

**REPORT OF THE COMMITTEE ON ESTIMATES FOR THE FOURTH SESSION OF THE ELEVENTH NATIONAL ASSEMBLY, APPOINTED ON WEDNESDAY, 24<sup>TH</sup> SEPTEMBER, 2014**

*Consisting of:*

Mr H H Hamududu, MP (Chairperson); Mr G Lubinda, MP; Mr E M Sing'ombe, MP; Mr R L Mpundu, MP; Mr A L Lufuma, MP; Mr L Chabala, MP; Mr R P Mtolo, MP; Mrs A C Kansembe, MP; and Mr P Phiri, MP.

The composition of the Committee changed following the appointment to ministerial positions of Mr G Lubinda, MP and Ms A C Kansembe, MP. The two were subsequently replaced by Dr G L Scott, MP and Ms I M Mphande, MP, respectively.

The Honourable Mr Speaker  
National Assembly  
Parliament Buildings  
**LUSAKA**

Sir

Your Committee has the honour to present its report on its deliberations for the Fourth Session of the Eleventh National Assembly.

**Functions of the Committee**

2.0 The functions of your Committee are as follows:

- (a) examine the Estimates and Excess Expenditure Appropriation Bill;
- (b) report on economics, improvement in organisation, efficiency or administrative reform, consistent with the policy underlying the Estimates, and examine whether the money is well laid out within the limits of the policy implied in the Estimates;
- (c) suggest alternative policies in order to bring about efficiency and economy in administration;
- (d) carry out regular examination and scrutiny of budgets, estimates and management thereof; and conduct budget hearings; and
- (e) make recommendations and report to the House for the formulation and implementation of future budget Estimates.

**Meetings of the Committee**

3.0 Your Committee held fourteen (14) meetings to study two topical issues, namely: *Zambia's fiscal deficit and its impact on the economy*; and *Zambia's utilisation of the \$750 million Eurobond*. In line with the topical issues, your Committee conducted field-based oversight activities on selected Eurobond funded projects.

**Report of the Committee**

4.0 The report of your Committee is divided into three (3) parts. Part I highlights the findings of the study on Zambia's fiscal deficit and its impact on the economy. Part II gives your Committees findings on Zambia's Utilisation of the \$750 million Eurobond while part III is the Conclusion.

## PART I

### 5.0 Zambia's Fiscal Deficit and its Impact on the Economy

According to the Ministry of Finance, Zambia's fiscal deficit over the past three years had increased from 2.2 *per cent* of GDP in 2012 to 4.5 *per cent* of GDP in 2014. The deficit increased to 5.7 *per cent* of GDP in 2013 compared to the 2014 out-turn of 4.5 *per cent*. The key drivers of this deficit were less than projected revenues and the budget overrun. With regard to revenues, domestic revenues averaged 18.0 percent of GDP over the period 2012-2014 with 18.4 percent of GDP recorded in 2014 compared to 18.0 percent in 2012. On the expenditure side, expenditure had steadily been increasing from an average of 20.0 percent of GDP over a period 2011-2012, to 23.4 percent of GDP over the period 2013 and 2014. In absolute terms, it had increased from K26.2 billion in 2012 to K38.8 billion in 2014.

Admittedly, the projected fiscal deficit was still within sustainable levels. However, there were concerns from various stakeholders about the seemingly high rate at which the deficit was increasing. There were fears that if left unchecked, the economy might fall into a debt trap as experienced during the pre-HIPC completion point of 2005. Most stakeholders contended that with Zambia's issuance of the US\$750 million and the US\$1 billion Sovereign bonds, respectively, its debt position would deteriorate further.

In light of the above, your Committee resolved to study in detail Zambia's fiscal deficit and its impact on the economy. The objectives of the study are to-

- (a) appreciate the drivers of the fiscal deficit in Zambia;
- (b) interrogate the effects of fiscal deficits on the economy;
- (c) appreciate measures by the Government to mitigate the effects of the deficit; and
- (d) make recommendations on the way forward.

In order to get a full understanding of the subject under consideration, your Committee interacted with the Permanent Secretary (Budget and Economic Affairs), Ministry of Finance (MoF); the Country Representative, World Bank (WB); the President of the Bankers Association of Zambia (BAZ); the Head of the Economics Department, University of Zambia (UNZA); the Executive Director, Zambia Institute for Policy Analysis and Research (ZIPAR); and the President of the Economics Association of Zambia (EAZ). The findings by your Committee are summarised hereunder.

#### 5.1 Understanding of the Fiscal Deficit

Your Committee was informed that the fiscal deficit should be understood as the difference between revenue and expenditure, typically expressed as a percentage of the County's Gross Domestic Product (GDP). The difference between revenue and expenditure could then be financed through concessional and non-concessional borrowing, among others. Whereas concessional borrowing was accompanied by conditionalities that might not be in line with the Government priorities, non-concessional loans came at a higher interest cost and could be accessed from multilateral institutions, foreign and domestic markets.

#### 5.2 Drivers of Fiscal Deficits in Zambia

Your Committee was informed that a number of factors were responsible for the record high fiscal deficit recorded in the last two years. Some of these factors are highlighted hereunder.

#### ***a. Public Sector Wage Bill***

Your Committee was informed that the public sector wage bill carried an especially large weight in the deficit. Personal emoluments as a share of GDP reached 8.2 *per cent* of GDP in 2013, and jumped to 11.1 *per cent* of GDP in 2014 following the untypically high wage adjustments for public sector workers. The Government's planned recruitment of teachers, health personnel and agriculture extension workers in the short to medium-term would further put pressure on the wage bill.

#### ***b. Public Infrastructure***

In its quest to prioritise the construction and rehabilitation of public infrastructure, the Government's spending on non-financial assets, mainly investments in road infrastructure, increased to 6.7 *per cent* of GDP in 2013 from 3.4 *per cent* of GDP in 2011. While the Government planned to spend K2.5 billion on road infrastructure in 2013, there was a budget overrun amounting to K3.6 billion.

#### ***c. Government Subsidies***

The Governments provision of fuel subsidies was one of the major drivers of deficit. Although there was no budget line, the Government spent K1.6 billion on fuel subsidies in 2013. In addition, the Government continued to spend more than the allocated budget on the Farmer Input Support Programme (FISP) and the Food Reserve Agency's (FRA) strategic food reserves budget for the purchase of maize. During the 2013/2014 agricultural season, the Government purchased more maize than the planned 500, 000 Mt strategic reserves thereby putting pressure on the Treasury. In absolute terms, the Government spent K1.1 billion against the budgeted K345 million.

#### ***d. Lower than Planned Revenues***

On the revenue side, there had been notable underperformance in domestic revenue collection in the recent years. In 2013, with the exception of the Value Added Tax (VAT), all domestic taxes underperformed. However, the projected deficit would be higher if outstanding input VAT refunds held by the Zambia Revenue Authority due to non-compliance with VAT rules on Export verification were netted out of domestic revenues. As at September 2014, the figure for the refunds amounted to K4.3 billion or 2.6 percent of GDP.

Your Committee was informed that domestic revenues in 2013 amounted to K24.5 billion and were below target by 1.0 percent largely on account of lower collections on Income Tax. Company Income Tax underperformed by 40 percent on account of lower mining tax revenues. Mineral royalties, customs and excise duties and grants were also lower than planned.

Your Committee was further informed that based on preliminary data up to October 2014, there had been a turnaround in the revenue performance compared to 2013. Domestic revenue was 7.1 percent higher than projected during the period January to October 2014. The improved performance in domestic revenue and reduced expenditure had led to the lower budget deficit expected in 2014.

### **5.3 Implications of Fiscal Deficits on the Economy**

#### ***a. Deficit and debt accumulation***

Your Committee was informed that the recent increase in the fiscal deficit in Zambia resulted in a higher stock of debt. Zambia's debt had substantially grown as a result of the recent budget deficit increasing to 30.2 percent of GDP in 2014 from 20.6 in 2011.

The stock of domestic debt increased from 12.3 *per cent* of GDP in 2011 to 14.6 *per cent* of GDP in 2014, while the stock of external debt increased from 8.3 *per cent* in 2011 to 17.8 *per cent* of GDP in

2014. The rise in debt stock had consequently led to increased interest payments from 0.9 percent of GDP in 2011, to 1.9 percent of GDP in 2014, and was expected to rise further to 2.2 percent of GDP in 2015. The increased spending on interest deprived needy sectors of the economy of the required resources. Your Committee noted that the interest payments for both the domestic and external debt in the 2014 national budget were higher than the budget for social protection.

***b. Deficit and Current Account***

The increase in the fiscal deficit in the last few years might have in part led to the reduction in the current account surplus which decreased from 5.9 per cent of GDP in 2010 to 0.7 per cent of GDP in 2013 when the fiscal deficit reached a record high.

***c. Deficits and the Crowding out of the Private Sector***

Your Committee was informed that the increase in the short-term interest rates and the decline of the private sector growth had been the most visible effects of the expansion of the budget deficit. Borrowing in the domestic capital market was a major means through which the Government could finance the deficit. As the supply of available funds was not infinite, the increased demand for funds by the Government pushed up short-term interest rates. In this regard, yields on new debt rose sharply during 2013 and 2014 for all maturities of treasury bills and the Government bonds. Year-on-year growth in domestic credit to the private sector fell to 13 percent in December 2013 from 38 percent in December 2012. Credit extension remained constrained in 2014, but growth had recovered to 23 per cent by October.

The increase in domestic borrowing to finance the fiscal deficit consumes domestic private savings available for private sector lending. In turn, the smaller residual pool of loanable funds in the market raised the cost of capital for private borrowers, reducing private investment demand and hence capital accumulation and growth. With relatively shallow financial markets and with most firms falling in the category of Micro, Small and Medium Enterprises (MSMEs) which had limited access to international finance, domestic debt issuance could lead to crowding-out of private lending.

## **5.4 Financing the fiscal deficit**

Your Committee was informed that until recently, the Government had been relying on concessional and non-concessional loans from multilateral and bilateral institutions such as the World Bank, International Monetary Fund (IMF) and other cooperating partners to finance the fiscal deficit. However, in 2010, the World Bank reclassified Zambia as a lower middle income country implying that Zambia had now become richer than before. As a consequence, bilateral and multilateral financiers were no longer willing to extend concessional loans to Zambia, preferring to direct resources to needy countries in the lower income bracket. With the unpredictability and dwindling of traditional sources of income over the years, the Government had had to diversify its financing sources by resorting to commercial borrowing both from domestic and external markets, among others, through the issuance of sovereign bonds.

Zambia had so far successfully issued two Eurobonds amounting to US\$1.750 billion in total. The country issued its debut 10-year US\$750 million international sovereign bond on 13<sup>th</sup> September, 2012. The Eurobond issuance, which had a coupon rate of 5.625%, was oversubscribed by more than 15 times. This led the country to increase the initially planned amount of US\$500 million to US\$750 million, with the excess funding allocated to additional investment projects. In order to augment funding to the selected investment projects under the first Eurobond, the Government again successfully issued a second Eurobond amounting to US\$1 billion in 2014 at a coupon rate of 8.5% which was oversubscribed by only US\$ 4.5 billion. While the former showed high level of investor confidence at relatively lower interest rates, the latter showed some degree of waning investor

confidence. In total, \$128 million would be paid in annual interest to service these debts up until 2022 when the first bond would be due for pay back.

## **5.5 Concerns Raised by Stakeholders**

Stakeholders who appeared before your Committee raised some concerns regarding the fiscal deficit in Zambia. Some of the concerns are highlighted here under.

### ***a. Unplanned Expenditures***

Some stakeholders were concerned that expenditure on a number of budget items was much higher than planned. They cited expenditure on the Food Reserve Agency (FRA), Farmer Input Support Programme (FISP) and fuel subsidies which were higher than planned. They worried that failure by the Government to stick to the budget plans had serious consequences on the performance of the budget. This might lead to excessive debt accumulation, erode investor confidence and stifle economic growth.

### ***b. The Value Added Tax (TAX) Rule Number 18***

Most of the stakeholders were concerned about the failure by the Government to amicably resolve the impasse with mining companies regarding the Value Added Tax (VAT) Rule Number 18. They contended that failure to find a lasting solution would continue to give the impression that domestic revenue had performed well when in actual fact it had not. They argued that the stringent requirements on VAT refunds introduced in 2013 run counter to standard international practice and undermine the investment climate. They argued further that it transforms the VAT from its intended purpose of taxing consumption into a tax on exports.

### ***c. Financing the Deficit***

Most of the stakeholders were concerned that financing of the fiscal deficit from domestic resources was higher than planned. The fear was that if the Government overly depended on domestic borrowing to finance the deficit, it might lead to crowding out of the private sector.

### ***d. Consumption Expenditure***

Most of the stakeholders lamented that the fiscal deficit was mainly driven by consumption expenditure such as personnel costs and subsidies. They noted that because of its size, the public sector wage bill carried an especially large weight on the deficit. Personnel costs made up over half of the Government's current expenses and in 2014 were equal to 9.7 per cent of GDP, up from 7.3 per cent of GDP in 2012. They were further concerned that fuel subsidies, fertilizer subsidies and maize purchases were key drivers of the fiscal deficit. They argued that empirical evidence has shown that farm subsidy programmes were not effective at promoting rural development, poverty reduction and competitiveness. The high cost of these programmes limited the fiscal space for productive investment in the agriculture sector. They proposed instead, investments in rural roads, integrated border management and agricultural extension services.

### ***e. Increase in Interest Payments***

Some stakeholders worried that spending on interest payments had more than doubled in the past two years and was projected to reach K3.6 billion in 2014. The growth in interest paid on domestic debt in 2014 accounted for most of this increase and was equal to 7.0 per cent of the deficit. This reflected both the sharp growth in the stock of the Government securities and rising interest rates. Yields on the 364-day Treasury bill were 20.49 percent in December 2014 auctions which is 481 basis points higher

than in December 2013 and 875 basis points higher than in December 2012. The increase in the interest rates would continue to put pressure on the Treasury.

***f. Unstable Exchange Rate Movements***

Most of the stakeholders were concerned about the failure by the Government to arrest the continued depreciation of the Kwacha. The depreciation increased the cost in Kwacha terms of servicing the debt, fuels inflation and generally increases the cost of living among the ordinary Zambians since Zambia is an overly import-dependent economy. Some stakeholders worried that the country has continued to import most of the products including those where the country has comparative and competitive advantage. They contended that there was urgent need to enhance export revenue through value addition as a way of arresting the problem of unstable exchange rate movements in the long-term.

***g. One-off Payment of Eurobonds***

Stakeholders were concerned that the Eurobonds would be redeemed in a one-off payment when the debts fall due. They worried that such a requirement posed a serious risk to the Country in the event of a large shock to export revenue in 2022 and 2024 which would push foreign debt service obligations above conventional thresholds.

## **5.6 Committee's Observations and Recommendations**

After carefully considering the subject, your Committee makes the observations and recommendations set out hereunder.

***a. Public-Private Partnerships (PPP)***

Your Committee observes that PPPs are a way of delivering and funding public services using a capital asset where project risks are shared between the public and the private sector. There is increasing interest in this financing modality, which features prominently in several national development strategies. However, in Zambia the PPP concept is still being developed and nurtured despite Zambia's huge infrastructure deficit. Your Committee is aware that restricting funding options to bonds only in the wake of declining concessional loans may be costly.

In light of the above, your Committee recommends that the Government should carefully assess its resource capacity and financing constraints in weighing the weaknesses and strengths of various sources of funding. It further recommends that wide options such as Public Private Partnerships (PPPs) should be explored in filling the expenditure gap. The PPPs can effectively work on roads through road tolls, hydropower and the garbage collection activities to mention a few.

***b. Revenue Mobilisation Measures***

Your Committee observes that the Government revenue, excluding grants, of about *17 per cent* of GDP in 2013 and 2014 was rather low. It notes that increasing government revenue is certainly important to reduce the deficit. The low tax revenue was due to tax exemptions, inefficiencies in the tax administration and other tax challenges such as tax planning activities by Multinational Corporations (MNCs).

In light of the above, your Committee recommends that the Government should implement comprehensive tax reforms that would improve compliance and efficiency in tax administration. There is also need to broaden the tax base by formalising the informal sector thereby bringing them in the tax net.

### ***c. Fiscal Consolidation***

Your Committee notes that while Zambia's fiscal deficit has been increasing, there are no deliberate measures towards fiscal consolidation. It is worried that the increasing deficits may in the long run erode investor confidence which may have adverse repercussions on the performance of the economy. It notes that public expenditure on salaries, new recruitments and pensions was likely to increase particularly if the wage freeze and the retirement age are reversed. Further, it notes that expenditure towards fuel subsidies and the purchase of maize through the FRA and the FISP has continued to be above the planned levels.

Therefore, your Committee recommends that Government should implement measures to contain the fiscal deficit by limiting the public sector wage bill and streamlining expenditures towards priority programmes. This would mean limiting expenditure on maize marketing, ensure cost reflective fuel pricing and rationalise capital expenditure.

### ***d. Strengthen Investment Appraisal System***

Your Committee observes that some of the projects being implemented by the Government have low rates of return and as such, are economically unviable to invest considerable amounts of borrowed money. It notes that a total of \$128 million in interest has to be paid annually on the Eurobonds issued with principal to be repaid at maturity in 2022 and 2024 for the \$750 million and \$ 1 billion Eurobonds, respectively.

In this regard, your Committee recommends that a comprehensive investment appraisal should be conducted during selection of projects devoid of political expedience. This should be coupled with continuous monitoring and evaluation of the utilisation of borrowed funds from international capital markets to ensure that the selected projects generated resources commensurate with servicing the respective debt obligations. Your Committee further recommends that social sector programmes should be funded through domestic revenue.

### ***e. Resolution of the VAT Refunds***

Your Committee observes that the impasse over refund of VAT to exporters reduced the size of the 2014 budget deficit, but resolving this impasse would affect the Government's future financing needs. The stock of unpaid VAT refund claimed was estimated to be K4.3 billion at year's end which was equal to half the size of the deficit. Further, your Committee observes that the stringent requirements on VAT refunds introduced in 2013 run counter to standard international practice, undermine the investment climate, and transform the VAT from its intended purpose of taxing consumption into a tax on exports.

In this regard, your Committee recommends that the Government should find a lasting solution to the standoff on the VAT refunds with exporters to ensure predictability of investment policies and renewed investor confidence.

### ***f. Rebalancing Discretionary Spending away from Maize and Fuel Subsidies***

Your Committee observes that maize and fuel subsidies take a huge proportion of the budget leaving limited resources for poverty reduction programmes.

In this regard, your Committee recommends that the Government should rebalance spending from maize and fuel subsidies towards public sector investments and services that stimulates inclusive growth and contribute more strongly to poverty reduction. Investment in rural roads, integrated border management, agricultural extension services, and in extending the tourism infrastructure into new

areas are critically needed to overcome binding constraints to pro-poor growth in agriculture, tourism and trade.

## PART II

### 6.0 Utilisation of the US\$750 Million Eurobond

In September 2012, the Government made a maiden appearance on the sovereign bond market through the accession of the US\$750 million Eurobond. Table 1 below gives a breakdown of the activities that were planned to be undertaken from the proceeds of the bond.

**Table I: Allocation of the Eurobond Funds**

No	Institution	Project	Allocation (\$)
1	ZESCO Limited	Power Distribution Project	69,000,000.00
2	ZESCO Limited	Kafue Gorge Lower Hydro Power Project	186,000,000.00
3	Zambia Railways Limited	Track Rehabilitation & Purchase of rolling	120,000,000.00
4	National Road Fund Agency	Refinancing on Formula One Road Project	145,000,000.
5	National Road Fund Agency	Kitwe - Chingola Dual Carriageway	100,000,000.00
6	Road Development Agency	Pave Zambia Programme	65,000,000.00
7	Development Bank of Zambia	Credit Line to SMEs	20,000,000.00
8	Ministry of Health	Modernisation of Tertiary Hospitals	29,000,000
9	Discount Premium		14,600,000
10	Transaction costs		1,400,000
	<b>TOTAL</b>		<b>750,000,000</b>

Many stakeholders were concerned that the failure by the Government to properly utilise and account for the Eurobond funds would have adverse effects on the economy. Your Committee, therefore, resolved to monitor the release and utilisation of the funds. The objectives of the study were to-

- (a) appreciate the efficiency in the releases of funds to respective projects;
- (b) compare the utilisation against the releases of funds;
- (c) appreciate the project cycle of the beneficiary projects;
- (d) appreciate the challenges in the utilisation of the funds; and
- (e) recommend the way forward.

In order to appreciate this subject fully, your Committee interacted with the Permanent Secretaries of the following Ministries: Finance (MoF); Transport, Works, Supply and Communications (MTWSC); Health (MoH); and Mines, Energy and Water Development (MMEWD). Your Committee also interacted with the Chief Executive Officers of the following institutions: Development Bank of Zambia (DBZ); Road Development Agency (RDA); Zambia Railways Limited (ZRL); and ZESCO Ltd. The findings of your Committee regarding the progress of project implementation and the utilisation of the funds by various recipient institutions are summarised hereunder.

#### 6.1 ZESCO Limited

Your Committee was informed that ZESCO Limited was allocated a total of US\$255 million for two projects: US\$69 million for the Power Distribution Project while US\$186 million was for the Kafue Gorge Lower Hydro Power Project.

##### i. Power Distribution Project

Your Committee was informed that under the Power Distribution Project, ZESCO Limited was aiming to rehabilitate its distribution network in order to match the increased power generation capacity, as well as improve the quality of service. The Power Distribution Project portfolio

consisted of thirty-two (32) individual components or sub-projects, twenty-five (25) of which were in Lusaka Division. The power distribution project once delivered was expected to result in the following outcomes:

- (a) improvement in the reliability of power supply in the project target areas;
- (b) increase in capacity to facilitate access to electricity services;
- (c) reduction in distribution losses, thus improving the efficiency of power distribution; and
- (d) overall improvement in the service delivery.

Your Committee was informed that as at end of November 2014, a total of eighteen (18) contracts worth USD 50.82 million had been signed. A further three (3) tenders were at various stages of the procurement process. Of the eighteen (18) contracts under execution, five (5) of them had been completed. These were the upgrading of Ngwerere Substation, construction of a workshop substation at ZESCO Head Office, construction of Heroes Stadium Switching Station, construction of Makeni Switching Station and replacement of 11kV switchgear at Avondale Substation. The total cost of completing these projects was US\$16,396,624.05. The pace of implementation, thus far, indicated that the balance of US\$18.18 million which was not yet committed might take a long time before it was spent. This might be the case because procurement processes in the project were lengthy.

#### *ii. Kafue Gorge Lower Hydro Power Project*

Your Committee was informed that an allocation of US\$186 million was made to ZESCO Limited as the Government equity in a Special Purpose Vehicle (SPV) in which private sector investors would participate. This was because the project would be developed through Public Private Partnership (PPP). The SPV aimed to raise equity funding from both the Government and private sector investors and debt to mobilise US\$2 billion which was the estimated project cost.

Your Committee was informed that the current allocation of \$186 million would not be sufficient to meet the required equity injection. Based on the existing shareholding proposal, and subject to any amendments to it, the shortfall in equity contribution was estimated at \$174 million as illustrated in the workings below.

<b>Breakdown of the Funds</b>		<b>US\$</b>
<b>Estimated total project cost</b>		<b>2,000,000,000.00</b>
<b>Financing Structure:</b>		
<b>Equity (30%)</b>		<b>600,000,000.00</b>
<b>Debt (70%)</b>		<b>1,400,000,000.00</b>
		<b>2,000,000,000.00</b>
<b>Equity/GRZ (60%)</b>		<b>360,000,000.00</b>
<b>Other Partners</b>		<b>240,000,000.00</b>
		<b>600,000,000.00</b>
<b>ZESCO Equity</b>		<b>360,000,000.00</b>
<b>2012 Eurobond allocation</b>		<b>186,000,000.00</b>
<b>Estimated Balance due</b>		<b>174,000,000.00</b>

The draw-down of the US\$186 million which is the Government equity contribution had been very slow. Of the amount, only US\$671,290.00 had been spent by the end of 2014. The amount was spent on three contracts of which the contract with Lahmeyer International, the reviewer of the Sino-hydro

Feasibility Study Report, had been fully executed at the cost of US\$142,897.00.

Your Committee was informed that the Kafue Gorge Power Project was behind schedule due to the change in policy on the procurement of the developer. The amount provided by the Treasury had been adequate in meeting fees to the consultants. However, there might be a challenge in raising the US\$1.5 billion which would be paid to the Engineering, Procurement and Construction (EPC) contractor. The Transaction Advisor was expected to play a significant role in advising the Government and other investors in the SPV in terms of packaging the project for the capital markets.

### *iii. Field-based oversight activities*

In order to appreciate the works being undertaken by ZESCO LTD on the ground, your Committee undertook a tour to Kafue Gorge Lower Hydropower Station. The decision to tour this project was informed by the large amounts of funds allocated to it and the expected benefits to the economy once the 750 MW of power were brought on stream. Your Committee developed a comprehensive questionnaire which was a useful tool in monitoring the projects. By employing this tool, your Committee was able to get credible information through triangulation between key respondents who were the Government officials, contractors and the local communities.

The findings arising from the tour showed that preparations for the commencement of the Kafue Gorge Lower were underway and the contractor was expected to be engaged by October 2015. There have been some delays in the commencement of the main project works and, therefore, a delay in utilisation of the US\$ 186 million funds from Sovereign Bond. The main delay had been due to the change of the procurement process for the Contractor and Equity Partners which had seen the withdrawal of the Memorandum of Understanding between GRZ, Sino-hydro Corporation and China Africa Development Fund. Construction works which were expected to commence in early 2013 had been delayed to allow for a transparent international competitive procurement process especially taking into account the large amounts of funds involved. Expenditures from the Sovereign Bond on the project had so far been in small amounts for consultancy services required for the implementation of the project. A large part of the funds would, however, be consumed as advance payment to the contractor by October/November 2015.

Your Committee was informed that the negative externalities of the project arising from the displacement of the local communities had been adequately addressed. Families who were living around the project area had been relocated, compensated and integrated into other communities.

## **6.2 Zambia Railways Limited**

Your Committee was informed that the Zambia Railways Limited was allocated an amount of US\$120 million to support the rehabilitation of the rail track and rehabilitation and procurement of rolling stock. Zambia Railways allocated US\$81.8 million to rail track rehabilitation and the balance of US\$38.2 million was allocated to rehabilitation of rolling stock.

The focus of the rail track rehabilitation was the replacement of expired wooden and steel sleepers with concrete sleepers over a section measuring 442 km. In addition to the rehabilitation of the main line, Zambia Railways was also rehabilitating the inter-mine network with the aim of re-establishing connectivity of Nchanga and Konkola Mine Plants. Part of this undertaking included works on a 32 km line between the two mining plants. Given the state of disrepair of the line, Zambia Railways was also rehabilitating shunting lines at both Chingola and Nchanga Stations as well as replacing washed away culverts and maintenance of bridges on the line.

In terms of implementation of the various components, significant progress had been achieved in the fourth quarter of 2014 culminating in the utilisation of about US\$96 million whilst the balance of US\$23 million had been committed to suppliers of rolling stock.

### ***i. Rail Track Rehabilitation***

With regard to rail track rehabilitation, a total of 126.47 kilometres was rehabilitated with concrete sleepers. This distance was a combination of various priority sections which were allocated to 32 contractors. Along the line, there were sections which were completely rehabilitated by replacing all the old sleepers with new ones. Notable achievements in this regard were the overhaul of seven (7) locomotives which had since been deployed on the main line and the Nacala Line. The number of wagons rehabilitated was forty-five (45) which included side-tippers to be deployed on the inter-mine network. Some progress was also made in terms of procurement of rolling stock spares and wagons.

Your Committee was informed that Zambia Railways Limited received its share of the Eurobond proceeds in early 2013, but commenced implementation in October, 2013. Zambia Railways Limited spent substantial amounts of time on procurement processes. As a result, it would take in excess of two years to exhaust the entire US\$120 million. This observation took into account that almost all the materials required were imported, including concrete sleepers. For equipment, all the requirements were made abroad and thus, had to be imported with long lead-times.

### ***ii. Inadequacy of the Funds***

Although the US\$120 million Eurobond funds had helped Zambia Railways Limited commence rehabilitation of infrastructure and rolling stock, the amount was far less than what the company considered adequate investment to bring the railway operations to a viable level. According to the company's five year Strategic Business Plan (2014-2018), a total of US\$526.4 million was required for re-capitalisation. To achieve the Strategic Business Plan target of 5 million tons of freight per annum and improved train speed of around 70Km per hour, the company required 4,600 new wagons whose estimated cost was US\$260 million, far in excess of the US\$120 million Eurobond funds. In addition, there were planned new inter-mine projects covering 97.1 kilometres estimated to cost US\$41million.

### ***iii. Green Field Railway Projects***

Your Committee was informed that there were other green field railway projects within the country and of a regional dimension which the company was planning. The projects were the:

- (a) Chipata-Mpika via Petauke (569km);
- (b) Nseluka-Mpulungu via Mbala (191 km);
- (c) North-Western Railway connection to Angola; and
- (d) Mulobezi-Kazungula Railway into Botswana and Namibia.

When the costs of these projects were taken into account, the inevitable conclusion was that Zambia Railways Limited required additional investments to attain the set objectives in the company's Strategic Business Plan.

### ***iv. Field-based oversight activities***

In order to appreciate the works on the ground being undertaken by the ZRL, your Committee undertook a tour to the inter-mine railway under construction. The selection of this project out of a sample of various projects under implementation by ZRL was based on the immense benefits expected in terms of carrying copper concentrates from mines to the smelters thereby, increasing the lifespan of the roads on the Copperbelt. ZRL had started connecting the railway linkages on the inter-mine. Prior to the cancellation of the concession agreement by the Government and the ushering in of ZRL in Sept 2012, the Inter-mine area was neglected resulting in the dilapidation of the rail infrastructure and complete erosion of the customer base.

The recent investment developments in the mines in terms of smelters, concentrators, refineries and other plants did not consider Zambia Railways Limited as their transporter. Therefore, there was no adequate access connectivity links for both off loadings and loadings coupled with lack of handling equipment such as weighing bridges, tipping facilities, offloading and loading equipment. However, ZRL had embarked on a robust revival plan whose main aim was to restore operations on the inter-mines by constructing the rail lines needed to link the mine plants to the rest of the ZRL rail network. The project was also anticipated to remove heavy transport haulage from the roads to railway thereby increasing the lifespan of these roads.

The Zambia Railways had rehabilitated and constructed railways lines to move copper and other minerals from various plants and to transport copper concentrates to the smelters. In the Konkola Plant, your Committee found that the line was operational. A trial run was done using the tippler wagons that were manufactured at Kabwe workshops.

The Zambia Railways was able to transport copper concentrates from Chililabombwe to Chingola after many years of rail inactivity. In the Nchanga Plant, the line was ready for operation and a trial run to transport anodes had been done. The rail, which was a reliable high capacity mode of transport, was being accessed by Konkola Copper mines. ZRL would begin to move more mining raw materials and products at a lower transport rate.

In terms of the benefits of the inter-mine project to local communities, the findings by your Committee shows that more jobs have been created directly and indirectly by ZRL through its implementation of the project.

### **6.3 Road Development Agency (RDA)**

Your Committee noted that an amount of US\$165 million was released for roads through the National Road Fund Agency (NRFA) for the Link Zambia 8000 Programme. Of this amount, US\$100 million was allocated to the project for the upgrading of 45.5 kilometres of the Kitwe-Chingola dual carriageway. The balance of US\$65 million was funding for the Pave Zambia Programme.

In addition to the US\$165 million for the Link Zambia 8000 Programme, an amount of US\$145 million was allocated to the NRFA to refinance the commercial bank loan contracted for the "Formula One" road project in Lusaka urban.

#### ***i. Kitwe-Chingola Dual Carriage Way***

In terms of progress, works on the Kitwe-Chingola Dual Carriage way revealed that as at November, 2014, a total of 13.5 kilometres had been surfaced out of the total length of 45.5 kilometres. Overall physical progress, taking into account work completed prior to surfacing, was at *40 per cent* against the planned target of *53 per cent*. The planned completion date for this project was June, 2016. The Link Zambia 8000 Programme was on course with progress at *15.86 per cent* by November, 2014. For the whole programme, comprising 24 road projects, a total of approximately 390.09 Km of roads had been surfaced out of the 2,460.09Km under construction and rehabilitation.

#### ***ii. Field-based oversight activities***

In order to appreciate what was obtaining on the ground, your Committee visited the following roads under the Link Zambia 8000: Chiawa-Chirundu; Chipata-Vubwi; Chama-Matumbo, Mbala-Nakonde; Kasama-Mporokoso and the Chingola-Kitwe. The findings of your Committee are highlighted hereunder.

*a. Poor Release of Funds*

Works on most of the projects had slowed down and in some cases had completely stalled because of poor releases of funds to the projects. Apart from the Mbala-Nakonde and the Kasama-Mporokoso roads where contractors were found on site, there were little activities taking place on the remaining roads.

*b. Cost Overruns*

Your Committee noted that as a result of non-release of funds to the projects, the contractors who had to meet the cost of maintaining equipment and labour were charging interest on the outstanding amounts for the completed works. This interest had been rising and might reach unsustainable levels, if not addressed on time.

*c. Value for Money*

Your Committee noted that the roads under construction were of high standard especially the Mbala-Nakonde Road and the Kasama-Mporokoso Road. However, they were concerned with the quality of the Vubwi-Chipata Road.

*d. Prioritisation of Roads*

Your Committee noted that the Kitwe-Chingola Road was of high economic importance and as such, required to be given priority to be completed into a dual carriage. Further, if not completed on time, the road poses serious danger to the road users because it is a busy one and has heavy trucks transporting goods such as copper concentrates and anodes.

## **6.4 Development Bank of Zambia (DBZ)**

Your Committee was informed that the Development Bank of Zambia was allocated a total of US\$20 million for on-lending to Micro, Small and Medium Enterprises (MSMEs). As at December 2014, the entire amount had been disbursed to a total of forty-eight (48) enterprises drawn from various sectors.

However, most of the enterprises were based along the line of rail, mainly in Lusaka, Copperbelt, Southern and Central Provinces. There were only two projects outside the line of rail; one in North-Western and another in Luapula Province. The total amount of disbursements at US\$22,532,463 was in excess of the proceeds received by the DBZ from the Ministry of Finance. This implied that the DBZ used its own funds amounting to US\$2,532,463. The fact that the DBZ had to use its own funds to meet the needs of its forty-eight (48) clients was an indication that more funds were required to meet the needs of MSMEs beyond its portfolio.

Your Committee was informed that the MSMEs in the euro-bond-supported portfolio were in different sectors and at different stages of development. While a good number of the MSMEs had been in operation for some time and used the euro-bond facility to refinance existing loans, others were start-ups. Therefore, an impact assessment of the effectiveness of the US\$20 million could not be undertaken effectively at the point.

## **6.5 Ministry of Health (MoH)**

Your Committee was informed that the Ministry of Health was allocated a total of US\$29,397,662 to support the programme for the modernisation of the following tertiary hospitals: University Teaching Hospital; Ndola Central Hospital; Kitwe Central Hospital; and Livingstone General Hospital.

The modernisation programme, which commenced in 2013, included upgrading of some of the Third Level hospitals to teaching hospitals while those at lower levels, that is First and Second, were also scheduled to be upgraded. The upgrading of hospitals was in line with the Ministry of Health National Health Strategic Plan (2011-2015) and the Revised Sixth National Development Plan (R-SNDP, 2013-2016).

By upgrading the hospitals, the Government was aiming to achieve the following objectives:

- (a) improvement of service delivery by provision of tertiary services as close to the people as possible;
- (b) provision of specialist care at the provincial level;
- (c) strengthening the referral system in the country in order to decongest the University Teaching Hospital;
- (d) provision of required infrastructure and equipment to meet medical needs of the many training schools which had been opened and those to be opened in the near future; and
- (e) reduction of referrals of patients abroad through provision of specialised treatment locally.

Your Committee was informed that given the limited funding, the Ministry of Health had phased the implementation of the modernisation programme, initially starting with the four tertiary hospitals. Therefore, the Eurobond funds were just a contribution to the programme. The other funds would come from the Saudi Fund, which had already provided a loan of US\$20 million for upgrading of the UTH, while the balance would be financed through the National Budget.

At the end of 2014, releases of Eurobond funds to the Ministry of Health amounted to K170 million. The first release in 2013 was K78 million while the second funding amounting to K92 million was made in 2014, with an outstanding balance of K34 million on the K204 million. The modernisation programme was an undertaking requiring huge capital investments. As at end of December 2014, the value of commitments was K460,486,994.62 against the confirmed funding amounting to K204,000,000. This implied that the deficit of K256,486,994.62 had to be financed by the subsequent budgets.

#### *i. University Teaching Hospital*

In terms of the civil works component, progress for the UTH was presented in Table 1 below.

**Table 1: UTH**

	<b>WORKS</b>	<b>CONTRACTOR</b>	<b>CONTRACT SUM (ZMW/K)</b>	<b>STATUS</b>
1	Construction of New Adult Medical Emergency Unit	Hua Chang Inv. Ltd	27,013,790.74	Contract Duration 18 months. Works ongoing and contractor doing super structure: 55% Complete
2	Rehabilitation of the Roads at UTH	China Jiangxi Invest. Ltd	33,819,092.90	Contract Duration 12 months: Ongoing 90% Complete
3	Construction of New Double Storey Carpark	China Jiangxi Invest. Ltd	11,220,280.15	Contract Duration 6 months: Ongoing 50% Complete
4	Provision of Architectural, Surveying and Quantity and	Spectrum Architectural Consultants	6,000,000.00	Supervision of works ongoing.
		<b>TOTAL</b>	<b>K 78,053,163.79</b>	

*ii. Ndola Central Hospital*

In terms of the civil works component, progress for the Ndola Central Hospital is presented in Table 2 below.

**Table 2: Ndola Central Hospital**

	<b>WORKS</b>	<b>CONTRACTOR</b>	<b>CONTRACT SUM (ZMW/K)</b>	<b>STATUS</b>
1	Provision of Architectural, Quantity Surveying and Engineering Services for the Modernisation of Ndola Central Hospital	Shelter Designs	6,000,000.00	Contract in the process of being signed
2	Construction of Psychiatric Ward	Jearmy Enterprises	14,539,522.36	Clearance obtained from Ministry of Justice to sign the contract. Contract award done. Construction to commence in September, 2014
3	Rehabilitation & Installation of CT-Scan		500,000.00	Contract Duration 12 months: Ongoing
		<b>TOTAL</b>	<b>K 21,039,522.36</b>	

*iii. Kitwe Central Hospital*

The progress on the civil works component for Kitwe Central Hospital was presented in Table 3 below.

**Table 3: Kitwe Central Hospital**

	<b>WORKS</b>	<b>CONTRACTOR</b>	<b>CONTRACT SUM (ZMW/K)</b>	<b>STATUS</b>
1	Provision of Architectural, Quantity Surveying and Engineering Services for the Modernisation of Kitwe Central Hospital	Shelter Designs	6,000,000.00	Contract in the process of being signed
2	Replacement of Elevators		2,000 000.00	Ongoing
3	Rehabilitation & Installation of CT-Scan		500, 000.00	Contract Duration 12 months: Ongoing
		<b>TOTAL</b>	<b>K8,500,000</b>	

*iv. Livingstone General Hospital*

Your Committee was informed that a total of K3,800,000 was spent on the rehabilitation of laboratories and replacement of elevators for Livingstone General Hospital. Another amount was spent on the installation of a CT-Scan. Thus far, expenditure of Eurobond funds at the Livingstone Hospital was limited to the procurement of equipment. These funds were combined with other Government funds allocated under the World Tourism Organisation (WTO) General Assembly budget.

*v. Field-based oversight activities*

In order to appreciate what was obtaining on the ground, your Committee undertook a tour to the University Teaching Hospital projects. The findings of your Committee are set out below.

*a. Construction of an ultra-modern car park*

The Construction of an ultra-modern car park which was being undertaken by China Jiangxi Invest Ltd had a contract sum of K11,220,280.15. The amount paid was K 4,520,019.12 leaving a balance of K6,700,261.03. The contract duration was 6 months and the project was 50 per cent complete.

*b. Access roads*

The construction of the access roads was being undertaken by China Jiangxi Invest Ltd. The project which had a contract sum of K 33,819,092.90 was progressing well. The amount paid was K 18,650,961.34 leaving a balance of K15,168,131.56. The contract duration was 12 months and the project was 90 per cent complete.

*c. Construction of new adult medical emergency unit*

The construction of the new adult medical emergency unit which had a contract sum of K 27,013,790.74 was progressing well. The Contractor, Hua Chang was found on site. The amount released so far was K 11,918,824.28 leaving a balance of K 15,094,966.46. The contract duration was 18 months and the project was 55 per cent complete.

## **6.6 Challenges of implementing Eurobond Funded Projects**

The challenges encountered with regard to the utilisation of the Eurobond are set out hereunder.

*i. Delays in project preparation*

Your Committee was informed that one of the major challenges was delays in project preparation and implementation by implementing agents. There were also delays in the procurement of goods and services. Site inspections revealed that many recipient institutions did not have ready project documents, civil works designs and project implementation plans when they received the Eurobond funds. Initially, the funds were planned to be spent in the 2013 national budget implementation period, but it had taken much longer for the funds to be absorbed. The case in point being ZESCO Limited which was allocated an amount of US\$186 million in 2013 for the Kafue Gorge Lower Power project of which only payments amounting to US\$671,290.00 had been paid to consultants by the end of 2014. As a result, ZESCO Limited maintained large balances in commercial banks. Subsequently, ZESCO Limited secured the services of a fund manager to invest the funds until payments could be made.

*ii. Inadequacy of funds*

Following submission from, and subsequent visit to, Zambia Railways Limited over the US\$120 million and the Kafue Gorge Lower allocation of \$186 million, it was clear that the funds were not sufficient to meet their required business plan budget for ZRL and required equity injection for ZESCO. This was also evident from the roads where construction had stalled such as the: Chipata-Vubwi, Kitwe-Chingola, Chipata-Chadiza and Chirundu-Chiawa Roads. The situation was also the same with the University Teaching Hospital where the construction of the car park had stalled because of inadequate funds.

## **6.7 Committee's Observations and Recommendations**

After carefully undertaking the study, your Committee makes the observations and recommendations set out hereunder.

***a. Kafue Gorge Lower Hydropower Station***

Your Committee observes that the construction of Kafue Gorge Lower Hydropower Station is a very important project that needs to be completed in time considering the current power deficit in Zambia and in the region.

In this regard, your Committee recommends that funds be released to fulfil the equity requirement by ZESCO in the SPV.

***b. Inter-mine connection***

Your Committee observes the inter mine connection is one of the key projects that is economically viable and may decongest the road on the Copperbelt. It observes that ZRL does not have adequate funds to fully implement this project.

In light of this, your Committee recommends that the Government should as a matter of urgency allocate the remaining balance to ZRL for it to fully implement the inter mine railway project.

***c. Outstanding amounts on various projects***

Your Committee observes that there are various projects that have stalled across the country as evidenced from the findings of your Committee. Your Committee is concerned that the continued delay in the release of the funds will increase the costs through interest accumulation.

Since commitments have already been made, your Committee recommends that the Government should take stock of all outstanding payments with a view to liquidating them. In addition, further funds should be raised to complete the outstanding works to mitigate the costs arising from mobilisation and remobilisation by contractors.

**PART III**

**7.0 Conclusion**

Your Committee wishes to pay tribute to all stakeholders who appeared before it and tendered both oral and written submissions. It also wishes to thank you, Mr Speaker, for affording it the opportunity to serve on the Committee for the year 2015. Your Committee also appreciates the services rendered by the office of the Clerk of the National Assembly. Your Committee is very hopeful that the observations and recommendations contained in this Report will go a long way in improving the economy of Zambia.