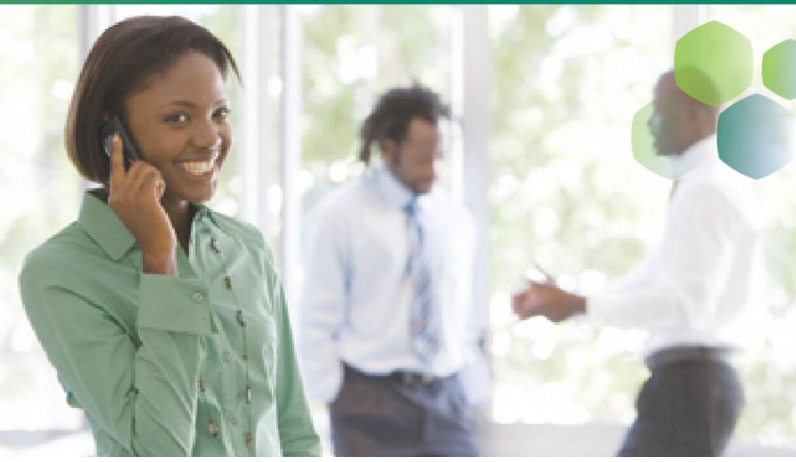
Monthly Economic Brief

September 2016



Highlights

Agric sector contraction weighing down growth prospects, 2016 GDP growth forecast revised down by 56%.

Budget deficit expected to end the year above US$1 billion as government rejects austerity proposals.

Trade deficit reached US$1.82 billion in August 2016.

Year on year inflation closed August 2016 at -1.43%, up from -1.60% in light of depressed aggregate demand.

ZSE market capitalization retreated 0.30%, closing the month under review at US$2.865 billion.

2016 GDP growth forecast downgraded to 1.2%

Presenting the 2016 mid-year fiscal policy statement, Minister of Finance Hon. Patrick Chinamasa revised the 2016 GDP growth projection from 2.7% to 1.2%. Treasury projects the mining sector to expand by 13.2% against a 4.2% contraction in the agriculture sector. Hon. Chinamasa acknowledged that the economy is facing strong headwinds; as such the 1.2% growth forecast has been generally viewed as generous. This notwithstanding, downward revision from 2.7% could be symbolic enough to capture prevailing difficulties.

H1'2016 budget deficit reached US$623 million

National revenues for the first half of 2016 closed at US$1.692 billion, of which taxes contributed 92%. The full year revenue forecast was revised downwards by 4% from US$3.85 billion to US$3.7 billion in light of a shrinking revenue base. Spending during the half year closed US$308 million above plan at US$2.3 billion, leading to a budget deficit of US$623 million. The full year deficit could close the year above US$1 billion. Employment costs (including 2015 bonuses of US$162 million) constituted 97% of total revenues in the first half.

The budget deficit has been primarily financed through government debt instruments. Hon. Chinamasa acknowledged the debt route is becoming increasingly unsustainable, highlighting that, 'lack of capacity to service debt has seen roll-over, posing risks to debt instrument holders.' To remedy the situation, Hon. Chinamasa prescribed austerity measures including public service salary cuts of 5% to 20%; 25,000 job cuts by December 2017 and suspension of bonuses for two years. The austere proposals were nullified a week later by government. The rejection of cost containment proposals against an apparent deficit considerably inflates the risk of a fiscal crisis - failure to settle a critical public obligation.

2016 eight months trade deficit reached US$1.821 billion

Zimbabwe's trade deficit for the year to August 2016 reached US$1.821 billion, 15% higher than in the previous month. Exports and imports over the period closed at US$1.508 billion and US$3.329 billion, respectively. Of the total exports, gold and tobacco contributed about 28% and 17%, respectively. Major imports were diesel, petrol and maize, accounting for roughly 16%, 9% and 8% of total imports, respectively. The nature of major imports makes it arguably difficult to address the trade deficit through import restrictions. Consequently, a sustainable solution could be through advancing exports. Persistent trade deficits could sustain cash shortages.

Multi-currency regime to stay, despite impending bond notes

Presenting the 2016 mid-year monetary policy statement, Reserve Bank of Zimbabwe Governor Dr John Mangudya reiterated that the multi-currency regime is here to stay. Dr Mangudya also disclosed that bone notes-export incentives will start being paid out by the end of October 2016. To date, export incentives worth US$56 million have been accumulated and they are expected to close the year at US$75 million at current export rates. Export incentives are also being extended to private money transfers, effective 1 October 2016.

Bond notes (trading at par with the US$) will be used and treated the same as bond coins. Issuance will be self-administered, based on export earnings; up to a ceiling of US$200 million. Bond notes are not a new currency, but zero-coupon, tax exempt debt instruments. To address market concerns regarding possible arbitrage opportunities, bond notes will be issued in transactionary small denominations of $2 and $5 only and an independent monitoring board may be formed. This notwithstanding; the market remains sceptical of the notes.

Depressed aggregate demand sustaining deflation

Year on year consumer inflation for August 2016 was -1.43%, up from -1.60% in the previous month. On a month on month basis, inflation firmed from -1.19% to -0.13%. Year to date inflation reached -0.82% on the back of depressed aggregate demand. The foreseeable outlook presents a high likelihood of persistent deflation in the absence of expansionary macro-economic policy to spur aggregate demand.

U.S Fed maintaining low interest rate policy

The United States Dollar retreated against most major trading currencies, registering declines of 0.5% and 4.9% against the Euro and South African Rand (ZAR), respectively, during the month ended 30 September 2016. On a year to date basis, the dollar extended losses against the Euro and ZAR to 2.7% and 10.8%, respectively. Dollar depreciation was primarily attributed to U.S policymakers maintaining a low interest rate policy in their latest (September 2016) meeting.

The near-term outlook presents noteworthy headwinds for the Euro in light of the Brexit pronouncements - Britain's decision to pull out of the European Union and accompanying announcements on modalities and timelines. The ZAR faces a less ominous outlook against the dollar, buoyed by an uncharacteristically conciliatory labour market. Resultantly, the ZAR may continue trending towards the psychological ZAR12 per dollar mark.

Weak dollar spurred international commodity demand

International commodity prices responded bullishly to the weak dollar. International trade is primarily conducted in dollar terms, such that a weak dollar makes commodities on the international market relatively more affordable in alternative currency terms. The following table highlights international commodity price movements during the month ended 30 September 2016.

Commodity	Price	Sept'16	YTD
Nickel (usd/ton)	10,525.00	8.34%	22.24%
Crude Oil (usd/barrel)	48.77	1.58%	32.89%
Gold (usd/oz)	1,325.40	0.79%	24.74%
Platinum (usd/oz)	1,035.65	-2.58%	18.74%
Coffee (usd/lb)	150.20	2.77%	21.28%
Maize (usd/ton)	128.73	3.56%	-8.97%
Sugar (usc/lb)	23.42	14.69%	53.98%
Cotton lint (usc/lb)	67.70	2.75%	6.25%

Platinum prices bucked the general trend during the month under review, retreating 2.58%. The decline represents more of a correction amid signs of the precious metal being overbought. Platinum prices had rallied significantly on the back of a supply deficit forecast for the year, driven by a combination of weaker mining output and a slowdown in recycling. Platinum prices maintained gains of 18.74% on a year to date basis, with scope for further gains in the foreseeable outlook.

Weak deposit uptake weighing on money market interest rates

Activity on the money market remained depressed in light of weak deposit demand associated with compromised borrower quality and inherent monetary policy uncertainties. Average interest rate quotes were largely unchanged across investment horizons. The average 90 days interest rate quote closed the month ended 30 September 2016 unchanged at 2.95%, down from 3.69% at the beginning of the year. The 360 days interest rate quote was also unchanged during the month at 3.67%.

Foreign investors still selling out…

The ZSE industrial index retreated 0.3% during the month ended 30 September 2016, extending its year to date decline to -13.84%. The mining index firmed 1.1% to extend year to date gains to 12.18% as highlighted in the following table.

Sector	Value	Sept'16	YTD
Commodities	233.99	3.70%	-19.60%
Consumer	138.17	-1.58%	-13.26%
Financial	78.83	3.86%	9.29%
Listed Property	91.72	-0.12%	-21.77%
Manufacturing	39.09	-6.83%	-15.28%
Industrial	**98.96**	**-0.30%**	**-13.84%**
Mining	**26.61**	**1.10%**	**12.18%**
Market Cap (usd bln)	**2.856**	**-0.30%**	**-11.08%**

The following tables highlight ZSE top and bottom 3 performing stocks for September 2016.

Top 3 Performers	Price USc	Sept'16	YTD
INNSCOR	23.05	19.43%	-23.06%
AXIA	3.60	12.50%	-52.00%
OLD MUTUAL	290.00	12.29%	42.57%

Bottom 3 Performers	Price USc	Sept'16	YTD
PPC	40.00	-33.33%	-60.00%
DAIRIBORD	3.60	-20.00%	-44.62%
ART	3.00	-11.76%	200.00%

For the tenth consecutive month, foreign investors were net sellers on the local bourse. Foreign investors registered net portfolio outflows of US$5.9 million, up from US$3.7 million in the previous month. The cumulative net portfolio flow position since the beginning of the year closed September 2016 at a negative US$36.1 million, compared to net inflows of US$3.9 million over the corresponding period last year.

The total value of ZSE trades in September 2016 firmed 83.4% to US$13 million, rebounding from US$7 million in the previous month; the lowest monthly value of trades in seven years. The average daily value of trades also registered a significant gain of 75% to US$0.6 million during the month under review, albeit under heavy selling pressure.

Economic Outlook

Major inherent threats to the macro-economy remain unchanged - budget and trade deficits. Fiscal policy prescriptions are noble in addressing the budget deficit, but face considerable political economy hindrances. Monetary policy prescriptions to improve the external position could be well meaning, but face the challenge of possible misinterpretation from a sceptical market. Consequently, the outlook presents a more of the same outlook, albeit with escalating downside risks if the twin deficits are not managed appropriately.