Here We Go Again: Zimbabwe Printing New Currency Amid Stress

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Is Zimbabwe printing a new currency akin to buying homeowner's insurance as the house fire is raging?

The country best known in financial circles for hyperinflation is Zimbabwe. In February 2007 inflation, driven by a near worthless fiat currency, exceeded 50% per month, or 12,875% per year, Cato Institute Senior Fellow Steven Hanke noted. The country famously once erased 12 zeros from its beleaguered currency during this period, when the denomination was the $100 trillion dollar bill, and is considered the poster child for monetary debasement. Fast forward to 2016 and will history repeat itself? With a trade deficit ballooning and the country gasping for a tradeable currency, Zimbabwe has decided to print its own version of the U.S. dollar.

Zimbabwe printing new currency after historic hyperinflation

With the claim of $200 million in support from the Africa Export-Import Bank, the nation's central bank governor appears to have gone full speed ahead with Zimbabwe printing new bond notes slated to have the same value as their U.S. dollar equivalents. What a central banker claims the value peg for a currency to be is not always the correlation assigned to it by free markets, particularly when knowledgeable financial professionals start to ask meaningful questions and model economic sustainability.

John Mangudya, Zimbabwe's central bank governor, stressed this was not a return the near worthless Zimbabwean dollar, which ceased in circulation in 2009 and the country chose between major currencies in which to transact business. With the U.S. dollar, South African rand and Chinese yuan the primary currencies used in the economy, local product price volatility was dramatically reduced as a result of a stable currency.

"This does not signal the reintroduction of the Zimbabwe currency," Mangudya was quoted as saying. "The fundamentals are not yet right for its comeback. This is just a measure to curb illicit flows out of the country."

Zimbabwe is faced with increasing economic woes and is starving for foreign currency reserves that can be used in trade. Primarily to blame for the cash shortage is a nearly a three to one trade deficit. The country was reported to have imported $490m in the first quarter against $167m in exports.

To address the problem, the country has placed restrictions on how much cash can be withdrawn from the country and the central bank had been encouraging residents to use the South African rand notes as the local currency. But locals were reported to generally prefer the U.S. dollar based on its value stability, particularly as South Africa's budget deficit continues to grow without even a sign of commitment to control spending.

Zimbabwe printing a new currency is not in itself a solution

Zimbabwe printing new bond notes (which are actually done outside the country) is not likely going to be enough to make this the defacto unit of financial measure in the country, nor has the central bank stated this as a goal. It is unclear how the bond notes will be treated locally as residents to buy groceries, pay local fees and transact business. But perhaps more importantly is how the new currency will be treated by trading partners who may be wary of Zimbabwe and its past performance towards debasing their currency to near the value of the paper it is printed on.

"Unless the country takes bold reforms, the economic difficulties will continue in [the] medium term," the International Monetary Fund said in a report Wednesday. "Given the outlook for the global economy, growth is projected to remain below levels needed to ensure sustainable development and poverty reduction."

For its part the IMF noted Zimbabwe's economic difficulties are stemming from increasingly erratic weather patterns where rising temperatures and drought have left the nation scrambling. That's more of an emotional appeal for assistance, but what really matters to trading partners is their ability to support the currency.

"Zimbabwe remains in debt distress and the level of international reserves is low. Despite the adverse environment, the authorities have reduced the fiscal deficit in both 2014 and 2015," the IMF said in a May 4 report. The numbers that speak to fiscal sustainability are what trading partners might examine first, if they consider accepting the new currency at all.

Of course besides massive hyperinflation nothing can go wrong until Zimbabwe cannot afford enough paper to print money, if that founds wild just ask Venezuela