

The Egyptian Center for Economic Studies



Business Barometer

January 2010

Issue No. 24

Performance and Expectations of the Egyptian Business Sector

The Egyptian Center for Economic Studies (ECES) is an independent, nonprofit research institute. It was founded by leading members of Egypt's private sector in 1992. The objective of the Center is to promote economic development in Egypt by assisting policy makers in developing appropriate policy reforms based on international experience. In pursuit of this objective, ECES conducts applied policy research and disseminates its findings through a select series of publications, lectures, conferences, and roundtable discussions.

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About the Business Barometer

In an attempt to provide timely information about the state of economic activity in Egypt, ECES published the first issue of the Industrial Barometer in 1998. The periodical reported the results of a biannual survey of 165 firms fully drawn from the industrial sector. However, to improve the depth of the report, the survey was expanded in the July 2000 issue to include 35 firms from the construction sector. This step converted the former Industrial Barometer into today's Business Barometer. The survey was further expanded in the July 2002 issue to include 10 firms from the tourism sector. In July 2006, the survey was expanded again to include a total of 320 firms (from 210). In July 2007, another 154 firms were added to the sample. These firms cover the transportation, communications and financial sectors. The new sample includes a total of 474 firms. In addition, a few questions were added to the survey questionnaire regarding the geographic distribution of exports, employment categories, prices of different inputs and types of investments. Starting the January 2009 edition, the Business Barometer includes two indices designed to summarize firms' evaluation and expectations for five successive periods. For detailed information about the sample, questionnaire and calculating the BB indices, visit the ECES website (www.eces.org.eg) under Business Barometer.

This edition of the Business Barometer reports the results of a stratified sample of 474 public and private firms. The survey covers their assessment of economic growth and the results of their operations in terms of production, sales, inventories, capacity utilization, prices, wages, employment and investments over the past six months of 2009. It also summarizes their expectations for overall future economic performance as well as their own activities for the first half of 2010.

The interpretations and comments expressed in this survey are those of the ECES team, and do not necessarily reflect those of the ECES Board of Directors.

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Overview

This edition of the *Business Barometer* (BB) reflects the views of 474 large firms regarding the overall performance of the economy and own activities during the second half of 2009, and their expectations for the first half of 2010. The surveyed firms cover manufacturing, construction, tourism, transportation, communications and financial intermediation.

With respect to the past six months, firms reported improved perceptions about economic growth compared to the previous survey. Regarding own activities, a large number of firms reported higher production, domestic sales, exports, input prices and wages, and stable product prices, investment and employment. Firms' positive perceptions during the last six months could be mainly explained by signs of recovery from the global economic crisis, at both the global and national levels. According to the IMF, the world GDP growth rate for 2010 is projected to reach 3.1 percent compared to -1.1 percent for 2009 and 3 percent for 2008. Egypt's real GDP growth in the first quarter of fiscal year (FY) 2009/10 registered 4.9 percent. Although lower than in the corresponding quarter of FY 2008/09 (5.6 percent), it is still higher than the rates achieved in the last two quarters (4.3 percent and 4.5 percent, respectively). Average inflation continued declining from a high of 22.4 percent during the period July-September 2008 to an average of 9.9 percent in the corresponding period of 2009.¹ The balance of payments returned to surplus (\$2.1 billion) in the first quarter of FY 2009/10 (July-September 2009) compared to a deficit of \$1.8 billion in the third quarter of FY 2008/09 (January-March 2009), mainly due to recent portfolio investment inflows following waves of net outflows in the last four quarters.

Nevertheless, the recovery remains ambiguous and fragile. Comparing current account data for the first quarter of FY 2009/10 with those of the corresponding quarter of FY 2008/09 reveals that non-petroleum exports decreased by 26.9 percent, petroleum exports by 40.9 percent, Suez Canal receipts by 24.0 percent,

services receipts by 18.7 percent, and imports by 16.7 percent. The current account deficit consequently increased to \$1.5 billion in the first quarter of FY 2009/10 compared to a deficit of \$1 billion in the first quarter of FY 2008/09.² Besides, the Dubai debt crisis negatively affected the stock market, as shown by several indicators. For instance, the EGX-30 fell by 16 percent in November 2009 compared to the previous month, foreigners' net purchases of stocks fell from 47 million shares in October to 1.8 million shares in November and market volatility³ increased from 1.2 to 2.4 in the same period.

Respondents' expectations for the upcoming six months are as positive as their evaluation. Relatively more firms are optimistic about economic growth as well as their own production, domestic sales, exports and investments, signaling more confidence in the recovery. Firms' positive outlook is a reflection of the general sentiment that the financial crisis has nearly ended, although experts are concerned that this outlook might be the result of firms' hasty reading of ongoing economic events.

The remainder of this edition of the *Business Barometer* presents the results of the estimated Business Barometer indices and elaborates on the main findings of the survey under four main headings: the level of economic activity (overall growth, production, sales, inventory and capacity utilization); prices and wages; investment and employment; and finally the constraints facing the surveyed firms.

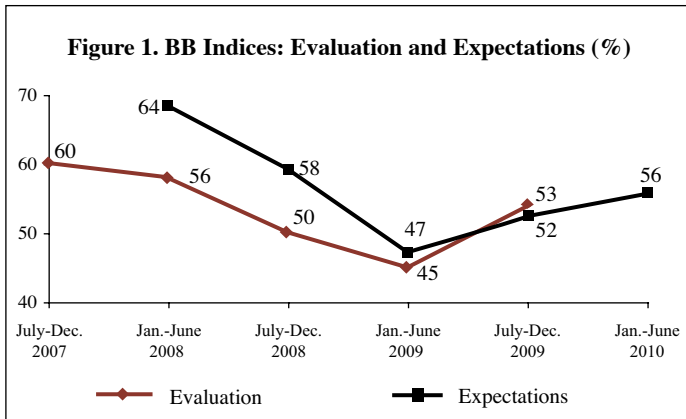
The Business Barometer Indices

Based on firms' responses, the Business Barometer Indices (BBI) were computed using the Principal Components Analysis method. Figure 1 portrays the two computed indices, one reflecting evaluation while the other presents expectations, for five consecutive periods.

²Data obtained from the Ministry of Finance.

³Measured as the standard deviation of daily percentage changes in EGX-30.

¹Data obtained from the Ministry of Finance.

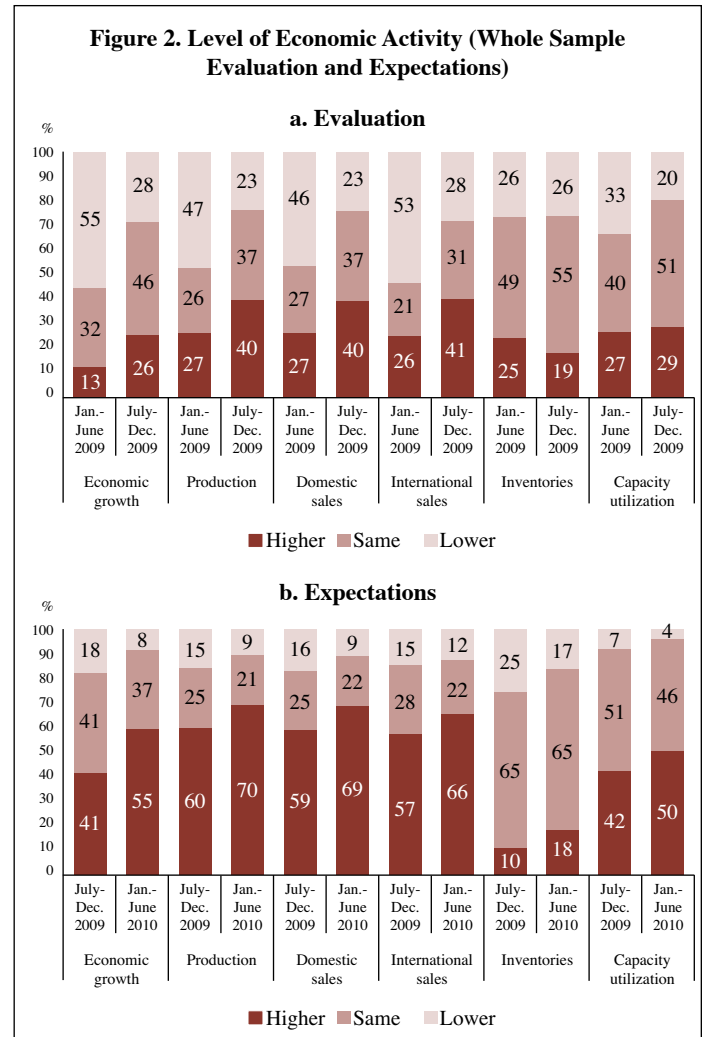


Source: Authors' calculations based on survey results.

As shown in Figure 1, the evaluation index has increased for the first time since July-December 2007, reaching close to its pre-crisis level in the first half of 2008. The evaluation index has also converged with the expectations reported by firms in the last survey for the period July-December 2009 (53 versus 52). This reflects the previously mentioned positive perceptions expressed by firms about the economy. Regarding expectations, the index also increased by 4 percentage points, reflecting continued optimism. These positive effects on the indices are mainly the result of responses on overall growth, level of production, and domestic and international sales.

The Level of Economic Activity

Figure 2a compares firms' evaluation of economic activity variables between January-June 2009 and July-December 2009. The figure shows that the percentages of firms reporting increases or steady levels of economic activity variables have increased.⁴ The largest increases have been reported in firms' perceptions about economic growth as well as in exports. Figure 2b portrays a similar pattern for expectations between July-December 2009 and January-June 2010, with an even stronger tendency to expect increases.



Source: Survey results.⁵

Higher economic growth with positive expectations

During the last six months of 2009, more firms (72 percent) reported higher / similar economic growth compared to the first six months of 2009 (45 percent). Firms' perceptions about economic growth are in line with actual real GDP growth rates. Real GDP growth rose to 4.9 percent in the period July-September 2009 compared to an average of 4.4 percent in the period January-June 2009.⁶

Firms' expectations are usually stronger than their evaluation as demonstrated by the comparison in Figures 2a and 2b. Regarding overall economic growth, expectations for the upcoming six months are higher

⁴Note that the decline in inventories is a positive sign.

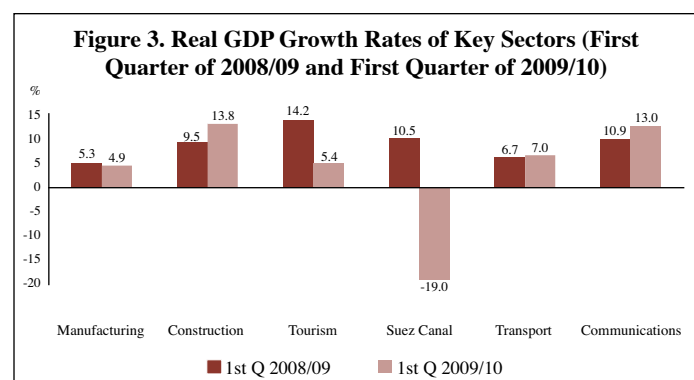
⁵Survey results are summarized in Tables 1 and 2.

⁶Data obtained from the Ministry of State for Economic Development (www.mop.gov.eg).

compared to the past six months (Figure 2b). In fact, 92 percent of the surveyed firms anticipate higher/stable economic growth during the first half of 2010 compared to 82 percent for the period July-December 2009 (Figure 2b).

At the sectoral level, construction and tourism were the most optimistic about overall economic growth in the past six months, while communications and transportation were the most pessimistic (Table 3). However, the outlook for the upcoming six months was the least optimistic in the tourism sector.

According to the Ministry of State for Economic Development (MOED) sectoral results—published only for the first quarter of FY 2009/2010—three main sectors have experienced lower growth compared to the first quarter of FY 2008/2009, namely, the Suez Canal, tourism and manufacturing (Figure 3).



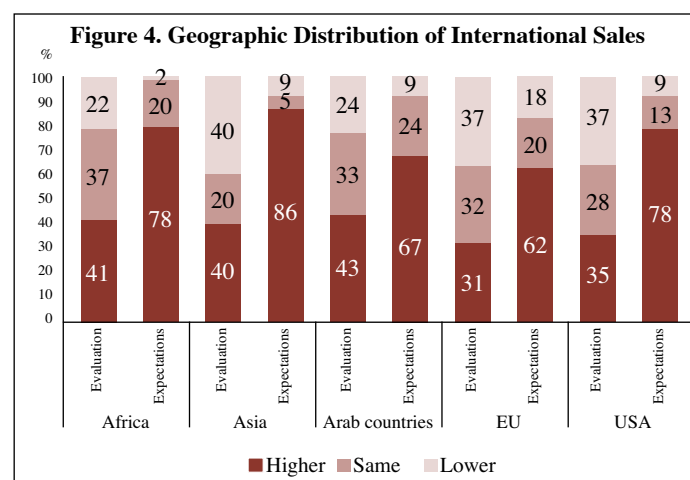
Source: The Ministry of State for Economic Development.

Increased production, domestic sales and exports, with higher expectations

Production, domestic sales and exports showed positive and similar patterns in both evaluation and expectations. On the evaluation side, the percentage of firms reporting increases rose by one and a half folds between the first half and the second half of 2009. Expectations witnessed a similar trend, as firms reporting increases in these three variables rose by 1.2 folds. As indicated in Table 3, the percentage of firms reporting increased production and domestic sales was more pronounced in the construction and tourism sectors, which is consistent with their perceptions about economic growth. Exports were most positive in construction and communications. Transportation was the only sector that recorded a

negative net balance in all three variables.⁷ Expectations for production, domestic sales and exports were the most optimistic in construction and manufacturing and the least optimistic in transportation and tourism.

In general, Figure 4 shows strongly positive export expectations for the first half of 2010 compared to the second half of 2009. Expectations are highest regarding exports to Asia and Africa, which still represent underexploited opportunities for Egyptian exports.



Source: Survey results.

Decreased inventories and higher capacity utilization with mixed expectations

The percentage of firms reporting decreased inventories remained the same (26 percent), while 19 percent of firms reported higher inventories compared to 25 percent in the previous survey (Figure 2a). This is a positive sign since inventory decreases reflect higher sales. The larger percentage of firms reporting decreased inventories was expected as some 40 percent of firms indicated an increase in both domestic and international sales. Expectations for inventories are negative as more firms expect them to increase and fewer firms expect them to decrease (Figure 2b). On the sectoral level, the inventories' net balance was negative in manufacturing (i.e., more firms reported a decrease than an increase in inventories), while the net balance was positive in construction. Other sectors do not usually provide data about inventories due to being service firms.

⁷Net balance represents the percentage of respondents indicating "higher" minus the percentage of respondents indicating "lower".

Capacity utilization results are mostly similar to those of other economic activity variables (except inventories), albeit less strong. This shows that the economy has yet to reach the point of full recovery. Sectorally, the most positive results for capacity utilization came from tourism and construction, while the most negative results came from communications, transportation and financial services. Contrary to the past six months, manufacturing and financial intermediaries have a good outlook for capacity utilization in the upcoming six months (Table 3).

reporting lower prices has decreased considerably (from 33 percent to 14 percent) with slightly more firms reporting an increase (from 11 percent to 15 percent). This is consistent with inflationary trends during the second half of 2009. In fact, year-over-year monthly inflation increased from 9 percent in August to 10.8 percent in September, then to 13.3 percent in October and 13.2 percent in November.⁸ While most firms in all sectors reported no change in output prices, 33 percent of tourism firms reported increases therein.

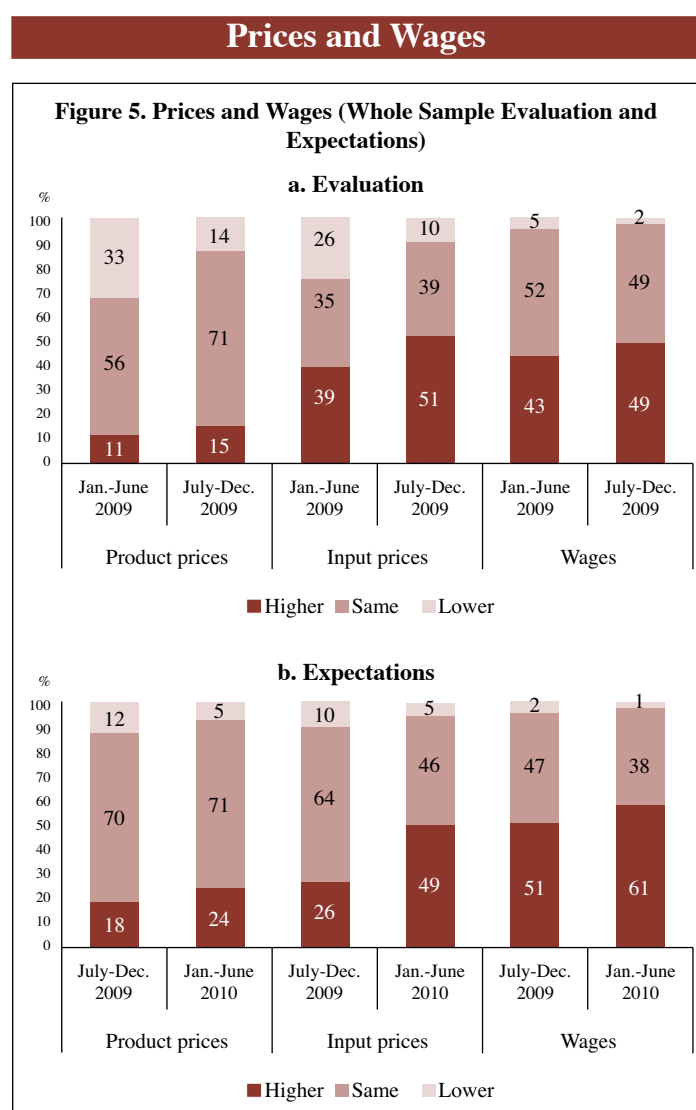
For the coming six months, the majority of firms anticipate stable output prices (70 percent), with an increase in the percentage of firms expecting higher prices (Figure 5b). At the sectoral level, the majority of firms in all sectors expect stable output prices over the next six months, with a tendency of increasing in tourism.

Increased input prices and wages, with similar expectations

More than half of the surveyed firms reported an increase in input prices during July-December 2009, with very few firms reporting a decrease therein. This represents a systematic impediment to firms' growth and Egypt's industrial development in general. Similar results apply for expectations.

Relatively fewer firms in the communications and construction sectors reported an increase in intermediate input prices (Table 3), with most firms in the other sectors, except communications, anticipating increased intermediate input prices during January-June 2010.

A large percentage of firms reported wage increases, with a larger percentage expecting wage increases in the first six months of 2010. Relatively fewer firms in transportation and communications reported paying higher wages over the second half of 2009, while most firms in all other sectors reported higher wages over the same period. As for expectations, 55 percent or more firms in all sectors plan to raise wages.



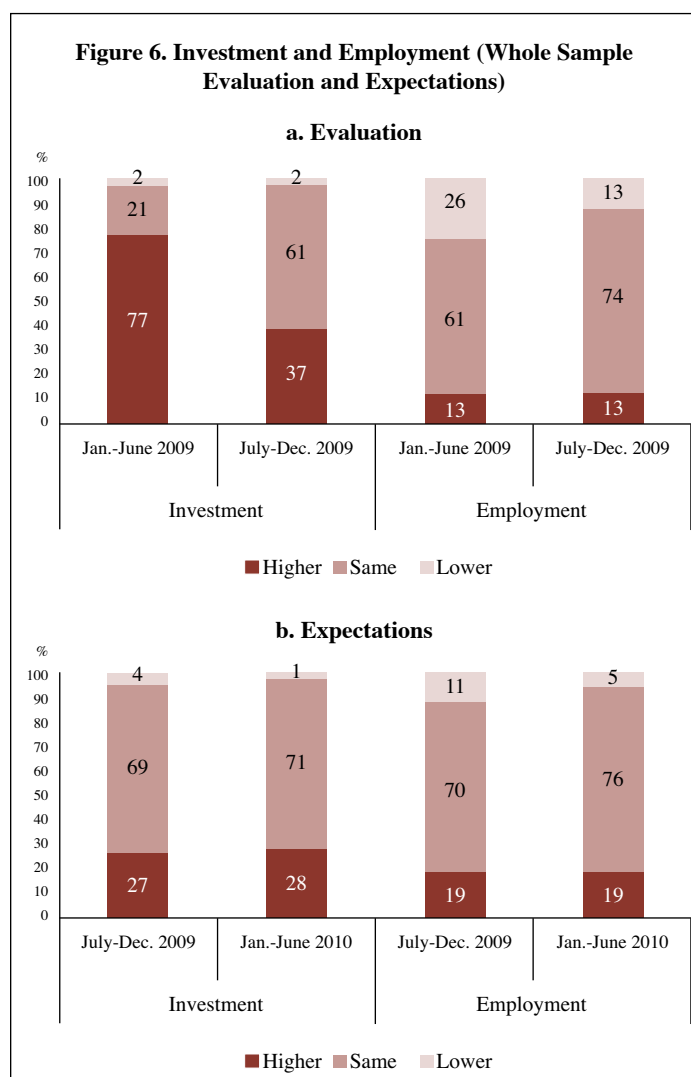
Source: Survey results.

Stable product prices and similar expectations

As shown in Figure 5a, 72 percent of firms reported stable product prices. However, the percentage of firms

⁸Data obtained from the Ministry of Finance (www.mof.gov.eg).

Investment and Employment



Source: Survey results.

Lower investment and stable employment, with moderate expectations

Contrary to the previous variables, the percentage of firms that increased investment declined considerably. As shown in Figure 6a, it decreased from 77 percent in January-June 2009 to 37 percent in the following six months. However, this decrease seems to have been planned by firms, as shown by their previous expectations (first column of Figure 6b). In July 2009, only 27 percent of firms planned an increase in their investment during July-December 2009. By types of investment, the largest percentage of firms reporting increases was in machinery and equipment.

For the first half of 2010, more than two thirds of the surveyed firms expect keeping the level of investments unchanged (Figure 6b), which is close to expectations voiced in the last survey.

The slowdown in investment reported by firms during the second half of 2009 is in line with the decreases in investments reported by the Ministry of Finance in the first quarter of FY 2009/2010. The ratio of domestic investments to GDP went down to 3.9 percent at end of September 2009, from 4.4 percent at end of June. The ratio of FDI to GDP also went down from 1.5 percent to 0.8 percent during the same period. At the sectoral level, the smallest percentage of firms reporting increases in investment came from the transportation and communications sectors. The majority of firms in all other sectors reported steady investments. Regarding expectations, 60 percent or more of firms in all sectors anticipate maintaining the same levels of investment.

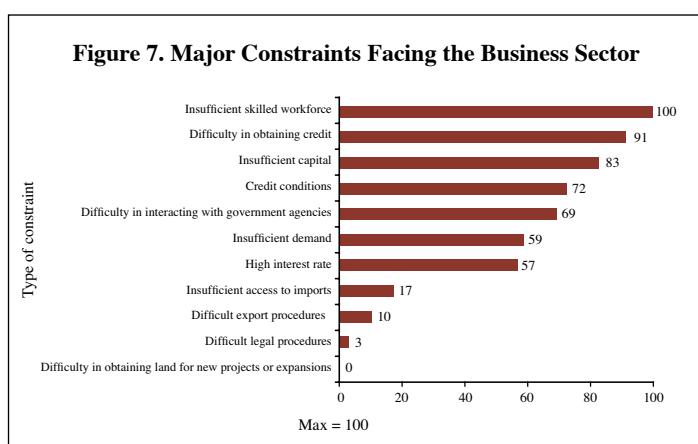
Regarding employment, firms reported stable employment during July-December 2009, as well as similar expectations for January-June 2010. Employment results at the sectoral level are homogeneous and consistent with whole sample results (Table 3). The net balances of transportation and communications firms have been negative, reflecting the negative results in their production and sales. All sectors expect stable employment during the coming six months, with relatively more firms planning to increase employment in construction (Table 3).

Labor is disaggregated into administrative and technical workforce. Each type includes permanent and temporary workforce. Results for all these types are similar to the aggregate results shown in Figure 6. However, temporary administrative manpower shows relatively less flexibility as 86 percent of the firms reported similar employment. Temporary technical manpower shows relatively more flexibility, as 73 percent of the firms reported similar employment, while 19 percent reported an increase, and 8 percent a decrease.

Business Constraints

Major constraints: insufficient skilled workforce, difficulty to obtain credit and insufficient capital

Figure 7 illustrates the constraints considered by firms as major factors affecting their performance. In the current BB edition, the main concerns include, in that order, insufficient skilled labor, difficulty to obtain credit, insufficient capital and difficult credit conditions. When probing for the key skills that are most needed in the labor market, they included skilled technical labor and production workers.



Source: Survey results.

Table 1. Survey Results: Summary of Whole Sample Evaluation (January-June 2007 to July-December 2009)¹

(%)

Indicator	January - June 2007			July - December 2007			January - June 2008			July - December 2008			January - June 2009			July-December 2009			
	Higher	Same	Lower	Higher	Same	Lower	Higher	Same	Lower	Higher	Same	Lower	Higher	Same	Lower	Higher	Same	Lower	
Economic growth	51	35	14	48	29	23	25	29	44	27	2	16	34	50	-34	13	32	55	-42
Business activity																			
Production	52	34	14	62	21	17	45	56	28	16	40	39	26	35	4	27	26	47	-19
Domestic sales	53	31	16	60	23	18	42	56	28	16	40	38	26	36	2	27	27	46	-20
International sales	51	37	12	64	18	18	46	57	26	17	40	34	26	40	-6	26	21	53	-28
Inventory	30	44	26	24	44	32	-8	23	58	19	4	29	51	20	9	25	49	26	-1
Level of capacity utilization ³	41	46	13	51	40	9	42	42	46	12	30	33	45	22	11	27	40	33	-6
Prices																			
Final product prices	40	52	8	49	44	7	42	56	41	3	53	37	47	16	21	11	56	33	-23
Intermediate input prices	80	18	2	92	6	2	90	98	2	0	98	69	16	15	54	39	35	26	13
Wage level	76	23	1	63	35	2	61	82	18	0	82	61	36	3	58	43	52	5	38
Primary inputs																			
Investment	40	57	3	51	47	2	49	60	37	3	57	60	38	2	58	77	21	2	75
Employment	27	58	15	34	52	14	20	33	55	12	21	25	58	17	8	13	61	26	-12

Table 2. Survey Results: Summary of Whole Sample Expectations (July-December 2007 to January-June 2010)¹

(%)

Indicator	July - December 2007			January - June 2008			July - December 2008			January - June 2009			July-December 2009			January-June 2010			
	Higher	Same	Lower	Higher	Same	Lower	Higher	Same	Lower	Higher	Same	Lower	Higher	Same	Lower	Higher	Same	Lower	
Economic growth	54	39	7	54	34	12	42	26	55	19	7	17	38	45	-28	41	41	18	23
Business activity																			
Production	79	15	6	75	16	9	66	68	19	13	55	41	21	38	3	60	25	15	44
Domestic sales	78	17	5	73	18	9	64	66	22	12	54	42	22	36	6	59	25	16	43
International sales	79	18	3	75	17	8	67	71	19	10	61	39	19	42	-3	57	28	15	42
Inventory	8	66	26	20	50	30	-10	14	60	26	-12	18	61	21	-3	10	65	25	-14
Level of capacity utilization ³	61	35	4	68	28	4	64	37	56	7	30	31	53	16	15	42	51	7	34
Prices																			
Final product prices	45	51	4	62	34	4	58	68	30	2	66	20	55	25	-5	18	70	12	6
Intermediate input prices	76	23	1	88	10	2	86	94	6	0	94	29	40	31	-2	26	64	10	16
Wage level	65	34	1	68	32	0	68	67	33	0	67	45	50	5	40	51	47	2	50
Primary inputs																			
Investment	61	39	0	53	45	2	51	40	57	3	37	38	57	5	33	27	69	4	24
Employment	33	57	10	31	63	6	25	22	70	8	14	19	67	14	5	19	70	11	7

¹ Numbers represent percent of total responses. Higher, same and lower may not add up to 100 due to rounding.

² <Net balance> represents the percentage of respondents indicating «higher» minus the percentage of respondents indicating «lower».

³ Higher = approaching full capacity; Same = normal capacity utilization; Lower = below capacity utilization.

Table 3. Survey Results: Summary of Business Sector's Evaluation and Expectations¹

(%)

Indicator	Manufacturing Sector						Construction Sector						Tourism Sector												
	Evaluation			Expectations			Evaluation			Expectations			Evaluation			Expectations									
	Higher	Same	Lower	Net Balance ²	Higher	Same	Lower	Net Balance ²	Higher	Same	Lower	Net Balance ²	Higher	Same	Lower	Net Balance ²	Higher	Same	Lower	Net Balance ²					
Economic growth	30	39	31	-1	58	37	5	53	41	46	13	28	59	34	7	52	35	46	19	16	42	42	16	26	
Business activity																									
Production	37	39	24	13	72	22	6	66	64	27	9	55	82	16	2	80	60	24	16	44	56	25	19	37	
Domestic sales	36	40	24	12	70	24	6	64	64	27	9	55	82	16	2	80	56	25	19	37	53	26	21	32	
International sales	40	33	27	13	70	24	6	64	89	11	0	89	89	11	0	89	47	18	35	12	35	24	41	-6	
Inventory	18	56	26	-8	17	66	17	0	35	43	22	13	23	68	9	14	0	100	0	0	0	100	0	0	0
Level of capacity utilization ³	31	47	22	9	52	44	4	48	42	46	12	30	55	45	0	55	35	61	4	31	38	58	4	34	
Prices																									
Final product prices	16	67	17	-1	28	68	4	24	14	79	7	7	29	69	2	27	33	60	7	26	33	55	12	21	
Intermediate input prices	52	36	12	40	48	47	5	43	40	47	13	27	52	44	4	48	64	33	3	61	53	41	6	47	
Wage level	51	47	2	49	58	41	1	57	66	34	0	66	68	32	0	68	65	35	0	65	60	37	2	58	
Primary inputs																									
Investment	37	61	2	35	30	69	1	29	54	44	2	52	40	60	0	40	35	60	5	30	21	79	0	21	
Employment	8	77	15	-7	20	74	6	14	30	57	13	17	29	61	11	18	14	74	12	2	9	86	5	4	
Indicator	Transportation						Communications						Financial Intermediaries												
	Evaluation			Expectations			Evaluation			Expectations			Evaluation			Expectations									
	Higher	Same	Lower	Net Balance ²	Higher	Same	Lower	Net Balance ²	Higher	Same	Lower	Net Balance ²	Higher	Same	Lower	Net Balance ²	Higher	Same	Lower	Net Balance ²	Higher	Same	Lower	Net Balance ²	
Economic growth	9	57	34	-25	54	35	11	43	10	45	45	-35	62	28	10	52	17	58	25	-8	45	47	8	37	
Business activity																									
Production	23	43	34	-11	63	16	21	42	38	38	24	14	62	31	7	55	32	39	29	3	71	15	14	57	
Domestic sales	25	42	33	-8	65	15	20	45	38	38	24	14	62	31	7	55	32	39	29	3	71	15	14	57	
International sales	7	46	47	-40	40	20	40	0	60	20	20	40	80	20	0	80	38	37	25	13	75	12	13	62	
Inventory	0	50	50	-50	50	0	50	0	0	0	0	0	100	0	0	100	0	0	0	0	0	0	0	0	0
Level of capacity utilization ³	17	59	24	-7	41	49	10	31	0	33	67	-67	0	100	0	0	8	77	15	-7	50	46	4	46	
Prices																									
Final product prices	11	75	14	-3	20	76	4	16	7	76	17	-10	3	80	17	-14	6	83	11	-5	17	81	2	15	
Intermediate input prices	52	43	5	47	43	57	0	43	14	86	0	14	14	72	14	0	80	20	0	80	80	20	0	80	
Wage level	23	75	2	21	66	30	4	62	17	80	3	14	66	34	0	66	51	44	5	46	57	41	2	55	
Primary inputs																									
Investment	23	77	0	23	21	79	0	21	13	74	13	0	13	81	6	7	42	58	0	42	21	79	0	21	
Employment	4	82	14	-10	16	82	2	14	10	66	24	-14	21	76	3	18	22	75	3	19	18	79	3	15	

¹ Numbers represent percent of total responses. Higher, same and lower may not add up to 100 due to rounding.

² «Net balance» represents the percentage of respondents indicating «higher» minus the percentage of respondents indicating «lower».

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