Assessing the impact of Private Sector External Debt on Economic Growth in Zimbabwe.

Technical Paper being done by

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in partial fulfilment of the requirements for qualification as a

GRADUATE FELLOW IN MONITORING AND ANALYSIS OF PRIVATE CAPITAL FLOWS

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DEDICATION

To my first born daughter, Deborah Rumbidzo Greatness

Indeed, greatness is our portion
EXECUTIVE SUMMARY

International capital flows have a considerable influence on growth patterns in recipient countries and positively influences the economic behaviour of these countries. Against this background, it is important to see how these capital flows have impacted on the economic performance of the country. The purpose of this paper is therefore to examine the impact of private sector external debt on economic growth in Zimbabwe for the period 1980-2009. While the macroeconomic determinants of economic growth have been analysed to a considerable extent in a number of empirical works, the incidence of private sector external debt on economic growth has remained largely underexplored.

Against the possibility of a linear relationship between these two variables, the paper combines both quantitative (time series) and quantitative (cross-sectional) analysis of the variable of private sector external debt to establish its contributory effect to economic growth. Using the Ordinary Least Squares approach, after testing for stationarity of the variables in the reduced neoclassical growth model, the study finds evidence of a strong contributory effect of private sector external debt on growth in Zimbabwe. Other significant explanatory variables of economic growth in Zimbabwe found to be positively significant were government expenditure and foreign direct investment, although its contribution was surpassed by private sector external debt. The incidences of public sector government debt and trade openness were found to have a negative impact on debt. These results buttressed the need for continued monitoring and analysis of this variable, which has been underexplored but has been a critical source of finance for development in Zimbabwe.
**LIST OF ACRONYMS**

<table>
<thead>
<tr>
<th>Acronym</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>CS-DRMS</td>
<td>Commonwealth Secretariat’s Debt Recording and Management System</td>
</tr>
<tr>
<td>CTP</td>
<td>Customised Training Program</td>
</tr>
<tr>
<td>DMFAS</td>
<td>Debt Management and Financial Analysis System</td>
</tr>
<tr>
<td>DMO</td>
<td>Debt Management Office</td>
</tr>
<tr>
<td>DOD</td>
<td>Debt Outstanding Disbursed</td>
</tr>
<tr>
<td>DRI</td>
<td>Debt Relief International</td>
</tr>
<tr>
<td>ED</td>
<td>External Debt</td>
</tr>
<tr>
<td>ELCC</td>
<td>External Loans Coordinating Committee</td>
</tr>
<tr>
<td>FDI</td>
<td>Foreign Direct Investment</td>
</tr>
<tr>
<td>FDP</td>
<td>Fellows Development Programme</td>
</tr>
<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
</tr>
<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
</tr>
<tr>
<td>LIBOR</td>
<td>London Interbank Offered Rate</td>
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<tr>
<td>MEMFI</td>
<td>Macroeconomic &amp; Financial Management Institute of Eastern &amp; Southern Africa</td>
</tr>
<tr>
<td>MOF</td>
<td>Ministry of Finance</td>
</tr>
<tr>
<td>MTP</td>
<td>Medium Term plan</td>
</tr>
<tr>
<td>NBER</td>
<td>National Bureau of Economic Research</td>
</tr>
<tr>
<td>OECD</td>
<td>Organization for Economic Co-operation and Development</td>
</tr>
<tr>
<td>PCMS</td>
<td>Private Capital Monitoring System</td>
</tr>
<tr>
<td>PGED</td>
<td>Private Sector Government Guaranteed External Debt</td>
</tr>
<tr>
<td>PNED</td>
<td>Private Sector Non-Guaranteed External Debt</td>
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<tr>
<td>PPGED</td>
<td>Public and Publicly Guaranteed External Debt</td>
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<td>PSED</td>
<td>Private Sector External Debt</td>
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<td>Public Sector External Debt</td>
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<tr>
<td>RBZ</td>
<td>Reserve Bank of Zimbabwe</td>
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<tr>
<td>STERP</td>
<td>Short Term Emergency Recovery Plan</td>
</tr>
<tr>
<td>UNCTAD</td>
<td>United Nations Conference on Trade and Development</td>
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<tr>
<td>VAR</td>
<td>Vector Auto Regressive</td>
</tr>
<tr>
<td>WB</td>
<td>World Bank</td>
</tr>
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<td>ZIA</td>
<td>Zimbabwe Investment Authority</td>
</tr>
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</table>
ACKNOWLEDGEMENT

I am forever grateful to God, who made it possible for me to go through this program and to successfully bring to completion my Technical Paper within the stipulated time frame. Indeed it was by his grace. I also extend my profound gratitude to the man who supervised this project, Dr. Satwinder Singh. Doc, you were such a pillar of valuable influence and guidance throughout the crafting of this project. From the very onset, you perceived my interest and to the very end, you logically guided the process. I am so convinced that it was through your impeccable contribution that this piece of work became a reality.

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# TABLE OF CONTENTS

**PUBLICATION** ......................................................................................................................... i

**DEDICATION** ............................................................................................................................... ii

**EXECUTIVE SUMMARY** ........................................................................................................... iii

**LIST OF ACRONYMS** ................................................................................................................. iv

**ACKNOWLEDGEMENT** .................................................................................................................. v

## SECTION ONE .............................................................................................................................. 1

1.1 Background .............................................................................................................................. 1

1.2 Foreign Private Capital Flows and growth ............................................................................. 3

1.2.1 Contribution to growth ...................................................................................................... 3

1.2.2 The growth of Private Sector External Debt ................................................................. 5

1.3 Macroeconomic developments in the country ...................................................................... 7

1.3.1 Evolution of Zimbabwe’s External Debt ......................................................................... 8

1.4 Debt developments in the MEFMI Region .......................................................................... 13

1.4.1 Contribution of external debt to GDP ........................................................................... 13

1.4.2 Efforts to capture private capital flows in the region ................................................... 14

1.4.3 A sample example of Tanzania and Zambia ................................................................... 15

1.5 Problem Statement ............................................................................................................... 17

1.6 Objectives and hypothesis of the Study ................................................................................. 18

1.7 Organization of the Study ...................................................................................................... 19

## SECTION TWO ............................................................................................................................. 20

2.1 What is Private Sector External Debt (PSED) ..................................................................... 20

2.2 Categories of Private Sector External Debt ....................................................................... 21

2.3 Link between Private Sector External Debt and Growth ................................................... 22

2.3.1 Closed economy without private capital flows ............................................................ 23

2.3.2 Open economy with international capital flows ........................................................... 24

2.3.3 Other linkages between private sector external debt and growth ................................ 25

2.4 Empirical studies on the impact of external debt on growth ............................................. 27

2.5 Private Sector External Debt Legal and Institutional Arrangements ................................. 31

2.5.1 The Legal Framework ....................................................................................................... 36

2.5.2 Institutional Arrangements .............................................................................................. 38

2.6 Section Conclusion .................................................................................................................. 40

## SECTION THREE ......................................................................................................................... 42

3.1 Introduction ............................................................................................................................. 42

3.2 Model Specification ............................................................................................................... 43

3.2.1 The general model ........................................................................................................... 43

3.2.2 Model Specification ........................................................................................................ 45

3.2.3 Definition and justification of variables .......................................................................... 45

3.3 Cross sectional analysis ........................................................................................................... 47

3.2.1 Data collection .................................................................................................................. 47

3.2.2 Structure of questionnaire ............................................................................................... 48
3.2.3 Sources of Primary data ................................................................. 48
3.2.4 Pilot study (questionnaire pretesting) and response rate ................ 49
3.2.5 Data Analysis ................................................................................ 49

**SECTION FOUR** ................................................................................. 50
Estimation and Interpretation of results .................................................... 50
4.1 Unit Root Tests Results ................................................................... 50
4.2 Estimation and Results ................................................................... 51
4.3 Explanation of the results ............................................................... 53
4.4 Section Conclusion ....................................................................... 56

**SECTION FIVE** ................................................................................... 57
Estimation and Interpretation of results .................................................... 57
5.1 Data Analysis ................................................................................ 57
5.2 Consistency of the time series and cross-sectional results ................. 57
5.3 Descriptive Analysis of the questionnaire ........................................ 57
5.4 Understanding of Private Sector External Debt ................................ 58
5.4.1 Level of appreciation of private sector external debt ..................... 58
5.4.2 Factors affecting private sector borrowing decisions .................... 59
5.4.3 Importance of Private Sector External Debt .................................. 60
5.5 Levels of private sector external debt ............................................. 61
5.5.1 Levels of PSED for period 2004-2009 ......................................... 61
5.5.2 Other major sources of funding over the period ......................... 61
5.6 Utilisation of private sector external debt ....................................... 62
5.6.1 Determination of how borrowed funds affected operations of companies ................................................................. 62
5.6.2 Application of funds borrowed .................................................. 63
5.6.3 Level of external debt arrears ..................................................... 64
5.7 Borrowing arrangements .............................................................. 64
5.7.1 Current procedural requirements .............................................. 64
5.7.2 Future borrowing arrangements ............................................... 65
5.7.3 Anticipated type of future PSED borrowing ............................... 66
5.8 Section Summary ........................................................................ 77

**SECTION SIX** .................................................................................... 68
Summary and Conclusions .................................................................... 68
6.1 Summary ...................................................................................... 68
6.2 Broad limitations of the study ....................................................... 70
6.3 Policy Recommendations from the study ...................................... 71
6.3.1 Foreign Private Capital Flows Surveys ...................................... 71
6.3.2 Private Sector External Debt Surveys ....................................... 72
6.3.3 Building capacity and strengthening the framework on reporting of PSED ................................................................. 73
6.3.4 Development of mechanism (software) for recording data on PSED ................................................................. 74
6.4 Areas for Future Research ............................................................. 75

**REFERENCE/ BIBLIOGRAPHY** ............................................................. 76

**APPENDIX 1:** Questionnaire on the collection of information on PSED .... 79
**APPENDIX 2:** Econometric Results of the time series estimation .......... 82
LIST OF TABLES

Table 1: Growth of Private Non-Guaranteed External Debt in Developing Countries ...................... 6
Table 2: External Debt and Debt Payment Arrears ........................................................................... 9
Table 3: Trends in External Debt/GDP Ratio .................................................................................. 14
Table 4: Summary of Literature Review on External Debt and Economic Growth ..................... 32
Table 5: Results of the unit root tests in levels .............................................................................. 50
Table 6: Test for stationarity of variables after differencing .............................................................. 51
Table 7: Modelling DGDP using OLS: The long run static model .................................................... 52
Table 8: The Long run economic growth function ........................................................................... 52
Table 9: Questionnaire response rate ............................................................................................... 58

LIST OF FIGURES

Figure 1: Government of Zimbabwe revenue and expenditure levels (1980-2007) ......................... 10
Figure 2: Private Sector External Debt and Foreign Direct Investment Trends in Zimbabwe .......... 13
Figure 3: PSED Developments in Tanzania .................................................................................. 15
Figure 4: Stock of Private Sector External Debt in Zambia ............................................................. 16
Figure 5: External Debt Classification by Debtor category ................................................................. 21
Figure 6: Schematic expression of the link between PSED and economic growth ....................... 26
Figure 7: Model Specification ......................................................................................................... 45
Figure 8: Trends in PSED and FDI ................................................................................................. 54
Figure 9: Level of understanding of Private Sector External Debt .................................................. 59
Figure 10: Factors Affecting Companies’ borrowing decisions ....................................................... 60
Figure 11: Importance of Private Sector External Debt as a source of Funding ............................. 60
Figure 12: Other sources of funding ............................................................................................... 62
Figure 13: Importance of Private Sector External Debt as a source of Funding ............................. 63
Figure 14: Application short term and long term borrowings ........................................................... 64
Figure 15: Comments on the flexibility of the current PSED borrowing mechanisms ................... 65
Figure 16: Application of anticipated future borrowings from PSED ............................................. 66
SECTION ONE

Introduction

This Section gives an overview of how private sector external debt has evolved to be an important variable for economic growth in an environment characterised by great efforts towards globalisation and privatisation. Global and regional developments are also outlined in this Section, as well as the research problem, objectives and justification of this study.

1.1 Background

Economic growth remains a subject of significance in many countries in spite of its economic performance having been varied across geographic boundaries (Rodrik, 2003), ranging from negative to strongly positive rates of growth. Such has been the importance of its long run performance (Fedderke, 2003), evidenced through the improvement of standards of living, poverty, employment and deficit reduction, that it has become such a matter of importance to policy makers across the globe. Consequently, sizeable resources have been channelled towards the exposition of this variable, which has significantly improved various social indicators, which include literacy, infant mortality and life expectancy in many countries in the last decade (Rodrik, 2003).

Due to its prominence, literature is rich with theories growth which became eminent as early as the 1930’s through the works of Harrod (1939) and Domar (1946) who were the proponents of the Harrod-Domar growth model which helped explain growth as solely driven by domestic savings. Solow (1956) and Swan (1956) also developed the neo-classical growth model which was a critique of the Harrod-Domar, and helped explain economic growth as a result of exogenous technological progress and the rate of labour force growth. The inadequacy of these theories to account for other important facilitants of economic growth like entrepreneurship and strength of institutions gave birth to the endogenous growth
theories through the works of Romer (1986), Lucas (1990), Rebelo (1991) and Mankiw (1992), which viewed growth as largely a function of the accumulation of knowledge and adequate stock of human capital.

Although these theories are supportive of the importance of long run growth (Fedderke, 2003), they have however centred more on domestic factors such as increasing domestic savings, accumulation of knowledge, capital formation, population growth, labour quality and quantity. This focus on domestic factors has spurned the growth of the traditional neoclassical models, which allows for capital mobility, or the ability of a country to borrow and lend, which increases transitional growth (Pattillo et al, 2002). This capital mobility therefore buttresses the importance of external factors, which equally include foreign private capital flows (foreign direct investment, portfolio investment and external debt), which are now regarded as important facilitants of this long run growth.

These variables are therefore important sources of financing capital formation in many developing countries, which are faced with inadequate internal capital due to low productivity, income and savings, hence the need for external financial support to bridge this gap (Adepoju et al., 2007). These foreign private capital flows, which have significantly increased over the past two decades in emerging markets and developing countries, are therefore considered an important tool for plugging the domestic resource gap in such countries (Gwenhamo, 2009), where they become an important source of sustainable growth, a development that buttresses the need for the exposition of their contributory effect on growth, hence a study of this magnitude.
1.2 Foreign Private Capital Flows and growth

1.2.1 Contribution to growth

The waves of financial globalization and privatisation of entities during the mid 1980’s to 1990’s marked the surge in international capital flows among industrial and developing countries. These private capital flows mainly include foreign direct investment (FDI), portfolio investment (PI) and external debt (ED). According to the Balance of Payments Manual 5 (BPM5), M5, FDI refers to an investment made to acquire lasting interest in enterprises operating outside of the economy of the investor, while external debt is defined as the outstanding amount of those actual current, and not contingent, liabilities that require payment(s) of principal and/or interest by the debtor at some point(s) in the future and that are owed to non-residents by residents of an economy. External debt includes public and private debt, of which private sector external debt is the focus of this research.

This remarked increase in flows has been associated with huge growth rates in some of the recipient countries, mainly in developing countries with well developed financial markets, well functioning institutions and sound macro-economic policies (Sethi et al, 1996). While some countries have benefited from this surge in international capital flows, others have experienced negative growth rates and destructive financial crises over the same periods.

Private capital flows to Africa have increased substantially since the 1990s, with inevitable consequences for macro-economic policy (Bhinda et al 1990) and growth patterns of recipient countries. This increase in flows which is equally attributable to the improved monitoring and reporting of private capital flows (Martin et.al 2004), has immensely benefited a number of countries. As the IMF (2008) notes, much of the growth experienced
in many African countries was largely attributable to these increased private capital flows, which quadrupled from USD11 billion (2000) to USD53 billion (2007) in Sub-Saharan Africa. Such a contribution to economic growth has been through the augmentation of capital, and the infusion of technology, which leads to the high growth rates (Sethi et al, 1996).

It is this dramatic increase in private capital flows which creates an economic expansion through employment creation, technology and skills transfer to industry and personnel, and increased Government revenue via taxation, which in turn contributes to economic growth and poverty reduction. As Seth et al (1996) notes, some countries have experienced periodic collapse in growth rates due to huge or small capital flows. According to the Zambian Foreign Private Investment Survey Report (2010), the reduced growth rate of 1.6% experienced in Sub-Saharan in 2009, was a culmination of the effects of the global financial crises and the reduced global capital flows, of which FDI and external debt have been the dominant capital flows to this region with insufficiently structured capital markets (Amani, 2004). FDI at global level declined drastically in 2009 by 37% to USD1, 114.0 million, after recording a 16% fall in 2008 (IMF, 2010)

Clearly, the rapid growth of private capital flows has been a significant facilitant of growth in many countries. Baillie (2000) supports the existence of a relationship between these variables, in a study that provides evidence that private capital inflows foster economic growth although this preposition is only valid for countries with financially level banking sectors.
1.2.2 The growth of Private Sector External Debt

Although the contribution of FDI, which is the widely researched stable and non-debt creating flow capital flow (Mwilima, 2003) remains unquestionable, the abundant research on this variable as well as the incidence of public and publicly guaranteed external debt, has created a gap in literature on the contribution of private sector external debt which is defined the outstanding amount at any time, of those current and not contingent, liabilities that require payment(s) of interest and/or principal by the debtor at some point (s) in the future and that are owed to non-residents by private residents of an economy” (IMF, 2001). As Singh (1994) notes, this component of debt has little empirically established answers to its contribution to growth as it has long been viewed as relatively insignificant, due to the preposition that it is market determined and allocated efficiently (Baball, 2000).

This gap in literature on the contribution of private sector external debt is however not consistent with the high levels of private debt flows to emerging markets and developing countries that were experienced during the boom period of 2002-2007. As Rodrik et al (1999) notes, international lending boomed in the 1990s, a period characterised by the doubling of the outstanding stock of debt in emerging markets from USD1 trillion to USD2 trillion between 1988 and 1997. The IMF (2009) notes that while in 1990 the private sector accounted for a mere 16% of all external loans disbursed to developing countries, the share of private sector external debt increased significantly to 77% in 2006. In addition, the private sector’s non-publicly guaranteed debt liabilities accounted for 44% in 2006, an increase from the 1990 figure of 5% of developing countries’ total external debt.

Principally, much of this debt is contracted by the private sector (Hallack, 2009) making it a very critical flow that now requires global attention through structured investigation into its
impact on the development of the recipient countries as well as a factor of growth and financial stability. As Table 1 clearly shows, the total of private sector external debt to developing countries has been increasing since 1970, although the figure may be an understatement due to the unstructured reporting of these flows.

**Table 1:** Growth of Private Non-Guaranteed External Debt in Developing Countries

<table>
<thead>
<tr>
<th>Year</th>
<th>USD Millions</th>
</tr>
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<tr>
<td>1970</td>
<td>0</td>
</tr>
<tr>
<td>1980</td>
<td>100</td>
</tr>
<tr>
<td>1990</td>
<td>200</td>
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<td>1996</td>
<td>300</td>
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<td>1998</td>
<td>400</td>
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<td>1999</td>
<td>500</td>
</tr>
<tr>
<td>2000</td>
<td>600</td>
</tr>
</tbody>
</table>

*Source: UNCTAD, World Bank Databases*

This increase in the share of private sector external debt to total debt is attributable to a number of factors which include:-

- The privatisation of the manufacturing and banking sectors (Hallack 2009) experienced by the developing countries in the 1990’s a development that has resulted in a boom in the amount of foreign currency denominated debt contracted by the private sector. These vigorous global privatization programmes which promote private sector participation as engines for growth (Baball, 2002);
- International developments underpinned by the deregulation of capital movement to acquire gains of mobile capital (Sayaka 2005),
• The increasing presence of foreign banks fuelling cross-border lending as well as the increasing reliance on short-term external debt by resident corporations.²

These factors have all but buttressed and underscored the importance and consideration of the private sector debt as an important global policy consideration and form of capital to many countries through its effect on economic growth in the form of financial support to private investments. As Reinhart and Rogoff (2010) also shows, the exposition of this variable is now important as historical evidence has proved that during incidences of financial crisis, private sector debt (both local and external) eventually becomes public debt. This therefore explains why private sector external debt has become such a variable of importance.

1.3 Macroeconomic developments in the country

The Zimbabwean economy is emerging from multiple challenges which have led to contraction in economic performance over the past decade (1999-2009) characterized by a hyperinflationary environment, acute foreign exchange shortages, constrained foreign private capital flows, and a general misalignment of major macro-economic imbalances (IMF, 2009).

Economic growth shrunk by a cumulative estimate of 50.3 percent between 2000 and 2008. The economy experienced hyperinflationary conditions, significant levels of informalisation of activity, as well as speculative and parallel market activities. Inflation rate reached an all high level of 231 million in July 2008 and the negative growth in the economy resulted in declining export growth, against the backdrop of rising imports. The drying up of balance of payments and budget support further compounded the challenges facing the economy.

The continued decline in the economy resulted in the dollarization of the economy in February 2009. This dollarization was enveloped in the introduction of a multi-currency regime, which allowed for the use of the United States Dollar (USD), British Pound (GBP), South African Rand (ZAR) and the Euro as specified foreign currencies and in the process, the Zimbabwean dollar was suspended. This development restored both macroeconomic and price stability. As a result, the economy is now forecasted to grow by 8.1% in 2010, and maintain an average growth rate of 6.5% up to 2015. Average annual inflation is projected at an average of 5.0% in the outlook period.

1.3.1 Evolution of Zimbabwe’s External Debt

Reminiscent to developments in other developing countries, the Zimbabwean economy has relied on both external and domestic finance to fund its developmental projects. In an environment characterised by a constrained savings base, external resources have greatly helped bridge this gap. Much of these foreign resources have been in the form of foreign direct investment and external debt.

As at June 2009, the country’s external debt amounted to USD4.8 billion, of which 44% was owed to multilateral creditors while bilateral and commercial creditors were owed 50% and 6% respectively. Of the total debt, 82.9% was contracted by Government, 16% was secured by the parastatal sector and the remainder by the private sector, whose contribution is the subject of this paper. Part of this debt was inherited from the pre-independence era, where the government inherited a colonial debt amounting to about USD700 million, of which USD594 million was private sector debt, USD98 million bilateral and USD5 million multilateral debt (Bond and Manyanya, 2002).
Table 2: External Debt and Debt Payment Arrears

<table>
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<tr>
<th></th>
<th>DOD</th>
<th>TOTAL ARREARS</th>
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<tr>
<td>TOTAL DEBT</td>
<td>6 432.0</td>
<td>4 492</td>
<td>3 757.5</td>
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<td>Public &amp; Publicly guaranteed</td>
<td>6 089.0</td>
<td>4 452.1</td>
<td>3 724.5</td>
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<td>Government Long term</td>
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<td>256.6</td>
<td>0.0</td>
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</tbody>
</table>

Source: Reserve Bank of Zimbabwe and the Ministry of Finance

On attainment of independence in 1980, the Zimbabwean Government adopted a highly controlled and inward looking approach to the economy, which culminated in the acceleration of growth largely buoyed by foreign capital which constituted about 70% of total capital stock (Clarke, 1980). Debt sustainability became an issue of concern soon after independence in 1980 when the new government embarked on a borrowing spree to address colonial vestiges.

With domestic savings only capable of funding three quarters of domestic investment, foreign capital constituted the balance and although FDI was the dominant flow, debt was an important factor. The first post independence decade saw the external debt climbing to USD3, 24 billion of which the Government accounted for 76%, public enterprises 18% and the private sector 6%. The country’s huge foreign debt was accumulated in just three years after independence with the debt service ratio rising from 3.8% in 1980 to 37.3% in 1983. It then remained high until 1993 before it declined to 25.3% in 1994. With inflows of FDI negligible and low due to the unfavorable restrictive policy environment in the first decade of...
independence (Gwenhamo, 2009), net capital inflows were exclusively borrowings (Jenkins, 1998).

The country’s fiscal position was further exacerbated by the severe drought which hit the country between 1983 and 1985. The Government had to commit its limited resources towards drought mitigation programmes thus adding more pressure on the fiscal balance. The country’s GDP declined by 2.2% leading to the shrinkage of the country’s revenue base. Inflation rose reaching a peak of 18% in 1983. Interest rates on Government stocks, however, averaged 13% during the period, while Treasury Bills were as low as 8%. Resultantly, the country’s fiscal deficit further deteriorated to about 33.3% of GDP. This led to an increase in the public domestic debt from 45% of GDP to 58% of GDP which was mainly financed from the domestic market.

**Figure 1**: Government of Zimbabwe revenue and expenditure levels (1980-2007)

![Graph showing government revenue and expenditure levels](attachment://graph.png)

*Source: Reserve Bank of Zimbabwe Quarterly Bulletins (Various editions)*

In 1990, the Government of Zimbabwe adopted the Economic Reform Programme with the support of the IMF and World Bank referred to as the Economic Structural Adjustment
Programme (ESAP). Some of the resources to finance the programme came from the Economic Structural Adjustment Fund (ESAF) of the IMF. This new programme was a total departure from centrally controlled and socially motivated policies of the 1980s as it emphasised the role of market forces through trade liberalisation, deregulation of prices, public sector restructuring, economic policy reform.

The adoption of ESAP culminated in the establishment of the Zimbabwe Investment Centre (ZIC) as a way of redressing the persistently low levels of fixed capital formation. This new policy and institutional arrangements helped promote FDI inflows which averaged USD50 million per year between 1990 and 1997 and reached a record high of USD444 million in 1998. ESAP however wrought significant quantitative and qualitative changes in the country’s debt situation with the new era of economic liberalisation spurning a scramble and appetite for new loans as companies and the Government sought to bridge the local savings gaps. As a consequent, ESAP absorbed approximately USD3, 5 billion in new loans over three years (Bond and Manyanya, 2002).

The policy thrust of ESAP resulted in the privatisation of a number of state owned enterprises as part of the Government’s effort to reduce its expenditure levels and ensure efficiency. Due to the liberalized environment and removal of foreign exchange restrictions, companies were able to freely borrow offshore resulting in a surge in the level of private sector external debt up to 1997.

In light of the enormous repercussions of the debt burden, the country introduced the External Loan Coordinating Committee (ELCC) as an external debt management exercise designed to ensure debt sustainability. The ELCC is a statutory committee comprising of the Ministry of Finance and the Reserve Bank of Zimbabwe officials. The Committee is
responsible for the processing of foreign loans by the private sector beyond USD5 million. All private sector loans below USD5 million are processed by Commercial Banks, who are then required to register such loans on approval with the ELCC.

However, the macroeconomic downturn that later characterized the economy in 1998 culminated in a decline in investment as well as the cancelation of BOP support and external finance from multilateral finance institutions. In the process, private sector external debt started declining as the country’s credit rating fell and companies failed to access this critical source of finance. In 1999, the Government failed to honour its external payment obligations and was suspended from further accessing any financial support from the IMF, World Bank and other international lending institutions. This period was also punctuated by the decline in the overall macro-economic framework evidenced by the general misalignment of many economic indicators. Both FDI and private sector external debt flows dried as foreign capital evaded Zimbabwe now considered a risky investment destination.

Since then, the country has not been able to pay its external obligations for nearly a decade (2000-2010) against the backdrop of progressive decline in export performance and the depletion of the foreign currency reserves, due to restrictive measures imposed on the country. The meagre foreign currency resources available to the country have been allocated towards critical social needs such as education and health delivery systems. Consequently, the country’s ability to settle obligations has been severely undermined. It is against this backdrop that the country has defaulted on its obligations resulting in accumulation of US$4 487 million in arrears as at 31 December 2009\(^3\). Figure 2 shows the trend in private sector external debt and FDI over the period.

\(^3\) RBZ Monetary Policy Statement (2010)
1.4 Debt developments in the MEFMI Region

1.4.1 Contribution of external debt to GDP

In response to these global trends and new emerging issues, MEFMI\(^4\) has been building capacity towards the accurate recording of data on foreign private capital flows to enhance country by country and regional analysis thereof. Countries such as Uganda, Zambia and Malawi, have instituted FPC Surveys designed to extract information on the magnitude and impact of private capital flows with a view of establishing the significance of these flows to the macro-economic landscape of their economies. This is in recognition of the MEFMI’s appreciation of the fact that capital flows have since become an important source of capital finance for most economies as they move towards embracing economic reforms, among them opening of the capital account and liberalisation of domestic financial markets.

\(^4\) Regional block comprised of 13 member countries namely, Angola, Botswana, Kenya, Lesotho, Malawi, Mozambique, Namibia, Rwanda, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe.
In the region, external debt constitutes a large proportion of public debt in the region due to availability of concessional multilateral and bilateral funding. In most countries in the region, domestic debt funds the budget deficit on a residual and gap filling basis, after all forms of external grants and concessional borrowing sources have been exhausted. Excessive reliance on external debt has exposed MEFMI regional economies to exchange rate risk arising from principal revaluation due to exchange rate changes. Table 3 shows the trends in the external debt to GDP ratio sampled MEFMI member countries.

### Table 3: Trends in External Debt/GDP Ratio

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<tbody>
<tr>
<td>Zambia</td>
<td>195.3</td>
<td>154.5</td>
<td>114.4</td>
<td>56.8</td>
<td>4.9</td>
<td>8.4</td>
<td>7.3</td>
<td>9.4</td>
</tr>
<tr>
<td>Lesotho</td>
<td>72.5</td>
<td>63.6</td>
<td>50.7</td>
<td>41.5</td>
<td>37.5</td>
<td>34.2</td>
<td>35.5</td>
<td>36.2</td>
</tr>
<tr>
<td>Swaziland</td>
<td>15.5</td>
<td>17.2</td>
<td>16.1</td>
<td>12.3</td>
<td>11.7</td>
<td>12.5</td>
<td>11.8</td>
<td>12.7</td>
</tr>
<tr>
<td>Malawi</td>
<td>132.3</td>
<td>121</td>
<td>112.6</td>
<td>108.3</td>
<td>14.4</td>
<td>14.4</td>
<td>16.3</td>
<td>17.7</td>
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<tr>
<td>Kenya</td>
<td>36.7</td>
<td>36.4</td>
<td>35.5</td>
<td>26.9</td>
<td>24.4</td>
<td>21.5</td>
<td>21.2</td>
<td>23.4</td>
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<tr>
<td>Rwanda</td>
<td>76.0</td>
<td>88.5</td>
<td>84.9</td>
<td>63</td>
<td>17.1</td>
<td>16.8</td>
<td>15.2</td>
<td>16.7</td>
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<tr>
<td>Tanzania</td>
<td>69.9</td>
<td>44.6</td>
<td>43.1</td>
<td>41.0</td>
<td>41.4</td>
<td>12.7</td>
<td>14.3</td>
<td>17.9</td>
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<tr>
<td>Uganda</td>
<td>57.5</td>
<td>63.7</td>
<td>56.3</td>
<td>47.9</td>
<td>44.8</td>
<td>12.3</td>
<td>12.1</td>
<td>14.7</td>
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<tr>
<td>Angola</td>
<td>65.8</td>
<td>44.3</td>
<td>33.3</td>
<td>23.8</td>
<td>12.1</td>
<td>9.9</td>
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**Source:** IMF Economic World Outlook, October 2010

### 1.4.2 Efforts to capture private capital flows in the region

In order to enhance the attainment of accurate statistics in the region, MEFMI developed a system for capturing private capital flows statistics. This system which is called the Private Capital Monitoring System (MEFMI-PCMS) was developed in 2007 as an IT solution designed to facilitate the efficient collection and processing of private capital flows data in line with Balance of Payments standards. The system effectively captures all the components on private capital flows, which include foreign direct investment, portfolio investment and
external debt, and has already been vigorously tested by MEFMI countries such which are Uganda, Malawi, Zambia and Tanzania.

1.4.3 A sample example of Tanzania and Zambia

Tanzania

In Tanzania, PSED stock increased from USD 92.6 million in 1990 to USD1, 555.2 million in 2009 following liberalization of the current account and reforms on foreign exchange controls. The increase represents growth rate of 1,679.5 per cent during the period and this steady increase in the stock of PSED was largely attributable to the increase in number and compliance of commercial banks and private entities that are exposed to international financial services. In addition, privatization of public corporations also contributed to the fast increase in PSED relative to the borrowing by the public sector.

Figure 3: PSED Developments in Tanzania

Two pieces of legislations are involved in the monitoring of private sector external debt in Tanzania. These are the Foreign Exchange Act, 1992 (Foreign Exchange Act) and the Bank of Tanzania Act 2006 (BOT Act). There are also regulations issued under the Foreign Exchange Act, and circulars issued by the Bank to complement the provisions of the Foreign Exchange Act and Regulations in providing regulatory guidance to banks and financial institutions in implementing the spirit of the legislative framework for foreign exchange transactions.

Zambia

According to the Zambia Report on Foreign Private Investment and Investor perceptions report (2010), Zambia’s stock of private sector external debt at the end of 2009 stood at USD5,018 million, which represented a 9.3 per cent increase compared to the stock position of USD4,590.2 million as at end 2008. As at end 2007, the private sector external debt stock was USD3,041.5 million, which was 42.4% higher than the end 2006 stock position of USD2,136 million, showing a significant increase in this source of finance. The mining sector accounted for 46.5 per cent and 47.9 per cent of the stock of private sector external debt stock in 2008 and 2009 respectively.

Figure 4: Stock of Private Sector External Debt in Zambia

It is evidently clear that the share of private sector in total debt has been increasing over time. While FDI has been the dominant factor, developments highlighted above confirm the increasing significance and budding of private sector external debt as a capital flow for plugging the domestic resource gap.

1.5 Problem Statement

As noted, private sector participation is increasingly becoming a critical source and engine for sustained economic growth (Baball, 2002) in this era of accelerated globalisation. As countries globally seek to compliment government efforts in a liberalised economy, effort is being tailored to foster increased private sector participation, whose life blood is embedded in its ability to have access to unlimited sources of finance of which private sector external debt, in its various forms, is equally gaining prominence.

The Zimbabwean economy is on a rebound and a rebuilding exercise following a decade of continued macroeconomic decay characterized by high inflation, shortage of foreign exchange, declining output, international isolation and failure to access global finance for development. As part of the desired growth path, the Government of Zimbabwe has identified the private sector as a critical contributing factor for the achievement of the desired economic growth (Short Term Emergency Recovery Plan, 2008 and Medium Term Program, 2009). The success of the private sector contribution to economic growth target remains underpinned by the level of access to external finance to compliment local savings which are currently below 5% of GDP (RBZ, Economic Bulletin, 2010). In addition, part of this rebuilding exercise entails liberalisation of economic activity and privatization of state.

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5 The initial liberalisation process was done in 1993, with the implementation of ESAP. In February 2009, the country also instituted a wholesome and partial liberalisation of exchange controls and economic activity.
owned enterprises (SOE’s) and in the absence of sustainable levels of local funding options, the anticipated growth in the private sector calls for such introspection of the relevance of private sector external debt, which carries hopes for a Zimbabwe starved of local savings.

With the local market constrained for finance due to the liquidity challenges facing the economy (RBZ, 2010), external finance remains a critical source of development funding. The need to improve such access has culminated in the liberalisation of trade and exchange control, to allow ease of foreign borrowing by local firms (RBZ Monetary Policy, 2010). The increasing private sector external debt levels in Zimbabwe, and other MEFMI member countries such as Uganda, Zambia and Tanzania, therefore raises the need to investigate whether the increased inflow of PSED being is being translated into growth, a research area that remains largely unexplored in the region.

Interestingly, an economy like Zimbabwe provides a good case study for an exposition of this magnitude. Traditionally, such low income countries do not have access to international capital markets and thus the impact of the share of private sector in the total external debt on growth on these economies can be different as compared to emerging market countries hence the need to understand this dynamics.

1.6 Objectives and hypothesis of the Study

Although there is a substantial literature on the impact of external debt on growth, relatively few studies have focused on the incidence of private sector external debt, and more importantly in the low-income countries. The underlying rationale of this paper is therefore embedded in the need to:-
i) Establish the impact of private sector external debt component on Zimbabwe’s economic growth patterns over the period 1980-2009;

ii) Add to existing literature on private sector external debt in Zimbabwe.

This is designed to redeem and support efforts supportive of the importance of this less analysed but relevant debt creating capital flow in Zimbabwe, as well as the MEFMI region. The pursuit of this overall research objective will therefore be underpinned by the exposition and unbundling of selected research questions, which are central to the relevance of this research paper. These questions are:-

iii) Identify factors that have affected the level of private sector external debt over time;

iv) Gauge how private sector external debt has compared to FDI as external sources of financing growth in Zimbabwe;

v) Add to the existing body of literature on private sector external debt in Zimbabwe.

Although there is limited documented research on private capitals flows in Zimbabwe\(^6\), the hypothesis of this research area is the existence of a positive relationship between private sector external debt and growth in Zimbabwe over the period under study.

1.7 Organization of the Study

This research is divided into six sections. The second section focuses on literature review, which includes theoretical and empirical literature review. Section 3 outlines the methodology followed in dealing with the subject matter while Section 4 covers data analysis and presentation of findings of time series analysis. The results of the cross-sectional analysis are outlined in Section 5. Section 6 outlines the conclusion and outline of recommendations, as well as the suggested areas for future research.

\(^6\) Zimbabwe has not done any national surveys on foreign private capital (FPC). Other countries in the MEFMI region, Uganda, Lesotho, Zambia, Malawi, have and are already implementing such surveys.
SECTION TWO

Theoretical and Empirical Literature Review

This Section outlines the theoretical and empirical perspectives underlying the concept of private sector external debt, which is one of the foreign private capital flows critical for growth in many economies. Due to this importance, the Section therefore reviews the various strands of literature on the contribution of this variable to variable for growth.

2.1 What is Private Sector External Debt (PSED)

The International Monetary Fund Guide for Compilers and Users (2001) defines Private Sector External Debt as “the outstanding amount at any time, of those current and not contingent, liabilities that require payment(s) of interest and/or principal by the debtor at some point (s) in the future and that are owed to non-residents by private residents of an economy” (IMF, 2001). This is also consistent with Baball (2000) who defines Private Sector External Debt (PSED) as borrowing from offshore by private companies of persons and such borrowings can be short term, medium or long term, guaranteed or non-guaranteed. Short-term PSED covers mainly trade credits received over short periods of not more than 1 year. Medium and long term PSED is debt that has an original maturity of more than 12 months. Trade credits can be in the form of pre-payments against deliveries, imports obtained either on consignment basis or under supplier’s credit, pre and post shipment export finance.

PSED is mainly contracted by private sector companies, privately owned banking institutions and individuals and according to Baball (2002), the key facets underlying this definition are:

- It includes only external borrowings by the private sector companies and individuals;
- The determination of external debt lies in the concept of residency and not currency;
There is need to understand the outstanding and current debt and the exclusion of contingent liabilities.

2.2 Categories of Private Sector External Debt

**Figure 5**: External Debt Classification by Debtor category

Source: PSED: Main Issues and Challenges for Monitoring (Debt Relief International Ltd)
2.3 Link between Private Sector External Debt and Growth

In order to establish the link between private sector external debt and growth, it is important to establish the channels through which foreign private capital flows affect growth. A number of studies have done, which seemingly suggest that private capital flows affect growth through various channels which include private investment. From a theoretical perspective, Seetanah et al (2007), argues that external debt affects economic growth the through the debt overhang, liquidity constraint, fiscal effect, productivity suppression and reduction in human capital accumulation channels. This gives rise to various theories on this external debt-growth relationship and as Omet and Kalaji (2007) notes, the effect of debt on growth can be summarised by three strands of thought which considers:-

i. External finance as a capital inflow that positively impact on the level of domestic savings and investment, and hence affects a country’s growth. In this instance, external finance compliments domestic savings and investment and increases growth (Eaton, 1993);

ii. External finance as a substitute to domestic savings and investment and therefore tends to crowd out them out (debt overhang theories, Krugman, 1988);

iii. Capital accumulation as the sole force driving growth (endogenous growth theories, by the likes of Cohen, 1991, 1992, etc).

Consistent with the work of Bailliu (2000)7, this exposition is done through the AK model of economic growth, which is an endogenous growth model (Wikipedia).

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7 According to Balliu (2000), Pagano (1993) uses a similar AK Model, to incorporate the effects of international private capital flows on a closed economy.
2.3.1 Closed economy without private capital flows

This AK Model seeks to answer how changes in financial variables, inclusive of private capital flows, affect an economy’s long run growth pattern. The AK Model applied in this analysis takes the following form:

\[ Y_t = A K_t \]  \hspace{1cm} (1)

where \( Y \) represents the total production in an economy, \( A \) represents total factor productivity, \( K \) is capital. In this model, output is a linear production function and it is assumed that there is no population growth in the model. Capital stock is also deemed to depreciate at the rate of \( \Phi \) per period while the economy produces a single good which can either be consumed or invested. Based in these generalised assumptions, the economy’s gross investment is therefore given by:

\[ I_t = K_{t+1} - (1 - \phi) K_t \]  \hspace{1cm} (2)

The above model assumes that banks and other institutions are responsible for transforming savings into investment. Assuming that a fraction of each dollar saved (\( \delta \)) is made available for investment, then capital market equilibrium is attained where net savings equals gross investment and this gives the following condition:

\[ \delta S_t = I_t \]  \hspace{1cm} (3)

Using equations (1) and (3), the steady-state growth rate of a closed-economy AK model with financial intermediation will be of the following reduced form:

\[ g = A \left( \frac{I}{Y} \right) - \delta = A \phi S - \delta \]  \hspace{1cm} (4)
According to Balliu (2000), financial development in this equation affects economic growth through two channels which a result of the increased financial intermediation ability to:-

- Efficiently allocate savings to investment and
- Effective allocation of capital to high yielding investments;

**2.3.2 Open economy with international capital flows**

This framework is further developed by opening up the economy to allow for the incidence of capital flows through investments by foreign residents, who are assumed to invest through the financial intermediaries. The inclusion of the net foreign private capital flows into the model is meant to enhance the flow of foreign capital to augment the level of existing savings. An increase in net foreign private capital flows (either FDI, external debt – public and private- portfolio flows) into the economy therefore increases the pool of savings available for investment.

Taking into account the presence of international foreign private capital flows (NFPCF), the new capital market equilibrium (equation 3 above) is therefore re-established as follows:-

\[
\delta * (S_t + NFPCF) = I_t, *
\]

(5)

The revised steady state growth for this open economy with the incidence of foreign private capital flows is

\[
\ddot{g} = A^{\ddot{I}} / \ddot{y} - \delta = A^{\ddot{I}} \theta (S + NFPCF) / \ddot{y} - \delta = A \phi \ddot{S} - \delta
\]

(6)

Equation (6) shows the effect of incorporating net foreign private capital flows into a simple endogenous growth model. In this model, these flows, which were considered to be the driver
behind the surge in growth experienced in sub-Saharan Africa in 2008 (IMF, 2008), indeed affect growth by:-

- Increasing the domestic investment rate. The incidence of capital flows increases the savings rate and where such savings are used effectively through investment, they tend to increase the investment rate.
- leading to investments associated with positive spillovers, and/or
- Increasing domestic financial intermediation (which likely involves the intermediation of foreign funds by the domestic financial system).

2.3.3 Other linkages between private sector external debt and growth

A number of models suggest and imply that debt may have nonlinear effects on growth. In these models, the channel for these nonlinear growth effects of debt is through investment. In the endogenous growth models (Cohen, 2001, 2002), capital accumulation is considered to be the force driving growth. While a country’s access to international financial markets is limited due to a number of factors, growth is considered to be relatively high in the early stages of borrowing and investment of such funds. The model, however, assumes that at a later stage, growth falls to lower levels as the impact of excessive borrowing negatively sets into the model. Schclarek et al (2005) discovered that debt affects growth through capital accumulation. Other empirically proved channel by which debt affects growth, is the indirect effect exerted by private and public investments through the debt overhang and crowding out effects.

Overall, the share of private sector in external debt affects economic growth through the provision of finance to the private sector, and the relationship tends to be relatively strong in
instances where resources are effectively used. Where private sector external debt is transferred towards debt repayments, this may strongly stifle growth.

Another relevant channel linking debt to growth is the model developed by Calvo (1998), which links the debt and growth relationship to capital flight. According to this model, high debt levels are usually associated with low growth. The transmission mechanism is evidenced through the incidence of a higher distortionary tax burden on capital that is required to service the debt. This leads to a lower rate of return on capital, lower investment and ultimately growth. On the contrary, low debt regimes are deemed to have high growth for the opposite reasons. In intermediate ranges of debt, however, the effect on growth is indeterminate.

**Figure 6**: Schematic expression of the link between PSED and economic growth

![Schematic expression of the link between PSED and economic growth](image)

**Source**: Author’s deduction from surveyed literature
2.4 Empirical studies on the impact of external debt on growth

Empirical studies on the external debt-economic growth relationship are numerous in the literature in both developed and developing countries. Although there is a substantial literature on the impact of external debt on growth, available literature has largely focused more on the effect of public and publicly guaranteed external debt (Karagol, 2009), deemed to have significantly ignited the debt crises that erupted in the 1980’s (Baball, 2002). The effects of this crisis forced many Governments to accord significant prominence on this type of debt through initiatives aimed at curbing its burden and in so doing the relevance, contribution and impact of private sector external debt on various macroeconomic variables was totally outmaneuvered.

Available literature suggests the existence of two theories on the impact of external debt on growth. According to Pattillo et al (2002), one school of thought on external debt suggest that reasonable levels of debt inflows have a positive effect on growth, while the other suggests that large, accumulated debt stocks may be a hindrance to growth. Although such different schools of thought exist, there is consensus ad idem amongst these theories, vis-à-vis the existence of a positive association between reasonable levels of current debt inflows and economic growth (Pattillo et al, 2002). Unsustainable debt levels are viewed as an impediment to economic growth, hence a negative relationship between these variables as explained in certain pieces of literature (Seetanah et al., 2007).

Karagol (2009) however notes that there exists difficulty with the generalisation of the potential relationship (positive or negative) between external debt and economic growth. In the process, he proposes such an exposition be done on a case by case (country-specific) basis to establish the direction of this relationship. Another general consensus within
literature is that the question of whether debt is good or bad for economic growth largely depends on how debt flows are appropriated. Evidence from many East Asian countries demonstrates that a lot of countries that lack capital, especially those in the developing bracket, place huge reliance on external debt, which has played a key role in economic development over the past thirty years.

While debt has been explored, the incidence of private sector external debt on growth remains largely unexplored and there is little established empirical view of its effect on the growth pattern of countries. Alfred et.al (2009) however considered private sector external debt to be insignificant variable in a study that sought to expound the relationship between debt and growth for a number of developing and industrial economies. In this study, he found out that for developing countries, lower total external debt levels are associated with higher growth rates with this negative relationship being driven by public external debt and not private sector external debt.

On the importance of external finance, Singh (2000) analysed how large corporations in developing countries finance their growth. He notes that in spite of the variation in corporate financing patterns amongst LDCs, corporations in this region relied heavily on external finance for growth, hence a positive relationship between external debt and growth. The basis of this conclusion was embedded in the realisation that less developed markets have thin financial markets, which limits the scope of internal financing options. Companies in these regions therefore tended to seek recourse from external markets, which then become critical sources of financing their operations. This point is buttressed by the work of Asante (2000), whose private investment model for Ghana, which incorporated Keynesian, neo-classical, and uncertainty variables, depicted a positive contribution of the growth rate of real credit to the private sector and hence economic growth.
In an effort to establish the contribution and role played by private capital flows in determining the level of economic growth, Bailliu (2002) conducted a study for a selected panel of 40 developing countries using a data range from 1975–95. The study looked at the broad contribution of capital flows to growth, as well as the contribution of the financial sector in linking capital flows and growth. By employing a dynamic panel data methodology, which was manipulated to adjust for country-specific effects, while accounting for the potential endogeneity of the explanatory variables, the study found out that capital inflows foster higher economic growth, above and beyond any effects on the investment rate. This was however only applicable in economies where the banking sector has reached a certain level of development, thereby suggesting a pivotal role played by the domestic financial sector in ensuring that international capital flows do indeed promote economic growth in developing countries.

Osei (2000) however noted that Ghana's external indebtedness (through its size, type, sources, structure, and terms) for sustained economic growth for the period 1983–90, was one of the factors constraining the rapid growth of the Ghanaian economy. This is further asserted by Jenkins (1998) who constructed a model for private investment in Zimbabwe. Using a two-step Engle-Granger approach to analyse non-stationary variables, which included debt, controls and availability of finance, Jenkins found out that the external debt to GDP ratio posed a long negative relationship and deterring effect on private investments in Zimbabwe.

Iyoha (2000) did an analysis of the poor performance of sub-Saharan Africa since the onset of the external debt crisis in 1982 by analysing the scope, nature, and severity of sub-Saharan Africa's external debt and its impact on economic growth for the period 1970–97. He found that large stock of external debt and heavy debt-service payments have had depressing effects
on investment, and debt reduction measures bring about corresponding reductions in the total debt stock, the debt-GNP ratio, and the debt-service ratio and have positive impacts on investment and growth of real GDP.

Kumari (2004) however found the existence a debt-growth relationship for some countries, with no significant relationship for others in an attempt to establish whether external debt really plays a significant role in the attainment of higher and sustainable rates of economic growth by relieving the foreign exchange constraint in the developing countries.

Another attempt to investigate the external debt-growth relationship was done by Ayadi et al (2007) for the Nigerian and South African economies. The study focused on the analysis of the effects of the external debts of the two countries in a new context through the use of innovative models and econometric techniques. The Neoclassical growth model, which incorporates external sector, debt indicators, and some macroeconomic variables, was employed to explore the linear and non-linear effect of debt on growth and investment. The results, confirmed a negative impact of debt (and its servicing requirements) on growth for both Nigeria and South Africa. A variation existed in the overall application of debt between the two countries, with South Africa performing better than Nigeria in the application of external loans to promote growth. In addition, for Nigeria, external debt positively contributed to growth up to a defined point, after which its ramification became negative.

Motivated by the desire to establish this relationship in the case of a small developing country, Seetanah et.al (2007) analysed the debt-growth relationship for Mauritius for the period 1960-2004, using a Vector Error Correction Model (VECM) to explain the short and long run relationships. They found out that for Mauritius, external debt had a negative influence on the level of the country’s output both in the short run and long run.
In order to evaluate the non-linear relationship between external debt and debt, Pattillo et al (2002), used panel data set of 93 developing countries over 1969-98 to assess the relationship using different econometric methodologies, regression specifications, and different debt indicators. They found out that:–

- For a country with average indebtedness, doubling the debt ratio would reduce per capita growth by half to a full percentage point. The differential in per capita growth between countries with external indebtedness (in net present value) below 100 percent of exports and above 300 percent of exports seems to be in excess of 2 percent per annum.

- For countries that are to benefit from debt reduction under the current HIPC initiative, per capita growth might increase by 1 percentage point, unless constrained by other macroeconomic and structural economic distortions.

- The average impact of debt becomes negative at about 160-170 percent of exports or 35-40 percent of GDP. The marginal impact of debt starts being negative at about half of these values.

- High debt appears to reduce growth mainly by lowering the efficiency of investment rather than its volume.

Another study on the relationship between external debt and growth was done by Schclare et al (2005). The study which focused on a number of Latin American and Caribbean economies used a dynamic GMM panel estimator for a panel of 20 Latin American and Caribbean countries with data averaged over each of the seven 5-year periods between 1970 and 2002. The findings were that for this group of countries, lower levels of total external debt were associated with higher growth rates. They noted that this negative relationship was largely driven by the incidence of public external debt levels, and not by private external debt.
levels. This study therefore ruled out the incidence of the component of private external debt levels on growth.

Table 4: Summary of Literature Review on External Debt and Economic Growth

<table>
<thead>
<tr>
<th>Date</th>
<th>Author and Model</th>
<th>The period and Base</th>
<th>Results</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>Seetanah et.al Vector</td>
<td>1960-2004, Mauritius</td>
<td>Noted that external Debt negatively affects growth both in the short run and long run.</td>
</tr>
<tr>
<td></td>
<td>Error Correction Model</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2007</td>
<td>Ayadi et al Innovative</td>
<td>Nigerian and South African</td>
<td>Confirmed a negative impact of debt (and its servicing requirements) on growth for both Nigeria and South Africa</td>
</tr>
<tr>
<td></td>
<td>models and econometric</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>techniques</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td>Schclare et al Dynamic</td>
<td>1970 and 2002 20 Latin</td>
<td>• lower levels of total external debt are associated with higher growth rates</td>
</tr>
<tr>
<td></td>
<td>GMM Panel Estimator</td>
<td>American and Caribbean</td>
<td>• No incidence of the component of private sector external debt levels on growth.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>countries</td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td>Pattillo et al panel data</td>
<td>1969-98 93 developing</td>
<td>• For a country with average indebtedness, doubling the debt ratio would reduce per capita growth by half to a full percentage point.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>countries</td>
<td>• The average impact of debt becomes negative at about 160-170 percent of exports or 35-40 percent of GDP.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>• High debt appears to reduce growth mainly by lowering the efficiency of investment rather than its volume.</td>
</tr>
<tr>
<td>2000</td>
<td>Osei</td>
<td>1983–90 Ghana</td>
<td>Found out that growth was constrained by external indebtedness.</td>
</tr>
<tr>
<td>2000</td>
<td>Iyoha Econometric</td>
<td>1970–97 Sub-saharan</td>
<td>Found out that large stock of external debt and heavy debt-service payments</td>
</tr>
<tr>
<td>Date</td>
<td>Author and Model</td>
<td>The period and Base</td>
<td>Results</td>
</tr>
<tr>
<td>------</td>
<td>-----------------</td>
<td>---------------------</td>
<td>---------</td>
</tr>
<tr>
<td></td>
<td>analysis</td>
<td>African countries</td>
<td>have depressing effects on investment.</td>
</tr>
<tr>
<td>2000</td>
<td>Singh</td>
<td>Latin America</td>
<td>Discovered that corporations in this region relied heavily on external finance for growth, hence a positive relationship between external debt and growth</td>
</tr>
<tr>
<td>2000</td>
<td>Asante</td>
<td>1970-1996 Ghana</td>
<td>Depicted a positive contribution of the growth rate of real credit to the private sector and hence economic growth</td>
</tr>
<tr>
<td>2000</td>
<td>Bailliu</td>
<td>1975–95 40 developing countries</td>
<td>The study found out that capital inflows foster higher economic growth, above and beyond any effects on the investment rate</td>
</tr>
</tbody>
</table>

*Source: Authors deduction from surveyed literature*

After such an exposition of the varied impact of external debt on economic growth as depicted by the various strands of empirical work done, it is clear that the area of private sector external debt remains largely unexplored. Its impact can therefore only be ascertained by a study of this magnitude. An assessment of the institutional and regulatory framework in Zimbabwe is therefore necessary to build on this analysis.
2.5 Private Sector External Debt Legal and Institutional Arrangements

Like many other countries that are cognizant of the increased global private sector external debt levels, Zimbabwe has a regulatory framework designed to assist in the accurate recording of data on private sector external debt to enhance its monitoring and analysis. This all forms, partly, the basis of the country’s overall debt management objective in Zimbabwe which is designed to ensure that debt is raised, managed and retired at the lowest possible cost, consistent with the country’s economic and financial situation.

Currently, all private sector loans must be registered through the External Loans Coordinating Committee, which was established in 1987 with the mandate of assessing all foreign loans as part of the Government’s objective to ensure debt sustainability. Public borrowings are guided by the State Loans and Guarantee Act, Audit and Exchequer Act, Reserve Bank Act and Exchange Control Act. The State Loans and Guarantees Act empowers the Minister of Finance to borrow on behalf of the state, while at the same time setting maximum limits to borrowings by the State. The Minister of Finance is also empowered to manage all public finances by the Audit and Exchequer Act. The Exchange Control Act empowers the Reserve Bank of Zimbabwe to monitor all external capital flows into and/or out of the country.

In the wake of the trade and exchange control liberalisation on the current account, all loans below USD5 million are processed by Banks under advice to the ELCC. Loans above USD5 million are registered by the ELCC, which keeps a data base showing all the loans approved, nature, character, type and purpose as well as the pricing and maturity features.
These structures have made it possible for the country to track foreign loans into the country in a manner that allows the effective quantification of magnitude of private sector external debt, a position buttressed by the World Bank (2004), which asserts that “Although reporting countries fully recognise the importance of collecting data on private sector non-guaranteed debt when it constitutes a significant portion of total debt, detailed data is available only in countries that have registration requirements covering private sector debt, most commonly in connection with exchange controls”.

**Text Box 1: A look at the External Loans Coordinating Committee (ELCC)**

**What is the ELCC?**

**The External Loans Coordination Committee**

The Committee is an arm of the Reserve Bank of Zimbabwe and was formed in the 1980s to implement an effective debt management policy by sanctioning and monitoring all new loan commitments undertaken by all sectors of the economy. The ELCC aims to achieve a tolerable debt structure, characterized by adequate spread of maturities, diversification of borrowing sources and maintenance of a margin of borrowing capacity. The committee does this by setting “ELCC criteria” - basically terms of reference or benchmarks to which all loans must comply. The basis of this debt management is to maintain a sustainable level of external debt servicing and control the types of and amounts of foreign borrowing. An external debt manager also has to ensure that the debt sustainability ratios are consistent with the country’s economic and financial situation.

**Where does the ELCC derive its powers from?**

The ELCC derives its powers from the Reserve Bank Act, Exchange Control Act and the State Loans and Guarantees Act.

**Why should the decisions of the ELCC be consistent with the macroeconomic framework?**

External debt policy not only affects the Balance of Payments (Bop) position and national budgetary framework but also overall macroeconomic planning, hence the need for this consistency.

**What is the current ELCC policy on approval of external loans?**
Authorised dealers or banks can process external loans of up to US$5 million without prior ELCC approval. However all applications for external loans in excess of the stipulated threshold must be submitted to Reserve Bank of Zimbabwe for ELCC approval.

2.5.1 The Legal Framework

Zimbabwe has a number of pieces of legislation for effective recording, collection and analysis of data on private sector external debt. These include the State Loans and Guarantee Act, Audit and Exchequer Act, Exchange Control Act (Chapter 22:05), and the Exchange Control Regulations, Statutory Instrument 110 of 1996, and various Orders, Notices and Circulars.

- The Exchange Control Act

The Exchange Control Act (Chapter 22:05) and the Exchange Control Regulations issued under the Act, are key elements in regulating foreign exchange transactions in Zimbabwe. Under the State Loans and Guarantee Act, all private foreign borrowing requires approval by the External Loans Coordinating Committee. However, in terms of the new arrangements under the liberalized framework that became effective in February 2008, the Reserve Bank through an Exchange Control Directive, delegated some of the functions to Commercial Banks to register loans below USD5 million.

This Exchange Control Directive represented a major step towards the relaxation of the regime. It consolidates all previous decisions taken to gradually relax controls and attempt to rationalize the requirements for documentations and regulatory monitoring in respect of transactions which remain largely restricted and subject to specific documentary
requirements and procedures. In relation to inward private sector debt, the Circular is generally permissive and requires banks and financial institutions to consider requests for foreign loans, overdrafts, deferred payments or guarantees by residents which exceed 365 days, subject to certain requirements that include:-

(i) Submitting a copy of executed loan agreement and disbursement and debt service schedules thereto by the approving bank to the Reserve Bank of Zimbabwe within 14 days of grant of approval;

(ii) Interest rate and other charges reflecting the prevailing market conditions for relevant currency of borrowing;

(iii) Tying repayment period to the ability of the project to generate enough funds to service the loans in a progressive manner.

(iv) Non inclusion of conditions precedent which requires opening foreign currency accounts with banks not registered in Zimbabwe.

(v) Referring to the Reserve Bank of Zimbabwe (Exchange Control Department) for further guidance loan agreements with terms and conditions which are not compatible with the requirements (ii) through (iv).

In relation to transfers in respect of scheduled debt servicing, the Exchange Control Directive requires that that:-

(i) Remittances should sight the relevant contract as approved by a commercial bank plus creditors’ demand notes. Such remittances should not be affected by any bank other than the approving bank.

(ii) Commercial banks should furnish the Reserve Bank of Zimbabwe with monthly reports on loans serviced in conformity with prescribed format indicating ELCC Debt Record Number.
In consideration of deferred payments for imports or any financial facilities tenure which do not exceed 365 days, the Circular directs that:

(i) Interest rate and other charges if any should reflect the prevailing market conditions for the relevant currency of borrowing at the time of signing the relevant agreement;

- **The Reserve Bank of Zimbabwe Act**

The Reserve Bank Act is the source for the Exchange Control Act, which empowers the Reserve Bank to request any information considered necessary for the compilation and publication of balance of payment statistics. Such information relates to Current Account and Capital Account components and is normally obtained from the Zimbabwe Stock Exchange (portfolio investment), Zimbabwe Investment Centre (foreign direct investment, retained earnings on investments etc) and Commercial Banks (exports, imports etc).

### 2.5.2 Institutional Arrangements

Empirical evidence from literature confirms that institutions are now a critical component in economics. In Zimbabwe, institutions involved in private sector external debt management in the country are the Reserve Bank of Zimbabwe, commercial banks and borrowing entities.

**Reserve Bank of Zimbabwe**

At the Reserve Bank of Zimbabwe, two Departments are involved in the management of private sector external debt and these are the Banks Supervision and the Debt Management Departments.
(a) Debt Management Department

The Department, which houses the ELCC, is responsible for analysis of all loan agreements above the USD5 million threshold, in addition to recording private sector external debt in the country. In performing such function, the Department:

(i) Receives copies of loan agreements from commercial banks and records them in the External Loans database;
(ii) Records new loans, disbursements and debt services in the Commonwealth Secretariat Debt Recording and Management System (CS-DRMS);
(iii) Advises the borrowing entities through their commercial banks; and
(iv) Advises Government in formulation of policies related to private sector external borrowings.

(b) Banks Supervision Department

(i) Receives reports on private sector external debt disbursements and debt service payments by commercial banks;
(ii) Also receives information on other components of private sector external debt, such as derivatives and other related debt securities.

Commercial Banks

Following the delegation of powers to approve foreign borrowing to commercial banks, the banks are supposed to:
i. Act as intermediary between Reserve Bank of Zimbabwe and borrowers;

ii. Scrutinize and approve external loans up to USD5 million in line with the existing ELCC guidelines;

iii. Advise their clients on appropriate market interest rates;

iv. Submit to Reserve Bank signed copies of loan agreements on behalf of their clients for registration; and

v. Submit reports on private sector external debt disbursements and debt servicing to the Bank on monthly basis using Form EL-2.

External Loans Borrowers

Being the beneficiaries of external loans, private sector borrowers perform the following responsibilities as part of the debt management framework:

i. Identify borrowing needs and sources of financing;

ii. Negotiate on the borrowing terms;

iii. Conclude loan agreements;

iv. Register loan agreement with Reserve Bank through their commercial banks;

v. Report disbursements and debt service payments to the Reserve Bank through commercial banks; and

vi. Report debt related transactions to the Bank as and when required.

2.6 Section Conclusion

This Section looked at the concept of private sector external debt, its classification and definition. In addition, effort was done to bring an appreciation of the how this important
variable under study affects the level of growth in the economic. The relevant channels of such effect were therefore expounded as well as the institutional and regulatory arrangements on private sector external debt in Zimbabwe. In order to build on the model to be estimated in Section 4, a review of various strands of literature on external debt and growth were also explored. Generally, the information suggests that this area remains largely unexplored, although its relevance and importance in a set up like Zimbabwe cannot be understated.
SECTION THREE

Research Methodology

This particular Section seeks to specify the research methodology applied in the exposition of the relationship between private sector external debt and economic growth in Zimbabwe. This included the empirical model used, justification of variables selected and the estimation methodology applied.

3.1 Introduction

The goal of this paper is to investigate whether the share of the private sector in external debt has had a bearing on Zimbabwe’s growth patterns over the period 1980 to 2009. This objective is achieved adopting the methodology similar to the one applied by Asante (2000), where he complemented time series analysis with cross-sectional data to analyse the determinants of private investment behavior in Ghana. Time series data alone was not deemed sufficient to accurately account for the dynamics characterizing the relationship between these two variables due to data inaccuracies, unavailability and inconsistency. Cross sectional analysis through the administration of a questionnaire was therefore adopted to establish the relevance of this variable as an option for financing for development by Zimbabwean companies.

In order to investigate how the share of the private sector in total external debt affected the country’s historical growth pattern, the study employs time series data, which was principally obtained from several sources which include the Reserve Bank of Zimbabwe Quarterly Economic and Statistical Reviews (various issues), the Central Statistical Office, Readers' digest of Statistics, International Financial Statements Yearbooks (various), OECD, IMF and World Bank sites, UNCTAD and various sites from the website. The macroeconomic data
covers gross domestic product (GDP) and external debt between 1980 and 2009 in Zimbabwe.

3.2 Model Specification

3.2.1 The general model

According to Ayadi et al (2008), the rationale underlying the adoption of external finance against domestic borrowing as a way of ensuring sustained development is better explained by the ‘dual gap’ analysis. This theory asserts that investment is a function of savings and investment that requires domestic savings is not sufficient to ensure economic development. Under such instances, it is therefore necessary to have complementary external goods and services. Based on this, and combining the works of Seetanah et.al (2007), Fosu (1999), Iyoha (2000), and mainly Ajayi (2007), we formulate reduced form neoclassical growth model, which takes into account the external sector, debt indicators and selected macroeconomic variables.

Time series data tend to exhibit a stochastic or deterministic trend with the mean, variance and covariance changing over time, and thereby rendering the series non-stationary. The first step is thus testing for stationarity for each individual data series before estimating the equations. The null hypothesis of non-stationarity of the variables is tested against the alternative hypothesis of stationarity using the augmented Dickey-Fuller (ADF)-(Dickey-Fuller (1979)). The ADF test establishes the data generating process (DGP) from the following:

- Pure random walk
- Random with drift/constant
• Random walk with drift and time trend

To show the Dicky-Fuller (DF) test, the AR (1) process is shown.

\[ Y_t = \mu + \rho Y_{t-1} + \epsilon_t \]

Where \( \rho \) and \( \mu \) are parameters and \( \epsilon_t \) is a white noise. \( Y \) is stationary, if \( 1 < \rho < 1 \). If \( \rho = 1 \), \( y \) is non stationary. The test is carried out by estimating an equation with \( Y_{t-1} \) subtracted from both sides of equations.

\[ \Delta Y_t = \mu + \gamma Y_{t-1} + \epsilon_t \]

Where, \( \gamma = \rho - 1 \) and the null and alternative hypothesis are

- \( H_0 : \gamma = 0 \)
- \( H_1 : \gamma > 1 \)

The t-statistics under the null hypothesis of a unit root does not have the conventional t-distribution. Dicky-Fuller (1979) shows that the distribution is nonstandard, and simulated critical values for the selected sample. Later Mackinnon (1991) generalizes the critical values for any sample size by implementing a much larger set of simulations. One advantage of ADF is that it corrects for higher order serial correlation by adding lagged difference term on the right hand side. One of the important assumptions of DF test is that error terms are uncorrelated, homoscedastic as well as identically and independently distributed (iid).

Phillips-Perron (1988) has modified the DF test, known as PP test, which can be applied to situations where the above assumptions may not be valid. Another advantage of PP test is that it can also be applied to frequency domain approach, to time series analysis. The derivations of the PP test statistic is quite involved and hence not given here. The PP test has been shown to follow the same critical values as that of DF test, but has greater power to reject the null hypothesis of unit root test.
3.2.2 Model Specification

**Figure 7:** Model Specification

\[
\Delta GDP_t = \beta_0 + \beta_1 GDP_{t-1} + \beta_2 FDI_{t-1} + \beta_3 PSGD_{t-1} + \beta_4 LPSED_{t-1} + \\
\beta_5 LGV_{t-1} + \beta_6 LTRD_{t-1} + \sum_{i=0}^{n} \beta_{12} \Delta PSGD_{t-i} + \sum_{i=0}^{n} \beta_{13} \Delta LGV_{t-i} + \sum_{i=0}^{n} \Delta LTRD_{t-i} + u_t
\]

Where

- \( \Delta \) = is the difference operator
- \( \beta_0 \) = is a drift component
- GDP = Real GDP per capita
- FDI = Foreign Direct Investment
- PSGD = Public Sector Guaranteed Debt
- PSED = Private Sector External Debt
- GV = Government Expenditure (Consumption)
- TRD = Trade Openness (sum between exports and imports)
- \( \mu_t \) = is a white-noise disturbance term.

3.2.3 Definition and justification of variables

i. **Real Gross Domestic Product**

The dependent variable, GDP, proxied by per capital real gross domestic product, is chosen to represent economic growth. Gross Domestic Product measures the total output of goods and services produced in the country for final consumption within the boundaries of the country, regardless of who owns the factors of production used in the process. This proxy is relatively a good measure of economic performance since it focuses on domestic production which has a significant bearing on the general welfare of a country’s nationals. This proxy used for the GDP is consistent with the works of Kumar and Pradhan (2002) and Katerina et al (2004).
ii. Private Sector External Debt

This variable captures the component of private sector debt, which is the main variable in this study. Due to data inaccuracies and unavailability, this data was accessed from the World Bank Data Hub. However, based on the assessment of theory, and more importantly the notion that this type of debt compliments local savings, we postulate a positive relationship between this variable and economic growth.

iii. Public Sector Guaranteed Debt

This variable has been incorporated to compliment the incidence of private debt in the model. Its inclusion is consistent with the model by Seetanah (2002), where he incorporates public stock of debt which, however, is calculated using the Perpetual Inventory Method (PIM). This method was not adopted for these two debt variables due to data limitations. However, such data was one again obtained from the World Bank data hub and the study postulates the existence of a negative relationship between the stock of public debt and economic growth.

iv. Foreign Direct Investment

This variable is used to proxy foreign capital stock but due data limitations on foreign capital stock, different proxies are used in empirical work. Some studies used real gross FDI inflows (Frimpong and Oteng-Abiye, 2006) while others used gross FDI inflows (Blin and Quattara 2004; Zhang 2006) Following Balasubramanyan et al (1996) and Alfaro et al (2004), we adopt an inward FDI stocks. Based on a number of studies, it is considered that FDI positively affects economic growth via spill over effects and hence this research anticipates a positive relationship between FDI and economic growth.
v. **Degree of openness (TRD)**

This variable is used to capture the impact of trade openness on economic growth. Several proxies have been used to proxy degree of trade openness and these include the ratio of exports to manufacturing output, ratio of world price to domestic price indices and sum of exports and imports expressed as a ratio of GDP (see Atique *et al* 2004). This study therefore adopts the ration proposed by Atique *et al* (2004), which is calculated as:

\[
\frac{Exports + imports}{GDP}
\]

This variable shows how open the economy is to international trade and the selected proxy is preferred as it gives better estimates that portray the Zimbabwean case.

vi. **Government Expenditure (GV)**

This is defined as total government consumption expenditure plus total government gross fixed capital formation. The totals are for both central and local government. It is included to shed light on whether the government expenditure has affected the relationship. Conventional macroeconomic theory has generally assumed that increased government expenditure tends to lead to high aggregate demand and in turn, rapid economic growth. Wagnerian theory, however, leads toward the opposite view contending that an increase in national income causes more government expenditure.

3.3 **Cross sectional analysis**

3.2.1 **Data collection**
As alluded, cross sectional analysis, done through the administration of a questionnaire (See Appendix 1), was adopted to compliment the results of the time series analysis and thus help further probe understanding on the effect and contribution of private sector external debt on growth. In this research, a questionnaire in English and with fifteen clear and concise questions (Saunders, Lewis and Thornhill, 2009) was used to collect data from private companies regarding their views on the effect of private sector external debt in their operations in Zimbabwe.

3.2.2 Structure of questionnaire

Burns et al. (2002) define a questionnaire as a vehicle used to pose questions that the researcher wants respondents to answer. In that regard, the questionnaire was simplified to help extract the information regarded critical for the achievement of the objective of this study. The questionnaire was structured in four sections. (Section A dealt with the Understanding of PSED, Section B looked at the level of PSED, while Section C sought to address issues of utilisation of borrowed funds. Section concluded by addressing the borrowing arrangements.

3.2.3 Sources of Primary data

Data for cross sectional analysis was collected from a pool of private sector companies with proven borrowing records, which information was obtained from the database by the ELCC. Information was also obtained Commercial Banks in Zimbabwe, which also administer the registration of loans. The research location was therefore restricted to companies in Zimbabwe with offshore borrowings. Tabassum (2010) defines the location of a research study as the place where the data is collected.
3.2.4 Pilot study (questionnaire pretesting) and response rate

As a way of enhancing survey effectiveness, the questionnaire was pretested with five companies to gauge the anticipated reactions to the questions. This exercise helped check for ambiguities in the questions and also estimate the level of understanding of the questions from the respondents and to help in the elimination of bias. The pilot survey used convenience sampling in the selection of respondents.

In order to ensure a high response rate of about 74% as indicated in Section 5, the researcher used some of the techniques below;

- Preliminary notification of respondents through phoning them and making appointments with their offices well in advance. This was done to make sure that the respondents were available during the time of probing and interviewing.
- Making of follow-up- this included contacting respondents periodically after the initial contact so as to keep reminding them of the task to complete the research instruments submitted to them.

3.2.5 Data Analysis

Due to the nature of the data collected and the need to ensure accuracy of results, care was taken to ensure that all the information was correctly captured and processed through the Statistics Package for Social Sciences (SPSS) version 16. SPSS, due to its richness and analysis, provided the statistical analysis benchmark to the quantitative data. Microsoft Office tools like Excel 2007 and Windows 2007 also provided the platform for graphics used in this research.
SECTION FOUR

Estimation and Interpretation of results

This Section outlines the steps carried out in the estimation of the economic growth variable to see the relevance and contributory effect of private sector external debt. The statistical properties of the data are also outlined as well as the results of the empirical model for the impact of external debt on economic growth in Zimbabwe.

4.1 Unit Root Tests Results

In order to estimate the relationship between private sector external debt and economic growth, it was necessary to investigate the univariate properties of all data series by testing the stationary properties of the variables used in the time series analysis. As Jenkins (2000) notes, such an exercise normally complex due to the small sample sizes which mean that significant results are difficult to produce for most of the variables. The variables were therefore tested for stationarity using the Augmented Dickey-Fuller (ADF) unit root tests. The tests were first conducted on variables in their levels and some of the variables were integrated of order one while others were not. Table 4 shows the results thereof.

Table 5: Results of the unit root tests in levels

<table>
<thead>
<tr>
<th>Variable</th>
<th>ADF Test statistic</th>
<th>I(d)</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP</td>
<td>-2.3180</td>
<td>Nonstationary</td>
</tr>
<tr>
<td>GDP_1</td>
<td>-1.6855</td>
<td>Nonstationary</td>
</tr>
<tr>
<td>FDI</td>
<td>-2.7854</td>
<td>Stationary at 10% los</td>
</tr>
<tr>
<td>PSED</td>
<td>-1.6782</td>
<td>Nonstationary</td>
</tr>
<tr>
<td>PSGD</td>
<td>-2.3853</td>
<td>Nonstationary</td>
</tr>
<tr>
<td>TRD</td>
<td>-6.5653</td>
<td>Nonstationary</td>
</tr>
<tr>
<td>GV</td>
<td>-3.7313</td>
<td>Nonstationary</td>
</tr>
</tbody>
</table>

Source: Eviews Workfile

---

8 The consequence of working with non-stationary data series in the estimation process is that this may yield a meaningless or spurious result that culminates in the attainment of apparently significant regression results from unrelated data.
Since the t-adf statistics of all the other variables besides FDI are less than the critical values of -3.6959 (1%), -2.9750 (5%) and -2.6265 (10%), we accepted the null hypothesis of non-stationarity of the variables in their levels. We therefore proceeded to first differencing of the variables to induce stationarity after which all variables became stationary. Table 5 below shows these results.

**Table 6:** Test for stationarity of variables after differencing

<table>
<thead>
<tr>
<th>Variable</th>
<th>t-adf</th>
<th>I(d)</th>
</tr>
</thead>
<tbody>
<tr>
<td>DGDP</td>
<td>-4.833</td>
<td>Stationary</td>
</tr>
<tr>
<td>DGDP_1</td>
<td>-4.5873</td>
<td>Stationary</td>
</tr>
<tr>
<td>DFDI</td>
<td>-5.6015</td>
<td>Stationary</td>
</tr>
<tr>
<td>DPSED</td>
<td>-3.1417</td>
<td>Stationary</td>
</tr>
<tr>
<td>DPSGD</td>
<td>-4.0192</td>
<td>Stationary</td>
</tr>
<tr>
<td>DTRD</td>
<td>-6.5653</td>
<td>Stationary</td>
</tr>
<tr>
<td>DGV</td>
<td>-3.7313</td>
<td>Stationary</td>
</tr>
</tbody>
</table>

*Source: Eviews Workfile*

As the results show, all the variables are now stationary as the ADF Test statistic is now greater than the 5% critical value of -2.9750. The null hypothesis of on non-stationarity of the variables in their first differences was therefore rejected and we concluded that the variables are integrated of order one, that is I (1).

### 4.2 Estimation and Results

After allowing for non-stationarity of the variables, the study applied the time series data on the empirical model using the Ordinary Least Squares (OLS) method. The dependent variable was estimated using the OLS techniques on the selected choice of independent variables. Although the sample size appeared relatively small (29 variables), the results seem

---

9 means that the after differencing, the PSED variable is I (1) at the 5% and 10% levels of significance but not at the 1% level of significance.
to be consistent with literature theory and the developments characterising the country’s
growth pattern over the period. The results of the estimated long run relationship, of which
private sector external debt is a variable of interest, are shown in Table 6. (See Appendix 2a)

Table 7: Modelling DGDP using OLS: The long run static model

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Std error</th>
<th>t-value</th>
<th>t-prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant</td>
<td>153.3739</td>
<td>138.4542</td>
<td>1.107759</td>
<td>0.4339</td>
</tr>
<tr>
<td>DGDP_1</td>
<td>-0.130630</td>
<td>0.106072</td>
<td>-1.231520</td>
<td>0.2324</td>
</tr>
<tr>
<td>DFDI</td>
<td>2.148541</td>
<td>1.299143</td>
<td>1.653814</td>
<td>0.1138</td>
</tr>
<tr>
<td>DPSED</td>
<td>6.091145</td>
<td>2.414700</td>
<td>2.522526</td>
<td>0.0202</td>
</tr>
<tr>
<td>DPSGD</td>
<td>-1.170157</td>
<td>0.604696</td>
<td>-1.935117</td>
<td>0.0672</td>
</tr>
<tr>
<td>DTRD</td>
<td>-5778.873</td>
<td>627.4161</td>
<td>-9.210590</td>
<td>0.0000</td>
</tr>
<tr>
<td>DGV</td>
<td>0.979264</td>
<td>0.439951</td>
<td>2.225847</td>
<td>0.0377</td>
</tr>
</tbody>
</table>

R-squared = 0.833829  Adjusted R-squared = 0.783978  Durbin-Watson stat = 1.592024

Based on the results, the t-value of lagged value of GDP was relatively insignificant and the
variable was dropped from the long run equation. In addition, the DW test was relatively low,
suggesting the presence of auto-correlation in the model. As a result, only variables deemed
significant were incorporated into the new long run equation and although the coefficients
slightly changed, all the remaining variables were correctly signed. The result of this new
estimation after factoring in the new variables is therefore shown in Table 7 (See also
Appendix 2b).

Table 8: The Long run economic growth function

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Std error</th>
<th>t-value</th>
<th>t-prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>C</td>
<td>172.0515</td>
<td>131.6985</td>
<td>1.306404</td>
<td>0.2049</td>
</tr>
<tr>
<td>DFDI</td>
<td>1.586549</td>
<td>1.215875</td>
<td>1.304863</td>
<td>0.2054</td>
</tr>
<tr>
<td>DPSED</td>
<td>5.138293</td>
<td>2.281795</td>
<td>2.251865</td>
<td>0.0346</td>
</tr>
<tr>
<td>DPSGD</td>
<td>-1.350012</td>
<td>0.576438</td>
<td>-2.341991</td>
<td>0.0286</td>
</tr>
<tr>
<td>DGV</td>
<td>0.886614</td>
<td>0.430949</td>
<td>2.057354</td>
<td>0.0517</td>
</tr>
<tr>
<td>DTRD</td>
<td>-5772.051</td>
<td>603.8274</td>
<td>-9.559108</td>
<td>0.0000</td>
</tr>
</tbody>
</table>

R-squared 0.825256  Adjusted R-squared 0.785542  DW stat 1.740063
The DW statistic of 1.7400 shows the absence of autocorrelation in the error term. The R
squared of this model is comparatively higher at 82% suggesting that 82% of the change in
economic growth was influenced by these variables. In addition, the t-values of the selected
variables are within the required range and are significantly different from zero (0).
Important to note is the t-statistic of the FDI variable, which is below the standard value of 2,
suggesting that the FDI variable, was not a critical component of growth in this model. The
result was however retained so as to explain it in comparison with private sector external
debt. Based on these results, the long run estimated growth function is therefore given as
follows:

\[
DGDP = 172.06 + 1.5807DFDI + 5.138 DPSED - 1.350 PSGD + 0.8867 DGV – 5772.051 DTRD
\]

4.3 Explanation of the results

The coefficients of the variables in the long run equation are correctly signed a position
consistent with theory and similar empirical works. In addition, the explanatory power
reflects that about 82% of the movement in the GDP over the period under study was
explained by the explanatory variables listed in the model.

Consistent with the postulated hypothesis, private sector external debt was an important
facilitant of growth during the period under study, as evidenced by its strong positive
relationship with economic growth. This result fully supports the theoretical arguments
adopted in this study, which presupposes that private sector external debt was the main form
of finance for the private sector during a period where FDI flows and domestic savings were
erratic.
Although the FDI-Growth relationship is positive, the FDI variable’s contribution to growth was surpassed by that of private sector external debt for the period under review. Over the period, the country recorded higher levels of private sector external debt as compared to foreign direct investment, as shown in Figure 8.

While it would have been largely anticipated that FDI was a significant variable, developments in Zimbabwe prove that FDI was relatively low for long periods in the country. The period after 1998 saw a fall in the stock of FDI, a development that could be explained by capital flight especially after the ‘controversial’ policies which increased the riskiness of investing in the country (Mhone and Bond, 2002). In addition, there was a growing tendency of lack of capacity utilisation in the manufacturing sector, resulting in idle capital as many companies operated below capacity and hence the low contribution of FDI to growth over the period under review.
It is therefore clear that PSED provided the most consistent form of financing for
development, an argument consistent with findings by Singh (2000), who noted that large
corporations in developing countries relied heavily on external finance for growth, hence a
positive relationship between external debt and growth. As the results seem to suggest, a 1%
increase in the stock of PSED contributes a total of 5% to the change in GDP, while a
percentage change in foreign investment flows results in a change in GDP to the magnitude
of 1.2%.

The long run parameter of public sector guaranteed debt is significantly and negatively
associated to the output of the country. This suggests that the increased public stock of debt,
negatively affects growth. This finding is consistent with that of Seetanah (2007), who found
out that a 1% increase in the stock of public debt affected output negatively by 0.17% for a
study they carried out for Mauritius. In our analysis for the Zimbabwean case, this
preposition holds as the continuously accumulating stock of public debt has slowed
Government’s ability to borrow for developmental activities. The results seem to suggest that
a 1% increase in the stock of public sector external debt for Zimbabwe, negatively affected
growth by 1.5% therefore confirming that the country’s stock of public debt has reached
levels of unsustainability.

As regards the incidence of trade openness, Zimbabwe is more of an import dependent
economy, which relies heavily on imports. These have significantly increased over time
resulting in a negative Current Account Balance (CAB) on the Balance of Payments (BOP).
The TRD variable therefore appears to have been a significant deterrent to growth over the
period. The variable tended to be negative over time, due to the volume of imports which
outstripped exports. The increased imports resulted in increased outflows of foreign
payments (mainly primary products and service payments), thereby reducing the level of
foreign currency savings available to foster economic growth. Export performance was equally restrained over the period and as such, foreign exchange generation critical for funding local operations was restrained. The variable therefore had a deterrent effect on economic growth.

The coefficient of government expenditure was correctly signed as anticipated. As explained, an increase in government expenditure is assumed to lead to high aggregate demand and in turn, rapid economic growth. Although government expenditure fluctuated over the period, it remained high, save for the later years when economic activity fell. The results show that an increase in government expenditure of 1% stimulates economic activity by 0.88%, which is a positive result consistent with economic theory.

4.4 Section Conclusion

It is therefore evident from the foregoing that the other variables incorporated were equally critical in the determination of the overall economic growth in the country. All the coefficients obtained in this model are consistent various strands of literature on economic growth. Of importance however, is the relevance and strong contribution of the private sector external debt, which has not been a widely researched area. In spite of this, the model however perfectly fits the Zimbabwean scenario. Although the explanatory power suggests that the model might be a good fit, there could be some unexplained element suggested by some variables deemed to have been necessary but were not included due to data problems (unavailability and stationarity). These results will therefore be compared with those in Section 5, which outlines the presentation of the cross sectional data obtained through the administration of a questionnaire.
SECTION FIVE

Estimation and Interpretation of results

This Section outlines the steps carried out in the estimation of the economic growth variable to see the relevance and contributory effect of private sector external debt. The statistical properties of the data are also outlined in this Section.

5.1 Data Analysis

This Section outlines the comparative data analysis on information gathered using the questionnaire to compliment and buttress the findings of the time series data. As alluded, time series data may not accurately capture the relationship between the variables. The cross-sectional results are therefore meant to support the long run relationship established by the time series data. The primary data was therefore analyzed with reference to key areas of the research questions deemed necessary to sufficiently explore the dynamics of the time series data.

5.2 Consistency of the time series and cross-sectional results

The findings of these two methods of data analysis suggest the presence of congruency between the time series and cross sectional analysis as the results thereof have uniform conclusions. The results from the survey are supportive and strengthen the time series results which points to a significantly positive relationship between private sector external debt and growth over the period under study. This uniformity is expounded by the analysis of the various questions on the contributory effect of private sector external debt, which were administered through the questionnaire.

5.3 Descriptive Analysis of the questionnaire

A properly structured questionnaire incorporating the on the dynamics of private sector external debt was questionnaire was distributed to companies for analysis according to a...
number of variables which included the overall appreciation of private sector external debt and knowledge of its importance, levels of private sector external debt per company, other funding sources, its utilisation and ease of accessing such funding. A total of 73 questionnaires were issued out to various private companies foreign loans registered with the External Loans Coordinating Committee (ELCC).

Of these, 54 questionnaires were successfully administered, giving a response rate of 75%, a response rate achieved through the constant interaction with respondents and the simple and easy to complete questionnaires.

**Table 9: Questionnaire response rate**

<table>
<thead>
<tr>
<th>Sector</th>
<th>Number</th>
<th>%</th>
<th>Distributed</th>
<th>completed</th>
<th>Response rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mining Sector</td>
<td>26</td>
<td>0.36</td>
<td>26</td>
<td>21</td>
<td>80.77</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>18</td>
<td>0.25</td>
<td>18</td>
<td>15</td>
<td>83.33</td>
</tr>
<tr>
<td>Tourism</td>
<td>12</td>
<td>0.16</td>
<td>12</td>
<td>7</td>
<td>58.33</td>
</tr>
<tr>
<td>Telecomm</td>
<td>3</td>
<td>0.04</td>
<td>3</td>
<td>3</td>
<td>100.00</td>
</tr>
<tr>
<td>Other Sectors</td>
<td>14</td>
<td>0.19</td>
<td>14</td>
<td>8</td>
<td>57.14</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>73</td>
<td>1.00</td>
<td>73</td>
<td>54</td>
<td>73.97</td>
</tr>
</tbody>
</table>

Although the distribution of the questionnaires was done independent of the categorisation by sector, many of the companies fell under the mining and manufacturing and services sectors, which have predominantly been the major economic activity drivers, contributing significantly to economic growth. This explains their dominant access to private sector external debt as a financing option.

5.4 Understanding of Private Sector External Debt

5.4.1 Level of appreciation of private sector external debt
Generally, the majority of respondents (92%) seemed conversant with the concept of private sector external debt, its dynamics and importance in the firms' operations. This level of appreciation was largely attributable to the fact that many of the questionnaires were completed by staff with traceable financial acumen and who seemed to have been involved in the respective company’s deliberations on financing options. Questionnaires that constituted the ‘average’ and ‘don’t know’ categories represented companies with little appreciation of the concept, vis-à-vis the concept of external debt, categorisation and dynamics thereof. Figure 9 shows the levels of appreciation of this type of debt, which buttresses the importance of this variable as an important facilitants of growth.

**Figure 9**: Level of understanding of Private Sector External Debt

![Level of Understanding of concept of PSED](image)

5.4.2 **Factors affecting private sector borrowing decisions**

Most of the surveyed companies were largely motivated to borrow offshore due to the unavailability of funds on the local market as well as the cost of funds. Many companies faced constraints for much of the period, due to the various prevailing foreign exchange regimes, and hence borrowed offshore to fund their operations.
5.4.3 Importance of Private Sector External Debt

Private sector external debt was viewed by 85% of the respondents as an important source of financing due to the limited availability of funding on the local market. All these companies borrowed offshore to support their local operations, which is supportive of Singh’s (1994) findings that private sector external debt is an important financing option for large corporation operating in developing countries.

Figure 11: Importance of Private Sector External Debt as a source of Funding
The importance of private sector external debt was largely underscored by the absence of other financing options over the period characterised by a sluggish and deteriorating macro-economic landscape. Foreign direct investment was at its lowest, and much of the investment experienced was into small to medium activities. These qualitative findings are supportive of the time series data which shows that private sector external debt was the most important variable affecting growth. As explained, it 1% increased in this variable had the potential to contribute 6% to economic growth, compared to FDI, which based on the results was insignificant.

5.5 Levels of private sector external debt

5.5.1 Levels of PSED for period 2004-2009

As regards the levels of PSED, not much information was collected as respondents indicated the need for more time. As a result, analysis of this variable was restricted.

5.5.2 Other major sources of funding over the period

Private sector external debt is one of the various forms of funding available to companies for financing their developmental goals. Due to the cost of external funds, companies will always opt for cheaper methods of financing their activities. During the period under review, export earnings retained in exporting entities foreign currency accounts proved to be a critical source of financing activity. During the period, exporting entities were allowed to retain part of their export earnings for own use while non-exporting companies had to buy such resources from the interbank market, which lacked constant funding.
Other company’s also borrowed locally to compliment or substitute for private sector external debt, although such borrowings were expensive. However, with difficulties in accessing foreign borrowings due to the country’s unfavourable credit rating and constrained FDI levels, companies had to borrow locally. Rights issues have however become a way of raising additional capital from existing shareholders and this option has been widely done by a number of companies, especially in the services sector. Figure 12 shows the distribution of the financing options over the period.

**Figure 12:** Other sources of funding

<table>
<thead>
<tr>
<th>Other Sources of Funding</th>
<th>2009</th>
<th>2008</th>
<th>2007</th>
<th>2006</th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Local borrowings</td>
<td>11</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Export earnings</td>
<td></td>
<td>15</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Retained earnings</td>
<td></td>
<td></td>
<td>9</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rights issues</td>
<td>12</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>FDI</td>
<td></td>
<td></td>
<td></td>
<td>7</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

5.6 Utilisation of private sector external debt

5.6.1 Determination of how borrowed funds affected operations of companies

One of the critical considerations of this research paper is to establish how the funds borrowed were utilised, an activity done through the administration of the questionnaire. Interestingly, much of the contracted debt was considered to have been helpful in addressing the various companies’ financing constraints.
5.6.2 Application of funds borrowed

As regards utilisation of these funds, the survey also sought to determine how the short term and long term borrowings were applied. While utilisation seemed unstructured, much of these borrowing were short term borrowings requiring repayments in the short term. The purchase of machinery (39%) and raw materials (36%) were the more dominant beneficiaries of short term loans and this was largely through trade credits.

As regards long term borrowings, mining machinery accounted for a larger proportion of these borrowings (62%) while raw materials accounted for the balance. Unlike the utilisation of short term borrowings, no long term resources were channelled towards the payment of salaries or repayment of other loans.
5.6.3 Level of external debt arrears

Mkhonta (1999) notes that external debt affects economic growth in two ways. One such mechanism is through the required debt service payments which stifle economic growth by transferring resources out of the country. The survey therefore sought to establish the companies in such situation. Results confirm that while many companies had faced challenges in repaying their loans during the period of reduced foreign exchange availability, 76% of these companies were on schedule in terms of their external debt repayments.

5.7 Borrowing arrangements

5.7.1 Current procedural requirements

The institutional arrangements in place on the borrowing of external debt have a bearing on the level and frequency of such borrowings as well as its reporting for monitoring and
analytical purposes. The recently instituted liberalisation of Exchange Controls and relaxation of ELCC guidelines\textsuperscript{10} on registration of loans, seem to have enhanced convenience and flexibility of such borrowings and hence the increased activity. Given the importance of private sector external debt across the surveyed companies, the 61% of the companies found these arrangements flexible.

\textbf{Figure 15:} Comments on the flexibility of the current PSED borrowing mechanisms

\begin{figure}
\centering
\includegraphics[width=\textwidth]{figure15.png}
\caption{Institutional Borrowing Arrangements}
\end{figure}

5.7.2 \hspace{1em} \textbf{Future borrowing arrangements}

The revised economic growth forecasts of 7.8% (Ministry of Finance, Budget Statement, 2011), have created an impetus towards a renewed economic hope. The mining sector is anticipated to be the major economic driver, followed by the manufacturing and agricultural sectors. These sectors are capital intensive and require huge financing options. It is therefore

\textsuperscript{10} As explained in Section 2, loans above USD5 million are authorised by the External Loans Coordinating Committee and those below USD5 million are administered by Authorised Dealers.
no surprise that much of the anticipated future borrowings are earmarked towards the purchase of equipment, machinery and raw materials to support this economic revival.

**Figure 16:** Application of anticipated future borrowings from PSED

<table>
<thead>
<tr>
<th>Future Borrowing Arrangements</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Repayment of earlier loan</td>
<td>25</td>
</tr>
<tr>
<td>Payment of Salaries</td>
<td>9</td>
</tr>
<tr>
<td>Payment of recurrent bills</td>
<td>29</td>
</tr>
<tr>
<td>Purchase of raw materials</td>
<td>52</td>
</tr>
<tr>
<td>Purchase of Equipment</td>
<td>54</td>
</tr>
<tr>
<td>Purchase of Machinery</td>
<td>45</td>
</tr>
</tbody>
</table>

Once more, the mining and manufacturing sectors which contracted much of the private sector external debt position over the past ten years, are anticipated to dominate offshore borrowing in the coming years, as they build operational capacity through recapitalisation arrangements and replacement of worn our equipment.

**5.7.3 Anticipated type of future PSED borrowing.**

Consistent with developments under the prevailing multicurrency system, the improved foreign currency resources available to companies has enhanced their ability to meet short term obligations like payment of salaries and bill, hence much of the anticipated borrowings will be long term in nature and channeled towards tangible investment. Accordingly, the future borrowings preferences were trade credits (39%), short term (32%) and long term borrowings (29%).
5.8 Section Summary

It is clear that for a low income country like Zimbabwe which has not had access to international developmental finance and consistent foreign private capital flows, the share of the private sector in the total external debt has greatly played a significant role in the overall continued operation of local companies. The findings of this survey also buttresses the long run equation estimated in Section 4, where private sector external debt was a significant variable for financing of many countries, a development which positively affected the level of growth in the economy through private sector participation in economic activity.

Such has been the impact and importance of this variable, that many companies whose capacity utilisation is above average, accessed private sector external loans as a strategic financing option over time. Their ability to make timely payments ensured that such external debt was a critical variable for the growth experience.
SECTION SIX

Summary and Conclusions

This Section presents the conclusions and overall research conducted by emphasising the broad objective of the paper, which relates to the contribution of private sector external debt to growth in Zimbabwe. In addition, the section also looks at the limitations on effective execution of this study, as well as the recommendations and the areas that can be explored as part of further and future research on this subject matter.

6.1 Summary

Private sector external debt has increased significantly over the past two decades and has become an important variable for policy consideration whose role and importance can’t be ignored. Global statistics suggest that the growth of private sector external debt has been bolstered by various factors, key of which has been the rigorous privatisation and liberalisation of the manufacturing and banking sectors in many economies.

Due to this growing relevance, this paper undertook both a time series and cross sectional assessment of the overall economic growth impact of the component of private sector external debt on in Zimbabwe. As Singh (2002) points out, and as literature shows, not much research has been undertaken on the growth impact of this variable as focus has largely been on the more stable private capital flows such as FDI and the incidence on public external debt. As results of this research reveals, private sector external debt has significantly increased in growth and significance in Zimbabwe. Baball (2002) confirms this position, by noting that private sector external debt has grown and has become an important variable for consideration.
In order to therefore assert the relevance of this variable, a combination of both quantitative (time series) and qualitative (survey work) analysis was employed to ensure a more balanced exposition of this variable. Based on the results of the time series estimation, which adopted a reduced neoclassical growth model that took into account the incidence of private sector external debt, this component has been a significant facilitant of growth over a period characterised by reduced foreign private capital flows. While ordinarily, the more stable and non-creating variable of FDI should have been dominant, this has not been the case in Zimbabwe. This is because much of the growth and sustainability experienced by the private sector was largely anchored on the funding through private sector external debt, whose relevance and significance was buttressed by the qualitative approach to analysis of its impact.

Indeed, the questionnaire survey proved that private sector external debt was, and is an important component of the financing structures of many companies in an environment characterised by limited financing options. The results of this background research support the hypothesis that although private sector external debt is a small component of external debt, it has had a significant impact on overall growth, by acting as a valuable source of funding for many companies in the country. While the mining sector, which as at 2011 economic forecast is deemed to be country’s major economic growth driver (Budget Statement, 2011) was the major beneficiary of private sector external debt, other sectors also significantly benefited from its incidence in the country.

Despite attracting limited attention from researcher on its growth impacts, results from this study supports the importance of private sector external debt, which has largely been overlooked due to its perceived insignificant magnitude, and yet Zimbabwe it was a relevant and complimenting factor to the continued operation of many firms in the country. The
results therefore help buttress the need to build capacity in the monitoring and analysis of 
private sector external debt in Zimbabwe and the region at large.

It is therefore an unquestionable reality that in the absence of literature on this variable, this 
study has significantly contributed towards the extension and expansion of the existing body 
of literature on private capital flows in Zimbabwe, and more specifically on this component 
of external debt. Although private sector external debt still remains a small variable, it played 
a significant role in the country’s overall growth patterns due to the absence and erratic flow 
of other foreign private capital flows, which are significant financing mechanisms for the 
growth of the economy.

6.2 Broad limitations of the study

The absence of reliable data and literature on the relationship between private sector external 
debt and growth, proved a limitation on the effective execution of this study. This is a 
challenge that is characteristic of developing countries, hence the limited research work on 
variables of this magnitude. In addition, due to time constraints and data limitations, this 
study was restricted to one country, Zimbabwe. As a result, results obtained from this study 
cannot therefore be generalised to other countries where the growth impact of the magnitude 
of private sector external debt may have varied levels of significance.

Another limitation arose from the sample applied in the determination of importance of 
private sector external debt in Zimbabwe. While technically the model used in the study is 
complimentary in terms of consolidating the time series and cross sectional effects of private 
sector external debt, it was restricted to a number of companies available on the ELCC 
database. Due to absence of a comprehensive database and accurate reporting system of all
companies with private sector external loans, the results should be treated with caution as to the applicability of this variable to these companies.

While the questionnaire was meant to extract as much information as possible, its time frame was restricted to a historical five year period, which is contrary to an ideal setup where the questions should have captured a significantly longer period. Time constraints and potential institutional memory limitations, compromised the potential to broaden the scope of the exercise by extracting information over a longer period.

6.3 Policy Recommendations from the study

6.3.1 Foreign Private Capital Flows Surveys

The effective monitoring and analysis of the relevance of this variable and other capital flows require the availability of accurate statistics on these variables. One way of ensuring the attainment of this objective is for the country to urgently consider the institution of Foreign Private Investment (Capital) Surveys, as a way of gathering accurate data on the country’s level of flows and stocks of foreign private capital. Already, other countries\(^\text{11}\) in the region have conducted at least one survey on private capital flows to boost their comprehension of the level of such flows. Surveys of this magnitude therefore have a bearing on the country’s grasp of the magnitude, source, direction and volatility of private investment in Zimbabwe. Consideration of institution of surveys should therefore be a priority for the Government, which is eager to see investment growing to within 25% levels of the country’s GDP (STERP, 2009).

\(^{11}\) Zambia (3), Uganda (9), Tanzania (6), Malawi (2), Swaziland (1), Kenya (1), Lesotho (3), Botswana (1).
Technical expertise to facilitate the institution of such surveys can be availed from bodies such as MEFMI, which has been the driving force in a number of Private Capital Surveys being instituted in the regional block.

6.3.2 Private Sector External Debt Surveys

Limitations and unavailability of consistent data on private sector external debt requires an urgent consideration for a survey on private sector external debt. It is therefore clear that in spite of the institutional and regulatory mechanisms in place, there is an apparent lack of coordination on the collection on information on this variable. A survey to therefore collect this data, may act as a substitute for the robust and expensive Foreign Private Capital flows, by only targeting companies with foreign borrowings.

Such a survey on private sector external debt will help ensure accuracy, timeliness and reliability of information on private sector external borrowings. Issues that can be captured in such a survey may include:

Name of borrowing entity

- Creditor institution
- Debt outstanding and disbursed
- Undrawn amount
- Principal paid
- Principal in arrears
- Interest arrears
- Etc.
6.3.3 Building capacity and strengthening the framework on reporting of PSED

While the issue of Private Capital Surveys is a medium to long term solution to the improvement of private capital flows statistics due to the cost implications of such countrywide surveys, there is need to enhance the recording and monitoring of private sector external debt. The need becomes an important factor, especially under the current framework characterised by the liberalisation of exchange controls in Zimbabwe.

As Baball (2000) notes, under fully liberalised regimes, reporting of information is problematic. This is in contrast to controlled regimes where collection of information is greatly enhanced by the controls. The liberalised framework therefore requires review of mechanisms on reporting of data, which is crucial for analysis of this magnitude. Areas requiring attention are therefore:

- **Legislative framework**

Given the importance of private sector external debt and its growth impact, there should be a provision with the legislation that provides for the authority to allow effective collection of information on private sector external debt. Under the current multicurrency system, Zimbabwe’s Exchange Control regulations are yet to be finalised. The provision of such legislation will ensure that all information of this debt is recorded by the registering agents and timely forwarded (reported) to the Central Bank.

It is therefore expedient to continuously review the relevant Acts, Regulations, Circulars and Guidelines and propose recommendations that compel commercial banks to effectively
participate in reporting of data on private sector external debt to the Central Bank for recording.

- **Institutional coordination**

As noted, institutions are a necessary factor in influencing economic activity in many countries. As noted in this research, there a number of institutions that are involved in the monitoring and analysis of private sector external debt. The achievement of the desired goals of effective surveillance and understanding of this variable requires effective institutional coordination. This need cannot be overemphasised as coordination amongst all parties involved in the collection, analysis and monitoring of private sector external debt remains a critical factor for evaluating the effectiveness of this variable, so as to avoid duplication of activities, which may affect the response rate (Baball 2002).

In Zimbabwe there is need to ensure coordination between the ELCC, Exchange Control, Bank Supervision Department, Authorised Dealers, Zimbabwe Investment Authority, Ministry of Finance and other relevant bodies through a PSED Working Committee.

### 6.3.4 Development of mechanism (software) for recording data on PSED

With the current framework for collection and recording of information on private sector external debt largely manual, the attainment of accurate data on this variable, requires the establishment of a system (software) that facilitates and fosters the recording of external debt statistics\(^\text{12}\). Some of the MEFMI countries that have instituted Foreign Private Capital Flows

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\(^{12}\) Most countries currently use DMFAS and CS-DRMS for the recording, management and monitoring of publicly guaranteed private sector external debt.
Surveys are currently using the MEFMI Private Capital Monitoring System (PCMS) for the recording and analysis of data on private capital flows.

Due the absence of such surveys in Zimbabwe, it is therefore prudent to create a system that manages and consolidates the recording of all information on private sector external debt by all parties involved in the registration of private sector debt in the country. Such a system may not necessarily need to be expensive, but rather, a simplified mechanism of reporting information on private sector external debt.

6.4 Areas for Future Research

The area of private capital flows remains vast and laden with various areas of possible research due to the long term implications private capital flows can have on an economy. Going forward, it becomes imperative that at both country and regional level, resources be channelled towards the actual evaluation of implications of foreign private capital flows on various economic variables. Areas that require exposition include:

- Conducting a panel exposition of this variable amongst the MEFMI regional countries to establish impact of such a variable on growth and make conclusive remarks on its contributory effect on growth;
- Establishment of a system and mechanism that addresses the inter and intra MEFMI regional private capital flows (i.e. intraregional private investment flows), as a platform of extending the harmonisation efforts;
- Assessment of the implications of changing exchange control regimes on the incidence, growth and methods of collection of data of private sector external debt;
- Exposition of the private sector external debt, vis-à-vis, its behaviour in terms of determinants, magnitude, source and direction in Zimbabwe and in the region.


31. **Reserve Bank of Zimbabwe (2010)** Monetary Policy Statements,


38. **Zambia Foreign Private Investment Survey report, 2010**
APPENDIX 1: Questionnaire on the collection of information on PSED

QUESTIONNAIRE FOR THE ASSESSMENT OF THE CONTRIBUTION OF PRIVATE SECTOR EXTERNAL DEBT (PSED) TO ECONOMIC GROWTH IN ZIMBABWE

GRADUATE DEVELOPMENT PROGRAMME

This questionnaire is designed to help collect qualitative information on the contribution of Private Sector External Debt (PSED) to growth in Zimbabwe. Information collected through this questionnaire will be treated strictly confidentially.

ENTERPRISE DETAILS

Name of Company .................................................................
Sector of operation .............................................................
Year of incorporation ............................................................
Year of commencement of operations ....................................
E-mail of questionnaire respondent ........................................

SECTION A: UNDERSTANDING OF PSED

1. Please rate your company’s level of understanding of Private Sector External Debt (PSED). Please tick as appropriate: Put the following i-iv in a line to save space—make the tick box smaller.

   (i) Excellent [□]  (ii) Very Good[□]  (iii) Good[□]  (iv) Average [□]

2. Please list 3 most important factors that affect your borrowing decisions as a company?

   (i) .................................................................................................
   (ii) .................................................................................................
   (iii) .................................................................................................

3. Do you consider external debt as an important source of funding for your type of operations? Please tick.
   Yes_____  No_____

4. If yes, please briefly explain why

   ........................................................................................................
   ........................................................................................................
   ........................................................................................................

SECTION B: LEVEL OF PSED

5. What levels of PSED you have for the following period. Complete Table 1 below:
<table>
<thead>
<tr>
<th>Period</th>
<th>PSED US$</th>
<th>Type of debt(^\text{13})</th>
<th>Source Country i.e. country of borrowing</th>
<th>Short term or long term(^\text{14})</th>
<th>Other Forms of funding</th>
<th>Annual Turnover</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2006</td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>2007</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2008</td>
<td></td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>2009</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

6. What were the other major sources of funding for your company operations during these periods? Please list one or two most important

<table>
<thead>
<tr>
<th>Period</th>
<th>Other Source of Funding</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>..........................................................</td>
</tr>
<tr>
<td>2005</td>
<td>..........................................................</td>
</tr>
<tr>
<td>2006</td>
<td>..........................................................</td>
</tr>
<tr>
<td>2007</td>
<td>..........................................................</td>
</tr>
<tr>
<td>2008</td>
<td>..........................................................</td>
</tr>
<tr>
<td>2009</td>
<td>..........................................................</td>
</tr>
</tbody>
</table>

7. What factors affect or motivate these borrowings? Please list two most important reasons.

**Long term borrowing (LTB)**

..........................................................

..........................................................

**Short term borrowing (STB)**

..........................................................

..........................................................

**SECTION C: UTILISATION OF BORROWED FUNDS**

8. How did the funds borrowed affect the positive operations of your a company? Please tick as appropriate: do as suggested for question 1

   i. A great deal/indispensable □
   ii. Very helpful □
   iii. Helpful □

---

\(^{13}\) For Example trade credits, loans from offshore banks or from sister (affiliate companies)

\(^{14}\) Long Term (more than 12 months), Short Term (less than 12 months)
9. How did you apply/use the amounts borrowed? Please tick as appropriate:

<table>
<thead>
<tr>
<th>Short-Term Borrowing</th>
<th>Long-Term Borrowing</th>
</tr>
</thead>
<tbody>
<tr>
<td>i. Purchase of Machinery</td>
<td>Purchase of Machinery</td>
</tr>
<tr>
<td>ii. Purchase of raw materials</td>
<td>Purchase of raw materials</td>
</tr>
<tr>
<td>iii. Payment of recurrent bills.</td>
<td>Payment of recurrent bills.</td>
</tr>
<tr>
<td>v. Payments of salaries</td>
<td>Payments of salaries</td>
</tr>
<tr>
<td>v. To repay an earlier loan</td>
<td>To repay an earlier loan</td>
</tr>
</tbody>
</table>

Other (Specify)…………………………………………. Other (Specify)………………………………………….

10. What is your status in terms of repayment of the loans? Put these in a straight line.

   In arrears [ ]  Repayments on schedule [ ]

11. If in arrears, has how has this affected your operations

   i. Reduction in operational income [ ]
   ii. Failure to access other lines of credit [ ]
   iii. Reduced production [ ]

**SECTION D: BORROWING ARRANGEMENTS**

12. What is your view of the country’s current procedures for borrowing external debt?

   (i) Cumbersome [ ]   (ii) Flexible [ ]   (iii) requires amendments [ ]

13. Do you foresee an increase in borrowing by your company in the short to medium term?

   ………………………………………………………………………………………………………………………………………

14. What type of borrowing do you foresee, i.e. short term or long term, trade credits etc?

   (i) Short Term Borrowing [ ]
   (ii) Long Term Borrowing [ ]
   (iii) Trade Credits [ ]

15. What will these borrowings be for?

   ………………………………………………………………………………………………………………………………………

   Thank you for taking time to complete this questionnaire
APPENDIX 2: Econometric Results of the time series estimation

(a) Estimation of long run equation using all variables

Dependent Variable: DGDP
Method: Least Squares
Date: 04/30/11 Time: 19:19
Sample(adjusted): 1983 2009
Included observations: 27 after adjusting endpoints

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>C</td>
<td>153.3739</td>
<td>138.4542</td>
<td>1.107759</td>
<td>0.2811</td>
</tr>
<tr>
<td>DGDP_1</td>
<td>-0.130630</td>
<td>0.106072</td>
<td>-1.231520</td>
<td>0.2324</td>
</tr>
<tr>
<td>DFDI</td>
<td>2.148541</td>
<td>1.299143</td>
<td>1.653814</td>
<td>0.1138</td>
</tr>
<tr>
<td>DPSED</td>
<td>6.091145</td>
<td>2.414700</td>
<td>2.522526</td>
<td>0.0202</td>
</tr>
<tr>
<td>DPSGD</td>
<td>-1.170157</td>
<td>0.604696</td>
<td>-1.935117</td>
<td>0.0672</td>
</tr>
<tr>
<td>DGV</td>
<td>0.979264</td>
<td>0.439951</td>
<td>2.225847</td>
<td>0.0377</td>
</tr>
<tr>
<td>DTRD</td>
<td>-5778.873</td>
<td>627.4161</td>
<td>-9.210590</td>
<td>0.0000</td>
</tr>
</tbody>
</table>

R-squared 0.833829 Mean dependent var -120.4248
Adjusted R-squared 0.783978 S.D. dependent var 1309.425
S.E. of regression 608.5965 Akaike info criterion 15.87860
Sum squared resid 7407793 Schwarz criterion 16.21456
Log likelihood -207.3611 F-statistic 16.72637
Durbin-Watson stat 1.592024 Prob(F-statistic) 0.000001

(b) Estimation of equation after dropping the lagged value of GDP

Dependent Variable: DGDP
Method: Least Squares
Date: 04/30/11 Time: 19:28
Sample(adjusted): 1982 2009
Included observations: 28 after adjusting endpoints

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>C</td>
<td>172.0515</td>
<td>131.6985</td>
<td>1.306404</td>
<td>0.2049</td>
</tr>
<tr>
<td>DFDI</td>
<td>1.586549</td>
<td>1.215875</td>
<td>1.304863</td>
<td>0.2054</td>
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<tr>
<td>DPSED</td>
<td>5.138293</td>
<td>2.281795</td>
<td>2.251865</td>
<td>0.0346</td>
</tr>
<tr>
<td>DPSGD</td>
<td>-1.350012</td>
<td>0.576438</td>
<td>-2.341991</td>
<td>0.0286</td>
</tr>
<tr>
<td>DGV</td>
<td>0.886614</td>
<td>0.430949</td>
<td>2.057354</td>
<td>0.0517</td>
</tr>
<tr>
<td>DTRD</td>
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<td>603.8274</td>
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</table>

R-squared 0.825256 Mean dependent var -77.67174
Adjusted R-squared 0.785542 S.D. dependent var 1304.710
S.E. of regression 604.2067 Akaike info criterion 15.83312
Sum squared resid 8031445 Schwarz criterion 16.11859
Log likelihood -215.6637 F-statistic 16.72637
Durbin-Watson stat 1.592024 Prob(F-statistic) 0.000000