February 27, 1992

UP FROM POVERTY: ADVANCING ECONOMIC DEVELOPMENT IN ZAMBIA

INTRODUCTION

Africa is a continent of poverty-stricken countries that are getting poorer every year. Zambia, located in the central part of southern Africa, is no exception. This country of 8 million people, once among Africa's wealthiest, long has suffered with one of Africa's worst performing economies. Zambia's real per capita gross national product (GNP) has fallen roughly two percent per year since 1965, and was a meager $380 last year. To make matters worse, Zambia is saddled not only with a foreign debt of at least $8 billion, or $1,000 for each Zambian, one of the largest per capita debts in the world, but with deteriorating roads and railways. Zambia also faces a potentially acute food shortage, despite its capacity to produce large food surpluses.

In seeking explanations for its economic problems, Zambia must look within, for it is Zambia's quarter-century experience with government-run economic policies which is causing its economic misery. Kenneth Kaunda, president of Zambia from the time it gained independence from Britain in 1964 until last November, transformed the free market economy that Zambia inherited into the kind of bloated, inefficient statist economy that has damned most of post-Independence Africa. Although Kaunda began dabbling with reforming his economy in 1982, he never went far enough to reverse his country's economic decline. Whether Frederick Chiluba, who was elected Zambian president last October 31, can succeed where Kaunda failed depends on whether he adopts far-reaching free market reforms.

Promoting Zambia. Chiluba last week met with George Bush at the White House. Also on his American itinerary was a meeting with the American Federation of Labor-Congress of Industrial Organizations (AFL-CIO) Ruling Executive Council in Bal Harbour, Florida, and a speech at the National Press Club in Washington. Throughout his American visit, Chiluba promoted Zambia to potential investors and underscored the need for additional foreign assistance. In their meeting, Bush expressed support for Chiluba's movement toward a free market economy.

The United States has an interest in Chiluba's success. American companies have a modest yet growing business with Zambia, exporting $80 million worth of goods and services to Zambia in 1990. Washington, moreover, would like to see the success of Zambia's experiment in democracy, witnessed by last year's election of Chiluba. And

Zambia's experiment in democracy, witnessed by last year's election of Chiluba. And Zambia will be watched closely by many Africans curious about the man who toppled the seemingly invincible Kaunda. If Chiluba were to make comprehensive economic reforms and ignite economic growth in Zambia, then he and his country could become a welcome model for other African nations to follow. Such a model would bolster the still fragile consensus of support for free market economics among Africans, making the free market conversion of other African economies politically easier.

America must accept part blame for Zambia's economic ills. Washington gave Zambia hundreds of millions of dollars in economic development aid since Kaunda began instituting a statist economy in the mid-1960s.[1] Although well-intentioned, this aid subsidized and prolonged the life of Kaunda's ruinous economic policies.

The Bush Administration and the U.S. Agency for International Development (AID), which administers U.S. aid policy toward Zambia, need to reverse the mistakes of the past and pursue a free market aid strategy toward this poor country. AID already has made some progress in doing this. Along with other bilateral donors and the International Monetary Fund (IMF) and World Bank, AID has been pushing Zambia toward free market reforms. Chiluba seems receptive to this, having taken the important step of reducing the government subsidy on consumer corn meal prices last December.

To assure that free market reforms take hold in Zambia, the Bush Administration should:

- **Require AID to develop a plan for Zambia's transition to a free market economy.** This should encompass the full range of the Zambian government's economic policies: credit and monetary policy, taxation, regulation, and property rights, among others. A comprehensive plan would give the U.S. Executive Director to the IMF, Thomas Dawson, additional information to assess when to use America's IMF voting muscle to ensure that Zambia's upcoming IMF-monitored free market transition program is devised and carried out effectively.

- **Instruct that AID's sound free market aid strategy toward Eastern Europe be adopted for Zambia and other African countries.** AID's technical assistance programs in Eastern Europe emphasize privatization and other free market reforms. Its programs in Zambia should be no different.

- **Mandate that AID use the Index of Economic Freedom to gauge aid to Zambia.** The Index of Economic Freedom is a means of quantitatively determining the extent to which a country's economy is a free market. It provides an analytically rigorous means of allocating resources among those countries receiving American development assistance.

1 The U.S. is not alone in its complicity. Kaunda managed to make Zambia one of the world's largest per capita recipients of foreign aid throughout the 1970s and much of the 1980s. In 1988, the U.S. was its tenth largest bilateral donor, providing Zambia with approximately 4 percent of its total foreign aid. Zambia's leading bilateral donors for 1988, in descending order, are Japan, Germany, Italy, Norway, Canada, and the Netherlands.

- **Send Peace Corps volunteers, if invited by Zambia, to promote the formation of small businesses.**

- **Stop undermining South Africa's economy, to which Zambia's economy is linked.** U.S. economic sanctions against South Africa effectively prohibit South Africa's access to IMF credit, which raises its cost for international capital. This policy enormously penalizes Zambia's economy; an economically strong South Africa is a necessary market for and source of Zambian goods. The U.S. should support South Africa's access to credit from the International Monetary Fund.

KAUNDA'S POLITICAL FALL

Zambia for 75 years was the British colony of Northern Rhodesia. A 1889 grant of a Royal Charter to the Cecil Rhodes's British South African Company (BSAC) marked the beginning of Zambia's colonial experience. The BSAC mining conglomerate, through the Royal Charter, acquired mining rights in exchange for promising to protect the tribal chiefs in the territory of Northern Rhodesia. This "Company Rule" lasted until 1924, when Britain began direct colonial administration over Northern Rhodesia. From 1953 through 1963 Northern Rhodesia was united with Southern Rhodesia (now Zimbabwe) and Nyasaland (now Malawi) in the Federation of Rhodesia and Nyasaland. Northern Rhodesia became the independent Republic of Zambia on October 24, 1964.[2]

Kaunda, who had been a leader of the Zambian independence movement and head of the United National Independence Party (UNIP), became president of Zambia in 1964. For eight years he tolerated political competition, and then banned opposition political parties. The foundation of "one-party participatory democracy" was cemented a year later by Zambia's 1973 constitution. The UNIP faced no political competition until December 1990, when Kaunda, responding to domestic and international pressures, allowed opposition parties to organize. After considerable foot-dragging, Kaunda on September 4, 1991, set October 31 as the date for Zambian national elections.

Decisive Victory. That election was won by Frederick Chiluba, the elected leader of the 300,000-member Zambian Congress of Trade Unions and the Movement for Multiparty Democracy (MMD). Chiluba took 81 percent of the vote against Kaunda, while MMD candidates won 125 of the 150 legislative seats against the UNIP and some fifteen minor party candidates. Kaunda, a figure with a high international profile, peacefully and graciously relinquished power after his massive defeat.

2 Zambia, bordering Angola, Botswana, Malawi, Mozambique, Namibia, Tanzania, Zaire, and Zimbabwe, is 290,585 square miles, slightly larger than Texas.

THE DISMAL ECONOMIC LEGACY OF KAUNDA

Zambia did not inherit a statist economy. Nor did Zambia inherit a foreign debt; at independence, Zambian foreign reserves totaled $3 billion. A 1964 Zambian White Paper on industrial policy recommended that the government choose the capitalist road to economic development and placed considerable emphasis on private foreign investment. This was Zambia's general course until 1968. That year, Kaunda denounced foreign investors as exploiting Zambia and he decreed that Zambia would rely on its own resources. He also insisted that Zambia's "humanist" philosophy, of which he was the chief philosopher, demanded public ownership of property. In 1968, too, he defined his vision for Zambia's future in the so-called "Mulungushi Declaration," proclaimed in the central Zambian town of that name. The Declaration's lofty aim: redistributing economic power in favor of "the poor and the weak."

Between 1968 and 1972 Zambia's predominately private economy was transformed into a predominately statist one. Kaunda's most important early strike against the private sector hit Zambia's crucial copper industry. The Zambian economy is dominated by mineral, particularly copper, exports. Zambia, in fact, is the world's fifth largest producer of copper, exporting approximately 450,000 tons per year. Zambia also exports a significantly smaller amount of cobalt, zinc, lead, coal, and several precious minerals. While mining comprises only some 15 percent of Zambia's GDP, it earns roughly 90 percent of Zambia's foreign exchange and provides the Zambian government with 30 percent of its revenue.

ZAMBIA DATABOX

Official Name: Republic of Zambia

Capital: Lusaka

Head of State: President Frederick Chiluba

Area: 290,585 square miles, slightly larger than Texas

Population: 8,112,782

Gross Domestic Product: $3.1 billion (1991 est.)

Per Capita Income: $380

Real Economic Growth Rate: 0.9%

Inflation: 85.0% (1991 est.)

U.S. Foreign Assistance: $20.7 million (1991)

External Debt: $8 billion (1990)

U.S. Investment: $56,000,000 (1989)

Total Exports: $1.29 billion (1990) — copper, zinc, cobalt, lead, tobacco
Exports to U.S.: $29 million

Exports to Africa: $120.9 million

Total Imports: $1.04 billion (1990) — machinery, transport equipment, foodstuff, fuels, manufactures
Imports from U.S.: $80 million

Imports from Africa: $69.0 million

Source: Michael Johns, *U.S. and Africa Statistical Handbook, 1991 Edition*, The Heritage Foundation, U.S. Department of Commerce, *Foreign Economic Trends and Their Implications for the United States*, Zambia, July 1991.

Heritage InfoChart

Nationalizing Industry. In 1970, the Zambian government took controlling ownership of all foreign-owned copper companies. Revenues from Zambian copper exports in the bullish international copper markets of the late 1960s and early 1970s were used by the government to nationalize most of Zambia's industrial sector. Throughout the 1970s, Zambia Industrial and Mining Corporation, Ltd. (ZIMCO), the state holding company, took controlling ownership of some 140 industrial enterprises, including the Zambian Consolidated Copper Mines, Ltd. (ZCCM). ZIMCO also seized control of Zambia's hotels, real estate ventures, and the country's sole insurance company. The result: some 80 percent of the Zambian economy today is controlled by state-owned enterprises.[3] The few areas of private-sector domination have been banking, commercial agriculture, construction, and highway transportation.

Zambia's state-owned and managed industrial, agricultural, and commercial enterprises, like the vast majority of those throughout Africa, are economic losers. Corruption is rampant, accountability is minimal, and concern for economic efficiency is placed well behind political considerations. The government was far more concerned with putting people on the public payroll than making production efficient. The Chiluba government at present is chasing down 10,000 "ghost workers" reportedly on the Zambian civil service payroll.

Staggering inefficiencies in Zambia's state-owned sector of the economy are shielded by a variety of government economic policies designed to discourage competing consumer imports. An overvalued exchange rate for the Zambian *kwacha*, government-controlled allocation of foreign exchange, import quotas, and tariffs effectively have guaranteed that inefficient Zambian state-owned producers face no sales competition from imports. Zambia's state-owned industries also enjoy minimal competition from the Zambian private sector firms, which must contend with an elaborate array of licenses, high taxes, and subsidies for state-owned enterprises.

Generous Benefits. The economic inefficiencies caused by these economic policies were masked temporarily in the 1970s by huge revenues from copper exports, as the world price for most raw materials surged. In 1974, for example, Zambia earned approximately $1.2 billion from exporting copper. These revenues financed generous welfare programs. As a result, the standard of living of most Zambians grew in the 1970s as tens of thousands fled the impoverished countryside seeking not only city jobs in the growing state-owned industries, but also the cities' generous education, health care, and consumer subsidy benefits provided by the government.[4]

This copper-financed boom of government spending, as predicted, proved unsustainable. Copper prices crashed some 40 percent between 1974 and 1975. Left facing a large number of city dwellers accustomed to a lifestyle that his government should never have provided and certainly could no longer afford, Kaunda refused to change policies. Determined to maintain his country's lifestyle, he borrowed heavily from foreign banks, governments, and the IMF. After it exhausted this foreign credit, Zambia borrowed more money from its domestic banks in 1977 and 1978 to pay for its expensive government programs. This government borrowing ignited an inflation rate of 16.5 percent per year in the late 1970s. Investor confidence plummeted and private credit was squeezed, among numerous other economic ills.

3 *Africa Report*, September/October, 1991, p. 71.

4 Other than South Africa, Zambia is sub-Saharan Africa's most urbanized country.

KAUNDA'S HALF-HEARTED REFORMS

With the technical and financial support of the IMF, the World Bank, Britain, Norway, and other countries, Kaunda made numerous attempts at free market economic reform starting in 1982. Significant free market economic reform, however, did not begin until the mid-1980s. At the behest of the IMF, Kaunda in 1985 reduced subsidies on many staple foods, cut the bloated civil service, decontrolled interest rates, and relaxed price controls. Without these moves, the IMF would not loan him the money to finance his growing balance of payments deficit.

Kaunda's reforms were thus grudging and thus ultimately failed. Meanwhile, economic conditions continued deteriorating. One result was the December 1986 riots in the copper mining towns of Kitwe and Ndola protesting the 120 percent rise in the price of corn meal, the staple food of Zambia. In response, Kaunda proclaimed that Zambia would cure itself with its own economic reform program, and not the one pushed by the IMF. Kaunda reintroduced price controls, inflated the *kwacha's* exchange rate, reimposed tariffs on imports, and weakened many of the free trade policies he had introduced after 1985.

Kuanda's attempt at an economic cure failed. And by September 1988 Zambia once again turned to the IMF and agreed to an aid-for-reform program. The following June, the Zambian government removed price controls on all items except corn, corn meal, and fertilizer. Kaunda unveiled plans in May 1990 for partially privatizing Zambia's bloated state-run enterprises. That year too, he liberalized the rules on the sale of corn, allowing producers to sell to private agents and millers, rather than requiring, as was the case, them to sell only to government-controlled cooperatives. As a result of these reforms, the IMF early last year commended Zambia for its progress, endorsing its new three year economic and financial program. This put Zambia on track to obtain new borrowing rights from the IMF, even though it was behind in its payments on past IMF loans.

Zambia's good standing with the IMF lasted only until last September, when Zambia violated the conditions of the IMF program. Kaunda's principal shortcomings were his failure to make a $20 million IMF loan repayment and to meet the IMF demand that Zambia's corn meal subsidy be reduced.

CHILUBA'S REFORMS

Chiluba's overwhelming electoral victory came about from more than Chiluba being an alternative to Kuanda. Chiluba was elected leader of the huge Zambian Congress of Trade Unions. Chiluba also enjoyed the distinction of having resisted Kuanda's attempts at co-option after spending a four-month stint in prison on political charges in 1981. Candidate Chiluba also had a political platform of bringing free market economic reforms to Zambia. Chiluba never denounced the IMF, a common and politically potent tactic in Africa. He also promised to privatize state industries. Indeed, his inauguration speech of November 2, 1991, was Reaganesque, as Chiluba told Zambians: "In this present crisis, government alone is not the solution to our problems. For too long, government was the problem."

After succeeding Kuanda, Chiluba tried to restore relations with the IMF and other international donors. He promised to dismantle all government monopolies, including building and insurance institutions. He also spoke of breaking apart and privatizing ZCCM, Zambia's state-owned and-controlled mining monopoly. Since then, dozens of state-run enterprise chief executives have been fired, including the head of ZCCM. And of major significance, Chiluba reduced state consumer subsidies for corn meal. Raising the price of corn meal, potentially difficult politically since Zambians have become accustomed to cheap corn meal, is an important sign that Chiluba is beginning to control Zambia's deficit spending.

The IMF and World Bank have been pleased with Chiluba's reforms. They and other Zambian donors will meet in Paris next month to consider whether to propose yet another IMF-monitored aid program for Zambia. As with past efforts to trade aid for reform, the donors will demand, among other reforms, that Zambia take steps to remove the state from the agricultural sector, further reduce subsidies on corn meal, and privatize some of ZCCM's operations.

OUTSTANDING CHALLENGES

A key to economic reform in Zambia is corn production and marketing. Corn is a staple food throughout much of Africa, including Zambia, where it is grown by more farmers than any other crop and accounts for nearly 75 percent of total marketed agricultural output. Zambian corn production was approximately 1 million tons in 1989-1990. Until Kaunda's 1990 reforms, the government monopolized all aspects of corn production and marketing through inefficient quasi-governmental agricultural cooperatives and the now defunct National Agricultural Marketing Board (NAMBOARD). Each year, Zambia loses about 30 percent of its harvest through mismanagement.

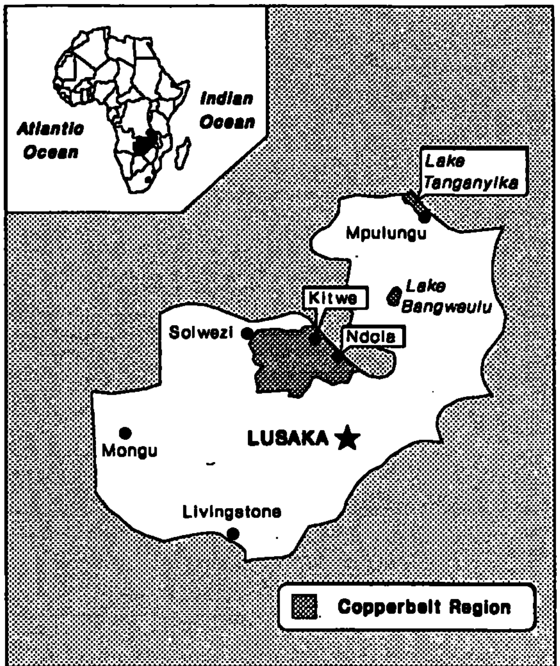
Another key to economic reform involves the government's longstanding policy of massively subsidizing corn meal prices for consumers. This consumer subsidy has cost the Zambian government about $400 million, or roughly 15 percent of its GDP over each of the past couple of years. The corn subsidy, moreover, is a double-edged sword. Not only does it cost the government to subsidize corn, but the government shortchanges the Zambian farmer, paying him a below market price for his corn. Thus, predictably, farmers grow less corn and plant groundnuts, tobacco, and other more profitable crops. Smuggling, also predictably, is common, with up to one-third of Zambian-produced corn illegally exported, principally to Zaire, where it fetches some three times the Zambian domestic price. And farmers now withhold corn from the market, waiting until the government raises its price, or until the black market price soars.[5]

The result this year may be severe shortages of corn. Many farmers, hurt by years of low prices, simply did not grow corn this year. Even having spent in advance its entire 1992 copper revenue to buy South African corn, Zambia faces severe corn shortages, having produced only half of its normal consumption. Zambia's abundance of fertile land makes this shortage all the more exasperating.

5 "Out of Maize," *The Economist*, October 5, 1991, p. 44.

The Distressed State of the Mining Industry

Zambia's mining industry is in sad shape. The main reason is the nationalization of the mining industry in 1970 and the takeover by ZCCM, Zambia's mineral monopoly, of freight, construction, and other unrelated industries, which drained it of operating capital. ZCCM also financially overextended itself by giving its workers expensive social services, such as schooling, health care, transportation, and housing. The results were waning investment, declining production, and a bloated bureaucracy.



Zambia's Copperbelt: With Ore Running Out, No Longer the Engine of Economic Growth

Even as mining production declined, ZCCM's work force rose from 60,000 in the early 1980s to 67,000 today. ZCCM also hurt itself with its "Zambianization" policy. Partly as political favors, Zambians were placed in ZCCM management jobs previously held by foreigners, mostly Europeans, sometimes with little regard for ability, training, or experience. As the number of ZCCM's European workers has fallen from 72,000 in 1964 to roughly 8,000 today, ZCCM now suffers from a serious shortage of technical, particularly geological, skills. Corruption in ZCCM, meanwhile, has been rife as well. It was reported over this past summer that ZCCM was being milked by top executives in a multi-million dollar copper scam dating back to the early 1980s.

Unless these drags on Zambian mining efficiency are minimized, the Zambian economy will be crippled by dramatically reduced levels of copper production. By the end of this decade, several of ZCCM's copper mines will have exhausted their known reserves. Zambian copper production could drop to less than half of its current level.

THE DIRE NEED FOR REFORM

Despite its dreary past, the Zambian economy shows some signs of hope. In 1987, the H.J. Heinz Company of Pittsburgh expressed a strong interest in acquiring major equity participation in Refined Oil Products, a major Zambian state enterprise. Zambian agriculture and livestock have demonstrated strong export potential to neighboring countries when Kaunda allowed the *kwacha* to be devalued in 1987. Similarly, a 1989 devaluation resulted in a 25 percent increase of non-mining exports. The devaluation of the *kwacha* makes Zambian exports more competitive as potential importers receive more *kwacha* for a constant amount of their nation's currency. And Zambian price decontrols in 1986 resulted in the greater availability to consumers of soap, cooking oil, and other basics that no longer were smuggled to neighboring countries.[6]

Still, sweeping and immediate free market reforms are necessary if Zambia is to begin growing economically. A gradualist or piecemeal approach to reforms, as tried off and on by Kaunda, is bound to fail. Privatization, for example, does not work well unless prices are free to reach market value.

Political Pressures. The political pressures on Chiluba also dictate that he move quickly on comprehensive reform. The slower he goes, the more time opposition groups, primarily those in Zambia's cities, will have to coalesce. A rejuvenated UNIP, Kaunda's old party, and other parties are mobilizing to oppose Chiluba's modest reforms.

The precipitous drop in Zambia's future copper production is another reason to move quickly on reform. Zambian copper mining revenues will decrease even in a best case scenario. This makes it essential for the Zambian economy to diversify, so that a strong agricultural sector replaces copper as the backbone of the Zambian economy. The sooner that additional free market reforms are brought to Zambian agriculture, the less damaging will be Zambia's declining copper revenues.

Zambia, most of all, must unleash the considerable but long-repressed entrepreneurial energies of its people. Chiluba must privatize Zambia's economy and eliminate price controls and excessive regulation burdening private enterprise, and otherwise relegate the government's role to that of facilitating a Zambian free market.

Greater Foreign Trade Is a Key to Reform

Foreign trade is critical to a country with a Zambian-sized internal market, with its minimal economies of scale and limited potential for domestic competition. Yet trade among southern African countries accounts for only 5 percent of these countries' total trade. Rather than trading with each other, southern African countries trade with the industrialized countries. In 1990, Zambian exports totaled approximately $395 million to Japan, $172 million to France, and $91 million to Italy. Most of these exports were copper. In contrast, $6 million worth of Zambian goods were sent to neighboring Zaire. This same year, Zambian imports totaled $166 million from Britain, $104 million from Germany, and $80 million from the U.S. Imports from Zaire, as reported by official statistics, were practically nonexistent. While this low level of trade among southern African countries is due in large part to these economies producing raw materials and cash crops in demand only by industrialized economies, there is no doubt that trade within the southern African region is artificially depressed by government trade restrictions affecting commerce in products, particularly food and consumer goods, for which there is a potentially vibrant regional market.

"Unofficial" Trade. Much of Zambia's trade problems stem from the political campaign against South Africa. At its formation in 1980, the Southern African Development Coordination Conference (SADCC), a political and economic association of ten southern African countries to which Zambia belongs, announced that its member states

6 Smuggling of subsidized consumer goods has resulted in chronic shortages of many essentials in Zambia.

would end their economic dependence upon South Africa.[7] In the early 1980s, some 64 percent of Zambia's imports and 20 percent of its exports passed through South Africa. The SADCC states attempted to improve their roads and railways to reduce their dependence on South Africa's transportation network. By 1987 Zambia claimed to have rerouted all of the copper exports that had previously passed through South Africa. That year too, Zambia began denying import licenses for items originating in South Africa. Although "unofficial" Zambian-South African trade continued, Zambia's attempts to distance itself from South Africa cost its economy several billion dollars in lost economic growth and higher transportation costs.[8]

While improvements in southern Africa regional trade may be slow in coming, Zambia can immediately and significantly improve its trade relations with South Africa. Chiluba, in fact, recognizes South Africa as a regional economic giant that must play a significant role if the much needed economic integration of the southern African region is to advance. Indeed, South Africa accounts for three-quarters of the region's total GDP. Chiluba announced last November 7 that Zambia would begin moving toward establishing official trade relations with South Africa.[9] South Africa's Gencor industrial conglomerate meanwhile is considering investing in Zambian mining. If this opening to South Africa continues, it would complement very well an internal policy of free market reform.

UP FROM POVERTY

America has an interest in the economic development of Zambia. Were Chiluba to bring free market economic prosperity to Zambia, Africa would have a sorely needed model of democratically-engineered, free market success. This model would bolster the still fragile consensus of support for free market economics among Africans, making the free market conversion of other African economies politically easier. Were free markets to spread through Africa, the result would be not only the potential growth of African markets for American goods and services, but a step toward getting Washington out of the international economic development business, which last year cost the U.S. well over $1 billion in grants and aid that has done little to stop the economic misery in much of Africa.

To assure that free market reforms take hold in Zambia, the Administration should:

- **Require AID to develop a plan for Zambia's transition to a free market economy.**

The U.S. Agency for International Development mission in Lusaka, Zambia's capital, should draft a comprehensive plan for the free market transition of the Zambian

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7 SADCC members are Angola, Botswana, Lesotho, Madagascar, Mozambique, Namibia, Swaziland, Tanzania, Zambia, and Zimbabwe.

8 *Africa News*, January 21, 1991, p. 11.

9 Trade statistics between South Africa and Zambia have been treated confidentially. According to South African sources, Zambia imported goods from South Africa worth approximately $180 million, and exported $2.2 million worth of goods to South Africa in 1991.

economy. This plan should assess and encompass the full range of the Zambian government's economic policies, including credit and monetary policy, taxation, government spending, regulation, wage and price controls, trade practices, foreign exchange allocation, and treatment of property rights. This plan would be useful to American officials dealing with the IMF's policy toward Zambia.

The U.S. Treasury official who advises the U.S. Executive Director to the IMF on how to bring America's significant voting power to bear on approving proposed IMF aid for reform packages is responsible for seven African countries in addition to Zambia. The U.S. Executive Director to the IMF meanwhile has only three staffers, each whom is responsible for devising America's IMF policy toward approximately 50 countries. As a result, U.S. officials at the IMF responsible for policy toward Zambia must rely primarily on the IMF's own advisory team in Zambia. The U.S. has little manpower and independently generated data with which it can critique and influence the agreement being negotiated between Zambia and the IMF, World Bank, and other donors.

Washington has been troubled by some previous IMF-monitored aid programs. The IMF, for instance, sometimes impedes the pace of privatization in developing countries. This was the charge leveled by Pakistani Finance Minister Sartaj Aziz at last October's IMF-World Bank meetings in Bangkok. Similarly, Czech and Slovak Federal Republic Minister Vaclav Klaus last October complained that IMF and World Bank advisors were promoting the very discredited statist policies that his country was trying to abandon.[10]

A well-researched AID program for Zambia's transition to a free market economy would enable the U.S. Executive Director to the IMF to exert maximum influence on the IMF and thus to minimize the chances of Zambia's economic reform being stunted by a less than comprehensive IMF program for Zambia's transition to a free market economy.

- **Instruct that AID's sound free market aid strategy toward Eastern Europe be adopted for Zambia and other African countries.**

AID is assisting directly the free market reform of the East European economies.

Example: AID contractors since last September have been assisting the sale of Poland's state-owned LOT Airlines. This work has included the appraisal of LOT's assets, the development of a privatization plan, and a search for potential investors.

Example: AID contractors, beginning last September, prepared the Czechoslovakian firm Pilzen Skoda for privatization. This work, which included reviewing past and current accounts and the implementation of proper financial systems, resulted in major segments of Pilzen Skoda being sold to private investors.

Example: AID contractors are preparing to assist Albania, Bulgaria, Estonia, and Romania reduce legal and procedural barriers to trade and investment and improve their contract law.

10 *Insight*, November 17, 1991, p. 15.

The economies of Africa and East Europe have much in common, including a limited window of opportunity for effective economic reform. Both Zambians and Poles, for instance, may have a limited tolerance for the pain that inevitably accompanies the comprehensive restructuring of statist economies. This has been demonstrated in Zambia, where 1986 riots over food prices derailed free market reforms. While Chiluba, unlike Kaunda, may be committed to a free market reform program, his time to act is limited. AID thus must do what it can to make Chiluba's privatization and other economic reform programs work.

Using its East European programs as models, AID could help overcome obstacles to privatization in Zambia. The Zambian legal and tax systems, for example, need to be reformed if privatization is to succeed. U.S. experts could work with Zambian officials to change Zambian laws that prohibit private enterprise and to lower or abolish and taxes that smother it. The Mines and Minerals Act, which regulates the Zambian mining sector, requires an overhaul to make private investing in Zambian mining more profitable. While World Bank staffers are aiding Zambia in privatization and trade reform, Zambia could use U.S. technical assistance with the complexities of tariffs, financial transfers, and taxation policies. And U.S. financial experts could help Zambia establish a stock exchange, which could be used to help sell state-owned enterprises to private investors.

Restructuring AID's policy toward Zambia along the lines of AID programs in Eastern Europe would require no more than AID's present expenditures on Zambia. AID last year spent approximately $20 million in Zambia. AID spending this year in Zambia could be considerably higher, in the $30 million range. Current AID programs include $10 million to pay off Zambia's IMF debt and to assist Zambia with its balance of payments deficit. Approximately $2 million is to prevent the spread of AIDS and $1 million to manage wildlife preservation programs. An agricultural assistance program costs approximately $10 million per year. While this agricultural program does assist private sector enterprises, the money would be better spent on transforming Zambia's economy fundamentally and rapidly by attacking the government's ownership and regulatory grip over it.

- **Mandate that AID use the Index of Economic Freedom to gauge future aid levels to Zambia.**

AID should make aid to Zambia contingent on progress toward free market reform. AID should examine Zambia's policies on credit, taxes, government spending, regulation, wage and price controls, free trade, protection of private property rights, and foreign exchange controls. Taken together, these economic indicators could become a prototype for an Index of Economic Freedom, a quantitative gauge of a country's progress in developing a market economy. As a pilot project for all Africa, the Index for Zambia later could be refined by AID and applied to all African countries receiving aid from the U.S. Such an Index, in fact, already has received considerable attention in Congress and at AID.

The Index of Economic Freedom for Zambia would score Zambia's progress toward economic reform, measuring, for example, the amount of the government's corn meal subsidy, involvement in mining, and interference with foreign trade. If Zambia makes progress removing its corn meal subsidies, its Index score, to be determined yearly, would increase, leading AID to favor Zambia in future foreign aid allocations. If, on the contrary, it scores poorly on this or other aspects of reform, Zambia's Index score would be lower and Zambia would have its U.S. aid reduced or even eliminated. A low Index score by Zambia could prompt Washington to reduce U.S. support for IMF or World Bank assistance; a high-score could prompt greater U.S. support.

Common Standard. The long-pending 1992 Foreign Aid Authorization bill, if enacted by Congress, would require AID to develop a series of factors that provide a common standard for evaluating and comparing recipient countries' progress in adopting economic policies that foster individual economic freedom. The Index of Economic Freedom, cited in this bill's report, should be used by AID in developing this series of factors to make this much-needed evaluation and comparison.

AID already has experience with a version of an Index of Economic Freedom. In a 1989 report entitled *Development and the National Interest: U.S. Development Assistance into the 21st Century*, AID economists developed a policy matrix comparing the economic policies of 42 developing countries. This comparative matrix, called an Economic Opportunity Index, allowed AID to demonstrate that free markets produce higher rates of economic growth. Singapore, for example, with its years of booming economic growth, scored in the 90s (on a scale of 100) on AID's Economic Opportunity Index; developing countries suffering from economic decline, like Congo, Guinea, and Mali, typically scored in the 20s. AID's experience with its Economic Opportunity Index confirms that an Index of Economic Freedom, which measures essentially the same factors, is feasible and that free market economies maximize economic growth.

It is AID policy to give priority to developing countries that are promoting free market reform. Had it further developed and refined the Economic Opportunity Index, AID today would have a superior means of allocating resources among those countries receiving American development assistance. AID's history of providing development assistance to countries unwilling or unable to bring about the required free market economic reforms demonstrates that it needs the discipline of an Index of Economic Freedom. This discipline is owed to the American taxpayer. It also would be good for Africans; the longer free market reforms are delayed by poorly designed foreign aid, the more painful will be the establishment of a free market.

- **Send Peace Corps volunteers, if invited by Zambia, to promote the formation of small businesses.**

Of the approximately 1,400 Peace Corps volunteers in Africa, some 140 are part of the Peace Corps' Small Business Program, which consists of volunteers experienced in accounting, purchasing, quality control, business management, financial analysis, and other areas helpful in developing small businesses. In the west African nation of Mali, for example, Small Business Program volunteers work through the local Chamber of Commerce to organize and teach accounting and marketing courses for small business owners.

While the Small Business Program in Africa makes much sense, the Peace Corps so far has been far too timid in promoting free markets in Africa. In Poland, by contrast, the Peace Corps Small Business Project gives municipal governments privatization expertise. The Peace Corps' Small Business Program should do the same for Zambia and other African countries.

If the Peace Corps is invited into Zambia, and the Chiluba government has demonstrated a commitment to foster private sector activity, then the Peace Corps should bring small business expertise to Zambia. The Peace Corps could provide would-be Zambian entrepreneurs with basic business skills. Peace Corps volunteers also could help privatize Zambian state enterprises, much as they have done in Poland.

- **Stop undermining South Africa's economy, to which Zambia's economy is linked.**

An economically strong South Africa is crucial to the economic development of Zambia and the entire southern Africa region. Chiluba has recognized South Africa's importance by beginning to reverse Zambia's economically damaging policy of restraining Zambian-South African trade. Chiluba's action will benefit the Zambian economy. Moreover, further economic warfare by Zambia and others against Pretoria only will create the economic and political turmoil that could slow South Africa's already precarious transition toward majority rule.

Yet, Washington contributes to this turmoil by keeping economic sanctions against South Africa.[11] The 1983 "Gramm Amendment" to U.S. Public Law 98-181, named after then Representative Phil Gramm of Texas, requires the President to instruct the U.S. Executive Director to the IMF to oppose South Africa's request for IMF credits. Such American opposition is influential, if not decisive, in denying South Africa credit.

Ironically, all the apartheid-related conditions enumerated by U.S. Public Law 98-181 for South Africa regaining access to IMF credit have been or are close to being met. These include a determination by the U.S. Secretary of the Treasury that IMF credit to South Africa, among other effects, would reduce substantially racially-based restrictions on labor and mobility, and would benefit economically the majority of South Africans. The remaining stipulation is that South Africa run a balance of payments deficit.

As a country with what is a developing economy by many standards, including a 40 percent unemployment rate, South Africa would like to stimulate economic growth by raising imports and consequently running a balance of payment deficit in the short to medium term. Access to IMF credit would reduce the cost of financing these deficits. Without South African access to IMF credit, commercial lenders rate South African loans as higher risks, thus increasing South Africa's cost of borrowing international capital. This is an additional and unneeded burden on any economy.

A healthy, trade-oriented South African economy would do more to promote Zambia's economic development than would any amount of foreign aid. Washington should recognize this and stop hurting Zambia's economy indirectly for the sake of what anyway is an obsolete South Africa policy. South Africa should be given diplomatic assurances of American support for reinstituting its access to IMF credit should it run a balance of payments deficit. It is foolish to assist Zambia with one hand and hurt it with the other while contributing to South African destabilization in the process.

11 Additionally, over 100 state and municipal governments have sanctions against South Africa.

CONCLUSION

Zambia's new president, Frederick Chiluba, offers new hope for Zambia—and Africa. Were Chiluba to bring free market economic prosperity to Zambia, Africa would have a compelling model of democratically-engineered, free market development success.

Though Zambia's deep economic wounds are primarily self-inflicted, America has a role to play in assisting Zambia and other African countries grow economically and raise living standards by developing free market economies. An Index of Economic Freedom, used in conjunction with IMF economic reform programs, would provide long-needed means of gauging this commitment to a free market economy. Not only would an Index help to assure that American development assistance dollars are wisely spent, it would prod African countries toward the free market.

Zambia's movement toward a free market will begin yet again as a new IMF-monitored structural adjustment program is developed for Zambia over the next couple of months. In the process, Washington should exert maximum leverage to assure that this reform program brings Zambia to a free market in a comprehensive and rapid fashion. An AID-drafted plan for the free market transition of the Zambian economy would be a weapon to combat any less than comprehensive IMF programs for this transition.

Economic Revival. East European-style AID and Peace Corps programs aimed at directly transforming the Zambian economy, including assistance with free market banking and tax reforms, would be appropriate for Zambia. Lastly, America's abandonment of its opposition to South Africa regaining access to IMF credit would assist Zambia by contributing to the revival of the important South African economy.

The free market revolutions underway in the former Soviet Union and Eastern Europe have forced the U.S. to redesign its aid policies toward these regions. The same should happen for Africa. Decades of foreign aid from America and elsewhere, no matter how well-intended, have done little to eliminate poverty in Africa. Now that free markets are struggling to be born there, America can help by restructuring its aid programs to give Africans the same economic freedoms as are being won by Russians and East Europeans.

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