Zimbabwe: State of the Operating Environment

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Outline

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1. POLITICAL DEVELOPMENTS

1.1 Political Environment

- Zimbabwe adopted a new constitution following a May 2013 referendum in which 93% of the votes were in favour of the new constitution. This paved way for the presidential and parliamentary elections, which were conducted in July 2013.
- ZANU PF won more than 2/3 of the parliamentary seats, thus ending the era of the Inclusive Government. All cabinet ministers are from ZANU PF. This in our view means that there will no longer be any policy inconsistency issues.
- SADC and AU endorsed the elections as free and fair, but highlighted some issues which needed to be addressed in the medium to long term
- It is clear that the future will be about indigenous participation in resources and about local value addition. This focus is emphasised in the Government's economic blueprint titled Zimbabwe Agenda for Sustainable Socio-Economic Transformation (Zim Asset) as well as the 2014 Fiscal Policy. We have already seen 16 roads being tendered by locals who will then partner international technical and financial partners.
- Notwithstanding the differences the political parties, the environment has remained stable, calm and peaceful. The new Government has indicated that it will continue to pursue business-friendly policies e.g. the multi-currency system. There is also a demonstration of consulting widely during the policy formulation process.
- Some investors have already made moves to take advantage of emerging opportunities in infrastructure development, e.g. energy infrastructure development (Sino hydro); road network rehabilitation (Group 5).

1.2 Re-engaging International Stakeholders

- Prior to 2009, relations between Zimbabwe and most international stakeholders had deteriorated considerably. In 2010, during the tenure of office of the Inclusive Government, a Re-engagement Committee was formed and some steady progress in rebuilding strained relations was achieved, e.g.
  - IMF, Africa Development Bank and the World Bank resumed interaction with the Zimbabwe Government, albeit at a technical assistance level since 2010.
  - The Bretton Woods institutions also provided technical guidance during the formulation of the Zimbabwe Debt Clearance strategy, which was finalized in June 2013. The IMF also agreed to place Zimbabwe on a Staff Monitored Program (SMP) during 2013. The SMP which was initially expected to last 6 months has been extended by another by another six months to June 2014. Government has committed to continuing the Staff Monitored Program with the IMF.
- The European Union (EU) and Australia have gradually softened their stance on Zimbabwe. The EU has delisted more than 80 people and entities from the list of financial restrictions in 2013, leaving only 10 names. The removal of restrictions against Government's mining company, Zimbabwe Mining Development Corporation (ZMDC), has enabled the country to conduct the first sale of diamonds through Antwerp Diamond Trading Centre in November 2013.
- While relations with the US have remained strained largely due to lack of constructive dialogue, in Europe some countries like Belgium are warming up to rebuilding relations with Zimbabwe.

1.3 Policy clarification

- **Indigenisation:** The new Minister of Indigenisation and Economic Empowerment is encouraging dialogue and has alluded to the fact that he will not adopt a "one size fits all" approach during implementation. Government has announced that resource based sectors such as mining would be treated differently from the non-resource based sectors, because Government viewed the depleting resource, e.g. the mineral in the case of mining, as the country's contribution in the business. The 51/49 shareholding arrangement would be pursued in resource based sectors and more flexibility would be allowed in the other sectors.
- **Multiple currency system:** The Government has indicated through the Fiscal and monetary policy statements that the system of multiple currencies adopted in 2009 will be continued during the term of office of the current Government which ends in 2018. In line with this commitment, Government has indicated that it is working on issuing bonds to attract foreign funding, including investments by Zimbabweans living in the diaspora.
- **Bank Capitalisation**: Clarity has already been provided around bank capitalisation with an extension for compliance to 2020. Minimum Capital requirements for banks remain at the December 2012 levels of US$25 million for Commercial Banks, US$25 million for Merchant Banks, US$20 million of Building Societies, US$15 million for Discount and Finance Houses and US$5 million for Microfinance Banks. Compliance with the level of USD 100 million for Commercial Banks have now been moved to 31 December 2020. Our Finance department will therefore compute a plan for reaching the USD100m and our dividend policy going forward. It will be important to ensure that whatever capital we retain does not restrain our lending activities. The deal sizes we are seeing in CIB and PBB are upwards of USD10m per client and at this stage the current capital levels are deemed adequate

2. ECONOMIC DEVELOPMENTS

2.1 Productive Sector developments

Gross Domestic Product (GDP):

- GDP growth which averaged 7.5% during the first three years of dollarisation, slowed down to 4 – 3% during 2012-13 period, due to apprehensions around political environment and elections. This was exacerbated by weakening international commodity prices, which adversely affected gold, nickel, chrome and cotton export earnings.
- In the outlook to December 2014, the Government is projecting real GDP to grow by 6.2% in 2014 and continue on an upward growth trajectory to 9.9% by 2018. Government underpins this rapid growth on increased activity in infrastructure development as investors take up opportunities in PPPs, increased Foreign Direct Investments as the indigenisation and investment policies issues are clarified, beneficiation in the mining and agriculture sectors, among other things.
- The IMF has deemed the growth projection too ambitious and has projected a 3-4% growth for Zimbabwe. Sectors providing growth opportunities are Power & Energy; Mining; Telecommunications and Agriculture. The manufacturing, however, continues to perform sluggishly, due to, inter alia, low competitiveness in the face of imports from China and the Southern Africa region.
- The Bank is able to cherry pick on viable opportunities and make a return for the shareholder.

2.1 Productive Sector developments...cont'd

GDP growth rates (%)

Selected Economic Sectors	Weights (%)	2009	2010	2011	2012	2013
		Actual	Actual	Actual	Actual	Estimate
Agriculture	16.1	10.4	19	10.5	3.8	4.5
Mining	8.3	15	40	25.3	15.8	5.3
Manufacturing	18.6	8	4.1	5	2.1	0
GDP at market prices	**100**	**5.1**	**7.8**	**9.3**	**4.4**	**3**

Source: Ministry of Finance 2014

2.1 Real Sector Developments...cont'd

(a) Agriculture: Selected key Food and Export crops

'000 tonnes	2012	2013	2014 proj	% Change
Tobacco	144	166	171	3.0%
Cotton	304	140	125	-10.7%
Maize	960	750	750	0.0%
Soya bean	70.5	72	80	11.1%

Source: Ministry of Agriculture, ZIMSTATs; TIMB

(b) Manufacturing: Volume of Manufacturing Indices

Manufacturing Subsectors	Average Capacity Utilization (%) in 2012	Average Capacity Utilisation (%) in 2013
Bakers	40.0	82.5
Battery	76.5	71.5
Building (construction and related)	59.5	44.1
Car Assemblies	30.3	13.1
Electric Appliances Manufacturers	43.8	37.5
Engineering Iron and Steel	36.7	27.7
Food, Diary and Beverages	58.2	42.0
Grain Millers	30.0	50.0
Chemical	41.6	30.0
Leather and Allied	27.5	11.3
Pharmaceuticals	58.0	20.0
Plastic, Packaging and Rubber	46.1	38.0
Paper, Printing and Publishing	58.3	55.0
Textiles and Clothing	34.4	35.3
Timber Processor	53.8	58.0
Average for the whole Industry	**43.2**	**39.6**

Source: ZIMSTATs; Ministry of Finance

(c) Mining Production Statistics

	2011	2012	2013	% change
Gold (kgs)	12992	14850	13929	-6.20%
PGM's (kgs)	20188	20357	20764	2.00%
Of which Platinum (kgs)	10826	10951	12747	16.40%
Coal (tonnes)	2562054	1738486	1999259	15.00%
Ferrochrome (tonnes)	161838	142512	83370	-41.50%
Nickel (tonnes)	7992	8181	9400	14.90%

Source: Chamber of Mines

(d) Foreign Direct Investment Inflows

US$M	2005	2007	2008	2009	2010	2011	2012
Botswana	279	495	528	579	559	587	612
Namibia	348	733	720	516	712	900	850
Mozambique	108	427	592	893	989	2093	5,200
Zambia	357	1324	939	695	1729	1982	2100
Zimbabwe	103	69	52	105	166	387	400

Source: *United Nations Conference on Trade and Development (UNCTAD): World Investment Report 2013*

2.2 Monetary sector developments

Banking sector developments:

- M3 money supply has progressively grown by 70% from USD 2.33 billion in December 2010 to USD 3.97 billion by December 2012. During 2013, money supply remained stagnant at around US$ 4 billion mainly due to abnormally high levels of outflows attributed to maturing credit lines which were not being renewed and a rising import bill and the apprehensions arising from political uncertainty. On the other hand, the level of exports and other receipts like diaspora remittances registered a decline in 2013.
- The Reserve Bank of Zimbabwe acknowledged that the economy faced serious liquidity challenges in 2013. This notwithstanding, the financial sector is still considered healthy because the few troubled banking institutions are of low systemic importance as they accounted for less than 10% of the banking sector's total assets, total deposits and total loans respectively, as at 31 December 2013.
- The Bank's strategy during this period involved targeting big movers of liquidity in the economy such as large mining companies, utility providers, the Zimbabwe Revenue Authority.
- The Reserve Bank is planning to issue Treasury Bills to simultaneously raise funds for Government to bridge short term financing gaps as well as facilitating interbank trading. Short term Treasury bills are acceptable collateral on the part of banking institutions requiring interbank borrowing. It is expected that Government will have borrowing limits that will be monitored by the Banking and Finance Committee of Parliament.
- The Government is planning to capitalize the Reserve Bank of Zimbabwe to start the Lender of Last Resort function with effect from 1 April 2014. This will enable the Central Bank to issue an overnight accommodation rate, which will give direction to commercial bank lending and deposit interest rates.

2.2 Monetary sector developments …cont'd

Government takes over Central Bank debt:

- The Reserve Bank of Zimbabwe (RBZ) debt of $1.35 billion is assumed by Government and creditors will get 5 year Treasury bills at 5%.

Gold Bonds:

- Holders of gold bonds previously issued by the Reserve Bank will also be paid by the Government.

Inflation:

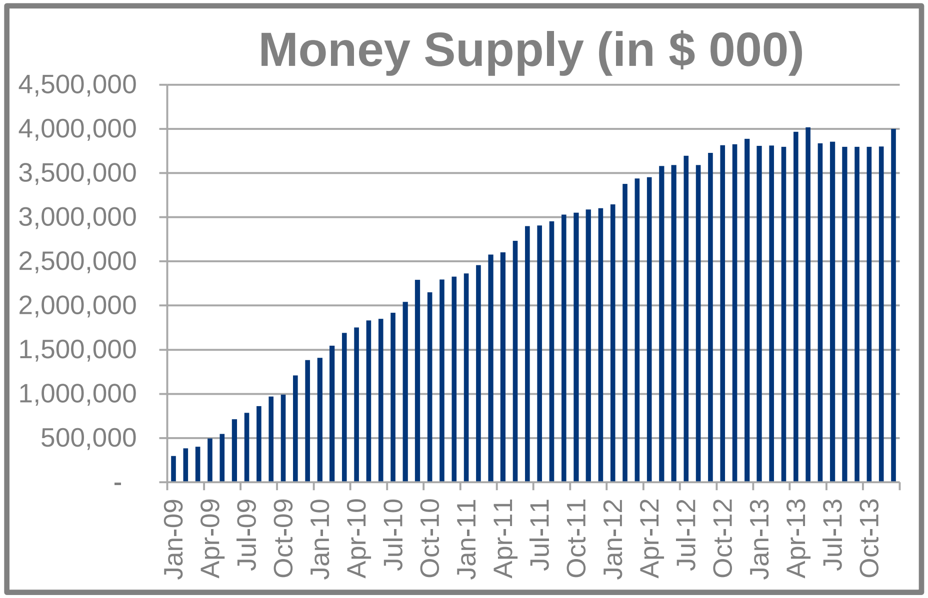
- Inflation was recorded at 0.33% (y/y) and -0.08% (m/m) during December 2013. A weakening SA rand has contributed to declining inflation in Zimbabwe during 2013, given that South Africa is the country's major trading partner. Some local businesses are facing a situation where cost of business is rising while the final consumer prices have stagnated. This phenomenon is attributed to the impact of cheap imports on domestic pricing trends.

Interest Rates:

- In December 2013 the Reserve Bank of Zimbabwe put aside the Memorandum of Understanding (MoU) which was signed in February 2013 between the central bank and banks as a way of checking the increase bank rates and charges.
- The authorities are expecting that Banks will self regulate and only increase prices when the cost outlays justify it.

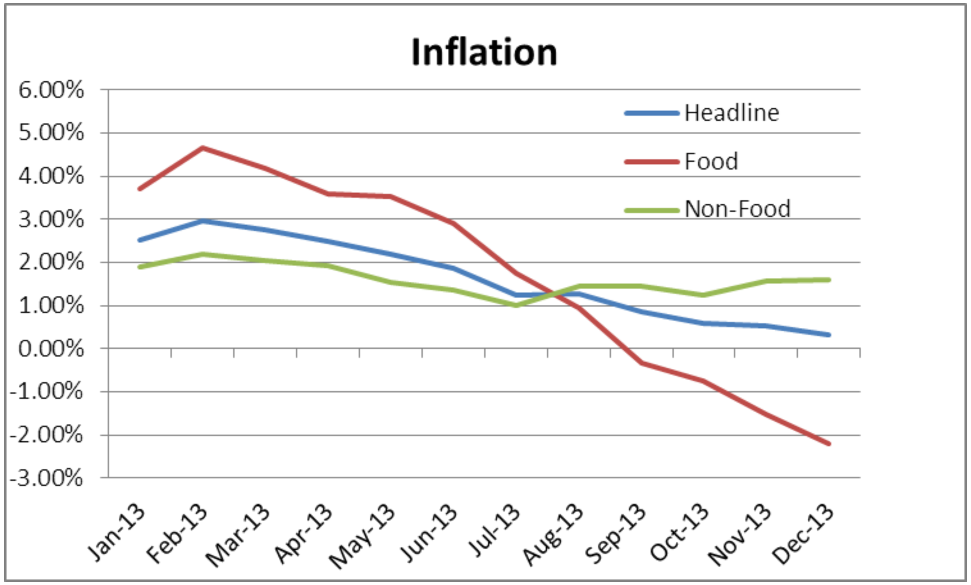
2.2 Monetary Sector charts

M3 Money Supply (US$ million): Jan 2009 – Dec 2013



Source: Reserve Bank of Zimbabwe, 2014

Inflation (%): Jan 2009 – Sep 2011



Source: Zimbabwe Statistics Agency, 2014

2.3 Public Sector Developments

- Due to the challenging environment in 2013 the fiscus was severely constrained and this situation made cash budgeting a difficult task. During 2013, revenue collections at US$ 3.43 billion were 5.8% below target. On the other hand, actual expenditures at US$ 3.83 billion were 3.5% in excess of budget. The resultant deficit of US$ 400 million clearly indicates that cash budgeting was not adhered to.
- The 2014 National Budget performance would be dependent of the performance of the economy because external budget support has remained elusive. Expenditure pressures exacerbated by wage bill increases, imply that the Government would most likely require a borrowing limit.
- During 2013, the budget was generally consumptive in nature, with 95% of expenditures being recurrent and only 5% being reserved for capital projects. For 2014 capital projects have been allocated 15% of the budget.

2.4 The External Sector developments

Balance of Payments:

- The country's trade deficit (US$ 4 bn), averaging 30% of GDP is unsustainably high. Monthly exports are averaging USD 350 million, while imports are averaging USD 700 million/ month.
- The significant inflows which somewhat cover this huge trade deficit include: short term trade finance facilities ($700m), accumulation of arrears ($350m), grants ($220m), net Foreign Direct Investment ($350m), net portfolio investment ($100m), and diaspora remittances ($939).
- The FDI flows averaging US$ 350 million in 2012 -13 are significantly lower than regional averages of over USD 1 billion. Zambia and Mozambique's FDI flows were around USD 2 billion each in 2012.

External Indebtedness:

♦A reconciliation and verification of the debt statistics by Government indicated that the total external debt stock, including arrears, stands at US$ 6.5 billion as at December 2012. This huge debt overhang which is 55% of GDP (including external payments arrears) adversely impact the country's credit worthiness and thus constrain new foreign capital inflows.

♦ Whilst Government has put in place a debt clearance plan/strategy, there is yet to be an agreement with the respective creditors.

♦ The IMF approved SMP is designed to help build the country's policy credibility ahead of negotiations on debt rescheduling with the external creditors.

2.4 The External Sector developments…(cont'd)

Selected BOP Statistics	2011	2012	2013	2014
(USD million)	Act	Act	Est	Proj.
CURRENT ACCOUNT (excl.official transfers)	**-3,127**	**-2,407**	**-2,359**	**-2,293**
of which TRADE BAL f.o.b	**- 3,066**	**-3,046**	**-4,248**	**-2,431**
of which Exports f.o.b	4,496	4,054	4,252	4,862
of which Imports f.o.b	-7,562	-7,100	-8,500	-7,293
CAPITAL ACCOUNT (Incl. Official Transfers)	**1,561**	**1,148**	**1,627**	**1,894**
of which Direct Investment (Net)	373	353	334	703
of which Long Term Capital (net) - Loans	723	31	275	383
of which Short term capital (net) -Loans	244	435	701	429
Errors and omissions	**784**	**879**	**-**	**-**
Overall Balance	**-783**	**-380**	**-732**	**-399**

Source: RBZ and Zimstats

2.5 View on the Economic Outlook

The economic prospects for Zimbabwe, in the outlook period, depends on a host of things including the following policy areas:

- **Indigenization** – there is scope for encouraging foreign investment as Government continues to clarify that the implementation will not be a *one size fits all approach*.
- **External Debt resolution** – there is need for formalization of the debt clearance strategy with relevant creditors so as to operationalise the rescheduling of debt repayments.
- **Land tenure system** – the 99 year lease should be made bankable and transferable. The majority of farmers have offer letters only.
- **Reengagement and normalization of relations** with the international community - noting that BRICS only constitute < 20% of global FDI. The Government should engage all influential stakeholders to unlock growth opportunities.
- **Currency management system** – dollarization has stabilized the economy and may continue to do so over the next 5 years. More needs to be done to stimulate growth and foster competitiveness of exports.
- **Fiscal discipline** – cash budgeting is most likely going to be discarded. Prudential limits and discipline within set limits would need to be set. Parliament would need to strongly enforce accountability.
- **Infrastructure rehabilitation and development** – economic activity basically requires reliable and robust water supply, telecoms, energy generation and supply, and transportation infrastructure.
- **Export led growth and management of BOP deficit** - to sustainable levels. Prospects of relief for the BOP are likely to be realised through the debt resolution strategy.