

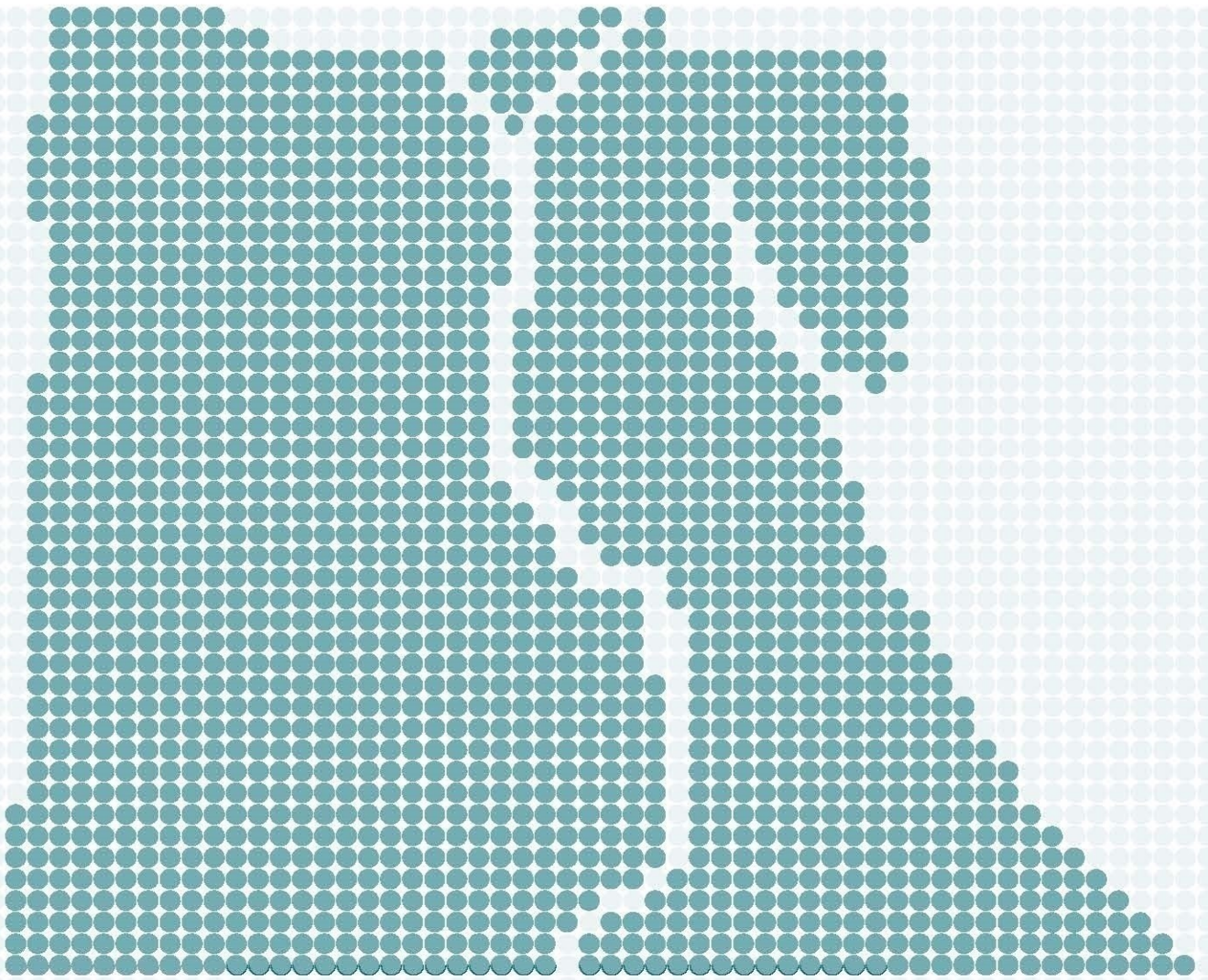


المركز المصري للدراسات الاقتصادية  
*The Egyptian Center for Economic Studies*

# Business Barometer

## Issue 49

## 2018



## Performance & Expectations of the Egyptian Business Sector

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The Egyptian Center for Economic Studies (ECES) is an independent, non-profit think tank that conducts specialized economic research, drawing on international experience and constructive discussions among various stakeholders. ECES's main objective is to propose sound economic policies, and institutional and legislative reforms that contribute to sustainable development in Egypt, all on the basis of combined economic efficiency and social justice.

### **Strategic Direction**

Economic efficiency and social justice are of core interest to ECES. Combined, they constitute the Center's strategic direction. ECES research and activities focus on studying past, present and future challenges facing the Egyptian economy, whether they are related to macroeconomic stability, microeconomic efficiency, or political economy aspects both on the internal and external dimensions. In its analysis, ECES is keen on adopting a comprehensive approach that encompasses legislative, institutional, policy and structural aspects of whatever problem or area addressed, not to mention implementation mechanisms. In all its activities, ECES relies on its competent team of in-house researchers, in addition to collaboration with external experts and like-minded think tanks as needed.

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# *Business Barometer*

Issue No. 49 – 2018

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## **About the Business Barometer**

The Egyptian Center for Economic Studies (ECES) publishes its Business Barometer (BB) survey periodically as part of its role in providing timely information about the developments of economic activity in Egypt based on an assessment of macroeconomic indicators produced by the relevant authorities. The survey covers an assessment by a sample of firms of economic growth and results of own operations in terms of production, domestic sales, exports, commodity inventories, capacity utilization, prices, wages, employment and investment during the quarter under review as well as their outlook for the same set of variables in the upcoming quarter.

ECES launched its first Business Barometer in 1998. The report analyzes the results of a sample survey of 121 private firms that cover manufacturing (50 percent), financial services (13 percent), construction (12 percent), transportation (10 percent), tourism (9 percent) and telecommunications (7 percent). The survey is conducted on a number of micro, small, medium and large firms as per the definition of the Central Bank of Egypt announced on March 5, 2017 (CBE).

This edition of BB provides an assessment of the performance of a sample of firms and results of their operations in the first quarter of FY 2018/2019 (July-September 2018). It also summarizes their expectations for overall economic performance as well as own activities for the second quarter of FY 2018/2019 (October-December 2018).

## Methodology

The BB Index is a simple average of the sub-indices of surveyed variables (production, domestic sales, exports, inventory, capacity utilization, prices, wages, employment and investments). The Index is calculated once for large firms and once for SMEs, both for evaluation and expectations.

Index Value	Index Definition
50 points	Same (no change in firms' performance and expectations)
Above 50 points	Higher (improvement in firms' performance and expectations)
Below 50 points	Lower (decline in firms' performance and expectations)

The index is calculated for each variable using the following equation:

$$X = \frac{I+S}{100+S} \times 100$$

where  $I$  is the share of firms reporting an increase and  $S$  the share of firms reporting "same."

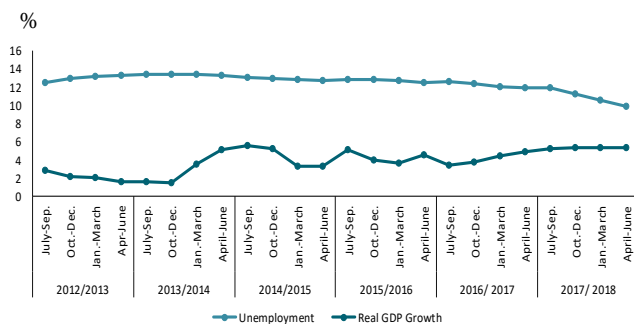
The index is designed to have a maximum of 100 points when all firms report an increase, a minimum of 0 when all firms report a decrease and a middle value of 50 when all firms report no change. Between 0 and 100, the index grows proportionally with larger shares of "increase," and inversely with larger shares of "decrease," while the change in "same" is neutralized by including it in the numerator and the denominator. A higher index thus reflects a better business climate and vice versa. It is worth noting that the index is inverted for inventories and input prices as increases of these two variables reflect an adverse business climate for firms.

## Overview

This section provides an overview of the main developments of the first quarter of FY 2018/2019 (July–September), as well as an assessment of the performance of the main macro indicators (as per the latest available data). It is worth noting that the quarter under review follows the latest round of petroleum subsidy reductions, re-pricing subway fare and raising electricity prices. The implications of economic developments in emerging markets for the Egyptian economy have also become apparent, which will be discussed later in more detail.

Despite these implications, Moody's raised the outlook for Egypt from stable to positive and confirmed the long-term rating at B3 in August. Moody's cited the improved economic and business climate in Egypt as a result of the ongoing economic reform program, which cannot be considered in isolation from the third IMF review in the context of the EFF, whose results were announced by the Executive Board of the International Monetary Fund (IMF) in early July. The review enabled the Egyptian authorities to withdraw the equivalent of SDR 1,432.76 million (about \$2.02 billion), bringing Egypt's total credit to SDR 5731.05 million (about \$8.06 billion).

**Figure 1.1: Real GDP Growth and Unemployment**

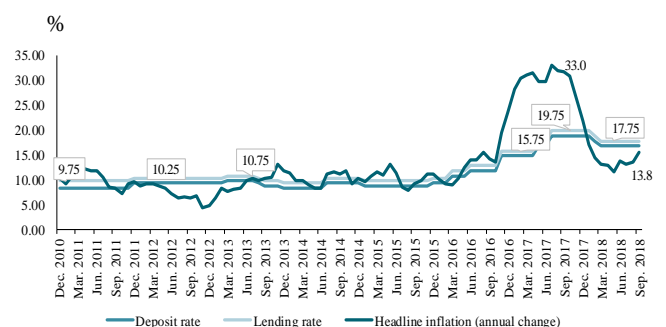


Sources: Ministry of Planning, Monitoring and Administrative Reform, Central Agency for Public Mobilization and Statistics (CAPMAS).

According to the IMF's third review, Egypt's economic situation continued to improve in 2018, with favorable prospects for near-term growth supported by tourism recovery and higher natural gas production. Recent official data showed that the annual growth in GDP for FY 2017/2018 was 5.3 percent, accompanied by a decline in the unemployment rate to 9.9 percent during the last quarter of the same fiscal year (Figure 1.1). The largest contribution to GDP growth came from manufacturing (including oil refining), extractive industries and tourism; the three accounted for 33 percent of growth. On the inflation side, it rose to 15.4 percent in September from 11.5 percent in May, which was expected on the back of reduction of fuel/electricity subsidies (Figure 1.2).

The monetary policy committee of the Central Bank of Egypt, at its most recent meeting in September, decided to keep the policy interest rate unchanged (Figure 1.2) in response to the temporary impact of financial supply shocks. The committee's press release stated that the impact of developments in emerging economies on domestic inflation remained under control thanks to macro-

**Figure 1.2: Inflation and the Policy Rate of Monetary Policy**



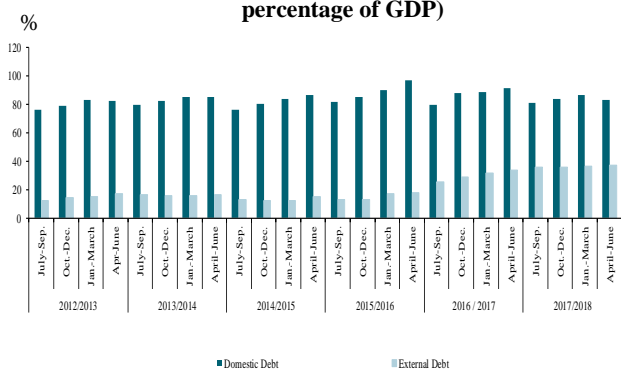
Sources: Central Bank of Egypt; Central Agency for Public Mobilization and Statistics (CAPMAS).



On the fiscal front, the Central Bank of Egypt (on behalf of the Ministry of Finance) canceled four consecutive auctions of Treasury bonds due to investors' request for higher interest rates. Demands for higher interest rates cannot be ignored in light of the economic developments in emerging markets. The cancellation of auctions prompted the Ministry of Finance to review the fiscal plan for the current fiscal year by resorting to short-term debt instruments. The Ministry of Finance was also forced to review the paths of the fiscal deficit and public debt for the next three years, which were announced in the financial statement for FY 2018/2019. These paths are based on the assumption that the domestic interest rate will be reduced to 14 percent, which is unexpected in the near term. The ratio of domestic debt to GDP reached 83 percent at end of June 2018, of which 42 percent was outstanding balance in Treasury bonds. As for external debt, it reached 37 percent of GDP at end of June 2018 compared to 34 percent in the corresponding month of the previous year (Figure 1.3).

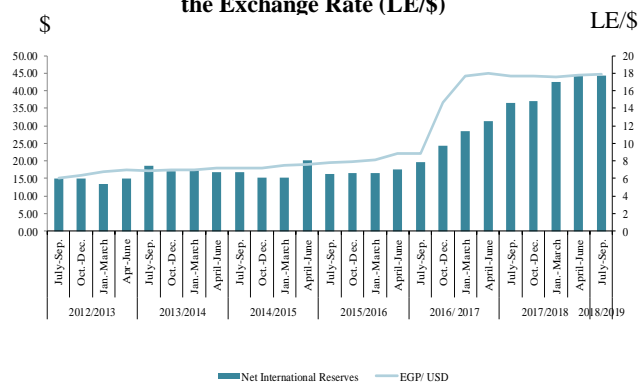
On the external side, the external balance as a whole fell from 5.8 percent of GDP in 2016/2017 to 5.1 percent of GDP in FY 2017/2018, which indicates an improvement in the current account deficit during FY 2017/2018; it dropped by \$8.4 billion to \$6.0 billion—only 2.4 percent of GDP (compared to \$ 4.4 billion in the previous fiscal year and 6.1 percent of GDP). This was mainly driven by the services balance, which posted a surplus of \$ 11.1 billion (compared to \$5.6 billion) due to a \$7.4 billion travel surplus (compared to \$1.6 billion) and a 15.4 percent rise in revenues from the Suez Canal to \$5.7 billion (compared to \$4.9 billion dollars). However, the trade deficit remained unchanged at \$37.3 billion, due to an increase in merchandise export revenues and imports. In addition, portfolio investments declined, with a net flow of \$12.1 billion (compared to \$16 billion) mainly due to a decrease in foreign investments in Egyptian Treasury bills, with net purchases of \$6.5 billion (compared to \$10.0 billion). Net international reserves stood at \$44.5 billion at end of September in light of the relatively stable exchange rate (Figure 1.4).

**Figure 1.3: Domestic and External Debt (as a percentage of GDP)**



Source: Central Bank of Egypt (CBE), *Monthly Statistical Bulletin*, various issues.

**Figure 1.4: Net International Reserves and the Exchange Rate (LE/\$)**



Source: Central Bank of Egypt (CBE).

## Business Barometer Index (BBI)

### Steady business performance and expected improvement in the coming quarter

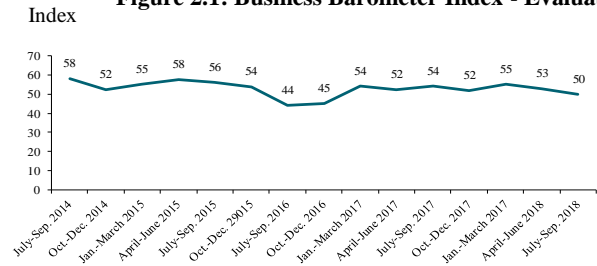
As per the survey results, the overall performance of businesses was steady during the relevant quarter (July-September 2018), with the index reaching 50 points. However, this performance is three points lower than in the previous quarter, which could be attributed to Government decisions that directly impact the business community, especially in connection with increased fuel prices, water and electricity tariffs, and taxes (Figure 2.1). The survey results also reflected Firms' positive outlook for the upcoming quarter (October-December 2018), albeit less optimistic compared to the previous quarter (Figure 2.2).

Survey results also reflect improved performance of **large firms** during July-September 2018, albeit lower compared to the previous quarter of April-June 2018. The outlook index also continued its upward trend in October-December 2018, although one percentage point lower than in the previous quarter (Figure 2.3).

Regarding performance evaluation of **SMEs**, the survey results showed a continued performance decline in the quarter under review to 48 points compared to 49 points in the previous quarter. This could be ascribed to several factors, such as higher tax rates, tighter credit, weak financing schemes for SMEs, and higher interest rate on loans, emphasizing the need to provide more support to SMEs to enable them to continue in the face of the burdens they bear due to economic reforms. The results also showed positive expectations for the

coming quarter, albeit lower compared to the previous one (Figure 2.4).

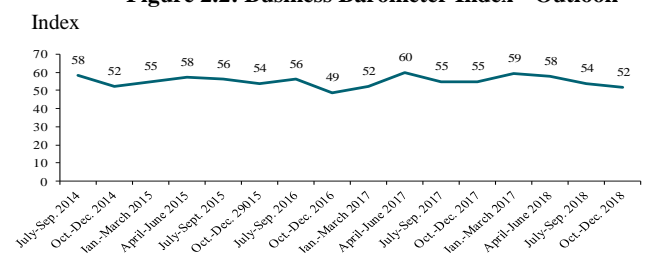
Figure 2.1: Business Barometer Index - Evaluation



Source: Survey results.

\* Data for the two quarters of January-March and April-June 2016 are unavailable.

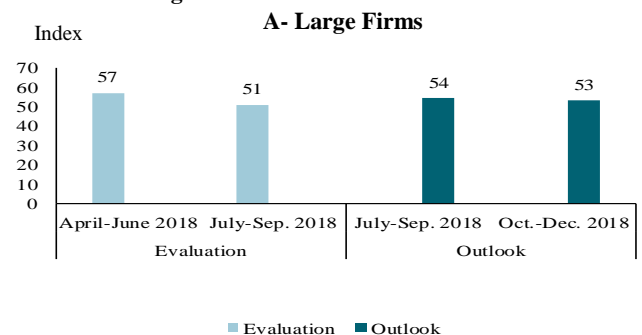
Figure 2.2: Business Barometer Index - Outlook



Source: Survey results.

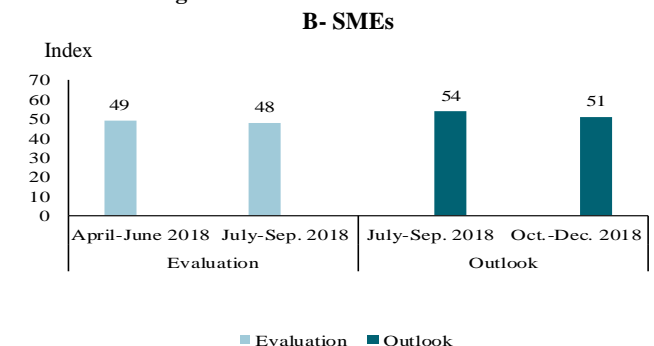
\* Data for the two quarters of April-June, and July-September 2016 are unavailable.

Figure 2.3: Business Barometer Index



Source: Survey results.

Figure 2.4: Business Barometer Index



Source: Survey results.

## Past Performance of Businesses

### Most economic activity indicators improved for large firms but declined for SMEs

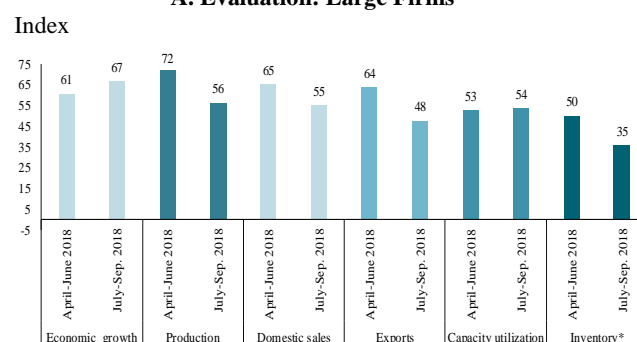
At the economic activity level, **large firms** reported positive views regarding domestic sales during the quarter under review, albeit lower than in the previous quarter, sustaining the improvement in the production index albeit lower than in the previous quarter. Exports declined compared to the previous quarter, leading to increased inventory in the quarter under review (Figure 3.1).

**SMEs** performance evaluation results were weak in aggregate, with all below 50; they are also lower compared to large firms. SMEs reported lower domestic sales and exports in July-September 2018, driving production and capacity utilization indexes below 50, leading to higher final product inventory for SMEs, as a result of both higher inflation and lower demand in the quarter under review. This is evidence that SMEs are more impacted compared to large firms by reforms (Figure 3.2).

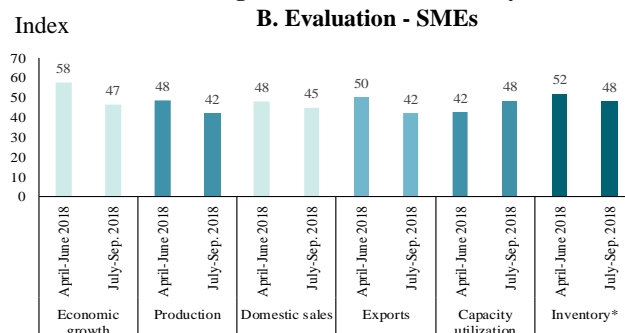
At the sectoral level, according to the views of the business community, the construction sector improved during the quarter under review (Table A1), which can be attributed to innovative solutions to increase sales in the domestic market, such as longer installment plans. Results also showed some improvement in the tourism sector, thanks to State-organized campaigns in several European and Asian countries to promote tourism. The transportation sector witnessed a marginal improvement in performance in the domestic market despite notable increase in energy and spare

part prices. The communications sector also witnessed steady performance, while manufacturing and financial intermediation declined due to performance challenges. Most production sectors, however, suffered from unavailability of production inputs locally, high prices of imported products and difficult customs procedures in general. On the other hand, the financial services sector is suffering from the increase in stamp duty on trading on the Egyptian stock exchange from 1.25 per thousand to 1.5 per thousand as of June 2018. Another increase therein to 1.75 per thousand is expected next year. Besides, more foreign investments exited the market during the quarter under review.

**Figure 3.1: Economic Activity  
 A. Evaluation: Large Firms**



**Figure 3.2: Economic Activity  
 B. Evaluation - SMEs**



Source: Survey results.

\* The index for inventory is inverted to indicate the negative impact of its increase on businesses. Hence, a higher inventory index indicates lower inventory and vice versa.

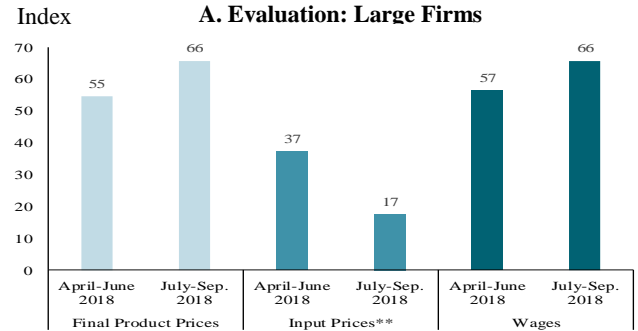
## Increased input and final product prices and higher wages

The past performance assessment of large firms and SMEs showed a continued rise in the prices of inputs during the quarter under review. The inputs index dropped below 50 points for all firms, indicating higher input prices (see Methodology). Moreover, wages continued to increase during the period under review. The higher input and wage indexes led to a continued increase in the final product prices index (Figures 3.3 and 3.4).

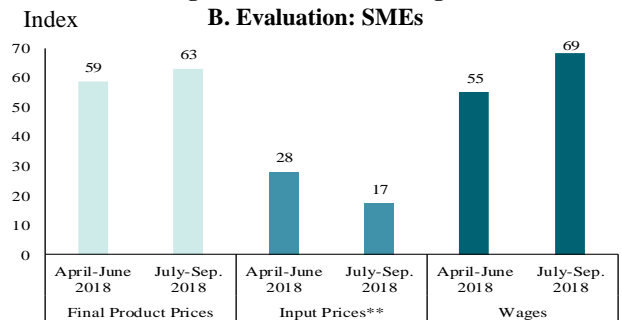
## Improved investment and employment

Survey results indicate an improvement in the investment index during the quarter under review for large businesses and SMEs. This can be attributed to business confidence in the reform efforts and measures taken by the Government to improve the investment climate such as amending the bankruptcy and capital market laws, and introducing a new law dedicated to SMEs. The index value for all firms remained unchanged. The results also show a minimal rise in the employment index for both large businesses and SMEs, indicating firms' ability to generate jobs in the quarter under review compared to the previous quarter (Figures 3.5 and 3.6).

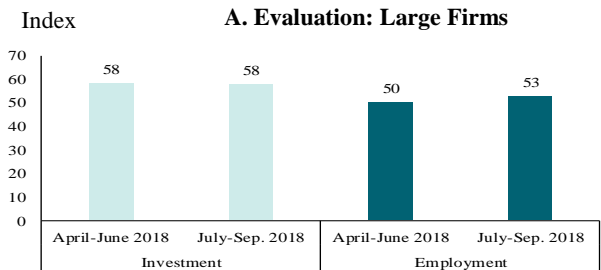
**Figure 3.3: Prices and Wages  
A. Evaluation: Large Firms**



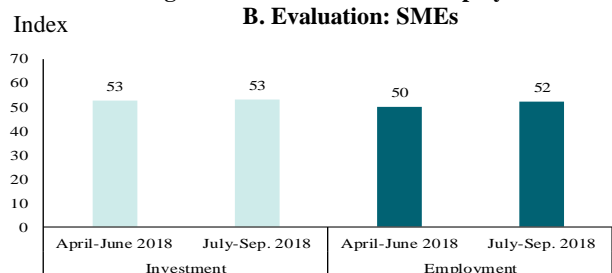
**Figure 3.4: Prices and Wages  
B. Evaluation: SMEs**



**Figure 3.5: Investment and Employment  
A. Evaluation: Large Firms**



**Figure 3.6: Investment and Employment  
B. Evaluation: SMEs**



Source: Survey results.

\*\* The input prices index is inverted to reflect the negative impact of rising input prices on the BBI. In other words, a lower index indicates higher input prices.

## Business Strategy Going Forward

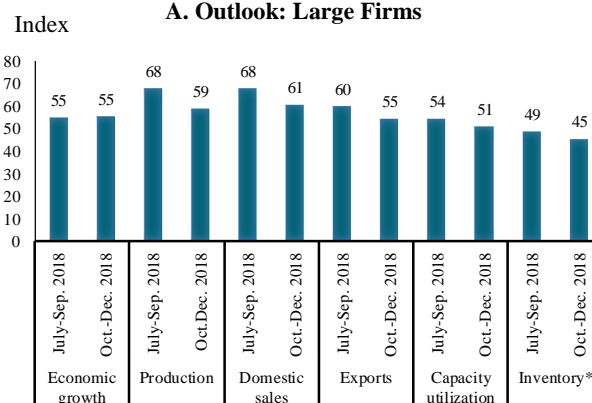
### Expectations of improved economic activity for firms

Firms' expectations remain optimistic about production, domestic sales and exports for October-December 2018, though less optimistic than in the previous quarter. Firms' expectations regarding economic growth diverged. While large companies expect growth to stabilize, SMEs expect it to decline compared to the previous quarter. Meanwhile, all firms noted a decline in capacity utilization compared to the previous quarter (Figure 4.1).

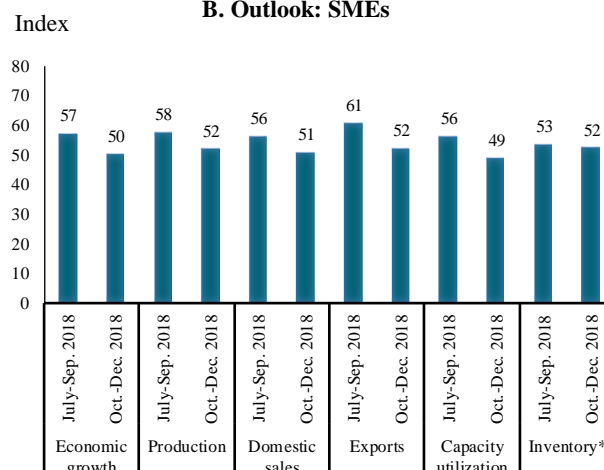
The business community expects all economic indicators to increase, albeit at a slower pace than the previous quarter, except for a minimal decline in capacity utilization (Figure 4.2).

At the sectoral level, the outlook for the coming quarter is positive for the financial intermediation and communications sectors, followed by the manufacturing sector (Table 2 in the Appendix). This can be attributed to the continuation of the government placement program. The results showed that the positive views regarding the telecom sector are linked to the completion of the new telecom law. The results also showed positive expectations for the tourism sector; with less positive expectations for the construction and transportation sectors during the quarter under review.

**Figure 4.1: Economic Activity  
 A. Outlook: Large Firms**



**Figure 4.2: Economic Activity  
 B. Outlook: SMEs**



Source: Survey results.

\* The inventory index is inverted to reflect the negative impact of rising inventory on businesses. In other words, a higher index indicates lower inventory and vice versa.

## Expectations of a rise in the prices of final products, inputs and wages

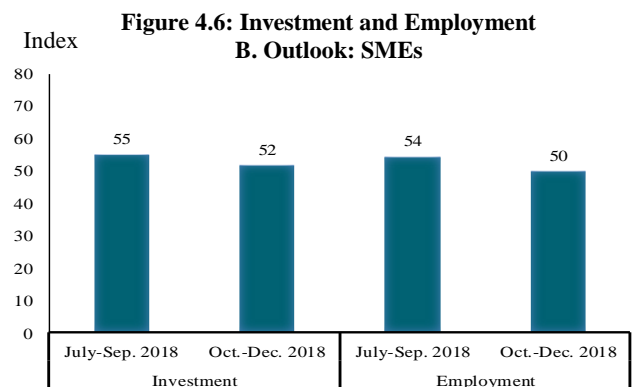
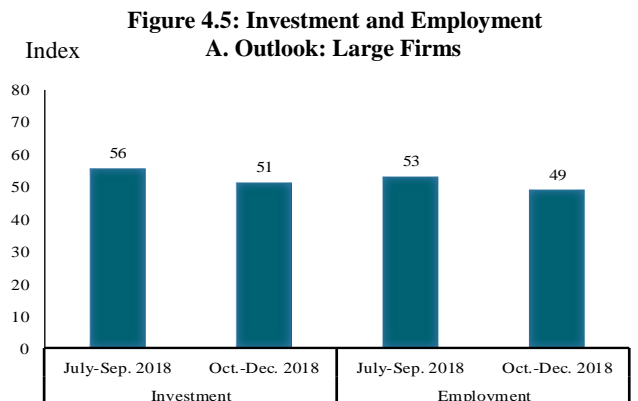
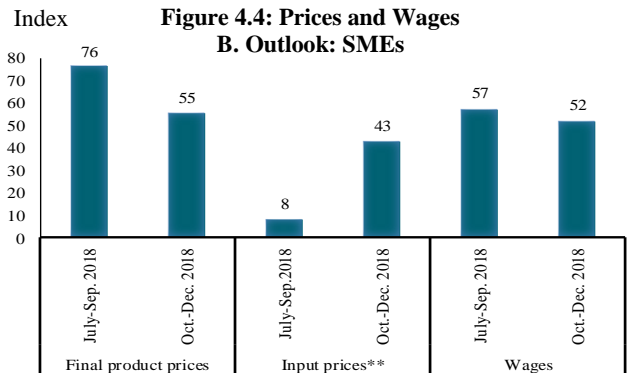
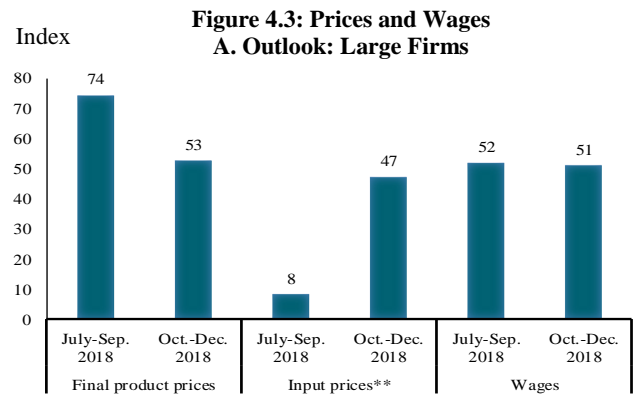
The expectations of large firms and SMEs were similar for October-December 2018, with both expecting a continued increase in input and final product prices as well as a rise in wages. These expectations, however, are lower than in the previous (Figures 4.3 and 4.4).

It should be noted that despite the continued rise in input prices, a marked improvement is anticipated in October-December compared to the previous quarter.

## Investment and employment expectations

Most large businesses and SMEs expect slightly higher investment during October-December 2018, albeit at lower rates than in the current quarter.

Large firms expect the employment index to fall, while SMEs expect it to remain steady compared to the previous quarter (Figures 4.5 and 4.6).



Source: Survey results.

\*\* The index for input prices is inverted to indicate the negative effect of the increase in input prices on businesses. Hence, a lower value of this index indicates higher input prices.

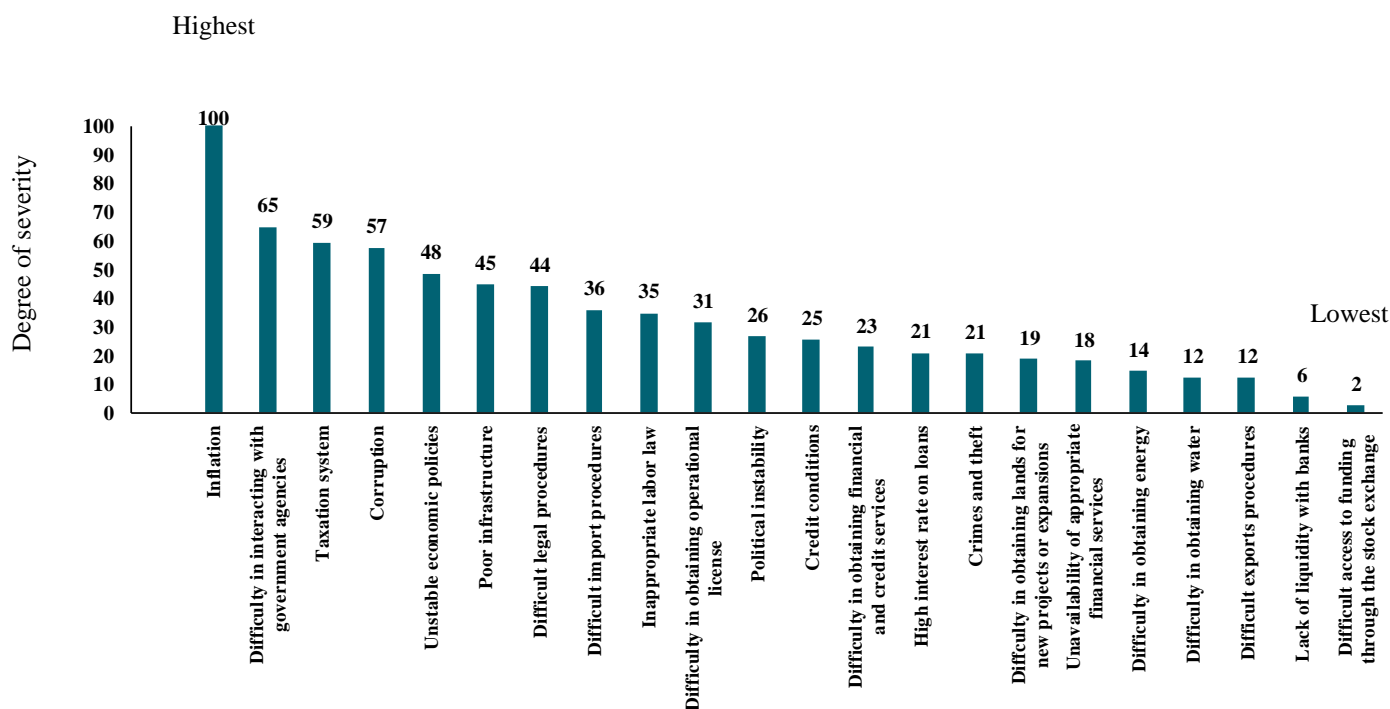
## Business Constraints

### Major constraints facing the business sector:

#### Major constraints: inflationary pressures, difficulty in interacting with government authorities, tax regime, and corruption

Figure 5 shows the major constraints that faced businesses during the surveyed period, arranged in a descending order of severity. In particular, firms expressed concern about rising inflation, difficulty in interacting with government authorities, the tax regime, and continued corruption due to higher inflation and introducing a tax on capital gains. It is worth noting that the order of constraints remains relatively similar to that of the previous survey, indicating minimal progress in removing these constraints. Also, obtaining funding from the stock market was ranked as the least constraint.

**Figure 5: Major Constraints Facing the Business Sector  
 (Normalized Index of Severity)**

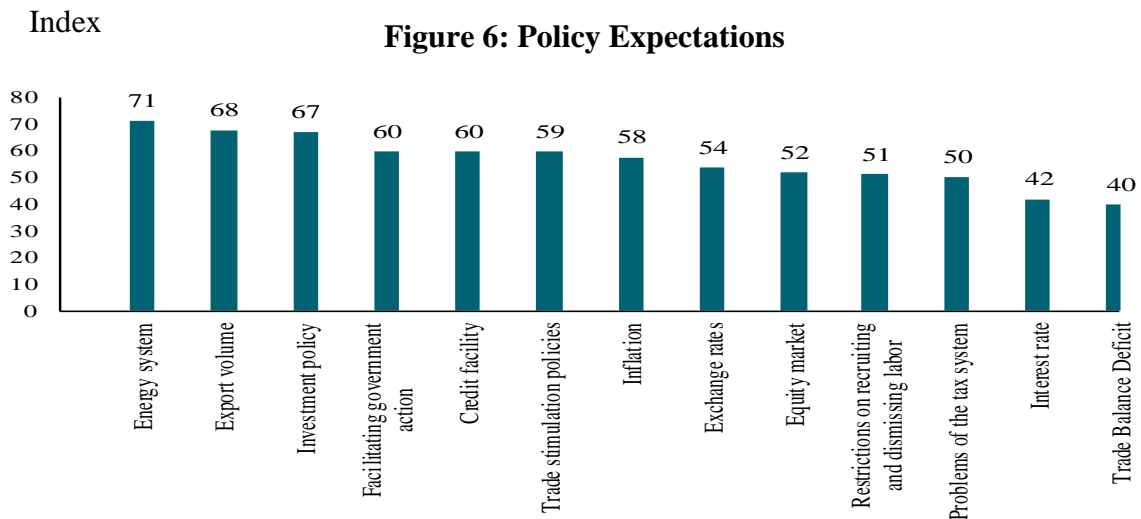


Source: Survey results.

## Policy Expectations

### Expected improvement in energy, exports, investment and government procedures

According to Figure 6, most firms expect improvements in: the energy system due to Government efforts in establishing new and renewable energy projects as well as availing an opportunity for investors to invest therein, the volume of exports, and investment policies thanks to availing a more conducive business environment for increasing FDI. Some constraining Government procedures are expected to be streamlined.



Source: Survey results.



**Table A1. Survey Results: Summary of Business Sector Past Performance of all Firms (July-August-September 2018)<sup>1</sup>**

Indicator	Manufacturing				Construction				Tourism				Transportation			Communications			Financial Intermediation					
	Percentage			Index <sup>2</sup>	Percentage			Index <sup>2</sup>	Percentage			Index <sup>2</sup>	Percentage			Index <sup>2</sup>	Percentage			Index <sup>2</sup>				
	Higher	Same	Lower	48	Higher	Same	Lower	55	Higher	Same	Lower	51	Higher	Same	Lower	51	Higher	Same	Lower	50	Higher	Same	Lower	44
<b>Economic growth</b>	30	41	30	50	0	71	29	42	40	50	10	60	42	42	17	59	25	38	38	45	13	50	38	42
<b>Business activity</b>																								
Production	21	28	51	38	57	29	14	67	60	30	10	69	58	17	25	64	25	38	37	45	6	19	75	21
Domestic sales	28	22	50	41	57	21	21	65	60	30	10	69	67	17	17	71	25	38	37	45	6	19	75	21
Exports	17	48	35	44	50	50	0	67	-	-	-	-	0	33	67	25	0	100	0	50	-	-	-	-
Inventory	24	57	20	49	64	21	14	29	30	50	20	47	67	17	17	29	0	71	29	58	25	50	25	50
Level of capacity utilization	8	74	18	47	36	64	0	61	0	80	20	44	25	50	25	50	0	100	0	50	6	88	6	50
<b>Prices</b>																								
Final product prices	48	49	3	65	64	36	0	74	40	60	0	63	83	17	0	86	13	75	13	50	13	69	19	48
Intermediate input prices	78	18	3	18	77	23	0	19	100	0	0	0	90	10	0	9	60	40	0	29	-	-	-	-
Wage level	66	34	0	74	64	36	0	74	30	70	0	59	25	75	0	57	50	50	0	67	31	69	0	59
<b>Primary inputs</b>																								
Investment	20	75	5	54	29	64	7	57	0	100	0	50	33	67	0	60	0	100	0	50	6	94	0	52
Employment	20	67	13	52	43	29	29	56	10	70	20	47	42	33	25	56	25	75	0	57	0	100	0	50

**Table A2. Survey Results: Summary of Outlook of all firms (by Sector) October-November-December 2018)<sup>1</sup>**

Indicator	Manufacturing				Construction				Tourism				Transportation			Communications			Financial Intermediation					
	Percentage			Index <sup>2</sup>	Percentage			Index <sup>2</sup>	Percentage			Index <sup>2</sup>	Percentage			Index <sup>2</sup>	Percentage			Index <sup>2</sup>				
	Higher	Same	Lower	52	Higher	Same	Lower	48	Higher	Same	Lower	50	Higher	Same	Lower	49	Higher	Same	Lower	53	Higher	Same	Lower	56
<b>Economic growth</b>	26	62	11	55	0	64	36	39	20	60	20	50	0	75	25	43	25	63	13	54	27	60	13	54
<b>Business activity</b>																								
Production	34	44	21	55	29	21	50	41	50	20	40	55	25	42	33	47	25	50	25	50	73	20	7	78
Domestic sales	33	42	25	53	29	21	50	41	60	0	40	60	25	42	33	47	25	50	25	50	73	20	7	78
Exports	30	48	22	53	33	67	0	60	-	-	-	-	0	67	33	40	50	50	0	67	-	-	-	-
Inventory	10	61	29	56	14	57	29	55	30	40	30	50	25	42	33	53	17	83	0	45	50	50	0	33
Level of capacity utilization	5	92	3	50	0	79	21	44	0	70	30	41	25	50	25	50	17	83	0	55	6	94	0	52
<b>Prices</b>																								
Final product prices	23	72	5	55	43	57	0	64	10	80	10	50	8	92	0	52	25	63	13	54	6	94	0	52
Intermediate input prices	28	70	2	42	23	77	0	43	0	100	0	50	0	100	0	50	25	75	0	43	-	-	-	-
Wage level	8	92	0	52	0	100	0	50	0	100	0	50	0	100	0	50	29	71	0	58	6	94	0	52
<b>Primary inputs</b>																								
Investment	8	90	2	52	0	100	0	50	0	100	0	50	17	83	0	55	0	100	0	50	6	94	0	52
Employment	3	93	3	50	0	79	21	44	0	90	10	47	8	83	8	50	14	86	0	54	6	94	0	52

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

<sup>2</sup>Equal to the simple average of the variables' indexes. The index's method of calculation is provided in the Methodology.

Table A3. Survey Results: Summary of Past Performance of all Firms (by size) (July-August-September 2018)<sup>1</sup>

Indicator	SMEs				Large firms			
	Percentage			Index <sup>2</sup>	Percentage			Index <sup>2</sup>
	Higher	Same	Lower		Higher	Same	Lower	
				48				51
<b>Economic growth</b>	21	47	32	47	39	48	13	59
<b>Business activity</b>								
Production	29	23	48	42	39	39	22	56
Domestic sales	34	19	47	45	36	41	23	55
Exports	18	41	41	42	15	62	23	48
Inventory	28	49	23	48	50	41	9	35
Level of capacity utilization	10	73	16	48	17	78	4	54
<b>Prices</b>								
Final product prices	45	49	6	63	48	52	0	66
Intermediate input prices	79	19	1	17	80	15	5	17
Wage level	54	46	0	69	48	52	0	66
<b>Primary inputs</b>								
Investment	15	81	4	53	26	74	0	58
Employment	22	62	15	52	17	74	9	53

Table A4. Survey Results: Summary of Outlook of all Firms (by size) (October-November-December 2018)<sup>1</sup>

Indicator	SMEs				Large firms			
	Percentage			Index <sup>2</sup>	Percentage			Index <sup>2</sup>
	Higher	Same	Lower		Higher	Same	Lower	
				51				53
<b>Economic growth</b>	19	63	19	50	26	65	9	55
<b>Business activity</b>								
Production	37	33	30	53	43	48	9	62
Domestic sales	38	31	31	52	43	43	13	61
Exports	29	47	24	52	29	57	14	55
Inventory	18	58	25	52	32	50	18	45
Level of capacity utilization	7	81	11	49	4	96	0	51
<b>Prices</b>								
Final product prices	21	76	3	55	17	74	9	53
Intermediate input prices	25	75	0	43	15	80	5	47
Wage level	7	93	0	52	4	96	0	51
<b>Primary inputs</b>								
Investment	7	92	1	52	4	96	0	51
Employment	5	89	6	50	0	96	4	49

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

<sup>2</sup>Equal to the simple average of the variables' indexes. The index's method of calculation is provided in the Methodology.