zimbabwe national chamber of commerce

"THE VOICE OF BUSINESS"

02 March 2020

ZNCC SUBMISSION TO THE PARLIAMENT PORTFOLIO COMMITTEE ON FINANCE AND ECONOMIC DEVELOPMENT

PREAMBLE

ZNCC is honoured to have an opportunity to present to the Portfolio Committee on Finance and Economic Development on issues affecting Business. The Chamber remains confident that these engagements will continue to provide a harmonious and productive working relationship between policy makers and industry. The Macroeconomic Environment is weighing on Industry performance and continues to be characterised by cash shortages, competition from the informal sector, high unemployment levels, limited local and foreign investment inflows and high cost of doing business.

In an effort to help improve the doing business environment the Chamber has been conducting **Evidence Based State of the Economy Surveys** to help inform Policy makers on challenges that are being faced by business and recommending on what needs to be done. Surveys have been submitted to the Policy makers and **challenges still remain on what needs to be done.** In 2018 the Chamber conducted a Survey on the Impact of Tax Policy on Business in Zimbabwe – **"Zimbabwe Tax Environment and its contribution to the New Normal Economy**. The survey was meant to capture business concerns about Zimbabwe's tax system and below are the challenges that were highlighted by Business:

Challenges with Tax Policy and administration *(from the findings)* and these still need to be addressed

- Most of the Business/interviewees regarded the system as punitive given operating environment as it increases cost of doing business rendering local products uncompetitive
- There is lack of enforcement on informal sector hence interviewers regarded it as selective
- there are no incentives granted for full compliance rather the existing laws extend periodic relief to defaulters
- tax policy formulation in Zimbabwe is done largely without consultation. This was particularly with regards to the 2% electronic transaction tax which the business said erodes buying power of customers and reduces company capital
- Too many taxes with high tax rates a burden to business
- Restrictive import management programme constricts tax revenue collection capacity
- A near optimal tax collection capacity weighed down by leakages
- Weak legal framework to tame the tax defaulters
- Tax system does not motivate tax payers to remit their dues
- Tax system is weighing on business – for example the 2% tax which was introduced to close the fiscal deficit has resulted in business carrying the cost

<u>In 2019 the Chamber conducted a Survey on the "Impact of Energy Challenges on Business in Zimbabwe"</u>

A submission with recommendations was made to policy makers and **challenges still remain.** The survey focused on a sample of 176 firms across five regions of Zimbabwe (Harare, Bulawayo, Mutare, Masvingo and Gweru); and operating in manufacturing sector (62% of the respondents), agriculture sector (17%), services sector (12%) and other sectors (9%).

From the findings:

- **Energy sources for majority of business** - All respondents (100%) indicated that their main source was electricity, and some will only use generators or solar to power their production activities (20% of their respective activities) as backup or as a second best option in the absence of electricity
- **Production time and production output** - Most firms said power outages affected their business activities with 40% of respondents indicating that the phenomena result in significant loses given that 50% of their production time were lost, while 45% of firms indicated that power outages resulted in more than 50% production output loses
- **Loss of customers -** Around 85% of businesses loses customers after power outages given that the businesses will not be able to effectively communicate with the said customers; they will not be able to meet deadlines agreed with customers and the delivery due dates will be missed

MONETARY DYNAMICS

The Reserve Bank of Zimbabwe Governor presented the 2020 Monetary Policy Statement on 17 February 2020 outlining the measures and policies being pursued by the Bank aimed at accomplishing the 2020 key strategic focus of ensuring exchange rate & price stability, the smooth functioning of the interbank foreign exchange market and providing support to economic activity.

The Chamber is of the view that there is need to build confidence and to create a conducive business operating environment. Policy pronouncements must feed into economic agents' expectations which shape the environment in the medium to long term. There is need to put mechanisms to build trust on monetary dynamics with the citizenry whose confidence need to be restored. Policy consistency and coordination is required and indications that the -6.5% economic decline for 2019 is largely explained by exogenous shocks in the form of the El-Nino and Cyclone Idai fuels the loss of confidence.

The central bank expects inflation to fall on the back of monetary targeting framework implementation, confidence building and stability in the foreign exchange market. However, the prevailing downside risks to mono-currency and the inflation outlook require more and decisive policy action in-order to steer the economy towards a sustainable disinflation path. Below are highlights from the Monetary Policy Statement and review.

Money Supply

Variable	Summary	Comments
Banking Sector Deposits	• Deposits recorded at ZWL$34.5b as at Dec 2019 • 50% of deposits concentrated across 200 entities	• The government continues to increase money supply to monetise the fiscal deficit and to finance subsidies via borrowing instruments • The above scenario feeds into the unsustainable growth in inflation and the attendant effects on the exchange rate • The RBZ is likely to use Non Negotiable Certificate of Deposits (NNCDs) to wipe away excess liquidity in the market • There is need to curtail quasi-fiscal activities - RBZ should not fuel money supply growth through funding Government expenditure

- Movement in money supply growth of more 250% Dec 2019 YoY is shows effects money supply growth given that challenges being faced in the economy such as inflation, poverty are emanating from money supply growth
- Meanwhile, there are contradictions in the MPS where it is indicated that the foreign currency deposits as a proportion of money supply went down to 37% by 31 December 2019 whilst on another note there is an indication that broad money was largely composed of deposits in domestic currency, 57.19%, while foreign currency deposits constituted 34.13% of the total
- RBZ should limit high powered reserve money targeting growth of 10-15% by end 2020, which is consistent with end of year inflation target of around 50%

Reserve Money and Broad Money Supply Drift

Year	2018	2019	M3 (YOY%)	M3 (MoM%)	RM(bn)	RM (YOY%)
Jan	7.84	9.86	25.8%		1.11	180%
Feb	7.83	10.39	32.7%	5.4%	1.67	220%
Mar	7.99	10.63	33.0%	2.3%	2.22	255%
April	8.12	11.35	39.8%	6.8%	2.33	350%
May	8.56	13.01	52.0%	14.6%	2.51	400%
June	9.14	14.77	61.6%	13.5%	3.33	430%
July	9.6	17.38	81.0%	17.7%	4.67	450%
Aug	9.5	19.69	107.3%	13.3%	6.00	480%
Sep	10.12	21.66	114.1%	10.0%	6.52	490%
Oct	10.07	24	138.3%	10.0%	6.8	513%
Nov	10.09	31	207.2%	9.5%	8.1	629%
Dec	10.01	35	249.7%	7.5%	9	711%

Foreign Currency Availability

- Foreign currency shortages are weighing on industry. Industry cannot import raw materials and this has led to low supply levels
- Forex challenges are a symptom of fundamentals which need to be addressed which include confidence deficit
- Foex challenges scare away FDI given that foreign companies do not want to operate in an environment where the foreign currency issue is volatile
- Interbank market has not been effective
- Reuters Forex Interbank Market System - With the introduction of the Reuters Forex Interbank Market System where banks are to become market makers in a user test environment, the reuters system is expected to enhance transparency, communication and ultimately, price discovery. However, there is need to put in place trading mechanisms that effectively attract buyers and sellers of foreign currency to the formal market
- The Monetary Policy Statement is silent on the time line when the reuters forex interbank market will be fully implemented – timelines are needed given that the current interbank market is not effective and is weighing on business
- From the MPS "the foreign currency deposits as a proportion of money supply went down to 37% by 31 December 2019, whilst foreign currency denominated loans in the banking sector stood at 22% of total banks' loans and advances as at 31 December 2019" – this shows that the 37% is an absolute figure given that the statement states that money supply went down to 37% but does not indicate the baseline
- On Export retentions – Capital intensive sectors such as the Mining sector should be allowed to retain 100% and others that are not capital intensive should be allowed to retain at least 80%
- Fuel dealers are accessing forex, there should be a mechanism where they should also go on the interbank market like everyone because this is an unfair subsidy to fuel dealers

Exchange rate stability

- On exchange rate stability there is no clear strategy to guarantee the stability
- Government should move from managing the exchange rate – market controls have never worked in this economy
- Continuing to treat exchange rate movements as a fundamental issue is deceiving ourselves. With the country's Balance of Payment position having improved from a deficit of US$1,387.98 million in 2018 to a surplus of US$311.2 million in 2019 largely driven by declining imports and growing exports one would have expected less pressure on the currency than it was in 2018 manifesting in a stronger domestic currency

Cash Shortages

- Cash shortages continue to weigh on Business operations and the transacting public
- On the perennial cash shortages it was highlighted that RBZ will gradually increase the notes & coins to the desired optimal proportion of bank notes and coins in circulation. A maximum withdrawal of Z$300 per week after the much hyped injection of new notes is not inspiring confidence. The market has a way of pre-empting the effectiveness of policy in gradualism. We probably need to balance the portfolio mix of money by replacing more of the RTGS with cash
- There is also a three tier pricing system for RTGS, ECOCASH and Bond which is caused by the lack of cash and ends up distorting pricing

Variable	Summary	Comments
Cash Notes and Coins In Circulation	• ZWL$1.1b (3.2% of M3) worthy of notes and coins reported in Dec 2019 to be in circulation. • The RBZ to gradually inject more cash to achieve a target of 10% of M3.	• Cash shortages continue to weigh on Business operations and the transacting public • Potentially the RBZ can inject ZWL$2.3b into circulation by way of new notes and coins

De - dollarisation

- To measure progress on de-dollarisation by the proportion of the use of the local currency in the economy vs proportion of foreign currency in banks and ignoring the amount of hard currency USD transactions taking place in the economy is deceptive
- Pronouncing a 5 year window to fully de-dollarise in face of current distortions will only fuel the uncertainty. Whilst the assurance that RBZ will not temper with the legal status of the public's foreign currency accounts is welcome, the issue still remains on confidence
- De-dollarisation framework is not convincing given that the realities on the market are pointing to re-dollarising and not de-dollarisation
- The MPS states that following the gazetting of Statutory Instruments 33 and 142 of 2019 that provided the de-dollarisation framework for the country to trade exclusively in local currency (mono-currency), the Bank is encouraged by the positive de-dollarisation process that has been taking place in the country. This is not the reality on the ground and there is no comparison on figures, its absolute compared to the relative statistics (unreliable measurements)
- Companies payrolls are becoming dollarized
- The size of the informal sector is large and that is where most transactions are taking place in foreign currency
- There is need for policy consistency given that Banking Sector Capital Requirements have been pegged in US dollars while there are pronouncements that the economy is de-dollarising
- Empirical evidence shows that inflation rates below 10%, local currency denominated investment instruments that guarantee positive returns, mandatory use of the local currency for all local transactions, sizeable foreign currency reserves, general consumer confidence in the policies, among others, are some of the necessary ingredients for a successful and sustainable de-dollarization program

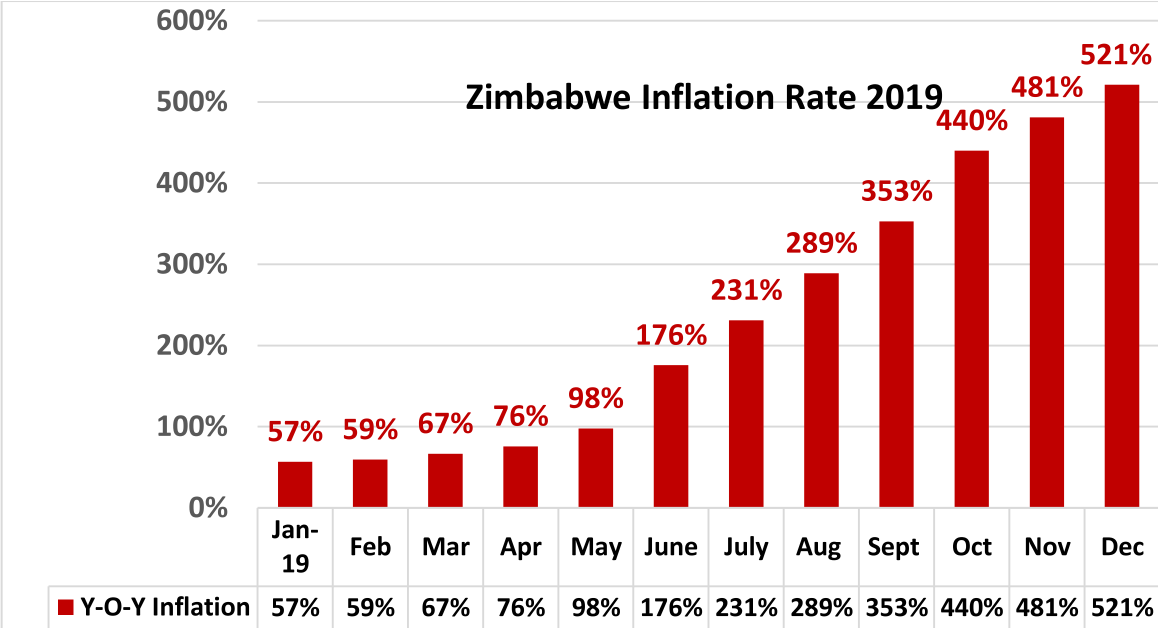
Interest Rates

- With the Monetary Policy Committee set to continue to proactively guide the market on the expected path of interest rates as part of its efforts to build on policy transparency and confidence, as Business we continue to clamour for low interest rates so as to encourage investment in the economy since borrowers will be accessing funding at sub-optimal prices

Collateral Registry

- From the Monetary Policy Statement Implementation of the Collateral Registry by June 2020 will enable the MSMEs to leverage on their movable assets to access funding from formal financial institutions. In this regard, banking institutions and microfinance institutions are required to submit to the Bank detailed strategies to support the productive sector during the period 2020-2021. The strategy document should be submitted to the Bank by 30 June 2020
- There has been much talk about collateral registry by implementation has been dragging and we are not sure if this is going to be implemented in June

Inflation



Inflation is a monetary phenomenon and has been as a result of increased Money Supply

What is needed to bring down inflation is:

- Anchored Inflation Expectations
- RM and Money Supply Growth
- An effective Interbank Market for Forex
- A uniform Exchange rate – "Law of One Price"
- Removal of all Pricing distortions
- Stabilising Fuel Prices

Foreign Direct Investment

- Foreign direct investment decline from US$717.1 million in 2018 to US$259 million in 2019 and decline in net portfolio investment inflows from US$54.7 million in 2018 to US$3.7 million in 2019 is a clear sign of low investor confidence in the economy
- The report of 299 blocked funds transactions with a value of US$861 million having been rejected for various reasons is not helping with confidence building

Operations of mobile money transfer companies and how it affects business

- Mobile money has been the biggest cash reserve in the country
- This is posing challenges on business and the transacting public given that funds cannot be transferred from one mobile platform to another mobile platform
- Business is negatively affected by the charges of not only mobile money transfer companies but banks as well, including the 2% Tax. It all adds up to the cost of doing business

Variable	Summary	Comments
Overnight Accommodation Rate	• The reference rate maintained at 35% p.a • The Treasury Bill Rate averaging 15-18%	• The government continues to borrow below the overnight accommodation rate, signalling their intention to continue to use market instruments like Treasury Bills to finance government operations.
Gold Deliveries	• Gold deliveries recorded a 17% decline from 33.6tonnes to 27.6 tonnes between Dec 2018 and 2019.	• This is going to affect foreign currency supply if the trend continues in 2020 • Erratic power supplies will continue to affect output.
Legacy Debts	• USD$457m in legacy debts to be finalised before 29 February 2020. • USD$861m worthy of payments rejected for various reasons	• The legacy debts will continue to place a strain on scarce foreign currency resources. • The practicality of the RBZ fully settling this debt is in doubt considering the dire foreign currency challenges currently being experienced.

OTHER ISSUES IMPACTING BUSINESS

Regulatory environment

- Too many Statutory Instruments governing the economy – more than 250 Statutory Instruments were introduced in 2019 and this poses a cost to business and points to **policy inconsistency**

Porous Boarders

- Smuggling has been rampant on ports of entry and this needs to be addressed and this is weighing on Business
- Locally produced goods are facing competition from smuggled goods which are sold at a cheaper price on the market

Infrastructure

- The economy continues to depend on road network which is costly for businesses instead of rail
- Dilapidation of both road and rail networks
- Water unavailability

Corruption

- Corruption has been weighing on business
- Perception risk is also a reality
- There is a lot of publicity around curbing corruption with no tangible results

Drought

- 65% to 70% of manufacturing companies are into Agro-processing but the Agriculture sector has not been performing well thereby having an impact on industry performance. Zimbabwe is also dominated by subsistence farmers

Political Noise

- Lack of buy in into POLAD by all Political Parties remains a stumbling block
- Political battles being fought beyond the borders