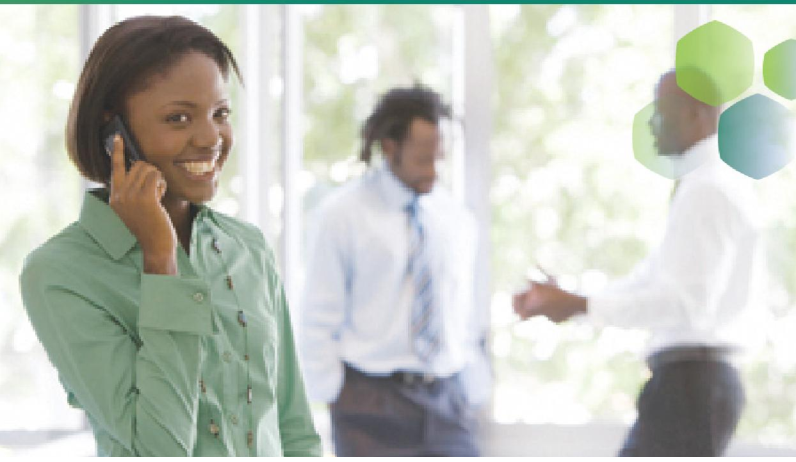
Monthly Economic Brief

January 2016



Highlights

Tight central government funding conditions weighing down aggregate demand.

The World Economic Forum warned that Zimbabwe faces a 61.5% probability of sliding into a fiscal crisis.

Inflation eased from -0.8% in 2014 to -2.47% in 2015 on weak aggregate demand conditions.

The South African Reserve Bank increased its benchmark interest rate by 0.5% to 6.25% to stem ZAR depreciation.

Total ZSE market capitalization closed the month 8.38% weaker at US$2.943 billion.

Generalised tension filled the atmosphere

Sporadic (though predominantly low-tone) incidents of rioting and generalised unease characterised the environment. Hot spots ranged from public service employees demonstrating against government's failure to honour 2015 bonuses, to transport crews demonstrating against increased operating fees. Street vendors also engaged municipal police in running battles as authorities intensified efforts to rid the streets of illegal vending. Overall, the atmosphere was relatively tense - particularly amid media reports of factionalism within main political parties.

Media reports alleged that opposition players are intensifying efforts to force an early election. This is despite a constitutional clause ensuring that the ruling party remains unchanged at least until elections in 2018. Former Vice President Dr Joice Mujuru's People First movement reportedly gained traction during the month under review, amid reports of several meetings between the movement and some opposition leaders. Political posturing is likely to dominate the environment, clouding the outlook and sustaining business-inhibiting public and investor uncertainties.

Old risks have escalated, new ones arising…

The first month of the year is a major forward-indicator of the year and January 2016 was no exception for Zimbabwe. Signs on the ground present a considerably difficult outlook. Old risks mainly centering on tight government funding have worsened while poor weather conditions are emerging as new risks.

A potentially record-breaking *El Nino* threatens the predominantly agriculture based economies of Southern Africa, Zimbabwe included. The last *El Nino* to hit Zimbabwe was in 1997/98 and it devastated crops and livestock. Without downplaying the risk; the macro-economic impact this time around could be partly diluted by a structural shift in the economy from an agriculture base to a services base.

Signs of fiscal distress became more apparent as government failed to honour bonuses in January 2016 as had been promised in December 2015. Reports of government prioritising settlement of salaries to uniformed services ahead of the rest of the public service intensified market concerns of compromised fiscal sustainability. During the month under review, the World Economic Forum warned that Zimbabwe faces a 61.5% probability of getting into a fiscal crisis in 2016.

Revised indigenisation frameworks

Government revised frameworks on the implementation of the indigenisation and economic empowerment act. The 'latest' frameworks dated 4 January 2016 replace those gazetted on 24 December 2015. They maintain empowerment credits that complement direct equity transfer, a development that has been broadly welcomed in the broad-based empowerment context. Of concern though, is that the latest frameworks omit an extended compliance period for affected firms, more-so given that the gazetted regulations still have some gaps on the fairly complex matrix for awarding credits. The proposed levy which is based on turnover, though still under discussion, is perhaps the biggest concern of the framework.

Inflation closed 2015 at -2.47%

Year on year inflation closed December 2015 at -2.47%, down from -0.80% in the previous year. Monthly inflation softened from 0.16% in November 2015 to -0.11% in December 2015. Deflationary pressures are broadly expected to persist given weak consumer demand conditions.

The Reserve Bank of Zimbabwe reported that money supply increased by 3.04% to US$4.74 billion in November 2015. On a year on year basis, money supply gained 7.5% in November 2015, up from 3.2% in the previous month. The (net) increase in deposits is likely due to a significant depreciation in the South African Rand (ZAR) in the final quarter of 2015 as well as reported increase in banking sector confidence. A weak ZAR would have lowered Zimbabwe's US$ import bill thus a lower outflow would have cushioned the net deposit stock, assuming exports were materially unchanged.

US$ maintained positive momentum

The U.S Fed rate hike rattled emerging market currencies before and after its enforcement in December 2015. Prospects of further rate hikes in 2016 fuelled speculation of continued weakness in emerging market currencies. South Africa's ZAR closed January 2016 5.99% weaker against the US$, at ZAR16.32 per US$, compared to US$15.40 at the beginning of this year. Hopes of a possible ZAR recovery are pinned on interest rate increases by the South African Reserve Bank, which increased its benchmark rate by 0.5% to 6.75% in late January 2016.

The US$ traded within a thin range against the Euro during the month under review. The direction however, favoured a continued drive towards parity between the 2 currencies as the US$ gained 0.14% against the Euro, closing at US$1.09 per Euro. Euro weakness was in part driven by speculation that the European Central Bank will maintain its quantitative easing program to boost Europe's faltering economic growth. Going forward, the prospect of parity before year-end is significantly higher than earlier anticipated.

Safe haven demand spurred gold rally

Commodity prices registered sustained weakness during the month ended 31 January 2016 as shown in the following table.

Commodity	Price	Jan'16	YTD
Nickel (usd/ton)	8,560.00	-0.58%	-0.58%
Crude Oil (usd/barrel)	34.49	-6.02%	-6.02%
Gold (usd/oz)	1,113.16	4.76%	4.76%
Platinum (usd/oz)	864.59	-0.87%	-0.87%
Coffee (usd/lb)	119.15	-3.79%	-3.79%
Maize (usd/ton)	144.18	1.96%	1.96%
Sugar (usc/lb)	13.33	-12.36%	-12.36%
Cotton lint (usc/lb)	61.64	-3.26%	-3.26%

Sustained commodity price weakness was primarily driven by weak global demand conditions and a flight to safety as investors dumped risky assets. Gold prices gained a noteworthy 4.76% in line with the flight to safety scenario. Maize prices also conspicuously bucked the weak trend, as *El Nino* related supply constraints threaten the global supply and demand balance.

Weak deposit uptake depressing deposit interest rates

Banking sector appetite for deposits remained weak on the back of an increasingly popular 'safe bank' lending model. Resultantly, money market interest rates faced continued downward pressure on a basic demand and supply basis. A low inflation premium driven by persistent deflation also worked against nominal money market interest rates.

The average money market interest rate over the 90 days investment horizon closed the month under review at 3.32%. In the same month last year, the same interest rate was at 5.76%. A weak inflation outlook and associated pressure on earnings inflate credit risk, incentivising continued cautious lending by banks, which translates to weak money market investment rates.

Foreign sales fuelled asset deflation on the ZSE

Persistent consumer price deflation erodes corporate earnings, escalating to asset price deflation as associated listed stocks depreciate in value. Weak aggregate demand conditions and the accompanying weak earnings outlook weighed heavily on the consumer sector as shown in the table below.

Sector	Value	Jan'16	YTD
Commodities	277.87	-4.52%	-4.52%
Consumer	138.87	-12.82%	-12.82%
Financial	72.90	1.08%	1.08%
Listed Property	112.93	-3.68%	-3.68%
Manufacturing	45.89	-0.54%	-0.54%
Industrial	**103.04**	**-10.28%**	**-10.28%**
Mining	**19.53**	**-17.66%**	**-17.66%**
Market Cap (usd bln)	**2,943**	**-8.38%**	**-8.38%**

During the month under review, the industrial index retreated 10.28%, while the mining index shed 17.66%. The local bourse declined by 8.38% in value, translating to US$269 million. The following table highlights the top and bottom 3 performing stocks for the month ended 31 January 2016.

Top 3 Performers	Price USc	Jan'16	YTD
STARAFRICA	0.80	33.33%	33.33%
CFI	6.06	21.20%	21.20%
TURNALL	1.10	10.00%	10.00%

Bottom 3 Performers	Price USc	Jan'16	YTD
MEDTECH	0.02	-50.00%	-50.00%
BINDURA	1.00	-34.64%	-34.64%
INNSCOR	20.70	-30.91%	-30.91%

Foreign investors, accounting for 62.6% of trades on the ZSE, bought stocks worth US$5.2 million in January 2016 against sales of US$9.0 million. The net foreign portfolio flows closed with a net outflow position of US$3.8 million, up from a net outflow of US$1 million in the same period last year.

Total trades on the ZSE closed the month under review at US$11.3 million, down 30.7% from the previous month. The average daily value of trades declined by 27.3% to US$0.567 million during the month ended 31 January 2016. Trades are likely to remain thin under tight liquidity conditions.

Economic Outlook

The outlook is less inspiring than earlier anticipated, as the market is increasingly void of positive milestones towards an inflexion from the current slump. Risks have become further skewed to the downside, particularly from a shrinking revenue base, translating to tight fiscal space and the cascading effects on household incomes. Overall, the environment is likely to remain difficult, with noteworthy risks from the possibility of adverse macro-economic policy measures in light of increasingly dire funding conditions. Caution remains prudent.