Program Information Document (PID)

Concept Stage | Date Prepared/Updated: 10-Apr-2022| Report No: PIDC34048

BASIC INFORMATION

A. Basic Project Data

Country	Project ID	Project Name	Parent Project ID (if any)
Zambia	P174911	Zambia Macroeconomic Stability, Growth and Competitiveness DPO (P174911)	
Region	**Estimated Board Date**	**Practice Area (Lead)**	**Financing Instrument**
Eastern and Southern Africa	Jul 28, 2022	Macroeconomics, Trade and Investment	Development Policy Financing
Borrower(s)	**Implementing Agency**		
Ministry of Finance and National Planning	Ministry of Finance and National Planning		

Proposed Development Objective(s)

The program development objective is to support reforms to restore macroeconomic stability, debt sustainability, and underpin a private-sector-led recovery and growth path.

Financing (in US$, Millions)

SUMMARY

Total Financing	275.00

DETAILS

Total World Bank Group Financing	275.00
World Bank Lending	275.00

Decision

The review did authorize the preparation to continue

B. Introduction and Context

Country Context

1. **Zambia's economic activity has picked up in 2021, driven by recovery from initial COVID-19 shocks and lockdown measures, higher copper prices, and post-election rise in market confidence**. Higher copper prices, improved rainfall pattern, and the post-election rise in market confidence have contributed to an expansion of 3.6% in 2021. The COVID-19 pandemic considerably worsened Zambia's macroeconomic imbalances and Zambia became the first Sub-Saharan African country to default on the Eurobonds in the midst of the COVID-19 crisis in 2020. Following its election in August 2021, the new government moved swiftly to declare that its top policy priority is to restore macroeconomic stability and promote sustainable recovery and growth, including through early agreement with the IMF on a program and conclusion of debt restructuring under the Common Framework. Reforms to restore fiscal and debt sustainability, improve agricultural productivity and access to markets, improve the operational efficiency of energy sector, and enhancing private sector access to finance are critical to promote recovery and a sustainable growth path.

2. **Zambia's macroeconomic policy framework is considered adequate for this operation, with the debt service standstill expected to be followed by debt treatment under the G-20 Common Framework (CF).** Government is establishing an exceptionally positive reform track record through high quality engagement and early reform actions. Following years of poor fiscal management, the approved 2022 budget and the 2022-24 medium-term budget framework provides a clear path of fiscal adjustment. Correspondingly, the government has kept a flexible exchange rate regime; and monetary policy maintains its focus on managing inflation whilst taking due consideration of financial stability issues. Government has demonstrated strong commitment by frontloading difficult policy actions including reforms to reduce oil and agricultural subsidies, while protecting social spending. Stakeholder outreach has also included the recent Eighth National Development Plan, presentations by the Minister of Finance to Parliament, and transparent and timely reporting of debt detailed information. The government will maintain the debt service standstill to all creditors, expect multilaterals, until an agreement is reached under the CF which brings back debt to sustainable levels.

Relationship to CPF

3. **The proposed DPO supports the objectives of the World Bank's Country Partnership Framework (CPF) for FY19-FY23 for Zambia.** Both the CPF and the DPO are underpinned by Zambia's Vision 2030 and the Eighth National Development Plan (8NDP) for the period 2022-26. Vision 30 articulates Zambia's aspiration to become a prosperous middle-income nation by 2020 and the 7NDP emphasizes the interlinkages between key sectors of the economy. The CPF has three focus areas: (i) more even territorial development: opportunities and jobs for the rural poor; (ii) public services and social projection for job participation; and (iii) institutions for resilience. The proposed DPO is listed as a key engagement under Focus Area III (Institutions for Resilience) in the CPF to increase fiscal and financial fitness. The DPO also helps to advance several objectives under the first and second focus areas in the CPF including a more productive agriculture sector, increased access to and quality of energy sector, and increased coverage and improved efficiency of social protection programs. The four pillars of this DPO (restoring fiscal and debt sustainability; increasing farmer productivity and access to agricultural markets; ensuring sustainable access to energy; and enhancing private

sector development and access to finance) are expected to lead to: (a) stronger fiscal and debt management for sustainable public expenditure on priority sectors; (b) improved policies to support accelerated and more inclusive agricultural development; (c) improved sustainable access to electricity and (d) enhanced private sector access to finance, with a special focus on SMEs.

C. Proposed Development Objective(s)

4. The program development objective is to support reforms to restore macroeconomic stability, debt sustainability, and underpin a private-sector-led recovery and growth path.

Key Results

5. The supported reforms complement and reinforce each other to restore fiscal and debt sustainability, address macroeconomic imbalances, and foster private sector-led economic growth. Improving the transparency and accountability by which debt is contracted are expected to contribute to better government debt management, ultimately lowering the risk of debt distress. Strengthening commitment controls and overall fiscal governance will improve budget credibility and fiscal discipline. Migrating to a cost-efficient electronic based agro-input system will contribute to diversification of the sector, thereby enhancing resilience and creating more fiscal space for investments in rural/agricultural public goods. Rationalizing market interventions and renewing the role of the Food Reserve Agency will help ensure that maize markets work more effectively and support growth of agriculture traders and exporters. Removing subsidies and improving efficiencies in the petroleum supply chain are expected to help address current fiscal imbalances and macroeconomic stability while improving ZESCO's financial sustainability. Establishing the Financial Stability and Monetary Policy Committees will strengthen Bank of Zambia's ability to monitor and respond to financial stability developments in the economy. Lowering costs of regulatory compliance will increase competition and investor confidence leading to higher investments and contributing to job growth. All together, these reforms are expected to restore fiscal and debt sustainability, improve agricultural productivity and access to agricultural product markets, improve the operational efficiency of energy sector, and supports the private sector development and job creation efforts of the Government through supporting legislations, regulation and institutions that are conducive to the operation of businesses, with a special focus on SMEs.

D. Concept Description

6. **The proposed Development Policy Operation is the first in a programmatic series to help Zambia restore macroeconomic and debt sustainability and promote private-sector-led inclusive growth.** The operation is for SDR XX million [US$275 million equivalent] and was requested by Government in support of their Economic Recovery Program (ERP) and the Seventh National Development Plan (7NDP). It is part of the World Bank's multi-sectoral response to help Zambia restore macroeconomic stability following the COVID-19 and debt crises, and to shift to a more sustainable and inclusive growth path. The Program Development Objectives will be achieved through policy and institutional reforms aimed at: 1) restoring fiscal and debt sustainability; 2) increasing farmer productivity and access to agricultural markets; 3) ensuring sustainable access to energy; and 4) enhancing access to finance and private sector development.

7. **The four pillars of this operation are strongly aligned with government's priorities to restore macroeconomic**

stability and lift the economy to a higher and more inclusive growth path. Pillar A will ensure that fiscal and debt management reforms take place to free-up resources for pro-poor and priority sector expenditure, especially for education, health and social protection. It will also ensure that there is a shift to a more sustainable fiscal and debt stance, to ensure sustainability and predictability of public investment. Pillar B provides support to planned agriculture reforms as part of a wider shift to inclusive growth and to boost the non-copper economy. Pillar C aims to improve the operational efficiency of the energy sector both to boost sustainable access and help address current fiscal imbalances and macroeconomic stability by removing subsidies and improving efficiencies in the petroleum supply chain. Pillar D will support the private sector development and job creation efforts of the Government through relevant legislation, regulations and institutions.

8. **The proposed DPO supports Zambia to restore debt sustainability and foster private sector led economic growth that lifts more Zambians out of poverty.** Resolving the severe macroeconomic imbalances that built up over the past decade and culminated into a debt crisis will require a combination of ambitious fiscal adjustment, structural fiscal reforms, and public debt restructuring. The government has shown commitment to undertake these significant economic reforms, including to improve the efficiency and inclusiveness of public spending and to promote a private sector-led and export-oriented growth path. To bear fruits on debt sustainability and growth, these reform efforts will need to be complemented by comprehensive and timely debt restructuring. The policy actions proposed under this operation (fiscal and debt management) will directly support this Government in meeting these challenges. Furthermore, the fruition of an IMF program would help ensure the Government is fully supported in its plan to improve fiscal sustainability.

E. Poverty and Social Impacts, and Environmental, Forests, and Other Natural Resource Aspects

Poverty and Social Impacts

9. **The overall poverty and social impacts of reforms supported by the DPO are expected to be positive as the Government will be able spend additional resources on priority sectors and increases investment.** However, these intended impacts will depend on how well the authorities target social expenditures and whether investments are well selected and implemented. Benefits are more likely to be felt over the medium-term. The proposed reforms of the Farmer Input Subsidy Program (FISP) are designed to limit the potentially negative impact of the reduction of program's beneficiary caseload, by targeting smaller farmers. During the preparation of the DPO, the impact of these changes on the very poor will be further explored through simulation models. Government has scaled-up its social protection measures while it cuts back on fuel and electricity subsidies. Some poor people (especially those in urban areas) will be impacted by higher fuel prices (for example via higher costs of public transport) but increases in the Social Cash Transfer Scheme (SCTS). and their coverage is expected to cushion this impact. The reallocation of budgetary savings through reform of regressive subsidies on fuel, electricity and agriculture, as supported under Pillars B and C, to the expansion of poverty-targeted and well-evaluated social spending will support pro-poor outcomes.

Environmental, Forests, and Other Natural Resource Aspects

10. **The proposed operation is expected to have positive environmental impacts, overall.** The operation will strengthen resilience against climate change impact and vulnerability, with positive effects stemming from increased

budget for agricultural public goods. This will allow more explicit investments in climate smart agricultural production systems, and improved agricultural production and value added. Agricultural diversification, as supported by the e-voucher program is expected to enhance resilience of agro-ecosystems by providing ecosystem services and is expected to enhance household resilience to climate change related shocks. The changes to the FISP, especially the e-voucher program, will de-emphasize maize production and facilitate the acquisition of inputs for other crops or livestock and fish farming. Supporting productive diversification and the potential for application of good practices such as intercropping and rotations is considered to enhance the resilience of production systems and to provide a range of ecosystem services. Another effect of the e-voucher system may be a reduction in fertilizer use, to the benefit of other inputs, such as improved seeds, small machinery, plant protection and vaccination materials. E-voucher system will allow a timely supply of fertilizer, accompanied by agronomic advice, farmers are expected to apply fertilizer more efficiently which may help to reduce greenhouse gas emissions. The reforms in the market regime will improve the long-term profitability of the sector and thereby the economic incentives for sustainable management. Phasing out price subsidies across the electricity and petroleum sectors is expected to result in more efficient usage by consumers as prices become market determined. Price subsidies encourage over-consumption, leading to higher global CO_2 emissions. Efficient energy usage will contribute to low-carbon development and encourage further investment in renewable energy generation, energy efficiency and access.

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APPROVAL

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