BIDPA Briefing

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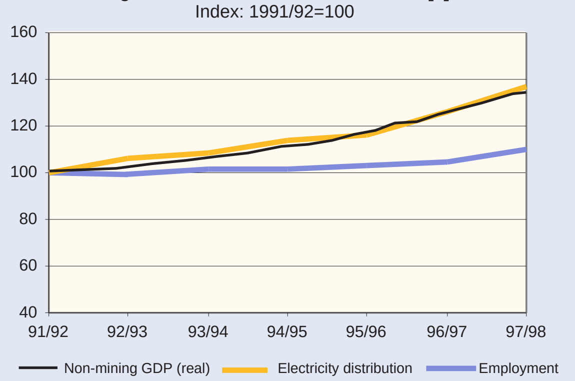
Overview

The Botswana economy continues to show healthy growth across the board, driven by most of the major components of aggregate demand - government spending, consumer spending, and private investment. This continued high economic growth, which we estimate at 7-8% for the non-mineral economy in 1998/99, has inevitably led to an upsurge in inflation, to reach 7.3% in March. Rapid expansion of bank credit remains an inflationary concern, with growth of 56% in 1998. On the export front, the growth of non-traditional exports is being constrained by sluggish economic growth in neighbouring export markets of South Africa, Zimbabwe and the SADC region more generally. As for diamonds, it appears that the bottom may have been reached in 1998. Diamond sales by the CSO in the first three months of the year indicate a small market recovery, and as long as there is no economic slowdown in the USA, 1999 should see an improvement in the international diamond market. With increased production as the expansion of the Orapa mine nears completion, Botswana will be entitled to sell more diamonds through the CSO, and hence should see higher diamond exports in 1999 than in 1998 and an improvement in the balance of payments.

Features of the Current Economic Boom

There seems little doubt that the Botswana economy is now growing quite fast. After a couple of years (1992-94) when growth in the non-mining economy was only about 3% a year, the growth rate rose to 5% in the following two years, and in the two years ending in June 1998 growth was nearly 8%. But beyond this headline growth rate, what does this mean for other aspects and indicators of economic activity?

Fig.1: Indicators of Economic Growth [1]
Index: 1991/92=100



One of the most striking aspects of the present boom is that employment has not grown significantly; whereas real non-mining GDP grew by 36% between 1991/92 and 1997/98, formal sector employment grew by only 10% over this period (see Fig.1). Furthermore, all of this employment growth has occurred in government; in fact, employment in the private and parastatal sector was actually lower in March 1998 than it was in March 1992.

The one encouraging sign is that employment growth has finally taken off, with an increase of 5.4% in formal sector employment between March 1997 and March 1998.

This illustrates a second feature of the boom: although the economy as a whole appears to have picked up from around 1994/95 onwards, several indicators of economic activity did not show any movement until much later (see Fig.2). Imports, for instance, which are normally closely associated with the general level of economic activity, only really started growing in 1997 and 1998. However, once recovery did start, growth was very fast, with imports in 1998 estimated to be 50% higher, in real terms, than in 1996.

A similar trend is apparent with another useful indicator of economic intentions and confidence, the level of building plans approved by local authorities. This almost doubled from 159,000 m² in 1995/96 to 311,000 m² in 1997/98, after having fallen by 50% in the previous three years. This decline and then recovery reflects the turmoil experienced by the construction sector over this period, but indicates that the business climate for that sector should now be very good. The level of credit from banks to businesses shows the same trend: a sharp reduction between 1994 and 1997 – down by more than one-third in real terms – and then recovery with a rise of 50% between June 1997 and the end of 1998.

It is not easy to understand these delayed reactions to the increase in the rate of growth of GDP. The most plausible explanation could be that after the relative recession in the early 1990s, businesses had spare capacity, and therefore did not need to borrow

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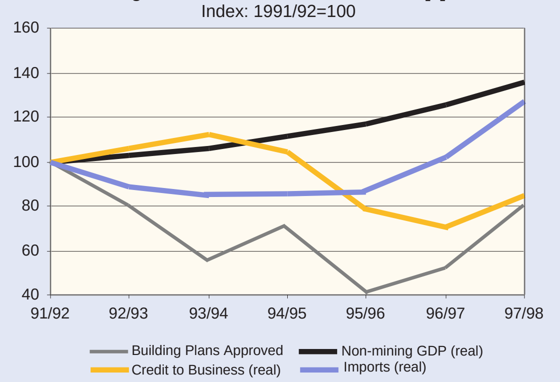
Fig.2 Indicators of Economic Growth [2]
Index: 1991/92=100



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as much as might otherwise have been expected. They may also have held on to some of their labour during the recession, so that when growth resumed they did not need to hire new workers for a year of two. If this argument is correct, it would appear that the slack has now being taken up, and that this explains the recent rapid acceleration in bank lending and other indicators.

Another point is that these indicators of economic activity (building plans, real imports, real business credit and employment) do not appear to be very closely related to GDP – the timing of their changes is different, and those changes are mostly larger (except for employment) than changes in GDP. However, there is one indicator that appears to track GDP very closely: use of electricity. As Fig.1 shows, the amount of electricity used in Botswana has increased more or less in line with non-mining GDP – the 37% increase in electricity consumption between 1991/92 and 1997/98 is almost the same as the 36% increase in real non-mining GDP over the same period. This close relationship may make electricity consumption useful as an indicator of economic activity, before GDP figures are published. In the 9 month period from July 1998 to March 1999, electricity consumption increased by 7.7%, which is in line with our expectations of current non-mining economic growth.

Savings and Investment

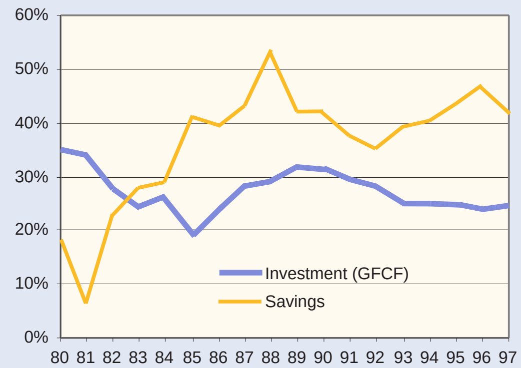
Savings and investment are two of the most important components of macroeconomic balance in any country. One of the striking characteristics of the Botswana economy over the past two decades, besides its rapid growth, has been a dramatic increase in the national savings rate. Gross savings rose from 19% of GDP in 1980 to 47% in 1996, peaking at over 50% in 1988. Botswana's savings rate, averaging over 40% of GDP since the mid-1980s, is exceptionally high by international standards.

In contrast to the upward trend in savings, investment (in fixed assets, i.e. excluding stockbuilding) has been much more stable over the period shown, averaging around 27% of GDP. Fluctuations in annual savings and investment rates around the long term trends are largely driven by activity in the mining sector – rapid increases in diamond exports lead to higher savings (in the late-1980s and mid-1990s), while the high level of investment in the early 1980s was also mining-led. The rise in investment in the late 1980s was however more due to increases in investment by government and the non-mining private sector. Of some concern is the apparent decline in the investment rate since the early 1990s, from 32% of GDP in 1990 to 24% in 1996/97.

Before 1983, investment exceeded savings and hence Botswana ran a deficit on the current account of the balance of payments and was dependent upon capital inflows to finance investment. However, since 1983 savings have exceeded investment and the current account has been in surplus. As Fig.3 shows, there is no obvious long-term relationship between savings and investment; increases in savings are not directly translated into higher domestic investment.

However, the latest national accounts data, for 1997/98 indicate an interesting picture for both savings and investment. There has been a slight increase in investment from 24% of GDP in 1996/97 to 25% in 1997/98, while savings declined by 5% over the same period. It is to be hoped that the increase in investment, although small, indicates that the economy is moving in the right direction in terms of policies directed towards enhancing investment. The key question, however, is whether this increase in investment will continue into the future and whether it is sustainable.

Fig.3 : Savings and Investment as % of GDP



The decline in savings is partly due to the poor performance of diamonds in international markets in 1998 that led to a major reduction in mineral revenues. In particular, government savings fell sharply with the move into a budget deficit, and as this was not matched by a corresponding increase in private savings a fall in the overall level of national savings was the inevitable result.

Is a rising investment rate and a declining savings rate a problem? Not yet, as the only short-term impact will be to reduce the rate at which the foreign exchange reserves grow. Furthermore it is important that a high investment rate is maintained in order to support economic growth, diversification and job creation. In the long term, however, a shortage of savings could become a constraint on investment, and hence it remains important to explore other possible sources of savings in order to replace those generated in the past from diamond exports.

Recent Growth in Tourism

The tourism sector has recently been seen as having considerable potential to contribute towards Botswana's economic diversification. Growth of the tourism sector would not just help to increase export earnings and create jobs, but it could also help to revitalise the declining rural economy. Internationally, tourism has become increasingly important to many countries, and is sometimes claimed to be the world's fastest growing industry. For many developing countries, tourism is a significant net earner of foreign exchange.

Although tourism is recognised as having potential in Botswana, identifying its present contribution to the economy is difficult, due to data deficiencies. For instance, tourism is not an identifiable sector in the national accounts, but instead cuts across other sectors, such as trade and hotels, and transport. Nor has any data on tourism expenditure been published since 1993. Hence

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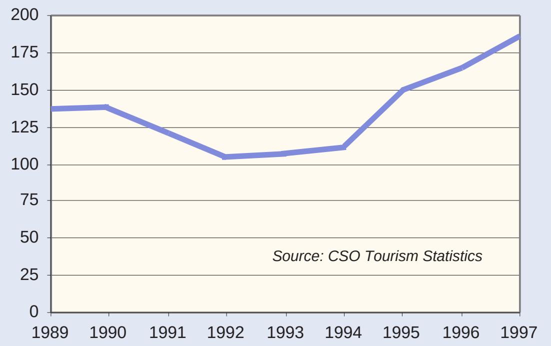
there is at present no reliable indicator of tourism's contribution to GDP.

However, there is up-to-date information on visitor arrivals and departures, and this is an internationally-recognised way of measuring the size of a country's tourism sector. In particular, the annual changes in arrivals represent a reliable indicator of industry growth (assuming that average visitor spending and length of stay remain unchanged).

Using these data, we can assess the growth of tourism in Botswana in recent years. Figure 4 shows visitor arrivals for holiday purposes (in contrast to international convention, we do not include business visitors as tourists). What is clear is that after suffering a downturn in the early 1990s, due to international recession and the Gulf War, which adversely affected the tourist industry worldwide, Botswana's tourism industry has benefited from rapid growth since 1992. Over the five years to 1997, the number of holiday visitors grew by 80%, or nearly 14% a year.

This is much faster than the rate of growth of total arrivals to Botswana (4% a year) and as a result the share of holiday visitors grew from 11% to 16% of all arrivals in Botswana over this period. It also exceeds the 5% a year growth recorded for the tourism industry internationally. Furthermore, if the trend in visitor arrivals does reflect the growth of the tourism sector as a whole, this sector grew faster than any other sector of the Botswana economy over this period.

Fig.4 Holiday Visitor Arrivals
('000s)



All of this is quite encouraging, if tourism is to become an increasingly important sector of the economy. The most rapid growth occurred in the last three years, and it is to be hoped that this trend can be sustained. Hence the importance of the new Tourism Master Plan, currently under development, and the need for good quality statistical information on more aspects of the tourism sector ~~than simply arrivals and departures.~~

Foreign Direct Investment in Botswana

The Bank of Botswana has recently produced the first data on the stock of foreign direct investment (FDI) in the country. The data, which relates to the end of 1997 and was derived from a balance of payments survey carried out during 1998, includes foreign liabilities of all resident companies, but excludes the liabilities of government. It takes a relatively broad definition of FDI, and includes shares, bonds, loans and trade credit, but not portfolio investment through the Botswana Stock Exchange.

According to the survey, foreigners had invested P5.2 billion in Botswana at the end of 1997. It is difficult to interpret this number on its own, because the lack of data for earlier years prevents us from identifying any trends in FDI – for instance, whether or not policies to attract foreign investment have been successful. However, to provide some kind of perspective, we can note that as at June 1997, the total fixed capital stock of the private sector was approximately P18 billion.

The BoB data show that the majority of FDI has been directed towards the mining sector, followed by the manufacturing, finance and trade sectors. The data also show that the main source of FDI for Botswana has been South Africa.

However, interpreting the data is further confused by an anomaly that has also plagued the balance of payments data in the past, that is, the position of the BCL copper-nickel mine. Because this mine has never been profitable, it has built up huge debts to its shareholders (the Government of Botswana, and Anglo American Corporation of SA). Again, due to BCL's poor financial position, it cannot pay the interest due on this debt. While the shareholders have not foreclosed on these loans – because to do so would mean the closure of the mine – the missed interest and repayments are treated as new incoming FDI, and are added to the stock of existing FDI. This would not matter if the amounts were small, but they are not, and BCL's accumulated debt is now reckoned to ac-

Fig.5: FDI (Equity) by Economic Sector

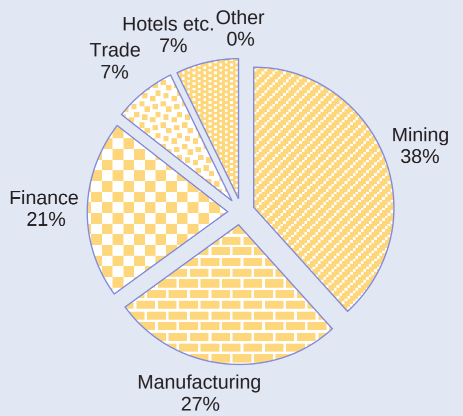
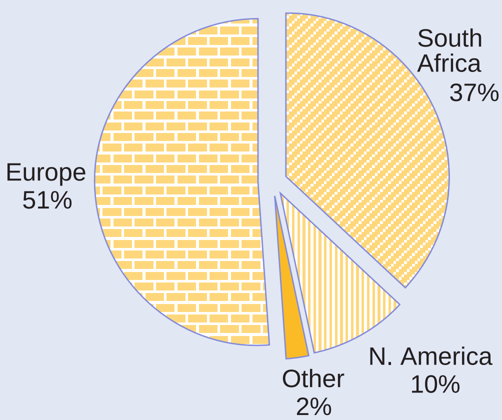


Fig.6: FDI (Equity) by Origin



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P5 billion of FDI. Imputed flows attributable to BCL are now identified separately in the annual balance of payments statistics, but are not so identified in the FDI figures; hence they distort the breakdown of “true” FDI across sectors and countries of origin, and tend to inflate the value of FDI from South Africa in the mining sector.

One way of avoiding the BCL problem is to consider equity investment only, and ignore loans and other types of liabilities that complicate the picture. Another advantage of concentrating on equity is that it represents share capital that is committed by foreign investors to Botswana on a more or less permanent basis.

This changes the FDI picture a bit, although not fundamentally. Mining is still the largest recipient, although manufacturing is not that far behind (see Fig.5). The importance of tourism, highlighted above, is shown by the 7% share attributable to inward investment in hotels and restaurants. By origin, the largest source of equity investment is Europe (Fig.6), which may reflect the domicile of De Beers Centenary, the government’s partner in Debswana. But it is nevertheless surprising that South Africa is not the largest source of equity investment in Botswana.

ECONOMIC FACTS AND FORECASTS

Quarterly	1997	1998				1999	
(end of period)	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Interest rates (%)							
BOBC (3 month)	11.40	10.26	10.21	10.46	10.66	11.55	11.75 f
Prime	14.00	13.31	13.25	14.00	14.00	14.25	14.75 f
Inflation (%)	7.8	6.9	6.1	5.9	6.4	7.2	7.5 f
Rand-Pula	1.28	1.29	1.36	1.30	1.32	1.33	1.34 f
Pula-US$	3.81	3.90	4.33	4.48	4.46	4.67	4.75 f
BSE index	708	811	949	954	947	990	-

Annual		1993	1994	1995	1996	1997	1998	1999
Growth (%)								
GDP (real)	d	4.2	2.7	6.6	7.2	8.3	7.5 e	-
Non-mineral GDP (real)	d	3.5	4.8	5.0	7.9	7.7	7.5 e	-
Exports (nominal)	b	15.3	18.4	19.7	40.7	27.8	-12.5 p	24 f
Imports (nominal)	b	9.2	2.7	20.4	8.2	43.9	28.6 p	15 f
Govt. spending (nominal)	c	11.8	-4.6	21.5	17.3	21.6	31.5 p	15 f
Govt. revenues (nominal)	c	14.3	-16.5	22.2	35.3	12.0	-0.1 p	26 f
Domestic (bank) credit	b	11.8	18.2	-3.7	1.2	5.6	56.1	25 f
Interest rates (%)								
BOBC (3 month)	a	13.5	11.9	12.0	12.2	11.4	10.7	12.0 f
Prime	a	15.0	14.0	14.5	14.5	14.0	14.0	15.0 f
Inflation (average, %)		14.4	10.6	10.5	10.1	8.9	6.5	7.0 f
Rand-Pula	a	1.32	1.30	1.29	1.28	1.28	1.32	1.36 f
Pula-US$	a	2.56	2.72	2.82	3.64	3.81	4.46	4.95 f
BSE index	a	279	313	333	352	709	947	-
Balance of Payments (Pm)								
Exports (diamonds)	b	3340	3727	3994	5272	7654	5929 p	7800 f
Exports (other goods)		841	1304	1994	2100	2454	3074 p	3300 f
Imports (goods, cif)	b	4290	4406	5305	5743	8256	10388 e	11950 f
Current account balance	b	1220	642	937	2108	3059	-375 p	250 f
Foreign Reserves								
Pula m	a	10509	11961	13249	19076	21619	26347	29000 f
US$ m	a	4097	4402	4695	5234	5675	5960	6000 f
Govt. spending (Pm)	c	4481	4277	5195	6092	7406	9736 p	11200 f
Govt. revenue (Pm)	c	5359	4473	5464	7395	8281	8271 p	10400 f
Budget surplus/(deficit) (Pm)	c	878	196	269	1303	875	-1465 p	-800 f
Govt. balances at BOB	a	5598	6705	6460	7204	15634	19212	20000 f

Notes: *a = end of period; b = calendar year; c = financial year (starts March); d = statistical year (starts July); e = BIDPA estimate; f = BIDPA forecast; p = preliminary data*
Details of assumptions underlying the forecasts can be obtained from BIDPA.

Sources: *CSO, Bank of Botswana, BIDPA*

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