Quarterly Survey of Business Opinions and Expectations

Second Quarter 2021

July 2021, Volume 31 (2)

Bank *of* Zambia

Bank of Zambia

REGISTERED OFFICES

Head Office

Bank of Zambia, Bank Square, Cairo Road P. O. Box 30080, Lusaka, 10101, Zambia Tel: (+260) 211 399300
E-mail: info@boz.zm

Website: www.boz.zm

Regional Office

Bank of Zambia, Buteko Avenue, P. O. Box 71511, Ndola, Zambia Tel: (+260) 212 399600
E-mail: info@boz.zm

Website: www.boz.zm

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Summary

Economic performance remained subdued in the second quarter of 2021 as all monitored indicators remained below the long-term average with the exception of seasonal agricultural related activities. This was mainly due to the negative impact of the third wave of the COVID-19 pandemic. The business community expects economic activity to continue to underperform in the third quarter and 12 months ahead owing to the persistent depreciation of the Kwacha, high inflationary pressures, high public debt service and uncertainity associated with post-election.

1.0   Introduction

The Bank of Zambia Quarterly Survey of Business Opinions and Expectations (QSBOEs) gauges the perspectives of the business community about prevailing macroeconomic conditions which form part of monetary policy decisions.

This Report presents findings of the Survey conducted in June on business opinions and expectations for the second and third quarters of 2021, respectively.

A total of 271 questionnaires were administered, out of which 81 responses were received. This represents a response rate of 29.9%, a deterioriation from 43.2% in the previous survey (Chart 1).

Chart 1: Response Rate (%): 2019Q3-2021Q2
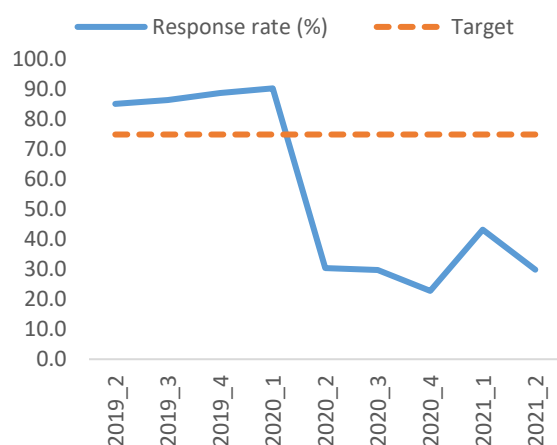
Source: Bank of Zambia

The highest response rates were recorded in Copperbelt, Central and Southern Provinces (Table 1). Increased COVID-19 infection and mortality rates, particularly in Lusaka Province, accounted for the lower response rate. In view of this, the Survey results must be interpreted with caution.

Table 1: Distribution of Responses by Province

Province	Frequency	Percent
Copperbelt	23	28.4
Central	21	25.9
Southern	10	12.3
Luapula	7	8.6
Eastern	5	6.2
Northern	5	6.2
Lusaka	4	4.9
Muchinga	4	4.9
North-Western	2	2.5
Total	81	100.0

Source: Bank of Zambia

The highest sectoral response rates were from the tourism, manufacturing and agricultural sectors while construction and services sectors recorded the lowest response rates (Table 2).

Table 2: Distribution of Responses by Sector

| Sector	Frequency	Percent
Tourism	28	34.6
Manufacturing	17	21.0
Agriculture	14	17.3
Merchant	13	16.0
Service	8	9.9
Construction	1	1.2
Total	81	100

Source: Bank of Zambia

The rest of the Report is organised as follows: Section 2 presents opinions of firms about economic performance during the second quarter as well as expectations for the third quarter and 12 months ahead. Section 3 provides opinions on input costs, wages, prices and profitability. Section 4 presents expectations about the monetary policy stance in the third quarter and the performance of the economy one year ahead. Section 5 concludes. A brief description of the Survey methodology is provided in the appendix.

2.0 Economic Performance in the Second Quarter of 2021 as well as Expectations of Economic Activity in the Third Quarter of 2021 and 12 Months Ahead

Economic performance weakened in the second quarter, expected to remain subdued 12 months ahead

Contrary to optimistic business expectations in the first quarter, economic performance remained subdued in the second quarter. The severe third wave of the COVID-19 pandemic, contributed to the unfavourable economic performance. The volume of sales, profitability, new orders, capacity utilisation and level of investment were below the first quarter levels. In contrast, seasonal agricultural related activities (output, volume of service, labour demand, inventories and domestic sales) improved (Chart 2).

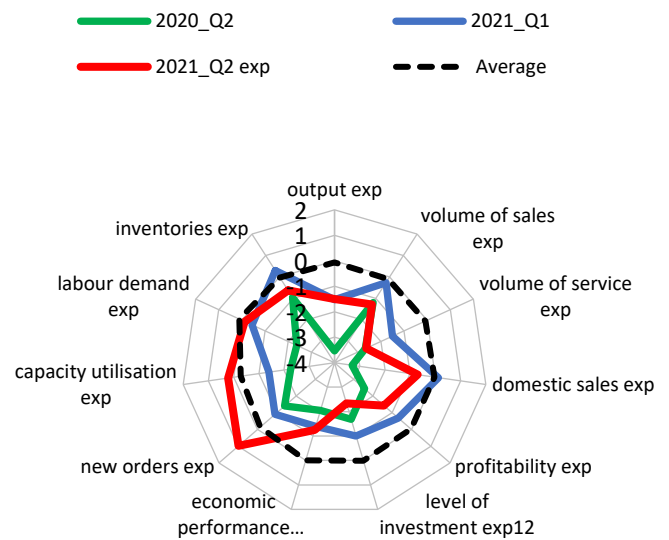**Chart 2: Business Opinion Response Patterns***
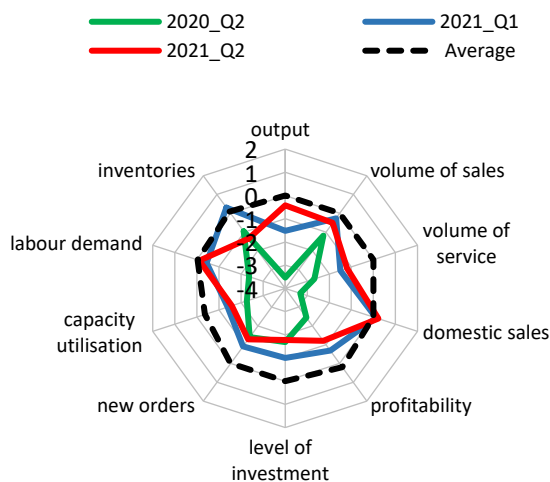
***Note**: The Survey indicators are standardised net balances of mean =0 and standard deviation=1. A value below the average indicates weaker economic performance while above the average indicates improved economic performance.

Firms expect new orders and capacity utilisation to exceed the long-term average in the third quarter. This largely reflects higher agricultural output, especially of maize following a record harvest in the 2020/2021 farming season, which is expected to trigger more manufacturing activity. The general economic outlook for the third quarter, however, remains weak (Chart 3).

Chart 3: Business Expectations Response Patterns

Note: The Survey indicators are standardised net balances of mean=0 and standard deviation=1.A value below the average indicates weaker economic perfomamnce while above average indicates imrpoved economic perfomamnce.

Over the next 12 months, growth prospects remain weak mainly due to uncertainity relating to post-election Governmnet policies coupled with persistent depreciation of the Kwacha and high inflation.

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

(Net balance, -0.14; Q1 2021 -0.33)

Output improved in the second quarter, but remained below the long-term average (Chart 4). This was largely attributed to the maize bumper harvest which subsequently, influenced output in the manufacturing sector.

Chart 4: Opinion on Output
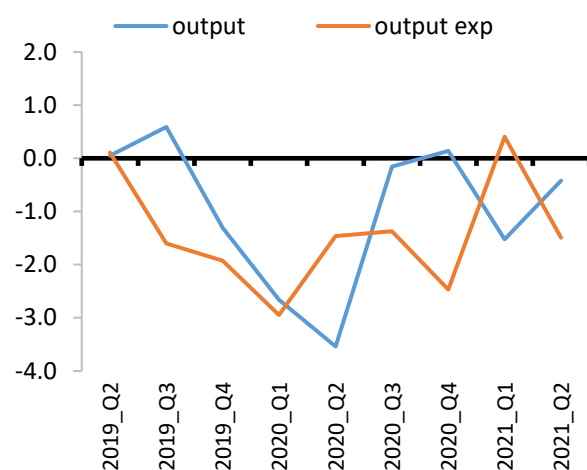
Note: The line at zero (0.0) represents the long-term average and it applies to all graphs in the report.
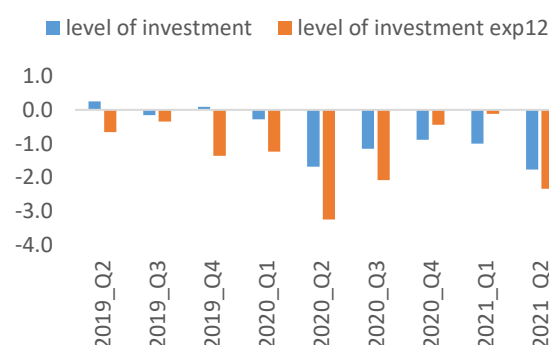
Source: Bank of Zambia

Firms, however, expect output to decline in the third quarter mainly due to seasonal fluctuations in agricultural output and the rise in input costs on account of the depreciation of the Kwacha.

2.2 How was your firm's level of investment?

(Net balance, -0.32; Q1 2021 -0.20)

The level of investment deteriorated further during the second quarter as some companies diverted funds reserved for investment to respond to the third wave of COVID-19 (Chart 5). In addition, low demand, high production costs, largely attributed to a weak Kwacha coupled with reduced profit margins, continued to affect investment appetite.

Chart 5: Level of Investment

Source: Bank of Zambia

Firms expect investment levels to deteriorate further in the next 12 months mainly due to uncertainty relating to Government policy after the General Elections, sustained depreciation of the Kwacha, high inflationary pressures and Government debt service obligations.

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

(Net balance, -0.47; Q1 2021 -0.21)

Capacity utilisation deteriorated further in the second quarter and remained below the long-term average (Chart 6). The third wave of the pandemic largely disrupted operations reinforced by the high cost of production.

Chart 6: Capacity Utilisation
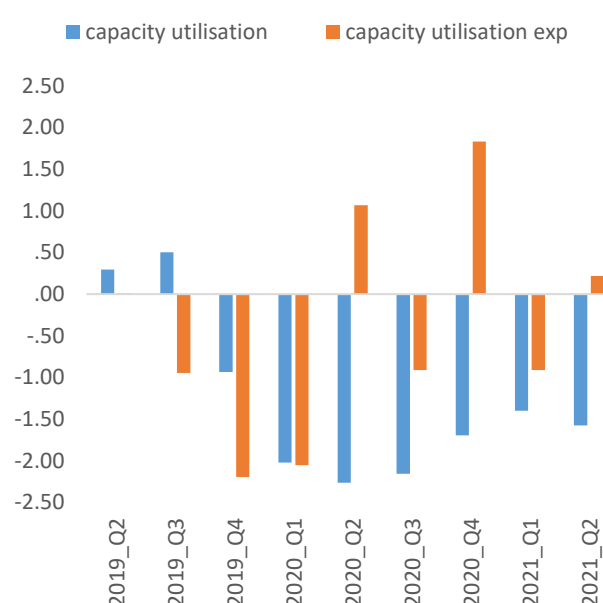
Source: Bank of Zambia

However, capacity utilisation is expected to rise sharply in the third quarter owing to increased supply of agricultural related raw materials and as economic activity is revived partly by the on-going COVID-19 vaccination programme.
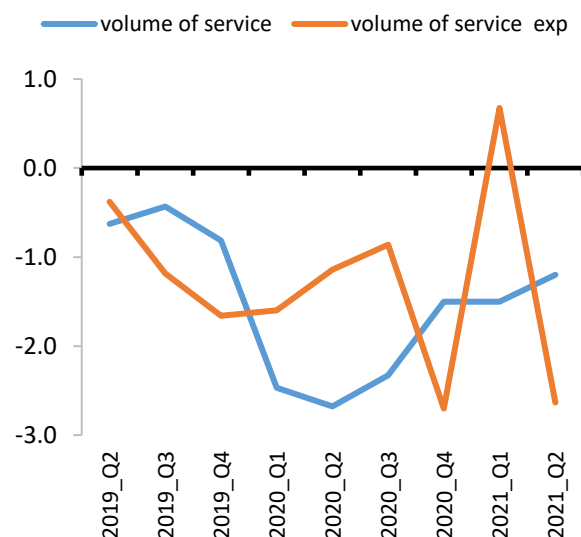
2.4 What has been your firm's experience with respect to the volume of service?

(Net balance, -0.41; Q1 2021, -0.48)

Despite remaining below the long-term average, the volume of service improved slightly in the second quarter (Chart 7). The provision of agricultural related services (i.e repair and maintenance of agricultural equipment as well as transportation of output and storage) mainly accounted for the

increase. On the other hand, the tourism sector continued to underperform largely due to the negative effects of the COVID-19 pandemic.

The volume of services is expected to fall in the third quarter as agricultural related services (i.e transportation of produce to storage facilities) reduce.

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

(Net balance, -0.50; Q1 2021, -0.41)

The volume of sales declined further in the second quarter and remained below the long-term average (Chart 8). This was largely on account of subdued consumer demand occasioned by the slowdown in economic activity due to the marked increase in COVID-19 infections. The depreciation of the Kwacha further depressed the volume of sales.
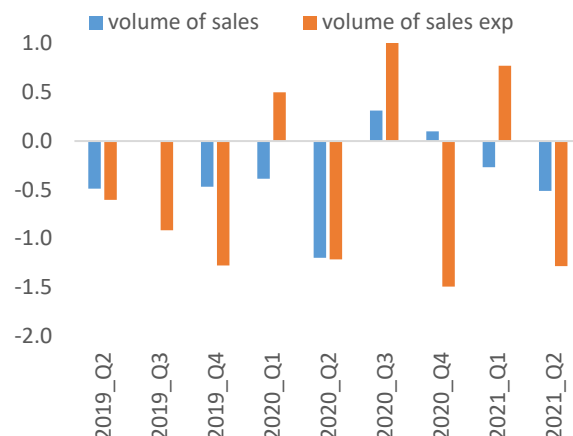
The volume of sales is expected to continue to underperform in the third quarter owing to the influence of a weaker Kwacha and the associated high inflationary pressures.

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

(Net balance, -0.04; Q1 2021, -0.06)

Consistent with business expectations, domestic sales rose in the second quarter albeit marginally on account of increased agricultural output (Chart 9).
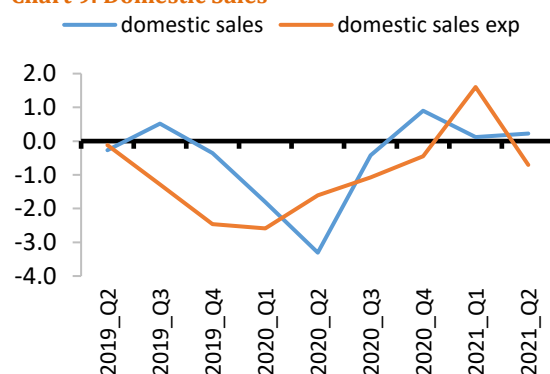
Domestic sales in the agricultural and manufacturing sectors are, however, expected to decline in the third quarter as agricultural output reduces and the Kwacha depreciates further.

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

(Net balance, -0.14; Q1 2021, -0.17)

Labour demand improved during the quarter, but remained below the long-term average (Chart 10). This was largely due to crop harvest related activities.

Chart 10: Labour Demand
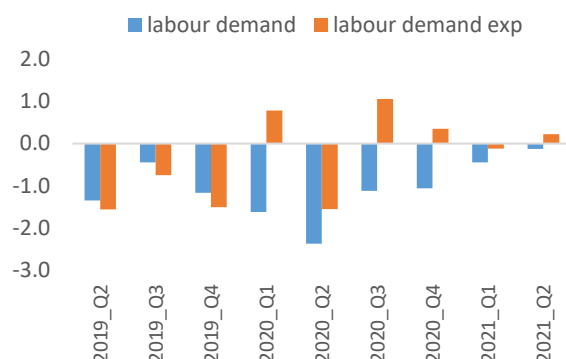
Source: Bank of Zambia

Labour demand is expected to rise further in the third quarter, supported by the pick up in economic activity boosted by the anticipated successful COVID-19 vaccination programme.

2.8 What is your current main source of investment finance and working capital?
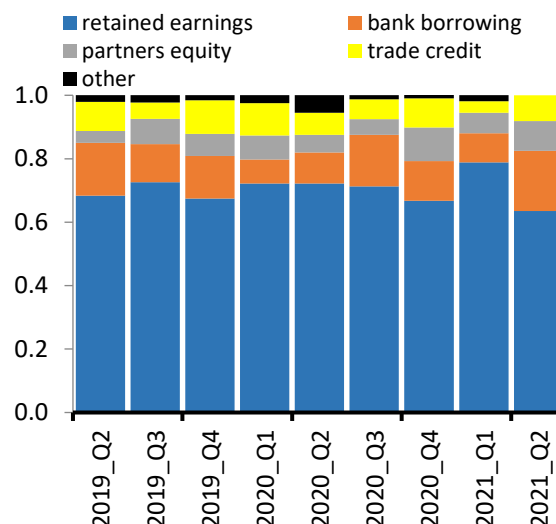
Retained earnings remained the main source of investment finance and working capital followed by bank borrowing and partners' equity (Charts 11A and 11B).

Chart 11A: Sources of Investment Finance
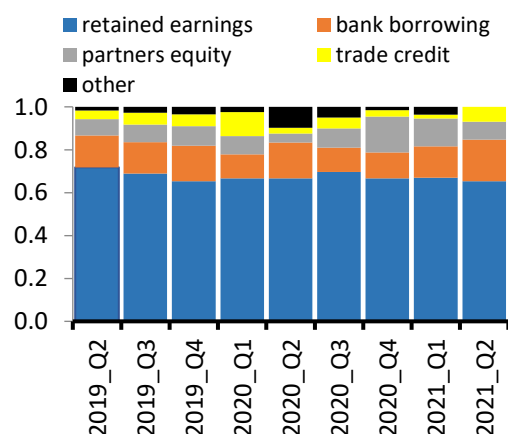
Source: Bank of Zambia

**Chart 11B: Sources of Working Capital**

Source: Bank of Zambia

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

(Net balance, -0.82; Q1 2021, -0.62)

Firms indicated that credit availability remained tight and lending rates rose in the second quarter. This was attributed to heightened default risk occasioned by the third wave of the COVID-19 pandemic and high inflation (Chart 12).

Chart 12: Credit Availability and Lending Rates
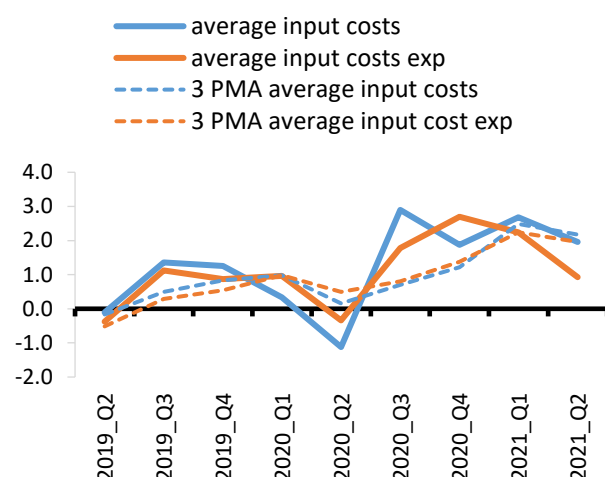

Source: Bank of Zambia

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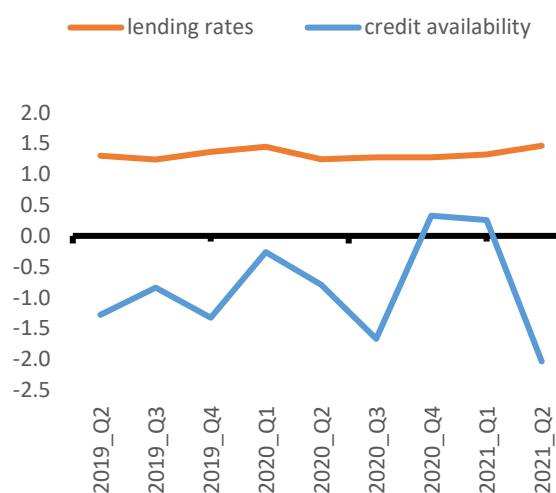
3.0   Evolution of Costs, Wages and Prices

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

(Net balance, 0.60; Q1 2021, 0.69)

Average input costs fell in the second quarter and the trend is likely to continue in the third quarter. This was mainly due to increased supply of cheaper agricultural raw materials such as maize grain to the manufacturing sector underpinned by a favourable harvest. Reduced operating costs in the tourism sector also explained the decline following a reduction in occupancy levels occasioned by the third wave of the COVID-19 (Chart 13).

Chart 13: Average Input Costs

Source: Bank of Zambia

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

(Net balance 0.08; Q1 2021, 0.12)

The wage bill declined in the second quarter mainly due to low profit margins, reduced working hours and employee redundancies induced by constrained business activity occasioned by the third wave of the COVID-19 pandemic (Chart 14). However, the wage bill is expected to pick up in the third quarter as business activity improves on optimism about the COVID-19 vaccination programme.

Chart 14: Evolution of Wages
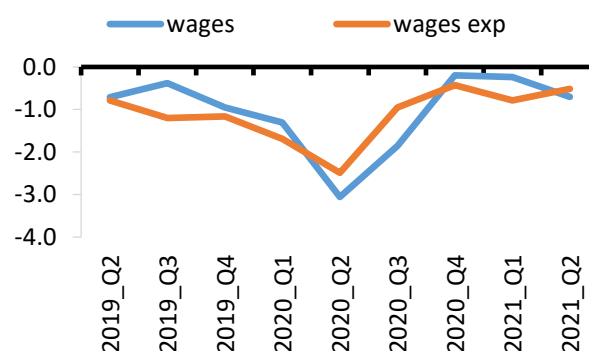
Source: Bank of Zambia

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

(Net balance, 0.32; Q1 2021, 0.38)

In the second quarter, average selling prices declined and are likely to continue on this path. This was largely due improved seasonal supply of maize grain to the manufacturing sector and promotions by most hotels, restaurants, and airlines to encourage the uptake of tourism services during the COVID-19 period (Chart 15).

**Chart 15: Evolution of Average Selling Prices**

Source: Bank of Zambia

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

(Net balance, -0.20; Q1 2021, -0.57)

Profitability declined in the second quarter and is likely to continue on this path in the third quarter. This is attributed to depressed consumer demand and elevated inflation occasioned by the third wave of the COVID-19 pandemic and the sustained exchange rate depreciation, respectively (Chart 16).
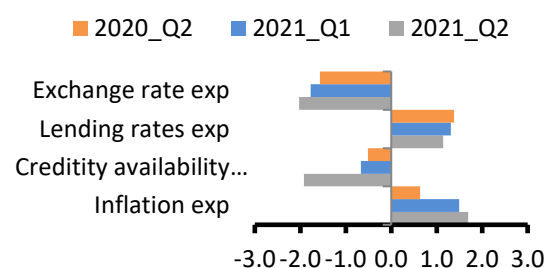
Chart 16: Profitability
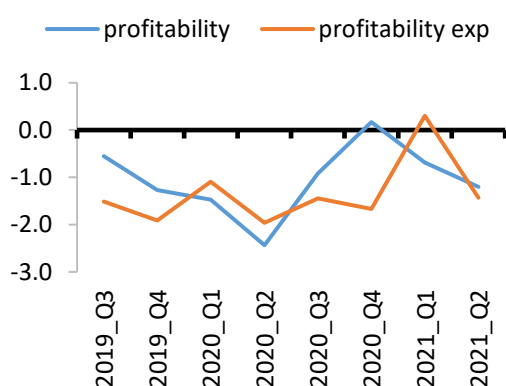
Source: Bank of Zambia

4.0 Expectations of Monetary Policy for Third Quarter 2021

The exchange rate is expected to depreciate further in the third quarter and lending rates remain elevated amid tight credit conditions and sustained inflationary pressures (Chart 17).

Chart 17: Inflation, Exchange Rates and Lending Rates Expectations

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

Source: Bank of Zambia

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

(Net balance, 0.69; Q1 2021, 0.50)

Inflationary pressures are expected to remain high in the third quarter (Chart 18). The majority of the respondents predicted inflation to be in the 23 – 25 % range (Table 3).

Chart 18: Inflationary Expectations Next Quarter
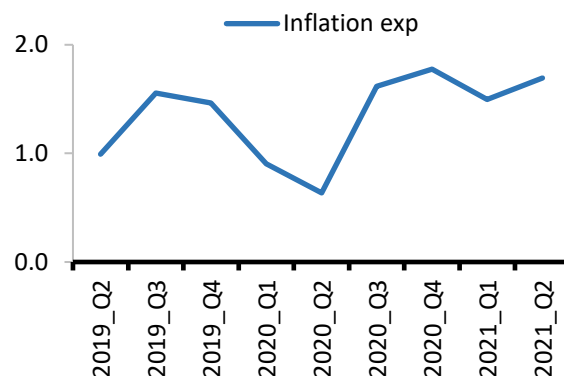
Source: Bank of Zambia
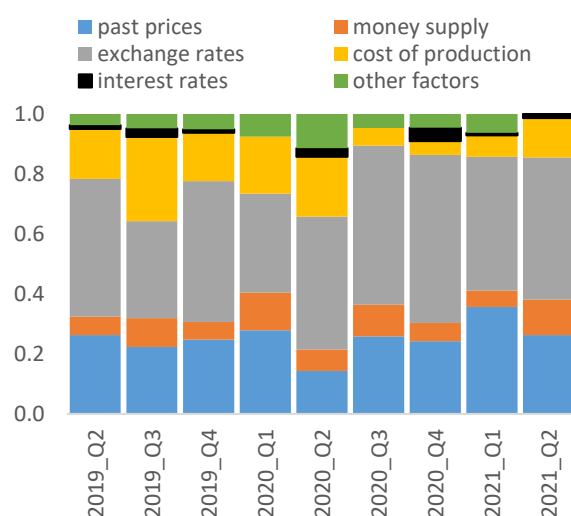
Table 3: Expected inflation rate at the end of the next quarter

Inflation Rate Ranges (%)	Frequency	Percent
11-15	1	1.2
16-19	3	3.7
20-22	5	6.2
23-25	13	16.0
26-28	4	4.9
29-31	2	2.5
38-40	2	2.5
Non response	51	63.0
Total	81	100.0

Source: Bank of Zambia

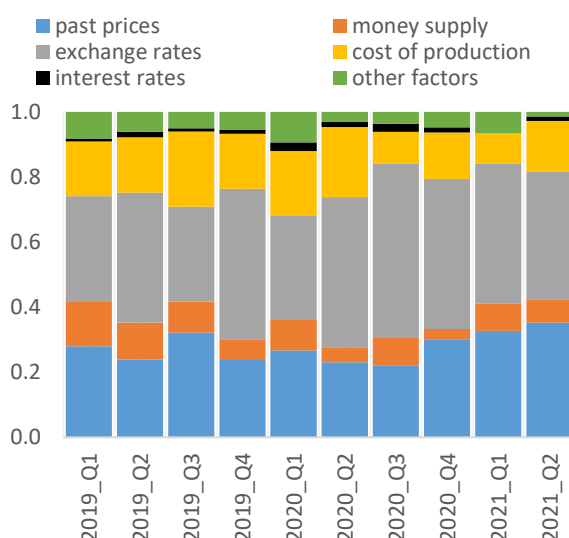## 4.2 What are the main factors explaining your expectations of inflation?

The key factors explaining inflationary expectations are exchange rate depreciation, past inflation and cost of production (Charts 19A and 19B).

Chart 19A: Key Drivers of Inflationary Expectations next Quarter

Legend: past prices, money supply, exchange rates, cost of production, interest rates, other factors

Chart 19B: Key Drivers of Inflationary Expectations next 12 Months

Legend: past prices, money supply, exchange rates, cost of production, interest rates, other factors

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, -0.86; Q1 2021, -0.78)

The Kwacha is expected to continue depreciating against the US dollar in the third quarter to between K23 and K25 (Chart 20 and Table 4). This is attributed to perceived low levels of international reserves. In addition, foreign exchange supply is viewed to

have declined mainly due to the fall in export earnings as a result of the COVID-19 pandemic.

Chart 20: Exchange rate expectations next quarter

Legend: Exchange rate exp
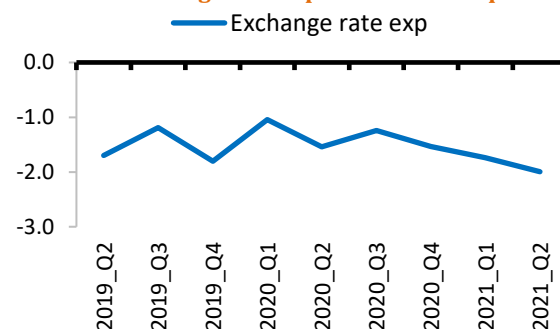
Table 4: Expected exchange rate at the end of next quarter

| Exchange Rate Ranges (K/USD)	Frequency	Percent
1-10	1	1.2
16-19	1	1.2
20-22	2	2.5
23-25	46	56.8
26-28	4	4.9
35-37	1	1.2
38-40	2	2.5
41-50	1	1.2
Non-response	23	28.4
Total	81	100.0

4.4 How do you expect credit availability to be over the next quarter?

(Net balance, -0.77; Q1 2021, - 0.65)

Tight credit conditions are expected to persist in the third quarter as credit risk associated with reduced business activity remain tight (Chart 21). As a result, most lenders are expected to implement stringent lending conditions in a bid to avert credit risk.

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**Chart 21: Credit availability expectations next quarter [1]**
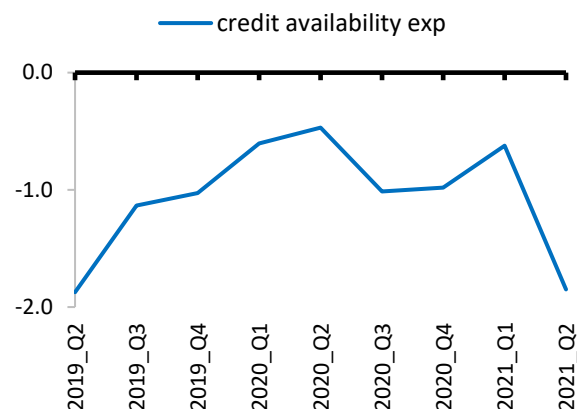
Source: Bank of Zambia

4.5 What do you expect to happen to commercial banks' lending rates over the next quarter?

(Net balance, 0.68; Q1 2021, 0.74)

Despite showing a declining trend, firms expect lending rates to remain high during the third quarter due to high inflation (Chart 22).

Chart 22: Interest rate expectations next quarter
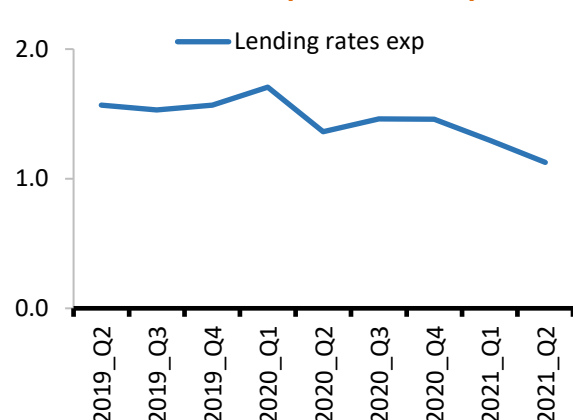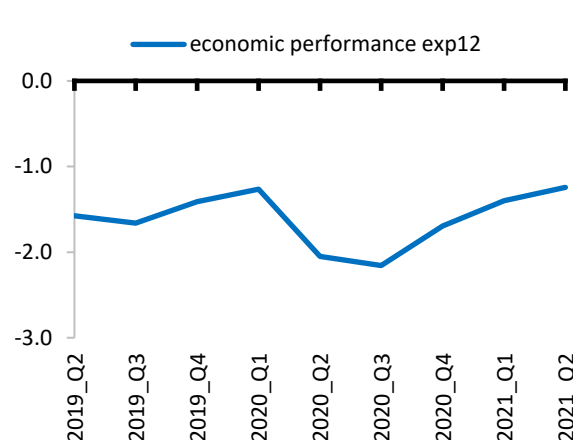
Source: Bank of Zambia

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

(Net balance, -0.23; Q1 2021, -0.28)

Economic performance is expected to remain subdued over the next 12 months (Chart 23). This is largely due to the uncertainty relating to Government policy after the General

Elections, persistent depreciation of the Kwacha and high inflation.

Chart 23: Economic Performance in the Next 12 Months

Source: Bank of Zambia

5.0 Conclusion

Contrary to business expectations in the first quarter of 2021, economic performance remained subdued in the second quarter occasioned by the third wave of the COVID-19 pandemic. Economic activity is expected to remain unfavorable in the third quarter largely on account of the lagged effect of the third wave of COVID-19, persistent depreciation of the Kwacha and the associated inflationary pressures.

Firms remain pessimistic about economic activity in the next 12 months on account of policy uncertainty post-General Elections, external debt service, sustained exchange rate depreciation and high inflation.

Appendix – 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,

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[1] Credit availability = tight (-)/ loose (+)

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 based on net balance statistic (N) methodology where qualitative responses are converted into quantitative measures as follows:

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

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 (negative) net percentage indicates that more respondents reported/expected an increase(decrease)/improvement (deteriorating) /tightening (lossening).