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Securities

2016 BUDGET SPEECH SYNOPSIS

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Introduction

The Minister of Finance and Development Planning, Honourable Kenneth Matambo, delivered the 2016/17 Budget Speech to the National Assembly on 1 February 2016. The 2016/2017 budget marks the end of the tenth 'National Development Plan' (NDP 10) and the transition to NDP 11; from Vision 2016 to Vision 2036; and United Nations Millennium Development Goals (MDGs) to Sustainable Development Goals (SDGs). According to the Minister, top national priorities to be addressed through the 2016/2017 budget are economic growth, employment creation and poverty eradication. Therefore, resources were proposed for allocation to infrastructure development to address the challenges of inadequate water and electricity supply; social infrastructure to address existing backlogs of classrooms and health facilities; and land servicing to facilitate business opportunities.

Global Economic Review

The year 2015 was characterised by a slowdown in global economic performance, underpinned by declining commodity prices and financial market volatility. Growing economic imbalances in major emerging markets such as China, Brazil and Russia further weighed down global growth rates. According to the 'World Economic Outlook' released by the International Monetary Fund in January 2016, growth in the global economy decreased to 3.1% in 2015, compared to the 3.4% registered in 2014. Against this backdrop, however, world output growth is expected to improve to 3.4% in 2016 on the back of the strengthening of growth in emerging markets and developing economies.

Regional Economic Review

The Minister asserted that the economic performance of the Southern African Development Community (SADC) region mirrors that of the global outlook. Growth in the SADC region is expected to have averaged 3.9% during 2015, compared to 4.6% recorded in 2014. Inflation in most SADC Member States eased in 2015, remaining below the region's target rate of 7.0%, with the exception of Malawi and Zimbabwe. Overall, inflation within the region is expected to have been stable at 5.6% during 2015; the same rate was recorded in 2014.

Gross Domestic Product

The slowdown of growth in the global economy, particularly in the major markets for Botswana's diamonds, had an immense contagion impact on the domestic economy. Sales of rough diamonds dropped sharply, prices consequently fell and as a result production of diamonds was reduced in alignment with market demand, contributing to the slow growth in the domestic economy. The domestic economy declined by 3.5% in Q3 of 2015, pulling down the 2015 growth estimate from 2.6% to 1.0% (2014: 3.2%), mainly attributable to the 14.0% decline in the mining sector. The Water and Electricity sector also registered a decline of 104.0%. Nonetheless, a modest recovery in the domestic economy is expected in 2016 and 2017, with growth rates projected to be 4.2% and 4.3%, respectively, mainly driven by recovery in both the mining and non-mining sectors. The mining sector, which accounts for 25.0% of domestic output, is forecast to grow by 0.6% in 2016 and a further 0.7% in 2017. Conversely, the non-mining sector, is expected to grow by 4.7% and 4.9% in 2016 and 2017, respectively, compared to the 3.9% recorded in 2015. Domestic policy initiatives such as the Economic Stimulus Programme are expected to support higher GDP growth in 2016.

Monetary Policy and Inflation

Consistent with the inflationary outlook, the Bank Rate was reduced from 6.5% at the beginning of the year to 6.0% in August 2015 with the expectation of lowering the cost of borrowing for investment in Botswana. Over the four quarters in 2015, the average year-on-year inflation rate fell from 3.8% in 2014 to 3.1% in 2015, mainly due to the decrease in fuel prices, which were adjusted downwards in February, August and December 2015, following a decrease in global crude oil prices. It is anticipated that this trend will continue, thus exerting downward pressure on domestic prices; inflation is therefore forecast to remain within the Bank of Botswana's objective range of 3% - 6% in 2016.

Balance of Payments

The Minister stated that the overall balance of payments for 2015 is estimated at BWP 3.3bn as at November 2015, a decrease from the BWP 11.4bn recorded in 2014. The current account surplus is estimated to fall, from BWP 22.9bn in 2014 to BWP 12.9bn in 2015. Despite the positive contribution of net inflows of receipts from the Southern African Customs Union (SACU) to the current account balance, it is expected to be offset by the trade deficit anchored by the weakening of global demand for rough diamonds.





Foreign Exchange Reserves

Foreign exchange reserves stood at BWP 84.9bn (USD 7.5bn and SDR 5.5bn) in December 2015 - an increase of 7.3% from BWP 79.1bn in the previous year, but due primarily to the depreciation of the BWP against major international currencies. Total amount of reserves in December 2015 - Government Investment Account, amounted to BWP 35.0 bn.

Exchange Rate Developments

The annual review of the Pula exchange rate mechanism (December 2015) saw the current basket weights being maintained at- 50% South African Rand and 50% IMF's Special Drawing Rights (SDR), while the rate of crawl was changed from 0% to an upward rate of 0.38% per annum for 2016. In terms of the bilateral exchange rate movements in 2015, the BWP strengthened against the ZAR by 13.6%, while it weakened against the SDR by 11.6%.

Performance of Public Enterprises

Public Enterprise	Profit/ (Loss) 2014	Profit/ (Loss) 2015
	BWP (m)	BWP (m)
Botswana Development Corporation	-7.8	202.2
Botswana Telecommunications Corporation Limited	0.14	146.8
Botswana Communications Regulatory Authority	48.1	31.7
Botswana Housing Corporation	16.3	9.8
Botswana Savings Bank	12.8	12.2
Water Utilities Corporation	-361.0	-367.0
Air Botswana	-100.0	-165.0
National Development Bank	-86.3	-37.2
Botswana Meat Commission	-9.6	-

Source: 2016 Budget Speech

Development of Vision 2036 and Adoption of Sustainable Development Goals

The development of *Vision 2036* has been launched - with a Presidential Task Team appointed towards the end of 2015 to guide national consultations on the development of the new Vision. The Team is expected to conclude its task in April 2016, with the draft Vision 2036 scheduled for presentation to Parliament in June 2016. The new Vision is expected to be launched in September 2016 to coincide with celebrations for the country's 50th anniversary of independence.

The United Nations adopted the Sustainable Development Goals (SDGs), which will cover dimensions such as climate, income inequality, health and gender equality, will guide the development process for the next 15 years.

Key Thematic Areas for 2016/2017

Investing in Infrastructural Development - All projects for water and electricity will be accorded high priority in the allocation of the budget in 2016/2017. Initiatives such as the construction of the North - South Carrier Water Scheme, and that of a waste water reclamation plant in Mahalapye are currently underway. Regarding energy, efforts continue to be made to address the technical issues facing the Morupule B Power Station. Moreover, to improve on the power generation situation in the country, the Morupule A Power Station is being refurbished, of which once complete should result in an additional output of 132 MW.

Creating Employment Opportunities - Some of the economic activities with potential for creating employment opportunities, which Government will be undertaking during 2016/2017 include, infrastructure backlog eradication, road networks and maintenance, wildlife and tourism initiatives, continued implementation of Economic Diversification Driver (EDD) initiatives, creation of Special Economic Zones (SEZ), as well as regulatory reforms and improving efficiency. The EDD and SEZ are considered important in promoting both domestic and foreign direct investments, thus bolstering growth and creating employment opportunities in the country.

Strengthening Human Capital - Substantial resources will continue to be channelled towards education and training with emphasis on ensuring that the skills and qualifications offered and acquired are more responsive to the needs of the labour market. Government adopted the Education and Training Sector Strategic Plan (ETSSP) in 2015, whose implementation is expected to address the quality of existing Vocational Education and Training programmes as a way of equipping the youth with appropriate skills. Furthermore, regarding the health sector, Government will continue to pursue avenues to improve the standard of health by continuously reviewing the policies and processes of delivering health in the country. One such avenue will be the implementation, in 2016, of the Medicines and Related Products Supply Chain Strategy, which will aim to ensure regular availability and rational use of essential medicines, and provide quality assurance and security of health commodities throughout the supply chain.



Enhancing National Security - Government will continue to make efforts to combat crime and corruption. Regular audits will be conducted in different areas such as: recruitment and promotions processes; acquisition and distribution of drugs; and procurement of medical equipment, to find loopholes within systems. Initiatives to combat security challenges such as cybercrime are being put in place, particularly through provision of capacity building in investigation, intelligence and forensics to strengthen security.

Strengthening Local Governance - The Honourable Minister highlighted Government's commitment to strengthen and foster their operations in providing local services and promoting local participation, as part of the efforts to create employment opportunities and alleviating poverty. Government developed the *Local Economic Development (LED) Framework* in 2015 in recognition of the potential for Local Authorities to drive economic growth. The LED initiative's objective is to enable communities to identify their development challenges and needs; understand their resource endowment; mobilise resources; and take action to grow and diversify their local economies. Furthermore, Government approved the *Strategy on Private Sector Participation in Land Servicing* in April 2015. Government continues to provide social welfare programmes. As at August 2015, a total of 207,385 beneficiaries were registered under temporary relief programmes.

2014/2015 Budget Outturn

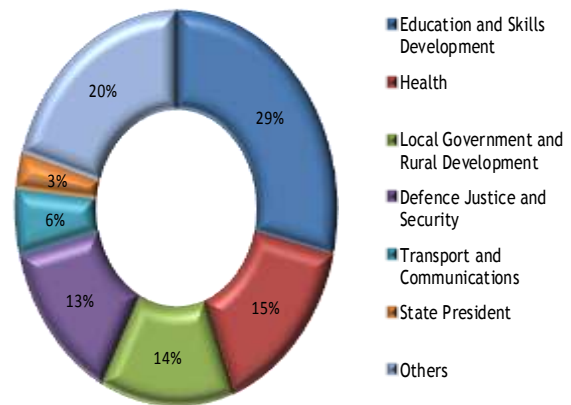
Total revenues and grants for the 2014/2015 financial year were BWP 55.9bn, an 8.46% increase on the revised budget of BWP 51.5bn. Total expenditure and net lending, conversely, declined from the revised budget of BWP 51.3bn to BWP 50.6bn, anchored by under expenditure in the development budget. The overall budget outturn for the 2014/2015 financial year was a surplus of BWP 5.3bn (3.7% of GDP), which is significantly higher compared to a marginal surplus of BWP 280.8m projected in the revised budget for the same year.

2015/2016 Revised Budget Estimates

For the 2015/2016 revised budget, total revenues and grants of BWP 51.8bn represent a 6.5% decrease from the original budget of BWP 55.4bn due to the fall in mineral revenues. Revised total expenditure and net lending for 2015/2016 are estimated at BWP 56.0bn, a 3.3% increase on the original budget estimate of BWP 54.2bn. The overall revised 2015/2016 budget shows a deficit of BWP 4.2bn (2.8% of GDP) compared to the original projected surplus of BWP 1.2bn.

The recommended Recurrent Budget for the 2016/2017 financial year amounts to BWP 36.99bn, 0.8% higher than the current year's original budget of BWP 36.7bn. The budget will be allocated as follows:

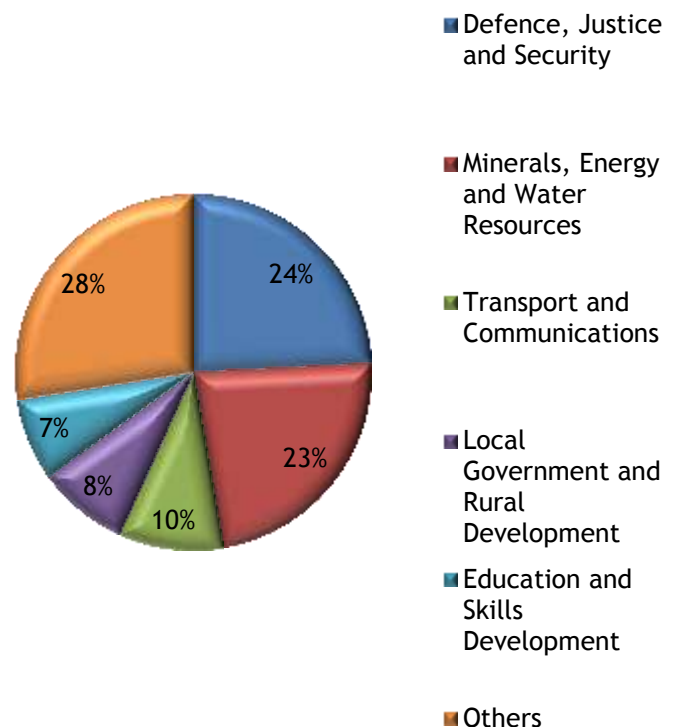
Breakdown of Recurrent Budget



Source: 2016 Budget Speech

The Minister recommended a Developmental Budget of BWP 14.8bn for the financial year 2016/2017. The graph below shows the proposed allocation of the budget.

Breakdown of Developmental Budget



Source: 2016 Budget Speech



Overall Balance

With estimated total revenues and grants of BWP 48.4bn for 2016/2017 financial year, and proposed total expenditure and net lending of BWP 54.44bn, the net result is an estimated budget deficit of BWP 6.1bn (3.8%) of GDP. The deficit will be financed through a combination of drawing down on Government savings, and domestic and foreign borrowing, subject to the analysis of the opportunity cost of each of these financing instruments.

Conclusion

In our view, the proposed budget will have minimal effect on the stock market. Given the sluggish economic conditions, the resultant slowdown in economic growth has put pressure on corporate earnings. However, against this backdrop, there are prospects of improved market activity as global diamond markets are forecast to stabilise. We expect the economy to be more stable in 2016, as Botswana benefits from the sound macroeconomic buffers built up in past years along with political stability. Government's intention to finance the budget deficit through the issuance of bonds and drawing from government reserves, will anchor economic stability. Furthermore, we believe that the highly anticipated Economic Stimulus Package will bolster economic growth and stimulate domestic activity. In our view, the economic recovery will have a knock-on effect on the stock market, thus, strengthening trading activity.

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