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THE POSSIBILITY OF REINTRODUCING THE ZIMBABWEAN DOLLAR

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ABSTRACT

The research was conducted to assess the possibility of reintroducing the Zimbabwean dollar. A descriptive research design was used in which data was collected from a sample of 183 respondents using questionnaires and interviews. This research found out that the current multicurrency regime has proved effective in that it has stabilized macroeconomic conditions, reduced inflation significantly and has provided a foundation for the resumption of economic growth. It was concluded that Zimbabwe was not yet ready to reintroduce the Zimbabwean dollar as there was need for commitment by the monetary authorities to maintain price stability, stem hyperinflation as well as guarantee the independence of monetary authorities.

Keywords: *dollarization, local currency, Zimbabwe*

INTRODUCTION

The period 1997-2008 is one that many will live to recall for a record of economic slump and hyperinflationary pressures in Zimbabwe. This period was characterised by a turbulent macro-economic environment which presented a very complex, mind blowing situation for policy makers, individuals and institutional investors and even the ordinary Zimbabwean out of the business arena. The path that the economy of Zimbabwe traversed was marked with deep setbacks like ever increasing average prices, artificial shortages, unstable energy supplies, contraction in economic activity, increasing unemployment and also soaring local and international relations. The country was ravaged by hyperinflation for a considerable period to such an extent that the value of the local currency, the Zimbabwean dollar (Z$), was estimated to have lost more than 99.99 percent of its value within a space of less than two years , between 2007 and 2008 (Hanke, 2008). The hyperinflation rate figures released by Zimbabwe's Central Statistical Office (CSO) in July 2008 indicated that the country's month-on-month inflation rate was estimated at 231.2 million percent, while the International Monetary Fund (IMF) estimated the hyperinflation rate to be 489 billion as of September 2008. (Makochekanwa n.d). During the hyperinflation period (2000 – January 2009, Zimbabweans felt the bitter brute as they had to cope with recurrent currency transitions from denomination notes of Z$5, Z$10 and Z$20 maxims to a currency whose denominations rapidly shifted from thousands, to millions, billions, trillions, quadrillion, hextillion, and ended at octillion by end of January 2009.

The erosion of the purchasing power was imminent and it caused a great challenge to the policy makers. The period saw policy makers going back and fourth the drawing boards every now and then to review interest rates and prices in both the commodity and financial markets to ensure stability and control in these markets. Monetary authorities alike continued to adjust policies so as to make sure that the economic ship would not succumb to the inflationary tide that had ravaged the country. Most businesses did fall prey to the deteriorating economic scam, as they could not afford to sustain their operations. Despite all the efforts the macroeconomic fundamentals went negative and not even one had been solved amicably. As long as there was no sustainable

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economic growth, stable Balance Of Payment, full or near full employment, then the achievement of low levels of inflation were just but a long run dream, yet in the long run we will all be dead (The Economist, 2005).

This led the country to voluntarily abandon one of its sovereign symbols, by adopting the use of other foreign currencies as means of payments, unit of account, store of value and standard of deferred payments (Makochekanwa n.d). In an attempt to restore credibility in the monetary system and also to arrest the hyperinflationary trend, the government of Zimbabwe voluntarily abandoned one of its sovereign symbols, its monetary currency, the Zimbabwean dollar (Z$) and introduced the use of multicurrency on 30th January 2009.

Following the introduction of this multi currency regime, month-on-month inflation trend sharply declined, as the country for the first time in more than a decade registered a positive economic growth rate and average production activities have leapfrogged from less than 10% in January 2009 to above 35% by end of December 2009. In short, the introduction of the multi-currency regime has improved the country's economic health. According to the country's three year macroeconomic framework announced by The Reserve Bank of Zimbabwe Governor on 23 December 2009, "Government will, therefore, maintain the principle of use of multiple currencies over the Framework period 2010 – 2012". The question that arises is when and how the country will reintroduce the Zimbabwean dollar. It is this apparent dilemma and uncertainty in the economy that has propelled the need for such an enquiry. The general populace seemingly is satisfied with the status quo but however uncertain as to the span of time that this multi-currency system is going to be operational. They argue that, the current system has brought sanity, stability and affordability into the economy as a whole. On the other hand others are of the view that, though there has been marked improvement in economic stability, inflation stability during the multi-currency era, Zimbabwe as a nation still has a national pride and sovereignty to protect and this can only be done through having its own currency. It is through these mixed ideas and uncertainty as to what should be done and whether the Zimbabwean dollar should come back or continue with the current system of multi-currency. Thus the main objective of this research is to assess the possibility of reintroducing the Zimbabwe dollar back into circulation. This investigation is paramount because firstly, the use of multicurrency is temporary, and secondly, the country needs a permanent single currency in its monetary system.

LITERATURE REVIEW

Dollarization

According to Bogetic, (2000), dollarization is the broad use of a foreign currency as the means of exchange for formal or informal transactions. It is important to distinguish between two types of dollarization: official or full dollarization, and unofficial or partial dollarization.

Unofficial dollarization occurs when monetary authorities adopt the US dollar as legal tender for all transactions. The US dollar takes over all functions of domestic money: unit of account, medium of exchange and store of value (Agnoli 2002, Hanke 2008, Cohen)

Unofficial or partial dollarization refers to the process by which individuals substitute domestic currency with foreign currency to make transactions and allocate their financial assets. In such cases, the monetary authorities do not necessarily promote or encourage dollarization. Partial dollarization typically responds to the need to protect the purchasing power of money income and assets in domestic currency from the perverse effects of high inflation rates. (Agnoli 2002, Hanke 2008, Cohen 2000)

The effects of dollarization

Several authors have highlighted that there are several effects of dollarizing an economy and these are summarised in the table below:

Advantages of dollarisation	***References***
Financial and monetary integration	Barro and Gordon (1983), Goldfajn and Olivares (2000), Cohen (2000),
Reduced transaction costs	Rose (2000), Kramarenko *et al* (2010), Makockekana (n.d)
Enhanced economic integration	Frankel and Rose (1998), Berg and Borensztein (2000), Dallas and Tavlas (2001)
Sound Financial system	Berg and Borensztein (2000), Agnoli (2002)

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Economic policy credibility	Fischer 91982), Eichengreen (2000), Agnoli (2002), Kramarenko *et al* (2010)
Disadvantages of dollarisation	
Forfeiture of national monetary autonomy	Frankel and Rose (1998), Makochekana (n.d.), Agnoli (2002), Kramarenko *et al* (2010)
Loss of seigniorage	Cohen (2002)Agnoli (2002), Burdekin (2008), Makochekana (n.d.) Kramarenko *et al* (2010)
Loss of effective lender of last resort	Berg and Borensztein (2000), Agnoli (2002), Makochekana (n.d.) Kramarenko *et al* (2010)
Loss of sovereignty	Cohen (2002)Agnoli (2002), Burdekin (2008), Makochekana (n.d.) Kramarenko *et al* (2010)
Inability to adjust exchange rates	Berg and Borensztein (2000), Agnoli (2002), Makochekana (n.d.)

Dollarization in other countries

Several big economies have officially dollarized and amongst them are:

i. Panama in 1904
ii. Argentina, which replaced its own currency with the US dollar in 1991, in response to hyperinflation and an economic and political crisis.
iii. El Salvador, which adopted the US dollar in 2001.
iv. Ecuador in 2000
v. Brazil and Mexico in the 1990s.

Cases where dollarization was abandoned

Dollarization is often seen as irreversible (IMF, 2006). Indeed, cases of abandoning dollarization are rare, and mostly related to the gaining of independence by the respective countries. An exception is Liberia, where political turmoil and civil war ended more than one hundred years of dollarization.

The Economist (2000) stated that dollarization should not be considered a blow to national pride but rather, a logical extension of the principles underlying the Convertibility Law. Some people may think that dollarization, if adopted, should be only temporary. The Economist (2000) further highlighted that the exit strategies for official dollarization are rather rare. They were often the result of a struggle for independence in the distant past, and the only example in modern history is Liberia where dollarization occurred due to the reduction of money in circulation, civil war, and the high fiscal deficit. As there is no empirical evidence, it is difficult to forecast what would happen to the economic performance of a country that opted for this strategy.

According to The Economist (2000), de-dollarization in unofficially dollarized countries has occurred more often. Whether it was voluntary (e.g. much higher interest rates for domestic currency deposits) or forced (Bolivia, Mexico, Peru and other countries have conducted forced conversion of foreign currency deposits), de-dollarization has caused adverse consequences, as a rule.

RESEARCH METHODOLOGY

The research took a descriptive design and was conducted in Harare which is the capital city and has the greatest population of the country. Data was collected using interviews and 200 questionnaires which were administered to a sample drawn from five strata's namely the academics, government departments, financial industry, business community and the public at large. A total of 183 questionnaires were returned and only 180 could be used for the analysis.

FINDINGS AND DISCUSSION

Data collection started by gathering information pertaining to the economic performance of the multi currency system that was in use in the country. The results are presented in fig 1 below.

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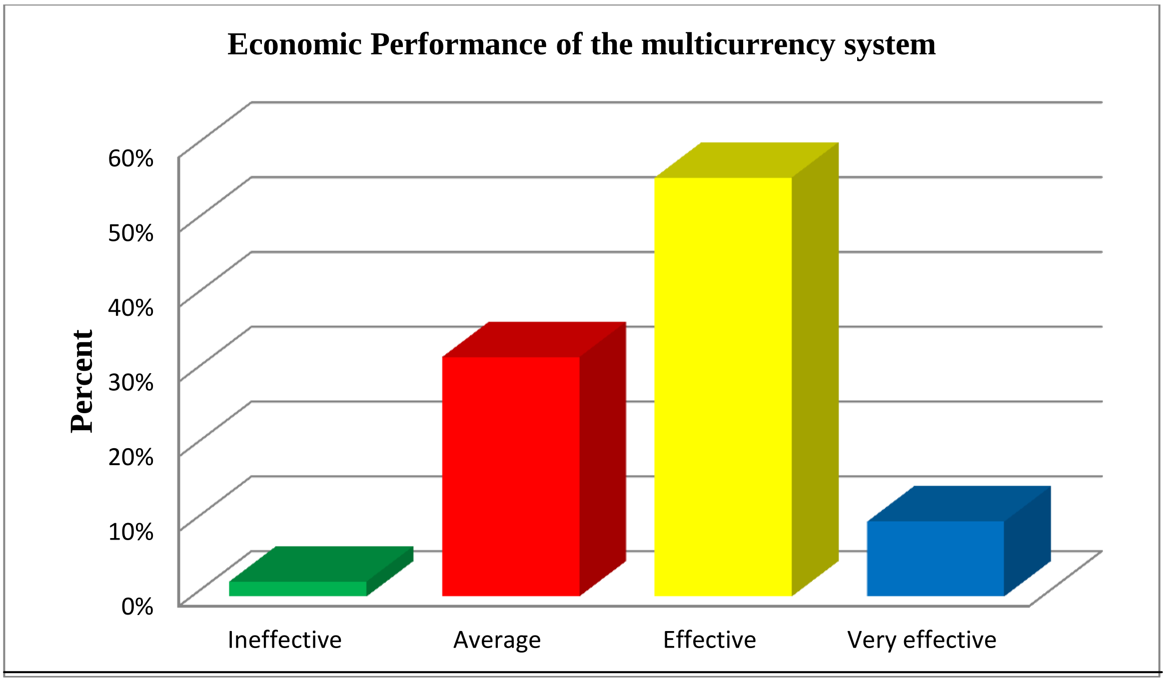

Figure 1: Economic performance of the multicurrency system

Source: Raw data

Of the total respondents 52% indicated that the multi currency system regime was effective, 10% indicated that it was very effective whilst only 2% said that the multicurrency system is ineffective, 32% rated it average. This shows that the majority of the respondents were in harmony with the multicurrency system.

The research brought out that the adoption of the multi-currency system in Zimbabwe has been effectively reducing inflation from 4 digit number to a single digit number within a short space of time. This current multi currency regime has brought about macro economic stability, thus restoring credibility and confidence to our economy.

Advantages of reintroducing the Zimbabwean dollar
Further the research sought to establish whether people can anticipate any advantages of using the local currency again. Results obtained are shown in the fig 2 below:

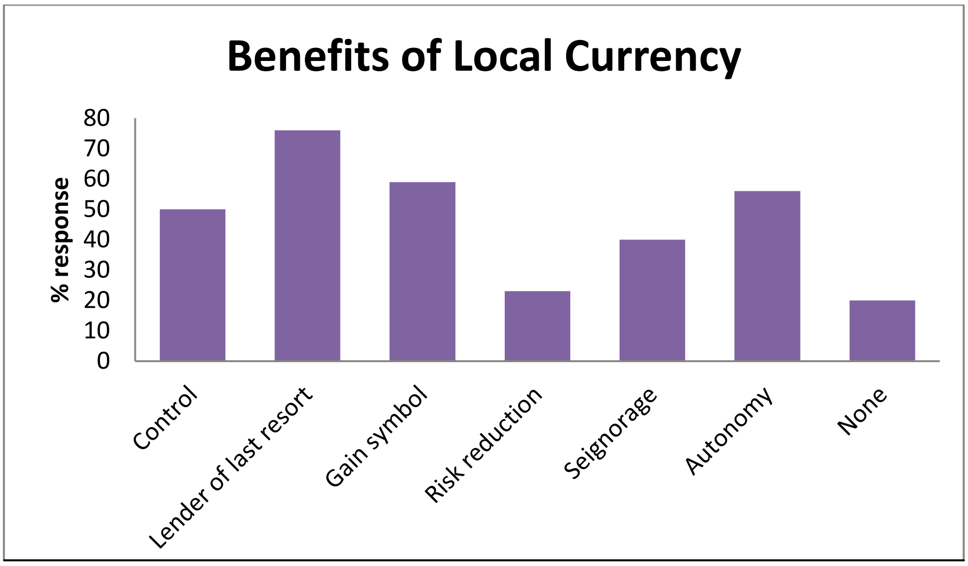

Figure 2: Advantages of re-introducing the Zimbabwean dollar (%)

Source: Raw data

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The research established that the reintroduction of the Zimbabwean dollar has several advantages. The major advantage cited by the business community was the fact that the reintroduction of the Zimbabwean dollar would reinstate the lender of last resort (76%) function of the Reserve bank of Zimbabwe. Thus in times of financial distress banks would be able to be rescued. Other advantages cited were the ability of the nation to regain its symbol (59%), Risk reduction (23%), seignorage (40%), control (50%) and the ability to influence exchange rates (56%). Of the total respondents 20% felt that the reintroduction of the Zimbabwean dollar brought no advantages at all to the nation.

The respondents interviewed cited that reintroducing the Zimbabwean dollar gives rise to several advantages. These included national autonomy over monetary and exchange rate policy, income from seignorage (the profit from issuing currency), and the ability of the central bank to act as lender of last resort to the banking system. Having a national currency provides the ability to use monetary policy to respond to external economic shocks and to adjust the exchange rate to address competitiveness concerns. However this analysis is in line with what Culp (1998) found out in Argentina's currency crisis that the peso which was Argentina's local currency, was essential to sovereignty and the nation's pride and was readily available and easy to control.

Disadvantages of using the Zimbabwean dollar

Respondents were also requested to indicate the disadvantages that would arise should they revert back to the use of the local currency. The following results were obtained.

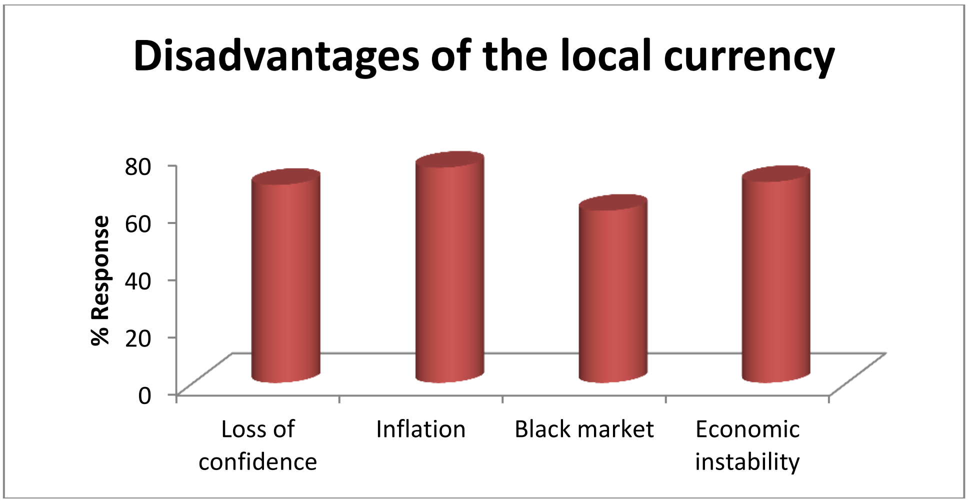

Figure 3: Disadvantages of re-introducing the Zimbabwean dollar (%)

Source: Raw data

Respondents indicated great concern if the local currency was to be brought back into circulation. It was felt that if the local currency was to be brought back into circulation then loss of confidence (69%) of the currency due to high inflation (75%) would start to be experienced. There was also the likelihood that the black market (60%) would flourish as people would seek to lock value of their money in more stable currencies. Of the total respondents 70% felt that there would be general instability of the economy if the local currency was to be reintroduced. Interviews conducted revealed that although several benefits of using the local currency had been cited, there were also major pitfalls that were associated with such a move.

Advantages of dollarisation

Respondents interviewed highlighted several benefits that they experienced from the use of the US dollar. They stated that the dollar circulates more widelyand has resulted in an improvement in economic activity. Supplies of basic commodities returned to the supermarket shelves and commodity prices came down. There was also disappearance of the winding queues at banks. Bankers and financial analysts indicated that dollarization was essential in attracting foreign currency and increasing its circulation in the formalized market. Dollarisation also led to the viability of the financial sector.

Disadvantages of dollarization

Whilst respondents noted several benefits of using the dollar as the official currency they however noted some problems that were associated. They indicated that there was a problem with coins and shipping these from the US was prohibitively costly. The financial sector contracted making it more vulnerable to liquidity and solvency risk.

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Respondents readiness for ZWD reintroduction

The research sought to establish whether the nation was ready for the reintroduction of the local currency. Responses are shown in the table below:

Reintroducing the ZWD

Should the Zimbabwean dollar be reintroduced	Analysis per strata					Total
	Academics	Business Community	General public	Financial Players	Government departments	
Yes	2%	5%	3%	1%	7%	**18%**
No	20%	4%	32%	6%	16%	**78%**
Not sure	0	1%	0%	1%	2%	**4%**
Total	**22%**	**10%**	**35%**	**8%**	**25%**	**100%**

Source: Primary data

From the table above, a significant majority of the respondents comprising 78% were against the reintroduction of the Zimbabwean dollar, whilst 18% were for the reintroduction, with remaining 4% being indifferent. Most of those respondents who said no to the reintroduction of the Zimbabwean dollar, that is 78% comprise 20% from the Academics, 4% from the Business community, 32% were from the general public, 6% and 16% were from the financial players and the government departments respectively. On the other hand, 18% (those who said yes) is made of 2%, 5%, 3%, 1% and 7% from the academics, business community, general public, financial players and the government departments respectively. This shows that the general public is not prepared for the reintroduction of the Zimbabwe dollar.

According to the findings above, it is apparent that people are not yet ready to have the Zimbabwean dollar reintroduced and this can be supported by a research in the Economist (2000) which highlighted that the exit strategies for official dollarization are rather rare.

One of the main reasons why people are not for the reintroduction of the Zimbabwean dollar is that the local currency will not bring macro- economic stability. Dollarization is expected to foster macro economic stability by solving the credibility problem that arises when a domestic central bank is unable to pre commit itself to a low rate of inflation.

Other researchers have brought out that a country can only be ready to introduce its local currency when there is a commitment by the monetary authorities of that country to maintain price stability, stem hyperinflation as well as guarantee the independence of monetary authorities. This may be established by reforming institutions such as the central bank or introducing a Currency Board in order to return the confidence of market participants in them (Kararach *et al*, 2010).

In a research carried out by Kararach *et al* (2010) restoring the local currency as well as maintaining a flexible exchange rate was ranked as the last option since it also requires the same level of commitment by the authorities. In addition the choice is negatively affected by the same moral hazard and adverse selection issues and the incentive compatibility constraints that are likely to make market participants remain uncertain about the behaviour of the authorities given past experience. It is extremely difficult to make market participants believe that the authorities will not abandon it in favour of printing more money and bringing back hyperinflation (Diamond and Dybvig, 1983 cited by *Kararach et al* (2010). This requires the credibility problem to be resolved first through the reform of institutions. Given the loss of credibility of the local currency in sight of the majority citizens, its come back can only be viable when a management system has been put in place to ensure that the currency will not return to the same problems which forced the country to abandon it in the first place thus his study recommended dollarization as the best currency option for Zimbabwe.

Capacity for Zimbabwe to administer its own currency

Responses obtained from both questionnaires and interviews brought out that reintroducing the Zimbabwe dollar at the present time would lead to a reversal of recent economic gains thus undermining macroeconomic stabilization, threaten a return to hyperinflation, and undermine the credibility that is beginning to be rebuilt. It is also clear that there is no appetite amongst firms and households for a return to the Zimbabwe dollar, and such a currency would not be willingly held. This is in line with Argentina's currency crisis as highlighted earlier.

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However those interviewed noted that while the problem of whether Zimbabwe is ready to administer the national currency or not was quite prevalent, nothing meaningful has been done by our monetary authorities and heads of governments to address this issue.

Conditions necessary for the reintroduction of the Zimbabwean dollar

According to Kararach *et al* (2010) challenges that compromised the Reserve Bank's credibility and integrity include weaknesses in the current Reserve Bank Act, the absence of a functioning board, involvement of the bank in non-core activities as well as deficiencies in the Reserve Bank's accounting practices. Bank operations, accounting and reporting systems failed to comply with requirements of the International Financial Reporting Standards (IFRS). Bank reforms being considered include putting in place a Reserve Bank governance structure that ensures effective oversight and accountability of the bank through an appropriate non-executive board and refocusing the bank to its core functions of supervising and regulating the financial sector, monetary policy and payments system. The reforms are also aimed at making the Reserve Bank independent by appropriately limiting the government's operations and oversight while ensuring that effective accountability mechanisms are maintained (Government of Zimbabwe (GOZ), Mid-Term Fiscal Statement, July 2009). An examination of the pre-reform scenarios and post-reform forecasts may be undertaken using banking models in which the money supply process is appropriately adjusted.

CONCLUSIONS

The research was conducted to investigate the possibility of reintroducing the Zimbabwean dollar. This research found out that the current multicurrency regime has proved effective in the sense that it has stabilized macroeconomic conditions, reduced inflation significantly and has provided a foundation for resumption of economic growth.

From the research it was found out that Zimbabwe is not yet ready to reintroduce the Zimbabwean dollar because as of late there was no commitment by the monetary authorities to maintain price stability, stem hyperinflation as well as guarantee the independence of monetary authorities.

RECOMMENDATIONS

It is recommended that while the issue of retaining our national currency is being debated the current multi-currency system should be maintained. Monetary authorities and heads of government reintroduce the Zimbabwe dollar if and only when there is a track record of sound fiscal policy implementation and adoption of new Central Bank legislation focusing on price stability and ensuring central bank credibility and accountability

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