INVICTUS SECURITIES

**Zimbabwe Stock Exchange**

# December Monthly Market Update & Economic Outlook

**Research**
research@invictus-securities.com
+263-(0) 4 776607

## Executive Summary

- *The 2020 Economic outlook is predicated on status quo conditions – notably that the authorities cling to their current "mono-economy" strategy, high likelihood of another poor agricultural season and amid continued absence of access to external funding/BOP support.*
- *Risks to the economy remain overwhelmingly to the downside.*
- *GDP is officially estimated to have fallen 6.5% in 2019, reflecting the worst year for the Zimbabwe economic performance since 2008 when GDP is estimated to have fallen 14%.*
- *The rate of local currency depreciation slowed substantially in the final quarter of 2019 to 11% from 67% in the first quarter*
- *In the ten months to October 2019, exports at US$3.5 billion were marginally lower (-3.5%) than in 2018, but imports plunged by a third to US$3.95 billion, from 2018 Dec ending-$19.42 billion.*
- *Monetary growth further accelerated during the month of Sept 2019 to settle at Z$23.33 billion, largely driven by Nostro accounts revaluation in line with currency depreciation, and amid increases in transitory deposits.*
- *In terms of market value, the ZSE market cap increased by 53% to conclude the year 2019 at Z$29.77 billion, whilst in real terms the market shrinked by a massive 90% to end at an USD effective $1.78 billion from*
- *High inflationary environment in 2019 prompted investors to seek haven in equities, amid limited lucrative alternative investments elsewhere in the market.*
- *In the Outlook, we expect fiscal policy to be expansionary, while monetary policy will have to be accommodative to finance government expenditure which is expected to substantially exceed the budgeted Z$64 billion*

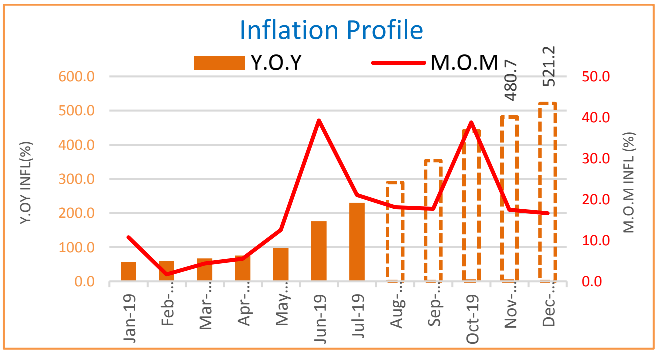
### *2019 in retrospect*

2019 was the worst year for the Zimbabwe economic performance since 2008 when GDP is estimated to have fallen 14%. GDP is officially estimated to have fallen 6.5% in 2019, but private sector analysts put the figure closer to 10% and probably even higher, with the rate of decline accelerating rapidly in the closing months of the year.

### *Inflation*

Year-on-year inflation reached 521% in December 2019, up from 481% in November 2019. The average inflation for 2019is estimated at 250%. Monthly inflation however further receded from 17.5% in November to 16.60% in December 2019, reflecting somewhat price stability attained during the months of November and December.

**Fig 1. Inflation Profile**




*Data Source, Zimststat, ISZ*

### The Exchange Rate

The rate of depreciation slowed substantially in the final quarter of 2019 to 11% from 67% in the first quarter – including 60% once-off devaluation – 54% in the second quarter and 56% in the third quarter.

Table 1: Exchange Rates

| Z$:US$ | Average | Year-End |
|---|---|---|
| Interbank | 8.7 | 16.8 |
| Parallel | 11.5 | 23 |

There was little evidence of convergence between the interbank and parallel rates, with the parallel rate premium remaining stubbornly high at 35% in the final quarter.

Given that only a small proportion of the forex market turnover takes place at the interbank rate, the parallel rate premium is a good indicator of the forward direction of the exchange rate but not of the rate of depreciation.

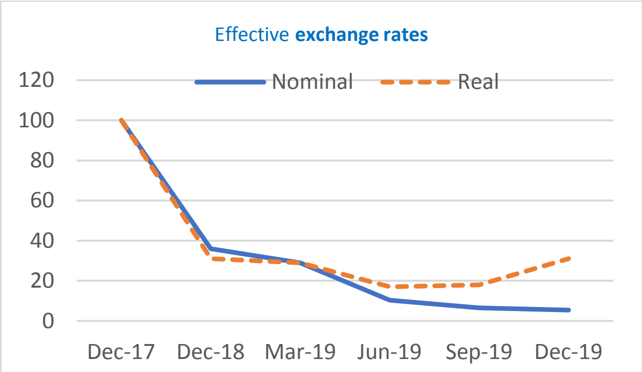
Table 2: Exchange Rate Index (December 2017 = 100)

| Year-End | 2017 | 2018 | 2019 |
|---|---|---|---|
| Nominal | 100 | 35.6 | 5.5 |
| Real | 100 | 30.7 | 31.0 |

The launch of bond notes in 2016 sparked the return of the parallel market which is used as the basis for the exchange rate index. The IMF estimates the parallel rate at 1.3 to the US dollar at the end of 2017 and 3.5 in 2018.

The nominal index declined almost 95% over the two years while the real rate was dragged down by devaluation of 63% in the parallel market in 2018, well before official devaluation of 60% in February 2019. As inflation accelerated in the latter half of 2019, the real effective exchange rate, which is the best indicator of a country's exchange rate competitiveness, started to rise.

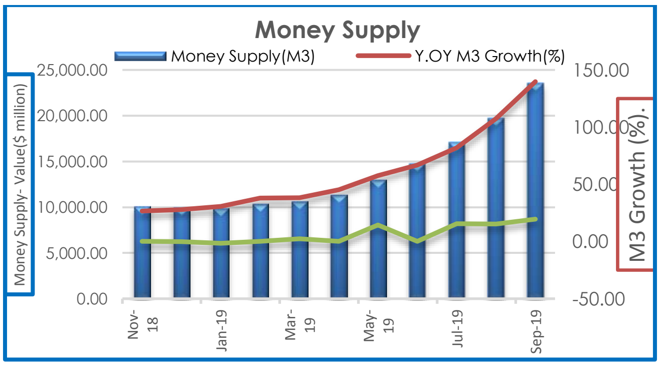
Fig 2: Effective Exchange Rates: Nominal and Real




### *Money Supply escalates*

Monetary growth further accelerated during the month of Sept 2019 to settle at Z$23.33 billion, largely driven by Nostro accounts revaluation in line with currency depreciation, and increases in transitory deposits. The largest component of broad money was transitory deposits in domestic currency, which constituted 47.21% of total deposits, followed by foreign currency deposits at 41.86%, while currency in Circulation constituted only 2.94%. The sharp rise in Money Supply will sustain inflationary pressures.

**Fig 3. Money Supply Growth up…**




*Data Source, RBZ, ISZ Market Survey*

### *External Sector: Foreign Trade*

In the ten months to October 2019, exports at US$3.5 billion were marginally lower (-3.5%) than in 2018, but imports plunged by a third to US$3.95 billion. The dramatic decline in the trade deficit to US$600 million from US$2.4 billion is a misleading indicator because import contraction reflects the sharp fall in aggregate demand in the economy, compounded by limited access to foreign currency to procure critical inputs, raw materials and other essentials.

For the year as a whole exports are estimated at just over US$4 billion which would leave a very small trade deficit of around US$200 million.

### The Balance-of-Payments

There are no up to date balance-of-payments estimates. In its September 2019 pre-budget strategy paper, the Treasury projected a current account deficit of US$238 million, down sharply from US$1.4 billion in 2018. The numbers in Table 1 have been revised in the light of more recent events.

After taking account of capital and financial movements, the overall deficit is estimated at US$200 million.

**Table 3: Current Account**

| US $ millions | 2018 | 2019 – Estimate | % Change |
|---|---|---|---|
| Exports | 4 670 | 4 300 | -8% |
| Imports | 6 600 | 4 800 | -28% |
| Balance on Services | -525 | -500 | -5% |
| Income Balance | -315 | -350 | + 11% |
| Transfers | +1 400 | +1 360 | -3% |
| (of which) Humanitarian Aid | +880 | +860 | -2.3 |
| Diaspora Remittances | +526 | +529 | +0.6% |
| Balance | -1 400 | -100 | - 93% |

## 2020 Economic Outlook

The outlook assumes the status quo both politically and in terms of macro-economic environment.

The political climate is forecast to remain polarized, probably becoming more so. High incidences of food shortages, high inflation and unemployment, and the possibility of another bleak agriculture season cannot be ruled out.

Wage explosion and industrial disputes will become more politicised and there is a risk of sporadic outbreaks of urban social unrest.

### *Risks*

The risks are overwhelmingly to the downside. Economic recovery will be constrained by a second successive drought year, hyperinflation and currency depreciation, sluggish world trade growth and weaker international metal prices, shortages of foreign exchange, fuel, load shedding, labour disputes, urban unrest and political uncertainty.

#### Growth: Another year of recession?

Table 4: Growth

| SECTOR | 2019 Estimated | 2020 Budget | 2020 Forecast |
|---|---|---|---|
| Agriculture | -20 | 5 | -5 |
| Mining | -14 | 4.7 | 2 |
| Manufacturing | -7 | 0.1 | -4 |
| Distribution | -12 | 4.2 | -2 |
| Finance | -6 | 4 | 2 |
| Electricity and Water | -22 | 2.1 | -4 |
| Transport | -5 | 2.1 | -2 |
| GDP | -11 | 3 | -3 |

*Source: 2020 Budget and Own Estimates*

The 2020 budget forecast, made in early November 2019, assumed normal rainfall in 2019/20, but the last two months of the year were abnormally hot and dry. Moreover, South African forecasters have predicted another drought year for the entire Southern Africa region, while in December the Famine Early Warning Systems Network (FewsNet) warned that the poor rainfall performance during the first half of the season will be compounded by the forecast of below normal rainfall during the second half of the rainy season (January to March 2020).

According to FewsNet the area planted for the 2019/20 season is expected to be "substantially below average", while livestock conditions, especially for cattle, are poor due to reduced water and pasture availability.

Regardless of the weather, agricultural output is forecast to decline due to lower plantings, shortages of water, seed and fertilizer and financial and profitability constraints. Accordingly agricultural value-added is predicted to decline to its lowest level since 2013. Depending on weather conditions over the next four months, the current estimate of a 5% decline could turn out to be optimistic.

### *Mining: Marginal Growth*

Mining GDP is forecast to increase marginally, despite weaker global prices for some metals and financial and input constraints. Load-shedding will be a major problem while the industry as a whole is suffering from the exodus of professional and technical skills and leakages.

#### *Manufacturing*

The outlook for manufacturing is poor due to the combination of supply-side shortages and weak domestic demand. Industrial GDP is forecast to fall another 4% to its lowest since 2010. Output is likely to be disrupted by supply-side shortages – load-shedding, fuel, and finance – and industrial disputes, which could well spill over into urban unrest.

#### *Wages: Explosion Ahead*

Average wages are estimated to have doubled during 2019 but failed to keep pace with rising prices, up 250% on average. The November2019 Total Consumption Poverty Line is estimated by ZimStats at Z$3 656 a month for a family of 5 people. This is estimated to be 50% above average formal sector wage excluding agriculture, and more than double average wage when farming is included.

By the end of 2020, the TCPL is forecast at between Z$8 000 and Z$9 000 a month meaning that formal sector wages will have to increase at least 300% during the year for an average family to escape from poverty. Meanwhile, Government has offered a 100% salary increase for its employees, who demand a USD 475 equivalent at interbank rate.

Consequently, wage inflation will be a problem for all sectors of the economy, with industry and services likely to be the hardest hit by the steep rise in living costs in urban areas.

#### Distribution: Lower Disposable Incomes will take their toll

The main threat to the distribution sector is the decline in real wages and while this will be cushioned by future wage awards, with profit margins eroding, firms will lay off labour, thereby exacerbating the continued downturn in aggregate demand. Distribution will also be hard hit by the steep increase in transport costs, fuel availability and load-shedding.

### Services: Government wage awards will set the pace

Substantial wage increases are anticipated across the economy, but especially in the services sector. In the budget, public sector wages are forecast to rise 130%, but because this will not keep pace with inflation, real wages would be some 50% below their 2018 level.

For this reason, the government wage bill will rise more than 150% and this will have knock on effects across the economy where employers tend to follow the trend in public sector wages.

### Expenditure: Budget Targets will be missed

Consumption spending, accounting for over 80% of GDP grew strongly in 2019 due to inflation, but in real terms it is estimated to have fallen at least 15%. A further 5% decline is anticipated in 2020, despite very strong wage growth.

After falling sharply in 2019 when inflation of 250% far exceeded wage growth (about 125%) wages are forecast to keep pace with 2020 inflation (about 175%). Over the two years, however, inflation will substantially exceed wage growth, as a result of which real consumption spending is forecast to decline by a quarter in the two years, 2019 and 2020.

Investment, constrained by weak corporate balance sheets, difficulty in accessing forex and lower domestic demand, will remain very depressed, though there will be an increase in public sector investment funded by credit creation.

### External Accounts Trade gap to Widen

The trade gap will widen in 2020 as import grow at least 10% while exports decline slightly. Humanitarian aid inflows, primarily food aid, will increase substantially but Diaspora remittances are likely to be relatively static.

Capital inflows will decline further, and the country will become increasingly dependent on trade-related offshore borrowing.

Table 5: 2020 OUTLOOK SUMMARY

| Z$ BILLIONS | 2019 Estimated | 2020 Forecast | % change |
|---|---|---|---|
| REAL GDP | 17 860 | 17 000 | -5% |
| Average Inflation | 250% | 200% | -20% |
| Year-end Inflation | 500% | 150% | -70% |
| Exports | US$4 300 | US$4 000 | -7% |
| Imports | US$4 500 | US$5 000 | +11% |
| Balance of Payments: Current Account | -US$100 million | -US$500 million | +400% |
| Govt Revenue | Z$21 billion | Z$65 billion | +210% |
| Govt Expenditure | Z$28.2 billion | Z$80 billion | +184% |
| Deficit | Z$7.2 billion | Z$15 billion | +108% |
| Money Supply (M3) | Z$26 billion | Z$$60 billion | +130% |
| Interest Rate (Corporate Loans) | 19.8% | 40% | +102% |

### Inflation: Stuck in Triple Digit Territory

Inflation is expected to slow from its 2019 levels but a host of factors will maintain strong upward pressure on prices. Wages will be a key driver along with food shortages, none food inflation catching up, unbudgeted government expenditure, rapid monetary growth, negative real interest rates and continued currency depreciation.

### Fiscal and Monetary Policy: Borrowing to survive

Fiscal policy will be expansionary, while monetary policy will have to be accommodative to finance government expenditure which is expected to substantially exceed the budgeted Z$64 billion. Even before the start of the fiscal year (Jan 1, 2020), the authorities had announced the re-introduction of grain subsidies, which were abolished in the November budget, as well as subsidies for 7 other food items. Transport subsidies have been increased, while upward pressure on salaries remain imminent.

In the absence of access to external funding, Government's efforts to borrow domestically have not been successful. Treasury Bill tenders for Z$1.77 billion in the latter half of 2019 yielded only Z$794 million (45%). This means that not only did the government fail to raise the budgeted Z$1.96 billion in domestic borrowing, but because the deficit was Z$1.3 billion above budget, it was left with a Z$2.5 billion funding gap.

This is likely to widen in 2020 when the deficit is expected to exceed the Z$5 billion forecast in the budget and the Treasury will also have to find a minimum of another Z$10 billion to finance loan repayments and capital spending that was not provided for in then budget.

Some of this will have to be funded by central bank credit creation while the RBZ has already promised to increase the note issue to 10% or 12% of money supply. In September, the note issue was Z$800 million or 3.4% of money supply, meaning that the authorities will need to print some $2 billion of new notes to meet its 10% target.

This allied with triple-digit inflation, and increased government and private sector borrowing will ensure that money supply doubles during 2020. Despite this, the authorities will maintain their negative real interest rate policy in order to avoid the build-up of non-performing loans in the banks, while also pressuring banks to make soft loans to distressed businesses. Financial System can be fragile.

## Conclusion

### Not If but When?

*The above outlook is predicated on status quo conditions – notably that the authorities cling to their current "mono-economy" strategy, there is another poor agricultural season and no successful re-engagement with the international community leading to a financial bailout.*

*Given the plethora of adverse conditions, domestically as well as – to a far lesser degree - globally, the situation outlined in this report looks to be unsustainable. The accelerating re-adoption of the US dollar and the rand, - the latter mostly in Matabeleland - suggests that Zimbabwe is close to the point of no-return so far as the currency is concerned. This means that it is no longer a matter of if the government will be forced to re-dollarize (or adopt the rand)* ***but when.***

*Re-dollarization would be a game-changer with far-reaching political as well as economic repercussions, as a result of which the outlook would change radically for the better ends.*

## *Stock Market Performance & Outlook*

### The Zimbabwe Stock Exchange: Real Prices and Volumes will fall

Equity price movements and sales volumes were dominated by inflation and exchange rate trends during 2019. The All Shares index rose 57%, but with inflation averaging 250%, investors experienced huge losses in real terms. Similarly, in US dollars market capitalisation collapsed to just $1.78 billion from $19.4 billion at the start on the year 2019.

Similar trends are expected in 2020. Corporate earnings will fall in real terms, partly as a result of the adoption of inflation-adjusted accounting by listed companies and currency depreciation. Volumes will continue to fall and as costs escalate, margins will be squeezed.

Equity prices will continue to increase in nominal terms as investors faced with negative returns on cash (except for foreign currency) and fixed interest securities seek the safer haven of foreign-listed equities in particular. Local listings will also be driven higher by excess liquidity conditions and inflation, though in real terms, values are likely to decline.

**Table 6: Investment Return, 2019**

| | | Money Market | | Stock Market |
|---|---|---|---|---|
| | Savings Deposits | Fixed Term Deposits | Treasury Bills | All-Share Index |
| Average Returns (%) | **4.74%** | **8%** | **15%** | **57%** |

## ZSE monthly performance

High inflationary environment in 2019 prompted investors to invest in equities as a safe hedge, in the absence of other meaningful alternative investments elsewhere in the market. The introduction of the local currency through the SI142 of 2019 sapped away the lucrative USD return which attracted foreign investors in the pre- Zim dollar return period. As a result, foreign investor participation dwindled largely in the second half of the year, although foreign currency remittance challenges deterred the exit.

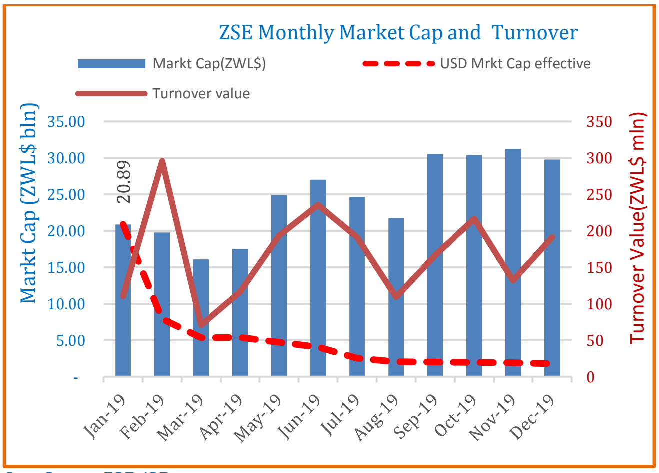
**Table 7: ZSE Indices Monthly Performance**

| ZSE Summary Performance | | | | Monthly | YTD |
|---|---|---|---|---|---|
| | | | | % Change | YTD % Change |
| | Dec-19 | Nov-19 | Dec 2018 | | |
| All share | 230.08 | 240.81 | 146.24 | -4.46% | 57.33% |
| Industrial Index | 766.34 | 801.38 | 487.13 | -4.37% | 57.32% |
| Top 10 | 202.68 | 216.29 | 145.02 | -6.29% | 39.76% |
| Minings Index | 316.66 | 344.42 | 227.71 | 8.06% | 39.37% |
| **ZSE Market Cap (ZWL$bln)** | **29.77** | **31.23** | **19.42** | **4.67%** | **62.74%** |

*Data Source: ZSE, ISZ*

The ZSE market registered positive performance in nominal terms, as the All-share index surged 57% to close the year 2019 at 230.08 points. In terms of market value, the ZSE market cap increased by 53% to conclude the year 2019 at Z$29.77 billion, whilst in real terms the market shrinked by a massive 90% to end at an USD effective $1.78 billion. Although the ZSE return stood comparatively higher, investors have lost value in real terms.

Fig 4: Market Capitalisation Vs Turnover.




*Data Source: ZSE, ISZ*

## Table 8: ZSE Monthly Stats Profile

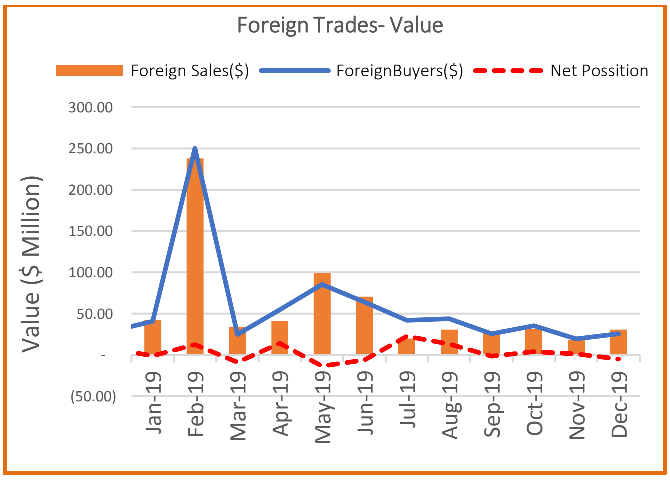
| | Market Cap (Billion ZWL$S$) | Turnover Value(Million (ZWL$) | Turnover Volume |
|---|---|---|---|
| Jan-19 | 20.89 | 110.28 | 122,780,138 |
| Feb-19 | 19.77 | 295.84 | 233,070,149 |
| Mar-19 | 16.08 | 70.81 | 123,377,596 |
| Apr-19 | 17.50 | 116.52 | 134,603,851 |
| May-19 | 24.92 | 193.52 | 237,215,616 |
| Jun-19 | 27.02 | 235.59 | 293,170,355 |
| Jul-19 | 24.64 | 191.07 | 163,579,896 |
| Aug-19 | 21.74 | 109.04 | 117,916,356 |
| Sep-19 | 30.53 | 166.56 | 335,373,072 |
| Oct-19 | 30.39 | 216.45 | 203,018,503 |
| Nov-19 | 31.23 | 131.81 | 125,439,151 |
| Dec-19 | 29.77 | 191.09 | 194,203,243 |

*Data Source: ZSE*

## Foreign Investor Participation

Cumulatively, foreign investors were net buyers in 2019, as foreign purchases stood at Z$709.99 million, outweighing the foreign sales which stood at Z$681, 41 million, reflecting a net position of Z$28.59 million. Overall, foreign investors' contribution to total turnover improved from 31% in 2018 to 34% in 2019.

**Fig 6: Foreign Trades**




## Share Prices Adjustments, slow

All counters ended the year 2019 higher, except for the duo of Seedco and Cassava which lost 8% and 1%, respectively. The compounded effect of high inflation and local currency depreciation however condemns most of the gains realised to be negative returns, in real terms.

## Table 8: Year-on-year Top Performers

| Counter | Dec-18 | Dec-19 | % Change |
|---|---|---|---|
| **Top Movers** | $ | $ | % |
| Medtech | 0,0002 | 0,0152 | 7500.00 |
| Ariston | 0,0240 | 0,1895 | 690.00 |
| RTG | 0,0242 | 0,1450 | 499.00 |
| ZHL | 0,0256 | 0,1500 | 486.00 |
| CBZ | 0,1405 | 0,6971 | 396.00 |
| **Top Fallers** | | | |
| Seedco | 2,0779 | 1,9025 | -8.00 |
| Cassava | 1,4219 | 1,4030 | -1.00 |

## Table 9: Monthly Top Performers - Dec 2019

| Counter | Nov-19 | Dec-19 | % Change |
|---|---|---|---|
| **Top Movers** | | | |
| Art | 0.0800 | 0.1300 | +63 |
| Edgars | 0.1550 | 0.2100 | +35 |
| ZHL | 0.1150 | 0.1500 | +30 |
| FMHL | 0.2400 | 0.3105 | +29 |
| Dawn | 0.0600 | 0.0730 | +22 |
| **Top Fallers** | | | |
| Afsun | 0.4348 | 0.2500 | -43 |
| OK Zim | 0.8775 | 0.5524 | -37 |
| Powerspeed | 0.2900 | 0.2000 | -31 |
| PPC | 5.1415 | 4.0000 | -22 |
| Axia | 0.8050 | 0.6400 | -20 |


**Research Team:**
**Mutandani Makuyana**
**(Email: m.makuyana@invictus-securities.com),**

**Tapiwanashe Kazunga**
**(Email: t.kazunga@invictus-securities.com).**

**Sales and Trading Team:**
**Tinashe Magodora**
**Email: t.magodora@invictus-securities.com),**

**Wellington Mapedzamombe**
**(Email: wellington@invictus-securities.com)**

**Telephone: (+263-242)776607/782770/788257/8**