

## Business Expectations Survey March 2015 – 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.<sup>1</sup>

This report presents results of the survey carried out between March and April 2015<sup>2</sup> for three distinct periods: the first half of 2015 (H1-2015; i.e., the current period); the second half of 2015 (H2-2015), and the twelve-month period to June 2016 (H2:2015-H1:2016). The survey sample covers 100 businesses in agriculture, mining, manufacturing, water and electricity, construction, trade, transport, and financial and business services. For this survey, 55 percent of surveyed businesses responded, compared to 63 percent in the September 2014 survey.

### 2. Survey Context: Recent Economic Developments

Outlook for economic growth in advanced countries is improving but weak in emerging economies

The world economy experienced modest growth of 3.4 percent in 2014<sup>3</sup>, which is expected to improve, albeit marginally, to 3.5 percent and 3.8 percent in 2015 and 2016, respectively, mainly due to recovery in the advanced economies. Compared to 2014, the outlook for advanced economies is improving, but is weaker in emerging markets, reflecting slower growth forecast for some large emerging economies, notably China. Advanced economies are forecast to grow by 2.4 percent in both 2015 and 2016, up from 1.8 percent in 2014, while for emerging markets and developing economies, growth of 4.3 percent and 4.7 percent is projected for 2015 and 2016, respectively, compared to 4.6 percent in 2014. Within the region, the outlook for South Africa is for modest growth of 2 percent in 2015 and 2.1 percent in 2016, constrained, in particular, by long-term power shortages. More positively, recent sustained falls in global oil prices are expected to provide some stimulus to the global economy.

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<sup>1</sup> The Appendix at the end of this report gives more details on the methodology.

<sup>2</sup> 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.

<sup>3</sup> The forecasts for global growth are taken from the IMF’s World Economic Outlook, April 2015.

In the domestic economy, growth prospects are constrained by water usage restrictions, power supply interruptions and uncertainty regarding the strength of the global recovery. Estimates of GDP released during the survey period indicate that the economy grew by 4.4 percent in 2014, down from 9.3 percent in the previous year. This slowdown mainly reflects the weakening of the mining sector which expanded by 4.5 percent, compared to growth of 23.9 percent in the previous year. Non-mining GDP slowed down from 6.8 percent in 2013 to 4.4 percent in 2014. The Budget Speech (presented in February just prior to the commencement of the survey), forecast growth for 2015 at 4.9 percent compared to an estimate at that time of 5.2 percent in 2014. However, recent sustained falls in global oil prices and projected strengthening of global growth should provide a broad base for recovery in demand for Botswana's mineral exports, while government expenditure will provide some stimulus to the economy. At the same time, continued shortages of electricity and water will continue to be a recurring burden on both businesses and households during the survey period.

### **3. Business Confidence and Performance**

Overall confidence on current business conditions has declined, but improvement is expected in subsequent periods

Overall confidence in the prevailing business conditions (H1-2015) is at 44 percent, 8 percent lower than at the time of the September 2014 survey. This was significantly lower than the 62 percent expected for this period in the earlier survey, a clear indication that expectations have been revised downwards. Nevertheless, similar to the trend in recent surveys, the anticipated level of optimism rises for the rest of the survey period to 62 percent over the next 12 months.

Confidence among domestic-oriented businesses is 45 percent, almost unchanged from 46 percent in the previous survey. However, there has been a substantial decline in the current confidence levels of export-oriented businesses from 88 percent to 43 percent, and this falls further to only 29 percent over the rest of the year.<sup>4</sup> This signals serious worries about prospects for local exports, possibly reflecting continued concerns about the strength of the global economy; however, there is a significant rebound in confidence later in the survey period, when export volumes are expected to increase.

### **4. National Output**

Moderate expectations on economic growth

Businesses expect real GDP to grow by 4.6 percent in 2015, slightly lower than the 4.9 percent indicated in the 2015 Budget Speech. GDP is expected to increase marginally by 4.9 percent in 2016.

### **5. Capacity Utilisation, Investment, Input costs and Employment**

Subdued expectations on production and profitability levels but strong sentiments on rising cost of inputs

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<sup>4</sup> While the results must be interpreted with caution, the substantial degree of overlap among participants in the current and previous surveys indicates that this sharp decline in confidence is not attributable to different respondents from within the survey sample participating in the two surveys.

Relative to the September 2014 survey, most businesses are less positive about the demand for their products/services in the current period and the second half of 2015. Hence, businesses generally expect only marginal increases in sales volumes and the volume of goods imported during 2015. Moreover, these expectations have been significantly revised downwards compared to the previous survey, particularly for production and profitability levels. Such revisions are consistent with challenging conditions reported by businesses.

However, the survey indicates that most respondents anticipate operating at above 50 percent of their productive capacity in the current period. Thus, the current levels of capacity utilisation by businesses are broadly comparable with those in the previous survey. Moreover, in terms of investment (building, plant and machinery, vehicles and equipment and other), there has been some upward revisions in expectations in the current survey compared to the September 2014 survey, and a majority of businesses still anticipate to undertake more investment in the second half of 2015.

Sentiment amongst firms regarding rising costs of inputs is still strong, although somewhat lower than in the September 2014 survey, with the exception of utilities and wages. Unsurprisingly, expectations of higher costs rise in the second half of 2015 and first half of 2016. The overall easing of expectations of rising costs of inputs is consistent with moderating inflation expectations (section 7).

## **6. Debt, Interest Rates and Access to Finance**

Access to finance considered increasingly difficult and domestic borrowing preferred to financing from South Africa and elsewhere

In line with their capital investment plans, businesses would prefer domestic borrowing followed by international borrowing, as opposed to funding from South Africa during the second half of 2015 and the twelve-month period to June 2016. This is consistent with the anticipated lower interest rates in Botswana during 2015 and the twelve-month period to June 2016. Expectations of lower borrowing costs in the domestic market could be due to the reduction of the Bank Rate from 7.5 percent to 6.5 percent in the months prior to the survey period, together with continued low prevailing rates of inflation. Interest rate increases over the outlook period are expected for both South Africa and the international market. In terms of access to finance, 46.3 percent (September 2014: 63.8 percent) of the surveyed businesses believe access to credit is normal; 13 percent (September 2014: 12.1 percent) consider access to be easy, while 40.7 percent (September 2014: 24.1 percent) rate access to be tight. Hence, an increasing number of businesses consider access to credit to be difficult, in line with recent concerns that domestic banks are responding to reduced liquidity by tightening their lending criteria.

## **7. Inflation Outlook**

Inflation expectations remain within the Bank of Botswana inflation objective

There has been a decline in inflation expectations for 2015 to 4.8 percent from 5.8 percent in the September 2014 survey, and to 4.9 percent in 2016. The downward trend in expectations is broadly consistent with observed trends in actual inflation. Moreover, a significant proportion of respondents (89.8 percent and 81.6 percent, respectively) expect inflation to be within the Bank of Botswana's medium term inflation objective range of 3 – 6 percent in 2015 and 2016. This is broadly similar to the September 2014 survey, with the high levels of confidence that the

objective will be achieved, possibly reflecting the sustained period since mid-2013 during which inflation has been within the objective range, adding to the Bank's policy credibility.

## **8. Challenges**

Weak domestic demand, inadequately trained skilled labour and electricity shortages present major challenges

Businesses listed insufficient domestic demand, skilled labour shortages and inadequate electricity supply as the top three factors that constrained their businesses. Domestic demand was the most cited challenge by businesses due to perceived slow growth in government spending and household disposable income.<sup>5</sup> The second most cited challenge is availability of skilled labour. Both these issues have been consistently highlighted in previous survey rounds. However, respondents have now ranked electricity shortages as the third most significant challenge facing businesses, an indication of the recent deterioration in the provision of reliable and adequate power supply.

## **9. Conclusion**

Business confidence deteriorated from 52 percent in September 2014 to 44 percent in March 2015. While the survey shows increased optimism in periods ahead, this could be fragile, with continued uncertainty regarding the strength of the global recovery, modest domestic economic growth and increasing challenges in the supply of key inputs (water and electricity) posing threats to business confidence. 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.

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<sup>5</sup> 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, March 2015 and September 2014**  
**(All results are percentages and net balances except for overall business conditions, which are gross balances)**

	MARCH 2015			SEPTEMBER 2014		
	H1 2015	H2 2015	H2 2015- H1 2016	H2 2014	H1 2015	H1 2015- H2 2015
<b>Output</b>						
• Production	-10.3	-2.6		17.3	52.3	
• Expected level of stocks	16.9	-10.3		-10.5	6.7	
• Volume of sales	7.3	4.2		32.4	52.1	
• Expected volume of goods exported	4.1	-17.3		13.7	69.4	
• Expected volume of goods imported	37.0	24.4		27.6	57.7	
• Employment	...	1.5	19.5	...	6.2	16.4
• Profitability	-19.1	-14.2	...	10.8	28.7	...
<b>Input costs</b>						
• Materials	...	45.9	56.2	...	68.5	73.5
• Rent	...	45.3	65.2	...	59.4	66.3
• Utilities	...	69.2	89.5	...	58.3	80.0
• Wages	...	60.9	81.5	...	56.7	66.1
• Transport	...	13.3	50.0	...	47.2	47.4
• Other	...	43.7	51.1	...	50.3	47.7
<b>Investment</b>						
• Buildings	36.2	30.8	...	16.0	20.9	...
• Plant and machinery	50.3	64.3	...	41.2	56.0	...
• Vehicles and equipment	64.5	59.2	...	38.1	42.1	...
• Other	46.5	48.7	...	45.4	44.6	...
<b>Expected volume of borrowing</b>						
• Domestic	...	9.9	10.9	...	7.0	26.5
• South Africa	...	-15.8	-1.9	...	-10.4	10.9
• Elsewhere	...	6.0	15.9	...	-1.9	-1.6
<b>Expected level of lending interest rates</b>						
• Domestic	...	-15.8	-10.7	...	24.9	28.8
• South Africa	...	24.7	34.5	...	23.7	27.4
• Elsewhere	...	17.3	16.7	...	22.6	24.9
<b>Business Conditions</b>						
Rating current business conditions satisfactory						
• Overall	44	...	...	52	...	...
• Exporters	43	...	...	88	...	...
• Domestic	45	...	...	46	...	...
Optimistic about business conditions in 6 months' time						
• Overall	...	51	...	...	62	...
• Exporters	...	29	...	...	100	...
• Domestic	...	54	...	...	56	...
Optimistic about business conditions in 12 months' time						
• Overall	...	...	62	...	...	63
• Exporters	...	...	83	...	...	100
• Domestic	...	...	60	...	...	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, 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.*

