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A Decent Work Approach to Development and Growth in Africa"

Policy Coherence for Generating Employment and Decent Work in Zambia

Background Paper

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- Abstract -

Zambia has seen impressive economic growth since 2001, with an average annual GDP growth rate for 2000-2006 of 5%. This growth is based on the adoption and enactment of a very good set of macro polices. Central to this achievement has been a reform package including public sector reforms, privatisation, and stringent fiscal and monetary policy. The resulting growth has been led by the country's industrial sector, especially copper-mining which has been strongly affected by the rise in copper prices. This leaves Zambia very vulnerable to fluctuations in external demand, and also makes the problem of the sectoral imbalance of the Zambian economy more intractable.

Decomposition of poverty by employment shows the poor and extremely poor to be amassed in agriculture, in self-employment or unpaid family work. Policy therefore needs to be addressed towards generating employment and increased sectoral diversification of this employment. The correspondence in estimates for informality and underemployment implies that informality is based much more on lack of demand, rather than on refuge from formality.

In order to make economic growth more sustainable, it must become more balanced and inclusive. Policy should focus on diversifying the economy away from mining. Manufacturing in particular should be encouraged as it remains relatively weak. More coherence is needed between existing policies for macro fundamentals, on the one hand, and, on the other, policies for more inclusive growth, employment and decent work, without which even the current growth becomes unsustainable in the medium to longer term.

Policy Coherence for Generating Employment and Decent Work in Zambia

Background paper for the High Level Forum on "Working out of Poverty: A Decent Work Approach to Development and Growth in Africa" Monrovia, 8-9 September 2008

1. The need for Policy Coherence

The ILO's Policy Coherence Initiative (PCI) for Africa is diagnostic and prescriptive. It is diagnostic in that it seeks to examine macro policy at the country level, for its impact on employment and the conditions of this employment – that is for its impact on Decent Work. It is prescriptive in that, on the basis of this causality it then suggests some policy shift to improve the employment impact, both in quantitative and qualitative terms.

Policy reform addresses a large variety of structural weaknesses in the economy, to stabilise macro fundamentals and make them more sustainable, thereby improving the environment for growth, poverty reduction, meeting the MDGs and improving welfare. The ILO through its PCI advocates that these reforms should focus on the more comprehensive set of objectives including both growth and employment, and argues that the policy mix therefore is more consistent and coherent, and its sequencing is more enabling for both objectives. Cross country policy experience shows that simultaneity of reforms can act to the detriment of employment and decent work, thus jeopardising the sustainability of these reforms. While coherence and judicious sequencing work to enable staying the reforms course for the longer run.

Zambia's growth path illustrates some of these down side policy risks, through a revealed susceptibility towards an enclave mining sector not well integrated with the rest of the economy.

Zambia has had good GDP growth in the last half decade, averaging 5%. This has almost doubled from GDP growth in the previous decade of the 90s, and the near stagnation during the 80s. This pick up in growth has been enabled by concerted macro policy reforms. The framework for these reforms was given under a Poverty Reduction and Growth Facility (PRGF) and a Staff Monitored Program (SMP), whose conditions were largely met, enabling significant fiscal support and debt reduction under the Highly Indebted Poor Country (HIPC) program. The reforms package has included public sector reforms, privatisation, and stringent fiscal and monetary policy reigning in budgetary deficits, current account balances, and curbing inflation to single digits. A Poverty Reduction Strategy Papers (PRSP) has been incorporated into the Government's Fifth National Development Plan (FNDP) in 2006.

The Government of Zambia is just beginning a review of its FNDP in the second half of 2008, with its development partners, donors and advisory agencies. This is a propitious moment to review the recent growth and policy framework for sustainability and impact, and suggest a wider, more coherent policy portfolio.

The policy framework chosen and the policy effort to stay the course of reforms have been critical in delivering this pick up in growth after a hiatus of nearly two decades. Policy must now be directed towards sustaining this growth. There are five broad areas of policy concern about the sustainability of this growth path in the medium to longer term.

First, much of this growth has been based on extractives, principally copper, and the rise in copper prices. While the price windfall has been very useful for growth, clearly long term growth cannot be based on reliance on such an exogenous factor. The pick up in growth has been based on little sectoral diversification away from mining, towards other sectors, especially manufacturing which remains relatively weak. If the country is to move more rapidly up the product ladder, it has to increase the value added in processing of extractives, which means increasing the linkages of the mining sector to manufacturing especially.

Second, much of this growth has been based on exports, of extractives, which has been a traditional reliance of the economy. As a result the domestic economy, gauged by domestic consumption, domestic production, and domestic investment and savings, have had relatively weak growth. More balance is needed in the drivers of growth, between exports and these domestic drivers of growth like consumption and domestic investment and savings.

Third, a large part of the reason for this somewhat narrow base for recent growth in Zambia is that it has not generated commensurate employment, neither in extractives, nor in other sectors. Of particular concern is the weak growth in employment in manufacturing. For the majority of the population of the country, the major form of participation in this growth has to be through generation of employment and improvement in the conditions of this employment, especially critical conditions of employment like the real wage and social protection for the vulnerable. Broader based, more inclusive growth has to base on generating more decent work.

Fourth, given the relatively low impact of recent growth on employment and critical conditions of employment, the impact on poverty has also been low. The only sustainable route out of poverty has again to be based largely on generation of decent work.

Fifth, the low impact of growth on employment and poverty could also be constrained by the very tight monetary and fiscal policies entailed by the PRGF and SMP frameworks. While these macro frameworks adopted have been indispensable for improving macro fundamentals and thereby generating growth, they have also contributed to the somewhat narrow base of this growth. An 8% of GDP cap on the public sector wage bill has constrained increasing employment in education and health services for an expanding population which works against meeting already elusive MDG targets. There is also an increasing call from the private sector, for increasing long held up public sector investment in infrastructure, to crowd in more private sector investment.

Zambia’s good growth in the last five years has been based on adoption and enactment of a very good set of macro polices. Sustaining this growth in the medium to long term however requires additional policies that broaden the base of this growth,

through sectoral diversification, more balance in the drivers of growth between exports and consumption, generating more employment and improvement in the conditions of this employment such as the real wage and social protection for the vulnerable, and allow a critical enabling role for the public sector. More coherence is needed between existing policies for macro fundamentals and policies for more inclusive growth, employment and decent work, without which even the current growth becomes unsustainable in the medium to longer term.

2. Growth

Zambia has had good GDP growth in the last five years, which comes after a long hiatus of nearly two decades. This growth has propelled Zambia into the ranks of the middle income countries with a GDP per capita of over $ 1000 in this very short time span.

Zambia's population is estimated at 11.7 million in 2006, by the Central Statistical Office. This has risen from 9.9 million in 2000, according to the Population Census. The high population growth rate of 3.1% over the 80s, has been reduced by HIV/AIDS to 2.9% over the 90s, and is expected to fall further to 2% by 2010. A high proportion of the population, 38%, is urbanised. 45% of the population is young, under 15 years, and getting younger[1].

Table 1shows that the country has had good GDP growth from 2001 onwards, of over 5% per annum, with one interruption in 2002 when it dropped to 3.3%. Average GDP growth between 2000 and 2006 is estimated at 5% per annum[2].

Table 1: Selected Economic Indicators: 1998-2007

Variable/Year	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Real GDP growth (%)	-1.9	2.2	3.6	5.2	3.3	5.1	5.4	5.2	6.2	5.7
GDP per Capita (USD)	348.54	327.55	330.56	360.47	362.69	402.59	490.96	635.57	922.70	1,018.18
Inflation (end period %)	30.6	20.6	30.1	18.7	26.7	17.2	17.5	15.9	8.2	8.9
Lending Interest Rates	46.6	31.8	40.3	39.1	42.8	37.7	29.8	33.9	27.9	24.4
Current Account Position (% of GDP)			30	28	(32)	(44)	(13.8)	(9.7)	0.4	(5.4)
Capital Expenditure % of total National Budget			29.7	37.8	39.2	39.8	36.5	29.2	21.5	17.6
Domestic resources % of total National Budget			66	48.1	60.4	57.3	63.5	70.6	71	72
Total Govt. Debt (Multilateral & Bilateral) USD Million	6,650.5	6,051.5	5,837.00	6,405.50	6,469.90	5,948.50	6,620	4,124	1,019.00	1,054.50
Copper export volumes (thousands of Mt)					330	353	393	439	476	526
FDI (in million of US $)					303	347	364	497	559	

Source: Ministry of Finance and National Planning

[1] Government of Zambia, Central Statistical Office, 2008.
[2] World Development Indicators, 2008.

This good GDP growth in the 2000s has picked up from very low growth over the previous two decades of the 80s and the 90s. At independence in 1964, Zambia had one of the most promising economies in Southern Africa with vast mineral resources. However falling copper prices in the global market in the 70s plunged Zambia's copper exports from $3.4 billion in 1974 to $1.8 billion in 1975. The decline continued through to the 90s, with the country's copper exports falling to $725 million in 1994[3]. Largely as a result of this decline in copper exports, coupled with the lack of a diversified economy, GDP growth in the 80s and the 90s was very low. GDP growth in the 80s averaged only 1% per annum, while in the 90s it plunged further to 0.5% per annum, as Table 2 shows[4].

Table 2: Growth of Output (average annual % growth)

	Gross Domestic Product		Agriculture		Industry		Manufacturing		Services	
	1990-00	2000-06	1990-00	2000-06	1990-00	2000-06	1990-00	2000-06	1990-00	2000-06
Zambia	0.5	5.0	4.2	2.1	-4.2	9.2	0.8	5.4	2.5	5.9

Source: World Development Indicators

As a result of the very low growth over the 80s and the 90s, Zambia was one of the poorest countries in Africa by 2000, with a GDP per capita of $330, as Table 1 shows. The good growth from 2001 onwards has tripled GDP per capita to over $1000 by 2007.

This GDP growth has been led by the industrial sector, which includes mining, growing at 9% over 2000-06, compared to a negative growth rate over the previous decade, as Table 2 shows. Within the industrial sector, the growth rate of manufacturing has been much lower over 2000-06, at 5.4% per annum, just below the growth rate for services at 5.9% per annum. Agriculture has not really contributed to the good growth in the 2000s, growing at only 2.1% per annum, which is a fall from its previous decade's growth rate of 4.2% per annum.

3. The Macro Policy Framework

The macro policy framework underlying this pick up in growth in the 2000s has been overloaded with reforms, because of the build up of a large backlog of structural problems in the economy over the 80s and the 90s. While the current set of reforms have been instrumental in delivering a much needed pick up in growth after a long hiatus, a number of structural challenges still remain for policy to address.

The structural issues to address in the Zambian economy have been myriad, a legacy of colonial policy, but also post colonial policy attempts at reversal.

The division of regional economic specialisation under colonization left Zambia, then Northern Rhodesia, with only copper and maize milling, with derivative

[3] World Bank, 1996.
[4] World Development Indicators, 2008.

manufacturing concentrated around the Copper Belt of Ndola where most of the import substitution companies were established. Copper was nationalised in the 1970s, copper prices also plummeted, and its output fell to 0.25 million tons by the 1980s, well below that of Chile.

In the early 80s an effort was made to diversify the economic structure, with a shift away from the mining sector, by creating a public sector driven manufacturing sector. Parastatals or State Owned Enterprises (SOEs) built up a small industrial base of food, beverages, tobacco, textiles and leather production. The government put in place price controls and heavily subsidised production. The result of maintaining these inefficient parastatals in a huge public sector was a mounting public debt.

Food security also became dependent on the staple maize, with an annual requirement of at least 1 million tons, however subject to harvests fluctuating with drought because of very limited irrigated land.

These structural weaknesses have had the effect of overloading the reform agenda. The Structural Adjustment Program (SAP), of the 1980s and 1990s cut the maize subsidy, reduced public sector expenditure and employment, introduced market determined exchange and interest rates, initiated privatisation, and instituted user charges to raise revenues. The SAP program did not reduce poverty, debt servicing became crippling, and the repeal of the maize subsidy provoked riots. The initial shock of these policies saw a further decline in the economy in the 90s. Real growth of GDP dipped into negative, inflation soared, along with interest rates and unemployment. By 1998, the inflation rate was 30% per annum, and the bank lending interest rate stood at 46%[5]. The budget deficit averaged 5.5% of GDP over this period[6].

The SAP in Zambia was succeeded by an IMF Staff Monitored Program (SMP). The targets of the Staff Monitored Program (SMP) had largely to be met, in order to meet large debt service repayments to the IMF due in 2004-05 without running down foreign exchange reserves, and to qualify for debt relief under the IMF-World Bank Heavily Indebted Poor Country initiative (HIPC)[7]. Meeting most of the targets of the SMP led to $320 million three year Poverty Reduction and Growth Facility (PRGF) ending in June 2007. This also facilitated a HIPC debt cancellation program of $3.9 billion in 2005. The IMF has written off another $0.5 billion in debt, while a Poverty Reduction Strategy Paper (PRSP) was instituted for $1.2 billion, and this is continuing under the Fifth National Development Plan (FNDP) begun in 2007. After six good reviews of Zambia's progress under the PRGF concluding in September 2007, another three year PRGF has been instituted.

As a result the external debt has dropped from $6.8 in 2003 to $2.6 billion by 2007 as Table 3 shows, with debt servicing falling by a near quarter, from $0.8 billion per annum to $0.2 billion.

These programs have entailed a number of policy reforms. Public sector employment was meant to be reduced from 140,000 to 80,000, but was settled at 110,000.

[5] MoFNP, 2007.
[6] Economist Intelligence Unit, 2008.
[7] Economist Intelligence Unit, 2008.

However a wage freeze was instituted and the public sector wage bill was capped at 8% of GDP. The current budget for 2007-08 has still set this cap at 8.6% of GDP[8]. Public sector monitoring has been streamlined.

Monetary and fiscal policies have been tightened to reduce the budgetary and current account deficits, and to control inflation. The budget deficit has been drastically curtailed from -6.6% of GDP in 2003 to -2.9% of GDP for 2006, as Table 3 shows. Public sector expenditures have been brought down from 31% of GDP in 2003 to 24% by 2006, although revenues have struggled to increase above 24% of GDP after 2003, dipping in some years. Medium term projections of the budgetary deficit put it at -1.4% for 2008, and -1.2% for 2009, assuming expenditure rising to 26% of GDP, and revenues rising to 25% of GDP.

Table 3: Macroeconomic Indicators

	2003a	2004a	2005a	2006b	2007b	2008c	2009c
Fiscal Indicators (% GDP)							
Public-sector revenue	24.9	23.8	23	21.9	24	25.5	24.6
Public-sector expenditure	30.9	26.7	25.7	23.6	25.3	26.9	25.8
Public-sector balance	-6.6	-1.7	-2.6	-2.9	-0.3	-1.4	-1.2
Net public debt	152	128.9	61.7	31.9	28.2	25.8	25.6
Prices and Financial indicators							
Exchange rate ZK: US$	4645	4771	3509	4407a	3845a	3537	4240
Exchange rate ZK: €	5860	6459	4139	5815a	5615a	5482	6233
Consumer prices	17.2	17.5	15.9	8.2a	8.9a	13.4	7.1
Stock of money M1(% change)	29.4	22.9	17.8	54.0a	14.6a	15	14
Stock of Money M2 (% change)	25	32	3.2	44.2a	25.3a	21.3	17.9
Lending interest rates (%)	40.6	30.7	28.2	23.2a	18.9a	18.5	18
Current Account(US $ m)							
Trade balance	-312	110	35	1293a	983a	1042	609
Goods:export fob	1081	1836	2195	3929	4594a	5122	4852
Goods: import fob	-1393	-1727	-2161	-2636	-3611	-4080	-4244
Service balance	-238	-215	-237	-209	-575	-560	-496
Income balance	-148	-410	-609	-1005	-1125	-1520	-1312
Current transfers balance	293	127	395	353	489	588	638
Current account balance	-405	-389	-417	433	-228	-451	-561
External debt (US $ m)							
Debt stock	6800	7455	5378	2325a	2596	2879	3076
Debt service paid	724	469	453	154a	209	248	261
Debt service due	785	698	481	215a	212	248	261
International reserves (US $ m)							
Total international reserves	248	337	560	720a	1090	1200	1250

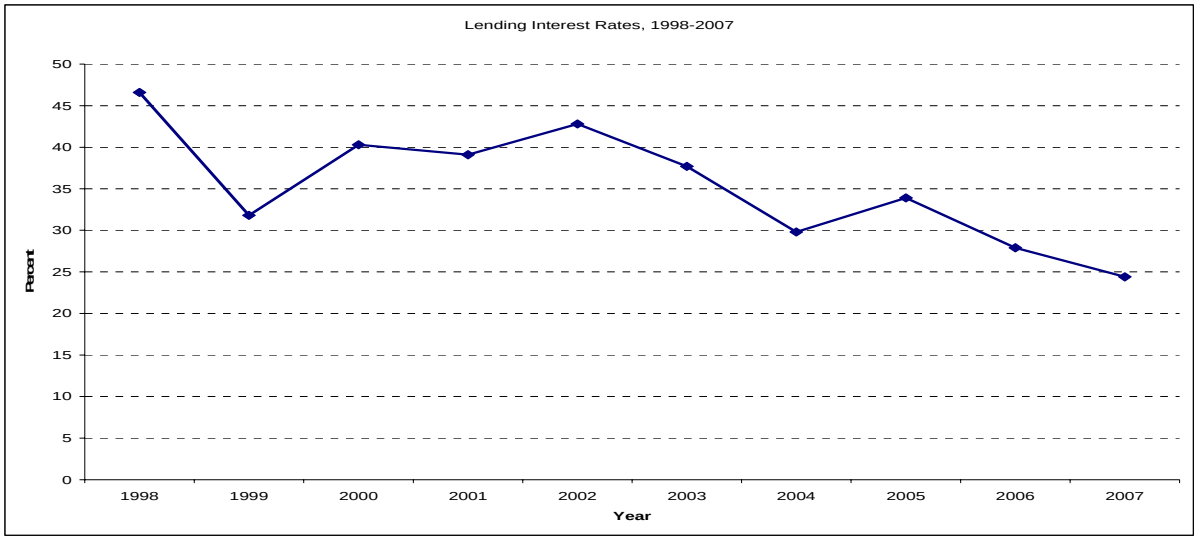
a Actual. b Economist intelligence unit estimates. c Economist Intelligence Unit forecasts.

Source: IMF, *International Financial Statistics*

[8] MoFNP, 2008.

The interest rate in 2002 was at a prohibitive 43% as Figure 1 shows. It had come down by 2007 to 25%, still keeping the cost of borrowing quite high. The Value Added Tax has risen to a very high level of 17.5%. The current account balance has remained almost constant on trend, at about $0.4 billion dropping to 16% in January 2008 over the past four years (Table 3). The Kwacha has appreciated by 17% over 2003-07, fuelled by strong exports, and foreign exchange reserves topping $1 billion by 2007. And inflation had come down from 27% per annum in 2003, just into single digits, 9% per annum, by 2007, as Table 4 shows. Inflationary pressures have been added by high world oil prices, and an appreciating South African Rand in which most imports are denominated, while good harvests and an appreciating Kwacha have kept prices down. The Kwacha peaked at a Dollar exchange rate of K 2700 in 2007-07, climbing down to K 3500 in 2008.

Figure 1: Lending interest rates, Zambia, 1998-2007



Source: Bank of Zambia

Table 4: Inflation at the end of year

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008[a]	2009[a]	2010[a]
Inflation	26.8	26	21.4	22.2	26.7	17.5	15.9	8.2	8.7	7.0	5.0	5.0

[a] Projected

Source: Central Statistical Office (2007) *Consumer Price Index Kuly 2007* Lusaka, CSO

The privatisation agenda has been somewhat more fraught. The government controlled holding company Zambian Consolidated Copper Mines (ZCCM) privatised three main groups of copper mines: KCM which produces half the copper output of the country has been sold to Vendanta Resources PLC; MCM the second largest producer has been sold to Glencone and Quantum but with the state retaining a 10% share; and the smaller Chambishi has been sold to Chinese interests branching into copper cathode production. While most of the copper mines have been privatised, the remainder are considered unprofitable and cannot currently be privatised. Large parastatals like the Zambian Electricity Supply Corporation (ZESCO) and the Zambian National Commercial Bank (ZNCB) have followed a newer option of

commercialisation, with the institution of private management and sale of minority shares, to which the IMF has agreed.
A National Agricultural Policy aims to double irrigated area to 90,000 hectares by 2015, although the potentially irrigable area is a half million hectares.

Regional Free Trade Agreements and the waning of preferential access for African exports under the American Growth Opportunities Act (AGOA) have increased regional competitiveness and resulted in a number of closures in the manufacturing sector.

4. The Structural Dependence of Growth on Extractives

The macro policy framework adopted and the entailed reforms have been a major element in the pick in growth over the 2000s. However another strong element contributing to this pick up in growth has been the sudden rise in copper prices. Much of the growth has been based on extractives, especially copper. Sectoral diversification has been low. Of particular note, the manufacturing sector does not appear to have benefited from this extractives led growth.

Recalling from Table 2, GDP growth over 2000-06 of 5% per annum, has been led by industry growing at 9.2%. Industry includes both mining and manufacturing. However this industrial led growth has not been based on manufacturing growth, which was only 5.4%. It has been led by mining, which Table 5 shows were growing at 8% in 2005, and 12% in 2006. Between 2001-05 mining growth averaged 11%. Copper largely, and cobalt, account for 90% of mining output and 65% of exports.

Table 5: Annual growth rates of Mining Sector

	2005	2006	2007	2008	2009	2010
Actual	7.9%	11.8%				
Baseline and Target	7.9%	13.9%	14.0%	14.5%	14.5%	14.5%

Source: MoFNP, Annual Economic Report, 2006

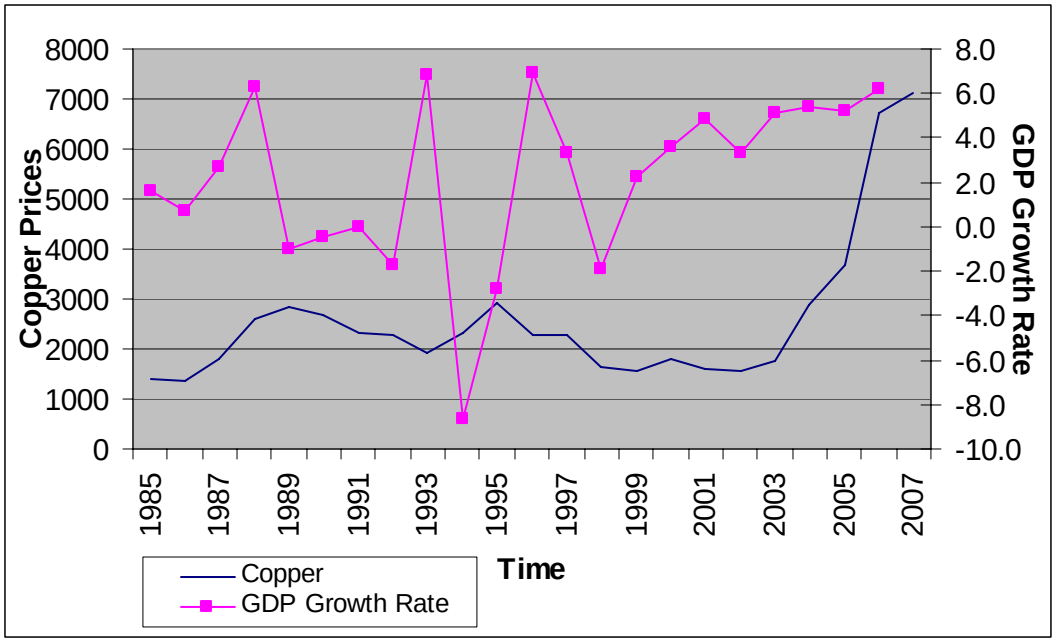
In fact copper prices explain Zambian growth in the long run quite well. Table 6 gives copper prices and Figure 2 plots them against GDP growth. In the second half of the 80s copper prices increase up to 1988-89, and GDP growth increases with them. The 90s is broken into three phases. In the 90s, copper prices fall till 1992-93, and GDP growth falls with them. From 1993 to 1995 copper prices rise as does GDP growth. And from 1995 to 1998-99 copper prices fall to their low of $1573 per ton, while growth slumps, becoming negative. After 1999, copper prices stop falling and start inching up, while GDP growth rises from negative to 4% per annum by 2002. After 2002, copper prices have risen by more than a factor of four, to $7132 per ton in 2007, while GDP growth has risen above 6%.

Table 6 : Market Prices and Unit Values (US Dollars per Metric Ton)

Time	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
COPPER	1417	1370	1781	2600	2847	2661	2339	2285	1915	2306	2932	2293
Time	**1997**	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	
COPPER	2275	1654	1573	1815	1580	1560	1779	2863	3677	6731	7132	

Source: IMF, *International Financial Statistics.*

Figure 2: Copper Prices & GDP Growth Rate



With the shooting up of copper prices in the 2000s, copper exports have risen from 300 million tons in 2002, to 560 million tones by 2006, with targets being set of reaching 1 million tons in the medium term. Exports have picked up from $1 billion per annum in 2003 to $4.5 billion by 2007.

So the copper windfall has been very good for growth, and the policy reforms allowed the mining sector to take better advantage of the price rise with a good supply response. However Zambian growth remains structurally dependent on the mining sector. Worse, the manufacturing sector has not benefited from the growth in mining. Table 7 shows that the mining sector increased its share of GDP from 6% in 2000 to 9% by 2006. The manufacturing sector however kept its share of GDP constant over this period at 10.5 %. The only sector that has grown with the pick up in GDP growth has been construction, doubling from 5% to 10% over this period. Trade at 18% of GDP, transport at 7% of GDP, and services at about 25%GDP, have all remained constant between 2000 and 2005. Agriculture has decreased its share over this period, from 17% to 14%.

Table 7: Share of GDP by Kind of Economic Activity – Constant Prices, 2000-2007

KIND OF ECONOMIC ACTIVITY	2000	2001	2002	2003	2004	2005	2006	2007*
Agriculture, Forestry and Fishing	17.2	16.0	15.2	15.2	15.0	14.2	13.7	13.2
Mining and Quarrying	6.4	7.0	7.9	7.7	8.4	8.6	8.7	8.0
Manufacturing	10.5	10.4	10.7	10.9	10.9	10.6	10.6	10.5
Electricity, Gas and Water	2.9	3.1	2.9	2.7	2.6	2.6	2.7	2.6
Construction	4.9	5.3	6.0	6.9	7.9	9.1	9.8	10.4
Wholesale and Retail trade	18.3	18.4	18.7	18.8	18.8	18.3	17.5	17.2
Restaurants, Bars and Hotels	1.9	2.3	2.3	2.4	2.4	2.5	2.8	3.0
Transport, Storage and Communications	6.3	6.2	6.1	6.1	6.1	6.5	7.4	8.5
Financial Institutions and Insurance	8.2	7.8	7.9	7.7	7.6	7.5	7.3	7.2
Real Estate and Business services	9.5	9.4	9.5	9.4	9.3	9.1	8.8	8.6
Community, Social and Personal Services	7.7	7.8	7.7	7.4	7.1	7.5	7.7	8.2
Less: FISIM	(4.9)	(4.8)	(4.7)	(4.6)	(4.5)	(4.4)	(4.2)	(4.1)
TOTAL GROSS VALUE ADDED	89.1	88.9	90.0	90.7	91.5	92.0	92.7	93.3
Taxes on Products	10.9	11.1	10.0	9.3	8.5	8.0	7.3	6.7
TOTAL G.D.P. AT MARKET PRICES	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: CSO, National Accounts

While copper prices are expected to stay high in the medium term, much more sectoral diversification is called for, certainly with better up stream and downstream linkages between the growth pole of mining and the manufacturing sector. More value added is needed in processing the output of the mining sector. Increasing food prices also imply the need for ramping up investment in agriculture, both for food security and as an export granary in Southern and Sub Saharan Africa.

5. The Structural Dependence of Growth on Exports

Export growth is critical for competitiveness. Zambia's reliance on export growth of extractives has been extremely high. This reliance has some plus and some minus points. The plus points are as seen above, that Zambian export growth of extractives has led to the pick up in growth over the 2000s after a long interruption in sustained growth over the 80s and the 90s. And this export led growth has been largely based on the rising price in copper, which is expected to remain high in the medium term given rising global demand. The minus points are, one, that copper exports are not sufficiently linked to domestic sectors like manufacturing, and domestic drivers of growth like consumption and investment. And, two, export of extractives has appreciated the exchange rate, which inhibits exports of higher valued added products of the manufacturing sector – euphemistically known as the Dutch disease. Policy clearly has to prioritise growth of manufacturing, and domestic consumption and investment, by increasing their linkages to export of extractives.

The enclave nature of export of extractives is seen through its weak impact on the aggregate economy. Table 8 shows the four drivers of growth, exports, consumption, investment and government expenditure for the period 2003-07, when growth has picked up. The table shows that between 2003 and 2007, export growth ranges between 10% and 13% per annum, clearly leading GDP growth ranging between 5% and 6% per annum. Consumption growth however is much weaker over this period,

ranging between negative and 8% per annum. So export growth of extractives is not feeding very well into growth of consumption for the mass of the population. Further, and very surprisingly, the high export growth of extractives is not being fuelled by gross fixed investment, which ranges between negative and 7%, with only one high of 12% in 2007. The fourth driver of growth has obviously been constrained by the macro framework adopted, to control inflation, government expenditures and restore competitiveness through privatisation of loss making SOEs. However its growth is still high, ranging between 8% and 11%, although slumping to zero in 2004.

Table 8: Expenditure on GDP (% real change)

	2003a	2004a	2005a	2006b	2007b	2008c	2009c
Private Consumption	-0.1	7.1	8.8	6.3	7.6	8.0	8.0
Government consumption	10.9	0.0	13.8	8.0	9.0	9.0	7.0
Gross fixed investment	6.1	-3.8	6.0	7.0	12.0	6.0	3.0
Export of goods and services	10.1	12.6	12.3	11.3	9.6	10.8	9.5
Imports of goods and services	3.7	10.9	20.6	12.6	15.0	13.5	10.2

a Actual. b Economist intelligence unit estimates. c Economist Intelligence Unit forecasts
Source: IMF, *International Financial Statistics*

An example of the weakness of the domestic component of investment is afforded through public investment. Table 9 gives the current and capital expenditures for the budget for 2005. Of a total budget of K 9.3 trillion, current expenditures are K 6.7 trillion, while capital expenditures are K 2.7 trillion. 82% of the capital expenditures are financed through foreign inflows.

Table 9: Expenditures, 2005

	Budget (K'Billion)	Releases (K' Billion)	Variance of Release Vs Budget	% Variance of Total Budget
Total Expenditures	9,395.2	8,845.8	-549.4	-5.8
Current Expenditures	6,670.2	6,056.2	614.0	-9.2
Capital Expenditures	2,725.0	2,789.6	64.6	2.4
Domestically financed of which:	488.5	565.1	76.6	15.7
PRP	109.0	239.5	130.6	119.8
Stadiums	5.0	3.5	-1.5	-30.9
GRZ/Road Infrastructure Projects	100.0	60.5	-39.5	-39.5
Counterpart (Non- PRP)	6.0	4.2	-1.8	-29.5
Ordinary Capital	161.1	88.9	-72.2	-44.8
Fuel Levy (road fund)	90.0	163.4	73.4	81.6
Rural Electrification Fund	11.3	5.1	-6.2	-55.1
Land Development Fund	6.1	-	-6.1	-100.0
Foreign Financed	**2,236.5**	**2,224.5**	**-12.0**	**-0.5**

The high export growth of extractives has led to a sharp appreciation of the Kwacha by 17% between 2003 and 2007. Further appreciation in this year, raises the level of appreciation over this period to 24%, which is a rate of 5% per annum. This appreciation of the exchange rate helps ward of importing inflation, but dampens the competitiveness of the manufacturing sector in exporting higher value added products. It is this factor which underlies the weak growth rates and constant shares in GDP of the manufacturing sector.

6. The Impact of Growth on Employment and Decent Work

The impact of the pick up in growth over the 2000s has been seen to be not only led, but also largely limited to growth in extractive exports. Growth in the manufacturing sector has not benefited from this growth led by the mining sector, nor has growth in trade and services. The only other sector that has grown significantly over this period has been construction. The impact of this growth in extractive exports on domestic consumption and investment also appears to be weak.

The only significant way in which growth can be participated in by the majority of the population of a country, is through generation of employment, and improvement in critical conditions of employment like the real wage and social protection for the vulnerable. That is, inclusive growth has to be based on generation of Decent Work. However, the impact of this pickup in growth on employment looks weak. Formal unemployment could well have increased over the 2000s. The sectoral employment structure remains unchanged over this period. While the informal economy, always predominant, has expanded further. Macro policy clearly now needs to prioritise employment along with growth in the FNDP and the Medium Term Expenditure Framework (MTEF).

The most recent Labour Force Survey (LFS) for 2005 gives an estimate of the labour force of 4.3 million.

Table 10 gives an estimate of the employment rate between 1998 and 2008. The table shows that the employment rate drops from 58% in 1996 to 55% by 2006. This drop in the employment rate, coincident with the pick up in GDP growth could be based on a falling labour force participation rate, for which we do not yet have a good estimate. Therefore it is more important to look at the unemployment rate.

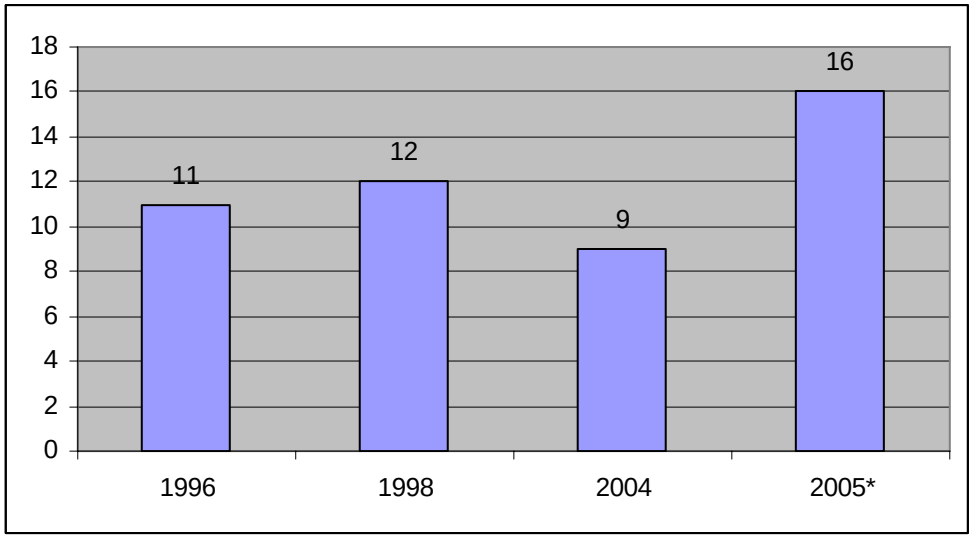
Table 10: Employment Rate amongst the Entire Population

	Male	Female	Urban	Rural	Zambia
1996	63	53	42	67	58
1998	59	50	37	65	54
2004	63	55	45	68	59
2006	60	52	39	65	55

Source: Central Statistical Office)2007) *Living conditions Monitoring Survey V,* CSO (2005) *Living Conditions Monitoring Survey Report, 2004,*CSO (1999) *Living Conditions in Zambia, 1998;*CSO (1997) *Living Conditions Monetary Survey 1, 1996* All Lusaka, Zambia

There are two parallel estimates of the unemployment rate. The primary estimate of unemployment has to be based on the LFS for 2005, compared to earlier estimates from LFSs and Living Conditions Surveys[9]. This is given in Figure 3. The figure shows that the registered unemployment rate rose between 1996 and 2005, from 11% of the labour force to 16%. Given that GDP growth has been 5% per annum between 2000 and 2006; this inverse impact on registered unemployment is unexpected.

Figure 3: Unemployment rates, 1996 – 2005



Source: CSO LFS, LCMS

A second estimate of the unemployment rate is based on a CSO estimate of unemployment for 2006, provided for the mid term review of the Fifth FNDP. This is given in Table 11, and shows an unemployment rate of 9% for men and 10% for women. If this estimate is credible, it shows a decline in the unemployment rate from 11% in 1996 to 9% by 2006. However even this estimate shows a slight increase in the rate of unemployment over the 2000s. And the more generally accepted figure for the unemployment rate has to be based on the LFS for 2005, of 16%.

Table 11: Unemployment Rate

	Male	Female	Urban	Rural	Zambia
1996	11	10	17	7	11
1998	9	7	13	4	8
2004	6	6	12	2	6
2006	9	10	19	3	9

Source: Central Statistical Office)2007) *Living conditions Monitoring Survey V,* CSO (2005) *Living Conditions*
*Monitoring Survey Report, 2004,*CSO (1999) *Living Conditions in Zambia, 1998;*CSO (1997) *Living Conditions*
Monetary Survey 1, 1996 All Lusaka, Zambia

[9] There are issues of comparability which are dealt with in a more detailed version of this paper.

The sectoral structure of the employed labour force also shows no impact of the pick up in growth. Table 12 gives the shares in employment across sectors for 1998 and 2005. The growth pole for the economy, the mining sector employed only 1% of the labour force in 2005, and this has dropped from 2% of the labour force in 1998. The manufacturing sector employed 4% of the labour force in 2005, which has remained unchanged since 1998. All the other non agricultural sectors show a similar constancy in their share of employment over time, or a drop, with construction unchanged at 1%, trade at 10%, transport at 2%, and catering an finance at 1% each, while community and personal services have dropped from 9% to 7%. The only increase in employment share has been in agriculture moving up from 70% to 72%.

Table 12: Percentage distribution of employed persons by sector, 1998, 2004 and 2005

Industry	1998	2004	2005
Agriculture, forestry and fisheries	70	69	72
Manufacturing	4	4	4
Construction	1	1	1
Trade, wholesale and retail distribution	10	10	10
Hotels and restaurants	1	1	1
Transport and communication	2	2	2
Finance, insurance and real estate	1	1	1
Community, social and personal services	9	9	7
Mining and quarrying	2	2	1
Electricity, gas and water	0	0	0
Not Stated	0	0	0

*2005 figures are LFS, the rest are LCMS data

The informality in employment also shows no signs of the impact of the pick up in growth, in fact the opposite, with informality increasing over time. Table 13 gives estimates of employment in the informal economy for selected years between 1996 and 2006. The table shows that almost three quarters of the labour force was employed informally in 1996, and this share has increased consistently over time to 82% of the labour force by 2006. 90% of the rural labour force is informally employed, while three quarters of the urban labour force is informal.

Table 13: Informal Sector Employment Rates

	1996	1998	2004	2006
Zambia	74	79	81	82
Rural	84	91	91	91
Urban	48	48	57	75

Source: Central Statistical Office)2007) *Living conditions Monitoring Survey V,* CSO (2005) *Living Conditions*
*Monitoring Survey Report, 2004,*CSO (1999) *Living Conditions in Zambia, 1998;*CSO (1997) *Living Conditions*
Monetary Survey 1, 1996 All Lusaka, Zambia

Table 14 presents a long time series of formal employment from 1985 to 2007. The table shows that formal employment has decreased in absolute terms, from 522,000 in 1985, to 501,000 by 2007. The formal employment share has gone down for agriculture from 15% in 1985 to 12% by 2007, for mining from 12% to 10%, for manufacturing from 15% to 11%, for construction from 8% to 3%, and for transport from 6% to 4%. The formal sector employment share has gone up for trade from 8% in 1985 to 13% by 2007, for financial services from 6% to 10%, for personal and community services from 28% to 36%, and for utilities from 1% to 2%.

Table 14: Percent distribution of formal employment by sector (1985 - 2007)

Year	Agricultural	Mining & Quarrying	Manufacturing	Electricity, Gas & Water	Construction	Trade	Transport	Business & Financial Services	Personal & community services	Total
1985	15	12	15	1	8	8	6	6	28	521,900
1986	15	12	14	1	8	9	6	6	34	526,500
1987	15	12	14	1	7	9	6	6	29	530,000
1988	15	12	14	1	7	10	6	6	29	533,400
1989	15	12	14	1	7	10	6	6	29	540,500
1990	15	12	14	1	6	10	6	6	29	543,300
1991	14	12	14	1	6	10	6	7	30	544,200
1992	15	11	13	2	5	9	6	7	31	545,900
1993	16	11	13	1	4	9	6	7	32	520,000
1994	16	10	12	1	4	10	6	7	35	496,000
1995	14	11	11	1	2	9	8	9	36	485,000
1996	14	10	10	1	3	10	8	8	37	479,400
1997	12	9	10	1	4	10	10	8	36	475,161
1998	13	8	10	1	3	10	10	8	37	466,925
1999	13	8	10	1	3	11	9	7	39	477,508
2000*	12	7	10	1	3	11	10	7	39	476,347
2001*	12	7	10	1	3	11	10	7	39	475,316
2002	10	9	16	2	1	12	5	12	34	429,406
2003	15	12	9	3	1	13	6	7	34	416,804
2004*	16	11	11	3	1	11	6	8	33	416,228
2005	15	7	9	1	2	15	5	5	40	436,336
2006	14	7	11	3	2	12	4	9	37	475,835
2007*	12	10	11	2	3	13	4	10	36	500,616

Source: CSO Quarterly Employment and Earnings Inquiry, 2007
*Data not collected for all quarters

Table 15 gives the occupational categories of employment, which could shed some light on the informality estimates for the 2005 labour force. The table shows that in 2005, of an employed labour force of 4.1 million, 43% were self employed, 38% were unpaid family workers, 17% were paid employees, and 1% were employers. The self employed plus the unpaid family workers add up to 81% of the employed, which is quite consistent with the informality estimate of 82% of the labour force seen in Table 13. This implies that the formal economy largely comprises the 17% paid employees and 1% employers, while the informal economy largely comprises the 43% self employed and the 38% unpaid family labour. It does not of course imply exact correspondence.

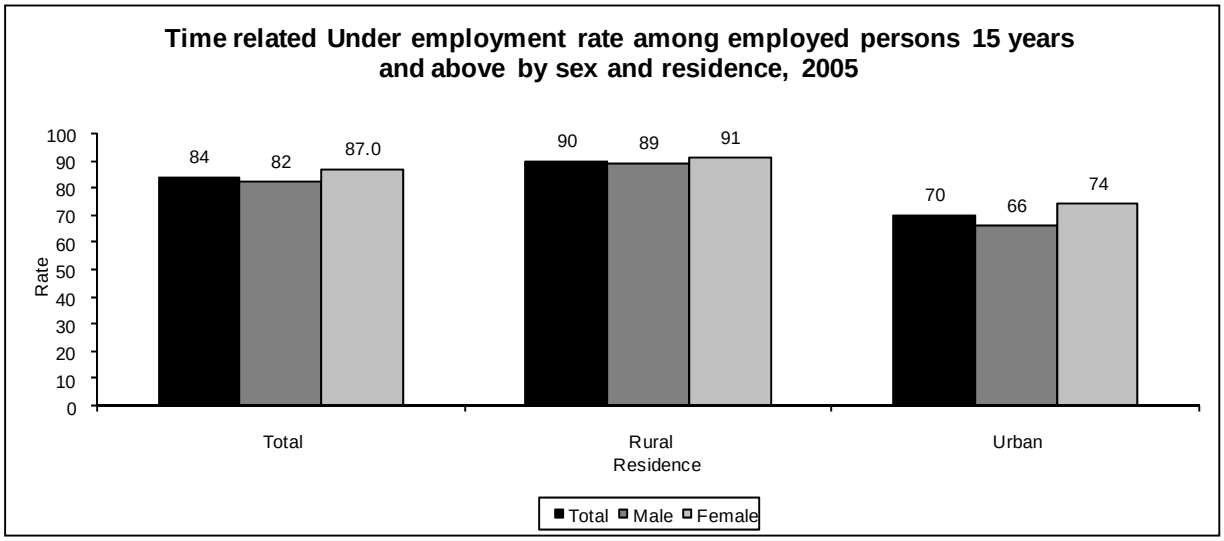
Table 15: Percentage distribution of currently employed persons aged 15 years and above by employment status and sex, 2005

	Employment status				Employed Persons	
	Self-employed	Employer	Paid employee	Unpaid family worker		
All Zambia	43	1	17	38	100	**4,131,531**
Male	51	1	22	26	100	2,213,835
Female	34	1	12	53	100	1,917,696

Source: 2005 Zambia Labour Force Survey

There is also a good correspondence between estimates of underemployment for 2005 and estimates of informality in employment. Figure 4 estimates time related underemployment in 2005 at 84%. This implies that largely everyone in the informal economy was underemployed. Table 16 corroborates that a large part of this underemployment was due to 72% of all employment in 2005 being part time employment.

Figure 4: Time related underemployment among employed persons 15 years and above by sex and residence, 2005



Source: 2005 Zambia Labour Force Survey

Table 16: Part-time employment rates by sex and residence, 2005

	Part-time employment rate			Number of persons
	Both	Male	Female	
Total	72	67	78	4,131,531
Rural	83	81	85	3,019,421
Urban	42	37	51	1,112,110

Source: 2005 Zambia Labour Force Survey

The pick up in growth over the 2000s therefore seems to have left a lot of slack in the labour market, with 16% registered unemployment, and 84% underemployment. This growth also seems to have left the traditional sectoral structure of the labour force unaltered, with an obviously capital intensive mining sector employing only 1% of the labour force, and not well linked at all to a manufacturing sector constant at 4% of the

labour force, or indeed any of the other sectors which have also been constant over time. Policy therefore needs to be addressed towards generating employment and increased sectoral diversification of this employment. The correspondence in estimates for informality and underemployment implies that informality is based much more on lack of demand, rather than on refuge from formality.

7. The Impact of Growth on Poverty

The pick up in growth in the 2000s has had some impact on poverty and income inequality, bringing both down. However the levels of poverty and income inequality in Zambia still remain very high. Regionally the poorer provinces are the western and central provinces, while the lowest poverty levels are around Lusaka and the copper belt. Decomposition of poverty by employment shows the poor and extremely poor to be amassed in agriculture, in self employment or unpaid family work. Poverty levels are the lowest amongst paid employees. Employment and critical conditions of employment like the real wage and social protection for the vulnerable then remains the most sustainable route out of poverty, as the ILO strongly contends[10], and Zambia's policy to alleviate poverty must focus on this.

Tables 17 and 18 give the incidence of poverty and extreme poverty in the total population for survey years between 1991 and 2006. The national poverty line used for this estimation by the Central Statistical Office, is based on a criteria of a minimal income to meet basic needs[11]. Extreme poverty is estimated using a national poverty line based on a criterion of a lower than minimal income to meet basic needs.

Table 17: Trends in Poverty

	1991	1993	1996	1998	2004	2006
Zambia	70	74	69	73	68	64
Rural	88	92	82	83	78	80
Urban	49	45	46	56	53	34

Source: Central Statistical Office)2007) *Living conditions Monitoring Survey V,* CSO (2005) *Living Conditions*

*Monitoring Survey Report, 2004,*CSO (1999) *Living Conditions in Zambia, 1998;*CSO (1997) *Living Conditions Monetary Survey 1, 1996* All Lusaka, Zambia

Table 18: Trends in Extreme Poverty

	1991	1993	1996	1998	2004	2006
Actual Poverty	58	61	53	58	53	51
Rural	81	84	68	71	65	67
Urban	32	24	27	36	34	20

Source: Central Statistical Office)2007) *Living conditions Monitoring Survey V,* CSO (2005) *Living Conditions Monitoring Survey Report, 2004,*CSO (1999) *Living Conditions in Zambia, 1998;*CSO (1997) *Living Conditions Monetary Survey 1, 1996* All Lusaka, Zambia

[10] ILO, 2003, the Working out of Poverty, The Director General's Report to the International Labour Conference.

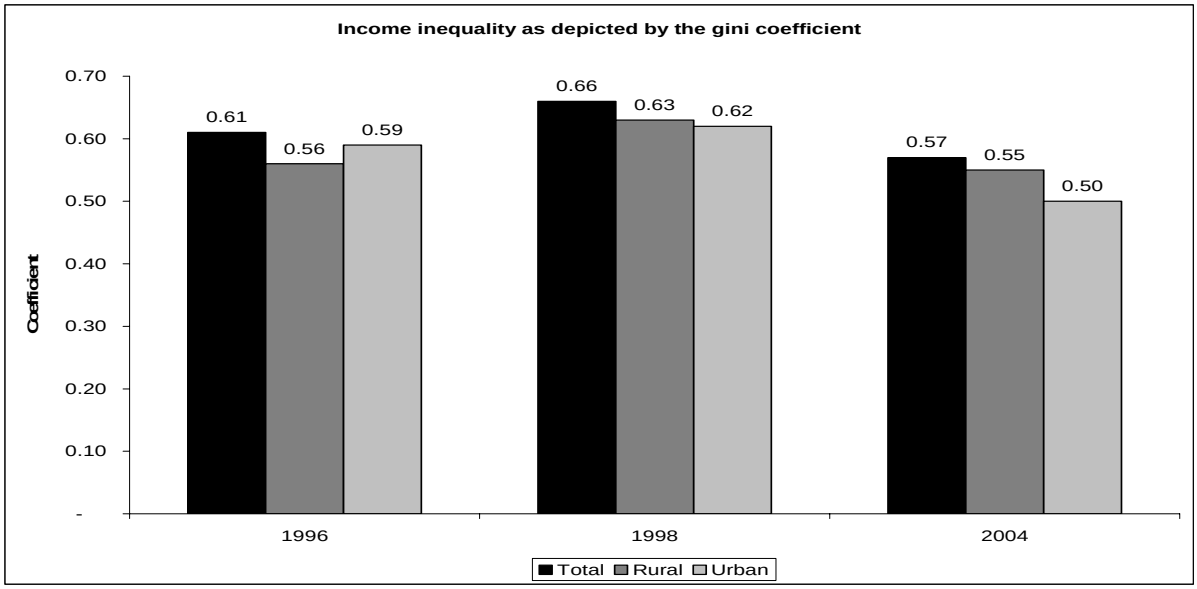
[11] Methodology discussed in more detailed paper.

Table 17 shows that headcount was at its highest in 1998, at 73% of the population, when GDP growth had fallen negative. The pick up in growth has reduced the headcount by 9% to 64%. Table 18 shows that extreme poverty was also at a high in 1998 of 58%, and the pick up in growth since has reduced the headcount by 7% to 51%.

The levels of poverty however remain very high, with near two third of the total population in poverty, and more than a half in extreme poverty. Poverty also remains strongly rural, with 80% of the rural population poor, while a third of the urban population is poor. Rural poverty has proved more stubborn to reduce over time, with rural poverty falling by only 3% between 1998 and 2006, while urban poverty fell by 22% over this period. Extreme poverty in rural areas also fell by only 4% between 1998 and 2006, while in urban areas it fell by 16%.

Figure 5 gives the Gini coefficient as an estimate of income inequality for 1996, 1998, and 2004. The Gini also peaks at 0.66 in 1998, along with poverty, when GDP growth fell negative. With the pick up in growth, the Gini index falls to 0.57 by 2004. Income inequality like poverty still remains very high in Zambia.

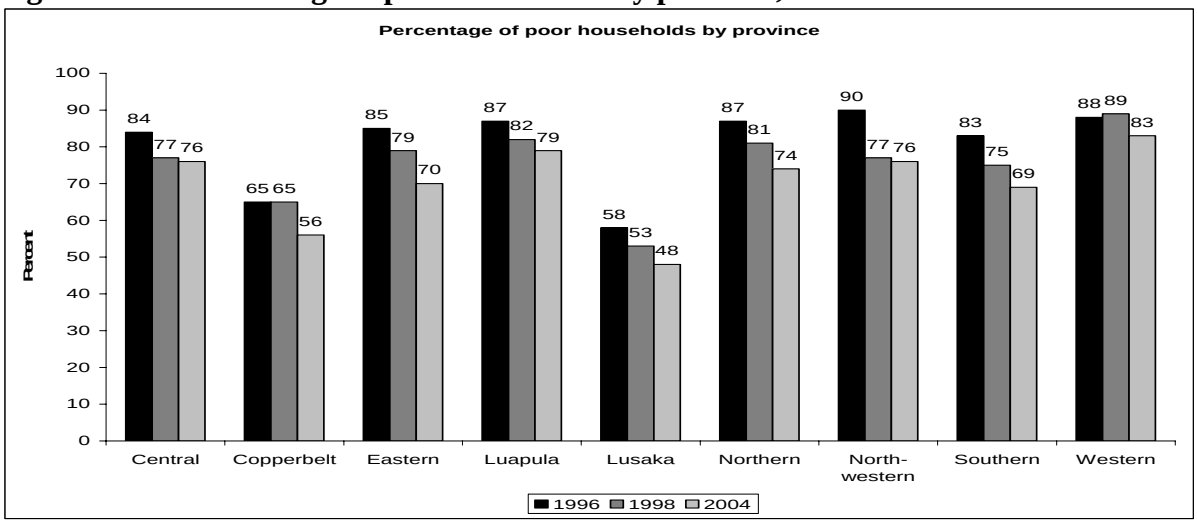
Figure 5: Trends in income inequality as depicted by the gini-coefficient, 1996-2004



Source: CSO, LCMS_1996, 1998 & 2004

Regionally, poverty is the highest in the western province, where the headcount was 83% in 2004, in Luapula with a headcount of 79%, and in the central and northwestern provinces with headcounts of 76% each (Figure 6). Poverty is the lowest around Lusaka with a headcount of 48%, and the copper belt with a headcount of 56%.

Figure 6: Percentage of poor households by province, 1996-2004



Source: CSO, LCMS_1996, 1998 & 2004

Policy to tackle poverty must focus on the causality behind such low incomes. Table 19 determines the incidence of poverty in the employed population, by sectors, for 2004. The amassing of poverty in the rural areas implies a high incidence of poverty in agriculture, which Table 19 shows to be 84% of the total employed population of 4.1 million. Table 20 similarly determines the incidence of poverty in the employed population by their occupations, for 2004. The table shows that the self employed, with a headcount of 54%, and unpaid family workers, with a headcount of 36%, were the poorest amongst the 4.1 million employed. Conversely, poverty was the lowest for paid employees, with a headcount of 10%. This finding has two strong policy implications.

Table 19: Percent distribution of employed persons by industry and poverty status, 2004

	Poverty Status			
Industry	**Extremely Poor**	**Moderately Poor**	**Non-poor**	**Total**
Agriculture	84	65	50	2,896,235
Mining	1	2	2	62,863
Manufacturing	3	5	5	147,841
Electricity, Water and Gas	0	0	1	17,639
Construction	1	2	2	57,921
Wholesale trade, hotels and restaurants	6	13	17	436,045
Transport and communication	1	2	4	84,100
Finance and business services	1	1	2	50,495
Personal and community services	4	10	16	360,630
Total	**100**	**100**	**100**	**4,113,769**

Source: CSO LCMS

Table 20: Percent distribution of employed persons by employment and poverty status, 2004

	Poverty Status			
Employment Status	**Extremely Poor**	**Moderately Poor**	**Non-poor**	**Total**
Self Employed	54	53	50	2,161,195
Paid Employee	10	22	32	775,661
Employer	0	0	0	6,003
Unpaid Family Worker	36	24	18	1,172,911
Other	0	0	0	14,065
Total	**100**	**100**	**100**	**4,129,835**

Source: CSO LCMS

One, employment, and critical conditions of employment like the real wage, and social protection for the vulnerable, have to be the main sustainable route out of mass poverty such as Zambia faces. The high levels of registered unemployment of 16%, and very high levels of underemployment, of 80%, endemic in the vast informal economy, despite the pick up in growth, compel this stubbornly high incidence of poverty. Policy for poverty reduction must focus on generating higher levels of productive employment, sustaining real wages compatible with productivity levels, and providing a social floor particularly for the vulnerable.

Two, the amassing of the vast majority of the population, and most of the poverty in rural areas, and in agriculture, implies the need for a massive increase in investment in agriculture. High food prices, the need for food security, and the vast potential for Zambian agriculture, with only a small fraction of its arable irrigated as yet, imply that the country can become the granary of Southern and Sub Saharan Africa.

A policy proposal that brings coherence between these two needs, generating employment, basic wages, a minimal social floor, with a strong rural focus, is an employment guarantee scheme. The pioneer of such a scheme is India's National Employment Guarantee Scheme, which guarantees 100 days of employment at just below the minimal wage to each household. This supply of labour is then used to develop much needed infrastructure. The budget for such a national scheme in India approximates 2% of GDP. However the ILO is suggesting initial pilots of such a social floor, in a number of lower income countries that cannot yet afford cash transfers. Zambia could usefully experiment with a pilot in its poorest provinces.

A major constrain is the budgetary framework to which Zambia is committed under the PRGF.

8. Budget Constraints on Growth, Meeting the MDGS, and Employment

The macro policy framework chosen by Zambia, and adhered to, has played a major role in delivering the pick up in growth over the 2000s. This sustained pick up in growth has come after a long interruption in growth over the 80s and the 90s. It has been based strongly on the increase in copper prices for exports. The policy reforms have enabled a more efficient supply response to the resurgent demand.

However the base of this growth has been quite narrow almost restricted to the mining sector. The structure of the economy has not diversified at all and remains dependent

on exports of extractives. Links between the mining sector and manufacturing, through for example higher value added from more processing, have been weak. So the sectoral share of manufacturing in GDP has remained very low and constant.

The impact of this pick up in growth over the 2000s on employment has been ambiguous at best, with registered unemployment possibly showing an increase, the mining sector remaining capital intensive and so hiring only 1% of the labour force, and the manufacturing sector employing only another 4% of the labour force. Agricultural employment has continued to predominate, while the informal economy beset by under employment and part time employment has increased in preponderance to four fifths of the labour force. The impact of this pick up in growth on poverty has therefore also been limited. Poverty remains entrenched in self employment and unpaid family work, while it is lowest in paid employment.

The ILO holds that the only sustainable means for more inclusive growth and significant poverty reduction has to be through generation of employment and improvement in critical conditions of employment, like the real wage, and the provision of a social floor especially for the vulnerable. There are two constraints on the generation of more decent work, one in the private sector, and one in the public sector. Both constraints are given by the macro policy framework, which needs to be eased, with a little more tradeoff of fiscal and monetary prudence for higher private and public investment, growth, and employment.

The private sector constraint on investment is quite clear. Zambia is part of a sub Saharan region that has one of the lowest savings rate in the world. Gross domestic savings in the region were 17% of GDP, compared to 26% in South Asia, and 24% in Latin America[12]. Zambia itself had a gross savings ratio of 23% in 2006[13]. A savings ratio of 23% gives a GDP growth rate of 5% with a capital output ratio of 4.6. Which means that for Zambia to squeeze out another 1% of GDP growth will require raising savings by another 4.6%. On the supply side, the current cost of borrowing of 19% is too high to permit this. On the demand side, aggregate demand in the domestic economy is already low because of high levels of poverty, unemployment, and underemployment, while highly regressive indirect taxation at very high rates further dampens demand for products and therefore investment.

The public sector constraint on investment is twofold. One, ILO's employer constituents are emphatic in their need for public sector investment in infrastructure, to enable private sector investment. They insist that two decades of attempting to secure private sector investment for public infrastructure in Africa has failed and consequently held back private investment in goods and services. Two, public sector investment in physical and social infrastructure has been constrained in Zambia by the 8% of GDP cap on the wage bill. An increasing population, and increasing coverage of it, requires increasing education, health and social services, not least to meet the MDGs. Moving the cap to its current 8.6% of GDP will not allow this. It will also not allow a very affordable social floor through an employment guarantee scheme which is the only viable macro answer to the large slack in the labour market and mass poverty.

[12] World Bank, 2007.
[13] World Development Indicators, 2008.