

Business Expectations Survey March 2017 – Summary Review

1. Introduction

The BES summarises views of the business community regarding their perceptions about the current and future state of the economy. The response rate improved marginally from 84 percent in the previous survey to 85 percent in the current survey, which is the highest achieved since the inception of the Survey.

1.1 The Bank's biannual Business Expectations Survey (BES) collects information on the local business community's perceptions about the prevailing state of the economy and economic prospects. In the survey, businesses respond to a range of questions relating to, among others, the business climate and the outlook for economic growth, inflation and business performance over the survey horizon, which starts from the first half of 2017 and ends in the first half of 2018. The survey responses mainly focus on the anticipated direction of change; i.e., whether conditions will improve, worsen or stay the same. The results are then consolidated on the basis of an overall 'net balance', obtained by summing up the positive and negative responses for each question/element. The major exception relates to the measures of overall business confidence and proportions on 'challenges' which are presented on gross basis. Thus, by design, the survey responses are predominantly qualitative, yet they provide valuable indicators to facilitate analysis and inform policy decisions.¹

1.2 This Report presents results of the survey carried out between March and April 2017² for three distinct periods: the first half of 2017 (H1:2017; i.e., the current period); the second half of 2017 (H2:2017), and the twelve-month period to June 2018 (H2:2017-H1:2018). The survey samples 100 businesses in agriculture, mining, manufacturing, water and electricity, construction, trade, transport, and financial and business services. Compared to the previous survey, the response rate improved marginally from 84 percent to 85 percent, which is the highest achieved since the inception of the Survey in 2004.

2. Survey Context: Recent Economic Developments

Modest economic growth is expected globally in 2017 and 2018, while in the domestic economy, growth is expected to be underpinned by improvement in global demand for diamonds and discretionary fiscal policy and further recovery in the global commodity markets.

2.1 The world economy is anticipated to grow by 3.5 percent in 2017³, before picking up the pace slightly to 3.6 percent in 2018. This reflects prospective improvements in performance in advanced, developing and emerging market economies. It is forecast that advanced economies will grow by 2 percent in both 2017 and 2018 compared to 1.7 percent in 2016, while the overall growth for the emerging market and developing economies is projected at 4.5 percent in 2017 and 4.8 percent for 2018, compared to

¹ The Appendix at the end of this Report provides more details on the methodology.

² A summary of most of the results is shown in Table 2.

³ The forecasts for global growth are from the IMF's World Economic Outlook, April 2017.

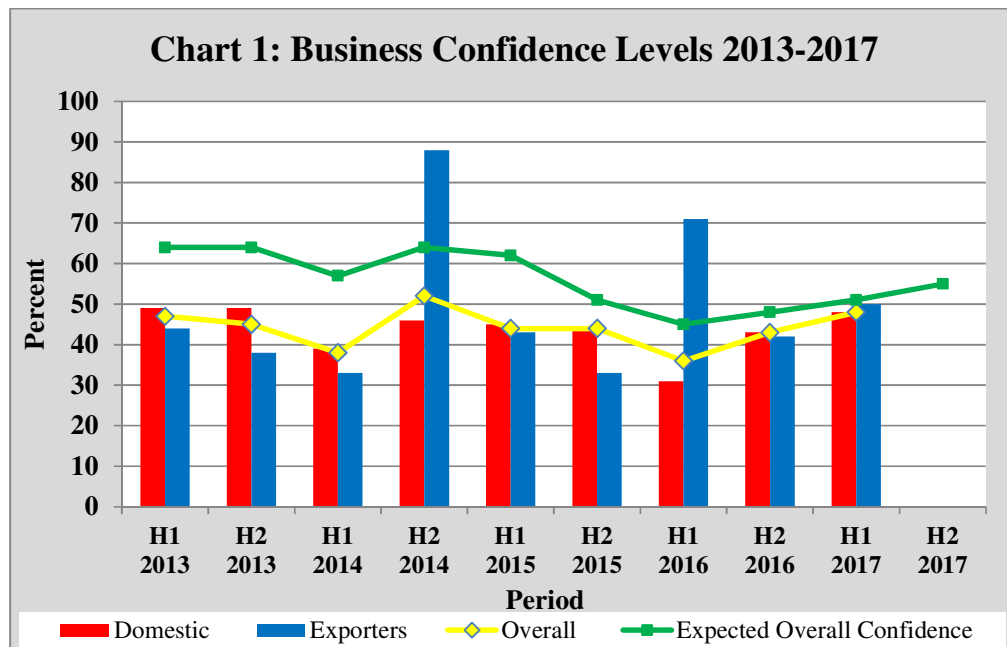
4.1 percent in 2016. However, uncertainty surrounding global trade policy and openness, as well as the moderation of growth in China, could adversely impact on medium-term growth prospects globally.

- 2.2 Regionally, the outlook for South Africa indicates growth of 0.8 percent for 2017 and 1.6 percent for 2018. The weak growth prospects for South Africa, which will potentially have an adverse impact on neighbouring countries including Botswana, are partly influenced by political uncertainty and the slow pace of structural reforms. Moreover, the recent downgrade of South Africa's credit rating to sub-investment grade could also undermine growth by constraining private investment and household consumption in that country. Potential negative spillovers into Botswana, though expected to be moderate, include risks of higher inflation, lower exports and SACU revenue.
- 2.3 In the domestic economy, growth has significantly improved compared to 2015. Real GDP grew by 4.3 percent in 2016, following a contraction of 1.7 percent in 2015. This strong recovery in economic activity mainly reflects the strengthening of the non-mining sector, which grew by 5.5 percent in 2016 compared to a contraction of 1.7 percent in 2015, mainly as a result of the recovery in the diamond trade which forms part of the trade sub-sector. Mining output declined at a slower rate of 3.7 percent in 2016, compared to a contraction of 19.6 percent in 2015, owing to improvements in the diamond market. The contraction in 2016 mainly reflects a reduction of 21.2 percent in copper and nickel output, following the closure of the BCL and Tati Nickel Mining Company in October 2016.
- 2.4 The Budget Speech presented in February for 2017/18 financial year forecasts output growth of 4.2 percent for 2017⁴. This is underpinned by the expected growth in global demand for diamonds, support for the domestic economy through discretionary fiscal policy, including the Economic Stimulus Programme (ESP) and further recovery in the global commodity market.

3. **Business Confidence and Performance**

Optimism among businesses strengthened in the first half of 2017 compared to the second half on 2016, and is expected to rise further in the survey horizon for both domestic market -oriented firms and exporters.

⁴ This forecast was based on a more conservative growth estimate of 2.9 percent for 2016, hence might no longer hold.



Note: The expected overall confidence (the green line) shows expectations as per the previous survey.

- 3.1 As shown in Chart 1, optimism among businesses strengthened from a confidence level of 43 percent in H2:2016, to 48 percent for the current survey period (H1:2017). However, firms seem to have developed some uneasiness with the business conditions in H1:2017, as their confidence level for the period declined by 3 percentage points compared to their perceptions about the same period in the previous survey.⁵ This lower confidence level is also reflected in the lower growth forecast of 1.9 percent for the domestic economy by local businesses. However, in line with previous trends, more firms expect better business conditions going forward, with an overall confidence level of 55 percent for the second half of 2017 and 67 percent for the twelve-month period to June 2018.
- 3.2 Confidence amongst domestic-oriented businesses is 48 percent in the first half of 2017 compared to 43 percent in the second half of 2016. Looking ahead, the level of optimism improves to 56 percent in H2:2017 and 65 percent in the year to June 2018. Similarly, the confidence level of export-oriented businesses increased from 42 percent in H2:2016 to 50 percent in H1:2017 and it is anticipated to remain the same in H2:2017, before recovering markedly to 75 percent in H2:2017-H1:2018. Thus, the overall expected upswing in business confidence for 2017 and the first half of 2018 is due to a more positive outlook by both export and domestic-oriented businesses.

4 National Output

Businesses expect subdued domestic economic activity in 2017, despite the 4.2 percent growth anticipated in the 2017 Budget Speech.

⁵ The reduced confidence about business conditions in the first half of 2017, than originally expected, is consistent with the downward revisions on expected levels of production, volume of sales and profitability.

- 4.1 *On average, businesses expected real GDP to have grown by 1.9 percent in 2016 and 2.3 percent in 2017, up from a contraction of 1.7 percent in 2015. Business' expectations of economic growth for 2016 are much weaker than the 4.3 percent estimated by Statistics Botswana. Nonetheless, the expected growth by firms for 2016 also suggests an improvement over the contraction of 1.7 percent realised in 2015, and is consistent with the improving business confidence.*

5 Capacity Utilisation, Investment, Input Costs and Employment

80 percent of businesses expect to utilise at least half of their productive capacity in the first half of 2017 compared to 85 percent in September 2016, consistent with the downward revision in expectations about levels of production, volume of sales and profitability in the first half of 2017.

- 5.1 *The survey indicates that 20 percent of the respondents anticipate to operate below 50 percent of their productive capacity in the current period, while 56 percent expect to produce between 50 and 80 percent of their capacity. The remaining 24 percent of the businesses expect their productive capacity to exceed 80 percent. As such, the current levels of capacity utilisation by businesses are broadly comparable to those reported in the September 2016 survey (54 percent expected to operate between 50 and 80 and 31 percent expected to exceed 80 percent). This suggests that the business environment is still challenging, but remaining largely stable.*
- 5.2 *Relative to the September 2016 survey, optimism about the demand for respondents' products during 2017 has slightly diminished, which though inconsistent with improving confidence for the year, is in line with downward revisions in expectations regarding production and profitability. However, in relation to higher production, expectations improve significantly from a net balance of 2.4 percent in H1:2017 to 17.9 percent for H2:2017.*
- 5.3 *Expectations regarding investment in buildings, plant and machinery, vehicle and equipment and other items have also been revised downwards across the board between H2:2016 and H1:2017. For H2:2017, there is a significant improvement in expectations regarding all categories of investment except for other items, which declines markedly from 73.8 percent to 63.4 percent. The generally improving expectations with respect to investment are consistent with the optimistic outlook for the latter part of 2017.*
- 5.4 *Sentiment amongst firms regarding the rising cost of inputs (materials, rent, utilities, wages, transport and other) remains very strong and greater for H1:2017 in the current survey than in the previous one. For utilities, the strong expectation of rising costs is in line with increased water and electricity tariffs implemented during the survey period. The upward trend in cost of inputs continues for the 12-month period from H2:2017 to H1:2018, except for utility and other costs, perhaps reflecting that businesses do not expect utility costs to rise again in the near future. The decline in the number of firms expecting further increases in other costs is consistent with expectations of moderate inflation, given that actual inflation continues to fluctuate around the lower end of the Bank's 3-6 percent medium-term objective range.*

6 Debt, Interest Rates and Access to Finance

The business community would prefer borrowing from South Africa in the second half of 2017 and in the 12-month period to June 2018, while firms are sceptical about domestic borrowing for the entire survey period.

- 6.1 *To finance their planned capital investments for the second half of 2017 and the 12-month period to June 2018, companies have indicated preference to borrow from South Africa with net balances of 8.7 percent and 7.3 percent, respectively, while remaining almost neutral (zero net balance) about borrowing from elsewhere in both periods. On the other hand, more firms are sceptical about domestic borrowing, as reflected in a net balance of -4.9 percent in H1:2017, which worsens to -12.8 percent in the longer horizon H2:2017-H1:2018, partly explaining the decline in growth of business credit by domestic commercial banks during the first quarter of 2017. This is contrary to the anticipated reduction in domestic interest rates by the business community, which is consistent with the reduction in the Bank Rate from 6 percent to 5.5 percent since August 2016.*
- 6.2 *However, sentiment about easy access to domestic credit remains weak, worsening from a net balance of 9 percent in the second half of 2016 to 6 percent in the first half of 2017. This could explain weaker expectations about domestic borrowing. In general, business sentiment about access to finance has improved, with the net balance of those viewing it as tight declining slightly from 44.9 percent in H2:2016 to 43.4 percent in H1:2017. Furthermore, the net balance of businesses which believe access to credit is normal rose from 46.2 percent in H2:2016 to 50.6 percent in the current period.*

7 Inflation Outlook

Inflation is expected to remain within the Bank of Botswana's medium-term inflation objective range for both 2017 and 2018, indicating credibility of the Bank's monetary policy.

- 7.1 *Businesses have revised their inflation expectations for 2017 from an average of 3.8 percent projected in the September 2016 survey to 3.3 percent in the current survey. Inflation is expected to increase to an average of 3.6 percent in 2018, consistent with the recent increases in utility and fuel prices and, to some extent, levies related to the Department of Road Transport and Safety, which are expected to result in a higher average annual inflation for 2017 than the 2.8 percent of 2016. Moreover, should Government implement additional upward adjustments in administered prices, average inflation is likely to crawl up. Finally, consistent with current trends and prospective developments, the majority of respondents expect inflation to continue to be within the Bank of Botswana's medium-term inflation objective range of 3-6 percent in 2017 (60 percent) and 2018 (68 percent).*

8 Challenges

Constrained domestic demand, restricted government spending and unfavourable exchange rate movements are the most cited impediments to doing business in the current survey.

Table 1: Challenges Ranked Top 3 in the Last Four Surveys

CHALLENGES TO DOING BUSINESS	RANKINGS				
	2015		2016		2017
	March	Sept	March	Sept	March
<i>Constrained Domestic Demand</i>	1		2	1	1
<i>Government Spending</i>		3	2	2	2
<i>Unavailability of Skilled Labour</i>	2		2		
<i>Water Shortages</i>		1	1		
<i>Inadequate Electricity Supply</i>	3	2	2		
<i>Strict Regulatory & Supervisory Framework</i>				3	
<i>Exchange Rate Movements</i>					3

8.1 *Similar to the previous survey, constrained domestic demand⁶ and government spending were ranked as the first and second most significant challenges facing businesses due to perceived slow growth in both government spending and household disposable income. The next ranked impediments to business operations are the exchange rate changes and unavailability of skilled labour, especially the difficulties encountered in recruiting foreign labour. This is also one of the areas that are highlighted among the main challenges to doing business in Botswana.*

9 Conclusion

9.1 *Overall business confidence increased from 43 percent in September 2016 to 48 percent in March 2017. Looking ahead, there is an increase in optimism, despite subdued demand in the domestic and global markets, which continues to threaten business confidence. 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 policy pronouncements as credible.*

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

TABLE 2: Results from the Business Expectations Surveys, March 2017 and September 2016
(All results are percentages and net balances, except for business conditions, which are gross balances)

	MARCH 2017			SEPTEMBER 2016		
	H1 2017	H2 2017	H2 2017- H1 2018	H2 2016	H1 2017	H1 2017- H2 2017
Output						
• Production	2.4	17.9		29.9	16.8	
• Expected level of stocks	-27.8	20.4		-8.1	-2.9	
• Volume of sales	-7.3	9.0		16.8	19.4	
• Expected volume of goods exported	2.2	-4.4		21.0	27.2	
• Expected volume of goods imported	-37.7	-24.5		-7.6	9.5	
• Employment	...	13.1	30.0	...	7.8	12.7
• Profitability	-28.8	-11.0	...	21.8	21.4	...
Input costs						
• Materials	...	79.4	93.7	...	76.0	72.0
• Rent	...	74.9	77.9	...	64.8	62.7
• Utilities	...	87.7	83.8	...	66.9	64.1
• Wages	...	73.1	83.3	...	68.0	56.6
• Transport	...	71.9	76.4	...	59.5	54.9
• Other	...	73.8	64.3	...	59.8	57.7
Investment						
• Buildings	15.1	29.3	...	19.4	21.1	...
• Plant and machinery	33.2	41.9	...	31.9	57.8	...
• Vehicles and equipment	31.1	42.2	...	40.1	50.7	...
• Other	19.1	-12.6	...	36.7	46.2	...
Expected volume of borrowing						
• Domestic	...	-4.9	-12.8	...	13.4	-2.3
• South Africa	...	8.7	7.3	...	-2.5	2.8
• Elsewhere	...	-0.1	0.1	...	-2.6	-2.6
Expected level of lending interest rates						
• Domestic	...	-11.6	-7.3	...	-12.3	3.9
• South Africa	...	1.4	8.0	...	5.8	15.0
• Elsewhere	...	-5.1	10.4	...	15.6	21.9
Business Conditions						
Rating current business conditions satisfactory						
• Overall	48	...	...	43	...	...
• Exporters	50	...	...	42	...	...
• Domestic	48	...	...	43	...	...
Optimistic about business conditions in 6 months' time						
• Overall	...	55	...	...	51	...
• Exporters	...	50	...	...	75	...
• Domestic	...	56	...	...	46	...
Optimistic about business conditions in 12 months' time						
• Overall	...	...	67	...	...	58
• Exporters	...	...	75	...	...	92
• Domestic	...	...	65	...	...	52

APPENDIX: METHODOLOGY

In processing the BES results, the following methodologies are used: The methods, as applied more generally and specifically in this Report, are discussed below. They closely follow those used by the Organisation for Economic Co-operation and Development (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, it is appropriately qualified.

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 over 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.