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February 2018

2017 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR NAMIBIA

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2017 Article IV consultation with Namibia, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its February 26, 2018 consideration of the staff report that concluded the Article IV consultation with Namibia.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on February 26, 2018, following discussions that ended on December 12, 2017, with the officials of Namibia on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on February 6, 2018.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for Namibia.

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IMF Executive Board Concludes 2017 Article IV Consultation with Namibia

On February 26, 2018, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Namibia.

Since 2010, Namibia has experienced a period of exceptional growth. Growth was partly attributable to temporary factors. An expansionary fiscal policy, the construction of large mines and buoyant credit supported growth and better living standards. However, robust growth masked rising macroeconomic vulnerabilities and deteriorating productivity performance. Moreover, structural impediments have contributed to keep unemployment and income inequality unacceptably high.

With temporary expansionary factors ending, the economy has reached a turning point. GDP sharply decelerated in 2016 and contracted in 2017 as construction in the mining sector came to an end and the government began consolidating. With the economy contracting and Southern Africa Customs Union (SACU)'s receipts temporarily increasing, the current account balance improved significantly. However, despite significant fiscal adjustment, the public debt ratio continued to increase and almost doubled over the last four years, exceeding in 2017 the median of the countries at the lowest tier of investment grade. Credit growth to the private sector has slowed down reflecting both banks' tight funding constraints and low demand from highly leveraged households. Headline inflation declined to 5.2 percent in 2017, from 7.3 at end 2016 and, in the context of the currency peg, the Bank of Namibia has followed the South African Reserve Bank (SARB) and reduced its policy rate.

The outlook remains positive with considerable vulnerabilities and risks. Growth is projected to resume in 2018, as mining production ramps up, construction activity stabilizes and manufacturing recovers, before converging to a long-term rate of about 3½ percent, below the average of recent years. Inflation is anticipated to remain below 6 percent. However, as SACU revenues are expected to decline, in the absence of policy action, the fiscal deficit would remain large and public debt would continue rising and approach 70 percent of GDP by 2022. On the positive side, the current account deficit is expected to narrow on average to around 6 percent of

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

GDP on the back of larger mining exports, but international reserve coverage is projected to gradually decline.

Downside risks dominate the outlook. They stem mainly from possible fiscal slippages that could undermine policy credibility, lower demand for key exports, further declines in SACU revenue, and slower recovery in mining and construction activities. Extensive macro-financial linkages could amplify the negative impact of shocks.

Executive Board Assessment[2]

Directors commended the authorities for Namibia's rapid growth, rising living standards, and macroeconomic stability achieved over the past years. Directors noted, however, that the country faces significant economic challenges and structural issues. Factors that temporarily boosted growth have come to an end, public debt is rising, reserve coverage is low, and risks and vulnerabilities in the financial sector remain. In addition, unemployment and inequality remain elevated. Against this backdrop, Directors emphasized the need for sound policies and structural reforms to ensure fiscal sustainability, strengthen the financial sector, and generate sufficient jobs to manage the upcoming demographic changes and reduce income inequality.

Directors welcomed the authorities' fiscal adjustment efforts and emphasized that additional consolidation is needed to ensure debt sustainability. They broadly agreed that efforts should be spread over the next years and include expenditure and revenue measures that support long-term growth, while addressing distributional concerns. In this regard, Directors saw merit in containing public wage growth, rationalizing transfers to extra-budgetary entities, and reducing tax exemptions. They welcomed the recent increase in social assistance programs while calling for better targeting to protect the poor and strengthen the distributional impact of public spending. To buttress the credibility of the adjustment, the authorities should improve budget formulation, tighten expenditure controls, and strengthen revenue administration and the management of extra-budgetary entities. Directors underscored the need to monitor and manage fiscal risks, particularly from off-budget financing of large investment projects.

Directors noted that the additional fiscal adjustment will support the ongoing macroeconomic adjustment process and contribute to bring the external position broadly in line with fundamentals. They agreed that, in the context of the peg with the South African rand, the Bank of Namibia (BoN) should maintain the policy rate in line with the South African Reserve Bank, and use macroprudential tools to manage risks from the leveraged private sector.

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

Directors commended the early steps taken in implementing the FSSA recommendations. They underscored the importance of monitoring and managing risks from banks' concentrated balance sheets, financial institutions' interconnections, and public and private sector indebtedness. Directors encouraged the authorities to address the existing supervisory and regulatory gaps in the non-bank financial sector. They also saw merit in the development of an explicit macroprudential mandate for the BoN, as well as a crisis management and resolution framework.

Directors emphasized the importance of implementing structural reforms to boost job creation to reap the benefits of the upcoming demographic changes and achieve more inclusive growth. They called for measures to focus on reducing skill mismatches through improving access and quality of secondary and higher education and training; better aligning wage and productivity dynamics; and enhancing the business environment.

Namibia: Select Economic Indicators

	2014	2015	2016	2017	2018	2019	2020	2021	2022
				Est	Proj	Proj	Proj	Proj	Proj
	(percentage change, unless otherwise indicated)								
National account and prices									
GDP at constant prices	6.4	6.0	1.1	-1.2	1.2	3.3	3.8	3.5	3.5
GDP deflator	6.3	0.4	7.9	6.1	5.8	5.8	5.7	2021	5.8
GDP at market prices (N$ billions)	139	148	161	169	181	197	217	237	259
GDP at market prices (Fiscal Year) (N$ billions)	141	151	163	172	185	202	222	243	266
GDP per capita (US$, constant 2000 exchange rate)	8,941	9,334	9,989	10,395	11,035	11,951	13,008	14,115	15,316
Consumer prices (end of period)	4.6	3.7	7.3	5.2	5.7	5.8	5.8	5.7	5.8
External sector									
Exports (US$)	-0.1	-13.2	4.3	13.5	9.2	7.6	6.3	3.8	3.5
Imports (US$)	9.9	-5.5	-12.7	-5.4	9.0	6.8	8.5	4.2	3.9
Terms of trade (deterioration = -)	4.2	-5.2	-7.1	0.5	1.1	-1.0	-1.4	-1.6	-1.4
Real effective exchange rate (period average)	-5.8	-2.4	-3.1	10.6	n.a.	n.a.	n.a.	n.a.	n.a.
Exchange rate (N$/US$, end of period)	11.6	15.6	13.7	13.5	n.a.	n.a.	n.a.	n.a.	n.a.
Money and credit									
Domestic credit to the private sector	17.9	13.8	8.6	4.5	4.9	5.4	5.8	6.3	6.4
Base money	35.7	-5.0	24.7	10.0	10.0	10.0	10.0	10.0	10.0
M2	6.9	10.2	4.9	6.3	7.0	9.2	9.7	9.4	9.4
Interest rate (percent)	6.0	6.5	7.0	…	…	…	…	…	…
	(percent of GDP)								
Investment and Savings									
Investment	33.6	34.6	25.7	22.8	23.5	23.8	24.0	23.6	23.9
Public	7.4	9.2	9.1	7.3	7.5	7.3	7.0	6.1	5.9
Private	26.0	24.9	15.1	15.5	16.0	16.5	17.0	17.5	18.0
Change Inventories	0.2	0.5	1.4	0.0	0.0	0.0	0.0	0.0	0.0
Savings	24.1	20.3	11.5	21.2	19.9	18.6	18.2	17.8	18.1
Public	0.4	-1.6	-3.6	-1.8	-3.2	-5.2	-5.0	-5.2	-5.7
Private	23.7	21.9	15.1	23.0	23.1	23.8	23.2	23.0	23.8
Central government budget 1/									
Revenue and grants	35.4	34.6	31.2	34.2	31.6	30.0	30.9	30.6	30.6
Of which: SACU receipts	12.9	11.5	8.6	11.4	9.4	7.8	8.6	8.4	8.4
Expenditure and net lending	42.1	43.2	40.5	39.4	40.1	39.9	39.9	39.4	39.9
Primary balance (deficit = -)	-5.2	-6.9	-6.7	-2.2	-5.1	-5.9	-4.5	-3.9	-3.6
Overall balance	-6.7	-8.7	-9.3	-5.2	-8.5	-9.9	-9.0	-8.8	-9.3
Overall balance: Non-SACU	-19.5	-20.1	-18.0	-16.6	-17.9	-17.6	-17.6	-17.2	-17.7
Public debt/GDP	24.8	39.4	44.3	46.5	51.4	57.3	61.9	65.7	69.7
Of which: domestic	16.2	21.3	28.9	30.4	33.9	40.1	45.5	50.3	56.1
Gross public and publicly guaranteed debt/GDP	28.4	44.2	49.6	54.0	59.5	66.0	71.2	75.7	80.3
External sector									
Current account balance									
(including official grants)	-9.4	-14.1	-14.1	-1.5	-3.6	-5.1	-5.7	-5.7	-5.7
External public debt (including IMF)	8.0	13.1	17.1	15.9	17.0	17.0	16.3	15.4	13.8
Gross official reserves									
US$ millions	1,198	1,580	1,791	2,193	2,158	2,155	1,799	1,588	1,579
Percent of GDP	10.0	16.7	15.2	17.5	16.5	15.6	12.3	10.3	9.7
Months of imports of goods and services	2.0	3.0	3.7	4.1	3.8	3.5	2.8	2.4	2.3
External debt/GDP 2/	43.0	48.2	60.2	60.6	64.4	66.3	67.3	68.5	68.7
Memorandum item:									
Population (in million)	2.2	2.3	2.3	2.3	2.4	2.4	2.4	2.4	2.4

Sources: Namibian authorities and Fund staff estimates and projections.

1/ Figures are for fiscal year, which begins April 1.

2/ Public and private external debt.

NAMIBIA

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION

February 9, 2018

KEY ISSUES

Context. Namibia has experienced a period of exceptional growth and economic stability, but faces significant policy challenges and structural issues. Strong growth was partly attributable to temporary factors that have come to an end. Public debt is rising and reserve coverage is below adequate levels. Financial institutions' interconnections and exposures, and elevated private sector indebtedness pose macro-financial risks. Structural impediments have contributed to keep unemployment and income inequality unacceptably high.

Outlook and challenges. With temporary expansionary factors ending, growth contracted in 2017 and is expected to resume in 2018. Downside risks weigh on the outlook, and emanate from possible fiscal slippages that could undermine policy credibility; lower demand for key exports; and declines in SACU revenue. The impact of shocks could be amplified by macro-financial linkages. Namibia's key policy challenges are to manage the ongoing adjustment process and bring public debt on a sustainable path, address macro-financial risks and financial sector vulnerabilities, and generate sufficient jobs to manage upcoming demographic changes and reduce income inequality.

Fiscal and monetary policy. Fiscal adjustment is needed to support the ongoing economic adjustment and bring public debt on a sustainable path. Fiscal adjustment needs to be spread over time and include expenditure and revenue measures that support long-term growth and address distributional concerns. Improved targeting of social cash transfers would better protect the poor. Reforms to improve public financial management systems, revenue administration and the management of extra-budgetary entities are essential to implement credible consolidation plans and contain fiscal risks. To support the peg, the BoN should maintain the policy rate at par with the SARB.

Financial stability. The 2018 FSAP recommended that risks from banks' concentrated balance sheets, financial institutions' interconnections, and private sector indebtedness be monitored and managed. The ongoing reviews of banks' asset quality and liquidity regulations are welcome steps to improve the banking sector oversight. New regulations to address regulatory and supervisory gaps for NBFIs should be sequenced. Assigning the BoN an explicit macroprudential mandate, until the Financial Stability Council is set up, is critical to manage macro-financial risks. Developing a full crisis management and resolution framework is needed.

Structural reforms. Selected structural reforms could boost employment and help reap the benefits of the upcoming demographic changes. Reforms to reduce skill mismatches, better align wage and productivity dynamics, and simplify business regulations would have the highest impact on employment and income inequality.

Approved By
Anne Marie Gulde Wolf (AFR) and Daria Zakharova (SPR)

Discussions for the 2017 Article IV consultation took place in Windhoek during November 30-December 12, 2017. The team comprised Mr. Palomba (head), Mses. Ganum and Jack (both AFR), and Messrs. Simone and Torres (both AFR). Mr. Mathieu (MCM) also joined the mission. Mr. Sishi (OED) participated in the discussions. Mr. Radick and Ms. Prado de Guzman provided research and editorial assistance for the preparation of this report.

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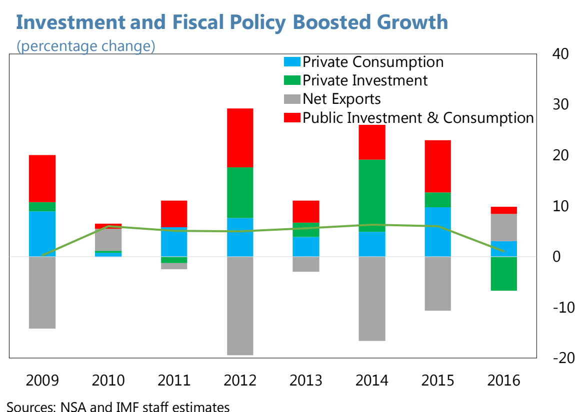
CONTEXT: ECONOMY AT A TURNING POINT

1. Since 2010, Namibia has experienced a period of exceptional growth fueled in part by temporary factors, while vulnerabilities have risen and structural challenges remain. Despite being a small commodity-dependent economy exposed to external shocks, between 2010–2015, Namibia's annual GDP growth averaged 5½ percent and living standards improved (Figure 1). This strong performance was in part due to the construction of large mines and an expansionary fiscal policy that temporarily boosted investment.[1] The peg with the South African rand contributed to contain inflation.[2] However, strong growth masked a deteriorating productivity performance, that negatively contributed to the recent growth dynamics, while macroeconomic vulnerabilities rose (Figure 2). Large fiscal deficits led to a sharp increase in public debt. The current account deficit widened, and international reserve coverage fell below adequate levels. Rapid credit growth financed the economic expansion, but also fueled fast-rising house prices and elevated private sector indebtedness. Yet, unemployment has remained high and inequality, although declining, is among the highest in the world.



2. In 2016, the economy reached a turning point and sharply decelerated and began contracting in 2017. The engines that temporarily boosted growth grounded to a halt and set off a complex adjustment process (Table 1).

- Real GDP growth decelerated in 2016 to 1.1 percent, as construction in the mining sector came to an end and the government began consolidating. Public and private investment declined, and consumption decelerated as unemployment rose. The weak performance continued in 2017, with the economy contracting in the first three quarters of the year as construction and retail and wholesale activities declined further.

- Despite weak domestic demand, the 2016 current account deficit remained large and wider than justified by macroeconomic fundamentals (Annex I). Lower imports and improved exports reduced the trade deficit. However, the current account deficit remained unchanged at 14.1 percent of GDP, as SACU receipts declined and income flows deteriorated. Moreover, external vulnerabilities built up. External public and private debt increased to 60.2 percent of

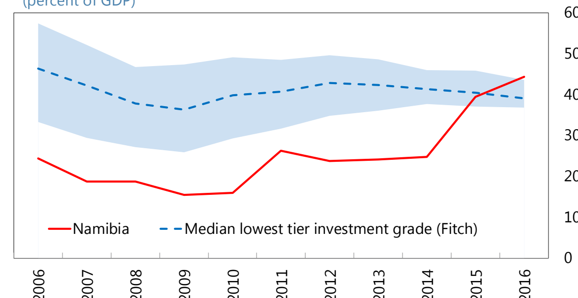
[1] Diamonds, copper, gold, uranium and zinc constitute about 40–45 percent of the country's goods exports, and account for about 8 percent of GDP (services account for about 60 percent of GDP). Over recent years, the construction of a large uranium mine (Husab) has boosted investment and is expected to make Namibia one of the world's largest uranium producers.

[2] Namibia, with Lesotho, South Africa and Swaziland, is a member of the Common Monetary Area (CMA) and its currency is pegged at par to the South African rand. CMA members and Botswana constitute the South African Customs Union (SACU).

GDP (48.2 percent in 2015), and the net international investment position turned negative. On the positive side, international reserve coverage improved to 3.7 months of projected imports, partly sustained by Bank of Namibia (BoN)'s swap operations.[3] With the economy contracting, in the first three quarters of 2017, the trade deficit narrowed further driven by import compression and the current account balance sharply improved because of a temporary increase in SACU receipts (Figure 3).

3. **The government began implementing a medium-term consolidation plan to bring public finances on a sustainable path, and contributed to the economic slowdown.** Despite a sharp decline in SACU revenue (3 percent of GDP), the FY16/17 deficit only increased by about ¾ percentage point of GDP to 11.1 percent of GDP (10⅓ percent in FY15/16), as the authorities implemented substantial reductions in non-wage expenses and capital outlays (Tables 2–3).[4] However, most of the spending reductions were introduced late in the fiscal year, prompting a sudden policy correction that led to the accumulation of about N$3.9 billion in domestic arrears (2.4 percent of GDP) and weighed heavily on the 2017 growth.[5] As the fiscal deficit remained large, public debt increased to 44.3 percent of GDP (including domestic arrears), above the median of the countries at the lowest tier of investment grade. Gross financing needs remained high (about 18 percent of GDP) and, as the authorities increasingly tapped domestic markets, yields on government debt rose (Figure 4). Against this background, Moody's and Fitch lowered the sovereign credit rating to below investment grade.

Government Debt Higher than Lowest Tier Investment Grade Countries
(percent of GDP)



Sources: MoF, WEO and IMF staff estimates
Note: Shaded area excludes top and bottom 20 percent of the distribution

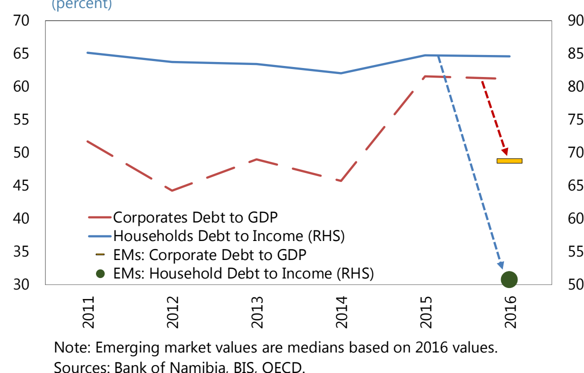
4. **With the economy adjusting, credit to the private sector and housing prices growth decelerated amid still elevated household indebtedness.** After averaging 14 percent between 2010–15, private sector credit growth started declining in 2016 and reached 4.5 percent at end 2017 (Figure 5). The deceleration reflected both banks' tight funding constraints and low demand from a highly leveraged private sector. Against this background, both corporate and household lending (including individuals' mortgage loans) decelerated, contributing to contain the annual increase in

[3] Since 2015, the BoN has participated in asset swap agreements, mainly with the government pension fund, of about N$9 billion (about US$670 million).

[4] Deficit figures reflect below-the-line financing information and include domestic arrears. Preliminary above-the-line revenue and expenditure data suggest a FY16/17 deficit of 9⅓ percent of GDP, including arrears. SACU revenues have been declining since FY14/15. The sharp decline in FY16/17 reflected past trends and an adjustment to offset past year overpayments.

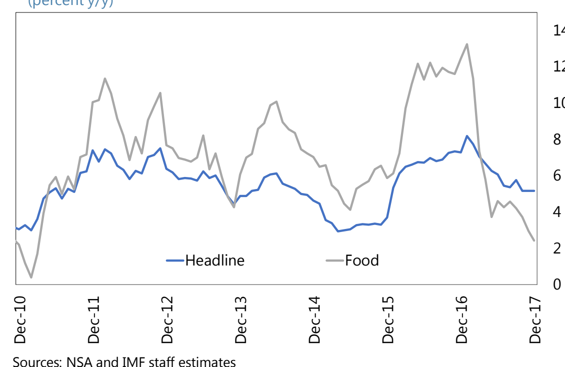
[5] Arrears mainly occurred in non-wage operational and capital spending and have been largely cleared.

house prices to 7 percent (9 percent on average over the last five years).[6] However, household and corporate leverage remained high and close to the level of more advanced economies (Figure 6). At the same time, banks' asset quality showed signs of deterioration, with NPLs increasing, albeit from very low levels. As government's financing needs remained high, banks' direct exposure to the public sector rose, and holdings of government securities reached about 10 percent of banks' assets.



Note: Emerging market values are medians based on 2016 values.
Sources: Bank of Namibia, BIS, OECD.

5. **Against this background, headline inflation has recently declined and the central bank has eased the monetary stance.** After averaging 7.3 percent in 2016, headline inflation peaked to 8.2 percent in January 2017, mostly because of high food prices, reflecting a prolonged drought and increases in administrative prices. Since then, inflation has rapidly declined and reached 5.2 percent in December 2017, reflecting better crop yields and economic slack. In the context of the currency peg, the BoN followed the South African Reserve Bank (SARB), and in August reduced its policy rate to 6.75 percent, citing lower projected inflation.



Sources: NSA and IMF staff estimates

6. **Authorities are adjusting their macroeconomic and developmental policies to deal with the new economic realities.** They have recently issued a new national development plan (NDP) emphasizing private sector financing of large infrastructure projects, and prioritized the implementation of high impact projects and policies in the social sectors. Broadly following staff's past advice, they have also embarked on medium-term fiscal adjustment plans, and adopted LTV ratio limits for non-primary residential houses to manage fast-rising real estate market prices. With the economy decelerating, and in preparation of the FY18/19 budget, they have recently revised their fiscal adjustment plans to better consider the economic cycle.

OUTLOOK AND RISKS

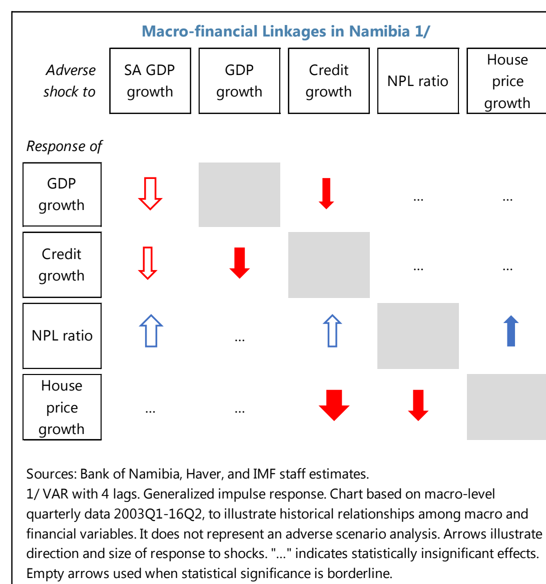
7. **With the economy adjusting, GDP contracted in 2017 and is expected to resume growing in 2018, against a background of significant vulnerabilities.** After three negative quarters, real GDP is projected to have contracted by 1.2 percent in 2017. Weak construction activities and the ongoing fiscal correction more than offset improvements in mining, as new mines began production, and in agriculture, as the drought came to an end, leading to the contraction. Growth is projected to resume in 2018, as mining production ramps up, construction activities stabilize and manufacturing recovers,

[6] The introduction in March 2017 of loan-to-value (LTV) limits for nonprimary houses may have contributed to further decelerate growth in mortgage lending.

before converging to a long-term rate of about 3½ percent, below the average growth registered in recent years (Annex II). As the economy recovers, headline inflation is projected to rise somewhat, but remain below 6 percent. However, SACU revenues are expected to decline and, in the absence of additional actions, the fiscal deficit would remain large and public debt would continue rising. Government's financing needs would absorb an increasing amount of domestic financial resources, possibly crowding out private sector credit. On the positive side, compared to 2016, structurally higher mineral exports and low imports would halve the trade deficit and reduce the current account deficit to around 5–6 percent of GDP by 2019 (Table 4). However, international reserve coverage would gradually decline and, in this context, external financial inflows and SACU receipts will remain critical to guarantee macroeconomic stability.

8. **Risks to the outlook are tilted to the downside.** The main risk arises from possible fiscal slippages that may undermine confidence in the government's ability to control public finances. Additional domestic risks arise from slower recovery in the mining and construction sectors, and sudden corrections in the overvalued housing market. External risks are also prominent. They emanate from further declines in SACU revenue if growth in South Africa deteriorates;[7] and, lower demand for key exports and subdued commodity prices, as China addresses domestic imbalances, protectionist pressures rise, and if growth in trading partners and Angola slows down. Additional risks arise from tighter global financial conditions prompted by rising US policy rates (Annex III).

9. **Macro-financial feedback loops could amplify the negative impact of shocks and prompt a sharper adjustment.** If external risks materialize and fiscal imbalances persist, exports and GDP growth would decline and external and fiscal balances deteriorate. Public debt would increase faster, and international reserve coverage decline. The impact could be amplified by further fiscal slippages that might undermine the credibility of the government's consolidation plans. Feedback loops could intensify these effects. With weak demand, private sector credit would decelerate, prompting a decline in house prices. With elevated household indebtedness, these developments would negatively affect banks' asset quality and financial intermediation, with strong feedback effects on growth, particularly if negative expectations take hold.[8]



Sources: Bank of Namibia, Haver, and IMF staff estimates.
1/ VAR with 4 lags. Generalized impulse response. Chart based on macro-level quarterly data 2003Q1-16Q2, to illustrate historical relationships among macro and financial variables. It does not represent an adverse scenario analysis. Arrows illustrate direction and size of response to shocks. "..." indicates statistically insignificant effects. Empty arrows used when statistical significance is borderline.

[7] The Namibia economy is closely linked to South Africa through three main channels: SACU revenue, imports of goods and services, and highly interconnected financial systems. Since Namibia mainly exports to global markets and not to South Africa, real spillovers appear limited (see "The Mystery of Missing Real Spillovers in Southern Africa", IMF, 2014).

[8] For possible adverse macroeconomic scenarios reflecting the impact of severe shocks and non-linear effects, see IMF Country Report 15/276, and the 2018 Financial Sector Assessment Program (FSAP) report, forthcoming.

Authorities' Views

10. The authorities concur that the economy is going through a complex adjustment process and broadly agree with the medium-term outlook and staff's risk assessment. They expect, however, GDP growth in 2017 to contract somewhat less than staff, due to a lower decline in government's activities and a strong recovery in manufacturing. They underscored the risks to the outlook from external shocks and acknowledged that further fiscal slippages may undermine the credibility of the government's consolidation plans. They concurred that without policy action, public debt dynamics are not sustainable and that macro-financial loops could amplify the negative impact of shocks. To lessen risks, they have devised plans to contain the FY17/18 deficit within budget projections while avoiding further arrears accumulation. They also intend to press ahead, in the context of the upcoming FY18/19 budget, with the revised medium-term adjustment plans announced in the November 2017 Medium-Term Policy Statement.

POLICY DISCUSSIONS

Discussions focused on the policies to manage the ongoing adjustment process and preserve macroeconomic stability by: (i) implementing credible fiscal adjustment plans to contain public debt dynamics and support long-term growth; (ii) managing macro-financial risks from a large and interconnected financial sector; and (iii) advancing structural reforms to leverage the growth benefits from the ongoing demographic transition and reduce unemployment and income inequality.

A. Calibrating and Designing Fiscal Adjustment

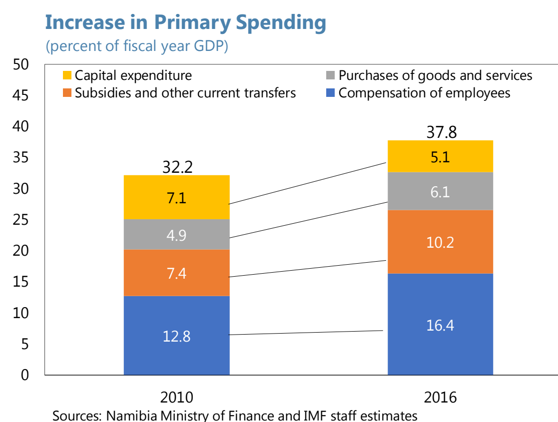
11. The FY17/18 Budget and 2017 Medium-Term Policy Statement envisaged a continuation of fiscal adjustment policies started in 2016 to stabilize public debt dynamics. The FY17/18 budget forecast significant reductions in non-wage current and capital spending to yield a deficit of 3.4 percent of GDP (5.6 percent including arrears payments).[9] Over the medium term, a gradual reduction in public spending (about 2 percentage points of GDP per year) would reduce the fiscal deficit and stabilize public debt dynamics. However, the extent and quality of measures underpinning the planned medium-term spending reduction remain to be identified.

12. Under current policies, staff estimates the fiscal deficit to narrow in FY17/18, but with SACU revenue declining, future deficits would remain large and public debt continue to rise. Despite higher revenue than projected by the authorities, staff expect rising wages and spending pressures from the previous year to bring the FY17/18 fiscal deficit to about 5 percent of GDP. While the projected deficit is lower than in the previous year (9.3 percent in FY16/17), the decline largely

[9] With the November 2017 Mid-Year Budget Review and Policy Statement, the authorities acknowledged some spending pressures and issued a supplementary budget, revising the deficit to 4 percent of GDP (before arrears repayments).

reflects temporarily higher SACU revenue and is not sustainable.[10] Over the medium term, SACU revenues are expected to decline and, in the absence of additional actions, the fiscal deficit is projected to increase to around 9–10 percent of GDP.[11] Against this background, public debt would continue rising and approach 70 percent of GDP by 2022, and government's gross financing needs would average about 21 percent of GDP per year, creating financing pressures and possible funding risks. This fiscal outlook is subject to significant risks. The main risks arise from larger contingent liabilities as the government plans to boost public-private partnerships (PPPs) and extra-budgetary financing of large infrastructural projects (Box 1; Annex IV).

13. Additional fiscal adjustment is needed to bring public debt on a declining path and support the ongoing macroeconomic adjustment. Under staff's baseline, 5–6 percent of GDP in measures is needed over time to reach a primary balance that can bring the public debt ratio on a declining path. While ambitious, the size of the adjustment is consistent with the authorities' plans and equivalent to the increase in spending observed in recent years. To contain the negative effects on growth, the adjustment should be spread over time and the pace in part depends on available financing.[12] Recent budget support from international financial institutions offers the opportunity to spread the adjustment over the next three years, starting with the FY18/19 budget, while still delivering sustainable medium-term debt dynamics.[13] However, uncertainty in South Africa might reduce Namibia's financing opportunities from the South African market, its main external debt market, and dictate a more frontloaded approach at the cost of lower growth. Additional fiscal consolidation will support the ongoing economic adjustment process and reduce external imbalances. It would curb domestic demand, and help reach an external position broadly in line with medium-term fundamentals, while allowing the accumulation of adequate levels of international reserves (Annex I). In addition, it would contain government's gross financing needs, and reduce financing and crowding out risks. However, in the near term, the adjustment would lower growth with possible negative effects on banks' asset quality.



Sources: Namibia Ministry of Finance and IMF staff estimates

[10] The FY17/18 estimated deficit excludes the payment of previous year's arrears, which are reflected in the FY16/17 deficit figure. However, it includes about 0.8 percent of GDP in capital originally classified outside the budget.

[11] The decline in FY18/19 SACU revenue reflects the latest SACU revenue agreement. SACU revenues are expected to stabilize thereafter as a share of GDP to historically low levels as import growth in South Africa, the main contributor to the SACU revenue pool, moderates.

[12] For discussion on fiscal multipliers in Namibia, see IMF Country Report 16/374. Given the openness of the economy and the relatively low fiscal multipliers, staff estimated that fiscal adjustment may negatively affect annual growth on average by 0.6 percentage points per year over the consolidation period.

[13] The authorities have recently negotiated a budget support and project financing loan with the African Development Bank. In addition, they have decided to increase domestic asset requirements for NBFIs, requiring NBFIs to convert part of their foreign investment into domestic assets.

Staff Medium-Term Projections (Reform Scenario) 1/
(Percent of GDP, unless otherwise specified)

	2016	2017	2018	2019	2020	2021	2022
Real GDP Growth (annual change)	1.1	-1.2	0.8	2.6	3.2	3.6	3.7
Credit to the Private Sector (annual change)	8.6	4.5	5.5	7.2	8.4	9.5	9.5
Fiscal Balance	-9.3	-5.2	-7.0	-6.6	-3.8	-3.1	-3.0
Revenue (including SACU receipts)	31.2	34.2	32.0	30.8	32.2	32.0	32.2
o/w additional measures (cumulative)	…	…	0.4	0.9	1.3	1.3	1.3
Expenditure	40.5	39.4	39.0	37.4	36.0	35.1	35.2
Current Expenditure	35.4	35.3	34.4	33.2	31.8	31.6	31.7
o/w additional measures (cumulative)	…	…	-1.3	-2.6	-3.9	-3.9	-3.9
Capital Expenditure	5.2	4.1	4.6	4.2	4.2	3.5	3.5
Fiscal Balance (excluding SACU)	-18.0	-16.6	-16.4	-14.5	-12.5	-11.6	-11.5
Primary Balance	-6.7	-2.2	-3.5	-2.8	0.3	1.0	1.3
Primary Balance (excluding SACU)	-15.3	-13.6	-13.0	-10.7	-8.5	-7.5	-7.2
Adjustment	…	…	-1.7	-3.5	-5.2	-5.2	-5.2
Gross Financing Needs	18.0	17.9	19.2	16.7	15.2	17.5	14.4
Public Debt (excl. guarantees)	44.3	46.5	50.1	53.1	53.0	51.9	50.7
Current Account Balance	-14.1	-1.5	-2.7	-3.0	-2.3	-2.3	-2.3
Gross International Reserves (months of imports)	3.7	4.2	4.3	4.5	4.6	4.8	4.9

1/ Fiscal data refer to fiscal year. Fiscal adjustment equally spread over three years starting in FY18/19, and a quarter is assumed to come from revenue.

14. Consolidation efforts should be anchored in long-lasting measures that address the sources of recent fiscal deterioration, and support long-term growth and better income distribution. Reductions in large and fast-rising expenditure items (e.g., wages, transfers), while protecting social assistance programs, and well-designed increases in domestic revenue (e.g., ¼ of the adjustment package) could enhance long-term growth and protect the poor. Staff put forward a menu of options being mindful of potentially undesirable distributional effects and local institutional capacity. On the spending side, with wages and transfers to extra-budgetary entities accounting for about 70 percent of primary spending, staff proposed as priorities to: (i) contain the size of the already large wage bill by constraining salary indexation and allowances, and limiting new hires; and, (ii) reduce transfers to extra-budgetary entities while rationalizing their functions. Staff also suggested to: (iii) prioritize capital outlays to further strengthen investment efficiency; and (iv) improve the efficiency of social spending by conducting spending reviews of social programs (Figure 7). Over time, these measures are likely to bring wage dynamics closer to productivity trends, with positive effects on labor market outcomes and long-term growth (Annex V). Improved targeting of cash transfers is also needed to

Possible Fiscal Adjustment Measures FY 18/19 – FY20/21
(In percent of GDP)

Measure	Budget Savings by FY20/21
Total	Up to 8.2
Expenditure measures	Up to 6.5
Contain the wage bill: limiting salary indexation and new hiring	2.5-3.5
Reduce transfers to public enterprises: reforming large enterprises (e.g., Air Namibia, Transnamib Holding)	0.2-0.4
Rationalize transfers to other extra-budgetary entities (e.g., sub-national governments)	1.5-2.0
Improve targeting of social grants, allowances and other benefits	0.7
Revenue measures	Up to 1.7
Increase domestic levies (e.g. fuel levy, luxury goods)	0.3
Increase SACU excises above SACU rates (e.g. alcohol,	0.8
Remodule PIT rates	0.3-0.6
Strengthen the corporate income tax and close tax loopholes (e.g., ringfence loss carry forward; limit interest deductions; introduce withholding tax on domestic and foreign sourced dividends)	++
Broaden the VAT base (e.g., eliminate zero rating and exemptions on real estate, telecommunications, fuel products	++

Sources: MOF and IMF staff stimates

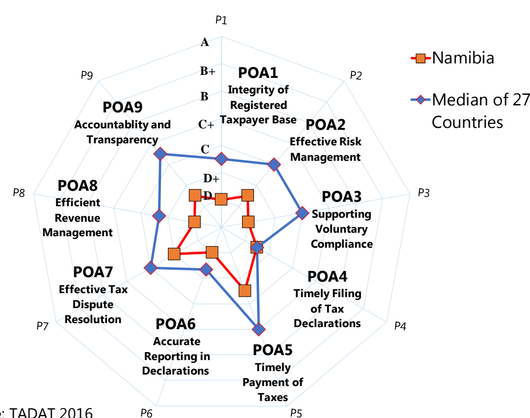
better protect the poor, and strengthen the distributional impact of government's spending.[14] On the revenue side, measures should aim at creating a level-playing field to support growth. Measures should focus on: reducing tax incentives and exemptions, eliminating tax loopholes (e.g., under the corporate income tax and the VAT), and boosting consumption taxation (Annex VI). The latter may require strengthening social transfers to offset possible negative redistributive effects from large reforms. Furthermore, improving the progressivity of the personal income tax could contribute to the adjustment and ensure more equitable burden sharing.

15. Fiscal adjustment should be supported by structural reforms to strengthen public financial management and tax administration, and rationalize extra-budgetary public entities. Improving budget formulation, expenditure controls, and revenue collection and streamlining public entities are critical steps to design and implement credible consolidation plans.

- *Public financial management (PFM)*. In the near term, continuing to strengthen commitment controls and budget execution processes is essential to manage a tight budget and prevent new arrears. Strengthening budget preparation and fiscal reporting, and the macro-fiscal forecasting capacity at the ministry of finance would support the design of credible budgets and adjustment plans. The planned introduction of a new information system is crucial in this respect. Moreover, improving public investment management (e.g., project appraisal) and undertaking spending reviews of social programs would support more efficient and growth-enhancing public spending. The recent enactment of the Public Procurement Act and the extensions of new procurement rules to extra-budgetary entities could contribute to reduce costs, particularly in public entities. Finally, the approval of the long-standing PFM bill should provide the legal framework to guide medium-term reforms.

- *Revenue administration*. Despite pockets of progress, there is significant room to improve tax administration to approach the standards of comparable countries. The authorities' efforts to push ahead with the creation of a semi-autonomous revenue authority, planned for 2019, are therefore welcome. However, reaping the benefits of such a change may take time. While creating a new revenue administration, the authorities should focus on addressing key deficiencies in business processes, managing taxpayer information systems, and human resource management. In the near term, it is particularly important to develop further the capacity to conduct in-house audits for large taxpayers,

Effectiveness of Namibia Revenue Administration



Source: TADAT 2016
Note: Median largely includes low and middle income countries.

[14] For a discussion of the need for better targeting cash transfers in Namibia, see IMF Country Report 16/373 and NSA and World Bank 2017, Does Fiscal Policy Benefit the Poor and Reduce Inequality in Namibia?

design a specific strategy to manage medium-sized taxpayers, and introduce a presumptive regime for smaller ones (Annex VI). The authorities should also avoid new tax amnesties on tax arrears that are likely to reduce tax compliance, particularly in the absence of a strong administration.

- *Extra-budgetary entities and public enterprises (PE).* With a few exceptions, public entities and enterprises represent a significant burden for public finances and a source of significant fiscal risks for the central government.[15] At the same time, they deliver essential services (e.g., electricity, water, education, health), operate in key network industries, and are critical to infrastructure development. The authorities are aware that these entities face performance and governance challenges, and intend to adopt a new governance structure to improve the performance of the sector.[16] In addition, reforms should focus on key areas, including: (i) review the scope and the off-budget mandate of all entities and enterprises, closing and merging unneeded ones; (ii) enforce a stronger control framework (e.g., creation of new entities, board appointments, business plans, performance agreements, borrowing powers); (iii) review cost structures, including the often large wage costs; and, (iv) establish clear demarcations between social, regulatory, and commercial activities to strengthen accountability and efficiency, and eventually foster greater private sector participation.

16. Concrete actions are needed to monitor and control fiscal risks, particularly from off-budget financing investment vehicles, while still supporting growth. With the budget footprint expected to shrink, the authorities have embarked on several initiatives to expand off-budget financing of public infrastructures, including through PPPs, PEs' investment programs, and special purpose vehicles. However, off-budget financing may create significant explicit and implicit contingent liabilities for the government and reduce the transparency of fiscal accounts (Box 1). Moreover, the announced increase in domestic asset requirements for non-bank financial institutions (NBFIs) would expand available domestic financing for new projects, but risks heightening the sovereign-financial sector nexus and increasing financial stability risks.[17] To mitigate these risks, it is critical to preserve transparency standards in the compilation of fiscal accounts, develop a fiscal risks framework, and limit increases in domestic asset requirements.

17. As the government consolidates, the central bank should continue supporting the peg. The BoN should continue maintaining the policy rate in line with the SARB. Moreover, it should consider using well-targeted macroprudential tools to manage risks from the highly leveraged private sector and still overvalued real estate assets.

[15] For an analysis of the budget burden of extra budgetary entities and public enterprises, see IMF Country Report 16/373.

[16] The recently created Ministry of Public Enterprises is also making strides in strengthening the monitoring of the sector and identifying performance issues in individual entities.

[17] Given the limited supply of domestic investible assets, the requirement also risks reducing portfolio diversification and profitability, and generating asset price inflation.

Box 1. Reporting, Monitoring, and Managing Fiscal Risks

Namibian fiscal accounts are exposed to risks from different sources, although information is limited. The main risks arise from observed forecast biases (e.g. high SACU revenue, low wage bill), macroeconomic shocks, and explicit and implicit contingent liabilities. The main explicit contingent liabilities in Namibia include loan guarantees, guarantees for housing loans to public employees, and PPP guarantees (mainly for local governments). By the end of FY17/18, government's loan guarantees are expected to amount to 7.5 percent of GDP. However, information on other types of explicit (i.e. PPPs, guarantees on housing loans) and implicit contingent liabilities is either reported with long lags, difficult to gather, or not reported. For example, information on housing loan guarantees is available with a three-year lag, and only a small set of public entities issue annual audited financial reports. In addition, information on exposures from local governments, non-guaranteed debt of extra-budgetary public entities (EBEs), special public funds (e.g., the National Energy Fund), and publicly-owned financial institutions is generally not available. However, initial estimates based on data from the Ministry of Public Enterprises suggest that non-guaranteed liabilities from EBEs could amount to about 20 percent of GDP.

Fiscal risks, particularly from contingent liabilities, are likely to increase in the future. Some public entities in the transportation sector are facing economic difficulties. Moreover, the authorities have recently embarked on several initiatives to boost off-budget financing of infrastructure investment, including through public corporations, PPPs, and special purpose vehicles. Contingent liabilities from these initiatives could be potentially large, with some projects (e.g., in the energy sector) expected to cost up to 7 percentage points of GDP.

The dearth of timely and reliable information on contingent liabilities complicates the identification, monitoring and management of potentially significant fiscal risks. The absence of information prevents the identification of the largest fiscal risks and the understanding of whether risks are manageable or require action before they threaten budget credibility and the sustainability of public finances. The lack of information may also pose risks to fiscal adjustment plans as they may be derailed by the materialization of unforeseen risks.

Following best international practices, Namibia should start preparing, and eventually publishing, a fiscal risks statement. This requires to start gathering information and analyzing the main macroeconomic and contingent liability risks facing the budget, and compiling the information in a risks statement. Fiscal risks statements are typically living documents that may start from simple lists of key risks with only qualitative and/or quantitative information (see table), and evolve into presenting scenarios that analyze the magnitude and likelihood of different risks. Several good practice examples are available, including in South Africa.[1] A fiscal risks statement in Namibia would help reduce the likelihood that the materialization of risks derails fiscal adjustment plans. In addition, it can increase market credibility of fiscal adjustment by demonstrating a desire and capacity to transparently report and manage risks.

Namibia. Typical Non-Macroeconomic Fiscal Risks

	Estimated Exposure	
	N$ million	Percent of GDP
Guarantees		
Loan Guarantees 1/	8,932	5.2
Housing Scheme	n.a.	n.a.
State Owned Entities		
Non-Guaranteed Debt 2/	34,003	19.8
Regional and Local Governments		
Non-Guaranteed Debt	n.a.	n.a.
Public Private Partnerships		
e.g. CSP project	11,600	6.7
Legal Risks		
National and international Courts	n.a.	n.a.
Others:		
Natural Disasters	n.a.	n.a.
Financing Fund for Investment	n.a.	n.a.
Memo Items:		
Long term fiscal costs		
Health	n.a.	n.a.
Pensions 3/	81,770	47.6

Sources: BoN, MOF, Ministry of Public Enterprises, Government Institutions Pension Fund (GIPF).
1/ As of June 2017.
2/ Liabilities of extra-budgetary entities net of loan guarantees (source: Ministry of Public Enterprises).
3/ Actuarial value of GIPF's liabilities that are fully funded.

[1] IMF 2016, Analyzing and Managing Fiscal Risks-Best Practices.

Authorities' Views

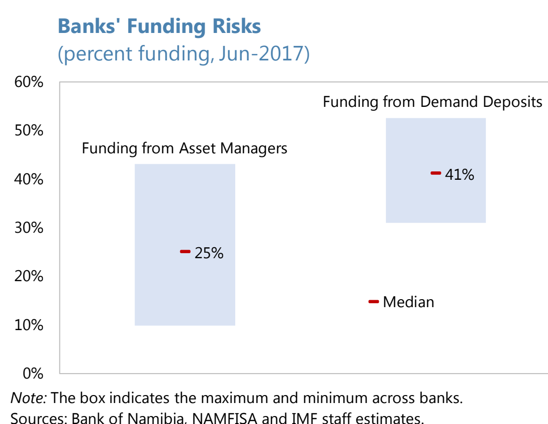
18. The authorities recognized that additional fiscal adjustment is needed to bring public finances on a sustainable path and have announced tight deficit targets for the upcoming FY18/19 budget. They concurred that a cumulative adjustment of 5–6 percent of GDP is needed over the next three years, starting with the FY18/19 budget, to bring the public debt ratio on a sustainable path. However, they consider past year arrears to be largely a one-off occurrence, and project the public debt ratio to peak at a significantly lower level than staff's estimate.

19. They agreed that the adjustment should be anchored in long-lasting measures and structural reforms that can strengthen policy credibility and support long-term growth. They concurred that measures to contain the public wage bill, and reform extra-budgetary entities and public enterprises are critical to achieve long-lasting adjustment, with positive effects on long-term growth. In this respect, they have already adopted a cabinet decision to limit new hires and are assessing measures to tame wage growth. They also plan to liquidate non-essential loss-making enterprises over the next year. In addition, they intend to adopt measures to broaden the tax base (e.g., income taxes, VAT) and close tax loopholes. To protect the poor, they have already increased old-age pensions and other cash transfer schemes, and plan to introduce proxy means testing to improve targeting. Finally, wary of possible fiscal risks from off-budget financing of large projects, they committed to preserve the highest fiscal transparency standards and to publish a fiscal risks statement, possibly starting with next year's budget.

B. Strengthening Financial System's Resilience

20. Namibia's financial sector has so far weathered the economic slowdown. The banking sector (assets about 75 percent of GDP) remains profitable and well capitalized. NPLs have recently increased, albeit from very low levels, while liquidity remains above regulatory requirements (Table 6).[18] However banks' loan books are concentrated, and banks extensively rely on wholesale funding, posing concentration risks. The financial sector comprises large NBFIs (net assets about 138 percent of GDP) with a fully-funded government pension fund and several large insurance companies dominating the sector. The presence of four large and heterogenous financial conglomerates with close linkages to South Africa, and significant financial and ownership interconnections between banks and NBFIs, add a layer of complexity to the financial system and its supervision. In addition, both banks and NBFIs are closely linked to the public sector, holding about 90 percent of government's domestic debt. Despite

Banks' Funding Risks
(percent funding, Jun-2017)



Note: The box indicates the maximum and minimum across banks.
Sources: Bank of Namibia, NAMFISA and IMF staff estimates.

[18] The BoN has recently completed a sample examination of banks' loan books and identified misclassification issues that can potentially increase NPL figures. In response, it has taken steps to enforce a bank asset quality review.

a well-developed financial sector and levels of financial inclusion that compare well to peer economies, a significant share of the population has no access to credit services, and financial development needs remain significant, with banks being reticent to lend to small businesses and the low-income and rural population (Figure 5).[19]

21. As the economy adjusts to more sustainable growth levels, specific sources of macro-financial risks arise from interconnections and exposures of financial institutions.[20] The 2018 FSAP identified key sources of risk:

- *Interconnections among financial institutions.* Asset managers and money market funds play a central role in connecting institutional investors to banks and foreign financial markets, creating complex interconnections. They manage about 30 percent of pension funds' and insurers' assets, and provide about ¼ of banks' funding (40 percent in some banks). They also invest about 40 percent of their assets abroad, largely in equities. Given that asset managers and money market funds are almost twice as large as banks, interconnections create potentially significant contagious channels between banks, non-bank financial institutions and foreign financial markets that need to be monitored.[21]

- *Banking sector's vulnerabilities.* Banks' highly concentrated loan books and extensive reliance on wholesale deposits point to significant counterparty, asset-class concentration and liquidity risks. FSAP stress test analysis suggests that banks can withstand significant increases in NPLs arising from an adverse macroeconomic scenario, but in the event of a severely adverse event, some banks would have difficulty in complying with future capital requirements, with possible negative effects on credit and growth.[22] Banks are also vulnerable to liquidity risks. While, on average, the banking system can withstand liquidity shortfalls, banks with large non-retail funding bases are likely to experience moderate liquidity shortfalls in case of shocks.[23]

- *Private sector indebtedness.* Elevated household indebtedness, combined with banks' large exposures to residential mortgages, raises concerns about households' vulnerabilities and banks' resilience. Corporate leverage is also elevated, but domestic banks' exposure to corporations is relatively limited, and foreign exposures appear concentrated in a few mining

[19] According to the 2014 Global Findex survey, 59 percent of adults had bank accounts, but only 7 percent borrowed money from a financial institution, and only 25 percent of small and medium enterprises accessed a credit line.

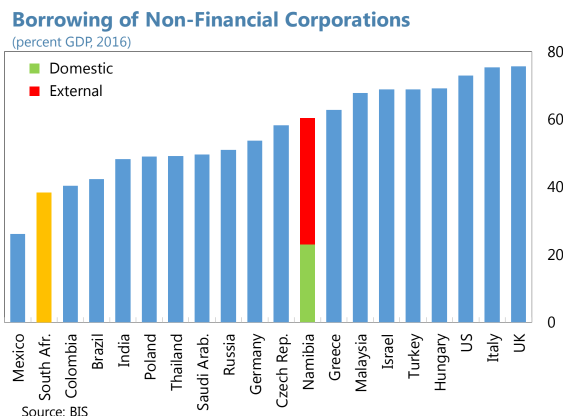
[20] Analysis based on the 2018 FSAP (forthcoming), and IMF Country Report 16/376.

[21] Given the relative size of asset managers, money market funds and banks, previous staff analysis (IMF Country Report 16/376) examined how even limited redemption shocks that prompt NBFIs to relocate assets away from banks' deposits could have severe liquidity implications for banks, affecting credit availability and eventually growth.

[22] Stress test analysis is based on balance sheet data as of June 2017, and covers the four largest banks, accounting for about 98 percent of total bank assets. The adverse scenario entails a temporary decline in GDP, accompanied by declines in commodity prices, growth in South Africa and the lending rate. A severely adverse scenario assumes a sharper decline in growth, with corresponding impact in commodity prices and South Africa GDP, and more than 20 percent decline in domestic house prices. For further discussion of stress tests, see the 2018 FSAP report, forthcoming.

[23] While relatively small, state-owned financial institutions may be an additional source of risk (see 2018 FSAP report, forthcoming).

companies (Figure 6). While information on individual borrowers is not available, households' estimated balance sheets suggest that the probability of default significantly increases with the household's leverage and debt service-to-income (DSTI) ratios. Past studies also suggest that middle-upper income households are particularly vulnerable to income and interest rate shocks. However, banks' balance sheets appear resilient to possible shocks to households' balance sheets and house price corrections (see below).



- *Decelerating residential real estate prices and banks' exposures.* Recently decelerating house prices and banks' and households' large exposure to mortgage loans raise concerns about risks from sudden corrections in the housing market. Staff estimate that, with the economy decelerating, house prices remain on average overvalued by about 10 percent, down from about 18 percent three years ago. FSAP sensitivity analysis suggests that all banks are resilient to a full correction in house price overvaluation. However, in the case of an overcorrection (e.g., 20 percent price decline), some banks would be unable to comply with capital requirements. Under these scenarios, banks would deleverage with negative effects on credit and growth.[24]

Residential House Price Overvaluation

	Jun-17	Jun-16	Sep-14
Regression Analysis	10.9	22.2	19.8
Price to Income	9.2	12.6	18.0
Price to Rent	10.2	13.5	17.0
Average	10.1	16.1	18.3

Source: IMF staff estimates

22. To strengthen the authorities' ability to monitor and manage the main sources of systemic risks in the financial sector, the mission reiterated the key FSAP recommendations (Annex VII).

- *Improving banking sector oversight.* The BoN has an effective supervision regime and continues improving its regulatory and supervisory framework. However, important shortfalls remain, particularly, in the liquidity framework and loan classification enforcement. Given banks' vulnerability to liquidity risks, the BoN should strengthen the liquidity regime to better align requirements to the risks posed by large and potentially volatile wholesale deposits. With evidence of possible loan misclassifications, the BoN should press ahead with plans to complete a system-wide review of banks' asset quality. In addition, given the extensive interconnections across financial institutions, the authorities should step up efforts to improve consolidated supervision of financial groups.

[24] Past analysis suggests that a one percent decline in real credit is associated with a 0.47 percent decline in real GDP in the long run (IMF Country Report 15/276).

- *Enhancing the supervision of NBFIs*. Over the years, the Namibia Financial Institutions Supervisory Authority (NAMFISA) has grown significantly and has been building its technical capacity. It now plans to embark on an extensive overhaul of the NBFI regulatory and supervisory framework to address regulatory gaps and introduce risk-based supervision. The first step in this process is to approve key legislation, including the NAMFISA and the Financial Institutions and Market bills. NAMFISA also plans to rapidly introduce an extensive set of implementing regulations. However, given the existing capacity and the possibility of compromising the adoption of a risk-based supervisory approach, NAMFISA should consider prioritizing and sequencing the new implementing regulations in partnership with industry.

- *Creating a macroprudential policy framework and expanding the authorities' toolkit.* Despite a large and interconnected financial system, no institution has an explicit macroprudential policy mandate. The planned Financial Stability Council (FSC), including the BoN, NAMFISA and the MoF, should have an explicit macroprudential mandate, including the power to issue macroprudential directives to regulators. As the creation of the FSC may take some time, in the interim, the BoN is the institution better placed to take the lead in assessing financial stability risks and exercise the macroprudential mandate, in consultation with NAMFISA and the MoF. The macroprudential toolkit should also be expanded, including by introducing DSTI limits and considering extending the recently introduced LTV limits to primary home purchases. DSTI limits would help tackle household vulnerabilities and curb the tendency for LTV limits to become less binding as property prices increase.

- *Developing a full crisis management and resolution framework.* The recent liquidation process of the SME Bank has shown that the crisis management and resolution framework needs substantial improvement. Key actions include: granting the BoN full bank and conglomerate resolution powers; requiring banks to submit recovery and resolution plans; operationalizing emergency lending assistance; strengthening cooperation with SARB in recovery and resolution planning of large groups; and, introducing a deposit insurance scheme that meets international norms.

- *Addressing information and data gaps.* Despite extensive progress to improve data availability, gaps remain. NAMFISA should continue to improve the collection of granular data critical for risk-based supervision. The BoN should accelerate efforts to develop household and corporate surveys to better gauge risks stemming from private sector leverage and operationalize its extended macroprudential toolkit.

Authorities' Views

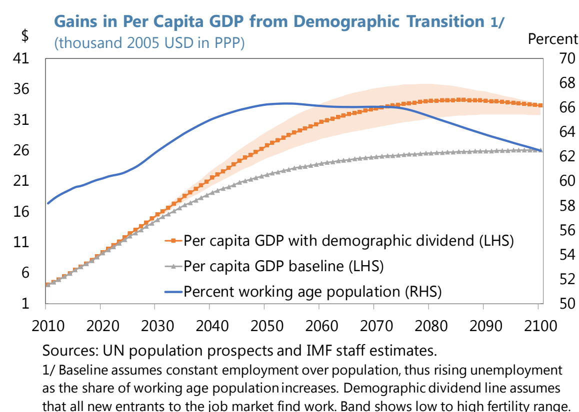
23. Authorities were in broad agreement with the FSAP findings and are moving ahead to address the key recommendations. They have already taken steps to complete a review of banks' asset quality by mid-2018 and are reassessing liquidity regulations to make them more forward looking. In addition, they plan to present to parliament key legislation to reform the legal and regulatory framework of the sector by early 2018. NAMFISA intends to issue an extensive set of regulations to implement the new laws and considers that sufficient consultation with the industry has taken place to implement these regulations. The authorities are committed to create

a macroprudential policy framework and agree for the FSC to have a macroprudential mandate and before its creation, to assign such mandate to the BoN. The BoN will also assess the opportunity to introduce further macroprudential limits at a later stage. Finally, the authorities agreed to take steps to strengthen the crisis management and resolution framework, including instituting a special resolution regime under updated Banking Institutions and Bank of Namibia Acts.

C. Leveraging the Demographic Transition

24. Structural impediments are keeping unemployment high and could limit the benefits from the upcoming demographic changes and the capacity to deliver more inclusive growth. Namibia is going through a major demographic transformation with more than 65 percent of the population, or about 3 million people, expected to be in the working age group by 2050 (Figure 8). Experience in other countries shows that similar transitions may boost potential growth but, if not managed properly, lead to long-term stagnation, inequities, and less inclusive growth. The potential benefits from demographic changes in Namibia could be substantial, with per capita income being potentially 25–50 percent higher. Key to a successful transition is the ability to create enough high-productivity jobs. However, this raises potential challenges in Namibia. The country has a low employment elasticity to growth and could be unable to generate enough jobs to reap the benefits of demographic changes even with sustained growth, risking instead rising unemployment. Increasing the elasticity of employment to growth is therefore critical to the country development and to deliver more inclusive growth.[25] Analysis shows that, compared to other countries, structural factors limit the capacity of the Namibian economy to create new jobs (Figure 9), including: (i) low education outcomes, particularly for higher education skills; (ii) weaknesses in the business environment, including for starting businesses and obtaining labor permits; (iii) wage dynamics in excess of productivity trends; and, (iv) employment still concentrated in less dynamic economic sectors (e.g., agriculture).[26]

Gains in Per Capita GDP from Demographic Transition 1/
(thousand 2005 USD in PPP)



Sources: UN population prospects and IMF staff estimates.
1/ Baseline assumes constant employment over population, thus rising unemployment as the share of working age population increases. Demographic dividend line assumes that all new entrants to the job market find work. Band shows low to high fertility range.

25. The authorities' strategy of supporting infrastructure investment and providing incentives to labor-intensive sectors has had limited impact, and new initiatives are planned. The recent increase in public investment has supported domestic demand, but has so far failed to crowd in non-mining private investment. Despite high social spending, health and education attainments remain relatively poor compared to other upper-middle income countries (Annex V). In addition, programs to support employment and tax incentive schemes have had limited impact on

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[25] For an analysis of employment elasticity to growth and inclusive growth in Namibia, see IMF Country Report 16/374.

[26] For an analysis of employment trends and responsiveness of employment to growth in Namibia, see IMF Country Reports 16/374 and 13/292.

employment and export diversification.[27] In addition, the authorities have recently issued a new national development plan (NDP5) and, with the Harambee Prosperity Plan, they have prioritized the implementation of high impact policies in the infrastructure, education and social sectors.

26. Policies targeted at improving the entrance in the labor market and the business environment could boost job creation and help reap the benefits of demographic changes. Considering the tight fiscal constraints, reforms in two areas could potentially improve employment dynamics:[28]

- *Human capital and skill mismatches.* Improving educational attainment, especially for higher education, would reduce skill mismatches in the labor market and boost the capacity to absorb new workers. This requires improving both access and quality of secondary and higher education, and strengthening technical and vocational training programs to better align skills to job needs. Strengthening the existing programs to acquire on-the-job training would facilitate the transition from school to work.

- *Wage dynamics and business conditions*. Reducing the gap between wage and productivity dynamics (e.g., containing public wages) has the potential to boost the elasticity of employment to growth. Moreover, streamlining business regulations (e.g., starting businesses, registering property and land) and the functioning of the labor market (e.g., increased labor permits for skilled workers, efficient dispute resolution processes) would contribute to reduce unemployment. Reforms in these areas might also boost development in labor-intensive sectors, e.g., manufacturing, further improving employment absorption.

Authorities' Views

27. Cognizant of the upcoming demographic transition, the authorities reaffirmed their commitment to implement policies that address high unemployment and inequality. They continue to strengthen technical, vocational and on-the-job training programs, including with tax incentives to employers for staff training. To ameliorate business conditions, they have recently simplified company registration requirements (allowing online registration), and are in the process of finalizing a new Investment Promotion Act aimed at stimulating entrepreneurship and foreign investment. However, they argued that well-targeted incentives and large infrastructure investment are critical to support the development of an industrial base and foster domestic value-added formation.

STAFF APPRAISAL

28. Namibia has experienced a period of exceptional growth fueled in part by temporary factors, but vulnerabilities have risen and income inequality remains unacceptably high. Between 2010 and 2015, an expansionary fiscal policy, the construction of large mines, and buoyant credit

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[27] The 2011–13 Targeted Intervention Program for Employment and Economic Growth (TIPEEG) mainly led to the creation of temporary jobs (National Planning Commission, Annual Report 2013–14). Export processing zones were created in 1995, and tax investment schemes exist for selected manufacturers.

[28] Based on IMF Country Reports 12/292 and 16/374.

supported growth and better living standards. However, strong growth masked negative productivity performance and rising macroeconomic vulnerabilities. Public debt increased sharply, the current account widened, and international reserve coverage fell below adequate levels. Rapid credit expansion also contributed to fast-rising real estate prices and elevated private sector indebtedness. Yet, structural impediments have kept unemployment high, contributing to still elevated income inequality.

29. With the temporary engines of growth coming to an end, Namibia's economy faces significant policy challenges. The economy has entered an adjustment phase. Real GDP is expected to have contracted in 2017 and start resuming growth in 2018. With low SACU revenue, public debt would rise, the external deficit would remain sizable, international reserve coverage would linger below adequate levels, and the overall external position would remain moderately weaker than justified by fundamentals. Downside risks dominate this outlook and stem from possible fiscal slippages that may undermine confidence in the government's ability to control public finances; lower demand for key exports; and further declines in SACU revenue. The negative impact of these shocks could be amplified by extensive macro-financial linkages. In this context, Namibia's key policy challenges are to: manage the ongoing adjustment process and bring public debt on a sustainable path; address macro-financial risks and vulnerabilities from the large and interconnected financial sector; and generate sufficient jobs to manage the upcoming demographic changes, reduce income inequality and deliver more inclusive growth.

30. Following recent consolidation efforts, additional fiscal adjustment is needed to bring public debt on a declining path. The last two budgets have marked a welcomed shift towards a tighter fiscal stance. However, with declining SACU revenue, staff assess that a cumulative 5–6 percent of GDP in measures is needed to ensure debt sustainability. While ambitious, the adjustment is equivalent to the spending increases observed in recent years and consistent with the authorities' consolidation plans. To contain the negative effects on growth, the adjustment should be spread over the next three years, starting with the FY18/19 budget. It should be carefully designed to include a combination of spending and revenue measures that support long-term growth, while mitigating negative distributional effects. Measures should include: containing public wage bill dynamics, rationalizing transfers to extra-budgetary entities, as well as reducing tax exemptions and boosting consumption tax revenue. These policies are likely to bring wage dynamics closer to productivity trends, and create a level-playing field with positive effects on labor market outcomes and long-term growth. Better targeting of social cash transfers would help protect the poor and strengthen the distributional impact of public spending. Reforms to improve budget formulation and expenditure controls, strengthen revenue administration and the management of extra-budgetary entities are critical to buttress the credibility of consolidation plans. Concrete actions, including the preparation of a fiscal risks statement, are also needed to monitor and manage fiscal risks, particularly from the expanding off-budget financing of large public investment projects.

31. Additional fiscal adjustment will play an important role in supporting the ongoing economic adjustment and reducing external imbalances. The adjustment would curb domestic demand and help reach an external position broadly in line with medium-term fundamentals, while facilitating the accumulation of adequate levels of international reserves. In this respect, the BoN

should maintain the policy rate in line with the SARB's rate. Moreover, it should consider using well-targeted macroprudential tools to manage risks from the highly leveraged private sector and still overvalued real estate assets.

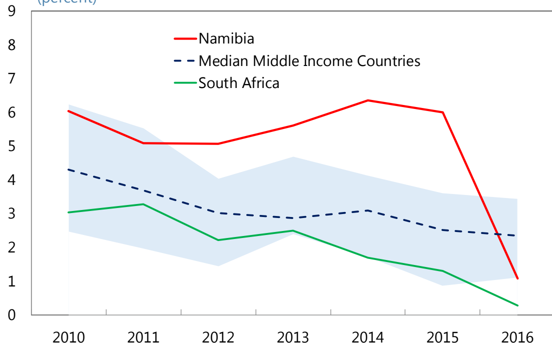
32. Early steps in implementing the FSAP recommendations and managing risks from financial institutions' linkages and exposures and private sector indebtedness are welcome. The ongoing review of banks' asset quality and the reassessment of liquidity regulations are positive steps to improve the oversight of the banking sector. With a large non-bank financial sector, the authorities should press ahead approving the planned legislative changes to address existing regulatory gaps and sequencing the implementing regulations, while introducing risk-based supervision. Given the significant interconnections between banks and NBFIs and cross-border linkages, the authorities should step up efforts to improve consolidated supervision of financial groups and monitor and manage macro-financial and financial stability risks arising from such linkages. In this respect, they should accelerate plans to create and assign to the Financial Stability Council an explicit macroprudential mandate with directive powers. Before the council is established, the BoN should exercise such mandate and complement the macroprudential toolkit with DSTI ratio limits and additional macroprudential measures as needed. Developing a full crisis management and resolution framework, including by granting the BoN and NAMIFISA full resolution powers and conducting recovery and resolution planning, is needed.

33. Reforms to boost job creation and reap the benefits of upcoming demographic changes are essential for achieving more inclusive growth and development. Structural reforms should focus on the areas with the highest potential that include: reducing skill mismatches in the labor market (e.g., improving access and quality of secondary and higher education, vocational and on-the-job training programs), better aligning wage and productivity dynamics (e.g., containing public wage increases), and streamlining business regulation (e.g., starting businesses, registering properties and land) and the functioning of the labor market (e.g., increased labor permits for skilled workers, and more efficient dispute resolution processes).

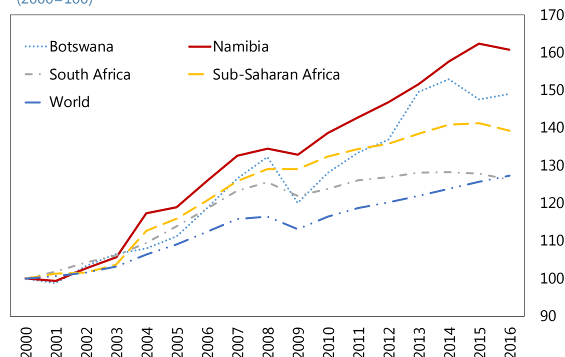
34. It is proposed that the next Article IV consultation with Namibia be held on the standard 12-month cycle.

Figure 1. Improved Living Standards, yet High Unemployment and Inequality

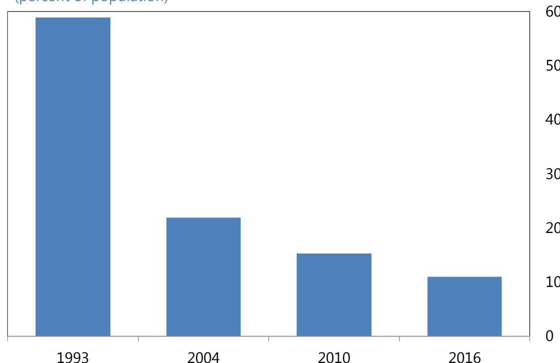
Until recently, Namibia had experienced a prolonged period of strong growth…



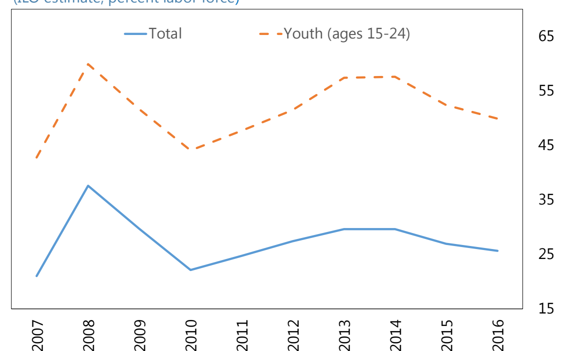
…and improving living standards, with growth in per capita income outperforming other countries in the region…



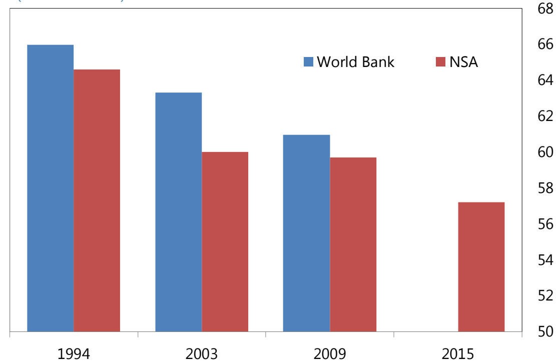
…and poverty declining.



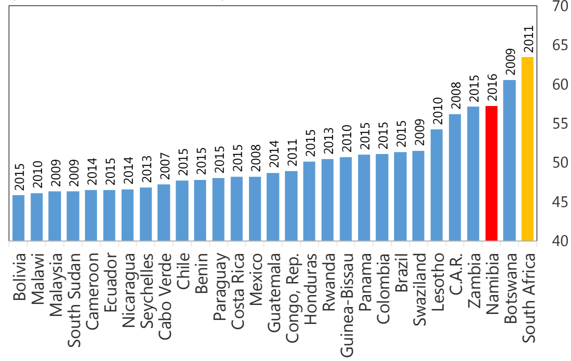
Yet, unemployment is persistently high, especially for the youth.



Inequality has been decreasing slowly …



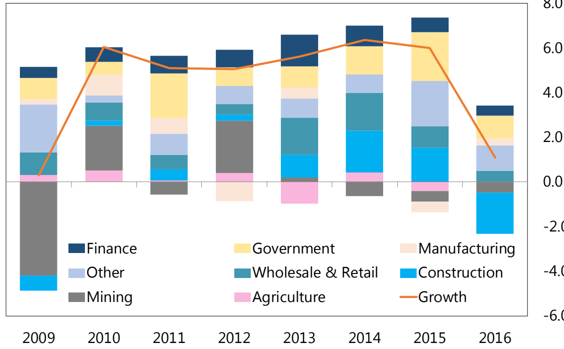
…and remains one of the highest in the world.



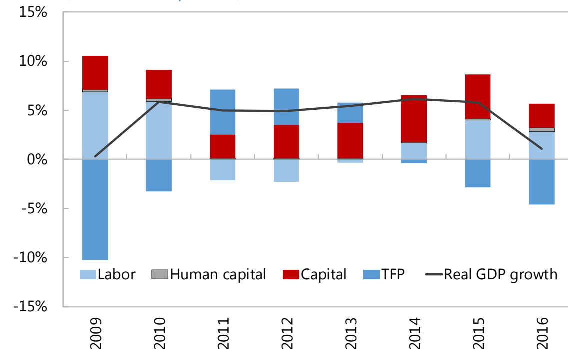
Sources: Namibia Statistics Agency, Bank of Namibia, ILO, World Bank, IMF staff calculations.

Figure 2. Economy at a Turning Point with Weak Productivity and Growth Deceleration

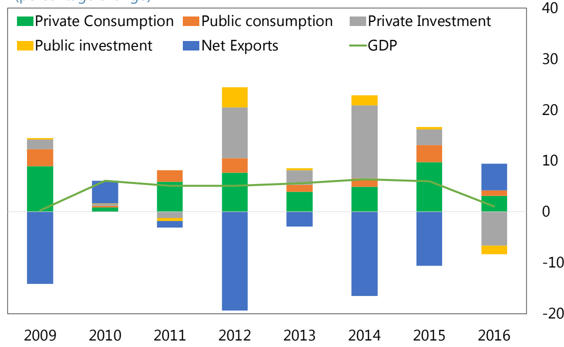
Until 2015, large mining construction, and an expansionary fiscal policy temporarily boosted growth…



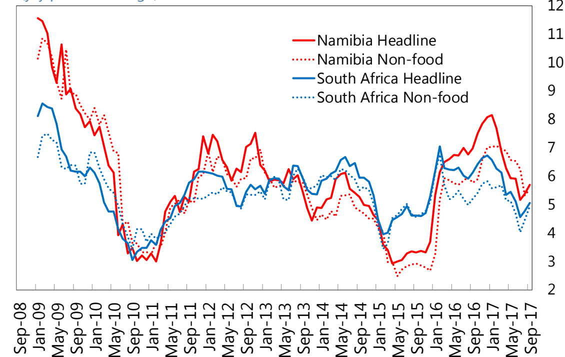
…masking declining productivity performance.



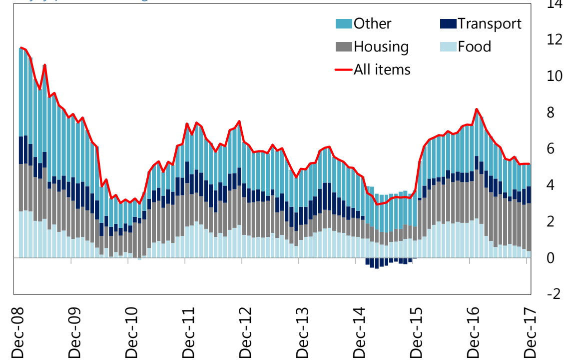
As mining construction halted and fiscal consolidation began, in 2016 investment collapsed and growth decelerated.



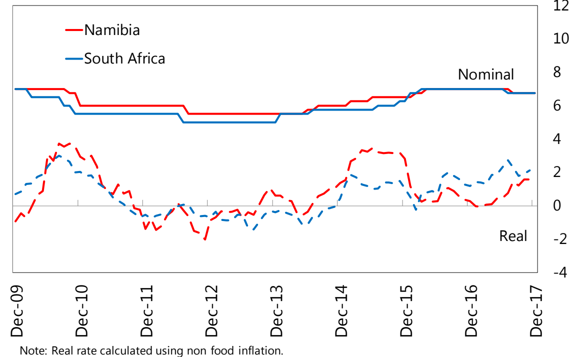
Inflation started declining….



…led by decelerating food prices and economic slack.



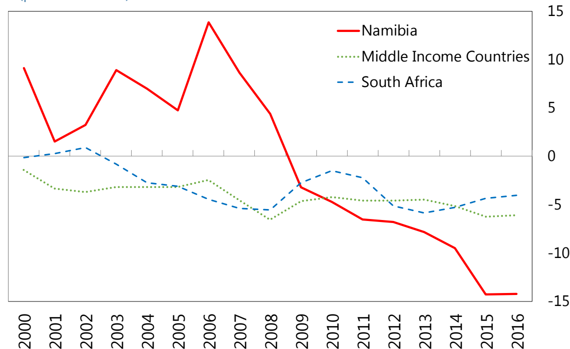
For the first time since 2012, the BoN lowered its repo rate following the South African Reserve Bank's policy.



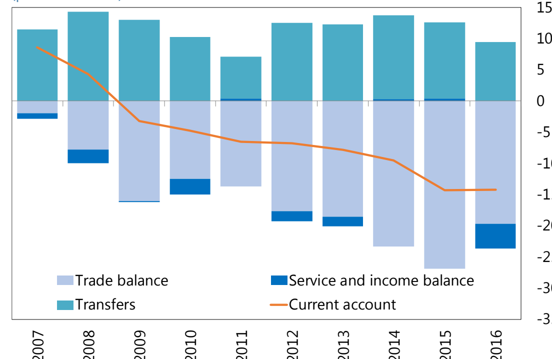
Sources: Namibia Statistics Agency, Bank of Namibia, Ministry of Finance, IMF staff calculations.

Figure 3. Persistent External Vulnerabilities

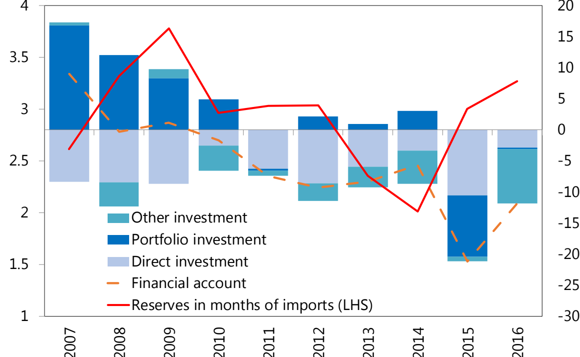
Although growth decelerated in 2016, the current account deficit remained large....



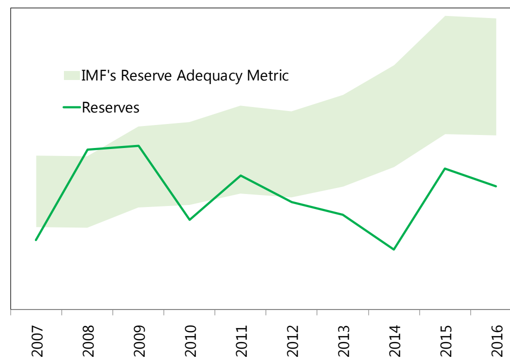
...as low SACU transfers and large income and service deficits offset an improving trade balance.



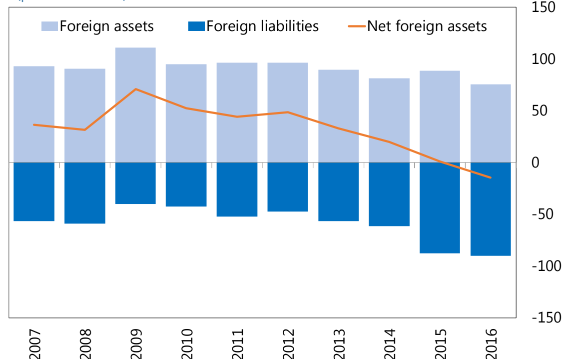
Despite low capital inflows, international reserve import coverage increased, boosted in part by BoN's swap operations.



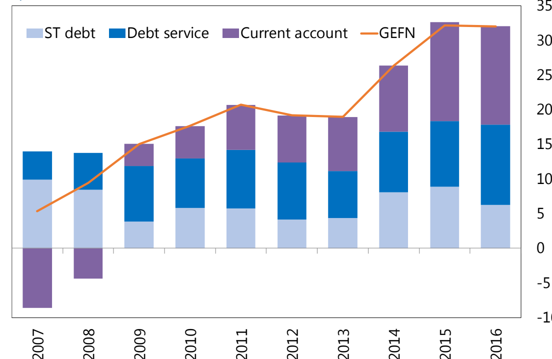
However, reserve coverage remained below adequate levels...



...the net international investment position turned negative...



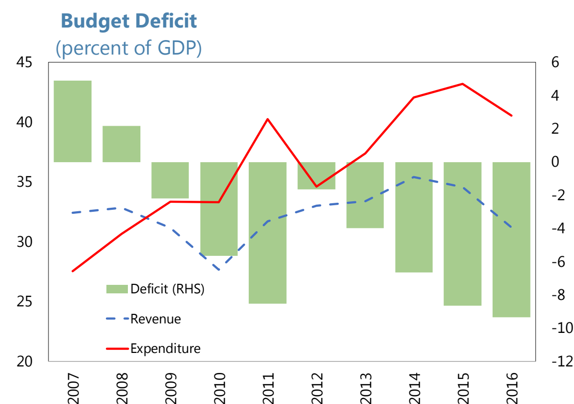
...and external gross financing needs remained high.



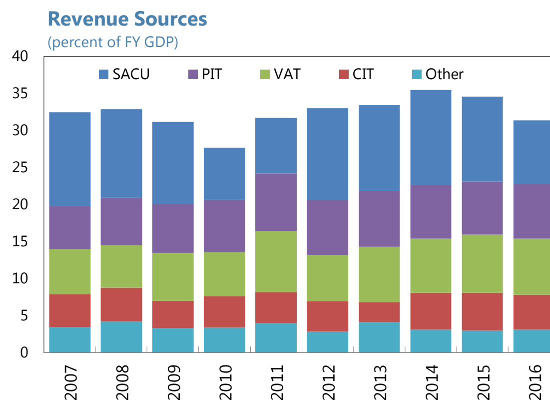
Sources: Bank of Namibia, Namibia Statistics Agency, IMF staff calculations.

Figure 4. Starting Fiscal Consolidation

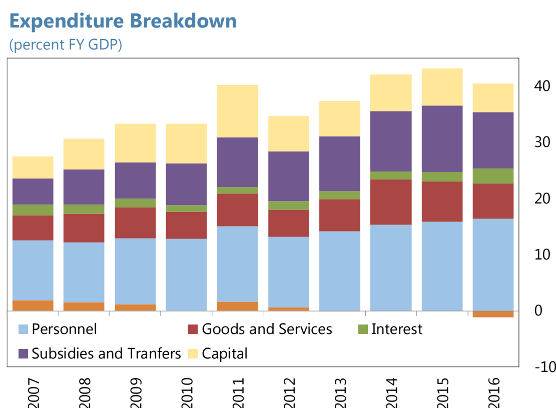
After years of expansionary policy, in FY16/17 the fiscal deficit narrowed....



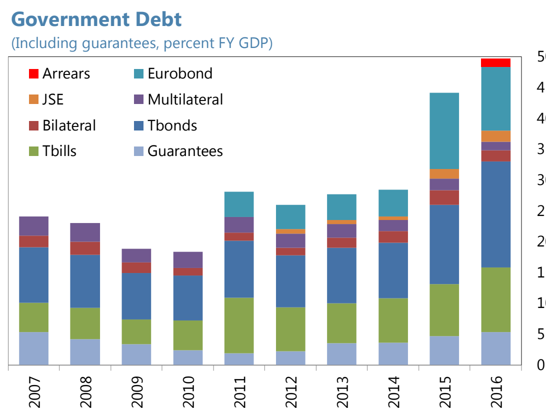
...despite a sharp reduction in SACU revenue....



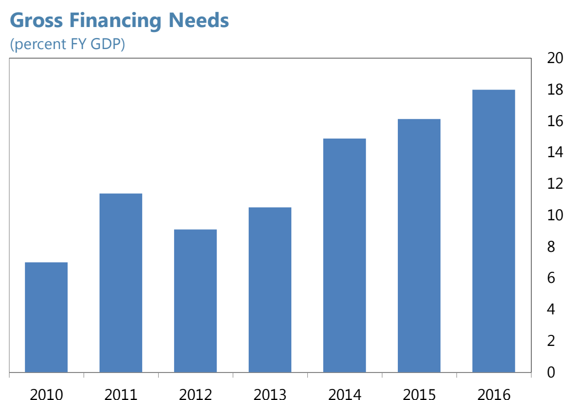
...as large reductions in non-wage recurrent and capital spending more than offset the revenue shortfalls and rising wage bill.



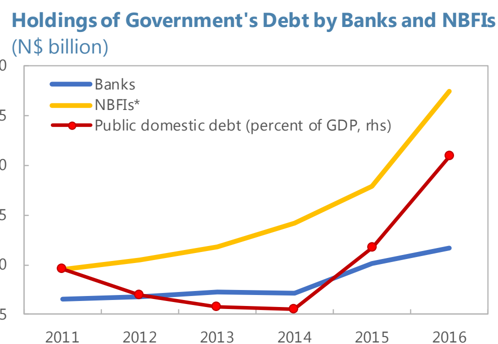
With still a large deficit, the public debt ratio, including recently accumulated domestic arrears, increased further.



Government's financing needs remained elevated...



...and domestic financial institutions' holdings of government securities have risen.

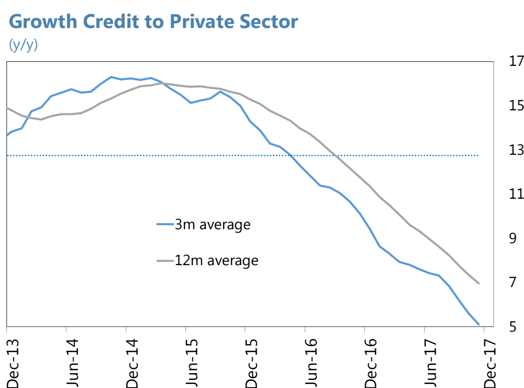


* Estimated as the residual of goverment's domestic debt stock minus the holdings of commercial banks.

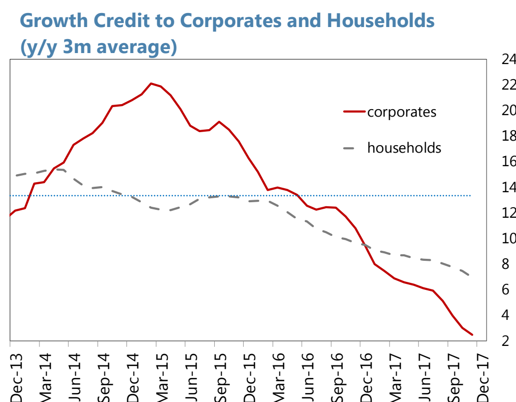
Sources: Bank of Namibia, NAMFISA, Ministry of Finance, IMF staff calculations.

Figure 5. Decelerating Credit and Improved Financial Inclusion

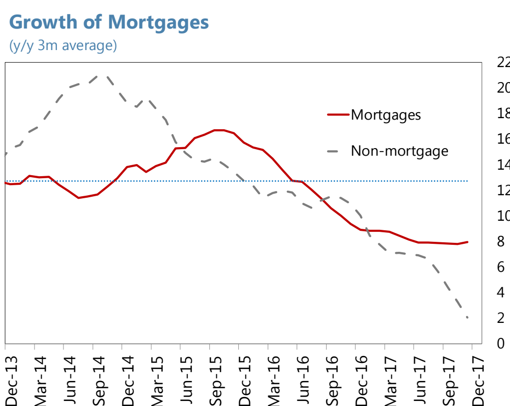
With the economy slowing down, private sector credit growth has been rapidly decelerating….



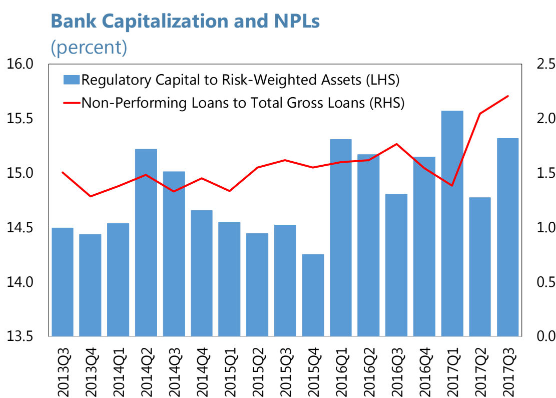
… for both corporates and households …



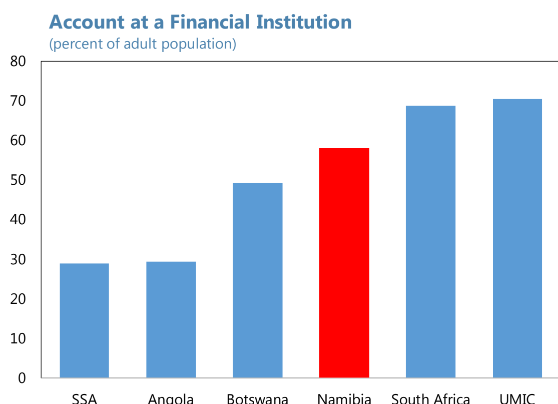
…driven by slower growth in both individuals' mortgage loans and other credits.



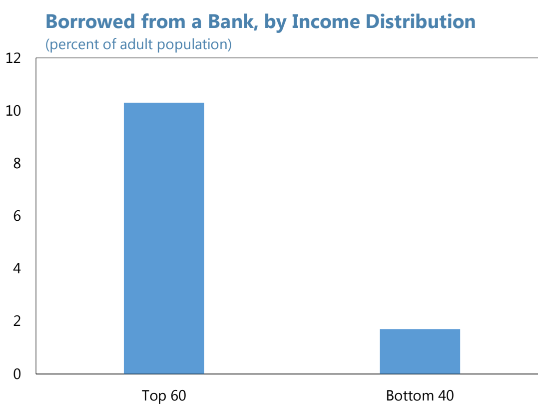
Banks are well capitalized, with good asset quality, although NPLs have increased recently.



Financial inclusion compares well to peers…



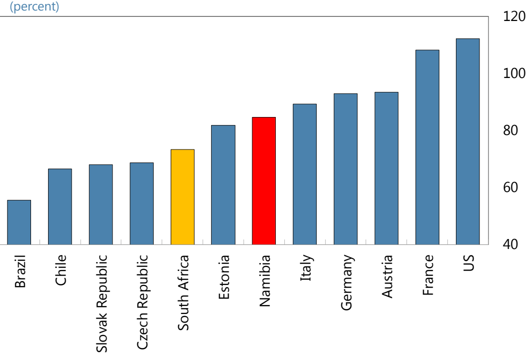
…but access to credit remains unequal.



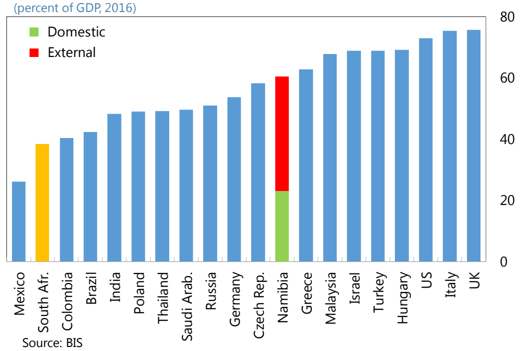
Sources: Bank of Namibia, Namibia Statistics Agency, First National Bank, and IMF staff calculations.

Figure 6. Significant Macrofinancial Risks

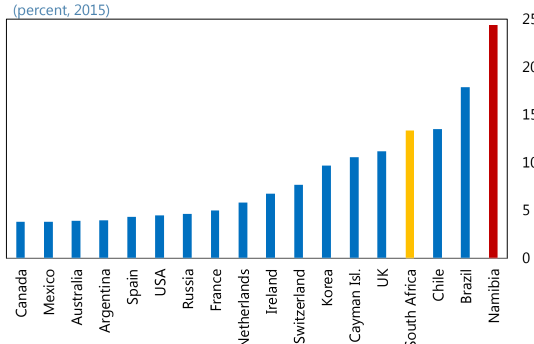
Private sector is highly leveraged, with both household indebtedness…



…and corporate leverage above the level of main EM economies and close to that of advanced economies.

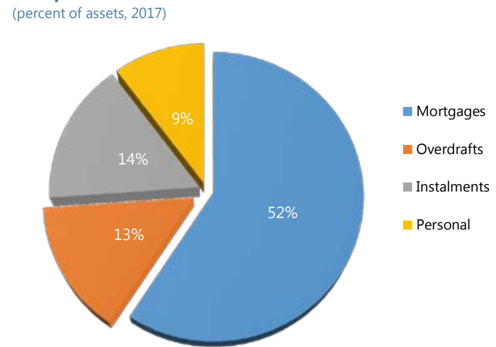


Banks' funding is highly dependent on wholesale deposits and…

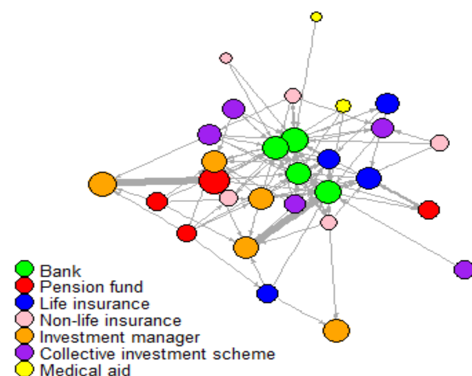


1/ Defined as non-bank financial institutions, e.g., pension funds, insurances.

…banks' loan books are concentrated.

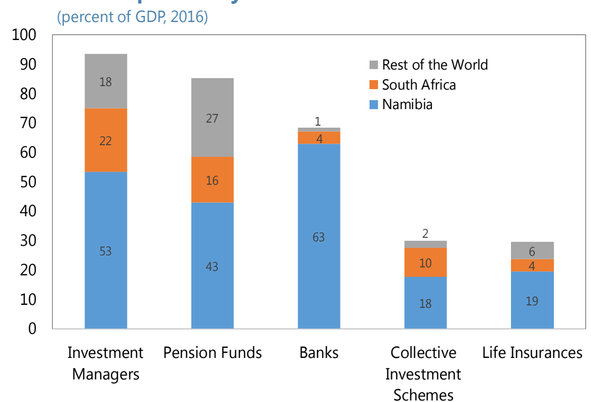


The financial system is highly interconnected…



Note: Node size reflects assets of institutions. Lines indicate exposures.

…with large foreign exposures.

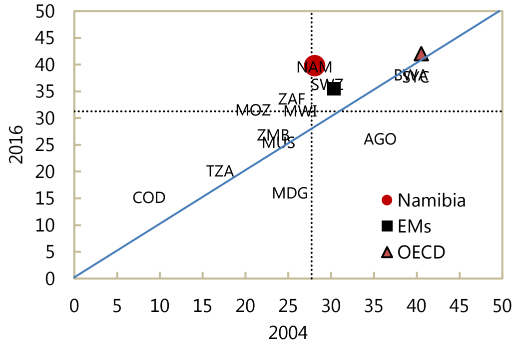


Sources: OECD, BIS, Bank of Namibia, Finanical Stability Board, SARB, and IMF staff calculations.

Figure 7. Public Spending Inefficiencies

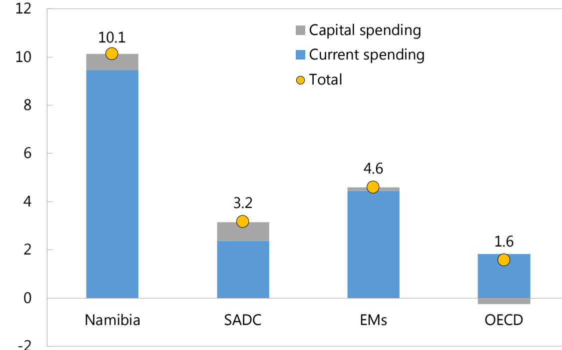
Public spending is higher than in most peers…

Government Spending (SADC Countries)
(in percent of GDP)



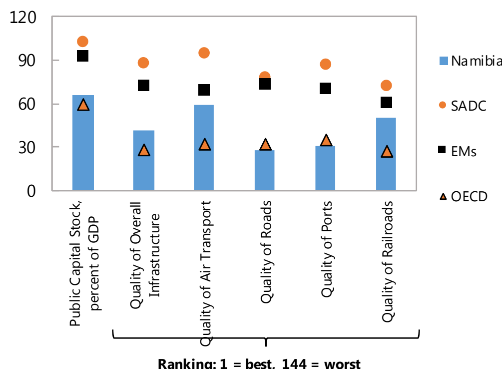
…as current spending, more than doubled over the last fifteen years.

Change in Total Spending, 2002-16
(percent of GDP)



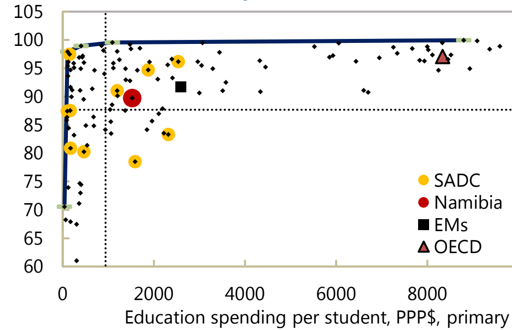
Physical infrastructure is relatively good.

Capital Stock and Infrastructure Quality, 2015



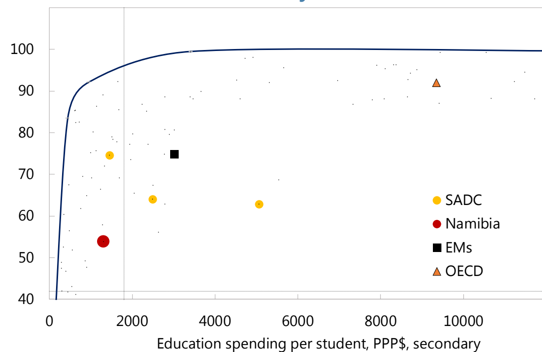
Despite high social spending, education outcomes remain poor…

Government Education Spending and Net Enrollment Rate, Primary Education



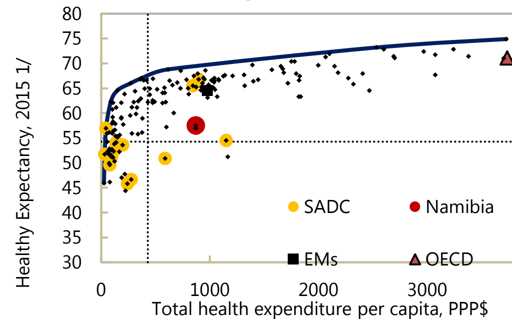
…particularly at higher education levels…

Government Education Spending and Net Enrollment Rate, Secondary Education



…and health outcomes are below peers in the region.

Health Efficiency Frontier

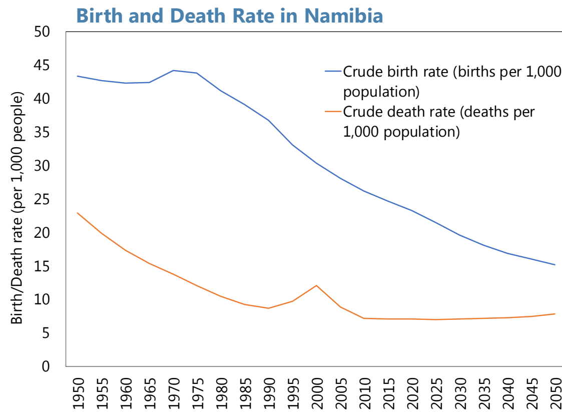


1/ Healthy life expectancy is a measure of health expectancy that applies disability weights to compute years of life expected.

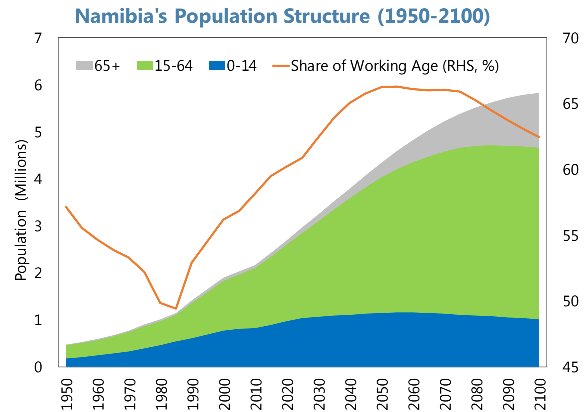
Source: IMF WEO, FAD Government Wage Bill and Employment Dataset, World Bank, ASPIRE, and IMF Pension Indicators.

Figure 8. Potential Benefits from the Ongoing Demographic Transition

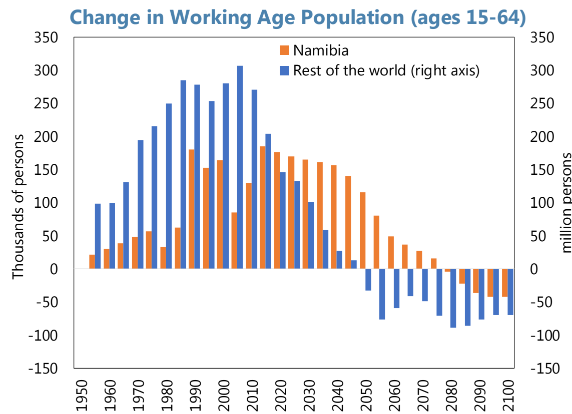
Namibia is undergoing a demographic transition, with declining fertility and mortality rates...



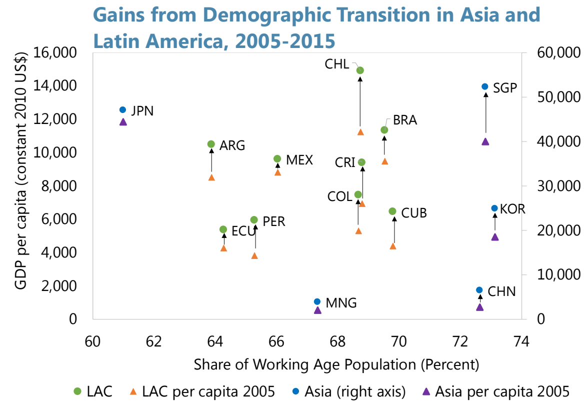
...and more than 60 percent of the population expected to be part of the working age group by 2050.



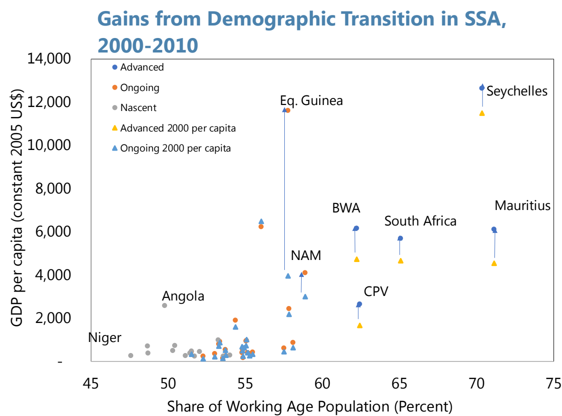
Countries that have gone through such transitions....



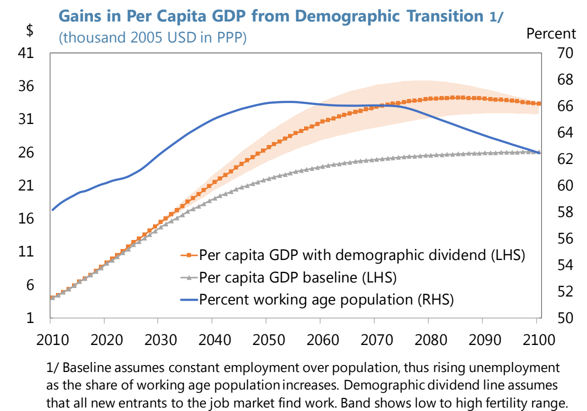
...have enjoyed significant increases in per capita GDP....



...including some small middle-high income countries in Africa...



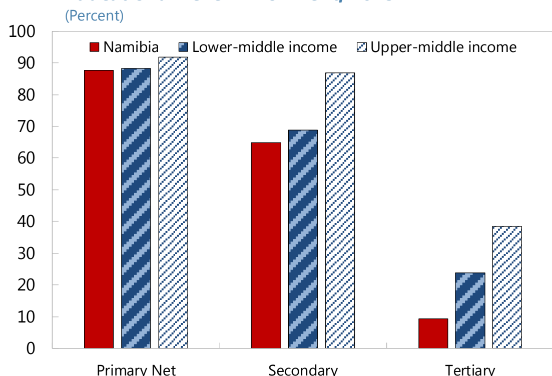
...suggesting that the growth benefits for Namibia can be significant.



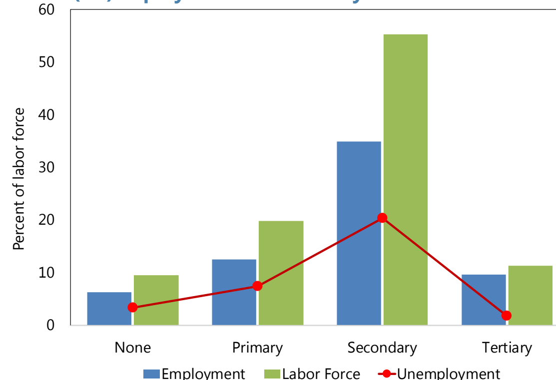
Sources: UN population prospects and IMF staff calculations.

Figure 9. Structural Impediments Might Limit the Benefits of Demographic Changes

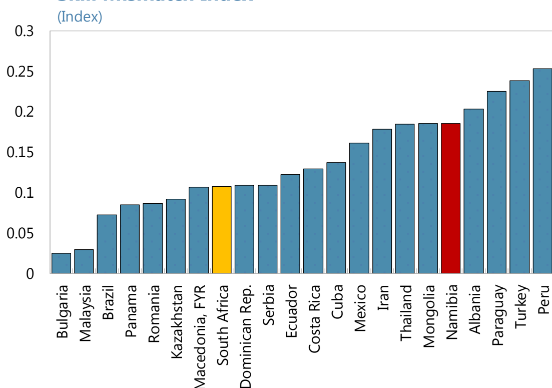
Secondary and tertiary education enrollment is low relative to other upper-middle income countries…



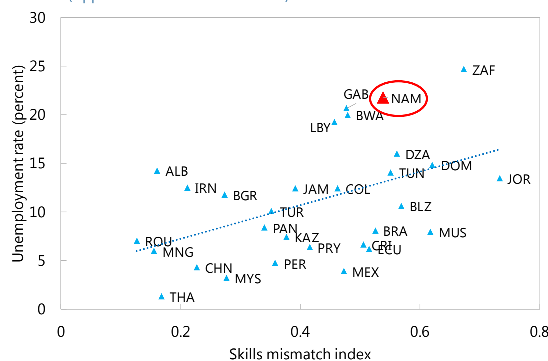
…with higher education skills being under high demand…



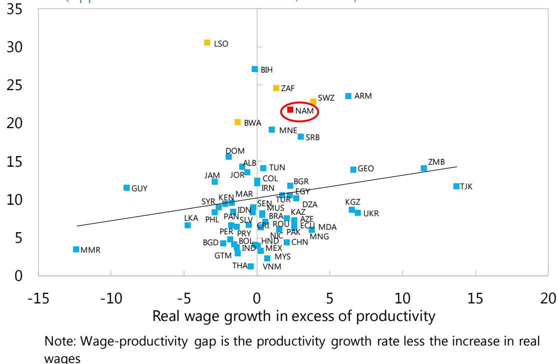
…leading to high skill mismatches in the labor market.



High skill mismatches are associated to higher unemployment.

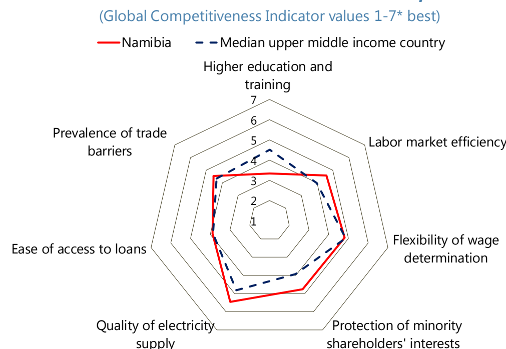


Disconnection between wage and productvity growth are also keeping unemployment high.



Note: Wage-productivity gap is the productivity growth rate less the increase in real wages

Weaknesses in business conditions and labor market functioning further constrain employment.



Sources: Namibia Statistics Agency, ILO, World Bank WDI, World Economic Forum GCI, and IMF staff calculations.

Table 1. Namibia: Selected Economic Indicators, 2014–22

	2014	2015	2016	2017	2018	2019	2020	2021	2022
				Est	Proj	Proj	Proj	Proj	Proj
	(percentage change, unless otherwise indicated)								
National account and prices									
GDP at constant prices	6.4	6.0	1.1	-1.2	1.2	3.3	3.8	3.5	3.5
GDP deflator	6.3	0.4	7.9	6.1	5.8	5.8	5.7	5.8	5.8
GDP at market prices (N$ billions)	139	148	161	169	181	197	217	237	259
GDP at market prices (Fiscal Year) (N$ billions)	141	151	163	172	185	202	222	243	266
GDP per capita (US$, constant 2000 exchange rate)	8,941	9,334	9,989	10,395	11,035	11,951	13,008	14,115	15,316
Consumer prices (end of period)	4.6	3.7	7.3	5.2	5.7	5.8	5.8	5.7	5.8
External sector									
Exports (US$)	-0.1	-13.2	4.3	13.5	9.2	7.6	6.3	3.8	3.5
Imports (US$)	9.9	-5.5	-12.7	-5.4	9.0	6.8	8.5	4.2	3.9
Terms of trade (deterioration = -)	4.2	-5.2	-7.1	0.5	1.1	-1.0	-1.4	-1.6	-1.4
Real effective exchange rate (period average)	-5.8	-2.4	-3.1	10.6	n.a.	n.a.	n.a.	n.a.	n.a.
Exchange rate (N$/US$, end of period)	11.6	15.6	13.7	13.5	n.a.	n.a.	n.a.	n.a.	n.a.
Money and credit									
Domestic credit to the private sector	17.9	13.8	8.6	4.5	4.9	5.4	5.8	6.3	6.4
Base money	35.7	-5.0	24.7	10.0	10.0	10.0	10.0	10.0	10.0
M2	6.9	10.2	4.9	6.3	7.0	9.2	9.7	9.4	9.4
Interest rate (percent)	6.0	6.5	7.0	…	…	…	…	…	…
	(percent of GDP)								
Investment and Savings									
Investment	33.6	34.6	25.7	22.8	23.5	23.8	24.0	23.6	23.9
Public	7.4	9.2	9.1	7.3	7.5	7.3	7.0	6.1	5.9
Private	26.0	24.9	15.1	15.5	16.0	16.5	17.0	17.5	18.0
Change Inventories	0.2	0.5	1.4	0.0	0.0	0.0	0.0	0.0	0.0
Savings	24.1	20.3	11.5	21.2	19.9	18.6	18.2	17.8	18.1
Public	0.4	-1.6	-3.6	-1.8	-3.2	-5.2	-5.0	-5.2	-5.7
Private	23.7	21.9	15.1	23.0	23.1	23.8	23.2	23.0	23.8
Central government budget 1/									
Revenue and grants	35.4	34.6	31.2	34.2	31.6	30.0	30.9	30.6	30.6
Of which: SACU receipts	12.9	11.5	8.6	11.4	9.4	7.8	8.6	8.4	8.4
Expenditure and net lending	42.1	43.2	40.5	39.4	40.1	39.9	39.9	39.4	39.9
Primary balance (deficit = -)	-5.2	-6.9	-6.7	-2.2	-5.1	-5.9	-4.5	-3.9	-3.6
Overall balance	-6.7	-8.7	-9.3	-5.2	-8.5	-9.9	-9.0	-8.8	-9.3
Overall balance: Non-SACU	-19.5	-20.1	-18.0	-16.6	-17.9	-17.6	-17.6	-17.2	-17.7
Public debt/GDP	24.8	39.4	44.3	46.5	51.4	57.3	61.9	65.7	69.7
Of which: domestic	16.2	21.3	28.9	30.4	33.9	40.1	45.5	50.3	56.1
Gross public and publicly guaranteed debt/GDP	28.4	44.2	49.6	54.0	59.5	66.0	71.2	75.7	80.3
External sector									
Current account balance									
(including official grants)	-9.4	-14.1	-14.1	-1.5	-3.6	-5.1	-5.7	-5.7	-5.7
External public debt (including IMF)	8.0	13.1	17.1	15.9	17.0	17.0	16.3	15.4	13.8
Gross official reserves									
US$ millions	1,198	1,580	1,791	2,193	2,158	2,155	1,799	1,588	1,579
Percent of GDP	10.0	16.7	15.2	17.5	16.5	15.6	12.3	10.3	9.7
Months of imports of goods and services	2.0	3.0	3.7	4.1	3.8	3.5	2.8	2.4	2.3
External debt/GDP 2/	43.0	48.2	60.2	60.6	64.4	66.3	67.3	68.5	68.7
Memorandum item:									
Population (in million)	2.2	2.3	2.3	2.3	2.4	2.4	2.4	2.4	2.4

Sources: Namibian authorities and Fund staff estimates and projections.

1/ Figures are for fiscal year, which begins April 1.

2/ Public and private external debt.

Table 2. Namibia: Fiscal Operations of the Central Government, 2014/15–22/23
(N$ millions)

	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
				Est	Proj	Proj	Proj	Proj	Proj
Total revenue and grants	49,954	52,200	50,848	58,804	58,508	60,752	68,542	74,278	81,242
Domestic revenue	49,843	52,048	50,848	58,754	58,454	60,693	68,478	74,207	81,164
Tax revenue	46,836	48,903	47,641	55,110	54,674	56,558	63,991	69,340	75,959
Personal income tax	10,197	10,794	12,002	12,488	13,238	14,629	16,303	17,821	19,746
Corporate income tax	7,019	7,722	7,708	8,491	8,850	9,561	10,349	11,190	12,089
o/w Diamond mining	1,980	2,199	1,611	2,157	2,268	2,354	2,446	2,540	2,639
VAT and sales taxes	10,270	11,903	12,389	12,981	13,541	14,822	16,253	17,783	19,456
Taxes on international trade (includes SACU receipts)	18,117	17,355	14,071	19,597	17,375	15,721	19,083	20,356	22,271
Other taxes	1,234	1,129	1,472	1,552	1,670	1,826	2,003	2,191	2,397
Nontax revenue	3,008	3,146	3,207	3,644	3,781	4,134	4,487	4,867	5,205
Diamond and other mineral royalties	1,244	1,369	1,368	1,832	2,068	2,261	2,433	2,620	2,746
Adminstrative fees, including license revenues	772	628	835	881	948	1,036	1,136	1,243	1,360
Other	992	1,149	1,004	931	765	837	918	1,004	1,098
Grants	110	152	0	50	54	59	65	71	77
Expenditure and net lending 1/	59,334	65,262	66,076	67,671	74,273	80,719	88,448	95,649	106,007
Current expenditure	50,198	55,205	57,670	60,654	65,725	72,119	79,163	87,131	96,688
Personnel	21,655	23,961	26,738	29,411	32,227	35,142	38,217	41,561	45,197
Goods and services	11,310	10,794	10,281	9,181	9,257	9,789	10,352	10,947	11,576
Interest payments	2,066	2,633	4,312	5,075	6,283	7,948	9,933	12,001	15,152
Domestic	1,600	2,031	2,831	3,676	4,667	6,019	7,948	10,090	12,507
Foreign	460	596	1,479	1,397	1,614	1,928	1,984	1,909	2,643
Subsidies and transfers	15,168	17,817	16,298	16,987	17,958	19,240	20,662	22,623	24,763
Capital expenditures	9,132	10,050	8,396	7,006	8,539	8,587	9,271	8,502	9,302
Acquisition of capital assets	6,004	7,441	7,537	5,969	6,423	5,867	6,433	7,039	7,701
Project Finance (extrabudgetary)	578	684	0	0	1,000	1,500	1,500	0	0
Capital transfers	2,550	1,925	860	1,037	1,116	1,220	1,338	1,464	1,601
Net lending	4	7	10	10	9	13	14	15	17
Overall balance 2/	-9,380	-13,062	-15,228	-8,867	-15,764	-19,967	-19,906	-21,371	-24,766
Primary balance	-7,314	-10,428	-10,916	-3,791	-9,481	-12,019	-9,973	-9,371	-9,614
Financing	6,013	15,627	18,102	8,867	15,764	19,967	19,906	21,371	24,766
Domestic financing (net)	5,712	2,229	17,970	6,151	11,581	18,289	19,079	20,973	26,751
of which: Accounts Payable	0	0	3,864	-3,864	0	0	0	0	0
External financing (net)	300	13,398	132	2,716	4,183	1,678	828	398	-1,986
Disbursements	578	13,484	492	3,000	4,500	2,000	2,000	8,500	500
Project loans	578	684	0	0	1,000	1,500	1,500	0	0
External bond	0	12,800	492	0	500	500	500	8,500	500
Amortization	-278	-86	-360	-284	-317	-322	-1,172	-8,102	-2,486
Discrepancy	-3,367	2,565	2,875	0	0	0	0	0	0
Memorandum items:									
Overall Balance (excluding SACU receipts)	-27,497	-30,416	-29,298	-28,464	-33,139	-35,688	-38,989	-41,727	-47,036
Overall Balance (excluding SACU and mineral revenues) 1/	-30,720	-33,984	-32,278	-32,453	-37,476	-40,304	-43,868	-46,887	-52,422
Public and publicly guaranteed debt	40,067	66,707	80,935	92,881	110,104	133,560	157,981	183,675	213,171
Public debt	34,953	59,563	72,187	79,918	95,045	115,879	137,262	159,549	185,183
Domestic	22,902	32,113	47,142	52,255	62,686	81,122	100,877	122,027	149,017
External	12,051	27,450	25,045	27,664	32,359	34,758	36,385	37,522	36,167
GDP at market prices (Fiscal Year)	140,981	150,984	163,011	171,928	185,009	202,299	221,836	242,717	265,549

Sources: Namibian authorities; and Fund staff estimates and projections. Fiscal year: April-March.

1/ FY16/17 expenditures include domestic arrears incurred in the year and paid in FY17/18. The authorities record arrears at the time of payment. Public debt in FY16/17 includes a temporary loan from the Central Bank repaid in FY17/18.

2/ Includes externally financed project spending not channeled through the state account.

Table 3. Namibia: Fiscal Operations of the Central Government, 2014/15–22/23
(Percent of GDP)

	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
				Est	Proj	Proj	Proj	Proj	Proj
Total revenue and grants	35.4	34.6	31.2	34.2	31.6	30.0	30.9	30.6	30.6
Revenue	35.4	34.5	31.2	34.2	31.6	30.0	30.9	30.6	30.6
Tax revenue	33.2	32.4	29.2	32.1	29.6	28.0	28.8	28.6	28.6
Personal income tax	7.2	7.1	7.4	7.3	7.2	7.2	7.3	7.3	7.4
Corporate income tax	5.0	5.1	4.7	4.9	4.8	4.7	4.7	4.6	4.6
o/w Diamond mining	1.4	1.5	1.0	1.3	1.2	1.2	1.1	1.0	1.0
VAT and sales taxes	7.3	7.9	7.6	7.6	7.3	7.3	7.3	7.3	7.3
Taxes on international trade (includes SACU receipts)	12.9	11.5	8.6	11.4	9.4	7.8	8.6	8.4	8.4
Other taxes	0.9	0.7	0.9	0.9	0.9	0.9	0.9	0.9	0.9
Nontax revenue	2.1	2.1	2.0	2.1	2.0	2.0	2.0	2.0	2.0
Diamond and other mineral royalties	0.9	0.9	0.8	1.1	1.1	1.1	1.1	1.1	1.0
Administrative fees, including license revenues	0.5	0.4	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Other	0.7	0.8	0.6	0.5	0.4	0.4	0.4	0.4	0.4
Grants	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Expenditure and net lending 1/	42.1	43.2	40.5	39.4	40.1	39.9	39.9	39.4	39.9
Current expenditure	35.6	36.6	35.4	35.3	35.5	35.6	35.7	35.9	36.4
Personnel	15.4	15.9	16.4	17.1	17.4	17.4	17.2	17.1	17.0
Goods and services	8.0	7.1	6.3	5.3	5.0	4.8	4.7	4.5	4.4
Interest payments	1.5	1.7	2.6	3.0	3.4	3.9	4.5	4.9	5.7
Domestic	1.1	1.3	1.7	2.1	2.5	3.0	3.6	4.2	4.7
Foreign	0.3	0.4	0.9	0.8	0.9	1.0	0.9	0.8	1.0
Subsidies and transfers	10.8	11.8	10.0	9.9	9.7	9.5	9.3	9.3	9.3
Capital expenditure	6.5	6.7	5.2	4.1	4.6	4.2	4.2	3.5	3.5
Acquisition of capital assets	4.3	4.9	4.6	3.5	3.5	2.9	2.9	2.9	2.9
Project Financed (extrabudgetary)	0.4	0.5	0.0	0.0	0.5	0.7	0.7	0.0	0.0
Capital transfers	1.8	1.3	0.5	0.6	0.6	0.6	0.6	0.6	0.6
Net lending	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance 2/	-6.7	-8.7	-9.3	-5.2	-8.5	-9.9	-9.0	-8.8	-9.3
Primary balance	-5.2	-6.9	-6.7	-2.2	-5.1	-5.9	-4.5	-3.9	-3.6
Financing	4.3	10.3	11.1	5.2	8.5	9.9	9.0	8.8	9.3
Domestic financing (net)	4.1	1.5	11.0	3.6	6.3	9.0	8.6	8.6	10.1
of which: Accounts Payable	0.0	0.0	2.4	-2.2	0.0	0.0	0.0	0.0	0.0
External financing (net)	0.2	8.9	0.1	1.6	2.3	0.8	0.4	0.2	-0.7
Disbursements	0.4	8.9	0.3	1.7	2.4	1.0	0.9	3.5	0.2
Project loans	0.4	0.5	0.0	0.0	0.5	0.7	0.7	0.0	0.0
External bond	0.0	8.5	0.3	0.0	0.3	0.2	0.2	3.5	0.2
Amortization	-0.2	-0.1	-0.2	-0.2	-0.2	-0.2	-0.5	-3.3	-0.9
Discrepancy	-2.4	1.7	1.8	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:									
Overall Balance (excluding SACU receipts)	-19.5	-20.1	-18.0	-16.6	-17.9	-17.6	-17.6	-17.2	-17.7
Overall Balance (excluding SACU and mineral revenues) 1/	-21.8	-22.5	-19.8	-18.9	-20.3	-19.9	-19.8	-19.3	-19.7
Public and publicly guaranteed debt	28.4	44.2	49.6	54.0	59.5	66.0	71.2	75.7	80.3
Public debt	24.8	39.4	44.3	46.5	51.4	57.3	61.9	65.7	69.7
Domestic	16.2	21.3	28.9	30.4	33.9	40.1	45.5	50.3	56.1
External	8.5	18.2	15.4	16.1	17.5	17.2	16.4	15.5	13.6

Sources: Namibian authorities and Fund staff estimates and projections. Fiscal year: April-March

1/ FY16/17 expenditures include domestic arrears incurred in the year and paid in FY17/18. The authorities record arrears at the time of payment. Public debt in FY16/17 includes a temporary loan from the Central Bank repaid in FY17/18.

2/ Includes externally financed project spending not channeled through the state account.

Table 4. Namibia: Balance of Payments, 2014–22 1/

(US$ millions, unless otherwise indicated)

	2014	2015	2016	2017	2018	2019	2020	2021	2022
				Est	Proj	Proj	Proj	Proj	Proj
Current account	-1,202	-1,633	-1,548	-190	-480	-723	-856	-903	-943
Trade balance	-2,981	-3,111	-2,154	-1,387	-1,507	-1,574	-1,811	-1,907	-1,999
Exports, f.o.b.	3,801	3,298	3,440	3,904	4,262	4,585	4,873	5,060	5,238
Of which:									
Diamonds	952	878	704	883	933	969	1,003	1,053	1,100
Other minerals	713	662	718	989	1,200	1,379	1,519	1,529	1,551
Imports, f.o.b.	-6,782	-6,409	-5,594	-5,291	-5,769	-6,159	-6,684	-6,967	-7,237
Services (net)	118	154	-79	63	26	4	-13	19	47
Transportation	-79	-77	-64	-43	-52	-56	-64	-66	-71
Travel	402	422	235	159	166	175	184	195	206
Other services	-205	-190	-251	-53	-88	-115	-133	-110	-88
Income (net)	-62	-86	-350	-227	-343	-319	-304	-365	-399
Compensation of employees	-27	-11	-2	-9	-7	-6	-7	-7	-7
Investment income	-35	-75	-348	-218	-336	-313	-297	-359	-393
Current transfers	1,724	1,410	1,035	1,360	1,343	1,167	1,272	1,350	1,409
Official transfers	1,688	1,394	1,014	1,317	1,317	1,137	1,239	1,320	1,378
Of which: SACU receipts	1,592	1,362	1,008	1,359	1,318	1,150	1,257	1,331	1,392
Other transfers	36	16	21	42	26	30	33	30	31
Capital and financial account	-885	-2,561	-1,410	-1,064	-424	-708	-376	351	-646
Capital account	-157	-108	-115	-167	-169	-167	-185	-190	-197
Financial Account	-728	-2,453	-1,295	-897	-256	-540	-192	541	-449
Direct Investment	-427	-1,218	-309	-787	-572	-559	-611	-616	-653
Portfolio Investment	389	-1,149	-34	205	1,187	728	1,164	1,805	860
Other Investment	-690	-86	-952	-315	-871	-709	-745	-648	-656
Errors and Omissions	25	-527	356	-525	…	…	…	…	…
				percent of GDP					
Current account	-9.4	-14.1	-14.1	-1.5	-3.6	-5.1	-5.7	-5.7	-5.7
Trade balance	-23.3	-26.9	-19.7	-11.0	-11.3	-11.2	-12.1	-12.1	-12.1
Exports	29.7	28.5	31.4	31.0	32.0	32.6	32.6	32.1	31.6
Imports	-53.0	-55.4	-51.1	-42.0	-43.4	-43.8	-44.7	-44.2	-43.7
Services (net)	0.9	1.3	-0.7	0.5	0.2	0.0	-0.1	0.1	0.3
Income (net)	-0.5	-0.7	-3.2	-1.8	-2.6	-2.3	-2.0	-2.3	-2.4
Current transfers	13.5	12.2	9.5	10.8	10.1	8.3	8.5	8.6	8.5
Of which: SACU receipts	12.4	11.8	9.2	10.8	9.9	8.2	8.4	8.4	8.4
Capital and financial account	-6.9	-22.1	-12.9	-8.4	-3.2	-5.0	-2.5	2.2	-3.9
Capital account	-1.2	-0.9	-1.0	-1.3	-1.3	-1.2	-1.2	-1.2	-1.2
Financial account	-5.7	-21.2	-11.8	-7.1	-1.9	-3.8	-1.3	3.4	-2.7
Direct Investment	-3.3	-10.5	-2.8	-6.2	-4.3	-4.0	-4.1	-3.9	-3.9
Portfolio Investment	3.0	-9.9	-0.3	1.6	8.9	5.2	7.8	11.5	5.2
Other Investment	-5.4	-0.7	-8.7	-2.5	-6.6	-5.0	-5.0	-4.1	-4.0
Memorandum items:									
Gross International Reserves (end of period)	1,198	1,580	1,791	2,193	2,158	2,155	1,799	1,588	1,579
Months of imports of goods and services	2.0	3.0	3.7	4.1	3.8	3.5	2.8	2.4	2.3
External debt (US$ millions) from IIP	5,497	5,575	6,584	7,644	8,567	9,329	10,059	10,787	11,390
Short-term debt (US$ millions)	1,025	684	650	847	802	746	761	789	774
Exchange rate (N$/US$, period average)	10.8	12.8	14.7	…	…	…	…	…	…
GDP at market prices (US$ millions)	12,796	11,577	10,945	12,608	13,298	14,071	14,940	15,751	16,571

Sources: Namibian authorities and Fund staff estimates and projections.

1/ Namibia adopted BPM6 at end 2016 and have revised BOP statistics since 2009.

Table 5. Namibia: Monetary Accounts, 2014–22 1/
(N$ millions, unless otherwise indicated)

	2014	2015	2016	2017	2018	2019	2020	2021	2022
				Est	Proj	Proj	Proj	Proj	Proj
Central Bank									
Reserve money	6,707	6,372	7,945	8,739	9,613	10,575	11,632	12,795	14,075
Currency	4,118	4,495	4,394	4,833	5,075	5,329	5,595	5,875	6,169
Reserves	2,589	1,877	3,551	3,906	4,539	5,246	6,037	6,921	7,906
Net foreign assets	11,686	24,275	24,329	26,720	26,558	26,944	22,175	22,459	22,909
Net domestic assets	-4,979	-17,903	-16,384	-17,980	-16,944	-16,369	-10,543	-9,664	-8,834
Monetary survey									
Broad money (M2)	74,366	81,934	85,949	91,326	97,757	106,750	117,154	128,184	140,242
Currency	2,544	3,042	2,884	3,279	3,443	3,579	3,710	3,656	3,359
Deposits	71,822	78,892	83,065	88,047	94,314	103,171	113,444	124,528	136,883
Net foreign assets	19,512	29,792	26,502	28,864	28,752	29,210	24,522	24,898	25,446
Net domestic assets	54,854	52,142	59,447	62,462	69,005	77,539	92,632	103,286	114,796
Domestic credit	77,066	83,316	95,879	104,537	110,993	118,405	126,675	135,967	146,039
Claims on central government (net)	4,002	-1,608	3,905	8,240	9,681	11,275	12,973	14,823	16,857
Claims on private sector	69,282	78,863	85,606	89,483	93,888	98,977	104,745	111,336	118,458
Others	3,781	6,061	6,368	6,814	7,424	8,152	8,957	9,808	10,724
Other items (net) 2/	-22,212	-31,174	-36,432	-42,074	-41,988	-40,865	-34,044	-32,682	-31,243
				percent of GDP					
Credit to the private sector	49.9	53.4	53.2	53.0	51.9	50.1	48.3	46.9	45.7
Broad money (M2)	53.6	55.5	53.4	54.1	54.1	54.1	54.1	54.1	54.1
Monetary base	4.8	4.3	4.9	5.2	5.3	5.4	5.4	5.4	5.4
				percentage change					
Credit to the private sector	17.9	13.8	8.6	4.5	4.9	5.4	5.8	6.3	6.4
Broad money (M2)	6.9	10.2	4.9	6.3	7.0	9.2	9.7	9.4	9.4
Monetary base	35.7	-5.0	24.7	10.0	10.0	10.0	10.0	10.0	10.0
Memorandum items:									
Velocity	1.9	1.8	1.9	1.9	1.9	1.9	1.9	1.9	1.9
Money multiplier	11.1	12.9	10.8	10.4	10.2	10.1	10.1	10.0	10.0
Exchange rate (N$/US$)	11.6	15.6	13.7	13.5	13.8	14.3	14.8	15.4	16.0
Domestic interest rates (end of period)									
Deposit rate	4.2	4.9	5.7	6.0	...	...	...	...	...
Lending rate	8.7	9.3	9.9	9.8	...	...	...	...	...
BoN repo rate	6.0	6.5	7.0	6.8	...	...	...	...	...
Three-month T-bill rate	6.3	7.5	8.9	7.7	...	...	...	...	...

Sources: Namibian authorities and Fund staff estimates and projections.

1/ End of period.

2/ Including valuation.

Table 6. Namibia: Financial Sector Indicators, 2010–Sep 2017

(Percent, unless otherwise indicated)

	2010	2011	2012	2013	2014	2015	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17
Banking indicators													
Capital adequacy													
Capital to assets	8.4	7.8	8.0	8.6	10.3	10.9	10.4	10.6	10.8	11.1	11.0	10.9	10.5
Regulatory capital to risk-weighted assets	15.3	14.0	14.2	14.4	14.7	14.3	15.3	15.2	14.8	15.1	15.6	14.8	15.3
Regulatory tier I capital to risk-weighted assets	11.1	10.8	10.9	11.5	11.9	11.8	12.2	12.3	12.3	12.4	12.0	11.2	12.4
Asset quality													
Large exposure to capital	130.0	147.0	135.0	112.5	170.9	212.5	123.9	126.3	113.8	125.1	129.9	123.7	148.0
Nonperforming loans to total gross loans	2.0	1.5	1.3	1.3	1.5	1.6	1.6	1.6	1.8	1.5	1.4	2.0	2.2
Earnings and profitability													
Trading income to total income	6.5	9.3	7.4	6.5	5.9	6.5	8.0	9.4	6.2	4.6	3.6	5.5	4.7
Return on assets 1/	3.5	3.7	3.3	3.1	3.6	4.8	3.3	2.2	3.6	3.5	3.0	3.0	2.9
Return on equity 1/	41.9	47.1	40.5	31.4	34.9	56.5	31.4	21.2	31.1	32.6	27.7	27.9	27.5
Interest margin to gross income	51.3	54.2	58.8	54.7	56.8	57.4	58.0	57.9	58.3	56.7	36.8	59.0	57.4
Noninterest expenses to gross income	57.3	52.3	54.0	54.8	52.8	51.6	51.7	54.1	53.7	51.0	33.6	55.5	56.0
Personnel expenses to noninterest expenses	49.5	51.5	58.1	50.3	49.7	101.7	118.4	107.6	53.8	49.5	53.9	52.7	54.5
Liquidity													
Liquid assets to total assets	10.7	12.4	10.9	10.7	11.6	11.7	10.8	11.4	10.7	11.4	9.7	10.6	13.6
Liquid assets to short-term liabilities	19.1	22.2	20.7	19.7	21.1	21.9	21.3	23.0	22.5	23.5	19.5	22.7	28.4
Customer deposits to total (non-interbank) loans	106.3	114.7	106.4	102.5	98.6	95.2	100.0	95.0	94.1	95.4	94.5	95.8	99.6
Exposure to foreign exchange risk													
Net open position in foreign exchange to capital	1.3	2.7	2.8	1.7	2.4	5.1	1.0	0.5	4.3	2.7	3.1	-0.8	-0.4
Foreign currency-denominated loans to total loans	0.1	0.3	1.3	2.0	1.4	1.5	1.2	1.3	1.0	0.9	0.7	0.6	0.7
Foreign currency-denominated liabilities to total liabilities	3.7	1.9	2.5	3.7	3.3	3.7	3.0	4.9	3.4	2.8	4.3	4.0	4.7
Memorandum item:													
Holdings government debt to risk-weighted assets	5.7	10.2	9.8	10.2	9.8	10.4	10.1	10.1	9.9	10.1	9.3	9.2	10.8

Sources: Bank of Namibia and IMF staff estimates.

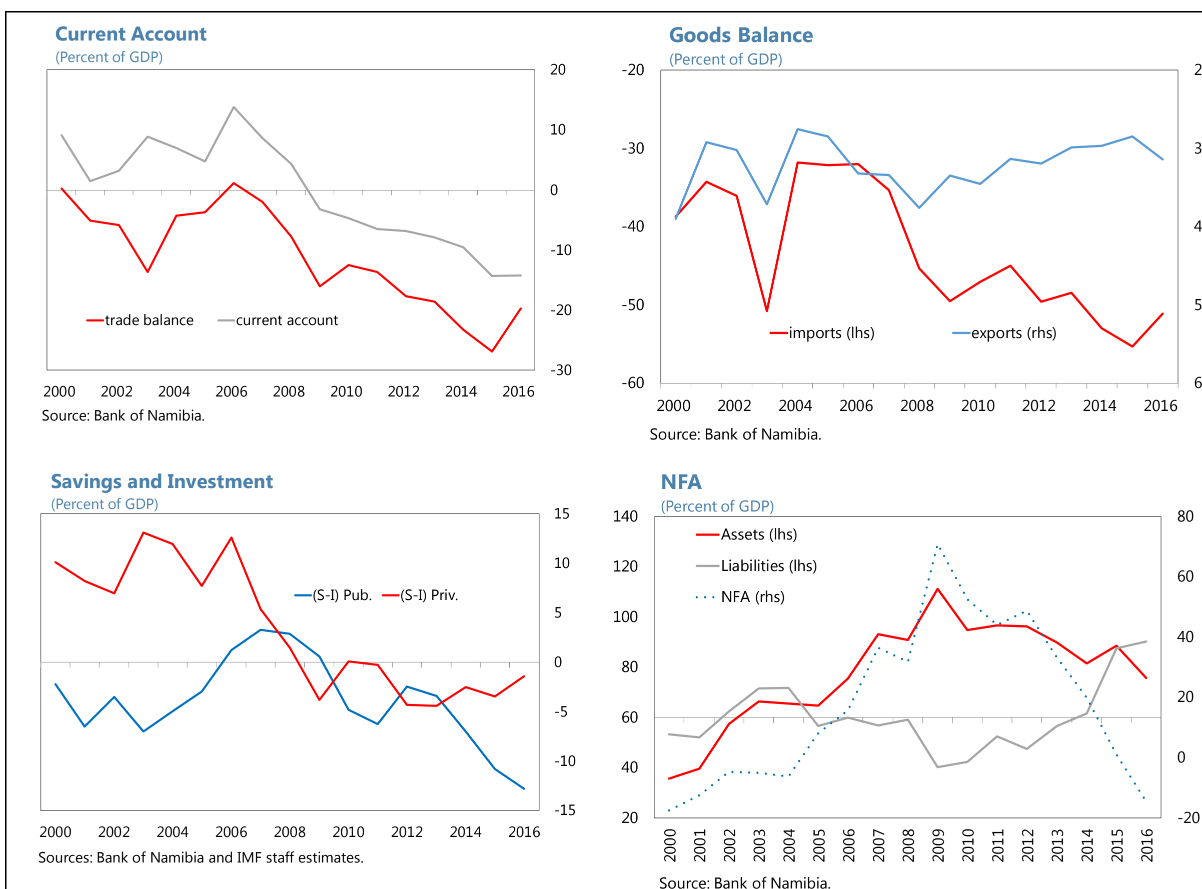
1/ Before taxes.

Annex I. External Sector Assessment

In 2016, Namibia's external position was substantially weaker than suggested by fundamentals, mostly because of large one-off events linked to the construction of new mines. During the first three quarters of 2017, the trade balance sharply improved as the construction of large mines came to an end and imports declined, while mining exports began increasing. These developments are permanent in nature and will likely lead to a change in the assessment of Namibia's external position to moderately weaker than suggested by fundamentals. Given the expected decline in SACU receipts, and a still large fiscal deficit, further fiscal adjustment, as recommended by staff, would help bring the external position broadly in line with fundamentals.

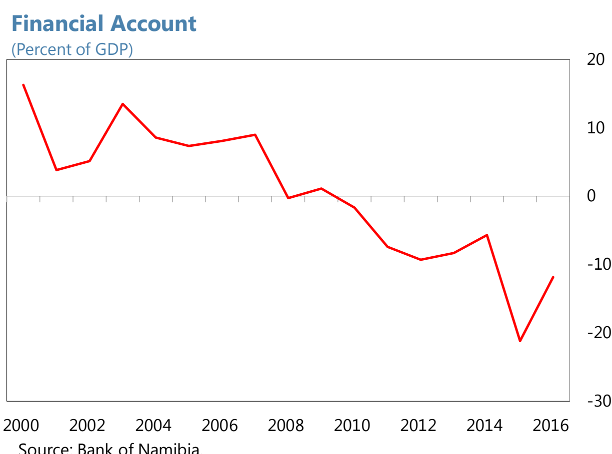
A. Recent Trends

1. Namibia's current account (CA) and net international investment position (NIIP) deteriorated further in 2016. Since 2006, the CA has been deteriorating, turning from positive to negative, until reaching a deficit of 14.1 percent in 2016. This trend is largely attributable to a surge in imports as a share of GDP during the global financial crisis, and a subsequent expansionary fiscal stance and the construction of new mines. The trade balance followed a similar trend, but in 2016 it took a different direction and improved due to both higher exports (from the recovery in the global diamond markets, and higher production from some new mines) and lower imports (as the

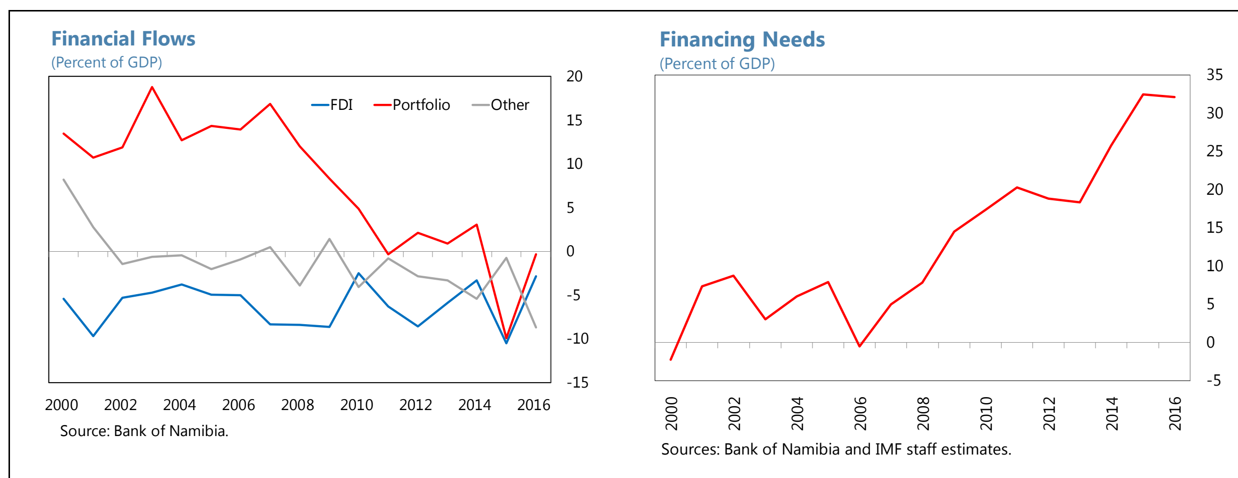


construction of new mines came to an end and the economy sharply deteriorated). However, an abrupt decline in SACU receipts and larger income and service deficits offset the improvement in the trade balance in 2016, leaving the current account deficit substantially unchanged compared to 2015. A savings and investment decomposition suggests that the main driver of the CA deterioration has been the decline in the public balance resulting from an expansionary fiscal stance. At the same time, the NIIP has been deteriorating since 2009 and in 2016, the net foreign position turned negative to -14½ percent of GDP (1 percent of GDP in 2015). In general, the deterioration in the NIIP is attributed to the sharp increase in external liabilities from both the government and non-bank corporates.

2. The CA deficit is mostly financed with FDI and other investments, while portfolio investments have generally registered net outflows. In the early 2000s, the net portfolio investment was positive due to large investments abroad by non-bank financial institutions, mostly the public pension fund. However, the issuance of Eurobonds in 2011 and 2015 generated large offsetting portfolio inflows. At the same time, in 2015 FDI increased while other investments fell as loans from parent mining companies were transformed into equity. Apart from these temporary changes, in 2016, financial flows returned to the composition observed pre-2015. The gross external financing requirements have continuously increased to about 32 percent of GDP, with about half corresponding to short term debt.



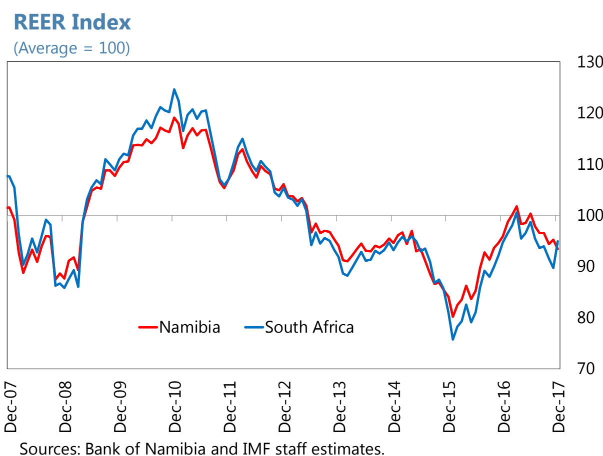
Source: Bank of Namibia.



Source: Bank of Namibia.

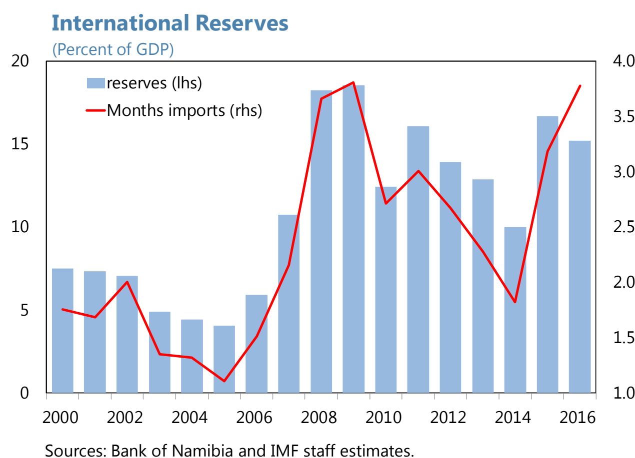
Sources: Bank of Namibia and IMF staff estimates.

3. The Namibian dollar is pegged at par to the South African rand and developments in the real exchange rate largely follow the rand. Namibia's real effective exchange rate (REER) has experienced large fluctuations over the past decade. Between 2010–2015, it depreciated by 30 percent, but appreciated by 20 percent thereafter. In June 2017, the REER returned to its ten-year average, although it depreciated by about 5 percent in the second half of the year.



Sources: Bank of Namibia and IMF staff estimates.

4. The stock of international reserves has fluctuated around 10–15 percent of GDP over the past ten years. At end 2016 reserves stood at 14.7 percent of GDP (3.7 months of projected imports), reflecting an increase in 2015 due to the issuance of the Eurobond and some swap operations by the BoN. In November 2017, reserves further increased to about 4.1 months of imports, reflecting the disbursement of an AfDB budget support loan and an improving current account.



Sources: Bank of Namibia and IMF staff estimates.

B. External Position Assessment

5. The Namibia's external position is assessed using two IMF's panel regression-based methodologies: the CA and REER External Balance Assessment (EBA)-lite models.[1] Both models assume that the CA and REER are endogenous variables that are simultaneously determined as a function of domestic and external variables, including fundamentals, policy variables, cyclical conditions, and the global economic environment. Thus, these methodologies assess the CA and REER in a multilateral-consistent manner, as each country's variables are measured relative to a weighted average of other countries' values.[2] Using these methodologies, a CA gap can be

[1] EBA-lite, an extension of EBA methodologies, uses annual data for 190 countries for the 1995–2015 period and incorporates fundamentals for low and middle-income countries. See further details of the EBA methodology in IMF (2013).

[2] Since the CA and REER are measured relative to other countries, they not only reflect a country's own characteristics but also external conditions within a simultaneously determined general equilibrium system. This also implicitly recognizes that developments in a small economy would mostly influence its own CA and REER, unlike those in a large country.

identified as the difference between the observed and the fitted value from the CA-EBA-lite regression model. In turn, the gap can be explained in terms of deviations of policy variables from their adequate levels and regression residuals (i.e., the unexplained portion). The gap is then converted into a REER misalignment using estimated trade elasticities.

6. The regression-based methodologies suggest that Namibia's REER is moderately overvalued, although the overvaluation is expected to rapidly narrow. The CA gap is estimated to be -8½ percent of GDP, with a fitted CA deficit of 5.6 compared to the actual deficit of 14.1 percent in 2016. The estimated elasticity of the trade balance to changes in the REER is -0.38. Thus, according to the CA-EBA lite approach, the REER would need to depreciate by 23 percent for the CA deficit to be reduced to the fitted value of the regression. However, this gap reflects large one-off events. Based on preliminary data for the first three quarters of 2017, the CA deficit is expected to sharply improve to about -1½ percent of GDP, as imports compress as a share of GDP due to the lower construction activity and the deceleration of the economy. With the 2017 CA deficit declines, the REER would no longer be overvalued but rather undervalued by about 11 percent (CA model). Since the collapse in imports in 2017 likely reflects a degree of overshooting while the increase in real commodity exports is largely structural, given the projected recovery in imports going forward, the CA deficit is expected to converge to a value that would suggest the REER to be moderately overvalued. Against this background, the advised fiscal consolidation will curb imports and help bring the external balance closer to fundamentals over the projection period. However, the REER methodology signals some undervaluation. Using 2016 data (annual averages), the REER is estimated to be undervalued by about 21 percent mainly due to the large depreciation occurred since 2010. Using data from 2017, the undervaluation would only be about 11 percent since the average real exchange rate has recovered. While the two methodologies lead to suggest different assessments, the CA model account for policy stance and is often more reliable.

Model	Observed	Fitted	Gap	Overvaluation
CA	-14.1%	-5.6%	-8.5%	23%
ln(REER)	4.34	4.55	n.a.	-21%

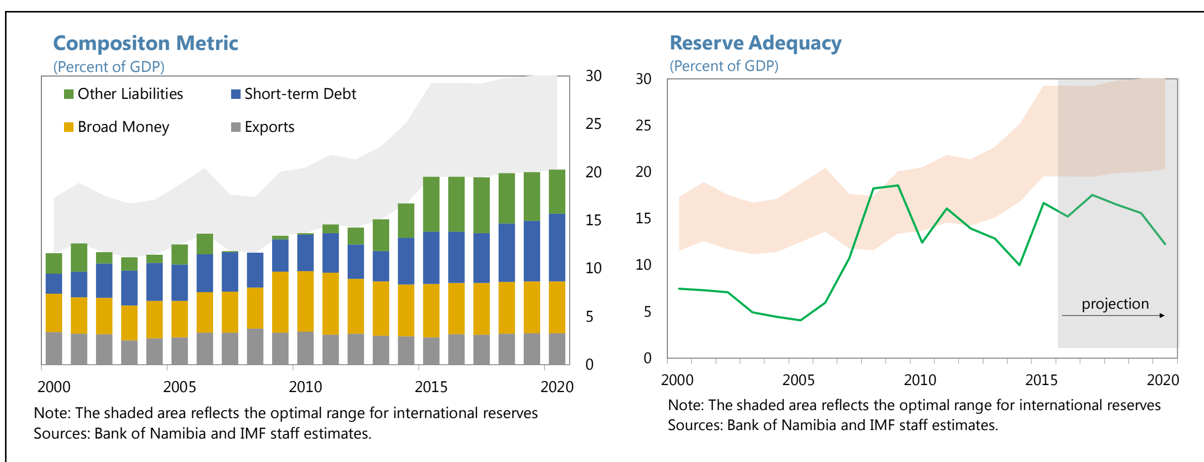
C. International Reserve Adequacy

7. Traditional measures of reserve adequacy are partial indicators of risks and may at times provide conflicting signals. While commonly used adequacy ratios—such as months of imports, cover of short-term debt plus debt service, or percent of broad money—are attractive for their simplicity, they only focus on one specific aspect of vulnerability, and could potentially provide conflicting signals. Moreover, they do not reflect the possibility that a balance of payments crisis can arise from various sources.

8. The IMF's metric to assess reserve adequacy for market access countries encompasses different sources of risk. It employs a risk-weighted measure of different sources of risk.[3] In particular, it incorporates four specific vulnerabilities: (i) export earnings to capture potential losses from terms of trade shocks; (ii) short term debt at remaining maturity (short term debt plus debt service) to reflect rollover risk; (iii) portfolio investments plus medium and long-term debt to account for drains from non-residents' investment; and (iv) broad money as a proxy for resident's capital flight.[4] The weight for each risk is computed based on the drains at the tenth percentile of the annual distributions of percentage changes of each of the items discussed above, during periods of exchange market pressures.[5] Separate distributions are estimated for countries with fixed exchange rates or capital controls. The weights for countries with a fixed exchange rate are:

	Short-term Debt	Other liabilities	Broad Money	Exports
Weights	30%	20%	10%	10%

9. Namibia's international reserves are below the lower bound of the IMF's adequacy metric. Based on the IMF's metric, reserves of 20 to 30 percent of GDP (or 100–150 percent of the metric) are considered adequate, but the latest level of 17½ percent of GDP (November 2017) is below such range. Over the past fifteen years, reserves have been sub-optimal most of the time and reserve coverage was adequate only between 2007 and 2010 due to a combination of temporarily higher SACU transfers and mining revenues, and some fiscal restraint.[6]



Note: The shaded area reflects the optimal range for international reserves
Sources: Bank of Namibia and IMF staff estimates.

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Sources: Bank of Namibia and IMF staff estimates.

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[3] For further details, see IMF (2011, 2013 and 2014). A separate methodology is used for non-market access countries but is not relevant for Namibia (being an upper middle income country with substantial capital inflows and outflows).

[4] Other risks, such as derivative exposures, are excluded due to data limitations.

[5] As in Eichengreen et. al. (1997), an exchange market pressure (EMP) index is constructed as the weighted average of reserve losses, exchange rate depreciation, and increases in interest rates. An episode of EMP occurs when the index deviates more than 1.5 times standard deviations from its average.

[6] It is also important to note that in August 2009 Namibia received US$200 million from an additional SDR allocation.

D. Conclusions

10. Namibia's current account deteriorated over the past decade, but is expected to improve in 2017 and, over time, stabilize at a deficit of about 6 percent of GDP. Despite the expected improvement, international reserves coverage is below adequate levels and is projected to decline over the coming years. However, the implementation of the advised fiscal consolidation would help curb domestic demand and reduce the external imbalance, bringing the CA account better in line with fundamentals, while increasing international reserves to adequate levels (under staff's reform scenario, the current account deficit would stabilize at a deficit of about 2 percent of GDP, largely due to the lower imports from fiscal consolidation, and international reserves would reach 20 percent of GDP by the end of the projection).

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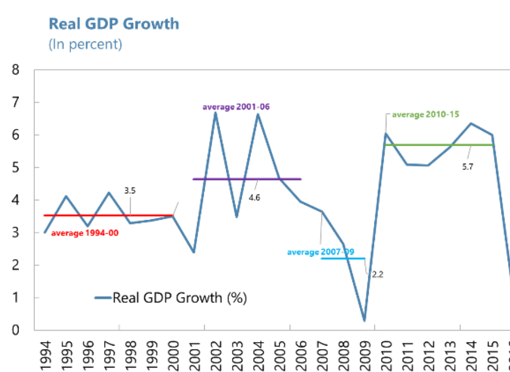
Annex II. Long-Term Growth Trends in Namibia: Returning to Normal[1]

During 2010–15, Namibia experienced a period of exceptional growth sustained in part by temporary factors, which masked receding productivity gains. With temporary expansionary factors coming to an end, recent strong growth appears to have had only short-lived effects on long-term growth trends. Using different methodologies, the analysis suggests that the long-term growth rate has remained at the pre-boom level at around 3½ percent.

A. Strong Growth Performance

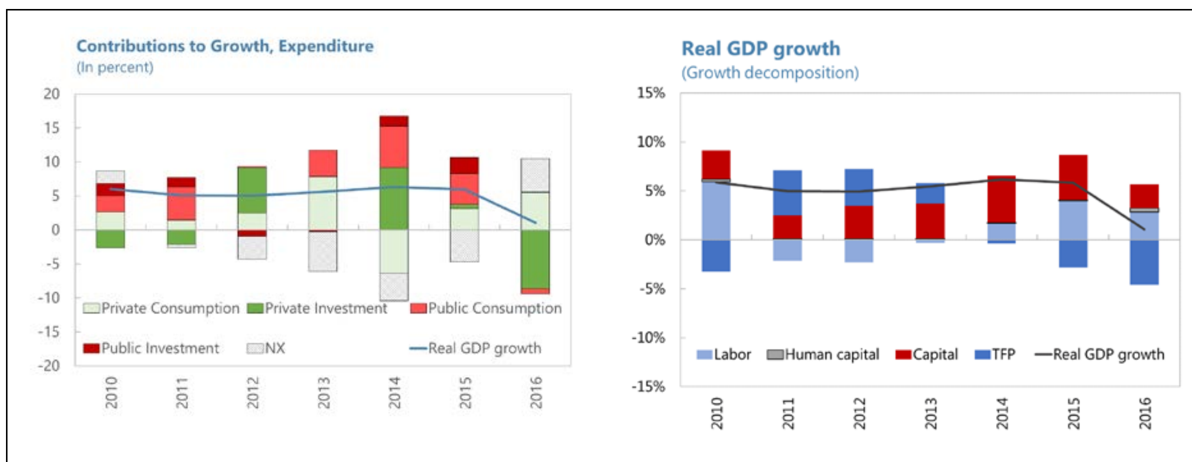
1. **During 2010–15, Namibia experienced a period of exceptional growth with real GDP growing at an average annual rate of 5.7 percent, well above previous trends**. This average growth rate was particularly high compared to what was observed since the country gained independence. In the mid to late nineties, immediately after independence, growth averaged about 3.5 percent, and in the early-2000s it increased to 4.6 percent. After dipping at the time of the global financial crisis, growth sharply recovered and stabilized at around 5½–6 percent for a prolonged period, before a recent sudden correction.



2. **The boost in growth was in part driven by temporary factors and masked weak productivity gains that may constrain positive effects on long-term growth trends.** Large-scale investment in the construction of new mines and an expansionary fiscal policy underpinned the growth increase. Since 2013, three large mines were constructed, including a large uranium mine (Husab), which is expected to become the world's second largest.[2] The construction boom brought a total of N$53.5 billion (in nominal terms) in new investments over a three-year period, with private investment contributing on average 3.3 percentage points to total GDP growth over the same period compared to an average of 1.2 points in the first part of the 2000s. In addition, growth was further fueled by an expansionary fiscal policy that over 2013–15 accounted for 3 percentage points of total growth on average, compared to a small and negative contribution in the first part of the 2000s. Both these factors came to a sudden halt in 2016–17. As a result, real GDP growth decelerated to 1.1 percent in 2016 and began contracting in 2017. These developments raise the question as to how the recent growth drivers may have affected long-term growth trends in Namibia.

[1] Prepared by Paola Ganum.

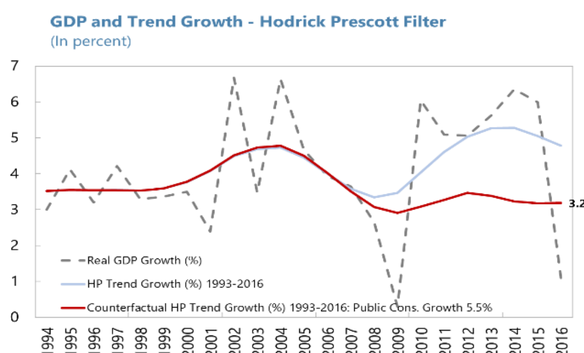
[2] Starting in 2013, three mines were constructed: B2 Gold constructed the Otjikoto gold mine, Swakop uranium developed Husab uranium mine, and Weatherly invested in the Tschudi copper mine.



B. Estimating Long-Term Growth Trends

3. What is the impact of recent growth performance on long-term growth trends in Namibia? Following the methods commonly used in the analysis of growth, long-term growth trends in Namibia could be estimated following three different methodologies: the Hodrick-Prescott filter (with an additional counterfactual exercise), a multivariate filter method, and the production function approach.[3] Given the difficulty in estimating long-term growth, the use of multiple approaches allows for comparing results and balancing merits and drawbacks of the different methodologies.

4. HP filter estimations suggest that long-term growth in Namibia is likely to have remained unchanged and close to the pre-2010 average levels. The HP filter separates trend and cyclical components, and it is widely-used for its simplicity. Estimates of HP trend growth for the period 1994–2016, for which actual data are available, point to an initial increase in potential growth up to 5.1 percent. However, potential growth has declined more recently to about 4.8 percent, reflecting the growth deceleration in 2016 and, given the features of the filter, is expected to decline more as the economy is now contracting. Indeed, one of the issues with the HP filter is that it suffers from a well-known end-point problem, i.e. that estimates of growth trends are very sensitive to latest observations or projections.[4] To isolate the impact of outliers on HP trend estimates, a simple two-step counterfactual exercise can be run to control for the recent



[3] For some examples of country analyses of growth trends, see IMF Country Reports 17/195 (Latvia), 16/105 (Turkey), 14/339 (South Africa), 13/313 (Brazil).

[4] A wide range of growth trends are obtained depending on the period used as a reference.

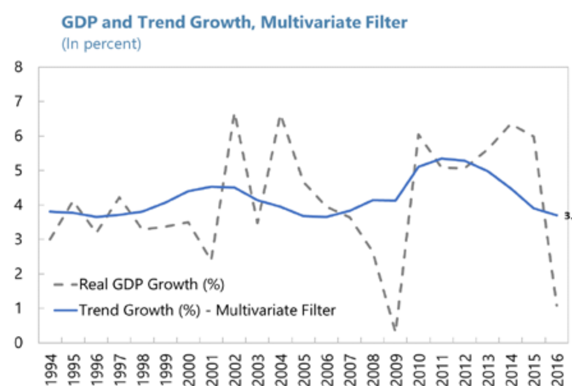
temporary drivers of growth. As part of this exercise, first, GDP during 2010–2016 was re-constructed by eliminating the temporary boost in public expenditure.[5] Second, an HP filter was applied to the revised GDP to extract the trend in growth. The result of this exercise is a rather stable trend in long-term growth, suggesting that factors boosting actual growth were cyclical and unlikely to affect structural trends.

5. Estimates from a multivariate filter approach again suggest that, after an initial increase, long-term potential growth is now close to past trends at around 3½ percent. Following Blagrave and others (2015), the multivariate filter approach offers a theoretical structure to estimate long-term growth rates by conditioning the data to basic economic relationships between the output gap and inflation (Phillips curve), and between output and employment (Okun's law). For Namibia, these relationships were estimated as:

$$\pi_t = 0.44\pi_{t+1} + (1 - 0.44)\pi_{t-1} + 0.11y_t + \varepsilon_t^{\pi}$$

$$\overline{U_t} - U_t = 0.25(\overline{U_t} - U_t) + 0.3y_t + \varepsilon_t^{u}$$

where, π_t denotes inflation rate, y_t output gap, U unemployment rate, and $\overline{U_t}$ indicates the structural unemployment rate. The coefficients of the Phillips curve and Okun's law are Bayesian estimates based on a stochastic process for output in Namibia (see Blagrave et al, 2015). This more structured approach shows that long-term GDP growth increased in 2010–2013, but has now approached the long-term trend value of about 3½ percent prevailing before the 2010s-growth surge.



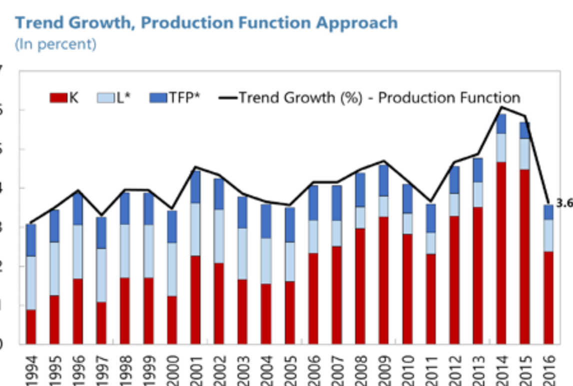
6. The production function approach highlights that trend growth was boosted by capital accumulation, but it has recently declined close to its past trend of about 3½ percent. Under this approach, potential output and growth depend on the supply of labor and capital inputs, and on how productively they are used. Using a typical Cobb-Douglas production function potential GDP can be estimated as:

$$Y_t = A_t K_t^{0.4} L_t^{0.6}$$

---

[5] Public consumption was re-estimated with an assumed conservative growth rate of 5.5 percent, which is twice as much as its average growth rate of 2.7 percent during 1994–2009, but lower than the average growth rate of 10 percent registered during 2010–2016. Then GDP was constructed as the sum of its demand-side components. In this counterfactual exercise, only public expenditure was excluded, although a more complete exercise would require additionally to exclude one-off mine construction activities.

where Y denotes real GDP, K the actual capital stock estimated using the perpetual inventory method, L indicates employment estimated using an HP filter, and A is total factor productivity (TFP).[6] This approach highlights that capital has underpinned an increase in long-term growth between 2011–14, masking however a declining productivity contribution to growth.[7] It also points to a recent return of long-term growth to pre-boom levels. The major factor contributing to the recent decline is again lower capital as real investment growth in 2016 declined 25 percent, with mining investment accounting for most of this decline.



C. Conclusions

7. Following a temporary increase in growth during 2010–15, trend growth is estimated to return to its previous norm of about 3–4 percent. The different methodologies used to estimate long-term trends after the temporary early 2010s boost in growth point to growth rates between 3.2–3.7 percent. Hence, long-term trends in growth appeared to have been little affected by the temporary increase in capital as productivity gains have receded at the same time. Recent studies have found similar declines in productivity in the region (e.g., South Africa, IMF Country Report 14/339), Europe (e.g., Latvia, Turkey) and South America (e.g., Brazil). More generally, the same trends have been observed across emerging market economies (IMF 2015). In the case of Namibia, given the high-growing wages and declining productivity, it is key to put a premium on structural reforms to improve productivity.

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[6] TFP is estimated in two steps. First, actual TFP is estimated as observed real GDP divided by actual capital and labor (with each input elevated to its respective share as expressed in the production function). Second, TFP is HP-filtered to extract its trend component. The capital and labor share coefficients reflect parameters commonly used in the literature on growth accounting for non-advanced economies.

[7] Results on productivity should be interpreted with caution since TFP is a residual and the quality of its measurement depends on the data quality of output, capital, and labor.

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Annex III. Risk Assessment Matrix[1]

Source of main risks	Relative Likelihood and Time Horizon	Expected impact on the economy	Recommended Policy Response
Weaker global growth, with: (i) slowdown in China and growth decline in other large emerging economies, particularly South Africa; (ii) structurally weak growth in key advanced economies.	**Medium /High** **ST, MT**	**Medium.** Current account and fiscal balance deterioration through lower commodity prices, depressed exports, and lower SACU revenues as South Africa growth deteriorates; rising public debt ratio and declining international reserve coverage.	Accelerate structural reforms to promote growth and private sector development. If government's financing becomes problematic or debt dynamics unsustainable, further fiscal consolidation would be required.
Tighter global financial conditions, with Fed normalization and ECB tapering balance sheet expansion prompting higher rates, stronger US dollar, and market corrections.	**High** **ST**	**Medium.** Higher interest rates, reduced financial inflows, and costly and tighter sovereign financing; additional strain on fiscal and external accounts. Possible rand depreciation and inflationary pressures.	Increase policy rate in line with the South African Reserve Bank. Seek additional external financing in rand to support reserves. Provide liquidity as needed. Tighten fiscal policy if financing becomes problematic, while protecting social spending.
Incomplete or weak policy implementation, that undermines confidence in the government's fiscal adjustment plans, e.g., triggered by political and capacity constraints, and materialization of contingent liabilities.	**Medium** **MT**	**High.** Fast rising public debt, and tighter budget financing; declining international reserves; possible disorderly fiscal adjustment and deterioration in financial sector's asset quality	Tighten fiscal policy over the next three years through long-lasting measures. Accelerate reforms to improve extra-budgetary entities' performance. Monitor and manage key fiscal risks and financial sector vulnerabilities.
Accelerated adjustment in real estate prices and credit growth, as house valuations align with fundamentals.	**Medium** **ST, MT**	**Medium.** Increase in nonperforming loans, erosion of banks' capital buffers and deleveraging. Lower growth as private sector credit and construction activity slow down.	Monitor building up of systemic risks. Accelerate plans to create an effective resolution framework. Provide emergency liquidity if needed. In case of a banking crisis, limit the fiscal costs and support the declining demand.
Weaker than anticipated domestic growth, e.g., from lower production from the new uranium mine, weaker consumption from highly indebted households.	**Medium** **ST, MT**	**Medium.** Larger fiscal and current account deficits. Increasing public financing requirements and public debt.	Step up structural reforms to promote growth and private sector development.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff under current policies). The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability of 30 percent or more; ST and MT are meant to indicate that the risks could materialize within 1 year and 3 years, respectively). The RAM reflects staff's views on the sources of risk and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

Annex IV. Debt Sustainability Analysis

In recent years, Namibia's debt indicators have deteriorated. With SACU revenue expected to decline, fiscal deficit and government's gross financing needs are projected to remain large and public debt to increase further, approaching the DSA risk threshold. This leaves Namibia's public debt outlook exposed to risks from delayed fiscal consolidation and vulnerable to macroeconomic and contingent liability shocks, with rollover and exchange rate risks compounding the risk assessment. The external debt profile indicates vulnerabilities to exchange rate depreciation and current account shocks.

A. Public Debt[1]

Background

1. Namibia's public debt ratio has been rising since 2010 driven by an expansionary fiscal policy. Between FY10/11 and FY16/17, the public debt to GDP ratio increased from 16 percent of GDP to 44.3 percent of GDP, and the average primary deficit exceeded 6 percent of GDP. Sharp increases in recurrent expenditures, particularly wage and transfers, kept the deficit large. Therefore, in FY16/17 public debt exceeded the authorities' own debt management ceiling (35 percent of GDP).

2. With rising gross financing needs, the authorities have been recently diversifying their funding sources. Between FY14/15 and FY16/17, gross financing needs averaged 16 percent of GDP, slightly above the typical 15 percent of GDP debt distress risk threshold. At the same time, the authorities have been diversifying their funding sources and borrowing instruments, expanding external borrowing, and extending maturities. In 2015, they issued a US$750 million ten-year Eurobond, and between 2015 and 2016 they issued rand denominated bonds for about N$2 million, while expanding the maturity structure with 30-year instruments. Nevertheless, the domestic market has remained the main source of government financing. Banks tend to buy short-term debt, while non-bank institutions focus on the longer-dated fixed rate and inflation indexed instruments.

3. Nevertheless, the maturity and composition of public debt carry some rollover and exchange rate risks. Since FY11/12 domestic short-term debt has averaged at about 42 percent of domestic debt and 27 percent of total debt. While the recent issuance of external debt has reduced the reliance of short-term debt, it has increased foreign exchange risks with non-rand foreign currency debt averaging about 32 percent of total debt at the end of FY16/17.

Outlook and Risks

4. Under the DSA baseline, the public debt ratio and government's financing needs will continue rising over the projection period, reaching debt distress levels (Figures 1–4). Under staff's baseline, the public debt ratio would reach about 69.7 percent of GDP by FY22/23, close to the high risk of debt distress threshold. The primary deficit would exceed 4 percentage points of GDP during most of the projection period and gross financing needs would continue to grow

[1] Analysis based on fiscal year (April 1-March 31).

reaching 23 percent of GDP by FY21/22. An expected decline in SACU revenue is one of the major factors underlying the deterioration. To finance the deficit, the projections assume additional bond issuances, both in the domestic market and in the Johannesburg Stock Exchange (JSE), and T-bills; they also assume that the Eurobond coming due in FY21/22 is replaced by more expensive bond financing. Because of these assumptions, reliance on long-term bond financing from non-bank financial institutions would roughly double by FY 22/23.

5. Alternative scenarios and stress analysis highlight debt vulnerabilities, particularly to macroeconomic and contingent liability shocks (Figures 5–6). With gross financing needs averaging above 20 percent of GDP, macroeconomic or contingent liability shocks could trigger a debt distress episode even if the debt level itself remains in a low or medium risk area. A contingent liability shock (with default of all guaranteed debt, equivalent to 21 percent of FY17/18 noninterest expenditures, combined with real GDP and interest rate shocks) would lead to a debt level and gross financing needs of 83 and 24 percent of GDP, respectively, by FY22/23. A SACU revenue shock (with an additional 3 percent of GDP reduction in SACU revenue, a temporary 2 percentage points real GDP growth shock and 225bps increase in interest rates) would result in an increase in the debt-to-GDP ratio and gross financing needs to about 80 and 241 percent of GDP, respectively. A macro-fiscal shock—entailing shocks to growth and interest rates, and a temporary lower primary balance—would result in the sharpest increase in the debt-to-GDP ratio and gross financing needs to 91 and 28 percent, respectively. Exchange rate and temporary real GDP shocks would have smaller effects on debt and on gross financing needs, but nevertheless they would both push the debt above the high risk of debt distress threshold given the initially high baseline debt ratio.

6. Under staff's reform scenario, the public debt ratio and gross financing needs would remain below critical thresholds. Under this scenario (see main text), additional measures of about 5–6 percent of GDP, spread over three years, would bring debt on a declining path and to around 51 percent of GDP by FY 22/23, and contain gross financing needs on average to below 17 percent of GDP over the projection period.

B. External Debt[2]

7. In 2016, Namibia's external debt continued to rise due to both public and private borrowing. The stock of public external debt increased by 4 percentage points of GDP, reaching 17 percent of GDP at end-2016. Private sector external debt (about 70 percent of total external debt) increased by 8 percentage points of GDP. About 90 percent of total external debt has long and medium-term maturities.

External Debt

(percent of GDP)	2013	2014	2015	2016
Total	37.1	43.0	48.2	60.2
Public (without guarantees)	7.9	8.0	13.1	17.1
Private	29.2	35.0	35.1	43.0
By maturity				
Short-term	8.1	8.0	5.9	5.9
Long and medium-term	29.0	35.0	42.3	54.2

Sources: BoN, and IMF staff estimates

[2] Analysis based on calendar year.

8. External debt is projected to slowly increase over time. The external debt-to-GDP ratio is foreseen to increase from 60 percent of GDP to about 69 percent as the non-interest current account deficit (CAD) is expected to only gradually approach the debt-stabilizing level (Table 1). Gross external financing needs (GEFN) are projected to average about 23 percent of GDP over the projection period, with short-term debt amortization amounting to about a third of the GEFN.

9. Sensitivity tests suggest that the external debt is vulnerable to current account and real depreciation shocks. Standardized sensitivity analysis indicates that a 30 percent exchange rate depreciation in 2018 would increase external debt to about 85 percent of GDP, as only about 20 percent of external debt is denominated in a foreign currency different from the South African rand. If the non-interest CAD widened by 3.5 percent of GDP (1/2 standard deviation shock) during 2018–22, external debt would increase to about 106 percent of GDP by 2022. The impact of real interest rate shocks is small due to the sizeable share of fixed-rate debt.

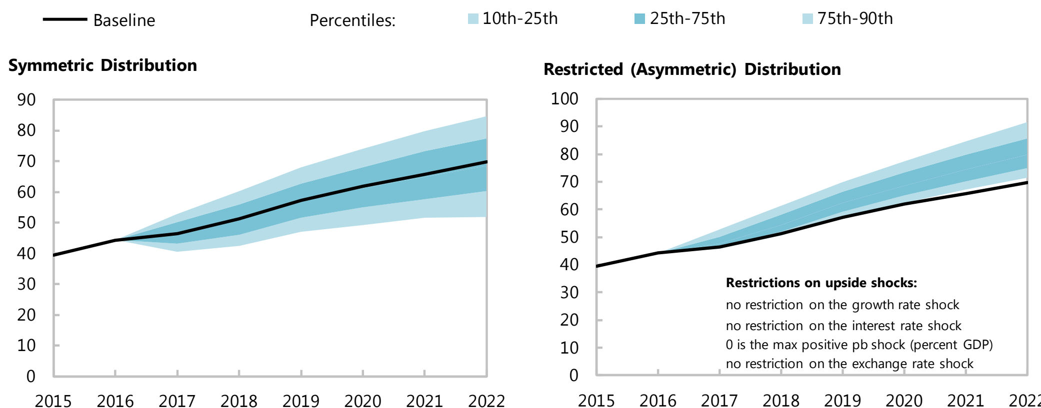
Figure 1. Namibia Public DSA Risk Assessment

Heat Map

Debt level [1/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs [2/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile [3/]	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

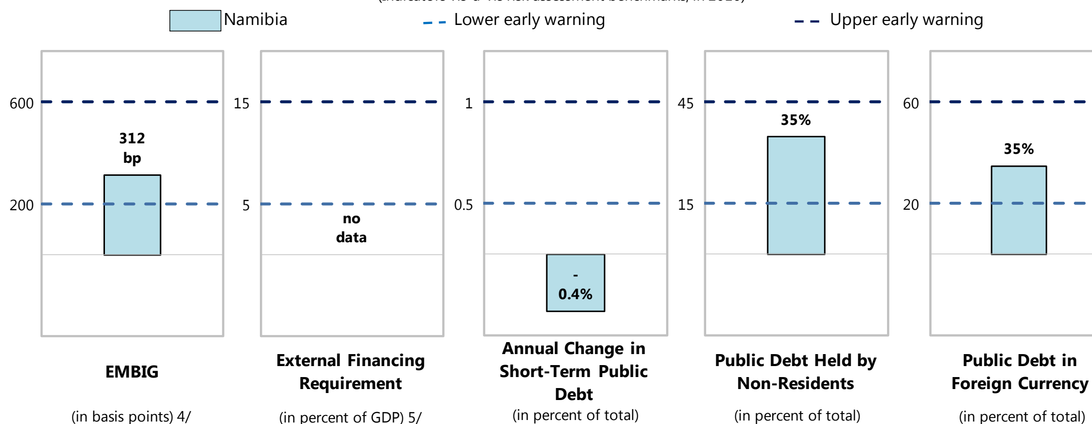
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2016)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.

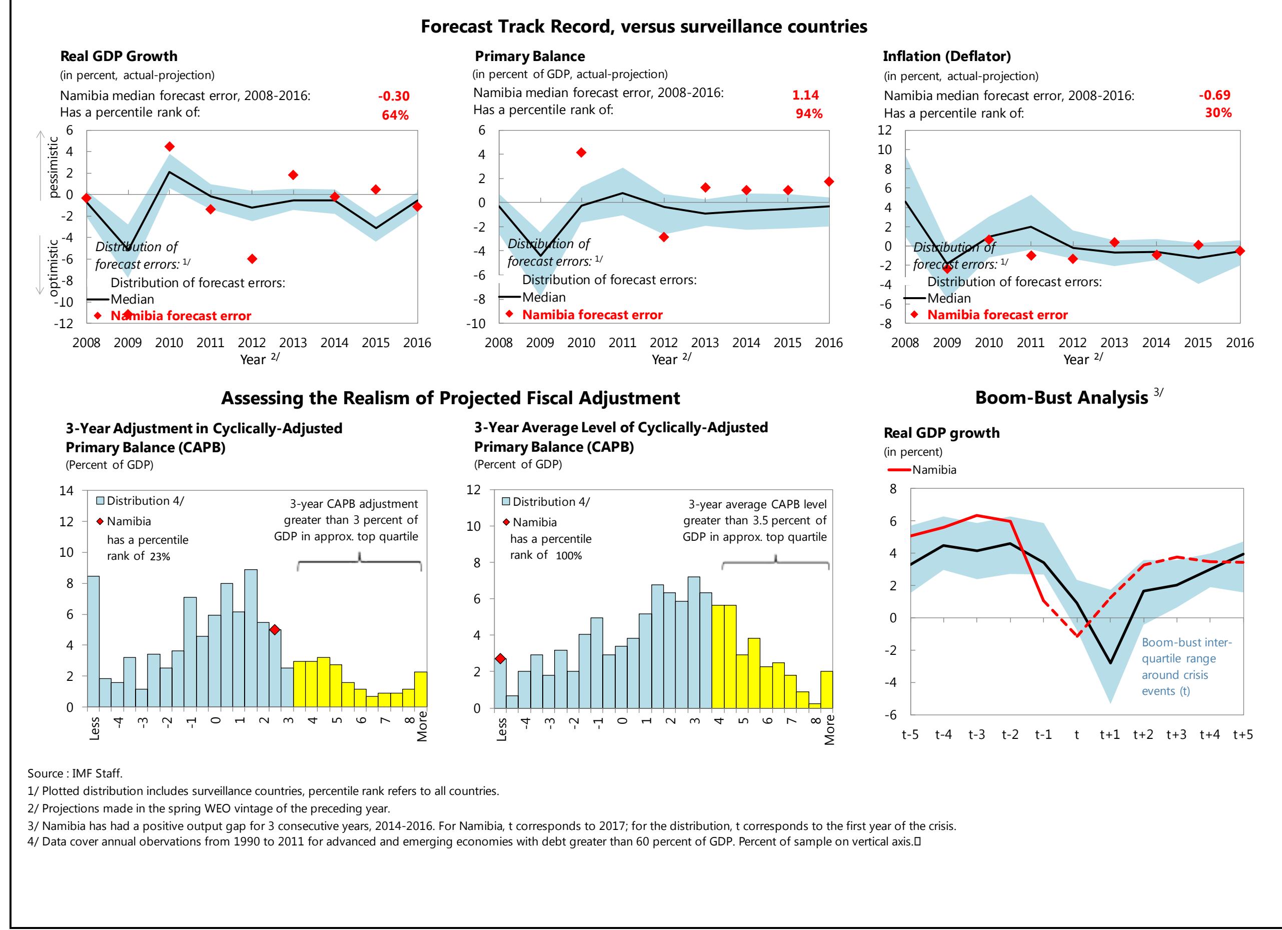
Lower and upper risk-assessment benchmarks are:

200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ EMBIG, an average over the last 3 months, 18-Oct-17 through 16-Jan-18.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Figure 2. Namibia Public DSA – Realism of Baseline Assumptions



Source : IMF Staff.

1/ Plotted distribution includes surveillance countries, percentile rank refers to all countries.

2/ Projections made in the spring WEO vintage of the preceding year.

3/ Namibia has had a positive output gap for 3 consecutive years, 2014-2016. For Namibia, t corresponds to 2017; for the distribution, t corresponds to the first year of the crisis.

4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure 3. Namibia Public Sector Debt Sustainability Analysis (DSA) – Baseline Scenario

(In Percent of GDP, unless otherwise indicated)

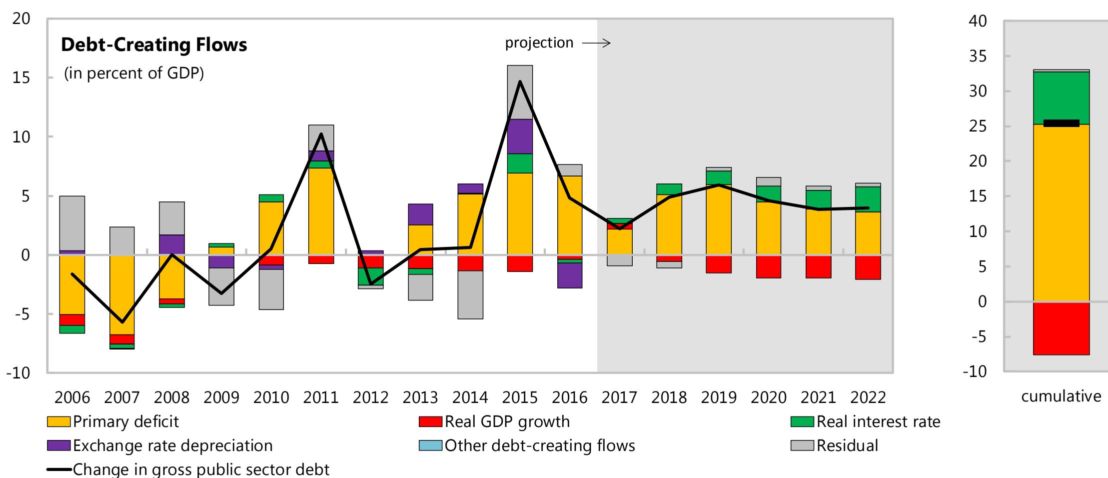
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2006-2014 [2/]	2015	2016	2017	2018	2019	2020	2021	2022
Nominal gross public debt	21.4	39.4	44.3	46.5	51.4	57.3	61.9	65.7	69.7
Public gross financing needs	...	15.9	18.5	15.6	20.7	19.9	20.6	23.2	20.7
Real GDP growth (in percent)	4.3	6.0	1.1	-1.2	1.2	3.3	3.8	3.5	3.5
Inflation (GDP deflator, in percent)	8.4	0.4	7.9	6.2	5.8	5.7	5.7	5.8	5.7
Nominal GDP growth (in percent)	12.7	7.1	8.0	5.5	7.6	9.3	9.7	9.4	9.4
Effective interest rate (in percent) [4/]	8.2	7.5	7.2	7.0	7.9	8.4	8.6	8.7	9.5

As of January 16, 2018		
Sovereign Spreads		
EMBIG (bp) 3/		298
5Y CDS (bp)		N.A
Ratings	Foreign	Local
Moody's	Baa3	Baa3
S&Ps	n.a.	n.a.
Fitch	BBB-	BBB

Contribution to Changes in Public Debt

	Actual			Projections							
	2006-2014	2015	2016	2017	2018	2019	2020	2021	2022	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	-0.1	14.7	4.8	2.2	4.9	5.9	4.6	3.9	4.0	25.4	
Identified debt-creating flows	0.0	10.1	3.9	3.1	5.5	5.6	3.9	3.5	3.7	25.2	
Primary deficit	0.5	6.9	6.7	2.2	5.1	5.9	4.5	3.9	3.6	25.2	0.1
Primary (noninterest) revenue and grants	32.0	34.6	31.2	34.2	31.6	30.0	30.9	30.6	30.6	187.9	
Primary (noninterest) expenditure	32.5	41.5	37.9	36.4	36.7	36.0	35.4	34.5	34.2	213.2	
Automatic debt dynamics [5/]	-0.5	3.2	-2.8	0.9	0.4	-0.4	-0.6	-0.4	0.1	-0.1	
Interest rate/growth differential [6/]	-1.0	0.3	-0.7	0.9	0.4	-0.4	-0.6	-0.4	0.1	-0.1	
Of which: real interest rate	-0.2	1.7	-0.3	0.4	0.9	1.1	1.3	1.6	2.1	7.5	
Of which: real GDP growth	-0.8	-1.4	-0.4	0.5	-0.5	-1.5	-2.0	-2.0	-2.1	-7.6	
Exchange rate depreciation [7/]	0.5	2.9	-2.2	...	...	...	...	...	...	...	
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Privatization Proceeds (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8/]	-0.1	4.6	1.0	-0.9	-0.6	0.3	0.7	0.4	0.3	0.3	



Source: IMF staff.

1/ Public sector is defined as central government.

2/ Based on available data.

3/ EMBIG.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

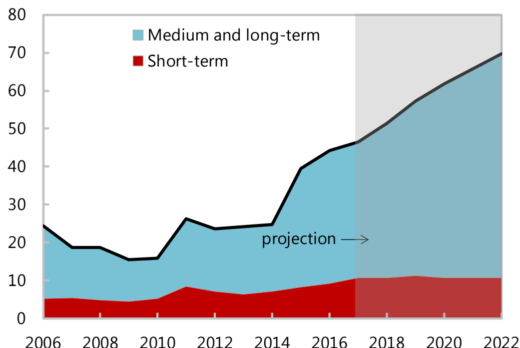
8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

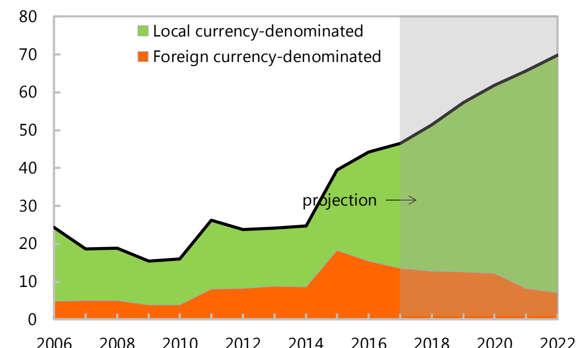
Figure 4. Namibia Public DSA – Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

By Maturity
(in percent of GDP)



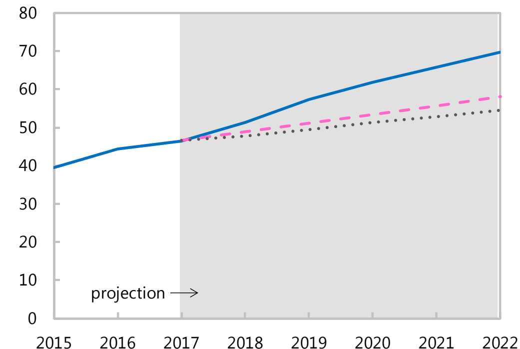
By Currency
(in percent of GDP)



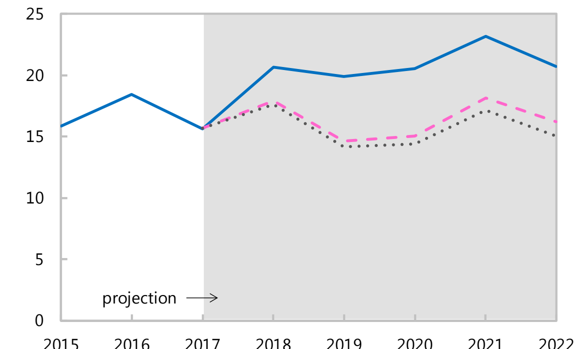
Alternative Scenarios

Baseline Historical Constant Primary Balance

Gross Nominal Public Debt
(in percent of GDP)



Public Gross Financing Needs
(in percent of GDP)



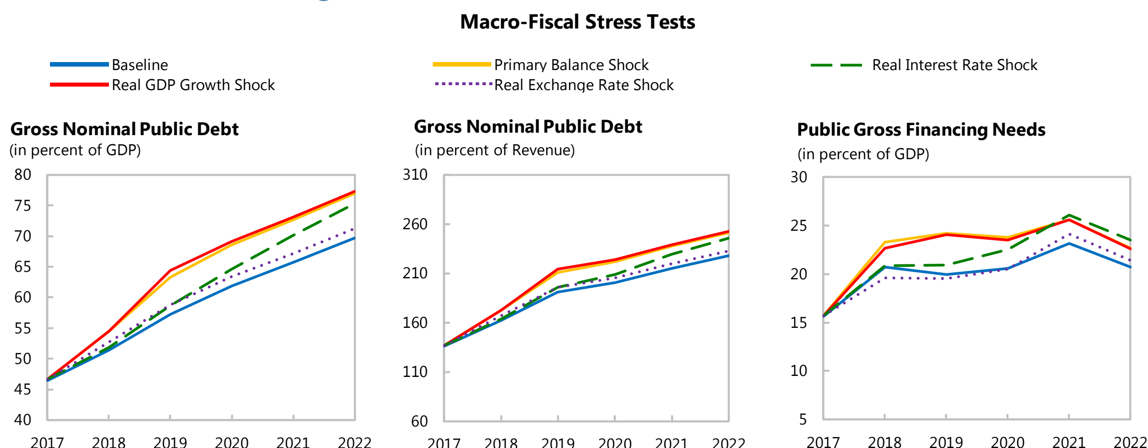
Underlying Assumptions
(in percent)

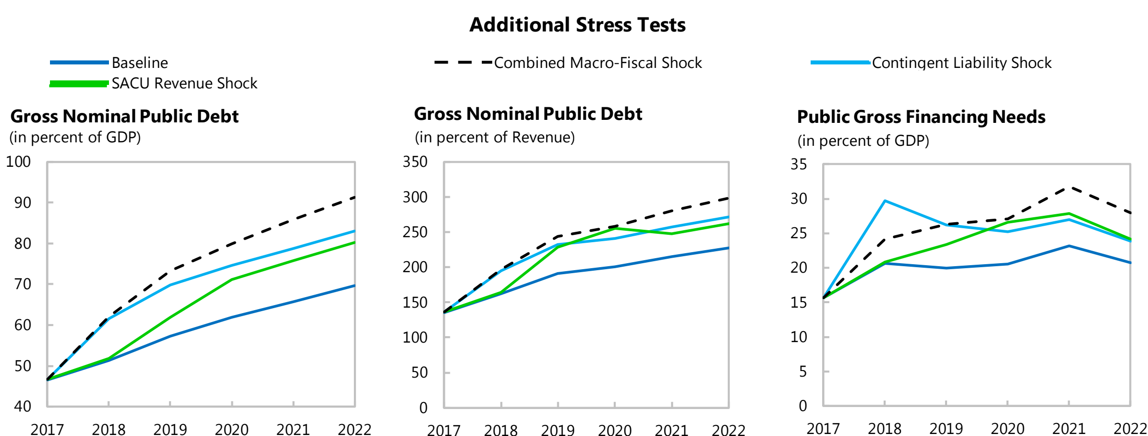
Baseline Scenario	2017	2018	2019	2020	2021	2022
Real GDP growth	-1.2	1.2	3.3	3.8	3.5	3.5
Inflation	6.2	5.8	5.7	5.7	5.8	5.7
Primary Balance	-2.2	-5.1	-5.9	-4.5	-3.9	-3.6
Effective interest rate	7.0	7.9	8.4	8.6	8.7	9.5
Constant Primary Balance Scenario						
Real GDP growth	-1.2	1.2	3.3	3.8	3.5	3.5
Inflation	6.2	5.8	5.7	5.7	5.8	5.7
Primary Balance	-2.2	-2.2	-2.2	-2.2	-2.2	-2.2
Effective interest rate	7.0	7.9	8.3	8.4	8.6	9.4

Historical Scenario	2017	2018	2019	2020	2021	2022
Real GDP growth	-1.2	4.2	4.2	4.2	4.2	4.2
Inflation	6.2	5.8	5.7	5.7	5.8	5.7
Primary Balance	-2.2	-2.3	-2.3	-2.3	-2.3	-2.3
Effective interest rate	7.0	7.9	7.7	7.7	7.7	8.3

Source: IMF staff.

Figure 5. Namibia Public DSA – Stress Tests





Underlying Assumptions
(in percent)

	2017	2018	2019	2020	2021	2022
Primary Balance Shock						
Real GDP growth	-1.2	0.7	2.8	3.3	3.5	3.5
Inflation	6.2	5.8	5.7	5.7	5.8	5.7
Primary balance	-2.2	-7.5	-8.3	-4.5	-3.9	-3.6
Effective interest rate	7.0	7.9	8.9	9.3	9.2	9.8
Real Interest Rate Shock						
Real GDP growth	-1.2	1.2	3.3	3.8	3.5	3.5
Inflation	6.2	5.8	5.7	5.7	5.8	5.7
Primary balance	-2.2	-5.1	-5.9	-4.5	-3.9	-3.6
Effective interest rate	7.0	7.9	10.3	11.0	11.7	11.2
Combined Shock						
Real GDP growth	-1.2	-1.0	1.1	3.3	3.5	3.5
Inflation	6.2	5.2	5.2	5.7	5.8	5.7
Primary balance	-2.2	-7.5	-8.4	-4.5	-3.9	-3.6
Effective interest rate	7.0	8.8	10.0	10.8	11.4	11.2
SACU Revenue Shock						
Real GDP growth	-1.2	1.2	1.3	1.8	3.5	3.5
Inflation	6.2	5.8	5.7	5.7	5.8	5.7
Primary balance	-2.2	-5.1	-8.9	-7.5	-3.9	-3.6
Effective interest rate	7.0	7.9	8.4	9.4	10.0	10.2

	2017	2018	2019	2020	2021	2022
Real GDP Growth Shock						
Real GDP growth	-1.2	-1.0	1.1	3.8	3.5	3.5
Inflation	6.2	5.2	5.2	5.7	5.8	5.7
Primary balance	-2.2	-6.5	-8.4	-4.5	-3.9	-3.6
Effective interest rate	7.0	7.9	8.5	8.9	8.9	9.6
Real Exchange Rate Shock						
Real GDP growth	-1.2	1.2	3.3	3.8	3.5	3.5
Inflation	6.2	18.0	5.7	5.7	5.8	5.7
Primary balance	-2.2	-5.1	-5.9	-4.5	-3.9	-3.6
Effective interest rate	7.0	8.8	8.2	8.4	8.5	9.4
Contingent Liability Shock						
Real GDP growth	-1.2	-1.0	1.1	3.8	3.5	3.5
Inflation	6.2	5.2	5.2	5.7	5.8	5.7
Primary balance	-2.2	-12.8	-5.9	-4.5	-3.9	-3.6
Effective interest rate	7.0	9.7	9.4	9.0	9.2	9.8

Source: IMF staff.

Table 1. Namibia: External Debt Sustainability Framework, 2012–2022

(In percent of GDP, unless otherwise indicated)

		Actual							Projections						
		2012	2013	2014	2015	2016	10-Year Historical Average	10-Year Standard Deviation	2017	2018	2019	2020	2021	2022	Debt-stabilizing non-interest current account 6/
1	**Baseline: External debt**	36.7	37.1	43.0	48.2	60.2			**60.6**	**64.4**	**66.3**	**67.3**	**68.5**	**68.7**	**-3.5**
2	Change in external debt	1.2	0.4	5.9	5.2	12.0			0.5	3.8	1.9	1.0	1.2	0.3	
3	Identified external debt-creating flows (4+8+9)	-4.6	-1.7	5.7	9.1	8.8			-1.8	-0.9	0.0	0.3	0.3	0.3	
4	Current account deficit, excluding interest payments	5.4	3.8	10.5	12.3	13.5			0.6	2.1	2.9	3.2	3.4	3.5	
5	Deficit in balance of goods and services	13.7	15.7	22.4	25.2	20.4			10.5	11.1	11.2	12.2	12.0	11.8	
6	Exports	42.0	43.7	44.3	42.9	37.3			35.6	36.6	37.2	37.2	36.7	36.2	
7	Imports	55.7	59.3	66.7	68.1	57.7			46.1	47.7	48.3	49.4	48.7	48.0	
8	Net non-debt creating capital inflows (negative)	-8.7	-6.6	-4.9	-8.1	-2.8			-3.9	-3.8	-3.2	-3.0	-3.2	-3.2	
9	Automatic debt dynamics 1/	-1.3	1.1	0.0	4.9	-1.9			1.5	0.8	0.2	0.2	0.2	0.0	
10	Contribution from nominal interest rate	0.3	0.2	0.2	0.3	0.7			0.9	1.5	2.2	2.6	2.4	2.2	
11	Contribution from real GDP growth	-1.7	-2.1	-2.3	-2.8	-0.6			0.6	-0.7	-2.0	-2.4	-2.2	-2.3	
12	Contribution from price and exchange rate changes 2/	0.1	3.0	2.1	7.4	-2.0			...	...	...	...	...	...	
13	Residual, incl. change in gross foreign assets (2-3) 3/	5.8	2.1	0.2	-3.9	3.2			2.2	4.7	1.9	0.7	0.8	0.0	
	External debt-to-exports ratio (in percent)	87.5	85.0	97.0	112.3	161.5			170.4	175.9	178.4	181.1	186.6	190.0	
	Gross external financing need (in billions of US dollars) 4/	2.3	1.8	3.4	3.5	3.4			2.2	2.9	3.3	3.6	3.9	4.2	
	in percent of GDP	17.4	14.3	26.7	29.9	31.0			17.6	21.6	23.4	24.1	24.8	25.3	
	Scenario with key variables at their historical averages 5/								**68.4**	**72.5**	**72.5**	**71.2**	**70.0**	**67.8**	**-10.1**
	Key Macroeconomic Assumptions Underlying Baseline														For debt stabilization
	Nominal GDP (US dollars)	13.0	12.7	12.8	11.6	10.9			12.6	13.3	14.1	14.9	15.8	16.6	17.5
	Real GDP growth (in percent)	5.1	5.6	6.4	6.0	1.1	4.2	2.2	-1.2	1.2	3.3	3.8	3.5	3.5	3.5
	GDP deflator in US dollars (change in percent)	-0.3	-7.4	-5.4	-14.6	-6.5	-0.5	9.5	16.6	4.2	2.5	2.3	1.9	1.7	1.9
	Nominal external interest rate (in percent)	0.9	0.7	0.6	0.7	1.3	1.6	1.6	1.7	2.6	3.6	4.1	3.7	3.4	3.4
	Growth of exports (US dollar terms, in percent)	6.1	1.6	2.0	-12.4	-17.9	3.2	11.7	10.0	8.6	7.4	6.2	4.1	3.7	
	Growth of imports (US dollar terms, in percent)	15.3	4.2	13.0	-7.5	-20.0	8.7	14.4	-8.0	9.3	7.1	8.5	3.9	3.6	
	Current account balance, excluding interest payments	-5.4	-3.8	-10.5	-12.3	-13.5	-4.2	6.9	-0.6	-2.1	-2.9	-3.2	-3.4	-3.5	
	Net non-debt creating capital inflows	8.7	6.6	4.9	8.1	2.8	6.8	1.9	3.9	3.8	3.2	3.0	3.2	3.2	
	B. Bound Tests														
	B1. Nominal interest rate is at historical average plus one standard deviation								**61.5**	**66.2**	**69.0**	**70.9**	**72.9**	**74.0**	**-5.5**
	B2. Real GDP growth is at historical average minus one standard deviations								**62.0**	**67.2**	**70.5**	**72.8**	**75.3**	**76.8**	**-5.5**
	B3. Non-interest current account is at historical average minus one standard deviations								**67.5**	**78.0**	**86.2**	**93.3**	**100.2**	**105.9**	**-8.1**
	B4. Combination of B1-B3 using one standard deviation shocks								**66.7**	**76.6**	**84.5**	**91.3**	**98.2**	**104.0**	**-5.8**
	B5. One time 30 percent real depreciation in 2018								**60.6**	**74.6**	**78.6**	**81.2**	**83.9**	**85.3**	**-8.8**

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollars, g = real GDP growth rate.
e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

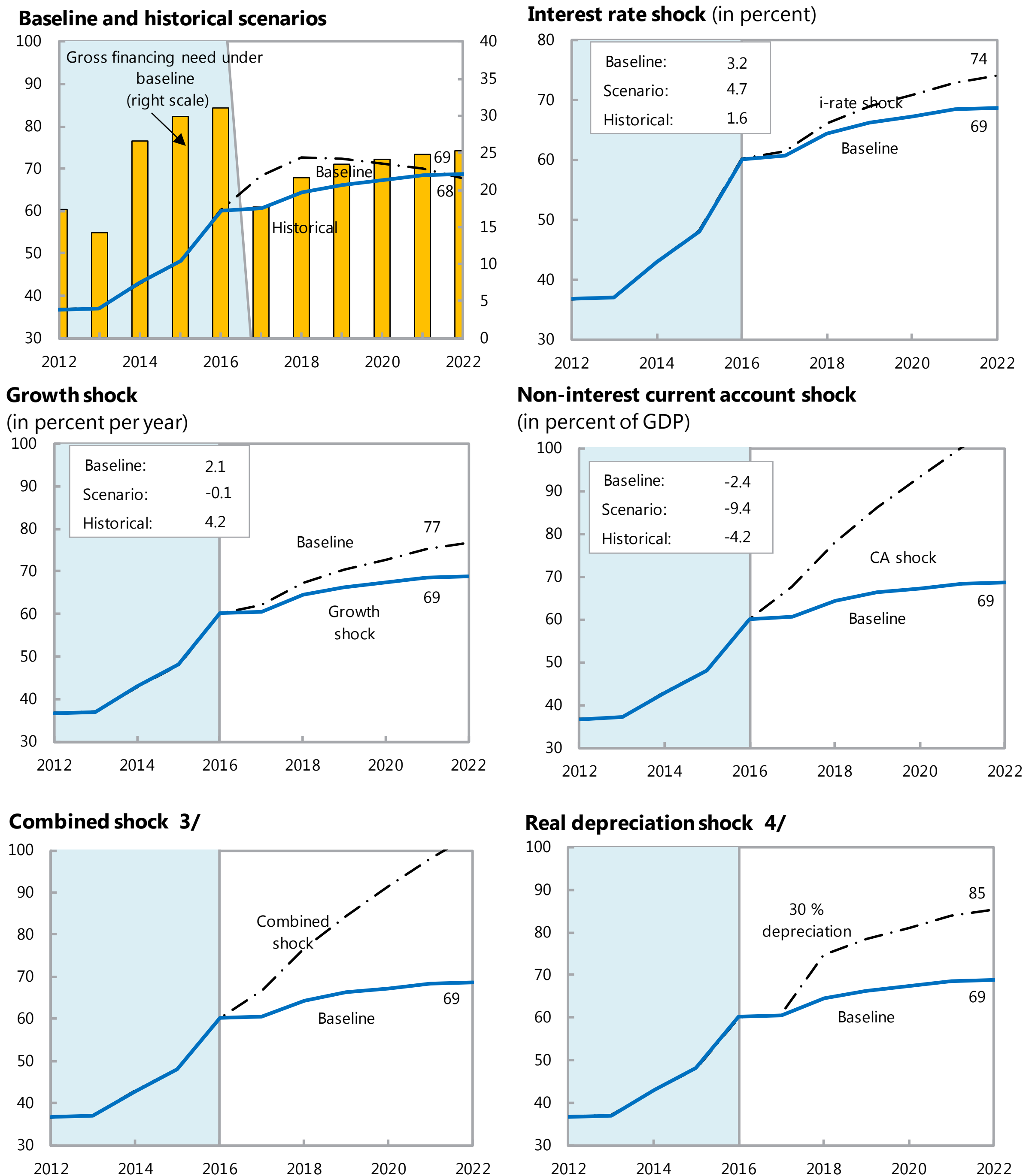
4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure 6. Namibia: External Debt Sustainability: Bound Tests 1/ 2/

(Percent of GDP)



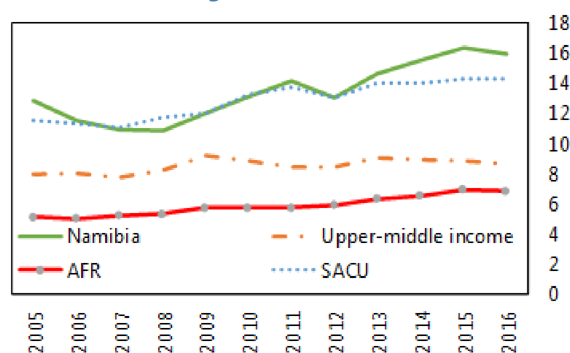
Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 2/3 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2018.

Annex V. Containing Public Wage Bill Dynamics: Policies and Benefits[1]

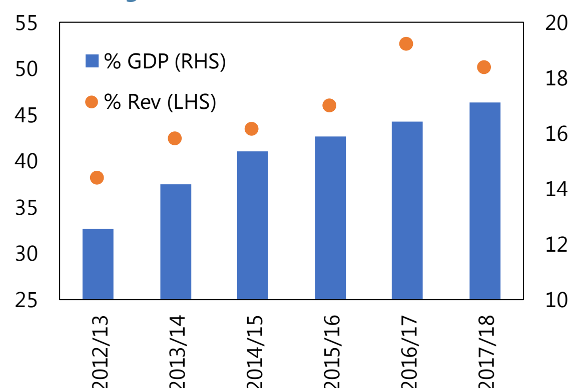
With several countries embarking on fiscal consolidation efforts, the public wage bill has come under increasing scrutiny as it accounts for a substantial portion of total public spending and, over the past decade, has increased in many countries. Evidence shows that SACU countries, and especially Namibia, have some of the highest public wage bills in the world and that public sector salaries are well above those in the private sector. The impact of such wage premium is likely to raise workers' reservation wages, appreciate the real exchange rate, and reduce the economy's ability to absorb foreign shocks. Moreover, except for South Africa, the public sector premium in SACU countries falls along the income distribution, which might exacerbate the brain drain for highly skilled labor.

1. SACU countries have some of the highest public wage bills in the world. Looking at 2016 worldwide data, on average countries spend about 8 percent of GDP on public wages, with European countries being on the higher side and Asian countries on the lower side, and wage costs increasing with countries' income levels.[2] In sub-Saharan Africa, East African countries record the lowest wage bill while Southern African countries, particularly SACU countries, register much higher wage spending (about 14 percent on average). Public wages also absorb a significant share of budget revenue. Countries worldwide spend on average about a 1/3 of their revenues in wages, with the share increasing to 35 percent in sub-Saharan African countries, and further rising to 40 percent in Southern Africa and 45 percent in SACU countries.

Median Public Wage Bill



Public Wage Bill



2. Within SACU and small-middle income countries, Namibia has large and fast-growing public wage costs. In FY 16/17, public wage costs for central government employees reached 16.4 percent of GDP (42 percent of primary spending), almost 5 percentage points of GDP higher than in FY12/13. They absorbed about 55 percent of tax revenue, 10 percentage points of GDP higher than in FY12/13 and 80 percent of its domestic revenue (excluding SACU) on its wage bill. Notwithstanding the already high spending,

[1] Prepared by Jose Torres, based on a forthcoming paper by Meyimdjui, Dieterich and Torres.

[2] The analysis includes data for 168 countries across all regions and income levels.

the public wage spending bill is expected to further increase and reach about 17 percent of GDP in FY17/18.[3]

3. The rapidly rising public wage bill in Namibia is largely the result of fast-increasing public sector salaries. Using government's payroll data, staff estimate that about 2/3 of the increase in the wage bill over the period FY12/13–16/17 reflected wage increases, while new hires only accounted for a third of the increase. More specifically, over the period FY12/13–16/17, on average, government wages increased in real terms by about 7 percent per year, well above the average inflation rate of 5.2 percent, while the number of employees increased by about 4 percent per year. Although the annual increase in real wages seems to be moderating over time, the increase remains extremely high when compared to the limited growth registered over the same period in total factor productivity (TFP) for the whole economy (about 0.5 percent).

Decomposition of the Wage Bill

	Employment		Wage Bill		Inflation	Real Wages
	Workers	Change	N$ million	Change		Change
2012/13	99,152	.	13,925	.	.	.
2013/14	106,607	7.5%	17,932	28.8%	5.9%	13.1%
2014/15	114,188	7.1%	21,655	20.8%	5.2%	7.1%
2015/16	116,723	2.2%	23,961	10.7%	3.4%	4.7%
2016/17	117,605	0.8%	26,738	11.6%	6.5%	4.0%
Cumulative Increase		18.6%		92.0%	22.7%	31.9%
Average annual increase		4.4%		17.7%	5.2%	7.2%

Sources: Ministry of Finance and IMF staff estimates.

4. Yet, the high wage bill does not translate into better public services. The elevated wage bill in Namibia reflects relatively high spending in health and education compared to other middle-high income countries and countries in the region (as a share of GDP). However, the higher spending in these sectors does not always deliver better outcomes. Key health and education outcomes in Namibia (e.g., maternal and child mortality, availability of hospital beds and physicians, pupil-teacher ratio, expected years of schooling) are substantially below the standards prevailing in middle-high income countries, although better than in countries in the region.[4] This suggests that there is room to improve the efficiency of public spending in health and education and make savings, without affecting the quality or access to these services.

[3] Only Lesotho, Zimbabwe, Saudi Arabia and Kuwait have a higher wage bill than Namibia (about 18 percent of GDP).

[4] It is worth noticing however, that the high HIV incidence in SACU countries may partially explain elevated health spending with elevated death rates.

Public Wage Bill, Health and Education Spending, and Outcomes

	Spending			Outcomes			
	Public wage bill (percent of GDP)	Education expenditure (percent of GDP)	Health expenditure (percent of GDP)	Under-five mortality rate (per 1,000 live births)	Maternal mortality rate (per 100,000 live births)	Physicians (per 1,000 people)	Expected years of schooling (for children entering school)
Namibia	16.3	10.2	5.4	46	273	0.4	11.3
High Income	9.9	5.0	5.3	5	9	2.9	15.5
Upper Middle Income	9.0	4.1	3.3	19	49	1.7	13.0
Low Middle Income	6.9	4.1	2.3	44	164	0.5	11.1
Sub-Saharan Africa	6.1	4.1	2.5	93	535	0.1	9.5
Southern Africa 1/	9.3	4.8	3.3	74	398	0.2	11.3

Sources: WB development indicators and Unesco.
1/ Includes: Botswana, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Seychelles, South Africa, Swaziland, Zambia and Zimbabwe.

5. However, rising salaries have led to public sector workers being paid more than similar workers in the private sector, in some cases by a wide margin.[5] Using traditional Mincer equations (see Appendix), staff estimate that in all SACU countries, public workers have a premium compared to private workers with similar characteristics. The estimated premia are about 10 percent in South Africa, to 15 percent in Namibia, 40 percent in Swaziland, and 50 percent in Lesotho and Botswana. It is worth noticing that these premia are lower-bound estimates as they do not account for public workers' greater job stability, and non-cash benefits commonly used in most SACU countries.

Public Wage Premium

	All	Excl. Agriculture	Formal	Urban
Botswana	0.60***	0.57***	0.57***	0.50***
Lesotho	0.64***	0.50***	0.32***	0.55***
Namibia	0.20***	0.19***	-	0.14***
South Africa	0.12***	0.087***	0.051*	0.14***
Swaziland	0.43***	0.40***	0.46***	0.45***

Sources: Household Surveys and IMF staff estimates.

6. Except for South Africa, public sector wage premia are particularly high for low-skilled workers, contributing to possible brain drain in BLNS countries.[6] A typical argument made in the region to justify high salaries is the need to address shortages of doctors and teachers, which force governments to pay higher wages for these professionals to avoid losing them to South Africa (which on average pays higher wages as the country is more developed). To assess the validity of this argument, staff ran quantile regressions of the Mincer equation for each country (see technical note) and the results show quite the contrary. The public premium is very high for low skilled

[5] For country-specific analyses comparing public and private sector salaries, see for example: Smith (1976) and CBO (2017) for the US, Mueller (1998) for Canada, Borland and others (1998) and Mahuteau (2017) for Australia, Depalo and others (2011, 2014) and De Castro, Salto and others (2013) for the EU, Panizza and others (2005) for 13 Latin American countries, and Kerr and others (2015) and Kwenda and others (2015) for South Africa.

[6] BLNS: Botswana, Lesotho, Namibia and Swaziland.

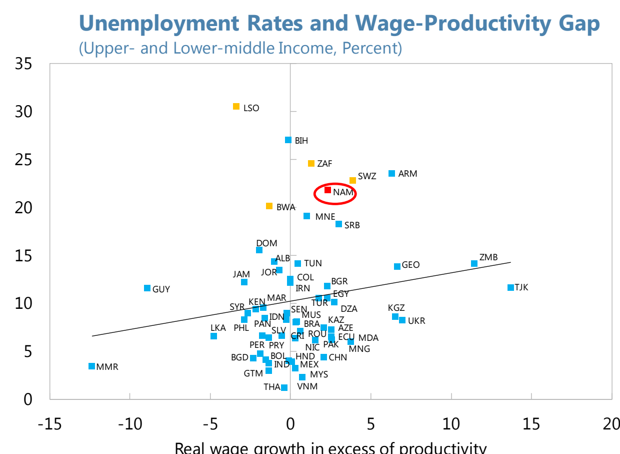
workers and falls along the income distribution. Differently from BLNS, however, in South Africa the premium tends to increase along the income distribution. Taken together these results might explain the scarcity of skilled labor in the BLNS, as these workers might be tempted to work in South Africa where their abilities are better rewarded. (See Technical Note)

Public Wage Premium by Income Quantiles

	q10	q25	q50	q75	q90
Botswana	0.81***	0.78***	0.61***	0.37***	0.36***
Lesotho	n.a.	n.a.	n.a.	n.a.	n.a.
Namibia	0.33***	0.33***	0.24***	0.15***	0.11*
South Africa	0.00	0.11**	0.15***	0.16***	0.16**
Swaziland	0.53***	0.49***	0.50***	0.42**	0.35*

Sources: Household Surveys and IMF staff estimates.

7. Containing the public wage bill is critical for fiscal adjustment and could correct macroeconomic imbalances with positive effects on long-term growth and employment. Empirical evidence for low and middle income countries suggests that wage increases above productivity gains are associated with higher unemployment rates (IMF, 2013). In the case of Namibia, staff's analysis suggests that public sector's wage dynamics, and most likely private sector wage increases, have widely exceeded changes in labor productivity, which tend to be associated with high unemployment. Moreover, empirical evidence for small-middle income countries shows that creating public jobs does not necessarily reduce unemployment and, in some cases, may increase it by creating pressures on the labor market (IMF 2013). Accordingly, controlling Namibia's public wage dynamics would bring wage increases closer to productivity trends, thus potentially boosting long-term growth and reducing unemployment.[7]



8. Reducing the public wage bill and controlling salary dynamics require a combination of short and medium-term measures. Short-term measures are needed to correct the expected increase in the wage bill under current policies and start containing real salary dynamics. However, cross-country experience suggests that short-term measures are not sustainable, and tend to distort

[7] Leigh L. and A. Mansoor, "Africa on the Move: Unlocking the Potential of Small Middle-Income States", IMF, 2013, and Annex VI

wage and employment structures (IMF, 2016).[8] Therefore, more permanent policies are needed to preserve initial gains and contain dynamics over time.

- ***Short-term measures.*** Experience from other countries suggests that several short-term measures are effective in bringing the wage bill under control, including maintaining salary increases below inflation trends and suspending automatic salary increase, e.g., "notch" increases for workers not yet at the highest point-value of their pay grade; introducing temporary hiring rules to reduce public employment (e.g., retirement replacement ratios); and reducing temporary and contractual positions as feasible.

- ***Medium-term measures.*** Over the medium term, there is considerable scope to improve the wage bill management. Specifically, it is important to link pay to some indicator of performance, and align job requirements with compensation while ensuring public and private sector compensation for workers with similar skills is comparable. In addition, strengthening human resource management (e.g., review presence of ghost workers), and improving wage bill controls (e.g., through biometric technologies, enhanced controls for the hiring of low-skilled workers) could deliver long-term savings. Finally, comprehensive organizational and functional reviews of ministries, departments, and agencies can produce tangible savings over the medium term by identifying areas of overlap or duplication.

9. Controlling the wage bill dynamics and real salary dynamics is important not only for fiscal reasons but also for their positive macroeconomic effects. The rapid rise in real wages tends to increase worker's reservation wages, appreciate the real exchange rate and reduce the economy's competitiveness and ability to absorb foreign shocks. For these reasons, the increases in real wages that were observed in the past five years are not sustainable from a macroeconomic point of view and are introducing a whole range of economic distortions. Thus, better linking pay dynamics to productivity and ensuring similar compensation for public and private workers with comparable skills would help bring the economy on a more sustainable development path.

Technical Note: Estimating Public Sector Wage Premia with Mincer Equations

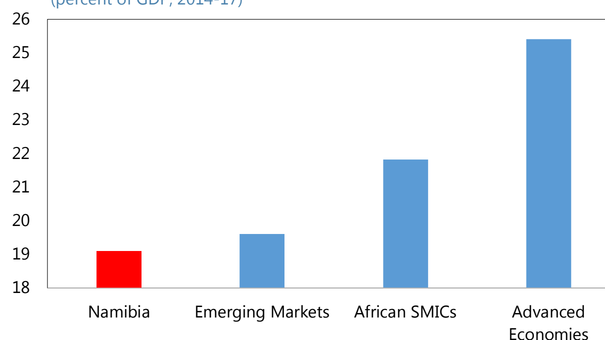
10. Using data from the latest available household surveys for each of the SACU countries (from 2009/10 for all countries), staff estimated traditional Mincer equations. These equations regress the log of the income per capita (as a proxy for individual wages) while controlling for education and age (as a proxy for experience) plus an additional dummy for public sector workers (to estimate the public premium).[9] To assess the robustness of the results, staff repeat the exercise only for workers in the formal sector, in urban areas or excluding the agricultural sector and also using propensity score matching (which reduces the bias from OLS estimates as it improves the comparability across samples).

[8] IMF, "Managing Government Compensation and Employment—Institutions, Policies, and Reform Challenges," June 2016.

[9] As traditional in the literature, staff also include additional controls for region, household size and composition, and number of employed persons in the household.

Annex VI. Mobilizing Tax Revenue in Namibia: Challenges and Reforms[1]

1. Improving domestic revenue mobilization is critical to the government's fiscal adjustment plans and the country's future economic development. The tax revenue-to-GDP ratio in Namibia (29.2 percent in FY16/17) is relatively high compared to peers, but about a third of such revenues are shared receipts from the Southern African Customs Union (SACU). Instead, domestic tax revenues over the last four years only averaged about 19 percent of GDP, somewhat less than the average in emergency market economies and other small middle income African countries. Combined with narrowed tax bases (see below), this signals some room to improve domestic revenue and collection efficiency. In addition to relatively low domestic revenue, the current dependency on volatile SACU revenue exposes the budget to significant shocks. The dependency also poses significant risks as SACU revenues are expected to remain low over the next years as growth in South Africa, the main contributor to the revenue pool, is expected to remain sluggish. Moreover, these revenues will likely decline over the long-term as trade liberalization in the region deepens.



Sources: IMF WEO and IMF staff estimates.
Notes: African SMICs include: Botswana, Swaziland, Lesotho, Mauritius, Cabo Verde, and the Seychelles. Emerging market economies exclude Mexico and Peru.

2. Reforms to broaden the tax base and avoid base erosion would greatly strengthen the efficiency of the Namibia's tax system and improve domestic revenue.

- The tax base could be broadened by eliminating special tax regimes under the corporate tax, removing some VAT zero-rating provisions, and making foreign investment income of Namibian residents taxable. Preferential corporate tax rates and inefficient tax allowances create separated tax regimes with different effective tax rates. The different effective rates can be exploited by shifting taxable profits and deductions across entities to minimize the tax liability. Moreover, the VAT tax base could be broadened by removing some unnecessary zero-rating of certain goods and services (e.g., residential property, residential utilities, fuel products, telecommunications). Finally, many residents have bank accounts and investments abroad that produce income that is currently not taxable in Namibia.

- There is room to curtail a variety of tax base erosion opportunities and strengthen the integrity of the tax system. These include, for example, ring-fencing business losses

[1] Prepared by A. Masters and G. Michielse (FAD).

(i.e. curtailing the possibility to offset losses and profits across different types of businesses); avoiding to treat construction workers as self-employed (rather than employees); eliminating exemptions for real property companies from capital gains taxation; and, finally, introducing earnings stripping rules to limit deductibility of interest expense as currently there is no limit.

3. Despite progress in some areas, there remains significant room to improve key tax administration functions. The most recent assessment of tax administration in Namibia took place in 2016 through the Tax Administration Diagnostic Assessment Tool (TADAT). The TADAT assessment identified a number of weaknesses in basic functions compared to international good practices. These include: inadequate data integrity and an inaccurate taxpayer register—critical to managing return filing, payment and the management of tax arrears; absence of documented processes and procedures; a lack of service delivery standards; and, limited control over taxpayer compliance.

4. Creating and reaping the benefits of a semi-autonomous revenue authority can take time and, in the process, significant operational improvements are needed. The authorities are moving ahead with the creation of a semi-autonomous revenue authority, planned to be operative in 2019. This is a positive step, but it does not eliminate the need for immediate operational improvements. Specifically, in the near term, it is important to develop further the capacity to conduct in-house audits for large taxpayers, design a specific strategy to manage medium-sized taxpayers and introduce a presumptive regime for smaller ones. Authorities should also avoid new tax amnesties on tax arrears that, particularly in the absence of a strong administration, are likely to reduce tax compliance.

Annex VII. FSAP Main Findings and Recommendations

The 2018 Financial Sector Assessment Program (FSAP) assessed risks and vulnerabilities in the financial sector, the strength of the oversight of banks and non-bank financial institutions, the financial stability framework and macroprudential mandate, and crisis management and financial market infrastructure.[1]

Risk and Vulnerabilities

1. **The 2018 FSAP has identified key risks and vulnerabilities in the financial system that need to be managed.** These include high loan and asset concentration, liquidity risks from significant wholesale funding of banks, extensive domestic and external interconnections of financial institutions, and high household indebtedness.

Banking Sector Oversight

2. **The BoN has made significant progress in addressing regulatory and supervisory gaps, but shortfalls remain.** Comprehensive regulatory regimes have been introduced for market risk, country risk, consolidated supervision, and AML/CFT. Risk-based supervision was introduced in 2015 and on-site examination reviews are intensive and challenging. Nevertheless, important shortfalls remain.

- ***Liquidity risk framework.*** Liquidity requirements are not tailored to the specific liquidity needs of individual banks and do not reflect risks posed by sudden outflows of potentially volatile wholesale deposits. Ahead of the introduction in early 2019 of Basel III regulations on liquidity coverage ratios (LCR) and net stable funding ratios (NSFR), the BoN should approve the mismatch limits in the interim and agree with banks on any behavioral adjustments on their short-term cash projections.

- ***Monitoring asset quality.*** The BoN has recently identified possible misclassification issues. Strengthened and better forward-looking assessment of asset quality is needed and indeed underway.

Regulation and Supervision of Non-Bank Financial Institutions

3. **Non-bank supervision while improved is still weak.** Major regulatory gaps exist and supervisory deficiencies are evident at the nonbank supervisor, NAMFISA, and no risk-based supervision is in place yet. These shortcomings also hinder the ability to conduct consolidated supervision of financial conglomerates.

- ***Legislation.*** Several financial sector laws are in the process of being upgraded and would bring the supervisory and regulatory frameworks in line with global norms. They will

[1] The FSAP report (forthcoming) also examined and made recommendations on financial development issues.

introduce a new framework for the supervision of unit trusts, revamp risk-based insurance solvency requirements, improve the governance of pension funds, increase focus on market conduct and adopt risk-based supervision for all sectors.

- ***Supervisory capacity and tools.*** While improved, NAMFISA needs to continue to build its technical competency and relations with industry, as well as its ability to contribute to consolidated supervision, including across borders. Moreover, there is still no risk-based supervision of NBFIs and, for example, existing capital requirements for pension funds and insurers are not risk-based, and stress tests are not used.

Financial Stability Framework and Macroprudential Mandate

4. The financial stability and macroprudential architecture needs to be updated. The Financial System Stability Committee (FSSC), with members from the BoN, MoF and NAMFISA, has no decision-making authority. No institution has an explicit macroprudential mandate. The macroprudential toolkit is limited and only includes so far LTV limits for non-primary house purchases despite elevated household indebtedness and banks' large mortgage exposures.

Crisis Management and Preparedness

5. A formal crisis management and resolution framework is required. The BoN and NAMFISA have not developed recovery and resolution plans for financial groups. Special resolution powers of the BoN and NAMFISA to close and liquidate failing institutions are limited. Fiscal backstop arrangements for resolution, emergency liquidity assistance (ELA) and deposit insurance funding in the event of major crisis should be considered and operationalized. A new deposit insurance scheme should be aligned with international norms

Development, Infrastructure and the Role of the State

6. The financial market infrastructure (FMI) is mostly modern, but new legislation on securities, electronic transactions, payments system and cyber crime should be expedited. Despite its sophisticated financial system, a large share of the poor and rural population is excluded from formal financial services. Inclusion should be promoted through digitization of social transfers and an improved regulatory framework for microfinance institutions. An improved credit information system for MSMEs, a secured transactions framework for movable assets, and a modernized insolvency regime would facilitate financial access. Severe problems at state-owned financial institutions require attention.

Namibia. 2018 FSAP Key Policy Recommendations	
Recommendations	**Timing***
Financial Sector Oversight Framework	
Ensure prompt enactment of the Banking Institutions, BoN, Financial Institutions and Markets (FMI), NAMFISA, Financial Services Adjudicator, Deposit Insurance, and Microlending bills, in-line with international norms.	I
Finalize the Joint Prudential Supervisory Engagement Framework between the BoN and NAMFISA.	
Assign an explicit macroprudential mandate, including the power to issue macroprudential directives to regulators, to the BoN Board until the Financial Stability Council is set up, and address data gaps.	I
Banking Sector Oversight	
Strengthen the existing liquidity regime ahead of implementation of the LCR and NSFR.	I
Enforce the proper classification of loans to ensure that banks identify, monitor and manage their credit risks effectively. Undertake independent asset quality review to determine the scale of under-provisioning across the sector.	I
Non-Bank Financial Institutions and Capital Markets	
Strengthen the accountability and transparency framework of NAMFISA.	NT
Introduce electronic central securities deposit (CSD), repo operations, and reporting of government bond OTC trades.	I
Crisis Preparedness and Management	
Introduce a special resolution regime for banks and nonbanks to ensure effectiveness and consistency with international best practice.	I
Initiate recovery and resolution planning for the four largest banks and their holding companies, in collaboration with SARB.	NT
Establish the Deposit Guarantee Scheme in line with international best practice.	NT
Take steps to operationalize ELA on short notice.	I
Financial Market Infrastructure	
Focus the scope of FMI oversight on systemic risk management and implement the oversight framework with special attention to operational risk and cyber resilience.	I
Development Issues	
Re-assess state-owned financial institutions' mandates and business rationale and restructure Agribank.	I
* I (immediate action) is within one year; NT (near-term action) is within 1–3 years; MT (medium-term action) is within 3–5 years.	

INTERNATIONAL MONETARY FUND

NAMIBIA

February 9, 2018

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By

African Department
(in collaboration with other departments and the World Bank)

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FUND RELATIONS

As of December 31, 2017

Membership Status

Joined: September 25, 1990; Article VIII

General resources account	**SDR (million)**	**Percent of Quota**
Quota	191.10	100.00
Fund holdings of currency	191.03	99.97
Reserve position in Fund	0.08	0.04

SDR Department	**SDR (million)**	**Percent of Quota**
Net cumulative allocation	130.39	100.00
Holdings	4.20	3.22

Outstanding Purchases and Loans None

Financial Arrangements None

Projected Obligations to Fund

(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming			
	2018	2019	2020	2021
Principal				
Charges/Interest	0.93	0.94	0.94	0.94
Total	0.93	0.94	0.94	0.94

Implementation of HIPC Initiative None

Exchange Rate Arrangements. The Namibian dollar is pegged to the South African rand. Namibia accepted the obligations of Article VIII, Section 2, 3, and 4 of the Fund's Article of Agreement, as of September 20, 1996. In December 2015, the Bank of Namibia suspended an agreement with the Bank of Angola on mutual currency conversion in effect since June 2015 (that exchanged Angolan kwanzas or Namibian dollars to US dollars). Namibia maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions.

Article IV Consultation. Namibia is on a standard 12-month consultation cycle. The last Article IV consultation was concluded by the Executive Board on December 2, 2016.

Technical Assistance, 2012–17

Department	**Dates**	**Purpose**
Fiscal Affairs		
Department (FAD)	March 2012	Revenue Administration Tax
	June 2012	Trade Facilitation
	November 2012	Tax Administration
	November 2012	Risk Management Follow Up
	December 2012	Program Budgeting: Cash and Debt Management
	February 2013	Customs Administration
	March 2013	Namibia Excise Legislation
	April 2013	Public Financial Management
	April 2013	Tax Administration
	April 2013	Development of PBB Instruments
	May 2014	Customs Administration
	December 2014	Tax Administration
	January 2015	Diagnostic on Revenue Administration
	February 2015	Legal framework/Program budgeting
	February 2015	PFM Act
	April 2015	Customs Administration
	April 2015	Legal Framework PFM
	June 2015	Tax Administration/Large Taxpayer Unit
	September 2015	PFM
	October 2015	Cash Management
	January 2016	Customs Administration
	April 2016	PFM
	July 2016	IFMIS
	October 2016	Budgeting
	February 2017	Revenue Mobilization
	May 2017	Budgeting
	August 2017	Budgeting
	August 2017	Fiscal Reporting (Chart of Accounts and IFMIS)
	October 2017	Budgeting
	November 2017	Macro-Fiscal forecasting
Monetary and Capital Markets		
Department (MCM)	April 2012	Implementation of Basel II
	April 2012	Supervision of Non-Bank Financial Institutions
	May 2012	Stress Testing
	November 2012	Payment Systems
	November 2012	Monetary Operations
	November 2012	Bank Supervision
	April 2013	Compliance with Basel II
	April 2013	Capital Market Institutions

	April 2013	Strengthening Non-Bank Financial Institutions
	July 2013	Stress Testing
	January 2014	Stress Testing
	September 2014	Basel II
	February 2015	Financial Stability Framework
	April 2015	Basel III
	June 2015	Macroprudential Framework
	April 2016	Basel III
	April 2017	Non-bank Regulation and Supervision
Statistical Department (STA)	May 2012	Quarterly and Annual National Accounts (DFID)
	Nov. 2012	Consumer Price Index
	January 2013	Quarterly National Accounts
	February 2013	Price Statistics
	April 2013	Standardized Reporting Monetary Data
	April 2013	BOP Statistics
	July 2013	Consumer Price Index
	November 2013	National Accounts
	November 2013	Consumer Price Index
	February 2014	National Accounts
	April 2014	Monetary Statistics
	April 2014	Open Data Initiative
	July 2014	National Accounts
	April 2015	Producer Price Index
	April 2015	BOP Statistics
	January 2016	GFS Statistics
	April 2016	e-GDDS
	September 2016	Monetary Statistics
	January 2017	GFS Statistics
	April 2017	Price Statistics
	September 2017	Price Statistics
	November 2017	National Accounts

JOINT WORLD BANK AND IMF WORK PROGRAM

Table 1. Namibia: World Bank and IMF Planned Activities
(as of January 2018)

Title	Products	Provisional Timing of Missions	Expected Delivery Date
A. Mutual information on relevant work programs			
World Bank Work Program	• Regular macroeconomic monitoring	First and third quarters of 2018	Periodic notes and forecasts through 2018
	• Social protection review	March-June 2018	Ongoing
	• TA on weights calibration statistics	January 2018	January 2018
	• WB-IFC-GIF PPP options assessment for Walvis Bay port and Hosea Kutako airport	First quarter of 2018	April 2018
	• Statistical Capacity TA (household survey data collection and analysis)	March 2018	June 2018
	• Poverty update note	March 2018	May 2018
IMF Work Program	• 2018 Article IV consultation	Late 2018	Early 2019
	• Fiscal risks	Early 2018	
	• Medium-term budgeting	Early 2018	
	• Macro-fiscal forecasting	Late 2018	
	• Custom administration	Early 2018	
	• Chart of accounts and IFMIS	Late 2018	
	• Basel III implementation (LCR, NFSR)	Early 2018	
	• Systemic risk and financial stability	Early 2018	
	• National accounts	Early 2018	
	• Producer price index	Early 2018	
	• GFS quality and coverage	Early 2018	
B. Requests for work program inputs			
Fund's request to the Bank	Periodic updates on progress with domestic structural reform agenda, including in the context of NDP5, the Industrial Policy Strategy, social protection reviews, and the Financial Sector Strategy.		
Bank's request to the Fund	Periodic updates on macroeconomic/fiscal developments and policies and Fund analytical and technical assistance reports provided to the authorities.		

STATISTICAL ISSUES

I. Assessment of Data Adequacy for Surveillance
General: Data provision has shortcomings but is broadly adequate for surveillance. The most important shortcomings concern the government finance statistics.
National Accounts: The base year for national accounts (NA) is 2010. Quarterly national accounts (QNA) estimates at constant prices are disseminated on the Namibia Statistics Agency's (NSA) website, though there is a need to improve its source data and coverage. Plans by the NSA to produce QNA estimates in current prices are ongoing. The NSA is assessing the integration of VAT data in the NA compilation framework. The NA are produced bi-annually and revised for the past three years. Major revisions for back years such as correction of errors and changes to the economic structure to reflect current economic situations occur at longer intervals. TA in NA resumed in 2017, and is expected to continue in 2018.
Price Statistics: The consumer price index is based on expenditures derived from the 2009/10 Household Income and Expenditure Survey (HIES) and may not be representative of current expenditure patterns. The NSA should update the CPI weights and item basket using the results of the 2015/16 HIES. Assisted by AFRITAC South, the NSA has compiled a producer price index (PPI) on a pilot basis. It is expected that a quarterly PPI release will be launched during 2018, once the pilot index has been quality assured. Labor market data, including labor force, employment, and wages are only collected on a biennial basis (the latest labor force survey is for 2016).
Government Finance Statistics: The MOF reports annual Government Finance Statistics for the budgetary central government on a cash basis in the GFSM 2001 format with poor timeliness, and a lack of detailed classifications and balance sheet data. Monthly data are also reported; however, reporting inconsistencies and conceptual issues severely affect data reliability. Limited data are available to assess fiscal risks, including from public entities. Work aimed at improving the coverage of annual and higher frequency data is ongoing under a DFID financed project and the next TA mission is tentatively scheduled for April 2018.
Monetary and Financial Statistics (MFs): The Bank of Namibia (BoN) reports monthly monetary statistics based on standardized report forms (SRFs) for the BoN and Other Depository Corporations (banks and money market funds). Concepts and definitions are broadly in line with the Monetary and Financial Statistics Manual. The BoN has started to report Other Financial Corporations (OFCs) data covering pension funds, insurance companies and the Development Bank since December 2017, and data have been published in the International Financial Statistics. However, timeliness needs improvement as OFC data are available only through March 2017. In addition, future work for OFCs should focus on covering asset managers and other remaining OFCs.
Financial Soundness Indicators: The BoN reports Financial Soundness Indicators (FSIs) for deposit takers on a quarterly basis. However, several reporting inconsistencies and conceptual issues affect the reliability of both recent and historical FSIs. FSIs do not cover nonbank financial institutions or other nonfinancial sectors.

Balance of Payment and International Investment Position Statistics: The BoN reports balance of payments (BOP) and international investment position (IIP) data on a quarterly basis with a lag of one quarter. Data is subject to substantial revisions. In July 2017, Namibia submitted quarterly BOP and IIP data on a Balance of Payments and International Investment Position Manual, sixth edition (BPM6) basis for the first time and reviewed the historical series from 1990. There is room to improve the compilation of external sector statistics, particularly to ensure consistency between BOP and IIP data; between IIP and MFSs; and to expand the coverage of the IIP and the financial account of the BOP. Namibia is planning to participate in the Coordinated Direct Investment Survey (CDIS) in 2018.
II. Data Standards and Quality
A ROSC (Data Module) for Namibia was published in 2002 and updated in 2005. In June 2016 Namibia implemented the recommendations of the Enhanced General Data Dissemination System (e-GDDS) by launching a National Summary Data Page (NSDP), which serves as a one-stop publication vehicle for essential macroeconomic and financial data in both human and machine-readable formats. The Namibian authorities have committed to follow the data dissemination schedule as provided in their metadata on the IMF's Data Dissemination Bulletin Board (http://dsbb.imf.org/Pages/GDDS/CtyCtgList.aspx?ctycode=NAM). The authorities are encouraged to make progress through the e-GDDS to higher data standards.
III. Reporting to STA
The MOF regularly reports annual data for publication in the Government Finance Statistics Yearbook. Work for reporting higher frequency data is ongoing. The BoN also regularly reports MFS, BOP and IIP data for publication in the International Financial Statistics (IFS) and the Balance of Payments Yearbook.

Table 1. Namibia: Common Indicators Required for Surveillance
(As of January 23, 2018)

	Date of Latest Observation	Date Received	Frequency of Data [1]	Frequency of Reporting [1]	Frequency of Publication [1]	Memo Items: Data Quality—Methodological Soundness [2]	Memo Items: Data Quality—Accuracy and Reliability [2]
Exchange rates	Dec. 2017	Jan.23 2018	D	D	D		
International reserve assets and liabilities of monetary authorities [3]	Dec. 2018	Jan 2018	M	M	M		
International investment position	Q3/ 2017	Jan. 2018	Q	Q	Q		
Reserve/base money	Nov. 2018	Jan. 2018	M	M	M	O, O, LO, LO	O, LO, O, O, O
Broad money	Nov.2017	Jan. 2018	M	M	M		
Central bank balance sheet	Nov. 2017	Jan. 2018	M	M	M		
Consolidated balance sheet of the banking system	Nov. 2017	Jan. 2018	M	M	M		
Interest rates [4]	1/15/2018	1/15/2018	D	D	D		
Consumer price index	Dec. 2017	Jan. 2018	M	M	M		
Revenue, expenditure, balance, and composition of financing [5]—general government [6]	NA	NA					
Revenue, expenditure and balance—central government	Q3/2017	Jan. 2018	B	B	B		
Composition of financing[4]—central government	Q3/2017	Jan. 2018	Q	Q	Q		
Stocks of central government and central government-guaranteed debt [7]	Mar 2017	Sept 2017	Q	Q	Q		
External current account balance	Q3/2017	Jan. 2018	Q	Q	Q		
Exports and imports of goods	Sep 2017	Dec 2017	Q	Q	Q		
GDP/GNP	Sep 2017	Dec 2017	Q	Q	Q	O, O, O, LO	LNO, LO, LO, LO, O
Gross external debt	Sep 2017	Dec 2017	Q	Q	Q		

[1] Daily (D), weekly (W), monthly (M), quarterly (Q), biannual (B), annually (A), irregular (I), and not available (NA).
[2] Reflects the assessment provided in the data ROSC published in September 2005, and based on the findings of the mission that took place from April 13 to 26, 2005, for the data set corresponding to the variable in each row. The assessment indicates whether international standards concerning (respectively) concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O), largely observed (LO), largely not observed (LNO), not observed (NO), or not available (NA).
[3] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[4] Both market-based and officially determined, including discount, money market, treasury bill, note, and bond rates.
[5] Foreign, domestic banks, and domestic nonbank financing.
[6] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[7] Including currency and maturity composition.

Statement by Mr. Mkwezalamba, Executive Director and
Mr. Sishi, Senior Advisor on Namibia
February 26, 2018

1. On behalf of our Namibian authorities, we thank staff for the constructive discussions during the Article IV Consultation as well as the Financial Sector Assessment Program (FSAP) report. The authorities generally agree with staff's assessment of the economic challenges facing the country and the policy recommendations.

2. In the last decade, Namibia pursued an inclusive growth agenda focused on job creation, infrastructure and skills development and poverty eradication. This strategy resulted in high growth and significant improvements in living standards, which enabled the country to attain upper middle-income status. Nevertheless, the economy continues to exude an under-developed manufacturing sector, slow industrialization, and a sizable informal economy.

3. Since 2016, the economy has faced significant challenges, mainly emanating from exogenous factors and domestic structural impediments. As a member of the Southern African Customs Union (SACU), Namibia has continued to be affected by volatility in SACU revenues. At the same time, low growth performance in key regional export markets have impacted domestic demand. Against this background, the authorities are making determined policy efforts aimed at addressing fiscal and external imbalances, while implementing structural reforms to raise potential growth.

Recent economic developments and outlook

4. Slow regional growth, particularly in Angola and South Africa, coupled with a severe drought and subdued commodity prices, depressed GDP growth from over 5 percent annually in the years following the global financial crisis to 1.1 percent in 2016. The authorities estimate that GDP contracted by about 0.6 percent in 2017, owing to weak performance in the construction, wholesale and retail trade, and the real estate sector. At the same time, the ongoing fiscal consolidation measures weighed negatively on growth. This notwithstanding, the authorities take note of staff's estimate of a 1.2 percent contraction in 2017. They, however, consider that recovery in the mining sector has been underway for some time and that agricultural production rose significantly, and this will partially offset the overall negative trend. Updated projections for the medium-term will be presented during the tabling of the 2018/19 Budget.

5. Regional dynamics have continued to contribute to the complexity of the current adjustment, with declining SACU revenue receipts leading to higher fiscal deficits and a simultaneous widening of the current account deficit in 2016, amplified by weaker export prices and high imports. During 2017, however, the current account balance improved significantly, due to the narrowing of the trade deficit and the temporary rise in SACU revenues. At the same time, the slowing economic activity led to a deceleration in private sector credit extension.

6. Meanwhile, inflation continued to decline due to lower food prices resulting from the recovery in agriculture, and economic slack. As a result, inflation slowed to 5.2 percent in December 2017, compared to 7.8 percent in the comparative period in 2016, and has slowed further to 3.6 percent in January 2018. Given these developments, the Monetary Policy Committee (MPC) of the Bank of Namibia (BON) maintained its policy rate at 6.75 percent in February 2018 to support economic growth and simultaneously safeguard the one-to-one exchange rate between the Namibia Dollar and the South African Rand.

Fiscal policy

7. The deterioration of the fiscal position underscores the need to reduce over-reliance on SACU revenues, and to address inefficiencies in government spending. The authorities have thus taken steps to curb the decline in buffers by focusing on targeted spending cuts, as well as a revenue strategy geared to close leakages and strengthen tax administration. Taken together, these policy actions should deliver a cumulative adjustment of around 6 percent of GDP over the medium term, which is consistent with the recommendations of staff.

8. On the revenue side, the authorities are already implementing several measures, including improving the capacity of the revenue service and the establishment of an independent revenue authority in 2019. The legislation for establishing the revenue authority was enacted in December 2017, paving the way for a smooth transition over 2018. Meanwhile, revenue performance has improved, from around 31 percent of GDP in 2016 to an estimated 34 percent of GDP in 2017.

9. Noting that spending inefficiencies were largely due to poor commitment control, the authorities have created a Central Procurement Board (CPB), which began operations in April 2017. The CPB was established in terms of legislation as an independent body to manage all government procurement and contracting. It is expected to curb the practice of some departments entering into contractual obligations without sufficient funds in their budgets. Further, in January 2018, Cabinet issued directives to all departments to reduce spending on specific items. These measures were augmented by stricter controls on public service recruitment, including through freezing staffing levels in most government departments.

10. The Namibian authorities are firmly committed to a stable level of public debt and consider that the recent increase in the debt ratio is in part due to the sudden deceleration in growth. Nevertheless, they will continue to implement measures to prevent further debt

build-up, including through addressing inefficiencies in spending and revenue management. While the rise in arrears in 2017 was unexpected, the range of measures taken to improve commitment control and spending levels are set to prevent recurrence of arrears of such magnitude in future.

11. Overall, fiscal policy is likely to be less pro-cyclical in the coming years compared to 2017, supported by regional economic recovery, improvements in commodity prices and a rise in global demand. Meanwhile, the authorities recognize inherent risks to measures which are designed to crowd-in private investment, such as private-public partnerships (PPPs) and reliance on the balance sheets of state-owned enterprises (SOEs). They are also committed to publishing a comprehensive fiscal risk statement during the coming budget period.

Monetary Policy and Financial Stability

12. The peg to the South African rand has served Namibia well, and the authorities remain committed to maintaining it. They also continue to seek long-term stability and robustness in the level of international reserves.

13. To curb the high private sector debt, more stringent macro-prudential measures have been implemented. The Credit Agreement Amendment Act, which was passed in June 2016, includes regulations stipulating minimum down-payments and maximum repayment periods for loans extended to finance movable goods such as motor vehicles. In March 2017, the authorities also implemented loan-to-value (LTV) limits for secondary mortgages. A full report on the impact of these measures will be published by the Financial Stability Unit (FSU) of the BON during 2018. Nevertheless, high-frequency data indicates a significant slow-down in bank credit to the private sector, from an annual average of 14.2 percent between 2012 and 2016, to 6.6 percent in 2017.

14. The authorities agree with most of the FSAP recommendations, and some of the measures are already being implemented, including the building of the technical capacity of the Namibia Financial Institutions Supervisory Authority (NAMFISA). They are fully committed to the implementation of a risk-based supervision framework for non-banks. Legislation clarifying the role of NAMFISA has been approved by the Executive and is awaiting completion of the Parliamentary process, together with the accompanying regulations. In this regard, the constitutional and legal authority of the BON will remain unchanged, while a new Financial Stability Council (FSC), chaired by the BON and comprising representatives of NAMFISA and the Ministry of Finance, will be established.

15. The authorities also concur with the FSAP recommendation to assign the overall mandate for financial stability to BON and have included an enabling provision in the BON Amendment Bill, which is awaiting Parliamentary approval. The FSC will be responsible for monitoring the stability of the financial system, including the contagion among financial institutions, asset exposure to capital markets, and Namibia Stock Exchange (NSX) asset price inflation amongst other responsibilities. The FSC will also initiate action to deal with adverse developments having a significant bearing on financial stability.

Structural reforms

16. The authorities are committed to addressing structural challenges, including high unemployment and poor labor absorption rates, inequality, and inadequate infrastructure in rural areas. In the context of the development objectives outlined in the 2016 Harambee Prosperity Plan (HPP), the authorities estimate that a growth rate of around 7 percent is necessary to address poverty and unemployment. Further, the Fifth National Development Plan (NDP5), launched in May 2017, provides details for addressing these challenges over the next five years. It outlines four pillars for sustainable development, namely economic progression, social transformation, environmental sustainability and good governance.

17. In terms of these plans, the authorities are undertaking alternative approaches for achieving their development goals. They consider that fiscal policy has played a critical role in meeting development challenges, but inefficiencies therein need to be addressed, while limiting any harm to medium-term growth prospects. Accordingly, a framework for PPPs is currently being implemented, and the authorities have sought the advice of experts from the Fund to help them create robust institutional frameworks. In this regard, they have stepped up efforts to improve conditions for doing business, including by simplifying company registration, and by investing in more vocational and on-the-job-training programs.

Conclusion

18. There is greater optimism about a gradual economic recovery over the medium-term. Nevertheless, the authorities will continue to be focused on resolving the current macro-economic imbalances, and have taken strong action in this regard, including through tougher fiscal measures, improving the management of financial sector risks, and addressing structural impediments to inclusive growth. Namibia continues to strive to widen economic opportunities by anticipating the demographic transition, including through the empowerment of women, investment in basic and high-level education, and infrastructure development. The analysis, advice and technical assistance provided by the IMF remain integral to the authorities' overall strategy and are highly appreciated.