Summary:

Botswana

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Issuer Credit Rating	A-/Stable/A-2

Key Rating Factors

Institutional and economic profile	Flexibility and performance profile
We expect diamond production will remain the key factor behind economic growth. • We expect diamond production will expand moderately in 2019-2022, supporting average real GDP growth of 4.2%. • We believe economic diversification will remain limited over the forecast horizon through 2022, potentially exposing Botswana to external shocks from diamond price volatility. • Parliamentary elections in the fall of 2019 will drive domestic policy in the coming months.	Botswana continues to maintain strong external buffers and a accommodative monetary and fiscal policy. • We anticipate Botswana's current account will remain in surplus over 2019-2022, albeit lower than we previously projected. • We expect the budget deficit will widen in 2019, but anticipate fiscal consolidation from 2020. • Inflation is set to remain near the lower end of the Bank of Botswana's 3%-6% target range over the forecast horizon.

Outlook

The stable outlook on Botswana reflects S&P Global Ratings expectation that the country's strong external buffers will continue to shield the economy from potential diamond sector volatility, and that the government's track record of prudent fiscal policies will continue.

We could lower our ratings on Botswana if, contrary to our expectations, the government's fiscal consolidation efforts in the coming years fail, and debt rises significantly. A material weakening of the external position could also put pressure on the ratings. Both fiscal and external pressures could stem from reduced production or global demand for diamonds.

We could raise the ratings on Botswana if the economy's growth rates significantly outperform those of peers at a similar stage of economic development, or if its economic structure were to diversify more significantly. However, we think that this scenario is highly unlikely over the next two to three years.

Rationale

Our ratings on Botswana reflect the country's stable institutional framework; its comparably high income levels attributable to diamond mining, which is potentially susceptible to external volatility; and its strong net external asset position. The ratings are supported by a track record of fiscal prudency and low government debt levels. Our ratings also take into account Botswana's crawling peg exchange rate arrangement, which anchors stability but somewhat constrains monetary policy flexibility.

Institutional and economic profile: Sound diamond production remains the key growth driver and parliamentary elections coming up in 2019 will dominate the policy agenda

We project Botswana's economy will expand by 4.2% in 2019, down only slightly from 4.5% in 2018. An expansionary fiscal stance ahead of the general elections in October 2019 should support this growth. Public sector salary increases should further underpin consumption growth, alongside investments in public infrastructure, for example important bridges. While we expect strong domestic demand this year, we also expect diamond output will increase at a moderate rate. That said, the country's most important economic sector is likely to benefit from resilient global demand, but price trends and demand for diamonds are highly susceptible to external factors, for example demand in the U.S. or China as key markets. We note that the global diamond market is historically volatile, which is why we view Botswana's economic concentration as a key risk--not least because global consumer preferences might evolve over time.

Botswana's natural wealth as one of the world's largest rough diamond producers has seen it emerge rapidly over the past few decades to middle-income status. We estimate GDP per capita of about $8,000 in 2019. Botswana's governments have contributed to this development by managing this wealth prudently, for example by accumulating sizable savings.

Diamond production accounts for 90% of goods exports and exposes the country to trade shocks. Debswana, a 50-50 joint venture between De Beers and the Botswana government, is the main producer of diamonds in Botswana in its Orapa and Jwaneng mines--the latter being the world's most valuable diamond mine. Debswana is investing into expanding operations, for example with the Cut 9 project at Jwaneng, which extends the mine's lifespan to 2035. Overall, we believe that diamond production in terms of carats recovered is set to increase at a moderate rate over the next few years.

De Beers and the government will negotiate a new sales agreement, with the current one expiring in 2020. We expect the two parties will continue their longstanding relationship. In the new agreement, Botswana's government will likely aim to increase local job creation along the diamond value chain to support economic diversification. That said, we think that progress will remain slow. Botswana could also build on established sectors, for example in tourism or meat production to support diversification. Although the non-mining private sector showed robust growth in 2018, the limited diversification is also mirrored in high youth unemployment, well above the 18% for the country as a whole.

Botswana has been a regional role model for efficient and stable institutions, which also have a track record of focusing on sustainable public finances. The government's focus on job creation will play an important role in the campaign for the October 2019 elections. In our view, it looks likely that President Masisi will remain in office. We do not expect any significant policy shifts following the elections, apart from a significant tightening of fiscal policy, not least because the president has recently been able to affirm his leadership in the Botswana Democratic Party, which was recently contested from within the party.

Flexibility and performance profile: Botswana maintains strong external buffers amid moderate fiscal stimulus in 2019

We now project Botswana's general government budget will post a deficit of 3% of GDP in fiscal year 2020 (fiscal year ends March 31, 2020), wider than our previous assumption of a deficit of 1.2%. This reflects our expectation of a further increase in government spending this year ahead of the upcoming October elections. We think that the government will increase both recurrent spending, for example on personnel, and capital expenditure. We maintain our previous assumption that the authorities will again tighten fiscal policy and return to a balanced budget by 2021. This assumption reflects the government's track record of prudent fiscal policies and successful consolidation. Sustained improvements in tax administration and collection could support revenue, but part of the projected fiscal consolidation will likely result from cuts to investment expenditure, as was the case previously.

The authorities will face lower mineral revenue due to Debswana's sizable investment projects at the Jwaneng (Cut 9)] and Orapa (Cut 3) mines, with the government agreeing to reinvest dividends in order to finance the projects. Mineral revenue accounts for over one-third of total government revenue. Receipts from Botswana's membership in the Southern African Customs Union (SACU) account for another quarter of revenue. Both of these significant revenue sources are potentially volatile due to price swings in international markets, changing trade patterns, and economic developments in neighboring South Africa.

We anticipate the government will continue to finance its deficits partly by drawing down on its sizable liquidity buffers, and only partly via domestic or concessional borrowing. Hence, we project gross general government debt relative to GDP will decline further to about 11% by 2022. Government debt net of liquid assets will be about 1% of GDP on average in 2019-2022 following years of a net asset position (government liquid assets exceeding government debt). About 56% of gross government debt is external, dominated by multilateral and bilateral lenders, while the remaining 44% is domestic debt. Interest-servicing costs are therefore low at below 2% of revenues. We also estimate that contingent liabilities from the financial and nonfinancial public sectors are limited.

We expect that robust diamond sector output will continue to bolster export revenue and sustain current account surpluses, averaging 3% of GDP over 2019-2022. These will keep gross external financing needs--current account payments plus short-term external debt at the end of the prior year plus long-term external debt maturing within the year--contained at a moderate 63% of current account receipts plus usable reserves over the same period.

In addition to diamonds, which drive the positive trade balance, Botswana's tourism sector has substantial growth potential and tourism exports account for about 15% of total exports. On the other hand, SACU receipts, at about 9% of GDP, could decline in the medium term.

Recurrent current account surpluses support Botswana's strong external balance sheet. We project its liquid external assets will exceed external debt by 40% of current account payments by 2022, down from 53% in 2018. Botswana's foreign currency reserves were Botswana pula (BWP) 71.4 billion ($6.7 billion) as of Dec. 31, 2018, of which BWP47.5 billion ($4.4 billion) is in the Pula Fund. The Pula Fund is a sovereign wealth fund established in 1994 with the intention of saving some diamond export receipts for future generations.

Botswana operates a crawling peg for the pula against the South African rand and the International Monetary Fund's special drawing rights--a basket of major currencies. The peg helps the Bank of Botswana, the central bank, control inflation, which we expect will remain near the lower end of the bank's 3%-6% target over the next two-to-three years. We therefore expect the central bank will continue with its accommodative monetary stance.

The Botswana banking sector remains resilient, with stable profitability and asset quality metrics. Private-sector credit continues to recover, but at a moderate pace. Credit to private enterprises and households recorded a year-on-year expansion of 7.4% in 2018 compared with 5% growth in 2017. In our view, concentration in the household lending segment remains a key credit risk for banks, accounting for two-thirds of total lending. We think contingent liabilities stemming from the banking sector are limited, given that the sector is largely dominated by well-managed South African banks and public sector banks account for about 2% of total market share. Despite the dominance of foreign banks, banks have relatively limited reliance on external funding, since they are largely funded by domestic customer deposits.

The central bank has broad operational independence and the crawling peg exchange rate regime provides a stability anchor. Nevertheless, the currency peg, along with the narrowness of the economy and local debt markets, limits the country's monetary policy options. We therefore equalize our local currency and foreign currency ratings on Botswana.

We equalize the ratings on the Bank of Botswana with our ratings on the sovereign, given that we consider monetary authorities as analytically inseparable from the sovereign.

Key Statistics

Table 1

Botswana Selected Indicators

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Economic Indicators (%)										
Nominal GDP (bil. BWP)	125.2	145.9	146.1	170.6	180.1	189.9	205.6	222.8	241.2	261.1
Nominal GDP (bil. $)	14.9	16.3	14.4	15.6	17.4	18.6	19.0	20.2	21.5	23.3
GDP per capita (000s $)	7.0	7.5	6.5	7.0	7.6	8.0	8.0	8.3	8.7	9.2
Real GDP growth	11.3	4.1	(1.7)	4.3	2.9	4.5	4.2	4.2	4.1	4.1
Real GDP per capita growth	9.3	2.2	(3.5)	2.4	1.0	2.4	2.2	2.2	2.1	2.1
Real investment growth	2.0	1.5	8.8	3.6	(8.8)	6.8	5.0	4.4	4.2	4.2
Investment/GDP	28.9	26.4	28.9	27.9	26.2	29.8	29.7	29.9	30.0	30.1
Savings/GDP	36.6	37.1	31.1	35.7	31.6	31.6	32.3	32.0	33.2	34.3
Exports/GDP	61.5	60.7	53.0	49.8	40.0	39.4	37.8	36.3	35.2	34.2
Real exports growth	37.8	7.7	(16.3)	0.4	(10.9)	4.1	1.5	1.9	3.0	3.0
Unemployment rate	20.0	20.0	17.7	17.7	17.7	17.7	17.7	17.7	17.7	17.7
External indicators (%)										
Current account balance/GDP	7.6	10.7	2.3	7.8	5.4	1.9	2.6	2.2	3.2	4.2

Table 1

Botswana Selected Indicators (cont.)

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Current account balance/CARs	10.4	15.0	3.5	12.6	10.5	3.7	5.5	4.8	7.3	9.9
CARs/GDP	73.3	71.3	63.9	62.0	51.2	49.9	47.1	45.0	43.6	42.4
Trade balance/GDP	(0.6)	4.6	(4.7)	9.4	4.7	1.7	1.3	1.0	1.1	1.2
Net FDI/GDP	2.1	2.5	1.4	(0.3)	1.0	0.6	0.4	0.4	0.4	0.4
Net portfolio equity inflow/GDP	(7.8)	(1.9)	(7.6)	(0.9)	(2.0)	0	(2.5)	(2.5)	(2.5)	(2.5)
Gross external financing needs/CARs plus usable reserves	56.5	54.6	54.6	52.8	54.5	58.8	60.2	62.0	63.3	63.8
Narrow net external debt/CARs	(50.3)	(54.0)	(62.5)	(54.1)	(63.2)	(51.1)	(48.4)	(44.6)	(39.8)	(36.2)
Narrow net external debt/CAPs	(56.2)	(63.6)	(64.7)	(61.9)	(70.6)	(53.1)	(51.3)	(46.9)	(42.9)	(40.1)
Net external liabilities/CARs	(47.7)	(52.6)	(65.6)	(56.9)	(67.4)	(64.0)	(65.9)	(63.7)	(62.0)	(61.7)
Net external liabilities/CAPs	(53.2)	(61.9)	(68.1)	(65.1)	(75.4)	(66.4)	(69.8)	(67.0)	(66.9)	(68.5)
Short-term external debt by remaining maturity/CARs	6.5	6.1	7.5	6.5	8.9	10.0	10.4	11.0	11.5	11.7
Usable reserves/CAPs (months)	9.4	9.4	11.2	10.7	10.8	10.1	9.4	9.0	8.4	7.9
Usable reserves (mil. $)	7,726.1	8,322.8	7,546.1	7,188.8	7,490.5	6,652.8	6,465.5	6,076.2	5,874.4	5,893.5
Fiscal indicators (general government; %)										
Balance/GDP	5.8	3.7	(4.8)	0.7	(1.1)	(2.5)	(3.0)	(0.2)	0.3	0.4
Change in net debt/GDP	(4.3)	(5.3)	1.6	3.3	(1.7)	2.5	3.0	0.2	(0.3)	(0.4)
Primary balance/GDP	6.3	4.1	(4.2)	1.2	(0.6)	(2.0)	(2.5)	0.3	0.8	0.8
Revenue/GDP	39.1	38.3	32.5	33.7	31.3	29.0	30.0	31.0	31.0	31.0
Expenditures/GDP	33.3	34.7	37.3	33.0	32.4	31.5	33.0	31.2	30.7	30.6
Interest/revenues	1.4	1.3	1.7	1.5	1.8	1.6	1.6	1.7	1.5	1.4
Debt/GDP	18.2	17.4	17.9	15.8	13.6	13.7	14.8	13.4	12.1	10.8
Debt/revenues	46.6	45.5	55.2	47.0	43.4	47.2	49.3	43.2	39.0	34.7
Net debt/GDP	(4.7)	(9.4)	(7.7)	(3.3)	(4.9)	(2.1)	1.1	1.2	0.8	0.3
Liquid assets/GDP	23.0	26.8	25.6	19.1	18.4	15.8	13.7	12.2	11.3	10.4
Monetary indicators (%)										
CPI growth	5.9	4.4	3.0	2.8	3.3	3.2	3.4	3.5	3.6	3.6
GDP deflator growth	2.3	11.9	1.9	12.0	2.6	0.9	3.9	4.0	4.0	4.0
Exchange rate, year-end (BWP/$)	8.7	9.5	11.2	10.6	9.9	10.7	10.9	11.2	11.2	11.2
Banks' claims on resident non-gov't sector growth	14.8	14.4	9.0	5.9	4.9	7.3	7.8	8.0	8.0	8.0
Banks' claims on resident non-gov't sector/GDP	34.4	33.7	36.7	33.3	33.1	33.7	33.5	33.4	33.3	33.3
Foreign currency share of claims by banks on residents	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Foreign currency share of residents' bank deposits	13.1	15.5	15.5	16.9	16.0	16.8	16.0	15.5	15.5	15.5

Table 1

Botswana Selected Indicators (cont.)	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Real effective exchange rate growth	2.0	0.6	2.3	1.8	(1.4)	N/A	N/A	N/A	N/A	N/A

Sources: Bank of Botswana, International Monetary Fund (Economic Indicators), Bank of Botswana (External Indicators), Bank of Botswana, Ministry of Finance and Economic Development (Fiscal Indicators), and Bank of Botswana, International Monetary Fund, Bruegel (Monetary Indicators).
Adjustments: None
Definitions: Fiscal year ends March 31 of the following year. Savings is defined as investment plus the current account surplus (deficit). Investment is defined as expenditure on capital goods, including plant, equipment, and housing, plus the change in inventories. Banks are other depository corporations other than the central bank, whose liabilities are included in the national definition of broad money. Gross external financing needs are defined as current account payments plus short-term external debt at the end of the prior year plus nonresident deposits at the end of the prior year plus long-term external debt maturing within the year. Narrow net external debt is defined as the stock of foreign and local currency public- and private- sector borrowings from nonresidents minus official reserves minus public-sector liquid assets held by nonresidents minus financial-sector loans to, deposits with, or investments in nonresident entities. A negative number indicates net external lending. N/A--Not applicable. BWP--Botswana pula. CARs--Current account receipts. FDI--Foreign direct investment. CAPs--Current account payments. e--Estimate. f--Forecast. The data and ratios above result from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information.

Ratings Score Snapshot

Table 2

Botswana Ratings Score Snapshot

Key rating factors	Score	Explanation
Institutional assessment	3	Generally effective policy making in recent years promoting sustainable public finances and economic growth. Cohesive civil society, although discontent regarding high unemployment could rise. There is a generally unbiased enforcement of contracts and respect for the rule of law. Statistics can be subject to large revisions.
Economic assessment	5	Based on GDP per capita (US$) and growth trends as per Selected Indicators in Table 1.
		Concentrated economy, with significant exposure to the diamond industry at above 20% of GDP.
External assessment	1	Based on narrow net external debt and gross external financing needs/(CAR + useable reserves) as per Selected Indicators in Table 1.
Fiscal assessment: flexibility and performance	2	Based on the change in net general government debt (% of GDP) as per Selected Indicators in Table 1
		The sovereign has a potentially volatile revenue base, since mineral revenues account for about 35% of revenues.
Fiscal assessment: debt burden	1	Based on net general government debt (% of GDP) and general government interest expenditures (% of general government revenues) as per Selected Indicators in Table 1
Monetary assessment	4	The pula is a crawling peg. The central bank has operational independence and uses market based instruments such as policy rates to transmit monetary policy to the banking sector and the economy, but effectiveness may be limited not least under the foreign exchange arrangement.
Indicative rating	a-	As per Table 1 of "Sovereign Rating Methodology."
Notches of supplemental adjustments and flexibility	0	
Final rating		
Foreign currency	A-	
Notches of uplift	0	Default risks do not apply differently to foreign- and local-currency debt.

Table 2

Botswana Ratings Score Snapshot (cont.)		
Key rating factors	**Score**	**Explanation**
Local currency	A-	

S&P Global Ratings' analysis of sovereign creditworthiness rests on its assessment and scoring of five key rating factors: (i) institutional assessment; (ii) economic assessment; (iii) external assessment; (iv) the average of fiscal flexibility and performance, and debt burden; and (v) monetary assessment. Each of the factors is assessed on a continuum spanning from 1 (strongest) to 6 (weakest). S&P Global Ratings' "Sovereign Rating Methodology," published on Dec. 18, 2017, details how we derive and combine the scores and then derive the sovereign foreign currency rating. In accordance with S&P Global Ratings' sovereign ratings methodology, a change in score does not in all cases lead to a change in the rating, nor is a change in the rating necessarily predicated on changes in one or more of the scores. In determining the final rating the committee can make use of the flexibility afforded by §15 and §§126-128 of the rating methodology.

Related Criteria

- Criteria - Governments - Sovereigns: Sovereign Rating Methodology, Dec. 18, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- General Criteria: Methodology: Criteria For Determining Transfer And Convertibility Assessments, May 18, 2009

Related Research

- Sovereign Ratings History, April 3, 2019
- Sovereign Ratings List, April 3, 2019
- Sovereign Ratings Score Snapshot, April 2, 2019
- Sovereign Debt 2019: Global Borrowing TO Increase By 3.2% To US$7.8 Trillion, Feb. 21, 2019
- Sovereign Debt 2019: Sub-Saharan African Eurobond Issuance To Moderate After Record Issuance In 2018, Feb. 21, 2019
- Sub-Saharan Africa Sovereign Rating Trends 2019, Jan. 14, 2019
- Botswana 'A/A-2' Long- And Short-Term Ratings Affirmed; Outlook Stable, Oct. 26, 2018
- Default, Transition, and Recovery: 2017 Annual Sovereign Default Study And Rating Transitions, May 8, 2018
- Sovereign Risk Indicators, April 11, 2019. An interactive version is also available at http://www.spratings.com/sri

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