



Comprehensive Economic Recovery in Zimbabwe

A Discussion Document

2008

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Manufactured in Zimbabwe

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Preface

This discussion document is the result of work commissioned by UNDP-Zimbabwe and based on extensive research conducted by a team of eminent Zimbabwean economists with technical support from the UNDP Country Office. The questions it raises and the suggestions it puts forward in terms of possible economic recovery trajectories for Zimbabwe are intended to trigger national debates which might help to inform sound policy formulation processes. The issuing of this document is taking place at a time when Zimbabweans of all walks of life and political affiliations have agreed to work together to overcome the enormous economic challenges that the country faces. It is hoped that this document will be read by all interested players, both national and international and thereby, in some small way, contribute to a rapid and sustainable recovery process for this country.

Dr. Agostinho Zacarias
UNDP Resident Representative

Executive Summary

This discussion document contains an economic recovery framework for Zimbabwe, based on analytical work conducted by a team of senior Zimbabwean economists. It provides an overview of the post-independence performance of the economy at both macroeconomic as well as sectoral levels, identifying key constraints to past growth, and breaks these down into financial, legal, institutional and policy variables. This methodological approach is carried forward and applied to the last ten years in order to elucidate those factors underlying the economic regression that has taken place. On this basis a package of remedial actions is put forward, the adoption of which it is believed will trigger a sustainable, pro-poor growth dynamic.

One common thread which runs throughout the document is that of the imperative of restoring macroeconomic stability as a pre-condition for recovery. Specific measures that flow from this include profound changes to current patterns of both monetary and fiscal policy management in order to correct widespread distortions which have acted as impediments to savings, investment and production.

At the same time, with a view to sustaining in the longer-term the recovery that would flow from such stabilization, the team has advanced a package of reforms in areas ranging from trade policy, public enterprises, the financial sector, agriculture, manufacturing, mining, tourism, the informal and SME sectors, and the labour market. These are sequenced, prioritized, and broken down into short and medium to long term actions. Key considerations which have informed the analysis underpinning the proposed package include the need to ensure that growth is broad-based, inclusive and sustainable, and that it addresses longstanding problems rooted in the economic dualism inherited at Independence. Particular attention was based to the need to remove existing impediments to the participation of the poor in growth, and the necessary measures required to ensure this transformation takes place are detailed in the document.

The document also contains proposals on how the country could best manage international assistance if Zimbabwe's traditional development partners, including the Bretton Woods Institutions, were willing to reengage with and support its recovery and longer-term development efforts. In addition, the role of the State in supporting recovery is analysed. The team advances a set of proposals which it believes are necessary in terms of changes to the various ways the State interacts with the economy and society.

Acknowledgments

The team of national economists, brought together and commissioned by UNDP to reflect on the economic challenges facing Zimbabwe, benefited from informal discussions with many Zimbabwean and non-Zimbabwean analysts too numerous to mention. Each encounter helped to deepen the shared understanding amongst team members of both general and specific aspects of the performance of the Zimbabwean economy. Without these discussions the document would have been all the poorer.

In addition, as the work progressed, extensive written comments on earlier versions were received from experts which have helped to shape both the scope in terms of areas covered, as well as improved the content of the final document. Unwitting contributors to this report, therefore, include Dr. Peter Robinson, one of Zimbabwe's most eminent economists. At very short notice, Dr. Robinson was willing to share his unique insights into issues related to both productive and social infrastructure with the team, encouraged the team to carry out further work on trade policy and the international competitiveness of the Zimbabwean economy, and pointed out other lacunae which needed to be addressed. Dr. Lloyd Sachikonye helped the team to impose restrictions on themselves in terms of their forays into the field of political economy, assisting the researchers to clearly delimit what they were capable of researching given their limited expertise in this area and therefore helping them to avoid the danger of 'overstretch'. Dr. Stephen Chipika provided the team with invaluable information on the current status of Zimbabwe's SMEs and informal sectors which was incorporated in the report. Dr. Peter Nicholas and Dr. Mungai Lenneiye of the World Bank in Washington and Harare respectively, as well as their teams, both commented extensively on draft versions, as did Dr. Stuart Tibbs, Dr. Alexis Ferrand and Ms. Joanne Manda. On a number of occasions, and as work progressed, preliminary findings were shared with a team of economists from the Ministry of Economic Development and useful feedback was received.

Dr. Agostinho Zacarias, UNDP's Resident Representative, played a key role in supporting the initial proposal for such an initiative, its rollout and subsequent formulation phases. Mr. Lare Sisay, UNDP's Deputy Resident Representative, was extremely adept at finding solutions to various operational and administrative constraints as these arose. It would be true to say that the team was provided with the means and the space to focus on their 'core business', and this is largely attributable to his unwavering support. Ms. Bettina Kittel, Special Assistant to the Resident Representative, worked in the engine room throughout, and quite simply 'made things happen'.

Finally, the Embassy of Norway made a generous financial contribution to the initiative, complementing the UNDP Country Office's own resources as well as funding received from UNDP's Bureau for Crisis Prevention and Recovery. Even more important than its financial contribution, however, was the encouragement received from Norwegian Embassy staff throughout the exercise. The team are indebted to all of the above who in their various ways made this work possible.

Dr. Mark Simpson
UNDP Chief Technical Adviser

Acronyms

AFC	Agricultural Finance Corporation
AfDB	African Development Bank
AMU	Arab Maghreb Union
AREX	Agricultural Research and Extension
ART	Anti-Retroviral Treatment
ASPEF	Agricultural Sector Productivity Enhancement Facility
AU	African Union
BACOSI	Basic Commodities Supply Side Intervention
BEAM	Basic Education Assistance Module
BWIs	Bretton Woods Institutions
CABS	Central African Building Society
CBZ	Commercial Bank of Zimbabwe
CEDC	Children in Especially Difficult Circumstances
CMB	Cotton Marketing Board
COMESA	Common Market for Eastern and Southern Africa
CPI	Consumer Price Index
CSCL	Cold Storage Company Limited
CSO	Central Statistical Office
CZI	Confederation of Zimbabwe Industries
DFID	Department for International Development (UK)
DRC	Democratic Republic of Congo
DSA	Debt Sustainability Analysis
DZL	Dairibord Zimbabwe Limited
EAC	East African Community
ECCAS	Economic Community for Central African States
ECOWAS	Economic Community of West African States
EDM	Emergency Drugs and Medical Supplies
ESAP	Economic Structural Adjustment Programme
ESOPs	Employee Share Ownership Plans
ESPP	Enhanced Social Protection Programme
FAO	Food and Agricultural Organization
FDI	Foreign Direct Investment
FTLRP	Fast Track Land Reform Programme
GDI	Gross Domestic Income
GDP	Gross Domestic Product
GFCF	Gross Fixed Capital Formation
GMB	Grain Marketing Board
GNP	Gross National Product
GNS	Gross National Savings
GPS	Ground Positioning System
GVC	Global Value Chains

HIPC	Highly Indebted Poor Countries
IBRD	International Bank for Reconstruction and Development
ICT	Information and Communication Technologies
IDA	International Development Association
IFAD	International Fund for Agricultural Development
IFC	International Financial Corporation
IMCCP	Inter-Ministerial Committee on Commercialization and Privatization
IMF	International Monetary Fund
IOM	International Organization for Migration
JOC	Joint Operations Command
JSA	Joint Staff Assessment
LDCs	Least-Developed Countries
MDG	Millennium Development Goal
MPC	Monetary Policy Committee
MTA	Money Transfer Agency
MTEF	Medium-Term Expenditure Framework
MVA	Manufacturing Value Added
NAC	National Aids Council
NEC	National Employment Council
NGO	Non-Governmental Organisation
NIT	National Investment Trust
NOCZIM	National Oil Company of Zimbabwe
NPV	Net Present Value
NRA	Nominal Rates of Assistance
NRZ	National Railways of Zimbabwe
ODA	Official Development Assistance
OECD	Organization for Co-operation and Development
OVC	Orphans and Vulnerable Children
PAF	Performance Assessment Framework
PAPPAF	Programme Aid Partners Performance Assessment Framework
PAZ	Privatization Agency of Zimbabwe
PE	Public Enterprise
PLARP	Parastatal and Local Authorities Reorientation Program
POSB	People's Own Savings Bank
PRSP	Poverty Reduction Strategy Paper
PSD	Private Sector Development
PSIP	Public Sector Investment Programme
PTC	Posts and Telecommunications Corporation
PWC	Public Works Component
QFAs	Quasi-Fiscal Activities
RBZ	Reserve Bank of Zimbabwe
RECs	Regional Economic Communities
REER	Real Effective Exchange Rate
RER	Real Exchange Rate
SADC	Southern African Development Community
SAP	Structural Adjustment Programme

SERA	State Enterprises Restructuring Agency
SIDA	Swedish International Development Agency
SME	Small and Medium-Enterprise
SPS	Social Protection Strategy
TCPL	Total Consumption Poverty Line
TFP	Total Factor Productivity
TVET	Technical Vocational Education and Training
UDI	Unilateral Declaration of Independence
UMP	Uzumba Maramba Pfungwe
UNAIDS	Joint United Nations Programme on HIV/AIDS
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
UNICEF	United Nations Children's Fund
UNIDO	United Nations Industrial Development Organisation
USAID	United States Agency for International Development
UZ	University of Zimbabwe
ZABG	Zimbabwe Allied Banking Group
ZESA	Zimbabwe Electricity Supply Authority
ZIMACE	Zimbabwe Agricultural Commodity Exchange
ZIMDEF	Zimbabwe Manpower Development Fund
ZIMPREST	Zimbabwe Programme for Economic and Social Transformation
ZIMRA	Zimbabwe Revenue Authority
ZINWA	Zimbabwe National Water Authority
ZISCO	Zimbabwe Iron and Steel Company
ZMDC	Zimbabwe Mining Development Corporation
ZSE	Zimbabwe Stock Exchange

Chapter 1

Overview and Key Messages

In 2006, UNDP's Regional Bureau for Africa published the results of a comprehensive Strategy and Management Review it had conducted. Amongst the recommendations it contained were that UNDP Country Offices should provide 'support through special initiatives to states in fragile transition processes' and that this might take the form of, amongst other actions, 'analyses of national policy environments'¹.

Launched in 2007 by the Zimbabwe Country Office, the key objective of the present analytical exercise was to arrive at a sound understanding of the extent and nature of the regression that has taken place in Zimbabwe over the last decade, and on this basis to provide insights into the key features of a possible comprehensive economic recovery trajectory for the country that would set it back on the path of growth and sustainable human development. This discussion document is meant as a modest contribution to ongoing debates among both international and national actors as to the best way forward for Zimbabwe in a post-crisis scenario.

1.1 METHODOLOGICAL APPROACH

The team of senior Zimbabwean economists that was brought together, and provided with an opportunity to reflect critically on the economic challenges facing Zimbabwe, adopted a common methodological approach in their work. This involved examining past performance in specific sectors/themes in order to tease out the key explanatory variables which underpinned the behaviour of these sectors since independence. A situational analysis of the present state of the sectors in question was then undertaken,

which in turn allowed each individual researcher to advance a set of policy recommendations in terms of what would be required to unblock existing bottlenecks to the resumption of growth at sectoral level. These bottlenecks were broken down into legal, institutional, human capital (capacity), policy frameworks and financial constraints, and an attempt was made to understand how they interacted over time and impacted on overall performance.

Respect for the principle of logical derivation was a constant consideration throughout the team's work. As a result, efforts were made to ensure that any given policy recommendation that was advanced in a given report was grounded in, and flowed logically from, the preceding analytical work, that it reflected the best evidence available, and that in terms of inter-sectoral consistency it did not contradict the recommendations contained in other reports.

In order to ensure both inter-sectoral consistency and the overall coherence of the framework contained in this document, reports were subjected at regular intervals to internal and external quality-assurance processes. Each individual report, therefore, underwent a number of revisions as the exercise progressed and new light was thrown on the behaviour of particular aspects of other sectors and aspects of the Zimbabwean economy.

1.2 CHOICE OF SECTORS AND THEMES AND STRUCTURE OF THE REPORT

While the intention was to ensure that the initiative was as comprehensive as possible in terms of the areas it covered, both time

¹ UNDP, Regional Bureau for Africa, *Strategy and Management Review*, New York, 2006, p.16.

and human-capacity constraints led to a curtailment of the initial list of sectors and themes that were to be analysed. The requirements for recovery in areas such as social-service delivery systems and the environment have not been addressed. The gender-specific impacts of the ongoing economic downturn have not been teased out in any significant manner, nor has the impact along gender lines of possible recovery trajectories. The latter is an area that particularly merits more work through *ex ante* Poverty and Social Impact Analysis.

THE ISSUE OF HOW THE STATE HAD OPERATED IN THE PAST, HOW IT IS CURRENTLY OPERATING, AND HOW IT SHOULD OPERATE IN A RECOVERY SCENARIO, ALSO BEGAN TO FEATURE PROMINENTLY AS A COMMON DENOMINATOR THAT CUT ACROSS THE FINDINGS IN ALL THE SECTORAL AND THEMATIC REPORTS

At the same time, new themes not on the original list at the time the exercise was designed were tackled as the work progressed. For example, it was felt that, notwithstanding the overall medium-term to long-term time horizon that was adopted, the issue of appropriate short-term economic stabilization measures could not be ignored. It was therefore agreed that short-term stabilization imperatives would be addressed, and that these should be coupled with some considerations on necessary countervailing social safety nets to deal with the inevitable deflationary impacts of such an adjustment process. The critical role of infrastructure, both productive and social, as well as trade policy and issues related to the international competitiveness of the Zimbabwean economy, were also addressed in the final stages of the exercise.

The issue of how the state had operated in the past, how it was currently operating, and how it should operate in a recovery scenario, also began to feature prominently as a common denominator that cut across the findings in all the sectoral and thematic reports. It was therefore agreed that these insights should be analysed during the consolidation phase of the exercise and brought together in a specific chapter.

A third theme, which also began to take on increasing importance as work progressed, was that of future aid flows in a scenario in which the international donor community was prepared to re-engage with Zimbabwe and support its efforts to recover. This issue was

seen by the team as one which also needed to be analysed and its effects factored into the proposed recovery strategy. Thought was given as to how Zimbabwe could derive maximum benefit from such a possible resumption of non-humanitarian international assistance. A chapter on aid flows and appropriate national aid-management systems was therefore drafted containing some insights into how this partnership might develop over time.

In terms of the structure of the report, it became clear during the consolidation phase of the exercise that a number of individual sector and thematic reports overlapped with others to such an extent that it made sense for them to be merged. So, for example, separate reports on land policy and recovery of the agricultural sector were merged. At the same time, as the analysis of certain sectors progressed, logic dictated that some chapters needed to be sub-divided. The report on the private sector was divided into two chapters, one covering generic problems and the other focusing on the specificities of manufacturing, mining and tourism. The key findings of a report on 'the developmental potential of the diaspora' were hived off into two other chapters; the human capital dimensions of the diaspora were brought into the chapter on labour markets and human capital, while the financial aspects of diaspora remittances are now reflected in the chapter on the recovery of the financial sector. Such changes are intended to both improve the flow of the document as well as to facilitate ease of comprehension on the part of readers.

1.3 SOME DEFINITIONAL CLARITY

A number of theoretical constructs and concepts appear throughout this document and therefore merit some elucidation for the benefit of the reader. Foremost among these is the concept of **pro-poor growth**. Given the vertiginous decline in poverty indicators in Zimbabwe, the team was seized of the need to design a recovery strategy that was not

only focused on triggering rapid growth but also addressed the need to reverse the extremely serious impoverishment of the vast majority of the Zimbabwean population over the last decade. The team was constantly aware of the fact that the concept of pro-poor growth does not translate into a single policy formula, and that the concept itself is ‘contested terrain’. Even a cursory reading of recent global economic history shows that countries with very similar growth rates can have markedly different success rates in terms of translating those growth rates into sustained poverty reduction. Nevertheless, there is widespread acceptance that growth, if not always sufficient for poverty reduction, is always certainly necessary.

What was clear to the team was that the key transmission channel between growth and poverty reduction is employment, and that Zimbabwe’s deteriorating poverty indicators are directly related to the collapse in employment levels, particularly in formal employment. To the extent that there is consensus within the development literature – and in a post-Washington Consensus world, it is one of the few areas of agreement – it is clear that sustained and rapid poverty reduction requires both robust growth as well as growth that in terms of its pattern (as broad-based as possible in terms of its sectoral and geographical distribution) allows the poor to participate in and derive benefits from a growth dynamic. Both the pace and pattern of Zimbabwe’s growth in a recovery scenario will define the extent to which the poor are able to participate in and benefit from growth.

In this light, the recommendations contained herein have sought to address the need to ensure that a recovery process in Zimbabwe is as **inclusive** as possible, and that the **integrability factor** of the poor in an expanding economy is enhanced. The related concept of **capability deprivation**, derived from the work of Amartya Sen ², has also

informed the thought processes of the team. This is reflected in recommendations contained in this document concerning the need to remove obstacles to the participation of the poor in the growth process, such as through increasing their access to land and financial services, as well as through the need to invest in human capital formation via the provision of basic social services.

These policy recommendations should be accompanied by the restoration of the market mechanism to its role as an engine of growth, in order precisely to ensure that the integrability and capabilities potential of the poor are realised. But the arguments for so doing go beyond purely economic outcomes, and should also be seen in the context of fundamental freedoms: As Sen has argued:

‘In recent discussions, the focus in assessing the market mechanism has tended to focus on the results it ultimately generates, such as the incomes or the utilities yielded by the markets.... But the more immediate case for the freedom of market transactions lie in the basic imperative of that freedom itself. We have good reasons to buy and sell, to exchange, and to seek lives that can flourish on the basis of transactions. To deny that freedom in general would be in itself a major failing of society.’³

Another related concept which features prominently throughout this work is that of **dualism** in the Zimbabwean economy. Applied initially to characterize the structure of the economy inherited at independence, the team has taken the concept forward and usefully applied it to the crisis period. At independence, the new government inherited an economy characterized by a relatively developed and diversified formal economy sitting alongside a neglected and under-developed peasant-based subsistence rural economy.

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² Amartya Sen, *Development as Freedom*, Random House, 2000.

³ Sen, p.112.

THE CRISIS YEARS
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OWNERS

Pre-independence policies had been directed to supporting the former, while the latter was largely left to its own devices. A reading of post-independence economic history indicates that this dualism was not addressed, and that if anything, with the collapse of the formal economy and the exponential growth of the informal economy both in urban and rural areas during the crisis period, the problem has deepened, with most economic transactions and units now operating outside formal systems. Policy recommendations are advanced in this report that aim to break definitively with this structural feature of the Zimbabwean economy.

The team also found much to agree with in relation to the notion of the **missing middle**, as expounded by Nancy Birdsall⁴, which resonated with their own analysis of the past and current structure of the Zimbabwean economy. The crisis years have seen the severe weakening of the country's middle class, as many have either dropped below the national poverty line or been forced to emigrate, as well as a gradual withering away of formal small and medium-sized enterprises of which they were previously the owners. The latter have suffered during the downturn through having only local systems to meet their financial needs; their skilled workforce has emigrated, and their markets have shrunk as a result of a collapse in aggregate demand. The economy is now dominated, on the one hand, by a number of large companies that have been able to survive the downturn through access to their

own secure lines of credit, input and export markets, and on the other, a massive and still-growing informal economy. This trend is observed to have cut across all sectors, from the financial services sector to agriculture, mining and manufacturing, and this dominant feature of the crisis economy will need to be tackled in a process of recovery.

In the course of the research, the centrality of the role of the state as either enabler or impediment to past, present and future growth and poverty-reduction efforts became a recurrent theme throughout all the reports. Given the decision to dedicate a specific chapter to the issue, the team conducted extensive research on comparative experiences in terms of international best practices on the role of the state as a facilitator of growth and poverty reduction. The concept of the **developmental state**, derived initially from research on the experience of Asian development models⁵, was seen to have some applicability to the Zimbabwean experience, though largely in a negative sense through the current absence of the key features which characterize such successful states.

Drawing on the experience of a number of Asian states, developmental state theory⁶ is based on the idea of a state's commitment to a technically sound, long-term national development agenda. Through its capacity to both design and implement policies that support such an agenda, developmental states are able to trigger and sustain growth as well as poverty reduction over extended

⁴ Birdsall, Nancy, *Do no harm: Aid, Weak Institutions, and the Missing Middle in Africa*. Working Paper 113, 2007, Center for Global Development, Washington DC. See also her *Reflections on the Macro Foundations of the Middle Class in the Developing World*. Working Paper 130, Center for Global Development, 2007, Washington DC. Central to the thesis is the argument that 'inclusive growth' necessarily translates into the movement of people out of poverty into the middle class, with a commensurate expansion of the wealth they command. Such a transformation is seen to be correlated to growth that is based on wealth creation and productivity gains through private sector activities, as opposed to the non-productive rent-seeking behaviour of elites, and is therefore more sustainable over the long-term. The argument is also linked to economic governance issues, with a strong middle class demanding sound macroeconomic governance (e.g., fair and efficient tax systems, fiscal probity, transparent budgetary processes, competitive exchange rates), as well as strong public accountability systems. Logic would dictate that absent such a class, the reverse would take place.

⁵ To these Asian examples might be added others closer to home, such as Botswana and Mauritius.

⁶ See, for example Fritz, Verena and Alina Rocha Menocal, *Developmental States in the New Millennium: Concepts and Challenges for a New Aid Agenda*, Development Policy Review, 2007, 25(5) pp.531-552.

periods, which in turn leads to a positive transformation of the economy and society within a condensed period of time. Such transformations have been characterized by rapid processes of industrialization, the adoption of new technologies, and the move to higher value-added production processes, running concurrently with a shift from subsistence to more commercial, export-oriented farming. An expansion of opportunities for all to participate in the modern economy, partly through the removal of impediments – be these legal or financial or in terms of improved access to other assets such as land – as well as through the provision and expansion of public services such as health, education and agricultural extension, has been key to the success of such states.

To these features of a developmental state might be added others, such as sound management of public finances, effective public borrowing, investment in human capital, the provision and maintenance of infrastructure, a respect for private property rights, and an ability to stimulate and cooperate with the domestic private sector which is seen as the key engine of growth, technological innovation and employment, as well as the main source of tax revenues. The chapter on how the state does business is informed by the various components that characterize such developmental states, and the concept is used to evaluate the past behaviour of the Zimbabwean state as well as being the basis on which policy recommendations are put forward in terms of how the state should be reformed and reoriented so as to enable it to support a recovery process.

1.4 MANAGING EXPECTATIONS

As the team set out to understand the realities of the current state of the Zimbabwean economy and society, it became clear that profound damage has occurred over time, some aspects of which are easily reversible, others less so. For

example, while the correction of price distortions and the restoration of reliable supplies of water and electricity may lead to a quick rebound in the mining sector, tourism and in some areas of manufacturing, the damage done to public sector capacity and the loss of the country's human capital base may well take decades to reverse.

An additional insight thrown up by the research was that, contrary to popular views, the country's growth model had been underperforming long before the onset of the current crisis. By way of example, the downturn in both manufacturing and mining in terms of value added per capita occurred before the deepening of the crisis associated with the introduction of the Fast Track Land Reform Programme in 2000, in the case of mining in 1998 and in manufacturing in 1996.

Historical data therefore provide an invaluable reality check. Over the long haul, i.e., the period 1960–2002, and even including the growth spurts of 1968–1974 and the early 1980s, far from being one of Africa's better performing economies, Zimbabwe lagged behind the regional average, growing at an annual average rate of 2.6 percent over the period, as against an average of 3.2 percent for sub-Saharan Africa. More significantly, with an annual population growth of 2.9 percent over the same period, this translated into real per capita incomes declining between 1960 and 2002. One key conclusion is, therefore, that neither the command economy of the 1980s (and certainly not the 'command economy plus' of the post-1997 period) nor the abortive liberalization experiment of the 1990s, succeeded in putting Zimbabwe on to a fast-growth track.

Full recovery, defined simply in terms of a return to the peak real per capita incomes of 1991, would take twelve years, assuming a bottoming out of the decline in the course of 2008, and uninterrupted growth of 5 percent annually from 2009 to 2020. And, given that Zimbabwe is susceptible to drought on average every three years, and that with the decline of commercial

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agriculture this vulnerability has increased, even the 5 percent annual growth in per capita GDP may be beyond the upper bounds of probability.

This cautionary note is necessary in order to guard against misplaced enthusiasm and a misreading of positive signals in the early years of a recovery scenario. While there will be a bounceback effect, possibly a strong one as current idle capacity is brought on stream once again, and as international assistance helps to overcome constraints to production, this may well peter out unless the necessary measures are taken to sustain this rebound. As was the case with the new post-independence government in 1980s, there is a danger that – in the same way that the early and robust growth rates evidenced in the first three years of independence were seen as indicative of long-term trends (and which, with the advantage of hindsight, should now be more properly attributed to the end of the war, the dismantling of sanctions, the utilization of spare capacity, and renewed access to markets and imported inputs) – an early rebound in a post-crisis scenario might be misinterpreted once again as translating into a sound and sustainable longer-term growth model.

1.5 A FINAL CAUTIONARY NOTE – THE PROBLEM OF DATA

One key difficulty faced by the team as it carried out its analytical work centred on the availability and quality of data sets. The deterioration in the national statistics system over recent years has been a marked one. Not only has the brain drain impacted adversely on national capacity in this area, but a shrinking state-revenue base has meant that even the recurrent costs required to support data-collection efforts are no longer

being covered. As a result, many data are quite simply no longer being collected, where they are being collected they are of dubious quality, where they are available they are no longer being analysed and, increasingly over recent years, on the grounds of ‘national security’, they are no longer being made available. Added to these difficulties facing economic analysts is that, in a hyper-inflationary environment, indicators based on the national currency are of limited utility as comparators.

The problem of up-to-date data and their reliability runs the whole gamut from the requirement for a new population census (the last one having been undertaken in 2002) through to the need to update the national poverty assessment in the light of the precipitous decline in macroeconomic indicators since the last assessment based on 2004 data, as well as outdated sectoral surveys, most significantly in the area of agriculture. To this might be added the lack of information in areas such as Zimbabwe’s total external debt stock that is owed to ‘other official bilaterals’, i.e., non-OECD (Organization for Co-operation and Development) creditors, and that will have a significant impact on any proposals regarding future debt relief and the country’s possible debt sustainability levels.

All statistics in this document therefore come with a serious ‘health warning’. It has become clear to the team that a significant effort will have to be made to update national databases. Reliable baselines are a *sine qua non* for the formulation of national and sectoral recovery plans, the setting of targets, the basis on which progress towards these targets can be monitored and evaluated, and the effectiveness of international assistance gauged. Seen in this light, it would be in the interest of both government and its international partners to address this constraint as quickly and comprehensively as possible.

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Chapter 2

Zimbabwe's Macroeconomic Situation

The objective of the present chapter is to pull together in a comprehensive manner the evolution of the country's economic management system since independence in 1980 and bring to bear the lessons learned from this experience. The chapter is also meant to bring together the links between macroeconomic policy positions, micro-economic dynamics, and developments in the sectoral structure of the economy.

A situational analysis of the developments in Zimbabwe is undertaken within a framework of four different periods: (i) the pre-independence period (ii) the control regime period, 1980–1990, (iii) the liberalization era, 1990–1996, and (iv) the deepening crisis period, 1997–2008. Through this timeframe a diagnostic analysis of Zimbabwe's economic performance is presented using some relevant economic indicators: GDP (Growth Domestic Product) growth per capita, inflation, sectoral trends, employment, real wages, and human development indexes.

What is highlighted in this chapter is the fundamental structural change in Zimbabwe's economy, which started with the onset of economic crisis in 1997 and deepened in the post-2000 period. The fundamental rupture with past patterns of growth that took place in 2000 means that lessons learned during the pre-crisis period should be treated with caution. At the same time, the analysis also makes clear that the economy has been operating sub-optimally throughout the post-independence period, a factor which is often ignored in research on Zimbabwe.

The main focus of this chapter is to put forward suggestions in terms of future macroeconomic management that could support a comprehensive economic recovery strategy. These macroeconomic policies should aim at achieving sustainable, broad-based and inclusive growth and poverty reduction. The chapter also throws light on

the short-term stabilization requirements, policy recommendations and actions contained in chapter 3 on stabilization and the section on an operational framework.

2.1 SITUATIONAL ANALYSIS OVER POLICY PERIODS

2.1.1 The pre-independence era, 1965–1979

In response to the imposition of international sanctions against Rhodesia's Unilateral Declaration of Independence (UDI) in 1965, the government assumed extensive interventionist powers, adopting inward-looking and import-substitution policies, designed to promote domestic manufacturing and achieve self-sufficiency in major consumer goods. Extensive intervention in the economy, mainly through elaborate controls on prices, wages, interest rates, and in exchange-rate markets, became pervasive.

Externally propelled protectionism during the UDI period, combined with the forced reinvestment of blocked profits, contributed to high growth rates during the period 1965–1973. The increased role of the state in economic activity was shown by increases in investment. The growth associated with the above factors soon came to an end, however after 1974, mainly as a result of the impact of the liberation war and the oil-shock-inspired global recession.

Notwithstanding this post-1974 downturn, in overall terms the UDI economy was well managed, albeit for the benefit of a racial minority, with stable prices, high savings and investment rates, and a slowly depreciating currency in real terms. It was also characterized by a great deal of government intervention, which worked closely with the white-dominated private sector.

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2.1.2 The control regime, 1980–1990

At independence in 1980, Zimbabwe's new government maintained the macroeconomic controls inherited from the Rhodesian government. Within the framework of a command economy, the government also introduced redistributive objectives that necessitated a large public sector and increased government spending on health, education, and other social welfare programmes throughout the 1980s. Although the 1980s might be interpreted as a decade of success, particularly when judged by improvements in terms of social indicators, the downside was the high cost in terms of unsustainably high budget deficits, whose harmful effects remained hidden behind a plethora of economy-wide controls. Zimbabwe's average growth rate of 4.3 percent per annum in the 1980s was the envy of sub-Saharan Africa during the so-called 'lost decade' for Africa. Upon closer inspection however, it was clear that there were problems with the growth model. For example, formal employment grew at just 1.9 percent per annum over the period.

A combination of fortuitous political and social factors and climatic conditions led to a 'boom and bust' experience in the 1980s. Zimbabwe's immediate post-independence period was greeted by exceptionally high growth rates: 10.7 percent and 9.7 percent for 1980 and 1981, respectively. This unprecedented economic boom could be explained by three factors:

- Favourable exogenous growth conditions at the end of the liberation war: lifting of economic sanctions, favourable world market conditions, two consecutive and exceptionally good rainfall seasons.
- The pursuit of fiscally driven redistributive policies, which in turn stimulated overall demand in the economy.
- The opening up of external markets.

The Zimbabwe government made it clear that the state was to play a central role in the country's economic and social development. The economic boom in the immediate aftermath of independence might have been misinterpreted by the government as obviating the need to strengthen the orientation and effectiveness of the state to manage the required transition towards broad-based, inclusive growth, and to ensure an internationally competitive economy, using both the private and public sectors.

When these favourable exogenous growth factors began to weaken by the mid-1980s, the economy was plunged into recession. This was initially sparked by two consecutive droughts (1982/83 and 1984/85), falling demand for Zimbabwe's exports in world markets, and the start of a decline in investment.¹ While some would argue that this 'boom and bust' pattern could be explained by exogenous factors, usually drought, the tendency for Zimbabwe's long-term growth rates to decline is strongly related to a controlled macroeconomic environment that failed to provide adequate and predictable resource flows and incentives for long-term investment.

Although output grew more strongly during the 1980s than in the rest of the post-independence period, Zimbabwe's weak export performance, low levels of capital formation and foreign-exchange scarcity subsequently led virtually all economic players – industrialists, government and labour – to accept the need for a package of reforms.

2.1.3 Economic liberalization period, 1991–1996

The key elements of the Economic Structural Adjustment Programme (ESAP) which began in 1991 were:

- A shift from import substitution to an open-market economy fostering export-driven growth.

¹ The investment ratio declined from 20 percent of GDP between 1980 and 1985 to 17.5 percent between 1986 and 1990 (Central Statistical Office, Quarterly Digest of Statistics).

- Monetary policy reform: market-determined interest rates and the removal of barriers to the financial sector.
- The establishment of a one-stop investment promotion centre – the Zimbabwe Investment Centre.
- The commercialization of public enterprises in order to facilitate autonomy in business decision-making on issues such as investment, pricing, accountability and efficiency in the utilization of resources.
- Liberalization of the labour market to allow free collective bargaining between labour and employers.

While the government vigorously pursued trade liberalization under ESAP, it stalled on public sector reforms. The government failed to adhere to the internal logic of the reforms. For example, fiscal stabilization which was required up-front was never seriously attempted because the government found it politically difficult to reduce its expenditure. Exogenous factors, in particular the 1992/93 drought (the severest in living memory), served only to aggravate an inherently precarious situation created by the government's own delays in public sector and public enterprise reforms. By 1995, these delays had given rise to high budget deficits – of over 8 percent compared to the ESAP target of 5 percent of GDP. At the same time, instead of the target of 5 percent GDP growth, the actual average growth rate achieved was 0.8 percent under ESAP from 1991 to 1995.

The economic reforms of the 1990s failed to induce the behaviour, by both the private and public sectors, that was needed to put the economy on a sustainable growth path through faster accumulation of physical and human capital that are key to gains in productivity.

The successor programme, the Zimbabwe Programme for Economic and Social Transformation, ZIMPREST (1996–2000), sought to continue the unfinished business of ESAP. This included the reduction of the budget deficit, facilitating public sector and public enterprise reforms, and financial liberalization. It also sought to address the broader social and political agenda of poverty reduction, land reform, black economic empowerment and the indigenization of the economy. Yet ZIMPREST faltered for reasons similar to those that impacted adversely on ESAP – the government's fiscal policy, which threw macroeconomic fundamentals into disarray and resulted in high budget deficits, high inflation, low foreign-exchange reserves, a weak balance-of-payments position and overall low growth.

The broad picture at the start of the deepening crisis period in 1997 was one in which the population had been made to bear a heavy social cost for the reforms, with little to show in terms of improved international competitiveness of the economy. The liberalization of the economy had not led to poverty reduction and economic diversification; on the contrary, economic performance and export competitiveness had been adversely affected by high production costs, declining terms of trade, climatic conditions and the real appreciation of the Zimbabwe dollar. The same phenomenon was observed in other sub-Saharan African countries that had 'implemented the rules of World Trade Organization (WTO) and reforms of the BWIs [Bretton Woods Institutions], opened up their economies, and implemented liberalization and privatization, but growth [had] not occurred' (Sindzingre, 2004: 7).²

2.1.4 The deepening crisis, 1997–2008

The onset of the economic crisis can be traced to the so-called 'Black Friday' crash

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² Sindzingre refers to the 1980s, when most of sub-Saharan Africa adopted SAPs (Structural Adjustment Plan) and had nothing to show for it. However from 1997 to 2002, the rest of sub-Saharan Africa grew by 1.8 percent, and by 4.1 percent since 2003, during the time that Zimbabwe's economy was sliding.

of the Zimbabwe dollar on 14 November 1997, which was precipitated by the government's unbudgeted payment of gratuities to war veterans. This was followed in 1998 by Zimbabwe's participation in the conflict in the DRC, which further contributed to the ballooning fiscal deficit. Following the reversal of reforms undertaken during ESAP and ZIMPREST, government policy became increasingly interventionist as the authorities sought to reverse economic decline. In several respects these interventions were designed to boost private sector performance, primarily through the provision of cheap bank finance at negative real interest rates, via a plethora of lending windows operated by the Reserve Bank of Zimbabwe. Private sector performance was however, constrained by an overvalued exchange rate, severe shortages of foreign exchange, a shrinking domestic market, and a variety of supply-side bottlenecks that included fuel, electric power, imported inputs and skills. At the same time, the steep decline of commercial agriculture after 2000 (see chapter 9 on land policy and agriculture) robbed industry of its traditional source of supply of domestic inputs while also

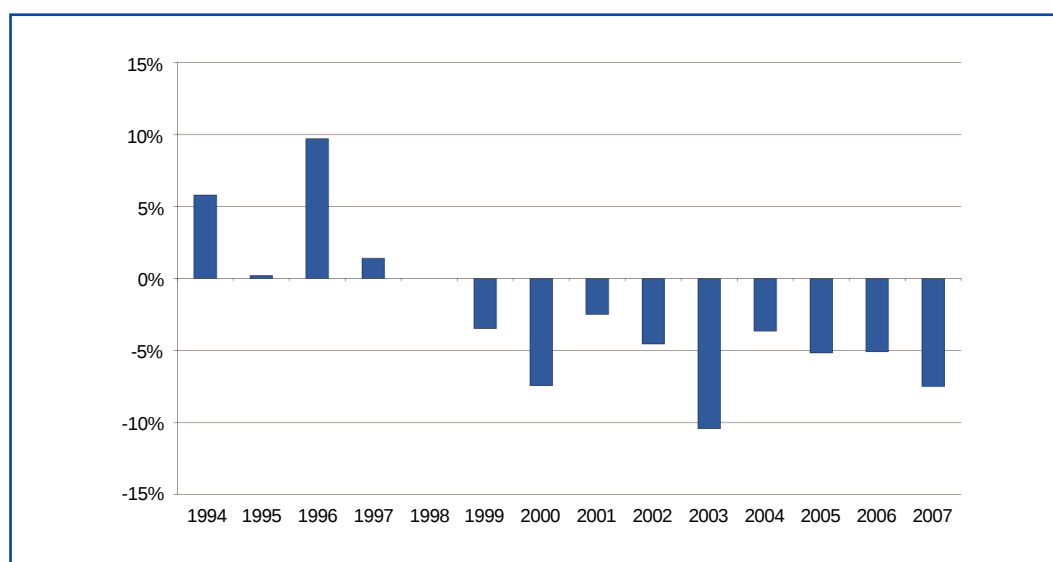
contributing to the economy-wide shrinkage of effective demand.

On the fiscal front, the government has continuously run large budget deficits, financed mainly through domestic banking sector borrowing. By the end of the 1990s, the interest burden on its rapidly growing domestic debt had come to exceed total expenditure leading to a debt trap.³

In real terms GDP growth stood at 5.8 percent in 1994, fell to 0.2 percent in 1995, mainly due to the 1994/95 drought, and rose to its highest level of the decade at 9.7 percent in 1996 before falling to 1.4 percent in 1997. Since the onset of the deepening economic and social decline in 1997, GDP growth has suffered a decline from 0 percent in 1998 to -7.4 percent in 2000 and to -10.4 percent in 2003. Thereafter, real GDP growth has averaged -5.9 percent between 2005 and 2007 (see Figure 2.1).

Zimbabwe's economic decline occurred at precisely the time that other African countries were beginning to achieve reasonable rates of growth. Compared with a cumulative gain of over 40 percent of GDP elsewhere in

Figure 2.1: GDP growth at 1990 prices, 1994–2007

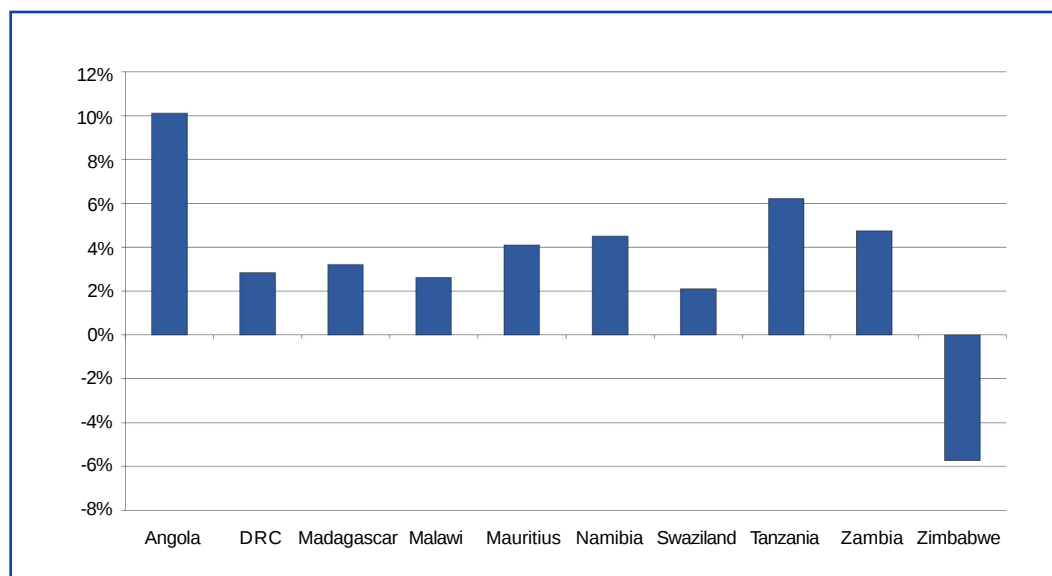


Note: The figure for 2007 is estimated

Source: Central Statistical Office

³ A country falls into a debt trap when it is forced to borrow to pay interest on existing debt. Where there is a primary budget deficit – that is, where non-interest expenditure exceeds revenue – then the total budget deficit will keep growing as debt increases and the cost of servicing that debt rises.

Figure 2.2: Average GDP growth rates of selected SADC countries, 2000–2006



Source: African Development Bank

Africa, Zimbabwe's GDP between 1998 and 2006 declined by –37 percent (Zimbabwe Institute, 2007: 37). Figure 2.2 compares Zimbabwe with a group of ten selected SADC countries with which Zimbabwe had earlier compared favourably in terms of GDP growth. It shows that Zimbabwe dropped to an average *negative* growth for 2000–2006 of 5.7 percent compared to these countries' average positive growth of 4.8 percent during the same period. Even if Angola is removed from this list, because its growth is fuelled by the oil-extractive sector, the remaining eight countries had an annual average growth rate of 4.2 percent over this period, well above that of Zimbabwe.

To these variables must be added the impact of the HIV and AIDS pandemic on the economy. Estimates from UNAIDS and the IMF in Southern Africa suggest that annual GDP growth rates may decrease by 1-2 percentage points as a result of the HIV and AIDS pandemic (see Lisk, 2002). It is estimated that economic growth could be 25 percent lower than it would have been without the pandemic over a 20 year period in high prevalence countries, their populations could be 20 percent lower by 2015, and their labour forces 10–22 percent smaller (ILO, 2000). Data from the 2002 population census suggests that the

intercensal population growth rate declined from 3.9 percent during the period 1982-1992 to 1.2 percent during the period 1992-2002 mainly due to the HIV and AIDS pandemic.

Zimbabwe is one of the worst affected countries by HIV and AIDS in Southern Africa, a region at the epicentre of the global pandemic. At the national level, life expectancy fell dramatically from just over 57 years in 1982 to about 50 years by 1995 and an estimated 39 years in 2003. Life expectancy is estimated at 37 years for men and 34 years for women in 2007. The dramatic decline in life expectancy is a result of the HIV and AIDS pandemic, which saw the HIV adult prevalence rate reach a level of 24.6 percent by 2003. A total of 1.6 million Zimbabweans under 50 years are living with HIV and AIDS. However, recent data from the Ministry of Health and Child Welfare suggest that adult HIV prevalence had declined to 20.1 percent in 2005, 18.1 percent by 2005/06 and 15.9 percent by 2007.

Another feature of Zimbabwe's deep-crisis period is the country's growing fiscal deficit which averaged –6.5 percent during 2000–2006 (Table 2.1). However, the fiscal deficit figure is a serious underestimate given quasi-fiscal expenditures not being reflected in the

Table 2.1: Zimbabwe's macroeconomic indicators, 2000–2006

Indicator	2000	2001	2002	2003	2004	2005	2006
GDP (current US\$ million)	8,135.8	12,882.6	17,875.6	7,913.1	4,712.1	3,372.5	7,033.7
GNP US\$	7,150.0	12,800.0	30,800.0	7,850.0	4,640.0	3,180.0	n.a.
Population	12,595.0	12,698.0	12,786.0	12,863.0	12,936.0	13,010.0	13,085.0
Current account balance (as % of GDP)	−0.4	−1.0	−2.6	−4.6	−5.6	−7.5	−4.0
Fiscal deficit, including grants (% of GDP)	−18.6	−7.0	−2.7	−0.2	−7.6	−6.1	−3.1
GNS per GDP (%)	11.1	7.0	4.9	−1.4	−3.2	−6.7	4.0
Gross official reserves (months of imports)	1.5	0.6	0.7	n.a.	n.a.	n.a.	n.a.
GDP growth rates	−7.3	−2.7	−4.4	−10.4	−3.8	−6.5	−5.1
CPI inflation	55.6	73.4	133.2	365.0	350.0	237.8	1,216.0

n.a. Data not available

Sources: African Development Bank database; IMF (for balance-of-payments current account balance)

national budget. All other major macro-economic indicators are in sympathy with the worsening fiscal account deficit, in particular the current account balance which according to the IMF's figures was also negative throughout this period, averaging −3.7 percent, while growth rates have also been in negative territory throughout the period.

Throughout this period, business confidence has been progressively undermined by public allegations and condemnations by the government of private sector involvement in 'profiteering' and 'economic sabotage'. In addition, national policy incoherence and inconsistency has made forward planning by the private sector an extremely precarious undertaking. Most recently, the Indigenization and Economic Empowerment Act (No. 14 of 2007) – which requires businesses to sell 51 percent of their shares to indigenous Zimbabweans, defined as those people and groups who were disadvantaged under colonial rule – has further compounded this uncertainty.

2.1.5 An overview of the long-haul: the continuous downward trend in economic performance since 1980

The macroeconomic aggregates show an almost continuous downward trend since 1980 (Table 2.2). As the table shows, formal

employment growth declined to just above 0 percent in the 1990s and became negative by the post-2000 period. However, the major sectors of the economy – agriculture, manufacturing and mining – had mixed growth paths, with the first two registering their highest growth in 1996 – 19.8 percent and 14.7 percent, respectively – mining's highest growth was in 1994 (10.8 percent) and 1998 (8.1 percent). Thereafter all the three sectors declined progressively with the decline becoming very steep in recent years.

Track record on inflation management

In order to counter the budget debt trap, the government introduced a policy of suppressed interest rates in 2001, which was combined with a fixed exchange rate and a foreign-currency surrender requirement on exporters. This strategy succeeded temporarily in reducing the burden in the budget of interest payments on the national debt, but at huge cost to the economy as a whole. As expected, negative real interest rates encouraged over-consumption and speculation, particularly in the foreign-exchange market. The parallel exchange rate depreciated rapidly, creating a lucrative wedge for the few who were able to access foreign currency at the official rate and either trade it directly at its market value or import luxury items for resale on the domestic market.

Table 2.2: Zimbabwe's economic performance, 1980–2006

Economic Indicators	1980–1990	1991–2000	2001–2006
Average annual GDP growth (%)	4.30	0.90	–5.70
Employment growth (%)	1.90	0.40	–7.50
End-of-year population (millions)	9.74	11.34	11.95
Formal employment (% of pop.)	12.20	10.90	7.00
Manufacturing VA average growth (%)	4.60	–0.70	–7.40
Manufacturing employment growth (%)	3.00	–0.70	–5.30
Inflation in final year of period (%)	12.00	56.00	238.00
MVI in final year of period (%)	138.10	100.70	67.80
Exports–GDP in final year of period (%)	23.00	43.00	24.00
Manufacturing as % of GDP	20.35	17.70	15.00
Agriculture as % of GDP	16.20	14.90	17.00
Mining as % of GDP	4.30	4.20	4.00
Savings–GDP	16.50*	17.90	–0.10
Investment–GDP	16.00*	19.40	6.30
Budget deficit (% of GDP)	–2.10*	–6.30	–5.80

MVI = Manufacturing Volume Index *Average for 1986–1990 only

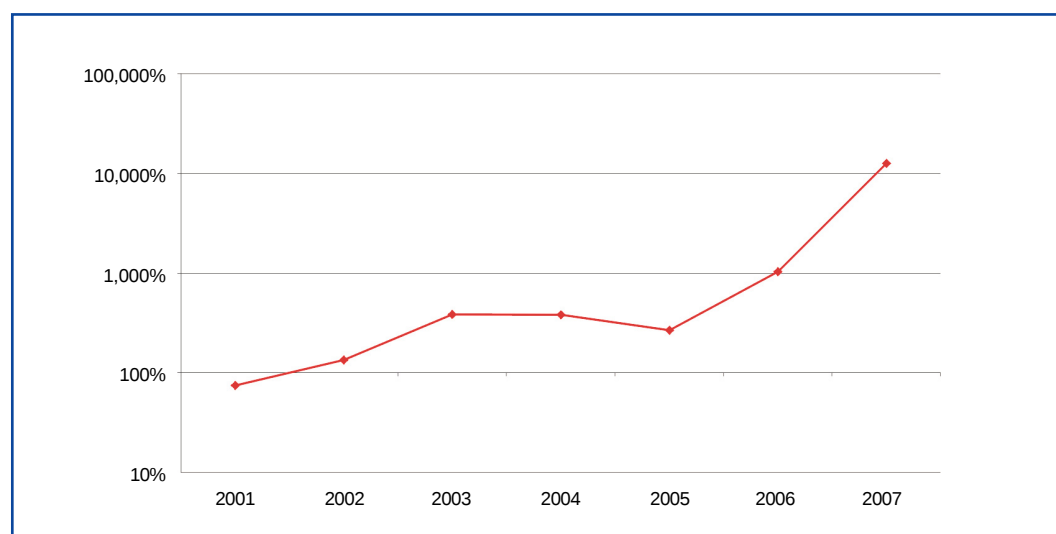
Sources: Central Statistical Office; International Monetary Fund (various publications)

Inflationary pressures had built up from 1997, when it rose from 19 percent in that year to 56 percent by 2000, to over 1,000 percent by 2006, and to an average of 12,563 percent in 2007 (Figure 2.3). Zimbabwe's inflation reached hyperinflation levels in June 2007. At the time of writing, the most recent official estimates (June) was that inflation was over 11.2 million percent year-on-year. Zimbabwe's inflation is fundamentally caused by excess government expenditure, financed

by the printing of money in an economy with a real GDP that has been declining for the last nine years. Money-supply growth has been completely decoupled from economic growth, the inevitable result being continued and accelerating inflation.

Emergency policy initiatives

After 1997, and in response to the recurrent falls in GDP growth rates and employment

Figure 2.3: Zimbabwe's CPI inflation, annual average, 2001–2007

Source: Central Statistical Office

levels, the government announced, with increasing regularity, a succession of turnaround economic blueprints/programmes (Table 2.3). As shown in Table 2.2, notwithstanding these programmes, real GDP has continued to decline every year since 1997.

It may be concluded from the coincidence in the timings of the declining macroeconomic indicators and the unveiling of these successive turnaround programmes that the programmes were either flawed in terms of their analytical content and policy recommendations, or were never implemented in a consistent manner.

2.2 MACROECONOMIC POLICIES AND THEIR IMPACT ON GROWTH AND POVERTY REDUCTION

2.2.1 Fiscal policy

Instead of being supportive of growth and poverty reduction, the government's

macroeconomic policies have often constituted the main binding constraints.

During the 1980s, Zimbabwe's record of social service delivery (education, health, basic services and infrastructure) and public sector growth (civil service, parastatals) was ostensibly impressive. However, this was achieved at a high cost in terms of unsustainably high budget deficits, whose harmful effects were high inflation and the crowding out of private sector credit. As shown in Table 2.2, the budget deficit rose from an average of -2.1 percent of GDP between 1980 and 1990, to -6.3 percent between 1991 and 2000, and -5.8 percent between 2001 and 2006.

2.2.2 Investment, gross fixed capital formation and savings ratios

The investment-GDP ratios, gross fixed capital formation (GFCF),⁴ and savings-GDP ratios in Figures 2.4, 2.5 and 2.6 show marked declining trends from 1996, with even more significant deterioration in performance after 2000.

Table 2.3: Zimbabwe's economic planning programmes, 1998–2008

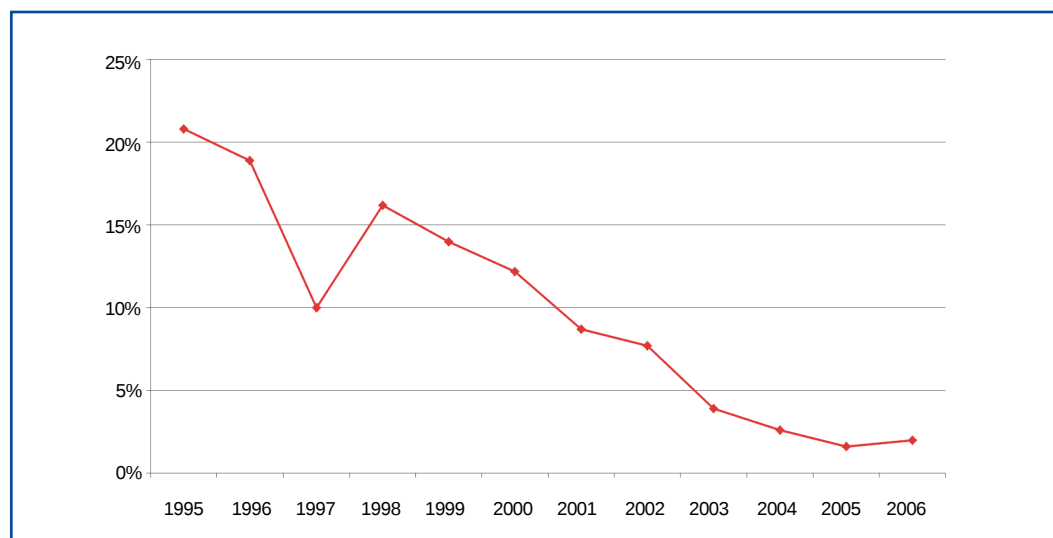
Date	Economic blueprint/plan	Responsible authority
29 Jan 1998	Vision 2020 and Long-Term Development Strategies*	National Economic Planning Commission, Office of the President and Cabinet
20 Feb 1998	Zimbabwe Programme for Economic and Social Transformation (ZIMPREST)	Ministry of Finance
28 Mar 1998	Three-Year Medium-Term Development Plan	National Economic Planning Commission, Office of the President and Cabinet
August 2001	Millennium Economic Recovery Programme (MERP)	Ministry of Finance
April 2003	National Economic Revival Plan (NERP)	Ministry of Finance
November 2004	Macroeconomic Policy Framework, 2005–2006	Ministry of Finance
April 2006	National Economic Development Priority Programme (NEDPP)	Ministry of Economic Development
Ongoing	Zimbabwe Economic Development Strategy (ZEDS)	Ministry of Economic Development

* Submitted for consideration by the National Economic Planning Commission and Cabinet, but was neither approved nor released.

⁴ Gross fixed capital formation is measured by the total value of a producer's acquisitions, less disposals of fixed assets during the accounting period, plus certain additions to the value of non-produced assets (such as subsoil assets or major improvements in the quantity, quality or productivity of land) realized by the productive activity of institutional units.

AFTER 1997, AND IN RESPONSE TO THE RECURRENT FALLS IN GDP GROWTH RATES AND EMPLOYMENT LEVELS, THE GOVERNMENT ANNOUNCED, WITH INCREASING REGULARITY, A SUCCESSION OF TURNAROUND ECONOMIC BLUEPRINTS/PROGRAMMES

Figure 2.4: Investment–GDP ratios, 1995–2006



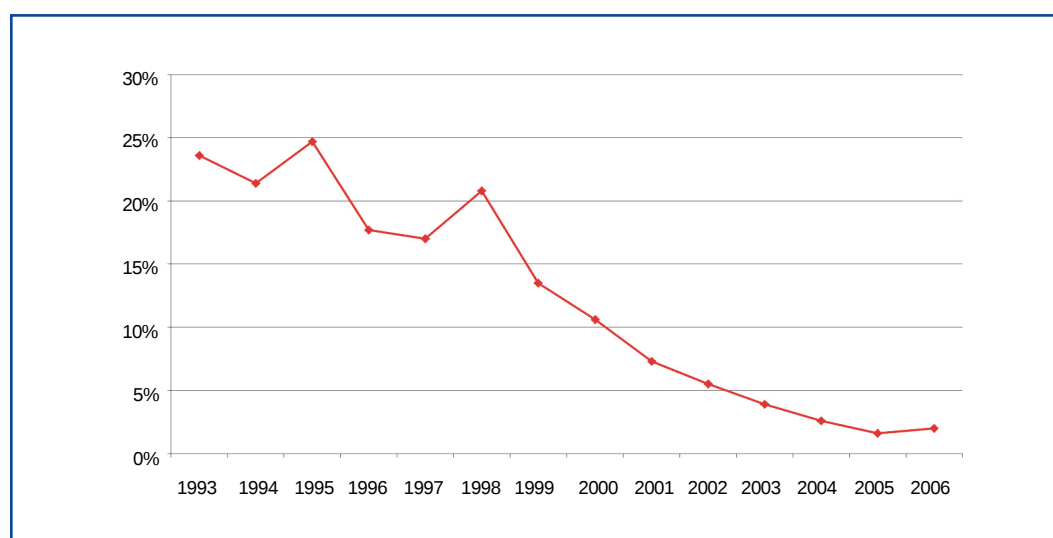
Source: Central Statistical Office, Quarterly Bulletin of Statistics, various issues

Investment as a percentage of GDP declined from an average of 15 percent in the 1995–2000 period to 4 percent from 2000 to 2006. The collapse of investment is further corroborated by the decline in the figures of gross fixed capital formation (GFCF) in Figure 2.5 below which declined from an average of 23 percent in between 1995 and 1997 (the onset of the deepening crisis), picking up slightly to 25 percent in 1998 before declining precipitously in the post-2000 period. GFCF in the 2000–2006 period averaged only 6 percent, declining to 2 percent in 2005 (Figure 2.5). These figures

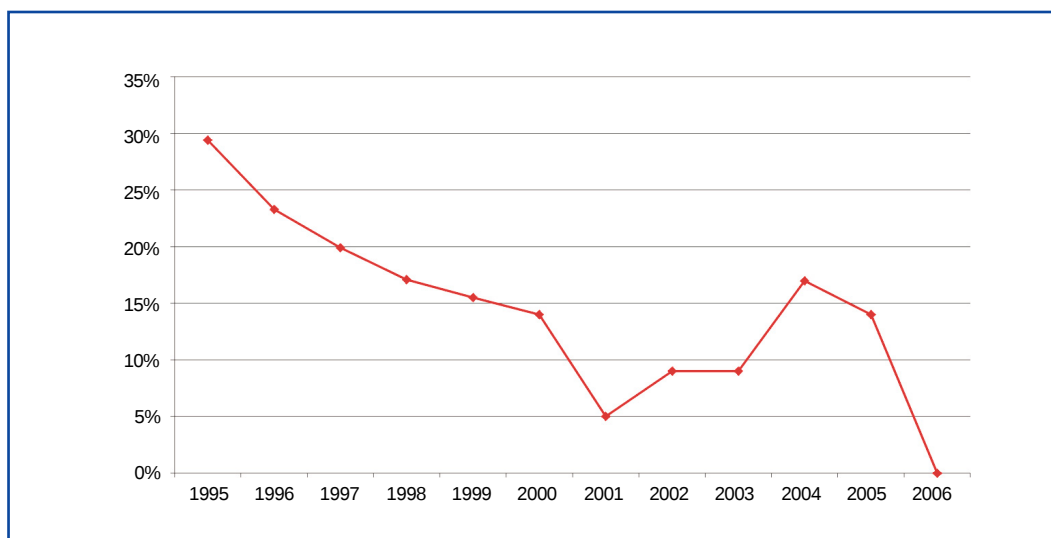
are dwarfed by the performance of GFCF in the pre-independence period, which averaged 24 percent between 1970 and 1974, and 17 percent between 1975 and 1979 (Zimbabwe, 1982: 5–6).

Another important indicator of the country's regression can be seen in terms of its gross national savings (GNS) as a percentage of GDP. This variable is important, given that increasing aggregate savings and investment are key contributors to growth. According to the CSO figures, the savings–GDP ratio declined from 28 percent in 1995 to a low of

Figure 2.5: Gross Fixed Capital Formation (GFCF) as percentage of GDP



Source: Central Statistical Office

Figure 2.6: Savings–GDP ratios, 1995–2006

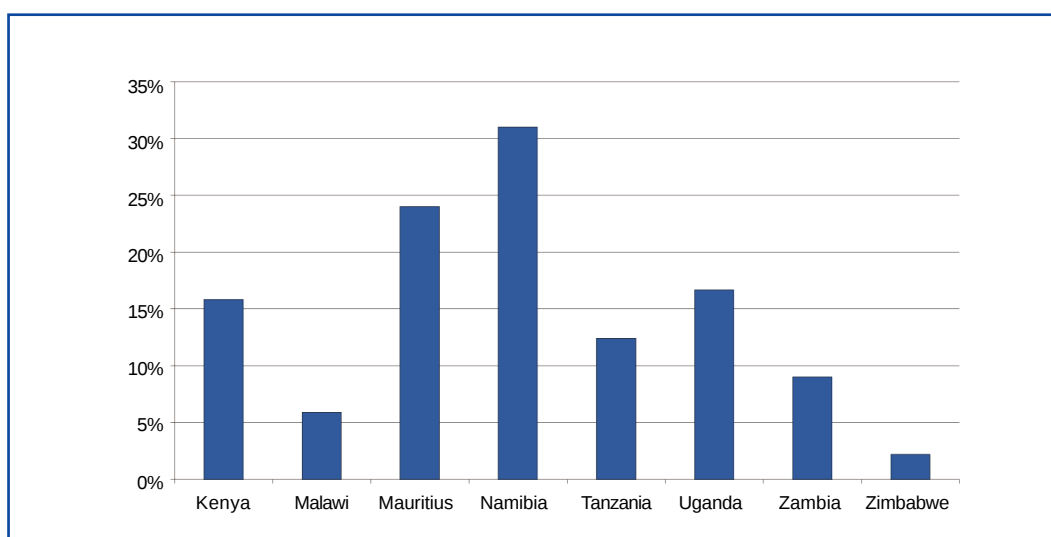
Note: The savings figure for 2006 is an estimate

Source: Central Statistical Office Quarterly bulletins (various issues)

Table 2.4: Gross national savings as percentage of GDP in selected regional economies

	2000	2001	2002	2003	2004	2005	2006	Average growth 2000-06
Kenya	15.7	16.1	18.5	17.2	14.2	14.6	14.3	15.8
Malawi	8.3	7.0	−0.8	3.3	5.1	8.6	10.0	5.9
Mauritius	25.8	26.0	26.0	27.3	23.7	19.6	19.7	24.0
Namibia	30.4	26.6	25.2	34.9	35.7	31.3	32.6	31.0
Tanzania	12.1	11.8	12.1	13.8	14.3	12.9	10.0	12.4
Uganda	12.5	14.3	14.5	14.8	21.5	21.1	18.2	16.7
Zambia	0.7	−0.8	6.7	10.7	14.0	15.2	16.4	9.0
Zimbabwe	11.1	7.0	4.9	−1.4	−3.2	−6.7	4.0	2.2

Source: AfDB Statistics Department and World Economic Outlook (September 2006)

Figure 2.7: Gross national savings as a percentage of GDP, 2000–2006

Source: AfDB Statistics Department and World Economic Outlook (September 2006)

5 percent in 2001, rising to 17 percent in 2004 before slightly dropping to 14 percent in 2005. A wide gap in figures between the official CSO figures and the AfDB's (African Development Bank) is shown by the differences in averages in the period 2003–2005. While the CSO records a positive savings–GDP average ratio of 14 percent, the AfDB comes up with a wide negative figure of 3 percent during the same period (Figure 2.6 and Table 2.4).

When compared to a select group of countries in the East and Southern African region, Zimbabwe lagged behind them all in GNS as a percentage of GDP from 2000 to 2006 (Figure 2.7), e.g., while Namibia and Mauritius top the list at 31 percent and 24 percent, respectively, Zimbabwe lagged behind at 2.2 percent.

2.2.3 Decapitalization and disarticulation of the economy

In the current situation, the impact of the macroeconomic variables on the structure of the Zimbabwean economy is schematically represented in Table 2.5.

Leaving aside the mining sector, which is currently on the ascendant, all other productive sectors – agriculture, manufacturing, and tourism – are on the decline. While productive investments are on the decline, speculative activities are on the ascendant. An increasing volume of economic activities are taking place outside the formal economy. There has been an overall reduction in the number of formal-sector economic units, as well as significant downsizing of the same. This has been accompanied by fundamental breakages in inter-sectoral linkages, such as the previously symbiotic nexus between the manufacturing sector and large-scale commercial agriculture,⁵ and a significant decline in the role of commercial banks as providers of finance to the private sector.⁶

2.2.4 Deepening poverty

The 2003 Poverty Assessment Study Survey (PASS II) showed that 72 percent of the population was living below the Total Consumption Poverty Line (TCPL), compared to 55 percent in 1995.⁷ This represents a 30 percent increase in the

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MANUFACTURING
SECTOR AND
LARGE-SCALE
COMMERCIAL
AGRICULTURE

Table 2.5: Main features of the Zimbabwe economy under crisis

<i>Declining</i>	<i>Growing</i>
Agriculture	Mining*
Manufacturing	Distribution and trade
Tourism	Telecommunications, finance, real estate
Private sector	Public sector
Formal economy	Informal sector
Domestic output	Foreign trade
'Real' investment	'Financial investment' (speculation)
Large formal firms and farms	SMEs/subsistence farming
<i>Diminishing</i>	<i>Increasing</i>
Middle-income segment	Low-income segment
Income from domestic employment	Diaspora remittances
Differentiation - style, quality, branding	Down-trading and cost leadership
Skills and entrepreneurship	Low skills and low technologies

* The mining sector may be growing in value terms but not in volume

⁵ See chapters 6 and 9 on private sector development and agriculture respectively.

⁶ See chapter 5 on the financial sector.

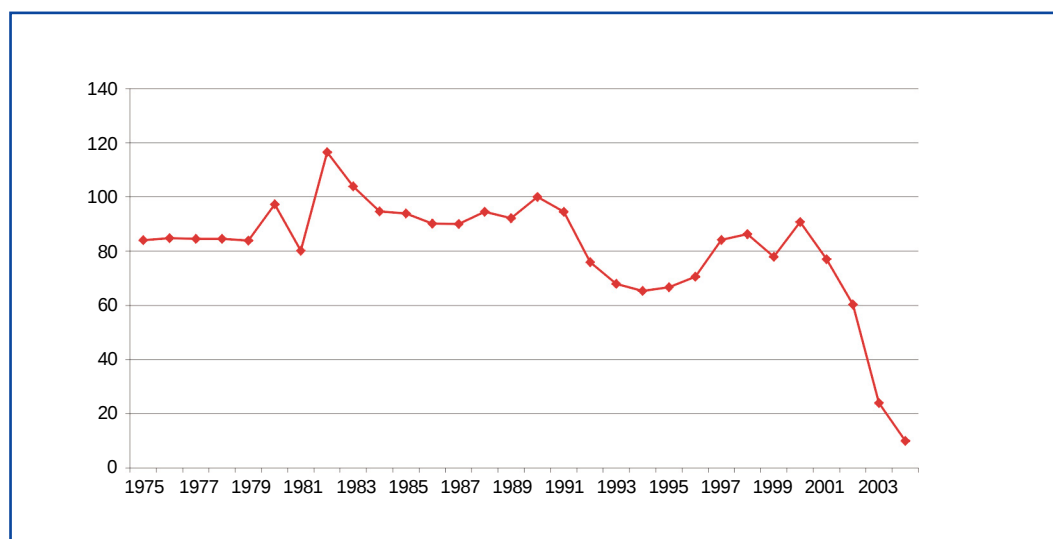
⁷ The TCPL is an income metric definition reflecting the minimum monthly income required by an individual to meet both basic food and non-food requirements.

incidence of poverty (Zimbabwe, 2006b: 61). The challenge of meeting the Millennium Development Goal target of halving the proportion of the population below the TCPL to 36 percent by 2015 has significantly increased.⁸ A similar trend can be observed with regard to the Gini coefficient of inequality⁹, which increased from 0.53 in 1995 to 0.61 in 2003. In addition, poverty took on an increasingly rural and woman's face, reflecting the latter's weak integrability capacity and their location in the marginalized segment of Zimbabwe's dual economic structure.¹⁰ Significant job losses have occurred with de-industrialization, and real wages have declined (see below). Given a rapidly contracting revenue base, the state reduced its investment in education, health, housing and other public services, and as a result social conditions among the poor have deteriorated markedly. Collapsing incomes and increasing poverty have in turn, translated into low levels of effective demand for goods and services. This has contributed

to significant underutilization of existing factory and shop capacities, as well as extensive environmental degradation, as people scavenge for firewood, water and other possible means of survival.

The vertiginous decline in terms of purchasing power is shown in Figure 2.8. Real average earnings peaked at an index of 120 in 1982, when wages were adjusted in line with the Poverty Datum Line as recommended by the Riddell Commission.¹¹ However, following the adoption of a wage-restraint policy in 1983, real wages fell, a trend that was repeated during the period of ESAP (1991–95) following the deregulation of wage-setting and rising prices. A period of worker militancy resulted in an increase in real wages between 1995 and 2000. But, by 2004, real average earnings were far lower than during the last years of the UDI period (1975–79), having collapsed to 10 on the real earnings index. The Zimbabwean economic crisis has seen demand become entrenched at very low

Figure 2.8: Average real earnings index, 1975–2004 (1990 = 100)



Source: Unpublished Central Statistical Office data

⁸ The status of the Millennium Development Goal was assessed in Zimbabwe & United Nations (2004), Zimbabwe Millennium Development Goals: 2004 Progress Report, Harare.

⁹ The Gini coefficient is the most commonly used measure of inequality. The coefficient varies between 0, which reflects complete equality, and 1, which indicates complete inequality.

¹⁰ Dualism is the co-existence of two distinct and different sectors in an economy, with few linkages between them. In the case of Zimbabwe, one is made up of the communal areas (with predominantly peasant-based farming activities) and an urban informal sector, while the other is a modern, commercially oriented and formal sector, consisting of industry, services, mining and commercial agriculture.

¹¹ Zimbabwe Report of the Commission of Inquiry into Incomes, Prices and Conditions of Service [Chairman: R. Riddell]. Government Printer, Harare, 1981.

levels as a result of both falling real incomes and shrinking producer and consumer markets.

2.3 ZIMBABWE'S EXTERNAL POSITION

2.3.1 Debt structure over time

With persistent budget deficits, added to new borrowing requirements each year, and with these deficits being incurred primarily to support recurrent expenditure rather than investments in infrastructure or productive assets, the debt burden increased significantly. Up to 1994 total debt (domestic and external) was less than 60 percent of GDP, but from 1995 total debt rose sharply, reaching 90 percent of GDP in 2000, 115 percent in 2006, and 189 percent (estimate) in 2007.

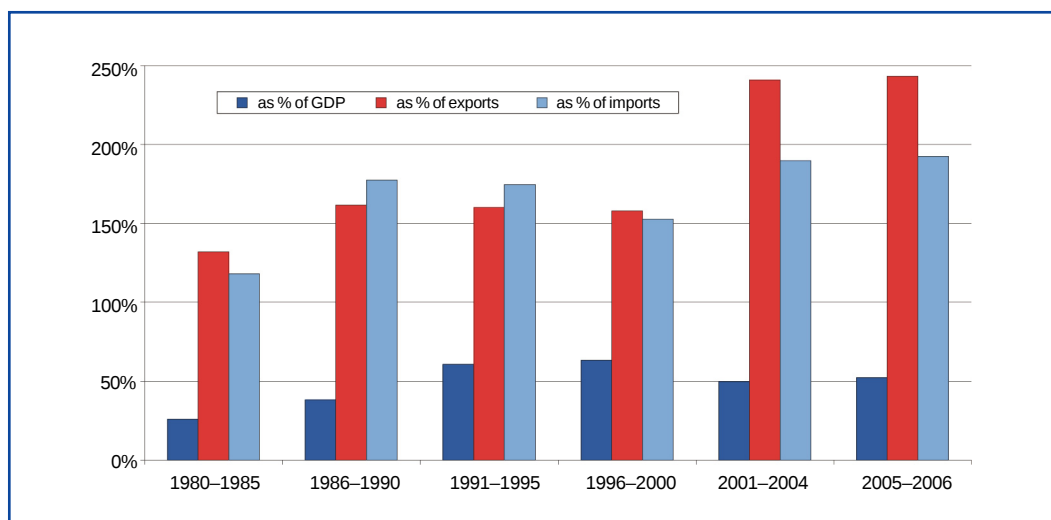
This has been coupled with an apparent attempt by the government to reduce its debt burden through the fuelling of inflation. During 2005 and 2006 the country's external debt averaged 53 percent of GDP,¹² 243 percent of exports and 192 percent of imports (Figure 2.9).

Zimbabwe began to default on its foreign-debt payments in 2000. Since 2000 the foreign-debt stock from the OECD countries has not increased significantly, and its increase as a proportion of GDP has been the result of relative price changes and a declining GDP. According to IMF data, the debt-service ratio increased from 24 percent in 2000 to an average of 30 percent over the period 2001–2004. Reported foreign-exchange reserves are at extremely low levels, with net effective reserves (taking into account contingent liabilities) being deemed by the IMF to be negative.

With the drying up of capital flows since 1997, Zimbabwe's external debt profile deteriorated rapidly, and the country ran up arrears in excess of US\$3 billion, including the 'pipeline' of current transfer payments for the year 2007 alone of US\$450 million. In fact the real extent of external indebtedness is unknown, partly because of the contingency liabilities of the government and the central bank in respect of offshore loans for which they have provided guarantees, partly because the full extent of the current payments pipeline is unknown, and also because details of loans from non-OECD countries such as China, India, Iran and Venezuela are not in the public domain.

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AND SHRINKING
PRODUCER AND
CONSUMER
MARKETS*

Figure 2.9: Zimbabwe's external debt structure, 1980–2006



Source: World Bank database

¹² The IMF (2008) estimates it to have reached 100 percent by the end of 2006, compared to an average of 21 percent for the sub-Saharan African region.

2.3.2 Foreign trade

Throughout the post-independence period, shortages of foreign currency have been a major constraint on economic growth and are largely attributable to weak export performance. Table 2.6 shows that average export and import growth (in US dollars) during the 1980–2007 period were on average higher than in the deepening crisis period of 1997–2007. Prior to the onset of economic decline, during the liberalization period (1990–1996) both export and import growth averages were the highest in terms of the whole post-independence period (Table 2.6).

At their peak in 1996 and 1997 exports of goods and services reached US\$3,090 million

and US\$3,168 million respectively, while imports accounted for US\$3,074 million and US\$3,759 million (Figure 2.10). Exports had started to peak with a time lag, i.e., at the end of ESAP, thereafter declining to US\$1,694 million in 2004 (US\$2,067 million for imports).

Exports per capita declined and stagnated during the 1980s before recovering strongly in the ESAP period, peaking in 1997, but since then they have halved. Figure 2.11 shows that per capita exports have declined by more than a third since 1980. As with exports there was a strong recovery in imports during the liberalization phase, but by 2007 imports per capita were 35 percent lower than at independence.

Table 2.6: Foreign Trade 1980–2007

Growth rates	Control regime (1980-1989)	Economic liberalization (1990-1996)	Deepening crisis 1980-2007	Average for (1997-2007)
% exports growth p.a.	2.2	6.7	−4.5	0.4
% imports growth p.a.	5.2	6.5	−4.0	0.3
Exports/GDP	24.5%	27.4%	32.9%	29.3% (1980–2006)
Imports/GDP	27.4%	35.5%	35.8%	32.8% (1980–2006)
Current account balance (% of GDP – average)	−3.8	−5.2	−7.0 (1997–2005)	−6.0 (1980–2005)
Terms of trade (1980 = 100)	111.0	107.0	116.5	111.0

Sources: World Bank: *African Development Indicators* (various editions). IMF Regional Economic Outlook for sub-Saharan Africa (various editions) and World Economic Outlook Database (2008); Reserve Bank of Zimbabwe: *Quarterly Monetary Policy Statements* (various editions); Central Statistical Office, Harare: *Quarterly Digest of Statistics and National Accounts* (various editions)

Figure 2.10: Export and import revenues

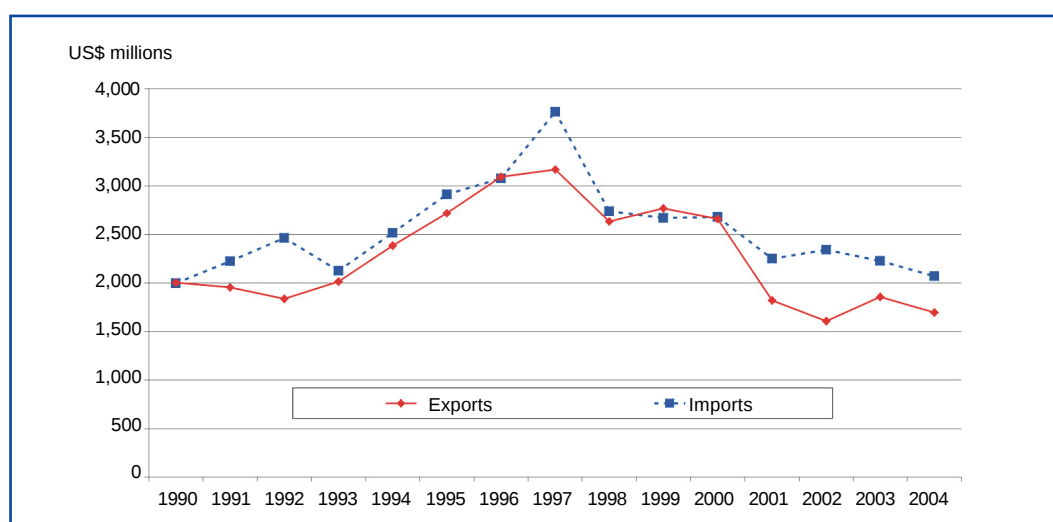
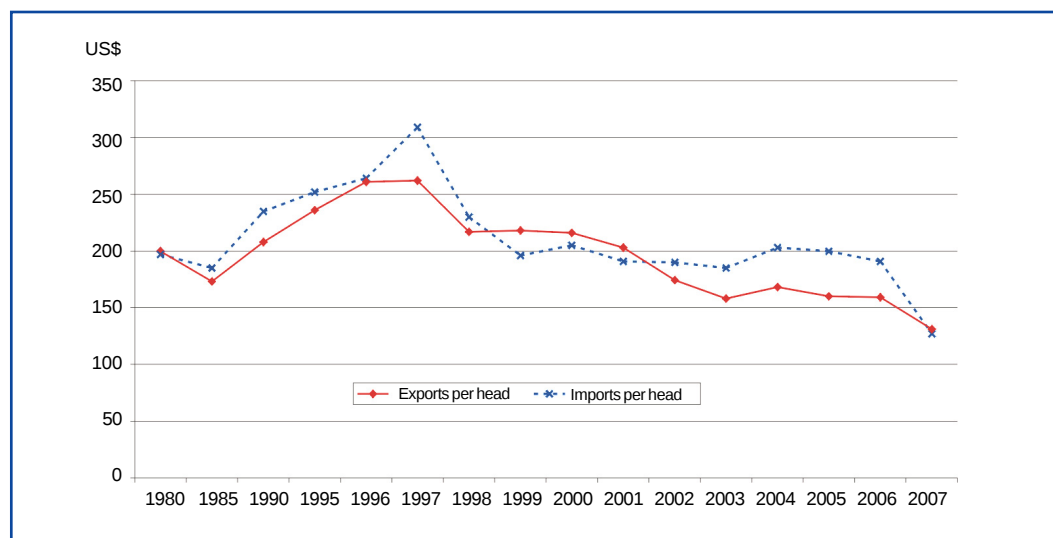


Figure 2.11: Exports and imports per capita, 1980–2007 (US\$)



Source: Central Statistical Office

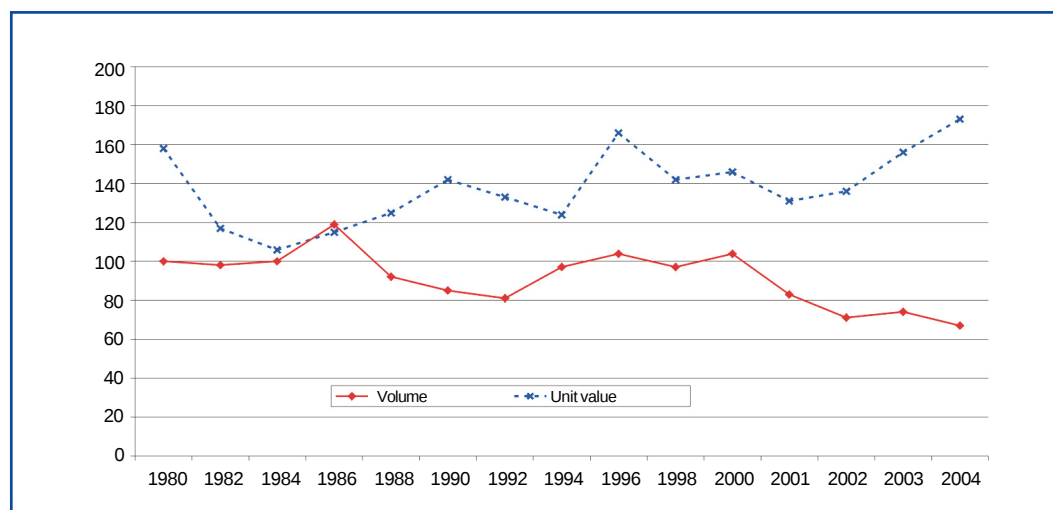
Even more striking is the weak performance of export volumes. These peaked in 1987, with a 28 percent increase on the figure for 1980. But as Figure 2.12 shows, by 1990 volumes had fallen by a third from their record 1987 levels. Exports reached their peak in 1996 in value terms, but volumes were only 4 percent higher than in 1980. Indeed, in only six of the twenty-five years for which volume data are available were exports greater than in 1980. By 2004, export volumes were one third below 1980 levels.

Figure 2.12 indicates that export revenues may have been sustained by strong export prices, which to some extent offset falling

volumes, especially since the start of the commodity price super-cycle in 2002/3. At the end of the 25-year period (1980–2004), however, export prices (in US dollars) were only modestly higher (up 9.5 percent) than in 1980. Indeed, for most of the period export prices were below 1980 levels. Despite this, Zimbabwe's terms of trade (1980=100) averaged 111 over the entire period (1980–2007), reflecting the fact that although export prices were depressed for most of the period, import prices were even more so.

No single factor explains Zimbabwe's poor export performance. Figure 2.12, does however, indicate that part of the

Figure 2.12: Index of export volumes and prices (1980=100)



Source: Central Statistical Office, International Monetary Fund

Table 2.7: Sectoral composition of exports, 1981–2007

% shares	1981	1990	1996	2000	2007 (provisional)
Agriculture	42.3	43.5	46.1	51.1	32.0
Mining	37.0	40.6	30.1	30.5	50.6
Manufacturing	9.9	14.1	21.0	15.5	16.8
<i>Main exports</i>					
Tobacco	22.0	20.1	30.5	30.6	16.7
Gold	7.5	13.8	12.3	12.1	
Ferrochrome	7.8	9.0	7.0	8.6	
Cotton	6.3	6.5	4.7	7.4	

Sources: Central Statistical Office; Reserve Bank of Zimbabwe

explanation rests with a weak supply-side response, especially during the crisis period which both export volumes and revenues have declined despite buoyant international commodity prices. Three other explanations stand out:

- Deteriorating competitiveness, as measured in the World Economic Forum's Global Competitiveness Index and the World Bank's Doing Business indicators.¹³
- An overvalued exchange rate during both the control regime period of the 1980s and the 2000–2007 deep crisis period.
- A significant change in the composition of Zimbabwe's export basket, evidenced by a growing reliance on mining and commodity exports with minimal value-addition, and a commensurate decline in exports of manufactured goods, especially medium and high-tech manufactures.

Table 2.7 shows that exports of manufactured goods reached their peak in terms of market

share in the late 1990s and have since declined, as have that of agriculture, mostly owing to the sharp contraction in the value of tobacco exports. The mining industry currently accounts for just over half of the total exports.

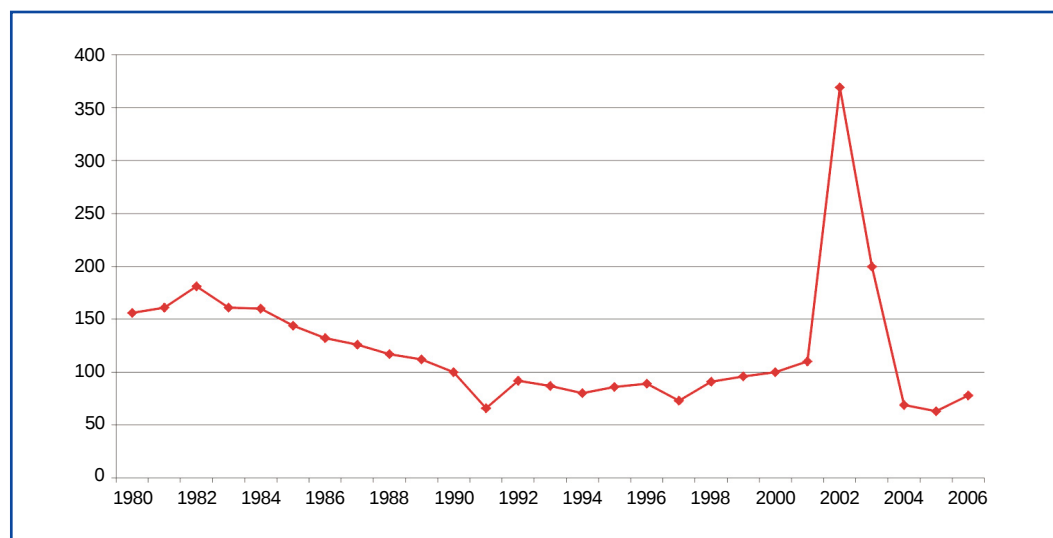
2.3.3 Exchange-rate policy

Figure 2.13 shows that the real effective exchange rate (REER) for the Zimbabwe dollar depreciated from 158 at independence in 1980 to 100 ten years later.¹⁴ During the 1990s, the REER depreciated further to average 84 over the decade, suggesting that despite the exchange rate, it was considerably more competitive during this reform decade than under the control regime of the 1980s – the more so given the fact that Zimbabwe's export prices were more favourable than the average for sub-Saharan Africa over the decade.

The REER was massively overvalued during the 2001–2003 period and while it returned to competitiveness in 2004/5 as hyperinflation took hold, it escalated to reach an estimated 74 in 2007 (IMF, 2008).

¹³ See chapter 6 on private sector development.

¹⁴ The REER is the weighted average of a country's currency relative to an index or basket of other major currencies measured in nominal exchange rates. The REER can also be understood in the context of the Real Exchange Rate (RER), defined as the relative price of tradables to non-tradables, which indicates the degree of competitiveness or profitability of the tradable-goods sector in the domestic economy. For example, an increase in RER will make the production of tradables relatively more profitable, inducing resources to move out of the non-tradables sector into the tradable sector.

Figure 2.13: Zimbabwe Real Effective Exchange Rate (REER) (1980–2006) (1990=100)

Source: *World Bank: African Economic Indicators (various editions); IMF Regional Outlook for sub-Saharan Africa (various editions)*

2.3.4 The balance of payments

For most of the pre-crisis period Zimbabwe ran a visible trade surplus that was more than offset by the deficit on invisible transactions, leaving a current-account deficit averaging 3.7 percent of GDP in the 1980s, 4.3 percent in the 1990s, and 3.7 percent from 2000 to 2006 (Table 2.8). Reflecting declining output and growing import dependence, the visible trade balance turned negative in 2002 and has since remained in the red.

On their own such figures are largely meaningless to the extent that they disguise the underlying macroeconomic and institutional factors at work. In the early 1980s imports were constrained by limited access to foreign currency and highly bureaucratic import-licensing and allocation systems. Liberalization after 1990 led to a short-term surge in imports (1991–1997) that

was followed by a transformation in the structure of imports as the demand for capital goods and intermediates fell away during the crisis period, to be partially replaced by increased food, electricity, fuel and most recently, consumer imports.

The current account figures also camouflage changing capital account profiles. In the 1990s Zimbabwe attracted very little Foreign Direct Investment (FDI), especially when the US\$450 million Hartley Platinum project is excluded. Bank lending was negative, while foreign aid disbursements were volatile, partly reflecting food crises (1982–83, 1992–94 and 2002 onwards) and since 1997, deepening donor unhappiness with the policies of the Zimbabwe government.

Table 2.9 captures the key capital account magnitudes, showing that there was a net outflow of private sector finance over the

Table 2.8: Zimbabwe: Balance of payments on current account

% of GDP	1980–1989	1990–1999	2000–2006
Exports of goods and services	28.0	36.0	27.0
Imports of goods and services	31.0	30.0	29.0
Visible trade balance	3.2	0.9	–0.5
Current account balance	–3.7	–4.3	–3.7

Sources: *World Bank: African Development Indicators (various editions); IMF Article IV Reports on Zimbabwe (various editions)*

Table 2.9: Long-term aggregate net Resource Flows, 1980–2005

Years	FDI	Portfolio	Bonds, bank & trade finance	Foreign aid	Total
US\$ millions					
1980–1989	–115	0	–115	1,950	1,720
1990–1999	420	100	–610	3,950	3,860
2000–2005	226	1	–112	935	1,050
Total	531	101	–837	6,835	6,630
% Shares	8%	1.5%	–12.5%	103.0%	100.0%

Source: *World Bank Debt Tables; Global Development Finance (various editions)*

ONE
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MANAGEMENT

1980–2005 period. In terms of net resource flows (excluding aid) the table shows that there was a net outflow of private sector finance over this period of US\$205 million due to the reduction in bank and trade finance lending which was negative. In other words, since 1980 Zimbabwe has been wholly reliant on official inflows of some US\$6.8 billion, partly offset by a net outflow of US\$205 million in private finance. Even during the post-2000 period the net inflow of aid funding, averaging US\$155 million annually, was only 23 percent less than the US\$195 million annually received during the 1980s.

2.4 MACROECONOMIC STABILITY AS A PRECONDITION FOR SUSTAINABLE GROWTH AND RECOVERY

The key constraint that has impeded growth in Zimbabwe and which needs to be tackled in order to trigger a sustainable, broad-based, pro-poor recovery dynamic is macro-economic instability. One overarching strategic objective in a recovery scenario will therefore be the return to sound macro-economic management.

In support of this, it is imperative that a process of institutional reforms be undertaken in order to build a developmental orientation within the post-crisis administration.

2.4.1 Sound macroeconomic management

Following a short-term macroeconomic stabilization programme, aimed at rapidly bringing down inflation and correcting price and exchange-rate distortions,¹⁵ a longer-term macroeconomic management framework should be put in place and contain the following key features:

Fiscal discipline

As shown earlier, the lack of fiscal discipline throughout the recent post-independence period has consistently had an adverse impact on growth. Having begun with the 1997 recourse to unbudgeted expenditures, the situation is now characterized by quasi-fiscal expenditures that outweigh budgeted expenditures. The resultant high inflation has reduced aggregate domestic demand, crowded out the private sector, and brought about the disarticulation of the economy and the collapse of real productive investment. Properly coordinated fiscal and monetary policies will be required in order to put the economy back on a sound footing.

Such financial conservatism imposes strong requirements, but these must be weighed against the overall objectives of public policy. Macroeconomic stability should not be treated as a stand-alone policy objective and the sole concern of government economic policy, irrespective of social costs given the

¹⁵ See chapters 3 and 6 on stabilization and private sector development respectively.

essential role of public expenditure in providing the means and conditions for the poor to integrate into growth dynamics through the strengthening of their capabilities.

Equitable, transparent and effective revenue collection

There has been an ongoing contraction of state revenues owing to the collapse of economic activity in the formal sector. In addition, tax evasion has been growing, in view of the decreasing capacity of revenue-collection authorities, as well as corruption. There is therefore a need to formalize the informal sector in order to expand the revenue base,¹⁶ as well as to restructure and modernize Zimbabwe Revenue Authority (ZIMRA). Such measures will help to address the perennial problem of Zimbabwe's low tax–GDP ratio, which is a key contributor to the state's limited financial capacity to provide essential social services and maintain infrastructure.

Sound and transparent budget system

A return to sound budgetary processes (allocation, expenditure, accounting and impact assessment) is not only key to assuring the judicious and effective use of state resources but will also help to restore the transparency of government transactions and strengthen the accountability of government and public institutions that are funded through the budget.

A competitive exchange-rate regime

Throughout Zimbabwe's post-independence history, shortages of foreign currency and the appreciation of the exchange rate have been major constraints to growth, in particular for export-oriented sectors. As shown above, Zimbabwe's precipitous decline in international competitiveness can largely be attributed to the maintenance of an uncompetitive exchange rate throughout

most of the post-independence period. The challenge of ensuring a competitive exchange rate will be heightened in a post-crisis scenario, which may be characterized by a significant inflow of foreign exchange in the form of overseas development assistance. Mitigation measures may be required in order to deal with the dangers of Dutch Disease under this scenario.¹⁷

Firm commitment to price stability

In the post-stabilization period the government should show a firm commitment to price stability by adopting an inflation-targeting regime, but one that recognizes that this does not entail targeting zero inflation and anti-deficit fundamentalism. The need to preserve a degree of fiscal policy space for Government, particularly during the process of recovery, must be factored into decisions regarding the fiscal stance and monetary policy to be adopted. What is clear however, is that institutional arrangements should be put in place that confer/restore independence in terms of monetary management to the central bank,¹⁸ and the clear separation of powers in terms of responsibility over fiscal policy (Treasury) and monetary policy (the central bank).

2.4.2 Institutional reform to build a developmental state

A developmental state is one that shows a clear commitment to a long-term national development agenda, has solid capacity and reach, and seeks to encourage growth and poverty reduction, and ensures the provision of essential public services.

A developmental state:

- invests in human capital
- soundly manages public finances
- engages in effective public borrowing

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¹⁶ See chapter 6 on private sector development.

¹⁷ See chapter 4 on aid flows.

¹⁸ See chapter 5 on recovery of the financial sector.

- engages in sound management of state assets
- is an efficient provider of infrastructure
- engages in market formation and deals efficiently with market failures
- is able to stimulate the domestic private sector
- has autonomy from the pressures of interest groups
- ensures respect for property rights.

GIVEN RECENT HISTORY, THE IMPORTANCE OF RESPECT FOR PRIVATE PROPERTY RIGHTS WILL NEED TO BE REAFFIRMED BY THE POST-CRISIS STATE

Given recent history, the importance of respect for private property rights will need to be reaffirmed by the post-crisis state. This will be key to restoring the confidence of both domestic and foreign investors, and is a *sine qua non* for raising and sustaining savings and investment ratios. It will constitute a central pillar of a predictable economic environment, on the basis of which it will be possible for economic agents to move away from the current, short-term survivalist strategies that are being pursued, and to engage in longer-term planning.

Institutional overlap

As shown throughout other chapters of this document, the deep-crisis period in Zimbabwe has seen a proliferation of state and semi-state institutions, many of them with unclear and overlapping mandates.¹⁹ Resources have increasingly been used simply to support the recurrent costs of maintaining these entities, with a diminishing percentage being directed to achieving concrete development objectives. An immediate requirement in a post-crisis scenario will be an in-depth audit of these entities, their utility and value-added, with a view to initiating an extensive programme of rationalization.

Policy unpredictability and incoherence

As mentioned above, one key feature of a developmental state is its capacity to both develop and pursue a long-term development vision. As shown in this chapter, policy incoherence, poor implementation rates, and the constantly shifting sands of national frameworks have seriously undermined the credibility of the state, led to the marginalization of the private sector, and constrained the scope for both state and non-state actors to engage in long-term forward planning. A multiplicity of decision-making bodies, often working at cross purposes, pursuing disconnected agendas without any apparent coordination and with increasingly short-term planning horizons, has been a key feature of public policy during the crisis period. In a recovery scenario, there is an imperative need for a single, technically sound and overarching national development strategy in which the roles and responsibilities of both state and non-state actors are clearly defined, and in which the former is assigned the role of facilitator rather than omnipresent economic agent.

Capacity

Throughout this document it is shown that physical capacity problems arising from decaying infrastructure and disinvestment by the private sector as a response to an unstable macroeconomic environment have become binding constraints to economic growth. In addition, the flight of skills from both the private and public sectors through out-migration has debilitated human capacity in both. The return of skills in the area of macroeconomic management and planning techniques in general will be essential for the development of sound national recovery policy frameworks. This should be accompanied by the retraining of existing staff, aimed at familiarizing them with the

¹⁹ See, in particular, chapters 7, 8 and 10 on labour markets and human capital formation, agriculture and land policy, and public enterprises respectively.

latest thinking on development issues and gradually weaning them off the prevailing dirigiste mindset in which the role of the state is all-pervasive.

2.5 CONCLUDING REMARKS

As this chapter has sought to demonstrate, Zimbabwe's post-independence development model ran into problems long before the current crisis, and with the exception of the first few years after 1980, has consistently failed to deliver robust growth rates. In addition, apart from a brief flirtation with free markets under ESAP, the management of the economy has been characterized by extensive – and in many cases counter-productive – state interventions in the economy. There has been continuous recourse to unsustainable fiscal deficits, without the necessary attention being paid to issues of productivity and growth.

While investments over time in human capital through expanded social sector programmes (health and education) are valid development objectives in themselves, it is also the case that they can be maintained and expanded only on the basis of a growing government revenue base, which itself presumes an expansion of the productive base of the economy. Some consequences of this lack of attention to issues of productivity, international competitiveness, and the importance of the role of the private sector in wealth generation, include extremely low rates of employment growth and an increasing informalization of the economy. A post-crisis scenario will present Zimbabwe with an opportunity to fundamentally rethink the developmental path it wishes to pursue in order to trigger sustainable, broad-based and inclusive growth.

WHILE
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PRODUCTIVE BASE
OF THE ECONOMY

Chapter 3

Stabilization for Sustained Growth

After a decade of decline, full economic recovery with a return to sustainable, inclusive growth will be a lengthy, three-phase process:

- Phase One – short-term macroeconomic stabilization, a period of at least two years.
- Phase Two – institutional and structural reforms designed to create a sturdy platform for strong growth. Ideally, some of these reforms should be implemented – or at least designed and initiated – during Phase One.
- Phase Three – second-generation institutional and structural reforms that are necessary to ensure that growth is both sustainable and inclusive and that Zimbabwe evades the experience of many other sub-Saharan African economies of short-lived growth spells that prove unsustainable. Many, perhaps most, of these second-generation reforms will have been launched during Phase Two, but the process will be complex and the delivery period lengthy.

Although stabilization programmes typically have a short-to-medium-term focus they must be seen in the context of securing a platform for long-run growth. Not only will the three phases overlap with one another, but recent experience suggests that front-loaded reforms are more likely to succeed, because, typically, opposition to radical reform is at its weakest in the first two years of a new administration. Failure to implement necessary reforms quickly and decisively allows entrenched interests to garner support and block progress.

Three features of a stabilization programme for Zimbabwe merit special attention:

1. The starting point is abnormally unfavourable in respect of inflation – officially estimated at 11.2 million percent

in June 2008 – and a consolidated budget deficit in excess of 80 percent of Gross Domestic Product (GDP).

2. In a number of respects Zimbabwe's economic crisis is structural in nature. Land ownership was not a problem that emerged suddenly nor was the failure to create sufficient jobs to absorb school-leavers. Similarly, the fiscal balance has been a serious constraint throughout the post-independence period, while the country has lived with an underlying balance-of-payments problem for the past 50 years. Above all, Zimbabwe's long-run growth record is poor, so that by the turn of the century per capita incomes were lower than in 1960.
3. A possible future transitional administration should be aware of the dangers of constrained decision-making fostering consensus-style compromises that both delay and undermine reforms. Because the politicians will understandably be working to short electoral cycles, they might be less willing to implement radical reforms for fear that the benefits will not materialize within the electoral time-frame.

It will be hoped that these aspects will concentrate the minds of a new administration, especially if the donor community as well as private sector investors hold back for some or all of the transitional period. This point is critical since, without substantial foreign assistance, sustainable economic recovery is impossible.

WITHOUT
SUBSTANTIAL
FOREIGN
ASSISTANCE,
SUSTAINABLE
ECONOMIC
RECOVERY IS
IMPOSSIBLE

3.1 COMPONENTS

Typical components of orthodox stabilization programmes include:

- Fiscal and monetary stabilization

- Exchange-rate and price liberalization
- Institutional reforms
- Reform of the domestic financial sector
- Debt management.

Phase Two and Three (structural) reforms usually include:

- Public sector restructuring
- Labour-market reform
- Trade reform
- Capital-account liberalization
- Doing Business and Investment Climate reforms not covered elsewhere
- Competition reforms.

*THE STARTING
POINT FOR A
STABILIZATION
PROGRAMME MUST
BE A COMBINATION
OF FISCAL
RETRENCHMENT
AND MONETARY
CONSTRAINT*

3.2 STABILIZATION: 2009/10

There is no single, unique stabilization model that is applicable to different countries at different times in different regional locations that followed different paths to economic decline and hyperinflation. However, the key basic principle that stands out is that the stabilization package must be seen to be credible, not only in the eyes of market participants, foreign as well as domestic, and the community at large, but also of external financial institutions and donor agencies. Credibility has less to do with sequencing during the short-run stabilization period proper (though sequencing decisions loom larger over time) than with political feasibility, administrative capability and focused targeting.

3.3 FISCAL CONSOLIDATION AND MONETARY STABILIZATION

There is broad, though not complete, agreement that, because Zimbabwe's

hyperinflation is directly attributable to fiscal expansion and reckless credit creation by the central bank, the starting point for a stabilization programme must be a combination of fiscal retrenchment and monetary constraint. The immediate priority is to terminate all quasi-fiscal operations and incorporate them into the national budget, as was tried in 2007 but abandoned in the 2008 budget.

The full extent of Zimbabwe's fiscal crisis is unknown, partly because of the very substantial discrepancies between budget data and that published subsequently by the Ministry of Finance, but primarily because quasi-fiscal activities have been excluded from the annual budget statements, except in 2006. Although the full extent of quasi-fiscal activities is unknown, estimates by the International Monetary Fund (IMF) put the overall financial borrowing requirement at 64 percent of GDP in 2005, when the central budget deficit was 3 percent of GDP, implying a quasi-fiscal deficit of 61 percent of GDP and of 82 percent in 2006, when the central government deficit was 7.5 percent, indicating a quasi-fiscal deficit in the region of three-quarters of GDP. The IMF (2008) has recently estimated the quasi-fiscal deficit for 2007 at 82 percent of GDP – a figure identical to that of 2006 (which seems unlikely), during which year there was also a central government deficit of 10 percent of GDP.

Table 3.1 summarizes the main budget figures for 2007/8, showing that, while the 2008 budget statement (November 2007) estimated a 2007 central government budget deficit of \$13.9 trillion, year-end figures published by the Reserve Bank of Zimbabwe (RBZ) show a surplus for the year of \$13.3 trillion. However, during 2007, the domestic debt of central government increased by approximately \$21 trillion, implying a quasi-fiscal deficit of some \$34.3 trillion, funded partially by the central government surplus and RBZ borrowing on behalf of the government.

Table 3.1: Zimbabwe: Budget balance 2007/08

2007

\$ trillions	Budget (Dec. 2006)	Estimated out-turn (November 2007)	Actual out-turn
Revenue	29.4	46.6	99.8
Expenditure	43.3	43.6	86.5
Deficit	13.9	+3.0 (surplus)	+13.3 (surplus)
Domestic debt, year-end	0.176 (2006)	21,176 (2007)	+21.0 (increase)

Sources: Government of Zimbabwe: *Financial Statements 2008 Budget*; Reserve Bank of Zimbabwe *Monetary Statistics* (January 2008)

2008

\$ trillions	Budget (Nov. 2007)	July 2008
Revenue	6,080 (38% of GDP)	n.a.
Expenditure	7,840 (49%)	n.a.
Deficit	1,760 (11%)	n.a.
Domestic debt, year-end	21,176 (2007)	790,600

Sources: Government of Zimbabwe: *Budget Statement 2008 and 2008 Half-Year Monetary Policy Statement* (July 2008)

The situation deteriorated dramatically in the first half of 2008. The projected budget deficit for 2008 is Z\$1,760 trillion,¹ but by mid-year, domestic debt had increased to \$790,600 trillion, which meant that that by the end of the second quarter the consolidated public sector deficit exceeded the budget deficit target for the full year by some \$789,000 trillion.

This explosive growth in domestic debt illustrates the magnitude of off-budget QFAs (Quasi-fiscal activities) that, in the first half of 2008 alone, exceeded budgeted spending by a factor of 200, translating into money-supply growth of 421,000 percent in the first four months of 2008.

Although the immediate cessation of all quasi-fiscal operations by the RBZ ought to be the top priority in a stabilization programme, the Government of Zimbabwe Short-Term Economic Stabilization Programme (July 2008) makes no reference to QFA operations. At the outset of the stabilization programme expenditures currently undertaken by the RBZ, including

lending, interest and exchange-rate subsidies, must either be discontinued or financed by transparent transfers from budget account. While this will achieve a much greater degree of transparency than at present, it will only contribute to reduced inflation if public sector spending – on both budget and quasi-fiscal accounts – is reduced.

In the near-term, the main spending cuts will have to come from the quasi-fiscal ‘budget’ with potentially severe knock-on effects in agriculture, parastatals, general government spending, importers and the financial sector. However, the IMF suggestion that there is scope for a substantial reduction in the public sector wage bill needs to be treated cautiously, given the security and crime risks inherent in sudden reductions in military spending and the heavy costs of terminal benefits, early retirement packages and re-training and re-skilling programmes.

Similar caution applies to the IMF’s recommended reduction in the capital budget. Table 3.2 (p.38) shows sustained under-investment by the public sector over a

¹ Budget Documents, November 2007.

20-year period and given acute infra-structural deficiencies across the economy – electric power, water, transport, roads, telecommunications, not to mention the social sectors (schools, health and housing) – an expanded public sector investment budget should be a priority. Indeed, the same IMF document that recommends reduced public sector investment refers to ‘the collapsing health infrastructure’ (IMF 2007). In the Zimbabwe context this is particularly important especially in the light of the IMF’s warning that in developing regions as a whole, ‘a disproportionate share of fiscal adjustment has been borne by the infrastructure’ (IMF 2006).

A disinflationary fiscal stance will necessitate a major reduction in the budget deficit including the incorporated quasi-fiscal activities, to be achieved by:

- Spending cuts.
- Securing aid funding to supplement domestic budgetary revenue during Phase One of the stabilization programme.
- Extra revenue measures, including improved revenue-collection efficiency, achieved in part by strengthening tax compliance, making it rule-based rather than discretion-based as at present.

While such measures will ensure a degree of monetary tightening, they will have to be accompanied by the imposition of hard budget caps in the parastatal sector as a result of the removal of subsidies in respect of food, fuel, electricity and air travel. Monetary tightening in the private sector will necessitate a sharp increase in interest rates allied with the speedy phasing out of concessional lending programmes.²

At the same time, statutory-reserve ratios should be lowered substantially, while

foreign-exchange flows are liberalized to allow the financial sector to trade foreign currency freely. In all probability, special arrangements will be needed whereby over-borrowed companies and farmers are enabled to reschedule their loans.

The current mismatch between the maturity of government securities and short-term deposits poses a serious liquidity threat for the banks, especially at a time when confidence in the sector is low. Open-market operations that incorporate anticipatory repurchase agreements would enable the financial market to be proactive in managing liquidity and in the market determination of interest rates. The implementation of reserve averaging will ensure that liquidity ratios are determined by prudential requirements to be met over a significantly long time and not at any specific time.³ The idea is to give more scope to financial institutions to manage their liquidity and eventually reduce reserve requirements.

3.4 STABILIZING PRICES

Stabilization should go hand-in-hand with price liberalization – the upfront removal of all price controls. At the outset policy-makers must choose between two potential anchors for price stabilization – the exchange rate or a monetary aggregate. The choice between the two is frequently deemed to be political rather than technical because exchange-rate stabilization is invariably associated with a short-lived consumption boom followed by recession, while a monetary-based programme results in a short-term consumption bust followed by economic recovery. It is therefore believed that an administration seeking a quick-fix solution ahead of elections will opt for the exchange-rate approach, while a newly elected government working to a five-year time-frame will prefer a monetary-based strategy.

² ASPEF and BACOSI – see chapter 5 on recovery of the financial sector.

³ Reserve averaging refers to the practice of averaging the statutory reserve payments of the banks over a period of time – at present it is averaged weekly – rather than tying the requirement to a bank’s position on a specific day.

In the Zimbabwe context such analysis does not apply, partly because the criteria for anchor selection will be influenced substantially by past experience – how and why the country slipped into hyperinflation. In Zimbabwe’s case, the administration sought to maintain an unworkable combination of a fixed exchange rate with fiscal and monetary expansion. The failure of this peculiar combination may influence future policy-makers...

Secondly, an exchange-rate approach is technically inferior where a country’s balance of payments on current account is vulnerable to adverse exogenous shocks – specifically the terms of trade in the form of rising energy prices or a decline in export prices for primary commodities (gold, platinum, tobacco, cotton, ferrochrome), or adverse climatic and structural influences in the domestic economy (drought and the supply-side bottlenecks created by land resettlement).

The exchange-rate anchor is then at risk on two fronts – the possible failure to narrow the purchasing power parity gap with trading partners because inflation does not decline rapidly enough, and a large current account deficit in the balance of payments, which must then be funded from capital inflows, including aid. There is then a serious risk that external funding – designed to loosen the import constraint that is holding back domestic production, investment and job creation – is wasted in seeking to defend a pre-selected exchange-rate peg.

Thirdly, an exchange-rate peg assumes the existence of substantial foreign reserves to defend the rate. Currently, Zimbabwe’s foreign reserves are negligible and it would be an extremely wasteful use of aid funds or offshore credit lines to use them to defend an arbitrarily-selected exchange rate.

Fourthly, an exchange-rate anchor targets inflation indirectly, unless it is formalized into

a currency board arrangement whereby the balance of payments on current account drives the size of the monetary base. Because purchasing power parity does not drive a country’s current account in the short to medium term, there is a danger that policy-makers will be distracted by a focus on two targets – the exchange rate and inflation – rather than just one, inflation.

In any event, there can be no guarantee that lower inflation – and thereby a real exchange-rate depreciation – will translate into rapid export growth and a reduced current account payments deficit, especially given the structural bottlenecks to export growth. In other words, while a stable exchange rate might help to restore price stability it might also leave the economy vulnerable to subsequent recession and devaluation, which has been the experience of many exchange-rate-based programmes.

For these and other reasons a monetary anchor is likely to be more effective. That said, there is no doubt that where the demand for money is unstable – as in Zimbabwe – a monetary-based strategy will encounter some very real problems. Unstable money demand is usually caused by high and volatile inflation, extensive unofficial dollarization in the form of a tendency of the public to shift to foreign currencies as a hedge against inflation, and political uncertainty and financial deepening. All three influences apply to Zimbabwe, with financial deepening⁴ being the least significant.

Accordingly, common sense suggests a ‘constrained discretion’ approach that strikes a balance between a rigid monetary rule and a wholly discretionary approach to monetary policy by the central bank (Bernanke, 2003). Precisely which monetary aggregate should be used is best left to the professionals in the central bank, but recent IMF programmes have tended to focus on the monetary base (reserve money),⁵ though IMF research in Zimbabwe has found a reasonably consistent

COMMON SENSE
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APPROACH THAT
STRIKES A
BALANCE BETWEEN
A RIGID MONETARY
RULE AND A
WHOLLY
DISCRETIONARY
APPROACH TO
MONETARY POLICY
BY THE CENTRAL
BANK

⁴ Financial deepening means increasing usage of financial services.

⁵ See chapter 5 on recovery of the financial sector.

relationship between notes in circulation (M0) and inflation, suggesting that this might make a suitable anchor for a short-term stabilization programme.

Kovanen (2004: 14) found ‘a strong linkage between currency in circulation and the price level’, suggesting that M0 (currency in circulation) would provide ‘a good leading indicator of future price movements’. He found also that there is a ‘well-identified long-run money-demand relation for currency in circulation’, which implied that currency in circulation could serve as an intermediate monetary operating target. He concluded that reserve money, used in the past both by the RBZ and in IMF programmes (1998/9) was ‘ineffective in the current high inflation environment’.

A serious drawback to a money-based stabilization programme will be the extent of dollarization, which increased sharply in the first half of 2008. During the transitional period when dollarization levels will remain high and may even increase it will be essential for the RBZ to adopt a tight monetary stance consistent with the underlying growth rate of real output.

Whatever the model adopted – exchange rate or money-based – and whatever the chosen monetary aggregate and degree of monetary discretion and flexibility, there should be an exit strategy within a specified time-frame, whereby monetary or exchange-rate targeting will be replaced, initially with implicit inflation-targeting (without a specified inflation target) and subsequently explicit inflation-targeting conducted by an independent central bank.

3.5 THE EXCHANGE RATE

In the real world, policy-makers have to choose between allowing the exchange rate to find its own competitive level and choosing a rate which they deem to be appropriate and defensible. However, where a monetary anchor is chosen, the requirement is to allow the exchange rate to

find its own level consistent with that monetary target. In choosing a (subsidiary) exchange-rate target as well as a monetary anchor the central bank is required to target two, invariably irreconcilable, targets.

However, political pressures may be such that the authorities find it necessary to have an implicit exchange-rate target as well as an explicit monetary one, notwithstanding the risks attached to such dual targeting. The difficulties of setting an exchange-rate target should not be underestimated. During the decade of crisis and decline the economy has undergone far-reaching structural change and hyperinflation, meaning that indicators of competitiveness stretch well beyond the exchange rate alone. Any attempt to ‘guess’ what might be a competitive exchange rate is fraught with danger.

Nonetheless, there is a widely held perception that the Zimbabwe dollar is seriously undervalued in the parallel market. The sharp 65 percent appreciation of the Zimbabwe dollar on the parallel market in the immediate aftermath of the 29 March 2008 elections suggests that this is, in fact, the case. Accordingly, in a post-crisis environment – and especially given the importance attached to exchange-rate management by all stakeholders – there is likely to be a public clamour, even before any stabilization programme is announced, that the parallel rate informs the exchange rate.

The foreign-exchange market was partially liberalized on 30 April 2008, when the RBZ allowed authorized dealers (banks) to purchase foreign currency at market rates. However, they were required to sell their foreign currency to priority buyers in proportions, specified by the central bank. Initially, the free-funds market, as it is called, traded at a premium over the parallel rate, but within weeks the gap between the two markets widened substantially to the point where by August 2008 parallel market dealers were buying foreign currency at rates ten to twelve times above the free-funds rate. At the same time, there is no effective inter-bank market because banks

buy foreign exchange to sell to their customers, not to other banks. The implication is that the authorities may well feel pressured to choose a rate somewhere between the ‘free-funds⁶’ and parallel-market rates as the starting point for an (eventually) unfettered inter-bank foreign-currency market.

There are three downsides to such an approach. The first is that an arbitrarily selected exchange rate may not be compatible with the monetary anchor, especially if, as is often the case, monetary targets are exceeded, with the result that inflation declines more slowly than projected. In that situation, an exchange rate assumed to be compatible with an implicit inflation target will not be so, and will be driven lower in parallel-market trading.

More seriously, the moment the RBZ shows its cards by stipulating a ‘market’ exchange rate, the market will assume that the central bank will use whatever resources it has available to defend that rate, or, at the very least, to manage an orderly retreat from that level in the event of it proving misconceived. For this reason, a low-risk strategy is one in which the central bank focuses on its monetary target, leaving the market to determine the exchange rate, thereby avoiding both the cost – indeed, the waste – and embarrassment of defending an inappropriate one.

Above all, in a country where exchange-rate determination has become an intensely political issue, macroeconomic stability dictates that exchange-rate decision-making be de-politicized and removed from the sphere of public bargaining where special interests, not economic common sense, become paramount. That in the last three years, tobacco auctions have had to be postponed pending a political decision on the ‘appropriate’ exchange rate and foreign-currency retention regulations for tobacco exports, underlines the desirability of depoliticization.

Ideally, all restrictions on current transactions should be abolished, along with capital controls affecting individuals. Subject to developments, capital controls on companies could then be reviewed subsequently. In the past, it has always been argued that pent-up foreign exchange demand exists in the form of former residents with blocked funds in the country that would be withdrawn immediately. However, in the light of the massive devaluation of the Zimbabwe dollar, pent-up demand is unlikely to be great, other than in the event that there is substantial disinvestment from the business and residential property sectors, where asset values may have been maintained. Once again, credibility is crucial – if the disinflationary package, including the exchange-rate stance, is credible, the relaxation of capital controls in respect of individuals might well have positive capital account implications, especially in a situation where substantial diaspora inflows are anticipated and, indeed, facilitated.

Within Zimbabwe, considerable publicity has been given to an alternative, unorthodox, strategy for disinflation, using an internationally determined or market-driven anchor. The attraction of these proposals is that they take political manipulation of the monetary and exchange-rate systems out of the equation, either by pegging the exchange rate to a foreign currency or to a country’s balance of payments.

Professor Steve Hanke of Johns Hopkins University in the United States has trailed a menu of three exchange-rate systems for Zimbabwe that he believes would be more suitable for speedily resolving the country’s hyperinflationary crisis and restoring economic growth because international experience is that central banks that have made the permanent transition to low inflation usually required a long transition period to establish their credibility, during which interest rates were ‘punishingly high’. Consequently, GDP growth was slow, living

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WHERE SPECIAL
INTERESTS, NOT
ECONOMIC
COMMON SENSE,
BECOME
PARAMOUNT

⁶ Free-funds in Zimbabwe refer to foreign currency receipts from the diaspora, travel and subsistence allowances, donations and any other foreign receipts not classified as exports.

standards stagnated, and poverty worsened during the stabilization phase. Hanke sets out three options for the next Zimbabwe government to consider: official dollarization, free banking, or a currency board, any one of which would establish stability and restore economic growth (see Box 3.1).

All three options are open to a variety of criticisms, both technical and political. On the technical side, it would be unwise for a future Zimbabwe administration to adopt a stabilization strategy that was not backed by major donors and the Bretton Woods Institutions. Given that the IMF favours an orthodox approach, along the lines summarized in this chapter, the adoption of full 'official' dollarization or a currency board might prove costly in terms of forgone support.

A serious objection to dollarization is that the business cycle in the US, whose monetary policy is being 'imported', is unlikely to coincide with that in Zimbabwe, meaning that the Zimbabwe authorities might be forced into a deflationary monetary stance, or to allow the currency to depreciate, when domestic market conditions required a very different approach.

Above all, in the light of the recent stance taken by central banks around the world as lenders of last resort, and the extreme activism of the RBZ, especially since December 2003, both as a lender of last resort and much further afield, it is very unlikely that a Zimbabwe government would accept the extreme solution of abolishing the RBZ, as advocated by Professor Hanke.

Hanke believes that Zimbabwe (formerly Rhodesia) – when a member of the Federation of Rhodesia and Nyasaland (1953–1963) – was wrong to abandon the currency board system that had existed since 1940 and replace it with a central bank. He believes that under a currency-board system the country would have had lower inflation and higher economic growth than under a central bank regime.

Although such statements cannot be validated one way or the other, the fact remains that, for the first half of the sanctions period (1965–1979), when the country operated with a central bank, inflation averaged 4 percent a year and the economy grew faster (8 percent annually) than at any time since independence in 1980. It follows that there is no necessary link

Box 3.1: Exchange Rate Options

The Three Options

1. Dollarization (or Randization). *Zimbabwe already has a high, but unknown, degree of unofficial dollarization – prices of cars and houses, fees for services, salaries of scarce personnel, are either paid or calculated in US dollars. Official or full dollarization is where a foreign currency – possibly the rand, or US dollar – has exclusive, predominant status as full legal tender so that the domestic currency is phased out and replaced by the US dollar or South African rand. Countries that adopt this model can no longer have an independent monetary policy and set their own interest rates but must 'import' the monetary policy of the country whose currency is chosen.*
2. Free Banking, which existed in Zimbabwe (then Southern Rhodesia) until 1940 when a currency board was established, leaves private commercial banks to issue notes and other liabilities with 'minimal regulation'. The banking system is unregulated – no reserve ratios, no legal restrictions on bank portfolios and no lender of last resort.
3. A Currency Board must hold foreign reserves equal to 100 percent of the domestic money supply determined at a fixed exchange rate. Hanke says that, as a result, money supply, and thereby interest rates, are determined 'entirely by market forces'.

* Steve H. Hanke, *Zimbabwe: Hyperinflation to Growth*. Harare: Imara Holdings, 2008.

between a country's monetary system and its economic performance.

Given the salience of national sovereignty in political discourse, the adoption of an exchange-rate policy that surrendered control of monetary policy to outsiders or even to market forces would be a high-risk strategy for a fresh administration. Furthermore, the suggestion that Zimbabwe should abolish its central bank when much smaller regional economies – Lesotho and Swaziland – find it necessary to operate a central-bank system even though they are members of the Rand Monetary Area is unrealistic.

Even more fundamentally, Hanke concedes that a 'government may try to undermine any of the options for monetary reform', which emphasizes the need for 'strong legal protection' to prevent the state from imposing its will. In other words, adopting a dollarization or a currency board is no guarantee of monetary and fiscal rectitude. As with any anchor, if the government of the day finds such externally imposed, or market-imposed, discipline burdensome politically, it will assume full sovereignty.

3.6 DOMESTIC FINANCIAL REFORMS

Given the centrality of credibility to any stabilization programme, there is a powerful case for the new administration to commit publicly to an autonomous, independent central bank. The credibility of a monetary-based stabilization programme will be substantially greater if the RBZ is perceived, both domestically and internationally, to be fully autonomous.

Since a new constitution is likely to be high on the political agenda during the immediate post-crisis period, the question of whether the RBZ's independence should be enshrined constitutionally should be part of the public debate over a new constitutional dispensation. Given Zimbabwe's unhappy recent history with a politically driven

central bank, the economic case for RBZ independence is very powerful.

There is much to be said also for the appointment of a Monetary Policy Committee charged with advising the Governor on monetary-policy issues. This would serve a dual purpose in ensuring that the central bank is kept well informed of market and private sector concerns and expectations while simultaneously ensuring that private sector participants appreciate the difficult nature of critical interest rate and other monetary policy decisions.

3.7 FISCAL REFORM

Just as monetary-policy credibility would be enhanced by a public commitment to the independence of the central bank, so fiscal credibility would be strengthened were the Minister of Finance to announce fiscal rules and targets for the stabilization phase. The centrepiece should be the announcement of public sector (including parastatals) domestic borrowing requirements over the stabilization period. The emphasis should be on domestic borrowing, thereby enabling public sector entities to draw on aid inflows or borrow offshore for critical social-service spending (education, health, housing, social welfare) and for essential and urgent investment in physical infrastructure. The actual level of public sector borrowing will have to be consistent with the monetary policy target and with the availability and cost of foreign funding.

Inevitably, there will be considerable overlap between short-term stabilization measures and the medium-to-long-term structural reforms necessary to revive economic activity. Because inappropriate fiscal and monetary policies (see chapter 2) contributed substantially to the country's economic decline, the need for sweeping reforms in these two related fields cannot be exaggerated.

A major – some would say the major – contributor to Zimbabwe's lacklustre long-

Table 3.2: Zimbabwe and sub-Saharan Africa: Fiscal aggregates 1985-2004

% of GDP	Zimbabwe	Sub-Saharan Africa (average)
Revenue (excluding grants)	26.1	21.2 (a)
Taxation	22.7	16.5 (b)
Expenditure	32.2	24.9 (a)
Budget deficit	6.3	3.7 (a)
Capital Expenditure	2.7	18.5 (b)
Wages and Salaries	10.8	7.4 (b)
Interest	6.1	5.1 (b)

Notes: (a) Sub-Saharan averages refer to 1997-2002 (IMF 2008). Zimbabwe figures cover 1985-2004.

(b) 1990-1998 (World Bank: African Economic Indicators, 2000)

term economic performance has been weak fiscal management. Table 3.2 summarizes the key aggregates showing that over the long haul (1985 to 2004) government spending exceeded total revenue, including grants, by 6.3 percent of GDP.

This is striking because Zimbabwe's revenue-to-GDP ratio of 26.1 percent is well above the recent average for sub-Saharan Africa (21.2 percent) as is its tax-to-GDP ratio. Zimbabwe's tax ratio of 22.7 percent of GDP is substantially above the sub-Saharan average of only 16.5 percent. Also striking is the fact that over the 20-year period capital expenditure was a mere 2.7 percent of GDP, compared with a sub-Saharan average of 18.5 percent, while Zimbabwe spent more on wages (10.8 percent of GDP) and interest (6.1 percent) than sub-Saharan countries.

These data are both encouraging and depressing. Encouraging because the country has a much greater taxable capacity than its African peers, but depressing because the

resources raised by the state did not translate into rapid, sustainable growth.

Moreover, the data in Table 3.2 do not reflect the fiscal impact of quasi-fiscal activities (QFAs) that have expanded dramatically since 2004. IMF estimates put the primary budget deficit (excluding interest charges) at 25 percent of GDP in 2006 compared with an officially stated 2 percent surplus. When government and RBZ interest charges are taken into account, the central government financing requirement increased to 80 percent of GDP.

The 2007 Budget

Budget measures approved by parliament have been overwhelmed by the combination of rapidly-escalating hyperinflation and the RBZ's quasi-fiscal activities. Table 3.3 shows that for 2007, parliament approved budget spending of \$6.2 trillion with a projected central government deficit of \$3.2 trillion. In the event, revenue was almost \$100 trillion, of which nearly half (\$45 trillion)

Table 3.3: The 2007 budget outturn

Z\$ trillions	2007 budget (November 2006)	Mid-term fiscal review (September 2007)	Outturn (July 2008)
Revenue	3.0	37.1	99.8
Expenditure	6.2	50.4	86.6
Deficit	3.2	13.3	13.2 (surplus)
Domestic Debt	0.176	n.a.	21.2
Financing	-	-	21.0
Total Deficit	3.2	13.3	34.2 (imputed)

Source: Ministry of Finance

accrued during the final month of the fiscal year (December). Expenditure of \$86.6 trillion was some \$80 trillion above the level initially approved by parliament.

The twin impacts of hyperinflation and the RBZ's quasi-fiscal operations effectively takes fiscal policy out of the hands of the Ministry of Finance and Parliament. Fiscal policy is effectively the preserve of the central bank, oversight is minimal and all pretensions to disinflation have been abandoned.

3.8 FISCAL SPACE

From the above it is clear that restructuring Zimbabwe's public finances will be far more complicated than simplistic expenditure reduction solutions suggest. Decades of government overspending and over-taxation, exacerbated since 2004 by massive off-budget QFA spending, cannot be switched off overnight. In the near term, the yawning fiscal gap will have to be filled by a combination of revenue-enhancing measures, substantial spending reductions, mostly from the quasi-fiscal budget, and foreign assistance, with revenue enhancing measures making the smallest contribution.

Fiscal space exists when a government can increase expenditure without impairing macroeconomic stability (IMF 2006). Additional revenue can be raised by increasing taxation, strengthening tax administration and implementing cost recovery for state-provided services. Reduced spending on lower priorities—such as defence – creates fiscal space as does increased borrowing by the state, additional foreign aid grants or credit creation by the central bank.

The link to sustainability is crucial. Some revenue-raising measures may inhibit economic growth and reduce welfare. Seldom is it simple to identify 'lower priority' expenditures. Underinvestment in infrastructure investment across Africa because of perceived lower priorities relative

to social spending have come back to haunt the continent's governments in the form of a severe infrastructure deficit. Increased borrowing translates into higher debt-service and foreign currency commitments, while credit creation by the central bank fuels inflation and currency depreciation.

Past experience (Table 3.2) suggests that because only a handful of sub-Saharan economies raise more revenue relative to GDP than Zimbabwe, fiscal space issues should not be a reform priority. In 2007, only four sub-Saharan countries (out of 44) had higher spending-to-GDP ratios than Zimbabwe (39.1 percent), while Zimbabwe's revenue generation (28.8 percent of GDP) comfortably exceeded the regional average (23.4 percent) (IMF 2008). Yet, above-average levels of revenue mobilization and spending by the state did not translate into increased public sector investment, faster economic growth or progress towards meeting the MDGs (Millennium Development Goal).

Accordingly, Zimbabwe's fiscal reforms need to target the composition and quality of expenditure on the one hand and the efficiency of revenue-raising measures on the other. 'The composition and efficiency of expenditure is a key to achievement of outputs and outcomes' (IMF 2006). Furthermore, and in the context of post-crisis Zimbabwe, this is a crucial consideration. Fiscal policy must take account of growth constraints, especially the institutional capacity to make effective use of available resources.

Compositional changes to spending patterns should target phasing down subsidies, whilst boosting social and investment expenditures. There will be scope too for savings in the field of general administrative spending by reducing the number of overlapping government departments and rationalizing the public service, though because Zimbabwe has long underspent on operations and management, savings are unlikely to be substantial.

The extent of savings will depend also on broader strategic issues. Given the rundown state of public infrastructure increased

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investment is essential but future administrations should ensure that where this can be undertaken more efficiently by the private sector or in private-public partnerships, public finance is conserved for use in areas that will not attract private participation – rural roads, schools, clinics and land reform.

This highlights the need to frontload structural reforms. It is essential to avoid the situation, experienced in so many other African countries, where privatization and other private sector initiatives have been delayed while government has sought, usually in vain, to rescue failed state enterprises. Copper mining in Zambia is a classic example. Public service and public sector restructuring should be high on the stabilization agenda.

3.9 TAXATION

Because Zimbabwe is a high-tax state, collecting 22.7 percent of GDP in tax revenue compared with 12.9 percent for low income countries as a whole and 16 percent for low-middle income countries, the focus of tax reform should also be compositional. Zimbabwe relies on direct income taxes for 47 percent of revenue, the bulk of this coming from individual taxpayers (39.6 percent) and the balance of 7.5 percent from companies.

There is therefore, a strong case for flattening the tax structure for individuals by raising thresholds for low income groups while also reducing the very high top marginal tax rate that exceeds 50 percent. At the same time the effective corporate tax yield could be raised by both lowering the company tax rate while abolishing some of the myriad tax-breaks that have been built into the system over the years. There is persuasive international evidence suggesting that such reforms increase the corporate tax yield while reducing tax bureaucracy and lowering collection costs.

In 2007, 95 percent of tax revenue was derived from four tax categories – profit and

income taxes (58 percent), VAT (24.5 percent) and customs and excise tax (12.5 percent). There is a significant number of ‘nuisance’ taxes that yield very little relative to collection costs that could be abolished. At the same time it is essential to widen the tax base by eliminating exemptions (VAT) and implementing pro-market reforms designed to formalize the informal sector bringing its participants into the tax net.

At the macroeconomic level, four broad reforms should be investigated:

- (a) The early compilation of a national balance sheet that identifies the country’s net worth in terms of assets and liabilities. Such data are not available and an inventory of this kind would make it possible to ascertain the rate of return earned on public investments as a guide to future policymaking.
- (b) A shift away from the existing UK-style secretive budgetary processes that limit the scope for public debate and participation until after the budget has been presented and acquired the status of a *fait accompli* thereby limiting the scope for positive changes.
- (c) Extending the budget cycle with the aim of ensuring that fiscal policy is framed on the basis of medium-term objectives and constraints. The setting of medium-term frameworks in respect of the share of revenue and public spending in GDP as well as the main categories of public expenditure – capital, interest charges and wage bills – would enhance both the transparency and efficiency of public sector financial management.
- (d) The explicit adoption of a wealth-based approach to budgeting whereby the authorities seek to increase national wealth by ensuring that resource depletion through mining, some types of agriculture, forestry and even tourism, is compensated by offsetting public investment in produced assets and human capital.

3.10 EXTERNAL FINANCE

Without foreign funding, stabilization is unlikely to succeed, which is why its implementation will depend on political reforms. It is fashionable for stabilization programme design to include projections of the funds required and their sourcing. Since this exercise is being conducted elsewhere (Bretton Woods Institutions and bilateral donors) it has been excluded from this exercise.

However, three points are pertinent. Typically such funding estimates are drawn up on the basis not of what will be required but what the providers think – often hope – will be available. There is no reason to believe that there is any meaningful relationship between availability and requirements. The net result is either for programme design to be tailored to suit the availability of finance or to fill the black hole of the remaining financial requirement with optimistic guesstimates of private (and remittance) inflows.

Secondly, the financing requirement is unknown and will depend on the policy stance taken by a new administration. One obvious unknown is the extent, if any, to which a new administration will agree to pay compensation for those whose assets were expropriated in the land-reform process. Estimates of this amount vary tremendously, but the full cost, relative to the likely availability of aid finance, would be very large indeed. Similarly, there is a case for compensating pensioners – especially, but not only, public sector pensioners, who have been seriously disadvantaged by government fiscal and monetary policies since 1997. Whether such compensation claims are included or excluded will have a dramatic impact on the likely post-crisis financing requirement.

Thirdly, Zimbabwe is fortunate to the extent that it has a strong domestic financial sector and would be able to access offshore commercial bank funding, especially through

the multinational banks operating in the country (Barclays, Standard Chartered, Stanbic and MBICA). It would also have access to portfolio inflows via the Zimbabwe Stock Exchange and investment in the official fixed-interest market, were treasury bills and government stock to be marketed externally.

3.11 DEBT SUSTAINABILITY AND DEBT RELIEF

The most recently published debt sustainability analysis was undertaken by the IMF for its February 2007 Article IV report, which concluded that, on current policies, Zimbabwe's external debt was not sustainable without debt relief (IMF, 2007). It noted that debt sustainability analysis projections were only indicative, as Zimbabwe does not have reliable external debt and debt-service data, while meaningful medium-term projections of macroeconomic variables were difficult given the high degree of uncertainty over future policies.

External debt was estimated at US\$5 billion (69 percent of GDP) at the end of 2005, of which US\$2 billion was owed to multilateral creditors, while arrears were put at US\$2.7 billion (38 percent of GDP). Under the assumptions of the baseline scenario, by 2011 the total stock of outstanding debt (both public and private) would amount to US\$7 billion or 103 percent of GDP.

By 2011 the net present value (NPV) of public and publicly guaranteed external-debt–GDP ratio was expected to exceed 90 percent, while the NPV of such external-debt–exports ratio was projected to exceed 440 percent. The debt-service–exports ratio was estimated at 24 percent, and the NPV of total external-debt–exports ratio would approximate 1000 percent by 2026. The IMF noted that, if policies were to improve, the debt indicators would improve as well, but the very high debt ratios in the baseline scenario suggested that better policies alone were unlikely to be sufficient to make Zimbabwe's external-debt

burden sustainable, meaning that debt relief from both multilateral and bilateral creditors will have to be part of the stabilization package.

The debt sustainability analysis estimated domestic public debt, denominated in Zimbabwe dollars, to be 19 percent of GDP in 2005 and 2006. Using the official projection for GDP in 2008 of Z\$16,000 trillion, this ratio had declined to 15 percent of GDP by March 2008. Even assuming that domestic debt continues to increase at the exponential rate experienced in the first quarter of the year, because nominal GDP will rise in line with inflation, the debt–GDP ratio is unlikely to increase materially. Indeed, in real terms – converted to US dollars at parallel market rates – Zimbabwe’s domestic debt burden is tiny, at less than US\$50 million, so that the foreign exchange cost of taking the debt off the government’s books and converting it into a foreign liability would not significantly affect the debt sustainability analysis. Accordingly, inclusion of the domestic debt, valued at current exchange rates, would have minimal impact on Zimbabwe’s debt sustainability analysis.

3.12 INSTITUTIONAL AND STRUCTURAL REFORMS

As noted at the beginning of this chapter, in all probability there will be – indeed, should be – overlaps in the three phases of stabilization. Because institutional and structural reforms are the main focus of the entire report, they are not discussed here, save to stress that some such reforms – fiscal targets and rules, an independent central bank, a depoliticized exchange-rate strategy and reform of the financial sector – will be necessary during the stabilization phase.

It is a fact that governments that move quickly soon after taking office to implement Doing Business and Investment Climate reforms achieve greater success than those

whose approach is more measured.⁷ Given that so many of these reforms are essentially uncontroversial, there is a very strong case for fast-tracking them in the interest of speeding up the pace of economic recovery, job generation and poverty reduction.

3.13 THE DEFLATIONARY IMPACT OF THE STABILIZATION PACKAGE

It would be idle to pretend that macro-economic stability can be restored without a substantial, but hopefully transitory, contraction in effective demand. In the Zimbabwe case formal economy contraction will be exacerbated by the immediate shut-down of much informal economy activity.

While loosening the foreign-exchange constraint, through exchange-rate adjustment and accessing external finance, will ensure a strong rebound in the formal economy, there will also be a simultaneous, and severe, contraction in the informal economy. Thousands, possibly hundreds of thousands, of Zimbabweans have resorted to informal cross-border trading and parallel-market activities in respect of foodstuffs, goods and services and foreign exchange. Currency and price-control liberalization, allied with improved access to foreign exchange by formal businesses, will quickly eliminate most of these activities, with the loss of thousands of informal-economy ‘jobs’ and income.

One consequence of this is likely to be a reluctance on the part of people in the diaspora to return to the country, while their beneficiaries at home in Zimbabwe will become, hopefully temporarily, even more reliant on remittance income than in the past.

3.14 SOCIAL DIMENSIONS

Stabilization measures will need to be accompanied by measures to protect

⁷ See chapter 6 on private sector development.

vulnerable sections of the community. This is where the international community can make a major contribution in the form of budgetary assistance to ensure that real spending on health, education, social welfare and food aid is not undermined, despite an overall contraction in the level government spending.

Countervailing measures to deal with the social dimensions of stabilization, and indeed the hardships associated with the crisis, should build on the Enhanced Social Protection Programme (ESPP) designed by the World Bank, government and civil society in 1999, which was developed on the basis of an extensive review of past programmes. The major components of the ESPP are:

- Basic Education Assistance Module (BEAM), which aims to reduce the number of people failing to attend school because of hardships, and providing school-fee waivers to reduce the rate of drop-outs.
- Children in Especially Difficult Circumstances (CEDC), which aims to identify and assist children in difficult circumstances through community support and implementation of component.
- Public Works Component (PWC), which seeks to put in place labour-intensive public works that offer employment to the poor.
- Emergency Drugs and Medical Supplies (EDMS) component.
- Social Protection Strategy (SPS), which set up studies, analyses, consultations and technical assistance aimed at improving strategic planning, monitoring and implementing programmes in the Ministry of Public Service, Labour and Social Welfare.

External assistance for the ESPP was made conditional on government paying the arrears on its debt with the World Bank. Its failure to do so resulted in the programme being

suspended in 2000. As the relationship between government and the international community deteriorated, government decided to go it alone, fast-tracking the BEAM component.

Subsequent safety nets implemented by government have drawn from the framework provided by the ESPP. However, the major drawback has been the absence of external funding. Interventions by government suffer from declining access, low quality of the interventions in terms of the extent of mitigation, and poor targeting of beneficiaries.

These building blocks derived from the ESPP should form the basis for designing safety nets to counter the adverse social effects of both the current crisis as well as a future stabilization programme. These development partner-driven efforts such as the donor-funded Programme of Support for the National Action Plan for Orphans and Vulnerable Children (OVC), run parallel to the government's social safety nets.

After the crisis, there will be a need to integrate other elements of the ESPP – such as the PWC and EDMS components – into a common funding arrangement leading eventually to sector-wide budgetary support. A case in point is the formal education support programme, which is currently being implemented by both the government and under the Programme of Support for the National Action Plan for OVCs. A suggested solution is to integrate the formal education support intervention supported by donors into the BEAM programme, leaving the other non-fee interventions with NGOs. Similarly, the public works programme and the emergency drugs and medical assistance intervention can be supported by donors through government.

Such cooperation during the stabilization period will provide invaluable insights into the longer-term institutional mechanism for the medium-term recovery of basic social service delivery systems,

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3.15 MEDIUM-TERM OUTLOOK

Table 3.4 assumes a starting point GDP of US\$6 billion (2007) with a 10 percent decline in output during 2008. From 2009, GDP is assumed to grow at an annual average rate of 6 percent while population increases by 1 percent a year. National savings start from a very low base of 4 percent in 2008 but investment grows rapidly reflecting both public and private sector spending on revamping the infrastructure and the private sector capital base.

The budget deficit is brought down rapidly from 16 percent of GDP to 2 percent reflecting spending cuts, gradual growth in revenue as a percentage of GDP and foreign aid (budgetary support) of some US\$1.8 billion over the five-year period. Project support (concessional loans) average some US\$235 million annually over the period. There is no provision for debt relief, other than a notional grant of \$200 million in 2009, designed to help finance the restructuring of domestic debt.

Table 3.4: Five-year scenario

	2008	2009	2010	2011	2012	2013
GDP (US\$ billions)	5.4	5.78	6.18	6.49	6.81	7.22
% Change	-10.00	7.00	7.00	5.00	5.00	6.00
Population (millions)	12.00	12.13	12.25	12.37	12.49	12.61
Per capita Income	450.00	477.00	505.00	525.00	545.00	575.00
Resource balance						
Savings (% of GDP)	4	7	10	12	14	15
Savings (US\$ millions)	216	405	620	780	950	1,080
Investment Gross Fixed Capital Formation (% of GDP)		14	21	25	28	36
GFCF (\$ millions)		810	1,300	1,620	1,910	2,600
Resource Gap (US\$ millions)		-405	-680	-840	-970	-1 520
Budget						
Revenue (% of GDP)		24	25	26	27	28
Expenditure (% of GDP)		40	36	34	32	30
Deficit (% of GDP)		16	11	8	5	2
Deficit (US\$ millions)		925	680	520	430	140
Financing (US\$ millions)						
Grants		700	450	300	200	140
Budget Support		250	250	150	100	40
Food		250	150	50	0	
Land			50	100	100	100
Debt Relief		200	0	0	0	0
Project Support		225	230	220	230	250
Balance of Payments						
Exports (US\$ millions)	1,400	1,610	1,820	2,050	2,275	2,550
Imports (US\$ millions)	1,700	2,400	2,600	2,800	3,000	3,400
Trade Balance (US\$ millions)	-300	-790	-780	-750	- 725	- 850
Net Invisibles (US\$ millions)	-400	-500	-600	-650	-750	-750
Transfers : Grants (US\$ millions)	200	700	450	300	200	100
Other Transfers (US\$ millions)	300	200	200	200	150	100
Current Account (US\$ millions)	-200	-390	-730	-900	-1,075	-1,350
Net Capital (US\$ millions)						
Project Loans		225	230	220	230	250
Portfolio		100	70	50	50	50
FDI		170	250	350	400	500
Funding Gap		-	180	300	400	500

It is assumed that debt relief in respect of foreign debt will be forthcoming but that this would be both budget and balance-of-payments neutral because Zimbabwe has not been servicing its foreign debt, nor has it made budgetary provisions for that purpose. Total foreign aid is projected at some US\$3 billion over the period, excluding debt relief, which, if factored into the calculations, would take the total to some US\$5 billion and this, realistically, is likely to be the upper bound of public international support, excluding private donors, such as NGOs.

In balance of payments terms over the five-year period there is an assumed financing gap of US\$1.4 billion. This assumes relatively modest inflows of foreign direct investment and takes no account of short-term capital flows nor of offshore borrowing by the public and private sector. The assumptions about the growth of imports and the deficit on invisible transactions are at the pessimistic end implying that in the current global economic environment the funding gap would be manageable.

3.16 RECOVERY PROSPECTS

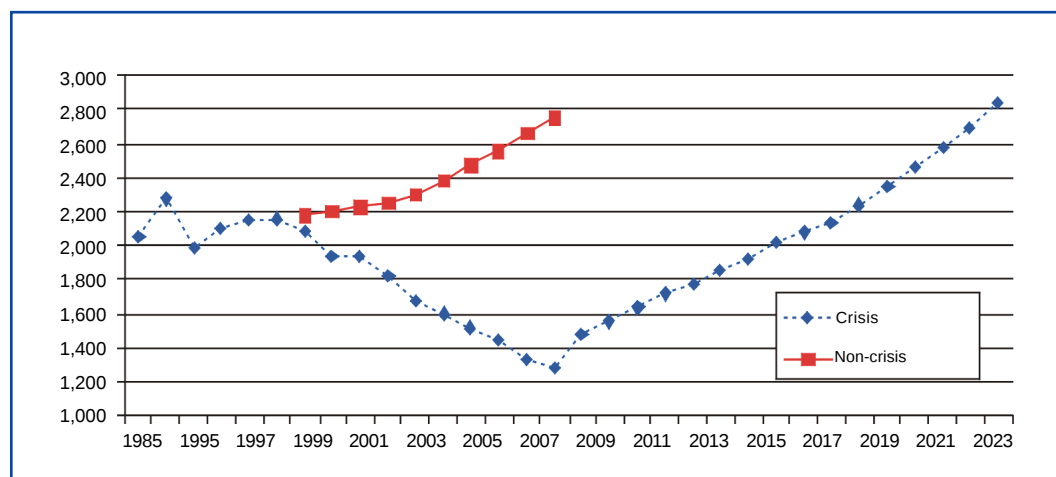
Although a strong short-term rebound is likely as spare capacity in the economy is brought back into production and foreign assistance resumes, so far-reaching is the damage incurred over the last decade that there can

be no quick fix. Full recovery – a return to the peak real per capita income levels achieved in 1991 – would take 12 years, assuming uninterrupted growth of 5 percent annually from 2009 to 2020 (Figure 3.2)

Historical data serve as a reality check. Over the long haul (1960–2002), far from being one of Africa's better performing economies, Zimbabwe not only lagged behind the regional average but grew more slowly than 24 of the 43 sub-Saharan economies from which comparable data are available. During this period, the Zimbabwe economy grew at an average annual rate of 2.6 percent compared with the sub-Saharan average of 3.2 percent. With population growth estimated at 2.9 percent annually over the period, real per capita incomes declined.

Moreover growth was driven entirely by factor accumulation – physical capital investment of 1.6 percent annually and increased employment of 1.8 percent a year. Productivity – more technically Total Factor Productivity (TFP) – declined at an annual rate of some 0.7 percent. Figure 3.2 also depicts also the extent to which Zimbabwe has fallen behind the rest of the region showing a counterfactual of where the country would have been in per capita income terms had it grown during the lost decade (1998–2008) at the average rate achieved by oil importing sub-Saharan economies.

Figure 3.2: Projected per capita income growth, 1985–2024



Sources: Central Statistical Office, Harare: National Accounts (various editions) and the International Monetary Fund: World Economic Outlook (April 2008)

In a no-crisis scenario, Zimbabwe's GDP per head in 2008 would be more than double its estimated level. Assuming annual per capita income growth of 5 percent annually it would take until 2024 to achieve the level of per capita that, without the crisis, would have been reached by 2008.

Clearly, the economy was underperforming before the onset of the crisis and recognition of this reality undoubtedly played a role in the decision to pursue a new and different growth path spearheaded by the Fast Track Land Reform Programme (FTLRP). The failure of land resettlement however should not be allowed to erase the lessons of the 1980s and 1990s. Neither the command economy model of the 1980s nor the abortive liberalization experiment of the 1990s succeeded. Nostalgia for a return to either is misplaced.

In any event, even were such a return to the past desirable, it is simply not feasible. Globalization, regionalization, technological progress and shifts in both the global and regional economic environments, not to mention the damage suffered during the crisis period, mean that a return to 1998 is not an option.

Going forward, expectations are high – in many respects unrealistically so. This report details the constraints that will inhibit growth in the years ahead. The 5 percent per capita projected growth rate from 2009 to 2024 is optimistic, not just in terms of the actual performance since 1960 but because:

- Physical infrastructure and human capital will put an effective ceiling on growth rates, certainly over the next five to eight years.
- The economic impact of HIV and AIDS will intensify before peaking after 2015. Regional studies suggest the disease

could reduce per capita growth by up to one percent annually.

- Reorienting and restructuring the economy during the post-crisis phase will have some disruptive effects, specifically in developing new growth engines – mining, tourism, financial services – to replace large-scale commercial agriculture.
- It will take several years for the hangover effects of hyperinflation and the collapse of the currency to be worked out of the system.
- Investor confidence – both domestic and foreign – will not return overnight, while domestic savings levels will be depressed for as long as a decade because of the trauma of hyperinflation.
- Public sector capability has been progressively eroded to the point where it will take decades to rebuild once-strong institutions.

For all these reasons it will be important not just to carefully manage expectations but to implement the prudent and stable fiscal and monetary policies necessary to re-establish business and investor confidence, both at home and abroad. The five percent projected annual growth in per capita GDP is almost certainly at – probably beyond – the upper bound of probability, given that Zimbabwe is susceptible on average to climate setbacks every three years and that, with the decline in commercial farming, the agricultural sector is now more vulnerable to drought than previously. If the potentially adverse effects of global climate change are also taken into account, then a long-run per capita growth rate of less than four percent looks more realistic, thereby extending the catch-up period by another four to five years.

ASSUMING ANNUAL PER CAPITA INCOME GROWTH OF 5 PERCENT ANNUALLY IT WOULD TAKE UNTIL 2024 TO ACHIEVE THE LEVEL OF PER CAPITA THAT, WITHOUT THE CRISIS, WOULD HAVE BEEN REACHED BY 2008

Chapter 4

Aid Flows and Management Systems

Multilateral and bilateral aid to the country decreased sharply as the crisis in Zimbabwe deepened after 2000. In a number of areas, such as agriculture and land resettlement, international assistance virtually ceased. The Organization for Co-operation and Development (OECD) donors have, however, continued to support the poorest and most vulnerable elements of society with the provision of vaccines, prophylactics, anti-retroviral drugs to fight HIV and AIDS and, crucially, food. Limited funds have also been channelled towards local community-based recovery initiatives, as well as in support of work in the areas of governance, democracy and human rights. It is noteworthy that, in stark contrast to prevailing international trends, and as a result of the estrangement between the Zimbabwe government and Western governments, such aid has been channelled outside government systems directly to beneficiaries through United Nations (UN) agencies or Non-governmental Organizations (NGOs).

The downturn in official development assistance coming into Zimbabwe coincided with a global rethink in the way in which aid was being delivered. A general disappointment with economic structural adjustment programmes and the 'Washington Consensus' in the 1990s, as well as the increasing dependence on aid, especially in Africa, gave rise to new principles, structures and processes in international aid delivery. Most notably, these were captured in the Paris Declaration of 2005. As Zimbabwe has not been involved in or privy to these processes, its institutional memory of aid is based on older practices, such as the dominance of project-based aid delivery mechanisms. In a post-crisis scenario, and in light of the emphasis now placed on national ownership and a likely high degree of dependence on aid flows, Zimbabwe must take the initiative

– with the assistance of donors – to define its own priorities, design its own development programmes, and build an institutional structure to significantly improve the effectiveness of aid.

4.1 AN OVERVIEW OF AID DELIVERY

4.1.1 The effectiveness of aid

The effectiveness of official development assistance in achieving economic development and broader development objectives can be divided into the process of delivering aid and the impact of aid in achieving development objectives. The process or **efficiency** of delivering aid relates to how various actors – especially the recipient and donor countries – can strengthen coordination mechanisms, reduce transaction costs for partner countries, improve aid predictability, and support home-grown development plans. The **impact** of aid relates to the current evidence of the efficacy of aid in achieving intended objectives and outcomes. Process and impact issues are closely correlated: the greater the efficiency of delivery, the more likely that aid will have the desired impact.

4.1.2 The impact of aid on growth

Following a number of studies, mainly by World Bank economists, the emerging consensus was that aid could have a positive impact on growth in 'good policy environments' (Dollar and Svensson, 1998; Burnside and Dollar, 2000). But a follow-up study by Easterly *et al.*, (2003) could not find support for this conclusion. Other studies showed diminishing returns to aid, and that it had no effect on growth when it reached 8 percent of the recipient country's GDP; additional aid

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thereafter was found to have a negative effect on growth (Easterly, 2006). This does not necessarily imply that aid in any one particular country cannot be effective, but it does suggest that donors and recipient countries, such as Zimbabwe, need to manage their aid flows – the process of delivering and absorbing aid – very carefully if the benefits of poverty reduction and growth are to be felt.

4.1.3 The efficiency of aid

International experience has shown that aid efficiency may be compromised for a number of reasons:

Ownership

When the government of Zimbabwe launched economic reforms in the early 1990s, the Minister of Information told the local press, ‘They’re not our reforms, they’re the IMF’s. We had to do them’ (Collier, 2007: 109). This was indicative of the failure of governments, especially in Africa, to accept responsibility for economic reform measures imposed upon them by the international donor community. In a review of its policy recommendations, the World Bank has been instrumental in suggesting more participatory approaches to economic growth and development with a view to increasing national ownership (World Bank, 2005).

An additional problem which has often emerged, particularly in highly aid-dependent economies, is a situation in which national leaders became more accountable to the donors who provide their governments with essential revenue than to their own citizens. This dependence on external aid flows also acts as a disincentive in terms of domestic revenue collection efforts and undermines domestic accountability systems. Senior technocrats and politicians become oriented towards convincing the aid agencies to keep the aid flow going rather than listening to their domestic population and focusing on the local development agenda. Sectors become accountable to multiple donors and not central government or parliament (Kanbur, 2003).

Disparate donor policies

Each donor country has its own agency for development cooperation that is managed in terms of principles and policies developed by its government, including development agendas and priorities, modalities, disbursements and conditions – including tied aid. It is often the case that multiple projects are implemented without consideration of the recipient country’s own priorities, policies and strategies and, as a result, undermine the partner country’s systems.

Fragmentation

Each donor agency also follows its own rules of planning and disbursement of funds, and these often do not coincide with the budgetary and planning processes of the recipient government. Apart from imposing their own conditionality and reporting requirements, donors appoint serial consultancy missions for planning and evaluating their own programmes. All in all, this imposes huge transaction costs on a recipient country’s already severely stretched administration.

The donors’ focus on funding multiple stand-alone projects in various sectors of the country, often led to perverse outcomes. Governments found it increasingly difficult to sustain recurrent expenditure once projects had run their course. The difficulty of meeting recurrent maintenance costs for infrastructure projects, and personnel costs for social service delivery projects, was compounded by a brain drain from the public sector to the donor sector. Project-based aid delivery ultimately undermines the recipient government’s incentives and its ability to perform a number of key functions, such as revenue collection, planning and budgeting, executing programmes, and monitoring and evaluation.

The micro–macro paradox

There is an apparent contradiction between the positive impact reported by evaluations of individual projects and the continued uncertainty regarding the net aggregate

impact of these projects on growth. In 1989 the World Bank's Operations Evaluation Department produced a report that contained evaluations of 2,000 projects over a 15-year time-frame (World Bank, 1989). Eighty-one percent of all projects were judged to have performed satisfactorily, with an average economic rate of return estimated at 16 percent per annum. However, micro and macro analyses seemed to yield different results, with many successful projects having no perceptible lasting effect on economy-wide growth rates. The suspicion was that many evaluations were flawed by significant data problems, subjective judgement, and methodological inadequacies. To this should be added the strong possibility that self-evaluations led to self-serving conclusions. There were strong incentives for evaluations to reach positive conclusions where the income and livelihoods of donor staff and recipients were dependent on future funding.

Asymmetrical partnerships

Despite the lip-service given to the principle of partnership, it seemed clear that the dominance of the donors progressively weakened the ability of, and incentives for, recipient countries to take greater responsibility for their own development. Donors have more recently been calling for greater ownership by the recipient countries, greater oversight, participatory approaches and enhanced communication by improving information flows between donors and recipients.

4.1.4 Paris Declaration on Aid Effectiveness

In view of the aforementioned problems and the persistence of poverty, especially in Africa, there was a growing realization of the need to reform aid delivery to improve its effectiveness. In March 2005, a meeting in Paris of developed and developing country

officials resolved to take far-reaching and monitorable action to reform the way in which aid is managed and delivered.¹ The Paris Declaration called for developing countries to have national development plans with clear strategic and budgeted priorities. It recommended that both donors and partner countries should move away from stand-alone project aid to programme aid. More specifically, it called for progress in five major areas: ownership, alignment, harmonization, mutual accountability and managing for results.

Ownership

Partner countries, meaning the recipients of aid, agreed that they should exercise effective leadership over their development policies and strategies, and coordinate development actions. Donors, on the other hand, agreed to respect a partner country's leadership and help develop and strengthen their capacity to manage the aid flows effectively.

Alignment

Alignment has two crucial elements. The first is that donors should align their support around their partner country's national development strategy document, such as a Poverty Reduction Strategy Paper (PRSP), and link their funding to a single framework of conditions and performance indicators derived from the PRSP. In particular, this means untying their aid and synchronizing their pledging and disbursement cycles with national planning and budgeting cycles. The second is that donors should align themselves to their partner country's institutional structures, systems and procedures, by strengthening them and working through them. The objective for Zimbabwe would be to work towards aligning the preferences of donors with those of the government.

¹ See <http://www.oecd.org/document/18/0,2340,en_2649_3236398_35401554_1_1_1_1,00.html>.

Harmonization

The donors also agree that – amongst themselves – their actions should become more harmonized, transparent and collectively effective. In effect, they agreed to common arrangements for planning, funding (joint financial arrangements), disbursements, monitoring and evaluation, and reporting. They also agreed to move to increase their use of programme-based aid and to reduce the number of separate, duplicate missions. Harmonization also means that donors agree to delegate responsibilities to ‘lead donors’ who are seen to have a comparative advantage or special expertise in a particular sector or area. This would reduce transaction costs considerably, because the recipient country would be able to deal comprehensively with one lead donor in a particular area who would be acting on behalf of several others. For Zimbabwe, with greatly weakened capacity, rapid moves towards harmonization would significantly lighten the burden on a post-crisis administration.

Managing for results

This requires donors and partners to jointly plan and manage aid flows in such a way that they focus on the intended objectives, and to use information derived from monitoring to improve the impact of aid. For donors, this means linking their programming and resource flows to specific results and aligning them to their partner’s performance assessment framework (PAF). Donors also agree to harmonize their own monitoring and reporting requirements with partner countries and move towards common formats for periodic reporting. Partner countries, for their part, have agreed to develop assessment and reporting systems that reflect key objectives of their PRSP or other medium-term development plans, and to translate these into annual and multi-year budgets to facilitate multi-year pledging and aid predictability.

Mutual accountability

This Paris principle makes both donors and partner countries jointly accountable for results. Partner countries commit to strengthening parliamentary oversight of government actions and to reinforcing participatory approaches by involving a broad range of development actors in designing and monitoring the implementation of national development and poverty reduction strategies. Donors, for their part, recognized the need to provide timely and comprehensive information on aid flows to enable partner countries to prepare comprehensive budget information to their parliaments and citizens.

4.2 APPLYING THE PARIS PRINCIPLES TO ZIMBABWE’S RECOVERY

4.2.1 Zimbabwe’s responsibilities

In terms of the Paris Declaration, Zimbabwe’s responsibilities would be to exercise effective leadership over its development policies and strategies, and to coordinate development actions. More specifically, they would have to:

- Develop national development plans, such as a PRSP, with clear strategic and budgeted priorities.
- Develop jointly with donors a performance assessment framework and agree on a single set of conditions that are derived from the PRSP.
- Translate a PRSP into a Medium-Term Expenditure Framework (MTEF) with annual and multi-year budgets to facilitate aid predictability.
- Strengthen Zimbabwe’s institutional structures, systems and procedures to facilitate the alignment and harmonization

of donor support so that they can synchronize their pledges and disbursement cycles with national planning and budgeting cycles.

- Strengthen parliamentary oversight and reinforce participatory approaches by involving non-state actors – the private sector, labour and civil society – in the process of developing a PRSP.

Leadership in national development

In accordance with the Paris principles, the Zimbabwe government will be required to take ownership and the lead in its own development agenda. The development process should be premised on open engagement, both internally and with donors, in order to build mutual trust and confidence. Through these consultation processes, the government would draw up a PRSP in which multi-sectoral strategies are clearly prioritized, sequenced and costed. Roles and responsibilities would be clearly attributed and linked to an MTEF, with progress indicators reflected in a monitoring and evaluation system. Moreover, the government would be committed to the reform of public institutions, particularly strengthening public financial management, accounting and reporting systems, and specifically budgetary processes and oversight. It is expected that these measures will build donor trust and allay their concerns around fiduciary risk. This, in turn, will allow for donor harmonization and assist donors to align themselves with Zimbabwe's own internally generated national priorities and strategies. It will also enable donors to move swiftly to direct budgetary support.

Building capacity to manage aid

The first priority will be to develop and strengthen the Zimbabwe government's institutional capacity to lead the development process and manage aid flows effectively.

Experience from other countries suggests that a special agency or a department for development cooperation needs to be established as a 'one-stop shop' for all aid. This could either be a dedicated agency that reports to the Ministry of Finance, or a department within the Ministry.² The main benefit of a parastatal agency is that it can immediately reduce fiduciary risk – a key requirement for donor alignment, harmonization and direct budgetary support – by recruiting professional staff and engaging reputable auditors. On the other hand, the principal benefit flowing from such an agency being housed in the Ministry of Finance is that it would be more closely linked into the government's financial and budgetary system. Either way, it needs to be linked and supported by other government agencies, such as the budgeting department, the economic policy and planning department, the Reserve Bank and the Central Statistical Office. Its key roles and responsibilities, on behalf of the government of Zimbabwe, would be to:

- Draw up a national aid policy framework containing guidelines and procedures so as to provide a coherent framework for government–donor interactions. If so required, this could include any new legal frameworks.
- Engage with the international donor community to build trust and confidence by ensuring the highest standards of transparency and accountability in order to reduce fiduciary risk.
- Develop a computerized management information system to track, trace and account for all aid flows, and disseminate information on aid to those who require or request it.
- Collect information and data, in cooperation with the Central Statistical Office, to carry out analysis and draw

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² Examples that might be looked at include Afghanistan's Assistance Coordination Authority which, while initially semi-autonomous, was subsequently moved to the Ministry of Finance.

up frameworks, strategies and plans in consultation with local stakeholders and international donors.

- Contribute to the design of a PRSP in consultation with key non-state stakeholders and donors, which establishes clear priorities for donor support that are linked to the MTEF and as a basis for negotiating debt relief.
- Develop a PAF based on a monitoring and evaluation system that eliminates individual bilateral conditionality.
- Encourage donors to align themselves with the government's PRSP and its systems and procedures, help them to move quickly towards providing direct budget support, and increase the predictability of aid flows in order to enable medium-term planning.

This aid management department should also be trained to undertake debt sustainability analysis (see below).

Development of a PRSP

As a pre-condition for foreign debt relief, a post-crisis Zimbabwe will have to start work on developing a PRSP. It should be noted that a significant level of effort will be required, particularly in light of human capacity constraints due to the brain drain, and the need for national actors to rapidly catch-up with the state of the art in the areas of poverty analysis and the design of poverty reduction programmes. International experience would indicate that the average time to develop a full PRSP currently stands at an average of 20 months, and therefore this is an undertaking that should be initiated as soon as possible in a post-crisis scenario. The quality and speed of the final document, which will have to be approved by the Bretton Woods Institutions, will depend on:

- The quality of existing poverty data
- National planning capacity

- The level of integration of government structures (especially between line ministries and the Ministry of Finance)
- The current status of consultation mechanisms between government and non-state actors.

The development of a PRSP in consultation with national constituencies and the establishment of an agency or department to manage aid should settle the question of Zimbabwe's 'ownership' of its own policies and processes. The main elements of a PRSP should include:

- A more fully integrated strategy that matches social sector plans with plans for the productive sectors. There will be a need to balance investment in the social sectors with the more difficult and longer term restructuring of economies to deliver pro-poor growth. This has been a key lesson learned in the course of the global experience with PRSPs, with the so-called '2nd generation' PRSPs. In contrast to the social sector bias evident in many '1st generation' PRSPs, more recent PRSPs grant much more attention to the centrality of robust growth rates in order to sustainably reduce national poverty levels on the basis of pro-poor growth models. These '2nd generation' PRSPs also highlight the role of the private sector in growth and what can be done to improve its performance, with many now also including analyses of areas such as trade, the financial sector and regulatory reforms.
- A sound analysis of the various transmission channels between growth and poverty reduction, as well as the impact of macroeconomic policies on both growth and poverty reduction.
- An analysis of the sources of growth, and the need for productive investment in other areas such as infrastructure and rural development.

- Addressing the tensions between fiscal stringency requirements for macro-economic stabilization and the need for increased poverty-reducing social sector spending.

Once a PRSP has been developed locally, the staff of the World Bank and IMF will conduct a Joint Staff Assessment (JSA) of the PRSP as a basis for further Highly Indebted Poor Countries (HIPC) debt relief and future concessional assistance. JSAs allow the Bretton Woods Institutions' boards to exercise due diligence and provide feedback to the country on how the PRSP might be improved.

Performance Assessment Frameworks

Zimbabwe should also establish a joint monitoring framework, known as a Performance Assessment Framework (PAF), which is a multi-annual matrix of priority targets and indicators derived from the PRSP. The PAF would be subject to an annual, joint review process by the Zimbabwe government and donors. Given clear annual and multi-year targets and indicators against which progress can be monitored, donors should be more willing to make commitments for the following years in a coordinated manner, and hence help address problems of aid predictability. And, by undertaking to use the PAF as the single conditionality framework for budget support, donors would help reduce bilateral conditionality and transaction costs substantially. Further progress could be made by donors improving their mutual accountability by agreeing to be assessed under a Programme Aid Partner's Performance Assessment Framework (PAPs-PAF) which normally involves an independent assessment of donor progress in terms of their adherence to Paris Declaration principles.

Moving quickly to budget support

By aligning themselves to a PRSP, donors should find it easier to move gradually away from stand-alone project delivery to direct

budget support modalities. The move to budget support will enable:

- a larger share of public expenditure to come under government oversight, i.e., on budget;
- greater public scrutiny through parliament; and
- greater accountability to donors.

Direct budget support will make fungibility more difficult, and it will contribute to a more transparent understanding of the impact of additional donor resources. Therefore, through a PRSP, it is hoped that donors will move quickly to provide budget support through:

- Sector-wide approaches that support a single-sector policy-implementation and expenditure framework that is implemented through a three-year MTEF or a sector investment plan.
- General budget support to the country's financial management system based on an overarching, mutually agreed national development strategy.

Drawing on experience from other countries, Zimbabwe should consider establishing an international budget support programme for its PRSP that includes:

- A mechanism for dialogue between donors and the government.
- A disbursement schedule linked to the country's budget cycle.
- A common set of benchmarks for assessing progress based on a PAF.

Disbursements might be based on a two-tranche system:

- A *base payment* that is made at the beginning of the financial year against satisfactory performance in terms of macroeconomic management criteria contained in the PAF.

- *Performance payments* based on progress made in terms of key sector indicators, and policy and institutional reforms.

One key benefit both to Zimbabwe and donors is likely to be reduced demand on Zimbabwe's national capacity, which has been eroded over the past decade, and lower transaction costs for both sides. Furthermore, it is likely to bring about improvements in terms of the integration of Zimbabwe's own budgeting, accounting and planning systems, as well as strengthening the mutual accountability of the Zimbabwe government and donors. In addition, a key consideration which will thereby be addressed is the need to enhance the accountability of the Zimbabwe government to parliament and other domestic constituencies.

Addressing donor fiduciary-risk concerns

National systems must be sufficiently reliable to address donors' fiduciary risk concerns and their need to answer to domestic constituencies in terms of the effectiveness of their aid. Zimbabwe should address these concerns by strengthening the country's public financial management systems and procedures, and by improving the administrative and oversight capacity of Parliament, the Ministry of Finance, the Comptroller and Auditor-General, and the Tender Board.

If it is decided to form a separate agency for managing aid flows, then a firm of auditors acceptable to both donors and the government should be appointed to ensure the highest standards of transparency, accountability and probity.

Consultations and oversight could more easily be exercised by civil society through the

formation of a review group made up of a network of local NGOs and other organizations with a special interest in monitoring aid effectiveness. This would not only include oversight in terms of policies, programmes and procedures, but ensuring that aid is delivered to where it is needed, when it is needed.

4.3 DEBT RELIEF AND BUILDING NATIONAL DEBT MANAGEMENT CAPACITY

4.3.1 The Highly Indebted Poor Countries Initiative (HIPC)

The chapter on stabilization deals with Zimbabwe's debt situation in 2005 – based on an IMF Staff report (IMF, 2007) – in some detail. Since then, however, it has not been possible to determine Zimbabwe's debt situation with any accuracy, or to make anything resembling a reliable or sensible projection. One of the first tasks for a post-crisis administration will be to undertake an audit of outstanding debt.

Zimbabwe would normally be eligible for debt relief under the HIPC initiative if it had a debt to exports ratio of 150 percent. In 2005, based on end-2004 data, the IMF estimated that Zimbabwe's debt/export ratio stood at 215 percent. In addition, the issue of Zimbabwe's need to be reclassified as an IDA-only country (i.e., with access to the World Bank's long-term interest-free loans and grants wing), which is a World Bank pre-condition for access to HIPC debt relief, would have to be addressed. Due to poor credit worthiness, Zimbabwe has, for a number of years, been a 'notional blend' country i.e., with notional access to both IDA and the IBRD funds at the end of 2004.³

³ The date of end of 2004 is of importance given that in December 2006 the Boards of the IMF and World Bank invoked the 'sunset clause' which had been extended a number of times since 1998. Over time the Boards had expressed concern with 'moral hazards' i.e., that continual extensions of the HIPC initiative may provide perverse incentives for countries to increase their borrowings in order to avail themselves subsequently of debt relief. As of December 2006 therefore, only countries that had already been assessed (or were assessed in the future) to have met HIPC income and indebtedness criteria based on end-2004 data, and that met policy performance criteria and adopted a IMF-WB supervised programme, were to be allowed into the HIPC stream.

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OF THEIR AID

Given its current extremely low per capita income levels, this should allow it to be reclassified as a Low-Income Country and therefore also as an IDA-only country. With the necessary political support from the IMF/WBI boards, a technical case could be developed which would make it eligible for HIPC.

If Zimbabwe's eligibility were thereafter confirmed, it would then need to take a number of measures to reach a *decision point* in order to trigger debt relief. First, it must reach agreement to clear outstanding arrears. Secondly, it should draw up and pursue an adjustment and reform programme for at least six months to demonstrate a track record of macroeconomic stability. Thirdly, it will need to develop an interim PRSP that not only outlines the nature and scope of poverty, but demonstrates a commitment and strategy to tackle poverty. And, fourthly, it would need to prepare a timeline and process for preparing a full PRSP, a three-year policy matrix, and a macroeconomic framework. This would include a strategy to use freed-up funds for national poverty reduction and sustainable pro-poor growth in the context of the PRSP.

After the IMF and World Bank have taken a decision to grant debt relief, all other creditors, such as the Paris Club, the African Development Bank and others, would commit themselves to providing sufficient assistance by a designated *completion point*.

4.3.2 Concessional funding assistance

Zimbabwe must then maintain macroeconomic stability with the assistance of the IMF Poverty Reduction and Growth Facility and carry out structural and social reforms. When this happens, full debt relief is then granted. The time between decision point and completion point can take from several months to several years.

4.3.3 Debt Sustainability Analysis

Zimbabwe should carry out a debt sustainability analysis (DSA). This analysis tries to arrive at a level of debt that would enable Zimbabwe to service its debt through export earnings, aid and capital inflows. This would require working with criteria used by the Bretton Woods Institutions and would need to integrate various risk scenarios. Normally three-year averages are used to even out volatility in export earnings and revenues. However, in Zimbabwe's case, other predictors may need to be used.

4.3.4 The dangers of 'slippage'

As Zimbabwe moves into debt relief processes, it must take cognisance of the fact that debt relief, in and of itself, is not a panacea. Further measures will be required. These should include export diversification so as to strengthen the capacity of the economy to cope with external shocks such as sharp deteriorations in its external terms of trade or fluctuations in the exchange rate. The dangers of this are very real. In 11 of 13 'post completion point' countries for which data were available in 2005, external debt sustainability had deteriorated. Since completion point, eight of these countries were once again above HIPC thresholds.

It is worthwhile recalling that, in addition to external shocks and the lack of a diversified export base – which lay behind the build-up of unsustainable debt during the 1980s and 1990s for many developing countries – poor debt management was also a major contributing factor. Zimbabwe is no exception. The dangers of slippage, i.e., a return to unsustainable debt levels after both rescheduling and debt stock reduction have been granted, should be countered by rapid progress in terms of strengthening debt management capacity. The latter is key to ensuring more prudent future borrowing and, in particular, that strong controls are exercised over who, including parastatals,

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CAPACITY

is entitled to borrow and what kinds of debts they contract. Enhanced information disclosure and public oversight will be essential components of this process of strengthening the country's debt management capacity.

4.4 AID FLOW MANAGEMENT

4.4.1 Aid flows and macroeconomic management

The substantial increase in aid flows anticipated in the post-crisis period will require careful management to maximize their beneficial impact on the economy. Normally it is argued that a hyperinflationary environment coupled with negligible foreign reserves necessitates a gradual scaling up of aid-financed spending. But Zimbabwe's case is atypical. Substantial aid inflows will be needed to finance the budget and provide the foreign exchange required to loosen the binding constraint on economic performance – foreign currency.

The spending of aid and its absorption are not one and the same. Typically, donors make aid payments to a country's central bank. These are then used by the government to increase domestic spending, while the central bank sells the aid dollars in the foreign-exchange market to finance imports. Experience shows that in countries where there is a sudden increase in aid, spending often exceeds absorption. Supply-side bottlenecks may account for this, or the government may spend the funds faster than the central bank sells the dollars to increase import supply. Whatever the reason, there is a net injection of spending power into the economy that increases import demand, exerts downward pressure on the currency and upward pressure on inflation. It is crucial that this scenario be avoided during the immediate post-crisis stabilization period.

In the short-term, aid will affect the economy in three main ways:

Imports

Foreign currency disbursed by donors will be used to finance essential imports. In Zimbabwe's case this will include food, fuel, electricity, medical supplies, inputs and capital equipment required by the productive sectors. The net effect is an increase in imports, funded either by aid transfers on the current account of the balance of payments or by aid inflows on the capital account.

Government expenditure

Aid provided in the form of budget support to the Ministry of Finance increases government expenditure and the budget deficit, thus raising the level of aggregate expenditure in the economy. Imports will increase as a result of this government spending (though, to the extent that these are funded from aid grants in foreign currency, there should be no adverse effects). But any increase in domestic aggregate demand not satisfied by increased domestic supply will add to inflationary pressure by creating excess demand for goods, services and skills. Because supply in Zimbabwe will continue to be constrained by the scarcity of foreign exchange and skills as well as infrastructural bottlenecks, there is a risk that increased aid disbursements will undermine the stabilization strategy aimed at reducing inflation dramatically over an 18-month to 2-year period.

However, provided aid inflows are used not to *increase* public spending, but rather to replace some of the quasi-fiscal expenditure of the central bank – currently financed through credit creation – the net impact will be to reduce deficit spending and slow money-supply expansion, thereby mitigating inflationary pressures in the economy. In any event, government expenditure must contract dramatically relative to GDP, both through the budget and the quasi-fiscal operations, to create space for private sector recovery. If the government can maintain control on its expenditure, aid is unlikely to pose a threat to macroeconomic stability.

An element of foreign aid will have to be used to retire domestic debt, thereby strengthening the financial system and institutional investors, who are the holders of such debt, mostly in the form of treasury bills. This will enable banks to resume intermediation – lending to customers – rather than being forced to hold government paper. This in turn will contribute to the recovery of the private sector.

Exchange rates

It is conceivable that aid inflows will give rise to exchange rate appreciation, thereby making Zimbabwe exports uncompetitive, the so-called Dutch Disease.⁴ In Zimbabwe's case this is unlikely because of balance-of-payments fundamentals, and because the gap between Zimbabwe's expected inflation rate and that of its trading partners is likely to mean ongoing currency depreciation over the short term.

Much of the policy advice on scaling-up aid flows to low-income countries is based on economies with undeveloped credit and capital markets. This is not the case in Zimbabwe, where there are strong, diversified, financial and capital markets, and where the absorptive capacity remains greater than in most other low-income countries in Africa. Accordingly, Zimbabwe is better placed than many, perhaps most, sub-Saharan African economies to use foreign aid efficiently.

4.4.2 Timing the surge

In transitional situations, it is often the case that big surges in aid take place at the beginning of a post-crisis situation – that is, they are 'front-loaded'. It is arguable that the effectiveness of such large flows is often compromised by weak national systems, be these public financial management systems, the dearth of reliable data with which to improve targeting, or the lack of sound national/sectoral policy frameworks. A post-

crisis Zimbabwe should seek to negotiate the timing of such a surge with donors in order to allow it time to ensure maximum absorptive capacity so that the longer term utility of such aid flows is maximized.

4.4.3 Managing the transition from reliance on aid to sustainable economic growth

Translating depleting resources into sustainable pro-poor economic growth

In the pursuit of rapid economic growth, developing countries often destroy their natural wealth base – for example, by mining. Because minerals are gradually depleted, a part of the income they generate, i.e., the royalties, should be saved and reinvested to build a sustainable and diversified economy. The problem is that countries with relatively high mineral wealth, such as Zimbabwe, often have a large poor population. The inclination, therefore, is for such governments to spend all royalty income from a depleting resource on consumption rather than saving and investing it for sustainable future growth. The wiser option, which has been followed by countries such as Botswana, Malaysia and Norway, is to use their royalties as an important source of development finance for investment in infrastructure, schools, hospitals or programmes of economic diversification.

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A wealth fund

To make the best use of its resources, Zimbabwe should adopt a portfolio-management strategy that is designed to ensure that its exhaustible mineral assets are channelled into production and profitable investments. This requires that:

- Estimates be made of the annual rate of resource depletion due to mining and other activities (see chapter 8 on manufacturing, mining and tourism).

⁴ See chapter 3 on stabilization.

- Revenues collected by government be deposited into a specific fund to compensate for depletion.
- These revenues from the fund are earmarked for reinvestment in productive assets and intangible capital, both within the mining sector and beyond.

The creation of such a fund needs to be ‘ring-fenced’ through appropriate safeguards, possibly legislation, against an incumbent government appropriating these funds for other purposes. Such a fund is also more likely to reduce the risks of Dutch Disease: an over-valuation of the currency and its distorting effects on the economy. Above all, a transparent ‘wealth-fund’ strategy requires the state to take explicit cognizance of resource-depletion issues, thus making government revenue mobilization and spending patterns much more rational and strategic.

IT IS CLEAR THAT EXTERNAL ASSISTANCE WILL BE REQUIRED IN ORDER FOR THE COUNTRY TO RECOVER ON ALL THESE FRONTS WITHIN A REASONABLE TIME-FRAME. YET AT THE SAME TIME IT WOULD BE ESSENTIAL FOR ZIMBABWE TO AVOID BECOMING ANOTHER HIGHLY AID-DEPENDENT ECONOMY

4.5 CONCLUSIONS

Given the extent of regression that has taken place over the last decade – exemplified by a collapsed economy, severely degraded infrastructure, a heavy internal and external debt burden and a precipitous decline in the country’s human development indicators – it is clear that external assistance will be required in order for the country to recover on all these fronts within a reasonable time-frame. Yet at the same time it would be essential for Zimbabwe to avoid becoming another highly aid-dependent economy. Inflows of aid must be managed in such a way as to ensure that there is in-built obsolescence of such flows, and that at the end of a period of intense international assistance, Zimbabwe is able to become a regenerated and international competitive economy, with a sound human and fixed capital base, and thus able to move ahead on the basis of its internally generated wealth.

Chapter 5

Recovery of the Financial Sector

There is now an overwhelming body of empirical evidence that financial-sector development matters for economic growth, and that the financial sector plays a critical role in the mobilization of savings in the economy, and in providing resources required for investment (World Bank 2007; McKinnon, 1973 and Shaw, 1973). The services of the financial sector in reallocating capital to the most efficient user and redistributing risk are a crucial catalyst for economic growth and hence development. Healthy and competitive financial markets are therefore an effective tool in spreading opportunity and fighting poverty.

The ‘Blue Book’ of the UNDESA and UNCDF (2006) observes however, that in most developing economies financial services are available only to a minority of the population. For instance, about 60 percent of the population in Southern Africa have no access to financial services. Financial-sector development strategies have largely focused on strengthening overall financial stability and increasing the availability of services to major economic actors – large firms, the government and wealthy households – leaving out the small-scale sector that constitutes the majority of economic actors. The Blue Book therefore recommends an inclusive financial-sector development strategy that makes financial services accessible to the low-income groups and small enterprises.

It is against this background that this chapter evaluates the requirements for recovery of the financial sector of Zimbabwe. Firstly, it traces the performance of the sector over three periods – the pre-reform period of the 1980s, the reform period of the 1990s, and the reform-reversal period of the 2000s. One constant feature throughout the post-independence period is that the financial sector lacked inclusiveness and hence failed

to cater adequately for the needs of the poor and the marginalized small-scale sector. Secondly, the chapter provides a situational analysis of the current status of the financial sector, highlighting constraints and challenges. In particular, the role of the Reserve Bank of Zimbabwe (RBZ) in fuelling hyperinflation through quasi-fiscal activities funded by printing money is given prominence. Furthermore, it is observed that from 2002 onwards price distortions emanating from government controls became so severe that in many instances analyses of official statistical data produce perverse outcomes. More specifically, official inflation and GDP are found to be underestimated as a result of highly questionable data sets. Finally, the chapter proposes sustainable and inclusive recovery policies and pathways for the sector.

HEALTHY AND
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IN SPREADING
OPPORTUNITY AND
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5.1 OVERVIEW OF THE FINANCIAL SECTOR

5.1.1 Development after independence

At independence in 1980, Zimbabwe had a much more sophisticated sector than any African country other than South Africa. Throughout the 1980s (as before independence) the financial sector was tightly controlled and highly oligopolistic, with multinational banks (Barclays Bank and Standard Chartered Bank) dominating the sector; market entry was restricted and competition limited. Operations were distorted by ceilings imposed on lending and deposit rates, portfolio restrictions, government-directed lending programmes, selective credit policies and exchange controls. Insurance and pension funds were essentially captive government-debt markets through the prescription of assets they could

hold. Small firms and low-income groups had virtually no access to credit. Those with small savings in the rural areas could only invest with the Post Office Savings Bank (POSB), which used the funds for on-lending to government. There was no lending window for these savers.

During the IMF-sponsored Economic Structural Adjustment Programme (ESAP) of the 1990s, financial reforms were initiated with a view to the removal of controls and widening the scope of services. Initially, the reforms led to the growth of the financial sector at an average rate of three percent per annum when other sectors of the economy were contracting. While foreign banks still dominated the market, new entrants – new commercial banks, merchant banks, finance houses, unit trusts, leasing firms, exchange bureaux, venture capital companies, formal and informal micro-finance institutions – emerged that created competition. However, the reforms did not address the structural causes that deterred financial inclusiveness. The formal banking sector continued to serve prime clients, as it had done for more than a century, leaving the small-scale sector unbanked¹. For instance, the majority of new entrants preferred to go into merchant and discount banking rather than into commercial banking in order to engage in trading risk-free government securities.

Notwithstanding their failure to achieve financial inclusiveness, empirical evidence has shown that financial sector reforms could not have worked because the macro-economic environment was not stable (Boyd *et al.*, 2001). With inflation rates in Zimbabwe averaging 32 percent per year

during the reform period of the 1990s – double the critical threshold of 15 percent,² inflation had already started to adversely affect the productive sector. Therefore, it is hardly surprising that neither existing banks nor new banks were in a position to service the untried small-scale sector, but competed for government business and established corporate customers. Hence, not much financial deepening³ took place. Nevertheless, government interpreted this market failure as reflecting reluctance by banks to service the small-scale sector. Instead of providing an enabling environment, the government's response was to increase the resources for subsidized schemes such as the Small Enterprise Development Corporation and the Capital Guarantee Corporation, initiatives that conflicted with the market orientation of the reforms. These schemes were not sustainable and by end of the 1990s were struggling to obtain financial resources.

It is noteworthy that the Zimbabwean financial sector was subjected to extended periods of financial repression⁴, with the exception of the reform period that lasted less than a decade. Empirical evidence shows that long periods of financial repression results in structural changes to economic activities (McKinnon, 1973). In Zimbabwe, the sectors that could not obtain finance from commercial banks became increasingly reliant on government intervention, producing a dependency syndrome that is evident to this day. This could partly explain why the country is trapped in a vicious circle of controls, reforms for a short period, and a return to controls with pervasive government intervention.

¹ The term 'unbanked' means having no access to financial services, especially to the credit facilities of commercial banks.

² This is the inflation-rate threshold beyond which inflation starts to undermine the development of the financial sector (Boyd *et al.*, 2001).

³ The term denotes increased usage of financial services.

⁴ The term describes a state of the financial sector characterized by controls on interest rates, market entry, competition, reserve requirements and lending to favoured sectors.

5.1.2 An overview of the current status of the sector

Presently, the financial sector comprises the Reserve Bank of Zimbabwe (RBZ) at the apex, discount houses, commercial banks, merchant banks, finance houses, building societies, the People's Own Savings Bank (POSB), insurance companies, pension funds, venture capital companies, asset management companies, developmental financial institutions, the Zimbabwe Stock Exchange, microfinance institutions and money transfer agencies (that intermediate remittances). The banking sub-sector currently comprises fifteen commercial banks, of which three have some degree of state ownership and the others are wholly privately owned, six merchant banks, three discount houses and four building societies. Four of the private commercial banks – South African-owned Stanbic Bank Limited and the Merchant Bank of Central Africa (MBCA), and British-owned Standard Chartered Bank and Barclays Bank – are multinational banks with a majority of foreign ownership. Collectively, these multinational banks command 55 percent of the commercial bank market share. These banks however, face the prospect of losing their majority foreign ownership as a result of the new Indigenization and Economic Empowerment Act (No. 14 of 2007) that requires them to indigenize 51 percent of their shareholding.

The three local banks that have a degree of state ownership (CBZ Bank, ZB Bank and ZABG)⁵ have been gaining market share through preferential treatment from the state, indicating an unfair playing field. While most institutions have the majority of their branches in major towns, there is a relative spread of branches throughout the provinces of the country, with the POSB and Central Africa Building Society (CABS) having networks that extend to rural and remote

areas. Lack of infrastructure such as reliable energy supplies, telecommunications and road network has however, hindered rural penetration.

The insurance sub-sector comprises nine life insurance firms, twenty-six general insurance firms and six re-insurers. Pension funds and insurance companies are required to invest at least 40 percent of their total asset portfolio in risk-free government paper such as treasury bills or bonds. Since government paper earns negative real rates of return due to hyperinflation and controls on yields, pension and insurance payouts have become very low and are unable to sustain the livelihoods of their beneficiaries. The only profitable avenue for them is investing on the stock exchange where asset values, in addition to moving in tandem with inflation, are exempt from capital gains tax of 5 percent. However, whatever gains are made from investments on the stock market are wiped out by highly negative returns earned from government securities.

In summary, the pension and insurance sub-sector is characterized by the following problems:

- High prescribed asset ratios in favour of government that earn highly negative returns and limit their investment.
- Many people are being retrenched and seeking payment of their pensions, as a result of the unstable macroeconomic environment.
- Both pension and insurance payouts are on the increase as a result of the HIV and AIDS pandemic.
- Payouts are on the increase, while the investment base is declining, so the sale of assets to meet payouts is not matched by new inflows of savings.

⁵ CBZ Bank was formerly known as the Commercial Bank of Zimbabwe, ZB Bank as Zimbank, and the ZABG is an acronym for Zimbabwe Allied Banking Group.

- Excessive regulation that from 1 August 1993 (but not yet aggressively enforced by government) set local shareholding at 51 percent.

Under normal conditions, the financial sector should be able to offer a wide spectrum of financial services that range from mortgage finance, leasing, hire purchase, international trade finance, retail banking, investment banking, corporate finance, microenterprise credit, short-term and long-term capital and securities. However, the majority of available finance is short term to medium term, ranging from one to five years. The stock market, insurance companies and pensions, provide medium- to long-term capital in the form of company shares, debentures, government stock, local government and quasi government bonds. In line with the continued decline of the formal sector since 2000, the microfinance sector that serves the small-scale sector and the informal economy has experienced phenomenal growth. The expansion of this sector, while a symptom of the malaise afflicting the formal sector, is however a welcome development because it provides financial services to the traditionally 'unbankable' poor and hence play a role in poverty reduction.

5.2 OVERVIEW OF PAST PERFORMANCE

From the 1980s to the late 1990s Zimbabwe's financial sector appeared quite sound, even though it was not inclusive in the sense that it largely served prime clients, ignoring small and untried clients. In response to the collapse of a merchant bank in 1998, the Reserve Bank responded by increasing the capital-adequacy requirement for the country's banks to 13 percent, a figure in excess of the internationally accepted minimum of 8 percent.

However, weaknesses in the banking sector involving newly established local banks were

encountered during the last quarter of 2003. The International Monetary Fund (IMF, 2005) cited these weaknesses as poor standards of corporate governance; inadequate risk management, and the use of depositors' funds for speculative investments; pervasive self-dealing, including unreported insider transactions; the use of subsidiaries and affiliates to evade prudential limits; the use of RBZ liquidity advances to support group companies; and deliberate misreporting to the RBZ to conceal losses and overstate capital. The IMF mission also noted inadequate supervision by the RBZ, arising both from a deficiency in the number of supervisory staff and the level of skills.

The IMF, (2007) further observed that, although the banking sector was reporting profits in nominal terms, profitability had declined in real terms and the sector faced liquidity risks. Bank balance sheets were shrinking in real terms owing to losses on an inflation-adjusted basis, arising largely from highly negative real returns on government securities and high levels of statutory reserves.

Factors that have since exacerbated liquidity risks include frequent ad hoc changes in interest rates, the lengthening of maturity of Treasury Bills at highly negative real interest rates, and the requirement that end-of-day excess bank liquidity be converted to long-term bills at highly negative real interest rates. The banking system has however, limited exposure to systemic risk because it is dominated by multinational banks. However, this stabilizing domination is now under threat from the Indigenization and Economic Empowerment Act. Foreign-exchange risk in the sector is subdued because of limited foreign-currency-denominated business.

On a scale of 0 to 10, ranging from poor to excellent, of the World Bank's *Doing Business Report*, Zimbabwe is given a score of 6.0 in its index of Legal Rights of Borrowers and Lenders for 2006.⁶ While

⁶ World Bank, *Doing Business*; Getting Credit Category: Methodology & Surveys <<http://www.doingbusiness.org/MethodologySurveys/GettingCredit.aspx>>

this score is higher than the median of 4.0 for low-income sub-Saharan African countries, it is lower than that of Zimbabwe's neighbour, Zambia, with a score of 7.0. Of particular concern, and indicative of lack of credit assessment infrastructure, is the fact that in terms of the rules that affect the scope, accessibility and quality of credit information available through either public or private registries, the World Bank gives Zimbabwe the lowest score of 0.0 on its index of Credit Information depth.⁷

5.2.1 The monetary policy of the Reserve Bank

Among the functions of the Reserve Bank of Zimbabwe (RBZ) is the responsibility for the formulation and implementation of monetary policy in its pursuit of price stability.⁸ The RBZ does not, however, have operational independence in carrying out this responsibility, as it is required by statute to consult the Ministry of Finance. The process of achieving this objective of price stability entails the identification of a monetary policy transmission process (through which its actions are transmitted efficiently) towards targeted goals.

Essentially, the evolution of Zimbabwe's monetary policy framework may be broken down into four periods:

- the control regime of the 1980s, when monetary policy was inactive;
- the shift in monetary policy strategy from controls towards monetary targeting of the early 1990s, whereby the operational target was net domestic assets⁹ as a movement towards active monetary policy;
- the shift in monetary policy strategy towards reserve-money¹⁰ targeting in the mid-1990s; and
- the current monetary policy regime, beginning in December 2003 and detailed below, that accelerated the reversal of earlier financial reforms.

5.2.2 The current monetary policy regime (from 2003)

The reversal of earlier financial reforms could be regarded as having started in 2001, when the government manipulated Treasury Bills to reduce interest rates in an endeavour to bring down a rising fiscal deficit. The 90-day Treasury Bill rate that was at around 48 percent in early January 2001 dropped to 10 percent by the end of April 2001 when annual inflation was running at 70 percent, plunging real interest rates into negative territory. The monetary system of indirect monetary control that had been adopted in 1998 was abandoned. Since then monetary policy actively promoted fiscal expansion. The situation became severe when the new central bank governor, who took office in December 2003, fundamentally changed the functions of the RBZ. Increasingly, the Reserve Bank usurped the fiscal operations of the Ministry of Finance. In addition, it assumed some of the functions of commercial banks in that it engaged in direct lending to the private sector in a very significant manner.¹¹ The central bank exhibited 'mission creep' as it began to undertake private sector and public sector functions outside its domain that included, among others, agricultural activities, manufacturing and retail activities (e.g., operating people's shops). As a result the

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⁷ <<http://www.doingbusiness.org/Documents/CountryProfiles/ZWE.pdf>>.

⁸ In terms of the Reserve Bank Act [Chapter 22:15].

⁹ This involved regulating central bank lending to government with a view to achieving price stability (controlling inflation), but the central bank could not control inflation because it could not control government borrowing.

¹⁰ Reserve money comprises currency issued by the central bank and bank reserves held by the central bank. Under reserve money targeting, the central bank fixes the level of reserve money consistent with the targeted level of money supply.

¹¹ Reserve Bank data show that the share of RBZ lending to the private sector increased from 0.6 percent in 2004 to 43 percent by the end of 2007.

THE QUASI-FISCAL
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RBZ has acquired a conglomerate structure and hence failed to focus on its core business. The Reserve Bank Act [Chapter 22:15] does not accord the RBZ the independence to carry out monetary policy and neither does it give it monetary policy goals. This has resulted in the RBZ operating on directives from the executive arm of government instead of adhering to a binding legal mandate.

Since 2004 the RBZ has engaged in quasi-fiscal activities that are funded by printing of money. Basically, these activities involve providing credit at derisory nominal interest rates to favoured sectors whose prospects of repaying are so low that these credits should more properly be viewed as subsidies. Huge losses are being incurred by the RBZ in connection with these quasi-fiscal activities. The main sources of these losses include subsidies,¹² realized exchange losses, interest cost on RBZ securities, and unrealized losses on foreign-exchange holdings. The RBZ records these losses using an accounting method that is not recommended by the IMF. Typically, it excludes realized and unrealized exchange losses and realized valuation losses from its profit-and-loss accounts but records them in a separate asset account, thereby overstating its net annual profits and capital.

Furthermore, despite operating in a hyper-inflationary environment, the RBZ does not employ inflation-accounting but uses historical-cost accounting, thereby misstating the true economic position. In fact, the financial statements of the RBZ might not reflect a fair and true picture of the state of affairs; indeed, they have even been qualified by their auditors in recent years. The IMF (2007) reported discrepancies between the budget financing requirements and financing data from banking and other sources. The latest published data in the IMF's *Government Finance Statistics Yearbook* are for 1997, and no recent data have been provided

for publication in its *International Financial Statistics*. These shortcomings suggest some weakening of technical capacity within the central bank.

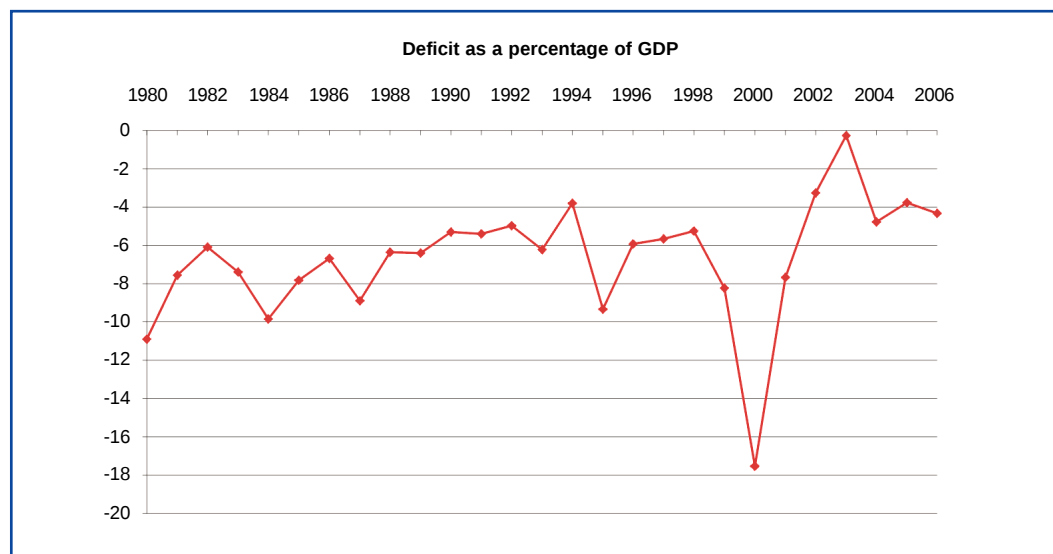
The quasi-fiscal activities have compromised control of the monetary targets. The RBZ has lost control of monetary management and is caught in a vicious circle. First, it engages in quasi-fiscal financing. Then, it endeavours to mitigate the effect of this financing through sterilization using RBZ bills. The sterilization of monetary expansion has, in turn, resulted in increased losses, as nominal interest payments on RBZ bills increase rapidly with rising inflation. In addition, rising interest payments have increased the financing requirement of central government, thereby creating further monetary expansion. Ultimately, the effectiveness of sterilization using RBZ bills is weakened. Since quasi-fiscal activities are not being consolidated in the national fiscal budget, the budget deficit as a percentage of GDP has been understated. Figure 5.1 shows the trend of a declining budget deficit as a result of the exclusion of the quasi-fiscal activities. Coorey *et al.*, (2007) have re-estimated the financing requirement after adjusting for quasi-fiscal activities to show the true position, which is illustrated in Table 5.1.

Notably, there is a widening gap between the primary balance and the financing requirement, indicating the magnitude of quasi-fiscal activities and possibly hidden expenditures under contingencies.

Munoz (2006) has illustrated that the escalation of inflation since 2004 was fuelled by rapid reserve-money growth emanating from the RBZ's quasi-fiscal activities. Table 5.2 shows contributions of individual balance-sheet items to changes in reserve money. Quasi-fiscal losses, indicated as 'other items net', are evidently major contributors.

¹² These involve free foreign exchange to public enterprises, price supports to exporters to partially compensate them for an overvalued exchange rate, and subsidized credit to troubled banks, farmers and public enterprises.

Figure 5.1: Trend of central government budget deficit (excluding quasi-fiscals)



Source: Derived from RBZ statistics

Table 5.1: Adjusted fiscal position

	2004	2005	2006 ^a	2007 passive scenario ^b
Percentage of GDP				
Central government				
Revenue	33.8	43.7	51.3	40.1
Expenditure	41.5	49.6	58.6	66.6
Of which: Wage bill	15.3	18.1	17.1	16.1
Overall balance	-4.7	-3.1	-5.4	-25.6
Primary balance	-1.7	3.7	2.3	-13.9
Adjusted fiscal position				
Primary balance	-26.9	-17.2	-24.7	-40.2
Financing requirement	-29.9	-64.3	-80.3	-88.0

^a Estimate. ^b Conservative estimate

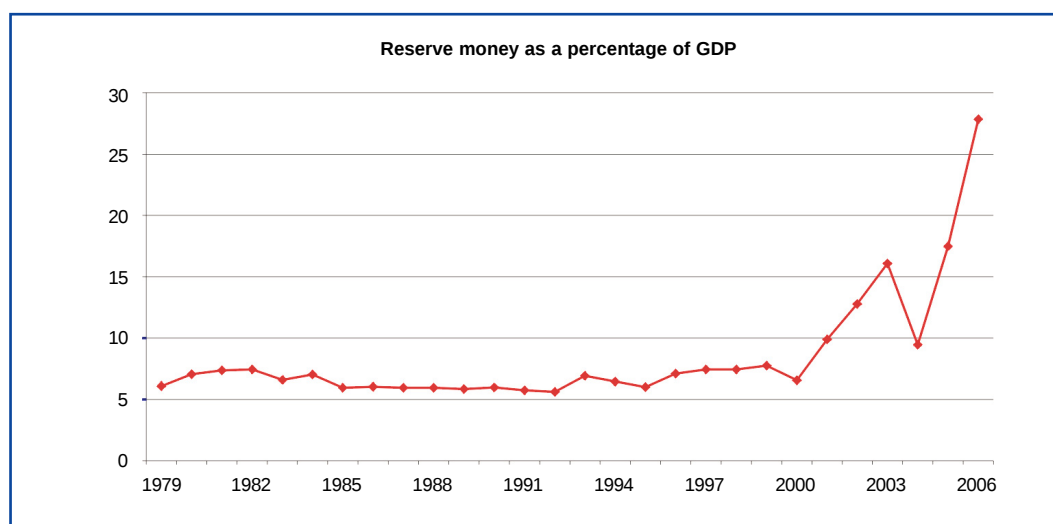
Source: Coorey et al., (2007)

Table 5.2: Contributions to changes in reserve money*

	2003	2004	2005	2006
Reserve money	10.6	6.7	13.8	20.2
Net foreign assets	-4.1	-7.1	-43.2	-1.4
Claims on banks	4.2	2.3	0.6	1.8
Net claims on government	4.3	-0.1	-3.3	-0.2
RBZ securities	0.0	-21.5	-32.2	-32.4
Other items net	6.2	33.1	91.9	52.4
Of which:				
Subsidies	4.0	13.9	20.3	15.4
Realized exchange losses	1.2	11.4	0.6	7.7
Interest cost of RBZ bills	0.0	5.1	40.4	41.0

* Change since end of previous year, as a percent of annual GDP

Source: Munoz (2006)

Figure 5.2: Trend of reserve money over years

Source: Derived from RBZ statistics

Analysis of the trend of reserve money as a percentage of GDP since 1980 shows a sharp increase since 2004 (Figure 5.2) meaning that the monetary policy of targeting reserve money had been abandoned in favour of printing money.

Predictably, the printing of money by the RBZ has led to hyperinflation, with inflation rising from an annual average of 386 percent 2003 to over 11.2 million percent by mid-2008. Accordingly, the domestic currency has been rendered worthless and have been redenominated twice in a space of two years. First, in order to make ever-rising denominations manageable for the public and business, three zeroes were removed in August 2006 when annual inflation averaged 1,017 percent. Second, ten zeroes were removed on 1 August 2008 when annual inflation was officially estimated at over 11.2 million percent. In an unprecedented move, the RBZ re-introduced old coins (which literally had become souvenirs) that had been demonitized in 2002 (incidentally when average annual inflation was 135 percent) as legal tender at their face value. The implication of this unprecedented move was that the RBZ completely lost track of its monetary base because it could no longer track notes and coins in circulation. Without an accurate

grasp of notes and coins in circulation when the printing press is in overdrive meant that fighting inflation became a wild goose chase.

Rising inflation has seen the value of the domestic currency against other currencies continuously declining. Since the currency crash on 14 November 1997, the exchange rate has been overvalued and a managed fixed peg characterized by multiple exchange rates. In addition to adversely affecting export competitiveness, the overvalued fixed exchange rate resulted in an informal parallel foreign-exchange market where agents buy and sell foreign currency at arm's length rates that approximate market rates. The foreign-exchange market was partially liberalized on 5 May 2008 for private agents while the government continued to access foreign exchange at a tiny fraction of its market value.

The informal parallel foreign-exchange market was further aided by RBZ controls on foreign currency deposit accounts which had thrived since the mid-1990s. The result was that people held foreign currency outside the domestic banking system. Migrant remittances were also intermediated on the informal market and there were no incentives to deposit them with banks.

5.2.3 The banking sector

The performance of the banking sector is analysed over three periods: (1) 1980–1990, when it was under explicit financial repression; (2) 1991–1999, when some financial reforms were initiated; and (3) 2000–2007, when there was a reversal of reforms and a return to controls. The performance of the country's agricultural financing mechanisms is also covered in the next section.

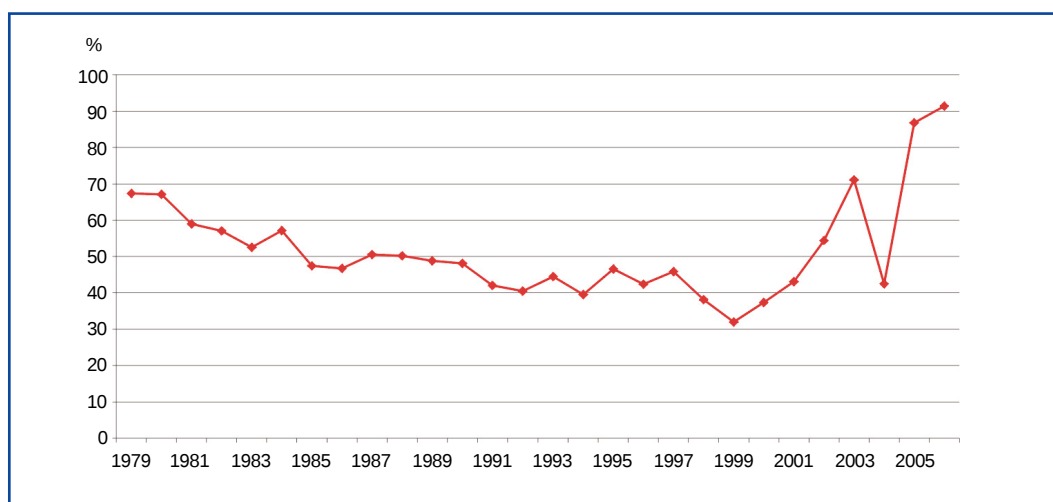
Analysis using the basic indicator of financial deepening, i.e., the ratio of money supply¹³ (M3) to GDP, yields a dichotomous result. First, as expected and illustrated in Figure 5.3, financial deepening has a downward slope during the 1980s when there was financial repression. During the reform period the ratio first stagnated at lower levels than in the pre-reform period, indicating the limited impact that reforms had on financial deepening. Thereafter the ratio started to decline in the last years of the 1990s.

The ratio shows a different trend after 2000. The financial-deepening ratio shows an

upward trend such that by 2003 it had reached its level at independence in 1980. Incidentally, this is the period when many new domestic banks entered the sector, and these included Time Bank, Kingdom Bank, Metropolitan Bank, Century Bank, Barbican Bank, Trust Bank, Royal Bank, as well as numerous asset-management companies. However, after 2003 the ratio of money supply to GDP declined sharply, from 70 percent to 40 percent by the end of 2004. This was to be expected, given the contemporaneous shake-up in the sector which resulted in the collapse of many of the new entrants.

A puzzling trend began to emerge after 2004. The financial-deepening ratio took an upward trend in defiance of fundamentals. The ratio no longer reflected healthy financial development but rather the printing of money and possible underestimation of prices in the measurement of GDP and the informalization of the economy. USAID, which has computed the ratio as an average of broad money supply to GDP over the whole period (rather than normally as at end of period), produced similar results (USAID, 2007).

Figure 5.3: Financial-deepening ratio (money supply as a percentage of GDP)



Source: Derived from RBZ statistics

¹³ Money supply measures are as follows:

M1 includes currency held by the public, plus travellers' cheques, demand deposits and other checkable deposits.

M2 includes M1 plus time deposits other than large certificates of deposit.

M3 includes M2 plus all large time deposits, institutional money-market funds, short-term repurchase agreements, and other deposits at institutions that are not banks.

The upward trend in the financial-deepening ratio after 2004 coincided with the explosion of quasi-fiscal operations. The share of non-earning assets emanating from quasi-fiscal activities rose from 22 percent in 2003 to 46.5 percent in 2004, 70.3 percent in 2005 and 83.3 percent by October 2006 (IMF, 2007). It was during this period that private sector lending by banks declined, falling from over 80 percent in 2002 to 34 percent in 2006. It is noteworthy that the average for sub-Saharan Africa is 76 percent, while the average in conflict economies is 44 percent, meaning that Zimbabwe is performing worse than countries in conflict. At the same time, government spending as a percentage of GDP rose from 25 percent in 2003 to 65 percent in 2006 against the rise in the financial deepening ratio from 40 percent to 90 percent. Figure 5.4 shows a trend that indicates that government expenditure is actually driving the perceived financial deepening. In fact, what is happening is not financial deepening but money creation by the central bank, which is funding fiscal and quasi-fiscal activities through the printing of money.

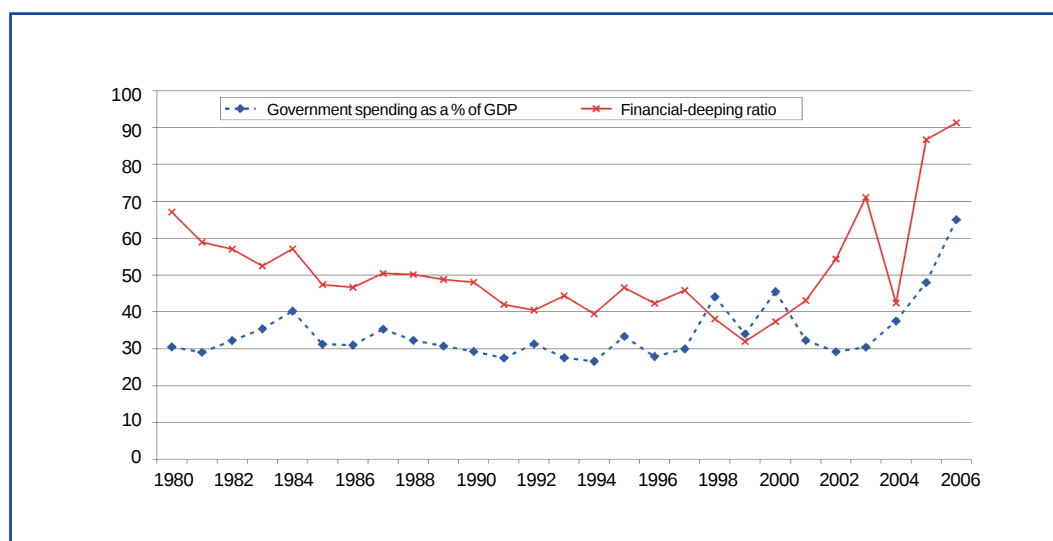
USAID (2007) estimated that the real interest rate on bank loans averaged -27.7 percent in the five years to 2005. This is in contrast to an average of 10.7 percent for

low-income sub-Saharan African countries, 5.6 percent for South Africa and 7.7 percent for Zambia. The critical role that interest rates play as a price mechanism for screening out inefficient or unproductive investments is completely negated by these high negative real interest rates. Borrowers are in more favourable positions than savers because they repay banks less than the amount borrowed after adjusting for inflation. There is an increasing incentive to borrow as inflation accelerates.

A broader picture is obtained when the currency (notes and coins) in circulation in the whole economy is analysed as a ratio of GDP, as illustrated in Figure 5.5.

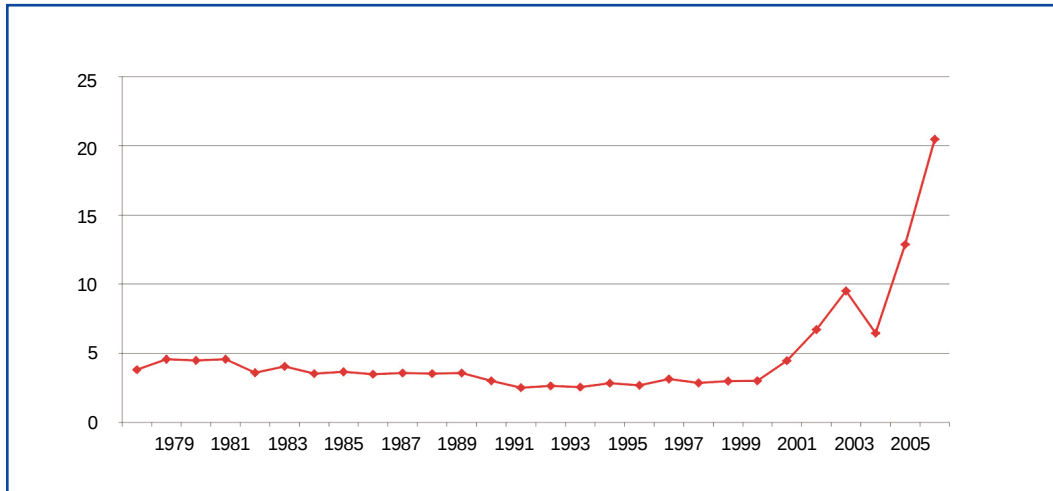
In line with countries with developed financial systems, the ratio of the currency in circulation to GDP had remained below 5 percent until 2002, when it started to rise exponentially, reaching 20 percent by 2006. In South Africa the ratio is well below 5 percent, an indication of a well-developed financial sector and a trend towards a cashless economy, where 'plastic money' is more widely used than cash (Akinboade and Makina, 2006). Thus Zimbabwe is retrogressing to a position similar to countries (usually failed states) with very weak financial sectors that operate largely on a cash basis.

Figure 5.4: Evolution of government spending and financial deepening



Source: Derived from RBZ statistics

Figure 5.5: Currency in circulation in the economy as a percentage of GDP

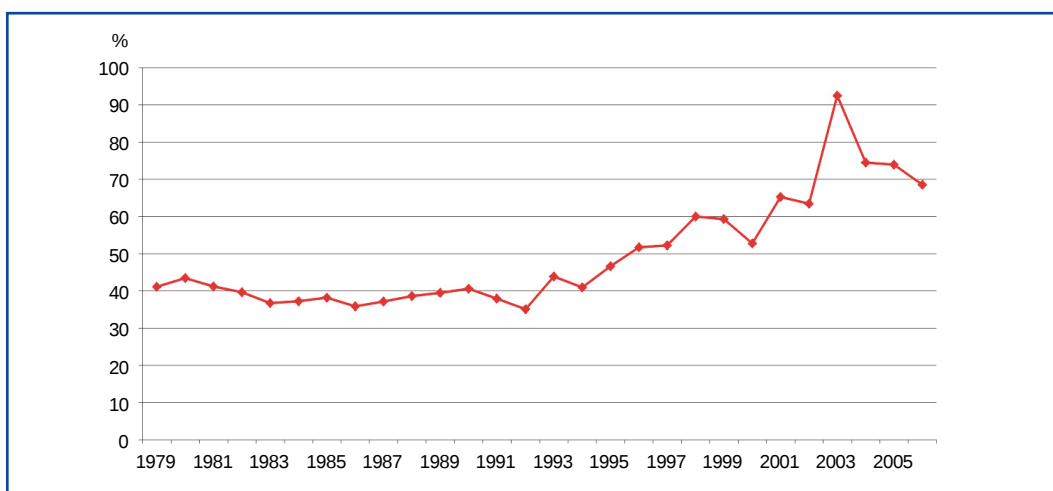


Source: Derived from RBZ statistics

Given concerns about the underestimation of GDP owing to price controls and the fact that the larger part of the economy has become informal, the ratio of narrow money (M1) to broad money (M2) could give a better picture of the retrogression of the financial sector. The M1 to M2 ratio should be inversely related to a country's level of financial development when there is increasing usage of financial services. If this ratio decreases, financial-sector development will be occurring because savings deposits would be increasing more rapidly than transaction (demand) balances. When there is a preference for liquidity, as is currently the situation, demand deposits have an abnormal weight in the total deposits. A ratio of 100 percent would suggest that all

deposits are on a sight (demand) basis. Figure 5.6 shows that the ratio in Zimbabwe has been moving towards 100 percent since 2003, meaning that most deposits are on a sight basis. In sum, this means that there is tremendous pressure for the withdrawal of funds from the banking sector. Controls on withdrawals are holding back a run-down on deposits. Ironically, quantitative controls on withdrawals by the Reserve Bank might have contributed to the stability of the banking sector in that they are preventing capital flight: otherwise the present hyperinflationary environment could have precipitated a run on deposits for conversion to foreign currency and commodities or investments on the stock exchange in order to preserve their value.

Figure 5.6: Ratio of M1 to M2



Source: Derived from RBZ statistics

5.2.4 Agricultural financing mechanisms

Both before and after independence, commercial banks provided short-term capital to farmers on the strength of their collateral, i.e., freehold title. In addition, lending (that included long-term) to agriculture was undertaken by the Agricultural Finance Corporation (AFC). In the 1970s it extended its lending to African small-scale commercial farmers to whom government had granted freehold tenure in specially designated areas, the African Purchase Areas, which had been in existence since 1930.

After independence, lending to farmers in communal and resettlement areas was boosted. Brownbridge and Harvey (1998) reported that there was a sharp increase in borrowers in the communal and resettlement areas, from 4,400 in 1980 to 70,000 by 1984. However, this represented only 8 percent of an estimated 850,000 farming households, meaning that access to credit for the small-landholder sector was minimal. Notwithstanding the small size of the communal farmers' loans, their repayment record was poor for several reasons. These included droughts—especially in 1982/3, 1984/5, 1987/8, and even more seriously in 1992/3 and because loans were guaranteed by the government, there was no incentive for the AFC to recover debts. Because of the poor loan-repayment rates, smallholder credit tailed off considerably. Even in 1985, at the zenith of smallholder agriculture production, only 8 percent of farmers received agricultural credit from the AFC. During the 1989/90 cropping season only 44,000 small-scale farmers received loans, a drop of over 40 percent from the peak 1985 levels (Rohrbach *et al.*, 1990).

In 2000 the AFC was commercialized and named Agribank so that it could operate as

a sound financial institution, able to mobilize savings that allocated credit to projects that were judged financially sound on the basis of market criteria. However, its intended customers, the resettled small landholders and communal farmers, had become accustomed to low, subsidized interest rates and government intervention, both in loan delivery and salvage from the non-payment of loans. This practice, inherited from the AFC, has been perpetuated by Agribank, despite it having been commercialized. The fast track land reform programme set in motion in 2000 has severely affected the performance of its lending, as subsidized loans were disbursed without consideration of their repayment.

Some innovative financing arrangements – that included out-growers' schemes operated by Olivine and Consolidated Farming Industries (CFI) and input schemes operated by the Cotton Company of Zimbabwe (Cottco) and later on by Cargill Cotton – have had a fairly good repayment record. Box 5.1 gives an example of one input scheme that does not require beneficiaries of credit to have title deeds to the land they are working on.

It must be noted however, that since the introduction of the fast track land reform programme, commercial bank lending to the agricultural sector has been limited, because existing collateral arrangements, including the recently introduced 99-year leases, do not provide adequate security of land tenure (Coorey *et al.*, 2007).¹⁴ The Gazetted Land (Consequential Provisions) Act [Chapter 20:28], which came into force in December 2006, made it an offence to occupy these farms without government authority, i.e., an offer letter to 'new farmers' or leases to existing farmers. In November 2006 President Mugabe handed over 125 leases to A2 farmers,¹⁵ but no further moves have since been made to provide leases – which

SINCE THE INTRODUCTION OF THE FAST TRACK LAND REFORM PROGRAMME, COMMERCIAL BANK LENDING TO THE AGRICULTURAL SECTOR HAS BEEN LIMITED, BECAUSE EXISTING COLLATERAL ARRANGEMENTS, INCLUDING THE RECENTLY INTRODUCED 99-YEAR LEASES, DO NOT PROVIDE ADEQUATE SECURITY OF LAND TENURE

¹⁴ 'Report of the Presidential Land Review Committee on the Implementation of the Fast Track Land Reform Programme, 2000–2002' [Chairman: C. M. B. Utete], 2003. Unpublished.

¹⁵ See chapter 9 on agriculture.

Box 5.1: Cotton Input Scheme

In the 1980s Zimbabwe's commercial farmers accounted for about 80 percent of cotton production, and since they had access to commercial credit, there was no need for a special input-credit scheme. The need for an input-credit scheme was felt only in the 1990s, when the share of small-scale farmers rose to 60 percent of total production. This scheme was introduced following the drastic 1991/92 drought season. The average yield of small-scale farmers had fallen dramatically and it was clear that the small farmers would not have the cash to purchase inputs for the next crop. Credits extended by the World Bank and the IMF were used to launch a new credit scheme which proved very successful. Within a year the production of small farmers was back to pre-drought levels.

When the Cotton Marketing Board was abolished in 1995, subsidies to the textile sector were reduced; the least efficient mill closed down, and the share of fibre (cotton lint) that had been sold at a discount to domestic textile mills fell from 40 percent to 20 percent. When the producer prices improved as a result of competition between buying companies, particularly following the entry of Cargill, the successor to the Cotton Marketing Board, Cottco decided to extend the operations of the input-credit scheme. When in 1999 Cottco took over Cotpro, a relatively smaller player in the market, it captured 75 percent of the market share, and this was attributed mainly to its efficient input-credit scheme.

The input-credit scheme is a group scheme in which farmers, organized into a close-knit group, are given input credits individually, but the continuity of the facility is dependent on the whole group's ability to repay the offered credit at the end of each season. In the event of one individual in the group defaulting, all the other members of the group will not be extended credit in the next season. Because of this typically Grameen Bank-style scheme¹⁶, the pressure is on all the members of the group to support each other during the season and to minimize the possibility of default. As a result the scheme has been successful, and Cargill, the next largest player in the Zimbabwean cotton market, later started its own input-credit scheme. The downside of the scheme is the temptation for individual farmers to engage in 'side-marketing', i.e., sell their cotton to 'poachers' who are normally small buyers who announce more attractive prices, which they can afford by not clearing input credits. To limit 'poaching', Cottco screened farmers more carefully and rewarded the most creditworthy by granting them the status of 'Gold Club Members'.

in any case, do not provide sufficient collateral for loans. The point is that there is no land tenure security, and not even leases for most occupiers. The government can issue and withdraw 'offer letters' at will. For example, in February 2008, the government reported that it had 'taken back' 1,449 farms that had been allocated to A2 farmers.

5.2.5 The stock exchange

The Zimbabwe Stock Exchange (ZSE) is a relatively well-developed stock market, with 80 trading firms, which achieved a market capitalization of over 70 percent of GDP in 2005, ahead of the median of 14.3 percent of low-income sub-Saharan African countries but still lower than South Africa's, which is

over 200 percent. USAID (2007) noted, however, that this could be an overestimation because of the underestimation of GDP caused by the spread of black-market transactions and unrecorded inflation. Nevertheless, the exchange is relatively vibrant in raising new capital for companies, as well as in providing a liquid secondary market. Imara Asset Management reported that the ZSE had gained 225,000 percent in nominal terms by the end of November 2007.¹⁷ Real (i.e., US dollar) returns were achieved. This has made the ZSE a useful avenue for investors to protect their capital in real terms, without which savings would already have been wiped out by hyperinflation and the economy could have been substantially smaller than it is.

¹⁶ This is a group lending scheme, whereby lending is done to a group of individuals that is collectively liable for repayment, popularized by Grameen Bank, a Bangladeshi microfinance institution. Repayment is enforced through peer pressure, so no physical collateral is required by the bank.

¹⁷ Investment Notes, December 2007.

Imara further observed a close correlation between the amount of money that is created by the RBZ and the ZSE. Since its Monetary Policy Statement in October 2007,¹⁸ the RBZ has been flooding the money market with BACOSSI and ASPEF public funds in addition to government and quasi-fiscal funds.¹⁹ While these funds may not directly go into the stock market, the liquidity of the banking system is increased as corporate and personal bank accounts are credited with the new monies from the RBZ. On the other hand, banks would need to invest these funds in new loans very quickly in order to avoid surplus liquidity being swept up into the compulsory 270-day, low-yielding bills of the RBZ. This scenario has led to the whole economy having access to low-interest loans from banks eager to lend to clients. Having obtained these loans, the borrowers need to spend the funds very quickly, or to invest the funds into the stock market, in order to preserve the real value of their capital. Alternatively, they buy foreign currency to preserve its value. When the borrowers require the funds, either for production or for consumption, they dispose of part of their stock-market holdings, or sell part of their foreign-currency holdings, and channel the money back into the banking system. In essence, the BACOSSI and ASPEF subsidized funds meant to boost productivity in the private sector are being diverted to speculative activities, a problem which the monetary authorities have themselves acknowledged (RBZ, 2008).

5.2.6 The microfinance sector

Microfinance institutions emerged in the early 1990s and have experienced phenomenal growth: there were 309 registered microfinance/moneylending institutions by the end of 2007. While some attract donor funding, the majority are

privately owned, operating on a commercial basis. To a large extent their growth was a reflection of the failure of the banking sector to cater for the small-scale borrower. Their growth has also been correlated with unemployment, deteriorating living standards, deepening poverty, and the growth of the informal sector. By providing financial services to the 'unbanked' poor communities, they have played a facilitation role in economic development through the provision of credit and the creation of employment. Microfinance institutions have the potential to provide for the 'missing middle' in the financial sector.²⁰

Despite the microfinance sector undergoing phenomenal growth, its performance has faced a number of constraints: although the government has recognized the role of microfinance in development, it has not created a proper regulatory environment. Currently, the sector is regulated under the Banking Act [Chapter 24:20], which is inappropriate for the unique features of the sector, especially the fact that they are prohibited from accepting deposits. Licensing procedures are burdensome and the licenses are issued for one year only, creating the uncertainty of renewal and hence deterring long-term funding commitments.

The Money Lending and Rates of Interest Act [Chapter 14:14] that stipulates the interest rates that the sector must charge is out of date, so the official lending rates are completely sub-economic. As a result, microfinance institutions that are licensed and regulated by the RBZ are threatened with closure, while those that operate informally thrive. The unstable macro-economic environment characterized by hyperinflation has not spared their operations. Out of the total of 309 registered institutions, only 150 were still operational by mid-2008, with the majority having

¹⁸ < <http://www.rbz.co.zw/pdfs/2007mid/mpsmidyear011007.pdf> >.

¹⁹ BACOSSI, an acronym for Basic Commodities Supply Side Intervention, is a subsidized lending scheme of the RBZ to the private sector for the purpose of producing basic commodities such as bread, mealie-meal, sugar, cooking oil, etc. ASPEF stands for Agriculture Sector Productivity Enhancement Facility, which is another RBZ subsidized lending scheme for the working capital needs of farmers.

²⁰ See chapter 9 on private sector development.

ceased operations and surrendered their licences due to viability constraints.

Nevertheless, information about the sector is scant and because there is burdensome regulations, many institutions that thrive operate informally in order to evade controls. In the absence of this information, it is difficult to identify and define the role of the sector vis-à-vis small- to medium-scale enterprises. There is a diversity of microfinance institutions in terms of ownership structure, size, location, products offered, sophistication and target markets. Hence, authorities accustomed to a ‘one size fits all’ policy find it difficult to develop appropriate policies. In addition, the role of the state and the central bank in microfinance development has not yet been clarified.

5.2.7 The diaspora remittance transfer mechanism

From 2004 the Reserve Bank designated money transfer agencies (MTAs), some of which are separate units of commercial banks, as the legal vehicles to provide remittance transfer services from the diaspora. The Reserve Bank also established its own MTA, Homelink (Private) Limited. Homelink was formed primarily to channel foreign currency from the diaspora to government instead of to the parallel market.

At the time of writing, there are only four banks that have business units registered as money transfer agencies (MTAs). Many

barriers to entry to the remittance market have prevented more financial institutions participating in this market. The services offered by MTAs are restricted – they are not, for instance, allowed to conduct bureau de change functions. The operating environment is both a barrier to new entrants and too stringent for those already operating. For a start, the minimum capital required of US\$100,000 is a huge barrier to entry. Other specific operational restrictions that need to be addressed are the following:

- The MTA is not allowed to purchase foreign currency from any person or institution under any circumstances.
- The MTA is not allowed to demand any fees, commissions or charges from the recipient customer but instead will be paid an agency’s commission in Zimbabwe currency by the RBZ.

The first prohibition prevents MTAs from competing with the informal remittance sector and thus makes them unattractive business propositions. The second reduces MTAs to being simply agents of the RBZ. As a result MTAs do not operate as independent businesses. Furthermore, the RBZ has given Homelink the responsibility of supervising other MTAs, which set-up allows it to be both referee and player as it has the power to recommend de-registration of competitors.

Generally, the performance of MTAs has been sub-optimal as Table 5.3 illustrates.

Table 5.3: Foreign-currency receipts (US\$), 2006–2007

Type	2006	Contribution (%)	2007	Contribution (%)
Export proceeds	847,766,400	62	648,608,172	62
Free funds	256,298,697	19	195,572,974	19
Gold receipts	126,773,818	9	93,517,127	9
Loan proceeds	102,930,006	8	83,371,326	8
Income receipts	24,264,596	2	16,737,628	1
MTAs	5,201,138	0	14,049,674	1
Capital investments	1,214,917	0	4,478	0
Total	1,364,449,572	100	1,051,861,379	100

Source: Reserve Bank of Zimbabwe

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BEING
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THROUGH FORMAL
BANKING
CHANNELS

The official statistics show that remittances channelled through official channels, MTAs, constitute an insignificant percentage of total foreign-currency receipts. Using incomplete data, the International Fund for Agricultural Development (IFAD) has estimated that diaspora remittances to Zimbabwe in 2006 amounted to US\$361 million, constituting 7.2 percent of GDP.²¹ However, some estimates put annual remittance flows (both informal and formal) at between US\$500 million to US\$1 billion, constituting between 7 percent and 10 percent of GDP (Makina, 2007; Orozco and Lindley, 2007).

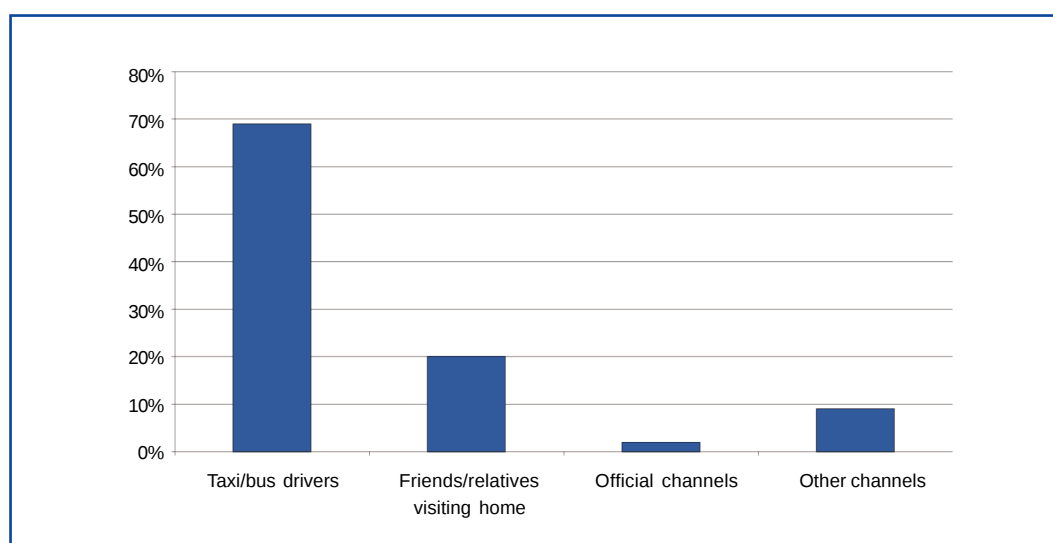
The problem of measurement is severe because remittances are being intermediated through informal channels. A survey study conducted in South Africa found that only 2 percent of Zimbabwean migrants use formal channels and that 98 percent use a variety of informal channels, as Figure 5.7 illustrates.

The result is that the government is unable to leverage remittances for development. This means that efforts need to be directed to removing the impediments to remittances being intermediated through formal banking channels so that they can be measured and become an input into policy formulation.

Remittances sent home by migrants are viewed as having a development impact that addresses issues related to the distribution of wealth and overall improvements in people's quality of life (Orozco and Fedewa, 2006). Policy recommendations have accordingly linked the financial intermediation of remittances as key to them being harnessed in order to strengthen their development impact. Financial intermediation of remittance flows can provide both senders and recipients with access to asset building which is just as essential to development as is education and health. It can lead to development because money transferred through financial institutions can also pave the way for senders and recipients to gain access to other financial products and services. Remittances give banks an opportunity of reaching out to both unbanked recipients and recipients with limited financial intermediation. The banking relationship that ensues affords recipients the ability to establish credit histories that foster access to credit.

The poor performance of MTAs has been attributed to the Reserve Bank's ever-shifting policies, particularly with respect to the payment of receipts in local currency or

Figure 5.7: Mode of remittance transfer from South Africa



Source: Makina (2007)

²¹ IFAD, Sending Money Home, Worldwide Remittance Flows to Developing Countries, 2007: < <http://www.ifad.org/events/remittances/maps/index.htm> >

foreign currency and inappropriate exchange-rate policy. When they were established in 2004, MTAs were allowed to pay recipients in foreign currency. The Reserve Bank however, changed this policy in 2005 and recipients were paid in local currency using the (controlled) foreign-exchange auction ruling rate. As a result MTAs experienced a decline in remittances and consequently operations became unprofitable. The difference between the official exchange rate and the parallel exchange rates forced Zimbabweans abroad to seek alternative means to send money to their families or other beneficiaries. The frequent changes in policy resulted in most MTAs' volume of business dropping to unsustainable levels and leading to the deregistration of many of them. In 2007, recipients were again given the option of receiving their money in local or foreign currency, as a result of which the volume of remittances increased significantly, as reflected in Table 5.3.

Corrective measures would therefore need to be directed at having a favourable exchange-rate policy and providing a conducive environment for MTAs to operate in.

5.3 CONSTRAINTS FACING THE FINANCIAL SECTOR

5.3.1 Macroeconomic environment

Hyperinflation has eroded people's savings and the capital of financial institutions because the regulations governing financial institutions force them either to purchase government treasury bills that yield highly negative real interest rates or to make deposits at the RBZ that pay no interest. Very high statutory-reserve requirements have effectively curtailed the financial sector's capacity to

intermediate savings and investment to support economic growth. They have inflated the spreads between lending and deposit rates as the cost of borrowing has increased, and passed it on to borrowers, further dampening growth, depressing returns on deposit and hence providing a disincentive for savings. The ever-growing rules and restrictions emanating from the RBZ have added to the administrative burden of both borrowers and banks.

The Indigenization and Economic Empowerment Act, which requires foreign-owned financial institutions to dispose of 51 percent of their shareholding to indigenous Zimbabweans,²² has added further uncertainty to the operating environment.

5.3.2 Legal environment and governance

The regulatory environment is fragmented and characterized by ever-shifting and unpredictable policies. The Banking Act does not take into account the fact that other banking institutions – such as building societies, the POSB, asset-management companies and microfinance institutions – have been directed by the Minister of Finance to be regulated under the Act, despite their having their own administrative Acts. The current situation has therefore resulted in financial institutions having to operate under multiple Acts: for instance, the POSB is governed by both the POSB Act and the Banking Act.

A by-product of a fragmented regulatory environment has been excessive regulation. Since the financial turmoil of 2003–2004, the authorities have tended to over-react, even where systemic risk to the financial system has not been evident. Excessive regulation is hampering the development of self-regulatory structures that complement official regulation. Self-regulatory structures

²² Indigenous Zimbabwean is defined in the Act to mean 'any person who, before the 18th April 1980, was disadvantaged by unfair discrimination on the grounds of his or her race, and any descendant of such person, and includes any company, association, syndicate or partnership of which indigenous Zimbabweans form the majority of the members or hold the controlling interest'.

such as industry associations are critical for moral suasion to be effective. While authorities must insist on transparency, financial institutions should be given some freedom to determine their own policies on matters for which they are held responsible.

The fact that much operational reliance is being placed on ministerial notices and RBZ discretionary directives shows that legislation governing the financial sector is inadequate. This is actually, as an example, crippling the microfinance sector. The sector is being burdened by interest-rate caps emanating from the outdated Money Lending and Rates of Interest Act.

5.3.3 Unfavourable operating environment for mobilizing diaspora remittances

As mentioned above, diaspora remittances, which could have been a significant source of foreign currency, have largely been intermediated outside the formal banking system. This is because of the absence of an enabling operating environment for institutions charged with mobilizing remittances. The following factors have acted as constraints:

- An inappropriate exchange-rate policy.
- Shifting policies on the currency (local or foreign) that recipients of remittances can receive.
- The capital requirement of US\$100,000 for an entity to enter the remittance transfer market, which is a barrier to entry for many would-be players.
- The operating guidelines and prohibitions (discussed earlier), which reduce the existing money transfer agencies to being simply agents of the RBZ.

5.3.4 Institutional constraints

In addition to usurping some Ministry of Finance functions and engaging in quasi-fiscal activities, the RBZ has also encroached into the activities of the

commercial banking sector: it has become a significant direct lender to the private sector. Private commercial bank lending is being crowded out. In addition, the RBZ is usurping mundane commercial bank activities, such as managing the foreign-exchange accounts of clients.

In the agricultural sector, the new land tenure arrangements act as a constraint to commercial bank lending. The commercial banking sector was accustomed to the freehold tenure system with regard to the farming sector; the existence of many small landholders without security of tenure is a novel and unresolved challenge.

5.3.5 Infrastructure constraints

Compounding the problem of servicing small landholders scattered in rural or farming regions is the lack of adequate infrastructure to achieve meaningful financial services outreach. The expansion of financial services requires well-functioning ‘hard’ infrastructure: telecommunications, electricity supply and roads. Power and telecommunications services are currently erratic and adversely affect the smooth functioning of the financial sector.

Furthermore, the absence of ‘soft’ infrastructure, such as credit data bureaux that monitor credit-risk profiles, is a deterrent to improving work ethics and business conduct. While there are mechanisms for assessing the credit profiles of prime clients, this is not the case for Small or Medium-sized Enterprises (SMEs) and small landholders who constitute the ‘missing middle’ in terms of access to financial services.

5.4 SUSTAINABLE RECOVERY PATHS AND POLICY RECOMMENDATIONS

Given that the causes underlying the financial sector’s malaise include the lack of strong credit cultures and governance mechanisms

in financial institutions, and pervasive official interference in financial markets (summed up as financial repression), the strategic action required entails both financial and institutional reform. The reform regime should, *inter alia*, address the shortcomings of the reform efforts of the 1990s and in particular, the failure to provide financial institutional capacity to service the small-scale sector.

The major strategic thrust must therefore be the development of an inclusive financial sector. The UNDESA and UNCDF Blue Book (2006) recommends that the government could play a supportive role by setting an overall policy stance, a regulatory framework, and legal structures that encourage responsive financial services for the poor.

5.4.1 Addressing the legal and regulatory environment

Legislation governing the RBZ, the Reserve Bank Act, does not give it operational independence and hence it is subject to political interference. This shortcoming should be eliminated through a constitutional amendment that confers independence to the central bank so that Parliament has direct oversight of the RBZ, thus attenuating the scope for political interference by the Executive. Furthermore, the conglomerate structure of the RBZ requires to be dismantled so that it focuses on its core business.

With regards to the overall regulatory environment, the UNDESA and UNCDF Blue Book (2006) recommends the designing of regulatory structures in tiers to recognize the differences in the structure of ownership, governance, capital, funding and risks faced by different financial institutions so as to keep regulations appropriate, simple and straightforward. This approach should be adopted to correct the current fragmented regulatory environment in Zimbabwe.

Cognisant of the fact that many financial institutions have evolved into financial groups

undertaking a number of activities such as asset management, banking, property management, broking services, etc., a new approach to regulation is required. There are two options that could be followed. The first is to centralize regulation by establishing a Financial Stability Committee comprising the three regulators – the central bank, the Insurance and Pensions Commission and the new Securities Commission – that would be tasked with setting up the modalities for supervising financial groups. A second option would be to adopt the partially integrated approach, as practised in South Africa. In this approach, a Financial Services Board under the Ministry of Finance is established to supervise the pension, insurance and securities industries. The central bank would be responsible for the systemic and prudential regulation of banks, while a self-regulatory banking council conducts business supervision. The advantage of such an approach is that it beneficially combines both official and industry regulation.

5.4.2 Restructuring the financial sector

Restructuring should start with the RBZ returning to its core business on the basis of a well defined legal mandate. The quasi-fiscal activities currently being undertaken by the Reserve Bank should be incorporated into the national fiscal budget. It should not be the business of the Reserve Bank to lend directly to public enterprises. Public enterprises should submit their bids for funding through their relevant ministries which are consolidated by the Ministry of Finance for Parliament to approve. If activities are funded through Treasury, fiscal discipline is directly enforced in the sense that they will impact on the fiscal budget that is monitored by the Parliamentary Committee on Budgets. This would in turn, force public enterprises to raise finance from the market on their own, thus minimizing their reliance on government subsidies.

Furthermore, subsidized direct lending to the private sector by the RBZ through facilities

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such as BACCOSI and ASPEF should be stopped. As explained earlier, these facilities are contributing to money creation in the same manner as the quasi-fiscal activities. The RBZ should desist from ‘mission creep’, and allow commercial banks to conduct their lending to the private sector at market interest rates. The same applies to interventions in the diaspora remittance transfer sector; this is best done by private operators, and in this regard Homelink should be privatized.

Technically, the main banking sector is well managed and the key requirement therefore is one of changing the macroeconomic and monetary policy environment. After all, it is dominated by multinational banks such as Barclays, Standard Chartered Bank, Stanbic and MBICA, whose shareholders maintain tight controls in ‘protecting the franchise’, so systemic risk in the financial system is very limited. This limitation of systemic risk is now under threat from the Indigenization and Empowerment Act and the government will need to repeal this legislation with a view to making it investor-friendly. The Growth Commission Report of the World Bank emphasizes that one way to speed up financial sector development is to attract foreign financial firms to invest in the sector. It observes that the entry of foreign banks brings expertise just as other forms of Foreign Direct Investment (FDI) do, and helps domestic banks to be robust through the transfer of technology and best practices.

There is also a need to restructure and recapitalize weak institutions and state-owned institutions. Agribank is an obvious example of a state bank whose restructuring is long overdue so that it can achieve its mission of being the leading commercial banker for the agricultural sector. Ideally, market-driven consolidations, i.e., mergers and acquisitions, are preferable to state-led consolidations. Agribank would best serve its market as a privatized institution, free from political manipulation.

5.4.3 Liberalizing the financial sector

The banking sector is still dominated by a few multinational banks, so there is scope for both foreign and local entrants in order to stimulate competition and the diversification of services. For this to happen, barriers to entry, including prescriptions on the level of foreign ownership of financial institutions, should be removed.

Liberalization would entail allowing a greater role for market forces through the relaxation of interest-rate controls and reserve requirements, curtailing directed lending, and the removal of exchange controls and freeing the exchange-rate regime. This would enable the sector to be in a better position to support the productive sector as it would allow it to allocate resources efficiently.

The growing mismatch between the maturity of government securities and short-term deposits poses a serious liquidity threat for the banks, especially at a time when confidence in the sector is low and depositors prefer to withdraw their money at every opportunity. This poses problems because the RBZ fixes Treasury Bill rates at negative real values and forces banks to hold them for a minimum of a year. As a result hyperinflation is eroding the assets of banks. In order for banks to meet the withdrawals of depositors and preserve confidence in the sector in the short-term, the central bank should relax reserve requirements and should issue more short-term bills at market rates so that the asset composition of the banks shifts towards short-term, low-risk securities.

Going forward, reform would be required regarding the structure of domestic public debt. Presently, 95 percent of domestic debt is held by the banking sector on an involuntary basis²³. This should be curtailed through binding fiscal rules so that majority of domestic public debt is gradually moved outside the banking system once real interest rates move into positive territory, i.e., with firms, private

²³ RBZ Half Year Monetary Policy Statement, 30 July 2008, p.19.

pension funds, insurance companies and foreign investors, on a **voluntary basis**.

5.4.4 Harmonizing monetary and exchange-rate policy

Monetary policy should be guided by indirect monetary control measures, which include, among others, open market operations that incorporate anticipatory repurchase agreements, and statutory reserve averaging.

Open market operations that incorporate anticipatory repurchase agreements would enable the banking sector to be proactive in managing liquidity and in the market determination of interest rates. Implementation of reserve averaging will ensure that liquidity ratios are determined by prudential requirements to be met over time rather than at any specific moment. The idea is to give more scope to financial institutions to manage their liquidity and eventually reduce reserve requirements.

A new exchange-rate policy should be put in place through liberalizing the exchange regime by unifying the exchange rate and removing restrictions on current international payments and transfers. The IMF (2007) recommends a substantial devaluation of the inter-bank exchange rate (official rate) and the elimination of all multiple exchange rates. In the first instance, balance of payments support needs to be secured to smooth exchange-rate volatility and capital flight, especially during the stabilization period. Normalizing relations with the IMF and World Bank would be crucial for the success of this remedial action. The inter-bank exchange rate could then be depreciated steadily and move towards the parallel market rate. When fiscal and monetary policy regimes have been harmonized (inconsistencies removed) the exchange rate should be allowed to be determined by the market.

A flexible exchange-rate regime, coupled with elimination of RBZ quasi-fiscal activities, would enable a monetary-based anchor as an operational target to reduce inflation and inflation expectations. Such a monetary anchor would enable the RBZ to build foreign currency reserves at appropriate times when the exchange rate is favourable.

5.4.5 Providing an enabling environment for microfinance institutions and small banks to thrive

While many microfinance institutions have developed successfully without official intervention, the government can still play an important role in building an inclusive financial sector. This can be achieved by a number of actions which include the following, among others:

- Bringing together all inclusive finance initiatives under the authority of one ministry or office as recommended by the *Blue Book*;
- Providing an appropriate legislative framework that recognizes the unique features of microfinance and that fosters upscaling to a financial systems approach (i.e., enabling the mobilization of savings in addition to provision of credit);
- Re-visiting the Moneylending and Rates of Interest Act that controls interest rates to be charged with a view to allowing microfinance institutions to set market interest rates commensurate with their cost structure;
- Facilitating ‘smart subsidies’²⁴ to fund the start-up of new institutions to cover capitalization and operating shortfalls; and
- Providing a user-friendly regulatory environment.

²⁴ As observed in the Blue Book, p.104, this is the concept of maximizing social benefits while minimizing distortions and mistargeting. Smart subsidies are rule-bound, time limited, and are usually implemented through the use of performance-based contracts.

Cognizant that the microfinance sector has unique features, the best approach will be to support industry self-regulation in the sector. Associations of the sector (e.g., the Zimbabwe Association of Microfinance Institutions) could be charged with, among other things, the design of appropriate regulations for the sector rather than them being imposed by the RBZ. Ideally, the RBZ should regulate only those microfinance institutions that have grown to the extent of taking deposits.

Cognizant of the many risks involved in extending loans to the small-scale sector, the government should encourage risk-sharing partnerships between commercial banks, NGOs, microfinance institutions and savings and credit cooperative societies. Such partnerships would enable commercial banks to provide retail banking services to the poor. The involvement of NGOs in microcredit activities as part of their development agenda has raised the question of how they should interface with the traditional banking institutions. This becomes imperative considering that these organizations lack adequate liquid resources, economies of scale and expertise to carry out sustainable lending operations. It has been long argued that NGOs that have embraced the provision of microfinance to disadvantaged communities as an add-on to their other development programmes could do so effectively in association with banks within a financial-systems framework. Aryeetey and Nissanke (1998), Schoombbee (2000), and Makina (2006), among others, have proposed risk-sharing relationships involving banks, informal institutions, NGOs and other semi-formal institutions.

In the same vein, there should also be a deliberate policy to promote competition among microfinance institutions. The *Economist* (2007) has reported that where there is healthy competition in microlending, as in Bosnia and Peru, interest rates have tended to fall substantially so that interest-rate caps become unnecessary.

5.4.6 Promoting innovative agricultural financing models

Bearing in mind that the fast track land reform programme has destroyed the collateral traditionally used for financing the agricultural sector, it is recommended that innovative financing models be promoted for small landholders.

By building good infrastructure in the rural areas, it is possible to encourage the setting up of microfinance institutions that service the needs of small landholders. The POSB should be restructured so that it can engage in lending to small landholder farmers. It already has an extensive rural and urban network of branches, so it can easily achieve the required outreach. Agribank is also a ready candidate for restructuring so that it operates on commercial principles with regard to lending to farmers.

An enabling environment should be provided for more private actors to become involved in contract financing for agricultural produce, as is being done by Cottco, Cargill and others; out-grower and input schemes have had a good measure of success to be promoted.

Another possible approach is to request that a portion of donor aid be channelled through multilateral financial institutions for the following purposes:

- Providing set-up costs for microfinance institutions that service small landholders in rural areas.
- Providing seed capital for farmers with a track record who have been dispossessed.
- Covering transaction costs for Agribank, in particular, and any other commercial banks that are willing to lend to small landholders on commercial terms (at market rates of interest to avoid the introduction of distortions).

- Providing concessional lending to medium to large commercial farmers for capital development (e.g., offering grace periods for such loans).

5.4.7 Improving credit-information infrastructure

Financial exclusion is linked to the absence of verifiable credit profiles of borrowers. This critical information constraint needs to be addressed through the establishment of

credit bureaux charged with the effective distribution of high-quality credit information. This will be very important for facilitating the expansion of bank credit to small-scale borrowers beyond the prime clients currently being served by the traditional banking sector. The creation of a credit-information infrastructure should ideally be an industry initiative, as it is a common good for the whole sector that offers financial services.

Chapter 6

Private Sector Development

Economic recovery in Zimbabwe will have to be driven by private sector activity, necessitating far-reaching business- and investment-friendly initiatives and reforms. Ever since the Unilateral Declaration of Independence in 1965, private sector development (PSD) has been hampered by interventionist state policies, especially in the fields of foreign-currency management, investment, pricing and employment. Over the 28 years since Independence, policy towards private enterprise has turned full circle – from a command economy designed to create a Marxist-Socialist state, through a flawed and poorly implemented structural adjustment liberalization programme (ESAP), and back to a dirigiste economy, where state actors have increasingly become obstructionist rather than facilitators.

The brief period of policy reversal (ESAP) during the 1990s soon foundered in the face of intense political pressure, and the degree of government intervention has now reached unparalleled levels, as reflected in the Index of Economic Freedom compiled annually by the Heritage Foundation and the Wall Street Journal. On this index Zimbabwe had a score of 29.8 in 2008 compared with a score of 48.5 in 1995.¹

By 2008 business confidence, which started the Independence era in a fragile state, has also turned full circle and is now arguably at its lowest ebb, reflecting not just the burden of state intervention and controls but also the pervasive uncertainty created by a combination of erratic, volatile and inconsistent policies and persistent threats against private enterprise.

At all levels – large domestic and multinational companies, the formal SME sector and the informal sector – PSD is currently constrained primarily by macroeconomic instability, policies inimical to growth, and a raft of unnecessary and counter-productive administrative red-tape interventions that stifle private initiative. A return to orthodox macroeconomic policies, albeit with a pro-poor bias, designed to reduce inflation, curb the budget deficit, stabilize the exchange rate and restore business confidence, would remove many – though not all – of the constraints on PSD. The restoration of macroeconomic stability is a necessary but not sufficient condition for a vibrant private enterprise sector. It must be accompanied and followed by far-reaching microeconomic and structural reforms of the Investment Climate and Doing Business variety.

6.1 THE PRIVATE SECTOR IN 2008

There is no single measure of the size of the private sector in Zimbabwe. Unpublished National Accounts suggest that the public share of value-added (GDP) declined from 26 percent in 2000 to 20 percent in 2005. Almost all of this contribution to GDP emanated from parastatals in the services sector, especially electricity, water, transport and communications, but also from government-provided services in education, health and public administration. The state's share of agricultural and manufacturing value-added is shown to be tiny, while that for mining is zero.

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¹ The Index of Economic Freedom is a systematic analysis of ten economic freedoms deemed necessary for economies to grow and prosper. The ten freedoms include business, trade, fiscal, labour, monetary, financial and investment freedom as well as freedom from corruption. The index also incorporates a measure of property rights and the size of government. See <<http://www.heritage.org/index/country.cfm?id=Zimbabwe>>.

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In fact, this is a substantial understatement of the size of the public sector because both the majority and minority stakes in mines, industrial companies and the financial sector are treated as part of the private sector in the national accounts. A more realistic measure is that of the RBZ, which estimates the size of the public sector at 40 percent of GDP.

Employment figures are not disaggregated by sector (public or private), and while bank lending figures – a widely used measure of the freedom of the economy and the extent of private sector participation – are available, these too are suspect since, once again, majority state-owned entities are treated as private sector operations and only the narrowly defined public enterprise sector, with 100 percent state-ownership, is treated as public.

Table 6.1 shows that since 2000 the share of bank credit going to the private sector has been only marginally above 50 percent. The definition of private sector credit is unusual because of the abnormal situation in Zimbabwe whereby the central bank has increasingly become a major lender to the private sector. Prior to 2004 the RBZ's private sector loans were negligible, but in 2005 the central bank accounted for 16 percent of total bank lending to the private sector, rising to 20 percent in 2006 before doubling to 43 percent in 2007.

The striking feature of the table is the rapid expansion of RBZ lending to the private sector, thereby supplanting the role of private

banks and reducing the role of the private sector. By 2007 central bank lending to the private sector accounted for no less than one third of total bank credit. Before 2004 the private sector's share of total bank credit averaged 76 percent compared with 24 percent going to the public sector, thereby illustrating the dominance of private sector activity. But since 2004 the public sector share has doubled to 50.6 percent while the private sector's share has fallen below half (49.4 percent).

6.1.1 Economic freedom

A telling yardstick of the significance, role and scope for growth of a country's private sector is the Index of Economic Freedom mentioned above. Figure 6.1 illustrates how Zimbabwe's index score has fallen some 39 percent since it was first ranked in the index in 1995.

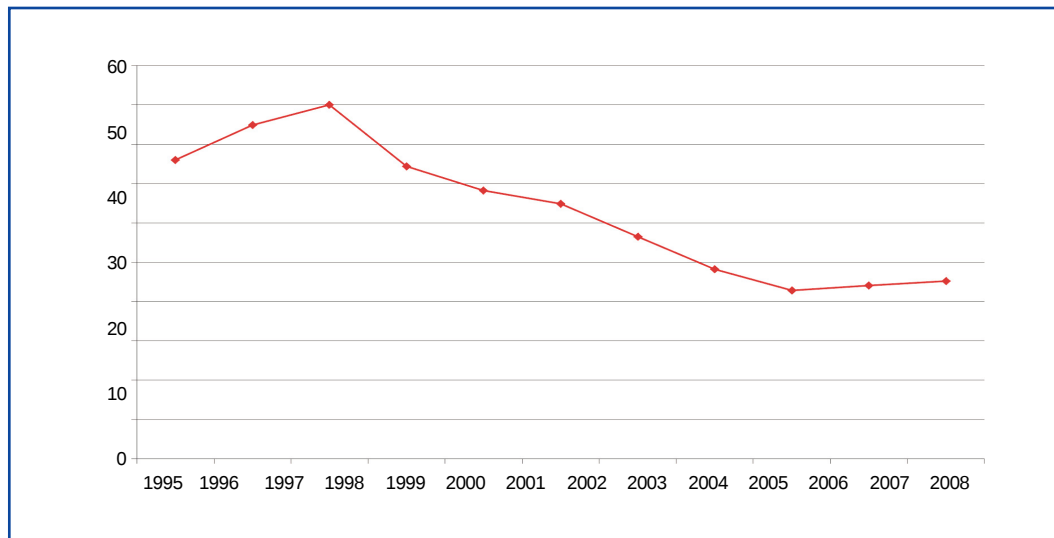
In its first listing in 1995, Zimbabwe's economy was more than 50 percent free in all of the ten indicators used, save one – corruption. By 2008, the economy was less than 30 percent free, and the highest score attained (57 percent) was for trade freedom while for monetary freedom the score was zero. The lower the measure of a country's economic freedom, the greater is the role of the state and the smaller is that of the formal private sector. Similarly, the more economic freedom is restricted, the greater is the role of the informal sector because high levels of economic controls are correlated with rising informality.

Table 6.1: Private sector share of bank credit

	Public (% share)	Private (% share)	(of which) RBZ lending to the private sector (% share)	RBZ lending to private sector as share of total credit (% share)
2000	40	60	–	–
2003	20	80	–	–
2004	31	69	0.6	0.4
2005	55	45	16.0	8.0
2006	41	59	20.0	15.0
2007	55	45	43.0	34.0

Source: Reserve Bank of Zimbabwe: Monthly Bulletin (various issues)

Figure 6.1: Index of economic freedom



Source: Heritage Foundation and the Wall Street Journal (2008)

6.1.2 The informal sector

Although Zimbabwe has a large, rapidly expanding informal sector,² there are no reliable hard data on its size and scope. In 2000, the informal sector was estimated to contribute 59 percent of GNP, making it the largest among 23 African nations for which calculations were made (Schneider, 2002); the average for Africa was estimated at 42 percent. The figure for Zimbabwe looks to be a substantial exaggeration, and a more meaningful estimate is the survey conducted for USAID, which found that in 1998 there were some 860,000 informal sector business establishments employing 1.6 million people, or approximately a quarter of the country's working-age population (McPherson, 1998). Ayyagari *et al.*, (2003) estimated that 15 percent of the total workforce was engaged in formal SME activity and 34 percent in the informal sector.

During the liberalization phase (1991–1996) the number of informal businesses in urban areas was estimated to have risen 30 percent, partly offset by a 14 percent decline in rural informal-sector establishments. Informal-sector urban employment rose 52 percent, while in rural areas there was a

9 percent increase. The largest number of businesses were in the retail trade (44.6 percent), followed by manufacturing (42.4 percent), with textiles (20.1 percent) the main industrial activity. Some three-quarters of the firms operated from home.

Although there are no hard data on recent developments in the sector, both the UN and the Zimbabwe government believe that since 2000 informal-sector growth has accelerated dramatically, reflecting the downturn in formal-sector activity (United Nations, 2005; Zimbabwe, 2006). The contribution of informal-sector business income to total family income doubled between 1995 and 2003 to 15 percent from 7 percent.

Informal-sector enterprises engage in low-technology, low-productivity activities, with very little capital and virtually no access to formal banking channels. Management is poor, workers are underpaid, staff turnover is high and businesses have a very high mortality rate. The majority of those employed are own-account workers (67 percent), with only 14 percent being permanent, paid employees. Most of the rest are seasonal or non-permanent workers.

² The informal sector is defined as the loose aggregation of firms and activities outside the regulatory framework of an economy.

Government policy towards the informal sector has been lukewarm and, in many respects, contradictory. For much of the post-Independence period, when formal sector employment was expanding, albeit too slowly to absorb the annual influx of job-seekers, the informal sector was seen as an inconvenient reality that would disappear with economic modernization. Although policy discouraged informal activity, the informal sector was tolerated rather than harassed by the authorities, until Operation Murambatsvina ('Restore Order') in 2005 when some 32,500 SMEs were demolished and around 700,000 people lost their shelter, sources of livelihood, or both (United Nations, 2005: 32).

There has never been a formal policy framework for the informal sector – the nearest approximation to one being the outdated Small, Micro and Medium Enterprises Policy and Strategic Framework covering the period 2002 to 2007 (Zimbabwe, 2002b). There is a government ministry charged with SME development, whose mandate also covers the informal sector, but its prime focus has been assisting the formal small-scale sector. As a result, policy towards the informal sector is in limbo, with responsibility diffused across no fewer than six government ministries. This absence of political commitment and of a legislative framework for addressing the needs of the informal sector have left it prey to ad hoc, piecemeal measures, devoid of any clear policy goals and strategic thrust.

It is no coincidence that informality in turn, is correlated with economic backwardness – the larger the informal sector, the lower productivity is, and therefore, the lower per capita income and the higher the poverty headcount (Lewis, 2004).³ Although there are no official data to confirm it, it is common cause that Zimbabwe's informal sector, starting from a high base, has grown rapidly as measured GDP has fallen since 1998.

The causation therefore runs from growing state intervention in the economy to declining economic freedom, an expanding informal sector, falling government revenue (because of the near-impossibility of taxing informal activities), declining productivity and lower income per head. As economic freedom shrinks, so obstacles to doing business increase. Indeed, many of the yardsticks used in measuring economic freedom are identical to those used in assessing the ease of doing business in a country.

6.2 CONSTRAINTS TO PRIVATE SECTOR DEVELOPMENT (PSD)

A number of constraints currently hinder the development of the private sector:

- A weak institutional framework for sustaining growth, with a raft of overlapping, conflicting and contradictory government controls covering most aspects of business activity.
- The absence of a conducive business environment for the needs of PSD.
- Poor physical infrastructure – especially power, transport, water and telecommunications.
- An acute and worsening skills shortage, especially in technical fields.
- The absence of an appropriate framework for public–private cooperation in infrastructure, environmental and social activities.
- The absence of effective policies and institutions designed to foster micro, small and medium-scale businesses.
- Weak, underfunded private sector organizations.

³ The poverty headcount is the proportion of the total population estimated to be living in 'extreme poverty', defined as having less than US\$1 a day.

6.2.1 Obstacles to doing business in Zimbabwe

Even when macroeconomic conditions are left out of the calculation, conditions in Zimbabwe are not conducive to private sector development. In the World Bank/IFC Doing Business 2008, Zimbabwe is ranked 152nd out of 178 countries, down from 145th out of 175 countries two years earlier.⁴ Almost all the countries below Zimbabwe in the rankings are low-income African states that are poorer than Zimbabwe, while all Zimbabwe's competitors in the Southern African Development Community (SADC),

with the exceptions of two recent conflict states, Angola and the Democratic Republic of Congo (DRC), have higher rankings (Table 6.2).

Nor can any reassurance be taken from the fact that, Mauritius, Kenya and Tanzania excepted, all the countries in the table slipped down the league table between 2006 and 2008. In other words, in terms of the ease of doing business, the entire region, with a handful of exceptions, is becoming less competitive globally. That Zimbabwe is not only near the bottom of the pile but also regressing is a matter of serious concern.

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Table 6.2: Ease of Doing Business rankings 2006 and 2008: Zimbabwe and comparators

Country	2006 (out of 175)	2008 (out of 178)
Mauritius	32	27
South Africa	28	35
Namibia	39	43
Botswana	44	51
Kenya	80	72
Swaziland	67	95
Zambia	92	116
Uganda	103	118
Lesotho	116	124
Malawi	106	127
Tanzania	150	130
Mozambique	137	134
Zimbabwe	145	152
Angola	155	167
DRC	175	178

Sources: World Bank and the International Financial Corporation: Doing Business Report (2007 and 2008)

Table 6.3: Zimbabwe: Rankings by individual obstacles to doing business

Item	Rank out of 178 countries	Procedures (number)	Time (days)	Cost (% income per head)	Minimum capital (% income per head)
Starting a business	143	10	96	21.3	54.6
Dealing with licences	172	19	952	11,799	n.a.
Registering property	79	4	30	25	n.a.
Enforcing contracts	74	38	410	32	n.a.
Closing a business	151	n.a.	3.3 years	22 (% of estate)	Recovery rate (cents in the dollar) 0.1
Paying taxes	144	52 payments a year	256 hours a year	Total tax rate 53% of profit	n.a.

Source: World Bank/IFC: Doing Business Report (2008)

⁴ <<http://www.doingbusiness.org/Documents/CountryProfiles/ZWE.pdf>>.

Zimbabwe features amongst the worst ten countries out of 178 in several different aspects of Doing Business:

- *Dealing with licences:* Zimbabwe is ranked 172. The cost of licences is the third highest in the world, while the time taken to obtain them, almost three years, is the third longest in the 178 countries surveyed.
- *The cost of retrenching labour:* 446 weeks salary – is the highest in the world.
- *Cost of property registration:* Zimbabwe is third from bottom with a registration cost of 25 percent of the property value.
- *Cross-border trade:* Zimbabwe, ranked 169, is one of the ten countries in the world where it is most difficult to engage in foreign business. Businesses need to obtain thirteen documents to import goods – only three countries require more.
- *Closing a business:* Zimbabwe has the second-lowest recovery rate in the world in respect of claims by creditors, tax authorities and employees.

Table 6.4 shows that Zimbabwe's corporate tax rates are uncompetitive. In the comparator countries only the DRC (229.8 percent) and Angola (53.2 percent) have higher tax takes. The total tax rate measures the amount of taxes and mandatory contributions payable by a business in the second year of operation, expressed as a share of commercial profits. This covers profit and corporate income tax, vehicle and fuel taxes, turnover taxes and social contributions and labour taxes.

Numerous research studies show a close (inverse) correlation between the level of regulation in an economy and economic performance. The World Bank argues that improving a country's Doing Business indicators to the level of the top quartile of countries is associated with a 9 percent

Table 6.4: Total corporate tax take

Country	Percentage of profits
Zambia	16.1
Botswana	17.2
Lesotho	20.8
Mauritius	21.7
Namibia	26.5
Malawi	32.3
Uganda	32.3
Mozambique	34.3
Swaziland	36.6
South Africa	37.1
Tanzania	44.3
Zimbabwe	53.0
Angola	53.2
DRC	229.8*

*A tax take of over 100% arises where non-profit taxes (vehicles, fuel, labour) and profit taxes exceed total profits.

Source: World Bank/IFC, *Doing Business Report* (2008)

reduction in the share of GDP accounted for by informal activity – an important consideration for Zimbabwe, which has a large, growing informal sector.

6.3 POLICY FOR PRIVATE SECTOR DEVELOPMENT

Zimbabwe has never had a strategy for PSD but, in the light of the anomalous and heterodox development path it has followed since UDI in 1965, the country clearly needs one now. Prior to 1980, the private sector was left largely to its own devices, though organizations such as the Industrial Development Corporation were set up to remedy perceived market failure and counter economic sanctions by undertaking investments that private enterprise found unattractive for reasons of cost or risk.

This preoccupation with market failure persisted after 1980 with the proliferation of official interventions designed to close investment and enterprise gaps left by the private sector's shortcomings while also establishing the primacy of the state as part of the overarching strategy of economic

transformation. During the post-Independence period, two strands of PSD stand out:

- Measures to empower indigenous business, culminating in the 2007 Indigenization and Economic Empowerment Act.
- Half-hearted, poorly implemented interventions designed to boost SMEs that seldom graduated beyond pious statements of intent. Thus, the 1997 Industrial Policy Draft (1996 to 2006)⁵ recommended the use of ‘appropriate fiscal measures and other incubation arrangements’ to encourage informal-sector SMEs to ‘graduate into the formal market’. The stated objective was to double estimated formal SME employment to 1 million jobs by 2006. ‘Government sees support for the SMEs as an important vehicle to reverse increasing urban poverty ... and a vehicle for relatively inexpensive job creation in urban areas through self-employment, using inexpensive capital equipment. Measures will be put in place to encourage SMEs to enter export markets.’

This preoccupation with job creation to the detriment of efficiency and competitiveness considerations captures official policy towards SMEs. Their attraction was – and is – their perceived potential for absorbing unemployed school-leavers or dropouts from the formal sector. The policy thrust is that of seeking to help emergent businesses to get ahead through a variety of incentives, inducements and subsidies, thereby insulating SMEs from competitive forces and using taxpayers’ funds to keep failing firms alive.

Yet Klein (2003: 22) found that, globally,

‘...every year around 5 to 20 percent of all firms enter the market and a similar number of older firms go out

of business. Most new firms are small and some 40–60 percent go out of business within five years after entering. Data from developing countries suggest that the average new entrant is a little more productive than firms exiting the market. In most economies, the turnover of firms helps increase productivity.’

The distinguishing features of a competitive economy are the freedom of firms to enter and exit markets. The state’s role should be that of eradicating entry barriers to new business formation while ensuring as level a playing field as possible for SMEs, without keeping inefficient firms alive at the expense of the taxpayer and economic and social efficiency.

As noted above, prior to the Indigenization and Economic Empowerment Act (2007) the nearest approximation to a PSD strategy was the 2002 framework for Small, Micro and Medium Enterprises (Zimbabwe, 2002b), which is more an appendage than a mainstream national policy for the integration of the informal sector into the modern economy. Existing policy has left intact existing biases against SMEs and informal-sector activities, and while there are instances of proactive firms outsourcing or sub-contracting operations to SMEs, these have often withered on the vine over time partly because they were never central to government development policy.

6.3.1 Prerequisites

- Macroeconomic stability.
- Good governance – political accountability, transparent and democratic political processes, legal framework, independence of judiciary, freedom of information, and an administration that aims at efficiency and effectiveness.
- Investment in physical infrastructure.

⁵ Produced by the Ministry of Industry and International Trade (mimeo).

- Investment in soft infrastructure, including human capital, skills development and ICT.
 - Structural reforms designed to improve the efficiency of markets.
 - Investment Climate and Doing Business reforms to eradicate bureaucratic, red-tape obstacles to new business formations
- (b) Capital Account Reforms (see chapter 3 on stabilization);
 - (c) Domestic Financial Reforms (see chapter 5 on financial sector); and
 - (d) Product Market Reforms (see chapter 10 on public sector restructuring, chapter 8 on manufacturing, mining and tourism, and chapter 9 on land policy and agriculture) – including reduced public intervention in agriculture, the phasing out of administered prices and export marketing boards. This category also covers liberalization of the telecommunications and electricity markets.

Taken together these six prerequisites embody the state's core business as a facilitator of PSD – creating the appropriate enabling environment for private enterprise, in part by maintaining macroeconomic stability, in part by direct investment in hard and soft infrastructure, in part through the implementation of structural reforms and the improvement of governance, and in part through private–public partnerships.

6.3.2 Structural reforms

Structural reforms include policy measures designed to remove impediments to the efficient allocation of resources (IMF 2008a). Often these are 'free market' in character, implying reduced state intervention in the economy across a broad front – the elimination of price, wage and interest rate controls, the abolition of state-owned monopolies and liberalization of foreign trade and capital flows.

Structural reforms also have a role to play in tackling market failure, where it exists, such as natural monopolies by introducing effective regulatory mechanisms. The IMF points out that those countries with well-supervised banking systems also score highly in the banking liberalization index, even though such supervision is a departure from the 'laissez faire' market norms.

There are four main categories of structural reforms:

- (a) Trade Reforms (see below) – tariff and current account balance-of-payments liberalization;

IMF data show that real productive and financial sector reforms have helped boost growth in emerging economies, with the most obvious positive results secured as a result of financial sector liberalization, trade liberalization and reduced state intervention in agriculture. Appropriate reforms have achieved improved access to credit, enhanced inflows of foreign direct investment and better decision-making by firms and governments because of improved allocative efficiency (see chapter 11 on how the state does business).

6.3.3 Trade policy

Export performance

Zimbabwe's export performance since 1990, can best be described as lacklustre and has largely been dependent on the outcome of the rainy seasons and global commodity prices. The output trends of the agricultural sector have tended to have pronounced effect on the economy, despite the relatively large contribution of the manufacturing sector to GDP. This is because the latter sector was largely dependent on the former for inputs.

As shown in chapter 2 on the macro-economic situation, the performance of Zimbabwe's foreign trade sector, both in terms of values and volumes reached its peak

at the end of ESAP period (1996-1997) and thereafter started to decline steadily in the post 1997 period. Given the multifaceted factors that explain Zimbabwe's poor export performance as shown above, trade policy objectives should link deeper macro-economic policy reforms to specific upfront reforms that will trigger both quick reactions of the private sector and sustained medium to long-term growth.

Short-term policy initiatives:

While the necessary improvement in the environment will take time to come fully into effect, immediate measures to bolster the competitiveness of Zimbabwean firms will include reversing the ills inherited from the current administration. These will include:

- eliminating all forms of poor economic governance such as uncontrolled expansion of the money supply and endemic fiscal imbalances;
- reducing inflation and stabilizing the exchange rate;
- restoring Zimbabwe's credibility and business confidence through revitalization of the markets which in turn will reallocate resources to the newer and more productive businesses;
- resuscitating the country's transport systems: rail transport system, air transport, and expanding container-handling facilities;
- restoring reliable supplies of coal, electricity, liquid fuels and water;
- ensuring supply of all other inputs to production, including access to foreign currency for imported raw materials and intermediate goods;
- overcoming telecommunications constraints and reinvigorating postal services;
- improving the operation of duty rebate schemes and reviewing the efficiency

of the Value Added Tax to further improve the indirect tax regime for exporters.

Medium to long-term initiatives:

Export commitment: Rebuilding export confidence is essential for Zimbabwe to achieve the levels of imports necessary for self-sustained growth. A post-crisis administration's trade policy should commit to a stable and predictable export-oriented environment, maintaining a competitive exchange rate rather than having specific export incentives. Bureaucratic hurdles to exporting should be eliminated, and all arms of government sensitized to the importance of assisting exporters.

Tariffs and regional trade policy: Such an administration should work with global alliances to shape international economic and trade agreements to the country's advantage. Particular attention should be paid at the regional and continental level to maximizing the gains for Zimbabwe from participation in COMESA and SADC trade and regional economic integration regimes. At the international level, the negotiations with the European Union (for new Economic Partnership Agreements under Cotonou) and at the World Trade Organisation (the Doha Round) should be pursued in tandem with the country's regional partners.

By aligning its production and trading structures, Zimbabwe could, in the medium term take advantage of regional policy instruments which are meant to merge into a single customs territory, ranging from:

- duty-free and quota-free trade amongst the constituent customs territories;
- a common method of valuing tradable goods (common customs valuation systems);
- a common level of protection Common External Tariff (CET), a common trade policy against imports from outside the Customs Union; and

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- a common administrative structure to manage trade policy, customs operations and revenue collection.

Zimbabwe should also review its position vis-à-vis all bilateral partners and the General Systems of Preferences by:

- establishing a business environment in which individual firms can build on their competitive advantage;
- investing in and encouraging far-sighted, sustained public sector building of competitiveness through supportive policies in the area of education, training, human-resource development, industrial relations and taxation;
- adopting a coordinated approach to industrial development and its environmental impact to ensure sustainable development;
- improving infrastructure, and acquiring up-to-date technology and technology support to the industrial and the services sectors;
- encouraging flows of foreign direct investment, particularly in industries and service sectors where the foreign investor brings specialized skills or market access;
- support to beneficiation so as to add value to agricultural and mineral raw materials and promoting the exploitation of value chains and systems to strengthen backward and forward linkages within and between firms and sectors to maximize growth and employment creation; and
- deepening and diversifying the country's industrial base, in part through the concerted development of industrial clusters.

Under a post-crisis government, international competitiveness should be underpinned by a stabilized macroeconomy, providing firms with a predictable environment in which to formulate coherent competitive strategies

and back these up with investments oriented to both the domestic and export markets. In this context, Zimbabwe's industrial and trade policy will be implemented through partnerships with the private sector and support institutions, including NGOs, in the following areas:

- Development of integrated national trade and industrial **clusters** characterized by increased specialization and growing interdependence within and among sectors (industry, agriculture, transport and infrastructure, education, technology, etc.).
- Fostering of linkages between industry and agriculture, thus engendering efficient and diversified production of goods and services for export and the domestic market.
- Attraction of foreign direct investment which creates synergies for the development of the clusters and creates jobs.
- A proactive strategy for structuring finance for export industries.

The fostering of entrepreneurship in the industrial sector and promotion of small and medium-scale manufacturing enterprises would be a central component of a post-crisis administration's industrial policies, including specific small-scale enterprise (SME) measures.

6.3.4 A focus on competitiveness

The Achilles heel of PSD policies in those sub-Saharan economies that are trying to implement them is the absence of a specific commitment to competitiveness. In an increasingly globalized world economy there is no hiding place for inefficient, low-productivity, low-technology firms. Fostering such businesses in the 'national interest' as so-called National Champions, ultimately penalizes the community.

Zimbabwe's recent experience is a reminder that countries cannot devalue or spend their

way to competitiveness, defined as a ‘set of institutions and policies supportive of high rates of economic growth’.⁶ A competitive country improves the living standards of its people through higher productivity.

Depending on resource endowments, geography and path dependence,⁷ policy-makers in emerging markets are confronted by two distinct roads to global competitiveness:

- A low road that implies stagnant, or declining, real wages, static or outdated, technology, technological downgrading, as in the subsidization of small-scale agriculture and SMEs, and a reliance on the exploitation of natural resources and low-wage labour.
- A high-road strategy that depends on a country being able to develop new and more efficient ways of producing and selling goods and services using state-of-the-art technologies, professional management, competitive domestic markets, efficient infrastructure and strong institutions.

When ESAP was launched in 1990, it seemed feasible for Zimbabwe to graduate over time to a high-road strategy, but Zimbabwe’s failure to move upmarket during the past twenty years, and the retrogression in infrastructure, skills, technology and industrial clusters, especially since 1997, has created a new type of path dependence that will make it extremely difficult, over the medium term, to implement a high-road strategy.

There is no such thing as a competitive economy – only an economy comprising competitive firms of all sizes. Competitiveness in business is a two-tiered concept – comparative or national advantage and competitive or strategic firm-level advantage.

Aside from factor endowments, Zimbabwe’s comparative advantage depends on macroeconomic stability, good governance and a sound, well-maintained and efficiently managed physical infrastructure. Unless these three conditions are met, enterprises of all sizes will be unable to become, and remain, competitive.

At the same time, firms do not become competitive purely on the basis of an accommodating macroeconomic environment. Structural reforms are needed to improve the efficiency and flexibility of markets, underpinned by the development of ‘soft’ infrastructure and the eradication of bureaucratic regulations that stifle entrepreneurial drive and initiative.

During the crisis period, Zimbabwe’s competitiveness has declined both absolutely and relatively to the point where today it is ranked third from bottom of 131 countries in the World Economic Forum’s Global Competitiveness Index.⁸ Fortunately, however, it is ranked higher on the Business Competitiveness Index (105th out of 127 countries), meaning that the efficiency and competitiveness of the country’s private sector is constrained by macroeconomic instability and bad governance (World Economic Forum, 2007). This is fortunate because it means that even after the depredations of the last decade, the country still has a solid platform for PSD.

6.3.5 A three dimensional approach

There are three distinct, but interlocking, dimensions to PSD:

- Foreign direct investment.
- SME development through clustering and networking – the promotion of intra-business linkages, including intra-SME linkages and linkages between small and

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⁶ World Economic Forum Global Competitiveness Report, 2007–2008.

⁷ Path dependence means that a country’s future growth path is influenced substantially by past investment in infrastructure, skills and technology.

⁸ See <<http://www.gcr.weforum.org>>.

large business, domestic and foreign, including participation in globalized production networks.

- Rebuilding and recreating the private sector's 'missing middle' (see 6.3.8).

6.3.6 Foreign Direct Investment (FDI)

Even before the onset of deep crisis Zimbabwe had a dismal track record in attracting foreign private capital. Over the 20 years to 2000, there was a net outflow of private capital, funded largely by the inflow of foreign aid, and in 2006 Zimbabwe's inward stock of FDI was estimated at US\$1.4 billion or less than one percent of the total for sub-Saharan Africa (Unctad, 2007). In the light of that statistic, it is remarkable that indigenization should play so prominent a role in government policy.

Even with the resumption of aid inflows, Zimbabwe will remain a capital-scarce economy, especially given the probable need to restructure the financial sector owing to the impact of lasting hyperinflation. In this situation, and given the urgent need to rehabilitate the physical infrastructure, it will be essential to facilitate FDI rather than deter it, which is the inevitable consequence of indigenization in its current legislative form.

Facilitation does not imply however, the use of incentives to attract FDI. Indeed, the poor performance in Zimbabwe (and in many other countries) of explicit FDI incentives, such as Export Processing Zones, tax holidays and preferential access to foreign currency, confirms the view widely held internationally, that such incentives are unlikely to attract foreign investors.

In an increasingly globalized international economy multinational companies make FDI decisions on strategic criteria: market

size and growth, locational attractions in terms of geography, natural-resource endowment, skill levels, the availability of low-wage labour, the ease of doing business, political stability, and a country's suitability as an export platform or as a site for off-shoring⁹. In modern economies the crucial attraction of FDI is that it is the most efficient channel both for the transfer of technology and for entry to global value chains (GVCs), possibly in the form of off-shoring.

Zimbabwe's weak FDI performance since the establishment of the Zimbabwe Investment Centre in 1990 suggests that this should be restructured as a purely promotional entity, removing its authority to license new investors, though this will not be possible should government proceed to implement the indigenization legislation. There is a case for monitoring investments involving the depletion of mineral resources and land ownership by foreigners or those that are a potential source of environmental degradation.

6.3.7 SME development – networking and cluster formation

In contrast, there is a much stronger case for selective official interventions designed to promote SME development. Individually, SMEs cannot compete for market opportunities that require large production capacities, homogeneous standards and regular supply. They are unable to achieve the higher productivity levels that specialization and economies of scale provide. Since SMEs are often the main source of employment, income, skills and consumable products for poor people, the constraints to SME growth and productivity enhancement act as further constraints to poverty reduction in general and thus to the realization of Millennium Development Goal 1 (MDG)¹⁰.

⁹ Off-shoring is the outsourcing of productive processes or links in a firm's value-chain to firms in other countries.

¹⁰ Global value chains arise from the offshoring of manufacturing and service operations to different countries where value can be added more cheaply or efficiently.

There is considerable evidence that SMEs underperform, not because of their size but because of their isolation. The ‘collective efficiency’ generated by clusters or by government-provided business parks and factory shells are likely to both improve SMEs’ access to funding and enhance their survival and growth prospects.

Clusters¹¹ are therefore an ideal mechanism for enhancing SMEs’ performance, reducing new-firm failure rates, and extending both the life cycle and growth potential of SMEs. Isolation is best tackled not by the use of subsidies, protection, tax-breaks or guaranteed preferences for state contracts but by system-wide initiatives aimed at enhancing collective efficiency. Policy should therefore target not the individual firm, but the network of firms in the knowledge that clusters of SMEs overcome the disadvantages of isolation by exploiting scale and scope economies that are external to the individual SME but internal to the cluster. Clusters enable firms to share learning and experience effects while increasing flexibility through inter-firm cooperation and specialization. By facilitating cluster formation, policy enhances collective efficiency through collaboration.

Despite the economic potential for SMEs to grow into the bedrock of the sub-Saharan African economies, they are left as an absorber of displaced labour from the shrinking formal sector. It has been argued elsewhere that ‘the policy of supporting value chains linkages between large-scale firms and SMEs cannot be left to spontaneous outcomes by isolated companies but should be part of expanding the current formal sector activities into the rest of each country’s national economy’ (Ndlela, 2006:101–4).

Unfortunately, from a policy viewpoint, there is general agreement that it is ‘difficult or nearly impossible for public policy intentionally to create clusters where they

do not already exist. Most successful clusters have evolved serendipitously. Although public policies have occasionally been a catalyst to cluster growth, their effects are as likely to be inadvertent as intentional’ (Cortright, 2006: 48).

The best public policy advice for creating clusters is a focus on establishing a business-friendly environment – institutions supportive of knowledge creation, a business culture that supports entrepreneurship, eradicating barriers to new firm formations and ready access to capital (ibid.).

Cortright provides four policy guidelines:

- Cluster development is not a public policy activity. Ultimately it is private sector firms whose conduct and strategies determine whether clusters evolve.
- Clusters cannot be treated as a single or separate activity. There is no case for a ‘Ministry for Clusters’. Cluster policies cut across different government departments and entities, and must involve dialogue with the private sector.
- Governments can – and should – play a supporting role, but cannot create clusters where none exist. It is not a case of governments ‘picking winners’.
- There is no single ‘cluster model’. Clusters develop differently in different regions and industries, though there are lessons that the Zimbabwe tourist industry could learn from the Cairns tourism cluster in Australia (Cortright, 2006: 52)

Cluster development aside, there is a strong pro-poor case for interventions designed to promote SME development. In Zimbabwe this has been confined largely to providing finance, either through the Small Enterprises Development Corporation or more recently, through special preferential interest-rate funds from private sector banks.

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¹¹ Clusters are ‘geographic agglomerations of companies, suppliers, service providers and associated institutions in a particular field linked by complementarities of different types’. (World Economic Forum, 2007)

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In Zimbabwe, as elsewhere, the pay-off from such interventions has been meagre, and there is an ongoing debate as to whether SMEs play a special role in economic development and thereby merit special policy privileges. Though there is no consensus on the issue, some recent macroeconomic evidence casts doubt on the claim that SMEs are 'especially important for growth and poverty reduction' (World Bank, 2005).

For this and other reasons governments and donors are developing new and different programmes designed to support SMEs, shifting the focus from support for individual SMEs to more system-wide approaches that involve:

- addressing market failures that create cost disadvantages for SMEs and restrict their access to markets;
- improving transactional efficiency in financial, product and input markets relevant to SMEs;
- reforming public policies and regulations that discriminate against SMEs or that produce fixed costs that create a competitive disadvantage for small firms; and
- investing in public goods that open up market access and enhance competitiveness (infrastructure, ICT, transport, water and power).

Hallberg (2000) contrasts these modern approaches with the more traditional stance that relied on direct and subsidized provision of financial and non-financial support to SMEs. Targeted interventions and institutions might still be required to improve SMEs' access to finance, business-development services and business-linkage opportunities, but these should be demand-driven, market-oriented and provided by private firms, non-profit intermediaries or private-public partnerships. The recent rapid growth in market-oriented methods of delivering microfinance services to SMEs is a good example of this new policy stance. The role

of the state should be that of reducing barriers to entry and risks associated with lending to SMEs.

Such Doing Business reforms often benefit small businesses more than large-scale firms, who can afford to invest in generators where power is not available and who are better able to access expensive legal or advisory services. This does not mean that SME-promotion programmes should be abandoned but that they should be restructured on the basis of best practice internationally, rather than on uncritical acceptance of the belief that the main constraint to SME development is finance. Furthermore, a striking feature of vibrant economies is the high birth rate (and death rate) of new enterprises. Low-cost finance tends to perpetuate SMEs that should be left to go under.

6.3.8 The missing middle

There is a growing consensus that many sub-Saharan African countries have a disconnect between their large corporate sectors and weak formal and informal enterprises (SMEs). Despite ongoing efforts to strengthen the SME sector, these businesses face a number of stifling financial and regulatory barriers, as a result of which a striking characteristic of African economies is the failure of small firms to graduate to 'middle economy' status, thereby leaving a vacuum in the form of a 'missing middle'.

One of the features of the Zimbabwe economy in the post-ESAP period has been the gradual declustering of the economy – in clothing and textiles, tobacco, food processing, gold mining and tourism – as a result of which many of the small and medium-sized businesses, once the bedrock of commercial agriculture, mining, manufacturing and commerce, no longer exist.

While accepting that SMEs may have the potential to play a critical role in filling the missing middle gap, their capacity to do so depends on the elimination of the many

constraints currently inhibiting the growth of small formal-sector enterprises and the transformation of progressive informal-sector business units into viable formal-sector operators. Yet again, there is a central role for the removal of red-tape obstacles to new business formation, in both the formal and informal sectors.

6.3.9 Business partnership programmes

Long-term survival and profitability requires enterprises to improve their performance continuously to stay ahead of competitors. The successful participation of SMEs in liberalized domestic and global markets depends heavily on their capacity to innovate and thereby to enhance their productivity. In this process, the economic networks and value chains in which a firm operates are key determinants. Multinational corporations are often major drivers of innovation, disseminating technological know-how and facilitating market access. In a globalizing economy it is vital that SMEs become attractive partners, e.g., as subcontractors or suppliers, for large firms. The integration of SMEs into global value chains is one dimension of the kind of global partnerships called for under MDG 8 that can lead to the transfer of know-how, skills and expertise, and contribute to their sustainable development, not only with regard to their economic but also to their environmental and social performance.

6.3.10 Private–public partnerships

There is an unanswerable case for close private–public cooperation and consultation. ‘Discovery’ in business is a two-faceted process. Entrepreneurs need to discover markets, processes and products that are competitive in domestic and foreign markets, while politicians and bureaucrats must discover what is holding industry back and

how public policy can be used to eradicate constraints and bottlenecks.

6.3.11 Global Value Chains (GVC)¹²

Few doubt that participation in GVCs contributes positively to industrial development and poverty reduction but, as with clustering, there is a question mark over the role of public policy and the extent to which it can facilitate GVC entry, becoming a supplier or contractor and thereby participating in the value chain. For Zimbabwe, the major obstacles include geography (its landlocked status and the proximity of a major industrial player, South Africa), the state of the infrastructure, the skills exodus, decades of official ambivalence (if not outright hostility) towards FDI, and a lack of understanding of the realities of global production networks.

The literature – and experience – of public policy in facilitating GVC entry is hardly reassuring. Resource endowment drivers – cheap labour or energy – are major influences, as also are the corporate strategies of buyer-driven value chains. Evidence from all around the world suggests that government investment incentives – tax breaks, labour law derogations, subsidized utilities, guaranteed dividend and profit-repatriation rates, often embodied in Export Processing Zone legislation – have a minimal impact on industrial location, offshoring and outsourcing decisions.

The decision-makers are private sector managers who are more likely to be influenced by Doing Business conditions than special – and potentially temporary – incentives. In any event, in a globalized economy multinational investors, producers and buyers think and act in strategic terms. Attractive tax rates or subsidized electricity tariffs will not influence investment or outsourcing decisions in Zimbabwe if

¹² Global value chains (also global production networks) are ‘interregional networks clustered around one commodity or product, linking households, enterprises and states to one another within the world economy’ (Gereffi and Korzeniewicz, 1994).

corporate headquarters has decided that, for strategic or logistical purposes, South Africa or Kenya is the most appropriate African location.

This, too, is a 'discovery' issue. Over time, firms will discover that there are new and additional value-chain links that they can provide. Arguably there is a role for the state in funding research and development to 'enable' the discovery process. Aside from such interventions the state's main functions should be investing in infrastructure, pushing through enabling environment reforms, and maintaining a constant dialogue with private sector entrepreneurs aimed at identifying bottlenecks and overcoming them.

From a narrowly pro-poor viewpoint entry-level activities within GVCs are desirable because they create new, usually low-income and low-technology, positions. However, as firms move up the value chain into more knowledge- and capital-intensive activities, the direct pro-poor impact is diluted, but to the extent that such GVC progression leads to increased exports and faster growth, per capita incomes rise, thereby reducing poverty.

6.3.12 Infrastructure

It is common knowledge that insufficient, inefficient infrastructure in developing countries remains a major constraint, limiting access to basic services such as a steady electricity supply, clean water, and road and telecommunication networks. In the Zimbabwean case, the infrastructure sectors have faced persistent underinvestment, a situation that now threatens to bring entire supply systems to a halt.

6.3.13 Information services

The rapid advances in information and communication technologies (ICTs) have far-reaching effects on both industrial governance and business systems. Successful institutions and enterprises use ICTs to improve their productivity and to apply new knowledge. In

particular it is essential for the SME sector to have access to adequate information to enhance productivity and facilitate market access. However, in most developing countries, the sector is suffering from market failures in the provision of business information, which is available only from stand-alone institutions, is often slow and cumbersome to access, is limited in scope and not provided for in an integrated manner. Moreover, access to information by itself is not sufficient; SMEs need tailor-made information solutions, i.e., business information services that assess, verify and apply information to a specific business problem.

In Zimbabwe, official controls have made it virtually impossible for SMEs and the informal sector in both urban and rural communities to access information. Under the Postal and Telecommunication Regulatory Authority of Zimbabwe (POTRAZ), stifling regulations are the order of the day, giving excessive market power to a few players in the ICT market.

6.3.14 Corporate strategies and state intervention

For most of the post-Independence period corporate managers have been forced to devote an inordinate amount of management time to meeting government regulations and building relationships with bureaucrats and party officials. This – together with the sheer volatility and unpredictability of government policies towards business, especially in the recent past – has taken its toll on strategy development while creating an 'introverted' managerial class, preoccupied with domestic issues to the point that entrepreneurs have lost sight of the bigger picture.

A striking (contemporary) example is the time and energy that managers are now spending on strategizing for indigenization. Corporate restructuring that makes little sense, either financially or organizationally, is being undertaken purely to meet, or to bypass, legislation requiring that 51 percent of all businesses be owned by indigenous Zimbabweans.

In the absence of the necessary paradigm shift, management time and effort that ought to be devoted to the ‘discovery’ of new markets, new processes, new ideas and new products, will be used to defend corporate earnings and the corporate franchise from political interference, with adverse consequences for industrial growth and poverty reduction. Without doubt, uncertainty over future ownership will deter fresh investment and job creation.

Decades of state intervention in the economy, and especially the experience since 2000, have created a business-culture divide within the private sector. On one side are the successful firms across all sectors of the economy, whose managements are convinced that state intervention is to blame for some, perhaps most, of their problems. Consequently, they want to see a level playing field in post-crisis Zimbabwe rather than one littered with carrot-and-stick interventions of the kind that are now commonplace.

At the other extreme are those, mostly smaller and newer, businesses that have grown up in a dependency-culture environment and whose success or survival depends on state assistance of one kind or another. For them, problem-solving involves seeking official assistance – cheap finance, fertilizer, seed, preferential access to foreign exchange and government or parastatal contracts. The consequence has been the promotion of rent-seeking rather than entrepreneurialism, and the emergence of a dependency culture within the private sector.

From a political-economy – and also from an inclusive-growth and empowerment viewpoint – bridging this divide will be a difficult task, not least because the paradigm or culture shift on which much of the above discussion is predicated would shatter the dependency culture that is becoming increasingly ingrained in Zimbabwe business.

Chapter 7

Labour Markets, Human Capital and the Diaspora

7.1 INTRODUCTION

In analysing developments in labour markets, human capital and the diaspora in Zimbabwe, we will use the three periods outlined in chapter 2 – the control regime period (1980–1990), the liberalization (ESAP) period (1991–1996) and the deepening crisis period (1997–2008).

This chapter first traces the nexus between growth, employment and poverty, outlining the role of the labour market in poverty reduction/eradication. While growth is a necessary condition for poverty reduction and its eventual eradication, it is not a sufficient one. The quality of growth, as measured by its employment intensity, is as important as its quantum in reducing poverty.

Zimbabwe's past performance demonstrates that employment growth follows output growth, reflecting the fact that the demand for labour is derived from that of output. During periods of output growth, employment grows at a slower pace and likewise, when output growth declines, employment growth has a lagged response, reflecting its quasi-fixed attribute. The employment intensity of growth, as measured by employment elasticities of output, suggests that the labour absorptive capacity of the economy has declined over time, in line with global trends.

While the elasticities were positive from 1991 to 1999, they became negative between 1999 and 2004 as the crisis deepened. As a result of the deepening crisis, out-migration intensified, resulting in a significant brain drain. Whereas Zimbabwe had made

considerable progress in human capital formation since independence, as the crisis deepened, human capital formation has failed to bridge the gap created by out-migration, creating serious human capital deficits in the economy. This has exacerbated a situation already made difficult by the HIV and AIDS pandemic, which is disproportionately affecting the productive age group.

The constraints to growth and recovery in the labour markets, human capital and the diaspora include the multiplicity of institutions, policy inadequacies in addressing the needs of the economy and, in particular, sustained employment creation and human capital formation, and an inability to stem the brain drain.

7.2 THE LABOUR MARKET AND POVERTY REDUCTION

Poverty reduction, and its eventual eradication, has assumed prominence in the new millennium; in fact, the first Millennium Development Goal targets halving poverty by 2015.¹ In this framework, the labour market, and decent employment in particular, are expected to play an intermediating role (the nexus) between growth and poverty reduction. In this regard, a development strategy that fully employs a country's human resources and raises the returns to labour (the wage) is considered a powerful tool for poverty reduction/eradication (Islam, 2003).

The link between growth, employment and poverty reduction is not automatic. Growth on its own is not sufficient to generate

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¹ Zimbabwe and UNDP, 2004: *Zimbabwe Millennium Development Goals: 2004 Progress Report*.

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significant improvements in employment and poverty reduction. In the context of sustainable human development,² growth is seen as a means, rather than an end in itself. Such an approach acknowledges that a country may achieve high levels of growth, but that does not necessarily translate into employment growth and poverty reduction. Growth is therefore seen as a necessary but insufficient condition for employment growth and poverty reduction. What matters is not just the level or quantum of growth, but its quality, implying that the type of growth matters as much as its level.

The importance of employment in poverty reduction lies in the fact that, quite often, the abundant resource that the poor possess is their labour, which they can use to earn a livelihood. The extent to which the poor can use their labour determines their incomes. Complementing their labour is the return to it, which itself is dependent on the assets they possess. If therefore, the quantity of employment and the returns to labour are low, poverty is often the outcome. Underemployment of labour and low returns to it are proximate causes of poverty (Heintz, 2006; Osmani, 2005). Thus, for growth to rapidly reduce poverty levels, the forces behind underemployment and low returns to labour should be addressed, in which case three factors – the growth factor, the elasticity factor and the integrability factor – become critical.

The growth factor relates to the rate at which the production potential of an economy is enhanced, while the elasticity factor indicates the extent to which the upward shift in the production function raises employment potential (both quantity and quality). The integrability factor refers to the extent to which the poor are able to integrate into economic processes such that, as growth and employment expand, they can take advantage of the opportunities that arise to improve the quality and quantity of their

employment. For any given expansion in growth, the employment response depends on three key factors: the sectoral composition of output, choice of technique and the terms of trade (relative price of output and input). The growth process associated with a bigger shift in employment – the one that is more employment elastic – is most helpful to the poor. The growth elasticity of employment is therefore an important intermediary in shaping the extent to which growth translates into poverty reduction. Note that a high elasticity of employment does not necessarily entail higher incomes for the poor: it simply expands the opportunities. It is the attributes of the poor (their capabilities) that will enable them to integrate fully into an expanding economy, determining the extent to which the poor benefit (the integrability factor).

Broadly stated, pro-poor growth is growth that benefits the poor and provides them with opportunities to improve their economic situation (Kakwani *et al.*, 2004). Note that there are different variants of pro-poor growth. The most applicable definition refers to relative or absolute pro-poor growth. The relative concept applies when growth benefits the poor proportionally more than the non-poor. It therefore implies a relative reduction in inequality. The absolute concept is such that the poor receive the absolute benefits of growth equal to, or more than the absolute benefits received by the non-poor. In this context, economic growth is usually associated with a decline in absolute inequality (Kakwani *et al.*, 2004; International Poverty Centre, 2007).

However, employment is not the only means of translating growth into poverty reduction. Social provisioning, especially with respect to basic services that encompass education, health, and income grants, among others, is critical. Hence a viable employment-centred strategy for development should also integrate social policies (Heintz, 2006).

² The UNDP defines human development as 'a process of expanding people's choices by enabling them to enjoy long, healthy and creative lives'.

7.3 OVERVIEW OF PAST PERFORMANCE IN ZIMBABWE

7.3.1 Growth, employment and poverty reduction: An analysis of the performance

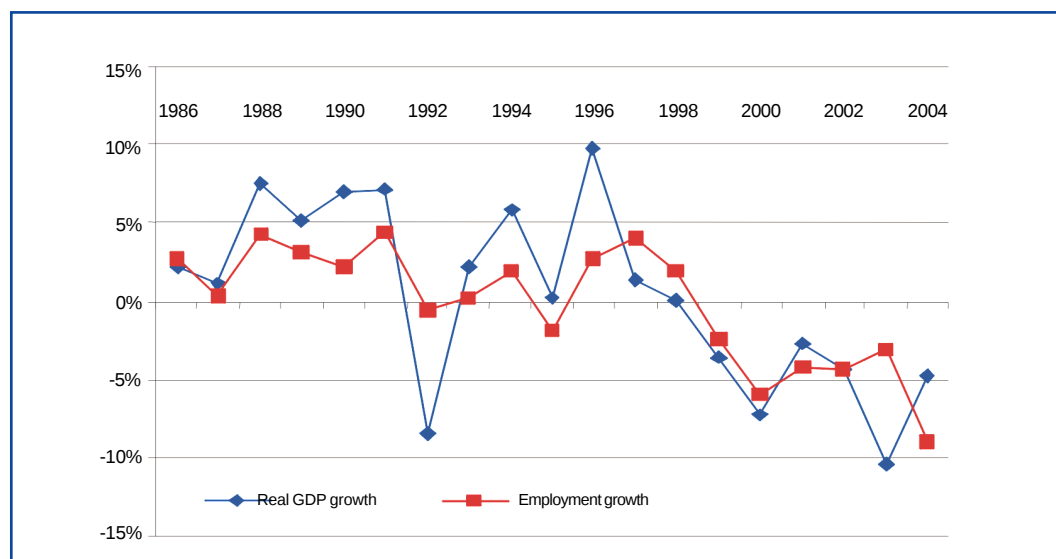
The relationship between growth and employment

It has been shown that the extent to which growth reduces poverty depends on the elasticity factor and the integrability factor. It is therefore necessary to assess the extent to which growth has been employment-intensive (the output elasticity of employment). Figure 7.1 illustrates the movement of real GDP and employment growth rates between 1986 and 2004.

Real GDP growth, which averaged 4 percent annually from 1985 to 1990, declined to 0.8 percent during the reform period of 1990–96 and to –3.7 percent from 1997 to 2004 in the crisis period. Likewise, employment growth decelerated from an annual average rate of 2.4 percent from 1985 to 1990 to 1.2 percent during the reform period and –2.8 percent during the crisis period.

Clearly, therefore, even before the onset of the crisis, growth had already declined to a very low level. As expected, the period of negative economic growth (1999–2004) is associated with negative employment growth. Significantly, the rates of growth of employment for this period are well below the annual average intercensal population growth of 3.9 percent from 1982 to 1992 and of 1.2 percent from 1992 to 2002. The decline in the annual average rate of growth of the population is due mainly to out-migration and the AIDS pandemic. Whereas 14 percent of the population (20 percent of the labour force) were employed in the formal sector in 1980, by 2004, only 10 percent of the population (13 percent of the labour force) were so employed.³ On the basis of an estimated 700,000 employees in the formal sector in 2007, this implies that only 6 percent of the population is currently employed in the formal sector. Ever since the early 1960s, the highest proportion of the population employed in the formal sector reached 17 percent in 1975. As shown in chapter 6 on private sector development, it is the informal economy that has borne the burden of employment creation.

Figure 7.1: Growth in real GDP and employment, 1986–2004



Source: Calculated from CSO data

³ The labour force or the economically active population refers to those aged 15 years and above who are available for the production of goods and services for cash or in kind. It comprises the employed and the unemployed.

Figure 7.1 shows that the rate of employment growth is lower than that of the overall growth rate when the economy is expanding. In addition, the rate of employment growth declines more slowly when the economy is shrinking.

The employment intensity of growth, as measured by the employment elasticity of growth, is therefore a critical indicator of the quality of growth. Table 7.1 shows the employment elasticities and GDP growth between 1991 and 2003.⁴

Generally, the employment elasticities of growth have declined markedly during the period under review, implying that the relationship between growth and employment generation has weakened over time. In other words the additional employment created at a given level of economic growth has fallen over time. Even studies that

calculated such elasticities for earlier periods suggest that the elasticities for Zimbabwe's manufacturing sector declined from 0.65 for the period 1963–79 to 0.06 over the period 1980–96 (see Heintz, 2006).

The level of employment in the formal sector has declined over time, and has been worsened by the current economic crisis, in line with global trends. Those groups that had experienced a higher level of employment intensity of growth (youths and males) in earlier periods appear to be the greatest losers during the downturn (1999–2003).

The trend in the elasticities of employment for Zimbabwe differs from that for the rest of the world and sub-Saharan Africa (Table 7.2); the elasticities of the latter two initially increased between 1995 and 1999 before declining. The decline experienced by

Table 7.1: Employment elasticities and GDP growth

	1991–1995	1995–1999	1999–2003
Total	1.84	0.26	–0.21
Youth	4.45	0.42	–0.68
Female	1.67	0.26	–0.13
Male	1.99	0.27	–0.28
Annual GDP Growth	0.10	3.70	–6.30

Source: Adapted from Kapsos (2005: 41, Table A2.9)

Table 7.2: Employment elasticities and annual average GDP growth

	1991–1995	1995–1999	1999–2003
Employment elasticity			
Zimbabwe	1.84	0.26	–0.21
World	0.34	0.38	0.30
Sub-Saharan Africa	0.73	0.82	0.53
GDP growth (%)			
Zimbabwe	0.10	3.70	–6.30
World	2.10	3.60	3.50
Sub-Saharan Africa	1.10	3.20	3.20

Source: Compiled from Kapsos (2005, various tables)

⁴ The International Labour Office (ILO) is now computing detailed employment elasticities of growth for various countries across the five continents which are published as part of the Key Labour Market Indicators. However, its elasticities for Zimbabwe for the period 1991–95 are questionable.

Zimbabwe, which had the highest employment intensity of growth between 1991 and 1995, is steep. Given that the labour regime was significantly deregulated after the early 1990s, rigidities in the labour market may not be responsible for this decline, especially during the latter period. As the 2007 Confederation of Zimbabwe Industries (CZI) Manufacturing Sector Survey found, the main constraint to job creation had to do with low levels of production, with labour market constraints hardly featuring at all (Table 7.3). The survey (2007: 30) established that ‘while in theory, the existence of distortions in the labour market abound, the lack of enforcement appears to have made these ineffective’.

Table 7.3 shows the major constraints to employment creation in the manufacturing sector in 2005 and 2006; the results suggest, as expected, that the demand for labour is derived mainly from the production process. Note that labour market rigidity is not an issue, with no firm citing National Employment Council (NEC) compliance (labour standards) as a constraint. Minimum wages and security regulations act as rigidities when foisted arbitrarily by some external force or institution. Where these are negotiated, as is the case in Zimbabwe, they do not cause unemployment or inflation. The onerous employment-security regulations that undermined employment creation in the 1980s were deregulated at the beginning of the ESAP period.

Table 7.3: Major constraints to employment in the manufacturing sector

Major constraints	2006	2005
Raw-material shortage	55	65
Low production	64	41
Foreign currency	18	29
NEC compliance	0	12

Source: CZI Manufacturing Sector Survey (2007: 30)

Average real earnings

Since pro-poor growth requires both an improvement in employment levels and the returns to labour, it is necessary to trace the trends in real earnings. In virtually all sectors of the economy, average real earnings have collapsed because wage increases have failed to match inflation. The average real earnings index for the whole economy peaked at 120 in 1982 before collapsing to 10 by 2004.⁵ Wage increases have therefore failed to compensate for increases in inflation, especially during the period of crisis. Such a marked decline in real earnings, coupled with the decline in employment levels, exacerbates poverty.

The 2007 CZI Manufacturing Sector Survey observes that the collapse in real wages is having adverse effects on the economy, arguing that ‘in addition to a shrinking economy, this has had a multiplier effect of seriously depleting the country’s disposable incomes. The erosion of disposable income as workers get poorer is shrinking demand for products as disposable incomes wane and hence reduces business viability’ (2007: 58).

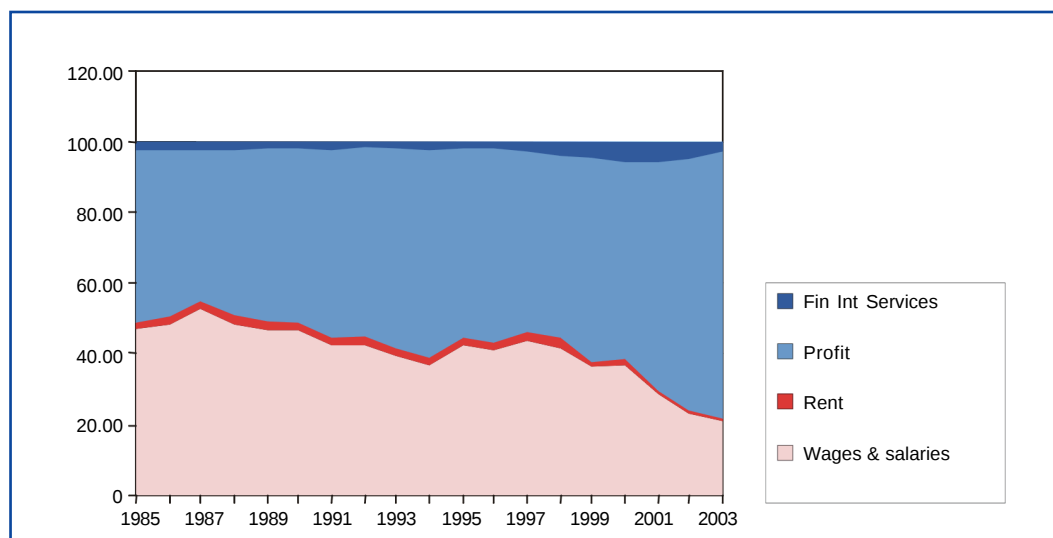
Functional distribution of income and income differentials

Calculations based on original data suggest that the wages’ and salaries’ share of Gross Domestic Income (GDI) declined from an average of 49 percent during the pre-ESAP period to 41.5 percent during the ESAP period, and to 29.9 percent during the crisis period of 1997–2003 (Figure 7.2). Profits, on the other hand, increased in the same periods from an average of 50 percent, to 58.4 percent, and to 73 percent. The increased share of profits had not been accompanied by increased investment because the environment was characterized by macroeconomic instability. In fact, investment is insignificant in gross terms. Such a development undermines the attain-

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EARNINGS INDEX
FOR THE WHOLE
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AT 120 IN 1982
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BY 2004

⁵ See chapter 2 on the macroeconomic situation.

Figure 7.2: Gross domestic income at current prices by factor (%)



Source: Derived from CSO National Accounts, 1985–2003

ment of sound industrial relations, which are critical for increased productivity. In this regard, the tripartite partners, government, business and labour have been trying to redress this development through negotiating a win-win social contract.

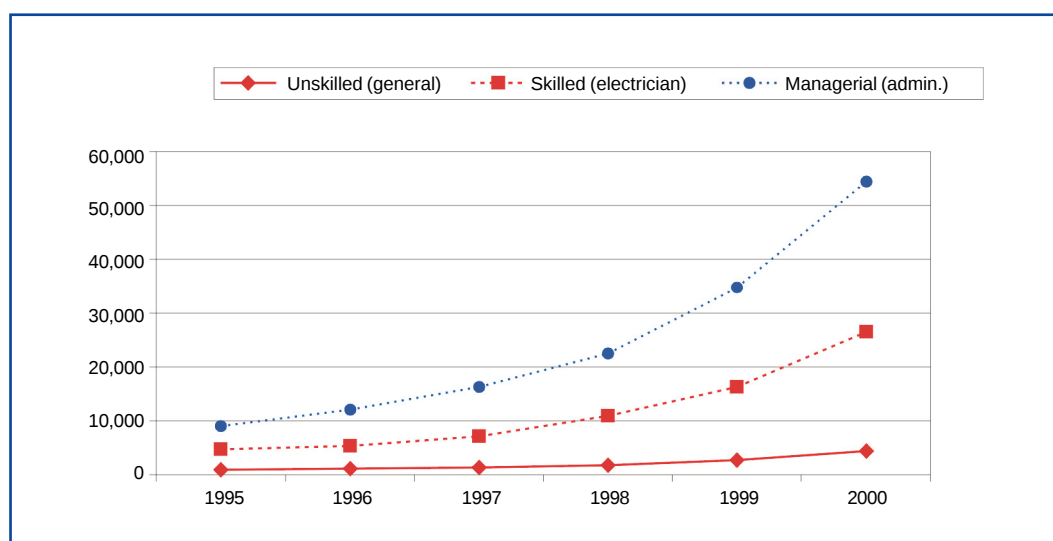
Figure 7.3 shows income differentials for the unskilled, skilled and managerial grades during the period 1995–2000. It illustrates that unskilled workers have borne the brunt

of the current economic crisis. This undermines a key principle in a sustainable-earnings structure – the need for equity and stability in the differentials, especially where these are based on a job-evaluation exercise.

Unemployment

Unemployment is measured using both its broad (passive) and strict (active) dimensions.⁶ According to the broad

Figure 7.3: Differential earnings for different occupations



Source: PriceWaterhouseCoopers, 2001

⁶ The use of the broader definition started with the 2004 labour force survey following recommendations of the 1998 User-Producer of Statistics symposium attended by stakeholders. CSO, 2004 Labour Force Survey, March 2006; CSO, Report on the Proceedings of the User-Producer of Statistics Symposium, Kadoma Hotel and Conference Centre, 8–12 November 2004, February 2005.

definition, unemployment ‘refers to the population age 15 years old and above which during the seven day reference period, did not work and had no job or business to go back to but who were available for work’.⁷ The strict definition requires that those without a job and are available for work actively look for work. In developing countries such as Zimbabwe, the broad definition is more appropriate because of the limited methods of job search available, especially in the rural areas, and the reality that, with limited job opportunities, most job-seekers are already discouraged from looking for work. Using the data for the seven days before the survey, the rate of unemployment using the strict definition was 4.4 percent (4.3 percent for males and 4.5 for females), while using the broad measure, the levels were 9.3 percent (12 percent for females and 6.8 percent for males). The levels are too low and do not reflect reality.

The Poverty Assessment Study Survey (PASS) II estimated unemployment using an alternative measurement to capture the effects of structural changes in the economy on unemployment, and to deal with the problem of underestimation arising from use of the conventional measure (Zimbabwe, 2006). Structural unemployment includes those who were usually unemployed, those who were involuntarily in the informal sector, the very poor and poor communal and resettlement farmers, the very poor and poor unpaid family workers, the very poor and poor in the informal sector, and the very poor and poor engaged in public works. Using this alternative definition, the rate of structural unemployment in Zimbabwe was 63 percent in 2003. Structural unemployment was higher for females (70 percent) than for males (56 percent) because of the inclusion of the very poor and poor in agriculture and the informal economy, who are largely women. Rural areas had a higher structural unemployment rate (62 percent) than urban areas (35 percent).

The Impact of HIV and AIDS

There has been a belated acceptance that HIV and AIDS is a workplace challenge. It poses serious threats to workers’ rights since people living with HIV and AIDS are subject to stigmatization, discrimination and hostility in their communities and at work. HIV and AIDS has a significant impact on the composition of the labour force in terms of age, skills and experience, with the productive age group 15–49 years the most affected. Losses of human capital due to HIV and AIDS are disproportionately higher among skilled, professional and managerial workers. The pandemic has profound adverse impacts on the economy, workforce, businesses and the infected and affected individuals and their families.

HIV and AIDS has manifested itself in the workplace through discrimination in employment, social exclusion of affected persons, distortions in terms of gender inequality, increased number of orphans often resulting in increased child labour, disrupted performance of small enterprises and the informal economy. It has also manifested itself through low productivity, depleted human capital, challenged social security systems and undermined occupational safety and health. The impact of HIV and AIDS at the enterprise level can be broken down into three categories, namely, direct, indirect and systemic costs. Direct costs, which are easier to quantify, arise from medical care and insurance costs, pension and retirement costs, recruitment and retraining costs, and costs of HIV and AIDS programmes. Indirect costs include reduced productivity, morbidity, and absenteeism due to illness and bereavements. The systemic costs relate to loss of skills, loss of tacit knowledge, reduced morale and breakdown of workplace discipline. HIV and AIDS is exacerbated by poverty and vice versa, making it a challenge to the fundamental principles and rights at work, and more importantly, the decent work agenda (see SAfAIDS and HIVOS, 2007).

⁷ Central Statistical Office, ‘2004 Labour Force Survey’, March 2006, p. 27.

Even though government promulgated Statutory Instrument 202 of 1998, 'Zimbabwe Labour Relations (HIV and AIDS) Regulations', the response at the workplace was slow, especially given that in the early years it was almost exclusively seen as a medical problem. For instance, the public sector policy on HIV and AIDS was only launched in 2005 in response to the severity of the pandemic on the provision of public services. It had emerged that between 1995 and 2002, the largest number of public employees who took sick leave of up to 90 days was in the 30–49 age group, including professional and technical grades, and that more female than male staff members had left the service on medical grounds. Terminations of service on medical grounds had increased from 0.05 percent in 1995, peaking at 3.23 percent in 2001 (see Public Service Commission, 2007). As the report concedes, before 2005, the priority on HIV and AIDS in government ministries was perceived to be low as most managers did not consider HIV and AIDS programmes as their core business, while others felt they were not equipped to take a leading role in HIV and AIDS issues.

7.3.2 Developments in human capital formation, 1980–2007

Human capital is defined as 'the stock of productive skills and technical knowledge embodied in labour'. This refers therefore to the acquired and useful abilities of people that prepare them for the world of work. Investment in human capital is mainly through education and training, thereby enhancing the integrability factor.

Primary, secondary and technical

Human capital formation during the colonial era was skewed in favour of whites. It has been noted that 25 percent of black children did not start school, while over 60 percent did not complete full primary education, and only 4 percent completed four years of secondary education (Riddell, 1979). Secondary education was divided into two

systems, F1 and F2, the latter offering a practical curriculum and the former a more academic curriculum. This dual approach was perceived to have a racial tone in that it was offered only to blacks and therefore seen to be inferior. As a result, F2 schools were phased out at independence and converted into conventional schools in 1981, and an opportunity was lost to develop technical and vocational education using the framework already in place.

A central component in skills-formation was the apprenticeship-training system which was established in 1934. According to the National Manpower Survey (Zimbabwe, 1981a), this skills-training programme was not only racially biased but was designed to ensure that it produced only a few graduates. Of the 5,103 apprentices in February 1981, 56 percent were Whites, 26 percent were Africans, 7 percent were Coloureds and 1 percent were Asians. Whites dominated the critical technical areas such that they represented 89 percent of apprentices in the aircraft field, 84 percent in electricity, and 68 percent in engineering. Intakes of apprentices averaged only 1,000 per annum in the pre-independence period. Furthermore, the system relied on immigration to cater for skills requirements, which undermined the development of comprehensive apprenticeship training and technical education. Consequently, at independence in 1980, blacks represented only 36 percent of all professional, technical and related staff, and only 24 percent of managerial and administrative personnel.

The post-independence government sought to reverse the racial imbalances in education provision and skill formation by adopting a policy of universal primary education. Primary school enrolment became almost universal at 97 percent.

Tertiary

To address the racial imbalances in Technical Vocational Education and Training (TVET), government built five additional

technical colleges between 1980 and 1990, which were later upgraded to polytechnics in 2001. The apprenticeship system was revamped to expand its catchment, and a trade-testing system was introduced in 1981 to classify workers into Skilled Worker classes 1 to 4, Class 1 being the highest. The rationalization of TVET in Zimbabwe was done under the comprehensive policy document of 1990 ‘Rationalization of Technical and Vocational Education in Zimbabwe’.⁸

In 2004, it became possible to upgrade TVET qualifications to graduate and post-graduate levels. A Bill establishing the Zimbabwe Qualifications Authority (ZIMQA) was drafted in 2005 to feed into the requirements of the SADC 1997 Protocol on Education and Training, which envisages the establishment of a Regional Qualifications Framework (Zimbabwe, 2006a).

7.4 THE DIASPORA

7.4.1 The size and nature of the diaspora

Since independence in 1980, emigration has occurred in two main waves. The first, during the early 1980s, involved mainly white Zimbabweans. It was reported that from 1980 to 1983 the country recorded a loss of 19,300 skilled and professional workers, mostly to South Africa, Australia and the UK. This migration wave was somewhat mitigated by returning Zimbabweans with high qualifications but limited experience, who filled most of the vacated posts (Zinyama, 2002).

The second wave began soon after the disputed general elections in 2000 and the commencement of the fast track land reform programme. The destinations have varied from nearby southern African countries to

as far away as New Zealand, Australia, the United Kingdom and the USA. What began as a trickle has turned into an exodus that has bled the country of a reservoir of skills that neighbouring countries and those abroad have welcomed.

From survey data it is estimated that the population of Zimbabweans resident outside the country is at least over two million. South Africa has the largest number, slightly over one million as at the end of 2007. Table 4 shows an extrapolated progression since the last census of 2001.

Table 7.4: Zimbabwe migrant population in South Africa

Year	Estimated migrant population (year-end)
2001	131,886*
2002	175,715
2003	255,604
2004	375,935
2005	522,364
2006	763,425
2007	1,022,965

* Actual, per Statistics SA census

Source: Makina (2007)

According to the International Organization for Migration, the UK has the second-largest population of Zimbabweans living abroad, with an estimated 200,000–500,000, while Botswana is estimated to have between 100,000 and 300,000. Other Zimbabweans are scattered throughout the USA, Canada, Australia, New Zealand as well as other neighbouring countries.

7.4.2 Driving forces of contemporary migration

Economic decline and political reasons are seen as the main supply-push factors driving migration of both skilled and unskilled

⁸ Ministry of Higher and Tertiary Education (1990), *Rationalisation of Vocational and Technical Education in Zimbabwe*, Harare.

THE IMPACT OF
THE BRAIN DRAIN
ON PUBLIC
SERVICE DELIVERY
HAS BEEN
DEVASTATING

workers (Chetsanga and Muchenje, 2003; Bloch, 2005; Makina, 2007). By and large, Zimbabweans living abroad have now acquired the critical feature of a traditionally defined diaspora, i.e., a homogeneous people with a common sense of displacement, both voluntary and involuntary, with a hope of returning home one day when the conditions that drove them into migration are removed. At least three surveys indicate that two-thirds of Zimbabwean migrants intend to return when the political and economic situation improves (Bloch, 2005; Chetsanga and Muchenje, 2003; Makina, 2007). There is clearly therefore scope for involving the diaspora in economic recovery processes in their home country.

7.4.3 The impact of the brain drain

Emigration survey data show that over 80 percent of people migrating to South Africa and the UK are between 21 to 40 years of age (Bloch, 2005; Makina, 2007). Information from the UK Home Office Skills Audit on pre-migration activities of

respondent migrants provides further evidence on the high skills base of those leaving Zimbabwe for the UK, showing that a very large proportion had been in management and professional jobs prior to leaving.⁹

The impact of the brain drain on public service delivery has been devastating. For example, in the case of health care, it is estimated that more than 80 percent of the doctors, nurses, pharmacists, radiologists and therapists who trained since 1980 have left. By 2003, the health sector had lost over 2,100 medical doctors and 1,950 State Certified Nurses, mostly to South Africa, Botswana, Namibia, the UK and Australia (Chikanda, 2005).¹⁰ Table 5 below highlights the extent of the brain drain by 2006.

The major medical training institution, the University of Zimbabwe College of Health Sciences, has also suffered from the brain drain. By March 2007, the institution had an overall vacancy rate of 60 percent. Table 7.6 shows the overall dire situation in the medical college.

Table 7.5: Staff situation at the major referral hospitals as at 31 January 2006, selected posts (Harare, Parirenyatwa, Chitungwiza, Mpilo and United Bulawayo Hospitals)¹¹

Designation	Establishment	In post	Vacancies	Vacancy rate (%)
Doctors/ Specialist Heads of Dept	22	1	21	95%
G.M.O.	106	27	79	75%
Chief Government Pathologist	3	1	2	67%
Junior Registrar	62	0	62	100%
Chief Medical Laboratory Scientist	6	2	4	67%
Senior/Principal Medical Laboratory Scientist	4	2	2	50%
State Certified Medical Laboratory Technician	171	99	72	42%
State Certified Medical Laboratory Technician	50	3	47	94%
Registered General Nurse/Sister	2,852	1,936	916	32%
State Certified Nurse	392	284	122	88%

⁹ Rachel Kirk, 'Skills Audit of Refugees' Home Office Online Report 37/04, <<http://www.homeoffice.gov.uk/rds/pdfs04/rdsolr3704.pdf>>.

¹⁰ 'A Review of National Strategies to Manage Mobility and Migration of Zimbabwean Skilled Professionals: The Health Sector Experiences'. A presentation by Dr O.L. Mbengeranwa, Chairman of the Health Service Board at the 'Strengthening National Capacities for Addressing Migration and Development in Zimbabwe' workshop, Troutbeck Inn, Nyanga, 18–19 September 2006.

¹¹ 'A Review of National Strategies to Manage Mobility and Migration of Zimbabwean Skilled Professionals: The Health Sector Experiences', A presentation by Dr O.L. Mbengeranwa, Chairman of the Health Service Board at the 'Strengthening National Capacities for Addressing Migration and Development in Zimbabwe' workshop, Troutbeck Inn, Nyanga, 18–19 September 2006.

Table 7.6: Staff situation at the University of Zimbabwe College of Health Sciences: March 2007

Designation	Establishment	In post	Vacancies rate (%)	Vacancy
1 Anaesthesia & Critical Care Medicine	16	2	14	88%
2 Anatomy	26	1	25	96%
3 Chemical Pathology	11	7	4	36%
4 Clinical Pharmacology	11	4	7	64%
5 Community Medicine	17	8	9	53%
6 Dentistry	12	6	6	50%
7 Haematology	7	0	7	100%
8 Histopathology	8	1	7	88%
9 Immunology	8	4	4	50%
10 Institute of Continuing Health Education	2	1	1	50%
11 Medical Laboratory Sciences	9	9	0	0%
12 Medical Microbiology	11	7	4	36%
13 Medicine	26	10	16	62%
14 Nursing Science	10	9	1	10%
15 Obstetrics and Gynaecology	26	14	12	46%
16 Paediatrics and Child Health	26	10	16	62%
17 Pharmacy	11	8	3	27%
18 Physiology	21	1	20	95%
19 Psychiatry	16	7	9	56%
20 Rehabilitation	10	7	3	30%
21 Surgery & Radiology	30	10	20	67%
Total	314	126	188	60%

Source: The Dean, University of Zimbabwe – College of Health Sciences

The impact of this huge brain drain which has affected all sectors is that it will act as a constraint on the speed of Zimbabwe's recovery given that a high level of human capital is one of the key ingredients for domestic development and for attracting FDI. Miyamoto (2003) shows that enhanced human resources development increases FDI by making the investment climate of a country attractive to foreign investors. On the other hand, FDI contributes to human resource development because multinational enterprises can be active providers of education and training. They bring new skills, information and technology to host countries. Thus, there is a virtuous circle between human resource development and FDI.

7.4.4 The impact of remittances

The most tangible link between migration and development is through the impact of remittances. World Bank data show that recorded remittances sent home by migrants

from developing countries reached over US\$200 billion in 2006, more than double the level in 2001. However, the true value of remittances, including unrecorded flows via formal and informal channels, is substantially higher. According to the World Bank, remittances through informal channels could add at least 50 percent to the globally recorded flows.

Survey data on Zimbabwean migrants also suggest that given opportunity migrants would like to contribute towards business related activities. Table 7.7 regarding migrants in South Africa and the UK shows that sending remittances ranks fourth among ways they would like to contribute to the development of Zimbabwe.

While there is a great willingness to contribute to the development of Zimbabwe, migrants cite some critical changes that would help them to contribute effectively, viz.: political changes (60 percent), economic

Table 7.7: Five most popular ways that respondents would like to contribute to development in their home country

	UK	South Africa	Total
Investment in business	62%	53%	58%
Transfer skills through working in Zimbabwe	44%	31%	38%
Transfer skills through training in Zimbabwe	44%	31%	37%
By sending remittances	32%	27%	29%
Investment in land development	34%	22%	28%

Source: Bloch (2005)

opportunities (50 percent), voting rights (49 percent) and better exchange-rate policy (47 percent).

The International Fund for Agricultural Development (IFAD) reported that in 2006 Zimbabwe received US\$361 million in remittances excluding hand-in-hand transfers, representing 7.2 percent of the country's 2006 GDP. The extent of under-reporting could be severe. An estimate of remittances in money and kind extrapolated using a conservative remitting population of one million migrants in the diaspora suggests that the home country could be receiving as much as US\$500 million per year, which is 10 percent of GDP and over 50 percent of exports. The RBZ data show US\$5.2 million (2006) and US\$14.0 million (2007) as having been transferred through money transfer agencies it supervises. What is clear is that no one knows with any degree of certainty the exact magnitude of remittances coming to Zimbabwe because remittance flows largely occur through informal channels and hence are unrecorded, this creates problems for policy making.

What is clear is that remittances play a major role in supporting livelihoods in contemporary Zimbabwe. A 2007 survey carried out by the Harare-based Mass Public Opinion Institute (MPOI) on survival strategies employed by the Zimbabweans at home found that remittances from friends and relatives rank

as the fourth most important source of livelihood for households after salary, farming and 'off-farm' and 'extra-job' activities. Remittances are reported to be an alternative source in providing for food (12 percent rely on them), health care (11 percent) and cash income (11 percent). In addition, they have become a critical source of foreign currency for the Government¹² (MPOI, 2007). An earlier study on *Remittances, poverty reduction and the informalisation of household wellbeing in Zimbabwe* by Bracking and Sachikonye (2006) found that in addition to reducing poverty, they contribute to productive accumulation. Another study by Pendleton *et al.*, (2006) confirms the extent to which remittances have become an essential part of household budgets and have reduced vulnerability at the household level through poverty reduction in both rural and urban households. About 90 percent of the 705 migrant households (i.e., households with at least one member who is resident outside the country) sampled throughout the country reported that family members who have migrated remit cash back home regularly using both formal and informal channels. An analysis of the importance of remittances in meeting household expenses shows that the net contribution of remittances ranges from 80-93 percent of total household expenditure.

In an economy in which the financial system does not work properly, remittances provide

¹² A government minister recently acknowledged as much in a private conversation with a reporter. Asked about the gravity of the economic crisis, he reportedly said: 'What's keeping us going is (sic) remittances from Zimbabweans who left the country. Without those, 50 percent of the people who are struggling to survive at the moment would die' ('Lunch with a dissident minister' *The Sunday Times (UK)*, 8 July 2007)

entrepreneurs with an alternative source of start-up capital, particularly in the informal sector. A study on the uses of remittances by households in rural southern Zimbabwe by Maphosa (2007) shows that while consumption tops the list, remittances have varied uses. Table 7.8 below illustrates the uses observed by the study.

While there is much emphasis on the beneficial effects of remittances, there are social costs to take into account. Families have been separated and the standard of living in the diaspora is scaled down in order to support those left home. Bracking (2003) provides an example of a migrant in Birmingham (UK) who reduced her living costs by living in a hostel with fellow Zimbabweans and walking to work to save money for remittances. A similar situation obtains in South Africa where cases of migrants living in crowded accommodation and informal settlements are common. A survey in Johannesburg found that 95 percent of 4,654 respondents had relatives they support back home, and remittances constituted 15–20 percent of their earnings (Makina, 2007). It is noteworthy that before the crisis remittances were an insignificant proportion of GDP. Recovery efforts that emphasize return of skills need to simultaneously focus on remittances as part of the financial start-up capital for returnees.

7.5 CONSTRAINTS TO THE GROWTH AND RECOVERY OF LABOUR MARKETS, HUMAN CAPITAL AND THE DIASPORA

7.5.1 Institutional constraints (labour administration)¹³

The key ministries that have jurisdiction over labour-market issues include the Ministry of Public Service, Labour and Social Welfare, and the Ministry of Youth Development and Employment Creation. Other ministries, such as Higher and Tertiary Education, Small and Medium Enterprises Development, and Women's Affairs, Gender and Community Development also overlap into labour-market issues.

In line with the ILO's Labour Administration Convention of 1978, the Ministry of Public Service, Labour and Social Welfare is responsible for coordinating and running the labour administration system of Zimbabwe. However, the Ministry of Youth Development and Employment Creation is responsible for issues pertaining to youth empowerment and employment creation. Clearly therefore, there are vast areas of overlap in the responsibilities of these two

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Table 7.8: Uses of remittances

Remittance use	Number of remittance-receiving households	Frequency
Food	79	98.8%
Fees	63	78.8%
Medical expenses	52	65.0%
Livestock	47	58.8%
Building and consumer goods	25	53.8%
Agricultural inputs	43	31.2%
Business	8	10.0%
Other	31	38.8%

Source: Maphosa (2007, p.130)

¹³ The 'system of labour administration' covers public administration bodies including ministerial departments, parastatal and regional or local agencies or any other form of decentralized administration and any institutional framework for the coordination of the activities of such bodies and for consultation with and participation of employers and workers and their organizations (ILO Convention 150 & Recommendation 158 of 1978).

ministries, often resulting in duplication. Furthermore, each ministry has tended to concentrate on its own interventions, with little coordination with the other.

Another ministry that overlaps into labour-market issues is the Ministry of Small and Medium Enterprise Development. This ministry was created after the 2005 Parliamentary elections, prior to which SMEs came under the Ministry of Industry and International Trade and issues relating to the informal economy fell under the Ministry of Youth Development, Gender and Employment Creation. The Ministry of Small and Medium Enterprises is now also responsible for the promotion of the informal economy and its integration into the mainstream economy. However, in spite of the SME Fund created by the Reserve Bank of Zimbabwe in 2006,¹⁴ the resources available have been inadequate. The Ministry of Women's Affairs, Gender and Community Development is responsible for the empowerment of women and gender mainstreaming, implying that it also overlaps into labour-market issues. However, it remains marginalized and poorly resourced.

The major weakness of these various labour-market interventions is that they are not properly coordinated, they are fragmented, duplicate each other, and are poorly funded. They also have a supply focus, with ministries implementing programmes even when they do not have the requisite competencies (e.g., in the area of business development). For instance, the centralized labour administration system is such that decentralized bipartite structures such as the National Employment Councils, formed by unions and employers at the sectoral level, have a very limited role, mainly in collective bargaining. Industrial-relations management and employment services are undertaken predominantly by Ministry of Labour officials.

Interviews with senior officials in the various ministries revealed a lack of clarity on the limits of their responsibilities in dealing with labour issues, and in particular with SME development and employment creation. The frequent reorganization of these ministries has not helped matters. However, the tendency to create ministries to deal with specific issues (e.g., SMEs, Indigenization, Youth Development) creates the impression that it is the public sector that has the primary responsibility for dealing with them rather than playing a facilitating role.

7.5.2 Legal constraints

The system of labour administration is characterized by a multiplicity of laws, resulting in segmentation. For instance, the Labour Act [Chapter 28:01] applies only to the private sector;¹⁵ while in the public sector, the Public Service Act [Chapter 16:04] applies. Even though the Amendments of 2002 had partially included the public sector under the Labour Relations Act, Amendment No. 7 of 2005 took them back to the Public Service Act. The Public Service Act does not recognize the collective-bargaining rights of public employees, and its structures for dealing with grievances and disputes are heavy-handed and unilateral. In fact, the Public Service Act does not have provisions for unions, and the various associations in existence do not have trade union rights; although a Joint Negotiating Forum was established in 1998, its role is merely advisory. The Urban Councils Act [Chapter 29:15] offers procedures and conditions at variance with those in the Labour Act, resulting in a conflict of laws in that a party to a dispute may choose to take recourse via the Labour Act or via the Urban Councils Act.

The Labour Act also contains draconian measures meant to curtail trade union activities, including the proscription of the

¹⁴ A ZW\$16 Billion (US\$29 000) Small to Medium Enterprises Revolving Fund was established following the Bank's announcement of the Mid-Term Monetary Policy Statement in July 2006.

¹⁵ Prior to 2003, the Labour Act was called the Labour Relations Act.

right to strike. Apart from criminalizing participation in unlawful collective job action, Section 109 of the Act also empowers an affected party to claim damages from an employee or trade union for losses incurred as a result of the strike. Unions risk their registrations being suspended for a period of twelve months, and cannot collect subscriptions during this period. Furthermore, recourse to draconian laws such as the Public Order and Security Act (POSA) [Chapter 11:17], the Access to Information and Protection of Privacy Act (AIPPA) [Chapter 10:27] and the Criminal Law (Codification and Reform) Act (No. 23 of 2004) are often invoked to curtail trade union freedoms. Even though the High Court ordered the State not to interfere with trade union meetings in 2002,¹⁶ this is often ignored.

National Employment Councils, which are best suited to dealing with disputes with regard to conditions of service in their sectors, are merely conciliatory bodies with no effective powers, implying that they still have to refer matters to the Ministry of Labour, resulting in a backlog of cases as a result of the centralized labour administration system. Despite the streamlining of the dispute/grievance procedures, and the introduction of a specialized Labour Court to deal with labour matters, delays still characterize their resolution, though the situation is much better than in previous years.

Furthermore, the Manpower Planning and Development Act [Chapter 28:02] grants the Minister of Higher Education unilateral powers to manage the Zimbabwe Manpower Development Fund (ZIMDEF) which is the country's national skills development fund as he/she deems fit, resulting in it being run in a non-transparent and unaccountable manner. This has been a bone of contention with industry, which feels let down by being unable to access the resources earmarked for skills training to which they have contributed.

7.5.3 Policy constraints

A key policy constraint is that, while Zimbabwe inherited a dual economy, with aspects of enclavity (separate existence), post-independence policies have only served to entrench this dual structure. The weak labour absorptive capacity of the economy can be traced to this dual and enclave structure, where the formal sector at independence employed only 20 percent of the labour force, the remaining 80 percent being located in the marginalized and vulnerable, mainly communal, non-formal sector. Instead of the economy being formalized as was to be expected, an informalization of the economy has occurred, such that the formal sector now accounts for only around 13 percent of the labour force.¹⁷ The majority of the labour force therefore continues to be simultaneously marginalized and excluded from the dynamic part of the economy, the formal sector, whose labour absorptive capacity has declined, as reflected in the negative employment elasticities of output.

While government sought to protect workers through labour legislation during the first decade of independence, that protection was onerous, with unintended unemployment consequences. The determination of wages by government, which characterized the period of the 1980s, undermined the role of labour-market institutions. The period of ESAP saw a deregulation of labour laws to achieve labour-market flexibility. However, the pendulum swung to the other extreme, resulting in a wave of retrenchments. Thus, neither extreme case – over-regulation and flexibility – helped the cause of employment creation and poverty reduction. Finding a balance between the imperatives of flexibility and security is an ongoing challenge that requires negotiation in order to arrive at a form of regulated flexibility.

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¹⁶ *Zimbabwe Congress of Trade Unions v. The Officer Commanding Police Harare District and the Commissioner of Police*, H-H 56/2002.

¹⁷ The growth of the informal economy as the formal sector shrunk is illustrated in chapter 6 on private sector development.

With respect to human capital formation, a key policy challenge is the need to ensure that education and training is more demand-driven: the current supply bias results in a poor fit between demand and supply. The current secondary-education curriculum does not develop children effectively according to their unique needs and inclinations, and does not lay a solid foundation for employability and the integrability of its graduates into the economy. A key weakness of the secondary-school curriculum is that, having an academic bias, it is not 'all inclusive' and lacks a 'pathways approach' that caters for the diverse abilities and interests of the pupils.

An important policy issue with respect to the overexpansion of the education and training system – which has compromised quality, resulting in lack of international recognition of Zimbabwean qualifications in recent years – is the need to ensure that expansion is within the limits of the available resources. The recent expansion of the university system to no less than nine such institutions is a case in point. The situation is compounded by the recent parallel development whereby technical colleges are also offering degrees. The proliferation of such institutions coincides with the decline in quality and the lack of recognition of Zimbabwean qualifications at regional and international levels.

7.5.4 Financial and capacity constraints

The multiplicity of institutions involved in labour administration, and the rapid and massive expansion of education and training provision have stretched available resources to the limit. With the withdrawal of cooperating partners after 1999, this has left a huge funding gap, undermining quality. Because of a lack of resources, refurbishment and replacement, the state of infrastructure and equipment has continued to deteriorate. The

role and importance of donors, especially with respect to technical and vocational education and training, is demonstrated by the fact that, for example, USAID built and equipped Belvedere Technical Teachers' College and Mutare Polytechnic, while GTZ (German Technical Assistance) equipped Harare Institute of Technology, Msasa Vocational Training Centre and Masvingo Polytechnic, and the Chinese built Chinhoyi Technical Teachers' College.

There is therefore an urgent need to rationalize the provision of technical and vocational education and training, and to promote stakeholder participation in funding. The lack of resources has resulted in low and unattractive salaries in the public system of labour administration, and in education and training systems. Coupled with the brain drain, it has effectively undermined the capacity of the systems to deliver an efficient and effective service.

A recent Zimbabwe National Student Union congress report aptly described conditions in the education sector:

*'A review of pertinent data shows that Zimbabwe is facing a sharp decline in public expenditure on higher education, deteriorating teaching conditions, decaying educational facilities and infrastructure, perpetual student unrest, erosion of university autonomy, a shortage of experienced and well trained teaching staff, lack of academic freedoms and an increasing rate of unemployment among college graduates.'*¹⁸

7.5.5 Constraints to return migration

Empirically, constraints to the development of human resources and immigration could be gleaned from survey data which examine conditions migrants require for them to return

¹⁸ *Financial Gazette*, 31 January 2008.

Table 7.9: Conditions for return to Zimbabwe by country of residence (%)

Condition for return	South Africa	UK	All
Improved political situation	72%	87%	80%
Improved economic situation	76%	83%	80%
Improved security	48%	72%	60%
Better health care	48%	64%	57%
Better employment prospects	47%	53%	50%
Better education for children	42%	51%	47%
Improved infrastructure	36%	43%	40%
After saving enough money	27%	39%	33%
To retire	28%	36%	32%
Offer employment	28%	31%	30%
Better education for myself in Zimbabwe	30%	25%	28%
Other	3%	3%	3%
None	6%	1%	3%

Source: Bloch (2005)

to Zimbabwe. The conditions for return are good proxy indicators for constraints that inhibit immigration, human resource development and retention. A survey in the UK and South Africa produced results illustrated in Table 7.9.

It is not surprising that economic and political considerations top the list of constraints or conditions for return as these are the main reasons cited as reasons for migrating.

7.6 SUSTAINABLE AND INCLUSIVE RECOVERY PATHWAYS AT THE LEVEL OF STRATEGIC THRUSTS AND DETAILED POLICY RECOMMENDATIONS

7.6.1 Strategic objectives

On the basis of the foregoing analysis, the key strategic objectives will be to:

- Rationalize the labour administration system to create a unitary, decentralized system.
- Reorganize Technical and Vocational Education and Training to make it more demand-driven and responsive to the needs of the economy, including the informal economy.

- Promote sustainable and inclusive recovery ‘pathways’ in the labour market, and in education and training provision (promoting integrability).
- Promote a shared approach to financing.
- Remove constraints that deter return migration (i.e., return of skills).
- Develop a manpower recovery plan for the public sector.
- Develop strategies that maximize the developmental potential of the diaspora.
- Mainstream HIV and AIDS as a workplace challenge.

7.6.2 Sustainable and inclusive recovery pathways

Rationalization of the labour administration system to create an integrated, coordinated and inclusive decentralized system

Global trends indicate that labour administration systems are being stream-lined in line with ILO Convention 150 and Recommendation 158 of 1978. The Convention provides detailed functions of a coordination unit of the labour administration system (the competent authority), which is usually the Ministry of Labour. It emphasizes

consultation, cooperation and negotiation between the public authorities and the most representative organizations of employers and workers as essential at local, national and regional levels and within the various sectors.

In consultation with other social partners, the competent bodies should:

- Develop, adopt, apply and review labour standards, including all relevant laws and regulations.
- Regulate terms and conditions of employment through collective bargaining.
- Ensure free exercise of employers' and workers' right of association.
- Put in place programmes to promote labour relations that encourage progressively better conditions of work and working life, respecting the right to organize and bargain collectively.
- Provide advisory services to enhance labour relations, promote the full development and utilization of machinery for voluntary negotiation.
- Provide conciliation and mediation facilities appropriate to national conditions to resolve disputes.
- Coordinate employment services, employment promotion and creation programmes, vocational guidance and training programmes, and unemployment benefit schemes.
- Promote methods and procedures of consulting employers' and workers' organizations on employment policies and promote their cooperation in the implementation of such policies.
- Share responsibility for the management of funds created to counter under- and unemployment or assist in the employment of certain categories of workers.
- Constantly review the structures of the national system of labour administration, in consultation with social partners.

Thus, labour administration plays its full role in development, if:

- It contributes to the maintenance of a healthy social climate that promotes development;
- The services that it offers are effective and correspond to the needs of users;
- The services and products contribute to the design of development strategies; and
- The social partners participate.

In the case of Zimbabwe, the first challenge is to reorganize the system of labour administration so that a unitary system is created under the Ministry of Labour. The multiplicity of institutions dealing with labour issues should be rationalized into one in which key social partners are consulted. When labour-market policy falls under one authority, it is easier to create conditions for a coordinated effort and to develop a common vision. The involvement of workers and employers creates a culture of joint responsibility, which promotes a long-term commitment to problem-solving.

A second challenge is the need to decentralize the system, especially by empowering National Employment Councils at sector level and works councils at shop-floor level, which are currently focusing almost exclusively on collective bargaining. These structures are better placed to play an active role in labour-relations management, employment services and training, among other functions, to avoid the current centralization and its attendant supply bias.

Reorganizing Technical and Vocational Education and Training to make it more demand-driven and responsive to the needs of the economy, including the informal economy

There is a need for the education and training systems to be re-oriented from their current supply focus towards more flexible, demand-driven systems, in line with global trends:

‘cooperation between the government and the private sector is the cornerstone of the process through which the government role changes as development proceeds’ (Middleton *et al.*, 1993: 129). As they say later,

‘The challenge is to move from policies dominated by social and supply objectives and programs financed and provided by governments to policies and programs that respond to market forces and promote employer and private training, and that establish appropriate complementary and supportive roles for the state.’ (253)

Bureaucracy and inflexibility may be reduced by allowing stakeholder participation in the governance structures at all levels. Given this new thrust, whereby training is viewed as a shared responsibility, there are implications for the governance structure of the publicly run vocational education and training institutions. The key issue here will be how to transform the supply-driven, centrally controlled and bureaucratic public institutions to make them more responsive to market forces.

According to the World Bank, ‘to respond to the needs of the economy demands a degree of freedom from short-term bureaucratic control that is difficult to achieve in line ministries. National training authorities (NTAs) have been found to be effective in this respect in several countries’ (1991: 23). Although the structure of successful organizations varies, the crucial aspect is a structure of governance that involves the various stakeholders (employers, unions, etc.) and creates adequate and stable funding, freedom to use resources flexibly, and a high level of professional capacity (World Bank, 1991; Middleton *et al.*, 1993; Zimbabwe, 2006a).

The implementation of the two-pathways policy at the secondary level of education should be accelerated, with the requisite equipment provided through partnerships with

the private sector and other stakeholders (e.g., students/parents). To promote inclusiveness, curricula should be redefined so as to meet the specific demands of the non-formal (including informal) and small-scale sectors. Skill requirements of the SME and informal sectors might be addressed within the formal education and training systems, along the lines taken by the Informal Sector Training and Resource Network (INSTARN) project in Zimbabwe, the Mubarak-Kohl initiative in Egypt, the Open Apprenticeship system in Nigeria, or the learnership programme in South Africa. In addition, mechanisms for cost-sharing between government, enterprises, parents and students should be put in place to enhance the sustainability of education and training provision and achieve high standards of quality (in terms of both inputs and outputs).

The delivery patterns in Technical Vocational Education and Training (TVET) worldwide reflect a variety ranging from school-based provision to non-formal training arrangements, or a combination of the two. In response to globalization, the trend favours a more market-oriented approach since skills are required to respond flexibly to rapidly changing demands. The restructuring of TVET systems worldwide suggests the following trends:

- Exclusive government-controlled TVET systems are opening up to a linkage with private TVET institutions and skills-development providers (including company-based training), sometimes co-financed from national budgets.
- Entrepreneurship in TVET and skills development is encouraged through microfinancing.
- Greater autonomy is being granted to TVET institutions.
- New financing and certification mechanisms are envisaged.
- The curricula for the training of trainers and apprenticeship are being revised.

- Dual forms of training are promoted (UNESCO-UNEVOC, 2004).

Developing a national employment policy framework

So far, the country has not implemented a coherent employment strategy. This is not restricted to Zimbabwe, as the Millennium Summit of Heads of State and Government adopted the need to put employment creation at the centre of development policies, resulting in the establishment of the Youth Employment Network (YEN) at the global level. To implement this global challenge, the Heads of States and Governments in Africa met in Ouagadougou, Burkina Faso, in September 2004 and directed Regional Economic Communities (RECs) to assist countries develop national plans of action on employment creation and poverty reduction.¹⁹

Promoting sustainable and inclusive recovery 'pathways' in the labour market, and in education and training provision (promoting integrability)

To sustainably address the challenges posed by unemployment, under-employment and widespread poverty, it is necessary to fully integrate the non-formal sector into the mainstream of the economy by tackling the dual and enclave structure of the economy and to consciously integrate disadvantaged and vulnerable groups such as youths, women, people with disabilities and mainstreaming HIV and AIDS as a workplace issue.

One way of achieving this integrative, transformative agenda is to facilitate the evolution of backward and forward linkages through the exploitation of value chains and value systems among firms and sectors via the removal of constraints identified by the private sector. Broadening the scope of a firm or industry's influence, and facilitating the establishment of firms and sectors with coordinated value chains, can lead

to a broad-based, more inclusive and employment-intensive growth path. A good example is the case of Kondozi horticultural farm that established extensive linkages with its hinterland in such a manner that, apart from direct employment in the concern, the communities were developed into out-growers (see chapter 9 on land policy and agriculture). Until its takeover by government, Kondozi provided an excellent example of exploitation of the value chains and systems of an individual entity in a virtuous manner. Useful examples have emerged in recent years in sectors such as tea/coffee growing, textiles and clothing, furniture, poultry, fish farming and among others. The role of the State should be restricted to facilitating such developments by removing constraints and creating an enabling environment.

An active labour-market approach, with some of the following interventions, will help to integrate and mainstream hitherto marginalized groups and sectors to enhance integrability:

1. Employability

The following should be established:

- Training and skills-development programmes, such as apprenticeship programmes.
- Vocational training programmes designed and implemented in partnership with the private sector.

2. Employment creation

Areas for job creation include the following:

- SME promotion and development;
- Labour-based public works where the State can use its resources to promote employment-intensive infrastructure development.

¹⁹ The original RECs in Africa have now been confirmed by the AU, i.e., ECOWAS, AMU, ECCAS, COMESA (including EAC) and SADC.

TO SUSTAINABLY ADDRESS THE CHALLENGES POSED BY UNEMPLOYMENT, UNDER-EMPLOYMENT AND WIDESPREAD POVERTY, IT IS NECESSARY TO FULLY INTEGRATE THE NON-FORMAL SECTOR INTO THE MAINSTREAM OF THE ECONOMY

- Business linkages.
- Self-employment programmes.
- Programmes targeting people with disabilities and other vulnerable groups.

The choice of technique of production is critical for improving labour intensity in the economy, and this can be influenced through macroeconomic policies. For instance, real exchange-rate depreciation is a powerful tool for changing relative prices in favour of the tradable goods sector. It raises the price of imported capital relative to labour, thus providing an incentive for the more intensive use of labour.

Promoting a shared approach to funding

Globally, the culture of supply-driven programmes funded by the public sector is increasingly giving way to a shared approach to funding. Users of the service are increasingly playing an important role in funding arrangements to ensure sustainability. In this regard, the private sector is now playing a more active role in funding training programmes. This is particularly critical in the context of Zimbabwe, where public funds are limited and the anticipated stabilization programme will entail significant cuts in expenditure.

However, given the imperative of developing the skills needed, cooperating partners and other stakeholders, and especially the private sector, will have to play a more visible role. The participation of the private sector in skills development in Zimbabwe is not a new issue. Many of the older training institutions, including technical colleges in Harare, Bulawayo and Kwekwe, were actually built and equipped by the private sector. The mining and hospitality sectors have taken a lead in this regard, having taken over the running of the mining and hospitality schools that used to be part of the Bulawayo Polytechnic. Other sectors, such as the motor industry, are moving in this direction. Mutare Technical College is working in

partnership with the forestry sector in Manicaland and is now offering a degree programme in wood technology.

Amendment of the Manpower Planning and Development Act to allow the private sector greater influence over the use of Zimbabwe Manpower Development Fund (ZIMDEF) would release resources for skills development.

Facilitating the return of skills

Cognisant of the impact of the brain drain through migration, the government would need to participate in programmes of voluntary assisted return. Furthermore, it should engage in co-development programmes with countries that have a high concentration of Zimbabweans, focusing on migrants' return or the 'return potential' as a development factor. The government should harness the potential for return migration by entering into beneficial arrangements with selected countries in order to formulate appropriate migration policies aimed at facilitating the mobility of skilled workers in ways that are beneficial to both the destination and sending country.

Immigration policies

Zimbabwe needs to put in place policies that make immigration compatible with economic, demographic, social and development objectives. It is necessary to design and adopt policies that incorporate into the country's productive activities foreigners whose technical knowledge and expertise are indispensable for current and future economic and social development programmes, whether in government or in the private sector. This requires the introduction of flexible immigration policies. Lessons learned elsewhere broadly classify such policies into three categories: selective immigration policies, directed immigration policies and spontaneous immigration policies.

Selective immigration policies would target foreign professionals, scientists, technicians and skilled workers. There are examples of

countries that have successfully implemented such policies. Since 1984, Australia has had an immigration policy that has been attractive to skilled workers whereby candidates are selected according to their prospective contribution to the Australian economy. New Zealand, the UK, Canada and the USA have adopted a similar approach and have increased the share of highly educated people among selected immigrants. In mainland Europe, Germany has introduced a flexible migration policy that allows for both temporary and permanent labour migrants. Zimbabwe should adopt similar policies in order to accelerate development.

Directed immigration policies, on the other hand, would target the entrance of people and groups who will be channelled to planned areas for development. It is an approach quite often applied in Africa. Zimbabwe has applied the approach with regard to medical doctors from Cuba, who are recruited to work in the rural areas. In a situation where the brain drain has occurred across the board, it is necessary to widen the categories of skills to which this policy applies.

Spontaneous immigration policies are very suitable to a developing country that cannot compete with developed countries in attracting skills. Such policies would allow the entry of those foreigners who come voluntarily at their own expense as long as they have the means to support themselves and are able to contribute to the development of the country. Zimbabwe would be advised to adopt this approach as part of its immigration policies.

Allow dual citizenship

Under the current laws of Zimbabwe, an emigrant who acquires citizenship of another country, or alternatively, who stays outside the country for seven years consecutively, loses his or her Zimbabwean citizenship. In addition, Zimbabwe migrants lose voting

rights when resident outside the country. In order to tap the developmental potential of the diaspora effectively, these laws need to be changed to allow for dual citizenship and accord voting rights so that the attachment of the diaspora to the homeland becomes permanent.

Updating data

The last major surveys, such as the population census, the Poverty Assessment Study Survey (PASS) and the labour force survey were last conducted in 2002, 2003 and 2004, respectively.²⁰ Much has happened since then, requiring new surveys to provide more accurate up-to-date data. It is therefore proposed that a major survey combining the three should be undertaken in 2009 so that policy is informed and based on accurate data. A detailed Labour Market Information System (LMIS) should be developed as part of the labour administration system.

7.7 CONCLUDING REMARKS

In conjunction with the overall and rapid decline in macroeconomic indicators, this chapter has clearly shown how developments in labour markets, human capital and the diaspora have promoted anti-poor outcomes, namely, declining levels of growth, employment, real incomes and increased out-migration. Constraints in terms of the multiplicity of institutional arrangements, the supply bias of interventions, especially in human capital formation, policies that have entrenched the exclusion of various groups and sectors, inadequate resources and declining capacity have compounded the deteriorating situation.

There is a need to rationalize the institutional arrangements to promote a better-coordinated and decentralized labour administration and an education and training structure that is more demand-driven. Shared approaches to

²⁰ Central Statistical Office (CSO), 2002: Census 2002 National Report, CSO, Harare. Central Statistical Office (CSO), 2006: 2004 Labour Force Survey, March.

funding are a critical aspect of ensuring sustainable, efficient and effective delivery. Furthermore, the need to put in place mechanisms to turn the ‘brain drain’ into a ‘brain gain’ by, among other things, facilitating the return of skills, participating in schemes

to assist returning migrants, allowing dual citizenship, and adopting more strategic immigration policies. All these measures will help to ensure that, over time, Zimbabwe has the human capital base necessary to support long-term recovery.

Chapter 8

Reviving Manufacturing, Mining and Tourism

A pervasive theme of this report is that the disconnect between developments in Zimbabwe over the past decade and those in the regional and global economies will affect the future structure, direction and performance of the economy. This chapter assesses three sectors critical to Zimbabwe's economic future, manufacturing, mining and tourism.

8.1 MANUFACTURING INDUSTRY

8.1.1 Introduction

Arguably, prior to the pre-occupation with land reform at the end of the 1990s, industrialization was at the head of the economic policy agenda because of the need to diversify from undue dependence on primary products, especially commodity exports, and the fact that – as sub-Saharan Africa's second most industrialized country after South Africa – policymakers believed that a platform for accelerated industrialization was in place. In the event, however, as Table 8.2 shows, the economy deindustrialized with the share of manufacturing value added (MVA) declining well before the setbacks associated with the Fast Track Land Reform Programme (FTLRP).

The most widely-used measure of industrial progress is manufacturing value added per head of population. In Zimbabwe, because both the value-added numbers and the

population estimates are subject to significant error – especially in recent years – MVA per head figures should be used with caution. Figure 8.2 shows that in both the 1980s and the 1990s – when the estimates were more reliable than those in recent years – MVA per head declined, fractionally in the 1980s, but some 10 percent in the 1990s. After 1999 the decline accelerated and MVA per head has virtually halved since then.

During the 1980s control regime period, growth was constrained by scarce foreign exchange and an overvalued exchange rate, as a result of which the main drivers of industrial growth were domestic demand and import substitution. Gross Domestic Product (GDP) (at constant 1990 prices) grew 4.4 percent annually during this period while manufacturing value-added grew 3.4 percent a year. As a result, manufacturing industry's share of GDP declined significantly to 20.5 percent in 1990 from 23.3 percent a decade earlier.

During the Economic Structural Adjustment Programme (ESAP), MVA growth more than halved to 2.1 percent annually, reflecting the combination of a sharp slowdown in GDP growth to 1.9 percent a year, associated with two severe droughts in 1991/2 and 1994/5, as well as the rapid liberalization of the economy including the dismantling of blanket import controls.

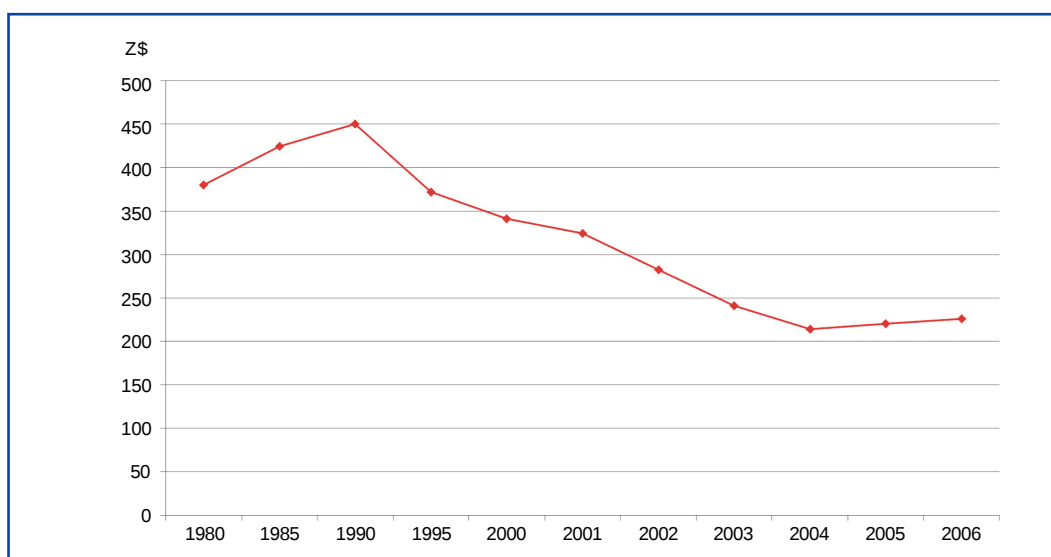
After peaking in 1990, MVA per head halved over the next decade, during which period GDP fell 30 percent. The process of

Table 8.1: Growth of GDP and MVA (1980–2006)

Phase	Years	GDP growth (% p.a.)	MVA growth (% p.a.)	MVA share of GDP start period	MVA share of GDP end period
1	1980–1990	4.4	3.4	23.3	20.5
2	1990–1996	1.9	2.1	20.5	19.7
3	1997–2006	–4.2	–7.1	19.2	13.0

Source: Central Statistical Office, Harare: National Accounts (2006)

Figure 8.1: Manufacturing value added per head, 1980–2006



Source: Central Statistical Office, Harare, *National Accounts (various editions)*

deindustrialization that took hold in the 1990s accelerated after 2000, and the decline in MVA since 1990 outstripped similar falls in GDP, as well as those in mining and agricultural value-added.

Although MVA has fallen further and faster than in any other sector of the economy, deindustrialization started well before the onset of the land-reform crisis in 2000. Indeed, during the 1990s, output volumes increased in just four of eleven sub-sectors of the industrial sector. By 1999, production had risen 25 percent in clothing, 185 percent in wood and furniture, 15 percent in non-metallic minerals and 7 percent in chemicals. Declines ranging from 30 percent in transport equipment to 4 percent in beverages underline the extent to which the fabric of the manufacturing sector had been weakened even before the steep post-2000 decline in economic activity.

8.1.2 Current situation

Although manufacturing industry was not derailed by a single exogenous shock, it suffered setbacks across a number of different fronts – ESAP, the severe 1991/2

drought, the maturation of import substitution industries, the overvalued exchange rate, the inability to grow manufactured exports and the FTLRP – that had the cumulative effect of virtually halving its contribution to GDP.

Unquestionably, because the sector was so closely integrated with commercial agriculture, the most devastating shock was the knock-on effect of the FTLRP. In the mid-1990s over half the inputs into agriculture – fertilizer, stockfeeds and insecticides – were supplied by the manufacturing sector, while in the reverse direction 44 percent of agricultural output was sold to the manufacturing sector, some 95 percent being supplied by the commercial farming sector and the balance by small-scale communal growers. An estimated 62 percent of commercial output and 29 percent of communal production was sold to manufacturing industry.

All industrial indicators reflect the steep decline experienced over the past decade: manufacturing employment in 2004 was 26 percent below its peak in 1998. Exports of ‘pure’ manufactures¹ halved between 1997 and 2004 while the number of products exported declined and export concentration

¹ i.e., excluding ferro-alloys, cotton and steel.

Table 8.2: The current state of manufacturing

%	2005	2006	2007
Capacity utilization	35.8	33.8	18.9
Output	-29.0	-18.0	-28.0
Employment	n.a	n.a	-12.0
Business confidence (% pessimistic)	54.0	77.4	70.0

Source: CZI Manufacturing Sector Survey (July 2008)

increased in terms of both markets and products. The 2006 survey of manufacturing by the Confederation of Zimbabwe Industries (CZI) found that four regional markets – Zambia, South Africa, Botswana and Malawi – absorbed 80 percent of manufactured exports, while the number of export firms declined by 15 percent over three years.

According to the July 2008 CZI Manufacturing Sector Survey, industrial production declined 59 percent between 2005 and 2007 and by the end of 2007, output in surveyed firms was less than 30 percent of its 2003 levels. Capacity utilization collapsed to less than 20 percent in 2007 with only 4 percent of firms operating at over three-quarters of installed capacity. At the other extreme, 75 percent of industry was operating at less than 50 percent capacity utilization.

The survey estimated that ‘most workers’ were not earning a living wage, with unskilled employees earning less than US\$20 a month. Only 2 percent of respondents described themselves as optimistic (4.8 percent in 2006) while 70 percent said they were pessimistic.

Interviews with industrialists conducted in mid-2007 confirm CZI survey findings that industry was operating at approximately one-third of its installed capacity and that output had halved since the onset of the crisis in 2000. Most industrialists interviewed warned that a significant proportion of existing capacity was theoretical rather than actual in the sense that substantial new investment would be needed to renovate and update

existing plant and machinery, a great deal of which was obsolete. Most said too, that they had been unable to keep pace with contemporary developments in technology and that efficiency had been undermined by inadequate maintenance, partly the result of shortages of both skills and imported spares and components.

Because of the price-control regime it would take companies up to two years to restore cash-flow viability, according to one multinational. His company’s chief competition – and he believed this to be the case for many manufacturers in Zimbabwe – is South Africa. The South African business model for consumer goods producers was buyer-driven, with South African corporates establishing strong retail chains in Southern African countries (Botswana, Mozambique, Zambia, the DRC and Tanzania), which made it very difficult for Zimbabwean firms to compete in regional export markets, especially because – for the most part – South African brand recognition is far stronger than that of Zimbabwe manufacturers.

Almost all those interviewed identified the loss of skills and the deterioration in the country’s training and education infrastructure as the most important single problem that industry will face in a post-crisis environment. An executive with the largest trainer of artisans in the country said that his company was losing about half of its qualified artisans each year.

It has become increasingly difficult to maintain quality standards. Operating costs are higher where there are no ‘experience effects’ (learning-curve effects) as a result

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of high rates of staff turnover and the fact that employees do not stay long enough to accumulate experience. Firms have resorted to poaching skills from one another, leading to wage inflation. Personnel previously categorized as technicians are now graded engineers, reflecting a downgrade of industrial capability across the board.

Some industrialists said that ‘skewed pricing systems’ were causing severe problems because they had inflated demand both locally and regionally. A Coca-Cola bottler said that, in US dollar terms, Zimbabwe has ‘the cheapest Coke in the world’, which both fosters smuggling and strains foreign-currency reserves because of the high import content of the product. A cigarette manufacturer concurred, saying that price controls had encouraged regional smuggling and that cigarettes manufactured in Zimbabwe were being sold in regional markets at ‘dumping’-level prices. Cigarette prices in Zimbabwe are less than half the world average.

For most manufacturers however, demand has been depressed since 2000, as a result of which manufacturers are unable to exploit scale economies. Because of the overvalued exchange rate it has been impossible to offset domestic market shrinkage by penetrating export markets. Consequently, manufacturers have been forced to ‘downtrade’ – producing smaller packs, skimping on quality, and aiming at the low-income market. This in turn, has undermined exports, except for low-technology and low-quality items, which are often produced more cheaply in regional markets.

Without exception, all executives stressed the need for ‘massive’ new investment in almost all aspects of infrastructure, but especially electricity, water and transport (particularly roads and railways). Almost all said that costs were inflated by the need to operate stand-by generators, while one food manufacturer said that all water had to be purified because it fell below required standards.

Most executives said that exports were a residual rather than a core activity, but one of the country’s largest industrial exporters said that his company was losing orders of some US\$4.5 million monthly owing to a variety of constraints, the most important being electricity supply, rail transport and skills. One paint manufacturer said that, because of high import content (approximately 80 percent), South Africa is a much cheaper source of supply and that neighbouring countries could source imports from South Africa both more cheaply and more reliably – given infrastructure and skills constraints – than from Zimbabwe. Others said that they had lost their export markets because regional or global headquarters had elected to serve Southern and East African markets from South Africa or Kenya.

All executives agreed that industry was under-investing, attributing this to market shrinkage, excess industrial capacity, the inability to access foreign exchange, and the high cost of securing new imported equipment. Views of future investment prospects were mixed, though most stressed the urgent need to refurbish and replace existing plant. Most thought that foreigners would be reluctant to invest unless and until they were given firm assurances in respect of property rights and indigenization proposals.

One multinational manager said that he doubted whether major multinationals would renew their interest in Zimbabwe: ‘The market is too small, it makes better sense to serve Zimbabwe from South Africa, or even as far afield as Kenya, using Common Market for Eastern and Southern Africa (COMESA) trade preferences’. He expected post-crisis Zimbabwe to attract corporate venturers and ‘buccaneer’ investors rather than mainstream multinationals like his own.

8.1.3 Constraints on recovery

Table 8.3, compiled from the 2007 CZI Survey of Manufacturing Industry, illustrates the two main constraints to short-term industrial recovery: access to foreign

exchange, and the partially overlapping problem of the difficulty of sourcing raw materials. The latter is only a partial overlap because it refers to the drying up of domestic sources of supply and not just imported inputs. Weak demand, both domestically and in export markets – adversely affected by the overvalued exchange rate for the Zimbabwe dollar – was identified as another major constraint to increased production.

Table 8.3: Major constraints on industrial production

	2006	2005
Foreign currency	69.4	79.7
Raw materials	58.9	70.9
Working capital	9.7	8.9
Demand	26.4	41.9
Power outages	8.3	6.3
Fuel availability	6.9	8.9

Source: *CZI Survey of Manufacturing Industry (2007)*

Interview evidence largely confirmed the survey findings, with one major difference – the rapidly deteriorating supply of technical and professional skills. Four major constraints stood out from the interviews:

- Policy uncertainty and unpredictability, especially in the fields of property rights, indigenization and pricing.
- Access to foreign exchange and raw materials, especially agricultural raw materials previously produced locally.
- Skills.
- Infrastructure – especially electricity, telecommunications, rail transport, roads and water.

8.1.4 Future strategy

Strategy for industrialization

Although on the surface it might appear that there are many similarities in the situation faced by manufacturing industry in post-

crisis Zimbabwe and those that existed both at independence and at the time of ESAP (1991), policy towards industry in the post-crisis era cannot be simply extrapolated from current and past performance.

In theory, post-ESAP deindustrialization since 1992 ought to have created the space for a revival in the manufacturing sector. In practice however, far-reaching structural change in the Zimbabwe economy, including the steep decline in domestic purchasing power and the contraction of large-scale commercial farming, has created a very different situation. In the past too, Zimbabwe could rely on a skills base unparalleled in sub-Saharan Africa, certainly in relative terms.

Unlike the situations in 1980 and 1990, there is substantial excess capacity in manufacturing, and while this will make it feasible to expand output very substantially without additional industrial investment, there are four serious drawbacks:

- A large – but unknown – proportion of the industrial capital stock is ageing or obsolete, expensive to operate, environmentally unfriendly, and well within technology frontiers, as a consequence of which productivity levels fall far short of state-of-the-art levels.
- A severe and rapidly worsening shortage of skills is raising operating costs while restricting the ability of firms to install and utilize state-of-the-art equipment.
- Infrastructural constraints – electricity, water, telecommunications, rail transport – are far more severe now than at any time in the post-Independence history.
- The announced commitment to an indigenization strategy – specifically targeting mining, manufacturing and finance – raises numerous questions concerning elements crucial to an industrial revival such as Foreign Direct Investment (FDI) and access to technology, brand names, patents and markets.

POST-CRISIS
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LAND
REDISTRIBUTION

Globally, the dynamics of industrial development have changed radically over the past twenty years, while in southern Africa, South Africa's strong resurgence from decades in the economic wilderness marks a major shift in regional dynamics. The emergence and rapid development of global – and, to a much lesser extent, regional – value chains has influenced the foreign investment strategies of multinational companies, who are much less inclined to invest in small markets, such as Zimbabwe, than was the case twenty years ago.

Moreover, while Zimbabwe's economy has been shrinking, those of its regional neighbours have expanded rapidly. The country that in 1980 was the second largest in Southern African Development Community (SADC) is now the second smallest, and the DRC is now the only SADC country where income per head is lower than in Zimbabwe.

At a time when manufacturing industry worldwide is becoming more skills- and knowledge-intensive, Zimbabwe has fallen behind technologically. In 1980 Zimbabwe was ranked 35th out of 93 countries in UNIDO's Competitive Industrial Performance (CIP) index,² just ahead of South Africa. By 2000 – the most recent figure available – Zimbabwe had slipped down the rankings to 57th position, while on the new enlarged CIP index for 2000, covering 155 countries, Zimbabwe was ranked 76th. Over the twenty-year period Zimbabwe's CIP index declined from 0.248 to 0.213, chiefly reflecting the decline in manufacturing's share of GDP and of manufactured exports in total exports.

Any meaningful strategy for the future of manufacturing industry must take account of these realities rather than assuming that an industrial sector, which at Independence in 1980 appeared to have considerable potential, will be able to pick up from where it left off in the late 1990s. Post-crisis policy-makers will need to factor into their strategies the fact that the Zimbabwe industrial model had run

out of steam well before the crisis created by land redistribution.

Because the world, the region and especially Zimbabwe itself have changed, the pre-crisis business model cannot be replicated in the 21st century. A post-crisis strategy must start with acceptance of this reality, acknowledging that the constraints on industrial policy, implicit in the new world order of the 21st century, are more restrictive than was the case during Zimbabwe's period of rapid industrialization, while the range of opportunities has changed, and quite possibly narrowed, flowing from the 'path dependence' implications of manufacturing evolution, especially since 1990.

8.1.5 The manufacturing sector from 2008

Assumptions

1. GDP growth will resume in 2009 following political changes in 2008 and a gradual normalization of relations with the international community.
2. Property rights will be restored and indigenization programmes rationalized.
3. Mining, construction and services will be the lead growth sectors of the economy, driven by investment in mining and infrastructure as well as foreign aid inflows.
4. Manufacturing will grow well above its trend rate as spare capacity is utilized, but industrial growth will be constrained by the shortage of skills, infrastructural capacity and domestic agricultural production.
5. Agriculture will restructure with the resumption and expansion of some large-scale commercial farming activities and growth of corporate farming, partly reliant on contract farming by small-scale producers.

² UNIDO, *Industrial Development Report*, 2004.

6. Growth in all sectors will be constrained by scarce skilled and unskilled labour with agriculture being most affected by the shift from a labour-surplus to a labour-scarce economy.
7. Manufacturing will restructure over the medium term as foreign direct investment revives.
8. Industry restructuring will be substantially influenced by regional economic integration, including the establishment of a free trade area in the SADC region.
9. Entry by major multinationals is unlikely but FDI by middle-rank multinationals, mostly from South Africa and Asia is probable.
10. Manufacturing value-added will continue to decline relative to gross output reflecting increased reliance on imported inputs and a dilution of linkages with domestic agriculture.
11. Government policy will prioritize Small and Medium Enterprise (SME) development in all sectors.
12. Initial official efforts to revive Export Processing Zones and rural growth points will eventually dissipate.

Scenarios for industrial development in the post-crisis era cannot be simply extrapolated from current and past performance for three main reasons:

1. First, the extent to which the economy over-industrialized during the period of industrial autarky (1965 to 1990) highlights the fact that Zimbabwe did not follow a typical developing country industrialization path. It is therefore essential that in the post-crisis environment, policymakers should learn from the mistakes of the past, graphically

illustrated in the IMF's Country Study of Zimbabwe in its 1998 ESAF Evaluation Report.

2. Because Zimbabwe's industrial structure at the start of the 1990s was 'peculiar', economic reform in Zimbabwe was 'more analogous to that in the transition economies than in the rest of Africa'. This was because the industrial autarky regime had given birth to a 'very large and diversified industrial sector serving largely the domestic market'.³

As should have been appreciated at the time, the ESAP reforms were substantially responsible for the steep 18 percent decline in MVA between 1991 and 2000, while the strong growth in manufactured exports generated by economic liberalization quickly ran out of steam reflecting exchange rate overvaluation, the ongoing scarcity of foreign exchange and mounting investor unhappiness at the slow, but inexorable, policy reversals, in particular, from 1997/8.

This failure of ESAP industry policy was doubly unfortunate. Not only did it discredit economic liberalization in the eyes, not just of government but of many in the private sector, but it strengthened the hand of those demanding increased state intervention in the economy, starting with land resettlement and direct management of the exchange rate and the country's foreign currency earnings.

3. On the surface it appears that there are many similarities in the situation faced by manufacturing industry in post-crisis Zimbabwe and those that existed at independence in 1980 and at the time of ESAP (1991). In theory, post-ESAP deindustrialization since 1992 ought to have created the space for a revival in the manufacturing sector.

³ IMF: Zimbabwe Country Study for ESAF Evaluation Report. Jan 1998 (page 171)

In practice, however, far-reaching structural change in the Zimbabwe economy, including the steep decline in domestic purchasing power and the decline, if not the demise, of large-scale commercial farming, has created a very different situation. In the past too, Zimbabwe enjoyed a labour-surplus economy, which is no longer the case.

8.2 THE MINING INDUSTRY

8.2.1 Introduction

Because the bulk of output serves export markets, the mining industry is less susceptible to the vagaries of domestic economic policy than manufacturing. Globally, corporate decisions to invest in mining exploration and development are driven by demand, cost and market considerations rather than by changes in government policies, though legislation limiting the extent of foreign ownership influences exploration and investment decisions adversely. Although there has been a resurgence of resource nationalism internationally since the onset of the primary commodities price boom in 2002/3, mining companies have become less risk-averse and more willing to invest in politically fragile locations because resources are short and prices are high.

For most of the post-Independence period in Zimbabwe exploration and investment were constrained by sluggish world markets for primary metal products. At the same time, during the control regime period (1980–1990), mining development was hampered by industry perceptions of official hostility to FDI, and specifically to foreign ownership, allied with viability concerns attributable to the government's commitment to a controlled and over-valued exchange rate. Accordingly, with depressed metal prices in international markets, the incentive to invest in Zimbabwe was muted.

Two events improved the exploration and investment environment for mining in the

1990s. ESAP promised a more competitive exchange rate, less state intervention and a more hospitable investment climate. Secondly, the discovery of rich platinum-group metal deposits – second only to South Africa in known reserves – and subsequently of diamond deposits, attracted the attention of both mining majors and juniors around the world.

Unfortunately, the high hopes associated with ESAP were short-lived. Far from fostering a more hospitable investment climate for mining companies, government policy moved initially towards the negotiation of mining leases on a case-by-case basis – as with BHP-Billiton's abortive Hartley platinum venture, now Zimbabwe Platinum, owned by Impala Holdings of South Africa – and subsequently to new ownership and fiscal regimes for mining, partly captured in the 2007 Mines and Minerals Amendment Bill that has since lapsed.

Because this coincided with the present commodity-price supercycle since 2002, investor interest in Zimbabwe's mining potential actually increased, despite the serious deterioration in the country's political-risk profile, its macroeconomic policy stance and the threatened compulsory sale of 51 percent of the shares of mining companies.

8.2.2 Current situation

The official volume-of-production index compiled by the Central Statistical Office (CSO) depicts a stagnant industry, with the volume of mining output having peaked in 1998. Although production stagnated over the 1980–2004 period – growing just 0.32 percent annually because prices (measured by the unit value index) grew 47 percent a year – the Zimbabwe-dollar value of production increased dramatically, driven by currency devaluation, particularly since 2000.

Data from the Chamber of Mines show a very different picture, with output peaking more recently (2003), driven by strong volume growth in low-value base minerals

Table 8.4: Mining production (1980–2004)

Period	Volume index average	Growth rate (% p.a.)	Unit value index average	Growth rate
1980–1989	92	+0.65	51.00	+13.00
1990–1999	108	+1.23	390.00	+26.00
2000–2004	95	–1.11	79,534.00	–
1980–2004	100	+0.32	16,083.00	+47.00

Source: Central Statistical Office, Harare

(limestone, black granite, quartz and chromite), but this production has since declined steeply with the result that, by 2006, the volume index was only half its 1980 level.

The volume figures show that, with the exception of platinum, production in 2006 was well below peak levels. Gold output, which peaked at 27.1 tons in 1999, had fallen back to its 1980 levels by 2006 and in 2007 declined further to 6.8 tons – its lowest level in more than a century. In the first quarter of 2008 gold production declined even more dramatically, while asbestos output has slumped more than 60 percent from peak levels, nickel production is down 42 percent and coal 60 percent.

The structure of the mining industry has changed radically since 1980, with a decline in the number of mines and an associated fall in the output and employment shares of small mines. In 1979 over half the mines (105

out of 200) employed no more than 50 people; by 1995, this number had fallen to 33 (35 percent of the total). Output has become increasingly concentrated in the hands of large producers so that by 1995, 17 mines (18 percent of the total) with upwards of 500 workers each accounted for almost 86 percent of employment compared to a third in 1979.

Anecdotal evidence suggests that since the mid-1990s the trend towards a concentration of activity in the hands of medium- to large-scale mines has intensified at the expense of the ‘missing middle’⁴ in the form of small- to medium-scale formal mining operations. At the same time, there has been an explosion in the number of informal-sector artisanal miners, though there are no statistics because their operations are essentially illegal in that they are outside both the tax and currency-control nets. Recently (2006/7) it appears that there has been a

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FORM OF SMALL-
TO MEDIUM-SCALE
FORMAL MINING
OPERATIONS

Table 8.5: Main commodities (% share by value)

	1980	1990	2000	2006
	% share by value			
Gold	36.6	38.6	51.6	27.9
Asbestos	17.7	11.0	16.0	2.4
Nickel	14.0	18.0	4.7	17.9
Chromite	4.7	4.6	4.6	7.6
Coal	7.0	12.4	14.0	5.9
Ferrochrome	n.a.	n.a.	n.a.	14.8
Platinum-group metals	n.a.	n.a.	4.4	21.7
Total	80.0	84.6	95.3	98.2

Note: Items do not add up to 100% because other minerals are excluded.

Source: Chamber of Mines of Zimbabwe

⁴ See chapter 6 on private sector development

sharp decline in such artisanal activity, reflecting operational difficulties (access to inputs), increased efforts to control black-market activities by the authorities, and technical mining problems. Specifically, in the last few years, informal-market miners have exploited the ‘easiest’ gold-panning and alluvial-diamond opportunities. Today more capital and know-how is needed and, because these are often not available, industry sources believe that artisanal activity, certainly in gold, has peaked for the time-being.

Mining’s chief contribution to the economy, especially in recent years, has been its capacity to generate foreign exchange, even with falling output. Since independence in 1980, mining has accounted for almost 40 percent of total exports, dominated by gold, with the other important contributors being ferrochrome, nickel and latterly, platinum, which will shortly become the country’s major export. Since the start of the commodity boom in 2002, the share of minerals in total exports has averaged 45 percent. The recent growth in the share of mineral exports in the total reflects the decline of agricultural and manufactured exports as well as the post-2002 surge in metal prices that has offset substantially falling production volumes.

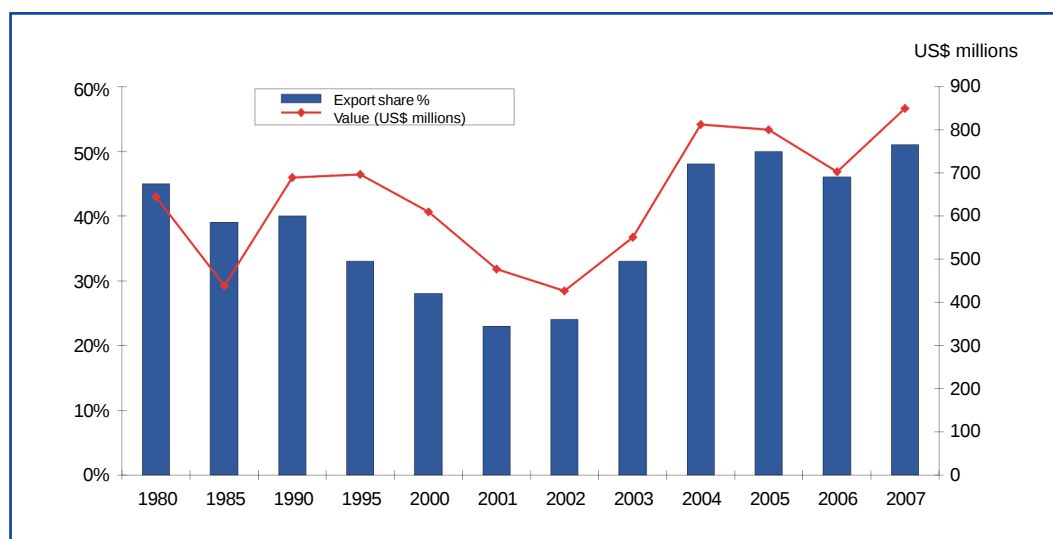
8.2.3 Employment and skills

Chamber of Mines data show that, after falling by a third between 1980 and 2000, employment has since recovered and is now some 25 percent (14,000 jobs) higher than at independence. However, this is entirely due to the quadrupling of employment in smelting and refining. Zisco, a loss-making parastatal, accounts for 30,400 jobs (86 percent of employment) in these industries, and it has increased nearly six-fold since 1980, despite a collapse in output over the period. The figures exclude informal/artisanal mining activities for which there are no hard output or employment data.

The Chamber estimates that more than half the industry’s skilled personnel emigrated from the country in 2007 and that in early 2008 there were 1,116 vacancies for professional and technical staff. In an unpublished report for the Zimbabwe Chamber of Mines (August 2007), Prof. Keith Viewing paints a picture of a severe and rapidly worsening skills shortage, exacerbated by the precipitous decline in the country’s capacity to regenerate skills.

Citing data provided by nineteen mining companies, Prof. Viewing estimates graduate vacancies to be between 166 and 233, including 48 mining engineers, 28 geologists,

Figure 8.2: Value of mineral exports and share in total, 1980–2007



Sources: Central Statistical Office, Harare, the IMF and the Reserve Bank of Zimbabwe

30 metallurgical engineers, 34 mechanical engineers, 12 electrical engineers, 5 surveyors and 7 in metallurgical assay. Vacancies for technicians are estimated at over 700, excluding the iron-and-steel sector, the cement industry and Chemplex, which produces critical chemicals and explosives used in mining.

The number of university graduates needed in mining disciplines is estimated to be between 480 and 550, but the maximum capacity of mining-related departments at the University of Zimbabwe (UZ) is 124 students per year, meaning that it will take four to five years to supply existing needs, let alone provide for the anticipated recovery and growth of the industry in a post-crisis environment.

A survey undertaken by the government, the National Human Resources Survey (2006) concluded that as many as 70 percent of 1,519 graduates surveyed indicated a wish to emigrate – 76 percent for graduates and 86 percent for postgraduates. UZ itself estimates that, of 2,800 students who graduate each year, only about 700 wish to stay in Zimbabwe.

The Viewing report sets out a number of detailed proposals for remedying the situation, virtually all of which require substantial injections of funding, both in local and foreign currency, as well as the normalization of relationships with the international community so that many more Zimbabwean students can be trained abroad, more expatriates recruited, and there can be increased resort to inter-company transfers. The unequivocal message of his report is that the shortage of skills will be a binding constraint on mining exploration, investment and development in the future.

8.2.4 Mining exploration and investment

The primary criteria influencing mining investment are mineral potential and

infrastructure, according to a World Bank survey (1992). The survey of forty international mining companies from North America, Europe, Australia, South Africa and Japan found that a guarantee of mining rights before starting exploration was ‘an essential precondition’. Other critical factors are a well-established mining code, contractual stability, profit repatriation, a guaranteed fiscal regime and access to foreign exchange. Accelerated depreciation and amortization and realistic exchange rates are important but ‘less essential’.

The survey found that respondent companies were generally not prepared to work in countries with mandatory local-majority participation, either government or private, though some companies saw minority-local participation and mandatory training of nationals as positive factors. Mandatory provision of social services, restrictions on wage negotiations and limitations on expatriate personnel were ‘minor disincentives’.

There is greater concern about political risk and corruption than about macroeconomic stability because mining projects are export-oriented and partially de-linked from the domestic economy. Higher risk premiums are required to justify investment in emerging markets, with an average return on equity of 25 to 30 percent and a payback period of 2 to 4 years compared with a return of 20 percent and a payback period of 5 to 6 years in industrial economies.

While mining houses are confident of being able to cope with market and technical risks, they have concerns about three main areas of political risk:

- Restrictions on a company’s ability to do business – obtaining exploration and mining rights, securing ready access to foreign exchange, being allowed to export directly rather than through a state-owned market authority, and the risk of losing mining rights or legal title as a consequence of host government action.

- The ability to control costs and maintain competitiveness: the risk of unilateral changes to the tax regime; the risk of price-control imposition or controls on inputs or output; the requirement that companies undertake marginal value-adding investments that may not be profitable; the requirement to carry out infrastructure or community or social investments not prescribed in the original investment agreement; and the risk of employment quotas set by the state.
- Ready access to foreign exchange to finance inputs and offshore payments for management fees, debt service, capital repayments and dividends.

Geological assessments suggest that underinvestment in exploration and production and not mineral potential have been the main factors limiting mining development in Zimbabwe. This is not a new phenomenon and pre-dates the onset of the political and economic crisis at the end of the 1990s. In 1992, the World Bank identified Zimbabwe, along with the DRC and Namibia, as 'Category A' countries⁵ requiring the highest level of exploration investment amongst African states of US\$100 million over a five-year period (\$20 million annually). In all three countries mining exploration had been constrained by political and economic uncertainty, with mining houses reluctant to invest in a country with a track record of policy unpredictability, especially in terms of property rights and exchange-rate management.

However, while the mining investment climate has improved in most African countries over the last decade, the opposite has been the case in Zimbabwe, as underlined in the Fraser Institute Annual Survey of Mining Companies.⁶ This shows that, since its first inclusion in 2002, Zimbabwe's position in its Policy Potential Index⁷ has deteriorated dramatically, both in absolute and relative terms. Zimbabwe's scores of 2 (2006) and 3 (2007) – a decline of 86 percent since 2002 – are the two lowest scores recorded for any jurisdiction since the launch of the survey in 1997.

Contemporaneous data (since 1997) on gross capital formation by sector are not available, but figures for the 1973–1996 period show investment in mining averaging 25 percent of output (both at current prices). However, these figures are seriously distorted by the abortive BHP Hartley Platinum project in 1995/6,⁸ as a result of which the investment-output ratio rose steeply from a 26-year average of 15.6 percent to 25 percent, because of investment of 44 percent of gross output in 1995 and 47 percent in 1996.

Were contemporary data available, they would show a steep decline in mineral investment since the late 1990s, with very few new projects, other than in platinum, and falling exploration expenditure, especially since 1998. Over the long haul, since 1968, the investment to gross-output ratio is estimated at between 10 and 12 percent.

⁵ The World Bank (1992) report defined a Category A country as one requiring exploration spending of US\$20 million a year for five years.

⁶ See <<http://www.fraserinstitute.org>>.

⁷ The Policy Potential Index is a composite index measuring the overall policy attractiveness of the 65 jurisdictions in the most recent survey (2007). It measures the effects on mining exploration and investment of government policies including uncertainty concerning the administration, interpretation and enforcement of existing regulations; environmental regulations; regulatory duplication and inconsistencies; taxation; uncertainty surrounding indigenous land claims and protected areas; infrastructure; socioeconomic agreements; labour issues; the geological database; political stability and security.

⁸ Australian mining group BHP Billiton invested an estimated US\$450 million to develop the Hartley Platinum Mine. The project ran into a number of technical problems and was subsequently abandoned. The mining property and assets were sold to Zimbabwe Platinum (Zimplats).

Assuming a very conservative depreciation factor of 10 percent, the industry's capital stock peaked in the early 1980s. The capital stock increased substantially during the 1970s, followed by a decline and then a marked recovery when platinum investment took off in the mid-1990s. Although there are no data for the post-1997 period, mining companies say that, outside the platinum and diamond sectors, investment in both exploration and new capacity has been minimal, with no new exploration licences being issued since 2003 despite the fact that companies had applied for new exclusive prospecting orders.

In sum, because both production and investment have declined, the industry is in an 'immature' state, which means that above-normal levels of investment in both exploration and productive capacity will be required during the post-crisis period.

8.2.5 Constraints on mining development

- *A difficult, indeed increasingly hostile, business environment:* Since the late 1990s the operating environment for mining companies has become increasingly uncertain, with question marks over the royalty and tax regime, exchange-rate management and most recently, the ownership regulations. A Bill tabled in Parliament in 2007 required foreign-owned mining companies to divest 51 percent of their equity stakes to indigenous Zimbabwean investors.⁹ Of this, 25 percent must be allocated to the state, which will pay for its stake in the mines from future dividends. However, this Bill has since lapsed, but it remains the intention of the present government to reintroduce it in the next parliamentary session.

- *Deteriorating physical infrastructure:* Erratic availability of electricity and of rail transport has hindered production and increased operating costs.
- *Scarce foreign exchange:* Restricted access to foreign currency has stifled new and expansion investment projects and increased downtime on the mines, thereby undermining productive efficiency and raising operating costs.
- *Exchange-rate mismanagement:* The long-run strategy of maintaining an over-valued exchange rate has deterred new investment and curbed output growth.
- *The skills exodus:* With mining skills in scarce supply internationally, Zimbabwe has become a substantial exporter of skilled mining personnel – geologists, engineers, technicians and managers.
- *Declining international competitiveness:* The combination of rapidly rising operating costs, deteriorating infrastructure, scarce skills and an over-valued exchange rate has undermined competitiveness.

BECAUSE MINERAL RESOURCES ARE BEING DEPLETED, IT IS ESSENTIAL THAT SOME OF THE PROCEEDS OF MINING ACTIVITY ARE RECYCLED INTO INVESTMENT IN PRODUCED ASSETS, SUCH AS INFRASTRUCTURE, AND INTANGIBLE CAPITAL

8.2.6 Strategy for mining development

Mining should be treated differently from other sectors for two main reasons:

- Because mineral resources are being depleted, it is essential that some of the proceeds of mining activity are recycled into investment in produced assets, such as infrastructure, and intangible capital.¹⁰
- Mining sector projects are unique in a number of respects, and this justifies an industry-specific policy regime, especially as regards taxation.

⁹ Mines and Minerals Amendment Bill [H.B. 14, 2007] Gazetted 16 November 2007.

¹⁰ Intangible capital is accumulated investment in people in the form of education, training, skills development and health facilities as well as investment in institutions, management systems and research and development.

IT COULD EASILY
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SINGLE
CONTRIBUTOR TO
EXPORTS BY SOME
DISTANCE, AND AN
IMPORTANT
SOURCE OF PUBLIC
REVENUE

A strategy for mining in post-crisis Zimbabwe should take into account five main considerations:

- Fostering investment, both domestic and (especially) foreign in major projects.
- Encouraging investment in value-added operations that will increase both export revenues and mineral rents.¹¹
- Ensuring that mining rents are mobilized by the state for investment in produced assets and intangible capital, thereby ensuring that wealth per capita is not eroded by resource depletion.
- Providing an appropriate social environment in terms of worker welfare, including health and safety considerations.
- Environmental protection.

This is a classic trade-off situation in the sense that policy measures adopted to foster investment limit the scope and extent of measures aimed at maximizing mineral rent collection by the state.¹² Similarly, social and environmental policies are likely to reduce the return on capital invested, thereby possibly deterring investment and reducing mineral rents. However, by establishing a clear and stable mining policy regime, the state can improve the investment environment, thereby lowering the risk premium and returns required by mining houses, lenders and investors.

All of this means that a mining strategy must take the form of a delicately balanced compromise between the measures taken to achieve the five goals outlined above. Policies change with global market conditions. Recently, as foreign direct investment in resource industries around the world has increased, so policies have become

increasingly nationalistic. The bargaining power of resource-rich countries has increased relative to that of mining exploration and development companies.

Mining companies, especially foreign groups who are long term players, need to be able to take a 10- to 20-year view, possibly longer. They are understandably wary of obsolescing bargain considerations, illustrated by the dispute between Zambian mining companies and the government, which raised taxes to extract the windfall rents flowing from record copper prices.

For their part, governments prefer flexibility because as recent global experience shows all too clearly, the mining industry is susceptible to boom-and-bust pressures, reflected in underinvestment in the 1980s and 1990s resulting in a price boom since 2002 and in all probability, overshooting of both prices and investment in new capacity.

Available geological evidence suggests that Zimbabwe is unlikely to become a minerals-driven economy in the same way as Botswana, Zambia or the DRC. This is because Zimbabwe is a minerals-diverse economy as distinct from a minerals-rich one, which in turn means that some, perhaps much, of the scope for mining investment lies in small to medium projects rather than in the mega-projects characteristic of the DRC, Zambia or South Africa. But, given appropriate business-friendly policies, the mining sector could – indeed, should – reverse the decline of the last twenty years. It could easily become the fastest-growing sector of the economy, the largest single contributor to exports by some distance, and an important source of public revenue to be used not to finance government consumption spending but job creation, diversification of the economy and poverty reduction efforts.

¹¹ Mineral rents or mining rents are defined as the surplus earned by a particular factor of production, such as capital or labour, over and above the minimum earnings necessary to induce that factor to do its work. Such rents arise from the scarcity of minerals like gold, diamonds or platinum, from windfalls due to sudden price increases, from monopolistic profits earned by a company able to corner the market (as in diamonds) from locational advantages (a mine being well situated to supply a nearby market), etc.

¹² Mineral rent collection refers to the use of taxes or royalties by governments to secure a share of surplus earnings (rents).

8.2.7 Mining industry prospects

Mining is seen by some as the sector most likely to drive Zimbabwe's economic recovery. There are three major snags to this thesis – the first is that the industry has missed out on the current commodity boom. Exploration spending will resume at a time when the global industry may well have entered a consolidation phase, while expansion will be seriously constrained by the global scarcity of mining industry skills.

The second concerns the lengthy gestation period of mining projects, especially in an environment where exploration spending has been abnormally low. When account is taken of infrastructural, financial and 'sentiment' constraints, it is likely to take a minimum of three to five years to bring new projects on stream.

The third is that mining accounts for no more than 5 percent of GDP. While its expansion will help to ease Zimbabwe's severe balance-of-payments constraint, it is unlikely to have a major impact in terms of direct employment and direct poverty reduction. Its main contributions will be foreign currency and inward foreign direct investment, assuming the adoption of investment-friendly policies and tax regimes.

These drawbacks notwithstanding, the potential does exist for a rapid rebound, mostly as a result of increased utilization of spare capacity. Due to energy and foreign currency constraints and erratic exchange-rate policies, the country's largest gold producer is operating at 16 percent capacity. Many other small producers are in a similar position and could increase production over the short term.

Zimasco which earns in the region of US\$200 million annually in foreign exchange has already embarked on a US\$30 million expansion project which will boost output and exports. Rationalization and regularization of diamond operations would channel funds currently being sold through informal and illegal channels into the formal banking sector. Similarly, coal and coke production

would be re-activated. Taken together these – and other – short to medium term measures will improve foreign currency earnings significantly and help bridge the gap before longer-term projects, especially but not only in platinum, are brought on stream.

8.3 TOURISM

8.3.1 Introduction

Tourism is a relatively new player in the Zimbabwe economy coming to prominence only after the economic reforms of the early 1990s. In 2006/7 its contribution to GDP was officially estimated at 4 percent, while it accounts for some 13 percent of foreign currency earnings, with a net contribution of 5 percent after adjusting for tourism-related imports. Since 2003, tourism's share of formal sector employment has averaged 6 percent.

Tourism contributes significantly to economic growth through the linkages with other industries such as agriculture, manufacturing and services. Backward linkages are by far the more important reflecting the industry's role as a purchaser of goods and services from other sectors, though these have weakened in recent years as the industry's import propensity has risen alongside declining domestic productive capacity. Typically, in tourism, forward linkages are modest.

8.3.2 Current situation

Although the Zimbabwe Tourism Authority (ZTA) established by the government as a promotional and regulatory authority collects and publishes a broad range of tourist statistics, their reliability has been called into question, especially recently when some of the data point to a strong industry-wide upsurge that is not reflected in most other indicators.

Tourism earnings stagnated during the 1980s, averaging some US\$40 million annually but

the industry took off in the first half of the 1990s benefiting from the ESAP reforms, especially in the field of exchange-rate management. Figure 8.3 shows foreign currency earnings trebling between 1990 and 1996/7, which were the peak years with earnings in excess of US\$200 million. Thereafter, as political problems proliferated and exchange and currency controls were reimposed and tightened progressively, earnings fell steeply to below US\$61 million by 2003 (Chart 1).

Revenue estimates for 2004/07, excluded from Figure 8.3, show a remarkable and inexplicable surge in revenues that conflicts with other data, including balance-of-payments figures and hotel occupancies. It is not obvious whether this is the result of exchange rates used for conversion purposes or whether it takes the form of diaspora and trading income declared as spending by tourists.

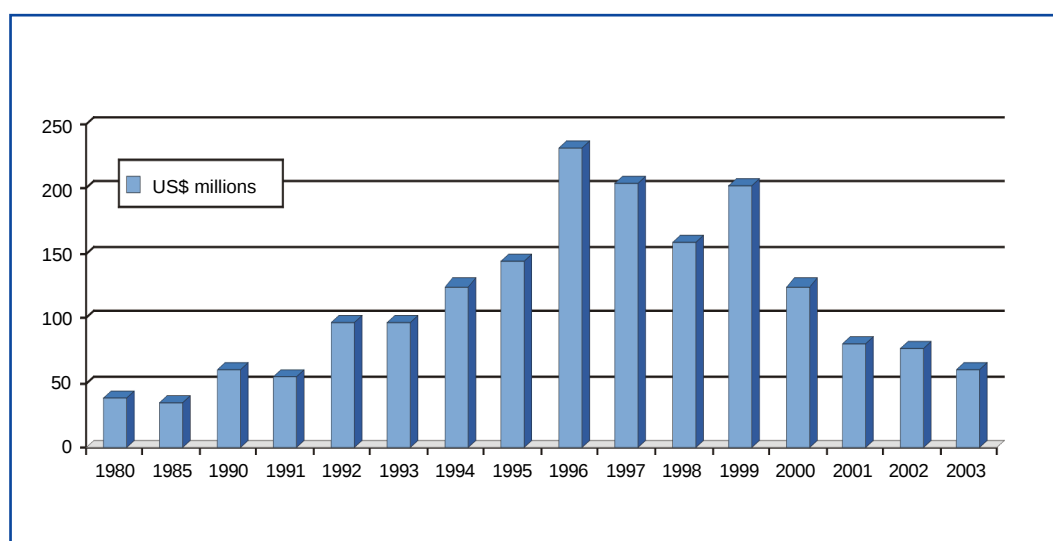
Whatever the explanation hotel occupancy and average spend data as well as the reports of hotel and tour operators suggest that the ZTA revenue statistics are substantially inflated. Room occupancy figures show that in 2007, when revenue was estimated at US\$365 million, occupancies averaged 43 percent, less than in 2003/4 (44.5 percent)

when revenues averaged US\$127 million. Similarly, bednights sold declined 18 percent over this period from 39 percent utilization to 32 percent and while tourist arrivals increased 11 percent between 2003 and 2007, tourism receipts are said to have increased sixfold. A further inexplicable statistic is the reported decline in the industry's workforce between 2004 and 2007, at a time when both arrivals and revenues were reportedly rising strongly. For these reasons, the published data, especially for recent years, must be treated with extreme caution.

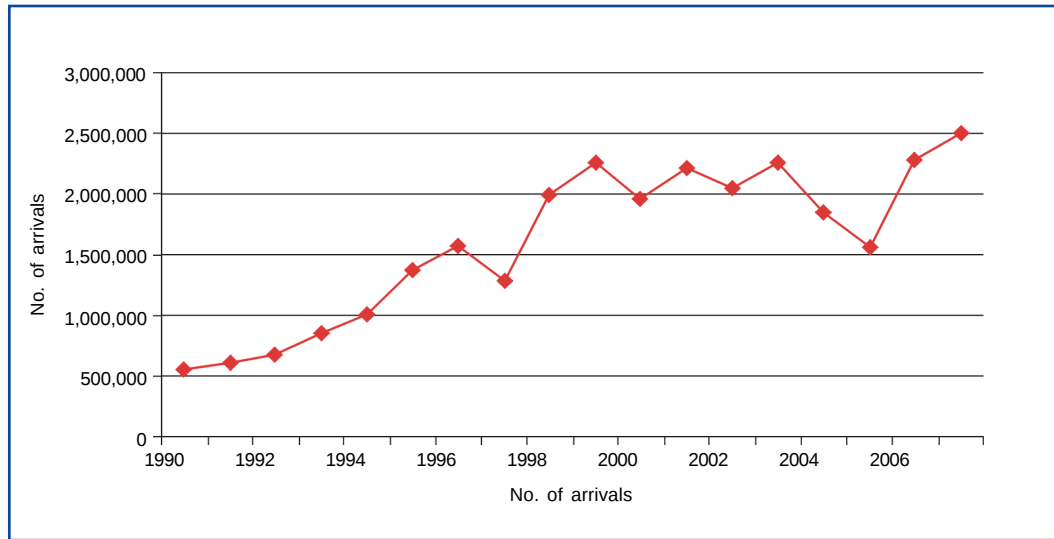
Figure 8.4 shows the trend in tourist arrivals in Zimbabwe during the period 1990 to 2007 while Table 8.6 provides an analysis of tourist arrivals, demonstrating that over half of total arrivals is classified as 'visiting friends and relatives' rather than paying tourists in the sense of staying at hotels or lodges and visiting tourist attractions. Only 27.7 percent of the arrivals in 2007 (25.8 percent in 2006) indicated that they were on holiday.

Room occupancy rates underline the changing structure of the industry. In 2007, domestic tourists accounted for 89 percent of the total reflecting the steep decline in foreign visitors. Far and away the most important reason for this is the country's poor

Figure 8.3: Zimbabwe: Tourist earnings 1980-2003 (US\$ millions)



Source: Central Statistical Office, Harare

Figure 8.4: Trend in tourist arrivals in Zimbabwe, 1990-2007

Source: ZTA (2007)

Table 8.6: Tourist arrivals by purpose for visiting, 2006 & 2007

Purpose	2007	2006	% change	% of total 2007	% of total 2006
Holiday	695,044	589,929	18	27.7	25.8
Visiting Friends & Relatives	1,411,151	1,197,734	18	56.2	52.4
Business	361,707	363,531	-1	14.4	15.9
Education	17,005	29,064	-41	0.7	1.3
Shopping	11,308	62,728	-82	0.5	2.7
Other	12,040	43,586	-72	0.4	1.9
Total	2,508,255	2,286,572	10	100.0	100.0

Source: Calculated from ZTA (2007)

image internationally and, since the advent of the crisis, the proliferation of country Travel Warnings that has decimated the tour operator business. When national governments issue the most severe travel warnings (Level One or Two), insurance cover is withdrawn and tour operators pull out of the market.

This bodes well for future prospects because it means that once the political and economic situations normalize, travel warnings will be withdrawn and international tourism will revive, especially from countries where Zimbabwe's political travails have been closely followed. Such countries include the UK, which until recently was Zimbabwe's largest international market along with Germany, the Nordic states, Australia and New Zealand.

8.3.3 Source markets

The Zimbabwe tourist market is a three-tiered one – domestic, regional and international. The international market, traditionally by far the most lucrative, has shrunk during the crisis period, leaving the other two tiers to take up the some of the slack. Ostensibly, the regional market has grown – in 2007 African arrivals accounted for over 91.3 percent of the total – but, as the depressed room occupancy numbers show, many of these are not tourists in the accepted sense of the word but people from the diaspora visiting relatives, business-people, shoppers, day-trippers, those in transit and those attending educational institutions. Of the 3.34 million arrivals in 2006, 56 percent were holidaymakers, 28 percent were in transit, 12.5 percent

Table 8.7: Source markets (1996 and 2006)

Region	1996 number	1996 % share	2006 number	2006 % share
South Africa	572,000	35.8	1,612,000	67.0
Zambia	448,500	28.1	150,400	6.2
Botswana	n.a.	n.a.	105,360	4.4
Mozambique	161,200	10.1	76,350	3.2
Malawi	n.a.	n.a.	88,600	3.7
UK and Ireland	85,000	5.3	21,600	0.9
North America	38,700	2.4	36,630	1.5
Australia-NZ	36,100	2.3	20,560	0.8
Other Europe	147,000	8.7	78,300	3.2
Asia	21,400	1.3	36,500	1.5
Other Africa	77,000	4.8	171,000	7.1

Source: CSO Harare

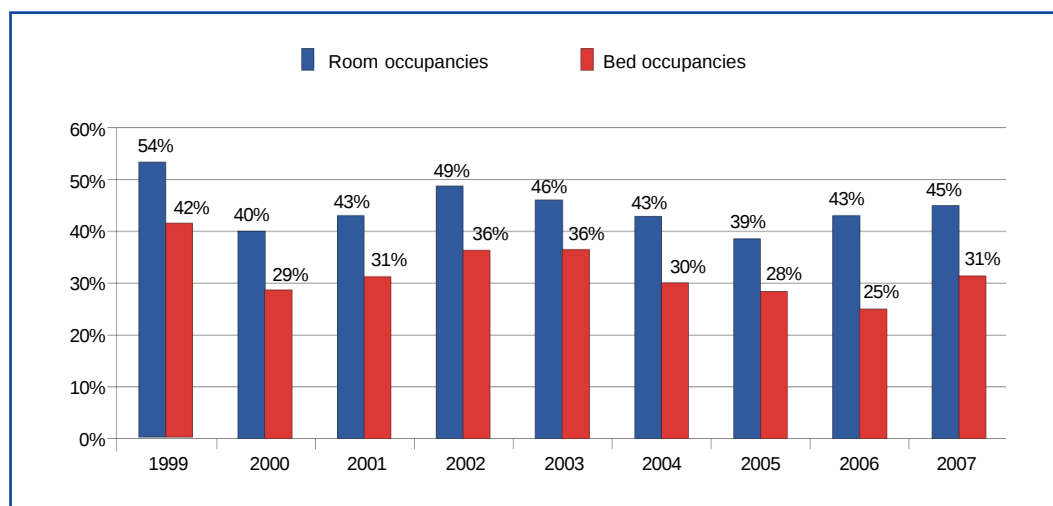
business visitors, and the balance of over 3 percent came for education or to shop.

Regional arrivals are predominantly South African – two-thirds of arrivals, excluding transit visitors and day-trippers – while another 18 percent came from Zambia, Botswana, Malawi and Mozambique. The US is the largest single international market (1.5 percent) followed by the UK and Ireland (1 percent). Ironically given all the publicity attached to the Look East policy of tourist promotion, the numbers have fallen some 40 percent from their peak in 2003 and the total Asian share is 1.5 percent, of which a third is from Japan and quarter from China and Hong Kong.

The steepest declines are from the Organization for Co-operation and Development (OECD) markets – the UK, continental Europe, Australia and New Zealand – where sensitivities about political events in Zimbabwe are greatest. The North American market has held up, partly reflecting the popularity of hunting – also popular with visitors from Spain, Portugal and Italy.

Room occupancy (bed occupancy) at 45 percent (31 percent) in 2007 is below the level of 54 percent (42 percent) achieved in 1999, and the industry now relies heavily on the domestic market, which in 2007 accounted for 89 percent of occupancies, compared with 11 percent for foreign visitors. This applies to all the Zimbabwean tourist resorts except the

Figure 8.5: Trend of room and bed occupancy, 1999-2007



Source: ZTA (2007)

Victoria Falls, where foreigners constitute 78 percent of the clientele (ZTA, 2007). Another adverse impact of the crisis is reflected in the deteriorating trend in the tourism receipts, particularly between 1999 and 2003 and 2005 (ZTA, 2007).

8.3.4 Administration

Tourism policy and policy formulation falls under the Ministry of Environment and Tourism, while policy implementation rests with the Zimbabwe Tourism Authority (ZTA). The latter was established by the Tourism Act of 1995. ZTA has also assumed extra responsibilities which include collection of tourism levies, the registration, grading and inspection of tourism facilities.

The Authority's main brief is to implement tourism policy as enunciated by the parent ministry with due regard for environmental and ecological issues, the marketing of Zimbabwe as a tourist destination, the promotion and establishment of standards, training, and human resource development. In recent years however, the ZTA has increasingly become control-oriented rather than an industry facilitator to the point where ZTA approval is required for a tour operator to import a new motor vehicle.

Two steps are necessary, one of which, the strengthening of the private sector Zimbabwe Council for Tourism and its transformation into a Tourism Business Council along the lines of the successful Business Council in South Africa, is already underway, the second is the restructuring of the ZTA itself. The ZTA needs to revert to its core business – marketing and promoting Zimbabwe as a tourist destination, managing hotel standards and cooperating with other stakeholders in the provision and upgrading of training facilities

8.3.5 Private sector services

Zimbabwe's tourism development is the prerogative of the private sector, with government mainly playing a regulatory role. The private sector provides the various

services such as accommodation, touring, entertainment, transport, catering, etc. The various sub-sector associations representing the diverse interests in the sector include: the Hotel Association of Zimbabwe (HAZ), the Zimbabwe Association of Tour and Safari Operators (ZATSO) and the Association of Zimbabwe Travel Agents (AZTA). The umbrella body of the various sub-sector associations in the industry is the Zimbabwe Council for Tourism, soon to be converted into the Tourism Business Council.

8.3.6 Competitiveness

Although Zimbabwe's tourism potential is not in doubt, currently it fares very poorly in terms of competitiveness with the 2008 Travel and Tourism Competitiveness Report (World Economic Forum, 2008) ranking the country 117th out of 130 countries. The report describes this as 'a low ranking for a country with such natural endowments such as the famous Victoria Falls. Indeed, Zimbabwe is ranked 33rd for natural resources overall, with a number of World Heritage natural sites, much protected land area, and rich fauna'.

But despite these strengths, the country has an extremely low overall ranking – well below that of regional competitors such as South Africa (60), Botswana (87), Tanzania (88), Namibia (93), Kenya (101) and Zambia (107). The World Economic Forum says this highlights Zimbabwe's weaknesses in all other areas assessed. Its policy environment (128) is amongst the worst in the world and it is ranked bottom for both law related to foreign direct investment and property rights. Safety and security are 'major concerns' (123) as are health indicators (128). The report concludes that better governance 'is imperative to get the country back on track for improved Travel and Tourism Competitiveness'.

8.3.7 Strategy and structure

Zimbabwe has never been a standalone tourist destination for long-haul international

THE ZTA HAS
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TOUR OPERATOR
TO IMPORT A NEW
MOTOR VEHICLE

tourists though it is one for regional visitors from nearby countries. It is part of the Southern African market and along with Botswana, Namibia and Zambia, is an 'add-on' for overseas visitors to South Africa, with Johannesburg as the regional hub.

Typically in the past, international, as distinct from regional, tourists would fly into Harare and then spend approximately six to eight days in the country, visiting Zimbabwe's premier tourist attractions at Kariba, the Victoria Falls and – sometimes – Bulawayo and Great Zimbabwe. There was also a number of niche markets ranging from golfing tours, especially to Nyanga and the Falls, canoeing on the Zambezi, houseboating on Lake Kariba as well as hunting and photographic safaris.

Since 2000 the industry structure has evolved with the Victoria Falls taking on the mantle of the Zimbabwe tourist hub, partly because in its post-2000 marketing strategy the industry set out to deliberately rebrand the Victoria Falls as a standalone destination, not tarnished by political events in the rest of the country. In the process, Harare lost its hub role – though many business visitors to Harare still visit the Falls. Because it is by far Zimbabwe's most important – and most profitable – tourist attraction, the Victoria Falls has managed to avoid much of the adverse publicity that has tainted the rest of the country.

Despite this, the Victoria Falls has lost substantial market share to Zambia, but Zambia is not as attractive a location in terms of actually viewing the Falls and Zambian hotels and tour operators have sought to exploit this political market windfall by raising hotel tariffs to the extent that the Zimbabwe industry is convinced that given a level playing field politically it will quickly recapture its lost markets.

Unfortunately, infrastructure, especially air travel capacity, poses a serious snag to this optimistic scenario underlining the necessity for expanding and revamping the Victoria Falls airport. On a cost competitiveness

basis, even with hyperinflation, Zimbabwe remains a relatively cheap destination, certainly when set against Kenya, Mauritius, South Africa, Botswana and Zambia, all of which are more expensive destinations. In some cases, room rates on the Zambian side of the Falls are double those on the Zimbabwe side. For this reason, tour operators have already indicated plans to return to the Zimbabwe market once the political crisis is resolved.

The key to enhanced performance is an extension of the period that tourists stay in the country. The typical 6-day visit of the past is now closer to two days. Accordingly, the challenge for the industry is to extend the period of tourist stay by broadening and diversifying the services and activities available. A one night extension in the accommodation period increases earnings by a quarter. At present Zimbabwe is a very short-duration destination – two days per visitor. The industry has set itself the target of raising this to three days.

8.3.8 Constraints on tourism development

Until the end of the 1990s, areas of tourist attractions in Zimbabwe were reasonably accessible as the country had a well developed transport and communications network. The major resorts were well served by road, air and rail transport. In the second half of the 1990s, the national airline, Air Zimbabwe, was complemented by two privately owned airlines in order to cope with internal tourist traffic. Zimbabwe Express and Expedition Airways had daily flights from Harare to Kariba, Bulawayo and Victoria Falls. Smaller but important tourist destinations like Masvingo, Chiredzi, and Buffalo Range were serviced by Expedition Airways. The Victoria Falls was also served by air directly from Johannesburg in South Africa, while Harare International airport was served by leading European carriers. However, as the crisis deepened, so both international airlines and local airlines retreated or disappeared altogether.

Today, airline infrastructure is the single most important constraint. Because of the changing structure of Zimbabwe's tourist market, with the tourism hub having shifted from Harare to the Victoria Falls, the crucial bottleneck is the handling capacity of the Falls airport. Even if all flights to the Victoria Falls – both domestic and international – were completely filled with tourists, the room occupancy rate would be no more than 40 percent. Unlike the airport at Livingstone on the northern side of the Zambezi River, the Victoria Falls airport is too small to cater for long-haul wide-bodied aircraft. To exploit the area's tourist potential to the full, the runway must be lengthened and the airport building enlarged or rebuilt altogether.

Tourism would benefit from the implementation of an 'open skies' policy (chapter 10 on infrastructure) that might attract back some international carriers which have ceased providing services to Zimbabwe. Air transport will be a key component of the short-term revival strategy, generating foreign currency as well as helping to boost employment.

The airline constraint could be eased also by requiring the national carrier to enter into code-sharing agreements with other airlines. This would immediately open up the number of landing slots available to international airlines and, provided it is accompanied by the extension of the runway and expansion of the Victoria Falls airport, it would increase capacity substantially.

In recent years, skills have become a major constraint. Ahead of the 2010 Football World Cup in South Africa, Zimbabwe has been hemorrhaging tourism skills, in part because Zimbabweans have a superior work ethic but also because their better education, and especially language skills, attract South African employers.

Although Zimbabwe currently has five tertiary institutions – of variable quality – that offer hotel/tourism training, this is an area that will require special attention in the future. There has been a steep decline in

industry standards, especially in the smaller hotels and destinations that rely on domestic business and that are unable to access foreign exchange. As a result, they are unable to provide even the most basic services in terms of food, beverages, accommodation and transport.

Other serious constraints are those that are generic to the current economic situation:

- Macroeconomic distortions, including an overvalued exchange rate which undermines the competitiveness of the sector;
- Inadequate and deteriorating infrastructure;
- A much increased reliance on imported inputs, reflecting weaker backward linkages, and
- Infrastructure, mainly water and electricity.

Accommodation: Although many lodges and tourism camps have either closed down or are in a low maintenance state, Zimbabwe generally still boasts of a wide variety of accommodation for international, regional and local tourists. These range from the simple camping sites through the rugged camps in the bush, luxury and exclusive safari camps and backpacker lodges to up-market five star hotels and lodges. Though the latter group of facilities are still in good condition and can readily accommodate visitors, there is need for a face lift of these premises and supportive systems.

8.3.9 The future

The Zimbabwe tourist industry of the future will be very different from that of the 1990s. The hub has already moved from Harare to the Victoria Falls and this is unlikely to be reversed. The use of small aircraft to ferry visitors to different destinations – Kariba, Bumi Hills, Hwange Game Park and Great Zimbabwe – will change the nature of the tourist package, especially as currently

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Zimbabwe provides these services more cheaply than its rivals in Botswana, Namibia, Zambia or Kenya.

Much has been made of the potential gains from the 2010 Football World Cup. This should be seen in perspective. There will certainly be an increase in the number of tourist arrivals to the region, but an unknown proportion of those will be substitution or replacement visitors. In other words, many tourists who might otherwise have come to Zimbabwe will go elsewhere to avoid the World Cup crowds. From Zimbabwe's viewpoint, possibly the main plus from the World Cup will be the opportunity to re-establish the country as an attractive Southern African tourist destination. It will be more of a promotional opportunity than a source of immediate growth.

The main strategic objective of a recovery and development policy for the tourism sector should be the removal of the various distortions that impede its recovery and sustainable growth and to develop and strengthen the backward and forward linkages between the tourism sector and other sectors of the economy.

By marketing Zimbabwe as a new and safe tourist destination, a post-crisis Zimbabwe will reinforce the dividends of political recovery under a new improved security environment with proactive programmes to increase domestic, regional and international tourism. This is because tourism and security are positively correlated, the more secure Zimbabwe becomes, the more it will be able to attract tourists.

8.3.10 Sustainable recovery policies

The overall goal of Zimbabwe's tourism policy will be to realize the country's tourism potential in an integrated approach that emphasizes local participation and beneficiation. Tourism will be an increasingly important element of the economy, utilizing local resources and mainly domestic capital to generate employment and foreign-

currency benefits for the nation as a whole. Compared to some of the economic initiatives that will be implemented, a rejuvenated tourism sector provides the quickest turnaround because it is not capital intensive.

The specific measures to be deployed will be:

- An international campaign to advertise the post-crisis Zimbabwe under the new and secure environment will offer different tourism expectations.
- Active participation in regional and cross-border tourism initiatives, including the Great Transfrontier Park project with Mozambique and South Africa.
- Diversification of tourism into cultural tourism, village-based tourism, ecotourism, conference and incentive travel, and sports and recreation (particularly golf). These strategies will extend the employment and income benefits of tourism to a much wider range of Zimbabwean workers.
- Encouragement of a **value chain approach** with strategies to encourage tourists to buy Zimbabwean products while visiting the country, particularly crafts and works of art, gold and jewellery.
- Identification of zones for the accelerated development of tourism infrastructure.
- Strategies to enable more Zimbabweans to enjoy national tourist destinations.
- Provision of clear mandates and adequate resources to institutions responsible for the promotion of tourism within Zimbabwe.
- Careful consideration of tourism in the finalization of land reform, including stopping the current depletion of wildlife and other natural resources and the destructive effects of gold-panning.

8.3.11 Pro-poor tourism

Pro-poor tourism increases the positive impacts of tourism on poor people. The approach seeks to increase participation of poor people at many points in the sector and aims to increase their economic and social benefits from tourism while reducing the negative impacts on the poor. Community tourism is an example of pro-poor tourism. The tourism supply chains also have to extend far into the local economy – not just benefiting tour operators, hoteliers and transport companies, but encompassing workers and entrepreneurs from different sectors. The strategy therefore should be balanced, not focusing just on jobs or community tourism, but enhancing the linkages and local economic development (Ashley, 2006).

Tourism export industry as part of an overall national export strategy: As JAMPRO (2005) highlighted, the tourism sector provides a ‘domestic export market’ in that: i) its clients are mainly foreign, ii) it is an earner of foreign exchange; iii) it provides the opportunity to showcase local products and testing their international acceptance, thus providing an intermediate export market; iv) it is a testing ground for the export market to determine export readiness of local producers; v) it creates demand for exports; and vi) enhances competitiveness of exports as producers have to meet the international quality standards. The tourism sector is therefore an integral part of the export sector and hence it should be part of an overall national export strategy.

Chapter 9

Land Policy and Agricultural Recovery

The roots of Zimbabwe's land policy and its agricultural development lie in the historical division of land according to race and the subsequent evolution of a dual agrarian structure.¹ At independence in 1980, this structure was characterized by two distinct agricultural systems: a predominantly white commercial farming sector, and a traditional (communal) farming sector. The government therefore embarked on two ambitious programmes. The first was to correct the historical imbalance in land occupation by resettling households on underutilized commercial farms in order to decongest the overcrowded communal areas. The second was a development plan to reorganize land use within the communal areas in order to reduce rural poverty.

Progress with both the resettlement programme and the Communal Land Development Plan, however, proved disappointing. By the late 1990s, less than half the targeted number of families had been resettled, and the number of households living in the communal areas had swelled to over one million. The Communal Land Development Plan had faltered and then petered out. In an effort to revive the resettlement programme, a donor's conference on land was convened by the UNDP in September 1998. Although agreement was reached, the Zimbabwe government decided instead to acquire commercial farms compulsorily for resettlement and to transfer responsibility for compensation to Britain in a new draft constitution.

When the government's draft constitution was defeated in a referendum in February 2000, it embarked on a Fast Track Land Reform Programme (FTLRP) in 2000,

leading to the occupation of thousands of commercial farms. Though it may have corrected the historical imbalance of land ownership, the implementation of the programme was neither just nor sustainable. The cost to the economy and the people has been devastating. Zimbabwe is therefore again faced with the need for an equitable and sustainable resettlement programme and policies to reduce poverty in the communal areas. Fortunately, agriculture has the potential to become a primary source of growth and bring about poverty reduction in a future recovery programme (Mellor, 2000). Such potential, however, is predicated on a fundamental reorientation in land policy.

9.1 OVERVIEW OF PAST PERFORMANCE: 1980–1997

9.1.1 Zimbabwe's inheritance

Farm sizes and farming potential

At independence in 1980, the Zimbabwe government inherited a patently unfair distribution of land as well as deep and persistent poverty in the communal areas. About 5,600 white commercial farmers had access to 15.5 million hectares of land, while over 780,000 smallholder farmers had to subsist on 16.4 million hectares of land. Whereas the average size of a commercial farm was over 1,000 hectares, the average size of a communal farm was less than 10 hectares. At that time, large and fecund white commercial farms lay alongside pools of communal poverty, where thousands of black smallholders had to subsist on tiny holdings.

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¹ Dualism was initially created and maintained by the entry of foreign capital or colonization into the pre-capitalist indigenous economy (Ndlela, 1981: 24).

Table 9.1: Percentage of land allocated across Natural Regions and land categories (1980)

Land category	Natural (farming) regions				
	I	II	III	IV	V
Large-scale commercial farms	71	69	45	28	26
Communal areas	13	21	39	50	49
Small-scale farming areas	—	4	4	4	2
State land	16	6	12	18	23
TOTAL PERCENTAGE	100	100	100	100	100
Percentage of total area	1.8	15.4	17.5	36.4	28.9

Source: Zimbabwe (1986a: p.96, Table 4)

There were also significant variations in the agricultural potential in the two farming sectors.² Table 9.1 shows that the most productive land, in Natural Regions I and II, was held by commercial farmers, while most of the poorer communal farming areas fell into Natural Regions IV and V, which have very limited agricultural potential. One of the objectives of post-independence land policy was, therefore, to acquire more commercial farmland in Natural Regions II and III for resettlement.

State marketing and agricultural research organizations

Parastatal organizations dominated the marketing of agricultural commodities in 1980. These had given the state leverage over agricultural prices and production when pursuing an import substitution strategy in the face of international sanctions imposed after UDI.³ The major agricultural marketing boards established before independence included the Grain Marketing Board, the Cold Storage Commission, the Dairy Marketing Board, the Cotton Marketing Board, and the Agricultural Marketing Authority. Zimbabwe therefore inherited a highly regulated and monopolistic agricultural marketing structure in 1980.

The state also had a sizeable stake in the country's research establishments.

Significant advances had been made in the development of hybrid seed maize for the higher rainfall regions, as well as short season varieties for the drier communal areas. Research into cotton, wheat, tobacco and oilseed production saw impressive gains in productivity and yields. Despite this impressive contribution of agricultural research to national development, it focused mainly on high input technologies that were beneficial to commercial producers rather than to smallholders. After independence, therefore, agricultural research focused more on the smallholder sector while attempting to maintain the technology gains in the commercial sector.

9.1.2 Socialist transformation, 1980–1990

The imperatives of land redistribution and poverty reduction

The priorities at independence were to correct the historical imbalance in land through an orderly, transparent and sustainable land redistribution programme, and to reduce poverty by relieving the pressure of population and livestock on communal land. The *Zimbabwe Conference on Reconstruction and Development* (ZIMCORD) was held in March 1981 to garner international donor support to meet

² Vincent and Thomas (1961) used rainfall patterns and soil characteristics to define five Natural Regions (I–V), which correspond to different zones of agricultural potential in Zimbabwe.

³ Rhodesia unilaterally declared independence from Britain in November 1965. Soon afterwards, the United Nations imposed international economic sanctions against the Rhodesian regime.

these national objectives (Zimbabwe, 1981c). The conference document reiterated the government's three key land and agricultural policies:

- To *intensify* agriculture in the communal areas to increase productivity.
- To create a more equitable distribution of land through *resettlement*.
- To reduce population pressure in the communal areas by encouraging 'non-farming' families to *migrate* to urban centres.

The new government's development philosophy, articulated in its *Transitional National Development Plan, 1982–1985*, foresaw the introduction of socialist property relations through cooperative enterprises and state participation in production, distribution and allied services (Zimbabwe, 1982). In its agrarian vision, peasant associations would stimulate the collective spirit and organize themselves into centralized villages. The predilection of government was therefore to control land through direct participation in agriculture, through land acquisitions, government leases and permits and, eventually, nationalization.

Agricultural intensification

In the 1980s, the state used various approaches to intensify agriculture: research and training, pricing policies and subsidized marketing outlets, and a communal land development programme. Research was restructured to cater for smallholder production by the initiation of programmes of on-farm research and extension, the development of new varieties of traditional small-grain food crops that were suitable for the semi-arid regions, and the use of hardy indigenous cattle and sheep for meat production. The government also maintained

the parastatal marketing and financing system, which initially helped smallholders to achieve production levels in maize and cotton in the mid-1980s that surpassed commercial production. Attractive producer prices, the expansion of maize collection depots throughout the country by the Grain Marketing Board (GMB), and loans provided by the Agricultural Finance Corporation saw stocks of maize reach record levels. In 1986, the Communal Land Development Plan was presented as an agrarian reform strategy based on 'clearly defined land use patterns, more intensive use of land, thus resulting in higher productivity' (Zimbabwe, 1986a: 54). Its central concept was the reorganization of land use within a consolidated village, with clearly demarcated residential and cropping areas according to minimum farm sizes. Land was to be held on the basis of a government lease.

Resettlement and migration

An 'intensive' resettlement programme was launched in 1980 to resettle 18,000 households from the overcrowded communal areas onto 1.1 million hectares of former commercial farmland over three years. This programme was superseded by an 'accelerated' resettlement programme, initiated as part of the *Transitional National Development Plan*. This called for the resettlement of 162,000 families on 9 million hectares of underutilized commercial farmland over three years (Zimbabwe, 1982). A third development strategy was to further decongest the communal areas by encouraging migration to towns and cities. In a bid to reduce the number of households in the communal areas to their estimated 'carrying capacity' of 325,000 households, 235,000 communal families were expected to join their family breadwinner who was working and living in an urban centre (Zimbabwe, 1981a).⁴

⁴ The 'carrying capacity' of the communal areas was the estimated number of families whose livelihoods could be sustained within the communal areas.

Table 9.2: Land acquisition and resettlement

Financial year	Land acquired (ha)	% of total	No. of families settled	% of total
1979	87,000	3	1,971	3
1980–1985	2,298,000	83	39,364	70
1986–1990	395,000	14	15,183	27
Total	2,780,000	100	56,518	100

Source: Mhishi (1995)

Evaluation of strategies

By the end of the 1980s, the implementation of these strategies had proved disappointing. As Table 9.2 shows, although over 56,500 families had been resettled, this fell well short of the target, and the programme lost momentum.

The slowdown was particularly noticeable after 1985. Only 14 percent of the total land targeted for resettlement was acquired between 1986 and 1990. This period also accounted for 27 percent of the households resettled compared to 70 percent during the preceding five-year period. Nor had the communal land reorganization programme gained traction. One study found that between 1986 and 1991 plans had been drawn up for only four out of ninety villages in the UMP district⁵ (Doré, 1993). By the 1990s the plan had been shelved. In the meantime, the expected migration of households to towns and cities had not materialized. Rather than the communal areas being decongested to their target population of 325,000 households, the number of households had increased to about one million by 1990.

The limits of intensifying smallholder agricultural production had also been felt. Smallholder maize production levels, which had peaked in 1985 at 1.7 million tonnes, declined during the four following years to below 1.35 million tonnes. Investigations revealed that the increase in maize production came from just 10 percent of farmers in the better agro-climatic areas (Natural Regions

II and III). Generous pricing policies had by 1986 created an oversupply of maize, while marketing support and subsidies saw large and unsustainable budget deficits develop. Meanwhile, owing to poor loan repayment rates, smallholder credit tailed off considerably. The number of small farmers who received loans during the 1989/90 cropping season had dropped by over 40 percent from its peak in 1985 (Rohrbach *et al.*, 1990).

9.1.3 Economic liberalization, 1991–1996

The commercialization of the agricultural marketing authorities

As part of Zimbabwe's economic structural adjustment programme (ESAP), changes were made to the constitutions of the agricultural marketing boards in 1991 that gave them greater autonomy in pricing and business decisions. The Dairy Marketing Board was commercialized in 1993 and then privatized as Dairiboard Zimbabwe Ltd in 1996. The Cotton Marketing Board was granted formal managerial autonomy in 1991, and its monopoly in purchasing, ginning, marketing and exporting cotton was removed. The Cotton Company of Zimbabwe (Cottco) was launched in 1994 to replace the Cotton Marketing Board. It was then privatized in 1997. The monopoly of the Cold Storage Commission was also broken in 1991, when beef marketing on the domestic market was liberalized. Private abattoirs were licensed and the Commission was rebranded as the

⁵ UMP stands for the communal areas Uzumba, Maramba and Pfungwe that constitute the district. UMP lies within Mashonaland East Province.

Cold Storage Company, but it still retained its monopoly on exports. The Grain Marketing Board was commercialized and the agricultural commodity exchange (ZIMACE) provided the benchmark for prices. By 1996 maize marketing and prices were completely decontrolled on the domestic markets. Maize trading throughout the country was freed and all subsidies removed. The decontrols were particularly effective because they were accompanied by the lifting of foreign currency and import restrictions, thus allowing the purchase of vehicles, processing equipment and other inputs (Muir-Leresche and Muchopa, 2006).

Land policy and resettlement

In 1990 the ‘willing seller – willing buyer’ land acquisition restrictions imposed by the Lancaster House Constitution expired. In July of that year the government unveiled a new national land policy. Among other measures, 5 million hectares of commercial farmland was to be acquired (over and above the area already settled) in order to resettle a further 110,000 families.⁶ Prices paid for land were to be fixed at a ‘realistic’ level. To make these new targets possible, the government set about clearing the constitutional and legal hurdles for full-scale resettlement. In 1992 the ‘willing buyer – willing seller’ principle and the payment of market prices for land were dropped. Instead, a substantially reworked Land Acquisition Act [Chapter 20:10] allowed for the compulsory acquisition of land based on a complex set of fifteen principles to derive a ‘fair’ price for compensation. Even so, the pace of resettlement remained stubbornly below 2,500 households per annum between 1990 and 1993 (Mhishi, 1995).

In May 1994 the resettlement programme became mired in controversy. It became apparent that land earmarked for resettlement had been allocated to senior government officials, including ministers

and military officers. In almost all cases, properties were received at well below market value. Although the President later called for the leases to be cancelled, senior officials continued to receive large tracts of land. Many never paid for the leases or, since the prices were never adjusted for inflation, paid derisory low rates. The manner in which leases were allocated and the lack of a transparent system to advertise the availability of farms led to concerns about the process as a whole (International Crisis Group, 2004).

Despite the passing of the Land Acquisition Act (to speed up the resettlement process) and constitutional amendments (to prevent farmers from challenging ‘fair’ compensation in the courts) the total number of families resettled by 1997 had risen to just 71,000 on 3.5 million hectares. Only 17,000 poor families – against the target of 110,000 – had been settled since 1990. But, rather than back-tracking, the President used the British government’s reticence to fund land redistribution to galvanize support for his 1996 electoral campaign, threatening to seize the land of white commercial farmers without compensation (International Crisis Group, 2004).

9.2 CURRENT SITUATION ANALYSIS, 1997–2008

9.2.1 The emerging crisis, 1997–1999

When the Zimbabwean President was unable to persuade the British Prime Minister to provide substantial funds for land acquisition in October 1997, he ordered his agriculture minister to identify and list 1,500 commercial farms covering 4 million hectares for rapid acquisition. He also made it clear that he expected Britain to pay:

⁶ This approximated the original target of 162,000 households on 9 million hectares, minus the households and the area that had already been settled.

*'We are going to take the land and we are not going to pay for the soil. This is our set policy. Our land was never bought and there is no way we could buy back the land. However, if Britain wants compensation, they should give us money and we will pass it on to their children.'*⁷

In an effort to broker a solution, the UNDP called for a donor's conference on land with the participation of Zimbabwean stakeholders. The Zimbabwe government's proposal for Phase II of its Land Reform and Resettlement Programme suggested resettling over 90,000 families over a period of five years at a cost of US\$1.9 billion. Eventually the conference agreed to a set of principles, including compensation for land, and to establish a UNDP Technical Support Unit. The unit's role was to assist in carrying out a two-year inception phase based on the acquisition of 118 farms on a 'willing seller – willing buyer' basis.⁸ By early 1999 the government had done little to follow up on the donor conference's recommendations and its focus had shifted. The President appointed a Constitutional Commission to draft a new constitution for the country. Inserted into the final draft constitution was a clause that allowed the government to acquire farms without paying compensation for land. Instead, this responsibility was shifted to the 'former colonial power' – Britain.

9.2.2 The Fast Track Land Reform Programme, 2000–2008

Land occupation and allocation

Following the rejection of the government's draft constitution in a referendum in February 2000 – the ruling party's first popular defeat since coming to power in 1980 – action was taken to shore up support before the

parliamentary elections scheduled for June 2000. Central to the strategy was a new radicalized approach to land reform that could secure the rural areas ahead of the elections. In a process marked by considerable coercion, thousands of party-sponsored settlers occupied commercial farms. The number of farms listed for acquisition rose to over 3,000 by the end of July 2000, by which time at least 1,600 farms had been occupied. The occupation of commercial farms was legitimized through changes in the constitution and legislation, and confirmed by the publication of *People First* in July 2001, the formal document of the FTLRP. Two models of resettlement were proposed: a Model A1, in which each household would be allocated at least 3 hectares of arable land, but with shared grazing; and Model A2 schemes based on small, medium and large-scale commercial farms with 99-year leases (Zimbabwe, 2001).

9.2.3 The re-imposition of state control over pricing

In July 2001, maize, maize products, wheat and wheat products were declared controlled products. This made it illegal to buy, sell or move these products within Zimbabwe, other than to the GMB. ZIMACE was officially suspended. These restrictions were further tightened in December 2001 when farmers were compelled to deliver maize and grain stocks to the GMB no later than 14 days after harvest. In early 2002, the holding of all grain stocks by farmers was banned and grain supplies were seized, leaving the livestock industry and farm-workers facing a crisis. Some smallholder farmers had grain stocks seized and all existing grain contracts were cancelled. By September 2006, government controls and food subsidies had led to bizarre price distortions. For example, the government had fixed the producer price of maize at Z\$33,000 per tonne which the GMB, as the

⁷ *The Guardian* (London) 15 October 1997.

⁸ Communiqué issued at the end of the International Donors' Conference on Land Reform and Resettlement in Zimbabwe, 9–11 September, Harare, 1998.

sole lawful dealer in maize, sold to millers at Z\$600 per tonne, representing a 98 percent subsidy.

9.2.4 The decline of agriculture

Commercial agriculture – prior to Zimbabwe’s current political and economic crisis – was the largest formal sector employer in the country and made significant contributions to national income and export earnings. Since the onset of the FTLRP in 2000, however, over 200,000 workers have lost their jobs and total commercial agricultural production has more than halved. Table 4.3 shows that, for a selection of commercially produced commodities, aggregate output in 2007 was only 42 percent of output in 1998. Before 2000, in a ‘normal’ non-drought season, the commercial sector would complement communal production to produce a national total of about 2 million tonnes of maize to meet the country’s needs. Today, the country is struggling to produce more than 1 million tonnes. Likewise, wheat production has declined from about 270,000 tonnes in 1998 to 62,000 tonnes in 2007 – falling well short of the national requirement of 350,000 tonnes.

However, there is wide variation in the decline in production levels of various commodities. Tea and sugar plantations remain at 83 percent and 69 percent of their 1998 levels, respectively, while maize, tobacco and beef production is down to about a third of previous levels. Coffee production has virtually ceased, and cotton is no longer produced by large-scale farmers.

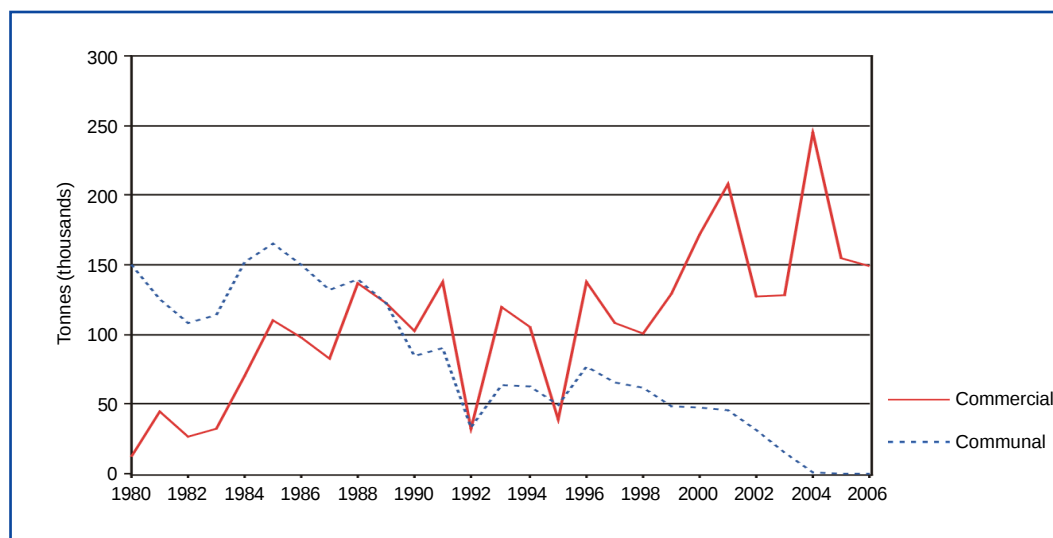
The right-hand side of Table 9.3 shows the proportion of the commodities still being produced by commercial farmers. For example, although there has been a substantial decline in wheat and dairy production, the *proportion* produced by commercial farmers has actually increased. This suggests that smallholder production of these commodities has declined. Conversely, the proportion of maize and beef produced by commercial farmers declined significantly, suggesting that any downturn in smallholder production has been less severe. Cotton is an interesting case. Whereas Table 9.3 shows that cotton production on commercial farms has shut down, Figure 9.1 shows that smallholder production overtook commercial production in the 1980s and maintained production levels after 2000 – largely due to

Table 9.3: Decline in commercial agricultural production for selected commodities between 1998 and 2007

Category	Crop	Commercial production		Percent of 1998 levels	Proportion of commercial production in total production		Percent of 1998 levels
		Tonnes (000)		%	%		%
		1998	2007		1998	2007	
Food crops	Maize	521	160	31	36	23	63
	Wheat	270	62	23	90	96	106
	Soyabeans	113	64	57	99	95	96
Export and Plantation	Cotton	77	0	0	28	0	0
	Tobacco	210	65	31	97	88	92
	Coffee	10	1	10	99	98	99
	Tea	18	15	83	99	97	98
	Sugar	553	384	69	97	96	98
Livestock	Dairy	184	86	47	93	98	105
	Beef	350	120	34	67	48	72
TOTAL		2,306	957	42			

Source: Commercial Farmers Union

Figure 9.1: Commercial and communal cotton production: 1980–2006



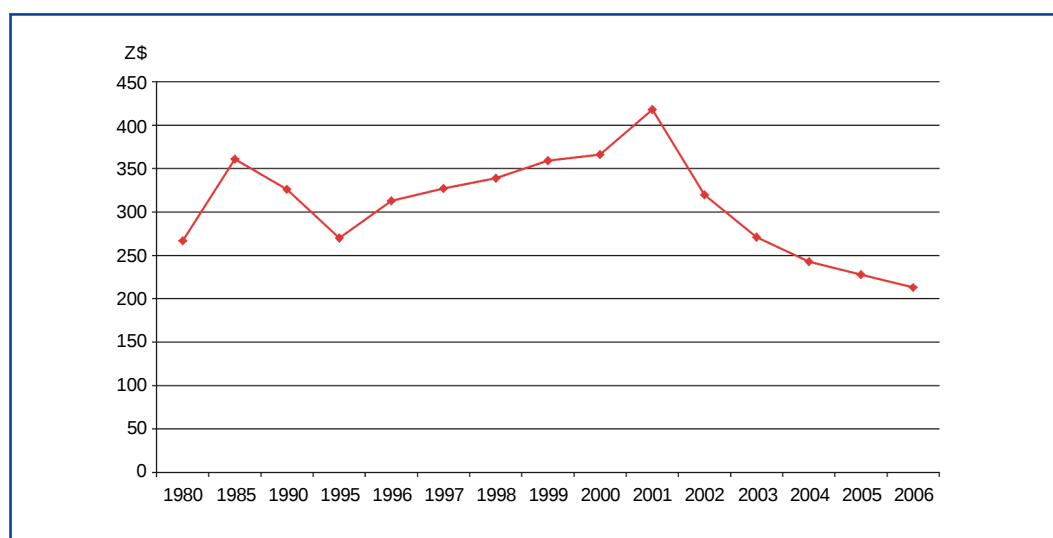
Source: UNDP (2008a)

cotton marketing corporations supplying inputs for growers and providing them with a ready market for their produce.⁹

More generally, Zimbabwe's agricultural performance can be measured by the per capita value added. Figure 9.2 shows that it has declined from its peak in 2001 to about half that level in 2006. This drop is explained not only by the impact of the FTLFP on commercial production, but also by critical input constraints. At a meeting of the

Parliamentary Portfolio Committee on Land and Agriculture in September 2007, it was reported that agricultural supply constraints (due to foreign exchange shortages) had been exacerbated by government price cuts on goods throughout the country in June 2007, in an exercise known as Operation *Dzikisa Mutengo* (Operation Reduce Prices). A representative for the fertilizer companies reported that costs of producing fertilizer were running at six to ten times the government controlled selling price, while the

Figure 9.2: Agricultural value added per head (constant 1990 prices)



Source: Central Statistical Office, Harare, National Accounts (various editions)

⁹ See Box 5.1 in chapter 5 on the financial sector.

Table 9.4: Income distribution from agricultural production for communal households in Uzumba communal area

Percentiles of annual crop income	TOP		Percentiles				BOTTOM
	5	10	25	50	25	10	5
Crop income (Z\$) ¹⁰	2,859	1,857	1,079	616	268	98	55
% of top 5%	(100)	(65)	(37.8)	(21.5)	(9.4)	(3.4)	(1.9)

Source: Doré (1993)

capacity to produce fertilizer had been crippled by power outages at the phosphorous producing mines. Seed maize could not be secured from growers because the prices offered were only one-fifth of the cost of importing seed. Acute shortages of fuel and equipment were also reported.

Indices of overall agricultural production, such as those in Figure 9.2, disguise the wide disparities between commercial and communal producers, as well as between smallholder farmers themselves. Average maize yields in the commercial sector are about four tonnes per hectare in a normal season (without drought), while communal areas manage to produce only about one tonne per hectare.

Table 9.4 shows the very wide disparities in agricultural production within the communal areas, with the bottom 25 percent producing less than one-tenth of the top 5 percent of smallholder farmers. Many households within the communal areas – especially those afflicted by HIV and AIDS – remain highly vulnerable to external shocks, such as droughts, input constraints and political unrest. The household food insecurity and vulnerability picture for the 2006/07 agricultural season was dire. One-third of the population, or 4.1 million people, needed food aid through to April 2008 (FAO/WFP, 2007). Worse was to follow. The most recent FAO/WFP Crop and Food Supply Assessment Mission estimated that about 5.1 million people in both the rural and urban areas

would need food aid at the height of the ‘hungry season’ between January and March 2009 (FAO/WFP, 2008).

9.2.5 The adverse impact of the Fast Track programme

Underutilization of land

In part, the decline in agricultural output can be attributed to the underutilization of commercial farmland that had been acquired but not settled. The Presidential Land Review Committee, commissioned in 2003 under the chairmanship of Dr Charles Utete, confirmed that only two-thirds of the applicants for those commercial farms divided up for A2 resettlement took up their offers of land.¹¹ This translates into 2.8 million hectares, or 7 percent of Zimbabwe’s total land area, that remained unutilized.¹² Anecdotal evidence suggests that the level of land use and intensity of production has remained low, and that significant portions of once highly productive commercial farms remain idle (FAO/WFP, 2008).

Loss of farming skills

The reduction in output can also be attributed to the displacement of skilled and experienced commercial farmers and their workers. In 2000, an estimated 320,000 farm-workers, representing about 25 percent of Zimbabwe’s total work force (in formal employment), were employed on commercial farms. In the aftermath of the land invasions over 200,000

¹⁰ The official exchange rate at the time of the survey was approximately Z\$5 to US\$1.

¹¹ Zimbabwe (2003: 39) Table 2

¹² Zimbabwe (2003: 42) Table 5

farm-workers and their families – an estimated one million people – lost their livelihoods and homes, as well as access to farm schools and other social amenities (Sachinkonye, 2003).

Subdivision of land into sub-economic units

The process of subdivision of farms did not take sufficient cognizance of the farms' layout and structure. The infrastructure of commercial farms was based on a homestead and centralized farm operations that included machinery, workshops, sheds and barns, as well as an irrigation system that was dependent upon a single water source and a system that branched out across the farm. The new subdivisions, however, cut across this infrastructure. As a result, many of the new farms do not have access to the former farm's resources and facilities, making them less efficient and viable.

9.3 CONSTRAINTS TO AGRICULTURAL GROWTH AND RECOVERY

Land policy – regarding the controversial resettlement programme and the stagnating communal areas – has been the key underlying constraint to agricultural growth and recovery. The other major constraints have been the fragmentation of national institutions and a trade regime that lacks competitiveness.

9.3.1 Resettlement

Governance constraints

Under Zimbabwe's constitution, the President has wide-ranging powers to make appointments throughout the public service, including the judiciary. When the judiciary acted to constrain executive powers after 2000, extra-judicial means were applied to

overrule the decisions of the Bench. In November 2000, the Supreme Court ruled that the FTLRP was illegal because proper procedures had not been observed. It therefore ordered the removal of illegal settlers. The following month, Supreme Court hearings on the land invasions were disrupted by ruling party supporters. On 21 December 2000, when the Supreme Court found the land programme to be 'entirely haphazard and unlawful', ruling party supporters called on Chief Justice Gubbay to resign or risk assault. The Chief Justice then took early retirement and the President used his powers to expand the bench from five to eight seats. The Supreme Court subsequently reversed its decision, pronouncing the FTLRP constitutional (International Crisis Group, 2004).

More recently, the President has relied on support from his service chiefs in the armed forces and trusted advisers, who meet as the Joint Operations Command (JOC). The purview of JOC goes beyond the purely military and now includes economic policy decisions, such as Operation *Dzikisa Mutengo* (Reduce Prices). JOC's main intervention in agricultural affairs was Operation *Maguta*,¹³ initiated in November 2005 to increase maize production with the help of the military on underutilized commercial farmland (see Box 9.1). Farms around the country were identified where army units could be deployed to produce food. Levels of land use and food production have, however, not recovered.

Financial constraints

In the Zimbabwean nationalist narrative, articulated by the President, 'The liberation struggle was principally about recovering our land from British colonial settlers who had expropriated it from us' (Zimbabwe, 2001: 1). Today, the President, on behalf of the state, acts as the *de jure* custodian of the communal lands. He also acts as the *de*

¹³ *Maguta* is a Shona word that means 'I am full' or 'satisfied' after eating.

Box 9.1. The Fate of Kondozi Estate

A high-profile case that demonstrates the limitations of the command approach to agricultural production was the government's acquisition of Kondozi Estate in Odzi in 2004. Kondozi, which employed 5,000 workers (as well as out-growers in the communal areas), had established export markets for vegetables and flowers in Europe and Canada valued at about US\$15 million per annum. Leading Zimbabwean banks had invested heavily in the project. After its seizure, the management of Kondozi estate was handed over to the Agricultural and Rural Development Authority (ARDA), a parastatal organization. The lucrative export markets were soon lost and the farm's assets were systematically stripped, leaving the estate derelict. In an effort to resuscitate production, a deputy army commander was charged with running the estate in 2005. Rather than restoring Kondozi's former export potential, maize was planted to boost food production under Operation Maguta. Sorghum was also planted on the former out-growers' land, the army retaining one third of production. It transpired however, that only 40 hectares of the 224-hectare estate had been utilized for food production, the remainder lying idle. The military's inability to use the prime farm productively prompted government to hand part of the estate over to Bonnezim (Pvt) Ltd., an agro-processing arm of the government-owned Industrial Development Corporation. The company was expected to lead a consortium of indigenous businessmen to revive part of the Kondozi Estate. The other part had been allocated to a senior Zimbabwe government minister.¹⁴

facto custodian of the 'lost lands' in the commercial farming sector. In post-colonial Zimbabwe, land was not transferred from white commercial farmers to black Zimbabweans, but purchased by the state on a 'willing seller – willing buyer' basis in terms of the Lancaster House Constitution. This was justified because the targeted beneficiaries of the resettlement programme were mainly landless and poor households from the communal areas who could not afford to buy land. According to the nationalist discourse, there was no reason to pay for land that they believed was 'stolen' in the first place. This meant, however, that the huge financial burden of meeting the costs of land – and then giving it away – had to be shouldered by the government. Indeed, the financial burden went far beyond the cost of land to include a costly administrative system of assessing the 'fair' value of land, as well as meeting the massive costs of providing infrastructure and administering the resettlement schemes. The land reform and resettlement programme was therefore founded on a financially flawed model: the more land that was acquired for resettlement the greater the fiscal burden.

Legal constraints

It is arguable that the unsustainable funding mechanism of the resettlement programme lay at the root of the government's motivation to erode the constitutional and legal rights of white farmers to avoid paying them for 'lost lands'. The process began with Constitutional Amendment (No. 11) in 1990, which required the state to pay only 'fair compensation within a reasonable time', rather than 'adequate and prompt compensation'. Then, in 1992, the Land Acquisition Act dropped the 'willing buyer – willing seller' principle in favour of administratively determined or 'fair' compensation for land. When this was contested, the government passed Constitutional Amendment (No. 13) in 1993, preventing farmers from seeking redress through the courts. By 1997, the President had signalled his intention not to pay compensation for land acquired for resettlement. This found expression in Constitutional Amendment (No. 16) in 2000, which made Britain responsible for paying compensation to white farmers.

The Land Acquisition Act was then amended in 2000,¹⁵ which staggered the payment of

¹⁴ 'Minister takes over huge parts of Kondozi Estate', *ZimOnline* 13 January 2007 <<http://www.zimonline.co.za/Article.aspx?ArticleId=729>>.

¹⁵ Act No. 15 of 2000.

compensation for ‘improvements’ (but not land) in cash, bonds or other securities over five years. Other amendments continued to erode the legal rights of farmers, but the Land Acquisition Amendment Act (No. 1 of 2004) went much further. It stated that the government would no longer adhere to the FTLRP land acquisition criteria. It confirmed that the government – now intent on acquiring over 11 million hectares – could seize any remaining farms owned by whites, as well as plantations, agro-industrial property, export-processing zones and wildlife conservancies. By this stage, any notion of compensation for land and improvements had given way to confiscation. The Acquisition of Farm Equipment and Materials Act (No. 7 of 2004) provided for the seizure of the evicted farmers’ equipment and material. Then, in 2005, Constitutional Amendment (No. 17) nationalized all farmland that had been gazetted for resettlement. Finally, the Gazetted Land (Consequential Provisions) Act (2006) made it illegal for farmers to remain on their own farms (now state land) unless they could secure a state lease from government.

The major implication of the nationalization of commercial farms was not simply that laws eroded farmers’ compensation significantly, or that the farmers lost their farms and any security of tenure, but that, by removing an economic value from land, it ceased to be treated as a factor of production. There was little incentive for those who did not pay for their farms to earn a return on land or capital, because there was no investment in the first place. The constraint imposed by the constitutional and legal changes was to convert land from an economic resource to a political resource that could be used by the government as an instrument of power, control and patronage.

White commercial farmers have since contested the Zimbabwe government’s constitutional and legislative changes by lodging an appeal with the Southern African Development Community (SADC) Tribunal in Namibia. They argue that the land-acquisition process was racist and illegal under various international legal instruments, including the SADC Treaty and the African Union Charter. Their application sought an order from the Tribunal declaring that the changes to the constitution violate their human rights protected under Article 6 of the SADC Treaty.¹⁶

Institutional and capacity constraints

The resettlement programme has been hampered by institutional and capacity constraints since the 1980s. The main criticism has been the over-centralization and lack of coordination of the programme. In February 1993, the Comptroller and Auditor-General reported that programme implementation had suffered owing to interference by politicians and the lack of government capacity to coordinate implementation. Furthermore, it was reported that productivity gains through resettlement had not been realized and that land acquired for resettlement remained unused. Equally disturbing was its conclusion that resettlement would have no impact on decongestion in the communal areas.¹⁷ A later review of the resettlement exercise by the Commission of Inquiry into Appropriate Agricultural Land Tenure Systems, under the chairmanship of Prof. Rukuni, found ‘no evidence of serious effort on the part of key ministries for strategic planning and effective implementation of the resettlement programme’ and that the administrative institutions were ‘uncoordinated and sometimes corrupt’ (Zimbabwe, 1994: 63). This was a serious indictment of the programme whose ‘superior

¹⁶ Zimbabwe Government representatives walked out of the SADC Tribunal on 18 July 2008 when the farmers’ lawyer applied for the Government of Zimbabwe to be declared in breach of the Tribunal’s order. Ruling party militia had abducted and brutally assaulted the appellants, who the Tribunal had allowed to remain on their properties. Judgment on the main appeal had not been passed at the time of writing.

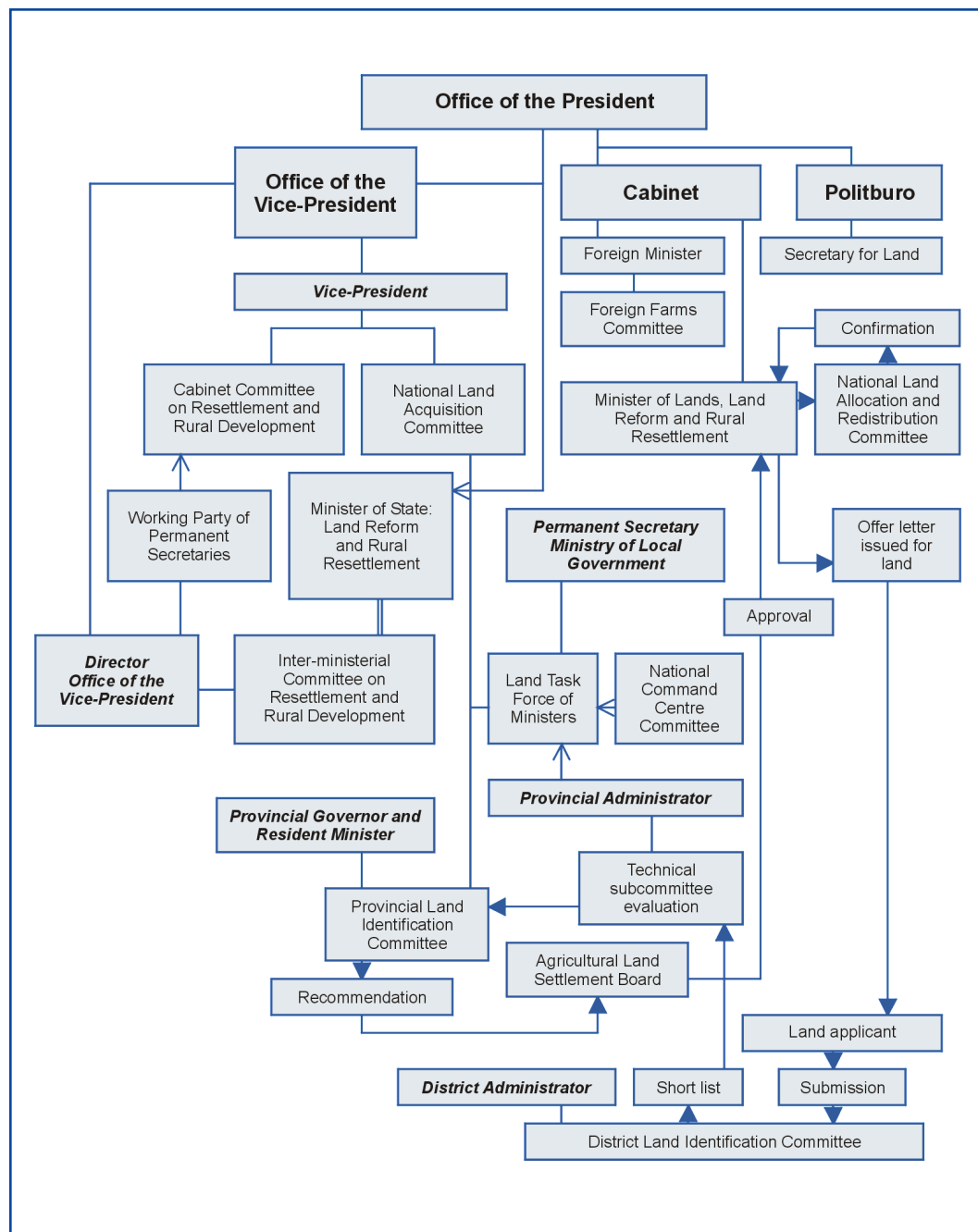
¹⁷ The *Daily Gazette*, 26 February 1993.

body' for coordination was the Cabinet Committee on Resettlement.

The Cabinet Committee has been in place since at least 1985 (Zimbabwe, 1985). Its role, however, remains unclear when the various committees, working parties, task forces and command centres (depicted in Figure 9.3) are added to the organizational structure for land identification, acquisition and settlement. This organization chart – derived primarily from the FTLRP document, *People First* – shows

the centralized nature of decision-making, the difficulty of defining responsibilities for land policy and implementation, and the problem of deciphering the actual decision-making process. As a result, most decisions are taken outside the confines of formal government institutional structures. The Utete Committee, for example, uncovered a process that did not follow official procedures at all. Many of those who had been allocated farms had no farming experience and were in full-time employment, often as civil servants. In general, the problem

Figure 9.3: Land acquisition and resettlement: Structure and processes



of district officials acting *ultra vires* was compounded by the activities of those persons, who, though lacking any official status or authority, nonetheless proceeded to allocate land, mainly in districts adjacent to the main towns and cities. The Committee's report concluded that 'the multiplicity of allocating authorities gave rise to double allocations, multiple allocations, and favouritism in land allocations' (Zimbabwe, 2003: 106).

Land tenure security constraints

The pre-2000 resettlement tenure system was based on three permits: a permit to reside, a permit to cultivate, and a permit to de-pasture stock (Zimbabwe, 1985). These permits accorded broad rights to the state, but provided few rights for the settler. The permit to reside, for example, specified that on expiry or revocation of the permit no compensation would be payable for improvements. As the World Bank remarked, 'It would be difficult to imagine a less secure form of tenure: uncertain duration, broad powers of termination on the part of the Ministry, and few rights to compensation for investments' (1991b: 78). However, despite flagrant breaches in the conditions of the permits by settlers, the state had neither the inclination nor the capacity to enforce the conditions of the permit (Doré, 1995).

Land tenure security has not improved since 2000. A1 settlers were to be issued with temporary occupation licences, which were expected to be converted into proper leases. However, it remains doubtful whether these licences were issued or converted to leases. With regard to A2 lease agreements, the UNDP found that they offered little security to settlers. It concluded that 'one must expect substantial insecurity of tenure in the resettlement areas' which would 'defeat the productivity goals of the resettlement programme' (2002: 30). The state grants virtually all the powers and rights to itself

and most of the obligations and duties to the lessee. Apart from 125 leases issued to A2 farmers by the President in 2006, it remains uncertain whether the government has continued to issue them. As a result, the occupation of commercial farms is legitimized by an 'offer letter' issued by the Minister of Lands, Land Reform and Rural Resettlement. These offer letters however, do not guarantee secure tenure. In August 2006, the President advised those who had been allocated farms to start producing food, otherwise the government would take them back.¹⁸ In early February 2008, the government revoked the allocation of 1,449 farms that had been allocated to A2 farmers because they had not been occupied or because they were lying idle.¹⁹

The government's abiding preference for 99-year state leases over agricultural land reaches back to the Communal Land Development Plan of 1986. The plan had proposed a 99-year inheritable lease, claiming that it gave security of tenure that was almost as good as freehold. Twenty years later, when most commercial farms were nationalized, the remaining farmers were required to receive state leases to continue operating. When issuing such leases to A2 and commercial farmers, it was claimed that they guaranteed security of tenure. State leases may, however, actually exacerbate insecurity of tenure for a number of reasons:

- The state has been inclined to impose onerous lease conditions on farmers.
- The state has neither the capacity to monitor and enforce the conditions of leases, nor the administrative capacity to set lease fees and update them.
- The state would face an insurmountable administrative burden of collecting rents, adjudicating disputes and enforcing evictions.

¹⁸ The *Financial Gazette*, 16 November 2006.

¹⁹ The *Cape Times*, 5 February 2006.

Furthermore, it is unlikely that state leases would be acceptable collateral to private financial institutions because state property cannot be alienated to third parties.

9.3.2 The communal areas

Capacity constraints

The state has consistently relied on centralized forms of decision-making and programme implementation. This applied as much to the implementation of the Communal Land Development Plan as it did to the resettlement programme. Despite the Department of Agricultural and Technical Extension Services (AGRITEX) being instructed to prioritize the implementation of the Communal Land Development Plan (1986) in the late 1980s, the Rukuni Commission reported little progress:

‘The main reason is the over-centralization of government with the relevant technical ministries using top-down methods of planning and implementation. The second problem is the poor coordination of the technical ministries who continue to exhibit territorial behaviour with no evidence of a well thought-out coordinated strategy.’ (Zimbabwe, 1994: 35)

As the 1980s drew to a close, less and less was heard of the programme until, by the mid-1990s, it had been forgotten.

Economic and environmental constraints

Under conditions of population pressure, the traditional system of agriculture tends to distort the allocation of factors of production, creating perverse incentives that undermine rural livelihoods and degrade the environment on which households depend. The system not only entraps families in poverty, but does not

offer any mechanism through which more efficient farmers can acquire more land to consolidate their holdings into larger, more viable units. Most importantly, perhaps, the traditional system does not offer a mechanism to decongest the communal areas. It does not provide any incentive for families to embark on a ‘migration of hope’ that allows them to improve their prospects by pursuing non-farm employment opportunities in urban centres.

The traditional system entraps households in poverty by allowing them free access to land and natural resources, thereby externalizing costs and subsidizing their living expenses.²⁰ This provides a perverse incentive for people to remain in the communal areas and so adds more pressure to land and natural resources. As the population builds up, land is continually subdivided into smaller and less viable farm sizes. As Figure 9.4 shows, risk-averse households with smaller farms (1.2–4.7 acres)²¹ tend to be entrapped in subsistence agriculture, producing maize for their own consumption. Conversely, cotton production becomes possible as farm sizes increase (6.6–14.6 acres). The inability of the traditional system to increase farm sizes thus frustrates national efforts to commercialize smallholder production and reduce poverty.

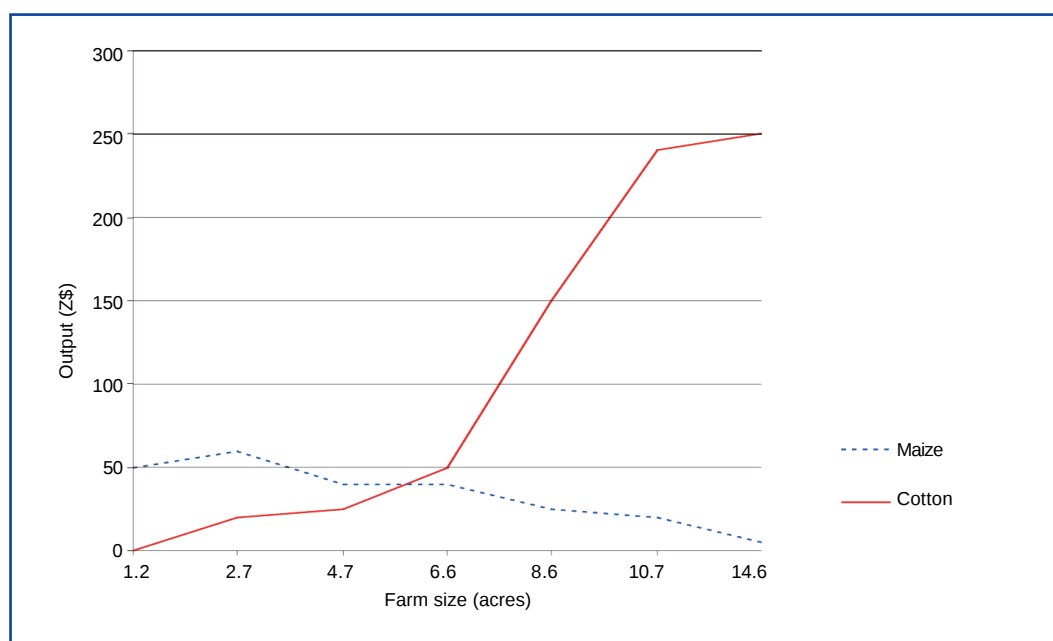
The administrative allocation of land by traditional leaders to every eligible family creates a profusion of tiny plots, each generating insufficient surpluses to reinvest in the capital improvements – cattle, equipment and inputs – that are required to off-set the diminishing marginal productivity of labour. Without labour-saving capital inputs, labour becomes critically short at peak periods in the agricultural calendar. This gives rise to the ‘labour paradox’ – that, although there is unsustainable pressure of population on the land, there is at the same time, a critical seasonal shortage of labour. But the process

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²⁰ An externality is a cost to society, such as environmental degradation, when individuals benefit from using a public good: for example, communal grazing areas. The cost is internalized when the user rather than society bears the costs of use.

²¹ 2,471 acres = 1 hectare.

Figure 9.4: Household maize and cotton production by farm size



Note: The figure for 2007 is an estimate

Source: Doré (1993)

does not end there. As land shortages are felt, households start extending their fields into grazing areas, thus reducing feed resources for livestock. Overgrazing and environmental degradation ensue, but cattle – smallholder assets, *par excellence* – are gradually squeezed out of the system. As a result, there are too many cattle for the environment to support, but too few to meet smallholders' cultivation requirements. This is known as the 'cattle paradox' (Cliffe, 1988).

The process of overstocking and environmental degradation is also attributable to the 'non-excludability' of common property resources. But they are also 'subtractable' (or rivalrous): if one person uses them, another's access is diminished. Because communal grazing land is a free and indivisible public resource – carrying no opportunity cost to the user – livestock owners have a strong incentive to add more livestock to common pastures. This incentive, however, becomes perverse when households continue to add more livestock to already degraded grazing areas, thus quickening the pace towards environmental decline – and eroding the very resource base on which their livelihoods depend (Hardin, 1968).

Institutional constraints

After independence, three distinct types of local governance institutions emerged in the communal areas: the traditional, the political, and the developmental. Alongside the traditional authorities, the ruling party had created and maintained its own political structures – both during and after the war. To complicate matters, the Prime Minister then issued a directive in 1984 for locally elected village and ward development committees to be established. As these were based on a centralized bureaucratic system, their jurisdiction cut across traditional boundaries that had been based on kinship, historical ties and natural features, as well as the resources they encompassed. This institutional complexity was compounded by the fact that local leaders simultaneously occupied different positions within the three separate structures. They were thus able to play multiple roles by drawing on different sources of legitimacy – the traditional authorities, the ruling party, and the local-government development structures. Although the development structures were in place, they were often subordinated to and crowded out by the more powerful political

and traditional organizations and so remained weak, ineffectual, and largely ignored (Zimbabwe, 1994).

9.3.3 National institutional constraints

Land and agricultural ministries

Overall there are five ministries responsible for land policy and agriculture. Land policy is covered by the Ministry of Lands, Land Reform and Resettlement and the Minister of State for Special Affairs responsible for the Land Reform and Rural Resettlement Programmes. It remains unclear, however, how the responsibilities of the two ministers are divided. Agricultural matters are dealt with by three ministries: the Ministry of Agriculture; the Ministry of Agricultural Engineering, Mechanisation and Irrigation; and the Ministry of Water Affairs and Infrastructure. Yet, it is not these ministries – with their fragmented roles and overlapping responsibilities – that take the lead in agriculture, but the Reserve Bank of Zimbabwe (RBZ). The RBZ, which has assumed supra-ministerial powers, has played a pivotal role in the provision of agricultural credit, farm inputs and food through its quasi-fiscal activities. It channels credit to farmers through the Agricultural Bank of Zimbabwe (Agribank) and the Agriculture Sector Productivity Enhancement Facility (ASPEF). Through its largesse farmers are provided with agricultural machinery, principally tractors, but also subsidised fuel and fertilizer.

Economic constraints on agricultural research

The Ministry of Agriculture is divided into ten different departments, each with its own director. However, their functional capacity has been severely weakened. The intractable problems faced by Zimbabwe's agricultural research establishments, for example, cannot be disguised. As government funding became increasingly constrained, the real earnings of researchers declined. The first casualties were qualified researchers who

were attracted abroad or by the private sector, further weakening government's research capacity. The next casualty was on-farm adaptive research because of the high travel and subsistence costs. The third casualty was the decline in capital expenditure, which fell to just 5 percent of requirements – far less than the depreciation of the infrastructural research base. By the end of the 1990s, meaningful research programmes were sustained only with international donor assistance (Tawonezwi and Hikwa, 2006). Now, even these have been suspended.

9.3.4 Trade and competitiveness

The overvaluation of the exchange rate represents an implicit tax on agricultural exporters (because farmers receive less in domestic currency for their produce), which lowers their incentives to invest, produce and export. The degree to which a government subsidises or taxes an agricultural commodity is measured by its 'nominal rates of assistance' (NRA). Table 9.5 shows large negative NRAs (i.e., taxes) for maize, cotton and tobacco up to 1990.

Table 9.5: Nominal rates of assistance for selected agricultural products, 1966–1990

Zimbabwe averages	Maize	Cotton	Tobacco
1966–1979	–22.0%	–27.3%	–20.1%
1980–1984	–16.6%	–38.7%	–32.4%
1985–1990	–18.4%	–42.6%	–37.9%

Source: Jansen and Rukovo (1992)

Ndlela and Robinson (2006) – who stress that the main macroeconomic influence on NRAs is *via* exchange rate overvaluation – confirm these distortions. For almost all agricultural crops in the 1980s they found NRAs well below zero. These, they say, arose from government's desire to maintain the multiple objectives of national food self-sufficiency, food security, low-priced food for consumers and access to marketing channels for all farmers wherever they were

located. Surprisingly, they found that the more liberalized regime of the 1990s continued to show high levels of negative NRAs to agriculture. They suggest that this was largely explained by the unreconstructed GMB, which continued to exercise a statutory monopoly and monopsony over both domestic and international marketing of maize and other major food crops.

They also found that farmers were taxed most heavily in the final five-year period of the Fast Track programme. Although, from 2004, massive direct subsidies to agriculture reversed these disincentives, agricultural production declined significantly due to a critical shortage of inputs.²² As soaring inflation and a fixed exchange rate made exports unviable, growers lobbied for special dispensation.

9.4 SUSTAINABLE RECOVERY POLICIES AND PATHWAYS

Strategic Objectives

- Establish institutions for the effective administration of a new land policy based on secure tenure and land markets.
- Bring the land reform programme to closure and the commercial and resettlement farming areas to their full productive potential.
- Reform the communal land tenure and administrative system to reduce poverty, improve environmental management, and commercialize smallholder production.
- Dissolve the dual economy and create pathways out of poverty by a process of migration and structural transformation.
- Increase and sustain agricultural productivity and growth.

9.4.1 Strategic Objective 1

Establish institutions for the effective administration of a new land policy based on secure tenure and land markets

Establish a Land Commission

There is wide consensus on the need to establish a Land Commission. The idea arose from the Rukuni Commission's recommendation for an independent National Land Board to advise government on land policy issues (Zimbabwe, 1994). It is therefore proposed that an independent Land Commission that reports directly to Parliament (through the appropriate Parliamentary Portfolio Committee) be established under a comprehensive Land Act. The Land Commission should be vested with clearly defined powers and the authority to:

- Build consensus on a national land policy based on wide consultation and best international practice.
- Plan and coordinate the implementation of an equitable, transparent and sustainable land reform and settlement programme.
- Plan and coordinate a land adjudication, demarcation and registration programme in the communal areas through democratic community assemblies.
- Develop a legal and institutional framework to support the systematic registration of land to improve tenure security and create an efficient land market.
- Establish a land tax to encourage the full utilization of agricultural land, dampen land speculation and raise revenues.

²² The NRA for the crops was -48 percent in 2004, while the direct rate of assistance was +49 percent.

- Work towards integrating the various tenure systems into a single legal and regulatory framework and land administration system.
- Over time, oversee the transformation of the dual agrarian structure into a single ‘unimodal’ structure of variable farm sizes that provide a ladder of opportunity.

The Land Commission should draw up a land reform programme for all agricultural land, defining priorities, coordinating implementation, supervising the programme, and monitoring its progress.

Establish a Land Fund

The UNDP (2002) first mooted the idea of a Trust Fund. It was then adopted as a recommendation by the Utete Committee (Zimbabwe, 2003). The most recent endorsement of a Land Fund came from the Zimbabwe Institute (2007). It is therefore suggested that a Land Fund be established, with a separate board, to service the Land Commission and other land and agricultural programmes. The Fund should be accountable to Parliament for expenditure, to donors for their funding, and to international financial institutions for their investments. A reputable firm should carry out annual audits to ensure a level of accountability and transparency that will reduce fiduciary risk to attract funds and investment.

Oversight and constraints on power

Policy oversight should be exercised by Parliament. The Land Commission should consult widely to formulate a sound land policy that is sanctioned by Parliament. In addition, the Land Commission should report annually to Parliament on its progress and future proposals, including a budget. Legal oversight should be provided by a Land Tribunal. The Land Commission will need to develop detailed rules, criteria and arbitration procedures to arrive at practical and fair decisions on the selection of settlers

and the allocation of land. Where it is unable to resolve disputes, aggrieved parties should be able to appeal to the Land Tribunal. Financial and operational oversight of the Commission and the Fund should be provided by the Office of the Auditor-General which, by custom, also reports directly to Parliament.

Building capacity for secure tenure and efficient markets

The development of an efficient land market is premised on a sound legal and regulatory framework, supported by competent land administration institutions. The two main institutions used for land administration are the Deeds Registry Office, which handles information on land ownership and transactions, and the Surveyor-General’s Office, which maintains the land survey database and maps (cadastre). Both these institutions should, in future, be located within the Land Commission.

State-led land reform to achieve market-led agricultural development

The trade-off between the need for state intervention and the efficiency of markets in national and agricultural development policy emerges from Zimbabwe’s recent economic and political processes. A consensus seems to be emerging, however, that countries do best where the public sector provides maximum support to the private sector to ensure that the legal and institutional frameworks support the development of markets that work in favour of the poor (Borras and McKinley, 2006). In Zimbabwe’s case, state-led reform, primarily through the Land Commission, should complete a process of land redistribution and reform as the basis for establishing vibrant markets that ensures rapid future growth in the agricultural sector. As the state plays a key role in implementing land policy for sustainable, pro-poor agricultural development, strengthening its capacity to function effectively should be a primary goal of any recovery strategy.

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INSTITUTIONS

9.4.2 Strategic Objective 2

Bring the land reform programme to closure and the commercial and resettlement farming areas to their full productive potential

The major goal for the land reform and resettlement programme should be to bring the commercial and resettlement farming areas to their full productive potential by bringing the land question to closure. The main policy recommendations are therefore to:

- Carry out a land audit to gather land and agricultural data and undertake a legal study as a basis for redesigning the resettlement programme.
- Revise the current land laws to conform to the post-crisis land policy and the agricultural recovery strategy.
- Replan settled farms to ensure their viability.
- Establish an equitable and transparent settler selection process based on need and ability.
- Provide all new settlers with secure tenure and suitable financing arrangements to ensure that agriculture is placed on a sustainable growth trajectory as early as possible.
- Arrange compensation to those who lost their farms, homes and livelihoods.

A land audit

As a first step, the Land Commission should gather information from a survey or audit to make well-grounded policy decisions. This audit could consist of three interlocking studies:

- a *farm acquisition and settlement survey* to document the acquisition process, the occupation of commercial farms, and the pattern of settlement under the FTLRP.

- a *legal study* to bring an authoritative judicial opinion to bear on the legality of that possession and settlement.
- a *physical and production survey* to determine the state of farm buildings and equipment, the extent to which the farms have been productively utilized, and the resource requirements to restore their productive potential (Zimbabwe Institute, 2007).

It is essential that the audit be conducted in a rigorous manner by independent researchers to ensure that its impartiality and credibility are never in doubt.

Revisiting current land laws

Zimbabwe's constitutional and legal provisions governing land are currently under review by the SADC Tribunal. However, it will be necessary for Zimbabweans themselves to revisit their land laws with a view to, first, providing secure tenure to encourage agricultural investments to bring land to its full productive potential; and, second, to provide for the building of institutions that enable the efficient operation of a land market. In general, new land laws should empower the Land Commission to carry out land tenure reform expeditiously.

Selection of settlers

The fundamental principle is that every citizen should enjoy the same rights in the acquisition and protection of their property, and that every Zimbabwean is entitled to earn their livelihoods from farming or be eligible for settlement, regardless of their gender, race, ethnic origin or political opinions. However, the state has a duty, to ensure that land, as a national resource, is used for the benefit of society as a whole by maximizing its economic use and social benefit. This means that agricultural land must be distributed fairly and transparently to those who can make the most productive use of it, such as master farmers, and those who have no other source of livelihood, such as communal

farmers or farm-workers. A fair and transparent selection process therefore requires that all applicants have confidence that their application will be processed fairly according to agreed criteria and laid-down procedures.

Secure land tenure

A moratorium needs to be placed on contested agricultural land, allowing those who presently occupy farms to continue operating until the Land Commission has carried out a land adjudication and rationalization exercise. Based on the findings of the land audit, this would entail (on a farm-by-farm basis or by dealing with categories of farms) reconciling on-the-ground realities of farm occupation with the principles of legitimacy, ability and need. The Land Commission's decision would be subject to appeal through a Land Tribunal.

Once the issue of ownership of the farm has been settled or a farm has been offered to a selected settler, the Land Commission would need to verify whether the boundaries of the subdivided farms have been clearly demarcated. It would also need to check whether the subdivisions of the original farm make the most rational and efficient use of the farm's resources. If not, it could call for a revised farm plan to modify farm sizes and boundaries before making a final determination and allocation.

The next step would be to replace the existing resettlement permits, offer letters or leases with a more secure form of tenure. While formal registered title offers the most secure tenure to obtain farming loans, this would not be feasible at present. Apart from being too costly and time-consuming, Zimbabwe does not currently have the capacity to carry out a formal land survey and registration exercise. An alternative approach, recommended by the Rukuni Commission, would be to use low-cost surveying techniques based on the latest electronic and GPS technologies for the less precise but less expensive surveying of boundaries. Once the Land Commission had

entered into a farm purchase agreement with the settler, it would confer ownership by issuing the settler with a land registration certificate – which could be a stepping-stone towards formally surveyed and registered freehold title in future.

Financing arrangements for land acquisition and farming loans

New farmers would not only need to enter financing agreements to acquire their farms, but to capitalize them with building and equipment, and to negotiate loans for working capital to finance seasonal inputs – seed, fertilizer, fuel, labour, etc. Depending on factors such as the size of the farm, the farmer's ability, resources available, and the preparation of a farm production plan, farmers could be eligible for a combination of moratoriums on repayments, concessionary loans and flexible repayment periods. This would give new farmers a reasonable time to establish themselves and repay their loans. The collateral for these loans would be the settlers' land registration certificates, which would be lodged with the financial institution negotiating and issuing the loans, such as the Land Fund or Agribank. Once the farm and any outstanding credit had been repaid, the certificate of registration would be returned to the farmer, who would be entitled to rent or sell his or her farm on the open market. Alternatively, the farmer could apply for their farm to be surveyed and upgraded to full registered title and to use the farm as collateral for loans with private financial institutions.

Those farmers who fail to meet the repayments on their loans could (with the agreement of the Commission) either rent or sell their land to repay their loans. Where the total loans outstanding exceed the realizable value of the farm, the Commission would be required to repossess and resell (or auction) the farm to recoup part of the outstanding loan, and write off the balance. The balance written off might include an 'exit package' so that the farmer is not left destitute and could make a fresh start in another venture.

Farmer support for planning and extension services

In order to give newly settled farmers every opportunity to succeed, there is a need for strong technical advisory and extension support, as well as the provision of infrastructure, facilities and social services – from roads and water, to schools and clinics – that should be established within designated rural service centres.

Initially, one of the key areas of support will be planning and production, especially if farmers are to make the best use of credit, which must be repaid. Planning is needed initially to rationalize the layout and demarcation of those farms that form part of a subdivided whole. Where resettled land has been allocated to communal grazing, this should be incorporated into individual self-contained family farms that are sufficiently large to accommodate some livestock. This will be essential to internalize the inevitable environmental costs. There will also be a need for production plans for crops and access to credit for the timely purchase of equipment and ordering of inputs.

Experienced commercial farmers who have been displaced, but do not wish to continue farming, could also play a valuable role in the farming sector by entering into agreements with new farmers in a number of innovative ways: by providing extension advice and services; by forming syndicates to realize greater efficiencies and economies of scale for the purchase of inputs and the marketing of produce; and by providing centralized processing of capital-intensive crops, such as tobacco or coffee, for outgrower settlers. The Commission, with the support of the Land Fund, could also contract former commercial farmers to mentor new farmers by assisting them with the demarcation and planning of their farms, the management of their farm operations, and providing them with sound agricultural advice. It would also serve to build bridges between new aspiring farmers and experienced, successful commercial farmers.

Pay compensation for land acquisition and losses

Most previous bilateral and multilateral documentation, including UNDP's report in 2002, emphasize the need to compensate farmers for land acquired for resettlement. However, it raises vexing questions. The first, mentioned in chapter 3 on stabilization, is who should be compensated. Many other Zimbabweans – who had their pensions wiped out, their homes razed during Operation Murambatsvina and more recently, who had their rural homes set ablaze – could also be legitimate claimants for compensation. The second is how much should be paid. The Movement for Democratic Change estimated that total claims for compensation by displaced farmers could exceed US\$8 billion – greater than Zimbabwe's GDP (MDC, 2007). The third is who will pay the compensation. The national coffers are empty and donors will be asked to forgive large debts and help with Zimbabwe's recovery and reconstruction. Thus, while in principle all those whose land was illegally seized should be compensated, the cost of full compensation is probably well beyond the means of both the state and sympathetic donors.

Set against these limitations, the payment of compensation would demonstrate the government's commitment to the principle of well-protected property rights. In particular, it would restore international confidence by sending a strong signal to investors that their capital would not only be welcome to help drive Zimbabwe's economic recovery, but reassure them that their assets were secure under Zimbabwe's laws.

Ethical considerations aside, Zimbabwe will be in no position to raise taxes to pay compensation and will therefore have to rely on the goodwill of the international community. The Government of Zimbabwe – and the Land Commission in particular – will need to engage with donors and farmers' representative organizations, such as the Commercial Farmers Union and Justice

for Agriculture, in order to negotiate compensation proposals that balance competing needs. On the one hand, there is a need to resolve historical injustices in the allocation of land and bring economic recovery to the agricultural sector. On the other, there is a need to respect the constitutional rights of all Zimbabweans and bring some relief to farmers who have suffered the loss of their homes, property and livelihoods. This will require a policy of reconciliation and healing to build goodwill and confidence between white and black Zimbabweans.

Given the inevitable funding constraints to meet compensation claims for land without jeopardizing Zimbabwe's economic and social recovery, it is incumbent upon the Land Commission to devise innovative ways of dealing with the issue of compensation paid to farmers. These may include:

- Allowing those commercial farmers who are still operating to remain on their farms; while allowing those whose farms have been acquired, but not occupied, to return to their farms.²³
- Offering another unoccupied farm as compensation to those commercial farmers who still wish to farm, but whose land has been occupied for settlement.
- Partially compensating commercial farmers through a recovery programme by assisting them to refurbish their properties and bring them back into full production.
- Returning those farms that have not been occupied to their original owners, who, if they do not wish to farm, can either rent or sell their properties on the open market.
- Allowing those Zimbabweans who wish to retain the farms they have occupied under the FTLRP, and who have the

means to pay for them, to negotiate the purchase of the farm from the previous owner through the Land Commission.

- Recouping the cost of settlement through farm purchase agreements between the new farmers and the Land Fund. A portion of these funds could be repaid to the original owner of the farm as compensation.
- Allocating a portion of the savings realized through debt relief to pay some compensation to retired farmers – possibly identified by commercial farmers' organizations – who find themselves in impecunious circumstances.

9.4.3 Strategic Objective 3

Reform the communal land tenure and administrative system to reduce poverty, improve environmental management and commercialize smallholder production

Safety nets and poverty traps

Although the communal areas capture households in a low-level equilibrium trap, they nonetheless provide a safety net for the poor and the unskilled. When population pressure builds up, the traditional system allows for the continual subdivision of land, thus providing at least 'something for everyone' and hence, enabling poor families to survive. Such limited security, however, comes at the expense of all existing communal households, who, when the communal land frontier is reached, must make do with less land and, hence, lower incomes. The communal areas are therefore as much poverty traps as safety nets.

The long term problem is that the whole traditional system of agriculture will stagnate and incomes will decline even further under the weight of population pressure. The perverse incentives that limit capital inputs and productivity will see poverty deepen. So

²³ The definition of whether a farm is occupied or not would be left to the legal study of the land audit to decide.

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too, will the problems of deforestation, extensive cultivation, overstocking and ecological decline. In short, the system is not sustainable. At some point, change must inevitably come, and, like so many reforms, the later it is left, the more painful it will be in the future. While such reforms involve greater risk, they also bring with them innovation, opportunities and pathways out of poverty.

An evolutionary approach to land tenure change may however offer a trade off between the security of customary tenure and the risk of market opportunities. In some areas, where land values are relatively high and land markets are emerging, a community may choose to move fairly rapidly towards building local democratic institutions and a simple land administration to enable local land tenure changes and land transactions. On the other hand, there are remote areas where the population density is relatively low, where customary law still holds sway, and where the cost-effectiveness of modifying the traditional tenure system would be hard to justify. This suggests a demand-led approach, where the direction and pace of change is determined (within a national policy and legal framework) by communities themselves.

Policy framework

This long term objective could be achieved by a series of steps that are initiated as part of a medium term recovery programme:

- The establishment of modern, democratic community assemblies, nested within a unitary and hierarchical administrative system.
- The transfer of *de jure* land ownership to communities.
- The establishment of a legislative and regulatory framework that allows community assemblies to initiate land tenure reforms themselves based on incentives, informed consent, the will of the community, and their participation in the land reform process.

- The adjudication and demarcation of ward, village and land use boundaries.
- The demarcation and issue of land registration certificates for residential and arable land which, subject to restrictions imposed by the community assemblies, enable informal rental and sales markets to operate.
- The establishment of a simple local land administrative system within a national institutional structure.

In addition, land registration certificates should be issued for 'common property regimes' and held in trust by community assemblies. These should have opt-out mechanisms to lease or to convert common property to other land uses or tenure systems.

Create unitary and democratic local governance institutions

A single local democratic institution at the grassroots level is required as a basis for making legitimate decisions regarding land issues on behalf of the community. As a first step, ownership of communal land that vests in the state should pass to the people who use it, invest in it, and whose livelihoods depend upon it. Communities, for their part, should form themselves into democratic village assemblies that can, within a broad regulatory framework, decide for themselves the path and pace of change in land tenure arrangements.

Priority for land tenure reform should be given to those communities that have met certain criteria, such as establishing their own governance and administration structures, that have reached agreement on village boundaries, and that have decided to proceed with a land-reform programme. Such a requirement would be both an incentive and a measure of a community's commitment and ability to embark on the slow and rocky path towards land tenure reform.

Building local land administration capacity

A local capacity to administer village land affairs, which is nested in higher levels of land administration, should be established at ward level. The World Bank (2003) argues that local institutions are needed to reduce red tape and resist powerful vested interests. According to an earlier World Bank report,

‘The creation of effective local land administration institutions is a precondition for serious planning for change in land administration in the communal areas ... If there is no effective implementation in these new, lower level institutions, it will do little good for central ministries to indulge in excessive planning. This applies to both tenure and land use planning.’ (1991b: 69)

In order to meet the costs of its administration, the ward assembly should be empowered to raise revenue by levying a small tax on land or a unit (flat) tax on households. This tax is both a participatory and a pedagogical device that not only enables and sustains sub-district administration, but it empowers poor citizens by giving them a voice in village affairs. It will therefore make village authorities more accountable for their decisions and actions.

Increase security of tenure to facilitate rental markets

While customary land rights are generally secure, they cannot be traded and exchanged beyond the community. But, while formal title may be legal in traditional settings, it may be neither cost-effective nor legitimate. In Kenya, for example, foreclosure on small farmers may be legal, but it has lacked local legitimacy (Alden Wily, 2006). Moreover, the underlying value of small pieces of land may not warrant the high survey, administrative and enforcement costs in circumstances where legal title may not be legitimate. An alternative, suggested earlier for resettlement, is the use of certificates of registration because they offer many of the benefits of formal rights, but at much lower cost. They

could be used, for example, as collateral with state institutions and the informal credit markets, but with reduced transaction costs. But the key attribute of certification and the increase in tenure security is that they would open up the potential to commercialize the communal areas through rental markets and create opportunities for migration.

Economists generally credit short-term land rentals with considerable potential to enhance agricultural productivity because they allow more productive farmers to acquire more land at lower transaction costs. This permits other landowners to leave the communal areas in order to participate more fully in the non-farm economy, or to use their rental income as a pension. Unlike land sales, rents require a more limited capital outlay, thereby leaving more resources for farm inputs. Evidence therefore suggests that temporary land transfers have a positive impact on equity, being generally pro-poor and beneficial for women (Place, 2002). Rental markets would require the establishment of a simple low-cost local administrative system, discussed earlier, to register informal transfers and rental transactions. Over time, as the rental market matures, the more productive farmers may wish to consolidate their holding by buying land that they previously rented. Given that the underlying value of the consolidated landholding rises, it may prove worthwhile for farmers to upgrade and upgrade their land to freehold title. This would not only give greater security of tenure, but the farmer would have access to formal credit markets for loans.

Financing for farmers

The collateral benefits of greater land tenure security on smallholder financing will take some time to develop. Alternative financial arrangements will therefore be necessary during the immediate post-crisis recovery period. To overcome the acute shortage of farm inputs, lines of credit could be opened for the private sector to ensure that adequate supplies of seed and fertilizer are made available to commercial farmers. Donor funds could then be channelled through the

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Land Fund (or similar revolving fund) to existing financial institutions, such as Agribank, that have a history of providing concessionary loans to small-scale commercial and A2 resettlement farmers.²⁴ With regard to smallholders, it may prove necessary to use the existing network of NGOs, known as C-Safe, to distribute seed and fertilizer packs with the food aid they provide to poor communal and A1 resettlement farmers. Alternatively, small cash grants could be made to these households. In effect, this would be a cash transfer to allow households to not only buy farm inputs, but possibly food, medicine or other necessities, bringing relief from the general deprivation that they have suffered recently. This would also provide an injection of capital into rural areas, where multiplier effects would stimulate the rural economy.

As the country begins to recover, different approaches to financial support to smallholders in the communal areas could be considered. For example, conditional cash transfers or basic income grants could be made to rural households to prevent them falling into destitution (Kakwani, *et al.*, 2005; Ferguson, 2007). Other recommendations, given in the chapter on the financial sector, include the development of commercial microfinancing enterprises and commercializing the People's Own Savings Bank to provide agricultural financing for smallholders. The most promising proposal, however, is the provision of credit and inputs for smallholders through corporate out-grower (contracting) schemes that could cover commodities from cotton, tobacco and horticulture to commercial forestry, poultry and ostrich farming – and much more.

In the medium to long term, land tenure reforms should begin to make themselves felt and farmers could begin to use their land as collateral. Both local informal credit markets as well as formal private financial markets could play an increasing role in

providing different types of loans to suit the various investment requirements of farmers.

Establish common property regimes over natural resources in communal areas

The medium term prescription for open access to natural resources and the externalization of costs is to convert them into 'common property regimes'. Central to this process is the exclusive control by a relatively small group of users over specific and bounded natural resources to encourage greater common responsibility for land use and resource management (Bromley, 1989). A common property regime requires a small group of users to enforce rules over resources within a particular area. Costs can be internalized by imposing a user fee, such as a stumping fee, or by a 'cap and trade' mechanism whereby the number of livestock to be grazed on a particular pasture is limited and the right to graze can be traded.

Unfortunately, these common property resource-management schemes are notoriously difficult to implement effectively. As there is no mechanism to determine, *a priori*, whether the 'correct' (shadow) price has been set for user fees (or the cap on livestock numbers), the inclination is to set them too low. This means that externalities will not be properly internalized, and the resource will continue to be depleted. Despite these problems, the common property regime remains an important first step in the event that a community should decide to transform the common property scheme into more individualized land rights. In this case it would be essential that the decision is consciously taken by the assembly, which must have clear and transparent mechanisms for making the change (World Bank, 2003). In Mexico, for example, a 75 percent majority of the *ejido* assembly can decide which of the community lands should be parcelled out to individuals and which should be held in common property (World Bank, 2002).

²⁴ Scrupulous oversight would be necessary to ensure that any previous biases in providing loans have been eliminated, and that every loan application is treated fairly and transparently on its own merits.

9.4.4 Strategic Objective 4

Dissolve the dual economy and create pathways out of poverty by a process of migration and structural transformation

Policy imperatives

The objective of reducing rural poverty is premised on gradually releasing more farmland to smallholders by decongesting the communal areas. A twin-track strategy

for alleviating pressure on communal land therefore rests, first, upon land tenure reforms that increase tenure security to facilitate a process of migration to non-farm employment opportunities in towns and cities (push factors). The second is strong economic growth to create non-farm jobs in rural centres and towns (pull factors). Box 9.2 illustrates these lessons from China.

Box 9.2: Lessons from China

When China started to reform its collective agriculture, it was largely a rural country in which 80 percent of its vast population lived in the rural areas. Today, only 60 percent do so. It is estimated that 200 million people have relocated from the rural to the urban areas. The first lesson that China provides is that this process of structural transformation is driven strongly by very high rates of economic growth in the urban-based industrial sector of the economy. Although its agricultural sector notched up impressive rates of growth of 6.3 percent annually between 1991 and 2005, it still lagged behind industry, which grew consistently above 10 percent per annum. This large productivity gap acted as a centripetal force, pulling rural migrants into higher productivity urban employment. Because they are now more productive and earn more, they have been an important source of growth and poverty reduction for China. The share of the population living beneath the 'cost of basic needs' poverty line in China declined from over 60 percent at the beginning of economic reform in 1978 to just 7 percent in 2007 (Dollar, 2008).²⁵

These powerful pull factors are sometimes seen as sufficient conditions for structural transformation, suggesting that policy makers can ignore the need for rural land tenure reform. Here, again, China's experience is instructive. The Chinese government disbanded its agricultural collectives by introducing a 'household responsibility system' that created family farms and strengthened farmers' land tenure rights. But, despite having private property rights enshrined in its constitution in 2004, and the passage of a new property rights law in March 2007, farmers land rights remain limited to renewable 30 year land-use leases. According to one commentator:

This new law will not bring the full property rights revolution China's development demands. Indeed, it will not meet the most crying need: to give peasants marketable ownership rights to the land they farm. If they could sell their land, tens of millions of underemployed farmers might find productive work. Those who stay on the farm could acquire bigger land holdings and use them more efficiently. Nor will the new law let peasants use their land as security on which they could borrow and invest to boost productivity. Nor, even now, will they be free from the threat of expropriation.²⁶

Indeed, it was large-scale expropriations of farmland for housing and factory construction that rendered millions of farmers landless, while enriching those who acquired it. As a result, land disputes have become a leading cause of social unrest, sparking thousands of protests across China by poor farmers outraged at the expropriation of their land for negligible or no compensation. The main reason for the widespread opposition within China to the property rights law was that it allowed continued expropriation of the farmer's land, while entrenching and protecting the rights of those who had appropriated it. The other lesson from China, therefore, is to initiate the process of granting farmers land rights at the earliest stages of reform in order to protect their land rights and to allow them to benefit from them.

²⁵ The World Bank's 'cost of basic needs' poverty line is based on the minimum consumption that a person needs; 2,100 calories per day plus other basic necessities of life.

²⁶ *The Economist*, 8 March 2007. Leader: 'China's next revolution' (p.11).

Create pathways out of poverty by decongesting the communal areas

It was shown earlier (Figure 9.4) that there is a strong and robust statistical relationship between the amount of land available to a household and its income from farming. When farms are very small, the household's priority is to meet its subsistence requirements by growing maize. As farms get bigger – towards 10 acres (4 ha) – more land is available for cash crops, such as cotton. Commercialization begins to emerge as the area set aside for growing food is minimized and household food security is based on the income from crop sales. More land must therefore be made available to those smallholders committed to farming if poverty in the communal areas is to be reduced significantly. However, this is more likely if those households who are interested in alternative (non-farm) livelihoods are allowed to convert their rural assets (land) into urban assets (land and capital). This requires that the underlying value of the land must be unlocked by communal land reforms that grant households more secure tenure over their land, which allows them to either rent or sell it. In the words of the World Bank:

'As opportunities in the non-farm economy increase, land markets allow households to engage in migration, specialization, investment, and inter-generational land transfer, thereby improving productivity and participants' earnings. Households with low agricultural skills are likely to be able to obtain higher incomes from off-farm employment than from farming, and thus will be better off if they rent out some or all of their land for others to cultivate.' (2003: 86)

These push factors from the communal areas must be matched by pull factors from rural centres, towns and cities: that is, strong economic growth to create employment

opportunities in micro or small enterprises and in the formal sectors of the economy. Without this solid growth households will simply substitute rural poverty for urban poverty in a 'migration of despair' (OECD, 2006). While sound economic policies are a necessary condition, they are not sufficient. They must be supported by social policies that channel non-farm activities into sustainable urban livelihoods, address the need for secure and affordable housing, and provide social services and utilities that root families in the urban environment.

Create a ladder of opportunity and a missing middle

A ladder of opportunity is presented by an agrarian structure where the smallest producers can gradually expand their farming operations, either through consolidation – for example, when they buy smaller neighbouring farms – or by buying a bigger farm elsewhere. There are two major conditions for this to apply:

- A land rental and sales market must allow farmers to transfer secure land rights from one person to another.
- The agrarian structure must consist of many farms of different sizes, so that the smaller producers can afford to take a series of small steps over time (up the ladder) to expand their farming operations.

Neither of these conditions currently prevail in Zimbabwe, which is characterized by a dual structure, with many tiny plots in the communal farms alongside large commercial farms. Although the FTLRP has perversely broken the mould of the dual agrarian structure to some extent, the absence of secure tenure precludes land transfers through a market. The objective therefore is to establish institutions and mechanisms for a land market to operate and create a 'missing middle'²⁷ so that, according to Hayami:

²⁷ See chapter 6 on private sector development.

‘...the agrarian structure of developing economies will gradually shift from the present bifurcated system to a unimodal structure where the middle class is dominant and in which even the landless labourers have a chance to ascend.’ (1989: 753)

The task ahead, therefore, is to transform the agricultural sector by gradually dissolving the dual agrarian structure by facilitating the consolidation of the many small communal land plots, while encouraging the subdivision of larger underutilized commercial farms. Eventually, a unimodal agrarian structure with a range of different farm sizes – but mostly medium-sized farms – should emerge. The first imperative, therefore, is for a land tenure reform programme in the communal and resettlement areas to provide secure tenure as a basis for a land market. It is this land market that will provide the mechanism for the amalgamation of very small plots into larger more viable units. The second imperative is to facilitate corresponding subdivisions of large underutilized commercial farms into smaller, more intensively utilized units through a land tax, discussed later in this chapter.

Growth centres as focal points for transformation

As communal and resettlement farmers begin to consolidate their holding and increase production, their earnings and their demand for a range of goods and services will rise. These goods will include agricultural inputs, such as improved hybrid seeds, fertilizer and capital equipment to improve productivity. They will also begin to include financial services, such as banking facilities for savings and loans. A growing prosperity among farmers would also place a demand on improved social services and infrastructure: better schools and health services, along with communications, roads and water supplies. Increased local agricultural production would also open up opportunities for the private sector to establish marketing outlets or agro-industrial

processing plants, whose size and sophistication could vary from small-scale processing plants, such as grinding mills, to more complex processing plants for the export of high-value goods. In this way, rural centres could become the focal point for the supply of goods and services for farmers, as marketing and processing centres for their production, and as destinations for migrants to live and work. Migrants could either find jobs or manage micro and small enterprises: trading, making goods or providing services.

This structural transformational scenario, however, is conditional upon:

- The evolution of communal land tenure security and land markets, both within the communal areas and rural centres.
- Land-use planning of rural centres to allow for the provision of infrastructure and social facilities.
- A commitment by government to plan and supply infrastructure and social services to growth points and other rural centres.

Along with these conditions is the need for a democratic local government framework that facilitates the growth of a civic culture.

While the synergetic effects of private, local authority and government investment would augment and concentrate rural skills and incomes in rural towns, communal land would be consolidated into ever larger holdings. Eventually, the complementary growth linkages between farm and town would result in a spatial metamorphosis as the distinction between farms and rural centres becomes more sharply defined. As the development of the symbiotic economic relationship between centre and hinterland matures, farm incomes should continue to rise and higher order goods demanded. The urban response would be to draw in more resources and diversify its activities, thereby increasing the town’s functional complexity and lending it a self-sustaining polarity. Over

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time, this process will allow rural centres to develop into small towns that have the essential services to support a vibrant farming community.

9.4.5 Strategic Objective 5

Increase and sustain agricultural productivity and growth

Restructure land and agricultural institutions

Sustainable agricultural growth will be dependent on efficient and effective public agricultural institutions. The establishment of a Land Commission will include the functions of land reform and resettlement, obviating the need for a ministry to perform the same functions. It seems evident, too, that the three agricultural ministries will need to be rationalized and restructured to increase their coordination and effectiveness. One obvious solution would be to create a single Ministry of Agriculture that incorporates the functions of the Ministry of Agricultural Engineering, Mechanisation and Irrigation and the Ministry of Water Affairs and Infrastructure. The current Ministry of Agriculture, with its 10 departments, also needs a simpler organizational structure. It could probably be reduced to four departments: veterinary services and livestock development; agricultural research and extension; agricultural water resources and irrigation; and finance and administration. Agricultural economics and engineering could fold into the department of Agricultural Research and Extension (AREX). Clearly, any final organizational structure will need to be discussed within the Ministry itself and be decided by the government.

Effective research and extension services

Zimbabwe needs to develop a demand-led, farmer-centred agricultural research and extension programme, as well as strengthen links between public, international and private research organizations. In their review of research in Zimbabwe, Tawonezvi and Hikwa

attribute past successes, first, to long term, focused and uninterrupted programmes; secondly, to strong and consistent government support and funding; and, third, to the active participation by farmers pressing for the type of research and extension that would benefit them most. They also believe that, 'It is necessary now more than ever to involve universities, the private sector and farmers in order for research to be demand-driven' (2006: 209). Funding for research, for example, could be augmented by contributions from farmers' unions, commodity associations and agricultural companies. If research is to be pro-poor, it should not only examine how farmers within the traditional agricultural system can become more technically efficient, but how the system itself can be transformed and commercialized.

The private sector should play a key auxiliary role in extension. Companies, eager to market their products – such as seed, fertilizer, chemicals and equipment – are excellent extension vehicles for disseminating agricultural information that could complement government efforts. The seed and fertilizer companies have, in the past, been successful agents of technological change through innovation diffusion by the supply of their products to communal area farmers. Cotton and tobacco marketing companies have, through contract schemes, also been advising growers on the use of new varieties and techniques to improve yields for their mutual benefit. For its part, the government should move away from its sprawling, costly and inefficient organizational structure and develop a more professional, cost-efficient and focused approach to extension, applying innovative techniques and working closely with the private sector and farmers.

Allow greater flexibility in farm sizes

Zimbabwe's resettlement programmes have in the past been based on standard farm sizes. In 1999 the government specified the maximum farm sizes allowed for different Natural Regions. According to Bruce, however, scale 'will vary not only by crop,

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but by land capability, and capital and labour endowments of the farm firm'. Because farm size varies with a multitude of factors, 'any attempt to stipulate it will necessarily involve substantial inefficiencies' (1990: 25). In economic terms this means that it is more efficient to allow factor markets to reflect scarcities through the price mechanism so that they are allocated efficiently on the basis of their relative marginal costs. Zimbabwe should therefore move away from the rigid, centrally imposed A1 and A2 resettlement models, based on standardized farm sizes, and opt for a more flexible approach. Yet it may be necessary, at least in the short term, to continue with administratively determined farm sizes to bring order to the disarray caused by the FTLRP. Once markets begin to operate, farms – aided by a land tax – should stabilize at their optimum sizes. Similarly, single-farm ownership should continue to apply for a prescribed period – of say, seven to ten years – after which date this limitation could be lifted.

Productivity gains from a land tax

A land tax has many advantages over ceilings on farm sizes set by bureaucrats. As a progressive land tax does not distort commodity prices, it is generally favoured by economists because:

'Conceptually, progressive land taxes would be more appropriate for reducing the tendency to hold land unproductively than land ownership ceilings. Taxes could reduce the scope for land speculation and induce large landowners to sell out or to use their land more intensively.' (World Bank, 2003: 168)

It encourages the full utilization of land because those wishing to hold agricultural land would have to ensure that returns from farming outweigh the tax paid on the land. Another advantage of a land tax is that, unlike most agrarian reforms that tend to impose a financial

burden on the state, a land tax generates revenue. Despite these advantages, land taxes have two major drawbacks: they are difficult to introduce and costly to administer. The watchword for introducing a tax is, therefore, simplicity. Policy-makers have suggested innovative methods of making the land tax administratively more simple and effective. For Zimbabwe, Doré (1993) proposed a simple 'insurance' tax evaluation method based on self-assessment.

To make a land tax more politically acceptable, a proportion of the proceeds should be allowed to accrue to villages and other local authorities. This could strengthen local capacity for land administration and transfers, as well as improve delivery of public services and the provision of infrastructure. Evidence presented by the World Bank (2003) suggests that greater local autonomy in setting tax rates can be highly desirable. Taxes on land provide an ideal mechanism for encouraging the more effective use of land, while the authority to set rates enhances local fiscal responsibility by making officials more accountable, thus strengthening the voice of the local population.

Pro-poor growth

As we argue elsewhere, it is the level of employment that defines the extent to which economic growth can be considered 'pro-poor'.²⁸ Mellor (2000) investigates three major sources of employment growth in agriculture: (i) yield-enhancing technology; (ii) increased land area; and (iii) a change in the composition of output to high-value commodities. As yield-enhancing technology has a relatively low elasticity of employment, and because land frontiers are reached relatively quickly, he argues for greater emphasis on the production of high-value commodities – particularly horticulture and livestock. This, he believes, can generate strong growth of between 4 and 6 percent per annum. And, because the agricultural sector in low-income countries (like

²⁸ See chapter 7 on labour markets.

Zimbabwe) are so large, it adds immense purchasing power to small farmers. It is the expenditure of this increased income on locally produced, labour-intensive, non-tradable goods and services – expanded housing, personal services, increased primary education, health services and local transport – that drives employment creation in the non-farm sector, underpinning broad-based poverty reduction. With this spurt in employment growth, labour markets tighten quickly in the local non-farm sector, causing real wages to stir and rise. That is why, claims Mellor, poverty declines so rapidly with increased agricultural output.

Improved market access for smallholders

Improved market access begins with rural infrastructure – roads, transport and communication networks – as conduits for agricultural supplies and commodities, as well as market information. The second requirement for smallholders is to secure investments in low-cost irrigation schemes based on appropriate technologies to produce high-value crops with both strong local demand and export potential. Groundwater supplies (boreholes, wells) and surface-water supplies (dams) should be developed or upgraded for productive purposes once the smallholders have established a maintenance mechanism for the scheme. An environmental plan would also help prevent silting and thus preserve the economic value of a water resource, such as a dam. And, third, smallholders can improve their access to higher-value export crops through corporate–smallholder partnerships (also known as contract farming or out-grower schemes). There are many examples of successful smallholder corporate partnerships in Africa. These vary from dairy projects in Kenya, forestry projects in South Africa, and tobacco production in Malawi. In Zimbabwe, models have been developed for smallholder partnerships in such diverse areas as horticultural and cotton production

and ostrich farming. In the initial phases, smallholders could provide land, water and labour for production, while the finance, extension services and marketing would be provided by corporations. Over time, as smallholder production develops, the more lucrative higher-level activities (further up the value chain) could be entered into by growers themselves.²⁹

The private sector's role in supplying inputs and marketing

Only a small proportion of smallholder production can be geared to produce high-value crops. Their production of other crops, such as maize, will benefit from more conventional agricultural input and marketing services. In order to avoid an unsustainable dependence on subsidies, a preferable alternative would be to develop markets where companies compete for the farmers' production, as well as the farmers' custom for their supplies of seed, fertilizer, chemicals and machinery. Through effective marketing the Seed Company was able to diffuse their hybrid seed to nearly all communal farmers during the 1980s. Fertilizer companies have established warehouses for smallholders where it was profitable to do so, while others have promoted their products through rural agents and outlets. These warehouses could also serve as commodity collection points.

Recruit, retain and develop farming skills

The success of agriculture is critically dependent on retaining the technical and managerial skills of experienced farmers and developing the skills of new farmers. Opportunities should also be created for the many former students who have passed through Zimbabwe's agricultural training schools. Those farmers and workers who were displaced by the FTLRP should be encouraged to return and lend their skills and experience to the rebuilding of agriculture.

²⁹ This has been achieved by forestry plantation growers in South Africa, including smallholders.

9.5 SEQUENCING OF LAND REFORM AND AGRICULTURAL RECOVERY POLICIES

Each of the five strategic thrusts, discussed above, focused on policy imperatives rather than the sequencing of recommendations. This section therefore briefly prioritises activities for recovery and reconstruction, starting with ‘quick wins’ from emergency post-crisis assistance, to short and medium term recovery strategies, to long term and generational objectives, such as structural transformation. Caveats are in order. First, brevity dictates that these categories are broad, incomplete, notional and flexible. Second, some activities are crucial at the earlier stages if long term and generational changes are to come to fruition. Third, it is not so much the pace of change that is critical, but the direction of change. And fourth, emphasis is placed on immediate activities rather than more distant ones.

9.5.1 Emergency relief and production (12 months)

Immediate measures will be needed to bring emergency food relief and get agricultural production underway. Food security is the top priority. The government must seek the support of the humanitarian community to secure food for distribution through the World Food Programme (WFP), C-Safe and other NGOs. The objective must be to fulfil their programme of food distribution to an estimated 5.1 million people by April 2009. Concurrently, restriction should be lifted on private sector trading to allow imports of food and trade between surplus and deficit districts, thus ensuring that households with purchasing power can access food through the markets (FAO/WFP, 2008). Competitive food markets would also help bring the cost of food down.

The second imperative is to get agricultural production moving. Seed and fertilizer packs, dipping chemicals to control tick-borne livestock diseases, and/or cash transfers

could be distributed through C-Safe’s network to boost smallholder agricultural production. Donor funds could also be channelled through a special fund to Agribank to provide concessionary loans to small-scale commercial and A2 resettlement farmers for their farm inputs needs. Lines of credit to the private sector should make seed, fertilizer, fuel, chemicals and equipment available to commercial farmers through commercial banks at market prices. Balance of payment support will be needed to tackle Zimbabwe’s energy crisis, primarily fuel for tractors, coal for curing tobacco, and electricity for irrigation and the manufacture of fertilizers. It is not just fertilizer factories that desperately need power, but the phosphate mines on which fertilizer factories depend.

9.5.2 Short term measures (1–3 years)

Food aid, as it is now delivered, should be wound down and phased out while more sustainable approaches to food security are put in place. These include:

- Liberalizing the trade in food, both domestically and internationally, and allowing farm input and commodity markets to operate competitively.
- Improving famine early warning systems and the targeting of beneficiaries, and establishing clear emergency food distribution mechanisms.
- Promoting smallholder production through improved extension services, well-maintained infrastructure, and widening the scope of corporate-smallholder outgrower (contract farming) schemes.

In addition, the government should undertake a comprehensive review of the relative benefits, feasibility and sustainability of conditional cash transfers and basic income grants as possible methods for improved household food security, social protection and development.

*IT IS NOT SO MUCH
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Any announcement of pre-planting prices as a crop production incentive is meaningless in a hyper-inflationary environment. An alternative approach – preferably in the first 2 years only – could be to express pre-planting prices in US dollars or rand (set approximately at purchasing power parity), but payable in Zimbabwe dollars at the time of delivery. Once the imperative of macro-economic stability has been achieved, pre-planting prices could be quoted in Zimbabwe dollars until such announcements are abandoned in favour of more market driven approaches.

The key short term measures – that will allow the process to unfold, and therefore need to start immediately – are the legislative changes to create the institutions whose activities are crucial for getting recovery underway. Foremost amongst these is the enabling legislation for the creation of a Land Commission, whose most urgent task will be a thorough land audit. Until this audit has been completed, it will be difficult to move forward and rationalize the occupation of farmland, provide loans for rebuilding farms infrastructure, and provide secure tenure to farmers. Concurrently, a Land Fund and Tribunal should be established, while the oversight functions and mechanisms of Parliament and the Office of the Comptroller and Auditor-General should be strengthened. The Ministry of Agriculture will need to be restructured so that the task of building capacity, especially in agricultural research and extension, can be resumed as soon as possible.

9.5.3 Medium term recovery (3–5 years)

Gradually, the government should move away from announcing pre-planting and minimum support prices, and allow the market to govern commodity prices. In a bid to reduce volatility in staple food prices and protect the poor, the government, through a restructured and commercialized GMB, could enter the market in surplus years, when prices are depressed, and sell onto the

market in deficit years, when prices are high. This would dampen price volatility, enable the government to maintain a sufficient level of buffer stocks in case of emergencies, earn a profit on its transactions, and export its surpluses.

This phase of recovery should also consolidate the gains of restructured agricultural institutions. A solid foundation should have been laid for robust and sustainable agricultural growth based on more competitive input and commodity markets, as well as agricultural research and extension. Likewise, the new land institutions – the Land Commission, the Land Fund and the Land Tribunal – should have moved beyond legal, organizational and funding concerns, to the planning of a sustainable land reform programme, implementing a transparent settler selection and farm allocation programme, and introducing a land tax in the commercial areas. It should also see the stirring of a land market, the beginnings of innovative financial arrangements based on secure tenure, heightened farm investment and greater productivity in the resettlement and commercial farming areas.

Once the land reform programme is underway, the Land Commission should turn its attention to establishing the legal and regulatory framework for land tenure reform in the communal areas.

9.5.4 Long term strategies and reforms (5–15 years)

Land tenure reform would begin by translating communal land policies into a workable legal and institutional framework. An unfolding programme would legislate the transfer of *de jure* ownership of the communal areas into the hands of community assemblies, which would have jurisdiction within adjudicated and demarcated boundaries. These steps could then be followed by the establishment of common property regimes and the registration of residential and arable land using low cost technologies. At the same time, a land or

unitary tax levied on smallholders would contribute to local administrative mechanisms to register land and the transfer of land through rental and sales markets.

By this stage, investments in rural social and physical infrastructure should have helped boost agricultural production and put it firmly on a path of sustainable growth. Smallholder farmers and small-scale enterprises are likely to have been weaned off subsidized state financing by restructuring in the financial sector. Agricultural loans would have become available through various channels, such as a restructured POSB, Agribank, contract farming, and microfinancing institutions. Informal credit based on the collateral value of communal plots should have become more common. Food handouts and other social protection measures for the most vulnerable households may have been replaced by conditional cash transfers or basic income grants, possibly administered through the POSB.

9.5.5 Generational change and structural transformation (15–50 years)

Over the coming decades most residential and arable land in the communal areas should have been registered. As the land market starts to develop and operate, small farms could be consolidated into larger holdings, while other families decide to migrate to urban centres in search of jobs and employment opportunities. Gradually, the larger and more profitable communal farms are likely to opt for freehold title; communities may decide to convert their common property regimes into individual land rights; and the communal areas will slowly decongest. As registered title becomes the norm, formal private sector financing based on the collateral value of land should become more common. Eventually, a unimodal agrarian structure should start emerging in Zimbabwe, with farm sizes ranging from the very small to the very large, but consisting mainly of medium-sized family farms. At this point, growth points and rural service centres

should have been transformed into small towns.

If this transformation process seems too far-fetched, we need only think of China, whose reforms started 30 years ago. Zimbabwe is not China, and is unlikely to follow China's path or its heady pace of development and modernization. But Zimbabwe has the human, capital and natural resource potential to grow and develop steadily into a transitional economy and shed its dependence on aid.

9.6 CONCLUDING REMARKS

Most of the recommendations in this chapter are not new. They are broadly a continuation of the seminal work of the Land Tenure Commission chaired by Rukuni (Zimbabwe, 1994). It was the Commission that suggested that village assemblies be elected in communal areas; that villages be surveyed and mapped; that all communal arable and residential land should be issued with land registration certificates; that resettled farms be replanned and given title; and that freehold tenure should be maintained for all commercial farms. It was the Commission that first recommended that a Land Board or Commission be established together with a more decentralized system of governance and land administration. And it was the Rukuni Commission that suggested that all laws on land be consolidated and streamlined, and that an agricultural land tax be introduced. It also recognized the importance of promoting rural centres and growth points in a process of migration and rural transformation.

There is also much to commend the Zimbabwe government's own suggestions in June 1998, when Phase II of the resettlement programme was being planned (Zimbabwe, 1998a). It, too, took on board recommendations from the Rukuni Commission and the advice of its friends within the international community: that the identification of settlers would follow formal criteria which would be made public prior to the selection process; that A2 settlers

would be better-off smallholder farmers with demonstrated competency in farming, such as master farmers and agricultural graduates; that disputes between farmers and the government should be settled through an administrative land court; and that agricultural land-use plans would be prepared to facilitate demarcating, surveying, and the granting of title. And, crucially, the government's report reiterated the principles that resettlement had to be implemented in a transparent, fair and sustainable manner and that compensation had to be paid to farmers whose land was acquired.

Naturally, this chapter has also suggested some changes. Whereas the Rukuni Commission foresaw resettlement areas being granted state leases on farms with an option to purchase, it has been argued here

that these leases do not provide secure land tenure, nor do they unlock the collateral value of the land. An alternative has therefore been proposed. Drawing on a recent World Bank review of land policy and the work by Alden Wily for the UNDP, a two-stage process of providing secure tenure was recommended for both resettlement and communal areas (World Bank, 2003; Alden Wily, 2006). This has the added advantage of facilitating rental markets and migration to non-farm opportunities in rural and urban centres in a process of economic structural transformation. In essence, therefore, the chapter has tried to recapture the broad consensus reached on land policy before the crisis deepened after 2000. This, it is hoped, will provide a solid foundation to construct a way forward that brings economic and social recovery for the benefit of all Zimbabweans.

Chapter 10

Restructuring of Public Enterprises, Infrastructure and Housing

This chapter focuses on the restructuring of public enterprises, and the infrastructure and housing sectors in Zimbabwe. An overview of global trends is provided, highlighting the fact that privatization, the main form of restructuring peaked during the 1990s and tapered off thereafter. It is argued that there has been an over-emphasis on the benefits of privatization, and the pendulum has since swung back to a more cautious approach, especially with respect to infrastructure. The global emphasis is no longer on pursuing privatization from a doctrinaire perspective, but rather taking a more eclectic approach (World Bank, 2004 and 2005; OECD, 2004; Nellis, 2006; UNDP, 2007; Gomez-Ibanez, 2007). According to Kikeri and Nellis (2004: 87)

‘Mounting empirical evidence of privatization’s benefits coincides with increasing dissatisfaction and opposition among citizens and policymakers. This dissatisfaction reflects the growing questioning of the benefits of privatization, the general downturn of global markets in the past few years and the resulting swing of the pendulum back toward increased governmental supervision, the over-selling of privatization as a panacea for all economic problems, and the concern that privatization does not produce macroeconomic and distributional gains equivalent to its microeconomic benefits.’

The public enterprise, infrastructure and housing sectors in Zimbabwe are then analysed, tracing their past performance and experiences with restructuring. Even though public enterprise reforms were a central tenet of the reform period beginning in 1991, the process was characterized by inertia

and serious implementation challenges, resulting in limited progress. The lack of maintenance, replacement and new investment in infrastructure resulted in a marked deterioration in its quality, and the neglect of the housing sector has created serious shortages of shelter and prohibitive rental and housing prices. The constraints to past growth and future recovery are then considered, and include legal and institutional aspects (overlapping and unclear roles and functions), policy, capacity (physical and human capital) and policy constraints.

Key broad strategic objectives are identified and strategic thrusts derived from them. For each of these a set of policies – a policy package – that includes measures for recovery, is advanced.

10.1 OVERVIEW OF GLOBAL TRENDS

The post-World War II period, and especially the 1950s and 1960s, saw governments around the world actively direct and control their economies (*dirigisme*). The scope of the public sector was expanded during this period, especially through the establishment of public or state-owned enterprises and parastatals. However, results did not match expectations, as political considerations overrode economic ones, resulting in public enterprises becoming a drain on the fiscus and being kept afloat through subsidies.

Owing to the widespread failure of public enterprises, a new market-oriented thrust replaced the hitherto popular statist approaches, finding political expression with the coming to power of Margaret Thatcher in the UK in 1979 and Ronald Reagan in the

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USA in 1981. This marked a period of neo-liberal revival that is unprecedented in recent history. The process of rolling back the State gathered momentum, with waves of privatization sweeping across continents. Structural Adjustment Programmes (SAPs) adopted by the World Bank and the International Monetary Fund (IMF) in the 1980s insisted that loan recipients privatize public enterprises. The pendulum swung decisively in favour of a minimalist state, with a focus on market (private sector) led development.

Over the period 1990–1999, global proceeds from privatization amounted to US\$850 billion, rising from US\$30 billion in 1990 to US\$145 billion in 1999. Proceeds from privatizations were lower in the new millennium, at US\$282 billion between 2000 and 2006.¹ Latin America and the Caribbean accounted for the bulk of privatization proceeds at 55 percent (the largest sales emerging from the sale of infrastructure and energy firms in Argentina, Mexico and Brazil), followed by Eastern Europe and Central Asia (21 percent), East Asia and the Pacific (14 percent), South Asia (4 percent), the Middle East and North Africa (3 percent), and sub-Saharan Africa (3 percent). In sub-Saharan Africa, sales of state enterprises rose from 175 in 1990 to more than 400 in 1996 and to more than 2,200 by 1998, concentrated mainly in Mozambique, Angola, Ghana, Zambia, Kenya, Tanzania and Guinea. Sales from Africa accounted for 3 percent of total sales from developing countries during the period 1990–1999 (Kikeri and Nellis, 2004).

For the period 1990–1999, privatization revenues were estimated to be US\$9 billion for 37 sub-Saharan African countries, less than that realized by sales in New Zealand alone, and under a third of what was realized

from two auctions of Brazilian telecommunications companies in the mid-1990s. A total of 979 privatizations occurred in sub-Saharan Africa between 1988 and 2003, with a total value of US\$11.7 billion, compared to privatization receipts amounting to US\$195 billion in Latin America over the same period (Nellis, 2006). More recent data show that, during the period 2000–2006, sub-Saharan Africa raised \$8.3 billion, 3 percent of the total for developing countries. Most privatization initiatives in sub-Saharan Africa have been at the behest of the Bretton Woods Institutions. It has been observed that 70 percent of all SAPs during the 1980s contained a privatization component (Cook and Kirkpatrick, 1995).

10.2 PUBLIC ENTERPRISES, INFRASTRUCTURE AND HOUSING PROVISION IN ZIMBABWE

10.2.1 The public enterprise sector in Zimbabwe

At the advent of independence in 1980, Zimbabwe inherited a large number of parastatals. These were present in all sectors of the economy, notably agriculture, mining, transport, energy, communications and finance. According to the State Enterprises Restructuring Agency (SERA), in 2006 there were 76 public enterprises.² More than 60 percent of the parastatals had been inherited from the Rhodesian administration. Thus, unlike the experience in most African countries after independence, Zimbabwe did not expand its parastatal sector through nationalization and expropriation but rather through the creation of new bodies.³ According to the Reserve Bank of

¹ Detailed data on privatization transactions and proceeds for the period 2000–2006 are available at <<http://rru.worldbank.org/Privatization>>. The data do not include non-cash transactions such as the use of vouchers.

² The Privatization Agency of Zimbabwe (PAZ), established in 1999, changed its name to the State Enterprises Restructuring Agency (SERA) in 2005. See <<http://www.sera.co.zw>>.

³ In Zambia for instance, nationalization saw the number of public enterprises increasing from 14 at independence in 1964 to more than 150 by 1986, constituting 80 percent of the economy. The level was even higher in Tanzania.

Zimbabwe (RBZ) (2007), the parastatals and local authorities sector accounts for at least 40 percent of Gross Domestic Product (GDP), and their contribution to the economy is even greater given their backward and forward linkages with the rest of the economy.

The major public enterprises, in which government has 100 percent shareholding and those in which government has a stake through RBZ shareholding, are reported in Table 10.1.

Public enterprise restructuring in Zimbabwe

The restructuring of public enterprises, and in particular privatization, came to the fore in Zimbabwe following the shift in economic strategy from the highly interventionist approach of the first decade of independence (1980–1990) to a more market-based strategy under the Economic Structural Adjustment Programme (ESAP) in 1991. In the government reform blueprint entitled, ‘Zimbabwe: A Framework for Economic

Table 10.1: Major public enterprises

A. Those with 100 percent government shareholding		
1.	National Railways of Zimbabwe (NRZ)	
2.	Zimbabwe Electricity Supply Authority (ZESA)	
3.	Zimbabwe Iron and Steel Company (ZISCO)	
4.	Cold Storage Company (CSC)	
5.	National Oil Company of Zimbabwe (NOCZIM)	
6.	Zimbabwe National Water Authority (ZINWA)	
7.	District Development Fund (DDF)	
8.	Grain Marketing Board (GMB)	
9.	Air Zimbabwe	
10.	Agricultural and Rural Development Authority (ARDA)	
11.	Tel*One	
12.	Net*One	
13.	Industrial Development Corporation (IDC)	
14.	Zimbabwe Mining Development Corporation (ZMDC)	
15.	Minerals Marketing Corporation of Zimbabwe (MMCZ)	
16.	Central Mechanical Engineering Department (CMED)	
17.	Zimbabwe Defence Industries (ZDI)	
18.	Zimbabwe Development Corporation (ZDC)	
B. Those with a government stake through RBZ shareholding		
<i>Enterprise</i>	<i>RBZ shareholding (%)</i>	
1.	Astra Holdings	66
2.	Cairns	65
3.	Tractive Power Holdings	65
4.	Fidelity Printers and Refineries	100
5.	Export Credit Guarantee Company	100
6.	Aurex	100
7.	Sirtech	60
8.	St Lucia Park	50
9.	Homelink	100
10.	Old Mutual	8
11.	Dairibord	21
12.	Cotton Company of Zimbabwe	7
13.	Infrastructure Development Bank of Zimbabwe	16.75
14.	Tuli Coal	70

Source: Reserve Bank of Zimbabwe (2007: 3–4)

Reform 1991-95' the negative impact of parastatals on the fiscus was highlighted. The largest of the public enterprises, the four agricultural marketing boards,⁴ the NRZ, ZESA, ZISCO, NOCZIM, the Posts and Telecommunications Corporation (PTC) and Air Zimbabwe were singled out as the most dependent on the fiscus. A key objective of ESAP was the reduction of the budget deficit from 10 percent of GDP to 5 percent by 1994/95. To achieve this, government sought, among other measures, to eliminate the large budgetary burden caused by subsidies by making the public enterprises operationally efficient and more commercially oriented. Subsidies to public enterprises were targeted to decline from Z\$629 million (US\$231 million) in 1990/91 to Z\$40 million (US\$4.5 million) in 1994/95.

For the period 1986–1991 the country's largest parastatals received from central government subsidies and advances exceeding Z\$2 billion (US\$1.6 billion), which contributed to the high budget deficit that was in excess of 10 percent of GDP by 1991. The question is then, whether with such support, these public entities performed effectively. The total losses of public enterprises, which had declined between 1986/87 and 1987/88, increased by 48 percent in 1988/89 compared to the level in 1985/86. Clearly, the performance of state enterprises left a lot to be desired. As the ESAP blueprint document stated, 'not only do public enterprises absorb a large proportion of recurrent budgetary expenditure in direct subsidies, grants and advances from government, but as a group they produce very small returns, if any, on capital invested' (Zimbabwe, 1991: 1, Annex 1).

The ESAP blueprint identified the causes of the poor performance of parastatals as follows:

- Government pricing policies did not allow a number of public enterprises to cover their costs.

- Various Acts required government to finance public enterprises' deficits from the national budget, even when these deficits were due to mismanagement.
- Government usually failed to pay for the costs of investment or activities carried out by public enterprises for purely social reasons.
- The capital base of many public enterprises consisted largely of loans, resulting in a heavy debt-service burden.
- Boards of directors and managers lacked autonomy and accountability. Line ministries were involved in day-to-day decision-making in the areas of personnel, salaries, investment and purchasing decisions.
- Corruption and mismanagement.
- Internal financial control systems and external monitoring systems for public enterprises' performance were inadequate.
- Their boards did not always include the expertise needed for effective management.

When the economic reforms were implemented, the major objectives of public enterprise reform were not dissimilar to those applied elsewhere:

- Efficiency improvements and economic development through the attraction of foreign investment, technology and know-how and the harnessing and encouragement of local entrepreneurial skills.
- Generation of revenues through sales and leases.
- Use of a full range of options, including outright sale of shares and assets, leasing

⁴ The Grain Marketing Board (GMB), the Cotton Marketing Board (CMB), the Dairy Marketing Board (DMB), and the Cold Storage Commission (CSC).

and management contracts, and contracting out of services.

According to the reform blueprint, the specific action to be taken regarding privatization or commercialization would depend on the category into which a parastatal fell. These entities were grouped as follows:

- Category 1(a): Enterprises to be retained because of their social functions (the Forestry Commission and Grain Marketing Board).
- Category 1(b): Enterprises to be retained because of their promotional functions (such as the Zimbabwe Broadcasting Corporation and the Zimbabwe Tourism Authority).
- Category 2: Enterprises to remain wholly owned by the government for strategic reasons (such as ZISCO and Zimbabwe Defence Industries).
- Category 3: Enterprises carrying out commercial functions (such as the Dairy Marketing Board, the Cotton Marketing Board and the Cold Storage Commission).

According to the ESAP document, those parastatals in Categories 1 and 2 would only undergo commercialization, while those in Category 3 would be privatized.

When government adopted economic reforms in 1991, public sector and parastatal reform featured prominently. In fact, the reform blueprint emphasized the importance of ‘frontloading’ this aspect so as to reduce public expenditure quickly, thereby reducing the budget deficit. Frontloading such reforms also made sense in terms of sequencing the

reforms in that, without stabilization, measures to deal with adjustment would not work. This sense of urgency was echoed in all subsequent economic strategies,⁵ including the budget and monetary-policy statements presented since ESAP. In spite of such concerns raised at the highest level, nothing of significance has taken place with regard to public sector and parastatal reform.

Performance of public enterprises since the onset of the reforms

Despite the reform programme emphasizing the need for privatization and commercialization, it was not until 1994 that a policy paper on the subject was prepared by an inter-ministerial Cabinet committee established in October 1994.⁶ Box 10.1 reports on the few stories of success in restructuring public enterprises in Zimbabwe.

Ten years after the government first announced its policy to privatize and commercialize parastatals, they continued to make huge losses. In fact, the target of reducing the budget deficit to 5 percent of GDP by 1994/95 was missed by a wide margin, with the out-turn at 13.5 percent of GDP. This was explained partly by the continued deterioration in the overall performance of public enterprises, whose losses amounted to Z\$2 billion (4 percent of GDP) in 1993/94, and which in the 1997/98 financial year had reached Z\$11 billion (8.6 percent of GDP). The major loss-makers were NOCZIM (50 percent of the total losses), ZESA (20 percent), the Cold Storage Company (8 percent), NRZ (6 percent) and ZISCO (6 percent). The State Enterprises Restructuring Agency observed that the recent performance of public enterprises suggests a progressive decline (SERA, 2008).

⁵ The Zimbabwe Programme for Economic and Social Transformation (ZIMPREST), 1996-2000, and the Millennium Economic Recovery Programme (MERP), 2001-2002, referred to public enterprise reform as ‘unfinished business from ESAP’. Annex 2 (pp. 51-55) of ZIMPREST provides a timetable for the commercialization and privatization of 52 public enterprises. A similar timetable appears in MERP, with over 40 public enterprises to be privatized/commercialized.

⁶ Inter-Ministerial Committee on Commercialization and Privatization (IMCCP), ‘Privatization and Commercialization Policy and Strategy Paper’.

Box 10.1: Some Success Stories in Restructuring Private Enterprises in Zimbabwe

The domestic marketing of agricultural products was gradually liberalized. Initially, the three main agricultural parastatals, the Dairy Marketing Board (DMB), Cotton Marketing Board (CMB) and Grain Marketing Board (GMB) were, in 1994, converted into companies wholly owned by government, i.e., corporatization. In January 1995, government took over the accumulated debts of these boards to enable them to start with a clean slate.

Dairibord Zimbabwe Limited (DZL) was fully commercialized and registered under the Companies Act in July 1994, with government retaining 100 percent equity. Having been run for four years from 1994 to 1997, DZL was privatized through its listing on the Zimbabwe Stock Exchange in September 1997, with the counter oversubscribed. DZL has been a success story, as exemplified by the following:

- i) The company is highly profitable and well capitalized through its own funds.
- ii) DZL achieved real growth in sales volumes, both on the domestic and export markets: the company is a net earner of foreign currency.
- iii) Government is collecting corporate tax from it, and not subsidizing its operations.
- iv) Employee motivation is high as the company can now afford market-related conditions of service (RBZ, 2007: 9).

The CMB was commercialized in 1992. Cottco was registered in 1994 and realized profits in 1995, culminating in its privatization in 1997. The introduction of competition in 1995 allowed new cotton trading companies into the market, enhancing efficiency in the sector. Thus, Cottco is also a success story, as evidenced by the following:

- i) It is now one of the blue-chip companies listed on the Zimbabwe Stock Exchange.
- ii) The company is one of the top exporters of cotton.
- iii) The opening up of the cotton sector has enhanced competition resulting in increased cotton output and fair compensation to growers (RBZ, 2007: 10).

The government raised over Z\$2 billion (US\$100 million) through the sale of Dairibord Zimbabwe Limited, the Cotton Company of Zimbabwe, the Commercial Bank of Zimbabwe (1997), the Zimbabwe Reinsurance Corporation (1999) and the Rainbow Tourism Group (RTG) (1999). The main method used in these privatizations was a public share offering (in the case of Dairibord, Cottco, CBZ and RTG). Other methods used in conjunction with the public share offering included Employee Share Ownership Plans (ESOPs) in the cases of Dairibord, Cottco and RTG, in which management and employees participated.

As a result of their deteriorating performance, public enterprises have experienced a high staff turnover, especially in critical technical and financial areas, which has undermined their operations. It is often the case that staff remain in an acting capacity in key executive positions for long periods. Some public enterprises go for long periods without boards, effectively being run from the parent ministry. An example of the skill shortages at the public enterprise level is illustrated by the human resources audit of the National Railways of Zimbabwe (NRZ) in 2007 (Table 10.2).

Low salaries and poor working conditions have affected morale, and hence productivity, in the parastatal sector. This has been exacerbated by the lack of technical expertise on boards, which tend to be appointed on the basis of political criteria.

Much of the infrastructure in the public enterprise sector is antiquated and constantly breaking down. Loans under the Public Sector Investment Programme (PSIP) have declined drastically, which has resulted in the non-replacement of plant. For instance, ZISCO is experiencing low plant capacity

Table 10.2: Human resource audit of the National Railways of Zimbabwe, 2007

Category	Actual	2007 budget	Shortfall	Actual–budget (%)
Managerial	93	182	89	51.1
Engineers	48	81	33	59.3
Artisans	529	771	242	68.6
Others	6,591	8,950	2,359	73.6
Apprentices	282	362	80	77.9
Total	7,543	10,346	2,803	72.9

Source: *Chenyika (2007: 7)*.

utilization, with a monthly production average of 12,473 tonnes which is less than the break-even production output of 25,000 tonnes per month.

Currently, ZESA is generating 49 percent of the total power requirements owing to low plant availability. Air Zimbabwe has very limited capacity in two B767s, three B737s and three MA60s.

The slow progress of public enterprise reforms is also related to a fear of strengthening the grip of foreign capital on the economy. This was exemplified by the emergence of an indigenization lobby in the 1990s, culminating in the government Policy Framework for the Indigenization of the Economy (24 February 1998).⁷⁻⁸ Issues of indigenization continue to take centre stage, as witnessed by the passing of the Indigenization and Economic Empowerment Act (No. 14 of 2007) by Parliament in 2007, which came into force on 17 April 2008.

Lack of political will and commitment, the unpredictable political and macroeconomic environment, and a lack of investor and donor confidence have also been identified as key constraints. An often ignored factor is the credibility of the government itself as an agent of change. This credibility is related to the extent to which the government enjoys the support of the populace. It is inconceivable that public enterprise reforms

can work in an environment characterized by mistrust, where business, labour and social groups are vilified as unpatriotic and agents' provocateurs. In such an environment of hostility and policy failure, public enterprise reforms are as much a casualty as any other aspect of the economy. Since a central tenet of public enterprise reforms is to unleash the discipline of markets, it is impossible to envisage its success in a generally anti-business environment.

SERA (2008: 2) itself identified the following as the causes of the poor performance of public enterprise reforms:

- Viability deficiencies as a result of the prevailing harsh macroeconomic environment, characterized by a high interest-rate regime and high inflation level.
- Under-capitalization.
- Inappropriate operating and financial structure.
- Leakage and abuse of resources owing to poor and ineffective management.
- A huge debt overhang in a high-interest rate environment.
- Serious deterioration of infrastructure owing to limited resources for both maintenance and new investments.

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PROVOCATEURS

⁷ It was revised in 2004. See <<http://www.indigenisation.gov.zw>>.

⁸ Zhou (2000) observes that the Z\$400 million allocated to the NIT since its formation in 1996 was diverted to pay gratuities to war veterans in 1998 (see *The Herald*, 1 October 1998).

- Shortages of foreign exchange, which have constrained the importation of essential spares.
- No access to external lines of credit.

Since the appointment of a new Governor of the Reserve Bank in December 2003, he has provided probably the most scathing attack from a government official on public enterprises, which he saw as a 'drag' and 'the critical missing link' for economic recovery.⁹ The RBZ unveiled an 18 to 24 months 'Parastatal and Local Authorities Reorientation Program (PLARP)' in January 2005 designed to spearhead the restructuring of public enterprises and local authorities.¹⁰ It was projected that the government would cease providing allocations from the budget from 2006. PLARP therefore sought to move public enterprises and local authorities towards sound corporate governance, efficiency, profitability and sustainable long term growth.

A review by SERA of the post-PLARP performance of public enterprises as at 30 June 2007 points to some positive developments. Perennially loss-making parastatals – such as ZISCO, GMB, CSCL, NOCZIM, Tel*One, Net*One and ZESA Holdings – had made some profit, with the exception of ZINWA, which realized a loss of Z\$15.6 billion (US\$52,000). Chenyika (2007) indicates that, following the NRZ's adoption of a turnaround strategy with the involvement of its social partners, its fortunes improved markedly, with the annual tonnage rising from 3.7 million in 2005 to 5.4 million in 2006. However, analyses from the RBZ and SERA suggest that the recovery is still fragile. When one considers what might have happened in the absence of support from PLARP, it becomes clear that the results are artificial. The RBZ has admitted that the funding

comes from printing money, which suggests that under normal conditions these enterprises would not have received such highly inflationary support. The Governor of the Reserve Bank reasoned: 'We are aware of the inflationary impact of printing money to fund infrastructure development, but what good will it do to us to have zero inflation and have people dying due to rail accidents as we have recently witnessed in Victoria Falls?'¹¹ Thus, even though the Reserve Bank had identified the year 2006 as the year it committed itself to attending to the unfinished business in the sector to achieve a turnaround, this was not achieved.

10.2.2 Current status of infrastructure in Zimbabwe

In the 1980s and into the 1990s, the view was frequently expressed that there was adequate investment in Zimbabwe's infrastructure and that it was well maintained. The supply of infrastructure services was therefore adequate to support productive sector investments and provide relatively high coverage of the needs at least of the urban dwellers, if not of the rural population. This generalization may have had some validity in relation to the maintenance aspects of transport, energy and water, but certainly did not apply to information and communications technologies (ICT), where poor maintenance of publicly owned facilities and underinvestment was very evident in a sector which was becoming increasingly important as a potential source of economic growth. In fact transport, energy and water also suffered from under-investment, but the effects only became really obstructive towards the end of the 1990s. In the post-2000 crisis, not only has there been a total lack of replacement and new investment, but real expenditure on maintenance has fallen to derisory levels.

⁹ See, for instance, the Monetary Policy Statement for the Fourth Quarter of 2005 presented on 24 January 2006: <<http://www.rbz.co.zw/inc/publications/legaldept/rbzpdfs/Monetary%20Policy%202006.pdf>>

¹⁰ See <<http://www.rbz.co.zw/inc/publications/legaldept/rbzpdfs/Supplement4.pdf>>.

¹¹ Quoted in *The Herald*, 16 September 2006, p. 11.

The resulting deterioration in the state of infrastructure has been marked:

- Tarred roads in urban areas as well as highways are visibly deteriorating, while many rural roads are becoming impassable. This has occurred despite a sharp decline in road transport due to the limited availability of fuel.
- The rail track has deteriorated significantly with a growing proportion of main lines having to operate under speed restrictions. Locomotive availability is poor and locomotive reliability is down to 16,000 km between failures, against a standard of 100,000 km. Wagon availability was 59 percent in 2005 and has continued to decline.
- Water supplies in urban areas have become erratic and quality uncertain, this being due to the unavailability of spare parts for pumps and other equipment and shortages of electricity and water purification chemicals.
- In the energy sector, fuel is in constant short supply and extremely expensive when available (in part due to rapid increases in the international price of petroleum products); electricity supplies have become extremely erratic, the economic costs of blackouts being exacerbated by the lack of planning of outages.
- In the telecommunications sector, there is a large backlog in both fixed line and cellular phone connections. Service quality is extremely poor, with call completion rates between mobile networks for example, being estimated to be less than 10 percent.

In all the above (except road transport), public enterprises (PEs) are the dominant suppliers of services and suffer from all of the problems identified above. These include

massive deficits on current operations and the accumulation of significant levels of debt. Another issue of particular concern when considering recovery strategies is the loss of skilled personnel at all levels.

The challenge of restoring Zimbabwe's infrastructure base is one of the most urgent reconstruction tasks and one that will be most demanding of investment resources. As is well known, the costs of rehabilitation of infrastructure are many times higher than the costs of regular maintenance. The economic cost of the recent neglect of maintenance, compounded by the legacy of past under-investment in infrastructure, will place a considerable burden on the country at the start of the recovery period (see World Bank, 2006 and 2007).

10.2.3 Housing provision

The UN Covenant on Economic, Social and Cultural Rights considers housing (shelter) as a basic socioeconomic right, and yet this is seldom acknowledged and reflected in national policy and in practice.¹² Furthermore, housing development generates strong forward and backward demand linkages, setting up powerful multiplier effects within the economy. The backward demand linkages for building materials, electrical and sanitary ware, roofing, and so on, will encourage the production of a wide range of manufactured products. Similarly, once a dwelling has been built, the occupants will want to furnish it, install electrical appliances, and need many consumables to maintain their homes. It is therefore not just the process of producing houses that would create employment, but the derived demand for labour for every product required by prospective and new homeowners. If the housing policy facilitates the construction of ultra low-cost housing for the urban poor, then employment created by micro and small-scale enterprises would be strongly pro-poor.

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START OF THE
RECOVERY PERIOD*

¹² This right is also enshrined in the UN's Universal Declaration of Human Rights; the Convention on the Elimination of All Forms of Discrimination against Women; the International Convention on the Elimination of All Forms of Racial Discrimination; and the Convention on the Rights of the Child, among others.

Following the attainment of independence in Zimbabwe, the new Government quickly recognized the challenge of meeting the housing needs of the urban population. A housing crisis had emerged following the influx of people into the urban areas during the war of liberation, which had resulted in the mushrooming of squatter camps. Thus, the Ministry of Public Construction and National Housing (MPCNH) was empowered by the Housing and Building Act, 1979 and the Housing Standards Act (Chapter 205) to formulate and administer the National Housing Policy. The policy was founded on **home-ownership** in order to address the housing shortage, tenurial insecurity, and encourage private investment in housing.

As a first step, the Government allowed the occupants who rented municipal houses to buy them, promoting home-ownership, secure tenure, and reducing the local authorities' housing maintenance costs. The introduction of 'state sponsored self-help housing' was made possible by assistance from the United Nations, the World Bank, the Commonwealth Corporation and USAID. Under these schemes, site development and the provision of services were undertaken by private sector contractors, who completed the civil engineering works and the physical infrastructure. Serviced stands were then allocated to those on the housing lists, who built their own houses using low cost, labour intensive methods. As opposed to building brigades, aided self-help was the most popular and cost effective method.

The government maintained the minimum standards embodied in the Model Building By-laws of 1977. While this improved the quality of high-density housing, the government was immediately faced with increased construction costs. As Auret observes:

'Historically, the housing delivery system has been characterised by unrealistically high standards for housing structures, infrastructure and public facilities – determined by the Government.' (1995:114)

Private sector participation in low cost housing included the provision of mortgage loans from building societies; employer assisted housing schemes, private individuals, real estate developers and NGOs.

During the ESAP period, housing was to be provided on a cost recovery basis. The MPCNH channelled funds into i) the National Housing Fund; ii) the Housing and Guarantee Fund; and iii) the Civil Servants' Fund. Rentals were paid to the Ministry's offices. The government launched the 'Pay for Your House Scheme' in 1992. Individuals made monthly payments into a fund. When their contributions reached half the construction cost, flats were built. The MPCNH was responsible for acquiring the land, preparing the plans and the eventual construction of the units. The scheme saw the building of flats and houses in Harare, as well as smaller towns. The major strength of the scheme was that it did not rely on budget allocations or subsidies.

However, as the government provision of housing stalled, the waiting lists lengthened. Government often found itself implementing interventions at odds with its stated objective of providing housing for all. For instance, ahead of the Queen's visit at the Commonwealth Heads of Government Meeting in Harare in 1991, many households were forcibly removed from informal squatter settlements, carted off to Porta Farm (on the outskirts of Harare), and had their homes bulldozed. Auret found the Government's action 'extraordinary in the light of the enormous shortage of accommodation' (1995:71). It was discovered that many squatters who had been moved to Porta Farm were income-earners who had been driven to live in informal squatter settlements by the shortage of accommodation and the high lodging costs charged by house-owners in Harare's high-density suburbs.

'In the last five years', wrote Auret, 'Government, acting apparently with no foresight or planning, has in fact increased

the number of homeless by evicting several large groups of people who were at the time adequately housed' (1995:73). By the mid-1990s, there were an estimated 1.5 million people without adequate housing and there were an estimated 100,000 people living in squatter settlements in and around Harare alone (Auret, 1995:1). Overcrowding was ubiquitous as illustrated by the fact that instead of one family occupying 300 square metres, four families shared 100 square metres of land and one toilet.

Even though an average of over 4,000 stands was allocated between 1994 and 1996, the waiting lists stood at over 100,000. In reality however, the housing needs were far more critical than the waiting list reflected. Many of those in lodgings had not bothered to register, either through ignorance or as a result of a sense of hopelessness (Auret, 1995:26). As the relationship between government and the donors deteriorated in the late 1990s, USAID, World Bank and other donor-supported housing projects came to an abrupt end, worsening the housing situation as demand outstripped supply.

Clearly therefore, the huge backlog in housing started well before the crisis period. The National Housing Delivery Policy of 2000 acknowledged a cumulative backlog of over one million housing units, while the National Housing Programme of 2003 noted that actual production of houses had been between 15,000 and 20,000 units per annum between 1995 and 2000 as compared with an annual target of 162,000 units. The situation was worsened by the government systematically demolishing at least 93,000 houses during Operation Murambatsvina, with few replacements being constructed in the subsequent Operation Garikai (a mere 3,325 new houses in the first year, according to a survey by Amnesty International). The setting up of the National Housing and Infrastructure Development Bank of Zimbabwe in recent years has not helped as it was grossly undercapitalized.

10.3 CONSTRAINTS TO GROWTH AND RECOVERY

10.3.1 Public enterprises

The legal, institutional and policy framework

The literature on public enterprise restructuring points to the importance of the following:

- The depth and quality of the programme design and management.
- The existence of appropriate legislation (e.g., restructuring/privatization law).
- The legal authority of the restructuring/privatization agency which allows it to undertake its work with minimal political interference.
- Transparency – the steps taken to inform the public about the programme and to encourage their maximum participation in the process (see, for instance, Godana and Hlatshwayo, 1998: 15).

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As shown below, weighed against these criteria, Zimbabwe's public enterprise restructuring programme fares poorly. The framework for public enterprise restructuring in Zimbabwe is a minefield, characterized by a multiplicity of pieces of legislation, institutions, and at times contradictory policies, and even policy reversals. Zimbabwe's institutions and procedures for restructuring/privatization were developed in an ad hoc manner, are cumbersome and non-transparent.

The Inter-Ministerial Committee on Commercialization and Privatization (IMCCP), established in 1994 to coordinate the commercialization and privatization process, was initially chaired by the Planning Commissioner and later by the Minister of Finance and Economic Development. The IMCCP convened ministerial level meetings to consider proposals and recommendations

of line ministries; if satisfied with their proposals, and made recommendations to Cabinet. Following the change from PAZ to SERA in 2005, the IMCCP was renamed the Inter-Ministerial Committee on Commercialization and Restructuring of Public Enterprises (IMCCR). Since 2005, when the Ministry of Finance and Economic Development was split into two, the IMCCP has been chaired by the Minister of Economic Development.

To drive the privatization process, the PAZ was established in September 1999 following criticisms of the piecemeal approach that had resulted in little progress. It was a semi-autonomous institution in the Office of the President and Cabinet and derived its authority from Cabinet. Its functions were set out as follows (RBZ, 2007: 8):

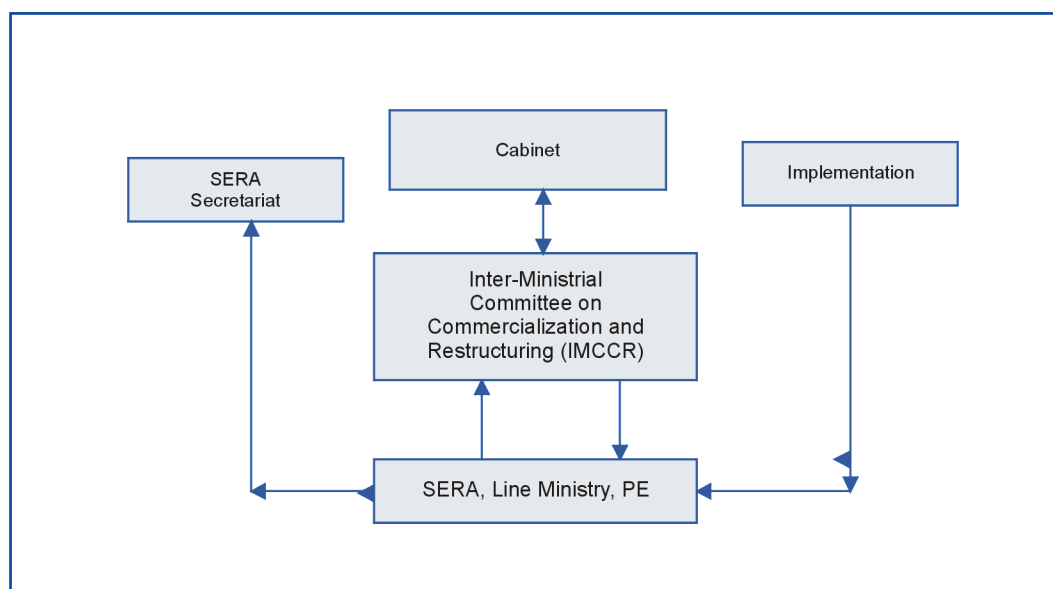
- To assist, support and accelerate the privatization process, working closely with the public enterprises and with line ministries, which have had responsibility for the various public enterprises.
- To facilitate a smooth flow from initiation through to approval by the Inter-Ministerial Committee of the privatization plan.

- To lead to an eventual successful privatization process.

- To contribute to job creation, and to increase Zimbabwe's foreign-exchange earnings.

Renamed the State Enterprises Restructuring Agency in 2005, it now falls under the Ministry of Economic Development and its director reports to the Secretary for Economic Development through the Principal Director for Economic Affairs; however, its authority derives from Cabinet. In conjunction with the relevant enterprise and its line ministry, SERA prepares an initial commercialization and restructuring plan, giving the overall rationale for restructuring and privatization, suggestions on the method of privatization, etc., and submits the plan to the IMCCR for approval. The IMCCR then reviews the plan, and accepts, modifies or requests modification and resubmission. When accepted the plan is submitted by the chairman of the IMCCR to Cabinet for approval; the Cabinet may request further modifications or amendments before final approval. Once Cabinet approval has been given, SERA is responsible for implementing the plan. The agency is charged with selecting and appointing professional

Figure 10.1: The institutional set-up for the commercialization and restructuring of private enterprises



Source: Adapted from Zhou (2000: 182)

advisers (consultants, lawyers and, as appropriate, merchant or investment bankers) to make any necessary preparations for the commercialization and restructuring of the enterprise, prepare the documentation, and execute the transaction. Figure 10.1 summarizes the institutional structure.

However, SERA clearly lacks autonomous existence: almost all the staff of PAZ were reassigned, resulting in the recruitment of new staff at SERA. It employs thirteen people, seven of whom are technical staff. A change agency such as SERA needs to be strategically positioned and empowered to be autonomous and make independent decisions. Locating it under a ministry, reporting to a Principal Director, does not give it real ‘clout’.

Players, structures and processes

At least 12 actors are involved in the commercialization and restructuring of public enterprises, creating confusion and thereby promoting clientelism, patronage and the pursuit of rent-seeking activities. The agencies involved in the process at different levels and in different capacities are:

- Management and board of the entity to be commercialized/restructured.
- The parent ministry.
- Ministry of Finance.
- Ministry of Economic Development.
- Department of State Enterprises and Parastatals in the Office of the President and Cabinet.
- Inter-Ministerial Committee on Commercialization and Restructuring.
- State Enterprises Restructuring Agency.

- The Vice-President with a specific mandate on public enterprises.
- RBZ and its PLARP facility.
- Cabinet.
- Various regulatory bodies/authorities in some of the sectors.
- The ruling party and aligned lobby groups.

The restructuring/privatization programme therefore hinges on the commitment and efficiency of these key players. The role of SERA is reduced to implementation and not decision-making, which has resulted in bureaucratic inertia and hence the lack of progress.¹³

The institutional set-up is also clouded by the existence of specialized departments and ministries in charge of parastatals. These include the Department of State Enterprises and Parastatals in the Office of the President and Cabinet and the Ministry of Indigenization and Empowerment. This ministry often makes strong pronouncements on the restructuring of public enterprises that contradict line ministries. With no clear policies on ESOPs, the under-capitalized National Investment Trust and evolving empowerment initiatives, the issue of indigenous participation has acted as a brake on public enterprise restructuring. There is a clear conflict between the renewed focus on immediate restructuring and the objectives of privatizing through indigenous participation. Issues of economic empowerment are not short term, and, in the context of the crisis and paralysis in the instruments of indigenous participation (e.g., NIT and ESOPs), no action has been taken. Furthermore, the legal framework has remained a minefield, with amendments to the laws under which public enterprises were created

¹³ In other countries (such as Zambia, Uganda and Tanzania), a similar institution was established through legislation, and hence had decision-making powers, was autonomous and reported to Parliament.

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SINCE 2005

lagging behind. The amendment of laws has been painstakingly slow, resulting in the absence of an enabling legal environment. Thus, the legal framework reflects the old control mindset, which has been used to telling effect by line ministries.

The introduction of the PLARP facility by the RBZ in January 2005 gave it direct entry into the issue of public enterprise restructuring. Thus, the RBZ has come out very strongly on the subject, coming up with its own structures, unilateral time-tables and processes that serve only to further complicate an already complex situation. SERA (2008) set out the Divestiture, Commercialization and Restructuring Programme for 2007–2008, and produced its own list of entities for restructuring. However, little progress has been made in terms of either list. It must also be noted that listing entities and prioritizing them for implementation has been undertaken in all economic blueprints since ZIMPREST (Zimbabwe, 1998b). This appears now a game of hit and miss, played with more enthusiasm than success. More fundamentally, however, there is no shared vision around issues of public enterprise restructuring, even within government, with the current approaches being more piecemeal and reactive. In addition, the existing structure hardly promotes stakeholder participation in the design of the restructuring plan, and hence workers and their unions have often resisted the reforms.

The role of the presidency and ruling party in restructuring also deserves mention. Zhou (2000) describes Zimbabwe as a ‘presidential state’, in which the influence of the presidency is widely felt. It is commonly accepted that most managers of public enterprises owe their existence to political connections, and hence to survive they have to support political positions. Worse still, the system is such that the change of a minister or Permanent Secretary is accompanied by changes in the board or management of

public enterprises, highlighting the role of patronage in appointments. Boards have been removed for disregarding the views of powerful individuals.

As the crisis has deepened, and the credibility of government waned, the space for wider participation in public enterprises and sectors in which they have a monopoly was closed, as evidenced by the reversal of the opening up, even to ruling party members, of the airwaves. Thus, the predominant mind-set of controls is evident in all sectors of the economy, and has effectively put paid to efforts to restructure public enterprises.

Capacity constraints

Virtually all public enterprises face severe capacity constraints, which have impacted adversely on their performance. One of the major constraints is financial, which manifests itself in terms of poor financing and a lack of proper financial management systems, poor liquidity management, lack of investment by the principal shareholder (government), poor financial accountability, poor pricing structures, financial mismanagement, and corruption. Almost all public enterprises have failed to produce timely audited financial statements, an issue that has been raised consistently by the various Parliamentary Portfolio Committees that oversee the sectoral enterprises.

The tariffs charged are well below economic cost, resulting in most public enterprises having to rely on subsidies from the state, with the RBZ bailing them out since 2005. Experiences with the PLARP facility suggest that they have a clear dependency syndrome and an ‘insatiable appetite for free money’. As the Governor of the RBZ observed, ‘For some parastatals, the tragedy is that not only are they repeatedly coming to the Central Bank for foreign currency, mainly at subsidized exchange rates, but also are doing so without a penny of local currency to buy the foreign exchange.’¹⁴

¹⁴ Monetary Policy Statement of 24 January 2006, paras. 12.16–12.17).

10.3.2 Infrastructure

Policy, institutional and regulatory framework for recovery

In 2006–2007, the World Bank commissioned infrastructure studies and stakeholder debates in the following sub-sectors: roads, railways, water, energy and telecommunications.¹⁵ The resultant reports provide recommended action plans over 3 time-frames: short term (6 months), medium term (2 years) and long term. The main elements of these action plans address changes that are required in the legal and institutional framework to facilitate the large investments necessary to restore these sectors and give assurances of sustainable infrastructure services thereafter (adequate maintenance systems and cost recovery tariffs being key elements).

Summarizing and adding to the recommendations of the infrastructure dialogue, the main policy, planning, legal and institutional changes which are needed to overcome existing constraints are as follows:

- **Roads:** Articulation of a National Transport Policy and preparation of a National Road Development Plan, reinforcement of the Road Fund (intended to finance road maintenance via the fuel levy), establishment of the State Highways Authority (to carry out major road maintenance) and of a community rural road maintenance system.
- **Railways:** Articulation of a National Transport Policy, amendment of the Railways Act to incorporate all forms of private sector participation, restructuring of the National Railways of Zimbabwe (NRZ) to shed non-core businesses and introduce Public Service Obligation Contracts for NRZ's core

business, with subsequent outsourcing and concessioning of rail transport.

- **Water:** Preparation of a Policy Framework Adjustment Note and a Water and Sanitation Sector Capacity Development Strategic Plan, amendments to the Water Act, establishment of a Water and Sanitation Tariff Regulation Commission and a system of community based management of water schemes in rural areas, restructuring of the Zimbabwe National Water Authority (ZINWA).
- **Energy:** Reform of the Zimbabwe Electricity Regulatory Commission (ZERC) so that it fulfils its intended functions, reversion to the pre-2000 institutional reform strategy in the electricity sector, preparation of a revised System Development Plan; in the petroleum sector, the creation of a fair and transparent system for predominantly private sector fuel importation, with the functions and assets of the National Oil Company of Zimbabwe (NOCZIM) being restructured.
- **Telecommunications:** Reform of the Postal and Telecommunications Regulatory Authority of Zimbabwe (POTRAZ) and the Universal Services Fund so that they fulfil their intended functions, review of the dominance of Tel*One in fixed line services and expansion of the training available in the sector.

One of the cross-cutting themes is the need to involve the private sector more intensively in the provision of infrastructure services. Scarce public investment resources are best directed to urgent needs in the social sectors and to housing. If properly managed, encouraging the private sector to engage in the infrastructure sectors should bring efficiency gains as well as investment resources.

¹⁵ World Bank (2006): *Zimbabwe Infrastructure Investment Note for Roads, Railways and Water Sectors*, and World Bank (2007): *Zimbabwe Infrastructure Dialogue in Roads, Railways, Water, Energy and Telecommunication Sub-Sectors*, Africa Transport Sector, Washington DC.

It would be useful for a framework law on public private partnerships (PPPs) to be passed. This would facilitate the structuring of PPPs in the public interest in all sectors where private participation might be considered. The main pre-requisite for effective private sector participation in infrastructure would be the establishment of independent, professional regulatory agencies. These are required to protect the interests of consumers, particularly in respect of being charged 'fair' prices for infrastructural services, while at the same time assuring investors of a predictable and impartial environment in which tariffs and other crucial parameters affecting their business viability will be set. The infrastructure regulators established so far in Zimbabwe – POTRAZ and ZERC – are a caricature of what is intended, having neither the professional competency that is required nor any vestige of autonomy in making key decisions in respect of licensing and tariff-setting.

Given the size of the Zimbabwe economy, the high level of skills required for world-class infrastructural regulation to be achieved and the limited pool of people to draw on, a single infrastructure regulatory authority should be considered for transport, telecommunications, water and energy. Successful multi-sectoral regulators are in operation in countries such as Ghana, Rwanda and Jamaica. Water is a special case, in that there are two major aspects requiring regulation: water as a natural resource, which is best handled as part of an environment regulator, and water as an infrastructural service, which has many similarities to electricity and similar services. It is the latter aspect which could be included in a multi-sector infrastructure services regulator.

10.3.3 Housing provision

Constraints to efficient and effective housing delivery included the following:

Onerous minimum housing standards and Inappropriate Policies

The government maintained the minimum standards embodied in the Model Building By-laws of 1977, which proved not only onerous, but also costly. The United Nations commission for Human Settlement in 1989 endorsed a new Global Shelter strategy, whose focus was to reduce government's role as a direct provider of housing, urging Government to concentrate on resource mobilization. Yet, in 1992, the MPCNH, contrary to its own policy of encouraging private sector participation and in defiance of a policy agreement with the World Bank, began to directly intervene in the construction of houses.

Poor planning and coordination

In March 1991 'the Harare City Council was in danger of losing funding from the World Bank to establish 3,653 stands because the land had been planted to maize and the 'Councillors refuse to take action out of fear of losing votes' (Auret: 1995:39). This problem persisted for a further four years. According to Auret, 'The current critical housing shortage can be attributed to a large degree to the lack of commitment on the part of the Government to low cost housing' (1995:109).

Unsupportive macroeconomic framework

Macroeconomic instability saw the cost of houses soar. Erratic supply of inputs, the collapse of the various housing schemes as a result of the withdrawal of donors, prohibitive interest rates, and suspension of mortgages, among other causes, exacerbated what was already a serious housing crisis.

Bureaucratic inefficiencies and corruption

The bureaucratic chain of authority involved in the process of housing delivery was long, cumbersome and fraught with potential

obstacles. Such a complex procedure invariably led to long delays and increased costs.

10.4 REMEDIAL ACTIONS AND POLICY MEASURES

10.4.1 Strategic objectives

Two broad strategic objectives should inform the process of restructuring public enterprises in Zimbabwe:

Economic objectives

- Improve the overall efficiency of the economy.
- Improve the efficiency, productivity and profitability of firms.
- Improve the quality of products and services, including affordable housing.
- Attract foreign investment, technology and know-how.
- Promote public-private partnerships in service provision.

Fiscal objectives

- Reduce government subsidies to public enterprises.
- Raise money from the sale of public enterprises.
- Increase tax revenue from privatized or commercialized enterprises.

The main aim of a housing policy should be to significantly increase the national housing stock for a variety of types of houses to meet the need for shelter of all Zimbabweans. An increase in housing stock will lower house and rental prices through a housing market that will benefit the poor significantly. The government, municipalities and other public agencies should facilitate the construction of

a mix of housing types, from high quality housing in low density areas, to low cost housing in high density areas, and ultra-low cost dwelling in specially designated areas. A wide range of house prices would create a ladder of opportunity whereby the poorest households could enter the market at the lowest level, but with the possibility of moving up market when their circumstances and resources allow.

10.4.2 Strategic thrusts

While the broad objectives of restructuring are widely shared, the methods by which these can be achieved remain ‘contested terrain’. However, there is an emerging consensus that a ‘one-size-fits-all’ ideological approach to restructuring will not work. As with the emerging wisdom with respect to development discourse, there are key principal success factors on which consensus has emerged:

- There is need for broad-based participation at all levels, from policy design/formulation to implementation, monitoring and evaluation to ensure national ownership.
- Institutional structures for broad-based participation are essential to avoid ad hoc consultations.
- There is a need to ensure universal access to basic services, especially in utility provision (water and sanitation, electricity, etc).

Lessons from experience suggest that, while some methods of restructuring are suitable in some cases (e.g., privatization where competitive markets work); other cases still require the active role of the state and the promotion of public-private partnerships (e.g., basic utilities and infrastructure). This represents a shift from a doctrinaire promotion of ownership change. As the authors of a World Bank Working Paper rightly observed: ‘Given the record,

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ENTERPRISE
RESTRUCTURING

moreover, it is difficult to recommend specific SOE [state-owned enterprise] reform strategies with great confidence' (Gomez-Ibanez, 2007: 49). The World Bank (2005: 195) also reported: 'The 1990s experience shows how difficult both privatization and regulation are. There is no universally appropriate reform model. Every restructuring and privatization program needs to consider explicitly the underlying economic attributes and technology of each sector and its institutional, social, and political characteristics.' And Nellis (2006: 9) observed that 'given the recent shift away from dogmatic promotion of ownership change, perhaps caution was the correct course of action, particularly regarding infrastructure'. The IMF (2007: 18) seems to be taking a similar position with respect to reform of public enterprises in Zimbabwe, placing an emphasis on putting public enterprises on a commercial footing, which includes possible privatization. In this regard, a case-by-case approach is recommended to take account of the specific situations of every public enterprise.

The importance of developing social-dialogue mechanisms to allow the voices of all stakeholders to be heard is a critical success factor in public enterprise restructuring (ILO, 1999). A restructured SERA should be the platform from which this recategorization is done in a participatory way, involving all key stakeholders. This categorization seems to be supported by latest thinking on the subject:

'Nevertheless, any effort at prescription should begin by dividing firms according to the degree of conflict between their commercial and non-commercial objectives and the level of development of their country's market, administrative and political institutions. Infrastructure enterprises often suffer from serious conflict between commercial and social goals only if because access to infrastructure services is considered so important to modern life. But in some firms this

conflict may be less severe if, for example, tariffs have never been allowed to fall too far below costs, over-staffing has never been too excessive or the potential technical efficiency gains are large enough to compensate customers or laid-off staff.' (Gomez-Ibanez, 2007: 49)

Thus, the strategy should be to begin with the 'low-hanging fruit', dealing with government shareholding in private entities, the cases where the enterprises are in competitive segments or where they do not have a sustainable role, such as ZINWA, NOCZIM, Tel*One and Net*One, among others. Where for instance, a public enterprise performs both commercial and social roles (e.g., Grain Marketing Board), there is need to separate these roles, with the social role reverting to a ministry.

In a nutshell therefore, restructuring should include both divestiture and non-divestiture options. Divestiture options involve the transfer of ownership rights, while non-divestiture options entail the transfer of operating or development rights from the public to the private sector. Divestiture options include direct sale, public share offering, private placement with a strategic investor, public auctions, employee/management buy-out, mass/voucher privatization and liquidation. Non-divestiture options include restructuring, commercialization or corporatization, contracting out, management and service contracts, leases and concessions and public-private partnerships. In practice, these two methods may not be mutually exclusive as, where divestiture is appropriate; preparation for privatization usually begins with the restructuring of the enterprise, with commercialization featuring prominently.

At the level of strategic thrusts, it is necessary to create an agent for restructuring that will drive the process and implement it. Such a change agent should be placed at a sufficiently high level to drive the process without being entangled in

bureaucratic red tape. With respect to infrastructure and housing delivery, it is clear that Government on its own should not shoulder the immense responsibilities of provision, hence the need to promote public-private partnerships.

Giving housing high priority from the start of the recovery period will provide an opportunity to address one of the country's most pressing social issues while at the same time generating a significant level of employment, both directly via the actual house construction and upstream in the construction material supply industries. The import content of low cost housing is very low. While the construction material supply chains include capital intensive industries (notably cement), many other items (such as window frames, doors, bricks and roofing sheets) are amenable to production both by formal industries and by small labour-intensive enterprises. A rapid increase in low-cost housing starts will provide considerable multiplier effects through the economy.

10.4.3 Recovery policies and policy measures

Public enterprises

The State Enterprises Restructuring Agency (SERA)

The participatory approach to restructuring has been promoted by the ILO through its Interdepartmental Programme on Privatization, Restructuring and Economic Democracy (IPRED). It emphasizes the importance of a tripartite approach in ensuring a smooth transition from a bureaucratic to an entrepreneurial culture. According to the ILO, 'Public sector reforms are most likely to achieve their objectives of delivering efficient, effective and high-quality services when planned and

implemented with the full participation of public sector workers and their unions and consumers of public services at all stages of the decision-making process.¹⁶

A participatory restructuring culture helps to transform the public enterprises into an effective results-oriented long term coalition by reconciling conflicting interests (Nellis, 2006). The ILO is promoting socially sensitive enterprise restructuring (Rogovsky, 2005). This approach is in line with the latest developments in the development discourse, where top-down, 'one-size-fits-all' traditional approaches are being replaced by an integrative, stakeholder approach that emphasizes transparency and accountability in decision-making processes. In this regard, the shift from dogmatic blueprints to participatory, inclusive approaches promotes win-win outcomes and, ultimately, sustainable human development.

SERA should be transformed into a multi-stakeholder authority – as was initially agreed at a stakeholders' workshop organized by the National Planning Commission in Nyanga in March 1996 (Godana and Hlatshwayo, 1998: 20–21) – and be re-established under an appropriate Act that gives it autonomy as the agency responsible for the planning, management, implementation and control of the public enterprise restructuring programme. This will help avoid the conflict of laws and the need to amend individual enabling Acts that established the specific enterprises. To facilitate communication and reporting to Cabinet, it should be linked to a specific Ministry.

Appropriate methods of restructuring

As discussed above, the method of restructuring to be adopted depends on the type of enterprise, suggesting a need to cluster them on the basis of their amenability to the two main methods: divestiture and non-

¹⁶ Quoted in Marcovitch (1999: 5)

divestiture. Divestiture options have the major advantage of not requiring continued dependency on the state for resources. This is particularly critical in the case of Zimbabwe, where the state has no resources and will have to implement a deflationary stabilization programme. Given the state of under-capitalization that characterizes most public enterprises, wherever feasible, divestiture options should be considered; where these are not feasible, as is the case with those providing basic services, non-divestiture options will have to be employed.

Given this development, cooperating partners will have to play a role in providing requisite resources. There is now a growing interest in funding infrastructure, especially given the failure by the private sector, on its own, to take up such investments following cut-backs by international financial institutions. (UNDP, 2007; World Bank, 2005). Public-private partnerships now offer the opportunity to share the costs of such massive investments. In this regard, the private sector, whose development also relies on the provision of quality infrastructure, will have to co-finance such investments. There are some interesting examples, especially with respect to the construction and maintenance of road networks – for instance, the toll road option (build, operate and transfer) in South Africa.

The strategy should be to begin with the divestiture of shareholdings. This should also include liquidating those enterprises that may not have any future role such as ZMDC. Water provision should be returned to local authorities, and the private sector can easily take over the supply of fuel, as is the case in other countries in the region and beyond. In those areas where competitive markets operate – including such enterprises as the CSCL, the IDC's subsidiaries, and telecommunications services – divestiture options should be applied.

The real challenge will begin with the infrastructure enterprises that may not be suitable for divestiture, and also in view of

their current state of under-capitalization. In some cases, such as Air Zimbabwe, a strategic investor should be identified. The example of Kenya Airways is a significant one, which teamed up with KLM to turn around its fortunes. Other enterprises, such as ZISCO should also follow this example.

Given that the driving force of the economy in the post-crisis dispensation will be the private sector, it will be necessary to open up sectors where markets work, such as telecommunications, media, especially the electronic segment, electricity and transport sectors.

There is therefore a lot of scope for private sector involvement in all sectors of the economy, which should be facilitated through the deregulation of existing monopolies.

Infrastructure sub-sector strategies

i) Transport

The restoration of the road and rail networks needs to be accompanied by the creation of a competitive market for the provision of transport services. This is particularly important in road transport, but applies also to rail and to boat services on Lake Kariba. In respect of air transport, an 'open skies' policy would be important in attracting back the international carriers which have ceased providing services to Zimbabwe. Having a range of international and regional carriers is a vital component of reinvigorating the tourism industry and of providing the air cargo capacity for the export of horticultural and other high value export products. These are key components of the short-term revival strategy, generating foreign currency and, as they are also labour intensive, providing an early boost to employment.

The restoration of affordable and reliable urban transport will also be critical in the early stages of the recovery period. Innovative solutions to urban transport problems need to be sought, drawing on examples from elsewhere in the world of

successful strategies which provide good services for commuters while reducing pollution and making greater use of indigenous fuels and technologies. Options for improving passenger services between Chitungwiza and Harare should receive particular attention.

ii) Water

Although vulnerable to drought, Zimbabwe is relatively well endowed with water resources. However, the main problems are inequitable access to water and a failure to exploit the development potential of water, arising from poor management of water resources in the past. A recovery programme affords an opportunity to establish a framework for sustainable, efficient and integrated utilization of water resources for the benefit of all Zimbabweans.

The main principles to be applied in formulating a strategy for the water and sanitation sector are:

- **integrated water resource management (IWRM):** holistic management of land and water, the importance of user participation, particularly of women, and the need to treat water as an economic as well as a social good
- **regulation:** separation of the roles of natural resource regulation and infra-structural services regulation (as discussed in Section 10.1.2) and the introduction of economic pricing of both raw and treated water, with transparent subsidy and other mechanisms to protect the poor
- **demand side management in urban water supplies,** with other urban centres emulating the extremely successful loss reduction and water efficiency strategy which is on-going in Bulawayo
- **sanitation:** provide rural and peri-urban communities with access to a range of technologies
- **productive water:** the Millennium Development Goals emphasize clean water for domestic purposes – equally important is the provision of water to rural households for enhanced agricultural production so as to raise incomes (thereby *inter alia* making it more likely that domestic water schemes can be maintained through financial resources raised within the communities).

iii) Energy

The immediate challenge in the energy sector will be to restore normal supplies of liquid fuels, electricity and coal, but in the medium term the energy strategy needs to ensure universal access to modern forms of energy, in part through embracing resources which have hitherto been neglected in Zimbabwe. These include both renewable sources (solar water heating, solar voltaics and small hydro-power schemes) as well as unexploited fossil fuel resources (coal bed methane and the extensive coal deposits which exist around the country, with only Hwange's coal reserves being mined at present).

In the electricity sector, the return to the previously envisaged unbundling of ZESA into generation, transmission and distribution companies (without any holding company) needs to be accompanied by the progressive development of a competitive electricity market. Experience in other countries suggests a three stage process:

- In the first stage, competition is introduced in the generation sector through independent power producers (IPPs) being licensed to compete with the state owned generation company; power purchase agreements (PPAs) are signed with the transmission company, which is licensed as a single buyer (this already exists in a small way with PPAs for the Rusitu hydro and Hippo Valley and Triangle bagasse schemes).
- In the second stage, large 'eligible' customers are permitted to purchase

power directly from competitive suppliers (wholesale competition), with a balancing market to ensure continuity of supply.

- In the final stage, a fully competitive market is developed, with suppliers competing for all customers, including domestic customers (retail competition). This may entail further development of the institutional structure, including a separate system operator and possibly also a market operator.

In Zimbabwe's case, the development of an internal competitive market will have to be coordinated with the development of a competitive regional pool by the Southern African Power Pool (SAPP). Supplies from SAPP have become increasingly important in sustaining electricity in Zimbabwe in recent years, and were maintained even when the country was unable to pay for its imports of electricity. In the recovery programme, Zimbabwe needs to restore its own generation capacity, but with the security of supply associated with SAPP and the very much lower cost associated with many of the potential generation projects located elsewhere in the region, the country would do well to consider joint venture developments of power stations not located on Zimbabwean soil. This strategy will bind Zimbabwe more closely to its partners in SADC, ensuring the necessary support in due course for large joint power projects such as Batoka.

iv) Information and Communications Technologies (ICT)

In the 21st century, ICT has become recognised as a fundamental ingredient of economic growth, social development and the deepening of democracy. The principles to be adopted for a national ICT strategy are:

- the creation of an enabling environment for the growth of the ICT industry
- provision of universal service and access to information and communications facilities in rural as well as urban areas

- investment in the convergence of telecommunications and information technologies.

Zimbabwe needs to work with other countries in Southern Africa to ensure that the region is able to capitalize on the opportunities that ICT is opening up. These include the export of services (finance and back-office banking services, call centres, etc.) that could become an important source of employment for Zimbabweans once the country's international image has been restored.

Pre-requisites for rapid growth in housing

Three pre-requisites for a major housing programme to be initiated are:

- **Changes in the legal, policy and institutional framework**

The report on Operation Murambatsvina by Anna Tibaijuka, the Head of UN-HABITAT, noted that Zimbabwe has had unrealistic housing standards. 'There is an urgent need on the part of all stakeholders and the Government of Zimbabwe to harmonise policies and strategies vis-à-vis the informal economy and housing for the majority of the urban population'. The Regional Town and Country Planning Act and the Housing Standards Act need to be transformed to become 'pro-active instruments of enablement and empowerment rather than exclusion'.

Housing is best managed by urban local authorities. 'As the sphere of government closest to the people, they are in the best position to strike a balance between demand and supply for housing, infrastructure and basic services. Lessons learned from successful practices in meeting the social, economic and aesthetic challenges of rapid urbanization and globalization indicate that positive and sustainable outcomes are indeed possible. They depend, to a large extent, on recognising that housing and urban development is a process, however imperfect, that is best managed through socially inclusive

dialogue and participatory decision-making'¹⁷.

Critically, therefore, housing authorities should focus on their core functions.

The government, municipalities and town management boards are the key facilitators in the provision of housing. Their prime role should be to:

- ensure that sufficient land has been banked for future housing development;
- provide secure tenure, introduce inexpensive survey techniques, and maintain a cadastre (records) of all land surveyed and transferred;
- build professional institutional capacity to plan and control urban development, and deliver housing effectively;
- supervise the tender process, surveying, and those contractors providing key services and infrastructure; and
- create incentives for private sector participation.

It is essential that public organizations focus on their core functions, leaving the private sector to fund development, install infrastructure and construct houses. Given the need to provide sufficient public funds for efficient public administration, any housing subsidies should be justified, prioritized and transparent. In particular, municipalities should sell any 'income generating' investments that often impose huge losses on the city, and use the capital generated to support its core business.

• **Provision of finance for housing**

Public sector funds will be needed to kick-start the housing programme. Allocations of public investment funds in the national budget should be channelled to local councils to expand public housing provision and provide

the stands for site-and-service and cooperative housing schemes. Home-owners and cooperative members can undertake the subsequent building themselves, or do their own contracting as and when they have the means to do so. Funding through building societies needs to be restored as part of the macroeconomic stabilization and financial sector reforms.

In the longer-term, it would be beneficial to enable institutional savings (pension and life-insurance funds) to be channelled into mortgage financing, as this would dramatically increase the resources available to people to borrow for home building. To do this, legal, taxation and regulatory changes would be needed to create an effective and financially sound secondary mortgage market.

• **Serviced stands**

Because of deficiencies in other infrastructure sectors, it will be difficult initially for local authorities to make available sufficient fully serviced stands. So as to allow progress to be made on house construction, imaginative means will have to be used to provide stands as rapidly as possible. Provision needs to be made for some aspects of infrastructure (such as connection to water supplies) to be connected at a later stage, which should if possible coincide with the completion of the construction of the dwelling.

Another strategy to overcome the initial problem of a lack of fully serviced stands would be for local authorities to encourage demonstration projects involving housing complexes with self-contained provision of water (from underground sources) and soak-aways for wastewater disposal. Housing estates involving innovative designs for affordable, low-income housing using local materials have been proposed in the past: some trial schemes should be promoted on a pilot basis as part of the drive to achieve rapid growth in housing construction.

¹⁷ Anna Tibaijuka, UN Special Envoy on Human Settlements Issues in Zimbabwe (2005): Report of the Fact-Finding Mission to Zimbabwe to assess the scope and impact of Operation Murambatsvina, Habitat, Nairobi.

Chapter 11

How the State Does Business

A recurrent theme of the sectoral and thematic analysis contained in this report is the need for comprehensive reform of the country's system of governance, or 'how the state does business'. The challenge of improving governance is not restricted to any field of activity but is a systemic one, requiring a reorientation of the state, a change in mindset and how it engages with the economy and society. Any sustainable socioeconomic recovery over the long term is dependant on this transformation. This chapter does not set out to offer a detailed strategy for addressing the complex governance challenges facing Zimbabwe, and the considerations it contains have been refracted largely through the prism of the economic analysis which lies at the core of the entire report. Future work on this theme is required and should be informed by the central question of how existing systems of economic and political governance might be reformed over time in order to arrive at a state form that is effective in delivering both development and security for the Zimbabwean people.

11.1 GOVERNANCE INDICATORS

Six governance indicators estimated by the World Bank (Kaufmann *et al.*, 2007) show a substantial deterioration that affects all aspects of life in the country – economic, social and political (Table 11.1):

- *Government Effectiveness* assesses the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies.

- *Voice and Accountability* measures the extent to which a country's citizens are able to participate in selecting their government, as well as freedom of expression, freedom of association, and a free media.
- *Political Stability and the Absence of Violence* measures perceptions of the likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including domestic violence and terrorism.
- *Regulatory Quality* measures the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development.
- *The Rule of Law* measures the extent to which agents have confidence in, and abide by, the rules of society and in particular, the quality of contract enforcement, the police, and the courts, as well as the prevalence of crime and violence.
- *The Control of Corruption* measures the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as 'capture' of the state by elites and private interests.

The message of this and other chapters is that progress in all aspects of life in Zimbabwe has been constrained by poor and deteriorating governance, leaving no room for doubt that in the future the state needs to do business in a more effective, efficient, equitable and transparent manner.

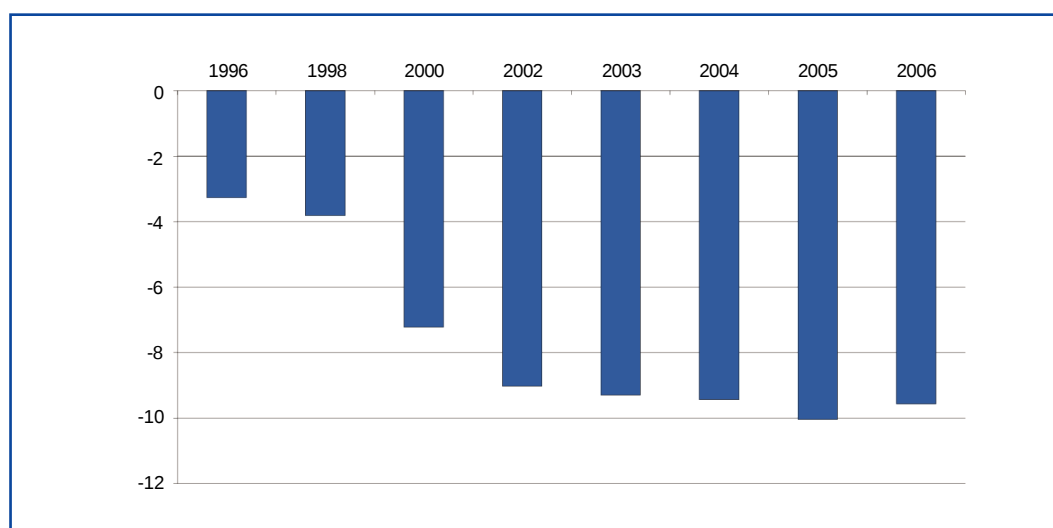
THE CHALLENGE OF IMPROVING GOVERNANCE IS NOT RESTRICTED TO ANY FIELD OF ACTIVITY BUT IS A SYSTEMIC ONE, REQUIRING A REORIENTATION OF THE STATE, A CHANGE IN MINDSET AND HOW IT ENGAGES WITH THE ECONOMY AND SOCIETY

Table 11.1: Zimbabwe: Governance indicators

	1996	2006
Government effectiveness	-0.44	-1.53
Voice and accountability	-0.65	-1.58
Political stability & absence of violence	-0.60	-1.18
Regulatory quality	-0.73	-2.21
Rule of law	-0.68	-1.71
Control of corruption	-0.17	-1.36

Note: An increase in the negative score denotes a deterioration in the indicator.

Source: World Bank (2007) *Governance Matters VI, 1996–2006*; Daniel Kaufmann, et al.

Figure 11.1: Aggregate governance indicators

Note: The greater the negative score, the poorer the state of governance

Source: World Bank (2007) *Governance Matters VI, 1996–2006*; Daniel Kaufmann, et al.

11.1.1 The developmental state

As noted in the first chapter, one key feature of a developmental state, a condition to which the Zimbabwe government arguably aspired when it took office in 1980, is that it should actively foster economic development while avoiding capture by particular groups. One key mode of interaction between states and their economies lies in the extent and nature of their intervention in the economy, with developmental states being characterized by a capacity to implement policies that are supportive of sustainable, broad-based and inclusive growth that over time leads to a structural transformation of the economy. In the case of Zimbabwe, as argued in this report, state-led development not only failed to achieve the intended results but also soon fell

into the trap of state capture, with the undesirable consequences analysed below.

11.2 DETERIORATION OF ECONOMIC GOVERNANCE OVER TIME

At independence in 1980, the new government inherited a highly regulated economy, albeit with a strong private sector and a mostly well-maintained physical infrastructure. Over the ensuing 28 years, the Zimbabwe government's approach to doing business has turned full circle, from a command economy approach in the 1980s, through a market liberalization phase during Economic Structural Adjustment Programme (ESAP), returning to a dirigiste command

economy as the crisis deepened after 1997. The brief period of orthodox economic reforms (ESAP) aside, political imperatives took precedence over economic goals, most marked in the FTLRP but also in exchange-rate policy, the pricing policies of parastatals and, most recently, the Indigenization and Economic Empowerment Act. To the observer, economic policies seem to have been driven by the need to secure immediate and medium term political goals, while paying scant attention to collateral social and economic consequences of such actions.

A number of analysts have argued that developments during the crisis period illustrate both the extent to which the state had been captured, but also the apparent transition from State Capture to Predatory State.¹ The point was forcefully made by President Mugabe in the course of his speech during the 26th August 2008 opening of the First Session of the Seventh Parliament:

‘Corruption imposes a huge cost burden on the conduct of business....efforts to revive the country’s economy could remain a pipedream unless they are supported by stern and decisive action to eradicate the scourge of corruption, which has now reached alarming levels....There will be no sacred cows seeking to hide behind the banner of social positions or party affiliation for their venal tendencies.’²

This change in the orientation of the state is reflected in the government’s deep-seated suspicion of independent business transactions, particularly those that did not involve the government or party. Rather than seeking to facilitate private sector business operations, it became official policy to make

extensive inroads into the private sector by acquiring majority or minority stakes in privately owned firms, a strategy latterly formalized in the Indigenization and Economic Empowerment legislation. In a predatory state, traditional macroeconomic and regulatory policy levers are deemed inadequate and the authorities seek to secure direct control over markets and economic actors. This process of encroachment has been both cause and effect of the economic downturn.

11.2.1 Market failure and the supremacy of the public sector

Since independence, policy-makers have tended to assume that markets will always fail and that the state’s role is to fix them. During the crisis period this focus changed, forcing the state to broaden its role from remedying market failure to seeking to mitigate the impact on sectors, firms and households of the unintended and unforeseen consequences of its own interventions through the takeover of whole sub-sectors of the economy.

This trend is a key explanatory variable which accounts for the proliferation of government ministries, parastatals, state-owned entities, new institutions, committees and working parties tasked with achieving specific goals – such as the state marketing of minerals to counter perceived transfer pricing – or to implement specific policies like price controls. Since the early 1990s government ministries and state administrative structures have increased in number, seemingly in direct proportion to the underlying deterioration in the socio-economic situation. Arguably, a major cause of the country’s economic decline

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DIRECT CONTROL
OVER MARKETS
AND ECONOMIC
ACTORS

¹ The concept of State Capture refers to a situation in which one group uses its disproportionate influence to exploit government policies to its advantage at the expense of society as a whole and in such a way as to secure long-lasting privileges. A predatory state consumes the surpluses of the economy, as government offices come to be treated as income-generating sinecures (World Bank, 2005). More recently, Larry Diamond has argued that such states in turn produce predatory societies where people get rich not through ‘productive activity and honest risk-taking...but by manipulating power and privilege, by stealing from the state, extracting from the weak and shirking the law.’ Diamond, Larry, (2008) *The Democratic Rollback: Resurgence of the Predatory State*, Foreign Affairs, 87 (2), <http://www.foreignaffairs.org/20080301faessays87204/larry-diamond/the-democratic-rollback.html>>p.3

² *The Herald*, Harare, 27th August 2008, p.5.

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has been an overblown state that has operated inefficiently while draining the fiscus.

The combination of mistrust of markets and of the private sector is illustrated in the way the state has managed public enterprises – insistence on control of marketing and pricing policies, denial of managerial autonomy to boards of directors and top management, seemingly arbitrary interventions in operational decision-making, and a monopoly over appointments at all levels.

The net effect has been to widen the role of the state, to curb economic freedom and to undermine the allocative efficiency of market mechanisms, graphically illustrated in government policy towards the pricing of agricultural produce. In 2005, intervention became more direct, with the launch of a military-style Operation Maguta to increase food production.

Over time an increasingly weak state – poorly resourced in terms of finance, skills and equipment – has been called upon to undertake a widening range of increasingly complex, often mutually incompatible, interventions. As shown in the chapter on the financial sector, the fact that almost half of bank lending to the private sector is undertaken by the Reserve Bank of Zimbabwe – in competition with private banks – reflects the government’s conviction that the ‘independent’ private sector cannot, or should not, be trusted to undertake policies deemed essential by the authorities.

11.2.2 Hostility towards foreign direct investment

Partly for historical and ideological reasons, but also because of a commitment to indigenization, policy towards FDI has always, at best, been ambivalent. The Zimbabwe Investment Centre, purportedly created to facilitate both domestic and foreign

investment, has in fact acted as a filter mechanism, enabling the state to block or restructure proposals deemed to conflict with its strategic goals in terms of indigenization or market competition. This hostility towards foreign investment is exemplified in terms of policy towards Foreign Direct Investment (FDI) in the financial services sector. In 1981, for example, the government rejected a takeover bid from one of the world’s largest banks (at the time), the Bank of America, for Zimbabwe Banking Corporation, when the latter’s South African parent, Nedcor, decided to divest. Arguably, the economically efficient policy would have been to accept the Bank of America bid, but instead ZB Bank (then known as Zimbank) was nationalized and became a vehicle for government patronage at the expense of its local shareholders.

11.3 INSTITUTIONAL STRUCTURE AND FUNCTIONAL OVERLAP

As noted throughout this report, Government ministries and state administrative structures have since the beginning of the 1990s increased in number and have been accompanied by an increasing concentration of administrative and financial powers at central level.

As of 2007, Zimbabwe’s government comprised 25 cabinet ministers, 21 deputy ministers and 8 ministers of state in the President’s Office. Coupled with the country’s 10 provincial governors who enjoy the status of resident ministers, Zimbabwe has a total of 64 ministers. Taking the case of one core function alone, namely agriculture – and against the background of the need to contain public expenditure – there seems to be little justification for the existence of five ministers, all dealing either directly or tangentially with land reform and agriculture.³

³ This core function of government is served by (a) the Minister of Agriculture, (b) the Deputy Minister of Agriculture, (c) the Minister of State for Land Reform and Resettlement, (d) the Minister for National Security, Land Reform and Resettlement, and (e) the Minister of State for Agricultural Engineering and Mechanization. As indicated above, to this list should be added the Reserve Bank given the growing number and scope of its interventions in the agricultural sector.

Although the present government structure has 18 core functions represented at ministerial level, this is arguably too large for a country of the size of Zimbabwe, particularly one with a shrinking GDP. Not only does this translate into heavy demands on both the fiscus and the country's constrained human resource base, but it gives rise to duplication, complicating the coordination of service delivery and accountability. State machinery, that has weakened over time as the institutional and infrastructural framework deteriorated, was called upon to do more and more with less and less in terms of funding, resources, skills and above all, experience.

11.4 CONCENTRATION OF POWERS

From 1990, with the expiry of some of the specific clauses of the 1980 Lancaster House constitution, the administrative machinery was restructured and the state began to create new centres of power authorized to override the conventional administrative machinery of government departments, parastatals and local government. Power shifted to the presidency, the central bank and most recently, the military, as well as to a plethora of ad hoc agencies and bodies seemingly established to create what is often seen as a veneer of consultation.

The presidency

The most fundamental change was the progressive centralization and fusion of powers in the presidency. Since 1990, the president has enjoyed extensive executive powers of appointment and veto throughout the civil service and public enterprises, including veto on the appointment of judges as well as the appointment (until 2008) of all 30 seats formerly reserved for whites in Parliament. A strongly centralized system

and concentration of powers has become the hallmark of political governance. In addition, the frequent use of the Presidential Powers (Temporary Measures) Act [Chapter 10:20] has become the norm rather than an exception. Presidential Powers are routinely used for a wide range of measures that normally and more properly should be scrutinized and approved by the legislature. The appointment of no fewer than eight ministers of state within the presidency also illustrates the shift of power from the legislature to the executive.

The central bank

On the economic front, a concentration of decision-making was also evident. In 2003 for example, the president effectively transferred a wide range of decision-making powers from government ministries, especially the Ministry of Finance, to the RBZ. Since then, crucial economic policy decisions, including many that lie far outside the normal purview of a central bank, have been taken and implemented by the Governor of the RBZ. These include setting exchange rates, announcing changes to the tax system, providing subsidies for agriculture, exporters, manufacturers and construction businesses, and bypassing parliament via quasi-fiscal spending programmes that exceed the central government budget approved by the legislature.

Joint Operations Command (JOC)

Comprising all the leaders of the security forces, some senior Cabinet ministers and the Governor of the Reserve Bank of Zimbabwe, the JOC came into public view when it launched Operation Murambatsvina in 2005,⁴ the ongoing Operation Maguta to increase food production in 2006 and, more recently, 'Operation Reduce Prices' in 2007 and other interventions in the economy. This suggests that the JOC plays an important

⁴ In the wake of the government's 2005 'slum clearance' campaign in urban and peri-urban areas, the UN Special Envoy on Human Settlement Issues estimated that some 700,000 people in cities across the country had either lost their homes, their source of livelihood, or both, with a further 2.4 million directly affected (United Nations, 2005).

role in economic decision-making, and that it may in fact be the ‘kitchen cabinet’, with the official cabinet relegated to a rubber-stamping role.

Other agencies and bodies

In addition, on an ad hoc basis, the government has established a plethora of agencies and bodies outside the bureaucracy charged with tackling specific problems. These include: the National Economic Consultative Forum (NECF) launched in 1997; the Tripartite Negotiating Forum (TNF), that included labour, business and government, in 1998; the National Economic Recovery Council (NERC) in 2006, as part of the National Economic Development Priority Programme (NEDPP), a bipartite body comprising government and business; and in 2007 a National Incomes Pricing Commission (NIPC) and a Cabinet Taskforce on Income and Pricing Stabilization, the latter possessing a ‘crack unit’ to implement its positions.

The net effect of this restructuring has been to erode the authority of parliament, while undermining the professional capability and indeed the morale of the public service. The shift to a system of direct controls, invariably exercised without resort to the legislature, has negatively affected transparency and accountability, denying both the legislature and the professional public service the opportunity to carry out their tasks, at the same time limiting media coverage of the decision-making process, public scrutiny and debate.

11.4.1 Policy incoherence and inconsistency

As shown in the chapter on the country’s macroeconomic situation, the government has produced a plethora of turnaround programmes, none of which have been implemented with any discernable degree of success. Coupled with the multiplication of bodies, and no clear lines of responsibility for the design and implementation of policies, the current landscape is characterized by

institutions often working at cross purposes. It is in this light that the decision to create another ministry tasked with ‘policy implementation’ becomes understandable. Such policy unpredictability has been compounded by an apparent move away from a rule-based system towards one characterized by the exercise of discretionary powers.

With different bodies such as the military being coopted for the implementation of Operation Maguta, the conventional arms of government such as the Ministry of Agriculture and Agribank have been marginalized, certainly in terms of policy-making, though they still have a role to play in terms of service delivery. For most of the post-2004 period too, the RBZ has usurped not only the role of the Ministry of Finance, but also that of sector-specific government ministries, such as those responsible for agriculture, mining and transport.

11.4.2 Goal confusion

Examples of goal confusion include long-standing failures to design coherent strategies for public enterprise reform and private sector development. Privatization initiatives have been embroiled with indigenization issues, not to mention widespread allegations of cronyism. It mattered more that private enterprises be owned and managed by ‘the right people’ than that they should be efficient and effective. Similarly, privatization decisions were driven by the need to reduce the budget deficit rather than the imperative of productivity and efficiency and delivering a cheaper and better service to customers.

Conflicting goals are also evident in the field of monetary policy. For example, the 2001 monetary policy, subsequently elaborated and expanded after 2004, was intended to curb inflation while at the same time using interest rate controls to reduce the cost of funding public sector debt and to promote specific sectors and activities – agriculture, home-building and exports. Because the goals were

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POWERS*

mutually incompatible, the strategy failed. Funding narrow state priorities was given precedence over fighting inflation.

11.5 HOW THE STATE SHOULD DO BUSINESS

At the end of the current crisis Zimbabwe will be characterized by a severely debilitated economy, the near collapse of its infrastructure, and a deeply impoverished population that is heavily reliant on international humanitarian assistance. Most of the country's state institutions will be a mere shadow of their past, severely weakened in terms of capacity to both design and implement technically sound policies. The dangers of overloading the state given its debilitated condition should loom large in the calculations of both domestic and international actors in a recovery scenario. Managing expectations will be an essential aspect of supporting sustainable recovery.

The desired shift on to a new growth path will have to start with the strengthening of all aspects of governance. In parallel, the formulation and implementation of a stabilization programme to coordinate fiscal and monetary interventions will be required so as to win back the confidence of domestic and international economic actors, leading in turn to the implementation of a sustainable and comprehensive medium to long term recovery strategy. But for this to happen, the orientation of government should be shifted away from an authoritarian, centralized system based on a command economy to an inclusive (pro-poor) market economy based on democratic principles, accountability and the rule of law.

This process of reforming the State should be rooted in an informed analysis of the political economy of reform in Zimbabwe – which lies outside the scope of this work. A sound historical understanding of previous attempts at reforms in areas as varied as civil service reform, administrative and financial decentralization processes, the role

of the judiciary, anti-corruption initiatives amongst others, will greatly enhance the prospects of success for governance reforms in the context of recovery. In particular, diagnostics which help to throw light on what worked, what did not and why, will be key to designing comprehensive governance reform strategies that are realistic in terms of timeframes, rooted in an understanding of the 'carrying capacity' of Zimbabwe to implement the necessary reforms, that are properly sequenced and that have widespread domestic support.

11.6 POLITICAL GOVERNANCE

11.6.1 Constitutional and legal reform

A reading of the recent historical experience of the country would indicate that consideration should be given to the following reforms:

- The establishment of a new constitution that provides for the unequivocal separation of powers to ensure effective checks and balances between a freely and fairly elected legislature, an independent and impartial judiciary and the executive branch of government.
- The repeal or amendment of laws that are an affront to fundamental human rights and the principles governing democratic societies.
- The rule of law must be restored by ensuring that agents of the state uphold their constitutional duty to protect the country's citizens, and that every citizen has the constitutional right to be heard in an independent and impartial court of law.
- There will need to be a move towards a more functional, rule-based system of government, away from discretionary and relationship-based systems, in order to minimize cronyism and corruption.

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RECOVERY
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11.6.2 Institutional reform and cooperative governance

- The independence, institutional capacity and powers of oversight vested in the Office of the Auditor-General need to be restored and strengthened to ensure strict adherence to laid-down government procedures.
- Annual audited accounts and regular independent evaluations of government departments, major projects, and parastatal organizations must be made available for public scrutiny.
- The scope, efficacy and powers of oversight vested in Parliamentary Portfolio Committees or Select Committees should be extended in order to constrain executive power and ensure greater state effectiveness.
- National economic statistics must be depoliticized, and the confidentiality of information collected from private sector companies ensured. The creation of an autonomous Central Statistical Office needs to be speeded up, with independent directors nominated by the Ministry of Finance, the RBZ and private sector organizations.
- A private sector think-tank should be established, with private sector/donor contributions tasked with ensuring that private sector organizations have the necessary research and strategy formulation capacity to maintain a robust policy dialogue with state institutions. This is of particular importance given the need for a post-crisis developmental state to understand the microeconomic foundations of economic policy (see below).
- A consultative and supportive relationship must be created between the public and private sectors, and between government and civil society, including labour.

- Long term, independent economic decisions should be made without undue political interference; independent institutions should be created and/or reconfigured with clear objectives. These should include, among others, the Reserve Bank of Zimbabwe and a future Land Commission.

11.7 DEVELOPMENT ORIENTATION

11.7.1 Rebuild institutions

Institutional decay is both a cause and a consequence of economic decline as well as a feature of state capture. Right across society, institutions, with the signal exception of civil society which has become stronger as the crisis worsened, have regressed. All walks of life have been adversely affected by the inability of public, and private institutions, to deliver the volume and quality of services required.

Future policy should focus on a combination of rebuilding institutional capability, abolishing redundant bodies and, where necessary, establishing new institutions such as the Land Commission. This will be a lengthy process, not just because it takes years – even decades – to reestablish the credibility and capacity of institutions undermined over a long period, but also because institutions such as the public service, education and health services and parastatals have suffered disproportionately from the exodus of skilled professionals and a consequent serious loss of institutional memory. This is yet another instance of the ‘missing middle’ phenomenon.⁵ Ministries, clinics, schools and parastatals are excessively reliant on youthful, inexperienced personnel because middle management have either sought greener pastures in the private and NGO sectors, or have left the country altogether.

⁵ See chapter 6 on private sector development.

This has profound implications for the process of nurturing a future developmental orientation within the state apparatus, which in the immediate post-crisis period will not have the capacity to perform some of the tasks that it would normally be expected to undertake. At the same time, however, there will be a window of opportunity to ensure that new entrants into the public service are provided with the necessary training, and existing civil servants are retrained, so that the post-crisis state plays a facilitating and supportive rather than obstructionist and dirigiste role in relation to economic recovery processes. Merit-based promotion systems, competitive salary structures, long term career prospects, a two-way traffic of personnel between the public and private sectors, and results-based training for all civil servants, will be some of the key ingredients in ensuring the necessary change in focus in the state apparatus. The notion of the State returning to its 'core business', however Zimbabwean society should over time choose to define this concept, should inform all governance reform initiatives.

11.7.2 Economic governance

- Inclusive and transparent economic policy-formulation processes need to be initiated. This will help to ensure the efficiency of the process of determining priorities among public problems and the allocation of resources to address them.
- There must be a return to macro-economic stability as a firm foundation for sustainable economic growth. It is in light of this consideration that the role of institutions such as the RBZ merit particular scrutiny in order to ensure that the past is not repeated.
- Property rights must be secured.
- Institutions must be built that allow competitive markets to function fairly and efficiently to sustain economic growth.
- Appropriate Doing Business and Investment Climate reforms should be introduced. Many of these might come under a set of first generation reforms in the area of economic governance, and would include as a matter of priority the abolition of a plethora of laws which have accumulated over time and which have served to criminalize the most basic forms of production and exchange.
- Appropriate regulatory frameworks need to be developed that create incentives for the rebuilding of the country's lost human and physical capital.
- Serious consideration should be given to the imposition of a ceiling (expressed as a percentage of the budget approved by parliament) on government borrowing without parliamentary approval and by setting a maximum percentage of the national budget that may be allocated to contingency reserves and/or donor counterpart expenditure not expressly approved by parliament.
- A budget report should be presented to Parliament mid-way through the fiscal year.

THE VARIOUS CONSTRAINTS, OFTEN BY ADMINISTRATIVE FIAT, THAT HAVE LEFT MUCH OF THE POPULATION IN A STATE OF DESTITUTION, WITH SEVERELY RESTRICTED CHOICES AND OPPORTUNITIES OTHER THAN TO EMIGRATE, SHOULD BE REMOVED THROUGH THE ADOPTION OF 'DEVELOPMENT AS FREEDOM' PRINCIPLES

11.7.3 Pro-poor policies

The various constraints, often by administrative fiat, that have left much of the population in a state of destitution, with severely restricted choices and opportunities other than to emigrate, should be removed through the adoption of 'development as freedom' principles.⁶ This involves a process of cultivating the people's capabilities by their

⁶ Amartya Sen's concept of 'development as freedom' is succinctly captioned by his statement: 'What people can positively achieve is influenced by economic opportunities, political liberties, social powers, and the enabling conditions of good health, basic education, and the encouragement and cultivation of initiatives' (Sen, 2000: 5).

THE LESSON IS THAT STATE-LED DEVELOPMENT IS UNLIKELY TO SUCCEED WITHOUT A STRONG LEADERSHIP COMMITTED TO INCLUSIVE GROWTH, BACKED BY WELL-MANAGED INSTITUTIONS, AN HONEST AND CAPABLE PUBLIC BUREAUCRACY WORKING WITH PRIVATE ENTERPRISE AND CIVIL SOCIETY

access to health and educational facilities, the freedom to exchange words, goods and gifts, and the freedom to enter markets, including labour markets. Amartya Sen (2000) identifies five instrumental freedoms, or types of rights and opportunities that help advance the general capability of a person: political freedoms, economic facilities, social opportunities, transparency guarantees and protective security. These can be seen as a process of expanding real freedoms that people enjoy, mainly through:

- Promoting pro-poor growth, being the extent to which the opportunities for employment, production and enhanced incomes reach the poor through improved access to credit and markets.
- Improved economic governance which includes the extent to which growth contributes towards social development in health, education, housing and social security within the context of macro-economic stability.
- The relationship between pro-poor policy and economic growth, mediated through employment creation.

11.7.4 A new focus on the microeconomic foundations of economic policy

A common feature of successful developmental states has been their deep understanding of microeconomics. Hitherto, the prime – usually the sole – focus of policy interventions has been at the macroeconomic level. The microeconomics of how markets work has been ignored. This focus must change, so that policy interventions enhance, rather than hinder, market efficiency. The challenge is clearly set out in the 2008 report of the World Bank's Commission on Growth and Development:

'The growth of GDP may be measured up in the macroeconomic treetops, but all the action is in the microeconomic undergrowth, where new limbs sprout and dead wood is cleared away. Most

growth-oriented policies and reforms are designed to foster this micro-economics of creation and destruction, and, crucially, to protect people who are adversely affected by these dynamics.' (World Bank, 2008: 2)

Markets work best where there is a level playing field so that all firms are treated equally, where entry barriers to the establishment of new businesses are minimal, and where state-provided infrastructure and state institutions reduce operating costs and business risks. By enhancing policy clarity, predictability and credibility, governments can help reduce business risk and thereby foster investment and job creation.

11.8 ADDITIONAL LESSONS FOR THE POST-CRISIS DEVELOPMENTAL STATE

Zimbabwe's experience underscores the need for a new and different model of economic development. Defining and prescribing the boundaries of the developmental state is essentially a political issue that cannot be set by technical criteria. However, valuable lessons can be learned from past experience.

Some protagonists of developmental state theory believe that some of the dictates of the broad 'good governance' agenda stand in the way of rapid economic and social progress and that it is enough for emerging markets to achieve 'good enough governance', defined as 'the minimal conditions necessary to allow political and economic development' (Grindle, Merilee, 2004:525).

Zimbabwe's experience is a cautionary tale and a useful corrective to, if not refutation of, 'good enough governance' as a development path. The combination of what donor agencies and multilateral lenders at one time seemed to believe to be 'good enough governance' and state-led development in Zimbabwe has degenerated progressively into the satisfaction of particularist rather than broader public interests. While accepting that

the broad ‘good governance’ agenda presents formidable challenges to all societies since it implies an ambitious range of institutional changes in order to ensure both sound economic and political development that need to be prioritized and sequenced, the danger lies in circumscribing this aspirational list in order to achieve more restricted goals. ‘Good enough’ governance can easily be gradually whittled down to ‘sufficient’ governance for all time.

In sum, this second-best approach to governance has already failed in Zimbabwe. The lesson is that state-led development is unlikely to succeed without a strong leadership committed to inclusive growth, backed by well-managed institutions, an honest and capable public bureaucracy working with private enterprise and civil society.

Developments since the late 1990s have inculcated a deep suspicion of the state within the private sector, both domestically and internationally. Accordingly, confidence-building measures, as outlined above, will be essential. Without in any way minimizing the crucial role the state will have to play in creating the appropriate environment for rapid, sustainable and equitable growth, the primacy of the private sector as the engine of growth must be acknowledged. In the words of the report of the World Bank Growth Commission (2008:4):

‘Government is not the proximate cause of growth. That role falls to the private sector, to investment and entrepreneurship responding to price signals and market forces. But stable, honest, and effective government is critical in the long run.’

Operational Framework

CURRENT SITUATION

A. Macroeconomic Management

- ❖ Hyperinflation officially estimated at over 11.2 million percent by mid-2008
- ❖ Unsustainable budget deficits and unmanageable public sector debt, foreign and domestic
- ❖ Uncontrolled monetary expansion driven by quasi-fiscal activities
- ❖ Volatile and unpredictable exchange-rate systems (multiple exchange rates, rapid dollarization and a collapsing currency)
- ❖ Pervasive controls in the financial sector
- ❖ Central bank operating outside its mandate
- ❖ Politicization of aid flows

B. Productive Sectors

- ❖ Diminishing international competitiveness
- ❖ Lack of secure and predictable property rights
- ❖ Rapidly-worsening shortage of skills arising from out-migration
- ❖ Hostile investment climate characterized by excessive, volatile and mutually-conflicting government interventions and uncertainty over economic empowerment initiatives
- ❖ Acute shortages of essential inputs, especially fuel, raw materials and intermediate inputs
- ❖ Uncertain agricultural land rights and land tenure insecurity
- ❖ Industrial and mining output down 50 percent to 60 percent since 2000 and all sectors operating well below capacity levels
- ❖ Production jeopardized and operating costs increased by infrastructural deficiencies, especially electricity
- ❖ Business decision-making undermined by volatile, often contradictory, regulatory environment
- ❖ Inadequate and dilapidated productive infrastructure
- ❖ Inefficient and subsidy-dependent public enterprises

C. Poverty

- ❖ High levels of unemployment and decent work deficits
- ❖ Growing informalization and deepening dualism in the economy
- ❖ Serious and rapidly increasing social distress and chronic food insecurity
- ❖ Limited access to financial services by small-scale borrowers
- ❖ Fragmented state-dominated labour administration system
- ❖ Supply-driven education system without a 'pathways' approach
- ❖ Inadequate and dilapidated social infrastructure
- ❖ Estrangement from traditional development partners and processes

D. How the State Does Business

- ❖ Institutional incoherence and inconsistency
- ❖ Contraction of the revenue base
- ❖ Concentration of decision-making in the executive
- ❖ Deteriorating governance indicators

STRATEGIC OBJECTIVES AND THRUSTS

A) Establish sound macroeconomic management

Strategic Thrusts

- ✓ Achieve price and exchange rate stabilisation
- ✓ Carry out fiscal consolidation and exercise monetary restraint
- ✓ Establish independent and orthodox central bank
- ✓ Improve national management of aid flows based on Paris principles

B) Revive and restructure the productive sectors

Strategic Thrusts

- ✓ Rebuild competitive markets
- ✓ Establish clear property rights and land tenure security
- ✓ Utilize diaspora skills and capital effectively
- ✓ Implement Doing Business reforms
- ✓ Ease skills constraint
- ✓ Improve efficiency of public enterprises
- ✓ Provide well maintained productive infrastructure

C) Ensure pro-poor growth

Strategic Thrusts

- ✓ Rapidly improve human development indicators
- ✓ Transform the dualistic structures in the economy
- ✓ Strengthen household food security
- ✓ Develop more demand-driven education and training systems
- ✓ Promote employment-intensive growth within a decent work framework
- ✓ Provide well maintained social infrastructure
- ✓ Engage with international donor community

D) Build a developmental state and good governance

Strategic Thrusts

- ✓ Reform national institutions
- ✓ Expand the revenue base
- ✓ Expand participation in national decision-making
- ✓ Strengthen the rule of law
- ✓ Transform State into a facilitator of private enterprise

STRATEGIC OBJECTIVE A: ESTABLISHING SOUND MACROECONOMIC MANAGEMENT

Short Term (2009–2010)

Strategic Thrust: Achieve price and exchange rate stabilization

Key Actions	Responsibility
➤ Remove interest rate controls and exchange-rate controls	Ministry of Finance/RBZ
➤ Remove capital controls on private individuals	Ministry of Finance/RBZ
➤ Reduce Statutory Reserve Ratios substantially	RBZ

Strategic Thrust: Carry out fiscal consolidation and exercise monetary restraint

Key Actions	Responsibility
➤ Eliminate quasi-fiscal activities	Ministry of Finance/RBZ
➤ Conduct public expenditure review	Ministry of Finance/Parliament
➤ Establish and publish fiscal rules	Ministry of Finance/Parliament
➤ Develop rolling MTEFs	Ministry of Finance
➤ Conduct mid-term budgetary reviews	Ministry of Finance
➤ Introduce budget caps for PEs	Ministry of Finance/Parliament
➤ Establish and publish money supply growth targets	Ministry of Finance/RBZ
➤ Strengthen public financial management, accounting and reporting systems and budgetary processes	Ministry of Finance/Parliament

Strategic Thrust: Establish independent and orthodox central bank

Key Actions	Responsibility
➤ Review RBZ Act 2004	Ministry of Finance/RBZ
➤ Create Monetary Policy Committee (MPC)	RBZ

Strategic Thrust: Improve national management of aid flows based on Paris principles

Key Actions	Responsibility
➤ Undertake an audit of outstanding foreign debt	Ministry of Finance/RBZ
➤ Reach agreement to clear outstanding arrears with BWIs and Paris Club	Ministry of Finance
➤ Carry out debt sustainability analysis	Ministry of Finance
➤ Seek re-classification as IDA only	Ministry of Finance
➤ Undertake audit of public domestic debt	Auditor-General/RBZ
➤ Seek foreign aid to restructure domestic debt	Ministry of Finance
➤ Deepen understanding of key state and non-state actors in management of international aid flows	Ministry of Finance
➤ Develop a National Aid Policy framework	Ministry of Finance

Medium Term (2011–2015)

Strategic Thrust: Price and exchange rate stabilization

Key Actions	Responsibility
➤ Introduce an inflation targeting regime	Ministry of Finance/RBZ
➤ Review capital controls on corporates	Ministry of Finance/RBZ

Strategic Thrust: Improve national management of aid flows based on Paris principles

Key Actions	Responsibility
➤ Establish an agency or department for Development Cooperation	Ministry of Finance/Ministry of Foreign Affairs
➤ Develop, jointly with donors, a performance assessment framework (PAF)	Aid Coordination Agency

STRATEGIC OBJECTIVE B: REVIVING AND RESTRUCTURING THE PRODUCTIVE SECTORS**Short Term (2009–2010)*****Strategic Thrust: Rebuild competitive markets***

Key Actions	Responsibility
➤ Ensure compliance with the tariff structure in line with commitments to COMESA, SADC and the World Trade Organisation	Ministry of Finance, ZIMRA, Ministry of Trade and Industry
➤ Secure lines of credit for private sector inputs	Commercial Banks/RBZ
➤ Improve smallholders access to credit, inputs and higher-value export commodity markets through contract farming	Ministry of Agriculture/Producers' Associations
➤ Facilitate restructuring and capitalization of weak banks through private sector driven mergers and consolidations	Ministry of Finance/RBZ
➤ Remove restrictions to participation of foreign banks	Ministry of Finance/Parliament

Strategic Thrust: Establish clear property rights and land tenure security

Key Actions	Responsibility
➤ Enact legislation to establish a Land Commission, a Land Fund and a Land Tribunal	Parliament
➤ Carry out a land audit	Land Commission
➤ Design a land reform programme	Land Commission

Strategic Thrust: Utilize diaspora skills and capital effectively

Key Actions	Responsibility
➤ Develop and implement a policy framework for return migration	Ministry of Labour /Ministry of Education
➤ Review legislation to enable dual citizenship	Ministry of Home Affairs
➤ Remove restrictions on the operation of MTAs	Ministry of Finance/RBZ

Strategic Thrust: Implement Doing Business reforms

Key Actions	Responsibility
➤ Develop strategies for key sectors (agriculture, manufacturing, mining and tourism)	Line ministries
➤ Establish a private sector think tank	Private sector
➤ Design SMEs policy framework	Ministry of Industry

Strategic Thrust: Ease skills constraint

Key Actions	Responsibility
➤ Carry out national manpower survey	Ministry of Labour/CSO
➤ Facilitate importation of skills	Ministry of Labour

Strategic Thrust: Improve efficiency of public enterprises

Key Actions	Responsibility
➤ Carry out public review of mandates of existing regulatory authorities	Ministry of Finance/Line ministries
➤ Carry out audit of PEs	Auditor-General/SERA
➤ Design strategies for privatization/restructuring	Ministry of Finance/SERA

Strategic Thrust: Provide well maintained productive infrastructure

Key Actions	Responsibility
➤ Restore national power generation capacity and water supply	Ministry of Energy/ZESA/Local authorities
➤ Design cost-recovery and maintenance strategies for public infrastructure and services	Ministry of Finance/Line ministries

Medium Term (2011–2015)

Strategic Thrust: Rebuild competitive markets

Key Actions	Responsibility
➤ Review (ongoing) tariff and non-tariff barriers to trade	Ministry of Finance/ZIMRA/ Ministry of Trade

Strategic Thrust: Establish clear property rights and land tenure security

Key Actions	Responsibility
➤ Implement a sustainable land reform programme, including a transparent settler selection and farm allocation process	Land Commission and Land Tribunal
➤ Reorganize settled farms to ensure their economic viability	Land Commission
➤ Rationalize the occupation of farmland based on the land audit	Land Commission
➤ Issue land registration certificates in resettlement areas and title to commercial farms	Land Commission
➤ Establish the legal, institutional and regulatory framework for land tenure reform in the communal areas	Land Commission/Parliament
➤ Transfer <i>de jure</i> state ownership of the communal land to communities	Parliament
➤ Introduce a land tax on commercial and A2 resettlement farms	Land Commission /ZIMRA Ministry of Finance

Strategic Thrust: Increase efficiency in revenue collection

Key Actions	Responsibility
➤ Draw up a new fiscal regime for mining	Ministry of Mines/Finance/ZIMRA

Strategic Thrust: Ease skills constraint

Key Actions	Responsibility
➤ Establish a National Training Authority	Ministry of Education

Strategic Thrust: Improve efficiency of public enterprises

Key Actions	Responsibility
➤ Enact legislation for public enterprise restructuring	Ministry of Finance/Line Ministries

Long Term (2015 onwards)

Strategic Thrust: Establish clear property rights and land tenure security

Key Actions	Responsibility
➤ Adjudicate and demarcate village and ward boundaries in communal areas	Ministry of Local Government/ Land Commission
➤ Establish common property regimes	Land Commission/AREX
➤ Demarcate and register smallholders' residential plots and arable land	Land Commission/Rural Development Councils
➤ Issue land registration certificates for residential and arable land in communal areas	Land Commission/Rural Development Councils
➤ Introduce a land or unitary tax on smallholders for local administration, land transfers and rentals	Ministry of Local Government/ ZIMRA
➤ Upgrade land registration certificates in communal and resettlement areas to full title	Land Commission

STRATEGIC OBJECTIVE C: ENSURING PRO-POOR GROWTH**Short Term (2009–2010)***Strategic Thrust: Rapidly improve human development indicators*

Key Actions	Responsibility
➤ Review and update all national human development strategies and action plans	Relevant line ministries
➤ Design and operationalize social safety nets	Ministry of Social Welfare/ UN agencies/NGOs
➤ Update national poverty survey	Ministry of Labour/CSO
➤ Update labour force surveys	Ministry of Labour/CSO
➤ Design an Interim- PRSP	Ministry of Finance/Social Welfare

Strategic Thrust: Transform the dualistic structures in the economy

Key Actions	Responsibility
➤ Design policy framework for the informal economy	Ministry of Industry
➤ Create an appropriate regulatory framework for microfinance institutions	Ministry of Finance/RBZ

Strategic Thrust: Strengthen household food security

Key Actions	Responsibility
➤ Announce pre-planting prices as a crop production incentive during two agricultural seasons	Ministry of Agriculture
➤ Rehabilitate AREX infrastructure	Ministry of Agriculture

Strategic Thrust: Develop more demand-driven education and training systems

Key Actions	Responsibility
➤ Establish consultation mechanisms between ministries of education and labour and private sector associations	Ministries of Education/Labour/ Private sector associations
➤ Conduct long term national manpower needs projections	Ministry of Labour
➤ Review mandate and operations of ZIMDEF	Ministries of Labour/Education

Strategic Thrust: Promote employment-intensive growth within a decent work framework

Key Actions	Responsibility
➤ Rationalise institutional overlap in area of labour market issues	Ministry of Labour
➤ Carry out reviews of laws governing labour administration	Ministry of Labour
➤ Finalize the National Employment Policy Framework	Ministry of Labour
➤ Develop a comprehensive Labour Market Information System	Ministry of Labour
➤ Implement labour-intensive national public works programme	Ministry of Labour

Strategic Thrust: Provide well maintained social infrastructure

Key Actions	Responsibility
➤ Carry out social infrastructure needs assessment	Ministry of Social Welfare
➤ Prioritize urgent needs	Relevant line ministries

Strategic Thrust: Engage with international donor community

Key Actions	Responsibility
➤ Engage technical assistance to strengthen national poverty analysis capacity	Ministries of Finance/Social Welfare

Medium Term (2011–2015)

Strategic Thrust: Rapidly improve human development indicators

Key Actions	Responsibility
➤ Design and implement a full- PRSP	Ministries of Finance/Social Welfare
➤ Review the relative benefits of conditional cash transfers and basic income grants	Ministry of Social Welfare

Strategic Thrust: Transform the dualistic structures in the economy

Key Actions	Responsibility
➤ Develop an integrability (active labour market) programme	Ministry of Labour
➤ Enact legislation to promote financial inclusiveness and microfinance institutions	Ministry of Finance/Parliament
➤ Improve credit information infrastructure	Private sector

Strategic Thrust: Strengthen household food security

Key Actions	Responsibility
➤ Improve targeting by national relief bodies	Ministry of Social Welfare
➤ Improve operational efficiency of emergency food delivery systems	Ministry of Social Welfare/ UN agencies/NGOs
➤ Reduce grain price volatility through domestic trading and the maintenance of buffer stocks	Ministries of Agriculture/Finance
➤ Develop a demand-led, farmer-centred agricultural research and extension programme	Ministry of Agriculture/Growers' associations

Strategic Thrust: Develop more demand-driven education and training systems

Key Actions	Responsibility
➤ Design a reform programme for the education and training system	Ministry of Education/Private sector

Strategic Thrust: Promote employment-intensive growth within a decent work framework

Key Actions	Responsibility
➤ Review existing labour administration legislation	Ministry of Labour/Trade Unions/ Employers' organizations
➤ Operationalise the comprehensive Labour Market Information System	Ministry of Labour
➤ Develop an integrated and decentralized labour administration system	Ministry of Labour

STRATEGIC OBJECTIVE D: BUILDING A DEVELOPMENTAL STATE AND GOOD GOVERNANCE**Short Term (2009–2010)*****Strategic Thrust: Reform national institutions***

Key Actions	Responsibility
➤ Review civil service pay scales	Ministry of Public Service
➤ Design civil service retention scheme	Ministry of Public Service
➤ Carry out review of inter-ministerial functional overlap	Ministry of Public Service
➤ Design a manpower recovery plan for the public sector	Ministry of Public Service
➤ Build oversight capacity of the Auditor-General	Ministry of Finance
➤ Carry out review of operations of the State Tender Board	Ministry of Finance/Parliament
➤ Create an autonomous Central Statistical Office (CSO)	Ministry of Finance
➤ Design a civil service reform programme	Ministry of Public Service
➤ Train key civil servants in results-based management and budgeting	All line ministries

Strategic Thrust: Expand the revenue base

Key Actions	Responsibility
➤ Rationalize the tax structure	Ministry of Finance/ZIMRA
➤ Increase efficiency in revenue collection	Ministry of Finance/ZIMRA
➤ Develop incentive structure for informal enterprises to be registered	Ministry of Finance

Strategic Thrust: Expand participation in national decision-making processes

Key Actions	Responsibility
➤ Review existing state/civil society/private sector consultation mechanisms	Civil society umbrella groups and private sector organizations/Line ministries
➤ Review current status of political, administrative and financial decentralisation processes	Ministries Local Government/Finance
➤ Build oversight capacity of parliamentary portfolio committees	Parliament
➤ Build multi-stakeholder oversight mechanisms for national minerals wealth fund	Ministry of Finance/Auditor-General/Chamber of Mines/NGOs

Strategic Thrust: Strengthen the rule of law

Key Actions	Responsibility
➤ Review laws restricting media, freedom of association and freedom of speech	Ministry of Justice/Parliament
➤ Initiate constitutional review process	Ministry of Justice/Parliament

Medium Term (2011–2015)***Strategic Thrust: Reform national institutions***

Key Actions	Responsibility
➤ Implement civil service restructuring	Ministry of Public Service
➤ Restructure the Investment Centre in consultation with the private sector	Ministry of Finance/CZI

Strategic Thrust: Expand the revenue base

Key Actions	Responsibility
➤ Design and implement aid obsolescence strategy	Ministry of Finance/Line ministries

Strategic Thrust: Transform State into a facilitator of private enterprise

Key Actions	Responsibility
➤ Train key staff in relevant ministries in the microeconomic foundations of economic policy and foreign trade issues	Ministries of Finance/Trade and Industry
➤ Carry out joint state/private sector growth diagnostics	Ministries of Finance/Trade and Industry/Private sector associations
➤ Design and implement international competitiveness strategy Private sector	Ministry of Trade and Industry/

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