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PART A

Part. A.

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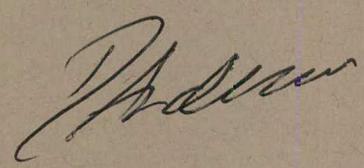
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Chancellor's (Lawson) Papers:  
Meeting with the Minister For Overseas  
Development and the Zambian Prime Minister  
September 1987 .

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YOUR TELNO 254

## VISIT OF PRIME MINISTER MUSOKOTWANE

## SUMMARY

1. THE ECONOMIC ARGUMENTS ARE UNCHANGED. MUSOKOTWANE HIMSELF IS A LOYAL BUT UNCONVINCED DEFENDER OF ZAMBIA'S ECONOMIC PLAN. NOTHING YET TO REPORT OF IBRD'S CURRENT DISCUSSIONS WITH ZAMBAIANS. OTHER DONORS SHARE OUR RESERVATIONS.

## DETAIL

2. THE WORLD BANK TEAM UNDER GEBHETRT DO NOT BEGIN SUBSTANTIVE DISCUSSIONS UNTIL NEXT WEEK, AND THERE WILL BE NOTHING SIGNIFICANT TO REPORT BY 7 SEPTEMBER, WHEN MUSOKOTWANE SEES YOU AND OTHER MINISTERS.

3. MUSOKOTWANE HIMSELF HE IS A LOYAL, HARD-WORKING, BUT UNCONVINCED DEFENCE COUNSEL, WHO FOUND HIMSELF OVERRULED AT THE POLICY-MAKING STAGE AND HAS SUBSEQUENTLY BEEN PUT UP-FRONT TO LOBBY DONORS AS THE ACCEPTABLE FACE OF ZAMBIAN ECONOMIC PLANNING. HE DESERVEDLY WON GOOD MARKS FOR HIS PRESENTATION OF ZAMBIA'S CASE ON THE PREVIOUS JUNE TOUR. THE RISK REMAINS THAT THOSE WHO BELIEVE IN THE NERP WILL PUT THE BLAME ON MUSOKOTWANE WHEN HE RETURNS WITH LITTLE OR NOTHING. THEY KNOW HIM AS AN OPPONENT OF THEIR POLICIES AND MAY TRY TO EASE HIM FORM OFFICE BY BLAMING HIS PRESENTATION RATHER THAN THEIR OWN INADEQUACIES FOR DONOR RELUCTANCE. MUSOKOTWANE IS CERTAINLY NOT IN THE TOPE RANK OF ECONOMISTS BUT HE IS AN HONEST TRIER AND IN PRIVATE HE ARGUES AGAINST CURRENT FOLLIES. I SHALL THEREFORE WISH TO PUT IT AROUND THAT WE FOUND HIM PERSONALLY MOST IMPRESSIVE BUT THAT HTE PLAN ITSELF WAS NOT CONVINCING. IF THIS LINE COULD BE REINFORCED AT THE HIGHEST LEVEL IT WOULD BE USEFUL. A PRE-CHOGM MESSAGE TO KAUNDA FROM THE PRIME MINISTER WILL BE UNDER CONSIDERATION

IN THE FIRST HALF OF SEPTEMBER (PRENDERGAST'S LETTER HD 2 ABG OF 5 AUGUST AND MY TELNO 270 REFER) AND A PARAGRAPH COULD BE TACKED ON THERE.

4. THE TALKS. IN RECENT CORRESPONDENCE AND PARTICULARLY IN MY TELNO 254 I SET DOWN THE SHORTCOMINGS THAT I FOUND IN THE NERP, AND THE RELEVANT DEPARTMENTS HAVE NOW HAD THEIR OWN OPPORTUNITY TO STUDY THE FULL REPORT. I HAVE NOTHING OF SUBSTANCE TO ADD. A USEFUL STARTING POINT, AND A WAY OF GAINING THE MORAL HIGH GROUND, WOULD BE THE DISCUSSIONS BETWEEN MUSOKOTWANE AND MR PATTEN OF LAST MARCH, AND THE SUBSEQUENT PRESS STATEMENT GOVERNING THE TERMS OF THE ADDITIONAL BALANCE OF PAYMENTS AID WE THEN OFFERED. AT THAT TIME MUSOKOTWANE WAS WORKING FOR AGREEMENT WITH THE IMF, AND WAS ABLE TO ASSOCIATE HIMSELF SINCERELY AND PUBLICLY WITH OUR THINKING, WHICH HE HAS NOT BEEN ABLE TO DO AFTER 1 MAY. SINCE I THINK IT POSSIBLE THAT THE AUTHORS OF THE PLAN ARE CLAIMING FOR IT A MEASURE OF DONOR SUPPORT, AND MAY BE HAVING SOME SUCCESS IN SO PERSUADING KAUNDA, IT WOULD BE SALUTARY IF MUSOKOTWANE COULD BE TOLD (AND BETTER STILL GIVEN A WRITTEN PAPER TO TAKE HOME) OUR UNDERSTANDING OF OTHER DONORS' ATTITUDES. IT WOULD ALSO BE USEFUL TO SPELL OUT IN TERMS WHAT WE AND THOSE OTHER DONORS WOULD DO IN THE EVENT THAT ZAMBIA RETURNS TO AN IFI-TYPE APPROVED ECONOMIC PROGRAMME.

5. OTHER DONOR. OUR READING OF THE SITUATION, BASED ON A RECENT INFORMAL DONORS' MEETING, IS THAT US, FRG, DUTCH, WORLD BANK AND NOW THE SWEDES ARE ADOPTING A HARD LINE, THOUGH WHETHER THEY HAVE MADE THEIR RESERVATIONS PLAIN IS NOT KNOWN. PRESENT SWEDISH AID AGREEMENT EXPIRES NEXT MONTH. ELSTROM, DEPUTY DIRECTOR, SIDA, WHO IS VISITING, SAID ON 2 SEPTEMBER THAT WHILE SOME FUNDS ALLOCATED FOR AUCTION UNDER PRESENT AGREEMENT HAD BEEN RELEASED FOR DISBURSEMENT BY FEMAC, IT WAS UNLIKELY THAT BALANCE OF PAYMENTS SUPPORT WOULD BE MADE AVAILABLE ON THOSE TERMS UNDER A NEW AGREEMENT, IF INDEED AT ALL.

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2213/023

FROM: J C MAY

DATE: 4 September 1987

1. MR DAVIS  
2. CHANCELLOR

cc PS/Chief Secretary  
PS/Economic Secretary  
Sir P Middleton  
Sir G Littler  
Mr Lavelle  
Mr H Evans  
Mr Mountfield  
Mr Batt  
Ms Rogan FCO  
Mr Brownlee ODA

**MEETING WITH ZAMBIAN PRIME MINISTER**

You have agreed to meet the Zambian Prime Minister, Mr Musokatwane on Monday 7 September at 11.00 am. Mr Musokatwane is likely to be accompanied by the High Commissioner, Mr Phiri and two aides. Mr Davis and I will support.

2. Mr Musokatwane is in Europe to discuss his country's New Economic Recovery Programme, and to look for new offers of aid, following the recent break with the IMF and the abandonment of the old economic recovery programme. He has a breakfast meeting with the Foreign Secretary on 7 September and appointments later in the day to meet Mrs Chalker and Mr Patten, where discussion is likely to focus on the Zambian economy, aid, South Africa, the Commonwealth Heads of Government Meeting and the Iran/Iraq War, (since Mr Musokatwane has just come from Iraq). We will let you know of any points of interest raised at the breakfast meeting.

3. With its heavy dependence on copper exports for foreign exchange earnings, high public expenditure policies, growing balance of payments deficits and debt, Zambia faces severe problems. Current policies aim for growth through independence, and, in the short run, the recent rise in raw material prices and the restriction on debt service payments may make such an approach appear manageable. This is unlikely to be the case in the longer term.

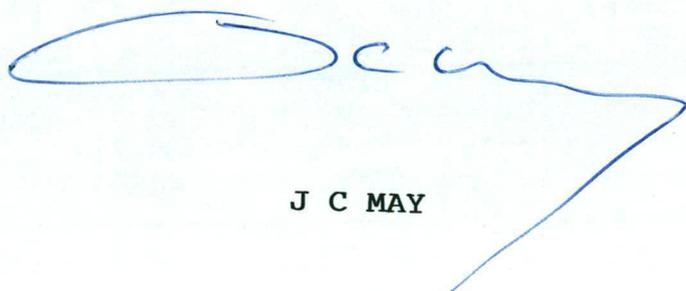
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4. Zambia formally broke relations with the IMF on 1 May this year and has been placed on a non-accrual basis by the IBRD. These developments have ended (for the time being at least) a decade of intermittent co-operation with the IFIs and indeed a notable degree of success in the adjustment process in 1985-86; under an IMF programme a foreign exchange auction had been set up (now abandoned in favour of an over valued fixed rate) and budgetary and trade reforms had been implemented. The New Economic Recovery Programme depends on assumed generous levels of donor assistance, and while much in the plan appears sensible, it is marred by an over expansionary and optimistic macro-economic framework.

5. Mr Musokatwane was personally in favour of agreeing to the IMF's terms in the recent negotiations and is likely to be sympathetic to the views you put forward. The difficulty will lie in his ability to persuade his colleagues at home to resume negotiations with the IMF and put sound economic policies into effect. You should know that Sir James Callaghan met privately with President Kaunda in August to urge renewed contact with the international financial institutions to provide a fallback should the new economic plan fail.

6. The main aim of the meeting should be to question Zambia's ability to go-it-alone via the new plan and to press for an agreement with the IMF, stressing the advantages - in terms of debt rescheduling and aid - which would flow from such an agreement.

7. I attach a supporting brief for the meeting, consisting of the objectives and line to take, with additional background information on the economy, relations with the IMF, the new economic programme, aid, and a biographical note.



J C MAY

STEERING  
BRIEF

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ZAMBIA - Meeting <sup>with</sup> ~~by~~ Mr Musokotwane, Prime Minister

### STEERING BRIEF

#### OBJECTIVE

1. To express serious reservations about likely success of Zambia's economic plans.
2. To encourage Zambians to mend their fences with the IMF and put sound economic policies into effect.

#### Line to Take

1. Aware of economic problems of many sub Saharan African countries. Clearly need special help, hence your initiative to give direct debt relief, and Camdessus's proposal to more than double very concessional Structural Adjustment Facility. But Funds scarce - right that these schemes should benefit only those countries following sound economic policies. Zambia likely beneficiary if they can reach agreement with IMF.

2. Zambia's economic situation very serious. Recognise social, political problems it presents. Welcome many aims of New Economic Recovery Programme eg, private sector exports/imports substitution, promotion of agriculture, rehabilitation of infrastructure. But have some doubts about how they will be achieved; eg:

- How can export-led growth be achieved if overvalued exchange rate maintained, tight foreign exchange controls applied?
- Are Government resources sufficiently secure to achieve aims without increasing inflation and eroding confidence?
- What incentive for increasing maize production if negligible increase in price paid to farmers?

3. Understand concern not to let value of Kwacha fall too far. But seems clear that kwacha currently overvalued. Some controlled depreciation crucial to any viable programme, and to provide incentives for producers. Believe budget deficit was main cause of inflation, not discontinued auction.

4. Equally important not to let value collapse - but this would not happen if foreign exchange available, which could be ensured by appropriate monetary and fiscal policies plus aid.

5. Convinced of need for Zambia to work out sound economic programme with IFIs: see no other solution to Zambia's problems. Glad President Kaunda has sent copy of Programme to Camdessus. Know IFIs will study carefully.

6. Only IFI-backed economic programme will give donors sufficient confidence to provide and maintain substantial aid flows. Even with recent copper price rise, we believe Zambia will still need exceptional assistance from IFIs and bilateral donors for foreseeable future.

7. If agreement with IFIs could be reached concessional funds would be released. UK ready to provide balance of payments support once agreement reached with IMF. Would also permit rescheduling through Paris and London Clubs.

8. IMF fully aware of social and political aspects of adjustment programmes. Camdessus made point strongly in speech at UNCTAD. Recognises that programme taking these into account more likely to succeed. IMF cannot force unacceptable policies on Zambia - main concern to get figures to balance and to restore growth.

9. Important to work something out with IMF before end September, or else risk of ineligibility.

2213/025

*Overvalued  
Balance of  
Payments  
XR  
PX  
IS*

**BACKGROUND**

**a) THE ECONOMY**

1. The economy is almost totally dependent on copper which accounts for roughly 50% of GDP and 90% of export earnings. Earnings from this source have been declining since 1974 although prices have picked up recently. The problem has been aggravated by Zambia's high level of indebtedness, much of it to the International Financial Institutions (IFIs) and therefore not open to rescheduling. Latest World Bank figures put Zambia's GNP at only \$300 per head.

2. The country suffers from recurrent drought - which is fairly severe in some areas at present - and the past neglect of its agricultural resources, although more recently they have been seeking to expand agricultural output with some success. Controls on imports have led to consequent underutilization of capacity in many areas of industry. The country also faces transport difficulties, in part associated with civil wars in neighbouring Angola and Mozambique, in part due to the deterioration of infrastructure caused by inadequate maintenance. In addition, the authorities have failed to reverse the high public expenditure policies which sprung from their early wealth based on high copper prices.

3. The Zambians have been slow to recognise the deep-seated nature of their economic crisis, and following extensive borrowing in 1970s and earlier 1980s total external debt is around \$5 billion. Debt service payments for 1987 estimated by IMF at SDR 800 million, ie 10-20% more than probable export earnings. About 40% of debt service payments is due to international financial institutions. Zambia has thrice been to Paris Club for official bilateral debt rescheduling; each time they have fallen into arrears on moratorium payments. They are now in arrears to IMF and the World Bank has suspended disbursements since May because of arrears. In the past Zambia was able to raise bridging loans to pay off IMF arrears, but they are now too large for that treatment.

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4. While seeking to expand agricultural production and reduce the role of public sector, Zambia has never been whole-hearted in following the economic and financial prescriptions of the IMF and World Bank. The IMF programme launched in early 1986 soon went off track due to inadequate fiscal and monetary control allied to a further decline in copper prices. The currency depreciated heavily at auction, despite rigging. The auction was suspended in January 1987 and finally abandoned by virtue of a decision taken in Lusaka in May when Mr Musokotwane and colleagues were in Washington and seemed to be on the verge of re-establishing IMF programme.

5. Tensions exist within the Government between the pro IMF and anti-IMF elements, the latter led by Dr Chivuno, the Governor of the Central Bank. The anti-IMF elements appear to have increased their influence over President Kaunda following maize meal riots in Copperbelt in December 1986, caused by partial removal of maize subsidy as part of the IMF programme. More recently, there have been demonstrations in Lusaka against proposed fuel price increases and the introduction of education fees.

**b) RELATIONS WITH IMF**

6. Zambia finally broke off relations with the IMF on 1 May, following a long period of negotiations over the terms for a new borrowing arrangement. Zambia's arrears to the IMF total over SDR 260 million (and its scheduled repayments to end 1990 total a further SDR 510 million). On 22 May, the IMF board agreed that Zambia should be declared ineligible to receive further IMF support at the end of July without further review, unless there were clear signs in the meantime that the authorities were willing to re-open a meaningful dialogue with the Fund. At the end of July the decision was further delayed until the end of September, to give Zambia further time. The UK objected to the manner in which this decision was put before the Board without notice, and therefore could not support delay. However, given that our vote would have otherwise tipped the balance against Zambia we abstained from the vote.

## c) NEW ECONOMIC RECOVERY PROGRAMME

7. The Plan, also known as the Interim National Development Plan for July 1987 to December 1988, was announced by President Kaunda on 18 August. It comprises a statement of policies and priorities, elements of a macro-economic framework and capital expenditure budgets covering governmental and parastatal investment outlays. It is prefaced by an unnecessarily negative assessment of the results of economic liberalisation and the foreign exchange auction in 1985 and 1986.

8. The theme is "growth from our own resources"; key policies outlined in the plan are:

- a debt service ceiling of 10% of export revenues, implying no debt repayments will be made and defaults on interest payments
- despite this, high levels of donor assistance
- over valued fixed exchange rate
- low increases in the price of maize, a disincentive to increased production
- doubling in subsidies
- controls on imports
- some sensible, but over ambitious, sectoral policies - eg promotion of tourism, agriculture, rehabilitation of infrastructure, export promotion, concentration on profitable copper mines.

9. The plan aims for just over 2% growth which is likely to be achieved. The budget figures include major problem areas, however, with no control over wages, increased subsidies, reduced public sector investment, and over optimistic assumptions on revenues. The forecast deficit is for 10% of GDP but is likely to be nearer 30%. Deficit

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financing is largely monetary and price instability is unlikely to be achieved.

10. In the light of Zambia's poor record of economic management and the many contradictions within the plan's policies, many of its objectives, including encouraging private investment, are unlikely to be achieved, particularly with an overvalued exchange rate. The limit on debt repayment and the balance of payments bonus this brings, and the higher price of copper may allow Zambia to survive in the short term however.

d) AID

11. In the past, Zambia had been a major recipient of aid. Currently this is restricted to technical co-operation and project aid. At the Paris Clubs donors' meeting in December, the UK pledged £30m in support subject to agreement with the IMF. The main support from existing aid is for rural development. The Integrated Rural Development Project, started in 1980, has been a considerable success, and a second phase is now in operation.

12. In April, UK agreed - exceptionally - to provide £8m in balance of payment support, as agreement with the IMF appeared close. This was withdrawn after Zambia broke off relations with the IMF in May. It was made clear at the time that the UK would provide a significant volume of balance of payments support if Zambia returned to the IMF, and would continue with our substantial programme of technical cooperation and project aid. That remains the position.

13. The majority of other donors seem to have adopted a similar approach to the UK. The World Bank, USA and Germany have withdrawn balance of payments support via the foreign exchange auction. World Bank project aid is also suspended due to arrears. French also consider restoration of IMF programme a precondition for aid. By breaking with IMF Zambians have foregone some \$234m of balance of payments support, though they have also left themselves free to limit their debt payments and conserve foreign exchange accordingly.

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14. Retrospective Terms Adjustment (RTA) was last considered in February, when it was agreed such an offer would be inappropriate in absence of an IMF adjustment programme. Amount involved is some £63m (ie repayments of capital and interest on past aid loans to Zambia from HMG; our present aid is all on grant terms). Zambia is one of only two countries covered by your initiative where we have yet to offer RTA.

## MUSOKATWANE, KEBBY SILLO

Prime Minister since April 1985. MP for Katombora.

Born 1947 of chiefly family, near Livingstone. Toka. Educated Monze and Certificate of Education at UNZA. A headmaster and taught at Chipata Teacher Training College. December 1973 elected MP for Katombora. 1977 Minister for Water and Natural Resources. December 1978 re-elected as MP for Katombora. January 1979 Minister for Youth and Sport Resources. December 1979 Minister of Finance. January 1983 Minister for Youth and Sport. November 1983 Minister of General Education and Culture. January 1987-1 May 1987 assumed additional responsibility for Ministry of Finance.

One of the younger generation generally moderate in his views and takes his Ministerial duties seriously. When he was Minister for Natural Resources, an ivory trader tried to bribe him but was immediately reported to the police and was charged with corruption.

At Education he was brisk and businesslike. As Prime Minister he has continued to display energy and commitment and great loyalty to Kaunda. In January 1987 he took over Finance (on Kabwe's (qv) dismissal) two days before the budget and handled the negotiations with the IMF in April-May before handing back the Finance portfolio (to Chigaga (qv), May 1987). Was personally in favour of agreeing to the IMF's terms, but found himself overruled on his return from Washington and loyally acted as Defence Counsel.

Commonsensical, if no great intellect. Hardworking and friendly. Apparently very religious. Wife, Reginah, a keen Girl Guide. Farms some cows c/o Haggis Evans.



*mpf*

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COPIES TO	SIR P. MIDDLETON SIR G. LITTLE MR LAVELLE MR HOEVANS MR D. G. DAVIS MR MOUNTFIELD MR SATT MR MAY.

*From the Private Secretary*

7 September, 1987.

*Dear Lynn,*

**PRIME MINISTER'S MEETING WITH THE PRIME MINISTER OF ZAMBIA**

The Prime Minister had a talk this evening with the Prime Minister of Zambia. Mr. Musokatwane was accompanied by the High Commissioner for Zambia.

Zambian Economy

Mr. Musokatwane handed over a message to the Prime Minister from President Kaunda about Zambia's New Economic Recovery Programme, together with supporting material. I enclose a copy of the message, to which Mr. Musokatwane spoke very closely. He claimed that the Zambian people understood the need for bold and painful measures, for which the government had prepared them. He stressed the intention to diversify away from copper, and develop non-traditional exports. Zambia's differences with the IMF did not relate to objectives but to methods and to speed of implementation. There were specific disagreements over the exchange rate and subsidies. While ready to take harsh measures, the Zambian government could not agree to increase the price of mealie meal by 100%. Even a 15% increase earlier had caused riots. He thought that some progress had been made towards convincing the IMF that some of their original prescriptions had been too severe. They had admitted in retrospect that the foreign exchange auction system could not have worked.

Mr. Musokatwane continued that Zambia hoped that the United Kingdom and its other friends would play a part in supporting the recovery programme. Additional aid was needed in the critical period between now and the end of 1988. This might include help to increase the production capacity of British firms in Zambia (presumably a coded reference to balance of payments support), commodity aid and emergency aid. Particular help was needed to cope with the effects of drought, for instance by building small dams and drilling boreholes. It might be useful to have a meeting next year of Zambia's main donors and creditors to discuss the best way forward.

The Prime Minister said that she would look carefully at President Kaunda's letter. It was clear that Zambia faced a very difficult situation. In such circumstances, it was often better to opt for a quick and painful adjustment than to draw out the agony. Agreement with the IMF was vital in order to open other doors. Zambia must not duck the steps which had to be taken. In practice governments often found it possible to go further than they believed they could. The IMF were not unreasonable. It was very important to prepare people thoroughly for difficult steps and explain the reasons. It sounded to her as though Zambia and the IMF were drawing closer on some points. Failure to follow IMF prescriptions often led to even greater problems in the long term.

The Prime Minister said that she would reply to President Kaunda in due course. It is for consideration whether it is better to do so before or after they meet at CHOGM.

#### The Gulf

Mr. Musokatwane said that he had been in touch with President Kaunda during the day. He would send a message to President Saddam Hussein urging him to cooperate fully with the United Nations Secretary-General in promoting a cease-fire.

#### CHOGM

In a brief exchange on the prospects for CHOGM, Mr. Musokatwane expressed appreciation for Britain's help to Mozambique. The Prime Minister said that she understood that President Kaunda would not now be visiting London before CHOGM. They might aim for a bilateral in Vancouver on Monday, 12 October.

I am copying this letter and enclosure to Alex Allan (HM Treasury) and to Martin Dinham (Overseas Development Administration).

*yes sir,*  
*C.D. Powell*

C.D. POWELL

Lyn Parker, Esq.,  
Foreign and Commonwealth Office.



*State House  
Lusaka, Republic of Zambia*

30th August, 1987.

*My Dear Prime Minister,*

On 23rd January, 1987 I wrote to you as I indeed did to other Heads of State or Government and to International Institutions, expressing my gratitude on behalf of the people of Zambia for the continued assistance that is being rendered to us in our efforts to restructure the economy. In that same letter, I also outlined the measures we had taken to implement the International Monetary Fund (IMF) Restructuring Programme as well as the problems we were facing as a result of implementing that programme. I must of course thank you for your response to that letter.

A lot has happened since I wrote that letter in January. As you know, on 1st May, 1987 I announced on behalf of our Party and its Government that we had decided to discontinue the IMF Restructuring Programme. The reasons were basically those that I had outlined in my letter of 22nd January, 1987. We found that in spite of all our determined efforts and much sacrifice by our people to implement a very difficult IMF programme and despite the very much appreciated support from donor countries

/...

The Rt. Hon. Mrs. Margaret Thatcher, MP.,  
Prime Minister of the United Kingdom,  
No. 10 Downing Street,  
LONDON.



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and International Institutions, the IMF Programme had not succeeded in arresting the country's economic decline. Instead, we found ourselves in a situation in which our currency had seriously depreciated against our major trading partners, an almost run-away inflation, unprecedented level of unemployment and increased external commitments.

Zambia has had a succession of programmes with the IMF for the past twelve years and we have been to the Paris Club three times - in 1983, 1984 and 1986 - to reschedule our debts and yet our economy continued to decline whilst our debt obligations, on the other hand, escalated. Our projections even indicated that for the next six years, we would be exporters of resources to the IMF. Obviously, we could not continue in such a situation. We had to try another programme but it required terminating the one with the IMF first.

I am now pleased to enclose for your information a copy of our New Economic Recovery Programme which we have worked out. You will observe that this programme is in fact an Interim Plan which will run from July, 1987 to December, 1988 after which we hope to embark on a new five year plan. We believe, however, that this Interim Plan is best suited to our circumstances and addresses realistically the problems that we face in our country. We hope, therefore, that in implementing this programme, we can count on your continued support and understanding as you have done in the past.

/...



- 3 -

Let me hasten to reaffirm that Zambia is still committed to the objectives of the restructuring programmes that we have worked out with the IMF since 1978 and which as a country we have tried to implement faithfully. These programmes have been supported by both the World Bank and donor community. We have together been working on programmes aimed at:-

- (a) diversifying exports and thereby reducing excessive dependence on copper exports;
- (b) improving capacity utilisation in the economy;
- (c) promoting labour intensive as opposed to capital intensive industries; and
- (d) increasing foreign exchange earnings.

The new restructuring programme has, therefore, been prepared with the same objectives in mind. In the main, the new programme advocates a development strategy which, while ensuring austerity, recognises the need to protect the most vulnerable members of our society who also happen to be the majority. The plan, therefore, focusses on:-

- (a) directing the country's scarce foreign exchange into the reactivation of selected high priority sectors;
- (b) stabilising the economy by controlling inflation; and
- (c) ensuring that the profits generated from the reactivated economy are reinvested in the selected sectors, so that the country's economic growth should depend principally upon such investment.

/...



- 4 -

Let me also restate that whilst we are emphasizing "Growth from our own Resources", this does not mean that Zambia no longer needs external assistance and support. Indeed, we need that support. We are the first to recognise our present limited capacity in earning foreign exchange and that is why one of our strategies remains the promotion of non-traditional exports.

In view of our Special relations and the support that your country has always extended and continues to do - in support of our economic endeavours - I thought it right and proper to send my colleague the Rt. Hon. K. S. K. Musokotwane, Prime Minister, to come and personally deliver this letter. This I thought would give you an opportunity to seek clarification on any matter relating to our New Economic Recovery Programme and actions we have taken in recent months.

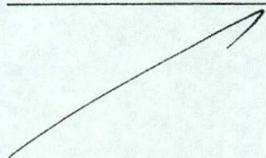
Let me end by once again appealing to you as I did to the conscience of the International Community to pass a fair judgement on the measures we have adopted. We still remain faithful members of the IMF, World Bank and other Multi-lateral Agencies and stand ready to discuss with them as we do with your country, any matter concerning our New Economic Recovery Programme. We, therefore, look forward to receiving your reaction in due course.

God's blessings.

*Your sincerely*

*160*

Kenneth D. Kaunda  
PRESIDENT OF THE REPUBLIC OF ZAMBIA



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1. ACCA  
2. PWP  
(Don't forget to send copies  
with comp slips to  
PS/Sir G Hare, PS/No 10,  
+ PS/Mr Patten)

NOTE OF A MEETING HELD AT NO 11 DOWNING STREET AT 11.00 AM ON  
MONDAY 7 SEPTEMBER 1987

**PRESENT:**

Chancellor of the Exchequer  
Mr P G F Davis  
Mr J C May  
Mr J M G Taylor

Mr Musokatwane, Prime Minister of Zambia  
HE The High Commissioner of Zambia  
Zambian Officials

**UK/ZAMBIAN ISSUES**

Mr Musokatwane said he had come to explain the economic difficulties facing Zambia and the steps being taken to deal with them. There was no disagreement between Zambia and the IMF on what needed to be done; only on precisely how to do it. The IMF programme had run into difficulties. In particular, the foreign exchange auction had led to chaos in exchange rates without achieving the necessary allocation of funds to priority areas; the fuel price increases the IMF wanted would have severely damaged copper production; the phasing out of fertilizer subsidies hit the peasant farmers who could not borrow rather than the larger agricultural producers who could; the benefits of price decontrol had gone to the middlemen rather than to industry; the constraints on Civil Service salaries caused most of the best brains to leave the Civil Service and those that remained were ill-motivated.

The New Economic Recovery Programme (NERP) gave priority to key sectors such as companies which were labour intensive, industries using local raw materials, and companies which generate foreign exchange. Its aims were stability and adjustment in the context of copper prices at a record low. There would be continuing reduction of subsidies and continuing retrenchment in the Civil

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Service. All the IMF's objectives were accepted by the NERP. But it was impossible to avoid restricting debt repayments.

The NERP covered the next 18 months. The critical time for Zambia was now. Mr Musokatwane was grateful for British project financing; what he hoped for now was more British investment. Zambia needed raw materials. He hoped that the Chancellor would be able to offer some commodity assistance.

The Chancellor thanked Mr Musokatwane for a very clear explanation. He appreciated the economic and political difficulties facing Zambia. He was very concerned about the position in Sub-Saharan Africa, which his proposals on debt were designed to alleviate. He would be pursuing these proposals in the coming months. But an important feature of the proposals was that the debtor country must have adequate reforming policies in place. There was no point in investing in failure. He was not convinced that the NERP was sufficient. For example, the Kwacha was still overvalued, the fiscal stance was too loose, and there were inadequate incentives for farmers to increase production. In the UK's view the Plan did not add up to a solution to Zambia's severe difficulties.

The way forward must be through agreement with the IMF. The IMF had a good understanding of Zambia's problems. If agreement could be reached the UK would be ready to back a new programme with additional assistance, as would other donors. The need to reach agreement with the IMF was now urgent: there was a danger that Zambia would be declared ineligible, and that would severely damage her financial standing.

Mr Musokatwane replied that in his long experience, the IMF did not sufficiently understand the differences between individual countries and did not tailor its conditions to suit them, but

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tried to impose the same conditions on all. The Fund was not originally designed for the role it was now undertaking and it still lacked the right machinery for it. It was changing, but too slowly.

Zambia hoped to hold a consultative meeting early next year under the auspices of the World Bank, whose staff were currently assessing the NERP. There was unlikely to be any agreement on a new IMF programme in the next few months.

The Chancellor said that the best way the UK could help Zambia was with attempts to reach an agreement with the IMF. The new Managing Director of the Fund was sensitive to the individual circumstances of countries such as Zambia. He would be ready to recognise Zambia's position. But some movement would also be necessary on Zambia's part.

A handwritten signature in black ink, appearing to read 'J C May'.

J C MAY

HM Treasury

8 September 1987

cc: Those present  
PS/Economic Secretary  
Sir G Littler  
Mr Lavelle  
Mr H Evans  
Mr Mountfield  
Mr Walsh  
Mr Cropper

REC. 10 SEP 1987

RECORD OF MEETING BETWEEN THE MINISTER FOR OVERSEAS DEVELOPMENT  
AND THE ZAMBIAN PRIME MINISTER, 3 PM 7 SEPTEMBER 1987

ACTING	PS/KST
TO	Sir P Middleton
	Sir G Kitter
	Mr Javelle
	Mr H P Evans
	Mr P G P Davis

Present:

Mr Musokotwane (Prime Minister, Republic of Zambia)      Mr Chris Patten (Minister for Overseas Development)

HE Mr Phiri (Zambian High Commissioner in London)      Mr Cahill (ODA)

plus three Zambian officials      Mr Dinham (PS/Mr Patten)

*Mr Mowford*  
*Mr Ball*  
*Mr J C May*

1 Mr Patten said that it was a great pleasure to see the Prime Minister and his associates in London; the British Government valued their relationship with Zambia very highly.

2 Mr Musokotwane described the points of difference between the IMF and Zambia. These related to:

- i) the auction, which was a poor instrument for determining the exchange rate;
- ii) the liberalisation of trade: it was inappropriate for an underdeveloped country to embrace a full system of liberalisation, making no distinction between priority and non-priority sectors of the economy;
- iii) the budget deficit: it was impracticable to reduce such items as fertiliser prices over the timescale envisaged by the Fund.

Zambia had therefore introduced an Interim Plan to restructure its economy. The Plan preserved the IMF's objectives, but chose other methods of achieving them. Zambia hoped the World Bank might provide assistance, with a view to a Consultative Group meeting early next year. "Our 'Mission Impossible' to Britain" (said Mr Musokotwane) was to persuade the British Government to provide aid in furtherance of the Interim Development Plan. Some of the companies which contributed most to Zambia's economy were British-owned; unless aid was provided they would work only at some 15 per cent of capacity. Britain could also assist Zambia with equipment for drilling boreholes in the drought-stricken areas.

3 Mr Patten said that British aid was provided in four main forms:

- i) disaster and emergency aid;
- ii) technical co-operation;
- iii) project aid;
- iv) "programme" or "commodity" aid.

On i), Britain had contributed so far only via the European Community towards drought relief for Zambia, and we should be glad to consider bilateral action if the Zambians would find it useful. On ii) and iii), we looked forward to continuing our existing aid commitments; our manpower aid to Zambia was the largest such programme which we had anywhere in the world, while our aid for rural development was regarded as a model of its kind. As for iv), Mr Patten referred to

the increase in the total of British programme aid to sub-Saharan Africa; the last few months had seen substantial new commitments to such countries as Uganda and Mozambique which were following recovery programmes agreed with the international institutions. The Chancellor's Spring initiative on debt also demonstrated Britain's commitment to helping to solve the economic problems of sub-Saharan Africa. The touchstone however for the grant of British programme aid was the question of whether or not the country concerned had agreed to follow an IMF programme. It was on the grounds that the Zambians were (as it then seemed) close to agreeing such a programme with the IMF that we had agreed in April to make £8 million available. We greatly regretted it when negotiations between Zambia and the Fund broke down at the beginning of May. With one negligible exception however we were not giving programme aid in Africa to any countries not following IMF programmes. Mr Patten wondered how the news that we had given aid to such a country would be received in countries such as Tanzania, Mozambique, Uganda and Ghana which had come to terms with the Fund at the cost of considerable sacrifice. We very much hoped that Zambia could reach agreement with the Fund again so that we could support her. The longer it took for such agreement to be reached, the more difficult it would be for us to find money for Zambia on account of other countries' claims on our resources. Mr Patten concluded by saying that he thought other donors were unlikely to differ from our view.

4 Mr Musokotwane said the Fund were likely to take some time before saying Yes or No to any renewed approaches from Zambia. He said that the Chancellor had agreed with him when they met earlier in the day that the IMF was not designed to cope with problems of the kind Zambia was experiencing. Could Britain provide additional project aid, if it could not make programme aid available?

5 Mr Patten acknowledged that Zambia's discussions with the IMF touched on spots which were politically highly sensitive in domestic terms. He doubted whether a substantial increase in project aid was a practical alternative to programme aid, if only because the sums involved in project aid were much smaller in scale and slower-moving. At the same time we would continue to keep in close touch with the Government of Zambia, whether in Lusaka, London or Washington. In general, we would lean over backwards to give our friends the benefit of any doubt: that said, the condition for British programme aid to Zambia was clear and it had not yet been met.

6 The meeting lasted 35 minutes and took place at the Prime Minister's hotel: the atmosphere was highly cordial throughout. Because of pressure of time (Mr Musokotwane was due at No 10 at 4 pm) Mr Patten was unable to raise the subject of the Director-Generalship of FAO.

Central and Southern Africa Department  
Overseas Development Administration  
8 September 1987

Distribution:

PS/Secretary of State	Mr Caines	Mr Munro
PS/Chancellor	Mr Ainscow	Mr Reeve
PS/Mr Patten	Mr Hudson	Mr Cullimore (CAFD)
PS/Mrs Chalker	Mr Buist	Mr Richardson (ERD)
	Mr Machin	Mr White (Lusaka)
	Mr J T Roberts	Mr Faint (UKDEL Washington)
	Mr Stegmann (BDDSA)	



FROM: P G F DAVIS

DATE: 14 SEPTEMBER 1987

CHANCELLOR

*Ch/ I think I should write as proposed to put the record straight. Content?*

- cc PS/Chief Secretary
- PS/Economic Secretary
- Sir P Middleton
- Sir G Littler
- Mr Lavelle
- Mr H P Evans
- Mr Mountfield
- Mr Walsh
- Mr May

*Put Mansel, but OK as*

**MEETING WITH THE MINISTER FOR OVERSEAS DEVELOPMENT AND THE ZAMBIAN PRIME MINISTER ON 7 SEPTEMBER 1987**

In ODA's note of the above meeting Mr Musokotwane is recorded as saying that you "had agreed with him... earlier in the day that the IMF was not designed to cope with problems of the kind Zambia was experiencing". You might wish to correct the impression that this gives in a short Private Secretary letter. I attach a draft.

*para 4 in note immediately below this minute.*

*P G F Davis*

P G F DAVIS

*Pl type for 75 sig.*

DRAFT LETTER FROM

PS/CHANCELLOR TO PS/MINISTER FOR OVERSEAS DEVELOPMENT

MEETING WITH THE MINISTER FOR OVERSEAS DEVELOPMENT AND THE ZAMBIAN PRIME MINISTER ON 7 SEPTEMBER 1987

The Chancellor was grateful for the record of the above meeting which you copied to me. He has noted, however, that Mr Musokotwane's reference, recorded in paragraph 4, to what had been said at his own earlier meeting with the Zambian Prime Minister does not reflect the full substance of the exchanges. *is record.*

~~2. Mr Musokotwane had made the point that the IMF was not originally designed for the role it was now undertaking. The Chancellor replied that the Fund now had considerable understanding of the difficulties which Zambia was experiencing. He added that the new Managing Director was sensitive to the individual circumstances of countries such as Zambia; and Mr Musokotwane acknowledged this.~~

*The Chancellor agreed with Mr M that the IMF had not been originally designed to deal with the current situation, but added that it had now acquired unrivalled expertise in this field and that he would head on for Zambia to conclude an agreement with the Fund.*

*Copies to Robert Cullshaw and John Sawers.*

*ZMG T-*



Treasury Chambers, Parliament Street, SW1P 3AG  
 01-270 3000

15 September 1987

M J Dinham Esq  
 Private Secretary to the  
 Minister for Overseas Development  
 Overseas Development Administration  
 Eland House  
 Stag Place  
 SW1E 5DH

*Dear Martin*

**MEETING WITH THE MINISTER FOR OVERSEAS DEVELOPMENT AND THE  
 ZAMBIAN PRIME MINISTER ON 7 SEPTEMBER 1987**

The Chancellor was grateful for the record of the above meeting which you copied to me. He has noted, however, that Mr Musokotwane's reference, recorded in paragraph 4, to what had been said at his own earlier meeting with the Zambian Prime Minister is incorrect.

The Chancellor agreed with Mr Musokotwane that the IMF had not been originally designed to deal with the debt problem, but added that it had now acquired unrivalled expertise in this field and that the overriding need was for Zambia to conclude an agreement with the Fund.

I am copying this letter to Robert Culshaw and John Sawers.

*Yours sincerely*  
*J M G Taylor*

J M G TAYLOR  
 Private Secretary