1.0 INTRODUCTION AND EXECUTIVE SUMMARY

1.1 Introduction

The manufacturing sector has struggled in line with the decline in economic activity for the past ten consecutive years largely due to the hyperinflationary environment that peaked at an official figure of 231 million percent in 2008. The 2009 manufacturing survey assessed the state of the manufacturing sector over the first half of the year 2009. A total of 100 companies in all the regions of the country were polled**.** The last report was published in 2008 and covered events up to December 2007.
In 2008 no survey was undertaken because of the hyperinflationary conditions which could not allow the companies to give accurate and meaningful economic data.

1.2 Executive Summary.

Beginning of the year 2009 there was a positive policy change that saw the government introducing the use of multi-currencies in the country. This was on the back of a Global Political Agreement that allowed unity of all the key political parties in the country. This policy framework together with other complementary policies embarked on by the authorities ushered in a breath of life into what was becoming a dying sector

Since then, it has been pleasing to note that there has been an improvement in capacity utilization recording marked strides in reviving the sector to levels about 32.3% for the first half of 2009 from an estimated level of below 10% at the beginning of the year (18.9% in 2007). Consequently, signifying this improvement in unutilized capacity; overall output volume grew by 110% over the period under review. This has been largely due to the introduction of a multicurrency system which has allowed companies to plan and budget.

The 2009 findings showed that the industry 57.5% prefers joining the SADC customs Union while 33.3% prefers COMESA and 9.2% are indifferent. The major reasons for choosing SADC Customs Union were proximity and a wider market. An analysis of exports has seen Zambia regaining its 2005 and 2006 leading position as main destination for Zimbabwe's manufactured products. Industry highlighted high production costs and working capital as major constraints to exports.

The bulk of the raw materials (69%) were imported, whilst the remainder was locally sourced. This was attributed to poor agriculture performance in Zimbabwe over the decade as Agriculture contributes 60% of the raw material needs for the Manufacturing industry. It is worth noting full recovery of the Manufacturing Sector is linked to the recovery of the Agricultural Sector.

In line with electricity saving measures most companies have installed power factor correction units to regulate power usage. Other electricity saving measures for some industries include switching on power when necessary and resorting to alternative power sources.

The majority of companies (83%) did not make any investment owing to lack of funds to undertake such projects. In instances were investment was made it was for replacement purposes due to increased demand.

The industry at large saw a staggering 72% increase in working hours in the second quarter of 2009 largely on the back of increased demand for products as companies built up volumes to meet the demand. In line with the increase in the working hours the total wage bill also increased by 72.9%.

Key constraints to business performance were lack of working capital, exorbitant utility tariffs, higher than regional tax structure, high wage demand and expectations, credit and liquidity crunch. Going forward, the industry indicates the need for affordable and long term lines of credit

2010 outlook is largely positive subject to commitment to the GPA by the three principals. In addition 13.2% of the industry is of the view that the likely prosperity of the tourism industry is going have spill over effects to other sector and the economy at large. Zimbabwe is fortunate that it remains endowed with serious potential embedded in its natural resources. Having said so, local players need to recognize that the playing field has changed significantly and hence presents new challenges. For long term survival and regional competitiveness, the players need to reposition themselves in line with innovative global technologies and trends.

We note that the direction of capacity utilization is positive, but the pace is slow. This is in part due to liquidity challenges in the market which then constrained working capital. There is also a drag in recovery linked to in some cases imported products from China and South Africa being cheaper and hence more price competitive than locally manufactured products. This should be a call on the local industry to be cost competitive and efficient to stay in the market. To be nationally competitive, there is need to also get utilities working. As long as local producers are having to supplement power with small costly generators, water with boreholes and additional purifiers they will struggle to compete regionally in the long term.

Going forward there is need for a strategic response at National level where the country's strengths are identified and investment incentives structured to drive the country towards exploiting its competitive advantages. Efficiency, cost competitiveness, consistency and cooperation between government and private sector are key to the revival of industry and the economy at large! Out goes speculation, in comes strategic thinking and customer value addition as key strategic imperatives.

2.0 OVERVIEW OF THE SECTOR

2.1 Introduction

The aim of the survey was to unpack the state of the local manufacturing sector over the first half of the year 2009 through a selection of factors emanating from economic developments in the country. The major objective of this study was to afford companies the opportunity to take stock of these economic developments, thus enabling the private sector to make informed policy proposals to the authorities and hence create a platform for recovery of the manufacturing sector, and the economy as a whole.

The beneficiaries of the study are undoubtedly the Government, Confederation of Zimbabwe Industries members, manufacturing and processing industries, development partners, potential investors. In addition, the entire country stands to benefit from the discussions that stakeholders will obviously deliberate following this publication. This study anticipates continued re-ignition of debate and dialogue in our pursuit of a lasting solution to the country's economic challenges. It also offers a platform for decisions based on empirical findings.

Methodology

The survey was carried out for the 1st two quarters of 2009, and had a sample size of 150 companies distributed around Mashonaland, Matabeleland, Midlands, and Manicaland. A combination of interviews and questionnaires were used in the exercise.

The key data from companies was to assess the micro economic trends and impacts across various manufacturing sub-sectors of macro-economic fundamentals. Companies were also useful in providing data on employment, supply side constraints, capacity use and business confidence. The sample was drawn from a population of both CZI members and non members with each of the industrial sub sectors being proportionately represented

Secondary data was collected from Central Statistical Office (CSO) publications, Ministry of Finance Treasury Bulletins, Reserve Bank of Zimbabwe publications. This provided information on historical trends for volumes of production, employment trends, and impact of the business-operating environment on business viability.

2.2. Economic Overview

The signing of the Global Political Agreement (GPA) on September 15, 2008 ushered in hope into the country. On the 11th of February 2009, the Inclusive Government was born after agreement among the three political principals that a transitional arrangement was necessary to stabilize the political and economic situation in Zimbabwe. The terms of the agreement provided for the crafting of a new constitution, the reengagement of the international community and mobilization of resources locally and internationally to kick start the Zimbabwean economy. Amongst the key parameters on which the agreement was crafted included the following:

1. Raise resources to fund critical government functions in order to facilitate other activities in the economy
2. Capacitate the institutions which provide services such as water, electricity and telecommunications in order to support industrial activity
3. Inject resources into the ***productive*** sector to stimulate production and recoup lost capacity

4. Institute a macroeconomic management system which engendered stability in all markets in order to facilitate trade and commerce through instrument such as ‘multicurrency system’.

The Zimbabwean economy entered 2009 in a state of collapse following a decade of progressive decline. This decline was precipitated by a combination of factors whose cumulative result was a virtual grind to a halt for the economy. In mid 2008, inflation stood at 231 billion percent**,** foreign currency had totally disappeared from the formal market and finance for business had become a nullity. Capacity utilization in was estimated to be below 10% in most sub-sectors of the manufacturing sector, with every other sector of the economy adversely affected.. Social services such as hospitals, education, utilities such as electricity, water and sanitation and infrastructure in general were all in a state of continuous decline. Fortunately for Zimbabwe, the above episode of hyperinflation came to an end with the adoption of the multi-currency regime.

In 2009, the authorities estimated a growth rate of 3.7% (Fiscal Policy Review) and a single digit inflation rate. This was a remarkable turn of events for an economy that was really in distress.

2.3. The Manufacturing Sector

The manufacturing sector was at its peak in the 1990s, well known for its diversity of products and as an important contributor to the country’s GDP (16%) – RBZ Monetary policy Review 2009. The sector played a key role in the economy as it supplied 50% of its output into the Agricultural sector whilst 63% of its input was from the agricultural sector. At the beginning of the year 2009 the sector was operating at an estimated capacity utilisation level of less than 10% (Fiscal Policy Review 2009). Capacity utilisation had been hampered over the years by hyperinflation, foreign exchange controls, and shortages of foreign currency, energy disruptions, water woes, working capital constraints, price controls among other things.

The introduction of the multicurrency system in January ushered a period of stability for the sector and some companies have increased capacity utilization. The ministry of Finance estimates that the sector will require about USD1billion dollars to quickly recoup lost capacity and then move onto new expansions. Immediate requirements for the manufacturing sector amount to US$1 billion and to date the government and other stakeholders have identified USD562 million which will be made available to the sector going forward (Mid Term Fiscal Policy 2009). Further to this, government expects capacity to grow to around 60% by year end

2.4. Importance of the Sector

The manufacturing sector was the biggest contributor to GDP between 1980 and 1990 at 22% followed by agriculture at 14%. It is estimated that agriculture accounts for up to 63% of manufacturing sector’s inputs. In turn, estimates also show that up to 40% of manufacturing output is used as inputs in mining and agriculture. However due to challenges relating to low capacity utilisation, foreign currency shortages and rising inflation over the years the manufacturing sector’s contribution to GDP has declined from 24% in 1991 to about 16% in 2007. The FULL recovery of the manufacturing sector is therefore inextricably linked to the fortunes of the other sub-sectors of the economy.

The government has identified strategic sub-sectors that will assist the Manufacturing sector to improve capacity utilization, These strategic sectors according to section 184 of the STERP document include companies in food processing, beverages, textile and ginning, clothing and footwear, fertilizer, pharmaceuticals, motor industries, packaging, paper printing and publishing, chemical and petroleum products, non-metallic mineral products.

2.5. Employment

The general response to the economic crisis was a massive migration by Zimbabweans in search of greener pastures. This resulted in a major loss of skill in the sector to the region. The sector used to contribute 15% to formal employment at its peak in the 1990's.

2.6. Exports

At its peak in the 1990's the manufacturing sector contributed exports and foreign exchange earnings of up to 37% - RBZ Monetary Policy Review 2009. Total shipments for the Manufacturing sector from 01 January to 30 June 2009 amounted to US$67.1 million, compared to US$123.5 million for the same period in 2008, reflecting a 46% decrease. Over the first six months of 2009, the sector accounted for 14% of export shipment (mining 44%, tobacco 26%, agriculture 13% horticulture 2% and hunting 1%).

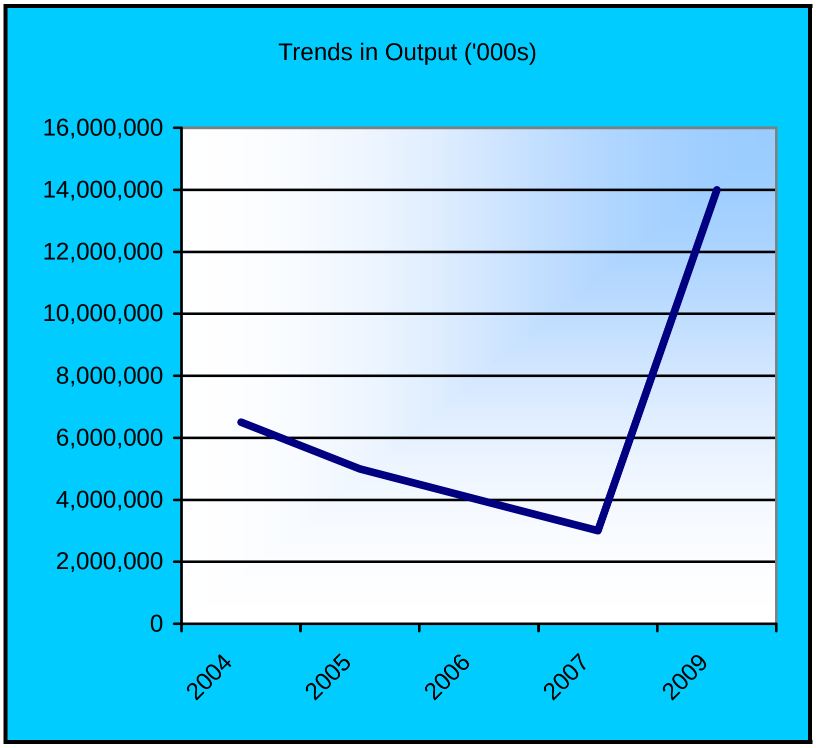
In part this decrease can be explained by a possible deliberate shift by the local manufactures to focus on the local market as trading and payment cycle are much shorter for the local environment than in exports. The market however needs to be cognizant of that Zimbabwe is a small market in global terms and therefore cultivation of export markets is central to long term growth.

3.0 2009 Survey Results – Review of trends and Constraints

3.1 Output volume growth analysis

Overall output volume grew by 110% over the first six months of 2009. 89.2% of the respondents recorded a positive output growth while 10.8% recorded negative growth in output. This was an improvement from the previous survey's finding in which only 30% recorded positive output growth and 70% recorded output decline.

Chart 1 – Trend in output



Source: Direct Information

A similar trend has been evident in exports where the decline in export value has improved compared to previous results. Below is a summary of the output export growth analysis. The table shows that 89.2% of the respondents recorded volume of exports growth greater than zero.

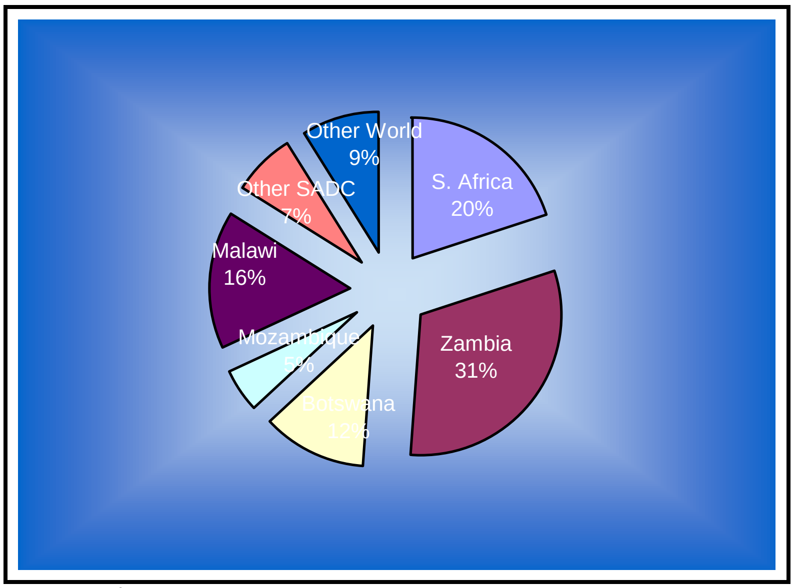
Figure 1: Output –Export growth analysis

Category	2006	2007	2009
Overall Output Volume Growth	78%	-28%	110%
Export Value Growth	22%	-35%	-5%
Output Volume Growth >0	20%	30%	89.2%
Output Volume Growth <0	80%	70%	10.8%
Export Value Growth >0	55%	66.7%	82.8%
Export Value Growth <0	45%	33.3%	17.2%

Source: Direct Information

4.0 Export Markets

Chart 2 - Export Destinations



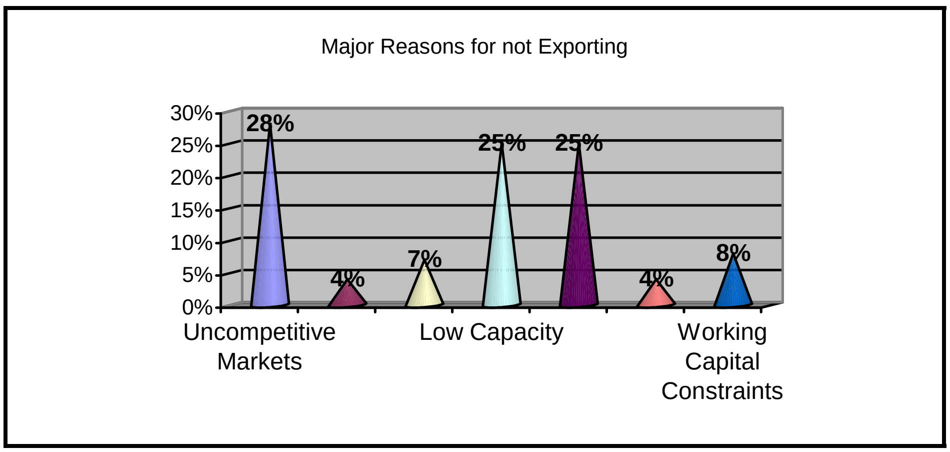
Source: Direct Information

The survey revealed that Zambia has regained its 2005-2006 position as Zimbabwe's leading export destination accounting for 31% of the manufacturing industry's exports for the first half of 2009 followed by South Africa (20%).

Figure 2: Leading Export Markets

Leading Export Market	2005	2006	2007	2009
South Africa	22%	20%	27%	20%
Zambia	30%	29%	23%	31%
Botswana	15%	18%	13%	12%
Mozambique	3%	5%	7%	5%
Malawi	15%	13%	11%	16%
Other SADC	7%	13%	7%	7%
Other World	9%	4%	13%	9%

Chart 3: Major Reasons for Not Exporting



28% of the surveyed firms cited uncompetitive export markets as the major reason for not exporting during the first six months of the year. Cost of production is still high. The unavailability of working capital has also hindered the sampled firms from exporting primarily because they (This labeling on this graph is too small for the eyes)
could not import enough requisite inputs to produce high quality goods demanded in international markets. Other key reasons for not exporting were low productive capacity and lack of foreign currency.

5.0 Capacity Utilisation

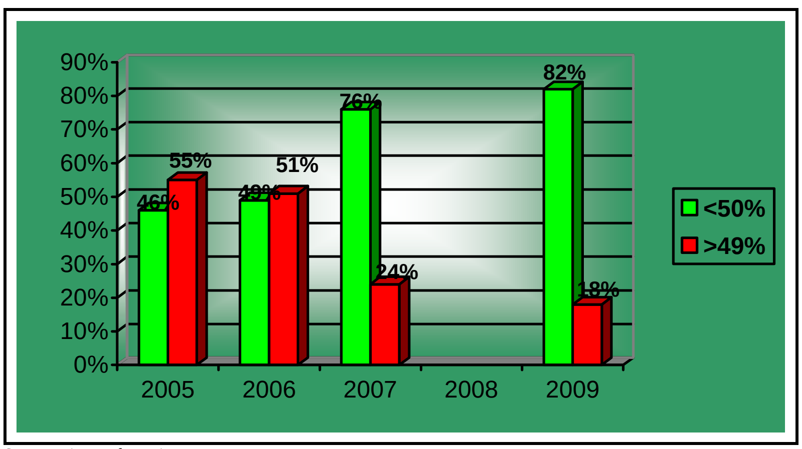
Figure 3 – Capacity utilization distribution Figure 3: Capacity Utilisation Distribution

Capacity	2005	2006	2007	2009
<30%	14%	18%	38%	45%
<50%	46%	49%	76%	82%
>49%	55%	51%	24%	18%
>74%	13%	97%	4%	6%
100%	3%	0%	0%	0%

Source: Direct Information

Average capacity utilization for manufacturing industry has improved to 32.3% in the first half of 2009. compared to the estimated less than 10% in 2008 (18.9% in 2007

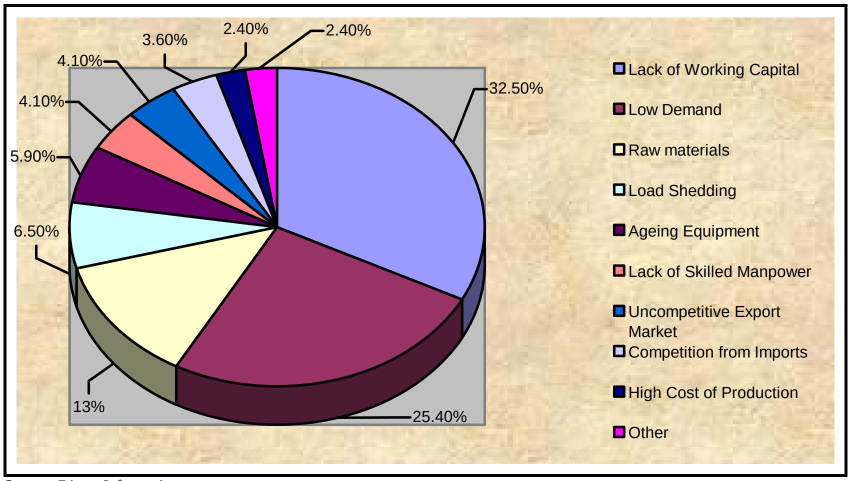
Chart 4: Trend in Capacity Utilization



Source: Direct Information

The distribution had more companies (82%) with capacity utilization less than 50% leaving the balance of 18% of companies with capacity utilization of above 49%, thus showing unprecedented levels of idle capacity in the economy. It must be noted that 6% of the industry is producing at more than 74%.

Chart 5: Major Capacity Constraints

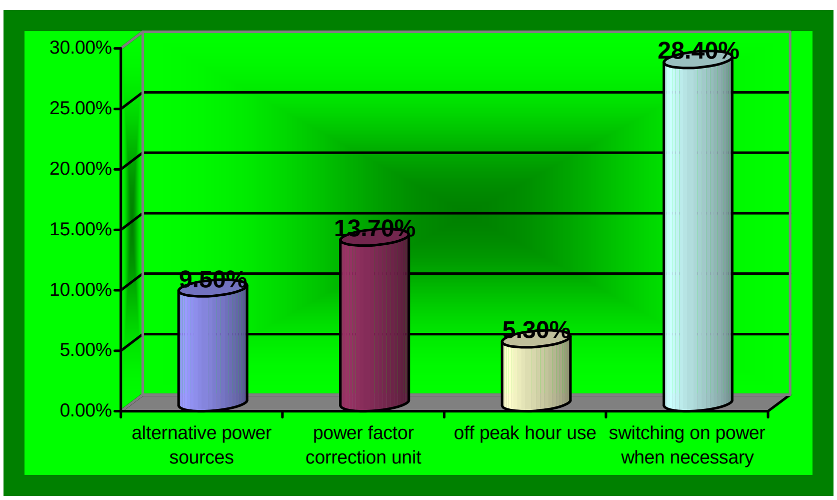


Source: Direct Information

Major capacity constraints have been attributed to lack of working capital, raw materials and low demand.

6.0 Electricity Saving Measures

Chart 6: Major Electricity Saving Measures



Source: Direct Information

Power shortage has become one of the key constraints to the manufacturing sector cited by 6.5% of the industry. However, 28% have now resorted to switching power as and when it is required in an attempt to save energy. A sizeable 13.7% of the industry has installed power factor correction units in order to regulated power usage.About 9.5% of the industries are now using alternative power sources for their operations and 5.3% that has now resorted to working off peak hours.

7.0 Raw materials

There has been an improvement in the supply of raw materials from the domestic market over the first six months of the year 2009. This has resulted in decline in imported raw materials, however imports still constitutes the bulk (69%) of the raw materials. However, given an estimated 60% of the domestic content comes from agriculture, the downturn of the agricultural sector had been hard hitting the productivity of the manufacturing sector.

Figure 4 – Quantity volume growth analysis of raw materials for Q2 2009.

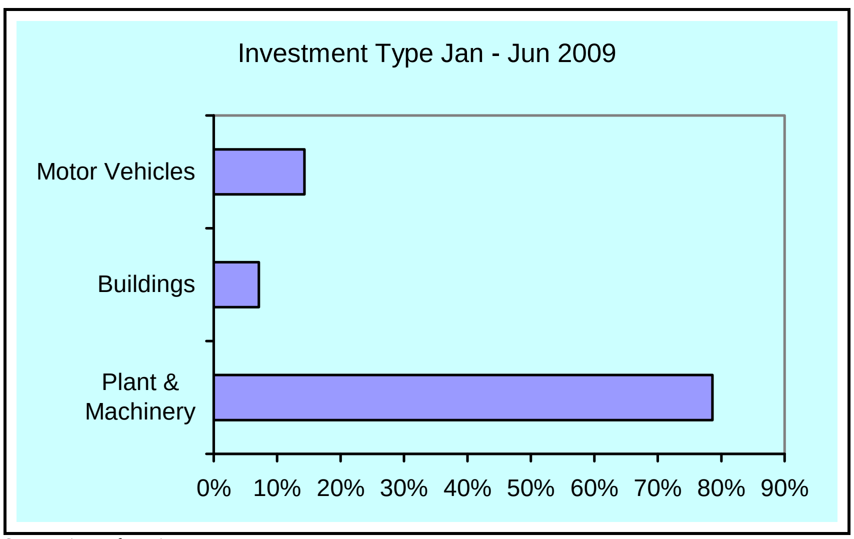
Figure 4: Quantity Volume Growth Analysis of Raw Materials for Q2 2009-10-16

	Domestic %	Imported %
Raw Material Quantity Growth	73.7%	53.8%
Raw Material Quantity Proportion	31.3%	68.7%
Raw Material Value Growth	39.4%	68.4%
Raw Material Value Proportion	49.0%	51.0%

Value growth of imported raw materials is higher (68.4%) compared to 39.4% for the domestic raw materials (39.4%). This shows an increase in the price of imported raw materials.

8.0 Investment

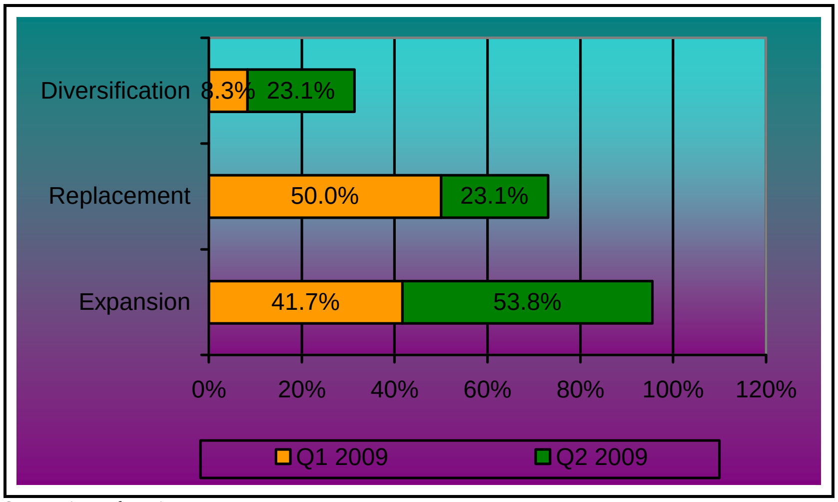
Chart 7: Investment Type



Source: Direct Information

On average, 17% of the respondents did invest in the first half of 2009 while 83% did not make any investment. The bulk of the investment was in the second quarter of the year at $1.2 million at cost. This was a nominal increase of 236% from investments of $354 thousand during the first quarter of the year.

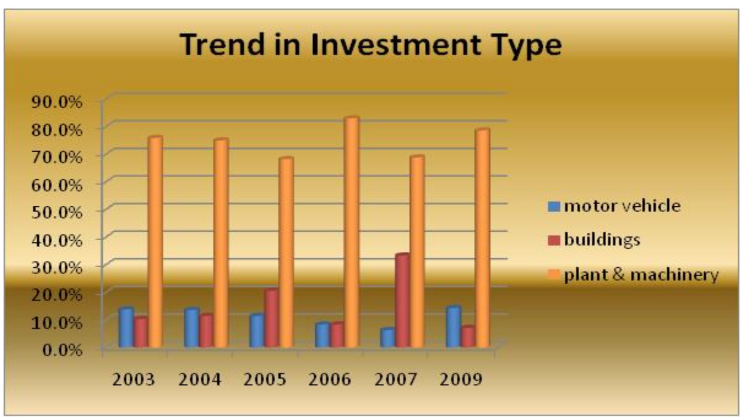
Chart 8: Reason for Investment



Source: Direct Information

The investment made in the second quarter was largely for expansion purposes with 78.6% responses having invested in plant and machinery. A different trend was however found in the first quarter when the bulk of the investments were for replacement purposes. This supports stabilization efforts by the authorities where the industry is now gunning for expansion as output increases.

Chart 9 – Trend in investment



Investments have remained the same, with the bulk of the investment going to machinery.

Source: Direct Information

9.0 Employment

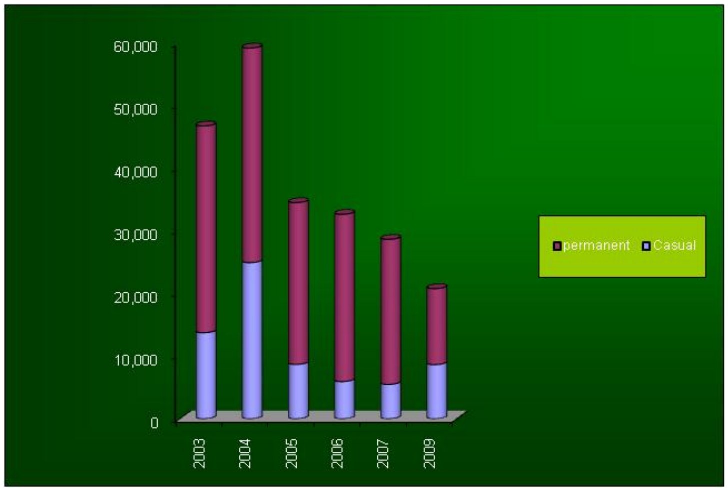
72% of the respondents have Increased working hours largely due to an increase in the capacity utilization in quarter 2 of 2009.

28% of the industry has found it difficulty to increase working hours. The total wage bill has gone up by 72.9%. This is in line with the increase in the working hours in quarter 2.

Figure 5 Employment Distribution

	Casual	Permanent
2003	13,729	32,967
2004	24,909	34,210
2005	8,678	25,798
2006	5,943	26,668
2007	5,491	23,126
2009	8,639	12,121

Chart 10 – Employment Distribution



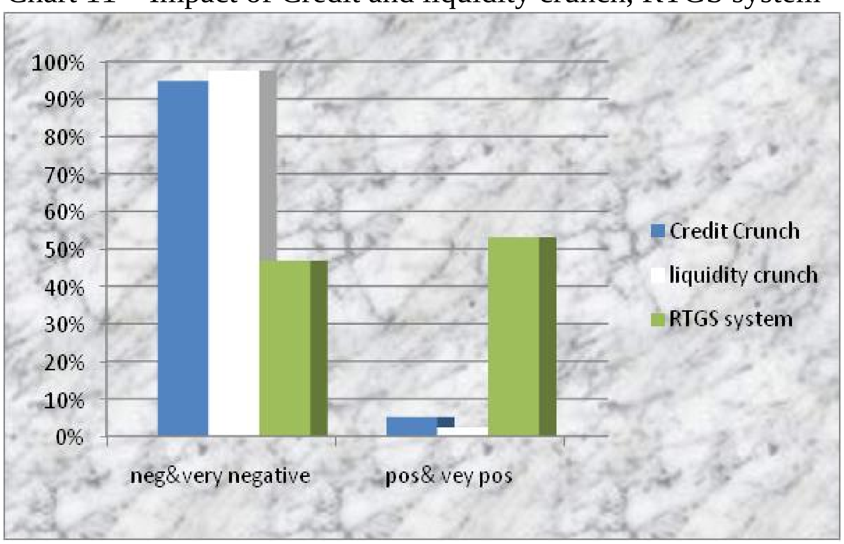
Source: Direct Information

Permanent employees increased by 3% from Quarter 1 to Quarter 2 2009 whilst casual workers increased by 7.3%. 11.8% of the companies have retrenched. Retrenchments have largely due restructuring through streamlining.

10.0 Business Performance

95% of the respondents indicated that the credit crunch had negatively affected business performance. The credit crunch also had an impact on the banks lending capacity as evidenced by the high response of the negative impact of liquidity constraints. This position is commensurate with the low levels of deposits in the banking institutions which were estimated at a mere $600 million in June of 2009.

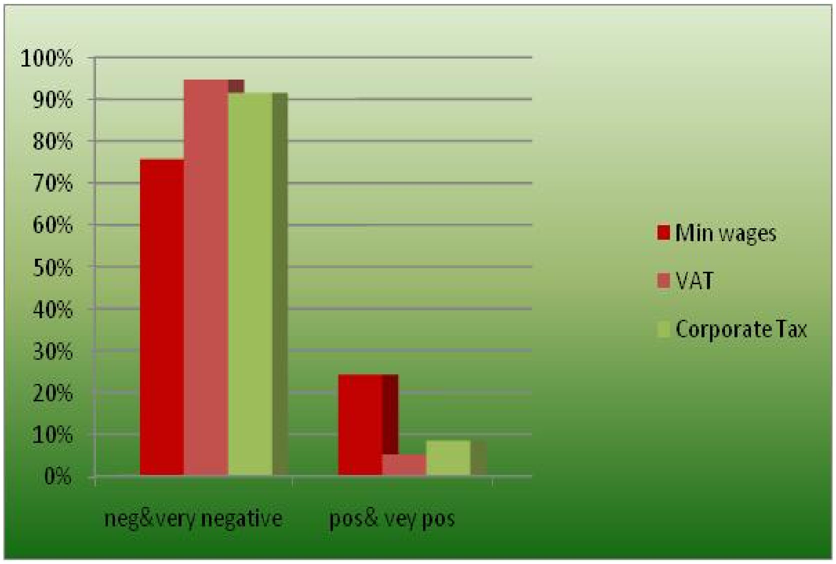
Chart 11 – Impact of Credit and liquidity crunch, RTGS system



Source: Direct Information

Chart 12 – Impact of Minimum wages, VAT and Corporate tax

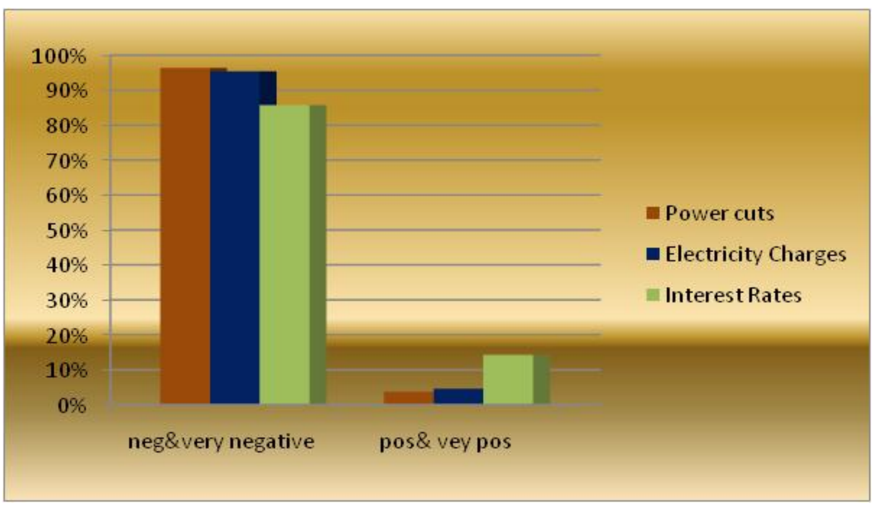
An analysis of corporate tax,
VAT and minimum wages shows that 91%, 95% and 76% respectively of the industry was negatively affected over the first half of 2009.



Source: Direct Information

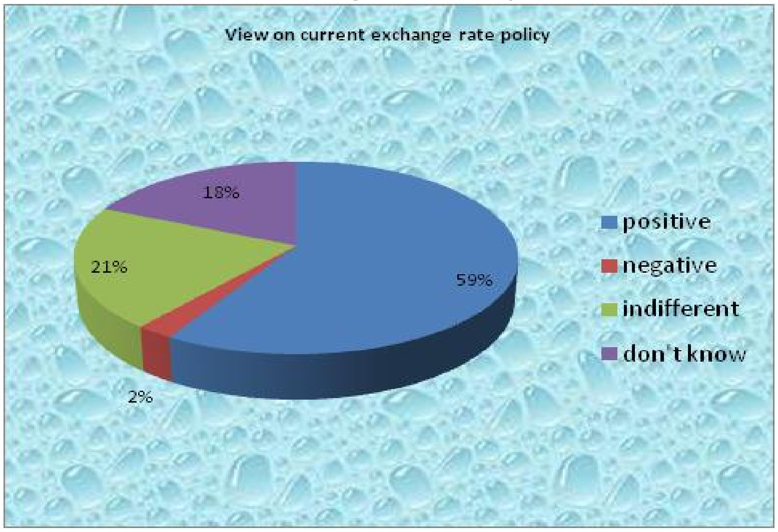
Chart 13 – Business constraints

96% of the respondents indicated that power Shortages are a constraint and this has been coupled with electricity charges that are higher than regional charges. High Interest rates on borrowing has also hindered business operations.



12.0 Policy environment

Chart 16 – Current Exchange rate Policy



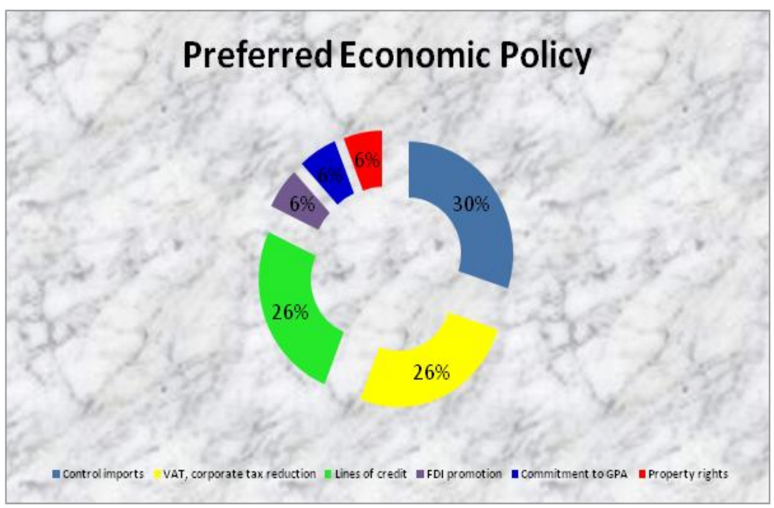
A review of the policy environment shows that 59% of the respondents are in favor of the current exchange rate policy saying this has brought about stability in prices in the economy. This is being viewed as a step in the right direction by the respondents. The current policy environment has ignited business confidence as the business fraternity is now able to plan unlike the situation in the last 18 months**.**

In terms of existing lines f credit with the outside world, 86.6% of the respondents indicated that they have no existing lines of credit and 13.4% of the respondents have access to lines of credit.

Preferred Economic Policy

30% of the respondents preferred the Global Political Agreement but indicated that there is need for commitment from all parties involved. This in turn, will ignite investor confidence which would see both local and foreign investors taking positions in the industry as well as injecting liquidity into the productive sector. 26% of the respondent indicated that VAT, corporate and income tax should be backdated to last year so as to give the industry some breather. This has been the same trend for lines of credit.

Chart 17 – Preferred Economic Policy

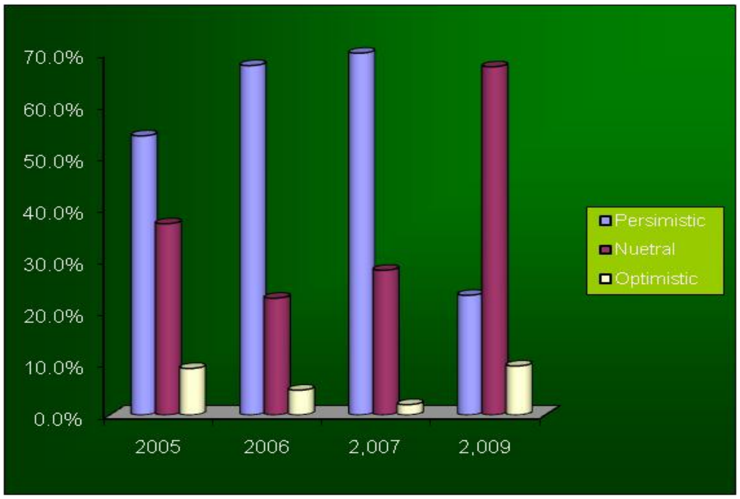


Source: Direct Information

3.0 Business Confidence

An analysis of the business confidence level evidently shows that confidence is building up since January 2009 with 9.5% of the industry optimistic about the future. 23.2% are pessimistic while 67.4% of the respondents are indifferent.

Chart 19 – Business Confidence



Source: Direct Information

Economic Outlook

50% of the respondents indicate that economic outlook for 2010 is likely to be positive subject to the outcomes of the Global Political Agreement (GPA). 13% of the respondents indicated that that the economic outlook is likely to be positive as a result of the 2010 World Cup to be held in South Africa. 5% growth to filter through from other sectors. 21% expect minimal growth while 7% cite investor confidence as key to a positive economic outlook.

14.0 Policy Implications

Observation 1 –Lines of credit
There have been improvements in availability of lines of credit, however these lines of credit are short term and very expensive for the local industry.

Impact assessment
As a result the industry has been experiencing working capital challenges resulting in low capacity utilization hence low productivity. The industry's inability to acquire spare parts has resulted in higher machine breakdowns. Consequently, capital investment has continued to drop over the last years.

Recommendation
There is need to engage the international community together with the local financial institutions to avail long term lines of credit which have favorable interest payment schedules. There is need for a creation of a stable economic environment, which will see an improvement in both foreign and domestic investment.

Observation 2 - Infrastructure
There has been serious dilapidation and underperformance of Zimbabwe's infrastructure (road, rail, air water and sanitation) from years of little maintenance and investment.

Impact assessment
Business have to employ costly workaround. These tend to raise production costs and are of limited viability over the long term. The huge costs make Zimbabwean products uncompetitive in the global market. If not addressed, this will soon become a bottleneck in the recovery process. Also the parastatals sector and local authorities account for 40% of the country's GDP. Full economic growth will not be achieved if the parastatals and utilities continue to under perform. The process of rehabilitating these institutions will in itself create jobs

Recommendation
There is need to attract more private funding into the rehabilitation of infrastructure alongside making them more autonomous and accountable to the country. To be able to do so requires that there has to be a PPP legal framework. There is also an opportunity of widening the investment universe through creation of a robust bond market with participation of local saving institutions such that they can also qualify in terms of prescribed asset ratios.

Observation 3 - Import competition
Our observation is that the industry was facing stiff competition from cheaper imported products.

Impact assessment
The market was flooded with cheap imports. The prevailing high cost of production has made it impossible for local producers to come up with an economic price system that would make the business viable. This could also be possibly be due to outdated production methodologies and an absence of economies of scale. More imports put pressure on the Balance of Payment position while exporting labor out of the local market into the producing countries.

Recommendation

There is excess production capacity into a shrinking market. This forces competition up and drives prices down. In response Zimbabwe producers will need to become efficient and clear about their competitive advantages. This will enable them to manage their prices and be globally competitive. On the back of their strengths the can then drive up production to benefit from cost reductions linked to economies of scale. Where possible, companies must also seek global alliances and technical partnerships that will enable them to leapfrog to latest technologies that are effective. Most players are obsessed with simply restoring previous operating methodologies. This is not good enough as some have fallen behind more modern methods and tools. This is time to innovate along one's trends.

Observation 4 - Taxation

Zimbabwe's tax structure has remained relatively higher that the region and his has constrained production and at the same time lowering demand through limited disposable income..

Impact assessment

This has reduced productivity through high production costs. Consequently, local products have become uncompetitive in the region.

Recommendation

Efforts should be made to widen the tax base and at the same time lowering the tax rate for compliance purposes. A reduction in VAT, corporate and income tax would stimulate demand as consumers will have more disposable income. Goods and services will also become cheaper through lower production cost.

Observation 5 – Foreign Direct Investment

We have observed that broadly the pace of inflows on investment is slow as international investors seem to be adopting a wait and see attitude.

Impact assessment

There is a dent on business confidence which will slow down the pace of recovery

Recommendation

Besides microecomic stabilization measures there is need to deliver a predictable and solid legal framework. There is need to consult widely but quickly to bring finality to amendments to the Mines and Minerals Act, the Economic and Empowerment and Indigenization Act and also put in place a creative PPP framework.

CONCLUSION

We are moving through a very exciting chapter in our history. We are on the brink of economic growth irrespective of the global financial crisis. Industry is committed to continuing to work closely with the Inclusive Government in order to realize our dream of economic recovery so that, as STERP says, we will " find our place in the sun, play our role in SADC, the African Union and the rest of the world".