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ZIMBABWE'S DEBT PROBLEM: LESSONS FOR THE FUTURE

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Abstract

Zimbabwe's debt has been considered unsustainable from within and outside the country. This study sought to establish the causes of such a scenario taking a qualitative approach through the administration of a questionnaire and interview to a purposively sampled respondent pool. The study managed to establish the root causes of un-sustainability of past loans to Zimbabwe. Conditionality in loans from lending institutions has had its fair share of blame in making debt un-sustainable. Droughts which have been a common phenomenon in Sub-Saharan Africa for the past three decades have had their contribution to the debt problem but the study concurred with Jones(2011)'s findings when it comes to sustainable means of funding droughts. Post independence, some debt which has burdened Zimbabwe was considered unjustified and odious. With supportive policies, foreign direct investment was inter-alia found to be a form of bailout capable of sustaining itself in the long run whilst addressing other economic fundamentals like employment.

Keywords – *Bailouts, debt sustainability, economic development, loans.*

Introduction

Zimbabwe's external debt is high and largely in arrears, cutting off the country from access to most external financing sources (UNDP 2012, p1). In particular, Zimbabwe remains incapable of accessing IMF resources because of its continued arrears to the Fund (Gono 2012, p2). A strong track record of maintaining macroeconomic stability and implementing reforms, together with a comprehensive arrears clearance strategy supported by development partners, will be essential for resolving Zimbabwe's large debt overhang (IMF Press Release 13/174).Such debt overhang is said to have emanated from loans given to Zimbabwe by both multilateral and bilateral institutions which were not invested in particular projects but were used to meet repayments of older debt (Jones 2011, p1). There are, however characteristics that must be visible on any form of debt to Zimbabwe that will guarantee debt sustainability. There is need, however to unravel the ills in the previous loans that Zimbabwe should not attempt to go back to if at all debt sustainability is to be achieved in future.

Background of the Study

Shaoul (1999) highlights the decision by the IMF to provide a standby loan of US$193 million which was meant to enable Zimbabwe to resume its repayments to international creditors. This was a decision reached at by the IMF in 1999 owing to the arrears in which Zimbabwe was in but the '*standby'* loans were meant for the repayment of previous loans. Structural adjustments loans given to Zimbabwe in the early 1990's were also used to repay debts that had been acquired in the 1980's (Jones 2011, p 4). Such has been the characteristic of some loans from multilateral institutions to Zimbabwe, which are not underpinned by any repayment model in future. Holding other variables constant, the characteristics of the loans provided to Zimbabwe have had their fair share in leading to an unsustainable debt situation. In as much as Zimbabwe is seeking a debt solution , once it has access to the international lenders it must also have a model debt package which will not lead to the same debt overhang.

The Zimbabwe government in 2009 was of the opinion that to address the priority areas which guarantee economic growth, an amount in excess of US$5-billion was required underpinned by consistent implementation of respective policies and other measures(STERP 2009,p 20). This was a requirement put forth by the Ministry of Finance without taking cognizance of the current debt overhang that has been considered an impediment to such funding. The RBZ estimated Zimbabwe's debt overhang to be in excess of US$8-billion and regards this as a serious developmental constraint since the turn of the century (Gono 2012, p 2). The UNDP Zimbabwe Brown Bag Dialogue series (2012) pointed out that Zimbabwe needs US$15-billion to cover the resource gap in the implementation of the Medium Term Plan which has to be in full force between 2011 and 2015. The plan no matter how good cannot be achieved without a comprehensive debt relief (Ibid).

Despite the variations in the amounts Zimbabwe may require to get the economy working, as noted above depending on the source of the data, the underlying fact is funds are required anyway to kick-start the economy and avoid overdependence on imports which do consume the cash that may be required to service foreign debt.

Despite both the STERP and MTP having had pointed out the need for prescribed funding for both to succeed, Zimbabwe has not received such funding to bring into force both plans. This is despite the fact the period for the implementation of STERP was up to 2010 and MTP covers 2011 to 2015. If Zimbabwe is to receive any bailout, there are characteristics which must be embedded which will ensure debt sustainability and avoid the known debt trap. There are loans which are best for Zimbabwe when not acquired.

Debt to Zimbabwe dates primarily from loans made in the 1980s and 1990s by private lenders such as banks; foreign governments such as France, Germany and the UK; and multilateral institutions like the World Bank, African

Development Bank and International Monetary Fund (IMF) (Jones 2011, p 4). The Zimbabwean government has been in default on most of its debt owed to the rest of the world, currently estimated to be around US$7 billion (ibid).

Dating as far back as 2009 debates have raged in economic circles on whether Zimbabwe should be accorded an HIPC status or not (ZDDI 2010, p1). The HIPC initiative though bearing evidence of having worked in such countries like Uganda, Mozambique and Burundi in Africa, has been briefly set aside in Zimbabwe with efforts being directed towards the Angola model which involves mortgaging the country's natural resources to emerging lenders which do not exert policy conditions on the country (ERODAD 2009).

Problem Statement

Bailout packages and loans given to Zimbabwe have characteristics that do not guarantee debt sustainability (Jones 2011). Loans in the past have been given for purposes of servicing existing debt and at times not put to any productive use which guarantees debt sustainability(ibid).Since Zimbabwe is in need of funding to address a number of macro-economic imbalances, it definitely will require funding that will not lead to a similar debt trap as is currently holding. Enhancing debt sustainability at debt acquisition point will be the main focus of this research.

Scope of the Study

Whilst drawing lessons from other countries that have received either bilateral or multilateral funding, Zimbabwe has been the main focus of the research. Since the affect of debt are cumulative, data has been used of debt from 1980 to first half 2013. Both bilateral and multilateral sources of financing have been considered in this research because the effects of defaulting on either are detrimental to the development of the debtor country.

Significance of the Study

It is the hope of the researcher that Zimbabwe's ministries of finance and economic planning and investment might find this research useful since they are referral points in debt acquisitions. This research will highlight what constitutes a bailout that is counter development. A lot of opportunities have been missed by Zimbabwe as a result of the current debt stock and overhang. This research project also aims to be a referral point for academics seeking answers as to why selected developing countries of their interest may be or may be in the process of getting into debt crisis. Future research by academics and practitioners is also expected to be ignited by the specific findings and recommendations from this research.

Limitations of the Study

Since the research will focus on future bailouts for Zimbabwe, and recommending the areas to be considered key to the determination of debt sustainability, some already signed loans or bailout agreements will be tightly guarded for sovereign security reasons. The researcher however will rely on officially published material on such data as and when relevant to this research.

Review of Literature

Gross external debt, at any given time, is the outstanding amount of those current, and not contingent liabilities owed to non-residents by residents of an economy that require payment(s) either of principal and/or interest by the debtor at some point(s) in the future (OECD 2000)[1]. This is in line with how the World Bank (1988) defines the same concept as the amount, at any given time, of disbursed and outstanding contractual liabilities of residents of a country to non-residents to repay principal, with or without interest, or to pay interest, with or without principal (ibid, p19).

Seyal (1988) regards it as very difficult if not impossible for a country to finance all of its development activities using internally generated funds. As such, an underscore is made on the need to borrow from either internal or external sources. Regard is given towards this view as normal within certain limits but concern is raised by the same author on the extraordinary debt growth in all countries generally, and less developed in particular (ibid).

Dessbonet and Weitzenblum (2011), reveal the temptation by states to take on higher levels of debt as emanating from the need for short-run gains. These gains may come in the form of temporary reduction in the income tax rate, which in turn stimulates labor supply and generates an overshooting of interest rate. They allude to the fact that welfare gains are likely to be felt even when debt levels are way beyond the long run optimal levels (Ibid). Dessbonet and Weitzenblum (2011) view is in sharp contrast with Keynes (1936), argument that governments should solve problems in the short-run rather than waiting for market forces to do it in the long run.

Despite there being benefits that accrue to countries acquiring debt (Sinn 2008), no such benefits do accrue to countries with unsustainable debt (IMF 2012). Espejo and Unigovskaya (2008) do give an outline of the benefits that accrue to African countries as a result of debt relief.

Investopedia defines odious debt as money borrowed by one country from another country and then misappropriated by national rulers. A nation's debt becomes odious debt when government leaders use borrowed funds in ways that do not benefit or even oppress citizens[2]. Some legal scholars argue that successor governments should not be held accountable for odious debt incurred by earlier regimes, but there is no consensus on how odious debt should actually be treated (ibid). In practice, countries often end up repaying it to uphold their ability to borrow at favourable interest rates. Sack (1929) as quoted by Howse (2007) regards odious debts as not an obligation for the nation but as the regime's debt and a personal

[1] External Debt Statistics: Guide for Compilers and Users (Draft), IMF, Washington DC, March 2000, Appendix III, Glossary of Terms.

[2] http://www.investopedia.com/terms/o/odious-debt.asp

debt of the power that has incurred it. Sack divided odious debts into several categories: war debts, subjugated or imposed debts, and regime debts (Ibid).

Killick (1998) define debt conditionality as actions, or promises of actions, made by recipient governments only at the insistence of aid providers; measures that would not otherwise be undertaken, or not within the time frame desired by the providers. The IMF justifies conditionality based on the requirements of the Articles of Agreement that the IMF must only provide 'temporary 'assistance under 'adequate safeguards' (Bird 2009). Conditionality may also be regarded as a means of ensuring that countries are able to repay the money they borrow (ibid). It is therefore intended to hamper moral hazard (Kanbur 2000). Conditionality thus seeks to lock governments into programmes of economic reform (ibid). In light of this, conditionality may also signal commitment to reform and therefore may transmit such to the capital markets and thus opening up other capital flows to a country that accepts such conditionality (Bayai and Nyangara 2013). The IMF also stresses that conditionality provides a guarantee to users that, provided they meet agreed performance criteria, future tranches of a loan will be forthcoming (Bird 2009).

Saach (1989) highlights without any hesitation that the IMF and the World Bank do offer high conditionality lending to countries in debt stricken countries (Saach 1989, p255).The role such lending plays is considered key as has been observed from the same study since 1982, but the results of the same lending have been condemned for not delivering the promised results (ibid). Saach and Warner (1995) in a follow up paper to Saach (1989) emphasise the burden of geography and poor policies on aid effectiveness. Burnside and Dollar (1997) find that when aid flows into good policy environments it helps growth, but how is this achievable given that conditions on the aid may not be in the best interest of the receiving countries?

It is also startling to note that Burnside and Dollar (1997) also find that aid does not generally flow to countries with good policy environments. As if in contradiction with their findings, Burnside and Dollar (1997) also discover using developing country data that aid does not induce good policy environments to emerge at all. Too firm a finding these seem since if aid finds its way to a good policy environment, it will not enable such an environment to emerge at all. But since aid seldom finds its way to such environments, the onus is on the debt receiving countries to consider Kanbur's (2000) recommendations which are also discussed below.

Kanbur (2000) concurs with Saach (1989) but takes the issue of conditionality further by diagnosing the dysfunctional nature of aid and the debt regime in Africa. Aid effectiveness in Africa is, according to his findings hampered by the current system which is characterized by aid dependence. Such dependence may only be eliminated through institutional reforms which will pave way for lower volumes of aid accruing to Africa (Kanbur 2000).

In as much as conditionality can be instituted by multilateral institutions, bilateral creditors can also offer loans with conditionality attached. The then Thatcher administration in the early 1980's supplied credit to the Zimbabwean government to the tune of US$140million tied to the use of British companies when making use of those funds (Jones 2011, p8). This practice, however, of tying aid to the use of British countries was made illegal in the UK in 2002(ibid).

Objectives of the Study

The objectives of this study have been premised on the need to :

- Determine the nature of loans and bailout packages given to developing countries by both bilateral and multilateral institutions
- Examine how debt crisis in developing countries have been addressed.
- Determine considerations put forth for bilateral bailouts to work.
- Assess how the various strategies ensure sustainability in servicing the loans

Methodology

Questionnaire and structured interview method were used to extract the primary data from the respondents selected based on purposive sampling. The study was conducted on a sample of 100 targeted respondents for the questionnaire, with 71 having responded back and 10 targeted respondents for the interview with 8- having been interviewed successfully. Secondary data was also collected from various journals, books, magazines, newspapers and reports prepared by researchers, etc.

Questionnaire Response rate

	NBI	Banks	Academics	Economic Research Units	Economists	OVERALL
Targeted	10	15	25	30	20	100
Responses	6	10	18	24	13	71
Success	60%	67%	72%	80%	65%	71%

Fig 1

Data Analysis

The Statistical Package for Social Sciences (SPSS) was used to get a general view of the preferred model bailout package for Zimbabwe. Results from the analysis have however been contrasted with results contained in the literature. It is from such contrasting that the conclusions and recommendation have been drawn. Interpretations will however have to be drawn from the data presented and relevant literature compared with obtained results.

Research Findings and Suggestions

The research findings and suggestions are based on extractions from primary data collected compressed for analysis using SPSS

a) Even though debt has a possibility of benefiting a nation, Zimbabwe's debt has done the reverse. Access to International financial institutions is being hampered by the current unsustainable debt stock

b) Acquisition of debt must not be motivated by the mere availability of the debt but by strict due diligence to the finer details of the debt covenants. The pricing of the debt has been highlighted to be misaligned to the return expected from the projects which were being funded thus creating a definite unsustainable future debt scenario

c) Debt must be channeled to productive purposes other than consumptive purposes. Catastrophic escapades in history like droughts must make use of grants even though these are subject to availability. Debt should have rather been used for such projects as dam construction which will counter the effects of erratic rainfall in Sub Saharan Africa

d) Conditionality in bilateral loan agreements has been seen as one precursor for debt sustainability. Countries offering loans to Zimbabwe have in the past received the loan proceeds for provision of services to the borrowing country. Major staff and raw materials for construction of selected structures in Zimbabwe have been provided by countries which would have funded Zimbabwe for such projects, thus effectively leading to questions to the retention of such funds in the receiving country.

e) There is need for transparency in debt acquisition and use. The fact that there is need for reconciliation on outstanding debt figures has been highlighted as an indicator lack of transparency in issues related to debt.

f) There is need to establish the odiousness of the debt inherited by Zimbabwe from Rhodesia. Since the inherited debt is suggested to have been acquired during the period when Rhodesia was under sanctions for purposes of funding Rhodesia's armed struggle, the inheritance of such debt should have been put under test even if the message during the time of independence was that of reconciliation.

g) War should not be financed using debt since this will be evidently exposing future generations to unjust debt burdens.

h) Ceteris paribus, Zimbabwe needs a comprehensive debt relief from its creditors. Creditors should also reward debtors who have either not defaulted or are in arrears of their debt.

i) Bailing out Zimbabwe for sustainability maintenance must be through foreign direct investment in manufacturing sector since raw materials leading to economic growth in other countries are being obtained from Zimbabwe.

j) Real GDP-indexed loans may be considered as a possible financing avenue for Zimbabwe since they introduce greater state contingency in sovereign debt contracts. Such loans may help stabilize the debt-to-GDP ratio, reduce the likelihood of debt crises and sovereign defaults and limit the pro-cyclicality of fiscal policy (see e.g. Borensztein and Mauro, 2004; Griffith-Jones and Sharma, 2006)

k) Loan contracts must be negotiated which are indexed to dollar value of exports other than the use of country grouping criteria (like Low Income Country). This however will depend on the effective application of the loan to the project for which it has been acquired and the success of such thereof.

l) Zimbabwe's public debt has also negatively affected private investment as also noted by Bayai and Nyangara (2013). If the debt issue is not addressed it has a negative effect on private investment which is benefiting other countries with sustainable debt scenarios.

Scope for Further Research

In light of the finding of this research project, there is need to investigate whether a debt tipping point for Zimbabwe may be established. Such a point will enlighten policy makers when debt will be getting unsustainable in the national books. Research may also centre on how Angola resolved its debt problem with special emphasis on drawing lessons for Zimbabwe

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