



BANK *Of* ZAMBIA

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

First Quarter 2019, Vol 2.5

Disclaimer:

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

APRIL 2019

PREFACE

The Quarterly Survey of Business Opinions and Expectations (QSBOEs) provides useful indications about current and future economic activity and assists in the formulation of decisions today that impact on future economic performance. Given the dominant role expectations play in shaping economic behaviour, the survey provides a guide to likely future developments.

Accordingly, the Survey undertaken by the Bank of Zambia is designed as a supplementary tool providing information on the business community's opinions and expectations about the current and future direction of the economy.

This Report is based on the results of the QSBOEs conducted from February – April 2019. A total of 282 questionnaires were distributed, of which 247 firms responded. This represented a response rate of 87.6%. Of the firms that responded, 35.8% were from tourism and services, 22.4% were merchants, manufacturing (17.5%), agriculture (11.2%) and construction (2.6%) sectors (see Figures 1 and 2).

Figure 1: Response Rates by Sector (%)

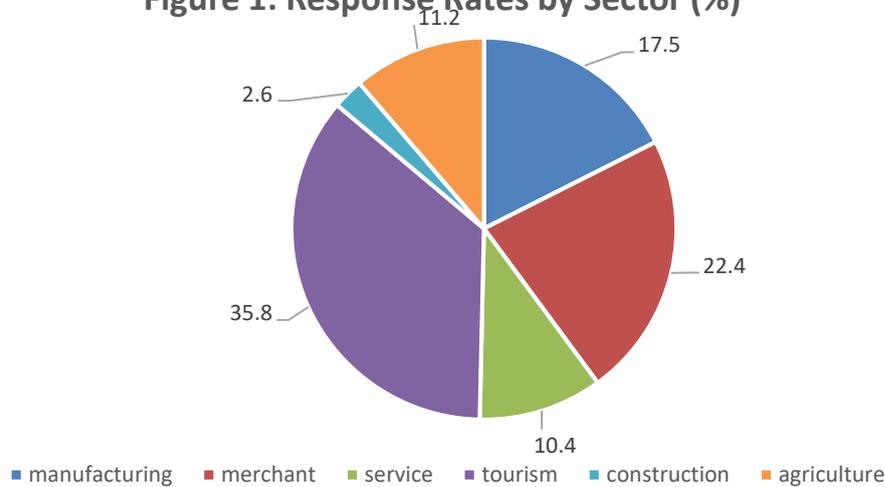
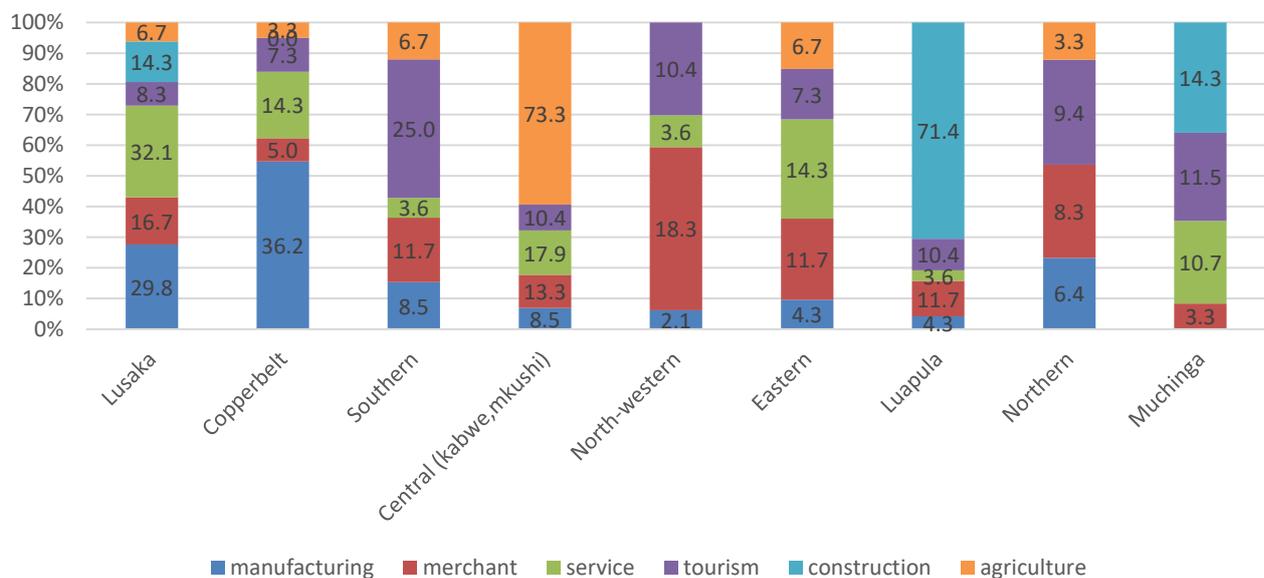


Figure 2: Sectoral Distribution by Region (%)



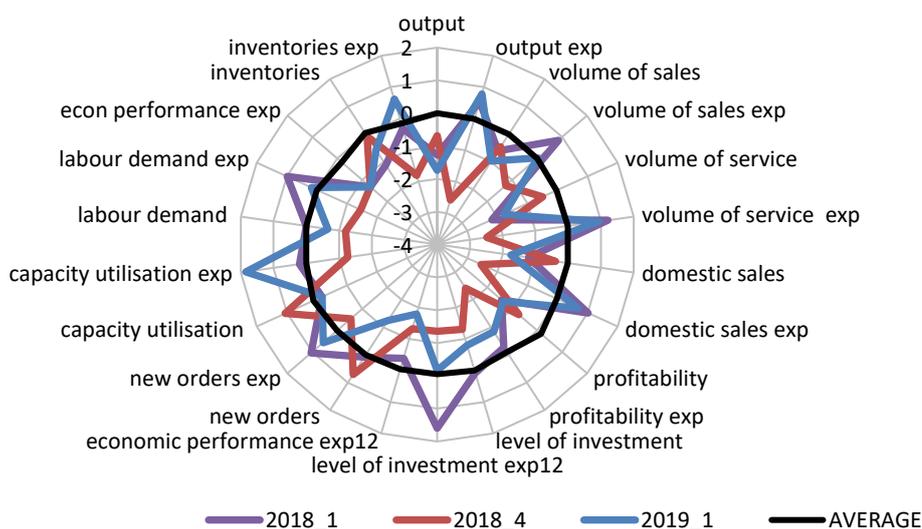
Executive Summary¹

The Survey of Business Opinions and Expectations conducted during the first quarter of 2019 showed that economic performance remained weak and below the historical average during the reviewed period. Most surveyed business entities reported a deterioration in performance of all the monitored indicators, with the exception of labour demand and the level of investment. Low demand, lack of money, high cost of doing business and the weaker Kwacha exchange rate against the US dollar negatively affected the operations of manufacturing, merchant and service sectors. In addition, slow diversification and rising Government debt service were highlighted as some of the major factors constraining economic activity. This notwithstanding labour demand rose slightly on account of an increase in seasonal workers engaged in wheat-planting and horticulture expansion by some commercial farmers, as well as the recruitment of train drivers by Zambia Railways following the Statutory Instrument on transportation of heavy goods, which compels 30% of bulky and heavy cargo to be transported by rail. Further, some investment was driven by refurbishment of business premises in the tourism sector and acquisition of new machinery and equipment by some commercial farmers.

Most respondents, expressed optimism regarding economic performance in the second quarter of 2019. Output, domestic sales, labour demand and capacity utilization are expected to increase due to activities related to the commencement of the agricultural harvesting period and tourism peak season.

The sentiment on economic performance over the next 12 months, however, weakened in contrast to the previous quarter. Most business entities expect a decline in economic activity mainly due to lower agricultural output in the 2018/19 season, high cost of doing business, subdued domestic demand, lack of money, rising commercial bank lending rates, the introduction of sales tax, as well as high external debt service by Government and slow fiscal consolidation. In addition, the Kwacha exchange rate against the US dollar is expected to weaken further resulting in higher inflation.

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 2019. The results are based on responses from 247 firms of the 282 questionnaires distributed, covering manufacturing, merchants, tourism and services, agriculture and construction sectors. This outturn represented a response rate of 87.6%.

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 2019 as well as expectations for the second quarter of 2019, while section II presents opinions and expectations for the same period on input costs, wages and selling prices, among other variables. Section III provides second quarter 2019 perceptions on variables that influence monetary policy, while section IV provides the general conclusion.

I. Opinions and expectations of economic activity

Economic activity remained subdued in Q1 2019 and expected to deteriorate over the next 12 months

The majority of respondents anticipated weaker economic performance during the first quarter of 2019, with most of the monitored indicators expected to perform below their historical averages. In line with these expectations, economic performance deteriorated further during the quarter under review. All the monitored indicators declined with the exception of labour demand and investment level (see Chart 1).

The subdued economic activity was largely attributed to reduced agricultural activity following poor rainfall, the high cost of doing business, low demand, lack of money, a weaker Kwacha exchange rate against the US dollar which negatively affected the manufacturing and merchant sectors and pressures emanating from high Government debt service. This notwithstanding, there was a rise in demand for seasonal workers engaged in wheat-planting and horticulture expansion by some commercial farmers, while some investment was driven by refurbishment of business premises and acquisition of new machinery and equipment by the tourism sector (see Chart 1).

An improvement in economic activity was anticipated during the second quarter of 2019 (see Chart 2). This optimism was premised on activities related to the commencement of the agricultural harvesting period and peak tourism season.

Most respondents however, expect a decline in economic performance over the next 12 months. The anticipated lower agricultural output in the 2018/19 harvesting season, underperforming manufacturing and merchant sectors, introduction of sales tax, subdued demand, lack of money, weaker Kwacha exchange rate against the US dollar, high cost of doing business, rising interest rates and high Government debt service were some of the factors that explained this sentiment.

Chart 1: Business Opinions Response Patterns for First Quarter 2019

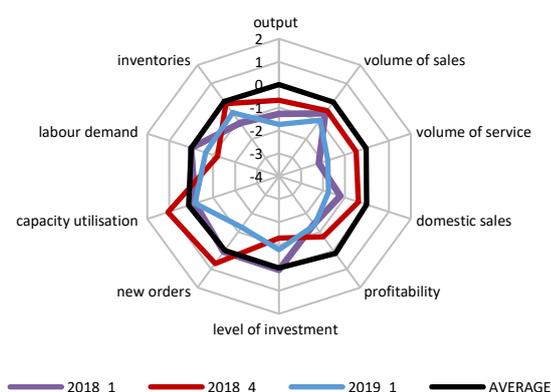
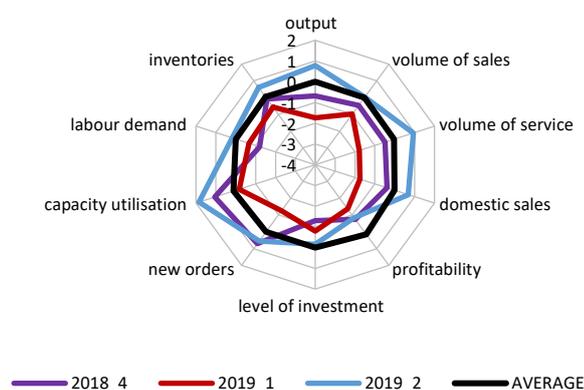


Chart 2: Business Expectations Response Patterns for second Quarter 2019



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

(Net balance, -29.3%; Q4 2018, -14.1%)

Most respondents reported a decline in output during the first quarter of 2019, owing to lower demand experienced largely by the manufacturing sector, as reflected in the fall in new orders and capacity utilisation. In addition, the agricultural sector reported a seasonal decline in activity for rain fed crops (see Chart 3).

Expectations for the second quarter 2019 showed an improvement in output on account of the commencement of the agriculture harvest period which would trigger a rise in the production of food related products by the manufacturing sector. Further, the commissioning of a new plant by Zambian Fertilisers Limited is expected to raise output in the manufacturing sector.

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

(Net balance, 3.3%; Q4 2018, 0.00%)

Total investment rose slightly during the quarter under review in comparison with the fourth quarter 2018. This was mainly due to the refurbishment of business premises in the merchant and tourism sectors, as well as acquisition of new machinery and equipment by some commercial farmers (see Chart 4).

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

(Net balance, -14.3%; Q4 2018, 0.00%)

Consistent with the fall in output, the manufacturing sector reported a decline in capacity utilisation during the first quarter of 2019 (see Chart 5). This was mainly on account of a reduction in new orders due to reduced demand and competition emanating from cheap imports.

However, capacity utilisation is expected to rebound in the second quarter. This sentiment is premised mainly on the anticipated increase in the manufacturing of foodstuffs during the crop marketing season as well as deployment of new machinery by some manufacturing companies.

Chart 3: Opinion on Output

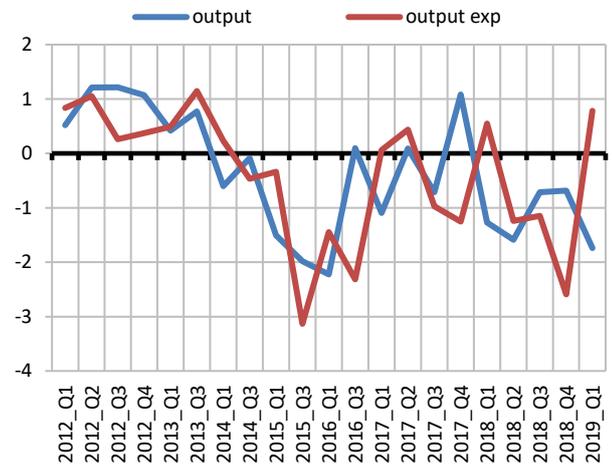


Chart 4: Level of investment

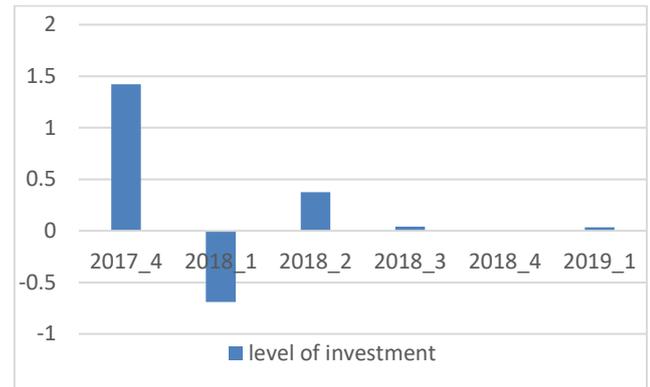
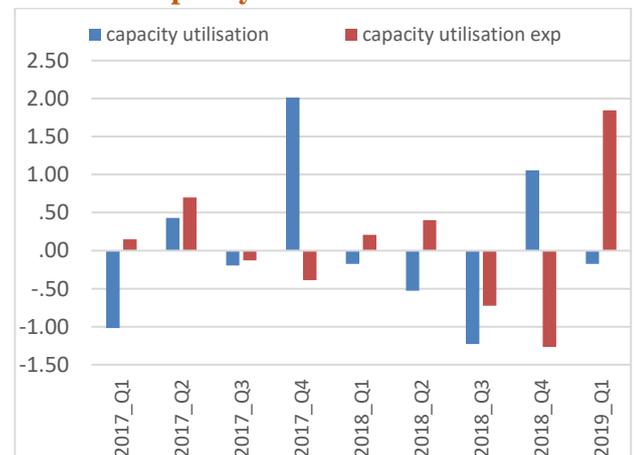


Chart 5: Capacity Utilisation



Q: What has been your firm's experience with respect to volume of service?

(Net balance, -38.5%; Q4 2018, -15.5%)

During the first quarter of 2019, most respondents reported a decline in the volume of service when compared to the fourth quarter 2018 (see Chart 6). This was due to the tourism off-peak season, a slowdown in savings and demand for financing services in the banking industry and low demand for services such as public transport.

The volume of service is, however, expected to rise during the second quarter of 2019, with the onset of the tourism peak season and adoption of new marketing strategies such as sales promotions in the hospitality industry, particularly during public holidays.

Q: What has been your firm's experience with respect to volume of sales?

(Net balance, -66.1%; Q4 2018, -41.3%)

A decline in volume of sales was reported by most respondents during the first quarter of 2019 (see Chart 7). This was largely explained by lower demand recorded by the merchant and manufacturing sectors, owing to tight liquidity in the economy.

In the second quarter, the volume of sales is, however, expected to pick up on account of an expected increase in activity related to the agriculture marketing season.

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

(Net balance, -35.2%; Q4 2018, -12.5%)

Most respondents reported a decline in domestic sales during the first quarter of 2019, due to falling consumer demand, subdued activity in the agriculture sector as well as low demand for new orders in the manufacturing sector (see Chart 8).

Domestic sales are, however, expected to improve in the second quarter mainly due to the commencement of the agricultural crop marketing season.

Chart 6: Volume of Service

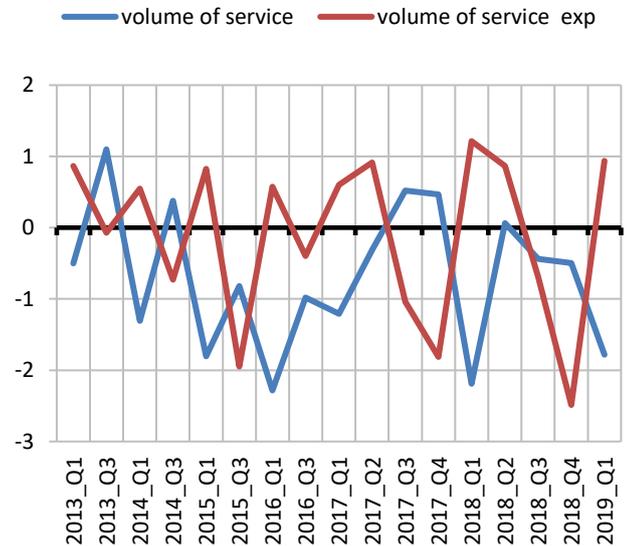


Chart 7: Volume of Sales

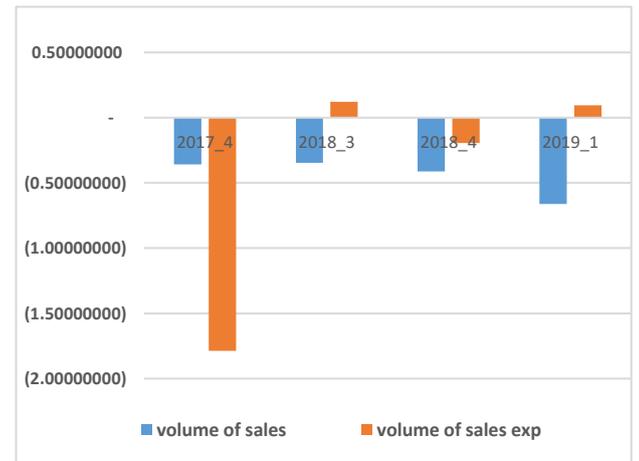
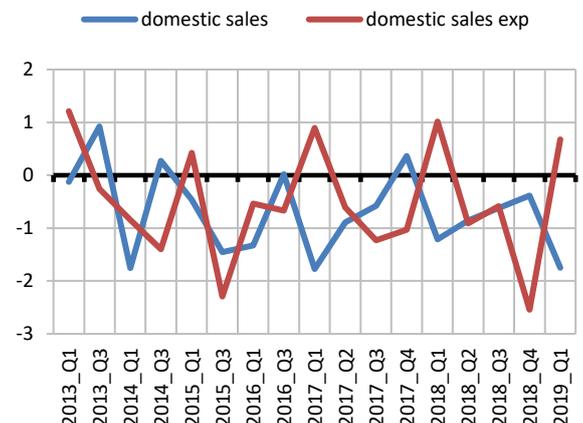


Chart 8: Domestic Sales



Q: How do you rate your firm's labour demand?

(Net balance, -9.2%; Q4 2018 -15.2%)

During the first quarter of 2019, labour demand showed a slight increase despite remaining below the long term average (see Chart 9). This largely reflected workers engaged in wheat planting and the expansion of horticulture production by some commercial farmers. In addition, there was a recruitment of train drivers and assistants in the railway industry following the implementation of the Statutory Instrument on Transportation of Heavy Goods, which compels the transportation of 30% of bulky and heavy cargo by rail.

A further increase in labour demand is expected during the second quarter of 2019 to facilitate increased activities in the tourism sector as well as crop harvesting and cane cutting in the agricultural sector.

Q: What is your current main source of investment finance and working capital?

Main source of financing remained retained earnings

Most respondents indicated that retained earnings remained the main source of investment finance and working capital, with 68.3% and 74.1% response rates compared with 70.4% and 70.2% respectively, in the previous quarter. This was followed by bank borrowing at 14.6% (15.9%) and 14.6% (15.3%), respectively (see Charts 10A and 10B).

Chart 9: Labour Demand

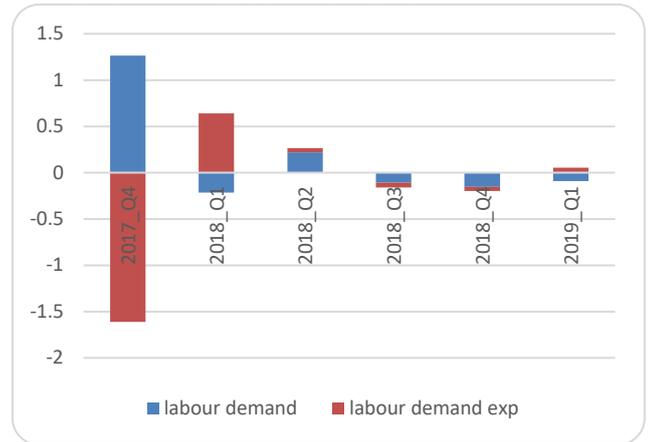


Chart 10A: Sources of Investment Finance

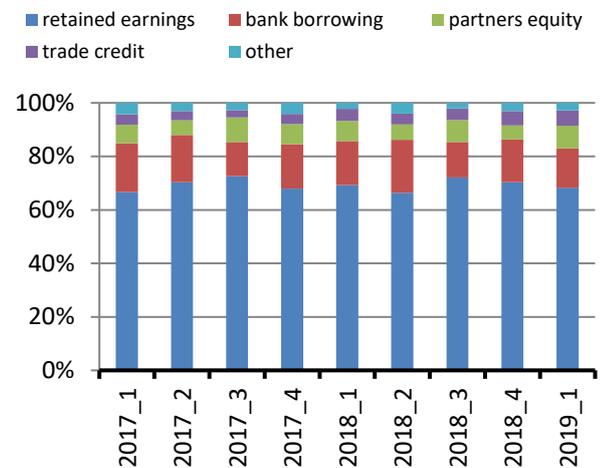
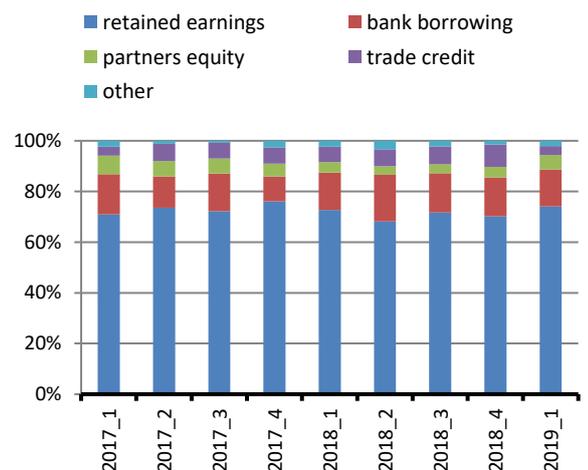


Chart 10B: Sources of Working Capital

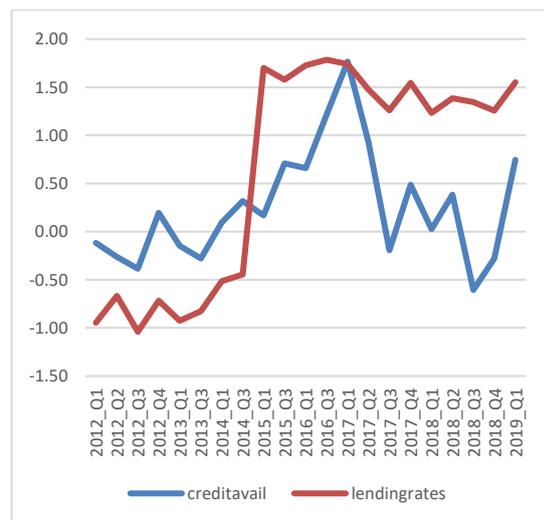


Q: What is your perception of the current availability of credit?

(Net balance, 69.3%; Q4 2018, 60.9%)

Tighter credit conditions were reported by the majority of the respondents during the first quarter of 2019 compared to the fourth quarter of 2018 (see Chart 11). This was mainly on account of stringent collateral requirements by lending institutions, high stock of non-performing loans (NPLs) and high lending rates due to high Government domestic borrowing.

Chart 11: Credit Availability and lending Rates



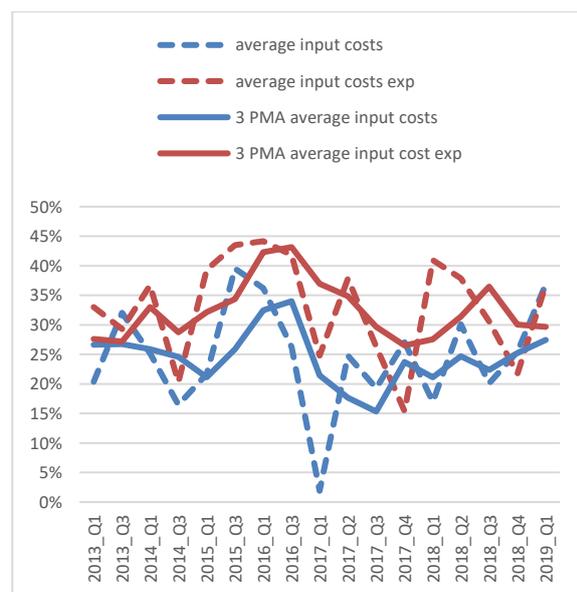
II EVOLUTION OF COSTS, WAGES AND PRICES

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

(Net balance, 36.9%; Q4 2018, 25.5%)

Average input costs increased during the first quarter of 2019 (see Chart 12). This was mainly explained by the rise in costs of imported raw materials following the depreciation of the Kwacha exchange rate against the US dollar. Additionally, the higher price of maize owing to short supply on the market contributed to an increase in average input costs for Millers.

Chart 12: Average input costs



Most respondents anticipate higher input costs during the second quarter of 2019 due to a weaker Kwacha exchange rate against the US dollar, the introduction of Government Sales Tax and expected hike in electricity tariffs.

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

(Net balance, 16.3%; Q4 2018, 17.2%)

During the first quarter of 2019, most respondents reported a decline in the wage bill compared to the fourth quarter of 2018 (see Chart 13). This was largely due to staff redundancies, attributed to reduced business activities and the upward adjustment in the minimum wage. Furthermore, the expiration of contracts for some employees in the tourism, manufacturing and merchant sectors led to a reduction in the wage bill.

The wage bill is, however, expected to increase in the second quarter of 2019, owing to the hire of seasonal workers with the commencement of the tourism peak season, cane cutting and agriculture crop harvesting period. In addition, annual upward salary adjustments are expected to be effected during the second quarter of the year.

Q: What has been your firm's experience during the quarter under review with respect to average selling prices?

(Net balance, 8.6%; Q4 2018, 13.4%)

The majority of the respondents reported a decline in average selling prices, although they remained above their historical levels, during the first quarter of 2019 (see Chart 14). The decline was mainly in response to stiff competition as well as subdued demand across sectors which prompted promotions and sales to clear goods.

During the second quarter of 2019, however, average selling prices are expected to gradually rise mainly due to the pass through of an anticipated depreciation in the exchange rate of the Kwacha against the US dollar, the expected introduction of sales tax and upward adjustment in electricity tariffs as well as high production costs.

Chart 13: Evolution of wages

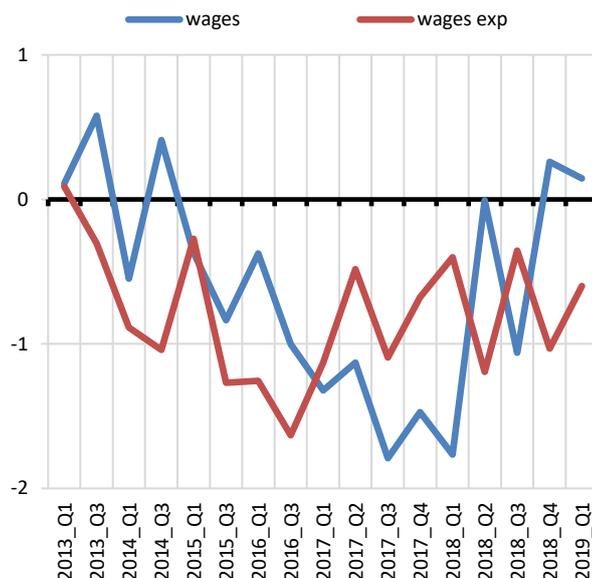


Chart 14: Evolution of average selling prices



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

(Net balance, -42.7%; Q4 2018, -29.9%)

During the first quarter of 2019, profitability continued to decline mainly due to higher input costs of production, subdued demand for goods and services, tight liquidity conditions, as well as low occupancy levels for lodges and hotels (see Chart 15).

The above, notwithstanding, profitability is expected to improve, but remain below the historical average during the second quarter of 2019. This is mainly on account of the anticipated higher sales during the crop marketing season, and adoption of new marketing and sales models by some respondents in the service and tourism sectors.

III EXPECTATIONS ON MONETARY POLICY FOR FIRST QUARTER 2019

Most respondents expect inflation to rise, but at a slower pace compared to the previous quarter. In addition, they anticipate a weaker Kwacha exchange rate against the US dollar, higher lending rates and tight credit conditions (see Chart 16).

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

(Net balance, 51.1%; Q4 2018, 60.5%)

During the second quarter of 2019, inflationary pressures are expected to rise but less sharply than the previous quarter, and remain above historical levels (see Chart 17). An anticipated general increase in food stocks on the market following the crop harvesting season coupled with the fall in consumer demand due to low liquidity is expected to moderate inflationary pressures.

Chart 15: Profitability

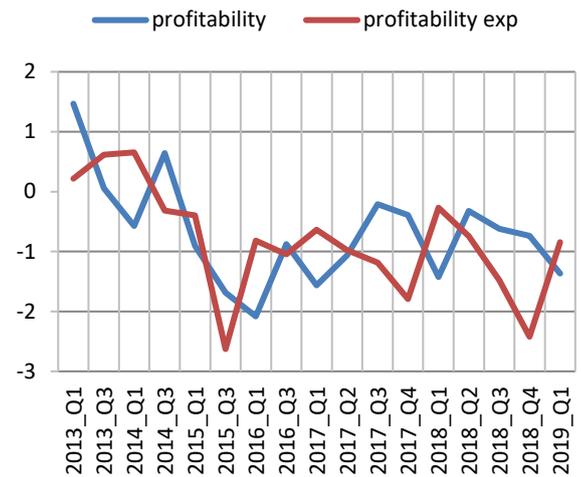
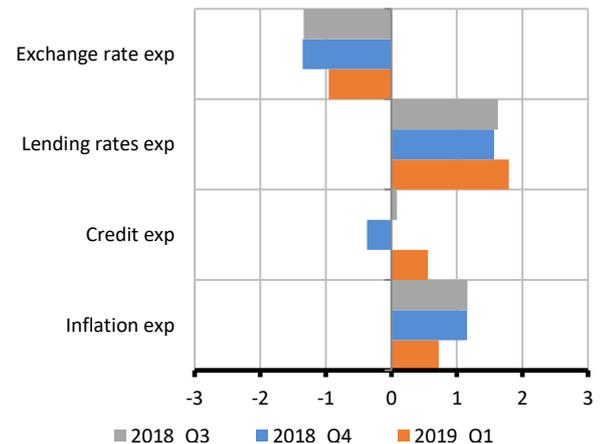


Chart 16: Expectations for rising inflation, weak Kwacha and high lending rates

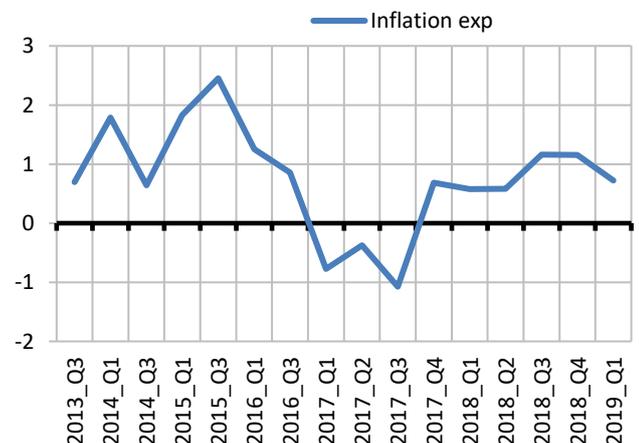


Notes:

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

Inflation expectations = increase, high (+)/decrease, low (-)

Chart 17: Inflation rate expectations next quarter



Q: Which is the main factor explaining your expectations of inflation?

Inflationary pressures are expected to largely emanate from the exchange rate depreciation, as indicated by 31.3% of the respondents compared to 31.5% in the previous quarter. This would be followed by past prices at 25.5% (29.3%) and higher cost of production at 22.2% (23.4%) (see Chart 18).

Q: How do you expect the performance of the Zambian Kwacha against the US Dollar to be at the end of the next quarter?

(Net balance, -40.8%; Q4 2018, -51.3%)

During the second quarter of 2019, most respondents expect the exchange rate of the Kwacha against the US Dollar to remain weak (see Chart 19). This is mainly premised on declining foreign reserves, negative external investors' perceptions of the economy due to high debt levels and low copper production.

Q: Over the next quarter, what do you expect credit availability to be?

(Net balance, 62.4%; Q4 2018, 54.0%)

The majority of respondents expect tighter credit conditions during the second quarter in comparison to the first quarter of 2019 (see Chart 20). This is largely attributed to low liquidity, high Government borrowing, stringent collateral requirements and high interest rates.

Chart 18: Inflationary expectations mainly driven by the exchange rate, cost of production, past prices

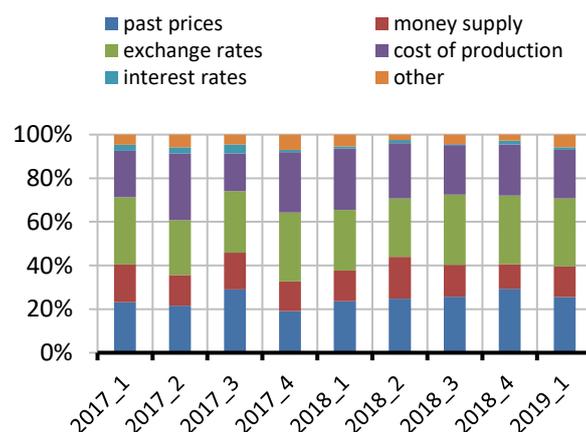


Chart 19: Exchange rate expectations next quarter

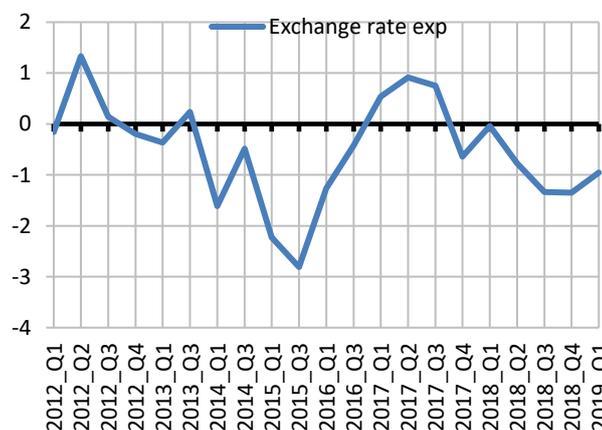
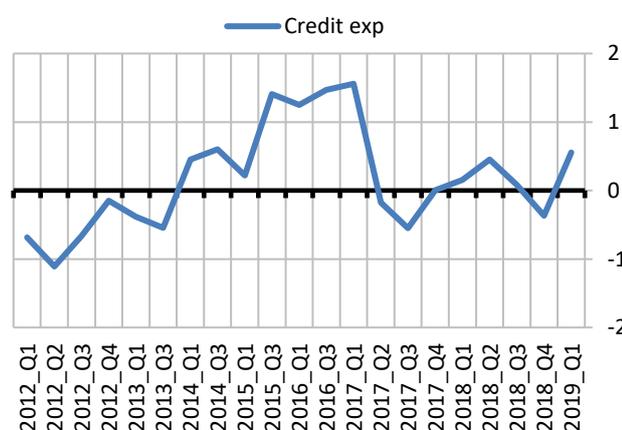


Chart 20: Credit availability expectations next quarter



Q: Over the next quarter, what do you expect to happen to commercial banks' lending rates?

(Net balance, 75.0%; Q4 2018, 67.9%)

Most respondents expect commercial banks' lending rates to rise during the second quarter of 2019 (see Chart 21). This expectation is largely attributed to high Government borrowing, high default risk and low liquidity in the economy.

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

(Net balance, -19.2%; Q4 2018, -8.7%)

Over the next 12 months, respondents expect economic performance to deteriorate (see Chart 22). Factors explaining the anticipated lower economic activity include inadequate demand, low liquidity, high commercial bank lending rates, slow diversification from mining, weaker exchange rate expectations, high taxes, unemployment, poor rainfall in the previous season, declining foreign exchange reserves due to high external debt service and slow fiscal consolidation.

Chart 21: Interest rate expectations next quarter

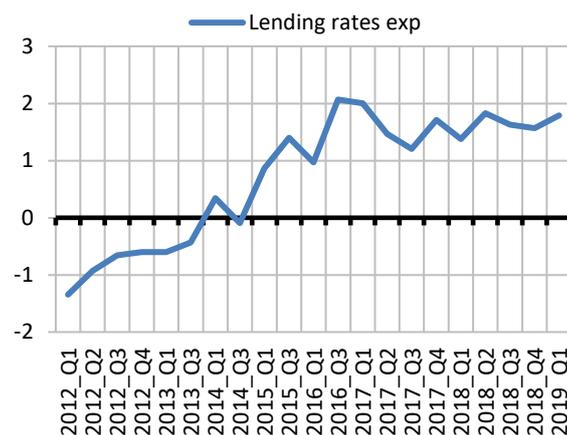
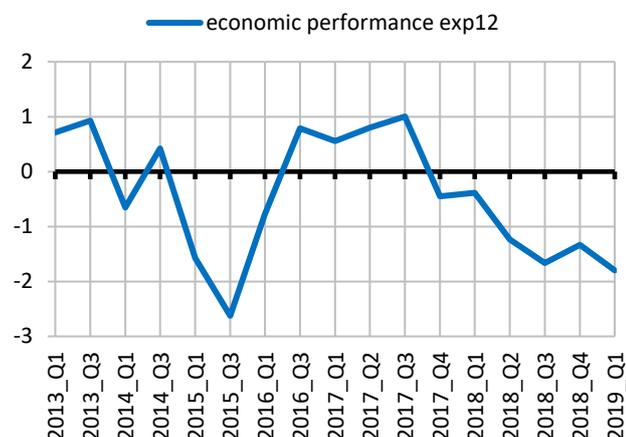


Chart 22: Economic performance in the next 12 months



IV CONCLUSION

The first quarter 2019 Survey of Business Opinion and Expectations conducted between February – April 2019 revealed that economic performance remained weak during the first quarter, as observed from most of the monitored indicators. This was mainly attributed to the high cost of doing business, exchange rate depreciation, low liquidity and subdued demand which negatively affected the merchant and manufacturing sectors. In addition, there was reduced activity in the financial sector as well as the agriculture and tourism sectors, the latter due to seasonal factors.

The outlook for the second quarter 2019 showed an improvement in economic performance premised on activities related to the agriculture crop harvest period and commencement of the tourism peak season.

With regard to factors that influence monetary policy, expectations for the second quarter of 2019 indicate rising commercial bank lending rates, tighter credit conditions and increasing inflationary pressures largely attributed to the pass through of a weaker Kwacha exchange rate against the US Dollar.

The sentiment on economic performance over the next 12 months, however, weakened in contrast to the previous quarter. Most respondents expect a deterioration in economic activity mainly due to the following reasons: an anticipated lower agricultural output in the 2018/19 harvest season attributed to poor rains, subdued domestic demand, lack of money, high cost of doing business, weaker Kwacha exchange rate against the US dollar, underperforming manufacturing, service and merchant sectors, introduction of the sales tax, rising unemployment, high lending rates due to Government borrowing and high default risk.

Appendix I: Background on the QSBOEs

This Report is based on the results of the QSBOEs conducted from March – April 2019. Out of the 282 questionnaires distributed, 247 firms responded, representing a response rate of 87.6%.

Survey Methodology

Data collection for the Quarterly Survey of Business Opinions 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 12 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.