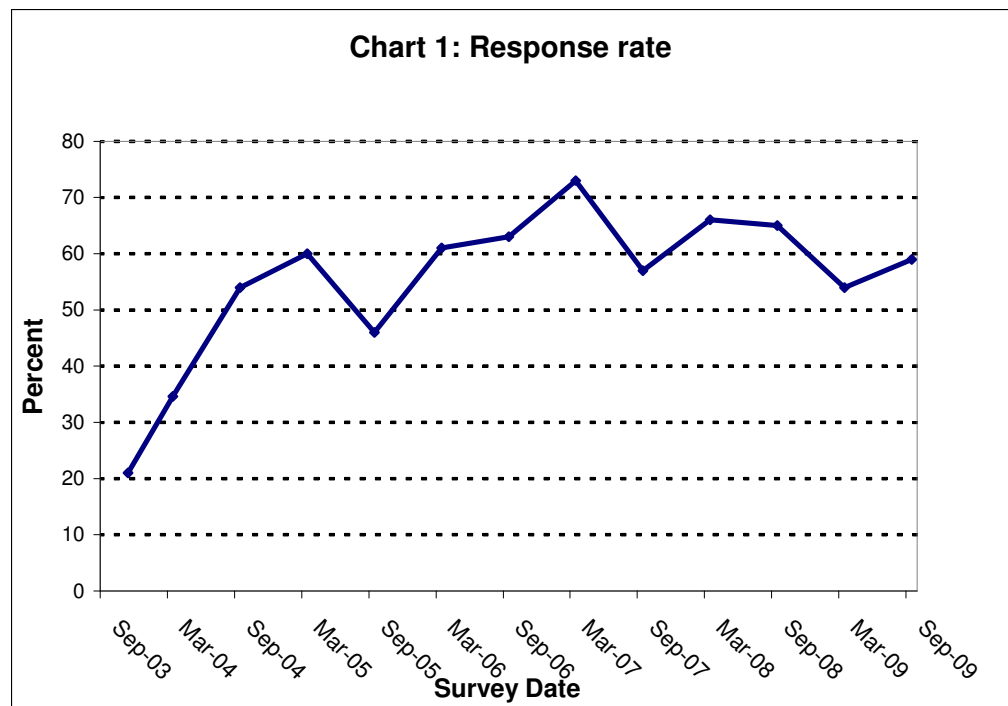


Business Expectations Survey September 2009: Summary Review

1. Introduction

This report presents results of the Business Expectations Survey carried out by the Bank of Botswana between September and November 2009.¹ The survey covers three periods: i.e., the second half of 2009 (H2 2009), the first half of 2010 (H1 2010), and the twelve-month period to December 2010 (H1 2010-H2 2010). Beginning with this survey, following the change in presentation of GDP estimates by the Central Statistics Office, output is no longer measured over the split year period (July-June) but, as is already the case with inflation, follows the calendar year.

The survey sampled 100 businesses in agriculture, mining, manufacturing, water and electricity, construction, trade, transport and banks, insurance and business services. As is evident from Chart 1, while the response rate was very low when the surveys commenced, it has now stabilised in the region of 60 percent. The response for this survey was 59 percent, slightly higher than 54 percent in the previous survey conducted in March and April 2009.



¹ A summary of most of the results is shown in Table 1, Appendix A.

2. Survey Context: Recent Economic Developments

Economic developments during the survey period generally suggest a more positive outlook compared to the bleak conditions prevailing during the March survey. Prospects for global economic growth in 2010 have improved, and this has already started to feed through in Botswana due, in particular, to renewed exports of diamonds, where output has recovered significantly faster than had been anticipated.

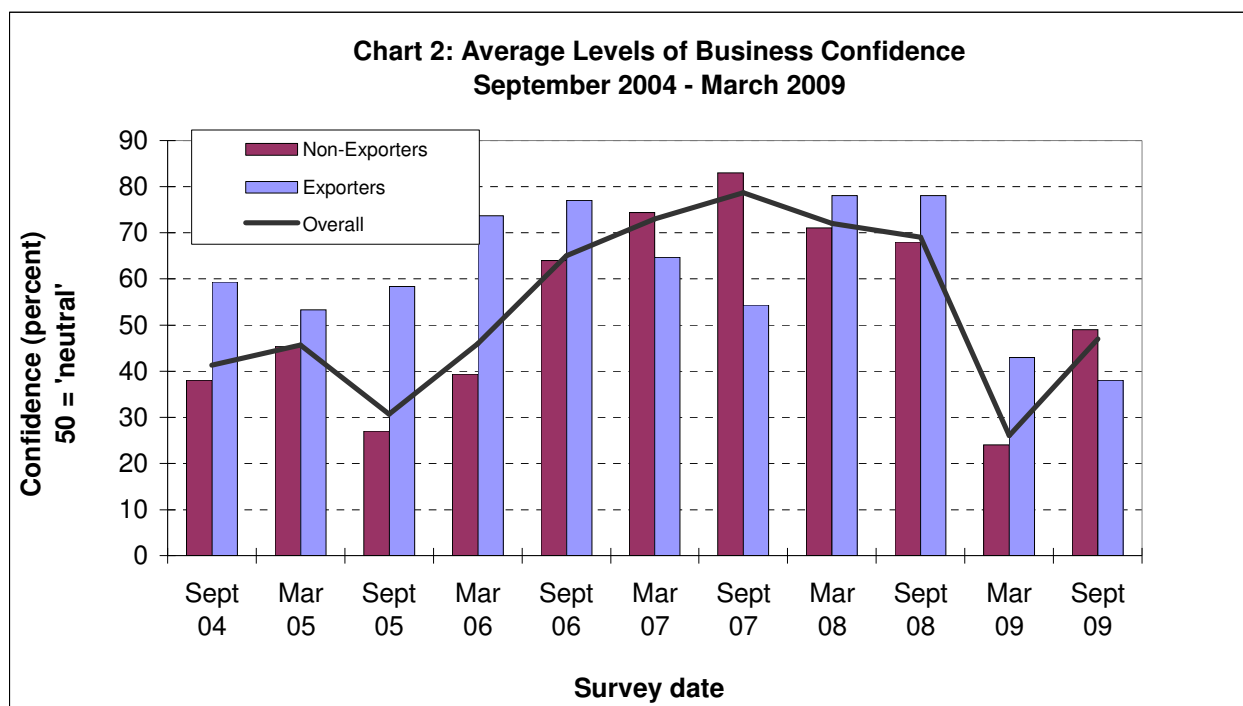
Outside of diamond mining, the performance of other sectors has been mixed. Supported by Government spending, growth of the non-mining private sector has been strong overall, notably in construction and agriculture (where new government support programmes were boosted by favourable rainfall). Manufacturing output has, however, been generally stagnant, with textile production in particular finding it difficult to remain competitive.

At the time of the previous survey, the Government's medium-term intentions regarding public expenditure were unclear and, with spending cuts being considered, this might have negatively affected the confidence of domestically-orientated businesses. However, the preparation of NDP 10 has now been completed and the Government has shown that it is willing to run substantial budget deficits funded, as necessary, by borrowing. Despite earlier commitments to rein in spending, a large supplementary budget of P5bn is proposed for 2009/10. However, the implication for the deficit may be less severe given the recurring problem of underspending.

3. Business Confidence, Profitability

There appears to have been a significant upturn in overall business confidence. At the time of the previous survey only 40 percent regarded prevailing business conditions as satisfactory, while even fewer (26 percent) were optimistic about conditions in the next six months. In contrast, although still relatively low, the satisfaction with current business conditions has risen to 47 percent, and this is maintained for the first half of 2010. For 2010 as a whole, confidence rises to 59 percent. This suggests that businesses are now more confident in both domestic and international economic conditions.

While expectations regarding profitability have also improved, the net balance is only marginally positive for H2-2009, consistent with most businesses remaining dissatisfied with current conditions. However, this is again a significant improvement on the previous survey. Prospects for profits turn sharply negative again in H1-2010, with a net balance of -39.9 percent. This is despite the greater optimism about improved conditions, and possibly underlines the extent to which there are lingering doubts about the extent of the current recovery. Here, there may be some anxiety that input costs are likely to start rising again. In particular, expectations of price increases for raw materials and transport, which had net balances of -1.0 and -7.4 percent in the March survey, have risen sharply to 44.3 percent and 58.9 percent, respectively.



Perhaps reflecting the continuing uncertainties regarding export markets, exporters are the most pessimistic of the firms surveyed, with only 38 percent satisfied with the current business conditions as opposed to 49 percent of firms for which the main market is domestic.² However, in line with the more positive outlook, looking a year ahead there is a sharp recovery in the optimism of exporters to 63 percent, compared to 59 percent for domestic businesses.

Overall, production is expected to fall in the current period, with a net balance of -58 percent, and then pick up in H1-2010, with a net balance of 49.7 percent. The same picture is reflected in sales where a negative net balance of -43.9 percent in the current period later becomes positive at 8.72 percent. At the same time, stock is expected to rise in both H2-2009 and H1-2010, consistent with firms' willingness to hold additional inventories as the market for their products continues to recover.

For GDP, growth of 1.7 and 2.6 percent is expected for 2009 and 2010, respectively. Given that this is now based on the calendar year, there is no direct comparison with the previous survey, although the sentiment regarding 2009 appears more negative. This may appear at odds with the general improvement in prospects, but the previous survey was conducted before the GDP estimates for the first quarter had been published, revealing the extent of the contraction due to the temporary closure of the diamond mines.³

² Within the sample of exporters (which make up 13 percent of respondents), the majority of respondents are manufacturers, while the others are from the mining and trade sectors. In total, exporters make up about 13 percent of survey respondents.

³ Indeed, given that contraction, overall growth in 2009 is likely to be negative.

4. Employment and Investment

Despite the improved outlook for production and sales, in 2010 expectations are for lower employment, especially in the first part of the year when the net balance is -40 percent. This may be explained by firms' desire to keep staff numbers to a minimum to maintain competitiveness and flexibility in the face of possible future shocks, while the gradual improvement later in the year is consistent with the tendency of employment to lag behind swings in economic activity.

Even though firms expect rising costs, they plan to increase their investment outlays on both plant and machinery and vehicles and equipment in both the current period and the first half of 2010. A pick up in investment is consistent with rising production in the absence of additional employment. Trends regarding investment in buildings are unclear.

5. Debt and Financing

Despite expectations of both higher output and additional investment, intentions regarding additional borrowing are, if anything, more negative than in the previous survey. This is most noticeable regarding borrowing in South Africa, with a negative net balance of about -42 percent throughout 2010. Borrowing in the domestic market is also expected to decline, albeit slightly in H1-2010, despite the series of interest rate cuts during 2009. This could indicate that firms regard the real cost of borrowing as remaining too high and, as a result, prefer to rely on retained earnings to finance investment, especially at a time when uncertainty regarding profitability might, in any case, limit access to borrowing from banks.

Businesses also appear to regard recent domestic interest rate cuts as being only temporary. Whereas in the previous survey there was a strong sentiment that rates would continue to be cut in both 2009 and 2010, this has been replaced by some expectation of rate increases. The basis for this is not clear, however, as there is no accompanying rise in inflation expectations (see below), while interest rates outside Botswana are expected to continue to fall.

6. Inflation Outlook

*There has been some further downward revision in expectations regarding inflation. For this survey, businesses expect average inflation to be 9.6 percent and 10.2 percent in 2009 and 2010, respectively, in comparison to 10.2 percent and 10.5 percent, respectively, in the previous survey. The sentiment that inflation would remain above the upper bound of the Bank of Botswana's medium term objective range in both 2009 and 2010 is held nearly universally by survey respondents. However, the extent of the downward adjustment remained modest in comparison to the observed trend in CPI inflation, where the average for the first ten months of 2009 was 8.8 percent. In turn, this suggests that businesses may *only have a narrow basis for* forming expectations regarding overall inflation, placing greater weight on expectations regarding production costs.*

7. Conclusion

Although still substantially below levels seen prior to the onset of the global economic downturn, business confidence in general has improved markedly in the current period compared to the March survey. Businesses, both domestic- and export-oriented, appear generally more optimistic, although individual indicators continue to suggest uncertainty and concern about the pace of recovery. Domestic confidence is likely to have been underpinned by willingness of the

Government to take significant additional debt over the medium term, rather than significantly curtail spending programmes, as businesses that mainly rely on Government spending may now be more reassured.

Inflation expectations are lower, but continue to fall only gradually despite the sharp decline in inflation during 2009. Moreover, there is some anticipation of monetary policy tightening during 2010.

TABLE 1: SELECTED RESULTS FROM THE BUSINESS EXPECTATIONS SURVEYS, SEPTEMBER 2009 AND MARCH 2009
(All results are percentages; all are net balances with the exception of overall business conditions, which are gross balances)

	SEPTEMBER 2009			MARCH 2009		
	H2 2009	H1 2010	H1-H2, 2010	H1 2009	H2 2009	H22009-H1 2010
Output						
• Production	-58.0	49.7	...	-49.0	-36.8	...
• Expected level of stocks	17.0	27.5	...	14.1	28.9	...
• Volume of sales	-43.9	8.7	...	-21.5	-0.8	...
• Expected volume of goods exported	-33.7	10.5	...	-36.8	-42.6	...
• Expected volume of goods imported	-37.6	3.8	...	-3.39	-39.4	...
• Employment	...	-39.8	-2.08	...	-52.3	-13.1
• Profitability	1.3	-39.8	...	-48.3	-58.0	...
Input costs						
• Materials	...	44.3	51.4	...	-1.0	0.7
• Rent	...	59.8	59.5	...	45.4	46.4
• Utilities	...	41.8	57.1	...	55.7	64.0
• Wages	...	29.4	38.1	...	32.9	23.8
• Transport	...	58.9	55.1	...	-7.4	67.5
• Other	...	59.6	64.2	...	43.6	10.7
Investment						
• Buildings	-12.9	11.8	...	-20.6	-36.8	...
• Plant and machinery	25.1	27.2	...	17.7	24.4	...
• Vehicles and equipment	40.8	49.7	...	-0.6	1.4	...
• Other	-33.4	-6.0	...	1.5	-22.4	...
Expected volume of borrowing						
• Domestic	...	-5.5	-21.3	...	8.42	-25.7
• South Africa	...	-42.8	-42.5	...	-32.3	-30.5
• Elsewhere	...	-23.5	-23.5	...	-27.4	-27.4
Expected level of lending interest rates						
• Domestic	...	4.1	22.1	...	-39.4	-24.6
• South Africa	...	-22.2	-6.2	...	28.8	-48.2
• Elsewhere	...	-26.6	-24.5	...	-23.5	-23.5
Business Conditions						
Rating current business conditions satisfactory						
• Overall	47	...	...	40	...	...
• Exporters	38	...	...	29	...	...
• Domestic	49	...	...	41	...	...
Optimistic about business conditions in 6 months' time						
• Overall	...	47	...	...	26	...
• Exporters	...	38	...	...	43	...
• Domestic	...	49	...	...	24	...
Optimistic about business conditions in 12 months' time						
• Overall	...	...	59	...	...	36
• Exporters	...	...	63	...	...	29
• Domestic	...	...	59	...	...	37

APPENDIX A

METHODOLOGY

In processing the survey results the following methodologies were used. They closely follow those used by the OECD and, to some extent, by the Bureau of Economic Research in South Africa.

The first step is to assign the plus (+), minus (-) and equal (=) signs to responses in accordance with the following criteria. The (+) sign is used to denote an increase or higher or more or above normal; the (-) sign a decrease or lower or less or below normal; and the (=) sign to denote the 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, BTS 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 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. Changes in the percentage of (=) replies can be interpreted as showing changes in the degree of uncertainty among respondents.

In the 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, e.g., 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.