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ECONOMIC REVIEW

first quarter january - march 2017

in this issue ...

COMMENTARY

Mixed signals from economic data in early 2017

Economic data released in the first quarter of 2017, much of which relates to the final quarter of 2016, presents a mixed picture of the economy and no clear direction. On the economic growth front, preliminary GDP data for 2016 show real growth of 4.3% for the year as a whole, well ahead of most estimates (including ours). This mostly reflects the impact of improved trading conditions in the diamond sector. With production relatively stable through 2016, the impact of the previous year's reduction in diamond output has fallen away from the GDP calculation, hence, growth of diamond output moved out of negative territory. However, lower production of copper-nickel, due to poor market conditions and mine closures, led to negative growth in the mining sector as a whole in 2016.

Notwithstanding the absence of growth in diamond production, diamond sales (mostly exports) were significantly higher, reflecting sales from stockpiles accumulated earlier, and an increase in diamond re-exports through De Beers Global Sightholder Sales (DBGSS). This in turn affects other sectors of the economy, with diamond sorting and valuing included as part of the Finance and Business Services sector, and diamond trading included under the Trade sector. Growth in the latter rose to 13.5% in 2016, including a massive 75% real growth in the wholesale sub-sector, following increased diamond throughput and a revision of historical data. Overall, this caused the non-mining private sector to grow by a huge 7.2% in 2016, compared to only 1.4% in 2015.

However, the usefulness of this measure (non-mining private sector growth) as an indicator of what is happening in the economy outside of mining is gradually declining. Three of the non-mining economic sectors – Manufacturing, Trade and Finance & Business services – all now include activi-

ties related to the diamond industry – respectively, diamond cutting and polishing, diamond trading, and diamond sorting and valuing. Increasingly, changes in the output of these sectors are driven by swings in the global diamond industry. In a way this is positive – it reflects the success of a policy drive to move the diamond industry downstream from mining into other value-added activities. But it does mean that there is no easy way to ascertain output trends in the economy outside of diamond-related activity. It would be relatively straightforward for Statistics Botswana to carve out diamond-related sub-sectors from the Manufacturing, Trade and Finance & Business sectors (in the same way that diamond mining is separated from other mining activities), and we hope that this will be done soon in order to allow the calculation of output and growth trends in the non-diamond segment of the economy.

In the meantime, the picture is mixed across the various sectors of the economy, with close to zero growth in agriculture and manufacturing, but healthier growth (over 4%) in construction, retail trade, hotels & restaurants, transport & communications, and banking.

The upturn in the global diamond market has helped to turn around the country's foreign trade position, with a large increase in total exports and a move from balance of trade deficit in 2015 to a substantial surplus in 2016. It seems likely that the current account surplus was largely offset by capital outflows, however, as official foreign exchange reserves declined during 2016, although the complete picture will not become clear until full balance of payments data for the year are released. Capital outflows most likely reflect the relatively low interest rates in Botswana as compared to South Africa, as well better investment opportunities for the private sector outside of Botswana.

The financial sector also presents a mixed picture. Credit growth has slowed substantially, to the lowest annual rate in nearly 20 years, and arrears on lending have risen through 2016. Although the level of arrears on bank lending has doubled over the past four years, the rate remains relatively low (6.6% of loans in arrears of 30 days or more, and 4.2% over 90 days). Banks seem to be dealing with the problem, however, through risk management, cost control and by being cautious with new lending. As a result, return on equity after tax for the banking sector increased from 12.6% in 2015 to 15.3% in 2016, although even this higher figure is still low by historical standards for Botswana's banks. There are also some signs of liquidity tightening in the financial sector, with rising interest rates on BoBCs, reflecting very slow growth in the deposit base of the banking system.

Inflation is also edging up, and at 3.5% in March is at the highest rate for over two years. Although likely to increase further it should stay below the 4.5% mid-point of the BoB's inflation objective range for the foreseeable future. Nevertheless, these developments all suggest that we may have reached the low point of the interest rate cycle, with the next move more likely to be upwards than downwards.

One of the major events of the first quarter, as always, was the presentation of the Budget in early February. Much of the content had already been flagged, in the Budget Strategy Paper and in National Development Plan 11, approved by Parliament in December 2016. Nevertheless, the projected fiscal position for 2017/18 is now more favourable than had been indicated earlier, with a large increase in expected receipts from the Southern African Customs Union (SACU). Hence, the projected budget deficit for 2017/18 is now P2.4 billion (1.4% of GDP), compared to the earlier estimate of P6.8 billion (4.1% of GDP).

The budget also projects a modest 4.4% increase in overall spending. The additional spending is concentrated on recurrent spending (up 8.6%), notably wages and salaries (up 18.5%) and grants and subventions (up 12.6%). Across sectors, the main beneficiaries are spending on health, urban and regional infrastructure and roads, as well as general public administration and transfers to local authorities. As in the past, education receives the largest share of spending, followed by general public services.

Figure 1 – Change in Budget allocation, 2016/17 – 2017/18

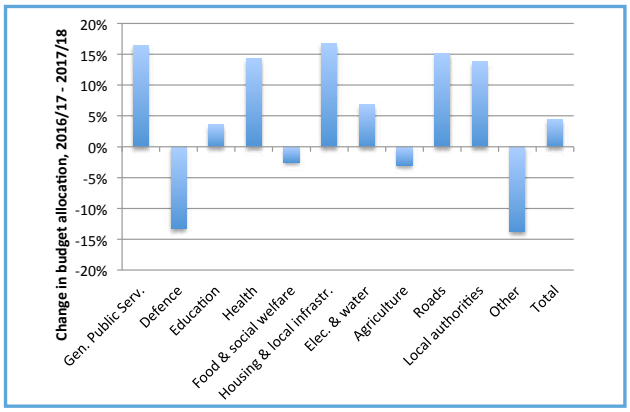
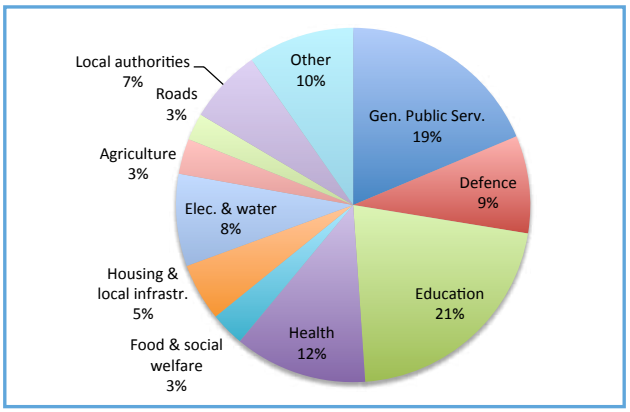
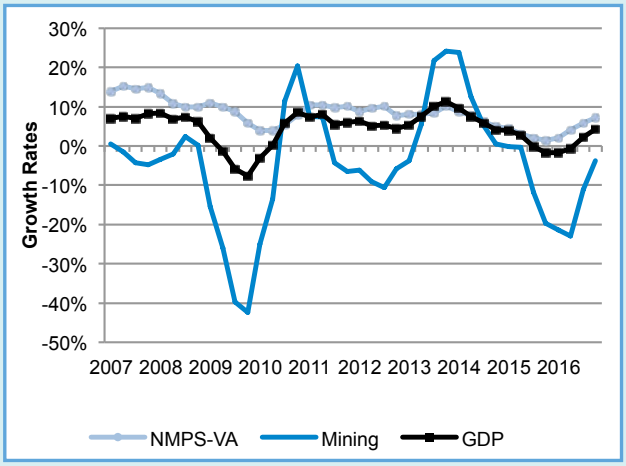


Figure 2 – Allocation of spending, 2017/18



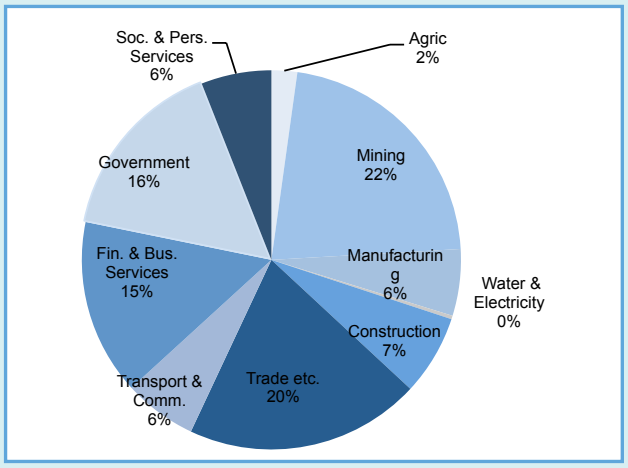
KEY ECONOMIC VARIABLES

Annual GDP Growth



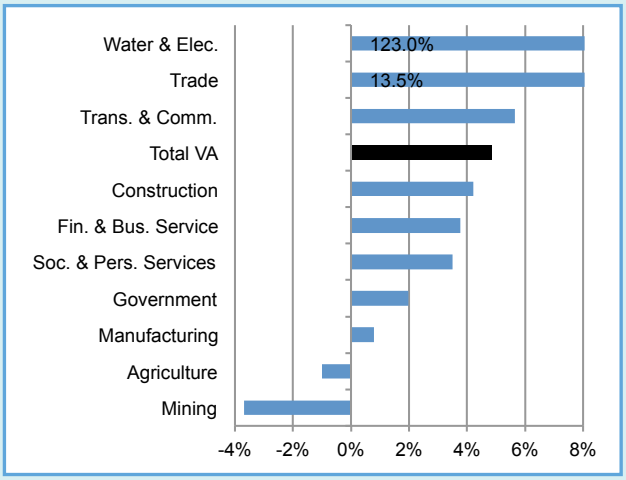
The rebound of the diamond market in 2016 from the weak demand that dominated 2015 contributed positively to overall economic growth. Year-on-year real GDP growth increased to 4.3%, significantly higher than expected and well above the negative 1.7% y-o-y growth recorded in 2015. Mining improved to minus 3.7% growth in 2016, up from minus 19.6% in 2015. The non-mining private sector (NMPS) grew strongly at 7.2% in 2016, up from 1.4% in 2015, although much of this was driven by the rise in diamond trading activities (included in wholesale trade). Statistics Botswana also made revisions to quarterly GDP estimates from updated data sources, affecting all 2016 estimates.

Sectoral GDP Shares



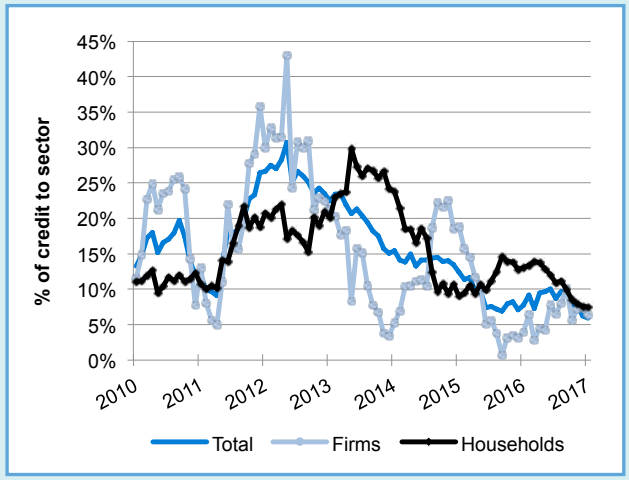
The structure of GDP in terms of economic sectors has not changed for the top four in comparison to 2015. Mining continues to dominate the economy, accounting for the largest share of GDP (22% at current prices) of any economic sector. Trade, which now includes other mining-related activities (De Beers Global Sight holder Sales and the Okavango Diamond Company), is the second largest sector, followed by Government and Finance & Business Services. Although the direct share of mining has been declining over the years, it now appears indirectly in other sectors, notably Manufacturing, Trade and Business Services, due to downstream activities.

Sectoral GDP Growth



Overall economic performance in 2016 was fair, with some sectors recording marginal declines while others improved, such as the Water & Electricity, Mining and Trade sectors. Water & Electricity grew 123% y-o-y in 2016 up from 7% in 2015, while Mining improved from minus 19.6% to minus 3.7% growth in 2016. Trade (the most affected sector from GDP estimate revisions) grew by 13.5% y-o-y in 2016 from the negative 3.9% (revised) in 2015 respectively. This robust growth largely reflects a 74% increase in real output in the Wholesale sub-sector, due to improved diamond aggregation and trading conditions.

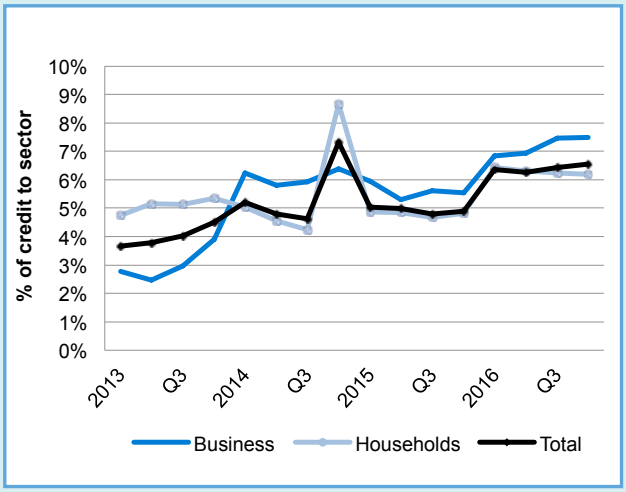
Annual Credit Growth



Bank credit recorded the lowest annual growth rate since 1997, decreasing from 7.8% in October 2016 to 5.9% in January 2017. The slowdown in credit growth is attributable to slower growth in lending to households, from 8.5% to 7.5% in October 2016 and January 2017 respectively. Amongst the components of household credit, growth in unsecured loans fell from 9.7% to 9.2% and in mortgages from 6.7% to 5%. On the other hand, annual growth in bank credit to firms increased from 5.6% to 6.5% in October and January respectively.

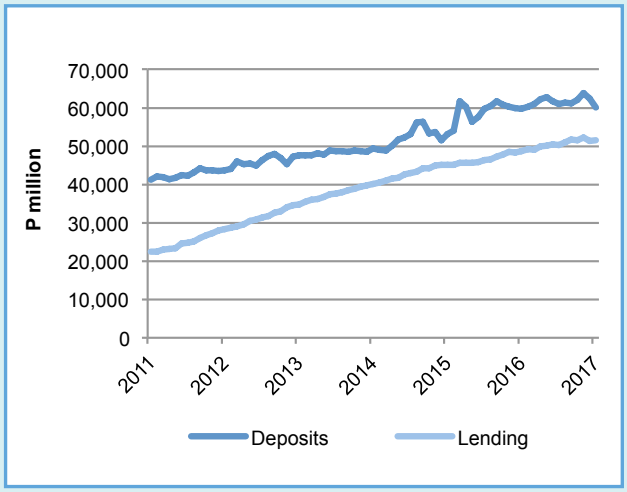
KEY ECONOMIC VARIABLES

Arrears on Bank Lending



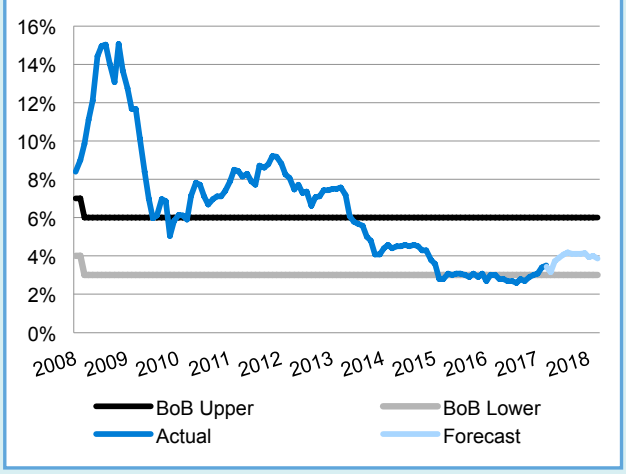
Total arrears as a proportion of outstanding bank credit increased further in the last quarter of 2016. Arrears increased from 6.4% in Q3 to 6.6% at the end of 2016, and compares to 4.9% in 2015. The increase in 2016 was driven by both households and businesses; arrears on lending to households increased to 6.2% in 2016 from 4.7% in 2015 and on lending to businesses increased to 7.5% in 2016 from 4.7% in 2015. There was also an increase in arrears on lending to government and parastatals, presumably reflecting the collapse of BCL. Nevertheless, according to the BoB MPC, default rates are relatively low and stable, and pose low risks to financial stability.

Bank deposits and lending



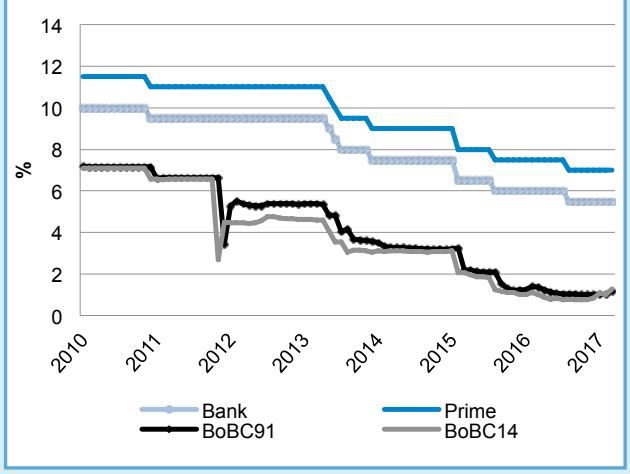
There have been some concerns about banking system liquidity in recent months, with overnight money market liquidity dropping to very low levels on some days. Nevertheless, there is no immediate liquidity problem – the banks still have excess liquid assets equivalent to around 5% of total assets, compared to less than 1% at the time of the liquidity crisis in late 2014. However, there is a potential medium-term problem in that the deposit base of the banking system is not growing – deposits have fluctuated around the P60 billion level for the past two years. With credit growing, albeit slowly, this will eventually lead to a liquidity squeeze unless deposits start to grow again.

Inflation and Forecast



Headline inflation increased to 3.5% in the first quarter of the year, after spending most of 2016 below the Bank of Botswana's lower limit of 3%. The increase in inflation largely reflects the effect of adjustments to administered fuel prices in March 2017, as well as higher food prices. Given trends in international fuel prices, the increase in inflation was largely expected. While inflation is forecast to around 4% by mid-year, it is expected to remain within the lower half of the Bank of Botswana's medium-term objective range of 3-6% throughout 2017.

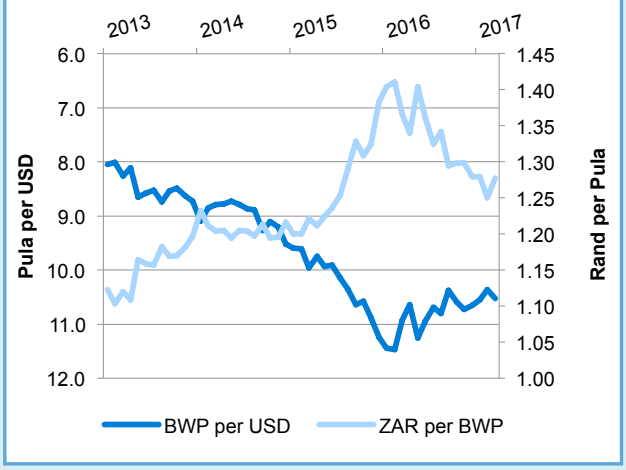
Interest Rates



The Bank of Botswana's Monetary Policy Committee (MPC) maintained the Bank Rate at 5.5% in its first meeting of 2017, continuing the era of low interest rates. The commercial bank Prime Lending Rate was also unchanged at 7.0%. However, money market rates increased, with the 14 day BoBC rate rising from 0.84% Q4 2016 to 1.26% in Q1 2017 and the 91 day BoBC rate rising from 1.01% to 1.18% over the same period. This may reflect a tightening of liquidity in the banking system.

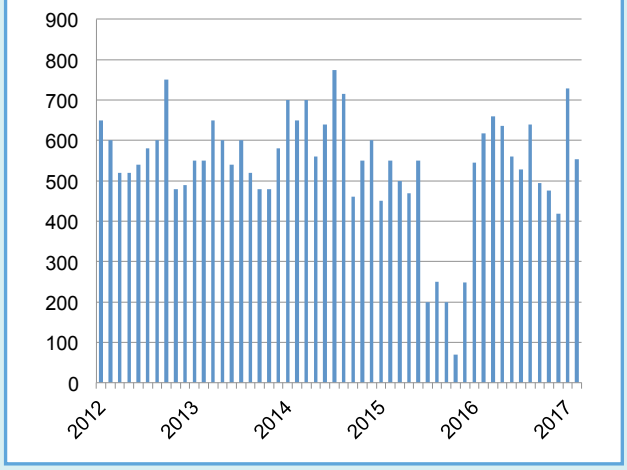
KEY ECONOMIC VARIABLES

Exchange Rates



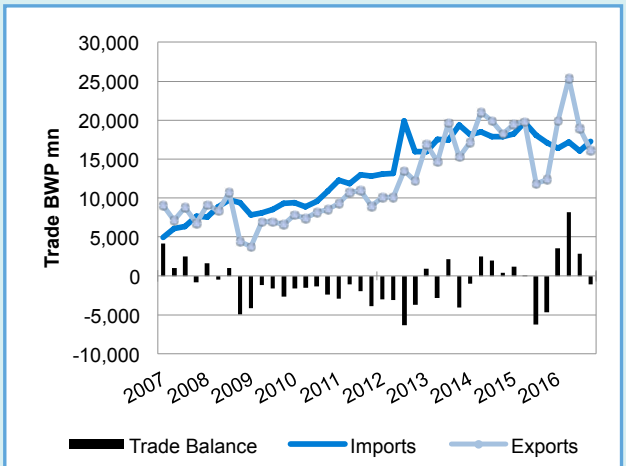
Foreign exchange rates were fairly stable for most of Q1 2017. However, exchange rates were shaken-up at the end of the quarter as a result of political events in South Africa, which caused the SA rand to weaken sharply against the US dollar, after a long period of appreciation. The Pula-US Dollar exchange rate was 10.53 at the end of March 2017 from 10.65 in December 2016. The Pula depreciated marginally against the Rand, by 0.4%, ending the quarter at ZAR1.278. The Pula exchange rate policy was reviewed in January 2017, and the rate of crawl against the basket adjusted to 0.26%, from 0.38%in 2016. Currency weights in the Pula basket weight were changed to 45% for the Rand and 55% for the Special Drawing Right (SDR) (from 50% each).

De Beers Diamond Sales



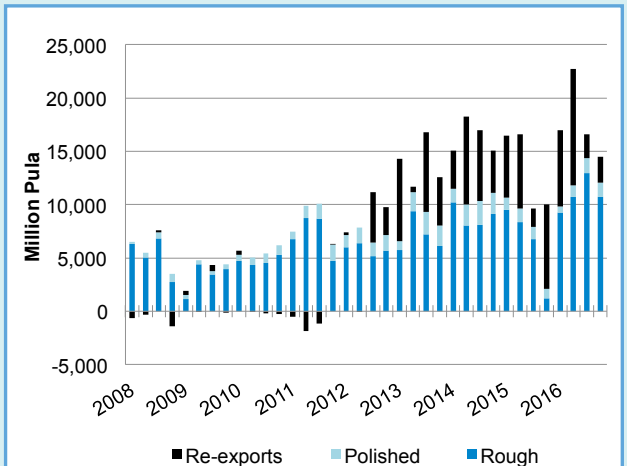
De Beers Global Sightholder Sales (DBGSS) recorded sales valued at USD1,282 million in Q1 2017, almost 9% higher than in Q1 2016. This reflected strong demand for rough diamonds, and an upturn in activities in the downstream market. Prices for rough diamonds were stable at sightholder and auction sales. Historically, De Beers has held ten sightholder sales each year; however, due to its commitments with state-owned diamond companies in Botswana and Namibia, the company may reduce the number of sightholder cycles.

International Trade



Total trade slowed in the last quarter of 2016. Total exports fell to P16.1 billion in Q4, from P18.9 billion in the previous quarter, while total imports increased to P17.2 billion from P16.0 billion in Q3. Export performance was adversely affected by the closure of the BCL mine and the suspension of copper-nickel exports, which had previously contributed around P1 billion to exports each quarter. The trade balance in Q4 2016 was a deficit of P1,099 million, compared to a surplus of P2,883 million in Q3. Nevertheless, overall trade performance during the year was much improved, with a surplus of P13,478 million in 2016, compared to a deficit of P9,706 million in 2015.

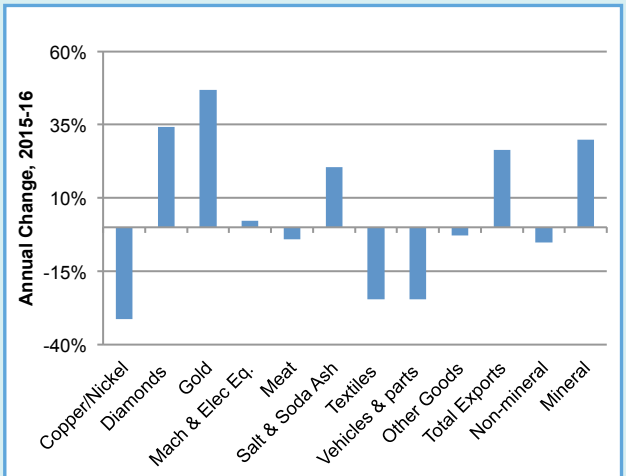
Diamond Exports



Global demand for rough diamonds improved significantly in 2016, a turnaround from the depressed demand that characterised 2015. Overall diamond exports from Botswana rose by 34% y-o-y in 2016, compared to a decline of 19% y-o-y in 2015. Across all diamond export categories, rough exports and re-exports increased by 69% and 1.1% respectively, while polished exports declined by 1.1% in 2016.

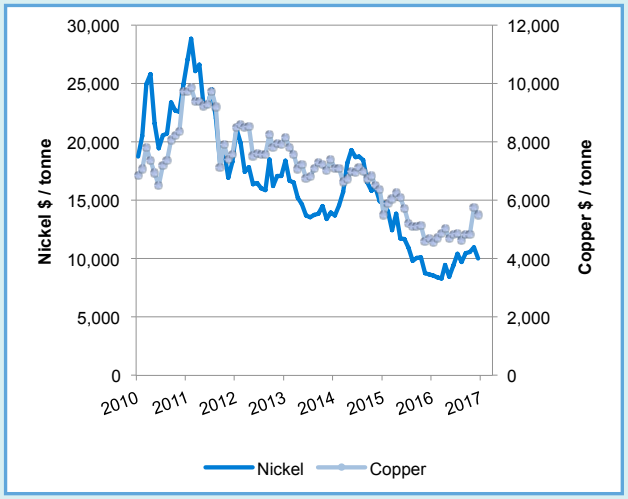
KEY ECONOMIC VARIABLES

Export Growth



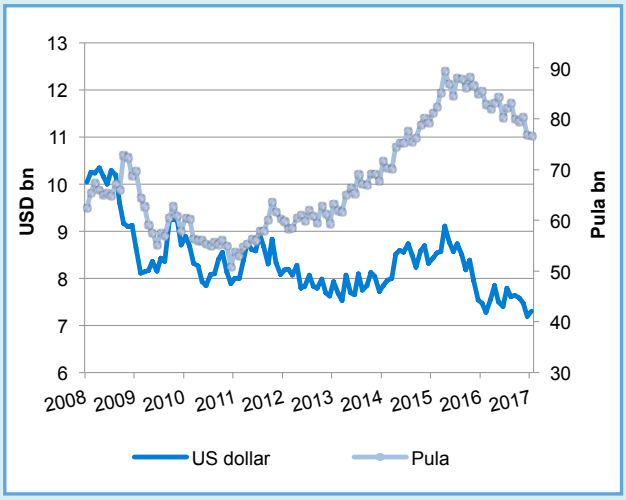
Export performance varied considerably across different categories of exports in 2016. As noted above, diamonds did well while copper-nickel did badly. Amongst other mineral exports, both gold and salt/soda ash showed strong growth in export values in 2016. Exports of manufactures, however, generally performed badly, with significant declines in exports of textiles and vehicle parts. Data for services exports are not yet available.

Copper & Nickel Prices



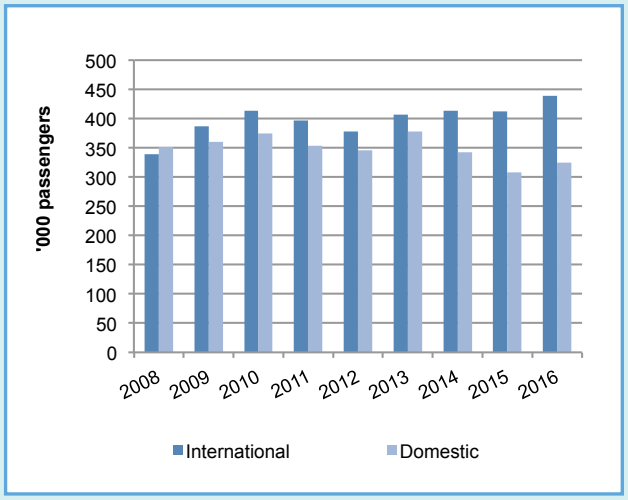
The international market for base metals - copper and nickel – has shown some improvement from the commodity slump in 2016, when prices reached historically low levels. Copper prices increased by 6.3% in Q1 2017 to USD5,848 per tonne, from USD5,500 in Q4 2016. However, nickel prices fell from USD10,007 in Q4 2016 to USD9,872 in Q1 2017, a 1.3% decline.

Foreign Exchange Reserves



Foreign exchange reserves declined by 9.5% in 2016 to P76.8 billion, down from P84.9 billion in December 2015. The decrease in reserves is attributable to drawing down on government savings as well as the appreciation of the Pula. Foreign reserves decreased in both the US Dollar and SDR terms, by 5% and 2% respectively.

Air Passenger Traffic



Air travel data show that the number of passenger movements in Botswana airports has increased for both domestic and international air travel. Domestic air passenger air traffic increased by 5.4% and international traffic by 6.4% in 2016. This resulted in total air passenger traffic increasing by 6% in 2016, compared to minus 4.6% in 2015. This is a positive reflection of growth in tourism.

NEWS HIGHLIGHTS

5th January	Revision of Pula basket weights. (Bank of Botswana)	In order to keep up with monetary policy developments in major trading countries as well as maintaining a stable and competitive real effective exchange rate (REER) of the Pula, the Government has revised the Pula basket weights to 45% South African Rand and 55% Special Drawings Rights (SDR). The rate of crawl has been changed from an upward crawl of 0.38% per annum to 0.26% per annum. The changes in the REER are in effect from 1 January 2017.
17th January	Alecto raises £1 million to restart Mowana mine. (Mining Weekly)	Alecto Minerals has raised £1 million through the issue of convertible loan notes to restart operations at its newly acquired Mowana copper mine in Northern Botswana. In December 2016, Alecto Minerals expressed its interest in acquiring a 60% shareholding in Cradle Arc Investments which wholly owns Mowana mine. According to Alecto Minerals, the funds will be extended to Cradle to resume operations at Mowana as well as forming part of transaction expenses related to the acquisition. Operations at Mowana mine are expected to resume in the first quarter of 2017.
18th January	BCL 'fatally insolvent,' liquidator reports. (Mmegi)	According to the provisional liquidator of BCL Ltd, the mine's operations are "fatally insolvent",making the reopening of the mine unrealistic and leaving options of selling the mine as a whole in or separate components. The liquidator has since applied for final liquidation of BCL. The BCL Group, which comprise of BCL mine, BCL Investments and Tati Nickel mine,was placed under provisional liquidation in September 2016, resulting in more than 5,000 jobs being lost.
24th January	Lucara appoints new mining contractor. (Market Wired)	Lucara Diamond Corp. announced the appointment of a new contractor, Moolman Mining Botswana (Pty) Ltd, at its Karowe diamond mine. The contractorwill provide full suite mining services including drilling, blasting, loading and haul functions for ore and waste. The contract will last for a period of six years.
27th January	Government raises P4 billion on bond market. (Mmegi)	Government raised P4 billion from the bond market in 2016, through Treasury Bills and re-opening existing bond issues, to help fund the projected P6 billion budget deficit. According to the Botswana Stock Exchange (BSE), the Bank of Botswana - which acts on behalf of the Government - held four auctions in 2016, in which P2 billion was raised from Treasury Bills and P2 billion from bond issues. Government revenues are projected at P48.4 billion for the 2016/17 financial year, and net expenditure at P54.4 billion.
30th January	Botswana's Okavango diamond sales jump 80% in 2016. (Reuters news)	Okavango Diamond Company's (ODC) sales jumped 80% to USD547 million in 2016 as global consumer demand for diamonds rebounded. Overall diamond volume also increased, by 115% to 3.44 million carats. ODC, which had ten tenders in 2016, receives an allocation of 15% of diamonds mined by Debswana.
5th February	Shumba Energy signs milestone agreement. (Sunday Standard)	Shumba Energy has signed an agreement to acquire 75% of the Morupule South project from Hodges resources. Morupule South is located south of the Morupule Colliery and has an estimated resource of 2.45 billion tonnes of JORC-compliant resource, including 1.2 billion tons of high-grade open cast mineable coal. According to the company, the acquisition is a window to tap into both the domestic and regional markets, given nearby rail access.

NEWS HIGHLIGHTS

8th February	Government is finalising its renewable energy strategy. (Mmegi)	The Minister of Finance and Economic Development has stated, during the 2017/18 Budget Speech, that the Government was finalising its Renewable Energy Strategy, aimed at attracting investment into renewable energy. Solar energy has been identified as a potential alternative source of electricity supply in Botswana. Moreover, the Government is collaborating with a German company to undertake a Green Energy feasibility study to identify other alternative sources of electricity.
8th February	Matambo tightens control on resource usage. (Mmegi)	During the 2017/18 Budget Speech, the Finance Minister announced the Government's intent to introduce measures that will reduce resource wastage at the same time broadening revenue resources. The Government plans to tighten controls in procurement by only awarding tenders or contracts where there is proof of availability of funds. Re-allocations of funds to cover over-expenditure will require Finance Ministry approval. The government intends to broaden its revenue base by adjusting various taxes and introducing Transfer Pricing rules in the Income Tax Act. In the 2017/18 financial year, total revenues and grants are estimated at P57.19 billion while total expenditure and net lending is estimated at P59.54 billion. This results in a forecast budget deficit of P2.35 billion or 1.43% of GDP.
14th February	Fresh bid to privatise Air Botswana. (Mmegi)	The Ministry of Transport and Communication has invited companies capable of providing efficient air transport services to submit Expressions of Interest to operate Air Botswana. So far, 17 companies have submitted responses.
14th February	Botswana chamber adopts Canada's sustainable mining programme. (Mining Weekly)	The Botswana Chamber of Mines (BCM) announced that it will adopt the Towards Sustainable Mining (TSM) initiative, a corporate social responsibility programme developed by the Mining Association of Canada (MAC) to improve environmental and social practices in the mining industry. BCM will be the first mining association in Africa to adopt the TSM, and the third outside Canada.
15th February	Water and electricity tariffs to go up. (Mmegi)	The Government has agreed that Water Utilities Corporation (WUC) and Botswana Power Corporation (BPC) can raise water and power tariffs from 1 April 2017. Water tariffs will be increased by 25% for Government and 15% for domestic and business use, while BPC will apply a 12% increase in electricity tariffs.
16th February	Tsodilo starts drilling programme at BK16 in Botswana (Mining Weekly)	Tsodilo Resources has started a drilling programme at its BK16 kimberlite project in the Orapa kimberlite field (OKF). The programme entails drilling pilot holes and is estimated to take seven weeks to complete. The diamondiferous 6 ha BK16 kimberlite pipe is known to contain rare and valuable Type IIa diamonds.
16th February	Lucara full year results. (Market Wired)	Lucara Diamond Corp. announced its financial results for the year ended 31 December 2016. Sales improved in 2016 compared to 2015; the miner recorded revenues of USD295.5 million in 2016, from USD223.8 million 2015. Earnings before interest, tax, depreciation and amortization (EBITDA) and operating margin during the period also increased, mainly due to the sale of a 813 carat Type IIa diamond for a record world rough price of USD63.1 million. Lucara will maintain a cautious outlook in 2017, and keep production between 290,000 and 310,000 carats at its key Karowe Mine.

NEWS HIGHLIGHTS

17th February	Over 250 job cuts as Ghaghoo mine closes. (Mmegi)	Gem Diamonds Botswana has put its the Ghaghoo Mine under care and maintenance, resulting in more than 250 jobs being lost. According to the company, depressed diamond prices for small stones contributed to unprofitable production at Ghaghoo, hence, the decision to place the mine under care and maintenance. Production at Ghaghoo was 55% lower at 40,976 carats in 2016 down from 91,499 carats in 2015.
20th February	Competition Authority blocks Universal House acquisition of Mmegi. (The Patriot)	The Competition Authority has rejected the acquisition of 28.73% shares in Mmegi Investment Holdings (Pty) Ltd by Universal House (Pty) Ltd on the basis that the transaction is likely to alter the market for the provision of commercial radio broadcasting services, thus, raising competition and public interest concerns.
21st February	De Beers profit jumps as diamond market stabilizes. (Rapaport news)	De Beers profit more than doubled in 2016 as trading conditions in the diamond manufacturing sector improved and inventory levels stabilized. Underlying earnings increased to USD667 million in 2016 from USD258 million in 2015, attributable to 30% year on year revenue growth in 2016. Sales increased by more than half in 2016, the bulk of it coming from mine inventories. Rough diamond production fell by 5% to 27.3 million carats from 28.7 million carats in 2015.
27th February	Cupric Canyon gets USD30 million to develop Botswana mine. (Mining.com)	Cupric Canyon Capital has secured a loan facility from Red Kite Mine Finance to begin production at Khoemacau Copper Mining (KCM) in the Ghanzi copper belt. Khoemacau mine is expected to produce 50,000 tonnes of copper and 1.4 million ounces of silver annually over the 25 years of the mine's lifespan. It is scheduled that full-scale construction on site will begin during the second half of 2017. Cupric Canyon is optimistic about the future and expects that expansion will increase copper production to 120,000 tonnes in 2019.
28th February	Alecto Minerals to shortly recommence mining activity at Mowana. (Mining Review)	Alecto Minerals has appointed a mining contractor to restart mining operations at the Mowana copper mine. The new contractor, Giant Transport Holdings, will undertake operations to clean the pit and begin reverse circulation grade control drilling. According to Alecto, the measured and indicated resource at Mowana is estimated at 683,000 tonnes of copper, with an inferred resource of 945,000 tonnes.
3rd March	BoB allays fears of looming liquidity crunch. (Mmegi)	The Bank of Botswana (BoB) has moved to dispel fears of a looming liquidity crunch, noting that the tight position in the market was a seasonal phenomenon resulting from heavy cash outflows set against lower inflows. Liquidity reduced towards the end of 2016 going into January 2017, and it is attributable in part to repatriation of profits by companies.
5th March	World Bank approves USD145.5 million to improve water availability in Botswana. (Sunday Standard)	The World Bank has approved a loan amount of USD145.5 million to Botswana for the emergency water security and efficiency project. It is envisioned that the funds would help improve the water situation in the country, which has been worsened by prolonged drought and infrastructural faults in the North South Carrier (NSC) which connects water supply from the northern dams to the southern part of Botswana.
8th March	National Lottery licence in the offing. (Mmegi)	The Gambling Authority is in the process of selecting a private operator to be licensed for Botswana's first National Lottery for a period of ten years. The successful bidder will be announced later this year and it is expected that the lottery will commence in 2018.

NEWS HIGHLIGHTS

13th March	Banks reports higher earnings. (WeekendPost)	At least two local commercial banks have reported an achievement of higher than expected earnings in 2016. Barclays Bank Botswana recorded an increase of 49% in Profit Before Tax (PBT), from P332 million in 2015 to P494 million for the year ended 31 December 2016. Another bank, Standard Chartered Bank Botswana, recorded a 50.7% increase PBT in 2016 to P104 million, up from P69 million recorded in 2015. Growth for both banks was driven by sustained revenue from the retail and banking segment. Expectations are high for the remaining banks.
14th March	Botswana's Choppies to spend P570 million on new stores. (Reuters news)	Choppies plans to continue with its expansion strategy to open new stores across Africa. The retailer plans to spend P570 million in its acquisition drive in the next 15 months. In its half year results for the period ending 31 December 2016, PBT narrowed to P72.3 million compared to P133.5 million recorded the same period last year. Choppies has been actively engaged in an expansion strategy and it operates in six countries at present.
17th March	IMF calls on Botswana to tighten banking laws. (Mmegi)	The International Monetary Fund (IMF) has advised Botswana to review its banking laws as it appears that the central bank does not have some of the legal powers required for implementing corrective action on banks that are in breach of prudential requirements or are conducting business in an unsound or unsafe manner. According to the report compiled by an IMF team that visited Botswana last year at the request of the Bank of Botswana (BoB), the current legislative framework guiding bank resolution and financial sector crisis management is weak and no longer provides an adequate framework for the conduct of the BoB's responsibilities.
27th March	Tlou raises AUD5.2 million for CBM projects. (Mining Weekly)	Tlou Energy has raised AUD5.2 million required for its coal bed methane (CBM) projects in Southern Africa through share placement to investors on stock markets in Australia and the UK. Tlou Energy plans to supply its first gas-fired power from its Lesedi CBM project in Botswana.
29th March	Botswana grants Sese mining lease. (Mining Weekly)	The Botswana government has awarded African Energy and First Quantum Minerals a mining licence for the Sese joint venture (JV) coal project. The JV plans to develop the Sese integrated coal and power project comprising of the 300 MW power station and a 1.5 million tonne per year captive coal mine. The mining license covers an area of 51.47 km2 and 650 million tonnes of measured and indicated resource.

MACRO-ECONOMIC DATA

Key Economic Data	unit	2012	2013	2014	2015	2016Q1	2016Q2	2016Q3	2016Q4	2017Q1
Annual Economic Growth										
GDP	%	4.5	*11.3*	*4.1*	-1.7	*-1.8*	*0.7*	*2.3*	4.3	..
Mining	%	-5.8	*24.2*	*0.5*	-19.6	*-21.3*	*-22.9*	-11.1	-3.7	..
Non-mining private sector	%	7.7	*10.1*	*4.9*	*1.4*	*2.0*	*4.1*	5.9	7.2	..
GDP current prices	P mn	109,870	125,158	145,868	*145,924*	*39,499*	*42,441*	*44,091*	43,657	..
GDP 2006 prices	P mn	75,515	84,081	87,569	86,081	*22,277*	*22,667*	*22,410*	22,422	..
Money & Prices										
Inflation	%	7.4	4.1	3.8	3.1	3.0	2.7	2.8	3.0	3.5
Prime lending rate	%	11.0	9.0	9.0	7.5	7.5	7.5	7.0	7.0	7.0
BoBC 14-day	%	4.6	3.1	3.1	0.97	1.0	0.84	0.76	0.84	1.26
Trade & Balance of Payments										
Exports - total goods	P mn	45,915	66,404	*76,261*	*63,484*	19,885	25,380	18,896	16,137	..
Exports - diamonds	P mn	36,143	55,367	65,328	52,730	17,003	22,741	16,581	14,456	..
Imports - total goods	P mn	62,114	70,218	*72,426*	*73,190*	16,380	17,192	16,013	17,236	..
Balance of visible trade	P mn	-16,199	-3,814	*3,835*	*-9,706*	3,506	8,188	2,883	-1,099	..
Balance of payments	P mn	-862	1,340	11,404	- 57	- 261	2,432	1,545	..	..
Foreign Exchange										
Exchange rate BWP per USD	end	7.776	8.718	9.515	11.236	10.929	10.941	10.373	10.650	10.526
Exchange rate ZAR per BWP	end	1.090	1.196	1.217	1.383	1.366	1.361	1.295	1.279	1.278
FX reserves	$ mn	7,628	7,726	8,323	7,546	7,559	7,402	7,631	7,189	..
FX reserves	P mn	59,317	67,772	79,111	84,881	81,891	80,283	79,990	76,653	..
Financial Sector										
Deposits in banks	P mn	47,216	48,512	51,492	59,961	61,078	61,700	61,198	62,438	..
Bank credit	P mn	34,555	39,763	45,116	48,307	49,040	50,476	51,703	51,316	..
BSE index		7,510.2	9,053.4	9,501.6	10,602.3	10,202.6	10,081.3	9,797	9,728	9,225
Business Indicators										
Diamond production *(a)*	'000 cts	20,619	23,134	24,658	20,732	5,429	5,305	4,601	5,557	..
Copper production (c)	tonnes	57,916	49,448	46,721	23,050	5,777	4,464	2,879	..	..
Nickel production	tonnes	17,942	22,848	14,958	16,789	7,303	5,801	3,774	..	..
Business confidence index		47%	45%	52%	44%	36%	..	43%	..	..
No. of companies formed		16,561	14,190	16,300	19,134	4,592	..	..	..	..
Electricity consumption	GWh	3,703	3,502	3,990	3,974	967	955	995	1,012	..
Crude oil (Brent)	$/bar	110.80	109.95	55.27	36.61	36.75	48.05	48.24	54.39	55.39
Employment (formal)										
Government		131,033	130,175	129,918	130,220	126,737	127,537	128,279	..	..
Parastatals		17,484	18,838	18,790	19,411	19,999	19,476	19,101	..	..
Private sector		188,531	189,894	191,399	191,484	193,460	195,747	197,107	..	..
Total		337,048	338,907	340,107	341,115	340,196	342,760	344,487	..	..

Govt Budget		2013/14	2014/15	2015/16 Outturn	2016/17 Revised	2017/18 Budget
Revenues	P mn	48,951	55,904	47,420	55,926	57,187
Spending	P mn	41,730	50,564	54,411	57,031	59,544
Balance	P mn	7,222	5,340	-6,991	-1,106	-2,357
Public debt & guarantees	P mn	30,790	33,398	34,057	34,826	34,787
Govt deposits at BoB	P mn	31,745	41,680	33,916	31,734	29,249
GDP	P mn	*131,221*	*148,027*	*148,353*	*156,094*	*167,374*
Revenues	%GDP	*37.3%*	*37.8%*	*32.0%*	35.8%	34.2%
Spending	%GDP	*31.8%*	*34.2%*	*36.7%*	36.5%	35.6%
Balance	%GDP	*5.5%*	*3.6%*	*-4.7%*	-0.7%	-1.4%
Public debt & guarantees	%GDP	*23.5%*	*22.6%*	*23.0%*	22.3%	20.8%
Govt deposits at BoB	%GDP	*24.2%*	*28.2%*	*22.9%*	*20.3%*	*17.5%*

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

Notes:

(a) 2013 figures include production from Boteti Diamond and Debswana

(b) 2016 figures include production from Gem Diamonds and Lerala mines

(c) Copper and Nickle production for Q3 2016 are for July and August only

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

SPECIAL FEATURE

Essential Business Environment Reform in Botswana

The process of economic diversification has been pursued for many years in Botswana, but with limited success. While the economy has become more diversified, there has been less progress in diversifying exports and sources of government revenues, and in creating employment. Achieving success in these areas will require dramatic change in the Botswana economy, and yet the need for this deep-seated structural change is not widely enough appreciated. Botswana's economic success over the past fifty years has been driven by the (well-managed) recycling of revenues from diamonds. This is not a sustainable development path for the future, however; this will require a shift from a resource-driven to a productivity-and-efficiency-driven economy, and at the same time a shift from a state-led to a private-sector-led economy.

The stimulation of private sector-led growth, by both domestic and foreign investors, obviously requires a supportive business environment, which in turn requires business environment reforms. At a high level, this is acknowledged by government, and there have been some initiatives to move business environment reform forward, such as the National Doing Business Committee. However, this does not seem to be having much impact, and there is a widespread perception of a deteriorating business climate. This is shown up in a range of quantitative indicators, such as:

Economic growth: the real growth rate of the non-mining private sector has been falling steadily, from 10% in 2011 to 1.4% in 2015, before recovering somewhat in 2016.

Employment creation has been weak: over the five years from 2012 to 2016, formal sector employment has increased on average by 1,850 jobs a year, compared to an estimated 20,000 net new entrants to the labour force each year;

Foreign Direct Investment (FDI) has fallen: in 2014-15 FDI inflows amounted to some 3% of GDP, compared to around 6% in the early 2000s;

Business Confidence is low: from a peak of 80% of firms rating current business conditions as satisfactory in 2008, confidence tumbled to 40% as a result of the global financial crisis in 2008-9; what is disturbing is that it has not significantly recovered since;

Doing Business rankings: Botswana's position (ranking) has fallen from 70 in 2016 to 71 in 2017 (out of 190 countries), and in general has deteriorated over time – in 2009, Botswana was ranked number 39 globally;

Global Competitiveness Report rankings: by contrast this has shown an improvement in Botswana's ranking, from 71 in 2015-16 to 64 in 2016-17.

Anecdotally, there are frequent complaints from members of the private sector about a deteriorating business climate and worsening economic conditions. This partly reflects the economic slowdown, in particular relatively slow growth in consumption spending by Botswana households – not a good environment for the many firms dependent on the local consumer market.

There are also concerns that Government has little understanding of the needs of the private sector and how it operates, and furthermore does not trust the private sector. This has been compounded by failures in the delivery of basic public economic services – notably water and electricity – which has cast doubt on government's ability to meet its side of the contractual bargain (provision of public goods and efficient planning) that is essential for a dynamic economy.

(Lack of) Progress with Business Environment Reform

This situation is exacerbated by what is seen as a lack of progress, or even reversals of progress, with regard to business environment reform. This can be illustrated with reference to a variety of positive reform actions that have been committed to but not implemented by government, or negative actions that have been carried out with little or no awareness (or concern) about their impact on the business environment.

This is not to say that nothing has been done. There have been some improvements in the speed of company regis-

tration, and taxes can now be paid electronically. But on balance, the pace of implementation of business environment reform has been glacial.

For instance, in 2013-14 Cabinet approved a set of wide-ranging reforms, including:

- The "one government" principle - state bodies (central as well as local government) should not require applicants/ clients to produce documents that are issued by another Government agency;
- Introducing a "negative list" approach: everything is legal, unless it is specified as being unlawful;
- E-Government: moving government processes online, while at the same time streamlining business processes;
- Limiting the number of licenses and permits: maintaining licenses for areas related to public health and safety only. Trade and general licensing requirements would be abolished, and some reserved activities would be opened up for foreign investors.

Cabinet further set timelines of 3 to 18 months for implementation of these reforms.

In addition, government considered a process of regulatory reform and introducing regulatory impact assessments, in order to minimise, or at least be aware of, the impact of new regulations on the private sector, with a view to ensuring that the benefits of any new regulations outweighed the costs.

Progress in these areas has been virtually non-existent. Although the official e-Government policy spanning the period 2011-16 has come to an end, there is not one single process of interaction with government or a government agency that can be started and completed online. And the persistent problem of "system down" when businesses and individuals try and deal with government goes from bad to worse – even the basics are dysfunctional. Government bodies frequently ask for certified copies of documents issued by other government bodies (so no "one government") They furthermore have introduced a totally illogical rule that certification "expires" even when the document being certified remains valid, and another that certification (of it being a genuine copy) has to be done by the issuer of the document, not by other entities such as the police, an attorney or a commissioner of oaths. All very frustrating and pointless, with no legal or logical basis, and seemingly designed solely to make life difficult for individuals and businesses. The proposal for regulatory review and impact assessment, for which a strategy was developed following a request for technical assistance from the World Bank, has not been pursued.

The trade licencing regime has still not been reformed in line with Cabinet decisions. Indeed, it has moved in the opposite direction, with new restrictions on the awarding of trade licenses to incoming investors in certain retail activities, with a negative impact on job creation and the property sector. Even an earlier (and welcome) decision to make trade licenses indefinite rather than subject to annual renewal has been undermined by the imposition of conditions on the payment of annual licensing fees that closely resemble the earlier license renewal conditions.

Although Cabinet agreed the reforms noted above, there was no mechanism in place for ensuring that the timelines were adhered to, nor for holding key institutions and individuals accountable for doing so.

Immigration, Work Permits and Visas

In many areas the situation for businesses has got worse, sometimes much worse. Central to the deterioration of the business climate has been the immigration and visa system. Although a points-based system (PBS) for work and investment permits was supposedly introduced several years ago, this has not helped. The intention was to have a liberal, open, transparent and objective basis for making decisions on work and investor permits. Instead, the system is illiberal, totally non-transparent and subjective, and has been used to make it far more difficult for investors to come to Botswana and for companies to recruit foreigners when they have a scarcity of skills. Totally contrary to the original intention of the system, it has even been used to force investors out of the country when they have been operating businesses for years or decades – leading to job losses in the process. No reasons are given for refusals or withdrawals of permits. Arbitrary additional requirements are introduced on a whim. It has become extremely difficult for even long-term residents to obtain permanent residence or citizenship, and there are no published criteria on what is needed to qualify.

In this environment, it is not surprising that there have been job losses, that employment has failed to grow, and that FDI is on the decline. Even obtaining visas for tourists or business visits has become more difficult. And Botswana does not offer facilities that are standard elsewhere, especially in countries that have limited international representation through embassies etc., of online visa applications, or "visa on arrival". And as with work permits, visa applications are refused with no reason given.

The Need for Openness

There is an increasing perception that Botswana is "closed for business" in relation to the international community. Although BITC was set up with the prime intention of facilitating exports and inward investment, its ability to do so is limited, in part because the "one stop shop" that has been promised for two decades has never materialised. This is in part due to the refusal of other ministries to give up power (e.g. granting work permits to investors) to BITC, and a reluctance by Governemnt to force through necessary change. Even when BITC identifies potential investors that it wants to bring to Botswana, visas can be refused.

The new Vision 2036 sets out very clearly that:

Botswana will be a destination of choice for investment. *We will avail conditions for doing business that are attractive for investment by creating a facilitative regulatory environment, supporting infrastructure, and a competitive, highly productive workforce. We will open up our economy and our country to the global world and to international expertise and know-how, and make foreign investors feel welcome. We will welcome foreign investors who wish to invest and live in Botswana (p.14).*

Given the deterioration in business confidence as well as in objective measures of business performance, it is evident that only deep and wide-ranging business environment reform will be sufficient to support a dramatic improvement in private sector growth, and to meet the aspirations and objectives of Vision 2036.

Mauritius and Rwanda

Botswana is ranked third in sub-Saharan Africa in the annual World Bank Doing Business survey, at number 71 globally, behind Mauritius (49) and Rwanda (56).

The experience of Mauritius is instructive; comprehensive business reforms through the Business Facilitation Act 2006, have supported a steady increase in investment and the development of new forms of economic activity. The Mauritius act has the following objective:

To provide for a new legal framework which would allow businesses to start operations on the basis of self - adherence to comprehensive and clear guidelines and the authorities to check for compliance by exercising ex post control, facilitate doing of business and acquisition of properties by foreigners and enable small enterprises to start their business activities within 3 working days.

In doing so, it amended existing legislation including the Building Act, Business Registration Act, Companies Act, Immigration Act, Investment Promotion Act, Local Government Act, Non-Citizens (Employment Restriction) Act, Non-Citizens (Property Restriction) Act and the Town and Country Planning Act.

The Act abolished trade licenses and allowed businesses to start operations within three days of incorporation. Residence permits and work permits for foreign investors, self-employed, and professionals were combined into an occupation permit, which is processed within three working days. Individuals holding an occupation permit can be eligible for permanent residence after three years. A new residence permit was introduced to allow non-citizens to retire in the country.

The Board of Investment (BOI), Mauritius' investment promotion organisation, plays a central role and is the single contact point for a wide range of foreign and domestic investors. The BOI has convening and directing powers, and, for instance, jointly runs the Occupation Permit Unit with the Passport and Immigration Department.

Rwanda has been through a similar – and even more dramatic – process of reforming the business environment; in 2009, it was ranked number 143 globally in the Doing Business survey. Like Mauritius, it has a highly effective investment promotion organisation (the Rwanda Development Board), with a functioning one-stop shop that can allocate land and provide other regulatory approvals to investors. Immigration is liberal for foreign investors and workers, while visas are either not required, or are available on arrival, for most nationalities. There has been a big push with e-Government ("Rwanda Online"), regulations affecting business have been reduced, and approvals speeded up.

"Game Changing" Reform in Botswana

Botswana is in need of similarly dramatic reform, based on opening up the economy, deregulation, and streamlining administrative procedures relating to all aspects of doing business in Botswana, for both citizens and foreigners. This includes:

- **Reform of immigration regulations for foreign investors and workers,** with a view to making them liberal, open, transparent, objective, and speedily and efficiently administered; similar changes are needed for the visa system for foreign visitors;
- **Abolishing trade licences,** and requiring licenses only where there is a public health and safety justification;
- **Reducing the range of reserved economic activities** from which foreign investors are excluded;
- **Liberalising land and property ownership** regulations for foreign investors;
- **Reform of zoning regulations** to allow more mixed-use development;
- **Reducing the scope of environmental impact assessments** for developments in non-sensitive areas;
- **Legally establishing the "one government" principle;**
- **Introducing legally binding time limits** for the consideration of applications for permits or authorisations, failing which "silence is consent";
- **Introducing regulatory impact assessments,** including a "bonfire" of existing regulations that are found to be unjustified, after review.

This also needs to be accompanied by **investment in appropriate infrastructure, especially that relating to e-Government.** For instance, it should be possible for all authorisations and permits to be applied for online; all statutory returns to public authorities should be possible online; national identity (Omang) cards need to be chip-based, biometric and machine readable, and the national ID database should be accessible by government departments and selected private sector entities. **Businesses should be given a single unique identifier,** used for all interactions with public authorities. Moving to electronic processes

can lead to a large increase in efficiency. While there has been an e-Government policy in the past, it has not been implemented; it is now necessary to fast-track these initiatives in a committed and coherent manner.

The proposed **Special Economic Zones (SEZs) could be used as a vehicle for implementing and refining regulatory and business environment reform.** Although the current focus of the SEZ policy is on infrastructure and financial incentives, this is insufficient; the SEZs should be primarily "regulation free" or "regulation-lite" zones. SEZs can then be used to pilot regulatory reform that can then be rolled out nationwide.

The importance of immigration reform cannot be overstated, and is probably the single most important element of business environment reform; without this, other interventions are unlikely to be effective. Immigration reform has been central to the success of Mauritius, and has underpinned an inflow of FDI. The liberal policy provides virtually automatic work and residence permits for skilled workers in certain specified (but very broad) categories of industries, and for investors bringing in investment over a certain amount. The result is an unemployment rate of 7%, and the establishment of new export-focused activities including IT services, health and education hubs, and financial services, as well as the long-established tourism sector. Mauritius has encouraged immigration despite it being the most densely population country in sub-Saharan Africa.

Botswana's attitude has been quite the opposite, and seems to be based on the flawed thinking that "one less job for a foreigner is one more job for a Motswana". This is completely wrong; international experience shows that foreign investors and skilled workers create jobs on a multiple of 5 to 100 citizen jobs for every foreigner. Evidence also shows that foreign-owned firms are also much more likely to be exporters than are locally owned firms, and less likely to be dependent on government procurement. And job creation is not the only benefit of FDI; even if direct job creation is limited, FDI generates economic activity and thereby increases GDP, boosts demand for goods and services and therefore creates jobs indirectly, and generates exports and foreign currency earnings.

The rising barriers to immigration and FDI are almost certainly one of the main reasons for declining economic growth, the slowdown in job creation and rising unemployment in Botswana. NDP11 illustrates the prevalent misguided thinking regarding this issue by referring to immigrants as a "source of problems" who can "create conflict" and "lead to social discord and instability" (para 2.19). Rather, it is the rising unemployment due to a lack of immigration that will lead to instability. Unless this is recognised, and if the immigration system remains based on thinly-disguised xenophobia and tied to a misunderstanding of how best to pursue citizen empowerment, the likelihood of transforming the economy onto a sustainable higher growth path is minimal.

Wide-ranging reform should ideally be done through a comprehensive Business Environment Reform Act, similar to Mauritius's Business Facilitation Act, which introduces wide-ranging changes and improvements to the business environment. All relevant legislation should be changed under a single omnibus Act, as amending individual statutes would take far too long. This will be politically challenging, as many in Parliament will need to be convinced of the merits of this approach. However, the first step must be for the Ministry of Trade and Industry to wholeheartedly commit to this; obtain buy-in at the highest levels of government; and begin the process of bringing other ministries and Cabinet on board. This must be done with a sense of urgency; time is passing, and if nothing is done Botswana will fall further behind other countries and the tensions arising from unemployment and failure to diversify exports and attract FDI will become even worse. And of course, **MITI should do nothing that runs counter to the objective of a liberal, open and competitive economy,** and it should take on responsibility for ensuring that other ministries do likewise.

Concluding Comments

The necessary reforms to the business environment are wide-ranging and extensive, and will change many of the current processes. This is of course the whole point, simple "tinkering" or, worse, doing nothing ("Business as Usual") will simply accentuate the process of declining growth and rising unemployment – with obvious implications for social stability. Because the business environment has deteriorated in recent years, and confidence has been undermined, drastic measures are needed – if appropriate measures had been taken earlier, then the degree of change required would have been less.

Drastic change is of course uncomfortable. There may be resistance, from those who are fearful of change, and perhaps from the few who benefit from the current inefficiencies and restrictions. There must be firm timelines and Ministers must be held accountable for implementing agreed policies. It will be essential that change is led from the top, to ensure that the Office of the President is fully on board, and willing to undertake active mobilisation to ensure there is widespread support and understanding. Without this, the change will fail, with disastrous implications for the Botswana economy. The biggest risk is that this fails and that the need for change, and the extent of change needed, is not fully appreciated and supported.

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