



BANK Of ZAMBIA

**QUARTERLY SURVEY OF BUSINESS
OPINIONS AND EXPECTATIONS
REPORT**

First Quarter 2017, Vol 1.1

Disclaimer:

The opinions and expectations presented herein are of the respondents and not of the Bank of Zambia.

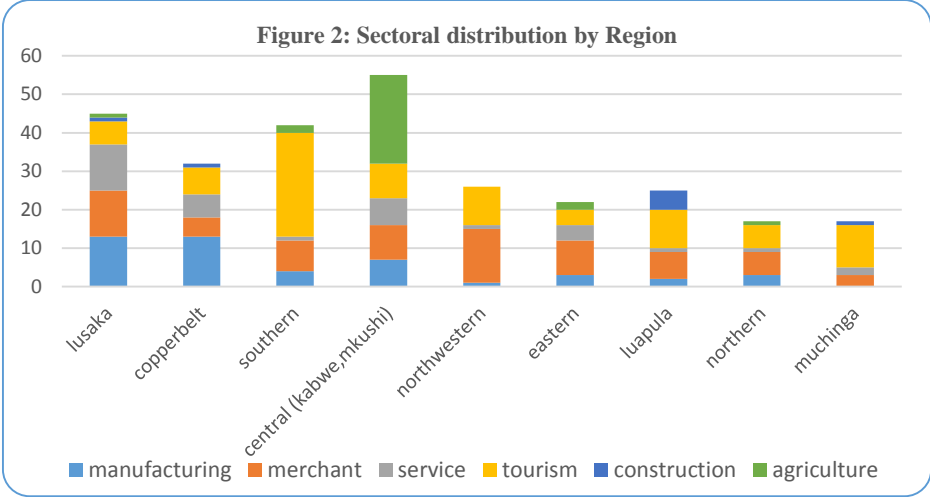
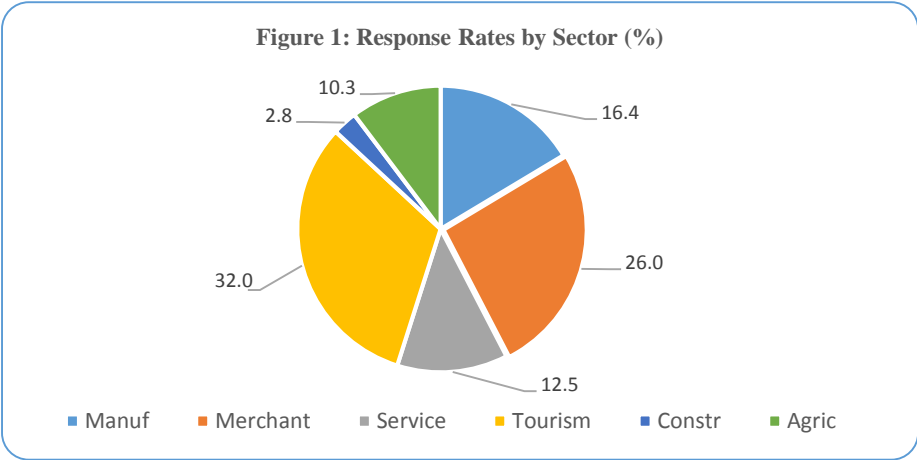
APRIL 2017

PREFACE

Business surveys provide useful indicators of current and future economic activity and assist in the formulation of decisions today that impact on future economic performance.

The Quarterly Survey of Business Opinion and Expectations (QSBOE) undertaken by the Bank of Zambia is designed as a supplementary tool to provide information on the business community’s opinions and expectations about the current and future direction of the economy for macroeconomic analysis. Business opinions and expectations provide a guide to likely developments because of the dominant role expectations play in shaping economic behavior.

This Report is based on the results of the QSBOE conducted from March - April 2017. Out of the 311 questionnaires distributed, 281 firms responded, representing a response rate of 90.4%.



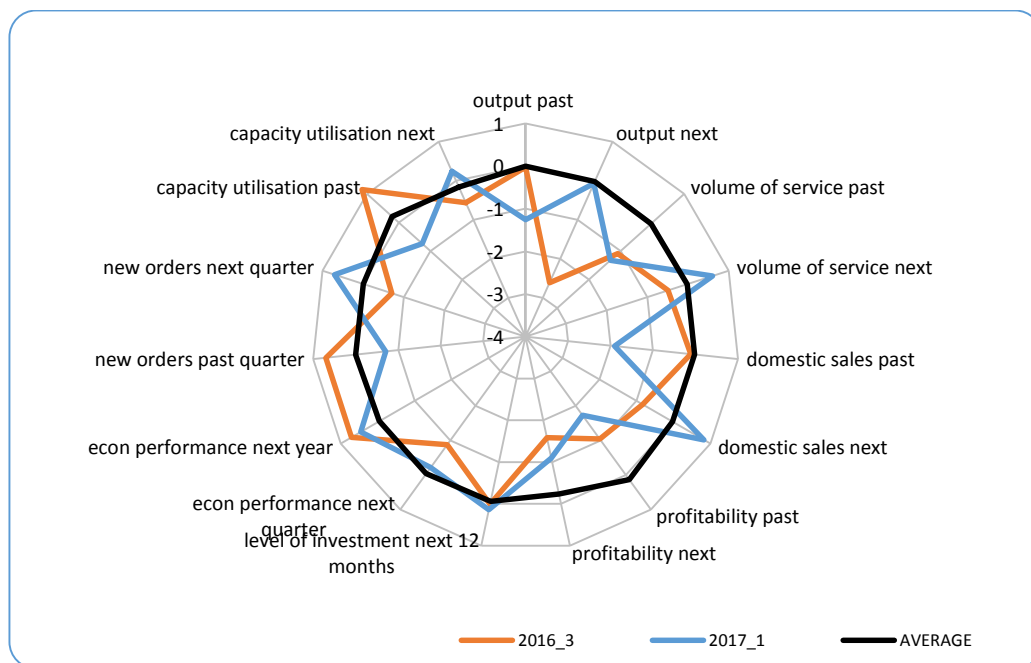
Executive Summary¹

Results of the first quarter 2017, Business Opinions and Expectations Survey indicate that economic activity weakened further. Businesses reported lower output and capacity utilisation mainly on account of continued electricity load shedding, the impact of the fuel price increase during the fourth quarter 2016 and subdued demand. The volume of services, particularly in the tourism sector also decreased due to the period of low seasonal demand. Subsequently domestic sales and profitability deteriorated.

This notwithstanding, firms anticipate an increase in output, volume of services and domestic sales during the second quarter, 2017. The prospects of a bumper agricultural harvest, onset of the high tourism season (May- October) and stability in the exchange rate, support this sentiment. Further, economic performance is expected to rebound above the historical average over the next twelve months.

With regard to monetary policy, most firms foresee a moderation in inflationary pressures. Although inflationary pressures are expected from cost-push factors following the rise in electricity tariffs, the pass-through from exchange rate stability, seasonal increase in food supply and subdued demand are expected to moderate these pressures. Credit conditions, however, are likely to be tight, while interest rates remain high.

Overall Survey Response Patterns*



*Note: The survey indicators are standardized net balances with mean=0 and standard deviation=1. A value within the black circle entails weaker economic conditions than historical average and a value outside the black line is better than historical average

¹ This Report presents findings of the Quarterly Survey of Business Opinions and Expectations conducted during the first quarter of 2017. Previously this Survey was conducted bi-annually. The results are based on responses from 281 firms covering manufacturing, merchants, tourism and services, agriculture and construction sectors, thus representing a response rate of 90.4%.

Introduction

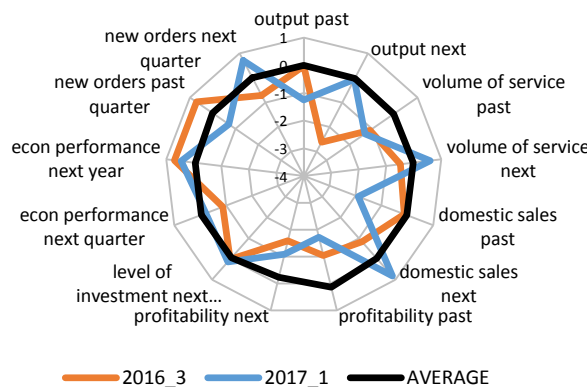
This Business Opinions and Expectations Survey Report is divided into four sections. The first section presents the response patterns related to economic performance during the first quarter of 2017 and expectations for the second quarter, while section II presents opinions and expectations on input costs, wages and selling prices. Section III provides perceptions on monetary policy for the second quarter and section IV provides the general conclusion.

I. Opinions and Expectations of Economic Activity

Economic Activity deteriorated...

The overall response pattern from the survey for the first quarter of 2017, showed that economic activity weakened and remained below the historical average (see Chart 1). Output, capacity utilization, the volume of services, domestic sales, and profitability were lower than the previous quarter. Firms, however, expect economic performance to improve during the second quarter, after two consecutive quarters of weak performance and to rebound above the historical average level over the next twelve months.

Chart 1: Business Opinions & Expectations Survey Response Patterns*



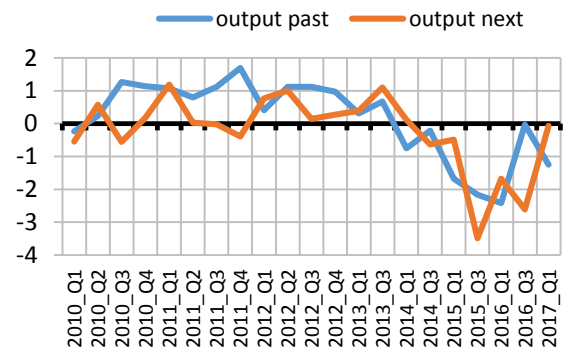
*Note: The survey indicators are standardized net balances with mean=0 and standard deviation=1. A value within the black circle entails weaker economic conditions than historical average and a value outside the black line is better than historical average.

Output declined in Q1 2017...
(net balance -20%, Q3 2016 -2.8%)

During the first quarter of 2017, overall output fell mainly due to lower productivity in the agriculture and manufacturing sectors (see Chart 2). This was also reflected in the decline in capacity utilisation, largely attributed to continued electricity load shedding and subdued demand.

Respondents were however, optimistic that output would improve during the second quarter of 2017, driven mainly by prospects of a bumper harvest in the agriculture sector, an increase in tourist arrivals with the start of the high season (May –October), as well as recovery in the manufacturing sector.

Chart 2: Opinion on Output

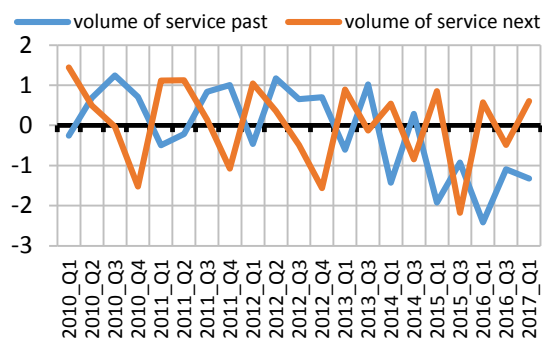


Volume of Service reduced...
(net balance -28.2, Q3 2016 -24.2%)

The balance of opinions showed a decrease in the volume of services during the first quarter of 2017, mainly attributed to low seasonal demand in tourism as well as high cost of doing business (see Chart 3).

Firms, anticipate an increase in the volume of services during the second quarter, with a net balance of 28.7% compared to 12.3% in the fourth quarter of 2016. This is mainly on account of the expected rise in tourist arrivals and improvement in banking activities following the easing in monetary policy.

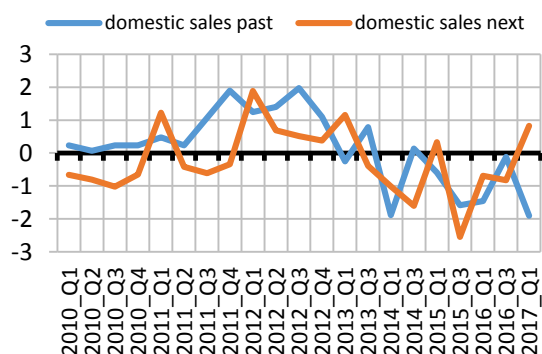
Chart 3: Volume of Service



Domestic Sales deteriorated...
(net balance -35.6%, Q3 2016 -5.7)

Most businesses experienced a decline in domestic sales during the first quarter, mainly due to subdued demand for manufactured and agricultural products. In addition, this period was low season for tourism activity.

Chart 4: Domestic Sales



However, businesses were optimistic that domestic sales would rise above the average historical levels in the second quarter 2017 (see Chart 4) as reflected in a net balance of 27.4% against 5.1% in the previous quarter. This sentiment was mainly based on the anticipated bumper harvest and commencement of the agriculture marketing season, prospects of higher tourist arrivals and an increase in new orders for manufactured goods.

Employment² unchanged...

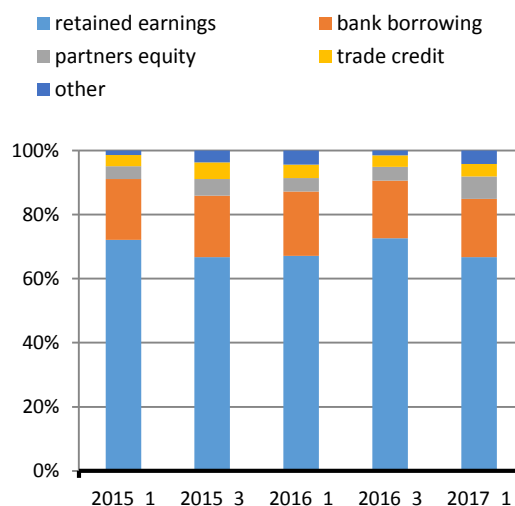
Most businesses (73.5%) reported no change in labour demand during the first quarter 2017. However, 15.4% of respondents reported a decrease in labour demand, while 11.0% reported an increase.

During the second quarter 2017, demand for labour is generally expected to remain unchanged as reported by 71.7% of respondents. 18.1% of firms anticipate a rise in demand for labour, particularly in the agriculture sector, while 10.2% of firms expect a decrease in labour.

Retained earnings main source of financing...

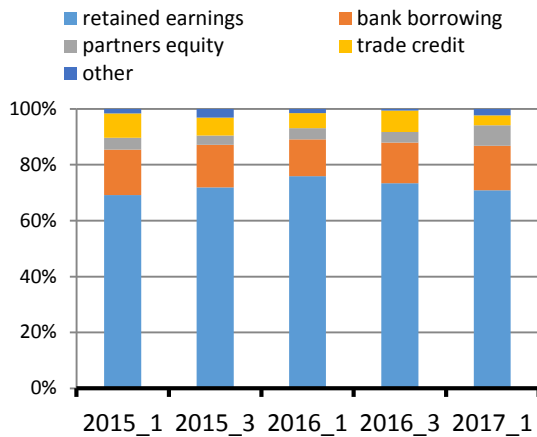
Investment finance and working capital were mainly supported by firms' retained earnings as indicated by 66.7% and 70.9% of respondents compared to 72.6% and 73.4%, respectively. Commercial bank borrowing was reported by 18.2% (17.9%) for investment finance and 15.9% (14.9%) for working capital.

Chat 5A: Sources of Investment Finance



² Employment question was asked for the first time so net balance could not be computed.

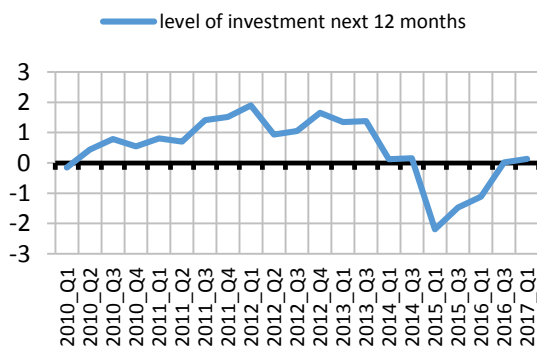
Chart 5B: Sources of Working Capital



Investment to rise in next twelve months...
(net balance 20.2%, Q3 2016 19.1%)

Over the next 12 months, investment spending is expected to improve, and revert to historical levels (see Chart 6), as expansion works are completed in some manufacturing firms. This expectation is supported by Governments growth policies to encourage diversification of the economy as stated in the Budget.

Chart 6: Investment plans in next 12 months

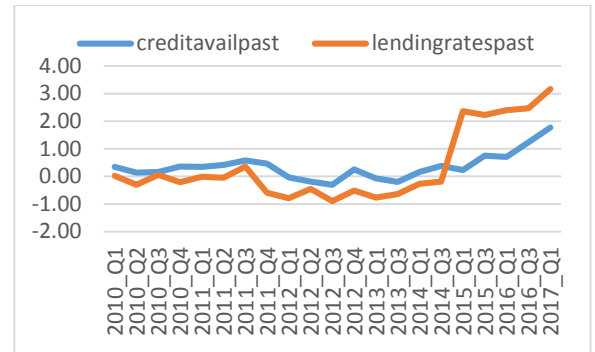


Credit conditions tightened

(net balance 77.7%, Q3 2016 73.2%)

Conditions in the credit market remained tight during the first quarter of 2017, (see Chart 7). High interest rates and collateral requirements by lending institutions were cited as the main contributing factors to the failure to access credit.

Chart 7: Credit conditions and lending rates



II Evolution of Costs, Wages and Prices

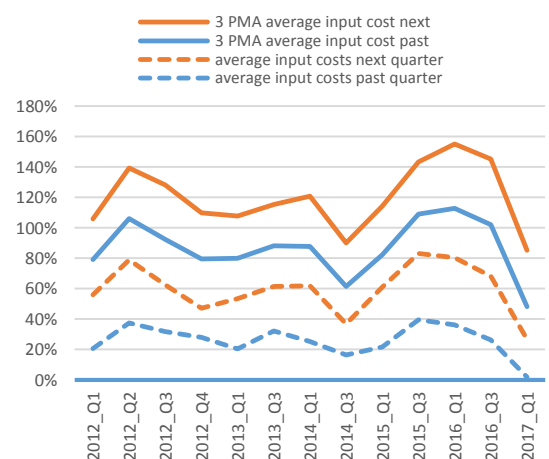
Input Costs still high...

(net balance 1.9%, Q3 2016 26.3%)

Most Respondents indicated that average input costs increased although the proportion of firms was lower when compared to the previous quarter. This was attributed to the impact of the fuel price increase in the fourth quarter of 2016, continued load shedding and high cost of agriculture inputs i.e. fertiliser, and army worm chemicals.

During the second quarter, firms expect input costs to moderate, despite the implementation of higher electricity tariffs, as reflected in the net balance of 24.8% (41.8%).

Chart 8: Average input costs

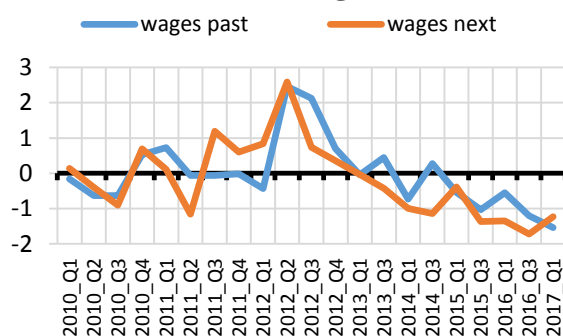


Wages increased...
(net balance 4.8%, Q3 2016 7.3%)

The balance of responses showed a rise in wages during the first quarter of 2017, mainly due to implementation of annual wage increments and higher cost of living, although wages remained below the historical average level.

Wage are expected to rise slightly in the second quarter (see Chart 9) with the increase in seasonal labour demand, particularly during the agriculture harvest period. This was indicated by a net balance of 13.8% compared with 9.4% in the fourth quarter 2016.

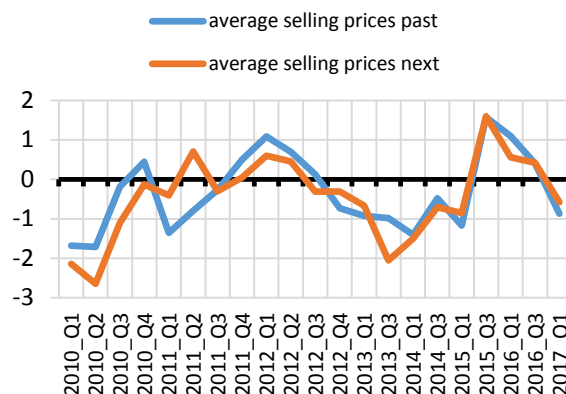
Chart 9: Evolution of wages



Selling Prices declined...
(net balance -15.1%, Q3 2016 8.6%)

Average selling prices decreased in the first quarter of 2017 (see Chart 10), largely attributed to stiff competition, low demand as well as accumulated stocks of maize and its products due to the ban on their exports. This trend is expected to continue in the second quarter of 2017, as reflected in the net balance of -1.5% compared to 17.5% in the fourth quarter 2016.

Chart 10: Evolution of average selling prices

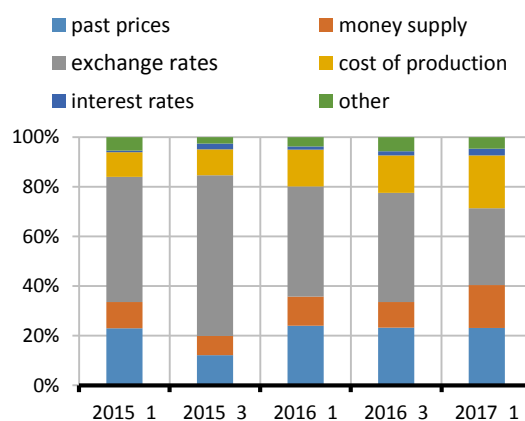


III Expectations on Monetary Policy for Second quarter

Inflationary pressures to moderate...
(net balance 18.5%, Q3 2016 54.0%)

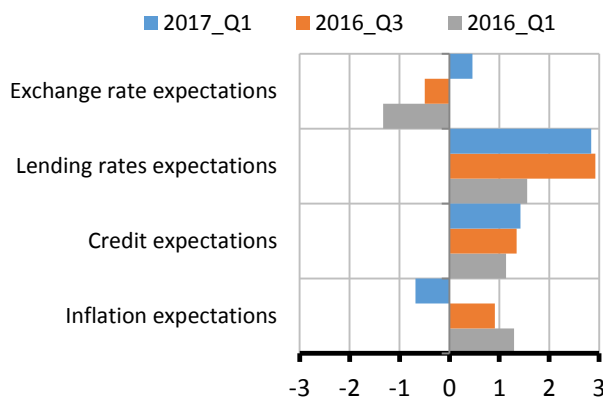
Although inflationary pressures are expected from cost-push factors following the rise in electricity tariffs, the pass-through from exchange rate stability, coupled with subdued demand are expected to moderate these pressures (see Charts 11 & 12).

Chart 11: Inflation expectations less driven by exchange rate pass-through effects and more by cost of production and money supply



31% (44.1%) of respondents indicated inflationary expectations driven by the exchange rate, 23.1% (23.2%) by past prices, and 21.2% (15.0%) by the cost of production, and 17.3% (10.3%) by money supply.

Chart 12: Expectations of lower inflation, stronger exchange rate, tight credit and high interest rates

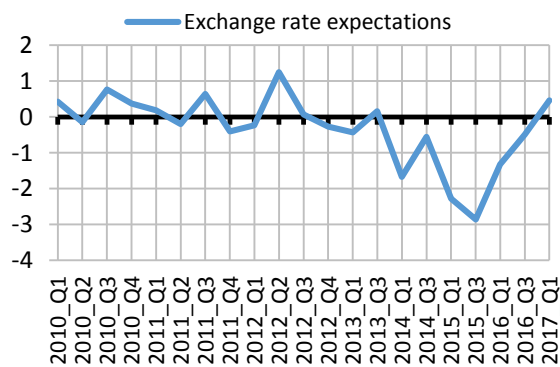


Kwacha Exchange rate against US dollar to strengthen ...

(net balance -1.2%, Q3 2016 -26.7%)

In the second quarter of 2017, the Kwacha exchange rate against the US dollar is expected to strengthen. This sentiment is premised on prospects of the recovery in copper exports due to higher global prices and the improvement in investor confidence particularly after an IMF programme is adopted (see Chart 14).

Chart 13: Exchange rate expectations next quarter



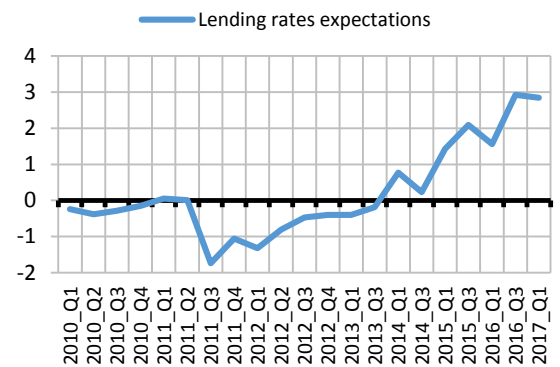
Interest Rates to remain high

(net balance 81.7%, Q3 2016 83.8%)

Commercial bank lending rates are expected to remain high and above the historical average, though declining marginally in the second quarter of 2017 (see Chart 12). This is

attributed to Government crowding out effect and the lagged response to the easing in monetary policy (following reduction in BoZ policy rate and SRR in February 2016).

Chart 14: Interest rate expectations next quarter



IV Conclusion

The Business Opinion Survey for the first quarter of 2017 revealed that economic activity deteriorated during the first quarter of 2017, and remained below the historical average. This was reflected in lower overall output and capacity utilisation which was a result of the depressed economy. In addition, the volume of services and domestic sales deteriorated mainly due to low seasonal demand in tourism and low disposable income. Subsequently, profitability declined as well.

Respondents were more optimistic about economic performance in the second quarter, with output, domestic sales and profitability generally expected to improve. This sentiment was supported by the anticipated agricultural bumper harvest and higher activity in the tourism, manufacturing and banking sectors.

On the monetary policy front, although inflationary pressures were expected from cost-push factors following the implementation of higher electricity tariffs, the stability in the Kwacha exchange rate against the US dollar, and subdued demand would moderate these pressures. The outlook

on the strengthening of the Kwacha exchange rate against the US dollar was based on the rebound in global commodity prices which is expected to boost export earnings and investor confidence, particularly once the country adopts an IMF programme. Respondents, however, foresee tight credit conditions due to high interest rates and collateral requirements by lending institutions.

Appendix I: Background on the QSBOE

This Report is based on the results of the QSBOE conducted from March - April 2017. Out of the 311 questionnaires distributed, 281 firms responded, representing a response rate of 90.4%. Of the 281 respondents, 32.0% were from tourism, merchants (26.0%), manufacturing (16.4%), services (12.5%), agriculture (10.3%) and construction (2.8%).

Survey Methodology

Data collection for the Quarterly Survey of Business Opinion and Expectations is done by means of a questionnaire which is designed to capture information on economic performance, sources of finance, and operational constraints for the current quarter, as well as expectations for the following quarter and the following twelve months. The questionnaire is administered to a sample of respondents in manufacturing, trading, tourism and services, construction and agriculture sectors. The sectors covered were selected on the basis of their contribution to GDP.

The Survey covers the Copperbelt towns of Luanshya, Ndola, Kitwe and Chingola, Southern (Mazabuka, Choma, Kalomo and Livingstone), Central (Chisamba, Kabwe and Mkushi Farming Block), Eastern (Petauke, Chipata and Mfuwe), North-Western (Kasempa and Solwezi), Northern (Kasama, Mbala and Mpulungu), Muchinga (Mpika, Chinsali, Isoka and Nakonde), Luapula (Samfya and Mansa) and Lusaka (Lusaka and Kafue).

Data analysis is done using the Net Balance Statistic (N) where qualitative responses are converted into quantitative measures using the following equation:

$$N = \frac{U - D}{U + D + S} * 100$$

Where U , D and S represent the number of respondents indicating Up, Down and Same, respectively.

The Net Balance Statistic method has the advantage of detecting the directional changes in performance/expectations of respondents in such surveys. The method indicates the predominance of either an improvement or deterioration in a variable. A positive net percentage indicates that more respondents reported/expected an increase/improvement/tightening and a negative net percentage means a decrease/deterioration/loosening, depending on the variable under consideration. This method has been used widely in the analysis of survey data.