

Botswana

Background

The discovery of diamonds soon after independence in the 1960s has helped to transform the economy from being largely underdeveloped and dependent on agriculture to a more dynamic one with the highest credit rating in Africa. Although diamond mining still dominates the economy, the share of services has risen notably in recent years. For decades, solid mining output and prudent financial management have underpinned robust economic growth and improved living conditions.

The country has an established history of peace and stability, with elections having been held regularly since independence. In the 2004 elections, as in all the previous ones, the Botswana Democratic Party retained power, with the opposition remaining divided and weak. The government has recommitted itself to diversifying the economy to create jobs and sustain the growth momentum, as the reliance on diamond mining is unsustainable and the required links between the mining industry and the rest of the economy have not developed fully. Tackling the HIV/Aids pandemic also remains a priority. Botswana has one of the highest incidences of HIV/Aids in the world, but also one of Africa's most progressive programmes for dealing with the disease.



Government

Government type:

Parliamentary republic

Capital:

Gaborone

Independence:

30 September 1966 (from UK)

Chief of state:

President Festus Mogae (since 1 April 1998)

Elections:

President elected by the National Assembly for a five-year term.

Election last held: 30 October 2004

Next election: October 2009

Source: CIA World Factbook 2004

People

Population:

2004: 1.7 million

Population growth rate:

-0.89% (2004 est)

Life expectancy at birth:

Total population: 30.76 years.

Male: 30.99 years.

Female: 30.53 years (2004 est)

Ethnic groups:

Tswana 79%, Kalanga 11%, Basarwa 3%, other 7% (including Kgalagadi and white)

Religions:

Indigenous beliefs 85%, Christian 15%

Languages:

English (official), Setswana

Adult literacy rate:

Definition: % of population aged 15 and over that can read and write.

2001: 79.8%

Source: CIA World Factbook 2003, UNDP Human Development Report 2004

Geography

Area:

Total: 600 370 sq km.

Land: 585 370 sq km.

Water: 15 000 sq km.

Land boundaries:

Total: 4 013km.

Border countries: Namibia 1 360km, South Africa 1 840km, and Zimbabwe 813km.

No coastline: landlocked

Climate:

Semi-arid with warm winters and hot summers.

Terrain:

Predominantly flat to gently rolling tableland, Kalahari Desert in southwest.

Natural resources:

Diamonds, copper, nickel, salt, soda ash, potash, coal, iron ore, silver.

Land use:

Arable land: 0.65%.

Permanent crops: 0.01%.

Other: 99.34% (2001 est)

Irrigated land:

10 sq. km (1998 est)

Natural hazards:

Periodic droughts, seasonal August winds blow from the west, carrying sand and dust across the country, which can obscure visibility.

Environment:

Overgrazing, desertification and limited fresh water resources.

Source: CIA World Factbook 2004



Health

People living with HIV/Aids:

Adults (age 15-49) 2003: 37.3%

Adults (age 15-49) 2003: 330 000

Women (age 15-49) 2003: 190 000

Children (age 0-15) 2003: 25 000

Tuberculosis cases (per 100 000 people):

2002: 338

Undernourished people (average for 1999 - 2001):

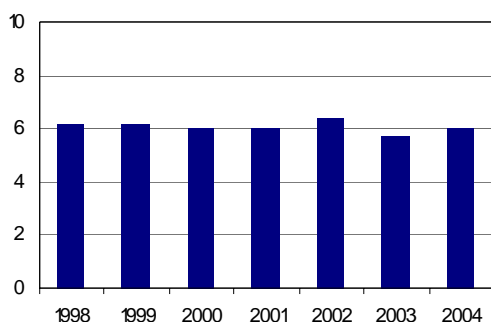
24% of population

Malaria cases (per 100 000 people)

2000: 48 704

Source: UNDP Human Development Report 2004, UNAIDS

Corruption perceptions index (2004)



Score: 6.0

(where 10 is "highly clean" and 0 is "highly corrupt").

Place: 31

146 countries surveyed, 1 = least corrupt, 133 = most corrupt).

(The surveys reflect the perceptions of business people, academics and country analysts. The surveys were undertaken over the past three years and no country has been included in the index without results from a minimum of three surveys).

Source: Transparency International

Restrictions on capital flows

- Foreign exchange controls were abolished in 1999.
- Profits, dividends and capital can be freely repatriated.

Source: Botswana Export Development & Investment Authority

Taxation

- For tax purposes, the Government of Botswana makes no distinction between production for the local market and for export.
- Companies: 15% for manufacturing and certified financial companies; 25% for the rest; tax rates on mining companies determined according to a specific formula with a range between 25% and 55%.
- Value added tax: 10%
- Capital gains tax: 25%; profits on disposal of listed shares are exempted.
- Individuals: 5% to 25%

Source: 2005 World Markets Research Centre

Sovereign credit rating

Standard & Poor's:

Local currency:

Long-term: A+ outlook: Stable

Short-term: A-1

Foreign currency:

Long-term: A outlook: Stable

Short-term: A-1

Long-term definition: "A" indicates a strong capacity to meet financial commitments. "+" indicates upper end of category. Short-term definition: "A-1" indicates strong capacity to meet financial commitments and is the highest short-term rating category offered by S&P.

Outlook definition: "Stable" indicates that the rating is unlikely to change over the next two to three years.

Moody's Investor Service:

Foreign currency debt A2/P-1

Foreign currency bank deposits A2/P-1

Botswana Government:

Issuer rating –foreign currency A2

Issuer rating –domestic currency A1

Long-term definition: "A" indicates good credit quality and "1" indicates top-end and "2" mid-range within category.

Short-term definition: "P-1" indicates superior credit quality and a very strong capacity for timely payment.

Outlook definition: "Stable" indicates that the rating is unlikely to change over medium-term.

Human development

HDI Ranking 2002

128 out of 177 countries

(1=most developed, 177= least developed)

Norway	1
Seychelles	35
Mauritius	64
South Africa	119
Egypt	120
Gabon	122
Morocco	125
Namibia	126
Botswana	128
Ghana	131
Swaziland	137
Lesotho	145
Uganda	146
Zimbabwe	147
Kenya	148
Madagascar	150
Nigeria	151
Senegal	157
Tanzania	162
Ivory Coast	163
Malawi	165
Zambia	164
Angola	166
DRC	168
Mozambique	171
Sierra Leone	177

The Human Development Index (HDI) measures a country's achievements in three aspects of human development: longevity, knowledge and a decent standard of living. Longevity is measured by life expectancy at birth; knowledge is measured by a combination of the adult literacy rate and the combined gross primary, secondary, and tertiary enrolment ratio; and standard of living, as measured by GDP per capita.

Source: UNDP Human Development Report 2004



		1998	1999	2000	2001	2002	2003	2004 ¹
Population	(Million)	1.56	1.59	1.65	1.69	1.70	1.70	1.69
Nominal GDP	(US\$m)	4 961	5 030	5 268	5 219	5 305	7 417	8 748
GDP/capita	(US\$)	3180	3 164	3 193	3 088	3 121	4 363	5 176
Exchange reserves -excluding gold	(US\$m)	5 941	6 229	6 317	5 897	5 474	5 339	5 358 ²
Import cover	(Months)	33.9	36.9	39.9	36.4	40.0	29.0	29.0
External debt ³	(US\$m)	468	525	477	417	462	375 ⁴	581
% of GDP	%	9.4	10.4	9.0	8.0	8.7	6.0 ⁴	7.8

1) Preliminary or estimates. 2) Sept. 3) Fiscal year, end of period. 4) June.

e = estimate, f = forecast

Economic structure

The mining industry - mainly diamonds - continues to contribute significantly to economic activity and accounts for 35% of GDP. Botswana remains the world's largest gem diamond producer, with output reaching a record 31 million carats in 2004, about a quarter of the world's production in terms of value. Mining's dominance on the production side persists despite government's continuous efforts to diversify the economic base. The sector accounts for only 3% of formal employment.

Agriculture's contribution has declined to the lower single-digits as the significance of the services sector - both in terms of contribution to GDP and employment - has risen notably in recent years. The sector now contributes around 51% to GDP and accounts for a large portion of formal employment while also creating many informal jobs. Tourism and telecommunications are contributing an increasingly rising share.

Government services (at central, local and parastatal level) remain significant contributors, accounting for 16% of GDP and around 45% of formal employment, making the government the largest employer.

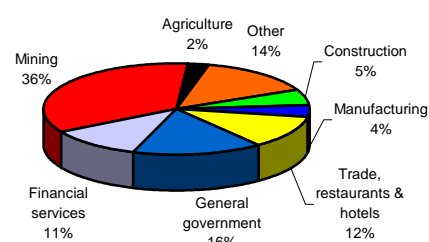
Real GDP growth

Botswana continues to experience high growth rates, with real GDP growth having remained in the 4% to 8% band in the past decade. The mining sector continues to be the main driver, while growth in the services sectors and government's disciplined approach to economic and financial management also contribute.

Diamond output remained strong during 2004, reaching a record output level despite labour instability at the major mines. Higher output was underpinned by investment in the diamond-mining sector in recent years, mainly in big projects such as Orapa. Output is expected to reach a plateau in the next few years. A recovery in global economic growth, particularly consumer spending in the US - the largest market for gem diamonds - supported demand during 2004. However, revenue growth is likely to have been moderate as higher global diamond prices were offset by a weak US dollar.

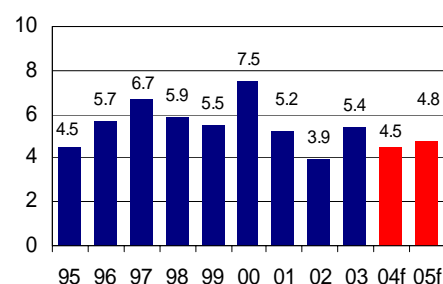
The services sector benefited from brisk growth in financial services, tourism, water and electricity and transport and telecommunications. The International Financial Services Centre has attracted fixed investment to the country, boosting the sector's contribution to GDP, particularly that of banks and insurance services. Tourism has benefited from Botswana's relative safe-haven status amid global geopolitical instability, while robust growth in the mobile phones industry buoyed the transport and telecommunications sector. It is clear that future growth will be driven by the services sector, although the trickle down from mining and related industries will be crucial.

Contribution to GDP



Source: Bank of Botswana

Real GDP growth %



Source: International Monetary Fund, Stanbic Bank



Consumer inflation (%)

Prudent monetary policy has contributed to the structural decline in inflation over the past decade. Botswana's inflation rate has been stable, never exceeding 20%, even during the boom years of the 1980s. Sound monetary policy in recent years has contributed to the lower inflation base, with inflation remaining within single-digits since 1997.

Food price increases were subdued throughout 2004, with the food inflation rate averaging 4.7% in 2004 from 11.6% in 2003. This low food inflation rate offset the negative impact of rising administered prices, mainly of fuel (up 26%) and telecommunication tariffs, as well as the effect of the pula devaluation. During the second half of the year, the pula appreciation helped to limit the rise in inflation. The inflation target band was widened to 4% to 7%, with the upper limit raised from 6%, following the devaluation.

We expect the inflation rate to remain high during the first half of this year before easing towards 6% during the second half. While base effects will ensure that the inflation rate stays high, subdued food and imported inflation, as inflation remains moderate in South Africa, and a steady pula against the rand will drive the inflation rate downwards. A significant amount of imports (76%) originate in the SACU¹, mainly South Africa.

Interest rates (%)

A prudent monetary policy regime over the past three decades has contributed to macroeconomic stability. During 2004, the Bank rate remained unchanged at 14.25%. The Bank of Botswana's mid-year review of *Monetary Policy Statement 2004* highlighted global inflation and oil prices as the main threats to domestic inflation, while it noted that moderate bank credit extension growth and government spending were favourable to a stable inflation environment. Commercial bank credit extension growth remained under control despite the 15% hike in public service wages in April 2004.

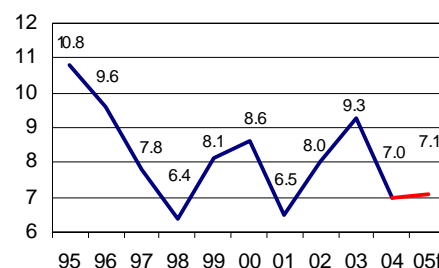
We expect the Bank rate to remain unchanged at 14.25% throughout 2005. Any monetary easing would indicate monetary accommodation of recent price shocks such as those in the telecommunications industry and could perpetuate the inflationary spiral. Although Interest rates policy is focused on controlling demand-induced inflation, monetary policy has to be countercyclical to inflation trends.

Pula exchange rate

Since 1989, exchange rate policy has been applied solely to promote competitiveness of non-mineral exports by maintaining a stable real exchange rate against the rand, with a certain exchange rate level, based on inflation differentials, maintained with the South African unit. The rand's rise in recent years thus resulted in a corresponding appreciation of the pula. This had a negative impact on Botswana's export earnings in pula terms and as a result the pula was devalued by 7.5% in February 2004 to restore competitiveness. However, the effect of the devaluation has since been eroded as the pula appreciated in line with a firmer rand during 2004.

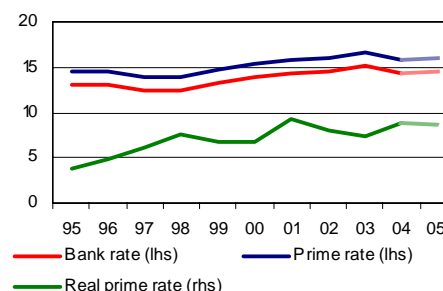
The pula gained 2.3% against the US dollar, while shedding 4.9% and 4.7% against the euro and the British pound, respectively. The pula has risen by 61.3% against the US dollar since January 2002. During 2005, we expect it to maintain its strength as the rand remains firm against a broadly weaker US dollar.

Consumer inflation – annual % average



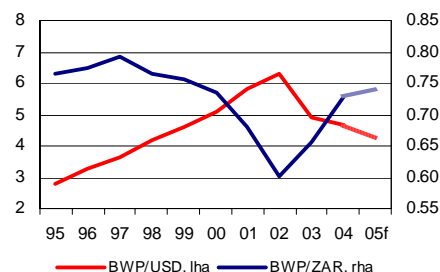
Source: Central Statistics Office, Stanbic Bank

Interest rates – annual average %



Source: Bank of Botswana, Stanbic Bank

Pula exchange rate



Source: Bank of Botswana, Stanbic Bank

¹ Southern African Customs Union.



Balance of Payments (US\$m)

Botswana's export sector is underpinned by diamond and beef sales to the European Union (EU), with the country recording a series of trade surpluses in recent years. We expect this situation to hold in the coming years as the country maintains trade agreements with the bloc.

The current account surplus widened during 2003, supported by net service receipts and a significant slowdown in income repatriations. During 2004, we expect the improvement in beef exports (albeit from a low base) and higher diamond earnings to have boosted total exports. Despite currency strength, indications are that diamond earnings benefited from both increased volumes and prices. In addition, copper prices rose during the year (nickel prices remained lacklustre). Imports also expanded, stimulated by a stronger currency and buoyant domestic demand, while high global oil prices added to the import bill. Net service receipts were recorded during 2003 and tourism earnings must have maintained that position in 2004. Looking ahead, the current account will remain in surplus, although it is likely to weaken marginally.

Currency strength will have a negative impact on the terms of trade as export revenue falls and the import bill rises on the back of rising demand and high international oil prices. This implies that the level of foreign exchange reserves is also likely to fall. Although raising exports can offset this threat, the potential for higher export volumes is repressed by capacity problems, with the country unable to meet its export quotas for beef and, more recently, ostrich meat to the European Union.

After a period of relative stability on the capital and financial accounts, net outflows, mainly from the financial account, rose sharply after 1998. While the Asian emerging markets crisis of that year triggered outflows, the lifting of exchange controls in 1999 also facilitated movement of capital. The deficit in the financial account widened as direct investment flows remained erratic and portfolio outflows accelerated. Government's repayment of long-term external loans, public sector investment and increased shareholding by Debswana and De Beers contributed significantly to outflows in recent years.

The overall balance of payments position has, however, remained in surplus over the past decade on the back of surpluses in the current and capital accounts, which facilitated a build up of foreign exchange reserves to more than 40 months of import cover in 2002. Expectations of lower mining output, subdued investment flows and rising income payments suggest that the balance of payments position will weaken in the coming years. However, we do not expect the situation to have a significant adverse impact on the level of reserves, which we expect to remain at more than 25 months of imports in the foreseeable future.

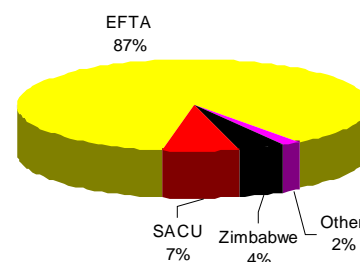
Balance of Payments

	1999	2000	2001	2002	2003	2004 ¹
Exports	2 661	2 682	2 325	2 325	2 876	3 076
Imports	1 876	1 778	1 612	1 647	2 177	2 752
Trade balance	785.6	904.5	713.6	678.4	699.5	324.0
Services & transfers						
Current account	619.0	546.7	600.5	170.9	750.9	450.0
Capital account	20.6	38.2	5.8	15.7	22.5	10.0

1) Stanbic Bank forecasts

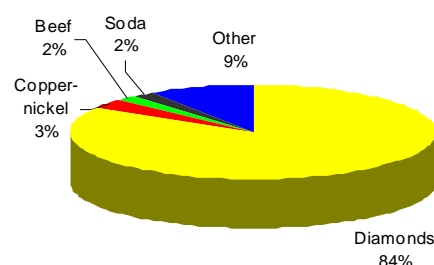
Source: Bank of Botswana

Destination of exports*



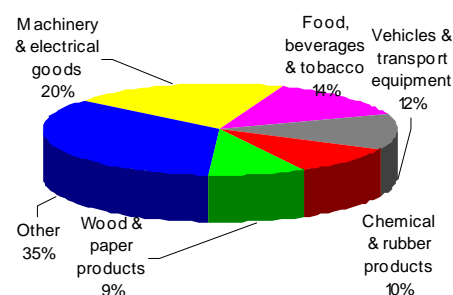
Source: EIU (*2000 data)

Composition of exports*



Source: EIU (*2003 data)

Composition of imports*



Source: EIU (*2001 data)



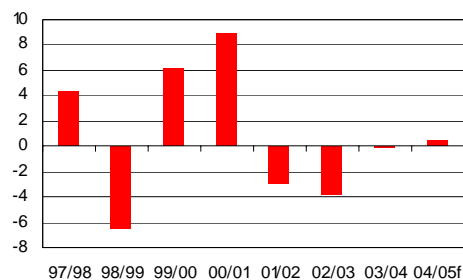
Government finances

Government has traditionally relied on the mining industry for most of its income, with mineral taxes historically contributing about half to total revenue. The rest of the revenue is largely made up of VAT, other taxes, non-tax revenue (including SACU receipts), while development grants accounted for only 0.4% of total revenue in 2003/04. A rules based approach to management of mining revenues has contributed to macroeconomic stability, avoiding the boom and bust type fiscal situations experienced by some of the continent's resource-based economies. This has enabled government finances to remain solid in recent years despite revenues coming under pressure as the strength of the pula resulted in lower export earnings in pula terms. The 2004/05 budget forecast a 13% rise in total revenues and grants to BWP18.21billion, with the increase expected from higher mineral revenue (of BWP8.07bn) on the back of rising diamond export volumes and prices as well as the devaluation of the pula. However, revenue is likely to be slightly below this level on the back of the strength of the pula. Total expenditure and net lending were forecast at BWP18.14bn (12% up on 2003/04) of which BWP14.57bn (80.3% of total) was recurrent expenditure, including BWP600m for public sector wage increases. The proposed budget thus had a small surplus of BWP70m, but the outcome is likely to be a larger surplus as tax revenue was boosted by strong domestic demand. In 2005/06 the government again faces the challenge of balancing the budget amid declining mineral taxes and a higher social spending burden. We expect rising tax revenue and higher gemstone prices to support revenue, while pressure will come from the impact of the stronger currency and a slowdown in SACU receipts. A restraint on spending to limit a possible deficit is likely during the fiscal year. Addressing a possible shortfall in fiscal revenue will thus remain a challenge and any action to tackle it will have to take overall macroeconomic policy into account so that long-term objectives as well as the authorities' long-established credibility are not forgone. In our view, another discrete devaluation like the one in February 2004 will be unfavourable. Devaluations - in addition to causing uncertainty – often fall short of ensuring the achievement of intended goals (developments in 2004 were a classic proof of this).

Economic outlook

Prudent macroeconomic policies and significant capital investments over the years have transformed Botswana into one of the most dynamic economies in Africa, catapulting the country from being the third poorest in Africa at independence to one of the richest today. Good governance, coupled with prudent economic management helped to transform the economy from being primarily based on agriculture to a more dynamic mix of mining and services. While the government should strive to diversify the economy towards manufacturing, new investment in the agricultural sector is needed to expand production capacity and take advantage of existing opportunities. Overall macroeconomic management will remain prudent, with coordination of monetary and fiscal policies continuing to play a pivotal role to ensure stability and limit the risk of fiscal profligacy. This implies that, should the government decide to finance its budget deficit by borrowing in the domestic market, there is no real risk to the stability of local financial markets; rather, this would have the benefit of deepening local financial markets. Diversifying the economy remains crucial as it will help to shield it from external shocks, particularly global commodity prices. Sound economic fundamentals and the absence of restrictions on capital flows make Botswana an attractive investment destination.

Budget deficit - % of GDP



Source: Bank of Botswana, Stanbic Bank



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