STATE OF THE ECONOMY *Report*

FIRST QUARTER 2019

An economic dashboard for Zimbabwe

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Produced by AEDS AFRICA ECONOMIC DEVELOPMENT STRATEGIES

in collaboration with

Publishers of dailynews dailynews on sunday

Editor-at-Large
Dumisani Ndlela

Magazine Editor
Dakarai Mashava

Report Authors
Dr Gift Mugano;
Dr Nyasha Kaseke;
Dr Richard Kamidza

Researchers
AEDS

Production & Technical Director
Tinashe Nekati

Design & Layout
Alwyn Mabehla

Proof Reading
Bothwell Matambanadzo

Transport
Annie Marime
Michael Chibwe

Visual Artists
Annie Mpalume
Brighton Goko

Editorial
Caroline Chiimba
Zvikomborero Muzamhindo

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FROM THE editor-in-chief

“The truth of the matter is that the average Zimbabwean business person neither has the time nor capacity to accurately establish on their own dependable information due to the abundance of sources with unverified economic details.”

Decision-makers: This is YOUR REPORT!

IN THE First World and elsewhere in the world, key information on economic fundamentals that business people need to help them make informed decisions that grow their enterprises is readily available at the click of a button.

Sadly, the Zimbabwean economy is characterised by paucity of evidence-based economic information that business people can rely on and easily access.

If they want information, local business people have to plough through several documents such as fiscal and monetary policies to glean important details on local and international prices, exchange rates, productivity levels, unemployment, trade performance and the political environment, among other factors.

The truth of the matter is that the average Zimbabwean business person neither has the time nor capacity to accurately establish on their own dependable information due to the abundance of sources with unverified economic details.

Given the foregoing, the Daily News had no hesitation to accept an invitation from the African Economic Development Strategies (AEDS) — a Zimbabwe-grown management consulting firm committed to drive the economic growth agenda of African economies to catch up and lead economic growth in the 21st century — to partner them in coming up with a maiden ‘State of the Economy’ Report packed with practical economic advice.

The quarterly report will, among other things, provide an economic dashboard on key economic indicators such as inflation, exchange rate, trade performance and budget performance, which are useful tools for decision-making purposes.

In order to accurately unpack the main causes of Zimbabwe’s economic challenges in addition to proffering practical solutions and predicting the Zimbabwean economy’s future, it is important to ensure that such an onerous task is carried out by thoroughbred economists with both the experience and the necessary aptitude.

We are very happy with the calibre of the economists putting together the ‘State of the Economy’ Report. These include the director and lead author Dr Gift Mugano, Dr Nyasha Kaseke, Dr Richard Kamidza and Latifa Kassim.

A report as critical as the ground-breaking ‘State of the Economy’ Report should not be the preserve of Harare.

In keeping with this, the AEDS and the Daily News will take forthcoming editions of the quarterly report to various cities and towns so as to allow business people in all parts of the country to acquaint themselves with the report and explore how it can make them improve their enterprises.

Hama Saburi
EDITOR-IN-CHIEF

We’re filling void in economic reporting

THE African Economic Development Strategies (AEDS) is a Zimbabwe-grown management consulting firm committed to driving the economic growth agenda of African economies to catch up and lead economic growth in the 21st century.

In pursuit of providing practical economic advice and closing the information gap in the economy, AEDS in conjunction with the Daily News, jointly produced “The State of the Economy Report”.

The report is expected to provide a new economic reporting in Zimbabwe by putting emphasis on discussions based on hard facts, rigour, pragmatism and objectiveness — telling it as it is!

For starters, in the last two decades, the Zimbabwean economy has gone through massive economic upheavals characterised by incessant company closures, unemployment, inflation, trade and fiscal imbalances as well as dwindling real incomes.

These economic fundamentals are largely influenced by the global economy, fiscal and monetary policies, local and international prices, exchange rates, productivity levels, unemployment, trade performance and the political environment among other factors.

Ironically, there hasn’t been a clear economic bulletin which provides thorough explanation as well as setting of the economic outlook for various economic players.

The purpose of the review is therefore not only to unpack root causes of the economic challenges but also to proffer practical solutions and as well as predicting the future.

In this regard, the report is expected to form a reference point, that is, an economic dashboard on key economic indicators which inter alia include inflation, exchange rate, trade performance and budget performance which are useful tools for decision making purposes.

Methodologically, this first issue was informed by data and critical literature which was sourced from reputable sources such as World Bank’s World Development Indicators, World Bank’s Ease of Doing Business reports, International Trade Centre, International Monetary Fund’s World Economic Outlook reports, Africa Development Bank, World Economic Forum’s Global competitiveness reports, United Nations Conference for Trade and Development investments report, etc.

Locally, researchers utilised data sourced from ministry of Finance and Economic Development, Reserve Bank of Zimbabwe, Zimbabwe National Statistics Agency (ZIMSTAT), Consumer Council of Zimbabwe, etc. Further, primary data was gathered through key informant interviews with key stakeholders such as the Governor of the Reserve Bank of Zimbabwe, Consumer Council of Zimbabwe, captains of industries and development partners, focus group discussions with top economists and experts.

It is my sincere hope that the collaboration between AEDS and the Daily News which saw the production of “The State of Economy Report” will fill a fundamental void in economic reporting.

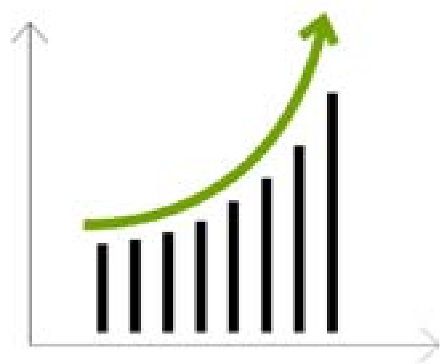
In the same vein, subsequent reports which will be produced quarterly are expected to provide a tracking mechanism on key macroeconomic issues such as progress on reforms, exchange rate performance, inflation dynamics, trade performance, progress on reforms, investments performance, etc.

Dr. G. Mugano
Executive Director
Africa Economic Development Strategies

Global and Regional Developments

GLOBAL economic growth is expected to decline this year. The decline will be caused by trade wars between major world producers and markets, moderating economic activity, heightened risks, financial stress, tightening of financial conditions and substantial financial pressure in emerging markets and developing economies (EMDEs). Zimbabwe, as a developing nation that relies heavily on the export of primary commodities, is negatively affected by these conditions, which may even further slow projected growth from four percent to 3,1 percent this year.

> "International commodity prices, which influence global economic activity, are expected to stabilise this year. However, commodity prices are likely to be negatively affected by escalating trade tensions between the United States and China, which will negatively affect commodity-dependent export countries such as Zimbabwe.



International commodity prices, which influence global economic activity, are expected to stabilise this year. However, commodity prices are likely to be negatively affected by escalating trade tensions between the United States and China, which will negatively affect commodity-dependent export countries such as Zimbabwe.

An upward trend in gold prices, which increased from US$1 249 per ounce in 2016 to US$1 269 per ounce in 2018, is a positive development for Zimbabwe.

Platinum, another major export earner for Zimbabwe, showed a downward trend from 2016 to 2018, with a price decline from US$987 to US$880. This is a big blow to the expanding platinum mining sub-sector.

Crude oil prices showed an upward trend from 2016 to 2018, with month-on-month average prices increasing from US$56,5 per barrel in December 2018 to US$64,1 per barrel in February 2019.

Uncertainty remains high in the market due to supply side factors by some members of the Organisation of Petroleum Producing Countries (Opec) while demand remains robust.

Supply side challenges are mainly a result of sanctions on Iran by Washington and Venezuelan production challenges even though the US output of crude oil is expected to rise.

Maize, wheat, cotton and tobacco prices increased from 2016 to 2018 while the price of soya bean declined during the same period. World supplies will be influenced by major producers of the commodity and the after-effects of trade wars between major trade partners.

Zimbabwe External Sector

The country's external environment remains unfavourable due to excessive foreign currency obligations, which are far higher than receipts. For the past 10 years (2008 to 2018), the country's imports have exceeded exports by a massive US$29,4 billion. The country imports that can be substituted locally are estimated at 41,47 percent of the total import bill.

From a policy perspective, the country should consider adopting deliberate import substitution and local content policies to reduce the importation of products that can be produced locally while also strengthening local value chains.

The country's foreign currency receipts are dominated by exports, which account for over 60 percent of total receipts.

Remittances average 17 percent while foreign investment receipts are below one percent of gross domestic product.

Since the country is not receiving the required foreign currency, it should make efficient use of available foreign currency by allocating the export receipts towards critical areas as opposed to product lines that can be produced locally.

Regardless of the country's high-risk profile, Zimbabwe is still attracting significant offshore finance. This is essential in the re-industrialisation process.

For instance, the tobacco sector received 63 percent of the total loans applied for. This partly explains the upward trend in tobacco output, which reached 252 million kilogrammes (kg) in 2018.

Zimbabwe lagged behind in terms of attracting foreign direct investment (FDI), shown by declining inflows from 2014 to 2017 (US$545 million in 2014 to US$289 in 2017), compared to other countries such as Mozambique, South Africa, Zambia and Namibia.

Fiscal and Monetary Policy Measures

Over the years, government operated under fiscal imbalances, with expenditure consistently exceeding revenue.

Imbalances were financed through issuing of Treasury Bills (TBs), resulting in an increase in money supply, which was not backed by hard notes and coins. This further created cash shortages in the economy.

Government reformed tax systems in October 2018 to deal with the budget deficit by introducing a two percent electronic money transfer tax. Since its introduction, the collecting agency — the Zimbabwe Revenue Authority (Zimra) has surpassed targets, which is a positive development for the country.

The Reserve Bank of Zimbabwe (RBZ) noted the disparities which were in the market as a result of the fixed exchange rate of US$1: Bond$1 (1:1). This was below the parallel-implied rate of US$1: RTGS$$3.0/3.5.

To deal with the problem, the RBZ floated the exchange rate by introducing the interbank exchange market. The RTGS balances were converted into currency, the RTGS dollar, in order to establish an exchange rate between the monetary balances and foreign exchange rates.

The RTGS dollar became the base currency for reporting. In order to retain foreign currency from exporters for strategic imports for the nation, the RBZ introduced export retention thresholds. It also mobilised lines of credit with the view of increasing the supply of foreign exchange.

Inflation Developments

Annual inflation has been increasing since September 2018 from an average of 5,4 percent to 66,8 percent in March 2019.

Month-on-month inflation rose to 16,4 percent in September 2018 and has since taken a downward trend, falling to 9,2 percent in November 2018 and 1,67 percent in February 2019.

The cost of living for an average family of six has been on an upward trend since February 2018, increasing from $588 to $732 in December 2018. This was mainly caused by the multi-tier pricing system.

This is what was partially corrected by liberalising the exchange rate.

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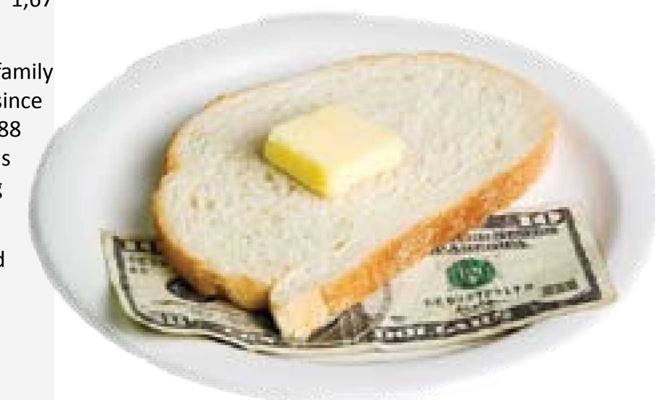


GLOBAL AND REGIONAL ECONOMIC DEVELOPMENTS

World ECONOMIC outlook update

Global economic growth is expected to slow to 2,9 percent in 2019 from three percent in 2018 due to the downside risks in the international environment, which include, inter alia, trade disagreements between leading global economies.

Such trade tensions among the World Trade Organisation (WTO) member countries are inevitable despite the Trade Facilitation Agreement (TFA) concluded at their Ninth Ministerial Conference held in Bali, Indonesia between December 3, 2013 and December 7, 2013 which became effective on February 22, 2017.

However, China and the US — the first and third to ratify the TFA on December 8, 2014 and January 23, 2015 respectively – have since been in direct trade war. Subsequently, the US exclusively imposed tariffs on Chinese products worth US$250 billion while China retaliated by setting tariffs on US$110 billion worth of the former's goods.

Furthermore, the US has threatened additional tariffs on US$267 billion worth of Chinese exports while China wants to retaliate with qualitative measures that would affect American businesses operating in the country. There are currently ongoing trade talks between the two countries.

Consequently, international trade flows and investment will be moderate, with financing conditions tightening, especially for developing countries or least developed countries.

Slow growth will emanate from episodes of financial stress and lost growth momentum from EMDEs.

Developing countries and emerging markets (China and India) are expected to stall growth at 4,2 percent this year due to downside risks, which have become more acute.

Growth in emerging and developing Asia will dip from 6,5 percent in 2018 to 6.3 percent this year.

Despite fiscal stimulus that offsets some of the impact of higher US tariffs, China's economy will slow due to the combined influence of financial regulatory tightening and trade tensions with the US.

India's economy is poised to pick up this year, benefiting from lower oil prices and a slower pace of monetary tightening than previously expected, as inflation pressures ease.

In sub-Saharan Africa, growth is expected to pick up from 2.9 percent in 2018 to 3.5 percent this year, mainly due to softening oil prices which have caused downward growth revisions for Angola and Nigeria.

Moderating activity and heightened risks are clouding global economic prospects, heavily affecting prospects of growth. The forecast slow growth for this year is expected to be the result of:

- Moderating activity and heightened risks;
- Trade wars between major world producers and markets;
- Financial stress and tightening of financing conditions;
- Softening international trade and investment;
- Substantial financial market pressure in some large EMDEs.

Economic activity in most advanced economies has been diverging of late.

However, growth in the US remains solid, bolstered by fiscal stimulus.

Growth in the Eurozone has been weaker than expected owing to slowing exports.

Poor world economic prospects will result in a weakening growth projection.

Summarised global economic growth developments and prospects for selected regions and countries are provided in Table 1

Table 1.1: Global and Regional Growth and Outlook (%)

	2016	2017	2018 Estimate	2019 Projection
World Output	2.4%	3.1%	3.0%	2.9%
Advanced Economies	1.7%	2.3%	2.2%	2.0%
US	1.6%	2.2%	2.9%	2.5%
Euro Area	1.9%	2.4%	1.9%	1.6%
Japan	0.6%	1.9%	0.8%	0.9%
Emerging Markets and Developing	3.7%	4.3%	4.2%	4.2%
China	6.7%	6.9%	6.5%	6.2%
India	7.1%	6.7%	7.3%	7.5%
Sub-Saharan Africa	1.3%	2.6%	2.7%	3.4%
South Africa	0.6%	1.3%	0.9%	1.3%
Zimbabwe*	0.6%	4.7%	4.0%	3.1%
Latin America and the Caribbean	-1.5%	0.8%	0.6%	1.7%
Brazil	-3.3%	1.1%	1.2%	2.2%
Mexico	2.9%	2.1%	2.1%	2.0%
Argentina	-1.8%	2.9%	-2.8%	-1.7%

*Zimbabwe growth rates are from ministry of Finance Treasury, RBZ and ZIMSTAT

Source: World Bank: Global Economic Prospects

ADVANCED ECONOMIES

Growth in advanced economies is forecast to drop to two percent this year. The growth forecast for the US also remains unchanged. US growth is expected to decline to 2.5 percent this year due to unwinding of fiscal stimulus and as the federal funds rate temporarily overshoots the neutral rate of interest.

Strong US domestic demand growth will support rising imports and contribute to a widening of the current account deficit. The Eurozone's growth is expected to fall to 16 percent from an estimated 1.9 percent in 2018, mainly due to a fall in export earnings emanating from a stronger euro, lower external demand and tighter monetary policy measures.

There is substantial uncertainty around growth in the United Kingdom due to the negative effects of prolonged uncertainty about the Brexit outcome and the positive impact from fiscal stimulus announced in the current (2019) budget. Japan's growth acceleration is expected to increase slightly by 0.1 percent from 0.8 percent estimated in 2018 to a projected 0.9 percent this year. This is mainly due to additional fiscal support to the economy this year, including measures to mitigate the effects of the planned consumption tax rate increase in October this year.

Causes of steady growth in many advanced economies are falling capacity and interest rate pressures emanating from withdrawal of monetary accommodation.

EMERGING AND DEVELOPING MARKETS

Growth for this group is anticipated to hold steady at a weaker than expected 4.2 percent this year. The steady prospect is mainly due to slowing external demand, rising borrowing costs and persistent policy uncertainties.

In China, activities remain high though downside risks are increasing. China's growth is projected to decline by 0.3 percent from an estimated

6.5 percent in 2018 to a projected 6.2 percent this year. Its economy will slow down due to the combined influence of financial regulatory tightening and trade tensions with the US. India is expected to have a positive growth from an estimated 7.3 percent to a projected 7.5 percent. Its economy is poised to pick up this year, benefiting from lower oil prices and a slower pace of monetary tightening than previously expected, as inflation pressures ease.

LATIN AMERICA AND THE CARIBBEAN

Economic growth in the region is projected to advance to 1.7 percent this year, supported mainly by a pickup in private consumption. Brazil is forecast to expand 2.2 percent, assuming fiscal reforms are quickly put in place and that a recovery of consumption and investment will outweigh cutbacks to government spending.

Mexico is expected to keep growth at two percent due to policy uncertainty and prospects of subdued investments.

Argentina is forecast for decline, with growth falling to 1.7 percent due to deep fiscal consolidation which will result in loss of employment and reduced consumption and investment.

SUB-SAHARAN AFRICA

Regional growth is expected to increase to 3.4 percent this year mainly from diminished policy uncertainty, improved investment in large economies and continued growth in non-resource intensive countries. Growth is also supported by firmer commodity prices.

However, potential downside risks such as public debt, financial sector strains and low external buffer are likely to hit many regional countries.

South Africa is projected to accelerate modestly to a growth rate of 1.3 percent due to constraints on domestic demand and limited government spending. Zimbabwe's growth rate, which significantly outpaced the average Sub-Saharan region's growth rate of 2.7 percent in 2018 by 1.3 percent, is likely to decline by 0.9 percent from four percent to 3.1 percent this year, below the regional average.

The negative growth prospects will be due to the contractionary impact of austerity measures (reduction in government expenditure), uncertainty in policy (monetary policy and fiscal policy reversals), economic reforms and drought prospects.

There is substantial uncertainty around growth in the United Kingdom due to the negative effects of prolonged uncertainty about the Brexit outcome and the positive impact from fiscal stimulus announced in the current (2019) budget.

International Commodity Prices

INTERNATIONAL commodity prices continue to influence global economic activities. Commodity prices are expected to stabilise this year following sharp movements last year (World Economic outlook, 2019).

However, escalating trade tensions between the US and China, including the imposition of tariffs on a range of products, have varying effects on metal and agricultural commodities. The recent US-China announcement of a temporary "truce" on tariff increases, and the announced reduction in Chinese tariffs on US car imports, are welcome steps toward de-escalating trade tensions. Final outcomes remain, however, subject to a possibly difficult negotiation process in the case of the US-China dispute.

This trade tension and policy uncertainties would lead to higher costs of imported intermediate and capital goods and higher final goods prices for consumers.

Beyond these direct impacts, there would be lower business investment, disruption of supply chains, and slow productivity growth. Zimbabwe, as a country that relies heavily on primary exports of metals (gold, platinum, chrome) and tobacco, is affected by reduced demand of its exports due to reduced productivity growth. This will adversely affect the country's mining operations, agricultural production, export receipts, mineral tax revenues and employment.

Precious metals (gold, platinum and diamonds) and industrial metals (nickel, chrome, tin) have been particularly responsive to these concerns, given their many uses in the manufacture of tradable goods.

Agricultural commodity prices (tobacco, maize, wheat, soya beans) were largely flat in 2018; they declined in the second half of the year, with developments varying by commodity.

Gold and Platinum prices

GOLD AND PLATINUM

METAL prices rose by six percent on average in 2018, which was less than predicted.

After increasing in the first half of 2018, the prices fell sharply in the second half following the imposition of broad-based tariffs by the United States on Chinese imports.

In addition, heightened trade tensions involving these economies have raised market concerns about global trade and investment prospects. This development has clouded the outlook for demand for commodities. Gold prices show an upward trend from 2016 to 2018 from US$1249 per ounce to US$1269.

Platinum slowed down from 2016 to 2018, showing a fall in price from US$987 to US$880 per ounce.Month-on-month prices for gold accelerated upwards from US$1 250 per ounce in December 2018 to US$1292 per ounce in January 2019. The prices maintained an upward trajectory to reach US$1320 per ounce in February this year.

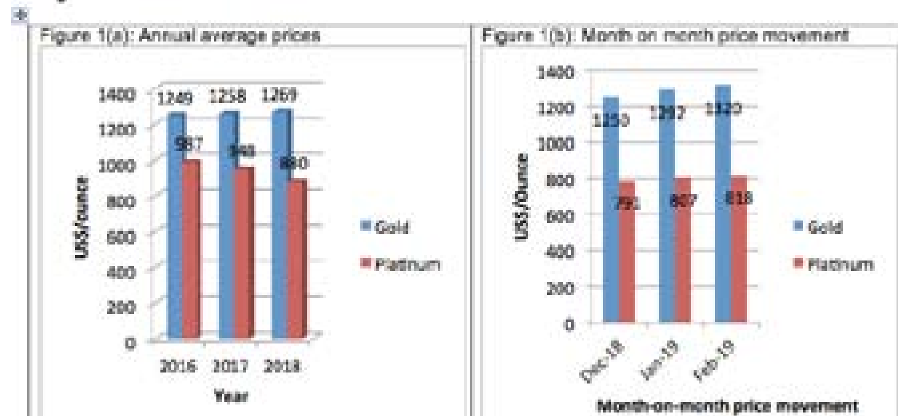
Implications for Zimbabwe

GOLD and platinum are major export minerals for Zimbabwe and account for a greater proportion of mineral tax revenue. Firming gold prices are a favourable development to both small scale and large scale producers. This has a positive effect on export receipts, employment and mineral tax revenue.

However, the retention policy from the monetary policy statement issued in February this year is likely to impact negatively on production and supply of gold to Fidelity Printers and Refiners – the only authorised gold buyer in Zimbabwe. It also promotes smuggling of the precious metal.

Falling prices of platinum will have serious effects on Zimbabwe's export receipts, tax revenues and employment. This, together with the foreign currency retention policy alluded to earlier, is likely to render the industry less viable.

Figure 1.1: Gold and Platinum Prices



Source: World Bank Commodities Price Data (March 4, 2019)

GLOBAL & REGIONAL DEVELOPMENTS

CRUDE OIL

CRUDE oil prices fluctuated markedly in the second half of 2018 with sharp declines towards the end of the year, mainly due to supply factors.

Oil prices averaged US$68,30 per barrel in 2018, a little lower than forecast but 30 percent higher than in 2017.

While global oil consumption contributed to this trend, supply side factors were the main drivers of price movements.

The continued decline in production in Venezuela and market concern over the impact of US sanctions on Iran contributed to this trend. The decline in prices also reflected rapid growth in oil production in the US, as well as a marked increase in supply by OPEC and the Russian Federation.

Oil prices are expected to average US$67/barrel this year. However, uncertainty is high due to supply factors by some OPEC countries (major supply sources for Zimbabwe).

Oil demand is expected to remain robust throughout the year but the expected loss in momentum across EMDEs could have a greater impact on oil demand than expected.

Considerable uncertainty remains about the full impact of sanctions on Iranian as well as the outlook for Venezuelan production. In the meantime, US output of crude oil is expected to rise this year.

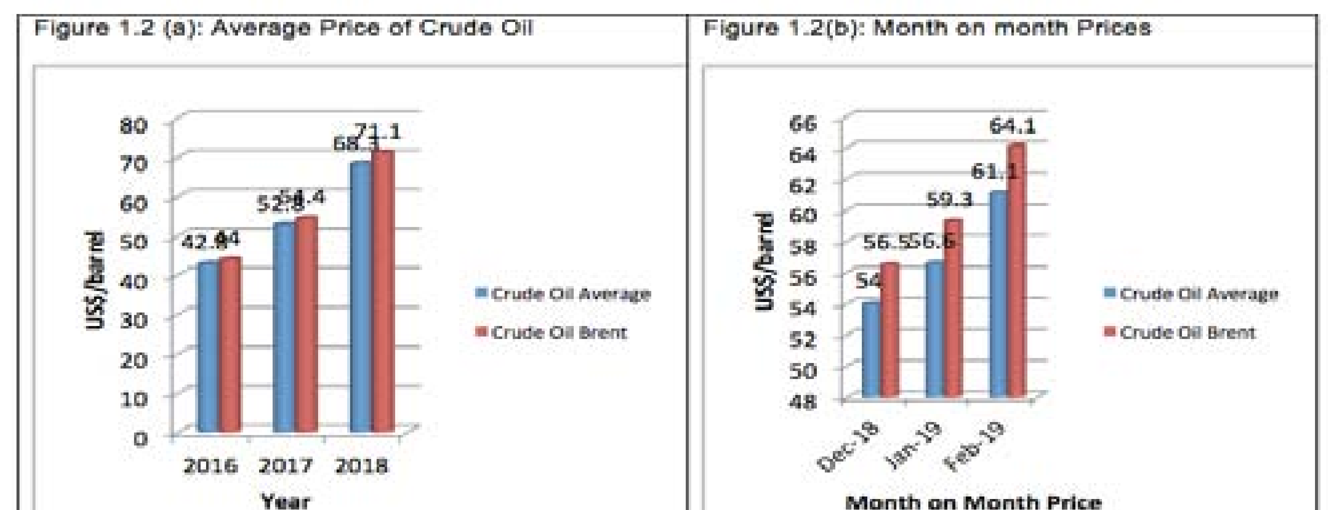
Implications for Zimbabwe

CRUDE oil is a strategic resource for the country as it drives the transportation of raw materials, movement of people and drives industrial machines.

An increase in the price per barrel has negative effects on the economy as it will cause prices of everything to go up. This increases the cost of doing business and the cost of living.

Given the current economic situation, characterised by rising prices across the board, an increase in price from the source market will worsen the situation.

Figure 1.2: World Average Prices of Crude Oil



Source: World Bank Commodities Price Data (March 4, 2019)

Maize and wheat prices

Table 1.2: World Average Prices

	Unit	Annual Average			Quarterly Averages					Monthly Averages		
		2016	2017	2018	Oct-Dec 2017	Jan-Mar 2018	Apr-Jun 2018	Jul-Sep 2018	Oct-Dec 2018	Dec 2018	Jan 2018	Feb 2018
Maize	$/mt	159.2	154.5	164.4	148.8	163.7	173.3	157.9	162.8	167.4	166.7	169.5
Wheat HRW	$/mt	166.6	174.2	209.9	179.8	192.2	215.7	222.4	209.4	211.3	209.8	219.0
Wheat SRW	$/mt	176.3	178.2	203.9	175.1	189.3	204.9	208.8	212.6	217.8	220.2	217.2
Soyabeans	$/mt	405	393	394	393	412	421	370	374	381	382	381
Cotton	$/kg	1.64	1.84	2.01	1.80	1.99	2.09	2.07	1.91	1.90	1.82	1.79
Tobacco*	$/kg	4.96	4.65	4.95	4.64	4.93	4.98	4.94	4.95	4.95	4.95	4.95

(US import prices converted from metric tonne of imports to price per kg)*

Source: World Bank Commodities Price Data (4 March 2019)

Implications for Zim

PRICES for Zimbabwe on most agricultural commodities were above the average world price mainly as an incentive to the farmer and the need to meet production costs which were high.

Zimbabwe received below normal rainfall in the 2018/19 season, which has turned out to be a drought, affecting output of most crops since local farmers largely depend on natural rains for their agricultural production. This also means that the quality of tobacco, which is the major export-crop, was compromised.

This will result in a shortage of maize and wheat. However, the falling international prices of maize are likely to benefit Zimbabwe in the face of a drought but the rise in wheat prices, coupled with the strengthening US dollar is likely to cause challenges in the importation of wheat given that Zimbabwe has introduced its own currency, the RTGS$, which is trading on the interbank market.

MAIZE prices accelerated from US$159,20 per metric tonne (MT) in 2016 to US$164.4o per MT in 2018. The soft red winter (SRW) wheat price increased from US$176,30 per MT in 2016 to US$203,90 per MT in 2018.

Hard red winter (HRW) increased from US$166,60 per metric tonne in 2016 to US$209,90 per MT in 2018. Wheat prices were slightly higher in 2018 as bad weather in Europe led to smaller harvests.

Estimates of the 2018-19 crop forecast have been raised for most commodities and high stock-to-use ratios for rice and wheat reduces the likelihood of a food price spike.

SOYA BEAN

Soya bean prices fell from US$405 per MT in 2016 to US$394 per MT in 2018. Soya bean prices in the US fell substantially following the announcement of tariffs by China on imports of US soya beans, while prices were higher in other countries such as Brazil.

The imposition of tariffs has led to trade diversion, with China's import of soya beans from the US declining by 25 percent while those from Brazil went up by 22 percent.

More recently, the gap in prices has since been closed as China has resumed purchases of US soya beans.

COTTON

Cotton prices increased from US$1,64 per kilogramme (kg) in 2016 to US$2,01 per kg in 2018. This is a favourable trend for Zimbabwe. However, world supplies are influenced by other major producers such as Egypt, Indonesia, Malawi, etc. The introduction of synthetic fibre is going to negatively affect the global demand for the white gold. On average, the monthly fall in prices is expected to reach US$1,79 per kg in February 2019 given that most producers are expecting to harvest the crop soon.

TOBACCO

Tobacco prices fluctuated between 2016 and 2018. They slowed from US$4,96 per kg in 2016 to US$4,64 per kg in 2017; then increased from US$4,64 per kg in 2017 to US$4,95 per kg in 2018: The prices averaging above US$4 per kg.

Review of ZIMBABWE'S external sector

THE country's external sector has largely remained under considerable pressure due to the demand for hard currency which has failed to match foreign currency inflows. This pressure is manifested through persistent and large trade and current account deficits that the economy has been recording since 2009. While exports of goods and services have been on an upward trend, this has been offset by the increase in imports of goods and services on the back of domestic supply gaps and rising international oil prices.

CURRENT ACCOUNT PERFORMANCE

Zimbabwe has since 2008 faced incessant trade deficits, which have accumulated to $29,451 billion. Each year, Zimbabwe's exports were roughly equal to 50 percent of imports.

This is not an ideal situation considering the fact that the country must realise trade surpluses that are necessary and sufficient for the stabilisation of currency under a dollarised environment.

Statistics from the International Trade Centre (ITC) show that the Southern African Development Community (Sadc) is the major source of Zimbabwe's imports with a share of 79 percent of total imports.

In 2018, Zimbabwe's major imports included mineral fuels ($1.5 billion), machinery ($467.8 million), cereals ($519 million), motor vehicles ($340 million), electricals ($263 million), iron and steel ($213 million), pharmaceuticals ($201.6 million), plastics ($181 million), animal and vegetable fats ($154 million), soya bean crude oil ($103 million) and fertiliser ($104 million). – *(UN COMTRADE, 2018).*

It is refreshing to note that exports surged up in 2018 by 55 percent. This is a clear testimony that Zimbabwe can generate export capacity ceteris paribus. Of concern though is the fact that the bulk of the country's exports, that is 87 percent, comprise of, among others, gold, flue-cured tobacco, ferrochrome, nickel, chrome and diamonds.

The largest foreign currency earners were gold ($1,030 billion), followed by tobacco ($892 million), nickel matte ($432 million), nickel ores and concentrates ($322 million), ferro-chromium ($207 million), chromium ores and concentrates ($81 million). – *(UN COMTRADE, 2018).* Consistently, trading statistics show that there are a number of lines which the country has been importing whose import values seem insignificant as single products but become very significant when combined.

As shown in table 2.2, these products make up $2.152 billion, that is, 41.7 percent of total imports, which can be substituted.

Table 2.1: Zimbabwe Trade Performance (2008 - 2018) (US $Billion)

Total Annual Imports from WTO Member States										
2008	*2009*	*2010*	*2011*	*2012*	*2013*	*2014*	*2015*	*2016*	*2017*	*2018*
2.832	3.527	5.852	8.599	7.363	7.704	6.380	6.002	5.212	5.437	5.189
Total Annual Exports with WTO Member States										
2008	*2009*	*2010*	*2011*	*2012*	*2013*	*2014*	*2015*	*2016*	*2017*	*2018*
1.694	2.269	3.199	3.512	3.882	3.507	3.064	2.704	2.832	3.556	4.265
Total Annual Trade Balance with WTO Member States										
2008	*2009*	*2010*	*2011*	*2012*	*2013*	*2014*	*2015*	*2016*	*2017*	*2018*
(1.138)	(1.258)	(2.653)	(5.087)	(3.480)	(4.197)	(3.316)	(3.298)	(2.379)	1.881	0.7625
										29.451

Source: UN COMTRADE (2019)

Table 2.2: Zimbabwe Major Imports Which Can be Substituted

HS Code	Product Description	$ Million
'10	Cereals	519
'30	Pharmaceutical products	303
'15	Animal or vegetable fats and oils and their cleavage products; prepared edible fats; animal ...	188
'72	Iron and steel	213
'31	Fertilisers	85
'48	Paper and paperboard; articles of paper pulp, of paper or of paperboard	81
'23	Residues and waste from the food industries; prepared animal fodder	78
'40	Rubber and articles thereof	67
'33	Essential oils and resinoids; perfumery, cosmetic or toilet preparations	60
'28	Inorganic chemicals; organic or inorganic compounds of precious metals, of rare-earth metals, ...	47
'34	Soap, organic surface-active agents, washing preparations, lubricating preparations, artificial ...	45
'11	Products of the milling industry; malt; starches; inulin; wheat gluten	41
'21	Miscellaneous edible preparations	38
'99	Commodities not elsewhere specified	35
'19	Preparations of cereals, flour, starch or milk; pastrycooks' products	30
'22	Beverages, spirits and vinegar	30
'29	Organic chemicals	30
'12	Oil seeds and oleaginous fruits; miscellaneous grains, seeds and fruit; industrial or medicinal ...	25
'17	Sugars and sugar confectionery	22
'03	Fish and crustaceans, molluscs and other aquatic invertebrates	21
'36	Explosives; pyrotechnic products; matches; pyrophoric alloys; certain combustible preparations	20
'63	Other made-up textile articles; sets; worn clothing and worn textile articles; rags	20
'96	Miscellaneous manufactured articles	20
'20	Preparations of vegetables, fruit, nuts or other parts of plants	20
'82	Tools, implements, cutlery, spoons and forks, of base metal; parts thereof of base metal	18
'76	Aluminium and articles thereof	18
'70	Glass and glassware	17
'44	Wood and articles of wood; wood charcoal	17
'94	Furniture; bedding, mattresses, mattress supports, cushions and similar stuffed furnishings; ...	17
'55	Man-made staple fibres	16
'24	Tobacco and manufactured tobacco substitutes	15
'07	Edible vegetables and certain roots and tubers	14
'04	Dairy produce; birds' eggs; natural honey; edible products of animal origin, not elsewhere ...	14
'64	Footwear, gaiters and the like; parts of such articles	13
'08	Edible fruit and nuts; peel of citrus fruit or melons	10
'83	Miscellaneous articles of base metal	10
'49	Printed books, newspapers, pictures and other products of the printing industry; manuscripts, ...	10
'68	Articles of stone, plaster, cement, asbestos, mica or similar materials	10
'35	Albuminoidal substances; modified starches; glues; enzymes	9
'61	Articles of apparel and clothing accessories, knitted or crocheted	8
'02	Meat and edible meat offal	7
'62	Articles of apparel and clothing accessories, not knitted or crocheted	6
'01	Live animals	5
'09	Coffee, tea, maté and spices	5
'52	Cotton	2
	Total	2,152
		41.47 %

Source: UN COMTRADE (2019)

WHAT is apparent is that Zimbabwe, for a number of decades, has been importing these products consistently. Against this background, from a policy perspective, the country should consider the following policy measures:

(a) Deliberate import substitution policy targeting imports which can be produced locally, that is, agricultural produce (cereals, vegetables, mushroom, etc) and manufactured produce (such as pharmaceuticals, fertilisers, paper, tooth picks, pampers, chewing gums, etc)

(see table 2.2);

(b) Related to the import substitution strategy, there is need for a funded industrialisation strategy targeting the imports identified in (a);

(c) Deliberate local content policy aimed at strengthening local value chains and operationalisation of value chain finance models through the creation of an enabling environment for business to support backward and forward linkages;

In addressing challenges linked to a low and narrow export base, the following measures are recommended:

(a) There is need for the country to build export capacity by investing in the traditional export lines, which are largely concentrated in the agro-processing industries, horticulture and minerals. This requires investment in retooling and full utilisation of resources like land.

Specifically in agriculture, government should promote joint ventures between white commercial farmers and resettled farmers. In this regard, lessons can be drawn from the Agricultural and Rural Development Authority (Arda);

(b) There is need for investment into factories with a view of promoting value addition and beneficiation to change the trajectory from exporting primary goods to exporting processed and finished goods.

This requires targeted investment campaigns for such specific projects which are aimed at our current export lines currently going out of the country as raw materials. The current work on special economic zones should consider designation of specific zones that are aimed at value addition and beneficiation;

(c) There is need for the implementation of the National Export Strategy developed by the Ministry of Industry and Commerce with a view to ramping up exports to traditional and non-traditional markets.

> "There is need for investment into factories with a view to promoting value addition and beneficiation with a view of changing the trajectory from exporting primary goods to processed and finished goods.

DOMESTIC ECONOMY

Foreign Currency Receipts

AS NOTED by the RBZ (2019), global foreign currency receipts into the economy for the period January to December 2018 amounted to US$6,3 billion compared to US$5,5 billion received during the same period in 2017, representing a 13.9 percent increase in foreign currency supply.

Table 2.3 shows global foreign currency receipts by source. Export proceeds contributed 68 percent of the total global receipts for the 52 weeks of 2018, while international money transfers accounted for about 17 percent.

Export proceeds have continued to be the major source of liquidity for the country.

International remittances declined by 19 percent from US$1.4 billion received in 2017 to US$1.1 billion received in 2018.

Of the US$1.4 billion, Diaspora remittances contributed US$619.2 million, a decline of 114 percent compared to US$699 million received in 2017 (RBZ, 2019).

The RBZ noted that the decline in Diaspora remittances is mainly attributed to the preference to send in-kind remittances by Zimbabweans in foreign lands, and the interception of remittances in South Africa by cross-border traders.

This has been a major contributor considering that South Africa contributes about 34 percent of the total Diaspora remittances.

Zimbabwe should work towards improving efficient use of foreign currency and endeavour to allocate foreign currency towards critical areas as opposed to products which can be produced locally.

Table 2.3: Global Foreign Currency Receipts (USD million)

Type of Receipt		Week 52 2018	% Contribution	Week 52 2017	% Contribution	% Change
Export proceeds		4,264.7	68%	3,556.2	64%	19.9%
International Remittances	Diaspora	597.4	9%	695.3	13%	-14%
	NGOs	530.4	8%	682.5	12%	-22%
Loan Proceeds		826.1	13%	533.5	10%	55%
Income Receipts		59.3	1%	57.0	1%	4%
Foreign Investments		22.8	0%	25.4	0%	-10%
Total		**6,300.7**	**100%**	**5,549.9**	**100%**	**13.5%**

Source: Exchange Control Records and Bank Supervision Application System (BSA)

Private Sector Debt

In the year 2018, Exchange Control approved and registered a total of 140 external loan facilities with a monetary value of US$1.28 billion. A three percent increase in the total approvals from the US$1.23 billion recorded in 2017 was observed as shown by the table below.

Table 2.4: External Loan Approvals per Sector

Sector	2017 Facility Approvals (US$)	2018 Facility Approvals (US$)	Variance (US$)	Variance (%)
Agriculture	828,165,567	801,593,999	-26,571,568	-3%
Financial	38,106,000	204,370,000	166,264,000	81%
Tourism & Hospitality	4,261,000	14,137,800	9,876,800	70%
Services	30,335,000	12,386,608	-17,948,392	-100%
Energy	252,444,000	40,615,000	-211,829,000	-100%
Retail & Distribution	37,187,879	356,225	-36,831,654	-100%
Mining	40,211,940	114,126,237	73,914,297	65%
Manufacturing	4,104,590	88,264,140	84,159,550	95%
Transport	931,797	5,421,652	4,489,855	83%
Construction	3,850,395	1,774,195	-2,076,200	-117%
TOTAL	**1,239,598,168**	**1,283,045,857**	**43,447,689**	**3%**

Source: External Loans and Exchange Control Review Committee Database

The sectoral spread of borrowings improved in 2018, with sectors such as Finance, Manufacturing, Tourism and Transport recording more than 50 percent increase in monetary value and number of facilities from 2017. Overall, tobacco finance facilities dominated the loans with a 63 percent contribution.

2.4 Actual External Loan Drawdowns

IN THE year 2018, loans amounting to US$844,9 million were advanced by financial institutions. It should be noted, however, that this figure includes drawdowns from facilities that were approved in previous years.

It is refreshing, however, to note that the country, regardless of its high risk profile, is still attracting significant offshore finance which is key in its industrialisation process.

Tobacco, which received 63 percent of the total loans, is a testimony to the effectiveness of finance to stimulating production.

Since the beginning of the land reform, tobacco output has been on an upward trend and in 2018 it reached 252 million kgs as noted by the Tobacco Industry and Marketing Board (2018). This clearly shows a positive causal link between finance and production.

Going forward, the reform agenda being spearheaded by government under the Transitional Stabilisation Programme (TSP) is critical in creating an enabling environment for capital to favour Zimbabwe.

The fiscal and monetary measures announced by the ministry of Finance and Economic Development and the RBZ are expected to give further impetus to the economy, which is key for attracting investments (see section on review of fiscal and monetary policies).

Foreign Direct Investments

OVER the years, Zimbabwe lagged behind with respect to attracting FDI compared to its regional peers.

Figure 2.1 shows that for the last 10 years, Zimbabwe failed to exceed the US$500 million mark in terms of FDI while countries such as South Africa, Mozambique and Zambia exceeded US$9 billion, US$6 billion and US$2 billion respectively (see figure 2.1).

The World Bank (2018) has identified the following as major constraints impeding investment in Zimbabwe:

(a) Red tape and corruption;

(b) Excessive administrative and registration requirements;

(c) Tax burden;

(d) Weak institutions;

(e) Political instability;

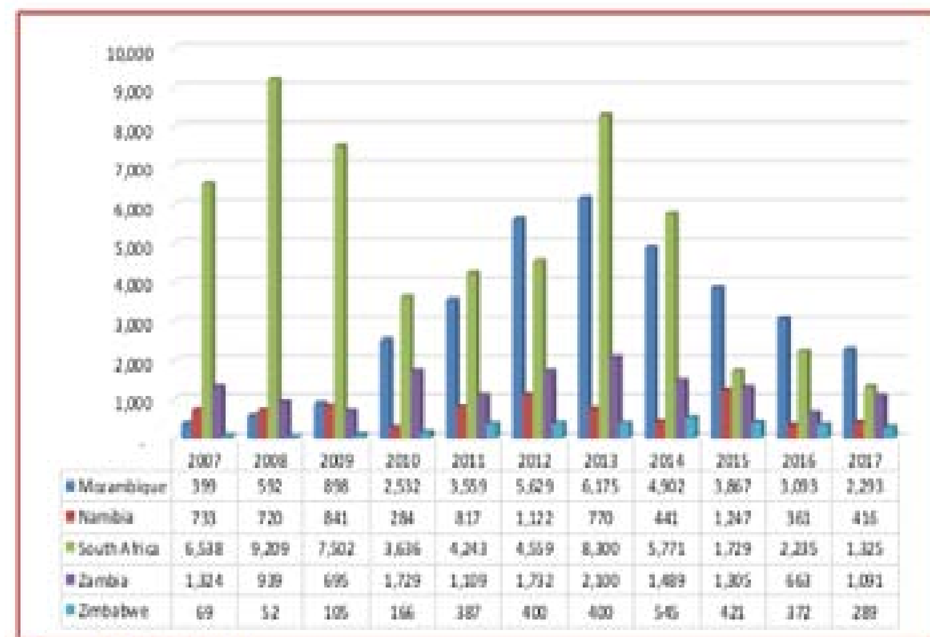
(f) Economic instability;

(g) Lack of policy clarity, policy reversals and policy inconsistencies;

Going forward, within the context of the TSP, fiscal and monetary policy measures must expedite full implementation of policy measures spelt out in these policy frameworks.

The mantra that "Zimbabwe is open for business", must be judiciously applied, whether in economics or politics.

Figure 2.1: Regional Comparisons of FDI



	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Mozambique	399	592	898	2,532	3,559	5,629	6,175	4,902	3,867	3,093	2,293
Namibia	733	720	841	284	817	1,122	770	441	1,247	361	416
South Africa	6,538	9,209	7,502	3,636	4,243	4,559	8,300	5,771	1,729	2,235	1,325
Zambia	1,324	939	695	1,729	1,109	1,732	2,100	1,489	1,305	663	1,091
Zimbabwe	69	52	105	166	387	400	400	545	421	372	289

Source (UNCTAD, 2018)

Review of FISCAL and monetary policy measures

ZIMBABWE has twin problems, which are trade imbalances (trade deficits) and fiscal imbalances (budget deficits). These twin problems are a result of one fundamental problem, that is, low production.

As noted earlier, Zimbabwe's trade deficit has accumulated to $32,15 billion over the past 10 years.

From a fiscal perspective, government expenditure consistently exceeds revenue thereby creating budget deficits, which are financed by TBs.

As noted by the ministry of Finance and Economic Development, the issuance of TBs increased from US$2,1 billion in 2016 to a cumulative US$6.2 billion by the end of August 2018 (ministry of Finance and Economic Development, 2019).

In 2014, TBs to gross domestic product (GDP) ratio was at 4.4 percent and had increased sharply to 36.5 percent by end of August 2018.

In the same vein, the overdraft with the central bank stood at US$2.3 billion (as at end of August 2018) and was expected to close the year at $2.5 billion by end of 2018, well above the statutory limit of US$762.8 million as provided under Section 11(1) of the Reserve Bank Act (Chapter 22:15) which requires that central bank lending to the State, at any time, shall not exceed 20 percent of the previous year's government revenue (Ministry of Finance and Economic Development, 2019).

This resulted in a rapid increase in money supply not sufficiently backed by hard notes and coins hence the cash challenges.

To date, the high deficit has ignited expansion of domestic debt from US$275.8 million in 2012 to current levels of US$9.5 billion against US$7.4 billion external debt (Ministry of Finance and Economic Development, 2019).

This brings total public debt to US$16.9 billion and is likely to violate the provision of Section 11(2) of the Public Debt Management Act (Chapter 22:21), which stipulates that the total outstanding Public and Publicly Guaranteed Debt as a ratio of GDP should not exceed 70 percent at the end of any fiscal year (Ministry of Finance and Economic Development, 2019).

This requirement is, however, far above the 60 percent SADC threshold, to which Zimbabwe assented to through ratification of the Finance and Investment Protocol. This, by itself, is a clear sign of fiscal indiscipline.

However, the incessant budget deficits have resulted in rampant increase in money supply, creating a significant mismatch between RTGS balances and hard notes and coins available hence soaring rates on the parallel market.

As noted by the RBZ (2019), broad money supply increased from $8 billion in December 2017 to $10.1 billion in January 2019 (RBZ, 2019).

With respect to exchange rate developments, the country witnessed foreign exchange (forex) premiums on the parallel market, which ranged from 1.40 to 1.80 to the US dollar in September 2018; this increased to the current levels of between 3.00 to 4.00 (RBZ, 2019).

This movement in forex premiums has had negative pass-through effects on inflation, which increased particularly from the September year-on-year level of 5.4 percent to 20.9 percent in October and closed the year at 42.09 percent and further rose to 59 percent in February 2019 (RBZ, 2019).

REVIEW OF FISCAL POLICY MEASURES

In dealing with budget deficits, which were noted to be one of the major impediments to financial sector stability, the minister of Finance and Economic Development Mthuli Ncube committed, in his 2019 budget statement, to limit the use of the RBZ overdraft facility and curtail RBZ advances to government in line with Section 11(1) of the Reserve Bank Act (Chapter 22:15), which states that borrowing from the apex bank shall not, at any given point, exceed 20 percent of the previous year's government revenue (ministry of Finance and Economic Development, 2019).

Government introduced intermediated money transfer tax from five cents per transaction to two cents per dollar transacted, effective October 1, 2018 (ministry of Finance and Economic Development, 2018).

This effectively means that Treasury is taxing two percent of every dollar transaction as opposed to five cents per transaction (averaging $80 million per month).

Further, in the 2019 national budget statement, government came up with various revenue enhancement as well as expenditure containment measures with a view of reining in the budget deficit to five percent of GDP.

These measures include:

- Remitting of all revenue collected into the Consolidated Revenue Fund with a view of upholding the principle of transparency and accountability in the utilisation of public resources by government ministries and departments;
- In dealing with the violation of the penalties under the Public Finance Management Act, the budget is working on penalties for financial misconduct by public officers ranging from fines, to imprisonment, or both. This move will help in reining in bad behaviour in government and wastefulness as noted by a record unbudgeted $2.3 billion budget deficit, which was spent in 2018;
- Payment of tax in the currency of trade will help government to cash in on forex.

These measures, if adhered to, will result in government closing the tap on budget deficit, which is critical in reducing money supply.

Finance minister Mthuli Ncube

Monetary Policy Measures

The RBZ noted that the current pricing structure, largely dominated by electronic money and bond notes at an implied parallel market exchange rate of around 3.0 to 3.5 to the USD, has created a plethora of challenges to the transacting public. The challenges include, inter alia, multi-tier pricing by business, speculative pricing, loss of government revenue, valuation and accounting difficulties, asset-liability mismatches and negative investor confidence.

Undoubtedly, if the current monetary arrangements are maintained they could pose the risk of a costly re-dollarisation of the economy, which would naturally move the economy into a recession (RBZ, 2019).

Already, the country has witnessed some businesses gradually reducing prices due to low demand in the economy. In the same vein, evidence shows that some market players that were charging prices in foreign currency experienced reduced demand for their products and were forced to revert back to pricing in RTGS and/or bond notes.

After taking into account the foregoing and the implications as well as putting in place safeguards to maintain stability in the forex market, the RBZ established in February 2019 an inter-bank foreign exchange market with a view of formalising the trading of RTGS balances and bond notes with US dollars and other currencies on a willing-buyer willing-seller basis through banks and bureaux de change under the following framework:

(a) Denominating the existing RTGS balances, bond notes and coins in circulation as RTGS dollars in order to establish an exchange rate between the current monetary balances and foreign currency.

(b) The RTGS dollars have become part of the multi-currency system in Zimbabwe. The legal instrument to give effect to this has been prepared.

(c) The RTGS dollars shall be used by all entities (including government) and individuals in Zimbabwe for the purposes of pricing of goods and services, record debts, accounting and settlement of domestic transactions.

(d) The use of RTGS dollars for domestic transactions will eliminate the existence of the multi-pricing system and charging of goods and services in foreign currency within the domestic economy. In this regard, prices should remain at their current levels and or decline in sympathy with the stability in the exchange rate given that the current monetary balances have not been changed. In this respect, the RBZ will commit all its efforts to use the instruments at its disposal to maintain stability of the exchange rate.

(e) The bank has arranged sufficient lines of credit to enable it to maintain adequate hard currency to underpin the foreign exchange market. This is essential to restore the purchasing power of RTGS balances by safeguarding price stability emanating from the pass-through effects of exchange rate movements.

(f) Foreign currency from the inter-bank market shall be utilised for current bona fide foreign payments except for education fees.

(g) All foreign liabilities or legacy debts due to suppliers and service providers such as the International Air Transport Association (IATA), declared dividends, etc shall be treated separately after registering such transactions with Exchange Control for the purposes of providing the bank with sufficient information that will allow it to determine the roadmap for expunging the legacy debt orderly.

(h) Foreign currency requirements for government expenditure and other essential commodities that include fuel, cooking oil, electricity, medicines and water chemicals shall continue to be made available through the existing letters of credit facilities and/or the Foreign Exchange Allocations Committee.

(i) Banks shall report activities of the inter-bank foreign currency market to the RBZ that shall closely monitor the foreign currency trades on a daily basis using the form and format stipulated by the central bank.

(j) Bureaux de change shall be authorised to purchase foreign currency without limits but shall be limited to sell foreign currency for small transactions such as subscriptions, business and personal travel up to a maximum aggregate daily limit of US$10 000 per bureau de change. Like with banks, bureaux de change and their agents shall report their activities of the inter-bank on a daily basis as required by the RBZ.

(k) In order to allow exporters to benefit from the inter-bank foreign currency market and to promote uninterrupted supply of foreign currency in the economy, the export retention thresholds which are in line with regional practice shall be as follows (See Table 3.1):

1. Similarly, in order to enhance liquidity within the foreign currency market, exporters shall be entitled to utilise their retained export receipts within 30 days, after which the unutilised export receipts will be off-loaded into the market at the prevailing market exchange rate.

2. All international remittances and individual funds received from offshore shall continue to be treated as free funds.

3. To anchor price stability, the central bank shall aggressively intervene in the market to sterilise liquidity so as to help contain inflationary and exchange rate pressures. The central bank will also implement a monetary targeting framework, with monetary aggregates as operational targets for monetary policy. Under this framework, the bank will appropriately target growth in base money with a view to helping stabilise and anchor macroeconomic stability.

The existing monetary policy instruments, including continued issuance of savings bonds and changes in the statutory reserve requirements, will be instrumental in achieving the reserve money target.

The fiscal stance taken by government to reduce recourse to the central bank overdraft and to limit the overdraft to statutory levels will provide further impetus on the central bank's ability to contain pressures in the goods and foreign exchange market.

Table 3. 1: Current and Proposed Retention Thresholds

Sector	Level (%)
Manufacturing	80
Gold (Large scale producers)	55
Gold (Small scale producers)	55
All other minerals	50
Tobacco & cotton merchants (for inputs schemes)	80
Tobacco and cotton growers	30
Horticulture	80
Transport	80
Tourism	80

Source: Reserve Bank of Zimbabwe (2019)

Rationale of LIBERALISING exchange rate

The exchange rate of 1:1 between the US dollar and RTGS currency undoubtedly created a number of problems ranging from creation of opportunities for rent-seeking behaviour such as corruption and arbitrage opportunities emanating from distortions.

By liberalising the exchange rate, the RBZ wiped away the possibilities of these ills. In the same vein, the 1:1 rate presented competitiveness and viability challenges for exporters.

For example, in the mining sector, 50 percent of total exports were retained by the RBZ and liquidated at a rate of 1:1 in an environment where the parallel market rate was 1:3.2.

This did not make economic sense.

By liberalising the exchange rate, the competitiveness of the export sector is expected to significantly improve.

As expected in international finance, a fixed exchange arrangement repels FDI as well as inflows of remittances. It is therefore hoped that this new move will give positive impetus as the country seeks to attract investors.

At a rate of 1:1, government was certainly at a disadvantage when it came to collection of customs revenue because the cost of imports in USD were accounted for at a rate of 1:1 thereby prejudicing government of fiscal revenue.

Under the new arrangement, one expects to see duties being calculated using the prevailing exchange rate. This is expected to drive fiscal revenue upwards.

For listed companies, it was not possible to present financial reports using parallel market rates; they had to stick to the official rate of 1:1.

This situation created a false impression on the real value of the company. Now this new arrangement makes it easier for the firms to showcase the true value of their net worth.

THE IMPLICATIONS OF MONETARY POLICY STATEMENT AND OUTLOOK

The recently announced monetary policy statement stands to provide positive effects on the economic front if the possible risks, which are associated with fiscal indiscipline, are eliminated.

The risks arise on the backdrop of the fact that, to date, there is about $10 billion in broad money supply made up of TBs, loans, savings bond and money in circulation.

The amount of money in circulation (available for use), according to the RBZ, amounts to $1.8 billion, that is, $437 million bond notes, $87 bond coins (giving a total figure of $524 million cash) and $1.276 billion in RTGS.

The remaining balance of $8.2 billion is in TBs, savings bonds and loans hence will not exert pressure on the exchange rate.

It is not expected that the available liquidity of $1.8 billion will be used to purchase foreign exchange as some economic agents will be using the money to pay for usual transactions such as salaries, fees, fuel, etc.

The risks, which may arise here come, on the back of the maturity of TBs as well as budget deficits (due to increasing pressure to raise salaries and other unbudgeted for expenditures), which may raise demand for foreign currency thereby causing sharp rises in the exchange rate.

On a refreshing note, the Minister of Finance has been on record that he will close the tape on budget deficits as well as managing TBs with a view of controlling money supply. The minister's stance was eloquently covered in his budget statement.

With respect to safety nets, the RBZ has promised to allocate sufficient amounts of foreign exchange mobilised from lines of credit and foreign exchange retention to stabilise the exchange rate through its participation on the market. This is very critical as it will keep the exchange rate in check.

Other important safety nets relate to the directive that 70 percent of the foreign currency must be allocated towards productive requirements and limit the sale of foreign exchange by bureaux de change to a maximum of $10 000 per day.

These measures will help in financing the productive sector with a view of generating foreign currency and at the same time helping in minimising abuse of forex.

With respect to price dynamics, in the short run, prices are likely to go up on the back of exchange rate pressure, pressure on wages and salaries as well as inflation.

However, in the medium term, it is expected that prices will stabilise and self-correction will take place, if and only if, government continues to provide safety nets as well as minimise the risks which come with fiscal pressures. From a trade perspective, the new exchange rate management system will address market distortions and give incentives to exporters and investors. Furthermore, the fair alignment of the exchange rate is set to trigger an expenditure switching effect across the economy which will benefit local producers, thereby limiting imports of consumptive goods and services.

Similarly, the measures are set to encourage export growth as the market determined exchange rate improves external competitiveness of domestic producers that include tobacco and cotton growers.

Notwithstanding the possible setbacks which are likely to come on the back of fiscal pressures and erosion of safety nets and political tension, it looks like guarantees put in place by the governor of the RBZ John Mangudya as well as the Minister of Finance give rise to a better economic outlook.

Monetary and Financial Sector Developments

GENERALLY, annual growth in money supply has been on a downward trend since July 2018, largely reflecting the slowdown in accommodation to government, fiscal consolidation, as well as central bank efforts to mop up excess liquidity from the market.

Liquidity sterilisation efforts through the RBZ's savings bonds have continued to bear fruit, mopping up a total of $1,96 billion worth of liquidity since their introduction in September 2017.

MONEY SUPPLY GROWTH

As noted by the RBZ, broad money supply increased from $8 billion in December 2017 to $10,1 billion in January 2019 (RBZ, 2019).

However, of concern is the fact that the country's money supply is dominated by transitory deposits, as evidenced by its composition by end of November 2018, where transferable deposits were 80,45 percent of total broad money; time deposits 14.17 percent; currency in circulation 4.88 percent; and negotiable certificates of deposits 0.50 percent.

This short term money does not augur well for investment as it falls short of the medium to long term credit requirements of most industries, which need re-tooling, refurbishment and new capital investment.

CAPITALISATION

THE banking sector remained adequately capitalised with average tier 1 and capital adequacy ratios of 23,84 percent and 30,27 percent respectively.

The banking sector aggregate core capital increased by 15,32 percent, from $1,37 billion as at December 31, 2017 to $1,58 billion as at December 31, 2018, largely due to organic capital growth.

All banking institutions were compliant with the prescribed minimum capital requirements. See table 4.1). However, the question which arises is whether the minimum capital requirement of $25 million is still relevant in the context of the new monetary policy measures, which have seen the exchange rate being liberalised.

In the context of vulnerabilities, which may come with exchange rate movements, it is therefore important for the banking institutions to implement capital preservation strategies.

PERFORMANCE OF THE BANKING SECTOR

The banking sector remained generally stable as reflected by adequate capitalisation and improved earnings performance for the period ended December 31, 2018.

However, as noted in table below, asset quality deteriorated as reflected by the increase in the average non-performing loans to total loans ratio during the period under review. This implies that there is a high default risk, which the banking sector should monitor closely. The table below shows trends in financial soundness indicators. Table 4.1

Developments on the ZSE

THE year 2018 saw the (Zimbabwe Stock Exchange) ZSE experiencing generally bullish sentiment, with the industrial and mining indices rising from 333.02 points and 142.40 points respectively, at the end of December 2017, to 699.89 points and 242.81 points in October 2018.

The growth was partly attributed to strong performance on some blue-chip counters, coupled with hedging tendencies against perceived losses of value on parallel market rates and inflation.

Although activity on the stock market declined in December 2018 in line with trends during the festive season, both the industrial and mining indices grew significantly by 46.28 percent and 59.91 percent respectively. The Top 10 Index, which tracks share price developments of wealth preserving counters, gained 45.02 percent to reach 145.02 points at the end of 2018.

By breaking the 100 points benchmark, it implies that blue-chip stock prices at 31 December 2018 have surpassed prices at the beginning of the year, when the index was introduced.

Table 4.1: Indicators of Financial Soundness

Key Indicators	Benchmark	Dec-17	Jun-18	Sept-18	Dec-18
Total Assets		$11.25bn	$12.35bn	$13.31bn	$13.98bn
Total Loans & Advances		$3.80bn	$4.08bn	$4.00bn	$4.22bn
Net Capital Base		$1.58bn	$1.61bn	$1.72bn	$1.83bn
Total Deposits		$8.48bn	$9.53bn	$9.57bn	$10.32bn
Net Profit		$241.94m	$176.09m	$283.98m	$389.85m
Return on Assets		2.61%	1.75%	2.61%	4.57%
Return on Equity		15.48%	11.16%	16.80%	20.59%
Capital Adequacy Ratio	12%	27.63%	26.32%	27.79%	30.27%
Loans to Deposits	70%	44.81%	43.53%	41.8%	40.71%
Non-Performing Loans Ratio	5%	7.08%	6.22%	6.69%	8.39%
Tier 1 Ratio	8%	23.97%	24.16%	22.68%	23.84%
Liquidity Ratio	30%	62.62%	68.45%	70.66%	68.00%
Cost to Income Ratio		75.36%	67.59%	66.85%	70.01%

Source: RBZ

DOMESTIC ECONOMY

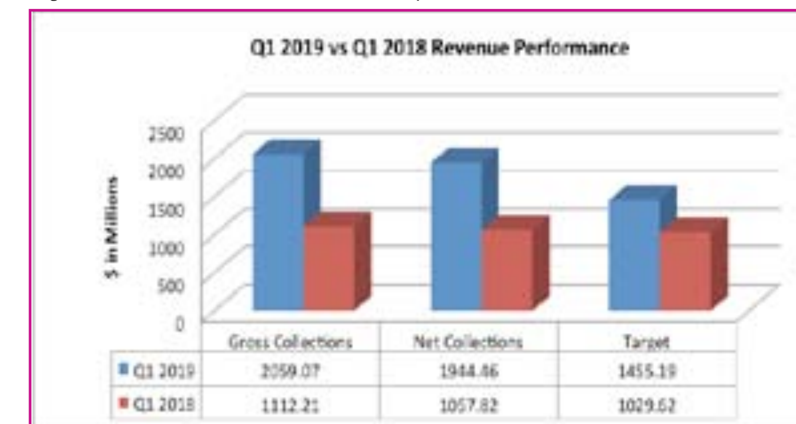
Fiscal Developments

THE fiscal challenges associated with government budget deficit have been overturned for Zimbabwe.

The government Consolidated statements of financial performance have revealed a strong positive variance between revenues and expenditure, reflecting a healthier position for the economy.

According to the ministry of Finance and Economic Development (2019), the revenue performance for the first quarter of 2019 surpassed the set target.

Figure 4.2: 2019/2018 Revenue Comparison



Source: Ministry of Finance and Economic Development (2019)

Gross collection amounted to $2.05907 billion against a target of $1.45519 billion which is a 41.5 percent increase. Net collections were $1.944 billion against a target of $1.45519 billion showing a positive increase of 33.6 2 percent .

Net collections are figures obtained after deducting refunds. Comparing 2019 to 2018 for the same quarter, gross collection has grown by 85.13 percent and net collections reported a growth of 83.82 percent.

These positive performances in revenue collections are attributed to the Intermediate Money Transfer Tax (IMTT) introduced in October 2018 and the improved effort by Zimra in promoting compliance.

Positive performances were also reflected on the monthly collections for the first quarter of 2019 (January to March) as portrayed in figure below. Net collections for January were $516.99 million in 2019 compared to $336.99 million in 2018.

For the month of February, collections increased to $558.74 million in 2019 compared to $316.84 in 2018 and in March, the collections increased to 4866.99 in 2019 compared to $403.93 million in 2018.

Figure 4.2.1: Comparison on Monthly Collections 2019 vs 2018

SOURCE: Zimra

Given revenue inflows of $516.99 million against a total expenditure of $385 million for January 2019, Treasury managed to have a record surplus of $131.99.

Expenditure in February amounted to $521 million against a target of $505.7 million, but the government covers this from the collections of $558.74 million.

Employment expenditure was $233,4 million against a budget target of $231 million, representing over expenditure $2,4 million. Expenditure on capital programmes amounted to $7,3 million against a target of $47,1 million, representing under expenditure of $39.8 for the period.

Inflation Developments

Annual headline inflation, which had been largely trending below five percent for the greater part of 2018, spiked to 21 percent in October 2018 and further to 42.1 percent, 56.9 percent and 59.39 percent in December 2018, January 2019 and February 2019 respectively as inflation pressures built up in the economy.

As noted by the RBZ, the price hikes, which were largely defined in October, were due to excessive speculative behaviour, unrelated to economic fundamentals. There were equally unjustified increases in parallel market rates for foreign exchange.

The end of the year saw both food and non-food prices spiralling out of control across most categories of the consumer basket.

Most discernible price increases were observed in categories that have significant import content, reflecting the sourcing of foreign exchange from alternative markets due to shortages.

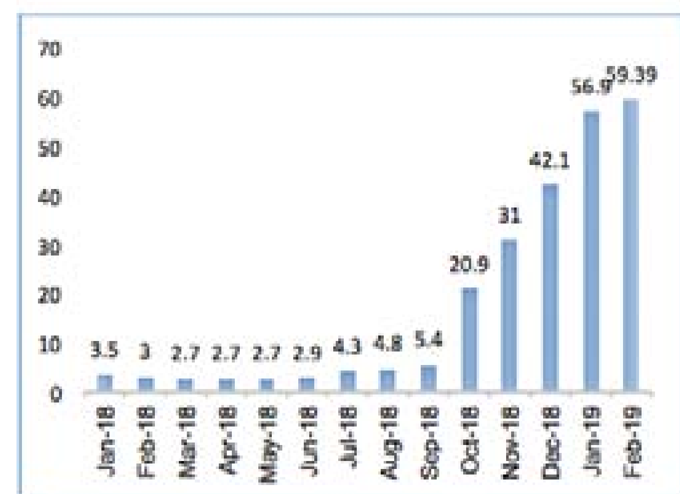
Month-on-month inflation, which had remained largely below the 1.5 percent threshold throughout the year, escalated to 16.4 percent in October 2018, before subsiding to 9.0 percent in December 2018, on the back of both food and non-food drivers. However, in January this year the monthly inflation rate shot up to 10.8 percent before it drastically fell to 1.67 percent in February ***(see figure 5.1).***

On an annual basis, the major drivers of year-on-year inflation in January this year were transport services (that is, passenger transport), transport costs (that is, cost of purchasing motor vehicles and motor cycles), household appliances, clothing and footwear and food and non-alcoholic beverages, with inflation rates of 192.75 percent, 130.41 percent, 125.19 percent, 82.13 percent and 63.71 percent, respectively (ZIMSTAT, 2019).

The overall inflation for January this year stood at 56.9 percent (see figure. 5.1). It is important for readers to appreciate that the weights, which are used to estimate the overall contribution of transport services, household appliances and clothing and footwear, for example, are marginal, that is, 5.31 percent, 9.76 percent, 1.34 percent and 6.05 percent respectively. Hence, the overall contribution of these headings to overall inflation is insignificant as it is weighed down by the low weights.

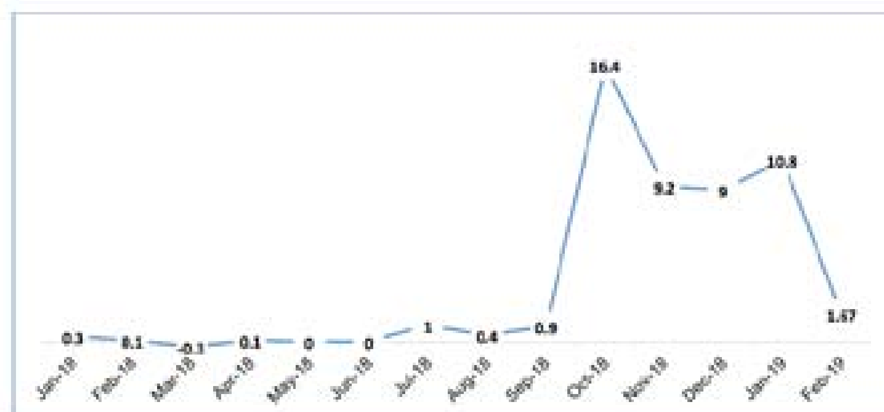
Alternatively, the food and non-alcoholic beverages, which constitute 33.53 percent to the overall inflation rate, had just moved up 63.71 percent between January 2018 and January this year, weighed down by the overall inflation rate. Based on the foregoing, the question as to whether the inflation rate figures represent a true reflection of the inflation dynamics in Zimbabwe is not misplaced.

Figure 5.1: Annual Inflation Profile (%)



Source: ZIMSTAT

Figure 5.2: Month-on-Month Inflation %



Source: ZIMSTAT (2019)

The fiscal authorities, on the other hand, have come up with a number of measures aimed at closing the tap on budget deficits and containing money supply, which are starting to bear fruit in terms of taming inflation.

For example, the month-on-month inflation rate for the month of February this year fell from 10.8 percent the previous month to 1.67 percent in February 2019, which is a clear testimony that the government is winning the war on inflation.

It is also important to note that month-on-month inflation is the correct indicator of the country's inflation rate as opposed to the year-on-year rate when making pricing decisions.

Pricing on the basis of year-on-year portends the risk of double pricing.

Juxtaposing Inflation Dynamics with Prices of Basic Goods

TABLE 5.1 shows that in line with inflation dynamics, the prices of basic goods tracked by the Consumer Council of Zimbabwe (CCZ) on a weekly basis on things like margarine, bread, flour, roller meal and meat rose by 490 percent, 108 percent, 261 percent, 41 percent and 201 percent respectively *(see table 5.1).*

The CCZ also noted that in line with the upward trend in the inflationary pressures, which has seen increases in prices of goods and services that include the commodities in table 5.2, the cost of living for a family of six shot up from $591 to $732 between January 2016 and December 2018 ***(see figure 5.3).***

The striking feature of the surge in the cost of living is that the country witnessed a sudden increase in the cost of living in October 2018 exactly the same time when the inflation rate went out of control ***(see figure 5.3).***

In taming inflation, the RBZ has come up with a number of instruments, chief among them being the liberalisation of the exchange rate which is expected to address distortions and rate spirals on the black market.

Although this measure may accelerate inflation through import push factors, in the medium term, and as price correction kicks in, the country expects the inflation rate to recede.

Going forward, it will be important to track how the cost of living will respond to these measures.

Table 5.1: Prices of Basic Goods Between 2016 and 2018

DESCRIPTION	January 2016 Prices ($)	December 2018 Prices ($)	Price Change ($)	% Change
Margarine 500g	0.89	5.25	4	490
Roller Meal 20kg	9.3	13.07	4	41
Brown Sugar 2kg	1.73	3.94	2	128
Tea leaves (100s)	1	2.57	2	157
Fresh Milk 500ml	0.69	1.17	0	70
Cooking Oil 750ml	1.25	2.97	2	138
Bread 700g	0.6	1.25	1	108
Flour 2kg	0.99	3.57	3	261
Rice 2kg	1.45	5.91	4	308
Salt 500g	0.18	1.34	1	644
Tomatoes 1kg	0.4	1.12	1	180
Onions 1kg	0.69	1.39	1	101
Cabbage 1kg	0.89	0.91	0	2
*Meat 1kg (**Economy**)*	3.5	10.55	7	201
Bath Soap	0.37	1.8	1	386
Laundry Bar	0.8	3.53	3	341
Washing Powder 500g	0.99	2.27	1	129

Source: Consumer Council of Zimbabwe (2018)

Figure 5.3: Trends in the Cost of Living for Family of Six

Source: Consumer Council of Zimbabwe (2018)

‘New exchange rate has brought new lease of life’

THE Interview represents an effort by Africa Economic Development Strategies (AEDS) and the Daily News to create a platform for newsmakers to respond to issues pertinent to their areas. In this inaugural interview, the executive director of AEDS Gift Mugano (GM) sat down with the Governor of the RBZ Dr John Panonetsa Mangudya (JPM) to hear his views on critical issues affecting the economy.

GM: In your Monetary Policy Statement (MPS) of February 20, 2019, you liberalised the exchange rate. Since it is now more than two months after the exchange rate was liberalised, what notable changes have been brought by this new exchange rate arrangement?

JPM: The decision to establish a flexible exchange rate market was taken after wide consultation with government and business taking into consideration the need to reduce distortions in the market caused by multi-pricing, enhance competitiveness and productivity. It removed distortions that had opened windows for arbitrage opportunities and rent-seeking behaviour. The demand for foreign currency, although it is still high, has also slowed down somehow because of the increase in the cost of accessing foreign exchange on the interbank market. This is a step in the right direction as it will help us narrow the current account deficit. With respect to the export sector, the new exchange rate arrangement has brought a new lease of life and improvement in the competitiveness of the sector.

GM: The market so far has responded positively to the MPS. What is critical going forward to restore stability is the need for sustained safety nets. What safety nets have been put in place by the monetary authorities to ensure that the rate does not run amok?

JPM: The central bank has,

Dr. Gift Mugano Executive Director Africa Economic Development Strategies

and continues to, mobilise lines of credit facilities to increase the supply of foreign currency on the interbank market, which will be buoyed by inflows from the sale of tobacco.

The exchange controls that are in place, such as the need to liquidate nostro accounts for exporters on the interbank market after one month and restricting the selling of foreign currency to a maximum of US$10 000 per day for bureaux de change, also come as an important safety net.

As our efforts to stabilise the country’s economy continue to bear fruit, the rate will eventually stabilise. It is however, important for stakeholders to note that there is need for concerted effort by everyone to substitute unnecessary imports with local production while enhancing exports. We are happy that government has taken important steps in the exercise of fiscal discipline which is critical in demand management.

GM: Gold producers are arguing that the 55 percent export retention is too high amid rumours that some, particularly artisanal miners, are holding on to their gold. Is there any substance to these rumours? Are their concerns justified? If so, what measures is your office working on to address this?

JPM: The problem is emanating from the exchange rate differentials between the inter-bank rate and the parallel market rate, whereby miners see the latter as more rewarding hence their concerns. Our role, as a central bank, is to bring sanity in pricing and exchange rate pricing is key: In this regard,

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'New exchange rate has brought new lease of life'

››› from P22

the RBZ is working on closing the gap between the parallel market rate and formal rates as alluded to earlier.

GM: Still on the new MPS, most exporting firms are arguing that the 30-month window for the utilisation of foreign currency, failure of which the proceeds will be liquidated into RTGS dollars via the interbank market, is too short and unfair. What is your take on this?

JPM: This measure provides a win-win solution to the entire economy. We want to guarantee viability of the export earners while at the same time securing the environment within which the exporters operate by making available essentials like fuel, medicines, etc which require foreign currency to be sourced into the country for the rest of the economy.

Those who are complaining are failing to appreciate that they have a national responsibility to contribute to the economic transformation of the country and that the products and services being exported are part of the national product of the country.

We do not need to personalise foreign exchange. It's a common good. Mining houses, for example, are extracting Zimbabwe's depletable minerals, which all Zimbabweans should benefit from and as such the country needs to share those foreign currency receipts in one way or another so that the country can import medicines, fuel and other critical requirements for everyone.

That is the rationale why some countries have significant reserves in their sovereign wealth funds for current and future generations.

GM: Isn't this 30-day "ultimatum" going to encourage wastage of foreign currency as companies will just buy anything they can lay their hands on just for the sake of clearing their accounts?

JPM: It is not necessarily true that some companies may use every means at their disposal to liquidate their foreign currency. There is a limit to that bad behaviour. In any case one of the roles of company directors and management is to enforce compliance with rules and regulations.

Banks are also expected to play their role in the value chain to ensure market discipline which is the most critical value proposition required in this economy. In addition to these processes, our Exchange Control is expected to effectively manage the foreign exchange transactions in the economy.

GM: There are rumours that some economic agents are using shelf companies to acquire foreign currency from banks for production purposes and in turn sell the money on the parallel market. Are these rumours true? Does the RBZ have enough instruments to combat this kind of chicanery?

JPM: If it is happening, then the problem will be with the banks themselves because the Know Your Customer (KYC) principle is a sure firewall against such malpractice. Where there is collusion between banks and their clients, we have the instruments to deal with this rent-seeking behaviour. It's all about discipline and going back to basics.

GM: There is a general view that the country's problem is not the shortage of foreign currency but its efficient usage. Do you subscribe to this view? If yes, what measures are you putting in place to address this anomaly?

JPM: The major challenges facing the economy are low productivity, low confidence levels and limited access to foreign finance due to geopolitical and country risk considerations.

The shortages of foreign exchange is therefore a symptom of these structural challenges. In 2018, for example, the country's foreign currency receipts totalled $6,3 billion — enough to sustain this economy under normal confidence levels.

We also need to ramp up production especially for those products that are required in the production of basic commodities. Wheat and soya bean production are examples of products that we need to produce in abundance to cater for the production of basic commodities such as bread and cooking oil.

GM: In 2017 and 2018, the country received foreign investment of $22,8 million and $25,4 million, respectively yet it attracted an average of $300 million in FDI per year over the same period. Can you explain why there is this disparity between the FDI receipts received and FDI attracted by the country and what needs to be done to narrow the disparity?

JPM: The US$300 million FDIs received in 2018 are signed up investment transactions which came to Zimbabwe either as cash or in the form of capital goods.

GM: What measures are you putting in place to tame inflation? What is likely to be the inflation outlook by end of the year?

JPM: In the medium to long-term, we expect inflation trends to recede. The new exchange rate measures themselves will see the elimination of pricing distortions which were causing shortages and inflationary pressures.

In taming inflation, the RBZ will continue to put money supply under check and work on mobilising more foreign currency receipts with a view of reducing pressure on the exchange rate so as to contain inflation.

At the moment, the inflation figures look high because of the year-on-year comparisons but when we reach October we expect the price differentials between the two periods to be small. In this regard, we are anticipating inflation figures of around 15 percent in the last quarter of the year.

We have also noticed that aggregate demand is falling on the back of low incomes and thus going forward we expect to see firms reducing their prices across the value chain due to low demand.

We strongly therefore advise business to use month-on-month inflation when pricing their products as a true indicator of inflation as opposed to annual rate of inflation.

WHO WE ARE

Africa Economic Development Strategies (AEDS) is a Zimbabwean grown management consulting firm committed to helping African economies catch up and lead global economic growth in the 21st century.

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+263 786 904 200
+263 242 852962
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