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Do Development Financing Institutions Spur Economic Growth in Zimbabwe?

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Abstract
The economy of Zimbabwe has primarily been declining since 1998. This is true despite the fact that the government of Zimbabwe established development financing institutions (DFIs) with the intention of enabling the major sectors to significantly contribute to the country's economic growth. Therefore, the study sought an empirical response to the question, "Do DFIs in Zimbabwe spur economic growth?" To test this link, Granger-causality criteria and Ordinary Least Squares estimation were used covering the period 1990-2020. Contrary to expectations, the analysis found that total development funding from the state owned DFIs had a negative impact on economic growth, while direct foreign remittances, official development assistance, trade openness, bilateral and multilateral funding all had a positive impact on growth. The Granger causality test results disproved the existence of a causal link between DFIs and economic growth in Zimbabwe. The study suggests, among other things, the necessity to increase DFI funding by cultivating an atmosphere economically favourable that enables both domestic and external DFIs to function at full potential.

Keywords: *Causality, DFIs, Economic growth, OLS, Zimbabwe.*

1. Introduction

Since World War II, the emergence of development finance institutions (DFIs) on a national and international level has attracted attention to the development of the global economy. In the last few decades, these development banks, which were founded with the goal of providing capital for investments, have expanded quickly in developing nations (International Finance Corporation, 2018). Maynard (1992) asserts that the private sector invented every sort of financial institution that exists today. Therefore, the creation of the Credit Mobilier by the Pereire brothers in 1852 might be considered the beginning of the history of DFIs from a historical and global perspective (Kitchen, 1986). Credit Mobilier was a French bank that provided funding for numerous infrastructure projects. Although this financial institution eventually rose to prominence as a major financier, between 1864 and 1867 it was pushed to fail by a scandal (Maynard, 1992). Later, numerous development banks imitated this in the 1970s and 1980s. These development banks all disappeared from their development order of business as a result of this massive disaster (Thorne and du Toit, 2009). In spite of the significant failures, many world governments continued to carry out the tasks of their national development banks (Kakwani and Son, 2006).

The situation was different for many developing economies, though, as they continued to have trouble finding long-term financing (Bruck, 2005). Despite these difficulties, a lot of governments today are still engaged in the business of establishing and assisting DFIs. This is due to the fact

that these DFIs are seen as essential participants in funding significant capital investment projects, which ultimately aid in long-term economic growth. While it is undeniable that these DFIs have the ability to raise a nation's overall welfare and income, for instance by creating jobs, this is still up for debate in Zimbabwe's data analysis (see Lemma, 2019). Despite the existence of four specialised DFIs, as well as bilateral and multilateral organisations providing development finance, Zimbabwe has continued to face an economic slowdown during the period under investigation (Government of Zimbabwe/GoZ, 2020). As a result, empirical research is required to evaluate if DFIs in Zimbabwe promote economic growth.

2. DFIs and the economy of Zimbabwe: An exploration

The GoZ prioritised growth and equality in 1980 and worked to develop all economic sectors from a well-coordinated policy standpoint. The creation of DFIs was considered one of the solutions for achieving this long-term policy objective. In order to enable and support the productive sectors that were recognized as the country's economic pillars—infrastructure, industrial development, small companies, and agribusiness—the government established four DFIs. Since then, this objective has been supported by both internal and external financial resources, as shown by numerous national budget statements. The four pillars were designed to expand and revitalise road infrastructure, dam construction, irrigation and other agricultural-related rehabilitation programs, as well as venture capital, particularly for small and medium-sized businesses. Table 1 includes information about the four DFIs in Zimbabwe, including their histories and goals.

Table 1. DFIs in Zimbabwe – Mandates and History

Institution	Mandate
Agriculture Finance Corporation (AFC)	This development bank's primary responsibility is to provide financing for sustainable agricultural development. It was founded in 1999 and registered under Zimbabwe's Banking Act Chapter 24:20 under the previous name of AgriBank.
Infrastructure Development Bank of Zimbabwe (IDBZ)	As the anchor to further stimulate and support economic development, this DFI's mandate is to provide long- and medium-term finance for important infrastructure projects. It started operations in June 1984 under the name Zimbabwe Development Bank (ZDB). On August 31, 2005, IDBZ was formally established as ZDB's replacement. It is currently governed by Act of Parliament Chapter 24:14.
Industrial Development Corporation of Zimbabwe (IDCZ)	Its mission is to support economic growth by fostering creative, sustainable, and inclusive industrial development. The IDC Act Chapter 14:10 of 1963 was used to incorporate IDCZ.
Small Enterprises Development Corporation (SEDCO)	Its mission is to support economic growth by fostering the growth of micro, small, and medium-sized businesses. Small and Medium Enterprise Development Corporation (SMEDCO), a prominent DFI, was created in 1983 in accordance with Act of Parliament Chapter 24:12.

Source: derived from AFC, IDBZ, IDCZ and SMEDCO websites and Acts of Parliament

Over the time period, external financial and technical support from the nation's developing partners was used to supplement these internal development efforts. The nation received official development assistance (ODA) from external development banks and partners prior to the founding of these four DFIs. These include multilateral organisations such as the World Bank (WB) and International Monetary Fund institutions, at the global level, and African Development Bank (AfDB), at the regional level (GoZ, 2018).

Other financial institutions, in addition to the AfDB and WB, such as China Exim Bank, Development Bank of Southern Africa, Kuwait Fund, and Abu Dhabi Fund, among others, made very sizable foreign currency contributions for a range of development projects, as detailed in numerous government reports. Ten targeted water bodies are included in the development projects, one of which being Tokwe Mukosi Dam in Chivi Rural District in Masvingo Province (GoZ, 2020).

With multilateral institutions typically having a bigger funding capability than the bilateral development banks, external development partners continue to play a crucial role in financing development capital projects today (Massa, 2011). The development funds from bilateral and multilateral DFIs, as well as the related economic growth, are summarised in Table 2 for the years 2011 through 2020.

Table 2. DFI Funding and Economic Growth in Zimbabwe (2011-2020)

Year	Bilateral US$m	Multilateral US$m	TDF US$m	Annual GDP growth %	TDF (%GDP)
2011	343.8	26.9	371	14.194	2.53
2012	438.6	212.5	651.1	16.665	3.80
2013	144.6	114.5	259.1	1.989	1.48
2014	358.1	175.6	533.7	2.377	2.99
2015	287	140	427	1.78	2.35
2016	217.9	134.6	352.5	0.756	1.92
2017	364.4	126.5	491	4.709	2.56
2018	372.5	148.9	526.7	4.824	2.62
2019	449.1	161.3	610.4	-6.144	3.23
2020	448.4	131.4	579.8	-6.249	3.28

Source: Authors' compilation from National Budget Statements and World Bank publications. Note: TDF is Total Development Funding (Cumulative amounts of investments for development purposes)

Table 2 indicates that large sums of development financing were availed during the period under study. From the table, it is clear that the DFI disbursements varied from one year period to the other. As noted, TDF for the external development partners in 2012 increased sharply from the previous year. In fact, it is the year that the country received the highest funding of US$651.1 million over the entire study period. This is a result of tremendous efforts done by the inclusive government to re-engage the international community including multilateral banks for more development funding (GoZ, 2012, 2011).

According to Table 2, bilateral development partners provided more development funding than their counterparts. The nation's debt overhang trap offers the greatest explanation for this. The

country had an estimated US$8.2 billion in total external debt as of 30 September 2020. (GoZ, 2021). Since it has been unable to pay its massive public debt stock and arrears for years, Zimbabwe's relationships with major international organisations, including the International Monetary Fund (IMF) and World Bank, have deteriorated, making it more difficult for it to obtain more funding (Saungweme and Odhiambo, 2018).

3. A survey of literature

The theoretical framework of DFIs and how they fit in the finance-growth nexus can generally be explained by two theories, that is the finance led growth theory and the growth led finance theory. The finance led growth theory, also known as the “supply-leading view” was first established by Schumpeter (1912), Patrick (1966) and Goldsmith (1969). It is thought that financial development has a positive impact on economic growth (Levine, 1997). By allocating financial resources to productive areas of an economy, enabling conditions that promote economic growth are produced (Rehman and Hysa, 2021). The presence of a financial sector, especially one with efficient financial intermediation like development banks, channels the limited resources from underperforming to overperforming economic sectors (Patrick, 1966).

The "demand-following approach," also known as the "growth led finance theory," postulates that as the economy's real side expands, the need for certain financial instruments in the financial market rises, creating a high demand that subsequently fuels growth in the financial services (Robinson, 1952). New financial markets and institutions, such as DFIs, are introduced in order to satisfy the high demand for financial services and goods (Levine, 1997). This implies that the demand-following approach views the expansion of the financial sector as essentially passive and as something that happens more or less spontaneously as a result of the growth process. Financial institutions and markets develop, widen, and improve in efficiency as the real economy grows (Patrick, 1966).

Studies that empirically examined the relationship between DFIs and economic growth, particularly in African countries, are still limited despite the fact that it is widely understood that development finance is essential and can fuel a country's economic growth. Zikhali (2021) looked into how DFIs affected South Africa's economic performance. The results of this analysis, which covered the years 1995 to 2018, using the Autoregressive Distributed Lag (ARDL) approach, showed that there is a long-term relationship between DFIs extensions and South Africa's economic growth.

The effect of DFIs on economic growth in Uzbekistan was examined by Jumaniyozov (2018). Using comparison analysis, annual data was chosen for the period 2005-2017. The results showed that foreign direct investment was the most effective source of economic growth assistance in the analysed country, followed by total development funding and multilateral development funding.

Islam (2015) conducted a study utilising cointegration analysis to examine how DFIs affected the Malaysian economy. Utilising total assets and financing operations from 1980 to 2012, their growth and contributions were examined. The research discovered a favourable and statistically significant long-term link between both factors and per capita real income. This implies that the role of DFIs in determining Malaysia's per capita income is significant.

Furthermore, Massa (2011) looked at the relationship between DFI investments and economic growth in a number of countries from 1986 to 2009, both high- and low-income. Using the Generalised Technique of Moments (GMM) method, the study revealed that a 10% investment by multilateral DFIs in research countries results in an increase in income of roughly 1.5%.

Te Velde (2011) studied the function of DFIs in addressing global concerns using a sample of 26 richer and poorer countries. According to the research, an increase in DFI by 1% would affect investment by 0.8%. The claim was that the decline in commercial banks' investments during and after the financial crisis of 2008–2009 was offset by DFI investments in developing countries. In turn, this supported the continuation of the economic recovery in crisis-affected countries.

Namusonge (2004) examined the role of development financial institutions in the acquisition of technological capabilities in small and medium enterprises in Kenya. The results indicated that technological capabilities hold the key to competitive advantage of enterprises globally. Santiso (2001) focused further on the roles performed by international DFIs, including the World Bank. He discovered that in order to affect change, there is a growing desire for improving the role performed by foreign DFIs in developing good governance. Multilateral DFIs effectively expand and refocus their development funds to achieve this.

Numerous studies on the direction of causality between financial development and economic growth, which is yet another crucial area, have been conducted worldwide and have yielded various points of view. An empirical study on the dynamic causal relationship between financial development and economic growth in Zimbabwe by Munyanyi (2017) showed that bank deposits support the demand-following hypothesis.

In Ethiopia, Sime (2016) applied the Johansen and Vector Error Correction (VEC) approach from 1973 to 2008. The Johansen test proved that there is long-term con-integration among the variables, however the VEC model showed that there is long-term bi-directional causation between private credit and real GDP growth rate. At the same time, a one-way causal relationship between the ratio of Deposit Money Bank assets to GDP and the real GDP growth rate was also established. There was no short-term causality between financial development and economic growth indices.

Abrahams (2016) conducted a comparable analysis from 1980/81 to 2014/15 using the Ganger-causation test for Ethiopia and discovered that there is bidirectional causality between the two variables. Similarly, Hyera and Mutasa (2016) also did an additional empirical investigation in Tanzania from 1980 to 2012. After applying the Johansen cointegration test, Granger causality, Vector Error Correction Model (VECM), and variance decomposition inside the VAR framework, the direction of causality between the two variables revealed mixed conclusions.

4. Methodology and data

In this study, the ordinary least squares method is used to estimate the impact model, while the Granger causality approach is applied to study the casual link between the variables. The research uses secondary data spanning from 1990-2020. The following sources provided the data for the model variables:

Table 3. Data and Variable Descriptions

Data source	Variables
World Bank online database	real GDP growth, direct remittances, external debt, foreign direct investments, official development assistance and trade openness
Government of Zimbabwe	Bilateral and multilateral development funding
Local state DFIs	Total development funding

The applied empirical model was developed after a careful analysis of literature on DFIs and economic growth. The following is the impact model representation:

$$\ln GDP = \beta_0 + \beta_1 \ln TDF + \beta_2 \ln BMF + \beta_3 \ln DR + \beta_4 \ln ED + \beta_5 \ln FDI + \beta_6 \ln ODA + \beta_7 \ln TO + \varepsilon \quad (1)$$

Where:
GDP = real gdp growth (proxy for economic growth)
TDF = total development funding
BMF = bilateral and multilateral funding
DR = direct remittances
ED = external debt
FDI = foreign direct investments
ODA = official development assistance
TO = trade openness
ε = error term
β_0 = constant
$\beta_1 - \beta_7$ = coefficients
$\beta_0, \beta_1, \beta_2, \beta_3, \beta_4, \beta_5, \beta_6$ and β_7 are the regression coefficients
Ln = the natural logarithm
The data is logged in natural logarithms to reduce variances between data sets and to interpret the coefficients as elasticities. To formally establish the causal relationship between internal DFIs and economic growth as well as the causal relationship between external DFIs and economic growth, the study outlined two causality models. The following are the causality model representations:

Internal DFIs (TDF) model

$$\ln GDP = \alpha_0 + \alpha_1 TDF + \varepsilon_t \quad (2)$$

$$\ln TDF = \alpha_0 + \alpha_1 GDP + \varepsilon_t \quad (3)$$

External DFIs (BMF) model

$$\ln GDP = \beta_0 + \beta_1 BMF + \varepsilon_t \quad (4)$$

$$\ln BMF = \beta_0 + \beta_1 GDP + \varepsilon_t \quad (5)$$

5. Data Analysis and Discussion

Table 4. Descriptive Statistics Results

	LNGDP	LNTDF	LNBMF	LNDR	LNED	LNFDI	LNODA	LNTO
Mean	0.716	0.192	0.070	0.038	44.607	1.160	38.555	31.295
Median	1.440	0.000	0.000	0.000	48.220	0.850	38.960	33.550
Maximum	19.680	1.420	3.800	0.150	71.990	3.570	76.370	43.400
Minimum	-17.670	0.000	0.000	0.000	20.060	0.020	0.000	19.160
Std. Dev.	9.220	3.385	1.401	0.045	16.075	0.984	20.700	7.458

Table 5. Unit Root Test Results

Variable	ADF Statistics	Level of Significance			Order of integration
		1%	5%	10%	
LNGDP	-5.591	-3.753	-2.999	-2.638	I(1)
LNTDF	-4.585	-3.769	-3.005	-2.642	I(1)
LNBMF	-6.076	-3.753	-2.998	-2.638	I(1)
LNDR	-7.110	-3.753	-2.998	-2.638	I(1)
LNED	-5.248	-3.809	-3.021	-2.650	I(2)
LNFDI	-4.824	-3.770	-3.005	-2.642	I(1)
LNODA	-3.833	-3.753	-2.998	-2.639	I(1)
LNTO	-5.872	-3.753	-2.998	-2.639	I(1)

Source: Eviews 12 software package

Table 5 indicates that LNGDP, LNTDF, LNBMF, LNDR, LNFDI, LNODA and LNTO are integrated of order one, I(1), while LNED is integrated of order two, I(2). The model variables therefore have a heterogeneous order of integration.

Table 6. OLS Regression Results

Dependent variable: GDP

Variable	Coefficient	Std. Error	t-statistic	Probability
C	-21.71781**	9.632798	-2.254569	0.0376
LNTDF	-2.54173*	0.615652	-4.128515	0.0007
LNBMF	0.812019	1.337311	0.607203	0.5517
LNDR	3.54444*	0.621280	5.704987	0.0000
LNED	-0.634699*	0.134348	-4.724293	0.0002
LNFDI	-2.722245	1.989869	-1.368052	0.1891
LNODA	0.412929*	0.090313	4.572214	0.0003
LNTO	0.823828*	0.249485	3.302121	0.0042
R-squared = 0.78341 DW = 1.896806 the F-statistic = 8.78 (0.000)				

Source: Eviews 12 software package

*Notes: *and ** imply significance at 1% and 5%, respectively.*

The findings indicate that local DFIs and economic growth have a statistically significant inverse relationship. Specifically, a 1% increase in the overall amount of development funds provided by state DFIs results in a 2.54 % decline in economic growth. Several factors, including various currency and parastatal reforms, may combine negatively to have this effect (IDBZ, 2020). The findings also indicate that external DFIs and economic growth are positively correlated. The study backs up the empirical research of Massa (2011), who concluded that multilateral DFIs have a positive and significant impact on economic growth, particularly in low-income countries, such as Zimbabwe. More specifically, an increase of 1% in development assistance from bilateral and multilateral partners results in an increase of 0.81 % in economic growth. The positive impact can be best explained by the fact that external DFIs offer funding for development purposes in foreign currencies like the USD, which has a higher value than the local ZWL and, as a result, contributes significantly in terms of monetary value as far as investments for development purposes are concerned.

The findings indicate that direct remittances have a positive impact on economic growth. The findings concur with empirical research conducted in the majority of African countries, such as studies by Chivundu et al. (2015) for Malawi and Bett (2011) for Kenya. Additionally, the findings show that external debt and economic growth are negatively correlated. According to the debt overhang theory, when external debt reaches a particular threshold, there is a negative relationship between it and economic growth. The outcome is consistent with this idea. Zimbabwe has a significant amount of debt that must be repaid to international lenders like the Paris Club, which is difficult due to a debt overhang (Saungweme and Odhiambo, 2018).

The direction of growth has been hampered by this debt burden. The findings are supported by a recent empirical study by Manasseh et al. (2022), which discovered that external debt has a detrimental effect on economic growth in thirty particular Sub-Saharan African (SSA) countries. Additionally, the findings indicate that trade openness and official development assistance have a positive impact on economic growth. The findings are consistent with earlier empirical research by Yiew and Lau (2018). Finally, the analysis discovered no relationship between FDI and economic growth.

Table 7. Granger Causality Test Results

Variable	F-Statistic	Prob
LNTDF does not cause LNGDP	0.27948	0.7594
LNGDP does not cause LNTDF	0.52471	0.6005
LNBMF does not cause LNGDP	0.09219	0.9124
LNGDP does not cause LNBMF	2.79686	0.0876

Source: Eviews 12 software package

Table 7 shows that the probabilities are above 0.05% level of significance implying that DFIs, both state-owned and external represented by LNTDF and LNBMF, respectively, do not cause economic growth in Zimbabwe. The results, however, show that there is a unidirectional causality flowing from GDP to BMF.

6. Conclusion

The major objective of this study was to examine the impact and casual relationship between DFIs and economic growth in Zimbabwe using the time series data for the period 1990 to 2020. The study employed the Ordinary Least Square technique and the Granger causality test. The main conclusions of this study are that while external DFIs have a positive impact on economic growth in the studied country, state-owned DFIs have a negative impact on economic growth in Zimbabwe. The results also indicated that there is no causal relationship between DFIs and economic growth, regardless of the type of DFI – internal or external. Basing on the findings of the study, state owned DFIs in Zimbabwe failed to spur economic growth from 2011-2020. The study also discovered that foreign direct investments and external debt both negatively impact Zimbabwe's economic growth. This demonstrates the validity of the debt overhang argument, which contends that Zimbabwe's economic growth is slowed in part by debt accumulation. Direct remittances, ODA, trade openness, and bilateral and multilateral DFIs, on the other hand, have a significant positive association with economic growth. The study suggests that the GoZ take steps to stabilise its currency or, failing that, switch to using US dollars. This aids in reducing financial risks, particularly exchange rate risk, which led to the devaluation of local currencies and the consequent significant losses suffered by state DFIs. The political environment must be favourable in order to draw external DFIs and private investors and allow them to function at full capacity. By doing this, very large amounts of development finance can enter the market, causing deep investments that, in accordance with Rodan's "Big Push theory," spur economic growth. The GoZ must reduce borrowing in the case of external debt and use the money borrowed to pay for capital expenditures. Finally, in order to avoid accumulating large amounts of debt that are harmful to the growth of the economy, this can be accomplished by adhering to borrowing restrictions and standards.

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