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ECONOMIC REVIEW

third quarter july-sept 2019

in this issue ...

COMMENTARY

Economic uncertainties from the diamond market and national elections

Introduction

The third quarter of 2019 has been a strange one for the economy, in part because national developments were dominated by the general elections scheduled for October 23rd. Because the election outcome was more uncertain than perhaps any previous election, there was a pervasive feeling that many key decisions were being put on hold until the outcome of the election was clear. This applied to both the private sector and the public sector. In the private sector, firms seemed to be adopting a "wait and see" attitude, pending the election outcome that could usher in a significant change in the economic policy environment. Similarly, in the public sector, the knowledge that there would a new Cabinet and widespread changes in ministerial appointments, whoever won the election, added to the air of uncertainty.

BDP scores another victory, despite a stiff opposition challenge

The 12th Botswana general election held on October 23rd was won by the ruling Botswana Democratic Party (BDP). While this was, in our view, always the most likely outcome, the election was perhaps the most closely fought in recent decades, and it seemed that there was a reasonable possibility that the main opposition grouping, the Umbrella for Democratic Change (UDC) might have won, or indeed that there could have been no overall majority, leading to a hung Parliament.

In the event, the BDP increased its share of the popular vote significantly, from 47% to 53%, which can be taken as a vote of confidence in the BDP and a personal victory for its leader, President Mogkweetsi Masisi. At the Parliamentary level, however, the result was similar to that of 2014 in terms of overall numbers; the BDP's representation increased from 37 MPs in 2014 to 38 in 2019. With 57 elected seats in total, this is a comfortable victory that secures President Masisi a 5-year term in office and marks his first victory in his own right.

The new government entails a mixture of continuity and change. While there is continuity in the form of ongoing BDP rule, President Masisi has made it clear that he intends to implement a transformational agenda that will enable Botswana to address current challenges. In doing so he will need to use his victory and the vote of confidence that it represents to introduce some dramatic changes, some of which might be politically unpopular, in the expectation that these will bring about dividends in the second half of his term.

Economic transformation is complex and difficult, and has to result in Botswana becoming more competitive and productive than it is at present. This may involve making the most of "4th Industrial Revolution" technologies such as artificial intelligence, but first of all it has to focus on getting the basics right and delivering public services efficiently – filling in potholes, getting streetlights to work, making sure there are medicines in clinics and textbooks in schools, and ensuring that the government data network is functional.

President Masisi's Cabinet will have many new faces, in part because there are so many new BDP MPs. They will have many urgent challenges, including dealing firmly with corruption; rational prioritisation of competing spending demands; improving implementation of projects; and having the courage to terminate or significantly change ineffective programmes. These are all pre-requisites for increasing the rate of economic growth and significantly improving job creation.

Economic Growth

On the economic front, the third quarter was a tricky one for the global diamond market. Market weakness continued, with overstocking and a lack of profitability in the midstream (diamond trading, cutting & polishing), a shortage of bank liquidity for financing diamond stocks, and market uncertainty in the US and China due to macroeconomic developments and their continuing trade dispute, now compounded by unrest in Hong Kong. As a result, sales of diamonds through De Beers have been very weak, with sales in the third quarter down by almost 50% on the same period last year. De Beers' strategy is to maintain prices, but take some of the pressure off sightholders by reducing the amounts they are required to buy, hence, easing financing pressures. De Beers is also buying back some diamonds, in a manner that indirectly reduces the prices that sightholders have to pay, thereby responding to market pressures for price reductions to restore margins in the mid-stream.

Both the pre-election economic doldrums and diamond weakness will eventually show in economic growth numbers for the third and fourth quarters this year (the latter compounded by a lengthy 3-day public holiday for the elections, leading to lower output and hence GDP). The most recent GDP numbers are for the second quarter to June 2019. These show a decline in annual GDP growth, to 3.9% over the year to June, down from 4.4% in the year to March 2019. The decline is mainly due to a slowdown in the growth of diamond mining, as Debswana took advantage of the weak market to bring forward planned maintenance, resulting lower output in the second quarter. Growth of the non-mining private sector was higher, at 4.4%, although this was still below the annual growth rate in March. Our forecast for GDP growth for the year as a whole remains at 3.5%-4%.

Certainly, the level of confidence shown by the private sector seems to have dropped, in contrast to the upbeat situation a year ago following the accession of President Masisi. This may partly reflect election-related uncertainty and a postponement of investment decisions. Bank lending to the private sector has been subdued, with negative year-on-year growth, hence a decline in absolute terms from the peak of just over P22 billion in October 2018 to P21.2 billion in July 2019. The Bank of Botswana's new quarterly Business Expectations Survey also shows a decline, with a net balance of 39% of firms having positive perceptions about business conditions in Q3 2019, down from 52% in June. On a more positive note, a net balance of 68% of firms have positive perceptions of conditions over the next 12 months (to Q3 2020).

Exports

The weakness in exports that we highlighted in the last quarter has been ameliorated to some extent in the second quarter. Relative to the poor first quarter, there have been some improvements. However, compared to 2018, export performance was weak in the first half of 2019; this applies across almost all categories of exports, both mineral and non-mineral (manufactured goods), with only the miscellaneous "other goods" export category showing an increase between the first half of 2018 and the first half of 2019. Given the importance of export-led growth to Botswana's future economic sustainability, this is of great concern.

There are presumably many factors behind this decline, including slower global and regional economic growth reducing export market opportunities. However, Botswana also seems to be falling victim to protectionist measures in South Africa, with government procurement contracts specifying 100 percent local content for certain inputs. This has affected one major Botswana exporter of manufactured goods particularly badly. Not only does this contradict the spirit of regional trade agreements (such as the SADC Free Trade Area), it also conflicts with the South African National Treasury's own "Economic Transformation" document released in August this year, which "identifies regional integration through contributing towards industrial development in Africa, as a component of South Africa's industrial policy.... this entails ensuring that there is reciprocity in trade with countries in the region by allowing them to export products to South Africa ... [and] needs to prioritize strategic regional value chains that facilitate mutually beneficial trade" (p52-3). Such counter-productive non-tariff barriers to trade need to be raised and dealt with at the highest political levels, if they cannot be resolved in other fora.

Inflation and Credit

Inflation has remained low, despite a small increase to 3.0% over the quarter. With inflation expected to remain around the lower end of the Bank of Botswana's inflation objective range for the foreseeable future, the Bank Rate (the main policy interest rate) was cut by 25 basis points to 4.75%, its lowest ever level. This may encourage borrowing and investment, but the sluggish pace of credit growth to the private sector, with interest rates already low, suggests that other factors are important in influencing economic activity. As interest rates are reduced, savings are discouraged; most deposit interest rates are already negative in real terms.

Coal, Energy & Climate Change

A highlight of the quarter globally was the meeting of the United Nations General Assembly and its particular focus on climate change, as well as growing international concerns about the impact of global warming and the lack of progress in mitigation measures. As with most other countries, Botswana is experiencing the impact of global warming, with rising temperatures and more erratic rainfall. This also raises important questions for Botswana's energy strategy, in terms of choices regarding future energy supply, and more generally the utilisation (or not) of Botswana's large coal reserves. While there is some support domestically for various coal-related projects, the reality is that such projects are now almost impossible to finance commercially, with banks declining to get involved. The apparent withdrawal of Marubeni and Japanese export credit and insurance entities from the proposed Morupule B 5/6 coal-fired power station project is an illustration of this. At the same time interest in solar power projects is rising, as costs fall, although the high cost of electricity storage is still a barrier. We will cover these developments in more depth in a future issue of the Review.

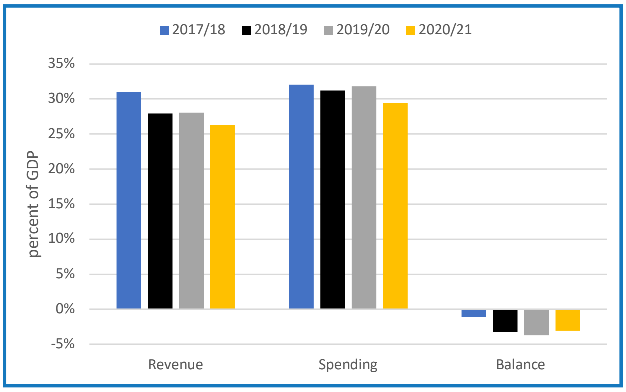
The 2020/21 Budget Strategy Paper

One of the most significant developments of the quarter was the release of the 2020 Budget Strategy Paper (BSP) by the Ministry of Finance and Economic Development. This included updated fiscal figures for the 2018/19 financial year, based on actual revenue and expenditure data, which can be compared with the revised budget figures presented at the time of the Budget in February this year. The BSP showed that 2018/19 revenue came in well below budget, mainly due to the under-performance of mineral revenues, reflecting diamond market weaknesses. At the same time, Government expenditure also came in below budget, with underspending on both the recurrent and development budgets. While underspending on the development budget is a regular occurrence, due to a variety of project and programme implementation constraints, it is unusual for there to be such a large underspend on the recurrent budget. As the underspend was larger than the reduction in revenues, the resulting budget deficit, at P6.4 billion, or 3.3% of GDP, was marginally smaller than that projected in the 2019 Budget.

Revised data for the current (2019/20) fiscal year show a downward revision of both revenues and expenditures as compared to the February 2019 Budge, with an increased deficit of P7.8 billion (3.8% of GDP) projected. The biggest change is the large downward revision of mineral revenues, from P21.1 billion to P16.7 billion, reflecting both market weakness and the impact of capital expenditure required for life-of-mine extensions at Jwaneng and Orapa. This is fortunately offset, to some extent, by windfall revenue from the Bank of Botswana (BoB), which has made an exceptionally large distribution of P5.0 billion to government, based on BoB's 2018 profits. On the spending side, overall expenditure has been revised slightly downwards, despite a significant projected increase in spending on personal emoluments following the public sector pay rise this year.

The BSP contains the first round of projections for the coming year's budget, i.e. for the 2020/21 fiscal year. This entails a modest increase in projected revenues in nominal terms (+1.5%), but, as this is slower than the rate of growth of GDP, the projections imply that revenues will fall from 28% to 26% of GDP. In order to keep the budget deficit in check, no increase in spending is budgeted. And this means that, due to the second increment to public sector salaries, the development budget has to be cut substantially, from P17 billion in 2019/20 to P12 billion in 2020/21. This illustrates the stark choice facing the country, given structural fiscal constraints: higher public sector salaries have to be paid for by lower development spending.

Figure 1:
Government Budget, 2017/18 – 2020/21



Source: MFED, Draft 2020/21 Budget Strategy Paper

Although the BSP does not present an explicit financing plan for budget deficits, it notes that a combination of drawdowns from the Government Investment Account (GIA) at the BoB and borrowing – mainly domestic – will be used. The scope for further drawdowns from the GIA is limited, at least if the government wishes to maintain a reasonable financial buffer that can be utilised in the event of future economic shocks. Hence the expectation is that deficits will be mainly financed by an expanded domestic bond issuance programme.

New Business-Related Legislation

The ending of the 11th Parliament in August 2019 also led to a flurry of legislative activity to complete various pieces of legislation, some of which had been in process for a long period of time. Amongst the key pieces of legislation concluded were the Trade Act, Industrial Development Act, Transfer Duty Act, Income Tax Amendment Act, Companies Re-Registration Act, BMC Transition Act, Financial Intelligence Act, and the Declaration of Assets & Liabilities Act.

Some of these laws are aimed at addressing weaknesses in Botswana's frameworks regarding anti-money laundering (AML) and international tax co-operation (notably the European Union's blacklist and greylist, respectively). The Trade and Industrial Development Acts reduce the scope of licensing requirements to businesses to where there are public health and safety concerns, and introduce much simpler registration requirements for most other businesses. Other objectives include strengthening the ability of tax authorities to deal with transfer pricing; providing the legal basis for company re-registration under the new Online Business Registration System (OBRS); enabling the corporatisation of the Botswana Meat Commission (converting from a statutory entity to a company limited by shares); requiring the declaration of assets and liabilities by those in public and political office; and reforming the scope of transfer duty on transactions involving immovable property.

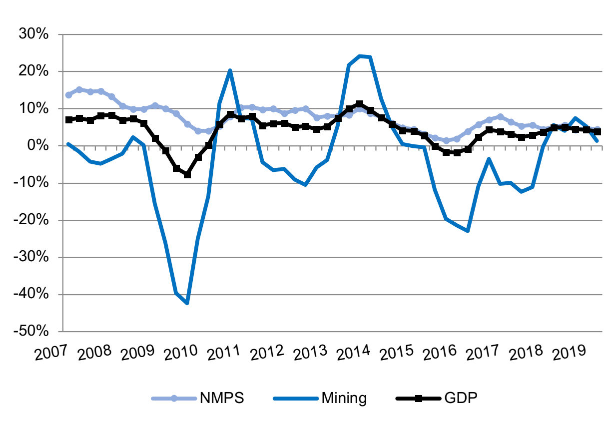
Some of these changes are driven by the ongoing Doing Business Reform Roadmap, and many have laudable objectives. The OBRS is a major step forward and will make it much easier to establish a business. Similarly with business licencing requirements, which have been reduced and streamlined. BMC reform enables its long-outdated monopoly on beef exports to be removed, and its eventual (part-) privatisation. Declaration of assets and liabilities can play a potentially important role in addressing corruption. The transfer duty amendment aims to close loopholes and extend the scope to include more types of property transactions, as well as provide relief for citizens buying houses.

But, along with the good, comes the bad and the ugly. Many businesses are concerned that the new transfer pricing rules will pose a heavy compliance burden. The OBRS removes all of a company's previous history from the record on re-registration. The declaration of assets and liabilities obligation is extremely far-reaching and appears to apply to any person or entity receiving public funds, including, potentially, all government employees, those supplying goods and services to government, as well as entities receiving any kind of subvention from government. And the rate of transfer duty on property purchases by foreign individuals and companies has been increased from 5% to 30%, which directly contradicts other efforts to make Botswana more attractive to foreign investors.

After years of concerns about the slow pace of getting new legislation passed, these reforms mark a welcome change. However, the downside is that some of the legislations have been rushed and the implications have not been thought through. Expect many amendments in the months and years to come.

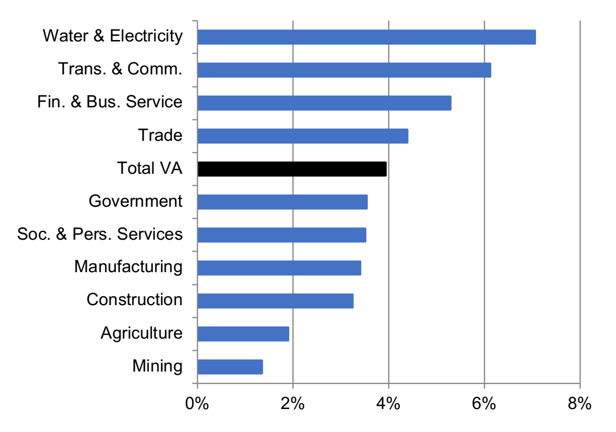
KEY ECONOMIC VARIABLES

Annual GDP Growth



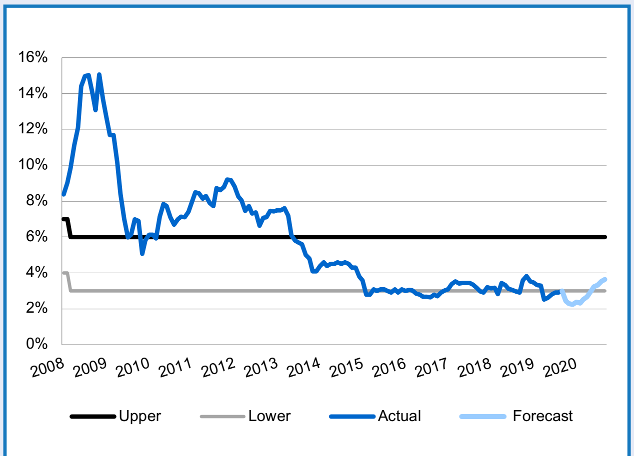
The Botswana economy slowed during the second quarter of 2019, as a result of the weakening global market for rough diamonds. Real GDP growth was 3.9% year-on-year in Q2 2019, down from 4.4% y-on-y growth recorded in Q1. Real growth in the mining sector experienced a sharp decrease from 5.3% y-on-y in Q1 2019 to 1.4% y-on-y in Q2 2019. Annual non-mining private sector (NMPS) growth also fell during the same period from 4.7% in Q1 to 4.4% in Q2. However, when excluding the wholesale sub-sector, which includes diamond trade, NMPS growth increased to 5.2% y-on-y in Q2 2019.

Sectoral GDP Growth



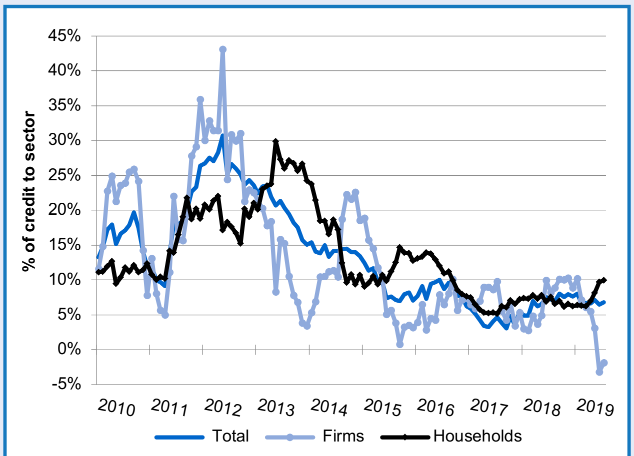
Economic performance was generally slower during Q2 2019, with most sectors experiencing lower y-on-y growth rates compared to the previous quarter. These include Mining, Agriculture, Construction, Manufacturing, Social & Personal Services, Trade and Transport & Communications. By contrast, Government, Finance & Business Services and Water & Electricity are the only three sectors which recorded higher y-on-y growth in Q2. As is generally the case, the fastest-growing sectors are mostly service sectors.

Inflation and Forecast



Annual inflation was 3.0% in September 2019, 0.2% higher than the inflation rate recorded in June 2019. Group indices were generally steady during the quarter, recording changes of less than 1.0%. In the medium-term, the annual inflation rate is forecast to go below the lower bound of the Bank of Botswana's medium-term objective range of 3-6% before gradually increasing in the second half of 2020.

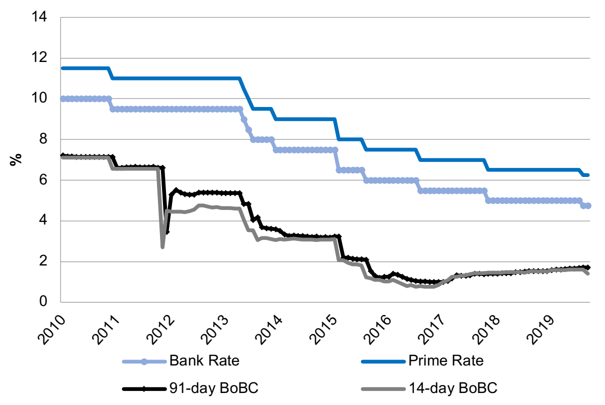
Annual Credit Growth



Annual bank credit growth rose marginally to 6.8% y-on-y in July 2019, up from 6.7% y-on-y in April. The increase in credit growth is attributable to credit to households, with growth up from 7.0% y-on-y in April 2019 to 9.9% y-on-y in July. Motor vehicle loans and unsecured personal loans were the main drivers of household credit growth. On the other hand, growth of credit to firms decreased significantly to minus 1.8% y-on-y in July 2019, from 5.5% in April 2019. This is of great concern, as it is the first time that annual credit growth to the private sector has been negative since the depths of the global financial crisis in September 2009. This subdued growth is as a result of businesses not fully utilising existing credit facilities as well as loan repayments by some companies.

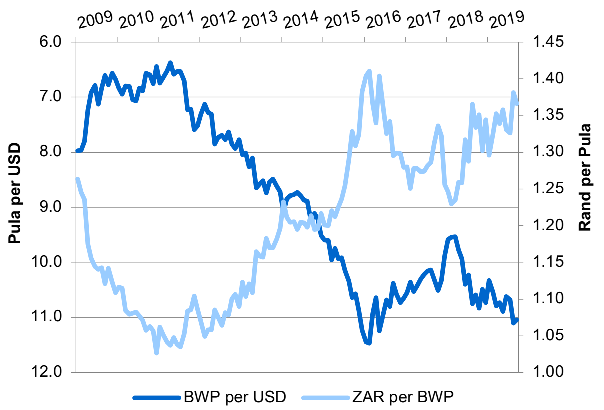
KEY ECONOMIC VARIABLES

Interest Rates



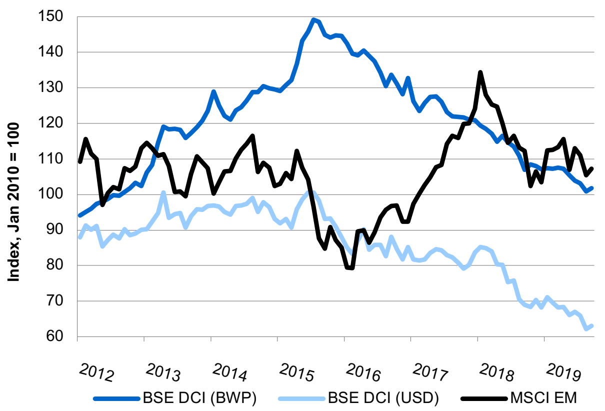
The Bank of Botswana's Monetary Policy Committee (MPC) reduced the Bank Rate by 25 basis points to 4.75% at the meeting held in August 2019. This was the first policy change since October 2017. The BoB noted that there were some upside risks to inflation from changes in administered prices, but that with weakening global growth and limited domestic demand pressures, the outlook for inflation was benign. This provided scope for monetary policy easing to support economic activity. The commercial bank Prime Lending Rate also changed from 6.5% to 6.25%. The 14-day BoBC and 91-day BoBC rates remained soft during the quarter with marginal changes.

Exchange Rates



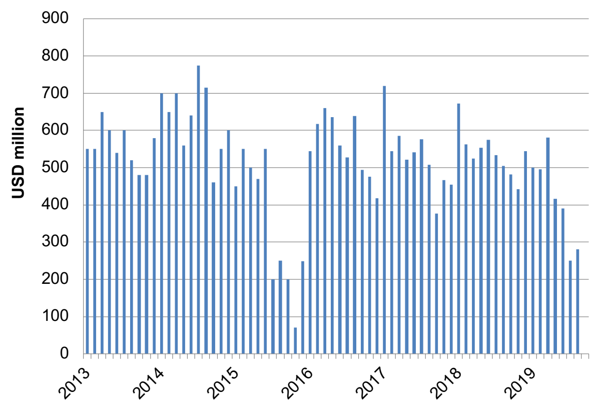
Foreign exchange rate trends were reversed during the third quarter of 2019, with the Pula weakening against the US dollar and gaining ground against the Rand. The Pula depreciated by 3.8% against the US dollar, ending Q3 2019 at 11.04 BWP per USD, from 10.62 in Q2. The Pula strengthened by 2.6% against the rand, to ZAR1.366 per BWP at the end of Q3, from ZAR1.331 in Q2. These developments are mainly driven by movements of the SA rand against the USD dollar in the context of the Pula basket exchange rate mechanism.

Stock Markets



The Botswana Stock Exchange (BSE)'s Domestic Companies Index (DCI) fell in Q3 2019 in both Pula and US dollar terms, by 2.1% and 5.9% respectively. At the end of the quarter, the DCI was 101.76 in Pula terms and 63.02 in US dollar terms, at January 2010 prices. The MSCI World and MSCI Emerging Markets indices also declined in Q3 2019, to 0.1% and negative 5.1% down from 3.3% and negative 0.3% respectively during the same period.

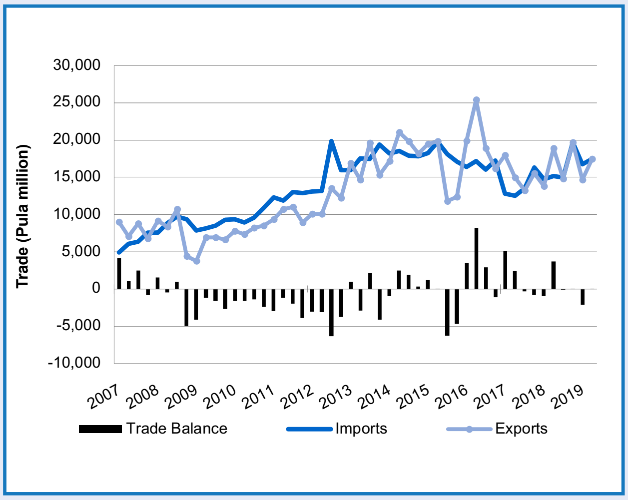
De Beers Diamond Sales



The global market for rough diamonds showed signs of severe weakness in Q3 2019, with the lowest Q3 sales since 2015. The global market is confronted with weak retail demand for diamond jewellery as well as an oversupply of rough diamonds and low margins in the midstream. De Beers Global Sightholder Sales (DBGSS) recorded sales of USD530 million in Q3, down from USD1,388 million in Q2, and approximately half of the value of sales in Q3 2018. Sightholders were also given supply flexibility options to either reject part of their allocations or exercise De Beers' buyback option to ease pressure without reducing rough prices.

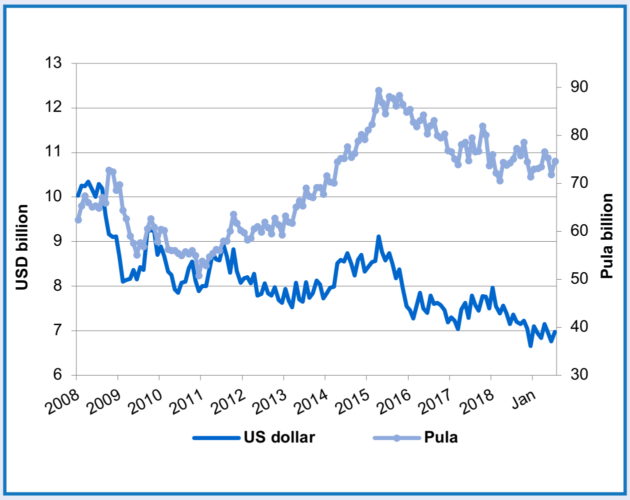
KEY ECONOMIC VARIABLES

International Trade



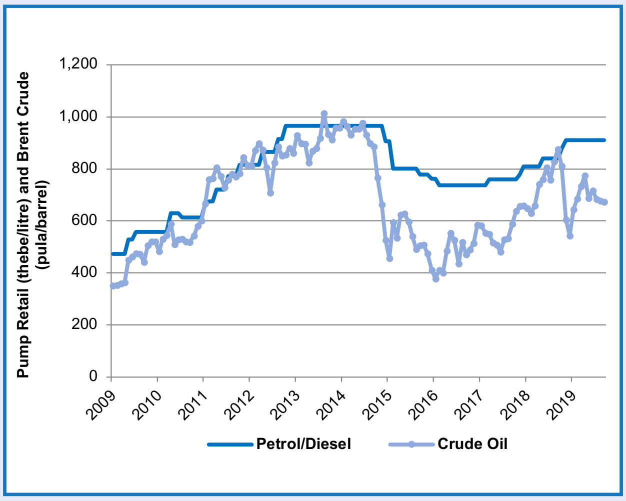
Total foreign trade picked up in the quarter to June 2019, with both imports and exports increasing during the period. Total imports grew by 4.2% from P16.7 billion in Q1 to P17.4 billion in Q2 2019. Exports rose by 19.3% from P14.7 billion to P17.4 billion. This resulted in a small trade surplus of P58.4 million in Q2, from a trade deficit of P2.1 billion in Q1. Most categories of exports grew in Q2, but only relative to a very weak Q1. Over the first half of 2019 as a whole, most categories of non-diamond exports declined relative to 2018.

Foreign Exchange Reserves



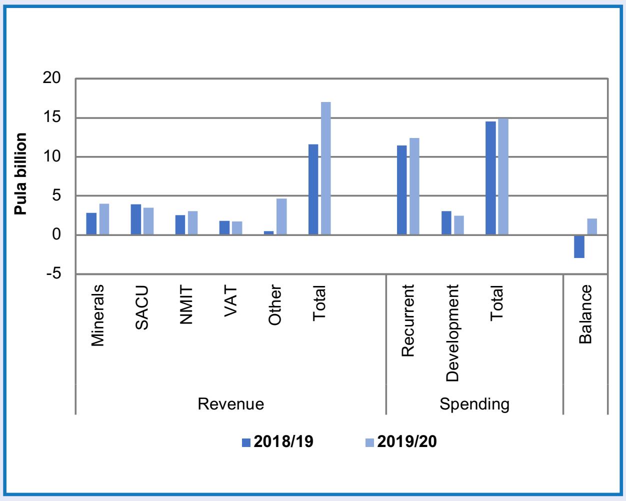
The foreign exchange reserves decreased across all measurement currencies - Pula, US dollar and SDR - in the first half of 2019. Foreign exchange reserves decreased by 2.3% in Pula terms to P74.58 billion in H1 2019. Similarly, foreign exchange reserves fell by 1.1% in US dollar terms and 1.4% in SDR terms, to USD6.77 billion and SDR4.86 billion respectively. The decrease in reserves reflects revaluation losses from movement in exchange rates as well as balance of payments deficits. The reserves were equivalent to 14 months of import cover of goods and services.

Fuel prices



Local retail prices for petrol and diesel have been held constant since they were increased in November 2018. However, international prices for fuel continued to move downwards in Q3 2019, dropping by 6.1%, following a decline of 2.2% in Q2. The decline in international oil prices seems to have been largely influenced by tensions between the USA and China over trade, which has led to concerns over global growth and the demand for oil. Despite this decline, local retail prices have not been reduced, because of the need to replenish the National Petroleum Fund (NPF), which has been depleted by unplanned fuel subsidies and illicit use of accumulated funds.

Quarterly Fiscal Data



Fiscal data for the first quarter of the 2019/20 financial year indicates a budget surplus of P2.1 billion for the period. This is a significant reversal from the deficit of P3.0 billion experienced in the same period in the previous year. The surplus is mainly due to "other income" of P4.7 billion, mainly comprising a one-off payment from BoB based on its 2018 profits. Because of this "windfall" income, the outturn should not be taken as representative of the year as a whole, for which a substantial deficit is projected. With regard to expenditure, development spending was 20% lower when compared to Q1 FY2018/19, and only 14.5% of the development budget for the year. Recurrent spending was largely in line with the budget.

NEWS HIGHLIGHTS

05/07/2019	Debswana's economic impact reached P18bn in 2018 (Mmegi)	Debswana's contribution to the economy of Botswana reached P18.4 billion in 2018, a seven percent increase when compared to 2017. According to a report published by Anglo American, this was achieved by an increase in corporate taxes, royalties to government, capital expenditure and wages paid by Debswana during the year.
09/07/2019	Firms optimistic in Q2 – Survey (Weekend Post)	Results from the Bank of Botswana's Business Expectations Survey indicate that firms were optimistic about economic activity during the second quarter of 2019. Despite anticipating limited access to credit in the domestic market, firms intended to increase their investment in buildings, plant & machinery, vehicles & equipment and other goods.
15/07/2019	ABN Amro restricts rough-sector lending (Rapaport)	Dutch bank ABN Amro has scaled back its financing of rough-diamond purchases. The bank will not be reducing their overall credit limit but restricting drawings under the rough-purchase sublimit. A letter from ABN Amro cites a "continued lack of profitability across a wide range of goods in the midstream pipeline." as the reason behind restrictions.
22/07/2019	Orapa mine scapegoated as Debswana production slumps (Weekend Post)	De Beers' rough diamond production decreased by 14 percent to 7.7 million carats during Q2 2019. Debswana production declined by 9 percent during Q2, driven by a 23 percent decline in production at the Orapa mine. This was due to a planned plant shut down, which was moved forward from the second half of the year.
24/07/2019	Jwaneng: USD2 billion investment for Botswana's brightest star (Mining Review)	Debswana has announced the Cut-9 expansion project for their Jwaneng mine. The Cut-9 project is expected to cost USD2 billion and will extend the life of mine by at least another five years.
26/07/2019	Govt shaves P2.3bn from BPC subsidy fund (Mmegi)	Government has cut P2.25 billion from the Botswana Power Corporation's (BPC) NDP 11 allocation for subsidies. The funds will be used for the Tshele Hills project, which is aimed at boosting national strategic oil storage capacity.
29/07/2019	Low equity turnover during 2019 H1 – BSE (Weekend Post)	Botswana Stock Exchange (BSE) Limited published their Market Performance Report for H1 2019 (1st January - 30th June). The report indicates that turnover was relatively low compared to the same period in the previous year. For the year to date, BSE recorded turnover of P866.9 million from a volume of 257.4 million shares traded. Over the same period last year, the BSE had a turnover of P1.1 billion and a total volume of 411.6 million shares traded. The top three traded companies were Wilderness Holdings, Botswana Insurance Holdings Limited and Sechaba Holdings.
31/07/2019	Cupric Canyon Capital awards Fluor Khoemacau contract (Mining Weekly)	The engineering, procurement and construction management (EPCM) contract for the Khoemacau copper and silver project has been awarded to Fluor Corporation. The scope of Fluor's work includes upgrading the existing copper concentrator plant and providing new mine surface infrastructure.
11/08/2019	Lucara profit drops amid lower-value output (Rapaport News)	Lucara Diamond Corp. profits declined to USD700,000 during Q2 2019, down from USD19.7 million in Q1 2019. This was due to an increase in production of smaller stones from its Karowe mine, which yielded a lower average price. Revenue from the Botswana deposit experienced a year-on-year drop of 34 percent, recording a value of USD42.5 million.
12/08/2019	Barclays opens Enterprise Development Centre (Weekend Post)	Barclays Bank of Botswana has opened an enterprise development centre. The centre will act as an all-services incubation base for local entrepreneurs. According to the bank's Head of Enterprise and Supply Chain Development, Ms Kushatha Chilisa, the centre is aimed at resolving numerous issues faced by SMMEs such as access to finance and a lack of office space amongst others.

NEWS HIGHLIGHTS

18/08/2019	Emerging manganese project in Botswana delivers hot economics (Mining Review)	Giyani Metals Corp. have reported positive results following a preliminary economic assessment (PEA) of their K. Hill manganese project. The PEA derived a pre-tax NPV of US369 million and an after-tax NPV of USD285 million for the project. The project carries a potential operating life span of nine years and is expected to produce 245,000t of high-purity electrolytic manganese metal (HPEMM).
18/08/2019	De Beers lets clients reject 50% of goods (Rapaport News)	De Beers will grant sightholders the ability to refuse more diamonds (50 percent) at their next sightholder sale in an attempt to ease pressure on the diamond market. De Beers have also increased their buy back commitment for customers' purchases to 20 percent, up from 10 percent.
19/08/2019	BPC goes for solar parks again (Sunday Standard)	Botswana Power Corporation has announced another round of invitation-to-tender for two solar PV plants with a total capacity of 100MW. The solar power parks are intended to reduce the country's dependence on power imports from Eskom in South Africa.
19/08/2019	UK firm revises botswana's economic prospects forecasts (Sunday Standard)	Fitch Solutions have revised their current account surplus projections for Botswana. They now forecast the current account surplus to be 1 percent of GDP in 2019 and 0.7 percent of GDP in 2020, down from initial projections of 8.2 percent and 7.8 percent of GDP respectively. The downward revision is due to the decline in diamond production, a sustained demand for imports and muted SACU income flows, all adding pressure on the current account surplus.
19/08/2019	Maatla Energy acquires P1.6 billion Mmamabula Energy & Coal mining (Weekend Post)	Maatla Energy has finalized a deal that has seen it acquire a majority shareholding stake in Jindal BVI Ltd from Jindal Steel & Power Limited. Jindal owns the Mmamabula coal deposit in eastern Botswana.
26/08/2019	Moody's cautions Letshego over credit risk from Pan African expansion (Weekend Post)	Moody's have maintained Letshego's Ba2 Corporate Family Ratings (CFR) and Ba3/Not Prime issuer ratings. Moody's went on to explain, "The stable outlook reflects our expectation that the company's financial fundamentals will remain robust over the next 12 to 18 months, despite elevated credit risks from its regional expansion".
28/08/2019	De Beers gem sales keep falling as buyers allowed to say no (Bloomberg)	De Beers recorded sales valued at USD280 million during their August sight sale, 44 percent lower than same period last year. This is attributed to midstream participants continuing to work down their polished diamonds stock and a reduction in manufacturing levels in key diamond cutting centres.
02/09/2019	BPC'S P2.3 billion transmission grid expansion on track (Sunday Standard)	The BPC North West Transmission Grid (NWTG) project registered a completion progress of 73 percent as at July 2019, against its target of 86 percent. According to project manager, George Moeti, a request for extension of time by the contractors is still under review. The NWTG project is aimed at providing the Northwest region of Botswana, along with the Chobe and Ghanzi districts, access to the national power grid. The cost of the project is P2.36 billion.
03/09/2019	BSE to collaborate with Zimbabwe Stock Exchange (Weekend Post)	The Botswana Stock Exchange (BSE) and Zimbabwe Stock Exchange (ZSE) announced that they will be signing a Memorandum of Understanding (MOU). The MOU will serve as a basis for co-operation between the two markets and is aimed at promoting cross-border investments and cross-border listings.
04/09/2019	Namibia and Botswana mull 20-year, 4.5 GW solar push (PV Magazine)	The World Economic Forum's Global Future Council on Energy has announced plans between Botswana and Namibia to develop 5 GW of solar capacity over the next twenty years. The project is expected to have three phases. The first phase could see a solar tender of 300-500 MW to meet domestic demand, the second phase is planned to allocate 0.5-1 GW more solar for exports and the third and final phase would generate 1-3 GW of solar to be traded across Africa.

NEWS HIGHLIGHTS

05/09/2019	WEF Africa: Botswana tells the world it wants to reduce dependence on diamonds (IOL Business Report)	President H.E Mokgweetsi Masisi has reiterated Botswana's desire to reduce its dependence on diamonds. Speaking at the World Economic Forum (WEF) President Masisi told an audience that Botswana would embrace the 4th Industrial Revolution and would focus on producing high quality products as the country's small population mean it cannot compete with other countries in terms of quantity, citing the beef market as an example.
06/09/2019	Botswana leader sees new diamond pact with De Beers after vote (Mining Weekly)	President H.E Mokgweetsi Masisi has stated that negotiations between Botswana and De Beers over a new diamond sales pact are "cordial" and "going as planned". The current 10-year deal expires in 2020 and negotiations over a new deal are aimed at improving profitability for both parties. The new deal is expected to be concluded after the general elections to be held in October 2019.
10/09/2019	Masama Coal Mine records first commercial sale (Weekend Post)	A market update statement by Minergy has stated that the Masama Coal project will record its first commercial sales during the month of September 2019. According to Minergy's CEO, Morné du Plessis, the company is completing the process of signing its first long-term customer and is in discussions with other regional industrial customers.
12/09/2019	Botswana, SACU seal post-Brexit deal (Mmegi)	The SACU-plus-Mozambique trading block has finalised a deal with the United Kingdom to allow trade to continue seamlessly between the two when the UK leaves the European Union. The formal signing of the agreement is expected to take place mid-October.
16/09/2019	Barclays 2019 H1 skyrocket to 49 percent growth (Weekend Post)	Barclays Bank published strong financial results for the half-year to 30 June 2019. Before-tax profits rose by 49 percent to P387 million in H1 2019, up from P260 million in H1 2018. The bank has attributed the strong performance to a growth in income, constrained costs and reduced credit losses.
19/09/2019	Karowe yields two massive stones (Rapaport News)	Lucara Diamond Corp. has recovered a 123-carat type II rough diamond and a 375-carat gem-quality stone from its Karowe mine in Botswana. Along with these two diamonds, the company has recovered 27 other diamonds over 100 carats.
23/09/2019	Strata-X seeks P110 million from BDC for Serowe coal funding (Weekend Post)	Strata-X Energy and Botswana Development Corporation (BDC) have signed a non-disclosure agreement for a financing strategy for the Serowe Coal-Bed Methane (CBM) project valued at P110 million. The agreement gives BDC a 60 to 90 day period to evaluate and conduct due diligence of the project with the aim of providing a financial package to develop the Serowe CBM project in the next three years.
26/09/2019	Better mining of energy minerals sought in U.S.-backed effort (Bloomberg)	The U.S., Botswana, Australia and Peru have announced The Energy Resource Governance Initiative, a partnership aimed at encouraging responsible mining of rare earths and other minerals which are used in car batteries, wind turbines and solar panels.
26/09/2019	Lucara recovers gem-quality blue, pink diamonds at Karowe (Engineeringnews.co.za)	Lucara Diamond Corp. announced the recovery of a 9.74-carat gem-quality blue diamond and a 4.13-carat gem-quality pink diamond from the direct milling of the South Lobe ore at its Karowe mine. The diamonds will be sold at the company's fourth quarter tender which will be held in December.
27/09/2019	Shumba's P20bn plant targets 25,000 barrels of fuel per day (Mmegi)	Shumba Energy has announced that its planned Coal-to-Liquids (CTL) plant is expected to produce 20,000 barrels of diesel and 5,000 barrels of petrol per day once fully functional. The CTL plant is currently undergoing a bankable feasibility study and is estimated to cost between USD1.5 billion and USD2 billion.

MACRO-ECONOMIC DATA

Key Economic Data	*unit*	2014	2015	2016	2017	2018	2019Q1	2019Q2	2019Q3
Annual Economic Growth									
GDP	*%*	4.1	-1.7	4.3	*2.9*	*4.5*	4.4	3.9	..
Mining	*%*	0.5	-19.6	-3.7	-11.1	5.3	5.3	1.4	..
Non-mining private sector	*%*	4.9	1.4	*7.1*	*5.6*	*4.7*	4.7	4.4	..
GDP current prices	*P mn*	145,868	146,066	*170,564*	*180,102*	*189,869*	48,850	49,242	..
GDP 2006 prices	*P mn*	87,569	86,083	89,787	*92,398*	*96,513*	24,485	24,814	..
Money & Prices									
Inflation	*%*	3.8	3.1	3.0	3.2	3.5	3.3	2.8	3.0
Prime lending rate	*%*	9.0	7.5	7.0	6.5	6.5	6.5	6.5	6.25
BoBC 14-day	*%*	3.07	0.97	0.84	1.45	1.52	1.60	1.60	1.40
Trade & Balance of Payments									
Exports - total goods	*P mn*	76,261	63,484	80,336	61,672	67,162	14,662	17,494	..
Exports - diamonds	*P mn*	65,328	52,730	70,781	54,384	60,411	13,519	16,088	..
Balance of payments	*P mn*	11,404	- 57	2 843	61	-4 204	- 907	..	..
Foreign Exchange									
Exchange rate BWP per USD	*end*	9.515	11.236	10.650	9.872	10.730	10.787	10.616	11.038
Exchange rate ZAR per BWP	*end*	1.217	1.383	1.279	1.256	1.344	1.353	1.331	1.366
FX reserves	*$ mn*	8,323	7,546	7,189	7,502	6,657	6,843	6,765	..
FX reserves	*P mn*	79,111	84,881	76,804	73,693	71,427	73,505	71,814	..
Financial Sector									
Deposits in banks	*P mn*	51,492	59,961	62,438	63,581	69,271	71,640	71,484	..
Bank credit	*P mn*	45,116	48,307	51,316	54,181	58,332	58,362	60,177	..
BSE index		9,501.6	10,602.3	9,727.7	8,860.1	7,853.5	7,885.6	7,622.5	7,461.0
Business Indicators									
Diamond production *(a)*	*'000 cts*	24,658	20,732	20,880	22,961	24,377	6,081	5,828	..
Copper production (b)	*tonnes*	46,721	23,050	16,878	1,239	1,462	..	..	..
Nickel production	*tonnes*	14,958	16,789	13,120	0	0	0	0	..
Business confidence index		52%	44%	43%	46%	..	..	..	..
No. of companies formed		16,300	19,134	17,133	20,707	..	..	..	..
Electricity consumption	*GWh*	3,990	3,974	3,929	3,772	3,919	966	926	..
Crude oil (Brent)	*$/bar*	55.27	36.61	54.96	66.73	50.57	67.93	67.52	60.99
Employment (formal)									
Government		129,918	130,220	129,216	129,009	133,238			
Parastatals		18,790	19,411	19,008	19,444	19,830			
Private sector		191,399	191,484	194,202	193,745	195,681			
Total		340,107	341,115	342,426	342,198	348,749			

Govt Budget		2016/17 (d)	2017/18 (d)	2018/19 Preliminary (d)	2019/20 Revised (e)	2020/21 Projections (e)
Revenues	*P mn*	57,398	56,411	*54,513*	*58,238*	59,125
Spending	*P mn*	56,275	58,393	*60,858*	*66,025*	66,067
Balance	*P mn*	1,123	-1,982	*-6,345*	*-7,787*	-6,941
Public debt & guarantees	*P mn*	36,864	*45,542*	*46,012*	*52,980*	
Govt deposits at BoB	*P mn*	29,819	30,094	*21,559*		
GDP	*P mn*	174,630	182,195	*194,901*	*207,568*	*224,607*
Revenues	*%GDP*	32.9%	*31.0%*	*28.0%*	*28.1%*	*26.3%*
Spending	*%GDP*	32.2%	*32.0%*	*31.2%*	*31.8%*	*29.4%*
Balance	*%GDP*	0.6%	*-1.1%*	*-3.3%*	*-3.8%*	*-3.1%*
Public debt & guarantees	*%GDP*	21.1%	*25.0%*	*23.6%*	*25.5%*	*0.0%*
Govt deposits at BoB	*%GDP*	*17.1%*	*16.5%*	*11.1%*	*0.0%*	*0.0%*

Sources: Bank of Botswana; MFED; Statistics Botswana; Department of Mines; Registrar of Companies; BSE; Econsult

Notes:

(a) From 2013, figures include production from Lucara Diamonds (Karowe mine) and Debswana. From 2016, figures also include production from Gem Diamonds (Ghagoo) and Lerala mines, which ceased in February 2017 and April 2017 respectively

(b) Copper production starting Q2 2017 for Mowana mine

(c) Numbers in Italics reflect revisions from the previous review

(d) Actual

(e) Budget

SPECIAL FEATURE

The Microeconomic Policy Environment

Botswana has traditionally paid a lot of attention to the management of macro-economic policy – including monetary policy, exchange rate and fiscal. The balance of macro-economic policy is generally seen as having been favourable and supportive of growth and stability. Currently, fiscal policy is playing a stabilising role, with a modest fiscal deficit within the context of a medium-term balanced budget objective. Interest rates are at their lowest ever level, in nominal terms. The nominal effective exchange rate is stable, although, as we have argued previously, the Pula is probably overvalued in real terms, which does not support export-led growth. The category of macro-economic stability is by far Botswana's best performance in the World Economic Forum's Global Competitiveness Index, where the country is ranked in first place globally.

So why is economic growth and employment creation not stronger? From an economic policy perspective, macro-economic policy is only part of the story; it is important to also consider the micro-economic policy environment. Micro-economics focuses on how individual markets operate, and the micro-economic environment is the set of prices, regulations, institutions, taxes and subsidies that govern the operation of markets. All of these characteristics create a set of prices and incentives that economic agents respond to – in terms of decisions regarding purchases, investment, production, employment, trade, etc. Micro-economic policy includes actions to change the way in which markets operate, such as to make them more efficient, remove distortions, correct market failures, and increase competition, and more generally to guide and influence the micro-economic decisions of economic agents. It has links to macro-economic policies, especially those that affect prices and the returns to different types of investment, such as exchange rates, tax and subsidy policy etc.

The markets in question include those for different types of goods and services, but also financial markets, labour markets, etc. Below we consider policies and outcomes in different markets and segments of the economy, as follows:

- Business environment (investment climate);
- Public enterprises (parastatals and state-owned enterprises);
- Financial markets;
- Labour markets;
- Market-facing / regulatory institutions;
- Subsidies policy and price controls;
- International trade policy.

Investment Climate – the "Doing Business" Environment

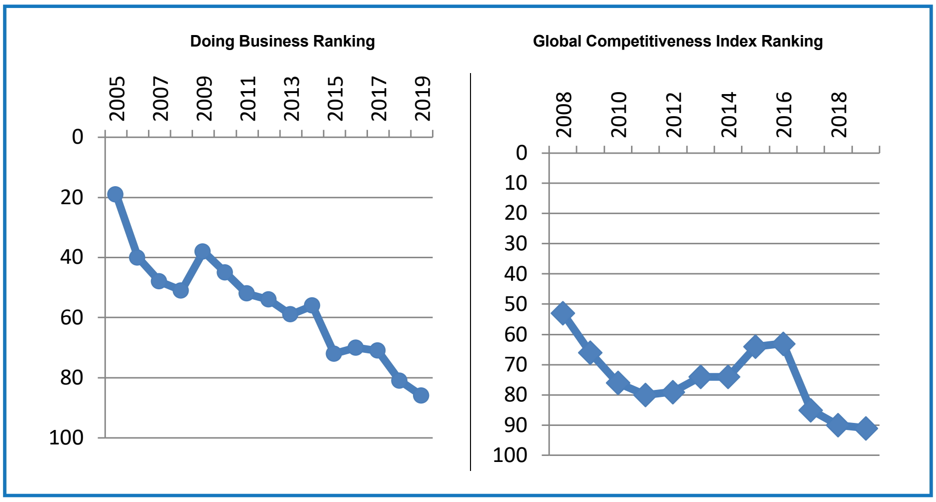
The investment climate in a country covers a wide range of factors that influence the attractiveness of an environment to private sector investors. Several aspects of the investment climate are assessed by the World Bank's annual Doing Business reports, which examine a range of factors relevant to the business life-cycle: starting a business, dealing with construction permits, getting electricity, registering property, getting credit, protecting minority investors, paying taxes, trading across borders, enforcing contracts, resolving insolvency and labour market regulation. Countries are given scores on all of these indicators, and are also ranked.

For Botswana, the absolute measure of the quality of the business environment (the DB score) has remained more or less unchanged in recent years. Nevertheless, Botswana's Doing Business ranking has declined, from 19 in 2005 to 86 in 2019 (Figure 1). This illustrates that other countries improved their business environment while Botswana stood still (leading to the lower ranking), and confirms the need to take action to improve the absolute Doing Business score through enhancements of the business environment.

A related assessment is conducted by the World Economic Forum (WEF), which rates each country under the Global Competitiveness Index (GCI) annually. The GCI covers a somewhat different set of indicators to the Doing Business assessment, specifically: macroeconomic stability, financial system, ICT adoption, infrastructure, health, business dynamism, skills, product markets, market size, innovation capability, labour market and institutions. Botswana's rankings on the GCI have also followed a downward trend over the years, albeit with a period of improvement between 2012 and 2016.

SPECIAL FEATURE

**Figure 1:
Business Environment Rankings**



Source: www.doingbusiness.org; www.weforum.org/reports/the-global-competitveness-report-2019

Considerable attention has been paid to improving the business climate in recent years. Initiatives include the establishment of the National Doing Business Committee; the adoption by Cabinet of the Doing Business Roadmap, with a range of action items, and the establishment of the Botswana One-Stop Service Centre (BOSSC) by the Botswana Investment and Trade Centre (BITC). Some improvements have been made, including the new Trade and Industrial Development Acts, and the introduction of online business registration by the Companies and Intellectual Property Authority (CIPA). However, a number of further reforms are needed:

- Speeding up of the legislative process, so that improvements in the business environment that require changes in the law are implemented faster;
- Continued progress in government in the transition from a "controlling" approach towards the economy and the private sector to a "supportive/facilitative" one;
- Reducing excessive regulation, and introducing Regulatory Impact Assessments, so that regulations are only introduced when the anticipated benefits exceed the costs;
- Further liberalisation of restrictive immigration requirements, through, e.g. online visa processing and improved availability of work permits for skilled workers and investors;
- Improving statistical capacity, to support evidence-based policymaking, and monitoring and evaluation;
- Improved screening of policies across government to ensure that they are consistent with the agreed Doing Business Road Map;
- Investment in ICT to improve connectivity and reduce costs;
- Improving the quality of public service delivery, shifting government services online (eGov), while ensuring reliability of the Government Data Network; and
- Implementing the "one-government" principle (whereby the public would have a single point of contact and would not have to deal separately with government departments and agencies even for a single process).

Public Enterprises – Privatisation and Reform

The number of parastatals (statutory entities) and state-owned enterprises (SOEs) has been increasing over the years, to around 60. These can be classified into different types, as follows:

- Commercial (18)
- Commercial financial (6)
- Regulatory (16)
- Developmental (11)
- Education (5)
- Other (4)

The Privatisation Policy (2000) proposed reducing the number of public enterprises through privatisation and rationalisation of those with overlapping mandates. Implementation of this policy has been slow, with one partial privatisation (Botswana Telecommunications Corporation, although this is still a SOE as majority share ownership remains with government), and two mergers[1]. Furthermore, some public enterprises are monopolies, which has an adverse impact on competition and efficiency in their respective markets.

[1] The International Financial Services Centre (IFSC) and Botswana Export Development and Investment Agency (BEDIA) were merged to form the Botswana Investment and Trade Centre (BITC), while the Rural Industries Innovation Centre (RIIC) and Botswana Technology Centre (BoTEC) were merged to form the Botswana Institute for Technology Research and Innovation (BITRI).

SPECIAL FEATURE

Many public enterprises require subventions (subsidies) from government, which adds to public spending, and may reflect inefficiency. Policy priorities should include identifying further parastatals for privatisation and rationalisation; removing monopolies and facilitating competition; improving parastatal governance and transparency; de-politicisation of appointments to parastatal boards and management; and assessment of whether subsidies to parastatals are achieving identifiable benefits and value for money. Fortunately, Government has committed to removing one of the most destructive monopolies in place, the BMC monopoly of beef exports. Public accountability and transparency requirements should be applied to SOEs (companies owned by government), as well as statutory parastatals.

Financial Markets

The financial sector has become more competitive and efficient over the past decade. Competition has been helped by the entry of new banks through the Bank of Botswana's licensing policy, such that in 2019 there are 12 deposit-taking institutions, including 10 licensed commercial banks, one statutory bank (Botswana Savings Bank) and one building society (Botswana Building Society, in the process of converting to a bank). For lending, in addition, there are three development finance institutions (National Development Bank, Botswana Development Corporation and the Citizen Entrepreneurial Development Authority (CEDA), various government funds (such as the Youth Development Fund (YDF), and a number of private sector non-bank lenders. In banking, interest rate spreads and profits have fallen as competition has increased. However, there are questions around the impact and cost-effectiveness of CEDA and YDF, neither of which operate on a commercial basis and require considerable subsidies.

Around the world, the financial sector environment is changing rapidly, largely driven by financial technology ("fintech"), the growth of payments instruments (notably mobile money, payment cards and phone-based apps). Much of the innovation is coming from outside of the traditional banking sector. Further regulatory reform will help to support similar developments to improve financial inclusion in Botswana, including allowing "regulatory sandboxes" to support innovation[2]. Fintech will help support the provision of "branchless" banking and financial services more generally through electronic, web and app-based channels rather than through physical channels, and thereby help reach those who are currently under-served or un-served financially. The high rate of mobile phone penetration in Botswana supports the potential of these methods of financial service delivery. This will require regulatory reform, for instance changes to banking regulations and the introduction of "tiered" bank licensing, to enable new types of financial institutions to enter the market. It is also important to ensure that Know-Your-Customer (KYC) regulations do not act as a barrier to the provision of financial services to the unbanked and underserved.

Botswana has relatively low access to finance for a country of upper-middle income status, with limited use of banks by those outside of formal employment. To improve access to finance, a Financial Inclusion Roadmap and Strategy covering the period 2015 – 2021 has been agreed, with five priority areas: development of the payments ecosystem; facilitation of accessible, low cost, savings products; development of accessible risk mitigation products; improvement of the working of the credit market; and consumer empowerment and protection.

Data on financial inclusion in Botswana lags and needs to be updated. The most recent FinScope survey, which provides comprehensive information on access to finance by households and on which the Financial Inclusion Roadmap was based, was carried out in 2014. A new FinScope survey is urgently required (one is planned for late 2019), and should be complemented by a FinScope SMME survey, to gather information on the financial situation of SMMEs and the constraints they face.

Labour Markets

Several microeconomic interventions have taken place in labour markets. These include the activities of parastatals such as the Botswana National Productivity Centre (BNPC) and the Human Resources Development Council (HRDC), focused on developing skills, increasing productivity, and improving the availability of labour market information (e.g., through HRDC's Labour Market Observatory). Other important labour market interventions include immigration policy and minimum wage policy. Immigration policy affects the ability of investors to enter the country and of firms to employ skilled foreign workers, and a liberal policy can enhance the international competitiveness of producers of tradeable goods and services. However, over the past decade immigration policy has been tightened and the number of work permits drastically reduced, and many firms have noted that this has had a negative impact on investment and growth, as well as on the creation of employment opportunities for citizens.

Minimum wage policy is aimed at providing some protection for workers in less skilled occupations and preventing employers from driving down wages to very low levels. The level of the minimum wage has important labour market implications, as it has an impact on the demand for labour

[2]BoB Annual Report, 2017. A regulatory sandbox allows firms to test innovations in financial products and services, in the market, in a controlled and usually time-limited environment, under the supervision of the financial sector regulator. It allows innovation where the existing regulatory framework may be unclear or unduly restrictive.

SPECIAL FEATURE

and the level of employment; setting it too high may lead to lower formal employment growth. However, it also has important social and distributional implications, as the beneficiaries of higher minimum wages are likely to be lower paid workers; in a society with high income inequality, this may be an important outcome. Hence, there are important trade-offs in setting an appropriate level of the minimum wage. In recent years, the minimum wage has risen in real terms, but this marked a reversal of a longer-term trend of declining real minimum wages[3].

The overall impact of labour market policies has not been as intended. Although the overall unemployment rate has not changed much – the 17.6 percent unemployment rate recorded in the 2015/16 BMTHS was similar to the 17.8 percent recorded in the previous household survey in 2009/10 – it does seem that a smaller share of the employed population is working in the formal sector – i.e., informal employment has grown faster than formal employment.

Competition and Market Regulation

A small economy such as that of Botswana is always vulnerable to monopolies, given that in many modern industries firms have to be large in order to achieve economies of scale. For instance, if there are too many banks, the result will be inefficiency as the banks are too small and the consumer is burdened by excessive costs. However, small numbers of firms in an industry need not be anti-competitive – the key issue is whether a market is "contestable". The global motor industry, for instance, is dominated by a small number of large firms, but the industry is contestable as all of those large firms are challenged by others, and no firm's position is secure. Similarly, in Botswana there is aggressive competition between the banks, even though the market is dominated by a few players.

There is, however, always a risk of collusion or market domination that acts against the interests of consumers and reduces the beneficial impact of competition – especially by blunting the incentive for innovation. Hence the role of market regulators is important – primarily the Competition Authority, but also industry-specific regulators such as the Bank of Botswana (BoB), Non-Bank Financial Institutions Regulatory Authority (NBFIRA), and the Botswana Communications and Regulatory Authority (BOCRA). Their role is not just about preventing monopoly pricing or the accumulation of undue market power through mergers and takeovers. It is also about setting rules that make markets more competitive. A particularly relevant area is making it easier for consumers to switch service providers. This is easy in the case of supermarkets, but not so easy in the case of banks or cellphone providers. In the latter case, requiring number portability – so that subscribers can change service provider while keep the same cellphone number – would be a big step forward; something that BOCRA can require of licensed telecommunications operators. Similarly, BoB could introduce regulations to make it easier to switch banks, as some other bank regulators have done.

The need for competition in a small economy is also a good reason to avoid protectionism, as imports provide a crucial source of competition, keep prices down, and benefit consumers. In Botswana, the impact of protectionism can be seen in the poultry sector, where imports are heavily restricted, the domestic industry is dominated a small number of firms, and prices are higher than in South Africa, at the expense of consumers.

Price Controls and Subsidies

Price controls and subsidies can be powerful tools to influence market prices and outcomes. However, they have to be used extremely cautiously, as they can equally create distortions and groups with interests in maintaining price controls and subsidies, even when they may not be economically beneficial; as a result, they can be extremely difficult to remove.

Price Controls

Botswana has not traditionally made extensive use of price controls, preferring to allow markets forces to operate. However, price controls are used in some important areas, including fuel (petrol, diesel), electricity and water. All three sets of prices are ultimately determined at Cabinet level, and hence have become politicised. The result is that they have been set at sub-economic levels in recent years, leading to losses at the producer level, which have to be made up through subsidies. There are also risks that economic decisions become distorted, for instance encouraging the over-use of scarce water supplies and discouraging water conservation and recycling efforts, and discouraging investment in renewable energy supplies.

Price controls can also prevent competition. For instance, the fixed retail fuel price means there is no price competition between suppliers, unlike in deregulated markets where fuel price competition is extensive. In Botswana, a simple change would maintain the objective of protecting consumers from exploitation where there is little competition (e.g. in rural areas) while encouraging competition. This would be to make the regulated price a maximum price, not a fixed price, which would allow fuel retailers to offer discounted prices as a competitive strategy, yielding benefits for consumers.

[3]Between 2011 and 2017, the minimum wage in retail rose by 23% in real terms, but between 1990 and 2017 it fell by 24%.

SPECIAL FEATURE

Subsidies

A variety of explicit or implicit subsidy programmes are in place in Botswana. Many of these take place through parastatals, and are the counterpart of the price controls mentioned above. The Botswana Power Corporation (BPC), for instance, has received extensive subsidies over the years (subsidies to BPC are the second largest item in the original NDP 11 development expenditure programme). Other parastatals receive subsidies, but this may reflect inefficient operations rather than sub-economic pricing – examples include the BMC and Air Botswana. Other subsidies are deliberate and aimed at achieving specific objectives, such as the subventions to CEDA that enable it to charge low interest rates on its loans, take on a higher level of risk, absorb the cost of loan defaults, and maintain an extensive outreach programme. Amongst the commercial and developmental parastatals, the largest subsidies over the period 2013/14 to 2017/18 are the following:

Table 1: Largest direct public enterprise subventions from Government, 2013/14 – 2017/18, P mn

Public Enterprise [1]	Total Subventions, P million
Botswana Power Corporation (BPC)	9,260
Citizen Entrepreneurial Development Agency (CEDA)	1,568
Botswana Agricultural Marketing Board (BAMB)	1,440
Local Enterprise Authority (LEA)	736
Botswana Meat Commission (BMC) [2]	693
Water Utilities Corporation (WUC) [2]	613

Source: Annual Reports; Estimates of Expenditure

Note: [1] Excludes Air Botswana, BCL Ltd and Botswana Railways, where information is not available. Smaller subventions were received by many other parastatals. The table includes direct budgetary subventions only, and does not include the value of equity injections, debt-to-equity conversions and debt guarantees, all of which represent additional subsidies. [2] Subsidies over the 5 years to 2015/16 – more recent accounts not available.

Some of these subsidies may be justified and delivering useful socio-economic outcomes. However, it is important to subject such subsidies to proper evaluation and assessment of their impact, in order to ensure that the scarce public financial resources that are being used achieve the desired objectives in a way that represents the best value for money. For instance, the cost to government of employment creation in LEA-supported enterprises appears to be in the region of P200,000 per job. It would be important to compare this with the cost of other interventions to support employment creation.

The need for cost-effectiveness evaluation applies both to subsidies for parastatals and direct subsidies to producers, such as the Integrated Support Programme for Arable Agriculture Development (ISPAAD) and the Livestock Management and Infrastructure Development (LIMID) programme; these receive subsidies of around P550m and P100m a year, respectively. The agricultural sector is probably the largest recipient of subsidies in Botswana (including those paid through BAMB and the Agricultural Credit Guarantee Scheme), but has not achieved sustained growth or significantly improved incomes for those engaged in agriculture. This suggests that a thorough evaluation of the effectiveness of agricultural subsidy schemes is called for. Indeed, the cost of ISPAAD subsidies appears to be greater than value added in crop production, which suggests that the subsidy is encouraging Batswana to undertake activities that destroy, rather than create, economic value.

Not all subsidies appear directly as a charge on the budget. The Economic Diversification Drive (EDD) provides price incentives for accredited local firms in the provision of goods and services to government and parastatals; hence leading to higher expenditure by government than would otherwise be achieved. The value of EDD price preferences is integrated into procurement budgets and has not been separately costed. A cost-benefit evaluation of the impact of the EDD would show what has been achieved through such expenditure. Similarly with projects implemented through the Economic Stimulus Programme (ESP), where normal public procurement rules that emphasised cost-minimisation were relaxed. EDD subsidies may also have provided firms with an incentive to concentrate on public procurement rather than exports.

In some cases, subsidies are combined with regulatory privileges that protected public enterprises from competition, such as with BMC and its beef export monopoly. This has introduced extreme distortions in the beef and cattle sector, which has contributed to the decline of beef exports and the gradual depletion of the national cattle herd as cattle rearing has become uneconomic. This has to be addressed through the removal of the beef export monopoly, and potentially the privatisation of BMC, to enable private sector investment in productive capacity and remove price distortions.

Trade Policy

Trade policy is included under microeconomic policy as it affects prices, competition and market access across different goods and services. Botswana's trade policy is influenced by participation in several regional and international trade agreements, including the SACU, the Southern

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African Development Community (SADC) Free Trade Area (FTA), the SADC-EAC-COMESA Tripartite FTA, the African Continental Free Trade Area (AfCFTA), and the SADC-EU Economic Partnership Agreement (EPA). In addition, Botswana imposes some of its own policies outside of these agreements, such as infant industry protection, along with other import levies, and import restrictions. Protectionist trade policy offers apparent short-term benefits, but is largely inconsistent with an export-led growth strategy, as it raises costs and prices and does not provide incentives for firms to become more competitive, and should therefore be used very cautiously. Protectionism is also inconsistent with the principles of the various trade agreements that Botswana has signed, most recently the AfCFTA, which are all premised on reducing trade barriers and increasing trade integration.

Also included under trade policy are broader issues of trade facilitation, including non-tariff barriers (NTBs), regulatory issues, border infrastructure, etc. These are usually issues that have to be negotiated bilaterally with neighbouring states. A focus on export-led growth requires that these issues are addressed, so that costs are not increased by a "thickening" of borders due to delays and bureaucracy. This includes issues such as 24-hour opening of key border crossings, one-stop border posts, electronic customs documentation, mutual recognition of standards, etc.

Overall Impact

The impact of micro-economic policies can be related to macro-economic outcomes, under which the overall rate of economic growth has been reasonable. However, growth has not been labour-intensive, nor has it been export-led. This suggests that micro-economic policies and interventions have had a bias against exports and have not supported labour-intensive economic activities. The pattern of growth in Botswana – led by services and non-tradeables as mining growth has slowed – shows that the impact of Dutch Disease has not been avoided. Future micro-economic interventions should therefore be focused on countering Dutch Disease effects, and shifting the incentives for investment and employment away from non-tradeables and the domestic market and towards exports.

This, in turn, means focusing on competitiveness and efficiency: government, and businesses providing non-tradeables (mostly domestic services), do not have to be internationally competitive, but businesses producing tradeables (exports and import substitutes) do. Policies, interventions and regulations that raise domestic costs and undermine competitiveness should be avoided at all costs.

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