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MONTHLY ECONOMIC BRIEF

Q2 2019

Highlights

- China's growth rate at its lowest in 27 years; as the trade war continues to hamper growth.
- Persistent Brexit uncertainty leads to downward pressure on global demand.
- Nigeria signs the AfCFTA leading to the largest trade agreement in WTO history.
- The end of the multi-currency regime in Zimbabwe and return of the ZWL.
- 2018 FDI in Zimbabwe strongest on record.
- Inflation closed June 2019 at a new post-hyperinflation peak of 175.66%.
- ZSE market capitalization gained ZWL11.021 bn (67.88%) to ZWL27.255 bn in Q2 2019.

Global economic growth at risk...

The US-China trade war has contributed to China's economy decelerating to its slowest growth rate in 27 years. This has led to speculation that both countries are increasingly under pressure to secure a trade deal as China's export figures fell by 1.3% in the second quarter of 2019. The United States has also been feeling the effects of the trade war as their exports fell by 8.2% in the second quarter.

An extended economic confrontation between the US and China (world's largest economies), threatens global economic output. Further downward pressure arises from persistent European Union fragility and broader geo-political stability concerns in the Middle East and North African regions.

Brexit uncertainty reduces global demand

To further exasperate global growth prospects; news on Brexit continues to remain uncertain creating pressure in the global economy. United Kingdom authorities have seemingly failed to finalise a Brexit deal after failing to compromise on key issues. This has led to Prime Minister Theresa May resigning. She has since been replaced by Brexit supporter Boris Johnson. A messy Brexit scenario will have huge effects for global trade. Any 3rd party trade deals from the EU will cease and $35bn worth of exports from the EU into the UK are expected to stop. On the flipside; this also presents opportunities for small countries to increase trade with the UK and/or the EU, separately; because the UK will also be looking for new trading partners with which it can negotiate trade deals quickly. Given that the majority of the UK's trade is with the EU this could open up access to the UK's markets especially for developing countries looking to increase exports.

Opportunity to improve Intra-Africa trade…

The African Continental Free Trade Agreement (AfCFTA) which officially came into force in May 2019 has just managed to sign Africa's largest economy - Nigeria. It is envisaged to be the largest trade agreement since the establishment of the World Trade Organization (WTO) in 1994. It is made up of 54 African countries and is expected to bring significant gains to intra-Africa trade. It is also expected to boost Africa's net income by US$2.8bn per annum. Currently, intra-African exports only make up 19% of total African trade and this agreement is expected to significantly improve this.

Increased tensions in the Persian Gulf

On June 13th an Oil tanker, passing through the Strait of Hormuz was attacked. Allegations are that the Islamic Republic of Iran was responsible for the attack. This led to fears that there could be future attacks on oil tankers in this region. The Strait of Hormuz is one of the most highly trafficked waterways and accounts for around 25% of global seaborne oil.

This raises concerns over the security of oil supply from the region, compounding the increased tension between the US and Iran over sanctions introduced by the US earlier in the year. The Persian Gulf is responsible for a large proportion of the world's oil supply, and this means that an increase in tension in the area will lead to supply-side uncertainty in the oil market. Global oil demand for the 2nd half of the year is expected to increase after a slow start in the 1st half of the year.

Although demand is expected to improve, the market is believed to be oversupplied which could help to contain international oil prices.

Global equities

There are concerns in the global equities market as investors do not believe that there is much room left to grow. This comes after the US indices have been at record highs with the S&P500, DJIA and the NASDAQ composite all closing at record highs. However, company earnings and revenue growth are expected to be down in line with depressed global growth and persistent trade tensions.

Investors were thought to be overconfident about earnings and had been bullish in the 1st half of the year. Asian equities have already shown this and have been trading weaker compared to their US counterparts. The effect on Asian markets is mostly to do with the effects of the trade war on China and this is expected to filter through to the global equities market in the 2nd half of the year. Currently, the US market is being kept bullish on the expectation that the US Federal Reserve might lower interest rates relatively soon.

US$ advances

On average the United States dollar (US$) traded stronger against most currencies including the British Pound (GBP) and the South African Rand (ZAR). This is more due to the fact that other currencies were weakening as the global economy appeared to be slowing down. The dollar also started the quarter off a lower base given its weakening in the 1st quarter of the year. The dollar closed the quarter ended 30 June 2019 1.14% firmer against the Euro and traded at $1.13661 per Euro.

The Euro is expected however to weaken against the dollar as generalized Brexit and associated Euro Area uncertainty weighs on the Euro. The United States also increased tariffs on steel imports to the US which is expected to reduce trade. The South Africa Rand (ZAR) appreciated in the period under review on the back of increased investor confidence in the post-election outlook, as investors anticipate improved policy stability.

Commodities traded mixed

Commodity price movements were mixed during the quarter ended 30 June 2019, as highlighted in the table below.

Commodity	Price	Q2'19	YTD'19
Nickel (usd/ton)	12,660	-0,90%	19,55%
Crude Oil (usd/bbl)	66,53	-2,36%	23,71%
Gold (usd/oz)	1 412,85	9,38%	10,08%
Platinum (usd/oz)	816,81	-3,74%	2,55%
Coffee (usc/lb)	108,85	15,37%	8,42%
Maize (usd/ton)	177,55	20,83%	20,03%
Wheat (usd/ton)	543,00	17,60%	6,89%
Sugar (usc/lb)	12,79	1,99%	4,41%
Cotton lint (usc/lb)	66,20	-12,87%	-8,82%

Oil prices registered a 2.4% decline, though maintaining strong year to date gains. Year to date gains have been supported by traders taking positions ahead of an anticipated rebound in manufacturing activity during the 2nd half of the year. There was further support from supply side constraints as the Organization of Petroleum Exporting Countries (OPEC) also continues to restrict supply compounded by the concerns of conflict in the Persian Gulf.

A softer dollar presented significant support to international commodity prices, as dollar denominated commodities became more affordable in alternative currency terms. Cotton went against the general trend, retreating a noteworthy 12.9% on the back of increased use of more competitively priced synthetic materials.

Economic Outlook

The global economy remains uncertain with key issues such as the US-China trade war and Brexit still unresolved. Broad sentiment on the global economic outlook remains bearish due to persistent trade and technology wars.

The International Monetary Fund (IMF) predicts a sluggish, but positive, global economic outlook - enough to avert a recession. The IMF predicts global GDP growth of 3.2% and 3.5% in 2019 and 2020, respectively, noting that risks to the forecasts remain skewed to the downside.

Zimbabwe| End of the multi-currency regime

In a shock announcement, government through the Ministry of Finance officially declared the end of the multi-currency system through Statutory Instrument (SI) 142 of 2019. Also in the instrument, government ordered that all local bank balances, bond notes and bond coins were effectively converted to ZWL at parity while the operation of foreign currency accounts will continue as usual.

To strengthen the Zimbabwe dollar; the central bank introduced tighter monetary measures. These include raising the overnight lending rate from 15% to 50% and mopping up about ZWL 1.2 billion from banks for settlement of unsettled foreign obligations (at par). To mitigate speculative activity; a 90 day vesting period was placed on locally bought fungible stocks. To facilitate efficient ZWL price discovery; authorities lifted administrative caps on bureau de change and the 2.5% margin on interbank foreign currency trades.

Through this announcement, the Government hopes that the measures will lead to reduced speculative activity and a more efficient foreign currency trading interbank market to improve price discovery. The downside risks to this are a rapid devaluation of the ZWL leading to increased costs of key imports such as fuel and electricity. Further risks come from the inherent shortage of foreign currency in the market and generally depressed market confidence.

FDI 2018 strongest on record…

According to the United Nations Conference for Investment and Trade; Zimbabwe registered US$745 million in Foreign Direct Investment (FDI) inflows (highest on record). The previous peak was US$545 million in 2014. Net inflows closed at US$718 million, up 134% from 2017. During the same period, FDI inflows to Zambia, Mozambique and South Africa closed at US$769 million, US$2.7 billion and US$5.3 billion, respectively. Zimbabwe's 2018 FDI inflows translate to 1.6% of total inflows to Africa - up from 0.8% in the previous year.

The United Nations also noted that Zimbabwe's Greenfield investment project announcements surged 1,329% from US$420 mln to US$6 bln in 2018. Foreign investment inflows are regarded as a proxy of an economy's investment attractiveness. The notable growth in FDI inflows in 2018 underscores the positive investor sentiment in 2018. Going forward, sustained investor optimism will be critical in closing the gap between FDI announcements and inflows.

IMF approval of Zim policies through SMP

In response to a request by Zimbabwean authorities; the IMF approved a Staff Monitored Program (SMP) for Zimbabwe. The SMP is an 'informal agreement between a country and IMF staff' and does not entail endorsement by the IMF Board. Under the SMP, IMF staff will monitor implementation progress on Zimbabwean authorities' self-imposed targets. Targets (to Jun'19) included; ZWL1.2 bn budget deficit ceiling and no new non-concessional foreign debt. The latest SMP covers the period from May 2019 to March 2020.

It is envisaged to build a track record of reform performance. Broadly, the SMP targets implementation of fiscal consolidation, monetary tightening and improved governance. The IMF however noted that 'risks to the SMP are very high', citing high political and social costs of reform. The IMF also noted that Zimbabwe's recent track record on technical assistance implementation has been mixed.

The SMP presents an opportunity to garner confidence-by-association. Further, if sincerely and fully implemented; technical assistance could help bridge inherent capacity constraints. The concomitant risk hinges on authorities failing to meet the self-imposed reform targets.

Narrower trade deficit…

In the first five months of 2019, the country's trade deficit decreased by 63.88% compared to the same period in the prior year. This was partly caused by a significant increase in the export of commodities in the mining and agricultural sectors. The major increases came in nickel mattes which increased by 50.75%, nickel ores which increased by 35.88% and tobacco exports which increased by 58.96% compared to the prior year. Total exports improved by 26.51% in the five months to May 2019 to US$1.558bn

Imports decreased by 16.23% compared to the first 5 months of 2018 to US$1.957bn. Major imports consisted of diesel, petrol and soya bean oil. The top contributors to imports are all necessities and therefore it seems unlikely that the import side of the current account can be improved by reducing imports. Given the drought currently being experienced; imports of food and electricity pose a threat to the trade balance.

The focus, therefore, needs to be on improving the country's exports to narrow the current account deficit. This should help to support monetary policy stability by improving the supply of foreign currency.

Tobacco marketing season update

The 2019 tobacco season started very slow and in the first week of trading, deliveries were down 93% from the same period last year. This was largely as a result of a complicated pricing and settlement currency framework which led farmers to withhold their tobacco. Since then auction prices improved and by the end of the quarter under review, volumes brought to auction improved significantly to 205 million kgs - 7% lower than the same time last year.

ZWL still finding its feet

The ZWL closed June 2019 at ZWL6.62 to the US$; about 54.5% weaker from the beginning of the quarter to 30 June 2019. The ZWL depreciation is in part a result of recent measures towards liberalizing the official interbank foreign currency market following official parity between the ZWL and US$.

Galloping inflationary pressures

Average consumer prices increased by 39.26% in June 2019, compared to 12.54% in the prior month with Year to June 2019 inflation at 94.37%. On a year on year basis, the period between June 2018 and June 2019 registered inflation of 175.66%, and this is in-part as a result of the depreciation of both the interbank exchange rate and the parallel market rate.

Equities closed firmer

ZSE market capitalization closed the quarter to 30 June 2019 at ZWL27.255 bn; up ZWL11.021 bn (67.88%) from the quarter's opening position as highlighted below.

Sector/Index	Value	Q2'19	YTD'19
Commodities	2410,18	63,36%	41,73%
Consumer	1176,39	64,15%	35,09%
Financial	1381,00	89,21%	49,32%
Listed Property	304,44	50,91%	42,81%
Manufacturing	459,51	32,02%	44,91%
Industrial	683,51	68,53%	40,31%
Mining	255,26	31,59%	12,10%
Top Ten	203,61	77,65%	40,40%
All Share	210,68	73,17%	44,06%
Market Cap (ZWL mn)	27 255,01	67,88%	39,53%

ZSE gains were primarily as a result of investors wanting to preserve value by investing in real assets, as a hedge against the high rate of inflation.

Total trades on the local bourse gained 11.4% to ZWL 545.3 million during the quarter ended 30 June 2019. The average daily value of trades also firmed 4.7% to ZWL 8.9 million during the same period. Foreign investors bought and sold stocks worth ZWL 203.8 million and ZWL210.3 million, leading to net outflows of ZWL 6.5 million during the quarter under review. The prior quarter registered net inflows of ZWL 2.2 million.

Economic Outlook

The Government faces a noteworthy task in creating a stable monetary policy, largely as a result of weak foreign currency reserves as well as compromised public and investor confidence. Resultantly, the ZWL faces a risk of further depreciation. Inflation expectations are anchored on the threat of increased import costs for critical imports such as fuel; with inflationary pass-through effects to the rest of the economy. Overall, the outlook is characterized by recession and excess inflation concerns.