ZAMBIA INSTITUTE FOR PUBLIC POLICY ANALYSIS

Journal

1st Quarter 2007

THEME Social Security

Features

Regulars

Freeway- Guaranteed Social Security?

Why is it that in Africa retirement benefits for pensioners and compensation payments to injured or disabled workers are so woefully inadequate? Is it because the required funds can provide rich pickings for the powerful, but the intended beneficiaries are weak and vulnerable? This issue of the Journal on the theme of Social Security will focus on the boast that in Zambia social security is 'guaranteed'.

Alas, our present situation is desperate. Most long service government employees suddenly become paupers on retirement, condemned to travel from office to office in Lusaka, begging for their legal entitlements. The reason? The Civil Servants' Pension Fund has been used as a cash cow by central government, which now owes it some K3 trillion. Former employees of local authorities, who depend on the Local Authorities Superannuation Fund, are not much better off.

Retired private sector employees, who paid contributions over many years to the Zambia National Provident Fund (ZNPF), are in the same boat. Their hard-earned savings have been destroyed by years of high inflation, combined with government borrowing at minimal rates of interest. Even those who have since saved with the National Pension Fund Authority (NAPSA), set up in 2000 to succeed the ZNPF, would be unwise to put faith in that big monopoly.For its efficiency is open to serious doubt, as is clear from an article in this issue.

As for the Workers' Compensation Fund Control Board (WCFCB), the same article reveals that this institution operates mainly for the benefit of its own employees, with little or no concern for the interests of its supposed beneficiaries. How else can one explain the amazing contrast between revenues received and claims paid?

These misgivings appear to be confirmed by the fact that both institutions treat their annual reports and accounts as highly confidential documents, to be kept away from public view, when they should be published in the press for all to see. Here, as elsewhere, secrecy invites suspicion.

What plans has the Ministry of Labour & Social Security to introduce improvements? Their article in this issue, entitled 'Reform of Social Security in Zambia', refers vaguely to certain 'challenges', but makes no mention of the current deplorable situation. Nor does it suggest that the Ministry has any clear ideas for reform or plans for positive action.

Yet, if the Ministry has no ideas of its own, it should at least try to learn from experience elsewhere. Chile is famous for having introduced competition into its national pension system, an example since followed by many other countries. This issue contains two articles about different aspects of Chile's experience.

A contribution from Steve Williams of African Life Insurance Company gives a balanced assessment of NAPSA and suggests how its performance could be improved by awarding competitive contracts. Similar measures could no doubt also be applied to pension schemes for civil servants.

Clearly, the boast that social security in Zambia is 'guaranteed' is laughable. But the lack of reliable benefits for pensioners and the disabled is no laughing matter. We need to act now to remedy a deplorable situation. This will not be easy, especially if political will is lacking. Just as important will be action to prevent a recurrence. Here we should ask, What is the 'free way'? The answer is obvious: competition. Monopolies deaden: competition enlivens. As a remedy it is uniquely effective. Let us open the doors which are now closed and barred against it. Competition alone can provide the guaranteed social security which is so long overdue for weak and vulnerable Zambians who are disabled or retired.

Reform of Social Security in Zambia

Anthony Dumingu

In 1983 Government appointed the Kabwe Commission of Inquiry. The main objective of the inquiry was to analyze the difficulties that social security schemes were facing and recommend possible remedial measures. Attempts to create fundamental reforms based on their findings were abandoned in the face of economic crisis and other preoccupations which dominated the 1980s.

As part of the Social Security Reform Programme the Second Government of the Republic in July 1992, through Gazette Notice No. 46 of 1992 approved the establishment of the Department of Social Security in the Ministry of Labour and Social Security. Among the objectives of the Department were:

I) To spearhead the implementation of the Social Security Reform Programme
Ii) To establish a comprehensive Social Security System Reform Programme
Iii) To establish a comprehensive social security system

The overall objective of the reform process was to improve the effectiveness and efficiency of social security schemes.
The reform of social security focused on addressing policy, legal and institutional issues and the existing social security institutions. The major outcomes of the reforms included the enactment of the following pieces of legislation:

- National Pension Scheme Act, 1996
- Pension Scheme Regulation Act, 1996
- Public Service Pensions Act, 1996
- Workers' Compensation Act, 1999

Despite government efforts to put in place a sound social security policy, there are still a number of challenges that need to be addressed. Most of the challenges relate to governance and administration of social security; financing and investment issues; legal and constitutional issues; harmonization of the supervision and regulation of social security schemes.

Government has within the framework of the Fifth National Development Plan (FNDP), National Employment and Labour Market Policy (NELMP), Millenium Development Goals (MDGs) and the Social Protection Strategy Paper realized that in order to address the prevailing poverty challenges, it is necessary to secure significant improvements in the provision of welfare and social security to its citizens. This goal has not been reached partly due to lack of an overall aggregated guiding strategy to address the challenges that have been highlighted.

The Ministry of Labour and Social Security is cur-

rently working on a policy implementation strategy that could be used as a vehicle for transforming the various programmes and strategies in the above mentioned core government documents into desired results.
Some of the objectives under the strategy are:

- To harmonize the fragmented social security policies in Zambia
- To harmonize the fragmented social security legislation and regulation in Zambia
- To extend coverage of social security contingencies to those currently excluded.
- To educate the public about the social security rights.
- To establish and maintain a social security data base.
- To carry out research of social security related issues.
- To provide an overall policy, regulatory and legislative framework for the Zambian Social Security System.

Wider consultations on the document shall be carried out through the National Social Security Reform Steering Committee.
The strategy highlights the guiding principles on a number of issues including Governance and Administration, social security financing, investment of social security funds, taxation of social security benefits, coverage, compliance and retirement age.

The policy also stipulates the existing legal framework and takes note of its fragmentation. It identifies the appropriate institutional framework. It has been realized that in order to efficiently and effectively achieve meaningful social security, it is imperative that there is co-operation and collaboration with stakeholders.

In order to establish a comprehensive social security system, the Zambian Government has maintained a three pillar social security system:

1st Pillar
Compulsory National Basic Scheme - National Pension Scheme Authority (NAPSA) is a basic scheme for all, no one can opt out of it. The pensionable (retirement) age for both males and females is 55 years.

2nd Pillar
Promotion of Occupational Pension Schemes

3rd Pillar
Individual/private informal arrangements and schemes.

To introduce competition and to ensure the survival of occupational pension schemes, the employee and employer contributions to NAPSA have been maintained as low as 10 percent.

In order to promote effective and efficient regulation of occupational pension schemes, government has amended the Pensions and Insurance Act and intends to transform the Pensions and Insurance Authority into a semi-autonomous institution run by a Board.

Author: Anthony Domingu, Principal Social Security Officer, Ministry of Labour & Social Security

Retirement Benefits - What Next?

African Financial Services Limited

The Minimum Wages & Conditions of Service Act contains a provision for a terminal benefit of 3 months pay per year of service, which has a major impact on social security. This provision has the following serious disadvantages.

1. Funding this benefit for long-serving employees can place an unaffordable burden on employers.
2. Lack of portability between employers penalizes the employee who moves to another employer or leaves employment to become an entrepreneur.
3. The benefit is lost to the employee who dies before completing 10 years service or before reaching retirement age.
4. An employee who is dismissed for a serious offence loses accrued entitlements to terminal benefits.
5. Employers can cause separations to avoid paying accrued rights.
6. All employees can lose out if the employer goes out of business.

The introduction of NAPSA, with its guaranteed pension indexed to national average earnings, provided an opportunity to replace this unsatisfactory provision, an opportunity which should now be taken.

Under the Act the above disadvantages are avoided if there is an approved pension scheme. A possible solution may lie in making occupational pension schemes mandatory for all employees and portable between employers. The schemes can be designed as defined contribution (like saving schemes) and have a contribution structure for minimum prescribed benefits.The benefits must be fully portable across employers, and benefits must only be accessed in situations such as retirement, early medical retirement or death. Employers wishing to give additional benefits or higher contributions can do so as long as the minimum requirements are met. This would help employers by making financial outflows more predictable, and would give employees the comfort that their terminal benefits are outside the control of the employer and have been funded. The Minister would then exempt all employers who sponsor occupational schemes from the terminal benefits provisions of the Minimum Wages Act .

While this solution may cover the medium to larger scale enterprises, small companies with very few employees may have to elect to amalgamate with other companies under industry classification and create industry pension schemes.

The issue of accrued benefits can be resolved by agreeing the quantum and arranging to fund this to the pension scheme over an agreed specified period.

The proposed solution of combining NAPSA and occupational schemes would remove the disadvantages described above and resolve the confusion arising from the terminal benefit provisions of the Minimum Wages & Conditions of Service Act.

The Two Elephants of Social Security

Game Scout

Elephants need watching. Though large and slow, they can get up to mischief. So can big organisations. My task has been to observe the two elephants of social security in Zambia and to record my findings. These 'elephants' are the National Pension Scheme Authority (NAPSA) and the Workers' Compensation Fund Control Board (WCFCB).

Both organisations were established by Act of Parliament. Both report to the Minister of Labour & Social Security, employ hundreds of people across the country, administer large amounts of money and enjoy compulsory membership. Given their status and their vital role in providing a safety net to some of the most vulnerable members of society, their effectiveness in performing that service must be open to scrutiny.

Yet members of the public have no access to the annual reports and accounts of these institutions. And even an M.P. who offered to help could not obtain reports from the National Assembly more recent than 1995/96 for Workers' Compensation, and 2003 for NAPSA. ZIPPA also drew a blank with the Ministry of Labour & Social Security. Moreover, the unauthorised publication of information about these institutions is an offence punishable by 3 months imprisonment!

"Guaranteed Social Protection" with NAPSA?

Inspection of NAPSA's accounts points to a crisis of record keeping within the organisation. Although NAPSA is required by law to send out Member Statements annually, its performance has been lamentable. The share of active members receiving statements fell from 44.8% in 2001 to only 17.6% in 2003. Distribution figures were conspicuously absent from the 2004 report.

The 2003 annual report cites poor quality of information submitted by members as a cause of the low number of statements issued. But a letter from a Kitwe company with over 2,000 employees points the finger back at NAPSA. It details several failed attempts to update and correct NAPSA's records since 2001 and draws attention to the causes. These include failure to provide social security numbers and inadequate systems to enable electronic submission of large volumes of information.

Although NAPSA only started work in February 2000, a source reported delays of 6-12 months in paying members. Given the number of members and the constant changes of employer-related and salary-related information, maintaining up-to-date records is a huge task for which appropriate electronic systems are essential. The regular despatch of statements to members would also facilitate the timely correction of mistakes.

NAPSA's failure to maintain accurate records was again emphasized this very month by an instruction that employers must in future supply full details for every employee every month, instead of only recording changes. This will place an enormous extra burden of work on large employers. It also amounts to an admission that NAPSA's records are already in a mess. What can we expect in 5, 10 or 20 years time? Clearly, NAPSA's motto, “Guaranteed Social Protection”, does not reflect the reality on the ground.

“Workers Have a Right to Compensation” - WCFCB

“Workers have a right to compensation”, states the WCFCB slogan. This is completely inconsistent with the paltry sums paid in compensation by the institution. Figures showing maximum monthly pensions of K150,000, and minimum pensions of K469 were published without shame in the 2001/2002 annual report. The payment of 'pensions' of K10,000 and less serves only to insult the injured.

It is worrying that WCFCB has been unable to issue an annual report and accounts since 2001/02. That report shows that debt collection was a serious problem. Total debts in 2001/2002 exceeded the year's total assessments of K27bn. K14.5bn of that amount was owed by major parastatals and district councils, and so could be uncollectible.

As with NAPSA, there are unacceptable delays in making payments. At WCFCB, it is quite common for release of the first payment to take over a year. An injured miner assessed with a 25% permanent disability, and therefore unemployed, waited 19 months before receiving his first payment.

When at last it came, this man's pension was a meagre K31,250 per month; only 4.6% of his final monthly salary of K686,500 and less than half of his employer's monthly assessment of K68,250 per employee. In another case an engineering industry worker on a salary of K231,351 when he was injured in 2000, was assessed as having a 2% disability and awarded a monthly pension of K1,000!!! No wonder that all the compensation paid in 2001/02 amounted to a miserable 5.5% of total income. Nor was this a new development. Past records show that total payments have rarely exceeded 5% of income.

It appears that pensions are updated at 5-year intervals. However, these awards are always far below the rate of inflation. A mine worker, whose injury was assessed at 17% permanent disability was in 1996 awarded a pension of just K6,840 (against his salary of K151,998). Increases in line with inflation would by 2006 have brought this to K53,720, but his monthly pension rose to only K11,490.

No explanation is available regarding how compensation for injured employees is calculated. Nor are details given to employers. They might champion the cause of their employees.

Employer assessment rates were raised by between 50% and 140% some 5 years ago, but there was no related rise in levels of compensation. Assesment rates now range from K2.82 per K100 to K6.93 per K100, depending on the industry sector. This far exceeds the maximum rate of 4% charged by most private sector insurance companies. Workers and employers alike have a right to know how such high contributions are spent.

Conclusions

My enquiries have revealed poor record keeping, ineffective debt collection, long delays in making payments and shockingly low compensation for injuries. Given their high administration costs, it would appear that the primary beneficiaries of these elephantine institutions are their own employees, rather than people unable to work due to age or injury.

The inconsistencies between motto and performance seem to have been lost both on the officials of these organisations and on their superiors at the Ministry of Labour & Social Security. It is vital to resolve this situation without further delay, so that workers' right to compensation is given substance, and social protection in retirement is truly guaranteed.

Note: $1 = Approx. K4,000

Pros & Cons of a Pensions Monopoly

Steve Williams

This article is my response to a request to look critically at the main arguments on both sides, and to put forward my views on the ideal situation.

The Arguments For Monopoly

1. NAPSA is a defined benefit scheme, not a money purchase scheme. It replaced a money purchase scheme (the Zambia National Provident Fund ZNPF), which, as a result of high inflation, political interference and lack of suitable investment vehicles, had failed to provide a good return to its members.

2. A national defined benefit scheme needs to be a unified scheme, and membership must be compulsory for all in order to benefit from the laws of large numbers (although this principle has already been compromised by a Statutory Instrument exempting some large employers)

3. If opting out is allowed, large companies which can afford to fund their own schemes will be the first to do so, leaving NAPSA with the smaller, poorer companies, who tend to be slower payers and less stable. This could well render the scheme unviable, and it would jeopardize pensions for the more vulnerable members of society.

4. NAPSA, because of its legal powers,is in a better position than private companies to ensure that contributions are paid by all employers.

5. A government sponsored scheme ensures that benefits will be paid. The Government cannot go out of business and (in theory) has the power to raise unlimited income through taxation. There are examples all over the world of private schemes which have come to grief leaving pensioners penniless.

The Arguments Against Monopoly

1. Without competition there is little incentive to minimize costs. Historically, state institutions all over the world have proved to be inefficient at administering social security schemes, and there is no evidence as yet to suggest that NAPSA will be any different.

2. Inefficient administration causes long delays in processing benefits.

3. High levels of costs relative to contributions and poor investment performance necessitate higher contribution levels to fund the guaranteed benefits. Political expediency usually results in this additional burden being carried mainly by employers.

4. Freedom to choose between pension providers creates competition, which (subject to prudent regulation) ensures that the providers which offer the best levels of service, the lowest levels of cost and the best investment returns will get the business, with resulting benefits for members.

The Ideal System

My own view is that the ideal system is a combination of the strengths of both sets of arguments. I believe there should be one compulsory national scheme which, after extensive consultation with stakeholders and actuaries, pays defined benefits according to rules set out in legislation. However, all operational aspects of the scheme (administration, investment management and benefit payment) should be contracted out to the private sector, under agreements providing strict benchmarks with respect to administrative costs, investment performance and benefit payment times.

The whole scheme should be run by a Board of Trustees, composed mainly of representatives appointed by employers and employees (not controlled by Government). Their functions (as with other pension fund trustees) would be to monitor the appointment and performance of the private companies to which they had sub-contracted these various functions, to safeguard the assets of the fund and to ensure that the members' interests were properly served. To enable members to monitor trustee performance, the Trustees would publish annual reports in the national press, together with the audited accounts of the fund. They should also hold the title to all the investments of the fund, which should be kept in private custody. The scheme should be regulated, along with all other pension schemes, by the Pensions and Insurance Authority under the Pension Scheme Regulation Act.

This would achieve the best of both worlds, a guaranteed and secure pension for all, administered efficiently by the private sector, but under the watchful eye of a competent and properly funded regulator.

Notes: *1. A defined benefit scheme guarantees certain benefits depending upon length of service, and is valued periodically to determine whether the contributions are sufficient to fund those benefits. If not, contributions can be adjusted. This will involve comparing the scheme's actual performance with the assumptions which were made when determining the contribution rate. These assumptions include:*

i) survival rate of members
ii) success in collecting contributions
iii) investment performance of the fund
iv) administrative costs incurred by the managers.

2. A money purchase scheme has a fixed level of contributions. Each member's contributions are invested and the fund is made available to the member on retirement. Thus the investment risk is passed on to the member, who will lose out if the performance of the fund is inadequate.

Author: Steve Williams is CEO of African Life Assurance Company Ltd. and a founder member of the Zambian Association of Pension Fund Managers.

Social Security in Chile

Christian Larroulet

Freedom is the principal basis upon which the Chilean pension system is founded: each worker saves for retirement and determines which private pension fund shall administer their savings. As such, each worker makes a personal commitment to their future.

The Chilean pension system provides people with ownership of their retirement savings. This way, they maintain an active attitude in relation to their responsibility to save, and can decide upon the right combination between profitability and risk. For the system allows them to choose among alternative funds that differ in their proportion of fixed and variable rates of return. This involves a cultural change in which workers are transformed from being merely receivers of a benefit to being actively responsible for their future pensions.

The State, however, is not relieved of its obligations, since it legally sponsors the system and requires contributions. This is a product of compulsory consumption, so there is a legal system that maintains a set of regulations These set limits on risk in portfolios, insulate the owners' equity in pension funds with respect to the administering entities, and regulate the conflict of interest associated with the administration of funds by third parties.

Furthermore, the State carries out a subsidizing role through the guaranteeing of minimum pensions. That is, those people with less than 20 years of contribution are guaranteed a base level pension of approximately 75% of the minimum salary. This base level is the equivalent of a targeted insurance, and it is greater for those that contribute according to a minimum salary. This system transfers funds from generation to generation according to the economic cycle during which they contributed.

The second element of subsidization takes place through the welfare pension, by which seniors are guaranteed a level of income at least equal to the poverty line, independent of their work or social security history. All people older than 65 may apply for this benefit if their income does not reach the indicated level.

Both instruments introduce community interests into the social security system, but not any more through a tax on work, for the people are the owners of their contributions. Instead, the community interests of these pensions are financed by income taxes in general.

The combination of both instruments, after 25 years of having the new social security system in place, has helped to bring rates of poverty and of extreme poverty in the senior population lower than those of any other age group. This is a success in a country like Chile, where poverty has decreased from 45.1% of the population in 1987 to 18.8% in 2003.

A further effect of this system is that it has positively impacted the economy. Various empirical studies have shown that the social security reform reduced the tax on work, thereby increasing employment and job security. Likewise, studies by high executives of Banco Central de Chile attribute a third of the growth in the economy to the social security system, through its contribution to saving, investment and macroeconomic efficiency.

Finally, the most important thing is that the reform of the pensions system allowed Chilean workers to be the owners of their savings and thus, of a majority percentage of the country's net equity. In this way, the workers form a direct partnership for the progress of the country and directly receive the benefits of development.

Author: Cristian Larroulet is Chief Executive of Libertad y Desarrollo, Chile

Putting Chile's Nest-egg to Work

Joshua Goodman, with acknowledgment to "The Economist"

Drivers in Chile don't have to wait until they're 65 to enjoy their pension benefits. Every day thousands do so when they speed from Santiago to Vina del Mar along the Rutas del Pacifico toll road, which opened in 2004 with funding from the country's deep-pocketed pension funds. A billboard reminds passing motorists: "Your savings are financing this highway, and this highway is financing your retirement."

Indeed, this year alone, the government's privately managed Pension Fund Administrators, or AFPs expect to buy nearly $1 billion in locally issued bonds to fund projects such as the new highway. And the AFPs expect to earn a healthy return on their investment: Annual real returns have averaged 10% for the last two decades. "It's a perfect circle for everyone involved," says Alvaro Gonzalez, local manger for Sacyr, a Spanish construction company that operates the highway.

The new expressway is the latest perquisite of a 23-year-old government-mandated but privately managed pension system that oversees some $50 billion in assets. That's the largest such pool of funds in Latin America, even though Chile is only the region's sixth-largest economy. The pension system's kitty has grown so fast, in fact, that the government relaxed its pension laws in 1996 to allow money to be invested outside Chile and to fund public works. Among the big-ticket projects funded recently are the extension of Santiago's highly efficient subway system, hundreds of miles of highways, and the construction of nearly 500,000 homes for low-income families. "Without the AFPs, it's unlikely Chile would have the modern infrastructure it does," says Axel Christensen, an executive with Santiago-based Moneda Asset Management.

Back in 1981, during the rule of dictator Augusto Pinochet, Chile replaced its pay-as-you-go retirement system with the 401(k)-like savings and investment program, which is fully portable, meaning workers' portfolios move with their jobs. The reform was an attempt to defuse a fiscal time bomb brought on by an aging population. Under the pension scheme, each month the 95% of Chilean workers option into the system have 10% of their salaries automatically routed to the pension fund of their choice. Although overseen by the Labour Ministry, the money is managed by one of six private AFPs, which were initially set up by local investors as highly regulated mutual funds that invested mostly in domestic equities and government bonds.

The Chilean government estimates that 10% of the country's growth since 1981 is directly or indirectly attributable to the new pension system, thanks to investments bankrolled by AFP funds. In the same period, the money under management at the AFPs has grown to the equivalent of 70% of gross domestic product. And since early retirement options were introduced in 1988, the average monthly pension benefit for workers retiring early has increased from $258 to $318. The average retired worker in the U.S., by comparison, gets $925 under Social Security, even though the U.S. has eight times Chile's per capita income. No wonder the "Chilean model" of pension reform is being emulated in a wide range of countries, from Poland to South Korea.

Chile's pension system has generated a critical mass of capital that has made the country's financial markets the most sophisticated in Latin America. Hundreds of Chilean companies from retail chain Falabella to airline LANChile today depend not on the whims of foreign investors but on the AFPs, which control 70% of the local equity and bond market. The only downside appears to be the local markets' dependence on the AFP funds and the possibility of an asset bubble at some point.

But the bottom line for most Chileans is that they are living better than ever in their golden years. And the economy is all the better for it.

Author: Joshua Goodman in Santiago, Chile.

Quotation of the Month

As the government, we are aware of these problems and we are working to ensure that by next year we harmonize all social security institutions for better service delivery. We are also keen to ensure that social security covers as many people as possible. In fact, not only covering them, but also ensuring that they are comfortable.

- **Patrick Kafumukache**, Minister of Labour & Social Security. 'The Post' 29.10.04

Topical Article

FRA Stepping into Worn-out Shoes

John Fynn

The Food Reserve Agency (FRA) was established by an Act of Parliament to make provision, as its name indicates, for food security by purchasing a small proportion of domestically produced staple food crops to be released onto the market in the event of poor harvests. However, it now seems to be fitting into the shoes once worn by NAMBOARD; those shoes that were worn-out and unfashionable because they carried the staple-food sector into a role that was a major influence in the collapse of the economy of the Second Republic.

NAMBOARD, we recall, monopolised maize marketing, promoted production through pan-territorial pricing in areas that were both agronomically and economically unsuited to it, stored maize at public expense and then released it onto the market at a price that crowded out private sector involvement. It was also in sole control of exports and imports. NAMBOARD's position as a parastatal meant that it was able to ignore market forces and to determine the gap between producer and consumer prices, a powerful political tool. NAMBOARD absorbed such a huge proportion of the national budget through its market-distorting mandate that it effectively undermined the economy. The concern is that nostalgia for government control of maize marketing is in danger of re-creating the same situation.

FRA is tending towards a pan-territorial and pan-seasonal pricing that will create a monopoly position by undermining private sector commercial viability. In 2006 FRA purchased maize at the floor price of K38,000 per 50 kg bag regardless of where it is or when it is purchased in an effort, no doubt, to be fair to all producers. Though relatively generous to remote producers, this is in contradiction of the market liberalisation ostensibly espoused by Government. It is not conducive to sustainable development because it promotes production in areas rendered uneconomic by transport costs, and it does not reward early production or private storage which inhibit price fluctuation. Traders braving the maize market in expectation of future increases in into-mill prices will face losses when FRA sells, as it may do, several months after harvest at its original purchase price.

FRA has purchased 405,000 tonnes of maize this season and plans to export 200,000 of this and to sell the remainder locally at a price based on three determinants:

- the cost of maize production plus storage and interest to the point of sale;
- the prevailing price of early maize
- the perceived threshold price for mealie meal at which consumers might resort to civil disobedience.

However, this combination does not provide comfort either to farmers or to traders since, although the cost of production per hectare remains fairly constant, the cost per tonne can double in a drought year, and because the overriding influence will be expected consumer tolerance rather than financial profitability.

There are welfare arguments for subsidising production in remote areas to provide income for villagers, and for subsidising the storage of maize to protect consumers from exploitative prices. But if Government decides that this is a worthy pursuit, despite its adoption of free market principles, it should either confine FRA buying to remote areas or extend subsidies to private sector players in order to promote efficiency through competitive buying. And, if private traders were certain that their markets would not be undermined by Government, they could develop, and be encouraged to develop, into companies that could be contracted to undertake functions now performed by FRA.

The main function of FRA is simply to ensure that there are sufficient stocks to tide consumers over the period it would take to import maize in the event of crop failure - about two months. Even this provision is questionable, since crop failure is unlikely to be absolute or sudden. Drought, pestilence or reluctance to plant all allow ample time to replenish stocks while the diminished crop is consumed. For example, assuming that complete self-sufficiency is normal, a devastating 50% crop failure should still provide six months' needs, during which time imports can be arranged, even from distant international sources. A reliable early warning system, an attentive trading sector and a capability to respond rapidly are much less costly means of ensuring food security than hoarding massive stocks in case the food runs out.

It is estimated by the Food Security Research Project that the maize export ban suppressed maize prices by 12%, which is more than will be added to yield by good rains. It can also be close to a farmer's profit margin. So the ban, with the accompanying monopoly given to FRA, means that he is unlikely to speculate again by applying his resources to contributing to Zambia's potential as the grain basket of Africa.

The direct cost of maintaining FRA could be reduced if it were to extend its operations to seasonal input supply at a profit, as did NAMBOARD. But the indirect cost of crowding out the private sector and distorting free market development cannot be justified. We learned that from NAMBOARD. Let's not forget it.

Author: John F W Fynn, Technical Assistant, Zambia National Union of Farmers

Economics Without Tears with DISHI

"Hoarding"

The press recently reported that farmers near Choma were hoarding maize because they expected poor rains to cause a shortage. That raises the question, is hoarding good or bad, helpful or harmful?

Our answer to that question may depend on the circumstances. If a peasant farmer hoards his maize crop so as to retain enough to support his family until the next maize harvest, we commend his foresight. But if a commercial farmer hoards his crop in order to take advantage of an expected shortage, which will enable him to charge hungry people a high price, we condemn him as an exploiter. We may even demand price controls, with punishment for those who overcharge.

The ordinary person thinks it wrong to try to profit from a food shortage. But the economist sees things differently. His emphasis is not on intention but on result, for economists concentrate on cause and effect.

Most of us see prices in terms of relationships, and we disapprove when some individuals take advantage of the misfortunes of others. For us, that is what matters. But the economist stands back and looks at things dispassionately. He sees that a high price does more than benefit the seller at the expense of the buyer. It also results in two general benefits.

First, it discourages waste. If maize, for instance, becomes more expensive, people start to economize in using it. The mother will cook more sparingly, and less nshima is left on the plate. She may also substitute sweet potatoes or cassava. In these ways she responds positively to the high price of maize by making what is available go further.

Second, suppliers of maize respond to the high price. They cannot suddenly produce more. But they can cast around for fresh supplies. They may find them in another district, from which the higher price of the commodity has now made the cost of transporting it over a distance worth while. In addition, both commercial farmer and peasant farmer (there is of course no clear line between the two) will plant more maize in the coming year, or more alternative crops, in the hope of either benefiting from scarcity or avoiding it.

So we should not blame the hoarder. He may have made a killing from an unfortunate situation. But he has also performed a service. By looking ahead, by providing costly warehousing and protecting his stocks against pests he has been able to provide a commodity when it was badly needed. In addition, the high price charged at a time of acute scarcity has had the beneficial effect of reducing demand and increasing supply. In short, hoarding for the sake of profit can provide a valuable service.

Tribute- Milton Freedman

Temba A Nolutshungu

The death of Milton Friedman, which follows closely on the death of Lord Harris, also a great exponent of classical liberal thought, signifies the exit of one of the great thinkers of his generation.

Thinkers such as Milton Friedman and Friedrich von Hayek argued for individual liberty in the economy and society at a time when the general tendency throughout the world was towards statist, socialist and dirigiste governance. They were armed with the conviction that the instinct for freedom was such an inherent characteristic of the human spirit that ultimately the struggle for freedom would prevail over policies and governments that negated it.

Proceeding from this conviction, the great proponents of liberty saw their task as to demystify and explain the reality of human action. In their view, collectivist policies emphasised the subordination of the will of the individual to that of the collective, as interpreted and defined by those in the citadels of government. Friedman regarded such a course as inimical to human nature and anathema to individual liberty and personal responsibility.

Friedman could explain complex economic concepts in a way that everybody could understand. He cogently and clearly explained not only that freedom delivers, but also why it delivers. He showed that people propelled by their own self-interest, generally engage in productive economic activities and in the process contribute to the welfare of others, just as Adam Smith had written two hundred years before.

In order to drive the point home, Friedman juxtaposed the freer economy of West Germany with socialist East Germany. Rising like a phoenix from the ruins of the Second World War, West Germany had become the second biggest economy in the world while East Germany was an economic fiasco. In a video based on his book Free to Choose he made the remark, as he stood next to the Berlin Wall, that despite the economic discrepancies between the two countries, their similarities were patently obvious: same culture, same language, the same work ethic, yet the economic outcomes were so different.

I came across 'Free To Choose' at a time when I was puzzled by the exodus of people from the countries of the socialist eastern bloc to the capitalist west, the west that I had so energetically denigrated during my struggle against apartheid. I was struck by the fact that the refugees were from all walks of life. And I was reminded that the Berlin wall had been erected not by capitalist Germany, to keep socialism out, but by the socialist German Democratic Republic to keep its people in and prevent them from escaping to West Germany.

Friedman's insights propelled me to broaden my inquiry. I compared South Korea and North Korea, Hong Kong and Communist China. Again there were the same similarities in cultures, languages, and work ethic on either side of their borders, one group economically successful and the other an economic disaster. Milton Friedman's study of West and East Germany provided compelling empirical verification that freedom delivers.

Friedman was to have a further influence on me. I was a victim, along with millions of my countryfolk of an omnipresent and omnipotent apartheid government, which dictated the lives of black people from the cradle to the grave and aroused in me a compulsive distaste for a leviathan state.

Milton Friedman taught me that government grew at the expense of individual liberties. His teachings motivated and defined my struggle as being about cutting government down to size and remaining perpetually vigilant against any signs of government encroachment on individual liberty.

He expounded on a Hayekian theme: the observation that knowledge is dispersed among individuals and further made more complex by their individual preferences, wants and needs, which are constantly changing. No single individual, or organisation, or institutional entity, could purport to be the reservoir of all that knowledge, as was attempted by the people in charge of command economies. Such fallacious policy-making would manifest itself in moribund economies, as was evidenced by the implosion of socialist economies towards the close of the 1980's.

Friedman explained that markets harmonise the individual economic efforts of people of diverse cultures and backgrounds. He showed that the spontaneity of the free market does not result from human design but from human action. In a free market the colour, race, culture and even political proclivities of people, consumers and producers alike, are of no consequence. He alluded to this phenomenon as the impersonal operation of market forces.

My personal experiences with apartheid laws, which interfered at every turn with people's lives, implemented at times with brutal force, made me wary of dictatorial government. Friedman's message that no government should have such power was a ray of light to me; apartheid was the antithesis of a free market. This insight has contributed tremendously to my outlook as I consider solutions to South Africa's challenges, reinforcing my view that those solutions are to be found in Friedman's non-divisive free market.

Milton Friedman, my guide and mentor, I salute you. I wish I had met you.

Author: Temba A Nolutshungu is a director of the Free Market Foundation.

Letters

Your November issue on Banking caught my attention but in no way did it convince me that our banks in Zambia are customer focused.

Let's take the case of Barclays Bank. Unless you are a member of Prestige Banking you have no access to the bank after 14:30hrs or on a Saturday morning.

Barclays is now opening new branches under the guise of a new initiative yet the same bank went out of its way to close branches in Luanshya and Mufulira. Imagine the poor guy in Luanshya who has to catch a minibus to Ndola just to access his money.

Over the years I personally have found that the quality of service one gets at Barclays is solely dependent on who you know at the branch.

Years ago Barclays came up with the Connect card which allowed you to make purchases by direct debit. But this service, which is common in developed countries, has never really been pursed to its fullest.

Allen Mate

Disclaimer

The views expressed in this journal are those of the authors. They are not necessarily shared by members or by ZIPPA, which has no official view.

Contributions & Mailing list

Readers are urged to contribute news or views in the form of letters or articles. They should be sent by email to zippa@zamnet.zm, or mailed to:
The Editor, ZIPPA Journal, P O Box 20516, Kitwe

If you change your email address please let us know.
If there is someone you want added to the mailing list, please mail us *"subscribe"* with the name and email address. If you wish to be removed from the list, please mail us *"unsubscribe".*

www.zippazambia.org