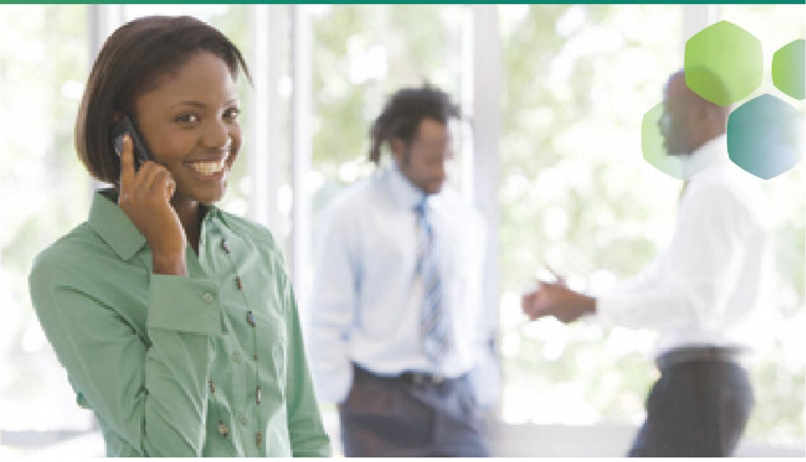
Quarterly Economic Brief

Q2' 2017



Highlights

Global cyber-attacks highlight data security vulnerabilities.

Ghana and China pursuing a US$15 billion mining deal.

Zimbabwe's total public debt was estimated at $11.8 billion as of March 2017.

Inflation sustained an upward trajectory; reaching a 43 month high of 0.75% in May 2017.

ZSE market capitalization firmed 49.96% to close Q2'17 at $5.937 billion.

Global | Straddling a dangerous path…

An increasingly fragile policy framework in South Africa triggered concern over investor protection following recent and seemingly escalating populist pronouncements. South Africa's ruling African National Congress (ANC) reportedly proposed at its policy conference that land expropriation without compensation should be allowed where it is 'necessary and unavoidable.' Such pronouncements raise the risk of a rushed and possibly chaotic land reform exercise on the horizons, threatening medium term growth prospects – with potential spillover implications for the entire Southern African region.

South Africa's monetary policy stability also came under increased threat amid reports the ANC plans to nationalize the Central Bank. South Africa's Central Bank is currently owned by private shareholders, with shares traded over the counter. Central Bank autonomy is a major credibility factor for public institutions, more so in light of shaky investor and public confidence. Although many Central Banks have been nationalized, from an era where they had started out as private companies – the move could adversely dent investor sentiment in the context of broader political economy vulnerabilities.

Digital platform poses new risks…

Questions over global digital security were raised after a computer ransomware spread across 150 countries, ravaging computer systems. The 'malware' would take over users' files, demanding $300 ransom to restore the files – with threats to double the ransom after 3 days, or delete them if victims failed to pay the ransom within 7 days.

Companies across the world warned employees to be vigilant when opening email. The U.K's National Crime Agency warning people not to pay ransom since there was no guarantee files would be restored. This notwithstanding, there were reports of unquantified amounts of ransom having been paid as desperate users tried to retrieve their files.

European Union (EU) Commissioner for Security Julian King said the EU was proposing legislation to reinforce cyber security, while computer firm Microsoft said the attack 'should serve as a wake-up call'. Russian President Vladimir Putin said 'Russia has absolutely nothing to do with it.' Overall, such cyber-attacks highlight the downside risk of digitalization.

A-luta continua… a more familiar problem:

The world's ninth poorest economy, Mozambique, faces funding constraints as creditors raise concern over public finance transparency. Creditors led by the IMF called for an independent audit of the country's loans as a first step to mending funding relations with Mozambique. The recently completed audit suggests 3 State entities cannot account for US$500 million of US$2 billion in undeclared government guaranteed debt.

In October last year, Mozambique announced it could not afford servicing its commercial dollar denominated debt and defaulted on its US$727 million Eurobond early this year, while missing payment on two State-guaranteed loans. Mozambique has since accrued arrears of US$490 million on the 3 loans. Mozambique's predicament makes a solid case for the nexus between public accountability and overall development prospects.

Heard that song before…

Tanzania's President John Magufuli signed into law new bills requiring government to own at least 16% in mining projects. The new laws; fast-tracked through Parliament, also increase royalties and state that no new mining licenses will be issued until Tanzania 'puts things in order.' Under the new laws, government can also renegotiate or terminate contracts with miners, while removing the right to international arbitration.

President Magufuli's arguably aggressive approach is considerably effective, though possibly not the most efficient. The 'bulldozer approach' also raises adverse medium to long-term downside risks, from damaged (foreign) investor sentiment. The concomitant risk hinges on possible future strategic isolation from the mainstream international community, low foreign direct investment and anemic economic progression.

Meanwhile…

Ghana reportedly agreed a US$15 billion deal with China, for development of Ghana's bauxite (used to make aluminum) mining sector including construction of refineries and railway infrastructure. Ghanaian authorities emphasized that the deal is more of a joint venture rather than a loan - with Ghana ceding some land in exchange for the funding. The two countries are currently 'in talks over the final terms of the deal.'

Ghana projects that the refineries alone will generate revenue of US$460 billion when completed. This notwithstanding, the deal has attracted considerable market scrutiny amid allegations Chinese miners have previously stripped resources from some African countries. The quality of governance within institutions seems to closely correlate to the quality of investors available to developing countries.

Political will and international support in Nigeria

Africa's most populous country, Nigeria, plans to roll out its first social-welfare program, with help from the World Bank. Nigeria plans to spend close to US$2 billion on the initiative this year. The need for such a project us underlined by reports of an estimated 65% of the population living on less than US$2 per day.

The welfare package has two conditions; that beneficiaries keep their children in school and immunize them. The intuition is that by ensuring education and health, the country can prosper from a wider pool of employable people. Reducing poverty is also broadly envisioned to yield knock-on effects for the entire economy, particularly by widening the consumption base. Authorities in Nigeria acknowledge that past welfare programs have failed, but believe this time will be different because there is strong political will and World Bank support.

US dollar on the back foot

The United States Dollar extended a weak run, closing the quarter ended 30 June 2017 soft. The dollar shed 0.1% against the South African Rand (ZAR) and 6.3% against the Euro to close the quarter under review at ZAR12.96 and US$1.14 (per Euro), respectively. On a year to date basis, the dollar extended its weakness against the ZAR and Euro to 4.9% and 8.4%, respectively.

Euro appreciation was supported by investors speculatively attempting to get-ahead of the European Central Bank's expected tapering of stimulus programs. Lower stimulus implies reduced funds injection making the Euro more valuable on a demand and supply basis - thus presenting some upside for Euro denominated asset holders.

Commodity prices mixed

International commodity prices were mixed during the quarter ended 30 June 2017, as highlighted in the following table.

Commodity	Price	Q2'17	YTD'17
Nickel (usd/ton)	9,270.00	-6.65%	-7.62%
Crude Oil (usd/barrel)	47.50	-9.71%	-16.91%
Gold (usd/oz)	1,243.58	0.12%	7.23%
Platinum (usd/oz)	924.61	-2.20%	1.98%
Coffee (usd/lb)	128.00	-7.85%	-5.50%
Maize (usd/ton)	147.14	4.25%	7.09%
Sugar (usc/lb)	507.75	20.25%	25.29%
Cotton lint (usc/lb)	13.69	-18.22%	-29.76%

Gold prices bucked the generally soft trend among hard-commodities. Gold prices were buoyed by generalized global vulnerability, in light of inflated geo-political tensions (as North Korea tested a long range nuclear missile), a new political administration in the United States (following the inauguration of Donald Trump as US President in January 2017.

Soft commodity prices were mixed, with sugar registering a noteworthy 20.3% gain during the quarter ended 30 June 2017. Global sugar supply concerns were triggered as major supplier Cuba projected its harvest to be 300,000 tons short of earlier forecasts. Cotton prices extended losses in light of cheaper synthetic substitutes.

Global Economic Outlook

Cyber security is likely to underpin a shift from traditional to new forms of global economic themes. Overall, the shift toward digital platforms is set to present new risks to global macro-economic stability. Generalized policy uncertainty sustains support for gold prices into the foreseeable outlook.

Weak, but positive growth

The IMF revised Zimbabwe's 2017 GDP growth forecast from -2.5% to 2%, citing favorable weather and a firm commodity outturn. The relatively bullish 2017 growth projection is dented by a projected -1.5% contraction in 2018, supposedly attributable to election disruptions and the fragility of transitory factors supporting current growth. At the conclusion of its 2017 Article IV consultations, the IMF warned that Zimbabwe requires international support and structural reforms in order to sustain positive growth.

The IMF forecasts inflation to close 2017 at 5%, before hitting a post-dollarization high of 8% in 2018. The inflationary outlook might be attributable to an increasingly fragile monetary policy framework, underpinned by a quasi-currency. Preparations for impending 2018 elections and associated monetary policy vulnerabilities could trigger inflation outcomes much more grim than the baseline projections. Past experiences with excessive inflation suggest spiraling inflation has no ceiling.

Long term view on sustainable growth prospects

The World Bank projects that Zimbabwe's economy will expand by 2.8% in 2017, underpinned by a rebound in agriculture. The World Bank also noted that medium term growth prospects 'remain modest' due to incomplete implementation of fiscal-adjustment policies. According to the World Bank, external arrears clearance will expand government's access to international capital - if sound fiscal management and structural reforms are successfully restored. Overall, the World Bank suggests near term underperformance will persist, though painting a more bullish outlook on the long term prospects

Compromised debt sustainability

The Parliament Budget Office estimated Zimbabwe's public debt as of March 2017 at around $11.8 billion. Domestic debt amounted to $4.3 billion, against external debt of $7.5 billion. The total public debt bill translates to 82% of GDP, while $5.2 billion of the $7.5 billion in external debt is in arrears. Resultantly, the economy's ability to settle its debts from internal resources is increasingly compromised, triggering the need for some form of future debt rescheduling.

In a press statement dated 27 April 2017, government announced it had met all conditions precedent to the repayment of World Bank and AfDB arrears (US$1.7 billion). Arrears clearance is generally viewed as the first step towards full international re-engagement – under an IMF financing program. Having met the conditions precedent; government intends to clear the arrears 'after evaluating possibilities of future flows from International Financial Institutions.' Arrears clearance - accompanied by confidence enhancing policy reforms and international support is likely to unlock new funding.

China cancelled Zimbabwe's debt…

China reportedly cancelled a number of Zimbabwe's debts. The debt cancellation was first announced in 2015 when China's President Xi Jinping visited Zimbabwe. Based on the December 2015 pronouncements during President Jinping's visit, the cancelled debt amounts to US40 million, making the gesture primarily symbolic in the context of Zimbabwe's total debt burden.

Good rains complementing government efforts…

According to a Southern Africa development Community (SADC) meeting of Agriculture Ministers; favorable rains after two consecutive drought years have driven a major rebound in grain output across the entire region. Countries that released their grain output figures showed impressive growth as follows; South Africa (83%), Namibia (80%), Malawi (38%) and Zambia (32%). In Zimbabwe preliminary estimates also predict a rebound in grain output.

The above normal rains in Zimbabwe might have been complemented by government initiatives such as 'Command maize production scheme and the Presidential inputs scheme.' Resultantly, government has reportedly taken a position that the command agriculture model should be applied to all sub-sectors of agriculture.

The ministry of agriculture said government's special maize output program 'command agriculture,' must not be politicised as it aims for national food security. The pronouncement followed fears of widening polarization within government over the expansion of command agriculture. Government plans to advance the program beyond maize. It has since secured a $487 million loan for the 2017/18 command agriculture season.

SI64 still stands - until local industry is up…

Minister of Industry and Commerce Hon. Mike Bimha said Statutory Instrument 64 (SI64 of 2016) that restricts imports of some basic commodities remains in place (until local industry can satisfy demand) - contrary to earlier media reports suggesting the policy had been reversed. Proponents of the policy cite a lower import bill and local industry revival, while the alternative view cites the possibility of limited supply creating inflationary conditions.

Inflated monetary policy vulnerabilities

Generalised uncertainty regarding monetary policy stability has reportedly sustained speculative market tendencies including hoarding of hard currencies and dual pricing. According to media reports, the central bank has issued about $160 million in bond notes (local quasi-currency) as at end of June 2017, against a US$200 million AFREXIMBANK guarantee.

Two retail outlets, Bathroom Boutique and Eurostar Electricals, were fined for contravening the Bank Use and Promotion Act. The court cited failure to bank cash by the companies. Bathroom Boutique was fined $9,700, while Eurostar was fined $20,000 for their alleged transgressions.

Surging inflation pressures

Having turned positive for the first time in 29 months in February 2017; inflation raced to a 43 month peak of 0.75% in May 2017. Year to date inflation reached 0.96% in May 2017, compared to -0.72% in the same period last year. Supply side constraints from import restrictions and compromised local output sustain an excess demand outlook fueling inflation and inflation expectations. Further inflationary pressure arises from speculative pricing tendencies associated with the market devaluing 'bond notes'.

Food inflation drove inflation during the quarter under review; though it tends to seasonally ebb in winter (improved supply from grain harvest). Food inflation against expectations could be attributed in-part to speculative pricing and import restrictions cited above. Going forward, further food inflation is expected from a mandatory government requirement for food producers to fortify processed foods starting 1 July 2017 – the cost of which is likely to be transferred to consumers.

Bond trading and Barclays deal…

The Zimbabwe Stock Exchange successfully re-introduced fixed income instrument trading in April 2017. The first listing was the first tranche ($5.4 million) of GetBucks Financial Service's $30 million medium term note. The $5.4 million instrument was in the form of promissory notes that were converted to three year paper attracting a yield of 11%.

First Merchant Bank (FMB) of Malawi purchased a majority stake in Barclays Bank Zimbabwe (subject to regulatory approval) from Barclays Plc. Barclays Plc is expected to retain 10% of the entity while 15% will go towards an employee share ownership scheme.

Listed equities in strong rebound…

The ZSE industrial index registered a strong rebound, gaining 41.03% during the quarter ended 30 June 2017. The mining index gained 19.18% over the same period as highlighted in the table below.

Sector	**30 Jun'17**	**Q2'17**	**YTD'17**
Commodities	556.57	49.69%	56.52%
Consumer	306.97	57.67%	46.20%
Financial	116.69	19.47%	22.43%
Listed Property	121.10	10.60%	1.80%
Manufacturing	88.65	30.81%	48.58%
Industrial	**195.97**	**41.03%**	**35.59%**
Mining	**69.79**	**19.18%**	**19.28%**
Market Cap ($ bln)	**5.937**	**49.96%**	**40.87%**

The following table shows the top and bottom three performing stocks during the quarter under review.

Top 3 Performers	**Price (c)**	**Q2' 2017**	**Market Cap ($)**
MASIMBA	4.80	152.63%	11,136,955
ECONET	35.38	120.44%	963,080,230
MEIKLES	25.00	108.33%	61,343,698

Bottom 3 Performers	**Price (c)**	**Q2' 2017**	**Market Cap ($)**
RTG	0.99	-16.81%	18,517,906
ART	5.50	-15.38%	24,033,755
ZIMRE	1.40	-15.15%	21,466,745

ZSE trades firmed 367.8% to $68.6 million during the quarter ended 30 June 2017; of which $39.7 million was recorded in the final month of the quarter. The average daily value of ZSE trades gained 63.7 % to close the quarter under review at $0.673 million.

Foreign investors remained net sellers, closing the quarter under review on a net outflow position of $13.5 million. Foreign investor participation declined from 52% in Q1 2017 to a post dollarization low of 28% in Q2'2017 - adding credence to the notion that local investors are moving from monetary assets to equities as an inflation hedging strategy.

Economic Outlook

The outlook presents significantly compromised fiscal stability, underpinned by increasingly unsustainable public debt. Widening budget deficits inflate associated risks such as a likely propensity towards expansionary and unorthodox monetary policy. Inflation dominates the economic outlook.