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QUARTERLY ECONOMIC BRIEF

Q1 2019

Highlights

- IMF projects global economic growth of 3.3% in 2019, down from 3.6% last year.
- U.S - China trade negotiations still ongoing, new threat from U.S - E.U tensions.
- World Bank predicts 4th consecutive year of SSA population growth exceeding GDP growth.
- Persistent socio-political fragilities threaten Zimbabwe's re-engagement prospects.
- Monetary authorities partially liberalized quasi local currencies.
- Inflation closed March 2019 at a new post-hyperinflation peak of 66.8%.
- ZSE market capitalization shed ZWL3.299 bn (16.89%) to ZWL16.235 bn in Q1 2019.

Global economic growth has decelerated...

The International Monetary Fund (IMF) warned that global economic growth has progressively decelerated from the 2nd half of 2018 into 2019 - citing a confluence of factors that weighed down on major economies. Consequently, global growth is projected to close 2019 around 3.3%, down from 3.6% last year. Chinese growth slowed due to policy tightening and trade tensions with the US. Euro Area was weighed down by weak business confidence, partly attributable to Brexit uncertainties. Going forward, risks remain tilted to the downside - centered on a further escalation of trade tensions, adverse financial market sentiment and generally tighter financial conditions.

Policy recommendations from the IMF (in light of deteriorating global growth momentum and limited policy space to combat downturns) include facilitating a soft landing in cases where policy support is to be withdrawn, while ensuring that supportive fiscal policy can maintain sustainable public debt. The IMF also prescribed that monetary policy must ensure inflation remains within targets and that inflation expectations are anchored. Further, the IMF warned that across all countries; policies must aim to increase productivity, improve inclusiveness and strengthen resilience.

Global trade tensions sustained

The United States (US) is reportedly 'considering' imposing tariffs on US$11 billion worth of goods such as aircraft, wine and cheese from the European Union (EU) – in response to EU subsidies supporting Airbus. This followed the World Trade Organization's (WTO's) assertion that EU subsidies are adversely impacting the US. The proposed US measure would translate to an escalation in trade tensions between the US and major global economies.

In 2018, the US imposed tariffs on steel and aluminum imports, ostensibly targeting China but also impacting the EU. US President Donald Trump has complained about China's trade policy since before he assumed office. US trade tensions with China have escalated since the US imposed tariffs of billions of dollars' worth of Chinese goods, attracting Chinese retaliation in kind. Negotiations to quell the tensions are still progressing, albeit at a painstakingly slowly pace.

Trouble brewing in sub-Saharan Africa

The World Bank revised sub-Saharan Africa's 2019 GDP growth forecast from 3.3% to 2.8%. The World Bank partly cited a commodity price slump in 2015 that it ended a decade of rapid regional growth. It further warned that recovery from the slump is compromised by depressed industrial production and recent trade disputes in major advanced economies. The latest growth forecast suggests regional economic expansion is expected to lag population growth for a fourth year running. Such conditions are ripe for socio-political vulnerability; further perpetuating regional macro-economic fragility.

Efficiency vs compliance… Boeing case

Only two years ago, Boeing was on one of the strongest companies, supported by a bullish earnings outlook. This was just before it was due to start delivering its new 737 Max aircraft. At the time; the company's management was accused of 'boasting' about how quickly Boeing had put the 737 Max to market - reportedly praising the Federal Aviation Administration's streamlined certification process under a new pro-business United States administration. By end of 2018, the company's revenue exceeded US$100 bn and profit closed at US$10.5 bn.

Fast-forward to the quarter under review and Boeing was facing possibly the biggest hazard in its 103 year old history; threatening earnings and its reputation. In October 2018, a 737 Max flown by Lion Air crushed and killed all 189 people on board. On 10 March 2019, an Ethiopian Airlines 737 Max crushed, also killing all 157 on board. The latest crush led to 737 Max planes being grounded amid concerns of a potential design flaw; putting the spotlight on 'streamlined compliance' and underlining the importance of 'responsible business' practice.

Financial sector integrity at risk

Two former Barclays traders were jailed for four and five years respectively, after being convicted of conspiring to 'rig the Euribor interest rate'. The Euribor interest rate is a reference rate used to determine interest rates of Euro denominated loans. The actions of the men are deemed to have deliberately undermined the integrity of the financial system, to either profit personally or advance the interest of their employer.

The traders' defense was that 'tweaking' interest rates up or down was common industry practice, though the court ruled the practice as corrupt – as the banks would have investments that benefitted from higher or lower interest rates. In 2015, a former UBS trader was sentenced to eleven and a half years over similar allegations. The litigation measures have affected traders from most major banking houses, broadly threatening the integrity of the industry.

US$ on the front foot

The United States Dollar (US$) closed the quarter under review stronger against most trading currencies. Dollar strength was supported by rising U.S Treasury yields associated with relatively tighter monetary policy attracting fund flows into the United States. The US$ closed the quarter to 31 March 2019 at US$1.12 per Euro, 1.5% firmer. It was also 1.8% firmer against the ZAR at ZAR14.63 per US$.

Euro depreciation was exacerbated by expectations of European Central Bank (ECB) monetary easing as Euro Area inflation closed March 2019 at 1.4% - against a target of 2%. ZAR depreciation was premised on generalized market fears of a politics-related credit rating downgrade and associated portfolio outflows.

Commodities traded mixed

Commodity prices closed predominantly softer during the quarter under review, as highlighted in the table below.

Commodity	Price	Q1'19	FY'18
Crude Oil (usd/bbl)	68.14	26.70%	-19.10%
Gold (usd/oz)	1 291.66	0.64%	-1.01%
Platinum (usd/oz)	848.52	6.53%	-14.32%
Nickel (usd/ton)	12 775.00	10.70%	-4.55%
Coffee (usc/lb)	94.35	-6.03%	-19.55%
Maize (usd/ton)	146.94	-0.67%	7.20%
Wheat (usd/ton)	461.75	-9.10%	19.11%
Sugar (usc/lb)	12.54	2.37%	-18.11%
Cotton lint (usc/lb)	75.98	4.66%	-7.62%

Oil prices were supported by signs of low global supplies in line with Organization of Petroleum Exporting Companies (OPEC) measures to cut supplies and prop up prices. Further supply side pressures were driven by political instability in Venezuela (world's largest proven oil reservoir) and associated production disruptions.

Soft commodity prices were predominantly softer due to a bullish harvest outlook across most crops. Sugar prices firmed, with support from increased ethanol production in Brazil reducing global supplies. Other big producers also faced weaker harvest prospects from adverse weather conditions.

Economic Outlook

The global economic growth outlook (measured by GDP) remains depressed, particularly in light of weakness in advanced economies, as well as spillover effects on emerging and developing countries. Persistent trade tensions in major advanced economies threaten aggregate economic output and weighs down on raw commodity demand.

Rising oil prices imply an additional tax on net oil importing countries, translating to consumer price increases. In the absence of fiscal buffers to protect vulnerable groups from inflation; social misery is likely to increase. Sub-Saharan countries face the additional burden of population growing fast than economic output – sustaining the risk of socio-political instability.

Zimbabwe| (Still) in transition

President Mnangagwa announced a 150% fuel price increase on 13 January 2019. He cited widespread market distortions and associated rent-seeking behaviors. Resultantly, trade and civil activist groups called for a three day mass stay-away in protest over generalized economic hardships. The ensuing protests attracted military intervention following unprecedented levels of socio-political fragility; characterized by looting, destruction of assets and several deaths.

President Mnangagwa condemned the violent protests, called for calm and reiterated that economic reform is a momentous task. This notwithstanding; South Africa's opposition DA party engaged the International Criminal Court and United Nations Human Rights Council, citing human rights abuses in Zimbabwe. Britain's Commonwealth Minister warned that reports of military brutality jeopardize Zimbabwe's Commonwealth re-admission chances.

Sanctions maintained…

Citing allegations of human rights abuses; the EU parliament urged Zimbabwe to urgently withdraw all military personnel and called on all political actors to exercise responsibility and restraint. The EU parliament went on to remind Zimbabwe that EU members' support is conditional on its respect for rule of law and international treaties/conventions. It further encouraged the European Council to tighten sanctions on Zimbabwe.

The EU Council responded by broadly maintaining sanctions on Zimbabwe, such as an arms embargo. The United States also extended sanctions against Zimbabwe by one year - citing policies that 'pose unusual and extraordinary threat to American foreign policy'. The United States targeted sanctions list for Zimbabwe includes 84 individuals and 56 entities - accused of gross corruption and/or human rights abuses.

The impact of sanctions is likely to go beyond the targeted list, due to the influence of the targeted individuals and entities. Sustained sanctions underscore the need for further policy reviews towards full international reintegration. Compromised foreign relations threaten debt rescheduling and foreign funding prospects.

Acts of God expose structural vulnerability

In February 2019, the United Nations (UN) warned that more than five million people in Zimbabwe required food aid due to El-Nino-induced drought conditions. A month later; the already dire situation was worsened by tropical cyclone 'Idai' damage of unprecedented magnitude that hit Zimbabwe, Mozambique and Malawi. The UN estimated that more than 250 people died, 90,000 were displaced and that 95% of physical infrastructure was damaged in Zimbabwe's Chimanimani district.

Cyclone Idai's true economic cost is yet to be fully quantified. What is certain though is an unbudgeted drain on an already compromised fiscus - with ZWL100 million having been set aside for relief and rehabilitation efforts. Private sector and international support to complement government efforts has been particularly encouraging - despite occasional allegations of misappropriation and politicization of aid. The natural catastrophes exposed the country's fragility as a small, partially isolated, economy.

Softer quasi local currency…

The Reserve Bank of Zimbabwe released an eagerly anticipated monetary policy in which it (re)denominated (non-Nostro) bank balances and Bond notes into a quasi-currency known as 'RTGS Dollars'. The RTGS$ (ZWL) was immediately devalued by 60% against the US$, from the earlier prescribed parity position. Further, the ZWL will be tradable for alternative currencies on an interbank foreign currency auction system to facilitate access and pricing of foreign currency on a market determined basis.

Some critical sectors such as electricity and cooking oil will continue to receive foreign currency through the allocation system. Current receipts will be required in order to access foreign currency on the interbank foreign currency auction system.

The pre-policy announcement period was characterized by wide-spread incomes and pricing distortions. The post-policy environment remains fragile. The introduction of an auction-based (local) currency pricing platform is envisioned to make the valuation of local assets more objective, yet softer in hard currency terms.

Though better than the arguably inflated parity, a softer local currency makes imports more costly in local currency terms - fuelling inflation as importers pass the added cost to consumers.

Tobacco marketing season off to a slow start

The 2019 tobacco marketing season opened on 20 March 2019. A Central Bank directive that farmers be paid in ZWL and apply for settlement of 50% of net sales proceeds in their FCA accounts attracted adverse sentiment with many farmers demanding full settlement in hard US$. The directive has since been amended to make it more acceptable. In the first eight trading days to 31 March 2019, deliveries to the auction floors were down 93% from the same period last year.

Treasury intervention led to tobacco trading being exempted from the intermediate money transfer tax (2%). This notwithstanding, some farmers and merchants still expressed concern at the settlement currency and generalized settlement complexities. Further, some farmers have reportedly called on government to intervene and ensure improved auction prices. Such price intervention however, would threaten the efficiency of the auction system.

ZWL weakness fuelling inflation

The ZWL closed March 2019 at ZWL3.01 to the US$, about 17% weaker from ZWL2.50 at the start of the month. The RBZ estimates that about US$3 million is trading on the auction platform daily. This notwithstanding, most importers are reportedly still not able to access foreign currency on the auction platform - sustaining the risk of a foreign currency crunch and the concomitant risk of a thriving parallel market.

Average consumer prices increased by 4.38% in March 2019, compared to 1.67% in the prior month. Between December 2018 and March 2019, the average price increase reached 17.54%, compared to 0.12% in the corresponding period last year. Year on year inflation for March 2019 reached 66.80%, mostly attributable to exchange rate dynamics over the period October 2018 to March 2019.

Equities on the back foot

ZSE market capitalization closed the quarter to 31 March 2019 at ZWL16.235 bn; down ZWL3.299 bn (16.89%) from the quarter's opening position as highlighted below.

Sector/Index	Value	Q1'19	FY'18
Commodities	1475.35	-13.24%	71.77%
Consumer	716.65	-17.70%	75.69%
Financial	729.89	-21.08%	393.76%
Listed Property	201.73	-5.37%	6.50%
Manufacturing	348.07	9.77%	62.23%
Industrial	405.57	-16.74%	46.28%
Mining	193.98	-14.81%	59.91%
Top Ten	114.61	-20.97%	45.02%
All Share	121.66	-16.81%	46.24%
Market Cap (ZWL mn)	16 234.71	-16.89%	93.02%

ZSE losses were partly attributable to the introduction of an interbank forex market system which kicked off at a favorable rate than the parallel market rate.

Total trades on the local bourse retreated 70.8% to ZWL76.1 million during the month ended 31 March 2019. The average daily value of trades also shed 78.3% to ZWL3.4 million during the same period. ZSE foreign investor participation during the quarter under review closed at 66.0%, up from 38.3%. Net foreign portfolio inflows for the quarter were ZWL1.75 mn, down from ZWL23.98 mn in the same period last year.

Economic Outlook

Zimbabwe is still in political-economic transition. The pace and potency of policy reform has been less than earlier anticipated - despite noteworthy progress being registered. Domestic policy reform momentum faces a significant threat from negative externalities; notably adverse weather, sustained strategic isolation, as well as commodity price fluctuations. In the absence of tangible reforms towards enhanced international support as well as public and investor confidence rebuilding; we maintain a sub-optimal view on the foreseeable outlook.