

**BUDGET ADDRESS BY THE HON. NG'ANDU P. MAGANDE, MP**  
**MINISTER OF FINANCE AND NATIONAL PLANNING**  
**DELIVERED TO THE NATIONAL ASSEMBLY ON FRIDAY, 9<sup>TH</sup> FEBRUARY 2007**

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1. Mr. Speaker, I beg to move that the House do now resolve into Committee of Supply on the Estimates of Revenue and Expenditure for the year 1<sup>st</sup> January 2007 to 31<sup>st</sup> December 2007, presented to the National Assembly in February 2007.

2. Sir, I am the bearer of a message from His Excellency the President recommending favourable consideration of the motion I now lay on the Table.

3. Mr. Speaker, on 28<sup>th</sup> September last year, the Presidential, Parliamentary and Local Government elections were held throughout the country in a calm and peaceful atmosphere. The re-election of the MMD into Government reflects not only the endorsement of the policies of the New Deal Administration, but also a vote of confidence in the leadership of His Excellency the President, Levy Patrick Mwanawasa, SC.

4. Given this fresh mandate, the New Deal Government will continue to work tirelessly to improve the lives of our people and therefore, has the resolve to pursue its economic agenda with renewed vigour to steer our country to greater heights.

5. Mr. Speaker, Honourable Members, the Budget Address enables the Government to review economic performance, identify challenges facing the nation and outline policies for meeting these challenges. Some of the major challenges include the consolidation of the macroeconomic stability and sustained growth in the economy. I wish to report, Sir, that we

have laid a strong foundation to meet the above challenges.

6. Sir, having achieved relative macroeconomic stability and positive economic growth, it is paramount that these achievements are translated into improved standard of living for our people. To achieve this, there is need for improved service delivery, hence the theme for this year's Budget **"From Stability to Improved Service Delivery"**.

7. Mr. Speaker, this budget has been drawn from the Fifth National Development Plan (FNDP) and has benefited greatly from the consultative process with the general public, business community, trade unions, civic and religious organisations, professional associations and our cooperating partners. This underlines the Government's will to consult on issues of national importance. May I, therefore, take this opportunity to thank individuals, various organisations and government officials that have contributed to the formulation of this budget.

8. Sir, I start my Address, in Part One, by briefly reviewing the performance of the global economy during the past year. The performance of the domestic economy during the same period is reviewed in Part Two. This is followed, in Part Three, by an outline of Government's economic and social policies for 2007. In Part Four, I present details of expenditure and the supporting revenue for the 2007 budget, respectively. Finally, in Part Five, I give my concluding remarks.

## **PART I**

### **PERFORMANCE OF THE GLOBAL ECONOMY IN 2006**

9. Mr. Speaker, the global economy was projected to grow by 5.1 percent in 2006 compared to 4.9 percent recorded in 2005. This growth was led by the United States of America at 3.4 percent, Japan at 2.7 percent and the Euro area at 2.4 percent. Further, emerging markets continued to grow rapidly at 7.3 percent with China sustaining growth of around 10 percent. Africa grew at 5.4 percent with Sub-Saharan African countries growing at an average rate of 5.2 percent.

10. Mr. Speaker, oil prices in 2006 increased significantly, partly as a result of buoyant global economic activity. The petroleum spot price rose to a record high of over US \$76 per barrel. This rise in prices was due to increased demand and the uncertainties in some major oil producing countries.

11. Sir, non-oil commodity prices, particularly that of copper also had a phenomenal increase in 2006, mainly spurred by demand from China which accounted for about one quarter of the total world demand for copper, aluminium and steel. The average price of copper rose to US \$3.05 per pound in 2006 from US \$1.67 per pound in 2005.

12. Mr. Speaker, these developments in the global economy had a positive effect on Zambia's terms of trade as the increase in oil prices was outweighed by the increase in copper prices.

## **PART II**

### **PERFORMANCE OF THE DOMESTIC ECONOMY IN 2006**

#### **MACROECONOMIC PERFORMANCE**

13. Mr. Speaker, let me now highlight the performance of the domestic economy during 2006.

14. Sir, the economy continued to perform well with the preliminary real Gross Domestic Product (GDP) growth estimated at 5.8 percent from 5.2 percent recorded in 2005. This performance was against the target of 6 percent set for 2006. Growth was largely driven by the mining, construction and transport sectors. Other sectors that registered positive growth were agriculture, tourism, manufacturing, wholesale and retail trade, and the services sector.

15. Mr. Speaker, inflation fell to its lowest level in the last 30 years. The annual rate of inflation was 8.2 percent as at end December, 2006 compared to the annual target of 10 percent and an outturn of 15.9 percent in 2005.

16. Mr. Speaker, these positive developments are due to continued implementation of prudent monetary and fiscal policies coupled with increased food production. This is reflected by the Government's containment of domestic borrowing within the set target of 1.6 percent of GDP. By end of the year, domestic borrowing was 1.5 percent of GDP.

17. Sir, the level of Government borrowing not only eased pressure on inflation and interest rates, but also helped to contain the interest cost on the domestic public debt.

18. Mr. Speaker, Zambia's external position continued to improve as reflected in the build-up of Gross International Reserves (GIR) to 2 months of import cover in 2006 from 1.6 months of import cover in 2005. Similarly, the current account deficit as a percentage of GDP excluding grants reduced from 11.8 percent in 2005 to 2.3 percent in 2006. Sir, the reduction of the current account deficit was due to increased export receipts arising from the record high copper prices and increased export volumes.

19. Sir, in addition, the historic debt relief received in 2006 and the increased budgetary support from our cooperating partners helped to strengthen the external position.

#### **SECTORAL PERFORMANCE**

##### ***AGRICULTURE***

20. Mr. Speaker, the agriculture, forestry and fishing sector continued to perform well in 2006, registering a growth rate of 2.4 percent. Excluding forestry and fishing, the agriculture sub-sector grew by 3.9 percent. This was mainly on account of increased production of crops. In particular, a bumper harvest of 1.4 million metric tonnes of maize was recorded during the 2005/2006 farming season compared to 866,000 metric tonnes in the previous farming season. This is as a result of not only the favourable weather and increased credit but also programmes such as the fertilizer support, food security pack and out-grower schemes which have boosted production of food and cash crops among the 800,000 small-scale farmers.

##### ***CONSTRUCTION***

21. Sir, preliminary data indicate that the construction sector registered growth of 9 percent. This however, was a slow down compared to the growth rate of 21.2 percent in 2005. Growth in this sector was driven by housing, road construction and other civil works. The increasing demand for cement has led to investments of US \$170 million, which will increase production to over 900,000 tonnes within the next three years.

##### ***MANUFACTURING***

22. Mr. Speaker, the manufacturing sector in 2006 grew by 3.3 percent compared to 2.9 percent in 2005. Growth was mainly driven by the food, beverages and tobacco sub-sector, which grew by 4.5 percent in 2006 compared to 3.6 percent in 2005. Positive growth was also recorded in the chemicals, rubber and plastics, fabricated metal products, base metal products, and the paper and paper products sub-sectors, mainly on account of increased domestic and external demand.

##### ***MINING AND QUARRYING***

23. Mr. Speaker, the mining sector continued to perform well in 2006. Preliminary estimates indicate that real GDP growth in the mining and quarrying sector increased to 11.8 percent from 7.9 percent in 2005. This was largely on account of the rise in mineral production. Copper production increased by 7.9 percent from 459,324 tonnes in 2005 to 492,016 tonnes in 2006. Cobalt production, however, reduced from about 5,537 tonnes in 2005 to 4,658 tonnes in 2006. Direct employment in the mining industry is close to 50,000 employees.

## ***TOURISM***

24. Sir, the tourism sector continued to record positive growth with an increase in investment and tourist arrivals. The number of tourist arrivals in 2006 is estimated to have increased by 3.1 percent to 670,000 from 650,000 in 2005. Earnings from this sector are estimated at US \$176.7 million in 2006 compared to US \$164.8 million recorded in 2005. The growth in this sector has continued to be driven by improved infrastructure and marketing as well as private sector investments.

## ***ENERGY***

25. Mr. Speaker, preliminary data show that the energy sector registered a growth of 11.3 percent in 2006 compared to 5.4 percent in 2005. This was on account of increased electricity generation following the completion of rehabilitation and upgrading of machinery at the Kariba North Power Station.

26. Sir, the Government continued with the Rural Electrification Programme and 43 projects across the country were financed. As a result, 35 Basic Schools, 5 Clinics and Health Centres, 5 other public facilities such as Court houses and markets and over 380 houses were electrified.

27. Mr. Speaker, the supply of petroleum products in 2006 was stable. The Government put in place measures to ensure that the shortage experienced in 2005 following the disruptions at INDENI refinery did not recur. Overall, there was a notable increase in the levels of Diesel and Jet A1 fuel consumed when compared to the volumes of 2005. This was due to the increased demand from mining activities in the country.

## ***TRANSPORT AND COMMUNICATIONS***

28. Mr. Speaker, preliminary data indicate that the Transport and Communications sector grew by 13.4 percent in 2006 compared to 11 percent in 2005. All the sub-sectors, namely communications, roads, rail and air transport recorded strong growth due to increased economic activity in other sectors.

## **DOMESTIC DEBT**

29. Mr. Speaker, the stock of domestic debt increased by 24.2 percent to K7,687 billion as at end 2006 from K6,189 billion at end 2005. As a share of GDP, the stock of domestic debt in 2006 was 20.2 percent compared to 19 percent in 2005. The increase in the stock of domestic debt was largely on account of the expansion in the stock of government securities, domestic arrears and awards and compensation.

30. Mr. Speaker, the stock of government securities increased by 25.7 percent to K6,706 billion from K5,337 billion. The increase was mainly due to restructuring part of the debt owed to Bank of Zambia into Government securities.

31. Sir, domestic arrears recorded a slight increase of 1.8 percent during 2006. In the same period, awards and compensation rose by 5.7 percent. However, pension arrears recorded a decline of 6.6 percent due to the Government's commitment to dismantle the arrears.

## **EXTERNAL DEBT**

32. Mr. Speaker, in 2006, Zambia benefited from additional external debt relief, which led to a significant

reduction in the debt stock. The relief was granted largely by the International Monetary Fund (IMF), the World Bank and the African Development Bank (AfDB) under the Multilateral Debt Relief Initiative (MDRI). Preliminary information indicates that the country's external debt stock stood at US \$635 million as at end of December 2006, a reduction of 86.7 percent from the end of 2005 stock of US \$4.5 billion. This year foreign debt service will be US \$33.9 million against the pre-HIPC and pre-MDRI figure of US \$373.2 million in 2004. Zambia is therefore no more a Heavily Indebted Poor Country.

33. Sir, this debt relief will generate substantial savings in terms of debt service, which will accrue to the nation over the next 20 years. These savings will be available to finance both private and public development programmes, thereby advancing towards the realisation of the Millennium Development Goals.

#### **EXTERNAL SECTOR DEVELOPMENTS**

34. Mr. Speaker, in 2006, the country's external sector continued to record significant improvements, with the trade balance recording a surplus of US \$1,176 million compared to a surplus of US \$10 million in 2005. The improvement in external sector performance was on account of a sharp increase in export earnings relative to imports.

35. Sir, total export earnings grew by 77.3 percent to US \$3.9 billion in 2006 from US \$2.2 billion in 2005. This was mainly on account of an increase in the international price of copper to record levels, coupled with the growth in copper export volumes. Export earnings were further enhanced by the 29.3 percent growth in non-

traditional export earnings to US \$754.9 million from US \$576.7 million. This was induced by the favourable economic environment and export promotion efforts.

36. Mr. Speaker, while exports grew sharply in 2006, imports only increased by 22.7 percent to US \$2.7 billion from US \$2.2 billion in 2005. The rise in imports was mainly due to continued investment and expansionary activity in the mining sector.

37. Mr. Speaker, the current account deficit was financed by external capital inflows in the form of foreign direct investment amounting to US \$338 million, project grants of US \$293 million and portfolio inflows of US \$148.6 million. Increased external capital inflows arose largely from the growing investor and donor confidence following the improvement in Zambia's overall macroeconomic performance.

#### **MONETARY AND FINANCIAL SECTOR DEVELOPMENTS**

38. Mr. Speaker, the end-year consumer price inflation reduced to 8.2 percent from 15.9 percent achieved in 2005 and was well below the target of 10 percent set for 2006. This outturn was a milestone as it was the lowest inflation rate achieved in more than three decades. This occurred against a backdrop of the persistent rise in oil prices on the world market and rapid growth in money supply. These inflationary pressures were mitigated, to a large extent, by stable food prices due to the bumper maize harvest.

39. Mr. Speaker, the rapid build-up of foreign reserves and the higher than programmed external budget support led to the injection of excess liquidity

in the economy. This caused a challenge in the conduct of monetary policy by the Bank of Zambia. To contain this liquidity, the Bank of Zambia intensified its open market operations, which were augmented by the sale of Government securities. In addition, the Government converted part of its non-marketable liabilities to the Bank into marketable Treasury bills and bonds to be used in open market operations.

40. Mr. Speaker, in 2006, the composite weighted average yield rate on Treasury bills and Government bonds declined. The average Treasury bills yield rate declined from 16.7 percent to 9.8 percent while the composite Government bond yield rate declined from 23 percent to 12.6 percent. Falling inflation and the continued high demand for Government securities by both local and foreign investors explain this drop in yields.

41. Sir, in line with lower inflation and yields on Government securities, the average commercial banks' lending rate further declined to 27.9 percent in December 2006 from 33.9 percent in December 2005. Although interest rates are falling, the current levels are still too high. Commercial banks should, therefore, further reduce their interest rates in line with inflation and other macroeconomic developments.

42. Sir, the foreign exchange market was characterized by general depreciation of the Kwacha against major currencies with intermittent volatility. In order to moderate the volatility and maintain stability in the value of the Kwacha, the Bank of Zambia intervened by way of purchasing and selling foreign exchange in the market. Overall, the average inter-bank mid-exchange rate

depreciated by 20.5 percent from K3,428 per US dollar in December 2005 to K4,132 per US dollar in December 2006.

#### **CAPITAL MARKET DEVELOPMENTS**

43. Mr. Speaker, capital markets continued to perform well. This is evidenced by growth in the market capitalisation of 52 percent compared to 11 percent in 2005 to end the year at K13 trillion or US \$3.2 billion. As a share of GDP, market capitalisation was 33.7 percent. In addition, the number of listed companies increased to 15 in 2006 from 13 in 2005.

44. Sir, there was a significant improvement in foreign portfolio investment in 2006. The net portfolio investment position improved by 49 percent from US \$5.3 million in 2005 to US \$7.9 million in 2006. This improvement was due to favourable economic environment coupled with good publicity and visibility that the Lusaka Stock Exchange has enjoyed from publications such as the Standard and Poors' World Stock Exchange Handbook.

#### **FOREIGN FINANCING**

45. Mr. Speaker, in 2006, a total of US \$560.5 million was received as foreign financing. Of this amount, US \$155.5 million was disbursed as direct budget support. This amount was US \$29.9 million higher than the programmed budget of US \$125.6 million. With regard to project support, preliminary data indicate that US \$405 million was disbursed compared to US \$423 million disbursed in 2005.

46. Sir, may I, on behalf of the Zambian people and, indeed on my own behalf, take this opportunity to thank our cooperating partners for

continuing to support our social and economic development agenda. This, once again, underscores the confidence that our cooperating partners have in this Government in implementing national programmes.

47. Sir, notwithstanding the current support, the 2006-2010 FNDP has an estimated financing gap of K2,982 billion over the Plan period. This mainly comes from the priority sectors of agriculture, education and skills development and health. In order for my Government to meet the objectives outlined in the priority sectors including the theme of this budget, I wish to appeal to our cooperating partners to scale-up support in line with the Joint Assistance Strategy for Zambia.

#### **SOCIAL SECTOR DEVELOPMENTS**

##### ***EDUCATION***

48. Mr. Speaker, in line with the Government's commitment to improve service delivery in the education sector 7,100 new teachers were recruited in 2006 with the majority placed in rural areas. In addition, the Government made significant progress in infrastructure development by constructing 46 Portal Frame schools with a total of 250 classrooms. Other school infrastructure such as classrooms, teachers' houses, laboratories and water reticulation systems were rehabilitated.

49. Sir, preliminary data indicate that pupil enrolment in basic schools increased by 13.1 percent to 2,848,357 in 2006 from 2,519,141 pupils in 2005. The net enrolment ratio for girls was marginally lower than that of boys in all the provinces. However, the completion rates at basic school level

increased from 11.4 percent in 2003 to 17.7 percent in 2006 for girls and 17.4 percent to 20.1 percent for boys.

##### ***HEALTH***

50. Mr. Speaker, the Government has remained committed to providing quality health services. In this respect, a total of 744 front line medical personnel were recruited, 20 health posts were completed out of 53 that were under construction and the procurement of medical equipment and drugs continued as planned. In addition, the Government commenced the construction of 20 health centres and 5 district hospitals at Chadiza, Mumbwa, Kapiri Mposhi, Samfya and Shang'ombo.

##### ***HIV/AIDS***

51. Mr. Speaker, the Government in 2006 made considerable progress in the implementation of the free Anti Retro Viral (ARV) policy. In this regard, over 75,000 Zambians are on free ARV drugs. In addition, the public sector workplace programme has reached 17,290 employees while the civil society and private sector have increasingly been participating in HIV/AIDS activities.

52. Sir, in order to increase awareness and mitigate the impact of HIV/AIDS on the affected households, the Government intensified Voluntary Counselling and Testing (VCT) services. In this respect, the number of VCT sites increased from 450 in 2005 to 600 in 2006. In addition, the Government scaled-up services in the prevention of mother-to-child transmission of HIV by covering all the districts.

## **STRUCTURAL REFORMS**

53. Mr. Speaker, the implementation of the Financial Sector Development Plan (FSDP) continued in 2006. The key milestones achieved were the enactment of the Microfinance Regulations and the granting of a licence to a Credit Reference Bureau agency. The other milestone achieved was the completion of the national survey on the demand and supply of financial services in Zambia covering all the districts. The results of the survey will provide the basis for developing specific products to enhance access to financial services.

## **BUDGET PERFORMANCE IN 2006**

54. Mr. Speaker, performance of the budget in 2006 was characterised by revenue shortfalls, which negatively affected budget execution. Preliminary figures on the total revenue and grants for the year show that receipts amounted to K8,240.9 billion, which was 8.4 percent below the budget estimate.

55. Sir, of the total revenue and grants, domestic revenues amounted to K6,600.7 billion against the target of K6,959.8 billion. This was mainly on account of under collection on domestic Value Added Tax and excise duty. Other tax types were generally on target. Grant receipts amounted to K1,640.1 billion out of which K523.3 billion was direct budget support. Direct Budget Support receipts were above target by 8.5 percent. This reflects the decision by most cooperating partners to increasingly provide programme grants as opposed to project grants as a result of their growing confidence in the Government's fiscal management.

56. Mr. Speaker, on account of shortfalls in revenue, expenditures were below target by 13.3 percent. Total expenditures amounted to K8,618.1 billion against the target of K9,942.4 billion. However, I wish to report that in spite of these limitations, cash releases for poverty reducing programmes were broadly in line with the budget.

57. Mr. Speaker, current expenditures accounted for 85.1 percent while the balance of 14.9 percent was absorbed by capital expenditures. Domestically financed expenditure for poverty reducing programmes amounted to K2,347.8 billion, representing 92 percent of the targeted amount of K2,554 billion. This is a reflection of the Governments' commitment to reducing poverty and uplifting the standard of living of our people.

58. Mr. Speaker, with regard to domestically financed expenditure on various functions of Government, preliminary data indicate that budgetary expenditure for general public services stood at K2,655.4 billion against the target of K3,860.9 billion. This was mainly on account of savings from domestic and external debt service arising from debt relief, lower interest rates and the appreciation of the Kwacha.

59. Sir, expenditure on public order and safety and defence stood at K1,168.2 billion against the budget of K1,042.4 billion and was above target by 10.8 percent. This was necessitated by the need for reinforcement of the security wings in order to conduct peaceful 2006 tripartite elections.

60. Mr. Speaker, expenditure on economic affairs amounted to K784.3 billion against the target of K916



billion and was below by 14.4 percent while environmental protection expenditure fell below target by 41.7 percent. Expenditure on road infrastructure of K505.5 billion was below the target of K882.0 billion. However, expenditure in agriculture was above target by K17.2 billion. Among the key programmes were the Fertilizer Support Programme and the Strategic Food Reserves. Expenditure on the Fertilizer Support Programme was K193.1 billion against the target of K198.8 billion while expenditure on Strategic Food Reserves was K140.0 billion against the target of K50 billion.

61. Sir, by the end of 2006, 98.6 percent of the budget allocation for social sector spending had been released. Total disbursements to this sector amounted to K2,042.7 billion against the target of K2,071.5 billion, reflecting Governments' commitment to improving service delivery.

62. Mr. Speaker, a total of K603.1 billion was released to the health sub-sector against the target of K570.3 billion and was 5.8 percent above target. This was mainly for the recruitment of additional front line medical personnel, purchase of drugs and medical equipment and infrastructure development and rehabilitation.

63. Sir, disbursements to the education and training sub-sector amounted to K1,269.6 billion. This represents 96.5 percent of the budget allocated to this sub-sector. These resources were mainly for the recruitment of additional teachers. Other key areas of intervention were the procurement of educational material and rehabilitation and building of school and college

infrastructure, including teachers' houses in the rural areas.

### **PART III**

## **ECONOMIC AND SOCIAL POLICIES FOR 2007**

### **MACROECONOMIC POLICIES FOR 2007**

64. Mr. Speaker, His Excellency the President, recently launched the Fifth National Development Plan (FNDP) 2006-2010 and Vision 2030 as the beacons for the country's future development efforts. The Plan outlines the country's policy interventions, strategies and programmes. The principal objective of the Plan is to accelerate economic growth so as to create jobs and broad based wealth. In this regard, the macroeconomic policies in 2007 have been set within this overall goal of the Plan. The Government will, therefore, align public expenditures with the objectives and priorities of the FNDP. Further, the Government will continue to focus on consolidating the macroeconomic achievements of the last five years.

65. Sir, Government's macroeconomic objectives for 2007 are to:

- (a) achieve a real GDP growth rate of 7 percent;
- (b) reduce inflation to 5 percent;
- (c) reduce the Government domestic borrowing to 1.2 percent of GDP; and
- (d) raise gross international reserves to at least 2.5 months of import cover.

66. Sir, economic growth in 2007 will be predominantly driven by private sector investments in the key

sectors of agriculture, mining, manufacturing, construction and tourism. The Government will support growth by accelerating the implementation of structural reforms and investing in key infrastructure such as roads.

67. Mr. Speaker, at the launch of the FNDP, His Excellency the President implored the private sector to participate in implementing the Plan. The Government, therefore, is committed to facilitating a business and investment climate that will spur private sector development by continuing with the structural reforms.

#### **FISCAL POLICIES**

68. Mr. Speaker, the 2007 budget objectives will continue to focus on contributing to macroeconomic stability, fiscal discipline, directing public resources to priority areas and expanding the revenue base. In this regard, the Government will constrain the domestic borrowing to 1.2 percent of GDP in order to limit the rise in the domestic debt. Limited Government borrowing will also contribute towards reducing inflation and interest rates.

69. Sir, in addition, the Government will continue to exercise strong control on its expenditures by reducing non-priority expenditures. The resources from debt relief provided under the MDRI and the HIPC Initiative will be directed to priority areas of agriculture, health, education and infrastructure in line with the FNDP.

#### **BUDGET EXECUTION**

70. Mr. Speaker, to enhance budget execution in 2007, the Government will strengthen treasury management and expenditure monitoring systems.

My Ministry will take the following actions:

- (e) advise Ministries, Provinces and Spending Agencies (MPSAs) to request for funds as and when they are required;
- (f) inform MPSAs of the resources to be disbursed for them to adequately prepare to implement their respective programmes;
- (g) require all MPSAs to prepare monthly reports on the utilisation of public funds;
- (h) consolidate reports from MPSAs on the utilisation of resources and disseminate them to the general public;
- (i) publish the release of resources by the Treasury to developmental programmes on a quarterly and in certain cases, monthly basis; and
- (j) undertake periodic and detailed public expenditure reviews.

71. Sir, these actions will widen stakeholder involvement in budget implementation and give an opportunity to all stakeholders to be fully involved in the monitoring and evaluation of programmes.

72. Further, Mr. Speaker, the new Division for Planning and Economic Management that was created in my Ministry will, among other functions, play a pivotal role in the monitoring and evaluation of project and programme implementation.

#### **MONETARY AND FINANCIAL SECTOR POLICIES**

73. Mr. Speaker, the Bank of Zambia will continue to pursue appropriate monetary policy in order to

achieve the inflation target of 5.0 percent. This will be complemented by prudent fiscal policy.

74. Sir, the Government remains committed to a flexible exchange rate regime. In this regard, the Bank of Zambia will confine interventions in the foreign exchange market to smoothening fluctuations and building up international reserves.

75. Sir, in order to ensure that commercial banks are adequately capitalised and enhance financial stability, the Bank of Zambia increased the minimum primary paid-up capital for commercial banks in December 2006 from K2 billion to K12 billion. This measure took effect in January 2007 and affects all commercial banks.

76. Mr. Speaker, in the same vein, the start-up capital for the deposit taking leasing institutions was increased to K1.5 billion from K250 million while that of development finance institutions is now K7.5 billion.

#### **DEBT AND AID POLICIES**

77. Mr. Speaker, following the significant reduction of external debt due to debt relief, the Government will focus on maintaining debt sustainability. In this regard, the strategy will be to rely on foreign grants to support development programmes and where such grants are not sufficient, concessional loans will be sought.

78. Sir, the Government policy on domestic debt is to maintain it to sustainable levels. To achieve this, the Government will reduce domestic borrowing, curtail the accumulation of new debt and clear the existing arrears in a phased approach.

#### **KEY SECTOR POLICIES AND INTERVENTIONS**

##### ***AGRICULTURE***

79. Mr. Speaker, in 2007, the Government policy will focus on increased investment in agriculture particularly irrigation development, livestock disease control, farm mechanisation and extension services.

##### ***MINING***

80. Mr. Speaker, in 2007, the Government will continue to promote both large and small-scale mining by providing a conducive business environment, up-dating current legislation and providing more geological information to allow for extensive exploration work.

81. Sir, for small-scale mining, the Government will provide support to this sector given its potential in employment creation and poverty reduction. In this regard, through the use of the mining revolving fund, small scale miners will continue to be assisted with funds for, among other things, hire of plant and equipment.

82. Mr. Speaker, on the regulatory and legal front, the Government will, this year revise the Mine Health and Safety Policy. This is in order to ensure a safe and healthy working environment to minimise the incidence of accidents in the mines.

##### ***MANUFACTURING***

83. Mr. Speaker, the manufacturing sector continues to be one of the priority growth sectors in the country. This is because it provides forward and backward linkages with other sectors such as agriculture, fisheries, livestock, mining and forestry. In this regard, the

Government will continue to provide incentives to unlock the potential of this sector in order to promote value-addition.

### ***ENERGY***

84. Mr. Speaker, the Government sees energy as a critical element for accelerated economic growth. In this regard, the Government will ensure that the sector's performance is able to meet the growing demand for energy.

85. Sir, it has been projected that by 2008, demand for electricity will outstrip current supply if generation capacity is not increased. In this regard, the Government will continue with the rehabilitation and the refurbishment of Hydro Power Stations and rehabilitation of transmission and distribution systems.

86. In addition, the Government is promoting the construction of new hydro power stations through public-private partnerships. We, therefore, welcome the signing of a pact between Zesco Limited and Tata Africa Holdings for the construction of a US \$150 million hydro power station at Itezhi-tezhi. The project is expected to generate about 120 mega-watts of power once completed.

87. Mr. Speaker, in the petroleum sub-sector, the Government seeks to ensure adequate supply of petroleum products. To this effect, the Government has put in place measures to build strategic reserves and recapitalise Indeni Oil Refinery for it to operate efficiently.

88. Sir, the Government has constituted a Ministerial Committee to spearhead the process of carrying out exploration work on petroleum oil and gas in the North Western Province.

This follows the positive indication arising from tests that were carried out some time back. The Committee will, during the course of the year, intensify its work so that interested companies can be invited to carry out further drilling and exploration works.

### **SOCIAL SECTOR**

89. Mr. Speaker, in the social sector, focus will be on improving the provision of public services in the areas of health, education and water and sanitation. In the health and education sub-sectors, this will be done through recruitment and retention of teachers and front line medical personnel as well as investment in infrastructure and procurement of educational materials. In the water and sanitation sub-sector, the Government will improve access to safe drinking water and basic sanitation in most of the rural, urban and peri-urban areas.

### **HIV AND AIDS**

90. Mr. Speaker, the HIV and AIDS pandemic sadly continues to affect the productive age group leaving a generation of orphans and vulnerable children, widows and widowers. The pandemic also continues to reverse the gains in human development that have been made in the past years and complicates the delivery of services in the country.

91. Sir, in 2007, the Government will continue to focus on a multi-sectoral response, improved service delivery and support research into the cure for AIDS which also includes the use of traditional remedies.

### **STRUCTURAL REFORMS**

92. Mr. Speaker, structural reforms will continue with the implementation

of the Public Expenditure Management and Financial Accountability (PEMFA) reforms, Public Service Management (PSM), Decentralisation, Private Sector Development (PSD) and Financial Sector Development Plan (FSDP). Under PEMFA reforms, the focus, in 2007, will be on enhancing compliance with internal controls and strengthening the capacity of institutions of good governance such as the National Assembly, Office of the Auditor General and Zambia National Tender Board. The key components on enhancing internal controls are the commitment control systems, enhanced financial management systems and Integrated Financial Management and Information Systems (IFMIS).

93. Sir, with regard to PSM, the focus will continue to be on rightsizing, pay reforms, service delivery improvement, payroll management and establishment control. In the area of PSD, the Government will speed up the process of improving business facilitation and economic diversification. In addition, the Government will establish Patents and Companies Registration Offices in Eastern, Southern and Copperbelt provinces. Similarly, the focus under the FSDP will be to continue with the process of expanding financial intermediation and access to financial services in all the districts.

94. Mr. Speaker, with the launch of the Decentralisation Policy in 2004, the Government has continued to progress towards the devolution of functions to the local levels. With this devolution, certain functions in some ministries will move to the district level by the end of 2007. Sir, an intergovernmental fiscal transfer system, through which funds shall be transferred to the district councils, has

been designed. To this effect, this budget has provided for the restructuring, recurrent and capital grants to assist district councils achieve solvency, fund retrenchments and ensure that they do not get back into the debt trap. The Government intends to continue with the decentralisation sensitization process to ensure that each and every Zambian is not left behind in this important national process.

95. Sir, following the enactment of the Zambia Development Agency (ZDA) Act, the Government operationalised the ZDA in January 2007. The ZDA will, among other things, address the high cost of doing business in Zambia. It is expected that the processing of various business formalities such as licensing would be simplified.

96. Mr. Speaker, the Government is establishing Multi-Facility Economic Zones (MFEZ) in order to diversify the economy and promote exports. I wish to report to this august House that two locations in Lusaka and Chambishi on the Copperbelt have been identified. The Japanese Government through the Japanese International Development Agency (JICA) has since engaged a Malaysian company, Kulim High Technology Park Corporation, to develop the Lusaka MFEZ. The Chambishi one will be developed by the Chinese and is poised to attract 50 enterprises with an estimated investment of US \$800 million over the next four years. In these zones, the Government will offer incentives to both Zambian and foreign firms in order to promote manufacturing and stimulate export activities, technological development, skills transfer and job creation.

**PART IV**  
**THE 2007 BUDGET**

97. Sir, before I get into the details of the 2007 budget, I wish to remind this august House that the resources available are limited. This calls for prudence in the allocation of resources to priority areas. Among the challenges in resource allocation is the need to avoid spreading resources too thinly across districts or programmes if impact has to be felt. In this vein, we need to complete on-going programmes before embarking on new ones and preserving the assets we already have. This, therefore, calls for boldness in allocation of resources to only few programmes.

98. Mr. Speaker, the Government proposes a budget of K12,042.4 billion or 26.6 percent of the GDP projected at K45,282 billion in 2007. Of this budget, K8,668.1 billion or 72 percent will be financed by domestic resources while the balance of K3,374 billion or 28 percent will be from external sources.

**EXPENDITURE MEASURES**

99. Sir, of the total budget, K9,053.3 billion or 75.2 percent will be spent on current expenditures while K2,117.5 billion or 18.1 percent will go towards capital expenditures. With regard to Constitutional and Statutory expenditures, K811.6 billion or 6.7 percent of the budget is being proposed, a major component of which is debt service.

100. Mr. Speaker, with regard to current expenditures, the Government has allocated K3,496.2 billion or 29 percent of the budget for personal emoluments and K3,042.5 billion or 25.3 percent of the budget for recurrent

departmental charges. A further K2,259.5 billion or 18.8 percent of the budget has been provided for Grants and other payments.

101. Sir, of the total allocation towards capital expenditures, K1,086 billion will be financed from the domestic resources while K1,091.5 billion will be financed from external sources. Of the total amount on domestically financed expenditure, K216 billion has been allocated for Financial Restructuring and K111.1 billion for enterprise development funds.

<b>Proposed Budget By Economic Classification</b>		
	<b>K' Bn</b>	<b>% of Total Budget</b>
<b>CURRENT EXPENDITURES</b>	<b>9,053.3</b>	<b>75.2</b>
<b>Personal Emoluments</b>	<b>3,496.2</b>	<b>29.0</b>
<b>Public Service Reform Programme</b>	<b>102.7</b>	<b>0.9</b>
<b>Recurrent Departmental Charges</b>	<b>3,042.5</b>	<b>25.3</b>
o/w Constitutional Review Process	202.6	1.7
Arrears	151.1	1.3
<b>Grants and Other Payments</b>	<b>2,056.9</b>	<b>17.1</b>
o/w Public Service Pensions Fund	266.0	2.2
Zambia Revenue Authority	197.0	1.6
Education	436.6	3.6
Health	326.6	2.7
<b>Fertilizer Support Programme</b>	<b>150.0</b>	<b>1.2</b>
<b>Strategic Food Reserve</b>	<b>205.0</b>	<b>1.7</b>
<b>CAPITAL EXPENDITURES</b>	<b>2,177.5</b>	<b>18.1</b>
Domestically Financed	1,086.0	9.0
o/w Roads	365.6	3.0
Financial Restructuring	216.3	1.8
Development Funds	111.1	0.9
Foreign Financed	1,091.5	9.1
<b>CONSTITUTIONAL AND STATUTORY EXPENDITURE</b>	<b>811.6</b>	<b>6.7</b>
Domestic Debt Interest	656.6	5.4
Foreign Debt (Interest and Amortisation)	129.3	1.1
Constitutional Posts	25.8	0.2
<b>TOTAL</b>	<b>12,042.4</b>	<b>100.0</b>

102. Mr. Speaker, in respect to constitutional and statutory expenditures, K656 billion has been allocated to interest payment on government securities, K129 billion for external debt servicing and K25.8 billion for constitutional posts.

#### EXPENDITURE BY FUNCTION

103. Mr. Speaker, let me now give an analysis of the expenditure by

function. This expresses the broad social and economic objectives that the Government aims to achieve through the various types of expenditure across all heads. Under this classification, a function groups all expenditures directly related to that function regardless of which Ministry, Province or Spending Agency is carrying out the activity.

BUDGET BY FUNCTION	2006		2007	
	Allocation (K' Billion)	% of Total Budget	Allocation (K' Billion)	% of Total Budget
<b>General Public Services</b>	<b>4,188.9</b>	<b>40.9</b>	<b>4,022.9</b>	<b>33.4</b>
<i>o/w General Government Services</i>	2,876.7	28.1	2,557.3	21.2
<i>o/w Debt and Investments</i>	1,380.9	13.5	<b>1,267.3</b>	10.5
<b>Defence</b>	<b>654.9</b>	<b>6.4</b>	<b>798.2</b>	<b>6.6</b>
<b>Public Order and Safety</b>	<b>391.7</b>	<b>3.8</b>	<b>451.9</b>	<b>3.8</b>
<b>Economic Affairs</b>	<b>1,844.8</b>	<b>18.0</b>	<b>2,326.2</b>	<b>19.3</b>
<i>o/w Agriculture &amp; Fishing</i>	580.0	5.7	1,062.9	8.8
<i>Transport (Roads, Rail, Air)</i>	904.5	8.8	920.0	7.6
<b>Environmental Protection</b>	<b>43.3</b>	<b>0.4</b>	<b>103.3</b>	<b>0.9</b>
<b>Housing and Community Amenities</b>	<b>292.0</b>	<b>2.9</b>	<b>787.4</b>	<b>6.5</b>
<b>Health</b>	<b>1,098.4</b>	<b>10.7</b>	<b>1,294.0</b>	<b>10.7</b>
<b>Recreation, Culture &amp; Religion</b>	<b>29.7</b>	<b>0.3</b>	<b>106.7</b>	<b>0.9</b>
<b>Education</b>	<b>1,647.4</b>	<b>16.1</b>	<b>1,808.4</b>	<b>15.0</b>
<b>Social Protection</b>	<b>45.7</b>	<b>0.4</b>	<b>343.5</b>	<b>2.9</b>
<b>TOTAL</b>	<b>10,236.8</b>	<b>100.0</b>	<b>12,042.4</b>	<b>100.0</b>

Source: Ministry of Finance and National Planning

#### GENERAL PUBLIC SERVICES

104. Mr. Speaker, the Government proposes to allocate K4,022.9 billion or 33.4 percent of the budget for General Public Services, which is a decline of 7.5 percentage points from the 2006 budget of 40.9 percent. This is in line with the Government's policy to direct more resources to poverty reduction programmes. Of this amount, 63.6 percent has been provided for general government services, 17.3 percent for centralised government services and the remainder to cater for executive and legislative government functions.

105. Sir, the Government has provided K2,557.3 billion or 21.4 percent of the budget for general government services. A key element of this function is debt and investments management whose allocation is K1,267.3 billion or 11 percent. Of this amount, K656.6 billion will cater for interest payments on Treasury bills and bonds and K449.5 billion is for arrears owed to suppliers of goods and services, road contractors and utility providers. An amount of K129.3 billion or 1.1 percent of the budget compared to K378 billion or 3.7 percent

of the budget in 2006 will go towards payment of external debt. This shows a significant reduction from the previous years and is indeed a true reflection of the positive effects of debt relief received under the HIPC initiatives and MDRI.

106. Mr. Speaker, the Government has allocated K318.1 billion to the executive function which includes the local government administration at 32 percent of the allocation. Sir, the Government intends to speed up the implementation of the decentralization policy through rationalisation of expenditure between central Government and local Government and transfer of resources from Central Government to local authorities. As a first step to the process, K102.7 billion has been provided in this year's budget. This includes a recurrent grant amount of K50 billion, K25 billion for restructuring grant, K17.7 billion for grants in lieu of rates and K10 billion for conditional capital grants.

107. Sir, the Government will continue with the constitutional review process in 2007. In this regard, K202.6 billion has been allocated for this process.

#### **ECONOMIC AFFAIRS**

108. Sir, the Government proposes to spend K2,236.2 billion or 19.3 percent of the budget to the Economic Affairs function. Of this amount, 45.7 percent has been allocated to the Agriculture and Fishing sub-function, 39.6 percent to the Transport sub-function and the rest to tourism, fuel and energy, mining and communication sub-functions.

#### ***AGRICULTURE AND FISHING***

109. Mr. Speaker, the Government proposes to spend K1,062.9 billion or

8.8 percent of the budget on the Agriculture and Fishing sub-function. Of this amount, K205 billion is for the Strategic Food Reserve Programme to facilitate purchase of maize and other crops. In addition, K150 billion is for the Fertilizer Support Programme for the 2007/2008 agricultural season. Other areas of intervention include K37 billion for Irrigation Development, K20 billion for Agriculture Infrastructure Development and K47.5 billion for Livestock Development. Further, provisions have been made of K40 billion for agriculture services and technological development and K25.7 billion for fisheries development.

#### ***TRANSPORT (ROAD, RAIL, AIR AND WATER)***

110. Sir, in the transport sub-function, the Government proposes to allocate K920 billion or 7.6 percent of the budget. An amount of K787 billion has been directed to road infrastructure development, rehabilitation and maintenance. Of this amount, K204 billion has been set aside for district roads, K156.1 billion for trunk roads, K111.5 billion for construction and rehabilitation of bridges, K107.7 billion for urban roads, K63.6 billion for feeder roads, K106.8 billion for main roads and K7.3 billion for road authorities enforcement and the rest for various road activities. In addition, the Government proposes to spend K11.4 billion for the rehabilitation of airports, which includes K8.5 billion for the extension of the runway at Livingstone International Airport. A further amount of K8.7 billion has been set aside for construction of the Chipata-Mchinji railway.

#### **SOCIAL SECTOR**

111. Sir, in line with the theme of this budget, the Government proposes



to spend K3,552.6 billion or 36 percent of the budget in the social sector. Of these resources, 41.7 percent is for education, 29.8 percent for health, 18.1 percent for housing and community amenities while the remainder is for culture, social protection and recreation.

### ***EDUCATION***

112. Mr. Speaker, the Government has allocated K1,808.4 billion or 15 percent of the budget to this function. The key programmes to be implemented include recruitment of an additional 4,000 teachers, rehabilitation and construction of basic schools and rural teachers' housing as well as purchase of school requisites.

113. Sir, in addition, K187.2 billion or 10.4 percent of the allocation has been provided for early childhood development and basic education, K62.5 billion for high schools, K292.6 billion for tertiary education out of which K130.9 billion is for technical and skills training.

### ***HEALTH***

114. Mr. Speaker, the Government proposes to allocate K1,294 billion or 10.8 percent of the budget in the health sector. Of this amount, K1,036.8 billion is for public health services whose key programmes include primary health care, secondary health care, community health care and HIV/AIDS including prevention of mother-to-child transmission. In addition, the Government will recruit an additional 1,900 front line medical personnel to help reduce the shortage of health workers and enhance service delivery.

### ***HOUSING AND COMMUNITY AMENITIES***

115. Sir, the Government has allocated K787.4 billion or 6.5 percent of the budget to the housing and community amenities sector. Out of this, K334.1 billion is earmarked for water supply and sanitation programmes, which will include provision of boreholes, water wells in rural, urban and peri-urban areas. In addition, K23.1 billion has been allocated for housing development while K15.3 billion has been allocated to community development.

### ***SOCIAL PROTECTION***

116. Mr. Speaker, the Government proposes to spend K343.5 billion or 2.9 percent of the budget on social protection. This includes K266 billion for grant payments to the pension fund and for dismantling of pension arrears. The remainder has been directed to other social programmes such as the Public Welfare Assistance Scheme (PWAS), street children activities and youth development programmes.

### ***PUBLIC ORDER AND SAFETY***

117. Mr. Speaker, the Government proposes to spend K451.9 billion or 3.8 percent of the budget toward Public Order and Safety. Of this amount, K344.2 billion or 71 percent has been provided for police services. Sir, it is the intention of this Government to improve the accommodation for the police service and as such, K30 billion has been set aside for this purpose. Other allocations include K58.5 billion for prisons, K45.9 billion for immigration, passport and registration and the remainder for the law courts and fire services.

### ***ENVIRONMENTAL PROTECTION***

118. Sir, the Government proposes to allocate K103.3 billion to the

Environmental protection function. Of this amount, K24.9 billion has been allocated for pollution abatement, K10 billion for waste management while K43.9 billion is for other environmental protection activities.

## REVENUE ESTIMATES AND MEASURES

119. Mr. Speaker, you will recall that during the official opening of the first session of the Tenth National Assembly in October 2006, His Excellency the President, Mr. Levy Patrick Mwanawasa, State Counsel, indicated that the concerns regarding high taxation would be considered in the 2007 Budget. However, in coming up with tax measures for 2007, the Government had to carefully balance the demand for tax relief and the dictates of national developmental programmes.

120. Sir, the Government expects to raise a total of K12,042.4 billion. Out of this amount, K8,125 billion or 67.5 percent will be generated locally while K3,374 billion or 28 percent will be sourced externally. The balance of K543.4 billion or 4.5 percent will constitute domestic borrowing.

121. Mr Speaker, the summary of the estimates of revenue and financing to support this year's expenditures is as follows:

	(K' billion)	
<b>TOTAL TAX REVENUES</b>		<b>7,807.4</b>
<b>Direct Taxes</b>	<b>3,440.1</b>	
Company Income Tax	935.1	
Pay As You Earn	2,088.3	
Withholding and other income taxes	339.3	
Mineral Royalty Tax	77.3	
<b>Excise Taxes</b>	<b>1,103.8</b>	
Fuel Levy	220.8	
Other Excise	883.0	
<b>Domestic VAT</b>	<b>669.1</b>	
<b>Trade Taxes</b>	<b>2,594.4</b>	
Import Tariffs	830.0	
Import VAT	1,762.1	
Export Duties	2.3	
<b>NON-TAX REVENUE</b>		<b>317.5</b>
User Fees and Charges	159.2	
Dividends, Interest and Other levies	41.2	
Exceptional Revenue	117.4	
<b>DOMESTIC BORROWING</b>		<b>543.4</b>
<b>TOTAL DOMESTIC REVENUE AND FINANCING</b>		<b>8,668.1</b>
<b>Total Foreign grants and loans</b>		<b>3,374.0</b>
<b>GRANTS</b>	<b>2,257.1</b>	
General Budget Support	630.2	
Project Grants	1,016.0	
Swaps to Education and Health	411.8	
MDRI Resources	199.1	
<b>FOREIGN FINANCING</b>	<b>1,116.9</b>	
Project Loans	826.3	
Programme Loans	290.5	
<b>TOTAL REVENUE AND FINANCING</b>		<b>12,042.4</b>

Source: Ministry of Finance and National Planning

## REVENUE MEASURES

### *DIRECT TAXES*

122. Mr Speaker, there are concerns that disposable income for workers in formal employment is low because of high Pay As You Earn (PAYE). To address these concerns, the Government proposes to adjust the PAYE regime to provide for the minimum tax exempt income of K500,000 per month from the current K320,000 per month. This is an increase of 56 percent. In addition, the Government proposes to reduce the

top PAYE tax rate from 37.5 percent to 35 percent while the lower positive rate has been reduced from 30 percent to 25 percent. The following shall be the proposed PAYE regime:

<b>Existing System</b>	
<b>Income Bands</b>	<b>Rate %</b>
0 - K320,000 per month	0
K320,001 – K1,142,000 per month	30
K1,142,001 – K5,706,000per month	35
Above K5,706,000 per month	37.5

<b>Proposed System</b>	
<b>Income Bands</b>	<b>Rate %</b>
0 - K500,000 per month	0
K500,001 – K1,200,000 per month	25
K1,200,001 – K5,200,000 per month	30
Above K5,200,000 per month	35

123. Sir, the above adjustment will give more disposable or take home income to the workers and make the Personal Income Tax more progressive. The estimated revenue loss arising from this measure is K211.7 billion, which will now be available for spending by the workers.

124. Sir, the Government also proposes to increase the tax credit applicable to persons with disabilities from K36,000 to K72,000 per annum. The measure will result in a revenue loss of K1 billion.

125. Mr Speaker, in order to ensure that workers have sufficient resources at the end of their active employment, the Government proposes to increase the exempt portion of terminal benefits from the current K10 million to K20 million. The 100 percent adjustment will result in an estimated revenue loss of K4.1 billion.

126. Mr. Speaker, the Government proposes to increase the allowable pension contribution amount from K15,000 to K60,000 per month in order to give relief on pension contribution. The measure will result in an estimated revenue loss of K7 billion.

127. Mr. Speaker, currently, if a person has income from emoluments, this is taxed under PAYE. However, if the same person also earns business income, the business income is added to the emoluments and taxed under the PAYE regime. This has resulted in some tax payers, particularly individuals who are in employment and are also engaged in business not declaring their business income in order to avoid being taxed at the higher rate of PAYE.

128. Sir, the Government, therefore, proposes to amend the law to allow individuals who are earning both business income and emoluments to have the two incomes taxed separately. That is, the business income will be taxed under turnover tax while the emoluments will be taxed under PAYE. The measure is aimed at encouraging declaration of any business incomes earned by small scale entrepreneurs who may also be earning personal emoluments.

129. Mr Speaker, the mining sector continues to be the anchor of our economy. At the time when copper prices on the international market were low, mining companies were offered tax concessions in order to make their projects viable. Now that the prices are high, there is need to review these concessions so that the nation can benefit from increased earnings from the mining companies. In this regard, the Government proposes a revision of the tax regime as follows:

- (a) increase company income tax for the mining sector from 25 to 30 percent;
- (b) increase mineral royalty from 0.6 percent to 3 percent of gross value for base metals and from 2 percent to 3 percent for precious metals; and
- (c) re-introduce withholding tax on dividends, interest, royalties, management fees and payments to affiliates or subcontractors in the mining sector at the standard rate of 15 percent.

130. Sir, the Government will engage mining companies with development agreements into negotiations so that there is mutual consent by contracting parties to revise the tax regime to the new rates.

131. Mr. Speaker, financing investment by equity is very difficult and, therefore, many companies rely on financing a significant proportion of their investments by loans. It has been observed that the current debt equity ratio of 2 to 1 is very restrictive by international standards. Mining companies requiring large resources for investment in Zambia have been affected by this restriction. The Government, therefore, proposes to relax the restriction for mining companies on the choice between equity and debt in financing their investments under the Thin Capitalisation rule from 2 to 1 to 3 to 1.

132. Mr. Speaker, the Government proposes to amend the law so that the 15 percent withholding tax currently paid by companies on interest earned on Government Bonds should not be final. The interest earned on Government bonds will now be taxed at the applicable corporate tax rate. This measure will not only broaden the tax

base but also align the treatment of interest earned on government instruments with other types of interest, such as interest earned on deposit accounts. The Government expects to raise about K21 billion from this measure.

133. Sir, the Government proposes to introduce a 3 percent advance tax, which will be levied on commercial imports. This measure will help broaden the tax base by capturing business importers who are evading tax. The Government expects to raise K19 billion from this measure.

134. Mr. Speaker, all the above measures will take effect from 1<sup>st</sup> April, 2007.

#### *VALUE ADDED TAX*

135. Mr. Speaker, there have been demands to adjust the level of VAT downwards from the current 17.5 percent. Having carefully considered the proposal, it became evident that the vatable goods and services were still limited in number and any downward adjustment at present would result in a significant loss of revenue. However, once the tax base is broadened, consideration will be made to adjust the rate.

136. Mr. Speaker, currently, interest on a finance lease attracts VAT while that on a loan from a commercial bank does not. In order to introduce consistency in the VAT treatment between a loan and a finance lease, the Government proposes to exempt interest paid on finance leases for VAT purposes.

137. Mr. Speaker, presently, petrol used in business is not allowable as an expense for VAT purposes. The

Government, therefore, proposes that VAT registered suppliers be allowed to claim 20 percent of the input tax paid on petrol to reduce the cost of doing business. The revenue loss as a result of this measure is K8 billion.

138. Mr. Speaker, currently, businesses below the VAT threshold of K200 million are not allowed to register for VAT. This has constrained a number of them from transacting with registered suppliers, thereby impeding their growth. The Government, therefore, proposes to re-introduce voluntary registration for small businesses that will meet the specified requirements.

139. Mr. Speaker, as part of the Government's efforts to broaden the tax base and generate more revenues, the Government proposes to standard-rate magazines. The estimated revenue gain from this measure is K2 billion.

140. Sir, the Government proposes to amend the VAT Act to ease the VAT administration with respect to Minimum Taxable Values (MTVs) by removing the requirement to legislate MTV prices of specified products. The Government also proposes to add talk time and mineral water to the MTV schedule. This measure will secure revenue for Government for products identified to have a long chain of distribution. The revenue gain is estimated at K1 billion.

141. Sir, the above measures will take effect from mid-night tonight.

#### ***CUSTOMS AND EXCISE***

142. Mr. Speaker, in order to reduce the cost of energy, the Government proposes to reduce excise duty on electricity from 5 percent to 3 percent. The 3 percent is being retained for the

Rural Electrification Fund, which is an important tool for ensuring that more of our people have access to electricity. The estimated revenue loss is K10.9 billion.

143. Sir, in order to mitigate the revenue losses arising from the above concessions, the Government proposes to increase excise duty on cigarettes from 115 percent to 145 percent or K90,000 per mille. In addition, the Government proposes to introduce a specific import duty of K15,000 per mille. From these measures, the Government expects to raise K57.5 billion.

144. Mr. Speaker, the Government proposes to increase excise duty on clear beer from 70 percent to 75 percent and on selected motor vehicles by 5 percentage points. The estimated revenue gain from these two measures is K19 billion.

145. Mr. Speaker, the above measures will be effective from mid-night tonight.

#### **CONCESSIONS UNDER THE ZAMBIA DEVELOPMENT AGENCY (ZDA) ACT.**

146. Mr. Speaker, in my 2006 Budget Address, I announced tax measures under the Zambia Development Agency Act. However, these were not incorporated in the tax legislation because the ZDA Act had not been enacted at the time of presenting the Budget. Now that the ZDA is operational, the Government proposes the following incentives to encourage investment:

- (a) Zero percent tax rate on dividends for companies operating in the priority sector and/or MFEZ under the ZDA Act for a period

of five years from the year of first declaration of dividends;

- (b) Zero percent on profits made by companies operating in the priority sector and/or MFEZ for a period of five years from the first year profits are made. For years 6 to 8, only 50 percent of the profits should be taxed and for years 9 and 10, 75 percent of profits should be taxed;
- (c) Zero percent import duty rate on raw materials, capital goods, machinery including trucks and specialized motor vehicles for five years for enterprises operating in the MFEZ; and
- (d) Deferment of VAT on machinery and equipment including trucks and specialized motor vehicles imported for investment in MFEZ and/or priority sector.

#### **OTHER MEASURES UNDER THE MINES AND MINERALS ACT**

147. Mr. Speaker, currently, Section 9 of the Mines and Minerals Act provides that the Development Agreements override any law or regulation. In order to ensure that Development Agreements are subordinate to the law and are binding only to the extent and confines of the law, the Government proposes to make amendments to the Section. The Government also wants to explicitly provide that there shall be no fiscal terms or Tax Schedule provided in the development agreements and that all fiscal matters should be provided for in the respective tax codes and only cross referenced in the development agreement. This is aimed at preventing any attempts to provide or negotiate any fiscal terms outside the tax law.

#### **HOUSEKEEPING MEASURES**

148. Mr. Speaker, the Government proposes to amend the Customs and Excise Act, Income Tax Act, Value Added Tax Act and the Mines and Minerals Act so as to update, strengthen and remove ambiguities in certain sections of these pieces of legislation.

149. Mr. Speaker, in line with the Harmonized Coding and Description System Convention of the World Customs Organization, the Government proposes changes to the customs and excise tariff book in accordance with the 2007 version of the said convention, which under goes revision every five years.

150. These measures are revenue neutral.

### **PART V**

#### **CONCLUSION**

151. Mr. Speaker, the relative macroeconomic stability achieved in the recent years has created the much needed environment conducive for sustained economic growth. For a continuous period of five years, Zambia's economy has maintained an annual growth rate of over 5 percent. To achieve higher growth rates, it is important that the macroeconomic stability is firmly entrenched, consolidated and supplemented by the application of our mental and physical capacities to rearrange and improve our work culture. In launching the Fifth National Development Plan and Vision 2030, we have set ourselves goals for accelerated development of our country. We must now individually commit ourselves to achieving these goals by setting individual targets of our contribution to the realisation of the national goals.

152. Sir, it is for this reason that our macroeconomic policies will continue to focus on empowering individuals to participate in national development. The macroeconomic fundamentals are meant to create space and opportunities for individuals. The Government is there to ensure the observance of individual rights as they go about with their business.

153. Mr. Speaker, in the last two years, we have received substantial debt relief from the international community. The fiscal space that has resulted from the debt relief has made it possible for the Government to start increasing allocations and spending in the priority sectors of education, health and agriculture. This year's budget is also addressing the concerns related to the housing situation for our law enforcement officers.

154. Mr. Speaker, we are providing resources for the restructuring and improvement of operations of the local authorities as an important step forward towards capacitating the key operatives in decentralisation. This year has also marked the resumption of the provision of grants in lieu of rates to our district councils. It is my hope that our local authorities will begin to make some noticeable contribution towards effective service delivery to their communities.

155. Mr. Speaker, we are reforming the tax system with the objective of broadening the tax base, lowering the tax rates and having a transparent and well administered tax system. However I wish to point out that it is only by broadening the tax base that much more relief can be provided to many of the current tax payers, while ensuring increased revenues to the Government to implement important developmental programmes. The Government will this

year continue to make extensive consultations on broadening the tax base, especially with regard to bringing more sectors of the economy into the tax net.

156. Mr. Speaker, we have also taken important steps to address the imbalances with regard to the fiscal regime in the mining sector. The objective of the Government is to have a fiscal regime which ensures that Zambia remains an attractive investment destination while also ensuring that a reasonable share of the mineral revenues accrue to the Zambian people by way of individual incomes and revenues to the Treasury. The reform of the mining fiscal regime will now restore credibility and predictability in the sector, which is essential for sustained investment.

157. Sir, the Government will soon be inviting the holders of existing development agreements to negotiate the fiscal terms in the agreements in line with the new regime. This again is a clear demonstration of the New Deal Administration's commitment to the rule of law and respect of the sanctity of agreements. I therefore call upon the mining companies to embrace these reforms so that we make Zambia a true centre of mining excellence.

158. Mr. Speaker, I now turn to one issue that is of great concern to many stakeholders and indeed to many in the Government. This relates to the implementation of the budget and its impact on the lives of the ordinary people. Sir, there is need to substantially improve upon budget implementation if we are to realize our development goals as outlined in the FNDP.

159. Mr. Speaker, in many instances, it is not the lack of resources that has

affected development outcomes, but rather a lack of efficient and effective implementation of programmes. When the available resources have not been applied judiciously and purposefully, someone has corruptly approved or certified the outcome instead of demanding quality goods and services from the private or Government supplier. This year, we shall place particular attention to ensuring more fiscal and monetary prudence and discipline. The outcome should be better and effective implementation of the development programmes and service delivery. This is in line with the theme of this budget which is, **“From Stability to Improved Service Delivery”**.

160. Sir, Controlling Officers in Government departments play a critical role in the successful implementation of development programmes and delivery of quality public service. The oversight

arrangements for Controlling Officers with regard to budget execution and fiscal prudence will further be strengthened this year to ensure that there is effective implementation and visible outcomes.

161. Mr. Speaker, monitoring of budget implementation should not only be left to those in the Government. All analyses indicate that there is need for changing the mindset of many Zambians by culture remodelling if we are to attain the goals of Vision 2030. All stakeholders, including local communities, NGO’s, business community, and indeed members of this august House, must take up the responsibility of developing the country by supervising Government programmes which use public funds.

162. **Mr. Speaker, I beg to move**