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**Zambia:** Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding

June 19, 2006

The following item is a Letter of Intent of the government of Zambia, which describes the policies that Zambia intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Zambia, is being made available on the IMF website by agreement with the member as a service to users of the [IMF](#) website.

June 19, 2006

Mr. Rodrigo de Rato  
Managing Director  
International Monetary Fund  
Washington, D.C.

Dear Mr. de Rato

The attached Memorandum of Economic and Financial Policies (MEFP) reviews the progress made in implementing the Government of Zambia's financial and economic program supported by the IMF under the Poverty Reduction and Growth Facility (PRGF). The memorandum reviews developments since the completion of the third review of the program on January 11, 2006 and sets out the policies that the Government of Zambia will pursue for the remainder of the year. Our strategy remains focused on achieving high rates of economic growth and reducing poverty through the continued pursuit of prudent fiscal and monetary policies and structural reforms to strengthen public expenditure management and accountability, improve the environment for private sector development, and strengthen governance.

The Government of Zambia requests the completion of the fourth review and seventh disbursement under the PRGF arrangement in an amount equivalent to SDR 5.5024 million. The Government also requests the IMF Executive Board to approve a modification of the quantitative program targets for June 2006, mainly to reflect revisions to the macroeconomic framework arising from additional spending on poverty-reducing programs made possible by the IMF's contribution to the Multilateral Debt Relief Initiative (MDRI) and the payment of domestic arrears in late 2005 that affected Government's net domestic financing in 2006. The proposed modifications also include a greater targeted buildup of international reserves than previously planned. For 2006 as a whole, the program will maintain the prudent fiscal stance and monetary restraint envisaged in the MEFP for the third review. To this end, the Government will take the necessary expenditure measures required to meet the end-year ceiling on net domestic financing. Efforts will also be made to strengthen collection of tax and nontax revenue, the VAT deferment on imported noncapital goods will be repealed by end-July 2006, and Statutory Instrument 1 of 2006, which extended reductions on selected taxes on petroleum products, will expire on June 30, 2006. Also, the Government has established a committee to review development agreements with the mining companies, including raising the royalty on minerals, and will undertake and complete before end-December 2006 a comprehensive assessment of tax policy and tax administration as part of a broad reform of Zambia's tax system.

In keeping with our objective of reorienting spending toward poverty-reducing programs, the Government of Zambia's budgetary expenditure on PRPs in 2006 (excluding spending financed by MDRI assistance) will be ½ percentage point of GDP greater than in 2005. Amongst other things, this will allow the recruitment of an additional 4,578 teachers and 800 medical personnel. The resources made available by the MDRI will be used to increase spending on priority poverty-reducing programs under the forthcoming National Development Plan 2006-2010. In 2006, the equivalent of the savings on debt service that would have been due to the IMF will be used to increase spending on agricultural projects.

The Government of Zambia believes that the policies set forth in the attached MEFP are adequate to achieve the objectives of its program, but it will take any further measures that may become appropriate for this purpose. Zambia will consult with the IMF on the adoption of these measures and in advance of revisions to policies contained in the MEFP, in accordance with the Fund's policies on such consultation.

The Government of Zambia authorizes the IMF to make the staff report for the fourth review under the PRGF arrangement and this letter and attached memoranda available to the public, including through the placement of these documents on the IMF website, subject to the removal of market-sensitive information, following the IMF Executive Board conclusion of the review.

Yours sincerely,

/s/

Ng'andu P. Magande, MP  
Minister of Finance and National Planning

## Memorandum of Economic and Financial Policies

### I. Review of Recent Developments and Performance Under the PRGF-Supported Program

1. **The Zambian economy continued to perform well in 2005 and early 2006.** Real GDP grew by about 5 percent in 2005, as a strong expansion in construction—driven by a robust demand for housing and large-scale investment in the copper sector—and a marked pick up in mining production outweighed a number of setbacks, including a drought in some regions of the country and fuel shortages caused by an extended shutdown of the country's oil refinery (Indeni). With a healthy recovery in agriculture underway, real GDP growth is set to increase to about 6 percent in 2006. The kwacha's appreciation created additional downward momentum for inflation, which fell to 15.9 percent in December 2005 and to 9.4 percent in April 2006—marking the first time in about 30 years that Zambia has achieved single-digit inflation. The prospects of a bumper crop in maize has helped to ease pressure on food prices in recent months. Cash crop production for the export market and the tourism sector have continued to grow at a strong pace in the first quarter of 2006. However, the sharp appreciation of the kwacha in late 2005 has posed a major challenge to the international competitiveness of these sectors.

2. **Poverty is still widespread in Zambia with 68 percent of the population falling below the poverty line in 2004.** In rural areas, the incidence of poverty is even more severe. Nevertheless, the rising trend in poverty rates that prevailed during the 1990s has begun to be reversed. As part of the expansion of poverty-reducing programs (PRPs) made possible through debt relief, the Government eliminated user fees for health clinics in rural areas beginning in April 2006.

3. **Fiscal performance was broadly in line with budget projections in 2005.** The overall fiscal deficit, including grants, was nearly equal to the budget target. Current expenditures were trimmed, beyond the savings on interest costs, to offset lower nontax revenue and the reductions in fuel import taxes and duties granted during the fourth quarter of the year to ease the burden on consumers from the Indeni shutdown. Relative to GDP, the overall fiscal deficit, including grants, was 2.6 percent, compared with the modified program target of 2.7 percent. Net domestic financing of government in 2005 was somewhat below the target, as some of the payments to road contractors did not clear government accounts until January 2006. Tax revenue amounted to 17.0 percent of GDP in 2005, compared with the budget projection of 17.7 percent, suggesting that a good portion of the economy's growth escaped the tax net. The weak revenue performance continued in the first quarter of 2006. In addition to an extension of the reduction in import and excise duties on petroleum products, the appreciation of the kwacha significantly lowered the kwacha value of revenues from VAT on imports and customs duties, as well as VAT on domestic goods and services valued in U.S. dollars (such as electricity purchases by the mining companies).

4. **The Bank of Zambia (BoZ) maintained the growth of reserve money—the BoZ’s operating target—broadly in line with the 2005 monetary program through most of the year.** On an annual basis, reserve money increased by 16 percent on average compared to 23 percent in 2004. Broad money (M3) remained flat during 2005, largely reflecting the valuation effect of the exchange rate appreciation on the U.S. dollar deposits in commercial banks.<sup>1</sup> The yield on government securities has come down sharply in recent months, driven largely by the decline in inflation and strong demand, particularly by nonbank institutions (pension funds) and foreign portfolio investors that have been active in the market since the third quarter of 2005. The average yield on Treasury bills declined from nearly 17 percent in late December 2005 to just under 8 percent in early May, accompanied by a decline in commercial banks’ average lending rate from 27.6 percent to 23.7 percent.

5. **The kwacha appreciated by 26 percent against the U.S. dollar in 2005 and has continued to strengthen at a more moderate pace in 2006.** The appreciation has been associated with increased market confidence in the economy stemming from the greatly improved prospects of the copper sector, the cancellation of the bulk of Zambia’s external debt, and expected continued commitment to prudent fiscal and monetary policies. The favorable market sentiment has been reflected in the substantial inflows of foreign investment in government securities. The real appreciation of the kwacha poses a challenge for nontraditional exports, which will have to step up improvements in productivity to maintain their competitiveness in international markets, and for government to implement the necessary structural reforms to lower the cost of doing business.

6. **Zambia’s external position has strengthened substantially in 2005 and early 2006.** In addition to a reduction in the current account deficit of the balance of payments relative to GDP, led by favorable developments in the terms of trade and rapidly rising export earnings, Zambia has benefited from extensive debt relief following the attainment of the completion point under the HIPC Initiative in April 2005, debt cancellation by Paris Club bilateral creditors in May 2005, and the cancellation of debt to the IMF under the Multilateral Debt Relief Initiative (MDRI) in early 2006.<sup>2</sup> Record high world prices of copper—Zambia’s principal export—together with strong growth in copper export volumes arising from a series of major investments in the sector following privatization, have driven export earnings sharply higher. Nonmetal exports also experienced strong growth in 2005, which continued through the first quarter of 2006. While imports also grew rapidly during this period—reflecting the economy’s robust growth, the strength of the kwacha, and high world petroleum prices—the current account deficit, including grants, narrowed from 5.5 percent of GDP in 2004 to 3.8 percent in 2005. Moreover, rising capital inflows, including about US\$120 million of portfolio inflows in 2005—a new phenomenon in Zambia, which

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<sup>1</sup> Evaluated at the constant program exchange rate, M3 grew by 13 percent in 2005.

<sup>2</sup> The Boards of the World Bank and the African Development Bank approved the MDRI for their respective institutions in March 2006. Implementation is expected to begin in July 2006.

continued into 2006—more than covered the current account deficit in 2005, allowing for an increase in the BoZ's international reserves by US\$135 million to US\$357 million by the end of the year. While still low, reserves grew from 1.2 months of imports in 2004 to 1.6 months as of end-2005.

7. **All quantitative and structural performance criteria and benchmarks under the PRGF-supported program were met through December 2005. However, there have been some difficulties and delays in meeting the benchmarks in early 2006 (Tables 1 and 2).** The March 2006 benchmark ceiling on net domestic financing was missed by K 256 billion. This was mainly due to end-2005 authorized expenditure, including the payment of K 120 billion in arrears to road contractors, some of which was executed in early 2006, and the shortfall in tax collections. On the structural side, the continuous performance criterion on restricting government spending to budgeted items and legal liabilities was observed through March, as were the benchmarks regarding the validation of external debt data, governance and transparency in budget execution, and the issuance of rules and procedures to implement and enforce a new cash management framework. Other measures (benchmarks for March 2006) related to the Public Expenditure Management and Financial Accountability (PEMFA) reform were not implemented as scheduled. New summary tables on budget execution were issued in May 2006. The layman's draft of the Financial Regulations was submitted in March to the Ministry of Justice and is expected to be finalized by end-June 2006. The corresponding final manuals will be issued to heads of accounting units by end-December 2006. Under private sector development, the electricity company (ZESCO) has not completed preparing the required information for the assessment of its performance under the commercialization process (end-April benchmark). In particular, the draft financial statement for the fiscal year that ended March 31, 2006 will only be available by end-July 2006.

## II. Medium-Term Objectives and the PRGF-Supported Program

8. **In line with the forthcoming Fifth National Development Plan (FNDP), scheduled to be launched in July 2006, and the medium-term macroeconomic framework as set out in the December 2005 MEFP for the third review under the PRGF arrangement, the Government aims to implement a macroeconomic policy framework and an agenda of structural reforms that will support strong economic growth and a substantial reduction in poverty.** Under this current scenario for 2006–2008, the Government aims to:

- Achieve real GDP growth of at least 6 percent a year;
- Bring down end-year inflation to no more than 10 percent in 2006 and 5 percent in 2007 and 2008;
- Limit domestic borrowing to 1.8 percent of GDP in 2006, 0.7 percent of GDP in 2007, and 0.5 percent of GDP in 2008 to strengthen the domestic debt position and limit the crowding out of credit to the private sector;

- Increase the coverage of official gross international reserves to at least 1.7 months of imports in 2006, 2.0 months in 2007, and 2.4 months in 2008;
- Remain current with foreign debt service; and
- Increase spending under the budget on Poverty Reducing Programs (PRPs) by at least ½ percentage point of GDP a year.

9. **The reduction in the Government's domestic borrowing over the medium term is the anchor to Zambia's macroeconomic stabilization effort.** That reduction will be achieved by gradually raising government revenues by introducing appropriate tax measures—notably by improving tax administration and widening the tax base by further bringing in the informal sector—while exercising strict control on government expenditures. In addition, the Government will explore the scope for revising the taxation of mining and renegotiating development agreements.. Increases in donor assistance, including in the form of budget support, would provide room for a greater expansion of government spending. A strengthening of budget execution will not only be critical to enable donors to increase budget support, but also to improve public sector service delivery and investment. The Government has a large outstanding stock of arrears to the Public Service Pension Fund (PSPF). Over 2006-2008, about 1.5 percent of GDP will be allocated to reducing the stock of pension arrears.

10. **The structural reform agenda is mainly aimed at increasing productivity.** Implementation of the Financial Sector Development Plan (FSDP) and the Private Sector Development (PSD) action plan will be instrumental in addressing the main credit and administrative constraints to private sector development in Zambia. The structural reform agenda will also include measures to improve the quality, efficiency, cost effectiveness, and delivery of public services. Increasing productivity in the public sector will rely on continued progress with ongoing reforms to strengthen PEMFA, public service management, including rightsizing of the civil service, and decentralization.

### III. Policies for the Remainder of 2006

11. **Economic and financial policies for the remainder of 2006 will remain largely in line with those outlined in the December 2005 MEFP.** However, in light of recent developments, notably the strong appreciation of the kwacha, the late payment of domestic arrears to road contractors, and the cancellation of obligations to the IMF under the MDRI, some modifications to the program are warranted, particularly in setting the quantitative performance criteria and benchmarks for the second half of the year.

#### A. Fiscal Policy

12. **Fiscal policy is aimed at containing the Government's net domestic financing over the remainder of the year—in order to observe the annual target of 1.8 percent of GDP—while increasing spending by the Government on PRPs by 6.7 percent of GDP,** in line with the original program target plus additional MDRI resources available in 2006. To

overcome the revenue shortfall during the first quarter of the year, efforts will be made to strengthen tax compliance, especially with regard to VAT, and the collection of tax arrears. Administration of the fertilizer program will be strengthened to overcome slippages in non-tax revenues. Statutory Instrument number 64 of 2005 as extended by Statutory Instrument number 1 of 2006 on petroleum products will lapse on June 30, 2006 and the deferment of VAT on imports of noncapital goods will be repealed by end-July. Nonpriority expenditures will be reduced by K 203 billion by decreasing expenditures on ordinary RDCs, domestically financed non-PRP capital expenditures and other emoluments. Expenditures that will be cut include purchases of office equipment and motor vehicles and commutation of leave days. At the same time, the Government will meet its commitments in a timely manner to further the progress achieved in paying down domestic arrears. In particular, it will stay current on its contributions to the Public Sector Pension Fund (PSPF) and NAPSA. Included in the PRPs budgeted for 2006, funds have been allocated for the recruitment of an additional 4,578 teachers and 800 medical personnel.

13. In view of the weakening revenue performance, the Government will expedite the planned review of the tax system with a view to broadening the tax base and enhancing its efficiency. To this end, the Government will undertake and complete by end-December 2006 a diagnostic review of tax policy and tax administration (end-December 2006 performance criterion) as part of the broad reform of Zambia's tax system. The recommendations of this review shall be implemented starting with the 2007 budget. The Government also has established a committee to review development agreements with the mining companies, including raising the royalty rate on minerals.

14. **The resources made available by the Multilateral Debt Relief Initiative (MDRI) will be utilized by Government to support programs to speed up achievement of the Millennium Development Goals (MDGs).** The resources will be used over time in line with annual debt-service savings. The transfer of debt relief resources to the government has been effected through a decrease in Bank of Zambia claims on the government, reflecting the onlending arrangement between the Bank of Zambia and the government of IMF resources disbursed to Zambia. The residual balance in the GRZ/PRGF deposit account at the Bank of Zambia from past onlending of IMF disbursements has been transferred to a special government deposit account. This balance, which became freely available for government's use as a result of the IMF's MDRI relief to Zambia, stood at K 213.6 billion (about US\$ 61 million) on January 6, 2006. Withdrawals from this account will be used to finance additional expenditures on priority poverty-reducing programs in 2006 and 2007. In 2006, the withdrawals will amount to US\$18 million in debt service savings for the year, and will be spent on agricultural projects, namely irrigation development and livestock disease control. From 2008 onward, when the funds in this account will have been exhausted, the Government will annually set aside resources equivalent to the MDRI debt-service savings in that year for additional expenditure on poverty-reducing programs.

## **B. Monetary and Exchange Rate Policies**

15. **The Bank of Zambia will maintain an appropriately firm monetary stance in 2006 to keep inflation on a downward path and curb further expectations of high inflation.** Reserve money growth will be limited to 10.3 percent. Accordingly, broad money

and credit to the private sector are projected to grow by 14.6 percent and 15.4 percent, respectively.

16. **The Government remains committed to a flexible exchange rate regime.** The BoZ will intervene as appropriate in the foreign exchange market to smoothen temporary fluctuations in the exchange rate and to build up international reserves without compromising the inflation objectives.

17. **The Bank of Zambia's scope to carry out sterilized intervention has, however, been constrained by the lack of adequate instruments.** To this end, the Government and the BoZ will adopt institutional arrangements that ensure that the BoZ has the necessary instruments to meet agreed monetary objectives. In particular, it has been agreed to convert the Government's outstanding bridge loan and a portion of the Mega bond held by the BOZ into marketable securities.

### C. External Prospects and Policies

18. **The balance of payments performed strongly in 2005 and looks set to continue doing so in 2006.** Supported by ongoing investment in the metal sector and a continued demand-driven rise in world copper prices, metal export receipts are projected to increase by over 50 percent in 2006. Similarly, nontraditional exports, including tourism, are set to grow by about 15 percent, resulting in a projected 48 percent increase in U.S. dollar terms of receipts from exports of goods and services in 2006. Imports of goods are expected to grow by 20 percent in U.S. dollar terms in 2006 owing to the combined effects of higher oil prices and the appreciation of the kwacha. Overall, the balance of trade in goods and services is projected to improve by about US\$460 million, but this is expected to be offset by income outflows related to foreign direct investment, leaving the current account (including grants) virtually unchanged at 3.8 percent of GDP.

19. **The capital account is expected to continue strengthening in 2006.** Overall, grants and loans from foreign donors are projected to increase by about 16 percent in 2006 to US\$676 million (5.5 percent of GDP), but budget support is expected to decrease to about US\$125 million (US\$100 million in grants) from the US\$155 million provided in 2005. At the same time, external debt service charged to the budget has been cut by one-third to about US\$90 million (0.7 percent of GDP) following attainment of the HIPC Initiative completion point. Based on expected continued improvement in Zambia's macroeconomic fundamentals, external investments in Zambia's sovereign debt market are expected to remain strong.

20. **The Government remains committed to maintaining and deepening the openness of its commercial and capital accounts.** The government will work with SADC and COMESA to strengthen their concerted efforts to reduce tariff and nontariff barriers to trade. At the same time, the government will consider unilaterally phasing out its 25 percent tax on exports of scrap metal.

## D. Structural Measures

21. **Structural reforms in 2006 are aimed at increasing productivity in both the public and private sectors and raising international competitiveness.** The agenda comprises reforms of public expenditure management and financial accountability (PEMFA), debt management, pension reforms, financial sector development, private sector development, and governance and accountability. Table 2 presents the specific measures that are included in the PRGF-supported program for 2006 as structural performance criteria and benchmarks.

### *Public Expenditure Management*

22. Following some delays in reaching agreement with the cooperating partners on the 2006 work plan, the implementation of the PEMFA reforms is set to make major progress; the process for contracting the installation of an integrated financial management and information system (IFMIS) is on course to initiate the pilot phase as presently scheduled.

- The contractor with the best technical and financial proposal has been selected and negotiations on the technical proposal have been concluded. The post qualification process has been completed ahead of schedule.
- To strengthen existing expenditure management systems, the Accountant General has issued rules and procedures for implementing and enforcing the new cash management system. The Accountant General will also prepare, within 60 days of the end of each quarter, quarterly reports for the Secretary to the Treasury on compliance with the commitment control system by ministry, province and spending agency (end-September 2006 benchmark).
- The Budget Execution Working Group has developed a new summarized report on budget execution and the first quarterly report (on releases and expenditures in 2006 Q1) was issued in May 2006.
- Final regulations and accounting manual for the new Finance Act will be completed and distributed to accounting heads by end-December 2006.

23. Progress, albeit slower than hoped, has also been made under the Public Service Management (PSM) program. Payrolls of most ministries have been transferred to the Payroll Management and Establishment Control (PMEC) system. The introduction of the PMEC system has significantly reduced headcount on the payroll, by removing large numbers of ineligible employees. To further strengthen the program, the Ministry of Defense will be transferred to the PMEC system, once a full head count and audit is done.

### *Debt Management*

24. The Ministry of Finance and National Planning (MoFNP) continues to monitor and validate end-quarter data on external debt stocks and, within 45 days of the end of quarter,

produces updated three-year schedules of projected debt service. The MoFNP is preparing an annual report on external debt management operations during 2005, and by end-June 2006, will validate the stock of on-lending agreements to ensure their effective enforcement. The MoFNP has also begun the process of developing a comprehensive database for the management of domestic debt, including contingent liabilities and the debts of the remaining parastatals (some of which are government secured), including the debts of the utility companies. In cooperation with the Bank of Zambia, the Ministry is also working on a program to strengthen debt management through further development of debt markets, including through the introduction of secondary markets for government securities.

### *Pension Reform*

25. The main challenges facing the pension schemes are to bring promised pension benefits more in line financially with employees' contributions under the PSPF, assure that resources are available to meet Government's current and past obligations to NAPSA and the PSPF, and to ensure a sound investment strategy is maintained for NAPSA's large and growing pension fund. To meet these challenges, Government will continue to pay down outstanding arrears on contributions to PSPF by at least K 100 billion a year during 2006–08, while fully meeting current obligations in a timely manner. Secondly, Government is undertaking pension reforms to slow down the pension liability accrual rate, protect only accrued pension benefits, and allow parametric changes to the PSPF pension system. Full implementation of the reforms will, however, need to await the amendment of Article 124 and related Articles of the Constitution, as well as relevant Acts.

### *Financial Sector Development*

26. **To enhance financial system stability, the Bank of Zambia (BoZ) is proceeding with the introduction of risk management systems.** The BoZ has taken a number of measures to further strengthen bank supervision. Online facilities for data submission have enhanced the timeliness and effectiveness of off-site supervision, while onsite supervision has been expanded to cover money laundering. A draft Deposit Protection Scheme Bill is being developed for banks and nonbank financial institutions (NBFIs). Nevertheless, introduction of legislation will be contingent on the establishment of the necessary preconditions for the introduction of the scheme, including the resolution of deposit-taking NBFIs. The necessary capacity is being developed to enable the BoZ to move to a fully risk-based approach to onsite supervision in 2007. A risk-management survey was conducted in the last quarter of 2005, and, drawing on the results of the survey, the BoZ has begun work on the development of risk-management guidelines that will form the basis of the risk-management framework for banks and NBFIs.

27. **The Financial Sector Development Plan (FSDP) includes a number of initiatives to foster increased availability of credit and the provision of financial services in rural and peri-urban areas.** These include the establishment of a Credit Reference Bureau and the development of a well-functioning microfinance system. Guidelines for the Credit Reference Bureau have been put in place and the BoZ has licensed one credit

reference services provider, which is able to meet standards of best practice. Regulations for the operation and supervision of microfinance institutions have been introduced, paving the way for the licensing of these institutions. Preparation of a rural financing policy and strategy will begin before the end of the year.

28. **The implementation of action plans for the problem nonbank financial institutions (NBFIs) is proceeding slowly.** The legal framework for the action plans is now in place, but other aspects of implementation have lagged. The Government remains firm in its commitment to reduce its shareholding in the DBZ to 25 percent. So far two investors have taken up equity in the institution, but more are needed. As for the National Savings and Credit Bank (NSCB), funding from IFAD and technical assistance for the installation of a new computer system have not yet been received; as a result, problems with unreconciled balances continue. The institution is exploring other options for its funding needs. Regarding the Zambia National Building Society (ZNBS), the Government has made a decision on the resolution of the institution, which will be effected by end-June 2006. Negotiations for the sale of 49 percent of the Zambia National Commercial Bank (ZNCB) have been completed and the privatization is expected to be completed soon.

*Private sector development*

29. **In the area of private sector development, the Government has focused its efforts on creating a business-friendly environment through the establishment of the Zambia Development Agency and the promotion of multi-facility economic zones (MFEZs).** The Government intends to provide infrastructure for the MFEZs and investors producing for both the domestic and export markets would be eligible for tax incentives. The Citizens' Empowerment Bill, which aims to provide opportunity to economically disadvantaged citizens to meaningfully participate in business activities, was recently approved by Parliament. With regard to reforms of costly labor regulations that inhibit formal sector employment, Government is presently processing Statutory Instruments for the Official Gazette that will limit minimum wage benefits and conditions of service to a more narrowly defined disadvantaged segment of the workforce. Consultations on other initiatives, such as the opening up to competition of the telecommunications international gateway and streamlining licensing requirements are ongoing.

30. Expanding Zambia's electricity generation capacity and network is a high priority in providing infrastructure support for private sector development. Moreover, Zambia could become a major exporter within the Southern African Power Pool. In agreement with the World Bank and IMF, and in lieu of privatization, the Government has pursued the commercialization of the state-owned electricity company (ZESCO), with the goal of achieving operational efficiency, sound financial management, and effective implementation of investment projects. By end-July 2006, ZESCO's management will provide all the necessary financial, technical, and managerial information to the World Bank and the IMF for an assessment of ZESCO's performance as required for the evaluation point under the commercialization process, particularly during the first year of operations under its new

business plan, which ended on March 31, 2006. To ensure the independence of ZESCO's operations, the Government will not on-lend or guarantee any external credits to ZESCO prior to a satisfactory assessment at the evaluation point. (Following a satisfactory assessment, the Government would continue to adhere to its policy of providing guarantees only on concessional borrowing.) In addition, prior to the evaluation point assessment, ZESCO will pay all of its tax arrears to the ZRA that were accumulated since the initiation of the commercialization process. Looking ahead, to reinforce transparency and corporate governance, Government will explore procedures in line with international best practice on reporting and managing ZESCO's profits from export sales.

### *Strengthening data*

31. **The Government will take steps to expand Zambia's capacity to collect and report quality economic data.** At present, there are serious shortcomings in the data for the national accounts, consumer price index, and the balance of payments. The rebasing exercises for the national accounts and CPI, both of which use 1994 as the base year, are long overdue. As a result, there are large distortions in the data and some important sectors and consumer products are not even represented in the statistics. Major gaps also exist in the BOP statistics, greatly handicapping analysis of external sector developments. Systematic data is lacking on the inflows and outflows of the mining sector, workers' remittances, foreign direct investment, and private sector income and capital flows. Moreover, data on donor support that does not pass through the government are not captured in the balance of payments. To remedy this situation, Government will allocate funding for a comprehensive economic census for the rebasing of the national accounts. The census will be completed by end-May 2007 (Benchmark). The Central Statistics Office will also commence the rebasing of the CPI statistics by July 2006, with the aim of completing the exercise by March 2007. In addition, the BoZ will request technical assistance from the IMF to shore up its survey methods for the BOP.

### **E. Technical Assistance Needs**

32. The Government has requested technical assistance from the IMF in the areas of tax administration and policy, including a diagnostic review of the present system. In addition, the Government will request technical assistance for the updating and rebasing of the national accounts and CPI statistics. Government will also seek technical assistance from the donor community for conducting the economic census, which would form the foundation for the rebasing of the national accounts. The BoZ will request a second follow-up mission in the area of liquidity management, monetary, and exchange rate policies. The BoZ will also request technical assistance to strengthen the balance of payments statistics.

### **IV. Program Monitoring**

33. Progress in implementing the PRGF-supported program will continue to be monitored quarterly, with semi-annual reviews, based on the quantitative and structural

performance criteria and benchmarks in Tables 2 and 3. The government requests modification of the performance criteria for end-June 2006, which will be the basis for the fifth review expected to be completed by December 2006, for the ceiling on Government's net domestic financing and the ceiling and floor on the BoZ's net domestic assets and gross international reserves, respectively (see Table 3). The program for the remainder of 2006 sets quantitative indicative targets for end-September and performance criteria for end-December, which will be the basis for the sixth review expected to be completed by May 31, 2007. In line with the schedule set out in Table 2, performance criteria under the structural program will be part of the basis for completing program reviews. The quantitative and structural performance criteria and benchmarks are defined in the attached technical memorandum of understanding.

MEFP: Table 1. Zambia: Quantitative Performance Criteria (PC), Benchmarks and Indicative Targets Under the PRGF Program 1/  
(In billions of Kwacha, unless otherwise indicated)

	2004	2005												
		Dec. Stocks		Status	Jun.		Status	Sep.		Status	Dec.		Status	
		Prog.	Act.		Prog.	Act.		Prog.	Act.		Prog.	Act.		
<u>Performance Criteria</u>														
1	Ceiling on the cumulative increase in net domestic assets (NDA) of the Bank of Zambia 2/ 3/ 4/ 5/ Adjusted ceiling	6,836	14	-185	<b>Met</b>	182	-41	<b>Met</b>	104	-306	<b>Met</b>	166	-344	<b>Met</b>
			94			296			286			226		
2	Ceiling on the cumulative increase in net domestic financing (NDF) 2/ 5/ Adjusted ceiling	3,305	60	168	<b>Met</b>	217	319	<b>Met</b>	301	513	<b>Not met</b>	500	611	<b>Met</b>
			190			374			496			661		
3	Floor on the stock of gross international reserves (GIR) of the Bank of Zambia (In millions of U.S. dollars) 2/ Adjusted floor	238	232	251	<b>Met</b>	204	275	<b>Met</b>	244	308	<b>Met</b>	246	331	<b>Met</b>
			225			192			194			259		
4	Ceiling on new external payment arrears (in millions of US dollars)		0	0	<b>Met</b>	0	0	<b>Met</b>	0	0	<b>Met</b>	0	0	<b>Met</b>
5	Ceiling on the stock of short-term debt and on contracting or guaranteeing of nonconcessional debt (In millions of U.S. dollars) 6/		0	0	<b>Met</b>	0	0	<b>Met</b>	0	0	<b>Met</b>	0	0	<b>Met</b>
6	Ceiling on cumulative new concessional loans collateralized or guaranteed by the central government or the Bank of Zambia for ZESCO.		20	0	<b>Met</b>	20	0	<b>Met</b>	20	0	<b>Met</b>	20	0	<b>Met</b>
7	Floor on the cumulative payment of domestic arrears of the government 5/		62	65	<b>Met</b>	100	144	<b>Met</b>	151	220	<b>Met</b>	284	413	<b>Met</b>
<u>Quantitative Benchmarks</u>														
8	Cumulative ceiling for the Central Government wage bill 5/		593	508	<b>Met</b>	1,236	1,090	<b>Met</b>	1,876	1,782	<b>Met</b>	2,531	2,455	<b>Met</b>
9	Ceiling on the cumulative arrears on the Central Government wage bill		0	0	<b>Met</b>	0	0	<b>Met</b>	0	0		0	0	<b>Met</b>
Memorandum items:														
10	Cumulative net balance of payments support (In millions of U.S. dollars)		-8	-14		-29	-41		4	-45		13	25	
	Balance of payments assistance		31	36		41	41		98	64		133	155	
	Central Government debt service obligations (excl. IMF)		-39	-51		-78	-83		-93	-109		-120	-130	
	Shortfall (-)/Excess (+) net BOP support			-6			-12			-49			12	
Program exchange rates														
	Kwacha/US\$	4,771												
	US\$/SDR	1.5478												

1/ The definitions of the indicative targets are contained in the Technical Memorandum of Understanding (TMU).

2/ Adjustors, including for balance of payments support are defined in the TMU.

3/ Excludes HIPC debt relief from the IMF.

4/ The ceiling will be adjusted for changes in the legal reserve requirements.

5/ Cumulative from the end of 2004.

6/ Nonconcessional loans are defined as having a grant element of less than 40 percent.

MEFP Table 2. Zambia: Performance Under the Structural Program for 2006<sup>1</sup>

Measure	Timing <sup>2</sup>	Status
<b>Performance Criteria</b>		
The government will refrain from paying any amounts for which it is not legally liable and which are not included in the budget.	Continuous	Observed.
The Investment and Debt Management Department (IDM) of the MoFNP will validate the stock of onlending agreements with a view to effectively enforcing these agreements. The IDM will report to the Secretary of Treasury on the validation of these agreements.	end-June 2006	Process of compiling the information has commenced and was finalized in March. Verification began in April.
Initiate the piloting of an integrated financial management and information system (IFMIS) in at least three line ministries.	end-September 2006	The process is on schedule. A contractor has been selected and negotiations on the technical proposal have been concluded. The post-qualification process has also been concluded. A contract is expected to be signed in June 2006.
Complete a diagnostic review of tax policy and administration.	end-December 2006	
The IDM will validate the stock of government contingent liabilities, including loan guarantees, and pension obligations. The IDM will report to the Secretary of Treasury on the validation of these liabilities.	end-December 2006	
Report on the findings of a preliminary review of the piloting of the IFMIS in at least three line ministries.	end-March 2007	The process of selecting a contractor to install the IFMIS is on schedule.
<b>Benchmarks</b>		
<b><i>Public expenditure management and financial accountability (PEMFA)</i></b>		
Issue summary tables, developed in consultation with the PEMFA Joint Technical Working Group (JTWG), using activities based budgeting classification and identifying poverty reducing programs.	end-March 2006	Reports based on recommendations from the Budget Execution Working Group were implemented in May 2006.

MEFP Table 2. Zambia: Performance Under the Structural Program for 2006<sup>1</sup>

Measure	Timing <sup>2</sup>	Status
Issue new regulations and revised accounting manuals for the new Finance Act.	end-March 2006	Layman's Draft Financial Regulations, will be finalized by end-June 2006. A technical team has produced initial draft manuals, which will be reviewed and finalized by end-December 2006.
In consultation with the PEMFA JTWG, issue (i) accountability rules and procedures under the new cash management framework and (ii) corresponding administrative procedures for enforcement, to ensure the timely release of funds by the Ministry of Finance and National Planning (MoFNP).	end-March 2006	Cash-flow framework was finalized and implemented with accompanying user manual in 2005. Loading of 2006 activities-based budget classification and cash-flow framework has been completed.
Submit to Cabinet the first draft ("Green Paper") of the Medium-Term Expenditure Framework (MTEF) for 2007-2009.	end-August 2006	Work in progress. Pending finalization of the Fifth National Development Plan.
The Accountant General will, within 60 days of the end of each quarter, submit to the Secretary to the Treasury quarterly reports on compliance with the commitment control system by ministry, province, and spending agency.	Continuous Beginning September 2006	
<b>Debt management</b>		
Validate end-quarter external debt stock data and, within 45 days, provide updated 3-year schedule of debt service falling due to the Budget Director.	Continuous	Observed through March 2006.
The MoFNP will issue an annual report on external debt management operations during 2005.	end-June 2006	Preparation of the report has begun.
<b>Financial sector development</b>		
The National Savings and Credit Bank (NSCB) and the Development Bank of Zambia (DBZ) submit to the Bank of Zambia (BoZ) plans for their incorporation under the Companies Act.	end-December 2005	Observed.
Execute the action plan adopted by the Government on the resolution of the Zambia National Building Society (ZNBS).	end-June 2006	.

MEFP Table 2. Zambia: Performance Under the Structural Program for 2006<sup>1</sup>

Measure	Timing <sup>2</sup>	Status
Submit to cabinet a proposal for the legal framework establishing a credit reference bureau, including the necessary amendments to privacy laws.	end-June 2006	BoZ has issued interim guidelines and is in the process of licensing a provider for credit referencing services. BoZ has commenced drafting the layman's law for credit reference agencies and will engage a consultant for finalizing a proposal by March 2007.
Incorporate the NSCB and DBZ under the Companies Act.	end- December 2006	
<b>Private sector development</b>		
ZESCO's management will provide all the necessary financial, technical, and managerial information to the World Bank and the IMF for an assessment of ZESCO's performance in line with the conditions for reaching the evaluation point under the commercialization process.	end-July 2006	
<b>Governance and transparency</b>		
Unbudgeted expenditure requirements will be funded only to the limits of the contingency resources indicated in the budget or only after the cabinet has approved any changes by finding compensatory funding within the approved budget resources.	Continuous	Observed through March 2006.
Publication of quarterly budget execution reports using the activity-based budgeting classification, within 45 days of the end of each quarter, including summary tables developed in consultation with the PEMFA JTWG.	Continuous	Observed. Report for the fourth quarter of 2005 was published on time, but coverage was incomplete. MoFNP is correcting the data.
<b>Statistics</b>		
The Central Statistics Office will complete a comprehensive economic census for the full rebasing of the national accounts.	end-May 2007	

<sup>1</sup>The definitions of the prior actions, structural benchmarks, and performance criteria are contained in the technical memorandum of understanding (TMU).

<sup>2</sup>Refers to end of month for non-continuous measures.

MEFP: Table 3: Zambia: Quantitative Performance Criteria (PC), Benchmarks and Indicative Targets Under the PRGF Program 1/  
(In billions of Kwacha, unless otherwise indicated)

	2006 Base	2006 Revised Base	2006					
			Mar			Jun.	Sep.	Dec
			Prog.	Act	Status	Prog.	Prog.	Prog.
<u>Performance Criteria</u>								
1 Ceiling on the cumulative increase in net domestic assets (NDA) of the Bank of Zambia 2/ 3/ 4/ 5/ Adjusted ceiling	3,019	2,911	-37	-236	Met	-138	-126	-241
				-236				
2 Ceiling on the cumulative increase in net domestic financing (NDF) 2/ 5/ Adjusted ceiling	3,825	3,917	136 121	392	Not met	439	629	706
3 Floor on the cumulative increase in gross international reserves (GIR) of the Bank of Zambia (In millions of U.S. dollars) 2/ Adjusted floor	331	342	8 11	11	Met	58	65	153
4 Ceiling on new external payment arrears			0	0	Met	0	0	0
5 Ceiling on the stock of short-term debt and on contracting or guaranteeing of nonconcessional debt (In millions of U.S. dollars) 6/			0	0	Met	0	0	0
7 Floor on the cumulative payment of domestic arrears of the government 5/ 7/			50	80	Met	89	155	238
<u>Quantitative Benchmarks</u>								
8 Cumulative ceiling for the Central Government wage bill 5/			654	621	Met	1,385	2,176	2,967
9 Ceiling on the cumulative arrears on the Central Government wage bill			0	0	Met	0	0	0
Memorandum items:								
10 <u>Cumulative net balance of payments support (In millions of U.S. dollars)</u>			0.4	3.8		-16.7	36.3	36.7
Balance of payments assistance			16.9	26.9		35.2	55.0	125.6
Central Government debt service obligations (excl. IMF)			-16.5	-23.1		-51.9	-18.7	-88.9
Shortfall (-)/Excess (+) net BOP support				3.4				
Program exchange rates								
Kwacha/US\$	4,550	3,509						
US\$/SDR	1.436	1.429						

1/ The definitions of the items in the quantitative program are contained in the Technical Memorandum of Understanding (TMU). Targets for September and December are indicative.

2/ Adjustors, including for balance of payments support are defined in the TMU.

3/ Excludes HIPC debt relief from the IMF.

4/ The ceiling will be adjusted for changes in the legal reserve requirements.

5/ Cumulative from the end of 2005.

6/ Nonconcessional loans are defined as having a grant element of less than 40 percent.

7/ This includes K100 billion for the payment of arrears to the Public Service Pension Fund.

**Technical Memorandum of Understanding for  
The Poverty Reduction and Growth Facility (PRGF) Arrangement**

**I. INTRODUCTION**

1. This memorandum sets out the understandings between the Zambian authorities and the International Monetary Fund (IMF) regarding the definitions of the quantitative and structural performance criteria and benchmarks for the program for 2006 supported by the PRGF arrangement, as well as the related reporting requirements. The definitions are valid at the start of the program, but may need to be revisited to ensure that the memorandum continues to reflect the best understanding of the Zambian authorities and IMF staff to monitor the program.

**II. QUANTITATIVE PERFORMANCE CRITERIA AND BENCHMARKS:  
DEFINITIONS AND DATA SOURCES**

**A. Net Domestic Assets (NDA) of the Bank of Zambia (BoZ)**

2. Net domestic assets (NDA) of the BoZ are defined as the monthly average (based on daily data) of reserve money less net foreign assets of the BoZ calculated at Kwacha 3,509.0 per U.S. dollar (program exchange rate).<sup>3</sup> Reserve money consists of currency issued, required reserves on Kwacha deposits, required reserves on foreign currency deposits (at the program exchange rate), positive current account balances of banks with the BoZ, and deposits in the BoZ of non-central government institutions. Net foreign assets of the BoZ are defined as gross international reserves (defined below) plus any other foreign assets, including the US\$25 million blocked reserves at the former Meridien Bank (MBZ), minus foreign liabilities (defined below). The Kwacha values are derived from the U.S. dollar values using the program exchange rate.

3. Foreign reserve liabilities are defined as short term (one year or less in original maturity) foreign currency-denominated liabilities of the BoZ to nonresidents and outstanding use of IMF credit.

4. The ceilings on NDA will be adjusted upward by the amount of the shortfall of balance of payments support net of debt service as indicated in Table 3 (item 10) of the Memorandum of Economic and Financial Policies (MEFP), up to a maximum of US\$20 million for the period end-December 2005 to end-December 2006. External disbursements that occur anytime during the month of the test date will be treated as if they

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<sup>3</sup> Unless otherwise defined, program exchange rates for 2006 between the U.S. dollar and other (non-Kwacha) currencies will be equal to the end-December 2005 rates. The U.S. dollar/SDR rate for program purposes is 1.4293. Any other assets (e.g. gold) would be revalued at their end-December 2005 market prices.

were disbursed on the first day of the month.<sup>4</sup> In the event of excess balance of payments support net of debt service, the ceiling on NDA will be adjusted downward by 100 percent of the additional excess support. However, if part of the excess support is used to reduce the stock of Treasury bills or bonds held by commercial banks and the non-bank sector, then the programmed NDA will be adjusted upward by that amount. The Kwacha value of the cumulative shortfall/excess will be calculated at the program exchange rate.

5. The ceiling on NDA will be adjusted downward/upward to reflect decreases/increases in the legal reserve requirements on deposits in commercial banks. The adjustor will be calculated as the percent change in the reserve requirement multiplied by the actual amount of required reserves (Kwacha and foreign-currency denominated) at the end of the previous calendar month.

### **B. Net Domestic Financing (NDF)**

6. Net domestic financing is defined as the Central Government's net borrowing from the banking and non-banking sectors (See table 1).<sup>5</sup> All government-issued securities will be recorded at cost (face value less discount). NDF will be defined as:

(a) the net position of the Government with commercial banks, including:  
(i) Treasury bills; (ii) government bonds; (iii) loans and advances; less (iv) support to MBZ; and (v) central government deposits (defined to include account balances under the authority of controlling officers); plus

(b) BoZ holdings of: (i) Treasury bills; (ii) government bonds; (iii) the Kwacha bridge loan (overdraft facility); less (iv) the government's position at the BoZ; and (v) the donor suspense account; plus (vi) the long-term non-transferable security issued against the government's total indebtedness to BoZ as at end-2002.

(c) Nonbank holdings will include: Treasury bills; and government bonds.

7. The NDF ceiling will be adjusted upward by the amount of the shortfall in balance of payments support net of debt service as indicated in Table 3 (item 10) of the MEFP, up to a maximum of US\$20 million for the period end-December 2005 to end-December 2006. In the event of excess balance of payments support net of debt service, the ceiling on NDF will

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<sup>4</sup> This implies that, for purposes of monitoring the NDA, the targeted NDA will be increased by the amount of the disbursement divided by the number of business days in the month and multiplied by the number of business days from the beginning of the month to the day prior to the disbursement.

<sup>5</sup> The Central Government includes all the administrations identified by the budget heads listed in the 2006 Yellow Book.

be adjusted downward by 100 percent of the additional excess support. The Kwacha value of the cumulative shortfall/excess will be converted at the program exchange rate.

8. The data source for the above will be the “Net Domestic Financing” Table produced by the BoZ Economics Department, submitted on a weekly basis, and reconciled with the monthly monetary survey.

### **C. Gross International Reserves of the BOZ**

9. Unless otherwise noted here, gross international reserves of the BoZ will be defined as reserve assets of the BoZ (See Table 2). Reserve assets are defined in the IMF BOP manual (5<sup>th</sup> edition) and elaborated in the reserve template of the IMF’s special data dissemination standards (SDDS). They exclude, for example, foreign assets not readily available to or controlled by the monetary authorities, and foreign currency claims on Zambian residents.

10. Gross international reserves consist of (i) monetary gold; (ii) foreign currency in cash; (iii) unencumbered foreign-currency deposits at non-resident banks; (iv) foreign securities and deposits; (v) SDR holdings and Zambia’s reserve position with the IMF; and (vi) balances in the BIS account related to debt service to Paris Club creditors. Gross reserves exclude non-convertible currencies, pledged, swapped, or any encumbered reserve assets including but not limited to reserve assets used as collateral or guarantees for third-party external liabilities, commercial bank reserve requirements in foreign currency, and the US\$25 million deposit in MBZ (in liquidation).

11. The floor on gross international reserves will be adjusted: (i) downward by the amount in U.S. dollars of the shortfall in balance of payments support net of debt service as indicated in Table 3 (item 10) of the MEFP, up to a maximum of US\$20 million for the period end-December 2005 to end-December 2006; (ii) upward by 100 percent of the cumulative excess balance of payments support net of debt service. However, if part of the excess support is used to reduce the stock of Treasury bills or bonds held by commercial banks or the non-bank sector, then the programmed reserves buildup will be adjusted downward by that amount; (iii) downward/upward for any shortfall/excess in the U.S. dollar value of programmed disbursements from the IMF under the PRGF arrangement; (iv) downward for any increase in BoZ short-term foreign currency denominated debt (to residents and nonresidents), using the definition of short-term debt below.

12. For the purpose of this target, as well as those for external debt and arrears, valuation will be in U.S. dollars using the program exchange rates.

13. Data on gross international reserves, including its components, will be reported by the BoZ on a weekly and end-month basis.

#### **D. External Payment Arrears**

14. The performance criterion on the non-accumulation of new external arrears is continuous. Official external payment arrears are defined as unpaid debt service by the Central Government and BoZ, beyond the due date and/or the grace period, if any. This definition excludes arrears subject to rescheduling.

15. Data on arrears are compiled jointly by the Ministry of Finance and National Planning (MoFNP) and BoZ and will be reported by the MoFNP on a quarterly basis.

#### **E. Official Medium- and Long-Term Concessional External Debt**

16. Official medium- and long-term concessional external debt is defined as all forms of official debt with original maturity of more than one year contracted or guaranteed by the Central Government and BoZ having a grant element of no less than 40 percent, but excludes debts subject to rescheduling. The grant element is to be calculated by using currency-specific commercial interest reference rates (CIRRs) reported by the DAC of the OECD; for maturities of less than 15 years, the grant element will be calculated based on six-month averages of CIRRs, and for maturities longer than 15 years, the grant element will be calculated based on 10-year averages. Adjustment lending from the IMF will be excluded.

17. This minimum grant element applies not only to debt as defined in Point 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274-(00/85) of August 24, 2000; see Annex), but also to commitments contracted or guaranteed for which value has not been received. This excludes non-concessional loans stemming from the rescheduling of external arrears.

18. Detailed data on all new concessional and non-concessional debt contracted or guaranteed will be provided by the MoFNP on a monthly basis.

#### **F. Official External Short-Term Non-Concessional External Debt**

19. Official external short-term non-concessional external debt is defined as the outstanding stock of external debt with original maturity of less than one year owed or guaranteed by the central Government or the BoZ. For this purpose short-term debt will include forward commodity sales but will exclude normal trade credit for imports. No new official external short-term debt will be contracted or disbursed during the program period. The term “debt” has the meaning set forth in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274-(00/85) of August 24, 2000; see Annex).

20. The data will be reported by the MoFNP and BoZ on a monthly basis.

### **G. Domestic Arrears of Government**

21. Domestic arrears are defined as: (i) any bill that has been received by a spending ministry from a supplier for goods and services delivered (and verified) and for which payment has not been made within 30 days after the due date of payments; (ii) wage, salary and any other payment to government employees, including pension contributions and all forms of housing allowances, that were due to be paid in a given month but remained unpaid on the 15<sup>th</sup> of the following month; and (iii) interest or principal obligations which remain unpaid 30 days after the due date of payment. Included in the quarterly program floors for payment of domestic arrears in 2006 is payment of K 25 billion each quarter toward Government's arrears on contributions to the Public Sector Pension Fund.

22. Information regarding domestic arrears is to be compiled through audits of the accounts of spending Ministries and agencies, conducted by the Internal Audit division of the MoFNP. The audits will be completed and data submitted to IMF staff by the Secretary of the Treasury within six weeks of the end of each quarter.

### **H. The Central Government's Wage Bill**

23. For the purposes of the wage bill, the definition of Central Government includes all expenditure heads covered in the 2006 Yellow Book. The Central Government's total wage bill will include payments on wages, salaries, allowances, and all other items specified as personal emoluments in the Yellow Book, and any direct or indirect payments of housing allowances to employees. The Government will provide, on a monthly basis and by budget head, the following data: (i) the number of all employees in the Central Government for each budget head; (ii) the basic salary, the allowances and any other personal emoluments released during the month; (iii) the arrears incurred during the month on the basic salary, on the allowances, and on any other personal emoluments; (iv) the number of employees retrenched and the corresponding retrenchment costs.

24. All the data will be submitted to the IMF staff by the MoFNP within three weeks of the end of each month.

## **III. STRUCTURAL PERFORMANCE CRITERIA AND BENCHMARKS**

### **A. Performance Criteria**

#### **Continuous Criterion**

25. The Government will refrain from paying any amounts for which it is not legally liable and which are not included in the budget.

### **Public Expenditure Management**

26. By end-September 2006, the Government will initiate the piloting of the Integrated Financial Management and Information System (IFMIS) in at least three ministries.

27. By end-March 2007, the government will report on the findings of a preliminary review of the piloting of the IFMIS in at least three line ministries.

### **Debt Management**

28. By end-June 2006, the Investment and Debt Management Department (IDM) of the MoFNP will validate the stock of onlending agreements with a view to effectively enforcing these agreements. The IDM will report to the Secretary of Treasury on the validation of these agreements.

29. By end-December 2006, the IDM will validate the stock of government contingent liabilities, including loan guarantees and pension obligations. The IDM will report to the Secretary of Treasury on the validation of these liabilities.

### **Fiscal Policy**

30. By end-December 2006, complete a diagnostic review of policy and tax administration.

## **B. Benchmarks**

### **Continuous Benchmarks**

31. Unbudgeted expenditure requirements will be funded only to the limits of the contingency resources indicated in the budget or only after the Cabinet has approved any changes by finding compensatory funding within the approved budget resources.

32. The MoFNP will publish quarterly budget execution reports using the classification system of activity-based budgeting within 45 days of the end of each quarter, including summary tables developed in consultation with the PEMFA JTWG.

33. The MoFNP will validate end-quarter debt stock data and, within 45 days, provide updated 3-year schedule of debt service falling due to the Budget Director.

34. Beginning by September 30, 2006, the Accountant General will within 60 days of the end of each quarter submit to the Secretary to the Treasury quarterly reports on compliance with the commitment and control system by ministry, province, and other spending agencies.

**Public Expenditure Management**

35. By end-March 2006, the Government will issue summary tables, developed in consultation with the PEMFA Joint Technical Working Group (JTWG), using activities based budgeting classification and identifying poverty reducing programs.
36. By end-March 2006, in consultation with the PEMFA JTWG, the government will issue (i) accountability rules and procedures under the new cash management framework and (ii) corresponding administrative procedures for enforcement, to ensure the timely release of funds by the MoFNP.
37. By end-March 2006, the MoFNP will issue the new regulations and the revised accounting manual needed for the new Public Finance Act.
38. By end-August 2006, the Government will prepare and submit to Cabinet a first draft of the Medium-Term Expenditure Framework (“Green Paper”) for the period 2007-2009.

**Debt Management**

39. By end-June 2006, the MoFNP will issue an annual report on external debt management operations during 2005.

**Financial Sector Development**

40. By end-June 2006, the Government will execute the action plan on the resolution of the Zambia National Building Society.
41. By end-June 2006, the MoFNP will submit to Cabinet a proposal for the legal framework establishing a credit reference bureau, including the necessary amendments to privacy laws.
42. By end-December 2006, the National Savings and Credit Bank and the Development Bank of Zambia will be incorporated under the Companies Act.

**Private Sector Development**

43. By end-July 2006, ZESCO’s management will provide all the necessary financial, technical, and managerial information to the World Bank and the IMF for an assessment of ZESCO’s performance in line with the conditions for reaching the evaluation point under the commercialization process.

**Statistics**

By end-May 2007, the Central Statistics Office will complete a comprehensive economic census for the full rebasing of the national accounts.