Business Expectations Survey March 2016 – Summary Review

1. Introduction

The BES reports on current confidence levels among local businesses as well as their expectations of movements in key economic indicators. As such, it is an important additional source of information for policy analysis

The Bank undertakes the Business Expectations Survey (BES) twice a year in order to collect information on perceptions among the local business community about the prevailing state of the economy, as well as future prospects. Businesses are asked to respond to a range of questions relating to, among others, the business climate and prospects for economic growth, inflation and business performance over the survey horizon, which is the next twelve months. The survey responses are mainly in the form of the anticipated direction of change: i.e., whether conditions will improve, worsen or stay the same. The results are then consolidated in the form of an overall 'net balance' between positive and negative responses. The major exception to this is the measure of overall business confidence, which is presented on a gross basis, and also the proportions quoted in the section on 'challenges'. Thus, by design, the survey responses are predominantly qualitative, yet they provide valuable additional indicators to inform analysis.[1]

This report presents results of the survey carried out between March and April 2016[2] for three distinct periods: the first half of 2016 (H1-2016; i.e., the current period); the second half of 2016 (H2-2016), and the twelve-month period to June 2017 (H2:2016-H1:2017). The survey sample covers 100 businesses in agriculture, mining, manufacturing, water and electricity, construction, trade, transport, and financial and business services. For this survey, 60 percent of surveyed businesses responded, compared to 51 percent in the September 2015 survey.

2. Survey Context: Recent Economic Developments

Prospects for the global economy and recovery to positive growth for the domestic economy expected

The world economy is anticipated to experience modest growth of 3.2 percent in 2016[3], 0.1 percentage point higher than in 2015, and 0.2 percentage points below the previous forecasts in January 2016. This reflects a slowdown and weak commodity prices in emerging markets, notably China, and weaker recovery in advanced economies. However, the recovery in the world economy is expected to strengthen, leading to growth of 3.5 percent in 2017, driven mostly by improved performance in the emerging markets and developing economies, as conditions in stressed economies gradually normalise. Advanced economies are forecast to grow by 1.9 percent in 2016, increasing marginally to 2 percent in 2017; while, for emerging markets and developing economies, growth of 4.1 percent and 4.6 percent is projected for

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[1] The Appendix at the end of this report gives more details on the methodology.

[2] A summary of most of the results is shown in Table 1. All results are percentages: all are net balances with the exception of overall business conditions, which are gross balances.

[3] The forecasts for global growth are from the IMF's World Economic Outlook, April 2016.

2016 and 2017, respectively, compared to 4 percent in 2015. Within the region, the outlook for South Africa has deteriorated, with growth of 0.6 percent forecast in 2016 and 1.2 percent in 2017, constrained, in particular, by long-term power shortages, leading to generally negative business sentiment.

In the domestic economy, economic growth prospects have improved somewhat compared to 2015. GDP estimates released during the survey period indicate that the economy experienced negative growth of 0.3 percent in 2015, down from 3.2 percent in the previous year. This slowdown mainly reflects the weakening of the mining sector, which contracted by 19.7 percent in 2015, following the 0.5 percent growth in 2014. Mining output shrank due to both reduced demand for diamonds and lower production of copper/nickel. Growth in non-mining GDP slowed from 3.7 percent in 2014 to 3.5 percent in 2015. The Budget Speech (presented in February prior to the commencement of the survey), forecast overall real GDP growth of 4.2 percent for 2016 and 4.3 percent for 2017. While this forecast may be optimistic, there could be some support for the domestic economy through discretionary fiscal policy (such as the Economic Stimulus Programme (ESP), which encompasses both spending on projects and measures to improve implementation), together with some further recovery in the global economy. However, continuing water rationing and the lingering risk of power supply disruptions remain constraints on economic activity.

3. Business Confidence and Performance

Overall confidence in current business conditions has declined, but is expected to improve in subsequent periods

The overall confidence in the prevailing business conditions (H1-2016) is at 36 percent, 8 percentage points lower than the level that prevailed during the September 2015 survey (H2-2015). This was considerably lower than the 45 percent expected for this period at the time of the previous survey, a clear indication that expectations have been revised downwards. The continued subdued level of confidence possibly reflects the recurring water shortages in the greater Gaborone area as well as the continuing (albeit reduced) risk of power outages. Nevertheless, similar to the trend in recent surveys, the anticipated level of optimism for the rest of the survey period (next 12 months) rises, in this case to 62 percent. Current confidence among domestic-oriented businesses is 31 percent, significantly lower than 44 percent in the previous survey, but rising to 58 percent towards the end of the survey period. However, there has been a substantial increase in confidence levels of export-oriented businesses from 33 percent in the previous survey to 71 percent in the current period. The business confidence for export-oriented firms further improves to 88 percent over the next 12 months. Thus, the overall recovery in confidence for the second half of 2016 and the first half of 2017 is due to revival in confidence for both export and domestic oriented businesses.

4. National Output

Moderate expectations about growth in the domestic economy

On average, businesses expect real GDP to grow by 3.3 percent in 2016 and by 3.5 percent in 2017. These are substantially lower than the government forecast of 4.2 percent and 4.3 percent for 2016 and 2017, respectively, announced in the 2016 Budget Speech.

5. Capacity Utilisation, Investment, Input Costs and Employment

Subdued expectations on profitability and employment; input costs expected to increase but more moderately than before.

Relative to the September 2015 survey, respondents have lowered their optimism about the demand for their products during 2016. In turn, this feeds through to some downward revisions in expectations regarding employment and profitability, especially later in the survey period (a result that may appear at odds with the rising levels of expected business confidence).

The survey indicates that most respondents anticipate operating between 50 and 60 percent of their productive capacity in the current period. Thus, the current levels of capacity utilisation by businesses are broadly comparable with those reported in the September 2015 survey, hence suggesting that the business environment is still challenging but stable. However, in terms of investment (building, plant and machinery, vehicles and equipment and other), there has been some downward revision in expectations in the current survey compared to the previous survey. Such revisions are in line with challenging conditions reported by businesses. Nonetheless, a majority of businesses anticipate undertaking more investment in the second half of 2016.

Sentiment amongst firms regarding rising cost of inputs is still strong, although somewhat lower than in the previous survey. In particular, expectations of higher costs have eased for materials, rent, transport and other, while remaining broadly unchanged for utilities and wages in the second half of 2016. The overall easing of expectations of the rising cost of inputs is consistent with moderating expectations for overall inflation (Section 7). However, expectations of higher costs sharply rise in the latter part of the survey (the twelve-month period to June 2017), with the exception of utilities and wages.

6. Debt, Interest Rates and Access to Finance

Improved sentiment on access to finance, while expectations of borrowing costs are mixed

In line with their capital investment plans, companies would prefer domestic borrowing to funding from abroad (South Africa and international markets) in the second half of 2016, but would opt to borrow from South Africa in the twelve-month period to June 2017. This is broadly in line with anticipation of lower interest rates in Botswana during 2016, especially given the prevailing low inflation.

In terms of access to finance, there is a reduction in the proportion of businesses which believe access to credit is tight (50.8 percent compared to 53.1 percent in the previous survey), and those viewing access as normal (35.6 percent compared to 40.8 percent in the September 2015 survey). However, there is a significant increase in the proportion of businesses which believe access to credit is easy (13.6 percent from 6.1 percent in the September 2015 survey). In general, the survey indicates that sentiment about access to finance has marginally improved between the September 2015 and the current survey, in line with reports from commercial banks that they are ready to provide business finance.

7. Inflation Outlook

Inflation expectations remain within the Bank of Botswana inflation objective, but above observed levels of inflation

There has been a decline in inflation expectations for 2016, to an average of 3.7 percent from 4.8 percent in the September 2015 survey, and a slight increase to 3.8 percent for 2017. However, despite this downward trend, the average expected level of inflation remains somewhat above observed levels of inflation. Observed inflation for the year to March 2016 averaged 3 percent and has not reached 3.8 percent since December 2014. Nevertheless, an overwhelming majority of respondents expect inflation to be within the Bank of Botswana's medium term inflation objective range of 3-6 percent in 2016 (98 percent) and 2017 (96 percent), possibly reflecting the sustained period during which inflation has been within the objective range, which adds to the Bank's policy credibility.

8. Challenges

Water supply shortages considered a major challenge to the business community

Similar to the previous survey, water supply shortages was the most commonly-cited challenge by businesses. In addition, electricity supply interruptions, domestic demand (government and private) and inadequate supply of skilled labour were all equally ranked as the second most pressing challenge. .

9. Conclusion

Overall business confidence deteriorated from 44 percent in September 2015 to 36 percent in March 2016. Looking ahead, there is an increase in optimism, despite uncertainty surrounding the supply of key inputs (water and electricity), while the subdued demand in the global market continues to threaten business confidence. Although the latest GDP projections (Budget Speech published in February 2016) forecast a recovery in the domestic economy in 2016, with growth of 4.2 percent, this appears to be at the upper end of expectations. Inflation expectations appear firmly anchored within the Bank of Botswana's medium-term objective range, adding to the credibility of the current monetary policy stance.

TABLE 1: Results From the Business Expectations Surveys, March 2016 and September 2015 (All results are percentages and net balances except for overall business conditions, which are gross balances)

	MARCH 2016			SEPTEMBER 2015		
	H1 2016	H2 2016	H2 2016- H1 2017	H2 2015	H1 2016	H1 2016- H2 2016
Output						
• Production	50.7	15.6		31.3	48.9	
• Expected level of stocks	-4.4	-8.2		7.3	8.9	
• Volume of sales	21.0	-25.2		49.7	54.9	
• Expected volume of goods exported	-11.2	-33.7		30.8	26.6	
• Expected volume of goods imported	-24.2	-26.4		41.0	45.7	
• Employment	…	17.4	19.5	…	31.7	37.6
• Profitability	9.9	-0.3	…	1.7	37.4	…
Input costs						
• Materials	…	43.9	59.4	…	75.7	75.5
• Rent	…	47.8	78.6	…	68.5	33.4
• Utilities	…	78.5	68.4	…	78.0	70.9
• Wages	…	74.0	65.0	…	72.3	58.2
• Transport	…	23.8	53.6	…	31.3	68.9
• Other	…	40.8	58.3	…	64.3	64.2
Investment						
• Buildings	19.5	36.1	…	14.6	53.9	…
• Plant and machinery	45.3	61.5	…	60.8	59.6	…
• Vehicles and equipment	23.5	44.6	…	35.0	62.5	…
• Other	39.3	55.1	…	28.4	57.3	…
Expected volume of borrowing						
• Domestic	…	2.9	14.7	…	-32.7	-35.8
• South Africa	…	-8.5	18.0	…	-43.7	-36.9
• Elsewhere	…	-6.0	-6.1	…	-5.4	-4.1
Expected level of lending interest rates						
• Domestic	…	-3.7	19.8	…	-26.9	9.5
• South Africa	…	30.3	44.6	…	7.7	-23.4
• Elsewhere	…	3.3	19.2	…	14.1	20.2
Business Conditions						
Rating current business conditions satisfactory						
• Overall	36	…	…	44	…	…
• Exporters	71	…	…	33	…	…
• Domestic	31	…	…	44	…	…
Optimistic about business conditions in 6 months' time						
• Overall	…	48	…	…	45	…
• Exporters	…	75	…	…	50	…
• Domestic	…	44	…	…	45	…
Optimistic about business conditions in 12 months' time						
• Overall	…	…	62	…	…	54
• Exporters	…	…	88	…	…	25
• Domestic	…	…	58	…	…	57

APPENDIX: METHODOLOGY

In processing the BES results, the following methodologies were used. The methods, as applied more generally and specifically in this Report, are discussed below. They closely follow those used by the OECD and, to some extent, by the Bureau of Economic Research (BER) in South Africa.

The first step is to assign the plus (+), minus (-) and equal (=) signs to responses to each question in accordance with the following criteria. The (+) sign is used to denote the following responses: "increase" or "higher" or "more" or "above normal"; the (-) sign to denote "decrease" or "lower" or "less" or "below normal"; and the (=) sign to denote "same" or "normal" or "uncertain". Even with this type of coding, responses to multiple choice questions are difficult to interpret when all are presented simultaneously. Because of this difficulty, the BES results are normally converted into a single number through the use of net balances (B). The net balance method transforms all responses to a particular question to percentages and discards the percentage of (=) responses and subtracts the percentage of (-) responses from the percentage of (+) responses, i.e., B = 100 (P – N), where B is the net balance and takes values from –100 to +100, P is the percentage of (+) responses in the total and N is the percentage of (-) responses in the total. Experience elsewhere, notably in the OECD, shows that this loss of information is unimportant for most uses of the BES information; and that for such purposes as cyclical analysis, the use of net balances is considered both practical and adequate. If, however, this information is considered important, it can be shown along with the net balances information. In addition, changes in the percentage of (=) replies can be interpreted as showing changes in the degree of uncertainty among respondents.

In this report, the majority of the survey results are reported on a net balance basis, a few on a gross balance basis (e.g., current business conditions) and yet others for which quantitative data were directly collected, i.e., for inflation and national output growth rates no netting or grossing is done, they are reported as annual averages. Net balances, as defined above, are used without the explicit reference to the term 'net'. Where a different concept of the word balance is used, e.g., gross, an appropriate qualifying word is included.

What follows is an example of how the net balances are interpreted. If 80 percent of the respondents expect an increase in investment expenditure in Q2 of 2003 compared with the same quarter in 2002, 10 percent expect a decrease, while 10 percent expect no change and/or are uncertain, it can be concluded that the net majority (70 percent = 80 percent – 10 percent) of respondents expect to increase investment expenditure in the next quarter. The reverse – that investment expenditure is expected to fall – would be true if the net balance was a negative 70 percent. A net balance value between 0 and 100 indicates an improvement compared to the corresponding period in the past, between 0 and –100 a deterioration, and 0 no change.

The business confidence index (BCI) reflects business conditions at a particular point in time; and, thus, there is no comparison with a past corresponding period. Unlike the reporting of most other results, the BCI is reported on a gross basis. That is, it is calculated as the percentage of respondents indicating 'satisfactory' conditions to the total number of respondents indicating 'unsatisfactory' and 'satisfactory' conditions. The BCI value varies from 0 to 100, with zero indicating extreme lack of confidence, while 100 indicates extreme confidence. As an example, a BCI value of 40 percent is interpreted to mean that 40 percent of all respondents (gross) rated prevailing conditions as satisfactory.