

THE QUARTERLY BUSINESS EXPECTATIONS SURVEY



MARCH 2020

BANK OF BOTSWANA

1. Introduction

Description of the Survey

- 1.1 The Bank's quarterly Business Expectations Survey (BES) collects information on the domestic business community's perceptions about the prevailing state of the economy and prospects. In the survey, businesses respond to a range of questions relating to, among others: the prevailing business climate; outlook for economic growth and inflation; and business performance over the survey horizon. The survey horizon comprises the quarter in which the survey is conducted, also referred to as the current period, the subsequent quarter and the next twelve months.
- 1.2 This Report presents results of the survey carried out in the first quarter of 2020, covering the first quarter of 2020 (Q1:2020 - the current period); the second quarter of 2020 (Q2:2020); and the twelve-month period (M12) from April 2020 - March 2021 (Q2:2020-Q1:2021). Thus, the Survey was conducted at the time when the coronavirus (Covid-19) that was first reported in Wuhan (China) began to spread rapidly across the globe and was later declared a pandemic by the World Health Organisation (WHO). The BES samples 100 businesses from eight economic sectors, namely: agriculture; mining; manufacturing; water and electricity; construction; trade, hotels and restaurants; transport and communications; and finance and business services. The response rate for the current survey is 77 percent, down from 82 percent recorded in the December 2019 survey. The lower response was mainly due to tight schedules of companies occasioned by the imminent lockdown warranted by the need to control the spread of Covid-19 in Botswana. Responding to the survey was therefore, not considered a priority as companies prepared for the lockdown.
- 1.3 The survey questions focus mainly on anticipated direction of change in selected indicators: i.e., whether conditions will improve, worsen or remain unchanged. The results are then consolidated into an overall measure called 'net balance'. This measure is obtained by summing the positive and negative responses to each question/element by firms belonging to the same sector, which are then weighted by the sector's contribution to nominal gross domestic product (GDP). Thus, by design, the survey responses are predominantly qualitative, yet they provide valuable information to facilitate analysis and inform policy decisions. However, responses to questions relating to GDP growth and inflation are quantitative and are consolidated into simple averages.

Highlights of the Survey Results

- 1.4 The results suggest that firms were less optimistic about economic activity in the first quarter of 2020, compared to the fourth quarter of 2019. Overall, businesses expected a decrease in exports and imports of goods and services; production; sales; stocks; profitability; and investment in buildings, vehicles and equipment in the first quarter of 2020. However, firms intended to increase investment in plant and machinery in the second quarter of 2020, despite anticipating tight access to credit in the domestic market. Meanwhile, firms expected cost pressure to fall significantly in the second quarter of 2020, mainly reflecting the anticipated downward pressure on costs of materials, utilities, wages and transport. Firms also expected inflation to remain stable and within the Bank's medium-term objective range of 3 - 6 percent, for both 2020 and 2021.

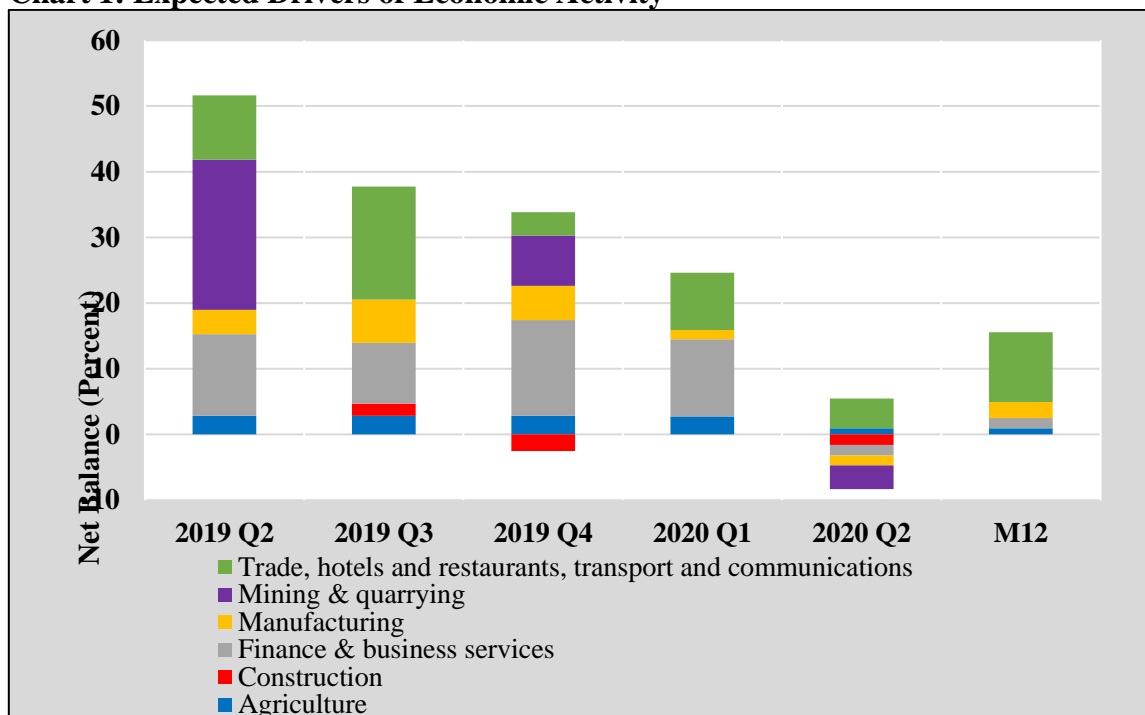
2. Economic Performance and Business Conditions

Economic Growth is expected to remain unchanged in 2020 compared to 2019

- 2.1 Firms expected overall output of the domestic economy to grow by 3 percent in 2020, the same as the growth rate reported by Statistics Botswana for 2019. On a quarterly basis, firms expected a decline in economic performance in the first quarter of 2020, compared to the fourth quarter of 2019, consistent with their expectation of: a decline in exports and imports of goods and services; production; sales; stocks/inventories; profitability; and investment in buildings, vehicles and equipment; and ‘other’ investments¹.
- 2.2 Overall, firms expected the economy to have grown by 1.4 percent in the first quarter of 2020, lower than 1.6 percent growth reported by Statistics Botswana for the previous quarter. These developments were influenced by the mining and quarrying sector’s perceptions of unchanged economic growth between the final and first quarter of 2019 and 2020, respectively (Chart1). Further, even though firms in the remaining sectors expected the economy to post a positive rate of growth in the first quarter of 2020, they were less optimistic than in the previous one. Businesses in the trade, hotels and restaurants and the transport and communications sectors were, however, more optimistic. Construction firms, on the other hand, expected economic growth to remain unchanged between the fourth quarter of 2019 and first quarter 2020. Most business sectors expect the economy to contract in the second quarter of 2020, followed by a recovery over the entire year.
- 2.3 Notably, the mining and quarrying sector, which predominantly targets the export market, is less optimistic about economic growth prospects over the survey horizon, This is consistent with the unfavourable market conditions, especially with respect to the diamond industry, occasioned by, among others, weaker global demand for rough diamonds associated with the US-China trade war and the interruption of trading due to the outbreak of the Coronavirus pandemic.

¹ ‘Other investments’ refers to any investments apart from the ones listed.

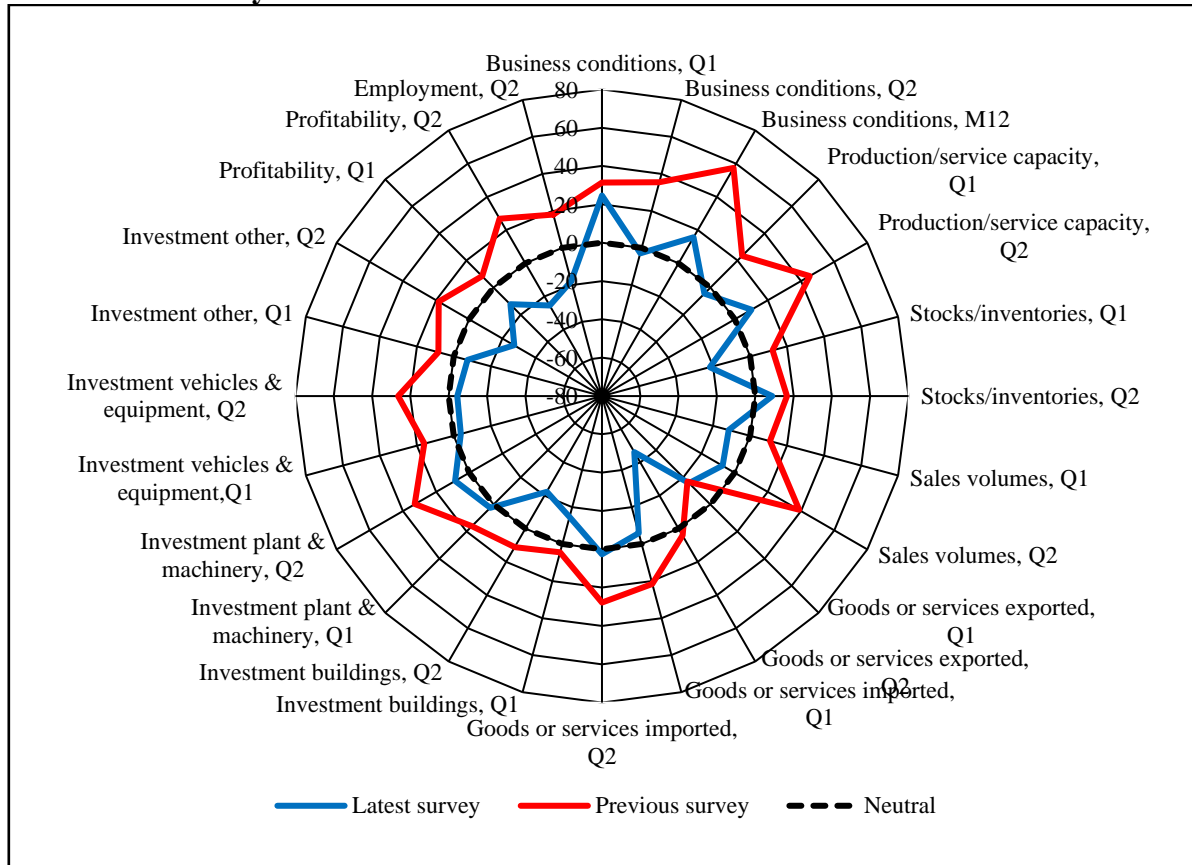
Chart 1: Expected Drivers of Economic Activity



Note: The chart shows net balances on each sector's expectations about economic performance from the second quarter of 2019 to the second quarter of 2020 and the 12 months period to March 2021. The net balances are weighted by each sector's relative share in GDP. For example, for a sector with (P+N) members in the sample, of which 'P' indicated positive perceptions and 'N' negative, with a weight of Z percent in nominal GDP, the weighted net balance is calculated as $[(P-N)/P+N] \times 100 \times Z$.

2.4 Firms expect business conditions to deteriorate in the first two quarters of 2020. However, business conditions are expected to improve in the twelve-month period to March 2021 (Chart 2). Firms expect sales; profitability; exports of goods and services; investment in vehicles and equipment, investment in buildings, as well as 'other' investments to decline in both the first and second quarters of 2020. This is apart from imports of goods and services which are only expected to decline in the first quarter of 2020 and remain constant in the second quarter and, investment in plant and machinery that is expected to rise in the second quarter of 2020. Employment, which is only recorded for the second quarter, is expected to decline in the current survey. The expected deterioration in business confidence during the first half of 2020, is consistent with the perceptions of weaker overall economic growth in the first quarter of 2020, and the overall contraction expected in the second quarter. The perceived generally weaker economic performance in the current survey compared to the previous one could be associated with the disruption of business operations following the outbreak of the Covid-19 pandemic.

Chart 2: Summary of Economic Conditions

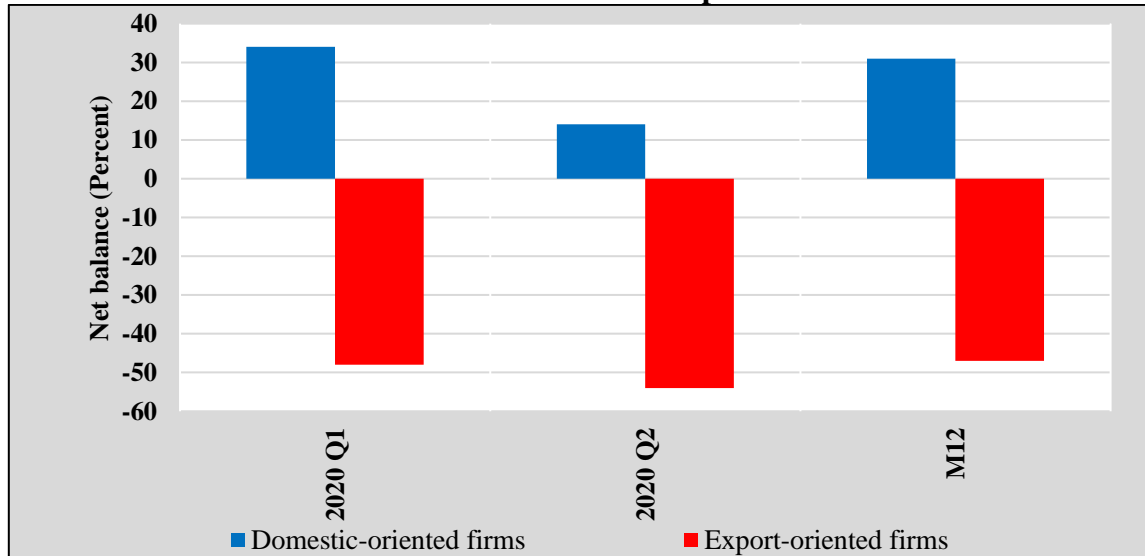


Notes: The chart summarises firms’ expectations about business conditions. The blue line represents the results of the March 2020 Survey while the red line represents the results of the December 2019 survey. The black dashed line is the static position, representing unchanged expectations. The net balances of how respondents view economic conditions are plotted along the slanted lines extending from the centre of the chart. Values moving further away from the ‘static’ line show an improvement, whereas those moving towards the centre of the chart represent a deterioration.

The results of the current survey, along the blue line, are interpreted as follows: Q1 denotes perceptions about business conditions in the first quarter of 2020, Q2 represents expectations about business conditions for the second quarter of 2020, while M12 depicts the perceived business conditions for the twelve-month period from April 2020 to March 2021. Similarly, the red line denotes perceptions about business conditions as envisaged in the previous survey.

2.5 As reflected in Chart 3, optimism of the domestic market-oriented firms declines for the second quarter of 2020, compared to the first quarter, but improves in the twelve-month period to March 2021 (M12), although remaining below the level recorded in the first quarter of 2020. The perceived improvement in optimism is in line with the anticipated universal economic recovery in 2021 by the International Monetary Fund. Confidence in the domestic market-oriented firms is mainly driven by the trade, hotels and restaurants, transport and communications sectors. However, export market-oriented firms are pessimistic about business conditions throughout the survey horizon. This is because export market-oriented firms are predominantly in the mining and quarrying sector which, as indicated earlier, expect a general stagnation in overall output in the next 12-month period.

Chart 3: Business Confidence for Domestic and Export Markets-Oriented Firms



3. Expected Lending Rates and Volume of Borrowing

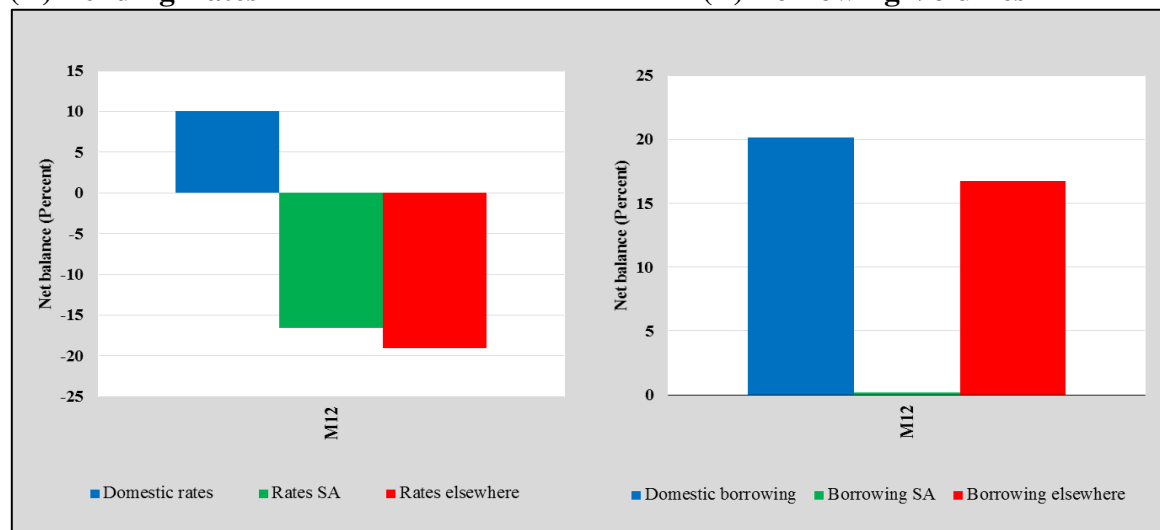
Domestic lending rates and borrowing volume are expected to rise in the year to March 2021

- 3.1 Firms expect the lending rates and the volume of borrowing from the domestic market to increase in the twelve-month period to March 2021 (Chart 4). Lending rates in the rest of the markets are expected to decline, while borrowing from elsewhere² is expected to rise sizeably and negligibly in South Africa.

Chart 4: Lending Rates and Borrowing Volumes

(A) Lending Rates

(B) Borrowing Volumes

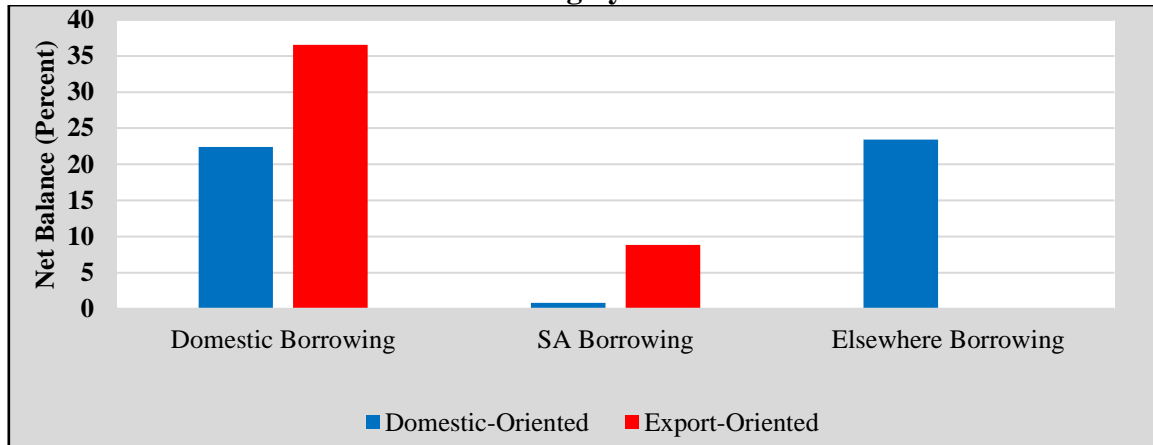


- 3.2 Firms in the domestic market perceived access to credit to be tight in the first quarter of 2020, mainly because they consider the domestic interest rates to be high. Meanwhile, export-market oriented firms perceived access to credit to be normal, and the interest rates to have remained unchanged in the review period. Some firms, especially those targeting the domestic market, prefer to borrow from both the domestic market and elsewhere (other

² 'Elsewhere' refers to any market other than Botswana and South Africa.

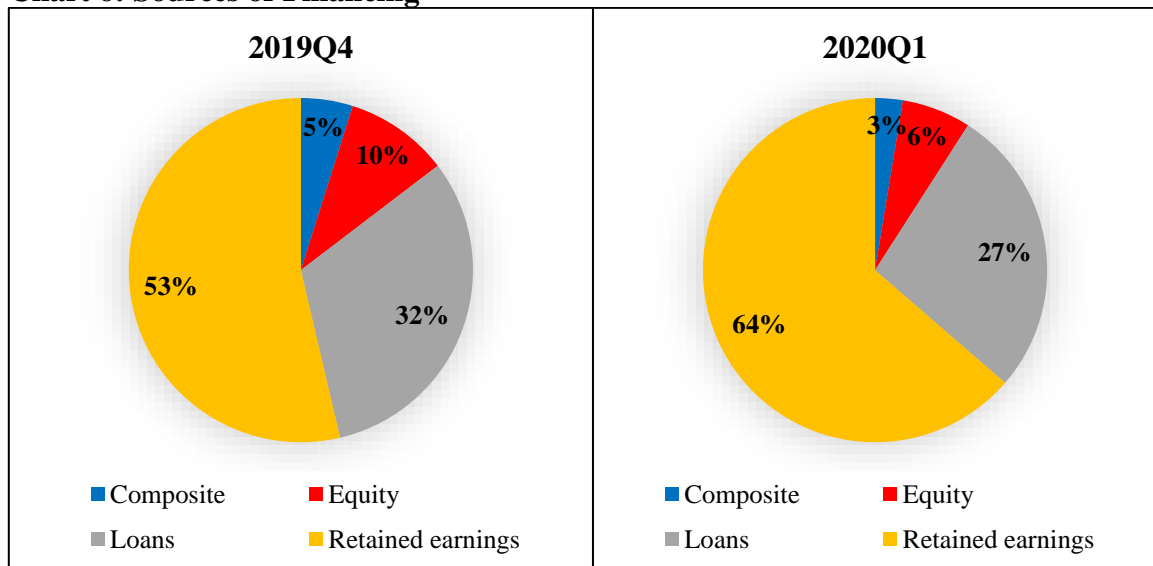
than South Africa market) in 2020. Conversely, export-oriented firms prefer to borrow from both the domestic and South African markets (Chart 5), while they have no plans to borrow from elsewhere.

Chart 5: Preferred Market for Borrowing by Firms



3.3 About 73 percent of the surveyed firms cited accessibility and affordability of their required loan products as the basis for their decisions to borrow locally or from abroad. Meanwhile, 22 percent of businesses indicated that their plans to borrow either from domestic or foreign markets are influenced by availability of suitable credit facilities. As in the previous survey, most firms preferred to finance their business operations mainly from retained earnings and loans, rather than using a combination of retained earnings and loans or equity (Chart 6). Retained earnings as a source of finance is more prevalent among the manufacturing, and trade, hotels and restaurants and the transport and communications sectors. Conversely, most of the firms in the finance and business services sector plan to fund their businesses through borrowing.

Chart 6: Sources of Financing



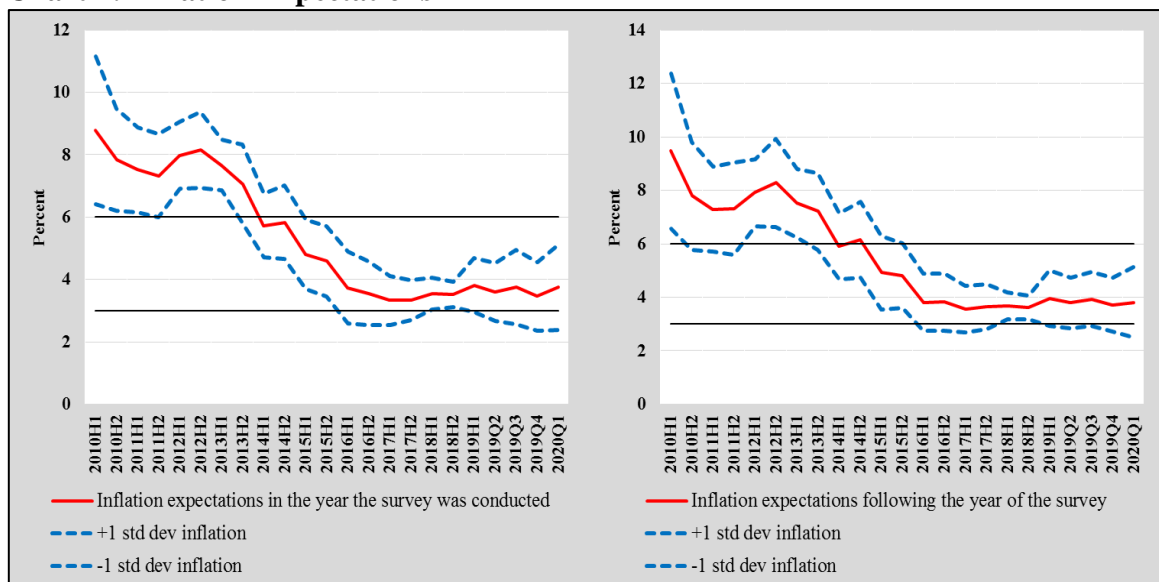
Note: Composite refers to a preference for a combination of more than one source of financing (e.g., retained earnings and loans).

4. Price Developments and Inflation

Cost pressures expected to decrease in the second quarter of 2020

- 4.1 Overall, firms expect cost pressures to be subdued in the second quarter of 2020, mainly attributable to the expected downward pressure on cost of materials, utilities tariffs, wages and other inputs to production. This is despite the rise in public sector wages in April 2020, that has potential to exert upward pressure on private sector wages. Firms' expectations about domestic inflation have generally been on a downward trend since 2013, and within the Bank's inflation objective range of 3 - 6 percent since 2014 (Chart 7). Furthermore, uncertainty about future inflation has generally declined as shown by the narrowing standard deviation (std dev) from the average expected inflation despite the noticeable divergence in the past five surveys. Firms' inflation expectations for both 2020 and 2021 average 3.8 percent, suggesting that inflation expectations are well anchored within the Bank's objective range.

Chart 7: Inflation Expectations



Note: The chart shows the average of inflation expectations across different surveys, as well as the standard deviation for the inflation expectations. Previously, the surveys were conducted biannually, but effective 2019 Q2, surveys are conducted on a quarterly basis. The bi-annual survey horizons comprised the half-year in which the survey was conducted/current period (H1) and the next half-year (H2).

5. Factors Affecting Business Conditions

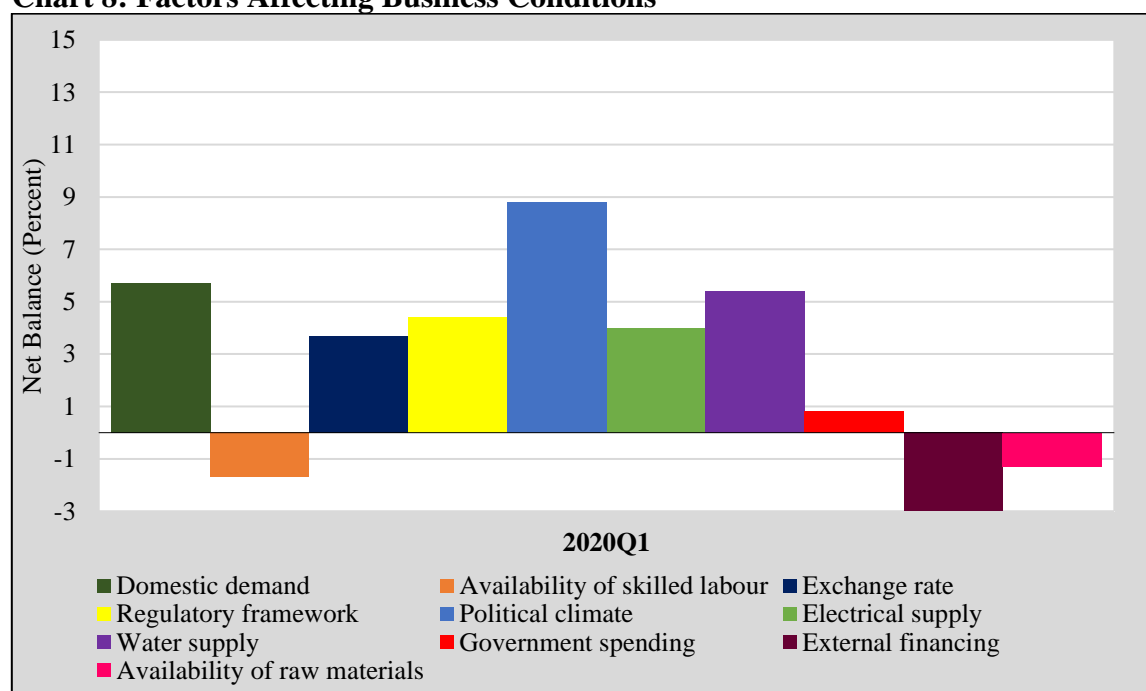
Lack of external financing is perceived to be a major challenge to doing business

- 5.1 A number of firms, particularly in the manufacturing, finance and business services, trade, hotels, restaurants, transport and communications sectors³, mentioned the difficulty in accessing financing from abroad as the greatest challenge to their business operations in the first quarter of 2020 (Chart 8). The second major business impediment cited is unavailability of skilled labour and this is predominant in the manufacturing and construction sectors, reflecting reported difficulties experienced in recruiting foreign skilled labour. Furthermore, a number of firms (predominantly in the manufacturing

³ The Trade, Hotels and Restaurants, and Transport and Communications Sectors are merged for ease of analysis since the two are interconnected.

sector) quoted shortage of raw materials as the greatest challenge to their business operations. On the positive side, the local political climate, domestic demand and the current regulatory framework are viewed as being the most supportive factors to doing business in Botswana (Chart 8). Another observation is that water and electricity sub-sectors contribute positively to economic activity, reflecting an improvement in the supply of these utilities which had previously been a serious challenge. This improvement is due to the ongoing efforts to upgrade the utility supplies through measures such as the implementation of the North-South Carrier 2 water project and the North-West Transmission Grid electricity connection. The two projects are conducted in stages, hence areas in the completed segments are already benefiting from improved utility supplies due to the projects.

Chart 8: Factors Affecting Business Conditions



6. Conclusion

6.1 Overall, firms were less optimistic about business conditions in the first quarter of 2020, compared to the previous quarter. Furthermore, business conditions are expected to deteriorate in the rest of the survey horizon, consistent with the anticipated decline in sales; profitability; exports of goods and services; employment; investment in vehicles and equipment, and ‘other investments’. The expected weakening of the business conditions is in line with the global economic hardships associated with the outbreak of the Covid-19 pandemic. Firms expect the economy to grow by 3 percent in 2020. Overall, firms expect average inflation to rise slightly to an average of 3.8 percent in both 2020 and 2021, while the Bank projects that inflation will remain below the 3 percent lower bound of the inflation objective in 2020 and revert to within the objective range in the first quarter of 2022.