



BIDPA

Briefing

The production of this publication is sponsored by Botswana Insurance Fund Management

bifm[®]

ISSN 1560-5817

3rd Quarter 1999

Overview

A range of economic indicators recently made available confirms that the economy has been growing rapidly over the past 18 months. Data on transport and communications show major increases in activity during 1998, and even employment showed a substantial increase in that year after years of sluggish growth. Other data, such as bank lending and electricity consumption indicate that this growth has continued during 1999. Particularly encouraging during the third quarter of the year was good news concerning the international diamond market, with forecasts suggesting that 1999 sales by De Beers are likely to be at an all-time high. This will impact favourably on Botswana's balance of payments and government budget, and contrasts with the gloom that characterised the industry at the end of 1998. The main negative points in the economy are a gradual increase in inflation and a continued unsustainable expansion of bank lending to households.

In this issue, in response to numerous requests, we have extended our economic forecasts out to the end of the year 2000. Obviously these are subject to much uncertainty and will be revised over time, but we hope that they prove to be useful and informative. They mostly show that the positive economic environment that exists at present should continue well into next year, but that a downturn in economic growth is expected heading into 2001.

Economic Developments

Minerals

The most notable economic development of the third quarter of 1999 has been the dramatic recovery in diamond sales. While there were signs of this in the second quarter, as highlighted in the last issue of the BIDPA Briefing, the recovery has been much faster than was anticipated by most commentators. Diamond sales by De Beers' Central Selling Organisation are now projected to be at least US\$5 billion for the year as a whole, which would be the highest level ever, and contrasts with forecasts of only \$3.5 billion for 1999 sales made at the end of last year. Whereas Botswana and other members of the CSO started the year expecting to stockpile 20-25% of production, it is now anticipated that stockpiling will be at most 5%. Not only will this have a positive impact on the economy as a whole, it will also provide a positive market environment for the major increase in Botswana's diamond production that will result when the Orapa expansion comes on steam early in 2000.

There are a number of explanations for this turnaround. There has been much faster than expected economic recovery in Asia, with diamond sales in Japan and South Korea showing

good growth. At the same time the US economy has continued to grow rapidly, with little sign of inflationary pressures emerging, which would have indicated a need for tighter monetary policy which would have restricted growth. There are also signs that De Beers' marketing campaign for Millennium Diamonds will lead to a healthy increase in sales, and although this will be a one-off event rather than a sustained increase, it is nonetheless welcome. Finally, the sharp drop in the CSO's sales in 1998 was in part due to the need to reduce stocks of rough diamonds in the cutting centres, which had built up to unsustainable levels given the problems that the retail market faced last year. With the market recovery in 1999, the cutting centres are again building up stocks, especially ahead of the good sales anticipated for the year end, and this has enabled the CSO to provide more supplies to the market.

For Botswana, this will have a positive impact on both the government budget and the balance of payments. Diamond exports are now projected at around P9 billion, or US\$2 billion for the year, an increase of 50% over 1998. This should lead to an increase in the current account surplus from around P500m in 1998 to P2 billion

this year. The government's target of P4.8 billion for mineral revenues in the 1999/2000 financial year, which appeared optimistic at the time of the 1999 Budget back in February, will now most likely be comfortably exceeded. We are now projecting a smaller deficit than the budget forecast of P400m, although, depending on expenditure trends, even a surplus is possible. Expenditure trends are important but somewhat uncertain, given that capacity and implementation constraints appear to be keeping actual spending somewhat below budgeted levels.

While diamonds are by far the most important of Botswana's mineral exports, there are positive developments elsewhere. The nickel price has increased by nearly 100%, from \$1.70 a pound last year to over \$3 a pound, and copper prices have also improved, although less dramatically. This has helped Botswana's troubled BCL copper-nickel mine. An emergency line of government funding was made available earlier in the year to keep the mine going in the face of operating losses, but BCL has not had to draw upon this since April.

Exchange Rates

Exchange rates of the pula against international currencies have been

Continued overleaf

Continued from overleaf

relatively stable during the year, reflecting the strength of the rand - to which the pula is loosely pegged - in international markets. The pula lost 2% of its value against the US dollar in the nine months to September, and remained stable against the broader SDR basket.

The rand has been remarkably resilient, showing only limited losses during the period of gold price weakness in the middle of the year, and recovering with the gold price towards the end of the third quarter. However, there is some concern that the stability of the rand has led to its becoming overvalued in international markets, and that further depreciation will be necessary to restore the competitiveness of South African producers of exports and import substitutes. This could become a more serious problem during 2000. Economic growth in South African looks set to recover, with growth forecasts of 3-3.5%, compared with only 0.5% in 1999. While this will be positive for Botswana and the rest of southern Africa, the recovery is likely to lead to an upsurge in South African imports and a deterioration in the current account of the balance of payments, which could again put the rand under pressure.

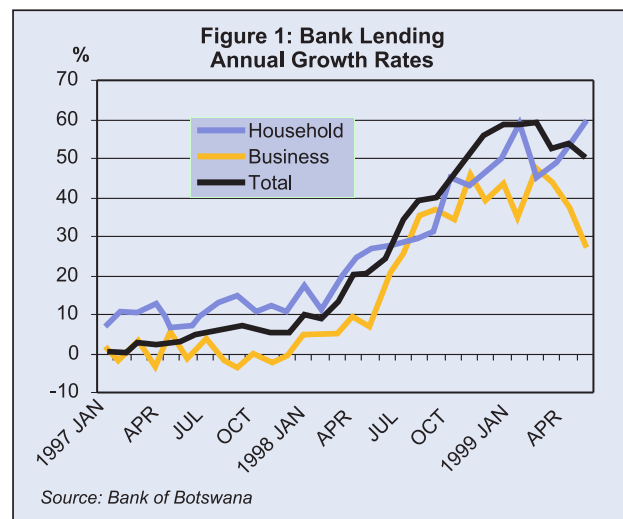
Inflation

Botswana inflation has crept up in recent months, rising from 6.9% in July to 7.0% in August and 7.6% in September. This increase may seem surprising, given that South African inflation fell to 3.9% in August, the lowest level for 30 years. However, the headline South African rate is highly influenced by changes in interest rates and mortgage bond payments, which have no direct impact in Botswana. The South African core inflation rate, which excludes such volatile items, is of more relevance as a determinant of price changes in Botswana, has shown little change in recent months, remaining in the 7.5-8% range. Hence we do not expect much of a reduction in Botswana's inflation rate until well into next year, especially as the recent increases in local fuel prices could well feed

through to other prices before the end of the year.

Credit growth

The rate of growth of bank lending, which has risen sharply over the past year, remains at very high levels (see figure 1). Total bank lending grew by 50% in the 12 months to June 1999, a slight reduction from previous months but still very high. Besides the problem of overall credit growth remaining at an unsustainably high rate, it is also worrying that recent months have shown a reduction in



the growth of credit to businesses but an increase in the growth of credit to households. This is exactly the opposite of what the economy needs. Household indebtedness is already worryingly high, and further growth increases the probability that a slowing down of the economy will lead to a repeat of the household debt crisis that was seen earlier in the 1990s. By contrast, business credit, which is at much more manageable levels, is needed to finance the expansion of economic activity.

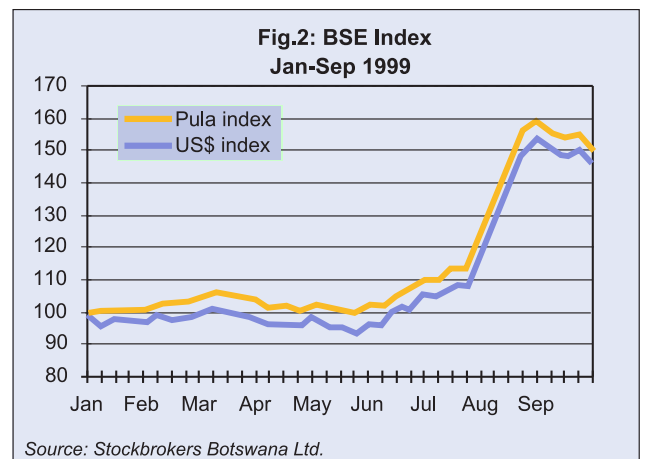
Botswana Stock Exchange

1999 has been a very good year so far for the BSE (see figure 2). The

domestic company index closed the third quarter at 1417, an increase of 50% over nine months. Most of this increase has been due to sharp rises in the value of the three commercial bank stocks that dominate the index, accounting for 66% of market capitalisation, following good profits performance. However, other local companies have also done well, with Inco Holdings, Botswana Insurance, Med Rescue and Sefalana all recording gains of over 40%.

In US dollar terms, the BSE index has risen by 45% since January, making it one of the better performers amongst developing country stock markets. However, it is not exceptional; several markets have done better, with increases of over 50%, notably Turkey, South Korea and India. Within Africa, Botswana has been the second best performer (see

figure 3). Perhaps surprisingly, the best African performer during the year has been Zimbabwe, with an increase of 79%, although it should



be noted that in 1997 the Zimbabwe market fell by 55%.

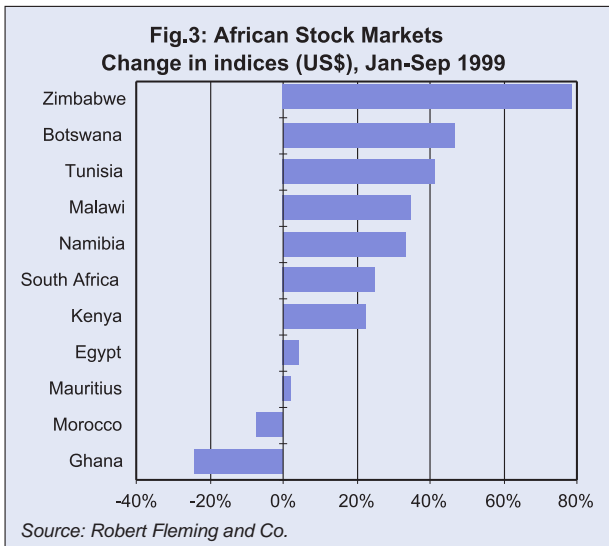
Over a three-year period, Botswana was by far the best-performing stock market in Africa, with an increase of 214% in US dollar terms. Several other markets - South Africa, Zimbabwe,

Continued overleaf

Continued from overleaf

Kenya, Namibia and Tunisia have experienced negative returns over this longer period. Even amongst those achieving positive returns – Mauritius (+3%), Egypt (+13%), Ghana (+22%) and Morocco (+75%) – none comes close to matching the BSE.

Another promising development on the BSE during the year has been new company listings. The recent listings of tourism company Chobe Holdings and information technology company RPC Data were both more than 2 times oversubscribed. Although small, these companies mark a diversification of listed stocks into new areas of economic activity



away from the BSE's traditional concentration on financial sector and consumer product stocks. Further listings are expected early in 2000.

Recent Economic Data

Employment and Earnings

The Central Statistics Office has recently released data on formal sector employment for 1998. Over the 12 months to September, employment rose by 6.5%, from 226,900 to 241,700. One encouraging aspect was that employment in the private sector rose by 6.9%, in contrast to recent years where employment growth had mainly been driven by an expansion of the public sector. However, employment growth in the private sector was largely the result of a

massive expansion of employment in construction (up 29%), which may not be sustainable when the current building boom comes to an end. Employment in the rest of the private sector rose by only 2.5%. Nevertheless it is encouraging that formal sector employment growth is significantly in excess of population growth, and hence should be contributing to a reduction in unemployment (although unfortunately there is no direct data on unemployment since 1996).

The CSO data also provides information average earnings, and reflects the impact of the large public sector pay rise awarded in mid-1998. Not surprisingly, average monthly earnings in central government rose sharply, by 38%, from P1360 to P1871, with earnings in parastatals showing a similar rate of growth. However, it appears that this did not spill over into the private sector, where average earnings rose by only 10%, from P1154 to P1272. This suggests that fears of a major boost to inflation from the public sector pay award have not been realised.

Transport and Communications

A second set of data issued recently by the CSO covers transport and communications statistics for 1998. These data, covering motor vehicle registrations, rail and air transport, telecommunications and mail services, present a picture of broadly based and rapid economic growth. This is consistent with other evidence of a booming economy, such as the employment data discussed above. A

Transport & Communications Statistics

	1997	1998	Change
Air passenger movements	366,665	404,072	10%
Aircraft movements	59,736	66,752	12%
Rail freight (tonnes)	2,432,148	2,782,377	14%
Privately-owned vehicles	89,935	105,404	17%
Telephone subscribers	83,690	101,974	22%
Volume of mail	-	-	26%

Source: Central Statistics Office

selection of these data is shown in Table 1.

Finally, our most up-to-date indicator of real economic activity is electricity consumption. According to data provided by the Botswana Power Corporation, consumption increased by 9.5% in the first 8 months of 1999 as compared to the same period in 1998.

BEDIA – One Year On

The Botswana Export Development and Investment Agency (BEDIA) has now been operating for almost one year. As its name implies, BEDIA was established to promote investment in Botswana, in particular in those export-oriented activities that are essential to the diversification of the economy and creation of employment. Its activities have focused on both outward and inward investment missions. The former have involved sending Botswana entrepreneurs to various countries to meet up with potential investors, especially those interested in joint venture projects. The latter have involved bringing potential investors to Botswana, to give them a chance to evaluate opportunities and to take concrete steps to establish new investment projects.

At this time, a number of promising projects are in the pipeline. By the end of 1999, it is hoped that three new projects will be operational. These comprise a factory in Francistown making garments for the European market, promoted by a Hong Kong based company; a factory near Selebi-Phikwe making blankets for the regional and US markets, undertaken by a company from India; and a project in Gaborone to be established by a prominent company from Mauritius making knitwear for the international market. Between them,

Continued overleaf



Continued from overleaf

these three projects are expected to create 2000 jobs - equivalent to nearly 10% of the current manufacturing labour force.

Further investments arising from BEDIA's activities are anticipated in the first half of next year. These include companies making telephone handsets, kitchen utensils, pharmaceutical

products, nails and wire products, as well as various activities in the garments and textiles sector. Several of these projects are expected to involve joint ventures between local and foreign investors.

Assuming that most or all of these and other projects come to fruition, BEDIA will be making a major con-

tribution to economic diversification and job creation. However, a key task is now to ensure that the well-known constraints to investment in Botswana - especially shortages of serviced land and skilled labour - are alleviated so that further investments are not delayed.

ECONOMIC FACTS AND FORECASTS

(end of period)	Quarterly								
	1998				1999				
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	
Interest rates (%)									
BOBC (3 month)	10.26	10.21	10.46	10.66	11.55	11.75	11.68	12.0 f	
Prime	13.31	13.25	14.00	14.00	14.25	14.75	14.75	15.0 f	
Inflation (%)	6.9	6.1	5.9	6.4	7.2	7.5	7.6	7.5 f	
Rand-Pula	1.29	1.36	1.30	1.32	1.33	1.30	1.32	1.36 f	
Pula-US\$	3.90	4.33	4.48	4.46	4.67	4.63	4.55	4.68 f	
BSE index	811	949	954	947	990	1033	1417	-	
	Annual								
	1993	1994	1995	1996	1997	1998	1999	2000	
Growth (%)									
GDP (real)	d	4.2	2.7	6.6	7.2	8.3	4.6 e	9.0 f	2.5 f
Non-mineral GDP (real)	d	3.5	4.8	5.0	7.9	7.7	9.0 e	8.5 f	2.0 f
Exports (nominal)	b	15.3	18.4	19.7	40.7	27.8	-12.5	37 f	13 f
Imports (nominal)	b	9.2	2.7	20.4	8.2	43.9	19.7	17 f	17 f
Govt. spending (nominal)	c	11.8	-4.6	21.5	17.3	21.6	31.5	15 f	11 f
Govt. revenues (nominal)	c	14.3	-16.5	22.2	35.3	12.0	-0.1	33 f	13 f
Domestic (bank) credit	b	11.8	18.2	-3.7	1.2	5.6	56.1	35 f	- f
Interest rates (%)									
BOBC (3 month)	a	13.5	11.9	12.0	12.2	11.4	10.7	12.0 f	11.0 f
Prime	a	15.0	14.0	14.5	14.5	14.0	14.0	15.0 f	14.0 f
Inflation (average, %)		14.4	10.6	10.5	10.1	8.9	6.7	7.2 f	6.7 f
Rand-Pula	a	1.32	1.30	1.29	1.28	1.28	1.32	1.36 f	1.36 f
Pula-US\$	a	2.56	2.72	2.82	3.64	3.81	4.46	4.68 f	4.89 f
BSE index	a	279	313	333	352	709	947	-	-
Balance of Payments (Pm)									
Exports (diamonds)	b	3340	3727	3994	5272	7654	5929	9000 f	10500 f
Exports (other goods)		841	1304	1994	2100	2454	3079	3300 f	3600 f
Imports (goods, cif)	b	4290	4406	5305	5743	8256	9670	11300 f	13000 f
Current account balance	b	1220	642	937	2108	3059	478	2000 f	2200 f
Foreign Reserves									
Pula m	a	10509	11961	13249	19076	21619	26347	30000 f	33000 f
US\$ m	a	4097	4402	4695	5234	5675	5960	6350 f	6750 f
Govt. spending (Pm)	c	4481	4277	5195	6092	7406	9736	11200 f	12450 f
Govt. revenue (Pm)	c	5359	4473	5464	7395	8281	8271	10950 f	12150 f
Budget surplus/(deficit) (Pm)	c	878	196	269	1303	875	-1465	-250 f	-300 f
Govt. balances at BOB	a	5598	6705	6460	7204	15634	19212	20000 f	20700 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

This edition of the BIDPA Briefing was written by Keith Jefferis
(e-mail: keithj@bidpa.bw).

Published by BIDPA, Private Bag BR29, Gaborone, Botswana.

Tel: (+267) 371750 Fax: (+267) 371748. Website: <http://www.bidpa.bw>

While every attempt is taken to ensure the accuracy of the information contained in this document, no responsibility can be assumed for any action based thereon. The Botswana Institute for Development Policy Analysis (BIDPA) is an independent, non-government research institute with two main areas of interest: development policy analysis, and capacity building. BIDPA's functions include carrying out research and consultancy in the fields of economic and social policy, as well as monitoring the performance of the economy and the management of public policy. BIDPA's clients include government, international organisations, NGOs, and companies.

BIDPA Briefing is sponsored by bifm, Botswana's largest manager of pension and insurance fund assets with over P1 billion under management. bifm encourages greater public understanding and awareness of Botswana business and economic issues and is therefore delighted to support BIDPA Briefing, providing independent analysis and economic forecasts to business and policy makers throughout Botswana. The views expressed in this edition of BIDPA Briefing are those of BIDPA and are not necessarily those of bifm.

bifm[®]