


WHY BOTSWANA'S
CREDIT RATING IS
BETTER THAN JAPAN - A BRIEF
ECONOMIC HISTORY

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Congratulations Japan - Moody's Sovereign Ratings, April 2008

(Domestic Currency Long Term Government Bonds)

- **Aaa**
- Australia, Austria, Bermuda, Canada, Denmark, Finland, France, Germany, Iceland, Ireland, Luxembourg, Netherlands, New Zealand, Norway, Singapore, Spain, Sweden, Switzerland, UK, USA
- **Aa**
- Aa1 Belgium
- Aa2 Italy, Portugal, Slovenia, Qatar, Kuwait, United Arab Emirates
- Aa3 Cyprus, Hong Kong, Taiwan
- **A**
- A1 Bahamas, **BOTSWANA**, Chile, China, Czech Rep., Estonia, Greece, Israel, **JAPAN**, Malta, Poland, Saudi Arabia, Slovakia
- A2 Bahrain, Korea, Latvia, Oman, South Africa, Hungary, Lithuania



Why was Botswana the first country in Africa to get an investment grade credit rating?

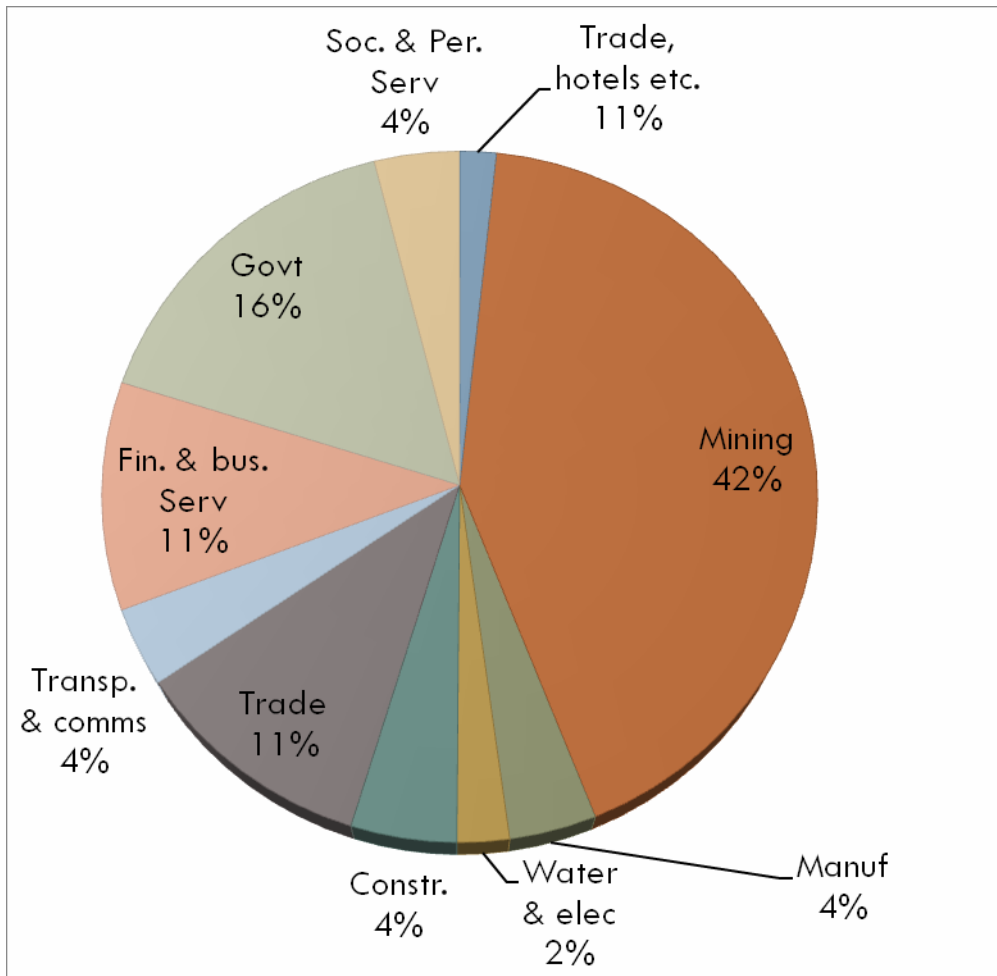
The Simple Answer - Statistics

- Strong growth
 - ▣ 8% a year avg. real growth over past 30 years, translating into 5% p.a. per capita GDP growth
- Healthy Public finances
 - ▣ Budget surpluses in 20 of last 24 years
 - ▣ Minimal debt, government large net creditor
- Healthy balance of payments
 - ▣ Last current account deficit was in 1982
 - ▣ FX reserves of 26 months of import cover
 - ▣ Strong IIP (Offshore assets P90.5bn Liabilities P18.7bn)
- Botswana is one of 13 “Success Stories” with high, sustained growth, identified by Commission on Growth and Development (almost all of the others were in Asia)

The Underlying Answer – The Policy Environment

- Minerals Policy
- Economic Diversification
- Monetary and Exchange Rate policies

Economic Structure (GDP, 2006/07)



- Mining continues to dominate GDP
- Mining & government contribute 58% of GDP, so non-mining private sector is well under half of the economy

Minerals Policy

- Mining – primarily diamonds - accounts for:
 - 40% of GDP
 - 50% of government revenues
 - 75% of exports
- No Resource Curse/Dutch Disease
- Key choices:
 - Ownership
 - Minerals taxation
 - Use of mineral revenues
 - Asset accumulation

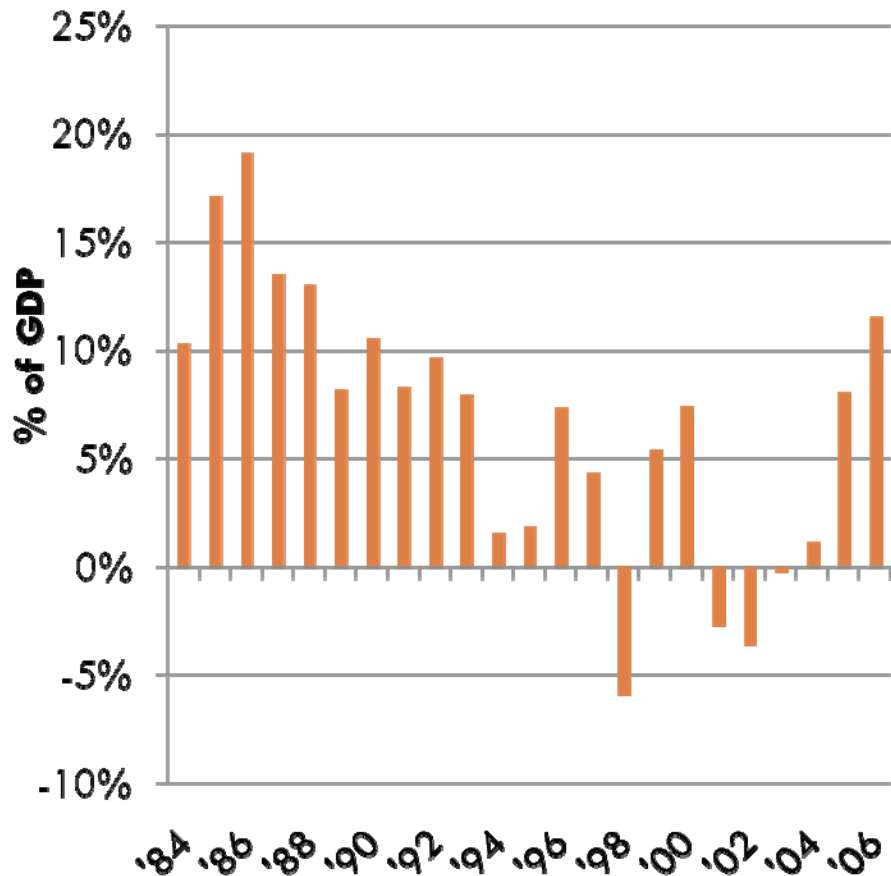
Minerals Policy

- Ownership
 - ▣ allow private sector to do the job of mining
 - ▣ some public ownership (paid for)
 - ▣ Govt. involvement in strategic decisions, as shareholder, but passive wrt management
- Taxation
 - ▣ allow investors to make reasonable return on capital, including compensation for risk
 - ▣ excess returns from mineral “rents” to be earned by government
 - ▣ through royalties, taxes and share of dividends
 - ▣ transparent and stable tax formula

Minerals Policy

- Mineral revenues reserved for investment
 - ▣ revenues derived from sale of asset
 - must be used to acquire new assets
 - not to be used to finance consumption
 - ▣ sustainable budgeting rule
 - recurrent expenditure financed from non-mineral revenues
 - ▣ mineral revenues used for:
 - investment in physical assets (social and economic infrastructure)
 - investment in human capital (education, health)
 - accumulation of financial assets
 - ▣ recognise limits of absorptive capacity and save rather than spend
- Result: budget surpluses and very high savings rate

Budget Balance

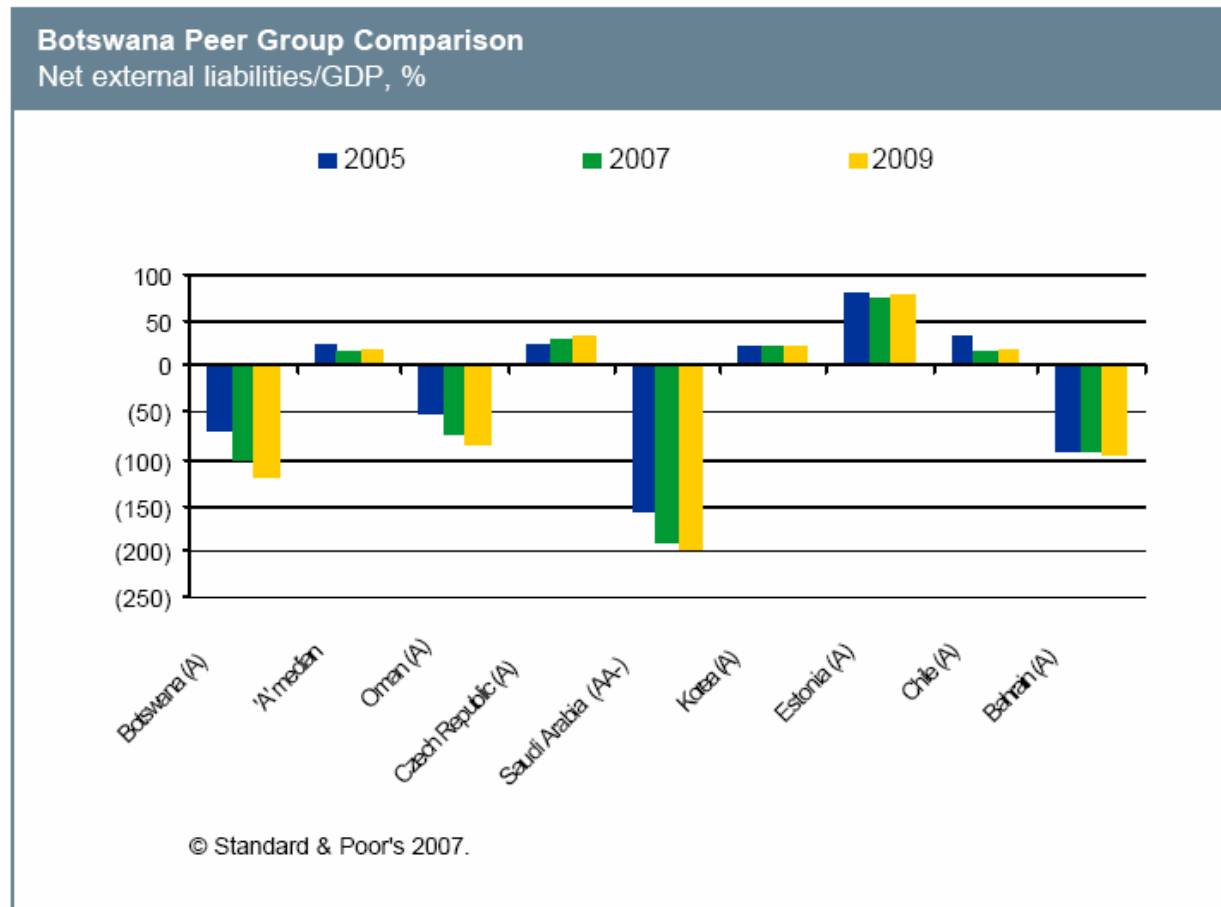


- Significant portion of mineral revenues accumulated as budget surpluses
- 2006/07 surplus over 11% of GDP – largest since late 1980s

Minerals Policy

- Mining Fund (an early SWF!)
 - ▣ Pula Fund - long-term investment portion of FX reserves
 - ▣ Managed for return, with substantial equity investments
 - ▣ Earnings have been substantial revenue source for government
 - ▣ Government balances at BoB financed by budget surpluses
 - ▣ Provides “cushion” for coping with mineral volatility – avoiding shocks

S&P “A” rated sovereigns



- Botswana's external position very strong, even by the standards of "A" rated countries

Economic Diversification

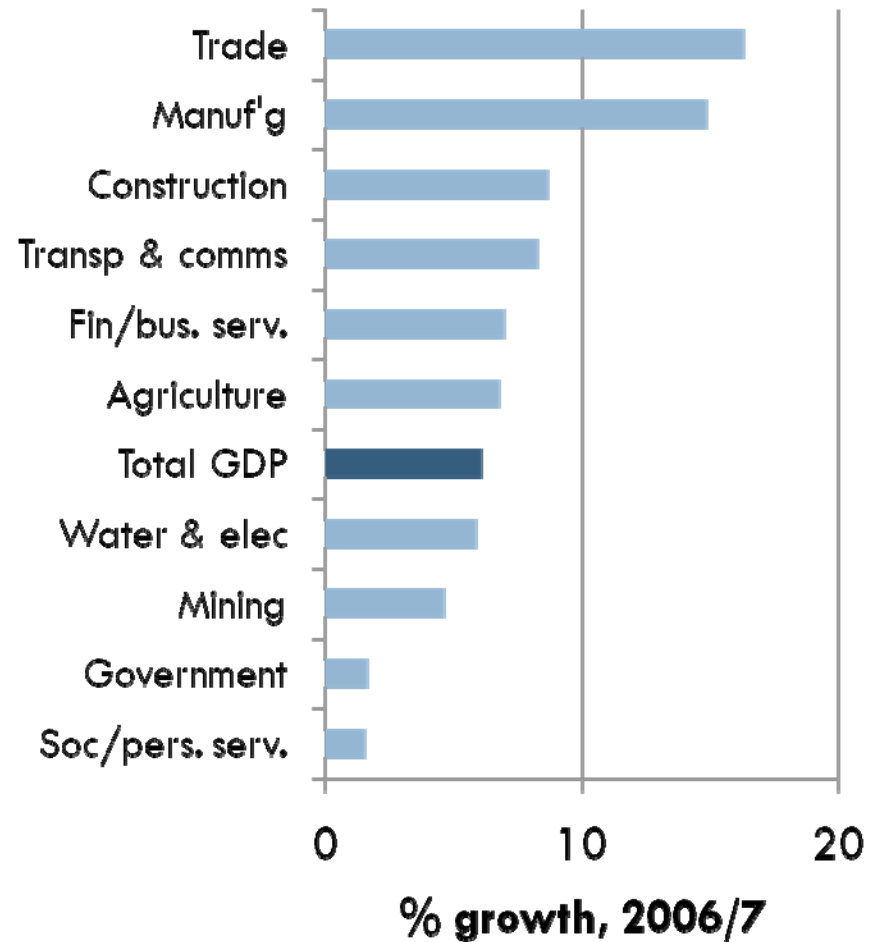
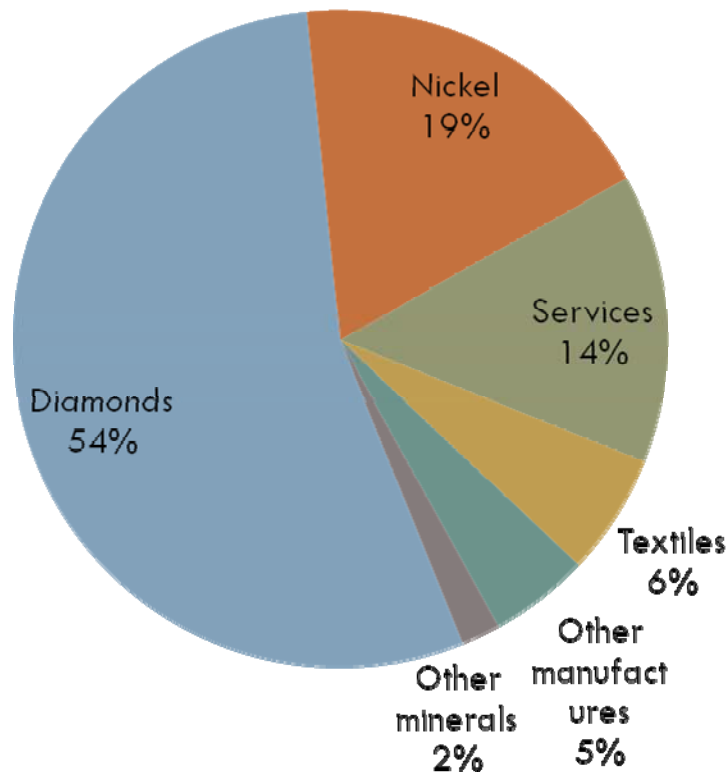
- Minerals bring revenues but:
 - would eventually run-out
 - could discourage other activities (Dutch Disease)
 - limited job creation (from diamonds)
- Consistent policy focus on economic diversification
 - Initially manufacturing, but high cost location
 - Now broadened to include services (tourism, finance)
 - Diversification of mining sector, including processing

Economic Diversification

- Has diversification been successful?
 - ▣ Perceptions are - no
 - Share of non-mining private sector in GDP has not grown
 - Unemployment still a major problem
 - ▣ But some encouraging signs:
 - Strong growth in NMPS recently (9.1% in 2006/07)
 - Share of imports in GDP declining, i.e. import substitution taking place
 - Exports becoming more diversified and less dependent on diamonds
 - Exports of services growing rapidly (15% of total)

Indicators of Diversification

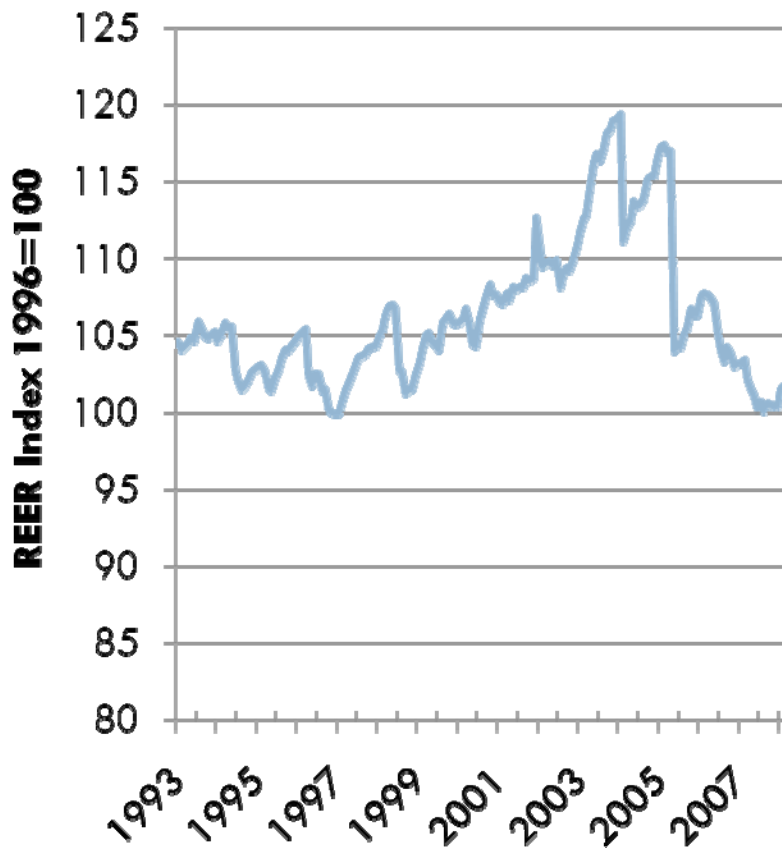
Exports, 2007



Monetary and Exchange Rate Policies

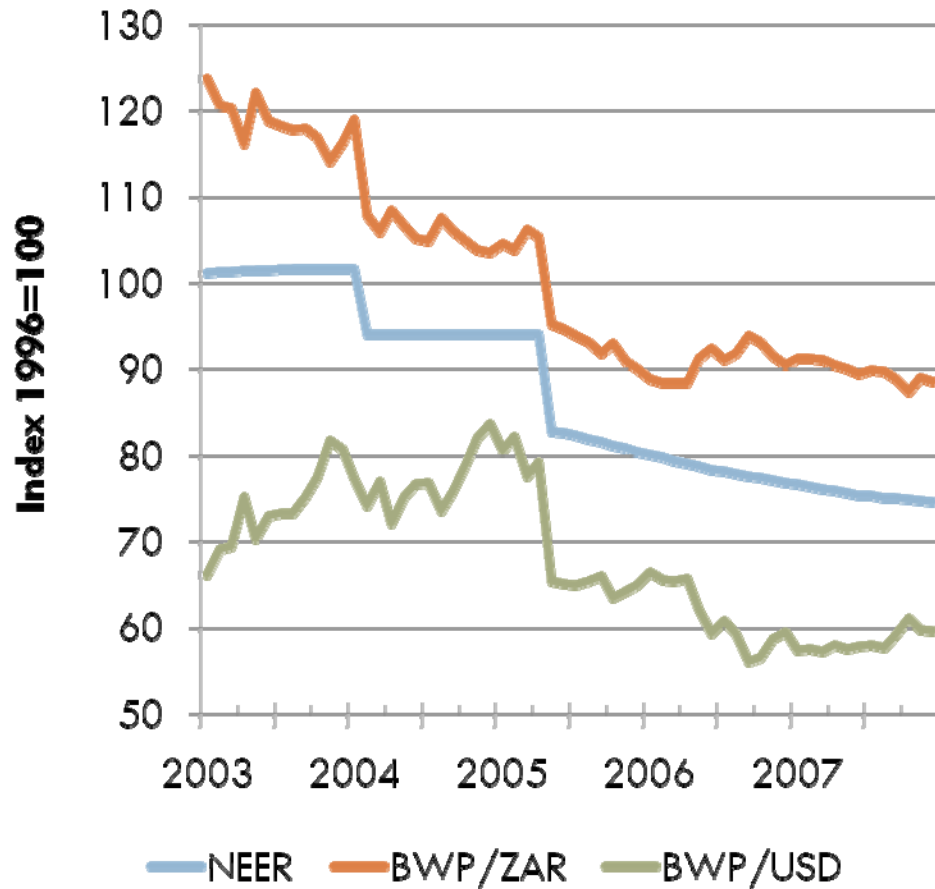
- Policy has followed an eclectic mix – focused on containing inflation and avoiding Dutch Disease
- Independent policies – not dictated from outside or following fashion
- Have been maintained consistently over a long period – giving macroeconomic stability

Exchange Rates - Real



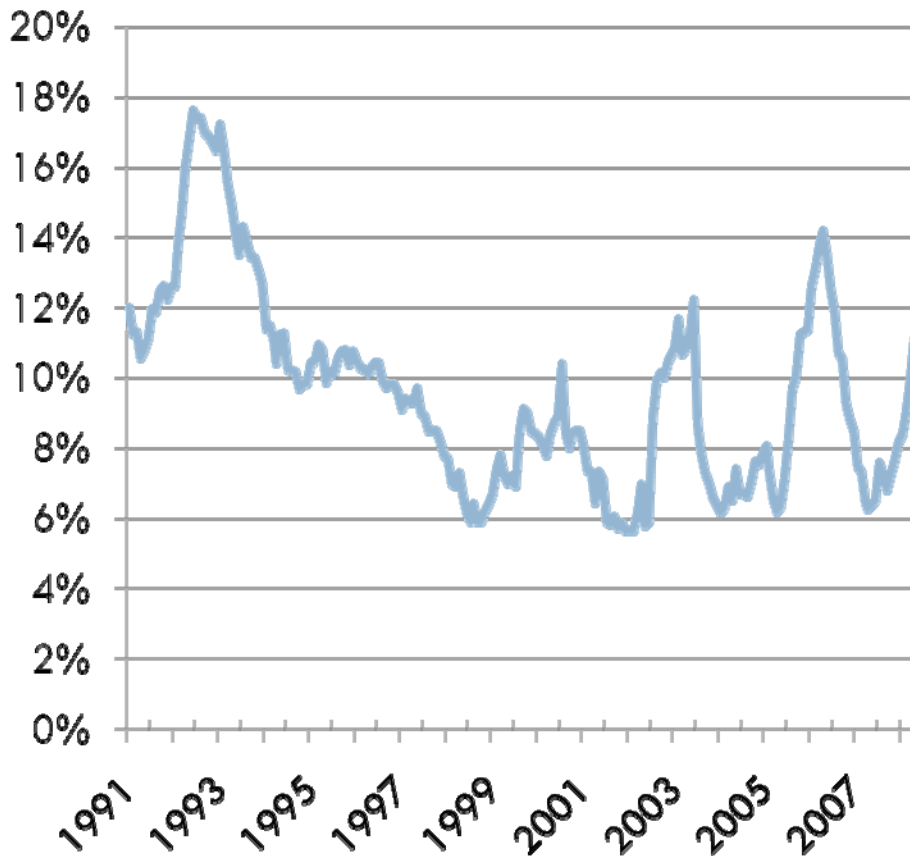
- Real exchange rate appreciation – declining competitiveness - a major problem for mineral exporters
- Botswana has generally achieved REER stability, although period of REER appreciation through to 2004
- Devaluations and crawling peg have achieved REER depreciation and restored competitiveness

Exchange Rates - Nominal



- Exchange rate basket peg – ZAR and SDR
- Overall nominal rate is fairly stable (NEER)
- Bilateral rates may fluctuate (driven mainly by ZAR-USD)

Inflation



- ▣ Anchored by exchange rate, supplemented by interest rate policy
- ▣ Inflation never a major problem but has nevertheless been generally on the high side – never down to SA or international levels
- ▣ Driven by expansionary government spending and slow productivity growth

Concluding Points – Key Attributes

- Policy stability and consistency
- Mineral revenues saved and invested in social, economic, human and financial capital
- Sustainable public finances
- Minimal debt (domestic and international)
- Strong BoP and international financial position
- “Buffers” to cope with external shocks
- Competitive exchange rate
- Business-friendly economic environment