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Zimbabwe Equity Strategy 2015

At a Crossroads...

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At a Crossroads

Urgent need to address structural and policy issues as GDP growth continues to decelerate

GDP growth for 2014, according to the government, came in at 3.1%, underperforming average GDP growth for SSA of 5.4% during the same period. Inflation entered negative territory in 2014, closing the year at an annual inflation rate of -0.8%. We have already seen an impact in the pricing environment with top tier names Delta (DELTA: ZH) and Innscor (INAF: ZH) having effected price reductions on various lines in CY14 and Econet (ECWH: ZH) compelled to effect tariff reductions in CY15. The Zimbabwean economy is coming under increasing stress characterised by depressed aggregate demand, high unemployment, pervasive structural issues linked to poor funding and weak commodity prices in Zimbabwe's key sectors, mining & agriculture, and a persistent current account deficit. It is now imperative that government implements productive and proactive policy reform to attract the much-needed FDI and restore the country's external position as a prerequisite for accessing external financing. Policy clarity, transparency and key structural reforms must be made in order to enhance the business climate to attract FDI, boost productivity and competitiveness, and build confidence. The largest impediment to growth remains ingrained in policy inertia and the lack of a compromise solution to the indigenisation policy. We believe that 2015 will see Government becoming compelled to take a more moderate approach to indigenisation and continue to take proactive measures to normalise relations with creditors and the foreign community. The economy is forecast to grow 3.2% in 2015 according to the MoF, although this forecast is fraught with downside risks emanating from depressed commodity prices, stagnant domestic demand, adverse weather conditions and pervading liquidity shortages. In our view, GDP growth in the year will likely be closer to 2.0%. We expect deflation to persist in 2015 on subdued demand, a softening rand and bearish oil prices; corporates that are highly leveraged will be hardest-hit by the pervading deflationary pressures.

The fiscus and external accounts under increasing pressure, however international relations appear to be thawing at best

Owing to a lack of fiscal manoeuvrability, the country continues to operate a budget deficit. Recurrent expenditure, which constitutes 92% of total expenditure, is crowding out much-needed capital projects. Particularly problematic is the ballooning and unsustainable wage bill, which makes up 80% of total public spend, well above the World Bank's recommended target of 25%. Reversing the budget from consumptive to developmental has become a key priority for the government and this can only be done by managing the wage bill. The external position remains unsustainable with a large current account deficit, low international reserves and an overvalued real exchange rate. The current account deficit constitutes about 24% of GDP while our SADC peers have current account deficit under 9% of GDP. Imports so far have been in line with our expectations and we expect them to remain relatively flat to lower in 2015 on the back of low domestic demand, further depreciation of the Rand and declining oil prices. Exports however, are likely to remain relatively flat to lower as well, on the back of softening commodity prices and subdued output forecast for 2015; therefore we expect little change in the current account deficit. We re-iterate the urgent need for government to take proactive measures to attract FDI to restore the country's external position as a prerequisite for accessing external financing. Encouragingly the IMF has re-opened its Zimbabwean office (July 2014) and the EU has formally lifted sanctions (Nov 2014) on the GoZ both of which bode well for the restoration of constructive foreign relations.

ZSE bearish in 2014, underperforming most SSA peers

Zimbabwean equities performance for 2014 left a lot to be desired in a generally poor year for SSA markets. The ZSE saw a 17.8% decline in total market capitalisation for the year to $4.747bn. The benchmark Industrial Index returned -19.5%, below the average return for SSA markets (excluding SA) estimated at -0.9% for 2014, while the Mining Index was a bright spot advancing 56.6%, driven by a 220% return in Bindura (BINDURA: ZH). The general poor performance was driven by below par GDP growth, a continued lack of FDI, downward earning revisions, as well as poor sentiment exacerbated by political events particularly in 4Q14. In 2014 15 counters registered positive gains notable amongst the larger caps being National Foods (NAFH: ZH) up 70% and Seedco (SEEDCO: ZH) up 7.8%, while 40 counters recorded losses. Performances of other key names were as follows; Econet (ECW: ZH) 0%, Delta Beverages (DELTA: ZH) -27%, Innscor (INAF: ZH) -32%, Ok Zimbabwe (OKZIMBAB: ZH) - 42%, BAT Zimbabwe (BAT: ZH) -7% and Seedco (SEEDCO: ZH) +8%. There appeared to be little discernible trend between sectors as regards performance reflecting the generally poor economic environment, although retail counters were hardest hit with seven of the top ten losers on the ZSE being exposed to the Zimbabwean consumer. The top performers reflected to an extent companies involved in value accretive corporate actions.

Equities outlook for 2015; with few catalysts to change domestic conditions regional diversification & cost control is key

In the absence of meaningful and visible catalysts, indications point to sustained pressure on consumer demand and continued liquidity constraints in 2015. As a result we anticipate corporate earnings to remain weak going forward, particularly in H1. We expect run rates to remain under significant pressure this year, notwithstanding the base effect from poor FY14 earnings that may translate to relatively lower declines. In our view the key theme for corporates will be protecting margin and/or market share, potentially seeking new markets offshore, and adjusting business models to service the lower end of the market given consumer down-trading or the ability to serve the informal sector. Whilst deflation will naturally exert downward pressure on pricing of goods particularly impacting corporates that are highly leveraged, we believe that lower oil prices and reduced prices of inputs (mainly due to a weak ZAR) will assist in helping margin protection by lowering costs. Our immediate preference at this time is companies not directly exposed to the Zimbabwean consumer like Seedco (SEEDCO: ZH, rated HOLD, TP $0.98) and Bindura Nickel (BINDURA: ZH, N/R). However we believe the falls in the market valuations may also represent a contrarian entry point in some of the more defensive consumer names, such as Econet (ECWH: ZH, rated BUY, TP $0.61), Delta (DELTA: ZH, rated HOLD, TP $1.11), Innscor (INAF: ZH, rated BUY, TP $0.85) and National Foods (NTFD: ZH, rated HOLD, TP $3.87)

IH Base-case Target Market Capitalization for 2015: $5.16bn (+10% upside)

We forecast a target market capitalisation of $5.16bn for 2015, based on our bare case scenario GDP growth forecast of 2% and subsequent earnings growth of 2.8%; this represents upside of 10% from current levels. Downside risks to the forecast emanate from potential underperformance in agriculture, sluggish GDP growth and possible worsening in liquidity conditions. Weak commodity prices and the ramifications of a stronger US dollar in 2015 will likely have negative implications for flows into emerging & frontier markets, with flow likely to favour developed markets again in CY15. We believe that the market has already priced in these risks to a large extent and that there are select buying opportunities at current levels in some of the more defensive counters and those not directly exposed to the Zimbabwe consumer. Overall we remain neutral on Zimbabwe equities relative to the rest of SSA markets.

Research Team

Dzika Danha
ddanha@ih-group.com

Lloyd Mlotshwa
lmlotshwa@ihsecurities.com

Joan Takaindisa
jtakaindisa@ihsecurities.com

Carla Simleit
csimleit@ihsecurities.com

Contact Details

Physical Address
4 Fleetwood Road
Alexander Park
Harare
Zimbabwe

Tel: +263 (4) 745 133/139

Email: info@ihsecurities.com

Website: www.ih-group.com

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Executive Summary

The Zimbabwean economy is coming under increasing stress characterised by depressed aggregate demand, high unemployment, pervasive structural issues linked to poor funding and weak commodity prices in Zimbabwe's key sectors, mining & agriculture, and a persistent current account deficit (cc +/-24% of GDP). It is now imperative that government implements productive and proactive policy reform to attract the much-needed FDI and restore the country's external position as a prerequisite for accessing external financing. Policy clarity, transparency and key structural reforms must be made in order to enhance the business climate to attract FDI, boost productivity and competitiveness, and build confidence. The largest impediment to growth remains ingrained in policy inertia and the lack of a compromise solution to the indigenisation policy. A recent softening in the political rhetoric and pronouncements around the indigenisation policy has not been accompanied by key improvements in subsequent implementation. It is our view that with the elective congress (Dec 2014) now behind us and the President having finalised the structure of the Presidium and politburo, some element of stability will begin to pervade the party; allowing succession politics to take a backseat to the economy, at least in the short to medium term. We believe that 2015 will see Government becoming compelled to take a more moderate approach to indigenisation, with the focus shifting towards creating a more conducive environment for much needed investment. We have also witnessed a general thawing in international relations between Zimbabwe and the foreign community; particularly important is the removal of the EU sanctions (Nov 2014), effectively allowing direct funding to take place to the GoZ (Government of Zimbabwe). Deflationary pressures witnessed in 2014 will likely persist in 2015, with the Rand likely to soften further whilst oil prices trend lower. Whilst deflation will naturally exert downward pressure on pricing of goods particularly impacting corporates that are highly leveraged, we believe that lower oil prices and reduced prices of inputs (SA based goods a large component) will assist in helping margin protection. Government has forecast GDP growth of 3.2% for 2015, on the back of moderate growth across all sectors and particularly coming from steady growth in mining, agriculture, ICT and tourism. There exists significant downside risk to governments' forecasts however, and in our view growth will likely be closer to 2.0% in 2015. Downside risks to 2015 GDP growth forecasts include:

- **Continued weakness in commodity prices**: With the exception of nickel and tobacco, most of the commodities of which Zimbabwe is a net exporter, including sugar, gold and platinum, are likely to witness further deterioration in prices in 2015. Subdued commodity prices will likely have a negative impact on the levels of production in the affected sectors, as funding and access to capital will remain depressed, and will also thin export earnings and put further downward pressure on the current account.

- **Adverse weather conditions:** Adverse weather conditions, including a late start to the rainy season and heavy rainfall once the rains arrived (resulting in flooding and leaching) as well as an expected drought in the second half of the rainy season, are likely to have a negative impact on agricultural yields in the 2014/15 season.

- **Pervading funding shortage:** As long as hard commodity prices remain low and cost structures high, we do not expect any significant capital injections into the mining sector in the short to medium term. Furthermore, governments' growth forecasts for agriculture are premised on a $252mn Presidential Input Scheme announced earlier this year. However, so far only $10mn has been raised for this purpose according to the National Budget statement with the remainder still to be mobilised, from sources not yet apparent. Only $2.2mn has been extended for the upcoming season by development partners (vs. $19.2mn last year). Most funding is likely to come from contract growers, although the level of funding is likely to remain fairly subdued, due to floors which were placed on small grain producer prices in 4Q14 as well as cessation of the operations of the main cotton contract-growing firms in 2014.

Our Equity Strategy: The ZSE saw a 17.81% decline in total market capitalisation for the year to $4.747bn. The benchmark Industrial Index returned -19.5%, below the average return for SSA markets (excluding SA) estimated at -2% for 2014, while the Mining Index was a bright spot advancing 56.6%, driven by a 220% return in Bindura (BINDURA: ZH). Consumer-facing counters were the hardest hit while the top performers reflected to an extent companies involved in value accretive corporate actions. The key themes that we believe will underpin the performance of the ZSE in 2015 include:

- **Corporate earnings to remain subdued exacerbated by deflation:** We expect liquidity pressure to persist in CY15 resulting in a continuation of low consumer demand and generally negative sentiment. Downward trading to basic, low margin goods will likely remain a trend exerting some pressure on consumer facing stocks. Deflation will be a key theme, with corporates that are highly leveraged being hardest-hit. However the reduced prices of inputs will aid in providing some protection to corporates that are efficient in their procurement strategy and not highly geared. Stringent cost control will be significant for corporates in CY15.

- **Defence of earnings via diversification & targeting of the informal sector:** We expect management teams to increasingly look at defending earnings via diversification; on the local front through introducing new product lines to diversify offering and shore up declining volumes in existing core products. We also expect to see some continuation of M&A activity as another route to diversification. Our immediate preference at this time is companies with strong offshore earnings that are therefore not directly exposed to the Zimbabwean consumer like Seedco (SEEDCO: ZH) & Bindura Nickel (BINDURA: ZH). We generally anticipate increased appetite in local corporates to grow business outside the country; however this will result in select firms placing shareholder value at risk by engaging in new, untested business activity.

- **Financial sector relatively stable despite rising legacy NPLs:** We expect weaker, undercapitalised banks to remain under severe pressure in this year maintaining the dichotomy between the larger and smaller institutions. Despite legacy NPL's rising to 20%, the sector has in our view remained relatively stable with banks maintaining robust liquidity levels, and we anticipate minimal disruption within the sector as a whole in 2015. The focus for the sector in 2015 will continue to be dealing with the NPL issues while also continuing to re-align business models to the 'new' more informal economy.

- **Ramifications of a stronger US dollar:** Although quantitative easing has tapered off in the US, an expansionary policy has been adopted by both the Eurozone (ECB) and Japan (BOJ) implying that global liquidity will remain supportive for capital markets. However weak commodity prices and the ramifications of a stronger US dollar in 2015 will likely have negative implications for flows into emerging & frontier markets, with flow likely to favour developed markets again in CY15. In our view, the continued dollarization of the Zimbabwean economy will however put the ZSE in good stead relative to SSA peers; it is our belief that the currency protection that Zimbabwean equities offers will be a key driver in attracting flows.

With this report we continue our coverage of 16 stocks including TSL (TSL: ZH) which we initiated upon during the year. Our universe of stocks represents 82% of the market capitalization of the ZSE. Our universe trades on a market cap weighted PER to 2015E and 2016E of 13.8x and 14.0x respectively. We believe that select equities hold value at current levels, particularly those counters not directly exposed to the Zimbabwe consumer, those more resilient to the current environment (export-facing or regionally-diversified counters) and those able to access the growing informal sector or the lower-end of the market in the face of down-trading activities. We have derived a base-case target market capitalization of $5.16bn for 2015, representing 10% upside.

Valuation Table

IH Universe Valuation Table

2-Feb-15

Company	Rating	Current Price	Mkt Cap ($mn)	Current Target price	Upside/ Downside	P/E			EV/EBITDA			P/BK			Div Yield
						2014(/E)	2015E	2016E	2014(/E)	2015E	2016E	2014(/E)	2015E	2016E	2014E
Financials															
Barclays	SELL	0.04	75.36	0.02	-56.5%	14.0	12.0	10.7				1.5	1.4	1.2	0.0%
CBZ Holdings	BUY	0.10	68.72	0.19	90.4%	2.2	1.8	1.6				0.3	0.2	0.2	3.7%
FBC Holdings	HOLD	0.09	60.48	0.09	3.7%	7.6	5.0	4.6				0.7	0.7	0.6	1.3%
NMBZ Limited	BUY	0.04	15.38	0.07	66.3%	5.7	3.1	2.2				0.3	0.3	0.3	0.0%
Non-Financials															
BAT Zimbabwe	SELL	11.50	237.3	9.76	-15%	22.3	22.3	23.1	14.7	14.6	14.9	22.5	23.1	17.8	4.6%
Dairibord Zimbabwe	BUY	0.08	28.6	0.11	33.7%	-	17.24	13.5	8.7	5.1	4.5	0.6	0.6	0.6	0.0%
Delta Corporation	HOLD	1.11	1,382.6	1.28	15%	13.1	17.0	16.0	8.3	9.5	9.0	3.4	3.1	2.8	3.1%
Econet Wireless	BUY	0.50	820.0	0.61	23%	6.9	7.8	11.3	3.0	3.6	3.9	1.4	1.2	1.1	2.6%
Edgars	BUY	0.09	26.4	0.11	20.2%	6.2	7.1	6.9	4.9	6.3	6.2	1.6	1.3	1.1	0.0%
Hippo Valley	BUY	0.50	96.5	0.84	68.0%	10.7	9.3	6.9	4.3	3.6	2.7	0.4	0.4	0.4	0.0%
Innscor	BUY	0.57	307.9	0.85	49.1%	5.1	9.4	9.0	4.2	3.9	3.7	1.5	1.1	1.0	2.3%
National Foods	HOLD	3.40	232.6	3.87	13.7%	13.9	14.3	14.1	9.2	9.4	9.2	3.2	2.7	2.4	2.4%
OK Zimbabwe	HOLD	0.14	163.8	0.14	-1.9%	16.9	20.4	21.5	8.1	8.7	8.9	2.4	2.3	2.2	3.0%
Seedco	HOLD	1.02	138.4	0.98	-4.1%	20.2	12.8	11.6	11.6	9.6	9.2	2.3	1.6	1.5	0.0%
Truworths	BUY	0.01	3.1	0.02	89.8%	12.6	34.1	16.4	8.8	13.1	11.1	1.7	1.7	1.6	0.0%
TSL	SELL	0.27	94.6	0.22	-15.3%	19.0	15.9	14.4	11.3	10.2	9.3	1.4	1.3	1.2	1.5%
Weighted Averages/Totals			3,760.5			11.98	13.83	14.04	6.95	7.42	7.23	3.62	3.40	2.89	3%

Macroeconomic Overview

Global recovery moderates; growth in SSA remains buoyant on supportive external demand conditions

Uneven global recovery continued despite setbacks in the year including a rapid decline in oil prices (-59% since June 2014), a rise in geopolitical tensions and subdued investment, particularly in advanced economies. Overall, the pace of recovery is becoming more country specific. In advanced economies, the legacies of the pre-crisis boom and the subsequent crisis (high debt and unemployment) still cast a shadow on the recovery. Emerging markets are adjusting to rates of economic growth lower than those reached in the pre-crisis boom and the post-crisis recovery. The IMF forecast global growth for 2014 at 3.3%, flat at the 2013 global growth rate and weighed down by a weak first half of the year, particularly in the United States, and a less optimistic outlook for several emerging markets. Projections of a growth rebound in global markets in 2015 to 3.8% are predicated on the key assumptions of a moderating of fiscal consolidation, the continuation of highly accommodative monetary policy and a gradual decline in geopolitical tensions. For emerging markets, the rebound reflects a variety of country-specific factors (including some recovery in countries affected by geopolitical tensions and/or domestic strife in 2014, or where growth this year has been much below potential). Global factors, as aforementioned, should also support growth in emerging market and low-income developing countries. The latter is projected to exceed 6% growth in both 2014 and 2015, although a projected easing in nonfuel commodity prices will likely induce some deterioration in the terms of trade for net exporters of commodities. Short term downside risks to these growth forecasts include a worsening of geopolitical tensions and a reversal of recent risk spread and volatility compression in financial markets. Medium-term risks include stagnation and low potential growth in advanced economies and a decline in potential growth in emerging markets. Although quantitative easing has tapered off in the US, an expansionary policy has been adopted by both the Eurozone (ECB) and Japan (BOJ) implying that global liquidity will remain supportive for capital markets. However weak commodity prices and the ramifications of a stronger US dollar in 2015 will likely have negative implications for flows into emerging & frontier markets, with flow likely to favour developed markets again in CY15.

Fig 1: Global Economic Growth 2012-2016E

	2012	2013	2014E	2015E	2016E
World	3.4%	3.3%	3.3%	3.8%	4.0%
Advanced	1.2%	1.4%	1.8%	2.3%	2.4%
Emerging & Developing	5.1%	4.7%	4.4%	5.0%	5.1%
Central and Eastern Europe	1.4%	2.8%	2.7%	2.9%	3.3%
Latin America and the Caribbean	2.9%	2.7%	1.3%	2.2%	2.8%
Commonwealth of Independent States	3.4%	2.2%	0.8%	1.6%	2.5%
Sub-Saharan Africa	4.4%	5.1%	5.1%	5.8%	6.0%
Zimbabwe	**4.4%**	**3.3%**	**3.1%**	**3.2%**	**3.9%**
Middle East and North Africa	4.8%	2.5%	2.6%	3.8%	4.5%
Developing Asia	6.7%	6.6%	6.5%	6.6%	6.5%

Source: IMF

Fig 2: Selected SSA Countries Economic Growth 2012-2016E

	2012	2013	2014E	2015E	2016E
Kenya	4.6%	4.6%	5.3%	6.2%	6.4%
Nigeria	4.3%	5.4%	7.0%	7.3%	7.2%
Mozambique	7.2%	7.1%	8.3%	8.2%	8.2%
Angola	5.2%	6.8%	3.9%	5.9%	6.2%
Zambia	6.8%	6.7%	6.5%	7.2%	7.7%
Zimbabwe	**4.4%**	**3.3%**	**3.1%**	**3.2%**	**3.9%**
Malawi	1.9%	5.2%	5.7%	6.0%	5.5%
Namibia	5.0%	4.3%	4.3%	4.5%	4.6%
Botswana	4.3%	5.9%	4.4%	4.2%	4.0%
South Africa	2.5%	1.9%	1.4%	2.3%	2.8%

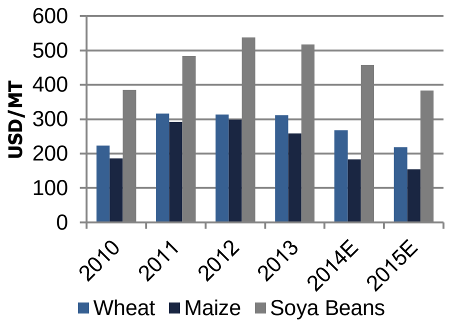
Source: IMF

Economic growth in sub-Saharan Africa was buoyant at 5.1% in 2013 and activity has remained strong in 2014 on the back of supportive external demand conditions, following further easing in external financial conditions since April 2014, and strong growth in public and private investment. Growth in South Africa has remained lackluster, dragged down by protracted strikes, low business confidence, and tight electricity supply; the significant depreciation of the rand has so far resulted in only a limited amount of much-needed external adjustment. The region's growth is projected to accelerate further to 5.8% in 2015. In many countries, activity will continue to benefit from the boost generated by infrastructure projects, the expansion of productive capacity, buoyant services sectors, a rebound in agricultural production, or combinations of those factors. Lower growth in emerging market economies, notably China, poses a protracted downside risk for the region, but especially for countries heavily reliant on commodity exports.

Global commodity prices remain subdued, negative impact on production in mining and agriculture

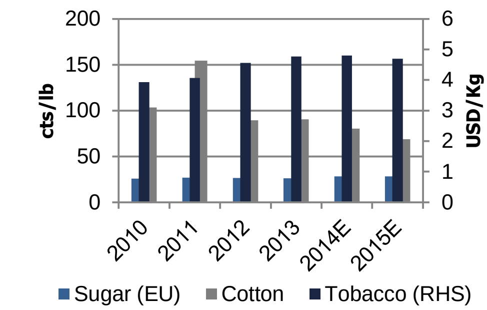
Following a peak in global commodity prices in 2011/12, a subsequent decline in commodity prices has negatively impacted the growth-driving mining and agriculture sectors in Zimbabwe. The cotton industry has been particularly hard-hit, following a 65% drop in lint prices between 2011 and 2014. Across the major commodities produced in Zimbabwe, as reflected in Figure 1 below, prices remained subdued in 2014 and are expected to decline further in 2015, with the exception of tobacco, where prices are set to remain firm, and nickel where international prices are increasing. Subdued commodity prices will likely have a negative impact on the levels of production in the affected sectors, as funding and access to capital will remain depressed. Furthermore, weak prices for commodities of which Zimbabwe is a net exporter (including sugar exports to the EU, gold and platinum), will thin export earnings and put further downward pressure on the current account. Slower growth in emerging markets that have underpinned the demand for commodities produced by Zimbabwe, particularly China and South Africa, is also of concern and may present further downside risks to current forecasts. There exists upside potential for the mining sector, emanating from the removal of sanctions on the Zimbabwe Mining Development Corporation, which is likely to boost diamond revenue going forward since Zimbabwe will start selling diamonds on an auction system and trade its diamonds at competitive prices in Antwerp. Furthermore, strengthening Nickel prices, +18% from the prior year following the Indonesian ban of nickel ore exports and expected to increase a further 8% in 2015, will offer some support to the mining sector.

Fig 3a: Global Commodity Prices (Row Crop)



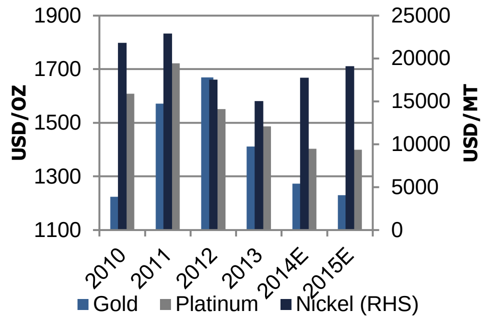
Source: IMF (August '14 update)

Fig 3b: Global Commodity Prices (Other Crop)



Source: USDA, IMF, MoF

Fig 3c: Global Commodity Prices (Mineral)

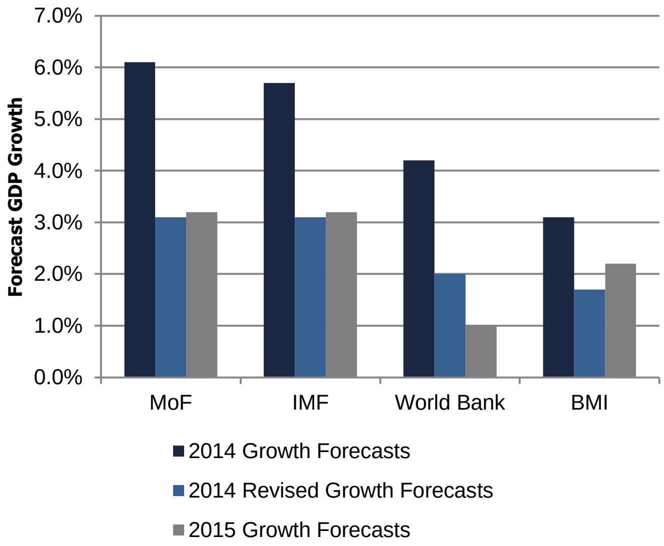


Source: IMF, KITCO

Economy at a crossroads; with post-hyperinflation growth drivers long gone, proactive reform is crucial

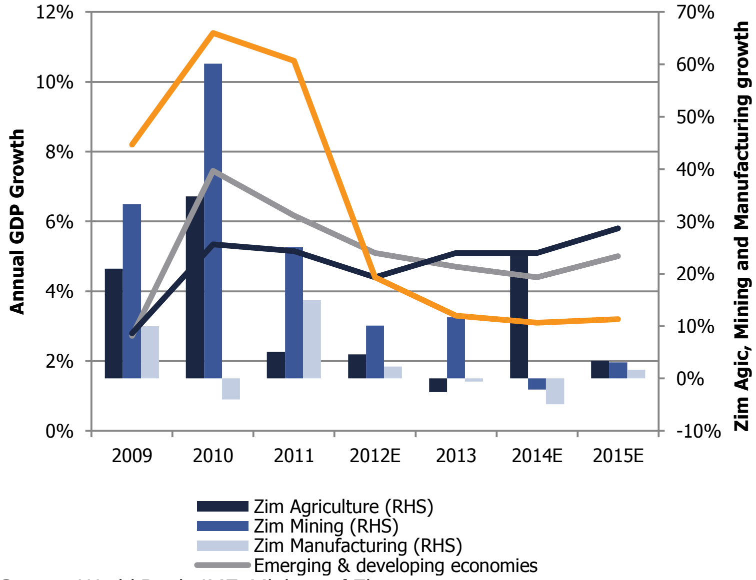
There is no doubt that the economic rebound experienced since 2009 has ended. GDP growth averaged 10.1% between 2009 and 2011, underpinned by strong performance in the mining and agriculture sectors, moderating to 4.4% in 2012 and decelerating further to 3.3% in 2013 as global agriculture and metals prices lost significant ground. At the end of 2013, the Ministry of Finance had forecast a recovery in GDP growth to 6.1% in 2014; this has since been revised downward to 3.1% following significant under-performance in mining (estimated sector growth for 2014 revised downward from 10.6% to -2.1%) and manufacturing (estimated sector growth for 2014 revised downward from 3.2% to -4.9%). The World Bank had initially forecast the Zimbabwean economy to grow 4.2% in 2014, in April this figure was revised downward to 3.0% with the World Bank citing low investment, weak mineral prices and headwinds from the global economy as reasons for the downgrade. In June, the growth forecast was again revised downward to 2.0%, on mounting evidence of weak FDI, liquidity constraints and lack of policy clarity. Similarly, the IMF slashed growth forecasts for 2014 from 5.7% to 3.1% whilst Business Monitor International (BMI) cut their growth forecasts from 3.1% to 1.7%. The baseline scenario is marked by sluggish growth in 2015 and over the medium term, with risks clearly to the downside in the near term. The MoF and IMF have forecast growth of 3.2% for 2015, a very slight improvement from 2014 growth levels. Key risks to the outlook include adverse weather conditions (late start to the rainfall, initial heavy rains followed by an anticipated mid-season drought), thinner agricultural funding, policy slippages, financial sector stress and lower than programmed tax collections and global commodity prices; Zimbabwe faces these risks with very thin buffers.

Fig 4: Zimbabwe GDP Growth Forecasts by Ministry of Finance, IMF And World Bank



Source: World Bank, IMF, Ministry of Finance

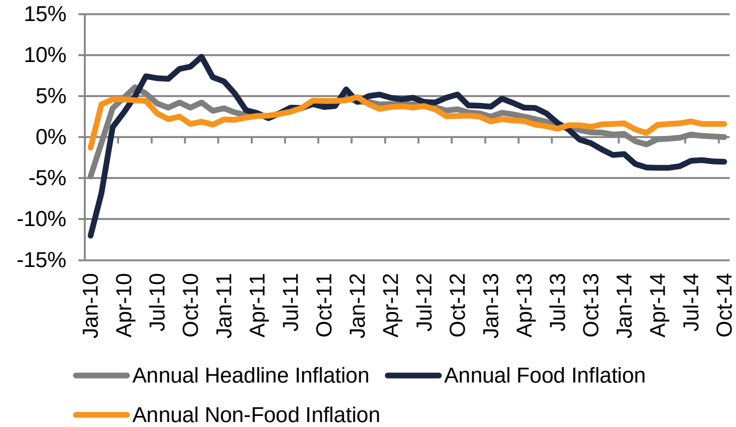
Fig 5: GDP Growth: Zimbabwe vs SSA vs Emerging & Developing Economies, 2009 – 2015E



Source: World Bank, IMF, Ministry of Finance

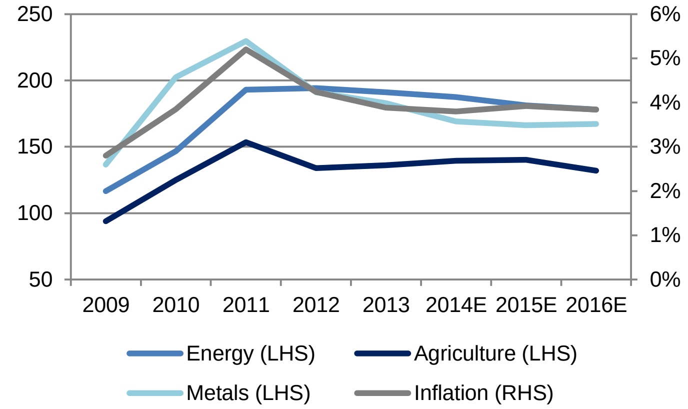
The external position is vulnerable, with a wide current account deficit, low international reserves and growing external arrears. With commodity prices looking to remain weak, and even continue retreating in the short to medium term and normalising growth in SSA and emerging market economies, Zimbabwe can no longer rely on these factors to spur growth, as was the case between 2009 – 2011. Credit and deposit growth have slowed down sharply, liquidity conditions remain tight, and the banking system remains fragile. The fiscus remains under pressure, largely due to unsustainable civil servant salaries and revenue shortfalls as the economy continues to weaken. Weak domestic demand, coupled with the appreciation of the US dollar against the South African rand has driven inflation into negative territory for most of the year (-0.8% annual inflation as at December 2014). Deflationary pressures have been stronger in tradable goods, suggesting that pass-through from a depreciating rand has played a significant role in pushing the economy into deflationary territory. The concern is that declining prices may further discourage investment in those industries targeted at the local market. Low productive capacities and hence thin revenues on the back of this development would also place further pressure on firms that are already faced with viability problems. Highly leveraged firms are especially of concern as these will be facing higher real debt burdens.

Fig 6: Zimbabwe inflation: food, non-food and headline inflation



Source: Reserve Bank of Zimbabwe

Fig 7: Global commodity prices and inflation 2009 – 2016E



Source: IMF, Ministry of Finance

Zimbabwe's economy is at a crossroads. With shaky fundamentals, sluggish demand and the inability to rely on firm commodity prices and strong growth fundamentals in other economies to continue to buoy growth, productive and proactive policy reform is now required to drive economic growth. There is a growing urgency in the need to restore the country's external position as a prerequisite for arrears clearance, resumption of debt service, and restored access to external financing. To that end, Government needs to accumulate international reserves and seek to mobilize international support for resolving the country's external debt situation. Policy clarity, transparency and key structural reforms must be made in order to enhance the business climate to attract FDI, boost productivity and competitiveness, and build confidence. Furthermore, there is a need to consolidate the fiscal position, eliminating the primary budget deficit by exercising strict fiscal discipline. The wage bill, which currently constitutes 80% of total expenditure, is unsustainable and continues to crowd out capital development projects, to which only 8% of the budget is channelled.

FDI remains subdued; for the first ten months of 2014, the country received FDI amounting US$146.6mn, compared to US$311.3mn during the same period in 2013. The currently depressed international commodity prices, coupled with the continued depreciation of the South African rand are also exerting further pressures on Zimbabwe's external position, although we expect some relief to come from declining oil prices. On the upside, we have seen some progress in the creditor re-engagement process, attested by the token re-payments made in the year and successful implementation of the first SMP programme with the IMF, which have resulted in normalizing relations with key institutions. Improved cooperation with creditors and normalising international relations culminated in the lapse of Article 96 of the Cotonou Agreement on 1 November 2014. This allows Government to work directly with the European Union (EU) and has paved way for signing of the 11th European Development Fund (EDF) in January 2015 between Government and the EU. One of the key elements highlighted in the 2015 strategy is to continue making progress in this regard, co-operating with creditors and continuing to make token re-payments throughout the year.

Economic scenarios analysis

While we are forecasting economic growth of 2.0%, we highlight that there are significant downside and upside risks to the forecast, a view held by a number of analysts in the market. Table 1 presents the range of economic forecasts that we believe to be feasible for the country in 2015.

Table 1: Economic Scenarios

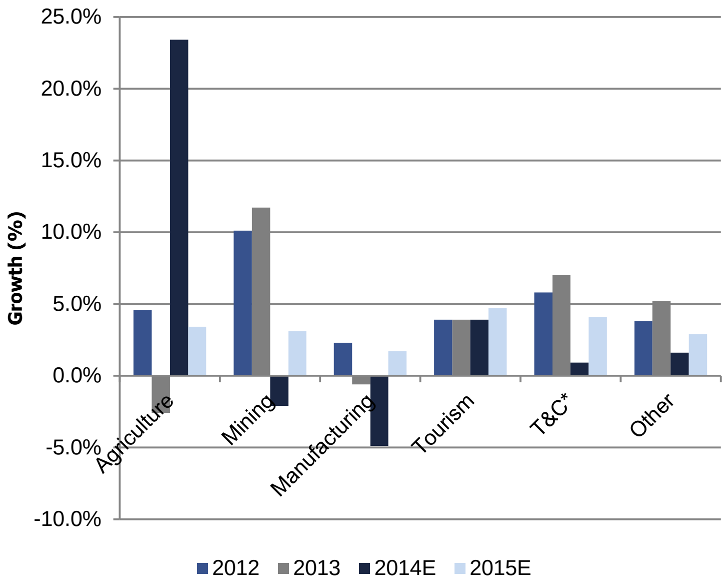
	Bear Case	Base Case	Bull Case
Agriculture Growth	**-7.5%**	**-2.0%**	**3.4%**
Underlying Assumptions	Downside risk to maize and cotton production forecasts. Assumes maize yield of 0.65 tons/ha (-4% y/y) off a total area planted of 1.45mn ha (-12% y/y) due to low levels of funding and adverse weather conditions. Cotton production negatively affected by closure of the main cotton merchants: Cottco, Olam and Carghill.	Assumes maize yield of 0.67 tons/ha (-2% y/y) off total area planted of 1.575mn ha (-5% y/y); distress in cotton industry supported by $9.5mn pledged by government	Sector supported by growth in production of maize, tobacco and cotton, underpinned by a $252mn Presidential Input Scheme. Assumes maize hectarage of 1.7mn ha (+3% y/y) and yields assumed to remain at 2014 levels of 0.68 tons/ha.
Mining Growth	**2.0%**	**2.6%**	**3.1%**
Underlying Assumptions	Sector growth weighed down by underperformance in gold (-5.0% y/y) as gold prices set to drop further, cost structures remain high and funding likely to remain scarce.	Assumes downside risks to gold production are partly offset by restarts at Metllon's Redwing mine and plant optimisation at Freda Rebecca; forecast 2.7% growth in gold output	Growth driven by strong performance in nickel (+11.6% y/y), gold (+10.3% y/y), chrome and coal (+20.9% y/y)
Manufacturing Growth	**-1.5%**	**0.1%**	**1.7%**
Underlying Assumptions	Continued de-industrialisation due to low domestic demand, working capital constraints, high costs and competition from imports - particularly as the Rand continues to deteriorate against the Dollar – likely to further contract the sector in 2015	Low capacity utilisation and low demand partly offset by supportive policy measures protecting against cheap imports and upside risk emanating from cooking oil sub-sector.	Growth hinged on supportive policy measures introduced in 2014 – particularly on dairy, beverages, furniture, cosmetics, motor vehicles and cooking oil. Some upside risk from production ramp-up in the cooking oil sub-sector following the recent and immanent acquisitions in Surface Investments and Olivine Industries respectively.
Economic Growth	**0.6%**	**2.0%**	**3.2%**

Economic Sector Overview

The economy grew 3.1% in 2014 according to the MoF, underpinned by strong performance in agriculture, which registered 23.4% growth in the year, outperforming the MoF's initial growth forecasts of 9.0%. Increased access to funding under contract growing schemes and the funds availed under government's $161mn input scheme, as well as an above-normal rainfall, boosted agricultural production in the 2013/14 growing season. Strong performance in agriculture offset a 2.1% contraction in the mining sector, which was negatively affected by retreating mineral commodity prices, notably in platinum and gold. Growth in the manufacturing sector contracted 4.9% in 2014, weighed down by antiquated plant and machinery, inflexible labour laws, cheap imports and high cost of production, among other challenges. Capacity utilisation has shed 3.3 percentage points, from 39.6% in 2013, to 36.3% in 2014. With the 2013 elections behind us, which had deterred some foreign visitors last year, tourism grew 3.9%, with estimated 2mn foreign arrivals in the year, up from 1.9mn in 2013. The SADC summit, hosted in Victoria Falls, also boosted tourist arrivals.

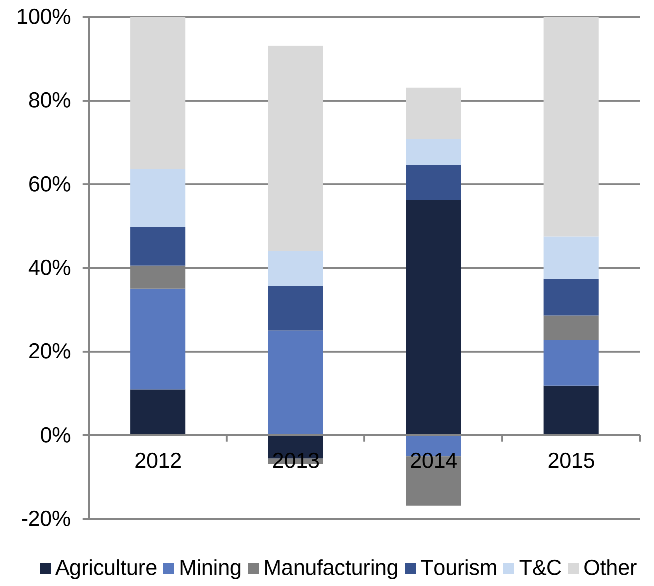
The MoF has forecast GDP growth of 3.2% for 2015, on the back of moderate growth across all sectors, as reflected in Figure 8 below, and particularly coming from steady growth in mining, agriculture, ICT and tourism. Agricultural growth for 2015 is projected at 3.4% by the MoF, supported by a $252mn Presidential Input Scheme announced earlier in the year; however, so far only $10mn has so far been raised for this purpose with the remainder still to be mobilised, from sources not yet apparent. Growth in agriculture is expected to be spurred by improved production in maize, tobacco and cotton. Growth in the mining sector is forecast at 3.1%, driven by nickel, gold, chrome and coal. Improved international prices for gold and nickel, as well as production ramp up in companies mining gold (Freda Rebecca Mine), nickel (Bindura) and coal (Hwange and Mokomo), are expected to aid in the sectors' recovery in 2015. The tourism sector is projected to grow by 4.7 % in 2015, following the implementation of the Tourist Policy, launched in July 2014 to promote domestic and international tourism in the country, as well as the introduction of the UNI-VISA project between Zimbabwe and Zambia. The manufacturing sector is expected to register a marginal growth of 1.7% in 2015, hinged on sustained implementation of supportive policy interventions announced in 2014. These measures, among others, relate to promoting competitiveness of the domestic industry through reviewing of import tariffs for selected sectors as well as downstream benefits from anticipated positive performance of the agriculture sector. The World Bank has forecast GDP growth for 2014 at a more moderate 2.0% and expects growth in 2015 to slump to just 1.0%, weighed down by liquidity constraints, low investment and weak mineral prices.

Fig. 8: Sectoral growth, 2012 – 2015E



***Transport and Communication* *Source: Ministry of Finance*

Fig. 9: Contributions to Economic growth 2012-2015E



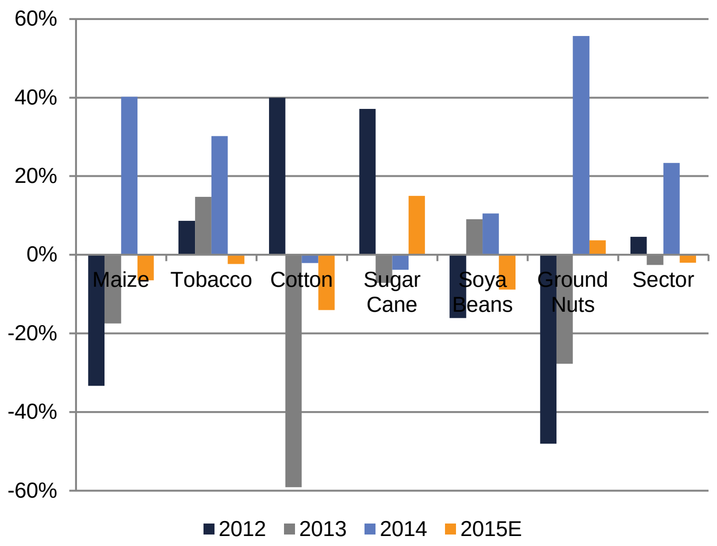
***Transport and Communication* *Source: Ministry of Finance*

Agriculture: Strong performance in 2014 but significant downside risk to government's 2015 outlook

Agricultural performance Zimbabwe is highly dependent on the weather outturn and access to funding and/or inputs. This is because, following the land redistribution program, farming is dominated by communal and small scale (A1) growers who do not have irrigation and have limited access to funding. The fact that most of these farmers do not hold title deeds severely restricts agricultural funding from traditional lending institutions that will not provide credit to farmers without security of tenure. Over 90% of Zimbabwe's agricultural land is now de facto state land and capital formation in agriculture has become heavily reliant on resources from the fiscus as private investment remains minimal due to the lack of clearly defined property rights. As the fiscus comes under mounting pressure, so crucial funding to the agricultural sector continues to dry up. The past two years were characterised by below-average rainfall and temporal distribution of the rain received, with too little or too much rain received at certain times of the season. Furthermore, in the midst of a liquidity crunch and in the absence of any credible collateral, credit from lending institutions dried up and government failed to avail sufficient funding for inputs as the fiscus came under mounting pressure. As such, agriculture has underperformed in recent years, growing a moderate 4.6% in 2012 and contracting by 2.6% in 2013. Fortunes turned in 2014 when the La Niña weather pattern brought normal to above normal rainfall to Zimbabwe and, ahead of the 2013 elections, government pledged to support 1.6mn households through a $161mn agricultural input scheme in the 2013/14 agricultural growing season. As a result of favourable weather conditions and funding support, the sector grew a healthy 23.4% in 2014. This growth was led by strong performance in maize and tobacco output, registering growth of 44% and 30% respectively from output achieved in the prior year.

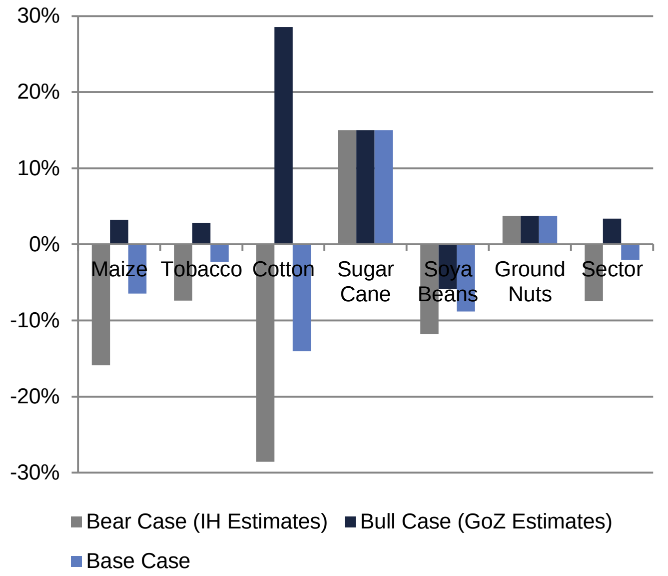
Government has forecast the sector to grow a more moderate 3.4% in 2015, supported by the $252mn Presidential Input Scheme announced earlier this year; however, so far only $10mn has been raised for this purpose with the remainder still to be mobilised, from sources not yet apparent. Growth in agriculture is expected to be spurred by improved production in maize (+3% y/y), tobacco (+3% y/y) and cotton (+32% y/y). We are far less optimistic about the upcoming agricultural season as there exists significant downside risk to government's forecasts. Adverse weather conditions, including a late start to the rainy season and heavy rainfall once the rains arrived (resulting in flooding and leaching) as well as an expected drought in the second half of the rainy season, are likely to have a negative impact on yields in the 2014/15 season. Furthermore, we anticipate severe funding shortages since Government has only mobilised $10mn (according to National Budget) funding so far for the Presidential Input Scheme (compared to $64mn that had been spent on agricultural inputs this time last year under the Government Input Scheme) and only $2.2mn has been extended for the upcoming season by development partners (vs. $19.2mn last year). Most funding is likely to come from contract growers, although the level of funding is likely to remain fairly subdued, due to floors which were placed on maize and other grain producer prices in 4Q14 as well as cessation of the operations of the main cotton contract-growing firms in 2014, namely Cottco, Olam and Cargill. Therefore, we expect lower hectarage and yields in the upcoming season, compared to government's optimistic forecasts. As reflected in Figure 11 below, in the bear case scenario we expect the sector to contract by 7.5% in 2015, Government's forecasts form the bull case scenario for the sector (+3.4%) and the bear case anticipates a 2.0% contraction in the sector.

Fig 10: Agriculture sector performance 2012-2015E



Source: Ministry of Finance & IH Estimates

Fig 11: Agriculture sector performance; bear, base and bull case scenarios



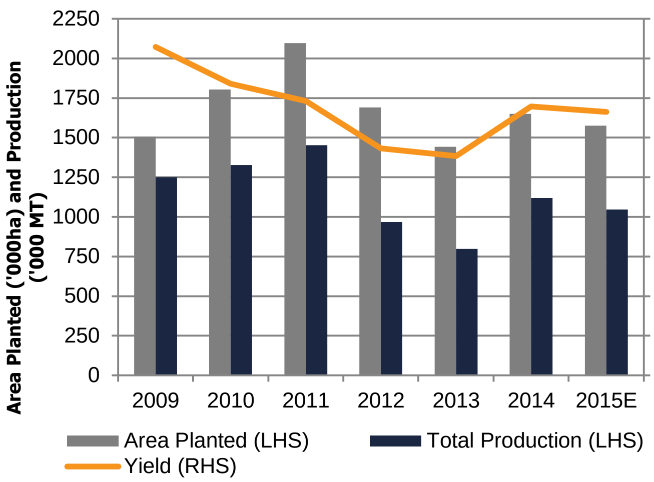
Source: Ministry of Finance & IH Estimates

Government estimates that 1.4mn tons of maize was produced this year off 1.65mn ha planted; however consensus amongst various players in the sector, including the Commercial Farmers Union, have estimated output at a more moderate 1.12mn tons. Total area planted increased 14% from the prior year, due to increased availability of funding from the public and private sectors. Government availed a $161mn input programme, of which $157.9 was set aside for inputs for farmers, specifically to buy 16,285 tons of seed and 243,000 tons of fertiliser. By the time the budget statement was released in early December 2013, $64mn worth of inputs had been distributed to farmers, including 15,242 tons of seed. Furthermore, the Food and Agricultural Organisation (FAO) in conjunction with other development partners, raised $19.25mn for the 2014 summer cropping season. A normal to above normal rainfall season also saw yields increasing a significant 23% from the prior year to 0.68 tons per hectare, to produce 1.12mn tons of maize, up 40.3% from the prior year.

Government anticipates positive growth in maize production in 2015. Whilst output estimates have not been disclosed, Government are targeting hectarage of 1.7mn ha, a 3% increase from the prior year. It appears that they have also assumed yields remain at 2014 levels of 0.68 tons/ha, translating to output of 1.16mn tons of maize (+3% y/y). Production is to be supported by funds availed under the $252mn Presidential Input Scheme, of which $181.4mn will be channelled to 1.6mn households farming maize and small grain. However, given that the significant amount of pressure on the fiscus, we remain sceptical that these funds will be mobilised in time to distribute the inputs to farmers before the end of the planting season. At the time of release of the 2015 budget statement on 28 November, only $10mn had been raised under the scheme through budget support, and only 774.8 tons of maize seed had been distributed to farmers, almost half of what had been distributed by the same time last year. They shaded area in Figure 13 below shows the portion of funds which had been mobilised by the beginning of December in 2014 and 2015, it is evident that funding and input availability is seriously lagging for the 2014/15 season. Development partners have extended only $2.2mn for the 2015 agricultural season, compared to the $19.25mn in agricultural support provided last year. Private sector support is also being jeopardised by the minimum producer price which was imposed on maize and other small grain, passed in August 2014 and effective from April 2014, under Statutory Instrument 122 of 2014. The SI set the producer price for maize at $390 per tonne, well above the import parity price of $305 per tonne and the average producer price of $320 which was being realised prior to the imposition of the price floor. Whilst we have seen a relaxation in the implementation of this policy, with maize import permits being allocated in Jan 2015, we believe that it may have had somewhat of an adverse impact on investment in contract schemes in 4Q14. We believe it may have deterred some firms from investing in contract schemes since the producer price of $390 is prohibitively expensive in an environment where firms cannot pass such an increment on to the consumer without serious negative implications on sales. That said, most of the funding for the upcoming season is likely to come from contract growers, National Foods (NAFH: ZH) has invested $6.2mn into contract farming for the 2014/15 agricultural season spread across maize, wheat and soya bean crops, with the combined hectarage covering 7500ha with total output expected at 50.3k MT.

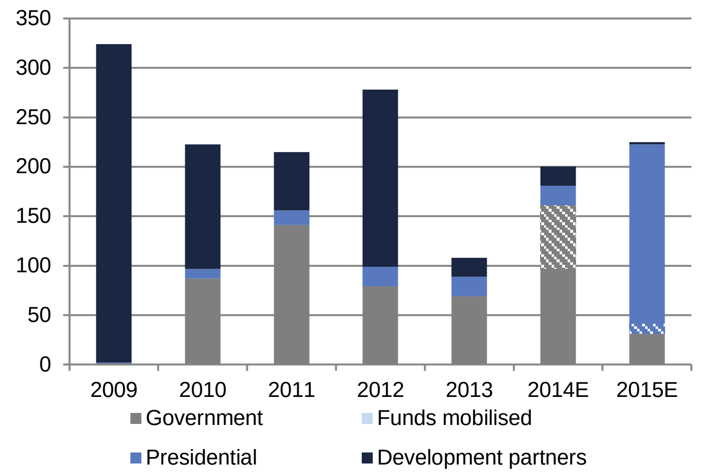
There is little in the way of relief from weather forecasts; the rains started late this year and when came down heavily when they did arrive, causing flooding and leaching in many regions across the country. Furthermore, the meteorological station has forecast a drought in the second half of the season. Adverse rainfall patterns will likely have a negative impact on yields; we expect yields to decline 4% y/y to 0.65 tonnes per hectare. Taking into account these downside risks, our maize output forecasts are much more bearish; we anticipate 943k tonnes of maize off a total area planted of 1.45mn ha, representing a 16% decline in output from 2014 levels. The base case scenario, which is an average of Government and IH forecasts, assumes maize output of 1.05mn tonnes, down 6% y/y, as reflected in Figure 12 below. This is based off a total area planted of 1.58mn ha and an average yield of 0.67 tons/ha.

Fig 12: Maize Production: 2009-2015E



Source: Ministry of Finance, Ministry of Agriculture & IH Estimates

Fig 13: Agriculture funding 2009-2015E

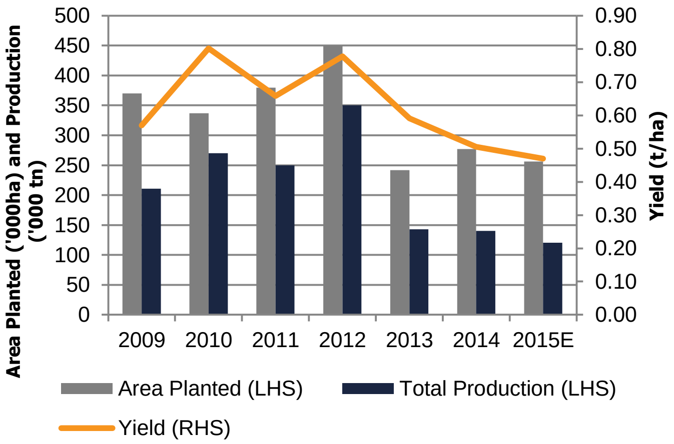


Source: Ministry of Finance, Ministry of Agriculture & IH Estimates

The cotton industry in Zimbabwe remains under severe stress. Following the spike in international lint prices in 2011, the subsequent decline in prices has wreaked havoc on the local cotton industry, deterring cotton farmers and financiers alike. As prices started to decline, most farmers abandoned cotton for more lucrative crops like tobacco, where funding is more readily available. Cotton merchants, whose contract schemes constitute about 98% of cotton production, came under significant pressure from depressed margins and low output. The fragmented structure of the industry led to issues of side-marketing, whereby some merchants began deliberately paying higher prices to entice sellers, including those holding contracted crop. Side-marketing and the resultant high default rates have proved to be the biggest challenge to viability and profitability of cotton merchants and therefore the sector. Traditional funding institutions prefer to fund crops with a low non-performing probability and target crops with well-structured and organised value chains such as tobacco, sugar cane and soya beans. Thus, funding for the cotton sector remains scarce.

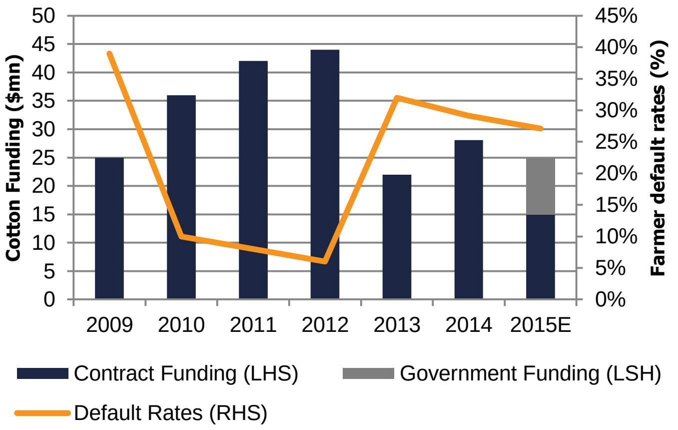
Cotton production in 2014 remained depressed at 140k tonnes, 2.1% below output levels achieved in 2013. In a bid to relieve the industry and aid value creation, Government has pledged $9.5mn towards inputs for 300k cotton farmers for the 2014/15 growing season. Through this support, government aims to raise total hectarage by 23k ha to put 300k ha under the crop, to produce180k tonnes of output, implying a yield of 0.60 tonnes per hectare. This assumes a 19% increase in yield and a 29% increase in output compared to the prior year. We remain sceptical however that this is achievable given the prevailing issues in the industry and withdrawal of funding from the major players, Cottco, Olam and Carghill, all of whom ceased operations in 2014 due to viability issues. Again, it remains to be seen where government will source the $9.5mn in funding, which in our view stands as a significant downside risk to government's production forecasts. Funding from contract growers will also contract in 2015 due to closure of the major players in the market; for the same reason we expect default rates to fall since there are fewer buyers in the market. Furthermore, we believe a yield of 0.60 tonnes per hectare is highly optimistic, given the weather conditions this year and that a yield of 0.51 tonnes per hectare was achieved last season, when weather conditions were favourable. Taking into account these downside risks, we have forecast a more moderate yield of 0.47 tonnes per hectare (-7% y/y) and believe it more probable that the area planted will be closer to 200 hectares of cotton. Assuming a yield of 0.47 tonnes per hectare and an average of IH and Government forecasts for area planted, the base case scenario per Figure 14 below, assumes cotton output of 120k tonnes, down 14% from the prior year.

Fig 14: Cotton Production: 2009-2015E



Source: Ministry of Finance, IH Estimates

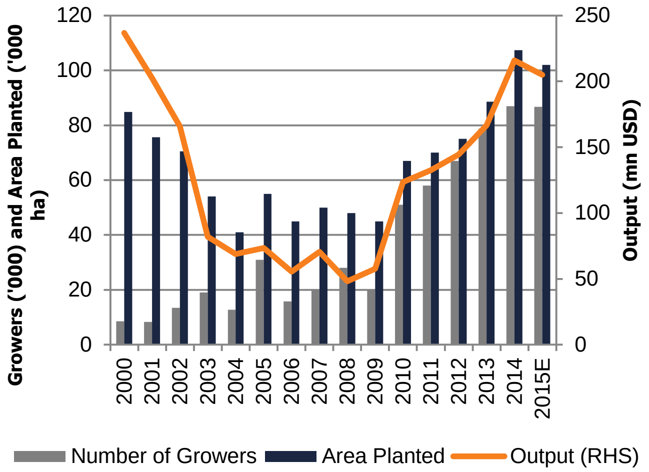
Fig 15: Cotton Funding and contract default rates 2009-2015E



Source: Ministry of Finance, IH Estimates

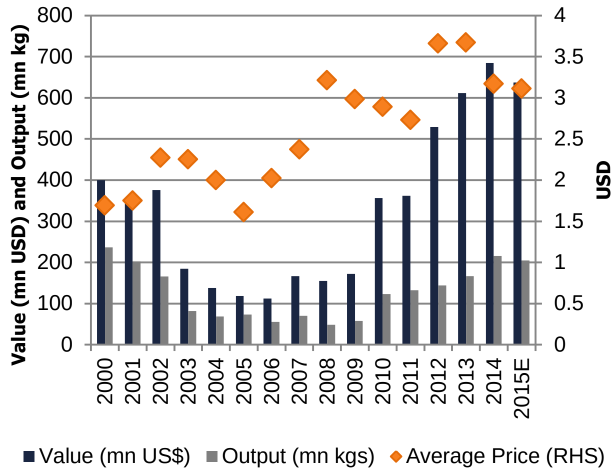
The other crop backing Government's agriculture growth forecast for 2015 is tobacco, which government expects to increase 3% from the prior year to 222mn kgs. So far, 86,751 growers have registered for the season, compared to 91,278 growers who had registered by the same time last year. Government projects overall hectarage of 90k ha, 16% below the 107k ha planted last year. Whilst we believe that the area planted will be closer to 102ha, based on the number of growers being 5% lower than last year and downside risk to yield due to adverse rainfall conditions, we anticipate tobacco output of 200mn kgs, 7% down from the prior year. The base case, assuming area planted of 102mn kgs and similar yields to those obtained last year, assumes output of 205mn kgs, 2% down from 2013 output levels. International tobacco prices are forecast to fall 2% to US$4.7/kg; we expect local prices to behave similarly, coming in 2% lower than 2013 levels at US$3.11/kg. As such, we anticipate tobacco value of US$638mn in 2015, 7% lower than the US$685mn realised from tobacco in 2014.

Fig 16: Number of growers, area planted and output



Source: TIMB, IH Estimates

Fig 17: Tobacco Output, Value and Average Price



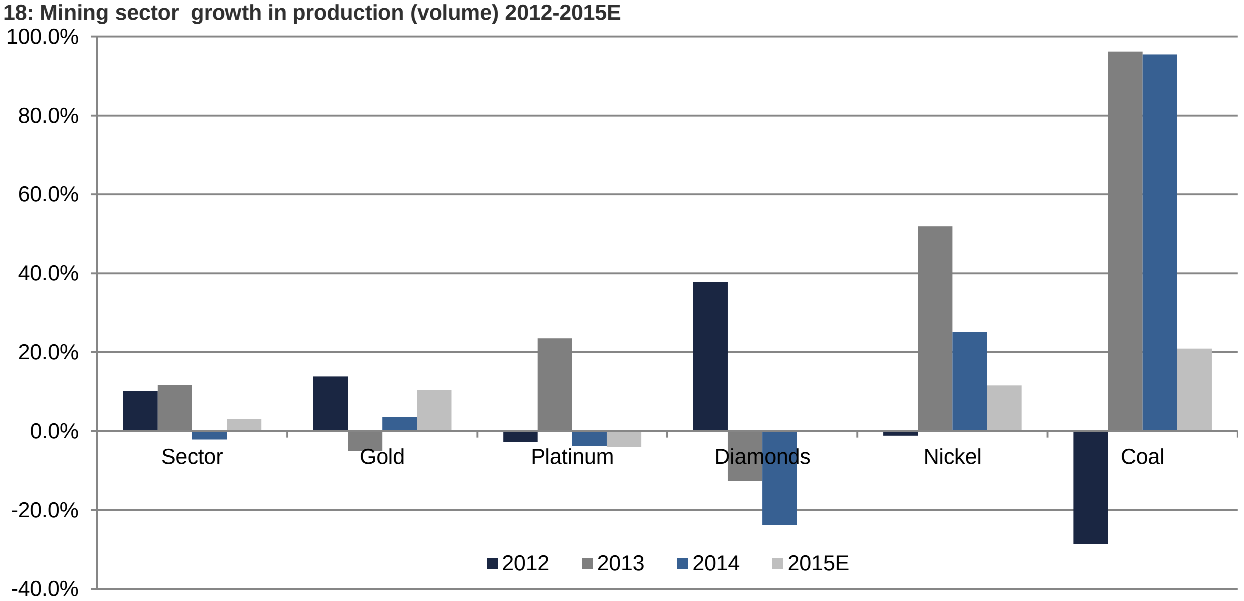
Source: TIMB, IH Estimates

Mining: Depressed commodity prices remain a drag on the sector

The mining sector has been underperforming over the past three years, mainly due to depressed mineral prices which has been one of the driving forces behind government's initiatives towards beneficiation in order to make the sector less vulnerable to price shocks. In 2012, the Ministry of Finance initially projected the sector to grow 15.9% but actual growth was 8.0%. In 2013 actual output grew 6.5% compared to government's initial growth forecasts of 17.1%. Once again, in 2014 the mining sector was initially projected to grow by 11.4%, largely driven by anticipated increased output for nickel, coal, gold and diamonds. However, continued weak international prices for some minerals, frequent power outages, obsolete equipment and inadequate funding for re-capitalisation undermined performance during the year. Consequently, output for gold, platinum and diamonds were subdued, necessitating a downward revision of sector growth to -2.6%.

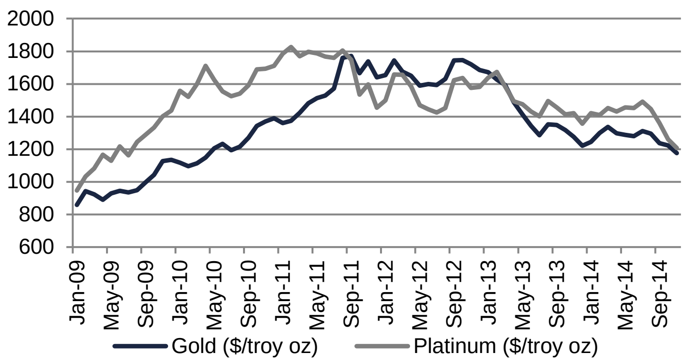
According to the World Bank's Commodity Markets Outlook Report (October 2014), commodity prices are expected to remain weak throughout 2015. The demand for precious metals has been low because of limited appetite for them on the global market, especially by China which consumes almost half of global metal supplies. Per Figure 18 below, the IMF also anticipates that mineral prices (including gold, chrome, platinum and coal) will remain depressed in 2015, with the exception of Nickel, where prices are on the rise. In light of this, government has forecast moderate growth in the sector of 3.1% in 2015, driven by nickel, gold, chrome and coal. We believe that even this may be optimistic however, given the significant downside risks to Governments' expectations for gold output and prices in 2015.

Fig 18: Mining sector growth in production (volume) 2012-2015E



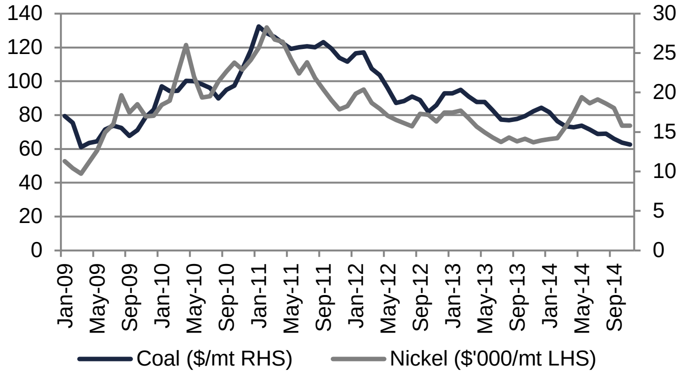
Source: Ministry of Finance

Fig 19: Gold and Platinum Prices 2009-2014



Source: IMF

Fig 20: Coal and Nickel Prices 2009-2013



Source: IMF

Table 2: Metals and Minerals Prices 2009-2016E

	2009	2010	2011	2012	2013	2014E	2015E	2016E
Gold ($/troy oz)	1135	1224.5	1571.5	1669.0	1411.2	1273.4	1230.0	1,345
Platinum ($/troy oz)	1,437	1609.0	1721.9	1551.5	1486.9	1403.5	1400.0	1,384
Coal ($/mt)	64.7	91.6	116.3	92.9	80.2	76.4	75.4	75.4
Nickel ($/mt)	14,672	21,810	22,909	17,542	15,030	17,738	19,087	19,111

Source: World Bank

Despite a 30% decrease in gold prices from monthly averages of US$1,671 per ounce in January to US$1,140 per ounce in December, gold production increased a moderate 3.6% in 2014 to 14,500kg. This was largely due to an increase in recorded output by small scale miners, after Fidelity Printers and Refiners was made the sole buyer and exporter of gold from 1 January 2014. With increased enforcement and monitoring, gold contribution by small scale miners increased from about 250kg (approx.8,800oz) per month in 1H14 to over 400kg (14,000oz) per month in 2H14. Table 3 below shows that production at the large-scale gold mines was fairly flat on last years' levels, whilst the closure of Dalny Mine in August 2013 negatively impacted on overall output levels. The high cost structure remains problematic, with the current high tax and power cost base exacerbated by the low and falling gold prices. A 5% increase in NEC mandated salary and wage levels, affected from 1 January 2014, put further pressure on large-scale mining operations. However, effective 1 October 2014, the royalty rate for large-scale gold producers was reduced from 7% to 5% which has eased some of the cost pressure. Nonetheless, further reductions will be necessary to reach a sustainable cost base if gold prices remain at the current depressed levels or indeed fall further.

Table 3: Gold Production, Costs and Average Prices for key gold mines; 2013-2014

Mine	Period	2013 Production (oz)	2014 Production (oz)	2013 AISC* ($/oz)	2014 AISC ($/oz)	2013 ARP** ($/oz)	2014 ARP ($/oz)
Blanket Mine	10 months to Oct 14	45,464	45,527	1,112	1,035	1,666	1,402
Freda Rebecca	12 months to Sept 14	58,704	56,510	1,186	1,161	1,319	1,234
Golden Quarry	9 months to Sept 14	10,265	11,006	1,454	1,071	1,502	1,267
Dalny Mine	closed in August 2013	9,348	-	n/a	n/a	n/a	n/a
Metallon Gold***	12 months to Dec 14	100,000	82,000	950	900	1,400	1,301
Renco Mine	6 months to June 14	9,595	11,429	n/a	n/a	1,313	1,164
Total Large Scale		233,376	206,472	1,176	1,042	1,440	1,274

**All In Sustaining Costs*
***Average Realised Price*
**** Includes How, Shamva, Mazowe and Arcturus mines*

Source: Company Data; IH Estimates

Government expects a 10.3% increase in gold production in 2015 to 16,000kg, on the back of 'capital injections by mining houses, rebound in international gold prices as well as production ramp-up at Freda Rebecca Mine'. However, in light of the IMF and World Bank's forecasts of lower average gold prices in 2015 (-4% y/y), we believe there is significant downside risk to these forecasts. Furthermore, in the face of serious liquidity shortages and a lack of investor appetite for Zimbabwe, as long as gold prices remain low and cost structures high, therefore squeezing profitability and investor returns, we do not expect any significant capital injections into the gold mining sector in the short to medium term. Improvements in performance across the large scale mines requires the installation of additional capacity, otherwise the mining operations will remain largely dependent on external, uncontrollable factors such as the gold price, key input costs and taxes levied on the gold mining industry. On the upside, Metallon's Redwing mine is set to be re-opened mid-2015 whilst plant optimisation at Freda Rebecca is to increase production from 4Q14, following various modifications that were undertaken in 2014 to improve mill efficiency. Furthermore, the registration and licensing of custom millers and gold buying centres across the country is expected to plug gold leakages, thereby leading to improved gold deliveries to Fidelity Printers and Refiners. Already, a total of 11.1 tons of gold was delivered to Fidelity Printers and Refiners by October 2014, surpassing the minimum annual requirement of 10 tons for the country's re-accreditation into the London Bullion Marketers Association.

Platinum production fell 4% from 13,000kg in 2013 to 12,500kg in 2014, weighed down by the closure of Zimplats' Bimha Mine in August 2014 due to underground collapse. The closure is estimated to have negatively affected annual production by around 70,000 platinum ounces (approx. 2,100kgs). The impact on platinum output was partly offset by a production ramp up at Zimplats' Mupfuti Mine. Platinum output is projected to decrease a further 4% in 2015 to 12 000kg, weighed down by depressed international platinum prices.

Nickel Production increased a significant 51.9% in 2014 to 15,020 tons, outperforming initial expectations of 24% growth in nickel production in 2014. Production was boosted by significantly improved performance at Bindura Nickel Corporations' (BNC) Trojan Mine, which shipped its first concentrate since its restart in April 2013. A new mining plan was devised for Trojan Mine, which was signed off in September 2013 following a competent person's review. The result was that higher grade ore (massives) could be accessed earlier in the life of the mine; the increased grade enabled BNC to supply more nickel into the market in 2014. Nickel production was also supported by firmer nickel prices in 2014, which improved by around 18% from the prior year following the Indonesian ban of nickel ore exports. Nickel production is forecast to increase a further 25.2% in 2015, supported by rising nickel prices (+8% y/y) and the resuscitation of the matte smelter refinery at BNC which is earmarked for 1Q15.

Coal output is projected to increase 20.9% to 7.8mn tons in 2015, from 6.45mn tons in 2014. The strong performance is largely attributed to anticipated production ramp-up following capital injections by Hwange Colliery Company, and improved output at Makomo Resources, emanating from the use of the washing plant.

Manufacturing sector remains depressed in the face of low domestic demand

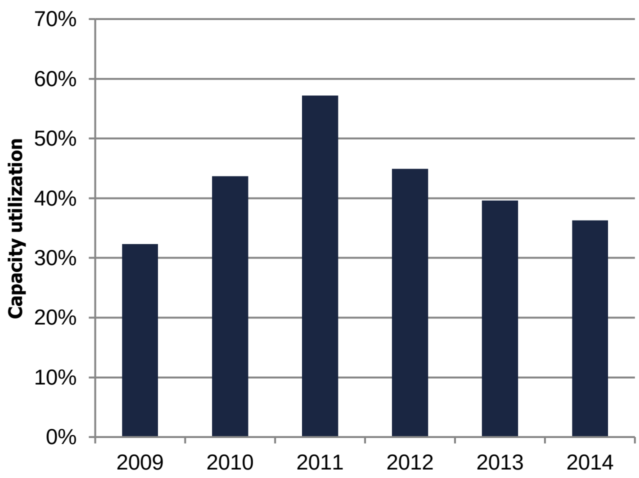
The Manufacturing sector remains a drag on the economy as deindustrialisation has reached catastrophic levels. The sector contracted 4.9% in 2014, with capacity utilization once again declining, from 39.6% in 2013 to 36.3% in 2014. The factors affecting industry and limiting capacity in the manufacturing sector remain unchanged with industry players citing low domestic demand, working capital constraints, competition from imports and antiquated machinery and machinery breakdowns as the primary constraining factors. As the Rand continued to depreciate against the Dollar throughout 2014, competition from South Africa, from which 41% of local industry competition emanates, intensified and has been a leading factor in pushing Zimbabwe into deflationary territory.

In 2015, the sector is expected to register a marginal growth of 1.7%, hinged on sustained implementation of supportive policy interventions introduced in 2014. These measures, among others, relate to promoting competitiveness of the domestic industry through reviewing of import tariffs for selected sub-sectors such as motor industries, beverages, clothing industry and leather industry. Table 4 below reflects the key policy changes affected in 2014 on sub-sectors of the manufacturing sector (excludes meat, vegetables and other miscellaneous edible preparations), mainly aimed at protecting the local industry against cheap imports. However, it should be noted that low demand is the key constraint to capacity utilisation in the sector and these policies (particularly import tariffs and increased excises) tend to push up the cost of living and therefore place further downward pressure on disposable income which in turn has an adverse effect on local industry. Furthermore, the downstream effects of an anticipated subdued agricultural season also pose downside risk to the manufacturing sector growth forecasts.

Pertinent excise reviews included the reduction of excises on clear beer from 45% to 40%, effective from 1 January 2015 and an increase in the excise duty on cigarettes from $15 per mille to $20 per mille, with effect from 1 December 2014. These respective reviews have positive implications for Delta and negative implications for BAT, who have responded by adjusting their respective prices. A tobacco levy on tobacco growers at a rate of $0.015 of each dollar of the selling price was introduced, which will negatively affect tobacco farmers and merchants alike. However, merchants such as TSL, who export most of their tobacco, will benefit from the corporate tax reductions outlined in the 2015 Budget Statement, applicable to companies who export 30% or more of their output.

Some upside risk emanates from the cooking oil sub-sector following a ramp up in production by local cooking oil manufacturer, Surface Investments, after Wilmar acquired a stake in the company last year. We expect Olivine Industries to increase production in 2015 following the acquisition of AICO's stake which went under tender in 4Q14 by a Wilmar related entity, expected to take place in 1Q15. Local cooking oil production will be supported by declining imports, following an increase in import duties on cooking oil, edible fats and soaps from 10% to 40%, affected in August 2014.

Fig 21: Manufacturing sector Capacity utilization (%)



Source: Ministry of Finance

Table 4: Policy changes effected in 2014 affecting the manufacturing sector

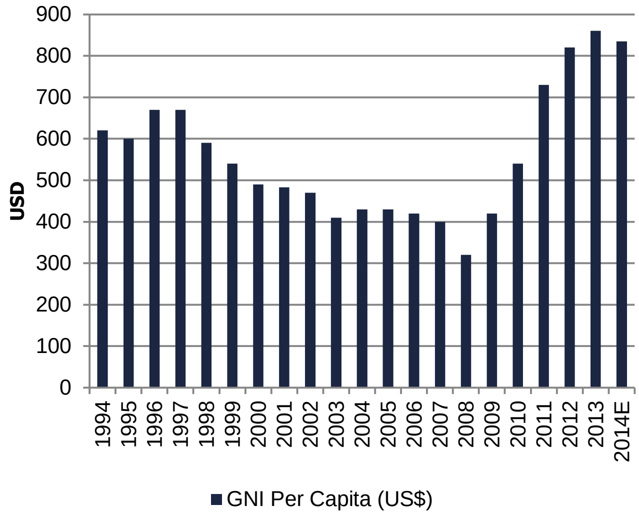
Sub-Sector	Policy changes effected in 2014
Export Tax on Raw Hides	Exempt from export tax, the sale of raw hides and skins for the period January to December 2014
Customs Duty on Motor Vehicles	Proposed tax measures as follows: single cab from 20% to 40%; Double cab from 40% to 60%; Buses from 0% to 40%; passenger motor vehicles of engine capacity below 1500cc from 25% to 40%. (1 Nov 14)
Customs Duty on Textiles and Clothing	Levy customs duty on blankets imported as raw materials (1 Oct 14)
Beverages	Excise on clear beer reviewed downwards from 45% to 40% (1 Jan 15); import tariffs on flavoured waters, other non-alcoholic beverages and other clear beer increased from 0 to 10% + excise (SADC region, from 1 Oct 14)
Dairy Products	Milk and cream import duty revised upward from $0.25/l to $0.50/l; other milk and cream from $2.50/kg to $5/kg; fermented milk and yoghurt from $10 to $25 + $0.25/l (SADC region, from 1 Oct 14)
Cigarettes	Excise duty was increased from $15 per 1000 sticks to $20 per 1000 sticks with effect from 1 Dec 14
Cement	Import tariff increased from 15% to 25% + surtax for Portland cement and white Portland cement; and for other petroleum jelly the tariff has been increased from 10% to 25% + surtax (SADC region, from 1 Oct 14)
Perfumery, cosmetics and soaps	Import tariff on various products in the sub-sector increased from 15% to 25% + surtax (SADC region, from 1 Oct 14)
Wooden furniture	Import tariff increased from 10% to 25% + surtax (SADC region, from 1 Oct 14)
Fuel	Excise duty on diesel and petrol was increased from 25c and 30c respectively, to 30c and 35c (15 Sept 14)
Tobacco	Reintroduction of a tobacco levy on growers at a rate of $0.015 of each dollar of the selling price (1 Jan 15)
Cooking oil, fats and soaps	Import duty on cooking oil, margarine, soap tablets and bars and washing powder increased from 10% to 40% (Aug 14)

Source: Ministry of Finance

Retail (Consumer) Sector: Informalisation and consumer down-trading key trends going into 2015

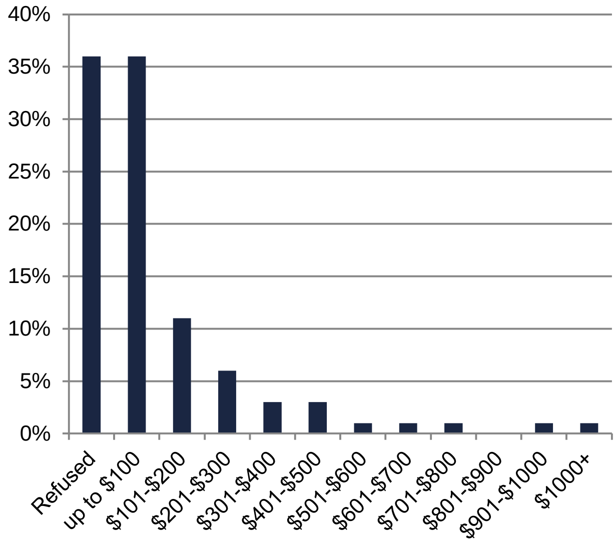
2014 has been characterised by the ongoing trend of consumer down-trading with a clear shift towards staples taking place, as Zimbabweans' incomes come under increasing pressure and unemployment continues to rise. The World Bank estimates Zimbabwe's Gross National Income (GNI) per capita in 2014 at $835, 3% lower than 2013 GNI levels. According to a ZAMPS consumer survey, of the respondents who disclosed their income levels, over 47% revealed they earn less than $200 per month. The Finance Minister has estimated that only 500,000 people or just 4% of the population are formally employed in Zimbabwe, and half of them are government workers. The latter have been stretched in 2014; although the civil servant salary increment promised in January 2014 was affected in April 2014, with the fiscus under mounting pressure government has been paying civil servants later in the month than they used to. Often, government workers will receive their salaries in arrears, in the first week of the following month. Furthermore, payment of 2014 bonuses has been staggered, with some civil servants yet to receive their bonuses.

Fig 22: GNI Per Capita (USD); 1994 - 2014



Source: World Bank

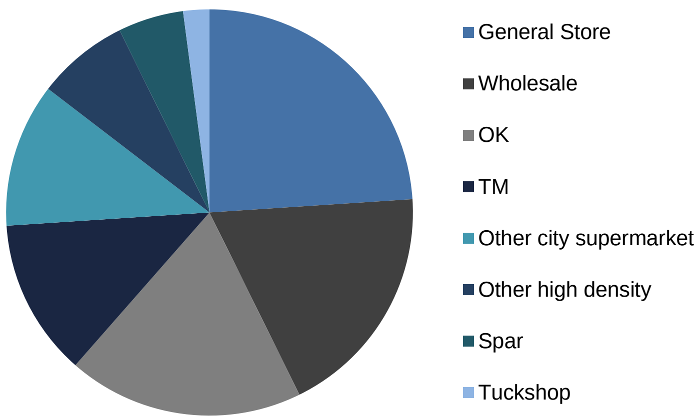
Fig 23: Personal Income Distribution; 2014



Source: ZAMPS

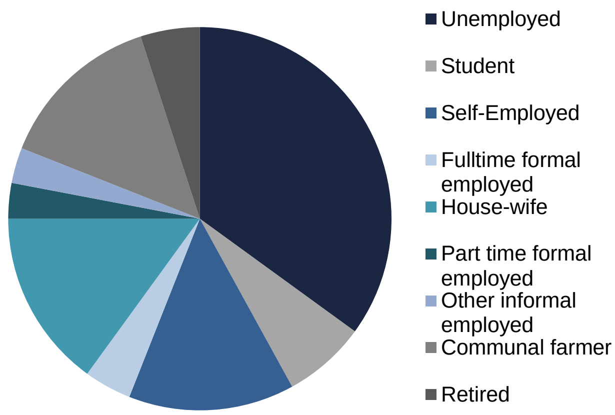
We also observe a continued trend of informalisation of the economy, with consumer counters operating in the traditional, formal sector losing market share to a growing informal sector. An estimated 5mn people, 38% of the population, are now working in the informal sector compared to the 3.7mn people (28% of the population) estimated to be working in the informal sector in 2012. The informal sector contributed around 20% to GDP, with 53.2% of value-add in the informal sector generated from agricultural activities (communal farming). As the economy becomes increasingly informal, traditional formal retail-outlets are feeling the pressure and struggling to maintain market share. As reflected in Figure 24 below, the ZAMPS survey revealed that 25% of respondents buy their groceries from informal 'general stores' and 'tuckshops', whilst the traditional formal retailers, OK Zimbabwe, TM and Spar only shared 18%, 12% and 5% of the market respectively.

Fig 24: Grocery Shopping Outlets Used; 2014



Source: ZAMPS

Fig 25: Sources of Income; 2014



Source: ZAMPS

In the face of informalisation of the economy and consumer down-trading, the operating environment remains particularly challenging for consumer counters, as reflected in their financials, shown in Table 5 below. We have observed subdued or even contracting top-line growth (-1.35% average revenue growth y/y) as demand and consumer spend remain depressed, and margins have also been coming under downward pressure as consumers switch to lower-margin alternatives and with companies unable to increase their prices without a commensurate drop in sales. Innscor (INAF: ZH) and particularly Dairibord (DZLH: ZH), whose product offerings are deemed non-basic, have been amongst the harder hit whilst National Foods (NAFH: ZH) faired much better given a more defensive product mix, registering top-line growth of 11%. Counters positioned to service the lower end of the market and/or with an ability to tap into the growing informal sector are therefore likely to remain defensive in this environment.

Table 5: Revenue, EBITDA and EBITDA Margins for ZSE-listed retail counters; 2014

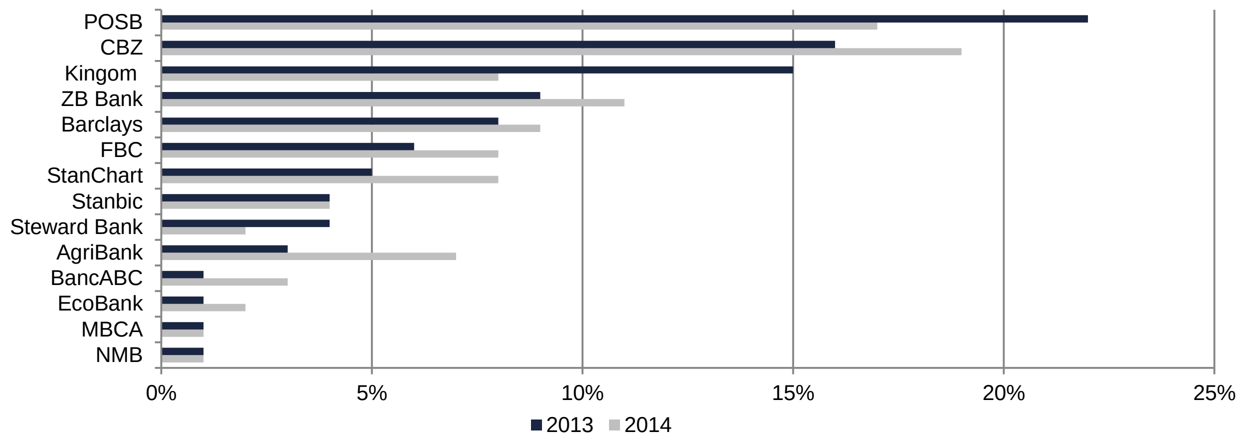
Company	Financial Period	Sub-sector	Revenues			EBITDA			EBITDA Margin	
			Curr	Prev	% Chg	Curr	Prev	% Chg	Curr	Prev
Afdis	12 Mnths to 30/06/14	Beverages	24.0	22.1	8.4%	3.3	1.9	73.7%	14.0%	8.7%
Dairibord	6 Mnths to 30/06/14	Dairy/Beverages	43.8	49.1	-10.7%	1.5	-1.0	251.8%	3.5%	-2.0%
Delta	6 Mnths to 30/09/14	Beverages	302.2	315.5	-7.6%	74.4	77.7	-4.3%	24.6%	24.6%
Edgars	6 Mnths to 05/07/14	Clothing Retail	31.6	28.7	10.2%	1.2	1.5	-21.5%	3.7%	5.2%
Truworths	12 Mnths to 6/07/14	Clothing Retail	23.8	25.3	-6.1%	0.8	2.0	-59.6%	3.4%	7.9%
OK Zimbabwe	6 Mnths to 30/09/14	Food Retail	232.1	243.6	-4.7%	9.5	9.5	0.2%	4.1%	3.9%
Innscor*	12 Mnths to 30/06/14	Food Retail	1010.9	980.6	3.0%	83.6	96.1	-15.0%	8.3%	9.8%
Meikles Limited	12 Mnths to 31/03/14	Hotel & Conglomerate	384.3	391.3	-1.8%	7.9	10.0	-21.3%	2.0%	2.5%
National Foods	12 Mnths to 30/06/14	Milling and Basic Foodstuffs	343.5	309.3	11.1%	24.9	20.4	22.1%	7.2%	6.6%
ART	6 Mnths to 31/03/14	Paper and Packaging	14.1	15.2	-7.5%	-0.2	1.1	-119.8%	-1.6%	7.4%
BAT Zimbabwe	6 Mnths to 30/06/14	Cigarettes and Tobacco	20.3	23.1	-12.1%	7.9	2.9	168.5%	38.8%	12.7%
Colcom	12 Mnths to 30/06/14	Pork and Related Products	66.6	60.8	9.5%	8.8	4.8	82.1%	13.2%	7.9%
Hunyani	6 Mnths to 30/04/2014	Paper and Packaging	19.0	20.9	-9.3%	-0.1	0.0	-348.8%	-0.6%	0.2%
Average			193.6	191.2						

Numbers adjusted for consolidation of associates for comparative purposes
Source: ZSE, Company Data

Rebuilding confidence in the financial sector

Due to an inactive interbank market, contagion effect has been minimised in the banking sector, weaker institutions have been gradually weaned out through natural attrition with minimal disruption to the sector as a whole. This has seen the financial sector remaining stable in 2014 with capital flight occurring to larger institutions perceived to have relatively stronger balance sheets. Figure 26 below shows the growth recorded in operational accounts opened and held within individual banks from 2013 to 2014. It is evident that there was a significant shift to institutions like CBZ which experienced 3.7% growth in accounts held and 10% growth in deposits.

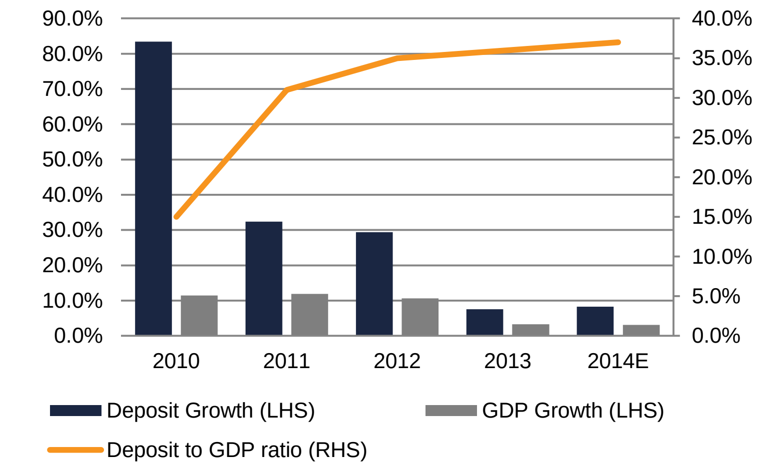
Fig 26: Bank Usage (2013 vs. 2014)



Source: ZAMPS

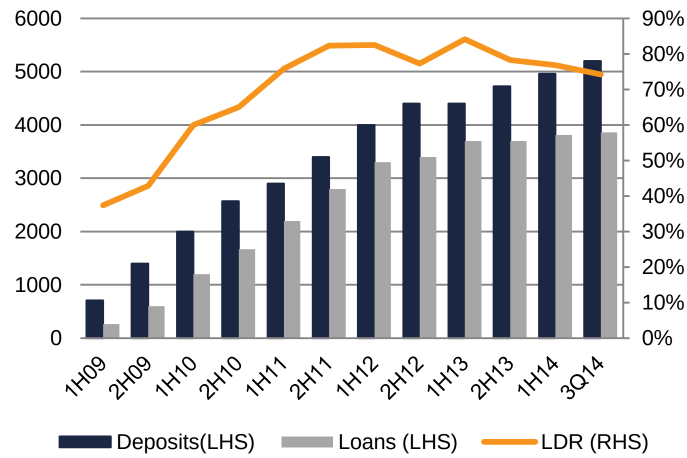
Deposits in the sector increased by 8.3% y/y, from $4.8bn in October 2013 to $5.2bn in October 2014. Loans are estimated to have risen 6.2% y/y from $3.64bn in October 2013 to $3.9bn in October 2014. The country's loan to deposit ratio has remained largely unchanged as it closed the period to October 2014 at 74%.

Fig 27: Deposit vs. GDP growth 2010- 2014



Source: Ministry of Finance, IH Estimates

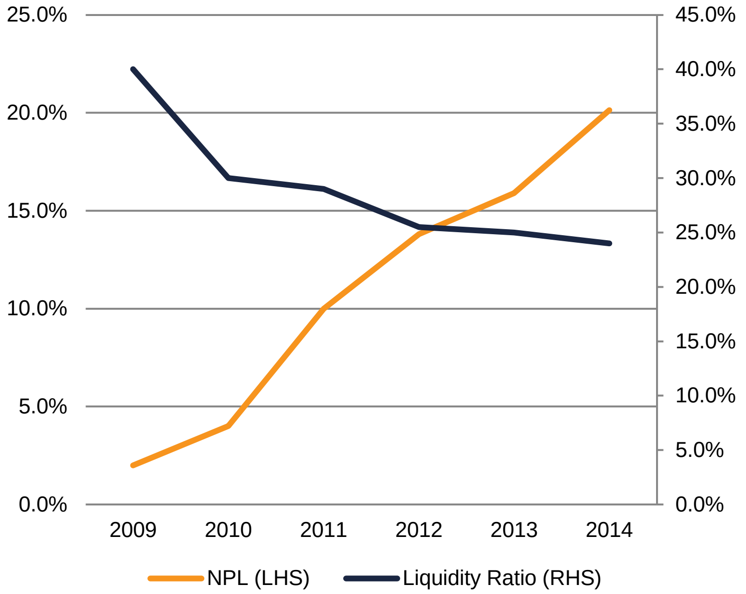
Fig 28: Loan and Deposits, & Loan deposit ratios 2009 to 2014



Source: Ministry of Finance, IH Estimates

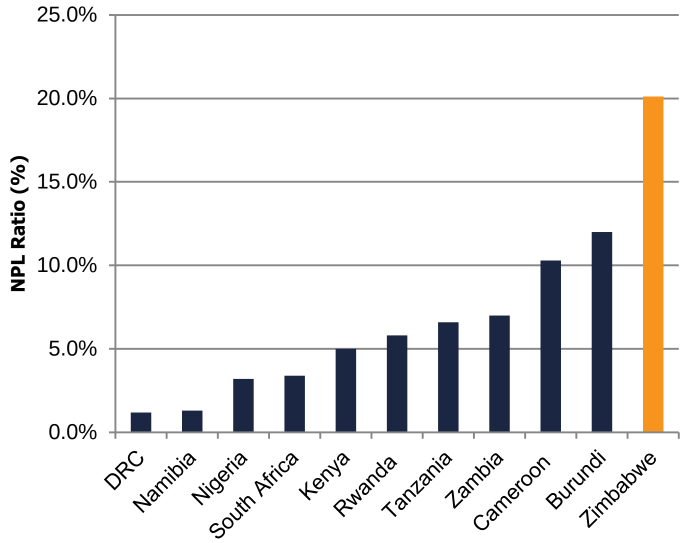
In light of the macroeconomic challenges constraining banks' capitalization initiatives, the Reserve Bank, in its Monetary policy introduced 3 segments as a measure to promote strategic groups based on current banking classes. The 3 segments namely Tier I, Tier II and Tier III, have different minimum capital requirements for their current state and to meet by 2020. Tier I is for large indigenous commercial banks and all foreign banks with a current requirement of $25mn and $100mn by 2020.Tier II includes commercial banks, Merchant banks, building societies, development banks, finance houses and discount houses; all with a minimum current requirement of $25mn and will remain at this level by 2020. Deposit-taking Microfinance banks constitute Tier II with a minimum current requirement of $5mn and $7.5mn by 2020. As at 30 September 2014, a total of 14 out of 20 operating banking institutions, excluding POSB, were in compliance with the minimum requirements.

Fig 29: Non-Performing Loans and Liquidity ratio 2009-2014



Source: Ministry of Finance, World Bank, IH Estimates

Fig 30: NPL Ratio vs. other African countries



Source: Ministry of Finance, IMF

Of grave concern is the continued growth in levels of NPLs, from 18.5% in 1H14 to 20.14% in 3Q14, well above the international benchmark of up to 5%. In response, Cabinet approved the establishment of a national special purpose vehicle (SPV), the Zimbabwe Asset Management Corporation (Pvt) Limited (ZAMCO) to acquire, restructure and dispose of NPLs from Banks in order to clean up and strengthen banks' balance sheets. Acquisition of these loans is intended to provide banks with the liquidity to fund valuable projects for the economy and to mitigate loss of confidence in the sector. Banks are to sell NPLs to ZAMCO under commercial terms, assigning collateral and all other rights attached to the loans. ZAMCO will be funded by a combination of new inflows, long term bonds and treasury bills. ZAMCO will manage the loan portfolio and the proceeds will be used to retire the borrowing, treasury bills or the bonds. To date, the SPV has taken over $65mn worth of NPLS from banks.

Another challenge faced by the financial sector is the lack of a centralised credit bureau as financial institutions continue to be exposed to heightened credit risk. Cognisant to this challenge, the RBZ is working on bridging the information asymmetry gap in the sector through establishing a central credit registry system within its structures. The system will comprise of private credit reference bureaus (CRBs), and a credit registry within the Reserve Bank, that will serve as a databank for licensed CRBs. The credit reference system is supposed to compliment the work of ZAMCO and help enhance financial stability by promoting improved risk management practices thus reducing credit risk, increasing the supply of credit to fuel growth-related activities and helping to promote lower interest rates.

Prior to the publication of the monetary policy, external loans of $1mn and above required External Loans Coordinating Committee (ELCC) approval whilst external loans below $1mn were approved at the Authorised Dealer's level. The threshold approval was increased from $1mn to $7.5mn in August by the Reserve Bank. In our view this effective relaxation of exchange controls will benefit the economy by making it more conducive for corporates to access offshore credit with minimal bureaucracy. This provides increased competition for local banks as top tier corporates are increasingly accessing offshore credit direct at lower rates and higher tenures. We expect lending rates in the sector to continue to moderate, exerting downward pressure on NIMs and therefore ROEs.

To address the lack of change in the economy which was affecting ability to price goods effectively to the extent that sweets and tokens/vouchers were issued as change, the RBZ decided to import special bond coins of 1c, 5c, 10c, 20c and 50c whose values would be at par with the equivalent denominations of US cents. Rand coins of 10c, 20, 50c, R1, R2 and R5 were also imported to buttress the multiple currency system which is dominated by US$ and Rands. The bond coins introduced in December were not received well by the general public amidst fears that this was an attempt to reintroduce the Zimbabwean Dollar, in our view this perception is unfounded. However we believe the RBZ must be more proactive in articulating the details of the $50mn bond backing these coins, it is still generally unclear which institutions subscribed to the instrument.

Mobile money continues to show high growth rates as the strategic thrust remains to bank the largely unbanked population of the country (estimated unbanked 80%). As the economy becomes increasingly informalised (estimated current formal unemployment +/-90%), conventional retail banking will become more difficult with the average Zimbabwean likely unable to meet the requirements to open a conventional bank account to begin with. Leveraging the technology of mobile banking, financial services can now be accessed from anywhere in the country without need for a physical bank branch/outlet and with 56% of the population living in the rural areas; a clear opportunity exists. According to a ZAMPS survey, the use of EcoCash increased from 47% in 2013 to 56% of the population in 2014 while the use of ATM Cards declined from 78% in 2013 to 75% in 2014. As awareness of mobile money markets increases, usage will increase and the usage of traditional banking methods will decrease in terms of volumes. However traditional banks will continue to control wholesale deposits, with mobile money naturally having restrictions around volumes that can be transacted on the platform (e.g. EcoCash daily individual limit $500). We are seeing banks placing increased focus on tailoring product to access the bottom of the pyramid by similarly leveraging technology, for example Barclays' "CashSend" card-less money transfer platform and "Hello Money" mobile banking.

Key Policy Progress and Reforms for 2014/15

- **Creditor Re-Engagement**

We have noted with satisfaction that 2014 has seen significant progress in the creditor re-engagement process, attested by the token re-payments made in the year and successful implementation of the first SMP programme with the IMF, which have resulted in normalizing relations with key institutions. Government has acknowledged that as Zimbabwe negotiates for debt relief, it will be important for the country to honour its obligations to cooperating partners. In this regard, Government is insistent on developing a culture and track record of honouring external obligations in order to unlock further such financing. It was in this spirit that Government made token loan repayments amounting to $180.4mn during 1H14, including monthly payments to the IMF ($150k) and quarterly payments of $900k and $500k made to the World Bank and ADB respectively. Already, normalising relations with other partners such as the Kuwait Fund and BADEA has seen the restructuring of loans and the respective repayments have since resumed. Similarly, as a way of normalising relations, Government will also starts making token payments to the European Investment Bank, whose debt amounts to $314mn, of which $238mn are arrears. One of the key elements of the 2015 strategy is to continue making progress in this regard. Pursuant to this, as part of the 2015 Budget, government has committed to continue with the token payments to the IMF, African Development Bank (AfDB) and the World Bank. Making this commitment with very limited fiscal space goes a long way to demonstrate government's renewed commitment to resolve Zimbabwe's debt problem and normalise international relations. Furthermore, the resultant removal of the EU Sanctions allowing direct funding to the GOZ in November 2014 may prove to be beneficial in attracting FDI.

- **Improved investment into infrastructure**

We are observing notable improvements in infrastructure development, mostly funded by foreign multilateral institutions. The China Export Import Bank has committed a tranche of $320mn to fund the expansion of the Kariba South Power Station which will provide the country with an additional 300MW of power by 2017, work on the project has already begun. In addition it is anticipated that funding for the 600MW expansion for Hwange Power will be secured in 2015. The China EXIM Bank has also provided a further tranche of $144mn for water and waste water rehabilitation, work on this project has also begun. Commitments are in place from the African Development Bank and the World Bank amounting to just under $100mn for infrastructure development. We believe this bodes well for the country in 2015.

- **Statutory Instrument placing floors on small-grains producer prices**

The Ministry of Agriculture gazetted a Statutory Instrument (Statutory Instrument (SI) 122 of 2014) placing floors on producer prices of maize, wheat, rapoko and millet, effective August and back-dated to 1 April 2014. The producer price of maize was set at $390/MT, making it illegal to buy maize for less than $390/MT whilst before the SI, private buyers had been offering prices as low as $200/MT. We foresee this having an adverse impact on cost structures for counters involved in the processing of maize meal, flour, beer, baby food, meat and other grain related products, such as National Foods (NAFH: ZH) and Delta (DELTA: ZH). Whilst these counters are sitting long on stock and have therefore not yet felt the effects of the SI, we estimate that full impact will be felt from 2Q15 when these companies' stock levels diminish and new grain is purchased at significantly higher prices. Given the uneconomic nature of the SI we don't anticipate the policy being in place in the foreseeable future nevertheless these counters will either lose margin or, if the increase is passed onto consumers, if the policy remains in place.

- **Beneficiation**

As articulated in the ZIM-ASSET and the Industrial Development Policy, Government is prioritising the cluster based value addition and beneficiation strategy as one of the key strategies to drive up productivity in the economy. The drive has begun with mineral beneficiation, with Government levying an export tax on un-beneficiated platinum and diamonds, VAT zero rating sales of rough diamonds to the local industry, and giving a two year window, beginning 1 January 2013, for existing platinum producers to set up a platinum refinery plant in the country, after which exports of raw platinum will not be permitted. Furthermore, Government imposed a 15% levy on the export of raw platinum during this window period. In the case of gold, Fidelity Printers and Refineries started refining from 17 December 2013 and the export of unrefined gold was banned. The latter has shown progress, with a total of 11.1 tons of gold being delivered to Fidelity Printers and Refiners by October 2014, surpassing the minimum annual requirement of 10 tons for the country's re-accreditation into the London Bullion Marketers Association. However, progress with regards to platinum refinery has been slow, in view of the quantum of resources required and also the timeframes required to undertake investment in the necessary new technology processes. In light of this, Government announced in the 2015 Budget that the window period for completion of domestic refining investment projects will be extended to December 2016, and the 15% tax on raw platinum exports suspended during this period. That said, Zimbabwe's largest platinum producer, Zimplats, has commenced work to refurbish a base metal refinery (BMR) which will cost the company around $192mn and upon completion, expected within two years, the refinery will process 270 000 tonnes of ore per month. Bindura Nickel Company (BINDURA: ZH) will also be restarting its smelter and refinery plant in 2015, at a cost of $26mn, part of which will be funded through the $20mn bond issued by the Company in 4Q14 and which was granted prescribed asset status. Therefore, the thrust towards beneficiation appears to be gaining traction and will ultimately hedge against the exogenous shocks to which Zimbabwe's mining sector has been exposed, particularly to international price shocks, and which has been hampering performance in the sector and therefore on the fiscus. We believe the fruits of these initiatives will be borne in the medium to long term, likely from 2016/17 onward.

- **Resumption of RBZ Debt, Setting up ZAMCO and Credit bureau**

Government announced in the 2014 Budget Statement that they would take over the Reserve Bank debt which arose from the Bank's quasi fiscal activities. The amount of validated Reserve Bank debt as at end July 2014 is US$200.4 million. Pursuant to debt validation by the Debt Management Office, Treasury bonds are being issued against the debt owed to creditor institutions. The tenors for the TBs are three, four and five years. To date, TBs amounting to US$200.4 million have since been issued to various banks and institutions. Furthermore, an amount of US$27.4 million worth of TBs was issued to Seed houses for inputs supplied.

- **Relaxation on Exchange Controls**

As part of measures to boost and sustain market liquidity and encourage FDI, the Reserve Bank in 2014 took certain investor-friendly measures to create conducive conditions that allow the free and unfettered inflow of foreign investment into Zimbabwe. In terms of the current Exchange Control policy on capital remittances, all disinvestment proceeds arising from pre-May 1993 investments required prior Exchange Control approval and are eligible for reinvestment on the domestic market for a period of 5 years prior to remittance. With effect from August 2014, this was changed to allow all disinvestment proceeds arising from both pre-May 1993 and post-May 1993 shall be fully remittable. In this regard, investors may remit offshore any capital plus appreciation to any destination of their choice, after Exchange Control approval has been granted. Given the need to streamline the approval processes so as to enhance timeous accessing of offshore loans, the threshold for approval of offshore loans by Authorised Dealers without need for prior Reserve Bank approval was from August 2014 increased from $1mn to $7.5mn. In order to encourage foreign investment inflows and further develop the country's bond market, exchange control restrictions on the level of foreign participation on primary issuance of bonds (previously restricted to 35%) and participation by foreign investors in the secondary market (previously prohibited) were removed. Finally, all non-resident Zimbabweans are now permitted to invest in any listed counter on the ZSE without any limit (previously limited to 70% participation).

Benign political environment expected in 2015, however policy inertia remains

As the economy comes under increasing stress characterised by depressed aggregate demand, high unemployment, pervasive structural issues linked to poor funding in key sectors – mining & agriculture, and a persistent current account deficit (cc +/-24% of GDP); attracting FDI has never been more crucial. The largest impediment however, remains ingrained in politics, specifically the lack of a compromise solution to the indigenisation policy. A recent softening in the political rhetoric and pronouncements around the indigenisation policy has not been accompanied by key improvements in subsequent implementation.

Deals are still approved on a discretionary basis as opposed to a clear, standardised manner with defined recourse. A present threat is the ongoing compulsory acquisition of land belonging to corporate entities including sometimes already indigenous, publicly listed entities (affected companies include CFI Holdings, CFI: ZH, Interfresh Limited, Zimplats). It is our view that government will come under increasing pressure to come up with a more cohesive policy that is clearly and consistently applied as the country's need for investment intensifies. In line with this, we have seen press reports indicating a more pragmatic approach to JVs within the agricultural space.

In December 2014 the ruling party ZANU PF held its 6th National People's Congress, effectively an elective congress where the party traditionally votes to appoint the presidium (President and VPs) to sit in government and votes to appoint the Politburo which is the highest decision making body in the party, therefore exerting significant influence on government policy. The lead-up to this congress particularly in H2 saw an increase in disruptive succession politics ultimately leading to some fundamental shifts within the party.

Then Vice President Joice Mujuru, lost her position both in the presidium and within the party structures amidst accusations of corruption and attempting to actively unseat the President. This was accompanied by the removal of influential figures perceived to be supporters of Joice Mujuru from the party structures, resulting in an eventual reshuffle of both the presidium and cabinet. The constitution of the party was amended granting the First Secretary and President of the party the power to unilaterally appoint members of the politburo and the Vice Presidents. Robert Mugabe was re-appointed as First Secretary and President, he then subsequently appointed Emmerson Mnangagwa and Phelekezela Mphoko as the new co- VPs. Of note was the entry of the First Lady Grace Mugabe into active politics, she launched her campaign through a well-publicized tour of the country's 10 provinces, she is now the Chairperson of the Women's League within the party and a member of the Politburo.

It is our view that with the elective congress now behind us and the President having finalised the structure of the Presidium and politburo, some element of stability will begin to pervade the party; we hope this will allow succession politics to take a backseat to the economy, at least in the short to medium term. We believe that 2015 will see Government becoming compelled to take a more proactive approach to the economy, with the focus shifting towards creating a more conducive environment for much needed investment.

Gradual thawing in international relations

On a positive note we have witnessed a general thawing in international relations between Zimbabwe and the foreign community; particularly important is the removal of the EU sanctions, effectively allowing direct funding to take place to the GoZ (Government of Zimbabwe). During 2014 a delegation from the United Kingdom Trade Mission visited the country for the first time in almost 2 decades and expressed optimism for future trade and investment in Zimbabwe. There have also been subsequent visits by delegations from Australia, Denmark and France. Table 6 below details formal commitments that have been made by various international bodies for funding into Zimbabwe.

Table 6: Funding commitments

Institution/nation	Tenure/where given	Value	Purpose
European Union	5 year program	$300mn	Reformation of health, agriculture and governance initiatives.
World Bank	5 year program	$44mn	Support economic reforms proposed through the Zimbabwe Reconstruction Fund (ZIMREF)
African Development Bank		$53.4mn	Youth, tourism, sanitation, transportation, emergency power, public finance
China Export Import Bank		$320mn	Kariba South Power Plant
China Export Import Bank		$144mn	Water and waste-water rehabilitation

Source: GoZ

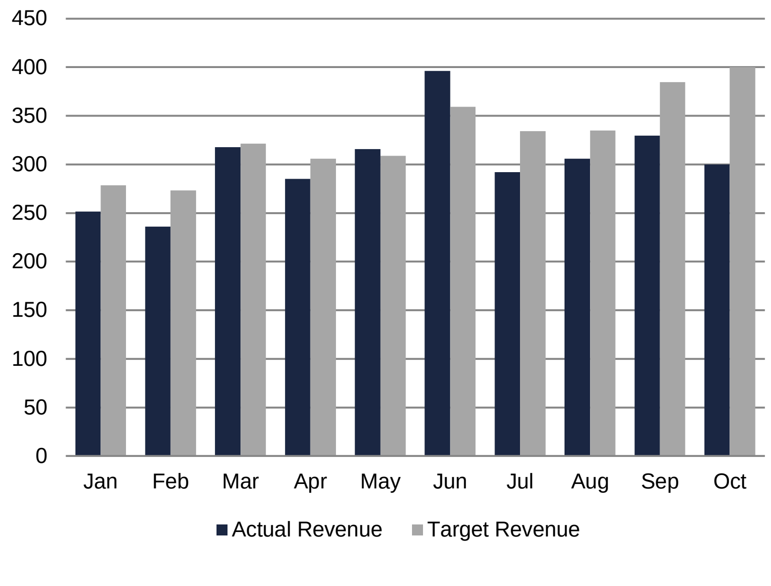
In a positive signal the IMF re-opened its Zimbabwean office in 2014, the institution has committed to give technical assistance to Zimbabwe with an aim to normalizing the country's relations with multilaterals. In October 2014, the Management of the International Monetary Fund (IMF) completed its third review in Zimbabwe under the Staff-Monitored Program (SMP) 1 and approved a successor SMP covering the periods October 2014 – December 2015. The SMP aims to strengthen the country's external position, as a prerequisite for arrears clearance, resumption of debt service, and restored access to external financing. We believe this is an encouraging and necessary step towards re-engaging the international community and beginning to restore confidence in the Zimbabwean economy.

Fiscal Position

Fiscal situation remains tight

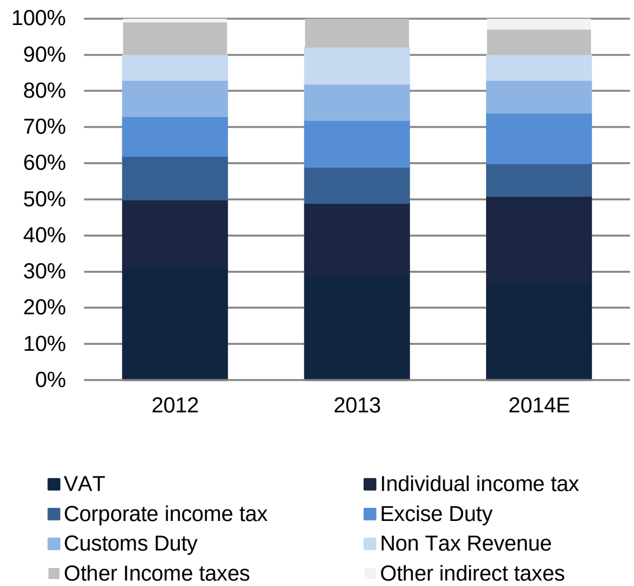
Total revenue collections for the 10 months to October 2014 stood at $3.04bn, falling 7% short of budget but improving by 1% from the same period last year. Underperformance this year was attributed to subdued economic activity, depressed aggregate demand and tax leakages, particularly at the ports of entry. Tax revenues comprise of 94% of total revenue while non-tax revenue contributed 6%. Value Added Tax and Pay As You Earn remain the main contributors to revenue, contributing 27% and 24% respectively. Monthly targets were met in May and June only this year, which resulted in the MoF revising downwards revenue projections for the year from $4.12bn to $3.93bn.

Fig 31: Actual revenue vs. Target revenue to October 2014



Source: Ministry of Finance

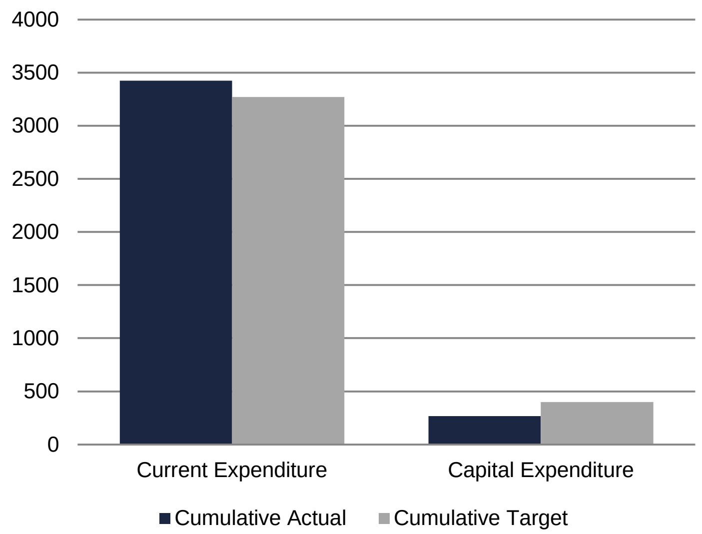
Fig 32: Total revenue composition up to FY14



Source: Ministry of Finance

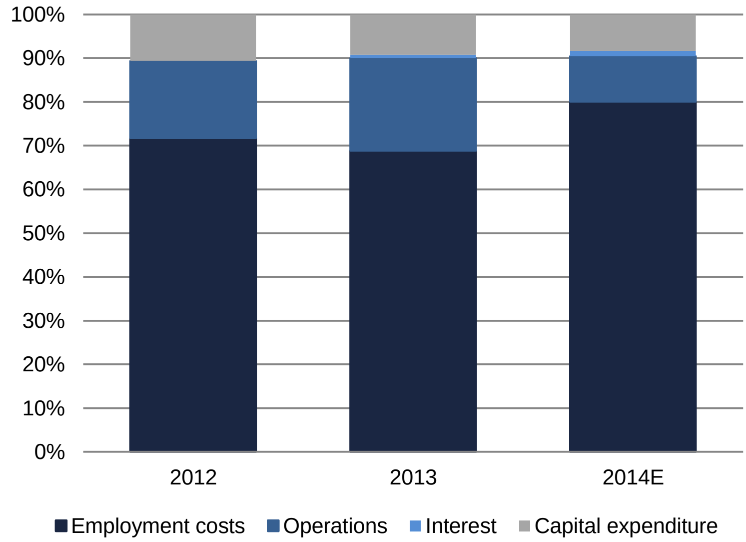
Cumulative expenditure to October 2014 amounted to $3.42bn, overrunning by 5% the target of $3.27bn on increased employment costs and loan repayments. Recurrent expenditure made up 92% of total expenditure crowding out capital expenditure which was only $261.7mn to October 2014. Employment costs increased in the year as civil service salaries were reviewed upwards in April; 80% of total expenditure went towards the wage bill, compared to 75% in 2013.

Fig 33: Current Expenditure and Capex: actual vs target to October 2014



Source: Ministry of Finance

Fig 34: Total expenditure composition : 2012, 2013 and 2014E



Source: Ministry of Finance

According to the MoF, revenue is anticipated to grow to $4.1bn in 2015, similar to levels forecasted for 2014 and 28.1% of the forecasted nominal GDP ($14.59bn). Expenditures are expected to increased from $4.03bn in 2014 to $4.115bn, giving a deficit of $15mn. Table 7 below shows the MoF's National accounts for 2013 to 2015. As can be seen, recurrent expenditure will continue to dominate total expenditures with employment costs taking up a large portion of the expenses.

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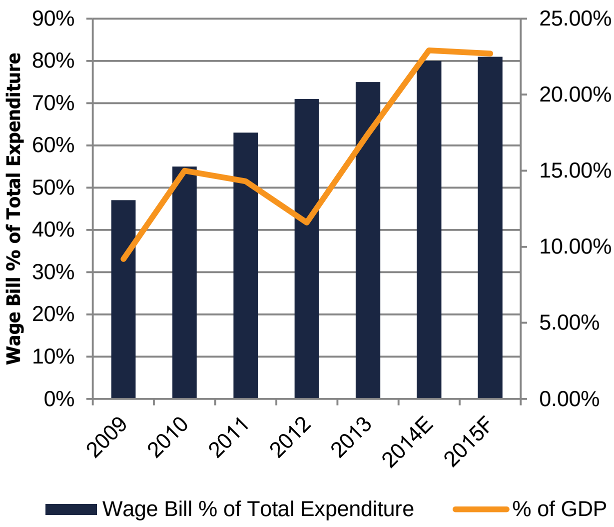
Table 7: National Accounts 2013-2015

National Accounts (Real Sector)	2013 Est.	2014 Est.	2015 Proj.
Real GDP at market prices (million $)	11,745	12,103	12,494
Nominal GDP at market prices (million $)	13,490	14,015	14,594
Real GDP Growth (%)	5	3	3
Inflation (Annual Average) (%)	2	(0)	0
Government Accounts			
Revenues & Grants (million $)	3,741	3,928	4,100
Expenditures & Net Lending (million $)	3,987	4,030	4,115
Current Expenditures	3,520	3,634	3,774
Recurrent Operations	1,153	384	384
Employment Costs	2,344	3,208	3,317
Capital Expenditure & Net lending	468	396	341
Balance of Payments Accounts			
Exports (million $)	3,507	3,487	3,659
Imports (million $)	7,704	7,471	7,628
Current Account Balance (million $)	(3,426)	(3,352)	(3,423)

Source: Ministry of Finance

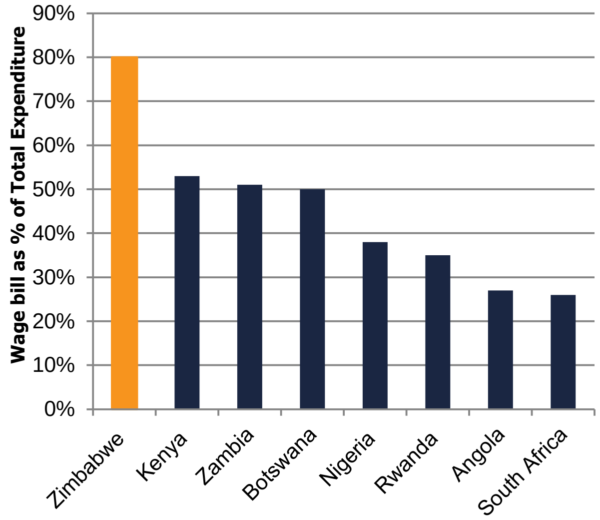
Reversing the budget from consumptive to developmental has become a key priority for the government and this can only be done by managing the wage bill. In the 2014 Budget, the MoF had targeted to achieve a reduction of the wage bill from 75% to between 55-65% by the end of 2015 only for it to increase to 80% by the end of 2014. Civil servants received an increase in their salaries during the year which was backdated to January 2014 further exacerbating employment costs. The World Bank's recommended spend on the wage bill as a percentage of total public spending is 25%. Figure 36 below shows how our peers are fairing in terms of wages, with Kenya holding the second largest wage bill as a percentage of revenue at 53%. It is clear that Zimbabwe's spend on the wage bill is both exorbitant and unsustainable.

Fig 35: Wage bill % of Total Expenditure vs. SSA Peers GDP (2010-2015F)



Source: Ministry of Finance, IMF

Fig 36: Wage bill as a % of Total Expenditure and



Source: Ministry of Finance

In response to the unsustainably high and growing wage bill and facing increasing pressure from external creditors to address the issue, under the last Staff Monitored Programme report, the government agreed to maintain a hiring freeze while allowing limited flexibility in filling critical vacancies. Government further agreed to index wages to inflation, streamline the civil service and committed to granting one salary increase in 2015 like was done in 2014. We await to see whether government will effect retrenchments in the civil service given the political implications of such a move (ZIMASSET; the government's economic recovery plan promised to create 2mn jobs by 2020). Given government's inability to consistently service the current wage bill, we also await to see how a further increment in 2015 would be funded. We expect Government accounts to come in at a deficit again in 2015 as projected by the Ministry of Finance. However, we believe this figure will be much higher than government has budgeted.

Fiscal Position

Taxation Analysis

CY14 saw a lot of fiscal changes being proposed and implemented as government tried to look for ways to increase revenue inflow, against a revenue growth target of 4% for CY15. The following are key policies that were implemented or changed in 2014 that will affect 2015 revenues.

The excise duty on cigarettes was last reviewed in 2012; government increased excises on cigarettes effective 1 December 2014, citing that the previous figure was not reflecting the social cost associated with the consumption of the product, therefore duty was increased from $15 per 1000 sticks to $20 per 1000 sticks, a 25% increase, effective 1 January 2015. This increase in tax will affect BAT (BAT: ZH) who has increased their prices by 33% to pass on the additional costs to a more price sensitive consumer, which will naturally impact on volumes. Below is a table depicting the excise duty on domestic cigarettes compared to our peers.

Table 8: Comparison of Excise duty on Cigarettes with SSA peers

Country	Tax Type	Excise on Domestic Cigarettes	Specific Excise Tax (Est. US$)	Average Retail Price (US$)
Botswana	*Ad Valorem*	39.1% on retail price	N/A	3.99
Kenya	Specific *Ad Valorem*	Higher of KSH1200/1000 sticks or 35%	$13/1000	1.64
Namibia	Specific	NAD1.75/10 sticks	$15/1000	3.05
SA	Specific	ZAR5.80/10 sticks	$52/1000	2.97
Tanzania	Specific	TZS26689/1000	$15/1000	2.39
Zimbabwe	Specific	$20/1000	$20/1000	1.50
Malawi	*Ad Valorem*	60% on retail price not exceeding MWK3, other 80%	N/A	2.00
Mozambique	*Ad Valorem*	45.8% on retail price	N/A	3.10
Nigeria	*Ad Valorem*	15.9% on retail price	N/A	1.09
Zambia	*Ad Valorem*	30.9% on retail price	N/A	1.69

Source: Numbeo, SARS, IH Estimates, Ministry of Finance Tobacco Atlas

On the reverse side of the spectrum, lager volumes in the country have seen a significant decline since Government increased excise duty from 40% to 45% in December 2012. Ultimately the decline in sales negated the initial increase in tax collections and eventually saw the government earning less tax on a net basis. In an effort to aid recovery in taxes, government has since reversed the excise duty from 45% back to 40% in the hope that volumes will begin to pick up, the new rate is effective 1 January 2015. Including the reduction in excise, Delta (DELTA: ZH) has reduced its prices CY14 in lager beer by a total of 13%. Whilst this has stimulated some marginal recovery in the mainstream and economy segments, the overall effect has been mainly to arrest the rate of decline in aggregate volumes. The table below shows the current excise duty on clear beer compared with our SSA peers.

Table 9: Comparison of Excise duty on Clear Beer with SSA peers

Country	Tax Type	Excise Duty on Clear Beer	Specific Excise Tax (Est. US$)	Average Retail Price (US$)
Botswana	Ad Valorem	45%		1.35
Kenya	Specific *Ad Valorem*	Higher of KSH70/litre or 50% per litre	$0.77/litre	1.42
SA	Specific	R2.87/litre	$0.25/litre	1.19
Tanzania	Specific	TZS375/litre	$0.21/litre	1.47
Zimbabwe	Ad Valorem	40%	N/A	1.07
Malawi	Ad Valorem	10%	N/A	1.41
Mozambique	Ad Valorem	40%	N/A	1.51
Nigeria	Ad Valorem	20%	N/A	1.35
Zambia	Ad Valorem	60%	N/A	1.50

Source: Numbeo, SARS, IH Estimates, Ministry of Finance

A 5% excise duty on airtime (Voice and data) was introduced in the Mid-Term Fiscal policy and affected on 15 September 2014. Again this was done in an effort to raise additional revenue to finance non-discretionary expenditures. However, comparing this to SSA peers, the rate at which telecoms are taxed in Zimbabwe is still lower than the average (11%) (Figure 37). POTRAZ prevented mobile operators from passing the tax onto consumers through increased tariffs so this is effectively a tax on revenue. This policy will have an impact on telecoms (within the listed companies space Econet (ECWH: ZH)), accelerating the decline which was already taking place in voice & SMS and squeezing margins. Another tax policy implemented in 2014 was the customs duty placed on mobile handsets pegged at 25% effective on the 1st of October. This will affect Econet's strategy to grow data ARPUs by retailing low cost smart phones.

Fiscal Position

Fig 37: Excise duty on airtime, Zimbabwe vs SSA peers

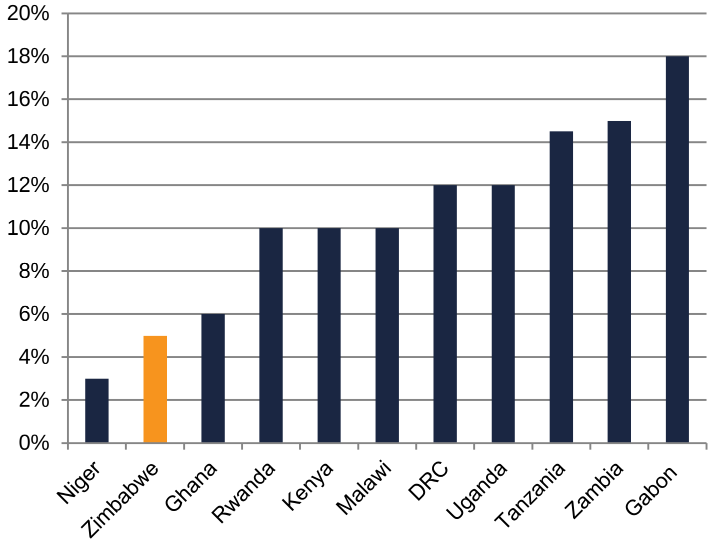


Fig 38: Mobile phone Tariffs Zimbabwe vs. SSA peers

Country	Specific Tariffs per minute	Est. US$/minute
Zimbabwe	$0.15	0.15
Zambia	K1.08	0.17
South Africa	66c	0.06
Kenya	KSH4.02	0.04
Tanzania	TZS234	0.13
Malawi	MK72	0.16
Namibia	N$1.50	0.13
Botswana	1.35 Pula	0.14

Source: Ministry of Finance,

Below is a table that shows other taxation policies affecting major industries in Zimbabwe that were implemented in 2014.

Table 10: Recent tax policies

Type of Tax	Policy Change 2014	Listed Companies affected
Mining Royalties	Royalties on gold produced by primary producers reviewed downwards from 7% to 5%. Presumptive tax on small scale gold miners reduced from 2% to 0% Royalties on rough diamonds sold to firms licensed to cut and polish diamonds removed (1 Jan 14)	Falcon Gold (FALGOLD: ZH), RioZim (RIOZIM: ZH)
Excise Duty on Fuel	Excise duty on petrol (Leaded and unleaded) was increased from 35c per litre to 45c per litre. Diesel was increased from 30c per litre to 40c per litre.	
Export Tax on Raw Hides	$0.75 per kg will apply on 25% of output of raw hides and skins other than domesticated bovine animals such as goats and sheet	Padenga (PADENGA: ZH)
Tobacco Levy on Growers	Reintroduction of tobacco levy on growers at a rate of $0.015 of each dollar of the selling price (1 Jan 15)	BAT (BAT: ZH)
Customs duty on Sugar	Suspended for 6 months due to plant and machinery upgrade at Star Africa	Star Africa (ZSR: ZH)
Import Duty on Dairy products	Milk and cream import duty revised upward from $0.25/l to $0.50/l; other milk and cream from $2.50/kg to $5/kg; fermented milk and yoghurt from $10 to $25 + $0.25/l (SADC region, from 1 Oct 14)	Dairiboard (DZLH: ZH)
Import Tariff on Cement	Import tariff increased from 15% to 25% + surtax for Portland cement and white Portland cement; (SADC region, from 1 Oct 14)	Lafarge (LAFARGE: ZH), PPC (PPC: ZH)

Source: Ministry of Finance

External Debt remains unsustainable

As at December 2014, the country's public and publicly guaranteed debt was estimated at $8.40bn comprising of $7.23bn worth of external debt and $1.17bn domestic debt. The table below shows a summary of the public and publicly guaranteed debt projection to December 2014.

Table 11: External Debt breakdown 2014 estimates

	US $ Millions	Debt Indicators (% of GDP)
External Debt		
Public External Debt	5,294	38
Publicly Guaranteed External Debt	1,257	9

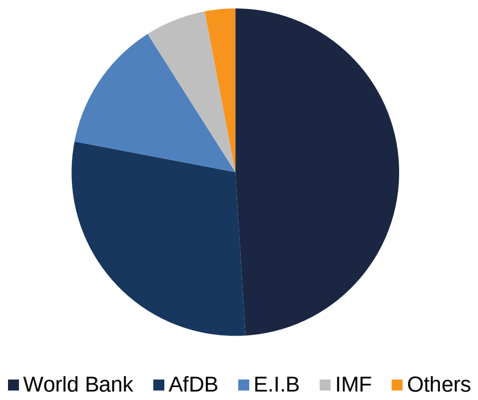
Fiscal Position

Reserve Bank External Debt	674	5
Total Public and Publicly Guaranteed External Debt	7,225	52
Domestic Debt		
Government Stock (Statutory Reserves)	34	0.24
TBs issued for Budget Cash flow support	264	1.88
CBZ Bank Facility	46	0.33
Reserve Bank capitalisation	101	0.72
Input Suppliers	45	0.32
Reserve Bank Debt	681	4.86
Total Domestic Debt	1,171	8.35
GRAND TOTAL DEBT	**8,396**	**60**

Source: Ministry of Finance

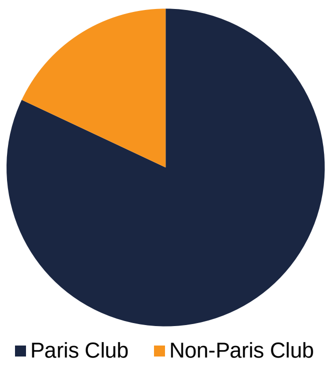
As at 31 December, Multilateral and Bilateral Debt were distributed as follows:

Fig 39: Multilateral Debt as at 31 December 2013



Source: Ministry of Finance

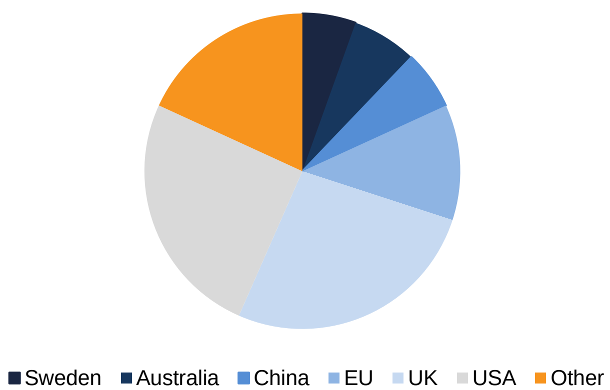
Fig 40: Bilateral Debt as at 31 December 2013



Source: Ministry of Finance

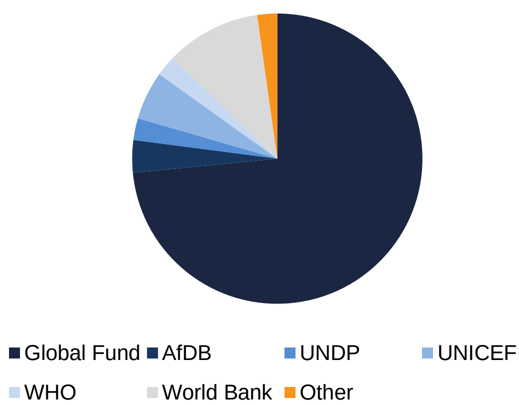
The country is also set to receive development assistance estimated at $468.2mn with Bilateral partners having pledged $248.8mn and Multilateral partners $219.1mn. These loans are to be allocated to projects such as social services, poverty reduction and infrastructure utilities. $557.04mn is expected in FY15 in the form of loans and joint venture arrangements. These resources will be channelled toward various ZIM ASSET infrastructure development projects, necessary for supporting the productive sectors.

Fig 41: Bilateral Support January – September 2014



Source: MoF

Fig 42: Multilateral Support January – September 2014



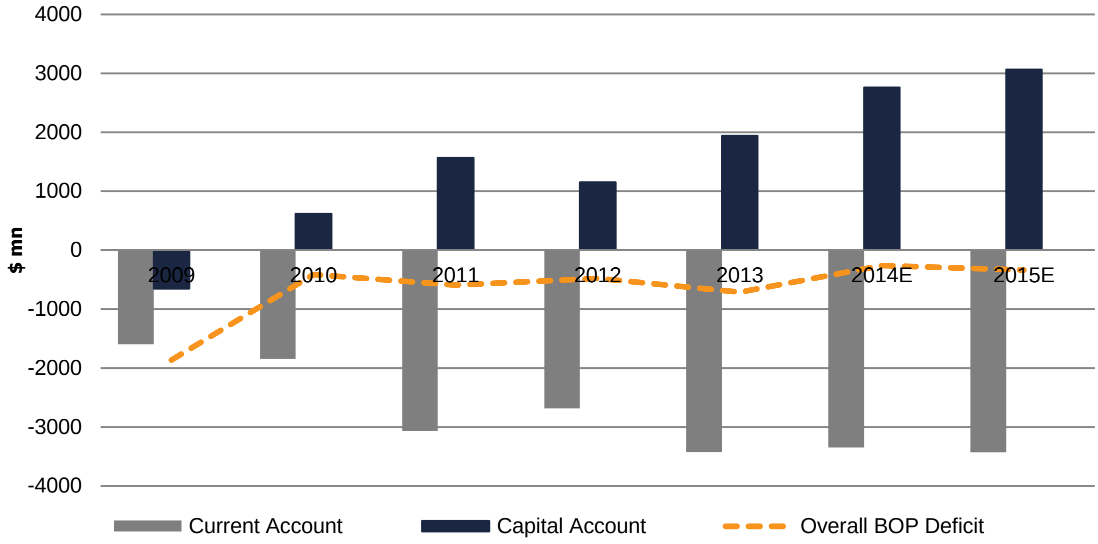
Source: MoF

The development partner support has also helped fund Zim Fund capital projects. These projects include the Hwange Ash Handling Plant, Electricity Sub-transmission System reinforcement and the distribution system reinforcement.

External Position

Figure 43 below summarises the composition of the Balance of Payments (BoP) from 2009 to outward projections to 2015, based on the Ministry of Finance's estimates. The external position remains unstable with a large current account deficit, low international reserves and an overvalued real exchange rate. The capital account, reflecting long and short term net capital, is projected at $2.76bn for 2014. The current account, however with a projected deficit balance of $3.35bn is dragging the BoP into a deficit. The resultant BoP deficit is forecasted to be $264.8mn, an improvement from $712.1mn in 2013. The MoF has projected that the capital account will remain in surplus improving by 11% from $2.76bn in 2014 to $3.065bn on account of short and long term capital inflows, foreign portfolio investment, as well as grants.

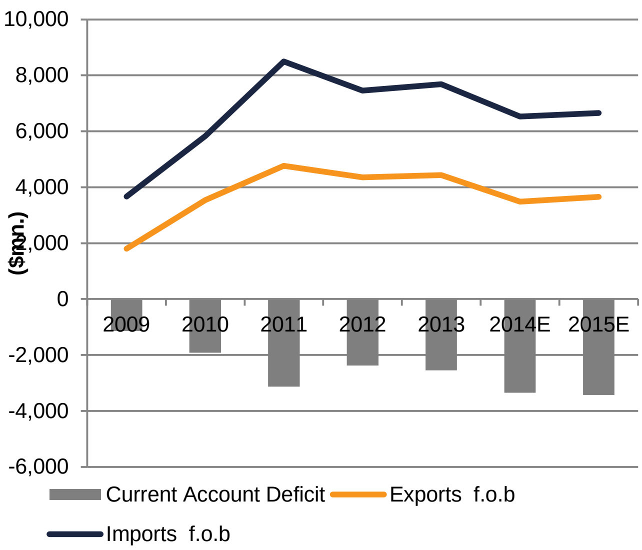
Fig 43: Current Account, Capital Account and Balance of Payments



Source: Ministry of Finance

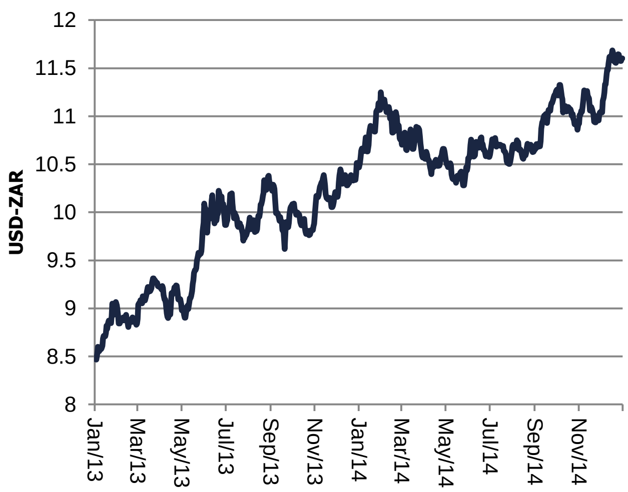
Total imports for the year amounted to $6.37bn down from $7.7bn in 2013 whilst exports for the same period closed at $3.06bn down from $3.51bn in 2013. The MoF had estimated imports for the full year at $6.53bn and exports at $3.48bn. The resultant trade deficit for the year was $3.3bn versus $4.19bn in 2013. The current account deficit estimated for 2014 is $3.35bn, up from $3.43bn in 2013. Figure 44 below traces the current account deficit since 2009. Imports so far have been in line with our expectations and we expect them to remain relatively flat to lower in 2015 on the back of low domestic demand, the depreciation of the South African Rand and expected fuel price cuts. The current account balance is projected to improve from a deficit of $3.43bn in 2013 to $3.35bn in 2014 but expected to deplete again back to $3.43bn in 2015 due to escalated trade deficits, low transfers and incomes. Currently the current account deficit constitutes about 24% of GDP while our SADC peers have a current account deficit that is under 9% of GDP.

Fig 44: Exports, Imports and Current Account



Source: Ministry of Finance

Fig 45: USD-ZAR 2013-2014



Source: Oanda

The recent drop in oil price (-59% since June 2014) is expected to make a significant impact on the economy, and specifically the external position. Fuel is the country's biggest import product constituting over 20% of total imports. A drop in oil prices will therefore have a material impact on the level of imports and shrinking the current account deficit and improving the trade balance. The decline in oil prices will also reduce the cost base for local corporates, particularly manufacturers and processors of goods. Whilst this is beneficial in terms of cost management and margins, if passed through via producer price reductions we expect the resultant downward pressure on prices to accelerate deflation within the economy. Given that Zimbabwe does not have its own currency, monetary policy interventions to stimulate demand and combat deflation will be difficult. We believe

External Position

highly leveraged businesses could come under immense pressure as price reductions come through impacting cash flows and potentially the ability to service outstanding loans.

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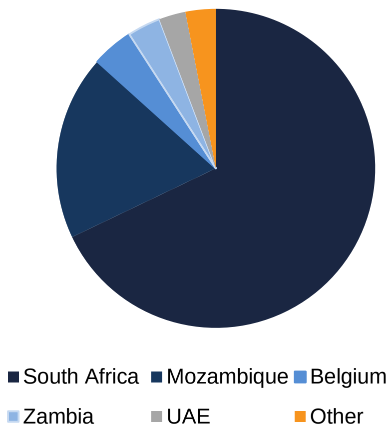
Analysis of exports

The country continues to face considerable pressure in the external sector on the back of subdued export performance. Exports to October 2014 amounted to $2.4bn and the Ministry of Finance expected them to reach $3.5bn by the end of 2014 but they closed the year at $3.06bn. The mining sector continues to drive the country's export earnings, accounting for 52% of total export earnings. Agriculture exports, mainly from tobacco and horticulture, accounts for 21% of earnings. The three largest exports for the period were flue cured tobacco (contributing 26%), gold (17%) and Ferro Chrome (9%). Figure 46 below shows the country's top 5 export destinations. South Africa takes 68% of the country's exports with Mozambique coming second at 18%. Exports are expected to increase to $3.66bn in 2015 from $3.06bn in 2014, driven by flue-cured tobacco, raw sugar and gold.

Fig 46: Monthly Export, Import and Trade Balance figures

Source: Ministry of Finance

Fig 47: Exports by destination



Source: Zimstat

Government set up various initiatives last year within the exports space, affected from 1 January 2014. Policies introduced included an export tax of 15% to be levied on un-beneficiated platinum and diamonds; Fidelity Printers and Refinery (owned by government) was allotted as the sole buyer and exporter of gold. An export tax of $0.75 per kg was to be levied on raw hide exports from January 2014 whilst the sales of rough diamonds on the local industry had been VAT zero rated.

A new corporate tax structure was proposed for exporting companies. Companies exporting between 30-40% of their goods will pay 20% corporate tax. Companies exporting 41-50% of their product will pay 17.5% corporate tax. Those exporting 51% and above of their product will pay 15% in corporate taxes. A reduction in these taxes will promote the manufacturing of competitive products in the country and encourage companies to export more therefore giving a boost to export figures.

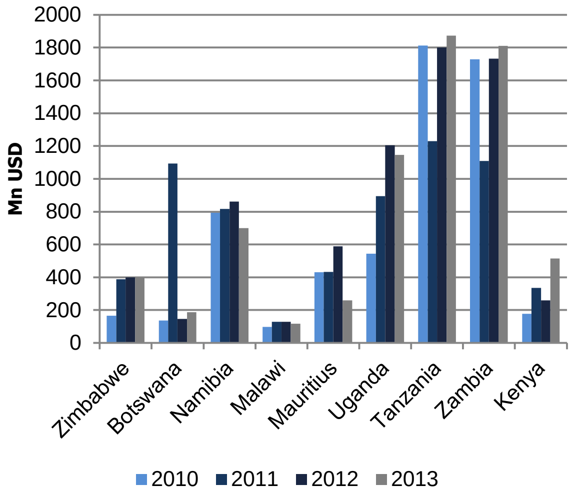
Foreign agents used by exporting companies to pre-sell products in external markets saw an exemption in withholding tax introduced (previously pegged at 15%). The condition to the tax exemption however, is that the agents cannot charge fees that exceed 5% of the value of exports based on the Free on Board prices. This measure incentivises agents to aggressively look for export markets.

FDI – key deals in 2014 and expectations for 2015

Foreign investment remains subdued due to the perceived country risk. The country received only $146.6mn to October 2014 compared to $311.3mn during the same period last year and far below the medium term policy (Monetary policy) target of $1bn for the year and some distance from the estimated requirement of $9.2bn to finance programs and projects espoused in the country's medium term plan (MTP). FDI into Zimbabwe has been on the incline since dollarization and though it remained flat in 2013 and declined in 2014, it still ranks mid-range amongst peer SSA countries (based on a four-year annual average). Post-dollarization, when Zimbabwe experienced a period of high growth off a low base, averaging 9.7% GDP growth from 2009 to 2011, there was room for high returns on investments which compensated for the country risks. Figure 47 below depicts Zimbabwe's FDI since 2009, compared to other developing African countries and Figure 48 shows FDI as a percentage of real GDP for the same countries

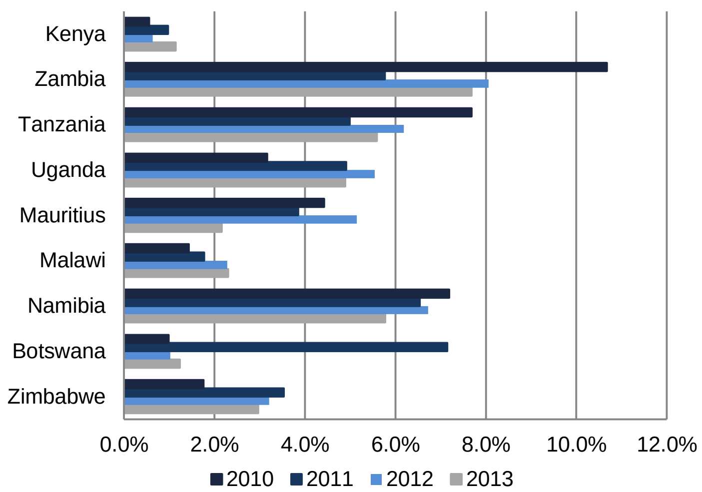
External Position

Fig 48: FDI received from 2010 to 2013 Zimbabwe vs. SSA peers



Source: UNACTD

Fig 49: FDI as a % of GDP Zimbabwe vs. SSA peers



Source: UNACTD

FDI inflows to Africa increased by 7% in 2013 to $50bn and are expected to continue to increase. However, in our view, we do not see Zimbabwe improving its share in the short to medium term due to the lack of a visible catalyst or change in policy affecting investments. FDI is likely to remain flat in 2015. The main deterrent to FDI at the moment is the lack of clarity around indigenisation policies and the inconsistency around implementation. Until we provide clarity and build a consistent track record in implementation we will continue to see subdued FDI inflows into the country. Table 12 below shows the major deals which took place last year, involving investments into both public and private enterprises by foreign investors.

Table 12: Foreign Equity Deals concluded in 2014

Company	Buyer	Value	Stake	Structure
Astra Holdings (ASTRA: ZH)	Kansai Plascon Africa Ltd and Hemistar Investments		81%	Kansai Plascon and Hemistar Investments now own 81% of Astra Holdings
TA Holdings (TAHLDS: ZH)	Masawara Holdings	$20mn	75.73%	
ABC Holdings (ABC: ZH)	Atlas Mara Co-nvest Limited	$210mn	95.84%	
Seedco	Vilmorin & Cie	$10.1mn		
Quton	Mayhco	$10mn	60%	
Hunyani Holdings Limited (HUNYANI: ZH)	Nampak Holdings Limited (Mauritius)	$2.6mn		Business Interest of Hunyani Holdings, CMB and MegaPak merged through the issue of 389.45mn Hunyani shares to the existing CMB and MegaPak shareholders. The Board then proposed to undertake an issue for cash of 46.49mn new ordinary shares in Hunyani Holdings to Nampak in consideration of $2.6mn. Name of Holding company Hunyani \ was then changed to Nampak Zimbabwe Limited
TOTAL		**$249.6mn**		

2014 major deals totalled $249.6mn which is a clear indication as to the country's shaky performance in 2014 and subdued investor appetite. With growth rates now slowing and falling in line or below peer SSA countries, the relative attractiveness of Zimbabwe compared to other SSA countries is waning. Of concern is the poor ranking of the country in terms of the World Bank Ease of Doing Business indices, which in 2014 ranked Zimbabwe 172 out of 189 countries and is expected to improve to 171 in 2015. According to this report, the three biggest problems foreigners face in terms of doing business in Zimbabwe are: the difficulty of trading across borders where costs to imports and exports are higher than SSA peers; starting a business takes an average of 90 days which is 63 days longer than our average SSA peers; dealing construction permits takes about 448 days while on average it takes about 156 days for our peers. As a destination for foreign investments, Zimbabwe generally lacks investment security, political stability, respect for property rights and an environment which has an assured high level of law and order. There is therefore a growing need to establish policy consistency and clarity in order to build investor confidence and re-establish Zimbabwe as an attractive investment destination.

It has been reported that in August, Zimbabwe and China signed 9 agreements which will see Asia providing financial support for the much-needed economic enablers in critical sectors such as energy, roads, national railway network telecommunications, agriculture and tourism a part of the ZIMASSET. On the 15th of September the country signed several trade and investment deals with the visiting high-powered Russian delegation in Harare. $1bn was also commissioned for the Integrated Platinum Group Metals Project in Darwendale on the 16th of September. A consortium of Russian firms comprising state defence conglomerate Rostec, Vi Holding and Vneshekonombank (VEB) also joined forces to invest in the Darwendale project. We do believe that the government has signed several MoUs (Memorandum of Understanding) with China and Russia but as it stands, it is still very unclear at what point funding will physically come through and projects will commence.

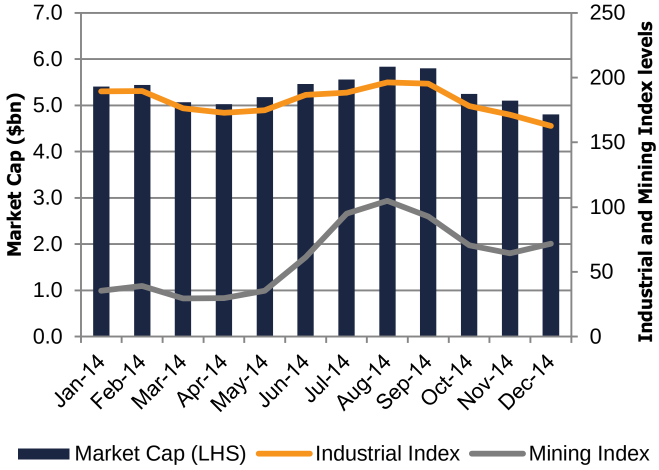
The Equities Market

Market Performance

ZSE bearish in 2014, underperforming most SSA peers

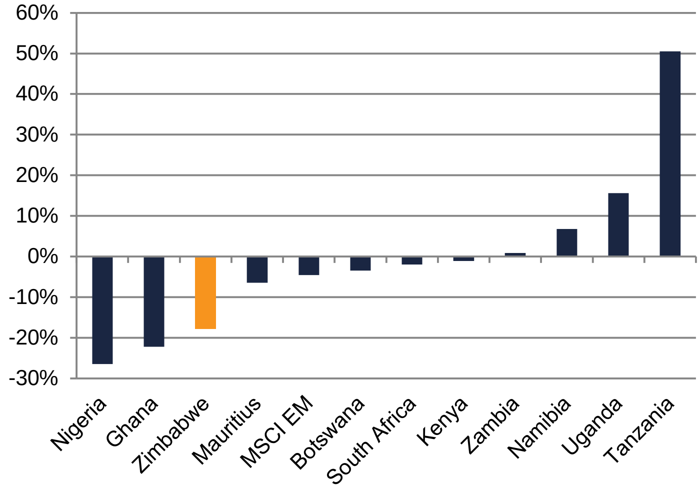
Zimbabwean equities performance for 2014 left a lot to be desired in a generally poor year for SSA markets. The ZSE saw a 17.81% decline in total market capitalisation for the year to $4.747bn. The benchmark Industrial Index returned -19.5%, below the average return for SSA markets (excluding SA) estimated at -0.9% for 2014, while the Mining Index was a bright spot advancing 56.6%, driven by a 220% return in Bindura (BINDURA: ZH). The general poor performance was driven by below par GDP growth, a continued lack of FDI, downward earning revisions, as well as poor sentiment exacerbated by political events particularly in 4Q14. Top performances (USD) in SSA came from Tanzania returning 51%, Uganda returning 16% and Namibia returning 6.8%. Worst performers were Nigeria returning -27% and Ghana -22%. Other notable markets returned in USD as follows: Kenya -1.1%%, Mauritius -6.5%, Zambia 0.9%, South Africa -2%. In 2015 15 counters registered positive gains notable amongst the larger caps being National Foods (NAFH: ZH) up 70% and Seedco (SEEDCO: ZH) up 7.8%, while 40 counters recorded losses. Performances of other key names were as follows; Econet (ECW: ZH) 0%, Delta Beverages (DELTA: ZH) -27%, Innscor (INAF: ZH) -32%, Ok Zimbabwe (OKZIMBAB: ZH) -42%, BAT Zimbabwe (BAT: ZH) -7% and Seedco (SEEDCO: ZH) +8%. There appeared to be little discernible trend between sectors as regards performance reflecting the generally poor economic environment, although retail counters were hardest hit with seven of the top ten losers on the ZSE being exposed to the Zimbabwean consumer. The top performers reflected to an extent companies involved in value accretive corporate actions.

Fig. 50: Performance of the ZSE Market Cap & Indices in 2014
(YTD: Market Cap -17.81%, Industrial -19.46%, Mining +56.61%)



Source: Zimbabwe Stock Exchange, IH Estimates

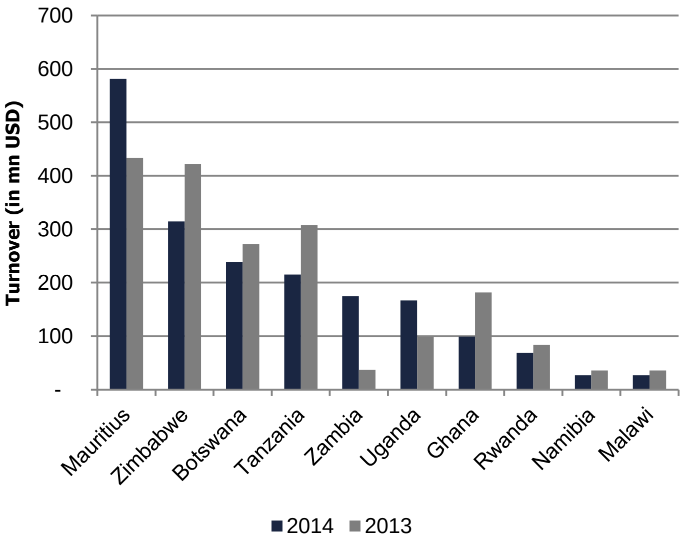
Fig 51:Performance of Zimbabwe YTD vs. selected SSA peers and EM



Source: Zimbabwe Stock Exchange, Bloomberg & Standard Bank

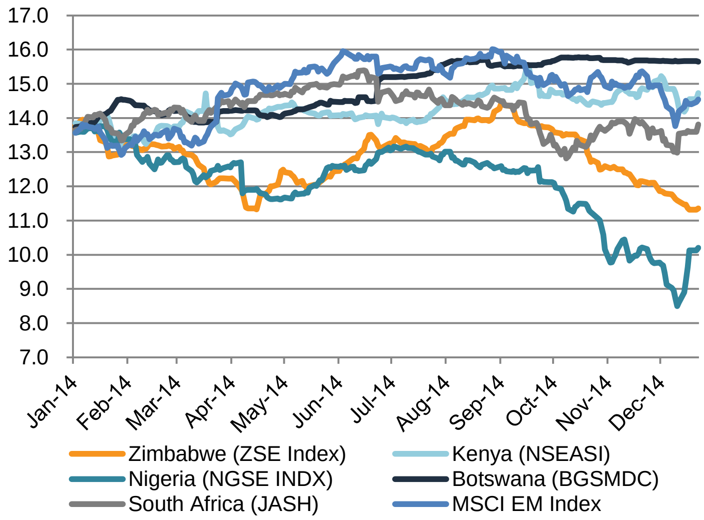
ZSE total market capitalization remained bearish throughout 1H14, sitting around $5.3bn until August 2014 when the bourse made a slight recovery to the year's peak of $5.83bn. Following political turmoil characterized by political in-fighting and factionalism that reared its head in October, the market lost ground closing the year at a total market capitalization of $4.80bn. Market activity remained subdued in 2014, with total turnover for 2014 of $452.9mn, down 7% on prior year. However relative to peer SSA countries (excluding South Africa, Nigeria and Kenya with turnover in 2014 of $280bn, $6bn and $2bn respectively), the ZSE remains one of the more liquid bourses. Africa, returning 2% and SSA (ex SA), returning -0.9%, outperformed emerging markets (MSCI EM -4.6%) but underperformed developed markets (MSCI DW +2.9%) and frontier markets (MSCI FM +2.9%).

Fig 52: ZSE Turnover vs.SSA Peers



Source: Zimbabwe Stock Exchange & Bloomberg

Fig 53: Comparison of PER: ZSE vs. SSA Peers and EM Index



Source: Zimbabwe Stock Exchange & Bloomberg

Market movers in 2014

Bindura topped the gainers board of the ZSE in 2014, registering 220% growth in the year after delivering strong financial results following the reopening of the Trojan mine in 2012 and first shipment of concentrate (since the restart) in April 2013. Furthermore, a new mining plan was devised for Trojan Mine, which was signed off in September 2013 following a competent person's review; the result was that higher grade ore (massives) could be accessed with the resultant increased grade enabling Bindura to supply more nickel into the market in 2014. Bindura's nickel production was also supported by firmer nickel prices in 2014, which improved by around 18% from the prior year following the Indonesian ban of nickel ore exports. The second highest gainer, TA Holdings, registered a 130% gain in the year after 41% shareholder Masawara Plc put out an offer to minorities to acquire all of the outstanding shares. 58.8% of minorities subscribed, resulting in Masawra Plc increasing its stake in TA Holdings to 75.7%. Nampak (formerly Hunyani), followed closely behind gaining 125% following a restructuring exercise whereby Hunyani merged with CarnaudMetalBox and Megapak Zimbabwe and undertook a $2.6mn capital raise. Other top performers involved in value accretive corporate actions included Willdale (WLDALE: ZH) (+100% return-capital raise), Zimplow (ZIMPLOW: ZH) (+83% following TPH acquisition in CY13), African Distillers (AFDIS: ZH) (+57% return-capital raise) and Seedco (+7.8% return-capital raise). Cottco (COTTCO: ZH) registered the largest loss after running into severe structural and liquidity related-issues, culminating in the company going under judicial management in 4Q14. Other significant losses were recorded in counters exposed to the Zimbabwean consumer, including retailers Truworths (TRUW: ZH), GB Holdings (GBHOLDINGS: ZH), Turnall (TURNALL: ZH) and Pelhams (PELHAMS: ZH), reflecting the depressed consumer environment as income levels dwindle and unemployment remains high.

Table 13: Top 10 Gainers and Losers of 2014

Top 10 Gainers	Y-o-Y Change	Top 10 Losers	Y-o-Y Change
Bindura	220%	Cottco	-97%
TA Holdings	130%	Truworths	-88%
Nampak	125%	GB Holdings	-75%
Willdale	100%	Turnall	-73%
Zimplow	83%	Pelhams	-70%
Star Africa	80%	ZBFH	-68%
Cafca	79%	Masimba	-65%
National Foods	70%	MedTech	-57%
Afdis	57%	Radar	-56%
Art	50%	RioZim	-55%

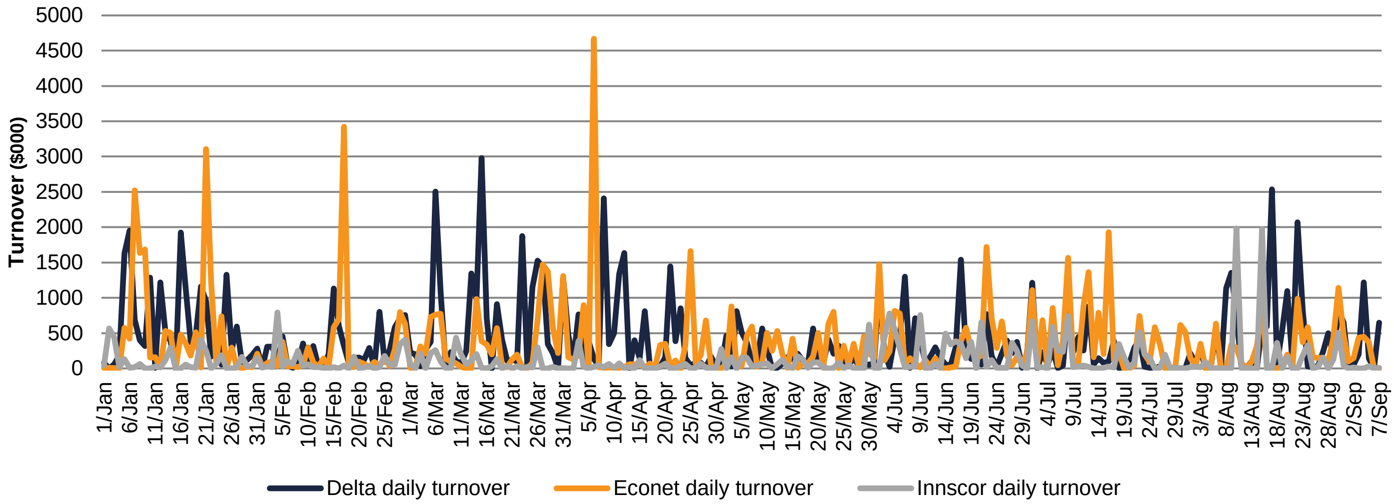
Table 14: Top 10 Most liquid counters in 2014

Top 10 Value Traded	Average Daily Turnover ($000's) 2014	2013
Delta	403.2	551.7
Econet	345.0	514.5
Seedco	212.9	28.8
Innscor	115.1	176.7
CBZ	79.8	117.2
Dairibord	40.5	59.9
Old Mutual	40.0	45.4
BAT	39.0	38.6
OK Zimbabwe	37.8	70.9
Zimplow	29.6	16.6

Source: Zimbabwe Stock Exchange, IH Estimates

Total turnover for the year amounted to $452.9mn down 7% on prior year. The three heavyweights saw a decrease in turnover compared to 2013 levels with Delta falling from $137.4mn to $100.8mn; Econet down from $128.1mn to $86.6mn and Innscor down from $44.0mn to $28.9mn.In terms of market capitalisation, they remained the three largest stocks on the ZSE, worth $1.27bn, $984mn and $324mn respectively as at 31 December 2014.

Fig 54: Daily Turnover Delta, Econet and Innscor Turnover, 2014



Source: Zimbabwe Stock Exchange

Contribution of foreign deal flow to market turnover maintains upward trend

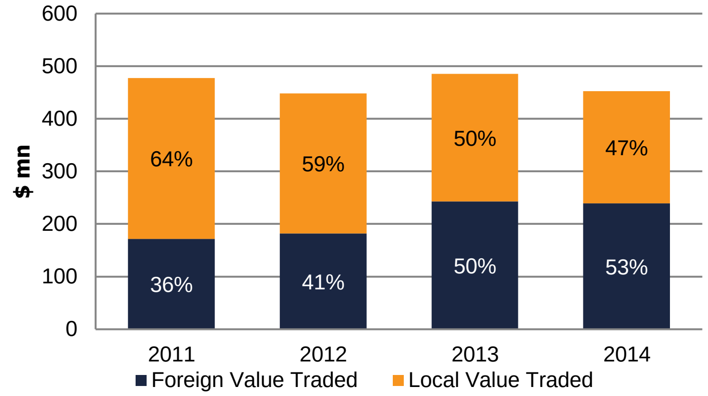
The decrease in turnover in most counters especially heavyweights Delta (-27%), Econet (-32%) and Innscor (-34%), led to a 7% fall in total turnover from $485.7mn in 2013 to $452.9mn in 2014. Other catalysts included the takeover of ABC by Atlas Mara and Cottco going under judicial management. Foreign investors' participation dipped a marginal 1% however contributing to 53% of total trades. Foreign deal flow as a proportion of the total value traded has risen from 36% in 2011 to 53% in 2014. It remains our view that even at these levels, this figure is severely understated. We believe foreign trades will continue to dominate local trades given the continued pressure on local liquidity.

Table 14: Turnover & Foreign turnover contribution

$mn	2011	2012	2013	2014
Foreign bought	190.	211.6	291	286.6
Foreign sold	152.	152.8	194.7	192.4
Foreign value traded	171.	182.2	242.9	239.5
Local value traded	306	266	242.8	213.4
Total value traded	477.	448.2	485.7	452.9
Turnover growth	**22%**	**-6%**	**8%**	**-7%**
Foreign turnover as % of total	**36%**	**41%**	**50%**	**53%**
Local turnover as % of total	**64%**	**59%**	**50%**	**47%**

Source: Zimbabwe Stock Exchange

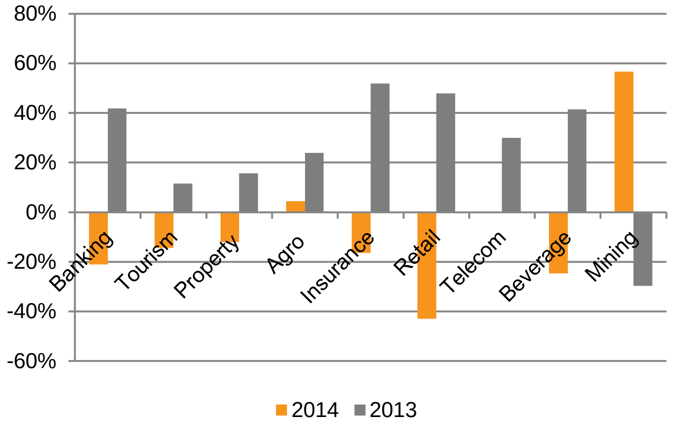
Fig 55: Foreign and Local turnover contributions



Source: Zimbabwe Stock Exchange

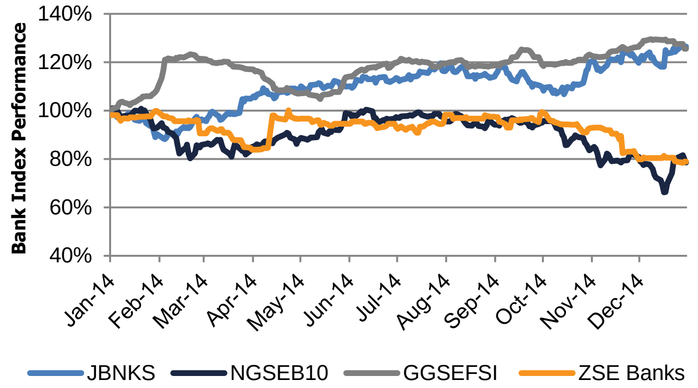
Sector Performances Review

Fig 56: ZSE Sector performances 2012 vs. 2013



Source: ZSE & IH estimates

ig 57: Performance of the ZSE Banks Index vs. SSA peers



Source: Bloomberg, ZSE & IH estimates

There appeared to be little discernible trend in performance between industrial sectors (ex-mining), reflecting the generally poor economic environment. Common issues affecting companies in all sectors included low domestic demand, deflation and a lack of liquidity. With the exception of the mining sector, performance in all other sectors came in below that recorded in 2013.

Retail sector hardest hit in 2014, unlikely to make a recovery in 2015

The retail sector (inclusive of food, clothing and lifestyle) was hardest hit, with our retail index returning -43% in 2014 compared to +48% in 2013. The Zimbabwean consumer is coming under an increasing amount of strain as the macro-environment worsens. 2014 has been characterised by the ongoing trend of consumer down-trading with a clear shift towards staples taking place, as Zimbabweans' incomes come under increasing pressure and unemployment continues to rise. The Finance Minister has estimated that just 4% of the population are formally employed in Zimbabwe, and half of them are government workers. The latter have been stretched in 2014; although the civil servant salary increment promised in January 2014 was affected in April 2014, with the fiscus under mounting pressure government has been paying civil servants later in the month than they used to. Often, government workers will receive their salaries in arrears, usually in the first week of the following month. Informalisation of the economy is also negatively affecting the sector as formal retailers face increasing competition from the informal sector. We expect little improvement to the sector as a whole going into 2015 as GDP growth is expected to underperform last year's growth levels. Furthermore, downside risk exists from the downstream effects of anticipated under-performance in the agricultural sector and possible retrenchments and salary cuts in the civil service as government comes under mounting pressure to address the ballooning and unsustainable wage bill. The plethora of import tariffs affected in 2014 aimed at protecting local industry will also exert downward pressure on retailer's margins, since in the most part stock and inputs are imported. Top picks in the retail sector include companies that are well-positioned to capture or serve lower-end customers or the informal sector as well as companies able to diversify into external regions (thereby minimizing exposure to the Zimbabwean consumer).

Mining sector top performer in 2014, selection on a per-company basis

Whilst the mining sector showed impressive performance in 2014 (+57% in 2014 vs. -30% in 2013) we highlight that this is reflective of strong performance in Bindura (BINDURA: ZH), which registered growth of 220% in the year, whilst the other listed resource-based counters recorded losses in the year. The sector as a whole under-performed in 2014, contracting by 2% in the year due to weakness in commodity prices, high costs and liquidity constraints. Bindura outperformed mining peers after a new mining plan was devised for newly-opened Trojan Mine, which was signed off in September 2013 and resulted in higher grade ore (massives) being accessed which enabled BNC to supply more nickel into the market in 2014. Nickel production was also supported by firmer nickel prices in 2014, which improved by around 18% from the prior year following the Indonesian ban of nickel ore exports. Performance at Bindura is expected to remain bullish in 2015 on the back of rising nickel prices (+8% y/y) and the resuscitation of the matte smelter refinery which is earmarked for 1Q15. In contrast, Falcon Gold (FALGOLD: ZH) is facing mounting pressures, including weak gold prices and liquidity problems which, in their latest results' outlook, management stated may result in the company being 'forced to consider shutting down its remaining mining operation, either temporarily or permanently, and/or liquidating the Company and its assets in a formal or informal arrangement'.

Banks trading at a significant discount to peers; expected to continue reducing NPLs in 2015

Zimbabwean banks posted lower USD adjusted returns then both Ghana and South Africa, whilst performing relatively in line with Nigerian peers. Despite the financial sector maintaining relatively robust liquidity levels, NPLs continue to rise; NPLs have risen from 1.6% in 2009 to the current 20%. All banking counters on the ZSE, with the exception of ABC (ABCH: ZH) which undertook corporate action in the year with the Atlas Mara transaction, registered negative returns in the year. The sector, as approximated by our banking index, lost significant ground in 2014 falling 21% in the year after registering a 42% gain in 2013. Banks are now trading at a significant discount to peers, at P/Bk valuation discounts of around 65% (average P/Bk for the sector of 0.6x vs. peers at 1.7x), making certain banks within the sector attractive at current levels. We expect weaker, undercapitalised banks to remain under severe pressure in this year maintaining the dichotomy between the larger and smaller institutions. The focus for the sector in 2015 will continue to be dealing with the NPL issues while also continuing to re-align their business models to the 'new' more informal economy.

Beverages affected by consumer down trading activities

Declining disposable incomes and generally negative sentiment have severely affected consumption patterns in this segment. We have particularly seen marked migration from aspirational high margin products to low margin affordable product. Using Delta's portfolio as a proxy, lager beer volumes have fallen over 25% during the course of the year whilst sorghum beer volumes have risen over 15% as consumers trade downwards. Sparkling beverage volumes have also steadily declined whilst alternative beverages like maheu (maize & soya based beverage) have increased. Government has reduced excise duty on lagers and Delta has put through some price reductions which going forward may arrest the rate of decline

New regulations on telecoms

Two major developments took place in 4Q14 which are expected to negatively impact on telecoms performance in 2015: firstly, a 5% excise duty on air time for voice and data was affected from 15 September 2014 which, because POTRAZ barred mobile operators from passing this onto consumers via a tariff increase, is effectively a tax on revenue. Then, in December 2014, POTRAZ issued a directive for all operators in Zimbabwe to reduce the minimum net-on-net tariff on voice and SMS from 23USc to 15USc with effect from 1 January 2015, then further downward to 12USc from 1 January 2016 and down to just 9USc from 1 January 2017. We expect this to have a negative impact on ARPUs and margins for telecoms, accelerating the already-declining voice & SMS ARPUs and seriously constraining sector revenue and earnings performance in 2015.

Central Securities Depository (CSD) – demonetisation of the ZSE

The introduction of the Central Securities Depository (CSD) on the ZSE in 2H14 will in essence shift the Zimbabwean equities market from paper based title securities (share certificates) to the holding of same securities in electronic form, effectively demonetizing the exchange. As a result the bulk of securities transactions will be processed in an electronic book entry format, thus expediting the settlement of equity transactions and ensuring compliance with international best practice. It is now mandatory to trade through the CSD, therefore all clients transacting on the ZSE must have a CSD account open with a local custodian. As at the 8th of September 2014, the CSD began on-boarding listed counters using a phased approach, where counters were on-boarded in batches each month. The last batch of counters is due to be on-boarded on 2 March 2015, after which the entire exchange will be trading on the CSD platform.

The CSD model in use on the Zimbabwe Stock Exchange is Custodian-centric as opposed to the previous model which was Broker-centric i.e brokers having the ability to collect/handle and administer share certificates and therefore playing a more prominent role in the settlement process. Under the Custodian-centric model investors must open a securities account with a registered local custodian; investors then deposit physical share certificates with the custodian as opposed to the broker and the custodian administers the 'dematerialization' process converting the paper based shares into electronic format. When transacting on the market, investors will still place their orders to trade via a stockbroker but storage, transfers, clearance and settlements will take place through the CSD system.

The implementation of the CSD has led to a revision in the transaction costs of trading on the ZSE. Whilst the transaction costs of trading on the ZSE were amended to include the charging of a CSD Levy, brokerage commission was revised downwards from 1% to 0.92%. The overall result being a slight reduction in the charges (see table x below). The current settlement cycle under CSD is T+5 days (however effectively still T+7 days as the CSD system excludes weekends), the intention is to ultimately reduce this to T+3 days. It is our view that the CSD will bring increased efficiencies to the ZSE and significantly minimise the risks of failed transactions and/or delayed settlements.

Table 15: Transaction costs on the ZSE before & after CSD

	Before		After	
	Buying (%)	Selling (%)	Buying (%)	Selling (%)
Brokerage Fee	1.00%	1.00%	0.92%	0.92%
Stamp Duty	0.25%	-	0.25%	-
Capital Gains Tax	-	1.00%	-	1.00%
ZSE Levy	0.10%	0.10%	0.12%	0.12%
CSD Levy	-	-	0.12%	0.12%
Securities Commissioners Levy	0.18%	0.18%	0.171%	0.171%
Investor Protection Levy	0.05%	0.05%	-	-
VAT	0.15%	0.15%	0.138%	0.138%
Total	1.73%	2.48%	1.719%	2.469%
Total Cost for Buying and Selling	4.21%		4.188%	

Source: ZSE

Automated Trading System (ATS)

The ZSE is currently working on systems to interface a new automated trading system (ATS) with the Central Securities Depository (CSD) in preparation for full automation of the bourse. The current plan is to complete the installation of the CSD platform and allow the exchange to trade for a trial period of 6 months to ensure efficient functionality of the platform before formally introducing ATS. In line with this plan it seems likely that ATS will be installed towards Q4 of this year. The ZSE currently operates as an open-outcry market, making it one of the very few remaining exchanges in the world still employing that method of trading; the ATS will allow stockbrokers to trade directly from their offices unlike the current situation where they have to be present at the bourse. Trades will be matched automatically and the surveillance capabilities of the ZSE will be significantly enhanced. Trading hours will then extend from the current 10am to 11am, with counters trading once in alphabetical order to continuous trading taking place from 9am to 12pm, which in our view will support a more efficient system of price discovery. The funding of the ATS project has been arranged and concluded with the Investor Protection Fund (IPF) through the issuance of a $1.5mn bond.

ZSE Equities Outlook

2015 Equities Outlook Summary

In the absence of meaningful and visible catalysts, indications point to sustained pressure on consumer demand and continued liquidity constraints in 2015. As a result we anticipate corporate earnings to remain weak going forward, particularly in H1. Our estimates show that revenues for consumer facing companies contracted 1.35% on average in FY14 and we expect run rates to remain under significant pressure in this year. In our view the key theme for corporates will be protecting margin and/or market share, potentially seeking new markets offshore, and adjusting business models to service the lower end of the market given consumer down-trading or the ability to serve the informal sector. Whilst deflation will naturally exert downward pressure on pricing of goods particularly impacting corporates that are highly leveraged, we believe that lower oil prices and reduced prices of inputs (SA based goods a large component) will assist in helping margin protection. However, our immediate preference at this time is companies not directly exposed to the Zimbabwean consumer like Seedco (SEEDCO: ZH) & Bindura Nickel (BINDURA: ZH). However we believe the falls in the market valuations may also represent a contrarian entry point in some of the more defensive consumer names, such as Econet (ECWH: ZH), Delta (DELTA: ZH) and Innscor (INAF: ZH). **We estimate our IH Universe of stocks trades on PER to 2015E of 13.8x, which is certainly not inexpensive, and the degree of uncertainty as regards the macro environment leaves us to be neutral on Zimbabwean equities relative to other SSA markets. Below is an expansion of the key themes that we believe will underpin the performance of the ZSE.**

- **Performance of key sectors, agricultural & mining**. We believe mining and agriculture which are both key drivers of the economy will be adversely affected by weakness in global commodity prices and pervasive structural issues linked to poor funding and foreign direct investment in both sectors. In addition we suspect late and then subsequently excessive rains, followed by a drought in the second half of the season, pose additional risks to agricultural output. Given that demand in the post dollarization era has been largely driven by expansion of the bottom of the pyramid (small to medium scale farmers, small scale miners, civil servants and the greater informal sector); we do expect slower stimulus in demand in 2015 relative to last year.
- **Corporate earnings to remain subdued exacerbated by deflation.** We expect liquidity pressure to persist in CY15 resulting in a continuation of low consumer demand and generally negative sentiment. Downward trading to basic, low margin goods will likely remain a trend exerting some pressure on consumer facing stocks. Deflation will be a key theme as the Rand appears likely to soften further whilst oil prices trend lower. We have already seen an impact in the pricing environment with top tier names Delta and Innscor having effected price reductions on various lines in CY14. Econet after government intervention through the regulatory body for telecom operators POTRAZ, was compelled to reduce tariffs along with competitors Telecel and NetOne. With revenues for consumer facing companies having contracted 1.35% on average in CY14, we expect sustained pressure on run rates in the short to medium term; we further expect pressure on margins to impact profitability in CY15. However the reduced prices of inputs (SA based goods a large component) will aid in providing some protection to corporates that are efficient in their procurement strategy and not highly geared. Corporates that are highly leveraged will be hardest-hit by the pervading deflationary pressures.
- **Defence of earnings via diversification & targeting of informal sector.** We expect management teams to increasingly look at defending earnings via diversification; on the local front through introducing new product lines to diversify offering and shore up declining volumes in existing core products. Delta has invested in its alternative segment introducing products like dairy based beverages, where the brewer has gained significant market share. Dairibord has introduced maheu (a maize & sorghum based beverage) and re-introduced fruit juices to defend aggregate volumes and diversify earnings. Corporates will have to tailor strategies and product to speak to the growing informal sector, cost control in new and existing lines will be a key theme as well, we expect to see a greater reliance on technology. We expect to see some continuation of M&A activity as another route to diversification; Zimplow Ltd (manufacturer of ploughs and agri-implements) acquired Tractive Power (distributor of mechanised farm machinery). However, our immediate preference at this time is companies with strong offshore earnings that are therefore not directly exposed to the Zimbabwean consumer like Seedco (SEEDCO: ZH) & Bindura Nickel (BINDURA: ZH). We generally anticipate increased appetite in local corporates to grow business outside the country; however this will result in select firms placing shareholder value at risk by engaging in new, untested business activity.
- **Financial sector relatively stable despite rising legacy NPLs**. Natural attrition continued to clean out the smaller, weaker institutions in the banking sector with the Central Bank cancelling ZABG's banking license earlier this year after the bank was deemed to be unsound. We expect weaker, undercapitalised banks to remain under severe pressure in this year maintaining the dichotomy between the larger and smaller institutions. However, we anticipate minimal disruption within the sector as a whole given the lack of a vibrant inter-bank market curtailing potential contagion effect from failing institutions. Despite legacy NPL's rising to 20%, the sector has in our view remained relatively stable with banks maintaining robust liquidity levels. The focus for the sector in 2015 will continue to be dealing with the NPL issues while also continuing to re-align business models to the 'new' more informal economy. We await to see the impact of the newly formed ZAMCO, a vehicle formed by the Central Bank to acquire asset backed NPLs, at this stage it is unclear what level of funding has been secured for the vehicle. Following a 21% decline in the sector in 2014, banks are now trading at a significant discount to peers (65% average discount for the sector), making select picks attractive at current levels
- **Capital constraints still leading to company closures.** Since 2012, we have seen 12 publicly listed companies either suspended or delisted mainly due to capital constraints. Notably in CY14, Cottco Holdings, the country's largest buyer, processor and marketer of cotton, applied for judicial management and was suspended from the ZSE. We anticipate continued distress in CY15 particularly amongst under-capitalised and highly geared corporates. In our view the most vulnerable sector will be manufacturing where low capacity utilisation and high fixed costs will exert pressure ongoing concerns.
- **Ramifications of a stronger US dollar.** Although quantitative easing has tapered off in the US, an expansionary policy has been adopted by both the Eurozone (ECB) and Japan (BOJ) implying that global liquidity will remain supportive for capital markets. However weak commodity prices and the ramifications of a stronger US dollar in 2015 will likely have negative implications for flows into emerging & frontier markets, with flow likely to favour developed markets again in CY15. In our view, the continued dollarization of the Zimbabwean economy will however put the ZSE in good stead relative to SSA peers; it is our belief that the currency protection that Zimbabwean equities offers will be a key driver in attracting flows.
- **Continued policy inconsistency to hinder much needed FDI.** Zimbabwe received FDI of $146.6mn to October 2014, well below SSA peers and some distance from the estimated requirement of $9.2bn to finance programs and projects espoused in the country's medium term plan (MTP). In our view FDI continued to be hindered mainly by the lack of clarity in government implementation of the indigenisation policy. With the Presidium now decided and the elective ZANU PF Congress concluded, it is our hope that succession politics will take a back-seat to the economy in the medium term. Given the persistent current account deficit and inflexibility around government debt (+/-70% of GDP), it is

now more crucial than ever for government to focus on creating an investor friendly environment framed by clear and consistently applied policies that will attract investment.

On the back of our macro-economic views on the factors driving equities performance in 2014, we present our views on the different sectors of firms listed on the ZSE. These are presented in table 16 below, along with the names of counters in those sectors. Differences in views on firms under coverage and their respective sectors are explained in the company notes in the following section.

Table 16: Sector Views

Sector	CY15 weighting	Comment	Company
Agriculture	**Neutral**	Early reports from the Commercial Farmers Union (CFU) and significant downside risk to Government's forecasts indicate that agricultural output may underperform forecasts this year. Yields will likely be negatively affected by adverse weather conditions, due to excessive rains, subsequent flooding and an anticipated late season drought. We have concerns around funding, particularly in maize and cotton, where structural issues continue to deter investment; we also have some concern around punitive price controls placed on small grains like maize which will affect agro-processors. We anticipate some downside risk from generally soft commodity prices in 2015. We are relatively more optimistic in names like Seedco which has diversified across the continent	Seedco (HOLD), BATZ (SELL), Hippo (BUY)
Banking	**Neutral**	Natural attrition continued to clean out the smaller, weaker institutions in the banking sector . We expect weaker, undercapitalised banks to remain under severe pressure in this year maintaining the dichotomy between the larger and smaller institutions. However, we anticipate minimal disruption within the sector as a whole given the lack of a vibrant inter-bank market curtailing potential contagion effect from failing institutions. Despite legacy NPL's rising to 20%, the sector has in our view remained relatively stable with banks maintaining robust liquidity levels. Following a 21% decline in the sector in 2014, banks are now trading at a significant discount to peers (65% average discount for the sector), making certain picks attractive at current levels	CBZ (BUY) NMB (BUY) ABCH(N/R) FBCH (SELL) Barclays (SELL) ZBFH (N/R)
Beverages	**Neutral**	Declining disposable incomes and generally negative sentiment have severely affected consumption patterns in this segment. We have particularly seen marked migration from aspirational high margin products to low margin affordable product. Using Delta's portfolio as a proxy, lager beer volumes have fallen over 25% during the course of the year whilst sorghum beer volumes have risen over 15% as consumers trade downwards. Sparkling beverage volumes have also steadily declined whilst alternative beverages like maheu (maize & soya based beverage) have increased. Government has reduced excise duty on lagers and Delta has put through some price reductions which going forward may arrest the rate of decline.	Delta (HOLD). Afdis (N/R)
FMCG	**Neutral**	This segment, similarly to beverages, is seeing significant down-trading which we expect to continue into 2015; naturally this will place considerable pressure on margins. The segment is particularly vulnerable to cheap imports which are likely to increase in the year owing to growing weakness in the Rand. This will intensify competition and exacerbate the deflation the country is currently experiencing. We are also seeing domestic competition rising in this sector and believe this will pose some downside risk to traditional players.	Dairibord (BUY), Innscor (BUY), National Foods (HOLD)
Construction	**Underweight**	The sector is currently dependent on residential developments and small scale projects. Infrastructural developments like roads, dam projects and power stations are required to drive revenues in the medium to long term. This has however been affected by limited government expenditure, with little prospect of new government-funded investment projects in 2015.	Lafarge (N/R)
Mining	**Underweight**	Indications are that hard-commodity prices will remain weak in 2015, similar to prior year. Alluvial deposits in diamonds appear to have been exhausted; with significant investment now required to embark on conglomerate mining. Generally mining costs look set to remain high as infrastructural challenges like power and water remain present. Improvements in performance across large scale gold mines requires the installation of additional capacity, which is being constrained by liquidity shortages. Platinum output will likely come in lower than prior year after Zimplats was forced to temporarily close the larger of their 4 mines. On a positive note nickel prices have been firm which bodes well for Bindura Nickel Corporation.	RioZim (N/R), Hwange (N/R), Bindura (N/R), Falgold (N/R)
Property	**Underweight**	Property companies continue to see low demand for space on the market as companies country-wide continue to rationalize and in some cases shut down. In addition there is relatively low demand for property (it is estimated Harare has +140k square metres of vacant office space), with new space continually being added to the market. As a result, the market is seeing limited scope for rental increments and landlords are in some cases having to reduce rentals to retain quality tenants. We anticipate occupancies will continue to remain under pressure and with limited scope for rental increases.	Pearl (N/R) Mashonaland Holdings (N/R) Dawn Properties (N/R)
Retail	**Neutral**	We believe fortunes will be quite mixed in this sector; it will essentially be impacted by low disposable incomes, down-ward trading to low margin goods and deflationary pressure. Whilst a weaker Rand bodes well for the supply chain of goods (60% of consumable goods imported from SA), it will also come with increased competition from smaller, mobile traders importing goods, often without paying duty and taking market share in select areas. However stocks in this sector have been over-punished which may present a cautious buying opportunity into weakness in select names.	OK (HOLD), Edgars (BUY), Truworths (BUY)
Telecoms	**Underweight**	The telecoms industry will face some downside risk from government and regulatory interventions around pricing. Effective October 2014 an excise duty of 5% on all mobile airtime was introduced and operators were not able to pass this cost to consumers. Effective January 2015 maximum thresholds were introduced on voice & sms tariffs. Voice was reduced from 23c to 15c net on net, 16c national to net, sms was reduced from 9c to 5c. We believe these measures will place downward pressure on earnings in the sector.	Econet (HOLD)
Tourism	**Overweight**	Liquidity constraints in the domestic market will continue to lead to poor performance in the local tourist market. The foreign market has however seen some improvement with increased foreign arrivals, particularly after the successful hosting of the UNWTO Conference in Vic Falls. We expect foreign arrivals to steadily improve in 2015, particularly now with EU sanctions largely lifted. However, government's newly levied 'tourist tax' of 15% on goods and services poses a real threat to competitive pricing in this sector which is already high relative to peer travel destinations..	African Sun (N/R)

IH Base-case Target Market Capitalization for 2015: $5.16bn (+10% upside)

Table 10 presents our Bear, Base and Bull cases for the ZSE's total market capitalization. Our base case market capitalization, based on GDP growth of 2% and subsequent earnings growth of 2.8% is $5,159bn at the end of 2015, representing upside of 10% from current levels. Under more bearish conditions, largely linked to underperformance in agriculture, and relatively flat GDP growth, we would expect the market to close 2015 at $4,888bn, representing upside of 4%. Our Bull case assumes more robust GDP growth at 3.2%, resultant earnings growth of 4.9% leading to total market capitalization of $5,238bn at year end, representing upside of 12%.

Table 16: Scenario Analysis for Market Capitalization

	Bear Case	Base Case	Bull Case
Economic growth	0.6%	2.0%	3.2%
Implied upside	4%	10%	12%
Target Market Cap ($mn)	**4,888**	**5,159**	**5,238**

The Companies

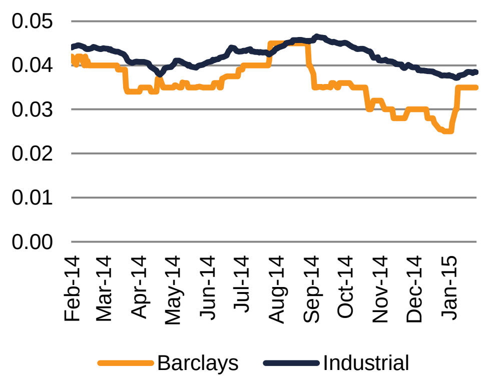
Barclays Zimbabwe

Improved earnings, higher liquidity

Barclays recorded an improved performance h/h for 1H14 as the focus remained on growing the loan book, whilst cautiously maintaining asset quality (loan to deposit ratio; 46.6% 1H14 v 42.4% 1H13). Interest income rose 18.5% h/h to $6.84mn 1H14 v $5.77mn in 1H13 despite a downward trend in interest yields. Interest expense however, fell a significant 50% h/h from $1.25mn in 1H13 to $650k in 1H14 resulting in an improved spread for the bank (NIM; 5.4% 1H14 v 6.3% 1H13). Non-funded income rose 5.1% h/h from $13.7mn in 1H13 to $14.4mn in 1H14 bolstered by a 63% lift in ledger fees ($5mn 1H14 v $3.1mn 1H13) despite generally subdued transaction activity in the environment. As a result total income grew a sturdy 9.1% h/h from $19.2mn in 1H13 to $20.9mn. Improved cost control saw operating expenses rise just 1.7% h/h to $18.4mn in 1H14 from $18.1mn in 1H13 yielding a cost to income ratio of 86.5% for the period, lower than the 93% recorded in prior comparable period; but higher than cost to income ratio of 85.8% achieved for FY13. The company saw PBT growth of 126% h/h from $1.1mn in 1H13 to $2.6mn in 1H14, a higher tax charge though resulted in a relatively less aggressive 106% increase in Net Income from $0.84mn in 1H13 to $1.7mn in 1H14. No dividends were declared in view of the need to increase the capital base in order to support future growth. Total assets rose 2.8% h/h to $297.7mn in 1H14 from $289.6mn in 1H13; loans and advances grew 13.9% h/h to $111.2mn in 1H14 from $97.6mn, concentrated in transport and distribution (30%) and light and heavy industry (28%). There was however a 4% decline in loans and advances from FY13 to 1H14 reflecting some seasonality on facility utilization by customers. NPLs rose significantly by 290% to $2.83mn in 1H14 (implied NPL ratio of 1.8%) from $0.72mn 1H13 and $1.1mn in FY13. An impairment charge of $800k was incurred in 1H14 versus $485k in 1H13, an increase of 65%. Total deposits rose 3.5% from $230.5mn in 1H13 to $238.6mn in 1H14, intuitively above total system deposit growth (1.9% in Q1 as reported by the RBZ), but slower than competitors like CBZ at 9.4%. Deposits were concentrated in trade and services (31%) and physical persons (31%). The bank's liquidity ratio closed the period at 54% significantly higher than the benchmark of 30% but lower than 57% as at 1H13. Capital adequacy was reported at 17%, higher than the required rate of 12%. RoAE came in at 4.0% for 1H14, compared to 2.2% at 1H13 and 7.0% as at FY13.

Market Data	
Report Date	02-Feb-15
Bloomberg Ticker	(BARC: ZH)
Rating	SELL
Current price $	0.04
Target Price $	0.02
Market Cap $mn	75.36
EV $mn	N/A
Market Weight	1.58%
Common Shares Outstanding mn	2153.14
Freefloat %	26.92%
Average Daily Value Traded $000's	11.07
Last Dividend declared	N/A
Dividend Yield	0.00
PER (+1)	11.96
PBV (+1)	1.36
Share price performance YTD	37.25%

12m share price performance ($) v. Ind. Index



Low cost of funds supporting relatively higher NIMs

Barclays' overlying strategy for 2H14 is to make banking more convenient to customers through further enhanced e-channels while exploring opportunities to increase efficiencies and contain costs. Internet banking volumes rose by 169% in H1 lifted by an increase in local transfer volumes; the ATM money transfer product CashSend grew 8% with customers sending higher value amounts through the channel. Whilst deposits saw slower growth than local competitors, Barclays maintained significantly lower cost of funding (FY14 est. 1.2%) thereby supporting relatively higher NIMs (FY14 est. 10.76%). We foresee the bank maintaining cost of funding in the short term with a marginal pick up to 1.3% in FY15 against potentially higher wholesale deposits. We expect deposits to see slightly more aggressive growth in 2H14 against some improvement in general liquidity, increasing by 6% y/y to FY14, we then forecast 8% y/y deposit growth in FY15. The bank aims to sustain current growth in their loan book and we therefore expect loans and advances to increase by 12% y/y to FY14, we do however expect a slow-down in growth to 10% y/y in FY15 (implied loan to deposit ratio in FY14: 49.15%). Whilst the bank has thus far maintained a low credit loss ratio through a strong focus on asset quality, we do believe that higher loan book growth will come with increased risk and therefore expect upward pressure on the credit loss ratio to 1.0% in FY14 v 0.6% in FY13. With lending rates trending downwards we do anticipate that NIMs will ease for the bank in FY15, also compounded by slightly higher cost of funding; we forecast NIM of 10.76% in FY14 but expect this figure to trend towards 9.68% in FY15.

We maintain our SELL Recommendation

As Barclays looks to emerge from its previously conservative approach and write more loan business, we expect some earnings growth to begin to come through exerting a positive impact on RoAE. We forecast RoAE of 11.4% to FY14 and then some uplift to 12.0% in FY15 before stabilising around 12.0% going forward. The bank has been passing up on dividends in order to increase the capital base to meet RBZ's requirement of $100mn by 2020 through retained earnings. However we do expect the bank to issue a small dividend in FY15 translating to a dividend yield of 0.8%. We forecast FY14 net income to come in at $5.38mn, 82% higher than FY13. We estimate that Barclays trades on PER (+1) 12.0x, and P/BV (+1) 1.36x to 2015E compared to regional peers at PER 7.97x and P/BV 1.73x for 2015E. Using a blended DDM and static ROE valuation method we arrive at an improved 12 month target price of USD0.02, however still implying significant downside at current levels. We therefore reiterate our **SELL** rating on Barclays.

	Total Income ($mn)	Net Income ($mn)	BVPS ($)	EPS ($)	DPS ($)	RoAA	RoAE	P/E	P/Bk	Div yield
2013	38.796	2.952	0.021	0.001	0.000	1.0%	7.0%	25.5	1.7	0.0%
2014E	42.132	5.380	0.023	0.002	0.000	1.7%	11.4%	14.0	1.5	0.0%
2015E	43.787	6.299	0.026	0.003	0.000	1.9%	12.0%	12.0	1.4	0.8%
2016E	46.005	7.029	0.029	0.003	0.000	2.0%	12.0%	10.7	1.2	1.1%
2017E	48.522	7.948	0.032	0.004	0.001	2.1%	12.2%	9.5	1.1	1.5%

BAT Zimbabwe

Cigarette sales flat, margin pressure from packaging and refurbishment costs

BAT's revenue for the six months ended 30 June 2014 came in at $20.33mn, 12.1% down from the $23.14mn recorded in 1H13; this was mainly as a result of the termination of the cut rag line in June 2013. Sales of their local brands were flat against the same period last year, whilst Dunhill volumes grew 65% on continued success in the Switch varieties; revenue from cigarette sales in 1H14 were down 1% y/y. GP Margins came under pressure in 1H14 as a result of increased packaging costs due to a change in size format, whereby the 10-pack SKUs are gaining popularity as consumers respond to affordability challenges, as well as increased refurbishment costs from manufacturing equipment upgrades. GP margins in 1H14 were 67.9% compared to 69.0% in 1H13. Depreciation costs also rose following the equipment upgrades; as a result operating profit on a like for like basis (excluding extraordinary income and expenses) was down 24.8% y/y. However, due to a significant reduction in share-based payment expenses associated with the BAT Zimbabwe Employee Share Ownership Trust, on a non-adjusted basis operating profit came in at $7mn in 1H14, compared to $2.4mn in 1H13. Net income for the period was $5.33mn, translating to EPS of $0.26. An interim dividend of $0.30 per share was declared, with $0.04 being financed from retained earnings. Due to the timing of payments for tobacco leaf purchases and the settlement of payables to related parties, operating cash flow of $5.0mn was generated, down from $15.4mn generated in 1H13.

Uplift in sales in 2H14; decline in FY15 following excise duty increase

We expect an uptick in sales volumes performance in 2H14 on the back of increased promotional activity and enhancements to the route to market made in 2H and as income generated from a bumper tobacco season filters through to consumers. As such, we have forecast sales volumes growth of 4% y/y in FY14 to bring in revenue of $42.1mn, down 5.6% y/y as a result of the cessation of the cut rag line in 2H13. We have forecast GP margins of 66.5% in FY14 (67.5% in FY13), weighed down by packaging and refurbishment costs. An increase in excise duties from $15/mille to $20/mille was announced in the 2015 budget statement and affected from 1 December 2014. In response to the revision in excises, BAT have increased the recommended retail price (RRP) of their core brands from $1.30 per 20s pack box to $1.50 per box, passing on to the consumer the full excise increase (from 30USc per box to 40USc per box) as well as an additional 10% increase in the trade price. Although the increase in excise and resultant price adjustments are expected to reduce industry sales volumes by 5% in CY15, management are still confident that BAT will register positive, albeit moderate, sales growth in FY15. According to management estimates, prior to the excise increase, only an estimated 40% of retailers were charging the RRP of $1.30 per box, whilst the remaining 60% were charging $1.50 per box due to coinage issues. Management feel that there is a better chance of achieving RRP compliance in retail at $1.50 because it is a more convenient price point for consumers and retailers. Furthermore, because cigarette prices have been increased industry-wide, with competitors increasing their prices from the convenient $1.00 per pack, management believe that they will be able to use this opportunity to grow BAT's market share. Whilst we believe BAT will gain some market share in FY15, we are less confident that the company will be able to achieve positive volumes growth in FY15, and have forecast a 2.5% contraction in sales volumes in the year. In a difficult operating environment, and where many retailers are now operating in the informal sector, we believe that it will be difficult to entice retailers to forfeit their margins and retain the $1.50 RRP. Theoretically, the newly availed coinage will make it easier for retailers to pass on such an increase without having to consider what pricing level is 'convenient' or 'rounded' to the customers; we do acknowledge however that take-up of the local coins has been slow, and that psychology plays a part in price-determination in Zimbabwe. We expect revenue to fall a more moderate 2.3% to $41.2mn in FY15, supported by the 10% trade price increase. The latter will also lead to some margin uplift in FY15; we forecast GP margins to increase from 66.5% in FY14 to 67.5% in FY15. We forecast EBITDA of $16.5mn in FY15 and PAT of $10.6mn.

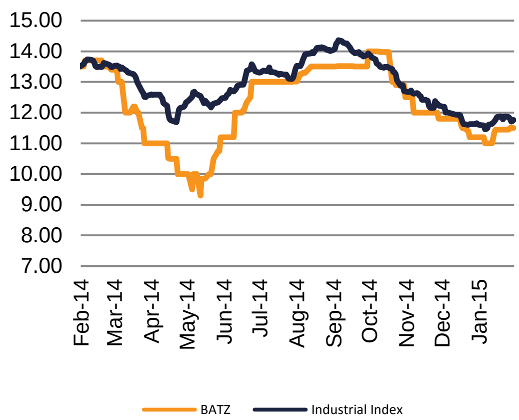
We maintain our SELL recommendation

Based on our adjusted forecasts, we estimate BAT Zimbabwe trades on a P/E (+1) of 22.3x and an EV/EBITDA (+1) of 14.6x, compared to peers with P/E of 16.1x and EV/EBITDA of 10.5x for 2014E. Using a weighted combined multiples valuation method (P/E & EV/EBITDA) and applying a 10% discount, we have arrived at a blended 12mnth target price for BATZ of **$9.76**, implying downside of 15% at current levels. We thus maintain our **SELL** recommendation.

Market Data

Report Date	02-Feb-15
Rating	SELL
Bloomberg Ticker	BAT: ZH
Current price $	11.50
Target Price	9.76
Market Cap $mn	237.29
EV $mn	230.21
Market Weight	5.03%
Common Shares Outstanding mn	21
Freefloat mn	15.5%
Average Daily Val. Traded $'000	38.56
Last Dividend declared	1H14
PER (+1)	22.28
EV/EBITDA (+1)	14.69
Dividend Yield	1.57%
ROE	30%
Share price performance YTD	3%

12m share price performance ($) v. Industrial Index



	Total income	EBITDA	Net Income	EPS ($)	DPS ($)	EBITDA Margin	EV	Net Debt	EV/Sales	EV/EBITDA	P/E	P/Bk	Div yield
2013	44.6	11.8	3.8	0.183	0.18	26.4%	230.2	-7.1	5.4	20.5	62.9	21.83	1.6%
2014E	42.1	16.4	10.7	0.516	0.53	38.9%	232.0	-5.3	5.7	14.7	22.3	22.46	4.6%
2015E	41.2	16.5	10.6	0.515	0.53	40.0%	233.7	-3.6	5.8	14.6	22.3	23.14	4.6%
2016E	41.3	16.1	10.3	0.497	0.35	39.0%	231.3	-6.0	5.6	14.9	23.1	17.80	3.0%
2017E	40.8	16.0	10.1	0.488	0.34	39.2%	228.6	-8.7	5.7	15.1	23.6	14.51	3.0%
2018E	42.4	16.6	10.5	0.507	0.41	39.1%	227.2	-10.1	5.5	14.5	22.7	12.86	3.5%

Banking

CBZ Holdings

Momentum in deposit growth remains strong amidst cautious lending

Given a highly constrained liquidity environment CBZH reported a fair set of results for 1H14 showing sustained momentum in deposit growth, amidst a clearly more cautious approach to lending. The group recorded total income of $69.6mn for the period (1H14), relatively flat h/h compared to $69.2mn achieved in prior comparable period (1H13). Net interest income fell 7% h/h to $41mn in 1H14 against slower loan book growth and lower NIMs; net interest income contribution to total income mix as a result declined to 59% in 1H14 from 63% in 1H13. Non-interest income, however, showed good improvement rising 16% h/h to $24.8mn, translating to a total contribution of 36% to mix (up from 31% in 1H13); this was primarily driven by higher commission and fee income in 1H14, up 28% to $18.8mn. Contribution to total income from underwriting income fell from 6% in 1H13 to 5% in 1H14 as net underwriting income declined 4% to $3.8mn in the period. Operating expenditure rose 10% to $46.4mn in 1H14, driven primarily by a 21% increase in admin expenses to $17.8mn, whilst staff costs were relatively contained (up 2% h/h). This yielded a cost to income ratio of 66.7% for the group up from 60.8% in 1H13 and higher than the regional benchmark of 60%. Total advances grew a moderate 1.5% to $1.04bn in 1H14 from $1.03bn in FY13 reflecting a more cautious approach to lending within the bank. NPLs closed 1H14 at a reported $66.8mn versus $47mn reported at FY13 yielding a higher NPL ratio of 6.1% for 1H14 versus 4.4% for FY13. Total provisioning increased 40% to $50.1mn in 1H14 from $35.9mn as at FY13, suggesting a coverage ratio of 0.75. Impairments for the half came in at $7.6mn versus $6.6mn for prior comparable half and $19.4mn as at FY13. Total deposits rose 9.4% to $1.5bn in 1H14 from $1.3bn as at FY13; given national deposit growth of 1.9% when last reported at 1Q14, we can safely assume that CBZ is likely ahead of the curve for the period and continuing to cannibalise deposits from weaker institutions. PAT fell 20% h/h to $12.8mn in 1H14 from $16mn in FY13, EPS came in at USc4.13 down 27% h/h. As a result annualised ROE continued to decline, falling to 11.8% as at 1H14 from 16% as at FY13; annualised ROA similarly fell to 1.8% as at 1H14 from 3% as at FY13. The group declared an interim dividend of USc0.183 suggesting 10.2 times cover.

Improving asset quality, diversifying income streams

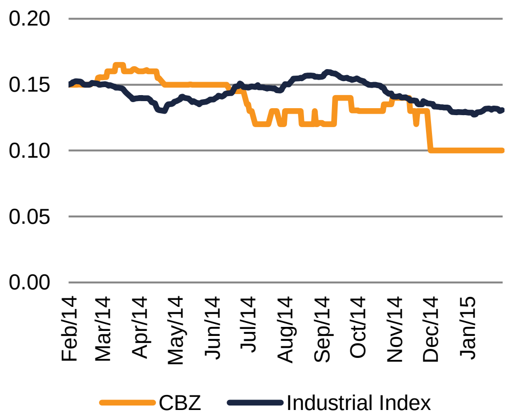
There is a clear drive within the bank to improve asset quality in the short term, as displayed by higher provisioning and increased impairments. We anticipate that CBZ will impair around $20.1mn in FY14, slightly higher than the $19.4mn impaired in FY13. This will continue to impact short term profitability for the group causing ROEs to moderate downwards – we forecast RoAE to close FY14 at around 13.1%, before recovering to 13.7% in FY15. In addition to enhancing collection efforts on failed relationships, management is looking to migrate better grade customers onto more conducive credit terms to enhance their repayment capacity. This will be done on the backbone of the $200mn bond that the group aims to complete this year; the target is a lower coupon rate of 7% versus 8.5% on the previous $68mn bond and tenure beyond 3 years. Along with this, the CBZ Global Fund has now been established in Mauritius as a vehicle to mobilise additional resources for onward lending into infrastructure, low cost housing and power. As a result we do expect to see some uplift in term loans and stable liquidity given less pressure on demand deposits particularly in FY15. Some earnings support will come through from non-banking income which stood at 5.2% of total income in FY13 and closed at 7% in 1H14, the group's long term goal is to increase non–banking income to 20% of mix; this will be primarily driven by income growth from insurance and plans to unlock value from the group's $67mn land bank. Management forecasts 20% total asset growth to FY14, 7% advances growth, 22% deposits growth and 8% total income growth.

Valuation remains attractive at current levels despite TP downgrade

We anticipate lower earnings in the short term (FY14/15) as the bank continues to clean the loan book through aggressive impairments. We estimate that NIM will close FY14 at 6.3% and then moderate to around 6.0% in FY15. We now forecast FY14 net income of $28.6mn (down 22% y/y) and then a subsequent recovery to $33.8mn in FY15. We now estimate that CBZ trades on PER (+1) 1.84x, and P/BV (+1) 0.24x to 2015E, compared to regional peers, at PER 8.80x and P/BV 1.79x to 2015E. Using a blended DDM and static ROE valuation method, we now arrive at a 12m target price of USD0.19, implying upside of 90% at current levels. We therefore reiterate our **BUY** rating on CBZ.

Market Data	
Report Date	02-Feb-15
Bloomberg Ticker	CBZ: ZH
Rating	BUY
Current price $	$0.10
Target price $	$0.19
Market Cap $mn	68.72
EV $mn	N/A
Market Weight	1.46%
Common Shares Outstanding mn	687.23
Freefloat (%)	37%
Average Daily Value Traded $000's	77.88
Last Dividend declared	1H14
Dividend Yield	3.69%
PER (+1)	1.84
PBV (+1)	0.24
Share price performance YTD	0%

12m share price performance ($) v. Industrial Index



	Total Income ($mn)	Net Income ($mn)	EPS ($)	DPS ($)	BVPS ($)	P/E	P/BV	Div Yield (%)	RoAA	RoAE
2013	150,545	36,469	0.06	0.00	0.35	1.90	0.34	2.8%	2.6%	20.0%
2014E	154,393	28,594	0.05	0.00	0.37	2.17	0.27	3.7%	1.7%	13.1%
2015E	163,683	33,799	0.05	0.00	0.42	1.84	0.24	4.4%	1.8%	13.7%
2016E	173,141	39,741	0.06	0.01	0.48	1.56	0.21	6.4%	2.2%	14.2%
2017E	183,955	46,435	0.07	0.01	0.55	1.34	0.18	7.5%	2.0%	14.5%

FMCG

Dairibord Holdings

1H14; Lower revenues but improved operating loss

Dairibord's 1H14 earnings reflected the current strain in consumer demand; the fall in revenue was however more significant than FMCG peers (peers average -1.8% v Dairibord -11%). This was attributed to lower disposable incomes having a more marked impact on products that are deemed non-basic; which constitute the bulk of Dairibord's offering. Revenue was down 11% h/h, falling to $43.79mn in 1H14 v $49.05mn in 1H13; this was against lower sales volumes, down 6% h/h to 30mn litres in 1H14 from 32mn litres in 1H13. Within the group's various segments, liquid milk volumes were up 2% on aggregate despite lower raw milk intake for the period (1H14 12.7mn litres v 1H13 13.3mn litres, down 4%); food volumes were down 14% h/h, beverage volumes were down 11% h/h. The group did benefit from FY13's rationalisation exercise, with overhead costs declining 8% in 1H14, in addition there was no repeat of the once-off costs experienced in 1H13 leading to an improved operating loss of $627k in 1H14 v operating loss of $3.1mn in prior comparable period. EBITDA came in at a positive $1.52mn in 1H14 v negative $1mn in 1H13. The company made a loss after tax of $337k for the period compared to a loss after tax of $3,4mn in 1H13 resulting in 1H14 EPS of –Usc0.09 v 1H13 –Usc0.95. In light of the subdued performance of the group and need to preserve cash, no dividend was declared. Borrowings increased by 37% in H1 to $9.7mn as the group continued to invest in new products and capacity development, however the structure of debt improved with the bulk of debt migrated to long term in contrast to prior comparable period (average all in cost 10.6%). Despite the operating loss, the group did sustain positive operating cashflows, albeit lower h/h; 1H14 $262k v 1H13 $1.9mn, the decline was attributed to increased working capital requirements to support new products.

Growing volumes through new products and product extensions

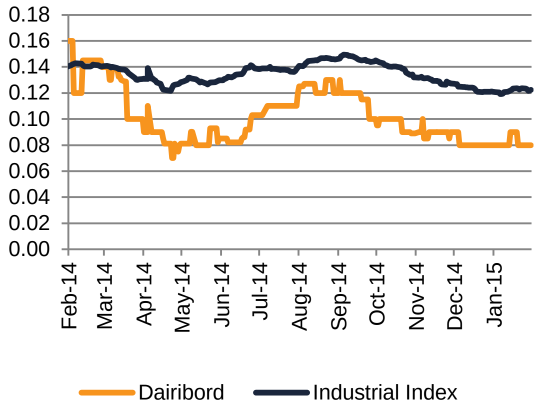
Capital investments made by the group in H1 amounted to about $4.8mn focused on lines viewed as having growth potential. Namely processing and filling equipment for new beverage Pfuko-Udiwo Maheu, a segment in which Dairibord will be challenging current market leader Delta for market share. Sales volumes are reported to be ahead of initial projections at this stage, however given late product launch in May, the impact on beverage volumes will most likely be felt in H2. Investments were also made in processing and filling equipment for Aqualite Water to meet rising demand for bottled water; and bulk yoghurts to increase line flexibility in SKUs, these plants were both commissioned in July, once again positioning the group for some volumes growth in H2. In addition a new ice cream plant was due to be commissioned in August which will allow for greater product innovation around ice-creams and improved production capacity and efficiencies. The group imported another 90 heifers under the Heifer Importation Scheme in 1H14 and a further batch of 90 heifers were expected in August, amounting to 180 heifers this year as raw milk supply remains a priority. The softening of global commodity prices bodes well for the group's cost structures with the cost of key inputs like milk powders and sugar moderating below previous highs. Malawi continues to be a challenge for the group with raw milk intake declining 35% h/h in 1H14 due to quality challenges, this resulted in a weak performance in Malawi's liquid milk segment which exerted downward pressure on the overall milk portfolio for the group. Management states that they have now deployed strategies to restore milk intake volumes in Malawi.

Upgrade in valuation on expected return to profitability in FY15

Whilst we do anticipate a recovery in sales volumes in H2 against the group's H1 investments into capacity; we foresee revenue closing the year 7% down y/y to $92.7mn. We estimate some EBIT recovery after the once off costs put through in FY13 and cost savings accruing thereof but still anticipate some cost pressure against lower revenues. We expect a reduced Loss after Tax of $57k to FY14, improved from the $1.8mn loss in FY13. However going forward we expect a return to profitability in FY15; we forecast revenue to rise 3.4% to $95.9mn and EBITDA to recover significantly by 68% to $7.4mn, against greatly improved margins relative to FY14. We anticipate PAT to come at $1.7mn reversing our forecast FY14 loss. We estimate that Dairibord trades on PER (+1) 17.2x and EV/EBITDA (+1) 5.1X to 2015E v peers trading at PER (+1) 22.36x and EV/EBITDA (+1) 12.72x to 2015E. We now derive a 12m target price of USc10.7c, implying upside of 34%. At current levels we rate Dairibord as a cautious **BUY**.

Market Data	
Report Date	02-Feb-2015
Bloomberg Ticker	DZLH: ZH
Rating	BUY
Current price $	0.08
Target price $	0.11
Market Cap $mn	29
EV $mn	32
Market Weight	0.60%
Common Shares Outstanding mn	358.00
Freefloat (%)	41%
Average Daily Vol. $000's	39.56
Last Dividend declared	FY12
Dividend Yield	1.2%
PER (+1)	17.24
EV/EBITDA (+1)	5.06
Share price performance YTD	0%

12m share price performance ($) v. Industrial Index



	Revenue	EBITDA	Net Income	EPS ($)	DPS ($)	EBITDA Margin	EV	Net Debt	EV/Sales	EV/CF	EV/EBITDA	P/E	P/Bk	Div yield
2013	100.1	1.7	-1.8	-0.005	0.000	1.68%	33.3	4.6	0.3	3.6	19.7	-16.3	0.6	0.0%
2014E	92.7	4.4	-0.1	0.000	0.000	4.74%	38.1	9.4	0.4	2.4	8.7	-502.3	0.6	0.0%
2015E	95.9	7.4	1.7	0.005	0.001	7.73%	37.5	8.9	0.4	3.0	5.1	17.2	0.6	1.2%
2016E	99.6	8.1	2.1	0.006	0.001	8.10%	36.6	7.9	0.4	2.7	4.5	13.5	0.6	1.5%
2017E	103.5	8.8	2.6	0.007	0.001	8.47%	35.2	6.6	0.3	2.5	4.0	11.0	0.6	1.8%

Beverages

Delta Corporation

1H15: Portfolio mix defends stability in aggregate volumes

Delta delivered a sobering but largely expected set of results for H1 to end of September 2015 reflecting sustained pressure on consumer spend in an increasingly difficult environment. Strengthening sorghum beer volumes (up 14% h/h to 2,037k hl) offset severe declines in lager beers (down 25% h/h to 695k hl) and sparkling beverages (down 9% to 708k hl) to provide some stability to aggregate volumes that were down a marginal 1% h/h to 3,553k hl. The business continued to make strides in alternative beverages, growing volumes in this segment 16% h/h to 93k hl in line with the strategic intent to increase footprint in the broader beverage space. Net revenue fell 4% h/h to $302.2mn ($291mn excl discontinued operations (on deconsolidation)– Megapak). With the continued migration of consumers down the value chain to more affordable product, operating margin declined from 23.04% in prior comparable period to 21.56% in 1H15. As a result EBIT fell 9% h/h to $56.9mn, whilst EBITDA fell 4% h/h to $74.4mn for the period implying a margin of 24.6%. Improved net finance income provided some uplift to earnings adding $2.24mn in 1H15 versus $1.12mn in 1H14. Similarly the share of associates profit was significantly improved in 1H15 at $1.06mn versus $361k achieved in 1H14. Attributable income for the group came in 7% below prior comparable period at $44.1mn for 1H15 versus $47.2mn in 1H14. Despite recording a decline in income, Delta declared an interim dividend of USc1.35 per share up 4% from prior comparable period; payable to all shareholders registered on the books as at 5 December 2014. The group showed an improvement in free cash-flows, producing $41.1mn for the period vs $35.4mn in 1H14 aided by lower capex spend. Investment activities were down 52% h/h to $13.6mn as the group spent significantly under the authorised capex budget for the period.

Delta 3Q15 trading update, leveraging product mix to defend value

With the group now largely captive to an illiquid market characterized by declining consumer spend, the forward looking strategy will have to centre on defending both volume and value through product mix management. Disturbingly the higher margin lager volumes have dropped to post dollarization levels last seen in FY11 with affordability still an issue despite price reductions amounting to 13% (including reversal of excise duty increment) effected in Q2/Q3. We see this trend being sustained to FY15, albeit a marginal recovery in mainstream and economy segments, as the consumer remains illiquid. Delta's 3Q15 trading update did show a slow-down in the rate of decline in lagers compared to the preceding quarter; lager beers were down 9% q/q and 20% for the 9 months. To defend aggregate volumes the group will continue to focus on the present opportunity in Chibuku and particularly the higher margin Chibuku Super where growth has been limited by capacity constraints; a second bottling line is due to be commissioned in June 2015 in the southern part of the country (Bulawayo) to improve availability of product. Due to the above mentioned capacity constraints particularly over the festive season, volumes declined 1% q/q but were up 8% for the 9 months. Potential threats to the business particularly in this space going forward include price controls placed on small grains by government, particularly maize (gazetted purchase price of $390 per ton vs regional price of $220/250 per ton); this could present a significant uplift in input costs that the business will not be able to pass onto to the consumer through higher pricing without substantial impact to volumes. Bulk packs imported from neighboring countries continue to affect SB volumes aided by current USD strength. SB volumes were down 5% q/q and 6% for the 9 months. On the regulatory side however, Delta has successfully lobbied government for the reduction of excise duties from 45% back down to 40%.

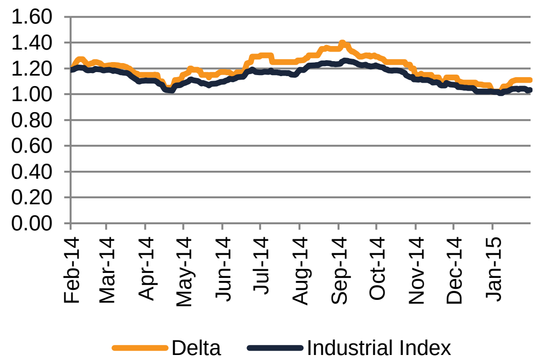
Downgrade in valuation on lower earnings

Given our observations on volumes, we now expect Delta's revenue to decline 8.8% y/y to $570mn in FY15, followed by marginal recovery of 1.5% to $578mn in FY16. We believe underperformance from lagers will reverse margin expansion & now forecast FY15 EBITDA to come in at $140.3mn, 15% lower y/y. Again we expect some uplift in FY16 in EBITDA to $143.7mn, up 3% y/y. We forecast a significant 22% y/y decline in net income to $81.6mn for FY15, with a subsequent recovery to $86mn in FY16. We estimate Delta trades on PER 16x to FY16 relative to SSA peers trading at 21.41x to FY16. We estimate on an EV/EBITDA basis Delta trades 9x to FY16 versus SSA peers at 10x. Against declining earnings, using a combined multiples and DCF approach we now revise our 12m target price downwards from $1.38 to $1.28 implying 15% upside at current levels. We rate Delta with a **HOLD** recommendation.

Market Data

Report Date	02-Feb-2015
Bloomberg Ticker	DELTA: ZH
Rating	HOLD
Current price $	1.11
Target price $	1.28
Market Cap $mn	1383
EV $mn	1386
Market Weight	29%
Common Shares Outstanding mn	1246
Freefloat (%)	12%
Average Daily Val Traded $000's	619
Last Dividend declared	1H15
Dividend Yield	3%
PER (+1)	16.95
EV/EBITDA (+1)	9.52
Share price performance YTD	9%

12m share price performance ($) v. Industrial Index



	Net Revenue	EBITDA	Net Income	EPS ($)	DPS ($)	EBIT Margin	EV	Net Debt	EV/Sales	EV/EBITDA	P/E	P/Bk	D/Y
2014	625.5	165.3	105.7	0.08	0.03	26.4%	1,367.4	-15.2	2.2	8.3	13.1	3.4	3.1%
2015E	570.3	140.3	81.6	0.07	0.03	24.6%	1335.7	-46.9	2.3	9.5	17.0	3.1	2.7%
2016E	578.3	143.7	86.5	0.07	0.03	24.8%	1,298.4	-84.3	2.2	9.0	16.0	2.8	2.8%
2017E	592.9	148.3	92.6	0.07	0.03	25.0%	1246.6	-136.0	2.1	8.4	14.9	2.5	3.0%
2018E	592.6	147.7	96.4	0.08	0.03	24.9%	1,191.4	-191.2	2.0	8.1	14.3	2.3	3.1%

Telecoms

Econet Wireless Zimbabwe

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Revenue in line with expectations, bottom line disappoints

Econet financials for the six months to August 2014 were broadly in line with our expectations at the top line, but the contraction in margins was much more pronounced than we expected. Revenue grew 4.2% h/h to $392.3mn, driven by data and EcoCash. The former registered revenue growth of 72% h/h to $54.9mn (subscribers +31% h/h and ARPUs +37% h/h) whilst EcoCash achieved revenue growth of 111% h/h (subscribers +23% h/h; value of transactions +108% h/h). Revenue from Voice & SMS continues to decline, bringing in revenue of $275mn in 1H15, down 6.8% h/h, weighed down by a 15% decline in Voice and SMS ARPUs. EBITDA margins fell a significant 5.4 percentage points from 44.9% in 1H14 to 39.5% in 1H15, due to a change in the sales mix as lower-margin data and overlay services continue to make an increasingly significant contribution to revenue. Operating costs increased 11.6% from the prior period to $251mn in 1H15, most notably from an increase in employee costs (up 23% h/h to $48mn), direct costs (up 94% h/h to $31mn) and computer costs (up 100% h/h to $10mn). The increase in costs is attributed to product development and expansion, as well as investment in the network, necessary to support the launch and expansion of new products in order to make inroads into these novice markets. The increase in direct costs was also due to an increase in MMT commissions (emanating from the mobile money transfer tax of US$0.05 per transaction, levied with effect from 1 January 2014) and cost of sales related to devices, as Econet has started selling data-capable smart phones, for as cheap as $55, to onboard customers onto data. EBITDA for 1H15 was $155mn, 8% lower than the $169mn EBITDA realised in 1H14. Depreciation and Amortisation increased 32% h/h, as a result of the amortisation of the $137.5mn licence renewal fee and high levels of capex in the year ($79mn or 20% of revenue). As a result, PAT declined 29.3% h/h to $49.8mn. An interim dividend of 0.61USc was declared.

Recent developments in the industry putting pressure on ARPUs and Margins

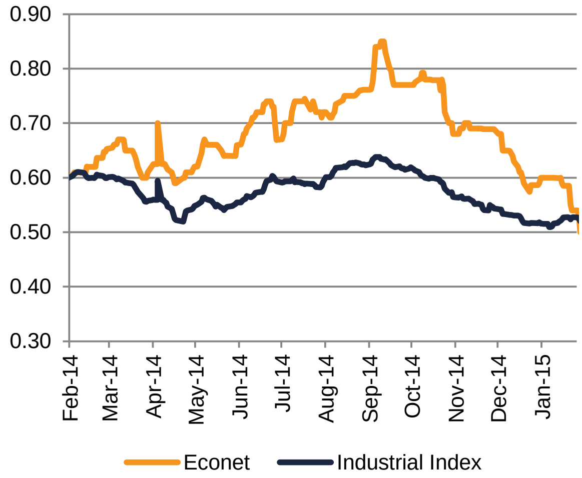
We expect to see a decline in voice and data ARPUs in 2H15, following a 5% excise duty on air time for voice and data, which was effected from 15 September 2014. Because POTRAZ barred mobile operators from passing this onto consumers via a tariff increase, this is effectively a tax on revenue. A 25% duty levied on mobile handsets effective from 1 October 2014, is not expected to have any material impact on existing ARPUs but will likely have a negative impact on Econet's strategy to grow data ARPUs by retailing low cost smart-phones. Last month, POTRAZ issued a directive for all operators in Zimbabwe to reduce the minimum net-on-net tariff on voice and sms from 23USc to 15USc with effect from 1 January 2015 (then to 12USc from 1January 2016 and down to just 9USc from 1 January 2017). In response, Econet has stopped all price promotions on voice and sms, with effect from 1 January 2015 and is no longer offering dynamic discounting or promotional bundles. Before the reduction in tariffs, Econet's average tariff was estimated at USc15, whereby the higher-end segment of the subscriber base, who did not take advantage of promotions and discounts (estimated to be around 50% of the total subscriber base) were paying close to the 20USc mark whilst the 50% lower end subscribers who made use of the bundles and discounts were paying around USc11. This means the 50% higher end of the segment will be, on average, paying less than they were before the tariff cut, whilst the lower-end 50% will be paying more. Since the lower-end subscribers are inherently more price sensitive, it is likely that volumes will drop, especially since competitors are at this stage still offering discounts and bundles, thereby increasing the churn rate. Therefore, we expect declining ARPUs on voice and sms as well as margin pressure coming from both the higher end subscribers (as tariffs fall) and from lower end subscribers (as volumes fall in response to higher average tariffs). We expect the full impact to be felt from FY16 since the tariff reduction will only affect 2 months of the FY15 year. We expect voice ARPUs to decline 10% h/h and 20% y/y to $4.72 in FY15 and data ARPUs to decline 8% h/h and grow a more moderate 51% y/y to $1.97 in FY15. We anticipate EcoCash revenue to grow 66% y/y to $55.4mn and revenue from overlay services of $28.3mn. Group revenue is expected to remain relatively flat (-0.2% y/y) at $748.5mn. We expect margins to deteriorate further to 38.5% in FY15 and to remain subdued in the short to medium term due to a high cost base against the tariff reductions and excise duty. We have forecast EBITA of $289.4mn in FY15, down 12.9% from FY14. With interest and depreciation charges expected to remain high, we have forecast net income for FY15 of $91.9mn, 23.0% down from FY14. Whilst our forecasts are based on the premise that the tariff cuts are affected each year, we highlight that the industry is lobbying government to reconsider the current thresholds therefore providing upside potential to our forecasts.

Despite downgrade to our target price we maintain a BUY recommendation

We estimate Econet trades on a P/E (+1) of 7.8x and EV/EBITDA (+1) of 3.6x versus SSA peers trading on P/E (+1) of 10.9x and EV/EBITDA (+1) of 5.5x. Using a combined multiples and DCF valuation method we now reach a target price of $0.61, implying upside of 23% at current levels. We therefore downgrade to a **BUY** recommendation on Econet.

Market Data	
Report Date	02-Feb-15
Rating	BUY
Bloomberg Ticker	ECWH: ZH
Current price $	0.500
Target Price	0.614
Market Cap $mn	820.01
EV $mn	997.94
Market Weight	16.90%
Common Shares Outstanding mn	1640
Freefloat (%)	40%
Average Daily Val. Traded $'000	14.14
Last Dividend declared	1H15
PER (+1)	7.79
EV/EBITDA (+1)	3.58
Dividend Yield	2.58%
ROE	22.2%
Share price performance YTD	-16.7%

12 month share price performance vs Industrial Index



	Revenue	EBITDA	Net Income	EPS ($)	DPS ($)	EBITDA Margin	EV	Net Debt	EV/Sales	EV/EBITDA	P/E	P/Bk	Div yield
2014	752.8	332.2	119.4	0.08	0.01	44.1%	997.9	177.9	1.3	3.0	6.9	1.4	2.6%
2015E	751.2	289.4	105.3	0.06	0.01	38.5%	1,035.4	215.4	1.4	3.6	7.8	1.2	2.6%
2016E	696.2	254.3	72.7	0.04	0.01	36.5%	995.1	175.1	1.4	3.9	11.3	1.1	2.2%
2017E	690.1	248.6	66.8	0.04	0.01	36.0%	950.7	130.6	1.4	3.8	12.3	1.1	2.4%
2018E	736.2	272.2	82.5	0.04	0.02	37.0%	887.8	67.8	1.2	3.3	9.9	1.0	3.0%

Retail

Edgars

Capacity expansion drives revenue growth; softening margins affect profits

Edgars group revenue grew 10.2% h/h to $31.2mn, with significant uplift coming through in the last 2 months (revenue was down 2.5% from the prior year at the end of April 2014), following the civil servant back pay and the launch of the 12 months to pay (MTP) accounts in April 2013. Revenue from the Edgars chain came in at $23.8mn, 7.4% up from the prior period and buoyed by new store openings; 2 new stores were opened in 2H14 and another 2 in 1H15 bringing the total number of stores to 28. Like for like, revenue increased 3% h/h driven by credit sales which constituted 89.9% of total sales (vs 89.4% in 1H14). In April 2014, the Group offered their Edgars chain customers the option to convert to 12 month to pay (12MTP) accounts, from the traditional 6MTP accounts. According to management, the product has been met with vigour and has given a significant boost to sales in the Edgars stores. The Jet stores brought in revenue of $5.6mn, contributing 18.8% to group revenue and up 12.3% h/h. Again, sales growth was underpinned by capacity expansion, with 7 new stores opened since 1H14 (to 25 stores in 1H15). Like for like, revenue was down 18% from the prior period, with sales being negatively affected by price-based competition from the informal sector, unbalanced product assortments and a migration of customers away from cash sales towards credit, offered in the Edgars stores. GP margins tapered down from 45.2% in 1H14 to 44.3% in 1H15, a result of a sub-optimal sales mix in Jet stores and price discounts to boost sales. EBITDA margins also came off significantly, from 5.2% in 1H14 to 3.7% in 1H15; this was largely due to increased debt collection costs which increased 37% h/h. Handovers, as a percentage of credit sales, increased from 1.2% to 1.6%; in absolute terms this represents a significant 44% increase. Provisions for bad debts also increased from 2.0% in 1H14 to 2.3% in 1H15. As a result of softness in margins, EBITDA came in at $1.2mn, down 21.6% from the prior period. Depreciation costs rose 14.1% h/h as a result of increased capex and finance costs grew 3.6% h/h, despite borrowings decreasing in the period. This was a result of increased finance costs, as the Group dipped into short-term borrowing facilities. The effect on bottom line was offset by a 29.7% increase in interest income, a result of increased past dues and the 12MTP facility. Net income came in at $1.05mn, 4.7% down from the prior period. EPS, at 0.41c, was down 8.1% from 1H15. Free cash outflows in the period were $469k, compared to outflows of $49k in 1H14, as cash was tied up in debtors.

Credit sales to drive growth, results in squeeze on margins and cash outflows

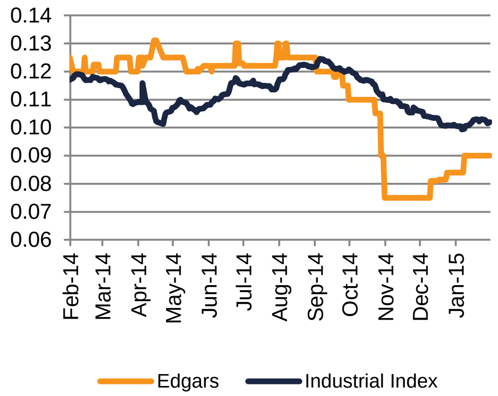
Management have asserted that they are now happy with their footprint and will be taking a much more conservative approach to future capacity expansion. It is highly unlikely that any more stores will be opened in 2H15, therefore the rapid capacity expansion which has been driving sales over the last 3 years, can no longer be relied upon. We do expect to see some sales uplift coming through in the Edgars stores from the 12MTP account offering, and have forecast revenue in the Edgars chain to increase 15.8% y/y to $59.5mn in FY15, of which 91% will be on credit. In the Jet chain, we have forecast revenue of $14.1mn, up 2.0% from the prior year, as only 2 new stores opened y/y (vs 7 new stores on a h/h basis). In both Edgars and Jet stores, we expect sales per square meter to increase in 2H14 on the back of higher civil servant salaries and due to the traditional pickup in sales in 2H. On a group level, we have forecast a 14.9% increase in revenue to $77.6mn. We expect GP margins to remain soft as there is little room to increase prices in the current environment, although management have indicated that the product issues in Jet are being resolved which could offer some margin support. EBITDA margins will remain weak on the back of increased debt collection costs. We have forecast EBITDA of $7.3mn for FY15, 14.0% down from FY14. Management indicated that $6mn debt is required in FY15 to finance the 12MTP account scheme; this along with increased average costs of debt, is expected to drive finance costs up by 16.6%. Consequently, we have forecast a significant 11.9% y/y drop in net income to $3.73mn in FY15. The extended payment terms will also impact negatively on cash flows; we expect free cash outflows of $4.5mn in FY15, compared to inflows of $893k in FY15.

Downgrading our TP

We now estimate Edgars trades on a PER (+1) 6.9x, and EV/EBITDA (+1) 6.2x to 2016E, compared to peers, at PER 15.6x and EV/EBITDA 10.4x. Using a weighted combined multiples valuation method (PER & EV/EBITDA), we have arrived at a target price of 10.76USc for Edgars, implying an upside of 20% at current levels. We therefore upgrade to a **BUY** recommendation on the stock.

Market Data	
Report Date	02-Feb-15
Bloomberg Ticker	EDGARS: ZH
Rating	BUY
Current price $	0.090
Target Price	0.108
Market Cap $mn	26.38
EV $mn	41.99
Market Weight	0.45%
Common Shares Outstanding mn	293
Freefloat (%)	46.00%
Average daily value traded $'000	8.35
Last Dividend declared	N/A
PER (+1)	6.95
EV/EBITDA (+)	6.18
Dividend Yield	0.00%
ROE	14%
Share price performance YTD	-5%

12m share price performance ($) v. Industrial Index



	Total income	EBITDA	Net Income	EPS ($)	DPS ($)	EBITDA Margin	EV	Net Debt	EV/EBITDA	P/E	P/Bk	Div yield
2014	67.6	8.5	4.2	0.015	0.00	12.6%	42.0	15.6	4.9	6.2	1.60	0.00%
2015E	77.6	7.3	3.7	0.013	0.00	9.5%	46.4	20.0	7.1	7.1	1.30	0.00%
2016E	82.0	7.5	3.8	0.013	0.00	9.2%	46.4	20.0	69	6.9	1.10	0.00%
2017E	84.5	7.5	3.9	0.013	0.00	8.9%	46.4	19.0	6.8	6.8	0.94	0.00%
2018E	88.3	7.8	4.4	0.015	0.00	8.9%	42.6	16.2	6.1	6.1	0.82	0.00%

Banking

FBC BANK

Misaligned costs in Turnall impact group earnings

FBCH's 1H14 financials were relatively mixed due to a disappointing performance in the manufacturing subsidiary (Turnall). Total income rose 11.4% h/h to $41mn, driven by a realised increase in insurance business underwritten in the 6 months. Net interest income rose 62.2% h/h to $16mn 1H14 from $9.9mn in 1H13, spurred by higher margins on the micro-finance book and a 17.7% increase in total loan book against prior comparable period. Non-funded income fell 7.2% weighed down by a 32.1% fall in manufacturing revenues ($12.9mn 1H14 v $19.0mn 1H13), this nullified an otherwise strong performance in net earned insurance premium, up 29.4% y/y to $9.3mn. Operating expenses went up a significant 17.9% h/h to $30.8mn on the back of a 65% increase in insurance claims and loss adjustment expense. Excluding impairments, we estimate a cost to income ratio of 75.2% for 1H14 (this differs from 81% reported by the group which includes impairments) up from 71.1% 1H13 and higher than the regional average of around 60%. PBT fell 21.8% (1H14 $7.8mn v $10.0mn 1H13) weighed down by a loss in Turnall (PBT; -$3.5mn 1H14 v $29k 1H13) due to the change in the business model from credit sales to cash sales, coupled with depressed demand. Net Income came in at $6.8mn, 17.5% lower than $8.3mn in 1H13. Total assets grew 6.2% to $489.5mn in 1H14 from $460.8mn in FY13; loans and advances however fell 6.8% to $247.8mn in 1H14 from $265.8mn in FY13, but were up 17.7% against prior comparable period (loans and advances; $210.6mn in 1H13). Loans were concentrated in individuals (30%), manufacturing (19%) and mortgage (11%). NPLs closed 1H14 at a reported $24mn, up from $17.4mn recorded in 1H13 but relatively flat against FY13 levels; the resultant NPL ratio was 9.1% in 1H14 versus 8.6% in FY13. Total provisioning was lower at $9.6mn compared to $10.6mn as at FY13, suggesting a provision ratio of 5.7%. Impairment allowance charged for H1 came in at $2.3mn versus $0.6mn for 1H13. Total deposits rose 8% from $299.7mn in FY13 to $323.6mn in 1H14, above total system deposit growth (4.9% in H1 as reported by the RBZ) but below competitors like CBZ at 9.4%. Deposits were concentrated in financial services (49%), individuals (12%) and wholesale and retail trade (10%). The bank's loan to deposit ratio closed the period at 77%, lower than FY13 at 89%, but higher than 71% as at 1H13. The Group's capital adequacy ratio came in at 17.67% as at 1H14 above the statutory requirement of 12%. A decision was made to divest from the manufacturing business resulting in a dividend in specie being issued at a rate of 0.39 ordinary shares in Turnall for every 1 ordinary share held in FBCH. The decision was intended to align the investments of the Group with its primary financially focussed business interests in commercial banking, mortgage finance, non-life insurance and stock-broking.

Focusing on asset quality, streamlining operating costs through technology

FBC's strategy going into 2H14 involves focusing on asset quality, with signs of a more conservative approach to lending coming through in 1H14 (7% contraction in loan book). The Bank and Building society clients have migrated to electronic channels which now drive the bulk of transactions, this is intended to lower operating costs, extend convenience to customers and create additional revenue opportunities. Management highlighted that the main contributor to non-performing assets was the micro-finance book yielding an NPL ratio of 14.55%, however this was compensated by more aggressive interest income yields on this book (contributed 23% to group PBT). Given the current environment and our expectation of embedded risk we expect the NPL ratio to rise to 9.5% in FY14 (from 8.6% in FY13) and thereafter begin to moderate. The building society released a total of 69 housing units in 1H14 and continues to develop and offload units to mortgage clients; therefore we expect this to drive the loan book up by 10% in FY14 from current levels. We expect a deposit growth of 20.8% from current levels on the back of a $60mn loan facility arranged by Afreximbank finalised in 2H. We also expect material reduction in cost of funding associated with that. On the insurance side, the group is looking to increase collectable premiums written and maintain strong underwriting discipline. Turnall's operating costs contributed an average of 15% the group's total costs, and we expect some cost savings to start filtering in 2H. We estimate FY13 NIM to have been 8.8%, but we expect it to fall to 7.9% in FY14 and continue softening thereafter. We forecast ROE to decline to 8.8% from 17.2% in FY13, as a result of the adjustment for the deconsolidation of Turnall that will be made by FBC. This will be done by putting through an amount of $6.8mn in the income statement as the negative adjustment in NAV resulting in the net income falling to $7.9mn.

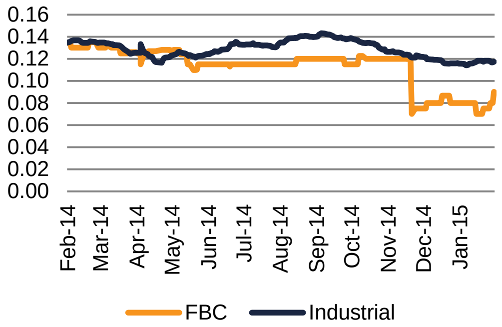
Valuation

We expect net income in FY14 to be $7.94mn, 43.6% lower than FY13. Given the constraint in profitability this year and the issue of a scrip dividend related to Turnall, we expect FBC to issue out a subdued cash dividend to shareholders. We estimate FBC trades on a P/BV (+1) of 0.72x and P/E (+1) of 5.00x versus regional peers at P/BV 1.71x and P/E 8.47x for 2015E. We rate the group trades at a premium to our Zimbabwe banking universe. Using a combined static ROE & DDM model we have arrived at a target price of $0.09 for FBC, implying an upside of 3.71% to our target and initiate on the counter with a **HOLD** recommendation.

Market Data

Report Date	02-Feb-15
Bloomberg Ticker	(FBCH: ZH)
Rating	HOLD
Current price $	0.090
Target Price $	0.093
Market Cap $mn	60.48
EV $mn	N/A
Market Weight	1.28%
Common Shares Outstanding mn	671.95
Freefloat %	47.13%
Average Daily Value Traded $000's	17.61
Last Dividend declared	FY13
Dividend Yield	1.31%
PER (+1)	5.00
PBV (+1)	0.72
Share price performance YTD	13%

12m share price performance ($) v. Ind. Index



	Total Income ($mn)	Net Income ($mn)	EPS ($)	DPS ($)	BVPS ($)	P/E	P/BV	Div Yield (%)	ROAA	ROAE
2013	79.50	14.1	0.021	0.003	0.16	4.29	0.57	3.4%	3.3%	17.2%
2014E	74.83	7.9	0.012	0.001	0.13	7.61	0.69	1.3%	1.6%	8.8%
2015E	76.72	12.1	0.018	0.003	0.12	5.00	0.72	3.0%	2.2%	14.2%
2016E	81.44	13.2	0.020	0.004	0.14	4.60	0.64	4.4%	2.2%	14.8%
2017E	87.49	14.8	0.022	0.006	0.16	4.07	0.58	6.1%	2.2%	14.9%

Agro-Industrial

Hippo Valley Estates Limited

A strong recovery staged in 1H15, stemming from Government intervention

Following Government intervention to curtail cheap imports which were flooding the local market, which came into effect in January this year, Hippo Valley has staged a firm recovery in 1H15 on the back of substantial improvements in domestic market sales. As expected, total cane deliveries to the mill declined (-8.2% h/h) due to a delayed start to the milling season and the cessation of deliveries from Green Fuel. Consequently, sugar production for 1H15 amounted to 167,425 tonnes, 6.4% below the 178,946 tonnes produced in 1H14. Production efficiencies were improved however, with the cane-to-sugar ratio falling from the 7.87 achieved in 1H14 to 7.72 in 1H15. In the period, 133,486 tonnes of sugar was sold to domestic and export markets, up 57.1% from the 84,990 tonnes sold in 1H14. Growth in revenue was dampened by depressed sugar prices, due to lower international sugar prices, especially on exports to the EU; the average selling price of $618 achieved in 1H15 was 18.7% lower than average prices achieved in 1H14. Still, revenue grew a healthy 27.7% h/h to $82.53mn in 1H15, in line with our expectations. EBITDA margins fell 160bps from 27.3% in 1H14 to 25.7% in 1H15, reflecting the decline in sugar prices combined with an increase in input prices. EBITDA of $21.17mn was realised in 1H15, up 20.3% h/h. A lower depreciation charge (-9.9% h/h) resulted in operating profits increasing 38.4% h/h to $15.21mn. Net finance charges also declined in the period, coming in 13.0% lower than in the prior period, due to a 29.2% fall in net debt in response to improved cash inflows, achieved through cost cutting measures implemented over the period and the high stocks at this time of the production cycle. As a result, net income increased a significant 58.0% h/h, from $5.66mn in 1H14 to $8.94mn in 1H15. This translated to EPS of USc4.7. No interim dividend was declared.

Lower production and moderate earnings growth expected for FY15

The Zimbabwe sugar industry is expecting a decrease in sugar production to between 440,000 tonnes and 475,000 tonnes for FY15, compared to 488,000 tonnes in FY14. We expect Hippo Valley to produce 235,427 tonnes of sugar in FY15 from 1.82mn tonnes of cane deliveries, based on the assumption that industry production will be upper-range and Hippo Valley will retain its 51% share of the market. With sugar prices expected to remain depressed in the 2014/15 selling season, we have forecast revenue of $146.43mn for FY15 (+7.6% y/y), off total sugar sales of 236,446 tonnes (+13.1% y/y). We have adjusted our initial sales volumes forecast upward by 5% as Hippo has regained market share faster than expected. We expect sales to be subdued in 2H15 due to depressed consumer spend experienced system-wide in the domestic market. We anticipate EBITDA margins to remain fairly subdued in FY15 at 21.6%, compared to 22.0% in FY14 as a result of continued depressed sugar prices and higher input costs, partly offset by on-going cost cutting initiatives as management attempts to counter the effects of lower sugar prices. The resultant EBITDA projection for FY15 is $31.67mn.We forecast a slight up-tick in operating margins in FY15 to 14.3% (14.0% in FY14), on account of the lower depreciation charge. We have forecast net income for FY15 of $10.38mn, up 15.5% y/y. We expect production to improve in FY16 due to the improved irrigation supply and more favourable weather conditions experienced last season, which in turn is expected to improved cane yields and sucrose content in the cane.

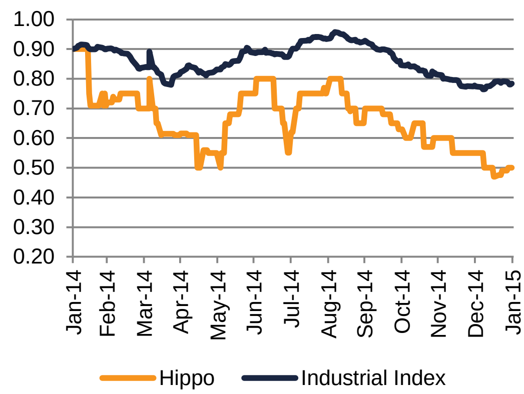
We maintain our BUY recommendation

Based on our adjusted forecasts, we now estimate Hippo Valley trades on a P/E (+1) of 9.3x and an EV/EBITDA (+1) of 3.6x, placing the stock at a significant discount to comparable sugar companies, at P/E 16.4x and EV/EBITDA 6.4x for 2015E. Using a weighted combined multiples valuation method (P/E and EV/EBITDA) and applying a 10% discount, we have arrived at a 12 month target price for Hippo Valley of **$0.84**, implying upside of 68%. We believe that the stock has been over punished by the market and rate the counter an attractive **BUY** at current levels.

Market Data

Report Date	02-Feb-2015
Bloomberg Ticker	HIPPO: ZH
Rating	BUY
Current Price $	0.50
Target Price $	0.84
Market Cap $mn	97
EV $mn	128
Market Weight	2.0%
Common Shares Outstanding mn	193
Freefloat	20.6%
Average Daily Value Traded $000's	5.33
Last Dividend declared	31.12.04
P/E (+1)	9.3
EV/EBITDA (+1)	3.6
Share price performance YTD	-9.1%

12m share price performance ($) v. Industrial Index



	Total income	EBITDA	Net Income	EPS ($)	DPS ($)	Operating Margin	EV	Net Debt	EV/Sales	EV/EBITDA	P/E	P/Bk	Div yield
2014	136.1	30.0	9.0	0.05	0.00	14.0%	128.0	31.5	0.9	4.3	10.7	0.4	0.0%
2015E	146.4	31.7	10.4	0.05	0.00	14.3%	112.5	16.0	0.8	3.6	9.3	0.4	0.0%
2016E	161.6	35.0	14.1	0.07	0.00	15.3%	94.9	-1.6	0.6	2.7	6.9	0.4	0.0%
2017E	166.1	35.9	16.8	0.09	0.00	15.7%	72.3	-24.2	0.4	2.0	5.7	0.4	0.0%
2018E	179.3	38.8	20.6	0.11	0.00	16.3%	48.1	-48.4	0.3	1.2	4.7	0.3	0.0%

Innscor Africa

Cost misalignment continues to impact performance

Innscor's FY14 financials reflected the fully consolidated results for former associate companies National Foods and Irvines; this note will focus on the adjusted numbers for comparative purposes. The group reported FY14 revenue of $1.01bn, 3% up y/y and fairly in line with our forecast of $1.03bn. EBITDA came in at $83.58mn for FY14 down 15% y/y and about 5% ahead of our forecast of $79.6mn. The group put through a fair value gain of $39.03mn linked to the consolidation of Natfoods and Irvines to arrive at a PBT of $92.4mn; however once adjusted PBT came in at $56.76mn, 26% lower y/y. An adjusted PAT of $42.64mn was recorded for FY14, whilst this was 30% lower than prior comparable period it outperformed our forecast of $31.1mn. Headline EPS at USc4.12 was 35% down on prior year; the board did however declare a final dividend of USc0.70 bringing the total dividend for the year to USc1.30. Main highlights within silos, Milling and Protein saw 9% y/y revenue growth to $421.2mn (48% of group revenue), EBITDA rose 20% y/y to $43.1mn (53% of group EBITDA). National Foods led growth in this silo, with revenue rising 11% to $343.5mn and EBITDA rising 22% to $24.9mn; performance was spurred by the maize milling business that saw 19% growth in volumes against a well-priced pipe-line of raw material. Bakeries & Fast Foods revenue fell 4% y/y to $262mn whilst EBITDA fell 24% y/y to $25.2mn for FY14. Notably bread volumes were down 10% y/y against lower demand and some loss of market share to competition. Spar revenue fell 4% y/y to $159.7mn and recorded a loss at operating level of $4.91mn, notably average spend per customer fell 21% from $10.78 in FY13 to $8.53 in FY14. Innscor maintained its strong cash generative abilities achieving operating cash-flows of $106.8mn in FY14, this enabled the company to maintain its expansion program both locally and abroad. CAPEX was recorded at $48.93mn with the bulk ($13.5mn) going towards bakeries. Net borrowings were conservative at $26.95mn (net gearing ratio of 9.86%) with management stating that local borrowings were at an average cost of around 8%.

Theme remains adapting the business model, correcting internal efficiencies

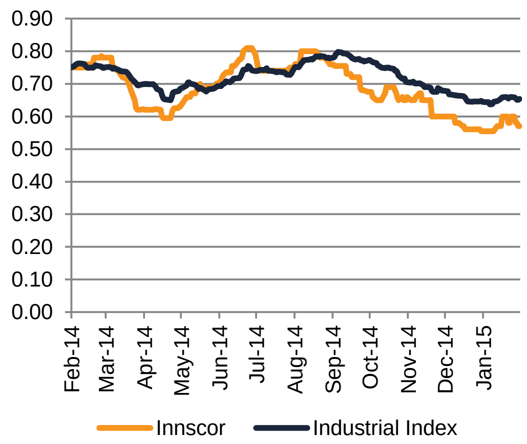
Strong performances from National Foods and Colcom enabled the group to defend the top-line. However various initiatives to address the internal cost structures of the business have yet to significantly impact margin development, particularly in the face of stronger competitive headwinds. Previous flagship silo Fast Foods and Bakeries saw a 24% drop in EBITDA; with Fast Foods incurring high 'above site' costs and Bakeries still weighed down by high fixed costs relative to throughput volumes given excess installed capacity. The group intends to consolidate the management structure of Fast Foods in which there were previously 3 regional head offices into 1 head office. Counters that are loss making or rated as having low chances of survival will be closed down, in addition there will be some movement to sites with cheaper rentals. Staff numbers will be reduced in Bakeries, bread and pie distribution will be combined to improve fleet capacity utilization. The performance of Spar remained poor in FY14, particularly at operating level, worsened by fixed asset impairments of $1.26mn related to 2 large store closures. Management re-stated plans to right-size stores and restructure Spar DC, our opinion is that this is clearly the most vulnerable area of the group's business portfolio particularly given competition and consumer income dynamics in this space; going into FY15 we anticipate continued decline in the top-line and a sustained loss at operating level despite a strong Zambian business. The group's internal focus remains to evolve from a decentralized structure with autonomous managers, to a more centralized structure by product group ensuring focused decision making, reduced duplication of roles and improved capital discipline and allocation. In our view FY15 will be a critical year for Innscor as the market looks for demonstrable profitability as a result of these initiatives.

Moderate margin recovery in FY15

Innscor's FY14 earnings performance was affected by $7.2mn in once-off costs and restructure provisions. Therefore we do expect some margin uplift in FY15 earnings, however in our view this will not be pronounced given sustained earnings deterioration in the business portfolios and the spectre of fixed producer prices for grains that will potentially affect margin performance in Natfoods, Colcom and Irvines. We forecast 2.4% revenue growth y/y to $1,035mn in FY15 and marginal EBITDA uplift from 8% in FY14 to around 8.3% in FY15. Given the recent consolidations of Natfoods and Irvines we now use an SOTP to value Innscor and arrive at a 12 month target price of US$0.85 implying upside of 49%. We believe the stock price has been over sold at current levels & upgrade Innscor to a **BUY.**

Market Data	
Report Date	02-Feb-2015
Bloomberg Ticker	INAF: ZH
Rating	BUY
Current price $	$0.57
Target price $	$0.85
Market Cap $mn	308
EV $mn	320
Market Weight	6.44%
Common Shares Outstanding mn	540.12
Freefloat %	56%
Average Daily Val. Traded $000's	134
Last Dividend declared	FY14
Dividend Yield	2.30%
PER (+1)	9.4
EV/EBITDA (+1)	3.9
Share price performance YTD	-18%

12m share price performance ($) v. Industrial Index



	Revenue	EBITDA	Net Income	EPS ($)	DPS ($)	EBITDA Margin	EV	Net Debt	EV/Sales	EV/CF	EV/EBITDA	P/E	P/CE	P/Bk	Div yield
2014	1,010.9	80.6	60.5	0.112	0.013	8.0%	334.8	27.0	0.3	2.3	4.2	5.1	3.7	1.5	2.3%
2015E	1,035.4	85.7	32.8	0.061	0.012	8.3%	336.8	29.0	0.3	2.6	3.9	9.4	5.3	1.1	2.1%
2016E	1,069.1	90.6	34.1	0.063	0.013	8.5%	337.7	29.9	0.3	2.5	3.7	9.0	5.0	1.0	2.2%
2017E	1,105.3	96.5	36.1	0.067	0.013	8.7%	335.9	28.1	0.3	2.4	3.5	8.5	4.7	0.9	2.3%
2018E	1,146.2	102.0	38.0	0.070	0.014	8.9%	341.7	33.8	0.3	2.5	3.4	8.1	4.4	0.9	2.5%

FMCG

National Foods

Efficient working capital management lifts performance

National Foods' FY14 financials surpassed expectations showing both top-line growth and margin upliftment in a difficult consumer environment. The company reported FY14 revenue of $343.5mn, 11% higher than prior comparable period and 8% ahead of our forecast of $319mn. There was a significant improvement in earnings with EBITDA rising to $24.9mn, 22% higher y/y and notably ahead of our forecast of $17.2mn. Net income for the company came in at $16.78mn, 20% higher y/y and again ahead of our forecast of $10.4mn. A non-recurring profit of $1.5mn was recorded during the year arising from the disposal of property assets. Basic EPS of USc24.54 was achieved in FY14 v USc20.38 achieved in FY13; the board declared a final dividend of USc5.18 bringing the total dividend for the year up to USc8.18. Due to the deficit in locally grown maize, wheat and soya, National Foods maintains long future priced pipelines of imported raw materials which can affect margin in times of commodity price volatility; in FY14 the maize pipeline was well priced leading to some growth in gross margin. The group showed efficient working capital management successfully mixing trade and bank funding to end FY14 with a cash surplus of $4.2mn; the company now has no gearing and is positioned to self-fund its growth in FY15. Volumes were 8% higher y/y to close FY14 at 538k tons (6% ahead of our forecast of 508k tons). This was mainly driven by 19% y/y volumes growth in Maize Milling combined with a 4% increase in average realisation per ton. The Flour Milling business experienced 2% volumes growth, however a lower average realisation per ton for wheat resulted in a 1% decrease in revenue; profitability fell 13% y/y as margin was sacrificed to hold volumes against flour imports. Despite losing market share in the Stock-feeds business, 6% y/y sales volumes growth was achieved, 3% revenue growth was realised but profitability remained flat. Under FMCG volumes sold in mainstream products improved 22% y/y, with margins improving from 21% in FY13 to 24% in FY14, this however remains a marginal part of the business.

Investments bode well for volumes, external margin development threat

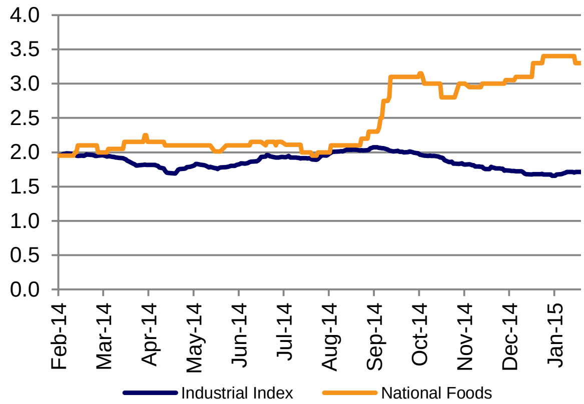
National Foods invested $3.6mn in capex for FY14 in various projects (down from $6.1mn in FY13), however a total of $7.2mn is budgeted for FY15. Given that the funding mix of this capex will be largely drawn from internal resources as opposed to debt, we anticipate a lower cash surplus in FY15 and therefore a lower dividend yield y/y. We only expect a marginal uptick in gearing. We have some concern around a Government SI stipulating minimum producer prices for grains including a fixed purchase price of $390 per ton for maize. Whilst we await to see whether this will be successfully implemented, we do as a result anticipate upward pressure on average raw material cost, compressing margin in FY15 relative to FY14. We believe that any subsequent attempt to pass cost onto a more price sensitive consumer will face notable resistance. In a positive signal for volumes, a total of 8 new depots were opened during FY14, with 20 depots now connected on 'real time basis' to a central processing system; we anticipate that this will see wider distribution of product in FY15 to meet localised demand in different locations. In Flour Milling, work to upgrade mills has begun, after which improved efficiencies are expected to be achieved in the next 3 years. Sufficient wheat has been purchased both in terms of quality and cost for throughput in the mills going forward. Some investment has been made into a contract farming out-grower scheme to secure local throughput into the business in maize and wheat, however the supply-side contribution of this scheme will remain limited in the short to medium term. A non-recurring profit of $1.5mn lifted earnings in FY14 from the sale of properties held, whilst the group will continue to unwind its property portfolio going forward, we have conservatively excluded any assumptions around that in our forecasts. We believe National Foods is well placed to invest in new categories that can leverage off an existing admin and distribution network to positively impact earnings in the short to medium term. In addition we see room for growth in the FMCG business where market shares remain relatively lower (20-40%) leveraging the same platform.

Valuation

We estimate that National Foods currently trades at a P/E (+1) of 14.30 to FY16E, compared to regional peers at 16.3x. The counter trades at an EV/EBITDA (+1) of 9.42x to FY16E compared to peers at 12.2x. Placing a 15% discount on the stock, we still arrive at a 12m target price of $3.87 implying upside of 13.7% at current levels. We now rate National Foods as a **HOLD** at current levels.

Market Data	
Report Date	02-Feb-15
Bloomberg Ticker	NAFH: ZH
Rating	HOLD
Current price $	3.40
Target Price	3.87
Market Cap $mn	232.56
EV $mn	249.02
Market Weight	5%
Common Shares Outstanding mn	68.40
Freefloat (%)	14.88%
Average daily value traded $'000	9.4
Last Dividend declared	FY14
PER (+1)	14.30
EV/EBITDA (+1)	9.42
Dividend Yield (+1)	2.41%
Share price performance YTD	38%

12 Month Share Price performance v. Industrial Index



	Revenue ($mn)	EBITDA ($mn)	Net Income ($mn)	EPS ($)	DPS ($)	EBITDA Margin	EV	Net Debt	EV/Sales	EV/EBITDA	P/E	P/Bk
2014	343.5	24.9	16.8	0.245	0.08	7.2%	228.3	-4.2	0.7	9.2	13.9	3.16
2015E	352.0	24.6	16.3	0.238	0.06	7.0%	232.1	-0.4	0.7	9.4	14.3	2.71
2016E	367.2	25.3	16.5	0.241	0.07	6.9%	233.6	1.1	0.6	9.2	14.1	2.37
2017E	381.4	25.9	16.8	0.246	0.07	6.8%	233.9	1.4	0.6	9.0	13.8	2.11
2018E	394.9	26.9	17.5	0.255	0.07	6.8%	235.2	2.6	0.6	8.8	13.3	1.89

NMB

Increased caution on lending, slower deposit growth

NMB returned to profitability in 1H14, despite a more cautious approach to the loan book and slower deposit growth. Core capital grew 3.2% to $44.8mn in 1H14 from $43.4mn in FY13 lifted by the increase in retained earnings. Total income came in at $16.8mn for 1H14, 9% lower h/h than $18.5mn achieved in 1H13. This was weighed down by net interest income down 10% h/h to $8.53mn for 1H14 and non-funded income down 8% h/h to $8.27mn for same period. Notably fee & commission income declined 10% h/h as the legacy effect of controlled fees from the MOU continued to impact customer charges. Operating expenditure rose 2% h/h to $13.35mn in 1H14 from $13.03mn in 1H13 driven by a 4% h/h increase in staff costs to $6.09mn for the period. The bank's resultant cost to income ratio came in at 82% for 1H14, significantly higher than 67% achieved at FY13 but similar to 81% for same prior comparable period (1H13). This is still notably higher than the regional average cost to income ratio of around 60%. The bank's impairment charge for 1H14 was $1.58mn, 16% lower h/h than $1.89mn for 1H13; the decrease was driven by increased security obtained on exposures. Gross NPLs were recorded at $38.74mn for 1H14, relatively flat against $38.73mn as at FY13, with the implied NPL ratio similarly remaining flat at 20% (against a reported industry average of approx. 18%). Total assets grew by 1.74% to $264mn in 1H14 from $259.48mn in FY13; loans and advances rose 1% to $179.13mn in 1H14 from $177.74mn in FY13 but were marginally down 1% against prior comparable period (loans & advances, $181.32mn 1H13). Loans were concentrated in distribution and individuals at 24% of book each. Total deposits rose 2% to $219.17mn in 1H14 from $215.43mn, fairly in line with total system deposit growth but behind local competitors. Same deposits were marginally up 1% h/h from $216.04mn in 1H13 and concentrated in banks & financial services at 22%. The bank's implied loan to deposit ratio for 1H14 came in at 81.7%, lower than 87% reported for prior comparable period. The bank's liquidity ratio closed the period at 35.6%, suitably above the statutory requirement of 30%; the capital adequacy ratio was reported at 17.44%, again suitably above the statutory requirement of 12%. The bank passed up on declaring a dividend for 1H14 in view of the need to retain cash in the business and to strengthen the statutory capital requirements for the banking subsidiary.

Focus remains on reducing NPLs whilst pursuing external credit lines

Given limited management guidance as at 1H14 on the bank's outlook, we expect that the core strategy will remain the same. There is a clear concerted effort within the bank to clean up the existing loan book, which has been demonstrated through aggressive impairments (FY13; $16.7mn vs FY12; $3.9mn). We expect to see some continuance in impairment losses coming through in H2, given that the bank's NPL ratio still remains high at around 20%; however write-downs will be lower than FY13 leading to some recovery in ROEs. In the medium term, we believe that plans announced by the RBZ for a new SPV (ZAMCO) to acquire non-performing assets in the banking sector bode well for the majority of banks including NMB; with sectoral NPLS estimated at approx. 20%. We expect the bank to remain cautious on the lending front and forecast net loans to rise just 4.7% y/y to FY14. We forecast that interest income will decline about 3.8% y/y to FY14, against some downward pressure on lending rates, impacting NIMs. We estimate the bank's NIM to have been around 11.7% in FY13 (relatively higher than established peers) and forecast that this spread will trend towards 8.9% in FY14. We do expect the bank to continue to pursue external lines of credit in order to underwrite more reasonably priced lending business to clients at longer tenure; we estimate average cost of funds to be sitting around 6.4% at present.

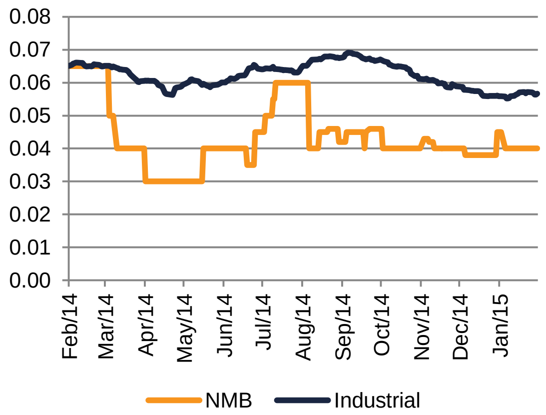
Improved valuation on recovery in RoEs

With the bank, in our view, having mostly cleaned up the book in FY13 following the investment of the 3 new strategic investors; we anticipate a recovery in net income to $2.71mn in FY14 (vs. loss of $3.32mn FY13), against lower impairments in this year. Whilst NIMs will begin to moderate for the bank, we foresee ROEs beginning to stabilise in the short to medium term, thus improving valuations. With the $100mn core capital requirement shifted to 2020, we do expect the bank to start paying a small dividend in FY15. We estimate NMB trades on PER (+1) 3.06x to 2015E versus peers at 8.47x to 2015E. We estimate NMB trades on P/BV 0.30x to 2015E versus peers at 1.71x. Using a blended DDM and static ROE valuation method, we arrive at a revised 12m target price of USD0.067, implying upside of 66% at current levels. We therefore now reiterate our **BUY** rating on NMBZ.

Market Data

Report Date	02-Feb-15
Bloomberg Ticker	NMBZ: ZH
Rating	BUY
Current price $	$0.040
Target price $	$0.067
Market Cap $mn	15.38
EV $mn	N/A
Market Weight	0.33%
Common Shares Outstanding mn	384
Freefloat (%)	29.43%
Average Daily Val. Traded $000's	1.39
Last Dividend declared	N/A
Dividend Yield	0%
PER (+1)	3.06
PBV (+1)	0.30
Share price performance YTD	-11%

12m share price performance ($) v. Industrial Index



	Total Income ($mn)	Net Income ($mn)	EPS ($)	DPS ($)	BVPS ($)	P/E	P/BV	Div Yield (%)	RoAA	RoAE
2013	37.7	(3.32)	(0.01)	0.00	0.11	(4.64)	0.35	0.0%	-1.4%	-8.9%
2014E	36.4	2.71	0.01	0.00	0.12	5.67	0.33	0.0%	1.0%	6.1%
2015E	40.8	5.02	0.01	0.00	0.13	3.06	0.30	1.6%	1.7%	10.3%
2016E	43.8	6.97	0.02	0.00	0.15	2.21	0.27	3.6%	2.1%	12.9%
2017E	47.3	7.91	0.02	0.00	0.17	1.94	0.24	5.1%	2.1%	13.0%

Retail

OK Zimbabwe

Decline in revenue and profitability reflecting subdued demand

OK Zimbabwe's 1H15 results continue to reflect the depressed state of consumer activity in Zimbabwe. Revenue declined 4.8% h/h to $232.1mn in 1H15, weighed down by depressed demand whereby negative sales were recorded in most businesses, as well as continued deflationary pressures (internal y/y inflation rate -5.6%). Through efficient procurement and an improved sales mix, buoyed by higher margins in the newly-established in-store bakeries, GP margins improved 120bps from 16.8% in 1H14 to 18.0% in 1H15. Overheads ex. depreciation increased 3.0% h/h due to increased advertising and promotional activity, more use of the DC to distribute centrally-received imports and higher security and utility costs. Consequently, EBITDA margins grew a more moderate 20bps in the period, to 3.9% and EBITDA realised in 1H15 of $9.12mn, was almost flat at 1H14 levels (+0.1% h/h). Depreciation charges grew 24.2% h/h as new equipment was installed in the refurbished branches and 4 new stores were opened in 2H14. As a result, operating profits fell 9.3% h/h to $5.94mn in 1H15. Net income declined 10.9% h/h to $4.31mn, weighed down further by increased finance charges. Operating cash flows registered a significant improvement with $8.79mn in operating cash flows compared to $6.8mn in 1H14. With no new stores opened in the 6 month period, additions to PP&E was significantly lower than in 1H14 (-64% h/h). Free Cash Flows therefore stood at $3.3mn for the half year (vs $0.6mn in 1H14). An interim dividend of USc0.19 per share was declared.

Downward revision of revenue and EBITDA margin forecasts

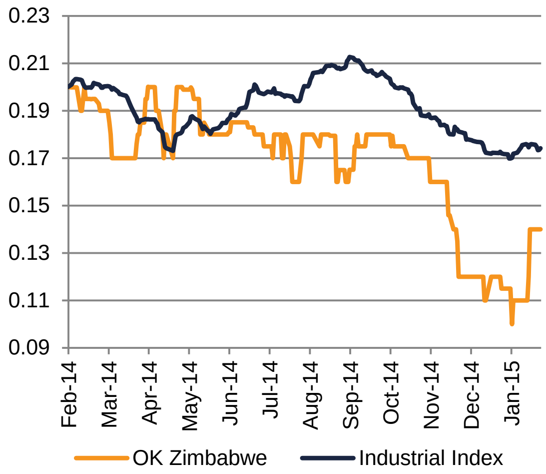
With no apparent near-term catalysts to change, we expect FY15 revenue to remain depressed. Moderate capacity expansion, through the opening of one new store in 2H15, as well as a slight improvement in sales over the festive season is expected to give some support to revenue in 2H15. Still, we expect revenue to come in lower than the prior year and have forecast a decline of 3.4% y/y to $467.35mn in FY15, 5.6% below our initial forecasts. Given the proven success of improved procurement efficiencies as well as margin uplift from the in-store bakeries and financial services business, we have revised our FY15 GP margin forecasts upward from 17.1% to 17.5%. This is a more moderate increase y/y (up 50bps) than on a h/h basis (up 120bps) because we believe the plethora of taxes levied on imported goods, most of which came into effect on 1st October, will put some drag on margins in 2H15. We also expect operating expenses to remain high in 2H15 on sustained high marketing and promotional activity as the retail sector is becoming increasingly competitive, with 3 new entrants: Choppies, Meikles Mega stores & expansion of wholesaling business by N Richards & Metro Peech, coming into OK Zimbabwe's market space. In light of this, we have forecast OK Zimbabwe's EBITDA margins to taper off from 3.9% in FY14 to 3.7% in FY15, compared to our initial EBITDA margin forecasts of 4.2% and 20bps below the EBITDA margins achieved in 1H15; our forecast EBITDA for FY15 is $17.46mn, down 8.3% y/y and 15.0% below our initial forecasts. With depreciation expected to increase 14.4% y/y, we anticipate net income to decline 17.0% y/y to $8.04mn

Subdued earnings performance lead to a HOLD recommendation

We estimate OK trades on PER (+1) 20.4x, and EV/EBITDA (+1) 8.7x, at a significant discount to peers, at PER 18.2x and EV/EBITDA 11.0x. Using a weighted combined multiples valuation method (PER & EV/EBITDA) combined with a DCF valuation (WACC 12.9%), we have arrived at a target price of $0.137 for OK, implying a downside of 1.9% at current levels and place a **HOLD** recommendation on the stock at current levels.

Market Data	
Report Date	02-Feb-15
Bloomberg Ticker	OKZIMBAB: ZH
Rating	HOLD
Current price $	0.140
Target Price	0.137
Market Cap $mn	163.79
EV $mn	154.81
Market Weight	3.47%
Common Shares Outstanding bn	1,170
Freefloat	36.00%
Average daily value traded $'000	50.20
Last Dividend declared	1H15
PER (+1)	20.38
EV/EBITDA (+)	8.71
Dividend Yield	3.00%
ROE	16%
Share price performance YTD	22%

12 month share price performance v. Industrial Index



	Total income	EBITDA	Net Income	EPS ($)	DPS ($)	EBITDA Margin	EV	Net Debt	EV/Sales	EV/EBITDA	P/E	P/Bk	Div yield
2014	483.7	19.0	9.7	0.008	0.00	3.9%	154.8	-9.0	0.3	8.1	16.91	2.45	3.0%
2015E	467.3	17.5	8.0	0.007	0.00	3.7%	152.1	-11.6	0.3	8.7	20.38	2.31	2.5%
2016E	461.2	16.8	7.6	0.007	0.00	3.6%	149.5	-14.3	0.3	8.9	21.53	2.19	2.3%
2017E	482.5	17.5	8.1	0.007	0.00	3.6%	148.1	-15.7	0.3	8.4	20.19	2.08	2.4%
2018E	504.7	18.4	8.7	0.007	0.00	3.6%	143.9	-19.9	0.3	7.8	18.90	1.97	2.6%

Agro-Industrial

Seedco

Margin uplift in 1H15, following income statement 'clean up' in FY14

Despite a contraction in revenue, Seedco's results for the six months ended 30 September 2014 reflect a significant improvement in profitability, as was expected, following the Income Statement 'clean up' which took place in FY14, which entailed various stock write-downs and provisions. Revenue declined 6.1% h/h to $16.04mn in 1H15, weighed down by subdued winter cereals sales, which were 25% lower than the prior period, partly offset by a 6% h/h increase in early maize seed sales. GP margins improved significantly, from 39% in 1H14 to 50% in 1H15, in the absence of the stock write downs which characterised 1H13 as well as price increases across most of the Group's markets. Operating expenses, at $12.4mn, were down 17.0% h/h, as a $3.1mn impairment of a deposit receivable from Interfin bank, which is under curatorship, was included in the 1H13 operating expenses. As such, the operating loss was reduced by 46.9% h/h to $$4.29mn; note the Group generates most of its revenue and profits in their 2H. Finances charges were $2.02mn for the period, 45.9% below the finance charges of $3.72mn incurred in 1H14, a result of efforts to reduce all US$ borrowing to below 9%, intensified debt collection as well as the positive effects of the $13.2mn cash injection from Limagrain which took place in 2H14. A $1.33mn loss for the period was recorded for the discontinued cotton operations, versus a $1.58mn loss recorded in 1H14. The resultant net loss for the period was $7.63mn, a 40.4% improvement to the $12.8mn loss realised in the prior period. Consequently, net operating cash flows improved from a $17.03mn outflow in 1H14 to a $10.85mn outflow in 1H15; bearing in mind over this period the Group is taking up stocks, maize seed intake for the period was almost 26,000MT (vs 22,100MT in 1H13). Due to the seasonal nature of the business, no interim dividend was declared.

We expect a significant jump in profitability in FY2015 on improved margins

In the absence of a government input programme in Zimbabwe, and severe shortages of funding, we anticipate a significant decline in Zimbabwe maize seed sales in FY15 (-23% y/y). Cotton seed sales are expected to remain depressed (-10% y/y) as global prices are at a 5-year low and the local industry remains in jeopardy, with more industry players pulling out this year. The local soya crop is however, expected to improve in the upcoming season on the back of strong producer prices realised in the 2013/14 season; we have forecast a 6% y/y increase in soya sales. With Zimbabwe's contribution to total seed sales now less than 30%, we remain confident that regional sales growth will offset the decline in Zimbabwe seed sales. We have forecast total seed sales of 63,051MT in FY15, up 1.6% y/y and 2% below our initial forecasts. On the back of higher seed prices across most of Seedco's markets, we anticipate revenue of $124.51mn, 3.6% higher than the prior year and in line with our earlier forecasts. On the back of fewer stock write-downs and higher prices, we anticipate GP margins of 49.2% in FY15, above our initial forecasts if 44.2% and 450bps higher than GP margins obtained in FY14. In the absence of the $3.1mn impairment on the Interfin deposit and a $2mn provision for slow moving debts which was realised in FY13, we expect significant uplift in EBITDA. We have forecast EBITDA margins of 21.6% (vs 18.6% in FY14 and 100bps above our initial forecasts), to translate to EBITDA of $26.93mn in FY15, 20.3% up from the prior year. With the second tranche of capital from Limagrain of $26.6mn, expected to come in next month, to be used in part to retire debt, we expect a further reduction in finance costs. We have forecast finance charges to decline 41.5% y/y to $4.65mn, off a 57.3% reduction in debt levels. We forecast net income of $18.75mn in FY15, a significant 58.4% improvement from net income of $11.83mn realised in FY14 and 7.2% above our previous forecasts. We also anticipate a 39.4% y/y improvement in operating cash inflows. Seedco has been issued with TBs for $23.9mn as part payment for the debt outstanding by Zimbabwean Government; these carry a coupon rate of 5% and a tenure of 3 – 5 years. The remaining $10mn outstanding is to be settled through tax offsets.

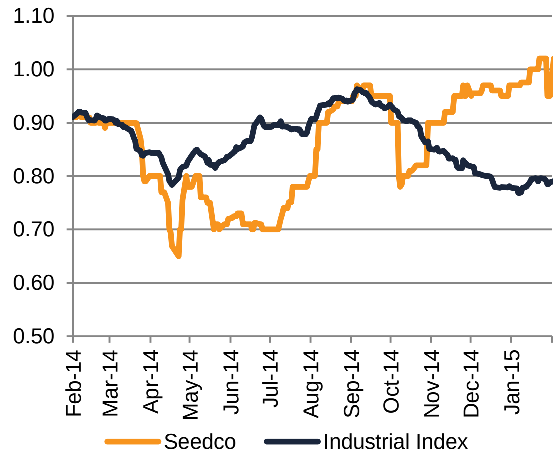
Neutral valuation at current levels

We estimate Seedco trades on PER (+1) 12.8x, and EV/EBITDA (+1) 9.6x to 2015E, at a discount to peers, at PER 16.5x and EV/EBITDA 10.3x for 2015E. Using a weighted combined multiples valuation method (PER & EV/EBITDA) and a 10% discount, we have arrived at a target price of $0.98 for Seedco, implying a downside of 4.1% at current levels and placing a **HOLD** recommendation on the stock.

Market Data

Report Date	02-Feb-15
Rating	HOLD
Bloomberg Ticker	SEEDCO: ZH
Current price $	1.02
Target Price	0.98
Market Cap $mn	239.13
EV $mn	270.97
Market Weight	5.05%
Common Shares Outstanding mn	234
Freefloat mn	16.7%
Average Daily Val. Traded $'000	211.57
Last Dividend declared	FY13
PER (+1)	12.75
EV/EBITDA (+1)	9.63
Dividend Yield	0.00%
ROE	13%
Share price performance YTD	5%

12m share price performance ($) v. Industrial Index



	Total income	EBITDA	Net Income	EPS ($)	DPS ($)	EBITDA Margin	EV	Net Debt	EV/Sales	EV/EBITDA	P/E	P/Bk	Div yield
2014	120.2	22.4	11.8	0.050	0.00	18.6%	271.0	31.8	2.2	11.6	20.2	2.35	0.0%
2015E	124.5	26.9	18.7	0.080	0.01	21.6%	247.1	8.0	2.2	9.6	12.8	1.65	0.8%
2016E	130.8	28.3	20.6	0.088	0.01	21.6%	237.5	-1.6	2.2	9.2	11.6	1.47	1.3%
2017E	139.1	30.1	22.1	0.094	0.01	21.6%	230.1	-9.0	1.9	8.6	10.8	1.32	1.4%
2018E	150.2	32.5	24.2	0.103	0.02	21.6%	223.6	-15.5	1.6	8.0	9.9	1.18	1.5%

Truworths

Contraction in credit sales and soft margins; bottom line disappoints

Truworths' released a disappointing set of results for the year ended 06 July 2014. Group retail sales fell 7.8% y/y to $21.97mn in FY14, 5.2% below our expectations. Revenue in Truworths stores fell 7.72% y/y to $7.9mn. Compared to the prior period, cash sales and credit sales (including the in-store credit card) were down 18.0% and 5.0% respectively; like for like credit sales contributed 58.6% to total sales (vs 79.3% in the prior period). In Topics stores, revenue contracted 8.99% y/y to $11.2mn, with cash sales falling 1.5% y/y and credit sales down 9.8% y/y; like-for-like credit sales constituted 70.7% of total sales in FY14, down from 89.9% in FY13. Number 1 stores posted revenue of $2.89mn in FY14, down 2.85% from the prior period; cash sales fell 9.3% y/y whilst lay-bye sales increased 16.4% y/y. There was a significant decline in credit sales as over-leveraged customers slowed down on their debt servicing obligations which resulted in a decline in overall credit sales since Truworths does not sell to customers who fail to pay 100% of their now-dues on a monthly basis. The number of active accounts remained flat on the prior year, as new account opening were restricted by the low and decreasing levels of formal employment. Sales to civil servants, who constitute a significant portion of the Truworths' and Topics' books ($140k and $1.4mn respectively), were extremely slow in 1Q14 as Government struggled to pay salaries on time. This has improved since April however, following an increase in civil servant salaries, albeit paid much later in the month. Costs were also higher than we anticipated. GP margins were 50.5% in FY14 compared to 52.2% in the prior year and coming in 50bps below our forecasts; weighed down by increased discounts and markdowns in an attempt to drive sales volumes. Occupancy costs increased 6.0% y/y as basic rentals increased 10% with the inclusion of 4 new stores which were opened in FY13. Computer costs increased 13.7% as more branches were connected onto the optic fibre network and D&A costs increased 19.6% y/y with $675k in capex undertaken in the period. Trade receivable costs declined 51.0% as the provision for doubtful debts fell 31.7% y/y due to reduced credit sales and improved collections and summoning in the period. PBT for FY14 was $491k, against our expectations of $1.1mn PBT. PAT in FY14 was $354k, down a significant 70.0% from FY13 and 57.8% below our expectations.

Informalisation and shrinking credit customer pool weighing down on revenue

Truworths' strict credit policy is weighing down on sales as the pool of quality credit customers is shrinking in an increasingly challenging consumer environment. Informalisation of the economy is also cannibalising the Group's market share; the informal clothing sector is estimated to service over 30% of the market. Management have asserted that in order to uphold the brand and associated quality, they will not be venturing into the informal sector. On the positive, we are comfortable that Truworths is preserving quality, in terms of brand and book, however this also means that in the current operating environment, sales are likely to remain subdued as consumers come under increasing pressure. We expect the cost of living to increase following a plethora of newly-levied taxes as well as the newly-implemented statutory instrument fixing the price of maize and other grains, which will push up basic food prices. This in turn will see consumer spend, and the ability to service existing debt, deteriorate further. Following from these exogenous shocks, we have downgraded our revenue forecasts. We expect revenue in Truworths stores to decline a further 3.0% between FY14 and FY15 whilst we anticipate Topics stores will register a small 2.1% y/y recovery in revenue, following the civil servant salary increase. We expect Number 1 stores, which service the lower end of the market, to grow revenue 1.5% y/y as consumers continue to down trade. At Group level, this translates to a small 0.2% y/y recovery in revenue in FY15 to $22.0mn. To boost sales, the Company has expanded the product range into small electrics and appliances; however given consumer liquidity is the key issue, we don't expect this to have a material impact in the short to medium term. Management will focus on cost cutting measures and reducing gearing, so we expect an improvement in margins in FY15. We expect GP margins to improve 20bps to 50.7% in FY15 and EBITDA margins to increase from 3.4% in FY14 to 6.3% in FY15, on the back of reduced occupancy costs. Given the high quality of the book, we expect trade receivables costs to remain low at 1.7% of sales. We anticipate a 12.7% drop in PAT to $309k in FY15.

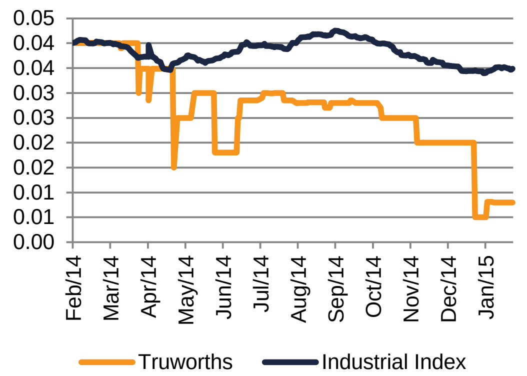
We maintain our buy recommendation

We estimate Truworths trades on PER (+1) 16.4x, and EV/EBITDA (+1) 11.1x to 2015E, compared to peers, at PER 19.0x and EV/EBITDA 11.2x for 2015E. Using a weighted combined multiples valuation method (PER & EV/EBITDA) and a 20% discount, we have arrived at a target price of USc1.50 for Truworths, implying an upside of 89.78% at current levels. We therefore upgrade to a BUY recommendation on Truworths.

Market Data

Report Date	02-Feb-2015
Bloomberg Ticker	TRUW: ZH
Rating	BUY
Current price $	0.008
Target price $	0.015
Market Cap $mn	11
EV $mn	19
Market Weight	0.22%
Common Shares Outstanding mn	384.07
Freefloat (%)	41%
Average Daily Val. Traded $000's	1.39
Last Dividend declared	FY13
Dividend Yield	0%
PER (+1)	34.1
EV/EBITDA (+1)	13.1
Share price performance YTD	2%

12m share price performance ($) v. Industrial Index



	Revenue ($mn)	EBITDA ($mn)	Net Income ($mn)	EPS ($)	DPS ($)	Operating Margin	EV ($mn)	Net Debt ($mn)	EV/Sales	EV/EBITDA	P/E	P/Bk	Div yield
2014	23.2	1.5	0.8	0.0022	0.00	6.7%	17.3	6.7	0.6	8.8	12.6	1.7	0.0%
2015E	22.0	1.0	0.3	0.0008	0.00	4.7%	18.6	8.1	0.6	13.1	34.1	1.7	0.0%
2016E	22.2	1.2	0.6	0.0017	0.00	5.5%	17.6	7.0	0.6	11.1	16.4	1.6	0.0%
2017E	23.1	1.5	1.0	0.0026	0.00	6.3%	17.0	6.4	0.7	9.4	10.7	1.4	0.0%
2018E	24.3	1.5	1.2	0.0031	0.00	6.3%	16.6	6.1	0.0	9.0	8.9	1.2	9.7%

Agro-Industrial

TSL

Robust top-line growth but disappointing bottom line performance

TSL's results for the year ended 31 October 2014 reflected robust top line growth but a contraction in net earnings, weighed down by a negative fair value adjustment on investment property, weak contribution from associates and margin pressure. Following a strong agricultural season (sector +23% in CY14), and particularly a bumper tobacco harvest (output +30% y/y), revenue grew a healthy 18.7% to $48.2mn in FY14, in line with our expectations of 19.3% revenue growth in the year. Tobacco Sales Floor (TSF) recorded revenue growth of 16% y/y, supported by a 10% growth in market share in the year to 50%. Propak Hessian achieved 24% revenue growth in FY14, having secured new customers following the strategic decision to reduce hessian prices. Agricura achieved 10% revenue growth in the year whilst TSL Trading's sales were subdued, partly owing to the earlier than anticipated end to the tobacco selling season in CY14. Bak Logistics achieved 7% revenue growth in FY14, mainly emanating from the General Cargo and Distribution divisions. Premier Forklifts, in its first full year of operations as a division of TSL, achieved strong revenue growth of c20%. Revenue generated by TSL Properties grew 9% y/y, with third party tenancy growing 8%. As expected, GP margins came under pressure in FY14 owing to start-up costs relating to TSL Trading and price reductions at Propak Hessian, affected in order to bring operating margins in line with the market. GP margins came off 230bps to 68.6%, in line with our forecasts. As a result, EBITDA grew a more moderate 6.2% from $8.9mn in FY13 to $9.5mn in FY14. In FY14, depreciation grew 16.6% y/y following capex of $3.6mn in the year. Share of profits of associates declined a significant 78.7% y/y, reflecting the generally depressed operating environment. Furthermore, a negative fair value adjustment on investment property of $1.2mn was posted (vs a $3.3mn positive adjustment in FY13), weighing down on net income. As a result net income came in at a disappointing $4.3mn, 26.9% down y/y and against our expectations of moderate growth (+2.9% y/y) at the bottom line. FCF improved significantly, increasing from a negative cash flow of $13.2mn in FY13 to positive cash generation of $4.6mn in FY14. This was due to an improvement in the working capital cycle, as receivables from TSL Classic Leaf fell significantly in the year as the associate becomes self-funding. A final dividend of 0.4USc was declared.

Agricultural outlook points to subdued earnings performance in FY15

Growth in agriculture is expected to decelerate significantly in CY15; Government's forecasts of 3.4% growth in agriculture and 3% growth in tobacco output are fraught with downside risks, emanating from adverse weather conditions, funding shortages and weak commodity prices. Furthermore, Government announced the re-introduction of a tobacco levy on tobacco growers at a rate of US$0.015 of each dollar of the selling price, with effect from 1 January 2015. This will negatively impact on TSL Classic Leaf's earnings, and possibly on other tobacco-facing divisions through downstream effects. As such, we expect revenue growth from TSL's agricultural operations to moderate in FY15. We have forecast revenue growth of 8.6% y/y, with much of that coming from the logistics and properties operations where we expect Premier Forklifts and 3rd party tenancy arrangements to make a more significant contribution to growth in FY15. With TSL Trading start-up costs behind us, we expect modest improvements in margins, with GP margins increasing 50bps and EBITDA margins remaining relatively flat at 19.7%. We expect contribution from associates to remain subdued, whilst the share of profit from Nampak Zimbabwe (formerly Hunyani) will likely decline in the year, following the change in ownership structure which saw TSL's stake in the company declining from 39% to 16.5%. We have forecast a 19.3 % increase in net income in FY15; however normalising FY14 net income (taking out fair value adjustments) this represents just 2.1% growth in FY15.

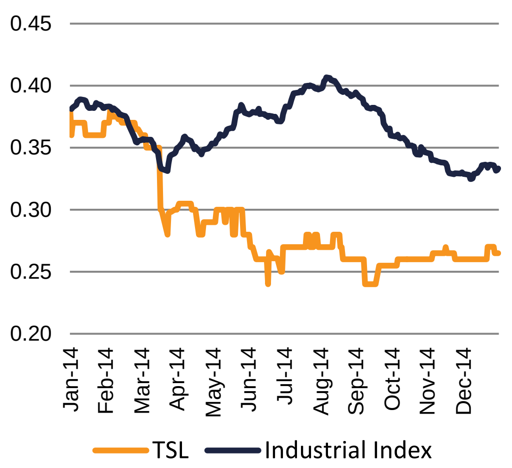
Downgrade to a SELL on weaker earnings prospectives

We estimate TSL trades on PER (+1) 15.9x, and EV/EBITDA (+1) 10.2x to 2015E, compared to peers, at PER 17.9x and EV/EBITDA 11.7x for 2015E. Using weighted combined multiples valuation and DCF methods, we have arrived at a target price of 2.25USc for TSL, implying downside of 15% at current levels and downgrading to a **SELL** recommendation on the stock

Market Data

Report Date	30-Jan-15
Rating	SELL
Bloomberg Ticker	TSL: ZH
Current price $	0.265
Target Price	0.225
Market Cap $mn	94.63
EV $mn	107.39
Market Weight	1.99%
Common Shares Outstanding mn	357
Freefloat (%)	26%
Average Daily Val. Traded $'000	19.00
Last Dividend declared	FY14
PER (+1)	15.94
EV/EBITDA (+1)	10.21
Dividend Yield	1.38%
ROE	8%
Share price performance YTD	-11%

12m share price performance ($) v. Industrial Index



	Total income	EBITDA	Net Income	EPS ($)	DPS ($)	EBITDA Margin	EV	Net Debt	EV/Sales	EV/EBITDA	P/E	P/Bk	Div yield
2014	48.2	9.5	5.0	0.014	0.40	19.7%	107.4	12.8	2.2	11.3	19.0	1.42	1.5%
2015E	52.3	10.3	5.9	0.017	0.37	19.7%	105.0	10.3	2.0	10.2	15.9	1.33	1.4%
2016E	55.1	10.9	6.6	0.018	0.41	19.9%	101.3	6.7	1.8	9.3	14.4	1.24	1.5%
2017E	57.1	11.2	7.1	0.020	0.44	19.6%	96.7	2.0	1.7	8.7	13.3	1.15	1.7%
2018E	60.1	11.5	7.7	0.022	0.48	19.1%	91.9	-2.7	1.5	8.0	12.2	1.07	1.8%

Disclaimer

Certification

The analyst(s) who prepared this research report hereby certifies(y) that: (i) all of the views and opinions expressed in this research report accurately reflect the research analyst's(s) personal views about the subject investment(s) and issuer(s) and (ii) no part of the analyst's(s) compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed by the analyst(s) in this research report.

Ratings Definition

Buy - Expected 1 year return is at least 20%

Hold - Expected 1 year return of between 0% and 20%

Sell - Expected 1 year return of 0% and below

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Research Team

Dzika Danha
ddanha@ih-group.com

Lloyd Mlotshwa
lmlotshwa@ihsecurities.com

Joan Takaindisa
jtakaindisa@ihsecurities.com

Carla Simleit
csimleit@ihsecurities.com

Contact Details

Physical Address
4 Fleetwood Road
Alexander Park
Harare
Zimbabwe

Tel: +263 (4) 745 133/139

Email: info@ihsecurities.com

Website: www.ih-group.com