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ANALYSIS OF ADDITIONAL ECONOMIC MEASURES RECENTLY INSTITUTED BY TREASURY ON 29 MAY 2023

The Zimbabwe dollar (ZWL) is massively deteriorating against the US dollar particularly in the parallel markets since the beginning of 2023. The resultant galloping inflation which is now independently estimated above 700% has prompted policy response from authorities. The first set of economic measures to stabilize the economy was introduced in early May 2023[1]. And on the 29th of May 2023, Treasury introduced another set of measures to stabilize the economy. These newest measures are analysed below.

1. Promotion of Use of ZWL

In a bid to promote the use of the ZWL in the economy, the Treasury announced that all Government Agencies including Parastatals will now substantially collect their fees in local currency, payments to ZESA by non-exporters will be made in ZWLs, and all customs duty to be payable in ZWLs except for designated or luxury goods and circumstances where the importer opts to pay in foreign currency (forex). *The policy stance is commendable as it signals the government's confidence in its own currency and helps shore up demand for ZWLs. As demand increases, the ZWL will regain and sustain its value against the US dollar (USD). By increasing tax revenue collected in local currency, demand for ZWLs will be created as people liquidate USD holdings to pay their dues to the taxman. All things being equal, this measure should help save the ZWL which at the moment is on the verge of total collapse and market rejection. In May 2023 alone, the local unit erased nearly 40% of its average parallel (alternative) market value as it slid from ZWL/USD 2200 in April to ZWL/USD 3600. Since the start of 2023 to date (YTD), it has lost a staggering 75% of its value in alternative markets which is only two (2) percentage points lower than a 77% decline registered in the entire 2022. The numbers show that the ZWL is failing to perform its store of value function. As a result, economic agents are dumping ZWLs in the market as soon as they earn them.*

However, for durable ZWL stability to be realized, the policy must be fully implemented and buttressed by other measures inter alia promotion of fiscal transparency across all tiers of government, sustainable (within limits) fiscal spending, tight monetary policy, efficient & effective public service delivery, and a flexible exchange rate regime which is key in attaining uniform market exchange rate.

2. Sterilization of Excess Liquidity

Treasury will continue to sterilize excess liquidity already injected into the economy through issuances of Treasury Bills (TBs) whilst RBZ will continue to sterilize through appropriate monetary policy tools. *Sterilization is an action taken by authorities to counter the effects on the money supply caused by their interventions in the foreign exchange markets. This policy move is key as it seeks to address the root cause of ongoing ZWL instability and pricing madness – excessive ZWL liquidity growth in the market.*

1. https://zimcodd.org/?sdm_process_download=1&download_id=6429

For instance, the latest RBZ statistics show the ZWL component of broad money (M3)[2] *spiking unsustainably by 12.8% in March 2023 to ZWL1.32 trillion from ZWL1.17 trillion in February 2023. From a year-on-year (YoY) basis, this ZWL component of M3 grew by a staggering 324% from ZWL312.22 billion recorded in February 2022. However, it remains to be seen if there will be adequate political will, especially in an election year to cut on burgeoning fiscal spending. Also, because of limited due diligence in public procurement processes & procedures, Treasury is making unjustifiably huge ZWL payments to government suppliers and contractors who in turn offload these balances in the parallel markets. Fiscal spending is also rising as government supports winter wheat farming, attempts to cushion public servants, engages in unproductive election-linked expenditures, and anchors the 2023 Agric marketing year funding grain purchases from farmers by the Grain Marketing Board (GMB). If some of these expenditures are not cut, liquidity will remain high thus exerting pressure on the exchange rate to depreciate.*

3. Monetary Policy Tightening

Treasury announced that RBZ will tighten monetary policy in order to reduce lending and hence money creation by banks. This policy may include hiking of RBZ benchmark policy rate – a short-term reference rate at which commercial banks can borrow money from their central bank. *Considering the status quo of increased liquidity in the market, hiking the Bank's policy rate will help discourage speculative borrowing by banks as well as other demanders of loanable funds. For this policy to yield results, there is also a need for tight monetary targeting by RBZ to ensure that the rate at which the money supply is growing is in tandem with the rate of growth of economic activity in the real sector.*

Also, Treasury announced that it will now fund the ZWL component of 25% foreign currency (forex) surrendered by exporters and will now collect all forex surrendered to service foreign currency loans assumed from RBZ. *This policy move will help reduce quasi-fiscal operations (QFOs) by RBZ thus clamping money supply growth. Before, the RBZ was unsustainably printing ZWLs to purchase forex from tobacco farmers and exporters. For instance, April 2023 merchandise exports stood at US$555 million and a quarter (US$138.8 million) of these exports were ceded to RBZ at the official rate (US$1: ZWL1047.44) as per the existing export surrender requirements. This means that roughly ZWL145.3 billion was printed and injected into the system in April 2023 through the purchase of USDs from exporters alone. With the value of exports expected to remain elevated throughout 2023, money printing to buy forex is unsustainable and fuel market instability.*

However, it is going to be a daunting task for Treasury which is already facing a very limited fiscal space to raise ZWLs to buy forex surrendered by exporters. The funds were not budgeted for in the 2023 budget and the TBs issued are discouraging as they usually carry a coupon rate that is way below inflation currently estimated independently at above 700%. To eliminate this and its other associated risks, the export surrender requirements must be eliminated.

2. Broad money is total money in circulation in the economy

4.Finetuning Exchange Rate

Treasury announced that weekly auctions will be limited to a maximum envelope of US$5 million and that all winning bids shall be paid within 24 hours of award. This, coupled with the pre-announcement of the available weekly auction envelope will help fast-track convergence of the interbank and auction exchange rates as it increases bidding competitiveness as well as eliminate opportunities for insider trading. *While this may help improve the efficiency of the auction market, it remains the public's view that this system must be completely disbanded as it is breeding exchange rate multiplicity and rent-seeking behaviors. Also, the continued use of a priority list on the auction exerts moral hazard thus influencing how people put their bids.*

More so, Treasury announced that all exporters' forex proceeds that remain unutilized after 90 days will be liquidated onto the interbank market. Of this, authorities are trying to reduce the opportunity cost of idle forex balances. In theory, this will increase business investment, production, and productivity. However, forced liquidation of forex proceeds will likely promote externalization. As such, instead of forcing the liquidation of export forex proceeds after 90 days, authorities should disband the auction system and fully liberalize the interbank market. To increase market efficiency including pricing of the ZWL, all market actors – public and private - must at least be subjected to the same market conditions.

5. Assumption of RBZ Debts

Treasury will assume all foreign currency debts from RBZ on 1 June 2023 and create a debt redemption fund to service other external liabilities in line with the arrears clearance program. These will be funded through new levies and other resource mobilization initiatives. Also, going forward all public foreign currency debt will be contracted solely by the Treasury. *While limiting state borrowing powers to Treasury is a welcome development that will positively contribute toward debt sustainability, the bypassing of Parliament in this process makes the debt assumption unconstitutional. Presently there is no Act of Parliament legalizing the Treasury to assume all RBZ external debts. The RBZ Debt Assumption Act (2015) is not in perpetuity and sets clear time limit of 31 December 2008 for debts assumed. It is also standard practice to conduct comprehensive debt audit prior to debt assumptions to ascertain and eliminate the possibility of assuming odious and illegitimate debt. The wisdom of this policy move is questionable particularly in the face of ongoing debt resolution and arrears clearance processes.*

6. Additional Taxes

The Treasury will introduce a 1% tax on all foreign payments. The policy move seeks to reduce Zimbabwe's spending on foreign goods and services by making imports a bit expensive. *It will discourage non-essential imports, save direly needed foreign currency, and increase government tax revenue which is key in supporting stable, sustainable, and inclusive socio-economic development. However, there is a need for some exemptions as this policy stance risks making crucial imports like industrial raw materials unaffordable thus posing a great danger to the already ailing local industry.*

Also, 2% USD cash withdrawal tax will be maintained. This policy move will also help reduce US demand by making cash withdrawal expensive. *While this may help to clamp ZWL decline, Treasury must increase the threshold to cushion low-income earners.*

7. Gold Traceability System

Through Fidelity Gold Refinery (FGR), the government will introduce a system to manage the traceability of gold from its origin, both from commercial and small-scale producers. *This is an important move because gold production tracking & monitoring will minimize the chances of gold smuggling and illicit trading. Also, traceability measures help in curbing criminality as information such as the exact source of gold, holder of gold buying license, and amount of taxes paid on gold exports can be collected and analyzed. The prevailing rampant illicit flows must be reduced as they are militating against the accumulation of gold reserves which are crucial in supporting the value of both the ZWL and gold e-cards recently introduced by RBZ.*