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**MINISTER OF FINANCE 2007 BUDGET STATEMENT**

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## IX. CONCLUSION



**I. MOTION**

1. Mr. Speaker Sir, I move that leave be granted to bring in a Bill to make Provisions in connection with Revenues and Expenditures of the Republic of Zimbabwe and to make Provisions for matters ancillary and incidental to this purpose.

**II. INTRODUCTION**

2. Firstly, Mr Speaker Sir, I wish to start my Budget speech by acknowledging the valuable support and cooperation that I continue to receive from Parliament in the formulation and implementation of the National Budget.
3. This is consistent with Government's commitment for improving the budgeting process by involving a wider range of stakeholders, including those at grassroots levels. Such involvement guarantees the ownership of the Budget by all stakeholders and is critical for sustaining consensus over the implementation of announced policy measures.
4. It is against this background that my Ministry undertook a nationwide consultative outreach programme aimed at involving the public as much as possible in the Budget formulation process. My Ministry benefited tremendously from the input of stakeholders to which Government attaches great value.
5. The central message from these consultations evolved around the following challenges among others:
  - Ever-increasing prices;
  - Continued distortions in the pricing of key commodities and utilities;
  - Unemployment and rising poverty levels;
  - Foreign exchange shortages;
  - Low industrial capacity utilisation;
  - Underutilised allocated land;
  - Inadequate measures to deal with rising levels of corruption in both the public and private sectors;
  - Deteriorating provision of basic public services;
  - Poor maintenance of infrastructure;

- Inconsistent policy pronouncements;
  - Declining clarity over the role and accountability of the key institutions of Government;
  - Perceptions of lack of commitment to effectively deal with the challenges facing the economy; and
  - Increasing indiscipline.
6. One of the consequences of the above challenges, Mr Speaker Sir, is the emergence of very large income disparities, with the majority of the lowest paid workers earning below the Poverty Datum Line.
  7. The deterioration in the welfare of our people has seen their capacity to access basic healthcare services, education, housing and other amenities collapse overnight, under the prevailing hyper-inflationary environment.
  8. This, Honourable Members, is happening at a time when a small proportion of the population is now accumulating wealth overnight, in part benefiting from the price distortions arising from some of the policies and facilities meant to protect the very poor.
  9. In this environment, the country continues to experience loss of critical skills, the dominance of the informal sector in the economy, declining capacity utilisation and de-industrialisation. These are some of the challenges that the Budget will have to address with 'head-on'.
  10. Regrettably some of the wealth accumulation is a direct product of the prevailing indiscipline in our economy. We have amongst the citizens, individuals benefiting from abuse of public resources and thereby contributing to unnecessary public expenditures and economic hardship.
  11. Mr Speaker Sir, we therefore need to declare war against indiscipline, and in this War, the Budget will not be found wanting. We will therefore need to review and strengthen the legislation and penalties for economic crimes.
  12. Mr Speaker Sir, Honourable Members will be aware of the partnership with the private sector in the context of the National Economic Development Priority Programme (NEDPP). The thrust of the NEDPP is the implementation of Quick

Win programmes and projects, whose objective is to stabilise the economy and lay the foundation for sustained economic growth.

13. The 2007 National Budget will play its critical role of addressing stakeholder concerns, support the NEDPP measures, foster macro-economic stability and restore business confidence.
14. Mr Speaker Sir, it is no secret that the country remains under siege, facing sanctions from the West, characterised by lack of balance of payments support, lines of credit, foreign direct investment and deliberate efforts to undermine our economic turnaround initiatives.
15. This makes it vital that we employ innovative tactics to survive in this environment, taking advantage of our abundant natural resource endowment and reliable cooperating partners.
16. Mr Speaker Sir, the 2007 Budget will be guided by the Results Based Budgeting principles adopted by Government in 2005. Hence, the expenditure allocations for the coming year are related to the anticipated and time-framed deliverables during 2007. I am happy to note that submissions from line Ministries now take the Results Based Budgeting format on board.
17. The setting of specific deliverable targets for the respective line Ministries under the 2007 Budget should also assist to 'turn the tables' on the major inflation drivers under Ministries' domains through active focus on productivity and close monitoring at the Ministry level. In this regard, the Budget will ensure that Ministries focus on their roles and responsibilities in fighting the overall inflation levels.
18. Mr. Speaker Sir, Honourable Members will be aware that the implementation of our Currency Reform exercise on August 1, 2006 resulted in the revaluation of the currency with the removal of three zeros from the old bearer cheques and the introduction of a new set of bearer cheques. Hence, in my presentation, all domestic currency statistics reflect the revalued currency.
19. Mr Speaker Sir, my presentation will cover the fiscal performance up to October 2006 and the estimates to year end. I will also touch on the economic challenges we are facing as a Nation.



20. Mr Speaker Sir, allow me to first of all give a brief overview of the Global Economic Outlook, as well as a review of recent Domestic Economic performance and projections for 2007.
21. My outline of the Fiscal Outturn during 2006, will be followed by the 2007 Expenditure Bids by line Ministries, before I turn to the Thrust and Priorities for the 2007 National Budget, and my Revenue Proposals.

### III. **GLOBAL ECONOMIC OUTLOOK**

22. Global economic performance remained strong in 2006, with emerging markets experiencing rapid growth, against the background of strong non-oil commodity prices, especially minerals. Performance was most notable in China whose growth is forecast to remain high at about 10% in 2006 and 2007. In India, growth is expected to remain at 8% percent in 2006, down slightly from 8.5% in 2005.
23. Thus global growth of 5.1% is forecast in 2006, up from the 4.9% realised in 2005. Global economic growth is forecast to slightly drop to 4.9% in 2007.
24. Economic growth in the United States is expected to increase marginally to 3.4% in 2006, compared to 3.2% in 2005. This is being driven by consumption and residential investment.
25. Economic recovery in Japan is continuing, with growth forecast to increase to 2.7% in 2006, after recording a growth of 2.6% in 2005.
26. In the Euro zone, a 2.4% economic growth is expected in 2006, up from 1.3% in 2005.
27. The strong recovery in Europe and an upswing in the Japanese economy will play a critical role in sustaining global economic growth.
28. Developing economies continue to grow, underpinned by fiscal consolidation, market-oriented reforms, increased foreign investment inflows and greater exchange rate flexibility.
29. In Sub-Saharan Africa, a 5.2% growth is expected in 2006. An upswing in economic growth to 6.3%, is expected on the back of increased oil output in Nigeria, Angola and Equatorial Guinea.
30. In Southern and Eastern Africa, growth of over 5% is expected in 2006. The region should benefit from recent efforts to further deepen regional integration and the opening up of markets through Free Trade Areas. In this regard, it is important that our business community be ready to take advantage of the opportunities that arise from deeper regional integration.

31. Strong global economic growth, especially in China and India, has continued to support the high international prices of primary commodities, especially copper, gold and platinum. Although oil prices have been coming down, the price still remains volatile.
32. In May 2006, gold and platinum prices reached record levels of US\$722 per ounce and US\$1328 per ounce, respectively. Brent crude oil prices reached a record high of US\$79 in August.
33. The threat of protectionist pressures, coupled with volatile oil prices, remain major risks to global growth.

#### IV. RECENT ECONOMIC DEVELOPMENTS

##### **Overall Economic Activity**

34. Mr. Speaker Sir, the Zimbabwean economy is expected to register a lower decline of 2.5% in 2006, compared to the 3.8% decline registered in 2005. This is on the back of the overall economic reversal of the downward trend experienced in agricultural production over the past few season.
35. The combination of a good weather outturn, coupled with the consolidation of our Land Reform Programme contributed to the anticipated 6.4% growth in agriculture in 2006.
36. The economy is projected to grow marginally by between 0.5% to 1% in 2007. This is due to the anticipated improved performance in agriculture and mining. The performance of the manufacturing sector continues to be negatively affected by low capacity utilisation and is expected to decline by about 7% in 2006. The sector is projected to decline at a lower rate of 2% in 2007.

##### *Agriculture*

37. Agriculture is anticipated to grow by about 6.4% in 2006. This, however, is lower than the original projection of a growth of 23%. The deviation is largely on account of lower than anticipated maize and wheat production.
38. Mr Speaker Sir, the outlook for agriculture for the 2006/07 season is promising, given Government's efforts to ensure adequate and timely supply of critical inputs such as seeds, fertiliser, fuel and chemicals. These efforts by Government, in partnership with key private sector stakeholders, has seen better coordination and supply of inputs and will result in increased productivity and better yields.
39. Early preparations and the timely provision of inputs create greater scope for farmers to adequately plan and hence, the increase in expected crop hectareage. The on-going rehabilitation of the greenhouse facilities is supporting the revival of the horticulture sub-sector.

40. Mr Speaker Sir, against this background, and also taking account of forecasts by the Meteorological Department of a near-normal rainfall season, agricultural output is expected to register a growth of 9.4% in 2007.

### *Mining*

41. Mr Speaker Sir, record high international mineral prices have seen improved foreign exchange realisations from mineral exports. Gold prices have risen to over US\$600 per ounce, while copper and platinum prices have risen above US\$7 000 per ton and US\$1 200 per ounce, respectively. Similarly, nickel prices have more than doubled to over US\$30 000 per ton.
42. However, the lack of extensive mining recapitalisation at existing mines and investment in new mining exploration programmes has remained a major constraint to the expansion of mining operations. This has been compounded by disruptions to power supplies, coupled with rising mining production costs which affect viability.
43. The spiralling cost of capital items, due to inflation, is being exacerbated by the rising parallel market exchange rates at which most imported items are priced.
44. The other serious challenges still facing the mining sector are the continued leakages in our mineral exports, especially gold and diamonds. Owing to the above challenges, gold deliveries declined by 24%, from 10 552.04 kgs in the period January - September 2005, to 7 991.57 kgs in 2006.
45. Asbestos production declined slightly from 93 326 tons by September 2005 to 82 252 tons for the same period in 2006. However, platinum production increased marginally from 3 563.34 kgs in 2005 to 3 822.77 kgs in 2006.
46. The law enforcing agents, together with the Reserve Bank should strengthen measures to address leakages in the mining sector. Policies to improve viability in the mining sector will be vigorously pursued by Government. This should support the revival of mining production, which is projected to decline by 14.4% in 2006.
47. In this regard, realising higher gold production and deliveries will require an appropriate exchange rate regime which ensures viability, on the back of all time high international mineral prices. Furthermore, the setting up and taking over of

some gold milling centres by Fidelity Printers and Refinery should contribute towards reducing leakages in gold export receipts.

48. In coal mining, the recent recapitalisation at the Hwange Colliery Company has started to bear fruit. As a result of this recapitalisation, the mining company has been able to open the new Chaba Mine and commence operations at the 3 Main underground mines.
49. Monthly coal production, is therefore projected to double by December 2006 to 425 000 tons, enabling the company to meet local demand of 412 000 tons and to resume exports.
50. Overall, mining output is estimated to grow by 4.9% in 2007.

#### *Manufacturing*

51. Mr Speaker Sir, price distortions, foreign currency shortages for the importation of essential raw materials and spares, energy shortages and declining real disposable incomes continue to depress production in the manufacturing sector. The sector is estimated to decline by 7% in 2006.
52. The inability by most manufacturers to source foreign exchange for importing raw materials from the inter-bank market has meant that they have increasingly relied on the parallel market, where the exchange rate is significantly depreciated. This has forced companies to incur higher production costs, which are ultimately passed on to consumers as higher prices. This has contributed to the escalation of higher inflation.
53. The shortage of foreign exchange to import adequate raw has compromised industrial capacity utilisation. Most companies continue to operate below 30% capacity which means higher production unit costs. This, against a background of rising demand, has contributed to price escalations.
54. Mr Speaker Sir, measures to ensure growth in the economy's industrial base have included support for distressed companies, Import Substitution and Value Addition.

55. Schemes already in place include the \$5 billion Fund to resuscitate distressed companies, which is being managed by the Infrastructure Development Bank. The Bank is also managing the \$500 million Value Addition and Import Substitution Fund.
56. This, coupled with the initiatives to vigorously promote toll manufacturing, should also see an improvement in industrial capacity utilisation. These measures, including an exchange rate regime which guarantees the viability of exporters, should assist to reverse the decline in industrial production. The manufacturing sector, Mr Speaker Sir, is projected to decline by 2% in 2007.

### *Tourism*

57. Vigorous marketing and promotional initiatives in Asia and the Middle East markets are starting to pay dividends as reflected by the increase in tourist arrivals from these regions. Growth of the regional and domestic tourism markets has also supported growth in the tourism industry.
58. In response to these marketing efforts, tourist arrivals during the period to September 2006, grew by 45% to 1 596 489 over the same period in 2005. The positive outturn to September 2006 reflects a 52% growth in tourist arrivals from African countries, mostly Southern Africa. Tourist arrivals are expected to grow by 23% for the year, with growing numbers coming from Asia.
59. As the tourism sector recovers there is need to plug all leakages of foreign exchange earnings. This should reverse the mismatch between increasing tourist arrivals and revenues.

### *Transport*

60. The economy is benefiting from improved performance and capacity of the National Railways of Zimbabwe (NRZ), against the background of concerted efforts by the Board, management and client stakeholders. This has seen significant refurbishment of locomotives and wagons, allowing the NRZ to generate enough revenue to sustain its operations, including liquidating statutory obligations for tax, pension, and medical aid contributions.

61. Sustaining this turnaround, will require further support in the rehabilitation of infrastructure, signalling equipment and the improvement of locomotive power and rolling stock capacity. Already, the NRZ is taking advantage of Government's Look East Policy in upgrading the Harare-Mutare, Bulawayo-Victoria Falls and Bulawayo-Chiredzi lines.
62. Road transport capacity has also benefited from improved fuel availability, from the Direct Fuel Import facilities, as well as the other facilities being coordinated by the Reserve Bank.

### **Inflation Developments**

63. Mr Speaker Sir, inflation remains one of the major challenges facing our economy. Year on year inflation rose from 613.2% in January 2006, to reach a peak of 1 204.6% in August. In September it however declined to 1 023.3%, before the rise to 1 070.2% in October 2006.
64. Such high levels of inflation have resulted in the erosion of disposable incomes and worsened poverty. Savings have been severely affected, with pensioners unable to make ends meet. On the other hand, the competitiveness of our exports has been eroded significantly by such high levels of inflation.
65. Some of the major drivers of inflation remain:
- The impact of public sector borrowing requirements, for budgetary financing;
  - Quasi-fiscal activities funded through the Reserve Bank;
  - High money supply growth;
  - Corruption;
  - Increase in parallel market activities;
  - Foreign exchange shortages;
  - Inflation expectations;
  - Price distortions and behaviour of economic agents; and
  - Structural supply bottlenecks.
66. Mr Speaker Sir, high levels of inflation have become increasingly self-sustaining through the breeding of expectations of even higher levels of inflation. In such an



environment producers are now adjusting their prices on the basis of their expectations of the cost of replacing stock.

67. Similarly, salary and wage settlements are being driven by high inflation and inflationary expectations as workers aim at avoiding further erosion of the purchasing power of their incomes.
68. This behaviour is contributing to the prevailing vicious wage-price spiral – where high inflation prompts high wage demands, and vice versa.

### **External Sector**

69. Mr Speaker Sir, our Balance of Payments (BOP) position continues to be under severe pressure, against a background of declining exports, absence of BOP support, lines of credit and foreign direct investment.
70. Reflecting this, a current account deficit of US\$543.3 million is projected in 2006 as both manufacturing and mining performance remain depressed. With agriculture and tourism still to fully recover, their contribution to export growth remains limited.
71. In 2006, mineral, manufactured and agricultural exports are projected to decline by 0.2%, 10.5% and 6.3%, respectively. As a result, exports are estimated to decline by 6% in 2006.
72. Imports, which increased marginally by 0.2% in 2005, driven by increased food, electricity, fuel and manufactured imports, are however projected to decline by 1.6% in 2006, against a background of foreign currency shortages.
73. On the capital account, net inflows amounting to US\$298.4 million are envisaged. Foreign direct investment into mining and some of our Parastatals under the Look East initiatives are the major factors contributing to the positive capital account balance

### *External Debt*

74. Mr Speaker Sir, Zimbabwe remains committed to honouring all its external loan obligations. The severe BOP position, partly arising from sanctions, however, limits our ability to meet our external loan obligations.
75. As a result, of the total external debt outstanding amounting to US\$4.1 billion at end of October 2006, external payment arrears total US\$2.2 billion.

**V. FISCAL DEVELOPMENTS IN 2006**

76. Mr. Speaker Sir, Honourable Members will recall that the 2006 Original Budget, together with the Supplementary Budget I presented to the House on July 27, provided for total expenditure and net lending of \$451.1 billion, revenue of \$250 billion, and a deficit of \$201.1 billion or 18.7% of estimated GDP.
77. Actual Budget performance to October 2006 shows total expenditure and net lending at \$263.2 billion, against revenue of \$229.1 billion. Given projections for the last two months of 2006, total revenues will rise to \$351.6 billion.
78. This, Mr. Speaker Sir, would reduce the budget deficit outturn to \$99.5 billion, implying a much reduced 2006 fiscal deficit of 9.2% of estimated GDP.
79. Improved revenue collections, largely on account of higher inflation, have not been translated into improved service delivery and project implementation, given the cost escalations which adversely affected the delivery of public services.

**Revenue Performance to October**

80. Revenue collection to October remained in line with the revised revenue targets and on course at \$229.1 billion, against the background of tighter enforcement of compliance by ZIMRA. Tax revenue accounted for \$220.9 billion of this. Non-tax revenue to October 2006, comprising mainly of fees, charges, and the 7.5% civil servants pension deductions, contributed \$8.2 billion.
81. The improved collection is due to increased enforcement of compliance by ZIMRA. This has resulted in significant increase in the number of PAYE and corporate returns being filed. Value Added Tax and Customs Duty have also significantly increased.
82. Value Added Tax collections amounted to \$61.5 billion, translating to 27.5% of total revenue, against a target of \$49.2 billion. VAT on local sales amounted to \$42.3 billion, and that on imports, to \$18.3 billion. Improved VAT collections were attributed to price increases of goods and services, as a result of the current hyper inflationary environment, and were also complemented by the August

2006, movement in the official exchange rate used in valuation of imports. VAT collections are expected to end the year at \$100 billion.

83. Individual Pay As You Earn (PAYE) tax collections amounted to \$58.1 billion or 26.3% of total revenue, against a target of \$34 billion and are expected to end the year at \$80 billion. The positive performance of PAYE reflects the award of higher than anticipated salary and wage settlements in both the private and public sectors.
84. Customs duty collections amounted to \$26.7 billion or 12.1% of total revenue, against a cumulative target of \$23 billion. This improved performance is partially attributed to the upward movement in the exchange rate, which impacted on the value of imports. Customs duty collections are expected to end the year at \$40 billion.
85. Corporate profits were constrained by low capacity utilisation arising from increased costs of production and shortages of foreign currency for the importation of raw materials and equipment. Cumulative collections for the period amounted to \$38.3 billion or 17.3% of total revenue, against a target of \$31.9 billion and are estimated to be around \$55 billion by year end.
86. Tax revenue collections from domestic dividends and interest were \$19.9 billion or 9% of total revenue, and are expected to end the year at \$22 billion. Major contributors to this revenue head were shareholders' tax, at \$12.9 billion, followed by tax on interest of, \$7 billion.
87. Carbon tax contributed \$2.9 billion, while other income taxes contributed \$2.2 billion to overall tax revenue as at the end of October 2006. The other income taxes were dominated by Withholding Capital Gains tax, which raised \$1.8 billion, and other Capital gains taxes which contributed \$366.4 million.
88. The tobacco levy, however, raised only \$50.9 million. This subdued performance was against the background of the challenges facing some of the new tobacco farmers. These relate to limited expertise, which contributed to the fall in yields. However, quality and quantity of product delivered to the auction floors should improve in the coming season benefiting from this year's early provision of inputs.

89. Excise duty collections performed above expectations at \$7.5 billion to the end of October 2006 and are projected at \$12 billion by year end. Alcoholic beverages continue to be the major contributor to this revenue head, benefiting from the frequent increases in the prices of alcoholic beverages and relatively stable demand.
90. Excise duty on beer accounted for \$4.5 billion, followed by that on tobacco, \$2.3 billion, & wines and spirits, \$812.1 million. The 5% excise duty on second hand vehicles generated \$370 million, while non-alcoholic beverages contributed \$483.3 million to excise duties.
91. 'Other taxes' collected over the ten months to October 2006, contributed \$3.9 billion to total tax revenue, with stamp duties remaining the major contributor at \$2.1 billion. Escalations in property values in a hyper inflationary environment, coupled with increased activity on the stock market, are underpinning stamp duty collections.
92. The banking levy realised \$827.3 million, followed by withholding tax on tenders, \$448.4 million, and the road access fee, \$374.8 million. However, the contribution of presumptive tax to 'other taxes' remained relatively small at \$112.8 million.
93. Overall revenue performance in the last two months of 2006, is expected to remain on course. The traditional year-end bonus payments, coupled with corporate tax payments should augment revenue collections during this period. Corporate tax payments under the contemporaneous tax system, wherein tax is payable in the fiscal year in which profits are generated, has greatly increased revenue under this sub-head.

#### **Expenditure Performance to October**

94. Total Budget expenditures and net lending for the ten-month period to October 2006 amounted to \$263.2 billion, against a target of \$321.7 billion.
95. Mr Speaker Sir, allow me to outline the performance of the key expenditure heads.

### *Employment Costs*

96. Employment costs for the period under review amounted to \$85.7 billion, against a target of \$76.3 billion.
97. This expenditure overrun is a result of reviews of public service incomes undertaken in January and May 2006, which were meant to cushion civil servants in the prevailing hyper inflationary environment. This also necessitated further review of housing and transport allowances with effect from October 2006.
98. Notwithstanding the above income adjustments, remuneration levels for the civil servant remain relatively low. This is compromising not only the capacity of Government workers to afford such basic necessities such as transport, accommodation, food, and medical service, but also the ability of Government to retain and attract skilled and experienced personnel.

### *Pension Payments*

99. In addition to reviewing salaries and allowances for civil servants, Government further reviewed pension benefits in January and May 2006. The reviews resulted in Pension payments of \$16.9 billion, against a target of \$15.1 billion. This enabled us to provide some cushion for retirees, as incomes were being eroded by inflation.

### *Goods and Services*

100. High inflation also impacts adversely on the capacity of Ministries to procure goods and services. This necessitated the provision of additional resources through the Supplementary Budget, mainly on account of increasing costs on transport, telecommunication, and utilities.
101. Overall expenditure for goods and services, at \$109.7 billion, exceeded targeted expenditure by \$118.4 billion.

### *Capital Expenditures*

102. Implementation of capital projects has also been affected by cost escalations arising out of hyper inflation. This has undermined our efforts to raise the Capital Budget to the levels targeted by Cabinet of over 30% of overall Budget expenditures.
103. Cumulative capital expenditure to October 2006, amounted to \$52.6 billion, against a target of \$72.9 billion.

#### *Lending*

104. Total net-lending as of October 2006, amounted to \$873.8 million, against a target of \$1.1 billion. Local Authorities remained the major beneficiary of Budget on-lending during 2006.
105. Delays in the submission of programme of works by some targeted beneficiary Local Authorities limited the extent of the upgrading of sewer and water reticulation facilities in our urban centres.

#### *Quasi-Fiscal Expenditures*

106. Mr Speaker Sir, Honourable Members will be aware that, in light of the scarcity of resources within the Budget envelope, some of the funding requirements for public and private sector projects were taken up by our Central Bank over the last three years. The emergence of some new priorities soon after the approval of the 2006 Budget, which could also not be met within the Budget envelope, exacerbated the situation.
107. Honourable Members will also be aware that the quasi-fiscal expenditures directly linked to price distortions and Government departments will ultimately be serviced by the tax-payer, hence, the need to fully reflect such expenditures in the Budget.
108. Such quasi-fiscal expenditures have risen to levels that are now undermining our turnaround efforts by systematically increasing the growth of money supply and therefore fuelling inflation, in addition to other negative effects on the economy.

109. These negative effects include instances where the quasi-fiscal expenditures did not achieve the desired supply response, owing to the abuse of availed facilities by some beneficiaries and the lack of deterrent measures.
110. In this regard, combating inflation will require the phasing out of all quasi-fiscal operations and adequately providing resources for prioritised expenditures within the Budget. This is also consistent with accountability and transparency over the allocation of public resources. Fulfilment of this requirement also assists the Nation to appreciate the totality of public sector expenditures and borrowing.
111. Hence, consistent with our Constitution and the Audit and Exchequer Act, beginning 2007, all such and any other additional public expenditures will be strictly and adequately reflected through the budgetary process.
112. Mr Speaker Sir, the stock of quasi-fiscal expenditures at the beginning of November 2006, amounted to \$372.9 billion. Of this amount, \$60.4 billion are quasi-fiscal expenditures for 2005, while \$8.4 billion is for the fiscal year 2004. This leaves the quasi-fiscal expenditures for the current fiscal year at \$304.1 billion as at November 2006.

#### Import Payments

113. Of the total quasi-fiscal expenditures, \$103.4 billion is related to Reserve Bank foreign exchange provision for various import programmes.
114. In this regard, fuel imports accounted for \$49.4 billion. GMB imports for seed, grain and fertilizer absorbed another \$25.5 billion. Payments for electricity imports, as well as other ZESA imports totalled \$13.3 billion. Air Zimbabwe foreign exchange requirements accounted for \$8.4 billion.

#### Agriculture Support Facility

115. In the absence of strong banking sector financial lending to the agricultural sector following the land reform, financial support for agriculture under the Agricultural Sector Productivity Enhancement Facility (ASPEF) amounted to \$101.2 billion.



116. Of the total ASPEF amount, \$60.4 billion went to farmers. Food security accounted for \$18.7 billion, while the winter wheat programme benefited to the tune of \$21.5 billion, with the balance spread between tobacco support, Agribank and the Agricultural and Rural Development Authority (ARDA).

#### Maize & Wheat Purchases and Subsidies

117. Furthermore, in the absence of the review of the Grain Marketing Board (GMB) maize and wheat selling prices at a time when the producer prices had been adjusted upwards, quasi-fiscal expenditures were also incurred. As at mid November 2006, support for maize and wheat purchases amounted to \$33.5 billion.

#### Exchange Losses

118. Distortions in the exchange rate, which stakeholder consultations suggest need to be corrected, have also contributed to us incurring quasi-fiscal expenditures. In this regard, total exchange losses were \$75.0 billion.

#### Tobacco, Gold & Cotton Support

119. The distortions in the exchange rate necessitated support prices for some exporters. In this regard, quasi-fiscal support expenditures benefited gold producers and tobacco farmers who received subsidy payments of \$8.9 billion and \$20.8 billion, respectively. Similarly, cotton farmers had received subsidies amounting to \$0.7 billion by November 2006.

#### Parastatals & Local Authorities

120. Mr Speaker Sir, a significant amount of the quasi-fiscal operations were incurred in support of the Parastatals and Local Authorities Re-orientation Programme.
121. This intervention was against the background of declining capacity to deliver basic public services, largely associated with poor corporate governance and management structures. Sub-economic tariffs exacerbated the situation.

122. Almost all of our Parastatals and Local Authorities benefited from this Programme, with draw-downs totalling \$17.8 billion by November 2006.

#### Productive Sector Facilities

123. The deteriorating macro-economic environment also had adverse effects on manufacturing and mining sector, necessitating the introduction of concessionary facilities.

124. In this regard, a total of \$0.1 billion was extended to resuscitate and capacitate distressed companies in manufacturing and, mining sectors.

#### Troubled Banks

125. Mr Speaker Sir, Central Bank measures to deal with the issue of problem banks and financial institutions have been with us for the last couple of years. In the process of restoring the integrity of the banking sector, insolvent institutions could not be salvaged.

126. Recapitalising those banks and institutions requiring liquidity and additional capital injection saw a number of troubled banks access the Troubled Banks Facility. Total support provided under this window amounted to \$3.2 billion as at mid November 2006.

#### Loans to Government Departments

127. A number of critical Government programmes and projects also benefited from quasi-fiscal expenditures. In total, over \$7.7 billion was extended to Government departments for various projects for the Ministry of Local Government, Public Works & Urban Development, the Zimbabwe Republic Police, road maintenance and upgrading.

#### **Domestic Debt**

128. Mr Speaker Sir, the level of public domestic debt, which had remained relatively stable during the first half of the year, has since been increasing rapidly against the background of increased expenditure demands on Government.
129. Total domestic debt declined from \$15.9 billion in December 2005, to \$14.9 billion by the end of April 2006, against the background of tight expenditure management.
130. However, domestic debt increased to \$46.1 billion by the end of June, largely driven by the review of civil service wages in May. By September, domestic debt had risen to \$119.4 billion, reflecting the impact of high inflation on Government operations and programmes. However by October 2006, domestic debt had fallen to \$97.8 billion.
131. In the prevailing hyper inflationary environment, the money market has largely operated at the short end. Reflecting this, Treasury Bills of under one year maturity continue to account for most of the public domestic debt at 76.2%, while 181-day paper accounted for 23.7%. Recourse to the highly inflationary overdraft facility with the Reserve Bank has, however, remained limited.
132. With over 98.5% of domestic debt being short term Treasury Bills of less than one year, the restructuring of domestic debt to long term paper becomes necessary. Such restructuring will reduce the interest burden to the fiscus.

#### **Budget Outturn Including Quasi-Fiscal Expenditures**

133. Mr Speaker Sir, I have already highlighted the need for us as a Nation to take a holistic approach in accounting for budget expenditures. This entails incorporating into the Budget, quasi-fiscal outlays incurred on behalf of Government by the Reserve Bank.
134. In this regard, I project the 2006 Budget expenditures to remain within the \$451.1 billion envelope approved by Parliament under both the original Budget presentation in December last year and the Supplementary Budget of July this year.

135. Quasi-fiscal expenditures are projected to end 2006 at \$372.9 billion. Incorporating these quasi-fiscal expenditures in the 2006 Budget outturn increases overall Budget expenditures to \$824.0 billion.
136. Mr Speaker Sir, such a high level of expenditure, against the anticipated revenue outturn of \$351.1 billion would imply a Budget deficit of \$462.9 billion (excluding interest payments).
137. As a proportion of GDP, this represents an unsustainably high Budget deficit of 43.0% of GDP, excluding interest. Such a high Budget deficit underpins the very high money supply growth rates of over 1 000% and the hyper inflation this Nation continues to experience.
138. Mr Speaker Sir, dealing with this challenge will require the adoption of bold expenditure management measures on our part.
139. Mr Speaker Sir, I now turn to the Expenditure Bids of Ministries for the 2007 Budget.

## VI. EXPENDITURE SUBMISSIONS FOR THE 2007 BUDGET

140. Mr Speaker Sir, my Ministry received from Ministries and Government Departments, various expenditure submissions for resource allocations, under the 2007 Budget.

141. High inflationary expectations appear to underlie most of the expenditure submissions from Ministries, given this year's experience. This reinforces the challenge before us of reversing the prevailing high inflationary expectations by adopting and implementing a credible and sustainable disinflation programme. Such a programme should be anchored on the complementarity between Fiscal and Monetary policies.

142. Honourable Members, for us to achieve single digit inflation, we will as a Nation, have to make sacrifices and endure some pain. We cannot run away from this fact, which I would like all of us to appreciate and acknowledge.

### *Overall Bids*

143. The total 2007 Budget expenditure bids of line Ministries and Departments amount to \$24.0 trillion. This request excludes interest payments that will accrue from the domestic borrowings required to finance the Budget deficit. These expenditure bids represent a growth of 5 313% over this year's anticipated expenditure outturn. The comparable overall revised Budget for 2006, following the Supplementary Budget, is \$331.4 billion, also excludes interest.

### *Capital*

144. Bids for the Capital Budget in 2007 amount to \$10.9 trillion, up 9 687% on this year's projected expenditure outturn of \$112.3 billion.

145. Given the above scenario, I have therefore, rationalised the expenditure bids by Ministries and Government Departments in line with our NEDPP priorities, ongoing Government projects and the capacity of the Budget to finance them in a manner that is consistent with our inflation targets.

146. Mr Speaker Sir, I now turn to the Thrust and Priorities of the 2007 Budget, which as I have already indicated will be presented along the principles of Results Based Budgeting which Government adopted in 2005.

## VII. THE 2007 BUDGET THRUST AND PRIORITIES

147. Mr Speaker Sir, as we move forward, it will be critical that the 2007 Budget expenditure levels be consistent with a credible anti inflation programme, targeted at drastically reducing money supply growth. This is the only way we will begin to have a firm hand in containing inflation, a prerequisite for building confidence and dealing with high inflation expectations.

148. A comprehensive package to re-enforce policy measures to restore macro-economic stability will therefore encompass the following:

- Consistent fiscal consolidation and expenditure restructuring focusing on capital development, health and education;
- Phasing out quasi-fiscal operations and allocating all resources through the National Budget;
- Elimination of wholesale subsidisation;
- Dis-inflation monetary policy and interest rate management framework targeting reduction in money supply growth;
- An appropriate exchange rate regime and incentives to ensure exporter viability;
- Unlocking Balance of Payments support and external lines of credit;
- Unlocking foreign exchange resources from the Diaspora;
- Curbing foreign exchange leakages in the economy;
- Removal of price distortions and conclusion of a Social Contract binding Government, business and labour;
- Enhancing agricultural production to ensure food security;
- Promotion of mining and tourism development;
- Supporting import substitution, value addition, toll manufacturing and SME development;
- Enhancing infrastructure development;
- Strengthening and streamlining National Social Protection Safety Nets and Programmes; and
- Supportive Parastatal and Local Authorities structural reforms.

149. Central to fiscal and monetary policies complementarity will be the targeting of money supply growth to levels consistent with inflation targets, guided by a

consistent monetary policy targeting framework, with quasi-fiscal expenditures curtailed and provided for in the fiscal budget. This will require us to ring-fence the existing stock of quasi-fiscal expenditures and confine them.

150. Experiences elsewhere have demonstrated that policy reversals and the abandonment of policy initiatives mid-stream, only serve to defer and magnify the level of pain endured in the implementation of the necessary corrective policy measures.
151. Piecemeal approaches and half-hearted implementation of critical policies will not deliver. The need for a credible and consistent Macro-economic Policy Framework aimed at reducing inflation and realising macro-economic stability cannot therefore be over-emphasised.

### **Macro-Economic Policy Framework**

152. The Macro-Economic Framework for 2007 consistent with the restoration of macro-economic stability will include the following:

- Fiscal consolidation characterised by an increase in the proportion of the Capital Budget to 24.4% of expenditures and lowering the Budget Deficit (excluding interest) to 17.6% of GDP.
- A dis-inflation programme targeted at reducing inflation from current four digit levels to 350-400% by December 2007 and subsequently to under 10% by December 2008.
- Reflecting all quasi-fiscal expenditures in the 2006 Budget.
- Phased amortisation of the quasi fiscal outlays through the fiscal Budget over three years starting in 2007.
- Phasing out quasi-fiscal activities and allocating all Government expenditures through the Budget.
- The promotion of a more intimate complementarity between fiscal and monetary policies.



- Support of interventions that free up the supply side of the economy from price distortions which in the past have undermined economic growth.
- Real GDP growth target of between 0.5% to 1% in 2007.
- Removal of distortions in the foreign exchange, fuel and other commodities markets which will be part of the process towards the elimination of parallel market activities.
- Stabilising incomes and prices under the auspices of the Incomes and Pricing Commission, supported by a Social Contract.
- Strengthening and streamlining Government's Social Safety Nets Programmes targeting the vulnerable.

### **Budget Framework for 2007**

153. Mr Speaker Sir, the Budget Framework for 2007 is premised on the following assumptions:

- Inflation target of 350-400% by December 2007;
- A real GDP growth of up to 1% and the respective nominal GDP level of \$8.5 trillion;
- Budget Deficit of 17.6% of GDP excluding interest;
- Budget revenues targeted at 35.3% of GDP, implying revenues of \$3.0 trillion;
- 2007 expenditure target of \$4.6 trillion excluding interest;
- Provision of \$100 billion for the phased amortisation of quasi-fiscal operations;
- Targeting Capital Budget to 24.4% of total expenditures or \$1.5 trillion and in line with the NEDPP objectives, prioritise the completion of ongoing projects.

154. The 2007 Budget Framework is therefore premised on the economy's capacity to finance Government expenditures, and provides an overall envelope of \$6.2 trillion. This is also consistent with an inflation target of 350 – 400% by

December 2007. Failure to contain expenditures within the economy's financial resource capacity would entail higher inflation, compromising prospects for economic recovery and growth.

### **Monetary Targeting Framework**

155. In order to achieve the inflation targets in the Budget Framework, it is imperative that greater focus be placed on the containment of monetary expansion, complemented by consistent and mutually agreed mechanisms of determining prices and incomes.

156. Pursuant to this, Treasury and the Central Bank have agreed on a new Monetary Targeting Framework, under a dis-inflation programme.

#### *Monetary Policy Anchor*

157. Under this dis-inflation programme, Treasury and the Reserve Bank have agreed on the targets for annual money supply growth consistent with the reduction in inflation. The Reserve Bank is therefore expected to meet the following annual money supply growth and inflation targets:

**Table 1: Annual Money Supply Growth and Inflation Targets**

|               | <b>Money Supply Growth</b> | <b>Inflation</b> |
|---------------|----------------------------|------------------|
| December 2007 | 415-500%                   | 350-400%         |
| December 2008 | under 65%                  | Under 10%        |

158. In order to support the Reserve Bank achieve these monetary anchor targets, Government borrowing requirements will be met from resources outside the Reserve Bank, and no Government Ministry, Department, Parastatal or Local Authority will seek funding directly from the Reserve Bank. Hence, all such funding requests to the Reserve Bank, more so when such expenditures are not reflected in the National Budget, will be rejected.

159. Similarly, Treasury will stay within its statutory limits and will only borrow should the eventuality arise.

160. To this end, the Reserve Bank will deepen its liquidity management interventions, supported by the phasing out of its quasi-fiscal operations from January 2007, with those directly related to price distortions and Government operations being transferred to the fiscal Budget.

#### *Quasi-Fiscal Expenditures*

161. Quasi-fiscal expenditure interventions by the Reserve Bank on behalf of the fiscus will be regularised through the Budget by absorbing, on a phased basis, amounts due from Government. These components of the quasi-fiscal outlays will be amortised through the fiscal Budget over the next three fiscal Budgets.
162. I therefore propose to allocate \$100 billion under the 2007 Budget towards the repayment of some of our quasi-fiscal outlays that were effected by the Reserve Bank in support of Government programmes. This is in line with our Monetary Targeting Framework, as well as the realisation of transparency in accounting for all Government expenditures in totality.
163. Mr Speaker Sir, let me point out that of the total quasi-fiscal outlays, not all of the obligations will be transferred to the fiscus. Quasi-fiscal expenditures related to allocations made to farmers, private sector companies, Public Enterprises and Local Authorities will be recovered from the beneficiaries of these outlays.
164. In this regard, a Technical Committee comprising Treasury, Ministry of Economic Development and the Reserve Bank has been set up to follow up on these outlays to ensure that the beneficiaries repay the facilities availed.

#### *Pricing Practices*

165. The realisation of the inflation and growth targets implied under the above Macroeconomic and Budget frameworks will not be without pain. The support of business, labour and other stakeholders, underpinned by a mutually Shared National Vision remains critical for success.
166. In its absence, mistrust among stakeholders prevails. At the same time, widespread speculative practices by producers underpinned by high inflationary

expectations and indexation aligned to parallel market activities are perpetuated and drive inflation higher.

167. Clearly, Mr Speaker Sir, such practices are largely driven by self interest, devoid of any commitment to a common Vision.

168. This often prompts ill-timed and often contradictory policy pronouncements and decisions which, not only impact negatively on confidence, but also increases uncertainty among economic agents. A notable example would be resorting to the re-introduction of unsustainable price controls which, however, can only worsen the supply situation.

169. This makes it vital that we develop consensus over pricing frameworks, under which the practices of enterprises are rooted. This should be supported by ethical and prudent business behaviour.

#### *Incomes Determination*

170. It will also be necessary that we extend this consensus to influence expectations that guide the determination of Incomes, by ensuring that all stakeholders participate in sharing the costs and benefits involved in the quest for the recovery of our economy.

171. Mr Speaker Sir, I therefore propose the development of mechanisms covering the determination of both prices of goods and services and incomes of workers. Under this, trigger mechanism arrangements, as well as frequency of prices and incomes adjustments, would be mutually agreed upon under the auspices of a Prices and Incomes Stabilisation Programme. I accordingly propose to set aside an amount of \$715.6 million for the set up and operational expenses for the programmes.

#### **Productive Sectors Support**

172. Mr Speaker Sir, I have also made reference to the positive correlation between improved supply side response and a reduction in inflation. In this regard, over and above the factors highlighted in the foregoing, it is imperative that the 2007 Budget incorporates measures to support the productive sectors of the economy.

173. Cognisant of this, Government remains committed to supporting improved capacity utilisation in the productive sectors of the economy. Targeted sectors include agriculture, manufacturing, mining and tourism.

*Agricultural Finance*

174. Mr Speaker Sir, Honourable Members will be aware that the backbone of financial support to agriculture, following our implementation of the Land Reform Programme, has remained with Government, directly through the Budget, as well as under the Reserve Bank's Agricultural Sector Performance Enhancement Facility.
175. I have already alluded to the \$76.7 billion agricultural support in 2006 under the Reserve Bank's ASPEF window, which is part of our quasi-fiscal expenditures through the Reserve Bank. Direct 2006 Budget disbursements in support of improving production in the agricultural sector totalled \$40 billion.
176. This includes \$2.4 billion availed for the tobacco crop and \$14.2 billion for the 2006/07 summer crop.
177. Government, however, has no capacity to meet the total financing requirements of the agricultural sector. Government will continue to play its part, and expects greater involvement of the private sector including the banking community. Historically, the banking community has funded the operations of commercial farmers.
178. Under the auspices of the National Economic Development Priority Programme, the private sector is being encouraged to go into the production of their requirements of feedstock for processing such as wheat and soya bean. I would like to challenge the private sector to fully participate in this programme in the forthcoming season.
179. Mr Speaker Sir, the banking community had raised concern with security of tenure as a major factor limiting its capacity to support farmers. The issuance of 99 year leases to some of the A2 farmers by His Excellency the President on November 9, 2006 should allay these fears, and introduce an environment conducive for banking sector involvement in the financing of agriculture. Already,

275 of the first 346 applicant A2 farmers to the Land Board have become the first beneficiaries of 99 year leases.

180. Mr Speaker Sir, 99 year leases guarantee beneficiaries possession of the farms for the next 99 years. A2 farmers' payment for improvements made by previous owners, including those they also make, enhances the available collateral for borrowing from banks and other lenders.
181. Mr Speaker Sir, the 99 year leases can be registered with the Deeds Office as in the case of title deeds, thereby enabling banks to recoup their money from the lessee or any other person to whom the lease might be transferred. The land, however, remains State property and can only be transferred with the consent of the State.
182. A1 model farmers will also soon be assured of security of tenure through the issuance of usufruct permits, which give the legal right to use and derive benefit from State land.
183. Mr Speaker Sir, these provisions make the lease agreement the ultimate security of tenure as provided for by our Laws. Hence, the 2007 Budget support to agriculture takes account of banks' increased participation through the re-introduction and opening of facilities and windows closed due to fears over security of tenure from the onset of the Land Reform Programme. The mobilisation of resources through the banking sector will be under the guidance of the Reserve Bank.

*Extension & Irrigation Rehabilitation & Development*

184. Mr Speaker Sir, the above arrangements should allow Government to focus its interventions at rigorous extension support, rehabilitation and development of irrigation infrastructure. I, therefore, propose to allocate a total of \$46.6 billion in support of mobility and operational expenses of AREX, Veterinary and Agricultural Engineering. I also propose to allocate an amount of \$6.2 billion for agricultural training through various Agricultural Colleges falling under the Department of Agricultural Education.
185. Mr Speaker Sir, I further propose an allocation of \$33.8 billion targeted towards irrigation rehabilitation and development.

186. I am further proposing a Budget provision of \$60.2 billion for Agricultural support with respect to grain, tobacco, and livestock production for the 2006/07 season, the 2007 winter wheat crop and the requirement of the earlier part of the 2007/08 agricultural season. This intervention will augment ASPEF resources.

#### *Viability of Agriculture*

187. Mr Speaker Sir, ensuring that the farmer positively responds to all this support necessitates our full appreciation of the other constraints in agriculture. Some of the constraints evolve around creating the environment for the sustainable viability of the producer.
188. Government will, therefore, timeously monitor and review agricultural producer prices, balancing this against changes in costs of production and reasonable rates of return for the farmer.

#### *Farmer Organisations*

189. Furthermore, it is important that we support and utilise the expertise of farmer organisations under the Agrarian Land Reform Programme, especially in the distribution of inputs and exchange of farming skills and experiences.
190. The Ministry of Agriculture is urged to support and build capacity of registered farmer organisations. This should enable farmer organisations to be more effective and to add value to the farmer. The disbursement details will be given in due course.

#### *Mining*

191. Mr Speaker Sir, Government needs to support the mining industry take advantage of the firm demand and prices of minerals on the international market. Most critical would be the efforts to address the high costs of production affecting the viability of the sector.

192. Recognising the mining sector as a major source of inputs for our manufacturing sector and an earner of foreign exchange, it is necessary that we begin to increase our interventions in the sector along the same lines as in agriculture. Inadequate support has meant that such facilities as the Mining Industry Loan Fund remain quite under-capitalised to the extent that it fails to make any meaningful impact on the sector. I therefore propose to allocate \$2.1 billion to the Mining Industry Loan Fund.
193. It is also critical that the relevant mining authorities always have properly coordinated early response mechanisms to deal with situations of illegal activities that undermine the realisation of foreign exchange.
194. Notable examples include the protection of deposits of diamonds and other precious minerals currently under siege from illegal miners in the Marange area.
195. To curtail leakages of minerals and to harness foreign currency earnings from the mining sector, I propose that, with immediate effect, all unregistered small scale mining operations be registered with the Ministry of Mines and Mining Development and all major mining zones declared 'protected areas' manned by security forces.
196. I, therefore, welcome the measures taken to ring-fence and protect the Marange diamonds deposit, which include support for improved technical expertise in diamond evaluation and putting up security structures in the area.
197. The capacity of the Ministry of Mines and Mining Development is set to be enhanced given the allocation I hereby propose an allocation of \$4.9 billion, for acquisition of technical equipment and operational mobility of the technical departments of the Ministry.

#### *Tourism*

198. Mr Speaker Sir, the tourism sector which is facing challenges ranging from negative portrayals of the country, to erratic fuel supplies, has been identified under the NEDPP as one of the sectors with a quick turnaround potential. In support, Government is upgrading and improving key infrastructure facilities such as airports and dry-land border posts, among others.



199. Furthermore, Government is supporting initiatives by the tourism industry for the rehabilitation of our tourist facilities, as well as ensuring sustainable energy supplies. I am therefore proposing to allocate \$10.4 billion for the completion of various tourism infrastructure projects in the Gonarezhou Trans-frontier Park.
200. Meanwhile, the Zimbabwe Tourism Authority is finalising details of establishing a Tourism Development Fund to support all critical tourism projects.

*Value Addition & Import Substitution*

201. Mr Speaker Sir, Government acknowledges the challenges that continue to hamper capacity utilisation in the manufacturing sector, resulting in the non-availability of some commodities on the market. Hence, our interventions and strategies also need to target the sector along the same lines as in agriculture.
202. Mr Speaker Sir, our interventions have focused firstly on capacitating companies to increase output. This should reverse some of the situations where capacity utilisation in industries had severely declined, consequently creating huge import demand pressures for commodities that could actually be produced locally.
203. Secondly, Government is supporting the re-orientation of our industries' production patterns through promoting value addition and processing raw materials into finished goods in order to increase export realisations.
204. This is being complemented by support for companies that, where applicable, capitalise on excess capacity by entering into toll manufacturing arrangements. Already, there are nine companies that are engaging in toll manufacturing at various levels, with another nine ready to start. These are benefiting from support from the Reserve Bank, as well as ZIMRA concessions on the operation of bonded warehouses for the imported raw materials.
205. Facilities already in place, and which require further support, include the resuscitation of distressed companies, of which a concessionary \$5 billion Fund is being managed by the Infrastructure Development Bank.
206. Mr Speaker Sir, of these resources, disbursements have gone smoothly with \$3.3 billion having been drawn down as of end of October 2006. Through this

intervention, 23 firms mainly in the manufacturing and export sectors were bailed out resulting in 10 000 jobs being saved. Applications for the remaining \$1.7 billion are at various stages of consideration.

207. Budget support for distressed companies can, however, only be a short term phenomenon. We will, therefore need to take measures to improve the business trading environment through addressing factors causing financial distress and affecting the viability of industry. Central is the improvement in the macro-economic environment characterised by low inflation and stable interest rates.
208. Furthermore, the 2006 Budget availed \$500 million to the Infrastructure Development Bank to establish the Import Substitution and Value Addition Fund. In this regard, 15 projects in agriculture, manufacturing, mining and tourism have been initiated and are at various stages of implementation.
209. I am, therefore, proposing additional financial support for Import Substitution and Value Addition Programmes amounting to \$6.8 billion in the 2007 Budget.
210. Such financial support should be complemented by policies that promote investment, Value Addition and Import Substitution, as well as the continued viability of exporting and the removal of other distortions undermining sustainable business activity.

### *Energy Supply*

211. Mr Speaker Sir, the difficult foreign exchange environment makes it necessary that we maximise the limited foreign exchange we have through better coordination of fuel procurement.
212. Currently, there are too many individual fuel importers. Such a situation is eroding the benefits of centralised bulk procurement and increasing the cost of procurement through the use of road transportation, instead of the pipeline. This is also causing serious damage to the road network. These high transport costs are ultimately being passed on to the consumer.
213. Our efforts to maximise on fuel procurement should be complemented by further support for the development of alternative sources of energy, such as bio-diesel, ethanol, solar, wind, etc. Already, a Solar Energy Policy document is in place. I

will therefore be providing resources to support the commercialisation of these projects, some of which are being undertaken to by our technical colleges.

214. With regards to electricity generation and supply, appropriate pricing structures still remain to be put in place. An Inter-Ministerial Committee has been established to look into the pricing structure of electricity.

### **Price Distortions**

215. Mr Speaker Sir, the removal of price distortions in the economy is critical to improving the operational environment for the business sector, guaranteeing their viability and the sustainability of production and achieving macro-economic stability.

216. In such a dynamic macro-economic environment, Government is closely monitoring the emergence of price distortions and undertaking regular corrective review of prices and marketing arrangements.

### *Grain Selling Prices*

217. Consistent with this, Government recently reviewed the producer prices for maize and wheat to \$52 450.30 and \$217 913.40 per tonne, respectively in order to guarantee the viability of farmers. This is being followed up by corresponding review of the GMB maize and wheat selling prices to millers, already approved by Cabinet.

218. Details of the new maize and wheat selling prices to millers will be announced by the Minister responsible for Agriculture, following the normal stakeholder consultations.

219. The implied subsidies per tonne of \$51 400 for maize and \$204 700 for wheat, at the current GMB selling prices of \$600 and \$12 300 respectively, distort consumption patterns and create room and opportunities for speculative and rent-seeking behaviour.

220. Given the prevailing GMB selling prices of maize and wheat to millers, the overall subsidy for this year's maize and wheat crops would amount to \$26 billion and

\$53 billion, respectively. These amounts had to be borne out of the 2006 Budget and the Reserve Bank. Such levels of untargeted and wholesale subsidies undermine the capacity of the Budget to intervene in other critical areas.

221. It is only through the removal of the existing mismatch between the buying and selling prices of these commodities that the requirements of this nature can be shifted away from the fiscus. I am confident, Mr Speaker Sir, that this can be avoided in 2007 by the adoption of prices that guarantee the viability of farmers and ensuring the ability of the Grain Marketing Board to finance and maintain the Strategic Grain Reserve.

222. I propose to set aside \$70 billion to meet the funding gap that may arise for payments to grain producers.

#### *Fuel*

223. The fuel market remains characterised by different prices for liquid petroleum products, notwithstanding recent efforts to unify petrol and diesel prices. This has perpetuated rent seeking behaviour in the pricing of fuel products, with some of the cheaper NOCZIM fuel ending up being resold at a premium on the parallel market by those able to access it.

224. The removal of the distortions inherent in the above arrangement therefore necessitates that bold measures be taken to unify fuel prices. This should be supported by ensuring that those able to utilise free funds to import fuel are permitted to do so at a reasonable return. Further, review of fuel prices should be in line with the already agreed price trigger mechanism arrangements.

225. Mr Speaker Sir, Government has made strides towards the production of alternative sources of fuel. I propose to allocate resources amounting to \$10 billion for further capitalisation and operational expenses of the development of bio-diesel and liquid fuel from coal. Thereafter the two projects will be financed through private sector investments since they are commercial by their nature.

#### *Local Authority & Public Enterprise Tariffs*

226. Mr Speaker Sir, price distortions, alongside mismanagement, poor corporate governance and an inadequate legal framework, are also contributing to the serious deterioration in Local Authorities and Public Enterprises' service delivery.
227. In the absence of Budget capacity to provide for the revenue shortfalls, delivery of such basic services as water, energy, sewerage waste management, refuse collection and infrastructure maintenance of roads, traffic lights and public lighting can no longer be taken for granted.
228. This has left some Local Authorities and such Parastatals as ZINWA in situations where they continuously call on the fiscus and the Reserve Bank to support procurement of daily consumables such as chemicals for water purification, as well as meeting their salary obligations.
229. Cognisant of this, measures are being instituted to address the anomaly under which the cash recoveries from the delivery of services by Local Authorities remain inadequate to cover costs.
230. This is covering the review of pricing structures for rates, water, electricity and other tariffs in line with inflation developments, to augment the economic and efficient operation of Local Authorities and Public Enterprises.

## **Foreign Exchange Generation**

### *Ring-fencing Export Generating Sectors*

231. Mr Speaker Sir, the experience over the past few years has amply demonstrated the need for a vibrant exporting sector in supporting the turnaround programme.
232. Inherent in the prevailing multiple export support arrangements is failure to fully and consistently compensate all earners of foreign exchange for rising domestic production costs. In this environment, generating additional foreign exchange remains one of the biggest challenges to economic recovery.
233. Against this background, Government remains alert to the loss of exporter viability caused by the continued rise in the costs of production, necessitating

urgent need to ring-fence export generating sectors. These sectors include manufacturing, mining, tourism, tobacco, horticulture and cotton.

234. Hence, Mr Speaker Sir, the Reserve Bank will implement an exchange rate framework that converges the existing duality in the foreign exchange market, through a combination of rapid dis-inflation and fair compensation to exporters and other generators of foreign exchange.

235. The Reserve Bank Governor will unveil the exchange rate framework, in his forthcoming Monetary Policy Statement.

#### *Non-resident Remittances*

236. Mr Speaker Sir, the Reserve Bank has already identified Non-Resident Remittances as an important potential source of foreign exchange if properly managed through schemes supported by fiscal and monetary incentives.

237. Appropriate supportive measures, targeted at supporting investment and other foreign exchange inflows from non-resident Zimbabweans, are also going to be unveiled by the Governor in due course. These will be reviewed regularly.

#### *Strategic Partnerships*

238. The injection of foreign exchange into the economy will materially enhance economic recovery prospects. Such an injection would allow for foreign exchange reserves build up and enable the country to begin to deal with its external payment arrears, putting the country firmly on the path to restoring its credit worthiness.

239. Mr Speaker Sir, last year, we identified strategic partnerships through the privatisation and commercialisation of a number of Public Enterprises, under some of our Look-East Policy initiatives, as a potential source of generating significant foreign exchange. High potential 'quick wins' include the National Railways of Zimbabwe, Tel-One and Net-One, Air Zimbabwe, and the Zimbabwe Iron and Steel Company.

240. Regrettably, Mr Speaker Sir, we have so far only been able to make minimal progress, if any. Moving forward with this process will require that we put in place a comprehensive framework with set targets and identify the potential enterprises and timeframes.

241. I will, therefore, be appraising Honourable Members on a regular basis on progress on the privatisation and strategic partnerships for the Parastatals.

### **Management of Public Enterprises**

242. Mr Speaker Sir, I have already raised the need for regular review of tariffs to economic levels, and embarking on strategic partnerships as part of the interventions to effectively deal with the inefficient operations of most Parastatals.

243. Over and above this, widespread cases of inefficient operations, inconsistent with our other efforts to reduce inflation and improving economic performance, will have to be addressed. Central to this would be the improved accountability of management and boards of Public Enterprises.

244. Mr Speaker Sir, respective Ministers have played a part in the prevailing operational inefficiencies of some Public Enterprises. On one extreme, is routine interference which undermines the accountability of the governance structures implied under the various legislation establishing our Parastatals. On the other, are situations of abrogation on legislated responsibilities, paying no attention to the 'goings on' in the Parastatals we are supposed to supervise.

245. Cases where boards and management sit back in the midst of serious operational deficiencies while waiting for Government intervention bear testimony to this.

246. Most Parastatals continue to operate for years without any proper accounting systems, notwithstanding that each Minister responsible for a particular public enterprise is required to table annual audited accounts of the particular parastatal in Parliament at least six months after the end of each financial year. Furthermore, key Parastatals are also operating without boards and substantive chief executive officers.

247. Mr Speaker Sir, it is high time that management and boards are made accountable through performance agreements and accorded the space to run these Public Enterprises as viable commercial entities.

### **Environmental Sustainability**

248. Mr Speaker Sir, in my nationwide pre-Budget consultations, stakeholders raised concern that ineffective monitoring and enforcement of regulations on the protection of the environment has become a major threat to environmental sustainability.

249. Illegal mining activities such as gold and diamond panning, veld fires, rampant poaching, water bodies pollution by industries, improper cultivation practices, and wanton cutting of trees in the newly resettled areas were all cited as causing tremendous damage to our environment.

250. On timber estates, illegal occupations, often responsible for numerous large forest fires and the destruction of plantations, are also playing their part in rapid environmental degradation right under our noses. Furthermore, uncontrolled logging activities are also resulting in deforestation.

251. This is also viewed as contributing to the changes in the weather pattern, with the Southern regions of our country becoming drier as the rainfall levels decline with each passing season.

252. In this regard, the Budget is supporting the Environmental Management Agency, established as a successor to the Department of Natural Resources, mandated by Government to oversee the sustainability of the environment.

253. I therefore propose to allocate \$25.8 billion in order to enhance the capacity of the Agency to enforce environmental protection.

### **Social Service Delivery**

254. Mr Speaker Sir, the adequate provision of social services, at both Central and Local Government levels remains a priority for the Budget.



255. Hence, fiscal interventions to arrest and reverse some of the declining provision of basic services are necessary. Innovative financing strategies to broaden the sources of financing beyond Government also need to be explored.

#### *Health*

256. Mr Speaker Sir, the persistent high inflationary environment, coupled with the shortage of foreign currency and manpower, is compromising provision of quality health service to the people. Improvement in levels of funding for medical drugs and supplies as well as hospital and clinical equipment remains critical.

257. I therefore propose to allocate a sum of \$590.1 billion towards the public health delivery services. The amount proposed includes \$345.5 billion for funding of central hospitals and \$9 billion preventives programmes which include Immunisation, TB and Malaria. Employment costs constitute 14.5% of the proposed Vote allocation.

258. Development and rehabilitation of health service infrastructure, including clinics, mortuaries and equipment accounts for **\$39.7 billion**.

#### *Access to Education*

259. Mr Speaker Sir, it remains necessary that Government shares the direct costs of tertiary education with the beneficiaries. This also improves accountability among students in tertiary institutions, as well as ownership of the institutions' facilities.

260. Honourable Members would have noted the many instances where, surprisingly, even well endowed parents display inability to pay tertiary education fees when they were able to get their children through ordinary and advanced level education without State assistance.

261. Government has therefore put in place mechanisms that embrace means testing, for support to students under tertiary training institutions. Means testing will now draw input from school authorities, both primary and secondary to improve on reliability of assessments of students to be targeted.

262. Quality primary and secondary school education, a right of every child, appears to have been negatively affected by inadequate funding over the last few years. Through the Annual Budget and contribution of partners, including parents, it will be important that due attention is given to the revitalisation of the education system.
263. In this, the 2007 Budget, I propose to allocate an amount of \$7.6 billion in relation to tuition and learning materials at schools. This allocation will be disbursed on the basis of improved per capita rates.
264. Mr Speaker Sir, I also propose to allocate an amount of \$4.0 billion for the maintenance of schools in rural areas, targeting at least four schools per District. In addition, I propose to allocate an amount of \$8.2 billion for the construction of schools, the objective being to phase out hot sitting in some schools as well as promote access to education by children in newly resettled areas.
265. To arrest the deterioration of assets and facilities at public institutions such as schools in rural areas, it has become necessary that we create a facility that enables access and quick disbursement of resources for minor repairs and maintenance. Government already operates a Building Grants facility to support and compliment efforts by communities and private organisations in constructing schools infrastructure.
266. I am aware that our communities fail to fully benefit from facilities of this nature that Government oftens puts in place due to lack of information on how they can access such facilities.
267. Mr Speaker Sir, I propose to allocate an amount of \$2 billion for minor repairs and maintenance through the Rural Capital Development Fund which is represented in our Rural Districts. In the case of schools, Schools Development Authorities/Committees can access the resources on the basis of written applications directly to the respective District Education Officers responsible for Buildings. The District Education Officers will be responsible for submissions to the Rural Capital Development Fund.
268. For support regarding construction of education facilities, I propose to allocate \$3 billion for facilities at both primary and secondary level. While administration of Building Grants remain with the Ministry of Education, Sport and Culture,

modalities for applying and accessing resources should change as proposed above.

269. Guided by the need to enhance supervisory capacity of the Ministry of Education, Sports and Culture, I propose to allocate an amount of \$6.0 billion to enable the Ministry procure vehicles for this purpose.

270. Mr Speaker Sir, for overall education delivery, the proposed allocation amounts to \$721.9 billion, out of which \$48.8 billion stands for administrative and teaching and learning expenses as well as capital transfers towards projects at State Universities.

### **Security**

271. Mr Speaker Sir, it remains critical, given global security developments, that we ensure adequate funding is availed for the maintenance of peace, law and order as well as security. To this end, I propose to allocate a sum of \$255.7 billion for recurrent expenses, excluding employment costs, and \$60.8 billion, for the Police, Army, Airforce and Prison Services.

272. Mr Speaker Sir, the Nation remains endeared to friendly countries, which remain in support of our efforts towards training and re-equipping our Forces.

### **Combating Indiscipline & Corruption**

273. Mr Speaker Sir, the stakes on the fight against indiscipline and corruption must be stepped up. We, therefore, have to set aside adequate resources in support of the institutions of Government responsible for fighting corruption and combating the rising prevalence of indiscipline in the economy. This is manifested through economic crime and rampant abuse of scarce public resources and other ills that threaten the very fabric of our society.

274. Over and above declaring war against indiscipline and corruption, the successful waging of this War will require that we also strengthen the laws and institutions dealing with economic crimes with a view to introducing harsher penalties, including the forfeiture of ill-gotten assets.

275. Pursuant to this, I propose to allocate funds towards supporting surveillance units with powers and skills to expose abuse of such assets as fuel, motor vehicles, subsidised grain, inputs, veterinary drugs, among others.

### **Public Service Conditions**

276. Mr. Speaker Sir, the availability of the critical human resource skills is central to public service delivery and implementation of public projects.

277. The erosion of real incomes in the prevailing high inflation environment has left Government with largely an unmotivated and poorly paid public servant.

278. Government continues to lose skilled manpower, trained at great cost in all the critical areas, including health, education and technical fields.

279. Mr Speaker Sir, it is therefore imperative that the 2007 Budget builds Government's capacity to retain and attract specialised and strategic skills, so as to capacitate institutional ability to fully implement National programmes.

280. In the prevailing hyperinflation environment, some of the necessary measures should include timely review of conditions of service, taking account of requests by the Public Service Associations for smaller but more periodic adjustments, as opposed to larger infrequent ones.

281. I propose that the review of the remuneration of civil servants be done on a quarterly basis in line with the inflationary developments in the economy. I therefore propose to set aside an envelope of \$1.4 trillion for the 2007 Public Services Employment Costs.

282. In order to ensure the attainment of quarterly adjustments in a manner that curtails inflation, Treasury will limit disbursements out of this envelope to an average \$40 billion per month, across the Public Services, during the first quarter of 2007. I therefore urge teams to the Public Service Joint Negotiating Council to be guided accordingly.

283. The significant provision, which represents a 1 205% growth over the 2006 provision, is motivated by the need to address the brain drain that is crippling the operations of Line Ministries hence the deterioration in service delivery. While this

resource envelope will not fully reverse the erosion of civil service incomes, the capacity of the economy to sustain the current civil service structure is the determining factor.

#### *Non-monetary Benefits*

284. Mr Speaker Sir, I have also taken note of the requests to augment non-monetary benefits of the civil servants, as part of the efforts to cushion them from the effects of the erosion of disposable incomes.

285. In this regard, support for such non-monetary benefits as access to housing and transport, will facilitate the provision of decent accommodation and affordable transport for lowly remunerated public servants.

286. I, therefore, propose to allocate \$3 billion towards the expansion of the Public Service Housing Loan Scheme.

287. I also propose to allocate \$852 million towards the Civil Servants Vehicle Loan Scheme.

#### *Skills Retention*

288. Mr Speaker Sir, notwithstanding the above Budget provisions to cushion civil servants through the review of conditions of service during 2007, additional intervention measures are still necessary to curtail further loss of skills.

289. Honourable Members will agree with me and acknowledge that the ultimate solution remains stabilising the macro-economic environment and realising sustainable growth.

290. In the transition, however, further Budget support for the Skills Retention Fund should go someway towards alleviating the brain-drain in some of the critical areas of the public sector.

291. Hence, I propose to allocate \$5.5 billion to the recently launched Skills Retention Fund for the benefit of targeted critical skills in the Public Service. This will allow

scope for the provision of premiums to be paid to expertise in key posts and professions. The funding requirement for this initiative is much higher and, to this end, Government will solicit for contributions from friendly cooperating partners.

### **Pension Reform**

292. Mr Speaker Sir, I have previously alerted the House that we also have a serious and growing pension payments.

293. The resources being raised from the contributions of serving members is inadequate to cover retirees' pension payments. This has limited our capacity to fully index to two thirds of a serving member's current salary. A sustainable arrangement would be the introduction of a Defined Contribution Pension Fund Scheme.

294. Mr Speaker Sir, beginning January 1 2007, all the pension deductions will be set aside for the establishment of the above Fund as a prelude to this. We still, however, need to provide funds to meet due pensions under Constitutional and Statutory appropriations.

### **Housing Delivery**

295. Mr Speaker Sir, housing is a basic necessity which can empower and enhance the social security of households, as well as stimulate our construction and other related sectors.

296. However, with average small stands costing anything above \$3.5 million, and a three bed-roomed house in the high density area costing around \$30 million, it is becoming increasingly unaffordable for the average family to purchase property.

297. In this environment, it becomes necessary that Government prioritises the mobilisation of both public and private capital for national housing over the coming years in conjunction with other stakeholders, including the private sector. This will also move resources away from speculative ventures and direct investment into the real sector, thereby stimulating growth of the economy.

298. Consultations with the insurance and pension industry have identified the use of indexed financial instruments to allow pension funds to invest in prescribed assets that will facilitate investment into housing, affordable to workers.
299. I will expect our National Social Security Authority to play a significant role in the provision of affordable houses to the workers.
300. Mr Speaker Sir, in support of this innovative way to attract capital into the housing market and broaden access to property ownership, Government is reviewing the relevant legislative framework, in consultation with the Insurance and Pension Funds.

### **Social Protection**

301. Mr Speaker Sir, stakeholder consultations also raised concern that the less vocal groups, who include the poorest, remain marginalised in the allocation of public resources, notwithstanding their level of vulnerability to the prevailing economic hardships.
302. Mr Speaker Sir, recent poverty assessments indicate increased levels of vulnerability in the country, especially among the marginalised groups who require both social protection and empowerment. In the case of children, it is estimated that there are over 1 500 000 orphaned and vulnerable children that are in need of protection.

#### *Targeting Social Protection*

303. The high incidences of poverty and vulnerability require that we strengthen and streamline our National Social Protection Safety Nets and Programmes. There is need to target the vulnerable groups, focussing transfers to the elderly, orphans, and the physically challenged. Public works programmes in both urban and rural areas will be targeted at the unemployed and able-bodied.

#### *Social Welfare*

304. Mr Speaker Sir, in order to cushion the elderly and physically challenged members of our society against rising inflation, I am proposing to review upwards the protection rates currently ranging between \$60 and \$250 per month.

305. I therefore propose in the 2007 Budget to increase the allocation to support Social Protection Programmes. This allocation also allows for the review of the current protection rates, ranging from \$60 to \$250 per month, taking account of the changes in inflation.

306. I further propose to allocate \$18.7 billion towards the administration of social protection programmes, including provision of transport to facilitate mobility.

#### *Basic Education Assistance Module*

307. Mr Speaker Sir, over and above other social protection requirements, orphaned and vulnerable children of school-going age also require social protection through such programmes as the Basic Education Assistance Module (BEAM). I therefore propose to allocate \$5.5 billion. for education assistance programmes.

308. It will also be critical that the Department of Social Services undertakes the necessary awareness campaigns of such protection programmes as BEAM, especially in rural areas.

#### *People Living with HIV/AIDS*

309. Mr Speaker Sir, the estimated over 600 000 people living with HIV/AIDS also face many challenges. These include financial difficulties to purchase anti-retro viral drugs (ARVs) which remain beyond the reach of many.

310. This is in spite of efforts to make them more affordable through support for local production initiatives by some of our pharmaceutical companies. Those able to access ARVs face the added challenge of sustaining the commensurate nutritional requirements.



311. Government has therefore, targeted resources under the 3% AIDS levy towards supporting our people living with HIV/AIDS under the coordination of the National AIDS Council.
312. I therefore propose to maintain the 3% AIDS levy in support of members of our society living with HIV/AIDS.
313. While concerns that a disproportionate share of these resources is being spent on administration, rather than supporting people living with HIV/AIDS, are being addressed by the Ministry of Health and Child Welfare, I propose that, with immediate effect, at least 70% of the collections under the AIDS Levy be earmarked for the purchase of Anti-retroviral drugs.

#### *Public Works Programmes*

314. Mr Speaker Sir, I have already made reference to the need to avoid direct cash transfer interventions, whether non-conditional or conditional, to those members of our society who remain able-bodied.
315. This stance by Government has seen us in the past support budget allocations for social protection in years of wider scale vulnerability, such as during a drought, through such public works programmes as 'food or money for work'. Consistent with this, I propose to allocate \$1.2 billion towards public works programmes during 2007.

#### **Empowerment**

316. Mr. Speaker Sir, in the prevailing environment of hyper-inflation and declining economic activity, the numbers of the unemployed groups continues to swell.
317. This, over and above social alleviation interventions, necessitates further Government support for income and employment generating programmes targeted at empowering the youth, women, and the poor, among others. These empowerment programmes should also mainstream disability, through support for the physically challenged.

318. The need to support empowerment programmes is also in recognition of communities as hubs of employment creation and income generation through various community based programmes and projects. Hence, these require continued support in line with the poverty reduction thrust of the Millennium Development Goals.

#### *Youth Fund*

319. Youths constitute 67% of our population, with around 400 000 leaving schools every year. The formal sector absorbs only 10% of these school leavers, resulting in a large number being unemployed.

320. Having realised the employment creation and income generating potential, Government through the Infrastructure Development Bank has set up a Youth Development Fund to avail capital to those projects that have been identified as highly productive.

321. I therefore propose to allocate \$10 million as an additional capital injection into the Youth Development Fund administered by the Ministry of Youth Development and Employment Creation through the Infrastructure Development Bank.

#### *Mainstreaming Disability in Budgeting*

322. Mr Speaker Sir, I have already alluded to the need for an all embracing empowerment strategy, with programmes also targeted at the physically challenged members of our communities. This is in recognition of the fact that disability should never be viewed as inability, and hence the need for charity. This results in the marginalisation of the physically challenged.

323. Empowering the physically challenged remains a socio-economic development challenge in our economy. As such, our development programmes should mainstream disability, and also target at empowering this group.

324. I therefore propose to allocate \$1.0 billion towards supporting income and employment generating projects of the physically challenged.

### *Small & Medium Enterprises*

325. Mr Speaker Sir, the role of Small to Medium Enterprises (SMEs) in inculcating entrepreneurship skills, employment creation and poverty alleviation, as well as foreign currency generation, is recognised worldwide. SMEs have played a significant role in sustaining India's high growth rates.
326. Supporting the development of SMEs is part of our economic development strategy. SMEs play a critical role in the beneficiation of local raw materials, and are an important tool for our empowerment and indigenisation programmes. They also play a significant role in ensuring the participation of women in the mainstream of our economy.
327. The graduation of many informal businesses into formal SMEs provides greater scope for access to formal banking lending programmes. In this regard, allow me to recognise the efforts of the Reserve Bank in coordinating the overall banking and financial sector to support initiatives targeted at the development of SMEs.
328. Already, many of our banking institutions have established dedicated units that offer financial support to SMEs. Financial support to SMEs is receiving a boost from resources being availed under the recently launched concessionary \$16 billion Reserve Bank facility for on-lending by banks to SMEs.
329. Mr Speaker Sir, urban based SMEs have taken greater advantage of this financial sector support, necessitating Budget intervention largely targeted at the rural areas as well. Already, through the 2006 Budget, I provided \$200 million in support of SMEs in rural areas through SEDCO under our Growth Points Resuscitation Programme (GPRP).
330. Mr Speaker Sir, notwithstanding that the Small Enterprise Development Corporation (SEDCO) was established by Government to spearhead the development of SMEs through provision of business loans and business development services, it has been failing to fulfil this mandate partly as a result of under-capitalisation.
331. While the corporation has supported some SMEs across all sectors of the economy in both rural and urban centres with 80% recovery rates, critical micro

lending programmes have remained under-funded. I, therefore, propose to provide \$54.3 billion towards the recapitalisation of SEDCO.

332. These resources will support the following programmes:

**Table 2: SEDCO Support Facilities and Programmes**

| <b>Programme / Facility</b>          | <b>Amount</b> |
|--------------------------------------|---------------|
| Lending                              | \$40 billion  |
| Business Infrastructure Development  | \$8 billion   |
| Capacity Building                    | \$0.8 million |
| Integrated Skills Outreach Programme | \$3 billion   |
| Capital Expenditure                  | \$1.5 billion |
| Work Related Programme               | \$1 billion   |

333. Successful utilisation of these resources through ventures in agro-based and other manufacturing activities should reduce the prevailing rural-urban migration pressure, as formal job market opportunities also arise at growth points and rural service centres. Surveys undertaken so far indicate successful inroads into milling, soap production, fence making, hardware supplies, furniture making and other activities.

334. Mr Speaker Sir, the provision of resources to rural based SMEs will contribute to increased economic activity in rural areas. This also enhances the scope for upgrading the existing infrastructure such as rural road networks, electricity, water, housing, schools and health care facilities.

### **Accountability over Public Resources**

335. Mr Speaker Sir, limited Budget resources warrant strengthening systems of accountability over the efficient and effective use of public funds and property.

336. Honourable Members will be aware that Ministries and Departments, as well as our Local Authorities and Public Enterprises are often vocal in their references to inadequate provision and access to budgetary and other scarce public resources.

337. Mr Speaker Sir, we all aware that our economy is under siege. This calls for the efficient use of the scarce domestic and foreign resources. We also need to fully

account for the use of these resources in a transparent manner and to avoid the abuse of such resources. This is critical to our economic survival as a Nation under sanctions.

338. Mr Speaker Sir, we cannot therefore continue operating in our 'business as usual' manner, tolerating wasteful use of resources, and imprudence in the utilisation of the scarce public resources. This, Honourable Members, can only worsen our economic situation and exacerbate inflation.

339. Dealing with inefficiencies in the utilisation of public resources and assets, requires the review of the financial management legal framework, and the introduction of penalties for non-compliance. I will, Mr Speaker Sir, therefore be proposing a new Public Finance Management Bill for the consideration of Honourable Members.

#### *Public Finance Management*

340. The proposed Public Finance Management legislation, once approved and assented to, will compel Ministries to take charge of their own accounts and produce their own reports, which would be tabled in Parliament. Furthermore, this will require them to produce financial reports for their respective Parastatals at the end of each financial period. This will improve accountability and enhance efficiency in the use of public resources.

#### *Audit*

341. It has also been observed that Government has not been producing audited financial statements, as line Ministries are failing to produce final accounts for the Comptroller & Auditor General's report.

342. I therefore also propose the introduction of the Audit Bill which seeks to improve accountability in the audit process, and eliminate the operational limitations inherent in the existing Audit & Exchequer Act.

#### **Institutions of Government**

343. Mr Speaker Sir, the successful formulation and implementation of Budget programmes critically depends on ensuring that Government institutions are operating efficiently and effectively.

344. The many instances where Memorandum of Understandings (M.O.U.s) are entered into and concluded by Ministries in the absence of proper coordination and due regard to established institutional processes are not conducive to the effective operations of Government.

345. Mr Speaker Sir, such behaviour by line Ministries which do not fully comply and recognise established institutional processes will not be tolerated anymore.

### **Operations & Maintenance**

346. Mr Speaker Sir, the 2007 Budget will also have to contend with the deteriorating public infrastructure, both in rural and urban areas. Major pressure areas relate to the rehabilitation of roads, bridges, dip tanks, schools, and health facilities, among others.

347. To sustain operations and maintenance requirements of Ministries and improve capacity to deliver essential services necessary for economic recovery, I propose to allocate a total amount of \$736.5 billion for operations and maintenance.

### *Maintenance*

348. Mr Speaker Sir, timely and adequate maintenance will be necessary if we are to benefit longer usage of the assets and infrastructure already acquired. To this end, there is need to ensure that funds are set aside for the maintenance of Government buildings, plant and equipment. I therefore propose the provision of \$69.3 billion for this purpose. The Ministries of Local Government, Public Works and Urban Development and that of Rural Housing and Social Amenities are jointly driving the maintenance programme.

### **Grants and Transfers**

349. I have made provision of \$329 billion for employment costs with respect to Grant Aided Institutions in line with adjustments assumed across the Civil Service.

350. Furthermore, I have also made provision of \$308 billion for operational expenses for these institutions.

#### *Street Children Fund*

351. Mr Speaker Sir, recognising the plight of children living on the streets, Government took the initiative to establish a Fund to act as a vehicle towards such children's rehabilitation and development.

352. I am happy to advise Honourable Members that all the steps necessary for the setting up of the Fund have been fulfilled. To this end, I propose to set aside an amount of \$1 billion as initial injection into the Fund. The Minister of Public Service, Labour and Social Welfare whose Ministry is charged with managing the Fund will lead further steps into the realisation of the objectives of the Fund.

#### **Capital Budget**

353. Mr Speaker Sir, stakeholders raised concern over the current structure of public expenditures, where infrastructure development is not sufficiently resourced to facilitate positive supply response. They cited the poor state of public infrastructure such as roads, incomplete dam projects, and other facilities.

354. Observations that the low Budget allocations for infrastructure projects have often been affected by the accommodation of previously unbudgeted recurrent expenditures were also made during these consultations. The little resources left for capital development are spread too thinly to make meaningful impact. This results in most Ministries being incapacitated to complete projects on time, undermining capital formation for economic growth and development.

355. This poses the challenge of increasing the capital budget and tightening controls on containing unplanned recurrent expenditure demands, some of which are not always related to emergencies and are often deferrable.

356. Mr Speaker Sir, in rationalising Ministries' expenditure bids, I indicated my proposal to avail \$1.5 trillion in support of the capital budget. This represents 24.4% of the overall expenditure level, in line with the Cabinet recommendation.

357. To avoid situations where allocations may not correspond to requirements to enable full project implementation, I have prioritised the completion of some on-going projects. This entails that some of the on-going projects will have to be postponed in order to redirect resources to those projects that are likely to be completed in 2007.

358. I have also availed \$8 billion to the Infrastructure Development Bank as part of its capitalisation.

#### *Road & Bridges Infrastructure*

359. Mr Speaker Sir, Government shares in the concerns of our people over the poor state of our road infrastructure. The deterioration in the roads infrastructure to a state where most is in need of rehabilitation is explained by the limited availability of equipment and the critical human resource skills coupled with the high cost of construction.

360. The unit costs for road maintenance activities range from \$2.255 million per kilometre to \$10.249 million for periodic resealing maintenance. In the case of road construction to surfaced standard, we need \$80 million per kilometre of road.

#### *Road Maintenance & Rehabilitation*

361. The funding requirement for our 2007 annual road maintenance programme is, therefore, estimated by the Zimbabwe National Road Administration (ZINARA) at \$24.1 billion. Programmed works include resealing a total of 385 kilometres at a cost of \$4 billion, re-gravelling 965 kilometres at a cost of \$10.3 billion and 385 kilometres of pothole patching at a cost of \$868 million. The balance of \$8 billion and \$1.1 billion relates to motorised grading routine maintenance, and grass cutting, respectively.



362. Honourable Members will be aware of the role of ZINARA in supporting the maintenance of both our trunk roads and recently, some of the major arteries into our towns and cities. ZINARA, which funds the Department of Roads, also finances roads for 59 Rural District Councils, 30 Urban Councils and the DDF network, thereby facilitating local authorities' road maintenance programmes through financial support.
363. Mr Speaker Sir, local authorities have at times failed to expeditiously utilise ZINARA road maintenance resources on account of lack of capacity to prepare programme of works documents as well as failure to account for prior disbursements.
364. In doing all this, ZINARA is currently funded through the 5% fuel levy collected on the landed import price of fuel. This, however, is now inadequate to support the extensive road maintenance programme facing us both for the trunk roads and the major arteries into the urban centres.
365. Through the 2007 Budget, Government would want all roads authorities to register some tangible progress in rehabilitation and development of the roads infrastructure.
366. I propose to allocate \$10 billion specifically targeted at pothole patching and resealing of some of the major roads in the residential areas of our cities and towns. This will also cover the main entry and exit access into our growth points.
367. With regards to the rural roads, I propose to allocate \$4 billion through the District Development Fund.
368. These budgetary resources will compliment the contributions coming through ZINARA.

#### *Rural Electrification*

369. Mr Speaker Sir, Honourable Members are aware of Government's establishment of the Rural Electrification Agency (REA) to spearhead rapid and equitable electrification of our rural areas through extending the electricity grid and promoting productive use of electricity in irrigation and cottage industries, thereby empowering rural communities.

370. While this was to be funded primarily through the 6% levy on all electricity consumers, the income from the levy has, however, remained inadequate for grid expansion. For 2007, the levy would raise only \$13.9 billion, against a requirement of \$128 billion to complete the targeted 1 000 projects. The overall backlog is 1 300 projects.
371. Furthermore, for the electricity end-use infrastructure development programme, four pilot schools milling projects carried out so far confirm that rural schools can engage in viable projects. Hence the Agency intends to develop 24 schools irrigation schemes and 58 schools milling projects at a cost \$5 billion during 2007.
372. I propose to allocate \$100.billion directly to village communities that want to take advantage of the electricity end-use infrastructure development by venturing into irrigation projects.
373. Given the huge resources required for the rural electrification programme and the projected deficit in domestic power generation, Government together with the private sector will vigorously promote the development of solar energy in the rural areas. The local manufacture of solar panels will be promoted through the provision of fiscal and monetary incentives.

#### *Telecommunications*

374. Mr Speaker Sir, increasing investment in mobile telecommunication across our urban, as well as expansion being made into our outlying rural areas, are enhancing access to communication and information throughout the country.
375. Further expansion in the next few years by the mobile networks should progressively raise the penetration rate of mobile phones to regional best practices of close to 50% of the population. New developments are set to see more base stations being put up, as the industry embraces the introduction of wireless and broadband internet access technology.
376. It is therefore critical that Government and cooperating partners support these expansion initiatives by the telecommunication industry, including the provision of foreign currency to import modern equipment and technology.

### *Water Projects*

377. Mr Speaker Sir, notwithstanding the fact that in per capita terms, we are among those countries with the largest water bodies, there are still many areas where we need to construct more dams, especially in light of the challenges over irrigation.

378. In this regard, ZINWA has approved the construction of new dams in support of irrigation.

379. However, owing to resource and other capacity constraints, it remains necessary that we prioritise the completion of ongoing dam construction projects before undertaking new ones.

380. I therefore propose to allocate \$127.1 billion for the following dams:

### *Public Private Partnerships*

381. Mr Speaker Sir, Government cannot finance the maintenance and development of all public infrastructure from its own resources. There is therefore need to involve the private sector in the development of infrastructure.

382. Embracing broader stakeholder participation in infrastructure development projects requires the finalisation of the legal and institutional framework for Public Private Partnerships (PPPs), as well as incentives and special dispensations for the private sector.

383. Government has already put in place operational guidelines which are meant to promote and facilitate the implementation of PPPs in infrastructure development. While a number of projects are under consideration, the overall implementation progress has been slow owing to the absence of effective institutional and legal arrangements among other factors.

384. The finalisation of the institutional and legal arrangements will facilitate quicker approvals, effective co-ordination, implementation and monitoring of all PPPs.

### **Called Up Guaranteed Loans**

385. Providing resources for non-performing called up guaranteed loans of Parastatals can only undermine the availability of resources for other critical budget requirements. With immediate effect, Parastatals will, therefore, be called upon to honour their loan obligations from their revenue.

## **2007 Budget Management**

386. Mr Speaker Sir, the Budget Estimates I am presenting are fairly large. It is therefore critical that Accounting Officers exercise due diligence in the management of resources placed under their stewardship.

387. In order to ensure that execution of this Budget is in a manner consistent with revenue inflows, budget releases by Treasury will adhere to the available cashflows. Where accountability is not demonstrated, budget releases will be withheld.

388. In the case of funds budgeted for acquisition of furniture, vehicles and equipment, releases shall be subject to recording of assets under the Public Finance Management system and production of reports thereof.

389. Line Ministries will also be expected not to embark on any expansion, but limit spending levels within budget provisions.

## **Public Procurement**

390. Timely completion of projects also requires tighter monitoring of programmes of Ministries in line with the principles of Results Based Budgeting. Delays in procurement and project implementation in an environment of high inflation ultimately leads to higher risks of increased costs and non-implementation.

391. Hence, ensuring that Government institutions are operating effectively, will require that we improve on the current delays related to our existing procurement systems and procedures.

392. In the interim, the tender value limits have been reviewed upwards as follows:

- For Competitive Quotations, from \$1 million to \$4 million;

- For Informal Tenders, from between \$1 - \$6 million to \$4 - \$20 million; and that
- Formal Tender procedures now only apply to all tenders above \$20 million.

### **Domestic Debt Restructuring**

393. The high budget deficits which have been financed mainly from domestic sources, have resulted in the accumulation of a huge and unsustainable public domestic debt overhang, which is currently close to \$153 billion or about 15% of GDP.
394. Over 98.5% of this is in the form of very short term Treasury Bill borrowings of less than one year maturity.
395. Such a debt structure calls for the restructuring of domestic debt and the adoption of Budget financing strategies which limit the rapid expansion of the debt.
396. In this regard, a programme to restructure domestic public debt is being put in place in order to minimise the debt service burden on the fiscus. This includes the restructuring of debt with a view to transforming the bulk of existing debt into medium to long term tenors. A critical requirement for this restructuring process would be the introduction of adequate instruments with prescribed asset status.
397. This will allow players in the Insurance and Pension Fund industry to meaningfully contribute to the debt restructuring programme.

### **Savings & Investment**

398. Savings are important for growth and prosperity because they provide a pool of investment capital for new and growing businesses. For the past six years, our savings and investment growth rates have remained below 10%. Such low levels cannot support the desired economic growth of between 5 – 7% consistent with the Millennium Development Goals.

399. Government has therefore prioritised the promotion of investment to sustain the above growth targets. However, the Zimbabwe Investment Centre and the Export Processing Zones Authority, which are mandated to promote investment are undergoing institutional re-organisation to enhance their capacity and focus.
400. Therefore the ongoing reforms that seek to amalgamate these institutions into a one stop centre, need to be buttressed together with a review of all inward investment approval procedures, so as to remove the administrative burden on applicants. The formation of the Zimbabwe Investment Authority will result in much more efficient approval processes and systems for inward investments.
401. Furthermore, in order to attract and give confidence to foreign investors, Government is fully committed to honouring all its international obligations under various protocols and international agreements including the Bilateral Investment Promotion & Protection Agreements (BIPPAs).

## VIII. REVENUE PROPOSALS

402. Mr Speaker Sir, I have already made reference to the need for us to relate the 2007 Budget expenditure allocations that I have announced to the capacity of our economy to finance them. This, Mr Speaker Sir, makes resort to new tax measures unavoidable.

403. The reliance on revenue is also in recognition of the reality that we are on our own, as foreign financing inflows have largely dried up.

404. Consistent with these submissions, the thrust of my tax proposals, Mr Speaker Sir, are broadly focused on the following:

- targeting taxation at consumptive activities, rather than on production;
- supporting the productive and export sectors;
- enhancing disposable income in the hands of the taxpayer, thereby stimulating aggregate demand;
- sharing the tax burden by widening the tax base through presumptive tax targeted at those outside the tax net and tightening tax loopholes;
- rationalisation of VAT zero-rating and exemptions, in line with regional best practices; and
- relating the level of fees and charges to the cost of delivering public services.

405. Allow me, Mr Speaker Sir, to therefore submit the proposals for the consideration of the House. The formulation of some of these proposals has benefited from the valuable input of Honourable Members, as well as those of business, labour and ordinary citizens, during the pre-Budget consultations.

406. A major input that came out from the pre-Budget consultations across the country was the need for the Budget to take account of the effect of the prevailing high inflation on the real value of incomes. In line with this, I will be proposing some relief measures, taking account of bracket creep.

### **Tax Relief Measures**

## *Income Tax*

### Pay As You Earn (PAYE)

407. Honourable Members will recall that during the Mid-Term Fiscal Review, the tax free threshold and tax bands were reviewed in July 2006 to cushion employees from the erosion of incomes arising from high inflation.
408. Mr Speaker Sir, inflation, has remained high, thereby, making further reviews from January 2007 necessary.
409. Government is aware of the growing salary gap between management and shop floor workers. The current tax structure is however not reflecting this income disparity where, low and high incomes of \$54 000 and \$600 000 per month respectively, are subject to the same marginal tax rate of 35%.
410. I therefore propose to raise the tax free threshold from \$20,000 to \$100 000 per month and spread the tax bands to end at \$1 million above which income is taxed at a rate of 35%. Accelerated rates of tax will apply on incomes above \$1 million.
411. These measures take effect from January 1, 2007.
412. I have already alluded to the need for me to report to Parliament on a quarterly basis the progress with the implementation of the 2007 Budget. This, Mr Speaker Sir, will present an opportunity for me to consider any necessary reviews to the tax free thresholds.

### Bonus Payments and Performance Related Awards

413. Bonus payments and performance related awards to employees are a welcome source of additional income for taxpayers, especially during the festive season and end of year for parents' preparations for the new school term requirements.
414. I therefore, propose to increase the tax free bonus from the current \$20,000 to \$100,000 with effect from November 1, 2006. This measure will release about \$430 million to taxpayers.



## Tax Credits

415. Mr Speaker Sir, tax credits reduce the tax liability of the elderly, blind and physically challenged members of our society, thereby assisting them to meet their special needs.

416. I, therefore, propose to increase tax credits for the elderly, blind and physically challenged from \$1,000 to \$10,000 per month, with effect from January 1, 2007.

## Rental and Investment Income Earned By Elderly Taxpayers

417. Furthermore, in support of the welfare of elderly taxpayers' dependent on rental and investment income, I propose to review upwards the exempt portion of such income from \$12,000 to \$112,000 per month.

418. Furthermore, I propose to widen the definition of investments, to include fixed term investments, in line with stakeholder submissions during the pre-Budget consultations.

419. These measures take effect from January 1, 2007.

## Tax Free Pension Contribution

420. Mr. Speaker Sir, pension contributions have remained a major source of domestic savings, hence, the need for tax incentives in support of pension schemes. Central to this has been the tax free pension contribution threshold, currently at \$6 000 per month.

421. In the prevailing high inflation environment, this threshold has lost value, especially for those contributing to both the compulsory NSSA scheme, as well as to private schemes, whose viability is now under serious threat.

422. I therefore propose to review the tax deductible limit on pension contributions from \$6 000 to \$75 000 to allow workers' contributions to both the compulsory NSSA Scheme and the voluntary private pension schemes to benefit from this pension contribution tax deduction.

423. This is with effect from January 1, 2007.

#### Retrenchment/ Severance Packages

424. In order to support meaningful investment by retrenchees, it is important that in the prevailing high inflation environment our Budget tax measures target to maintain the real value of the non-taxable portion of retrenchment packages.

425. With effect from December 1, 2006, I propose to increase the non-taxable portion of retrenchment package from the greater of \$1 million or one third of the retrenchment package, up to \$1.5 million to the greater of \$25 million or one third of the retrenchment package, up to \$100 million.

#### Capital Allowances

426. Government efforts to assist companies engaged in expansion projects continue to be hampered by the continued erosion of capital allowances due to high inflation.

427. In this respect, I propose to increase the value of capital allowances with effect from 1 January 2007, as follows:

- passenger motor vehicles from \$1 million to \$10 million
- staff housing from \$1,500,000 to \$16 million

#### Donations to Schools, Hospitals & Clinics and Research and Development

428. Mr. Speaker Sir, Government is facing challenges in mobilising adequate resources to support health, education and research & development facilities. Individuals and private institutions are, therefore, encouraged to donate to schools, hospitals and research and development.

429. I, therefore, propose to increase allowable donations from \$500 000 to \$25 million with effect from January 1, 2007.

430. I further propose to increase allowable deductions for attending conventions or trade missions from \$10 000 to \$1 million with effect from January 1, 2007.

#### Corporate Tax Payment System

431. Mr Speaker Sir, Honourable Members will be aware that corporates are now taxed under the contemporaneous arrangement wherein we tax their profits in the year in which they are earned. Hence for 2007, the current legislation requires them to make quarterly payments of 10% in March, 40% in June, 40% in September and 10% in December on the year's estimated profit, with a 10% margin of error allowed.
432. However, in the prevailing unstable macro-economic environment, many companies continue to face a volatile business production and trading environment.
433. I therefore propose to waive penalties under circumstances where corporates fail to forecast profits within 10% margin of error. Interest on outstanding tax payable will however remain payable. ZIMRA will also support companies in improving on their estimations of corporate profits.
434. Furthermore, in order to support improved cash flow positions of corporates, I propose to review quarterly corporate tax payments on taxable income for 2007 as follows:

**Table 3: 2007 Quarterly Corporate Tax Payments**

|                   | <b>From</b> | <b>To</b> |
|-------------------|-------------|-----------|
| March 25 2007     | 10%         | 10%       |
| June 25 2007      | 40%         | 25%       |
| September 25 2007 | 40%         | 30%       |
| December 20 2007  | 10%         | 35%       |

#### Small Business Enterprises

435. Government recognizes the significant contribution of Small and Medium Scale Enterprises (SMEs) to the growth of the economy. The current tax regime does not however, grant any tax incentives specific to this category of entrepreneurs.
436. In order to support the initiatives of SMEs, I propose to grant special initial allowance of 150% on the cost of any plant and machinery acquired and brought into use for the first time in the business operations.
437. This measure takes effect from January 1, 2007.

#### Capital Gains Tax

438. Mr. Speaker Sir, capital gains tax applies on disposal of immovable property and marketable securities not registered on the stock exchange. Capital gains on sale of assets are ascertained after adjustment for an allowance for inflation. Other deductions such as cost of improving the property are also allowed in arriving at the taxable gain.
439. The inflation indexation allowance adjusts gains for the effects of inflation by giving an allowance equal to the amount by which the cost of the asset would have risen on a monthly basis if its value had kept pace with inflation, as measured by the increase in the consumer price index since the asset was acquired.
440. Currently, the inflation allowance is calculated using the annual average consumer price index for every year the asset is held.
441. I propose that the inflation allowance be calculated using the difference between the all items consumer price index (CPI) in the month of disposal and purchase, divided by the consumer price index for the month of purchase. The inflation allowance will similarly be calculated in respect of improvements.
442. This measure takes effect from January 1, 2007.
443. The proposed method of calculation is in line with international best practices.

## Roll-Over Provisions

444. A taxpayer is allowed to rollover the proceeds of a principal private residence disposed in order to acquire another principal private residence. These provisions however, do not apply where a taxpayer disposes an undeveloped residential stand in order to acquire another stand.
445. In view of the hardships currently faced by taxpayers in developing residential stands, I propose to extend the roll-over provisions currently applied on principal private residence to residential stands with effect from January 1, 2007.
446. However, this measure will not apply to taxpayers who own residential properties and can benefit from roll-over provisions of such properties, on disposal.

## Tax Reserve Certificates

447. Some taxpayers use Tax Reserve Certificates in order to settle their tax debts when they are due. Interest earned on Tax Reserve Certificates deposited with the Commissioner General is fixed and also exempt from withholding tax on interest. The current interest rate of 21.75%, which was put in place many years ago, hence has lagged behind the current market rates.
448. In order to enhance the attractiveness of the Tax Reserve Certificate as an advance tax payment instrument, I propose to review the current rate of interest from 21.7% to the average monthly Treasury Bill Rate with effect from January 1, 2007.

## *Value Added Tax*

### VAT on Agricultural Equipment

449. Mr. Speaker Sir, in order to support agricultural activities and boost productivity under the Land Reform Programme, Government extended VAT exemption to agricultural equipment.

450. However, stakeholders raised concern that the VAT exemption on agricultural equipment reduced the competitiveness of locally manufactured equipment. VAT input tax incurred on inputs into the production process can not be claimed if the finished product is exempt.
451. In order to level the playing field between locally manufactured and imported agricultural equipment, whilst providing the necessary support to the agricultural sector, I propose that exempted agricultural equipment be zero-rated for VAT purposes with effect from January 1, 2007.

#### VAT on Pipeline Transportation Service

452. Mr. Speaker Sir, importation of fuel by road transport is causing severe damage to the road network. There is therefore need for incentives to encourage use of the pipeline.
453. In order to encourage use of the pipeline, I propose to zero rate pipeline services with effect from January 1, 2007.

#### VAT Exemption on Pension Fund Administration Services

454. In recognition of the role of Pension Funds as a vehicle for mobilising savings, VAT does not arise on services offered by an actuary, insurance agent or insurance broker as defined in the Insurance Act, to the extent that those services are rendered to or on behalf of an insurer or a Pension Fund registered under the Pension and Provident Act.
455. Recent developments in the financial sector are such that the business of fund administrators is no longer restricted to institutions defined in the Insurance Act. Services offered by an independent Pension Fund administrator are however, not exempt from VAT.
456. I, therefore, propose to extend VAT exemption to services offered by independent Pension Fund administrators to the extent that those services are rendered to or on behalf of a Pension Fund registered under the Pension and Provident Funds Act.

### *Customs Duty*

#### Customs Duty on Raw materials

457. Mr. Speaker Sir, Government's thrust to enhance capacity utilisation of companies necessitates a reduction of costs which include duties on raw materials and capital equipment among others.

458. In this regard, I propose to provide relief to selected items of raw materials through duty reduction, with effect from January 1, 2007.

#### Ports of Entry Clearance of Goods

459. Mr Speaker Sir, traders raised concern over challenges of clearing their goods, especially during weekends, and after 1200 hours, when Real Time Gross Settlement (RTGS) transactions become unavailable.

460. Requests for alternative payment methods have therefore been submitted, notwithstanding the existence of pre-clearance facilities which allow goods to be cleared before they arrive at the port of entry.

461. The Reserve Bank is aware of these concerns and is monitoring the situation in conjunction with banking institutions, ZIMRA, and freight agencies.

### *Estate Duty*

462. Currently, the principal residential property is exempt from estate duty. Furthermore, there is a tax free estate duty of \$10 million above which a maximum duty of 5% is levied on any additional property.

463. I propose to raise the tax free threshold to \$100 million.

### **Use of Technology in Tax Collection**

464. Harmonisation of standards and regulations relating to trade and tax administration is central to achievement of regional integration. The SADC model Customs Act, when adopted will fully address harmonisation issues such as electronic submission of information to tax authorities.
465. Information processing using the traditional manual system is associated with delays, thereby impacting negatively on businesses operations and revenue collection.
466. In order to embrace technological advancements in line with international best practice, I propose that the relevant provisions of the revenue Acts administered by ZIMRA be amended to facilitate the application of information technology in areas such as the filing of returns electronically, registration of taxpayers and use of digital signatures among others.

### **Learning Material**

467. Mr Speaker Sir, Government has always gone out of its way to support the development of human resources, both through direct budgetary allocation towards education and indirectly through provision of targeted tax relief measures.
468. Currently educational material is exempt from import duties as well as VAT. Furthermore, importation of school requisites is catered for through a duty free certificate issued by the Minister responsible for education.
469. Government remains committed to providing affordable education, and in this regard, stakeholders are thus invited to advise on cases where taxes are being paid on educational material.

### **Registrar for the Fiscal Appeal Court**

470. Mr Speaker Sir, the current practice where a Legal practitioner employed by ZIMRA can be appointed as Registrar for the Fiscal Appeal Court presents potential for conflict of interest.



471. I therefore propose that legal practitioners employed by ZIMRA be relieved of the duty to act as Registrar of the Fiscal Appeal Court.

## **Housing Delivery**

472. Consultations with the insurance and pension industry have identified the use of indexed financial instruments to allow pension funds to invest in prescribed assets that will facilitate investment into property, affordable to workers. Indexation to wages would allow workers to make repayments that rise in line with their incomes.

473. Mr Speaker Sir, in support of this innovative way to attract capital into the housing market and broaden access to property ownership Government is reviewing the relevant legislative framework, in consultation with the Insurance and Pension Funds. Some of the proposals made will incentivise investors, while protecting the interests of prospective home owners upon implementation.

## **Revenue Enhancing Measures**

### *Withholding Taxes*

#### Director's Fees

474. Tax on fees payable to non-executive Directors is, in most cases, only remitted after assessment, resulting in loss of value due to deferment of the payment of tax.

475. I, therefore, propose to subject fees earned by non-executive Directors to withholding tax at a rate of 20%, with effect from January 1, 2007, in line with practice elsewhere in the SADC region.

#### Tenders, Consultancy and Other Services

476. The Income Tax Act provides for withholding tax of 10% on the value of tenders above \$5 000 awarded through the State Procurement Board. The withholding tax is also levied on consultancy and other services offered to Government and quasi-Government institutions, and on trade of goods and services between registered and unregistered businesses.

477. I therefore propose to increase this amount to \$500 000 with effect from January 1, 2007.

#### Remittances

478. The current legislation provides that withholding tax on interest, dividends, fees and royalties collected should be remitted to ZIMRA within a period of 30 days or such longer period as the Commissioner General may allow, taking account of the manual payment mechanism in place.

479. In view of improvements in payment transfer arrangements, I propose to reduce the period within which collected tax can be remitted to ZIMRA from 30 days to 15 days with effect from January 1, 2007.

#### *Deemed Benefits*

#### Motoring Benefits

480. Taxation principles of equity and fairness demands that equal income be taxed at the same rate. Motoring benefits that accrue to employees increase the gross income earned which should therefore be taxed in the hands of the beneficiary.

481. In line with this principle, I propose to adjust upwards the deemed motoring benefits with effect from January 1, 2007 as follows:

**Table 4: Deemed Motoring Benefits**

| <b>Engine Capacity</b>               | <b>Current</b> | <b>Proposed</b> |
|--------------------------------------|----------------|-----------------|
| Up to 1500 cc                        | \$9 000        | \$100 000       |
| Over 1500cc but not exceeding 2000cc | \$15 000       | \$160 000       |

|                                      |          |           |
|--------------------------------------|----------|-----------|
| Over 2000cc but not exceeding 3000cc | \$18 000 | \$200 000 |
| Over 3000cc                          | \$24 000 | \$260 000 |

### *Corporates*

#### Self Assessment

482. Honourable Members will recall that, during the 2006 Budget, I announced that, prior to implementation of self assessment system, ZIMRA will undertake a consultative exercise during the course of the 2006 fiscal year.

483. ZIMRA has since embarked on comprehensive stakeholder consultations, hence is ready to implement the self assessment system. This will place greater responsibility on taxpayers for assessing tax payable, thereby allowing revenue collectors more time to focus on auditing compliance standards of the major taxpayers.

484. I, therefore, propose to introduce the Self Assessment System on income earned from January 1, 2007.

### *Value Added Tax*

#### Threshold for Registration

485. Honourable Members may recall that the VAT registration threshold was reviewed during the 2006 Budget to take account of the impact of inflation.

486. In order to enhance the administration of the tax, I propose to review upwards the threshold for VAT registration from the current level of \$6 million to \$60 million per annum, with effect from 1 January, 2007.

487. This measure will not apply to registered VAT operators.

## Rationalisation of Zero Rated & Exempt List

488. Mr. Speaker Sir, SADC Member States agreed to rationalise and harmonize VAT zero-rated and exempt goods and services under the SADC Tax Memorandum of Understanding (MOU). In pursuance to this commitment, some Member States have reduced their list of zero-rated and exempt products to less than twenty items.
489. Although progress has been made towards rationalisation of exempt and zero-rated goods and services, our list however remains long, compared to other SADC Member States.
490. In this regard, I further propose to streamline the list of zero-rated and exempt goods and services to include lamb, goat and sea food with effect from January 1, 2007.

## Remittance Period

491. Under the current legislation, VAT collected should be remitted to ZIMRA by the last day of the first month following the end of the tax period relating to the registered operator.
492. In order to improve the accounting process of VAT collected, I propose to change the payment date for VAT remittances to the 20<sup>th</sup> of the first month after collection, with effect from January 1, 2007.

## Auditing

493. Mr. Speaker Sir, I am aware of increased cases of non-compliance whereby some operators maintain parallel sets of trading books as they seek to evade payment by understating their tax obligations. This practice has potential to impact negatively on revenue collection.
494. ZIMRA will thus intensify audit coverage in order to reduce revenue leakage.

## **Value for Duty Purposes**

495. Mr Speaker Sir, Government remains committed to fair competition with all potential trading partners. It is in line with this spirit that we have called on our industries to adapt to the more open globalised trading arrangements.
496. Concerns were, however, raised over the impact on local textile industry of dumping and unfair pricing. Stakeholders therefore called upon Government to levy protective customs duties.
497. In order to even the playing field between local manufacturers and importers, I propose to review the basis for determining the value for duty purposes. Announcement on the applicable rates will be made in due course.
498. Furthermore, I remain ready to invoke necessary measures to protect our local industries against any identified practices of dumping into the domestic market. I will also be capacitating quality control institutions such as the Standards Association of Zimbabwe.

## **Value Addition**

499. Honourable Members will recall that in the 2006 National Budget Statement, I announced Government's intention to introduce tax measures that discourage the export of unprocessed commodities such as black granite with potential for value addition. A committee was subsequently put in place under the National Economic Development Priority Programme (NEDPP) to look into Import Substitution and Value Addition.
500. Sectors with potential for value addition have since been identified and appropriate support has partially been availed in line with commitments. Funding for either import substitution or value addition activities has been extended to companies in fertilizer manufacturing, oil pressing, pharmaceuticals, printing services, industrial valve manufacturing, tyre manufacturing, quarry blasting, copper and copper products manufacturing and chrome processing.

501. In order to discourage exports of raw or unprocessed products, I propose to introduce a levy on the value of selected unprocessed products, once measures to curtail obstacles that hinder the processing of value addition are implemented.

## **Other Revenue Measures**

### *Customs Duty on Cigarettes and Tobacco Products*

502. Mr. Speaker Sir, an influx of hazardous, inferior and under priced imported cigarettes continues to impact negatively on the competitiveness of locally manufactured products despite efforts to curb the importation of these products through imposition of deterrent customs duties. The duties have however not been effective due to the disparity between the rate of inflation and the static exchange rate.

503. In order to level the playing field between locally manufactured and imported cigarettes, I propose to amend the calculation of the specific component of customs duty on imported cigarettes. Customs duty on imported cigarettes will therefore be determined as follows:

- the greater of 60% plus US\$5.00 per 1000 cigarettes, exchanged at prevailing inter-bank market rate, or 60% plus Z\$3300 per 1000 cigarettes to be automatically adjusted monthly for inflation as determined by the Central statistics Office published Consumer Price Index for alcoholic beverages and tobacco.

### *NOCZIM Debt Redemption Levy*

504. The NOCZIM debt redemption levy is currently pegged at \$25 per litre of petrol and diesel. This has limited NOCZIM's capacity to liquidate its debt obligations, which continue to rise in the prevailing interest rate environment.
505. I, therefore, propose to review the levy upwards to from \$25 to \$60 per litre, with effect from January1, 2007.

### *Carbon Tax*

506. Fuel consumed by local motorists is subject to carbon tax at a rate of \$5 per litre of petrol or diesel. In the case of foreign registered vehicles, the tax is charged in foreign currency according to engine capacity.

507. In order to relate the current rate of carbon tax to the market price of fuel, I propose to review upwards the current rate from to \$5 to \$100 per litre of both petrol and diesel, with effect from January 1, 2007.

### *Presumptive Tax*

508. Mr Speaker Sir, the current levels of Presumptive Tax need to be aligned to reflect their real value, following erosion by inflation.

509. In order to realise this, as well as complement Government efforts in the maintenance of roads, I propose to review upwards the current rates of presumptive tax as follows:

#### Driving Schools

- Vehicles used for class four training – from \$8,000 to \$120,000 per quarter; and
- Vehicles used for classes 1 and 2 training – from \$12,000 to \$180,000 per quarter

#### Haulage Trucks

- Of carrying capacity of less than 20 tonnes – from \$12,000 to \$180,000 per quarter; and
- Of carrying capacity of more than 20 tonnes – from \$20,000 to \$300,000 per quarter.

#### Commuter Transport Operators

- Of carrying capacity of 15 to 24 passengers – from \$6,000 to \$90,000 per quarter;
- Of carrying capacity of 25 to 36 passengers – from \$12,000 to \$180,000 per quarter; and
- Of carrying capacity of 37 passengers and above – from \$18,000 to \$180,000.

#### Taxi-Cab Operators

- From \$6,000 to \$90,0000 per quarter

#### *Automated Financial Transaction Tax*

510. Automated financial tax is currently charged at the rate of \$10 each transaction.

511. I propose to increase the rate to \$50 per transaction, with effect from January1, 2007.

#### *Stamp Duty*

512. Stamp duty on cheques is pegged at \$10 per each cheque issued.

513. I propose to increase stamp duty to \$100 per cheque issued, with effect from January 1, 2007.



## **Budget Deficit & Financing**

514. Mr Speaker Sir, the projected nominal GDP of \$8.5 trillion for 2007, and the anticipated revenue target of 35.3% of GDP, would entail total 2007 Budget revenues of \$3.0 trillion.
515. This level of revenue, against the above proposals to rationalise the 2007 Budget expenditure allocations to \$4.6 trillion, excluding interest, would imply a Budget deficit of \$1.5 trillion.
516. The resultant overall expenditures of \$4.5 trillion, with revenues of \$3.0 trillion, leave an overall Budget deficit for 2007 of 17.6% of estimated GDP.
517. Under this scenario, all effort will be made to contain non-interest expenditure within the expected revenue inflows of \$3.0 trillion. Any borrowings will be channelled towards financing the interest on existing debt.
518. In light of the fact that the country will remain under sanctions, I have not made major assumptions with regards to foreign financing of this Budget deficit. The financing of the projected 2007 Budget deficit is, therefore, largely from domestic financial savings.

IX. **CONCLUSION**

519. The objectives of this Budget are to stabilise prices, grow the economy, create jobs and raise the standards of living of our people. In order to achieve these objectives, we need a Shared Vision and consensus on what policies are necessary to address these challenges. It goes without saying that we are going to need complementary policies that are well synchronised. And above all, we need the will and commitment to implement these tough policies.

520. When it is all said and done, Mr Speaker Sir, I believe the Zimbabwean economy is a resilient one, and it will carry us through. We may wish to get comfort from the words of Saint Paul in his letter to the Corinthians.

521. Mr Speaker Sir, 2 Corinthians Chapter 4 Verses 16 – 17, I quote: “Therefore, we do not lose heart. Though outwardly we are wasting away, yet inwardly we are being renewed day by day. For our light and momentary troubles are achieving for us an eternal glory that far outweighs them all.”

522. Mr Speaker Sir, I now commend the 2007 annual Budget to the House and I place it on the table.

Minister of Finance

**HARARE**

30 November 2006