The Economist

Zimbabwe after hyperinflation

In dollars they trust

Grubby greenbacks, dear credit, full shops and empty factories

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Small change, old and new

THE OK Mart store in Braeside, a suburb of Harare, is doing a brisk business on a sunny Saturday morning. The store, owned by OK Zimbabwe, a retail chain, is the country's largest. It stocks as wide a range of groceries and household goods as any large supermarket in America or Europe. Most are imports. For those who find the branded goods a little pricey, OK Zimbabwe offers its own-label Top Notch range of electrical goods made in China.

The industrial district farther south of the city centre looks rather less prosperous. Food manufacturers and textile firms have down-at-heel outposts here. Half a dozen oilseed silos lie empty. Only a few local manufacturers are still spry enough to get their products into OK stores. One is Delta, a brewer that also bottles Coca-Cola. Another is BAT Zimbabwe, whose cigarette brands include Newbury and Madison.

This lopsided economy is a legacy of the collapse of Zimbabwe's currency. Inflation reached an absurd 231,000,000% in the summer of 2008. Output measured in dollars had halved in barely a decade. A hundred-trillion-dollar note was made ready for circulation, but no sane tradesman would accept local banknotes. A ban on foreign-currency trading was lifted in January 2009. By then the American dollar had become Zimbabwe's main currency, a position it still holds today.

Zimbabwe's dollar had been too liberally printed: a swollen stock of local banknotes was chasing a diminished supply of goods. Now the American banknotes the economy relies on have to be begged, borrowed or earned. Even so, the monetary system works surprisingly well. A scarcity of greenbacks keeps inflation in the low single digits. The economy has made up much lost ground.

The changeover was daunting, says Kevin Terry, the boss of CABS, a Harare-based lender. Banks had to start almost from scratch. Inflation had wiped out the value of both loans and deposits. "We had no customers, no deposits, a bucketload of expenses and zero revenue," says Mr Terry.

A big question was where the dollars needed to oil Zimbabwe's banking system would come from. The central bank could scarcely ask America's Federal Reserve for a credit line. Happily, the dollars came.

Those swimming around a thriving informal economy washed into banks in search of a return: in Zimbabwe banks will pay 12% interest on three-month deposits. Dollars that had been squirrelled away in New York or London came back to Zimbabwe. Some firms could fall back on foreign credit: CABS borrowed $1.5m from its parent, Old Mutual Group, a big insurer. Then came the hot money as violence after disputed elections in 2008 receded and the economy recovered. Bank deposits increased by 31% last year, to $4.4 billion.

This is no normal banking system, however. The lengthiest term that savers are prepared to lock up their money for is 90 days, so banks can lend only for short periods. Terms are long enough for a retailer to turn over stock, but not to finance the refit of a factory. There is no lender of last resort if a bank runs short of cash or suffers a run. Lending between banks is limited. Excess cash is often parked abroad rather than lent locally. So liquidity has to be marshalled carefully. Banks keep cash worth at least 30% of their loans in reserve, further constraining how much they can lend.

The risk of a run means depositors flock to the five biggest banks: CBZ, the largest, and four foreign-owned banks. But the indigenisation policy of Robert Mugabe's Zanu-PF party, which requires foreign-owned firms to hand over at least a 51% stake, clouds even this modicum of financial stability. The immediate threat to banks has receded thanks to an unlikely alliance between Gideon Gono, the central-bank governor who is close to Mr Mugabe, and Tendai Biti of the Movement for Democratic Change, who is finance minister in an uneasy coalition government.

The indigenisation drive is nonetheless another bar to much-needed capital spending. Zimbabwean industry cannot compete with imports, in part because its machinery is old, says John Robertson, a Harare-based economist. Investment requires a long-term vision. Under hyperinflation the long term was tomorrow. Now inflation is under control but long-term credit is scarce. Last year's trade deficit was $3.6 billion. Zimbabwe has to attract yet more dollars to fill this gap. "The country is borrowing itself into the grave," frets Tony Hawkins of the University of Zimbabwe.

Consumers are in sunnier mood. People who have seen their debts eroded by inflation are all too willing to borrow even at high interest rates. Retailers are thriving. OK Zimbabwe is one of the few firms able to invest. It raised $20m of fresh capital in 2010 and used the money to open new stores and refurbish old ones. The firm coped with a month-long transport strike better than its South African peers, says Albert Katsande, its chief operating officer. Its dependence on imports forces it to hold high levels of stocks.

Sweet dreams

A problem for all retailers is a shortage of small change. One-dollar bills are filthy from frequent handling. The South African rand is the main currency in Bulawayo, Zimbabwe's second city, and one-rand coins are used in place of dimes all over the country. If coins are short, a credit note or sweets may be offered instead. Items that are frequent purchases have rounded prices. A loaf of bread usually sells for $1.

Given their own experience with money-printing, locals are queasy about "quantitative easing" as practised by the Fed and other rich-world central banks. Yet for all the printing of electronic dollars by the Fed, the greenback is a hard currency in Zimbabwe. Few are clamouring for its replacement by a local brand.

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