Business Expectations Survey March 2008: Summary Review

1. Introduction

The report summarises the results of the eleventh Business Expectations Survey, conducted between September and November 2008. The survey covers three periods: the second half of 2008 (H2, 2008), the first half of 2009 (H1, 2009) and the twelve-month period to December 2009 (H1 – H2 2009); however, inflation and output measures are based on the national accounts year (June-July), and the calendar year, respectively.

The survey covers 100 businesses from the agriculture, mining, manufacturing, water and electricity, construction, trade, transport, and the financial and business services sectors. The response rate for the current survey was 65 percent, a significant improvement from the 57 percent recorded at the same time last year. Maintaining the response rate at over 60 percent is considered satisfactory.

The table at the end of the report provides a summary of the main results of the survey. Once again, the results of the survey should be interpreted with caution, as the sample size is still limited and mainly concentrated in Gaborone, hence, possibly leaving out divergent views from elsewhere in the country.

2. Survey Context: Recent Economic Developments

Since August, the Government has effected four fuel price reductions (one per month) in response to the steep fall in international oil prices. However, the extent to which this quickly resulted in revisions in expectations of future trends in transport costs may have been dampened by the general uncertainty surrounding oil market trends. The significant recent movements of the Pula (depreciation against the dollar; appreciation against the rand) would also have affected perceptions of likely movements in costs. More generally, although inflation overall had fallen in both September and October, this has been principally due to fuel price reductions, with inflation pressures continuing to build in other commodity groups, notably food.

While the period during which the survey was conducted coincided with a rapid deterioration of the outlook for the global economy[2], the likelihood of a large negative impact for Botswana only became apparent closer to the end of 2008. The impact of the rapidly deteriorating outlook for minerals exports will, therefore, only materialise in the next survey, in March 2009. In addition, given the extent to which business confidence has been supported by buoyant domestic demand due to rapid growth in government spending, a sharp slowdown in exports may not immediately translate into a loss of overall confidence.

3. Business Confidence and Profitability

There was continued optimism regarding the general prospects of the economy, with real GDP expected to grow by 6 percent in both national accounting years of 2007/08 and 2008/09. This is largely unchanged from the previous survey, despite the CSO having released estimates that growth in 2007/08 was lower, at 3.3 percent. This discrepancy could reflect a lack of publicity for the CSO estimates or, alternatively, a greater focus of

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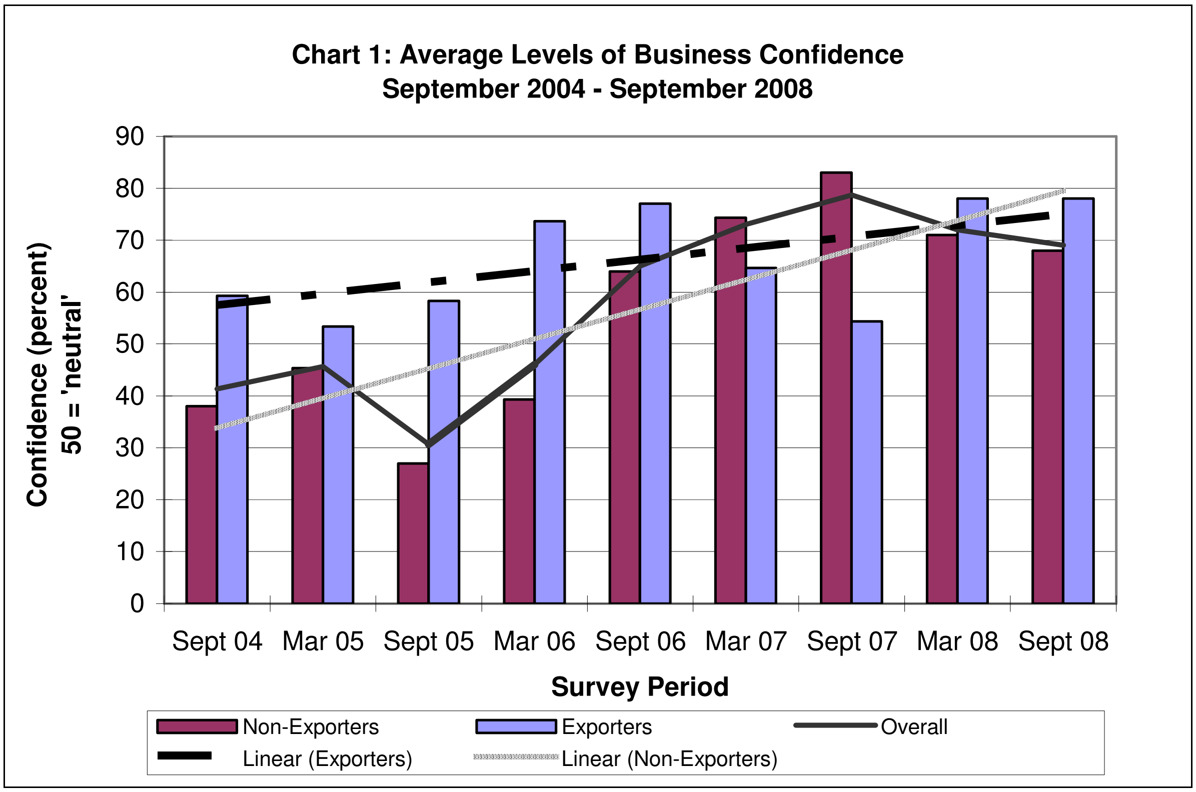
2 *The failure of Lehman Brothers, which is widely seen as the trigger point for the latest phase in the crisis, was in mid September, about the time the survey forms were distributed.*

respondents on the non-mining sector, which grew faster than the economy overall. The optimism regarding the overall economic performance is generally in line with the expectations of the Mid-Term Review of NDP 9, which may have continued to serve as a reference point.

Business confidence levels for H2, 2008 have firmed significantly, rising to 82 percent compared to 65 percent in the previous survey. That confidence among exporters (78 percent) was only slightly less than for domestic businesses (82 percent) probably reflects the delayed impact of the global slowdown. While there is some moderation of expectations going forward with the overall confidence level of 2009 falling to 73 percent, this still remains well above the neutral level. Chart 1 shows that in the four years that the survey has been running, the overall business confidence[3] has generally been rising, but with a noticeable downturn resulting from the 12 percent Pula devaluation in May 2005.



The generally positive economic outlook is supported by the proportion of firms (82 percent) which, at the time of the survey, regarded business conditions as generally satisfactory. However, this fell, somewhat, to 71 percent going in to 2009, which may be a sign that there was already some unease that the state of the economy could worsen. Regarding the principal performance indicators such as production and volume of sales, positive net balances, point to the current buoyancy, although there were negative sentiments, both for H2, 2008 and for 2009, about trends in profitability, which may be due to continued concerns over rising inputs costs.

[3] *The chart plots the simple average of the three periods covered in each survey.*

Most firms ranked domestic demand as the top among the most important factors influencing their business decisions, followed by the availability of skilled labour, access to raw materials and the exchange rate, respectively. The significance of domestic demand in guiding business decisions is a reflection of the heavy reliance of many businesses on Government contracts, while the appearance of the exchange rate among the top concerns in the current survey reflects concerns about the substantial movements in bilateral exchange rates between the Pula and trading partner currencies around October 2008.

4. Employment, Wages and Investment

As was the case in the March Survey, expectations on employment levels are positive, but weak. The current survey records a net balance of 7.1 for employment in the first half of 2009, although this increases somewhat for the year as a whole. This is against a background of strong expectations of higher wages, which could reflect efforts by workers to maintain their purchasing power, as well as the wider impact of pay increases and introduction of scarce skills allowances for civil servants.

With net balances of about 80 percent or more, input costs are confidently expected to increase. Compared to the previous survey, there has been some easing of expectations of higher transport costs, and this could have been more pronounced if the extent of the scope for fuel price reductions had been more apparent. Expectations of higher utility prices is consistent with the costs of increasing electricity supply, while the anticipated upward pressure on the costs of raw materials and other inputs (for construction, for example) may reflect concerns about possible scarcity due to the simultaneous undertaking of large scale projects in the region.

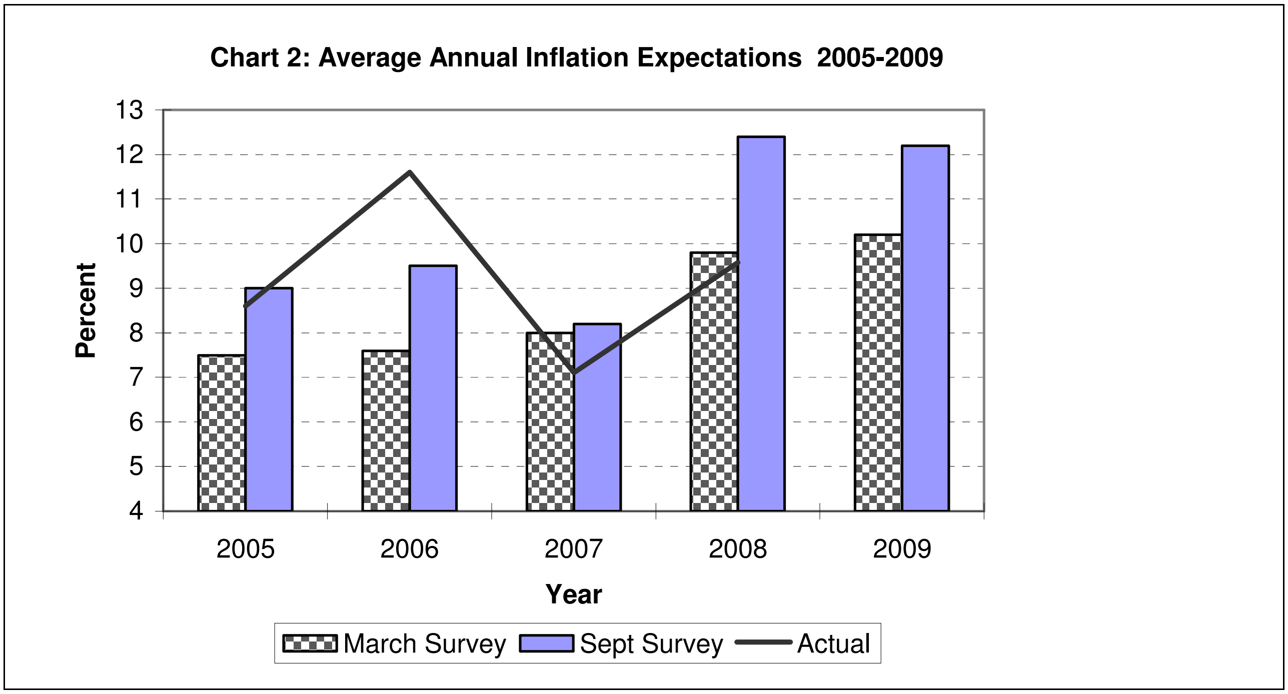
The level of investment spending is currently strong, and is expected to continue into 2009. This is with the exception of investment in new buildings, which could indicate that either capacity is sufficient or, possibly, shortage of suitable land is a constraint.

5. Debt and Financing

While there is some expectation of increased domestic borrowing, the low net balances (at about 20 percent) suggest this will be limited. Borrowing from South Africa and elsewhere, is expected to decline. While similar to the results of previous surveys, the reported low expectations of additional borrowing appear at odds with the observed rapid rates of commercial bank credit growth, suggesting that this is a part of the survey that requires further investigations. There is some easing of expectations of higher interest rates, both domestically and internationally, possibly influenced by the cuts in rates by major central banks that commenced in October.

6. Inflation

Businesses had revised upwards their expectations of inflation from earlier in the year. The expected average inflation in 2008 and 2009 was 12.4 percent and 12.2 percent respectively, compared to 9.8 percent and 10.2 percent in the previous survey. Chart 2 shows that annual average inflation expectations have exceeded actual average inflation per annum, since 2007.



The expected increase in prices for 2008 (12.4 percent) is very close to 12.1 percent, which is the actual average CPI of the first three quarters of the 2008, suggesting that, for near term expectations firms are following actual price movements. There was near universal expectation that inflation would remain outside the Bank of Botswana's objective range during 2009. Expectations are likely to have been informed, in particular, by earlier increases in food and fuel prices; consequently, it is likely the more recent cuts in fuel costs will likely have had a similar effect in revising expectations downwards. There may also have been some concern about the likely impact of the new levy on alcohol.

7. Conclusion

While the results of the survey provide valuable insight into sentiment among Botswana businesses, the results must be interpreted very cautiously. The timing of the survey, which was predominantly before the escalation in negative news about prospects for the economy, means that the generally optimistic orientation may not accurately reflect current sentiment. In this respect, the next survey, to be conducted in March, 2009 (and, therefore, after the 2009 Budget Speech) will be key.

It is, nonetheless, encouraging to know that, at least until recently, the confidence of businesses that had been gradually restored following the devaluation in May, 2005, had been broadly maintained. Furthermore, while the survey gave a strong indication that expected inflation remained well above the Bank of Botswana's objective, at the time this would have been a reasonable assessment. Now that the scope for lower fuel prices, which had been the main driver of inflation in 2008, has become more apparent, there must be a strong likelihood that expectations regarding inflation will respond accordingly.

Technical Note – Survey Sample and Methodology

a) *This survey is carried out biannually covering 100 businesses in agriculture, mining, manufacturing, water and electricity, construction, trade, transport and banks, insurance and business services. For purposes of consistency and continuity, in most instances the same businesses are covered in each round of the survey. Of these businesses, 72 percent are large-scale and 28 percent medium-scale, with size classification being based on number of employees (i.e., large = 100+). By way of comparison, the quarterly balance of payments survey only covers about 40 businesses.*

b) *This report covers the survey carried out between September and November 2008, for the periods H2 2008, H1 2009 and H1 – H2 2009. There is, however, a departure from these periods for questions concerning output and inflation, where, respectively, the national accounting (July – June) and calendar years are used.*

c) *The survey questions cover firm's expectations regarding general business conditions, national output, company production and capacity, stocks/inventories, volume of sales, imports of goods and services, employment, input costs, investment, profitability, company borrowing, and inflation. Questions typically require 'relative responses' (higher or lower, more or less, satisfactory to unsatisfactory, etc.). However, questions on national output and inflation require more specific numerical answers.*

d) *The methodology used closely follows those used by the Organisation for Economic Cooperation and Development (OECD) and, to some extent, by the Bureau of Economic Research (BER) in South Africa.*

TABLE 1: SELECTED RESULTS FROM THE BUSINESS EXPECTATIONS SURVEYS, MARCH 2008 AND SEPTEMBER 2008

(All results are percentages; all are net balances with the exception of overall business conditions, which are gross balances)

	MARCH 2008			SEPTEMBER 2008		
	H1 2008	H2 2008	H2 2008-H1 2009	H2 2008	H1 2009	H1 2009-H2 2009
Output						
• Production	59.0	85.0	…	69.2	56.6	…
• Expected level of stocks	-37.1	33.9	…	21.3	21.3	…
• Volume of sales	70.2	81.6	…	80.0	70.0	…
• Expected volume of goods exported	56.4	55.6	…	28.7	31.4	…
• Expected volume of goods imported	53.5	42.2		50.2	54.6	
• Employment	…	16.0	16.7	…	7.1	18.1
• Profitability	34.4	57.6	…	-12.4	-11.8	…
Input costs						
• Materials	…	85.2	88.8	…	92.1	88.1
• Rent	…	58.8	74.0	…	87.8	78.7
• Utilities	…	89.3	87.8	…	92.5	90.2
• Wages	…	90.4	89.6	…	90.1	76.9
• Transport	…	92.3	91.1	…	84.7	90.5
• Other	…	91.1	85.8	…	89.6	93.4
Investment						
• Buildings	29.6	72.9	…	6.1	27.2	…
• Plant and machinery	68.8	80.3	…	75.2	80.0	…
• Vehicles and equipment	49.5	45.9	…	54.9	67.9	…
• Other	61.5	65.3	…	30.1	65.7	…
Expected volume of borrowing						
• Domestic	…	27.1	14.0	…	17.9	21.2
• South Africa	…	5.6	2.4	…	-2.7	-2.8
• Elsewhere	…	20.7	15.8	…	-1.7	-1.8
Expected level of lending interest rates						
• Domestic	…	54.0	69.7	…	50.4	39.9
• South Africa	…	84.7	78.4	…	51.3	7.3
• Elsewhere	…	74.7	79.3	…	37.6	32.2
Business Conditions						
Rating current business conditions satisfactory						
• Overall	71.0	…	…	82.0	…	…
• Exporters	78.0	…	…	78.0	…	…
• Domestic	70.0	…	…	82.0	…	…
Optimistic about business conditions in 6 months' time						
• Overall	…	72.0	…	…	69.0	…
• Exporters	…	78.0	…	…	78.0	…
• Domestic	…	71.0	…	…	68.0	…
Optimistic about business conditions in 12 months' time						
• Overall	…	…	73.0	…	…	71.0
• Exporters	…	…	78.0	…	…	78.0
• Domestic	…	…	72.0	…	…	70.0