

Economic Review

Real GDP Growth

5.9%

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Headline Inflation

5.0%

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Trade Balance (Pula)

-6.5bil

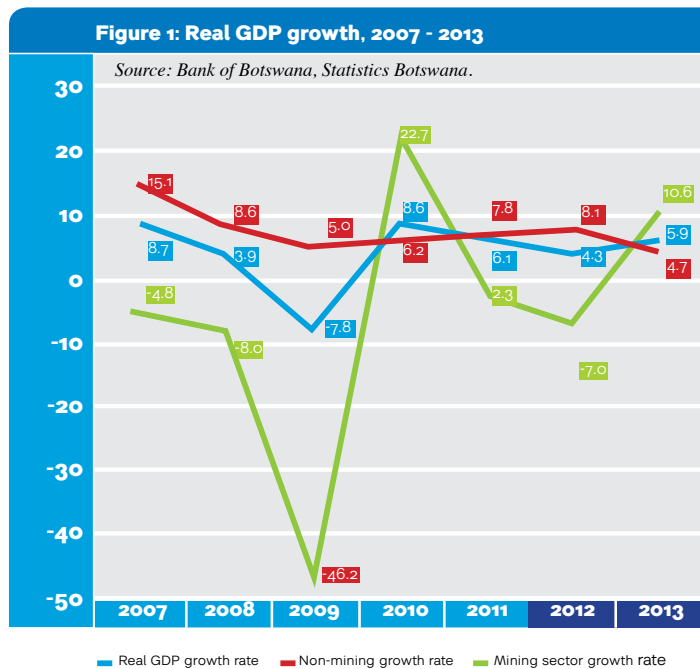
International trade data released in February 2014 show an improved trade balance from -16.4 billion in 2012 to 6.5 billion in 2013

Introduction

This review provides the opportunity to assess the outcomes of the key economic variables of the economy in 2013 and evaluate prospects for the current year. A 10.6 percent growth rate in the mining sector has been the major catalyst of real economic growth to 5.9 percent from the 4.3 percent recorded in 2012. However, the non-mining sector has experienced sluggish growth. The sector grew by 4.7 percent in 2013, down from the 8.1 percent recorded in 2012. A notable contributor to this decline is the water and electricity sector, which declined by 30.9 percent in 2013. In addition, there was a 0.5 increase in inflation from 4.1 percent in January 2014 to 4.6 percent in February 2014, before a marginal decrease to 4.4 percent in March 2014. Inflationary pressures were due in part to an increase in the alcohol levy and the introduction of the tobacco levy in December 2013 and February 2014 respectively. Lastly, there is a positive economic outlook for the advanced economies. This is expected to help steer the 2013 mining (diamond) sector recovery into 2014.

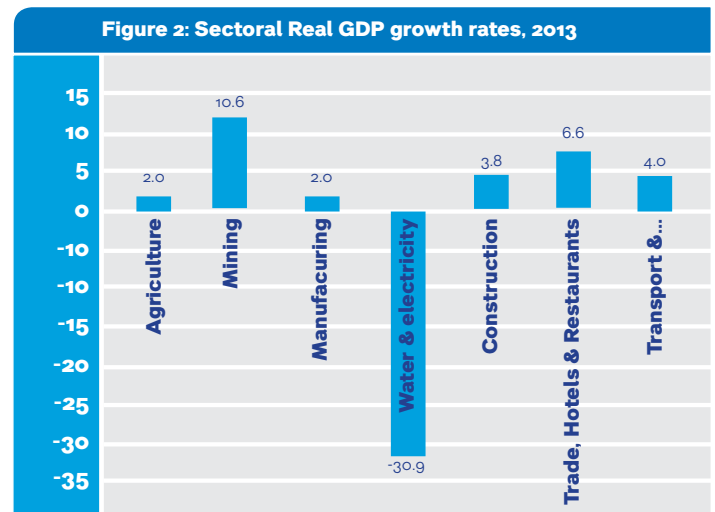
Economic Growth

Real GDP grew by 5.9 percent in 2013, an improvement from the 4.3 percent recorded in 2012 (Fig 1). The improvement in real GDP growth was mainly driven by the recovery of the mining sector, which grew by 10.6 percent in 2013 (Fig 2), after a 7.0 percent decline in 2012.



However, growth in the non mining GDP raises some concerns. It grew by 4.7 percent, down from the 8.1 percent recorded in 2012. This was largely due to the poor performance of the water and electricity sector (-30.9 percent – see fig 2), and the sluggish performance of manufacturing (2.0 percent) and agriculture (2.0 percent). The government (budget speech, 2014) attributes the poor performance of the water and electricity sector to the fact that the cost of inputs exceeded the value of sales. This is said to have been mainly due to the challenges arising from the delay in the commissioning of Morupule B Power Station,

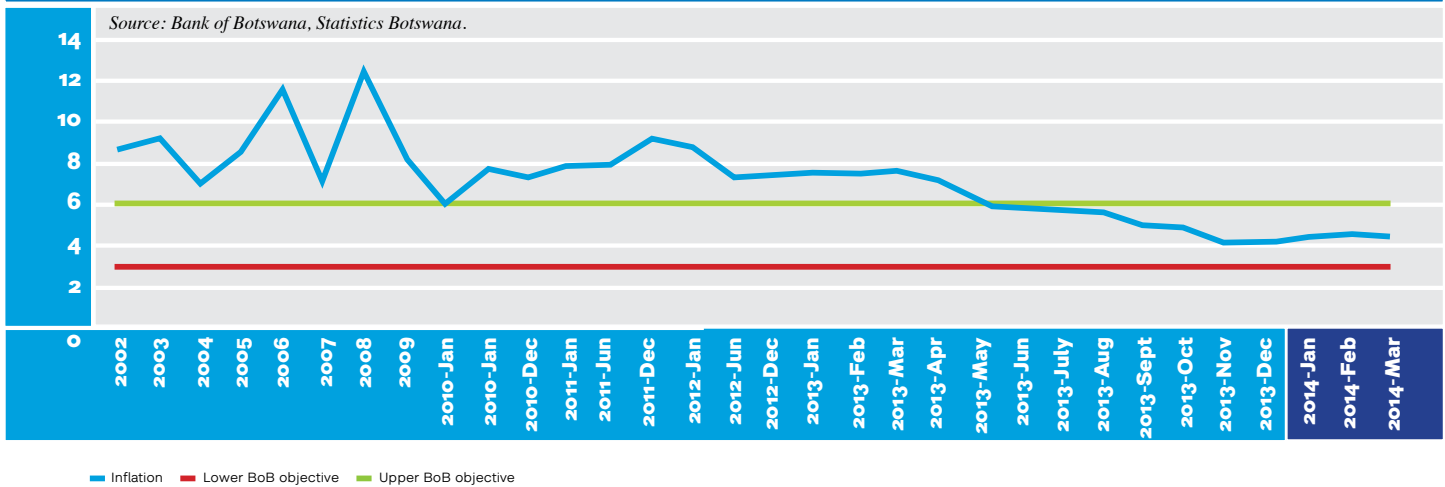
which resulted in a shortage of domestic power supply, and increased costs of imports from South Africa. It is of great concern that the water and electricity sector has faced challenges in the last few years, which calls on the authorities to expediently attend to these setbacks. If unresolved, the challenges within this sector may undermine other government economic efforts such as controlling inflation since price increases may be effected in the medium to long term to offset the said costs of inputs. Diversification efforts may also be affected since sectors that may provide impetus to the diversification process such as agriculture and manufacturing are utility intensive.



Inflation and Monetary Policy

The inflation rate went up from 4.1 percent in January 2014 to 4.6 percent in February 2014 before receding to 4.4 percent in March 2014, but still higher than the 4.1 percent recorded in January 2014. The upward inflation movement was largely due to the increase in alcohol levy in December 2013, as well as the introduction of a 30.0 percent tobacco levy (sin tax) on the 14th of February 2014.

Figure 3: Inflation level, Jan 2010 - March 2013

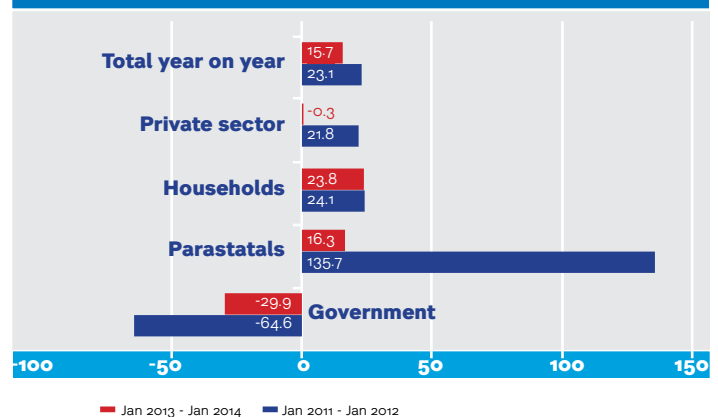


Going forward, we expect inflation to reach 5.5 percent during the second quarter of 2014, mainly on account of the anticipated increase in public sector wages and potential increases in administered prices. More importantly, moderate domestic demand is expected to help keep inflation within the Bank of Botswana's inflation objective range of 3 – 6 percent.

Credit Growth

Year on year credit growth between 2012 and 2013 was 15.7 percent, down from 23.1 percent recorded during the 2011 – 2012 period. The highest growth rate was recorded by the household sector (23.8), followed by parastatals. The fall in the overall bank credit may be attributed to recent calls by among others, the International Monetary Fund (IMF) to monitor bank credit growth. It may also be due to the fact that restraint in public sector wage increases has led to reduced appetite for lending or that banks have become more cautious in their lending activities. The Government is the largest single employer.

Figure 4: Credit Growth, Jan, 2011 – Jan 2012 and Jan 2013 – Jan 2014



International Trade

International trade data released in February 2014 show an improved trade balance from -16.4 billion in 2012 to 6.5 billion in 2013.

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Figure 5: Overall Trade Balance, Jan 2012 - Feb 2014 ('000 pula)

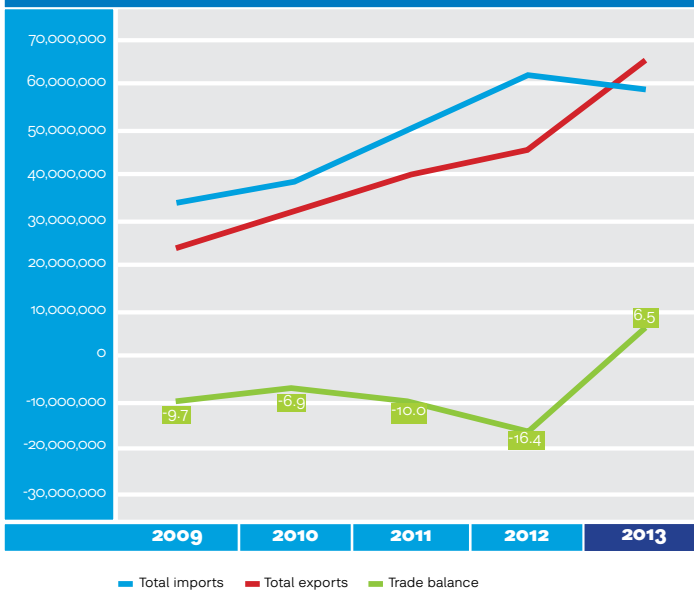
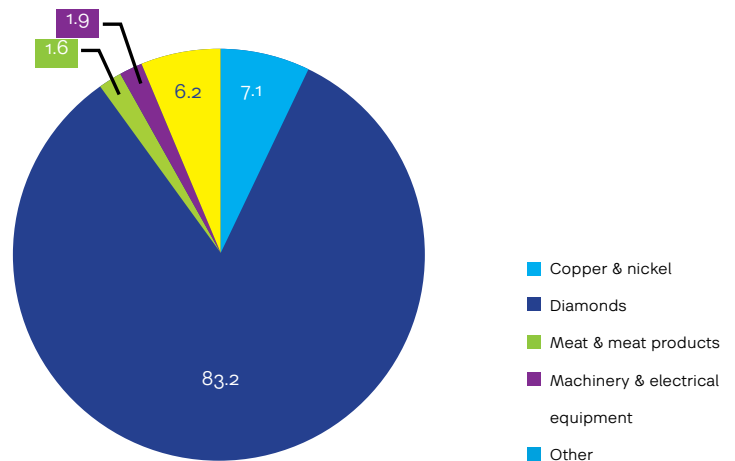


Figure 6: Composition of Exports, 2013



Economic Outlook

In terms of the composition of exports, diamonds accounted for the largest share (83.2 percent) in 2013, followed by Copper Nickel (7.1), machinery and electrical products (1.9) and the meat and meat products sector accounting for a paltry 1.6 percent. This shows the continued reliance of Botswana on mining, which has a combined diamonds and copper and nickel contribution to exports at 90.3 percent of exports. This is an astonishingly high proportion and reinforces the long standing call to not only diversify production but also diversify export commodities. The poor performance of the meat and meat products sector has been attributed to the delisting of the Botswana Meat Commission (BMC) from the European Market. It is therefore important that all be done to improve the export performance of the meat and meat products industry, including diversifying the export markets and adhering to the sanitary and phytosanitary standards as required by the major markets.

The latest budget forecasts a surplus of P922 million, an improvement over the P835 million in the revised estimates. This augurs well for the country's economic outlook, at least as far as maintaining a surplus budget and some degree of sustainability is concerned. However, it is a concern that the surplus was partly achieved through under expenditure of the development budget (11.0 percent of the revised estimates). Under expenditure of the development budget implies not realizing total planned investment, which in turn affects the economy's productivity and growth. That is, under spending of the development budget in 2013/14 will compromise the growth potential in 2014/15. To address this problem, the Government has indicated that there are plans to improve project implementation, including delisting of non performing contractors. However, the fact that under spending has been a recurring problem over the past years casts doubts on the authorities' strategies aimed at improving project implementation.



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Another concern relates to the persistent power shortages. These are likely to manifest themselves in two folds. First, productivity losses arising from power interruptions. Second, an increase in power prices in the medium and longer term, which would in turn lead to increased costs of doing business. Unless the power challenges are addressed as a matter of urgency, economic growth and productivity will be negatively affected during 2014/15 and beyond.

On a positive note, Inflation outlook during 2014/15 is positive in the medium-term. This is largely due to expected lower domestic demand and low levels of inflation within the major trading partners during this period. However, pressure to increase public sector wages remains and may intensify as October 2014 closes in. In an event of a salary increase; care should be taken to ensure that such an increase is backed by economic fundamentals such as productivity growth.

Further, the IMF economic outlook published in April 2014 anticipates the strengthening of the global economy. This global recovery is expected to be led by the advanced economies. This increases prospects of steering the 2013 diamond market recovery into 2014. For example, in the United States, GDP grew by 3.3 percent in the second half of 2013, compared with 1.2 percent in the first half or an average 2.3 percent. In addition, the US economy is expected to grow by 2.8 percent in 2014 and 3.0 percent in 2015. The IMF further states that the Euro Zone has finally emerged from recession, although there are concerns about low inflation. Economic recovery picked up in Asia in the second half of 2013, with an expected growth for the year at 5.2 percent and 5.5 percent in 2014. This outlook is therefore positive for the improved performance of the diamond market, and the Botswana economy in general.



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