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AN ENQUIRY INTO THE FUTURE ECONOMIC GROWTH IN ZIMBABWE

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ABSTRACT

Economic growth is an elusive goal in Sub-Saharan Africa where research has highlighted countless causes of its poor growth and development. The term economic growth is defined as ‘an increase in the capacity of an economy to produce goods and services, compared from one period of time to another’. In the long run, economic growth should give rise to an improvement in the quality of life of the citizens of a country. The common measure of economic growth of a country is the Gross Domestic Product [GDP]. This paper argues that there is poor economic growth in Zimbabwe. The descriptive survey design was used to collect data from Government; Business and Labour units in Masvingo situated about 300km South West of Harare. Questionnaires and interviews were used to collect data which were then recorded and analysed on tables, pie charts and graphs. The target sample size in question was 100 respondents comprising retailers, service providers, SMEs (informal trader), manufacturers’ and government departments. However, the research ended up with a sample of 96 respondents because 4 respondents failed to return their questionnaires and could not be contacted for interviews. The challenges bedevilling future economic growth of Zimbabwe have been identified in this paper as poor law and order maintenance, corruption, allocative and productive inefficiencies, lack of separation between political and economic issues, undeveloped/under-developed human mindsets, inflationary pressures and policy inconsistency. The paper also argues that unless an in-depth understanding of policy and empowerment of the Small to Medium Enterprises (SMEs) and Micro Finance Institutions (MFIs) is done, the future is bleak for the economy of Zimbabwe. The paper goes further to call for an understanding of policy and its implementation into the dynamic and complex
socio-economic environment. It also examines the capacity in Industry and Commerce in Zimbabwe and compares it with what is currently obtaining at regional and global levels and explains the constraints that stifle the nation’s economic growth. The paper reaches the conclusions that it is only through technological advancement, motivation of people to save and provision of capital to Industry and Commerce by financial institutions, policy consistency by government, empowerment of SMEs and MFIs, stimulation of Foreign Direct Investment [FDI] and appointment of key personnel on merit rather than particularism that would ensure economic growth for the future in Zimbabwe. Economic growth thus can be achieved in the long term if current leaders focus on long term solutions rather than what benefits them now without thinking of future generations, hence the need for innovation for sustainable development.

**KEYWORDS:** Economic Growth, Empowerment, Policy Consistency, Quality Of Life. Gross Domestic Product, Sustainable Development, Dollarization.

**INTRODUCTION**

Following a decade of economic meltdown and hyper-inflationary pressures, the Zimbabwean policy makers in January 2009 abandoned the Zimbabwean dollar in favour of a multi-currency system, ‘as a way of trying to avert macro-economic instabilities [Nzaro and Njanike, 2010]. On the 12th of April 2009, the Zimbabwean dollar was formally suspended as a legal tender. In the words of Tendai Biti, Minister of Finance, in his maiden address to Parliament, he said, “the Zimbabwean dollar is no longer a currency that the public and any trader will accept, our national currency has, thus become moribund”. This meant the adoption of a number of currencies as official modes of exchange in place of the depreciated Zimbabwean dollar. Under the system and according to Kramenko et al [2010], transactions in hard currencies were authorised, payment of taxes were made mandatory in foreign currency and the foreign exchange system became largely liberalised.

The introduction of the multi-currency system notably saw the month on month/ year on year from an unimaginable 89,700 zillion [89,700,000,000,000,000,000,000.00 in November 2008 [Hanke and Kwok, 2009:355] to 6.216% by end of 2009, according to the Zimbabwe Statistical Office. Concomitantly, the quality of life for the majority of Zimbabweans was generally improving [Madzimure, 2009]. According to the Reserve Bank of Zimbabwe [RBZ], the Zimbabwean economy has witnessed substantial growth since 2009 with an estimated 8.1% growth in 2010, up from 5.7% in 2009, and about 9.3% in 2011. Conversely, the adoption of the multicurrency system by Zimbabwe resulted in the loss of seigniorage and
the national currency, which has been regarded as loss of autonomy and monetary sovereignty. It is in view of the circumstances and conclusions highlighted that this paper calls for an enquiry into the future economic growth of Zimbabwe.

2.0 Methodology

The research study used the qualitative descriptive survey design to draw information from respondents on the enquiry into the future economic growth in Zimbabwe. Respondents were interviewed and/or given questionnaires for their completion before these were collected, processed and analysed. Out of an initial sample of 100 respondents, only 96 were interviewed and responded favourably through completion of the sent questionnaires. The descriptive survey research design is a very popular and powerful tool when it comes to assessing opinions and trends in research studies. Information obtained from such a design is then presented, analysed and interpreted through the use of graphs and tables.

The respondents in this study comprised retailers, service providers, informal traders [SMEs], manufacturers and government departments.

3.0 The Concept of Economic Growth

The term economic growth as earlier on alluded to is ‘an increase in the capacity of an economy to produce goods and services, compared from one period of time to another’. In the long run, it should meet the key objectives of an improvement in the standard/quality of life of the citizens of a country and sustainable development of the respective nation.

In an effort to address the afore-mentioned key objectives of a nation with regards to economic growth, this paper looked at six thematic parameters namely; measures that enhance macro-economic policies; causes of inflationary pressures; effectiveness of dollarization as an inflation controlling mechanism; the impact of non-inflationary growth; constraints of productivity on economic growth; and the contribution of financial institutions towards growth and development.

3.1 Measures that enhance Macro-economic policies

Macroeconomic policies according to Grant (2000) are the long term measures an economy would put in place in its quest to grow and develop (improve the living standards of its citizens). According to Beardshaw (1998), macroeconomic policies are the conditions that countries set to attain in order to achieve prosperity in the long run.
There are 4 basic macroeconomic policies that every economy aims at attaining in the long run, and these are employment, stable general price level, output and economic growth. The discussion to follow will focus mainly on the measures that developing countries, and in particular, Zimbabwe can employ to enhance own macroeconomic policies in their quest to grow. The rationale behind countries setting the 4 objectives above is for their economies to attain economic growth. Grant, (2000) argues that policies that can promote economic growth can be generally put into two categories, namely demand-side and supply-side policies. Demand-side policies are associated with the Keynesians who argue that these policies promote economic growth by ensuring that aggregate demand (AD) rises at a smooth rate in a given economy over time. The policies involve active or discretionary demand management i.e. the government should manipulate AD by means of fiscal policy – which acts through raising government spending and/or cutting taxes when the private sector’s demand is too low and vice versa.

Keynesians tend to favour changing government spending rather than taxation in the belief that changes in government expenditure tend to have a greater multiplier effect as the recipients of such expenditure are known for having high marginal propensity to consume (MPC) than taxpayers. Grant (2000) goes further to assert that supply-side policies on the other hand seek to promote economic growth by increasing the productive capacity of the economy via raising quantity and quality of factors of production. The New Classical Economists favour free market supply-side policies which include trade union reforms in an economy, privatization, commercialization, deregulation, direct tax cuts as well as benefits cuts. Keynesians on the other hand go for interventionist supply-side policies including increasing government spending on education, training and investment grants. Most economists, the world over, favour a combination of demand and supply-side policies to make growth compatible.

Romer (1989) as cited by Showdon B and Vane H.R (2002) argues that a country can implement economic growth to raise the welfare of all individuals in the economy. Showdon and Vane go further to make reference to the Pacific Basin Model of economic development which subscribes to the vision of a prosperous world order that was based on transfer of prosperity from the Northern rich states to the Southern poor states. Showdon and Vane (2002) in quoting Lucas (1988) observe that the consequences for human welfare involved questions around sustained economic growth as the most important determinant of living standards. Therefore there is need for developing economies to understand causes of economic growth and to review the differential growth performances of countries such as
India (large poor), USA (large rich), Sierra Leone (small poor) and Switzerland and Japan (small rich), and let alone consequences of such countries for human welfare improvements.

3.2 Measures that could be used to enhance macroeconomic policies in Zimbabwe.

The experiences (referred to in the preceding section) of both developed and developing states go a long way in explaining the significance of economic growth when it comes to improvement in living standards of human beings, the world over. In the case of Zimbabwe a substantial number of measures can be used to enhance its macroeconomic policies, in its quest to grow and develop. Some of the critical measures the country can employ in this regard are discussed in detail below.

3.2.1 Measures targeted at reducing unemployment level and increasing output.

Zimbabwe has not done much in the area of reducing unemployment after it had gone through a devastating recession in the period 2006-2008. Keynesians believe that unemployment, in an economy, is caused by lack of AD and advocate for increasing demand (DD) as shown in the diagram below:

![AD curve diagram](image)

The diagram has it initially that output Q is produced in an economy, but however this output level is below full employment level, Q* (and the economy is in a deflationary gap). Thus an increase in government expenditure would shift AD curve from AD to AD! thereby raising output to full employment level (Q*). Increases in government expenditure have a magnifying effect on an economy’s GDP because of the multiplier effect. Hence it is critical for Zimbabwe to massively use idle capacity to boost its productive capacity to create
employment and in the process enhance one of the fundamental macroeconomic policies countries seek to attain in the long run, in their growth processes (that of increased output).

3.2.2 Fiscal Policy Measures and Economic Growth in Zimbabwe.

By Fiscal policy (FP) we mean the measures that a country can adopt with the aim of influencing AD in the economy. According to Rodan (1943) backward economies were mainly characterized by low disposable incomes, with low buying power, and further by high unemployment levels and underemployment in agriculture. He goes further to argue that for such countries to break out of such a predicament, it was necessary for them to industrialize. Rodan’s work was refined by Nurkse (1953) who says that backward states were caught in two vicious (interconnected) poverty circles i.e. from both demand and supply sides of their economies. Zimbabwe therefore is found wanting in both demand and supply sides of development. Hence for enhancement of its macroeconomic policy of increasing output it should massively address the issue of income and wealth redistribution with a lot of rationality and impartiality as a precondition for economic growth.

3.2.3 Monetary Policy Measures and Economic Growth in Zimbabwe.

Monetary policy (MP) refers to measures that monetary authorities of a country can employ to influence the level of money supply (MS) in an economy. The economy is in a deflationary state in terms of Money Supply and therefore Zimbabwe should put in place measures that would influence the level of Money Supply (MS) in this multi-currency era to grow. Nurkse (1953) argues that developing states faced serious problems when it came to generation of savings and capital stocks for investment purposes. The rich people for example, in such states, who could be expected to save, could not do so, because they had the tendency to copy consumption patterns of advanced states (so called duesen berry effect) which reduced the marginal propensity to save (MPS) (the demonstration effect).

Nurkse has it that the preconditions for backward states to break out of the poverty circles were creation of strong incentives for investment along with increased mobilization of investable funds. Zimbabwe should create conditions that are critical for luring foreign direct investment (FDI), lucrative tax rate regimes (income and corporate tax systems), as well as come up with legislation that stresses the requirements of a capitalist economy, in its quest to generate capital stocks needed for economic growth. It should also invest massively in human capital to equip it with entrepreneurship skills and management capabilities which are a pre-requisite for economic growth, (Hirschman 1958). A country can have capital stock for economic development, but as long as its human capital is not skilled, economic growth may
not come its way (the case for Zimbabwe’s agrarian reform and newly instituted Indigenisation Act).

Therefore Zimbabwe’s MP should attempt to encourage private investment and consumer spending by relaxing restrictions on Commercial Banks’ lending activities, and lowering the rate of interest as well. It is argued however, that for MP to be effective it should be used in conjunction with FP if the country’s policies are to be consistent and reinforce each other.

3.2.4 Price policy measures and economic growth.

The effects of hyperinflationary environment that befell Zimbabwe in the period 200-2008, have not been overcome, as yet. The impulse price adjustments which were a feature of the day in that period still bedevil our general price level today (in this multi-currency era). The government’s efforts to combat inflation can be reinforced through reintroduction of policy measures such as price controls, which are a good weapon for attacking symptoms of inflation in an economy, (Grant, 2002). Grant asserts that price controls combined with income policies may deal well with the problem of cost-push inflation. Income policy measures are aimed at linking the growth rate of national income to that of productivity, so as to prevent excessive rises in factor incomes which raise costs and hence the general price level. Hence for stability to obtain in the economy, government should put in place price control measures that reinforce the rate of growth of income (which should also be directly linked to the growth rate in productivity) for its economic growth to be compatible.

In the need to remedy cost-push inflation, the government of Zimbabwe can reduce corporate tax rate, which will lead to a fall in costs of production to firms. This can be attained by introducing measures like reducing indirect taxes and cutting down on income tax, in an attempt to lower wage claims, reduce prices charged by government concerns, subsidise production costs and lower wages in the public sector, (Grant 2000). It is argued that the above mentioned measures are critical when it comes to enhancing stability of prices as a macroeconomic policy, all countries of the world aim at attaining. The government can also come up with measures aimed at addressing its balance of payment (BOP) position. Measures can be taken to correct BOP disequilibrium, which depends on the size, cause and the priorities of the government. It is important for the government, according to Grant (2000), to put in place measures that allow the exchange rate to be determined by forces of demand and supply, impose import controls (import substitution) as well as improve competition of the country’s goods and services abroad (export-led growth). The Zimbabwean economy has continued to fail to score in its desire to increase the level of its exports relative to imports; hence more funds are used on imports as compared to that
generated from exports. Measures have to be put in place that boost domestic production and at the same time reduce importation. For instance, tariffs may be imposed that make imports more expensive than local goods and services and by so doing domestic production would increase. The country would have excess goods for exportation which would then generate the much needed foreign currency for the economy.

### 3.2.5 Key macro economic considerations for economic growth

The discussion above was premised on the four fundamental macroeconomic policies, of employment, general price level, output and economic growth, which economies pursue in their quest to grow and develop. A number of measures advocated for by scholars who could be used to enhance the policies were outlined and elaborated from both the supply and demand sides. The main policy measures discussed are monetary policy, fiscal policy, income policy, price policy and balance of payment policy. It was however; argued that if a country crafts legislation heavily premised on savings generation for investment purposes, encouraging income and wealth redistribution and export led growth, then its vision of economic growth will be a reality. The major challenges facing the economy as alluded to by the respondents however, included sound policy formulations and their immediate dumping thereafter (e.g. ESAP, ZIMPREST, MERP, BACCOSSI) etc and the non-independence of the Central Bank (the formulator of MP – which has the main influence on the whole economy when it comes to MS and economic growth). Unless the government successfully implements the policies parliamentarians craft from time to time, all the measures used to enhance such policies would be in vain, and the economy would remain far away from realizing economic growth.

### 3.3 Causes of Inflationary Pressures in an Economy

Inflation is defined as a sustained or continuous rise in the general price levels [Makinen, 2003]. This view was supported by Goldenweiser as quoted by Mutungwazi [2005] who asserts that inflation occurs when the volume of money actively bidding for goods and services increases faster than the available supply of goods. Such inflation is caused by a number of underlying factors as shown in the forthcoming section.

#### 3.3.1 Theoretical Causes of inflation

Monetarists strongly believe that the major cause of inflation is the increase in money supply. This assertion is based on the quantity theory of money as proposed by Milton Friedman which says; MV=PY

Where M=Money supply

V=velocity of circulation
The Monetarists assume that within the same period that real growth and the velocity of circulation are constant; an increase in money supply will lead to an increase in prices. The increases in wages and prices adjust quickly and will not be observable. Inflation is always and everywhere a monetary phenomenon according to Monetarists.

Keynesians led by Maynard Keynes argue that inflation is not only influenced by money supply growth alone. They argue that inflation can be caused by demand pull factors. This is when customers demand more of the available goods and services leading to shortages that will send prices rising. They also attribute inflationary pressures to cost push factors. This is where increases in wages or increases in the cost of production lead to prices of finished goods being pushed up.

Inflation can also be caused by exchange rate factors. If a country imports goods and services, its prices are affected by changes in the exchange rate. If the domestic currency depreciates against the currency of the country where goods are imported from, that has an effect of raising prices in the domestic market.

3.3.2 Causes of Inflationary Pressures in Zimbabwe

Empirical evidence from the research found out that in Zimbabwe inflation has been as a result of a number of factors:

3.3.2.1 Food price increases

The government scrapped import duties on basic commodities in 2009 to encourage the flow of these commodities into the country after the emptying of shop shelves in the wake of the hyperinflation. The reinstatement of import duties in July 2011, at a time when industry remained depressed, led to a general increase in the prices. According to the RBZ Monetary Policy Statement of July 2011, annual food inflation accelerated from 2.3% in May 2011 to 3% in June. This is likely to increase as a result of the duty import reinstatement. Zimbabwe experienced a number of price increases, with most changes being done bi-annually. Out of the research sample in question, 43.75% of all firms interviewed showed that they increased prices semi-annually. Such increments after some time have managed to keep inflation figures low to a single digit of around 5%. However, other firms representing 6.25% of the population changed their prices after every three months. This could have been attributed to efforts by business to deal with price irregularities that were brought by the multicurrency era.
Chief amongst the factors that caused such increases especially bi-annually was the increase in the cost of operational expenses. There are also other factors that contributed to this rise as the fall in value of the dollar against the rand, making imports from South Africa dearer. The resulting action was to up prices to cater for such changes. In addition, the government made an imposition of import duty on food items around June 2011. This upped the general prices of imported goods.

The increased importation of goods was believed to have resulted from the low levels of productivity in the Zimbabwean economy. About 43.75% of the interviewees’ believed that low production had a bearing on the general increase in prices.

3.3.2.2 Low productivity resulting from lack of technology

The cost of production of goods is reduced by the employment of technology. This is a direct result of increased productivity. According to Haberter (1960:7) if the best use is to be made of productive resources, then the industries’ cost will fall leading to reduced prices. The Zimbabwean case has been characterised low productivity against a background of obsolete
technology. This has had a tendency of pushing the costs of production high leading to increase in price levels.

### 3.3.2.3 Low capacity utilization

Capacity utilization refers to the extent to which an enterprise or a nation actually uses its installed productive capacity. Thus it refers to the relationship between actual output that is produced with the installed equipment and the potential output which could be produced with it if capacity was fully used. From the research, it was found out that most Zimbabwean firms are operating at above medium capacity. A 50% of the sample population firms were operating at between half their full capacity to three quarters their capacity [50-75%]. Few firms operated above 75% capacity.

**Table 1: Capacity Utilisation Schedule**

<table>
<thead>
<tr>
<th>Capacity Utilisation Rate [%] Categories</th>
<th>Results</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 - 25</td>
<td>6.25%</td>
</tr>
<tr>
<td>25 – 50</td>
<td>18.75%</td>
</tr>
<tr>
<td>50-75</td>
<td>50.00%</td>
</tr>
<tr>
<td>75-100</td>
<td>25.00%</td>
</tr>
<tr>
<td>Total</td>
<td>100%</td>
</tr>
</tbody>
</table>

Though there are about 75% companies in Masvingo working at above medium capacity, these firms continue in failing to meet the demands of the market, hence result to importation to supplement their local production. A further research should be done at national level to ascertain if most firms are operating at above 50% capacity. Also a further research to ascertain why such firms continue to fail to meet national market demands should be done. One key factor for this argument is that there are increased operational expenses, hence the reason for not achieving full capacity status.

### 3.3.2.4 Price disparities caused by the introduction of the multicurrency system

The introduction of the multicurrency system has led to a mismatch in prices that has led to, in most cases, increases in costs of production. The prices of raw materials have in some instances been highly unstable and in some cases going above the fair prices of the finished products. This has been exacerbated by the shortage of coins as change. Retailers have capitalised on the shortage of change to round off prices, leading to an increase in the prices of commodities.
3.3.2.5 Poor law and order situation

There is a general lack of citizen responsibility by people in management. Such people cause artificial shortages for their personal gain so that prices will rise. Corrupt tendencies and allocative inefficiencies have the effect of increasing prices of goods. In Masvingo it was found out that there are times when commodities like cement for example, are supplied to wholesalers but then released in small quantities and channelled to the black market that charge exorbitant prices and causing shortages.

3.4 The Effectiveness of Dollarization in controlling inflation

Dollarization emerged in the 1980s as an economic phenomenon in Latin America. Dollarization is defined by Cohen (2000) as the legal adoption of the dollar as a full replacement for local money. Cecchetti (2008) concurred and said it is when one country adopts the currency of another country for all its financial transactions. He further suggests that the currency may not necessarily be the United States dollar. Monaco used the French Franc in 1865 and it now uses the Euro (Cecchetti; 2008:473). Investopedia defines dollarization as situation where the citizens of a country officially or unofficially use a foreign country’s currency as legal tender for conducting transactions. It goes on to say that the main reason for dollarization is because of greater stability in the value of the foreign currency over domestic currency. It therefore implies that dollarization has been seen to be effective in controlling inflation.

According to Ortiz (1983) as cited by Ghalayani (2011) dollarization can be differentiated between official (de jure), unofficial (de facto) and semi-dollarization. De facto occurs when residents, generally in private transactions, prefer the foreign exchange over domestic currency because of the bad track record of the local currency. The practice is not classified as legal tender. Residents of the country protect themselves against currency depreciation and high inflation. Official dollarization is when foreign currency is given legal tender status and there is no domestic currency. Examples of countries that have used de jure include Panama, El Salvador and Ecuador. Semi-dollarization is where both the domestic and foreign currency is used as legal tender but foreign currency plays a secondary role to domestic currency.

In Lebanon dollarization was a reaction to economic instability and high inflation. Gosh et al (1998) provided empirical evidence that countries with high levels of dollarization sacrifice the flexibility of their monetary policy but gained long term benefits of lower inflation and a more stable exchange rate, they noted that sample economies exhibited faster economic growth than non-dollarized ones.
Inflation has been defined by Cecchetti as the rate at which prices in general are increasing over time. In Zimbabwe the rate of inflation had reached very high levels, over 2million percent when authorities decided to dollarise. The decision to dollarise was largely prompted by the high levels of inflation and the depreciation of the exchange rate. In Vietnam the high inflation was caused by loose monetary policy and the dramatic depreciation of the national currency, Goujon (Journal of Comparative Economics, 2006; 34; 564-581). In his findings he concluded that dollarization managed to bring inflation levels down for Vietnam although the Central Bank lost control of the monetary policy and it could also not react to crises within the banking industry as it was not responsible for printing the money.

In Ecuador, within six months of dollarization, the interest rates dropped, the banking system re-established itself, growth resumed and inflation fell drastically, (Cecchetti 2008:473). Ecuador managed to be integrated into the world markets, increasing its trade and investments because of dollarization. The fear of depreciation was removed as a strong currency was in use.

In a research conducted by Ghalayani in Lebanon (Euro journals; 2011; 14) it was found that dollarization had brought down inflation to one digit levels.

3.4.1 The Zimbabwe “dollarization”

In Zimbabwe ‘dollarization’ was neither sought nor encouraged by monetary authorities when it started. The lack of confidence in the domestic currency brought in de facto. Citizens in 2008 started preferring transacting in American dollars and the South African Rand. The Zimbabwean dollar had been removed thirteen zeros since 2006 but it still continued to deteriorate. In late 2008 another twelve zeros were slashed and this, together with the growing political uncertainties provided an opportunity for speedy dollarization. The monetary authorities themselves were printing a lot of the local currency to finance their budget deficit and for quasi fiscal operations. The exchange rate was fixed and this gave rise to a thriving black market. It meant that citizens would get their useless domestic currency from the bank and trade it on the black market for a better currency to be able to transact. It was believed that even the monetary authorities would print money and trade the local currency on the black market for foreign currency. This further fuelled inflation and the lack of confidence in the local currency. Inflation rose to over 200 million percent and prices would more than double within 24 hours, Ploch (2010).

The high level of inflation was mainly as a result of the unsustainable growth in money supply and the low levels of productivity in the local industries. Most basic commodities were imported from the neighbouring South Africa and so imported inflation did not spare
Zimbabwe. It became evident that the local currency could not transact anywhere except in
government departments. The problem was that the government departments needed currency
with which to carry out their transactions too, but what they were collecting could not be used
in transacting. It was inevitable that dollarization be official. In 2009 the Zimbabwean
monetary authorities announced the adoption of a multicurrency system, where the South
African rand, the American dollar and the Botswana pula could be officially used to transact.
The kind of dollarization in Zimbabwe was unique in that although it announced a
multicurrency system, the American dollar is the currency that is used in financial reporting
and in most business transactions.

3.4.2 How effective has been dollarization in reducing inflation in Zimbabwe?

According to Ploch (2010) as cited in the Congressional Research Service paper, Zimbabwe’s
Gross Domestic Product had decreased over 50% since 2000, unemployment was estimated
at 90% in 2008 and inflation was 200 million %. After the introduction of the multicurrency
system in 2009, inflation fluctuated between -3% and 1%. This was mainly because there was
no exchange rate in use, goods which had disappeared from the shelves, because of price
controls, was back on the shelves. The demand pull factors were eliminated by the
introduction of the multicurrency system. In 2009 the Minister of Finance presented a budget
of US $1.9billion, in 2010 the figures rose to US$ 2.25billion. Inflation rose to 3.5% and in
2011 it is estimated to rise to almost 4%. The negative growth that was experienced prior to
the multicurrency period has been reversed as Gross domestic Product has been recorded at 4.8%.
The industries that had been shut down during the hyperinflationary period have started
operations. Although most industries are still operating way below full employment, citizens
can get some locally produced goods. Inflation is caused by low productivity which makes
the few available goods fail to meet demand leading to constant rises in prices. The locally
produced goods together with the basic commodities that citizens have been allowed to
import duty-free have kept inflation levels down. Just like in the other countries that have
dollarised, Zimbabwe has experienced reduced levels of inflation.

It however remains to be seen if this one digit figure can be sustained given the failure by the
government to attract foreign investment and to utilise productive capacity to its maximum.
While the multicurrency system stabilized the inflation rate, it might be a temporary
phenomenon if the productive capacity is not utilised, if the American dollar continues to
slide against the rand. This is so because currently most of our goods come from South
Africa. If the American dollar is to continue to depreciate against the Rand, this will affect
the prices in Zimbabwe.
The current call for wage increases is another milestone that could retard the achievements made so far by the multicurrency system. Given the low productive capacity that is obtaining in industries if salaries are continuously increased the unit cost of production will increase resulting in increased prices.

Currently Zimbabwe has liquidity challenges as it cannot print the American dollar. This means that the cost of borrowing the scarce commodity is high. The high interest rate experienced by businesses is passed on to consumers in the form of increased prices. In the long run if liquidity does not improve the inflation rate may continue on an upward trend.

The absence of small denominations when the multicurrency system was introduced gave rise to price distortions. Prices of goods had to start at $1 because there was no smaller denominations and no change when one produced $1. Attempts have now been made to address the problem of change by creating accounts in large supermarkets where the small change will be credited for use on the next visit or credit notes given as change for use on one’s next purchase. These still pose challenges where the customer does not frequent that shop.

Another observation that the researcher noted is that the Zimbabwean citizens need to change their mind set and appreciate acceptable profit margins in business. In the hyperinflationary period each trader aimed at profit margins of 100% and more to be able to restock. After the introduction of the multicurrency system, traders still expect high profit margins thereby making goods very expensive.

Despite the above findings, ‘dollarization’ has managed to bring down the rate of inflation in Zimbabwe. This is evidenced by the stability of prices in general. In this research study, it was also found out that the greatest part of the population sample (62.5%) strongly agreed that the introduction of the multi currency system brought about price stability.

**Figure 3: Multicurrency System brought about Price Stability**
3.5 The impact of non-inflationary growth on economic growth of a country

Non-inflationary growth is the growth of the economic activity of a country without any tendency to inflate prices. Other economists however are of the opinion that a modest inflation rate may actually be good for growth.

The theory of inflation states that inflationary pressures will inevitably result from high levels of economic activity defined as real GDP growth that exceeds some natural or normal rate. The essence of the theory of inflation is that when the money supply grows faster than the money demand balances, inflation occurs, that is inflation is dependent on the growth rate of money demand.

3.5.1 Economic indicators of inflationary pressures in growth period

3.5.1.1 The unemployment rate in relation to full employment.

On average, labour comprises roughly two thirds of total production costs for business. When unemployment rate reaches or falls below full employment, labour shortages build. As producers try to expand production and find labour being increasingly scarce, they employ overtime which is costly and also the pressure for wage increases mounts up. This then translates to high production costs which in turn lead to high prices of goods and services and this leads to an increase in inflation.

3.5.1.2 Labour cost index.

This refers to wages, salaries and benefits paid by firms to their employees. Even in high technology US economy labour comprises two thirds of total production costs to a firm. If the index is rising at a fairly rapid pace and consumer demand is strong, firms are likely to pass on higher production costs to consumers by raising prices. The majority of Zimbabweans in formal employment are earning wages below the poverty datum line. As the economy grows more and more workers are now demanding decent salaries and wages. Obviously as companies concede to these wage demands they also factor these increased salaries in their prices thereby contributing to increased inflationary pressures.

3.5.1.3 Utilization of productive capacity.

Capacity utilization refers to the amount of physical capital available to firms that is in use. For example machinery, office space, factories, computers and telecommunications infrastructure to assist workers in production of goods and services. In the short run it is fixed. As various producers reach capacity, they are likely to begin charging customers high production costs resulting from additional shifts, overtime and other costs related to
increased use of available capital. Adding extra capital would take several years.

In this case, Zimbabwe is operating above medium capacity, actually in the range of 50%-75% capacity and this only means local industry on its own can satisfy demand and this can also build up inflationary pressures. Although the inflationary pressures were being contained by duty free imports, the reintroduction of duty on these products immediately led to the local producers pushing up their prices and as a result the Minister of Finance threatened to scrap away these duties that he had introduced to protect local industries.

3.5.1.4 Commodity prices.

High raw materials and commodity prices are often passed on to the final product.

Coming out of a debilitating recession, Zimbabwe is way behind in terms of technological development. This therefore means that the raw materials used in the industry are very expensive and the technology used in processing those raw materials is also inefficient resulting in high costs of production leading to high prices and creating inflationary pressures.

3.5.1.5 Changes in business inventories.

Rapid growth in demand for goods and services will deplete business inventories. As business increase production to meet additional demand and to rebuild inventories to desired levels, inflationary pressures may build up.

3.5.1.6 Worker productivity gains.

Worker productivity refers to output per worker during a given period of time. As workers gain job experience, knowledge and skills, they become better at their jobs and productivity improves. Brain drain in Zimbabwe has greatly impacted on productivity as those workers who had the skills and experience in industry immigrated to other countries for greener pastures. The scrounge of the AIDS Pandemic has not spared the nation either as the little number that remained is being swept away, thereby greatly constraining the productivity growth of our country. As a result the little that is produced is not produced efficiently and this means it is highly priced.

In an attempt to boost local production, the government has put protectionist policies to protect those industries that are failing to produce at low costs as well as to meet local demand. Inevitably inflationary pressures will rise.
3.5.2 Conditions for non inflationary growth.

As the economy emerges from a recession, unemployed resource (workers, factories, machinery, and other capital goods) are put back to work. Economic growth is characterized by a falling unemployment rate and the absorption of excess capacity. Growth is robust, and the combination of excess capacity and the steady growth in productive capacity keep a lid on price pressures. The situation is one where there is a large gap between actual output and potential output. If output is well below its potential (maximum), there is plenty of excess capacity (or slack) in the economy and producers can easily expand output with the existing productive capacity available. Since there is a surplus of unemployed labour, wage demands remain muted and the utilization of mothballed equipment is cheaper than buying new capital. Importantly, higher supplies easily satisfy the increased demand for goods and services.

In Zimbabwe although the conditions for non inflationary growth will to some extent meet those mentioned above, more is needed to be done to create the right conditions. Even as the economy is operating at medium capacity more capital injection is required to rebuild the infrastructure that was either destroyed or became obsolete during this decade long and promote production orientated firms. There is therefore a great need for capacity building to enable the economy to experience real economic growth.

3.6 The role of productivity in an economy

Productivity is a measure of the efficiency of production. It is a ratio of what is produced to what is required to produce it, that is, a measure of output from a production process per unit of input. At national level productivity growth raises living standards because more real income improves people’s ability to purchase goods and services, enjoy leisure, improve housing and education and contribute to social and environmental progress.

Productivity is also important to companies because it enables them to meet their obligations to workers, shareholders and government through taxes and other statutory obligations and still remain competitive.

According to Wikipedia, “Productivity is not everything, but in the long run it is almost everything”

If productivity is improved consistently the costs of production or unit cost come down drastically and therefore it increases consumer welfare as prices come down.
On the other hand productivity can be increased by increasing working hours, retrenching more workers or making workers work under adverse conditions. If productivity is increased under such conditions, it is not improved but worsened.

3.6.1 The relationship between productivity and economic growth

The main reason productivity has an impact on the economic growth is due to the fact that it improves the stability of business enterprises and the efficiency of the private enterprises and therefore increases the level of investment in the economy thereby increasing the potential output of the economy as a whole in the long term. This enables the economy to grow with less inflation and therefore increasing the economic growth rate.

As well as it increases sustainably the real income of the workforce in general in the long term, it also increases the consumption potential of consumers and therefore increases the aggregate demand and through the multiplier effect produces consistent economic growth.

Productivity improvement has the effect of attracting international capital to the economy and the investment in the economy thereby increasing the potential to produce or lift the production possibility curve to the right.

Ajith Nivard Cabraal, the Governor of Central Bank Of Sri Lanka, in his keynote address at the Annual General Meeting of the International Chamber of Commerce in September, 2008 in Colombo, had this to say about productivity, “For sustained prosperity, productivity is the key; Economists agree that in the long run, productivity growth is the principal means of improving the living standards. The rate of productivity growth influences the economy in important ways, even in the short run, by affecting key variables such as output growth, employment growth and the rate of inflation.”

Cabraal further explained that when natural resource endowment of countries limits further expansion of agriculture and industry, a greater need for improving productivity arises. A high degree of productive capacity utilization is conducive to high productivity of labour and capital.

However this is in direct contrast to the situation prevailing in Zimbabwe where industrial capacity utilization is below fifty percent (Minister of finance in his First Quarter Economic update in April 2011). John Robertson, an economic researcher and analyst paints an even gloomy picture when he says, “The sector’s capacity utilisation is nowhere near fifty percent, and it is around thirty percent.” Also, as revealed in this research study is the fact that most firms in Zimbabwe are services orientated and are operating above medium capacity. However, when it comes to production, most firms are working below capacity.
The greatest beneficiary of a long term productivity growth is the quality of social, physical and technological infrastructure. Valentino Piana (2001) is of the opinion that the rich countries’ GDP soared mainly through productivity increase. He states that countries with a low productivity increase are among the poorest of the planet. Wide productivity differentials in the world are the main explanation of dispersion of per capita income.

3.6.2 Constraints of Productivity in an Economy

In developing countries, there are two types of economies which are generally functioning. These economies are somewhat unrelated to each other. One economy is the market economy and the other is a traditional non market or subsistence market. The occurrence of dualism stands in the way of optimum utilization of resources. Therefore it is an obstacle to economic growth.

3.6.2.1 Inefficiencies within the micro economy

When developing economies remain closed to competition, when they are dominated by local monopolies or when production is in the hands of the state, prices might not reflect the marginal cost of production. Opening up the economy to free trade and privatization of industry may promote a more competitive environment, and decrease allocative inefficiency.

3.6.2.2 Imbalances in the structure of the economy

This arises when too much resource are allocated to sectors with little growth potential. From the discussion above it is clear that the productivity of the Zimbabwean economy is in limbo and we discuss the factors that are constraining it.

3.6.2.3 Lack of adequate capital

Most Zimbabwean companies are facing a crippling working capital shortage. This has been worsened by the liquidity challenges facing the economy. Even banks which are traditionally the lubricant of the economy are also not spared the liquidity challenges. The chairman of
FBC Holdings, Mr Herbert Nkala had this to say in his statement for the year ended December, 2009, “The financial sector has been adversely affected by inadequate liquidity in the market exacerbated by the absence of the lender of last resort and the lack of a functional interbank market. As a result, lending has been curtailed as banks sought to preserve liquidity by adopting conservative loan to deposit ratios. “From 2009, the situation seems to continue unabated as witnessed by the statement from the Chairman of Caps Holdings, Mr F C Mtandah, in his half year results for the period ended 30 June, 2011, where he highlighted that liquidity challenges persisted from the previous year and “…..interests rates remained unviable at an average of 23 percent per annum resulting in the appetite to borrow being lost which in turn worsened the existing working capital gap.”

The capital that is required to fuel industry could also have been facilitated by banks through their intermediation role. However this is not the case because there are very little or no savings that can be channelled to industry and commerce. Depositors are just using banks as conduits to facilitate their transactions on lee and as result banks are also levying those transactions heavy charges which even worsens the already unfavourable situation.

Obviously this lack of working capital will affect productivity of the companies, thereby dampening the industrial as well as the agricultural and mining output. Since the whole economy had collapsed during the hyperinflationary period, the economy needs more capital injection to boost the production capacity. Also banks are only lending short term and at prohibitive interest rates and this makes it almost impossible to finance the purchase of capital equipment under such conditions. This therefore means that the production capacity remains constrained.

### 3.6.2.4 Poor governance and corruption

The hyperinflationary period that we are coming from has completely swiped the little vestiges of the morale fibre that we still had, as corruption, shady deals and shortcuts within the corridors of government and private sector became the new culture. This culture seems to be now deeply imbedded in most institutions and it greatly constrains any growth in productivity. Surely the nation needs some heavy doses of its old upright morals that made it the jewel of Africa by then to disentangle it from this cancerous culture that is stifling productivity.

### 3.6.2.5 Political Instability

Political instability also has major impact on productivity as it completely discourages investment in productivity enhancing equipment. Even labour productivity is compromised as workers will not be comfortable come to work. It is also a recipe for capital flight as investors
will divest to other stable destinations. Once investors start withdrawing their capital then obviously there will not be much production. Foreign direct investment is also negatively affected by political instability and FDI is one of the sources of capital that is paramount for productivity growth.

**3.6.2.6 Productive Inefficiency**

Producers in less developed countries may not be able to produce at the lowest possible average cost. This may be because of the failure to apply technology to production or because of the inability to achieve economies of scale. Opening up the economy to free trade may help reduce this type of inefficiency and encourage technology transfer.

**3.6.2.7 Regulatory constraints**

Labour regulations also affect productivity growth in that the government can put in place legislation that discourages investment in productivity enhancing machinery. The current Indigenization bill in Zimbabwe is scaring away investors. The way the bill is being pushed is a cause for concern as there is already a stamped in some political circles by politicians and those who are politically connected to get some shares of blue chip companies for a song. Surely this does not auger well to the investors as their property rights are completely disregard. This is happening at the time when the country is really thirsty for foreign direct investment as that is the only feasible way through which Zimbabwean companies can restore productivity. John Robertson summarized the current situation prevailing in Zimbabwe as follows, “The government’s indigenization policy for instance is scaring away potential investors for its lack of clarity 24śś as it is widely viewed24śś as political, which has also led to some suiting investors putting on hold expansion plans for their businesses.”

**3.6.2.8 Infrastructural Deficiencies**

Lack of a well developed infrastructure also negatively affects productivity in that it interferes with production in various sectors of the economy. For example the poor road network in Zimbabwe greatly inhibits productivity as it is now tedious for companies to move their products by road. Municipalities are failing to provide clean and adequate water to industry and as a result companies are now diverting the hard to find capital to drill some boreholes so that they remain in business. Electricity supply has been so erratic that most companies have again diverted their hard earned capital to secure some generators, which are very expensive to run thereby impinging on economic productivity.

**3.6.2.9 Skills Shortages**

The hyper inflationary period that forced the closure of many companies caused serious brain drain in Zimbabwe. This meant that most skilled and semi skilled workers emigrated to some
economically stable countries thereby leaving the country with very limited skilled and semi skilled labour force. The lack of skilled labour force means that companies are facing serious shortages of qualified personnel to work in their production processes. This may force companies to shelve acquisition of sophisticated machinery if they do not have qualified personnel thereby compromising on productivity. According to the Bureau of Economic Research of South Africa, larger firms suffer more from infrastructure deficiencies and skilled labour shortages and service firms have more serious problems with communication deficiencies.

As Cabraal puts it, the main factor increasing productivity is the availability and quality of capital and labour resources particularly skilled and semi skilled workforce and the flexibility of the labour market.

**Figure 5: Causes of Low Productivity**

It was noted from the research study that most of the firms interviewed strongly agreed that lack of technology and inconsistent government policy were the main factors that contributed to low productivity.

**3.6.3 How Productivity can be improved**

According to Valentino Piana (2001) prolonged structural increase in productivity is the result of many factors which include the following:

3.6.3.1 Capital accumulation through investments – If companies or economic players manage to accumulate capital for future development, it becomes easier to embrace any productivity enhancing technologies that comes on the market. The more the companies that adopt this approach the more the national economy benefits from
increased technology. Automation and computerization will minimize the tasks that must be performed by employees thereby increasing productivity.

3.6.3.2 The long lasting diffusion of new technologies often imported from abroad. Productivity can also be needed if the market players are ready to infuse new technologies in their modus operandi in order to increase productivity.

3.6.3.3 Domestic innovative efforts – Governments can promote innovativeness in their citizenry by putting in place lucrative incentives and even fund those inventions contributes to an increase in productivity. For example the government should prioritize the restructuring and funding of SIRDC as a starting point in the journey towards increased productivity in our economy. The innovative capacity of private and public institutions should be enhanced through incentives.

3.6.3.4 Imitations of organizational and technological modes of production from world class practices. In this local organizations will be benchmarking themselves against world class practices and aim to compete with those considered to be the world leaders in labour and economic productivity.

3.6.3.5 The development of physical infrastructure including efficient transport, energy and telecommunication network. If this aspect is well developed foreign direct investment will flow and local companies would find it easier to increase their output at lowest costs. If electricity is readily available without any interruptions in supply, the roads are well maintained and telecommunication is available at favourable rates, surely nothing could stand in the way of this economy to grow and develop. Honestly these inadequate infrastructures weigh in heavily on production costs of Zimbabwean companies.

3.6.3.6 Increase the level of education competencies. Though there are increased educational levels in Zimbabwe, the educational system however needs to be aligned with the requirements of industry, so that commerce and industry directly benefits from the educational system. Skills relevant to the local industry needs to polished through the educational system putting much emphasis in research and development.

3.6.3.7 Business taxation and regulatory regime also affects productivity. If business is overly regulated, it affects investment in productivity enhancing activities because of the cost regulation. Regulations should instead reward investment in productivity enhancing assets.

3.6.3.8 Encouragement of stronger competition – stronger competition promote the search for productivity improvements and the ability to achieve them, as every company will be
forced implement productivity improving methods for them to survive the competitive environment.

3.7 The Role of financial Institutions in Economic Development.
The financial system is made up of financial markets and financial institutions. In Zimbabwe financial institutions include Reserve Bank of Zimbabwe, Commercial banks, credit unions, insurance companies among others. An efficient financial system is crucial for the growth of the economy Rousseau (2003) cited in Ghatak and Sanchez-Fung (2007) found statistical evidence showing that the development of banking and securities markets have been significant in explaining the economic expansions in countries such Japan, and United States. The major role of the financial system is to distribute capital in the economy. Financial institutions play this important role of channelling scarce financial resources to the sectors of the economy where their returns are highest. According to Hubbard (1994:39), “The financial system provides mechanisms to transfer funds from individuals and groups who saved money to individuals and groups who want to borrow money.” Savers supply funds and borrowers demand money.

The financial institutions pool together small amounts of savings from surplus units into large funds. The bigger funds are then given out as loans to big firms which invest in huge capital equipment.

Ghatak (1995:65) states that, “The use of monetary and credit is regarded as an important way to achieve economic growth.” This has the implication that the Reserve Bank of Zimbabwe has a major role to play in order to promote economic growth. It has to create credit to banks which in turn loan out the money to sectors such as agriculture, mining and manufacturing. The loans will enable firms to invest in plant and machinery. The investment in plant and machinery helps to increase the output of goods and services.

Ghatak (1995) points out that another role of the central bank in a country is to promote integration of the organized and unorganized money markets. The money market in Zimbabwe is made up of the organized and unorganized markets. The organized money market is made up of the Reserve Bank of Zimbabwe, commercial banks and other financial institutions. The unorganized sector is made up of the money lenders and traders. It is believed that the unorganized money market controls a greater proportion of the economy. Money in the unorganized money markets does not enter the formal banking system. Monetary policy is therefore rendered ineffective because of the existence of this money market. It is therefore crucial that the money market be integrated with the organized market.
The integration increases the supply of savings in banks. More funds for investment will therefore be available.

Commercial banks play the role of transforming savings into investments. This is the financial intermediation role. Ghatak (1995) argues that economic growth needs more investment. Investments are financed from savings. One major role of financial intermediaries is to mobilize savings and channel them to deficit units in the economy. Investment is the greatest engine for economic growth. It involves the purchase of goods that are not for immediate use but are meant to produce goods and services. Savings play an important role of financing investment. Commercial banks play the role of attracting money from savers. The money is then used to create credit.

Banks offer three key services. These are risk sharing, liquidity and information. Financing institutions offer many assets. Investors on the money markets can have a diversified portfolio. This helps to reduce risk. Risk reduction helps to attract savings. People are motivated to reduce hoarding of money.

3.7.1 Constraints faced by financial institutions

It was pointed above that the unorganized money market controls a significant proportion of the money market. The unorganized money market does constrain the financial institutions in a number of ways. Ghatak (1995:71) identifies the following characteristics of the unorganized money market.

1. Secrecy about financial dealings
2. Blending of money-lending with different types of economic activities e.g. trading
3. Flexibility of loan operations
4. Personal and informal dealings with customers and
5. Simple or crude system of maintaining accounts.

These characteristics make it easier for the unorganized money market to out compete the organized sector in attracting savings. For example, money lenders offer an interest rate of at least 10% per month which when annualized is much greater than 5% offered by banks.

According to Ghatak (1995:72) the existence of financial dualism has the following effects.

i) It has reduced the size of monetary transactions and perpetuated non-monetary transactions.

ii) It has restricted the growth of banks in rural areas. This in turn has decreased the use of bank credit.
iii) The existence of the unorganized sector has deprived the economy of an array of financial assets with which savings could have been more effectively directed towards investments for realizing a higher rate of economic growth.

iv) The presence of financial dualism has perpetuated some ancient customs like gold hoarding which have prevented the use of available resources for productive investment.

v) The impact of monetary policy has been considerably weakened by the presence of dichotomy in the rural money market.

Another constrain faced by financial institution is lack of confidence in the economy. This deters investors from coming into the country to invest in banks. The globalization of the world economy has also motivated many to hold foreign securities for fear of investing in Zimbabwe where political risk is high. These actions have reduced bank deposits in Zimbabwe. Banks and finance therefore crippled in terms of their credit creation. Banks are also constrained by lower levels of deposits. The low level of salaries in Zimbabwe has greatly reduced the level of deposits. Most funds that are held in banks are funds in transit. Firms may deposit money to fulfil statutory requirements and then withdraw as soon as possible. The financial institutions are therefore unable to advance long-term loans needed to buy capital equipment.

According to research findings, the low levels of savings have tempted banks to survive by charging high fees. This however, deters - would be investors and thereby cause lower levels of savings. Banks therefore have to reduce bank charges in order to attract savings. Banks also need to relax conditions for new customers to open accounts. Some savers have large amounts of money to save but they may not be in a position to meet the requirements. This limits the level of savings in the economy.

4.0 Conclusion and Summary

Zimbabwe is faced with a number of challenges in its pursuit for economic growth. The greatest challenge is how to improve productivity in a non-inflationary environment. Today, the country is more centred on services provision. It is therefore our recommendation, that as an economy, Zimbabwe can carry on with the service orientation but have targeted sectors of the economy that can be productively improved. Amongst such key sectors is Agriculture, SMEs and MFIs.

5.0 Suggestions for further research

5.1 There is need to conduct a study that includes the plight of the rural folk to include their contribution to economic growth as their output is not usually captured.
5.2 In addition, it is also recommended that a research be conducted on the embedded price distortions that dollarization has brought in businesses.

5.3 Also, there is a need to carry out a research on how to develop the mindset of Zimbabwean economic agents, including micro-financing institutions [MFIs], small – to - medium enterprises [SMEs] which are very important to economic development, from being subsistence orientated to being economic agents of development.

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