

Business Expectations Survey September 2016 – Summary Review

1. Introduction

The BES generally provides a summary of views of the business community pertaining to expectations about their performance and the economy at large. In the current survey 84 percent of the surveyed firms responded, up from 60 percent in the previous one.

- 1.1 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 starts from the second half of 2016 until end of 2017. 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’, which sums the 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 economic indicators to inform policy analysis.¹*
- 1.2 This report presents results of the survey carried out between September and October 2016² for three distinct periods: the second half of 2016 (H2-2016; i.e., the current period); the first half of 2017 (H1-2017), and the twelve-month period to December 2017 (H1:2017-H2:2017). The survey sample covers 100 businesses in agriculture, mining, manufacturing, water and electricity, construction, trade, transport, and financial and business services. For this survey, there was a substantial improvement in the response rate, as 84 percent of surveyed businesses responded, compared to 60 percent in the March 2016 survey. The current response rate is also the highest³ achieved, since the inception of the Bank’s Business Expectations Survey in 2004.*

2. Survey Context: Recent Economic Developments

Although the world economy is expected to grow modestly in 2016 and 2017, the outlook for advanced economies remains subdued, while domestic prospects continue to be constrained by lower mining production.

- 2.1 The world economy is anticipated to experience modest growth of 3.2 percent in 2016⁴, before recovering to 3.4 percent in 2017. The forecasts are 0.1 percentage point below the previous forecasts made in April 2016 for both years. This reflects a subdued outlook for advanced economies. The expected recovery of the world*

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 significant improvement in the response rate was due to a vigorous pursuit of firms which, in the previous surveys, had been perpetually unresponsive.

⁴ The forecasts for global growth are from the IMF’s World Economic Outlook, October 2016.

economy in 2017 is driven mostly by improved performance in the emerging market and developing economies. Advanced economies are forecast to grow by 1.6 percent in 2016 and 1.8 percent in 2017 compared to 2.1 percent in 2015. For the emerging market and developing economies, growth of 4.2 percent and 4.6 percent is projected for 2016 and 2017, respectively, compared to 4 percent in 2015. Within the region, the outlook for South Africa has deteriorated, with growth of 0.1 percent forecast for 2016 and 0.8 percent for 2017, constrained, in particular, by concerns over power shortages⁵, leading to generally negative business sentiment. This was in spite of the undertaking by Eskom, made in early 2016, to cease load shedding for the rest of the year, and the ongoing construction of an additional power plant expected to become fully operational by January 2017.

- 2.2 In the domestic economy, growth prospects are constrained by lower mining production, resulting from uncertain and sluggish global economic activity. The economy experienced a negative growth of 0.3 percent in 2015, down from 3.2 percent in 2014. In the 12-months period ending in June 2016, GDP contracted by 0.3 percent compared to a 3.1 percent expansion in the same period in 2015. The weakening of total output mainly reflects the contraction of the mining sector by 23 percent, compared to a modest negative growth of 0.4 percent the previous year. The recent closure of the BCL and Tati Nickel mines is expected to have an adverse impact on total mining output as production ceases in the two mines.
- 2.3 Non-mining GDP improved marginally to 4 percent in the twelve-months to June 2016 from 3.8 percent in the same period in 2015. The Budget Strategy Paper for 2017/18, forecasts an output growth of 3.5 percent and 4.1 percent for 2016 and 2017, respectively. This is underpinned by the expected recovery in diamond production on the back of a projected increase in commodity prices and growth in global demand for diamonds in 2017. Growth prospects would be further supported by the stable electricity and water supply, following infrastructure developments.

3. **Business Confidence and Performance**

The proportion of respondents expecting business conditions to improve increases in the second quarter of 2016, and rises further in the near (first quarter of 2017) to medium term (the whole of 2017).

- 3.1 Overall business confidence in (H2-2016), is 43 percent, 7 percentage points higher than the level of 36 percent that prevailed during (H1-2016) reported in the March 2016 survey. The higher confidence level in the second half of 2016 is, however, five percentage points lower than the 48 percent anticipated for the same period at the time of the March 2016 survey. Nevertheless, similar to the trend in recent surveys, there is an improvement in the level of confidence for the rest of the survey period, rising to 51 percent in the first half of 2017 and to 58 percent for the entire 2017.
- 3.2 For domestic-oriented businesses the level of confidence is 43 percent in (H2 2016), compared to 31 percent in the first half of the year reported in the March survey.

⁵ According to 2016 Ibrahim Index of African Governance (2006-2015), South Africa registered the largest deterioration (about 30.1 percent) in electricity infrastructure (measured by electricity supply and reliable electricity supply) in Africa over the period from 2006 to 2015.

Looking ahead, the level of optimism improves to 46 percent in (H1 2017) and 52 percent in (H1 2017 – H2 2017). However, the confidence level of export-oriented businesses declined significantly, from 71 percent in (H1 2016) as reported in the previous survey, to 42 percent in (H2 2016). Going forward, business confidence recovers markedly to anticipated levels of 75 percent and 92 percent in H1 2017 and the whole of 2017, respectively. Thus, the overall expected upswing in business confidence for 2017 is due to a more positive outlook by both export and domestic oriented businesses.

4. National Output

Growth prospects for the domestic economy are expected to remain subdued over the survey horizon; that is from the second quarter of 2016 to the end of 2017.

- 4.1 *On average, businesses expect real GDP to grow by 2 percent in 2016 and by 2.6 percent in 2017. These are lower than the government forecasts of 3.5 percent for 2016 and 4.1 percent for 2017, indicated in the Budget Strategy Paper for 2017/18. Nevertheless, the expected economic growth rate for 2016 by the business community, is an improvement over the actual contraction of 0.3 percent realised in 2015, and is consistent with the improving business confidence.*

5. Capacity Utilisation, Investment, Input Costs and Employment

The majority (85 percent) of businesses expect to utilise at least 50 percent of their productive capacity in the second half of 2016, while at the same time anticipating to raise investment and employment levels in the first half of 2017. This is in spite of strong business sentiments about rising costs of inputs in the period.

- 5.1 *The survey indicates that 15 percent of the respondents anticipate operating below 50 percent of their productive capacity in the current period, while 54 percent expect to produce between 50 and 80 percent of their capacity; 31 percent of the businesses expect their productive capacity to exceed 80 percent. Thus, the current levels of capacity utilisation by businesses are broadly comparable with those reported in the March 2016 survey (46 percent anticipated operating between 50 and 80 and 33 percent expected to exceed 80 percent), hence suggesting that the business environment is still challenging, but stable.*
- 5.2 *The challenging business environment notwithstanding, survey respondents are relatively optimistic (compared to the previous survey) about the demand for their products in the current period and the first half of 2017, hence, they expect to accumulate lesser levels of inventory during this period. In turn, this feeds through to more positive expectations regarding production, employment and profitability in the current period and the remaining period of the survey. Nonetheless, expectations for investment in building, plant and machinery and other items in H2 2016, have been revised downwards in the current survey, compared to expectations for the same period expressed in the March Survey. However, there is an improvement in expectations relating to investment in vehicles and equipment between the two surveys. Looking ahead, a majority of businesses anticipate to undertake more investment in the first half of 2017, indicative of the optimistic outlook for 2017.*

- 5.2 Overall, sentiment amongst firms regarding rising cost of inputs is still strong and higher than in the March 2016 Survey. However, expectations of higher costs eased for wages and utilities, while remaining broadly strong for materials, rent, and transport and other items in the first half of 2017. Expectations of rising costs of inputs decreases in the later period of the survey, consistent with moderating inflation expectations (section 7).

6. Debt, Interest Rates and Access to Finance

The business community anticipate an easy access to credit with a bias towards domestic borrowing in the early part of 2017 due to favourable interest rates, before opting to borrow from South Africa later in the year.

- 6.1 For capital investment, companies would prefer to borrow domestically than abroad (South Africa and international markets) in the first half of 2017, but would opt to borrow from South Africa in the 12-months period to December 2017. Regarding borrowing costs, there is some anticipation of lower domestic interest rates in the first half of 2017 before rates start to rise in the later part of the year. Expectations of lower domestic interest rates are aligned to the reduction of the Bank rate from 6 percent to 5.5 percent since August 2016, together with prevailing low inflation, which continues to fluctuate around the lower end of the Bank's 3 – 6 percent range.
- 6.2 In terms of access to finance, there is a reduction in the proportion of businesses which believe access to credit is tight (44.9 percent compared to 50.8 percent in the previous survey), while the number of those viewing access as easy has fallen from 13.6 percent in the March 2016 Survey to 9 percent. However, there is a significant increase in the proportion of businesses which believe access to credit is normal (46.2 percent from 35.6 percent in the March 2016 Survey). In general, compared to the March 2016 survey, the business sentiment about access to finance has improved.

7. Inflation Outlook

The expected average inflation for 2016 and 2017, remain above the prevailing average levels, but within the Bank's inflation objective, suggesting confidence in the Bank's monetary policy.

- 7.1 Businesses have revised their inflation expectations for 2016 slightly downwards to an average of 3.6 percent from 3.7 percent in the March 2016 Survey. Inflation expectations of 3.8 percent for 2017 remained the same as in the March 2016 Survey. Despite the relatively low average inflation expectations, they still remain above actual inflation which averaged 2.8 percent in the 9 months to September 2016. Nevertheless, the majority of respondents expect inflation to be within the Bank of Botswana's medium term inflation objective range of 3-6 percent in 2016 (66 percent) and 2017 (68 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

The limited domestic market and constrained government spending are viewed as the predominant impediments to doing business in Botswana, whilst the supply of utilities is no longer a major concern.

- 8.1 Respondents now rank constrained domestic demand⁶ and government spending as the first and second most significant challenges facing businesses due to perceived slow growth in household disposable income and public expenditure. The next ranked impediments to business operations relate to regulatory and supervisory framework and availability of raw materials. Respondents also highlight unavailability of skilled labour and weak international demand among the serious challenges they face. Unlike in the past, water and electricity shortages have not been cited as significant challenges of doing business in Botswana as a result of stabilisation of water and power supply in most of 2016.

Conclusion

- 9.1 There has been an increase in overall business confidence to 43 percent in September 2016 from 36 percent in March 2016. Looking ahead, there is an increase in optimism, despite uncertainty surrounding demand for commodities in the global market, which continues to threaten business confidence. However, business expectations of output growth are below the latest GDP projections by the government (Budget Strategy Paper 2017/18) of 3.5 percent in 2016 (revised from 4.2 percent in the 2016 Budget Speech) and 4.2 percent in 2017 with constrained demand being the main operational challenge. Inflation expectations appear to be firmly anchored within the Bank of Botswana's medium-term objective range, suggesting that the business community views the Bank's pronouncements of its policy stance as credible.

⁶ This is unsurprising given the dominance among respondents of those for which the main market is Botswana.

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

	SEPTEMBER 2016			MARCH 2016		
	H2 2016	H1 2017	H1 2017- H2 2017	H1 2016	H2 2016	H2 2016- H1 2017
Output						
• Production	29.9	16.8		50.7	15.6	
• Expected level of stocks	-8.1	-2.9		-4.4	-8.2	
• Volume of sales	16.8	19.4		21.0	-25.2	
• Expected volume of goods exported	21.0	27.2		-11.2	-33.7	
• Expected volume of goods imported	-7.6	9.5		-24.2	-26.4	
• Employment	...	7.8	12.7	...	17.4	19.5
• Profitability	21.8	21.4	...	9.9	-0.3	...
Input costs						
• Materials	...	76.0	72.0	...	43.9	59.4
• Rent	...	64.8	62.7	...	47.8	78.6
• Utilities	...	66.9	64.1	...	78.5	68.4
• Wages	...	68.0	56.6	...	74.0	65.0
• Transport	...	59.5	54.9	...	23.8	53.6
• Other	...	59.8	57.7	...	40.8	58.3
Investment						
• Buildings	19.4	21.1	...	19.5	36.1	...
• Plant and machinery	31.9	57.8	...	45.3	61.5	...
• Vehicles and equipment	40.1	50.7	...	23.5	44.6	...
• Other	36.7	46.2	...	39.3	55.1	...
Expected volume of borrowing						
• Domestic	...	13.4	-2.3	...	2.9	14.7
• South Africa	...	-2.5	2.8	...	-8.5	18.0
• Elsewhere	...	-2.6	-2.6	...	-6.0	-6.1
Expected level of lending interest rates						
• Domestic	...	-12.3	3.9	...	-3.7	19.8
• South Africa	...	5.8	15.0	...	30.3	44.6
• Elsewhere	...	15.6	21.9	...	3.3	19.2
Business Conditions						
Rating current business conditions satisfactory						
• Overall	43	...	...	36	...	...
• Exporters	42	...	...	71	...	...
• Domestic	43	...	...	31	...	...
Optimistic about business conditions in 6 months' time						
• Overall	...	51	...	...	48	...
• Exporters	...	75	...	...	75	...
• Domestic	...	46	...	...	44	...
Optimistic about business conditions in 12 months' time						
• Overall	...	...	58	...	...	62
• Exporters	...	...	92	...	...	88
• Domestic	...	...	52	...	...	58

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, 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 purposes such 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 information on the net balances. 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. 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.