NATIONAL COMPETITIVENESS COMMISSION

Enhancing Zimbabwe's Global Competitiveness

ANALYSIS OF THE IMPACT OF THE TARGETED FINANCE FACILITY ON BUSINESS COMPETITIVENESS

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1.0 Introduction

1.1 The Reserve Bank of Zimbabwe (RBZ) has realised that banks do not have enough capacity to meet the requirements of the productive sectors in Zimbabwe. Accordingly, the Bank has set up a facility called the Targeted Finance Facility (TFF) to increase funding for the productive sectors of the economy.

1.2 The facility has been objectively set up to finance working capital requirements of the borrowers to increase and improve productivity.

2.0 The TFF Operational Modalities and loan Characteristics

2.1 The facility will be availed through the normal banking channels. The Reserve Bank will lend collateralised loans to the banks, which will, in turn, lend to their customers which is the productive sectors in this case.

2.2 The banks will perform the credit risk of the beneficiaries implying that banks will be fully responsible for credit assessment and customer due diligence.

2.3 The lending banks are fully accountable for the way funds are utilized by the borrowers (fully responsible for ensuring that the funds are applied for the purpose for which they were borrowed) and are therefore expected to monitor the performance of the borrower throughout the loan tenure.

2.4 Funds are only disbursed to the lending banks upon the submission of a drawdown list indicating the names and loan amounts of the ultimate beneficiaries. This implies that funds will not be readily available for lending.

2.5 All the loans disbursed under this facility will be in ZiG and borrowers can repay in ZiG or in foreign currency at the ruling exchange rate.

2.6 The maximum tenure for the loans under this facility shall be 270 days running from the disbursement date.

2.7 The banks will borrow from the central bank at an interest rate of 20% per annum and on-lend at a maximum all-in interest rate of 30% per annum. The interest rate is subject to review by the Monetary Policy Committee (MPC).

2.8 If funds are found to have been abused by the borrower, the full loan amount becomes immediately due and payable. The loan will attract a penalty interest rate equivalent to the prevailing overnight accommodation rate for the duration that the loan was outstanding. The penalty will be levied on the borrower through the lending bank.

3.0 Likely Impact on Business Competitiveness.

3.1 Working capital plays a very crucial role in a firm's day-to-day operations. Precisely, it represents short-term financial resources available to meet a company's current obligations and operational needs. It therefore facilitates smooth operations, ensures liquidity in a firm, supports firm growth, improves financial stability, enhances supplier relationships and provides flexibility to business.

3.2 Lack of working capital in a firm has got huge negative implications on a firm's productivity and competitiveness. It may lead to disruptions of operations, bottlenecks in supply chain, employee retention and low morale and inability to maintain equipment which all negatively affect productivity.

3.3 Lack of adequate working capital may also lead to a reduction in market responsiveness as firms cannot respond to market opportunities such as increasing production to meet sudden demand or launching new products thereby reducing its competitiveness.

3.4 It can also lead to loss of customer trust and higher costs. Often, firms without working capital delays in fulfilling orders due to operational challenges which damages the firm's reputation leading to loss of market share. Firms with inadequate working capital usually resort to high-cost short-term borrowing to cover-financial gaps. This increases financial costs and reduces price flexibility leading to high product prices and low competitiveness.

3.5 Lack of adequate working capital limits a firm's investment in growth and its ability to offer competitive terms. Firms in working capital predicament cannot offer competitive credit terms compared to competitors. This limits their competitiveness. They also cannot invest in marketing, research, development and innovation which are all critical elements of competitiveness.

3.6 Persistent working capital shortages can erode a firm's competitive advantage, weaken its bargaining power and ultimately push a firm into insolvency.

3.7 The realization by the RBZ that commercial banks are lacking capacity to adequately finance productive sectors and the idea of coming up with a financing facility to boost banks' capacity to meet the requirements of the productive sectors in Zimbabwe is well appreciated.

3.8 The concept has got the potential to improve productivity and competitiveness of the productive sectors in Zimbabwe. However, the facility presents some potential design and operational challenges that are likely to hinder its effectiveness in archiving the desired objectives.

4.0 Shortfalls of the Concept

4.1 **Market relevance**

4.2 The loans under this facility are denominated in ZiG only even though the economy is almost fully dollarized. There is therefore a low probability that these loans will be relevant in a dollarized[1] economy.

4.3 If the market responds positively to this facility, it is likely that the funds will find their way to the black market for USD resulting in the destabilization of the exchange.

4.4 **Loan maturity**

4.5 A loan maturity period of 270 days which is far less than a year may result in large repayments over a short period which could deplete working capital, potentially leading to liquidity issues.

4.6 **Penal provisions**

4.7 Considering the short loan maturity period, a penalty interest rate equivalent to the prevailing overnight accommodation rate for the period the loan is in arrears for overdue loans may act as a deterrent factor for borrowers. The maturity period is short and inconsistent with business turnaround times. Accordingly, there are high chances that businesses may be reluctant to lock itself in this tight debt.

5.0 Recommendations

5.1 The RBZ is recommended to:

- Consider expanding the facility to include USD loans.
- Consider expanding the loan repayment period to more than 2 years basically for 2 important reasons:
    i. This is a business and not personal short-term loan
    ii. This is working-capital loan

[1] Note that are other provinces and towns that do not accept Zig for trade transactions except in huge supermarkets (Beitbridge and Chiredzi for instance).