



BANK *Of* ZAMBIA

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

First Quarter 2018, Vol 2.1

Disclaimer:

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

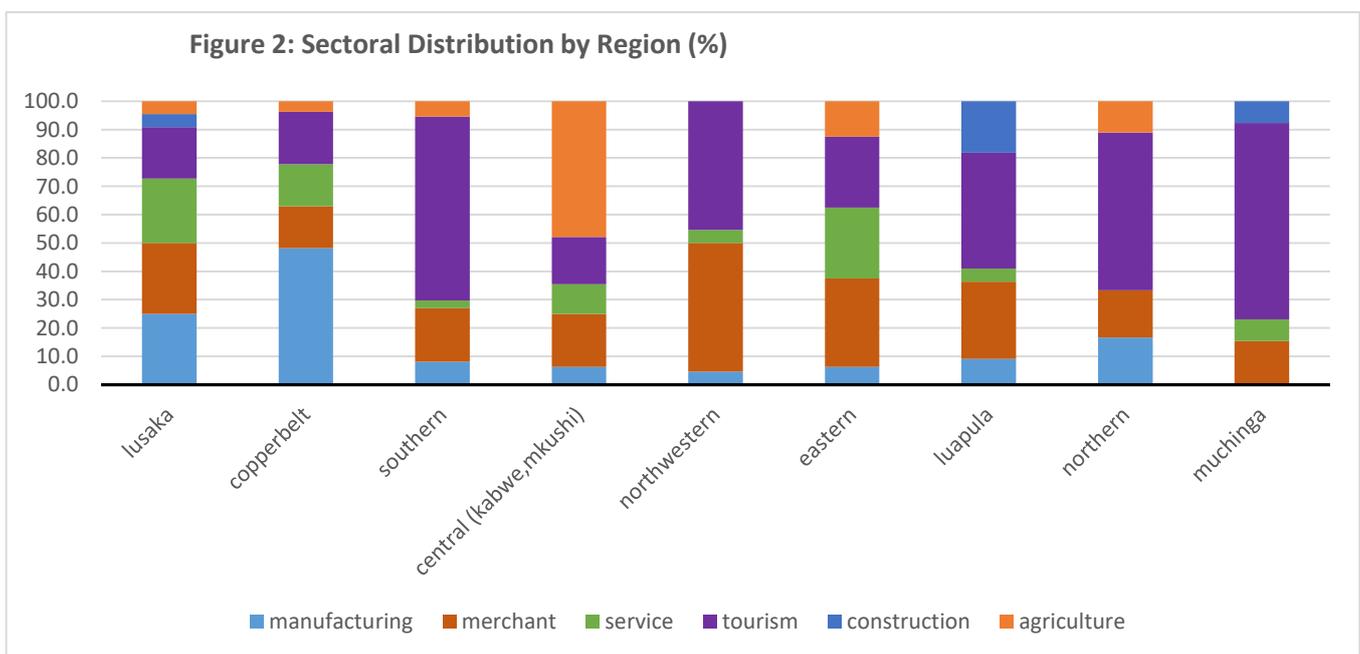
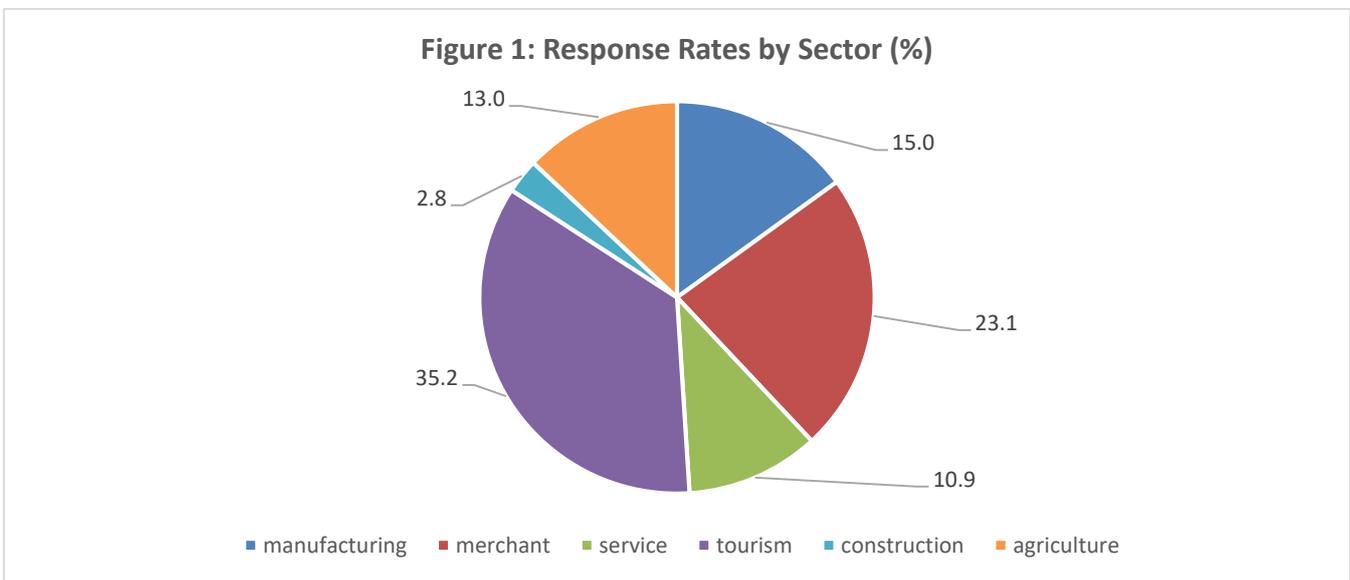
MAY 2018

PREFACE

The Quarterly Survey of Business Opinions 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.

The business opinions and expectations survey provides useful indicators of current and future economic activity and assist in the formulation of decisions today that impact on future economic performance. The survey provides a guide to likely future developments because of the dominant role expectations play in shaping economic behaviour.

This Report is based on the results of the QSBOE conducted from February - March 2018. A total of 285 questionnaires were distributed, of which 247 firms responded, thus representing a response rate of 86.7%. The sectoral response shares and distribution are indicated in Figures 1 and 2 below.



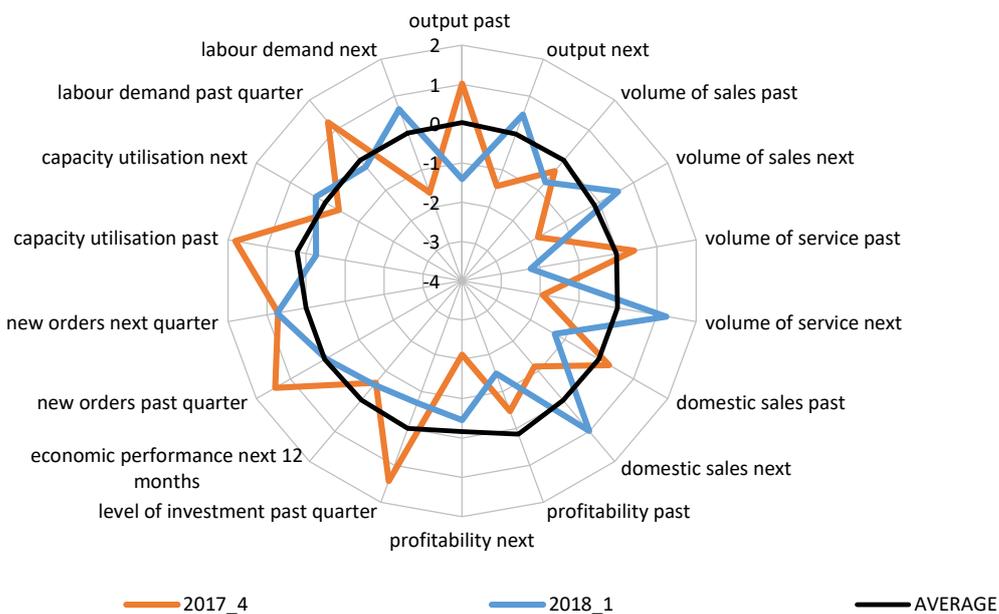
Executive Summary¹

The Quarterly Survey of Business Opinions and Expectations for the first quarter of 2018 showed that economic activity deteriorated compared to the fourth quarter of 2017. Capacity utilisation, level of investment, output, labour demand, domestic sales and profitability were all below their average historical performance, largely attributed to the slowdown in economic activity after the festive season, low demand, effects of the cholera outbreak, partial drought and off peak tourism period.

The outlook for the second quarter of 2018, however, indicated an improvement in the performance of all indicators. Capacity utilisation, output, volume of service, volume of sales, labour demand, domestic sales and new orders are all expected to be higher than the previous quarter as well as above their historical average performance. Profitability is also expected to improve, but remains below the historical average performance due to higher production costs. The anticipated improvement in economic activity is mainly supported by higher activity in the agriculture sector during the harvest period which feeds into the manufacturing sector, infrastructure development after the rainy season, as well as tourism peak season.

Respondents expectations indicate that economic performance will remain relatively subdued over the next 12 months, showing only a slight improvement (see Figure 3). This prospect is mainly on account of lower agricultural output, the high cost of doing business, low demand, credit constraints, rising taxes and the high national debt burden which may constrain capital expenditure. Nonetheless, high copper prices and moderate inflation continue to provide positive sentiment towards the economy.

Figure 3: Overall Survey Response Patterns*



*Note: The survey indicators are standardised 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 2018. The results are based on responses from 247 firms of the 285 questionnaires distributed, covering manufacturing, merchants, tourism and services, agriculture and construction sectors, thus representing a response rate of 86.7%.

Introduction

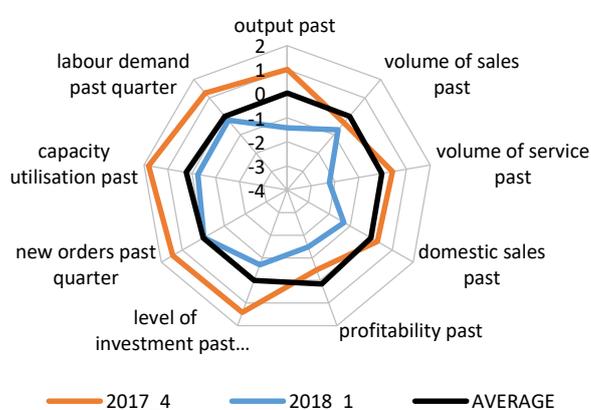
This Business Opinions and Expectations Survey Report is divided into four sections. The first section presents the response patterns related to economic performance during the first quarter of 2018 and expectations for the second quarter, while section II presents opinions and expectations on input costs, wages and selling prices, among other variables. Section III provides first quarter 2018 perceptions on variables that influence monetary policy, while section IV provides the general conclusion.

I. Opinions and Expectations of Economic Activity

Economic Activity declined in Q1 2018

In the last report, respondents had indicated that economic performance would decline in the first quarter of 2018. Consistent with this expectation, the overall response pattern from the survey for the first quarter of 2018 indicated that economic activity deteriorated, mainly attributed to poor economic conditions. This was explained by reduced investment level, capacity utilisation, labour demand, output, volume of service, volume of sales, domestic sales and profitability which were all below the fourth quarter 2017 performance and their historical averages (see Chart 1).

Chart 1: Business Opinions Response Patterns

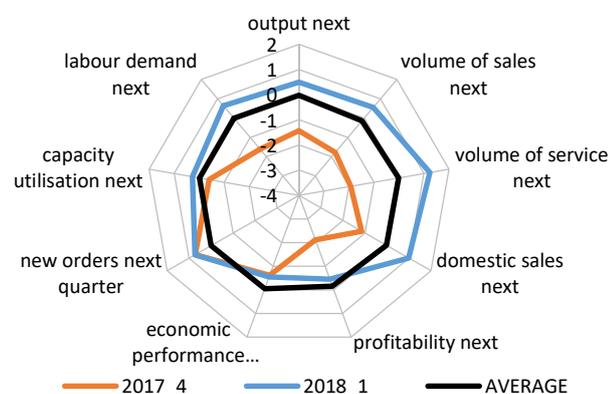


The expectations for the second quarter of 2018, however, showed stronger economic

performance, as reflected in improved capacity utilisation, labour demand, output, volume of service, volume of sales, domestic sales and profitability. All these indicators were above their historical levels.

However, expectations indicated that economic performance would remain subdued over the next 12 months. This was largely on account of the anticipated lower agricultural output resulting from the partial drought, high cost of doing business, credit constraints, poor business climate, high Government debt service and high unemployment in the economy (see Chart 2).

Chart 2: Business Expectations Response Patterns



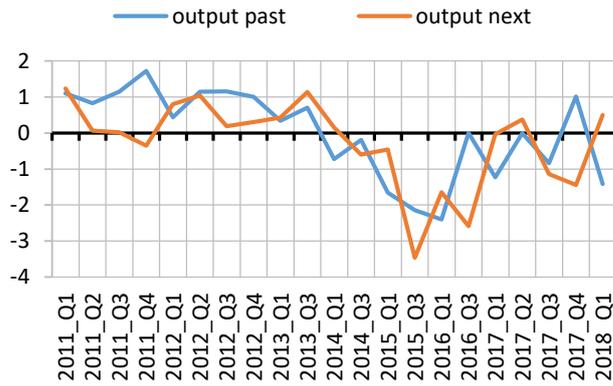
Q: What has been your firm's experience with respect to Output?

(Net balance, -22.6%; Q4 2017, 11.5%)

Output decreased during the first quarter of 2018 and was below the historical average. This was mainly due to the partial drought which resulted in lower activity in the agriculture sector. In addition, the high cost of production in the manufacturing sector associated with the fuel price increase negatively affected output.

Expectations for the second quarter of 2018, however, revealed an improvement in output mainly attributed to the harvest period in the agriculture sector and deployment of new production machinery in the manufacturing sector (see Chart 3).

Chart 3: Opinion on Output

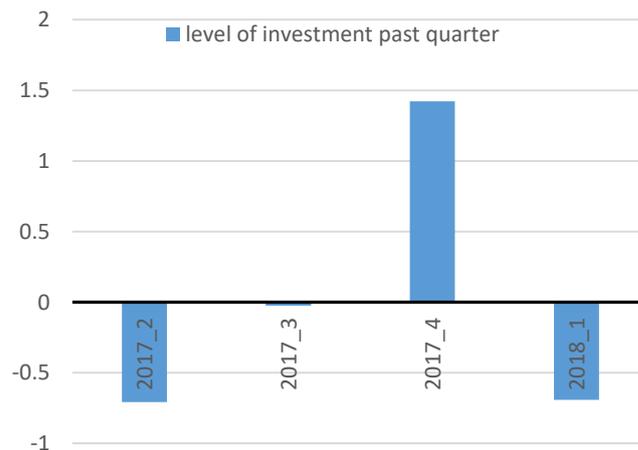


Q: How was your firm's level of Investment?

(Net balance, 9.0%; Q4 2017 21.0%)

Respondents indicated that total investment decelerated during the quarter under review compared to the previous quarter. This was mainly attributed to the high cost of doing business, reduced business activity mainly in the services and merchant sectors, poor economic climate (contracting economy) and low commodity prices in the agriculture sector (see Chart 4).

Chart 4: Level of investment



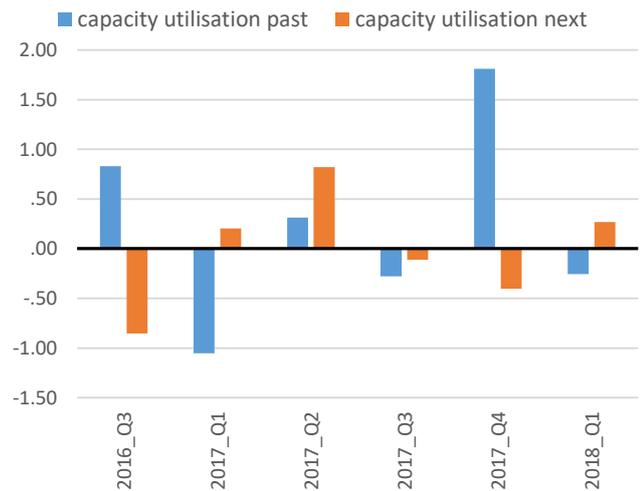
Q: What has been your firm's experience with respect to Capacity Utilisation?

(Net balance, -14.3%; Q4 2017, 11.1%)

Most respondents indicated that capacity utilisation fell during the first quarter of 2018 compared to the fourth quarter of 2017. This was mainly due to stiff competition from cheap imports, low consumer demand and high cost of production in the manufacturing sector.

Capacity utilisation was, however, expected to improve in the second quarter of 2018 due to an anticipated increase in consumer demand, tourism and supply of agricultural raw materials into the manufacturing sector (see Chart 5).

Chart 5: Capacity Utilisation



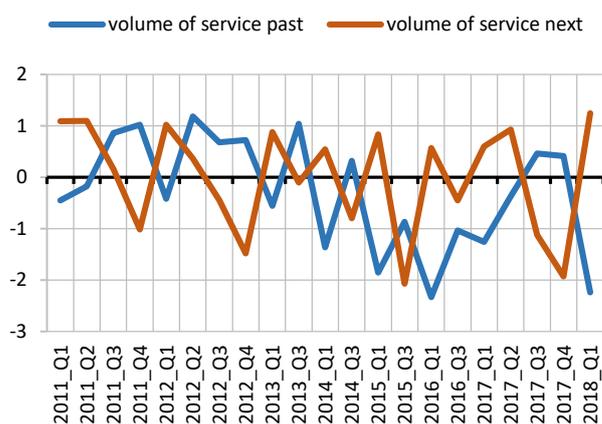
Q: What has been your firm's experience with respect to Volume of Service?

(Net balance, -45.7%; Q4 2017, 1.6%)

The volume of service declined during the quarter under review and was below the historical average. This was mainly on account of reduced tourism activities during the rainy (off-peak) season, cholera outbreak, increased levies and slow-down in economic activity.

The volume of service, however, was expected to improve and rise above the historical average in the second quarter of 2018. This expectation was premised on the recovery of the tourism sector during the peak season and an anticipated increase in bank deposits resulting from improved marketing strategies e.g. digitalisation on mobile platform (see Chart 6).

Chart 6: Volume of Service



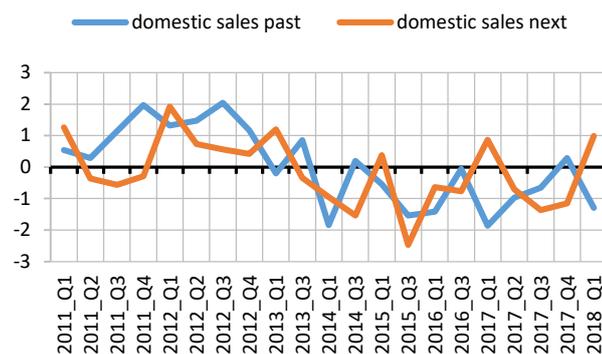
Q: What has been your firm's experience with respect to Domestic Sales?

(Net balance, -26.2%; Q4 2017, 0.0%)

Domestic sales fell below the historical average level during the first quarter of 2018. This was mainly due to subdued demand in the economy after the festive season and stiff competition in the manufacturing sector (see Chart 7).

During the second quarter of 2018, however, domestic sales are expected to improve, mainly on account of an anticipated rise in demand attributed to the crop marketing season in the agriculture sector.

Chart 7: Domestic Sales



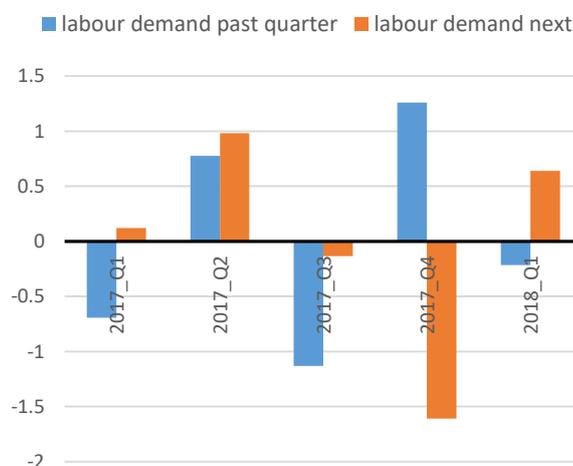
Q: How do you rate your firm's Labour Demand?

(Net balance, -1.8%; Q4 2017 6.5%)

Labour demand decreased during the first quarter of 2018, largely as a result of low activity in the service and tourism sectors, reduced area planted in the agriculture sector due to poor rains and prolonged fish ban in fisheries sub-sector.

Demand for labour was, however, expected to improve during the second quarter of 2018, largely as a result of the commencement of the harvest season in the agriculture sector, investments in infrastructure in the tourism sector during peak period as well as bank branch expansion (see Chart 8).

Chart 8: Labour Demand



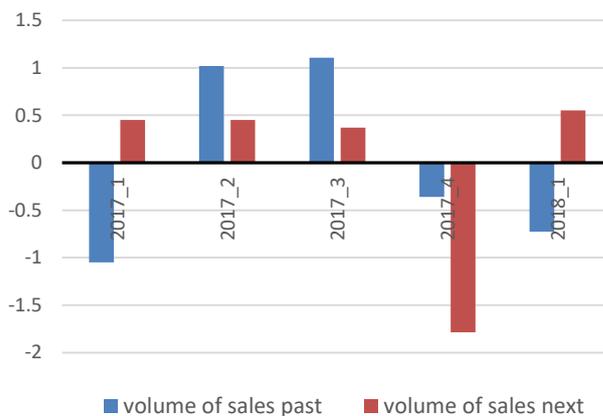
Q: What has been your firm's experience with respect to Volume of Sales?

(Net balance, -48.3%; Q4 2017, -26.3%)

The merchants sector recorded a decline in volume of sales in the first quarter of 2018 compared to the fourth quarter of 2017. This was largely on account of reduced demand after the festive season, increased cost of fuel, reduced construction activities during the rainy season (off-peak) and increased competition within the sector.

The outlook for the second quarter, however, indicates an increase in the volume of sales. This expectation is premised on an increase in demand as the agricultural marketing season commences and construction activities increase during the peak season (see Chart 9).

Chart 9: Volume of Sales



Q: What is your current main source of Investment Finance and Working Capital?

Main source of financing remained retained earnings

Retained earnings continued to be the main source of investment finance and working capital in the first quarter 2018, at 69.2% (67.9%)² and 72.7% (76.1%), respectively. This was followed

² Figures in brackets are for Q4 2017

by Bank borrowing at 16.5% (16.7%) and 14.8% (9.8%), respectively (see Charts 10A and 10B).

Chart 10A: Sources of Investment Finance

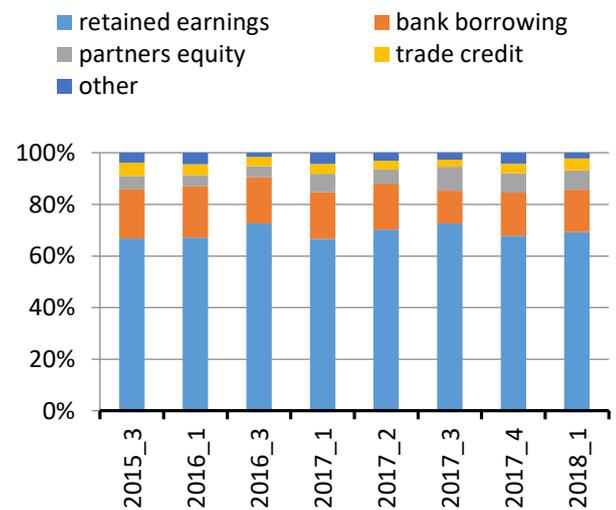
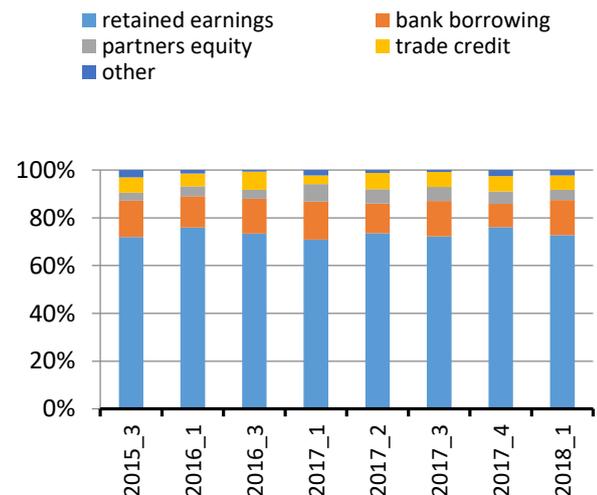


Chart 10B: Sources of Working Capital



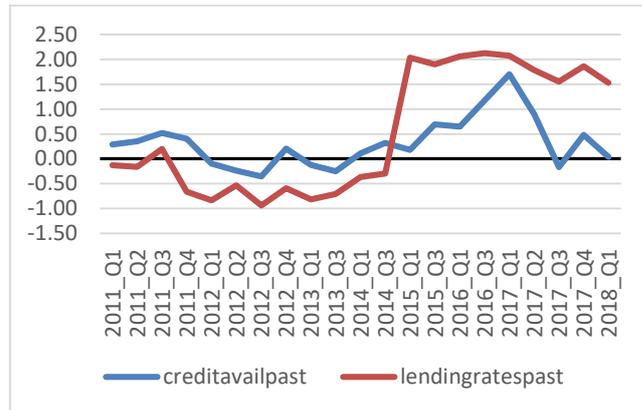
Q: What is your perception of the current Availability of credit?

(Net balance, 63.4%; Q4 2017, 67.2%)

Respondents indicated that they continued to observe tight credit conditions during the first quarter of 2018, despite the reduction in the Bank of Zambia policy rate in February 2018. They stated that this was mainly on account of stringent

collateral requirements by commercial banks, rising stock of non-performing loans, longer loan processing periods and low liquidity (see Chart 11). This, notwithstanding, credit conditions in the first quarter of 2018 were less tight compared to the fourth quarter of 2017.

Chart 11: Credit conditions and lending rates



II EVOLUTION of COSTS, WAGES and PRICES

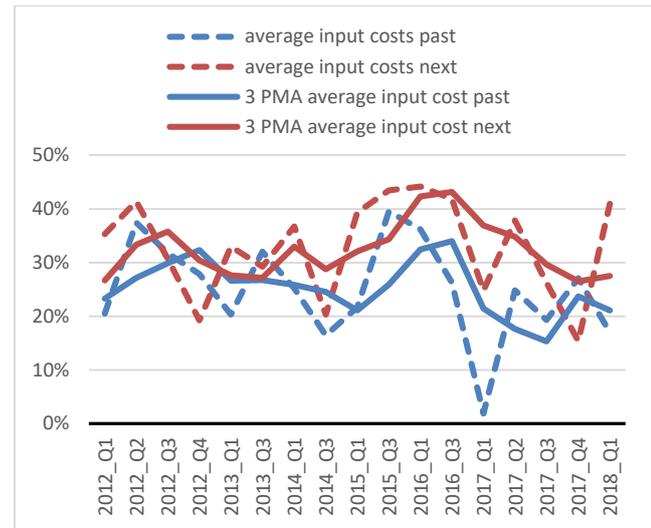
Q: What has been your firm's experience during the quarter under review with respect to Average input costs?

(Net balance, 17.0%; Q4 2017, 27.1%)

Average input costs remained above the historical average during the period under review. This was mainly attributed to the increase in the price of fuel, property rates and cost of raw materials. The high electricity tariffs and the introduction of new taxes also contributed to high average input costs (see Chart 12).

Respondents expect average input costs to remain high during the second quarter of 2018, due to increased production costs.

Chart 12: Average input costs



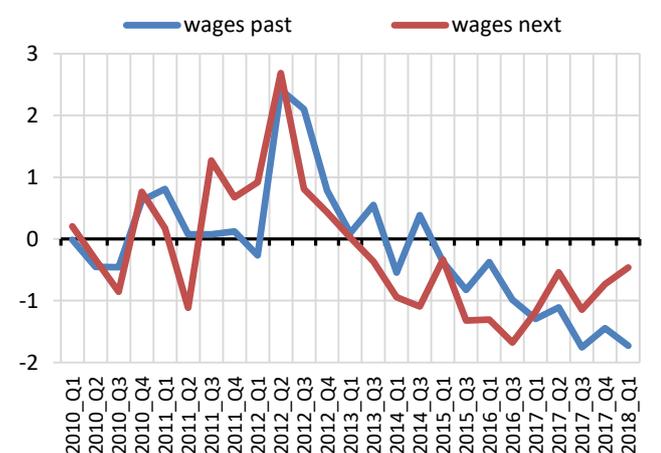
Q: What has been your firm's experience with respect to the Wage bill?

(Net balance, 1.3%; Q4 2017, 3.6%)

During the first quarter of 2018, the wage bill decreased in comparison to the fourth quarter of 2017. This was mainly attributed to reduced sales and business activity in the merchant sector as well as tourism and agriculture sectors, respectively.

The wage bill is, however, expected to rise during the second quarter of 2018, mainly on account of the expected higher activity in the agriculture and tourism sectors (see Chart 13).

Chart 13: Evolution of wages



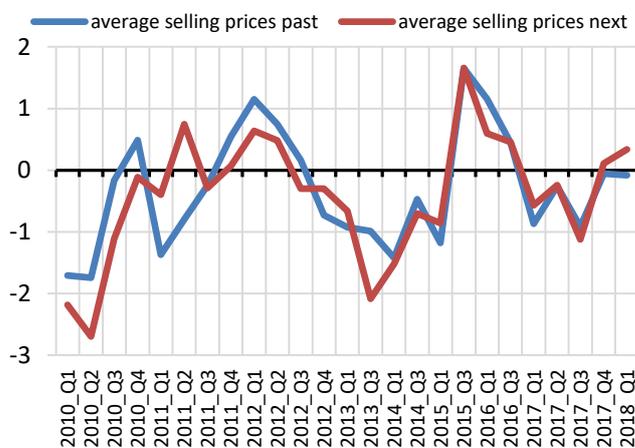
Q: What has been your firm's experience during the quarter under review with respect to Average Selling Prices?

(Net balance, -0.88%; Q4 2017, -0.40%)

Average prices fell during the first quarter of 2018, when compared to the fourth quarter of 2017. This was mainly on account of stiff competition, low demand and trade discounts in the merchants and services sectors. In the banking industry, the average interest rate fell on account of the reduction in the monetary policy rate and the statutory reserve ratio (see Chart 14).

Average selling prices are expected to increase in the second quarter of 2018. This expectation is premised on a rise in the cost of inputs (transport costs and electricity) which may be passed onto consumers and the rise in demand for services in the tourism sector.

Chart 14: Evolution of average selling prices



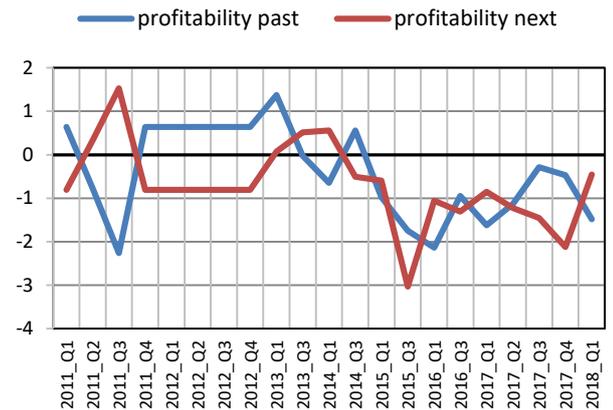
Q: What has been your firm's experience with respect to Profitability?

(Net balance, -43.9%; Q4 2017, -22.9%)

Most respondents indicated that profitability continued to fall during the first quarter of 2018 and was below the historical average. This was mainly attributed to high production costs, subdued demand, high cost of raw materials and low sales due to stiff competition.

Profitability was, however, expected to rebound in the second quarter of 2018 mainly on account of an anticipated increase in tourist arrivals coupled with high demand for conference facilities during the quarter. In addition, the crop-marketing season in the agriculture sector was expected to contribute to the availability of food commodities and improvement in profitability for food processing firms (see Chart 15).

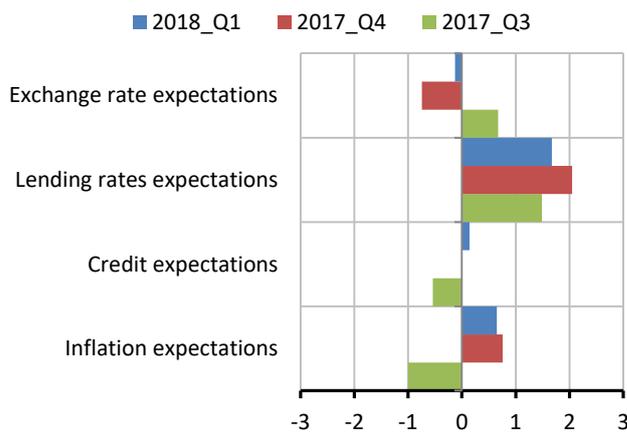
Chart 15: Profitability



III EXPECTATIONS on MONETARY POLICY FOR SECOND QUARTER 2018

Most respondents' expectations for the second quarter of 2018 indicated an increase in inflation and lending rates although lower than the previous quarter, a slightly weak exchange rate and tight credit conditions (see Chart 16).

Chart 16: Expectations of high inflation, weak exchange rate, tight credit conditions with high lending rates



Notes:

- Exchange rate = appreciation, strong (+)/depreciate, weak (-)
- Lending rates = increase, high (+)/decrease, low (-)
- Credit conditions = tight (+)/loose (-)
- Inflation expectations = increase, high (+)/decrease, low (-)

Q: Over the next quarter what do you expect the Price level to be?

(Net balance, 48.1%; Q4 2017, 50.2 %)

Most respondents anticipate that inflationary pressures will increase during the second quarter of 2018, although lower than that reported in the fourth quarter of 2017. This was premised on the increase in transport fares following the upward adjusted in fuel prices, high taxes, lower food output and an anticipated slightly weak exchange rate (see Chart 17).

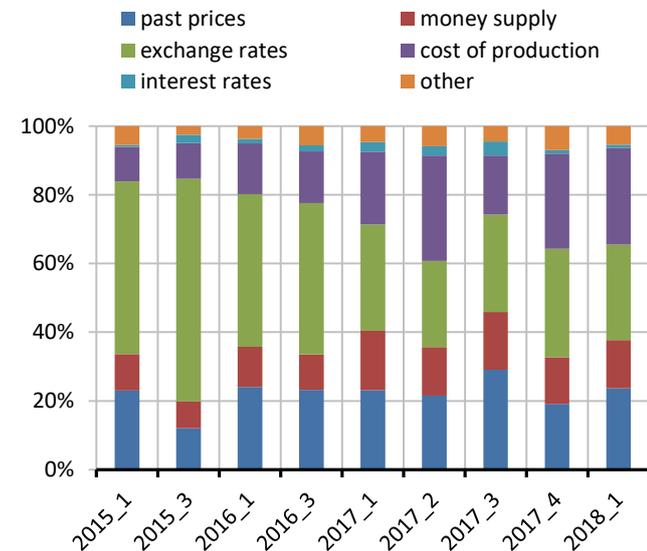
Chart 17: Inflationary expectations above historical average in Q2 2018



Q: Which is the Main factor explaining your Expectations of inflation?

The main drivers of inflationary expectations were cost of production as indicated by 28.2% of the respondents compared to 27.6% in the previous quarter, followed by exchange rates at 27.7% (31.7%) and past prices at 23.6% (19.1%) (see Chart 18).

Chart 18: Inflation expectations mainly driven by cost of production and exchange rates

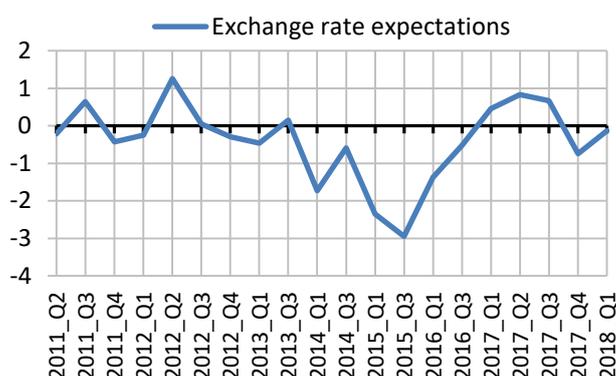


Q: What do you Expect the Value of the Zambian Kwacha against the US Dollar to be at the end of the next quarter?

(Net balance, -16.5%; Q4 2017, -32.5%)

Most respondents anticipate the Kwacha exchange rate against the US dollar to remain weak, though stronger than the previous quarter. The exchange rate is mainly supported by higher copper prices and the related export earnings. However, negative sentiment related to high external debt service, low foreign reserves and delayed IMF program may have a negative influence on the exchange rate (see Chart 19).

Chart 19: Exchange rate expectations next quarter

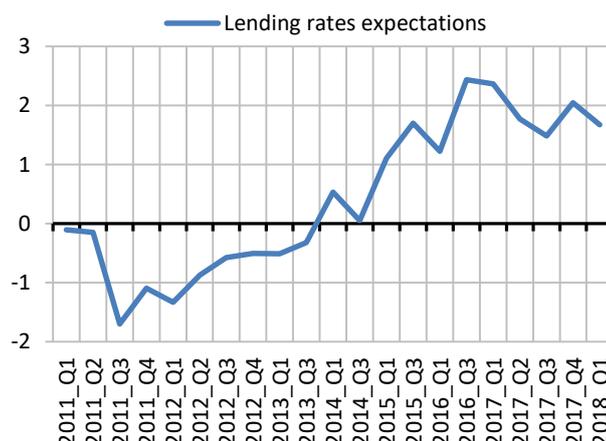


Q: Over the next quarter, what do you expect to happen to Commercial Bank Lending Interest rates?

(Net balance, 61.8%; Q4 2017, 72.5%)

Commercial bank lending rates are expected to decline slightly due to the easing in monetary policy, but nonetheless, remain higher than the historical average. This expectation is attributed to high Government borrowing and increasing volumes of non-performing loans (see Chart 20).

Chart 20: Interest rate expectations next quarter

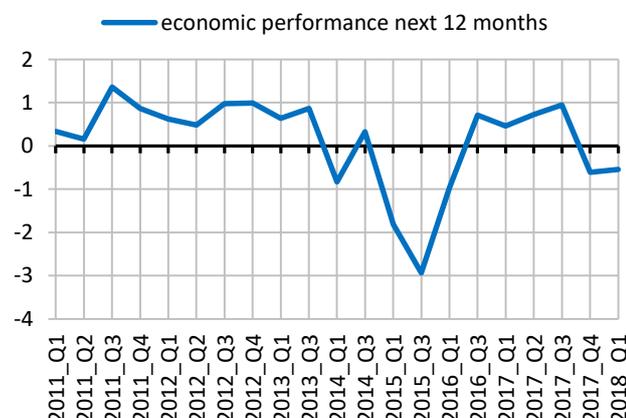


Q: What is your expectation of the performance of the Zambian economy in the next 12 months?

(Net balance, 12.5%; Q4 2017, 11.1%)

Expectations indicate that economic performance will remain subdued over the next 12 months, showing only a slight improvement. This is mainly on account of the lower agriculture output, high cost of doing business, low demand, credit constraint, rising taxes and high debt burden. However, the moderate inflation and high copper prices continue to provide positive sentiment towards the economy (see Chart 22).

Chart 22: Economic performance in next 12 months



IV CONCLUSION

The Survey of Business Opinions and Expectations conducted in the first quarter of 2018 showed a deterioration in economic activity compared to the fourth quarter of 2018, with all the variables performing below historical averages. This was mainly due to a decline in consumer demand after the festive period, higher cost of production, partial drought affecting the agriculture sector and low activity (off-peak season) in the tourism sector.

The outlook for the second quarter of 2018, however, indicated an improvement in output, capacity utilisation, new orders, volume of sales and services, domestic sales, labour demand and profitability. This would be supported by the agriculture harvest period, peak tourism season and construction activity after the end of the rainy season.

Most respondents anticipate a moderate rise in inflation during the second quarter of 2018, on account of the high cost of production following the increase in transport fares and taxes as well as lower food output in the 2017/18 harvest season.

Economic activity is expected to remain subdued over the next 12 months, mainly on account of lower agriculture output, the high cost of doing business, low demand, credit constraint, rising taxes and high debt burden. Nonetheless, the high copper prices and moderate inflation continue to provide positive sentiment towards the economy.

Appendix I: Background on the QSBOE

This Report is based on the results of the QSBOE conducted from March - April 2018. Out of the 285 questionnaires distributed, 247 firms responded, representing a response rate of 86.7%.

Of the 247 respondents, 35.2% were from tourism, merchants (23.1%), manufacturing (15.0%), agriculture (13.0%), services (10.9%) 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.