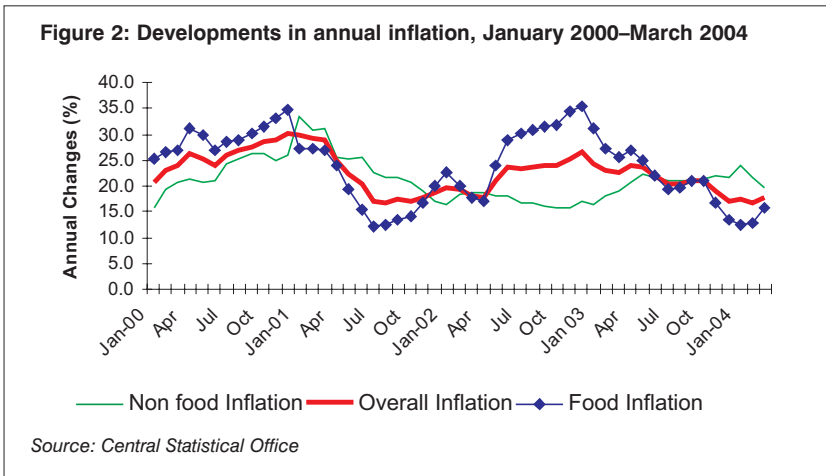
However, despite the drop in overall inflation over the past decade, inflation has tended to stick around the lower end of two-digits and, consequently, the achievement of low and single-digit inflation has remained elusive. Continued fiscal deficits, prolonged dry spells and unfavourable movements in the exchange rate have been mainly responsible for the stickiness of inflation. The BoZ has continued to focus its activities towards the achievement of single-digit inflation over the medium term. This is because the achievement of low and stable inflation is essential for investment confidence and economic growth, and therefore for the generation of government revenues with which to finance many competing needs, including the provision of security to the Zambian population.

Composition of inflation

Developments in overall inflation have been largely influenced by both food and non-food components, with the former being a key factor. In Zambia, food accounts for 57% of the consumer price index (CPI). The rest is accounted for by non-food factors, which include mainly movements in energy prices such as electricity and fuel. Fiscal operations as well as the pass-through effects of the exchange rate are also important non-food inflation determinants. This is why it is important that fiscal and monetary policy actions are specifically directed at containing the non-food component of inflation.

Developments in inflation

After falling to 20.1% in December 1999, overall inflation rose to 30.1% in December 2000, mainly on account of the higher than programmed increase in money supply (67.5%), which, in turn, was largely attributed to increased government borrowing. Also contributing to the increase in inflation were the pass-through effects of the depreciation in the exchange rate (58.3%), the increase in petroleum prices (100%) and electricity tariffs (25%). In December 2001, overall inflation declined significantly to 18.7%. This favourable



development was accounted for by the slowdown in money supply and the appreciation of the kwacha, complemented by the stability in the price of petroleum products and electricity tariffs. The year 2002 closed with overall inflation at 26.7%. The increase in inflation was largely on account of the increase in food inflation to 35.5% in December 2002 from 20.2% in the same month in 2001 (see Figure 2).

Adverse weather conditions during the 2001/2002 agricultural season – which resulted in food shortfalls, in particular the country’s staple food crop, maize – led to increased food prices.

In 2003, consumer price developments were favourable. The annual overall inflation rate declined to 17.2% in December 2003 and was broadly in line with the December 2003 projection of 17.1%. Consumer inflation was mainly driven by food inflation, which dampened inflationary pressures for most of the year following favourable weather conditions and sufficient input distribution in the 2002/2003 agricultural season, which led to adequate food supply in 2003. Annual food inflation fell to 13.5% compared with a rise of 35.5% in December 2002. However, non-food inflation rose to 21.7% at end-2003 from 17.2% recorded in the previous year.

Rising non-food prices were attributed to several factors, including higher than programmed growth in money supply due to the easing of monetary policy at end-October 2003, which was aimed at facilitating a flow of liquidity to the productive sectors of the economy, particularly agriculture. In addition, fuel prices increased on account of the rise in the price of petroleum products on the world market. Furthermore, the appreciation of the South African rand made goods and services imported from South Africa more expensive in kwacha terms.

The overall inflation rate increased to 17.4% in January 2004 from 17.2% in

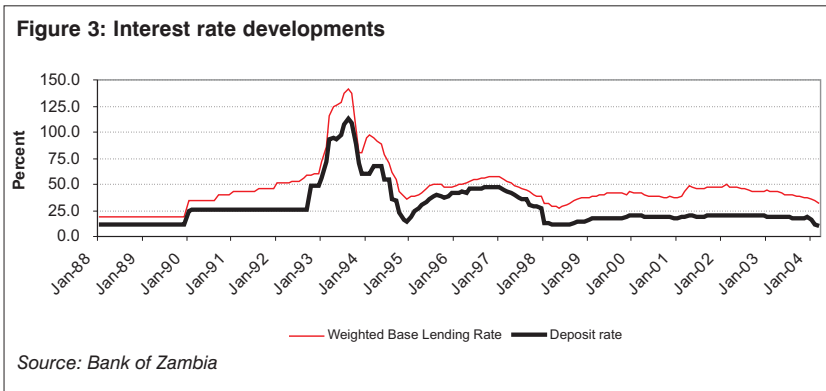
December 2003. This fell to 16.8% in February 2004, before edging upwards to 17.6% in March 2003. Food inflation declined to 12.5% in January 2004 from 13.5% in December 2003. Food inflation increased to 12.9% in February 2004, before rising further to 15.9% in March 2004. The non-food inflation rate increased to 23.8% in January 2004 from 21.7% the previous month. In February 2004, non-food inflation declined to 21.6% before declining further to 19.6% in March 2004.

Interest rates

During the 1970s and 1980s, Zambia pursued a policy of fixing interest rates administratively for long periods and at relatively low levels, with the perceived purpose of promoting economic growth. However, these administrative actions introduced economic distortions into the financial structure of the economy including the following:

- Economic growth was hindered arising from the inefficiency in the allocation of resources (with credit controls and distorted price indicators). These controls contributed to both low levels of domestically generated savings and investment, as well as reducing the economy's growth rates.
- The financial system remained generally under-developed with inefficient lending patterns that failed to achieve their distributional goals. With interest rates set at low levels, financial repression curtailed domestic resource mobilisation, thus making the economy dependent on foreign savings, as reflected in the huge foreign debt.
- The economic distortions provided an incentive for fiscal indiscipline as the government obtained almost zero-interest denominated resources to finance its deficit. Among the state-owned banks, poor lending decisions (often politically influenced) and low repayment rates ultimately led to large budgetary bailouts.
- In the face of high inflation rates and fixed nominal interest rates, real interest rates remained negative for the larger part of the period, leading to low domestic savings.

A growing awareness of these economic costs led to financial 'liberalisation' as the dominant policy paradigm. Therefore, in the 1990s, many countries allowed market forces to play a greater role in their economies. In the financial sector, this greater role meant liberalising financial prices, including interest rates and exchange rates, so that the market sets them, and developing financial markets so that credit could be allocated more efficiently.



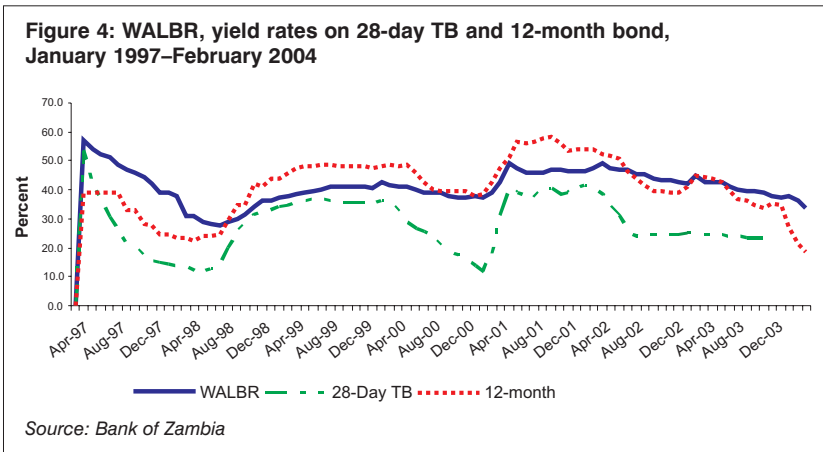
Indeed, Zambia embraced the financial sector liberalisation policy prescription and embarked on a fairly ambitious reform programme. This programme entailed a variety of measures including: the liberalisation of interest rates; establishing the freedom and procedures for entry into and orderly exit from the financial sector; the reduction of commercial banks' reserves and liquidity requirements; the elimination of credit allocation directives; the elimination of preferential credit at concessionary interest rates; the liberalisation of the exchange rate; and the removal of controls on the current and capital accounts of the balance of payments. These policy actions were aimed at allowing the market forces of demand and supply to effectively allocate resources to the most productive sectors, and hence contribute to higher private sector credit for investment, to achieve high economic growth over a long period of time.

Following the liberalisation of interest rates in October 1993, nominal interest rates increased and the spread between the weighted lending base rate and the deposit rate at commercial banks widened. By the second half of the 1990s, nominal interest rates declined, although the banks' average lending rate remained significant while the deposit rate was set too low (see Figure 3).

Developments in interest rates

In the recent past, an anchor relationship has emerged between the commercial banks' lending rates and yield rates on government securities. Owing to the fall in inflation over the past years, commercial banks appear to have switched their anchor of base lending interest rates from inflation to Treasury bill yield rates, and more recently to government bond yield rates.

In the light of this, there is a fairly close behavioural relationship between yield rates on government bonds and commercial banks' lending base rates. The movement in the lending base rate closely follows those of yield rates on government securities (see Figure 4).



As Figure 4 shows, yield rates on government securities have trended downwards. Consistent with developments in government securities' yield rates, commercial banks' interest rates have also edged downwards. The weighted average lending base rate and the average lending rate decreased to 37.7% and 45.3% at end-December 2003 from 42.5% and 50.0% at end-December 2002, respectively. The average savings rate for amounts above K100,000 and the 30-day rate for deposits above K20 million fell to 7.6% and 17.9% from 8.1% and 19.5% over the same period, respectively.

By end-March 2004, the weighted average lending base rate and the average lending rate had declined to 31.8% and 39.1%. The average savings rate for amounts above K100,000 and the 30-day rate for deposits above K20 million fell to 6.8% and 9.9%, respectively. The downward trend in interest rates was mainly due to loose liquidity conditions in the system. Further, the BoZ actions such as the conversion of foreign exchange statutory reserves held in kwacha into United States (US) dollars and the reduction of the statutory reserves ratio on both foreign currency and kwacha deposits contributed to lowering the cost of funds for commercial banks in particular, and interest rates in general, as elaborated below.

Efforts aimed at lowering interest rates

The key players in the determination of interest rates – namely, the government, the BoZ, commercial banks and the public – must play their meaningful and responsible roles if efforts in lowering lending interest rates are to bear fruit. In recognition of the importance of credit towards contributing to economic growth and macroeconomic stability, the BoZ reduced the legal reserve requirement to 14% in October from 17.5%, to contribute to the lowering of lending interest rates. By taking this action, the BoZ expected more

loanable funds to be available in the banking system; a condition that contributed to the lowering of lending rates. In addition, the BoZ completed the conversion of statutory reserves on foreign currency deposits to US dollars to release kwacha into the financial system. This was aimed at providing loanable funds to commercial banks, thereby contributing to lowering interest rates. Following the completion of the conversion, most banks reduced their base rates, though their rates are still very high.

Foreign exchange market

Features

In 1992, the foreign exchange market was liberalised bringing into force a floating exchange rate regime, which allowed for the freeing up of capital and current accounts and the elimination of restrictions on both accounts. The introduction of foreign-currency denominated accounts in 1995 and the establishment of the bureaux de change followed these reforms.

In an attempt to make the foreign exchange market more efficient, the BoZ, in conjunction with other major stakeholders, established in July 2003 a broad-based foreign exchange inter-bank system as the main vehicle to drive the foreign exchange market in Zambia. Prior to this date, the BoZ was the primary dealer to which major foreign exchange suppliers sold their foreign exchange. In turn, the BoZ auctioned foreign exchange to commercial banks. The broad-based foreign exchange inter-bank system was introduced to address the shortcomings that characterised the previous trading system, particularly the feature of multiple exchange rates and the extreme information asymmetry, which tended to undermine the efficiency of the market. The advantage of the broad-based inter-bank system is that foreign exchange trading became more transparent, as players now have a more even distribution of information about foreign exchange availability. This even distribution ensures that certain profitability, which was exploited by the skewed distribution of information, has virtually been erased.

With the introduction of the inter-bank system, commercial banks have assumed the role of primary dealer, buying foreign exchange and selling to buyers in the market, which includes the BoZ. To support the system, the wholesale source of foreign exchange moved from the BoZ to the commercial banks. These initiatives have all been aimed at enhancing the role of the market in the determination of the exchange rate, as well as to contribute to the stability of the kwacha, bearing in mind all market fundamentals.

Exchange rate developments

Following the increased confidence related to the new trading system and the

broad-based weakness of the US dollar in international markets in the second half of 2003, the kwacha was fairly resilient against the US dollar, depreciating by 7.5% to end the period at K4,661.59, compared with a depreciation of 13.2% in 2002. However, the kwacha remained weak against other major currencies. The K/£ exchange rate depreciated by 16.5% to K8,024.08 compared with the previous year's depreciation of 24.1%. Furthermore, the K/Euro and the K/ZAR exchange rates weakened by 25.0% and 35.4% to K5,648.59 and K680.60, compared with the previous year's depreciation rates of 33.8% and 55.6%, respectively.

Challenges facing the government

Competing needs

In spite of resource constraints, a broad range of challenges, or objectives – including social, economic, civil and military objectives – have to be met by the government. Their expenditure implications have to be accommodated within a sound macroeconomic and fiscal framework consistent with other competing needs. In Zambia, the list of competing needs or spending pressures is endless and may include the following: organisation of elections; public sector training; improvement in roads and other transport infrastructure; rural development and agricultural support; electrification promotion; water supply and sanitation; tourism promotion; redressing education infrastructure; education and training; rehabilitation of prison infrastructure; expansion of judicial capacity; extension of legal aid; development programmes focused on women and children; special protection measures for children; public welfare assistance schemes; social safety nets; and defence and security.

Spending pressures may also include water supply, clinic building and district health services, medical care and hospital rehabilitation. Each of these programmes represents a pressing claim which government should try to accommodate. However, neither the economy nor the public sector has the capacity or financial resources to meet all these claims immediately. As the government is confronted with many pressing needs, it cannot allocate substantially increased resources to all priority services.

Through the PRSP, the government recognises that it is only possible to focus on competing needs through growth stimulation, which in turn may only be achieved through a stable macroeconomic environment – which is an attractive environment for investment stimulation. Due to economic stagnation, Zambians are not able to accumulate enough savings on their own to fund desirable investment projects. Consequently, if Zambia were to depend on its own resources alone, it would be practically impossible to focus even on its basic needs. In this regard, the government makes every effort to attract credible foreign investors so as to augment Zambia's own savings. Owing to the

centrality of investment, institutions involved in facilitating investment would be accorded appropriate resources from the resource envelope to facilitate their work.

Limited resource envelope

Another challenge that the government faces is the limited resource envelope. The resource envelope is the level of resources available for public expenditure over a given period of time. This amount is always limited, and therefore choices have to be made on the areas of the economy to be supported. The resource envelope for Zambia is derived from the domestic revenues collected by the revenue authority and other public sector agencies through tax (e.g. customs and income taxes) and non-tax sources (e.g. fees and fines), respectively. The growth of the economy expands the resource envelope, as it increases incomes in the economy and, ultimately, tax.

During the current Medium-Term Expenditure Framework¹ for 2004–2006, the amount of resources that can be raised domestically has been set at 17.6% of GDP for tax sources and 0.5% of GDP for non-tax sources. The government is committed to increasing the proportion of domestically generated resources to finance competing needs, but it also recognises the current difficulties facing the country with regard to generating domestic revenue.

In addition to domestic revenue, donor inflows are expected to support public expenditure programmes to augment domestic resources. Donor inflows come in the form of project assistance and programme aid. Project assistance is donor inflow that is directly related to a particular project. Programme aid refers to assistance that comes in the form of balance of payments and general budget support and is not tied to any particular public expenditure programme or project.

In view of the liberal environment in the Zambian economy, the government will encourage the full participation of the private sector, non-governmental organisations, community-based organisations and communities themselves in financing the competing needs of the Zambian economy.

Resource allocation

Resource allocation is probably the most serious challenge in the Zambian economy. The PRSP indicates broad areas where scarce national resources are to be channelled to meet the goals and objectives agreed upon through the consultative PRSP preparation process. However, as indicated earlier, the competing needs are too numerous for an economy under pressure.

In allocating scarce resources, the government recognises that basic education and health are powerful tools on which substantial resources should be focused. There is also a need to provide social safety nets to minimise the

impact of poverty. In this regard, the main challenge is to create and expand poor people's opportunities to earn a decent income through the facilitation of credit schemes, the provision of marketing and technological information related to improved productivity and product marketing, the provision of infrastructure such as industrial estates, etc. All these activities require financing from the limited resources.

The activities listed above are by no means the only ones. There are numerous competing needs to focus on. Further, in recognition of the fact that resources are limited and that there are several competing needs to be financed, it is important to realise that the volume of the resource envelope targeted towards a particular activity need not necessarily define the level of importance attached to that activity. This is because some priority activities may require relatively small expenditures during a given period before full-fledged support commences.

Regarding meeting the expenditure needs of defence and security, this has generally been increasing in Africa. This is due primarily to the involvement of many countries in the region in the resolution of conflict, either directly or indirectly. While African defence and security expenditure may represent a small share of the world total, it constitutes a heavy economic burden in many African countries where provision of adequate social needs is also competing for the same scarce resources at the disposal of governments.

Fiscal developments

During the period 1999–2003, total revenue and grants averaged 25.4% of GDP. Of the total revenue and grants, domestic revenue was 18.4% of GDP while grants were 7.0% of GDP. Total domestic revenue comprised tax revenue of 18.0% of GDP and non-tax revenue of 0.4% of GDP. This is shown in Table 2.

On the expenditure side, total spending averaged 31.1% of GDP during the period 1999–2003. Most of the spending was on recurrent activities at about 18.5% of GDP, while developmental spending was about 11.2% of GDP. In addition, funds averaging 1.4% of GDP have been spent on net lending activities during the period under review. Consequently, the overall budget recorded an average deficit of 6.4% of GDP. Indeed, it is clear from the foregoing that spending pressures are many, but that resources are limited.

Conclusion

During the past 10 years, Zambia's macroeconomic conditions have generally been on an improved and stable path. This has been reflected in the positive developments in most of the macroeconomic indicators reviewed in this paper. The recovery in real GDP growth, declining inflation rates, a downward trend in lending interest rates and stability in the exchange rate all go to indicate an

Table 2: Fiscal development for Zambia, 1999–2003 (in % of GDP)

	1999	2000	2001	2002	2003
Revenue and grants	25.7	25.1	24.8	26.3	25.1
Domestic revenue	17.7	19.4	19.1	18.0	18.1
Of which:					
Tax revenue	17.2	19.2	18.6	17.6	17.4
Non-tax revenue	0.5	0.2	0.5	0.4	0.7
Grants	8.0	5.7	5.7	8.3	7.0
Expenditure and net lending	29.4	31.0	32.1	31.9	31.2
Current expenditure	16.8	16.9	19.6	19.5	19.7
Capital expenditure	10.6	10.0	11.8	11.9	11.5
Net lending	2.0	4.1	0.6	0.5	0.0
Change in balances	(0.3)	(1.1)	(0.8)	(0.7)	(0.6)
Overall balance (cash)	(3.7)	(7.0)	(8.0)	(6.4)	(6.6)
Of which:					
Domestic balance (Cash)	(1.3)	(3.3)	(4.7)	(4.1)	(4.1)

Source: Ministry of Finance and National Planning

improvement in the macroeconomic environment. The government will continue to pursue market and structural reforms with the view of consolidating on the gains so far attained. This will facilitate a focus on competing needs, which may require more of the national resources.

Furthermore, in deciding its public spending priorities, government takes account of the particular economic challenges facing Zambia, looking towards faster growth. Through the recently introduced activity-based budgeting, the government will deliver budgets that express the priorities of the nation. The government considers activity-based budgeting as a rational mechanism for linking public expenditure with clear policy objectives and goals.

As Mpuku and Zyuulu² noted, there is no one development strategy that can be universally recommended and applied in developing countries to achieve the desired social and economic goals.

Each country must understand its own political, economic, social and cultural history as well as the aspirations of its people in developing a social-economic strategy for the country. Indeed, these statements are true in relation to the allocation of scarce resources among various competing needs. Stern³ comments that "there are two pillars that form the basis of a sound strategy of development. They are the pillars of creating a good climate for investment and productivity growth, and empowering people including the poor to participate in that growth". Ultimately, a growing economy enables government to better finance its defence and security requirements, among other competing needs.

This is the essence of focusing on competing needs through the promotion of economic growth and macroeconomic stability.

Notes

- 1 Ministry of Finance and National Planning, October 2003.
- 2 H C Mpuku & I Zyuulu, *Contemporary issues in social-economic reform in Zambia*, Ashgate Publishing Company, Hants, England, 1997, pp 139.
- 3 N Stern, A strategy for development, an address to the People's University of China, Beijing, China, June 2001, pp 1.