

Business Expectations Survey September 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.¹

This report presents results of the survey carried out between August and September 2015² for three distinct periods: the second half of 2015 (H2-2015; i.e., the current period); the first half of 2016 (H1-2016), and the twelve-month period to December 2016 (H1:2016-H2:2016). The survey sample covers 100 businesses in agriculture, mining, manufacturing, water and electricity, construction, trade, transport, and financial and business services. For this survey, 51 percent of surveyed businesses responded, compared to 55 percent in the March 2015 survey.

2. Survey Context: Recent Economic Developments

Uneven prospects for the global economy, and slower growth in the domestic economy

The world economy is projected to experience modest growth of 3.1 percent in 2015³, 0.3 percentage points lower than in 2014, and 0.2 percentage points below the forecasts in the July IMF’s World Economic Outlook. This is in line with the decline in global growth in the first half of 2015, reflecting a slowdown in emerging markets, notably China, and weaker recovery in advanced economies. However, the world economy is expected to improve, albeit marginally, to growth of 3.6 percent in 2016, mainly due to recovery in the advanced economies. Advanced economies are forecast to grow by 2 percent and 2.2 percent in 2015 and 2016, respectively, up from 1.8 percent in 2014; while, for emerging markets and developing economies, growth of 4

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 forecasts for global growth are taken from the IMF’s World Economic Outlook, October 2015.

percent and 4.5 percent is projected for 2015 and 2016, respectively, compared to 4.6 percent in 2014. Within the region, the outlook for South Africa has deteriorated, with growth of 1.4 percent forecast in 2015 and 1.3 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.

In the domestic economy, growth prospects are constrained by water usage restrictions, power supply interruptions and reduced mining output. Estimates of GDP released during the survey period indicate that the economy grew by 4.2 percent in the twelve months to June 2015, down from 6.1 percent in the previous year. This slowdown mainly reflects the weakening of the mining sector which expanded by 1.3 percent, compared to growth of 15.2 percent in the previous year. Non-mining GDP improved marginally from 4.5 percent in 2014 to 4.8 percent in 2015, but remains weak by historical standards. The Budget Strategy Paper for 2016/17 forecasts growth for 2015 at 2.6 percent compared to an earlier estimate of 4.9 percent presented in the February 2015 Budget Speech. This slowdown is underpinned by the decrease in global demand for rough diamonds. Higher growth of 4.9 percent is projected for 2016, which could be supported by the continuing sustained fall in global oil prices and projected strengthening of global growth (albeit marginal) providing support for some recovery in demand for Botswana's mineral exports. However, recurring shortages of electricity and water will continue to be a significant burden on both businesses and households. While government expenditure will continue sustaining the economy, the plans for an Economic Stimulus Programme had not been announced at the time the survey was conducted.

3. Business Confidence and Performance

Overall confidence on current business conditions remains unchanged, but improvement is expected in subsequent periods

Overall confidence in the current period (H2-2015) is 44 percent, the same as for March 2015 survey. This was significantly lower than the 51 percent projected for this period in the earlier survey, a clear indication that expectations have been revised downwards. The continued subdued level of confidence reflects recurring water shortages in the greater Gaborone area as well as power outages. Nevertheless, similar to the trend in recent surveys, the anticipated level of optimism rises for the rest of the survey period to 54 percent over the next 12 months. This is comparable with the recent Deloitte Chief Financial Officers survey for Botswana which found that, despite the diamond demand slump, businesses are more upbeat about economic growth prospects next year and beyond, than their Southern African peers.

Confidence among domestic-oriented businesses is 44 percent, slightly lower than 45 percent in the previous survey, but rising to 57 percent by the end of the survey period. Furthermore, there has been a significant decline in the confidence levels of export-oriented businesses from 43 percent in the previous survey to 33 percent in the current period. The business confidence for export-oriented firms improves to 50 percent over the next 6 months and later falls to 25 percent for the whole of 2016. Thus the overall recovery in confidence for 2016 is entirely due to some

revival in confidence by domestic oriented businesses⁴, while confidence in prospects for improvement in export markets remains weak.

4. National Output

Moderate Expectations for Economic Growth

On average, businesses expect real GDP to grow by 4.6 percent in 2015, substantially higher than the 2.6 percent indicated in the Budget Strategy Paper for 2016/17, but broadly in line with the 4.9 percent announced during the Budget Speech. However, businesses' growth forecast of an average of 4.9 percent for 2016 is in line with growth expectations stated in the Budget Strategy Paper for 2016/17.

5. Capacity Utilisation, Investment, Input costs and Employment

Positive expectations on production, profitability and employment, but strong sentiments on rising cost of inputs

The subdued levels of business confidence 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 2016. In turn, this feeds through to more positive expectations regarding production, employment and profitability, especially later in the survey period. This is consistent with the greater optimism among local businesses regarding growth prospects for 2016.

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. However, in terms of investment (building, plant and machinery, vehicles and equipment and other), there has been some downward revisions in expectations in the current survey. A majority of businesses nonetheless anticipate undertaking more investment in the first half of 2016.

Sentiment amongst businesses regarding the rising cost of inputs is still strong, and higher than in the March 2015 survey. Expectations of higher costs ease in the first half of 2016 and in the twelve-month period to December 2016, with the exception of transport. The overall easing of expectations of rising costs of inputs in the latter period of the survey is consistent with moderating inflation expectations (section 7).

⁴ This is unsurprising given the dominance among respondents of those for which the main market is Botswana.

6. Debt, Interest Rates and Access to Finance

Access to finance considered increasingly difficult while expectations on cost of borrowing is mixed

Companies expect to reduce borrowing in both domestic and international markets during the first half of 2016 and the twelve-month period to December 2016; this is particularly pronounced in the case of borrowing from South Africa. Regarding borrowing costs, there is some anticipation of lower interest rates in Botswana in the first half of 2016 before rates start to rise later in the survey period. Expectations of lower domestic interest rates could be due to the reduction of the Bank Rate from 6.5 percent to 6 percent just prior to the period when the survey was conducted, together with continued low prevailing rates of inflation. Elsewhere, signals regarding expected borrowing costs are mixed, while interest rates are expected to rise internationally.

In terms of access to finance, there is a significant increase in the proportion of businesses which believe access to credit is tight (53.1 percent compared to 40.7 percent in the March 2015 survey) with corresponding reductions in those viewing access as normal (40.8 percent from 46.3 percent) or easy (6.1 percent from 13 percent). This is in line with recent concerns that domestic banks had responded to reduced liquidity by tightening their lending criteria, although seemingly at odds with reports from the banks that there is little appetite for borrowing among domestic businesses.

7. Inflation Outlook

Inflation expectations remain within the Bank of Botswana inflation objective, but above observed levels of inflation

Businesses have revised their inflation expectations for 2015 slightly downwards to an average of 4.6 percent from 4.8 percent in the March 2015 survey and to 4.8 percent from 4.9 percent in 2016. However, despite this downward trend, the average expected level of inflation remains significantly above observed levels of inflation that, in the 10 months to October 2015 averaged 3.1 percent, and has not been as high as 4.6 percent since August 2014. However, a substantial majority of respondents expect inflation to be within the Bank of Botswana's medium term inflation objective range of 3 – 6 percent in 2015 (94 percent) and 2016 (90 percent). This is broadly similar to the March 2015 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

Water shortages and electricity outages present major challenges

Respondents have now ranked water and electricity shortages as the first and second most significant challenges, respectively, facing businesses, a clear indication of the recent deterioration in the provision of these utilities. Seemingly, the unreliable supply of water and power will continue to be a recurring burden on businesses. Government spending and domestic demand were the other factors cited as major challenges by businesses due to perceived slow growth in government spending and household disposable income. Although the concerns over inadequate skilled labour and the associated challenge of securing work permits are currently overshadowed by these other problems, they are still ranked by respondents as major constraints for doing business.

9. Conclusion

The business confidence of September 2015 survey, at 44 percent, remains the same as for the March 2015 survey. Looking ahead, there is some increase in optimism, albeit tentative due to challenges in the supply of key utilities (water and electricity), while the anticipated decrease in demand for diamonds in the global market continues to threaten business confidence. The latest GDP projections (Budget Strategy Paper 2016/17 published in October 2015) indicate a decline in the growth rate of the domestic economy compared to earlier projections (Budget Speech published in February 2015). However, 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.

TABLE 1: Results From the Business Expectations Surveys, September 2015 and March 2015
(All results are percentages and net balances except for overall business conditions, which are gross balances)

	SEPTEMBER 2015			MARCH 2015		
	H2 2015	H1 2016	H1 2016- H2 2016	H1 2015	H2 2015	H2 2015- H1 2016
Output						
• Production	31.3	48.9		-10.3	-2.6	
• Expected level of stocks	7.3	8.9		16.9	-10.3	
• Volume of sales	49.7	54.9		7.3	4.2	
• Expected volume of goods exported	30.8	26.6		4.1	-17.3	
• Expected volume of goods imported	41.0	45.7		37.0	24.4	
• Employment	...	31.7	37.6	...	1.5	19.5
• Profitability	1.7	37.4	...	-19.1	-14.2	...
Input costs						
• Materials	...	75.7	75.5	...	45.9	56.2
• Rent	...	68.5	33.4	...	45.3	65.2
• Utilities	...	78.0	70.9	...	69.2	89.5
• Wages	...	72.3	58.2	...	60.9	81.5
• Transport	...	31.3	68.9	...	13.3	50.0
• Other	...	64.3	64.2	...	43.7	51.1
Investment						
• Buildings	14.6	53.9	...	36.2	30.8	...
• Plant and machinery	60.8	59.6	...	50.3	64.3	...
• Vehicles and equipment	35.0	62.5	...	64.5	59.2	...
• Other	28.4	57.3	...	46.5	48.7	...
Expected volume of borrowing						
• Domestic	...	-32.7	-35.8	...	9.9	10.9
• South Africa	...	-43.7	-36.9	...	-15.8	-1.9
• Elsewhere	...	-5.4	-4.1	...	6.0	15.9
Expected level of lending interest rates						
• Domestic	...	-26.9	9.5	...	-15.8	-10.7
• South Africa	...	7.7	-23.4	...	24.7	34.5
• Elsewhere	...	14.1	20.2	...	17.3	16.7
Business Conditions						
Rating current business conditions satisfactory						
• Overall	44	...	...	44	...	...
• Exporters	33	...	...	43	...	...
• Domestic	44	...	...	45	...	...
Optimistic about business conditions in 6 months' time						
• Overall	...	45	...	...	51	...
• Exporters	...	50	...	...	29	...
• Domestic	...	45	...	...	54	...
Optimistic about business conditions in 12 months' time						
• Overall	...	...	54	...	...	62
• Exporters	...	...	25	...	...	83
• Domestic	...	...	57	...	...	60

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.