The South African Institute of International Affairs
RESEARCH PROJECT

Africa's First Welfare State

The Experience of South African Firms Doing Business in Botswana

Neuma Grobbelaar
Ian Taylor

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About the Authors

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About the SAIIA Business in Africa Project

This is the fourth country case study in a comprehensive review of business conditions prevailing in Africa, conducted by SAIIA's Business in Africa project. The report forms part of a series of country and sectoral studies undertaken with a view to extrapolating specific policy recommendations for African

governments on how to create a more supportive business environment in Africa.

The New Partnership for Africa's Development (Nepad) initiative emphasises the critical importance of the private sector in the continent's economic development. South Africa's track record as a significant, and even more important, a fellow African investor is a notable indicator of business confidence in the future of Africa. It is also paving the way for the private sector to play a stronger role in the continent's development.

Although it is generally assumed that South African investors are less averse than others to taking risks in view of their knowledge of, and proximity to, the African market in terms of appropriate technology and products, the SAIIA Business in Africa project aims to verify whether this is indeed the case. Moreover, the research aims to identify critical areas in which reform is essential if Africa's private sector is to contribute to growth.

The Business in Africa project is headed by Neuma Grobbelaar, the Deputy Director of Studies at SAIIA, and assisted by Hany Besada, the Business in Africa researcher.

The following reports have been published by the project thus far:

Games D, *A Preliminary Survey: The Experience of South African Firms Doing Business in Africa*, Business in Africa Report 1, SAIIA, 2003.

Grobbelaar N, *'Every Continent Needs an America': The Experience of South African Firms Doing Business in Mozambique*, Business in Africa Report 2, SAIIA, 2004.

Games D, *An Oil Giant Reforms: The Experience of South African Firms Doing Business in Nigeria*, Business in Africa Report 3, SAIIA, 2004.

Besada H, *Glimpse of Hope in West Africa: The Experience of South African Firms Doing Business in Ghana*, Business in Africa Report 4, SAIIA, 2005.

Methodology and Rationale

This report is based on a series of interviews that were conducted in Botswana in April/May 2004 with resident South African companies to research their experience of the Botswana business environment. SAIIA surveyed just under 20 South African firms currently operating in Botswana. The focus group comprised a representative segment of South African corporate and parastatal involvement in Botswana, and covered all sectors (construction, retail, property, services, mining, franchising and industry). The one-on-one interviews with businesses in Botswana were supplemented by follow-up meetings at some of the head offices of those companies in South Africa. In addition, interviews were conducted with a range of representatives of government and of private sector institutions that are directly involved in this area.

Surprisingly, the Botswana environment is characterised by a paucity of data on foreign investment which makes it difficult to draw conclusions and make comparisons over time. The data provided by the Botswana Department of Industrial Affairs and the Bank of Botswana (BOB) assisted the authors to overcome some of these problems. The study was also informed by research conducted by the Botswana Institute for Development Policy Analysis (BIDPA), the UN Economic Commission of Africa (UNECA), the UN Conference on Trade and Development (UNCTAD), the International Monetary Fund (IMF), the World Trade Organisation (WTO), the Ministry of Finance and Development Planning and the BOB.

The purpose of the study was to identify some of the pitfalls associated with doing business in a country such as Botswana, while also giving credit to some of the success stories. The study was also informed by Botswana's being a member of the Southern African Customs Union (SACU), as is South Africa.

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Executive Summary

Botswana has traditionally been a strong economic partner of South Africa. The foundation for this relationship dates back to the establishment of the Southern African Customs Union (SACU) in 1910. As former British colonies, both South Africa and Botswana share many institutional, political, economic and cultural traditions. As a result, South Africans generally find the operating environment both familiar and reassuring.

The country's spectacular growth over the last three decades has its origin in the prudent management of its rich diamond resources. The South African-based diamond giant, De Beers, has been the most significant investor since 1968 in this sector through its joint partnership with the Botswana government in the holding company, Debswana. However, South African investment in other sectors has increased substantially since 1994, with the dismantling of apartheid and the growing outward expansion of South African business activity into the rest of Africa.

Some of the main findings of this study are as follows:

- Most South African investors view the Botswana business environment as **stable, fairly free of corruption and investor-friendly**. Many South African companies have a long-standing presence in the country that predates 1994. However, investment has increased in every sector in Botswana since the 1990s, including property development, banking and mining, although franchising and retail seem to be the most dominant. Although the latter is the most visible, it is not perceived in Botswana as adding substantial value to the economy.
- Botswana's membership of **SACU holds clear advantages for South African investors**, and has strongly supported the

growth of the South African retail sector in Botswana. However, the study found that the Botswana government has mixed feelings about the benefits of SACU to its economy — especially in its earlier form, prior to the adoption of the re-negotiated customs agreement in 2002. SACU has been accused of undermining Botswana's manufacturing base and drawing foreign investment away from that country. The close economic inter-linkages between the two countries also imply that South African economic policy decisions often have unintended consequences for Botswana.

- Apart from mining, Botswana's **other sectors such as manufacturing, tourism and offshore financing are all contingent on the health of the South African economy** and its trade relations with regional neighbours, in particular Zimbabwe.
- Many South African businesses that were interviewed regarded Botswana as a **springboard into the rest of Africa** for their operations. Botswana's good infrastructure was cited as a positive factor in this assessment.
- Most South African companies considered the Botswana government's strong local employment policy as a positive and understandable factor. However, they mentioned as drawbacks some of the difficulties that they had experienced in acquiring work permits for foreign employees where necessary skills were not available in Botswana. Ironically, the **small population of Botswana is a factor that inhibits the expansion potential of the economy**. Indeed the reluctance of the Botswana government to embrace the employment of non-Batswana raises the question whether the country will be able to sustain its current high growth levels. There are also increasing numbers of alarming

xenophobic incidents in Botswana which are related to the spillover of economic refugees from Zimbabwe.

- Many Batswana and South Africans commented that although **consultation is one of the founding principles that ensures Botswana's political stability**, in reality this often translates into vacillation and a lack of decisive and quick action. This is reinforced by the dominance of the political space in Botswana by the Botswana Democratic Party (BDP) since independence. Although the uninterrupted rule of one party has also led to the development of a strong and vigorous opposition within the party itself, concerns were raised during the course of the survey that one-party dominance could have a negative impact on policy-making in the longer term.
- Related to the above, **a substantial proportion of society rely on the largesse of the Botswana government**. The country's social welfare policies, especially with regard to free education and subsidised housing, are becoming increasingly unsustainable. In recent years, the country has also experienced 'qualified' unemployment. Efforts to develop entrepreneurs through various assistance policies have been highly controversial, although the government's intentions are sound.
- A **key challenge for government policy is the diversification of the economy**. The Botswana government faces many obstacles in this regard. A number of these are external, and therefore difficult to manage at a domestic level. This study highlights some of the problems that the government has to overcome.
- However, **Botswana deserves credit for the development of an integrated, long-term vision for its society and its economy**. The government has not shirked its task of

identifying the many problems and challenges facing its society in a transparent and open manner and has flagged the diversification of its economy as a key objective.

- As in the case in other countries in the SADC region, the **dominance of South African business in Botswana** (especially in the highly visible sectors) **is very apparent**. Some companies that have been in the country since the 1960s are now considered Botswana businesses; however, many of the newcomers are strongly associated with South Africa. Careful management of local sensitivities, combined with good corporate practice, is required to ensure the positive reception of South African investors in Botswana, as it is in the other countries on the continent in which South Africa has business interests.

Introduction

'Diamonds are not forever...' was a constant refrain that echoed throughout the majority of the interviews conducted during this study. Interestingly, both the private and public sector held this view.[1] Botswana has made remarkable strides since attaining its independence on 30 September 1966, to establish a solid economic foundation for the creation of Africa's first welfare state.[2] The prudent management of its primary resource, diamonds, has led to the growth of a stable, highly educated and prosperous society. The country's current middle-income status contrasts with its extremely low level of economic development at independence. Today Botswana has the highest per capita income levels in sub-Saharan Africa, and has achieved AA ratings from Standard and Poor's (S&P) and Moody's Investors Service. It is the only country in Africa that has managed this feat.

However, Botswana, like many other countries that are reliant on one or two resources or commodities for the majority of their revenues, exports and economic growth, has found it extremely difficult to wean its economy from its reliance on diamonds. Unlike Sierra Leone and Angola, Botswana's wise use of its resources places it in a uniquely advantageous

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1 This is a refreshing perspective, and an acknowledgement that Botswana cannot afford the luxury of relying on only one commodity to bolster its long-term economic performance, as many states in Africa have done.

2 The term 'welfare state' references the contemporary social protection European model where the state accepts responsibility for the provision of comprehensive and universal welfare to all its citizens within the boundaries of affordability. Botswana certainly represents a first in Africa in the manner in which the government has targeted and implemented service delivery and opportunity to the marginalised and less privileged in its society.

position to address the diversification of its economy. However, this will not happen without some painful adjustments.

On the positive side, Botswana has the advantage of strong, stable economic growth combined with the circumspect management of its economy; political stability; low corruption; a highly educated population in African terms; and investor-friendly policies.

On the negative side, Botswana is facing the scourge of HIV/Aids; a small and possibly dwindling population; adverse climatic conditions; high poverty levels among certain sections of its society (particularly in the rural areas, and especially in the western districts of Ghanzi and Kgalagadi); the complacency and dependency on government of a large segment of the population; and a somewhat insular vision within this group of the challenges that Botswana faces.

The Botswana government presented a budget deficit for the first time in 1998/99, after 16 years of operating a budget surplus.[3] This sparked alarm in a society that has traditionally managed its economic situation with minimum disruption of its economic growth. However, it also gave renewed urgency to the debate about how a small, landlocked country such as itself should be addressing the many challenges that it faces.

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[3] A deficit of P1,388 million was recorded for the budget in 1998/99, compared with the originally projected surplus of P279 million. This was the result of the adverse effects of the Asian crisis on government revenue and an increase in the public sector wage bill. The last budget deficit recorded before 1998/9 was P21 million (2.16% of GDP) in 1982/83. See *National Development Plan 9* (NDP9) (2003/04-2008/9), Ministry of Finance and Development Planning, Government Printer, Gaborone, March 2003, p.36.

Overview of the Socio-Economic Environment

Botswana is situated in the interior of Southern Africa, and is completely surrounded by its neighbours: Namibia, Zambia, Zimbabwe and South Africa. It is a large country with a surface area of 582 000 square kilometres, comparable to France or Texas, and with a small population of about 1.7 million.[4] Because the Kalahari desert covers 80% of its territory, the majority of Botswana's population are settled in the east and southeast of the country, the highest rainfall catchment areas. However, even in these parts the rainfall is highly irregular, and long spells of drought are common throughout the country. This has a significant impact on the country's ability to develop its rural and commercial agriculture. As a result, Botswana is a highly urbanised society: over 50% of its population live in cities.[5]

As is often the case in developing countries, almost 12% of the entire population live in the capital city. However, unlike most African cities, Gaborone has a well-developed road infrastructure and has invested substantially in the planning of its layout. The overcrowding that is associated with many of Africa's fast-growing urban areas is absent. This is explained by its low figure of approximately 200 000 inhabitants — if those living in the surrounding areas are included. Gaborone is also the economic heartland of Botswana. Other large towns are Francistown, Lobatse and Selebi-Phikwe, with populations of 105 000; 60 000 and 50 000 respectively. The age demographic

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4 The 2001 Population and Housing Census yielded a population count of 1 680 863, according to the NDP9. *Ibid.*, p.9.

5 Urbanisation in Botswana increased from 45.7% in 1991 to 54.2% in 2001. *Ibid.*, p.19.

is weighted heavily towards the younger age groups: about 43% of the population are less than 15 years old.[6]

Although Botswana's demographic profile carries the imprint common to a developing society, the country differs in two important instances from its neighbours in the rest of Africa.

- First, Botswana has enjoyed consistently high economic growth since its independence in 1966.
- Second, this prosperity has been accompanied by remarkable political and social stability.

The political situation

Many observers believe that Botswana's strong economic performance is founded on the political stability that has been created though its reliance on customary village assemblies, which echo the Swiss canton system. The tradition of consultation and consensus-building that is vested in this practice has enabled Botswana to modernise its political system in a way that retains a broad sense of national unity and has provided civilian leadership that is far-sighted and consistent. Today, its parliamentary system is based on a marriage of the Westminster model and traditional Tswana governance practices such as the *kgotla*.[7] A House of Chiefs, modelled on the British House of Lords, represents the

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6 *'Investing in Botswana'*, published by the Commonwealth Business Council and Botswana Export Development and Investment Authority, London, 2003, p.11.

7 The *kgotla* (traditional meeting place) is an important avenue for reaching the people and has traditionally been used as a forum for public discussion. See Osei-Hwedie, B & D Sebudubudu, *Strengthening parliamentary democracy in SADC countries: Botswana Country Report*, SAIIA, 2005, p.2.

paramount chiefs and advises the government on issues related to customary law or tribal issues, for example matters related to property ownership in connection with tribal land.[8] The National Assembly is similar to the British parliament,[9] although it is headed by an executive president who also leads the government.

The country has had a flourishing multi-party democracy since 1966, although its political life has been dominated by

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8 The House of Chiefs is composed of 15 members representing the chiefs of the 'principal' eight tribes, four elected members for a term of five years, and three members specially elected by the first two groups. Reform of the House of Chiefs is currently underway due to complaints by the non-Setswana groups that the constitution is biased towards the eight 'principal' Setswana-speaking tribes, the Bamangwato, Batawana, Bakgetla, Bakwena, Bangwaketse, Bamalete, Barolong and Batlokwa. See www.gov.bw and 'Minority ethnic groups feel new bill still discriminates', *IRIN-News*, 13 April 2005.

9 However, female representation in parliament is still relatively low. There are various reasons for this state of affairs. Botswana is still predominately a patriarchal society. For example, even though women have the right to participate in discussions at *kgotla* meetings, many 'still feel that they do not have the right to speak.' Customary law (succession, inheritance, marriage) under Botswana's eight 'principal' Setswana-speaking groups is patriarchal, whereas only minor groups such as the Wayeyi, some Basarwa and Herero groups are matrilineal. In addition, Botswana's use of a 'first past the post' electoral system, rather than a party list system, has contributed to their fairly low representation in parliament (only 17%), well below the SADC quota, which was that females should make up 30% of MPs in parliaments throughout the region by 2005. None of Botswana's parties have quotas for women. However, this is slowly changing. A number of women have indicated that they will be contesting senior posts within the party hierarchies of the different Botswana parties during upcoming party elections. See *Ibid.*, Osei-Hwedie *op.cit.*, p.24, 'Women must take up the challenge' and 'Women Vie for Top Party Posts', *Mmegi/The Reporter*, 18 April 2005.

the BDP. This party, founded by Sir Seretse Khama, the first president of independent Botswana, has won every election since 1966. However, in contrast to national polls in other resource-rich countries like Nigeria, the Democratic Republic of Congo and Sierra Leone, each of the elections in Botswana has been contested freely and fairly, and has been held on schedule.

The government has traditionally enjoyed an absolute majority in parliament. It reasserted this dominance in the most recent general elections on 30 October 2004, when it won 44 seats out of a total of 57. Indeed it managed to consolidate its position, having secured only 27 seats in 1994. The weakness of the opposition has been accentuated by defections from the Botswana National Front (BFN) in order to establish new parties, which has fractured the main opposition party and split the votes of their constituents.[10] This meant that the BDP won constituencies even in areas where the BFN and the Botswana Congress Party (BCP) together had won the majority of the votes. Following the outcome of the election, political observers such as Professor Mpho Molomo remarked that the only option open to the opposition parties would be to unite in order to make more gains in the next election. He argued that there are no fundamental differences between these parties, as both follow

Botswana has had a flourishing multi-party democracy since 1966.

[10] Not only are the opposition parties divided, but the ruling party has been very effective in incorporating into its own plans the party agendas of the opposition and responding to legitimate opposition concerns. For example, when the opposition parties demanded that the voting age be reduced from 21 years to 18 years, the ruling party acceded to the request.

a social democratic agenda, with an emphasis on poverty alleviation and higher employment.[11]

One-party dominance in Botswana has led to the development of a strong back bench and vigorous opposition within the party. However, there is general agreement that the continued domination of the political scene by one party does not bode well for the entrenchment of democracy, despite the consistent quality of leadership in the party and its positive impact on political stability. In October 1997, Botswana held its first referendum on constitutional reform, introducing a wide range of new regulations in response to disaffection within the BDP and calls for reform by the BNF.[12] They included:

- lowering the voting age to 18;
- introducing an independent electoral commission; and
- making provision for citizens working or living abroad to vote.

More important, parliament adopted a new constitutional rule following the referendum which limited the period that a president may serve in office to two terms of five years each,[13]

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11 See '*Botswana needs strong opposition*', BOPA, 2 November 2004.

12 See EIU, *Botswana Country Profile 1998-99*, p.7.

13 This is widely viewed (with some exceptions) as a positive political development, especially because Botswana's political life is strongly dominated by one party. President Ketumile Masire, the predecessor of the current incumbent, President Festus Mogae, was in office for 18 years. However, in a presentation titled 'Presidential Succession in Botswana: No Model for Africa', Professor Kenneth Good, a lecturer at the University of Botswana, was highly critical of the possibility that the president might hand over power to the vice-president without elections and 'against the will of the people'. (Technically, President Mogae's term of office will run out before elections are due, because of the limited term ruling and the fact that he took over from his predecessor before elections were held.) Professor's Good's views on this and other issues have sparked controversy, especially after the

and made provision for the automatic accession of the vice-president in the case of the death or retirement of the president before the next scheduled election. This emphasis on an ordered presidential succession has bolstered investor confidence in the country.

The current vice-president, Lt-Gen Seretse Khama Ian Khama, is expected to accede to the presidency in five years. The former vice-president, Festus Mogae, took over from President Ketumile Masire when the latter stepped down in 1998, following division within the party.

Table 1: Representation of political parties in parliament

	1989		1994	
	Seats	*% of vote*	*Seats*	*% of vote*
Elected seats				
Botswana Democratic Party (BDP)	31	75%	27	54%
Botswana National Front (BNF)	3	15%	13	37%
Botswana People's Party (BPP)	0	5%	0	5%
Botswana Congress Party (BCP)	-	-	-	-
Other	0	5%	0	4%
Nominated seats				
Botswana Democratic Party (BDP)	4	0	4	0
Total	38	100%	44	100%

Botswana government ordered the deportation of the academic under the National Security Act without offering reasons for this decision. He is contesting the order and was seeking redress through the courts at the time of writing. See 'Defamation suit added to Good's deportation woes', *Business Day*, 18 March 2005 and Wray Q, 'More than Diamonds', *Leadership*, April 2005, pp.24-25.

Table 1: Representation of political parties in parliament (continued)				
	1999		2004	
	Seats	% of vote	Seats	% of vote
Elected seats				
Botswana Democratic Party (BDP)	33	57%	44	51.7%
Botswana National Front (BNF)	6	26%	12	26.1%
Botswana People's Party (BPP)	-	-	-	1.9%
Botswana Congress Party (BCP)	1	12%	1	16.6%
Other	0	5%	-	4.7%
Nominated seats				
Botswana Democratic Party (BDP)	4	0	4	0
Total	44	100%	61	100%
Source: EIU, EISA, Electionworld and others.				

An *Executive Opinion Survey* conducted by the World Economic Forum in 2003 found that there was a high level of public trust in Botswana's political leadership. The country was ranked first out of 25 African countries and ninth out of a total of 102 countries by the Global Competitiveness Report 2003–4.[14] The survey also reported a similar level of faith in the country's public institutions, especially with regard to the independence of the judiciary. In addition, Botswana was rated second out of a total of 25 African countries as demonstrating little favouritism in the decisions of government officials (17th out of 102, according to the Global Competitiveness Report), and also second least prone to the diversion of public funds by functionaries. There also seems to be strong confidence in the effectiveness of the government's strategies to reduce poverty. (Here Botswana was ranked third

[14] See Hernández-Catá E (ed), *The Africa Competitiveness Report 2004*, World Economic Forum, Geneva, Switzerland, 2004, p.115.

out of the sample of 25 African countries.) All indicators point to significant domestic trust in the country's public institutions. Botswana was also ranked as the least corrupt country in Africa and 'cleaner' than many European and Asian countries by Transparency International in 1999 and 2000.

Political stability has been enforced by the fact that Botswana has a highly homogenous society.[15] Botswana's population comprises four main ethnic groups: Tswana (79%), Kalanga (11%), Basarwa (3%) and others (7%). The last grouping includes the Kgalagadi, white Botswana citizens and expatriates.[16] Over 90% of the population are Setswana speakers. This has meant that Botswana is not subjected to the kind of ethnic tensions that have racked so many African states. English is the other official language, and is used especially in the business world.

However, in recent years there have been serious allegations of ill-treatment of the Basarwa, the Khoisan hunter-gatherers who make up about 3% of the population. The Basarwa have historically inhabited the Kalahari Desert, but were relocated to new settlement areas in order to incorporate their traditional hunting grounds into a huge transfrontier game park. The resettlement of the roughly 2 500 residents of the Central Kalahari Game Reserve (CKGR), first mooted in 1986, has sparked local and international protest, and has threatened to tarnish the image of Botswana.[17]

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[15] Botswana is described in the 9th National Development Plan as a non-racial country that affords all its citizens equal rights. NDP9, *op. cit.*, p.1.

[16] See Seakamela S, '*Public sector governance in Botswana*', SAIIA, 2003. (unpublished paper).

[17] However, the government argues that relocation is in the best interests of the Basarwa, as it will ensure better provision of services, such as education, health and sanitation, to these previously

The country is faced with a potentially more serious destabilising threat on its northeastern border with Zimbabwe. Political unrest and deteriorating economic conditions in that country have caused an influx of Zimbabwean economic refugees, both skilled and unskilled. Many of the Zimbabweans (125 000 a month)[18] who trek to Botswana's cities, towns and mines in search of jobs enter the country illegally. Consequently, there has been an oversupply of labour which has been associated with an increase in crime, especially in the northeastern part of the country and in the major towns (particularly Francistown) and villages in close proximity to Zimbabwe. Almost 90% of farm workers in Botswana are Zimbabweans. The influx has led to an alarming growth of xenophobic incidents in Botswana. The media have filed various reports on the alleged ill-treatment of Zimbabweans in Botswana by the authorities and nationals. Tension between the two countries has also grown following the construction of a 500-kilometre-long electric fence by the Botswana government along its border with Zimbabwe, to halt the movement of animals into the country. The aim is to prevent the spread of foot-and-mouth disease (FMD).[19] Botswana suffered two serious outbreaks of FMD in 2002 and 2003.[20]

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isolated communities. A group of Basarwa is presently challenging the Botswana government in the Court of Appeal on the relocation.

18 'Zim slams "barbaric" treatment of citizens', on *www.iol.co.za*, 11 May 2004.

19 Zimbabweans have accused the Botswana government of building the 2.4 metre high fence to prevent them from entering into the country.

20 The outbreak of various diseases has been attributed to the crisis in Zimbabwe's agricultural sector following that government's fast-track land reform programme, as funding is lacking to control pests and diseases.

However, the crisis in Zimbabwe has also had a negative effect on the Botswana economy. Botswana's critically important tourism sector is highly vulnerable to regional instability. Also most of its tourism packages have been developed with a regional focus. In the past, many of these tours included visits to sites such as the Victoria Falls in Zimbabwe.

The economic situation

Botswana has enjoyed the highest average economic growth rate in the world since independence in 1966, and continues to be Africa's greatest economic success story. The country's economic growth averaged about 9% per annum from 1966–99. Not even the Asian tigers have managed to achieve these consistently high growth rates since independence. The country's economic success is based on the successful exploitation of its diamond wealth, the adoption of prudent fiscal policies, and a cautious and pragmatic foreign policy, particularly towards the European Union (EU) and South Africa, its main trading partners. The government has also relied heavily on sound external advice in devising its economic policies.

Before independence in 1966, poverty in Botswana was widespread and the economy was heavily dependent on foreign aid and subsistence agriculture. The poverty rate was reflected in the low GDP per capita of $100 per annum, low social indicators and rudimentary infrastructure. The mainstay of the Botswana economy at this time was the beef industry. The discovery of diamonds in 1969 was the catalyst that changed the economic destiny of the country. The exploitation of this commodity rapidly surpassed cattle ranching as the

country's primary source of foreign exchange, and mining became the most significant contributor to its fiscus.

Successive years of uninterrupted growth, coupled with fiscal discipline and sound management, enabled Botswana to transform itself into a middle-income country with a GDP per capita of $3,100 by 2002. The far-sighted use of the revenues gained from the exploitation of its mineral resources has allowed the government to finance substantial improvements to the social and physical infrastructure of the country, resulting in huge improvements in the general standard of living.

Table 2: Selected education statistics in Botswana

Category	*Value in 2001*
Compulsory, legally guaranteed free education	6–15 years (age group)
Expected number of years of formal schooling	11.6 years
Gross intake rate in primary education	112.3%
Duration of primary education	7 years
Gross enrolment ratio in secondary education	71.2%
Secondary education age group	13–17 years
Gross enrolment ratio in tertiary education	4.4%
Total public expenditure on education as % of total government expenditure	25.6%

Source: EFA Global Monitoring Report, 2005.

These include comprehensive health services, free education[21] (often also at tertiary level, through the availability of generous grants and scholarships) and generous housing schemes attending to the needs of the most vulnerable members of society, rightly earning Botswana the title of Africa's first welfare state. (Botswana spends just under 40% of

[21] Parents are expected to provide their children with school uniforms. Comment from BEDIA, 8 April 2005.

its total budget on social development, including education, health, food programmes, welfare, housing development and others, and its social grants reach about 40% of the population.)[22]

In the area of health, the government has been able to extend comprehensive health services to all its citizens with only nominal costs being charged at hospitals and clinics. Even though the country is sparsely populated, over 85% of the rural population live within 15 kilometres of a health facility.[23] The government has also developed very generous financial assistance schemes to assist local entrepreneurs.

However, these social development achievements come at a price that has become increasingly difficult for the Botswana government to meet without making use of its substantial foreign reserves or incurring budget deficits. Unlike other African countries, Botswana finances well over 90% of its development programmes from domestic funds, in particular from the Domestic Development Fund (DDF).

Table 3: Development expenditure under the NDP8, P million

Domestic Development Fund	External grants	External loans	Funds to be negotiated	Total development expenditure
22,189.11	417.27	767.05	1,053.47	25,934.50

Source: Ministry of Finance and Development Planning, 2003.

Donor contributions to development projects as a percentage of overall expenditure on development have

22 War veterans, destitutes, orphans and all people above the age of 65 receive grants and food parcels from the government. Interview with BOCCIM, Botswana, May 2004.

23 See *Africa Investor Magazine*, Africa Practice LTD, Enfield, United Kingdom, June 2004, p.4.

decreased substantially from 28% (1985–91), to 12% (1991–97) and to 5.5% (1997–2003).[24]

Over the period of high economic growth the government, through the careful use of its mineral resources, built up foreign reserves to the value of over $5.9 billion in 2003, translating into 27 months worth of import cover at the end of that year. At the same time it maintained a budget surplus throughout most of the 1990s without incurring any domestic debt, and only an insignificant amount of foreign debt. The country has never borrowed from the IMF.[25]

Table 4: Selected key economic and social indicators

	1997	*1998*	*1999*	*2000*	*2001*	*2002*
Total population (in million)	1.58	1.61	1.65	1.68	1.70	1.71
GDP ($ billion)	5.38	5.71	6.01	6.47	6.81	7.02
GDP growth	6.9	6.0	5.4	7.5	5.3	3.1
GNI per capita	3,260	3.290	3,020	3,040	3,170	3,010
Inflation (%)	9.0	6.5	7.7	8.6	6.6	8.1
Gross domestic investment as % of GDP	28.1	33.5	27.5	19.0	21.7	24.8
Gross domestic savings as % of GDP	43.0	39.8	38.1	40.3	39.7	38.5
Total external debt ($ million)	575	532	504	453	400	480
Foreign reserves ($ million)	5,675	5,941	6,229	6,317	5,897	5,474
Government surplus/deficit (including grants) as % of GDP	5.8	2.7	-2.1	7.5	6.3	-3.1

Source: IMF and World Bank Development Indicators, 2004.

Botswana's good economic standing has earned it the highest sovereign ratings in Africa from both Standard and

24 NDP9, *op. cit.*, p.78.

25 See Bleany M & L Lisenda, 'Monetary policy after financial liberalisation: A Central Bank reaction function for Botswana', *Credit Research Paper, No 01/17*, University of Nottingham, October 2001, p.2.

Poor's (S&P) and Moody's Investors Service (Moody's). S&P gave the country a rating of 'A' for long-term debt and Prime-1 (P-1) for short-term debt. Moody's assigned a rating of 'A2' to Botswana for its long-term foreign currency debt, a P-1 for short-term foreign currency debt and a 'A1' rating for its domestic currency debt.

Structure of the economy

Although Botswana is a market-driven economy, the government either owns or has a major stake in most big corporations in the country. This is a result of Botswana's colonial legacy. At the time of the country's independence very little economic activity took place, and the private sector was too underdeveloped to drive the economy. It was left to the state to stimulate economic growth and activity. However, the government is now gradually withdrawing from the business sector, and has indicated that all state enterprises except Debswana and the Diamond Valuing Agency will be privatised. Parastatals in the electricity, telecommunications, transportation, water, housing, agriculture and mining sectors have been commercialised to operate as private businesses, with the state as a key shareholder. In line with the government's citizen empowerment initiative, Botswana citizens aiming to purchase state enterprises are given preference over other buyers.[26] In 2000, Air Botswana was the first state-owned company to be put up for sale, but

The government is a key player in the economy.

[26] However, some analysts argue that too much attention is paid to ownership and control issues rather than the impact of privatisation on national competitiveness. See UNCTAD, *Investment Policy Review*, Geneva, 2003, No UNCTAD/ITE/IPC/Misc.10, p.62.

the transaction was not carried through, owing to unfavourable market conditions. (This is directly related to the comparatively small size of the market.)

The mining sector, in particular diamond mining, dominates economic activity and contributes about 34% of GDP, 80% of export earnings (with diamonds alone providing 75%) and 50% of government revenues.[27] The country has two large mining companies, namely Debswana, a joint venture company owned by South Africa's De Beers and the Botswana government in an equal partnership,[28] and Bamangwato Concessions Ltd (BCL), which also has substantial government equity participation. Since the early 1980s, the country has been the world's largest producer of gem diamonds, with an output that represents about 40% of total global production. Three large diamond mines have opened since the country's independence. These are:

- the Orapa diamond mine, which started production in 1971;
- the Letlhakane diamond mine, opened in 1979; and
- the Jwaneng diamond mine, which became operational in 1982.

Debswana has doubled its diamond treatment capacity at the company's Orapa mine in recent years, following the completion of the $400 million Orapa 2000 project, which increased Debswana's total annual production to 26.5 million

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27 The highest share of the mining sector's contribution to GDP was 52.6% in 1983/84, dropping to 36.5% in 2000/01. NDP9, *op. cit.*, p.27.

28 Debswana was incorporated in 1969, with an original shareholding by De Beers of 85% and by the government of 15%. This was restructured into an equal partnership in 1992.

carats.[29] This has been the biggest single capital investment in Botswana.[30] Debswana employs a total of 6 300 workers.[31]

BCL operates a copper-nickel mine at Selebi-Phikwe and a soda ash mine at Sua Pan. However, the contribution of these minerals to government revenues is insignificant, although BCL remains an important employer providing jobs for about 5 000 people in Selebi-Phikwe. The company has experienced significant financial difficulties in the past. It received support until 2000 from the EU's Sysmin fund[32] as part of the Lomé agreement, which governs aid and trade between EU and the Africa, Caribbean and Pacific (ACP) countries.[33] After significant restructuring and substantial government investment in its soda ash operations, which opened in 1991, it is now operating on a profitable basis. Coal bed methane gas has also been discovered in the northwestern part of the country in commercially viable quantities. Development of these gas fields started in early 2004.

Ecotourism is a growing industry because of the country's enlightened conservation practices and extensive nature reserves. The country has one of the world's unique ecosystems, the Okavango River Delta; the Chobe Game Reserve is home to one of the largest herds of elephants in the world; and the Central Kalahari Reserve is an authentically

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29 *Invest Africa 2004*, published by the African Business Roundtable and Nepad Business Group, London, 2003, p.79.

30 See UNCTAD, *op. cit.*, p.6.

31 See *Debswana Annual Review 2002*, Gaborone, 2002, p.2.

32 The Sysmin fund was set up by the EU to protect developing countries from fluctuations in mineral prices on world markets. The arrangement ended in 2000.

33 *BIDPA Briefing*, Botswana Institute for Development Policy Analysis, Gaborone, Second Quarter, 1999.

unspoilt wilderness. This sector contributes approximately 12% to GDP.

In contrast, agriculture accounts for a mere 3% of GDP (principally through beef exports), even though about half of the population live in rural areas and are largely dependent on subsistence crops and livestock farming. Growth of the agricultural sector is constrained by erratic rainfall and poor soils. The beef industry employs about 5 000 people,[34] and the national herd is estimated at between 2 and 3 million strong. Cattle-raising used to dominate Botswana's social and economic life before independence, and at that time contributed about 40% to GDP. The sector suffered a major setback following a severe outbreak of foot and mouth disease in 2002 and the beginning of 2003,[35] resulting in a 64% drop in beef export earnings. Corn, sorghum, millet and beans are the principal subsistence crops; and cotton, peanuts and sunflowers are the main cash crops. Despite its diminishing economic importance, the sector remains a social and cultural touchstone.

Agriculture contributes only 3% to GDP.

The manufacturing sector, which currently accounts for 5% of GDP, has been identified as a core component of the government's attempt to diversify the economy. Unfortunately manufacturing has fared rather poorly over the last 10 years: growth declined from 5.3% in 1998/99 to 0.6% in 1999/2000. A Botswana government spokesman expressed disappointment

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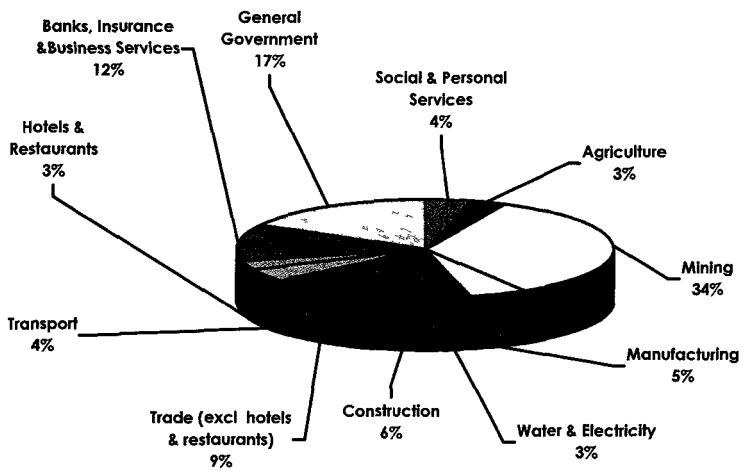
34 Gaolathe B, Minister of Finance and Development Planning, *Republic of Botswana Budget Speech*, 2004, p.13.

35 *'Vet services on high alert after anthrax outbreak in Chobe'*, Integrated Regional Information Network (IRIN) News, 21 September 2004.

at its performance, and explained that companies that had been set up in the past, had responded to the incentives offered by the government, but had developed very few linkages to the rest of the economy.[36]

Figure 1: Sectoral breakdown of GDP



Source: Bank of Botswana, Annual Report, 2003

For example, the Financial Assistance Policy (FAP), which was set up in 1982 to attract investment into small-scale consumer industries, was so generous that many foreign and domestic investors found it profitable to operate the companies for the duration of the employment subsidies, a period of five years,

[36] Interview in Botswana, May 2004.

and then to close them down once the subsidy had ceased.[37] The closure of the country's main automobile assembly plant following the liquidation of the Motor Company of Botswana (MCB) Hyundai assembly plant,[38] which occurred in the wake of the liquidation of its South African parent body, the Wheels of Africa Group of South Africa, also contributed to the decline of this sector.

A slowdown in growth since 2001?

Despite ongoing efforts to diversify the Botswana economy and to wean it from state intervention, the well-being of the country remains closely intertwined with the welfare of the mining sector. Its poor performance over the last three years has thus had a direct impact on economic growth, and has led to a gradual slowdown since 2001.[39] This is partly explained by the fact that diamond production, which received a huge boost following the expansion of the Orapa mine in 2000, has now levelled off. Output at the established mines at Jwaneng, Orapa and Lethlakane has peaked, and the development of new fields is not currently being envisaged.

Several exogenous and endogenous shocks have affected economic growth.

Other parts of the mining industry have performed erratically. Whereas the output of soda ash has increased by 20.7%, from

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[37] See UNCTAD, *op. cit.*, p.10.

[38] *African Economic Outlook 2002/2003*, Development Centre of the Organisation for Economic Co-operation and Development (OECD) and the African Development Bank, 2003, p.50.

[39] The output in the mining sector declined by 3.1% in 2001/02 compared to growth of 17.2% in the previous year.

P91.7 million in 2000/01 to P110.7 million in 2001/02, copper and nickel production contracted by 8.4%.

However, several other factors have contributed to the decline of the real growth rate in Botswana from 8.4% in 2001 to 2.3% in 2002.[40] Botswana's heavy reliance on one resource has made it vulnerable to global economic conditions. It was therefore affected by the global economic downturn that followed the terrorist attack against the World Trade Centre in September 2001.[41] Botswana's budget deficits of 3% of GDP in 2001/02 and 6% of GDP in 2002/03 coincided with a global decline in demand for diamonds.[42]

In an effort to counter the sharp price fluctuations on the international diamond market, the Diamond Trading Company (the company through which Botswana markets all its diamonds), imposed strict quotas on its sales from mid-2001. Even though Botswana built a substantial stockpile that was cleared by the end of 2002, it still sold more diamonds to world markets than any other country in the world.[43]

The depreciation of the US currency in 2003 has also had a marked effect on government finances. The level of foreign exchange reserves was P23.7 billion at the end of December 2003, a 20.7% decline from P29.9 billion in December 2002, largely reflecting the appreciation of the pula against major

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40 *Investor's guide to Botswana, op. cit.*, p.14.

41 Botswana is also vulnerable to the 'Dutch disease': a diamond-led exchange rate appreciation that could make its non-mineral exports less competitive, thus hampering diversification. See WTO, *SACU-Botswana: Trade Policy Review*, World Trade Organisation, WT/TPR/S/114/BWA, 2003. p.A1-56.

42 Invest Africa 2004, *op. cit.*, p.78.

43 Botswana is the second largest global producer of diamonds by volume after Australia, and the largest in terms of output value. See UNCTAD *op cit*, p.X.

international currencies in this year. Botswana is also affected by the exchange rate link between the pula and the rand, which has meant that any volatility in the rand against major international currencies has been transmitted to the pula. Botswana's currency is fully convertible and is valued against a basket of currencies that is heavily weighted towards the South African rand and the IMF's Special Drawing Rights (SDR).[44] This link with the rand has been a source of controversy during periods of currency volatility, and is unpopular with those who have actual or perceived interests in a stronger link to the US dollar. However, given that Botswana's main competition is from South Africa, broad national interests favour a stable and competitive exchange rate that permits domestic producers to compete against South African producers in both local and export markets. In 2000 and 2001, Botswana's international competitiveness, as measured by the real effective exchange rate, deteriorated by 4% and 7% respectively, which disadvantaged domestic producers in Botswana's import and export markets.[45] This set of constraining global and domestic events was compounded by the recurrence of foot and mouth disease in 2003, which seriously affected the beef industry. Furthermore, regional food shortages induced by drought in the region and the upheaval in the Zimbabwean agricultural sector have led to higher interest rates aimed at controlling inflation.

Botswana is also increasingly faced with the social and economic cost of HIV/Aids. This disease presents a major threat to the overall sustainability of Botswana's economy. Some estimates put the infection rate at 38.8% (the second-highest in

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[44] The SDR's value is set by the IMF as a weighted average of the US dollar, the euro, the yen and the pound sterling.

[45] See WTO *op. cit.*, p.A–56.

the world after Swaziland's). One of the most immediately visible effects of the pandemic has been on population growth.[46] According to the Central Statistical Office, the population (without Aids) could have been expected to double over 30 years, rising from 1.3 million to 2.6 million from 1991–2021 (an annual average increase of 2.8%). However, because of Aids, the Botswana Institute for Development Policy Analysis (BIDPA) estimates that the population will rise to only 1.9 million by 2021, an annual average increase of 0.9%.[47] Life expectancy at birth has also decreased dramatically, from 65.3 years in 1991 to 55.7 in 2001, and is expected to decline to 39.7 years by 2005.[48]

Table 5: HIV prevalence by age group

	1996	*1997*	*1998*	*1999*	*2000*
15–19	27.2	28.0	28.6	21.5	25.3
20–24	40.9	41.4	42.8	38.7	41.0
25–29	34.0	41.0	45.2	43.3	52.6
30–34	32.0	33.3	38.2	42.0	49.6
35–39	22.2	25.6	27.2	33.3	41.6
40–49	20.0	23.1	23.9	25.5	34.9

Source: BIDPA Briefing, March 2001.

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46 The 2001 Population and Housing Census recorded a much lower annual population increase of 2.4% over the last decade. In the 1981 census, the population growth rate was 3.6%, while the 1991 census recorded a slightly lower rate of 3.5%. See *BIDPA Briefing*, First Quarter, 2003.

47 By 2002 an estimated 138 000 Batswana had died of Aids, with 69 000 children orphaned by the epidemic. See IMF, Botswana 2003 Article IV Consultation, *IMF Country report No 04/225*, July 2004, p.4 and *BIDPA Briefing*, March 2001.

48 See NDP9, *op. cit.*, p.11 and EFA, *Global Monitoring Report (GMR) 2005: Education for All — The quality imperative*, UNESCO, Paris, 2004, p.258.

BIDPA has identified the following potential macro-economic effects that HIV/Aids is likely to have on the economy:

- a reduction in the productivity and size of the labour force as a result of the ill-health of employees or stress associated with the care of ill family members, and absenteeism due to sick leave or the need to care for sick family members;
- an increase in health spending by individuals, employers and the government, diverting funding away from other important sectors of economy;
- a rise in costs related to sick pay and high labour turnover for companies;
- an increase in spending on the training of new employees to replace sick workers; and
- a decline in the country's international competitiveness, and in the profitability of business investment in Botswana.

In addition, it is calculated that every income earner can expect an additional dependant over the next 10 years as a result of the pandemic. Thus the national income dependency ratio is expected to increase from 5.4 to 6.4. For the poorest 25% of households the predictions are that the average income earner will support eight dependants during this period.[49] The negative impact of HIV/Aids is compounded by the fact that the country is losing many of its well-trained personnel to richer countries that offer them higher salaries and better working conditions.

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[49] NDP9 *op. cit.*, p.25.

Botswana's capacity to deal with the Aids threat is hampered by the country's lack of a medical school:[50] 95% of its doctors are foreigners.[51] However, the government is taking the pandemic seriously. In 2002, Botswana launched an ambitious national campaign against Aids with the help of international donors, promising its citizens that there will be no new HIV cases by 2016, the 50th anniversary of the country's independence. As a result, the country's health expenditure has increased by 21.7% per annum, from P158 million in 1992/93 to P1,131 million in 2002/03. Observers expect that the cost of combating HIV/Aids through the provision of anti-retroviral therapy and ensuring access to health care will rise from 5% of GDP in 2003 to 10% by 2010.[52] However, some experts believe that the hidden costs of Aids have yet to reveal themselves. A decrease in growth by about one percentage point of GDP over the last five years has already been attributed by some academics to the impact of the pandemic.[53]

Botswana faces an HIV/Aids pandemic.

However, in general, overall government expenditure has increased substantially over the last decade. This is reflected in recurring deficits. For example, cumulative development expenditure, net lending and the FAP (intended to foster local entrepreneurs) were 70% higher than was initially envisaged in the government's planning. This additional demand on the fiscus has been exacerbated by adjustments in the public sector wage bill, the establishment of a Public Officers' Pension

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50 The government has flagged the establishment of a medical school in Botswana as a priority.

51 Africa Investor. June 2004, p.9.

52 See WTO *op. cit.*, p.A1–53.

53 Interview Botswana, May 2004.

Fund in 2001, the adverse international conditions already noted, the rise in oil prices and endogenous shocks such as drought and the outbreak of foot-and-mouth disease. The five-year government budget review under the 8th National Development Plan (NDP8) vividly reflects the effects these have had on government expenditure. (Note Appendix E.)

Growth projections by the government for the period 2003–09 suggest that the economy will expand by an estimated 5.5% rather than the 8% which has been identified as the minimum to eradicate absolute poverty in Botswana by 2016.[54] The government is also committed to sustainable budgeting, which implies that recurring budget expenditure has to be financed from other recurrent sources of revenue, such as income tax, VAT (at 10% the lowest in the region), customs duties or interest earnings on savings. However, over the last couple of years, the government has been forced to use its revenues from minerals (a non-renewable asset) to finance recurrent expenditure. This presents a particular challenge to the government and the private sector: to ensure growth of the economy in non-traditional sectors.[55]

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[54] Botswana uses a national average poverty datum line (PDL) of P101 per person per month, according to June 1994 prices. This translates to $37.2 per month or $1.23 per day, which is slightly higher than the internationally used rate of $1 per person per day. See NDP9, *op. cit.*, p.63.

[55] Botswana's economic growth recovered somewhat in the 2002/03 financial year, reaching 7.8%, but slowed down to 5.7% in the 2003/04 financial year owing to a downturn in the mining industry. Overall mining output was 6.9% of GDP in the 2003/04 financial year as opposed to 10.3% in the previous financial year. The Minister of Finance and Development planning announced that real GDP growth is expected to slow down further, to between 4–5% in the current and next financial year, because of slower growth in the mining and non-mining sectors. See 'Mines put damper on Botswana's growth', *Business Day*, 8 February 2005, p.5.

Diversification of the economy

Over the last 25 years, the government's pursuit of economic diversification has been a central tenet of Botswana's economic policy framework. For example, the theme of the 8th National Development Plan (NDP8) was *Sustainable Economic Diversification*. Even though some progress towards expanding the country's economic base was achieved during the NDP8, as illustrated below, the country remains heavily dependent on diamond exports.

Table 6: GDP by economic activity — Selected years

Economic activity	*1966*	*1975/76*	*1985/86*	*2000/01*
Agriculture	42.7%	20.7%	5.6%	2.6%
Mining & quarrying	-	17.5%	48.9%	36.5%
Manufacturing	5.7%	7.6%	3.9%	4.1%
Water & electricity	0.6%	2.3%	2.0%	2.4%
Construction	7.8%	12.8%	4.6%	5.8%
Trade, hotels, restaurants	9.0%	8.6%	6.3%	10.3%
Transport	4.3%	1.1%	2.5%	3.8%
Banks, insurance & services	20.1%	4.7%	6.4%	10.9%
Central government	9.8%	14.6%	12.8%	16.0%
Social & personal services	-	2.8%	2.5%	4.0%
GDP total at constant market prices (Pula million)	908.6	2,083.5	5,708.1	16,524.4
GDP excluding mining (Pula million)	908.6	1,718.1	2,917.3	10,497.1
GDP per capita (Pula)	1,682.5	2,861.9	5,175.0	9,793.4
Real GDP growth	-	18.4%	7.7%	8.4%
Real GDP growth (excluding mining)	-	11.8%	11.6%	4.0%

Source: Central Statistics Office from National Development Plan 9, 2003.

It is critical for Botswana to develop other, sustainable, sources of income. The current national development plan, the NDP9, runs for six years, from 1 April 2003 to 31 March 2009. Its theme is *Towards Realisation of Vision 2016: Sustainable and Diversified Development through Competitiveness in Global Markets*.

The private sector has been invited to become a partner of the government in the latter's endeavour to diversify the Botswana economy. A pivotal meeting held in 1988 by the private sector, represented by the Botswana Confederation of Commerce, Industry and Manpower (BOCCIM), and the president and his entire cabinet under the banner of a National Business Conference (NBC), attempted to map out how the diversification of the economy could be brought about. This 'smart partnership' was retained and strengthened by the current president, and has produced an effective platform for dialogue between the government and the private sector. BOCCIM now has a High Level Consultative Council (HLCC), which is chaired by the president and attended by all cabinet ministers, their senior officials and representatives of the private sector. They meet twice a year to review progress made since the previous NBC was held, and to make decisions on issues that are raised on a sectoral basis.[56]

This consultation process led to the adoption in 1997 of a *Long-Term Vision for Botswana: Towards Prosperity for All* known as the *Vision 2016*, which represents a blue-print of the type of society the country wishes to achieve by the year 2016.[57] The

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[56] By 1 February 2001, BOCCIM's active membership stood at 1 605 companies. See *BOCCIM at a Glance*, Botswana Confederation of Commerce, Industry and Manpower, Gaborone, 2001. p.7.

[57] *Small States in Transition–From vulnerability to competitiveness: The experience of Botswana*. Port of Spain, Trinidad & Tobago. January 2004.

National Development Plans, which are guided by Botswana's four national principles (democracy, development, self-reliance and unity), form the basis for the strategies, policies, programmes and projects directed towards achieving the goals of the *Vision 2016*.[58]

To foster new platforms for growth in sectors other than mining, the government has taken steps to broaden the production base by encouraging FDI in these alternative fields. The government hopes to bring about the expansion of the country's industrial base, which, if successful, would mean the country would rely less on imports from South Africa.

FDI outside mining is encouraged to support diversification.

Among other areas that Botswana is most actively looking to develop are those where the country has a clear comparative advantage: its tourism industry; glass and jewellery manufacturing; diamond cutting and polishing; and tannery and leather products (which are by-products of the beef industry). In addition, the country is hoping to provide greater impetus to its textile and garments industry and its information technology sector.[59]

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http://www/intracen.org/execforum/ef2004/Trinidad Tobago/TT-01-Botswana.pdf

[58] The *Vision 2016* calls for the transformation of the Batswana into a nation that is 'educated and informed; prosperous, productive and innovative; compassionate, just and caring; safe and secure; open, democratic and accountable; moral and tolerant; and united and proud'. See *NDP9*, p.12 and *Vision 2016 Towards Prosperity for All — Long Term Vision for Botswana*, Presidential Task Group for a long term vision for Botswana, Gaborone, September 1997.

[59] These sectors are being promoted through incoming and outgoing missions and marketing campaigns in targeted

The tourism sector in particular holds enormous potential, and consequently the government aims to expand its current role as a significant foreign exchange earner and creator of employment. Growth in tourism would not only assist the country's economic diversification, but could help to revitalise the declining rural economy.

The government has also given attention to the expansion of its agro-industries, manufacturing base and financial services sector.

It has also invested heavily in both land-based and cellular telecommunications[60] to achieve its goal of establishing Botswana as a global financial centre.[61]

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countries such as South Africa, the United Kingdom, Mauritius, India, Belgium and Italy. See *Annual Economic Report 2003*, Ministry of Finance and Development Planning, Government Printer, Gaborone, February 2003, p.31.

60 The telecommunications industry was first liberalised in 1997, leading to stiff competition in the sector. As a result the incumbent fixed line operator lost out on its bid to provide mobile services to two new mobile phone entrants. The liberalisation of the market also resulted in the entry of a host of internet service providers. Current planning is in the pipeline to liberalise the telecommunications market even further. Comment from BEDIA, 8 April 2005.

61 In 1999 the government looked at various examples for the establishment of the International Financial Services Centre (IFSC), and decided to opt for the onshore Ireland model rather than the offshore Mauritian model because the operation of the Dublin IFC was closer to Botswana's *Vision*, which factored in stronger linkages with the local economy. In addition, Botswana did not want to tarnish its hard-won reputation for transparency.

Box 1: Botswana Export Development and Investment Authority, BEDIA

BEDIA was established in 1997 to promote investment into Botswana, and began its operations in 1999 with a special focus on those export-oriented activities that are essential to the diversification of the economy and the creation of employment. Its operations involve both inward and outward investment missions. BEDIA has introduced a 'One-Stop Service Centre' to provide investors with ongoing support services, such as assistance in purchasing or leasing property, and obtaining both work and residence permits and licences and grants. BEDIA has two external offices, in London and Johannesburg. The office in Johannesburg opened its doors in November 2000, well before the establishment of the London office in 2003. This reflects the importance attached by Botswana to investment from South Africa.

Employment creation

The government's diversification drive is partly a response to growing unemployment in the country Despite the significance of the mining sector as a contributor to the economy, diamond mining in Botswana is highly capital intensive, and employs just over 6 000 workers Debswana is the second-largest employer in the country outside government. Increasing advances in technology and the pressure put on

companies to cut costs are expected to reduce this figure by 50% in the next decade.[62]

The state provides about 45% of all formal employment (including jobs at central/local level and within parastatals).[63]

Table 7: Breakdown of employment		
Category	***1997***	***2001***
Government share	42.2%	39.2%
Private sector share	52.0%	55.5%
Parastatal share	5.8%	6.3%
Total formal sector employment (number)	226,800	272,800
Total employment (number)	345,400*	483,400**
* Measured in 1996 ** Measured in 2000 Source: National Development Plan 9, 2003.		

Unfortunately, despite the country's strong economic growth and efficient institutions, poverty remains high in certain strata of society. Not enough jobs are created to absorb new entrants into the economy. Therefore, even though Botswana's education system is one of the best in Africa, its citizens are frequently unable to find jobs in the highly competitive formal labour market.[64] As a result much of the employment growth recorded in Botswana has been in the informal sector.

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62 The financial sector is a significant employer, accounting for about 7% of total employment. Foreign banks alone employed about 2,000 workers in 2000. See UNCTAD *op. cit.*, pp.18, 19.

63 *Invest Africa 2004, op. cit.*, p.77.

64 According to the *2003 African Economic Outlook* of the AfDB/OECD, the quality of teaching in Botswana is low, owing to the high number of untrained teachers. p.82.

Table 8: Total employment and unemployment, 1991-2001				
	Unemployed	***Employed***	***Labour force***	***Unemployment rate (%)***
1991 Census	61,265	379,938	441,293	13.9
1993/94 HIES	107,723	391,804	499,527	21.6
1995/96 LFS	94,528	345,405	439,033	21.5
1998 DS	115,703	345,405	461,108	25.1
2000 MIS	90,729	483,432	574,161	15.8
2001 Census	109,512	453,385	562,897	19.5

HIES: Household, Income and Expenditure Survey
LFS: Labour Force Survey
DS: Demographic Survey
MIS: Multiple Indicator Survey
Source: Annual Economic Report 2003, Ministry of Finance and Development Planning, p11.

To address this problem, the government has launched a series of initiatives aimed at empowering its citizens by instilling an entrepreneurial culture within the Batswana. The Citizen Economic Empowerment Policy is a key instrument of the country's National Development Programme (NDP) and comprises a set of programmes designed both to enable the Batswana to participate meaningfully in every aspect of the economy, and to benefit the broad spectrum of society in a socially just way.[65]

Following a series of recommendations made by the National Conference on Citizen Economic Empowerment in 1999, the Citizen Entrepreneurial Development Agency (CEDA) was established in August 2001 to manage both existing and new programmes for the development of citizen-owned businesses.

[65] *BIDPA Briefing*, Fourth Quarter, 2001.

Financial assistance schemes such as the FAP[66] and the Micro Credit Scheme for Small, Medium and Micro Enterprises (SMMEs), which were initiated in 1982 and originally managed by the National Development Bank, were taken over by CEDA. The Agency subsidises interest payments and provides training, monitoring and mentoring as opposed to outright grants. The two criteria required to qualify for assistance from CEDA are that the applicant has to be a Botswana citizen and be 18 years of age or older. The Agency has 12 offices country-wide, in order to make the programme widely accessible.

CEDA is not a profit-making entity, and lends at significantly reduced rates. The loans for small and micro firms start from P500 and rise to P150,000 repayable at 5% interest per annum over a five-year period. The loans for small and medium enterprises fall into the P150,001 to P2 million bracket, and are repayable at 7.5% interest per annum over a seven-year period. Although CEDA offers loans within these ranges to enterprises in all sectors of the economy, it does not provide loans for shareholding and some areas of property development.[67]

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[66] The FAP was set up in 1982 to accelerate economic diversification by addressing the financial constraints facing small and medium-sized national and foreign investors wishing to expand their activities in manufacturing and non-traditional agriculture. The policy was extended in later years to include tourism and small-scale mining. Grants were linked both to wages and the number of Botswana workers employed. The wage subsidy was very generous and began at 80% of the wages bill for unskilled labour in the first year, tapering off to 20% in the fifth and final year. The generosity of the FAP attracted many unscrupulous national (and some foreign) investors, and the scheme was abandoned in 2000. See UNCTAD *op. cit.*, pp.41, 48.

[67] The services sector received the biggest share (49.7%) of CEDA support (25.7% of which was in transport); retail (supermarkets, butcheries) received 20.14%; manufacturing (bakeries and brick

By the close of the financial year ending 31 March 2004, CEDA had received 5 882 applications for loans totalling more than P3 billion, and approved 1 137 applications valued at more than P1 million, which were expected to create 9 000 jobs throughout the country. About 545 beneficiaries and 877 promoters have received training and mentoring since the inception of CEDA.[68] The Agency has sub-contracted its mentoring activities to external consultants in the appropriate fields. Monitoring of CEDA-funded projects is done by CEDA officers, using two methods to measure the success rate. These are observing the progress of funded projects, and noting when the loan is repaid. The success rate is currently standing at 65%.[69]

In 2003, the University of Botswana undertook a study to evaluate the performance of the projects funded by CEDA in comparison with those that were not. After interviewing about 348 CEDA beneficiaries and 380 citizens who had started businesses without grants, the survey concluded that CEDA is an important catalyst for improved performance in Batswana-owned enterprises, and provide an appropriate strategy for the development of viable, stable businesses.

However, in his 2004 budget speech, the minister of finance and development planning conceded that the mentoring programme has encountered some difficulties, owing to the problem of identifying industry specialists to mentor projects. Even though CEDA is a clear improvement on the shortcomings

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making) 13.62%; agriculture (livestock breeding, diary and poultry) 10%; and property development (office blocks) 6.6%. Interview with CEDA, Gaborone, May 2004.

[68] *CEDA Annual Report 2003*, Citizen Entrepreneurial Development Agency, Gaborone, 2003. p.5.

[69] Interview with CEDA, May 2004.

of the FAP,[70] many observers, including several Botswana and South African businessmen, questioned the effectiveness of this scheme to cultivate entrepreneurship.[71]

Table 9: Total number of employees by sector, 1995 and 2001		
Sector/Economic activity	***1995***	***2001***
Agriculture	4,467	5,997
Mining and quarrying	8,408	8,252
Manufacturing	23,381	30,874
Electricity and Water	2,594	2,861
Construction	22,084	28,470
Commerce	44,944	49,904
Transport and Communications	9,006	10,120
Finance and business services	17,452	19,177
Community and personal services	10,097	4,238
Education	3,608	6,480
Central government	69,426	85,354
Local government	15,921	21,040
Total	231,387	272,812
Source: Bank of Botswana, 2001.		

70 See NDP9 for a complete overview of the shortcomings of the FAP, which included abuse of incentives and fraud related to employment generation levels. More importantly, the failures of the FAP made it clear that success in business does not rely solely on the availability of funding, but that education, the development of industrial disciplines and skills, good management and entrepreneurial skills are essential prerequisites. See NDP9, *op. cit.*, pp.123–124 and UNCTAD, *op. cit.*, p.42.

71 Also see 'BIDPA calls for scrapping of Assistance Schemes', *Mmegi/The Reporter*, 15 April 2005.

Trade and Business Linkages Between South Africa and Botswana

Botswana has traditionally adopted a cautious and pragmatic approach towards its huge neighbour. Although the country joined in the international condemnation of apartheid, its geographic and economic vulnerability deterred it from imposing economic sanctions against South Africa. Instead, the country maintained the extensive and close economic relations with South Africa that had existed even before Botswana's independence, although political relations were strained. For example in 1985 and 1986, Botswana was the subject of military incursions (ostensibly directed at ANC targets) by the South African defence force. It was only in 1992 that relations between South Africa and Botswana were formalised with the establishment of representative offices in both countries. These were upgraded to full diplomatic level on 22 June 1994.

Botswana and South Africa share a great deal more than a geographical border: there is a long and rich shared cultural and colonial history that extends to migration across the border and intermarriage. Labour migration between South Africa and its neighbours (including Botswana) dates back to the mid-19th century, when the discovery of gold and diamonds led to the development of South Africa's mining industry. Nonetheless, the number of migrant workers from Botswana has dropped quite significantly — from 16,893 in 1990 to 11,817 in 1997.[72] More recently, South Africa has also

Both countries share a rich cultural history.

[72] *http://www.sadctopcompanies.co.zw/topbotswana.html.*

emerged as a much-favoured destination for tertiary students coming from Botswana.[73] There are currently an estimated 10 000 Batswana enrolled at various South African universities, colleges, technikons and private training institutions. Many Batswana professionals have elected to live in South Africa, where they earn a good living. Their exposure to the South African business culture is ploughed back into their society when they return to their country of origin.

The cultural proximity between the two countries is amplified by the reception of South African radio broadcasts in large parts of Botswana. Until fairly recently, ordinary households could also receive the television broadcasts of the South African Broadcasting Corporation (SABC).

Air links with Botswana are well established, with a daily schedule of about 12 direct flights offered between SA Express Airways and Air Botswana.[74] Local and South African bus companies also offer daily services between Johannesburg and Gaborone. Road linkages between the two countries are well-developed. Most South Africans travelling to Botswana either do so, for business (mostly in sales, but also often in technical support services) or for tourism. At the same time there is lively cross-border traffic, mostly of Botswana citizens visiting South Africa. Many people prefer to do some of their shopping in South Africa, because of the strength of the pula in comparison with the rand. Border towns such as Mafikeng benefit from this practice, especially over the festive season.

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[73] The fees charged at South African universities are much more affordable than those in Britain or in the United States.

[74] These include the introduction of new direct flights between Cape Town and Gaborone and between Cape Town and Maun. The latter has been introduced to offer a better regional tourism package to visitors.

Although bilateral relations between the two countries are described as cordial, there is a certain amount of discomfort felt in Botswana over South Africa's dominance in the region. Most South African business people in Botswana acknowledge that the country finds it hard to maintain its economic independence from South Africa. This is related to both the interconnectedness of the two economies, and the small size of Botswana's population and economy in comparison with South Africa's.

On certain regional issues, notably Zimbabwe, Botswana has taken a somewhat different stance from that of South Africa. It has openly criticised the breakdown of law and order which has resulted in the collapse of Zimbabwe's economy and a huge influx of economic refugees into Botswana.[75] Over 1 000 illegal immigrants from Zimbabwe are repatriated weekly. The increase in illegal aliens is taxing the country's infrastructure,

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[75] This difference between the two countries was most strikingly evident in the Botswana government's statement distancing itself from a SADC communiqué condemning the continued suspension of Zimbabwe from the Commonwealth in December 2003. See *'Botswana not party to decision by some SADC members on Zimbabwe'*, Botswana Government, 15 December 2003 on *http://www.zwnews.com/print.cfm?ArticleID=8207*. However, in recent months there seems to be an apparent softening in Botswana's stance. The Botswana National Observer Mission (BNOM) declared following the 31 March Zimbabwe elections that 'the mission satisfied itself that the poll complied with the SADC principles and guidelines governing democratic elections and concluded that the elections were free and fair.' However, the mission did qualify that 'the designation of the elections as free and fair is not only contingent upon what happens on the poll day but also upon the existence of a conducive political environment in the country' and that their 'mandate was limited to observing the poll.' See *Press release of the Botswana National Observer Mission on Zimbabwe Parliamentary Election on the 31st March 2005*, Botswana Government, 8 April 2005.

which is already thinly stretched. Botswana's more critical stance on Zimbabwe is a direct result of the social and political vulnerability of its society to the threat posed by an uncontrolled influx of economic refugees.

A defining feature of the bilateral economic relationship between South Africa and Botswana has been their common membership of the Southern African Customs Union (SACU), which allows for a free flow of trade between its members. It was established in 1910 between the Union of South Africa and the British protectorates of Bechuanaland (Botswana), Basutoland (Lesotho) and Swaziland. Namibia was a *de facto* member of the agreement until it joined officially in 1992.[76] Although SACU members were and still are free to enter into other agreements either collectively or separately, all such arrangements have to comply with the provisions of the SACU agreement, which therefore determines the nature and form of Botswana's external tariff policy (and that of all the other members). Under the original SACU agreement, South Africa levied and collected most of the customs, sales and excise duties for all its members, and paid out a share to each, based on the proportion of their imports in the union.

A renegotiation of the SACU Agreement was initiated in 1994. Agreement on a draft was reached on 19 October 2001, and the final version, which included a much contested compensation arrangement, was signed on 22 October 2002 and came into force on 15 July 2004.

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[76] Namibia joined in 1992 after gaining independence. Previously, as an administered region of South Africa, it was automatically included in the SACU.

Box 2: The Southern African Customs Union (SACU)

The independence granted to Botswana and Lesotho in 1966 and Swaziland in 1968 prompted the renegotiation of the 1910 SACU Agreement in 1969. This resulted in an increase in the proportion of resources from the common revenue pool allocated to smaller members of SACU.[77] However, the effectiveness of the 1969 Agreement was hindered by a number of factors, including:

- the tariff protection of South African industries against international price competition, which had a price-raising effect on imports into Botswana, Lesotho and Swaziland (known as the BLS countries);
- the polarisation that resulted from a growth of investment mainly into South Africa, with its associated employment opportunities and tax income benefits, at the expense of the BLS countries;
- the loss of fiscal sovereignty for the BLS countries, as South Africa determined SACU's trade policy; and
- the delay in distributing revenue, especially the allocation and presentation of required documentation on imports, caused by procedural issues.

Concerns in the BLS countries about these issues gathered momentum during the 1970s. Initially all SACU members were also part of a Common Monetary Area (CMA), which provided a framework for gradual economic integration approaching that of a common market. However, the Botswana government, prompted by its Central Bank, opted to leave the CMA in 1976, as it believed that its policies were not designed with Botswana's own interests in mind, and that it failed to stimulate or contribute enough to local economic development. Since the creation of its national currency (the pula)[78] in that year, Botswana has typically maintained more liberal exchange controls than its neighbours, including South Africa. In 1999, the country abolished its exchange controls. However, Botswana's convertible currency remains closely linked to the rand.

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77 For example Botswana's customs union receipts rose from R3 million in 1967 to R50 million in 1975.

78 The name of Botswana's currency is derived from its most precious resource, water. Pula means 'rain' in Setswana.

Table 10: Major events in the history of the Common Monetary Area (CMA)	
Year/period	***Major events***
Before 1961	Informal monetary union under British rule. The pound is the common currency.
1961–74	Countries become independent (except Namibia). The rand replaces the pound as the common currency. The CMA is still an informal arrangement.
1974	South Africa, Botswana, Lesotho and Swaziland sign the Rand Monetary Area (RMA) treaty.
1976	Botswana opts out of the RMA and sets its own monetary policy. However, the pula remains linked to the rand (60–70%) through a currency basket.
1986	South Africa, Lesotho and Swaziland sign the trilateral agreement CMA, replacing the RMA. Additional provisions concerning capital account liberalisation, intrazone fund transfers and seigneorage[79] compensations are made.
1992	After independence in 1990, Namibia joins the CMA.
Source: Grandes M, Southern Africa's Monetary Area: an Optimal Currency Area? Which Costs? Which Benefits?, OECD, 23 July 2003, p.3.	

SACU's objectives are encapsulated in Article 2 of the new agreement.[80] These are:

- to facilitate the cross-border movement of goods between the territories of the member states;
- to create effective, transparent and democratic institutions which will ensure equitable trade benefits to member states;

[79] Seigneorage refers to the profit made by a government by issuing currency, especially the difference between the face value of coins and their production costs.

[80] WTO, 'Trade Policy Review: Southern African Customs Union — Report by the Governments', World Trade Organisation WT/TPR/G/114, 24 March 2004, p.8.

- to promote conditions of fair competition in the common customs area;
- to substantially increase investment opportunities in the customs union area;
- to enhance the economic development, diversification, industrialisation and competitiveness of member states;
- to promote the integration of member states into the global economy through enhanced trade and investment;
- to ensure the equitable sharing of revenue arising from customs, excise and additional duties by member states; and
- to facilitate the development of common policies and strategies.

The new agreement attempts to address the shortcomings identified in the 1969 Agreement. It is more democratic and makes provision for institutional structures that oversee the implementation of the agreement. These consist of:

- a council of ministers;
- a commission comprising senior officials from all member countries;
- a secretariat with headquarters in Namibia;
- a tribunal to resolve disputes;
- a tariff board of experts who make recommendations to the council of ministers; and
- several liaison committees.

The new agreement incorporates a revised revenue-sharing formula, which is divided into three components: customs, excise and development. The customs duty revenue is shared in proportion to members' intra-SACU imports. The excise component is distributed on the basis of each country's GDP

after a 15% deduction for development purposes has been made.[81] The development component is intended to benefit the less-developed countries within SACU. Another important feature is that South Africa will no longer be the sole custodian of the common revenue pool. Instead the location will now be determined by the Council of Ministers.

Although it has been reported that Botswana has considered leaving SACU on many occasions, the country has always been persuaded to remain in the union by the net advantages offered by its SACU membership.[82] Until recently, SACU receipts have been Botswana's second most important source of government revenue after its mining sector. However, the government's earnings from the SACU Common Revenue Pool are expected to fall in 2002/03 to P 1.541 billion, down from P1.735 billion in 2001/02 and P 2.188 billion in 2000/01. According to the World Trade Organisation (WTO), SACU revenue accounted for 15% of total government revenue in 2001/01 versus 13% in 2001/02.[83]

South Africa is also Botswana's largest trading partner on the African continent. Membership of SACU offers the latter's exports unfettered access to this important market. However, a comparison of Botswana's trade with SACU versus its trade with the rest of the world demonstrates that the customs union has had limited value in fostering greater regional integration between its members, despite the age of the agreement. This also brings forward one of the biggest challenges facing SACU

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81 *The new SACU Draft Agreement*, International trade and Economic Development Division, Department of Trade and Industry, See www.dti.gov.za.

82 Siphambe HK, *The implications of Globalisation for Foreign Direct Investment in Botswana*, Department of Economics, University of Botswana, 2003, pp.5–6.

83 WTO, *SACU–Botswana: Trade Policy Review op cit.*, p.A1–72.

members: that of developing a regional industrialisation policy. It remains to be seen whether the renegotiated SACU agreement will provide the framework for closer economic co-operation between its members.[84]

Table 11: Value of Botswana's imports and exports to SACU in comparison with the rest of the world, 2003[85]			
Botswana's imports from SACU		***Botswana's imports from the world***	
$m	*Annual growth in value, 1999–2003, %*	*$m*	*Annual growth in value, 1999–2003, %*
9,141	1%	264,819	6%
Botswana's exports to SACU		***Botswana's exports to the world***	
$m	*Annual growth in value, 1999–2003, %*	*$m*	*Annual growth in value, 1999–2003, %*
5,923	2%	1,990,329	41%
Source: International Trade Centre, www.intracen.org			

Trade

Trade figures within SACU are generally not reflected on a bilateral basis. However, from the aggregate figures that are

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84 There is little evidence in Botswana and in the region that South African companies are investing sufficiently in the manufacturing sector to ensure the growth of new southern supply chains that feed into regional production hubs and support regional industrialisation. It seems that the Japanese-inspired 'flying geese' trade and development model has not yet materialised in Africa, despite South African investment in the region. See Grobbelaar N, 'Can South African business drive regional integration?' in *South African Journal of International Affairs*, II, 2, Winter/Spring 2004, pp.101–102.

85 These figures are based on statistics provided by the Botswana government, and differ somewhat from the figures provided by Botswana's export partners. See Table 12.

available, it is clear that SACU is Botswana's largest import partner. South Africa, as the biggest economy in SACU, is therefore Botswana's largest trading partner, with trade heavily skewed in the former's favour. This is confirmed by the calculations of the International Trade Centre (ITC), based on COMTRADE data of the UNSD (see below.) However, a significant feature of Botswana's overall trade balance is that it enjoys a healthy trade surplus, in comparison with most African countries that are net importers and generally maintain an overall trade deficit. Botswana's key exports are meat products, salt, rawhides/leather, apparel, precious stones and nickel.

Table 12: Comparison of Botswana's import and export statistics with those of partner countries, 2001

Imports			*Exports*		
Country	*Value, $m*	*Number of products*	*Country*	*Value, $m*	*Number of products*
South Africa	2,978.8	1,131	UK	4,642.8	30
UK	170.0	207	South Africa	339.8	479
US	66.6	140	Norway	129.5	6
France	42.0	81	Italy	17.2	4
Italy	34.3	50	Zambia	17.2	81
Germany	18.8	99	Germany	14.3	12
China	14.7	141	US	13.0	31
Singapore	12.5	16	France	6.3	14
Japan	11.4	27	Greece	5.2	1
Belgium	8.6	33	Canada	3.6	8

Source: ITC, based on COMTRADE data of the UNSD.

Botswana depends on South Africa for most of its imports (in the past up to 80%), and for the transhipment of its beef and copper-nickel alloy exports. Moreover, Botswana is affected by

opening of trade only at second hand, to the extent that South Africa has liberalised its trade policy and, by definition, that of SACU.

Table 13: Botswana's trade partners					
Country	**1997**	**1998**	**1999**	**2000**	**2001**
Botswana's main export partners (% of total imports)					
SACU region	14.3	17.2	10.4	6.7	6.5
Zimbabwe	3.7	2.9	2.4	3.9	2.6
Other Africa	1.1	1.3	1.1	0.9	0.8
EU	79.1	77.1	84.1	87.2	89.0
US	1.0	1.0	0.7	0.6	0.2
Other	0.2	0.6	0.7	0.7	0.9
Botswana's main import partners (% of total imports)					
SACU region	72.1	74.8	76.6	73.9	77.6
Zimbabwe	4.5	3.9	3.9	3.5	3.2
Other Africa	0.5	0.6	0.3	0.3	0.3
EU	9.0	10.1	9.2	16.5	12.3
US	1.1	1.4	1.8	1.6	1.8
Other	3.0	4.4	5.6	4.0	4.5
Source: Bank of Botswana Annual Report, 2002.					

Another market that could increase Botswana's trade potential is the 13-nation Southern African Development Community (SADC),[86] the headquarters of which are in Gaborone. SADC's Trade Protocol, which was launched on 1 September 2000, calls for the elimination of all tariff and non-tariff barriers to trade among its 11 signatories by 2012. If successful, this will give Botswana companies and investors free access to a far larger regional market.

[86] Angola, Botswana, the Democratic Republic of the Congo, Lesotho, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe are members of SADC.

Investment

Botswana has actively sought foreign direct investment (FDI) since independence, and has eschewed the rampant nationalisation policies that have characterised most African countries. Instead it has opted to exploit its most precious national resource (diamonds) in joint ventures with foreign investors. This translated into significant FDI gains for the country. Botswana received a disproportionately large amount of FDI as compared with the group of least developed countries (LDCs) to which it belonged at independence. The country received consistently high FDI inflows in the 1970s, with a record of $127 million recorded in 1979. Between 1975–2000, flows based on five-year annual averages remained stable, hovering between $50 million (1981–85) and around $70 million (in 1986–90 and 1996–2000), except for the 1991–95 period, when they were negative.[87]

During the 1990s Botswana lost its pre-eminent position as a key recipient of FDI in Africa. This period did not necessarily herald a complete downturn in FDI to Botswana; rather it signified strong growth in FDI to other countries in the region, in addition to an overall slowdown in global investment flows, particularly to Africa. For example, countries such as Mozambique, Uganda and Tanzania attracted significant investments from the early 1990s. These were driven mainly by the introduction of market-orientated policies, privatisation programmes and/or generous incentive schemes for the exploitation of their natural resources[88] (see Table 15). Although the political changes in South Africa since 1994 first ushered in a period of low foreign investment, this was substantially

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[87] UNCTAD, *op. cit.*, p.4.

[88] *Ibid.*

reversed in the second half of the 1990s. A number of South African companies with investments in Botswana also returned to their home country when the sanctions ended and South Africa became integrated into the global economy.

This reorientation of FDI over the last 15 years illustrates some of the challenges faced by Botswana as it attempts to position itself as a competitive investment destination in the region.

Table 14: FDI flows to selected countries in Africa, 1989-2002 (in $)

Country	*1989–1994*	*1995*	*1996*	*1997*
Botswana	-29	70	70	100
Mozambique			72	64
Namibia	70	153	129	84
Swaziland	67	44	22	-15
South Africa	301	-	818	3,817
Zimbabwe	13	118	81	135

Table 14: FDI flows to selected countries in Africa, 1989-2002 (in $) (continued)

Country	*1998*	*1999*	*2000*	*2001*	*2002*
Botswana	90	37	54	26	37
Mozambique	235	382	139	255	406
Namibia	77	111	153	275	181
Swaziland	152	100	39	78	107
South Africa	561	1,502	888	6,789	754
Zimbabwe	444	59	23	4	26

Source: Various World Investment Reports.

Despite the downturn in FDI into Botswana, South Africa remains the country's biggest investor, accounting for more than half (52%) of total foreign investment in 2002. Many South African companies that are significant investors in Botswana have been involved in the country since well before South

Africa's transition to democracy. The most visible example is De Beers, which is also Botswana's biggest single investor. Because its subsidiary company is domiciled in Luxembourg, that country is also described as the second-largest investor in Botswana, accounting for about 32% of total FDI.[89]

Table 15: Value of investment by Botswana's main foreign investors (P million)

Country	*1997*	*1998*	*1999*	*2000*	*2001*	*2002*
South Africa	3,311	3,871	3,940	6,572	6,829	5,423
Luxemburg	1,331	2,010	2,262	2,561	3,081	3,356
United Kingdom	118	113	1,303	1,111	814	673
Germany	616	761	859	1,208	18	181
Japan	224	306	196	74	549	851*
US	448	465	226	340	385	32

* This value includes investment from all Asia-Pacific countries.
Source: Bank of Botswana, 2003.

Botswana allows foreign investment is allowed in all sectors, except in those that are reserved for small and micro enterprises. The latter include commercial activities such as retail, small general trading, petrol stations, bottle stores, butcheries, fresh produce shops, village restaurants, supermarkets (excluding chain stores), simple speciality operations (for example clothing and footwear boutiques), and taxi and security services. Also reserved are government building projects that include minor maintenance and building

[89] At the end of 2000 about 80% of FDI was in mining, followed by retail and wholesale trade (8%), finance (6%) and manufacturing (4%). Most of the FDI was from South Africa (60%), followed by Europe (37%). Luxembourg invested 25% of the latter figure. See WTO, *op. cit.*, p.A1–58.

works up to P150,000 in value; road contracts and railway maintenance (such as fencing); culvert construction; bridge painting; plant hire; and industrial activities which include bread baking and sorghum milling, and the manufacture of school furniture, uniforms, ordinary cement and bricks, and burglar-proof security bars. Foreign investors may participate in reserved activities with up to 49% equity under certain conditions.[90]

Box 3: The importance of FDI to the Botswana economy

Most of the South African companies surveyed pointed out that the economy of Botswana extremely reliant on foreign investors, who are active in every sector. However, an analysis by UNCTAD of the ratio of FDI stock to GDP in Botswana as compared with the same in other countries, did not find that the participation of foreign firms in the economy is excessive. UNCTAD argues that the ratio of 23% in 1999 is considerably lower than the average ratio in most SADC countries such as Lesotho (36%), Namibia (53%), South Africa (42%) and Zambia (74%). However, it is also significantly lower than in countries in whose economic development FDI played a significant role, such as Singapore (97%), Malaysia (65%) and Ireland (51%). The UNCTAD report admits that the Botswana figure might be an underestimate because of the number of joint ventures in the mining sector that have been excluded, but points out that the Botswana government should do more to attract FDI in view of its shortage of indigenous managerial, technical and professional skills, lack of hard and soft technology and minimal access to, and knowledge of, foreign markets.[91] FDI has also in the past played a significant role in encouraging and sustaining investment in certain industries.

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90 *Ibid.*, p.A1-66.

91 See UNCTAD, *op. cit.*, pp.1, 8, 14.

A breakdown of foreign investment by sector in 2000 by the Bank of Botswana identifies investment in mining as the leader. This is followed by investment in retail and wholesale, and finance. Both sectors have received significant investment from South African companies over the last four years.

The tourism industry is another sector to which South Africans have committed substantial amounts of capital. It is an important employer and revenue earner for Botswana, its income having grown from $117 million in 1990 to $223 million in 2000. In 1999, tourism accounted for 4–5% of GDP, even though its share of FDI was only 1.1%. This decreased further in 2000, to 0.2%. The tourism sector employed 2 630 workers in 1988, which increased to 9 900 by 1998, according to the Hotel and Tourism Association of Botswana. Most hotel lodges and hotels in Botswana's major tourism areas are foreign-owned.[92]

South Africa is also very visible in property development and construction. (See Table 16 for a breakdown of total foreign investment by sector and source in Botswana.)

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[92] These establishments also seem to cater almost exclusively for well-heeled, hard currency paying foreign visitors, especially in the Maun area. This has raised the issue of access for ordinary Botswana citizens to some of their own tourism sites. *Ibid.*, pp.9, 22, 46.

Table 16: Stock of foreign investment, by sector and source, 31 December 2000				
	FDI		*Other investment*	
	Value, P'000	*Share, %*	*Value, P'000*	*Share, %*
Investment by sector				
Mining	7,791.74	79.3	1,363.21	28.6
Manufacturing	343.49	3.5	233.69	4.9
Finance	618.92	6.3	140.59	2.9
Retail & wholesale	773.02	7.9	95.06	2.0
Electricity, gas & water	0	0	403.24	8.4
Real Estate & business services	161.15	1.6	69.62	1.5
Transport, storage and communication	105.18	1.1	130.21	2.7
Construction	15.62	0.1	25.22	0.5
Hospitality/tourism	17.37	0.2	1.26	n/a
Public administration	0	0	2,304.43	48.2
Other	0	0	15.31	0.3
Total	**9,826.49**	**100.00**	**4,781.58**	**100.0**

Table 16: Stock of foreign investment, by sector and source, 31 December 2000 (continued)				
	FDI		*Other investment*	
	Value, P'000	*Share, %*	*Value, P'000*	*Share, %*
Investment by source				
North and Central America	96.96	1.0	242.72	5.1
United States	96.95	1.0	242.72	5.1
Europe	3,627.66	36.9	1,505.79	31.4
United Kingdom	970.10	9.9	141.20	2.9
Germany	0	0	1,207.85	25.2
Luxembourg	2,478.34	25.2	82.60	1.7
Asia-Pacific	910	N/A	74.22	1.5
Africa	5,998.66	61.0	604.98	12.6
South Africa	5,982.76	60.9	588.86	12.3
Middle East	102.36	1.0	9.81	2.0
Other	0	0	2,355.12	49.1
Total	**9,826.54**	**100.0**	**4,792.99**	**100.0**

Note: Figures may not add to 100, owing to rounding.
Source: Bank of Botswana, Annual Report 2001, p.57 and WTO, 2004.

In contrast to the figures provided by the Bank of Botswana, the sixth survey conducted by the South African Reserve Bank reveals that despite the country's proximity to Botswana, South Africa's foreign assets and liabilities in Botswana are much more limited than indicated by the Botswana authorities. As at December 2001, about 6% or R1.5 billion of South Africa's total foreign assets in the rest of Africa were in Botswana.

This discrepancy may be explained by the fact that the Botswana government permits foreign firms to finance their investments in non-FDI forms such as loans from either the domestic market or international capital markets.[93]

Another reason for the discrepancy may be the small size of investments by individuals or family-owned business, which have been excluded from the Reserve Bank survey, as well as the timeframe that is covered by the survey. (See Table 17 on facing page.)

[93] Botswana's high national savings allow co-financing of FDI-sponsored investment through domestic lending — predominantly government equity. See UNCTAD *op. cit.*, pp.9, 15.

Table 17: Foreign assets of South Africa in Botswana, 31 December 2001 (R millions)			
Category	***Value***	***Sub-total***	***Total value***
Direct investment:			
Public corporations	-		
Banking sector		100	
Equity capital	84		
Reinvested earnings	16		
Private non-banking sector		308	
Equity capital	57		
Reinvested earnings	49		
Short-term capital	202		
Total direct investment			408
Portfolio investment:			
Private non-banking sector		200	
Equity securities	200		
Total portfolio investment			200
Other investment:			
Public corporations		393	
Long-term loans	393		
Short-term loans	-		
Banking sector		232	
Long-term loans	-		
Short-term loans	207		
Deposits	25		
Private non-banking sector		265	
Long-term loans	1		
Short-term loans and trade finance	264		
Total other investment			890
Total foreign assets			**1,498**
Percentage of overall foreign assets held in Africa			6%
Source: South African Reserve Bank Survey 1995–2001.			

Results of the Survey

A sample of South African companies with operations in Botswana in the mining, construction, retail, financial services, hotel, transport and property development sectors were interviewed in Botswana in April/May 2004. Many of the companies that took part in the survey by the South African Institute of International Affairs had moved into the country well before South Africa's political transition took place, attracted by both Botswana's generous incentives to foreign investors and its political stability. Several of these companies have been settled for so long in Botswana that they now consider themselves as indigenous Botswana companies, and are viewed as such by their employees, the government and their customers.

As has been noted, the bulk of South African investments are in diamond mining. Among other sectors, the most visible South African investments are in the retail and restaurant-franchise businesses, the property sector, and tourism.

All representatives or managers of South African companies interviewed confirmed that their enterprises were either the dominant player or one of the main competitors in the field. Some companies control almost 100% of the market. However, other South African, Botswana and international firms compete strongly in certain sectors.

Greenfield investments or acquisitions have dominated the way in which South African companies have ventured into the Botswana market. Very few mergers have taken place. The majority of companies interviewed have entered into joint ventures with local partners. Most companies believe that this makes good business sense (in terms of ensuring a better understanding of the business environment and providing

better services to clients). In general, over 98% of employees in South African companies are locals. They are represented at every level of management, often at chief executive officer (CEO) level.[94]

All companies interviewed indicated that the contribution of their operations in Botswana to their parent companies' earnings was very small: almost all of these companies account for less than 10% of the overall earnings of the parent company.[95]

The survey required the South African firms to rate the investment-friendliness of Botswana; their main reasons for investing in that country; the types of investment activities entered into; the main constraints facing South African companies in Botswana; and lastly, their recommendations to

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[94] Although the Botswana government does not enforce the same black economic empowerment (BEE) policies as does this country, most South African companies realise the importance of equal opportunities, and have brought local partners on board. As stated above, they also follow strong localisation principles in their employment strategies. This approach reflects the BEE requirements stipulated at head office level in South Africa. However, some South African companies that have operated as fully incorporated Botswana companies for years (predating 1994) expressed the view that there is very little knowledge of the Botswana market in South Africa and that many of the 'new' policies that are now being enforced (from South African head offices) have no relevance within the Botswana context because most of them are already standard business practice in their companies. This was a distinct difference between the firms that had entered Botswana in the early 1990s and after, and the longer established companies.

[95] Many of these companies have a presence in other parts of the world (including the rest of the African continent) and hence, the contribution of the Botswana subsidiaries to their parent companies is small.

both the Botswana and South African governments on how to improve bilateral business relations.

How investment-friendly is Botswana?

Virtually all the companies surveyed described the investment climate in Botswana as very business-friendly. The range of incentives for foreign-owned businesses, the receptiveness of government to policy input from the private sector and the fairly corruption-free environment were offered as the main reasons for this view.

Botswana offers a number of incentives to foreign investors. The country abolished foreign exchange controls in 1999; has a low corporate tax of 15% for registered manufacturing companies and companies operating within the jurisdiction of the International Financial Services Centre (IFSC); imposes no prohibitions on the foreign ownership of companies; allows dual company listings; and has traditionally maintained a moderate inflation rate. For example, in 2003 inflation was 6.4%. The maximum personal and marginal tax rate is 25%, in comparison with the regional average of 35%.[96]

All the South African companies interviewed emphasised that public–private sector relations were on a sound footing. All were members of BOCCIM, the main institutional platform for interaction between the private sector and the government. BOCCIM actively deals with a wide range of issues that might hamper business operations, and gives many South African, local and other foreign companies ready access to, and a

[96] WTO, *op. cit.*, p.A1–65.

voice with, the Botswana government.[97] The government is also very willing to engage with companies when they experience business-related problems. The appointment into senior positions in some of the larger South African companies of local representatives who are familiar with the operating environment also supports easy access to political decision-makers. Again, the relatively small size of Botswana's business sector means that business networks are fairly easy to establish.

Business networks are fairly easy to establish.

The majority of companies interviewed stated that corruption is not a major issue in Botswana when compared with the situation in other African countries where they also have operations. This is a result of Botswana's competent and relatively well-paid civil service, and the government's commitment to rooting out corruption. The Directorate of Corruption and Crime (DCC) has a mandate to investigate cases, implement preventive strategies and conduct public education programmes.[98] The lack of corruption is reinforced by strict adherence to the rule of law, respect for contracts and the protection of property rights. Although the resolution of legal disputes takes a long time, all the companies interviewed expressed strong confidence in the courts. During the survey, cases were cited in which the courts had found in favour of the

[97] A strong indication of the value of BOCCIM is that South African companies have not found it necessary to establish a South African–Botswana Business Chamber despite the number of companies involved in Botswana, illustrating the strong confidence that local institutions can deal with private sector issues.

[98] The director of the DCC reports directly to the head of state. Botswana also has an anti money-laundering policy that requires banks to share information on suspect transactions.

plaintiffs even though the respondents were connected to individuals high in the political hierarchy.

However, there were some companies (especially those that have been operating in Botswana for over 15 years) that held the opinion that even though the government does not tolerate corruption, business morals have deteriorated over the last five years. There have been instances of fidelity fraud, the fudging of books, the use of sub-standard materials, payments outside agreed contracts, and problems related to the allocation of tenders. However, even though business ethics have declined owing to internal and external influences, the business environment is still a great deal more open than in the rest of Africa and compares favourably with that of South Africa.

Some companies also commented on the ethos of the local business community, and questioned the impact on the local entrepreneurial spirit of the government's generous handouts (of land, materials and subsidised credit) to local businesses. The criticisms made were that these policies have not led to sufficient domestic investment in productive activities.

However, an important indicator of South African business confidence in Botswana was that all companies surveyed considered themselves highly committed to the country. This stance is informed by the government's dedication to good governance and maintaining the level of political stability in the country. Moreover, very few companies had found it necessary to approach the South African High Commission to assist them in dealing with problems that might threaten their operations in Botswana. This demonstrates a strong confidence in the ability of Botswana's institutions and legal framework to deal with such issues.

Main reasons for investing in Botswana and nature of investment

Companies gave a wide variety of reasons for their decision to invest in Botswana. At the top of the list were that country's political security and stable economy. The South African business community had no doubts that the BDP would win the elections on 30 October 2004 with a comfortable margin (as was also borne out by the event). However, most business people interviewed, especially Botswana nationals, emphasised the importance of the growth of a strong and active political opposition for the future prosperity and sound management of the country. It was also considered necessary to counter complacency among the political leadership. Many felt there is low political interest among the population, and that this does not bode well for the future. They also pointed to the potential for social instability arising from unemployment, especially among the growing group of young graduates.

Some companies were attracted to Botswana by the high level of disposable income (in African terms) among the population, by the successive years of strong economic growth and the lack of competition in certain industries in Botswana. Among those influenced by the last reason were companies especially in the banking and insurance sector, that followed their customers. Because of Botswana's geographical proximity to South Africa, others regarded its market as offering them opportunities both to spread their wings into other African countries and to expand their market share. The country's central position and good north–south infrastructure has enabled South African companies to use Botswana as a launching-pad for their operations and their goods into the rest

of Africa.[99] (Many South African construction companies have a presence in Botswana because of the government's emphasis on maintaining and expanding the country's infrastructure.)

Another factor that has supported the migration of South African business activity into the country (especially in the retail sector) is Botswana's membership of SACU, which assures duty-free access to businesses across the borders of both countries. As a result the cityscape of the capital, Gaborone, is strongly reminiscent of a smaller South African city such as Nelspruit. This perception is reinforced by the appearance of various South African retailers, restaurant franchises and South African-built malls over the last couple of years throughout the city, and the widespread use of English by both the business community and citizenry. (This stands in strong contrast to Mozambique, the second-largest recipient, after Mauritius, of South African investment into the rest of Africa since 1994.)

A few of the smaller companies owned by individuals cited as their reasons for moving into Botswana the uncertainty surrounding South Africa's political transition, the high incidence of crime and the tough competition they face in their home country. Botswana is considered to be a much safer environment than South Africa. Also, the Botswana government does not hesitate to act strongly against crime.[100]

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[99] The growth of Botswana's mining industry has led to the development of a relatively high standard road system, with paved highways that connect all major towns and district capitals from south to north. The recently upgraded Trans-Kalahari highway connects the country with Walvis Bay in Namibia.

[100] The death penalty, which South Africa has abolished, is still used in Botswana. The case against Maria Bosch, a South African woman who was accused of murdering her husband, resonated in South

South African companies also identified working with Botswana's labour force as a positive factor. Although some workers are unionised, the unions are not militant, and the culture of consultation that is prevalent throughout Botswana is also to be found in union–corporate relations.[101] More than one company pointed out that the mining sector is the most strongly unionised, particularly workers at Debswana.[102]

Companies generally also expressed confidence in the government's ability to manage the economy well.

The main constraints facing South African companies in Botswana

The factors that South African companies regard as bad for business in Botswana include its underdeveloped manufacturing base; its small population; the high incidence of HIV/Aids; repayment difficulties; a shortage of skilled labour; bureaucracy; a shortage of serviced land; the high cost of utilities; the unfair advantage enjoyed by some companies of Asian origin; the narrow base of raw materials; and the high transportation costs for imports and exports. The latter is attributable to Botswana's being landlocked and its distance from the nearest sea-ports. However, some of these problems, such as the limited market size, insufficient raw materials and the cost of utilities, are more severe than others (such as payment difficulties and red tape). Companies unanimously

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Africa when she was executed shortly after a high-profile trial that elicited banner headlines in the South African press.

[101] Interview with BEDIA, 24 April 2004.

[102] This perception was reinforced by the illegal strike action of about 400 workers from Debswana in 2004 and the protracted negotiations following this action.

expressed the sentiment that despite its high level of disposable income, the population is too small to make this an advantage for business.

The role of government in the economy

Contrary to expectations, companies did not mention the lack of privatisation or the dominant role the government plays as the main driver of the economy as inhibiting factors, although the latter was indirectly flagged when the cost of utilities; unfair competition from parastatals; the lack-lustre performance of the economy outside the mining sector; and the absence of an entrepreneurial spirit in Botswana were cited. For example, from June 2001–May 2002, data from the Bank of Botswana showed that the country received 65.3% of its total revenues from state-owned enterprises and property, and that government expenditure had consumed 27.2% of GDP in 2001.[103]

This reluctance on the part of South African companies to attribute the disadvantages of operating in Botswana to the government's dominance of the country's economy may be a result of their confidence in the government's prudent fiscal policies and sound management ability. However, it might also be a tacit acknowledgment of the broader debate about the need for governments of developing states to participate substantially in the economy. This perspective is perhaps also an indication of the true developmental status of Botswana despite its economic success and high growth rate.[104]

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[103] Index of Economic Freedom 2004: Establishing the link between economic freedom and prosperity, The Heritage Foundation and the *Wall Street Journal*, Washington, 2004, p.113.

[104] Some companies, especially those in the construction sector, pointed out that work in the industry is cyclical and directly related

However, there is more that the government can do to use its influence positively. The liberalisation of the essential services has not yet taken place, and Botswana does not have legislation that governs the awarding of public infrastructure concessions.[105] The government still has monopolies over fixed-line telecommunications, electricity and water supplies, sewerage services, the national airline and the railways, despite a commitment made in 1998 to privatise these institutions.[106] Although some companies readily admit that the local private sector is still too small to take over many of the roles in the economy now filled by the government and that putting certain key social services into private hands may have implications for the ability of the population to afford them, some studies have suggested that the government's dominance is crowding out the private sector.[107]

Research conducted on behalf of the Norwegian Foreign Ministry in 2000 found that the economic justification for continued government involvement in urban housing, cleaning services, food services, gardening, refuse collection and food services should be questioned.[108] The report made the case for a smaller and more efficient government because its current

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to government expenditure. Therefore any factor that decreases government revenue and thus government spending, such as losses in diamond sales or the depreciating dollar, has a direct effect on their business.

[105] *UNCTAD, op. cit.*, p.27.

[106] *EIU, op. cit.*, p.24.

[107] See Nordas KN & A Gergis, 'Making government smaller and more efficient: The Botswana case', *Evaluation Report 6/2000*, Chr Michelsen Institute and Botswana Institute of Development Policy Analysis (BIDPA) & Norwegian Foundation for Research in Economics and Business Administration, Royal Norwegian Ministry of Foreign Affairs, 2000.

[108] *Ibid.*, p.25.

expansion rate is unsustainable. According to the study, government spending in Botswana grew faster than in any other country in the world from 1965–89. In the five-year period between 1992–97, total employment increased by only about 4%, in contrast to employment growth of 22% in central government.

Market size, payment difficulties and lack of finance

All companies interviewed believed that Botswana's market size is the most significant factor inhibiting growth. This is also the main reason why South African companies are not committing more funds to their Botswana businesses or expanding their operations, despite Botswana's impressive macroeconomic performance and reportedly high disposable income of its citizens. Even a highly successful company such as Kgalagadi Breweries Ltd (KBL) (SABMiller), which is the parent company's second most profitable operation in Africa after South Africa, and contributes 7% to SABMiller's overall profits from the continent, is operating at only 75% of its capacity.[109] This poses a particular challenge to the Botswana government's hopes that the private sector will play a more prominent role in expanding the economy and hence raises questions about what an 'adequate' involvement by the state in the economy should be.

Market size is the biggest impediment to growth.

Some companies pointed out that Botswana's high disposable income figures are misleading, as there is extreme inequality between the rich and poor in the country. Twenty-four percent of the population lived in absolute poverty on an

[109] Kgalagadi Breweries Ltd (KBL) contributes 3% of GDP in taxes.

income below $1 a day in 2001. This proportion doubled to an average of 50.1% during 1990–2001 if $2 a day is taken as the base-line figure.[110] In addition, Botswana is a highly indebted society: a large proportion of disposable income is committed to the payment of life insurance, hire purchase agreements on vehicles, mortgages, and, more recently, the cost of using cellphones. As a result, people are left with limited purchasing power and high personal debt.[111]

The respondents also complained that delays in the payment of debts, even by government and government officials, occur fairly frequently.[112] Although there is generally a high respect for the rule of law and the country has a credit bureau system, it is not as effective as its counterpart in South Africa. Not only is the legal system fairly slow to process cases, but a person cannot be put on a credit blacklist before prosecution and conviction. This has prompted local banks to become very selective in issuing credit and loans. The current prime rate is 15.75%, increasing to 17–18% depending on the type of loan. Local banks, in particular commercial banks, are now favouring the middle and upper income classes, making it

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[110] See *Africa Competitiveness Report 2004*, p.112 and *EFA Global Monitoring Report 2005*, p.259.

[111] Sechaba Brewery Holdings Limited claimed in its 2003 annual report that the introduction of VAT had had a significant impact on inflation, placing many of its products beyond the reach of low-income consumers. The further announcement by government that it would freeze public sector salaries also placed consumer spending under pressure, demonstrating a lack of depth in disposable income. See Chairman's Statement, *Sechaba Brewery Holdings Limited Annual Report 2003*, Gaborone, 2003, p.5.

[112] Although most companies (big and small) interviewed in the sample group had experienced problems with payment, Batswana eventually do pay their debts, no matter how long it takes.

difficult for members of low-income groups to obtain access to financial services.

One property agent explained that banks are also far more willing to provide finance for the purchasing of motor vehicles than for buying property, as it is a great deal easier to repossess the former.[113]

Botswana remains a cash-driven economy: the use of credit cards is not common, and cards used to buy petrol on credit from petrol service stations are not used.

The shortage of skilled labour and other labour issues

The group surveyed also pointed out that the lack of skilled manpower was a setback for their businesses. This seems disingenuous given that the country spends roughly 30% of its budget on education, and has a literacy rate of 80%.

However, the education system is based on the British model, with a strong bias towards the needs of the public sector, and insufficient emphasis on technical, functional and middle management skills.

One respondent remarked that everyone in Botswana wanted to have an MBA or a doctorate. This has led to a significant mismatch between the skills acquired and the skills required by the labour market. For example, an engineering faculty was established at the University of Botswana only in 1995.

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[113] It seems that buyers of property are also expected to put down a deposit of between 17–20% of the purchasing price to qualify for banking loans, which makes it very difficult for buyers at the low end of the market to enter the property market.

Table 18: Tertiary education: Distribution of students by field of study, 2001	
Field of study	***Percentage***
Education	25.6%
Humanities and arts	22.5%
Social sciences, business and law	29.2%
Science	14.4%
Engineering, manufacturing and construction	4.2%
Agriculture	1.3%
Health and welfare	2.4%
Services	0.4%
Total number of students	8,000
Source: EFA Global Monitoring Report, 2005.	

Moreover, despite the huge investment in education and training in Botswana, the extraordinarily rapid growth of the economy and the shrinkage of the population attributable to the HIV/Aids pandemic have contributed to continuing shortages of skilled labour. Most of the respondents confirmed that this has led to low productivity levels in their companies.

Incidentally, the lowest ranking that Botswana has ever achieved on any of the global investment climate indicators is for its lack of skilled labour. The *Africa Competitiveness Survey* reported in 2001 that Botswana was ranked in 20th place out of a total of 24 African countries on the availability of suitably educated workers.[114] Increasing unemployment rates among young graduates have resulted in a dislike of foreigners (especially Zimbabweans). These xenophobic tendencies have been fed by perceptions among the Batswana that foreigners and Zimbabweans (who are well educated and prepared to take on menial tasks for low pay) are taking over their jobs.

[114] See UNCTAD *op. cit.*, p.33.

Although there is a statutory minimum wage for industry of about R500 per month that is set by the Minister of Labour, this varies from sector to sector and is much lower in agriculture[115] (see Appendix C). Whereas labour costs in Botswana are considered reasonable, some companies pointed out that these were growing. One company has paid 2% more to its general staff other than management over the last five years, in line with the minimum wage framework outlined in the *Vision 2016*, which was developed to eradicate poverty by the year 2016. The same company pays a driver P1,900 per month, in contrast to the going rate of P700.

In general, companies found that the government was receptive to their concerns in the case of labour disputes. Such problems could be sorted out fairly expeditiously through the Department of Labour.

Bureaucracy

The lack of access to skilled labour is compounded by the bureaucratic difficulties associated with obtaining work and residence permits for expatriates. According to Botswana law, a foreigner may be granted a work permit provided if no citizen is available to fill the post, and the company has a localisation plan.[116] It can take between three to seven months for foreign nationals to receive a work permit. Furthermore,

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[115] Discussion with BEDIA, 20 April 2004. In the construction industry, for example, labour costs are considered to be much lower than in South Africa. The lowest level of skilled workers are paid about P2.60 per hour, which is a statutory requirement. Minimum wages are set for the building industry, the car service and distributing sector, road transport, the hospitality and entertainment industry, manufacturing and retail and wholesale trade. *Ibid.*, p.32.

[116] Work and residence permits are awarded for 3–5 years, and may be renewed under the same conditions.

there is no differentiation between investors and employees. Government officials are often afraid to make controversial or unpopular decisions, and have therefore tended to follow the historical approach of consulting widely and extensively — often causing long delays which affect business profits. Companies believe that BEDIA has not succeeded in speeding up immigration processing, a source of considerable frustration for expatriates working in Botswana. However, cases that are deserving of 'fast-tracking' are supported by interventions from BEDIA and waivers are offered to allow some expatriate staff who are critical to operations to continue carrying out their work while awaiting their work permits.

Unfair competition

Some companies complained that the playing field is tilted in favour of companies owned by locals, particularly in the construction and property development sectors. The government plays a disproportionate role in the latter sector, and is the chief developer of office space (because of the inability of the local private sector to fill the gap). As a result, Botswana companies are awarded contracts ahead of South African firms, even if their bids are less competitive. However, it should be noted that construction firms are classified according to various grades based on company size and ownership. Although certain projects are reserved for local companies,[117] this sector is very competitive, with several

[117] Small-scale work is reserved for citizens. This includes projects valued below P350,000 for a grade OC contractor; P900,000 for a grade A contractor and P1.8m for a grade B contractor. Larger jobs are reserved for citizens or joint ventures with a majority ownership, namely grades C and D, with values up to P4m and

international firms (especially from China), other South African companies and local enterprises tendering for the same projects. Some of those interviewed believed that Chinese companies are able to quote much lower prices because they are heavily subsidised by their government. South African firms also pointed out that profit margins in infrastructure development are slim, and that despite the emphasis of the government on cost recovery measures, Build, Operate and Transfer (BOT) projects are rare.

Cost of utilities and access to land

Another frequently mentioned constraint on investment was the exorbitant cost of utilities in Botswana in comparison with those in South Africa. Botswana has the highest electricity rates of all SADC countries. The electrification charges in rural areas are particularly steep, owing to the low population density of 2.8 persons/km^2, and the expense of connections to the national grid. (Botswana is a net importer of power from Eskom, South Africa.) In addition, interviewees raised the concern that although the inflation rate has been fairly constant over the last couple of years, there seems to be a standard annual escalation of 15% for water[118] and electricity, and 10% for rentals (for both business and residential premises). For example, rent for a three-bedroom house ranges from R6,500–R7,000 per month, and about R15,000 a month for a four-

P8m each. The largest projects (grade E), to the value of over P8m, are open to foreign suppliers. See WTO, *op. cit.*, p.A1—74.

[118] Water in particular is considered a scarce resource. Its cost has escalated exponentially due to rapid urbanisation and industrialisation.

bedroom house.[119] According to some companies, the cost of utilities is a factor that contributes to the uncompetitiveness of the manufacturing industry. However, some business people also suggested that utility costs are driven up by foreigners[120] in Botswana, and that therefore this group is targeted to foot the bill.

Table 19: Comparative analysis of infrastructure services costs, late 1990s, $

	Botswana	*Mozambique*	*Namibia*	*South Africa*	*Kenya*
Air freight to Europe (per kg)	1.84	2.18	2.33	1.70	1.70
Sea freight to Europe (per 20-ft container)	2.00	1.50	1.08	1.00	1.40
Electricity (per kwh)	0.10	0.04	0.04	0.06	0.02
Water (per m3)	1.02	0.35	0.67	0.30	0.35
Telecom to EU (per minute)	4.04	3.60	1.23	2.21	4.00

Source: Namibian Investors, 1998–1999, UNCTAD *op.cit.*, p.61.

This speculation was confirmed by property agents active in Gaborone, who pointed out that the residential property market is very robust, with demand outstripping supply,

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[119] 'SA buyers boosting Botswana Market', *www.Property24.com*, 16 April 2004. See *http://ww.property24.co.za/property24news/full Article.asp?articled=1862.*

[120] In addition to South African investors, other foreigners who have taken up residence in Gaborone are linked to the SADC Secretariat. Several newcomers to the banking sector have also recently set up offices in Botswana that are linked to the International Financial Services Centre.

especially at the high end of the market which caters for foreigners. Land in Botswana is divided into three categories: tribal (71%), state (23%) and freehold (6%). The Land Boards administer the allocation of tribal and state land through the granting of leases or by converting it to freehold status. Tribal land is normally let under short-term leases or permits (less than 10 years), and state land is leased for long-term purposes (about 99 years).[121] Land regulations require that plots be developed within two years of being handed over. Despite this ruling, large areas of serviced industrial and commercial land have been left underdeveloped in recent years by property owners hoping to make a speculative profit.[122] The government has been unable to enforce its requirements and repossess the plots.[123] There now seems to be a glut in the commercial property sector following a boom in the last few years. This was spurred by foreign investors who invested in the retail sector, and leased space in many of the shopping malls that have sprung up all over Gaborone and now also in Francistown. Yet, even though retail space in Gaborone has more than trebled, rentals have not come down.

Interestingly, the constraints mentioned by South African companies doing business in Botswana bear a close resemblance to the most problematic factors identified in the Executive Opinion Survey 2003 of the World Economic Forum.

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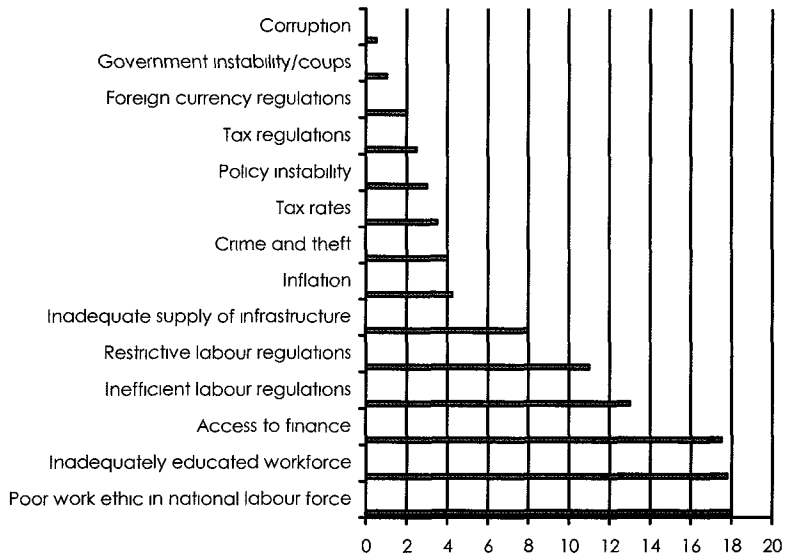
[121] UNCTAD, *op. cit.*, p.37.

[122] See Kalabamu FT & S Morolong, 'Informal land delivery processes and access to land for the poor in Greater Gaborone, Botswana', *Working Paper 3*, University of Birmingham, DFID, 2004, for a comprehensive discussion of the land issue in Botswana.

[123] In a survey that was conducted in 2002, several foreign companies stated that a group of national investors had established a monopoly on land in Gaborone for speculative purposes. *Ibid.*, p.37.

Figure 2: The most problematic factors for doing business in Botswana



Note: From a list of 14 factors, respondents were asked to select the five most problematic for doing business in their country and to rank them between 1 (most problematic) and 5. The bars in the figure show the responses weighted according to their rankings.

Source: World Economic Forum, Executive Opinion Survey, 2003.

The Impact of the South African Business Presence in Botswana

South African investors have had a considerable effect on the Botswana economy, largely through the early entry of some companies into that market and through the number of companies operating in the country. It could be argued that the prudent management of Botswana's diamonds in joint partnership with De Beers has laid the foundation for the success of the entire economy.

However, South African companies have also played an important role in other areas. Apart from contributing to the diversification of Botswana's economy, its business presence has provided much-needed employment opportunities, raised competitiveness levels in certain sectors, helped to instil a business culture and built the capacity of local people. All the companies interviewed during the survey made contributions to medical aid and pension funds for their employees, provided for severance benefits and in some cases paid gratuities to their workers at regular intervals. Some of the bigger companies had also become involved in social upliftment programmes related to causes such as road safety, SOS villages, HIV/Aids, protection of the environment and youth projects, some of them sports-related.

There is concern about the 'hegemonic' influence of South African investment.

However, there are concerns among Botswana about the 'hegemonic' influence of South African investment. These are compounded by the huge trade imbalance in South Africa's favour. Botswana exports very little to South Africa, and there are negligible domestic linkages between the two economies.

An additional cause for concern is that although the government encourages companies to buy from local producers, most of the surveyed companies admitted that they obtained a large proportion of their requirements from South Africa. In addition, those local producers used by South African companies tend to import their goods from South Africa. The reason offered by the South African companies for not buying more locally is the limited size of the manufacturing sector, which affects the capacity of local suppliers to produce cost-effectively and in the required volumes.[124] One manager in the retail sector made it clear that his company would only consider sourcing products locally if it was certain that they would be delivered on time and at the most competitive rate throughout the company's entire global supply chain.[125]

Botswana suppliers, on the other hand, complained that the South African retail sector (which is the most visible sector in Botswana, especially in the urban areas) uses the country as a market for South African products, which undermines local

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[124] A survey conducted by UNCTAD in 2002 amongst foreign investors made the same finding, reporting that foreign affiliates imported around 60% of their inputs and that there had not been a significant change in the situation over the last five years. This suggests that government policies have not achieved success in growing a larger domestic supplier base. UNCTAD *op. cit.*, p.80.

[125] In contrast Botswana's biggest investor in the mining sector, Debswana, has actively supported citizen entrepreneurship and linkages with the local economy mainly through two initiatives, its Supply Chain Management Office and Peo Holdings. Debswana's procurement policy through its supply chain office has supported local businesses significantly and its local expenditure in 2004 was about P240 million. Peo is a seed investment organisation which has assisted in stimulating the growth of SMMEs in Botswana. By the end of 2004, 43 businesses had been established. See Debswana Managing Directors Media Briefing on 18 April 2005, www.debswana.com.

manufacturing capacity. They also claimed that the buying authorities that are located at company head offices in South Africa have very little knowledge of Botswana's market conditions. As a result, there is no trade–off between the two countries; South Africa enjoys the benefit of an economy of scale relative to the size of Botswana's market. South African retailers were also accused of marking up the prices of goods, making them more expensive in Botswana than similar products on sale in South Africa.[126]

South African retailers and restaurant franchises have taken advantage of the construction of several mall complexes by South African property developers in partnership with local entrepreneurs over the last couple of the years. In each case a large South African retailer has acted as an anchor tenant, and most of the commercial space has been taken up by a mix of smaller South African retailers, restaurants and other lessees. However, there is a common belief that most of these ventures will not be sustainable owing to Botswana's relative lack of disposable income, and small market size.[127] One of the options that the Botswana government might wish to investigate is to emulate the South African tourism model, which combines game safaris with shopping safaris. However, this would entail developing a focused and flexible tourism strategy that would entice the appropriate kind of tourists to the country. At present Botswana can hardly afford the

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[126] A cursory comparison by the researchers did not find any truth in this assertion. In fact some consumer goods, clothing and especially footwear were markedly cheaper than in South Africa.

[127] There was only one Stuttafords and one Edgars outlet in Botswana in the capital city Gaborone in May 2004, an indication that there is a belief of limited purchasing power among high-income earners.

environmental impact of mass tourism on its fragile ecology, as the government already acknowledges.

Another highly visible South African business presence in the country is the rapidly increasing number of restaurant franchises, which cater for the urban youth and the upwardly mobile middle class. In contrast to investment by retailers, restaurant franchises are welcomed because they create local employment, transfer business skills (through capacity building and management training), train local chefs, and 'produce' meals some of whose ingredients are obtained locally. This in turn supports small farmers and other agricultural producers.

As stated earlier, although South Africa is the most significant investor in Botswana, investment from this country has not managed to fulfil the Botswana government's employment creation targets. Nor has it provided sufficient impetus to improve local manufacturing capacity. Thus, the Botswana government continues to face a range of challenges, especially in view of the levelling off of diamond production and the government's limited success (despite some progress) in diversifying the economy. As a result some government officials and academics have openly expressed disappointment in the quality of South African investment in Botswana, even though they recognise the importance of this investment. However, this opinion requires further scrutiny. Obviously, South African investment in mining and financial services has been critical to the well-being of the Botswana economy, and is generally regarded as positive and desirable. Similarly, investment in the tourism and construction sectors is also regarded as important. However, South African ventures into the retail sector have clearly disappointed; and this seems to have had a disproportionate impact on the way that South African investment is perceived.

Clearly, it is up to the Botswana government and local industry to invest in a more supportive framework to ensure better linkages between South African retail companies and the local manufacturing sector if it wishes to ensure that more products are bought locally. In this respect it faces many of the problems that other governments in Africa, including South Africa, encounter in finding the right balance between the role of FDI to stimulate growth in the local economy, and achieving the most desirable outcomes (employment, the transfer of skills and diversification).

Some negative effects of South African policies on Botswana's economic objectives

During the course of this research project, it became clear that many of the economic policies adopted by the South African government to address local economic imbalances, or to ensure that the country is placed on a more secure economic footing, have had unintended consequences in Botswana.[128] Some events had no direct link with interventions by South African policy-makers but are still viewed by many Batswana as having been deliberately orchestrated by the latter.

The most pertinent case in the latter category was the failure of the Hyundai Assembly plant in 2000. Despite obvious evidence to the contrary, there is still a belief in Botswana that South Africa's strong labour union movement, through its

[128] The conclusion of the South African–European Union Trade and Development Co-operation Agreement (TDCA) was widely criticised in the region. In Botswana it was felt that not enough consultation had taken place with the SACU partners, and that the agreement eroded the special concessions made to the other members of SACU.

alliance with the South African government, was not willing to accept the development of a competing motor vehicle industry in the region.[129] Many Botswana observers thus believe that the failure of the Hyundai assembly plant was a result of manipulation by the South African automobile industry in order to protect its turf. On balance, however, even though vehicle exports were the second-largest foreign exchange earner after diamonds at the time, their net contribution to the balance of payments was relatively small. The assembled vehicles had a much higher import content (about 85%) than most other exports, and the $60 million plant was essentially built to produce vehicles for the South African market from partially knocked-down components.[130] At the height of its operations the Hyundai plant employed 600 workers and produced only 7 000 units over the two-year period, compared with the break-even target of 15 000 per annum.[131] As a result, the actual effect on the economy was minimal, although the job losses following the failure of the venture and the interest arrears accruing to the Botswana Development Corporation (BDC), which had financed 50% of the construction of the assembly plant, were serious. On another level, the Hyundai example also illustrates the disadvantages of Botswana's location. Its isolation from global supply chains in combination with its landlocked situation are factors that favour South Africa rather than Botswana. It remains to be seen whether this issue will be resolved by a commitment to a common industrialisation policy under the new SACU agreement.

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[129] This view was recently reiterated by Botswana's former head of state, Sir Ketumile Masire, in the South African media. See 'Africa's elder statesmen warn South Africa: "Don't become like America", *The Saturday Star*, 12 March 2005, p.15.

[130] See UNCTAD *op. cit.*, p.21.

[131] *Ibid.*, pp 10–11.

Another example relates to the development of Botswana as an international financial centre. The International Financial Services Centre (IFSC), which had hoped to attract a large number of businesses from South Africa, suffered a major setback following the changes in taxation rules in South Africa in 2001. A key draw-card of the IFSC, which was intended to give South African companies good reason to register in Botswana, was its low corporate tax rate of 15%. However, the South African government introduced new tax regulations that required South African companies operating in foreign countries that charged a lower corporate tax rate than in South Africa to pay additional taxes[132] if that rate was less than 90% of the South African rate.[133] The new rules not only affected South African firms using the IFSC, but all companies with investments in Botswana. For example, manufacturers pay a 15% corporate tax rate in Botswana, whereas other companies pay 25%; both of these are less than 90% of the South African rate. The problem was addressed only in August 2003, when the two countries negotiated a new double taxation agreement which replaced the 1977 arrangement, in an effort to remove the fiscal obstacles to bilateral trade and investment. The new agreement also provided the necessary certainty and predictability on tax treatment for both South African and Botswana companies seeking to establish a presence in each other's territories, as companies would not

Some SA policies have unintended consequences in Botswana.

[132] At a rate equal to the difference between the foreign and the South African tax rate.

[133] *BIDPA Briefing*, Third Quarter, 2000.

be taxed again on profits that they would be repatriating to their respective countries.[134]

The interconnectedness of the two markets is also demonstrated by the impact of the exchange rate differential between them. Traditionally, a stable and competitive exchange rate has been critical to the success of Botswana's non-traditional exports and economic diversification strategy. Over the period 1989–98, exchange rate stability against the rand enabled non-traditional exports (excluding vehicles) to grow at an average rate of 15% per annum, and to become an important source of jobs.[135] However, the appreciation of the pula by more than 10% against the rand in recent years, has made it extremely difficult for Botswana producers to compete with their South African counterparts. It may also have deterred potential investors, who would prefer closer proximity to their market in any event, from setting up operations in Botswana. In 2003-04, the South African rand has appreciated sharply against the dollar. The lack of exchange rate stability in the region is a serious concern because it affects investment both in Botswana and South Africa.

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[134] Alan Boshwaen, CEO of IFSC, was quoted in *The Citizen*, 18 August 2003.

[135] *BIDPA*, Third Quarter, 1998.

Some Policy Recommendations

The representatives of South African businesses interviewed (some of whom were also Botswana nationals) identified a number of policy recommendations for the Botswana government that would support foreign investment and strengthen the business environment in that country.

- **More support should be given to BEDIA to enable it to act as a true 'one-stop service centre'.** This agency, which is tasked with assisting investors with the purchasing or leasing of property, obtaining work and residence permits, obtaining necessary licences and factory space, and obtaining other regulatory approvals, has not always been able to fulfil these tasks in a timely and comprehensive manner.
- Botswana **should acknowledge the need to appoint skilled foreign workers**, and address the provision of work permits for these workers more effectively.
- **Ways should be found to bring utility costs down**, even though foreign companies accept the government's policies to ensure cost-sharing and recovery.
- The government **should pursue open-skies agreements**, which would assist in integrating Botswana with international aviation networks and would boost business and tourism.
- **Priority should be given to employment creation**, particularly by refining skills training and by cultivating true entrepreneurs. Many South African and Botswana business people questioned the government's current efforts to create an entrepreneur class in Botswana, even though they fully support the government's empowerment drive.
- The **stigma attached to HIV/Aids should be addressed** to complement the government's existing policies to combat the spread of the disease. Most business people identified

the growing incidence of HIV infection as a national crisis that has to be factored into their business planning.

- **Increasing productivity levels** and countering the development of an entitlement culture should be made prime objectives.
- The government **should implement its privatisation plans, and design a deliberate policy to develop second-tier industries.** Too many industries in Botswana are still first-tier concerns, which are highly susceptible to negative shocks. Many foreign businesses also felt that the government should do more to level the playing field, both between government-run and private businesses and between locally and foreign-owned businesses. These inequalities interfere with the competitiveness of the economy.
- The government **should place more emphasis on the development and support of small businesses (both foreign and local) wishing to establish themselves in Botswana.**
- **Regulations (for example related to the property and banking sectors) should be strengthened.** Again, services related to the registration of businesses, especially foreign ones, should be streamlined to speed up the process. Many companies felt that regulation in their particular sectors was weak, and often well behind that of South Africa. They also claimed that many South African practices could offer useful models to Botswana.
- The government **should act more quickly on issues raised by the private sector.** All businesses represented in the survey lauded the government for its openness to the concerns of the private sector, the ease of access to all tiers of government and the generally good policies followed. However, they all complained about the lack of action

(saying that a great deal of discussion took place with very little result), and/or the slow implementation of decisions.

- **Plans should be made to exploit Botswana's many other resources (such as gas, gold and coal) more effectively**, to expand the mining sector.

Recommendations were also made to the South African government for changes that would support business co-operation between the two countries and encourage the business environment in Botswana.

- The South African government should be aware that there is **a great deal of sensitivity felt by Botswana nationals on grounds of the perceived arrogance** (mostly of individuals) **and the dominance of South Africa in the region.**[136] One Botswana businessman ventured that the ANC-led government does not seem to get on well with the BDP, despite cordial relations on the surface, and that these reservations seem to spill over into the policy environment.
- **More high-level bilateral meetings on a functional level between the two countries should be scheduled**, to address problems that might arise from the introduction of new South African economic policies.[137]

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[136] South Africa was also accused of being too dominant in the Nepad process, which made its fellow African neighbours less receptive to the concept.

[137] Some progress has been made in this regard. The first South African presidential visit to Botswana took place from 11-13 March 2003 during which an agreement was signed on the establishment of a Joint Permanent Commission for Co-operation. A first senior officials' meeting was held in 2004. In certain areas co-operation is very close, such as for example, tourism. The establishment of the Kgalagadi Transfrontier Park, the first cross-border peace park to be established in Southern Africa, was a direct result of this co-operation.

- Pretoria should look at ways to **assist Botswana to import the necessary business skills through joint education and training** programmes and education exchange agreements.
- **SADC governments should be encouraged to use contractors from the region** (South African and other) in development projects, and to offer special incentives to ensure that companies from the region do business here. (The companies interviewed pointed out that businesses from China have access to preferential loans which allow them to underprice their tenders. They often gain government contracts despite using their own imported labour, even though this is discouraged by the Botswana government.) Companies felt that even though Botswana does not qualify for overseas development assistance,[138] many of the skills that are required for development projects could be sourced from the region (especially South Africa, Zimbabwe and Namibia) rather than from abroad.
- The government **should also recommend that reputable South African companies move into the Botswana market** in partnership with local companies. This would assist in levelling the playing field in Botswana, and help to expand its economy.
- **Joint industrialisation policies should be considered**. Large manufacturing firms in South Africa could obtain some of their inputs from Botswana. However, this type of co-operation would require a closer working relationship between the governments and the private sectors. At the moment, South Africa's manufacturing base is simply too competitive and the efficiency levels too high, which has resulted in a swamping of the local market. Although there is

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[138] Botswana stopped qualifying for soft loans from the World Bank when per capita income reached P3,000.

a movement within the region towards free trade (both through the SADC Trade Protocol and other regional agreements), South Africa should show more awareness of the difficulties faced by small economies such as Botswana's.

- **Economic relations with Botswana should not be regarded as a zero-sum game**. Co-operation between South Africa and Botswana can contribute to providing a more competitive regional offering. Some Botswana companies felt that SACU should have a services component. The South African government was also accused of a contradictory policy towards the region. On the one hand, it is attempting to ring-fence South African capital, whereas on the other hand it is promoting greater economic co-operation under the Nepad umbrella. The Botswana companies interviewed emphasised that real and not nominal partnership is required, and that South African companies that wish to expand into the rest of Africa should be allowed to seek the most competitive advantages for themselves.

Lessons from Botswana

Several lessons can be drawn from the Botswana case study that are of relevance to many of Africa's small economies, especially those that are highly dependent on one commodity for their economic growth and well-being.

First, a small landlocked country such as Botswana is very vulnerable to developments in other countries within the region. On the one hand, it suffers the contagion effect of currency fluctuations in South Africa; and on the other hand, it is affected by the economic implosion in Zimbabwe. There is very little that the Botswana government can do to counter these external shocks. Also, as illustrated in this report, South African economic policies often have unintended consequences for its neighbour because of the relative size of the South African economy compared with that of Botswana, and the interconnectedness of the two economies. A closer political and economic dialogue between South Africa and its SACU neighbours (not only Botswana) could help to address these issues before they become matters for concern.

Second, despite Botswana's success in achieving strong and sustained economic growth since independence, this has not been accompanied by a significant increase in jobs. Even though the country has established a sound macro-economic environment, the micro-economic situation is much less satisfactory, with high levels of poverty and inequality. South African business people also commented that not enough investment (either foreign or domestic) is attracted into the economy's productive sectors, and faulted the government's generous financial assistance policies to local businesses for this development. They also criticised the dominant role played by government-owned businesses in the economy. It is clear that

the government will have to reassess its social policies in this new era of lower growth. It will have to adopt more cost-sharing measures with the private sector and communities.[139] Privatisation is also a key element of a more effectively-run economy. However, it remains a critical question whether the population is ready for the hard social adjustments that would be required and affordability remains an issue.

Third, it is essential that more emphasis is placed on skills creation, to support the diversification of the economy. In the short term, many of these skills can be imported from other countries in the region. Although the Botswana government is highly sensitive towards the social implications of the large-scale importation of labour, its current lack of appropriate skills presents a serious hindrance to its economic growth. Both South Africa and Zimbabwe represent important labour markets for Botswana. However, supplying the economy's need for appropriately trained workers would require both an overhaul of Botswana's migration laws and greater domestic emphasis on the development of the skills needed for the development and expansion of second- and third-tier sectors of the economy. This was also a key criticism made in the Investment Policy Review of UNCTAD in 2003, which claimed that there is a tendency in Botswana to conflate skilled immigration with illegal immigration.[140]

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[139] The government has begun this process and has recently announced the reintroduction of school fees from January 2006. The announcement sparked an outcry among opposition parties and educators. See 'Reintroduction of school fees draws mixed response', IRIN, 22 March 2005.

[140] See UNCTAD, *op. cit.*, p.18.

Fourth, the quality of foreign investment outside the mining sector in Botswana has been disappointing.[141] Botswana is faced with many of the constraints that are typical of the rest of Africa. Its economy and manufacturing sector are not integrated into global production hubs; it is landlocked; and despite a well-developed infrastructure, its market is too small to attract the scale and scope of foreign and domestic investment that it needs. Investments in the retail sector and various shopping malls have dominated over the last couple of years, but serious questions arise as to how sustainable they are in view of the country's limited market size and the consequent lack of disposable income. In addition, linkages with local suppliers are weak, despite the government's efforts to promote local business interests. Botswana has opted to develop a knowledge- and service-driven economy in the medium to longer term. This is a sound choice, but, as mentioned previously, it also entails making great demands on its society.

Fifth, Botswana has set itself the goal of reducing the number of people living in poverty to zero by the year 2016 — that is, to reach developed country status by then. However, as acknowledged in its Ninth Development Plan, **the severe impact of HIV/Aids on its society is likely to render this goal unattainable.**[142] The pandemic is also expected to severely reduce domestic savings, which will in turn cut back the growth potential of the economy. Growth of 8% per annum until 2016 is required to achieve the *Vision 2016* goals, which in turn require investment of 41% of GDP per annum to accommodate a

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[141] This opinion was expressed by government representatives who were interviewed.

[142] NDP9, *op. cit.*, p.24.

population increase of 2.1%.[143] This simply underlines the importance of attracting sufficient levels of domestic and foreign investment into the country and effectively dealing with the pandemic.

Lastly, Botswana's development of an integrated, long-term vision for its society and its economy deserves credit. The government has not shirked its task of identifying the many problems and challenges facing its society in a transparent and open manner. It has also targeted the diversification of its economy as a central goal in its planning. Although it can be faulted for the effectiveness of its implementation, it inspires confidence among foreign and local firms that Botswana has a plan, and is not relying on only one sector or commodity to drive the economy. The government's commitment is borne out by its willingness to suspend and revisit the introduction of a new foreign investment code following substantive criticism from UNCTAD in 2003 that the proposed restrictions on FDI under certain circumstances would be counterproductive.[144] Botswana also proved its ability to remain flexible in responding to the needs of foreign investors in its most strategic industry. Its announcement of a new mineral investment strategy propelled it into third (from fifth place, after Australia and Canada) in an international *Resourcestocks World Risk Survey* of the global mining industry in 2005. South Africa, in contrast, scored 21st out of a total of 25 countries.[145]

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[143] *Ibid.*, p.23.

[144] See UNCTAD *op. cit.*, p.51.

[145] Tanzania and Zambia were also ranked ahead of South Africa, in eighth and 18th place respectively. Zimbabwe was ranked last in 25th position. See 'SA near bottom of global mining risks survey', *Business Report*, The Star, 15 February 2005.

Conclusion

The positive experience of South African companies in Botswana confirms its status as one of the best-performing economies in Africa.

South African firms generally expressed strong confidence in the government's ability to manage the economy well, although they also emphasised the importance of more effective decision-making and implementation.

However, this study also highlighted, again, the sensitivities aroused in the rest of the region by the economic dominance of South Africa.

Even though South African investors have generally found that they have been welcomed with open arms, there is a strong emphasis in Botswana on partnership. The close cultural ties that bind South Africa and Botswana together and that underpin the business environment of both societies ought to be accompanied by greater complementarity in the two countries' economies.

Perhaps the new SACU agreement will institutionalise the level of political and economic dialogue necessary to support this process.

This study also highlights the future challenges facing Botswana which will seriously impact on the government's ability to provide the social network that it has developed since independence. However, the Botswana government has clearly demonstrated that it is aware of the potential pitfalls and is willing to engage with this issue in a sustainable and affordable manner.

Lastly, it is a pity that Botswana has been so reluctant to participate in the Nepad African Peer Review Mechanism

(APRM). As this study showed, many lessons can be drawn from the Botswana experience for other African states.

Much could be learnt from the Botswana government's pragmatic, structured and farsighted approach and use of six-year planning cycles to deal head-on with its economic and development challenges. One would hope that the government would revisit this decision, especially as many of the practices endorsed by Nepad are already prevalent in Botswana[146].

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[146] Dr Baledzi Gaolathe, Botswana's Minister of Finance and Development Planning said as early as the OECD Global Forum on Investment in Johannesburg in 2003 that 'we do not think that it is necessary for Botswana to join the APRM. We have nothing to hide. Our system is already beyond APRM. *eAfrica*, Volume 1, December 2003, p.2.
See also *Botswana and Nepad and the APRM: Two official perspectives*,http://www.sarpn.org.za/documents/d0000725/P823-Botswana_NEPAD_APRM.pdf.

Appendix A

Exports by major commodity and destination, 1996 and 2001				
	1996		*2001*	
Commodity	*Value, $m*	*Share, %*	*Value, $m*	*Share %*
Mining	1,745	85.7	2,047	90.1
Diamonds	1,597	78.5	1,937	85.2
Nickel/copper	125	6.1	70	3.1
Soda ash	23	1.1	40	1.8
Non-mining	291	14.3	226	9.9
Meat	85	4.2	73	3.2
Textiles	59	2.9	43	1.9
Other	147	7.2	110	4.8
Total	2,035	100.0	2,274	100.0
Destination				
SACU	372	18.3	236	10.4
Other Africa	75	3.7	80	3.5
Zimbabwe	63	3.1	54	2.4
Europe	1,564	76.7	1,925	84.7
United Kingdom	1,106	54.3	1,512	66.5
United States	19	1.0	16	0.7
Other	5	0.3	17	0.7
Total	**2,035**	**100.0**	**2,274**	**100.0**
Imports by commodity and source, 1996 and 2001				
Commodity	*Value, $m*	*Share, %*	*Value, $m*	*Share %*
Food, beverages, tobacco	294	16.9	264	14.0
Wood and paper	127	7.3	153	8.1
Textiles and footwear	129	7.4	112	5.9
Chemicals and rubber	178	10.2	176	9.3
Fuel	111	6.4	81	4.3
Metal and metal products	153	8.8	164	8.7

Imports by commodity and source, 1996 and 2001 (continued)				
	1996		*2001*	
Commodity	***Value, $m***	***Share, %***	***Value, $m***	***Share %***
Machinery and electrical equipment	280	16.1	401	21.2
Vehicles and transport equipment	245	14.1	257	13.6
Other	221	12.7	282	14.9
Total	**1,739**	**100.0**	**1,891**	**100.0**
SACU	1,356	78.0	1,448	76.6
Other Africa	107	6.1	79	4.2
Zimbabwe	100	5.7	74	3.9
Europe	118	6.8	174	9.2
United Kingdom	45	2.6	51	2.7
Republic of Korea	76	4.4	49	2.6
United States	22	1.3	35	1.8
Other	60	3.4	106	5.6
Total	**1,759**	**100.0**	**1,891**	**100.0**
Source: Botswana Authorities, WTO SACU Paper, 2004.				

Appendix B

List of some South African companies that have invested in Botswana by sector	
Financial	First National Bank, Stanbic Bank, Alexander Forbes
Retail and Wholesale	Pick 'n Pay, Game, Truworths, OK Bazaars, Woolworths, Shoprite, Edgars, Barlow, Pep
Construction	Natfranc, LTA-Griniker, Murry and Roberts
Franchises	Debonairs, Mug&Bean, Wimpy, Spur
Tourism	Sun International, SAA Express and individuals
Mining and oil	De Beers (through Debswana), Anglo, Engen
Manufacturing	First Paper House, Unitrans, Truck Africa, PG Glass, Horizon, Saatchi & Saatchi
Health	Netcare
Agriculture	Individuals

Appendix C

Minimum monthly wages in Pula					
Sector	***1998***	***1999***	***2000***	***2001***	***2002***
Building and quarrying	175	190	205	225	240
Manufacturing	175	190	205	225	240
Wholesale	165	180	205	225	240
Retail	155	170	185	205	215
Hotels and catering	175	190	205	225	240
Motor trades and transport	175	190	205	225	240
Night-watchmen	150	165	180	200	210

Please note: May data except for 1999 & 2000, which is July.
Sources: Central Statistics Office, Statistical Bulletin; Bank of Botswana, Annual Report & EIU, Botswana Country Profile, 2003.

Appendix D

Bilateral relations between South Africa and Botswana: Agreements signed	
Date	***Agreement***
27 June 1963	Agreement concerning postal services — insured parcels
27 February 1969	Extradition Treaty
24 August 1973	Boundary Agreement
24 December 1973	Labour Agreement
10 November 1977	Agreement for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to taxes and income
30 December 1991	Agreement with regard to the establishing of a Representative Office
3 March 1999	Bilateral Agreement on recognition of Kgalaladi Transfrontier Park
30 June 2000	Agreement for establishment of a Joint Permanent Commission on Defence and Security
11 March 2003	Agreement regarding the Establishment of a Joint Permanent Commission for Co-operation
16 April 2004	A revised agreement for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income
Source: South African Department of Foreign Affairs, www.dfa.gov.za.	

Appendix E

NDP8 Government budget review: Actual and estimates (P million)				
Revenues	***1997/8***	***1998/9***	***1999/00***	***2000/1***
Minerals[a]	3,627	4,041	4,829	5,912
Minerals[b]	4,681	3,187	6,687	8,368
SACU[a]	1,163	1,112	1,112	1,112
SACU[b]	1,186	1,261	1,931	2,188
BOB[a]	1,751	1,351	1,431	1,505
BOB[b]	947	1,217	1,200	1,167
Other taxes[a]	1,274	1,343	1,491	1,665
Other taxes[b]	1,467	2,012	2,145	2,392
Total revenues[a]	7,815	7,846	8,864	10,194
Total revenues[b]	8,281	7,678	11,963	14,115
NDP8 Government budget review: Actual and estimates (P million) (continued)				
Revenues	***1997/8***	***1998/9***	***1999/00***	***2000/1***
Recurrent expenditure[a]	4,652	5,179	6,060	6,885
Recurrent expenditure[b]	4,827	6,157	7,048	8,383
Development & net lending[a]	2,400	2,389	1,792	1,769
Development and net lending[b]	2,580	2,908	3,490	3,153
Total expenditure[a]	7,052	7,568	7,852	8,655
Total expenditure[b]	7,406	9,065	10,538	11,536
Surplus/deficit[a]	763	279	1,012	1,539
Surplus/deficit[b]	875	-1,388	1,426	2,579

NDP8 Government budget review: Actual and estimates (P million) (continued)				
Revenues	***2001/2***	***2002/3[c]***	***NDP8 Period***	***% share of total***
Minerals[a]	6,581	6,986	31,976	55.3%
Minerals[b]	6,996	7,040	36,959	53.7%
SACU[a]	1,112	1,112	6,723	11.6%
SACU[b]	1,732	1,554	9,852	14Z.3%
BOB[a]	1,634	1,756	9,427	16.3%
BOB[b]	1,167	1,150	6,848	9.9%
Other taxes[a]	1,851	2,066	9,690	16.8%
Other taxes[b]	2,837	4,773	15,626	22.7%
Total revenues[a]	11,178	11,920	57,816	100%
Total revenues[b]	12,707	14,426	69,170	100%
Recurrent expenditure[a]	7,756	8,740	39,273	76.7%
Recurrent expenditure[b]	9,935	11,939	48,289	70.1%
Development & net lending[a]	1,804	1,773	11,928	23.3%
Development and net lending[b]	3,698	4,502	20,331	29.5%
Total expenditure[a]	9,561	10,513	51,200	100.0%
Total expenditure[b]	13,670	16,642	68,857	100.0%
Surplus/deficit[a]	1,617	1,407	6,616	11.4%
Surplus/deficit[b]	-964	-2,216	312	0.5%

a: NDP8 Forecast
b: NDP8 Actual
c: Budget Estimate
Source: NDP8, MFDP and CSO.

Appendix F

Tax Concessions for Development Purposes (information provided by BEDIA)

Development Approval Orders (Section 52 of the Income Tax Act (CAP 52:01))

This pamphlet is issued for the guidance of entrepreneurs and other organisations who may wish to know the type of benefits which can be obtained by way of taxation relief for development purposes.

A Development Approval Order (DAO) is the means whereby the Minister responsible for finance may prescribe that a business be granted additional tax relief in respect of a project for the development of the economy of Botswana. Until 1977 little attention had been paid by the business community of Botswana to the advantages of seeking aid under such an Order, but in that year three DAO's were approved by Parliament. The Honourable Minister in presenting the applications explained that Government was prepared to forego tax revenues if there was evidence of advantages to the community to be obtained by granting additional relief to deserving enterprises. The advantages itemised were:

(a) those likely to accrue from new projects particularly in regions previously underdeveloped

(b) those to be derived from training Batswana in modern techniques

(c) those which would create job opportunities for Batswana in substantial and growing numbers

(d) those which would provide the means to enable Batswana to learn how to efficiently manage capital and labour, and

(e) those which could expand production for domestic consumption and for export.

Again in his Budget Speech of 1979 the Honourable Minister referred to the fact that the development approval order had been little used and stated that Government was most anxious that those engaged in pioneering ventures for the benefit of the national economy should take full advantage of the provision of 'tax holidays' in justifiable cases. This pamphlet therefore seeks to give publicity to the scheme and to draw the attention of appropriate persons to the provisions of Section 52 of the Income Tax Act.

Section 52 of the Act prescribes the Minister's authority to make Development Approval Orders, and for ease of reference the Section is reproduced in its entirety as an appendix to this paper.

It will be noted that every Order so made is subject to its being approved by resolution of the National Assembly. The purposes of making the Order are generally outlined in the Section as also are the points which the Minister may take into account when he considers the merits of any application he received. Five of these criteria have previously been mentioned above but it is worth emphasising that the numbers of Batswana to be employed, their training of both in skills and management techniques, the region in which the project is situated, and the progress towards localisation will weigh heavily in any decision made.

Prior to the introduction of the Income Tax Act in 1973, the tax legislation provided for "Development incentives" but such incentives were particularly directed to giving additional relief in respect of capital expenditure. It will be fairly obvious from

the evidence required as stated above that the additional tax relief under a DAO is concerned more with the growth in employment of Botswana citizens and with the establishment of labour intensive industries.

The making of an order under the present legislation does not grant exemption to qualifying enterprises from income tax, as such, but rather provides additional tax allowances in respect of expenditure which achieve the purposes of the stated objectives. However the effect of the granting of such relief may reduce the chargeable income derived from the development project to a point at which no tax is chargeable. The additional allowances would probably be related to the salaries and wages paid to Botswana citizens and training costs, including salaries and allowances paid to expatriate staff wholly engaged in the training of Batswana staff.

As a simple example, the trading account of a business considered worthy of additional relief might read as follows:-

Materials purchased	10 000	Sales	50 000
Wages	20 000		
Gross Profit	20 000		
	50 000	Gross/	50 000
Expenses	**5 000**	**Profit**	**20 000**
Net Profit	15 000		
	20 000		20 000

Assuming all the expenses were allowable for tax purposes and the business in the example was run by a company, the net profit would be chargeable to tax at 35% and the tax payable would be:-

P15 000 at 35% = P5 250

If in this instance a Development Approval Order had been made and the relief provided for an allowance of an

additional 100% of the wages paid to Botswana citizens, and the whole of the wages were in fact paid to Batswana, there would then be deducted for tax purposes an additional amount of P20 000 (twice the wage paid) and the position would be: -

Profit P15 000 – P20 000 = (P5 000) Loss

Where, however, as a result of the additional deduction allowable a profit is turned into a loss (as in the example quoted) or a loss becomes a greater loss) then such loss or greater loss cannot form part of an assessed loss for tax purposes and be carried forward into a subsequent tax year. Orders are made for agreed periods but it may be expected that a period of five (5) years would receive favourable consideration. This will allow the amount of tax saved over the period to be used for further development within the enterprises including increased employment of citizens.

It should be noted from subsections 7 to 10 of section 52 that if the performance of an organisation which is granted additional relief is not found to come up to expectations, provision is made for development approval orders to be amended or revoked.

Application for a Development Approval Order

Applications should be made, on the prescribed form to:-
The Permanent Secretary, Ministry of
Finance and Development Planning
Private Bag 008
GABORONE

The form calls for the following information:-

1. Identification of Claimant;
2. Identification of Claimant's Business;
3. Identification of Development Project for which additional Income Tax relief is sought;
4. Identification of additional relief sought the claimant can specify:

(a) Period for which additional relief is requested (normally not to exceed 5 years)

(b) Nature of expenditure (both capital and revenue) incurred or to be incurred in relation to the development

(c) Types and rates of additional relief requested in relation to expenditure in (b)

In addition an application should be supported by the following statements and documents:-

(a) A financial statement or forecast for each of the claimants accounting years for which additional income tax relief is requested;

(b) In the case of a company claimant, a copy of the Memorandum and Articles of Association;

(c) In the case of a private company particulars of the directors and shareholders showing names, addresses, nationality and individual shareholdings;

(d) In the case of a public company particulars of the directors and corporate shareholders showing names, addresses, nationality and individual shareholdings;

(e) A detailed statement as to why the development project will be beneficial to the development of the economy of Botswana. This statement must indicate the extent to which the criteria earlier mentioned in these notes will be satisfied.

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