Bank *of* Zambia

Quarterly Survey of Business Opinions and Expectations

September 2020
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Summary

The opinions and expectations of the business community in the third quarter of 2020 were more optimistic than the previous quarter. The relaxation of COVID-19 containment measures and subsequent improvement in demand explained increases in the volume of sales, output, domestic sales and profitability. However, new orders reduced while capacity utilisation remained unchanged. New orders remained subdued due to low demand for locally manufactured goods attributed to rising inflation and a weaker Kwacha. Capacity utilisation was unchanged for the second consecutive time due to high production costs and persistent electricity load shedding. The depreciation of the Kwacha, high and rising public debt, tight credit conditions, persistent electricity loadshedding and rising inflation were cited as the key factors constraining growth. The business community expect economic activity to continue improving into 2021. However, they expect the uncertainty surrounding the long-term solution to the COVID-19 pandemic and excess Government spending in 2021 to weigh on growth prospects.

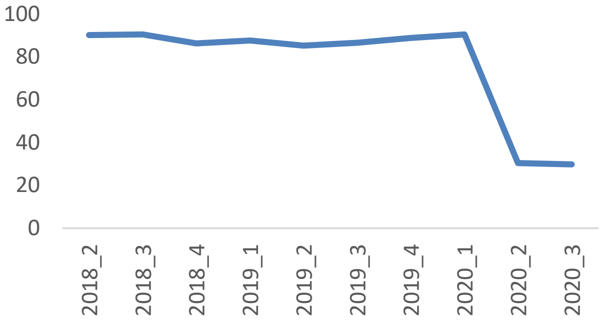
1.0 Introduction

The Quarterly Survey of Business Opinions and Expectations (QSBOEs) provides useful information about current and future economic activity which informs policy decisions. The Survey provides an indication of likely future developments given the dominant role that expectations play in shaping economic behaviour. Further, the Survey acts as a supplementary tool to providing information on the business community's opinions and expectations about the current and future direction of the economy.

This report presents findings of the Survey conducted in September 2020 on business opinions and expectations for the third and fourth quarters of 2020, respectively.

A total of 289 firms were surveyed, out of which only 86 responded representing a response rate of 29.8% (Chart 1).

Chart 1: Response Rate(%)



The distribution of the responses by province and sector are summarised in Tables 1 and 2, respectively .

Table 1: Distribution of Responses by Province

Province	Frequency	Percent
Lusaka	17	19.8
Copperbelt	22	25.6
Southern	6	7.0
Central	18	20.9
North-Western	9	10.5
Eastern	1	1.2
Luapula	4	4.7
Northern	5	5.8
Muchinga	4	4.7
Total	86	100

Table 2: Distribution of Responses by Sector

Sector	Frequency	Percent
Manufacturing	23	26.7
Wholesale and Retail	13	15.1
Service	10	11.6
Tourism	27	31.4
Construction	1	1.2
Agriculture	12	14.0
Total	86	100

Reduced working hours, rotational working sequences and work-from-home arrangements induced by COVID-19 has contributed to the poor response rate in the last two Surveys. In addition, prolonged hours of electricity load shedding negatively impacted the ability of respondents working-from-home in completing questionnaires. A large number of respondents are yet to adjust to the current exclusively impersonal data collection method that includes electronic mail and telephone calls. In the past, actual physical visitation by Bank of Zambia officials made a significant difference to achieve high response rates above 75%. In addition, some respondents were frustrated and unwilling to participate in the Survey due to the poor performance of their businesses in view of the general low economic activity occasioned by COVID-19. Given this low response rate, the Survey results may not be as representative of the sectors and should therefore be used with care.

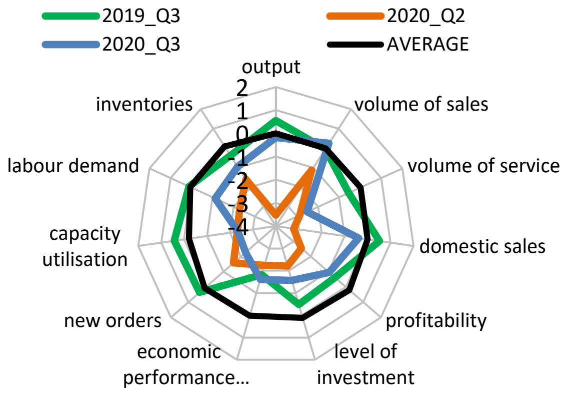
This Report is divided into four sections. Section 2 presents responses on firms's opinion on economic performance during the third quarter and expectations for the fourth quarter as well as 12 months ahead. Section 3 presents opinions on input costs, wages, selling prices and profitability for the third quarter and expectations for the fourth quarter. Section 4 provides expectation of the monetary policy stance in the fourth quarter. Section 5 concludes. The Survey methodology is described in the Appendix.

2.0 Opinion on Economic Performance in the Third Quarter of 2020 and Expectations of Economic Activity in the Fourth Quarter of 2020 and 12 Months Ahead

Economic performance marginally improved but remained below the long-term average; expected to improve further over the next 12 months

The Survey results indicate a favourable economic performance during the third quarter relative to the second quarter (Chart 2). The volume of sales exceeded its long-term average and the previous quarters' expectations. Other indicators such as volume of service, domestic sales, profitability, level of investment, economic performance, labour demand, inventories and output improved relative to the second quarter except for new orders. New orders remained subdued due to low demand occasioned by rising inflation and a weaker Kwacha. Capacity utilisation was unchanged for the second consecutive time as production costs rose and electricity load shedding persisted.

Chart 2: Business Opinions Response Patterns*

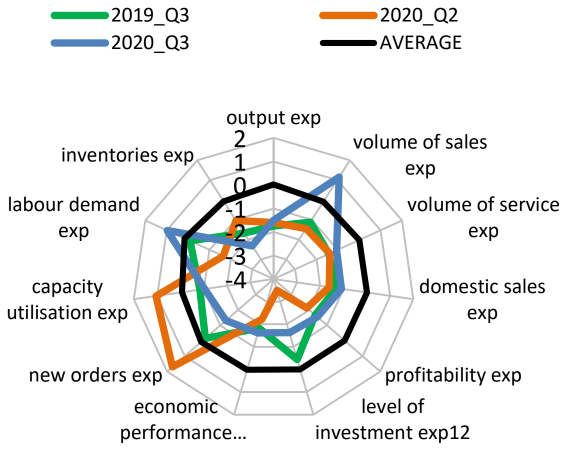


*Note: The survey indicators are standardised net balances with mean=0 and standard deviation=1. A value within the black circle entails weaker economic conditions than historical average and a value outside the black line is better than historical average.

The improvement in economic performance was largely attributed to the moderate relaxation of COVID-19 containment measures, which resulted in increased economic activity.

Economic activity is expected to continue improving in the fourth quarter as labour demand and high volume of sales increase. This is explained by improved activity in the agriculture as well as wholesale and retail sectors. Specifically, the planting season is expected to increase demand for labour and agricultural inputs. In addition, the expected increase in consumer demand during the festive season is likely to increase the volume of sales and labour demand for the wholesale and retail sector. However, persistent exchange rate depreciation, electricity load shedding and the associated rise in input costs will continue to weigh on economic activity. This is likely to be exercerbated by continued tight credit conditions due to elevated public debt (Chart 3).

Chart 3: Business Expectations Response Patterns



Note: exp referes to expectation

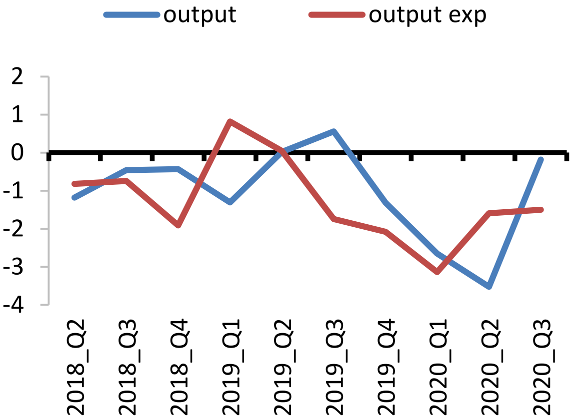
Firms are more optimistic about economic performance over the next 12 months as the adverse effects of COVID-19 are expected to begin to diminish. This is despite the constraints on growth highlighted above.

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

(Net balance, -0.10; Q2 2020, -0.68)

Despite remaining below its long-term average, output was better in the third quarter (Chart 4). This was largely due to improvements in agricultural output following the harvest of wheat and maize seed.

Chart 4: Opinion on Output



Note: exp referes to expectation

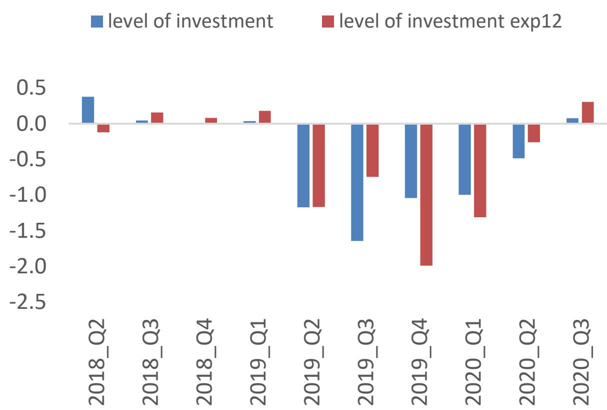
However, output is expected to remain constrained in the fourth quarter mainly due to high production costs attributed to persistent loadshedding and weaker Kwacha.

2.2 How was your firm's level of investment?

(Net balance, -0.22; Q2 2020, -0.30)

Total investment by the business community improved during the third quarter (Chart 5). This was largely driven by the expansion of branch networks and refurbishment of office buildings by some financial institutions.

Chart 5: Level of Investment



Note: exp referes to expectation

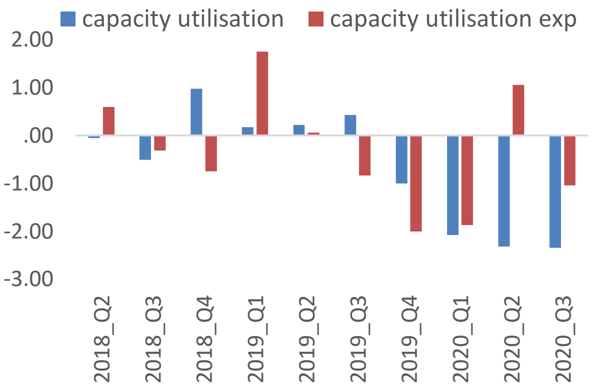
Total investment is expected to continue on a recovery path over the next 12 months, driven by plant and machinery expansionary by some milling companies and financial institutions.

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

(Net balance, 0.00; Q2 2020, -0.59)

Capacity utilisation remained weak and below the long-term average in the manufacturing sector during the third quarter. This was mainly on account of relatively low demand for mealie meal as consumers looked for cheaper alternative processing sources for maize grain, high cost of production and persistent electricity load shedding (Chart 6).

Chart 6: Capacity Utilisation



Note: exp referes to expectation

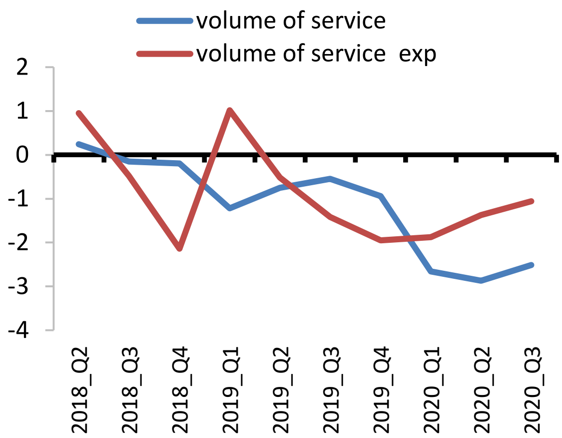
In the fourth quarter, capacity utilisation is expected to remain subdued. Sustained electricity loadshedding and high input costs exacerbated by COVID-19 are expected to adversely affect capacity utilisation.

2.4 What has been your firm's experience with respect to the volume of service?

(Net balance, -0.68; Q2 2020, -0.76)

The volume of service improved slightly during the third quarter as measures to control the spread of COVID-19 pandemic were eased (Chart 7). However, the volume of service remained below the long-term average largely on account of the slow uptake of physical conferencing facilities following the widespread use of virtual meeting facilities. In addition, the depreciation of the Kwacha, rising inflation and the decline in consumer demand contributed to the negative outturn.

Chart 7: Volume of Service



Note: exp referes to expectation

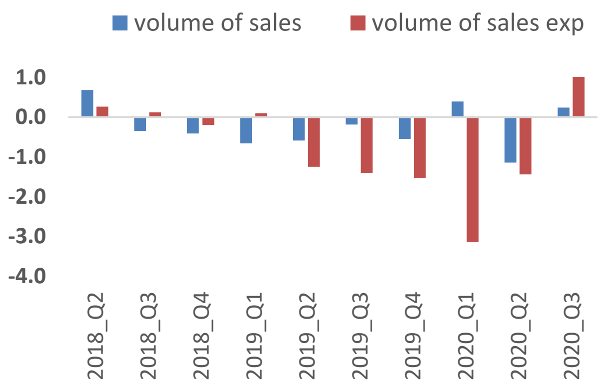
In the fourth quarter, the volume of service is expected to pick up further, albeit at a slow rate, as demand generally gains momentum following the relaxation of the COVID-19 containment measures.

2.5 What has been your firm's experience with respect to the volume of sales?

(Net balance, -0.20; Q2 2020, -0.75)

The volume of sales rebounded in the third quarter based on improved consumer demand following the partial relaxation of COVID-19 pandemic prevention measures (Chart 8).

Chart 8: Volume of Sales



Note: exp referes to expectation

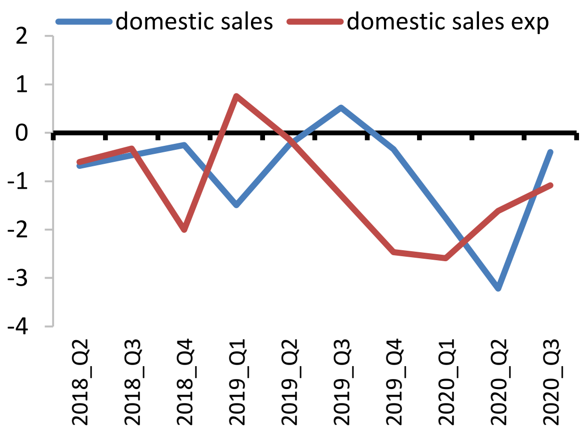
The volume of sales is expected to remain high and exceed the long-term average in the fourth quarter. This is largely premised on the anticipated increase in demand for goods and services during the festive season as well as agricultural inputs following the commencement of the planting season.

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

(Net balance, -0.15; Q2 2020, -0.67)

Domestic sales improved in the third quarter largely due to the partial relaxation of COVID-19 pandemic restrictions (Chart 9). However, domestic sales remained below the long-term average due to low demand attributed to rising inflation, stiff competition from cheaper imports and the prolonged negative impact of COVID-19 pandemic.

Chart 9: Domestic Sales



Note: exp referes to expectation

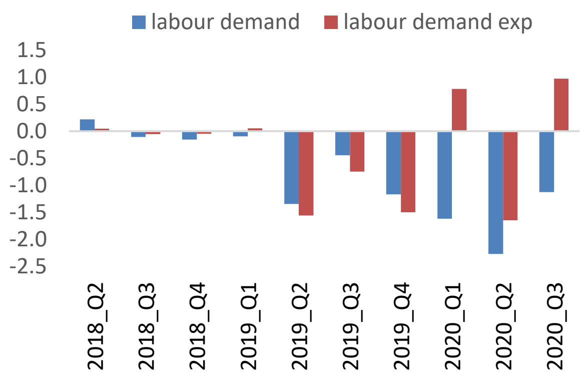
In the fourth quarter, domestic sales are expected to continue rising as the adverse effects of COVID-19 dissipate and demand recovers.

2.7 How do you rate your firm's labour demand?

(Net balance, -0.27; Q2 2020, -0.49)

Labour demand improved but remained below the long-term average (Chart 10). Increased social gatherings following moderation in COVID-19 confinement measures had a positive impact on labour demand. However, the rise in operating costs associated with sustained electricity loadshedding, reduced profitability and tight credit conditions were cited as the drivers of subdued labour demand. To sustain business operations, some firms layed off employees.

Chart 10: Labour Demand



Note: exp referes to expectation

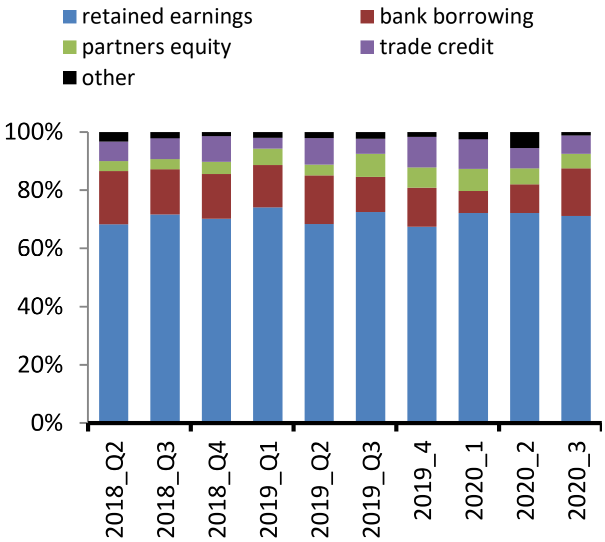
Labour demand is expected to continue rising and may exceed the long-term average in the fourth quarter on anticipated increase in agricultural activities and festive season-related sales.

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

Retained earnings remained the main source of investment finance and working capital in the third quarter, with 69.6% and

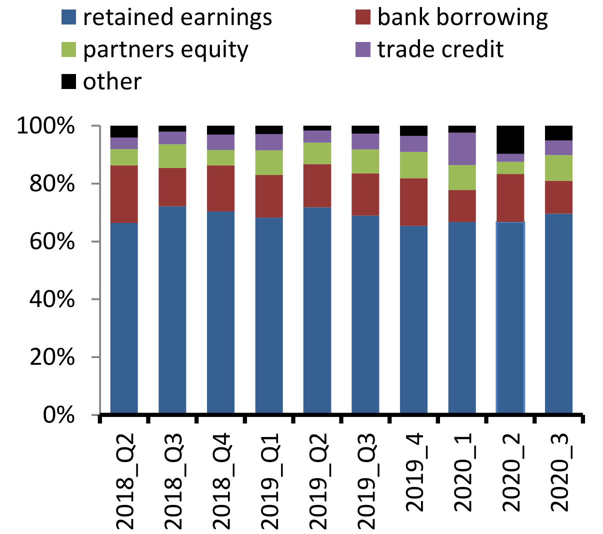
71.3% response rates from 66.7% and 72.2% in the second quarter, respectively (Charts 11A and 11B). This was followed by bank borrowing.

Chart 11A: Sources of Investment Finance



Note: exp referes to expectation

Chart 11B: Sources of Working Capital



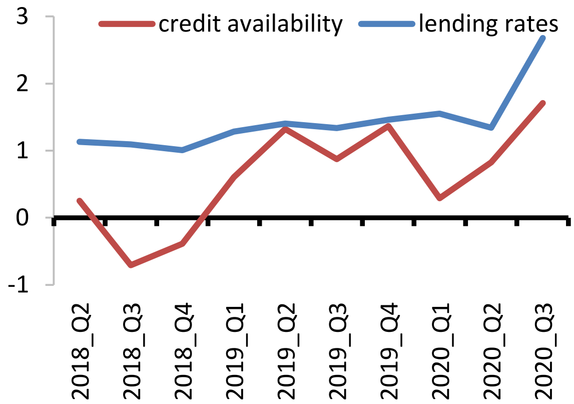
Note: exp referes to expectation

2.9 What is your perception of the current availability of credit?

(Net balance, 0.79; Q2 2020, 0.71)

Despite consecutive reductions in the monetary policy rate and the introduction of the Bank of Zambia Targeted Medium-Term Refinancing Facility (TMTRF), persistently tight credit conditions were reported for the third quarter (Chart 12). This was mainly reflected in relatively high lending rates and stringent lending conditions offered by Financial Service Providers. Tight credit conditions were largely attributed to sustained high Government borrowing and low appetite by banks to lend mainly due to negative growth occasioned by COVID-19.

Chart 12: Credit Availability and Lending Rates



Note: exp referes to expectation

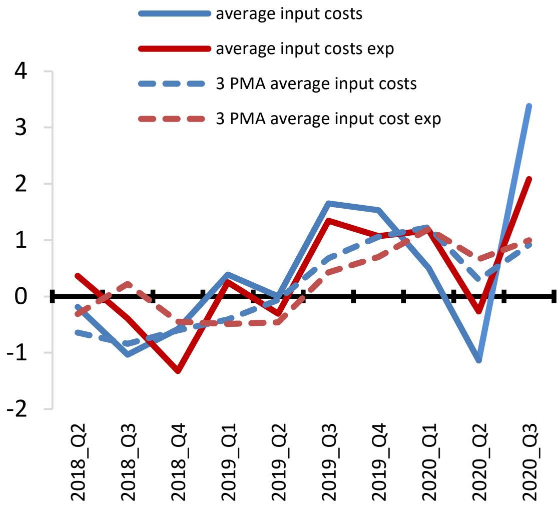
3.0 Evolution of Costs, Wages and Selling Prices

3.1 What has been your firm's experience with average input costs?

(Net balance, 0.72; Q2 2020, 0.19)

A weaker Kwacha and disruption in the flow of raw materials, especially imports due to COVID-19, are reported to have been the keys driver of rising input costs in the third quarter. Seasonal increases in the cost of labour and electricity loadshedding compounded the situation (Chart 13).

Chart 13: Average Input Costs



Note: exp referes to expectation

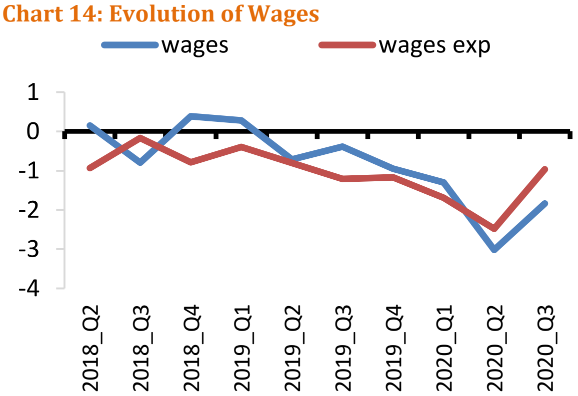
A rising trend in input costs is expected to continue in the fourth quarter on account of the depreciation of the Kwacha, sustained electricity loadshedding and the effects of COVID-19 restrictive measures.

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

(Net balance - 0.02; Q2 2020, -0.13)

The wage bill increased in the third quarter, but remained below the long-term average. This was largely on account of the increase in working hours following the partial relaxation of COVID-19 restrictions (Chart 14).

Chart 14: Evolution of Wages



Note: exp referes to expectation

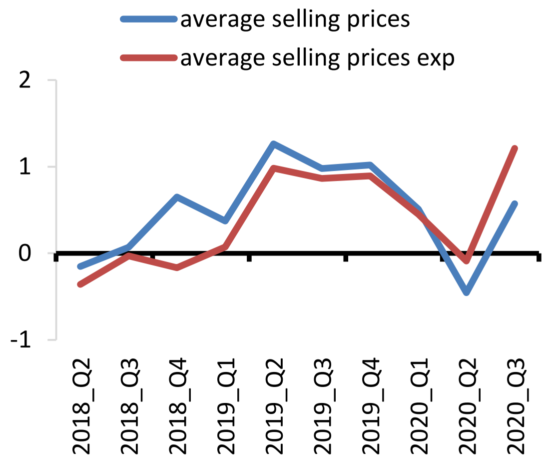
Firms expect a further rise in the wage bill in the fourth quarter as working arrangements normalise in line with the relaxation in COVID-19 pandemic restrictions, and seasonal demand for labour picks-up during the planting season.

3.3 What has been your firm's experience with respect to average selling prices?

(Net balance, 0.12; Q2 2020, -0.06)

Average selling prices increased in the third quarter and will continue in the next quarter mainly due to the depreciation of the Kwacha, increased input costs and rising inflation (Chart 15).

Chart 15: Evolution of Average Selling Prices



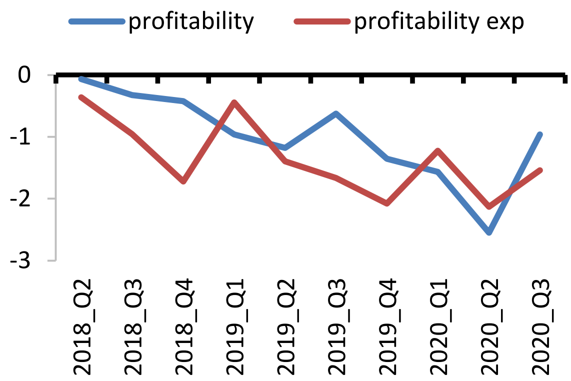
Note: exp referes to expectation

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

(Net balance, -0.57; Q2 2020, -0.81)

The third quarter posted a slight improvement in profitability and remained below the long-term average (Chart 16). The low profits were attributed to the increase in input costs largely due to the depreciation of the Kwacha and promotional prices to maintain the customer base in the wake of depressed demand induced by COVID-19.

Chart 16: Profitability



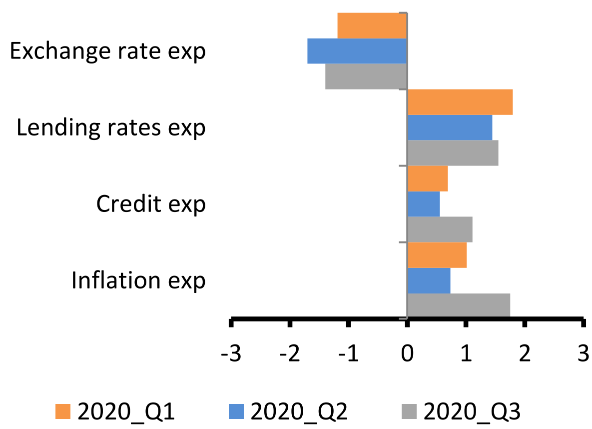
Note: exp referes to expectation

Profitability is expected to pick up in the fourth quarter as demand gains momentum with the re-opening of the economy.

4.0 Expectations of Monetary Policy for Fourth Quarter 2020

Firms expect the exchange rate to continue depreciating in the fourth quarter, but at a reduced pace. Lending rates and inflationary pressures are expected to remain high while credit will continue to be tight (Chart 17).

Chart 17: Inflation, Exchange Rates and Lending Rates Expectations



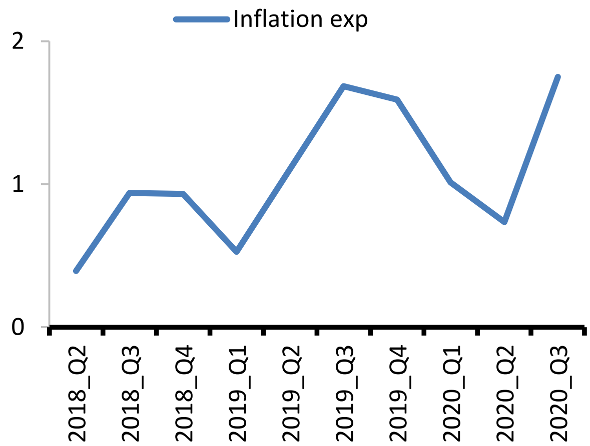
Notes:
- *Exp referes to expectation*
- *Exchange rate = appreciation, strong (+)/depreciate, weak (-)*
- *Lending rates = increase, high (+)/decrease, low (-)*
- *Credit conditions = tight (+)/ loose (-)*
- *Inflation expectations = increase, high (+)/decrease, low (-)*

4.1 What do you expect the price level to be over the next quarter?

(Net balance, 0.80; Q2 2020, 0.56)

Inflationary pressures are expected to continue rising in the fourth quarter (Chart 18). This is largely on account of anticipated persistent depreciation of the Kwacha, low supply of imports, and high production costs related to increased loadshedding.

Chart 18: Inflationary Expectations Next Quarter



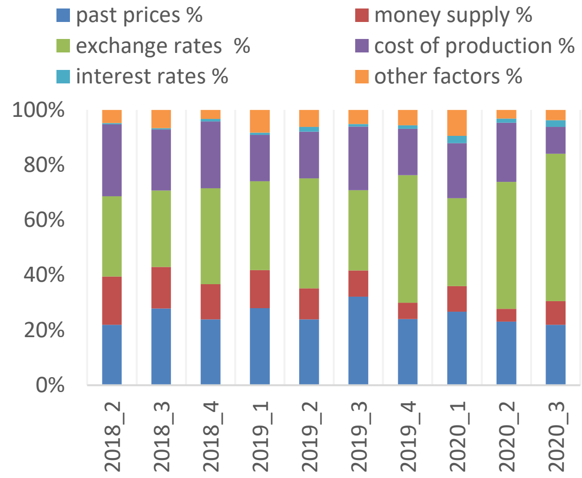
Note: exp referes to expectation

In the next 12 months, inflationary pressures are expected to continue rising on account of the depreciation of the Kwacha, high production costs as well as the anticipated excess Government spending in 2021.

4.2 What is the main factor explaining your expectations of inflation?

The main factor explaining inflationary expectations is the anticipated depreciation of the Kwacha, past inflation, high production costs and money supply (Chart 19).

Chart 19: Key Drivers of Inflationary Expectations

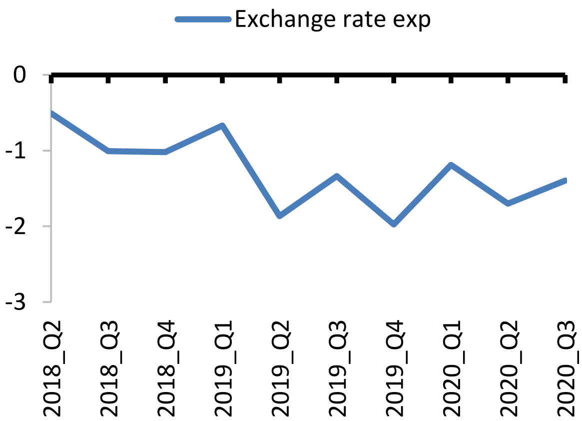


4.3 How do you expect the performance of the Kwacha against the US dollar to be at the end of the next quarter?

(Net balance, -0.63; Q2 2020, -0.72)

The Kwacha is expected to continue depreciating mainly due to the adverse effects of COVID-19 pandemic, uncertainty about Zambia's debt position and inflationary expectations (Chart 20).

Chart 20: Exchange Rate Expectations Next Quarter



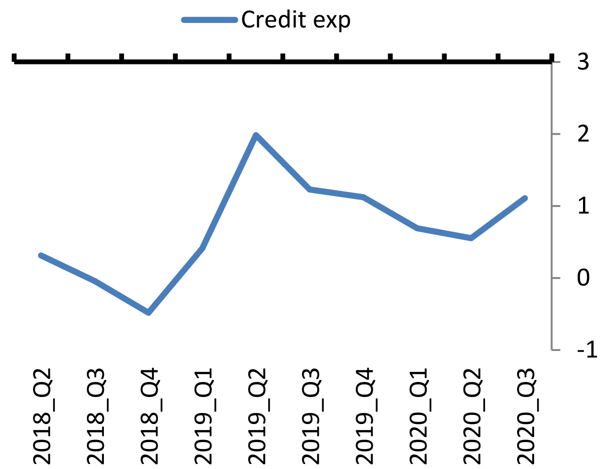
Note: exp referes to expectation

4.4 Over the next quarter, how do you expect credit availability to be?

(Net balance, 0 .69; Q2 2020, 0.64)

Credit availability is expected to rise in the fourth quarter (Chart 21). This notwithstanding, access to credit is expected to be constrained by continued high Government borrowing, uncertainty about finding a long-term solution to the COVID-19 pandemic and low supply of foreign currency denominated loans.

Chart 21: Credit availability expectations next quarter



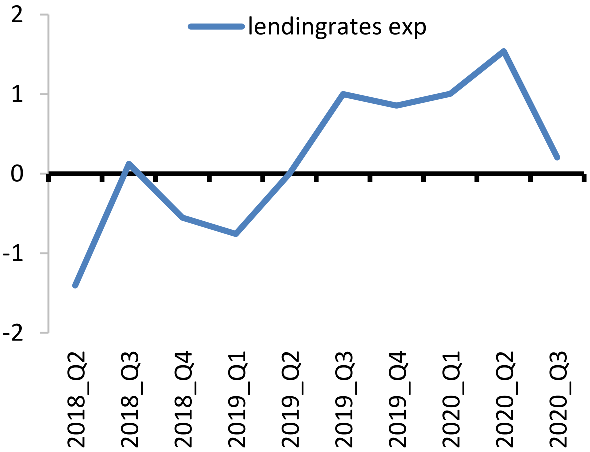
Note: exp referes to expectation

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

(Net balance, 0.81; Q2 2020, 0.77)

In the next quarter, commercial banks' lending rates are expected to reduce but will remain above the historical average (Chart 22). High Government borrowing and inflationary pressures are expected to contribute to relatively high lending rates.

Chart 22: Interest Rate Expectations Next Quarter



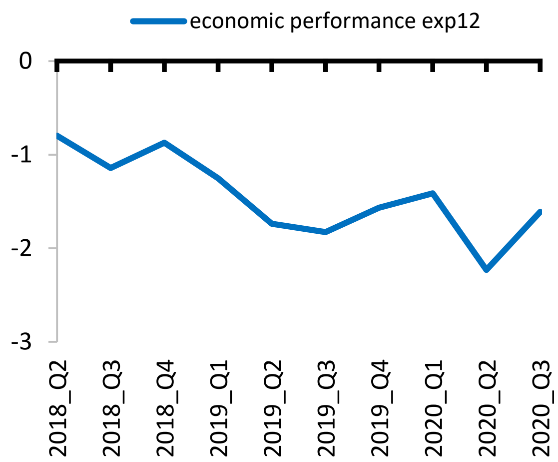
Note: exp referes to expectation

4.6 What is your expectation of the performance of the economy in the next 12 months?

(Net balance, -0.46; Q1 2020, -0.49)

Economic performance is expected to pick up, but will remain below the historical mean (Chart 23). The reduction in COVID-19 pandemic cases and the subsequent rise in economic activity are expected to underpin growth. On the other hand, firms expect the continued depreciation of the Kwacha, rising inflationary pressures, high production costs and tight credit conditions to continue weighing on growth.

Chart 23: Economic Performance in the Next 12 Months



Note: exp referes to expectation

5.0 Conclusion

In comparison to the high pessimism expressed by firms in the second quarter about growth prospects, this Survey has revealed improvements in opinions about the performance of the economy from the third quarter of 2020 up to the third quarter of 2021 .

The third quarter outturn reflected, to a large extent, increased volume of sales, output, domestic sales and profitability. This positive performance was attributed to the relaxation of COVID-19 containment measures leading to the pick-up in economic activity in most across.

The reduction in COVID-19 pandemic cases and the subsequent relaxation of containment measures are expected to invigorate economic activity from the fourth quarter of 2020. However, the continued depreciation of the Kwacha, rising inflationary pressure, high production costs, and tight credit conditions are expected to continue weighing on growth. Firms remain unclear about a COVID-19 long-term solution and growth prospects.

Appendix I - Survey Methodology

Data collection for the Quarterly Survey of Business Opinions and Expectations is done through a questionnaire 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 12 months ahead. The questionnaire is administered to a sample of respondents in manufacturing, trading, tourism and services, construction, and agriculture sectors selected on the basis of their contribution to GDP.

The Survey covers the Copperbelt (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) Provinces.

Data analysis is undertaken based on Net Balance Statistic (*N*) methodology where qualitative responses are converted into quantitative measures as follows:

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

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

The Net Balance Statistic method is widely used in the analysis of survey data and has the advantage of detecting the directional changes in performance/expectations of respondents in surveys. It 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. On the other hand, a negative net percentage means a decrease/deterioration/loosening, depending on the variable under consideration.