Botswana

key figures

• Land area, thousands of km^2	582
• Population, thousands (2004)	1 795
• GDP per capita, $ (2002/2003)	4 440
• Life expectancy (2000-2005)	39.7
• Illiteracy rate (2004)	19.4

African Economic Outlook 2004/2005
www.oecd.org/dev/aeo

Botswana

WITH A TRACK RECORD OF sound macroeconomic policies, good governance, reliable institutions and political stability, Botswana remains one of the top-performing economies in Africa. The country has managed its diamond wealth efficiently, in stark contrast to the widely cited cases of natural resource curse experienced by many developing countries. Botswana also has the reputation of being the least corrupt country in Africa and has the highest sovereign credit rating on the continent. These virtues, together with prudent macroeconomic management, have helped Botswana to achieve decades of robust economic growth, transforming itself from one of the poorest countries in the world to a middle-income country. With real per capita income currently in excess of $4 700, Botswana is one of the richest countries on the African continent.

Botswana faces difficult challenges in the years ahead, however, as the economy remains heavily dependent on diamond production, which is near full capacity, and an HIV/AIDS epidemic threatens to undermine past economic gains. To respond to these challenges, Botswana in 2003 launched the Ninth National Development Plan (NDP9) covering the period 2003/04-2008/09, which focuses on diversifying the economy away from mineral production and addressing the problems of unemployment and poverty. Concurrently, the authorities have prepared a comprehensive National Strategic Framework (NSF) for HIV/AIDS that consolidates all the programmes related to the pandemic and is considered to be among the best in Africa.

The end of growth in the diamond industry and high HIV/AIDS infection rates threaten a historically high-performing economy.

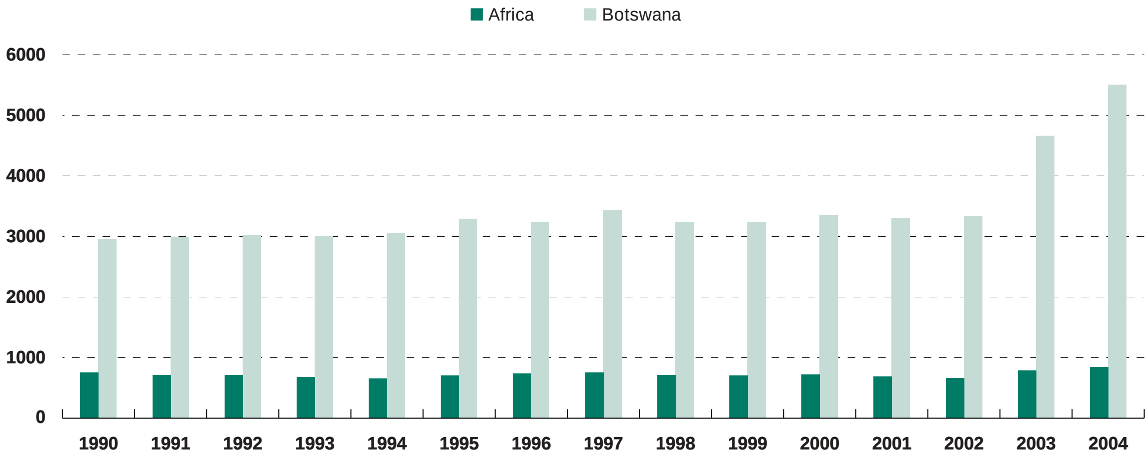
Botswana is also likely to be severely hit by the end of the Multi-fibre Agreement (MFA) on 31 December 2004, which paves the way for quota-free trade in textiles and clothing. Despite the protection Botswana enjoys under the African Growth and Opportunity Act (AGOA), this will expose the country to competition from larger low-cost producers, such as China and India, which can sell their goods at lower prices on the global market.

Figure 1 - Real GDP Growth

Source: Bank of Botswana and IMF data; estimates (e) and projections (p) based on authors' calculations.

Real GDP continued to grow at a strong pace in 2002/03 and 2003/04 (5.5 per cent and 5.2 per cent respectively)[1], owing to productivity gains in the diamond sorting process and good performance in the

Figure 2 - GDP Per Capita in Botswana and in Africa (current $)



Source: IMF.

private non-mining sector. The latter suggests that the authorities' efforts to diversify the economy are starting to take hold. Growth is expected to slow in the medium term, however, owing to the levelling off of diamond production and the impact of HIV/AIDS. Inflation declined in response to prudent monetary policy. The devaluation of the pula, Botswana's currency, in February 2004 helped maintain external competitiveness despite the appreciation of the South African rand and the US dollar, to which the pula is pegged. After two consecutive years of fiscal deficit, the overall fiscal balance was slightly in surplus in 2003/04, as capital expenditure was scaled down to offset revenue shortfall.

Recent Economic Developments

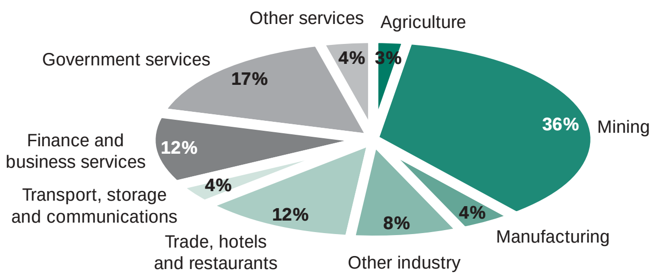
The economic fortunes of Botswana, the world's largest exporter of diamonds, are largely driven by developments in the mining industry. The mining sector as a whole is the largest contributor to GDP, export earnings and government revenues. In 2003/04, the share of the mining sector in GDP was 34.7 per cent, down slightly from 35.9 per cent in 2002/03. This was largely attributable to the drop in the international price of diamonds, which led to a 12.4 per cent decline in the value of Botswana's diamond output. The outlook for 2004/05 is positive, as substantial foreign investment is expected to bring efficiency gains in diamond production.

The non-mining sectors show considerable variation in their GDP shares. General government services appear to command the lion's share of GDP, with around 17.2 per cent in 2003/04, followed by financial services (10.5 per cent) and retail/wholesale trade and hotel services (10.2 per cent). This is not surprising, given that the government plays a leading role in the implementation of public investment and development programmes, as well as being an important source of wage employment in the country. Thus, government-induced demand has been very significant for the growth and development of the domestic economy.

Agriculture, which at independence accounted for the largest share of GDP, now contributes less than 3 per cent. The level of industrialisation in Botswana is low, as reflected in the relatively small proportion of real GDP originating in the manufacturing sector. Despite the increased pace of modernisation and diversification in recent years, occasioned by the government's multifarious interventionist policies, the GDP share of

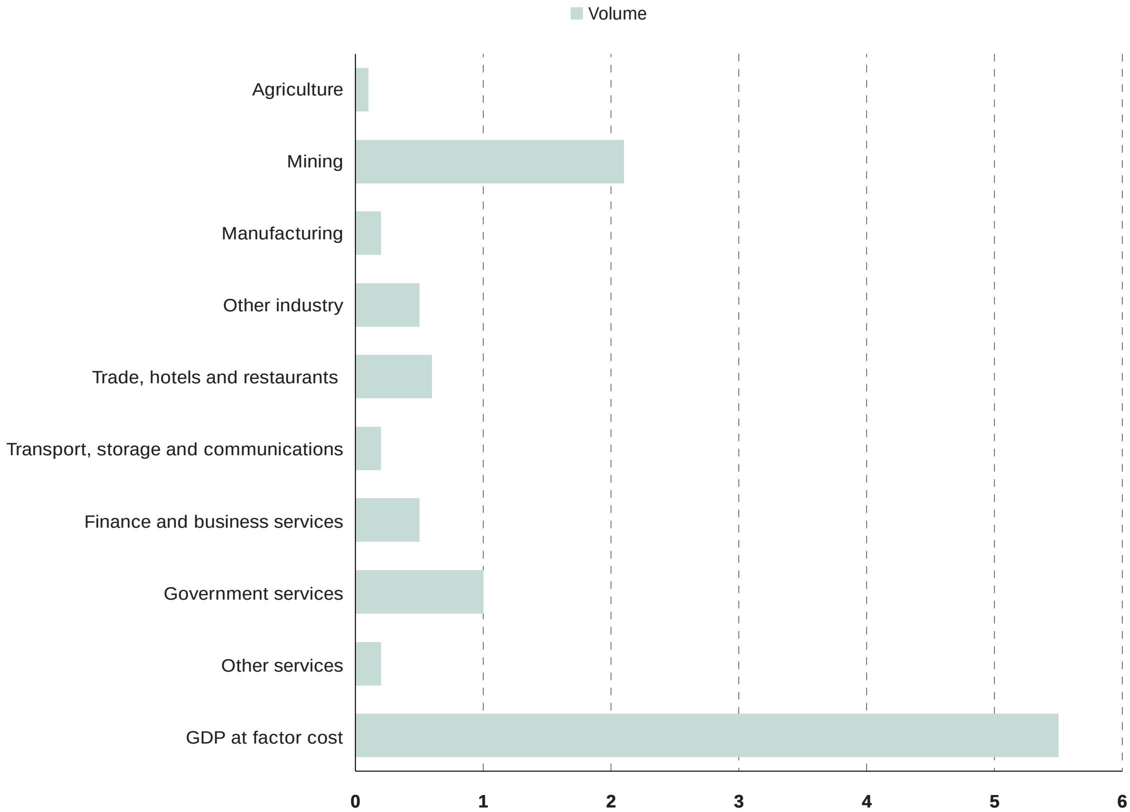
1. The national accounts data cover the period July-June and the fiscal data cover April-March, while balance-of-payments and monetary data are based on the calendar year.

Figure 3 - GDP by Sector in 2002/03 (percentage)



Source: Authors' estimates based on Bank of Botswana data.

Figure 4 - Sectoral Contribution to GDP Growth in 2002/03 (percentage)



Source: Authors' estimates based on Bank of Botswana data.

manufacturing, which averaged 5.7 per cent in the 1970s, declined steadily to 4.7 per cent in the 1990s and 3.7 per cent in 2003/04. Clearly, this declining trend is inconsistent with the country's hopes and expectations of nurturing a vibrant and diversified economy, as within the manufacturing sector itself very little diversification has occurred. Despite the government's investment promotion drive, through the Botswana Export Development and Investment Agency (BEDIA), the manufacturing sector consists of a narrow range of activities, including the traditional meat and meat products industry, brewery, textiles and garments, tannery and leather products, glass and information technology products.

The financial services, trade, and hotels and restaurants sub-sectors have seen their contributions to GDP rise steadily over the years, reflecting their response to the expansion of the booming tourism industry. Tourism, which contributes nearly 4 per cent to GDP, is Botswana's second-largest export sector behind diamonds, bringing around 1.1 billion pula into the country annually. In 2003/04, a new tourism model, grounded in community-based projects, was introduced throughout the country. This was designed to attract a more diverse group of tourists and benefit the rural communities in which most tourism properties are located. The strength of Botswana's tourism industry is underscored by the listing of two tourism firms, AfriTourism Limited and Chobe Holdings, on the Botswana Stock Exchange. Another company, Okavango Wilderness Safari (OWS), received approval last year to join Botswana's International Financial Services Centre (IFSC). Another noteworthy feature of the services sector is the growth in the telecommunications sub-sector, particularly cellular phones. During 2003/04, the sector maintained the growth momentum it gathered in the preceding year, with mobile telephone services growing by over 10 per cent. It should be added, however, that reforms in the financial services sector constitute an integral part of the government's diversification strategy. The partial privatisation of the pension fund and the recent launching of an offshore centre are key financial services reforms that may have important implications for the conduct of monetary policy.

Despite the surge in oil prices, Botswana has witnessed strong growth in domestic demand. In 2003/04, total gross domestic investment accounted for 25.5 per cent of GDP, compared with 24.5 per cent in 2002/03. The increase was due to growth in private investment, however, as public investment was scaled back owing to revenue shortfalls. Domestic consumption increased as well. Gross national savings, which accounted for over 45.3 per cent of GDP in 2002/03, fell slightly to 37.2 per cent in 2003/04. Here again, the decline was due to a decrease in public savings.

Table 1 - Demand Composition (percentage of GDP)

	1996/97	2001/02	2002/03	2003/04	2004/05(e)	2005/06(p)	2006/07(p)
Gross capital formation	**26.0**	**24.7**	**24.5**	**25.5**	**27.2**	**29.1**	**30.7**
Public	13.9	11.7	11.1	11.2	11.4	11.5	11.5
Private	12.0	13.0	13.4	14.3	15.8	17.5	19.2
Consumption	**56.5**	**62.1**	**54.7**	**62.8**	**62.5**	**61.9**	**62.0**
Public	26.6	33.0	34.7	37.3	37.7	37.6	37.8
Private	30.0	29.1	20.0	25.5	24.7	24.3	24.2
External sector	**17.5**	**13.3**	**20.8**	**11.6**	**10.3**	**9.0**	**7.3**
Exports	55.7	49.1	49.2	44.6	43.6	43.2	41.7
Imports	-38.2	-35.8	-28.4	-32.9	-33.3	-34.2	-34.5

Source: Bank of Botswana and IMF data; estimates (e) and projections (p) based on authors' calculations.

Macroeconomic Policies

Fiscal and Monetary Policy

Botswana's National Development Plans set out guidelines for the country's fiscal policy stance. A major objective of fiscal policy is to ensure that public resources are used efficiently and effectively to provide the economic and social infrastructure needed for rapid private sector development, including that needed for economic diversification and the growth of enterprises producing for export.

Following two years of sizeable deficits (in 2001/02 and 2002/03), the government announced its intention to return to a long-standing tradition of surpluses. This will require a boost in non-diamond revenue in the years ahead, as resources from diamonds are expected to plateau along with production, and outlays on education and health, including HIV/AIDS, will need to be increased.

In 2003/04, a prudent fiscal policy resulted in a slight surplus. Faced with a shortfall in revenue (mostly due to inadequate collection of the value added tax introduced in 2002), the authorities raised levies on petroleum products and cut capital expenditure. Concurrently, in the context of the partial privatisation of the civil service pension fund initiated in 2001, the government continued to draw on its deposits with the central bank to transfer funds corresponding to accumulated pension claims to the private pension fund managers.

Table 2 - Public Finances[a] (percentage of GDP)

	1996/97	2001/02	2002/03	2003/04	2004/05(e)	2005/06(p)	2006/07(p)
Total revenue and grants[b]	**41.7**	**39.7**	**41.0**	**44.8**	**44.5**	**44.3**	**44.1**
Tax revenue	29.3	33.1	35.1	38.6	38.4	38.3	38.1
Grants	0.5	0.2	0.2	0.5	0.5	0.4	0.4
Total expenditure and net lending[b]	**33.9**	**42.7**	**45.0**	**44.5**	**44.8**	**44.9**	**45.9**
Current expenditure	22.4	31.0	33.2	35.1	35.3	35.2	35.4
Excluding Interest	*21.9*	*30.8*	*32.9*	*34.8*	*35.1*	*34.9*	*35.2*
Wages and salaries	7.8	12.3	11.3	10.7	10.5	10.3	10.1
Interest on	0.5	0.3	0.2	0.3	0.3	0.2	0.2
Capital expenditure	12.6	11.6	10.9	10.5	10.6	10.7	10.7
Primary balance	**8.3**	**-2.7**	**-3.8**	**0.6**	**0.0**	**-0.3**	**-1.6**
Overall balance	**7.7**	**-3.0**	**-4.0**	**0.3**	**-0.3**	**-0.5**	**-1.8**

a: Fiscal year begins 1 April.
b: Only major items reported.
Source: Bank of Botswana and IMF data; estimates (e) and projections (p) based on authors' calculations.

Monetary policy is formulated with the aim of achieving a low, stable rate of inflation while maintaining a stable real exchange rate that supports the international competitiveness of local producers. The tight monetary policy introduced at end-2002 to stem inflationary pressures was relaxed towards the end of 2003 as those pressures abated. The Bank of Botswana (BoB) rate, which was raised from 14.25 per cent to 15.25 per cent in November 2002, was lowered in steps to 14.25 per cent by end-2003 and remained at that level in 2004. The prime rate for commercial banks, however, remained at 15.75 per cent in 2004. The monetary authorities also made extensive use of open market operations to absorb excess liquidity through the sale of Bank of Botswana certificates (BoBCs) in the domestic money market.

In response to the prudent monetary policy of the central bank, inflation declined from 10.7 per cent in 2002/03 to 6.3 per cent in 2003/04, and it remained at about the same level in 2004 despite the February 2004 devaluation of the pula, the oil price hike and the attendant rise in the prices of electricity and petroleum products (6 per cent and 16-19 per cent respectively). Partly reflecting the monetary policy stance, growth in domestic credit decelerated sharply in 2003 and 2004.

Exchange rate policy is directed at achieving an equitable balance between maintaining the competitive position of domestic producers, especially producers of non-traditional exports, and avoiding monetary instability and high inflation. For sustainable economic diversification, the creation of productive employment opportunities and expansion of economic opportunities for Botswana entrepreneurs, it is necessary that greater emphasis be given to maintaining the international competitiveness of domestic producers of exports and tradable goods. Therefore, Botswana's macroeconomic policy aims at maintaining a stable real effective exchange rate (REER) in order to ensure international trade competitiveness. To this end, the exchange rate policy maintains a stable nominal effective exchange rate (NEER) by pegging the pula to a basket of currencies including the Special Drawing Right (SDR) and the South African rand, in proportions that reflect Botswana's trade shares. By promoting the stability of the NEER, the exchange rate mechanism has also acted as a nominal anchor for monetary policy. Between December 2000 and December 2003, the pula appreciated in real terms against the basket of currencies by about 25 per cent, after adjusting for the effect of VAT. It appreciated by 13 per cent against the SDR, 23 per cent against the US dollar and 11 per cent against the British pound, but depreciated by 6 per cent against the rand. Meanwhile, the trade-weighted NEER of the pula remained stable, appreciating by only 0.3 per cent over the same period. On 5 February 2004, the pula was devalued by 7.5 per cent against the basket to offset the steady real effective appreciation over the past three years, in order to improve the economy's external competitiveness by providing an important boost to exporters and domestic producers competing with imports. Tourism, textiles, diamonds, copper, nickel and agricultural products are among the many sectors expected to benefit from the devaluation.

External Position

Botswana has an open economy, with a share of trade (imports plus exports) in GDP exceeding 75 per cent. Exports have been highly concentrated on a limited number of commodities (minerals) and directed at just a few destinations (mostly Europe). In 2003/04, diamond exports amounted to 9.2 billion pula ($1.8 billion), around 80 per cent of total exports. This figure represents a 4.4 per cent increase over the country's 2002/03 diamond exports of 8.8 billion pula ($1.4 billion). During the same period, copper and nickel exports increased significantly in pula terms (by 66 per cent), although they represent a very small proportion of total exports. Imports also grew strongly in 2003/04 despite the devaluation of the pula and high oil prices. In nominal terms, imports increased from 3 366 million pula in 2002/03 to 4 813 million pula in 2003/04, an annual increase of 42 per cent. The 2003/04 balance of payments showed an overall surplus of about 1 000 million pula, compared to a surplus of only 300 million pula recorded in 2002/03. At the end of December 2003, foreign exchange reserves stood at $5.3 billion (SDR 3.6 billion), which, despite a decline of 5 per cent from November 2002, was still equivalent to 26 months of import cover.

The current economic development strategy for Botswana emphasises the advantages of attracting foreign direct investment (FDI) to the country. From 1997 to 2001, total FDI increased by 77 per cent, with the mining sector accounting for the largest share (86 per cent) as well as the bulk of FDI growth. Non-mining FDI grew rather slowly, the important recipients being the finance sector (7.5 per cent of total FDI) and the retail and wholesale trade sector (6.7 per cent), while manufacturing FDI grew relatively slowly and in the construction sector it actually declined over the period.

Table 3 - Current Account (percentage of GDP)

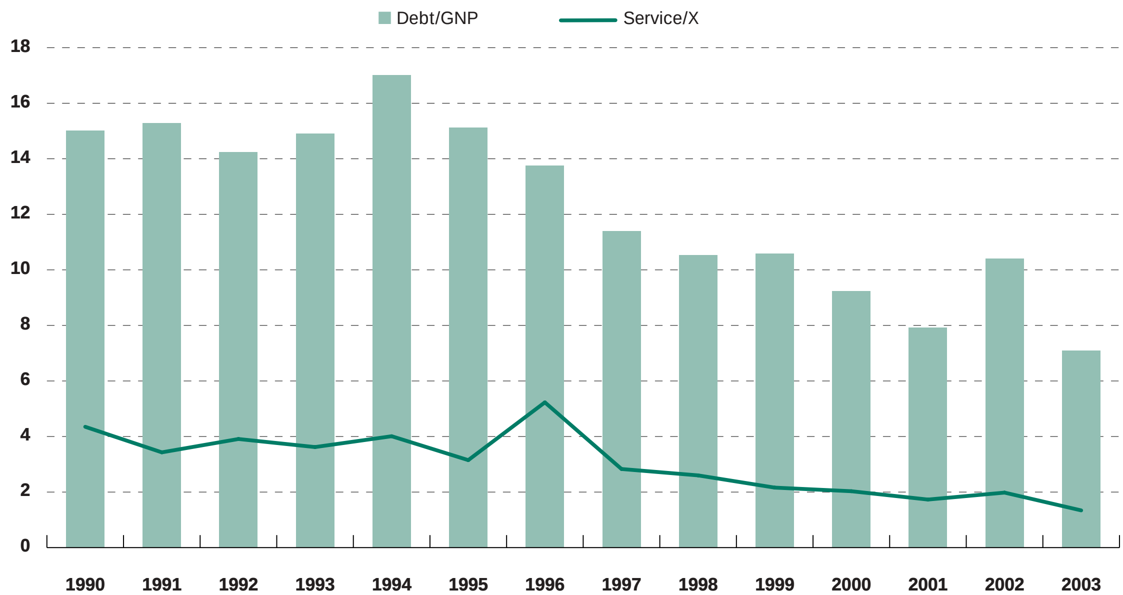
	1996/97	2001/02	2002/03	2003/04	2004/05(e)	2005/06(p)	2006/07(p)
Trade balance	18.2	12.4	16.8	13.9	12.6	11.5	10.0
Exports of goods (f.o.b)	51.6	42.1	42.9	38.4	37.6	37.1	35.8
Imports of goods (f.o.b)	-33.4	-29.7	-26.1	-24.6	-25.0	-25.6	-25.8
Services	-4.1	-1.8	-0.2				
Factor income	-3.9	-8.2	-6.1				
Current transfers	3.7	3.9	1.8				
Current account balance	**14.0**	**6.4**	**12.4**				

Source: Bank of Botswana and IMF data; estimates (e) and projections (p) based on authors' calculations.

Botswana's trade policy over the years may have been dictated largely by its membership of the Southern African Customs Union (SACU). Under the SACU agreement, all trade negotiations or agreements between Botswana and third parties must be acceptable to other SACU members. Botswana is also a member of the Southern African Development Community (SADC) and host to the SADC Secretariat. The SADC Trade Protocol, signed in September 2000, envisages the creation of an SADC free trade area by 2005. Botswana is also a beneficiary of the United States' African Growth and Opportunity Act (AGOA), which provides duty-free access to the US market for over 65 000 products from sub-Saharan Africa. Initially, Botswana was excluded from the AGOA protocol because it was classified as a middle-income country. In August 2002, however, the United States amended the AGOA provisions (AGOA II), allowing Botswana's textiles and garments to enter the US market duty-free. Botswana has also benefited from the WTO's Generalised System of Preferences (GSP), a tariff reduction facility offered by industrial countries to designated less-developed countries (LDCs) on certain export products. Foreign investors, especially in the textile sub-sector, have opted to locate their operations in Botswana in order to utilise the country's unused GSP facility and export to the United States.

The phasing out of the Multi-fibre Agreement on textiles and clothing on 31 December 2004 is likely to have adverse effects on Botswana's exports of textiles and clothing despite the GSP and the AGOA arrangements. It is likely that Botswana will be seriously hit for two reasons. First, despite AGOA protection, the end of the MFA will expose Botswana to competition from larger low-cost producers, such as China and India, which can sell their goods at lower prices on the global market. The fragmented nature of activities in the textiles and clothing sector in Botswana means that the country cannot compete effectively with the more efficient Asian producers in terms of unit labour cost, quality and productivity. A study carried out by the WTO in September 2004 shows that with the phasing out of the MFA, India and China alone are likely to grab about 80 per cent of the world market for textiles and clothing. The remaining 20 per cent will have to be shared by the rest of the world, including other highly competitive suppliers like Indonesia, Thailand and Pakistan. This means that little market share will be left for African countries such as Botswana and Mauritius. Second, most participants in the textiles and clothing sector in Botswana and other African countries are Asians who shifted their activities to Africa to jump the quota wall and maximise the market access opportunities provided by the AGOA initiative. With quota-free trade in textiles and clothing, many of these Asian producers have already started to relocate to their own countries, thereby exposing the supply constraints that often characterise production and exports in Africa. This is a wake-up call for Botswana and other African countries to diversify production and to upgrade the quality of their exports.

Figure 5 - Stock of Total External Debt (percentage of GNP) **and Debt Service** (percentage of exports)



Source: World Bank.

Structural Issues

Botswana has recently embarked on reforms of its large public sector with a view to improving the efficiency and effectiveness of government services. The public sector employs 44 per cent of formal sector personnel (81 000 civil servants and 12 000 employees in parastatals) and accounts for 17 per cent of GDP, second only to the mining sector. Although the public sector has a considerable presence in Botswana's economy, there are no reserved sectors and no resistant monopolies. The reforms include the adoption of the Performance Management System (PMS), Work Improvement Teams (WITS), Computerised Personnel Management System (CPMS), Organisation and Methods (O&M) Reviews, the Performance Based Reward System (PBRS) and decentralisation. The government has also reorganised and restructured some ministries and departments in order to improve efficiency and effectiveness in service delivery. Part of the reform has led to the establishment of autonomous authorities or boards, working largely on commercial principles. Examples include the Public Enterprise Evaluation and Privatisation Agency (PEEPA), the Public Procurement and Asset Disposal Board (PPADB), the Botswana Export Development and Investment Authority (BEDIA), the Citizen Entrepreneurial Development Agency (CEDA) and the Local Enterprise Authority (LEA). As of November 2004, all ministries and independent departments had developed their strategic plans and annual performance plans, in line with the PMS requirements. The process of introducing the PMS at the level of local authorities, which is considered to have greater impact on overall government service delivery, is moving gradually forward. The mainstreaming of PMS in the central government is expected to be completed during the 2004/05 financial year. In the case of WITS, around 565 facilitators and over 2 500 team leaders have been trained under the scheme. In addition, more than 16 WITS awareness sessions have been held for top managers, while 1 000 of the planned 1 150 teams have been registered. Over 700 projects have been undertaken and more than 400 completed.

Enforcing market discipline and promoting efficient allocation and use of economic resources, through the encouragement of private sector involvement in the country's economic development, has been one of the key aspects of public policy and public sector reform agenda in Botswana. With the promulgation of a comprehensive privatisation policy (Government Paper No. 1 of 2000), a new body called the Public Enterprise Evaluation and Privatisation Agency (PEEPA) was set up. Since its establishment, PEEPA has undertaken a review of the operations and activities of government departments and public enterprises, and has developed a draft Privatisation Master Plan which provides the framework and guidelines for the implementation of reforms to increase private sector participation in the economy. In addition, PEEPA has developed guidelines and manuals, including the Contracting Out Guidelines and the Divestiture Procedure Manuals, to help managers of public institutions implement privatisation in a consistent, transparent and equitable manner. Plans are also under way to introduce PPP procurement guidelines. In anticipation of government approval of the draft Privatisation Master Plan and increased activity in the coming year, PEEPA has been recruiting more personnel to boost its human resource capabilities. Throughout 2004, PEEPA has intensified its public awareness campaign, both through the press and by hosting a series of workshops with key stakeholders.

Government has done much to create a sound business environment through provision of infrastructure and enactment of laws and regulations to facilitate the operations of the private sector, as well as a stable macroeconomic environment. All these services are provided through consultations with all stakeholders. The government plays the role of a facilitator and has given the private sector the lead in developing the economy. It has established a High-Level Consultative Council (HLCC) for public-private sector dialogue, chaired by the President himself and having as members all the cabinet ministers as well as private sector actors. The Council meets twice a year to review issues of economic and socio-political importance. Similarly, each ministry has a Ministerial Consultative Forum, which also addresses cross-cutting issues. Finally, there is the national consultative council on manpower and employment, another public-private sector initiative, which reviews issues relating to training and development.

Botswana has long realised the importance of small and medium-sized enterprises (SMEs) in fostering economic growth and creating jobs. This has led to the introduction, over the last two decades, of targeted financial support as well as advisory programmes to help the people of Botswana establish their own enterprises. In their initial stage, these programmes were set up more in response to specific problems encountered than as the basis of a comprehensive and more focused government policy on SMEs. It is estimated that there are about 56 300 SMEs currently operating in the country, employing 125 000 people, including business owners[2]. In a 1996 study of the role of SMEs in Botswana, these enterprises' contribution to GDP was estimated at 30-45 per cent, while that of large firms was estimated at 38-48 per cent of GDP. SMEs are believed to account for 15 per cent of formal employment, implying that job creation is one of their most important contributions.

The Botswana authorities affirm that, in contrast to most other African countries, lack of finance has not been a bottleneck for SMEs in Botswana, as the government made resources available to these firms through its various enterprise development programmes (see box on next page). In particular, the government established two financial schemes – the Micro Credit Scheme and the Credit Guarantee Scheme – to provide citizens with easy access to start-up capital. SME development has suffered from other problems, however, including lack of premises, excessive laws and regulations, lack of information on government assistance programmes, lack of business start-up training and lack of entrepreneurial "role models". As a result, the survival rates of SMEs in Botswana have not been encouraging. Approximately 80-85 per cent of small enterprises in Botswana cease trading within five years of start-up. In addition, few SMEs have managed to grow and make the transition from SMEs to larger enterprises (only one or two out of 100 SMEs succeed in doing so).

To respond to these challenges, the authorities adopted a National Policy on Small, Medium and Micro Enterprises, which was drafted in 1999 by a Task Force on SMEs led by the private sector. The objectives of the policy are to foster citizen entrepreneurship and empowerment; encourage the development of a competitive and sustainable SME community; achieve economic diversification; create sustainable employment opportunities; promote exports; promote the development of vertical integration and horizontal linkages in primary industries (agriculture, mining and tourism) for SMEs; and improve efficiency in the delivery of products to business. An appropriate institutional framework and mechanisms for the implementation of the policy were put in place through the establishment of the Citizen Entrepreneurial Development Agency (CEDA). CEDA seeks to develop sustainable citizen-owned businesses through the provision of finance and the development of business skills. It offers three forms of assistance: *i)* financial assistance in the form of loans to citizens at subsidised interest rates, aimed at assisting those who wish to start or expand their businesses; *ii)* a training, monitoring and mentoring programme for SMEs; *iii)* a venture capital fund launched in September 2003 to provide risk capital to citizen-owned projects and/or joint ventures between citizens and foreigners. In all cases, the business owner is encouraged to contribute to the project cost in the form of equity or an owner's contribution so as to share the risk. The contribution

2. There are *i)* approximately 50 000 micro-enterprises (with fewer than six workers including the owner and annual turnover of less than 60 000 pula), of which 70 per cent are located in rural areas; 65 per cent of them are involved in trading, 25 per cent in manufacturing and about 10 per cent in other sectors; about 75 per cent of the micro-enterprises are owned by women, lack formal registration and operate from residential premises; *ii)* about 6 000 small enterprises (with fewer than 25 employees and annual turnover of 60 000 to 1 500 000 pula), of which 80 per cent are located in urban areas; approximately 40 per cent of small enterprises are in the services sector, 20 per cent in manufacturing, 16 per cent in retailing, 10 per cent in transport/distribution, 6 per cent in construction and 8 per cent in agriculture; and *iii)* about 300 medium-sized enterprises (with fewer than 100 employees and annual turnover of 1 500 000 to 5 000 000 pula), mostly involved in manufacturing activity.

Experiences in Financing SMEs: From FAP to CEDA

Entrepreneurs generally identify access to capital as their greatest challenge. In the case of Botswana, however, financing appears to be less problematic as the government has been providing adequate financial resources or guarantees to those intending to start up businesses. The policy of financing SMEs with 100 per cent government grants began in earnest in 1982 with the establishment of the Financial Assistance Programme (FAP). Prior to this period, several schemes had been introduced to provide government support to SMEs, such as the Botswana Enterprise Development Programme, the Rural Industrialisation Programme and the Business Advisory Service, but the failure rate was almost 100 per cent. In response, the FAP was introduced as an incentive and subsidy policy aimed at creating employment opportunities and encouraging investment in a range of economic activities. Its original intention was to stimulate investment in sustainable economic activities that would produce either exports or import substitutes. The FAP has been regularly reviewed and evaluated (in 1984, 1988, 1995, 2000), and appropriate reforms have been carried out in response to these evaluations. One of the criticisms of the FAP, just like its predecessors, is that it was giving free money to people without scrutiny. In addition, the massive administrative problems and the grant element of the scheme provided incentives for fraud and abuse. As a result, the review in 2000 concluded that the FAP was no longer effective in achieving its objective of promoting sustainable employment creation. Although some jobs were created as a result of the FAP, the cost of creating them was unsustainable and unacceptably high. The review also concluded that the FAP was inappropriate to 21st-century Botswana and that it was not addressing the main constraints to investment and the development of sustainable productive enterprises. The review therefore recommended that the FAP should be replaced with alternative forms of support for effective promotion of SMEs.

In 2001, the FAP was replaced by CEDA. Unlike its predecessors, CEDA provides financial assistance to SMEs in the form of subsidised loans (not grants) and risk sharing, although no collateral is required from beneficiaries of this scheme as long as they are citizens. The scheme is meant to be a soft window for citizens wishing to start a business or expand existing operations. CEDA also focuses on entrepreneurial and management training, monitoring and mentoring. This is important because adequate financing without the necessary knowledge and skills may result in a high rate of business failure. Very few Botswana citizens have the requisite education and training in business management and entrepreneurship. After independence, the school system did not help matters either, as it was heavily biased against self-employment. Instead, it churned out people prepared only for civil service employment. Moreover, government taxation and other policy measures promoted cattle farming as a comparatively low-risk, high-return form of investment, which introduced an inherent bias against SMEs. As a result, relatively few Botswana citizens engaged in business apart from highly fragmented, small-scale agricultural activities. Although CEDA has overcome some of these apparent weaknesses of SMEs in Botswana, the business failure rate is still high, albeit with a few success stories notably in the services industry, and particularly in the transport and information technology sub-sectors.

may be in cash, in kind or a combination of the two. Small and medium-scale projects may be assisted even if the owner cannot raise a contribution.

In October 2004, the government inaugurated the board of the Local Enterprise Authority (LEA) and the Small Business Council (SBC). The LEA is to provide assistance to SMEs in the preparation of business plans, feasibility studies and market surveys. It also aims to improve the business skills and competence of SME entrepreneurs through the provision of training and advisory services in entrepreneurship development, technology and marketing, and to identify SME firms with export potential and help them enhance their productivity and competitiveness for export markets. In addition, the LEA seeks to promote business linkages between SMEs and big industries, including the purchase of locally produced goods and services by larger firms, as well as to facilitate and co-ordinate the provision of infrastructure and facilities such as factory shells and working space. The SBC is to act as an advisory body that will have a consultative role regarding policy as it affects small business in Botswana. In this regard, it is expected to examine policies and procedures as they stand, with a view to identifying all policy constraints and impediments to the growth of the SME sector. In a further move to facilitate the development of local entrepreneurship, the President, in his State of the Nation Address on 8 November 2004, declared that by March 2005 a total of eight SME pilot clusters would be established to promote productivity growth through internal competition and economies of scale.

Political and Social Context

Botswana is the longest-lived democracy in Africa. The country holds elections every five years, and its ninth free and fair elections were held on 30 October 2004. The democratic process is enriched by the plurality of political parties, of which there are currently 12. The ruling Botswana Democratic Party (BDP), however, continues to hold a majority of seats in Parliament, fuelling the continuing fear of lack of proportional representation in Parliament. Such concerns eased greatly when the opposition parties made substantial gains in the 2004 election, winning 13 out of the 57 seats contested and leaving the ruling BDP with a sweep of 44 seats. Female participation in politics is encouraged at all levels in Botswana, even though in the October 2004 presidential and parliamentary elections, only four out of 57 elected MPs were women, while five of the recent appointments to cabinet are women (gender-related issues are discussed in detail below). The public sector has shown ample take-up of this important aspect of good governance. A full-fledged department dealing with gender development was established long ago in the Ministry of Labour and Home Affairs in order to co-ordinate gender development efforts in the country.

Botswana is rich, and at the same time very poor. Despite its macroeconomic success, Botswana has serious problems of poverty and high unemployment compared to countries at a similar level of economic development. It has been argued that the poverty situation in Botswana appears to be more of a structural problem, attributable to a rather narrow economic base which tends to limit opportunities for employment, a poor endowment of agricultural resources, a small and sparsely distributed population (1.7 million in 2001) and a very small and fragmented domestic market. It has also been posited that many of the poverty reduction programmes have not achieved the expected results due to a lack of effective co-ordination among different government departments, inadequate monitoring and evaluation of programmes, and insufficient participation by the poor in programme design, implementation, monitoring and evaluation. Recent statistical data (2003) show that the proportion of the population living below the poverty line in Botswana has declined to 30 per cent, from 59 per cent in the 1980s, owing to the government's national poverty reduction strategy. Given the high per capita income of this diamond-rich country, however, this is still considered to be too high. A related problem is unemployment, which is estimated at nearly 20 per cent of the labour force. The high unemployment rate may be attributed to a number of factors. First, the mining sector, which is the backbone of the economy, is an enclave that is unable to absorb the teeming numbers of unemployed due to its capital intensity. Second, many people engaged in the traditional agriculture sector have been forced to abandon this activity as a result of incessant problems of bad weather and disease. It should be noted that the Kalahari region of Botswana is prone to recurring drought and harsh weather, and the country has in the past experienced severe outbreaks of diseases such as cattle lung disease and foot and mouth disease, with devastating consequences on cattle herds and the beef industry. Third, the education system is not producing people with the right skills mix to be gainfully employed, particularly in the private sector, which has become increasingly skill-intensive. A number of new measures are being taken to address poverty and unemployment issues in Botswana. The government has set up a committee to submit a comprehensive progress report on the implementation of its Poverty Reduction Strategy Paper. Additionally, a total of 16 programmes estimated to cost 165 million pula are included in NDP9 under the respective sectoral projects of the concerned ministries. It is planned that in 2005 a poverty reduction programme advisor will be attached to the Ministry of Finance and Development Planning to oversee the poverty strategy programme. According to a recent UNDP Status Report publication on progress towards the Millennium Development Goals (MDGs), Botswana is on track to halving the proportion of people below the $1 per day poverty line by 2015.

Another major challenge facing Botswana is the devastating impact of the HIV/AIDS pandemic. The high prevalence rate of HIV/AIDS continues to reduce the capacity of some of the most productive members of society, thus affecting both employment and growth. This has already started to reverse some of the hard-earned economic and social gains of the past decades, as reflected in a lowering of life expectancy rates. The first case of HIV-related illness in Botswana was diagnosed in 1985. Since then, the virus has spread rapidly from urban to rural areas, leaving no district spared. During the 1993-2002 period, HIV spread rapidly among all age groups and the prevalence rate more than doubled, reaching 35.4 per cent at the end of the period. This figure, however, masks wide variations between genders and regions; in 2002, for instance, HIV prevalence among pregnant women by health district ranged from 27 per cent in Kweneng West district to 52.2 per cent in Selibe/Phikwe.

Botswana, supported by the international community, has devoted considerable resources to fighting the disease. The government is committed to giving high priority to combating the pandemic by designing and implementing appropriate medium- to long-term programmes. Through the National AIDS Co-ordinating Agency (NACA), the authorities recently prepared a comprehensive National Strategic Framework (NSF) for HIV/AIDS that consolidated all existing programmes related to the pandemic and established new programmes to prevent HIV transmission and to mitigate the impact of HIV/AIDS. This strategy is considered to be among the best in Africa. The government has increased budgetary allocations to the HIV/AIDS programme to 6 per cent of the total budget. In December 2003, 17 voluntary counselling and testing centres were up and running in the country, and some 100 000 people had made use of these services. Furthermore, over 11 450 patients were on antiretroviral (ARV) treatment. In addition, under the Prevention of Mother-to-Child Transmission (PMTCT) programme, as of February 2004, 11 329 pregnant women had received counselling, 71 per cent or about 8 000 of the mothers who received counselling were tested for HIV, 30 per cent of those tested were HIV-positive, and 1 697 were already being treated with the antiretroviral drug AZT. In addition, 1 543 infants who were found to be HIV-positive after birth were given AZT. The target of the government is to increase PMTCT uptake from 28 per cent of HIV-positive pregnant women to 50 per cent by March 2005. Routine voluntary HIV testing also started at the beginning of 2004 as part of an effort to address the stigma associated with HIV/AIDS. To complement the government's efforts, the Global Fund, an American non-governmental organisation, recently approved an $18.5 million fund to be used over a two-year period to assist in prevention, care and support actions targeting HIV/AIDS. This initiative will support the establishment of alternative care models such as hospices, day care centres and community-based counselling centres. National, bilateral and multilateral agencies continue to provide technical and financial support to efforts to address the HIV/AIDS pandemic in Botswana. The government is hopeful that it will halt the spread of HIV/AIDS and reverse the trend by 2015.

Other cross-cutting issues related to progress towards some of the MDGs, including universal education, gender mainstreaming and environmental sustainability. Botswana has already achieved the 100 per cent target for primary school enrolment and a 100 per cent transition rate from primary education to junior secondary education. Secondary school enrolment is currently above 90 per cent, and the immediate focus is on achieving an enrolment rate of 100 per cent within the next few years. The government is also striving to improve the overall quality of education at all levels, with strong emphasis on technical, management and vocational education. Botswana has already eliminated gender disparity in primary and secondary education. The net school enrolment ratio for girls is greater than that for boys, and Botswana is the only African country where the female literacy rate exceeds that for males. In view of all these remarkable statistics, one would have expected a much higher gender development index (GDI) for Botswana. The latest available GDI for Botswana is 0.581 for the year 2002, a score lower than that of countries such as Mauritius (0.778), Cape Verde (0.709), Equatorial Guinea (0.691) and South Africa (0.661). Moreover, the current involvement of women in economic and socio-political activities does not reflect the real progress made on the education and literacy fronts. As stated earlier, Botswana has only four women out of 57 MPs and five women out of 17 cabinet ministers. In terms of public sector employment, the figures are much more encouraging but still fall short of expectations: in 2003, women accounted for around 46 per cent, 39 per cent and 38 per cent of the total number of employees in central government, parastatals and local government respectively. Women are relatively disadvantaged in terms of access to social services and economic opportunities such as access to arable land and command of resources. They are also disproportionately afflicted by the HIV/AIDS pandemic. It is noteworthy, however, that the government, through its Vision 2016 and the NDP9, has initiated a comprehensive national programme towards increased gender mainstreaming in all spheres of the economy.

In the field of environmental protection, Botswana has sufficient water resources, particularly in the northern part of the country, to sustain a variety of wildlife. Water is also being tapped through the North-South Water Carrier pipeline to meet the domestic and industrial needs of the more urbanised South. The country faces two main problems: that of over-grazing and soil erosion in the western part of the country, with its attendant consequences for the ecosystem and agricultural development; and that of household waste and air pollution. The government is, however, committed to integrating environmental issues into development policies and programmes.

