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Zimbabwe Economic Policy Dialogue
Policy Notes for the New Government - 2013

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EXECUTIVE SUMMARY

A. INTRODUCTION

1. In past four years, the World Bank, in close cooperation with the Government of Zimbabwe, and the support of international partners - has carried out a number of studies and technical assistance activities in key areas of the socio-economic recovery. In line with Bank’s Africa Strategy of fostering Africa’s economic transformation and poverty reduction, the overall goal of these studies has been to support broad-based development of Zimbabwe by facilitating evidence-based debate and policy-making. Studies have been striving to generate data, provide independent analysis and foster learning from other countries’ experiences. All reports are available.

2. As a new government for 2013-2018 is about to take function, sectoral teams at the World Bank have distilled key analysis from those studies, and prepared the attached short policy notes. The policy notes attempt to summarize in a short space the main findings, challenges, constraints, and lay out policy options.

3. Zimbabwe's economic past, which was underpinned by historically solid underlying economic fundamentals such as a large, educated workforce, a strong propensity to save, and a relatively diversified economic base suggests that its current economic challenges need not preclude a positive future. While the past decade of hyperinflation and weak economic management has undoubtedly eroded a significant share of Zimbabwe's physical and human capital, these can be rebuilt with the combination of sound economic policy and proper incentives to private sector investors, both domestic and foreign. It is therefore imperative that, however policymakers choose to proceed with regard to the future direction of the economy, they deliver well-articulated, credible, and stable economic policies. Such policies will enable and unleash the creative energies and entrepreneurial spirit of the private sector, the one that has delivered so often in the past.

4. Policies in 2009-2013 have led to an initial successful stabilization of the Zimbabwean economy, which has recovered growth after a decade-long contraction. Despite a vigorous initial rebound, growth is fading. The Zimbabwean economy has not yet entered a phase of sustained economic transformation and broad-based socio-economic recovery. At the same time poverty remains widespread, with 70 percent of Zimbabwean living under the national poverty lines, and 22.5 percent (2.8 million people) in extreme poverty. Policies over 2013-2018 will be critical in defining Zimbabwe’s path to development and shared-prosperity, and stopping the decline in human development indicators (education and health) in order to re-establish Zimbabwe as a leader in Africa.
5. The attached policy notes highlights the breadth and complexity of challenges in fostering long-term development. Addressing these challenges is a long haul task that will require a good sense of overarching priorities, as well as strong commitment to long-term objectives and policy consistency.

6. Zimbabwe’s prospects for recovery and long-term development hinges on addressing three main challenges:
   1. Fostering Broad-based Economic Transformation
   2. Eradicate Extreme Poverty and Rebuild Human Capital

B. PRIORITIES FOR FOSTERING ECONOMIC TRANSFORMATION

7. A strategy for economic transformation will require revitalizing private sector’s confidence and investment through removal of anti-investment biases, including clarification of the implementation of the indigenization program. This should be tackled as a priority. Strengthening of the resilience and efficiency of the financial intermediation role of the financial sector should be pursued with great vigor.

8. The mining sector presents a strong potential for response to stronger policies, as investment and production levels from known deposits is still way below potential. However, vigorous growth is unlikely to resume without improvements across all aspects of mining sector policies. A sustainable diamonds policy aiming at leveraging diamonds for a broad-based recovery should be developed. In order to insure that the mining has a positive impact on the indigenous development, improvement of policies around the mining sector should also include linking use of mining sector rents to foster human development, infrastructure development, and creation of linkages with other sectors of the economy, following mineral-led development policies as in Chile, Malaysia and Indonesia.

9. The agricultural sector presents a strong potential for increased supply-response provided, however, that the conditions are reunited. Yields in staples are still below historical levels, and sustained medium-term growth will difficult to achieve without improving overall incentives and conditions in the agricultural sector (in particular, productivity growth, water management and irrigation, marketing arrangement, and enhance land security). The quality of policies in the new agricultural sector and mineral sector will be key determinants of growth over the 2013-2018 period.

10. Finally, the socio-economic recovery will not pick up steam without improved financing and access to public services and strong public management systems. Lack of policy consistency would likely undermine positive efforts.
C. ERADICATING EXTREME POVERTY AND BUILDING HUMAN CAPITAL

11. The decade-long economic crisis caused widespread poverty and decline across all dimensions of human development. The 2009 stabilization has had an immediate positive impact on human development, but data still highlight widespread vulnerability, and delayed recovery of delivery of basic services. There is a widening gap in access to services, while a strong rural-urban divide has developed. In rural areas, 84 percent of the population is below the national poverty line. The maternal mortality ratio is one of the highest in the region. There are approximately one million orphans. Infant mortality (80 per 1000), low immunization (83 percent) and malnutrition (32 percent stunting among children under 5) represent continued threats to children. Every year, 4,800 children under 5 die of diarrhea. There are significant barriers to education. Underemployment and low agricultural productivity contribute to poverty in rural areas. In the upcoming lean season, almost one in five people living in rural areas will not be able to meet their basic food requirements. Eighty-four percent of employment is in the informal sector.

12. The overall Human Development Indicator value highlights how human development was arrested in mid-1980s, and how a protracted stagnation first, and the 2000-2008 crisis, led to a progressive loss of ground in international comparison. At the same time, the HIV/AIDS had a devastating impact on health outcomes (maternal mortality, adult mortality, and infant mortality) and on human resources in the country. There is the need to jumpstart the process of accumulation of Zimbabwe’s human capital again.

13. Re-building Zimbabwe's Human Capital and returning the country to its rightful position as an Africa leader in human development will not be easy especially given the continued widespread poverty. The attached Policy Notes for Education, Health and Social Protection sectors, developed in partnership with the National Ministries, provide a feasible road map for this critical journey. While each Note highlights sector specific policy options, three theme provide an overall way forward: (i) reversing inequality in budget allocations by a strong and persistent focus on the needs of the poor and vulnerable reflected in prioritized allocations for high quality education and health services as well as well targeted safety net functions; (ii) improving allocative efficiency of social sectors spending by strategically prioritizing programs to minimize fragmentation and ensure full funding of priorities; and (iii) strengthening technical efficiency in the three sectors by ensuring non-wage inputs are fully funded.
14. Reversing the decline in human capital will also require actions in other related sectors: (i) improvements in the agricultural sector for achieving food self-sufficiency, and reducing poverty in rural areas; (ii) job creation; and (iii) linking revenues from the mining sector to investments in human capital.

D. RECOVERING ACCESS TO INTERNATIONAL FINANCIAL MARKETS

15. Zimbabwe’s anticipated infrastructure investment patterns from until 2030 will be substantially higher than comparable economies. Infrastructural investment needs in Zimbabwe across the four major infrastructure subsectors, will total US$40 billion. Such a long-term strategy cannot be pursued without re-gaining, in the medium-term, access to international financial markets. Such a strategy should rest on both short term and medium term objectives, to be pursued with vigor and high level of consistency.

16. In 2011, Zimbabwe adopted the Zimbabwe Accelerated Arrears Clearance Debt and Development Strategy (ZAADDs), which aims at resolving arrears with bilateral creditors and international financial institutions. The country should build a track record of sustainable macro-economic policies as central priority, and engage with creditors (Paris Club, International Financial Institutions) in view of agreeing on steps to address existing arrears.

17. The strong increase in aggregate demand, and current account deficits, over the 2009-2013 period, have been financed by external saving, mostly in the form of short-term capital inflows. Foreign Direct Investment (FDI) has remained extremely limited, amounting to less than 10 percent of the total inflows. Strengthening of countries internal policies and domestic financial markets appears to be a necessary pre-condition for improving countries’ capacity to successfully absorb more capital flows. Accordingly, a sustainable strategy will require policies in support to macro-economic stability, increasing investors’ confidence, and encouraging allocation of capital to long-term investment.
DIAGNOSTIC

The Zimbabwean economy remains highly diversified in comparison with other African economies, with a broad-based potential for recovery in all sectors, from mining to agriculture, manufacturing and services. However, growth has been slowing down, and prospects for sustained recovery are uncertain, as both short-term factors and unresolved long-term legacies are hampering a recovery. Future growth will depend on addressing existing vulnerabilities, overcoming the long-term legacies of the decade-long crisis, and entering sustained structural transformation. Failure to address vulnerabilities and overcoming long-term legacies will result in sluggish growth, despite the broad-based potential of the Zimbabwean economy.

Four years into the recovery, the effects of a decade-long crisis are still evident: socio-economic decay, increased vulnerability of the agricultural sector, growth of informality, decay of key infrastructure, poor integration with the global economy, brain-drain, de-industrialization, and persistent uncertainty over property rights. Moreover, Zimbabwe has not yet overcome the long-run negative trends that were evident prior to the decade-long crisis: stagnation of the process of structural transformation, loss of competitiveness of the manufacturing sector, arrested human development, short-termism of institutions, and political tensions.

Despite encouraging results in stabilizing the macroeconomic and fiscal framework, the outcome of recent economic policies has been mixed: (i) rapid growth in the wage-bill has led to continued underfunding of the necessary public and social services and infrastructure development, (ii) the country has yet to establish a link between mining development and broad-based socio-economic recovery, (iii) uncertainty around implementation of indigenization policies has stunted the recovery of levels of FDI, with depressing effects extending to domestic investment, (iv) a stronger integration into the global economy is yet to be achieved, (v) the important external debt overhang has not yet been resolved, and the country has been increasingly relying on non-concessional forms of financing, (vi) lack of policy consistency upset efforts toward economic reforms and recovery.

1 Drawn from the Zimbabwe Growth Recovery Notes.
The analysis carried out in the 2012 Growth Recovery Notes reveals a deeply changed Zimbabwean economy from pre-crisis times. The 2013 Zimbabwean economy has a larger share of primary products than prior to the crisis. Mining has emerged as the most dynamic sector (replacing the role of agriculture in the pre-crisis Zimbabwe), supported by high international prices of commodities. The structure of sectors themselves has changed. The mining sector, formerly dominated by gold and important small-scale production of over 40 minerals, is now led by large platinum operations that have surpassed gold. Diamonds have been quickly rising to prominence since 2010, becoming a major export in 2012. Following the controversial and disorderly land reform process, the agricultural sector went from being dominated by large-scale commercial farming, to production mostly centered on small-scale production. Moreover, the recovery of the Zimbabwean economy after the decade-long crisis is happening amidst a substantially changed global economy, with the rise of demand from China and India, and the rise of new global value chains.

The mining sector is emerging as the driver of growth in the current phase of the recovery. The new agricultural sector also presents an important potential of supply-response to improved conditions, along with potential of recovery in tourism. Growth in the manufacturing sector appears instead more dependent on the internal demand generated by the two main driving sectors: agriculture and mining. Accordingly, the quality of policy in the mining and agricultural sector will be a strong determinant of the pace of growth of the Zimbabwean economy in 2014-2018. Stronger policies in the mining and agricultural sector will ultimately have positive downstream effects on the manufacturing sector and on services. These relations are illustrated in the figure below. Policies supportive of supply-response in the mining and agricultural sectors to favorable external demand and international prices will also determine the capacity of the Zimbabwean economy to increase domestic saving and accommodate increased flows of imports of capital-goods to support investment into mining, agriculture, tourism, and finally manufacturing and services. At this stage of recovery, both mining and agriculture (led by exports-crops, tobacco and cotton) are heavily dependent from the intensity of external demand. Furthermore, development of mining’s potential requires transfer of technology and FDI, both in the medium-term (as the country develops its current potential), and the longer-term (to support the process of discovery). A vigorous supply-response will require development of infrastructure, in particular energy sources and a sound management of water.
The autonomous nature of mining growth, driven mostly by the intensity of external demand, is evident from the dynamics of its recovery, which started around 2005 with the development of big operations in platinum, while the country was still in the midst of economic turmoil. Dollarization and liberalization in 2009 just deepened the recovery, facilitating a supply response of other minerals, in particular gold. The mining sector led the rebound with average annualized growth of 35.5 percent over the 2009-2011 period and contributing 3.7 percentage points to overall GDP growth of 8.4 percent. The average share of GDP of mining has grown from an average 10.2 percent in the 1990s to an average 16.9 percent in 2009-2011. Strong external demand for primary commodities (in particular platinum and gold) has supported higher production levels, which recovered the pre-2000 levels in terms of value. The mining sector has become the leading export sector, carrying the lion’s share of export growth in recent years and accounts for 50 percent of total exports over the period 2010-2012. Consequently, exporters operating in this sector are the largest and those growing the fastest vis-à-vis exporters in agriculture and manufacturing sectors. Though the mining sector is heavily concentrated (herfindahl index of 46 percent) it is more subject to churning: the entry and exit rates in the sector are higher than in agriculture and manufacturing, and have accelerated in 2012-2013.

At the same time, as the overall production volumes remain subdued due to still unmet capitalization needs, the weakened Zimbabwean economy has been unable to fully exploit the benefits of high international prices to boost exports further over the 2010-2012 period. The outlook is compounded by the dampening of international prices of minerals which occurred since 2012. Dynamism in 2012 has been increasingly dominated by alluvial diamonds, which in 2012 reached a peak export level of 15 million carats. Despite the brisk recovery, the traditional mining sector has not yet recovered the pre-crisis peak-volumes. Still unfavorable legal and
taxation regimes, as well as a business climate seen an unwelcoming to FDI, are stunting levels of investment on exploitation of known deposits. The baseline scenario (unchanged policies) estimates that level of exports in the mining sector will reach US$ 5 billion in 2018, largely below the potential of existing projects. Moreover, levels of investments in exploration are extremely limited.

**In the absence of substantially stronger policies, development of the mining sector may remain stunted and limited to a temporary rebound due to stronger external demand, with limited permanent downstream effects on the rest of the economy.** Moreover, an approach exclusively geared at short-term maximization of rents-extraction from temporary favorable external conditions may present adverse effects on the country’s overall competitiveness and lead to worsening of economic governance. With stronger policies, the mining sector can become the turnkey for longer-term sustainable development. Mineral windfalls can also support mitigation of external vulnerability, investment into infrastructure, higher domestic saving, reduced vulnerability of the banking sector, and lower cost of capital for investment in the manufacturing and agricultural sector. McMahon et al (2012) estimates that under dramatically improved business conditions, existing mining projects could absorb up to US$12 billion of investment by 2018, bringing with an export potential of more than US$11 billion per year.

Most of the old large-commercial pre-2000 agricultural sector has been dismantled, and the existing large-commercial sector is still battling recovery. The Zimbabwean agriculture has lost its leading role of the past and from this perspective it has lost the opportunity to lead a potentially vigorous supply-response to recent higher international prices. However, as Binswanger and Moyo (2012) points out, the new smallholders sector still has substantial potential for growth under the present external conditions, and for poverty reduction. The coincidental confluence of liberalization, dollarization and higher international prices over 2009-2011 supported agricultural profitability and production has responded vigorously to the dramatically improved incentives, in particular in export-crops. Commercially oriented family farmers in the communal areas and in the resettlement areas (including the smaller commercial farms) have reacted vigorously to better incentives on the ground expanding cropped areas. Supply-response has been constrained for semi-subsistence farmers and commercial farmers who have been struggling to expand areas and invest in productive capacities. Increase in yields has also been limited.

**As far as sectoral export performance is concerned, the agricultural sector has been slowly expanding.** Although less dynamic than the mining sector, the contribution of the agricultural sector to export growth has remained positive and stable in the period 2010-2012.

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2 In the survey carried out by McMahon et al (2012), the dramatic improvement of business conditions scenarios assumes that all major bottlenecks, including infrastructural, have been removed by 2018.
Within a context of dollarization, liberalization and high international prices of commodities, Binswanger and Moyo (2012) found that the new agricultural structure with many smaller farms presents a high potential for long-term growth and employment generation. In addition to favorable incentives, the supply response needs to be supported by agricultural services and technical change. There are not yet forthcoming. The strong improvement of incentives that occurred since 2009 need to be maintained. At the same time, policy-makers ought to devote careful attention to improving competition in input and output markets, contract farming, rehabilitation of infrastructure and agro-processing facilities, resolution of remaining uncertainties regarding land tenure and resolution of conflict on land rights.

Profits can be the driver of the recovery of the changed agricultural sector if conditions for a supply-response are reunited. Moyo and Binswanger (2012) emphasize the importance of high agricultural profits for production incentives, growth and retained earnings to enable financing of inputs and investment by the famers in an environment of extreme scarcity of capital, liquidity, and high costs of credit. In the medium to large-scale commercial farming sector, equity financing of investment has not yet responded to the favorable agricultural incentives regime. Recovery of agricultural production remains constrained by the need to adapt to the new agricultural functional structure and finance the necessary investment in a context of still very low domestic savings. The transformation of the agricultural sector during the controversial land reform has left a charged and complex legacy of policy issues that are limiting the supply-response and that will take time to be resolved.

Zimbabwe’s agriculture has yet to develop resiliency. The persistent vulnerability of the new agricultural sector to shocks has been evident in the 2011-2012 and 2012-2013 agricultural years, as late onset of rains, prolonged intra-seasonal drought, and lower planted hectarage, have led to the write-off of half of the potential maize harvest. The very recent decline in international prices and the slowdown in agricultural growth between 2010-2011 and 2011-2012 indicate that the sector, as in the past, remains vulnerable to drought and international price volatility which will need to be addressed by appropriate policies and programs. Vulnerability could become persistent.

Development of the agricultural sector will be critical to achieving long-term broad-based growth of the Zimbabwean economy. Higher productivity in the agricultural sector can fuel a broad-based process of economic transformation and long-term growth with agriculture taking up again its role as a supplier of saving, labor, and inputs to other sectors, and contributing to food security and exports.

Zimbabwe’s manufacturing sector still presents one of the strongest diversifications in the Sub-Saharan African context, however with very limited entry of new firms following the 2009 stabilization and older firms still dominate the landscape. Firms have shrunk in size and have grown more reliant on imported inputs that used to be sourced mostly locally. These firms are ‘survivors’, their current stress levels are, however, extremely high. Davies, Kumar and Shah (2012) highlight that recovery of manufacturing sector is suffering more from supply-side than demand-side constraints to
capacity utilization. While regional comparison reveals that factory-floor productivity and unit labor costs are competitive (but rising fast), lack of competitiveness stems mainly from the consequence of the decade-long crisis, and hyperinflation. Firms are operating obsolete machinery, there are limited availability and high cost finance, power outages, higher input costs due to loss of domestic linkages, lack of access to exports markets due to unreliable supply-chain, and overall uncertainty. Davies, Kumar and Shah (2012) point to micro-economic and institutional policies.

The complex situation for the manufacturing sector is also reflected in terms of export performance. The manufacturing sector’s share in total exports has been in persistent decline since 2010—it went from 31 percent in 2010 to 18 percent in 2012. Consequently, its contribution to export growth has been negative in recent years. While the export base is the largest (compared to agriculture and mining), the average size of the exporter in the sector not only is the smallest of the three sectors, but it also has been declining in 9 percent on average over the 2010-2012 period. Despite the large number of exporters, concentration is high: the top 1 percent of exporters hold 66 percent of exports (this percent is 34 in agriculture).

Investment levels remain subdued with only few firms investing at very low levels. Firms are lamenting poor access to finance, while at the same time profitable investment is not taking place. Smaller publicly listed firms were not able to cover their cost of capital over the 2-year period (Lim and Pommerenke 2012). Better access to finance alone might therefore not stimulate economic growth, unless expectations of profitability improve for the majority of smaller firms in the economy. This points to policies that can support incentives through better investment climate for both domestic and international investors.

At the same time, Zimbabwe is developing a competitiveness gap. The appreciation of the real exchange rate suggests that the price structure of the economy has shifted against tradable products. This has negatively affected recovery in production of tradable products, as capacity constraints hampered a domestic supply response to the strong spike in internal demand that followed 2009 stabilization. The distribution sector has filled the gap instead, supplying imported goods, keeping prices of tradables at low levels and contributing to a current account deficit. The process of de-industrialization might continue.

As dollarization precludes an exchange rate policy, a response should focus on sound fiscal policies, including public wages moderation, support to increased productivity in the private sector and facilitation of entry of new firms. Short-term protectionist measures could lead to short-term gains at the expense of medium-term recovery. The effectiveness of such measures could also be stifled by the incapacity of part of the firms to respond to price-changes, due to broader bottlenecks to production (including decay of machinery, access to power, costly access to finance, broken linkages with domestic suppliers). A strategy to support manufacturing grounded on broader measures aimed at

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3 Enterprise Survey, 2011. Surveyed firms reported access to finance as the top constraint.
reducing costs of business (including reducing the country risk premium to facilitate access to finance), and supporting public services (energy, water, transportation) is more likely to be effective in the medium-term. Stronger policies in mining and agricultural sectors would also stimulate international demand for manufactured goods and the establishment of new horizontal and vertical linkages with the manufacturing sector. Detailed studies on mining linkages, and on bottlenecks to value-addition in agriculture could inform the elaboration of micro-policies in support to recreation of domestic linkages with the manufacturing sector.

Although there is great potential for growth derived from the development of mining and agricultural sectors, the reality of the Zimbabwean export sector is far from ideal. In fact, when Zimbabwean exporters' performance is benchmarked with the experience of exporters in competing/Neighbor countries, the competitiveness gap mentioned above transcends manufacturing. Zimbabwean exporters in general perform below regional average in several fronts related to exporter dynamics. Based on preliminary analysis conducted using exporter-level from customs authorities in Ethiopia, Malawi, Senegal, South Africa, Tanzania, Zambia and Zimbabwe, it is noted that Zimbabwe's export base (number of exporters) is the second smallest within the group. Exports are concentrated in a small group of very large exporters (the top 1 percent of exporting firms hold three-quarters of total exports). Zimbabwean exporters have some of the lowest average growth rates during the period (-7 percent) and they are less diversified than the average exporter in the group, especially in the case of product diversification. In terms of churning -entry and exit rates of exporters-, although slightly below the average for the group, Zimbabwe is far from being the country with the least dynamic export sector (Zimbabwe's entry and exit rates are 37% each, while average rates for the group are 44% and 38% respectively). Finally, in terms of first-year survival of entrants, Zimbabwean exporters are on the average (38 percent) surviving more than Malawi, Zambia and Tanzania exporters.

Access to finance is a major constraint. Banking institutions have nearly doubled their loan-to-deposit ratio over the last two years, but are now paying for it through an increasing fraction of non-performing loans, indicating that the underwriting process has not adequately priced credit risk. On the supply side, banks obtain most of their funding from deposits, relying on domestic savers for funds, but have largely exhausted this source of financing. As a result, Zimbabwe has become increasingly reliant on foreign sources of capital, as evidenced by its current account deficit, estimated at 36 percent of GDP in 2011. In the medium term, higher investment activity will need to be supported by policies supporting the expansion of domestic saving.

The low level of domestic savings has been matched by a marked increase in the current account deficit. The surge in aggregate demand has been financed by external saving, mostly through short-term capital inflows. Foreign Direct Investment (FDI) has remained extremely limited, amounting to less than 10 percent of the total inflows. A growth pattern that is over-reliant on capital inflows is unlikely to be sustainable, without an equivalent parallel increase in the volume of domestic saving and improvement in the effectiveness of financial intermediation of the domestic market.
The experiences in the last two decades suggest approaching the management of FDI inflows with the goal of building resilience, in particular through (i) strengthening domestic process of saving intermediation; (ii) policies to stabilize private capital flows (encouraging inflows into more stable forms of FDI: equity investment, greenfield investment; reduce perceived economic and policy uncertainty; promoting the diversification of sources and destinations of FDI); (iii) promote the developmental impact of private capital flows, aimed in particular at maximizing potential spillovers effects and attracting FDI to new sectors beyond the traditional focus on mineral extraction.

CORE OPTIONS FOR AN AGENDA OF ECONOMIC REFORM

1. Create conditions for increased FDI flows, transparency, and longer-term management of the mining sector

The mining sector has yet to attract enough FDI and technological transfer to reach its production potential and much less attracted investments in discovery. As a result, the true mining potential remains unknown. Little is know about the potential of the diamonds sector as well. The composite mineral tax regime is very costly by regional and international standards, and inefficient in optimizing the revenue from mining as it fails to balance maximizing state revenues while encouraging investment into new exploration. While increased royalties might temporarily increase revenues to the state, it does so by adding to the costs of extraction, lowering the cut-off level and sterilizing resources, resulting in a lower overall level of production and taxation. Optimization of the taxation system requires the overhaul of fee structure and incentives. Moreover, lack of transparency is threatening long-term growth potential. If the introduction of stronger policies is delayed, the mining sector might lose the opportunity to lock-in a share of international investments, leading to slower growth of the sector and reduced effects on internal demand.

Medium-term recommendations:

i. Carry out a complete review of policies and conditions around diamonds discovery, extraction and commercialization;

ii. Remove bias against investment in the application of indigenization legislation and review security of tenure for companies to encourage exploration, while at the same time operating through international bidding systems;

iii. Overhaul of fee structure, namely royalties, and fees for prospecting and exploration, to increase exploration and maximize share of revenues;

iv. Move toward extractive industries transparency, with a special emphasis on diamonds’ industry;

v. Support transparent partnerships in financing infrastructure around mining operations (energy and transport) to foster development of bulk commodities (iron ore and coal);

vi. Learning from successful policies in other countries, use fiscal flows from mining sector to build national assets in support of the recovery in the
agricultural, manufacturing sectors, and the broader socio-economic development;

vii. Support development of domestic horizontal linkages with manufacturing and services sectors by removing bottlenecks to the development of firms that will increase domestic procurement of goods and services by the mining industry.

2. Adapt policies to support profitability in the new structure of the agricultural sector

In the current international framework of high commodity prices, agricultural sector presents an important potential, however, not all conditions for a supply-response are reunited. Higher profitability can be achieved by easier access to export markets, efficient marketing and processing chains, utilization of known inputs and technologies, and adoption of new technology. It can be supported by limited and sharply targeted provision of public goods and services such as research and extension, infrastructure, effective regulation, and justified anti-dumping measures.

Agriculture, in particular the ‘maize economy’, still features widespread vulnerabilities, which, if not addressed, may become permanent. As in other countries, food grain production and marketing pose the challenge of ensuring domestic food availability and food security in the face of volatile prices in international markets, and volatile production due to drought. Maneuvering through these risks, countries need to reconcile the need to provide adequate incentives to their own producers with the need to provide affordable staple food.

Medium-term recommendations:

i. Maintain the post-2009 favorable macroeconomic and trade policy environment, resisting the temptation of reversing 2009 reforms; especially those affecting inputs for the sector;

ii. Support supply-response in new farming structure by improving overall conditions (in particular, productivity growth, water management and irrigation, marketing arrangements);

iii. Enhance land security and address conflicts resolution;

iv. Improve overall business conditions to encourage FDI flows into agri-business and creation of effective linkages with farming and markets;

v. Study food-security options, and develop a strategy to attain national and household food security.

vi. Increase transparency in the implementation of policies directly affecting the sector (e.g. technical standards, SPS and other non-tariff policies);

vii. Build technical capacity for a fair and transparent implementation of policies regarding trade remedies such anti-dumping, countervailing duties and safeguards.

3. Adopt a medium-term strategy for re-manufacturing Zimbabwe

The ongoing debate on support to manufacturing sector assumes that low capacity utilization stems from lower prices due to important inflows of imports. We challenge
this diagnostic on two counts. First, our analysis shows that the poor-supply response of
the manufacturing sector is primarily driven by supply-constraints and not by demand
constraints. Second, the decline of manufacturing sector has not been a recent episode
that can be ascribed to the consequences of the 2009 liberalization, but has been
following a longer-term trend over about two decades. Davies, Kumar and Shah (2012),
highlight that protectionist measures are likely to be ineffective, and increase distortions
of incentives. Correcting existing distortions caused by high levels of economy-wide
costs of doing business is bound to have broader positive effects. Medium-term potential
for growth in manufacturing will be affected by the pace of mining and agricultural
growth, and the capacity to rebuild linkages with these autonomous drivers of growth.
Improving the overall operating conditions of the private sector can support both areas of
growth. On the one hand, unlocking Zimbabwe’s potential for investment in mining is
bound to have significant downstream positive effect on manufacturing. On the other
hand, ending autarchic policies and fostering a stronger integration on regional and global
value chains can support export-oriented firms.

Medium-term recommendations:

i. Resist protectionist measures, that generate anti-export bias and might
increase overall prices, and aim at micro-policies to improve service delivery
to firms instead, and reducing overall cost of business, including prioritizing
bottleneck releasing investments in infrastructure;

ii. Support internal demand by supporting higher levels of growth in mining and
agriculture, and fostering domestic linkages;

iii. Support competitiveness of the sector by applying sound fiscal policies (and
wage moderation), reducing firm’s costs by improving the quality and price of
services (efficiency of state owned enterprises);

iv. Remove anti-investment bias, and support FDI flows toward firms with
export-potential, this can also help alleviate the pressures arising from the lack
of access to finance both short and long term credit;

v. Improve credit availability by strengthening efficiency of financial
intermediation, and expanding domestic savings;

vi. Implement practical measures that facilitate information to exporters on all
the different procedures and fees involved in the exporting activity (e.g. single
window scheme, government e-portal);

vii. Support investment in infrastructure that can help further reduce transport
costs;

viii. Move forward the agenda on regional integration, by supporting negotiations
pro-market access in the region and by applying policies to exporters from
neighboring countries in consistent manner.

4. Adopt a sound fiscal management policy, and support efficient and reliable
delivery of public services

To avoid the state crowding out domestic savings, more effort will need to be put into
maintaining fiscal balance. The state should contain the explosion of nominal wages,
safeguard fiscal space for the provision of basic services and the implementation of the
capital budget including projects for necessary rehabilitation of essential infrastructure. The energy sector appears a short-term key constraint to vigorous growth. Without a prompt increase of capacity at fair prices, potential for recovery in mining and agriculture (and conversely in the manufacturing sector) will remain stunted. Stronger management of water will also be required to support higher yields in agriculture.

Medium-Term recommendations:

i. Strengthen efforts to maintaining fiscal balance, and avoid crowding out financing of private sector investment;

ii. Review expenditures mix, and increase emphasis on services delivery to citizens and firms,

iii. Increase level of spending in service delivery and investment, grounding them on permanent flows to the treasury, and avoid unfunded development of services

iv. Prioritize public investments by adopting energy and water investment frameworks;

v. Reserve a substantial part of fiscal revenues from minerals, in particular diamonds, to finance investment into national assets, and human capital development, strengthening the linkage between fiscal revenues from mining and broader socio-economic development.

5. Reform and Rebuild Economic Institutions

Finance is another important constraint that will determine the pace of growth. Provided more welcoming policies to international investors are in place, external finance can be valuably absorbed (in the form of FDI or portfolio investment) in mining, commercial agriculture, tourism, some selected services sectors (ICT, energy), and more export-oriented firms in the manufacturing sector. Financing of smaller-scale agriculture, the broader manufacturing sector and services, however, will only expand at the pace of expansion of domestic saving. Strengthening the resilience and the efficiency of the domestic financial sector can accelerate this, as it will increase the capacity to handling domestically increased revenues from the mining sector. A sound management of fiscal revenues from the mining sector will finally increase the public sector capacity to support long-term growth prospects by financing the necessary infrastructure, including strengthening the domestic capacity to leverage of PPP-financing.

The overall analysis of growth potential highlights the urgency of an overall improvement of business climate and reduction of non-factory floor costs of operating firms. The state should improve both the work environment where real factor of production are deployed, and the quality of mediation of the transformation of nominal endowment of mineral resources into real deployable endowments. The economic legacy of short-termism of incentives, and economic institutions more prone to short-term extraction raise the risk of the country remaining at lower-level equilibrium. Policies supporting the mining and agricultural sector will need to overcome these legacies. Economic institutions will need to mature from extraction and control function, to a facilitating role aimed at unleashing the full potential of private initiative.
Medium-Term recommendations:

i. Strengthen all aspects of institutional management around the mining sector;
ii. Increase oversight and efficiency of State-Owned Enterprises, and proceed with priority reforms (in particular: telecommunications, energy, food security);
iii. Strengthen resiliency and efficiency of the domestic financial sector;
iv. Strengthen public financial management systems across all levels of the public sector;
v. Increase transparency and improve access to statistical information that allows the study of the impact of policies on growth, productivity and welfare.
MINING SECTOR DEVELOPMENT

1. **Preamble:** The World Bank has prepared a series of Economic Recovery Notes to guide its engagement with the new administration in Zimbabwe. The notes are intended to outline issues, challenges and policy options in the key sectors of the economy.

2. **Situation Analysis**

   2. The quality of policies in the mining sector will be a strong determinant of the pace of growth of the Zimbabwean economy in 2014-2018. In 2013, the Zimbabwean economy has a larger share of primary products than prior to the crisis. The mining sector rebound, aided by the new diamond bonanza and high commodity prices of gold and platinum, has surpassed that of other sectors, in spite of a difficult policy climate for FDI (replacing the role of agriculture in the pre-crisis Zimbabwe). The mining sector has become the leading export sector, accounting for 47 percent of total exports in 2012.

   3. But the rebound is not sustainable. The sector remains under-capitalised and production volumes for all but a few minerals have not reached pre-crisis levels. Prices of most commodities have retreated from their historic highs and traditional capital markets accessed for mining investment are tight. Globally, miners are focusing on brownfield expansion and only the best greenfield mining projects with clear, predictable positive cash flows are being financed. In addition to these global constraints, recapitalization of the sector in Zimbabwe has been further depressed by (a.) political uncertainty, (b.) insecurity over mining rights due to the implementation of indigenisation legislation, and (c.) the perception that fiscal policy remains focused on short term maximization of rent redistribution at the expense of encouraging growth of the tax base and strengthening legal certainty of the management of mineral rights. Diamonds, the one sub-sector that is expanding rapidly with new investment, is suffering from a near complete lack of transparency and its contribution to socio-economic development of the country thus has been limited.

   4. In the absence of development friendly policies, development of the mining sector may remain stunted and limited to the temporary rebound caused by strong external demand with limited positive impact on the rest of the economy. The World Bank’s baseline scenario (unchanged policies) estimates that the level of exports in the mining sector will reach US$ 5 billion in 2018 compared to US$ 11 billion with changed policies (McMahon et al 2012). Moreover, an approach exclusively geared at short-term maximization of rents capture and redistribution from temporary favourable external conditions is creating adverse long term effects on the country’s overall competitiveness.
and will sterilise\textsuperscript{4} certain subsoil resources in the medium to long run. High prices have masked some of the policies of the past ten years. As prices relax from their historic highs, it will be important to restore confidence in the sector to secure its continued growth and long term potential for broad development.

5. **With improved policies, the mining sector can become the turnkey for longer-term sustainable development.** Mineral windfalls can support mitigation of external vulnerability, provide critical investment into infrastructure, generate demand for supply of goods and services, re-connect with a manufacturing sector that once served the mining sector and provide incomes in rural communities where other livelihoods have struggled.

6. **With the right policies, mining can be pro-poor.** Mining contributes to poverty reduction in a number of ways – the most direct linkages being job and income generation along with opportunities for growth for lateral or downstream businesses. Indirect benefits include linkages through infrastructural investment – new and better roads or railways, access to water supply – and social services provided by large-scale mines (schools, clinics and housing).

7. **There are a number of other indirect benefits from a vibrant and well governed mining sector.** Other major benefits are indirect – increased foreign exchange earnings, higher domestic saving, reduced vulnerability of the banking sector, and greater government revenues. While rich mineral endowments provide scope for economic development and poverty reduction, many economies driven by extractive industry activities have failed to leverage this wealth efficiently. Governments sometimes blame this on exploitive foreign investors and multinational mining companies for this, but often it is due to state policies leading to consumption, rather than investment of mineral rents.

**CONSTRAINTS AND CHALLENGES**

8. With the potential positive contributions of the sector in mind, together with the current sub-optimal performance, the remainder of this note highlights constraints, challenges and the resulting priority policies for the long term sustainable and inclusive development of Zimbabwe’s mining sector.

9. In summary, those constraints and challenges to the development of the sector are:

   (i) An **unstable investment environment** coinciding with a retreat in commodity prices from historic highs;

   (ii) Increased reliance on the mining sector as the engine for growth has resulted in numerous uncoordinated fiscal and non-fiscal demands, the cumulative impact of which is not well understood;

\textsuperscript{4} The term “sterilise” or “sterilisation” is used throughout this note to refer to a situation where a policy renders or causes an entire resource (or portions thereof) to be sub-economic in the medium or long-run.
(iii) Aside from the recent “diamond rush”, an outdated mining cadastre, combined with (i) and (ii) above has led to very little new investment in exploration and greenfield projects;

(iv) Aged infrastructure and interruption of key services such as energy limits the safe and efficient operation of mines, restricts the value added from the sector’s products (forward linkages) and limits the ability of Zimbabwean enterprises to supply services or manufactured inputs;

(v) Reduced linkages to the broader economy due to a shrinking manufacturing sector (backward linkages), a stagnant to shrinking tax base (fiscal linkages), lack of investment in ancillary mining infrastructure (spatial linkages) are all aggravated by the unstable policy environment;

(vi) The significant lack of transparency in mineral revenues, particularly with respect to diamonds, is hurting Zimbabwe’s governance credentials and diminishing the value of its diamond wealth; and

(vii) The lack of an articulated diamond strategy, limited knowledge of the country’s diamond resources and inability to attract leading mining companies significantly limits Zimbabwe’s ability to leverage its finite diamond resources for inclusive and sustainable development.

10. Items (i) to (v) are discussed in section B.1 on the legal/policy framework, while items (vi) and (vii) are discussed with specific reference to diamonds in section B.2.

**LEGAL FRAMEWORK, INDIGENISATION AND POLICY FLUX**

11. Not unlike many countries, Zimbabwe’s mining sector is governed through a number of acts and regulations. The Ministry of Mines and Mining Development (MMMD) manages the mineral sector in accordance with the Mines and Minerals Act, the Mining (General) Regulations of 1977, and their amendments. Mining operations are also regulated by sections of the Environmental Management Act of 2002 and its 2007 amendment, the Explosive Act, the Forest Act, the Parks and Wildlife Act, the Public Health Act, and the Suppression of Money Laundering Act.

12. A new Draft Minerals Policy contains many modern features and is a step in the right direction. Based off a comprehensive analysis commissioned by the Zimbabwe Economic Policy Analysis and Research Unit (Jourdan et al. 2012), the Draft Minerals Policy contains a number of best practice policies such as the stimulation of backward, forward, spatial and fiscal linkages, calls for improved transparency and the introduction of progressive taxation. However, in addition to some “best practice” policies, the Draft Minerals Policy envisages a greater role for the state in the market including the determination of market prices and extraction rates of certain “strategic minerals”. Depending on the degree to which this is limited through regulations supporting a new mining law, market interference could choke off investment in strategic sectors and financially burden state owned companies charged with the success of such policies.

13. Overall the Draft Minerals Policy and other Acts contain a number of different requirements on mining companies and it will be important to understand the cumulative fiscal and non-fiscal burden to ensure the sector’s long-run sustainability. Where possible, Government’s multiple objectives should be cast within
a flexible framework (such as a scorecard\textsuperscript{5}) to balance and communicate government’s priorities and track and assess industry performance. The World Bank is currently preparing a short course and financial modelling tool for the Government to assist it in assessing the cumulative effect of policies on the sector and how these may affect aggregate future revenues.

14. **Possibly the biggest policy negatively impacting the mining sector is the indigenization policy.** Ownership of mineral resources should be seen as a source of necessary capital and not a goal. The consequences of ownership need to be fully understood before a rushed and ideological application of the law takes place since indigenisation, is in essence, a (potentially very high) tax on foreign capital that dampens overall investment, sterilises lower grade deposits and has possible negative effects on fiscal linkages. The Government would be well advised to put more emphasis on fiscal linkages, expansion of the sector and increasing domestic linkages than pursuing ownership goals that are likely to further dampen already depressed investment levels.

15. **While the Government continues negotiations with a number of mining companies concerning their indigenisation plans, uncertainty creates disincentives for investors and restricts capital in an already capital starved economy.** The mining sector is highly capital intensive and requires continuous investment throughout the life of operations to open up new resources or to leverage scale economies. Indigenisation policies may have limited “immediate run” effects and can be seen as a successful way to redistribute rents, but they are almost guaranteed to have detrimental long run effects as: (i) investors/miners making new capital investment decisions see increased risk associated with mining in Zimbabwe due to policy uncertainty; (ii) minority shareholder interests in Zimbabwean companies will attract a valuation discount (due to a lack of control); (iii) foreign technology and know-how are less likely to be deployed to subsidiaries where the owner of the technology does not control how it is used; and (iv) domestic capital and technology itself continues to be in short supply. As the cost of capital increases, production shifts from capital intensive to less capital intensive methods. This tends to limit the scale of the operation, increase operating costs which, together with the high cost of capital, either renders projects completely sub-economic or increases the cut-off grade—i.e. the grade below which it is not economically feasible to mine. In both cases, the result is the same in that the resource is inefficiently depleted, portions of the resource are sterilised and the medium to long run prosperity of the sector is diminished.

16. **Discussions of expropriation and ad hoc taxes increase policy uncertainty and the cost of attracting capital.** Politicians have recently proposed amendments to the mining regime which, if approved, would allow the state/indigenisation partners to appropriate a 51% stake in mines without payment. As JP Morgan wrote in a recent note to investors: “Clearly the regulatory regime surrounding mining in [Zimbabwe] is in a

\textsuperscript{5}The scorecard could be designed to give effect to provisions contained within the various pieces of legislation governing the mining sector. It should facilitate the application of legislation, identify government and industry priorities and provide a mechanism for measuring overall compliance with the "spirit" of different policy objectives.
state of flux, which poses a valuation risk.” (Shepherd et al. 2013). Investors typically deal with these types of risks by increasing their required returns to capital and assigning less value to more distant cash flows – both of which are rational and efficient responses to distortionary policies and policy uncertainty with downside bias.

17. **Policy uncertainty and flux also have short and long run effects.** Uncertainty creates long term distortionary effects and sterilizes resources since optimal timing of their depletion can sometimes be postponed, ultimately resulting in missed opportunities. Short term policies, such as temporary royalty hikes or other non-tax requirements that increase the marginal costs of production, can have short run distortionary effects. The degree to which the impact is distortionary in the short run is ultimately a combination of the policy itself and the flexibility of producers to respond to changes in the short run.

18. **Policy weaknesses, uncertainty and flux can be addressed.** Comprehensive policy reform is a long term process requiring consultation with a set of informed stakeholders. With the 2013 elections now complete, the Government should continue dialogue with industry, the manufacturing sector, affected communities and other stakeholders to set clear policies for the future, together with a realistic timeframe for implementing these policies and associated regulations.

19. The required dialogue between stakeholders is complex and will take time; however, if managed properly and if stakeholder concerns are given due consideration, it is an opportunity for Zimbabwe to show that it is “open for business” and is committed to the sustainable and inclusive development of the sector. Indigenization may address issues of perceived “fairness” in the short run, but sustainably addressing Zimbabwe’s historical inequalities is a long term strategy requiring a focus on long term, non-distortionary tools such as the stimulation of linkages at the national and community level and removal of ineffective policies and barriers.

20. **In the short term, focus should be on identifying immediately actionable activities to stimulate linkages.** The World Bank shares the government’s desire to share the prosperity of mineral resources; however, this is most effectively done by developing these linkages, rather than indigenization or nationalization. In support of this objective, World Bank has recently launched a study to examine potential barriers to, and opportunities for, stimulating backward linkages through local content. This study is aimed at: (i) ameliorating market failures around coordination and imperfect information to identify opportunities for backward linkages; and (ii) identifying distortionary and restrictive policies that are acting as barriers to the growth of the manufacturing and service sectors. In addition the World Bank has carried out a study on the current shortcomings of Zimbabwe’s mining cadastre and concludes that the introduction of a modern mining cadastre would have important implications for the transparent management of both the large scale and small scale mining sectors and continued long term investment in exploration and sustainability of the sector. Finally, continued support for transparency initiatives such as the ZMRTI will be key to demonstrating Zimbabwe’s good governance credentials.
DIAMONDS

21. **In recent years, Zimbabwe has experienced a resource boom with the discovery of alluvial diamonds.** There are two distinct types of diamond resources that make up Zimbabwe’s diamond industry: the traditional kimberlite mines at Murowa and River Ranch; and the recently discovered alluvial mines in the Marange and Chimanimani areas, in which the Zimbabwe Mining Development Corporation (ZMDC) is in joint ventures with other partners. In four of the ZMDC controlled mines in the Marange area, production in 2011 was 9 million carats and expected production in 2012 was 11 million carats. Production is expected to peak at approximately 12 million carats over the next few years, though with further investment production could reach 15.2 million carats per year by 2018.

22. **Information regarding the sector is inadequate and is almost certainly leading to a sub-optimal use of this finite resource.** There is very little information available throughout the value chain from the development of the resource to the financial benefits derived therefrom. Furthermore, there is significant confusion among various government departments regarding actual production and revenues being generated from diamond mining. Conflicting information, combined with a limited to non-existent understanding of the overall resource by government and the low levels of technical capacity of those players involved in the mining itself is almost certain to lead to suboptimal development of the resource. The government should prioritise the collection of more information on the diamond resources and carefully examine what options it has regarding the optimal development of the remaining resource.

23. **Little information for planning purposes has resulted in unmet expectations.** Zimbabwe lacks fiscal space and revenue underperformance has put public finances under severe pressure. As a result of a large shortfall in diamond-related revenues, in particular, lower-than-expected dividends from joint-venture enterprises under the ZMDC and the larger-than-budgeted increase in allowances to civil servants, the budget faced significant fiscal slippages in 2012. Among the suite of possible explanatory factors we highlight: (i) Government’s low technical understanding of the potential of the resources together with a diamond mining sector that is characterised by little experience; (ii) poor transparency which exacerbates weaknesses in the fiscal regime, and a low level of capacity to correctly assess and collect taxes resulting in the potential leakage of diamonds and diamond revenues.

24. **A recent survey of stakeholders by the World Bank has identified the Marange and Chimanimani diamonds as the major source of opaqueness in mining revenue transfers in the country.** The Marange and Chimanimani diamonds are under European Union and United States sanctions which make it difficult to attract reputable companies to participate in their development, and for those companies that are currently active to participate in improved transparency initiatives such as the ZMRTI. In addition the state owned ZMDC and Mineral and Marketing Corporation of Zimbabwe are both
under U.S. sanctions. According to the World Bank survey, these sanctions are seen as the major reservation regarding stakeholders’ willingness to participate in the ZMRTI.

25. **Improved transparency is a catalyst for increased diamond wealth.** Despite Zimbabwe’s diamond trade remaining KP compliant, a lack of transparency regarding revenue flows limits Zimbabwe’s ability to market its diamonds through legitimate channels and receive global market prices. Over the course of 2013, the global diamond industry has seen a major transformation with De Beers’ historically important trading hub shifting from London to Gaborone. This move is significantly important for southern Africa, making it the global destination for rough diamond trading and attracting the world’s most legitimate diamond traders to the region. This is good news for Zimbabwe’s diamonds, both in terms of prices and governance, but requires that Zimbabwe improve the governance of its sector before these benefits can be realised. Continued opaqueness limits Zimbabwe’s access to main markets and has resulted in the current export route to Dubai, side-lining European and American dealers (Kerr and England 2013). This is not good for governance or the prices Zimbabwe receives on its diamonds. In fact, these actions may be contributing to worse governance since the current pool of buyers, who circumvent sanctions to purchase diamonds, may be less scrupulous than the American and European traders.

26. **Opaqueness of “lootable” resources is a well-known transmission mechanism for the “resource curse” through civil conflict.** Research has shown that resources that are easily “lootable” (such as gemstones and some precious metals) appear to be particularly harmful for growth in countries with weak institutions. (Mehlum et al. 2006) Resource-inspired conflict is never inevitable and to protect against the risks of civil conflict the single most important action is to increase transparency. (Ross 2003) Furthermore, it is no surprise that mining companies are generally in favour of increased transparency as it has many positive spill-overs – public information forms a basis for a common understanding and disclosure of taxes and other payments help to ‘legitimise’ the sector in the eyes of communities and other affected stakeholders. A lack of transparency undermines clear public understanding and development of consensus on how finite resources can contribute to sustainable and inclusive growth.

27. **Diamond sector reform is necessary to leverage this finite resource for increased prosperity.** As noted by the IMF (2013), the new diamond policy, approved and published in late 2012, is a step in the right direction towards increasing transparency and accountability. The policy envisions, inter alia, tasking the Zimbabwe Revenue Authority to work with the MMMD in monitoring diamond proceeds, and placement of a government-appointed diamond valuator to value all rough diamonds (with an

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6 In December 2011, the U.S. imposed bilateral sanctions on two of the mines. These are subsidiaries/joint ventures of the ZMDC, which is on the U.S. sanctions list. Since 2001, members of the international community (the USA, EU, Canada, New Zealand and Australia) have imposed various sanctions and restrictive measures on named individuals and institutions in Zimbabwe, even while maintaining specific instruments for humanitarian support. For a list of individuals and organisations facing U.S. sanctions see: [http://photos.state.gov/libraries/zimbabwe/231771/PDFs/2011_08_18_zimbabwe_sdns.pdf](http://photos.state.gov/libraries/zimbabwe/231771/PDFs/2011_08_18_zimbabwe_sdns.pdf); and [http://photos.state.gov/libraries/zimbabwe/231771/PDFs/sdn_list_condensed.pdf](http://photos.state.gov/libraries/zimbabwe/231771/PDFs/sdn_list_condensed.pdf)
independent valuator to settle disputes between producers and the government-appointed valuator).

**POLICY OPTIONS**

28. **The many reforms that are taking place at an accelerated pace require prioritisation.** Priorities need to be identified and communicated and resources need to be assigned to meet these objectives, particularly over the next twelve months. The Government has committed to fast-track amendments to the Precious Stones Trade Act that give force of law to certain aspects of the Diamond Policy and bring the Act in line with international best practices. Amendments are to be submitted to cabinet and to parliament by the end of September 2013. In addition, a new Mines and Minerals Act is to be submitted to Parliament by the end of December 2013. Zimbabwe needs new legislation, but it also needs sustainable policies that can leverage the mining sector for broader development whilst retaining its ability to attract capital. Though new legislation is needed urgently, the government should not compromise on consultations with industry, communities and other affected stakeholders to meet this objective.

29. From the above discussion, a number of key reforms for the Government to pursue immediately should therefore include:

   (i) **Stimulate backward linkages** through local content with a focus on (a.) eliminating market failures regarding lack of coordination and imperfect information to identify opportunities for backward linkages; and (b.) identify and remove distortionary and or restrictive policies acting as barriers to the growth of the manufacturing and service sectors.

   (ii) **Modernise the mining cadastre** to improve transparency of license allocation, improve land-use planning and stimulate investment in exploration and the long term sustainability of the sector.

   (iii) **Continue support for the ZMRTI and work towards Extractive Industries Transparency Initiative (EITI) validation** as key step towards: (a.) demonstrating Zimbabwe’s good governance credentials; and (b.) improving the value of Zimbabwe’s mineral resources.

   (iv) **Clarify the indigenization policy and create an environment of stability** through which long term issues, such as addressing historical inequities, shared prosperity and long run investment sustainability can be solved.

30. While working with a longer time horizon in mind, the Government should:

   (i) **Review the Draft Minerals Policy and the Mines and Minerals Act with a view towards providing a stable and predictable climate for investment.** Towards this objective the government should undertake the following:
       a. Develop an internationally competitive legislative framework for the mining sector, including a modern fiscal regime that takes into account the impact of tax and non-tax obligations on the long term sustainability of the sector; and
       b. Develop a mining sector roadmap to identify and evaluate opportunities to stimulate forward, backward, fiscal and spatial linkages from the sector to
the broader economy through both policies and infrastructural investments.

(ii) **Develop and communicate a diamond strategy** that is grounded in detailed technical and financial information, optimises the finite resources and leverages Zimbabwe’s diamonds for development.

**REFERENCES**


AGRICULTURE AND FOOD SECURITY POLICY NOTE

SITUATION ANALYSIS

1. Agriculture plays a significant role in the socioeconomic development of Zimbabwe, as a food and feed provider, employer, and income earner, accounting for 16-20% of GDP and employing 70% of rural population. Its decline was a key factor in the collapse of the Zimbabwean economy overall (with nearly half the population depending on food aid in the crisis years). The country's MTP recognizes that fast and sustained growth in the agricultural sector is critical to its economic and social development goal of food self-sufficiency and reducing poverty for a large segment of the population. To facilitate faster growth in the agricultural sector, the Government has recently finalized the drafting of the Zimbabwe Agricultural Investment Plan (ZAIP), which ensued from the Country led Comprehensive Africa Agriculture Development Program (CAADP) process. The ZAIP reinforces the need to achieve agricultural development and food security, and sets the road map throughout 2014-18, with the objective to attain at least 6 percent annual growth in the sector (ZAIP, 2013).

2. Two fundamental shifts have had important implications for both the structure of the country's agriculture sector and for strategies for achieving sustainable food security. First, the Fast Track Land Reform Programme (FTLRP), initiated in 2001, has radically reconfigured the agrarian structure in Zimbabwe. In particular, the number of small and medium-scale farmers has increased while the commercial farm sector has diminished. In the short term, this shift in the agrarian structure has contributed to a significant decline in overall agricultural output, particularly of cereal food crops. This is due, in part, to the sorts of capital, technological, and credit constraints that are faced by smallholders around the region. The FTLRP has also introduced new forms of agrarian differentiation as it lessened the stark differences between commercial and small-scale farmers, while increasing the heterogeneity within the smallholder sector in terms of A1 and A2 land beneficiaries. High levels of smallholder heterogeneity are a common attribute of smallholder production systems in the region and have important implications for the appropriate types of interventions needed for driving agricultural productivity growth and achieving food security. Yet, in the medium to long-term this new agrarian structure may offer significant opportunities to use agriculture as a vehicle for poverty reduction and economic growth.

3. Second, beginning in 2009, Zimbabwe introduced a multi-currency regime, and initiated a process of agricultural market liberalization, which included scaling back the scope and scale of the Grain Marketing Board (GMB) to create space for greater
private sector participation in food markets, and freeing up cross border trade of agricultural commodities (USAID, 2012), thereby sharply improving domestic producer incentives and profitability. In the context of a changing agrarian structure, the liberalization of agricultural markets has prompted an important reorganization of agricultural markets. For the grain markets in particular, Zimbabwe has witnessed a proliferation of “informal” small-scale trading systems and associated small-scale milling enterprises. The current policy environment in which there are no exchange rate distortions, a tariff structure that is moderate and fairly uniform, and no impediments or taxes on agricultural exports is a favorable environment to provide the best possible price incentives, given the level of international prices. It is important that this basic policy framework will be maintained in the future (Binswanger-Mkhize and Moyo 2012). Free access to export markets and good domestic marketing arrangements are the key factors in ensuring high profitability. **Full transmission of world market prices to domestic markets, will also ensure good incentives for domestic production, and that domestic food prices remain favorable for consumers.**

4. **Contract farming arrangements have contributed significantly to the consistent performance of the cotton sector and the recovery of the tobacco sector.** In both crops the growth continued to be exceptionally rapid up to 2011-12. There is potential for further development for food crops and livestock products that are more perishable, and require significant processing or packaging near the area where they are produced, while it has little potential in other products. The commodity-specific arrangements are usually very specific to the requirements of the product, and therefore successfully emerge out of intensive consultations of the producers and the contracting firms. Monitoring by third independent parties of contractual performance of the value chain, the division of the gains within it, and the negotiations of the prices and other contract terms has shown good results (ASI, 2012).

5. **These changes are occurring within a global food economy characterized by projections of sustained high and volatile global food prices** (Figure 1). In the short run, high food prices will negatively affect the urban poor and net buyers of food in rural areas, which in southern and eastern Africa account for approximately 40-60% of the rural population (Jayne et al 2010). Yet, high food prices offer significant opportunities for surplus food producers, in Zimbabwe and the region, to accumulate capital and drive economic growth (Binswanger-Mkhize and Moyo 2012). Striking an effective balance in this food price dilemma is at the heart of both short and long-term strategies for achieving agricultural-led growth, poverty reduction, and sustained food security.
6. **At a sub-regional level, Zimbabwe lies at the center of several important trends in terms of food production and demand.** In terms of maize production the SADC region has witnessed a significant increase in aggregate production since 2005/06 (Figure 2). Much of this has been driven by supply increases from Malawi and Zambia, where large-scale, yet expensive, maize input and output market subsidies coupled with favorable weather conditions have promoted an expansion in maize production (Jayne et al 2008; Burke et al 2010). However, much of this expansion has come from increases in land area under maize cultivation, not from productivity improvements (Ricker-Gilbert et al 2013). Moreover, despite significant public expenditure to encourage maize production, levels of rural poverty and childhood stunting remain virtually unchanged in both countries. A careful re-thinking of these subsidy schemes is therefore warranted.

7. **In many ways Zimbabwe stands at an agricultural crossroads.** In the context of significant shifts in the organization of production, marketing, processing, and trade it is critical for the new Government to embark on an effective strategy for promoting food security and agricultural growth through appropriate policies and investments in the sector.
CONSTRAINTS AND CHALLENGES

8. **The persistent vulnerability of the new agricultural sector to shocks has been evident** in the past two agricultural seasons, as late onset of rains, and prolonged intra-seasonal drought, and the decline or late arrival of subsidized or free inputs have led to the write-off of about 45 percent of the potential maize harvest in 2011-2012. A similar pattern is emerging for the 2012-13 agricultural season, with current estimates predicting a 3.5% decline in agricultural growth for 2012, largely due to lower maize production, resulting from adverse weather conditions, lower acreage planted and sub-optimal yields. It is therefore easy to imagine scenarios in which vulnerability becomes persistent: (1) Profitability could be undermined by an appreciation of the real exchange rate driven by mineral exports, a foreign investment boom and a resumption of significant foreign aid flows. This would make it very difficult to regain competitiveness in horticulture, milk, wheat, and to continue growth in sectors that have already responded to improved incentives. (2) A possible sharp decline in international commodity prices, especially in cotton and tobacco prices could undermine these important sectors. (3) Price incentives and profitability could also be undermined by reintroduction of command and control measures in agricultural markets, maybe in an attempt to deal with price volatility. (4) Unfavorable developments which would undermine security of land tenure, and with it the prospects for investment in the commercial and estate sectors, and in agro-industries vital for contract farming, and in private agricultural research. (5) Lack of fiscal resources could constrain the revitalization of public agricultural research and extension, as well as extension contracted to the NGO sector or farmers’ associations. (6) The lack of foreign investments and foreign aid, and continued capital flight could perpetuate the extreme scarcity of investible resources in the economy, including for agriculture. And (7) a sequence of droughts could sharply reduce food crops outputs, and increase the import bill, and result in decapitalisation of food producers in the farm sector (Binswanger-Mkhize and Moyo 2012).

9. **Most of the growth of output observed until 2010-11 came from area expansion.** In maize and other commodities, 2011 yields remain far below potential or even historically achieved yields (Fig.3). Low yields are mainly due to limited utilization of crop and livestock inputs, caused by higher input costs, limited own capital and extremely limited and unaffordable credit. However, contract farming in cotton and tobacco are exceptions because inputs are provided as part of the contracts from a growing number of firms involved in the export business.
Fig 3 Maize Area Planted and Overall maize yield trends


10. The decline of the irrigation sector contributed to sub-optimal sector performance. Irrigation schemes are troubled by low productivity, poor market access, high transport costs, and unreliable power supply. The installed irrigation infrastructure is estimated to be between 30 to 75% functional, and only 70,000-135,000 ha are being irrigated. On the basis of available internal renewable water resources and the existing storage capacity (103 km$^3$), the irrigation potential of the country is estimated at around 365,000 ha, considerably less than irrigable land, estimated at 600,000 ha (MAMID-Alterra, 2013; Mazungu, 2011; Irrigation Masterplan, 2012). It is estimated that even without additional investments in storage capacity, about 200,000 ha can be developed from existing under-utilized storage capacity and dams under construction (MAMID, 2013).

11. Most farmers remain poorly capitalized. Capital scarcity, the limited availability and high cost of credit, and sharply constrained fiscal resources, mean that most investment and input finance will have to come from retained farm profits. It is, therefore, very important that a favorable macro-economic policy regime be maintained.

12. There is a need for a cohesive strategic framework (across sectors) that facilitates markets and trade, which would create incentives for agricultural investments and innovation, increasing the agricultural sector’s competitiveness, as well as public and private investments in efficient transportation, storage and retail infrastructure and delivery of key support services. Coupled with an efficient market environment and trade framework, possibly in combination with a well-conceived strategic grain reserve for emergency purposes, this should ensure sufficient food availability in the country and increased access to food, thus improving Zimbabwe’s food security on a sustainable basis. There is a need to reconcile the attempts to set adequate incentives to producers, while providing access to affordable staple food to their consumers, especially the poorer ones among them. In Zimbabwe, the process of reconciliation of these objectives remains unresolved.
ISSUES AND OPTIONS

13. The agriculture sector would continue to benefit if the new Government decides to uphold the post 2008-2009 conducive macro and trade policy environment in which inflation is low or moderate, there are no exchange rate distortions, and the tariff structure is moderate and fairly uniform. Preference could be given to maintain the current low levels of tariffs for agricultural imports for raw and processed agricultural commodities. It is important to avoid backsliding into quantitative controls in input and output markets, as that could easily evolve to policies that reduce producer incentives.

14. The GoZ may wish to focus on the rehabilitation of degraded irrigation schemes and their redesign to suit the new farm structure. A thorough effort is required to adapt irrigation technologies and systems to serve the full range of farm types. Imports of smaller water pumps and water distribution equipment, such as mini-centre pivots, etc. suitable for smaller farms has already begun, and should be further facilitated including by strengthening of local agro-industry. The financial requirements for irrigation development and rehabilitation are beyond the capacity of the government alone. Approximately US$370 million is required to bring irrigation schemes back to pre-2000 performance levels and a further US$250 million to develop new irrigation schemes from underutilised dams. To attract this level of funding for irrigation from commercial sources, there is a need for lease arrangements for periods over 25 years that are acceptable to financial institutions and which give adequate security of tenure to farmers (MAMID-Alterra report, 2013).

15. The Government may wish to consider a transitional approach to a market-led growth strategy for the sector. If the strategy includes input subsidies, these should be carefully targeted, temporary, and designed to encourage private sector development in input markets, aimed at addressing the primary, short-term production constraints facing producers. Yet, the focus of these interventions must keep the medium to long-term development of producer and consumer markets squarely in mind. Thus, subsidies to overcome current input and credit constraints at the producer level should attempt to augment and encourage private sector investment in input distribution, which may entail utilizing the private sector to distribute the subsidies. Another important dimension of this transition strategy is that the targeting of beneficiaries is specific and comprehensive enough to not displace private investment. While short-term investments aimed at stimulating growth may be necessary, these should not come at the expense of long-term investments in known drivers of agricultural growth and poverty reduction, including infrastructure improvements to ensure that farmers can lower their input costs and raise their share of output prices, investment in agricultural research, to develop the types of seeds and farming practices needed to respond to the vagaries of climate change, and
extension service to train farmers. Moreover, institutional strengthening will be needed to ensure that government actions in the markets are predictable, coherent, and line with long-term objectives.

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RE-MANUFACTURING ZIMBABWE: CONSTRAINTS AND OPPORTUNITIES IN A DOLLARIZED ECONOMY

I. COMPETITIVENESS AND CONSTRAINTS IN ZIMBABWEAN MANUFACTURING

Until the late 1990s, Zimbabwe was noted as having one of the most developed manufacturing sectors in Sub-Saharan Africa. Half of Zimbabwe’s GDP came from manufacturing, and its manufacturing base consisted of companies producing a wide array of products, from food-stuffs to steel. Manufacturing steadily declined after 1996. Changes in fiscal and monetary policies, including the policy of maintaining an overvalued official exchange rate, adopted from 1998 on, worked against domestic producers in favour of imports. The subsequent period of hyperinflation led to further deterioration of production capacity, leaving behind a sector that we observe today. Manufacturing now contributes less than 15 percent of GDP.

Despite the decline and some sectoral shifts, Zimbabwe continues to have a diversified manufacturing base, with businesses operating in low-skill, labor intensive industries such as apparel to sophisticated capital intensive industries such as steel manufacturing. The current landscape, however, shows a skewed distribution, with a negligible number of businesses that started in the last ten years, and a manufacturing sector, which has many small old firms mixed in with large old businesses. In the short-term, manufacturing reversal has to come about through changes in behavior of existing firms—the resilient firms that survived the downturn. Adjustment of these firms has to be complemented with policies that promote the entry of new firms—a process that faded after 1997.

The Enterprise survey of 2011 and the Competitiveness survey of 2012 indicate that constraints vary among firms. Top performers firms, which have the highest capacity utilization rates, have significantly higher labor productivity, and are larger than others. Firms in the top quartile are significantly more likely to rank electricity as a problem to capacity expansion, compared to other firms, and significantly less likely to rank access to finance as a constraint. These results suggest that policy interventions to spur growth of efficient businesses should be targeted towards improving the overall business environment, and infrastructure constraints in particular. On the other hand, businesses operating at low capacity are more constrained by lack of demand: they appear smaller and less productive than other firms. These firms are significantly more likely to report lack of demand as a major constraint to capacity expansion, and significantly less likely to report obsolete equipment as a problem. For these firms, a recapitalization fund is unlikely to boost capacity utilization; overall market conditions need to improve. While policies such as import duties may help increase demand conditions for these firms in the short-term, the lack of import competition would deter movements towards efficiency.
Zimbabwean workers are competitive regionally: Zimbabwe’s unit labor costs average 23 percent of value added, comparable to Kenya, and Namibia, and significantly lower than other countries, particularly South Africa.

However, capital is obsolete and will require substantial investments to rebuild. Almost three quarters of firms reported capital to be obsolete and requiring repairs. These figures are highest for firms in the capital-intensive heavy manufacturing and food processing sectors, indicating that increases in capacity utilization will require significant additional investments.

REASONS FOR NOT PRODUCING MORE. PERCENT OF FIRMS REPORTING EQUIPMENT PROBLEMS

But very few firms are making significant investments: The table below presents differences in investment rates across comparator countries. We see that only one-third of firms report any investments in 2010, and those that are investing report very little investment, averaging only 1 percent of sales. These rates are at least five times higher in other countries.

INVESTMENT CHARACTERISTICS: ZIMBABWE AND COMPARATORS

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<thead>
<tr>
<th></th>
<th>Zimbabwe</th>
<th>Botswana</th>
<th>Kenya</th>
<th>Mozambique</th>
<th>Namibia</th>
<th>South Africa</th>
<th>Zambia</th>
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</thead>
<tbody>
<tr>
<td>% of Firms Making</td>
<td>33 %</td>
<td>54 %</td>
<td>54 %</td>
<td>43 %</td>
<td>67 %</td>
<td>50 %</td>
<td>42 %</td>
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<tr>
<td>Investments</td>
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<tr>
<td>Average</td>
<td>1 %</td>
<td>8 %</td>
<td>5 %</td>
<td>7 %</td>
<td>5 %</td>
<td>8 %</td>
<td>6 %</td>
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<tr>
<td>Investment/Sales</td>
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<td>Ratio</td>
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Lack of Long-Term Finance is constraining business investment and growth. Differences in investment rates across countries could be related to supply and/or demand constraints. Firms with excess capacity are less likely to make new investments compared to others. Market uncertainty and lack of demand could also be driving differences in investment rates across firms. In addition, firms that are credit constrained cannot invest in new machinery and equipment. Access to long-term finance is one key factor limiting additional investments in capital stock.
Business Productivity is also adversely impacted by lack of short-term capital. Earlier studies on Zimbabwe noted the developed financial sector, and the prevalence of financial linkages through supplier and customer credit. However, changes in the macro environment have adversely affected availability of capital stock. As highlighted in the chart below, businesses now have much lower access to overdrafts and supplier credit. Small and Medium firms in particular have seen a sharp drop in access to short term capital.

Domestic Input Linkages have broken: A thriving industrial sector is supported by inter-industry linkages within the local economy. Historically, the UDI era compelled local businesses to develop domestic linkages, which remained strong through the 1990s. The World Bank RPED survey conducted during the 1990s showed less than one-third of businesses using imported raw materials, and the imported content was 15 percent of all raw materials. This has changed over time. More than half of manufacturing firms now report using imported raw materials, and the share of imported raw materials has increased to 29 percent. Noteworthy problems with domestic sourcing include lack of finance and unreliability of supplies.

Export decline has been fuelled by unreliable supplies to customers and inability to compete on price: The share of manufacturing output exported has fallen dramatically. The 1992 survey showed that more than a quarter of firms were exporters; the present survey shows that less than 10 percent of firms are now exporting any part of their output. Firms have been adversely impacted by both their inability to compete on price and to be able to supply products on time. More than two-thirds of firms noted these to be the most important reason for getting out of export markets; more than half of firms that reported inability to supply products on time also reported their inability to compete on price. There were no clear differences across sectors or size groups, indicating that the current environment is not conducive for export-led growth across the board.

**REASONS FOR NO LONGER EXPORTING: FIRMS THAT USED TO EXPORT**

- Couldn’t supply products on time: 74%
- Couldn’t compete on price: 68%
- Importers worried about reliability of supply: 68%
- Couldn’t compete on quality: 21%
- Trade policies of importing countries: 15%

Source: Competition Survey, 2011

Other reported constraints preventing moving into export markets are mainly financial: Almost half the firms that are currently non-exporters reported that they had either tried to export, or could export, if they had access to finance. The data show that businesses in Zimbabwe are not deterred by lack of knowledge of export markets or
importing country barriers. Thus, lack of short-term finance for exports is limiting export-led growth, especially for firms that could potentially compete globally.

There are other constraints, however. Electricity supply remains erratic, and imposes large costs on businesses. Businesses in Zimbabwe suffer the highest losses due to erratic power supply, compared to other countries regionally. Figure 9 below presents the reported average number of outages in a month, and the losses due to these outages across comparator countries. Estimated losses average almost 8.9 percent of total sales in Zimbabwe. Just reducing these costs would significantly increase competitiveness with imports, or ability to compete with lower prices in export markets.

Export and Import Delays add to business costs: Very few firms in Zimbabwe export; a vast majority of those that do report that their main export destination is within SADC; only 1 percent of firms reported exporting to the EU or USA. Reported export clearance times for firms ranged between 3-7 days, with an average of 4 days, which is high considering that most of the products are only being shipped to neighboring countries.

Uncertainty dominates all other constraints. Almost three quarters of businesses report uncertainty to be a major or severe constraint. It is the single biggest problem impacting businesses across the board. Without a stable macro-economic environment and a set of credible policies, no effort to improve the state of the manufacturing is likely to have any impact.

COSTS OF UNRELIABLE POWER SUPPLY

II. POLICY APPROACHES AND OPTIONS

The salient picture that emerges is that the manufacturing sector is dominated by aged firms that are a shrunken version of their former self (loss of size, capital, ability to export etc.). The years of turmoil have seen few new entrants into the sector, probably because of policies that not only made returns to trading, speculation and rent-seeking much higher than those of producing but also because uncertainty tipped the balance away from activities that required high investment in fixed assets. The sector thus has an older profile than is typically found in other economies.

Yet these very firms, the core of the existing sector, are ‘survivors’. They have somehow survived a massive crisis through a mixture of expedient management; use of old networks and other means. However, they are under huge stress. They operate in an uncertain policy environment, they are finance-constrained, their overhead costs are high, and domestic input supply is yet to revive. They are partly surviving now by shifting away from production towards trading imported goods with which they previously competed. Although it appears that these core firms remain competitive as far as labor costs are concerned (because of high labor productivity compared to labor costs), this is a precarious advantage. Not only is the labor force old with very limited new hiring, but also wages are rising fast.

At a macro-level, dollarization precludes short-term policy-induced increases in private credit growth. Therefore the focus is on microeconomic policies. One set of questions about policy approach relates to asking whether there should be activist/targeted policy for distressed firms or sub-sectors in the manufacturing sector or a non-targeted approach be taken to provide generalized benefits to all firms, current distressed and non-distressed, as well as firms yet to come. Another set of questions
relate to policy instruments. Should the government try to provide price advantage as through tariffs, or subsidize costs as through sharing political risk or subsidizing inputs such as electricity? The following discussion gets into the pros and cons of various approaches without getting into the details of specific policy prescriptions.

**Over the past three decades all statements of policy intent in Zimbabwe, as spelled out in numerous policy documents**, have been of the activist and targeted kind. Suggested policies rest on the assumption that explicit targeted interventions are required to revive Zimbabwe’s debilitated manufacturing sector. The Medium Term Plan, the Industrial Development Policy and the National Trade Policy spell out sectors to be supported. Actual policies used have included imposition of tariffs and establishing special funds to support distressed industries.

**However, protection-oriented policies may not be effective in today’s circumstances.** Particularly, providing price advantage to import-competing firms through tariffs may not be productive in the long run. The competition survey shows that import parity prices are on average 15 percent lower than the price of domestically produced goods. Therefore, theoretically a protection of about 15 percent would allow the import-competing firms to be competitive. While this has been the preferred approach of the government thus far, and is sought for by the distressed firms, such protection is likely to be counter-productive in the longer run. It creates incentives for firms to be inward looking. Most importantly it creates incentives for firms to keep producing goods that they should otherwise try to get out of if they are not competitive anymore. It can stifle innovation. While the government may think that the protection is only for a short period, once in place it is generally hard to unwind. Our results also indicate that inability to compete on prices is not uniform across all businesses. Efficient firms report supply constraints being the biggest bottleneck to output expansion; without addressing these constraints, price increase may not actually produce the expected supply response.

**So which options could the government pursue?** The three highest ranked business constraints identified in the survey were political uncertainty, access to finance, and electricity supply. While the survey dealt only with existing firms, it is likely that these constraints also act as a disincentive for new entrants. Tackling them is likely to do more to re-invigorate the manufacturing sector in a sustainable way than will more specific industrial policies. It may be argued that Zimbabwe should tackle these general problems as well as providing target support where needed. However, the tightness of the trade-offs in the current policy environment probably precludes this. Financial support from government to private firms almost certainly reduces resources available for infrastructural investment. Would industry in Bulawayo be better served by financial aid to selected firms or by investing a similar amount in tackling the city’s perennial water problems? Continued public investment in electricity and water upgrading is essential. Since this is likely to take some time before it results in improvements in supply, the government could think of ways to subsidize industrial use of electricity and water in the

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7 These statements are found not only in documents dealing explicitly with Industrial Policy (1999, 2004, and 2011) but also in the many other Plans and Policy Statements issued over the years.
interim period. This will essentially be a subsidy to compensate for the higher costs due to failure to ensure adequate and reliable supply of these essential services.

To increase export competitiveness, government policy and interventions should be aimed at enabling domestic firms to improve their technology, go out there and participate in regional production networks, and compete on price and quality in areas of their advantage. Foreign linkages have played an important role in Zimbabwe’s manufacturing. Our results show that-firms with ISO certifications, foreign licenses or some foreign ownership stakes survived the crisis and are more efficient than other firms, due to network advantages. In an overall environment of tight credit, promoting these linkages would help alleviate credit constraints and also provide firms with access to technological know-how and foreign markets.

On the issue of access to finance, the government may be in a position to share part of the political risk inherent in country risk premium, which is high for individual borrowers. Therefore, continuing to get sovereign credit lines and then on-lending to sound financial institutions, while allowing them to make decisions on which firms to lend in the manufacturing sector could be the preferred approach. The attempt to direct credit to sub-sectors or geographic regions in the country may not turn out to be productive.

Changes in the global value chains, regional markets, and the reality of the new agricultural sector and the new mining sector, point to the need to frame manufacturing development within the context of irreversibly changed global, regional, and national markets. Some support to the sector could help managing the consequences of an ongoing process of deindustrialization. However, it would be ill advised to limit support to industrialization through re-enactment of old protectionist measures. On the one hand, the cost and benefits of re-capitalizing a structurally regressing sector has to be carefully evaluated. The current low rate of return on investment (see Chapter 5) and rising level of non-performing loans in the banking system clearly raise the issue of the opportunity of focusing policy and scarce capital resources on raising productive capacity. On the other hand, supporting measures would need to be evaluated in the light of a dual track approach, in which prominence is given to forward looking re-industrialization, by rebuilding domestic linkages with the mining and agricultural sectors and by fostering re-integration in global and regional markets.

Medium-term potential for growth in manufacturing will be affected by the pace of mining and agricultural growth, and the capacity to rebuild linkages with these autonomous drivers of growth. Unlocking Zimbabwe’s potential for investment in mining is bound to have significant downstream positive effect on manufacturing, provided the necessary improvement of the overall business climate is also realized.
SECCTORAL AND INSTITUTIONAL CONTEXT

1. Prior to the decade-long crisis, Zimbabwe had a very robust and competitive base for private sector development largely on account of the substantial investments made in human capital and infrastructure after independence in 1980. In the last decade, most private firms lost their competitiveness, many closed, downsized, or lost productive capacity, due to decay of capital and loss of working capital. The 2009 stabilization has somewhat reversed the trend. However, many firms are still battling with low investment, high operating environment costs, and limited access to finance. While the majority of firms have downsized and investment is still down, within the region the human capital base of Zimbabwe is still relatively sound and infrastructure is relatively decent in comparison with some of its African neighbors. With the right business environment, the private sector in Zimbabwe would be able to recover its leading role in growth.

2. The World Bank has undertaken analytical and Technical Assistance activities in recent years including the 2011 Zimbabwe Enterprise Survey, the 2011 Zimbabwe Finscope Financial Consumer Survey and more recently the 2012 Finscope MSME Survey. In addition, the World Bank also produced the Zimbabwe Growth Recovery Notes series which included specific notes in (a) Agriculture; (b) Manufacturing; (c) Mining and (d) Investment Finance.

3. The work undertaken reveals a deeply changed Zimbabwean economic structure with MSMEs and small holder farmers taking a more prominent role and supply response. The Zimbabwe Growth Recovery Notes highlight this fact and go on to state that the Zimbabwean economy still remains highly differentiated compared to other African economies and that there is a broad based potential for recovery in all sectors including agriculture, manufacturing and services. The notes identify mining and agriculture as the two sectors capable of growth which could drive the rest of the economy including the manufacturing sector. A competiveness gap has also been identified as growing due to the appreciation of the real exchange rate shifting the price structure against tradable products. While dollarization precludes an independent exchange rate policy, an appropriate policy response would be to focus on sound fiscal policies, public wages moderation and support to increased productivity in the private sector.

4. Improving the Investment Climate. In 2013, Zimbabwe ranked 172nd out of 185 countries in the World Bank/IFC Doing Business rankings (significantly behind the Sub-Saharan Africa average of 140). Dealing with construction permits, resolving
insolvency, trading across borders, getting electricity and starting a business were Zimbabwe’s worst Doing Business indicators, all significantly below the Sub-Saharan average and also below regional comparators. Key rule of law based indicators such as enforcing contracts and protecting investors are equally low and need to be improved.

**Doing Business 2013: How Zimbabwe compares regionally**

<table>
<thead>
<tr>
<th></th>
<th>Ease of Doing Business Ranking</th>
<th>Starting a Business</th>
<th>Dealing with Construction Permits</th>
<th>Getting Electricity</th>
<th>Registering Property</th>
<th>Getting Credit</th>
<th>Protecting Investors</th>
<th>Paying Taxes</th>
<th>Trading Across Borders</th>
<th>Enforcing Contracts</th>
<th>Resolving Insolvency</th>
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<tr>
<td>Zimbabwe</td>
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<td>South Africa</td>
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6. The 2011 World Bank Enterprise Survey for Zimbabwe captures the experiences of businesses currently operating in the country and identifies political instability, access to finance, electricity, competition from informal sector and tax rates as the top five problems for enterprises.

**Business constraints—percentage of firms ranking problem to be major or severe**

![Percent of Firms ranking problem to be major or severe](image)


7. It is necessary to further explore leveraging international trade to deepen the recovery. Zimbabwe’s exports have become more resource- than labor-intensive and are concentrated in primary products with little processing. While there is a relative high demand for capital-intensive mining activities, there is little development around
industries that could take full advantage of the relative abundance of skilled and unskilled labor in Zimbabwe, with a positive impact on employment and poverty. Future growth prospects would substantially improve with a strategy of openness and overcoming structural constraints to export diversification and sustained growth, e.g., by improving Zimbabwe’s trade facilitation agenda, reducing nontariff barriers, improving the business environment and supportive institutions, and facilitating partnering of domestic and international investors with a view of accessing global value chains.

8. **Efficient financial intermediation and increased access to finance is necessary to address capital decay, limited working capital and economic growth.** The current high real interest rates and unavailability of longer term credit is a major hindrance to economic recovery. On the demand side, data indicates that lending institutions nearly doubled their loan-to-deposit ratio over the past two/three years resulting in an increase in non-performing loans. From a supply side point of view, financial institutions have been obtaining most of their funding from the deposits of domestic savers, resulting in only short term credit being available. As this source of financing is becoming exhausted, as evidenced by its current account deficit which was 36 percent of GDP in 2011, Zimbabwe has become increasingly reliant on foreign sources of capital. On financial inclusion, the 2011 Zimbabwe Finscope Consumer Survey showed that 38% of adults in Zimbabwe are formally served (including both banked and other formal bank products/services). Although this is ahead of other countries such as Zambia (23 percent), Tanzania (16 percent), Mozambique (13 percent) and Rwanda (21 percent), it is still significantly behind South Africa (67 percent), Namibia (65 percent), Swaziland (50 percent) and Botswana (59 percent).

9. **Infrastructure remains a significant binding constraint to private sector growth in Zimbabwe.** In 2012, the World Bank, with funding from the Public Private Infrastructure Advisory Facility (PPIAF) Trust Fund carried out a PPP Rapid Needs Assessment (RNA) for Zimbabwe. The report recommended that the PPP process proceed to work in parallel in two areas: (a) strengthening the legal and institutional environment for PPPs and; (b) support the government on work in preparation of particular PPP pipeline deals. This would facilitate stronger government commitment to the PPP agenda and ensure benefits of learning by doing. Under legal and institutional reforms, it was recommended to provide support in this area by (i) providing assistance for drafting of the PPP Act, (ii) providing advice on establishing a PPP Unit (these two actions would serve as a base to start a meaningful transformation process for the Zimbabwe PPP framework) and (iii) further revision of sector regulations which would be necessary in order to ensure a smooth implementation of reforms supporting PPPs. Under (b) support the government on work in preparation of particular PPP pipeline deals, given the lack of a proper regulatory framework, it was recognized that the selection and implementation of projects might only be viable at a later stage. The two
areas of recommendations summarized above would be considered within the context of the transition that Zimbabwe is currently undergoing including the need to highlight the importance and impact of the Indigenization Act on PPPs.

11. **The 2012 Growth Notes highlight agriculture as one the two sectors (the other being mining) in Zimbabwe capable of growth which could drive the rest of the economy including the manufacturing sector.** Agribusiness is the main link between the agriculture and manufacturing sectors. Key activities for strengthening this link include (i) assessing market channels for agriculture value chain partners; ii) working with suitable domestic and multinational corporations to encourage business linkages with SMEs and smallholder farmers; iii) implementing customized training for small holder farmers and SMEs and iv) developing value chain linkages. The World Bank Group led by the IFC has been focusing on supporting agribusiness through its Sustainable Business Advisory (SBA) tool to provide business and technical standards knowledge that enables SMEs and smallholder farmers to competitively access existing market channels and inputs including financing through a corporate value chain approach.

**CONSTRAINTS/CHALLENGES**

9. **Policy inconsistencies:** The private sector has not been given ample opportunity to flourish. Private initiative has been consistently stifled by policies aimed at steering the economy in a central fashion, backed by policy inconsistency and uncertainty over regulations and taxation levels.

10. **Land Tenure:** Financing of the agricultural sector is largely curtailed by the lack of secure tenure for the current owners. It is advisable that the new government quickens the issuing of secure tenure for the land to enable both institutional and individual investment on the land.

11. **Limited domestic resources:** The revenue base (targeted at US$3.8bn for 2013) does not allow for the provision of the necessary levels of finance for socio-economic investment. At the same time, fiscal resources are already absorbed by mostly wages (67 percent of monthly revenue) thus crowding out necessary spending.

13. **Integration with the Global Economy:** Stronger growth will be facilitated with efforts to more strongly integrate the Zimbabwean economy into the global and regional markets. GoZ will need to immediately re-establish links with the international community and get sanctions removed so that the country can move on again. This move should spur the unlocking of international capital. Policies to foster increased access to international capital, and stronger domestic levels of investment should be pursued with vigor.
POLICY OPTIONS

14. **Improving the Investment Climate.** Economic recovery however critically depends on an environment conducive to private sector activity, including recovery of both domestic and international investment. In the short term, the Government needs to resolve the uncertainties caused by the Indigenization Act, which is stunting levels of domestic and foreign investment. The application of the Indigenization and Empowerment policy needs to be clarified, and applied in a manner consistent with the broader objectives of increase investment and growth. It is also important that Zimbabwe its Investment Climate reforms on key Doing Business indicators where its performing worst and the key rule of law indicators such as enforcing contracts and protecting investors. The World Bank Group’s Investment Climate Team is ready to assist and has already signed a MoU with the Ministry of Economic Planning and Investment Promotion and the Ministry of Small and Medium Enterprises and Cooperatives Development.

15. **Financial Sector Development:** In view of the importance of developing resilience and greater financial intermediation in the financial sector, we recommend Zimbabwe undertakes a Financial Sector Assessment Program (FSAP) whose findings and recommendations could form the basis for a Financial Sector Development Strategy and program.

16. **Public Private Partnerships (PPPs).** The new government of Zimbabwe should engage the private sector in developing much needed infrastructure, power generation and water sector, PPPs can assist the financially constrained GoZ to mobilize private capital for the delivery of public goods and services that are much needed at the moment. The recommendations the 2012 Zimbabwe PPP RNA report could form a good basis for moving forward.

17. **Agricultural Value Chain Approach:** Resuscitation of Agriculture through a value chain work spearheaded by Ministry of Industry and Commerce working closely with key players such as the Ministry of Agriculture and the private sector would drive agriculture productivity through eliminating inefficiencies and developing market linkages with national, regional and international markets.
SITUATIONAL ANALYSIS

1. **The public service wage bill in Zimbabwe is high by regional and international standards.** Employment costs are now at the unsustainable level of 67 percent of total expenditures, crowding out essential expenditures on services and the capital budget, so necessary to creating the fiscal space for recovery. As Figure 1 below illustrates, Zimbabwe stands out as the second highest in terms of public service wage bill as a share of GDP in Sub-Saharan Africa. The wage bill in 2011 rose to 17 percent of GDP, significantly higher than the regional mean of 7.3 percent. It is more striking to put the Zimbabwe wage bill situation in a dynamic perspective: the share of GDP spent on public service wages and salaries went from 8.4 percent of GDP in 2009 to 12.7 percent in 2010, 17 percent in 2011 and 22 percent in 2012.

![Figure 1: Cross-country Public Service Wage Bill Comparison, 2011 (% of GDP)](image)

Source: IMF.

2. **The wage bill increased progressively in recent years, making Zimbabwe an outlier in the region and the world.** Employment costs increased by almost 50 percent of budget outturn in 2010 to 70 percent in 2012, while non-wage expenditures have been declining. Of the remaining 30 percent of total current expenditures, operational costs
accounted for 20 percent and capital expenditure for 10 percent. With the 2013 wage adjustment factored in, the overall public sector wage bill was projected to increase to US$2.645 billion, representing 67 percent of total expenditure in 2013.

3. The actual fiscal burden of employment costs appears under-estimated, as a significant number of senior public servants have access to supplementary indirect allowances (e.g. petrol, travel allowances) and in-kind benefits (e.g. vehicles) on top of their regular pay, drawn from other budget line items. In addition, as part of the total public service compensation package, Zimbabwe spends 4.1 percent of GDP on public service pensions, accounting for more than a quarter of the total wage bill.

4. At the same time, public servants’ compensation has been continuously eroded. Despite the fact that 70% of domestic revenues are earmarked for wages and salaries, public servants’ salaries remain low and, at the lower grades, do not present a “living wage”. Low wages have forced public servants to adopt a number of coping strategies such as (i) not turning up for work or not working a full day; (ii) taking on a second job; (iii) joining the informal economy; and (iv) migrating. Wages are, therefore, inextricably linked to productivity and performance.

5. As fiscal revenues are projected to stagnate in 2014, any further increase of the wage-bill beyond cost-of-living compensation would lead to compromising government’s capacity to finance expenditures necessary for the socio-economic recovery, and fuel fiscal unsustainability. It is advisable to adopt a medium-term approach to reform of civil-servants compensation.

CONSTRAINTS AND CHALLENGES

6. World wide experience in public service reforms in general, and wage bills management in particular, all point to the fundamental challenges on political, analytical, and technical fronts. The stickiness of the problem is structural, requiring longer-term solutions. The problem cannot be solved in isolation from the planning and budgeting processes, as well as relevant public policies aimed at enhancing the environment for private sector development. A recent review of the African civil services\(^8\) indicates that a number of countries have been subjected to perpetual rounds of reforms and such reforms in many cases have aggravated problems. The public service is increasingly becoming an unbearable burden on the budget, while in other countries, governments have lost the capacity to pay for a high quality public service due in part to the poverty of their economies, the structure of politics and administration, globalization, and wrong-headed reform programs (Civil Service Pay Reforms in Africa, December 2010).

7. The Government of Zimbabwe has recognized the importance of wage bill management and the urgent need to correct the unsustainable path on which it has been heading. This requires actions to be taken in both the short- and medium-terms. Apart from short-term measures of control, effective solutions to contain the wage bill will require decisions and actions with a medium- to long-term time frame, strong leadership from both trade unions and the political directorate, and a willingness to collaborate in forging strategies and policies with medium- to long-term targeted results. As noted in the January 2013 Aide Memoire, meaningful and sustained change calls for several ingredients, such as: (a) strong and clear ownership at the level of Ministers and the Chief Secretary; (b) a shared vision and acknowledgement that the status quo is not viable; (c) a genuine process of consultation and inclusion; and (d) evidence-based decision-making.

8. However, reforms should not be undertaken without proper and detailed assessment and analysis of the situation to fill the knowledge gaps and plan ahead the medium- to long-term reform agenda. It is critical that the Government develop a thorough understanding of the impact of various options to manage the wage bill on staffing and the budget. Detailed and sound analysis of salary packages, in-kind benefits and incentives, travel costs, and other direct or indirect expenditures, as well as pension payments and adjustments to the employment levels, should precede any policy intervention. Special care should be taken to fully evaluate reforms that potentially create future liabilities.

Going forward, the challenge facing policy makers is two-fold: (1) to devise a credible mechanism and institutional arrangements to monitor wage bill outturns per ministry, semi-autonomous agencies and parastatals, as well as the wage composition; and (2) elaborate options to connect the issues of wage bill and performance in a practical way.

OPTIONS

9. The size of the wage bill calls for prompt action. Low-hanging fruit are few however, and meaningful reforms are likely to be longer-term in nature. It is important that the Government and Unions engage in a joint exercise to build the analytical underpinnings and further explore feasible reform options, in coordination with options for reform for the public service pension scheme. These should, ideally, be elaborated in a medium-term roadmap towards wage adequacy and a sustainable wage bill based on scenarios for the performance of the economy. The draft Issues and Options paper prepared by the Bank (January 2013) presents a set of major issues to discuss in

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9 For more details on pension system, see Social Protection Policy Note.
identifying the policy options on the way forward:

- How can the Government (1) ensure effective wage bill control and (2) modernize the HR and payroll system?
- What are the best methods to (3) improve the conditions of service and (4) enhance performance and productivity of the public service to maintain a competent, motivated and results-focused work force?
- How can (5) the current institutional setup be strengthened?
- And lastly, how can (6) Government and unions forge a social compact with a view to giving public servants a living wage while achieving a sustainable wage bill in the medium-term based on an evidence-based approach?

10. **Some specific policy interventions** to be considered **over the short-medium terms include:**

- Developing a clear-sighted understanding of issues and options for effective containment of the employment costs in line with expected fiscal framework.
- Establish Guiding Principles for a collective and inclusive process, which all major stakeholders could agree on and be committed to.
- Further constructing database and data mining/analysis aimed gaining a comprehensive understanding of the present situation, obtain relevant benchmark indicators, and model the impact of various HR and pay and pension reform options under different growth scenarios. As part of the strategy, a comprehensive set of salary surveys for public-private and regional benchmarks will be a critical follow-on to the payroll audit survey already completed.
- Define policy options that lay out effective measures to control the public sector wage bill over the medium- and long term in conjunction with modernizing the institutional setting and incentives and improving the conditions of service to enhanced staff performance and productivity. (Timeframe: Progressive within FY2014-2015.)
- Introducing an HR Management Information Service linked to the IFMIS system to ensure adequate financial management control over the payroll.
I. SITUATIONAL ANALYSIS

1. The 2011 Enterprise Survey indicated that businesses in Zimbabwe suffer the highest losses due to erratic power supply, compared to other countries regionally. Estimated losses average almost 8.9 percent of total sales in Zimbabwe. Just reducing these losses would significantly increase. Overall, increasing the efficiency of service delivery by parastatals is a key factor in restoring firms’ competitiveness.

2. Since the government of Zimbabwe embarked on a successful stabilization plan to eradicate hyperinflation, parastatals and local authorities that provide infrastructure services have been under pressure to improve efficiency. Between 2009 and 2012, parastatals in electricity, railways and water increased sales, but those in ICT reduced revenues (e.g. TelOne lost revenue in the fixed communications business while NetOne lost share to competitors).

CAPACITY CONSTRAINTS

3. But they operate in a context of significant capacity constraints. ZESA generation capacity is limited with transmission and distribution networks being obsolete (only minor investments have been done during these years), while at the Department of Harare Water (DHW), production and treatment capacity has remained constrained.

4. There are significant losses in the distribution network; NRZ’s infrastructure is too old (only some investments in railways and refurbishment of rolling stocks have been exerted during these years); ICT parastatals need capitalization either to face competition in a dynamic market or to replace old infrastructure. In the energy sector, challenges on the operating side include the improvement of operational efficiency, cost reduction (including reducing losses, the target of non-technical losses is 3%). At a general level, they lack of capacity to meet demand (the sector faces a constraint to get electricity from neighbor countries), they have weak financial performance, infrastructure is obsolete and still subject to vandalism, and needs rehabilitation, refurbishment and modernization.

REVENUES

5. Improving collection ratios continues being a challenge for those infrastructure parastatals with post-paid revenues, e.g., ZINWA, DHW and TelOne. NetOne

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revenues are mostly prepaid; ZETDC improved collection ratios significantly, through disconnections and innovative incentive schemes.

| Infrastructure Parastatals collection ratios (cash revenue / accrual revenue) |
|-----------------------------|--------|--------|--------|
|                            | 2009   | 2011   | 2012   |
| ZESA                       | 53%    | 91%    | 105%   |
| ZINWA                      | 22%    | 40%    | 57%    |
| NetOne                     |        | 95%    |        |
| (post paid)                | 44%    | 76%    | 81%    |
| TelOne                     | 33%    | 68%    | 69%    |

| Infrastructure Parastatals profits (in million of dollars) |
|---------------|--------|--------|--------|
|               | 2009   | 2010   | 2011   | 2012   |
| ZESA          | -174   | -95    | -55    | 7      |
| ZINWA         | -3     | -3     | 2      | 3      |
| NRZ */*       | -53    | -37    | -50    | -37    |
| NetOne        | 8      | -14    | -8     | -2     |
| TelOne        | -25    | -35    | -19    | -5     |

6. **If collections were 100%, actual tariffs levels would cover operational costs but typically they are not enough to pay for capital costs.** In the electricity sector, there was a 50% tariff increase in 2011. The increase in collections would allow ZETDC to generate a surplus that could be used to improve infrastructure. In other sectors, there have not been tariff reviews (in railways and petroleum sectors, prices are set freely). For DHW, tariffs are lower than economic costs, even after having increased and rebalanced in 2011.

7. **Some components of costs increased significantly between 2009 and 2012, specifically labor costs:** NetOne average labor costs are higher than other parastatals and have increased in real terms. For example, compared with a cumulative inflation of 10% observed since 2009, labor costs at Netone increased by 77%, more than doubled at TelOne and NRZ, and increased more than 150% at ZETDC. As a result, the ratio of labor costs to revenues has increased over time.

<table>
<thead>
<tr>
<th>Number of Employees</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>ZESA</td>
<td>4,208</td>
<td>4,023</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Plant + Contracts)</td>
<td>5,808</td>
<td>5,623</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ZINWA</td>
<td>2,429</td>
<td>2,523</td>
<td>2,502</td>
<td>2,494</td>
</tr>
<tr>
<td>NRZ</td>
<td>8,648</td>
<td>8,646</td>
<td>8,021</td>
<td>7,799</td>
</tr>
<tr>
<td>NetOne</td>
<td>288</td>
<td>331</td>
<td>349</td>
<td>373</td>
</tr>
<tr>
<td>TelOne</td>
<td>2,453</td>
<td>2,453</td>
<td>2,453</td>
<td>2,318</td>
</tr>
</tbody>
</table>
### Average Labor Cost (Labor cost / personnel)

<table>
<thead>
<tr>
<th></th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>ZESA</td>
<td>9,061</td>
<td>12,599</td>
<td>19,601</td>
<td>23,767</td>
</tr>
<tr>
<td>ZINWA</td>
<td>7,624</td>
<td>9,085</td>
<td>8,965</td>
<td>9,824</td>
</tr>
<tr>
<td>NRZ</td>
<td>5,069</td>
<td>7,009</td>
<td>10,209</td>
<td>10,473</td>
</tr>
<tr>
<td>NetOne</td>
<td>34,915</td>
<td>56,492</td>
<td>63,436</td>
<td>61,927</td>
</tr>
<tr>
<td>TelOne</td>
<td>11,000</td>
<td>18,068</td>
<td>21,784</td>
<td>23,301</td>
</tr>
</tbody>
</table>

Notes: *1/ Staff cost / total employees (2009 and 2010: assuming same number of employees as in 2011, i.e., 5,808); *2/ Staff cost / number of employees as stated by NetOne.

### Ratio of Labor Cost to Revenues

<table>
<thead>
<tr>
<th></th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>ZESA</td>
<td>11%</td>
<td>13%</td>
<td>17%</td>
<td>16%</td>
</tr>
<tr>
<td>ZINWA</td>
<td>42%</td>
<td>42%</td>
<td>40%</td>
<td>46%</td>
</tr>
<tr>
<td>NRZ</td>
<td>68%</td>
<td>64%</td>
<td>81%</td>
<td>79%</td>
</tr>
<tr>
<td>NetOne</td>
<td>10%</td>
<td>24%</td>
<td>23%</td>
<td>26%</td>
</tr>
<tr>
<td>TelOne</td>
<td>12%</td>
<td>25%</td>
<td>36%</td>
<td>39%</td>
</tr>
</tbody>
</table>

Source: financial statements and complementary information provided by parastatals.

8. Wage-costs increases and the differences in the level of average labor costs are significant: the level range from more than US$60,000 per employee per year in the case of NetOne (which represents 26 percent of revenues), over US$23,000 in TelOne (39 percent of revenues) and ZESA (16 percent, but this is only ZETDC) and about US$ 10,000 in NRZ (79 percent of revenues) and ZINWA (46 percent of revenues).

There is some evidence of inefficiency in this dimension: the net result of the evolution of sales and labor costs is an increase in the labor cost-to-revenue ratios in 27 percent for TelOne (recall the reduction in sales), 16 percent for NetOne, 11 percent for NRZ and 4-5 percent for ZESA and ZINWA.

9. Parastatals carry significant web of arrears (both payable and receivable), not only inter-parastatal and with government but also with the private sector.

10. Although there are cross-arrears among public agencies and with the government, most arrears are held by private parties (both families and business). Notwithstanding, public debtors - either parastatals or government– increased their share in total debtors through time, due to cumulative unpaid debts: currently, they range from 8 percent (NetOne) to 46 percent (ZINWA and TelOne).

Similarly, a higher share of the parastatals’ credit is owed to the private sector,

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12 In 2009, the only significant case was NRZ. The ratio of state trade debtors to total debtors was 36 percent (quite similar to the current ratio).
although the share of public creditors also increased in time. In this case, it is worth to notice that ZESA’s import arrears reduced significantly from the past, to US$22 million. This could be done with assistance from advance payments by clients.

II. POLICY OPTIONS

a. Define Medium Term Strategies

*Electricity Sector*

11. The government should consider elaborating a medium-term strategy for rehabilitation and expansion of power infrastructure. ZESA could lead this effort, and in this case should options for strategic partnerships should be delineated. Alternatively, the expansion could be elaborate through independent players, in which case the Government should delineate licensing provisions that enhance business climate to potential investors in generation, transmission, and distribution, establish interconnection rules. Under the option of the government retaining full control of parastatals, it is imperative to assess the alternative of opening the room for private participation through the subsidiaries.

*Railways Sector*

12. NRZ’s ability to improve revenues depends on the ability to set rates, which is conditioned by road transportation, and demand, which is conditioned on the evolution of customers’ activity. A coordination of intermodal transportation could help on the feasibility of NRZ to increase rates, but demand issues will depend on the capacity of main clients (e.g., Hwange Colliery and Zimasco) to expand production. For the mid-term, the government should start a full revision of planning and restructuring, including a regulatory framework for railways that delimits roles between the Minister, the regulatory agency, and operators (including NRZ), the role of NRZ in the sector (infrastructure manager or operator), and the role of the private sector (as strategic partner of NRZ or as independent player)

*Water and Sanitation*

13. Medium-term strategies should address investment needs to tackle the lack of capacity in production, distribution and treatment to meet demand. Available funds should be assigned to prioritized projects (e.g., reducing non-revenue water versus increasing supply).

*ICT*

14. In the medium-term, assess the role of parastatals in the ICT sector. This may involve privatization or strategic partnership. Under the option of the government retaining full control on parastatals, the government can assess the alternative of divesting

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13 TelOne faces problems collecting from the government but also from individuals and SMEs. It is also worth to mention that this company wrote off debts by domestic users, but could not write off credits from interconnecting companies for the corresponding accounts. Currently this is a judicial issue under discussion.
TelOne into subsidiaries, and open the room for private participation through subsidiaries.

b. Improving Regulation of Infrastructure

15. Improved regulation of parastatals could support increasing operational efficiency. The 2010 and 2012 notes provided the following priority recommendations, (i) separation of ownership and regulatory functions in different authorities, avoiding vertical or horizontal relationships among them; (ii) creation of a Regulatory Agency in sectors other than energy and ICT (e.g., railways, water, etc.); (iii) capacity building in ZERA and other agencies; (iv) independence—both political and financial—of regulatory authorities (this includes a transparent rule–public contest procedure— for appointment of board members among qualified applicants, rather than involving stakeholders in the selection); and (v) the merger of POTRAZ and BAZ. In the area or general regulation, it is advisable to (vi) unify regulation in road and railways, and delineate a regulatory framework in water and sanitation. These recommendations will help providing a level playing field for public and private sector players and efficient provision and control.

16. In the water and sanitation sector government should consider delineating regulatory framework with relevant dimensions such as (i) unification of acts (a single Water Act vs. multiple acts), (ii) the figure of the regulator (multi-sector vs. single-sector regulator, regulator within the government, centralized vs. decentralized regulator and provision that is standard practice in many countries), (iii) the figure of the service provider (which not necessarily is an autonomous parastatal), and (iv) the configuration of the coordination of water activities (separation or coordination of water resources management and water supply by ZINWA).

c. Tariffs Review

17. Tariffs should reflect incremental costs of services, subject to cost and demand conditions and profitability constraints. To pursue goals different from efficiency, regulators implement low-consumption and/or access schemes financed with direct subsidies or cross-subsidies. A thorough evaluation of the cost structure and tariffs in key parastatals is necessary. Based on that, in the medium-term the government should consider the merits of a full tariff review under efficient provision of electricity and operation of the system, including the peak/ off peak price relationship for large users, and a reassessment of the decision regarding the fixed price. An important task in the electricity sector is to assess the long run cost of electricity under efficient provision of electricity and operation of the grid. The review should also be accompanied by inclusive-oriented policies (lifeline tariffs for low-income users), a reassessment of the decision regarding the fixed charge, and consumer education / guidance (improve electricity saving through demand side management).

18. In the water sector, tariffs appear to be sub-economic, and even more if collection problems are taken into account. Municipalities spend little on essential fixed assets and their asset registers are generally in poor state, with values recorded at
depreciated historical costs rather than replacement value. A tariff review\textsuperscript{14}, including both clear and raw water is advisable in the short term, while in the medium term a more efficiency-based performance-oriented mechanism should be envisaged.

\textsuperscript{14} Detailed recommendations are expressed in the 2011 Zimbabwe Urban Water Tariff Study
INDIGENIZATION POLICY AND ECONOMIC LINKAGES: CHALLENGES AND TRADE-OFFS

BACKGROUND

1. The Government of Zimbabwe first put in place a “Policy Framework on the Indigenization of the Economy” in February 1998. The policy was revised in October, 2004 and adopted by Cabinet as the “Revised Policy Framework for the Indigenization of the Economy.” The indigenization policy framework provided for the formulation of the IEE legislation, culminating into the enactment of the Indigenization and Economic Empowerment Act (Chapter 14:33), March, 2008. The main objective of this Act is outlined in section 3 as “to endeavor to secure that at least 51 percent of the shares of every public company and any other business shall be owned by indigenous Zimbabweans.” To facilitate the implementation of the Act, the GoZ promulgated the Indigenization and Economic Empowerment (General) Regulations in February, 2010 through SI 21 of the same year and as amended as at 25th March 2011. The Regulations provide that all businesses with a net asset value equal to or above US$500 000 located in Zimbabwe should formulate plans that will lead to 51 percent of the shares in the firm being transferred to “indigenous” Zimbabwean shareholders within five years from the date of operation of the regulations. The IEE defines empowerment as, the “creation of an environment which enhances the performance of the economic activities of indigenous Zimbabweans into which they would have been introduced or involved through indigenization”.

2. The Indigenization and Economic Empowerment Act (IEEA) of 2008 defines indigenization as “a deliberate involvement of indigenous Zimbabweans in the economic activities of the country, to which hitherto they had no access, so as to ensure the equitable ownership of the nation’s resources”. It further defines an ‘indigenous Zimbabwean’ as “any person who, before the 18th April, 1980, was disadvantaged by unfair discrimination on the grounds of his or her race, and any descendant of such person, and includes any company, association, syndicate or partnership of which indigenous Zimbabweans form the majority of the members or hold the controlling interest.”

3. Plans for detailed implementation of the legislation have not yet been clarified.
SITUATIONAL ANALYSIS

*The Existing anti-investment bias has been stunting domestic investment*

4. Despite the economic rebound, domestic investment in Zimbabwe remains at levels lower than predicted by prevailing levels of financial development and institutional quality and has not yet scratched the surface of addressing the capital stock deterioration that occurred during the crisis.

5. **Large shocks create considerable uncertainty about variables that affect the decision to invest and even after stabilization it takes time before investors revise expectations significantly.** This inertia effect may partly explain the low levels of investment seen during the Zimbabwe recovery. On the other hand, investors may remain uncertain about future political stability and policy frameworks. Alesina and Perotti (1993) show that investment is adversely affected by anticipated rapid political changes and even more so when such changes are expected to affect the basic “rules of the game” (tax laws, property rights) and raises risks of expropriation, which is the case in Zimbabwe. Such an effect is not directly caused by any idiosyncratic risk aversion by firms. Serven (1997) shows that uncertainty becomes a powerful deterrent to investment even with risk-neutral firms, as larger spread of the distribution of future returns from investment raises the probability of negative outcomes of investment, resulting in a higher level of marginal productivity of capital determining the decision to invest. The overall result is a bias against investment.

6. **There are serious concerns about the availability of financial capital to support investment, both in terms of debt and equity.** Zimbabwean brokerage firm Invictus Securities estimates in its report, “Mid-Year Equities Market Review” (August 2012), that companies listed on the ZSE require US$1 billion in equity to fully recapitalize and renew their depreciated asset base. However, there has been no IPO since dollarization, and only a limited number of seasoned equity offerings, consisting mostly of rights issues and a handful of private placements and convertible loans.

7. **Stronger policies and institutions could lead to a substantial recovery of investment.** Lim and Pommerenke (2012), deploying scenario analyses, estimate that if Zimbabwe were able to significantly accelerate her rate of financial development and institutional advancement, she could substantially jump-start investment in the country, translating into total investment levels that are between 21 percent and 69 percent higher than would be the case in a benchmark scenario.

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FDI Levels are Subdued

8. **FDI levels have remained subdued and medium-term recovery will hinge on higher levels of FDI.** FDI is however most commonly associated with larger domestic investment and higher productivity from spillovers, more than overall increased availability of credit in the economy.

9. **Foreign sources of capital have become increasingly difficult to access, due to the indigenization law and uncertainty about its implementation.** The reliance of the banking system on domestic savers is especially acute for commercial banks (at 63.8 percent), especially since many of these banks cannot draw on foreign parent banks to meet their loan financing needs.

10. **Linkages from FDI:** Estimations from a meta-analysis of 47 countries by Havranek and Irsova (2010), suggest that a 10-percentage-point increase in foreign presence is associated with a 11 percent larger productivity of domestic firms in supplier sectors, implying in the case of Zimbabwe that FDI in the manufacturing sector would present important (backward) spillover effects and stronger productivity in the agricultural sector. The same body of research suggests that forward spillovers (to client sectors) and horizontal spillovers (in the same sector) would be of limited economic importance. In addition, fewer spillovers are generated by fully owned foreign affiliates compared with joint ventures.
Firm Ownership has changed, and Foreign Ownership has declined\textsuperscript{16}

11. Indigenization policies of the government played a significant role in deterring new foreign investment in Zimbabwe after 1996. However, Zimbabwe already had a large base of multinationals, many of which had been established prior to independence. How did the ownership change after 1992?

12. The table below compares 1992 RPED survey data to compare business ownership in Zimbabwe in 1992 to ownership of businesses today. A greater share of manufacturing firms has some foreign ownership, indicating that foreign firms were better able to withstand the downturn, relative to locally owned enterprises. However, only 3 percent of firms are now majority foreign owned, indicating dilution of foreign stake. These results hold for all sizes of firms.

### FOREIGN OWNERSHIP SHARES: 1992 VERSUS 2011

<table>
<thead>
<tr>
<th></th>
<th>1992</th>
<th></th>
<th>2011</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>% with some foreign ownership</td>
<td>percent of firms Majority Foreign Ownership shares</td>
<td>% with some foreign ownership</td>
<td>percent of firms with Majority Foreign Ownership</td>
</tr>
<tr>
<td>Overall</td>
<td>16 percent</td>
<td>10 percent</td>
<td>20 percent</td>
<td>3 percent</td>
</tr>
<tr>
<td>Small</td>
<td>5 percent</td>
<td>2 percent</td>
<td>10 percent</td>
<td>1 percent</td>
</tr>
<tr>
<td>Medium</td>
<td>8 percent</td>
<td>8 percent</td>
<td>17 percent</td>
<td>3 percent</td>
</tr>
<tr>
<td>Large</td>
<td>31 percent</td>
<td>20 percent</td>
<td>31 percent</td>
<td>5 percent</td>
</tr>
<tr>
<td>Very Large</td>
<td>26 percent</td>
<td>14 percent</td>
<td>43 percent</td>
<td>7 percent</td>
</tr>
</tbody>
</table>

13. Firms with some foreign ownership continue to be the largest employers within manufacturing. Median size of these firms is 108 workers, compared to an average of 30 workers for fully locally owned firms. Foreign owned firms have higher productivity compared to local enterprises-this is mainly due to access to foreign technology (68 percent of foreign firms have ISO certification, compared to 24 percent of local businesses) and access to short term capital.

14. Foreign linkages have played an important role in Zimbabwe’s manufacturing. Our results show that-firms with ISO certifications, foreign licenses or some foreign ownership stakes survived the crisis and are more efficient than other firms, due to network advantages. In an overall environment of tight credit, promoting these linkages would help alleviate credit constraints and also provide firms with access to technological know-how and foreign markets.

\textsuperscript{16} From: Zimbabwe Growth Recovery Notes, 2012, “Re-Manufacturing Zimbabwe”.

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Domestic inter-industry linkages were broken

15. At the same time, domestic inter-industry linkages were broken during the decade long crisis. The development of these linkages was important in the evolution of Zimbabwe’s manufacturing sector. A stylized account would be that the sector grew up on the basis of firms processing agricultural outputs and providing increasingly sophisticated manufactured inputs into the agriculture and mining sectors. Initially perhaps these inputs were repair and maintenance services, but they evolved into engineering and other manufacturing. Once they reached a certain level of maturity their reliance on agriculture and mining diminished. Of 100 firms surveyed, 91 firms reported sourcing at least some inputs locally. Of these firms, most bought their inputs from other manufacturers (58 percent) followed by agriculture (33 percent), with remainder buying inputs from the mining industry.

CHANGES IN DOMESTIC INPUT SOURCING: 1999-Present (percent of firms)

<table>
<thead>
<tr>
<th>Sector</th>
<th>Decrease</th>
<th>Increase</th>
<th>Stayed the same</th>
</tr>
</thead>
<tbody>
<tr>
<td>Food</td>
<td>66.67</td>
<td>14.81</td>
<td>18.52</td>
</tr>
<tr>
<td>Textiles</td>
<td>54.55</td>
<td>18.18</td>
<td>27.27</td>
</tr>
<tr>
<td>Garments</td>
<td>76.47</td>
<td>17.65</td>
<td>5.88</td>
</tr>
<tr>
<td>Light manufacturing</td>
<td>58.33</td>
<td>16.67</td>
<td>25</td>
</tr>
<tr>
<td>Heavy manufacturing</td>
<td>57.14</td>
<td>28.57</td>
<td>14.29</td>
</tr>
<tr>
<td>Total</td>
<td>63.64</td>
<td>19.32</td>
<td>17.05</td>
</tr>
</tbody>
</table>

Source: Competition Survey, 2011

16. Repairing these linkages are an important step towards reducing costs of production and increasing competitiveness. All sectors except light manufacturing report a multitude of problems with domestic inputs including poor quality, higher prices and insufficient quantity. We also see that firms sourcing inputs domestically are much less likely to get credit compared to firms sourcing from abroad—a further indication that domestic supply linkages were broken.

PROBLEMS WITH DOMESTIC INPUT SUPPLY

<table>
<thead>
<tr>
<th>Sector</th>
<th>Poor Quality</th>
<th>Insufficient Quantity</th>
<th>Higher Prices</th>
<th>Lack of Finance</th>
<th>Paper work required</th>
<th>Long Wait</th>
<th>N</th>
</tr>
</thead>
<tbody>
<tr>
<td>Food</td>
<td>59 percent</td>
<td>89 percent</td>
<td>74</td>
<td>78</td>
<td>11</td>
<td>22</td>
<td>27</td>
</tr>
<tr>
<td>Garments</td>
<td>67 percent</td>
<td>72 percent</td>
<td>72</td>
<td>94</td>
<td>11</td>
<td>39</td>
<td>18</td>
</tr>
<tr>
<td>Heavy</td>
<td>27 percent</td>
<td>64 percent</td>
<td>77</td>
<td>86</td>
<td>9 percent</td>
<td>9 percent</td>
<td>22</td>
</tr>
<tr>
<td>Light Manufacturing</td>
<td>17 percent</td>
<td>58 percent</td>
<td>58</td>
<td>83</td>
<td>8 percent</td>
<td>33</td>
<td>12</td>
</tr>
<tr>
<td>Textiles</td>
<td>50 percent</td>
<td>67 percent</td>
<td>75</td>
<td>58</td>
<td>0 percent</td>
<td>33</td>
<td>12</td>
</tr>
</tbody>
</table>
17. In 2012, the World Bank carried out a survey of investment potential of existing mining projects. The survey revealed that without investment friendly policies, development of the mining sector may remain stunted and limited to the temporary rebound caused by strong external demand with limited positive impact on the rest of the economy. The World Bank’s baseline scenario (unchanged policies) estimates that the level of exports in the mining sector will reach US$ 5 billion in 2018 compared to US$ 11 billion with changed policies (McMahon et al 2012). Moreover, an approach exclusively geared at short-term maximization of rents capture and redistribution from temporary favourable external conditions is creating adverse long term effects on the country’s overall competitiveness and will sterilize certain subsoil resources in the medium to long run. High prices have masked some of the policies of the past ten years. As prices relax from their historic highs, it will be important to restore confidence in the sector to secure its continued growth and long term potential for broad development.

18. While the Government continues negotiations with a number of mining companies concerning their indigenization plans, uncertainty creates disincentives for investors and restricts capital in an already capital starved economy. The mining sector is highly capital intensive and requires continuous investment throughout the life of operations to open up new resources or to leverage scale economies. Indigenization policies may have limited “immediate run” effects and can be seen as a successful way to redistribute rents, but they are almost guaranteed to have detrimental long run effects as: (i) investors/miners making new capital investment decisions see increased risk associated with mining in Zimbabwe due to policy uncertainty; (ii) minority shareholder interests in Zimbabwean companies will attract a valuation discount (due to a lack of control); (iii) foreign technology and know-how are less likely to be deployed to subsidiaries where the owner of the technology does not control how it is used; and (iv) domestic capital and technology itself continues to be in short supply. As the cost of capital increases, production shifts from capital intensive to less capital-intensive methods. This tends to limit the scale of the operation, increase operating costs which, together with the high cost of capital, either renders projects completely sub-economic or increases the cut-off grade i.e. the grade below which it is not economically feasible to mine. In both cases, the result is the same in that the resource is inefficiently depleted, portions of the resource are sterilized and the medium to long run prosperity of the sector is diminished.

19. Discussions of expropriation and ad hoc taxes increase policy uncertainty and the cost of attracting capital. Politicians have recently proposed amendments to the mining regime which, if approved, would allow the state/indigenization partners to appropriate a 51% stake in mines without payment. As JP Morgan wrote in a recent note to investors: “Clearly the regulatory regime surrounding mining in [Zimbabwe] is in a
state of flux, which poses a valuation risk.” (Shepherd et al. 2013). Investors typically deal with these types of risks by increasing their required returns to capital and assigning less value to more distant cash flows — both of which are rational and efficient responses to distortionary policies and policy uncertainty with downside bias.

20. Policy uncertainty and flux also have short and long run effects. Uncertainty creates long-term distortionary effects and sterilizes resources since optimal timing of their depletion can sometimes be postponed, ultimately resulting in missed opportunities. Short-term policies, such as temporary royalty hikes or other non-tax requirements that increase the marginal costs of production, can have short run distortionary effects. The degree to which the impact is distortionary in the short run is ultimately a combination of the policy itself and the flexibility of producers to respond to changes in the short run.

There are only limited linkages between the domestic and the international financial markets

21. The critical role of quality of domestic financial markets. The relation between capital inflows and investment is complex and multifaceted. Countries’ ability to translate foreign capital flows into domestic investment is affected by a variety of variables, including the type of capital flow, the presence of domestic saving, and level of human capital, political stability, health and depth of domestic financial markets. Overall, strengthening of countries internal policies and domestic financial markets appears to be a necessary pre-condition for improving countries’ capacity to successfully absorb more capital flows.

22. The impact of bank access to foreign sources of financing appears to be asymmetric: domestic banks with international parents have been able to draw on parent bank lines of credit to obtain liquid capital, and have consequently maintained larger balances on their Nostro accounts, while domestically-based banks have had to rely primarily on their domestic deposit bases in order to fund their day-to-day lending operations. Regulations related to risk management put in place by the Reserve Bank in early 2012 have since induced banks to localize their Nostro holdings, but the broader issue of access by banks to hard currency remains a concern, and further weakening of the linkage with foreign banks could lead very destabilizing effects.

AREAS OF CONCERN FOR IMPLEMENTATION

23. The IIE Law has significant potential to adversely affect the investment climate and competitiveness of Zimbabwe, jeopardizing efforts toward the economic recovery. Indigenization of the banking sector could have potentially high destabilizing effects.
24. Act has attracted significant concern by both domestic agents and international investors. There are in particular five areas of concern, to be addressed while designing implementation:

(i) **Uncertainty over modalities of implementation of the legislation.** Uncertainty has caused delay in investment decisions, depressing levels of both domestic and foreign investment during a critical stage of the economic recovery. At the same time, uncertainty has increased the perception of risk, further heightening the country risk premium\(^{17}\). For firms that are able to obtain external finance for investment, collateral to loan ratios are particularly high in Zimbabwe, averaging more than two times the value of the loan. The legislation will likely exacerbate this.

(ii) **Increased cost of doing business.** Zimbabwe’s cost of doing business is very high in regional comparison: costs-power outages, higher input costs due to lack of domestic linkages, lack of finance, uncertainty, have increased business costs in Zimbabwe rendering firms uncompetitive. In many sectors, indigenization requirements have the effect of further raising the cost of doing business. Zimbabwe already has a very poor investment climate as reflected in the World Bank Doing Business Index. In 2013 it was ranked 172 out of 183 countries worldwide on the overall ease of doing business. On the Global Competitiveness Index, Zimbabwe is ranked 132 out of 142. In the mining sector, enactment of the act has caused Zimbabwe’s to drop to the ten bottom investment destinations in the mining sector according to the 2013 Fraser Institute Survey.

(iii) **Concern over rule of law and protection of domestic and foreign**

\(^{17}\) For a developing country like Zimbabwe, a conservative country risk premium falls in the range of 4 to 6 percent, including inflation and liquidity premiums, yielding a cost of equity between 12 and 14 percent (Lin and Pommerenke, 2012).
On the back of the implementation of the Fast-Track Land Reform Program a decade ago, domestic and international investors have expressed concern about the risk of lack of compensation in the shareholding. Further, domestic and foreign investors have expressed the concern that initial agreements might be questioned at a later stage, and that levels of indigenization might be raised.

(iv) **Depressing effects on domestic recapitalization investments.** There is lack of clarity on how to protect future investment by the non-indigenous domestic minority shareholder. At the same time, in view of low level of domestic saving, it is unclear how the new indigenous majority shareholders can carry most of the load of investment necessary for recapitalization.

(v) **Banking Sector Development.** The Reserve Bank of Zimbabwe has expressed strong concern about indigenization of the banking sector, stressing the peculiar nature of the sector, and indicating inconsistencies between indigenization and financial sector stability and development.

(vi) **Macro-economic considerations.** Indigenization is de facto a substantial tax on capital. So far, there has been no consideration of the fiscal consequences of modalities of indigenization, which could be substantial. Despite the very important amounts involved, there has so far been no review of vendor-financed scheme’s agreement with publicly guaranteed debt regulations. The sustainability of indigenization of existing firms has not been ascertained.

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**ECONOMIC LINKAGES AND TRADE-OFFS**

25. There is a need for stakeholders to dialogue and build consensus on the economic empowerment agenda in Zimbabwe. Policy weaknesses, uncertainty, and flux can be addressed. Comprehensive policy reform is a long-term process requiring consultation with a set of informed stakeholders.

26. The Government of Zimbabwe recognizes the key importance of both restarting the process of domestic investment, and increasing foreign investment in key sectors of the economy, to support growth and development. Finally, as we understand it, the ultimate objective of the indigenization legislation, is to ensure that Zimbabwe’s development is supported by a process of reparation and creation of economic linkages.

27. Shares-ownership is one but many tools that can be used to leverage increased economic linkages from firms, including, among others, fiscal linkages and policies in support to domestic procurement. There is however a direct trade-offs: the increased cost of capital determined by regulations on ownerships negatively affect potential fiscal flows. The cost of capital in Zimbabwe is about 12 percent, and already constitutes a major constraint to operations. Regulatory uncertainty further increases the country risk premium. By increasing cost of doing business, it also increases cost-
related obstacles to increased domestic procurement of goods and services, negatively affecting the process of rebuilding the broken domestic linkages.

28. Implementation of the indigenization objective should be cast into a broader view of economic of shared economic prosperity, taking into account the following: (1) Impact on overall investment (domestic and foreign) and creation of economic domestic linkages, (2) Clarification of financing modalities and overall sustainability, (3) Impact on poverty reduction; (4) Monitoring and evaluation framework to measure the progress made over time and take corrective actions when necessary.

29. Stability of the financial sector should be pursued in priority. Consideration of the stability of the banking sector in Zimbabwe should inform decisions with regards to indigenization of this sector.

30. Implementation lead to adapting policy tools to a broader set of goals aimed at maximizing domestic economic linkages, and reduce the limit of 51 percent ownership whenever other tools (fiscal linkage, technology linkages, domestic procurement…) present a more favorable impact on the domestic economy.

31. A clarification is necessary regarding protection of future investments by non-indigenous domestic firms.

32. Investment protection: implementation of the IEE should respect Bilateral Investment Protection Agreements, and ensure existing and future investment is protected.

33. Finally, the implementation of the IEE programme should be part of a broader developmental agenda, which will contribute to reduce poverty, empower the poor by providing increase access to basic services, while promoting a private sector led growth.
SITUATION ANALYSIS

1. Prior to the Fast Track Land Reform Program (FTLRP) in 2000, Government had acquired and redistributed about 3 million hectares of agricultural land, well below planned targets due to the weaknesses of the Lancaster House Constitution, escalating land prices, inadequate external funding of the program, and poor cooperation from the former large scale commercial farmers. By the end of Phase I of the land reform programme in 1997, the government had resettled 71,000 families (against a target of 162,000) on about 3 million hectares. As a result of the FTLRP, over 11 million hectares of land have been acquired and transferred to new farmers. Consensus building and policy and program formulation are constrained by limited objective assessments of the impacts of the land reforms on agriculture, especially given the absence of adequate data on the nature of agricultural production, beneficiaries, available infrastructure and social services. Recent GoZ efforts to review the land reform process have contributed to more informed policy debate on land, agricultural and economic policy formation and opened the space for policy dialogue among previously polarised actors.

2. The outcome of the Zimbabwean land reforms has been being broadly redistributive (Table 1) and allocated land to over 150,000 families on a differentiated range of farm sizes, adding about 140,000 families to the existing 1.7 million small producers in Communal and Older Resettlement Areas and around 8,000 small scale commercial farmers (SSCF), while reducing the number of large scale commercial farms to below 300. Since the early 1990s, Land Reform in Zimbabwe distributed land to two types of farm models, the A1 and A2 models\(^{18}\). Redistribution also happened within the A1 and A2 schemes in diverse agro-ecological regions across all the provinces (Moyo et al. 2009, Scoones et al. 2010, Matondi 2010, World Bank 2006). The area and number of large scale privately and state owned agricultural estates were reduced, while retaining the existing large scale conservancies, whose equity is now shared between the former white owners and new black shareholders.

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\(^{18}\) A1 model targeted landless and poor families, providing land use permits on small plots for residence, cropping and common grazing, while the A2 scheme targeted new ‘commercial’ farmers, providing larger individual plots on long-term lease to beneficiaries with farming skills and/or resources (including for hiring managers).
### Table 1: Estimated landholdings by farmer groups: 1980, 2000 and 2010

<table>
<thead>
<tr>
<th>Farm categories</th>
<th>Farms/households (000’s)</th>
<th>Area held (000 ha)</th>
<th>Average Farm size (ha)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No</td>
<td>%</td>
<td>No</td>
</tr>
<tr>
<td>Family farms</td>
<td>700</td>
<td>98</td>
<td>99</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Small/middle commercial farms</td>
<td>8.5</td>
<td>1</td>
<td>8.5</td>
</tr>
<tr>
<td>Large farms</td>
<td>5.4</td>
<td>1</td>
<td>4.95</td>
</tr>
<tr>
<td>Agro-Estates</td>
<td>0.2</td>
<td>96</td>
<td>0.29</td>
</tr>
<tr>
<td>Total</td>
<td>714</td>
<td>10</td>
<td>1,13</td>
</tr>
</tbody>
</table>

Sources: Moyo (2011a) *1: Combines Communal, Old Resettlement and A1 Areas. *2: Combines A2 and SSCF.

3. The largest number of land beneficiaries are people who had a relatively low social status and limited political or financial (commercial) connections, although some of them may have had important local connections and influence (Scoones et al., 2010; Moyo, 2011a). Scoones’ survey of 400 households across 16 sites in Masvingo province showed that the majority of the new settlers were ordinary people, with about 50% hailing from nearby communal areas and another 18% from urban areas. The remaining third of household heads was made up of civil servants (16.5% overall), business people (4.8% overall), security service personnel (3.7% overall) and former farm workers (6.7% overall). The majority of the land beneficiaries were resettled from neighboring rural settings to which many remain connected (mainly Communal Areas and farm workers). The urban beneficiaries are mainly working class people and the unemployed. A low proportion of the land beneficiaries remain in formal employment since the job market has been deteriorating.

4. The Ministry of Lands and Rural Resettlement (MLRR) has recently expressed its desire to strengthen the national capacity for land administration and governance, working towards guaranteeing and securing fairness and efficiency in land allocation, increasing capacity for dispute resolution, land valuation and compensation, and the crafting and installation of a state of the art cadastre, farm registry, and a decentralised, user friendly and electronic land information system that serves the needs of the public, business, and government sectors. The MLRR is considering a ‘Comprehensive Land Reform Programme’ (CLaRP) to assist in the development of these capacities including land use planning as a way towards the restoration of full productivity of agricultural land, and the restoration of Zimbabwe’s status as a stable food secure country.
CONSTRAINTS AND CHALLENGES

5. The execution of the land reform was accompanied by significant losses in production during the first five years and a breakdown of economic linkages. Production during the FTLRP was affected by: (i) effects of drought on yields and absolute output; (ii) reduced plantings and yields occasioned by either limited access to, or late delivery of, inputs or negative price incentives to production; (iii) reduced areas put to crops as a result of the reduction of plantings as large areas previously under production in the former LSCF farms remained under-utilized due to the slow rate of land uptake by new settlers; (iv) limited capacity (financially and in skills) to produce particular commodities; (v) a sharp reduction of livestock through slaughtering due to risk avoidance strategies and cattle rustling, (vi) the destruction and disappearance of much of the machinery stock, including irrigation equipment; and (vii) the reduced agro-industrial capacity to supply inputs due to forex shortages; (viii) conflicts between new and former farmers and their workers over the use of land, fixed farm equipment and various farm infrastructures; (ix) the loss of markets for horticulture, due to cancellation of contracts due to negative publicity in the major markets. These factors affected production and productivity differently, leading to a substantial loss of the intricate agro-industrial linkages which underpinned 60 percent of the country’s industrial base, a deterioration of the food security status, and reduced export earnings (World Bank, 2006).

6. Much of the on-farm infrastructure was removed, stolen, or vandalized in the process of taking over farms. Key machinery was moved by original owners to warehouses and/or sold, while much of what remained was looted or has broken down due to lack of maintenance. In addition, as about 80 percent of the original land owners have either left the country or stopped farming, the wealth of knowledge and skills, acquired over many years, has been severely affected.

7. There is a lack of clarity on the direction of legal and regulatory adjustments to be pursued. The outstanding issues include legal procedures, compensation to previous farm owners, security and transferability of property rights, and multiple claims of farm ownership, A2 farm sizes, and farms under BIPPAs (‘Bilateral Investment Protection and Promotion Agreements’). The land acquisition process has been subject to frequent legislative changes: At the start of the land reform, the sequence of the acquisition process according to the Land Acquisition Act was as follows: notice of the intent of acquisition (Section 5), decision of the court stipulating that land can be acquired (Section 7), and acquisition of land (Section 8). As many courts ruled in favor of farmers, the Act has been amended frequently to prevent any future legal challenges. The new Constitution is viewed by some as the penultimate solution as it allows the
government to compulsorily acquire agricultural land while the dispossessed land owners are denied the right to challenge such acquisitions in the courts.

8. **The Government has not been able to meet compensation expectations of the former commercial farmers.** The compensation value appears to consider only fixed assets (‘improvements’) and the Constitution states that the Government would not compensate for the value of land, with the exception of land covered under BIPPAs. Moreover, compensation has so far been made to only 210 out of 6,124 farmers (MLRR, 2013). Those offered compensation are generally being given a quote as to the amount of such compensation, with little indication provided as to how the value has been determined.

9. **The Government’s plan to replace title deeds with 99-year leases for all land acquired under the land reform program remains challenging, and implementation is slow:** The lease and permit tenures have so far mostly been assigned in the form of offer letters, as the more “formalized” tenure documents are still to be issued, pending finalization of the land surveys in the A2 areas and the issuance of formal permit documents in the A1 sector. Although most of the title deeds for 6,700 acquired farms, covering about 11 million hectares, are still in the hands of the original owners, provisions in the Constitution have essentially nullified these title deeds and the land is now regarded as having reverted to the state. However, some owners have taken their case to the international courts for arbitration and contend that the issue of legal ownership of the land is still unresolved, especially as the government has failed to pay fair compensation to the majority of dispossessed former owners.

10. **There is limited on information on selection process and the recipients of the productive farms acquired under the A2 scheme.** Questions regarding the equity of the redistribution process remain, especially given that no payments have been made by the recipients for the land itself. There has not been enough public information regarding the overall identity of those allocated farms.

11. **Farm workers’ rights to residential land, including compounds and food security plots were marginally addressed.** The land rights of farm workers in terms of their access to residential land and infrastructure on former LSCF land and access to small food security plots have always been informal and incidental to their provision of specific labour services to landowners. An estimated 90,000 ex-commercial farm workers (50% of the total number employed on commercial farms prior to the FTLRP) have been

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19 An outstanding 2009 International Center for Settlement of Investment Disputes (ICSID) arbitral award requires Zimbabwe to pay 8.22 million Euros plus interest to foreign claimants whose land was expropriated and for which no compensation was paid. The award remains unpaid. (Funnekotter and Others v. Republic of Zimbabwe, ICSID Case No. ARB/05/6.)
left without secure housing, land, and jobs. While a few, about 4,600, have been resettled, many were displaced. Many still reside on farms without secure land rights. Numerous ex-farm workers, especially those who were part-time and seasonal workers (up to 50% of the total number of workers in the 1990s), returned to their communal area homes. The fate of the fully displaced ex-farm workers needs to be thoroughly quantified and addressed. Ex-farm workers and other vulnerable groups remain a critical social protection challenge facing the government.

12. The capacity of the land administration system to comprehensively oversee and adjudicate the expanded land allocations and land survey and registration, as well as to refine the land policy and land laws is relatively constrained. Limited external support towards strengthening the land records is being considered by some development partners. While there is broad agreement that a further land audit is required, there is still no consensus on the precise scope, nature and methodology of the audit. Some donor funds have been made available to start-up the audit design.

13. A number of aspiring land beneficiaries was not included, and land disputes continue in various localities. There are numerous formal and informal (‘illegal occupations’) demands for access to land in various parts of the country (Moyo 2011b), and the GoZ has continued acquiring and allocating land on a small scale on some of the remaining or undistributed farms. The key pressure points for such demand are around: (i) large estates; (ii) on LSCF/A2 in some peri-urban areas; and (iii) on some conservancies. There are also cases of some existing A2 farmers and/or aspiring beneficiaries attempting to extend their land into A1 farming or smaller A2 plots. Furthermore, the transparency of land holding and its “accountability” has been queried, leading to calls for another land audit.

OPTIONS

14. In the medium-term, the GoZ may want to consider best practice options, drawing from international experience, to address the compensation issue, improve land tenure security, make land usable as collateral for loans, and establish a comprehensive land administration to manage information and conflicts to help improve land utilisation and land productivity rates. In addition, the GoZ may wish to embark on a comprehensive review of the conditions under which the state leases some of its land to investors, to help support optimization of land use. International experience points to sound land policies facilitating growth in agricultural productivity via secure land tenure, thus enhancing opportunities for investment and “sweat equity.” Land reforms in China in 1978 dismantled collective farming and conferred land rights to households, unleashing a period of prolonged growth in agricultural productivity that transformed rural China. In Africa, impact studies have confirmed that a recent massive
land certification program in Ethiopia and an ongoing country-wide registration program
in Rwanda have been associated with significant increases in investment (Deininger et
al., 2007a, and Ali, Deininger, and Goldstein, 2011, Byamugisha et al., 2013).

15. **Sound land policies would also be beneficial to accelerating flows of private
investment into agriculture and other land-based industries, including light
manufacturing.** While it has long been known that land tenure security is associated
with private investment (Place, 2009), the recent surges in investor interest in Africa in
agriculture (following the 2008 food and commodity price boom) and in oil, mineral
resources, and tourism, have put a special premium on land tenure security: without it,
investors cannot be sure of reaping the full benefits of land deals and investments, nor
can local communities receive protection and full compensation for their land rights or a
fair share of returns from investments on their land (Deininger et al., 2011b, Byamugisha
et al., 2013). Without secure tenure, risks remain high for both investors and
communities.

16. **The merits of leading, facilitating and accelerating the compensation process,
may be worthwhile considering by the GoZ.** The new Government may wish to
engage more purposefully with all parties to agree on the parameters which will guide the
compensation mechanism, and provide mutually agreeable standardised benchmarks of
values to acquired land and improvements\(^{20}\), whilst bearing in mind that land acquisition
and compensation are embodied in complex governance issues whose solutions are also
equally complex. Resolving this issue would require building competent institutions to
speedily and effectively dispose of land cases, updating expropriations and compensation
laws, and providing compensation which is deemed acceptable to all stakeholders.

17. **The agriculture sector stands to benefit greatly from a clear land tenure
policy and the re-establishment of a land market, which will expand and improve
investment incentives.** The GoZ may want to consider the option to provide A2 farms
with long term (99 year) transferable leases, with an option to buy the land. This would
entail some flexibility with respect to allowing and promoting the option to buy the land
in A2 areas, with immediate paying up of the full costs of the infrastructure on the
acquired land. This would enhance the availability of resources for a possible future
compensation fund. The leases could be granted on condition that optimal land uses and
investments are undertaken. A cost recovery fee could be considered for infrastructure
allocated to them in addition to inflation pegged land rents. Subletting of land could be
regulated to avoid re-concentration of landholdings. It would therefore be beneficial to
consolidate the land tenure administration system, especially the land registration, lease

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\(^{20}\) The MLRR has recently indicated that it is willing to engage in deeper dialogue and consultations with all stakeholders to put in
place a “consensus based compensation mechanism” acceptable to all (MLRR, July 2013).
administration and land use aspects, to ensure that new landholders comply with the conditions provided for (Binswanger-Mkhize and Moyo 2012). This type of lease could also be considered under the A1 scheme, particularly for the more market-oriented farmers. While 99 year transferable leases are used in many countries to provide tenure security and for making land assets usable as security for loans, including mortgages, clarifications are needed with respect to rules and procedures for the cancellation of such leases if land is left idle, underused, or misused, the renewal of such leases, and a land tax could be considered to optimize land use for productive purposes. In sum, a clear land policy would foster prudent land management and stimulate economic development, reduce poverty and promote social stability by improving security of tenure, simplifying the process for accessing land and making it fair, transparent and efficient, thus establishing a viable land market.

18. **The GoZ could consider the advantages of putting in place effective dispute resolution mechanisms and a comprehensive land administration system:** While there is limited consensus at this juncture, medium-term prospects for growth may hinge on the pragmatic resolution of exiting disputes and other conflicts and controversies around land tenure, including the land audit, its appropriate methodology and its objectives. However, progress at the policy level alone may not be sufficient to resolve remaining land conflicts and insecurities of tenure, or reduce insecurities associated with possible further redistribution of land, and threats of eviction. A decentralized process of land administration and conflict resolution that involves all the local claimants and stakeholders as well as independent outsiders may be needed to accelerate the process of resolution of land conflict. The upgrading of landholding records and land administration capacity, and public availability of records (e.g. in the deeds office) will facilitate formal recognition of land tenure.

19. **Clarifying the procedures for further redistribution of some lands owned by government and excess land held by some A2 farmers and private estates, could bring about positive impacts on productivity and the livelihoods of beneficiaries.** Any further land redistribution agenda could consider improving secure access to land for former commercial farm workers, women and others who feel excluded and have the promise to farm productively. Land reforms and redistribution have been implemented by many countries with the aim of redistributing land to the landless/land poor segments of the population. While there is generally consensus on the need for land redistribution, there is often controversy on how to do so peacefully and legally (Binswanger-Mkhize, Bourguignon, and van den Brink, 2009). Malawi and South Africa’s experiences with redistributive land reforms offers constructive lessons, both good and bad, to other SSA countries, including Zimbabwe. Box 1 provides an overview of the programs in these two countries to highlight the associated positive impacts accruing to beneficiaries in the form of productivity, income, and food security gains, and may provide important lessons for
the design and implementation of further redistribution interventions in Zimbabwe (Byamugisha et al., 2013).

**Box 1: Redistributing Agricultural land in South Africa and Malawi**

**South Africa.** The new government that came into power at the end of apartheid in 1994 introduced land reforms with three components: tenure reform, restitution, and redistribution. From 1994 to 2000, under the redistribution component, a Settlement/Land Acquisition Grant (SLAG) of R16,000 was allocated to beneficiary families with incomes below R1,500 per month. In 2001, the SLAG was replaced by a Land Redistribution for Agricultural Development (LRAD) program, with grants ranging from R20,000 to R100,000 given on a sliding scale corresponding to beneficiary contributions of at least R2,500; these were given to individuals, rather than households, with no income eligibility criteria. Due to a law restricting subdivision of land, beneficiaries had to form groups to afford to acquire and operate large farms, and essentially became absentee landlords with contracted farm managers. Due to these peculiarities and other program constraints, implementation was slow and ineffective. As of March 2011, only 6.27 million hectares, representing 7.2 percent of land owned by white African farmers, had been redistributed to black African farmers, with minimal impact on beneficiaries’ livelihoods. This is far from the goal of 30 percent redistribution by 2014.

**Malawi.** To address the highly unequal distribution of its overcrowded arable land, which co-exists with underutilized large-scale farms, Malawi piloted a land reform program with funding from the World Bank (2004b). The pilot project aimed to increase the income of about 15,000 rural poor families through a decentralized, community-based, and voluntary approach in four districts, modeled on Brazil’s market-based approach to land reform (under implementation since the mid-1990s). The pilot had three key elements: (i) voluntary acquisition by communities of land sold by willing estate owners; (ii) resettlement and on-farm development, including transportation of settlers, establishment of shelter, and purchase of basic inputs and necessary advisory services; and (iii) survey and registration of redistributed land. Land reform beneficiaries, organized in voluntary groups, were self-selected on the basis of pre-defined eligibility criteria. Each family received a grant of USD $1,050, managed directly by beneficiaries, of which up to 30 percent was for land acquisition, and the rest for transportation, water, shelter, and farm development. Land for the project was acquired either from willing sellers, the government, or private donations, and was registered initially under group title; it is expected that individual titles will be provided to beneficiaries upon demand in the future. Implementation was decentralized through District Assembly institutions and required capacity enhancement, especially for surveying and registration (additional financing was approved by the World Bank in 2009).

Lessons learned from the pilot were expected to guide implementation of a broader Land Reform Program initially designed in 2004, but this is currently being revised. According to the impact evaluation, the project achieved even better results than the Brazilian model it was based on (World Bank, 2009), such as: an average of over 1.5 hectares of land were distributed to each of 15,142 rural households (Brazil: 40,102 households); agricultural incomes increased an average of 40 percent per year for beneficiaries (compared to non-beneficiaries) between 2005/06 and 2008/09 (Brazil: 6 percent); the economic rate of return was 20 percent (Brazil: 13 percent); and there were positive impacts on the livelihoods of beneficiaries and surrounding communities, with improvements in land holdings, land tenure security, crop production, and productivity, and consequently on income and food security (Brazil: similar results).

*Source:* For South Africa, adapted from Lahiff and Li 2012; for Malawi, adapted from Tchale 2012.
REFERENCES


I. SECTORAL CONTEXT

1. The Government of Zimbabwe is coming from a base in early 2000 where traditional building blocks of the public financial management (PFM) system were in the process of being strengthened, largely through the implementation of an Integrated Financial Management Information System (IFMIS) to support its basic financial management functions for the Consolidated Revenue Fund (CRF). During the hyperinflationary period leading up to 2009, key building blocks of the PFM in Zimbabwe degenerated, including the IFMIS that was underpinning budget planning, execution, control and reporting. With the tabling of a budget in January 2009, several fundamental changes to the PFM system were introduced: (i) allowing the Government and others to operate in USD, ZAR and any other convertible currency; (ii) centralizing the expenditure and payment authorization systems to balance expenditure to available cash resources; (iii) opening a new set of foreign currency accounts for the Consolidated Revenue Fund and line ministries at the Commercial Bank of Zimbabwe (CBZ – in which the Government has a minority shareholding); (iv) issuing of foreign currency vouchers as an interim measure to pay a USD 100 allowance to staff; and (v) discontinuing by Reserve Bank of Zimbabwe (RBZ) of its quasi fiscal operations.

2. Key areas of PFM reforms in Zimbabwe are:

- **Legal Framework for PFM Work in Zimbabwe:** The Public Finance Management and the Audit Office Acts were promulgated in October 2009 by the Parliament of Zimbabwe and Presidential assent was given for these two laws in April, 2010 to become operational. These laws provide for greater transparency and accountability by the Accountant-General, Accounting Officers and all who utilize public funds. The draft Public Finance Management Regulations is ready for consultation and adoption. The scope of the Comptroller and Auditor-General’s responsibility to audit has also been increased to include audits at the District Levels in the Country.

- **Reviving the Integrated Financial Management Information System (IFMIS):** Significant progress has been made on the IFMIS. The system is currently accessible from all the 38 ministries in Harare and Provinces. The IFMIS is being used to capture financial data of government on a continuous basis since 2011 and financial statements are being produced on monthly and quarterly basis. There has been a significant transformation in accountability and transparency in the public sector as financial statements are being published (gazette) allowing the citizenry access to information on how public funds are being generated and utilized. For the first time in recent memory, the consolidated annual financial statement for the 2012 financial year was completed and submitted to the Auditor General for
auditing within the three months after year end as stipulated by the Public Financial Management Act. This intervention needs to be consolidated especially in the planned rolling out the IFMIS to the Districts to ease data capture and facilitate online transactions and financial management at district levels.

- **Country Integrated Financial Assessment:** In 2011, the Government of Zimbabwe (GoZ) in collaboration with the World Bank and other Development Partners prepared the Country Integrated Fiduciary Assessment (CIFA) for Zimbabwe and the report was published in 2012. The CIFA report identified several strengths in the PFM system of Zimbabwe as well as some weaknesses. The CIFA also included a Country Procurement Assessment Report (CPAR) which assessed (i) the compliance of public procurement practices with the procurement legislative and regulatory framework and (ii) the availability of regulations, documentation, and tools to support implementation. After finalization of the reports, a PFM Action Plan has been prepared (under the leadership of the Accountant General) in consultation with various stakeholders. The PFM Action Plan provides a comprehensive roadmap to cover the whole PFM cycle incorporating the PFM System (PFMS) roadmap and the policy recommendations in CIFA report and is intended to ensure that PFM activities are synchronized with government policy.

- **External Audit:** The constitution provides that the public accounts of Zimbabwe and of all accounting officers, receivers of revenue and other persons entrusted with public moneys or property of the State shall at least once in every financial year be examined, audited and reported on by the Comptroller and Auditor-General (CAG) on behalf of the House of Assembly. Furthermore, the Audit Office Act expands the scope of the CAG’s coverage to include the audit of local authorities and gave operational independence that the CAG needs in order to do the work professionally. To give full effect to the Constitution and the provisions of the Act as well as to deliver the CAG’s mandate, draft regulations and a strategic plan have been drafted.

- **Public Procurement:** The government has taken some positive steps including the enactment of the Public Procurement Act and implementation of Regulations. Substantial progress has been made in strengthening the capacity of the State Procurement Board (SPB). Technical staff underwent training in various fields of public procurement management. Computers have been networked with the objective of creating a platform for the publication of laws, tender and award notices. A consultancy assignment to carry out capacity needs assessments of procuring entities was undertaken. The SPB is one of the 12 GoZ entities where a

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US$15million e-Government system is being rolled out. The SPB has specifically requested for assistance to carry out an e-Government Procurement systems implementation readiness assessment. To address issues of capacity primarily for common use items and simple high volume but low value procurements, the support may include the consideration of the use of framework contracts and e-Procurement. An additional area of need is to develop and institutionalize procurement training in order to address procurement capacity needs in Zimbabwe in addition to modernizing institutional arrangements and procurement systems based on an updated procurement law which the Government of Zimbabwe is in the process of developing.

II. ISSUES/CHALLENGES

3. Some of the key issues and challenges highlighted in the CIFA study and requiring attention are in the following areas:

Financial Management

- **Budget credibility and fiscal discipline**: The budget has not served as an effective instrument for directing expenditures and allocating resources. Expenditure variances have been substantial.

- **Budget transparency and comprehensiveness**: The budget development process and the level of information contained in budget documents show substantial needs to improve the use of the budget for effective allocations of resources to priority functions and to provide feedback on results achieved. The budget classification is not consistent with GFS and COFOG standards. The results-based budget, when fully implemented, will facilitate reporting performance results as well as financial data. The Parliament would be expected to play a role in the strategic allocation of budget resources in a time of such shortage. Zimbabwe is heavily reliant on the performance of its Public Enterprises which were rated low in transparency; fiscal risks of SOEs are not well monitored.

- **Policy-based budgeting and service delivery**: The assessment shows that there is basis for a sound budget framework because of the multiyear budget framework and the results-based budgeting system which provides for monitoring and evaluation of activities. However, this need to be fully implemented and followed through in the budget execution phase to ensure service delivery goals are met including through full implementation of the results-based budgets reporting processes.

- **Predictability and control in budget execution to achieve intended strategic allocations of resources**: On the revenue side, the assessment showed a well-based underlying tax framework despite some collapse in revenues in a number of
areas resulting from the economic collapse. There is scope for improved systems to enhance revenue management and improve revenue estimation to increase control over fiscal discipline. Tax arrears are a problem to be dealt with seriously. There is relatively low rating performance in some aspects of the payroll, procurement, and internal controls. Internal audit needs to be more effectively utilized to encourage service delivery intentions to be met.

- **Accounting, recording, and reporting to achieve fiscal discipline and service delivery:** The assessment showed that IFMIS (SAP accounting system) is a significant resource in servicing management information needs. Further effort is required for its outputs to be more useful through improved reports to demonstrate that the resources were actually received by the front-line service delivery units. More support is needed for the integrity of the system through frequent audit by internal audit and the Auditor General using appropriate computer assisted audit techniques (CAATS). The accounting standards used for annual financial statement reporting should be the International Public Sector Accounting Standards (IPSAS) which will provide the Parliament and the public with a more credible and meaningful summary picture of the government’s revenues and spending.

- **Effectiveness of payroll controls:** The custom developed payroll system used by the Salary Services Bureau is an old system and is in need of replacement. There is a need to improve the degree of integration and reconciliation between personnel records and payroll data and the need to adopt a unified accounting system especially commitment control over payroll and other expenditure.

- **External scrutiny and audit:** The assessment for external audit and legislative scrutiny of audit reports show that the checks and balances in the PFM system need to work better to ensure that the expenditure is well controlled and scrutinized. Publication of audit reports is long overdue. There are opportunities to improve the set of Finance Regulations and wider use of internal audits and improved response to internal audit results.

### Public Procurement

- **Legislative and Regulatory Framework for Public Procurement:** Further strengthening is needed in procurement methods; exceptions to eligible bidders; registration of bidders; complaints mechanism; additional procurement regulations; standard bidding documents; and manuals.

- **Institutional Framework for Public Procurement and Management Capacity:** Many of the findings were inconsistent with international standards partly because of the economic conditions that prevailed during the hyperinflation days. Challenges include: the lack of procurement plans; procurement of items not
budgeted for; SPB’s transactional functions conflicting with its regulatory functions; procurement function at the procuring level not being well organized; lack of systems to collect and disseminate public procurement data; lack of sustainable capacity development and training strategy; and lack of quality standards for staffing and monitoring performance.

- **Procurement Operations and Market Practices:** Owing to the adverse economic conditions over the past ten years, the level of procurement operations has been low. It would be wrong to gauge future operations based on the current operations. A post procurement review (PPR) was carried out to determine whether the process used for the few operations was compliant with the Act and procurement regulations. Most of the reviews were not fully conclusive because of lack of records. Practically, all procuring entities maintain their records manually and there appears to be no consistent system for filing procurement records. The review observed serious capacity problems in some of the entities reviewed but also noted that the Act does not give SPB the authority to delegate procurement operations to procuring entities. Delegation is limited within the SPB itself. Zimbabwe has a centralized procurement system with minimum authority delegated to procuring entities. Delegation of authority and responsibility are the key to having a well-functioning system, especially if procurement is to be decentralized. When the procurement system is decentralized, the Public Procurement Act should include a provision for procuring entities with low capacity to delegate to other entities with capacity and to be able to outsource capacity by use of procurement agents.

### III. OPTIONS FOR THE WAY FORWARD

4. To help address these challenges, a draft comprehensive action plan has already been prepared under the leadership of the Accountant General. This draft plan needs to be formally approved by the government for implementation, so that, funding requests could be initiated from the ongoing Analytical Multi Donor Trust Fund (AMDTF) and other possible sources. The plan includes all the links of the PFM chain covering all PFM institutions. Approval of the plan should be followed by a joint Government Donor meeting to discuss and agree on funding and implementation modalities.
SITUATION ANALYSIS

1. Zimbabwe will face great difficulties in achieving the education-related Millennium Development Goals (MDG) due to the reversal, during the last decade, of the earlier trend of rising primary and secondary enrollments and completion. Thanks to its historical efforts in investing in education sector, Zimbabwe has one of the most literate populations in Sub-Saharan Africa (more than 90 percent, with nearly 99 percent among 15-24 year olds in the country\(^\text{22}\)). However, its trajectory to achieve the MDGs related to education has been adversely marred by the lack of funds and efforts during the economic crisis period (2000-2009). Post 2009, though more resources were channeled in to the sector, they have not yet succeeded in reversing the decline in both access and quality.

2. The most substantial issues in school education are related to the decline in basic education access and quality, and the widening regional and economic disparities in education access and quality. These issues are accentuated by a delicate school governance system and weak accountability framework. The resources available to the education sector are inadequate, and their use is often not targeted, nor efficient.

3. There is a decline in both basic education participation and completion rates, both at primary as well as at secondary levels. The Net Enrolment Rate (NER) at primary level has declined from around 99 percent in 2002 to 91 percent\(^\text{23}\) in 2009 and further down to 81.4 percent in 2011. The primary completion rate has also declined from around 74 percent in 2000 to 68 percent in 2006, and is feared to have declined further during the last few years reflecting the decline in primary NER. From 2001 to 2006, secondary education enrollment declined from 51 percent to 46 percent\(^\text{24}\) and further declined to around 40 percent in 2011, as a result of the low transition rate from primary to secondary education.

4. Equally alarming is the drop in quality in primary and secondary education. The grade 7 pass rates, which used to be 70.5 percent in 2007 declined to 39.4 percent in 2009, and went further down to 31.2 percent in 2012. Similarly, at O levels, the pass rates have remained dismally low, between 15 percent - 18 percent during the period 2008-2012. The analysis of grade 6 SACMEQ assessment results show that only 4.5

\(^\text{22}\) Labor Force Survey, 2011  
\(^\text{23}\) Zimbabwe School Information, 2009  
\(^\text{24}\) UNDP (2010)
percent children could do critical reading\textsuperscript{25} and another 11.7 percent could do analytical reading\textsuperscript{26}. These are some of the critical skills that are relevant for emerging markets.

5. **The national averages education outcomes and its deterioration often camouflage wide variations across districts, schools and household by their income levels.** Analysis indicates positive correlation between Grade 7 examination pass rates and the level of school income per pupil. The pass rates for both female and male students are nearly three times higher in the top group of districts with the highest per pupil school income compared the bottom group of districts. Examination results follow both school income as well as trending geographically: eastern districts achieve substantially higher results than the western districts.

6. **The significant concerns in tertiary education sectors are related to the serious constraints in the supply of skilled labor for critical sector, including education itself.** Though the overall number of students enrolled in tertiary education programs are increasing, the gross enrolment ratio at tertiary education sector is only 3.9 percent\textsuperscript{27}. However, the number of students enrolled in teacher training programs has not been increasing, thus imperiling the availability of qualified teachers for school system. Similarly, the number of students enrolled in technical and vocational trades is also not increasing, resulting in the shortage of skilled people available in the labor market.

7. **Evidences from Labor Force Survey 2011 show that the employment outcomes for those with different levels of education are bleak, which is partly due to the impact of the economic crisis and partly due to the limited relevance and quality of the education.** Zimbabwe’s labor force participation rate (LFPR) is estimated to be over 87 percent, around 12 percent of those employed are under-employed, which means their full potential is not utilized. Only around 16 percent of those employed had some skills (5 percent had professional qualifications, another 6 percent skilled and 5 percent again semi-skilled), leaving around 83 percent unskilled.

8. **Funding for the education sector has been seriously affected the economic crisis.** Zimbabwe spent around 8.5 percent of its GDP and around 26 percent of its budget on basic education sectors (primary and secondary) in 2005. In 2010, Zimbabwe was spending around 2.49 percent of its GDP in education sector, and the share of basic education in overall public education had reduced from around 30 percent in 2001 to 15 percent in 2010. There appears to have been an effort to protect the spending in higher

\textsuperscript{25} Reads from various parts of the text so as to infer and evaluate what the writer has assumed about both the topic and the characteristics of the reader (source: SACMEQ Policy Brief, November 2011)

\textsuperscript{26} Locates information in longer texts (narrative, document or expository) in order to combine information from various parts of the text so as to infer the writer's personal beliefs (value systems, prejudices and biases) [source: SACMEQ Policy Brief, November 2011].

\textsuperscript{27} According to UNESCO Institute of Statistics, Gross enrolment ratio at tertiary level is the sum of all tertiary level students enrolled at the start of the school year, expressed as a percentage of the mid-year population in the 5 year age group after the official secondary school leaving age. (Source: UNESCO Institute of Statistics)
education in relation to school education. The tertiary and higher education sector as a whole has experienced a significant gain in its share of public spending, from 3.2 percent of the budget in 2009 to 5.7 percent in 2011. In 2011, per student spending was around US$115 per primary and US$200 for secondary. Around the same time, the estimated per student spending for higher education in the country was around US$1800. Of the higher education spending, almost 89 percent was on universities, and only around 5 percent on teacher education and technical and vocational education institutions.

9. Apart from a reduction in total public spending on education, the quality of spending has also deteriorated. More than 95 percent of the primary and secondary education spending is on wages / salaries and the non-salary investment is very minimal. Around two-thirds of all civil servants in the country are Teachers, of which 60 percent belong to primary education sub-sector while 35 percent in secondary education. Non-salary recurrent expenditure of the Ministry of Education has been declining rapidly since 2010 where it was US$20.6 million, to US$17.9 million in 2011 to US$7.9 million in 2012. In 2012 only US$10.2 million were spent of the combined non-salary recurrent and capital budget. A further breakdown of non-salary recurrent expenditure to primary and secondary schools reveals that only US$0.40 per student at the primary level and US$1.60 per student at the secondary level were actually spent in 2012.

10. The reduced government spending has increased the burden on household’s income with the increased “out of pocket expenditure”. While primary education is considered to be “free”, and though the Basic Education Assistance Module (BEAM) provides assistance for tuition fees, levies, and examination fees to orphans and vulnerable children (OVC) through block grants transferred directly to schools, the financial barriers to education remain a concern. The schools generally charge some school fees. The average annual fee charged ranged between US$5 to US$25 depending on the location and the size of the school in 2009. There are other fees too (such as the examination fees). This means that the out-of-pocket expenditures of households must be quite sizeable. While the latest data is not available, historical data shows that in 2008, out of pocket expenditures for basic education accounted for almost 10.2 percent of all households’ spending. The impact of the increased burden is seen in the increased dropouts from primary and secondary education.

11. There are also disparities in how the per student payments are distributed across regions in the country. The BEAM pays about two and a half times more per beneficiary in top school income quintile districts (US$68 on average) than in bottom

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quintile districts. This presumably reflects higher fees in the higher income districts, but is also a reflection of targeting inefficiencies in resource allocation\textsuperscript{30}.

**CHALLENGES IN THE EDUCATION SECTOR**

12. Zimbabwe’s challenges in education sector have arisen from a combination of the impact of the crisis on public investment in education and deterioration of school governance. The decline in public investment has resulted in the corrosion of learning environment in schools like (i) inadequate school infrastructure, and non-availability of teaching-learning materials in adequate quantity (ii) shortage of teachers and their quality, and (iii) lack of information on the diagnostics about pedagogical process that result in learning outcomes at school level.

13. **Inadequate school infrastructure and lack of teaching learning materials affect learning environment:** The system suffers not only from insufficient infrastructure, but also from dilapidated school infrastructure. The student classroom ratio (SCR) was 50:1 on an average in 2012, but it ranged from 58 in the poorest districts to 47 in the richest districts. Classrooms in poorer districts are more crowded than those in the upper quintiles of school income. Only 53 percent of schools had safe and reliable drinking water, but only 40 percent of schools in the lowest district quintile have regular access to water of appropriate standards, compared with 66 percent of schools in the top district quintiles on average.

14. **One of the major sections of education affected by crisis and now affecting the quality and outcomes is the quantity-quality-accountability shortage among teachers.** The PTR (Pupil Teacher Ratio) at primary levels has been on the rise – from around 37:1 in 2006 to 40:1 in recent years. PTR vary somewhat in aggregate, but qualified teachers are in particularly short supply in poorer districts. The EMIS data reveals that the average PTR for qualified teachers averaged around 45:1 in 2012, it ranged between 61 and 34 for educationally poor and developed districts. While there is shortage of teachers in the system, there are even more serious challenges in terms of rampant teacher absenteeism, high rates of teacher attrition and teacher motivation. The reasons for these challenges could range from low remunerations to poor working conditions and insufficient monitoring and accountability mechanisms. The issue of teacher shortage and capacity is not only relevant for basic education sectors, but also in all higher education and technical institutions.

15. **Targeting resources at system and school level is affected by lack of information about what helps in school effectiveness, especially regarding pedagogical process:** The analysis of SACMEQ data on school resources reveal that

\textsuperscript{30} World Bank Policy brief (2013) mimeo
only 54 percent schools in Zimbabwe had teacher guides for language and math; and only 68 percent schools had adequate number of exercise books, pencils, rulers etc. However, there is no information linking the teaching learning materials or pedagogy to the process of acquiring learning competencies, assessment and feedback mechanism, that could throw light on what exactly needs to be improved to increase learning among children. While targeting funding where it has maximum impact is important, often targeting is not possible due to paucity of data and lack of analysis.

PRIORITIES AND OPTIONS

16. **The Go Z could prioritize its goals and actions in terms of those which needs to be done immediately and those which is required in the long term.** The Ministry of Education, Sport, Arts and Culture (MOESAC), is required to translate its vision (reflected in Education Medium Term Plan: EMTP 2011-2015 and its Operations Plan) to deliverable actions and prioritize them on the basis of what is relevant for immediate action; what is appropriate for medium term and what should be done for long term impacts. From the analysis of the education sector challenges, one could think of prioritizing actions (i) that should be initiated immediately to arrest the decline in primary and secondary enrolments and graduation; and (ii) actions that require long term sustainable efforts, covering all sub-sectors of education.

17. **In the short and medium term, MOESAC could focus on basic education sectors (primary and secondary) given its impact on MDGs.** This would involve: (i) increasing the share of public expenditure for primary and secondary education; (ii) develop a targeting mechanism to increase allocations for poorer regions and households; (iii) create a basic standard for learning environment in all schools and estimate its costs (iv) enhance the enrolments in teacher preparation programs and improve their quality (v) establish monitoring and evaluation system to monitor progress in each school on key output and input indicators.

18. **In order to rejuvenate the basic education system, GoZ should increase the share of primary and secondary education allocations in the budget.** The government should try to get back to its previous allocation levels for basic education sector. Following international best practices (like OECD countries on an average invest around 6 percent of their GDP on education, and 4 percent on primary education alone), the country should target to invest at least 5 percent of its GDP in basic education.

19. **The allocative efficiency of the public investments in basic education could be leveraged with alternative mechanisms.** In order to ensure better flow of funds and its efficacy, decentralized mechanisms for planning and implementation at appropriate levels

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could be used. By improving coordination and convergence with the ministries with competence /complementarity for education sector programs, better service provisions could be ensured in the short run (for example, coordinating with Ministry managing infrastructure projects to ensure better school infrastructure like drinking water and toilets availability). International assistance and private sector engagements could be encouraged for leveraging government funding.

1. **In order to increase allocative efficiency, MOESAC should develop a targeting mechanism to increase allocations for poorer regions and households.** The mechanism for targeting poorer regions could be a formula that gives more weightage to not only education related under-development, but also socio-ethnic, climatic, economic, and infrastructure vulnerability of regions as well. For targeting poor and vulnerable households, a variety of supply side interventions or demand side interventions or a mix of both could be resorted. One such supply side action for basic education sector could be subsidizing basic education sector completely or partially. Complete subsidizing would involve abolishing tuition fees, examination fees and other fees charged from students while partial subsidization would involve reducing and fixing school fees to a minimum level for all students or for some students. In the shorter term, the country could resort to partial subsidy for all students and full subsidy to the children from the most vulnerable sections of the society. On the possible demand side interventions, the children from the poorest strata of households could be provided with cash transfers / subsidies and the appropriate amount that would make an impact on the targeted results could be decided on the basis of some initial pilots.

2. **Create basic standards for improving learning environment in all schools and estimate its costs:** School attendance and learning requires certain basic facilities and enabling learning environment. It is important to define the minimum facilities as per standardized norms first. Internationally, most educationally lagging countries who are aiming to improve their education sector targets to have desirable classroom size (student-classroom ratio), functional toilets and drinking water facilities per students, classroom desks and benches, good quality blackboards, all core-subject text books for all students, learning materials like pencils, chalks etc., and if possible, additional learning/reading materials and school libraries. At secondary level, it would also involve providing laboratory and ICT facilities as well. The basic infrastructure like classrooms and teaching learning materials like text books, blackboards and pencils/pen are non-negotiable needs at short term. Hence the costs for these should be estimated using per student / group of students / classroom norms. Since such estimations follow gaps and norms, it would automatically promote targeting of resources.

3. **Enhancing enrolments in teacher preparation programs and planning to improve their quality is critical for meeting the immediate needs of teachers as well as future projected needs of teaching force.** Creating an enabling teaching learning
environment in school also depends on the teachers. The country is already facing teacher shortages, and more importantly, qualified teacher shortages. Since the immediate enhancements in primary and secondary education investments is expected to reverse the decline in enrolments, more and more students are expected to enter the system, spiraling the students to teacher ratio. So it is important to plan for increasing teacher vacancies, and hence more intake in teacher education programs. Since the teaching requirements in the short term requires adapting for revised curriculum and modern pedagogies, the existing teachers also needs to be re-trained and trained for their professional development. This would amount to investing substantially in teachers’ in-service training as well.

4. **In the short and medium term, developing national higher education and vocational /skills standards framework will facilitate preparing the sector for future expansion and improvements.** While the immediate focus should be on improving basic education, it is important to do preparatory work for future development of higher education as well as vocational training and skills development. The Government of Zimbabwe should invest in developing curriculum and standards for those skills that are required in the emerging economic markets. This would require investments in planning as well as learning from international best practices.

5. **Strengthening the monitoring and evaluation (M&E) system is key to facilitate better planning; it is essential to track progress of activities and results at school and system levels.** The messages emerging from various evidences – for example, the regional inequities existing in the country / system in terms of school / institutional resources, poor learning outcomes, employment trends, and emerging market analysis – all indicates that it is important to improve the use of analysis and evidences for better planning and implementing education programs Targeting improved investments in basic education sector requires evidence based planning. Similarly, to gauge the progress in interventions and understanding the effect of investments on improving school inputs and outputs, a strong data base, updated periodically, is important.

6. **In the long term, the country should aim to expand both basic and post basic education system, building on the strong system in place for basic education sector and foundations available for higher education sector.** This would involve: (i) with the basic elements for improving enrolments, retention and teaching learning in place, ensuring learning outcomes at primary and secondary levels; and (ii) improving post-basic education, and within that, most importantly, improving vocational education and training.

7. **In the long run, improving and sustaining quality of education at primary and secondary level involves constantly evolving and adapting innovative education methods.** The investments in the long run in primary and secondary education sectors should, hence focus on (i) adapting curriculum and pedagogy that focus on critical
thinking and reasoning abilities; (ii) assessment systems that enable comparison of the country with other countries at global level; and (iii) adapting modern technologies like ICT enabled education.

8. **The technical and vocational education sector should get its due attention in the long run.** While it is important to invest in technical and vocational education, skill development and training in the short run as well, the sector assumes more critical when there is an improvement in primary and secondary school graduation rates, and when the secondary school graduates throng the system demanding vocational training and skills development to enable them for job market. In the long run, the government should focus investing more in the sector. This would entail: (i) investing more to expand the technical and vocational education and training (TVET) institutions, which involves planning to increase TVET institutions as well as increasing the facilities and materials in the TVETs; (ii) diversifying the course, content, curriculum and pedagogy for training to make it more relevant for market and adaptive; (iii) incentivizing youth to enroll and participate in TVET programs, with a focus on targeting more towards those from poor and vulnerable backgrounds; (iv) investing in improving the industry- training interface and practical content; (v) investing in trainers, both for improving quantity and quality; and (vi) improving the mechanisms for certification and re-certifications, allowing options for mid-career training courses.

9. **Higher education and Research and Development (R&D) sectors need special attention in the long run.** With economic recovery, and with basic education sectors developed, Zimbabwe in the long run needs to prepare itself to be a knowledge economy. This require consistent investments to improve (i) expansion and modernization of higher education institutions, both facilities and intake; (ii) diversifying courses and improving curriculum; with improved focus on those areas where the country is anticipating future labor / professional needs; (iii) investing in the number and quality of faculty; (iv) investing in research and development activities in the university departments; and (v) incentivize the participation of women and those from poor and vulnerable backgrounds in higher education.

10. **Exploring funds for investing in education through alternative sources:** While basic education is primarily the domain of public investments, for the expansion of TVET and higher education, more private sector investment needs to be encouraged in the country. The private sector engagement could be encouraged through providing grants-in-aid for their participation and functioning or through a public-private partnership mode.
ZIMBABWE RECOVERY NOTES

HEALTH SECTOR POLICY NOTE

**Key Messages**

- The economic challenges that Zimbabwe faced over the last decade have been detrimental to its once robust health care system.
- As a result, the Government of Zimbabwe (GoZ) now funds its health sector at a level substantially lower than that of many other Sub-Saharan African countries. Consequently, the major financial burden of health care falls on households in the form of out-of-pocket payments (OOPs), rendering the health system inequitable and inefficient.
- While Zimbabwe has shown some signs of progress across certain HIV/AIDS and malaria indicators, the country’s broader health outcomes have stagnated to the degree that Zimbabwe lags behind Sub-Saharan Africa peers in the achievement of key health related Millennium Development Goals (MDGs).
- The recent efforts of the Ministry of Health and Child Welfare (MOHCW)—with the support of development partners—have not been able to fully relieve the health sector from the consequences of the prolonged period of stagnation and decline. Additionally, recently rising rates of non-communicable diseases (NCDs) pose further challenges.
- Zimbabwe’s health system can be strengthened to address inequities and technical and allocative inefficiencies through: (i) a larger Government budget for health; (ii) equitable and evidence-based health budget allocation policies and strategies; (iii) increased non-wage budgets; (iv) effective pre-payment mechanisms and targeted subsidies to reduce OOPs; (v) enhanced government-donor coordination via direct joint financing and better data tracking and reporting; (vi) improved public expenditure management; and (vii) improved quality of care.
- Increasing coverage of the basic package of evidence-based maternal and child health (MCH) interventions will improve progress toward MCH-related MDGs. One strategy for potential scale up in Zimbabwe is Results Based Financing (RBF), which can: enhance the flow of resources to decentralized levels of the health sector; improve provider accountability and performance; and improve equity and service delivery. Data from Zimbabwe and from other countries in Latin America and Africa confirms RBF’s effectiveness in increasing utilization of high impact interventions by the poor.

**Mixed Health Outcomes**

1. Zimbabwe continues to experience mixed health-related outcomes as a result of a health system weakened by the protracted effects of HIV and AIDS, out-migration of skilled personnel and a lengthy economic crisis. There has been, in particular, a sharp decline in key indicators such as coverage of key primary health care interventions, life expectancy and the tuberculosis (TB) notification rate. While communicable diseases have been successfully controlled, non-communicable diseases (NCDs) are on the rise.

2. Despite these challenges, the country’s health system has begun to show signs of recovery through the concerted efforts of the MOHCW and its partners. In the past five years, Zimbabwe has made good progress in the fight against HIV and AIDS, with rates of infection falling and achievement of near universal ART coverage for adults.
### Box-1: Mixed Progress in Health Outcomes

<table>
<thead>
<tr>
<th>Positive Trends</th>
<th>Concerns</th>
</tr>
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<tbody>
<tr>
<td>• Malaria incidence rate has declined from 5.8% to 2.5% during 2009-11</td>
<td>• New hypertension cases increased from 8,000 to 20,000 during 2010-11 – partly reflecting improvement in diagnosis</td>
</tr>
<tr>
<td>• HIV prevalence has dropped from 23.7% to 13.1% during 2001-11</td>
<td>• Diabetes prevalence per 100,000 increasing and now at 5,000</td>
</tr>
<tr>
<td>• Increased immunization rates (fully immunized) from 52.6% (2005/6) to 63% and 64.3% in 2009 and 2010/11 respectively</td>
<td>• Over 10 years’ decline in under-5 stunting is low at 2%</td>
</tr>
</tbody>
</table>

### Health Related MDGs Unlikely to be Met
3. Maternal and child health (MCH) indicators in particular are off-track from MDG targets. Zimbabwe’s maternal mortality ratio (MMR) has increased from the early 90s and surpassed the progressively declining regional average. The current MMR is one of the highest in the region at approximately 960 deaths per 100,000 live births, far from the MGD target of 145. The under-five mortality rate has improved from 105/1000 in 2000 to 84/1000 in 2010-11, but this progress lags behind desired target of 34/1000 by year 2015. Similarly, the infant mortality rate of 57/1000 in 2010-11 demonstrates some improvement from the 2005-06 rate of 60/1000 but is still far from the 2015 target of 22/1000.

4. TB is still a major cause of morbidity with a notification rate of 434/100,000. During 2009-2011, the malaria case fatality ratio increased from 3.0% to 4.5%.2 Currently, 28% of children between 6-59 months are stunted (the MDG target is 7% by 2015).

### Status on Equity, Allocative Efficiency and Quality of Care

#### a) Equity: Poverty, health status and access to health services

### Government Health Spending and Households’ Financial Burden of Care
5. Diverting from the trend among other developing countries, government health spending in Zimbabwe fell from 39% to 18% between 2001 and 2010 (NHA). As a consequence, households bear the largest share of health expenditures in the form of out-of-pocket payments (OOPs), which increased from 36% to 39% over that period. However, there is no pre-payment financing option protecting the poor from income shocks and catastrophic health expenditures.
6. User fees are the largest contributor to household OOPs. The National Integrated Health Facility Assessment (NIHFA) showed a significantly high percentage of facilities charge user fees. These varied across provinces with Bulawayo, Mashonaland East and Central having the highest percentages of 89%, 63% and 60% respectively at the clinic level. For hospitals, the highest percentages were found in Mashonaland East and Matabeleland North and South.

Inequalities in Access to Health Services
7. Zimbabwe has a high urban-rural poverty disparity (Zimstat Poverty Report 2011). The overall Gini index was 42.3 in 2012 with the urban index at 39 and the rural index at 37 reflecting the prevailing adverse status of the urban poor. Still, the overall poverty rate is higher in rural areas (84.3%) than urban settings (30.4%). There are likewise inequalities in financial protection, service utilization, and health status between the rich and the poor (DHS 2010/11). While 20% of women aged 14-49 in the richest income quintile have health insurance, coverage is almost non-existent among the poorest quintile. Rich women are twice as likely as poor women to deliver
in a health institution and three times more likely to have a postnatal check-up 2 days after delivery. Both infant and under five mortality are much higher among the poor.

Table 1. Inequality in financial coverage and key MCH indicators reported by surveyed women 15-49 years

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>Poorest Quintile</th>
<th>Richest Quintile</th>
</tr>
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<tbody>
<tr>
<td>Financial protection</td>
<td></td>
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<tr>
<td>Health insurance coverage (%)</td>
<td>0.5</td>
<td>20.0</td>
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<tr>
<td>Service Utilization</td>
<td></td>
<td></td>
</tr>
<tr>
<td>At least one ANC check-up (%)</td>
<td>88.4</td>
<td>94.6</td>
</tr>
<tr>
<td>Institutional delivery (%)</td>
<td>46.2</td>
<td>89.9</td>
</tr>
<tr>
<td>C-section (%)</td>
<td>2.5</td>
<td>9.2</td>
</tr>
<tr>
<td>PNC check-up within first 2 days after birth (%)</td>
<td>15.7</td>
<td>46.6</td>
</tr>
<tr>
<td>Children 12-23 months reported receiving all basic vaccines (%)</td>
<td>54.6</td>
<td>72.8</td>
</tr>
<tr>
<td>Children with diarrhoea who received no treatment (%)</td>
<td>25.3</td>
<td>11.8</td>
</tr>
<tr>
<td>Health Outcomes</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Infant mortality (per 1,000 live births)</td>
<td>55</td>
<td>48</td>
</tr>
<tr>
<td>U5 mortality (per 1,000 live births)</td>
<td>85</td>
<td>58</td>
</tr>
</tbody>
</table>

Source: ZDHS 2011

8. **Allocative Efficiencies**

8. **Budgeting and allocative efficiency:** The Zimbabwe health sector’s evolving budget and resource allocation system remains skewed towards curative rather than preventative care. Although the medical care allocation includes health facility-based preventive care, there is no disaggregation to reflect sub-components for preventive and purely curative purposes to enable tracking. The health budget also requires disaggregation by allocation at different levels of care.

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<td>9</td>
<td>14</td>
<td>14</td>
<td>15</td>
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<tr>
<td>Medical Care</td>
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<td>82</td>
<td>81</td>
<td>80</td>
<td>74</td>
<td>74</td>
<td>83</td>
</tr>
<tr>
<td>Preventive Services</td>
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<td>11</td>
<td>11</td>
<td>7</td>
<td>10</td>
<td>6</td>
<td>10</td>
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<td>Research</td>
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<td>1</td>
<td>0</td>
<td>2</td>
<td>2</td>
<td>2</td>
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</tbody>
</table>

Source; Ministry of Finance Budget estimates 2002-2013; * Estimates

9. While some localized examples of evidence-based budget allocation and tracking are reported (i.e. use of population and trends in utilization of health services; number of health facilities and size of catchment areas; and seasonal trends of disease), there are no national guidelines to enforce a standardized evidence-based resource allocation formula of the health sector budget at the Ministry of Finance (MOF) or the MOHCW at national and decentralized levels.

10. **Prioritization of the health sector budget:** In view of the limited resources due to Government fiscal constraints, it will be challenging but important to make strategic choices to ensure that fewer but higher impact areas are well funded to avoid spreading resources thinly across many public sector health programs.
11. **Wage expenditures:** High recurrent expenditures are crowding out preventive care and capital expenditures. In particular, the overall country wage bill is among the highest in Sub-Saharan Africa because of severe fiscal constraints; the limited allocations by Treasury are prioritized to pay wages and maintain the system.

![Figure 7: Wage as % of Expenditure on Health](image1)

Figure 7: Wage as % of Expenditure on Health

![Figure 8: Non-Wage Expenditure](image2)

Figure 8: Non-Wage Expenditure

12. **Institutional arrangements and management of resources:** The current demand-based resources allocation framework assumes that districts and provinces have feasible annual operational plans on which to base their budget proposals. However, according to the NIHFA survey only 65% of facilities were reported to have an annual work plan in place. Funds management is an additional challenge, especially with vacancy of hospital administrators at 30%.

13. **Harmonization of funding and donor coordination:** There is room for much stronger coordination between government and donor funding to enhance budget prioritization and tracking at the various levels of care and to ensure optimal use of available funds. Given that donors contribute 19% and Government 18% of all total health expenditures, it would be strategic and timely for the MOHCW and the MOF coordinate and institutionalize a resource planning, mapping and tracking mechanism. Such a mechanism is particularly important in the absence of a joint health sector work plan and results framework consolidating development partner and Government health sector financing, and will strengthen accountability for overall resource flows at different levels of the healthcare system and promote better synergies in expenditure prioritization.

c) **Improving Quality and Efficiency of Care**

14. **Quality of care is an important aspect of technical efficiency linked to health workers’ knowledge and, more importantly, to what health workers actually do in their interactions with patients. Health workers in Zimbabwe are not performing well by either measure.** The 2012 NIHFA showed moderate knowledge levels amongst health workers in the area of Maternal, Neonatal and Child Health (MNCH), indicating the need for strengthening quality improvement mechanisms. The results indicated higher mean knowledge scores in Child Health (56.8% (SD=17.9)) compared to Maternal Health (47.7% (SD=16.9)). The observation component of the assessment identified variations in the actual skills...
for specific aspects of care and anomalies in practices against their standards on some components of care.

Figure 9: Provider Competence Standards

Figure 10: Adherence to Clinical Standards

15. The current status reflects weakened health worker production, motivation and supervision efforts, and limits capabilities to implement the standards of care. The facilities assessed by NIHFA had in one year approximately 7 visits and 2 visits from the higher authorities of DHE and PHE respectively. Though these visits were reported as useful, they were program-specific and focused more on administrative issues than clinical contents and did not holistically cover all aspects of service delivery. The vertical health programs and fragmented monitoring and reporting procedures were reported to contribute to the workload burden of the frontline health workers.

Constraints to the Health System

a) Supply-Side Constraints

16. Zimbabwe’s healthcare delivery system, rural and urban faces inadequate skilled human resources, supplies, infrastructure, managerial capacities, staff motivation and service quality. Thus, low levels of satisfaction force clients to seek self-treatment or purchase supplies and drugs from the expensive private sector. The shortage of human resources is exemplified by the 25% vacancy rate of nurses in public health facilities in urban areas. As per a 2012 survey, health workers are dissatisfied with salary, employment benefits, opportunities for promotion and the general state of health facilities. The service delivery system remains disorganized; decentralization is not fully effective at the level of planning and budgeting; performance appraisals and monitoring are irregular; and data reporting and management lack rigor. A weak referral system and limited technical support to Community Health Workers (CHWs) (or other mechanisms to retain them) are other concerns. Community participation in health services delivery is generally limited given that health center committees (HCCs) function at varying levels across different districts.
**b) Demand-Side Constraints**

17. On the demand-side, the largest barrier to care is inability to pay for care as a result of poverty and user fees at the point of care in both rural and urban areas. A World Bank study indicates that the minimum OOPs for a household in urban areas (Bulawayo and Harare) on MCH care was around US$200. Another barrier is Zimbabwe’s inadequate and expensive transportation system, even in urban areas. Ambulance fees charge $20 irrespective of the distance to the health facility. In rural settings, mothers who live beyond 10km from a health facility tend to deliver less in health facilities. Though socio-cultural barriers are crucial determinants of healthcare, community awareness of MCH has improved substantially. A recent survey highlights that regardless of gender, most participants had knowledge of the health risks associated with pregnancy and childbirth in cities. Regarding NCDs, however, there is limited prevailing knowledge of signs, symptoms and management. CHWs play a crucial role in improving health seeking behaviour and health facility utilization and the community is satisfied with their services.

**Efforts to Strengthen the Health System**

18. The Government of Zimbabwe, with the support of development partners, has embarked on some progressive steps:

i. Together with the Global Fund and other development partners contributing to the Health Transition Fund (HTF), the MOHCW has launched an initiative to re-equip CHWs and enhance their mentorship to support disease surveillance.

ii. The MOF’s recent unfreezing of 2,000 nursing posts for recruitment promises to help address the health workforce shortage.

iii. The MOHCW is leading the development of a Quality Assurance and Quality Improvement Strategy to establish benchmarks for quality and mechanisms for integrated quality supervision. However, the MOHCW needs to scale-up work on quality of care and develop integrated standard guidelines for care.

iv. The successful roll-out of the HTF by the MOHCW with the support of several development partners is a major step forward towards strengthening the supply side-aspects of the health system.

v. The implementation of the RBF approach in 18 districts of the country since March 2012 is also reflective of the MOHCW and development partners’ commitment to improve health outcomes through innovative mechanisms.

19. Despite the achievements in certain areas, the overall health sector performance is largely mixed, requiring realization of some unmet health and service delivery indicators in the near future.
Strategic Recommendations and Opportunities

20. The following short- and medium-term recommendations can strengthen current efforts to accelerate Zimbabwe’s health system performance and pace towards the attainment of broader goals:

1. **Increase government non-wage health expenditures**
   a. Presently, government expenditure on health is comparatively lower than that of many regional peers. Reliance on donor financing is not sustainable, while charging user fees at the point of service delivery is highly regressive. To address this problem, it will be important to prioritize steady increases in allocation for the non-wage budget toward cost-effective preventive and primary care high impact interventions. **(short-term)**

2. **Improve allocative efficiency**
   a. The Treasury’s current health sector budget envelope can be reviewed for opportunities to shift from long-standing non-performing programs to cost-effective and high impact interventions that are currently under-funded—such as child and maternal nutrition. **(short-term)**
   b. For the purposes of financial tracking and management, an expenditure tracking survey and a financing module in the HMIS/DHIS2 at different levels of care would strengthen financial accountability and resource tracking. **(short-term)**
   c. Clear evidence-based models for resource allocation will minimize skewed and inefficient resource allocations and can include such approaches as: (i) coordination of government and donor funding sources through supporting common sector annual work plans and M&E frameworks to avoid duplication and asymmetry in spending; (ii) encouragement of decentralized (and coordinated in tracking) budgeting and management systems for effective resource generation and addressing community needs; and (iii) more emphasis on prevention than cure. **(medium-term)**
   d. The Government needs to enhance MOF investment on prevention, particularly emphasizing the CHW Program including harmonisation of the cadre (Village Health Workers, Community Home Based Care Givers, and Community Based Distributors). **(medium-term)**

3. **Quality Improvement**
   a. It is a critical time for the health sector to shift from vertical approaches to integrated standards of care in supervision and mentorship. This shift requires leadership of the MOHCW and cooperation of development partners. **(short-term)**
   b. The Government would benefit from engaging tertiary institutions in the supervision and mentorship of health workers to facilitate continuity in skills development and efficient dissemination of emerging sound practices in service delivery. **(medium-term)**
   c. The HMIS needs to incorporate quality of care indicators which can be used to assess the sector’s progress towards implementation of quality improvement interventions. **(short-term)**

4. **Finalize an evidence-based health financing strategy**
   Efforts underway to develop a health financing strategy are commendable. However, a sound health financing strategy must be informed by robust empirical evidence. The strategy should clearly delineate the resources, programs and time
frames that will be needed to achieve stated objectives; and the domestic and external mechanisms for financing those objectives. (short-term)

5. **Reduce inequities**
   
a. Given the health system’s strong reliance on user fees which have catastrophic financial effects on economically disadvantaged populations Central Government budget allocation should give more weight to poorer provinces and districts based on the Zimstat Poverty Data of 2011. (medium-term)
   
b. The MOHCW and other relevant Government Ministries and Departments need to consider rolling-out and evaluating innovative interventions that minimize OOPs. These interventions may include pre-payment mechanisms such as social health insurance schemes, or models with Government subsidy such as the RBF. The efficacy of the models can be assessed in the context of their ability to improve access, service delivery and reduce inequities in utilization of priority health services. (medium-term).
SOCIAL PROTECTION POLICY NOTE

SITUATION ANALYSIS

1. Zimbabwe faces high levels of poverty and vulnerability and the social protection system (safety nets, social insurance and labor market programs) needs to respond to these. About 72.3 percent of Zimbabweans (9.1 million people) are poor and 22.5 percent (2.8 million people) extremely poor, with poverty and extreme poverty more prevalent in rural areas. About 8 percent of households have a chronically ill member (primarily as a result of HIV/AIDS) and 30 percent are home to an orphan. There are approximately one million orphans. Infant mortality (80 per 1000), low immunization (83 percent) and malnutrition (32 percent stunting among children under 5) represent continued threats to children. There are significant barriers to education, particularly at the secondary school level, with 38 percent secondary gross enrollment rates among the extreme poor. Youth unemployment remains high in urban areas (46.8 percent compared to 5.3 for rural youth). Underemployment and low agricultural productively contribute to poverty in rural areas. Eighty-four percent of employment is in the informal sector and this has implications for social protection coverage.

2. Zimbabwe has a wide range of social safety net programs, but the poor remain largely underserved as programs are poorly implemented (targeting, coverage, and monitoring) and financing is erratic and unsustainable. A pilot harmonized social cash transfer program (HSCT) is being implemented with support from UNICEF alongside multiple longstanding cash transfer programs. There are various public works programs implemented by the Government, donors, and NGOs. The Basic Education Assistance Module (BEAM) provides school fee waivers with funding from Government (for secondary students) and donors (for primary students). Assisted Medical Treatment Orders (AMTO) provides fee waivers for health care and there are other small in-kind transfers (Agricultural Inputs; School Feeding; and others). Public Assistance provides support to elderly and disabled poor and indigent families on the basis of a means test. Overall, coverage of safety net programs is low. Public assistance only reaches about 3 percent of extremely poor households, while the HSCT reaches about 20,000 households with plans to expand to 55,000 (which represents about 11 percent of extremely poor households). On average, about 48 percent of students identified as needing BEAM through the community selection process actually receive BEAM financing. AMTO provides benefits to 15,000 out of 24,000 targeted beneficiaries. Coverage of public works programs is unknown, but most programs target food insecure areas with limited opportunities for the urban unemployed to participate in.
3. **Social insurance (pensions) cover formal workers only, and most poor and vulnerable are not covered by any kind of pension or insurance.** Zimbabwe operates two main pension schemes, with public service pension scheme being the largest provider (44 percent) followed by the National Pension Fund (38 percent). Approximately 11.9 percent of males and 8.9 percent of females in the 60+ age cohort receive a pension, while self-employed workers are not covered. In addition, with the current structure and parameters, the pension system is not fiscally sustainable.

4. **At least five ministries implement active labor market programs, but programs are not well aligned to labor market needs and do not reach many of the vulnerable.** The Ministry of Labor and Social Services provides job intermediation services. The Ministry of Youth, Indigenization and Empowerment provides non-formal training, micro-finance, and entrepreneurial training for persons with disabilities. The Ministry of Small and Medium Enterprise and Co-operative Development provides entrepreneurial training and financing. The Ministry of Education provides second chance education and non-formal training and the Ministry of Women’s Affairs, Gender and Community Development provides business loans for women. These programs reach less than 1 percent of unemployed youth.

5. **Social protection programs were adversely affected during the recent economic and political crisis.** Fiscal revenues became erratic and the number of beneficiaries declined. For example, beneficiaries of education fee waivers declined from about 969,900 in 2005 to 74,970 in 2007, increased to 734,590 in 2010 with support from donors, but decreased to 406,300 in 2012. Access to employment based social protection declined when about 248,000 workers were retrenched between 2004 and 2011. The number of contributors to the National Pension Scheme (NPF) declined from 1.3 million in 2005 to 1.2 million in 2006 and remained at about that level through 2010. The value of pensions collapsed in the face of hyperinflation.

6. **Since the crisis, the government has made advances in reinvigorating its social protection system but programs remain fragmented and comprise a collection of programs rather than a coherent system.** The Social Transfers Policy Framework (STPF) is an initiative of the government which aims to bring coherence to social transfers and the government initiated HSCT attempts to target households based on poverty. The STPF proposes to harmonize social transfers, improve their quality, relevance and adequacy, and prescribe guidelines to all stakeholders in the design and implementation of social transfers. The STPF includes: (i) proxy means tested HSCT for labor constrained households; (ii) productive community works (PCW) for labor endowed households; (iii) agricultural inputs for the rural poor; and (iv) fee waivers for health and education. A Public Community Works Policy Framework and Operational
Guidelines for PCW programs and for the HSCT have been developed. At the same time, the government has moved to restore the value of pensions.

7. **Additional data and analysis is required to inform social protection reforms.** This includes evaluating the incidence and poverty impacts of social assistance programs, costing of expanding coverage of social assistance programs and pension reform scenarios, assessment of labor market needs, and evaluation of labor market programs. Information on the range of public works programs implemented by international and NGO agencies, as well as analysis of the requirements and options for strengthening targeting systems is also needed. For the most part, there are no evaluations of the actual impact of social protection programs.

**CONSTRAINTS/CHALLENGES**

8. **There is important scope for further harmonization of social transfer programs.** Cash and in-kind transfers as well as public works programs are all administered by different units in the MLSS and have separate administrative and information systems. This results in duplication of functions and limits opportunities for economies of scale and capacity building. Strategies for linking households with labor market programs are needed. PCW should be implemented in a systematic and continuous manner as opposed to ad hoc and scattered. Further harmonization of cash and in-kind transfers is possible, for example, by ensuring that beneficiaries of the HSCT receive BEAM assistance. Similarly, it is possible to harmonize WFP food provision with the HSCT so that cash, instead of food, is provided in districts where markets function.

9. **There are no temporary employment opportunities for unskilled workers that provide timely and predictable benefits so they can plan accordingly.** Zimbabwe’s public works are project based, which means that once a project is completed the opportunity for employment in the community ends, at least for that project cycle. Communities may or may not get a second project.

10. **Pension schemes are not sustainable.** Both the Public Service Pension Fund (PSPF) and the National Pension Fund (NPF) are defined benefit schemes financed on a pay-as-you-go basis where contributions from current workers are used to pay for pensions. The standard retirement age for both schemes is 60 (early retirement possible at age 55). The PSPF is not pre-funded, contributions from civil servants and government are treated as general revenue and benefits are disbursed from the Consolidated Fund. The NPF provides old-age, invalidity and survivors’ pensions and grants for publicly and privately employed persons. An estimated 20 percent of the working age population contributes but despite the recent increase in the contribution rate, future liabilities of the NPF are only partially funded.
11. **Labor market programs are supply driven with limited private sector participation in the design of the programs.** Other constraints include the low levels of coverage; limited English and math skills of trainees; outdated equipment; and fees that present barriers to training for the most vulnerable. There is duplication in the provisions with no mechanism for determining whether individuals benefit from more than one scheme, particularly finance schemes.

12. **Social protection spending in Zimbabwe is about average for the Africa region, however, fiscal flows are unreliable, benefits are often late or not paid at all, and there is room for increased efficiency of the spending.** Social assistance expenditures (including safety net and labor market programs) are estimated at US$113.3 million (or 1.2 percent of GDP). An estimated 5.1 percent of GDP is spent on pensions (including government, employer, and individual contributions). The variance between budgeted and actual expenditures has been significant. Paying some benefits and not others increases inequities and inefficiencies in the allocation of resources for beneficiaries, both individuals and institutions. Increased harmonization of programs presents an opportunity for increased efficiencies.

**OPTIONS**

13. **The significant gaps in the social protection system relate to the coverage and quality of programs and not to the menu of programs offered.** However, Zimbabwe needs to rationalize spending for social protection and also improve the effectiveness of expenditures by: a) prioritizing existing programs; b) improving the effectiveness of these prioritized programs (targeting, coverage, as well as funding and monitoring of programs); c) strengthening pension systems; and d) developing a social protection system with improved coordination and synergies through the required operational tools (management information systems, registry of beneficiaries, monitoring and evaluation, and payment systems).

14. **Zimbabwe needs a fully articulated social protection strategy.** The country currently has an uncoordinated set of safety net programs implemented by multiple agencies and a patchwork of policy documents that cover some aspects of social protection. However, these do not form a coherent whole. The strategy should spell out the government’s objectives for its social protection system; the resources and programs that will be needed to achieve those objectives; and the arrangements for implementing the strategy. The strategy should include a comprehensive reform plan and clear long-

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32 Difficulties in accessing data on actual expenditures required the use of revised estimates for some programs and actual expenditures for others. In addition, since donor resources do not flow through the government budget, it was necessary to use data on Government spending for 2012 and data on donor spending for 2010. This is clearly not an ideal approach; however, it does allow for some tentative estimates on social assistance spending.
term objectives. It should also be based on extensive consultations with stakeholders and a far-reaching communications strategy to inform the public of the particulars of the strategy. The first step would be to establish an interagency committee with a mandate to oversee the development and implementation of the strategy.

15. **Cash transfers need to prioritize the extremely poor households.** From the fiscal and institutional capacity perspectives, it is not possible to target all poor, so it would make sense to prioritize the extreme poor. In Zimbabwe, the extreme poor represent roughly one-quarter of the population, and, given the pattern of vulnerability, it would make sense to focus on extremely poor children, elderly, and persons with disabilities. Further development of targeting systems would be required to ensure that programs reach the most vulnerable. A fully harmonized cash transfer program in which all cash transfers are implemented as a single program targeted to extremely poor households with children, elderly and/or disabled persons is needed.

16. **Social transfers need to do a better job of reducing barriers to education and health.** Financial constraints continue to be the primary reason that children are not in school. An improved allocation strategy in which BEAM grants to schools are determined based on the incidence of poverty in a catchment area is required. Expanded coverage BEAM and cash transfers, higher cash transfers for secondary rather than for primary school students, could also help. Despite free primary health care, the main barrier preventing the poor from seeking treatment for illness is cost. Ensuring the quality of service in the public health sector (including availability of prescription medicines) with better targeting of fee waivers for secondary and tertiary care would reduce obstacles to health care among the poor.

17. **A comprehensive approach to the overall pension system is needed for long term fiscal sustainability and benefit adequacy.** Parametric reform of pension schemes (contributions, benefit and retirement rates) is needed. Without reforms, the NPF will need to start to deplete reserves in 2029. At the same time, Zimbabwe is facing fiscal pressure from the increasing costs of public sector pension scheme, which account for 4.1 percent of GDP. Any reform option needs to also consider the converging rules of the NPF and PSPF to avoid distortions in labor mobility due to pension benefits provided. The NPF recently increased the contribution rate and ceiling, both of which are expected to contribute to improved fiscal sustainability. However, additional parametric changes, in particular in the eligibility requirements (e.g. benefit calculation, retirement age), might be considered to further improve fiscal sustainability and benefit adequacy. Whatever improvements are introduced to the NPF, expanding pension coverage would continue to be a serious challenge given the high informality in labor markets. One option to overcome this issue could be a voluntary savings arrangement for informal workers. At the same time, Zimbabwe is facing fiscal pressure from the increasing costs of PSPF.
with contributions not sufficient to cover the pension payments leading to a projected deterioration in the fiscal balance. Government needs to consider an overhaul of the PSPF to contain the increasing fiscal burden.

18. **Zimbabwe needs to ensure that the social protection system responds to crisis by making a strong fiscal commitment to its safety net.** In order to do this, Zimbabwe would need to identify Government resources for safety net programs as opposed to its current reliance on external financing. In addition, budgets need to be predictable and may even need to be scaled up in times of crisis. This can be partially achieved through increased efficiency of existing spending on social assistance, but it will also require giving greater priority to the safety net.
1. **Preamble:** The World Bank has prepared a series of Economic Recovery Notes to guide its engagement with the new administration in Zimbabwe. The notes are intended to outline issues, challenges and policy options in the key sectors of the economy. The Bank is planning to prepare a comprehensive Infrastructure Policy Note over the coming months to update the Bank’s knowledge base in all infrastructure sectors. This note is a primer for the Infrastructure Policy Note and addresses the key infrastructure sectors: water, energy, transport and Information and Communication Technology (ICT), with a focus on water and energy, the two sectors in which the Bank has been most active over the past 5 years. The note includes an overview of infrastructure and an annex on each infrastructure sector.

**OVERVIEW OF INFRASTRUCTURE IN ZIMBABWE**

2. **Raising Zimbabwe’s infrastructure endowment to that of the region’s middle-income countries could boost annual economic growth by 2.4 percent.** Many studies have shown the links between improved infrastructure and economic growth. The overall improvement in per capital growth rate over the past two decades in Southern Africa was 2.1 percent, of which 1.1 percent is attributable to better structural policies and 1% to improved infrastructure. Infrastructure is a key component of the investment climate, reducing the costs of doing business and enabling people to access markets. In the case of Zimbabwe, infrastructure is key to unlocking the growth potential in mining, agriculture, manufacturing and tourism. If Zimbabwe’s infrastructure could be improved to the level of Mauritius (the African leader) annual per capita growth rates would be 2.4% higher than they are at present (World Bank, 2011). This impact would come from primarily from improvements in ICT, increase in power-generating capacity and better road infrastructure (figure 1).

![Figure 1: Potential contributions of infrastructure to annual per capita growth (%) (World Bank, 2011)](image)
3. **Zimbabwe made significant progress in infrastructure development in its early period as an independent state.** By African standards, Zimbabwe has impressive backbone infrastructure, including power, roads, ICT, and water. The country is historically well integrated with its neighbors when it comes to power and transport networks, allowing Zimbabwe to participate in regional trade and act as a critical transit country for landlocked neighbors Zambia and Botswana and a key link in the north-south surface corridors.

4. **However, low levels of infrastructure investment over the past decade have led to a dramatic deterioration of the country’s competitiveness and poor service delivery.** Energy demand – estimated at over 2,000 MW far outstrips supply, at less than 1,200 MW, leading to black-outs and unreliable services. Half the trunk road system is in a state of disrepair. Water supply and sanitation services, once the envy of the continent, have deteriorated dramatically resulting in the 2009 cholera epidemic that caused 4,300 deaths and over 100,000 cholera cases.

5. **Looking ahead, Zimbabwe faces a number of important infrastructure challenges.** Zimbabwe’s most pressing challenges lie in the power and water sectors. Inefficient and unreliable power supply poses major risks to the economy, while the maintenance and upgrading of existing power infrastructure no longer looks to be affordable. At the same time, overhauling the water and sewerage system is imperative for preventing any future public health crisis.

6. **Since 2009, the Government has started to reinvest in infrastructure to address the estimated $14 billion capital works needed over the next decade.** In order to achieve the countries “ideal” investment targets such as achieving the MDGs in water, rehabilitation of all transport and energy infrastructure, providing sufficient power generation to meet all demand will require sustained expenditure of almost $2 billion per year over the next decade, with heavy emphasis on rehabilitation; more than half is needed for the power sector. This overall level of spending would represent one of the largest infrastructure burdens for any African country. Investment alone would absorb 31 percent of GDP, roughly twice the unprecedented infrastructure investment effort made by China during the 2000s.

7. **As of today, the country seems to find itself in the difficult position of having more infrastructure assets than it can afford to sustain.** Given the magnitude of the burden, some less ambitious infrastructure spending scenarios should be considered. Zimbabwe has the potential to close this gap by raising additional public funding for infrastructure from increased fiscal receipts of various kinds. The funding gap can be addressed by raising additional financing, lower-cost technologies or less ambitious development targets.
As much as $752 million of additional resources could be recovered each year by improving efficiency (World Bank, 2011). The most vexing problem is the under-recovery of costs in power, roads, and water. Every year up to $321 million is lost due to undercharging in these three infrastructure sectors. Raising power tariffs to cost-recovery levels could save $220 million annually, a better-balanced road fuel levy could bring in an additional $71 million, and more economically reasonable water tariffs could recover additional $48 million per year. Collection of bills also needs to be improved as a result of poor collection discipline; Zimbabwe is losing $255 million per year in the power sector and $18 million per year in the water sector. Overstaffing in power and water parastastals is also quite significant. Cutting staff levels to economically viable benchmarks could save $71 million and $8 million in the power and water sectors, respectively; reducing distributional losses could save another $27 million and $10 million in the water and power sectors, respectively. Looking across sectors, the power and water sectors can benefit the most from tackling identified inefficiencies, followed by the roads sector (figure 3).
Zimbabwe has not captured as much private financing for infrastructure as many of its neighbors. Over the early 2000s, Zimbabwe captured private investment commitments worth only around 0.4% of GDP, predominantly in the ICT sector. Most of Zimbabwe’s peers have done significantly better in this area. Notable are the absence of private investments in the power sector. Countries such as the Democratic Republic of Congo, Liberia, Nigeria, Uganda, Kenya, and Senegal have all captured between 1.8 and 2.5 percent of GDP, while the most successful country in this regard, Guinea-Bissau, has captured in excess of 3% of GDP (figure 4).
10. **Infrastructure in Zimbabwe:** Raising Zimbabwe’s infrastructure endowment to that of the region’s middle-income countries could boost annual economic growth by 2.4%. Zimbabwe made significant progress in infrastructure development in its early period as an independent state; however, low levels of infrastructure investment over the past decade have led to a dramatic deterioration of the country’s competitiveness and poor service delivery. Since 2009, the Government has started to reinvest in infrastructure to address the estimated $14 billion capital works needed over the next decade. As of today, the country seems to find itself in the difficult position of having more infrastructure assets than it can afford to sustain. The funding gap can be addressed only by raising additional financing or, alternatively, by adopting lower-cost technologies or less-ambitious development targets. But due to its economic and political turmoil, Zimbabwe has not attracted as much private finance into infrastructure as other African peers.

11. **Water is key to economic development in Zimbabwe.** Historically, Zimbabwe’s economy has been strongly linked to climate (rainfall in particular), and so there has been a close link between water resources and the overall economy. Before and for almost two decades after independence, Zimbabwe employed a water sector strategy that relied on the development of dams, water supply and sewerage systems and irrigation systems coupled with institutional and legal reforms to counter its highly variable climate and meet its growing water needs for domestic supply and irrigation. This was an effective strategy until the late 1990s but failed in the last decade because of the economic and political crisis. Rehabilitating dams, restoring power supply and irrigation systems, rehabilitating water and sewerage systems and reinstating the institutional and legal reforms as part of the country’s recovery while essential will no longer be sufficient, because human induced climate change poses an additional burden and threat to long-term economic recovery that is not yet widely recognized, appreciated and integrated in development planning.

12. **Improving water security--how well water resources are harnessed, utilized, conserved, protected and managed for multisectoral uses--is a core development challenge for Zimbabwe’s economic recovery, growth and social development** (Government of Zimbabwe, 2013). Water is central to the performance of key sectors of the Zimbabwean economy – rural and urban development, agriculture, energy, industry, mining, tourism, and the environment. Figure 5 shows a close relationship between precipitation and GDP from the early 1980s until the late 1990s. However, this link was broken at the start of the new millennium when other factors, including new settlement
policies and increasing international isolation led to decline in GDP even when precipitation remained high. Revitalizing the more than 160,000 ha of irrigated agriculture, and restoring the extensive network of dams operated by ZINWA and adapting to climate change will be a key challenge going forward.

![Figure 5: The correlation between rainfall and GDP in Zimbabwe (GoZ, 2013)](image)

13. **Water supply and sanitation services, once the envy of the continent, are in a state of disrepair.** For example, access to urban sanitation in 1990 was at 99% one of the highest of the developing world fell to 40% in 2008. This deterioration led to the cholera crisis in 2008 that claimed 4000 lives and 100,000 cases. The Government has to be commended for the hard work it has done over the past 4 years to restore water and sanitation services, but even more needs to be done to rehabilitate water and sanitation services across the country to avoid future cholera cases, and other water-borne diseases such as typhoid and dysentery.

14. **Over the past decade there has been widespread failure in the sector, primarily as a result of a collapse of revenue and a loss to the sector of technical expertise.** Water services are characterized by intermittent water supply, untreated sewerage, high losses and high non-revenue water (for example, estimated at 57% for Harare), poor billing and low revenue collection rates, weak institutional capacity and generally low funding. Service in rural areas mainly relying on hand-pumps and pit latrines are significantly worse, and issues such as open defecation have become a major problem (estimated at 37% in rural areas). Spending in order to redress this critical situation has been low, resulting in few improvements being made over the past year and the threat of water related diseases such as cholera and typhoid remaining high.

**CHALLENGES**

15. **Due to lack of proper maintenance, Zimbabwe’s water and sanitation infrastructure is in very poor condition, constituting a threat to public health.** The deterioration of the water network can be seen in the extremely high distribution losses,
which amount to almost half of the water produced, and does not compare favorably with regional comparators (figure 6). Along with technical water supply problems, the quality of service has greatly deteriorated in recent years. Access to shallow wells and boreholes is the prevalent form of water supply covering about 50 percent of the population, significantly higher than for the peer group. But in 2004 around 75 percent of hand pumps were not functioning, and the situation has worsened since then.

![Figure 6: Non-revenue water in selected countries (World Bank, 2011)](image)

16. **Zimbabwe’s water quality has deteriorated significantly over the last decade.** The consequences of pollution and deteriorating water quality are being felt economy-wide and across all segments of the society, with greatest impact on the poor who have fewer alternative sources of water. With most cities located upstream of their raw water sources the cost of treating water in urban areas has significantly increased, while utility revenues have dwindled. The MWRDM is preparing a strategy for protecting water sources and managing water quality.

**POLICY OPTIONS**

17. **Since 2009, the Government has been committed to restoring the functionality of the water sector, and has made significant strides.** Partly as a result of the cholera crisis in 2008/9, the Government has made a great effort to address the challenges in the sector, in particular: (i) Restoration of the National Action Committee: in 2010, the sector agreed on an expanded scope of the National Action Committee to manage water across the seven affected ministries and multiple service providers and implementing agencies under the chairmanship of the Ministry of Water Resources Development and Management (MWRDM); (ii) National Water Policy: In December 2012, the Government approved a new National Water Policy that clarifies the policy
positions on key issues such as institutional responsibility, sector financing and technical standards. The policy, the only sector policy approved by the GNU provides the MWRDM the necessary authority to implement the needed reforms in the sector; (iii) Water Sector Investment Framework: the Government is developing a framework to guide all sector investment decisions, both from the PSIP and other financiers. The draft analysis will be ready for the 2014 budget cycle in order to influence the 2014 budget and will provide the economic rationale for investments in various sub-sectors, i.e., water resources (dams, pipelines), urban and rural water supply and sanitation, currently all split between different ministries; (iv) Scaling-up of rural water supply and sanitation: the Government and UNICEF are implementing a rural water supply and sanitation upgrading program in five of the eight provinces in order to rehabilitate the 50,000 hand pumps currently serving rural areas. Implementation of this program is underway; and (v) urban water supply and sanitation: a number of Development Partners such as AfDB, GiZ, AusAid and others are supporting urban water supply and sanitation, but a larger, more systematic program to rehabilitate urban water and sanitation systems is needed to tackle the problem.

18. **However, there are significant gaps in policy, capacity and investments needed to fully restore the sector.** While the sector has made significant achievements over the past 5 years culminating in the approval of the National Water Policy, there are a number of gaps in implementation of the policy, and the necessary capacity and resources needed for a fully functional sector, in particular: (i) implementation of the key institutional and financial policies in the National Water Policy such as the establishment of a regulatory framework, clarification of the role of urban and rural local authorities as water service authorities, further consolidation of the central government oversight of the sector, clarification and support to the National Action Committee to support in the coordination of the sector, and advise on investment allocation; (ii) identification and addressing key policy, legal and regulatory misalignments between the constitution, policy, various acts impacting the sector and current institutional arrangements; (iii) further commercialization of water service deliver to ensure financially sustainable water service providers and efficient delivery of services through cost-reflective tariffs, improved revenue collection and cost saving measures, while safeguarding the affordability of tariffs for consumers, and ensuring service providers are held accountable for quality services; (iv) implementation of the water sector investment framework, once prepared. Early drafts of the analysis show that much greater benefits will be obtained through a priority focus on rehabilitation rather than new works, and attending to water losses rather than investing in new supplies; (v) investments in water supply and sanitation need to prioritize those that will result in improved sanitation and hygiene outcomes. In urban areas, this means prioritizing onsite water connections and cost-effective means of treating and disposing human waste. In rural areas, this means rehabilitating hand pumps and adopted strategies to reduce open defecation; (vi)
improving the financial viability of urban utilities is necessary to underpin and sustain improvements in services. This means raising tariffs where these are below cost, strengthening systems to bill and collect revenues, implementing fair and robust credit control policies and substantially reducing wastages and leakages in the system (physical and financial); (vii) mid-term strategies should address investment needs to tackle the lack of capacity in production, distribution and treatment; (viii) a climate change strategy for the water sector needs to be developed and implemented to inform water resources planning, design and management decision making.

19. **Regional leadership within the context of the Zambezi River basin has the potential to unlock significant growth opportunities.** Zimbabwe is set to host the Zambezi Watercourse Commission from January 2014. The “Agreement on the Establishment of the Zambezi Watercourse Commission” (the ZAMCOM Agreement) came into force on June 19, 2011 after six of the eight riparian countries completed their ratification processes and deposited their ratification instruments with the SADC Secretariat. Zambia acceded to the agreement in July 2013 while Malawi, who signed on July 13, 2004, has not yet acceded. The principle objective of the ZAMCOM Agreement is “to promote the equitable and reasonable utilization of the water resources of the Zambezi watercourse as well as the efficient management and sustainable development thereof”. Results of a multi-sectoral investment analysis have shown that cooperative water development in the Zambezi River basin could result in substantial benefits. The development of hydropower generation plans could facilitate over US$10 billion in investment alone, improving regional energy security by increasing firm energy production by 35,000GWh/yr and providing an additional 60,000 GWh/yr in average energy. Ensuring a predictable and transparent process to facilitate investments on the Zambezi River (such as the proposed 1600MW hydro-electric scheme at the Batoka Gorge) could provide much needed investments and bridge the energy security gap. The ZAMCOM Secretariat will facilitate development of a Strategic Plan for the Zambezi River basin that has the potential to guide investments and consolidate the regional gains that can be made through cooperative ventures.
ANNEX 2: ENERGY

SITUATION ANALYSIS

20. **Infrastructure in Zimbabwe:** Raising Zimbabwe’s infrastructure endowment to that of the region’s middle-income countries could boost annual economic growth by 2.4%. Zimbabwe made significant progress in infrastructure development in its early period as an independent state; however, low levels of infrastructure investment over the past decade have led to a dramatic deterioration of the country’s competitiveness and poor service delivery. Since 2009, the Government has started to reinvest in infrastructure to address the estimated $14 billion capital works needed over the next decade. As of today, the country seems to find itself in the difficult position of having more infrastructure assets than it can afford to sustain. The funding gap can be addressed only by raising additional financing or, alternatively, by adopting lower-cost technologies or less-ambitious development targets. But due to its economic and political turmoil, Zimbabwe has not attracted as much private finance into infrastructure as other African peers.

21. **Zimbabwe’s power sector plays a strategic role in enabling and promoting economic activity across the country and in the delivery of key social services.** Because of its geographic location, Zimbabwe’s power network infrastructure is also vital to the neighboring countries within the Southern Africa Power Pool. However, power demand is almost double current supply, and there is extensive suppressed demand that further dampens economic recovery and growth. In addition, the Zimbabwe Electric Power Supply Authority (ZESA) once one of the best in Africa is now in a seriously compromised physical and eroded financial state. There is an urgent need to rehabilitate existing energy assets to restore system stability and security; as well as to improve the financial performance of the utility.

22. **Energy is among the top-three constraints faced by firms in Zimbabwe.** According to the 2011 Enterprise survey, 47 percent of firms ranked electricity supply as a severe constraint to business. Estimated losses average almost 8.9 percent of total sales in Zimbabwe. Just reducing these costs would significantly increase competitiveness with imports, or ability to compete with lower prices in export markets. Overall, increasing the efficiency of service delivery by parastatals is a key factor in restoring firms’ competitiveness. Electricity shortages are also affecting the agricultural sector, and in particular tobacco curing, compromising quality.

23. **Zimbabwe’s installed capacity and access to electricity compare favorably to countries of similar income in Africa.** Total installed capacity at 1,960 megawatts (MW) and per capita capacity at 146 MW are three and seven times higher, respectively,
than what the nation’s African low-income peers have in place. Zimbabwe’s overall access rates and rural access rates are also better than the average for African low income countries. Estimates from 2009 indicate that these access levels had improved to 40 percent of Zimbabwe’s population from 30 percent in the early 2000s. Almost 80 percent of the urban population had access to electricity and almost 20 percent of the rural population had access to electricity. Most of this performance is the result of systematic investment carried out in and around the late 1980s, when Zimbabwe established a relatively good power infrastructure backbone with decent installed capacity and a recognizable national grid, and attained good access levels. Thus, unlike many other parts of Sub-Saharan Africa, Zimbabwe has developed the semblance of a national grid.

CHALLENGES

24. **However, Zimbabwe’s power infrastructure is starved of new investments.** Zimbabwe has not seen any investments to expand its generation infrastructure since 1988, when Hwange Power Station added 440 MW. Only around 60 percent of the 1,960 MW of installed capacity is operational. Installed capacity in per capita terms is following a clear downward trend. Power transmission and distribution networks have been further corroded due to damage and theft. ZESA (Zimbabwe Electricity Supply Authority), the integrated power utility, faces an unsustainable financial situation that leaves no room for new investments. Sixty-eight percent of Zimbabwe’s installed capacity is thermal as of 2008, and ZESA uses 2.4 million tonnes of coal per year for thermal power generation. Between over half of its coal comes from the state-owned Hwange Colliery Company, which has continuously subsidized the coal ZESA buys. Other inputs such as water (for hydropower generation) and transportation services are also provided at below-market costs. Yet, despite the highly subsidized prices, ZESA was unable to pay Hwange for its coal supply. The inability of ZESA to pay for coal has in turn weakened the financial capacity of its supplier.

25. **Recent efforts to level tariffs with costs have not been enough to allow ZESA to reach cost-recovery status.** The average true cost of power is about $0.10 per kilowatt-hour (kWh) in Zimbabwe, which is already relatively low by African standards. Nonetheless, due to subsidies of various kinds, at present tariffs amount to only $0.06 per kWh, among the lowest in Africa (figure 7)
26. **Progress in rehabilitation of power generation has been slower than planned.** Investment by the central government over the last three years (2010-2012) reached US$68 million, with US$169 million financed by utilities. The significant problems causing disbursement delays of funds available through fiscal support persist: (a) slow approval process of tenders through the State Procurement Board; (b) Uncertainty of funding being available when needed to meet contractual obligations; and (c) late availability of funds leading to cash flow problems in the procurement process.

27. **ZESA’s “hidden costs” remain high in absolute terms, but they have been coming down in recent years.** The World Bank (2011) calculates the hidden costs associated with losses, underpricing and collection inefficiencies. Compared to other southern African countries, hidden costs in 2009 are still high at around 400% of sector revenues, second only to those found in the Democratic Republic of Congo (figure 8). While not included in the estimates of hidden costs in figure 5, labor-related inefficiencies further curtailed ZESA’s financial security, draining as much as 16 percent from revenues in 2009. As of 2007, ZESA employed around 6,455 staff and was plagued by low staff utilization that reduced the scale of operations. The number of workers per gigawatt-hour of power produced was 0.86, four times larger than the figure for several other countries.
POLICY OPTIONS

28. **Rehabilitation of Energy Assets**: Investments are needed to (a) repair the ash dam retention wall at the Hwange power station; (b) repair critical items at Kariba dam; (c) restore generation capacity and reliability at both Hwange (from about 400MW to 700MW), at Kariba and (d) ensure system stability in both transmission and distribution to reduce outages.

29. **Improving financial viability**: Restore the financial viability of the utility by improving electricity cash flows/revenue generation after years of uneconomic tariffs and other leakages, and implement broad policies and institutional reforms.

- Tariffs should be reviewed (level and structure) to reflect efficient system costs. This should include a review of all cost components including labor costs. This review should also be accompanied by inclusive-oriented policies (lifeline tariffs for low-income users) and consumer education / guidance (improve electricity saving through demand side management).

- Improve metering strategy. This includes finding the way to effectively meter within premises, defining a more predictable and efficient load shedding policy, and advancing with pre-paid metering (which, according to ZETDC, indirectly helps to rationalize consumption).

- For the mid-term, government should delineate its view on the electricity sector, in order to develop a strategy for rehabilitation and expansion of infrastructure, i.e., whether it should be done through ZESA, in which case it should delineate the options for strategic partnerships, or through independent players, in which case it should delineate licensing provisions that enhance
business climate to potential investors in generation, transmission, and distribution, establish interconnection rules, etcetera. Under the option of the government retaining full control on parastatals, assess the alternative of opening the room for private participation through the subsidiaries (see TelOne).

- Consider pursuing regional power sector integration. There are generation projects in the region that Zimbabwe could try to sign up for which would deliver power much sooner that the big projects even if these go ahead. Discarded coal-fired generation in Mozambique is a good example. An important caveat to the regional approach is that SADC trade is presently constrained by transmission bottlenecks, particularly in the Zimbabwe system. Even so, some additional power could be made available from Mozambique in the short term. The Government may consider the feasibility of transmission projects rather than generation projects, particularly a project as large as Hwange.
ANNEX 3: TRANSPORT

SITUATION ANALYSIS

30. **Infrastructure in Zimbabwe**: Raising Zimbabwe’s infrastructure endowment to that of the region’s middle-income countries could boost annual economic growth by 2.4%. Zimbabwe made significant progress in infrastructure development in its early period as an independent state; however, low levels of infrastructure investment over the past decade have led to a dramatic deterioration of the country’s competitiveness and poor service delivery. Since 2009, the Government has started to reinvest in infrastructure to address the estimated $14 billion capital works needed over the next decade. As of today, the country seems to find itself in the difficult position of having more infrastructure assets than it can afford to sustain. The funding gap can be addressed only by raising additional financing or, alternatively, by adopting lower-cost technologies or less-ambitious development targets. But due to its economic and political turmoil, Zimbabwe has not attracted as much private finance into infrastructure as other African peers.

31. **Zimbabwe has a relatively dense national road network**. Total road density is 100 km/1,000 square kilometers (km2) doubles the figure for neighboring Zambia and almost triples that of Mozambique and the network spanned almost 44,000 km in 2008. The classified network roads under state jurisdiction totaled 18,253 km in 2010, according to the recent Zimbabwe Road Condition Survey, while there are an additional 5,000 km of urban roads, and around 39,000 km of unclassified roads. The rural-accessibility index in Zimbabwe, at 46 percent, is more than double the regional averages.

32. **Zimbabwe has strong road connections with the SADC**. Zimbabwe is linked to its neighbor South Africa the largest regional economy and home to the busiest port in Africa and other countries such as Mozambique, Botswana, Zambia, the Democratic Republic of Congo, Malawi, and Tanzania through the North–South Corridor, the most extensive corridor system in the region. In addition, the North–South Corridor serves as a link to other important corridors that branch off from it, such as the Trans-Kalahari, Beira, Lobito, Dar es Salaam, and Nacala corridors (Curtis 2009). Along the corridor, the core road artery runs 7,500 km from Dar es Salaam in Tanzania to Durban in South Africa, via Lusaka, Zambia, through the Chirundu border crossing and on to Harare, Zimbabwe, and then into South Africa at Beitbridge. But as a result of recent political unrest in Zimbabwe, an alternative route has opened up, bypassing Zimbabwe has a functional railway network.
The state-controlled National Railways of Zimbabwe (NRZ) rail network has a single-track route length of 3,077 km, of which 2,759 km are operational. The Bulawayo Beitbridge Railway (BBR), a build-operate-transfer (BOT) project, consists of around 317 km and runs from Beitbridge on the border with South Africa to Heany Junction near Bulawayo. Zimbabwe has the highest rail-traffic density in the region aside from South Africa. NRZ has very high freight density at around 902,000 tonne-km/km, while most other southern African railways are serving substantially less. Passenger density is also comparatively high.

**CHALLENGES**

While Zimbabwe boasts one of the most extensive road networks in the region, its condition has deteriorated rapidly over the past two decades. As of 2008 Zimbabwe has one of the lowest percentages of roads in good condition the region. The roads in poor condition include key regional arteries, such as the corridor leading to the port of Beira in northern Mozambique, hindering the competitiveness of the port even though it is significantly closer to Zimbabwe than the port of Durban. The 2010 Zimbabwe Road Condition Survey paints an even more dismal picture of the current quality of classified roads. Only 34 percent of total classified roads are in fair or good condition and only 14% are in good condition. The quality of paved/sealed roads is somewhat better than that of gravel and earth roads; nevertheless, a daunting 50 percent of classified paved roads are in poor condition and require costly rehabilitation. Based on the results of this survey, the government estimates that $2.9 billion would be needed to rehabilitate Zimbabwe’s entire classified network.

Based on the physical configuration and condition of Zimbabwe’s infrastructure network, it is possible to estimate the resources that would be needed to clear the current rehabilitation backlog and maintain the network in good condition. Comparing recent spending against these norms indicates that Zimbabwe has not succeeded in securing adequate resources for road-network preservation and Maintenance. There is a shortfall of about 50 percent between recent spending on road maintenance and rehabilitation and the requisite amounts. As the benchmarking shows, this situation is quite commonplace in Sub-Saharan Africa (figure 9).
POLICY OPTIONS

36. **The biggest challenge facing Zimbabwe’s transport sector is institutional capacity, especially in road network management.** The importance of a well performing transport sector especially to underpin Zimbabwe’s economic turnaround cannot be overstated. It would be expected that a more robust economy would induce additional strains and stresses on the transport infrastructure. This interplay between the transport infrastructure and Zimbabwe’s economic performance requires judicious management. There is therefore a pressing need for a review of the transport sector and to also address capacity constrains in the roads, railways and urban transport subsectors.

37. **With respect to regional integration,** Zimbabwe should consider improving the condition of the international road corridors that pass through its territory, along with reducing transit costs and transit time, to gain the most from its strategic location in the heart of the southern Africa region and its proximity to the region’s largest economy and trading partner, South Africa.

38. **The Government should consider improving road sector revenues** through a review of the existing road user charging system.

39. **Zimbabwe needs to function more effectively as a regional transit country.** Zimbabwe is on the crossroads especially within SADC, occupying a strategic position on the North–South corridor but it faces one of the highest export and import costs in the region. The administrative costs and delays associated with moving freight across its borders are significant and include lengthy documentation time and high customs clearance fees and terminal-handling charges.
ANNEX 4: ICT

SITUATION ANALYSIS

1. **Infrastructure in Zimbabwe**: Raising Zimbabwe’s infrastructure endowment to that of the region’s middle-income countries could boost annual economic growth by 2.4%. Zimbabwe made significant progress in infrastructure development in its early period as an independent state; however, low levels of infrastructure investment over the past decade have led to a dramatic deterioration of the country’s competitiveness and poor service delivery. Since 2009, the Government has started to reinvest in infrastructure to address the estimated $14 billion capital works needed over the next decade. As of today, the country seems to find itself in the difficult position of having more infrastructure assets than it can afford to sustain. The funding gap can be addressed only by raising additional financing or, alternatively, by adopting lower-cost technologies or less-ambitious development targets. But due to its economic and political turmoil, Zimbabwe has not attracted as much private finance into infrastructure as other African peers.

2. **The ICT sector of Zimbabwe has shown relative progress during the past years though faces some challenges that are slowing down the pace of progress.** Support from the government and donor agencies in targeted areas of the ICT sector can help unlock the full potential of ICT in Zimbabwe. Despite Zimbabwe’s political and economic situation, it has maintained parity with Sub-Saharan African averages for many ICT indicators. Fixed telephone line penetration exceeded the Sub-Saharan average in 2008 and Internet access penetration was about the same. Mobile penetration has lagged due to chronic network underinvestment as a result of the country’s economic situation. But the market more than doubled in 2009, lifting mobile subscriptions per 100 inhabitants to 24, reducing the gap between Zimbabwe and the rest of Sub-Saharan Africa.

CHALLENGES

3. **Zimbabwe has made some institutional reforms such as the creation of the Postal and Telecommunications Regulatory Authority of Zimbabwe (POTRAZ).** The country has introduced competition in the mobile sector with three operators: Econet, Telecel, and Net-One. It is also moving toward a streamlined licensing system. Despite the reforms, the level of competition remains low. There is only one fixed-line operator and four Internet service providers (ISPs), and Econet dominates the mobile market. Fixed operator Tel-One and its mobile subsidiary Net-One are state owned. Foreign investment is limited to Telecel, which is 60 percent owned by Orascom of Egypt.
4. **A major issue has been the country’s rampant inflation causing frequent tariff changes to ICT pricing.** The dollarization of the economy in 2009 brought this to an end by introducing stability to tariffs, which are now expressed in U.S. dollars. Zimbabwe’s fixed-line and mobile retail pricing is similar to peer averages. Fixed broadband is expensive, almost twice as much as the Sub-Saharan average, which is already high by international standards.

5. **Internet-access penetration in Zimbabwe is average for the southern African region.** There are no comprehensive official data on the number of Internet users in Zimbabwe, though the Zimbabwe All Media and Products and Services Survey found that 22 percent of urban dwellers aged 15 years and older used the Internet in mid-2010 (Ndlela 2010). This amounts to some 645,000 people or 5.1 of the total population. International connectivity is a challenge for Zimbabwe due to its landlocked situation. Much of Zimbabwe’s international connectivity has been through satellite (figure 10).

![Figure 10: Internet service trends](image)

**POLICY OPTIONS**

6. **Broadband:** Government should formulate a broadband policy and given urgent attention to the reform of ICT parastatals to turn the recent progress of infrastructure development into available broadband at affordable rates. Government should take an aggressive role to foster: (a) ICT policy that coordinates and promotes infrastructure development, maintains competition, establishes a fair interconnection regime, and ensures open access; (b) Urgent reform of parastatals in the ICT sector and capital
injection through possible strategic investors; (c) Effective utilization and disbursement of universal service fund (USF) and new policies for universal access; and (d) Spectrum management and licensing to free up spectrum for broadband and reinforce a market-based, technology-neutral licensing regime.

7. **Electronic Government:** Government can employ new technology trends, including mobile platform, cloud computing, social media, and open government. Government can increase the role of the private sector, including with public private partnerships (PPPs), to offer e-government services. Additional best practices can help alleviate the capacity and resource constraints of the government, and overcome the high-risk, high reward profile of e-government applications.

8. **Mobile Banking for Social Protection and Financial Inclusion:** Mobile banking can serve three important objectives in Zimbabwe: (a) Social protection through electronic cash transfers; (b) Financial inclusion through branchless banking; and (c) ICT-enabled transformation using mobile platform. The growth of new service providers for mobile banking in Zimbabwe is a promising trend. Some caution is warranted since few operators in the world have yet achieved scale. Government can help operators achieve scale by creating demand. Government can serve as an anchor customer of mobile banking by issuing selective government payments electronically.

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