MONTHLY ECONOMIC BRIEF

Q3 2019

Highlights

- The US Federal Reserve Bank warned of increased recession risks.
- Collapse of Thomas Cook brought responsible business and corporate governance to the fore.
- The IMF completed its first Zimbabwe Staff Monitored Program review.
- (Implied) inflation closed September 2019 at a new post-hyperinflation peak of 353.3%.
- ZSE market capitalization gained 12.9% to ZWL$30.770 bn in Q3 2019.

Confluence of global downside risks…

Generalized global macro-economic vulnerability dominated environment themes during the quarter ended 30 September 2019. The broad concern was around a potential global recession - particularly in light of structural fragilities in the United States, European Union and China. Protracted uncertainties around the U.S-China trade crunch, exacerbated by protracted Brexit negotiations sapped confidence and weighed on gross investment growth.

Fed warns of recession risk

The U.S Federal Reserve warned that chances of a recession in the U.S over the coming 12 months are around 35% - about the highest since April 2008. The probability is based on the shape of the U.S yield curve, where it closed with the 3 month Treasury yields higher than over the 10 year tenure. Such yield curve shapes (humped) have traditionally acted as a reliable recession predictor over the past 50 years.

Other recession forward indicators are less adverse though. Oil prices have historically been a key predictor - as all recessions post 1980 followed a price jump of at least 90%. Oil prices so far have stayed relatively in check (down 26% year on year as of September 2019). Another common indicator (the Sahm indicator) assumes a 0.5% rise in unemployment over three months points to a recession. U.S unemployment closed September 2019 at a 50-year low.

Brexit (no) update…

The United Kingdom is set to exit the EU on 31 October 2019 (Brexit). Brexit came out of a June 2016 referendum and was originally scheduled to have occurred by 29 March 2019. This notwithstanding, negotiations for a 'soft exist' deal from the EU have been protracted and the exit date has been postponed several times. The latest update is that negotiations are still on-going and another extension is possible.

If the UK fails to broker a deal and embarks on a 'no-deal Brexit', the direct implications include stricter EU boarder checks on British goods. This could entail increased delays at ports as well as trade and commerce bottlenecks. Further adverse consequences on Britain include a weak currency and a contraction in economic output. The net impact of Brexit remains indeterminate, with concerns mostly around uncertainty.

Political-economy lessons from Argentina

Argentina's currency crisis deteriorated, with the government declaring that it was necessary to adopt 'a series of extraordinary measures to ensure the normal functioning of the economy'. Resultantly, foreign currency purchases were restricted following a steep drop in the Argentinian Peso. Further, external payments require approval by the central bank and the country sought to defer IMF debt repayments.

During the quarter under review, the Argentinian Peso fell to a record low of 65 per US$ against the USD; inflation closed the first of the year at 22% and the economy contracted by 5.8% in Q1'2019. Elections in October 2019 also fuelled overall fragility. Argentina continues to be a text book example of the implications of political-economy instability and associated diminishing returns from over-regulation.

Thomas Cook collapse opens can of worms

Travel company Thomas Cook collapsed after 178 years of operation, leaving more than 9,000 people directly unemployed and about 150,000 British holidaymakers stranded oversees. The company's head Peter Fankhauser said he was 'deeply sorry' for the company's historic collapse. He however defended the £8.3m he has been

paid since November 2014, saying that around half the amount was in the form of shares - which were now worthless has he had not cashed them before the company's liquidation on 23 September 2019. Mr Fankhauser's remuneration has attracted criticism from staff, unions and politicians. With politicians questioning the role that management actions and accounting practices played in the company's collapse.

Global equities on the back foot

Global equity markets struggled during the quarter to 30 September 2019. Developed market equities closed the quarter under review 1% weaker, while emerging market equities retreated 4.3% over the same period.

Within developed markets, Japan bucked the general trend, gaining 3.1%, while Hong Kong shed 12% (mostly attributable to incessant anti-government protests). Within emerging markets, Taiwan registered the only positive return (5.2%), while South Africa retreated 12.6% - attributable to an increasingly fragile political environment.

US$ registered strong gains

The United States Dollar registered strong gains against most trading currencies. Firmer than anticipated economic data, in the context of concerns of a possible recession; supported the US$. The US$ was also propped up by signs of a slowing Chinese economy weighing down output in many emerging market economies.

The US$ gained 6.4% and 3.8%, against the South African Rand (ZAR) and the Euro, respectively, in the quarter to 30 September 2019. Resultantly, the US$ closed the period under review at ZAR15.09 per US$ and US$1.09 per Euro. The Zimbabwean Dollar (ZWL$) shed 56.4% to ZWL$15.20 per US$ over the same period.

Commodities traded mixed

International commodity prices were mixed at the end of the quarter under review. Nickel prices registered a conspicuous upswing - partly attributable to worries of a possible ore export ban by major producer; Indonesia. The ban was initially set for 2022, but market rumour of it being pulled to 2019 spurred speculative buying.

Commodity	Price	Q3'19	YTD'19
Nickel (usd/ton)	17 405.00	37.48%	50.82%
Crude Oil (usd/bbl)	60.95	-8.39%	13.33%
Gold (usd/oz)	1 484.05	5.04%	15.63%
Platinum (usd/oz)	915.48	12.08%	14.93%
Coffee (usc/lb)	100.65	-7.53%	0.25%
Maize (usd/ton)	146.55	-17.46%	-0.93%
Wheat (usd/ton)	488.75	-9.99%	-3.79%
Sugar (usc/lb)	12.67	-0.94%	3.43%
Cotton lint (usc/lb)	60.69	-8.32%	-16.40%

Confusing US-China trade crunch signals exacerbated by Brexit uncertainty during the quarter under review presented safe haven support for gold, extending year to date gains.

Improved geopolitical conditions in the Middle East and North Africa region (particularly Syria and Saudi Arabia) eased supply pressures and weighed down oil prices.

Soft commodity prices closed the period under review softer, weighed down by less than earlier feared harvest projections in major crop producers such as the United States and Brazil.

Economic Outlook

In the absence of a major supply shock, oil prices are broadly predicted to remain under check, containing global inflation. The concomitant risk is weaker growth among net oil exporters and a net negative impact on global growth.

Downside risks on the global economy include muted though noteworthy recession concerns in the United States and rising global socio-political instability - particularly given widespread anti-government protests across the world. Downside risks would be incomplete without mentioning persistent Brexit uncertainties. Extreme weather events also pose an inherent downside risk.

Full and actual reasons for the collapse of travel giant Thomas Cook will become clearer with time; yet what is clear already is that corporate governance and responsible business practices should never be taken for granted. Resultantly, we anticipate more top-down reforms towards enhanced responsible business practices as compared to the current bottom-up push.

Zimbabwe| Still work in progress…

That macro-economic reforms would be painful was anticipated; yet the magnitude of social misery attributable to on-going reforms (or lack of it) is still shocking. Further concern is that the reform agenda is still on-going and suggests more to come, particularly regarding monetary policy refinements. This is notwithstanding Minister Finance Hon. Mthuli Ncube's reported assertions that austerity is over and authorities are soon to adopt growth inclined macro-economic policies.

IMF predicts steeply negative 2019 growth

The International Monetary Fund (IMF) staff predict that Zimbabwe's 2019 GDP growth will be 'steeply negative'; while pressure on the exchange rate has increased - partly due to weakening confidence and recent monetary expansion. The IMF noted key challenges as containing national spending and rebuilding confidence in the local currency. Going forward, the IMF prescribed intensified effort on both economic and political reforms. The assertions were made at the conclusion of the first review of the IMF Staff Monitored Program.

Slow transition…

In his State of the Nation Address (SONA), President Mnangagwa reiterated that authorities are systematically pursuing the transitional stabilization program. A budget surplus in H1'19 of ZWL$803 mn allowed government to absorb unplanned spending such as post-cyclone rehabilitation, public wage adjustments and social safety nets. Government set aside ZWL$1.8 bn to augment command agriculture funding (ZWL$2.8 bn from the private sector), as well as inputs for vulnerable households.

To address prevailing electricity shortages; President Mnangagwa said government resorted to cost-reflective electricity tariffs and increased electricity imports. He also attributed relative improvements in fuel availability to cost reflective pricing. The SONA suggests an appreciation of the prevailing (dire) economic conditions, though legacy concerns around macro-economic policy inconsistency and compromised market confidence weigh heavily on overall policy efficacy.

MPS: 'Transition to normalcy'

The 2019 mid-term monetary policy themed 'transition to normalcy' was notably skewed towards supporting the ZWL$. Highlights included an increase in the overnight rate from 50% to 70% and the (planned) introduction of US$ denominated bonds. Further, government issued legislation outlawing the use of foreign currencies for quoting and settlement of all local transactions. Violation of the legislation attracts civil and/or criminal penalties.

Transition towards orthodox monetary policy tools such as the overnight rate underpins the policy theme. Higher interest rates are envisioned to contain inflation. A noteworthy risk is that the market might view US$ bonds as signalling re-dollarization. Overall, inherent exchange rate fragility is likely to persist in the absence of tangible foreign currency supply side interventions. If not managed carefully, reactionary monetary pronouncements could form the new normal.

Housecleaning issues…

On the 15th of July 2019 President Mnangagwa appointed an eight member commission to lead the Zimbabwe Anti-Corruption Commission (ZACC). The eight were selected from a pool of 12 recommended by Parliament following public interviews of 38 candidates. ZACC is broadly expected to zero-in on alleged irregularities stemming from the Auditor General's report, the NSSA audit report, Hwange Colliery issues as well as Command agriculture concerns.

Earlier to the appointments, ZACC officers had been endowed with arresting powers. The move was meant to enhance ZACC's effectiveness in addressing corruption. By the end of July 2019 (first month), ZACC had already made some high profile arrests on serious graft allegations. A major highlight was the arrest of the then Minister of Tourism Hon. Prisca Mupfumira. By the end of Q3'2019, ZACC was conspicuous by its silence, despite the blistering start.

Conspicuously familiar tone…

Foreign Affairs and International Trade Minister Dr. Sibusiso Moyo reportedly said the removal of

sanctions on Zimbabwe will increase investment and aid the implementation of land and security sector reforms. The Southern African Development Community (SADC) declared 25 October 2019 as a 'Solidarity day' against sanctions imposed on Zimbabwe by the US and EU. The SADC resolved to 'conduct various activities' in their respective SADC countries on the day to call for the immediate removal of the sanctions. SADC cites the sanctions on Zimbabwe as militating against regional growth.

Skating on thin ice…

The United States imposed targeted sanctions on Zimbabwe's Ambassador to Tanzania; Anselem Nhamo Sanyatwe (and his wife). He faces allegations of leading security forces that killed several civilians during post-election protests on 1 August 2018. The (targeted) measure is of no direct consequence to the macro economy, but is of grave symbolic importance. It ostensibly sends a warning that the 'international community' is watching and is growing less accommodative.

No ceiling to price increases…

According to the Zimbabwe Statistical Agency (ZIMSTAT); the total consumption poverty datum line (PDL) for five closed September 2019 at ZWL$2,191.62. The September 2019 PDL represents an increase of 56.1% for the quarter under review. Over the same period, ZIMSTAT consumer inflation was 68.2%. Using the old base (old currency), year to date inflation for September 2019 would be 227.0%; while year on year inflation would be 353.3%.

92 day TBs oversubscribed

Beginning July 2019, the RBZ issued TBs on an open tender basis. The first issuance in July 2019 was meant to map the yield curve while subsequent issuances were 'to fund government programs' and have conspicuously grown in amount. During the quarter under review, the RBZ issued TBs worth ZWL$324 million, over the 92 and 365 days horizon at interest rates between 13.7% and 15.6%.

Equities closed firmer

ZSE total market capitalization closed the quarter to 30 September 2019 at ZWL$30.770 bn, up 12.9% from the quarter's opening position of ZWL$27.255 bn as highlighted below.

Sector/Index	**Value**	**Q3'19**	**YTD'19**
Commodities	2839.75	17.8%	67.0%
Consumer	1341.36	14.0%	54.0%
Financial	1438.84	4.2%	55.6%
Listed Property	345.34	13.4%	62.0%
Manufacturing	648.23	41.1%	104.4%
Industrial	**774.55**	**13.3%**	**59.0%**
Mining	**317.75**	**24.5%**	**39.5%**
Top Ten	**218.09**	**7.1%**	**50.4%**
All Share	**232.52**	**10.4%**	**59.0%**
Market Cap (ZWL bn)	**30.770**	**12.9%**	**57.5%**

The ZSE industrial index advanced 13.3% during the quarter ended 30 September 2019 on the back of gains in most small and mid (by market capitalization) stocks.

Total trades on the local bourse retreated 14.5% to ZWL$466.5 million during the quarter ended 30 September 2019. The average daily value of trades also shed 19.1% to ZWL$7.2 million during the same period. ZSE foreign investor participation closed at 20.1%, down from 38%. Net foreign portfolio inflows for the quarter were ZWL$33.9 mn, compared to net outflows of ZWL$6.5 mn in the prior quarter.

Economic Outlook

A generalized fatigue clouds the environment. Broadly battered public and investor sentiment weighs heavily on near-term recovery prospects; exacerbated by continued strategic isolation from mainstream foreign capital and an incessant work in progress policy stance. Rising social misery poses a muted but noteworthy threat to overall environment stability. We anticipate muddling-through and survivalist tendencies to persist.