

**Botswana: 2002 Article IV Consultation—Staff Report; Staff Statement; and Public Information Notice on the Executive Board Discussion**

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 Article IV consultation with Botswana, the following documents have been released and are included in this package:

- the staff report for the 2002 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on **May 22, 2002**, with the officials of Botswana on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on August 12, 2002.** The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- a staff statement of **October 9, 2002** updating information on recent developments.
- a Public Information Notice (PIN) summarizing the **views of the Executive Board as expressed during its October 9, 2002 discussion** of the staff report that concluded the Article IV consultation.

The document(s) listed below have been or will be separately released.

Selected Issues and Statistical Appendix

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

BOTSWANA

**Staff Report for the 2002 Article IV Consultation**

Prepared by the Staff Representatives for  
the 2002 Consultation with Botswana

Approved by José Fajgenbaum and Shigeo Kashiwagi

August 12, 2002

- The 2002 Article IV consultation discussions were held in Gaborone during May 10-22. The mission met with Minister of Finance and Development Planning Baledzi Gaolathe, Bank of Botswana Governor Linah Mohohlo, other officials of the government and the Bank of Botswana, commercial bankers, and representatives of the business community and NGOs. The staff team comprised Mr. Green (head-AFR), Mr. Akatu (AFR), Mr. Ding (TRE), Mr. Mfunwa (AFR), and Mr. Poddar (AFR).
- At the conclusion of the previous Article IV consultation, on March 12, 2001, Directors observed that, while Botswana could readily finance government deficits in the short run, high rates of growth in government spending could be inflationary. Directors expressed concern over the economic and social consequences of HIV/AIDS and welcomed the government's focus on preventing the spread of the disease. They endorsed Botswana's exchange rate peg as a suitable monetary anchor.
- Botswana accepted the obligations of Article VIII, Sections 2(a) and 3 on November 17, 1995. It maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions, except for the multiple currency practice discussed in paragraph 30.
- Botswana's relations with the IMF, including technical assistance, are summarized in Appendix I, and its relations with the World Bank Group in Appendix II. Statistical issues are discussed in Appendix III and in the *Report on the Observance of Standards and Codes—Data Module*, on the IMF web site. The quality and timeliness of data are generally adequate for conducting surveillance, but the timeliness of national account and labor market data could be improved. Accounting periods for national accounts, the government finances, and the balance of payments could be aligned for better policy analysis. International reserve and debt data meet GDDS quality benchmarks and Botswana is preparing to participate in the Fund's General Data Dissemination System (GDDS). Social and demographic indicators can be found in Appendix IV.

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### Executive Summary

- Sound policies and substantial reserves have helped Botswana weather two external shocks in 2001 and the regional food shortage in 2002. Output growth in the nonmining sector, an indicator of the economy's underlying strength, picked up. Consumer price inflation fell to a 20-year low at the end of 2001 but is expected to rise in 2002, owing to sharply higher regional food prices and increases in administered prices. The external current account remains in surplus.
- HIV/AIDS is Botswana's foremost economic and social challenge. The government is tackling the virus head-on through extensive prevention programs, and it intends to provide advanced drug therapies to all those in need. Health spending was increased by 50 percent in 2002/03 (April-March), but the long-term cost implications of HIV/AIDS are unclear.
- Medium-term growth will slow not only because of the plateau in diamond production, but also because of HIV/AIDS. Benefits stemming from structural policies will offset the impact of HIV/AIDS to some extent.
- A fiscal deficit in 2001/02 and another projected for 2002/03 are mainly due to cyclical factors and the rise in health spending. They should not be seen as a deviation from the government's commitment to a sustainable budget. The 2002/03 deficit is to be held to the amount attributable to temporary factors and to HIV/AIDS.
- The staff team recommended that the authorities enhance policy coordination to improve the fiscal-monetary policy mix. A domestic balance measure of the fiscal stance could give a better indication of the government's claim on resources and allow the government to set fiscal policies more in line with inflation objectives. It would also help the Bank of Botswana assess the monetary stance.

Botswana: Selected Financial and Economic Indicators, 1996-2001

	1996	1997	1998	1999	2000	Est. 2001
	(Annual percentage change)					
GDP at constant 1993/94 market prices 1/	5.6	8.1	4.1	8.1	9.2	1.2
Consumer price index (period average)	9.6	8.9	6.5	7.8	8.5	6.6
Broad money	18.8	28.6	39.4	26.3	1.4	31.2
	(In percent of GDP)					
Budget balance (including grants) 2/	8.2	5.0	-6.0	6.3	9.1	-2.4
External current account balance	10.4	13.9	4.1	12.2	10.2	7.4
Gross reserves (months of imports)	33.3	28.8	28.2	31.2	32.6	32.1

1/ July-June.

2/ April-March.

## I. RECENT DEVELOPMENTS

- The cyclical decline in the global diamond market caused GDP growth to slow to near 1¼ percent in 2001/02 (July-June). However, private nonmining output grew by about 6 percent, in line with growth in the past decade.
- Fiscal policy was expansionary in 2001/02. Government spending rose by 16 percent during the year, despite a major decline in revenue. Thus, there was a downward swing of 11.5 percentage points in the government's overall balance.
- Monetary policy is anchored by the pegged exchange rate arrangement. During 2001, the pula appreciated in real effective terms by 6.7 percent. Domestic interest rates have been unchanged since October 2000.
- Botswana has been affected by unusual weather conditions and the regional food shortage. The existing social safety net is helping to alleviate adverse consequences for the poor.

1. **Botswana was buffeted by two external shocks in 2001: weak demand for diamonds and volatility in the South African rand exchange rate against major currencies** (Tables 1 and 2 and Figure 1). Based on preliminary information and projections, output growth slowed in 2001/02 (July-June) to about 1¼ percent from 9¼ percent in the previous year, entirely owing to a cyclical drop in diamond production, which has recently been reversed (Figure 2).<sup>1</sup> Private sector nonmining output, which is perhaps a better gauge of underlying economic activity, expanded by an estimated 6 percent in 2001/02, in line with average growth in the 1990s. Growth in the manufacturing sector weakened in 2001/02, and the rise in nonmining output largely reflected the strength of service industries. Public infrastructure and several new private shopping centers boosted the construction sector, while manufacturing lagged, in part reflecting a 6.7 percent real appreciation of the pula during 2001. The expansion of credit to the private sector, which serves as a proxy for domestic demand, has been strong, especially to households. At the same time, however, increasing real interest rates over the past 18 months have helped to slow credit growth to the business sector and thus dampen business investment. Employment in the formal sector increased by 4 percent during the year ended March 2001, but unemployment is estimated to have been 15 percent. More recent data are not available.

2. **Price developments were generally positive in 2001 and the first half of 2002** (Figure 2). Consumer price inflation declined to under 6 percent at the end of 2001, compared with 8½ percent at the end of 2000, largely because of lower inflation in

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<sup>1</sup> Diamond production was reduced because of a drop in global demand that has since been reversed.

Botswana's trading partners and the modest real effective appreciation of the pula. Inflation was under 6 percent in June 2002, as higher imported food costs were offset by low rates of increase in other imported goods and local services. Government wages were raised by 20 percent in 2001 as a catch up to past inflation, but also to make public service more attractive and thereby address vacancies. The rise boosted household demand and perhaps put upward pressure on private sector wages. Minimum wages were raised by 10 percent.

3. **Botswana's government budget moved into deficit in 2001/02 (April-March)** (Table 3). The deficit, estimated at 2½ percent of GDP, was only the second in nearly 20 years and, as in the preceding occasion, is largely attributed to an unexpected drop in mineral revenue. (Mineral revenue constitutes more than one-half of government income.) At the same time, recurrent spending was increased by P 834 million (3 percent of GDP) in the three supplementary budgets during 2001/02, with about one-third of the rise going to teacher salaries (see above). This rise was mostly offset by lower-than-planned capital spending, and, as a result, total government spending increased by 16 percent in 2001/02, or nearly 10 percent in real terms.

Selected Countries: Fiscal Indicators

	Budget Balance <sup>1/</sup> (percent of GDP)	Expenditure growth <sup>1/</sup> (percent change)	Expenditure <sup>2/</sup> (percent of GDP)
<b>Botswana</b>	<b>2.4</b>	<b>15.2</b>	<b>43.0</b>
Lesotho	-4.0	9.4	44.4
Namibia	-3.4	11.2	38.2
South Africa	-2.3	8.6	26.3
Swaziland	-0.7	16.7	31.5

<sup>1/</sup> Average, 1998-2001

<sup>2/</sup> 2001/02

4. **The Bank of Botswana held interest rates unchanged from October 2000 through June 2002** (Tables 4 and 5). Thus, rates on three-month Bank of Botswana Certificates remained in the 12½ -13 percent range through 2001, while in real terms rates rose to 7 percent at the end of 2001, compared with 4 percent a year before, as inflation moderated. The stock of Bank of Botswana Certificates, the main instrument used to manage liquidity, increased by P 1.4 billion (4¾ percent of GDP) during 2001, as an expansionary fiscal stance and the transfer of public pension assets to private sector managers necessitated the absorption of excess liquidity (see paragraph 25).

5. **Botswana's external current account recorded a surplus of 10¼ percent in 2000** (the last period for which data are available; Table 6). The surplus largely reflected the buoyant global diamond market and diamond exports (which account for approximately 70 percent of Botswana's receipts). The current account is estimated to have been in surplus also in 2001, albeit a considerably smaller one mainly because of lower diamond export

earnings. End-2001 reserves were US\$5.9 billion (32 months of imports), or approximately one year's GDP.

6. **Thirty-nine percent of Botswana's adult population is thought to be infected with HIV.** Demographic projections indicate that, by 2006, the number of AIDS cases could more than double, the number of AIDS deaths reach 45,000 a year, and the working-age population could actually decline. The government's comprehensive response to this tragedy is outlined below.

## II. REPORT ON DISCUSSIONS

7. **Economic diversification is Botswana's overriding policy objective.** Diversification is necessary if Botswana is to reduce unemployment and poverty and adjust to the plateau in diamond production. Thus, discussions with the authorities focused on monetary and fiscal policies to provide a sustainable macroeconomic environment that is conducive to private sector development, specific diversification strategies, structural measures to boost efficiency, especially in government, and Botswana's poverty reduction strategy. They also covered HIV/AIDS, in particular the fiscal implications of the disease, and impediments to growth including HIV/AIDS, shortages of skilled labor, a scarcity of serviced land, and competitiveness.

### A. Economic Prospects

8. **Sound policies have enabled the economy to withstand two external shocks in 2001 and the regional food shortage in 2002.** Output growth is expected to rebound in 2002/03 (July-June), reflecting stable mineral production and strong growth in the private nonmining sectors. The service sectors will account for most economic growth as tourism rebounds, growth in retail sales remains buoyant, and new shopping malls open. The manufacturing sector is expected to grow only modestly and below the ten-year average growth rate because of the adverse effects of the recent real effective appreciation of the pula. Unusual weather patterns and their impact on crops are expected to hold crop production close to last year's level, which was suppressed by drought. Nevertheless, the impact on real GDP growth is minor because crop and cattle production combined represent only 2 percent of Botswana's economy. However, the regional food shortage and buoyant domestic demand are expected to contribute to a rise in consumer price inflation to 6¾ percent by end-2002, somewhat outside the Bank of Botswana's indicated range of 4 to 6 percent. The current account surplus would shrink to 6¾ percent of GDP in 2002, compared with 7½ percent in 2001, owing to relatively flat diamond revenue, lower interest income on reserves, a decline in Southern African Customs Union (SACU) revenue, and higher food imports.

9. **In the medium term, it is unlikely that Botswana will match the 8½ percent average economic growth and surpluses in the external current account and government budget that it has recorded over the past 15 years** (Table 7 and text table). Officials at the Ministry of Finance and Development Planning and the staff team agreed that

real GDP growth would be lower because diamond production—accounting for roughly one-third of the economy—had reached a plateau. Unless a significant new deposit is discovered, this sector would no longer serve as the economy’s engine of growth or sustain rapid external and government revenue growth. The government has been preparing for this structural change for some time through its diversification strategy and prudent macroeconomic policies. Looking ahead, however, it is likely that spending growth in nonhealth areas will be restrained and government budgets will be closer to balance, compared with surpluses in the past. Current projections show a surplus emerging from 2005, reflecting improvements in efficiency and tax administration. These projections are uncertain and will depend heavily on HIV/AIDS spending (paragraph 27). The external current account would correspondingly move from substantial surpluses toward balance.

Medium-Term Scenario, 2000-05  
(Annual percentage change, unless otherwise indicated)

	2000	2001	2002	2003	2004	2005
Real GDP 1/	9.2	1.2	3.8	3.6	3.5	3.4
Private nonmining GDP 1/	3.1	6.0	5.6	5.1	4.9	4.8
Consumer price index	8.5	6.6	6.3	6.2	5.1	4.6
Fiscal balance 2/ 3/	9.1	-2.4	-5.0	-2.8	-2.4	0.9
Current account 3/	10.2	7.4	6.2	2.1	0.9	-0.3

1/ Year beginning July 1.

2/ Year beginning April 1.

3/ Percent of GDP.

10. **The nonmineral economy has become Botswana’s main source of output and employment growth.** Staff projections indicate that output in these sectors would expand by about 5 percent a year in the near term but slow to 4 to 4½ percent in the medium term, as the detrimental impact of HIV/AIDS would be partially offset by productivity gains. Including the mineral sector, real GDP growth would fall to 3½ percent in the medium term. The authorities were more optimistic, however. They suggested that the staff could be overstating the impact of HIV/AIDS, noting that firm evidence of the macroeconomic consequences of this pandemic had yet to be documented and that the current anti-AIDS efforts would restrain new infections and prolong the lives of those infected. Therefore, Botswana’s labor force would be larger than in the staff’s assumptions and domestic saving higher. In addition, the officials envisaged higher private sector investment and greater productivity gains from structural reforms ranging from easing restrictions on foreign labor to financial market development (see section II.E). Preliminary work in preparation for the ninth National Development Plan (NDP-9) suggested an annual real GDP growth rate close to 5½ percent in the medium term.



## B. Monetary and Exchange Rate Policies

11. **Monetary policy is anchored by Botswana's exchange rate peg to a basket comprising the South African rand and the SDR.**<sup>2</sup> The Bank of Botswana also seeks to maintain low inflation, and aims to hold future inflation within an indicated range that is based on average inflation in trading-partner countries.<sup>3</sup> As noted above, the current range is 4 to 6 percent.

12. **The pegged-basket framework has been under strain, but it remains appropriate for determining the value of the pula.** During 2001, implementation of the basket was complicated by the approximate 40 percent depreciation of the South African rand against the SDR. The mission observed that the pula's appreciation in effective terms and bilateral appreciation against the rand since 2000 had put nontraditional exporters at a disadvantage and had reduced one element of Botswana's attractiveness to foreign investors, compared with countries in the rand area. At the same time, the staff team recognized that an attempt to correct this loss in competitiveness through a nominal depreciation during the volatility in exchange markets in late 2001 and early 2002 might have been seen as a return to what appears to have been a rand-targeting policy in the past. A depreciation could have undermined public perceptions of policy stability and the gains made in breaking expectations of nominal depreciations to offset domestic inflation above that in trading partners. In the event, exchange rate developments in the first half of 2002 partially restored Botswana's competitiveness within the rand area as the rand recovered considerably against the SDR.

13. **Nevertheless, under Botswana's policy framework, cost containment will be necessary to reverse the competitiveness lost since mid-2000.** The authorities and staff agreed on the need for producers to seek productivity gains and for workers to moderate their wage demands, as demonstrated by the lackluster performance of Botswana's manufacturing sector over the past years. The mission team suggested that cautious monetary and fiscal policies can contribute to this objective and that wage restraint in the public sector would

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<sup>2</sup> The currency weights are undisclosed, but most analysts assume they correspond to Botswana's nondiamond trade shares for South Africa (approximately 70 percent) and the advanced economies (approximately 30 percent, represented by the SDR). The weights can vary with changes in the rand-SDR exchange rate because the basket formula is additive (similar to that for the SDR).

<sup>3</sup> The Bank of Botswana is currently able to target two variables, the exchange rate and future inflation, with one instrument because Botswana's financial market is not sufficiently developed to allow investors to take positions with respect to the currency or domestic assets. The 2000 Article IV consultation indicated that the ability to pursue an independent interest rate policy under the pegged exchange rate would decline as capital markets developed. See SM/01/67.

also need to play a role in containing inflationary pressure because in the past government wage developments tended to lead private sector wages. Business representatives confirmed this linkage but noted that it was not as strong as in the past. The mission encouraged the authorities to watch for signs of improving competitiveness, for example by monitoring the nonmineral trade balance, foreign investment inflows, and wage costs when assessing the adequacy of the exchange rate.

14. **Current real interest rates are high.** Bank of Botswana officials explained that, in pursuing the inflation objective, they monitored two intermediate targets, private sector credit and government spending. Rapid growth in these measures at the end of 2001, and also in disposable income, was seen as an indicator of incipient demand pressure, and, therefore, it was judged unwise to ease monetary policy. The situation was largely unchanged at the time of the consultation discussions, although there had been some indirect signs that demand pressures were abating. In particular, business representatives told the staff team that borrowing costs had curtailed investment, but households had not done so to the same extent because of recent income gains. Nevertheless, the mission concurred with the Bank of Botswana's analysis and felt that a reduction in rates was not appropriate at the time of the discussions. It recommended that the central bank wait for signals of easing inflation pressure before considering a relaxation of monetary policy.

### C. Fiscal Policy

15. **Botswana's fiscal policy is anchored by the National Development Plan (NDP) and the overarching principle of sustainability.** To achieve budget sustainability, Botswana has restricted the use of mineral revenue to development spending, including all spending on health and education, and has relied on nonmineral revenue sources for recurrent spending. In consequence, Botswana's government budget has typically been in surplus, except when influenced by special circumstances, such as a cyclical drop in the global diamond market. Thus, Botswana has accumulated considerable reserves that have allowed the government to weather temporary deficits, while building physical infrastructure and strengthening education and health services. In the period ahead, the accumulated financial resources will help the country adjust to the new diamond plateau environment and pay for part of the HIV/AIDS prevention and treatment programs.

16. **The 2002/03 budget projects a deficit of 4¼ percent of GDP.** Ministry of Finance and Development Planning officials explained that this projection reflected temporary factors including continued weakness in the diamond market and completion of the investment projects in NDP-8. They also noted that provisions for health spending had been increased by 50 percent owing to HIV/AIDS and related illnesses. They stressed that the deficit in no way represented a decision to jettison the sustainability principle and that future budgets would be balanced. In the staff's view, the 2002/03 deficit would be justified only to the extent that it reflected temporary developments and spending on HIV/AIDS. The mission observed that the 2002/03 deficit could be slightly larger than budgeted (5 percent of GDP versus

4-8 percent) because diamond revenue in pula terms would run below initial estimates.<sup>4</sup> Accordingly, the staff suggested that the increase in capital spending be contained to keep the deficit from significantly exceeding the budget estimate. Ministry officials indicated that capital spending would likely fall below budgeted levels because of capacity limitations.

17. **Botswana is working hard to improve tax administration in order to strengthen medium-term budget sustainability.** Mineral revenue now accounts for about one-half of total government income, and stronger tax administration is expected to boost revenue from domestic sources as mineral revenue begins to decline as a share of GDP. Thus, the staff welcomed the new value-added tax (VAT) that replaced the domestic sales tax on July 1, 2002, observing that the associated near-term uncertainty in revenue projections for 2002/03 was outweighed by prospects for efficiency gains in the future. Ministry of Finance and Development Planning officials indicated that they would monitor VAT implementation carefully and address problems as soon as they developed. They signaled their interest in establishing a revenue authority as a further means of bolstering domestic tax collections.

18. **Government spending accounted for 43 percent of GDP in 2001/02, one of the highest ratios in the region, and it is budgeted to rise to over 50 percent of GDP in 2002/03.** This increase represents growth in current and capital spending of 21 percent and 40 percent, respectively. Ministry of Finance and Development Planning officials indicated that they were striving to hold down spending increases, in particular through public sector reform and the NDP process. The staff team welcomed these efforts as the best way to contain costs in a sustainable way. It also welcomed the stated intention to adjust government salaries for inflation yearly and thereby reduce the likelihood of less frequent, but large, adjustments, as these had caused inflationary pressure in the past. The staff team recommended that supplementary budgets be used for emergency situations only. The officials agreed in principle with the recommendation, and pointed out that this was, in fact, government policy.

#### **D. Policy Coordination**

19. **The current mix of fiscal and monetary policies appears to be impeding private sector investment.** The mission expressed concern that increases in government spending and the resulting high interest rates were crowding out private spending, particularly business investment. As noted above, government spending growth is one of the main indicators used by the Bank of Botswana in determining monetary policy and was a factor behind the current level of interest rates. Private sector representatives indicated that their borrowing costs were very high and were beginning to curtail business investment. The staff saw this evidence as supporting the crowding-out hypothesis and thus an important argument for containing

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<sup>4</sup> After the budget projections were finalized in early January, the pula appreciated against the U.S. dollar. As a result, mineral revenue in pula terms could fall below budget assumptions by as much as P 1 billion (3 percent of GDP) in 2002/03.

growth in government spending. Ministry of Finance and Development Planning officials observed that the government's policy was to promote the private sector and economic diversification, and that there was no firm evidence linking government spending to crowding out of the private sector in Botswana. Nevertheless, they were committed to a sustainable fiscal path—a course of action that would entail bringing down the growth of government spending.

20. **The staff team suggested that better coordination of monetary and fiscal policies would facilitate private sector development.** It agreed with the authorities that a better understanding of the link between government spending and crowding out could improve the policy mix. One possibility would be for the Ministry of Finance and Development Planning to develop a domestic balance measure of fiscal policy jointly with the Bank of Botswana.<sup>5</sup> Other countries, particularly those with high incomes from natural resources, use domestic balance measures to judge the impact of government spending and domestic taxes on local resources and inflation. In Botswana, the Ministry of Finance and Development Planning could use it when formulating the budget as an indicator of the direction of interest rates needed to achieve the inflation objective for a given budget. In turn, the same measure could be used by the central bank in its monitoring of the economy and inflationary pressure. The authorities indicated that they would consider the suggestion.

#### **E. Structural Issues**

21. **Implementing structural reforms aimed at improving productivity and lowering costs is an important way Botswana can boost competitiveness and achieve its diversification objective.** The mission commended the authorities on their market-based approach to diversification that focuses on providing an environment for development—including the removal of obstacles and constraints on the private sector—rather than targeting specific sectors. Thus, discussions in this area covered labor market issues, public sector reform, and financial market development.

22. **Despite Botswana's admirable education record, shortages of skilled workers have been impeding economic growth.** Foreign workers have been used to fill in skill gaps, but these workers have sometimes faced difficulties in securing work and residency permits. To address these problems, the government opened a one-stop permit center as a means of smoothing the application process. The staff welcomed this initiative and suggested that a further easing of restrictions on foreign workers, as was done for the International Financial Services Center, would be a desirable next step. The authorities indicated that such actions could be considered but that creating job opportunities for Botswana citizens would remain a high priority.

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<sup>5</sup> A domestic balance indicator for Botswana could exclude mineral revenue, income on external reserves, and government purchases of imported goods and services.

23. **The government has made significant progress in its public sector reform efforts.** Noteworthy accomplishments include a new performance management system, reorganization of some ministries, and formation of a privatization agency, that will work to restructure and privatize public enterprises when desirable.<sup>6</sup> The staff welcomed these initiatives as part of the government's overall strategy to promote private sector development. In addition, the mission welcomed plans to make more serviced land available for use by the private sector, and to address the housing shortage by continuing to sell the Botswana Housing Corporation's stock of structures. The staff team observed that the government could also look for other ways to reduce its presence in the economy, for example by turning over to the private sector some of the development projects anticipated under NDP-9.

24. **The staff commended the authorities for their emphasis on maintaining a sound financial sector and their interest in improving financial services available to investors and business.** At the time of the discussions, Botswana's commercial banks exceeded international capital adequacy standards and local liquidity requirements. Supervisors at the central bank indicated that they had already put in place procedures to guard against money laundering and an IMF technical assistance team would visit Botswana in August 2002 to review their procedures. Officials at the Ministry of Finance and Development Planning reported that nonbank financial institutions were being monitored on an ongoing basis, and they agreed with the staff representatives that more could be done in this area. Minister Gaolathe indicated that he would consider revisiting the priority assigned to a review of supervision, and he agreed that the rapid growth in the financial industry in recent years and last year's privatization of government employee pensions had increased demands on the current setup.

25. **The contributory pension system for government officers has affected Botswana's financial market.** By the end of the 2001/02 financial year, P 2.6 billion had been transferred from government deposits at the central bank to pension managers, and the 2002/03 budget provides for an additional P 5 billion through a below-the-line transaction. These are mostly for benefits accrued under the old system. The mission observed that the transfer of funds to the private sector could be causing asset price inflation, as evidenced by the approximate 65 percent rise in Botswana's equity index in 2001. It expressed its concern that pension managers were required to invest at least 30 percent of the funds locally, as this could distort investment decisions and contribute to asset price inflation. Ministry of Finance and Development Planning officials stressed that they were following the situation carefully, and that the 30 percent minimum local asset requirement was not binding at the time of the discussions. They added that the government was looking into the possibility of creating a pula-denominated government bond to absorb pension assets as well as to promote longer-term private sector financing. The staff team welcomed these proposals, and recommended

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<sup>6</sup> Privatization of Air Botswana was put on hold owing to conditions in the global air industry.

that the government consider a temporary suspension of the 30 percent local investment ratio for a transition period, particularly during the P 5 billion transfer.

26. **International perceptions of Botswana's financial strength and commitment to sound policies were bolstered when it received investment-grade sovereign debt ratings.** These ratings should help to attract direct investment and the expertise that often comes with it. The staff team observed that the authorities could further improve perceptions by making information on fiscal policies and the budget more easily accessible to the public. The annual budget speech, the semiannual monetary policy statements, and various websites all helped investors keep current on economic and policy developments. Nevertheless, publication of additional information, such as three-year macroeconomic projections and revisions to the budget outlook when supplementary budgets were presented to parliament, could facilitate monitoring by the public. There would be little added cost since much of this information was already available within the Ministry of Finance and Development Planning.

#### F. Other Issues

27. **Botswana's comprehensive approach to HIV/AIDS and its progress in implementing it is encouraging (Box 1).** At the time of the last consultation discussions in December 2000, prevention programs were being strengthened and treatment cost estimates were ten times the current figures. Since then, education and prevention programs have been put in place or expanded, and the government has begun a pilot program to treat all patients in need with advanced antiretroviral (ARV) medication. Officials explained that it was too early to evaluate the effectiveness of the various initiatives in preventing new infections and prolonging life. For example, recent survey evidence seemed to suggest that younger age groups are changing their behavior to avoid infection more than older groups. It was also too early to estimate the future budgetary implications of HIV/AIDS with any degree of accuracy but expenses could reach 4¼ percent of GDP by 2006. Unknowns include how many patients will seek treatment, how effective the treatment will be in prolonging life, and the extent to which other medical costs such as those associated with opportunistic infections will be reduced.

28. **Poverty alleviation has been a long-running objective in Botswana but any success over the past ten years has not been documented.** The most recent figures—47 percent of individuals were below the poverty line in 1994—are certainly out of date. Since that survey, real per capita income has increased by more than 28 percent, and poverty alleviation programs, including a destitute allowance and drought relief, have been implemented (Figure 3). Looking ahead, at the time of the consultation discussions, an agricultural development plan had been presented to parliament, and a draft poverty reduction strategy was being evaluated. This plan is a cornerstone of Botswana's poverty reduction initiative because it was believed that poverty mainly exists in the rural, agricultural areas. The authorities indicated that existing programs, such as drought relief, would mitigate the impact on the poor of the unusual weather conditions in 2001/02 and the regional food situation. They did not see a need for supplementary funding because crop produce would be close to that of the previous year.

### Box 1. Fiscal Implications of HIV/AIDS

The direct costs to the government of HIV/AIDS are difficult to estimate, given the uncertainties about the effectiveness of prevention programs, the number of people who will need treatment, and the effectiveness of the treatment itself. Even more difficult to estimate are indirect costs that would be borne by both the government and the private sector.

#### Direct costs

Botswana has put in place a comprehensive HIV/AIDS program (see table below). The 2002/03 budget provides P 326 million (about 1 percent of GDP) for identified HIV/AIDS spending. Prevention programs are the largest budgeted expenditure followed, tragically, by orphan care. Total spending on HIV/AIDS is higher since some programs, such as support to the destitute, benefit AIDS victims but are not captured in the tabulation total.

HIV/AIDS Programs in 2002/03 Budget  
(Millions of pula)

Program	Amount
Antiretroviral therapy (ARV)	28.5
Infrastructure for ARV	47.3
Prevention and education	124.9
Home-based care	34.9
Orphan care	90.8
Total	326.4

Over the medium term, provision of ARV medication is likely to rise sharply. It is possible that by 2006 there will be between 90,000 and 180,000 patients receiving ARV medication. The actual number will depend on how quickly the program can be expanded and the extent to which individuals come forward for testing and treatment. Assuming the current P 7,200 annual cost of treatment prevails over this period, total costs could reach P 1.4 billion, or 4¼ percent of GDP. This estimate is within reach of Botswana's ability to finance treatment, in part because of international support for bringing down the cost of medication. To the extent that treatment proves effective, Botswana could gain from lower costs of treating related illnesses, such as tuberculosis, and indirect costs such as workers staying in the labor force.

#### Indirect costs

On the expenditure side, the government is likely to face high wage rates, especially for skilled health workers. Death benefits and funeral expenses for government employees will also rise. Botswana's revenue base is more sustainable than most African countries, as most of the revenue is generated from the capital-intensive mineral sector, which should be less affected by AIDS than other sectors. However, earnings on international reserves are likely to fall as government deposits are used to finance HIV/AIDS costs. Finally, taxes will shrink as companies' costs rise, and as individuals fall sick and exit the labor market.

29. **Botswana is a member of the Southern African Customs Union (SACU) and, therefore, does not have a fully independent trade policy.**<sup>7</sup> Until very recently, SACU tariff schedules were set almost entirely by South Africa. Under this arrangement, average tariffs fell from around 30 percent in 1990 to 7 percent presently, in part because of free trade arrangements with the European Union and the Southern African Development Community. However, a new SACU agreement gives some decision-making power to a regional tariff board, on which the smaller member countries will be represented. This body will lead future trade reform. The agreement also changes the formula for revenue sharing among the countries to give more resources to the poorer countries. SACU revenue to Botswana is expected to fall as a share of income, reflecting not only the effect of Botswana's high per capita income on the formula, but also reductions in the common external tariff rates and preferential agreements, such as a free trade area with the European Union. However, revenue from excise taxes, also collected jointly, is expected to rise.

30. **Botswana has a multiple currency practice that stems from the Foreign Exchange Risk-Sharing Scheme, which was abandoned in 1990.** The authorities indicated their intention to eliminate the practice by 2006, when the last arrangements under the scheme would expire.

### III. STAFF APPRAISAL

31. **Botswana was buffeted by two external shocks in 2001, and then hit by adverse weather conditions and the regional food shortage in 2002.** Real GDP growth is estimated to have fallen to close to 1¼ percent in 2001/02 from over 9 percent a year earlier, and the external current account surplus to have narrowed considerably; both outcomes are almost entirely due to a temporary decline in the global diamond market. The near 40 percent depreciation of the South African rand in 2001 contributed to a weakening in Botswana's competitive position and dampened growth in the manufacturing sector. This weakening was partially reversed in the first half of 2002 as the rand recovered from low levels against major currencies. The unusual weather conditions in the 2001/02 crop year will have little impact on total output because of this sector's small size, although the regional food shortage contributed to a sharp rise in inflation in early 2002. Safety net programs already in place will limit the impact of the food shortage on the rural population.

32. **Substantial financial resources and an appropriately tight monetary stance helped Botswana weather these adverse external conditions in 2001/02.** Nevertheless, the authorities face many challenges, including the fight against HIV/AIDS, poverty alleviation, achieving a better mix of fiscal and monetary policies, and promoting economic growth as diamond production and revenue reach a plateau. The authorities have demonstrated their

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<sup>7</sup> Botswana has implemented the reporting system that is required to track exports under AGOA. At the time of the consultations, five firms were approved under the program.



commitment in all of these areas, and the staff team is confident that they will implement the chosen strategies well.

33. **In the near term, output growth is expected to recover to about 3¼ percent, well below the 8½ percent average rate of growth over the past ten years.** The slowdown is largely due to the plateau in Botswana's diamond production. The nonmining economy, which is perhaps a better indicator of the economy's underlying strength than overall real GDP, is expected to expand by 5 percent a year in the next few years, close to its historical performance. Despite a tight monetary policy, inflation would pick up in the short term, because of the regional food situation, high world oil prices, and increases in administered local prices. The external current account surplus would diminish because of stagnant diamond exports and continued strong import demand.

34. **HIV/AIDS is expected to lower medium-term growth in the nonmining sector by up to 1½ percentage points a year.** Estimates place the infection rate as high as 39 percent of the adult population, although some studies point to an infection rate closer to 25 percent. In either case, the pandemic is a human tragedy of unimaginable proportion, with potentially far-reaching economic consequences. This impact, however, will depend on the true underlying infection rate and the effectiveness of prevention and treatment programs being undertaken, and will be offset to some extent by anticipated gains in productivity and investment stemming from structural policies and financial market development.

35. **Botswana is facing the daunting medium-term challenge of HIV/AIDS head-on.** The government is to be commended for its enlightened approach to the crisis. It has adopted a coordinated response that aims to prevent further infection through education and treatment of pregnant women, provides palliative care, and eventually will treat all patients with advanced antiretroviral drugs. From a cost perspective, the health budget was increased by 50 percent in 2002/03. However, the medium-term fiscal implications are highly uncertain; future spending on HIV/AIDS will depend on the effectiveness of prevention efforts, the number of patients seeking treatment, and potential reductions in expenses related to opportunistic infections.

36. **Budget deficits in 2001/02 and 2002/03 are unusual.** To a large extent, they reflect a drop in diamond sales that has been largely reversed. The 2002/03 budgeted deficit, however, also reflects rising healthcare costs that are very likely to continue for the foreseeable future. While these deficits are easily financed, Botswana is likely to face difficult spending decisions in the future as HIV/AIDS demands rise and diamond revenue growth slows. NDP-9 is the appropriate planning tool with which to make these choices.

37. **The Bank of Botswana has held interest rates unchanged since mid-2000 despite declines in domestic inflation.** This tight monetary stance has been necessitated by demand and inflationary pressures. However, the policy appears to be slowing business investment disproportionately more than household demand and is, therefore, working against Botswana's medium-term diversification objective. An easing of monetary policy would help, but only when demand conditions permit. Such an easing would be facilitated by a

better balance between monetary and fiscal policies. Over the past few years, the monetary policy has been kept tight to offset the impact of high growth in government spending. The staff agrees with the Bank of Botswana that rapid increases in government spending are an indicator of incipient inflationary pressure, even though the resulting budgets have not been a problem from a deficit or financing point of view. To better assess the necessary policy setting, the staff recommends that the authorities develop and adopt a domestic balance measure of the fiscal stance.

38. **Botswana's exchange rate arrangement and inflation objective form an appropriate framework for financial stability.** During 2001 and early 2002, the mechanism was tested by large fluctuations of the South African rand against major currencies that led to significant swings in the pula-rand and pula-SDR exchange rates, with the net effect of an erosion in competitiveness. A nominal depreciation could have restored this loss, but it would have also reversed gains in the system's credibility achieved over the past 18 to 24 months. It will be important, however, for the authorities to monitor the competitive position closely, while pursuing the envisaged structural reforms.

39. **The authorities are to be commended for their attention to structural policies.** These policies are aimed at providing an environment in which the private sector can take over as Botswana's engine of growth. Recent achievements include addressing shortages of skilled labor by easing the permit process, making more serviced land available for private development, and taking steps to strengthen government efficiency. These achievements will be reinforced by the recently updated privatization policy and the agency set up to implement it. Banking supervision is well in hand, but rapid growth in the nonbank financial sector suggests that supervision arrangements in this area need to be reviewed on a priority basis. The staff welcomes the authorities' careful monitoring of asset price increases following the privatization of government employee pensions, and recommends that the domestic investment requirement be lowered if a shortage of viable investment opportunities develops.

40. **Data are generally adequate, but long reporting lags, especially in the national accounts, balance of payments, and some fiscal data, are a problem that hampers the assessment of macroeconomic conditions.** In addition, different reporting periods are used for data for the major sectors, further complicating economic analysis. The staff welcomes the recent efforts to strengthen data such as participation in the Fund's General Data Dissemination System (GDDS), and urges the authorities to move forcefully ahead to complete that process in order to address comprehensively deficiencies in their statistical system.

41. **The staff notes the authorities' intention to eliminate by 2006 the multiple currency practice** arising out of the Foreign Exchange Risk-Sharing Scheme, which was abandoned in 1990. It therefore recommends temporary approval of the multiple currency practice until October 30, 2003, or the conclusion of the next Article IV consultation with Botswana, whichever is earlier.

42. **It is recommended that Botswana remain on the 12-month consultation cycle.**

Table 1. Botswana: Selected Economic and Financial Indicators, 1998-2003

	1998	1999	2000	2001	2002	2003
				Est.	Proj.	
(Annual percentage change, unless otherwise indicated)						
National income and prices						
Real GDP 1/	4.1	8.1	9.2	4.7	3.2	3.0
GDP deflator 1/	2.5	9.0	6.0	6.4	6.4	6.5
Consumer prices (average)	6.5	7.8	8.5	6.6	5.0	5.0
Consumer prices (e-o-p)	6.4	8.4	8.5	5.8	4.8	4.8
Nominal GDP (in billions of pula) 1/	21.5	25.4	29.4	32.7	35.9	39.4
Diamond production (in millions of carats)	19.7	21.3	24.6	25.9	25.2	26.0
External sector						
Exports of goods, f.o.b. (in U.S. dollar terms)	-26.3	28.4	0.8	-27.3	2.5	0.7
Of which: diamonds	-31.9	45.5	0.2	-34.2	3.1	3.8
Imports of goods, f.o.b. (in U.S. dollar terms)	3.9	-6.0	-5.2	-23.9	3.9	1.0
Terms of trade	5.6	10.2	-2.8	-2.4	-1.7	-1.5
Nominal effective exchange rate (depreciation -) 2/	-2.2	0.1	1.6	4.6 ...	...	...
Real effective exchange rate (depreciation -) 2/	-0.9	6.0	3.8	6.7 ...	...	...
Nominal average exchange rate (pula per U.S. dollar), avg	0.2	4.6	5.1	6.9 ...	...	...
Nominal average exchange rate (pula per U.S. dollar), eop	0.2	4.6	5.4	7.0 ...	...	...
(Twelve-month percentage change, unless otherwise indicated)						
Money and banking						
Net foreign assets	24.3	8.3	16.8	22.7	-12.5	-12.1
Net domestic assets	20.9	3.6	21.7	20.4	-19.1	-20.7
Net domestic credit	19.5	-0.3	20.2	16.5	2.3	-3.8
Net claims on government	23.9	6.1	19.7	15.3	-1.8	-2.9
Claims on nongovernment	-46.6	-35.5	-22.5	-11.4	-22.1	2.2
Other items (net)	25.1	14.5	25.5	29.6	-63.5	-118.5
Money and quasi money (M2)	39.4	26.3	1.4	31.2	10.6	9.7
Broad money (M3) 4/	34.5	28.9	-1.1	27.6	8.0	8.7
Velocity (GDP relative to M2)	3.6	3.2	3.7	3.2	3.2	3.2
(In percent)						
Interest and credit 5/						
Bank of Botswana lending rate	12.5	13.3	14.3	14.3 ...	...	...
Commercial banks						
Prime lending rate	14.0	14.8	15.8	15.8 ...	...	...
Deposit rate	8.8	9.7	10.2	10.2 ...	...	...
(In percent of GDP, unless otherwise indicated)						
Investment and savings 1/						
Gross investment	33.5	31.2	29.6	32.3	31.7	30.0
Public	14.5	13.4	13.0	14.2	13.9	13.1
Private	19.1	17.8	16.6	18.2	17.8	16.9
Gross national savings	43.6	38.9	39.6	40.3	37.5	33.9
Public	15.3	11.4	13.9	17.0	13.4	10.3
Private	28.3	27.5	25.7	23.4	24.2	23.6
Central government finance 3/						
Total revenue and grants	36.2	49.0	49.8	41.9	43.9	43.1
Total expenditure and net lending	42.8	42.7	40.7	42.2	45.6	45.3
Current expenditure	29.6	28.9	29.6	30.2	33.2	33.1
Capital expenditure	13.9	14.1	11.1	11.8	11.8	11.8
Net lending	-0.6	-0.3	0.1	0.2	0.6	0.4
Overall balance (including grants)	-6.6	6.3	9.1	-0.3	-1.7	-2.2
Primary balance	-6.1	6.7	9.4	0.1	-1.4	-2.9
Domestic financing	6.4	-6.1	-8.5	-0.3	1.1	2.5
Foreign financing	0.1	-0.1	-0.6	0.6	0.5	-0.2
External sector						
External current account balance (deficit -)	4.1	12.2	10.2	8.2	5.9	3.6
External debt in percent of GDP 6/	9.4	10.3	8.9	7.8	7.1	6.5
Total public debt in percent of total exports	25.5	20.9	19.4	19.7	17.9	16.5
(in millions of U.S. dollars, unless otherwise indicated)						
Change in reserves (increase -)	-265.8	-288.5	-89.4	510.6	630.7	728.6
Gross official reserves (end of period)	5,940.7	6,229.2	6,318.7	5,808.0	5,177.3	4,448.7
(In months of imports of goods and services)	28.2	31.1	32.6	38.7	33.2	28.2

Sources: Botswana authorities; and Fund staff estimates and projections.

1/ Year beginning July 1.

2/ Annual average.

3/ Year beginning April 1.

4/ Money and quasi money (M2) plus Bank of Botswana certificates.

5/ As of end-December.

6/ Medium- and long-term public and publicly guaranteed debt outstanding.

Table 2. Botswana: Sectoral GDP and Savings-Investment Balances, 1995/96-2002/03 1/

	1995/96	1996/97	1997/98	1998/99	1999/2000	2000/01	2001/02 IMF staff projections	2002/03 IMF staff projections
(In millions of pula)								
Consumption	8,721.5	10,025.7	11,589.1	13,515.7	15,365.6	17,986.3	19,636.8	21,808.9
Public	4,006.7	4,711.0	5,452.9	6,578.8	7,524.5	9,268.1	10,131.0	11,906.4
Private	4,714.7	5,314.7	6,136.1	6,936.8	7,841.1	8,718.2	9,505.8	9,902.5
Gross investment	3,371.0	4,603.9	6,056.1	7,917.2	4,681.3	4,610.9	7,635.1	8,656.0
Public	1,672.0	2,239.6	2,695.5	3,333.2	2,934.5	3,371.9	3,735.4	3,963.2
Private (including changes in stock)	1,699.0	2,364.3	3,360.5	4,583.9	1,746.8	1,239.0	3,899.7	4,692.8
Net exports of goods and services	2,111.4	3,110.6	2,517.4	90.9	5,315.8	6,755.3	4,306.6	4,268.3
Exports of goods and services	7,411.6	9,881.6	11,392.8	10,051.5	15,318.5	16,510.3	15,406.6	16,322.2
Imports of goods and services	-5,300.2	-6,771.0	-8,875.4	-9,960.6	-10,002.7	-9,755.0	-11,100.0	-12,054.0
Gross domestic savings	5,482.4	7,714.5	8,573.5	8,008.1	9,997.1	11,366.2	11,941.7	12,924.2
Public	1,552.2	2,405.7	3,461.9	2,961.6	2,339.2	5,080.8	2,839.1	2,658.9
Private	3,929.2	5,308.8	5,111.6	5,046.5	7,657.9	6,285.4	9,102.6	10,265.3
GDP at market prices	14,203.9	17,740.2	20,162.6	21,523.7	25,362.7	29,352.5	31,578.5	34,733.1
(in percent of GDP)								
Consumption	61.4	56.5	57.5	62.8	60.6	61.3	62.2	62.8
Public	28.2	26.6	27.0	30.6	29.7	31.6	32.1	34.3
Private	33.2	30.0	30.4	32.2	30.9	29.7	30.1	28.5
Gross investment	23.7	26.0	30.0	36.8	18.5	15.7	24.2	24.9
Public	11.8	12.6	13.4	15.5	11.6	11.5	11.8	11.4
Private (including changes in stock)	12.0	13.3	16.7	21.3	6.9	4.2	12.3	13.5
Net exports of goods and services	14.9	17.5	12.5	0.4	21.0	23.0	13.6	12.3
Exports of goods and services	52.2	55.7	56.5	46.7	60.4	56.2	48.8	47.0
Imports of goods and services	-37.3	-38.2	-44.0	-46.3	-39.4	-33.2	-35.2	-34.7
Gross domestic savings	38.6	43.5	42.5	37.2	39.4	38.7	37.8	37.2
Public	10.9	13.6	17.2	13.8	9.2	17.3	9.0	7.7
Private	27.7	29.9	25.4	23.4	30.2	21.4	28.8	29.6
(Annual change in percent)								
Real GDP	5.5	5.6	8.1	4.1	8.1	9.2	1.2	3.8
<i>Of which</i> : private nonmining real GDP	6.3	4.7	6.7	8.3	6.2	3.1	6.0	5.6
Agriculture	6.6	-7.5	5.9	-7.6	-8.7	4.9	2.4	1.5
Mining	4.5	5.8	9.5	-2.8	12.1	19.6	-7.8	1.0
Manufacturing	7.8	3.7	5.4	5.7	3.5	1.6	3.0	4.5
Water and electricity	0.2	4.6	9.9	12.9	11.3	6.7	7.0	6.0
Construction	3.3	5.5	4.3	11.5	2.4	1.6	7.8	5.0
Trade and hotels	9.8	13.9	4.7	5.6	6.2	7.0	6.5	7.0
Transport	0.4	4.3	9.1	16.2	2.6	5.0	5.5	5.0
Finance and business services	9.7	1.2	9.7	9.0	4.3	2.9	8.0	6.5
General government	5.2	8.3	9.3	6.3	6.0	6.6	7.5	4.0
GDP deflator	9.8	18.3	5.2	2.5	9.0	6.0	6.3	5.9
Nominal GDP	4,715	5,315	6,136	6,937	7,841	8,718	9,506	9,902
Consumer prices (annual average) 2/	10.8	9.6	8.9	6.5	7.8	8.5	6.6	6.3

Sources: Botswana authorities, and Fund staff estimates and projections.

1/ Historical data are based on export and import data from the national accounts (July-June year), which differ significantly from balance of payments data.

2/ Calendar year.

Table 3. Botswana: Central Government Operations, 1997/98-2002/03 1/

	1997/98	1998/99	1999/00	2000/01	2001/02 Revised	2002/03 Budget	2002/03 Staff proj.
(In millions of pula)							
Total revenue and grants	8,281.3	7,677.6	11,963.1	14,115.1	12,611.0	15,411.4	14,042.6
Total revenue	8,169.2	7,539.9	11,837.1	14,050.5	12,553.1	15,380.4	14,011.6
Tax revenue	6,767.3	5,639.5	9,937.8	12,077.6	10,583.0	13,017.2	11,648.5
Mineral revenue	4,681.1	3,186.6	6,687.3	8,367.8	6,879.0	8,492.0	7,500.0
Customs Union receipts	1,186.1	1,261.3	1,931.2	2,188.4	1,731.9	1,541.0	1,648.9
General sales tax/value-added tax (VAT)	327.9	400.5	483.7	523.8	607.2	1,006.0	1,006.0
Other	572.3	791.1	835.6	997.6	1,365.0	1,978.3	1,493.6
Nontax revenue	1,401.8	1,900.4	1,899.3	1,973.0	1,970.0	2,363.1	2,363.1
Interest	251.7	208.6	166.3	205.2	183.5	180.6	180.6
Property income 2/	984.2	1,252.9	1,232.2	1,194.7	1,098.4	1,185.7	1,185.7
Other	165.9	438.9	500.8	573.1	688.2	996.9	996.9
Grants	112.1	137.7	126.1	64.5	58.0	31.0	31.0
Total expenditure and net lending	7,304.2	8,957.4	10,427.5	11,536.5	13,348.1	17,030.5	15,745.9
Current expenditure	4,826.6	6,157.3	7,047.9	8,383.1	9,627.2	11,642.4	11,642.4
Wages and salaries	1,686.4	2,153.2	2,418.7	2,743.3	3,456.2	3,884.2	3,884.2
Interest	86.2	92.8	92.5	83.1	94.6	104.1	104.1
Other	3,054.0	3,911.3	4,536.7	5,556.7	6,076.3	7,654.1	7,654.1
Of which: health	411.2	468.4	542.6	1,063.7	865.0	1,322.7	1,322.7
Capital expenditure	2,695.5	2,934.5	3,451.0	3,134.6	3,679.7	5,187.0	3,902.4
Net lending	-218.0	-134.4	-71.4	18.8	41.3	201.1	201.1
Primary balance (deficit -)	1,063.4	-1,187.0	1,628.1	2,661.6	-642.5	-1,515.0	-1,599.2
Overall surplus or deficit (-)	977.1	-1,279.8	1,535.6	2,578.6	-737.1	-1,619.1	-1,703.3
(In percent of GDP)							
Total revenue and grants	42.3	36.2	49.0	49.8	40.7	45.4	41.4
Total revenue	41.8	35.6	48.5	49.6	40.5	45.3	41.3
Tax revenue	34.6	26.6	40.7	42.6	34.1	38.3	34.3
Mineral revenue	23.9	15.0	27.4	29.5	22.2	25.0	22.1
Customs Union receipts	6.1	6.0	7.9	7.7	5.6	4.5	4.9
General sales tax/VAT	1.7	1.9	2.0	1.8	2.0	3.0	3.0
Other	2.9	3.7	3.4	3.5	4.4	5.8	4.4
Nontax revenue	7.2	9.0	7.8	7.0	6.4	7.0	7.0
Interest	1.3	1.0	0.7	0.7	0.6	0.5	0.5
Property income	5.0	5.9	5.0	4.2	3.5	3.5	3.5
Other	0.8	2.1	2.1	2.0	2.2	2.9	2.9
Grants	0.6	0.7	0.5	0.2	0.2	0.1	0.1
Total expenditure and net lending	37.3	42.3	42.7	40.7	43.0	50.2	46.4
Current expenditure	24.7	29.1	28.9	29.6	31.0	34.3	34.3
Wages and salaries	8.6	10.2	9.9	9.7	11.1	11.4	11.4
Interest	0.4	0.4	0.4	0.3	0.3	0.3	0.3
Other	15.6	18.5	18.6	19.6	19.6	22.5	22.5
Of which: health	2.1	2.2	2.2	3.8	2.8	3.9	3.9
Capital expenditure	13.8	13.9	14.1	11.1	11.9	15.3	11.5
Net lending	-1.1	-0.6	-0.3	0.1	0.1	0.6	0.6
Primary balance (deficit -)	5.4	-5.6	6.7	9.4	-2.1	-4.5	-4.7
Overall surplus or deficit (-)	5.0	-6.0	6.3	9.1	-2.4	-4.8	-5.0
Memorandum item:							
GDP (fiscal year)	19,557.0	21,183.4	24,403.0	28,355.1	31,022.0	33,944.5	33,944.5

Sources: Ministry of Finance and Development Planning; and Fund staff estimates and projections.

1/ Fiscal year beginning April 1.

2/ Includes Bank of Botswana revenue.

Table 4. Botswana: Monetary Survey, 1995-2002 1/

	1995	1996	1997	1998	1999	2000	2001	2002 Apr.
(In millions of pula; end of period)								
Net foreign assets	12,213.0	18,657.7	22,321.2	27,747.3	30,051.3	35,110.5	43,074.8	39,288.9
Bank of Botswana	12,115.5	18,355.6	21,636.5	26,502.4	28,866.8	33,900.4	41,211.5	37,514.5
Assets	12,115.5	18,355.6	21,636.5	26,502.4	28,866.8	33,900.4	41,211.5	37,514.5
Liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Commercial banks	97.5	302.1	684.6	1,245.0	1,184.5	1,210.1	1,863.3	1,774.4
Assets	196.4	453.8	805.1	1,416.5	1,345.6	1,434.9	2,230.9	2,157.6
Liabilities	-98.9	-151.7	-120.4	-171.6	-161.1	-224.8	-367.7	-383.1
Net domestic assets	-9,527.4	-15,468.1	-18,217.6	-22,025.8	-22,823.3	-27,782.0	-33,458.1	-29,591.3
Net domestic credit	-4,747.2	-5,509.5	-13,543.1	-16,178.7	-16,131.3	-19,383.5	-22,573.2	-19,020.7
Net claims on the government	-6,523.2	-7,305.5	-15,440.5	-19,137.0	-20,307.2	-24,309.3	-28,031.8	-24,764.9
Bank of Botswana	-6,506.5	-7,266.6	-15,406.9	-19,122.0	-20,255.8	-24,205.1	-27,972.0	-24,704.8
Commercial banks	-16.7	-38.9	-33.6	-15.0	-51.4	-104.2	-59.8	-60.0
Claims on nongovernment	1,776.1	1,796.0	1,897.3	2,958.3	4,175.9	4,925.7	5,458.6	5,744.2
Claims on parastatals	94.7	70.5	61.4	266.7	527.6	458.1	479.9	451.2
Claims on the private sector	1,681.4	1,725.5	1,835.9	2,691.6	3,648.2	4,467.7	4,978.8	5,293.0
Of which: households	781.8	849.5	943.0	1,389.5	1,995.0	2,429.6	2,947.9	3,115.0
private enterprises	777.9	776.5	832.1	1,071.4	1,523.4	1,914.8	1,966.7	2,144.3
Other items (net)	-4,780.3	-9,958.5	-4,674.5	-5,847.1	-6,692.0	-8,398.5	-10,884.8	-10,570.7
Money plus quasi money	2,685.6	3,189.9	4,103.5	5,721.6	7,228.2	7,328.5	9,616.7	9,697.6
Money	829.3	950.9	1,037.8	1,513.0	1,774.6	1,896.6	2,350.7	2,472.4
Currency	222.7	247.1	275.7	352.7	403.7	427.0	481.4	508.8
Current deposits	606.6	703.8	762.1	1,160.3	1,370.9	1,469.6	1,869.3	1,963.6
Quasi money	1,856.3	2,239.0	3,065.7	4,208.6	5,453.7	5,431.9	7,266.0	7,225.2
Memorandum items:								
Broad money (M3)	3,189.6	4,158.5	4,987.5	6,710.0	8,649.4	8,557.0	10,919.2	13,410.9
Of which								
Bank of Botswana certificates 2/	504.1	968.6	885.9	988.4	1,421.2	1,228.6	1,302.5	3,713.3
Broad money (M4)	3,408.6	4,454.7	5,469.3	7,649.4	9,745.0	9,669.1	12,064.9	14,626.8
Of which								
Foreign currency accounts	219.0	296.2	481.8	939.4	1,095.6	1,112.0	1,145.6	1,215.9
(Twelve-month percentage change)								
Net foreign assets	14.4	52.8	19.6	24.3	8.3	16.8	22.7	6.7
Net domestic assets	-15.0	-62.4	-17.8	-20.9	-3.6	-21.7	-20.4	-3.0
Net domestic credit	3.2	-16.1	-145.8	-19.5	0.3	-20.2	-16.5	8.2
Net claims on the government	3.3	-12.0	-111.4	-23.9	-6.1	-19.7	-15.3	4.2
Claims on nongovernment	-3.6	1.1	5.6	55.9	41.2	18.0	10.8	12.2
Claims on parastatals	-36.0	-25.6	-12.8	334.2	97.8	-13.2	4.8	-12.3
Claims on the private sector	-0.8	2.6	6.4	46.6	35.5	22.5	11.4	14.9
Of which: households	20.9	8.7	11.0	47.3	43.6	21.8	21.3	18.9
private enterprises	-18.4	-0.2	7.2	28.8	42.2	25.7	2.7	14.1
Other items (net)	-41.5	-108.3	53.1	-25.1	-14.5	-25.5	-29.6	-31.9
Money plus quasi money (M2)	12.3	18.8	28.6	39.4	26.3	1.4	31.2	20.1
Broad money (M3)	9.4	30.4	19.9	34.5	28.9	-1.1	27.6	40.9
Broad money (M4)	...	30.7	22.8	39.9	27.4	-0.8	24.8	53.7
(Annual change in percent of beginning-of-year money stock, unless otherwise indicated)								
Net foreign assets	64.4	240.0	114.8	132.2	40.3	70.0	108.7	30.7
Net domestic assets	-52.0	-221.2	-86.2	-92.8	-13.9	-68.6	-77.5	-10.5
Net domestic credit	6.6	-28.4	-251.8	-64.2	0.8	-45.0	-43.5	21.1
Net claims on the government	9.4	-29.1	-255.0	-90.1	-20.5	-55.4	-50.8	13.4
Claims on nongovernment	-2.8	0.7	3.2	25.9	21.3	10.4	7.3	7.7
Claims on parastatals	-2.2	-0.9	-0.3	5.0	4.6	-1.0	0.3	-0.8
Claims on the private sector	-0.6	1.6	3.5	20.9	16.7	11.3	7.0	8.5
Of which: households	5.7	2.5	2.9	10.9	10.6	6.0	7.1	6.1
private enterprises	-7.3	-0.1	1.7	5.8	7.9	5.4	0.7	3.3
Other items (net)	-58.6	-192.8	165.7	-28.6	-14.8	-23.6	-33.9	-31.7
Money plus quasi money (M2)	12.3	18.8	28.6	39.4	26.3	1.4	31.2	20.1
Broad money (M3)	11.5	36.1	26.0	42.0	33.9	-1.3	32.2	48.3
Broad money (M4)	142.5	39.0	31.8	53.1	36.6	-1.1	32.7	63.3
Memorandum items:								
Nominal GDP (million of pula; calendar year)	13,232.8	15,972.0	18,951.4	20,843.1	23,443.2	27,357.6	30,465.5	33,155.8
Growth of nominal GDP (annual change in percent)	13.6	20.7	18.7	10.0	12.5	16.7	11.4	8.8
Velocity (GDP rel. to broad money, M2)	5.2	5.4	5.2	4.2	3.6	3.8	3.6	3.4

Sources: Bank of Botswana; and Fund staff estimates and projections.

1/ End of period.

2/ Bank of Botswana certificates held by non-banks.

Table 5. Botswana: Assets and Liabilities of the Bank of Botswana, 1995-2002  
(In millions of pula; end of period)

	1995	1996	1997	1998	1999	2000	2001	2002 Apr.
Foreign assets	12,115.5	18,355.6	21,636.5	26,502.4	28,866.8	33,900.4	41,211.5	37,514.5
Pula fund	4,247.9	5,394.2	17,654.1	23,561.9	24,453.7	28,711.6	32,175.9	30,600.6
Liquidity portfolio	7,673.2	12,689.6	3,721.3	2,545.2	4,074.9	4,833.4	8,533.8	6,437.5
Matched assets/liability portfolio	0.0	17.1	11.9	18.5	16.3	22.6	29.6	37.2
Fund accounts	198.0	247.8	246.4	376.4	321.9	332.8	471.6	438.9
Holding of SDRs	113.5	150.4	156.1	203.4	178.3	208.8	276.7	258.7
Reserve position	84.5	97.3	90.3	173.0	143.6	124.0	194.9	180.2
Loans and advances to financial institutions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Fixed assets	96.7	98.5	100.0	108.0	122.0	131.1	129.3	127.2
Other assets	1,159.3	-16.2	-6.1	1.5	1.8	2.4	0.1	1.4
<b>Assets = liabilities</b>	<b>13,371.4</b>	<b>18,437.9</b>	<b>21,730.4</b>	<b>26,611.9</b>	<b>28,990.7</b>	<b>34,033.9</b>	<b>41,340.9</b>	<b>37,643.1</b>
Reserve money	405.4	453.4	572.0	707.3	807.9	857.3	969.5	942.2
Currency in circulation	318.5	355.9	417.1	497.7	606.8	606.5	701.1	662.9
Currency outside banks	222.7	247.1	275.7	352.7	403.7	427.0	481.4	508.8
Pula currency in banks	95.9	108.8	141.4	145.0	203.2	179.5	219.7	154.1
Bankers' deposits	86.8	97.5	155.0	209.6	201.1	250.8	268.4	279.3
Private sector time deposits	47.8	46.7	62.7	25.7	171.9	183.4	183.8	237.2
Bank of Botswana certificates outstanding	1,963.8	2,815.7	3,308.2	3,246.2	4,230.2	3,712.4	5,147.7	5,922.9
Bankers	1,459.7	1,847.1	2,424.2	2,257.8	2,809.0	2,483.8	3,845.2	2,209.6
Others	504.1	968.6	883.9	988.4	1,421.2	1,228.6	1,302.5	3,713.3
Government deposits	6,506.5	7,266.6	15,406.9	19,122.0	20,255.8	24,205.1	27,972.0	24,704.8
Capital and reserves	2,922.8	6,085.5	1,866.0	3,201.6	3,387.3	4,353.7	6,629.7	5,640.9
Paid-up capital	3.6	3.6	25.0	25.0	25.0	25.0	25.0	25.0
General reserve	234.1	5,754.6	1,600.0	1,600.0	1,600.0	1,600.0	1,600.0	1,600.0
Revaluation reserve	2,685.2	327.4	241.0	1,576.6	1,762.3	2,728.7	5,004.7	4,015.9
Other liabilities	1,525.2	1,770.1	514.7	309.0	137.7	722.1	438.2	195.1

Source: Bank of Botswana.

Table 6. Botswana: Balance of Payments, 1995-2001 1/

(In millions of U.S. dollars, unless otherwise indicated)

	1995	1996	1997	1998	1999	2000	2001 Est.
Current account balance	299.7	494.5	722.0	204.7	618.3	546.8	389.1
Trade balance	554.9	750.0	896.1	78.0	784.7	904.6	662.8
Exports, f.o.b.	2,160.6	2,218.1	2,822.1	2,072.8	2,658.4	2,682.6	2,325.7
<i>Of which:</i>							
Diamonds	1,440.9	1,586.2	2,104.0	1,479.8	2,119.5	2,236.1	1,937.1
Imports, f.o.b.	-1,605.8	-1,468.1	-1,926.0	-1,994.8	-1,873.6	-1,778.0	-1,662.9
<i>Of which</i>							
Food, beverages, and tobacco	-305.3	-294.3	-296.9	-296.9	-305.3	-293.6	-264.2
Chemical and rubber products	-177.0	-177.7	-205.4	-200.7	-203.4	-203.0	-176.1
Metal and metal products	-166.3	-153.4	-241.4	-228.0	-189.7	-151.1	-164.2
Machinery and electrical equipment	-300.1	-279.8	-398.4	-480.5	-463.2	-463.0	-400.9
Services	-183.9	-181.0	-230.7	-235.2	-155.9	-223.3	-201.8
Transportation	-149.1	-140.4	-175.0	-164.9	-162.2	-174.4	-154.8
Travel	16.7	15.6	43.2	72.2	87.3	24.5	26.0
Other services	-51.5	-56.4	-98.9	-142.6	-81.0	-73.4	-73.0
Income	-32.4	-253.5	-144.9	120.3	-262.3	-352.2	-276.8
Compensation of employees	13.2	-13.9	-10.5	-15.0	-26.3	-36.8	-36.8
Investment income	-45.6	-239.2	-134.4	135.3	-235.9	-315.4	-240.0
<i>Of which</i>							
Earnings on reserves	359.7	441.0	545.4	531.3	347.6	281.9	285.0
Dividends and profits	-346.5	-599.0	-572.7	-313.2	-575.1	-587.3	-531.1
Current transfers	-38.8	178.9	201.5	241.6	251.8	217.7	204.9
Capital and financial accounts	-19.4	48.6	22.5	-171.6	-223.2	-162.4	-204.6
Capital account	14.4	6.2	16.9	32.0	20.6	38.2	18.0
Financial account	-33.9	42.4	5.6	-203.6	-243.8	-200.6	-222.6
Direct investment	29.5	72.2	96.1	92.3	35.2	55.1	55.1
Portfolio investment	-30.6	-4.5	-33.2	-52.0	-35.0	-43.1	-43.2
Other investment	-32.8	-25.3	-57.3	-244.0	-244.0	-212.6	-231.3
<i>Of which</i>							
Net government long-term borrowing	-12.3	-19.6	51.3	22.4	-25.8	-32.4	-16.5
Other net private long-term borrowing	-3.8	13.0	-10.0	27.5	1.8	2.0	2.1
Short-term borrowing	36.4	58.3	71.5	20.3	46.4	46.1	60.4
Reserve assets (increase -)	-294.5	-331.5	-647.2	-265.8	-288.5	-89.4	421.4
Net errors and omissions	-14.3	-211.6	-97.3	232.7	-106.6	-294.9	-605.9
Memorandum items:							
Current account (percent of GDP)	6.3	10.3	13.9	4.1	12.2	10.2	7.4
Trade balance (percent of GDP)	11.6	15.6	17.2	1.6	15.5	16.8	12.6
End-of-year reserves 2/	4,696.2	5,027.7	5,674.9	5,940.7	6,229.2	6,318.7	5,897.3
In months of imports of goods and services	27.5	33.3	28.8	28.2	31.2	32.6	32.1
Exchange rate							
U.S. dollar per pula (period average)	0.3608	0.3029	0.2741	0.2380	0.2163	0.1965	0.1720
U.S. dollars per pula (end of period )	0.3544	0.2744	0.2625	0.2243	0.2159	0.1865	0.1432

Sources: Botswana authorities; and Fund staff estimates.

1/ Based on pula-denominated estimates converted at the period-average exchange rate.

2/ Includes valuation adjustment.



Table 7. Botswana: Medium-Term Scenario, 2002-2007

	2002	2003	2004	2005	2006	2007
	IMF staff projections					
	(Annual percentage change, unless otherwise indicated)					
National income and prices						
Real GDP 1/	3.8	3.6	3.5	3.4	3.5	3.3
Real private nonmining GDP 1/	5.6	5.1	4.9	4.8	4.7	4.7
GDP deflator 1/	5.9	5.3	4.7	4.4	4.2	4.2
Consumer prices (average)	6.3	6.2	5.1	4.6	4.4	4.3
Nominal GDP (in billions of pula) 1/	34.7	37.9	41.1	44.4	47.8	51.5
External sector						
Exports of goods, f.o.b. (in U.S. dollar terms)	-2.0	3.9	3.2	3.3	5.0	2.5
Imports of goods, f.o.b. (in U.S. dollar terms)	-4.0	14.0	4.9	5.3	5.3	5.3
Terms of trade	1.6	-4.3	0.8	0.4	0.9	0.5
Central government finance 2/						
Total revenue and grants	11.4	4.9	13.0	10.7	10.5	8.1
Total expenditure and net lending	18.0	4.1	4.5	4.1	4.2	4.4
	(Twelve-month percentage change)					
Money and credit						
Net claims on government	15.0	19.2	5.8	0.2	-1.3	6.4
Claims on private sector	19.2	3.5	2.8	18.6	46.2	35.0
Money and quasi money (M2)	0.7	18.4	8.7	8.2	8.1	7.3
	(In percent of GDP)					
Investment and savings 1/						
Gross investment	24.6	25.3	25.8	26.2	27.1	28.4
Public	11.6	11.1	10.1	8.8	7.7	6.7
Private	13.0	14.2	15.7	17.4	19.4	21.7
Gross national savings	34.6	33.5	32.1	31.2	32.0	33.2
Public	8.5	8.2	8.5	9.4	11.1	12.4
Private	26.1	25.3	23.6	21.8	20.8	20.8
Central government finance 2/						
Total revenue and grants	41.4	42.6	41.1	43.0	44.1	45.3
Total expenditure and net lending	46.4	45.4	43.5	42.1	40.6	39.3
Overall balance (including grants)	-5.0	-2.8	-2.4	0.9	3.5	6.0
External sector						
External current account balance (deficit -)	6.2	2.1	1.4	0.4	0.5	0.5
External debt in percent of GDP 3/	7.7	7.1	6.6	6.2	5.9	5.5
Total public debt in percent of total exports	18.6	19.2	18.3	17.6	16.7	16.3
	(In millions of U.S. dollars, unless otherwise indicated)					
Change in reserves (increase -)	-528	672	224	236	206	188
Gross official reserves (end of period)	6,425	5,754	5,530	5,294	5,088	4,900
(In months of imports of goods and services)	32.3	26.3	24.8	23.1	21.5	20.2

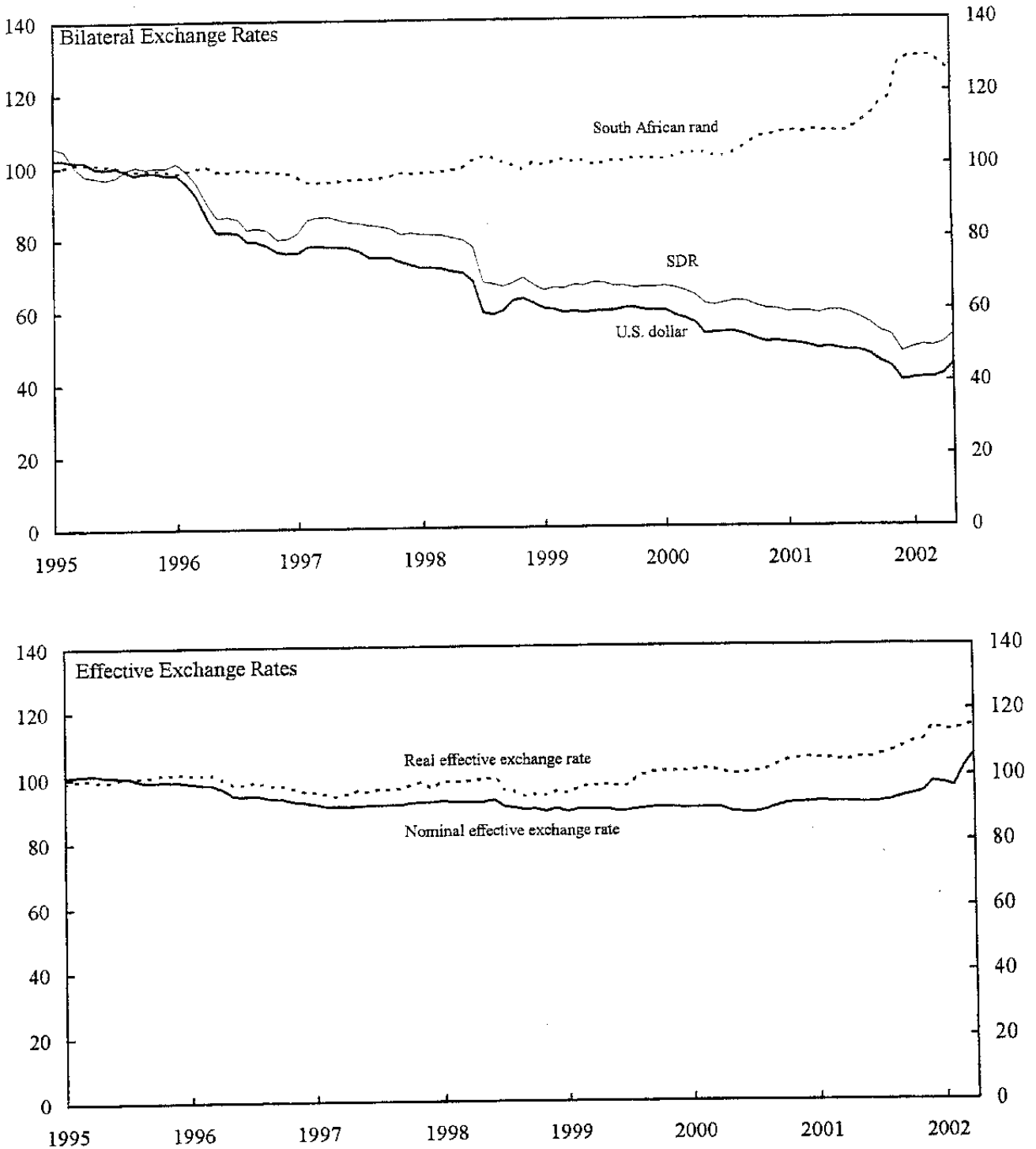
Sources: Botswana authorities; and Fund staff estimates and projections.

1/ Year beginning July 1.

2/ Year beginning April 1.

3/ Medium- and long-term public and publicly guaranteed debt outstanding.

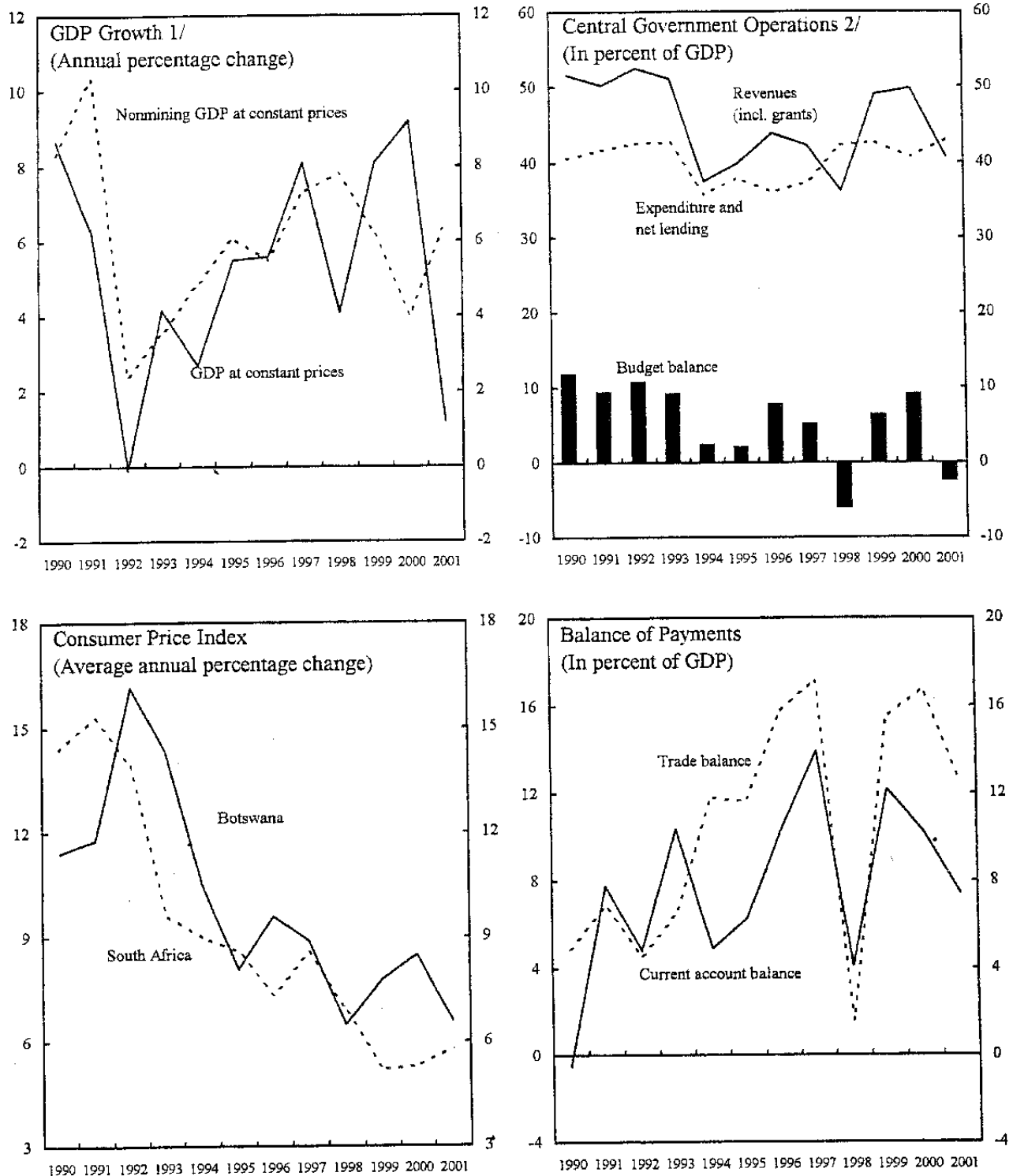
Figure 1. Botswana: Selected Exchange Rate Indicators, January 1995-June 2002  
(1995 = 100; foreign currency per pula) 1/



Source: Botswana authorities.

1/ A rise in the index indicates an appreciation of the pula.

Figure 2. Botswana: Main Economic Indicators, 1990-2001

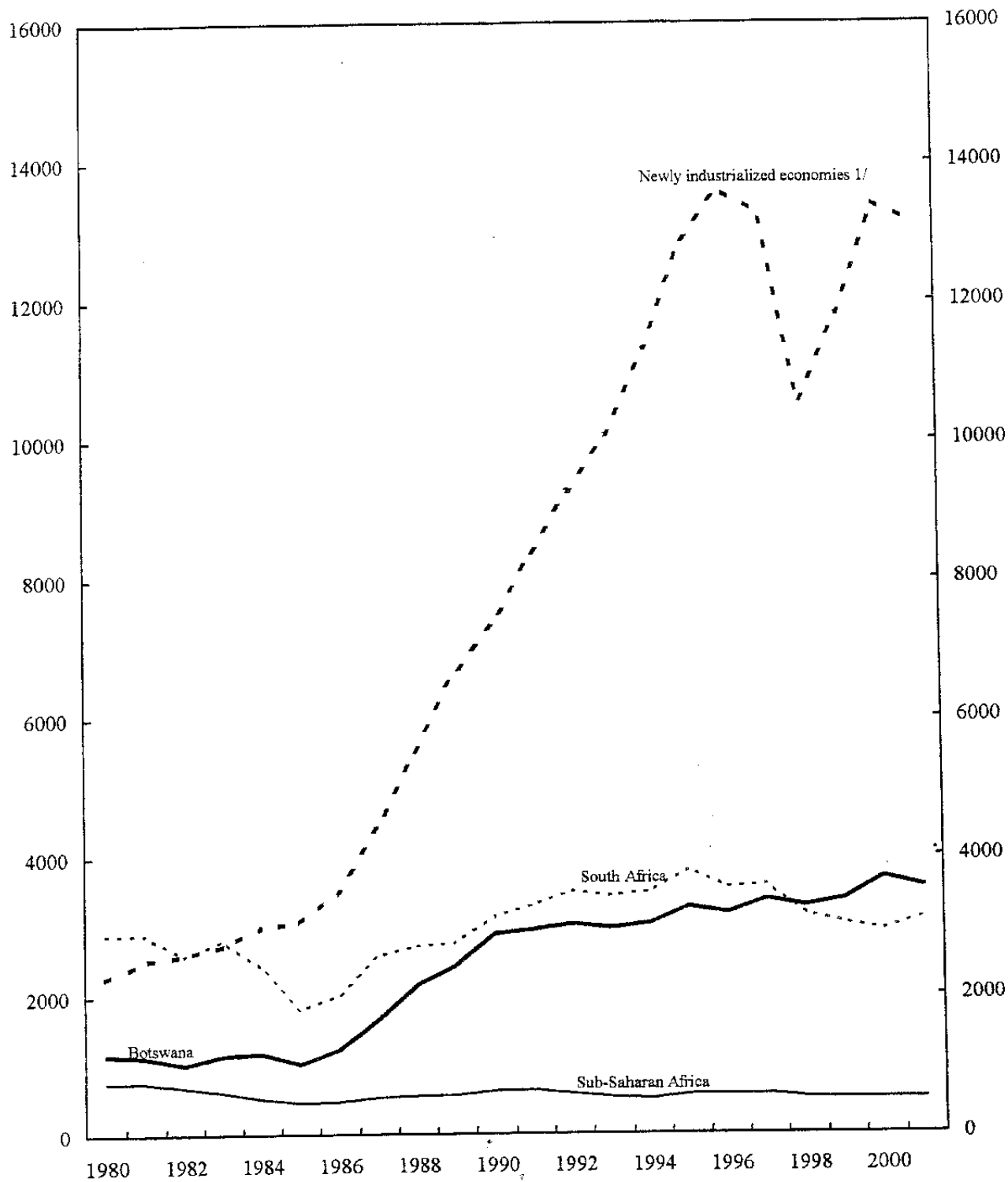


Sources: Botswana authorities; and Fund staff estimates.

1/ National accounts year beginning July 1.

2/ Fiscal year beginning April 1.

Figure 3. Botswana and Selected Countries: Per Capita GDP, 1980-2001  
(In U.S. dollars)



Source: World Economic Outlook Database.

1/ Hong Kong SAR, Taiwan Province of China, Korea, and Singapore.

**Botswana: Relations with the Fund**  
(As of June 30, 2002)

I.	<b>Membership Status</b>	Joined July 24, 1968; Article VIII	
II.	<b>General Resources Account</b>	<u>SDR (million)</u>	<u>% of Quota</u>
	Quota	63.00	100.0
	Fund holdings of currency	43.72	69.39
	Reserve position in Fund	19.29	30.63
	Financial Transaction Plan transfers (net)	4.00	
III.	<b>SDR Department</b>	<u>SDR (million)</u>	<u>% of Allocation</u>
	Net cumulative allocation	4.36	100.0
	Holdings	32.06	735.42
IV.	<b>Outstanding purchases and loans</b>	None.	
V.	<b>Financial arrangements</b>	None.	
VI.	<b>Projected obligations to Fund</b>	None.	
VII.	<b>Contribution to Funding of the Enhanced Structural Adjustment Facility</b>		

In July 1994, Botswana deposited with the Fund, as trustee, an amount equivalent to US\$10 million for the benefit of the subsidy account of the Enhanced Structural Adjustment Facility (ESAF). In April 1997, Botswana made a five-year deposit of SDR 14.6 million in the ESAF-Heavily Indebted Poor Countries (HIPC) Trust.

**VIII. Exchange rate arrangement**

The exchange rate of the Botswana pula is determined on the basis of a basket of currencies. On July 25, 2002, the representative rate was US\$1 = 6.1614, and the exchange rate of the South African rand to the pula was R 1 = P 0.5996.

**IX. Article IV consultation**

The last Article IV consultation was concluded by the Executive Board on March 12, 2001.

The Executive Board took the following decision:

1. The Fund takes this decision relating to Botswana's exchange measure subject to Article VIII, Section 3, in the light of the 1999 Article IV consultation with Botswana conducted under Decision No. 5392-(77/63), adopted April 29, 1977, as amended (Surveillance over Exchange Rate Policies).

2. As described in SM/99/204, Botswana maintains a multiple currency practice arising from the Foreign Exchange Risk-Sharing Scheme (FERS) applicable to outstanding external loans obtained by certain public enterprises before October 1, 1990, which is subject to Fund approval under Article VIII, Section 3.

3. In view of Botswana's discontinuance of the FERS scheme in 1990, and of its intention to eliminate the multiple currency practice by 2006, when the last loan under the scheme will mature, the Fund approves the retention by Botswana of the multiple currency practice until March 31, 2002 or the conclusion of the next Article IV consultation with Botswana, whichever is earlier.

**X. Technical assistance**

**Resident advisors**

<b>Department</b>	<b>Dates</b>	<b>Position</b>
MAE	1997	Central Banking Advisor
	1999-2000	Banking Supervision Advisor
STA	1997	Balance of Payments Advisor
	2001	ROSC Data Module

**XI. Technical assistance missions**

<b>Department</b>	<b>Dates</b>	<b>Purpose</b>
MAE	January 2001	Banking Supervision Advisor
	February 2001	Monetary Operations
	December 2001	MEFMI-Monetary Operations
	August 2002	Banking Supervision, Anti money laundering
FAD	November 1997	Introduction of a value-added-tax (VAT)
	September 2000	Implementation of VAT next steps
	February 2002	Tax Administrator (SADC Region)
STA	May 2001	Inspection for Visit for long-term BOP Advisor
	July 2002	BOP Statistics: Peripatetic visit

**Botswana: Relations with the World Bank Group  
(As of June 30, 2002)**

1. Botswana became a member of the World Bank and the International Development Association (IDA) in 1968, and is now a contributor to IDA. There are no active IBRD/IDA projects in Botswana. The Economic Development Institute (EDI) of the World Bank conducted a regional course on the Southern African Development Community (SADC) in Botswana in 1997. In FY 2000, about 50 participants from Botswana attended World Bank Institute (WBI) courses, and a regional program on Economic Policy in Labor-Surplus Economies was held in the country.
2. Botswana joined the International Finance Corporation (IFC) in 1979 and the Multilateral Investment Guarantee Agency (MIGA) in 1990. The current investment portfolio is small—an equity investment of \$0.8 million in a leasing company.
3. Botswana joined MIGA in 1988. No MIGA guarantees for investment in Botswana have been issued to date. Botswana has benefited from a number of MIGA's technical assistance activities and has participated in several of MIGA's annual Africa Mining Investment Symposia.

### Botswana: Statistical Issues

1. The core statistical data for surveillance—exchange rate, international reserves, reserve/base money, central bank balance sheet, broad money, interest rate, and consumer price index data—are available on a monthly basis and are reported to the Fund with an acceptable degree of regularity and promptness. In general, the quality of these data is adequate to conduct surveillance. The authorities have started generating quarterly data for the national accounts and balance of payments. However, the time lag in compiling the national accounts and labor market data needs to be reduced. Intensified efforts are needed to develop a unified accounting period for preparing and presenting economic data; the current arrangements—according to which the balance of payments statistics are compiled on a calendar-year basis, and the national accounts and the budget on July-June and April-March bases, respectively—impede the preparation of an integrated set of economic data. Most economic data are made available to the general public through a number of official publications, including the *Annual Report* and *Botswana Financial Statistics* of the Bank of Botswana, the *Annual Economic Report* of the Ministry of Finance and Development Planning, and the *Statistical Bulletin* of the Central Statistics Office (CSO).
2. The data module of the Report on the Observance of Standards and Codes (ROSC) was conducted in 2001. The mission concluded that, by developing and forcefully implementing an action plan now, Botswana should be able to meet most, if not all, the remaining requirements for SDDS subscription within a period of two years or more. Because of the long lead times involved, an early priority in this regard should be to advance the level of GDDS participation by preparing metadata, including plans for short- and long-term improvements for posting on the Dissemination Standards Bulletin Board.
3. Furthermore, the mission observed that Botswana's statistics producing agencies have a legal and institutional framework that supports statistical quality and demonstrate an awareness of quality as the cornerstone of statistical work. Resources are mostly commensurate with the needs of current statistical programs, but may be inadequate for the further development of statistical systems.

#### Real sector

4. Authorities have started producing national accounts data both on annual and quarterly bases; data are available through 2000/01 (July-June). Annual employment and wage information are available but are rarely reported to STA for publication in the *International Financial Statistics (IFS)*. The national accounts would benefit from the adoption of the System of National Accounts 1993 and improved response to source surveys.
5. The consumer price index is comprehensive and provides a breakdown of the index between urban and rural areas, as well as between tradables (domestic and imported) and nontradables. In early 1997, the index was rebased from November 1991 to November 1996, and the weights were changed to reflect the findings of the 1993/94 Household Income and Expenditure Survey. With respect to the producer price index, the data could be improved by



the collection of more comprehensive source data and the adoption of best international practice for the data compilation.

### **Fiscal accounts**

6. Central government finance data for publication in the *IFS* are reported with a two-to-three month lag. The timeliness of the reporting can be improved, as these data are produced monthly, with a lag of three-to-four weeks, for use in the Ministry of Finance and Development Planning (MFDP). No annual government finance data for publication in the *GFS Yearbook (GFSY)* have been reported since 1996. However, comprehensive annual government finance statistics on consolidated central government are published by the authorities with a 12-month lag after the end of the reference year in MFDP's Annual Statements of Accounts..

7. Compilation and dissemination of central government finance data are largely based on the 1986 methodology of the IMF (*1986 GFS Manual*), and cover all central government activities, including balances of financial assets and liabilities of the central government units. The classification of revenue, expenditure, and financing data, are broadly consistent with the 1986 methodology, with a few exceptions. Monthly data are compiled, but the level of accuracy is less than for audited annual fiscal data, which are made available with a 12 month lag. The monthly data are available for internal use by Ministry of Finance and Development Fund, and are timely (with a lag of less than a month after the end of the reference month; but up to three months for March, the last month of the fiscal year). Most detailed data of the accounts are sufficiently detailed for GFS purposes, but source data could be improved to allow consolidation of general government statistics. In general, the published data have been audited by the Auditor General. Accuracy and reliability are clearly favored at the expense of timeliness.

### **Monetary accounts**

8. In compiling the monetary survey, the Bank of Botswana follows broadly the methodology recommended in the Fund's *Monetary and Financial Statistics Manual (MFSM)*. However, commercial banks do not apply strictly the principle of "center of economic interest", but classify their accounts into resident and nonresident mainly according to the nationality of the account holder. Moreover, the monetary survey does not cover four deposit-taking institutions (two merchant banks, one building society, and one savings bank), which account for around five percent of the deposits of the system.

9. Monetary data for publication in *IFS* are reported on a regular basis. The timeliness of reporting has improved in 2002. However, data for the monetary authorities are still being reported to STA with a longer lag (one additional month) than those for the deposit money banks.

### **External trade and balance of payments**

10. Botswana reports data annually on the balance of payments and the international investment position. A resident IMF balance of payments statistics advisor assigned to the Bank of Botswana in October 1997 concluded his term in July 2000. The project helped establish BPM5 as the basis for balance of payment statistics, revised the Foreign Investment Survey, contributed to the development of quarterly statistics, and improved estimation methodologies. However, delays in supplying source data are a major concern and hamper efforts to improve the timeliness of statistics. Balance of payments statistics are compiled in conformity with internationally accepted statistical frameworks, but estimation methods for the BOP need to be updated. While procedures underlying the compilation of data are sound, some estimation methods need to be updated.

Botswana: Core Statistical Indicators  
(As of July 19, 2002)

	Exchange Rates	Foreign Reserves	Reserve/ Base Money	Central Bank Balance Sheet	Broad Money	Interest Rates	Consumer Price Index	Exports/Imports	Current Account Balance	Overall Fiscal Balance	GDP/GNP	External Debt/Debt Service
Date of latest observation	June 2002	May 2002	Apr.. 2002	Apr. 2002	Apr. 2002	May 2002	June 2002	2000	2000	2001/02 <u>1/</u>	2000/01 <u>2/</u>	Mar. 2002
Date received	July 2002	July 2002	July 2002	July 2002	July 2002	July 2002	July 2002	Mar. 2002	Mar. 2001	Feb. 2001	Feb. 2001	May 2002
Frequency of data <u>3/</u>	M	M	M	M	M	M	M	M/Q	A	A/Q	A	A/O
Frequency of reporting <u>3/</u>	M	M	M	M	M	M	M	M/O (Quarterly reporting irregular)	A	Q	A	A
Source of data <u>4/</u>	A	A	A	A	A	A	A	A/N	N	A	N	N
Mode of reporting <u>5/</u>	C	C	C	C	C	C	C	C/M/V	C/M/V	C/M/V	C/M/V	C/M/V
Confidentiality <u>6/</u>	C	C	C	C	C	C	C	C	C	C	C	C
Frequency of publication <u>3/</u>	M	M	M	M	M	M	M	Q	A	Q	A	A

1/ April-March.

2/ July-June.

3/ M = monthly; Q = quarterly; A = annual; and O = other.

4/ A = direct report by the authorities; and N = official publication.

5/ C = cable or facsimile; M = mail; and V = staff visits.

6/ C = unrestricted use.

**Botswana: Social and Demographic Indicators**

Area (square kilometers)	581,730	Health	
Population (1997/98 estimate)		Physician per 10,000 population (1990-98)	0.2
Total (million)	1.57	Access to safe water (1993/94) 1/	
Growth rate (percent a year, 1965-99 average)	3.2	Percentage of population	
Density (per. sq. km.)	3.0	Total	83.2
GDP per capita (U.S. dollars, 2000 estimate 1/)	3,500	Urban	100.0
		Rural	76.1
Population characteristics		Education	
Life expectancy at birth (years, 1998)	40.0	School enrollment (1997)	
Birth rate per 1,000 people (1999)	33	(in percent, net )	
HIV/AIDS prevalency rate	39		
Labor force (1999, million)	0.65	Primary education	81
Female (in percent of total)	45.4	Secondary education	45
		Adult literacy rate (2000)	75

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Source: World Bank, 2001 *World Development Indicators*.

1/ Botswana authorities. National accounts year beginning July 1.

**Statement by the IMF Staff Representative  
October 9, 2002**

1. The following information has become available since the staff report was issued on August 14. It does not change the thrust of the staff appraisal.
2. The transition from sales tax to value added tax (VAT) has gone well. Most traders registered before the July launch, and despite some teething problems, the system is working without significant disruptions. We will continue to monitor the VAT, in particular the impact on prices, government revenue, and the refund mechanism for exporters.
3. Headline inflation rose from just under 6 percent in June 2002 to 8.8 percent in July and 9.9 percent in August 2002. Much of the rise is the result of the replacement of the sales tax with the VAT, which is more broad-based. The impact in July—about 3 percentage points—is in line with staff expectations, but a larger than expected rise in food prices in August could push inflation for the year above the current projections of 6¾ percent. In its mid-year review of monetary policy, the Bank of Botswana indicated its intention to be guided by underlying inflation, that is excluding the VAT effect, when assessing inflationary developments, provided that public and private wage settlements are not adjusted to compensate for this tax increase. The staff supports this view.

The regional food situation has not caused problems in Botswana on the scale experienced by some of its neighbors, and the authorities are providing relief to those in need through existing drought relief programs. These include short-term employment projects, which this year have been undertaken as part of the National Master Plan for Agricultural Development.



INTERNATIONAL MONETARY FUND

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November 1, 2002

International Monetary Fund  
700 19<sup>th</sup> Street, NW  
Washington, D. C. 20431 USA

## **IMF Concludes 2002 Article IV Consultation with Botswana**

On October 9, 2002, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Botswana.<sup>1</sup>

### **Background**

Abundant diamond resources, coupled with sound macroeconomic policies, have enabled Botswana to achieve one of the highest growth rates in the world. Over the past 30 years, real per capita GDP growth averaged more than 7 percent a year, allowing Botswana to move from one of the poorest countries in the world to a position as a middle-income country today. Botswana remains heavily dependent on its diamond sector: it accounts for more than one-third of GDP and 70 percent of export earnings.

HIV/AIDS is Botswana's foremost economic and social challenge. The government is tackling the virus head on through prevention programs and it intends to provide advanced drug therapies to all those in need. Health spending was increased by 50 percent in the 2002/03 (April-March), but the long-term cost implications of HIV/AIDS are unclear.

Real GDP growth slipped to an estimated 1¼ percent in 2001/02 (July-June), largely reflecting a downturn in the global diamond market and a drop in Botswana's diamond production. The nonmining sectors performed better, especially the service industries. Their success is in part a

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<sup>1</sup> 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. 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. This PIN summarizes the views of the Executive Board as expressed during the October 9, 2002 Executive Board discussion based on the staff report.

product of Botswana's market-friendly environment, sound macroeconomic policies, and investments in education and physical infrastructure.

Consumer price inflation fell below 6 percent at the end of 2001, reflecting the tight monetary policy but also better inflation performance in Botswana's trading partners and a modest appreciation of the pula in effective terms. Inflation picked up in early 2002 as food prices in the region shot up, but subsequently retreated to under 6 percent in June 2002.

The overall fiscal balance moved into deficit 2001/02 (April-March), only the second deficit in 20 years. It is mainly attributed to the decline in mineral revenue, but also a 16 percent rise in government spending.

The Bank of Botswana held interest rates unchanged over the period October 2000–June 2002. Yields on Bank of Botswana Certificates have been steady in the 12½-13 percent range, but real interest rates have increased as inflation has come down. The pula was buffeted by volatility in the South African rand exchange rate against major currencies in 2001 and into early 2002, but the country's pegged exchange rate arrangement worked well, holding the effective exchange rate to an appreciation in the 5–7 percent range.

Botswana's external current account recorded a surplus of 10¼ percent in 2000 reflecting the buoyant global diamond market in that year. The current account is estimated to have been in surplus also in 2001, albeit considerably smaller mainly because of lower diamond export earnings. End year reserves were US\$5.9 billion (32 months of imports). Botswana, as a member of the Southern African Customs Union, is seeing its external tariffs decline.

### **Executive Board Assessment**

Directors noted that since the last Article IV consultation, Botswana's economy has been hit by several negative shocks, including a temporary decline in global diamond demand, the near 40 percent depreciation in the South African rand in 2001, and the regional food crisis. Directors commended the authorities for pursuing prudent macroeconomic policies, which, together with Botswana's substantial financial reserves, have helped the country weather these adverse external shocks.

Looking ahead, Botswana's medium-term growth prospects will depend on the continued sustained development of the nonmining economy, as diamond production and revenue reach a plateau, and on decisive action to contain the enormous social and economic costs of the HIV/AIDS pandemic. Directors were encouraged by the authorities' demonstrated commitment to meet these challenges successfully through the continued implementation of sound and market-friendly economic policies.

Directors commended in particular the government's head-on approach to the challenges of HIV/AIDS, by adopting a coordinated response that aims at preventing further spread of the infection, alleviating suffering, and treating all patients with advanced medication. They also welcomed the establishment of a national AIDS coordinating agency to help spearhead the

program at the highest political level and help to mobilize international support. While the cost implications of the authorities' response are still highly uncertain, Directors noted that its budgetary impact is likely to be very high over time. They welcomed the authorities' commitment to expenditure restraint and public revenue enhancement, including the recent introduction of the VAT. Looking ahead, Directors urged the authorities to use the forthcoming National Development Plan 9 as the appropriate planning tool for addressing the budgetary impact of HIV/AIDS in a comprehensive manner, and for making the difficult choices concerning government resources and spending in a medium-term policy framework.

While Botswana's tight monetary stance is appropriate in view of demand and inflationary pressures, Directors agreed that an easing of monetary policy would be desirable to promote business investment and support the medium-term diversification objective. They stressed, however, that moves in this direction should be part of a broader effort to achieve a better balance between fiscal and monetary policies, and should be made only as demand conditions permit. To facilitate a better coordination of monetary and fiscal policies, Directors saw merit in the proposal of adopting the domestic budgetary balance as the main measure of the fiscal stance.

Directors considered that Botswana's exchange rate arrangement and inflation objective continue to constitute an appropriate framework for ensuring financial stability. A number of Directors saw scope, however, to further improve the transparency of the framework. Directors noted, that adherence to the framework was tested during 2001 and early 2002 by significant swings in regional currencies, which had resulted in an erosion of competitiveness. They underlined the need for close monitoring in the period ahead. Directors also underscored that continued structural reforms to lower domestic costs, as well as wage moderation, will be key to strengthening competitiveness.

Directors commended the authorities' commitment to structural reforms aimed at promoting private sector activity, and welcomed in particular their efforts to address shortages of skilled labor, make more serviced land available to the private sector, and update their privatization policy. They also encouraged the authorities to consider turning over to the private sector some of the projects anticipated under the National Development Plan. Directors noted that the quality of banking supervision is adequate, and welcomed the authorities' plan to review supervision of the nonbank financial sector in view of the recent rapid growth in this area. They also recommended that the authorities enhance their supervisory capacity over banks in the international financial services center. Directors commended the efforts to combat money laundering and the financing of terrorism, and encouraged them to follow up on recent Fund technical assistance in this area.

While welcoming Botswana's commitment to good quality statistics, Directors urged stronger efforts to reduce reporting lags and better harmonize data in the various macroeconomic accounts. Some Directors also encouraged the authorities to give a higher priority to the collection of timely data on poverty indicators.



**Public Information Notices (PINs)** are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board.

**Botswana: Selected Economic Indicators**

	1998	1999	2000	2001
<b>Output and prices (Change in percent) 1/</b>				
Real GDP	4.1	8.1	9.2	1.2
<i>Of which:</i> Private nonmining GDP	8.3	6.2	3.1	6.0
Consumer prices (period average)	6.5	7.8	8.5	6.6
<b>Investment and savings (percent of GDP) 1/</b>				
Gross investment	33.5	26.9	17.0	20.1
Public investment	14.5	13.4	11.5	11.7
Private investment	19.1	13.5	5.5	8.4
Gross domestic savings	43.6	39.2	37.4	36.1
Public domestic savings	15.8	11.8	14.0	13.4
Private domestic savings	27.8	27.4	23.3	22.7
<b>Central government finance (percent of GDP) 2/</b>				
Total revenue and grants	36.2	49.0	49.8	40.7
Total expenditure and net lending	42.3	42.7	40.7	43.0
Overall government balance (excluding grants)	-6.7	5.8	8.9	-2.6
Overall government balance (including grants)	-6.0	6.3	9.1	-2.4
Primary balance (including grants)	-5.6	6.7	9.4	-2.1
Total public debt outstanding	9.4	10.3	8.9	8.0
<b>Money and credit</b>				
Money and quasi money (end year; percent change)	39.4	26.3	1.4	31.2
Bank of Botswana lending rate (end year; in percent)	12.5	13.3	14.3	14.3
<b>External sector (millions of U.S. dollars)</b>				
Trade balance	78	785	905	663
Current account balance	205	618	547	389
Gross official reserves	5,941	6,229	6,319	5,897
<b>Exchange rates</b>				
Botswana pula per U.S. dollar (period average)	4.2	4.6	5.1	5.9
Real effective exchange rate (1990=100)	96.6	102.4	106.3	115.5

1/ National accounts year beginning July 1; figures for 2001 are estimates..

2/ Fiscal year beginning April 1