



BRIEF ON THE 2024 ANNUAL BORROWING PLAN AMMENDMENT

**PARLIAMENTARY BUDGET OFFICE
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1.0 INTRODUCTION

The 2024 Annual Borrowing Plan (ABP) Amendment was presented to the National Assembly on Friday, 21st June 2024, together with Supplementary Estimates of Expenditure No. 1 of 2024. This is in accordance with Section 9 of the Public Debt Management Act, 2022 (PDMA), which empowers the Minister of Finance to review the ABP when necessary. The Minister is subsequently required to submit the revised ABP before the National Assembly for approval. The revised ABP has been necessitated by the Supplementary Estimates of Expenditure No.1 of 2024, which require additional debt financing. In line with the National Assembly of Zambia Standing Orders, 2024, the revised ABP was referred to the Planning and Budgeting Committee for consideration.

In the revised Plan, the Government intends to raise an additional K6 billion in domestic financing and US \$490.78 million in external financing, of which US \$195.5 million will be disbursed in 2024.

2.0. COMPLIANCE WITH LEGISLATION

Section 8(3) of the PDMA, prescribes that the ABP, and by extension, the revised ABP, should consist of the following:

- a) the total borrowing needs for the next financial year;
- b) the purpose of the loans to be contracted;
- c) debt instruments to be used;
- d) broad terms of the borrowings;
- e) the indicative timing of the borrowing operations;
- f) the maximum limit that the Government intends to borrow in that financial year; and
- g) the overall net increase or decrease in public debt.

Observation: The revised ABP complies with the provisions listed above except for the indicative timing of the external borrowing operations outlined in the Plan.

Additionally, Section 10 of the PDMA, provides for the submission of an update on the implementation of the ABP to the National Assembly on a bi-annual basis. However, the first update on the implementation of the 2024 Annual Borrowing Plan is yet to be submitted to the National Assembly. This document is key for the consideration of the revised 2024 ABP.

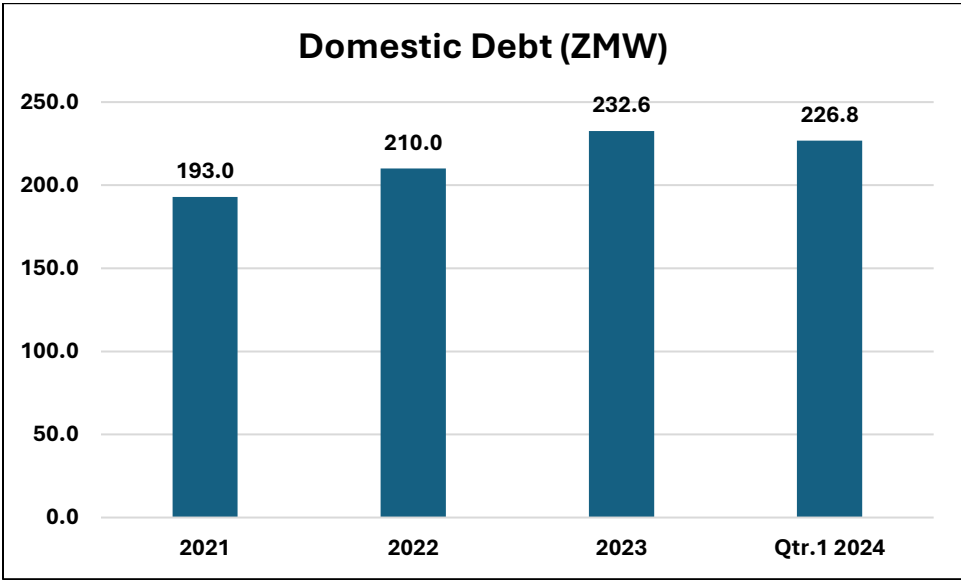
3.0 DEBT POSITION

This section illustrates the growth in the stock of both domestic and external debt in the period 2021 to Quarter 1 of 2024.

3.1 Domestic Debt

The stock of domestic debt increased by 17.5 percent from K196 billion at the end of 2021 to K226.8 billion at the end of the first quarter of 2024. However, the domestic debt stock decreased by 2.5 percent between the end of 2023 and the end of the first quarter of 2024 due to large maturity payments and subdued investor participation in Government securities auctions which is attributed to tight liquidity conditions in the market, especially for commercial banks. This poses a major risk to the 2024 financing target and consequently to budget execution.

Figure 1: Domestic Debt Stock

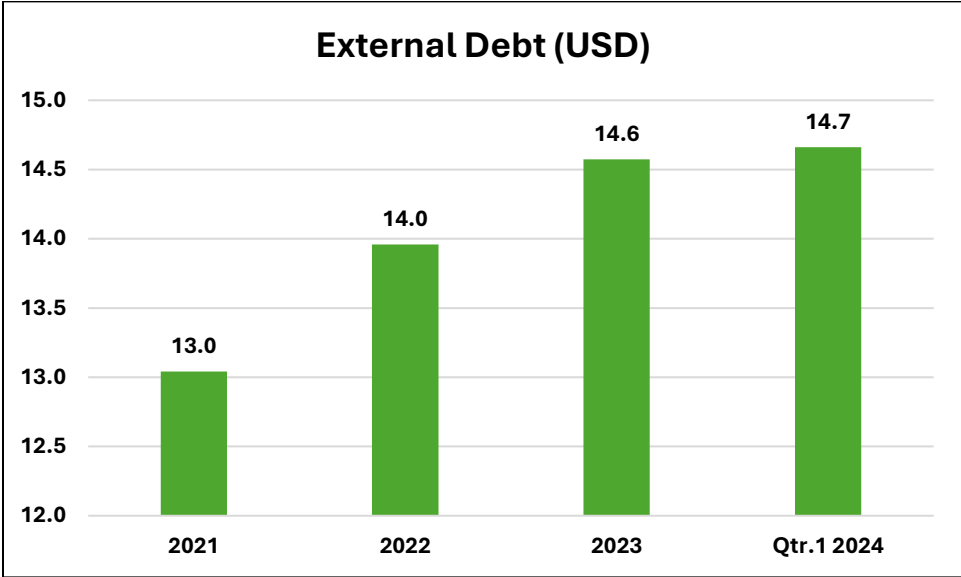


Source: MoFNP Debt Statistical Bulletin

3.2 External debt

The stock of central Government external debt recorded an increase of 12.4 percent from US\$13 billion at the end of 2021 to US\$14.7 billion at the end of the first quarter of 2024.

Figure 2: External Debt Position



Source: MoFNP Debt Statistical Bulletin

4.0 ADDITIONAL BORROWING NEEDS FOR THE 2024 FINANCIAL YEAR

The National Assembly approved the contraction of domestic financing amounting to K16.3 billion. The proposed additional borrowing in the 2024 revised ABP of K6.0 billion represents an additional 36.8 percent, bringing the total domestic financing to be contracted in 2024 to K22.3 billion or 3.4 percent of Gross Domestic Product (GDP).

Regarding external debt financing, for the 2024 fiscal year, US \$416 million was approved for contraction in the initial ABP while the revised ABP proposes to contract an additional US \$490.78 million, representing an additional 118 percent in external debt financing for the year 2024. This therefore brings the total external contraction to US \$907.11 million.

In comparison to the 2023 financial year, the National Assembly approved a total of K15.6 billion as the maximum limit on net domestic financing and US \$1.40 billion as the maximum limit on external financing.

Observation: The total domestic financing of K22.3 billion represents 3.4 percent of GDP. This is above the 2024 Budget target of limiting domestic borrowing to no more than 2.5 percent of GDP. The additional borrowing may result in a higher-than-projected fiscal deficit.

4.1. Domestic Financing

The K6 billion to be contracted domestically is for the purpose of a liability management operation on fuel arrears. The Revised Dismantling of Domestic Arrears Strategy (DDAS) 2024-2029 identifies fuel arrears as the most expensive category of arrears due to the application of late interest payments embedded in the contracts. Therefore, the Government intends to clear these arrears within 2024 using less costly debt financing than the contractual rate for late payment interests.

The total stock of fuel arrears amounts to K23.29 billion. However, only a budget provision of K16.2 billion has been allocated toward clearing these arrears. According to the DDAS, the Government intends to bridge the gap between the stock (K23.29 billion) and the proposed payment amount in 2024 (K16.2 billion) through negotiating for discounts with suppliers. Under this operation, the K6 billion additional borrowing will be contracted from local banks or through the issuance of Government securities. The balance towards full clearance of the arrears will also be raised through the issuance of Government securities.

The indicative terms and instruments for the additional domestic borrowing are shown in Table 1 below:

Table 1: Indicative Instruments and Terms for Domestic Borrowing

Description	Terms
Additional amount to be contracted	K6,000,000,000
Maturity	Maximum of 7 years
Grace period	Nil
Interest Rate	Below 13.5 percent per annum if borrowed in USD or Government Securities market yield rates if borrowed using Government Securities.

Source: 2024 Revised Annual Borrowing Plan

Observations: As part of the liability management operation, the Government intends to borrow K6 billion from the domestic market, specifically from local commercial banks or issuance of Government securities. However, the under subscription of Government securities, on average, evidenced in the first half of 2024 indicates the constrained liquidity being experienced by commercial banks. Additional participation by the Government in the domestic market may crowd out the private sector.

Additionally, the terms of the additional K6 billion to be borrowed from local commercial banks indicate that the amount may be borrowed in foreign currency, specifically United States Dollars. This is not consistent with the debt sustainability reforms outlined in the International Monetary Fund (IMF) Extended Credit Facility discouraging the raising of funds domestically using instruments denominated in foreign currency. This is due to the adverse impact of exchange rate volatility on domestic debt denominated in foreign currency.

4.2 External Financing

The Government plans to contract an additional US \$490.78 million from external sources. The loans are earmarked for budget support and the implementation of projects in various sectors, including health, agriculture, and infrastructure development. The indicative terms for the additional external borrowing are shown below:

Table 2: Indicative Instruments and Terms for External Borrowing

Description	Terms
Additional amount to be contracted	US \$490,776,000.00
Maturity	Minimum of 10 years
Grace Period	Minimum of 5 years
Interest Rate	Between 0 and 2.5 percent per annum
Interest Type	Fixed

Source: 2024 Revised Annual Borrowing Plan

Observation: Notably, the minimum maturity for the additional loans is shorter at 10 years, compared to 12 years in the initial 2024 ABP and 25 years in the 2023 ABP. Despite the grace period, shorter-dated maturities present amortisation risks due to elevated annual principal payments compared to longer-dated maturities.

5.0 PROJECTED DISBURSEMENTS FROM EXTERNAL LOANS IN THE 2024 FINANCIAL YEAR

The projected disbursements in 2024 from additional loans amount to US \$195.5 million, whereas the projected disbursements from the initial 2024 ABP are projected at US \$914.75 million¹, amounting to a total of US \$1.1 billion. This is shown in Table 3 below.

Table 3: Projected Disbursements in the 2024 Financial Year

Description	Disbursements (USD)
2024 ABP	914,746,655.26
2024 Revised ABP	195,500,000.00
Total	1,110,246,655.26

Source: PBO Construction using 2024 Annual Borrowing Plans

Observation: While the cumulative disbursements for the 2024 financial year amount to US \$1.11 billion as shown in Table 3, the revised ABP states that cumulatively, disbursements on additional loans to be contracted and already contracted loans are now estimated at US \$1.35 billion, establishing a gap of US \$240 million in disbursements not accounted for in the revised Plan.

6.0 PERFORMANCE OF THE 2023 ANNUAL BORROWING PLAN

This section highlights the performance of the inaugural 2023 ABP to identify lessons learned.

6.1 Performance of Domestic Borrowing in 2023

In 2023, Government securities were on average undersubscribed, with Treasury bills recording an average subscription rate of 95.0 percent and Government bonds averaging 73.9 percent subscriptions. The under subscription was partly attributed to

¹The amount includes disbursements from loans to be contracted in 2024 in the initial ABP (US \$203.97 million) and disbursements from already contracted loans (US \$710.78 million).

the limit on foreign investor participation in the primary market and tight liquidity conditions.

Observation: Under subscriptions continue to be a major risk even in 2024. For the period January to June 2024, the Government raised gross financing of K21.7 billion through Government securities against a target of K35.4 billion, representing an under subscription rate of 39 percent or K13.7 billion. Treasury bills recorded an average subscription rate of 54 percent, while Government bonds averaged 77 percent. The underperformance was attributed to tight liquidity conditions resulting from measures to moderate exchange rate volatility, control inflation, and cash consolidation efforts by the Government.² There is therefore a higher likelihood that the risk will persist and threaten budget credibility.

Notwithstanding the under subscription, the outturn was consistent with one of the guidelines for implementing the Debt Management Strategy (2022-2025), which is to minimise refinancing risks by assigning more weight to Government securities with longer maturities, thereby smoothing the domestic debt maturity profile.

6.2 Performance of External Borrowing in 2023

According to the 2023 Annual Borrowing Plan Performance Review Report, as of the end of December 2023, seven new loans amounting to US \$1.06 billion were signed out of the planned eleven external loans. Regarding the remaining four new loans:

- i. the ***Development Policy Operation (DPO 2)*** loan amounting to US \$75.0 million and the ***Zambia-Tanzania Interconnector*** loan amounting to US \$240.0 million were converted to grants following Zambia's reclassification

²To address inflationary pressures and stabilize the exchange rate, the Bank of Zambia increased the statutory reserve ratio (SRR) from 17 percent to 26 percent and the Monetary Policy Rate (MPR) from 11 percent to 12.5 percent. Additionally, the Government streamlined cash management by transferring unutilised balances from commercial bank accounts to the Consolidated Fund at the Bank of Zambia.

from a lower-middle-income to a low-income country by the World Bank in July 2023.

- ii. the ***Farm Block Transformation Programme*** and the ***Kabwe Water Supply Emergency Works*** project loans were not contracted in 2023 due to the non-completion of project preparation activities.

Observation: The non-completion of project preparation activities has significant financial and economic consequences such as delayed service provision and increased project costs due to inflation and changing market conditions.

6.3 Disbursements of Already Contracted Loans

From the total of US \$1.45 billion anticipated to be disbursed from existing loans, including the IMF Extended Credit Facility and Special Drawing Rights, US \$1.24 billion had been disbursed by the end of 2023. This left US \$207.68 million of the projected amount undisbursed. The failure to fully disburse was largely due to delays in meeting project implementation milestones. This implies potential issues in project planning, execution, or coordination that must be resolved to enhance resource efficiency and effectiveness. As a result, projects may take longer to finish than anticipated, potentially leading to cost overruns, particularly due to exchange rate volatility and inflation, among other factors.

7.0 ADDITIONAL FINDINGS

- i. Due to internal approval policies of respective creditors, some external loans to be contracted in 2024 will only be disbursed in the 2025 fiscal year. Although there is a commitment to limit external debt to concessionary borrowing, the targeted sources of financing should be disclosed to enhance transparency.

- ii. King Salman Hospital is one of the major public projects that has dragged on for several years. It is not clear if the US \$35 million loan will see the project to completion. The Ministry of Finance and National Planning needs to provide further information on the Project particularly how much it has been funded from inception to date.
- iii. The Kalabo–Sikongo Road Project is an active matter in the Special Report of the Auditor General on External Public Debt. The road project was previously financed from a syndicated loan amounting to US\$43.7 million by four lenders - BADEA, KAFED, OFID, and SFD. US \$19.4 million was drawn, leaving a balance of US\$24.3 million.

The Government intends to borrow US \$50 million in a split arrangement for the Tapo-Kalabo-Sikongo Angola Road–Project I (US \$20 million) and Project II (US \$30 million). Clarity is needed on the status of the previous loans on part of the Road Project, particularly that there was an undrawn loan amount.

8.0 CONCLUSION

The revised Annual Borrowing Plan was necessitated by the Supplementary Estimates of Expenditure No. 1 of 2024 and presented to the National Assembly for approval, in compliance with the PDMA. The increase in the contraction of both domestic and external debt, aimed at managing fuel arrears and supporting projects in various sectors, raises significant concerns regarding debt sustainability, budget execution, under subscription, and exchange rate volatility. Ensuring transparency, effective project completion, and addressing the under subscription risk of Government securities are critical for maintaining budget credibility and debt sustainability.