Austerity without injuring the poor

“Happy are those who work for peace; God will call them his Children,”
Mathew 5:9

February 2004
1. INTRODUCTION

The Catholic Centre for Justice, Development and Peace is endeavouring to contribute to national issues through an analysis of the budget as has become its practice. In doing this, CCJDP pays particular attention to the social dimensions of the budget, that is the impact on the livelihood and well-being of the Zambian people and the promotion of social justice and equity.

As usual the CCJDP’s contribution is based on three cornerstones. These are:

i) First hand experience of people’s conditions through our grassroots contacts in many different parts of the country,

ii) Empirical and analytical data through research and widespread consultation, and

iii) The basic principles of the Church’s Social Teaching that emphasises the values of solidarity, common good, community and focus on the poor.

The Church has marked this year as the year of Justice and Peace, we are therefore urged and challenged to promote justice and peace in all we do. It is in this perspective that we will look at this year’s budget to examine how well it upholds the rights and dignity of the poor, the rights of workers and how it promotes economic governance.

The presentation is organised in four parts. Part one will look at the process of budgeting for the 2004 budget and makes analysis of macroeconomic target set by government. Part II specifically looks at tax issues and analyses the social sectors with particular attention to health, education, social welfare, agriculture and local Government. Part III looks at concerns over public funds management and lastly. Part IV, is the conclusion and recommendations.
Part I

1. PROCESS ISSUES (Formulation of 2004 Budget)

We commend government for the release of the green paper on the Medium Term Expenditure Framework (MTEF) in the last quarter of 2003. The MTEF indicated the parameters for 2004 budget as well as gave space for the discussion of Poverty Reduction Programmes (PRP) in the budget. This consultative process was positive though the time was inadequate; in addition discussion on PRPs seemed to be inconsequential, as there was no possibility of increasing allocations already set. No legal framework guarantees these consultations and government is not bound by any law to call civil society let alone accept their contributions. It is our recommendation that government legalizes a participatory and consultative process that would be geared towards promoting accountability and efficiency. This should not only be done at the central level like Lusaka but also at lower levels as well.

2. Recap Of Macroeconomic Targets Set By Government.

For once the macroeconomic targets set by government this year look realistic. The Gross Domestic Product growth is set at 3.5 %, inflation at 15 % and gross international reserves of 1.5 months of imports and the budget deficit has been limited to 2.0 % of GDP. In comparison to 2003, we see that the revised indicators set mid year were achieved. GDP grew by 4.3 % from at target of 4.0 %. This represents an increase of 0.3 %. Annual inflation fell from 26.7 % at the end of 2002 to 17.2 %. This was 0.7 % lower than the set target. However, non-food inflation at end of December 2003 remained at 21.7%. As a net importer of food, Zambia will continue to face difficulties with this inflation.
Only 1.3 months of imports of gross international reserves were achieved against the target of 1.9. The budget deficit worsened to 5% from the target of 1.5 of GDP. This was mainly due to huge internal borrowing by government.¹

However, while the targets for this year seem realistic, the government has left out food security and poverty reduction as macroeconomic targets. This makes us question whether these two areas are not priorities of government this year? For example, the government could identify a health goal or education goal and set a target for the year. For instance, a target for the reduction of maternal mortality to 400/100,000 could have been set for this year, or for the MTEF. With the introduction of Activity Based Budgeting (ABB) this is feasible. We recommend that such goal setting should be made a priority.

A general observation that can be made is that targets in 2004 are all less ambitious than what the government had set to achieve in 2003. This is pragmatic given that in the past two years government had to revise macroeconomic targets at the mid year review.

It is also important to note that the unsatisfactory performance of the budget last year, specifically the budget overrun, led to a donor credit squeeze. Thus the government has planned to finance this year’s budget with more domestic resources (63.5%) than external resources (36.5%). This is aimed at cushioning the impact of donor squeeze. This year’s budget of K8,328.6 billion is 20.2% higher than last year’s budget of K6,931.5 last year’s.

While we appreciate the increase in this year’s budget, we are dismayed by the lack of financial discipline shown by government spending agencies. It appears that the Ministry of Finance has

¹2004 Budget Speech, presented by Hon Ng’andu P Magande, Minister of Finance and National Planning, 6 February, 2004.
failed to control government’s excess expenditures. This is shown by the supplementary expenditure of K1.3 trillion in 2003. Supplementary expenditure only shows the lack of efficiency in government spending. Government needs to completely do away with the excess expenditure bill, which legalizes supplementary expenditures. ii

As the government embarks on the Activity Based Budgeting, there is need to consider the repeal of the excess expenditure bill if Budget reforms being implemented by government are to be meaningful. There is need for more strict control at permanent secretary level.

Part II

1. TAX ISSUES

The government has in this year’s budget moved away from a flat rate of 30% on personal income to a graduated system with rates increasing from 0, 30, 35 and 40 percent. Government has also increased the tax threshold from K1,920,000 to K3,120,000. This is a progressive tax system that has shifted the burden of tax from the low to higher income earners. With these changes the government will gain K23.8 billion. The proposed reform reduces the PAYE burden on those earning less than K 1.5 million per month by say K 105 billion per year, and it increases the PAYE burden on those earning more K 1.5 million per month by say K 130 billion per yeariii.

The new progressive tax system will ensure that benefits accrue more to people who earn less. For instance, of the 460,000 PAYE payers, 0 % earn less than K 250,000 per month and the benefits vary according to your income as shown in the table below.

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ii Mwanawina, 2003
iii RIZES/CSO Project February 2004
<table>
<thead>
<tr>
<th>Income range (K)</th>
<th>% of wages/ salary earners.</th>
<th>% Benefit/losses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 250,000</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>250,000-300,000</td>
<td>5</td>
<td>8-9</td>
</tr>
<tr>
<td>300,000-500,000</td>
<td>47</td>
<td>5.4  –8.2</td>
</tr>
<tr>
<td>500,000-700,000</td>
<td>15</td>
<td>4.0-5.4</td>
</tr>
<tr>
<td>700,000-1,000,000</td>
<td>13</td>
<td>2.8-4.0</td>
</tr>
<tr>
<td>1,000,000-1,500,000</td>
<td>8</td>
<td>0-2.8</td>
</tr>
<tr>
<td>1,500,000-2,000,000</td>
<td>5</td>
<td>Loss 0.4-2.0</td>
</tr>
<tr>
<td>2,000,000-3,000,000</td>
<td>3</td>
<td>Loss 2.0-3.7</td>
</tr>
<tr>
<td>3,000,000-4,000,000</td>
<td>1</td>
<td>Loss 3.7-4.5</td>
</tr>
<tr>
<td>4,000,000-5,000,000</td>
<td>1</td>
<td>Loss 4.5-5.0</td>
</tr>
<tr>
<td>5,000,000-7,000,000</td>
<td>1</td>
<td>Loss 5.0-7.7</td>
</tr>
<tr>
<td>7,000,000 and more</td>
<td>0.8</td>
<td>Loss 7.7-10.0</td>
</tr>
</tbody>
</table>


From the above table we can see that benefits of this proposed tax system will accrue more to those earning less that K 1,500,000, At K 1.5 million benefit to a tax payers are Zero and any thing more, the Tax payers starts losing. In effect, one can say it promotes the solidarity of the “ rich with the poor”. It is in fact pro-poor in nature.

The Tax Policy Unit concedes, that “a salient feature of the Zambian society is its income inequality.iv The last tax system was somewhat harsh on the poor and relatively mild on the rich. The Zambian worker at the bottom end of labour market paid more tax than their counterparts in the COMESA region.v This is why in the last Pre- and Post budget submission, CCJDP advocated for the introduction of a progressive tax systemvi.

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v ibid
It is now common knowledge that the tax changes have generated much heated debate and opposition within the labour movement and the public in general. For people to see the benefits of a progressive tax system, government needs to control its tendency to spend excessively on such things as vehicles, travel and sitting allowances at the expense of declining health, education, infrastructure and social welfare for the core poor. Government needs to check its record of poor accountability, lack of transparency, misappropriation of funds and blatant corruption that go unpunished.

While we commend government for the introduction of progressive tax system, we still appeal to government to do the following in the interest of the poor:

- Raise the tax threshold to K 350,000 per month. The proposed threshold is still very inadequate to make a difference on income poverty. In effect, Zambia has a low tax threshold compared to other countries in the region. The proposed threshold is only $ 650 per annum compared Uganda $ 905, Zimbabwe $ 1130, Namibia $ 1425 and South Africa $ 1950.
- Remove the revenue gain of K 23.8 billion and make tax changes revenue neutral.
- Reduce the budget deficit not by revenue gains but by reducing on the current expenditure pattern.

In budget 2004 the government has failed to adequately address the challenge of broadening the tax base. A presumptive tax of 3% on turnover of K200million per annum for small and medium scale business has been introduced. Since small and medium scale business will not be obliged to keep strict record of accounts, there is a likelihood that some will be under declaring their turnover. Secondly, we are concerned that the implications of 2004 presumptive tax on turn over has not been adequately analysed.
In last year’s budget a presumptive tax on public transport was introduced, this was a good attempt at bringing into the tax net the so-called informal sector. It would have been beneficial for government to explain how the presumptive tax on public transport performed. How much revenue was collected? The failure to adequately address such issues makes the public doubt government’s commitment to broadening of tax base, consequently making the 400,000+ tax- payers in the formal sector be resentful of changes that continue to make them bear the cost of the 10 billion people of Zambia.

Apart from the failure to bring into the tax net the informal sector, we have also observed that the Zambian economy is predominantly driven by tax from wage and salary earners not business. Whilst new tax bands are introduced on Pay As You Earn raising additional revenue, mineral tax continues to fall and company tax does not seem to be raising in the same proportion as PAYE. This seems to be made worse by “incentives” given to foreign investors.

2. SECTORAL ANALYSIS.

It can be argued that a quickest way of reaching out to the poor is through adequate and efficient funding to the social sectors. The poor benefit directly from government expenditure by accessing good healthcare, good education, good public health, good community facilities and infrastructure to mention but a few. However, there are other factors that may affect outcomes than just level and quality of spending.

The PEMFAR Reportvii notes that social spending increased in the 1990s from 22 percent to 36 percent of the domestically financed discretionary spending from 1991 to 1996. However, social

spending has fallen in real terms. This deterioration in real financing may have partly contributed to the deterioration in social outcomes and increased poverty.

a) **EDUCATION AND HEALTH**

There has been a decline of 11.6% in the allocation to the education sector, from K 844 billion in 2003 to K 756 billion in 2004 budget. This shows the poor coherence between sector objectives and budgetary allocations. Whilst government proclaims a lofty objective of providing “relevant, equitable, efficient and quality education for all”\textsuperscript{viii} it fails to put money on the table. How will education for all be achieved? The current level of funding has implications for the quality of outcomes the country gets. The sustained economic development of this country requires educated people.

Findings of CCJP research on Budget Tracking and Expenditure Monitoring (2003) in five provinces indicated that the policy of free education was being supported through grants of K2.6m per term.\textsuperscript{ix} This was clearly insufficient to meet costs but is something that schools are grateful they had. Statistics from the Economic Report (2003) indicate that enrolment at basic schools increased from 1,865,677 in 2002 to 2,030,714 in 2003, representing an increase of 8.1%. This was mainly attributable to free education policy.\textsuperscript{x}

\textsuperscript{viii} Oxford Policy Management, Unit Costs of Education in Zambia, Final Draft Report, July 2002
The budget does not seem to have made any provisions for increments in the size of grants to basic schools as the table below shows.

<table>
<thead>
<tr>
<th>Province</th>
<th>2003 Budget: Basic Schools District Education Boards</th>
<th>2004 Budget: Grants to basic Schools – Requisites &amp; Grants to Basic Schools</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lusaka Province</td>
<td>K1.95 billion</td>
<td>K1.6 billion</td>
</tr>
<tr>
<td>Copperbelt Province</td>
<td>K1.14 billion</td>
<td>K5.28 billion</td>
</tr>
<tr>
<td>Western Province</td>
<td>K1.26 billion</td>
<td>K1.1 billion</td>
</tr>
<tr>
<td>Eastern Province</td>
<td>K1.88 billion</td>
<td>K1.37 billion</td>
</tr>
</tbody>
</table>

One of the key problems in education is the shortage of teachers, at one school in Eastern Province there was only one teacher for all the grades. One of the reasons that the current Teacher Education Programme (ZATEC) was introduced was to attain a high number of trained teachers to be deployed in schools in the shortest time possible. Budget 2004 has failed to provide for absorption of the almost 9000 trained teachers, thereby again fails to help the country achieve the goal of education for all yet Economic Report of 2003 shows that there has been a decline in the number of basic schoolteachers, from 40,488 in 2002 to 38,891 in 2003. This was mainly due to natural attrition and non-recruitment.

The constraints on employing new teachers may be arising from creditor demands on the government. If the cost of attaining macro economic stability and a balanced budget are to be borne by the poor children of Zambia then there is need to re-look some of these agreements. A significant proportion of Zambia’s people rely on government provided education since they cannot send their children to private school.
HEALTH SECTOR.

The health sector continued to face difficulties due to inadequate funding and lack of adequate trained staff, especially in rural health centres. In 2003, the government allocated K 802 billion to the health sector, but this has gone down to K 719 billion in 2004 budget showing a decrease of 10.2 %.

The Economic Report of 2003 shows expenditures in 2003 declined from US$ 65 million in 2002 to US $ 63 million in 2003, a percentages decline of 3.07 %. Unfortunately, this year’s budget also shows that the government will spend less than what was spent last year in 2003. This raises concern on the implication of the decline in allocation to the sector especially among the poor who cannot afford to go to private hospitals. Health services in Zambia are in a terrible state as can be seen at University Teaching Hospital where anaemic patients have to buy blood from the blood bank. Despite the user fees in hospitals, patients do not have access to drugs let alone free blood. They still have to buy drugs from chemists outside the health institutions. Yet the new Value Added Tax measures of 2004 will make locally produced medicines more expensive.

The above notwithstanding, the Economic Report of 2003, shows that there is marginal increase in the number of doctors, nurses and clinical officers of 8.3 %, 5.8 % 3.0% respectively from 2002. The increase in Management and Administrative Staff was 105.5%. This again shows the failure of the system to put money where the critical staff is. Zambia needs more medical staff especially in the rural areas, yet they seem to be employed at a snail’s pace compared to non-critical staff in the same sector.

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xi Economic Report, 2003
It is unfortunate that statistics show that, for last year alone, deaths from the top eleven diseases show an increase and yet the budget to fight these diseases has gone down. The sector also experienced shortage of drugs, poor staffing levels and the disease incidence increased.

For instance, the incidence rate for malaria was 736 in 2002 and this rose to 995 in 2003. The incidence rate for Diarrhoea rose from 161 in 2002 to 200.8 in 2003. There has been a marked improvement in allocation for malaria control for 2004 to K 14.8 billion compared to 315 million in 2003. However an increase in allocation will not itself result in better services therefore it is our hope that money will go directly to combat diseases not to pay sitting allowances.

Unfortunately, the allocations to Drugs and Essential Drug Kits have gone down to K47 billion from K65 billion in 2003. This is a reduction of 27 percent. This is quite serious because it means that the poor who cannot afford private medical care will not have access to drugs when they go to hospitals. Apparently missing is the donor-funded component. This is the reason the CCJDP urges government to ensure getting back on a PRGF so as to reduce the deprivation the poor will face.

Funding for ARVs in last years budget was given to ministries and some few hospitals, however, the picture is somewhat different this year. Only a few ministries have benefited. But there are certain fundamental questions to be asked. How efficient were the resources for ARVs used. Is there rationalization between resources going to the ministries and what is going to the National AIDS council? Has Zambian trained enough personnel to test people before administering ARVs. How are the nutritional needs taken care of?
While there is decline in the health budget of 10.2% there defence budget has only reduced by 3.1 percent. The budget for Zambia Intelligence services has increased by 105%. How does the government justify this anomaly? Is there a threat to Peace in Zambia? Yet at the end of the year, both agencies, which are not economic, nor poverty reducing sectors will overspend their original budgets by huge margins!

c) We note the increase in allocation to Ministry of Community Development and Social Services. Farmer Support programme has reduced to K1 billion, the Food security pack programme has been allocated K28 billion, just K800 million more than was spent in the 2002-2003 programme. The Ministry notes with regret the unwillingness of farmers to be weaned of from such programme. Implementation of these support programmes is wrought with misapplication and poor pay back. For value of money there is need for the emphasis on repayments and punishment of dishonesty.

d) LOCAL GOVERNMENT

Funding for local government need to be totally overhauled in order to enhance its capacity to deliver at the local level. The government should consider legally assigning a proportion of revenue, say 5% to local government particularly earmarked for District Development Programmes. However there needs to be much done to ensure absorption capacity and accountability at local authorities.

e) DEBT

Zambia is walking on a tight rope in as far as the debt cancellation is concerned. The government has to ensure that the Staff Monitoring Programme is strictly adhered to so that the country can have a Poverty Reduction and Growth Facility (PRGF) by mid
this year. The consequences of not having a PRGF and not reaching the HIPC completion point will be grave for Zambians.

Government has to ensure that they control the domestic debt and reduce the budget deficit. If the domestic debt increases, it affects discretionary spending thereby affecting allocations to social spending.

4. PRESIDENTIAL TRAVEL AND PAYMENT TO MEMBERS OF PARLIAMENT

This does not send a message of austerity, what is needed is a freeze on travel not wages. To show good leadership the government should have declared that there would be no travels this year. K30 allocated for President’s travel could pay even 4000 teachers, thereby reducing the number of teacher not on the pay roll by close to two thirds.

The budget indicates that Members of Parliament will be paid a mid-term gratuity of K34.2 billion. Why should this be the case when their terms of office are not over? Surely gratuity is paid at the end of term? We urge MPs to reject this payment. The government has failed to offset its debt to Pensions board; as a result many men and women who served government for several years, even 20 years, have not been paid. Why should politicians who only got to parliament 2 years ago be paid before time? Where is justice?

5. INFORMATION DISCLOSURE, TRANSPARENCY AND ACCOUNTABILITY

The failure of government in this area is amply shown by poor disclosure on the budget overrun and the delayed release of information on the mid term review in 2003. This year’s failure to provide budget information is another case in point. The “Yellow
Book” on Estimates of Revenue and Expenditure is not yet available to the public, nor is the Economic Report. The latter in its current format is rather incomplete; there is no chapter on Agriculture.

Another concern is the rampant misapplication of resources; HIPC reports continue to indicate this. We hope that the Auditor Generals office will tackle this problem effectively.

6. POVERTY REDUCTION STRATEGY PAPER (PRSP)

The first PRSP for Zambia came to an end but no convincing figures on how poverty has been reduced can be found anywhere. This year’s budget shows that K 537.4 billion has been provided, which is an increase of 27.7 % from 2003. However, what is clear now is that only about half or less, of the allocated funds are disbursed by the close of the year. The level of funding of PRP does not seem to show that the PRSP is the cornerstone of budgeting and development. Current PRP funding is too inadequate to make a dent on poverty reduction. It would be interesting to hear from the IMF and World Bank on whether the original conception of PRSP is being achieved in Zambia?

It is not even clear how this poverty reduction expenditure is defined. What is more poverty reducing, the repair of toilets at police stations or salaries for teachers? There is need to critically look at what are poverty-reducing programmes in the various ministries are, for instance in Ministry of Finance and National Planning, PSCAP K32 billion is indicated as a PRP programme. All that has happened under this programme is the purchase of all models of vehicles, whilst Zambians continue to suffer.
7. CONCLUSION AND KEY POLICY RECOMMENDATIONS

It can be seen from the above arguments that government needs to critically look at the expenditure side and ensure that the poor people’s interests are catered for. The Activity Based Budget introduced this year calls for fiscal discipline, transparency and accountability on the part of government. We therefore recommend the following:

- The legal framework surrounding the budget preparation process is changed to guarantee consultations between government and civil society. It is our recommendation that government legalizes a participatory and consultative process that would be geared towards promoting accountability and efficiency. Consultations should be done both at district and provincial level.

- Budgetary controls by the Ministry of Finance should be enhanced. We are dismayed by the lack of financial discipline shown by government spending agencies. It appears that the Ministry of Finance has failed to control government’s excess expenditures. This is shown by the supplementary expenditure of K1.3 trillion in 2003. Supplementary expenditure only shows the lack of efficiency in government spending. Government needs to completely do way with the excess expenditure bill, which legalizes supplementary expenditures. xii

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xii Mwanawina, I, paper on budget submission of non-state actors, 2003.
• While we support the progressive tax system, we recommend that a raise in the tax threshold to K 350,000 per month is necessary. The proposed threshold is still very inadequate to make a difference on income poverty. In effect, Zambia has a low tax threshold compared to other countries in the region. The proposed threshold is only $ 650 per annum compared Uganda $ 905, Zimbabwe $ 1130, Namibia $ 1425 and South Africa $ 1950.

• Remove the revenue gain of K 23.8 billion and make tax changes revenue neutral.

• Reduce the budget deficit not by revenue gains but by reducing on the current expenditure pattern

• One of the key problems in education this year is that the Budget 2004 has failed to provide for absorption of the almost 9000 trained teachers not on the pay roll. Economic Report of 2003 shows that there has been a decline in the number of basic schoolteachers, from 40,488 in 2002 to 38,891 in 2003. This was mainly due to natural attrition and non-recruitment. We recommend that savings made from cuts in the presidential trips should go towards the recruitment of teachers. The cost of attaining macro economic stability and balancing the budget should not be borne by the poor children in Zambia schools.

• Government should do everything possible to control the high disease incidences. For instance, the incidence rate for malaria was 736 in 2002 and this rose to 995 in 2003. The incidence rate for Diarrhoea rose from 161 in 2002 to 200.8 in 2003. There has been a marked improvement in allocation for malaria control for 2004 to K 14.8 billion compared to 315 million in 2003. However an increase in allocation will not itself result in better
services therefore it is our hope that money will go directly to combat diseases not to pay sitting allowances.

• This year’s budget has provided a reduction of excise duty on the manufacture of cigarettes to make them cheaper, though this is in the immediate seen as a way to protect jobs, government should reconsider this reduction. This is particularly because of the health cost related to smoking-related illnesses.

• The allocations to Drugs and Essential Drug Kits have gone down to K47 billion from K65 billion in 2003. This is a reduction of 27 percent. This is quite serious because it means that the poor who cannot afford private medical care will not have access to drugs when they go to hospitals. Apparently missing is the donor-funded component. We therefore recommend that government ensure that it gets back on a PRGF so as to reduce the deprivation the poor.

• The budget indicates that Members of parliament will be paid a mid-term gratuity of K34.2 billion. Why should this be the case when their terms of office are not over? Surely gratuity is paid at the end of term? We urge MPs to reject this payment. The government has failed to offset its debt to Pensions Board; as a result many men and women who served government for several years, even 20 years, have not been paid. Why should politicians who only got to parliament 2 years ago be paid before time? Where is justice?

• There is a serious lack of information disclosure on the part of government in as far as budgetary execution is concerned. We recommend that government avails
accurate and timely information to the stakeholders for the sake of transparency and accountability. The failure of government in this area is amply shown by poor disclosure on the budget overrun and the delayed release of information on the mid term review in 2003. This year’s failure to provide budget information is another case in point. The “Yellow Book” on Estimates of Revenue and Expenditure is not yet available to the public, nor is the Economic Report. The latter in its current format is rather incomplete; there is no chapter on Agriculture.

- Another concern is the rampant misapplication of resources; HIPC reports continue to indicate this. We recommend that the Auditor Generals office be adequately funded to enable it tackle problems of misapplication of HICP funds.

- The first PRSP for Zambia came to an end but no convincing figures on how poverty has been reduced can be found anywhere. This year’s budget shows that K 537.4 billion has been provided, which is an increase of 27.7% from 2003. However, what is clear now is that only about half or less, of the allocated funds are disbursed by the close of the year. We recommend that government fully disburses PRP funds.

- The definition of poverty reducing expenditure is not clear. What is more poverty reducing, the repair of toilets at Police stations or salaries for teachers? There is need to critically look at what poverty-reducing programme in the various ministries are, for instance in Ministry of Finance and National Planning, PSCAP K32 billion is indicated as a PRP programme. All that has happened under this programme is the purchase of all models of vehicles, whilst Zambians continue to suffer. We recommend that
government and civil society agree a clear definition of poverty reducing expenditures.