Executive Summary

Zambia is one of the dynamic growth poles of Southern Africa, thanks to important progress in recent years in strengthening its policy framework for investment. The economy is landlocked but is strategically land-linked to eight neighbors in the middle of Southern Africa and has significant development potential and good economic prospects.

Zambia boasted a real Gross Domestic Product (GDP) of 5.9% per annum between 2004 and 2010, exports expanded ten-fold and FDI increased eight-fold, reaching USD 1.3 billion in 2007 and hit a record USD 2.4 billion in the first half of 2010. The economy has been relatively resilient in the recent global downturn, benefiting from stable macro-economic policies, good harvests and buoyant demand for copper, especially from emerging markets. Zambia's economy continued to grow in 2010 with real GDP of 7.6%. While extractive industries still attract the bulk of investment, the services sector, especially banking and tourism, and agriculture, have also catalyzed significant volumes of FDI.

Breaking away from the centrally planned economy, Zambia began to liberalise its trade regime in the early nineties, and embarked on a privatization programme in 1992. Zambia, today, is recognised as one of the most open African economies to foreign equity ownership. An ambitious reform agenda was launched in 2004 under the Private Sector Development Reform Programme (PSDRP) to improve the investment climate and boost the private sector's contribution to economic growth. Moreover, the government has articulated the country's long term development objectives in the Sixth National Development Plan (SNDP) and the National Long Term Vision 2030.

The government of Zambia has undertaken with the OECD an *Investment Policy Review* based on the OECD Policy Framework for Investment. The *Review* makes the following main recommendations for further progress in mobilizing investment for the development.

Develop a harmonised national investment policy

Several growth drivers are cyclical: commodity prices and harvests can decline. A key challenge is to sustain the high levels of foreign investment, spur more domestic investment and enhance economic diversification. Weaknesses in the regulatory framework remain apparent. The investment code of 1994 was amended on numerous occasions and finally incorporated into the Zambia Development Agency Act of 2006. While this has contributed to simplifying the legislative framework for investment by unifying different sets of laws and regulations governing investment and business, it causes confusion over what is the primary piece of legislation for investment, especially when other pieces of legislation still include investment-relevant provisions. While Zambia is a signatory to a range of bilateral and other international treaties that govern international investment, it lacks a harmonised legislation for investment, including provisions on national treatment. Improving investment policy co-ordination should thus be treated as a priority.

Take better advantage of the investment promotion and facilitation options available

In terms of investment promotion and facilitation, the mandate of the Zambia Development Agency (ZDA) is comprehensive in addressing private sector development needs but remains broad. The current ZDA Act and its numerous provisions affect the ZDA's capacity to promote and facilitate investment in a focused manner. If the ZDA is to undertake effective investment promotion, it needs to be given a more streamlined mandate and independent Charter. Revising the ZDA Act to that end should provide the grounds for a more focused and gradually a more autonomous agency. This would imply aligning its mandate to an investment policy, which is currently lacking.

Undertake a cost-benefit analysis with regards to fiscal incentives

Tax incentives have been used by the government as a tool for promoting investment, especially in mining, Zambia's most important export sector. Focussing on a predictable and fair tax system should be the primary objective of the government. In addition to their uncertain effectiveness, particularly in the resource sector, such incentives are costly to administer and invite corrupt practices in tax administration. The government should undertake a cost-benefit analysis of its fiscal incentives, in particular for investment in the mining sector. Also, the process of registering with the ZDA to obtain incentives for investment in certain priority sectors can be a lengthy bureaucratic process, thus costly for both the administration and the investor. Therefore, rationalising the complex incentive scheme would help the government reach the right balance between domestic resource mobilisation and providing an investor-friendly tax regime.

Improve the consultative mechanisms for policy development

The government of Zambia attaches high priority to undertaking consultation throughout the policy development process, a mechanism that is applied in both trade policy through the sector advisory groups (SAGs), and in investment climate reform through the Private Sector Development Reform Programme (PSDRP). The SAGs and the PSDRP Steering Committee and Working Groups are established with fair representation of different stakeholders, which includes the private sector, yet the irregularity and lack of coherent agendas for their meetings have undermined their effectiveness.

Strengthen the framework for PPPs

The government has put in place legal and institutional frameworks for Public Private Partnerships (PPPs) to address large scale infrastructure development that is beyond financing capacities of the Treasury. Through the PPPs, the government aims to address energy deficits by facilitating private investment in new hydropower generation plants and in the rehabilitation and expansion of major road networks. These initiatives are important for stimulating increased investment in economic activities and facilitating international trade. The initiative to promote PPPs should be further strengthened by increasing the transparency and disclosure of the bidding process. Also, the institutional framework needs to be revised in order to improve the management and implementation capacity of the PPP unit.

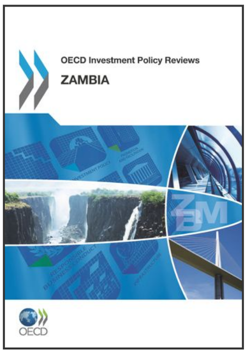
Strengthen the oversight and enforcement mechanisms of the regulatory framework

Improving policy oversight and enforcement is a cross-cutting challenge for Zambia's government. This is valid for issues linked to taxation, competition as well as corporate governance and responsible business conduct. Zambia was one of the first countries in the region to establish a competition authority, and continues to be a regional leader in this area, having recently enacted legislation to incorporate consumer protection, the Competition and Consumer Protection Act. The Competition and Consumer Protection Commission (CCPC) requires financial and technical resources to effectively implement its enhanced and expanded mandate. It would also benefit from a clear demarcation between laws that regard its oversight over different sectoral regulators and jurisdictions. While the CCPC seeks to become more of a promoter of good competition practices, its basic functions should not be neglected.

Develop mechanisms to channel industry demands to human resource development agendas

Zambia has taken big steps towards meeting its education objectives and the MDG 2 (Achieving universal primary education), reaching close to full primary school enrolment. However, Zambia faces challenges in training skilled personnel that can meet the needs of industry especially in technical functions. This is particularly evident in science education, which can provide a strong platform for technical training. As a result, there is a general shortage of technical skills. A major challenge in this regard is the identification of industry demands and catering to these needs via curriculum development. This weakness has in part contributed to a situation where strategic business linkages between foreign investors with high production and service standards, and local suppliers, are few.

The government is well positioned to follow through on the above challenges in order to fully realize its potential for attracting and benefiting from investment and reaching its socio-economic objectives. Through analyzing different policy dimensions affecting the investment climate, this *Investment Policy Review* has highlighted progress achieved, while identifying remaining bottlenecks to be tackled. The main reforms the government of Zambia is considering as a result of this assessment include the development of a harmonized investment policy, as well as the review of its tax incentives system and its framework for PPPs. Addressing these as well as the other issues highlighted in the review would further contribute to improving Zambia's policy framework for investment.



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