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1. INTRODUCTION AND BACKGROUND

- 1.1 Zimbabwe has, over the past few years, received considerable adverse international media reports, as well as covert and overt alienation by some few countries, primarily on the back of the inevitable Land Reform Program the country implemented.
- 1.2 Within this context, debate has also been generated on whether or not Zimbabwe, as a country was under sanctions.
- 1.3 Others have argued that the “smart sanctions”, imposing travel bans on targeted individuals have not imposed an adverse burden on the economy as a whole.
- 1.4 However, adverse publicity, coupled with punitive measures by some foreign governments, multilateral institutions, as well as some private sector entities have worked to constrain the policy options available to the country, which in effect has worked to worsen the socio-economic environment, with the poor and the vulnerable groups being the hardest hit.
- 1.5 This Supplement explores the contextual form and meaning of a country under sanctions, and evaluates the extent to which the Zimbabwean economy’s performance has been constrained due to the phenomenon of sanctions.

2. DEFINITION OF SANCTIONS

- 2.1 Sanctions generally entail restrictions upon international trade and finance that one country imposes on another for political reasons. Traditionally, sanctions have taken the form of **arms embargoes**, imposition of **trade and financial restrictions**, **interruption of relations by air and sea** and **diplomatic isolation**.
- 2.2 Sanctions are basically measures applied in response to **perceived wrong doing by a state**, such as **an act of aggression against another state** or **human rights violation** from the perspectives of international conventions.
- 2.3 Sanctions are used as a policy of **segregation for political and economic isolation** by the imposing entities.
- 2.4 In recent years, the coverage of sanctions has widened to include other elements that are not directly linked **to trade and commerce** such as **culture and sports**.
- 2.5 Sanctions may also involve bans on **economic, sporting and cultural contacts** between countries, as well as “person – to-person” sanctions such as withholding visas or other diplomatic documents from citizens of another state.

- 2.6 **Economic sanctions** are usually the most common of all sanctions imposed on a nation. They imply the deliberate government aspired withdrawal, or **threat of withdrawal of trade and financial relations including technical cooperation.**
- 2.7 The United Nations Secretary General, Mr Kofi Annan highlighted that **‘sanctions remain a blunt instrument, which hurt large numbers of people who are not their primary targets’.**¹
- 2.8 In an effort to refine the effectiveness of sanctions, there has been a shift towards targeted sanctions which impose **travel bans** and **freezing of foreign bank accounts** of targeted individuals or entities.

3. TYPES OF SANCTIONS IMPOSED ON ZIMBABWE

Declared Sanctions

- 3.1 These are sanctions which are pronounced and normally legislated by the imposing country or organization. Targeted sanctions or smart sanctions fall under this category.
- 3.2 Targeted sanctions are meant to be precise, seeking to focus their impact on targeted individuals, with a **theoretically minimal** negative impact on the **general populace**. Typical examples of targeted sanctions for Zimbabwe include the Zimbabwe Democracy and Economic Recovery Act of 2001 by the US.
- 3.3 **The Zimbabwe Democracy Economic Recovery Act Of 2001 (Zidera)**
- 3.3.1 The Zimbabwe Democracy Economic Recovery Act of 2001 Section 4(c) Sub-section 1 **allows US executive director to each international financial institution to oppose the vote against any extension by the respective institution of any loan, credit, or guarantee to the Government of Zimbabwe; or any cancellation or reduction of indebtedness owed by the Government of Zimbabwe to the United States or any international financial institution (Zimbabwe Democracy and Economic Recovery Act, 2001).**

¹ Excerpts from Introductory Remarks made by Secretary General of the UN to the International Peace Academy’s “Seminar on Sanctions”, New York City, 17 April 2000

Undeclared Sanctions

- 3.4 These types of sanctions are **not announced but are implied from the declared sanctions**.
- 3.5 A good example is where Non-Governmental Organizations have moved their operations out of Zimbabwe since the enactment of the Zimbabwe Democracy and Economic Recovery Act of 2001. This Act outlines the scope of targeted sanctions on Zimbabwe by the USA.

4. ANALYSIS OF EFFECTS OF SANCTIONS ON ZIMBABWE

Impact on the Financial Sector

- 4.1 The combined effects of declared and undeclared sanctions on Zimbabwe has been to worsen the country's BOP position as characterized by the following:

Decline in BOP Support

- 4.2 Zimbabwe's balance of payments position has deteriorated significantly since 1997. In 1997, it deteriorated from a deficit of US\$21 million to US\$740 million. This unfavourable development emanated from the combined effects of poor export performance, high import demand, and reduced capital inflows, on the back of adverse publicity.
- 4.3 A combination of current account deficits and reduced capital inflows, resulted in **excessive pressures on foreign exchange reserves**, which, as a result, declined from **US\$830 million (3 months import cover in 1996) to US\$272 million (1 month import cover) by end 1997**.
- 4.4 The attendant foreign exchange shortages severely constrained the country's capacity to meet foreign payment obligations and **finance critical imports, such as drugs, grain, fuel and electricity**.
- 4.5 Reflecting the shortages of foreign exchange, there has been a significant **build up in external payments arrears**. At the end of **1999, total foreign payments arrears amounted to US\$109 million and have since increased astronomically to US\$2 073.7 million by end of 2005**.

- 4.6 This unfavourable development in the external sector has worsened the country's creditworthiness as the country's risk profile was heightened. This subsequently led to the drying up of traditional sources of external finance from the donor community.
- 4.7 The withdrawal of the multilateral financial institutions from providing Balance of Payments support to Zimbabwe had a **demonstration effect** as some other bilateral creditors and donors also followed suit by either scaling down or suspending disbursements on existing loans for both Government and Parastatal loans.
- 4.8 Prior to these developments, the country had an impeccable record of prompt debt servicing and was highly rated in the international financial markets.
- 4.9 The capital account, traditionally a surplus account, has been in deficit since 2000. This largely resulted from the perceived high country risk by both multilateral and bilateral creditors. As such, international investors preferred other countries for investment, thus depriving Zimbabwe of the much-needed foreign direct investment.

Table 1: The Balance of Payments Summary: US\$ millions

	1997	1998	1999	2000	2001	2002	2003	2004
Current Account	-796.5	-355.6	39.1	-135	-86.5	-217.1	-345.9	-416.7
Capital Account	-63.9	74.1	189.1	-315.1	-403.4	-232.8	-221.4	-244
Overall Balance	-740	-298.2	0.5	-171.1	-193.8	-371.5	-488	-302.8

- 4.10 The overall balance of payments position is estimated to have recorded a **deficit of US\$266 million in 2005**. This was financed through the accumulation of arrears which ended the year at US\$2 073.7 million.

Sustained Decline in Offshore Financing

- 4.11 The combined effect of arrears has been to worsen the country's relations with international creditors, thus creating a vicious circle.
- 4.12 The current wave of declared and undeclared sanctions is negatively affecting the image of the country, thereby distorting how financial markets assess the risk profile of Zimbabwe.

- 4.13 As a result, Zimbabwean companies are finding it extremely difficult to **access offshore lines of credit** because of the perceived country risk. Against this background, Zimbabwean companies have, over the past 5 or so years been dealing with their international suppliers strictly on a cash-upfront basis, with very minimal credit terms.
- 4.14 If the private companies manage to secure offshore financing it is usually at very high interest rates. Risk premiums have been pegged at high rates ranging from 8 to 15% above LIBOR, making it very expensive to borrow.
- 4.15 Zimbabwean importers are asked to pay cash upfront resulting in a significant squeeze on private sector cash flows. The deterioration in the balance of payments has led to bigger challenges, including underutilization of capacity and foreign exchange shortages.

Sustained Decline in Long-Term Capital

- 4.16 The sustained decline in long-term capital inflows has had ripple effects on the country's **employment levels, and its ability to provide basic goods and services to its people, ultimately leading to a decline in the standards of living.**
- 4.17 The result has been large scale emigration, especially of skilled labour, thus further straining the economy's capacity to hasten the pace of economic turnaround and development.

Table 2: Long-term Inflows of Capital: Private Sector

YEAR	US\$ m illions
1997	100
1998	144
1999	125
2000	19.6
2001	8.9
2002	5.7
2003	3.5
2004	1.5
2005	0

Source: Reserve Bank of Zimbabwe

Socio-Economic Impact

- 4.18 Zimbabwe has seen widespread reversal and cessation of donor funding in the areas of social development such as health, education, and infrastructure development.
- 4.19 The withdrawals of the above donor funding programmes has had devastating effects on social services provision such as HIV and AIDS programmes, among others.
- 4.20 Some irrigation schemes which had sustained the lives of a substantial number of rural people have been dealt a heavy blow, which has resulted in increased levels of poverty in the rural population.

Impact on Health Sector

- 4.21 Health Services Support Programmes which were suspended include the following:
- i) Supporting the provincial health service capacity building and policy issues to Ministry of Health & Child Welfare (MOHCW);
 - ii) Development of a gender strategy Support to HIV/AIDS activities;
 - iii) Integration of Zimbabwe Essential Drugs Action Program (ZEDAP) to national laboratories;
 - iv) Establishment of the health information system; and
 - v) Support to the Health Services Fund Transport Management.
- 4.22 The City of Harare Health Department used to derive benefits from the various Joint Research Projects with international stakeholders and these have since been stopped, as part of the sanctions, effectively constraining the health delivery system.

Impact on Agricultural and Rural Sector Development

- 4.23 Some programmes for the Agricultural sector aimed at enhancing forestry extension services; development of agriculture policy; marketing information system; supporting irrigation schemes to small holders; provision of training to smallholder farmers; and direct support to farming households to assist them in income generating activities were also suspended, as part of the sanctions on Zimbabwe.
- 4.24 Against this background, the Government had to reallocate its purse to forestall constriction of the rural economy.

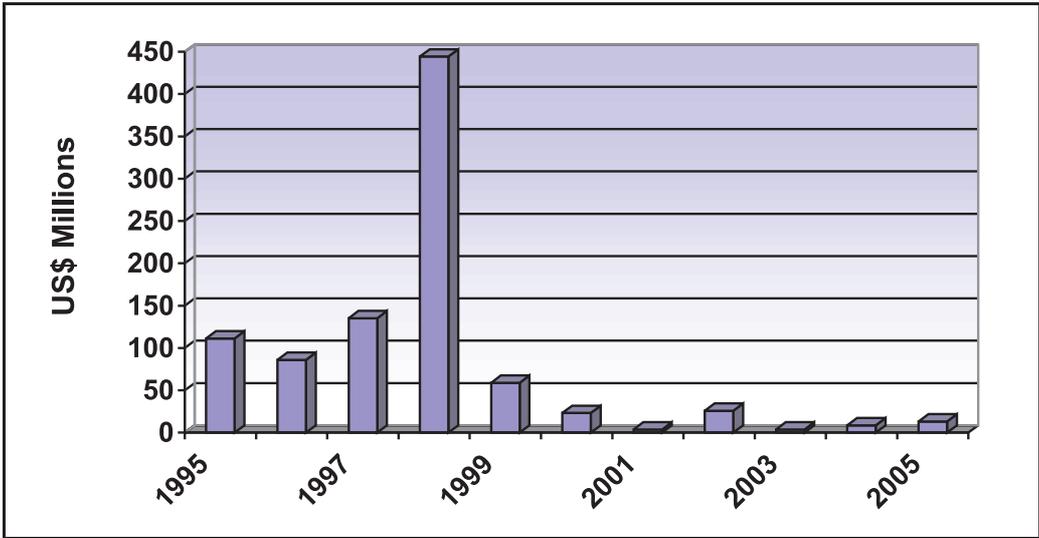
Impact on Education Sector

- 4.25 The Education Sector Support Programme which was established in January 1996, supported by donor funds was suspended after completion in 2000 and no new programmes have since been funded.
- 4.26 The project facilitated the **supply of text books, special education needs, construction of school buildings, capacity building and promotion of gender equity in education in the rural areas.**
- 4.27 All this has been put on hold following the imposition of sanctions.

Impact on Investment and Growth

- 4.28 Foreign Direct Investment (FDI) is a key driver of economic growth in any developing economy. The purpose of **FDI is to stimulate economic growth and employment creation.** FDI also **positively impacts on the country’s balance of payments position.**
- 4.29 The negative perception that has come with sanctions has negatively impacted on **foreign direct investment** coming into Zimbabwe, as investors tend to shy away from economies that are perceived as risky. In 1998, FDI inflows amounted to US\$444.3 million and by 2003 the inflows had declined to a mere US\$3.8 million.

Figure 1: Foreign Direct Investment Inflows



Source: Reserve Bank of Zimbabwe

- 4.30 The low investment levels in the export sector have exacerbated foreign exchange shortages, leading to shortages of fuel and imported raw-materials.
- 4.31 Yes, it is true that the transitory effects of the Land Reform Programme and inflationary pressures have contributed to a decline in output and hence underperformance of GDP but it is equally true that declared and undeclared sanctions have also resulted in the contraction in GDP.
- 4.32 It is time that the debate focuses on the significance of sanctions on achieving their objectives, compared to the devastating effects on the livelihood of the generality of Zimbabweans.

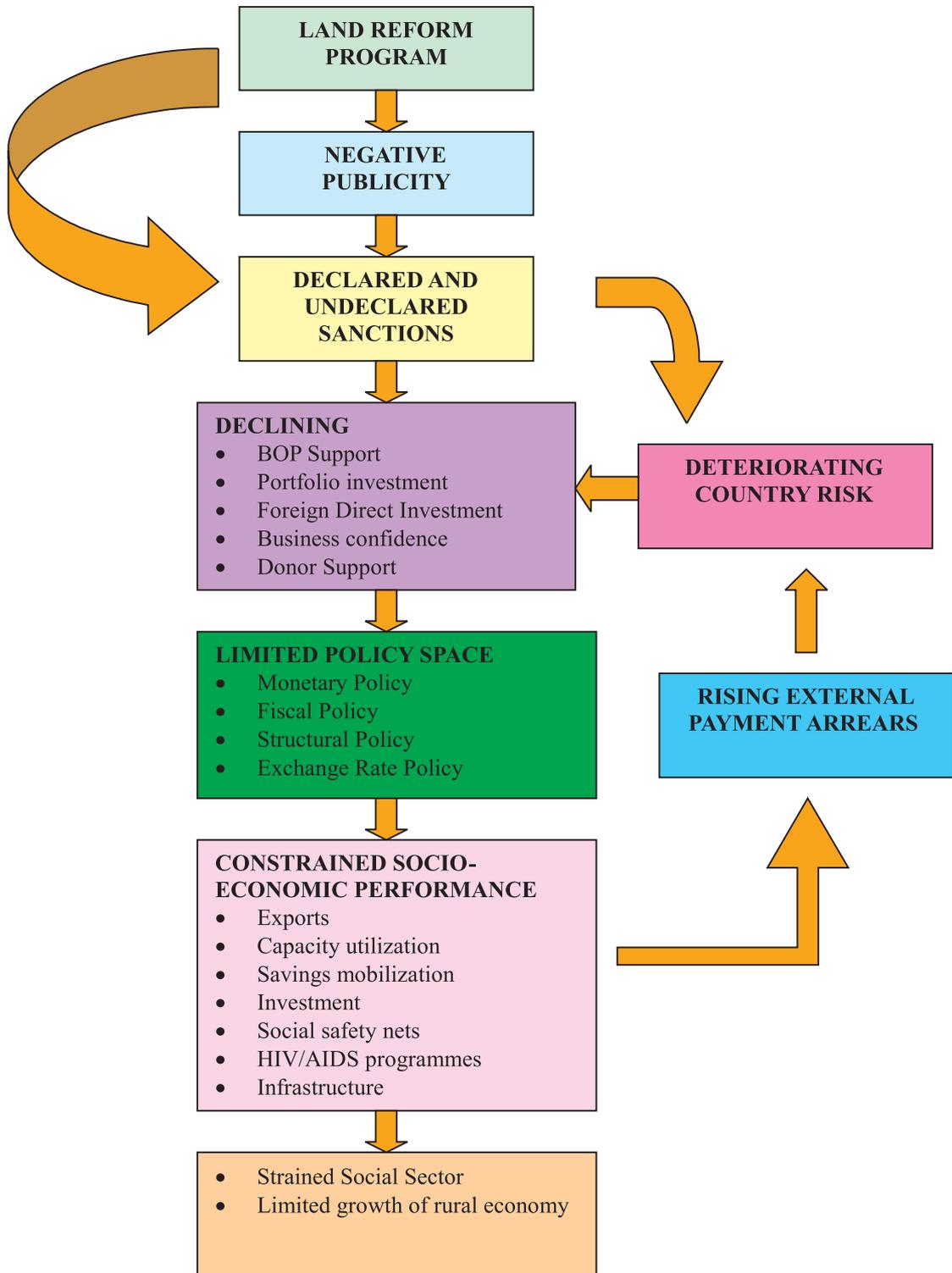
5. IMPACT OF SANCTIONS ON REGIONAL COOPERATION

- 5.1 The “smart sanctions” are also affecting the smooth running of regional groupings such as SADC and COMESA.
- 5.2 The European Union, through the European Development Fund compensates COMESA member states for revenue losses suffered under the tariff phase down exercise under specific conditions which take into account macroeconomic policies.
- 5.3 As part of the sanctions Zimbabwe has not benefited from the fund and this could affect, in the long term, its tariff reduction process in line with other countries in COMESA, thereby undermining the regional initiatives.
- 5.4 Targeted sanctions have also resulted in Zimbabwe failing to be represented at regional pact meetings such as ACP- EU meetings. This means that the country is unable to present trade policy recommendations favourable to its people.

6. CONSTRAINTS ON POLICY

- 6.1 The cumulative effects of declared and undeclared sanctions has also been to narrow the policy space for the country and Authorities have had to realign policies, such as fiscal and monetary interventions to unlock more self-reliant instruments, as part of the turnaround programme.
- 6.2 Ordinarily, in a case where a country's internal savings fall short of supporting ideal investment levels, the attendant internal gap is typically closed through Capital inflows, Foreign Direct Inflows, Portfolio investment and or international BOP support. But in the case of Zimbabwe, this was not the case since the external component has largely been **campaignned away**, leaving a very tight and limited policy space for monetary and fiscal policies.
- 6.3 The limited policy space has, thus, become a binding constraint on such policies as exchange rate management and interest rate determination, where an eclectic strategy had to be pursued, including concessional financing of the productive sectors and measured exchange rate adjustments.
- 6.4 Under conditions of a tight external sector position, aggravated by lack of international balance of payments support, the applicability of orthodox or free market based policy interventions becomes very limited.
- 6.5 A vicious circle has thus evolved since the imposition of sanctions on Zimbabwe. The resultant decline in economic activity emanating from the sanctions has given rise to rising external payment arrears, and high country risk, which in turn, has adverse effects on economic activity.

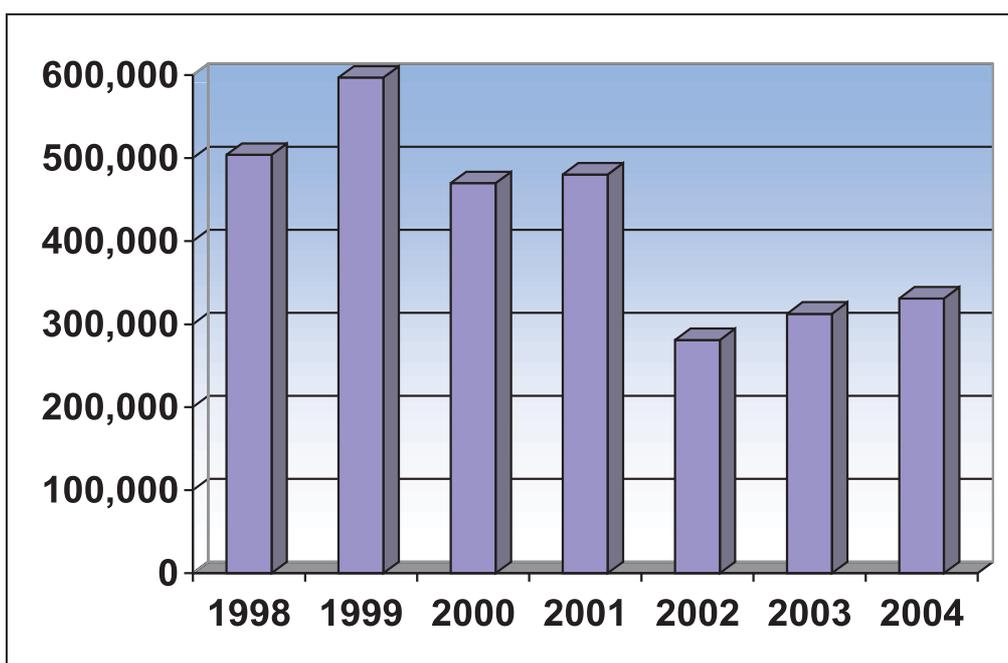
Figure 2: The Origin, Evolution and Pervasiveness of Sanctions on Zimbabwe



7. THE MEDIA AS A PENAL TOOL

- 7.1 The negative international image on Zimbabwe has largely been non-factual bad publicity.
- 7.2 The Land Reform Programme has been misunderstood by the world due to bad publicity and calculated distortions of facts on the ground.
- 7.3 The negative publicity by local, regional and international media has thus, in effect, worked to undermine and destroy business confidence and investor sentiment towards Zimbabwe.
- 7.4 Bad publicity has dealt Zimbabwe's tourism sector a painful blow.
- 7.5 Zimbabwe, as a tourist destination, has been falsely perceived to be an unsafe and risky country to visit, thus leading to a reduction in the number of tourist arrivals, thereby reducing foreign currency earnings.
- 7.6 Similarly, ordinary Zimbabwean travelers are finding it difficult to obtain visas to travel abroad due to **negative perceptions** and **xenophobia** arising indirectly from the targeted sanctions.
- 7.7 The trend on international tourist arrivals shown in Figure 3 below portrays a Zimbabwe portrayed as a war zone and yet Zimbabwe has been a peaceful country, not only in the region but compared to any other country in the world.

Figure 3: International Tourist Arrivals



- 7.8 International tourist arrivals dropped from a peak of 600 000 in 1999 to 470 000 in 2000, before declining further to 281 105 in 2002.
- 7.9 Recent turnaround measures have, however, started to reverse the adverse trend.

8. THE ADVERSE DEMONSTRATION EFFECTS

- 8.1 Deteriorating BOP support at a time when Zimbabwe's export sector was constrained inevitably pushed the country into growing external sector payment arrears.
- 8.2 Against this background the IMF, World Bank and the ADB suspended their financial support to Zimbabwe, sparking widespread demonstration effects on other financiers and the donor community at large, who took the cue and also suspended their support. This put further pressure on the country's external sector, constraining the recovery process.
- 8.3 It is for this reason that institutions such as the IMF sought to exercise the highest level of restraint through the publication of balanced country reviews, so as to avoid "talking weak economies into crises."

9 TO RETALIATE OR NOT TO RETALIATE?

- 9.1 The pervasiveness and intricacy of the sanctions under which Zimbabwe is working to stabilize its business environment have generated considerable debate on whether or not Zimbabwe should undertake retaliatory measures.
- 9.2 Others have observed that whilst some industrial countries are working to undermine economic growth and development in Zimbabwe through declared and undeclared sanctions, their transnational corporations are lining their pockets with hefty dividends arising from extractive activities in the Zimbabwean economy.
- 9.3 The argument, some have put it, is that Zimbabwe ought to consider levying some dimension of a “sanctions tax” on such entities, as a retaliatory measure.
- 9.4 As Monetary Authorities, we do not believe this is the optimal way forward, and we are pleased that our Principals are of the same progressive view.
- 9.5 Our considered view is that through constructive engagement, the international community should assume a greater mode of objectivity and appreciate the true Zimbabwean story for what it is, without inflammatory and often self engulfing emotions from gross inaccuracies.
- 9.6 Through constructive engagement, win-win frameworks can be generated, without the need to fight fire with fire.
- 9.7 Indeed two wrongs do not make a right. Time has come for the international community which is part of the Sanctions League to reconsider their position and remove these sanctions totally.
- 9.8 Whatever message the sanctions were meant to convey has been conveyed all these years and there are more serious issues for the world to deal with than continue to inflict pain and suffering on the Zimbabwean population.

10. CONCLUSION

- 10.1 Sanctions are a pervasive phenomenon with far reaching implications for the ordinary Zimbabwean, contrary to the view that these affect only the targeted individuals.
- 10.2 Thus, social sectors and the most vulnerable groups are the hardest hit, contrary to the postulate that the “smart sanctions only apply to and adversely affect the targeted few.”
- 10.3 As Zimbabweans, the lessons are very clear: there is need for unity of purpose and speeded upliftment of output in agriculture on the realization that we are our own saviours.
- 10.4 There is need for a renewed deep sense of patriotism to safeguard what is ours and also the need to progress the business operating environment in a manner that enhances confidence, in order to unlock value in the country for vast investment opportunities strewn across all sectors, including agriculture, tourism, manufacturing and mining (Zimbabwe has the largest coal bed methane deposits and the second largest platinum deposits in the world).
- 10.5 Policy consistency; respect for private property rights; investment protection; a zero tolerance to lawlessness and corruption as well as full implementation of set socio-economic programmes are also vital steps that all Zimbabweans must take to heart as a tool against the adverse wave that is increasingly putting the country under siege.
- 10.6 As a united front, victory is certain.

Thank you.

DR G. GONO
GOVERNOR
RESERVE BANK OF ZIMBABWE

24 JANUARY, 2006

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