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Article

The dynamics of public debt in Zambia : a critical review

The Dynamics of Public Debt in Zambia: A Critical Review

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Abstract: This paper critically discusses the dynamics of public debt, both domestic and foreign, in Zambia and how it has influenced the economy's growth process over the period from 1964 to 2015. The structural and institutional reforms as well as the legal and public finance administrative frameworks that shaped the level, structure, and composition of public debt stock in Zambia over the review period were highlighted in the paper. Two distinct episodes of public debt were identified. The first phase is from 1980 to 2004, in which public debt surpassed gross domestic product. The second phase is from 2005 to 2015, in which public debt-GDP ratio was on a declining path following the implementation of public debt relief initiatives and a boom in economic activities. Although Zambia's government debt is currently sustainable according to International Monetary Fund/World Bank indicative thresholds, the country, like many other lower middle-income countries, is still experiencing some debt management challenges emanating from weak debt institutional frameworks. The study, therefore, recommends that the government: (1) limits both domestic and foreign borrowing to reduce high interest payments on debt in future; (2) aligns its infrastructure expenditures with domestic revenues to ensure budget sustainability; (3) implements and adheres to cash budgeting system to control fiscal deficits; and (4) expands its domestic revenue base by diversifying the economy and promoting massive industrialisation.

Keywords: Domestic Public Debt; Foreign Public Debt; Zambia

JEL Classification: H52; H62; H63; O11

1. Introduction

In theoretical literature, varying perceptions exist on the nature of the relationship between domestic and foreign public debt and economic growth. First is the view that large public debt is bad, owing to its crushing burden on taxpayers and the need for the government to create new money to service it (Lipsey et al., 1963, p. 389). This view is augmented by the fiscal conservative and classical perspectives of the 18th Century, which support a balanced fiscal budget to avoid inevitable future economic downturns (Blanchard, 2002). The conservatives and classicalists posit that government spending by politicians is mostly wasteful, leading to unrelenting public sector indebtedness and depressed economic growth rates (Hume in Holtfrerich, 2013). Second is the opposing Keynesian perspective, which views domestic and foreign public debt as a critical tool that most governments use to ensure full employment. Third is the Ricardian Equivalence Hypothesis (REH), which supports the nonexistence of an economic relationship between public debt and growth (Barro, 1974; Churchman, 2001). According to the Ricardian school of thought, government debt has no real impact on the optimisation behaviour of the private sector (Barro, 1989).

Empirically, separate studies by De Grauwe (2011) and Ramey and Ramey in Panizza and Presbitero (2013) show that high public debt poses some constraints on national growth by limiting a country's policy space. Nevertheless, Panizza and Presbitero (2012) argue that the correlation between public debt and economic growth does not imply causation. Furthermore, Reinhart and Rogoff (2008) modelled the neutrality of high government debt to gross domestic product (GDP), citing Japan, where the public debt

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to GDP ratio exceeds 150% but is not hampering the country's economic growth process, as an example.

Accordingly, the public debt-growth nexus is more complex than generally perceived and is potentially influenced by innumerable other unobserved factors across countries. The study of the public debt-growth relationship is thus important since it explains the ability of fiscal policy and monetary policy in influencing economic activities. Furthermore, since studies of this nature have not been able to afford satisfactory coverage to Zambia, extending the public debt-growth nexus study to the Zambian economy is indispensable – given the country's debt levels that are continuously growing and the debt composition and structure that is also changing.

Against this background, the objective of this study is to analyse the evolution of the public and publicly guaranteed debt stock in Zambia. The study highlights the debt reforms, trends, and challenges from 1964 to 2015 in Zambia. The rest of the paper is structured as follows: Section 2 discusses public debt reforms in Zambia; Section 3 examines trends in public debt in Zambia; Section 4 discusses the challenges facing public debt management in Zambia; and Section 5 concludes the paper.

2. Public Debt Reforms in Zambia

Between the late 1970s and the mid-1990s, most African economies, Zambia included, embraced a chain of structural adjustment programmes intended to stimulate economic growth through increased investment levels and reduced government overall indebtedness. Nonetheless, economic growth rates remained subdued due to poor investment response, essentially owing to the high investment risks associated with most Africa States (Andersson et al., 2000). Thus, Zambia's profound public indebtedness since the early 1970s originated mainly from natural factors (such as periodic and devastating droughts), declining terms of trade for commodity exports, poor gross investment levels, massive infrastructural developments, public sector financial indiscipline, and increasing social demands. According to Andersson et al., (2000, p. 30), the poor performance of the Zambian economy between 1973 and 2000 caused severe state revenue constraints, forcing the government to rely on seigniorage, domestic and foreign borrowing (mainly non-concessional), and on excessive rundown on export earnings at the country's central bank in order to increase fiscal space. Furthermore, the inability by the country to adequately service foreign public debt led to interest on debt accruals, prompting government debt stock to continue trending upwards in the 1980s, even after new borrowings had ceased (World Bank, 1993, p. 15). Consequently, by 1980, Zambia was in a serious debt crisis, which subsequently led to a series of public debt reforms. Some of the reforms were well designed, while some were not. Overall, public debt reforms in Zambia have centred on improving the legal, institutional, and public financial management frameworks of the country. In 2001, Zambia's cumulative public debt exceeded 235% of gross domestic product (GDP), relative to a public debt/GDP ratio of 44% recorded in 1970 (International Monetary Fund "IMF", 2008; World Bank, 2012).

The sluggish economic growth that characterised the Zambian economy after 1973 compelled the government to implement economic and financial reforms aimed at strengthening budget cycle processes and procedures, with the ultimate goal of curtailing rising public debt levels (Chirwa & Odhiambo, 2016; World Bank, 1993, p. 2). Basically, the debt reforms in Zambia can be put into two distinct periods – 1980 to 2005 and 2006 to 2015. The first category, 1980 to 2005, was characterised by the government's stringent reforms aimed at reducing the debt burden (United Nations Development Programme "UNDP", 2016); while the second category, 2006 to 2015, was associated with reforms that focussed more on maintaining public debt within sustainable levels (Bank of Zambia "BOZ", 2015a).

Between 1988 and 1994, Zambia's average annual domestic revenue was around 17% of GDP, a level which was insufficient to meet the government's recurrent expenditure demands and also inadequate to reduce the country's over-reliance on domestic and foreign borrowing (World Bank, 2007). Thus, the major domestic public debt management reforms undertaken by the government of Zambia in the 1990s were aimed at boosting the revenue capacity of the government and restricting fiscal deficits. These reforms included: (1) adoption of a cash budgeting system; (2) introduction of value-added tax; (3) implementation of new government securities trading arrangements, and (4) revision of the country's foreign exchange laws (BOZ, 2006; GRZ, 2006; World Bank, 1993; 2001; 2017).

The introduction of a cash budget system in 1993 limited government ministries' expenditures to disbursed funds only (Government of the Republic of Zambia "GRZ", 2007). In 1993, the government introduced a new treasury bill tender system called the auction system, to "deepen the domestic capital, money and foreign exchange markets", in addition to mopping up excess liquidity (BOZ, 2015: 10). This exercise caused a swift upsurge in nominal interest rates from approximately 60% in September 1992 to over 200% by the end of 1993 (World Bank, 2001). The liberalisation of the treasury bill and the government bond markets meant that the prices of these securities were to be determined by market forces. Through the Foreign Exchange Control Act of 1994 and the re-introduction of the auction system of treasury bills in 1995, there was a cessation of foreign exchange repressions and liberalisation of interest rates (BOZ, 2015). Consequentially, the soaring real interest rates between 1991 and 2000, averaging 15.5%, attracted many private investors to the government issued debt (GRZ, 1993; BOZ, 2010). Apart from financial market liberalisation, the government also reformed its taxation systems, resulting in the replacement of sales tax with value-added tax in July of 1995 (GRZ, 2017). The government's motive in introducing value-added tax in 1995 was to reduce inflationary pressures in the economy and to enhance the revenue performances of the state by minimising tax evasion (Organisation for Economic Co-operation and Development "OECD", 2006).

In the post-Highly Indebted Poor Countries (HIPC) period, domestic public debt reforms were focused largely on curtailing central government budget imbalances. The reforms included rationalisation of the civil service salary bill, integration of planning and budgeting processes, introduction of new public expenditures controlling frameworks, adoption of new mechanisms of selling government securities, and amendment of the country's constitution, especially on public finance management and accountability (World Bank, 2017; Fagernas & Roberts, 2004). For instance, in 2006, the frequency of auctions for government securities was reduced from weekly to fortnightly for treasury bills, but was increased from quarterly to every two months for government bonds (BOZ, 2006). This government policy initiative was envisioned to enhance liquidity management by progressively moving away from issuing shorter-term debt securities to issuing longer-term securities. Further, to promote more efficient and sustainable domestic public debt levels, in 2015, the government implemented the Treasury Single Account (TSA) system (GRZ, 2015a). The TSA system is an integrated structure of bank accounts that indicates the current cash resources of the government. The purpose of instituting the TSA system was to boost the government's capability to efficiently and effectively administer public financial resources through refining existing payments processes and eliminating unwarranted procedures (GRZ, 2015b).

In the budget statement of 2014, the government reintroduced the cash budgeting system in an effort to substantially reduce domestic public debt arrears that had accumulated in recent years. In reverting to the cash budgeting system, beginning 2014, the government intends to lower its deficit financing syndrome by progressively reducing fiscal deficit to 3% of GDP by 2020 (GRZ, 2013).

The other domestic public debt reforms in Zambia were aimed at fostering public financial discipline and were therefore embedded in the country's constitution amendment – Constitution No. 2 of 2016 (amended) – and other supplementary statutory instruments and acts. In the amended constitution, each stage of the budgeting process, along with the modalities surrounding the issuance of domestic public debt, is guided by specific articles. For instance, the Bank of Zambia was assigned the sole responsibility of issuing government securities and giving financial guidance to the government of Zambia (Zambia Institute for Policy Analysis and Research "ZIPAR", 2015). Other pieces of legislature include the Public Finance Act. The Public Finance Act of Zambia prescribes how budget deficits will be financed and provides annual limits of how much the responsible minister should contract on behalf of the government (the Public Finance Act No. 15 of 2004 of the Laws of Zambia).

Apart from domestic public debt reforms, the government has also, over the review period, embraced a series of foreign public debt restructuring exercises. The foreign public debt reforms were aimed at reducing external indebtedness and maintaining sustainable government debt levels. These reforms included the revision of foreign debt national policies to enhance effective re-engagement with traditional creditors; the introduction of new foreign public debt management systems, including the introduction of computerised financial management information systems; and the introduction of new institutional debt management frameworks (GRZ, 2006; 2013; IMF, 2015). In the late 1990s, the government of Zambia undertook joint public expenditure reviews with the World Bank, coupled with the implementation of the Integrated Financial Management Information System (IFMIS) and the Public Expenditure Tracking Surveys "PETS" (Clements *et al*., 2003; World Bank, 2001). The objective of these initiatives was to improve public sector service delivery performance through the monitoring and tracking of foreign public debt commitments and domestic expenditures, thus helping to contain foreign public debt within sustainable levels.

Other foreign public debt reforms in the post HIPC included the government's adoption of consistent public debt sustainability analyses (DSA). The debt sustainability analyses were being done in collaboration with the IMF. The intention behind the DSA was to closely monitor the sustainability of foreign public debt levels and to make informed government debt decisions on prospective new borrowing needs of the state, debt requirements, and sources in the medium- to long-term period (Ministry of Finance "MOF", 2014). In order to minimise future liquidity challenges in the post debt relief period, and to strengthen fiscal discipline through prudent foreign borrowing, the government implemented the Medium-Term Debt Management Strategy "MTDS" (IMF, 2008). The MTDS is a policy guide that provides a framework for debt contraction, redemption and refinancing so as promote fiscal sustainability and stimulate economic growth.

Foreign public debt approval and contraction in Zambia is currently guided by numerous legal statutes. The Constitution of Zambia No. 2 of 2016, amended; the Loans and Guarantees (Authorization) Act, Chapter 366 of the laws of Zambia; the Bank of Zambia (Amendment) Act, 2013, in conjunction with the Bank of Zambia Act of 1996, Chapter 360 of the laws of Zambia; the Local Loans Act, Chapter 353 of the laws of Zambia; and the Public Finance Act No. 15 of 2004 of the laws of Zambia are some of the frameworks that help in the management of foreign public debt in Zambia in the post HIPC era (African Forum and Network on Debt and Development "AFRODAD", 2005; GRZ, 2012). For instance, according to Part VI, Article 63 subsection two (d) of the Constitution of Zambia No. 2 of 2016, amended, the National Assembly shall approve foreign public debt before it is contracted (Part VI of the Constitution of Zambia, 2016, amended). Further, Article 207 subsection two(a) of the constitution states that the National Assembly shall specify and approve terms and conditions of a loan, grant, or guarantee (Part VI of the Constitution of Zambia, 2016, amended). The afore-described statutes were enacted and enforced with the prime objective of cautioning the country against external shocks arising from unsustainable foreign borrowings.

The public debt reforms discussed above have significantly influenced the structure and composition of Zambia's public debt during the period under review. The debt reforms also contributed to the considerable decrease in the country's debt stocks. They have also enhanced the study country's economic growth prospects during the review period. Presently, the country is among the Southern

African Development Community (SADC) countries whose overall public sector debt level is sustainable under the World Bank and IMF baseline scenarios (IMF, 2015). Besides sound macroeconomic policies and a strong public debt management framework, improved diversification of the export base and improved project appraisal are needed in Zambia to maintain debt sustainability, especially in the face of a projected rise in non-concessional borrowing and potential external financial and economic shocks (IMF, 2015).

3. Public Debt Trends in Zambia

The evolution of Zambia's public debt over time was correlated with domestic factors such as policy failures, domestic political developments, and unexpected world economic shocks. On one hand, the domestic component of Zambia's public debt came largely from treasury bills and government bonds; infrastructure loans; borrowings from commercial banks through loans and advances; parastatals debts; and accumulation of arrears on statutory liabilities such as pensions (BOZ; 2000; 2005; 2010; 2013; IMF, 2005a; ZIPAR, 2015). On the other hand, the foreign public debt component was a result of excessive non-concessional borrowing, mainly from multilateral and bilateral financial institutions, private banks, and export credit agencies (BOZ, 2010; IMF, 2012a; World Bank, 2015a). The non-attractiveness of government securities in the 1990s, owing to high inflation and increased government payment defaults, also motivated the government to rely mostly on foreign borrowing (BOZ, 2015, p. 10).

In 1964, after attaining political independence, the Zambian government sought to attain economic sovereignty by setting as priority goals industrialisation and economic diversification (United Nations Economic Commission for Africa "UNECA", 2016). In line with these objectives, the country embarked on a series of political, financial, social, and economic reforms with the intention of stimulating economic growth through increased investment flows, efficient utilisation of domestic resources, increased export volumes, and finding sustainable ways of reducing domestic and foreign public debts (Fraser & Larmer, 2010). Focus was placed on massive infrastructure development through extensive expansionary government policies.

Despite the huge public sector investment in the early 1970s, exogenous factors such as the fall in world market prices of unrefined copper, and the global oil shocks of 1973 and 1978, increased the cost of imports and exacerbated macroeconomic instability (Langmead et al., 2006). Also, the massive nationalisation programme of the late 1960s, which the government of Zambia termed the "Africanisation program", significantly increased government expenditures, thereby worsening the financial position of the state (Andersson et al., 2000). Consequentially, weakening terms of trade – especially of unrefined copper and soaring international oil prices – caused extensive balance of payment problems and unsustainable budget deficits in Zambia, resulting in debt financing (United Nations Conference on Trade and Development "UNCTAD", 2012). In 1973, for instance, Zambia went into a loan contract with the World Bank to caution itself from the oil price shock (United Nations Development Programme, 2006, pp. 11-12).

However, the government erroneously perceived the adverse developments in the domestic and world economy, particularly copper export prices, as temporary. It continued to maintain high levels of consumptive and capital expenditures, opting to finance the resultant budget disparities through local and foreign borrowing (Fraser & Larmer, 2010). Moreover, the various infrastructural development projects that were undertaken by the government in the mid-1970s, such as the opening up of the Tanzania-Zambia corridor, helped to accelerate the depletion of the state's foreign reserves, forcing the government to opt for debt financing instead of scaling down capital costs (UNCTAD, 2011). Furthermore, the Zambian government's commitment to supporting liberation struggles in the SADC region between 1960 and 1980 contributed to the negative compounding effect on state revenues, leading to incessant reliance on deficit financing (McCulloch *et al.*, 2004a). Subsequently, by the mid-1980s, Zambia had plunged into a dreadful public debt crisis position, becoming one of the most highly indebted nations in the world (Hill & McPherson, 2004).

From a historical standpoint, in pre- and post- independent Zambia, the mining sector (largely copper) was the mainspring of employment, foreign currency receipts and government income (Andersson et al., 1989; Rakner, 2003). Hence, the twin effect of sagging world copper prices and the de-industrialisation course experienced by Zambia in the late 1970s until the late 1990s constrained the central government's revenues from mineral taxation and exports, which declined by 82.6% from ZMK339 million in 1974 to ZMK59 million in 1975, and further to ZMK12 million in 1976 (Organisation for Social Science Research for Southern and Eastern Africa "OSSREA", 2007). During this period, the aggregate contribution of raw copper to export revenues exceeded 90%, whilst the general manufacturing sector accounted for only 6.9% (World Bank, 2015b). Thus, with reduced government tax revenue and export receipts, especially mineral revenue, the government had to revert to excessive domestic borrowing – resulting in a radical rise of domestic debt stock in nominal terms, reaching over ZMK566 billion in 2000 (Fagernas & Roberts, 2004; McCulloch et al., 2000a). The central bank of Zambia responded by issuing credit on the domestic market to finance recurrent government expenditures, such as the payment of civil service and the importation of fuel, and to fund work-in-progress capital projects (Fagernas & Roberts, 2004). Thus, the substantial rise in domestic public debt during this period can be accredited to numerous factors, but mainly rooted in the adopted liberalisation policies and the continuous fall in gross government revenues – estimated to have declined by 30% between 1990 and 1998 (McCulloch et al., 2000b). These factors include: (1) the rolling-over policy, which dealt with capitalisation of the principal and interest on public domestic debt; (2) high interest rates, determined by the forces of demand and supply; (3) continued unsustainable government budget deficits; and (4) high liquidity in the banking sector (MOF, 2004). By end of 1994, Zambia was in a domestic public debt trap, where government expenditures were rising fast, domestic debt was increasing exponentially, and domestic interest rates were soaring (African Development Bank, "AfDB", 2015).

The persistently high inflation levels experienced in the Zambian economy in the late 1980s had a reducing effect on the real domestic public debt since they were not matched with equal adjustments in domestic nominal interest rates (Central Statistical Office of Zambia, 2014). The rise in central government's expenditures after 2000, amid falling tax revenues, seems to have perpetuated the need for the government to finance itself through domestic borrowing (IMF, 2004). Additionally, the recurrent budget allocation overruns by the central and local governments after 2006, which were financed by domestic credit, aggravated the domestic public debt dynamics in Zambia.

According to the central bank, despite the auction system of treasury bill introduced in 1993 and 1995, the secondary market for Zambia's government securities remained underdeveloped and narrow, characterised by few government liabilities with parastatals (BOZ, 2015). Henceforth, the raised credit repeatedly fell short of the state's financial needs, compelling the government to rely on foreign borrowing, mainly from multilateral and bilateral financial organisations – mostly the World Bank, IMF, and the Paris Club (BOZ, 2012). Foreign public borrowing grew from the moderately low levels of US$3.8 million between 1975 and 1984 to approximately US$7.3 billion in 2004, representing a 187% increase (SADC, 2010). The period from 1970 to 2000 can be described as 'foreign debt-led' in the sense that Zambia ran a persistent current account deficit and borrowed significantly from global financial institutions and world capital markets to finance the fiscal gap. For instance, in the five-year period between 1975 and 1980, Zambia's foreign public debt increased nearly threefold, from US$1137 million to US$3366 million, respectively (Swedish International Development Cooperation Agency

"SIDA", 1989). According to SIDA (2003), Zambia's total foreign public debt had further increased to US$7.3 billion by 1991, with most debt measurement variables deteriorating to unprecedented levels.

By 1992, Zambia's foreign government debt had reached alarming levels, which prompted some creditors, such as the Paris Club, to cancel part of the debt owed to them by this country. In 1996, the Bretton Woods institutions introduced the HIPC initiative, targeting developing countries in serious debt challenges (IMF, 2001). In December 2000, Zambia's foreign public debt was at least double its GDP. Fortunately, the Bretton Woods institutions agreed that Zambia had reached the Decision Point of the HIPC initiative (IMF and the International Development Agency "IDA", 2001). During the interim period, between decision and completion points, Zambia received foreign public debt cancellation amounting to US$452 million and US$98 million from the IMF and IDA, respectively (IMF, 2005b). Other creditors that extended debt relief to Zambia between 2000 and 2005 were the Organisation of the Petroleum Exporting Countries (OPEC) Fund for International Development, the AfDB, the European Union (EU), and the Paris Club (UNDP, 2006).

In April 2005, Zambia reached the HIPC Completion Point, and it received remarkable foreign public debt relief from the Group of Eight (G8) countries, Paris Club, and other creditors (GRZ, 2006b; 2015). The debt relief was in the form of foreign public debt stock cancellation and rescheduling. A total of US$3.8 billion foreign public debt was cancelled, reducing accumulated foreign public debt from US$7.3 billion in 2004 to US$4.5 billion by December 2005 (GRZ, 2010). The foreign public debt burden was further reduced in 2006, when the Bretton Woods institutions and the African Development Fund (AfDF) decided to wholly cancel the debts owed to them by Zambia under the Enhanced HIPC initiative and the Multilateral Debt Relief Initiative "MDRI" (GRZ, 2006b; MOF, 2006). The Multilateral Debt Relief Initiative was a redefined and deepened edition of HIPC.

In January 2006, the IMF wrote-off US$581.6 million, representing 97% of the value of debt owed to it by Zambia (GRZ, 2008). Consequently, the MDRI reduced Zambia's debt by a further US$2 billion to US$2.5 billion by the end of 2006 (World Bank, 2014). Figure 1 shows the trends in public debt growth in Zambia during the period from 1980 to 2015.

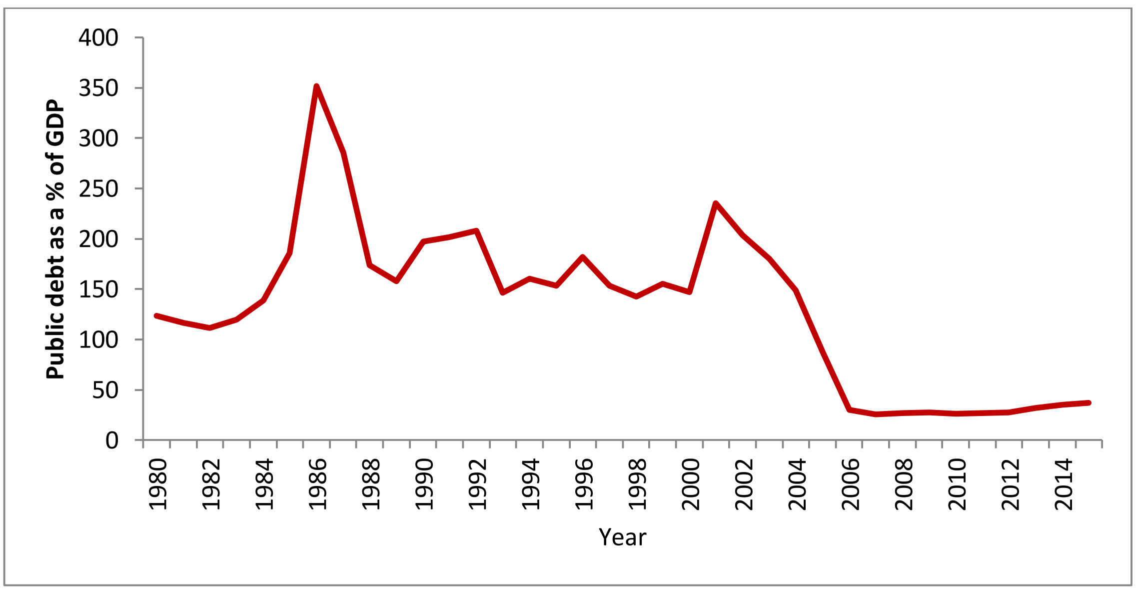

Figure 1. Public Debt Trends in Zambia (1980-2015)

Source: World Bank (2012; 2015)

In Figure 1, two distinct episodes of public debt to GDP growth in Zambia can be established. The first episode is from 1980 to 2004, in which Zambia's public debt was exceptionally higher than GDP. During this period, the recurrent budget was largely financed by monetised domestic revenue and domestic borrowing, with more than 80% of the capital budget financed from foreign borrowings (Fagernas & Roberts, 2004). Apart from accumulating interests on public debt, the deterioration in real fiscal resources between the mid-1980s and the mid-1990s brought about substantial declines in most economic and social categories of expenditure (World Bank, 2012). Contrary, however, the cumulative effect of rising aid inflows, debt relief initiatives and the stabilisation of the domestic economy, culminated into marginal reduction in public debt growth rates in the late 1990s. Also, a combination of the new government's revenue and spending reforms, which helped to curb public expenditure, and the commencement of domestic public debt redemption through the help of an increased level of concessional foreign public borrowing, contributed to the marginal decline in debt-GDP ratio – although it remained above 100% (Fagernas & Roberts, 2004). The persistently high levels of inflation, averaging 118%, recorded during the period of 1984 to 2004 also had a compounding effect on the nominal value of public debt (World Bank, 2015c). Similar to other indebted countries, the period from 1980 to 2004 was characterised by the exceptional burden of foreign public debt arising from debt interest payment defaults, which reached approximately US$3 billion by 2004 (UNDP, 2006, p. 11). From a backward-looking perspective, the high levels of public debt between 1980 and 2000 were associated with lower and volatile growth rates, averaging 0.95% (Chirwa & Odhiambo, 2016).

The second episode defines the period after the debt relief of 2005 and 2006. This phase is characterised by public debt levels that were below the national gross output. The low ratio of government debt-to-GDP of less than 50% was a result of a combination of debt relief initiatives and a series of government financial reforms that were implemented in 2005 and thereafter. The reforms were aimed at enhancing effective public debt and government expenditure management.

Despite high growth rates averaging 5.6% between 2000 and 2014 (World Bank, 2012; 2015), the government relied more on borrowed funds to finance its programmes due to a combination of low domestic tax revenues and increasing infrastructural development expenditures (UNECA, 2016). The rising trend in Zambia's public debt relative to GDP after 2010 was due to a drastic increase in government borrowing, domestic and foreign, to fund protracted public sector investments, owing to the government's priority to transform the country into a middle-income country by 2030 (MOF, 2006). Although the Fifth National Development Plan had prescribed a maximum limit of not more than 0.5% of GDP on domestic public borrowing, the Zambian government exceeded it by 2% in 2013 due to a number of reasons. These include a sizeable amount of carryover funds, an expansionary monetary policy, and an increase in the issuance of long-term public sector securities (BOZ, 2016). Accordingly, an analysis of Zambia's public debt reveals an upward trend in the post-Highly Indebted Poor Countries initiative era. Table 1 provides a summary of the Bretton woods institution's loans to Zambia between 1970 and 2005.

Table 1. Summary of the Bretton Woods Institution's Loans to Zambia between 1970 and 2005

Year	Loan Description
1973	The World Bank disbursed the requested by the Zambian government following the global oil price shock.
1978	The World Bank, through the International Development Association, extended new loans to Zambia.
1981	The IMF, made some loan disbursements to Zambia under the Extended Fund Facility (EFF).
1982	The IMF cancelled the EFF.
1983	The World Bank stopped making new loan and aid disbursements to Zambia.
1984	The World Bank agreed to give Zambia a new loan towards the resuscitation and development of the Copper Sector.
1985	The Bretton Woods institutions made some Structural Adjustment Programme loans disbursements to Zambia.
1987	The Zambian government cancelled all Bretton Woods sponsored reform programmes. The IMF and the World Bank suspends financial aid and loans to Zambia.
1992	The Zambian government clears loan arrears to the World Bank. The IMF started to make some new loan disbursements.
1995	The IMF and Zambian government signed a new loan of US$1.3 billion under the 3 year Enhanced Structural Adjustment Facility (ESAF) and 1-year Structural Adjustment Facility (SAF). Also in 1995, the World Bank issued new loans to Zambia under the Economic Recovery and Investment Project.
1999	The IMF disburses part of the $350 million loan under the extended ESAF.
2000	Zambia reached the IMF and the World Bank HIPC Decision Point. As a result, Zambia received partial foreign public debt relief.
2004	Through the Poverty Reduction and Growth Facility, the IMF made new loans to Zambia, to the tune of US$320 million.
2005	Zambia reached the IMF/World Bank HIPC completion Point and received enormous debt relief from the Bretton Woods institutions.

Source: GRZ (2006a; 2006b); IMF (2001; 2005a)

4. Challenges Faced in Public Debt Management in Zambia

Notwithstanding the existence of several government debt management statutes and strategies, some of the challenges faced by the government of Zambia are: (1) the lack of a comprehensive long-term plan or institutional arrangements to coordinate fiscal and monetary policies; and (2) the absence of public debt analysis methodology to ensure that government debt is kept within sustainable levels and that risks associated with future public borrowing are well calculated and known (BOZ, 2015b).

Zambia's current legal and administrative system on public debt is fraught with loose ends, which include duplication of or overlapping functions and the absence of clear borrowing limits to all government arms and associated institutions (AFRODAD, 2010). For instance, whereas the General Loan and Stock Act, Chapter 350 of the laws of Zambia empowers the central bank to administer government securities that were publicly issued, this law also allocates the mandate of registering government securities to the national treasury (GRZ, 2012). Also, whereas the law provides the maximum borrowing limit for the central government, it is silent about this issue for local governments and other arms of the government, except when requesting guarantees (AFRODAD, 2012). Additionally, according to AFRODAD (2012), there currently are no clear statutes to govern the approval of guarantees from the Ministry of Finance.

There is also potential for conflict between debt issuance for monetary and fiscal policy objectives since government domestic debt issuance directly affects the domestic capital market through the establishing of benchmark prices, which also impact on financial sector stability and growth and, hence, affect the effectiveness of monetary transmission mechanisms (World Bank, 2015b). In other words, government issuance of domestic debt can restrain the options open to monetary policy authorities, and vice versa. Even with prescribed limits on domestic public borrowing, the maturity structure of government debt securities can directly affect the shape of the yield curve and thus influence the operations of monetary authorities (World Bank, 2015b).

According to the Bank of Zambia (2015, p. 7), the absence of a proper government debt management framework, weak fiscal performance, exchange rate instability and high inflationary pressures in the 1980s and 1990s contributed to unsustainable domestic public debt levels. During this period, the government failed to effectively monitor and control the expenditures of its line ministries in line with the stipulated financial rules and regulations, leading to huge fiscal deficits (World Bank, 2005, p. 3). Consequently, the government was compelled to borrow additional financial resources to finance its budget. Moreover, the domestic market for government securities in Zambia is still narrow, and the treasury securities are dominated by the banking sector – mainly commercial banks (OECD, 2010; 2014). The challenge with this arrangement is that commercial banks should match short-term liability deposits with short-term treasury bills, thus depressing the full development of the government bond market (OECD, 2007). The dominance of the banking sector in government securities also reflects weaknesses in the commercial lending operations (OECD, 2007).

Although in 2012 the government issued Eurobonds, which possibly attracted foreign investors to the government securities, there are still challenges associated with the development of more long-term domestic public debt instruments that attract potential investors (IMF, 2014a). Domestic debt of between two and three years makes the government extremely susceptible to short-term maturity securities and refinancing vulnerabilities given the volatility of inflation and world interest rates (IMF, 2014b). Also, since the market for government securities is still underdeveloped, it is difficult and costly to introduce tax incentives to promote the demand for treasury bills and government bonds in Zambia (OECD, 2010). While non-resident holders of government bonds are typically low, their presence increases volatility, meaning that Zambia's domestic markets can be hit by exogenous shocks (OECD, 2014).

The other challenge that is making domestic public debt management difficult in Zambia is that local governments (municipal councils) are not involved in the overall national debt management strategy formulation (AFRODAD, 2012). The implication, according to AFRODAD, is that local councils end up making too many financial demands on the central government, leading to continuous fiscal deficits, which ultimately lead to either domestic or foreign public borrowing. This challenge can be alleviated by inclusive policy and strategy making, where local governments are involved in shaping of national policies that affect them. In addition, local governments can be made to seek adequate approval from the central government so as to ensure that their borrowing conforms to the national developmental objectives.

Pertaining to the powers to borrow, the Local Loans Act authorises the president and/or the minister responsible for finance to acquire funds in the domestic financial markets through the issuance of specified government securities, that is, bonds and debentures (GRZ, 2016; ZIPAR, 2015). The president is permitted to issue a warranty without an appropriation act or approval from the parliament, an instance which brought about unconstitutional excess expenditures (World Bank, 2005: 1). Thus, the clause actually makes both government expenditure management and domestic public debt control highly difficulty and unmanageable (World Bank, 2005).

Although Zambia has explicit statutory measures governing the contracting and servicing of foreign public debt, the framework is not always adequately implemented and is poorly harmonised (IMF, 2015, p. 9). For example, the Loans and Guarantees Act of the laws of Zambia is only limited to the contraction, and not reporting, of foreign public debt. Hence, there are no proper foreign public debt management guidelines regarding the types of foreign public debt reports to be produced by either the central bank or the Ministry of Finance (IMF, 2012b). Also, since the President's Office has exclusive control over national foreign debt contraction, this arrangement may actually make the control of foreign debt difficult in addition to fostering abuse of national financial resources (AFRODAD, 2011: 27).

Furthermore, the management of foreign public debt is constrained by the weak institutional arrangements in the country, resulting in duplication or overlapping of functions between government authorities, especially the central bank and the Ministry of Finance (Macroeconomic and Financial Management Institute “MEFMI”, 2007, p. 23). Other challenges associated with foreign public debt management in Zambia include the absence of clearly set out foreign public borrowing limits to local government authorities and the lack of foreign public borrowing thresholds, like public debt/GDP ratio, interest paid/ GDP ratio, and interest paid/tax revenue ratio, which are fundamental principles for foreign public debt management (World Bank, 2013). The Zambian government should also set out commitment control rules while empowering the Ministry of Finance to undertake foreign public debt audits in local municipalities - government’s main sources of public guaranteed debt – which are currently non-existent (Office of the Audit General, Zambia, 2011, p. 21).

5. Conclusion

This paper has discussed the dynamics of both domestic and foreign public debt in Zambia from 1964 to 2015. The highlighted debt management reforms were in the form of legal, institutional, and administration frameworks, as well as contractual agreements with major foreign creditors such as the IMF, World Bank, and the Paris Club. The paper revealed that between 1970 and 1999, adverse developments in the domestic and world economies prompted massive public borrowing, both domestically and externally. Consequently, beginning the late 1980s, Zambia was in a severe public debt crisis, compelling the government to embark on a multiplicity of economic and financial reforms. The reforms were aimed at reducing the country’s indebtedness and also reviving the country’s economic fortunes. Also discussed in the paper is the considerable rise in the country’s public debt after 2012, being caused by new non-concessional loans and the issuance of Eurobonds – resulting in an increased threat of high repayment obligations by 2020. High nominal interest rates, insistent economic crises and lack of clear institutional arrangements to coordinate and synchronise government debt were some of the identified debt management challenges discussed in the paper. To ensure future sustainability of public debt, the paper recommends that the government: (1) limits both domestic and foreign borrowing to reduce high interest payments on debt in future; (2) aligns its infrastructure expenditures with domestic revenues to ensure budget sustainability; (3) implements and adheres to cash budgeting system to control fiscal deficits; and (4) expands its domestic revenue base by diversifying the economy and promoting massive industrialisation.

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