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Botswana
Opportunities for Industrial Development in Botswana: An Economy in Transition

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Southern Africa Department
Industry and Energy Operations Division

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CURRENCY EQUIVALENT

Currency Unit = Botswana pula (BTP)
US dollars/Botswana pula (end period)

1975	1.1500
1980	1.3480
1985	0.4760
1986	0.5442
1987	0.6387
1988	0.5166
1989	0.5341
1990	0.5344
1991	0.4825
1992	0.4431

GLOSSARY OF ABBREVIATIONS

ABCON	Association of Building and Construction Contractors
ACP	Africa, Caribbean, Pacific countries
AFA	Automatic Financial Assistance
ALSP	Accelerated Land Servicing Program
ANC	African National Congress
BAS	Business Advisory Services
BEDU	Batswana Enterprises Development Unit
BCCI	Botswana Chamber of Commerce and Industry
BDC	Botswana Development Corporation
BFTU	Botswana Federation of Trade Unions
BGI	Botswana Game Industries
BHC	Botswana Housing Corporation
BLNS	Botswana, Lesotho, Namibia, Swaziland
BLS	Botswana, Lesotho, Swaziland
BMC	Botswana Meat Commission
BoB	Bank of Botswana
BOCCIM	Botswana Confederation of Commerce, Industry and Manpower
BRIDEC	Brigade Development Center
BSM	Botswana Stock Market
BTechC	Botswana Technology Center
B/ZTA	Botswana/Zimbabwe Trade Agreement
CCU	Common Customs Union
CFA	Case-by-case Financial Assistance
CSO	Central Statistics Office
DAO	Development Approval Order
DFI	Development Finance Institution
DSL	Department of Surveys and Lands
EC	European Community
ECU	European Currency Unit
EPZ	Export Processing Zones
FAP	Financial Assistance Policy
FDI	Foreign Direct Investment
FIA	Financial Institutions Act
FIAS	Foreign Investment Advisory Service
FSC	Financial Services Company Limited
FY	Financial Year
GATT	General Agreement on Tariffs and Trade

GSP	Generalized System of Preferences
HATAB	Hotel and Tourism Association of Botswana
IECC	Industrial Extension Coordinating Committee
ILO	International Labor Organization
LPS	Local Preference Scheme
MCI	Ministry of Commerce and Industry
MFDP	Ministry of Finance and Development Planning
MLGLH	Ministry of Local Government, Lands and Housing
MOH	Ministry of Health
MRWA	Ministry of Mineral Resources and Water Affairs
NBFI	Non-Bank Financial Institution
NDB	National Development Bank
NDP	National Development Plan
NDP7	Seventh National Development Plan
NEMIC	National Employment, Manpower and Incomes Council
NGO	Non-Governmental Organization
NMR	Non-Mineral Revenue
OBU	Off-Shore Banking Units
OECD	Organization for Economic Cooperation and Development
OPIC	Overseas Private Investment Corporation
OSAS	Overseas Services Aid Scheme
PDL	Poverty Datum Line
PDSF	Public Debt Service Fund
PTA	Preferential Trade Agreement
RIDP	Regional Industrial Development Program
RRC	Regulations Review Committee
RSA	Republic of South Africa
RSF	Revenue Stabilization Fund
SACU	Southern African Customs Union
SACUA	Southern African Customs Union Agreement
SADC	Southern African Development Community
SADCC	Southern Africa Development Coordination Conference
SHHA	Self-Help Housing Agency
SIP	Special Incentive Package
SPRDP	Selebi-Phikwe Regional Development Program
SME	Small and Medium Scale Enterprise
thebe	1/100th of a pula
TIPA	Trade and Investment Promotion Agency
UA	Unit of Account
WTO	World Tourism Organization

Botswana	is the country
Setswana	is the language
Motswana	is an individual citizen of Botswana
Batswana	is plural for Motswana

FISCAL YEAR

Government = April 1 to March 31

BOTSWANA

OPPORTUNITIES FOR INDUSTRIAL DEVELOPMENT IN BOTSWANA

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PREFACE

This report was undertaken at the request of the Botswana authorities in recognition of the importance that industrial development plays in the nation's seventh National Development Plan (NDP 7). A greater focus on industrial development has been occasioned by the recognition that the diamond sector is unlikely to provide the stimulus to growth that it has done over the past twenty years -- as well as the need to generate employment opportunities for Botswana's growing labor force and the need to diversify the economic base of the country.

This report has been undertaken on a fully collaborative basis with the Government of Botswana. Work on the report has been undertaken on an equal basis between a World Bank team which visited Botswana twice from February 24 to March 6, 1992 and from October 18 to 31, 1992, in conjunction with a Botswana counterpart team.

The work of the two teams has been guided and fully reviewed by a Reference Group within Botswana chaired by Mr. Tumelo (Deputy Secretary, Economic Affairs in the Ministry of Finance and Development Planning), with members representing a wide range of interests within Botswana including, the Ministry of Finance and Development Planning, the Ministry of Commerce and Industry, the Trade and Investment Promotion Agency, and the private sector through their representative bodies -- the Botswana Confederation of Commerce, Industry and Manpower (BOCCIM) and the Botswana Chamber of Commerce and Industry (BCCI).

The World Bank team was comprised of Simon Bell (task manager), René Bonnel (World Bank country economist for Botswana), and Caroline Doggart, Refael Benvenisti and Charles Krakoff (consultants).

The Botswana counterpart team was comprised of Lebani Cephas, Armand Boucher and Ed Edwards (Ministry of Finance and Development Planning), Thabologo Ndzinge and Fergus Chambers (Ministry of Commerce and Industry) and Tony Jordan (private sector representative).

This work was undertaken within the Industry and Energy Operations Division of the Southern African Department of the World Bank. Mr. David Cook (AF6IE) and Mr. Stephen Denning (AF6DR) are the managing Division Chief and Department Director, respectively. Mr. Ali Mansoor (AFTEF) was the lead advisor and Mr. Pedro Belli (AF6IE) was the peer reviewer for the study. Ms. Adriana Arriagada and Ms. Noemi Dacanay provided secretarial support for the work.

BOTSWANA
OPPORTUNITIES FOR INDUSTRIAL DEVELOPMENT IN BOTSWANA

EXECUTIVE SUMMARY

1. ***Introduction.*** In the period since independence in 1966, economic growth has been maintained at consistently high levels. Whereas Botswana was classified as one of the least developed countries in the world twenty five years ago, by 1992, it was one of the richest countries in Sub-Saharan Africa with a per capita national income of almost $3,000 -- about even with that of its large neighbor, the Republic of South Africa. The growth of GDP over this period averaged between 9 and 10 percent per annum.

2. The major impetus for this rapid development came from the discovery of diamonds in the period immediately after independence. Diamonds rapidly replaced beef and copper/nickel as the major source of export earnings. In addition, the Government's partnership in the De Beers Botswana Mining Company Ltd. (Debswana), has generated large fiscal revenues in the form of taxes, royalties and dividend payments which have led to ongoing Government budget surpluses and the accumulation of substantial public sector savings. At the same time, foreign exchange reserves have grown rapidly and are equivalent to about two years of import cover or 16 months of imports of goods and services.

3. The transformation has indeed been dramatic. Botswana changed from essentially a cattle herding and rural based economy, dependent upon external sources of assistance, to a financially strong middle income country with an increasing dependence on diamond exports and diamond revenues. Whereas only 4 percent of the total population lived in urban centers at independence, by 1990 this had increased to 30 percent. Since independence, the number of university graduates has increased from 22 to 3,100; the amount of tarred roads has increased from 20 kilometers to 2,664 kilometers; the number of workers in formal employment has increased from 14,000 to 222,700. Schooling, health care and the provision of other public services has improved dramatically. The country's infrastructure, which was hardly developed at all during the period when Bechuanaland was a protectorate of the British Government, has improved significantly, with a road system linking the main urban centers, and the extension of dependable water, electricity and telecommunications services to many parts of the country.

4. With one of the consistently fastest rates of growth in the world, coupled with sound macro-economic management by the Government, the transformation which has taken place has been on a scale not seen in many countries. Economic transformation has brought with it a fundamental social transformation, as Batswana have coped with the change from being pastoralists and cattle herders to participants in a strong, dynamic modern economy. This rapid, and fundamental transition in economic and social conditions, is an important backdrop to understanding the process and pattern of development in Botswana as well as its future direction.

5. In spite of the very rapid growth over this period, income distribution remains highly skewed. The fruits of economic growth and social transition have been disproportionately shared among the citizens of Botswana. For example, during the current drought, many rural Batswana have survived on food hand outs from the Government and the international donor community, and life remains difficult and extremely traditional, without the trappings of modern life. However, as indicated in the seventh National Development Plan (NDP 7), Government transfers have been utilized to re-dress the problems caused by the pattern of income distribution. As a result, health facilities are widely available and utilized throughout Botswana, free education up to (and including) secondary level has produced one of the highest rates of literacy in Sub-

Saharan Africa, and road, rail and telecommunications links now make access to remote rural areas much easier. Nonetheless, as also indicated in the plan, it remains important to ensure "that all Batswana have access to the basic amenities of life consonant with human dignity" and share in the fruits of development.

6. Botswana's achievements have appeared even more impressive as they have taken place within a region of the world which has generally experienced prolonged economic stagnation. Growth in many of the neighboring countries of the Southern Africa region has either languished or fallen in real terms, with resultant hardship in those countries. Botswana's experience is consequently unique within the region.

7. However, in the early 1990s, several developments are likely to change the direction of Botswana's future development. *First* among the changes, is the projection in NDP 7, that during the first half of the 1990s, the Government budget will move from a cash surplus to a cash deficit position. The NDP 7 plan period is expected to be a transition period during which the growth in earnings from the diamond sector is expected to taper off -- with a concomitant impact upon the growth in Government revenues from this source. Although similar projections for a transition were made in the previous plan period (NDP 6), a stronger case is made in NDP 7 for this eventuality and the recent decision by Debswana to stockpile diamonds (from September 1992) lends greater credence to this view. The world wide economic recession has also taken its toll on the economy generally, outside of the diamond sector, with a slowdown in business activity during 1992.

8. The *second* change is the rapid economic and political developments which are taking place in the Southern African region -- with imminent political change in the Republic of South Africa, a newly independent Namibia on Botswana's western border, and with other countries in the region pursuing structural adjustment programs which are substantially altering their economies and potentially their trading relationships. The most important change, in this regard, is taking place in South Africa, providing an uncertain future for the Southern Africa Customs Union (SACU) -- the oldest customs union in the world -- which has inextricably linked Botswana to the economies of Lesotho, Swaziland and RSA since 1910. In addition, there are changes in world wide relationships which have led to the establishment of a North American Free Trade Agreement and closer links between the countries of Europe through the European Community. Such developments are likely to lead to changes in trading relationships for Botswana, in ways which are still unclear.

9. *Last*, the sheer magnitude of the change that has taken place in Botswana over the past twenty six years has meant that Botswana now has a substantially more complex and sophisticated economy. Government policies need to adjust accordingly. Whereas Botswana was pre-occupied in the post independence period with providing basic infrastructure and basic social services to its growing population, and developing Government institutions to oversee and assist in the management of various aspects of the economy -- by the 1990s monetary policy, fiscal policy, and the entire role of Government have become substantially more complex.

10. These three fundamental developments have lent a greater sense of urgency to two concerns to which the Government has, for some years, been sensitive. The first of these is a need to create employment opportunities for its population -- and the second, is the need to diversify the economic base away from its growing reliance upon the diamond sector. These concerns involve a careful balance between generating employment opportunities in both rural and urban areas, and ensuring that rural development takes place at a rate that will avoid

excessive rural-urban migration. Despite the rapid urbanization which has taken place since independence, the Government has so far been successful in generating employment opportunities for a growing workforce and for additional rural immigrants to urban areas -- while also significantly reducing overall levels of unemployment.

11. The Government views the development of the industrial sector (manufacturing and service sectors), as an important answer to these twin objectives of employment creation and economic diversification. Prominence has been given in NDP 7 to the development of industry, and this report constitutes an important element in the debate as to how to create sustainable economic opportunities in this sector. Botswana has the luxury of financial resources to assist in ameliorating the disadvantages which do exist in promoting industrial development -- while amplifying its advantages. This report focuses on how Botswana can best utilize its financial resources, in combination with its other advantages, to ensure the development of a sustainable industrial base.

12. ***Botswana's Industrial Structure***. In line with overall rapid growth in the economy, the industrial sector (manufacturing, construction, commerce, financial and business services) in Botswana has also experienced rapid growth -- with the growth rate for these sectors averaging about 8.7 percent per annum in real terms over 1982 to 1991.

13. In the overall economy, employment has grown roughly in proportion to GDP. From 1982 to 1991, total formal employment grew from 100,200 to 222,700 -- 9.2 percent per annum -- compared to real GDP growth of 8.1 percent per annum over this same period. Employment in the industrial sector has grown faster than in the economy as a whole -- increasing at an annual average rate of 11.7 percent per annum. Over 1982 to 1991, total employment in this sector grew from 43,100 to 117,000. Highest growth rates were experienced in manufacturing (15.3 percent per annum) and finance and business services (12.3 percent per annum).

14. Botswana has a minimum wage which has eight differing categories and five different minimum wage levels. Average wages have been increasing rapidly. Although from 1980 to 1986 there was a decline in real earnings in many sectors, between 1986 and 1991 there was very rapid growth, reflecting better conditions in the diamond sector -- real increases over this period range from 5.7 percent to 12.9 percent. This demonstrates the strong connection between wage levels and the growth of the mineral resource driven economy. It also has important implications for the development of labor intensive industries. With one of the highest levels of per capita national income in Africa, it will be difficult to keep wages sufficiently low to compete with other countries in the region in attracting labor intensive manufacturing industry.

15. Although it is difficult to quantify, evidence from some manufacturing industries appears to confirm the generally held view that levels of productivity are low by the standards of both the region and the world as a whole. This has been a general concern of Government and investors alike which has been so pronounced that the Government has established a National Productivity Center to address this particular problem in both the public and the private sectors. Low levels of labor productivity mean that Botswana's comparative advantage in labor intensive activities is further eroded. Consequently, realigning wages and productivity is of vital concern to policy makers.

16. The Government has attempted to promote citizen involvement in industrial development, by reserving certain activities for Batswana -- manufacture of school uniforms, school furniture,

burglar bars, protective clothing, cement and baked bricks, and the milling of sorghum and the baking of bread The Government is also committed to rural industrial development and considers industrialization an important component of its rural development strategy. In this regard, tourism has been identified as an industry with potential to contribute to rural development and employment creation -- nearly 70 percent of employees in tourism are located in rural areas and 40 percent of all jobs in the north west of Botswana are linked to tourism.

17. Unfortunately, the available data on the industrial sector do not provide a comprehensive picture of the sector. It is therefore important that Botswana should conduct an industrial census so that future policy decisions pertaining to the sector are based on a more solid understanding of the composition of sub-sectors involved in industry, sub-sectoral employment levels, profitability of differing types of industry, and so on. All the evidence, nonetheless, points to strong growth over the past decade in most areas of industrial activity.

18. Up to the present, industrial sector growth has largely been based on domestic sales rather than production for export. If predictions made in NDP 7 are correct, and the growth in domestic demand halves over the first half of the 1990s, then the industrial sector will need to look to other markets to promote growth. The easier domestic markets have been addressed and, with rapid increases in income over this period, consumers are developing more sophisticated demands. Consequently, the stimulus which gave rise to industrial growth in Botswana in the 1980s may no longer be present. This implies a need to re-examine industrial promotion policies to ensure that they assist the development of more outward looking, export-oriented industries; the further development of service oriented industries; the identification of additional niche markets; and higher quality production.

19. Future industrial development policies need to focus on achieving higher levels of productivity, lower labor intensity in production, higher skilled employees, and better quality products -- in order to meet competitive pressures in domestic and international markets. Given Botswana's current level of development and per capita national income, it may also be more appropriate to try to move quickly up the industrial development ladder toward the production of higher value, better quality products. With wages inevitably driven upwards by the enclave diamond sector, Botswana may find it increasingly difficult to compete in the production of low value, high labor content products.

20. In addition, the available data indicate that formal sector employment has been growing faster than the increase in the labor force, implying a reduction in the unemployment rate. This is likely to have been off-set, to some extent, in 1992, by the effects of the international recession on business activity in Botswana. However, as unemployment levels have been declining, then the pressure to focus on the employment of large numbers of unskilled workers may be less intense, and more emphasis can alternatively be placed on increasing, skills, quality and productivity -- implying a commensurate change in emphasis in industrial development policies.

21. Nonetheless, in order to assist the authorities to make better informed policy decisions with respect to industrial development strategies, wage levels and employment, it will be necessary to develop better and more timely information on labor market activity. Currently unemployment data are only collected sporadically, information on productivity is mainly anecdotal, and the interrelationships between the formal, informal and traditional agricultural sectors are not well known. A better understanding of these relationships, based upon more accurate data will be important. For example, current trends indicate a significant decline in unemployment rates over the 1980s -- however, the ability of the economy to maintain

unemployment at current levels will depend upon numerous factors including overall economic growth, rural-urban migration, Government policy towards rural areas and informal activities, and movement between informal and formal employment. Although the economy is unlikely to continue generating jobs at the rate of ten percent per annum as it has done over the recent past, a lower rate of growth in employment may still lead to further reductions in the overall rate of unemployment. A better understanding of the dynamics between these various markets is therefore important to assist policy makers choose the most appropriate policies.

22. ***International Trade and Foreign Investment.*** Botswana's trading relationships have largely been influenced by its long standing membership in the Southern African Customs Union (SACU) -- and to a lesser extent by its relationship with Zimbabwe. SACU has allowed for a common external tariff, duty free access within the customs union area and rights of transit across RSA territory for the five participating members of the agreement -- South Africa, Botswana, Swaziland, Lesotho and -- more recently -- Namibia.

23. SACU was renegotiated in 1969 to take into account the "price raising effects", "industrial polarizing effects" and "loss of fiscal discretion" caused by the agreement on the smaller members of the union. This renegotiation, led to a dramatic increase in Botswana's customs union receipts from R3 million in 1967 to R50 million in 1975 -- an increase from about 20 percent to 50 percent of Government's total revenues.

24. All the participating members involved in SACU became discontented with the agreement during the latter part of the 1970s and attempts were made again to alter the agreement -- but no satisfactory conclusions were reached and the agreement remained unchanged throughout the 1980s. Botswana, Lesotho, Namibia and Swaziland (the BLNS countries) essentially contended that they were still inadequately compensated by South Africa for membership in the customs union. They were also concerned about the serious time lags in the distribution of revenue, which accrue to South Africa, and are not paid out in full for two years. Last, they were concerned that membership of SACU polarized industrial development in South Africa to the detriment of the BLNS countries.

25. The future of SACU remains unclear. The current South African Government has indicated that SACU is becoming financially unaffordable and that it would like a change in the arrangements. Meanwhile, the ANC has indicated that the Government should not make major economic policy decisions prior to its involvement in such processes. Despite the on-going uncertainty over the agreement, during the 1992/93 financial year, Botswana is estimated to receive R1,300 million -- 24 percent of total revenues -- from this source. This represents the Government's second most important source of income after the diamond sector.

26. The other major trade agreement of note is the Botswana/Zimbabwe Trade Agreement. However, in the early 1980s, this agreement also became strained with the relocation of many Zimbabwean companies to Botswana, immediately after Zimbabwean independence, targeting exports back into the Zimbabwean market. In addition, some Botswana manufacturers felt that they were injured by dumping from Zimbabwe. The recent major devaluation of the Zimbabwe dollar, as a consequence of the structural adjustment program in that country, has substantially impaired Botswana's ability to export to that market.

27. Other important trade arrangements include the Lomé Convention -- which provides Botswana with a liberal beef quota, at higher than otherwise obtainable prices -- and the

Generalized System of Preferences. Botswana is not a member of GATT or PTA -- but participates actively in SADC.

28. Over the 1980s, Botswana's exports were increasingly dominated by diamonds -- accounting for 80 percent of exports in 1990 compared to 60 percent in 1980. On the other hand, most imports come from South Africa under SACU. African imports (mainly from South Africa) accounted for 86 percent of Botswana's imports in 1989, while more than 80 percent of its exports were directed outside of Africa. Hence, Botswana has become a major source of hard currency for the region as a whole. This may mean that Botswana can exert an influence on the future direction of regional trade and related economic relationships larger than its economic size might suggest.

29. External sources of capital have also played an important role in Botswana's growth -- in terms of both foreign investment and external aid. Most foreign investment comes from South Africa as a consequence of the close links between the two economies and the attractiveness of the Botswana setting. Most of this foreign investment has been in mining -- mainly from Anglo-American and De Beers. Non-mining foreign investment has also mainly come from South Africa and has been attracted by subsidy and tax breaks under the Financial Assistance Policy (FAP) scheme and other promotion programs.

30. A comparison of Botswana with other countries in the region indicates that Botswana has been particularly successful in attracting foreign investment. With less than 1.5 percent of the SADC region's population, it produces 9 percent of the combined GDP (1989) and has attracted 52 percent of the incoming direct foreign investment (over 1985-89). Meanwhile, there has been strong dis-investment from the South African economy.

31. The future political and economic situation in the region, and its impact on trading relationships, remains unclear. Many possible outcomes can be contemplated -- regional fragmentation, continuation of the two subgroupings SACU and SADC, gradual full regional integration, or an amalgamation of SADC and SACU. Whatever the ultimate outcome, it is clear that Botswana must strive to meet, at least, the test of regional competitiveness, and ideally, the more strenuous test of international competitiveness. Consequently, Botswana's industrial development policies should be based upon promoting productive efficiency rather than protected, or otherwise subsidized, inefficiency.

32. ***Advantages and Constraints to Industrial Development in Botswana.*** Botswana has many advantages for foreign investors, many of which are possibly not well known to investors from outside of the region. These include: democracy, stability and security; access to markets -- SACU, SADCC, Lomé, GSP; responsible fiscal policy which has led to the accumulation of substantial Government surpluses; effective monetary policy which includes effective exchange rate management and minimal controls over foreign exchange transactions; reliable utility services; a Government which is committed to increasing the quality of human capital at a rapid rate; and freedom to produce, market and finance. It is necessary for Botswana to build upon these advantages -- which are certainly not insubstantial -- in aggressively promoting industrial development.

33. There are also, however, many constraints -- although the Government has already taken some measures to address these problems following the recommendations of the Revised Incomes Policy of 1990. A common complaint of industrialists operating in Botswana is the high cost of

utilities. Power, is at least twice as expensive as in Zimbabwe and South Africa; Botswana's water prices are 10 times those of Zimbabwe and 2½ times those of South Africa; telecommunications differentials are up to twice those in neighboring countries. Against this, however, one must consider the reliability of supply in Botswana and the lower increases in prices which have been experienced in Botswana in the recent past. Bad policy with respect to the pricing of utilities in some neighboring countries is having an adverse impact which is likely to increase prices much faster than in Botswana, with inevitable industrial dislocation.

34. Nonetheless, the utility parastatals should strive to increase efficiencies within their organizations and to adopt, wherever possible, a more pragmatic approach to the importation of utilities. For example, the region is a surplus power producer, with South Africa, Zimbabwe, Zambia and Mozambique, all having the potential capacity to export relatively cheaper electricity into the Botswana market. These possibilities should be aggressively investigated as a means of meeting future increases in domestic demand and reducing average utility costs.

35. A further constraint is the high level of wages combined with a low level of productivity -- which has reduced Botswana's attractiveness as a potential investment market. Although every attempt must be made to bring wage levels more into line with productivity, while simultaneously trying to increase overall levels of productivity, wage levels are likely to continue to be driven by Botswana's relatively high per capita national income -- resulting in higher wage levels than would otherwise be the case in an economy without such a historically healthy natural resource sector.

36. The availability of land for industrial development and housing has also acted as a major constraint on the development of the sector. The Government has attempted to address this problem by embarking on an ambitious Accelerated Land Servicing Program in 1987. Although this has had a positive impact on site availability, present indications are that the supply of industrial sites will continue to fall far short of demand over the foreseeable future unless further positive steps are taken to redress this imbalance.

37. The regulatory framework has also acted as a constraining influence. Problems exist with respect to (a) work and residence permits for expatriates, (b) industrial and commercial licenses, (c) land board regulations, and (d) the employment act and labor policy. Although attempts are being made to rectify these problems, and although important advances have been made throughout 1991 and 1992 in terms of streamlining procedures and removing some controls, this remains a continuing, albeit declining, constraint.

38. In addition, long term finance is generally perceived by the private sector to be a constraint, although this may in part reflect a long period of negative real interest rates. Commercial banks are relatively long term lenders compared to similar institutions in neighboring countries and the Botswana Development Corporation and the Botswana Building Society are also important providers of long term finance in the economy. Nonetheless, in recognition of the fact that this may remain a constraint even after interest rates are raised to more appropriate levels, the Government has recently embarked on a review of its development finance institutions and the availability of long term finance, in conjunction with the World Bank, to examine ways in which delivery mechanisms can be improved. The availability of short term trade finance and working capital is not a constraint in the current environment of high excess liquidity in the banking system.

39. Last, citizen investors face particular constraints which impede their greater involvement in the industrial sector. These constraints include: (a) lack of entrepreneurial, technical and business skills, (b) limited access to finance, (c) limited access to land and basic infrastructure, and (d) a lack of identified markets.

40. *Investment Promotion Policies*. The major institutional players in the industrial sector include the employers association, the Botswana Confederation of Commerce, Industry and Manpower (BOCCIM); the Botswana Federation of Trade Unions, which represents twelve of the sixteen existing unions; and the Ministry of Commerce and Industry, which has the dual role of promoting and regulating industrial development. Dialogue between the private and public sectors is important in supporting industrial development and, as Botswana is a relatively small country, this should not be difficult. Two recent private sector conferences have been important in assisting in this process and should be encouraged. In addition, private sector representatives are often included in Government reference groups dealing with economic issues.

41. Botswana's current system of industrial incentives includes:

(a) the Financial Assistance Policy (FAP), which was introduced in 1982 for new and expanding businesses -- providing a series of subsidies based on labor employed, sales, assistance for initial capital investment, and skills training

(b) the Selebi-Phikwe special incentive package -- which supplements FAP subsidies with corporate tax concessions and withholding tax exemptions -- for investments in the Selebi-Phikwe region which export 100 percent of their output outside the SADC and SACU regions

(c) a local preference scheme

(d) exclusive licenses

(e) infant industry licenses

42. The most important of these schemes, having the biggest impact upon the development of the sector, have been the FAP and the Selebi-Phikwe program. FAP provides different incentives to small scale investors, on the one hand, and medium and large scale investors, on the other. Assistance to medium and large scale enterprises is in the form of a wide range of grants and tax holidays spread over the first five years of a project's operation and is open to citizens and non-citizens alike. Several of the grants (specifically the labor grant and the capital grant) are directly related to the number of personnel employed -- the labor grant reimburses 80 percent of wages paid to unskilled and semi-skilled workers in the first two years, falling to 60, 40 and 20 percent in the following three years, while the capital grant provides an additional P1,000 per job created by foreign owned companies, and P1,500 per job created in a fully citizen owned company. The sales augmentation grant and training grants are not based upon employment, but rather on the level of sales and training needs respectively. In addition to the above incentives, the Selebi-Phikwe promotional program provides for a company tax rate of 15 percent for the first twenty years of operation, and a ten year exemption from withholding tax on dividends paid to non-residents -- for large companies locating in the Selebi-Phikwe region and producing for the export market. In addition to the above, these two incentive programs

provide additional assistance to companies which are located in rural areas and which are owned and managed by women entrepreneurs.

43. The FAP has been an economically sound promotion policy, based upon assisting companies overcome initial disadvantages of operating in the Botswana market. The scheme has been based on assistance over a five year period, with a reduction in financial support toward the end of the period as the company assumes greater financial viability and capacity to stand on its own feet. Estimates indicate that FAP has helped to create around 11,500 permanent jobs and has helped to encourage local entrepreneurs move into industrial activities -- although the failure rate has been quite high for the small scale Batswana sector (in common with similar schemes in other countries).

44. There are, however, many problems with FAP and the Government has become increasingly concerned with some aspects of its operation. Disbursements under the scheme have been increasing at 65 percent per annum -- rising from P0.3 million in 1982 to P20.3 million in 1990 -- while commitments have been increasing at an even faster rate recently, rising from P15 million in 1990 to P38 million in 1991. In addition, there have been numerous instances of abuse, demonstrated failure to achieve competitive levels of productivity after the expiration of the five year labor grant, and a tendency for an uncompetitive cost structure to remain after subsidies are removed.

45. The extent to which FAP is creating sustainable industries is an important issue for policy makers. A major focus of the program is to diversify the economic base so that Botswana will have activities, other than diamond production, which will support economic development in the future when diamonds are less likely to provide the engine of growth that they have done in the past. If FAP creates industries which can only survive on continued Government support, then they will have effectively not assisted in diversifying the economic base as their continued operation will be dependent upon Government revenues which, in turn, come mainly from the diamond sector. Reliance on the diamond sector will have consequently been reinforced rather than reduced. The ultimate development of sustainable, self supporting industries, is therefore an important plank of Government policy. The extent to which the FAP and Selebi-Phikwe programs are achieving this objective is increasingly being questioned.

46. There is also some concern that companies receiving FAP will leave Botswana once their FAP grants have expired -- and it is specifically in the labor intensive industries targeted by FAP that the potential for this kind of mobility is the greatest. However, this must inevitably be weighed against the valuable experience that such enterprises can provide to an unskilled work force -- if only for a limited period.

47. It is further questionable, whether Government policies should be subsidizing, as opposed to encouraging, investment (especially medium and large scale investments) in rural areas -- and whether this encourages uneconomic investment decisions. FAP may well be encouraging activities in which Botswana has an inherent competitive disadvantage.

48. Although the experience with the Selebi-Phikwe project has been considerably more limited, many of the same criticisms apply. Several companies have closed down as a result of an inability to compete in a more difficult economic environment. Employment levels have also fallen substantially from their 1991 highs.

49. These schemes have also bred a class of "rent seekers" -- and some well known cases of fraud and corruption. As many of the recipients of assistance under FAP and the Selebi-Phikwe initiative are provided assistance on a case-by-case basis, the scope for significant problems is considerable. The cases of fraud are well known within Botswana and the instances of pressure from industrialists on the Government, for continued additional assistance, have been in evidence during the difficult economic period of the early 1990s.

50. Given the progress achieved in creating employment opportunities and the overall constraints of the Botswana market, industrial policy now needs to be tailored more to provide sufficient incentives to all types of industrial activity, rather than specifically skewing development in favor of labor-intensive manufacturing. The available unemployment data suggest that the unemployment problem is declining over time -- although under-employment inevitably continues to exist on a significant scale in rural areas. The Government will need to ensure the continued development of manufacturing employment opportunities to absorb the growth of the unskilled labor force and continued rural-urban migration, however, it should now be possible to do so without specifically focussing on labor intensive activities. Growth should come from a broader range of industrial activities -- including more skill intensive manufacturing industries, service industries, down stream processing, and other niche market activities.

51. In addition, Botswana should move from a discretionary, case-by-case system of incentives, to a more transparent and more easily manageable system. Such a system will not have the disadvantage of skewing industrial development in a particular direction to the detriment of other sub-sectors, and will not be open to the types of abuse experienced by the current programs.

52. Consequently, the recommendations made in this report have been premised upon two important principles. The *first* is that Botswana should reconsider its current policies of encouraging industrial development to favor specifically labor intensive manufacturing industry. This is relevant given the declining need to absorb large numbers of unskilled individuals into the labor force. It will also be increasingly important to develop better quality labor, with greater skills, as the economy advances within the ranks of the middle income countries. The *second*, is that promotion policies should move away from case-by-case provision of incentives to a more transparent and uniform system which provides automatic benefits to the entire industrial sector.

53. These changes in policy should, however, be undertaken within the context of a better understanding of the industrial sector and the dynamics of the labor market as indicated above (see paras 17 and 21). For example, should policy makers consider that unemployment levels will increase substantially in the near future, it may wish to provide a more targeted system of industrial incentives which continued to focus on the development of labor intensive industrial activities. However, if the economy continues to grow at a rate which is sufficient to absorb new entrants without leading to a substantial increase in unemployment, then it would be more appropriate to provide a system of incentives which applied to a broader range of industrial activities.

54. Within the existing framework of lower unemployment it may well be possible for the authorities to consider abolishing most of the current FAP incentives for medium and large scale enterprises (the capital grant, labor grant, sales augmentation grant, and tax holiday) while retaining the training grant and extending incentives to a broader range of enterprises. Continued assistance for training is considered important, given the need to both disseminate and elevate skills amongst Batswana employees. Given the potential abuse of the training grant, however,

it is recommended that the Government should closely monitor the application of this grant to ensure that it contributes to improved efficiency.

55. FAP could be retained in its current form, for small scale activities of Batswana enterprises. A continuation of FAP assistance to this sector is necessary to further assist Batswana entrepreneurs in the industrial sector. To widen the net of investors that would be covered by this assistance, it is recommended that the upper limit on size be increased to take account of inflationary trends since the limit was last revised, and possibly increasing the level further to provide assistance to the smaller of the former medium scale grouping. However, given the high rate of failure of small scale FAP, it will be very important that the Government monitor and evaluate this program more carefully than it has done in the past.

56. Medium and large scale enterprises might instead be assisted by an incentive package which seeks to introduce a more flexible system of wages, increase labor productivity, develop higher skilled jobs, and provide for a lower rate of corporate income tax -- all of which are discussed in greater detail below. If these changes were implemented, it would also be appropriate to re-examine the need for the special Selebi-Phikwe incentive package in its present form.

57. The Government may, however, wish to wait until the forthcoming FAP evaluation is completed before it makes final decisions on redesigning or abolishing FAP. Nonetheless, it may be possible to use the recommendations made in this report in preparing the terms of reference for the evaluation.

58. ***The Enabling Environment.*** Botswana's current industrial development environment -- and the 1988 Industrial Development Act -- seeks to "supervise" industrial development. This has tended to create a class of rent seekers rather than developing an efficient and competitive class of industrialists. Rather than supervising development, the Government needs to replace existing policies with more transparent mechanisms of assistance and to manage industrial development utilizing "management by exception" techniques. Current policies are too interventionist (i.e. non-transparent and not applied "across the board").

59. An appropriate tax framework could be established to provide incentives to potentially sustainable industrial activities. Currently, Botswana has relatively high effective tax rates but with many exceptions -- which has resulted in a low average rate of taxation. It would be preferable to remove all exemptions from established tax policy and to determine a lower overall rate of corporate (and personal) tax. It should even be possible to reduce corporate tax rates while increasing overall tax revenues by eliminating exemptions, increasing the efficiency of tax revenue collections, and extending the coverage of broadly based consumption taxes. The only exception to this would be the mining sector which is already governed by separate tax arrangements which suit the nature of this particular industry.

60. Low rates of corporate taxation have been used in many other countries as a method of providing industrial incentives. As Botswana currently does not have a fiscal constraint, it has less need to raise corporate tax revenues from the non-mining sector. The authorities could therefore easily apply a lower non-distortionary tax to all non-mining sectors of the economy. Nonetheless, given the need to widen the tax base, and the fact that the early 1990s is projected to be a transition period from budget surpluses to budget deficits, Botswana should consider lower rates of corporate taxation within the context of a full taxation commission review and in

conjunction with information on public revenue projections. However, as the tax authorities are already considering further reductions in income tax rates -- independently of industrial promotion policy -- it may be possible to reduce rates, to some extent, before a full commission reviewed tax policy more generally.

61. Policy with respect to the availability of industrial land will also need to be reviewed as a matter of utmost urgency. Limited access to land has acted as an important deterrent to industrial development. Government efforts to speed up land development through the Accelerated Land Services Program, are not likely to be sufficient to meet the existing industrial sector demand.

62. Given the considerable importance attached to land in traditional Botswana culture, it may be necessary to deal with industrial land in a special way -- different from the way in which land is dealt with for residential and commercial purposes. Consideration should be given to allowing foreign investors to own, or lease long term, industrial land. Moreover, industrial land needs to be developed with a much longer planning horizon -- ideally over a 20 year period. Land could then be developed rapidly to meet the existing excess demand. It is also important that undeveloped industrial land be taxed by local authorities at a much higher rate than developed land so as to encourage development for industrial purposes rather than encouraging individuals to hold onto land for purely speculative purposes. Last, a Land for Industry Committee should be established -- or created from existing committees dealing with land issues -- comprising high level representatives from relevant ministries, to oversee the planning process for industrial land.

63. The FAP labor grant was designed to compensate manufacturers for low levels of labor productivity in Botswana. However, the available evidence indicates that the time required to achieve internationally acceptable levels of productivity is longer than the five year period over which FAP labor grants are paid. Although grants could be extended for a longer duration to ensure that productivity does increase sufficiently over the period of support, it is alternatively suggested that substantive progress should be made toward bringing the level of wages and the level of productivity into a more appropriate balance.

64. With respect to wages, a first best solution would be to abolish the minimum wage system which establishes an arbitrary floor for wages above the market clearing rate. This may, however, be difficult to achieve politically. Alternatively, the Government could consider: (a) collapsing the current minimum wage system of eight different employment categories and five different "minimum" wages, into a single true "minimum" wage; (b) manufacturing wages could be exempt from minimum wage legislation as rural workers and domestic help now are; and/or (c) real minimum wage levels could be allowed to erode faster.

65. The extent to which real wage levels will actually decline will depend upon several factors including the level of unemployment and the extent to which workers are prepared to substitute their leisure for lower rates of remuneration. Although unemployment is relatively low by developing country standards, there is still a sufficiently large pool to exert downward pressure on wages. In addition, in a rapidly growing economy with a highly segmented labor market, the unemployed will almost certainly be unskilled workers. The evidence from markets which are not regulated by minimum wages legislation (rural workers and domestics) also supports the view that there is some potential for reducing wage levels. On the other hand, anecdotal evidence from some formal sector employers indicates that there is a threshold level of wages below which workers are unprepared to work. Consequently, the extent to which real wage reductions can be achieved, may be limited in the current context. Nonetheless, it would

certainly be preferable to have a more flexible system of wages rather than continuing with a rigid system of minimum wages. In the event that unemployment rates did increase substantially beyond their current low levels, it may be possible, with a more flexible system, to achieve higher real reductions in wage levels. A better understanding of labor market dynamics as enunciated above, would assist in bringing greater clarity and understanding to this debate.

66. Efforts will also be needed to increase the productivity of Batswana workers. Schemes to improve productivity, such as the greater utilization of piece rate systems, should be vigorously pursued. Current restrictions which only permit payment on a piece rate basis over and above the minimum wage, should be amended. The Productivity Center should also be supported in its efforts to investigate and develop ways to increase productivity. Nonetheless, the biggest increases in productivity are likely to come from continued on-the-job training of workers and better supervision and management by overseers. Increases in productivity, are therefore likely to be realized only over the medium term.

67. To enhance the efficiency of the financial system and its provision of both the working capital and long term finance requirements of the industrial sector, it is necessary that interest rates move to positive real levels. Positive real lending rates will provide a clearer indication of the effective demand for capital, while reversing the previous policy which has, by maintaining negative real interest rates, tended to encourage inefficient investment and to distort capital intensity/labor intensity choices. Lending by commercial banks at negative real rates of interest has also encouraged excessive consumption. A move to positive lending rates will be important to generate additional household and business savings, and to promote the development of properly and efficiently functioning money and capital markets -- leading to private sector mechanisms for the further development of long term financing requirements.

68. The commercial banking system currently provides some finance for periods up to five, and sometimes even ten, years. By the standards of most countries of the region, this is a reasonably good record. Commercial banks, with a tradition of financing short term trade credits, are unlikely to be further involved in long term lending, if such lending is based on their current short term structure of deposits. These institutions mainly provide working capital needs -- generally on overdraft -- but as these are normally rolled over, they also serve as a longer term source of funding.

69. The domestic development finance institutions also assist in meeting the long term financing needs of industry. The most successful, and most prominent of these, has been the Botswana Development Corporation -- which has evolved into an important source of long term equity and loan capital in the economy. Stock Brokers Botswana also provides an intermediation function which has the potential to provide significant additional long term financial resources to industry. Private, and possibly public, pension and insurance funds may also develop into important sources of longer term capital.

70. Nonetheless, it will be important to improve the operation of the existing development finance institutions to enhance their capacity to channel long term funds to the economy. The Government of Botswana and the World Bank are currently reviewing the operations of these institutions and considering the development of more efficient delivery mechanisms. It may well be possible to provide a more effective method of channelling the savings of the Government to support the long term financing needs of both the public and private sectors through a more appropriately designed and managed on-lending institution.

71. Small and medium scale industrial development is financed by "own funds", some commercial bank lending, and the Financial Assistance Policy. In addition, some resources are available through Tswelelo, which provides a comprehensive range of financial and non-financial services to the SME sector. Given the difficulties involved in interfacing the formal financial system with the financing requirements of the SME sector, it is recommended that Tswelelo and FAP should continue to service the financing needs of this sector.

72. It is important that the current moves to further relax the regulatory environment for the employment of expatriate personnel be carried through. Past procedures have been very cumbersome -- involving four Government agencies -- Labor, Immigration, Security and Commerce. Although the system is gradually being streamlined, it could benefit from the introduction of positive lists of occupations which ensured very easy access for required professions.

73. As indicated, Government should continue to resist pressures to subsidize utility prices, but should ensure that the parastatal utility companies operate as efficiently as possible. This may involve the establishment of a parastatal monitoring unit in the Ministry of Finance and Development Planning which, it is understood, is currently under consideration. In addition, Government needs to adopt a more pragmatic approach to the importation of utilities, where possible. With several cheap producers in the region, and a move to greater SADC inter-regional cooperation, it should be possible to reduce increases in electricity prices by importing power to meet future increases in demand. Although the importation of water resources may be more problematic, possibilities for greater regional cooperation exist in the area of telecommunications.

74. To ensure a successful industrial development policy with the fullest possible participation by external foreign investors, it will be important to develop more effective investment promotion activities. These are currently provided through the Trade and Investment Promotion Agency (TIPA). However, the current status of the agency within the Ministry of Commerce and Industry has conferred certain important disadvantages which have impacted on its ability to perform this role as it should. It is recommended that investment in Botswana should be promoted by an independent, well managed, promotion agency with a clear strategy, through an organization with a proper institutional structure.

75. Given the constraints of such an agency operating within the MCI, this almost certainly means that TIPA should be made an independent parastatal organization. Given the fact that it is unlikely to have independent sources of funds, at least initially, it will almost certainly have to rely upon the Government for financing, although every effort should be made to solicit alternative funding sources -- including international bi-lateral donor agencies. Ultimately, the agency should aim to develop greater financial independence from Government -- financing its activities, as much as possible, on the basis of fee payments.

76. Should the Government be unprepared to make TIPA an independent parastatal then, at the very least, it should be provided substantially greater autonomy within the confines of MCI, to ensure that it can perform its promotional activities to fullest advantage.

77. Investment promotion should be targeted at those countries which are most likely to come to Botswana. Regional investors -- particularly from South Africa and Zimbabwe -- are the most important investors currently operating in Botswana and for this reason are probably likely to continue to be the most important investors for the future. However, investors from other countries should also be solicited. The most important markets in this regard are the newly

industrializing countries of Asia (the NIC's). Europe, the United States of America and Japan may also be a source of some limited amounts of foreign investment.

78. *Opportunities for Investment in Botswana*. The basic premise of this report has been that all types of industrial development should be promoted and encouraged in a non-discriminatory and transparent manner. Every effort should be made to encourage all types of industries be they more labor-intensive manufacturing industries; other manufacturing industries which are not necessarily labor intensive; service industries; or down-stream processing. Many of these are likely to involve the development of niche markets. Incentives should be provided to all of these activities, and others, on an equal basis.

79. The need for manufacturing industry to provide employment opportunities for unskilled entrants to the labor force will continue for some years to come. Nonetheless, an equally important strategy of industrial development policy should be to encourage a movement up-market in terms of skills, product quality and overall productivity, more suited to a middle income level developing country. Continued emphasis on education, vocational training, and skills enhancement -- by both the public and the private sectors -- will be important in this regard. Hence, manufacturing industries of all types, not only labor-intensive ones, should be encouraged.

80. Equally important will be the development of service industries. Over the recent past, some of the fastest growing components of the industrial sector have been the service sectors. It is highly likely that they will continue to grow at a relatively faster rate. Incentive mechanisms should equally aim to encourage such industries. The report points to the possible development of the following types of service industries: on-line transactions; postal re-expediting; computer programming; medical services; financial services; off-shore banking; and grain storage. This list is not exhaustive, nor does it necessarily represent those service industries which may ultimately be best suited to development within Botswana. Consequently, further in-depth expert review of individual possibilities is recommended. Given non-discriminatory incentives and a supportative enabling environment, the private sector itself should be able to identify promising opportunities as they surface.

81. The development of down-stream processing is also an activity which should be encouraged. The experience with diamond cutting and jewellery manufacturing has shown that companies may find attractive and potentially profitable opportunities in these areas. Although the possibilities may be limited (as has been demonstrated by some of these activities) they should be encouraged with equal vigor in common with other industrial activities. The focus of attention for down-stream processing, has been hides and skin; salt and soda ash; uncut diamonds; semi-precious stones; timber; raw silk; game products; cattle bones; tallow; indigenous fruits; handicrafts; and, cotton.

82. Last, the continued development of tourism will be important, especially for the rural areas of Botswana. The recent approval of the Government Tourism Policy is an important step in this direction.

83. *Conclusions, Priorities and Transition Strategies*. Movement to a new system of industrial incentives will require the development of a transition strategy. For example, current FAP recipients, and investors operating at Selebi-Phikwe must continue to receive the benefits

which have been promised. It will also be necessary to establish some date in the future, after which no further new benefits will be provided under the existing arrangements -- to allow for business people who have been planning on the basis of receiving FAP and/or developing at Selebi-Phikwe to follow through on their plans. It should not be necessary to make this transition period longer than twelve months. This would imply that large- and medium-scale FAP recipients would remain in the present system for a six year period (a one year transition plus the five years of FAP benefits), after the decision to move to an alternative incentive structure.

84. During such a transition period, priority should be given to addressing the "enabling environment" issues discussed above. Most importantly, the Government should give priority to pursuing actions that will enhance the productivity of labor -- such as introducing piece rate systems on a wider basis, addressing the industrial land issue as a matter of urgency, and moving forward on the various regulatory constraints which adversely impact upon industrial development. At the same time, the Government will need to be diligent in pursuing a policy which seeks to bring minimum wages more into line with productivity.

85. Over the twelve month transition period the Government should also devote its attention to designing the details of the most appropriate incentive structure -- reviewing the extent to which it can reduce the corporate tax rate, within the confines of fiscal policy.

CHAPTER 1

INTRODUCTION

A. PURPOSE OF THE STUDY

1.1 The seventh National Development Plan (NDP 7) establishes the framework and priorities for development and recurrent budget expenditures over the six year period from 1991 to 1997. This plan explicitly assumes that industrial, trade and commercial policies, and the legal framework for business operations, will be conducive to the development of the private sector. This report reviews these areas of policy and makes recommendations to facilitate the achievement of the relevant development strategies contained in the Plan.

B. THE STRATEGIC CONSIDERATIONS

1.2 The first twenty five years of development in Botswana were largely dedicated to creating the physical and administrative infrastructure of nationhood. At independence, very little infrastructure existed and Botswana was classified as one of the Least Developed Countries in the world. A quarter of a century later, it ranks as a middle income country. Although continued development of physical and administrative infrastructure will be necessary, social and economic development has reached a juncture where other broad strategic considerations -- especially concerning industrial development -- are important.

1.3 The first set of considerations involves fundamental changes in Botswana's relationships with the rest of the world. Changing political and military relationships in Europe and the Middle East will have repercussions for Botswana -- as for other developing countries. New regional trade arrangements in Europe and North America will have implications for access to those market areas. Most important, the new environment in the Southern Africa region is likely to produce fundamental changes in Botswana's economic relationships with its neighbors. These new external factors are likely to substantially alter the development patterns of the past twenty five years.

1.4 The second set of considerations arises from the rapid growth of Botswana's economy and the increasing wealth and complexity of the society and economy which this wealth has conferred. Mineral sector wealth has made possible a shift, from an agrarian, to an industrial and commercial society. This shift is important, as livestock and arable agriculture are unlikely to be able to support broader economic growth. Industrial growth, including services, is therefore necessary.

1.5 The growth and deepening of the financial system will require active management of money and capital markets and foreign currency relationships. The greater range of goods and services available will raise issues of product and service standards, consumer protection, and credit regulations. As the business services sector expands, intellectual property matters, such as patents, trademarks, industrial design and copyright protection, will become important. In addition, the rapid growth of wealth is raising issues of income distribution which, if not addressed, may endanger peace and social stability. NDP 7 responds to this issue by placing priority on the need to extend employment and the benefits of economic growth beyond the resource sectors, and has placed emphasis on diversification into secondary and service industries.

Employment creation, diversification, rural development programs, and the encouragement of small industries and the informal sector, will help ameliorate the problem of income distribution.

C. THE FIRST QUARTER CENTURY

1.6 Botswana can build on a solid base of accomplishment achieved over the past twenty five years. At independence, the new nation inherited very little in the way of economic or social infrastructure on which to build a modern state. Almost 70 percent of the country is covered by desert and the climate is arid or semi-arid. Average rainfall varies from 650mm in the north-east to less than 250mm in the south-west, and is highly variable from year to year. Hence, agricultural activities, both pastoral and horticultural, are very unstable. Similarly, the supply of water to support population centers and economic activities is crucially important. At independence, the population was a little over 540,000 and nearly 96 percent rural. The dominant activity was raising cattle.

1.7 By the early 1990s the country had been transformed. The population had grown to an estimated 1,340,000. The average population growth rate, has been around 3.4 percent per annum from independence to 1991. However, over 30 percent of the population now lives in urban communities. Life expectancy increased from 48 years to over 60 years. Primary school enrolment rose from 72,000 in 1966 to 283,500 in 1990. Secondary school enrolment rose by an average of 16 percent per annum from 1965 to 1990, reaching 56,800 students in the latter year. Students registered at universities increased from 22 in 1965 to 3,100 in 1989/90. These improvements in the demographic characteristics of the population were accompanied by substantial increases in per capita income which rose from P537 in 1965 to an estimated P5,950 in 1991 (measured in 1991/92 prices).

1.8 The improvement in the physical infrastructure of the country is equally striking. With only 20 kilometers of tarred road in 1965 -- mainly in Gaborone -- by 1990 this had reached 2,664 kilometers of trunk roads. Production of electricity increased from 5 million kwh in 1965 to 845 million kwh in 1989. The telephone system has been modernized and extended to provide most of the country with service, and international connections have been developed using satellite facilities. Potable water is available in all sizable population centers. The rail system has been re-equipped and expanded to serve new mining projects. More recently, an accelerated program to increase the supply of housing and serviced sites for industry and commerce has been initiated to meet high demand in rapidly growing urban centers.

1.9 Although underemployment continues to be a major problem, there has been a very large increase in employment in the formal sector. Excluding those employed abroad, formal employment rose from 14,000 in 1965 to 222,700 in 1991 -- the latter figure representing almost 50 percent of the labor force in that year. Most of the remainder of the labor force is engaged in informal activities in rural and urban areas. About 17,000 people work in the South African mines and it is highly likely that many of these workers will return to Botswana. Although these returnees will bring skills and established work habits, they will also place additional strain on the local employment market.

1.10 Table 1.1 provides some comparative economic and social data for the two years, 1965 and 1990.

Table 1.1: Selected Economic and Social Indicators

	Units	1965[a]	1990[a]
Population	number	540,000	1,340,000
Population growth	percent p.a.	3.7	3.4
Urban Population	percent	4	30
Life Expectancy	years	48	60+
Primary School Enrollment	number	72,000	283,500
University Students	number	22	3,100
per capita income	const. 1991/92 pula	P537	P5,950
Tarred road	kilometers	20	2,664
Electricity production	mill kwh	5	845
Formal sector Employment	number	14,000	222,700

[a] May not always represent stated year exactly - but one year either side.
Source: Government of Botswana.

D. THE ROLE OF THE DIAMOND INDUSTRY

1.11 The substantial improvement in incomes, social services, infrastructure and employment since independence were primarily supported by income from the mining sector. Although copper, nickel, coal and beef made significant contributions -- diamonds were the dominant factor.[1] The revenues flowing directly to the Government from diamond mining have increased dramatically, despite the recession in the international diamond market which necessitated a measure of stockpiling in the period 1982 to 1985 (and again in 1992). In 1988/89 the mining sector accounted for over 50 percent of GDP.

1.12 Through a series of agreements, Government is assured of a high proportion of the profits arising from diamond mining -- receiving royalties and taxes as well as dividends on its 50 percent shareholding in the Debswana Diamond Company. Since 1982/83 these revenues have permitted the Government to support strong growth in expenditures on infrastructure, health and education, and an expansion of Government services -- while still achieving budgetary surpluses in most years. Diamond exports have ensured a healthy balance of payments, with a healthy foreign exchange reserve position and low levels of foreign borrowing. Botswana's debt servicing burden is relatively small and the economy is in a strong position to continue to finance its future development requirements.

[1] Diamonds were discovered shortly after independence and mining began at Orapa in 1971.

E. THE NEED FOR DIVERSIFICATION

1.13 The need for diversification stems directly from the concentration of economic activity and income in resource industries. Diamond mining, non-ferrous metals, and beef farming, are the three major sources of foreign exchange -- although soda ash exports may become a major source of future revenue. Unfortunately, none of these industries is labor intensive, and thus the economic structure presents a major problem of employment creation and income distribution. Productive opportunities are needed to absorb savings from the mineral sector -- to avoid their use in conspicuous consumption, inflating wages and costs, and their use in investments with low rates of return. The need to find alternative productive opportunities has been a fundamental objective of economic and industrial policy in Botswana since shortly after independence. This is the premise underlying the Government's rural development strategy, its programs for small and medium scale enterprises, and its encouragement of the informal sector. It is also a basic premise for the reservation policy under which certain activities are reserved for Botswana citizens.

1.14 The need for diversification of the economy is not a new objective. Nonetheless, the rapid growth of mineral income -- especially during NDP 6 -- and the prospect that this growth cannot be maintained, has imparted a new sense of urgency. Political and social pressures for a better income distribution are growing -- aggravated by concern about rural-urban migration. This places a higher priority on the National Settlement Policy to allocate infrastructure to areas with genuine promise for industrial development. Equally important, the diversification of the economy into new secondary industries and services will itself be partly dependent upon the widening of the domestic market for the products produced by these sectors. Although the market in Botswana will seldom, if ever, be adequate to support new secondary industries and services by itself, a strong and growing domestic market is, nonetheless, an important requirement for the survival and success of such enterprises.

F. THE REGIONAL ENVIRONMENT

1.15 A dominating factor in the future evolution of Botswana's economy will be the changes taking place in the Southern Africa region. Political developments in the Republic of South Africa will have the most important repercussions. Whether the evolution is turbulent or relatively well controlled will itself be important to Botswana. Similarly, the direction of change will also be critical. If the task of restructuring employment and spending patterns in RSA causes the next government to turn inward, and become highly protective, it will be difficult to achieve industrial diversification in Botswana. If the new government, alternatively, follows a more open policy, then new possibilities arise, as well as new competitive challenges. It is not clear which alternative will occur but, in either case, Botswana will be required to respond promptly and appropriately.

1.16 The economic relationship with RSA has been organized primarily by the Southern African Customs Union Agreement (SACUA). This arrangement, begun in 1910, has had advantages and disadvantages for Botswana. It has simplified the administrative burden of collecting customs revenues, and has been a major and dependable source of Government revenues. It has also significantly determined Botswana's international commercial and industrial polices, since the larger partner has effectively determined changes in these policies. Although there are provisions permitting the smaller members of SACUA to provide temporary protection

for new "infant" industries serving the domestic market, in practice it has been difficult to use these provisions to any significant extent. With a changing geo-political situation in the region, the SACU arrangement may no longer be the most suitable vehicle for facilitating regional trade and industrial arrangements. Such arrangements may be more appropriately accommodated under alternative regional trading arrangements. A review of SACUA, commenced several years ago, is currently in a state of semi-suspension until political evolution in RSA has been more clearly resolved.

1.17 Other changes within the region are also important -- including the movement, by many countries, away from command economies to market based systems. This may also change the nature of their economic and trading relationships with Botswana. Although Botswana has a market oriented economy, the emergence of other regional market directed economies will bring changes in the form of modifications in comparative advantage. It will be important to be able to adapt quickly to changes in market prices and competitive relationships that a regional market system is likely to produce. This is a new environment to which the private sector and public policy makers in Botswana will have to adjust.

G. THE EVOLUTION OF INDUSTRIAL POLICY IN BOTSWANA

1.18 *The 1960s*. During the first years of Independence Botswana made little effort to attract foreign investors in the industrial sector as Government attention was focused on more pressing development needs -- including the provision of basic physical and social infrastructure. Consequently, resources allocated to the development of industry were limited. This made Botswana a less attractive market for foreign investors than its neighbors. The limited local market, low raw material base, high cost of utilities, shortages of skilled manpower and inadequate educational and recreational facilities, restricted the establishment of industries other than mining.

1.19 The Industrial Development Act of 1968 was approved to ensure that investors had objectives compatible with Botswana's long-term development goals. The Act provided for the formulation of protective measures aimed at supporting local industry in accordance with the infant industry provision of the SACU agreement. The Act also provided the legislative framework for the licensing and regulation of industrial investment in the manufacturing sector.

1.20 In addition, the Customs Union agreement, signed in 1910, which incorporated Botswana, Lesotho, Swaziland and the Republic of South Africa, was renegotiated in 1969.[2] The revised agreement provided a new basis for revenue sharing and introduced a variety of measures that could be used to ensure the effective participation of smaller countries in the growth of the regional economy. It made provisions for the protection of new industries serving domestic markets -- from competition from other producers within the Customs Union -- for a limited 8 year period. Customs duties increased from one-fifth to almost one-half of Botswana's domestic revenues between 1968/69 and 1969/70. After 1969, the SACU agreement became a major factor in the determination of Botswana's industrial policy.

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[2] Namibia joined SACUA following its independence in 1990.

1.21 *The 1970s*. During this period attention began to shift within Government toward more active measures to promote the diversification of the economy -- from beef and minerals -- and to encourage the creation of employment opportunities in industry. In order to address the issue of diversification more effectively, emphasis was placed on institution building. Various institutions were established to implement industrial policies including financial institutions such as the Botswana Development Corporation (BDC) and the central bank -- the Bank of Botswana (BoB).

1.22 The Ministry of Commerce and Industry, which has portfolio responsibility for the formulation of industrial policy and the promotion and regulation of industry and trade, also strengthened its institutional capacity by creating the Botswana Enterprise Development Unit (BEDU), the Rural Industrial Officer Cadre, and the Business Advisory Services (BAS) -- in the mid to late 1970s -- with responsibility for the development and promotion of small scale industry. These institutions were merged into one unit in 1987 -- Integrated Field Services, IFS -- to streamline their activities and promote better coordination.

1.23 *The 1980s*. Industrial development in the 1980s was characterized by new industrial policies and a significant change of attitude toward the private sector by Government. A detailed study of employment policies (Lipton 1978), of policy initiatives and strategies (Financial Assistance Policy 1982), the National Policy on Economic Opportunities (1982), and the Industrial Development Policy (1984) demonstrated the increased attention which Government was paying to the development of the industrial sector.

1.24 In 1982 the Government introduced a new approach to industrial development with the *Financial Assistance Policy* (FAP). FAP is a program of assistance to industry aimed at supporting new and expanding productive enterprises that create employment -- in the form of grants. The grants are limited to five years, and decline over this period for medium and large scale projects. For small scale projects the grants are provided on a one-off basis. The package, which is designed to expand economic activities and diversify the economy, constitutes a major plank of the Government's industrial development effort. FAP grants assist investors by providing additional cash flow in the early years of a project; subsidizing the use of unskilled and semi-skilled citizen labor during the first five years of a project; and providing a cash subsidy on the basis of total sales.

1.25 By 1985, the manufacturing sector provided 12.6 per cent of total wage employment in the private and parastatal sector, compared to 7.4 per cent in 1975. However, most manufacturing activities were concentrated in urban areas. In 1988, special incentives were given to companies establishing in the Selebi-Phikwe region to promote employment and exports from that region. A further special incentive package was introduced for the area in 1989. To qualify for the incentives, manufacturers must locate in Selebi-Phikwe, export 100 percent of their output outside of the SACU region, employ over 400 Batswana within two years, and invest at least 25 percent of fixed and permanent working capital as equity. In return, investors qualify for FAP incentives, receive a nominal corporate tax of 15 percent for the first 20 years of the project, and are exempt from withholding tax on dividends for 10 years.

1.26 The direction and character of recent industrial development in Botswana was established by the *Industrial Development Policy*, Government Paper No. 2 of 1984. The aim of the policy is to ensure that the industrialization process promotes job creation. It also promotes a better spatial distribution of income earning opportunities, and increased participation

by Batswana in business activities. The legal backing for the implementation of the industrial policy is the *Industrial Development Act*, enacted in 1968, and amended in 1988. This Act provides the legislative framework for licensing and regulation of industrial investment in the manufacturing sector. The Act requires all industrial enterprises with ten or more employees, or an energy consumption of at least 25 horsepower or 18.7 kilowatts for machinery employed, to apply for a license to operate.

1.27 One of the recommendations of the *Presidential Commission on Economic Opportunities* (1982) was to encourage the creation of economic opportunities for Batswana and encourage their participation in commercial, manufacturing and construction services. Consequently, certain industrial and commercial sectors have been reserved for citizens[3] so that the long-term goal of an industrial and commercial sector principally owned and managed by citizen-owned companies can be achieved.

1.28 A *Local Preference Scheme* was first introduced in 1976, and modified in 1986. Under this scheme, local suppliers may qualify for contract awards from Government institutions as long as they are within a fixed premium over the lowest foreign bid. The original preference was a maximum of 12.5 percent of sales. It now gives local manufacturers a maximum preference rate of 40 percent of value added[4] locally on purchases by the Central Government, local authorities, and parastatal bodies.

1.29 Through the *Revised National Policy on Incomes, Employment, Prices and Profits*, Paper No. 1 of 1990, the Government recommended eliminating controls on prices, with the Government striving to create conditions conducive for competitive pricing rather than fixing margins. To this end the Government will eliminate restrictive licensing practices -- except to safeguard the public interest and to ensure that monopolies are not created. Furthermore, through consumer councils, the Government will aim to increase consumer awareness of market conditions and the forces of supply and demand as factors that influence pricing policies of private organizations.

1.30 The Revised Incomes Policy has mandated changes to the Industrial Development Act of 1988 and the Trade and Liquor Act of 1986. The changes involve the automatic granting of industrial licenses once planning permission -- required under planning, zoning, health or other regulations -- has been approved. Licensing authorities will no longer be expected to make commercial judgements on applications and licensing will no longer be open to objections by competitors. It is expected that these changes will increase competition. The Revised Incomes Policy also provides that, any wage above the Government mandated minimum wage applicable to formal sector employment, be determined by market forces and collective bargaining.

1.31 During NDP 7, development efforts will focus on broadening the industrial and commercial base through the diversification of economic activities. Rural development will also depend to a great extent on the diversification of the economy. The Government will emphasize diversification through creating a better enabling environment for private sector development,

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[3] For example, manufacturing of school uniforms and school furniture, burglar bars, protective clothing, cement, baked bricks, milling of sorghum and baking of bread.

[4] The premium is with respect to Batswana value added. Non-citizens adding value in Botswana attract no premium.

attracting investment and promoting exports, strengthening intersectoral linkages and encouraging the informal sector. Further, the Government will promote the application of science and technology innovations, relax constraints on construction, and strive to improve industrial relations.

H. THE PURPOSE OF AN INDUSTRIAL POLICY

1.32 *The Objective*. An industrial policy is one of several policies which Government employs to steer the economy in desired directions. Such a policy must have an overall set of objectives against which it can be judged. The fundamental thrust of economic policies as set out in NDP 7 are:

(a) *Sustained Development*. The key to sustainability has been identified as diversification from the current narrow base. The Government aims to achieve this by investing the wealth from mineral exploitation in viable productive activities that collectively can become the engine of economic growth -- to replace the diamond sector.

(b) *Rapid Economic Growth*. As the rate of growth of the minerals sector slows, it will become increasingly important to transform the nation's mineral wealth into productive capital formation in the rest of the economy.

(c) *Economic Independence*. This requires diversification of production and markets, so that the effect of adverse developments in any single product or market is reduced. This must, however, take into account the economic cost of diversification. A diversification strategy which seriously compromises other objectives -- should not be adopted.

(d) *Social Justice*. The ultimate aim of development is to improve quality of life. Hence all groups and regions should share in the benefits of development.[5]

1.33 *The Role of Policy*. The purpose of an industrial policy, however, should not be to promote industrialization for its own sake. An appropriate industrial policy can contribute to Botswana's development objectives -- while an inappropriate industrial policy can thwart those intentions. Varied success in other developing countries, with respect to industrialization, aptly illustrates this point. Hence it is important to distinguish between policies which promote an "appropriate" from an "inappropriate" industrial policy.

1.34 Intervention by Government can contribute to achieving its primary objectives in several ways. For this reason, Government's industrial policy thrust should focus on the following:

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[5] Benefits which accrue to foreigners are not considered part of the objective. It will be necessary to pay foreigners for the services which they contribute to Botswana, but care should be taken not to pay more than the value of their services.

(a) *Tilting the structure of production towards comparative advantage.* To the extent that incentives bias industrialization in the direction of Botswana's comparative advantage the diversification of the economy will be in productive activities which are viable in the long run, and are capable of taking over as the engine of sustained economic growth.

Alternatively, if a set of industries is established which are permanently dependent on subsidies derived from the mineral sector then, when the mineral sector ceases to generate surpluses, the economy may wither. Hence, diversification must be sustainable.

(b) *Increase productivity and efficiency in the use of resources.* Industrialization policy can contribute to the objectives of NDP 7 by ensuring that the incentives for use of the nation's resources reflect their true cost to Botswana. Decision makers should face real costs when deciding where to invest and which technologies to employ.

(c) *Offset Distortions.* Closely related to (b) is the role of policy in off-setting ongoing distortions in the economy. For example, if the Government decided to set a minimum wage above the value of the product of labor, this would result in less than optimal efficiency in the use of labor. Ideally the reasons for the distortion and its appropriate size should be examined to minimize its impact. If the distortion nevertheless remains, it may be possible to offset the extra cost of the distortion by a subsidy.[6] However, this will, of course, be a second best solution.

(d) *Break Constraints.* One of the most effective ways in which Government industrialization policy can contribute to the nation's objectives is to break down constraints which prevent the economy from achieving what could otherwise be accomplished. The constraints found in many developing countries -- foreign exchange and savings -- are not problematic in Botswana. The continued focus on breaking other constraints, however, is a productive role for industrial policy.[7]

(e) *Stimulate the process of economic growth.* Policy can accelerate economic growth by directly affecting the growth process. An important contributor to economic growth is the accumulation of capital, both physical and human. The accumulation of such capital should primarily be addressed by Botswana's overall planning and macroeconomic policies.

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[6] The most efficient policy intervention is one which deals directly with the distortion and does not introduce any side effects. Thus, for example, a trade tax or subsidy might be used to deal with a labor market distortion, but such an intervention is highly inefficient because there is no necessary relationship between the degree to which the labor market distortion is offset and the size of the trade tax or subsidy, and the trade distortion has well known real costs to the economy.

[7] In focusing on constraints, however, it is important to remember that the beneficiaries must ultimately be Batswana. Sometimes foreign investors point to "constraints" which are primarily designed to affect the distribution of benefits between Batswana and foreigners.

Industrial policy itself can affect two other major determinants of economic growth: "learning by doing" and entrepreneurial "rewards". The learning by doing phenomenon has been identified as crucial in many developing countries as it takes time for both management and workers to become fully effective at their tasks. Industrial policy can promote this by focussing its assistance on infant industries. The role of the entrepreneur in identifying profitable opportunities and committing the resources to make that opportunity bear fruit is central to the process of economic growth. Industrial policy can contribute by ensuring that the rewards go to those who bear the risks of productive enterprise, and not to those who attempt to seek special favors from Government.

I. SUMMARY

1.35 By the start of NDP 7, in 1991, Botswana's economic environment had altered remarkably since independence. World markets have become much more competitive and the countries of the Southern Africa region are becoming more market oriented. Changes in the Republic of South Africa raise the possibility both of increased instability in a very large neighboring market, and of new growth and outward looking expansion and competitiveness. Within Botswana, good progress has been made in establishing the basic infrastructure for economic development; the financial system has deepened and provides a much wider variety of services, and savings and investment instruments; and industrial policy is moving away from its early protective and regulated mode to become more competitive and market oriented. In this more complex, competitive and rapidly changing environment, it is essential that Botswana has an appropriate set of economic and industrial policies to achieve the objectives of NDP 7. This report reviews existing and possible future trade and industrial policies -- making recommendations for changes which might be appropriate for the challenges ahead.

CHAPTER 2

SURVEY OF BOTSWANA'S CONTEMPORARY INDUSTRIAL STRUCTURE

A. STRUCTURE OF OUTPUT AND TRADE

2.1 Botswana's economy has experienced continuous strong growth since independence. In the most recent year for which complete GDP data are available, 1987/88 to 1988/89 the average annual rate of growth was 9.95 percent in real terms (see chart 2.1). As indicated, this growth stems largely from the minerals sector -- particularly diamond mining -- which accounted for around 45 percent of GDP in 1989/90 (see chart 2.2). The mining sector also accounts for a large share of Government revenues. This has enabled the Government to provide infrastructure and a range of investment incentives without recourse to significant foreign borrowing.

2.2 The industrial sector (manufacturing, construction, commerce, financial and business services) has also experienced rapid growth. Between 1982 and 1991, the average annual growth rate for these sectors was 8.7 percent in real terms. The highest was finance and business services (12.1 percent per annum), followed by construction (10.3 percent), commerce (8.8 percent) and manufacturing (5.2 percent).

2.3 A detailed assessment of the manufacturing sector is difficult to make due to a lack of data about sub-sectors. Although some indication of growth patterns can be obtained from licensing data (see Annex 1, tables 13 and 14) -- little follow-up on licenses has taken place so there is no certainty that the performance of the firms has followed their licensing plans. Nevertheless the pattern of licenses suggests that the most rapid expansion was in textiles (including clothing), dairy and agro-industries, building materials, metal products and chemical and rubber industries. Solid but more moderate growth rates are indicated for plastics, electrical products, wood products and meat products. It is also noteworthy that traditional lines of manufacturing activity, tanning and leather works and handicrafts, appear to have experienced only modest growth.

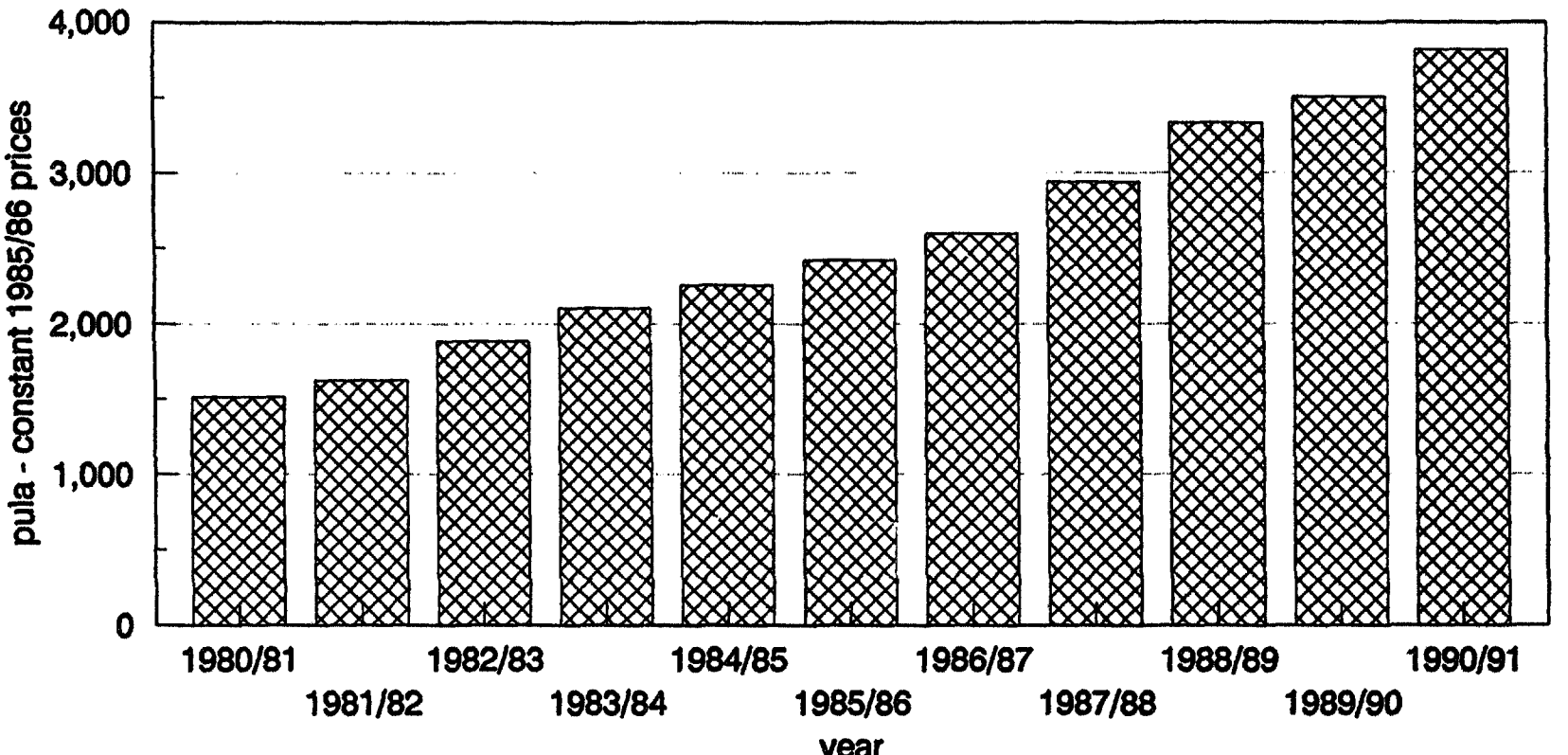
2.4 The manufacturing sector still accounts for a relatively small proportion of GDP (about 4 percent). This share rose to nearly 8 percent in the early 1980s but declined to its 1979/80 share as diamond output grew rapidly. Nonetheless, the manufacturing sector grew relatively rapidly over the past decade, permitting the sector to diversify away from a heavy dependence on the Botswana Meat Commission into a variety of other products. The growth has been in response to an expanding domestic market (51 percent), export markets (23 percent), and import substitution (26 percent). The non-BMC manufacturing equivalents are: domestic demand 54 percent, exports 8 percent and import substitution 38 percent.

2.5 These data are important as they indicate that a large proportion of industrial growth has been attributable to domestic sales (74 percent of the total -- and 92 percent of non-BMC related growth). If predictions in NDP 7 prove correct, that the growth in domestic demand will roughly halve over the plan period, then a major shift in growth toward exports will be necessary, if current rates of industrialization are to be maintained. These issues are taken up in greater detail in chapter 3.

Chart 2.1

Gross Domestic Product, 1980/81 to 1989/90

(constant 1985/86 prices)

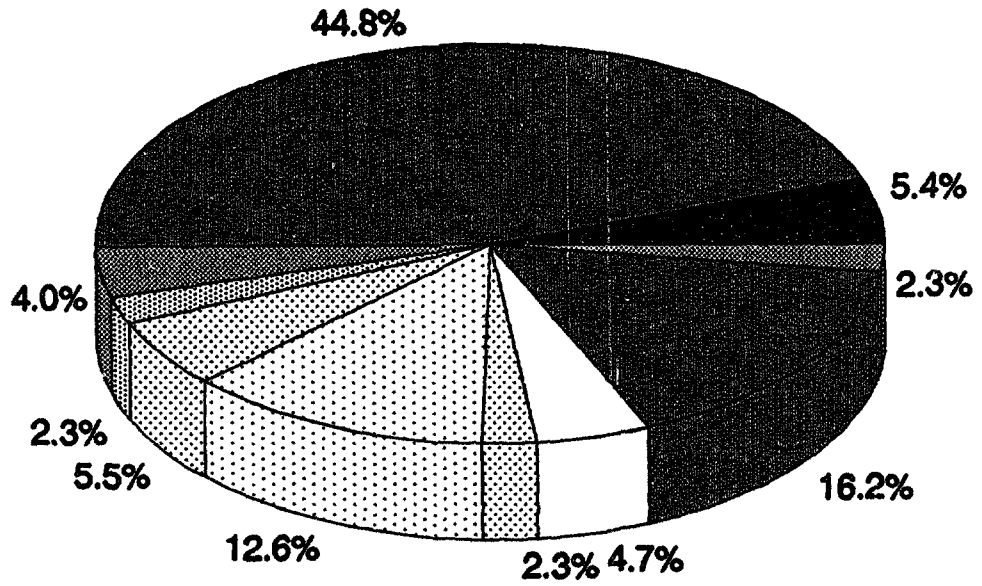


1987/88 and 1988/89 are provisional data
1989/90 is an estimate
1990/91 is a flash estimate

Chart 2.2

GDP by Type of Activity - 1989/90

(percent)



- Agriculture
- Mining
- Manufacturing
- Electricity & Water
- Construction
- Trade
- Transport & Comm.
- Financial Instit's
- Government
- Social Services

Data are estimates.
Data have been adjusted to take account of the Dummy Sector which represented -1.6%

2.6 Charts 2.3 and 2.4 provide information on trade between Botswana and major trading partners in 1989. The Common Customs Area -- mainly the Republic of South Africa -- is Botswana's main source of imports, followed by Zimbabwe and the United Kingdom. Over the period 1980 to 1989, imports from the CCA rose from P466.6 million to P2,235.5 million, those from other African countries (mostly Zimbabwe) rose from P36.1 million to P208.9 million and those from the United Kingdom rose from P7.3 million to P175.8 million.

2.7 The major destination for exports over this period (for which diamonds accounted for about 80 percent) was Europe (mainly Switzerland), followed by the RSA, other Africa (mostly Zimbabwe) and the United Kingdom. Over 1980 to 1989, exports to Switzerland rose from P239.5 million to P3,354.8 million, those to the CCA increased from P25.9 million to P112.3 million, those to other African countries increased from P32.9 million to P224.1 million, and exports to the United Kingdom rose from P8.3 million to P11.5 million, but fluctuated as high as P59.6 million in 1986. The prominence of Switzerland is a result of diamond exports -- which are mainly consigned to that country.

2.8 The data show that from 1980 to 1989, Botswana's major export markets were outside the region while most imports came from South Africa and the SADC region.

B. EMPLOYMENT, UNEMPLOYMENT, WAGES, PRODUCTIVITY AND PRICES

2.9 ***Employment and Unemployment.*** A major concern of the Government has been to create employment opportunities for a growing labor force. Of the two major economic sectors, the mineral sector is capital intensive, and employs relatively few people, while the agricultural sector is growing very slowly. New job creation in the formal and informal sectors is therefore a high priority.

2.10 The Government is the largest single employer (see chart 2.5), but its role in promoting private sector income-earning opportunities is also important. It has sought to promote private sector activities by first, establishing a favorable investment climate for private initiatives. Second, education, training and extension services have been provided to enhance the employability of the labor force and increase worker productivity. Third, social and economic infrastructure has been provided to encourage the efficient utilization of resources. Finally, policies have been adopted to ensure that the relative factor costs of production reflect their relative scarcities so that labor intensive sectors and technologies are not penalized by subsidized capital and infrastructure.

2.11 Despite constraints to employment growth in the mineral and agricultural sectors, economic opportunities have grown rapidly and formal employment has been growing roughly in proportion to gross domestic product (see chart 2.6). From August 1982 to March 1991, formal sector employment grew from 100,200 to 222,700 -- an annual rate of 9.2 percent per annum compared to a real GDP growth rate of 8.1 percent per annum. All sectors experienced increases in employment although growth in some was only modest.

Chart 2.3

Direction of Trade - Exports, 1989

(percent)

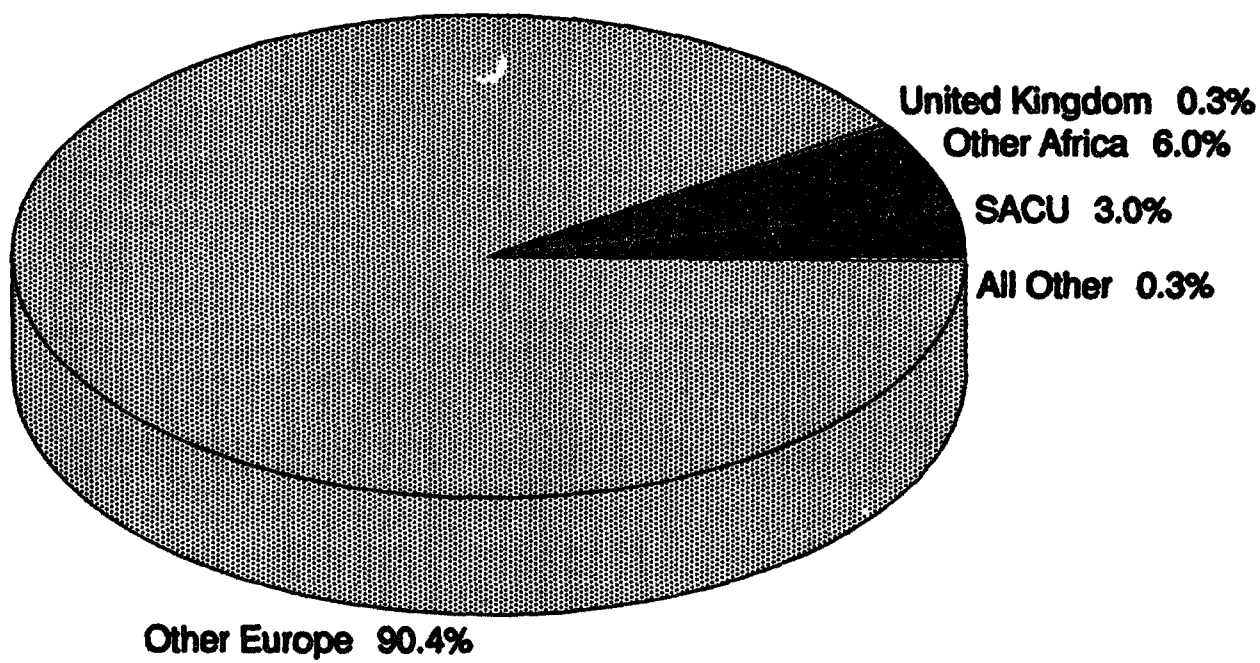


Chart 2.4

Direction of Trade - Imports, 1989

(percent)

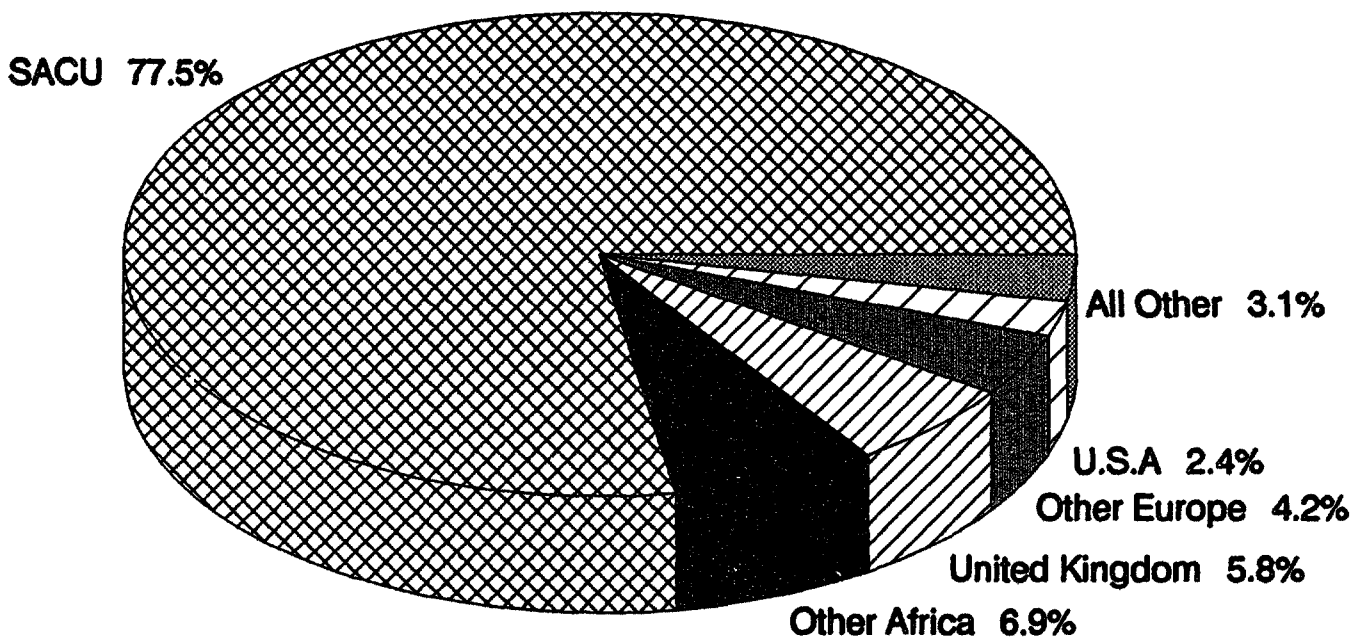


Chart 2.5

Employment by Sector

(September 1991)

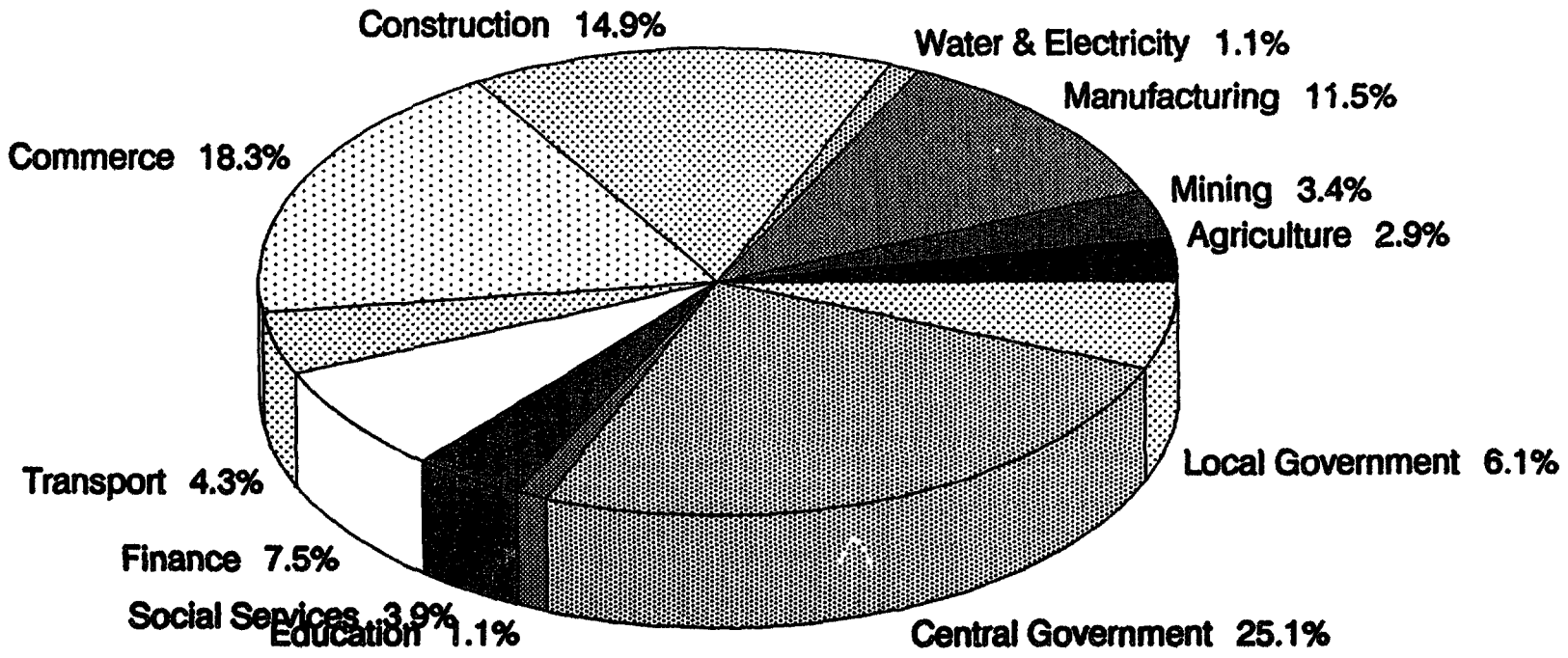
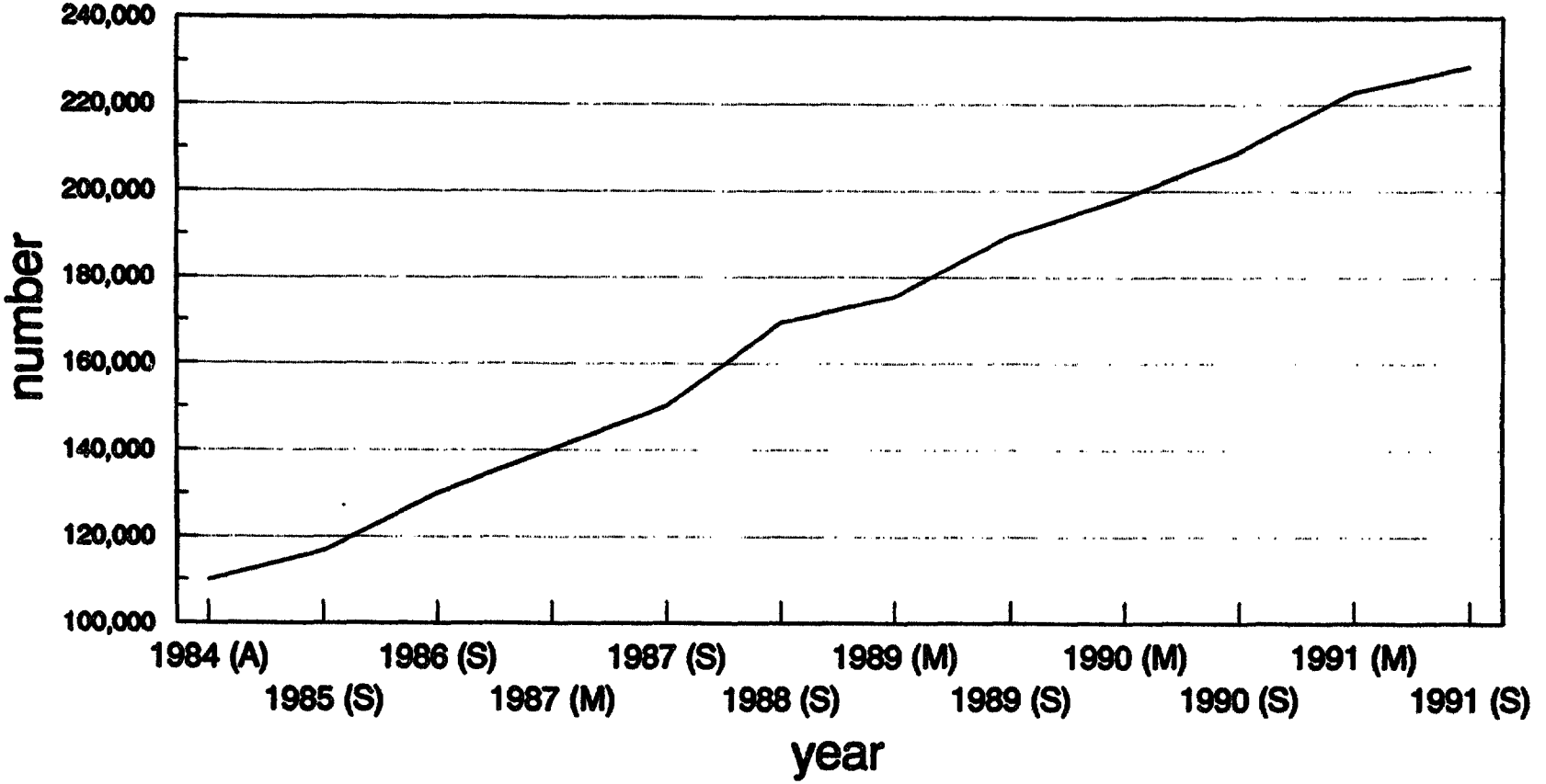


Chart 2.6

Formal Sector Employment

(1984 to 1991)



Data are for varying periods ending in March (M), August (A) and September (S)

2.12 Although the labor force is dominantly male, the participation rate of women has increased, especially over the last two years. The participation rate of women in formal employment reached 34 percent in 1991 -- which was above the world average and high by Sub-Saharan standards. Non-citizen employment has also increased substantially, from 5,100 in September 1985 to 11,380 in March 1991. Most of this increase occurred after 1986 as the economy's rate of growth accelerated and requirements for skilled manpower expanded rapidly. The number of Batswana working in South African mines declined from 21,000 in September 1986 to 17,400 in March 1989. It is possible that many of these will return to Botswana in the near future, thereby placing an additional strain on the local employment market.

2.13 Employment in the industrial sector grew at an annual rate of 11.7 percent from August 1982 to March 1991, rising from 43,100 to 117,000 -- representing over half of total formal sector employment. Employment in the public sector has been growing at a slower rate of 7.9 percent per annum compared to 9.9 percent per annum in the private and parastatal sectors over the same period. The major growth areas for employment in the industrial sector since 1981 have been manufacturing (15.3 percent per annum), construction (10.6 percent), commerce (10.6 percent) and finance and business services (12.3 percent). It is the Government's intention to pursue investment, price and wage policies that will maintain and further increase employment in these sectors.

2.14 Unfortunately, reliable *unemployment data* are not collected in Botswana on a regular basis. It is therefore difficult to track recent developments. Nonetheless, the growth in formal sector employment is known to have averaged around 10 percent per annum throughout most of the 1980s -- with lower growth in the early 1980s and faster growth in the second half of the decade. The rate of growth in the population has been 3.4 percent -- which is well below the rate of growth of the labor force. However, the rate of urbanization, as a consequence of rural-urban migration has also been very rapid. Estimates of the size of the labor force, based upon a 1984/85 Labor Force Survey, indicate an estimated labor force of around 428,000 workers in 1991 (see table 2.1).

2.15 A recent study "*Micro and Small-Scale Enterprises in Botswana*" found that between 53,000 and 88,000 workers were employed in the small and medium scale sector -- unaccounted for in the formal sector employment figures. These enterprises were mainly in rural areas (69 percent) and are mainly involved in trade and manufacturing activities. In addition, estimates, based upon the 1981 Census, indicate that more than 150,000 workers are employed in traditional agricultural activities. In contrast to workers in small and medium scale enterprises -- who typically work 11.5 months per year, and 27.9 days per month -- workers in traditional agriculture experience substantial fluctuations in work patterns. Long periods of under-employment are followed by intense periods of activity, in response to seasonal activity in the sector.

2.16 During 1991, total formal sector employment is known to have reached 220,000. In combination with (an estimated) 70,000 workers in the informal sector and, at least, 150,000 workers in traditional agriculture -- Botswana's estimated labor force of 428,000 was close to fully employed.

2.17 The available unemployment data over the 1980s also supports the position that the unemployment problem has been declining over the decade. Data from the 1981 Census

indicates that, in that year, unemployment was 20 percent. If discouraged workers are excluded from this estimate (workers who are no longer seeking work but who are still unemployed), the unemployment rate was 14 percent. The next available data is from the Labor Force Survey in 1984/85, which indicated that by the middle of the decade, total unemployment had increased to 25 percent, and the rate excluding discouraged workers had risen to 16 percent. This increase was a consequence of an on-going drought, and the effects of the world recession -- which impacted on diamond sales. The most recent estimates, which are from the 1991 Population Census, indicate that the unemployment rate had fallen significantly to around 14 percent by 1991.

Table 2.1: Population, Labor Force, Employment, and Unemployment Trends 1984 to 2001

	1984	1986	1991	1996	2001
Population (de facto)	1,049,000	1,128,000	1,334,000	1,567,000	1,822,000
Working age population	506,000	544,000	651,000	792,000	968,000
Estimated labor force (15-64 years)	368,000	393,000	428,000	503,000	618,000
Formal sector employment	110,000	130,000	207,400	298,000	398,000
Average annual growth		8.7	12.3	6.2	6.0
Estimated traditional agriculture	121,500	153,500			
Estimated informal employment	43,400	47,000			
Total employment	274,900	330,500			
Estimated unemployment	93,100	62,500			
Unemployment rate	25.3	15.9			
Formal sector/labor force ratio (%)	29.9	33.1	48.4	59.2	64.4

Source: T. Nyamadzabo, *The Human Factor: How can Botswana Ensure that there is Adequate, Appropriately Trained and Motivated Labor Force*, paper prepared for the 1991 Francistown Conference on Private Sector Development.

2.18 Hence, a clear picture emerges of high rates of unemployment at the beginning of the 1980s, which continued to rise throughout the first half of the decade, but which fell steeply by the early 1990s. By 1991, employers were reporting shortages of unskilled workers, although this undoubtedly, in part, reflects structural and frictional employment problems. This situation is known to have reversed somewhat in 1992, with the impact of the international recession. Lay-offs have been reported, and the construction boom has slowed down considerably -- inevitably leading to an increase in the unemployment rate in 1992.

2.19 Although it is difficult to be precise, given the lack of available data, it seems clear that the absorption of large numbers of unskilled workers is not as pressing a concern, as

it was in the early 1980s. There will certainly be an on-going need to create employment opportunities for unskilled workers, but it may well be possible for policy makers to extend their vision of the development of the industrial sector more broadly, to include the encouragement of a wider range of activities, rather than focussing as much on the development of labor-intensive manufacturing industry as has been necessary in the past.

2.20 *Wages*. The original Incomes Policy of 1972 adopted a clear position of wage restraint in the labor market. The aims of Government intervention, with respect to wages, were to promote the objectives of rural development and employment creation, and to limit monopsonistic pricing in labor markets and monopolistic pricing in product and housing markets. Structural limitations -- such as the small size of the market, and underdeveloped infrastructure -- having restricted the effectiveness of competition.

2.21 However, as the economy has grown and diversified, Botswana has been transformed from predominantly rural-based into a rapidly growing modern economy. Areas where market failures are likely to cause problems have now diminished. Hence, at the end of the 1980s, it became appropriate to review the policy and its implementation mechanisms again.[1] This review culminated in Government Paper No.1 of 1990, *The Revised National Policy on Incomes, Employment, Prices and Profits*, which outlined revised policies in five broad areas.

2.22 It was decided to allow relative wages between urban and rural areas, and salaries among Government, parastatals and the private sector, to primarily reflect market forces. Parastatals are allowed some wage freedom within broad limits set by Government. The salary structure within the Government was also decompressed in order to retain qualified executive personnel. The modified wages and salaries structure now rewards greater responsibility and offers attractive incentives to develop professional and technical manpower. Higher rewards should also induce students to choose vocational, technical and professional courses of study -- thus increasing the supply of scarce skills.

2.23 The minimum wage system establishes differentials according to major industries and occupations. These wages are only applicable to employees in the formal sector. The overriding need in the urban and rural informal sectors is to create income-earning opportunities, many of which will be for self-employed and casual workers. As informal sector employment is often of low productivity, the application of a minimum wage -- which would be largely unenforceable -- could unnecessarily limit job creation.

2.24 The Government has also agreed to use the Poverty Datum Line (PDL) as a new guideline, among other factors, in determining minimum wages. In order to develop an appropriate relationship between the minimum wage and the PDL, the PDL must be adjusted for direct cash income and the number of wage earners in a household. The minimum wage derived on this basis is also adjusted for cost of living changes.

2.25 Minimum wages vary by industry and occupation (see table 2.2). As at May 1991, the highest minimum wage was P1.03 per hour. Minimum wages have increased steadily from 1980 to 1991, largely to adjust for changes in the cost of living. For the construction,

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[1] The *National Policy on Incomes, Employment, Prices and Profits* had previously been reviewed and revised in 1976 and 1982/83.

manufacturing, hotel, garage and motor trades, the minimum wage increased from 36 thebe per hour to P1.03 per hour -- an average annual increase of 10 percent. For the wholesale and retail trades it increased from 36 thebe[2] per hour to 97 thebe per hour in May 1991, an increase of 9.4 percent per annum. This compares with nightwatchmen for whom the minimum wage increased from 26 thebe per hour to 81 thebe per hour, an increase of 10.8 percent per annum. Normal working hours are 8 to 9 hours a day -- or about 45 hours a week. Hours worked over and above normal working hours on a rest day or a paid public holiday are charged at double the basic wage.

Table 2.2: Minimum Hourly Wage Rates (thebe per hour)

	August 1980	June 1985	May 1991
Building, Construction, Exploration and Quarrying	36	56	103
Manufacturing, Service & Repair Trades	36	56	103
Wholesale Distributive Trades	36	50	97
Retail Distributive Trades	36	49	91
Hotel Catering & Entertainment Trades	36	56	103
Garage, Motor Trades & Road Transport	36	56	103
Retail & Wholesale, Night Watchmen	26	37	81
Night Watchmen (excl. Retail and Wholesale)	26	43	81

Source: Ministry of Finance and Development Planning, Botswana.

2.26 Average real wages have been increasing rapidly over the period 1980 to 1991. The highest annual growth rates were recorded in the formal agricultural sector (4.0 percent), followed by mining and quarrying (3.4 percent), education (2.2 percent) and electricity and water (2.1 percent). However, from 1980 to 1986 there was a decline in real earnings for many sectors. Real earnings increased from 1986 onwards, reflecting growth in diamond revenues and the end of the drought. Most of the rapid increase from 1986 to 1991 occurred in the formal agricultural sector (12.9 percent), water and electricity (7.6 percent), construction (5.7 percent), transport and communication (11.8 percent) and local government (7.2 percent).

2.27 The average annual monthly real cash earnings of citizens employed in the private and parastatals sectors grew by 1.3 percent compared to a decline of 1.3 percent for non-citizens over 1980 to 1991. This led to a modest narrowing of the gap between citizen and non-citizen earnings -- although earnings of non-citizens remained much higher due to the technical and professional nature of these employees. Expatriate recruitment and remuneration has always been

[2] 100 thebe equal one pula.

a source of concern among Batswana as inducement allowances and other benefits offered to expatriates have tended to boost their overall compensation far above compensation levels of citizen workers doing the same job. Nonetheless, some inducement is necessary to recruit expatriates in areas where skills are in short supply.

2.28 Recently, the Government abolished the previously used system for determining expatriate benefits (based upon the British Overseas Services Aid Scheme (OSAS)) -- and expatriate salary packages in Government and parastatals are to be rationalized. De-compressed salary scales at senior and management levels should provide sufficient attraction to engage most expatriates without the need for extra supplementation. Depending on the type of expatriate skill required, Government and parastatals will be free to negotiate the level of inducement supplements, subject to certain limitations.

2.29 ***Productivity***. There is concern over the low, and possibly declining, levels of labor productivity in the private and public sectors. Given the central role of productivity in future economic development, Government intends to establish a National Productivity Center that will focus on improving productivity. There has not been, as yet, any serious attempt to collect disaggregated data on labor productivity in all sectors of the economy. Changes in productivity levels can only be crudely ascertained by dividing sectoral output by number of employees.

2.30 Taking the crude measures as calculated for five sectors -- manufacturing, construction, commerce, finance and business services -- the later three sectors have a much higher and more rapidly growing productivity than manufacturing and construction. In the latter sectors, the trend has been more or less constant. As already noted, these measures should be treated with caution.

2.31 ***Labor Market Information***. It will be important for the authorities in Botswana to develop a better understanding of the dynamics of the labor market, as well as increasing the robustness of labor market data. For example, the available data indicate that the growth of employment in manufacturing has been twice as fast as the growth of output in the same sector, which intuitively seems unlikely. The cause for this apparent distortion is not understood, although it may well be related to industrialists over-stating employment levels because of the connection between Government grants under the FAP program and employment levels in manufacturing. In addition, the data suggest possible "over-employment" in Botswana, when one takes employment in the informal and traditional agricultural sectors into account -- again a result which does not seem likely. The quality, and frequency of data related to unemployment and productivity, also requires urgent upgrading. Better quality, and more timely information on labor market issues will assist policy makers in adopting the most appropriate policy decisions with respect to wages and employment.

2.32 In addition, changing economic circumstances and lower rates of growth in the economy generally, may mean that unskilled labor is not as rapidly absorbed in the future as it has been in the recent past. Rates of rural-urban migration may be faster or slower than what they have been during the 1980s. Skill levels of workers in the manufacturing sector may be increasing at a pace which permits the growth of more sophisticated manufacturing activities. Developments such as these will also impact upon policy decisions with respect to employment. To assist policy makers in making the most appropriate decisions, it will therefore be necessary to develop a better understanding of the characteristics of the four main segments of the labor

force -- the formal employment sector, the informal sector, traditional agriculture, the unemployed -- their dynamics over time, and the interactions between them.

2.33 *Cost of Living*. As noted in NDP 7,

> "While there were significant fluctuations, the average increase over the period September 1985 to December 1990 was 10.4 percent. The rate of inflation began increasing in 1988, and peaked at 12.5 percent in June 1989, at which point the Pula was revalued by 5 percent against other currencies. Subsequently, the rate of inflation subsided until the Gulf conflict erupted, whereupon it increased from about 10 percent to 12.8 percent per annum at the end of 1990".

From December, 1990 to December 1991,the change in the cost of living index was 12.6 percent (see chart 2.7).

2.34 Imported inflation -- especially from South Africa and Zimbabwe -- is the primary factor increasing the cost of living. The depreciation of the pula against other currencies in 1990 and 1991 also contributed to the increase. The use of the exchange rate alone has proved inadequate to curb inflation. In order to keep prices from rising rapidly, fiscal policy and containment of domestic resource costs will be used, particularly through improvements in the productivity of workers and local producers. Movement to positive real rates of interest will also dampen the demand for credit with a concomitant beneficial impact upon inflation.

2.35 There have been some changes announced by the Central Statistics Office (CSO) regarding the cost of living (COL) Index as measured by changes in consumer price indices. First, a new COL index has been introduced with a new base, replacing the old series. Second, the weighting system has been revised, based on later expenditure data contained in the 1985/86 Household Income and Expenditure Survey. Last, the basket of goods and services has been revised and extended from 152 to 235 items.[3]

2.36 Food has been assigned a lower weight in the new basket -- only 27 percent of average incomes are estimated to be spent on food items, compared to 37 percent in the old basket. On the other hand, the proportion of income spent on drink and tobacco has increased three fold. Similarly, a greater proportion of expenditure is now allocated for housing and household operations, medical care and transport -- compared to clothing and footwear. These changes reflect the growth of incomes in the last six years which has led to a shift from basic necessities toward goods and services that could be considered luxuries.

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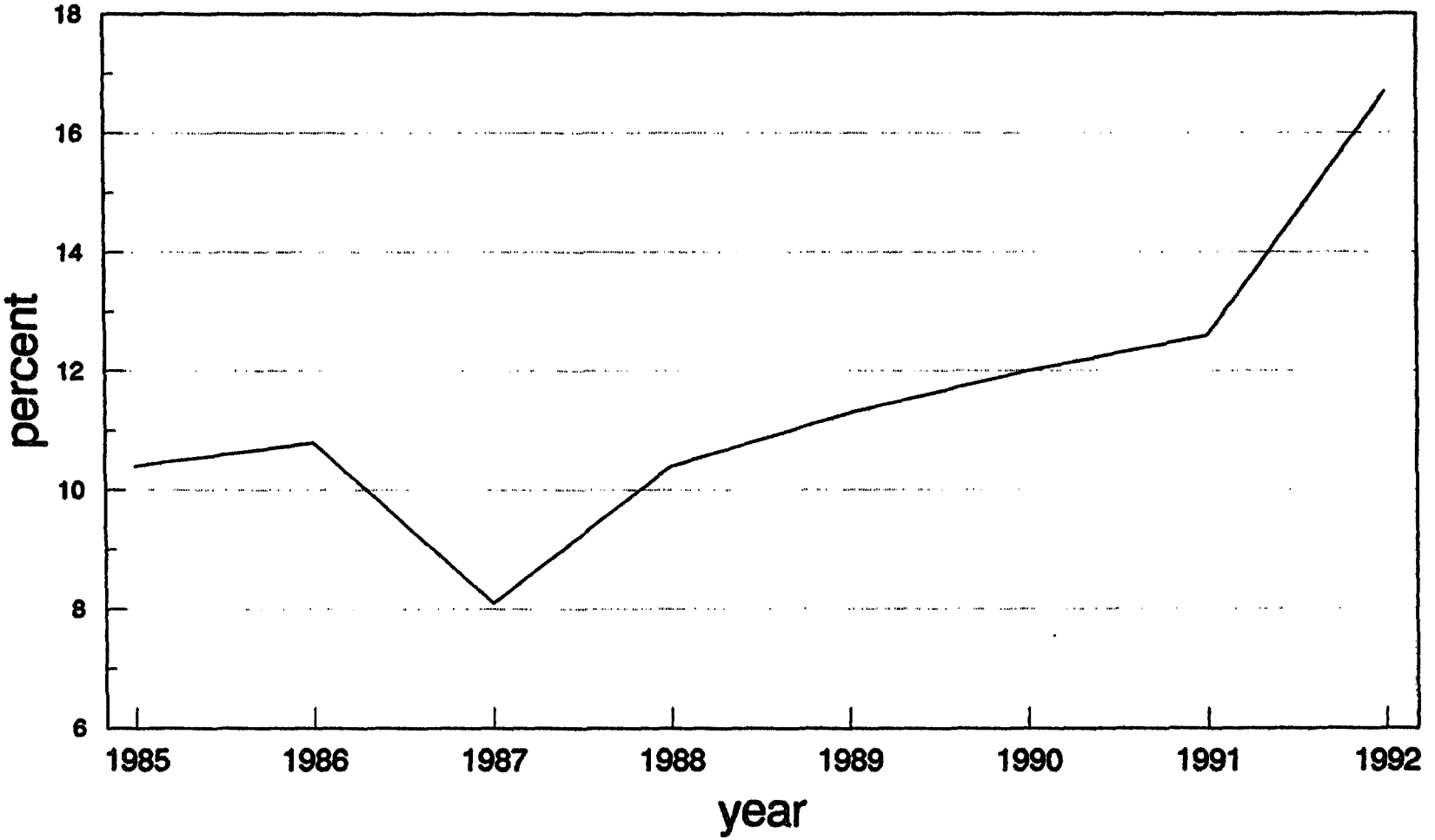
[3] Table 12 in annex I, shows relative weights of sub-groups in the COL baskets with September 1985 and November 1991 as bases, respectively.

Chart 2.7

Annual Rate of Inflation - 1985 to 1992

(percent)



C. THE INDUSTRIAL SECTOR

2.37 *Company Formation*. Company formation has been very rapid in Botswana, particularly over the past two years (see table 2.3). The Companies Act of 1959 governs company formation. This legislation distinguishes between private, public and external companies -- the most common form being the private company. This Act is now being amended and updated to ensure that books of account are maintained in Botswana, that there is a resident auditor, and that reporting requirements are improved.

2.38 *Industrial Property Legislation* covers laws regarding copyrights, patents, design protection and trade marks. Under these laws an investor or trader -- whether a Botswana citizen or not -- is obliged to first apply for and be issued a patent or industrial design or trade mark registration in the United Kingdom or South Africa. Only then may they be registered in Botswana. The local legislation simply extends the protection provided in those countries. New legislation is being developed to permit the original registration of intellectual property in Botswana and to bring the coverage into line with international standards.

Table 2.3: Number of Newly Registered Companies

Year	Number
1985	862
1986	1,055
1988	1,101
1989	1,370
1990	1,856
1991	2,212
1992 (up to 13th March)	444
TOTAL	8,800

Note: A breakdown of registered companies by sub-sector is not available. Estimates from the Central Statistics Office indicate that manufacturing firms accounted for 15 - 20 percent of newly registered companies during NDP 6.
Source: NDP 7.

2.39 *Manufacturing Sector*. The Ministry of Commerce and Industry has the primary responsibility for policies and programs affecting the manufacturing sector -- the only major program for which it is not responsible is the FAP program for large scale business. The Ministry administers the *Industrial Development Act of 1968* and the Infant Industry Protection clause of the Southern African Customs Union Agreement. The Ministry also inspects

manufacturing industries to ensure that licenses are used for their intended purpose. It also checks against illegal manufacturing practices. The *Industrial Development Act of 1968* has been the main tool for regulating industrial development in Botswana. During NDP 6 and prior to 1988 all manufacturers with more than twenty-five horse power of installed equipment were required to have a manufacturing license.

2.40 The Act was comprehensively reviewed in 1988 and extensively modified. The main change was the establishment of an independent *National Industrial Licensing Authority* with membership appointed by the Minister of Commerce and Industry. The Authority is responsible for the issuance of licenses to manufacture any product for sale at any place in Botswana and, where necessary, the suspension or cancellation of such licenses. It also reviews and advises on industrial development policy and is responsible for the inspection of industrial enterprises to ensure that they comply with regulations made under the Act and the labor law. It also collects information required to monitor industrial development.

2.41 The 1988 Act required all locally-owned manufacturing enterprises employing ten or more people and/or using 20 kw or more of any form of energy, to obtain an industrial license from the Ministry of Commerce and Industry. All non-citizens require such a license, irrespective of the number of employees or the horse power of their machinery. The applicant must be specific in the description of the product to be manufactured and should a manufacturer wish to extend the product range, or introduce a new product, a new license is required.

2.42 The 1988 Act permitted the granting of an exclusive license in special circumstances -- thus preventing the establishment of any competition. Such licenses were granted for a maximum period of four years but can be extended for an additional four years. Three companies were given such a license during NDP 6. This policy is currently being reviewed.

2.43 In order to promote the active participation of citizens in industrial development, the Government implemented an industrial reservation policy. A number of industries, which require relatively simple technological skills and low levels of capital, were reserved for citizens. These include the manufacture of school uniforms and school furniture, burglar bars, protective clothing, cement and baked bricks, and the milling of sorghum and the baking of bread. The rapid increase in the number of citizens operating in these enterprises reflects growth in local entrepreneurial talent (table 13, annex I).

2.44 Despite increased participation by citizens in industrial development -- the ownership of formal sector enterprises remains concentrated in foreign companies. Local ownership is fairly limited and is usually in the small scale sector. The constraints citizens face include: lack of capital; competition from imported products; and a lack of entrepreneurial skills (see chapter 4). Most major manufacturing firms are wholly or partially foreign-owned. Where joint ventures do exist, they are frequently between foreign investors and the Botswana Development Corporation. Foreign investment is needed to provide employment and technology -- and to train Batswana for positions at all levels of technical and management expertise. Over time, it is expected that the relative share of citizen owners and entrepreneurs in the workplace should gradually increase.

2.45 During NDP 6 the number of companies licensed increased steadily. Investors were drawn by the favorable investment climate and liberal licensing procedures. They tended

to locate in regions with better infrastructure, larger markets and good transport links. This has meant that manufacturing firms are highly concentrated in urban areas. There are very few industries in the semi-arid areas of central and western Botswana. Similarly, the north west, with forest and agricultural resources, has undeveloped potential because of long distances to markets and inadequate infrastructural support.

2.46 *The Trading Sector*. The *Trade and Liquor Act 1986*, requires that individuals who engage in any trading activity must operate with a license. Trading licenses and liquor licenses are differentiated in the Act. As in the case of manufacturing licenses, some activities are reserved for citizens -- including fresh produce, general dealers, butcheries, bars and bottle stores. The National Licensing Authority, MCI is responsible for the issue and renewal of licenses for agents, hotel liquor, auctioneers, drillers, exporter/importers, and external representatives. Local Authorities, which are located at city, district and town council offices, issue and renew licenses for dry cleaners, filling stations, fresh produce, pharmacists, garage/workshops, general trading, hair dressers, motor dealers, travel agents and other local businesses.

2.47 Information on the patterns of licenses is given in tables 16 to 19 in Annex 1. Certain licenses issued -- especially from 1987 to 1989 -- have not been renewed and it is assumed that these businesses are no longer operating (of a total of 145 licenses issued by the National Licensing Authority, only 124 are operational).

D. RURAL INDUSTRIAL DEVELOPMENT

2.48 The Government is committed to rural development and considers industrialization to be an important component of its rural development strategy. In the past, the rural strategy concentrated on the provision of basic infrastructure such as education, water supplies, health posts and clinics, and the provision of transport and communications links. Substantial mineral revenue enabled the Government to provide these services fairly rapidly. More recently, rural development strategy has focused on low income levels in rural areas, and the need to create additional income earning opportunities for rural dwellers.

2.49 The Government aims to promote development in all parts of the country and to avoid excessive concentration of industries in urban areas. Industrial and commercial development is encouraged in large villages through the activities of the Integrated Field Services (IFS), youth brigades and non-government organizations. The IFS, a division in MCI, focuses on entrepreneurship, technical and business training, and provides marketing assistance. It also implements and monitors the small-scale Financial Assistance Policy.

2.50 The creation of income earning opportunities in rural areas is being assisted by a number of initiatives including:

(a) Strengthening the institutional capabilities of the IFS stations and establishing new stations.

(b) Channelling funds to Rural Industries Promotions (RIP) for development and the adaptation of appropriate technology.

(c) Extending FAP to certain service industries.

(d) Constructing more factory shells.

(e) Identifying foreign and domestic marketing opportunities.

(f) Promoting rural/urban economic linkages.

E. CONCLUSIONS

2.51 During the last half of the 1980s Botswana's economy grew and diversified rapidly. While many African countries experienced a decline in manufacturing output, and low capacity utilization, Botswana enjoyed rapid growth and high capacity utilization. This was in response to rapidly growing incomes, strong domestic demand and the availability of foreign exchange to purchase imported raw materials and consumer goods. A wide range of manufacturing firms were able to operate at high capacity levels throughout the period -- with the major constraint on further development being a shortage of serviced factory space.

2.52 In the early 1990s, however, several important developments have taken place which will impact upon future growth. The first of these is a lower rate of growth in the domestic market anticipated over the NDP 7 plan period. The second is the external environment. With easily available foreign exchange and a strong currency, the Botswana market is open to foreign competitive pressures which are particularly severe from large regional economies such as South Africa and Zimbabwe. In the broader international sphere, rapid increases in manufacturing productivity are combining with new trading arrangements, and new sources of supply from Asia and Eastern Europe, to create highly competitive markets.

2.53 With a small internal market, many firms in Botswana are rapidly reaching the stage where they need international sales if they are to expand further. The required standards of competitiveness are therefore those of the regional and international markets and not those of the relatively easy and affluent domestic market in Botswana. The pressure to increase productivity and competitiveness is consequently increasing.

2.54 The next stage of industrial growth will probably, therefore, be more difficult. The first stage of industrial expansion, carried by a wave of high income from the resource industries, responded primarily to domestic demand and to domestic requirements for labor intensive employment of unskilled labor at relatively high wage rates. The next stage will require industry with higher productivity, lower labor intensity, and higher skilled employees -- if it is to meet the competitive pressures in domestic and international markets. The challenge therefore, is to define a pattern of development -- and corresponding policies -- that will respond to both the need for competitiveness and the need to employ an unskilled labor force.

CHAPTER 3

INTERNATIONAL TRADE AND FOREIGN INVESTMENT: IMPLICATIONS FOR BOTSWANA'S INDUSTRIAL DEVELOPMENT STRATEGY

A. INTRODUCTION

3.1 Botswana's trading relationships within the region have been largely influenced by its long-standing membership in the Southern Africa Customs Union (SACU) and, to a lesser extent, its involvement in a bilateral trade agreement with Zimbabwe. Botswana's participation in the Lomé Convention and other preferential export arrangements as well as SADC regional development cooperation programs, have also been significant. These and other institutional arrangements affecting Botswana's international trading relationships are reviewed in this chapter. This is followed by a review of foreign investment in Botswana.

3.2 Subsequent sections appraise the outlook for Botswana's regional economic relations based on recent and prospective developments with respect to the SACU Agreement (SACUA) and other factors likely to affect the regional environment for international trade and foreign investment. Some statistical comparisons are made between Botswana and other countries in the Southern African region. While the substance and timing of changes in the framework for regional economic interactions cannot be predicted with much confidence at this early stage in the adjustment process, it is nevertheless clear that Botswana's economy will be substantially affected -- particularly with respect to its industrial development potential. The concluding section summarizes the implications for formulation of Botswana's future industrial development strategy and indicates some aspects of economic research and policy analysis that need to be addressed.

B. REVIEW OF INTERNATIONAL TRADE

3.3 Botswana's international trading relationships have been shaped to a considerable extent by SACUA, which links Botswana, Lesotho, Namibia, Swaziland and South Africa in a customs union. External trading relationships, particularly those with countries in the Southern African region, have been shaped by the provisions of the customs union agreement. Of particular importance are the common external tariff and excise tax schedules which, under the current agreement, are set by RSA.

3.4 ***Brief History of SACUA.*** The current status and future prospects of SACUA can best be understood in a historical context. Since its inception in 1910 (when the Union of South Africa was initially established, and when Botswana, Lesotho and Swaziland were separate protectorates) this agreement has provided for a common external tariff structure, for duty-free movement of goods within the CU area, and for rights of transit across RSA territory for imported goods consigned to the other three smaller, land-locked members. Furthermore, it was originally provided that revenue to the Governments of Botswana, Lesotho, and Swaziland would be based on their respective historical contributions to total regional imports (which, for Botswana in 1910, was estimated at 0.28 percent, and subsequently amended to 0.31 percent in 1965).

3.5 When the Bechuanaland Protectorate became the independent nation of Botswana in 1966, the highest priority for the new Government was an adequate and reliable source of revenue. As the formula for determining revenue to be paid to the BLS was, by then, grossly out of line with the imports attributable to the national markets, in the latter part of the 1960s,

Botswana, Lesotho and Swaziland, called for a re-negotiation of SACUA. The governing document was amended in 1969, with the result that large increases were achieved in the revenue received by the BLS countries. The new formula remained based on their respective annual share of imports. Furthermore, RSA agreed to provide compensation to the BLS for certain effects of the customs union.

3.6 The specific effects of SACUA, recognized as warranting compensation from RSA, in addition to the up-dating of the statistical basis for computing revenue, included:

(a) the "price-raising effect" on imports into the BLS countries caused by the common tariff (as set by RSA), and the protection thereby afforded to RSA producers from international price competition;

(b) the "industrial polarization effect" resulting from the tendency of industries serving the entire CU market to be located in RSA; and,

(c) the "loss of fiscal discretion" on the part of the BLS, due to the fact that RSA retained the power to set tariff and excise tax rates for the entire CU.

The "compensation factor" that was agreed upon in 1969 -- as an offset for these effects -- was 42 percent of the "revenue share". As a result the BLS country revenue base was multiplied by 1.42.

3.7 There were other disadvantages of SACUA for the BLS countries which were not explicitly taken into account in the 1969 arrangement. The most significant of these were:

(a) A serious time lag in the distribution of the revenue. This is due to the procedures involved in collecting, presenting and agreeing on the pertinent import statistics, which causes the payments to be delayed initially for two years and then subject to further adjustments in the ensuing two years. The result entails, in effect, an interest-free loan to RSA for the duration of the lag.

(b) The scope for the BLS countries to provide protection for their "infant industries" is limited. Narrowly defined eligibility criteria and the provision that all duties collected revert to the RSA Treasury made this industrial promotion technique extremely expensive for the BLS.

3.8 Nevertheless, compared to the previous formula, the 1969 formula provided Botswana with rapid revenue growth during the 1970s and 1980s, because the new provisions fortuitously became effective just before the import-intensive construction boom initiated by Shashe, Orapa and other smaller mining projects in the early 1970s. The result was a dramatic increase in Botswana's receipts from the revenue pool -- from R3 million in 1967 to R50 million in 1975 -- or from about 20 percent to 50 percent of Government's total revenues for these years.

3.9 A further significant change in the revenue formula occurred in 1977 when the "stabilization factor" was introduced. Payments to the BLS had fluctuated substantially as a result of adjustments in RSA's external tariff and excise tax policies with respect to certain imports such as petroleum. These variations around a mean of 20 percent of imports, were dampened, and constrained by a 17 percent lower boundary and a 23 percent upper boundary. This proved to

be important for Botswana because the 17 percent lower boundary rate has been applicable to the calculation of its revenue for most years since the stabilization adjustment was agreed upon.

3.10 During the latter part of the 1970s all involved parties became dissatisfied with the revenue formula for various reasons, and a decision was taken at the 1980 meeting of the Customs Union Commission (the governing administrative entity) to establish a study group to review the appropriateness of the formula and its administration. The resulting recommendations called for technical modifications in the statistical estimating procedures, for marginal adjustments in the calculation of the compensation and stabilization factors and, more generally, for simplification of the formula. The BLS countries proposed acceptance of the Study Group's recommendations at the 1982 Commission meeting, but RSA declined to agree and eventually decided, in 1984, to refer them to its own review committee, chaired by Professor McCarthy of Stellenbosch University.

3.11 The resulting McCarthy committee report, issued in 1986, acknowledged the legitimacy of some of the BLS complaints about the revenue formula and certain other aspects of SACUA -- such as the time lags in the payment of revenue to the BLS countries which resulted in interest-free loans to RSA, and the import substitution industrialization policies of RSA causing polarization of industries serving the regional markets from within RSA. The main focus of the report, however, was on the rationale for changing the formula in ways that would be advantageous from RSA's point of view. Specifically, it ignored the price-raising effect of RSA's tariff on BLS purchases from RSA and the rest of the world, and argued that the compensation and stabilization adjustment factors were unjustified. Instead, it proposed a "clean formula" which would simply divide up the customs revenue collected on imports from the rest of the world. The BLS countries unanimously rejected the recommendations contained in the McCarthy Report at the 1986 Commission meeting. In 1988 the BLS agreed, with RSA, to establish another SACUA renegotiation study group. This group, comprised of representatives from the four partner states, met several times during the remainder of the decade, without making any progress toward definition of the negotiable issues.

3.12 The result was that SACUA remained unchanged throughout the 1980s while dissatisfaction with it continued to increase. RSA remained concerned over the required revenue payments and Botswana was concerned about the inadequacy of the compensation.

3.13 Post-1990 SACUA developments are discussed later in this chapter -- following a review of other institutional arrangements governing Botswana's international economic relationships during the 1980s.

3.14 ***Botswana/Zimbabwe Trade Agreement.*** The Customs Agreement between the Federation of Rhodesia and Nyasaland, the Bechuanaland Protectorate and Swaziland -- which originally came into force in 1956 -- was the forerunner of the present-day trade agreement between the Republic of Botswana and the Republic of Zimbabwe (B/ZTA). While this bilateral arrangement was premised on mutual recognition of the benefits to be derived from free trade, following the achievement of independence by Zimbabwe in 1980, several developments generated friction in the trading relationship between the two countries.

3.15 Of particular importance was the relocation to Botswana of some Zimbabwean manufacturing enterprises -- motivated by the severity of Zimbabwean foreign exchange controls and the easier access to imported inputs in Botswana. The stresses in the relationship became

more pronounced as Zimbabwe experienced increasingly severe balance-of-payments difficulties (causing the Zimbabwean authorities to impose import quotas and tighten local content requirements on goods imported from Botswana); and, as several manufacturers in Botswana perceived that they were injured by the "dumping" practices of some Zimbabwean enterprises.

3.16 After several years of protracted negotiations, a new agreement was finally signed in October, 1988. The provisions of the amended document, and especially their administration, reflected reservations on the part of both contracting parties. In particular, Zimbabwe has continued to seek ways to prevent Botswana's SACUA affiliation from serving as a vehicle for RSA goods circumventing the more restrictive provisions of the RSA/Zimbabwe trade agreement. On the other hand, Botswana has continued to object to Zimbabwean impediments to its exports -- occasionally resorting to retaliatory measures.

3.17 The current version of the B/ZTA provides that trade in goods, certified to have been produced within the two countries, is generally to be free of customs duties and quantitative import or export restrictions. However, in order to qualify for such treatment, there are many specific qualifications and exceptions dealing with "rules of origin" and related documentation procedures, as well as limitations on transport facilities and ports of entry. As a result, the net effect of the agreement may not be substantial. Furthermore, definitions of "local content", "manufacturing processes", "direct labor costs", and so on, have generated administrative difficulties and on-going disputes.

3.18 Recently the Government of Zimbabwe has embarked upon a structural adjustment program which calls for trade liberalization and general economic deregulation. The initial macroeconomic policy reforms have been manifested in a significant real devaluation of the Zimbabwe dollar. This has made it difficult for Botswana to sell in Zimbabwe, and increased Zimbabwe's competitive advantage in the Botswana market.

3.19 *Other Institutional Arrangements*. Since 1975, Botswana's exports have been eligible for preferential treatment under the Lomé Convention -- a treaty between 69 African, Caribbean and Pacific (ACP) countries and the European Economic Community (EEC) for virtually tariff-free access by the ACP countries to the European market based upon negotiated quotas. Throughout this period Botswana has been favored with a particularly liberal beef quota (presently 18,916 tonnes per annum until the year 2000), which it has never managed to fill. Over the past two years nearly 60 percent of the beef quota has been filled, resulting in approximately P140 million per annum in export receipts from this source. Not all beef produced in Botswana is eligible for sale in the EEC market -- due to the risk of foot and mouth disease in some parts of the country. About P40 million is sold elsewhere, including some to RSA at SACU prices which are somewhat above world prices but less than the EEC price.

3.20 Botswana also benefits from the Generalized System of Preferences (GSP), a tariff reduction facility offered by industrial countries to designated lesser developed countries on limited quantities of specified LDC export products. Entitlements under this program have been particularly useful to Botswana in recent years as an inducement to Asian investors, whose home country GSP quotas (especially for the U.S. market) are filled, to engage in textile production for export under Botswana's otherwise unutilized quota. The most recent figures available show that Botswana's textile exports to the United States amounted to nearly P1.5 million in 1988. The Selebi-Phikwe Regional Development Program has made use of Botswana's textile import quota

for the U.S. market in attracting foreign investors -- and also the preferential access for Botswana manufactured goods in the EEC market under the Lomé Convention.

3.21 Botswana has so far elected not to join the General Agreement on Tariffs and Trade (GATT), largely because, as a party to SACUA, Botswana has no discretionary authority over its tariffs. However, this position has recently been undergoing reconsideration and the indications are that when the current Uruguay round of GATT negotiations are concluded Botswana will probably take the steps necessary for GATT affiliation. The decision will be influenced by an appraisal of the constraints GATT rules would impose on freedom to provide subsidies in connection with industrial employment creation programs such as the Selebi-Phikwe Regional Development program, relative to the benefits of ensuring MFN treatment in sales to GATT members.

3.22 Botswana has also elected to remain outside of the Preferential Trade Agreement (PTA), initially formed in 1981, and presently encompassing most countries in Eastern and Southern Africa. This is largely because, as a party to SACUA, it could not adopt the regional trading and related foreign investment policies on which the PTA is premised.[1] Furthermore, from Botswana's perspective, PTA's "rules of origin", which were designed to restrict trade with RSA, would yield little if any advantage for most of Botswana's exportable industrial products, due to their high RSA import content. However, the PTA is presently in the process of modifying its rules with respect to local content and foreign ownership which may change the requirements for affiliation. If this occurs, and a way is found to exempt SACU members from the granting of preferential entry to PTA goods, Botswana will need to reevaluate the costs and benefits of PTA membership.

3.23 Botswana has been an active participant in the Southern Africa Development Coordination Conference (SADCC) since its creation in 1980. The basic objective of this association of the ten "front line" states has been to reduce individual and collective economic dependence on RSA, with the coordination of regional infrastructure development projects (and related external financial assistance) being the principal means employed for pursuing this objective. While SADCC initiatives, until recently, had not focused on regional trading relationships, the 1992 summit changed the name of the organization to the Southern African Development Community (SADC). Further, the institution's programs were redirected towards a broadened concept of regional economic cooperation and integration -- perhaps including RSA -- with more emphasis on facilitation of international trade within the region.

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[1] Lesotho and Swaziland have joined the PTA and have been granted a temporary exemption by PTA to the requirement to grant preferential entry to PTA sourced goods -- which SACU does not permit. That exemption is due to expire, and Lesotho and Swaziland may soon have to choose between PTA and SACU.

Table 3.1: Imports, c.i.f. incl. duty (pula million and percent)

	1980	1985	1986	1987	1988	1989	1990
Totals (pula million)	535	1,095	1,331	1,572	2,183	2,971	3,483
percent of GDP	61.4	45.5	47.4	42.0	40.3	49.8	54.0
Categories (% of total imports)							
Vehicles & Equipment	11.8	13.7	16.7	15.4	19.2	15.7	n.a.
Food & Beverages	15.7	17.5	16.7	16.1	14.4	10.2	n.a.
Fuel & Chemicals	20.9	19.6	17.8	17.0	14.7	14.1	n.a.
Wood & Metal Products	14.2	12.3	13.0	14.0	12.5	14.5	n.a.
Textiles & Shoes	8.4	8.1	7.8	8.8	8.3	8.1	n.a.
Mech. & Elect. Products	16.4	17.0	25.7	16.6	18.6	23.7	n.a.
Other Goods	12.7	11.7	11.5	12.1	12.3	13.8	n.a.

Source: Statistical Bulletin, June, 1991.

Table 3.2: Exports, f.o.b. (pula million and percent)

	1980	1985	1986	1987	1988	1989	1990
Totals (pula million)	390	1,386	1,622	2,666	2,681	3,712	3,342
percent of GDP	44.6	57.3	57.7	71.2	49.8	61.4	48.4
Categories (% of total exports)							
Diamonds	60.4	75.6	74.2	84.4	73.8	77.1	78.2
Copper/Nickel	20.7	8.6	7.5	4.4	13.8	11.6	7.7
Meat and Meat Products	7.2	7.0	7.4	3.1	4.2	3.8	3.9
Animals & Hides	0.8	1.0	0.8	0.3	0.5	0.2	0.0
Textiles	4.0	2.1	2.7	2.2	2.2	1.0	10.2
Other Goods	6.5	5.6	7.5	5.4	5.3	2.6	0.0

Source: Statistical Bulletin, June, 1991.

3.24 ***Botswana's International Trade and Payments in the 1980s.*** As shown in tables 3.1 and 3.2, the ratio of imports to GDP has declined during the past decade -- from 61 percent in 1980 to 54 percent in 1990 -- while the export to GDP ratio has increased -- from 45 percent to 48 percent over the same period. There have been some changes over the period in the shares of various categories of imports, with "vehicles and equipment" and "mechanical and electrical products" showing significant increases. Much more pronounced has been the substantial increase in the share of diamonds in total exports -- from 60 percent in 1980 to almost 80 percent in 1990 -- with corresponding relative declines in all other export categories. The second and third largest export commodities -- copper/nickel matte and meat/meat products -- which together accounted for 28 percent of total export revenues in 1980, accounted for less than 12 percent in 1990.

3.25 Table 3.3 shows the main sources of imports and destinations of exports over the past decade. SACU countries -- effectively, RSA -- have been the main source of supply of Botswana's imports throughout the period, although the share declined from 87 percent in 1980 to 79 percent in 1989 -- with Europe accounting for most of the difference. There has been a more pronounced change in the relative share of exports going to different destinations, with Europe's share increasing from 63 percent to 91 percent -- reflecting growth in diamond export earnings -- and the USA and RSA shares declining sharply.[2]

[2] The decline in the USA's share is largely attributable to the fact that copper/nickel matte exports were re-directed from there to Norway over this period.

Table 3.3: Direction of Trade

	1980 to 1985	1986	1987	1988	1989	1990
IMPORT SOURCES (% total imports)						
RSA, other SACU	87.0	74.4	76.7	79.6	77.4	78.8
Zimbabwe	6.6	7.2	7.4	7.5	6.4	6.7
Other Africa[a]	0.1	0.3	0.2	0.2	0.6	
Europe	2.5	12.4	8.7	9.1	10.2	12.5
U.S.A.	3.0	2.8	2.8	1.9	2.3	0.6
All Other	0.8	3.0	4.2	1.8	3.0	1.4
EXPORT DESTINATIONS (% total imports)						
RSA, other SACU	6.6	5.6	5.6	4.2	5.4	3.0
Zimbabwe	3.1	3.0	5.2	3.9	6.9	6.0
Other Africa[a]	5.3	0.9	0.8	0.9	1.1	
Europe	63.4	84.7	87.7	90.5	85.9	90.7
U.S.A.	21.0	5.3	0.2	0.2	0.3	0.1
All Other	0.5	0.4	0.5	0.3	0.3	0.1

[a] Numbers for "Other Africa" in 1990 are subsumed into the "Zimbabwe" numbers.
Source: Statistical Bulletin, June, 1991.

3.26 What is noteworthy, however, is the different focus of Botswana's imports and exports. African sources of imports amounted to 95 percent and 86 percent respectively, in 1980 and 1989, while exports to African destinations amounted to only 15 percent and 9 percent, in the same two years. Thus, Botswana has become a major source of hard currency earnings for the region as a whole -- enhancing Botswana's freedom to manoeuvre in the reformulation of regional trade and related economic arrangements.

3.27 The balance of payments position over the past decade is shown in table 3.4 -- including goods ("visibles") and services ("invisibles") and transfers[3]. The substantial but variable surpluses on current account over the past six years, together with the (mostly positive) capital account balances, have resulted in a large cumulative increase in foreign exchange reserves -- to over P7.7 billion by end 1991. While this favorable situation is primarily attributable to the export earnings of the diamond industry, of which Government commands a sizeable share, there is also a less apparent but no less important relationship with Botswana's success in attracting foreign investment into the mining and other sectors of the economy.

[3] Customs union revenues are treated as *transfers* in the balance of payments accounts.

Table 3.4: Balance of Payments (pula million)

	1980	1985	1986	1987	1988	1989	1990
Visible Trade Acct.	-45	445	459	1,322	813	1,279	274
Services Account	-115	-364	-346	-501	-520	-718	-530
Net Transfers	99	170	210	284	409	443	512
Current Account Balance	-61	251	323	1,607	1,222	2,117	786
Private Capital	101	200	235	-168	-70	250	446
Government Capital	-15	-14	17	27	14	-34	-54
Banking Sector	4	53	-45	-2	-11	12	-78
Capital Account Balance	91	239	207	-143	-67	228	315
Net Error/Omission	13	11	37	-26	62	-69	7
Overall Balance	42	501	566	1,437	1,217	2,276	1,108

Source: Statistical Bulletin, June, 1991.

C. REVIEW OF FOREIGN INVESTMENT

3.28 Botswana's rapid rate of economic growth has depended, to a substantial degree, on capital provided from external sources. The mines were mainly developed by foreign investors, although Government has financed a significant part of the related infrastructure investment requirements -- by borrowing abroad. Much of the remaining investment in the private sector (with the principal exception of cattle ranching) has also been foreign financed, owned and managed -- although recently there has been increasing citizen investment in trade and transport.

3.29 ***Changes in the Structure of External Financing.***[4] At independence Botswana was almost entirely dependent on British aid which, for the most part, was tied to purchases of British goods. An important objective of Government, therefore, was diversification of foreign aid sources. The success of the initiatives taken is evidenced by the fact that the number of

[4] This section draws heavily on C. Harvey and S.R. Lewis, *Policy Choice and Development Performance in Botswana*, 1990, pages 198-209.

donors providing more than P1 million in aid to Botswana, increased from one over 1967-71 to nine over 1977-82 -- with the share of total foreign aid provided by the UK declining from 78 percent to 9 percent between these two periods. This achievement was assisted by the attractiveness of the Shashe project, and various rural development programs, to a growing number of international financial institutions and bilateral assistance agencies, as well as by demonstration that Botswana was capable of managing aid-financed projects more efficiently than many other African countries. Even though the Government's financial position was greatly strengthened during the 1980s, because of rapidly expanding diamond exports, Botswana nevertheless continued to be unusually successful in attracting foreign donor agencies.

3.30 The sustained availability of foreign aid and the increasing strength of the balance of payments has meant that Botswana has largely avoided the need to borrow externally on commercial terms -- the principal exception being a US$45 million[5] Euro-currency loan negotiated in 1978 to finance the purchase of equity in the Jwaneng diamond mine, which was not fully drawn and was repaid early. However, during the 1980s there have been substantial amounts of long-term external borrowing by Government and various parastatals, often at near commercial interest rates, from the World Bank and various other multilateral development finance institutions. Total public external debt outstanding increased from $155.6 million to $565.5 million over 1980-1990, and the debt service ratio[6] increased from 1.9 percent to 5.3 percent over this period.

3.31 Private foreign investment has always been welcomed, as a matter of official policy, and the attraction offered foreign investors has generally taken the form of a well managed and stable macro-economic environment rather than extraordinary financial inducements or tax concessions.[7] The statistical information available on the amounts, sources and allocation of private foreign investment is limited, however, and much of what is reflected in the capital account of the balance of payments does not represent new capital inflows but rather reinvested profits. Furthermore, the large mineral development projects -- Shashe, Jwaneng and, more recently, Sua Pan -- have accounted for the major share of total private foreign investment, and also for significant shares of externally-financed public investment expenditures.

3.32 From the information which is available, however, the following can be deduced. In every year but one (1987) there was a net inflow of private long term capital -- including reinvested earnings -- the cumulative total amounting to P1,426 million over the 11-year period 1980-1990. Private short term capital movements were much more erratic, with negative net amounts in 5 of the 11 years, and a net cumulative outflow of P42 million over 1980-1990. Overall, therefore, the balance of payment accounts indicate that private foreign capital inflows amounted to about P1.4 billion over the period. The relative shares of equity and debt capital in the total amount of external financing brought to Botswana by foreign investors cannot be determined from the available data, nor can the geographic sources be identified.

3.33 However, it is evident from casual observation that the largest single share of direct private foreign investment in Botswana is from firms based in RSA -- including national

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[5] Unless specified otherwise all "$" amounts in this report are United States dollars.

[6] Total Government and Government-guaranteed debt service payments : total exports of goods and services.

[7] Since 1982, the Financial Assistance Policy (FAP) has been a significant exception.

companies and subsidiaries of multinational enterprises. While this is related to the fact that the Botswana economy is closely tied to RSA by SACUA, the principal explanation is that private foreign investment is mainly in the mining sector of the economy, and it has been the large RSA-based mining companies -- most notably, the Anglo-American-DeBeers group -- which have the greatest knowledge and interest in Botswana's mineral endowment. In addition to having outstanding technical, managerial and financial qualifications for conducting mining activities in Botswana, linked to regional and international product markets, as well as considerable locational advantages in managing such activities from their RSA headquarters, there is also the fact that they are familiar with the geology of Botswana and, in several instances, had acquired long-term leases on some of the most attractive sites before Botswana achieved political independence.

3.34 Despite the advantages that Anglo-American, DeBeers and other companies have had as investors in the mineral sector, Botswana has still managed to negotiate mining concession agreements and joint venture arrangements that compare well internationally. Furthermore, the working relationships established with Government, on the one hand, and with local employees and private sector suppliers, on the other hand, have mostly been constructive and mutually beneficial. Compared with the experience of numerous other mineral dependent developing countries, the economic and socio-political dividends that Botswana has been able to derive from its relationships with foreign investors in the mining sector have been quite advantageous.

3.35 In addition to the large-scale mining sector investments from RSA, and agricultural ventures of South Africans -- some of which also have pre-independence origins -- a number of subsidiaries of RSA-chartered companies have been established in Botswana in the areas of construction contracting, small-scale manufacturing, wholesale and retail trading, and various services industries (banking and insurance, accountancy and management consultancy, transportation and tourism). Botswana has been attractive to these enterprises because of the close proximity and profitable opportunities it has afforded, and also because of prolonged economic depression and political uncertainty in RSA. Another factor has been Botswana's liberal foreign exchange control regime.

3.36 While there has been relatively little external capital investment associated with these non-mining ventures, the technology and management skills they have made available to Botswana have contributed significantly to the development processes in the private sector. It is noteworthy, however, that very little of the non-agricultural commercial activities conducted by RSA-based enterprises has been oriented towards production of exportable goods and services for the RSA market -- instead they have, for the most part, served as instrumentalities for facilitating the export of RSA goods and services to the Botswana market or, in some instances, through Botswana to other countries. A significant exception is the recent investment to develop soda ash production facilities at Sua Pan, which is oriented primarily to the RSA market.

3.37 The other principal, but much less important, source of foreign investment from the Southern African region has been Zimbabwe. Most of this investment has taken much the same form as the non-mining activities of RSA-based enterprises, and has been propelled by similar motivations. Nonetheless, some Zimbabwean investors (and possibly a few Zambians) have found Botswana a good base from which to export to their home country market -- drawing on the ready availability of inputs from RSA afforded under SACUA and the conducive policy environment and well-functioning infrastructure facilities provided by Botswana.

3.38 Along with other countries in the region, Botswana is currently trying to attract foreign investors from Europe, North America and Asia. In addition to recent investment promotion missions to preferred sources of foreign investment (such as Japan), and investigation of successful investment promotion schemes in other countries (such as Mauritius), the Government is a member of the Multinational Investment Guarantee Agency (MIGA), sponsored by the World Bank, and is eligible for the Overseas Private Investment Corporation (OPIC) insurance coverage, sponsored by the United States. It is also a member of other international organizations intended to provide reassurance to potential foreign investors. Further efforts required along these lines -- including revision of existing national policies governing foreign investment and intellectual property -- are detailed in subsequent chapters.

3.39 ***Benefits and Costs of Foreign Investment.*** Botswana has obtained significant net benefits from private foreign investment in the mineral sector. By relying on foreign equity to finance a significant portion of large, risky projects, Botswana has been able to undertake projects which would not otherwise have been possible. Some of these have been very profitable -- both for the investor and Botswana -- and some not. The terms of the arrangements have generally involved a return to the foreign investor on the risk capital, and a return to the Government of Botswana for the mineral rights in the form of taxes plus dividends on equity. In addition, Botswana has obtained access to the latest technology in mineral exploration and extraction -- again some of which has been successful and some not. Further, Botswana has gained entry to international markets on favorable terms for many of its mineral exports. On balance, the strategy of sharing risks and returns has enabled Botswana to realize a positive net benefit from foreign investment in the mineral sector.

3.40 Whether Botswana has obtained positive net benefits from foreign investment in the industrial sector is less clear. Much of the foreign investment in the non-mineral sectors has been attracted by subsidy and tax breaks under FAP and other promotional programs, including infant industry protection under SACUA. Most of these arrangements are limited in time, and founded on the infant industry concept. During the infant phase many have transferred to the foreign investor most, if not all, of the returns that would otherwise have accrued to Botswana.[8] Indeed, in some cases it is arguable that the net benefit to Botswana has been negative during the infant phase. This makes it important that, on the expiry of the infant phase, Botswana reap sufficient benefits to justify the earlier benefits foregone. If, however, the promotion of foreign investment attracts footloose industries which move on when the temporary assistance expires, then the benefits to Botswana may be zero or even negative.[9]

3.41 Part of the rationale for promoting foreign investment in industry has been to prepare the economy for the day when mineral revenues are no longer the engine of growth. The long-term viability of the assisted industries is central to this objective of diversification. Otherwise, the outcome is not sustainable. If supported new industries cannot stand on their own

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[8] Some of the arrangements also had the effect of transferring tax revenue from the Botswana treasury to the treasury of the investor's home country. Such "reverse foreign aid" arises when a tax concession is granted to an investor but, under double taxation treaties, had the tax been paid in Botswana it would have been creditable by the investor against his tax liability to his home government. Such is the case under Botswana's double taxation treaties with the UK and RSA, the two major sources of foreign investment in Botswana.

[9] Although it is recognized that even footloose industries may provide "external" benefits in the form of increased skills, a better disciplined work force, and so on.

feet without assistance, when mineral revenues dry up, Botswana's ability to provide ongoing subsidies will also cease. Then Botswana will have neither the diamonds nor the industry. In addition, if a promotional program creates an industry which is dependent on ongoing Government assistance for its survival, that action creates a constituency which will put pressure on Government to provide on-going subsidies at the end of the infant period.

D. COMPARISON OF COUNTRIES IN SOUTHERN AFRICA

3.42 Botswana's future industrial development opportunities will be conditioned by the broader regional economic context, with respect to both international trade and foreign investment. A statistical profile of the national economies in the Southern African region is given in table 3.5. As this table illustrates, Botswana is an important player in the Southern African economic league. With 1.5 percent of the SADCC country population Botswana produces nearly 9 percent of the combined GDP of the region and, in recent years, it has attracted over 52 percent of the incoming direct foreign investment. The structure of the Botswana economy, however, is significantly different from Zambia, Zimbabwe and RSA. For example, Botswana's industrial sector represents a substantially smaller share of GDP -- less than five percent compared with around twenty five percent for the other three.[10]

3.43 If RSA and Zimbabwe adopt, and successfully implement, the prescriptions being proposed by the World Bank and the IMF (supported by other sources of external financing), they will become more open to international competition. While this is likely to reduce the relative size of their import-substitution industries, it will also mean that Botswana should expect to face international price and productivity standards to a substantially greater extent than in the past. Botswana's industries would then be required to compete with the more industrialized countries in the region for markets and investment and also withstand broader international competitive pressures transmitted via the more open economies of these two large neighbors.

3.44 The potentially rapid changes in the economies of Botswana's neighbors implies that Botswana must ensure that its industrial development strategies, as well as its international trade and foreign investment promotion policies, reflect the evolving competitive opportunities, within the Southern Africa region and the international economy. This will need to be done with reference to prospective changes -- not only in the circumstances of individual countries -- but also in the institutional framework within which regional economic competition will be conducted in future. It is important for Botswana to anticipate what adjustments may be required in order to establish and sustain mutually beneficial economic relations with RSA and Zimbabwe. Therefore, an important aspect of Botswana's future industrial development strategy will be the development of capacity to monitor and appraise developments in the economies of neighboring countries, as well as refining its capacity to influence, through negotiations, the course of events with respect to changes in the institutional framework for its regional economic relations.

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[10] While manufacturing, as a percent of GDP, may be one-sixth of that of Zimbabwe and Zambia, manufacturing GDP per capita in Botswana is more than half that in those countries. Hence, the gap may not be as great as suggested by table 3.5.

Table 3.5: Southern African Country Comparisons

	Population 1989 (million)	GDP ($ bn.) 1989	GNP per capita dollars 1990	Manufac -turing (% GDP) 1989	Exports ($ bill) 1989	Foreign Direct Investment ($ mill) 1985-89
Angola	10.0	7.7	...	4	3.0	-27.5
Botswana	1.3	2.5	2,040	4	1.3	354.2
Lesotho	1.8	0.3	530	14	0.1	37.5
Malawi	8.8	1.4	200	9	0.5	1.0
Mozambique	15.7	1.1	80	n.a.	0.1	1.7
Namibia	1.8	1.7	...	5	n.a	n.a.
Swaziland	0.8	0.8	810	n.a.	0.5	192.3
Tanzania	27.3	2.5	110	4	0.4	10.1
Zambia	8.5	4.7	420	24	1.4	128.8
Zimbabwe	9.7	5.3	640	25	1.6	-20.1
SADCC Total	85.7	28.0	272	--	--	678.0
Republic of South Africa	35.0	80.4	2,530	24	23.8	-453.0

Sources: UN, World Bank, IMF, OECD and SA Statistical Service data, as reported by C. Stoneman and C. Thompson in *Southern Africa after Apartheid: Economic Repercussions of a Free South Africa*, Africa Recovery Briefing Paper, No. 4, December, 1991, published by the UN.

E. RECENT AND PROSPECTIVE SACUA DEVELOPMENTS

3.45 With respect to recent developments with SACU, it was not until early 1991 that the BLNS members of the renegotiation study group (Namibia had become a member of SACUA in its own right in 1990) were able to formulate their proposals for presentation to RSA. These included a revival of some of the same technical revisions of the revenue-sharing formula that had been rejected by RSA in 1980, and also called for increased compensation for the price raising and industrial polarization effects. The BLNS also proposed payment of interest by RSA on their lagged revenue shares; enlarged scope for protection of agricultural producers and manufacturing industries against price competition from RSA; and, better mechanisms for

participation in decision-making with regard to the level and structure of tariffs levied on imports from outside the CU area and with respect to RSA's industrial development policies.[11]

3.46 RSA responded to these combined proposals in April, 1991 by informing the BLNS countries of its unilateral decision to suspend the terms of reference for the study group. The rationale for, and implications of, this decision were stated by RSA as follows:

> "An in-depth analysis of the very comprehensive proposals has revealed that, viewed against the industrial development needs of the customs union area as a whole, the 1969 Customs Union Agreement has become an out-dated instrument for economic cooperation in the area. Furthermore, cosmetic amendments .... will not address the real underlying problems faced in particular by the less developed members of the Union. The divergent development needs of the contracting parties therefore require a collective reflection on the most appropriate forms of economic cooperation which will ensure optimum economic development in the region. Such forms may even extend beyond the current boundaries of the Union".

This statement was accompanied by the announcement of a unilaterai decision to suspend indefinitely the terms of reference of the Study Group pending the outcome of the *collective reflections*, and by a proposal that in the meantime, "the Agreement in its present form should continue to be applied."

3.47 The RSA position was subsequently explained more fully in a formal statement presented at an extraordinary meeting of the Customs Union Commission convened in Swaziland in June, 1991. The following excerpts capture the essence of the message conveyed at that time:

> "RSA understands that the BLNS countries .... are .... striving .... to establish a financial situation for themselves which does not leave them in a worse position than under independent circumstances outside the Customs Union. It is also clear that .... [RSA's CU partners] .... regard their industrial development situation within the Customs Union as unsatisfactory and therefore wish to obtain increased protection against South African industrial development."
>
> "On the other hand, South Africa has come to the conclusion that:
>
> (a) the Customs Union, even in its present form, is becoming financially unaffordable: and,
>
> (b) that it .... [must] .... aspire to greater freedom in respect of industrial development."

3.48 Other points contained in the statement can be summarized as follows:

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[11] Recent research has indicated that the cost/benefit ratio of SACUA for Botswana (and, by extension, for Lesotho, Namibia and Swaziland) is much less favorable than previously assumed, largely because of the *price raising effect*. See J. Clark Leith, *The Static Welfare Economics of a Small Country's Membership in a Customs Union: Botswana in the Southern Africa Customs Union*, *World Development*, Vol. 20, No. 7 (July 1992). There are differences of opinion about the implications of the results of this econometric analysis for Botswana's strategic options and negotiating strategies.

(a) RSA has concluded that accommodation of the differing trade and industrial objectives of the SACU members is impossible within the existing Customs Union Agreement.

(b) Serious attention must be given to the creation of a "looser type of economic cooperation with broader regional participation".

(c) RSA has formed a multidisciplinary task force to study options, and its findings will be used as the basis for submitting proposals to the BLNS countries for their consideration "in the near future".

3.49 Over a year has passed since RSA made this commitment to provide the BLNS countries with the results of their task force deliberations. During this period there have been momentous political developments in RSA as well as elsewhere in the Southern African region, including growing insistence on the part of the ANC that major economic policy decisions should be deferred until such time as all interested parties in RSA can play a proper role in the decision-making processes. In short, there is currently little prospect that any significant changes in SACUA, and related domestic RSA trade and industrial development policies, will be proposed by the present Government. Such proposals are likely to be postponed until a transitional Government is in place -- or until a new, post-apartheid Government is installed, and has had time to formulate its own economic policy agenda.

3.50 The ANC has, however, recently indicated that it favors a Southern African Development Community based on "balance, equity and mutual benefit", and is opposed to a role for South Africa as a "power point for growth".[12] The PAC, for its part, favors "redress to deal in a corrective manner, with initial resource, trade, development level imbalances, maldistributional effects of economic co-operation and integration, etc.."[13]

3.51 In the meantime the existing SACUA arrangements are continuing to function as they have since the 1969 re-negotiation and the subsequent amendments in the 1970s -- and present indications are that they will continue to do so for some time. The disadvantages incurred by the BLNS countries remain and Botswana is in a difficult position. The revenue generated from the CU is about one quarter of Government's revenues and would be difficult to replace quickly. Yet the uncertainty about the nature of the future regional trading relations makes it undesirable to commit to a strategy which may be unsuited for the eventual outcome. More specifically, the distributions to be received by Botswana in quarterly installments during FY 1992/93, with respect to the estimated entitlements from revenues paid into the pool during FY 1990/91 and adjusted by actual data for FY 1989/90, amount to R1,300 million -- 24 percent of total estimated revenues for FY 1992/93 -- compared to R500 million for Lesotho and R400 million for Swaziland. Botswana's revenue has been augmented by the large import requirements of the soda ash production facilities as well as the construction boom elsewhere in the public and private sectors.

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[12] Secretary-General of the ANC to the annual summit of SADCC, 17 August 1992.

[13] President's speech to SADCC summit, 17 August 1992.

F. OUTLOOK FOR BOTSWANA'S REGIONAL ECONOMIC RELATIONS

3.52 It is clear that Botswana must prepare for the adjustments which will be required in its trade, fiscal and industrial policies as a result of the impending major modification or outright replacement of the existing SACUA with some, as yet unknown, alternative regional arrangement. Present indications are, however, that there will be sufficient time for these preparations to proceed without undue haste and in an orderly manner. Thus, while there is no immediate crisis, and while Botswana is relatively well positioned to adjust to whatever changes may be in prospect for the regional economic environment there are difficult problems to be resolved in attempting to devise an appropriate strategy and to analyze the related policy alternatives. This uncertainty, in turn, impinges on future industrialization possibilities.

3.53 Not only is there uncertainty about the likely course of RSA initiatives on SACU, but it also remains to be seen what effect the on-going structural adjustment of the Zimbabwean economy will have on Botswana/Zimbabwe trade. RSA, probably in conjunction with major changes in SACUA, may also liberalize its trade. If so, this would imply that Botswana should base its strategic planning on the assumption that, before long, competition from Zimbabwe and RSA will be closer to world market prices than at present. While this will be of considerable benefit to Botswana's consumers, it is likely to place competitive pressures on producers selling in domestic and regional markets.

3.54 The degree of uncertainty about the future course of events in these areas is well illustrated by the recent proliferation of "post-apartheid Southern Africa" studies and symposia. While numerous individuals and institutions are actively engaged in this sub-field of "futurist" speculation, and the vested interests of international institutions, national governments and spokesmen for various ideologies are well represented, a consensus of sorts is emerging regarding the range of plausible outcomes. Without pretending to capture the details of either the processes that would be involved, or the results that would be achieved, the main competing "scenarios" for future economic cooperation in Southern Africa can be differentiated as follows:[14]

(a) regional fragmentation, in which each country would adopt a "go it alone strategy" seeking to establish bilateral economic linkages both within and outside the region;

(b) the persistence of two sub-groupings roughly comprising the existing regional division on which SADCC and SACU are based, but with some overlapping (as already exists) and perhaps some marginal shifting of membership;

(c) gradual movement toward full regional economic integration based on internationally-determined market forces guiding trade and investment flows, organized within either a region-wide customs union, free-trade area or common market framework;

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[14] Adapted from C. Stoneman and C. Thompson, *Southern Africa after Apartheid; Economic Repercussions of a Free South Africa, Africa Recovery Briefing Paper*, No. 4, December, 1991, published by the UN.

(d) an amalgamation of SADCC (after RSA affiliation) and SACU, with coordination of regional development along SADCC lines and compensation along SACU or similar lines (perhaps with some linkage to the PTA).

Another possibility, of course, is that the present unsettled political conditions in RSA will continue or perhaps worsen, preventing initiation of movement along any of the lines indicated above, for an indefinitely long period.

3.55 Although Botswana may not be in a position to exercise a major influence on the ultimate choice among these or other alternatives, efforts must be made to determine Botswana's national interest and to proceed to seek ways to further that interest. An appropriately structured regional trading arrangement could also be in the national interest of all countries of the region.

3.56 There are, of course, numerous sub-sets of scenarios that can be postulated regarding the course of events that might lead from the existing SACUA and SADCC arrangements. For example, it is conceivable that RSA will strive to keep the BLNS countries within the SACUA net while seeking to expand that net to encompass other countries in the region. Under this scenario, SACUA membership might be offered to Zimbabwe and other SADCC countries sequentially, in combination with gradual reductions of the common external tariffs and compensation levels, and in association with special arrangements for protecting key industries and making allowances for group decision-making. It is envisaged that this would bring about a gradual evolution of SACU into an expanding Southern African economic community at a pace keyed to RSA's capacity to adjust to its own internal structural adjustment requirements. While this is only one of many possible scenarios -- and not necessarily the most likely one -- it serves to illustrate the relevance of political economy hypotheses and of time-phasing considerations.

3.57 In any case, it is clear that there is need for additional work on the evaluation of Botswana's options, based on sound theoretical principles and systematic policy analysis which take both economic and political factors into account. Such work should be oriented primarily toward formulation of a strategy for pursuing national interests including, where relevant, industrial development objectives, within alternative institutional frameworks.

G. IMPLICATIONS FOR BOTSWANA'S INDUSTRIAL DEVELOPMENT STRATEGY

3.58 The principal implication to be drawn from the present status of economic research and political discussion is that Botswana should premise its industrial development strategy, for the foreseeable future, on the assumption that, whatever potential opportunities may be identified for consideration, they will need to be capable of passing, at the very least, the test of regional competitiveness and, ideally, the more strenuous test of international competitiveness. For the immediate future, sights will have to be set higher for those activities which must sell in international markets (minerals) than for those activities which sell in regional markets (consumer goods). However, as noted, the prospect that regional producers will liberalize their trade regimes suggests that ultimately all producers will have to pass the international test. This implies, in turn, that comparative advantage should be the cornerstone of trade and industrialization policy.

3.59 This does not, however, mean that there is no room for Government-supported industrial promotion policies. Quite the contrary -- there is an important role for policy. The appropriate role for Government should be primarily that of providing the "enabling environment" necessary to encourage the requisite entrepreneurship and profit-oriented decision-making within the private sector -- by both domestic and foreign investors. Whatever the role Government undertakes to play, the guiding principle should be that Botswana's industrial development is premised on productive efficiency rather than on protected or otherwise subsidized inefficiency, and that it must be firmly rooted in the nation's true comparative advantage.

3.60 It should also be recognized that there exists an inherent link between the industrialization strategy appropriate for Botswana and the institutional framework for international trading relations within which Botswana's industries will be required to compete. In other words, the country's international trading policies and domestic industrialization policies are integrally linked. Both the institutional arrangements underlying trade policy and the comparative advantage underlying industrial policy must serve the country's long term national interests. Botswana therefore should develop a pro-active strategy for advocating the new arrangements it would prefer within those fora and councils which will be most influential in determining the outcome of the on-going deliberations.

H. CONCLUSIONS

3.61 Botswana should seek to clarify its industrial development opportunities by taking action along three separate but interrelated lines. First, a concerted effort should be made during the period immediately ahead to exercise an effective voice in the formulation of the new rules for regional economic competition. Second, more attention should be paid to understanding the industrial development problems and policies of other countries in the region, and to anticipating opportunities for more productive and mutually rewarding economic interactions. Last, the preparations necessary to compete more effectively should be commenced without delay -- based on a proper regime for "getting into condition" for vigorous pursuit of the country's industrial development objectives within the prospective new regional competition.

3.62 It is the basic recommendation of this chapter, therefore, that the policy agenda should be oriented towards the establishment of greater clarity regarding where Botswana's national interest lies with respect to:

(a) future institutional arrangements governing international trade and foreign investment;

(b) the economic relationships to be developed with the other countries comprising the Southern African region; and,

(c) the domestic economic policy framework required to guide progress towards the country's industrial development objectives.

CHAPTER 4

INDUSTRIAL DEVELOPMENT IN BOTSWANA: ADVANTAGES AND CONSTRAINTS

4.1 Botswana has certain natural advantages and disadvantages with respect to the promotion of industrial development. These define the basic setting within which industrial development must take place. Industrial strategy and policies should take full advantage of natural endowments, while ensuring that natural handicaps are not magnified. Such strategies, and the policies for their implementation, may also establish opportunities for development that would not otherwise exist, or impede development by creating unnecessary obstacles to progress. While a knowledge of natural advantages and constraints is essential to the identification of industrial development opportunities, there is little that an industrial strategy can do to change them. This chapter therefore focuses on those advantages and constraints that an improved industrial strategy can enhance in the former case and diminish in the latter.

A. ADVANTAGES

4.2 ***Democracy, Stability and Security.*** Botswana has a long democratic tradition which confers certain advantages. Issues are widely discussed and openly debated at both local and national levels before policy decisions are taken. This approach enhances the implementation of policies because they have widespread support before their adoption. The firm adherence to democratic principles has resulted in a politically stable nation since Independence in 1966. While the Botswana Democratic Party has controlled the central Government and Parliament since Independence, many of the local authorities have, at one time or another, been governed by members of the opposition.

4.3 Respect for the law ensures that legislation in Botswana is fairly and strictly enforced. The police force, supplemented by private security agencies, provides reasonable protection for people and property. The Botswana Defence Force has developed into a significant instrument for national defence, and can assist police in emergencies. The security situation in Botswana is further enhanced by the fact that peaceful and democratic solutions are emerging in response to difficult situations in neighboring countries in Southern Africa.

4.4 ***Access to Markets.*** Being landlocked, the cost of accessing distant markets may be more expensive than in countries which have direct access to the sea. On the other hand, however, Botswana has direct land access to a larger number of countries in Southern Africa than most of its neighbors. This represents an opportunity whose full potential has yet to be realized. Moreover, as peace, stability and democracy return to the region, the growth of demand in these regional markets should resume, and Botswana should ready itself to supply a share of this enlarged market.

4.5 In addition, as indicated in chapter 3, Botswana benefits from favorable access to the European Economic Community market through the Lomé Convention -- and to other developed country markets through the Generalized System of Preferences.

4.6 ***Responsible Fiscal Policy.*** It has been a long standing objective of Government to reserve its mineral revenues for investment in viable development projects. While the division between development and recurrent expenditure in the budget does not correspond precisely to

investment and consumption spending, the distinction does provide a rough indication of the success Government has had in achieving this objective.

4.7 Table 4.1 shows that in 9 of the past 11 years, Government's non-mineral revenue (which is not independent of mineral revenues), has exceeded its recurrent expenditure and provided a recurrent surplus to help finance development expenditure. That surplus, together with Government's mineral revenue and foreign grants, has exceeded Government's development expenditure in 10 of the 11 years. Indeed, the overall surpluses achieved have enabled Government to accumulate substantial cash balances over the decade.

Table 4.1: Consolidated Cash Flow Budget of the Central Government (pula million)

	1983/84	1984/85	1985/86	1986/87	1987/88	1988/89	1989/90	1990/91	1991/92 Rev.	1992/93 Est.
Revenue and Grants	563	803	1,133	1,548	1,825	2,556	2,751	3,741	3,804	4,161
Grants	48	39	41	68	106	110	40	118	70	46
Domestic Revenue	515	764	1,092	1,480	1,719	2,446	2,711	3,623	3,734	4,115
Mineral Revenue	194	376	581	845	1,034	1,508	1,596	2,005	1,773	1,859
Non-Mineral Revenue (NMR)	321	388	511	635	685	938	1,115	1,618	1,961	2,256
Recurrent Exp. (RE)	273	345	432	581	696	907	1,155	1,439	1,793	2,110
Recurrent Surplus (NMR - RE)	48	43	79	54	-11	31	-40	179	168	146
Mineral Revenue	194	376	581	845	1,034	1,508	1,596	2,005	1,773	1,859
Grants	48	39	41	68	106	110	40	118	70	46
Development Revenue	290	458	701	967	1,129	1,649	1,596	2,302	2,011	2,051
Development Exp. + Capital Transac.	187	270	287	427	616	881	1,060	1,504	1,837	1,941
Overall Surplus/Deficit	103	188	414	540	513	768	536	798	174	110

Source: 1982/83 - 1989/90: Statistical Bulletin (June 1991), pp. 22-3; Later years: Financial Statements, Tables and Estimates of Consolidated and Development Fund Revenues 1992/93, page 7.

4.8 These positive cash balances and the related accumulation of foreign exchange reserves are less an explicit intent of Government than a reflection of the inability to identify domestic investment opportunities in both the public and private sectors that promise rates of return equal to or greater than those obtained from investing abroad. However, the expectation is that cash balances and foreign exchange reserves will be drawn down as viable investment opportunities are identified in Botswana that can be implemented effectively and will contribute to sustainable development.

4.9 As indicated in table 4.1, the recurrent surplus has declined over the last two years. Projections in NDP 7 show that an increasing share of recurrent expenditure will need

to be financed by drawing on mineral revenue. According to those projections, by 1996/97, over 80 percent of mineral revenue will be required to finance 48 percent of recurrent expenditure. NDP 7 is essentially a transition period from rapid growth of mineral revenue to a period of more modest growth. Toward the end of this plan period, development spending will be declining, but recurrent expenditure will continue to rise -- reflecting the large development expenditures incurred during the last half of NDP 6 and the first half of NDP 7. It is expected that NDP 8 will see a resumption of growth of development expenditure as the growth of recurrent expenditure subsides.

4.10 *Effective Monetary Policy.* Responsible fiscal and economic policies have contributed to the nation's healthy foreign exchange position. Foreign exchange reserves were P7,707 million at the end of 1991 -- equal to about 18 months of imports of goods and services. The effective management of these reserves, the exchange rate and interest rates, by the central bank -- the Bank of Botswana -- has also strengthened the foreign exchange position.

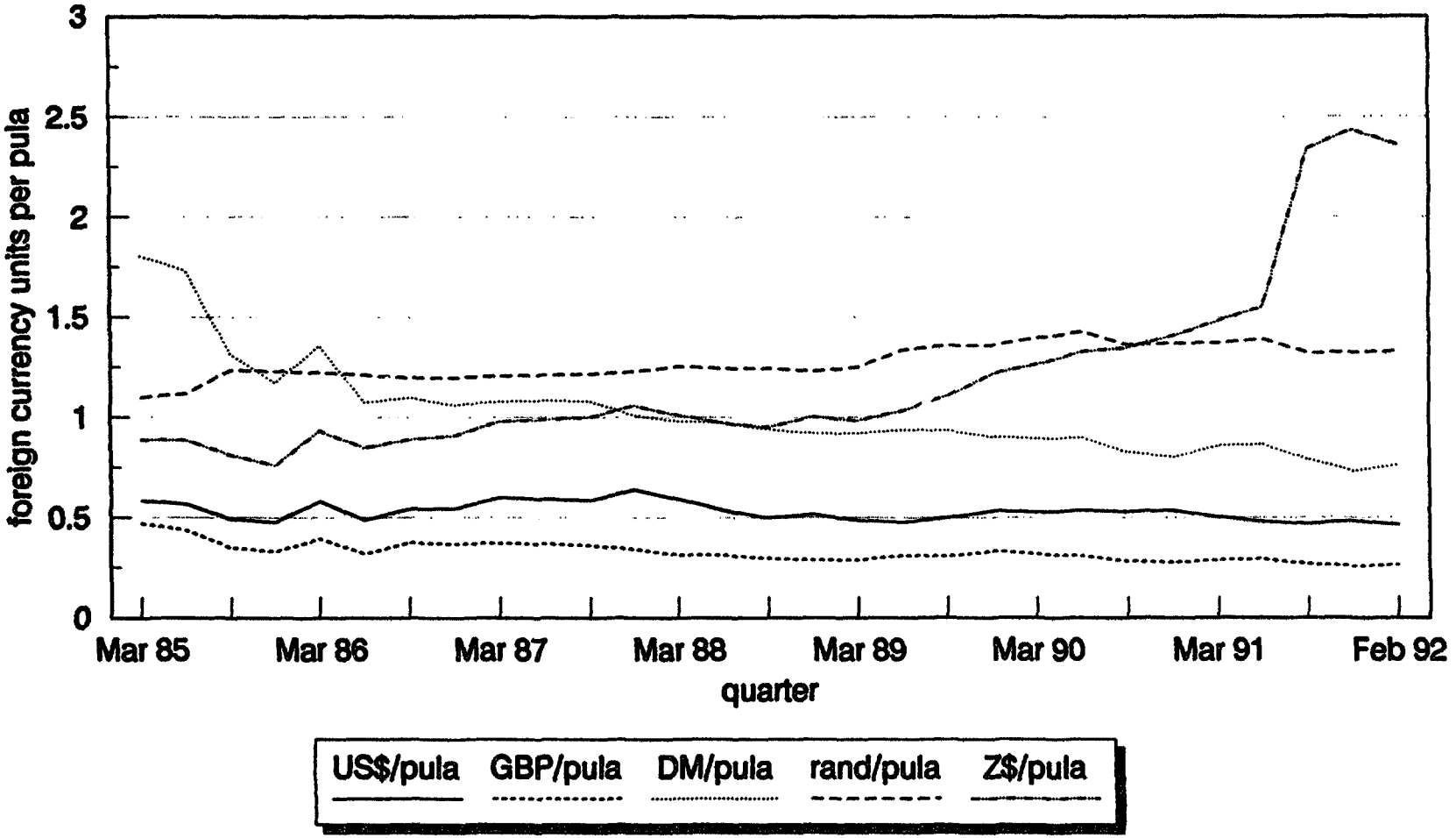
4.11 Exchange rate management has focused on maintaining relative stability of the pula with respect to the rand and other major currencies. Occasional adjustments in the exchange rate have been made to reduce the impact of inflation in South Africa on inflation in Botswana, but over the last two years this policy has been modified to encourage non-traditional exports. Hence, the burden for controlling inflation has fallen more heavily on the management of interest rates and the containment of domestic resource costs through fiscal policy, wages policy, and improved productivity. Nevertheless, it is expected that domestic inflation will more closely reflect the inflation rate in South Africa than it has in the past. Chart 4.1 depicts quarterly movements in key exchange rates over the last 7 years. The two 5 percent devaluations that took place in August 1990 and September 1991 are easily identifiable. The sharp rise in the exchange rate between the Zimbabwe dollar and the pula reflects the structural adjustment program being undertaken in that country.

4.12 Controls over foreign exchange transactions are minimal, and are used more to gather information than to limit movement of currencies. Exchange is made through authorized dealers. Both permanent and temporary residents may transfer their assets upon emigration, but transfers in excess of P150,000 may be phased over three years. Permanent residents are not allowed to use foreign exchange facilities for investment abroad, and resident travellers abroad are limited to P500 in local currency and the equivalent of P1,000 in foreign currencies. Export proceeds must be remitted through an authorized dealer within 6 months of the date of export. Insurance cover cannot be taken with non-resident companies. Local borrowing by a non-resident company is limited to P300,000 plus 4 times the level of its equity -- but for manufacturing concerns the Bank of Botswana may allow up to 8 times equity. Foreign borrowing by residents requires the approval of the central bank. In all, the foreign exchange regime in Botswana is the most liberal in Southern Africa, and offers investors an opportunity, unique in the region, to move their capital about with relative freedom. Consideration is currently being given to further liberalization.

Chart 4.1

Pula Exchange Rates (quarterly)

(1985 - 1992)



4.13 Policy with respect to interest rates has not been as effective as it could have been in terms of promoting domestic saving and the efficient allocation of loanable funds. Table 4.2 shows nominal and real interest rates over an 11 year period in terms of the prime lending rate and the 88 day deposit rate. Chart 4.2 graphs the real deposit and real prime lending rate. As indicated by the chart, both of these rates have been negative for a number of years, in real terms. Given that positive real rates of interest have prevailed in South Africa and the OECD countries over this period, there is an incentive to move funds out of Botswana for investment elsewhere.

Table 4.2: Nominal and Real Interest Rates

	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Prime Rate	11.0	14.5	13.0	11.5	11.5	10.0	10.0	7.5	8.0	9.0	12.5
88 days deposit	9.0	12.5	11.0	9.0	9.0	7.8	7.8	5.5	5.5	7.8	10.9
Inflation Rate	14.6	12.7	8.3	6.5	10.4	10.8	8.1	10.4	11.3	12.0	12.6
Real Prime Rate	-3.6	1.8	4.7	5.0	1.1	-0.8	1.9	-2.9	-3.3	-3.0	-0.1
Real Deposit Rate	-5.6	-0.2	2.7	2.5	-1.4	-3.1	-0.3	-4.9	-5.8	-4.3	-1.7

Source: Bank of Botswana, Annual Reports and unpublished data.

4.14 Negative real interest rates were undoubtedly a factor in the rapid rise in the share of commercial bank lending going to households, primarily for consumption purposes. Between end 1986 and end 1991, outstanding credit to households increased from 18 percent to 32 percent of total commercial bank credit.

4.15 Over the last two years, real interest rates have become less negative. By March 1992, the nominal prime rate had risen to 13.5 percent and the 88 day deposit rate to 11.9 percent. However, more recently, the inflation rate has risen to 14.6 percent, thereby making these higher nominal rates more negative in real terms. Since May 1991, the mechanism for effecting changes in interest rates has involved the issue of Bank of Botswana certificates, which have virtually replaced a central bank call facility previously offered to certain large depositors. Seven auctions were held in 1991, and the amount outstanding at the end of the year was P771.8 million -- with commercial banks holding 44 percent.

4.16 ***Rapid Development of Human Resources.*** Education and training are central to the Government's development strategy. This is reflected in the fact that education accounts for 20 percent of the Government's recurrent expenditure -- a larger share than any other activity. A set of policy prescriptions for education were prepared by the National Commission on Education appointed in 1975. These formed the basis for the National Policy on Education adopted in 1977. The wide range of educational programs and activities relating to primary, secondary, vocational and technical education, teacher training, non-formal education, curriculum

development and evaluation and higher education undertaken by the Ministry of Education since then were based on this Policy. By 1991, about 90 percent of all primary school age children attended school (more precise data will emerge from the 1991 Census and the 1992 Literacy Survey). Access at junior secondary school level had reached 85 percent of young people in the catchment age group.

4.17 A second National Commission on Education was appointed in 1992 to review the present system with particular reference to secondary education in the light of the country's present and future economic and social changes. The 1992 Commission will be particularly concerned with the structure of secondary education in terms of length and content and its relevance to higher education during the next 15 to 25 years.

4.18 The goal of the Government's education policy is to provide nine years' basic education to all Batswana. Since 1988, the curriculum is divided into a basic 7 years primary and 2 years junior secondary, followed by 3 years secondary schooling for qualifying pupils. The Primary School Leaving Examination (PSLE) is taken at the end of the primary level; Junior Certificate Examination (JCE) at the end of junior secondary; and Cambridge Overseas School Certificate (COSC) at the end of senior secondary. The first two examinations are local, while the COSC is a UK examination.

4.19 Primary school leavers who are not admitted to junior secondary schools may apply to the Brigades for vocational training or to a Primary Teacher Training College after at least two years working as an unqualified teacher. Options for junior secondary school leavers include vocational and teacher training, secretarial or commercial training. Senior secondary school leavers may go on to technical courses at the Polytechnic, degree courses at the University of Botswana or a variety of specialized training schools (agriculture, secondary school teaching, nursing, administration and commerce).

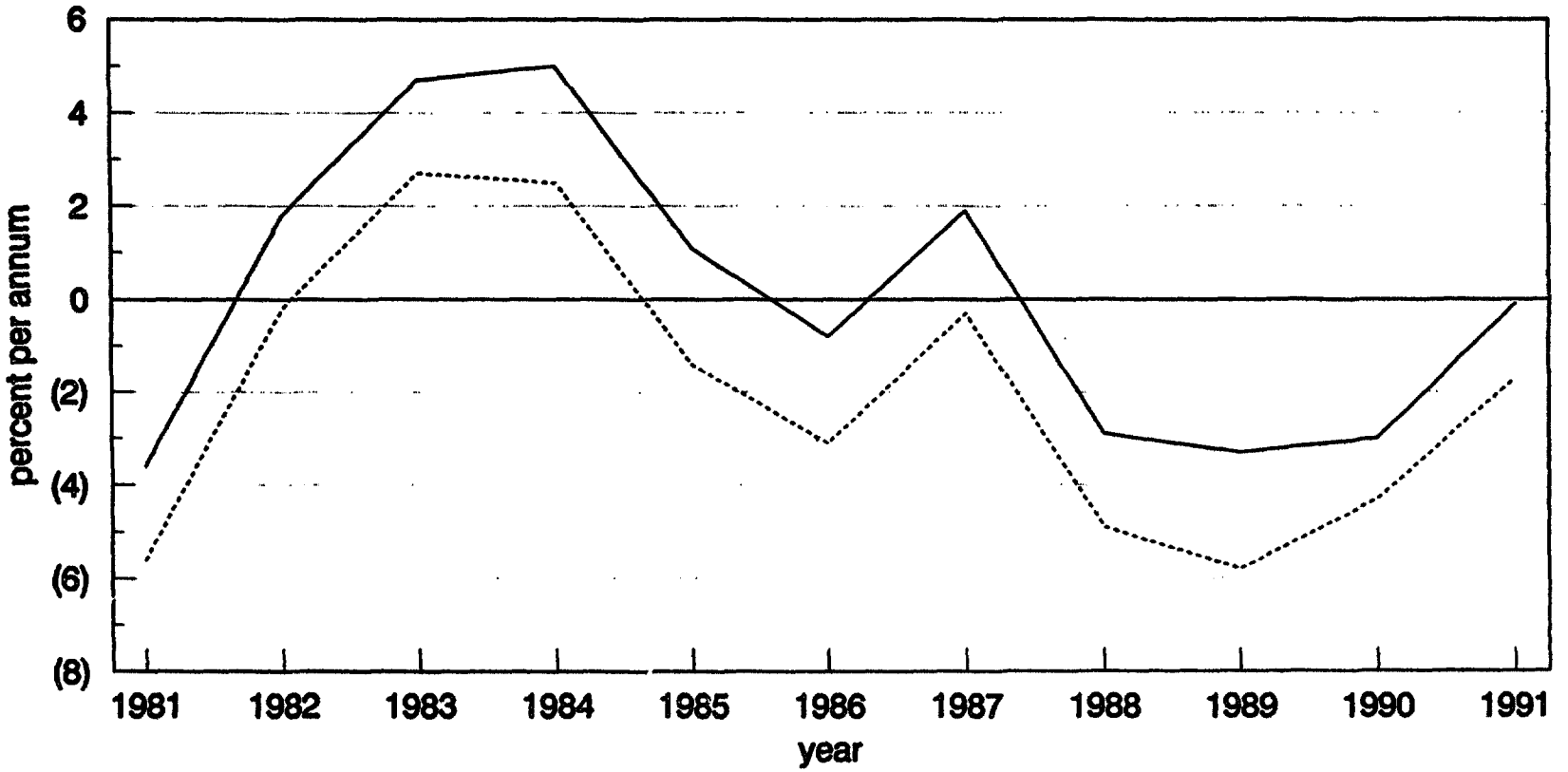
4.20 Apprenticeships and industrial training courses are available for a range of designated trades. The list is shorter for apprenticeships than it is for industrial training; the former includes among others, auto-mechanics, carpenters/joiners, plumbers and pipefitters, refrigeration, air conditioning and borehole mechanics. Applicants must be at least 15 years old. Employers who participate in the apprenticeship scheme give up to 4 years training at the completion of which the apprentice must pass a test to obtain the relevant National Craft Certificate. Having qualified, the former apprentice may be bonded for up to 4 years to the enterprise where the apprenticeship was served, or be free to seek employment elsewhere. Industrial Training schemes give part-time training only; participants may choose to take the National Craft Certificate test at the end of a course. There is a wide choice of skills.

4.21 Hence, although education and skill levels may be at a lower level than many of the other countries in the region, there has been a substantial effort to redress this issue. Indeed, whereas resources for education and training are being curtailed in many of the neighboring countries, as they come to grips with fiscal imbalances, Botswana has, by contrast, increasingly been able to fund the education and training requirements of its population.

Chart 4.2

Real Interest Rates

(percent per annum, 1981 - 1991)



real prime rate ——— real deposit rate ·····

4.22 ***Freedoms to Produce, Market and Finance.*** As described, Government has recently taken a number of steps to reduce burdensome regulations and restrictions on entry imposed through licensing. The intent is to promote competition and consumer awareness as the primary means of ensuring fair trade, reasonable prices and quality goods and services. For most producers serving the domestic market, import parity prices provide effective competition. For those competing in foreign markets for sales, competition, wages policy and increases in productivity should contain factor prices and the prices of intermediate inputs at reasonable levels.

4.23 A new financial sector development strategy has recently been initiated by Government in recognition of the expanding capacity of the private sector to satisfy a growing proportion of the demand for long and short term capital. This strategy entails: (1) progressively reducing the Government provision of parastatal finance, (2) narrowing the gap between Government and private sector lending rates,[1] (3) promoting competition among commercial banks by encouraging new entrants, (4) reviewing the mandates and performance of development finance institutions, (5) promoting efficient money and capital markets through a realistic interest rate structure, progressive privatization and the extension of financing opportunities open to the private sector, (6) adhering to opportunity cost criteria in the investment of Government funds, (7) improving the management of external assets and liabilities, and (8) fostering the development of the stock market.

4.24 ***Infrastructure and Utility Services.*** As indicated in Chapter 1, the social and physical infrastructure in Botswana has expanded rapidly since Independence. Road, rail and air facilities serve much of the country and are modern and well maintained in the more densely settled areas. Primary health care and basic education have been extended throughout the country and most major centers have more advanced facilities. The nation is served by a university that is rapidly expanding in enrollments and quality. Major utility services, such as power, water and telecommunications are now widely available, and the services are reliable, accessible and well maintained, with service records that are the envy of many nations in Africa.

4.25 The above advantages have created an enabling environment that is superior to most in the Southern Africa region. This environment does not seek to artificially equalize costs with those in competing nations, but rather provide a favorable atmosphere in which foreign and domestic entrepreneurs can profitably invest in those activities in which Botswana has a genuine comparative advantage.

B. CONSTRAINTS

4.26 The basis for improving industrial development policy must lie in strengthening Botswana's advantages while easing the constraints that inhibit more rapid industrial development. The discussion of constraints in this section attempts to identify the scope that realistically exists for relaxing apparent constraints. It should be noted, however, that Government has already taken some measures to address these constraints to development following the recommendations of the Revised Incomes Policy of 1990.

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[1] The Government lends funds to certain parastatals through two special funds - the Public Debt Service Fund (PDSF) and the Revenue Stabilization Fund (RSF) - at rates of interest which have traditionally been several points below other domestic market rates.

4.27 *Utility Costs*. Many existing and prospective enterprises in Botswana complain about the high cost of utility services. Given the distances over which such services must be delivered and the cost of distribution networks that must serve sparsely settled rural areas -- and the consequent limited economies of scale that can be achieved -- it is understandable that utility costs in Botswana exceed the costs prevailing in more densely settled neighboring countries with less costly access to sources of supply.

4.28 Comparisons with costs in neighboring countries are difficult to make for a variety of reasons. It is Government policy in Botswana that prices for services in excess of basic needs should be based upon full cost recovery. If prices are subsidized elsewhere, comparisons will reflect the relative costs to customers, but not the relative costs of production. Moreover, rate schedules for power, water and telecommunications may differ among countries, and the quality and reliability of service may also vary. Finally, restating charges in a common currency using official exchange rates may not yield realistic comparisons. In these circumstances, the best that can be done is to compare costs to typical consumers of utility services.

4.29 *Power*. A small business consumer of electricity in Botswana, charged on the "Business I Tariff", might consume 1,700 kilowatt hours per month at a total cost (April 1992) of about P450. A similar consumer in Zimbabwe would pay the equivalent of about P100 and in South Africa about P230. A medium to large business consumer of electricity in Botswana, charged on the "Business II Tariff", might consume about 17,000 kilowatt hours per month at a total cost of P4,040, with some variation depending on load factors. Similar consumers in Zimbabwe and South Africa would pay the equivalent of P900 and P1,850, respectively. Hence, variations in cost among these countries do not differ substantially by market size. The cost of power in Botswana is about 4½ times the cost in Zimbabwe and about 2 times the cost in South Africa. There is some evidence that, recently, costs in South Africa have been rising more rapidly than costs in Botswana.

4.30 Surveys in selected industrialized countries reveal several cases where unit electricity costs to industrial and commercial users are about half comparable costs in Botswana (US, UK, France, Holland, and Sweden); some where costs are even lower (Canada and Australia); and some where costs are 70 to 80 percent of costs in Botswana (Germany, Italy, Belgium, and Ireland). Clearly, firms that rely heavily on power as an input are at a serious disadvantage if they choose to locate in Botswana.

4.31 *Water*. Current figures show that the cost of water for industrial users in Botswana is substantially higher than in neighboring countries, with the differentials being greater at higher average levels of consumption. Large users in Botswana pay about 10 times the cost in Zimbabwe, about 5 times the cost in Bophuthatswana, and about 2½ times the cost in South Africa. Moreover, when costs rise in Botswana by about 70 percent (in real terms) to cover the cost of new supplies via the north-south carrier, these differentials will increase further.

4.32 *Telecommunications*. Telephone calls exhibit similar differentials. While it costs P15.60 to make a 10 minute, subscriber-dialled, full rate phone call from Gaborone to Johannesburg, the equivalent cost to place the same call in the opposite direction is about P5.50. The same call to Nairobi costs P54.50 from Gaborone and P40.60 from Johannesburg. Placing a similar call to London costs P70.60 from Gaborone and P40.60 from Johannesburg. The cost

for a 10 minute call to New York City from Gaborone is P85.70, while from Johannesburg the cost is P40.60.

4.33 The effect of these differentials in utility costs on the total operating costs of businesses located in Botswana depends on how large a proportion of total costs can be attributed to utilities. Evidence from Selebi-Phikwe suggests that power represents no more than 1 to 2 percent of total costs for the manufacturing firms currently operating there. A recent study on "Water Use and Affordability" found that, for major consumers, water costs were less than 1 percent of total costs. Even with these low levels of usage, differentials in utility costs might raise total operating costs in Botswana by 2 percent, which is not negligible for profit-seeking business firms.

4.34 Utility costs are clearly higher in Botswana than in neighboring countries. While some reductions in the apparent differentials may be possible through closer surveillance of efficiency and cost-cutting measures by parastatal boards, and possibly by applying more realistic methods of accounting for capital costs, very little can be done to reduce the real costs of producing utility services in Botswana, and these are clearly higher than in either Zimbabwe or South Africa.

4.35 The inevitable conclusion is that businesses requiring large inputs of utility services to conduct their operations may not choose to locate in Botswana. The high cost of utility services should guide new and expanding businesses in the direction of activities, such as financial, business and tourism services, in which utility costs are a negligible part of the total costs of operation.

4.36 *Long Term Finance.* There have been many allegations of a shortage of long term finance. The Bank of Botswana, in a study conducted in 1988, estimated that 15 percent of the total demand for long term (in excess of one year) finance over the following four years would not be satisfied. Estimates of the demand for mortgage finance that will arise following the implementation of the Government's Accelerated Land Servicing Program have also suggested that established sources of long term finance will fall short of needs.

4.37 These estimates of a serious shortfall in long term finance were made at a time when real deposit and lending rates were negative. Another survey conducted by the Bank of Botswana in 1987, for example, which elicited responses from only 66 of the 200 businesses contacted, did not ask respondents what interest rate they had in mind when estimating their need for long term finance. At rates higher than those prevailing at the time of the survey, many respondents would undoubtedly have reduced their estimated demand for long term funds. The provision of commercial, industrial and housing sites alone will not lead to industrial and residential development -- as this is also dependent on the interest rates charged on longer term, and mortgage, finance.

4.38 Nevertheless, concerns expressed about the reluctance of commercial banks to lend long term may be soundly based when the maturity structure of commercial bank lending in Botswana is compared with maturity structures in other more developed countries. It should be noted, however, that lending by regional commercial banks tends to be very short term. Many countries in the region are undergoing structural reform programs, which do not lend themselves to the growth of longer term markets in financial instruments. Table 4.3 shows the maturity

distribution of commercial bank lending in Botswana over the last six years by both number and value of loans.

Table 4.3: Maturity Distribution of Commercial Bank Loans by Number and Value

	1986	1987	1988	1989	1990	1991
Number of Loans (%)						
Under 12 months	51.1	58.3	55.9	55.9	53.1	49.6
1 to 5 years	47.4	39.8	42.5	42.5	43.8	44.4
Over 5 years	1.4	1.9	1.6	1.6	3.2	6.0
Value of Loans (%)						
Under 12 months	54.1	53.5	53.1	55.3	60.2	56.1
1 to 5 years	39.6	39.5	39.7	35.9	32.3	34.2
Over 5 years	6.3	7.0	7.3	8.8	7.6	9.6

Note: Column totals may not add to 100 percent due to rounding.
Source: Bank of Botswana, Annual Reports and unpublished data.

4.39 There is evidence that the maturity distribution has been lengthening, but the increase in long term loans has come about mainly at the expense of medium term loans. Moreover, a Housing Finance Survey conducted by the Bank of Botswana, at the end of 1988, indicated that 33 percent of medium and long term loans were housing loans, and half of these were to finance staff housing.

4.40 Domestic saving has largely been Government saving. Until other forms of domestic saving and more efficient capital markets are developed, the principal source of long term finance will be Government savings channelled through parastatals. Table 4.4 shows the principal institutions engaged in lending in Botswana.

4.41 Lending by institutions other than commercial banks has grown more rapidly than lending by commercial banks, albeit from a much smaller initial base. Whereas loans by these institutions accounted for only 25.4 percent of total domestic loans in 1984, they represented 40.1 percent in 1991. As much of this lending is long term, it is reasonable to conclude that the maturity distribution of domestic credit in Botswana, as a whole, has been increasing. If equity provided by the Botswana Development Corporation is included as long term financing, the percentages are 28.4 and 42.7, respectively.

4.42 Most of these lending institutions, other than the commercial banks, have received financing from Government -- primarily through the Public Debt Service Fund (PDSF). Loans from this fund and the Revenue Stabilization Fund (RSF) are also available to other parastatals, and the city and town councils. Total PDSF/RSF loans outstanding amounted to P217.8 million in 1984 and P702.4 million in 1990.

Table 4.4: Commercial Bank and Non-Bank Credit (pula million)

	1984	1985	1986	1987	1988	1989	1990	1991
COMMERCIAL BANKS	238.6	257.0	273.4	285.2	368.9	529.7	757.5	1,041.0
NON-BANK LENDING								
Leasing Companies								
Contracts Receivable	7.9	9.3	12.1	18.7	26.2	40.6	125.3	207.9
Property Loans	0.0	0.0	0.0	0.0	6.9	10.8	n.a.	n.a.
National Development Bank								
Loans and Investment	39.9	46.6	41.6	45.4	33.7	62.5	71.1	88.8
Botswana Building Society								
Short Term Loans	1.4	1.9	2.6	2.8	3.7	3.9	4.8	6.4
Mortgage Loans	17.0	19.7	23.5	33.1	49.0	69.8	103.9	184.6
Botswana Housing Corporation								
Mortgage Loans	0.2	0.2	0.1	1.1	4.0	9.3	9.1	11.6
Botswana Savings Bank								
Loans and Advances	0.0	0.0	6.5	7.1	11.6	16.6	22.0	25.4
Botswana Cooperative Bank								
Advances	4.4	5.3	5.9	5.9	4.8	8.3	16.5	46.6
Tswelelo (Pty) Ltd.								
Loans, Advances & Leases	0.0	0.3	1.3	3.3	5.0	7.3	8.3	10.3
Botswana Devt. Corporation								
Loans	10.6	14.1	19.4	23.5	26.7	49.2	81.2	115.2
Total Non-Bank Loans	81.40	97.40	113.00	140.90	171.60	278.30	442.20	696.80
TOTAL LOANS	320.00	354.40	386.40	426.10	540.50	808.00	1,199.70	1,737.80
Botswana Devt. Corporation								
Equity	13.1	25.2	29.6	37.4	46.0	46.9	64.6	78.4

Notes: End of calendar year figures except: NDB (1984 and 1985 are March), Tswelelo (1985 and 1986 are June), and BDC (all years are June).

Source: Bank of Botswana, Annual Reports; Botswana Development Corporation, Annual Reports; Botswana Housing Corporation, Annual Reports; National Development Bank for NDB loans in 1989, 1990, and 1991.

4.43 External borrowing is also an important source of finance, particularly for non-financial parastatals. The total outstanding debt channelled to or through Government amounted to P549.2 million at the end of September, 1991. The major sectors benefitting from this foreign borrowing are energy (P103.7 million), education and training (P99.3 million), transport (P97.4 million) and water (P65.8 million).

4.44 Sources of long term finance for major projects, corporations and institutions do not appear to be an important factor inhibiting development. The availability of long term finance for small and medium scale enterprises and households may be a continuing, if diminishing, problem; but how much of the apparent excess demand is a reflection of an inappropriate structure of interest rates and how much is evidence of immature capital markets and risk averse lending agencies cannot be determined until positive real interest rates are achieved.

4.45 Nonetheless, there remains a general perception within Botswana that long term finance is an important constraint on industrial development. Unfortunately, commercial banks are unlikely to lend much beyond the terms currently available -- and, in fact, by the standards of the region, Botswana's commercial banks are relatively long term lending institutions. Should a high demand for long term financing remain, even when interest rates become positive in real terms, then the Government will need to consider alternative mechanisms for providing such financing. One concept, being considered by Government, is the establishment of a fund to channel term credit from Government to industry, and other sectors, for productive purposes. The Government of Botswana has also recently requested the World Bank to work with it to re-examine the role of the development finance institutions in Botswana and the provision of longer term finance through these institutions. This work will hopefully shed some light on how additional long term financial resources can be made available for viable enterprises, at positive real rates of interest.

4.46 ***Short term finance.*** Short term working capital, including pre- and post-shipment credit is available through the commercial banking system at market rates of interest. Although there has been some debate within Botswana concerning pre- and post-shipment credit, this debate appears to center around the cost of such finance rather than its availability. In light of the move towards positive real rates of interest within the economy generally, any move to create a subsidized window for such activities would subvert the main thrust of financial sector reform. Export credit insurance is also available through local insurance companies.

4.47 ***Wages Policy and Productivity.*** As noted in chapter 2, there is increasing concern over productivity levels in both the private and public sectors of the economy. From a policy point of view, however, productivity must be seen in relation to the cost of labor. If increases in productivity and inflation are fully reflected in higher labor costs, Botswana's international competitive position is not improved. The use of the exchange rate as a means of promoting non-traditional exports can be made virtually ineffective if wages and other domestic resource costs are adjusted to reflect the consequent increase in import prices.

4.48 Government is the largest employer in the country. Its decisions on wages and salaries, therefore, tend to set guidelines for similar decisions in the private sector. Recent data indicate that real monthly wages for citizens employed in the private and parastatal sectors increased at an average annual rate of 0.17 percent between August 1980 and March 1986, but by 2.5 percent per annum between March 1986 and March 1991. Real wages of non-citizens in

the private and parastatal sectors decreased in both periods at annual rates of 0.44 percent and 2.26 percent respectively. Real wages of Central and Local Government employees increased by about 2.6 percent in the latter period (data are not available for the earlier period).

4.49 The recent rise in real wages is in sharp contrast to crude measures of changes in productivity (see table 4.5). GDP in 1985/86 prices amounted to P15,500 per formal sector employee in 1980/81, reached P19,600 in 1985/86 and fell to P17,100 in 1990/91. Eliminating the special sectors of agriculture, mining, social services and Government, GDP per employee increased from P12,400 in 1980/81 to P13,100 in 1985/86, and then fell to P10,300 in 1990/91.

4.50 Relating changes in GDP produced outside of agriculture, mining, social services and Government to changes in employment reveals that the change in GDP per additional worker amounted to P16,300 between 1980/81 and 1985/86, but to only P8,000 between 1985/86 and 1990/91. It seems possible that recent increases in real wages have exceeded increases in productivity, and have contributed to the rising rate of domestic inflation and a weakening competitive position in international markets. However, these data should be treated with caution, as changes in these ratios may reflect other changes in the economy such as changes in the structure of production from capital to more labor intensive modes of production.

4.51 Nonetheless, the increase in Government wages and salaries that took effect on April 1, 1992 was limited to 10 percent -- about 2.5 percent below the inflation rate in 1991 -- thereby increasing Botswana's competitive position. This increase, together with normal creep, should maintain the level of real wages within Government. A continuation of this policy, if reflected in private sector wages, should bring the change in real wages for the economy as a whole, closer to the present rate of increase in productivity.

4.52 *Land and Housing Issues*. One of the biggest constraints to further industrial development in Botswana is the shortage of serviced industrial and commercial plots. Although this affects all investors in Botswana, it is thought to have a bigger impact on smaller local investors. The Ministry of Commerce and Industry, Tswelelo and some local authorities have attempted to alleviate the problem by providing factory shells for small and medium scale enterprises. The Botswana Development Corporation also provides factory shells -- although the rents are considered high, especially by small local investors. Moreover, when serviced land becomes available, it is frequently purchased and held for speculative purposes. Such speculative activity confirms the scarcity of this important resource and the economic rents which can be obtained.

4.53 In order to address the problem of serviced land for industrial, commercial and residential purposes, Government embarked on an ambitious P500 million Accelerated Land Servicing Program (ALSP) in 1987. The program is intended to eliminate the backlog in the supply of serviced urban land -- by the end of 1994. A related objective of the program is to establish the urban foundation for the growth of the manufacturing and service industries, which will provide employment opportunities for a rapidly growing population while supporting diversification of the national economy's productive base.

Table 4.5: GDP/Employment Ratios, 1980/81, 1985/86, and 1990/91
GDP (1985/86 prices)/Formal Sector Employment

Year	1980/81	1985/86	1990/91	Change 1981 - 86	Change 1986 - 91
GROSS DOMESTIC PRODUCT (mala million)					
1. Agriculture	158.3	132.4	215.5	-25.9	83.1
2. Mining	530.3	1,133.9	1,533.0	603.6	399.1
3. Manufacturing	100.6	124.2	198.7	23.6	74.5
4. Water & Electricity	28.1	57.7	91.3	29.6	33.6
5. Construction	116.4	96.0	201.9	-20.4	105.9
6. Trade, Hotels & Restaurants	265.8	319.9	539.2	54.1	219.3
7. Transport	28.3	66.5	136.2	38.2	69.7
8. Financial & Business Services	48.5	97.6	157.7	49.1	60.1
9. General Government	199.8	325.7	642.0	125.9	316.3
10. Social and Personal Services	35.0	66.7	98.1	31.7	31.4
GDP at Market Prices	1,511.1	2,420.6	3,813.6	909.5	1,393.0
GDP: Sec 3, 4, 5, 6, 7 & 8	587.7	761.9	1,325.0	174.2	563.1
FORMAL SECTOR EMPLOYMENT					
1. Agriculture	4,800	3,500	6,700	-1,300	3,200
2. Mining	7,300	7,500	7,800	200	300
3. Manufacturing	6,400	10,600	26,000	4,200	15,400
4. Water & Electricity	1,600	2,000	2,500	400	500
5. Construction	15,200	12,000	33,800	-3,200	21,800
6. Trade, Hotels & Restaurants	15,300	20,400	41,000	5,100	20,600
7. Transport	3,900	5,700	9,100	1,800	3,400
8. Financial & Business Services	4,900	7,300	16,200	2,400	8,900
9. General Government	32,600	49,000	68,500	16,400	19,500
10. Social and Personal Services	5,400	5,500	11,100	100	5,600
EMP, excl BDF	97,400	123,500	222,700	26,100	99,200
EMP: Sec 3, 4, 5, 6, 7 & 8	47,300	58,000	128,600	10,700	70,600
GDP (mala) per EMPLOYEE					
1. Agriculture	32,979	37,829	32,164	19,923	25,969
2. Mining	72,644	151,187	196,538	3,018,000	1,330,333
3. Manufacturing	15,719	11,717	7,642	5,619	4,838
4. Water & Electricity	17,563	28,850	36,520	74,000	67,200
5. Construction	7,658	8,000	5,973	6,375	4,858
6. Trade, Hotels & Restaurants	17,373	15,681	13,151	10,608	10,646
7. Transport	7,256	11,667	14,967	21,222	20,500
8. Financial & Business Services	9,898	13,370	9,735	20,458	6,753
9. General Government	6,129	6,647	9,372	7,677	16,221
10. Social and Personal Services	6,481	12,127	8,828	317,000	5,607
TOTAL ECONOMY	15,514	19,600	17,124	34,847	14,042
SECTORS: Sec 3, 4, 5, 6, 7 & 8	12,425	13,136	10,303	16,280	7,976

Source: Central Statistics Office and Ministry of Finance and Development Planning.

4.54 The program will provide serviced land in six urban areas for over 31,000 residential housing units, over 400 commercial plots, 641 industrial plots (of which 114 will be rail served), and central business district sites in three urban centers. Sites for schools, community centers, health facilities, recreational amenities, playgrounds and parks will also be

developed. The scope of the program entails provision of new primary, secondary and tertiary infrastructure including roads, drains, sewage systems, water and power reticulation as well as the upgrade of existing systems. While Government has been solely responsible for land development, the private sector is expected to be involved in servicing about 20 percent of the land under this program.

4.55 The allocation of plots on State land is the responsibility of the Department of Surveys and Lands (DSL) – tribal and freehold land is also available. Table 4.6 shows the number of plots allocated by the department from 1986 to 1991. The table reveals sharp fluctuations in the number of plots allocated. According to DSL, applications received by December 1990 under the ALSP amount to 40,000 residential, 6,000 commercial and 4,000 industrial plots. A comparison of applications with the number of plots to be provided under the ALSP reveals a continuing shortage. However, it is not known how much of this demand is real and effective.

Table 4.6: Land Allocation by the Department of Surveys and Lands 1986/87-1990/91

Land Use	1986/87	1987/88	1988/89	1989/90	1990/91	TOTAL
Residential	643	94	90	1,461	3	2,291
Commercial	150	46	4	56	5	261
Industrial	194	30	101	90	42	457
Multi-purpose	0	10	6	19	6	41
TOTAL	987	180	201	1,626	56	3,050

Source: Department of Surveys and Lands.

4.56 To help maintain up-to-date information, Government has begun computerizing all land records and land management procedures. Information on institutional and district housing is also being computerized. However, this will take time as the program is still encountering bottle necks.

4.57 The principal *suppliers of housing* are -- the Botswana Housing Corporation (BHC), the Self-Help Housing Agency (SHHA) and private individuals. Institutional and district housing are also provided by Government. Nonetheless, BHC is the dominant provider of housing in urban areas. Botswana's housing market is highly segmented and those who have access to BHC rented housing enjoy a considerable housing subsidy. On the other hand, those without such access have to seek rented housing at market prices. For higher cost housing, the free market is relatively small, and constraints on supply have tended to increase rents far beyond BHC levels and significantly above the long-run supply price of housing.

4.58 The BHC is making a contribution towards relieving the current housing shortage, through the construction of housing units and the servicing of land as Government agent for

ALSP. The Corporation is making an effort to sell a significant portion of its housing stock to citizens through two programs: the Tenant Purchase Scheme, under which buyers must continue to live in their houses; and outright sales to the public. Steps are being taken to define the future role of BHC in the housing market, and ensure that it can contribute to the development of the housing market with decreased recourse to Government assistance and without undermining private sector initiatives.

4.59 *Regulatory Framework Issues*. Regulatory constraints on industrial development have long been recognized in Botswana. Regulatory issues fall into four main areas: provisions under the Non-Citizens Act which require that foreigners hold valid work and residence permits for Botswana; licensing issues through the Licensing Boards in the Ministry of Commerce and Industry; regulations for obtaining land through the land boards; and restrictions on employment under the Employment Act. With a need for expatriate skills to service a rapidly growing economy, these regulations have an important impact on investors. The demands of strong economic growth and a limited supply of citizens with requisite skills implies that additional expatriate assistance will be necessary over the medium term.

4.60 *Work and Residence Permits*. Some streamlining procedures have been adopted with respect to work and residence permits which include: matching work permits to the period of a worker's contract; exempting expatriates in parastatals from applying for work and residence permits; increasing the maximum duration of a residence permit from three to five years; making permanent residence available to persons resident for ten or more years; providing six month waivers for expatriates so that they can commence working while waiting for a work permit; and, providing potential investors with longer term visitor permits (three months).

4.61 Major administrative changes in the processing of work and residence permits -- including computerization and staff training -- have also been initiated. To reduce the backlog in immigration and work permit allocations, Regional Immigration Selection Boards are being established in Lobatse, Gaborone, Selebi-Phikwe and Francistown.

4.62 However, there is on-going concern over the slowness of the bureaucracy surrounding the work and residence permit system for expatriates in Botswana. The regulatory environment remains highly restrictive. Hence, despite a commitment by Government to encourage investment and employment creation in the industrial sector, at the implementation stage much of this encouragement is lost in bureaucratic controls. Extensive recommendations were made in the Revised National Policy on Incomes, Employment, Prices and Profits (March 1990) to address some of these problems. The Regulations Review Committee is charged with the responsibility of monitoring the implementation of these recommendations.

4.63 One problem involves "waivers". Waivers require periodic renewal and, as a result, applicants are always uncertain whether the waivers will be renewed or permits will be eventually issued. Some improvements are being made, however. Whereas waivers were being issued for three months, they are now issued for not less than six months. It is hoped that processing of applications for work and residence permits will take the Regional Immigration Selection Boards less than six months from the date of submission. However, serious consideration is being given to the introduction of indefinite waivers. Once the Regional Immigration Selection Boards are established -- hopefully by the end of 1992 -- priority in processing of work and residence permits will be given to critical occupations. In anticipation

of these developments, and the greater decentralization of this function, the current board has adopted new measures to eradicate a backlog of about ten thousand applications.

4.64 *Industrial and Commercial Licenses.* Licenses will be granted automatically by the Licensing Authorities once planning, zoning, health and other regulations are satisfied. Authorities will not make commercial judgements on applications and existing license holders will not be allowed to block new applications. The aim of these changes is to ensure that licensing procedures are quicker and more certain.

4.65 *Land Board Regulations.* Regulations in obtaining land through the various land boards adds a further layer of regulation and bureaucracy to an already cumbersome process. Even though the 1990 Incomes Policy Paper recommends an improvement in the efficiency of the departments responsible for the allocation of land, the implementation of the proposal may remain problematic.

4.66 *The Employment Act and Labor Policy.* It has been Government policy to encourage the participation of employers and employees in formulating policies on labor issues. This is reflected in the composition of the Labor Advisory Board, the National Employment, Manpower and Incomes Council (NEMIC), the Minimum Wages Advisory Board and other bodies. Government also considers it an important responsibility to maintain industrial peace between employers and employees. Its role is to assist the process of collective bargaining, encourage the formation of representative organizations and, as a last resort, act as arbiter.

4.67 This policy has been reasonably successful and Botswana has enjoyed a relatively high degree of industrial peace. Government has involved itself directly in the maintenance of adequate levels of wages, industrial labor protection, industrial safety and other aspects of labor protection. Management interests are represented by the Botswana Confederation of Commerce, Industry and Manpower (BOCCIM). The Botswana Chamber of Commerce and Industry (BCCI) has also been established to represent the interests of small locally owned businesses. The interests of labor are represented by the Botswana Federation of Trade Unions (BFTU).

4.68 It is felt that impediments exist within the Employment Act which do not permit effective collective bargaining. Consequently, amendments to the Employment of Non-Citizens Act, the Employment Act, the Trade Disputes Act and the Trade Unions and Employers' Organizations Act are being discussed in Parliament with a view to removing constraints to collective bargaining.

4.69 *Schooling, Housing and Health Facilities for Foreign Investors.* Schooling, housing and health facilities in Botswana are all recognized as inadequate to cater for a rapidly growing population. This has made it even more difficult to recruit expatriate skills when such services are in short supply.

4.70 Government recognizes that private English medium schools have an important role, since their availability is a consideration in attracting investors and skilled expatriates to Botswana. These schools are required to be self-financing but, in line with the recommendations of the Presidential Commission on the Review of Incomes Policy, Government will make land available for the establishment of private schools and will provide curriculum materials and professional advice.

4.71 As regards housing, Government's objective is to ensure that every citizen has access to safe and sanitary housing. The emphasis will be on the provision of an adequate number of serviced residential plots for sale to the public. This is an appropriate solution to achieve levels of private residential housing that are affordable to middle and higher income citizens. The Government's strategy is designed to ultimately move toward equilibrium in the markets for housing and serviced land, while ensuring that citizens have access to affordable housing.

4.72 *Particular Issues for Citizen Investors*. Citizen investors face more serious constraints than foreign investors. Some of the more important constraints include: lack of entrepreneurial, technical and business skills; limited access to finance, land and basic infrastructure; lack of identified markets; and, competition from imported products.

4.73 *Lack of entrepreneurial, technical and business skills*. Entrepreneurship is still underdeveloped in Botswana. This has impacted on the ability of local businessmen to establish and run profitable enterprises. Government, has tried to address this problem by reserving certain activities for citizen entrepreneurs and providing them with marketing assistance and consultancy services. The Ministry of Commerce and Industry, through its Integrated Field Services (IFS), provides extension services to these investors. Lack of technical, business and management skills are also an important restriction on the development of successful local businesses.

4.74 *Limited access to finance*. It is often difficult for local investors to secure finance from lending institutions because they have not established banking relationships or a business track record. Many citizens also fail to secure financing due to poor project preparation prior to submitting proposals to financiers. They are also frequently not able to offer adequate security on loans. The situation is even worse for women married in community of property because, under existing laws, they are considered legal minors and therefore cannot borrow in their own right. This is an important impediment for a potentially large pool of local entrepreneurs. Government has tried to offer subsidies through programs such as FAP and the Small Borrowers Fund (operated by the NDB) to alleviate this problem.

4.75 *Access to land and basic infrastructure*. The inadequacy of basic infrastructure, especially in rural areas, is also a limiting factor in sustaining viable business enterprises. In addition, rural enterprises face high transportation costs for raw material supplies, which have to be transported from urban areas. Access to, and availability of, serviced land can also be problematic for small local investors -- and the cost of plots is very high.

4.76 *Lack of identified markets*. This can also be a problem for local investors because potential markets are far away, and communication is often difficult. Moreover, transport problems reduce the reliability of delivery to distant markets.

4.77 *The Implementing and Monitoring Capacity of Government*. In many instances, the slow progress that has been made in recent years in overcoming the several constraints that have been identified in this chapter can be traced to the gap that has developed between the implementation and monitoring capacity of Government and the increasing scale and complexity of Government activities. Many decisions that have been taken by Government with respect to policies, projects and the operations of parastatals, and publicly announced, have been slow to be implemented, and the monitoring procedures of Government seem to have been lax in

identifying delays in implementation. Moving toward automatic, uniform and transparent systems of incentives should reduce the burden now placed on the implementation capacity of Government. Nonetheless, it is recommended that a thorough review of the Government's monitoring procedures should be undertaken.

C. CONCLUSIONS AND RECOMMENDATIONS

4.78 This discussion of the advantages and constraints confronting domestic and foreign investors, contemplating the initiation or expansion of business in Botswana, indicates that there is scope for improving Botswana's industrial development policy. Clearly, Botswana must build upon its existing advantages of stability, responsible economic policy (both fiscal and monetary), rapid human resource development, efficient and well maintained infrastructure and utility services, and the freedoms to produce, market and finance. Any attempts to erode these advantages must be resisted and every effort made to build further upon these.

4.79 Similarly, efforts should be made to ameliorate, as much as possible, the disadvantages which exist. For example, high utility costs must be closely monitored, and efforts made, through closer surveillance of efficiency and cost-cutting measures by parastatal boards, to help reduce the real costs of producing utility services in Botswana. In addition, businesses requiring large inputs of utility services in order to conduct their operations may not wish to locate in Botswana. The high cost of utility services should guide new and expanding businesses in the direction of activities -- such as financial, business and tourism services -- in which utility costs are a negligible part of the total costs of operation.

4.80 In the absence of positive real rates of interest, it is difficult to judge the extent to which a shortage of long term finance may be inhibiting industrial development. It appears to be less of a problem for larger firms than for small and medium scale enterprises and households, and the severity of the constraint is thought to be diminishing. Nevertheless, authorities in Botswana should move towards a more appropriate structure of interest rates -- with positive real lending rates -- so that the real demand for long term finance can be determined. Currently unsatisfied demand for long term financial resources may, in part, reflect negative rates on lending rather than immature capital markets and risk averse lending agencies. Ongoing work, involving the Government and the World Bank, on the development finance institutions, may assist in developing these institutions as more effective medium and long term financiers within the economy. Other options, such as the establishment of an on-lending fund for long term lending, may also warrant further examination.

4.81 It is important that real wage increases do not get out of line with increases in productivity. As a major wage setter within the economy, the Government should ensure that salary increases for civil servants are not above the level of price inflation -- and preferably at a lower level to take account of normal creep within the salary structure and to achieve some reduction in real wages, pending significant increases in productivity.

4.82 Land and housing continue to be a constraint on industrial development in Botswana. It appears that they will remain a constraint even after the ALSP has been fully implemented. It will therefore be necessary for Government to continue, on an on-going basis, to ensure that serviced land is made available for residential, commercial and industrial purposes. This process may be accelerated by the greater involvement of private sector developers. It will

also be important for BHC to move out of the housing rental business and to redefine its role in a substantially deregulated market in which the Government is no longer a major landlord.

4.83 Despite some favorable developments, the regulatory framework in Botswana could be improved further. Of particular concern is: the slowness of the bureaucracy surrounding work and residence permits for expatriates; the continued inadequate operation of the waiver system; the priority processing of work and residence permits for "critical occupations"; and, a lack of efficiency in the departments responsible for the allocation of land. These issues must be urgently resolved if the Government is to seriously encourage investment in the industrial sector. In addition, there is a need to monitor the industrial and commercial licensing system, which has recently been streamlined, and ensure that the redrafted Employment Act meets the needs of a pro-active industrialization policy.

4.84 As they are an important segment of the potential pool of investors, yet facing particular difficulties, the Government should continue to support the activities of citizen investors. This support should not come from restricting markets and the activities of foreign investors, but rather through intensified programs to help develop entrepreneurial, technical and business skills and the preparation of projects for financing. Continued assistance through the provision of small scale factory shells may also be appropriate.

CHAPTER 5

INVESTMENT PROMOTION POLICIES

A. POLICY FRAMEWORK

5.1 The Government of Botswana is committed to playing a supportative role in an economy that is essentially private sector driven. Policy measures relating to the development of the industrial sector are intended to create an enabling environment for private enterprise development. From the 1966 Transitional Plan for Social and Economic Development, published at independence in 1966, to the current NDP 7, the guiding principle has been to encourage private initiatives within general confines laid down by Government. Among the seven main policies identified in NDP 7 for the development of industry and trade, the recognition of the private sector's role comes first, followed by related policy elements of varying importance, as follows:

(a) create a more enabling environment for private sector development;

(b) attract investment and promote exports;

(c) strengthen intersectoral linkages;

(d) encourage the informal sector;

(e) improve the application of science and technology innovations;

(f) relax construction constraints;

(g) improve industrial relations.

5.2 The strategy for industrial development as defined in the current plan differs little from its predecessors. It provides continuity, and scope for adjustment and improvement where there is a perceived need for such measures. The main policy elements for encouraging private sector growth in the Seventh Plan period include -- sound economic management, a less restrictive regulatory regime, investment and export incentives, employment incentives, and human resources development.

5.3 *Sound Economic Management.* The Government of Botswana has pursued prudent macroeconomic policies which have allowed manufacturing and agriculture to grow, notwithstanding the overwhelming importance of the mining sector. In particular, macroeconomic management has ensured that the real exchange rate has not risen in response to large balance of payments surpluses generated by mineral revenues. Expenditure levels have been maintained well below income, and a long run of budget surpluses has led to a build up of Government cash balances. Two special funds were created in 1972/73 -- the Revenue Stabilization Fund (RSF) and the Public Debt Service Fund (PDSF). The RSF operates as a buffer between year to year fluctuations in revenue and long term public expenditure requirements. The PDSF invests in domestic projects which should yield a flow of interest and principal repayments to match Botswana's debt service obligations abroad. Both the RSF and the PDSF fund local development finance institutions.

5.4 *Exchange rate policy* has been used to influence the domestic inflation rate and to maintain the competitiveness of domestic enterprises producing tradeable goods. Devaluation of the pula over the recent past has helped to improve the competitiveness of manufactured exports and keep prices of locally produced goods in line with those of competing imports. However, for social reasons, the Government is cautious about measures likely to increase import prices -- not only is the economy highly import-dependent, but the share of imports in the consumption basket of the poorest groups is relatively large because many basic food stuffs are imported. The distributional implications of exchange rate policy have meant that the authorities have tried to keep a close link between wage rate policy and movements in the exchange rate.

5.5 Management of the exchange rate is complicated by the fact that the main exports -- minerals and beef -- are dollar denominated while most imports and manufactured exports are priced in rand or Zimbabwe dollars. This makes Botswana particularly sensitive to cross exchange rate movements. Real exchange rates between the pula and the rand, and the pula and the Zimbabwe dollar (calculated at the nominal rate of exchange, adjusted for inflation in the two countries) fluctuated within relatively narrow limits until recently. Since 1990 the rapid depreciation of the Zimbabwe dollar, in conjunction with that country's adjustment program, has made it very difficult for producers in Botswana to sell competitively to Zimbabwe -- previously an important market for manufactured exports. The appreciation of the pula against the rand has been more gradual.

5.6 Since 1972, Botswana has adhered to an *incomes policy* which has helped to maintain the competitive position of local producers by limiting increases in wages. A revised National Policy on Incomes, Employment, Prices and Profits was introduced in 1990 which does away with some of the more restrictive aspects of the previous policy, allowing free and direct wage negotiations between employees and employers in the private sector. Parastatals have also been given greater flexibility in determining wages and grading structures. Changes in Government salary levels include the decompression of senior management salaries and higher initial pay for those with particular professional or technical skills, in the hope of stemming the outflow of senior and skilled employees to the private sector. Minimum wages are established for unskilled workers in retail and wholesale trades, manufacturing and certain services. Minimum wage regulations do not apply to agricultural workers or domestic workers. Current policy is particularly concerned with improvements in labor force performance and future wage increases are likely to be more closely linked to higher levels of productivity.

5.7 The Government has also used *money and credit* policies in its management of the economy. As part of a more active interest rate management program, issues of Bank of Botswana Certificates were introduced in 1991 to support efforts to move interest rates to positive real levels. The changes are expected to encourage higher domestic savings as account holders move out of current deposits into longer term, interest bearing assets. Exchange control rules governing domestic borrowing by foreign-owned companies in Botswana have also been relaxed, to stimulate demand for credit. These regulations are now more favorable than in most countries in the region.

5.8 ***Fewer Restrictions.*** Although the macroeconomic environment for private enterprise is considered favorable, the business community sees Botswana's regulatory system as unnecessarily restrictive. The most criticized regulations involve access to land for business and housing purposes, the employment of foreigners, and industrial licensing procedures (see chapter 4). A 1982 Presidential Commission on Economic Opportunities and a 1990 Presidential Commission for the Review of the

Incomes Policy both addressed, inter alia, the impact of unnecessary regulations on Botswana's faster economic development. The 1990 Commission's report was the basis for a White Paper which became the Revised National Policy on Incomes, Employment, Prices and Profits. It was approved in 1990 and led to the resuscitation of the Regulations Review Committee (RRC). The RRC prepared a blueprint for legal and administrative changes required to implement the proposed reforms. Overcoming entrenched civil service regulatory attitudes, however, remains one of the most intractable problems.

5.9 ***Investment and Export Incentives.*** Botswana's business environment offers key advantages which are important to foreign investors. Political stability, the proven commitment to good governance, sound economic management, a relatively stable currency, an open door policy towards foreign participation in the economy and the provision of a level playing field for domestic/foreign and private/public investment make Botswana a more attractive proposition in the global investment market than could be achieved with an incentive package alone.

5.10 A specific investment promotion policy was introduced in 1982 with the introduction of the Financial Assistance Policy. FAP was designed to assist new businesses and the expansion of existing businesses which produce or process goods for import substitution or export. Applicants are divided into small, medium or large scale, depending on the proposed level of investment. Small scale projects are restricted to citizens. All financial assistance is in the form of grants, if the conditions attached to the assistance are met. The two main types of assistance for medium and large scale enterprises are:

(a) Automatic Financial Assistance (AFA) in the form of reimbursements;

(b) Case by Case Financial Assistance (CFA) in the form of grants which are part of taxable income;

Other assistance programs include:

(c) The Selebi-Phikwe Special Incentive Package to promote export manufacturing projects in this region. In addition to reimbursements and grants available under the AFA and CFA systems, qualifying investors may be granted corporate tax concessions and withholding tax exemption on dividends paid from after tax profits. One of the preconditions for the Special Incentive Package is that 100 per cent of the project's output is exported outside the Southern African region (SADCC and SACUA).

(d) The Local Preference Scheme for manufacturers resident in Botswana. This scheme takes the form of a 40 per cent price advantage on local (Batswana) value added when tendering for sales to the Government, local authorities and parastatal companies, subject to fairly strict local content ratio requirements.

(e) Exclusive licenses may be granted for a specific product, for a specific area in Botswana, or for the whole country if demand for the proposed product is limited.

(f) Infant industry tariff protection may be granted under the provisions of the Southern African Customs Union Agreement (SACUA) to enable new industries to compete with producers in the Common Customs Area, provided that the higher tariff duty is levied equally on goods produced in other SACUA countries or imported directly or indirectly

from outside the Common Customs Area. New industry tarift protection may be granted for four years, extendable once only, for a further four year period.

Under the terms of the FAP White Paper (1982), investors may only benefit from one of three major incentive schemes, FAP, local preference or tariff protection, at any one time.

(g) Whilst most of the above incentives are particularly designed to promote labor-intensive activities, capital-intensive projects can benefit from discretionary incentives granted in the form of Development Approval Orders and Tax Agreements under the Income Tax Act. The benefits of these incentives are felt only when enterprises begin to make profits.

5.11 Botswana's network of *trade agreements* makes up for some of the disadvantages of being a small landlocked country in a mostly low income, low growth region. These include: membership of the Southern African Customs Union (SACU); a bilateral trade agreement with Zimbabwe; a 1956 agreement covering trade with Malawi; the Southern African Development Community (SADC); and the Preferential Trade Area (PTA) in which Botswana is an observer. Particular export advantages are also available under the terms of the Lomé Convention for ACP States; Botswana is covered by the Generalized System of Preferences (GSP); and it is associated through RSA and SACUA with the General Agreement on Tariffs and Trade (GATT).

B. INSTITUTIONAL FRAMEWORK

5.12 Government and the private sector are considered to be equal partners in providing an institutional framework for development of the industrial sector -- as indicated in NDP 7. Policy making is also increasingly becoming part of a dialogue between the private and public sectors. What has made this possible is the emergence of an articulate private sector counterpart to the Government, in the form of the Botswana Confederation of Commerce, Industry and Manpower (BOCCIM) -- which represents private sector and some parastatal interests. From a small talking shop, it has grown into a reasonably well staffed, pro-active organization lobbying for private enterprise interests. Financed by membership subscriptions related to number of employees, BOCCIM now has over 1,000 affiliated organizations. BOCCIM advises employers on collective bargaining and other labor related matters and represents its members in tripartite bodies such as the National Employment, Manpower and Incomes Council. BOCCIM operates a small business division -- for businesses with ten or fewer employees -- which had 500 members at end-1990. It also operates a counselling scheme under which member firms can receive assistance from established member enterprises. In addition, the Botswana Chamber of Commerce and Industry (BCCI), was established in 1990 to represent the interests of small, mainly Batswana-owned, businesses.

5.13 The interests of organized labor are represented by the Botswana Federation of Trade Unions (BFTU) to which twelve of the sixteen existing unions are affiliated. Union membership represents about 20 percent of the private sector work force. The trade union movement suffers from a lack of experienced Batswana negotiators. Strikes have become more frequent since 1989, particularly in the public sector. This is partly due to the inadequate collective bargaining machinery established under the Employment Act of 1982, and other shortcomings of the 1982 Trade Disputes Act and the 1983 Trade Unions and Employers' Organizations Act. Suggested amendments to all three laws have been put

forward and these are currently under consideration by Parliament. A plan to set up an industrial court to arbitrate on labor-related grievances and disputes is also at an advanced stage of discussion.

5.14 The main public sector institution concerned with industrial policy formulation, investment promotion and trade policy is the Ministry of Commerce and Industry (MCI). Two MCI departments are particularly important in their interaction with the private sector and in promoting investment. First, the Department of Industrial Affairs provides support services through its administration of FAP and the Local Preference Scheme, as well as being responsible for the Integrated Field Services; it also plays a key regulatory role in ensuring compliance with the Industrial Development Act. Second, the Department of Trade and Investment Promotion, whose role is self-explanatory.

5.15 The dual role of the MCI can, and does, lead to conflicts of interest within the Ministry. The difficulties encountered in reconciling MCI's role as a regulator (licensing authority), and a promotor (attracting investors, involvement in some of the committees which approve FAP projects), lead to delays which discourage foreign investors and are potentially harmful to small scale investment.

5.16 Somewhat removed, the Selebi-Phikwe Regional Development Program (SPRDP) is managed by a special project unit funded by the Ministry of Finance and Development Planning with a World Bank loan. Selebi-Phikwe is a copper-nickel mining town with a limited life determined by ore supplies. The Government wishes to ensure the town's economic viability once the life of the mine has come to an end. Hence, the SPRDP was established in 1988 to promote investment in non-mining activities. The incentives available for industrialization are the same as those offered elsewhere in Botswana plus special tax breaks for wholly export oriented enterprises.

5.17 Other public sector support organizations for private enterprise development deal with small scale and rural industries, technology adaptation, and financing. These include:

(a) *Integrated Field Services*, part of MCI's Department of Industrial Affairs, which provides technical and management training and marketing assistance to promote citizen-owned small and medium scale production. IFS offers consultancy services and training to local traders and is the agency responsible for coordinating the activities of small business extension agencies. It offers training and other types of assistance to rural producers.

(b) *Rural Industries Promotions* is concerned with the dissemination of appropriate technology in rural areas. It operates the Rural Industries Innovation Center in Kanye and the Pioneer Rural Industries Center in Palapye.

(c) The *Brigades* are private sector and community-owned trusts. They provide technical training for small scale industrial and commercial activities in rural areas. The *Brigades Development Center* (BRIDEC), reporting to the Ministry of Education, offers auditing and business management services to Brigades.

(d) The *Botswana Technology Center* (BTechC) is a parastatal organization reporting to MFDP. It advises private and public sector entities on appropriate technology choices.

(e) The *Industrial Extension Coordinating Committee* (IECC) acts as a coordinating agency for the agencies and financial institutions listed here.

(f) The *Industrial Development Advisory Committee* defines and formulates industrial policies, objectives and strategies. Members include MCI, MFDP, MMRWA, MOH and MLGLH.

(g) The *Botswana Development Corporation* (BDC), established in 1970, provided an important first step on the road to a coherent system of industrial development support services. It provides loan and equity finance to new and expanding firms. Through its subsidiary, *Tswelelo*, it assists small citizen-owned enterprises. Another subsidiary, *Botswanacraft*, purchases and promotes production of handicrafts in rural areas. BDC is Botswana's largest development finance institution.

(h) The *National Development Bank* (NDB) is also a parastatal development finance institution. It provides long and short term loans to industry, trade and agriculture.

5.18 Finally, Botswana's public utility companies produce reliable supplies of electricity, water and telecommunications services. Prices to consumers are not subsidized,[1] thus avoiding distortions in demand and inadequate returns on investments. Such distortions, particularly on energy use, are apparent elsewhere in the developing world where they have had economically crippling effects. Nevertheless, producers in Botswana feel themselves at a disadvantage in terms of utility costs compared with subsidized and lower cost sources of supply in neighboring countries, and consequently press for price reductions. While the utilities' operations must be closely monitored to ensure efficiency, the Government would be sacrificing long term viability for a short term, marginal, reduction in manufacturing costs if utility subsidies were introduced. In the case of energy and water, artificially low prices also encourage waste whilst discouraging investment in new and more efficient ways of using these resources. Certainly neighboring countries' subsidization schemes for utility prices will have to be phased out -- with inflationary consequences -- as governments realize that low prices may undermine a utility company's financial viability and hence its ability to maintain, let alone increase, supply. Such policies are clearly not sustainable over the longer term.

C. PRIVATE/PUBLIC SECTOR DIALOGUE

5.19 Botswana is a small country in which relations between the private and public sectors should be part of everyday life. However, there are few formal, established mechanisms for private/public sector dialogue. Two recent conferences on private sector development, sponsored by BOCCIM, have provided an opportunity to bridge this gap. The second conference took place in September 1991, in Francistown, and brought together representatives from the private, parastatal and Government sectors to discuss the respective roles of the private and public sector in Botswana's development. The list of recommendations made at the end of the conference covered most of the issues on which the private sector has been trying to persuade the Government to act. They were also referred

[1] Although it is important to note that Government equity injections into these utility parastatals, and subsidized loans, from the PDSF and the RSF, do provide some element of subsidy to these institutions.

to in the 1992 Budget Speech[2] when the Government committed itself to a further review of the recommendations and the formulation of an appropriate action program. NEMIC was to be responsible for the follow up. The recommendations concern two investment environment issues which have surfaced repeatedly in reviews of Government investment promotion policies in the recent past. These are:

(a) the need to provide serviced industrial land and residential housing;

(b) the need to orientate education and training towards technical, professional and management skills.

5.20 Other recommendations reflect specific aspects of the early 1992 political and economic environment and include, inter alia: redeploying the "peace dividend" due to the changed conditions in the Southern African region, from the Botswana Defence Force to the police; rooting out corruption wherever it exists; promptly implementing national policies; and, establishing mechanisms for more effective high level contacts between the private sector and Government.

5.21 In the 1992 Budget Speech, the Minister for Finance and Development Planning stated again that the promotion of the private sector was essential to diversification and national development, and stressed the need to raise productivity and efficiency in the civil service. The intention to treat the private sector as "the engine for future growth in Botswana" certainly exists -- delivering effective support and eliminating unnecessary restrictions, however, remains a slow process in the face of bureaucratic inertia.

5.22 In parallel with efforts to improve the administrative framework for private sector operations in Botswana the Budget foresaw a need to redouble efforts to attract foreign investment. Here again an enabling environment, efficient public sector performance and freedom from unnecessary regulations are recognized as essential preconditions. Behind the drive to attract foreign capital lies the Government's perceived inability to provide all the resources for additional investment from mineral revenues. Other sources of domestic savings will be explored (hence the rise in interest rates to encourage household savings), but additional foreign investment, and the modern technologies and technical skills that accompany it, are key objectives in the formulation of Botswana's investment promotion strategy

D. CURRENT INDUSTRIAL DEVELOPMENT STRATEGY: A CRITICAL REVIEW

5.23 The industrial sector has grown rapidly -- employment has been created in the sector and the economy has become more diversified. With support from such Government programs as FAP there has also been an increase in the number of citizen-owned productive enterprises. Investment promotion policies have been even-handed in their influence on the orientation of industries; both import substitution and export sectors have benefited. A lack of protection has encouraged internationally competitive manufacturers -- an essential development given the small size of the domestic market.

5.24 Free access to South Africa's much larger and richer market has benefited Botswana's

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[2] Budget Speech, February 10, 1992, para 52.

manufacturing sector in the past, and is a vital element in determining its future potential. Unlike manufacturing industries in other parts of Sub-Saharan Africa, inputs and outputs have not been subsidized by the rest of the economy. Although FAP has encouraged labor-intensive production, the availability of foreign exchange and low interest rates also favored capital-intensive investments, including unrestricted imports of know-how and state-of-the-art technology. While industry in most African countries suffered from low rates of capacity utilization, Botswana's enterprises faced the unusual problem of acute land shortages for expansion.

5.25 The initial conclusion is that the commitment to private sector driven industrial development is a success. However, there are several issues which will need to be addressed in designing the industrial investment strategy for the 1990s. Most important, will be the extent to which the development of labor intensive manufacturing industry for its impact upon generating large numbers of unskilled jobs, should continue to be the prime focus of policy makers. This will depend upon developments in the labor markets and the ability of the economy to continue to absorb new entrants into the labor force and immigrants from rural areas. To assist policy makers in selecting the best set of incentives for industry, and the extent to which they should be focussed on large volume, low skill employment creation or alternatively the scope that exists to move towards higher value, higher productivity, and high quality production, will depend upon a better understanding of these markets. Although it is unlikely that Botswana will be able to consistently generate new employment opportunities at the rate that it has done over the 1980s, it is not known what level of employment creation will be necessary to absorb all new entrants while leaving rates of unemployment at their current relatively low levels. Better and more timely data on wages, employment, unemployment and productivity in all segments of the labor market (both formal and informal) will be required, to allow a more comprehensive analysis of labor market trends and the subsequent adoption of the most appropriate policies. In the absence of better information in this regard, the following analysis is based on the premise that, even at lower rates of employment growth, Botswana should be able to maintain unemployment at relatively low levels, and will therefore be able to adapt incentive policies accordingly. Nonetheless, a more fuller substantiation, through more detailed analysis based on data not currently available, would be useful.

5.26 ***Financial Assistance Policy***. Botswana introduced its Financial Assistance Policy (FAP) in 1982, intending to:

(a) create sustainable employment for unskilled workers;

(b) produce goods for export or to substitute for imports;

(c) diversify the economy to lessen dependence on large scale mining, beef exports, and growth of the public sector;

(d) improve citizen skill levels through training;

(e) promote infant industries.

Given the emphasis on employment generation, FAP incentives were structured to encourage greater employment of unskilled and semi-skilled workers. The FAP Capital Grant, for example, is based on the number of actual or projected employees, and the FAP Labor Grant on wages paid to unskilled and semi-skilled workers. FAP also seeks to achieve geographical diversification of industry by offering

greater incentives to those companies locating in rural areas or in the Selebi-Phikwe region.

5.27 The Financial Assistance Policy with respect to medium and large scale enterprises is a well designed scheme based upon sound economic criteria of providing initial financial support to assist companies overcome disadvantages arising from operating in the Botswana market. The financial support, which is largely based on employment levels, is designed to gradually phase out over the five year period of assistance, as the company matures and begins to operate on a more financially self sustaining basis. FAP has indeed served to generate employment for unskilled personnel and has helped to diversify the economic base. In many respects it has, therefore, been successful in achieving the goals which it was designed to address. However, in other respects, the operation of FAP has not been as effective as originally expected. Increasingly, the Government is beginning to question the efficiency of a scheme with disbursements which are increasing at 65 percent per annum; leading to outlays of P20.3 million in 1990/91; is the subject of fraud and corruption; and has promoted industries of questionable sustainability. Increasingly, there is also a need to consider a broader system of incentives for all industries in which Botswana may have a comparative advantage to compete and thereby generate employment -- in a sustainable manner.

5.28 From 1982 through fiscal year 1990/91 the program had disbursed P69.6 million and had committed P238.7 million[3], contributing to the creation of some 20,000 jobs. Medium and large-scale FAP projects registered projected new employment of 26,435 from 1982 through 1991, and actual new employment of 12,631, of which about 10,400, or 80 percent, were in manufacturing and the remainder in agriculture. Small-scale FAP projects showed projected creation of 9,138 new jobs during the same period, of which 6,500, or 70 percent, were in manufacturing and about 2,600 in agriculture. Due to inadequate monitoring of small-scale projects, the actual number of jobs created is unknown. Largely as a result of the Selebi-Phikwe initiative, there was an acceleration in FAP commitments after 1989. From P21.7 million in 1990, commitments for medium and large scale projects increased to P57.6 million in 1991. Commitments for large-scale projects in Selebi-Phikwe grew from P2.8 million in 1990 to P27.4 million in 1991.[4]

5.29 Conclusions on employment creation attributable to FAP should be treated with caution, and should be examined in the context of overall growth in employment in the economy. As table 5.1 shows, there are significant differences between projected employment, actual employment and sustained employment. As discussed below, an estimated 50 percent of small-scale FAP recipients have failed, reducing net employment creation from small-scale FAP to around 4,000 to 5,000 jobs from 1982 to 1991. While the failure rate for medium- and large-scale companies is far lower than 50 percent, evidence of reduction in employment levels in such companies following expiry of the FAP grants, combined with a failure rate of 10 to 15 percent (the figure obtained in the 1988 FAP evaluation, cited below), indicate that the actual, net increase in employment from medium- and large-scale FAP companies is between 8,000 and 9,000 during 1982 to 1991. Combined with small-scale projects, the total, continued increase in employment attributable to FAP is probably not more than 14,000, or 1,400 per year. By contrast, overall formal sector employment grew from 97,400 in 1981 to 228,900 in 1991.

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[3] FAP commitments are for the full five years of grants payable; hence, commitments through 1991 reflect expected disbursements through 1996 on projects already approved.

[4] Ministry of Finance and Development Planning, Botswana, unpublished figures, 1992.

The private and parastatal sectors accounted for the bulk of this new job creation, increasing by 92,700 jobs to 157,500 between 1981 and 1991. FAP-assisted industrial companies accounted for possibly 11,500 (12 percent) of the increase in non-Government jobs over this period. Since many small-scale industrial projects, such as bakeries or carpentry, are not classified as manufacturing industries, FAP-assisted companies accounted for around 50 percent of the jobs created in the manufacturing sector, in which employment grew by 20,000 jobs from 1981 to 1991.

Table 5.1: Projected, Actual and Sustained FAP Job Creation 1982 to 1991

	Projected jobs created	Actual jobs created *	Actual jobs remaining after FAP (estimate)
Small-scale (industrial)	6,536	6,536	3,250
Small-scale (agriculture)	2,602	2,602	1,300
CFA (manufacturing)	15,018	6,654	4,990
CFA (agriculture)	4,910	2,295	1,721
AFA	6,507	3,682	3,300
INDUSTRIAL: Med./Large	21,525	10,336	8,290
Small-scale	6,536	6,536	3,250
TOTAL INDUSTRIAL	28,601	16,872	11,540
TOTAL	35,573	21,769	14,561

* Actual, as opposed to projected, small-scale FAP job creation is unknown.
Source: Ministry of Finance and Development Planning.

5.30 Formal sector employment growth in almost every one of the past ten years has exceeded 10 percent, far outpacing the rate of population growth. Growth in the private and parastatal sectors has averaged over 13 percent annually over the past ten years. While unemployment and underemployment continue as problems, all evidence suggests that the rate of unemployment is declining and that jobs are being created at a higher rate than the rate of growth of the labor force. This calls into question the need for a policy, such as FAP, that subsidizes employment creation.

5.31 Although Small-Scale FAP's actual contribution to employment growth is unknown, there is little doubt that the program has had a positive effect on job creation and development of economic opportunities, especially in rural areas. By the end of 1991, 1,708 industrial and 1,172 agricultural projects -- 85 percent of them in rural areas -- had received FAP small-scale assistance. The cumulative total FAP contribution to these projects was P11.6 million. FAP small-scale assistance during 1982 to

1991 supported the creation of some 3,250 industrial and 1,300 agricultural jobs. Projects were concentrated in knitting and sewing, carpentry, bakeries, brick-making, and metal working.

5.32 It is difficult to determine how many of these projects ultimately survived. The 1988 evaluation of small-scale FAP, conducted by the Ministry of Finance and Development Planning (MFDP), reported that, of a total of 747 small-scale FAP projects approved from 1982 to 1986, 142 failed or otherwise ceased operations. That report cautioned, however, and anecdotal evidence suggests, that the actual failure rate is likely to be much higher, and that some 50 percent of small scale enterprises fail. This estimate is supported by the 1988 evaluation of the whole FAP program[5], which suggested that 40 to 50 percent of small-scale FAP recipients fail. Although this may appear high, a 50 percent success rate among entrepreneurs with little or no prior business experience and a work force with minimal wage-earning experience is impressive. Furthermore, the evaluation report suggested that this was lower than the failure rate for non-FAP small-scale enterprises, and less than the failure rate for small-scale enterprises in other countries. While small-scale FAP clearly will not provide the sole solution to Botswana's unemployment problems, it is providing necessary assistance to entrepreneurs and workers, some of whom otherwise might have few opportunities in the formal sector. When combined with the technical assistance provided by Integrated Field Services to small-scale enterprises, small-scale FAP appears to make a useful contribution to future industrial development.

5.33 Small-scale FAP is at present restricted to those companies whose total fixed investment does not exceed P25,000.[6] It may be appropriate to raise this limit again. Inflationary effects indicate that the P25,000 in 1985 would be worth about P60,000 today. Raising the limit to this level, or even higher will, however, require changes in the way small-scale FAP is administered. While the present system requires a sponsor's contribution of only five percent of the total capital investment, allowing people to obtain up to P60,000 in unsecured and unaccountable grants would be an invitation to wholesale corruption. Raising the limit would therefore require more stringent qualification criteria and an increase in the sponsor's required contribution. For companies with total fixed investment exceeding P25,000, for example, the required sponsor's contribution could be raised to 10 percent or even as high as 25 percent. In addition, for companies at the higher end of the small-scale range, FAP rules could state that FAP grants could form no more than 50 percent of the total project cost, obliging project promoters to seek funds from commercial banks or other sources, thereby reducing the scope for fraud or poor project conception and management. These changes to FAP will entail a more rigorous concentration of effort to evaluate, assess, audit and monitor small-scale FAP projects, both as a means of evaluating the success of the program and as a way to avoid larger losses through an enlarged program.

5.34 FAP assistance to medium-scale (total investment between P25,000 and P900,000) and large-scale (total investment greater than P900,000) enterprises provides a wider range of grants and tax holidays, spread over the first five years of a project's operation, than is the case with small-scale FAP. It is intended to assist entrepreneurs who are assumed to have greater resources of capital and greater technical and managerial ability than those receiving small-scale FAP. Open to citizens and non-citizens

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[5] *Evaluation of the Financial Assistance Policy: FAP and its Role in Botswana Business Development*, Ministry of Finance and Development Planning, 1988.

[6] In 1985, this was raised from P10,000 to P25,000 to take account of inflation and to correspond more closely with National Development Bank limits for small borrowers.

alike, medium and large-scale FAP is, at least in part, an incentive to foreign businesses to invest in Botswana rather than in other countries. As such, it must be evaluated in comparison to other countries offering a combination of financial and tax incentives and economic and business conditions that compete directly with those Botswana has to offer. In common with the small-scale program, medium and large-scale FAP offers greater incentives to projects in rural areas and the Selebi-Phikwe region, and calculates grants based on total employment and wages paid to unskilled and semi-skilled workers, as well as on domestic value added.

5.35 The case in favor of medium- and large-scale FAP is not as persuasive as for small-scale FAP. Concerns include:

(a) Potential for abuse, especially with the FAP capital grant;

(b) Demonstrated failure of companies to achieve competitive levels of labor productivity before expiration of the FAP labor grant;

(c) Evidence that many companies reduce the number of people they employ once the FAP grants have expired;

(d) Lack of long-term benefits from the Sales Augmentation Grant (SAG), and the inability of a short-term benefit such as the SAG to redress what may be a permanent or long-term cost disadvantage for Botswana businesses;

(e) Evidence that rapid employment growth has taken place in sectors which have not qualified for FAP assistance, both reducing the acuteness of the unemployment problem and calling into question a program whose primary purpose it is to subsidize employment in labor-intensive manufacturing industries;

(f) Potential conflict between FAP's purpose of stimulating job creation and its purpose of assisting infant industries (the possibility that, by encouraging over-employment FAP delays or prevents companies from developing internationally competitive technology and labor productivity).

5.36 The 1988 evaluation of FAP, reviewing the first five years of the program, conducted a survey of 71 small, medium and large-scale FAP recipients, seeking to identify the extent to which FAP grants had stimulated employment creation. Of 39 medium and large-scale FAP recipients, 15 (38 percent), reported that FAP incentives had caused them to employ more people than they otherwise would have done, or to have undertaken investments they otherwise would not have made.[7] 645 jobs out of a total of 2,341 employed, or 28 percent, were said by the respondents to be the direct result of FAP incentives. This may have resulted in temporary over-employment rather than long-term increases in sustained employment. An estimated 65 to 70 percent of FAP medium and large-scale recipients, although they continue to operate after the subsidies have expired, do so with some reduction in their work force. It is reportedly a common practice for companies to begin shedding workers at a modest rate after the third year of FAP grants (usually the point at which companies are evaluated to determine

[7] *op. cit.*, pp. C-7 to C-8.

whether they must reimburse a portion of the capital grant if actual employment is lower than the figure on which the capital grant was based), and to accelerate their retrenchment after the fifth year.[8] Precise figures on the extent to which this occurs are difficult to obtain, since the Internal Audit Department of MFDP lacks the resources to carry out regular and random audits of companies, and conducts no audits once the FAP grants have expired. The 1988 FAP evaluation, however, cites one example of a company employing 103 workers which, once FAP grants expired, dismissed 73 and claimed to be able to operate with the remaining 30 workers with no loss of production capacity.[9] The 1988 evaluation also suggests that this is not an isolated case, although it presents little in the way of detailed evidence. Whatever changes are made in FAP incentives, there is a clear need for more detailed auditing of projects, both during and after the period in which grants are paid out, so that the effectiveness of the program can be evaluated more accurately.

5.37 Perhaps no other element of the FAP program is so readily subject to fraud and misrepresentation as the *Capital Grant*. Since in most cases the suppliers of capital equipment are located outside Botswana, the potential for over-invoicing (shipment of machinery of lesser value than that indicated on the invoice), and other abuses is enormous, potentially involving collusion between the company in Botswana and the overseas equipment suppliers. Although Government can demand repayment of the appropriate portion of the FAP capital grant if the project fails to meet projected employment levels, this does not protect against companies that willfully misrepresent the facts in order to obtain fraudulent FAP assistance. The existence of several well-documented and well-publicized cases of FAP fraud indicates that the proportion of risk to benefit with FAP capital grant assistance is high, and the potential for abuse great. Since by far the largest FAP capital grants have been paid to well-capitalized foreign investors who could, presumably, find adequate capital to invest in a viable project, the rationale for continuing the FAP capital grant in its present form is unclear. There remains, however, a need for some form of assistance to companies which possess good marketing plans and good management, yet lack the capital to start up on their own or even to qualify with respect to the capital requirements of BDC and the commercial banks. According to FAP auditors, some 10 percent of medium and large-scale FAP recipients fall into this category. One response to this problem could be the establishment, by existing financial institutions, of a venture capital fund.

5.38 The *Labor Grant* component of FAP, which reimburses companies for a portion of wages paid to unskilled and semi-skilled workers over their first five years of operation or expansion (80 percent in the first two years, then 60 percent, 40 percent and 20 percent, in years 3 through five, respectively) was intended to compensate for the low productivity of Botswana workers, the expectation being that by the time the grants expired the workers would have received sufficient training and experience to become competitive with workers in other countries. In addition, it was expected that the Labor Grant would induce some companies to adopt more labor-intensive manufacturing methods.

5.39 Wages in Botswana, while not excessively high by Southern African standards, exceed those in other countries, particularly in Asia, that are receiving large inward flows of investment. In Indonesia, for example, average hourly wages are less than half those in Botswana, while the basic level of skills and productivity is considerably higher (see table 5.2). In other countries, such as Vietnam, the

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[8] Personal communication, MFDP Chief Internal Auditor, 1992.

[9] *op. cit.*, p. 50.

wage/productivity comparison is even more to Botswana's disadvantage. This difference does not appear to have been reduced, even in companies that have received the full range of FAP grants over a five-year period. One textile and garment factory reported that its workers in Botswana could produce about 7 pairs of jeans per worker per day. The comparable figure for workers in southern China is 24, while in Zimbabwe and South Africa it is 14. These comparisons work to Botswana's disadvantage in virtually all industries. Botswana bricklayers, for example, are less than one-fourth as productive as their counterparts in South Africa, and as little as five percent as productive as bricklayers in Europe or the Far East. As to the adoption of labor-intensive manufacturing technology, the 1988 FAP evaluation pointed out, "Standard industry practices, quality needs, or production scale [most] often dictate the technology used. Only rarely does the firm have a real choice between labor- and capital-intensive production technology which FAP's temporarily lowering of net labor costs will affect. On the contrary, as FAP also lowers capital costs, it might stimulate more capital-intensive technology."[10] The FAP Labor Grant, therefore, fails to accomplish its principal objectives. It appears to have contributed only marginally to the creation of stable, long-term employment for large numbers of Batswana. It has had only modest effects on increasing the productivity of Botswana workers. And, to the limited extent that it has induced companies to employ, at least temporarily, more workers than they need, it has subsidized inefficient and more costly manufacturing processes. The FAP Labor Grant should, therefore, be abolished. If some form of labor subsidy is still considered essential, it may be preferable to introduce a system of tax credits for employment of semi-skilled and unskilled workers.

Table 5.2: Botswana's Comparative Manufacturing Wages and Productivity

Country	Hourly Wage (garment industry) US$	Production Time (T-shirts) minutes per unit	Unit Labor Cost (T-shirts) US$
Botswana	0.62	21.5	0.22
South Africa	1.61	6.0	0.16
Philippines	0.67	5.0*	0.06
Indonesia	0.25	5.0*	0.02
Thailand	0.92	5.0*	0.08

* Estimate.
Source: Lonrho, World Bank, National Clothing Federation of South Africa.

5.40 The *Sales Augmentation Grant* (SAG), which pays companies an amount equivalent to eight percent of gross sales in the first two years, and six percent, four percent and two percent in years three, four and five, respectively, is often justified implicitly as a compensation for the high cost of utilities, land, construction and transport in Botswana, since it increases with sales volume in the same manner as most direct costs and some overheads do. It also is represented as a sort of export incentive, compensating exporters for the high cost of inland transport to South African ports and for the

[10] *op. cit.*, pp. 63-64

exceptionally high wharfage charges assessed. Its official justification, however, is to help companies break into new markets by subsidizing their sales in their early years of operation while they seek to develop those markets. With the possible exception of land and construction costs, the cost disadvantages addressed by the Sales Augmentation Grant will persist after the grants have expired. Even construction costs, which are passed on in the form of higher rents charged for industrial buildings, have an effect long after the five-year grant period. While some companies may, in fact, need assistance in identifying and penetrating new markets, it is by no means clear that all SAG recipients do, nor is it clear that the SAG has provided any direct assistance in doing so. To the extent, therefore, that the Sales Augmentation Grant is meant to counteract a specific set of disadvantages, it cannot be judged successful. To the extent that it is simply a relatively unfocussed and generalized subsidy to all manufacturers, it is hard to justify. Consequently, there seems to be no compelling reason for retaining the Sales Augmentation Grant in its present form or in any more focussed adaptation.

5.41 The FAP *Training Grant* provides for reimbursement of 50 percent of off-site training expenses incurred during the first five years of operation. In a skills short environment, such as Botswana, a grant of this kind has substantial merit. There have been suggestions that the training grant be expanded to include on-site training as well, or that 100 percent of the cost be reimbursed by Government. In most industries, on-the-job training has proved to be far more effective in training large numbers of people in the skills and processes required by an individual company, many of which skills are also transferable to other manufacturing processes. There is a need, therefore, for Government assistance to be more flexible with regard to on-site training, in spite of the obvious difficulties in distinguishing between on-the-job training and normal production, and in identifying which costs and activities might be eligible for reimbursement. The current FAP Training Grant, however, permits reimbursement of on-site training costs, provided that the firm convincingly separates and substantiates the claimed costs. This provision of FAP does not appear to have been significantly abused. However, if FAP were to cover 100 percent of off-site training costs, then companies would not be subject to any cost discipline of their own and might send too many workers to training courses of questionable value. By continuing to bear some portion of the cost of training, FAP recipients will be encouraged to select the most cost-effective forms of training and to send only those workers most likely to benefit. Certain features of the existing Training Grant should, however, be changed:

(a) All formal sector companies should be eligible for the Training Grant. This should include service sector companies and companies already in operation. However, training grants should be targeted to supporting activities which contribute to a demonstrated improvement in efficiency.

(b) The revised Training Grant scheme should extend for 10 years from its date of inception, and should apply to all companies claiming the grants until the scheme expires. Government should undertake a mid-term and a final review to determine whether the program should be extended and how successful it has been. If it is extended, all companies, including those receiving grants under the initial scheme, should be eligible to continue receiving the grants.

(c) The current requirement that training outside Botswana, on-site training, and training costing more than P2,500 per trainee per year must obtain special permission for FAP reimbursement should be eliminated. Government should establish clear regulations as to the costs and activities that may be covered. A company in doubt as to the eligibility

of certain expenses may seek an advance ruling from the FAP authorities; otherwise, approval should be automatic, and claims subject to audit.

(d) The Training Grant may be increased to cover up to 75 percent of training costs.

(e) Since worker productivity is as much a function of management and supervisory skills as of the skills endowment of workers, training of citizen management and supervisory staff should also be eligible for the FAP Training Grant.

(f) A cap should be placed on eligible training costs, relative to workers' wages (for example, the total training grants payable to a company should not exceed some proportion of its total wages paid to unskilled and semi-skilled workers. This proportion, depending on available resources and a more rigorous analysis of the program's costs and benefits, might be between 25 and 50 percent).

5.42 The 1988 FAP evaluation, based on its survey of both FAP and non-FAP companies, concluded that "most firms' major problem is the inability to identify a competitive market segment, often because of fierce competition from South African firms, but also because of insufficient marketing management skills or a flawed initial business plan." This is a problem that FAP does not address, but which could be addressed in any revision of the program. Establishment of a mechanism by which companies could obtain partial funding for market research and marketing strategy consultancies, as well as assistance in drafting terms of reference for such studies, could be a significant benefit to Botswana companies, particularly those with an export orientation[11]. Most likely under the administration of TIPA, such a program could fund between 50 and 75 percent of the cost of a market study, requiring co-payment of at least 25 percent by the company itself, and could help to identify appropriate consultants and help in preparing terms of reference. This program could also obtain assistance from the Africa Project Development Facility (APDF), African Management Services Corporation (AMSCO) and other donor-funded entities that assist companies in developing countries to conduct market and feasibility studies.

5.43 The 1988 FAP evaluation concluded that Automatic FAP (AFA) failed to fulfill the purpose of the overall FAP program and should be abolished. Among the reasons for this conclusion were:

(a) AFA beneficiaries had been mainly non-citizens;

(b) AFA approval procedures made no provision for evaluation of projects to separate viable from unviable projects, or those supporting national development goals from those that do not;

(c) AFA, because it offers tax holidays, supports those firms that can make profits from the outset, rather than providing necessary support to firms that otherwise might fail without FAP support.

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[11] However, care would need to be taken to avoid abuse of such a facility through potential "over invoicing" of such work.

5.44 As the Botswana economy grows, however, and investment increases, a case-by-case system becomes far more difficult to operate and to monitor. Hence, any system that provides for automatic and transparent procedures is preferable. It is instructive that, as of 1988, no AFA projects were known to have failed. This is due, in large part, to the tendency of more clearly profitable projects to seek AFA grants, while companies whose ultimate viability remained questionable would tend to seek CFA subsidies. Also, actual employment from AFA projects through 1991 amounted to 57 percent of the number of jobs projected, while CFA projects created only 41 percent of projected jobs.[12] A system providing its main benefits in the form of targeted tax incentives, while not immune to abuse, is nonetheless more secure than a program that pays direct cash grants. Such a system also avoids providing incentives to companies with a high likelihood of failure.

5.45 The following changes to the FAP program are consequently proposed. Government may, however, wish to wait until the forthcoming FAP evaluation is completed, and may use some of these recommendations in preparing the terms of reference for the evaluation.

(a) Elimination of the Capital Grant, Labor Grant, Sales Augmentation Grant, and Tax Holidays for medium- and large-scale enterprises. These programs will have to be phased out so that companies which invested in projects with the promise of certain benefits will not find these benefits abruptly revoked;

(b) To compensate for elimination of the Labor Grant, Government should consider eliminating the minimum wage or, alternatively, allowing inflation to erode the real value of the statutory minimum wage (if a minimum wage is to be retained, differing rates for different industries and job categories should be abolished);

(c) If some form of labor subsidy is still considered essential, the Government should consider replacing the Labor Grant with a tax credit for employment of semi-skilled and unskilled workers;

(d) In place of Tax Holidays, Government should institute the lowest possible rates of personal and corporate income tax consistent with the revenue requirements of Government;

(e) Establishment of a fund, possibly, under TIPA administration, to help companies identify and develop market opportunities through the retention of qualified consultants with knowledge of specific markets. Such a program should require payment of a portion of the cost of such studies by the sponsoring company -- and care would need to be taken to avoid "over-invoicing" for such work;

(f) Government should encourage the development of venture capital facilities to help entrepreneurs whose projects are viable but who lack adequate capital;

(g) Retention of a modified Training Grant, the main features of which should be: (i) a 10-year program covering all existing and new medium- and large-scale enterprises, subject

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[12] MFDP, Financial Assistance Policy Statistics, 1992.

to Government evaluation and possible renewal on expiry of the initial 10-year period; (ii) covering up to 75 percent of allowable training costs rather than 50 percent; (iii) extending coverage to citizen supervisory and management personnel; (iv) automatic approval of benefits, provided adequate substantiating evidence is provided; (v) coverage of defined on-site training activities. Grants should be given to support training that will contribute to improved efficiency;

(h) Retention of FAP benefits for small-scale enterprises. While the threshold on total fixed investment should be raised to include more enterprises, corresponding increases in the amount of FAP grants payable should be reviewed carefully;

(i) Extension of all remaining FAP benefits to the services sector;

(j) Elimination of regional and gender biases in FAP;

(k) Upgrading of the evaluation, monitoring, and audit functions. Companies in the medium- and large-scale sectors should be required to submit audited accounts and copies of income tax returns on a regular (quarterly, semi-annual, or annual) basis. A program of random audits of FAP recipients should be undertaken. Follow-up of FAP recipients for at least five years after the expiry of FAP benefits should be undertaken to ensure that reliable and accurate assessments of the program can be undertaken;

(l) Adoption, wherever possible, of automatic, as opposed to case-by-case, procedures for approval of FAP benefits.

5.46 The adoption of such a program, however, should be undertaken within the context of a better understanding of labor markets in Botswana and the likely developments in these segmented markets over the 1990s (as indicated earlier in this chapter). The above recommendations are, in part, premised on a continuation of conditions prevailing during the 1980s which saw unemployment rates decline and labor shortages develop in some areas, by the beginning of the 1990s. The future capacity of the economy to continue generating new employment opportunities at a rate of 10 percent per annum, as it has done over the past decade, is not known -- but does not seem likely. It is also unknown whether future growth in employment, even if it is below 10 percent per annum, will be sufficient to absorb a growing workforce and in-coming rural migrants so that unemployment rates do not increase significantly from their current levels. Should economic conditions deteriorate markedly such that employment growth falls to a significantly lower level or should rural migration accelerate, bringing large numbers of unskilled laborers to the urban areas in search of employment, then the Government may wish to continue with a more targeted incentive system based upon generating employment in labor intensive manufacturing industry. To assist policy makers make more informed decisions in this regard, the quality and timeliness of labor market data will need to improve (employment, unemployment, productivity, and wages data -- in all segments of the labor market, formal and informal), and policy decisions should be made on the basis of a better understanding of the dynamics of labor market relationships for both the present and the future. Final decisions on the future of FAP should be made in the light of the above issues relating to the labor market and within the context of the FAP review scheduled for 1993.

5.47 A descriptive section on FAP is included as Annex 2 to this report and a statistical data base on FAP is included as Annex 3.

5.48 ***Selebi-Phikwe Regional Development Project.*** In spite of its appeal to investors, an assessment of the Selebi-Phikwe Regional Development Project (SPRDP) should address the extent to which Government should promote -- through subsidies or other means -- investment in specific regions of the country, and the extent to which such efforts are likely to succeed. There is little question that, without the promotional activities of SPRDP few, if any, of the companies establishing projects in Selebi-Phikwe would have done so. Apart from the benefits resulting from a well-conceived and executed promotional strategy it is difficult to attribute investment in Selebi-Phikwe to any incentives uniquely available there. Seven of the eight companies that set up factories in Selebi-Phikwe with the assistance of SPRDP did so before the Special Incentive Package (SIP) was enacted. As table 5.3 shows, of 56 companies visiting Selebi-Phikwe since the project's inception, 42 of them were from South Africa, Zimbabwe, and Botswana. Of the six companies that have so far received SPRDP assistance, five of them have been established by investors with strong connections to Zimbabwe, and have been oriented towards the Zimbabwe, South Africa, and Botswana markets, as has been the case for most industrial companies established in Selebi-Phikwe before the SPRDP was established. Only one company receiving SPRDP assistance is a large, labor-intensive manufacturing company oriented toward markets outside Southern Africa. The difficulties this company has experienced, and its subsequent reorientation to the South African market, indicate that the natural focus of manufacturing companies in Selebi-Phikwe and, possibly, in Botswana as a whole, is the regional rather than the world market. Since the SIP for Selebi-Phikwe specifically excludes exports to Southern African countries from the major tax benefits, this experience calls into question the orientation of the SIP towards extra-regional exports, as well as its overall ability to attract investment.

5.49 SPRDP has had to begin by educating potential foreign investors about Botswana before highlighting Selebi-Phikwe's unique advantages. As a result, SPRDP has had an impact on foreign investment in Botswana as a whole. Although precise figures are unavailable, some companies initially attracted by SPRDP have ultimately invested in other parts of Botswana. The apparent success of SPRDP in promoting investment in Botswana as a whole as well as in Selebi-Phikwe suggests that many organizational and operational features of SPRDP may be appropriate as a model for a national investment promotion strategy.

Table 5.3: Origins of Prospective Investors Visiting Selebi-Phikwe

Country of Origin	Number of Visitors
South Africa	18
Zimbabwe	14
Botswana	10
Hong/Kong	6
Other	7

Source: Ministry of Finance and Development Planning.

5.50 This apparent success also indicates that, as generous as the Special Incentive Package for Selebi-Phikwe may be (the only company currently benefiting from the SIP, with employment of 550 Batswana, expects to receive P12.3 million over a five-year period), it may not be sufficient to induce companies to invest in Selebi-Phikwe rather than in other regions where, although the financial incentives may be less generous, other factors are more advantageous. An evaluation of SPRDP conducted in 1992[13] concluded that for the large-scale export-oriented firms the SIP was designed to attract, "Selebi-Phikwe as a location has several disadvantages which provide a disincentive for investment there," and cited higher transport costs, distance from the seat of Government, lack of financial and commercial/industrial services, and general quality of life for expatriates as the most important factors. In a general critique of the SIP and FAP, the report states, "There is much more to attracting inward investment than the value of incentives; the success of Mauritius shows that rapid growth is possible without offering high levels of grants to incoming firms. The lesson of Mauritius is that the overall investment climate is much more important than the value of incentives."[14] This is as true for Botswana as a whole as it is for any regional set of incentives.

5.51 If the SIP and FAP programs are substantially eliminated, Selebi-Phikwe will have no special advantages. It does not necessarily follow, however, that further investment will go elsewhere in Botswana. The advantage to investors of having a facility such as the SPRDP, which not only tries to attract investors, but actively assists them through every stage of project implementation, is clear. Other attractions specific to Selebi-Phikwe include relatively lower costs, and greater availability of, such crucial inputs as land, construction services, and factory buildings, as well as greater proximity to Zimbabwe which, despite poor current market conditions, promises to be an important market for Botswana companies over the long term.

5.52 To the extent, therefore, that Government can influence companies' investment decisions with respect to location, it does so best by providing infrastructure in areas in which it wishes to encourage investment as well as by assisting or carrying out promotional campaigns geared towards investment in a particular region. Otherwise, it is not clear that Government can or should, by means of subsidies or other incentives, try to influence companies' locational decisions. To the extent that such incentives may succeed, they may also result in a distortion of investment decisions with consequences that Government may ultimately be called upon to mitigate.

5.53 Table 5.4 provides information on the employment created in the Selebi-Phikwe region under the SPRDP. Although the data are adversely impacted by the effects of the international recession in the latter year, the overall picture is one of only moderate employment growth. Since inception, the program has created just over 1,000 permanent jobs, which have been concentrated in three companies.

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[13] Maendeleo Development, *Review of the Selebi-Phikwe Regional Promotion Programme*, Draft Final Report, Ministry of Finance and Development Planning, August 1992.

[14] *ibid.*, par. 4.103.

Table 5.4: Investments and Job-Creation in Selebi-Phikwe to 1992

Company	1989	1990	1991	1992	Cumulative Total Jobs Created
Seemac	315	-	-	45	360
Foaroc	20	4	-	-24	-
Sportsline	-	850	-	-300	550
Marble Products	42	50	58	-	150
MDT	13	-	-	-13	-
Gantron	185	-	-	-185	-
Fashion Enterprises	150	-	-150	-	-
Barkati	-	53	-53	-	-
TOTAL	725	957	-145	-477	1,060

Source: Ministry of Finance and Development Planning.

5.54 ***Botswana Development Corporation (BDC).*** The Botswana Development Corporation Limited (BDC) has operated in Botswana with considerable autonomy. Perhaps because its Board of Directors includes representatives of the private sector and external funding agencies, BDC has not been subjected to, or has managed to avoid, pressures from Government to support particular projects. While BDC has been criticized for being too strict in its lending policies, it is almost universally praised for evaluating projects on sound economic and commercial, rather than political, grounds.

5.55 Criticisms have been levelled against BDC concerning its dominant position in the Botswana economy. Many of these criticisms are justified. As table 4.4 shows, the total BDC loan portfolio represents 6.6 per cent of commercial bank and non-bank credit. With the inclusion of BDC's equity investments, it represents 10.6 per cent of the total. This is a significant share of the economy, which may be exceeded by the influence BDC exerts on developments throughout the formal sector -- excluding the mining and beef industries. This is undoubtedly a consequence of BDC's central role in the development and diversification of industry in Botswana. When BDC was established Botswana had virtually no other industries apart from diamonds and beef. Subsequent diversification into other industries owes a great deal to BDC's effectiveness as a catalyst as well as to the financial resources at its disposal. With no tradition of trading or other entrepreneurial activity, Botswana's industrial development would have been much more difficult to achieve without the presence of BDC. Nonetheless, what was an inevitable dominance of the industrial sector by BDC in the early years of industrial development is no longer necessary or desirable.

5.56 It is also alleged that BDC seeks excessive control and that it tries to protect its investments by withholding support from new enterprises that might offer competition. There are many cases, however, in which BDC has supported new investments in industries in which it has already invested through other companies. Indeed, BDC risks being criticized for blocking new investment if it fails to support a company that might compete with an existing BDC investment but might, on the other hand, be criticized for seeking to establish a monopoly should it support several companies in the same industry. Still, irrespective of their merit, many of these perceptions persist, with the consequence that BDC might be in danger of being penalized for its success.

5.57 Many Batswana are sensitive to foreign dominance of Botswana's economy. BDC, however, has made it possible to avoid 100 per cent foreign ownership of the industrial sector, first by serving as a proxy for direct participation by individual citizens and, second, by creating the vehicles for wider citizen stock ownership through the Sechaba Investment Trust and Stockbrokers Botswana. BDC was also instrumental in broadening the share ownership in Financial Services Company and Botswana Insurance Holdings, and in successfully listing shares of both companies on the Botswana share market.

5.58 BDC justifies its retention of controlling shares in profitable enterprises by arguing that these companies generate the cash flow that it requires to lend or invest in new projects. BDC argues that divestment of profitable enterprises would reduce its funds available for loans or investment and would increase its dependence on direct equity and loan contributions, thereby reducing its operational autonomy. However, BDC has always had substantial autonomy even though when it was established it was almost entirely dependent on Government funds. In addition, there is no evidence that in divesting itself of profitable holdings BDC would become more highly dependent on Government funds. BDC ought to be able to obtain a price for its holdings that reflects the value of expected future income they would generate. It is true that, given the relatively small size of the Botswana share market, divestment of some of BDC's large holdings would need to be undertaken gradually, so as not to disrupt the market.

5.59 The charge that BDC is too strict in its lending and investment policies is only partly justified. Current policies are largely a correction of earlier laxity which resulted in considerable losses from failed companies. Furthermore, given that in 1990/91, BDC showed an income statement loss provision in excess of P11 million, it could be argued that its investment and lending policies should be more strict rather than more lenient.

5.60 BDC's requirement that project promoters contribute at least 25 per cent of total project cost, as a means of ensuring a genuine commitment, sometimes presents problems for projects that are viable, but for which the promoter does not have adequate funds to invest. This is especially true for projects where a company must build its own factory shell because those available do not meet its requirements. This raises the overall capital cost and increases the contribution required from the promoter. Conversely, in projects where the fixed investment is low but working capital requirements are high, a company may find it impossible to provide the collateral required by BDC. Although ensuring a high level of investor contribution is obviously important to ensure a commitment by the investor to the proposed project, it is also necessary to maintain a flexible approach to this basically sound requirement.

5.61 Also at issue is BDC's role in providing serviced land and industrial buildings. There is evidence of a lack of understanding on the part of BDC as to what the market wants. BDC strategy has been to buy and develop serviced land, erect industrial units and lease them to clients. As, in most

cases, factory shells are built long before tenants are identified, it is inevitable that they do not always meet all individual tenant requirements.[15] Many investors would prefer to buy and develop land and factory space to their own specifications and are convinced that this would be less costly in the long run than renting from BDC. Since BDC's industrial property developments have been financially disappointing, and are not liked by industrial investors, BDC should gradually withdraw from this market and release land owned by, or reserved for, BDC onto the open market. This may, however, require reform in land allocation policies to allow non-citizen private companies to obtain land on which they can then develop industrial buildings and estates.

5.62 Criticism, even though some of it is unjustified, can ultimately result in political pressures to change BDC. In the interest of avoiding such an outcome, and in response to the inevitable and desirable changes in BDC's role that will accompany the maturation of Botswana's economy, BDC should:

(a) Continue and accelerate the spin-off of BDC-owned companies into Sechaba Investment Trust (SIT), through direct sale of shares, or by public issues. Although the price BDC receives should reflect the expected future income stream from the companies involved, such divestments should nonetheless be carefully planned in consideration of the likely market response. It is noted that during 1992, BDC investments in four companies are in various stages of being spun off, and that certain investment holdings continue to be reduced through sale of shares;

(b) Pursue its current 1990-1995 Strategic Plan goal of equity and loan investments in the order of 35 to 65 per cent. Equity investment in new projects should be limited to 49 per cent and reduced as quickly as continued project viability will allow. BDC's goal should be to retain no more than 30 per cent of the equity in any subsidiary or affiliate company, and to divest itself of all holdings in companies that can achieve adequate capitalization without BDC participation;

(c) Explore means of improving flexibility in reducing equity contribution and collateral requirements, given the basic requirements of project viability and significant sponsor involvement. Reduction of collateral requirements and the practice of lending against a company's expected future cash flow (a common practice in many countries) may require more rigorous project assessment practices, which BDC should undertake to develop.

5.63 *Duty Drawback System*. Botswana, like most countries, provides a mechanism by which exporters can be exempted from, or refunded, the import duties they pay on raw materials for goods ultimately exported. Botswana uses a *duty drawback system* in combination with *bonded warehouses*. Most exporters establish a bonded warehouse on their premises. Raw materials are imported under bond and placed in the warehouse. When materials are removed from the warehouse and placed in production, the company pays the appropriate duty. When the finished goods are subsequently exported, the company applies to the Customs Department for reimbursement of the duties. Companies without a bonded warehouse on their premises simply pay the duty when the goods are imported and apply for the drawback upon export. This system appears to work fairly smoothly, with the drawback refund normally

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[15] BDC will build, and has built, to uaer's specifications, where these can be ascertained.

paid within two to three months of application. It might be possible to shorten this period significantly.

5.64 Duty exemptions may not be feasible in Botswana, since they may violate terms of the SACU agreement. It will require considerable study before Botswana can determine whether it should designate EPZs and if so, where. Another alternative might be a bonded warehouse system, which has been used in other countries. A study in the Philippines concluded that bonded warehouses involved an average cost of only 1.74 per cent of the import value. Under this scheme, the company imports its raw materials in bond. For those goods it exports, no duties are paid. For those goods released into the local (or SACU) market, import duties are paid at the time of shipment. This reduces the cost to the exporter and also reduces the cost to Government of administering the scheme. Given the advantages to exporters, and the potential for attracting additional investors, bonded warehouse facilities can be made available to eligible industrialists producing for export.

5.65 *Local Preference Scheme*. As indicated elsewhere in this report, a local preference scheme was introduced in 1976 to give local producers preference in the supply of goods for Government contracts. Contracts are awarded to local producers as long as the contract price is within a fixed premium of the lowest foreign bid. This scheme was modified in 1986 and the preference changed from being based on sales (with a preference of 12.5 percent) to local value added (with a preference of 40 percent). This scheme was introduced to support the development of citizen activity in commercial, manufacturing and construction activities. Unfortunately a detailed analysis of the effectiveness of the local preference scheme was not undertaken within the context of this report and it may well be useful to commission an independent study to review how successful the scheme has been in achieving its objectives.

5.66 However, certain observations are possible on the impact of the scheme. Firstly, providing local preference (even based upon local value added) means that these goods are likely to be produced less efficiently and at a higher price. On the other hand, the introduction of the scheme was an implicit recognition of the higher cost of local production and was an attempt to address this problem. In addition, the preference is based upon local value added, and is therefore relatively limited given the need to import much of the raw materials required for industrial production. The shift from a sales based preference to one based upon local value added has reduced the distortionary effect of the scheme. It may therefore be a cost worth bearing to assist the development of indigenous entrepreneurs. A possible modification to the scheme may well be to gradually reduce the level of preference provided on local value added by a set percent each year. However, the adoption of such a policy would necessarily have to be based upon a detailed examination of the impact of the scheme to date.

E. INVESTMENT PROMOTION POLICIES IN THE REGION

5.67 Investment incentives for the private sector in Sub-Saharan Africa play an important role in the region's industrialization programs. In most cases incentives offer a form of compensation for the disadvantages that investors perceive to exist in particular locations: tax concessions in high tax countries; export earning retention facilities where there are foreign exchange restrictions; protection through trade and industrial licensing policies in small, low purchasing-power markets; credit and equity participation through development finance institutions; and concessionary interest rates to compensate for high cost and shortages of capital. Initially investment codes were mainly oriented towards large scale foreign enterprises -- subsequently benefits were made available to domestic, especially small scale,

enterprises. The incentive structures favored capital-intensive investments while the high wage structure, rigid labor laws and political pressure to expand employment, discouraged labor-intensive techniques[16].

5.68 Botswana's incentive system, operating as it does in a relatively distortion-free environment, has been clearly targeted to encourage particular investments. The experience of investment promotion policies in neighboring countries is less relevant to Botswana's circumstances as their incentives reflect an overriding need to boost foreign exchange earnings -- almost at any cost. In Lesotho, Mozambique, Namibia, Swaziland, Zambia and Zimbabwe, incentives concentrate on export industries. Tax reductions and lengthy tax holidays (costly in terms of revenue foregone), import duty exemptions, foreign exchange retention schemes, subsidized land and labor, and credit at concessionary interest rates are all offered. Among these the only item which would materially improve the existing investment environment in Botswana relates to land. Even then there is no need for subsidized industrial space as access to a free market for land would be sufficient.

5.69 Mauritius is the one country in the region which resembles Botswana in terms of population size and an open and growing economy -- where the experience of incentives offers relevant lessons. Mauritius succeeded in attracting a large number of textile and garment manufacturers with its Export Processing Zone (EPZ) incentives. It has become a major tourism destination for the affluent long haul market. Recently, legislation was introduced to attract offshore banking and other foreign exchange earning services. The response to the latter has been slow, partly because of the perceived obstacle of rigid central bank controls. There appears to be a good case for Botswana to look at the Mauritian system with a view to adopting certain key elements of the island's incentives. For example, export industries in Botswana would benefit if corporate tax reductions were expanded from Selebi-Phikwe to the entire country. Tax concessions for offshore financial and other services, accompanied by the necessary changes in foreign exchange control and banking regulations, would also give Botswana a head start in the international services sector.[17]

5.70 Finally, incentives for private investment in the tourism sector, and an enabling administrative framework, could form the basis for expansion in an industry which has a big employment multiplier effect in rural areas. Tourism is also known to be an important channel for attracting industrial investment, as demonstrated by such diverse countries as Mauritius, Barbados, the Bahamas, Madeira and Malta. Certainly, increasing Botswana-awareness abroad will be achieved faster and on a wider scale by attracting more tourists than by TIPA promotion activities. Whatever new incentives are adopted, if Botswana does not resolve the major bottlenecks of land shortages and immigration and other regulatory restrictions, it will not be able to hold its own in the region in competing for foreign investment.

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[16] World Bank Technical Paper No 25, *Industrialization in Sub-Saharan Africa.*

[17] Whereas Mauritius has been less than successful in developing off-shore banking and foreign exchange services, this has been partly occasioned by its slowness to eliminate controls on these activities. In addition, Botswana is likely to have a higher chance of success in such activities as a result of its proximity to RSA and its ability to therefore act as a conduit for investment into and out of that country.

F. FINANCING INDUSTRIAL DEVELOPMENT

5.71 The credit environment in Botswana is far more favorable to investors than it is in most of Sub-Saharan Africa. The banks are highly liquid, interest rates are negative in real terms, there has been no crowding out by the public sector[18] and the provisions for foreign companies borrowing in Botswana are liberal. Nevertheless, the commercial banking sector has made only a minor contribution to financing industrial development, mainly in the form of short term working capital. At end-November 1991 outstanding commercial bank credit to manufacturing industries accounted for 12 per cent of total commercial bank credit and amounted to P127 million.[19] This compares with a share of 8 per cent and a total credit value of P23 million five years earlier. BDC commitments to industrial enterprises at end-May 1991 amounted to P60 million -- 30 per cent of its investment portfolio. Currently, investment in the manufacturing sector amounts to about P150 million a year (P124 million in 1989/90)[20]. Assuming that commercial bank credit finances P50 million (similar to the 1991 year-on-year increases in loans to industry) and BDC expands its own lending to the sector by a planned P5 million a year[21], up to P100 million, or two thirds of the total, would be left for financing by own funds, reinvested profits and foreign capital.

5.72 Long term lending by the commercial banks, particularly for large scale industrial projects, has grown very little, for several reasons. One is that the commercial banks are inhibited by the short term maturity structure of their deposits. At end-November 1991, 86 per cent of deposits had a maturity of less than 30 days. Deposits for 12 months or more accounted for less than 4 per cent of the total -- down from 5 per cent four years earlier. There is hope that recent interest rate adjustments will eventually increase longer term deposits. The banks' relatively small capital base is another reason why large industrial loans are difficult, as exposure to any one borrower may not exceed 25 per cent of bank capital. Since the commercial banks' combined capital at end-1991 was only P153 million they could support combined loans to any one entity to a maximum of P38 million. This compares with loans outstanding from the Government's PDSF/RSF lending programs of P91 million and P45 million to the power and water corporations, respectively[22]. Finally, there is a lack of expertise among the banks in the assessment of long term risks, while prudent banking practices inevitably involve a certain risk aversion.

5.73 *Foreign capital* is a key factor in the development of Botswana's industrial sector. The favorable investment climate and unobtrusive foreign exchange controls attracted foreign investors, initially into the mining sector, and subsequently into a wide range of manufacturing enterprises. Net annual inflows of private direct investment have risen rapidly, from US$6 million in 1970, to US$59

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[18] The crowding out that has taken place has been the Government, through its own lending program to the parastatals, crowding out the banks from lending to these institutions, as the Government lending funds have been on more attractive terms than commercial bank lending.

[19] Bank of Botswana Review, Vol 6, No 11, Table 1.10.

[20] Ministry of Commerce and Industry.

[21] BDC Five-Year Strategic Plan, p49, and May 1991 Income Statement.

[22] NDP 7, Table 6.3.

million in 1985 and US$129 million in 1989. The net foreign private capital inflow into Botswana in 1989 was five times larger than the comparable total for Mauritius[23]. Preliminary estimates for 1990 indicate further growth, to some US$200 million in net private long term capital receipts[24]. Even if manufacturing accounted for only one tenth of this net inflow it would contribute P40 million to the estimated P100 million current annual level of industrial investment not met by domestic financial institutions.

5.74 Diversification of the financial sector is one of the Government's priorities for the NDP7 period, among which broadening and strengthening the operations of *the stock exchange* features prominently. In early 1992, ten companies were registered on the Botswana Share Market (BSM). The volume of shares traded has grown rapidly, while the index rose even faster. Total market capitalization in June 1991 reached P460 million, two and a half times more than at the start of operations in June 1989. About two thirds of trading business has come from institutional investors. Foreign investors, again mainly institutional, account for some 15 per cent of BSM turnover. Further listings are essential to diversify the range of stocks available. The 1991/92 budget introduced tax incentives to encourage companies to go public and offer their shares for quotation on the BSM. The 1992/93 Budget Speech also mentioned BDC efforts to make more shares available to the public by divesting itself of more of its holdings to the Sechaba Investment Trust. Sechaba is a quoted company in which BDC has a direct holding and management role. Given the upbeat performance of the BSM and the high level of liquidity, there is scope for larger domestic companies and foreign companies' local subsidiaries to be listed on the stock exchange. BDC has played an important role in building up and diversifying Botswana's financial sector by its backing of the BSM, by underwriting the creation of the first brokerage house, Stockbrokers Botswana Ltd, and by establishing the Financial Services Company (FSC), which includes factoring and invoice discounting among services offered. FSC, in turn, has a holding in French Bank Corporate Finance (Botswana) Ltd – a corporate finance and merchant banking company which contributes to the diversification of Botswana's financial intermediation services.

5.75 *Small and Medium Scale Enterprises* (SMEs). Although commercial bank lending to industrial SMEs is relatively insignificant, there is evidence that this may be a demand problem rather than one of credit availability. In 1990, a BOCCIM survey of SMEs[25] showed that 90 per cent of the respondents had been provided credit in the preceding two years; 70 per cent of the credit came from commercial banks; and the average loan amounted to P92,000. The loans were mainly for working capital and the purchase of vehicles. The implication is that commercial banks will provide credit to SMEs, if there is an acceptable business plan and the application is for a short term loan. Longer term finance available to SMEs is mainly provided by Tswelelo and NDB. However, faced with financial difficulties, NDB is unlikely to make a significant contribution to SME financing needs in the near future.

5.76 Tswelelo's role is to provide a comprehensive range of financial and non-financial services to small citizen-owned enterprises which do not have access to commercial bank credit. After early losses, Tswelelo now has a portfolio which is well above average for SME credit facilities in Africa.

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[23] World Development Bank Report 1991, Table 15.

[24] Bank of Botswana Bulletin, Vol 9, No 2, Table 4.4.

[25] SMEs defined as owning assets of less than P250,000 - excluding land and buildings.

Loans to manufacturing enterprises account for about 20 per cent of total loans outstanding, but for only 8 per cent of arrears. Two thirds of the loans were for P25,000 or less. After financial restructuring in the context of a five-year development plan, Tswelelo is favorably placed to expand its support activities to SMEs.

5.77 The FAP case by case scheme, as it applies to SMEs, offers capital grants for the creation of jobs and the acquisition of fixed assets, the latter payable before a project is started. To qualify as a small scale project the entrepreneur must be a citizen and the capital investment may not exceed P25,000. A medium scale project would have a fixed capital investment of between P25,000 and P900,000 and FAP assistance would be granted to both citizen and foreign investors. The 1988 FAP evaluation indicated that potential grant recipients are inclined to make over-optimistic projections and the project failure rate is high. Inadequate auditing, monitoring and supervision of projects have also caused problems for the implementation of the FAP program. As indicated above, if the program is to be expanded to include a higher limit, then substantially more rigorous evaluation, monitoring and supervision will be crucial.

G. CONCLUSIONS AND RECOMMENDATIONS

5.78 The existing investment promotion policy framework encourages a form of industrial development that is private sector-led and relatively free of distortions. Investment is relatively unbiased in terms of ownership, capital or labor intensity, domestic or foreign market orientation. Botswana offers important attractions to long-term investors in the form of access to factors of production, including serviced land, local capital and foreign exchange. Problems do exist, however, in the form of low labor productivity, difficulties encountered in securing land and housing and in cutting through the barriers of immigration, residence permit and licensing regulations -- and these loom large in an environment that is otherwise favorable to industrial investment. Incentives, particularly FAP, are designed to encourage citizen entrepreneurship, labor intensive production and export industries, by giving them a financial advantage over other types of investments for a limited period of time. However, there is some doubt about the efficiency of this scheme, and its economic benefit/cost ratio -- although this will need to be evaluated more rigorously in the context of the third FAP review scheduled for 1993.

5.79 As industrial policy will continue to be driven, at least in part, by employment concerns, it is recommended that data and information related to labor markets should be collected on a more regular basis and in a more timely fashion. In addition, the capacity to analyze changing conditions and dynamics within the labor market and different segments of the labor market should be developed. A better understanding of the impact of lower economic growth, faster rural-urban migration, quicker skills development, and so on, will be important in making policy prescriptions relating to industrial incentive schemes as well as policies on wages, employment and productivity. In the absence of more solid data and analysis on labor markets, the following recommendations are premised on a continuing ability of the economy to absorb the new entrants into the workforce, as well as additional rural-urban migrants, without adversely impacting on unemployment to any large degree.

5.80 It is important that the amendments proposed to the Employment Act (1982), Trade Disputes Act (1982) and Trade Union's and Employers' Organizations Act (1983), currently before Parliament, be approved and brought into effect as quickly as possible so as to provide an adequate collective bargaining machinery for employees and employers. In addition, the plan to establish an

industrial court to arbitrate on labor related grievances and disputes should be carried through to completion as rapidly as possible.

5.81 Industrial development will be greatly assisted by an on-going dialogue between Government and the private sector. This should be relatively easy in a country as small as Botswana. The initiation of the Francistown seminars by BOCCIM has been an important step in this direction. However, the Government should take a more pro-active stance in ensuring that lines of communication between the public and private sectors are maintained. Specifically, any outstanding recommendations made at the Francistown seminars should be analyzed by the Government, and if appropriate, pursued as a matter of urgency.

5.82 Foreign investment will remain an important source of investment in Botswana for the financial and technical resources which it delivers. Government policies will need to continue recognizing the importance of this source of capital investment. Nonetheless, domestic financial resources will also become increasingly more important. The recent development of the stock market is an important step in this direction and recent moves to encourage companies to go public are to be applauded. Equally important will be the ability of the banking system to mobilize resources from the household sector, an ability which will be crucially linked to the rate of return on this form of saving. Hence, the move to increase deposit rates to make them positive in real terms should be accelerated.

5.83 As the generation of high numbers of low-skilled jobs does not appear to be the pressing problem that it has been in the past, it is recommended that the FAP capital grant, labor grant, sales augmentation grant and tax holiday be eliminated for automatic financial assistance and case-by-case financial assistance. These schemes permit potential abuse and fraud, do not necessarily lead to increases in labor productivity within the scheme's time frame, and may well lead to the development of uncompetitive companies after the expiration of the benefits package. It is also questionable whether FAP should be trying to promote medium and large scale investments in rural areas, and whether FAP should have a labor intensive bias. The development of an efficient industrial sector with a potential for long term viability will be enhanced by encouraging industries to establish themselves in the most economically attractive locations, uninfluenced by subsidized distortions.

5.84 To compensate for the elimination of the labor grant, the Government should eliminate the minimum wage or seek to erode its real value at a faster rate to bring wages and productivity more into line with other countries competing for foreign investment. This issue is discussed in greater detail in chapter 6. If some form of labor subsidy is considered necessary, it would be preferable to replace the labor grant with a tax credit for employment of semi-skilled and unskilled workers.

5.85 Low general rates of corporate tax for all corporations operating in Botswana (also discussed in greater detail in chapter 6) should replace existing tax holidays and case-by-case tax arrangements. This should form the main component of the Government's industrial incentive program, to replace the Financial Assistance Policy.

5.86 FAP benefits should only remain for small scale enterprises -- the definition of which should be adjusted upward, possibly to include all companies with total fixed investment of a level up to P100,000 (and periodically revised in light of inflationary trends). Although there is no particular rationale for a cut off level of P100,000, it should be increased to at least the inflation adjusted level of P60,000 -- and possibly slightly higher if medium-scale FAP assistance is no longer to be provided. The

actual level could, however, be analyzed in greater detail in the context of the 1993 FAP Review. Given the high failure rate on small scale FAP projects, evaluation, monitoring and follow up work would need to be substantially enhanced within the Government -- possibly by diverting personnel previously involved on medium- and large-scale FAP projects. FAP benefits should also accrue to the small scale service sector.

5.87 The FAP training grant should be retained, but substantially modified to support training that will contribute to improved efficiency. Given the obvious need to improve skill levels in Botswana, it is recommended that the grant should be extended to all enterprises (including services) and should cover up to 75 percent of allowable training costs. Given the importance of management supervision in increasing labor productivity, the training grants should be extended to cover the training of citizen supervisory and management personnel. As much as possible, training grants should be provided on an automatic basis and, where possible, should also be extended to cover defined on-site training activities. However, as training subsidies can also be wasteful, it will be important for the Government to carefully monitor these to ensure that they are cost effective in terms of increased worker productivity.

5.88 In addition, the Government should: (a) establish a fund, possibly under TIPA administration, to help companies identify and development market opportunities; (b) encourage the development of venture capital facilities; (c) and eliminate regional and gender biases in FAP.

5.89 Many of the promotional features of the Selebi-Phikwe Regional Development Project should be extended to the entire Botswana economy to provide a "national investment promotion strategy". These benefits should apply country-wide and be provided in perpetuity.

5.90 With respect to the Botswana Development Corporation, it is recommended that it should: (a) accelerate the spin-off of its companies either into the Sechaba Investment Trust, through direct sales of shares by Stockbrokers Botswana, or by public issues; (b) it should pursue its strategic plan goal of equity and loan investments in the order of 35 to 65 percent; equity investments in new projects should be limited to 49 percent and reduced as quickly as possible thereafter; (c) explore ways of improving flexibility in reducing equity contribution and collateral requirements, given the basic requirements of project viability and significant sponsor involvement.

5.91 Given the advantages to exporters, and the potential for attracting additional investors, a bonded warehouse scheme should be permitted for any company which may request such services. Under such an arrangement, duty is only payable on those inputs which are placed in bond and subsequently used in the production of goods sold in the local (SACU) market. Duties would become payable at the time of shipment of the finished good.

5.92 During this period of financial difficulty for the National Development Bank, Tswelelo should be developed as the chief source of financing for the small and medium scale sector. Tswelelo's past track record has improved considerably and further efforts should be made to bolster its strengthened position. Over time, after the restructuring of the NDB, further support from this source may be forthcoming. Nonetheless, financial support for SMEs in Botswana has been reasonably good within a wider African context.

CHAPTER 6

THE ENABLING ENVIRONMENT

6.1 Rapid growth in Botswana during the 1980s has been supported by sound macroeconomic policies. As NDP 7 pursues most of the objectives in NDP 6, there will be only minor changes in macroeconomic and sector policies in the 1990s. These changes will come as a result of changes in the international and regional environment that promote competition and reduce confrontation and protection (see chapter 3). Other policy changes will result from the new level of development and sophistication of the Botswana economy and the need to address some of the more pressing constraints in some sectors.

6.2 During NDP 7, the Government will adopt more efficient methods of intervention into certain sensitive areas such as foreign ownership, the control of land and the use of foreign labor. A major problem in some areas is the continued use of a case-by-case regulatory approach to investment, land, and expatriate workers. This approach is inefficient, highly discretionary, and rarely subject to transparent criteria of approval. It also constrains the capacity of the Government to achieve stated objectives, overloading official systems and diverting the attention of administrators from areas where regulatory functions are needed. The main function of the system is to provide guidance and exert control. The guidance function has always played a minor role in Botswana as the Government has used market mechanisms to guide private sector activities. In a new environment, the control function will need to be modified to adjust to new circumstances and goals.

6.3 Increasingly, developing countries in Africa and Asia are moving to a system of management by exception, concentrating the efforts of the administration in sensitive areas and liberalizing in other areas. This approach utilizes concepts such as *the negative list* which enables streamlining of administrative procedures while freeing Government personnel to concentrate on more important activities. Thus industrial licensing can be streamlined through the introduction of negative lists. Activities that appear on the negative list would continue to need licenses and permits -- the others would only need to register for statistical purposes. Industrial activities on a negative list could include those that produce harmful products or bi-products, industries which are particularly polluting, or reserved activities. Some developing countries are opting for virtual abandonment of the industrial license (Malawi and Sri Lanka). The same concept can be useful to regulate the use of foreign workers. Certain skills and professions can be placed on a negative list and the rest granted automatic permits -- or alternatively, a small positive list can be devised for occupations within which expatriates would obtain virtually automatic permits (possibly engineers, doctors, accountants, and so on). With respect to land, agricultural, residential and commercial land could remain on a negative list barring it from direct allocation to foreigners. However, land for industry should be excluded from ownership limitations and cumbersome allocation and regulation procedures.

A. THE OVERALL MACROECONOMIC ENVIRONMENT

6.4 Over the NDP 7 period, there is expected to be a substantially reduced accumulation of external reserves as a result of slower growth of diamond export earnings combined with growing imports. In addition, Botswana may lose some of its competitiveness in regional markets as a result of internal inflationary pressures and depreciation of its regional market partners currencies (as is already occurring in Zimbabwe). To prevent domestic

inflationary pressures from undermining profitability and external competitiveness, there will be a continued need to emphasize prudent fiscal and monetary policies, as well as efforts to improve productivity and efficiency. It is important to ensure international competitiveness, so as to facilitate the diversification of the economy and promote foreign investment. A major issue has been, and will continue to be, the relationship between the exchange rate and industrial development. A healthy foreign exchange position has exerted an upward influence on the pula and has thereby helped to reduce inflationary pressures arising from imported inflation. On the other hand, a strong currency places competitive pressures on the development of manufacturing industries. Exchange rate policy in Botswana has always had to balance between these twin objectives of reducing the impact of imported inflation and encouraging industrial development. At the current time, and in line with the industrial policy objectives enunciated in NDP 7, the encouragement of industry has a more prominent focus in the minds of policy makers.

6.5 The introduction of positive real *interest rates* (for both deposits and lending) and the creation of a competitive environment in the local capital market, will further contribute toward the drive for improved efficiency and the creation of a competitive environment. Some of the more important policy changes will include increasing financial sector competition, re-evaluating DFI policies and operations, and encouraging banks to increase the availability of long term finance.

6.6 A slowing down in the growth of the diamond sector, in combination with expansionary budgetary policies, has contributed to a recent deterioration in the fiscal position of the Government. In these circumstances, improvements in *fiscal policy* should be considered, including: reform of both direct and indirect taxes (broadening the tax base, lowering rates, and introducing a VAT tax); attainment of full cost recovery in parastatal operations; and, gradual and selective parastatal privatization. The parastatal sector is the recipient of substantial resources through the development budget, soft loans through the Public Debt Service Fund (PDSF), and direct subsidies. In some cases this sector competes with the private sector -- most notably in services and real estate.

B. TAXATION POLICIES

6.7 Tax rates are not unduly out of line with the corporate tax rates of neighboring countries which are competing with Botswana for foreign direct investment -- although, as shown in table 6.1, Zambia, Tanzania, Kenya, Swaziland and Transkei all have lower corporate rates, and Lesotho has lower rates on manufacturing. As shown in table 6.2, corporate tax rates in foreign direct investment source countries are, for the main part, lower than in Botswana -- although not substantially so. However, as tax rates are one of the important determinants in an investor's decision to invest, Botswana may need to consider lowering rates to make them even more competitive than those of other countries competing for foreign investment.

6.8 In addition to low corporate tax rates, many countries offer extra income tax incentives to investors. These tax incentives can take two basic forms: either a low rate of corporate tax (and/or low rates of withholding tax on dividends) for certain sectors (farming, manufacturing, exports, and so on), or specific tax incentives in the form of tax holidays or other tax facilities (investment and capital allowances, research and development and training cost allowances). Botswana already offers some of these additional benefits. These incentives are currently being given on a discretionary case-by-case basis in Botswana, and include:

Table 6.1: Corporate Income Tax in Competing Countries for Foreign Direct Investment

	General (percent)	Special Rates
Zambia	35.0	Exports and Farming - 15 percent
Zimbabwe	42.5	
Malawi	40.0	
Tanzania	35.0	
Kenya	35.0	
Botswana	40.0	Farming - 0 percent
Swaziland	37.5	
Lesotho	45.0	Farming - 0%, Manufacturing - 15 percent
South Africa	48.0	Transkei - 35 percent
Namibia	42.0	

Source: Ernst and Young, 1992. The rate for Zambia is 1993/94.

Table 6.2: Corporate Income Tax in Source Countries for Foreign Direct Investment

	General (percent)	Special Rates
South Africa	48.0	Tax Agreement with Botswana
United Kingdom	35.0	Tax Agreement with Botswana
United States of America	34.0	
Germany	50.0	
France	34.0	
Japan	37.5	
Korea	34.0	
Taiwan	25.0	
Singapore	30.0	
Hong Kong	17.5	
Malaysia	35.0	
Indonesia	35.0	
Thailand	30.0	
Philippines	35.0	

Source: Ernst and Young, 1992.

(a) The Minister of Finance and Development Planning (MFDP) can grant far reaching tax incentives by the issue of a Development Approval Order (DAO)[1]. The Order specifies the types and rates of additional tax incentives for a specific project. The DAO has legal validity only after being approved by resolution of the National Assembly.

(b) The MFDP can create an individual tax regime for any person through a Tax Agreement. The tax agreement (created under Section 55 of the Income Tax Act), may vary the provisions of the Tax Act in any manner (creating, for example, a tax holiday) but must be ratified by an Act of Parliament. The Selebi-Phikwe Tax Agreement, covering tax concessions in this location, is a case in point. In addition, there are four other agreements with foreign investors -- all in mining activities.

(c) Parastatals are also granted special tax regimes. They are either exempted (Botswana Telecommunication Corporation and the development finance institutions) or have special tax arrangements (Botswana Development Corporation and the Botswana Meat Commission). The special tax regime for the BDC group of companies (all companies with BDC equity participation) involves a special allowance that permits losses from any of its member companies to be written off against profits of any other member of the group (within 6 years after the end of the tax year).

(d) The MFDP can exempt certain kinds of income from withholding tax on dividends and on technical assistance fees. These exemptions are given on a case-by-case basis to certain corporations and shareholders.

6.9 In addition to these tax incentives, under the Income Tax Act, the Financial Assistance Policy (FAP) provides for a tax holiday under the Automatic Financial Assistance (AFA) program. This incentive (reimbursements of business taxes) also involves project evaluation and project approval criteria.

6.10 All tax systems introduce elements of distortion. Nonetheless, an important element in designing an appropriate tax structure is to make it as efficient as possible and to reduce the amount of distortion which is introduced. Tax policy interventions are generally designed to strengthen or weaken: externalities -- such as research and development and training investments; risk and uncertainty -- such as the situation in the Southern African region; unemployment and inadequate growth; and imperfect competition. Specific tax incentives are used to provide lower rates on certain sectors, and to provide for investment and capital allowances. Tax holidays, although popular among investment promoters, are generally less desirable as their overall impact on investment decisions depends on issues such as: the existence of a tax treaty, with a tax sharing clause, with the investor's home country; the availability of allowances and carry forward provisions; the size of the depreciable assets of the beneficiary firm; the expected flow of income in the first years of operation; and so on.

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[1] Section 53 of the Fourth Schedule of the Income Tax Act. Only four Orders have been issued up to 1990.

6.11 The revenue structure of Government in Botswana is dominated by receipts from the mining sector (see table 6.3). The impact of mineral revenue on total Government revenue is so large (54 percent of total revenue and grants) that it dwarfs the size of other revenue sources. Non-mineral income tax is only 8 percent of total revenue, and corporate income tax only 4 percent. The fiscal and taxation policies of NDP 7 are designed to mainly pursue NDP6's objectives. However, the current system is largely based on a case-by-case approach, which results in a non transparent system with questionable objectives and limited coordination with the objectives of the industrial development strategy. The recommendation of this report is that the current case-by-case approach to tax incentives should be replaced by a comprehensive, simple, and uniform system of incentives for growth. The change could either take the form of a comprehensive tax reform that would re-examine the direct and indirect tax systems and their management, or a more limited re-assessment of some of the current specific type income tax arrangements and the introduction of new alternative incentives. Whatever decision is taken in this regard, it is highly recommended that the current system be replaced by a more uniform and transparent system of incentives.

Table 6.3: Tax revenue by Type
(pula million)

	1980	1982	1984	1986	1988	1990
Mineral	101	99	376	845	1,507	2,005
Customs pool	102	114	156	192	293	478
Non-mineral income tax	38	58	87	121	165	290
Property	1	1	1	1	2	3
Motor vehicles	1	1	2	2	3	1
Business licenses	1	1	1	1	2	8
Sales tax	0	2	5	13	17	59
Other	0	3	1	2	0	0
Total tax revenue	244	279	629	1,177	1,989	2,844
Total revenue and grants	307	394	803	1,548	2,556	3,741

Source: External Trade Statistics, 1989. CSO, Government of Botswana, 1992, pp 44.

6.12 It is recommended that corporate and personal tax rates should be reduced to a substantially lower rate so that industries would be attracted by the low tax environment in Botswana. This measure would send a positive signal to investors in the Southern African region. It is understood that the tax authorities are currently considering reducing rates to 30 percent. It is estimated that such a move would lead to a reduction in Government revenue of approximately P60 million. A reduction of the tax rate to 30 percent would make investment in Botswana more attractive than investment in neighboring countries (see table 6.1). An even lower corporate tax rate would be more attractive, and it should be noted that several countries in the region have established tax rates as low as 15 percent for non-traditional exports and

manufacturing. It is recommended that any action on reducing tax rates should be implemented in conjunction with the elimination of the FAP incentive program to medium and large scale firms -- as outlined in chapter 5 -- which would represent a reduction in expenditure by the Government.

6.13 Although even lower uniform rates may be desirable, this may conflict with other Government fiscal objectives, especially in the current transition period from a surplus Government budget position to a deficit budget position. Consequently the Government may wish to consider alternative second best options. It is emphasized, however, that these truly are "second-best" solutions and go against the basic principle of a low uniform and transparent system of incentives for all -- as argued in other sections of this report. These include:

(a) a reduction in the corporate tax rate for manufacturing and/or non-traditional exports[2] to 15 percent -- resulting in a reduction in tax revenue of around P17 million[3] -- and the elimination of FAP and other special tax incentives.

(b) it would also be possible to combine a lower overall rate with the option enunciated above.

Table 6.4: Companies Tax Assessment for the Year 1990/91, by Sector Excluding Mining
(pula million)

Sector	Tax Due	Percent
Trading	108.1	72.5
Finance	7.7	5.2
Agriculture	0.4	0.3
Manufacturing	9.8	6.6
Construction	2.5	1.7
Transportation	2.2	1.5
Other services	17.9	12.1
All external companies	0.8	0.1
All Companies	149.4	100.0

Source: Department of Taxes reports.

[2] The reduced tax rate would be on the foreign currency income of non-traditional exports to outside the SACU market -- excluding diamonds, copper, nickel and products based on cattle farming.

[3] The revenue loss on manufacturing is estimated at 62 percent of the total tax due from manufacturing (see table 6.4). Total non-traditional exports, including tourism, to non-SACU markets, is estimated at P450 million (see table 6.5). If one assumes a profit margin of 10 percent on export value, total profit is approximately P45 million. The reduced tax rate from 40 percent to 15 percent will decrease tax revenue from P18 million to P6.75 million -- a revenue loss of just over P11 million.

6.14 The above estimates of revenue reduction, actually overestimate the net revenue effect to the Government as there will be a revenue gain from the elimination of the FAP and other tax incentives. The cost of the current tax incentives (DAO, tax agreements, and special tax incentives to certain investors) is not known except for the FAP tax holiday cost (the refund) which is about P1 million. In addition, Government expenditure would be reduced by the extent of the grants currently made to medium and large scale FAP projects -- which in 1991/92 were around P40 million (although these would also have to continue where existing commitments had been made). In addition, the introduction of the new reduced rates could be associated with the introduction of a value added tax (VAT) -- which would help to compensate for any net reduction in income tax revenue.

Table 6.5: Value of Major Exports
(Units of Account million)

	1987	1989
Diamonds	2,738	3,722
Copper, nickel matte	144	611
Meat and meat products	102	166
Hides and skins	9	21
Other goods	237	349
Total	3,231	4,870

Source: CSO, Government of Botswana.

C. POLICIES RELATING TO WAGES, PRODUCTIVITY AND EMPLOYMENT

6.15 Current ***minimum wage*** rates in manufacturing are considered, by some local and foreign investors, to be an inhibiting factor to further industrial development. This issue may increase in importance with increased competition in both the domestic market (reduced protection in SACU) and the export market for labor intensive products. Although minimum wages in urban areas in South Africa are higher than in Botswana -- in some regions (including some of the homelands) the reported non unionized wages are about one half the Botswana rates. The rates in countries such as Malawi and Tanzania are even lower (about P80 to P100). Labor rates in South and Far East Asian countries are about the same as the Malawi rates. The current policy is to compensate for the high labor cost constraint on export oriented manufacturing by the provision of labor subsidies and other incentives under FAP. There, nonetheless, remains an urgent need to address the issue of the minimum wage, if the Government is to seriously address the issue of un-skilled employment.

6.16 As discussed in chapter 5, the *FAP Labor Grant* is intended to compensate manufacturers for the low productivity of Botswana workers for a five-year period, after which the workers are expected to have approached competitive levels of productivity. However, the time required to achieve regionally and/or internationally acceptable levels of productivity appears

to be longer than the time frame provided by the FAP assistance. Two solutions are possible. The first, to extend FAP labor grants for a longer period, is unjustified as there is no indication how long it might take for Botswana to increase its labor productivity to internationally competitive levels.

6.17 Other alternatives are for Government to either eliminate the minimum wage or to move aggressively to reduce its real level. Botswana's high wage rates and low levels of productivity are disincentives to investment. In the absence of a minimum wage, it is likely that wage rates would move closer to a market clearing level -- as they have done for rural workers and domestics where minimum wages do not apply. Such action could result in wages that are below the poverty datum line. If this did occur, the Government could chose to provide direct income support to top up the differential for employed persons. FAP, in fact, provides *de facto* income support for individuals fortunate enough to have a job. By eliminating FAP and the minimum wage, Government would remove a significant source of Botswana's competitive disadvantage, while removing the bias that exists in its income support policies in favor of people already employed.

6.18 The extent to which wages were flexible downwards will depend upon several factors. The lower the rate of unemployment, the more likely that wages will be sticky in a downward direction. Although unemployment is estimated to be relatively low by developing country standards (at around 14 percent in the 1991 Census), there is still a sufficient pool of unemployed workers which would serve to exert downward pressure on wages. In addition, in a highly segmented labor market, such as Botswana's the unemployed are likely to be unskilled laborers who would earn the minimum wage. In a high growth economy, individuals with even a rudimentary level of skills are likely to be in high demand, and at higher levels of education and training, there is an acute shortage of workers, necessitating the utilization of expatriate skills. Nonetheless, there will also be a certain trade-off between salary levels and alternative activities (including leisure) beyond which wages will not fall. Hence, although the extent to which wages would decline in the absence of a legislated minimum wage, is unknown, the continued existence of unemployed workers with low skill levels, argues for some amount of downward flexibility -- as do the lower wage rates paid to those occupational classifications which are currently not covered by the minimum wages legislation.

6.19 Given the inevitable political problems that would be associated with eliminating the minimum wage, the authorities may wish to pursue other "second-best" policies which would reduce real wage levels -- and thereby increase competitiveness -- while leaving the minimum wage in tact. One such option would be the collapse of the current minimum wage structure from a system of eight categories and four different minimum wage levels (see table 2.1), to a single true *minimum wage* at the lowest level determined by the above categories.[4] This could lead to a potential wage reduction from P1.03 per hour, paid to some categories of minimum wage earners, to 81 thebe -- a reduction of 21 percent. Another option could be to exclude wage earners in manufacturing industry from the minimum wage requirements -- in exactly the same manner that agricultural workers and domestic workers are currently excluded from coverage. As a precedent has already been set in this regard, extending this exclusion may be easier to

[4] This would mean using the current minimum wage of 81 thebe per hour -- payable to night watchmen -- as the basis for all minimum wages in Botswana. No other minimum wages would be defined.

achieve than eliminating the minimum wage entirely.[5] Last, the Government should be even more diligent in ensuring that the real value of minimum wages is eroded by cost of living increases -- so as to achieve more competitive salaries in the industrial sector.

6.20 ***Productivity***. Non-unionized wages in neighboring countries are reported to be substantially below the minimum wage in force in Botswana, and are certainly lower when weighted by relative productivity. However, minimum wages not only affect wage levels -- they also make it difficult for employers to relate remuneration to productivity. Piece rates are a common method used to relate workers' incomes directly to their productivity, but this method of payment is seldom used in Botswana. It is understood that the use of piece rates, that may result in some workers receiving less than the minimum wage, requires special dispensation from the Commissioner of Labor, and that even then the dispensation is limited to an initial training period.

6.21 While an artificially high wage structure is of obvious concern to foreign investors, and the development of the industrial sector, this cannot be examined in isolation from productivity. It would, therefore, be preferable to act on both wage levels and productivity to ensure a more appropriate alignment between the two. This will involve reducing the real level of wages while increasing productivity. Nonetheless, without ready access by employers to the piece rate mechanism, in situations where it is appropriate, a powerful tool for stimulating productivity is lacking. Hence it is recommended that, in addition to reducing the real level of wages, that the Government should encourage piece rates in appropriate settings by leaving the establishment of such rates to the collective bargaining process.

6.22 The Government's ***employment policy***[6] aims to increase employment opportunities for indigenous workers by both expanding total employment opportunities and replacing expatriates by qualified Batswana. The policy also aims to control the growth of self employed foreigners and foreign employers as part of an overall policy to encourage the growth of Batswana owned businesses. This latter system is regulated by the work and residence permit system for expatriates. Non-citizen employees and self employed non-citizens must apply for a work permit and a residence permit from the Ministry of Labor and Home Affairs -- the Government sector is no longer subject to the same requirements.

6.23 The shortage of skilled workers, however, can be felt at all levels of industry. Rapid growth in the economy and a lack of skills locally, has created an ongoing need for workers to be imported on a temporary basis to fill a range of skilled, technical and managerial vacancies, for which there are no suitable local candidates. Given the very high relocation costs, companies wish to minimize their use of expatriate workers. Provided that the Government monitors the overall levels of foreign workers it should be possible to simplify and speed up the granting of work and residence permits. A relatively open labor market will help to keep pay scales for skilled workers (and production costs) at levels comparable to those prevailing in South Africa, a major source of temporary immigrant skills.

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[5] The social arguments for maintaining minimum wages at a Government determined "living level" appear to be less relevant in a situation where other workers are already receiving lower salaries -- and somehow managing to survive -- and this is sanctioned by the Government.

[6] This discussion follows the findings of an ILO Report, *Strengthening the Labor Department and Enhancement of Training for Localization*, January 1987.

6.24 The processing of work permit applications involves four Government agencies: Labor, Immigration, Security and Commerce. The Training and Localization Unit of the Ministry of Labor is involved in the evaluation of applications. Its evaluation process involves ascertaining whether the vacancy had been properly advertised, that no *suitable* local candidates were available, that the expatriate candidate possesses *suitable* qualifications, and so on. The other Government agencies are responsible for ascertaining that the applicants will be involved in the activities appearing in their application, that their services are required according to sectoral plans, and that they have no criminal record or subversive intentions. Botswana employed about 7,000 non-citizens in 1990 -- 2,300 in the public service and 4,700 in the parastatal and private sector. A further 1,200 non-citizens were self employed or employers. Their share of total employment in the formal sector was 3.4 percent and 3.6 percent (6.7 percent in 1976) respectively of the total employment in the private and parastatal sectors. Self employed non-citizens were estimated to represent about 30 percent of self employed persons or employers in the urban sector, in 1985. Since then, the number of registered local businesses has increased from about 4,800 in 1985 to 11,500 in 1990. The number of self employed and employers that are non-citizens increased during this period by only 20 percent. It is therefore highly likely that the percent of businesses owned by local investors has increased dramatically over this period.

6.25 These attempts to manage the labor market reflect a policy dating from the early days of independence when Government was struggling with foreign domination in the market for skilled workers. However, higher education is predicted to expand rapidly in the 1990s and satisfy most of the demand, for certain skills, from local sources. Botswana's education planners are aiming to establish an education system that is flexible enough to adjust to changing demands, and to provide Batswana with an education which helps them to be adaptable within a changing world. These developments will make it more complicated to manage the labor market in the 1990s.

6.26 The current labor permit allocation and regulation system have also been criticized for their negative impact on efficiency and the flow of foreign investment. An investment climate study found that difficulties in obtaining work and residence permits were regarded by potential investors as one of the main obstacles to investment -- although some local observers saw this more a problem of perception than reality. However, even if this is a perception problem it may have a real negative impact if it discourages potential foreign investors. It is therefore advisable to move the current system toward a more targeted immigrant labor control system similar to those used in more developed countries.

D. LAND POLICIES

6.27 The ***land tenure system*** in Botswana is a sensitive issue -- involving deep traditional values. Current tribal and urban land systems -- embodying the right of every Motswana to the use of land -- are considered superior to land tenure systems in other countries which have created a class of landless, and therefore extremely poor, rural people. A related problem is the perception that non-citizens have dominated the urban property development boom in recent years. Meanwhile, in tribal areas there are difficulties in raising loans as land is communally, and not individually owned, and is therefore not transferable. In these cases, land cannot be used as collateral -- unless the land is changed to a common law lease. Past studies reveal that rural and urban Batswana feel strongly that land on which their homes are built should be owned by the family and by future generations of the family and there is strong feeling among

"traditionalists" on the Land Boards and in tribal authorities against any change in the land tenure system.

6.28 The land tenure system and the institutions which support it can have a strong influence on the pace and pattern of development -- especially in the manufacturing and service sectors. The movement of Batswana from a traditional rural society to a modern urban society will necessitate a re-evaluation of some of these old concepts. The modern urban Batswana have different ways of life and different needs. New activities emerge that require large tracks of land with well developed infrastructure. Traditionalists feel that the land tenure system requires close supervision by the country's leaders -- including ministers, tribal chiefs and land boards. However, this is creating a severe bottleneck with resulting scarcity in certain markets, increased land prices, hardship for urban dwellers, and inhibited investment in manufacturing and services which limit the growth of employment opportunities. Land for industrial and service activities is made artificially scarce in Botswana, its price is consequently very high (due to scarcity rents), and the procedures for obtaining plots is long and cumbersome.

6.29 Hence, the shortage of serviced industrial plots is one of the biggest constraints to further industrial development in Botswana. As land is maintained as an artificially scarce commodity, it is frequently not used but held for speculative purposes -- further impeding industrial development and driving up its price. Although the Government has embarked on the Accelerated Land Servicing Program, current indications of demand and supply suggest that this will not be sufficient to address the existing demands for industrial land. Land Board regulations also add an additional layer of regulation and bureaucracy to an already cumbersome process

6.30 To deal with this problem, it is recommended that land for industry should be dealt with completely separately from other types of land. The planning horizon for industrial land should be extended to more than the current 20 year period. Large industrial zones should be demarcated in all towns in all regions -- in urban as well as in rural areas -- and access should not be limited to local investors but open to all. To assist the planning process it is recommended that a Land for Industry Committee be established in the Department of Town and Regional Planning (DTRP) in the Ministry of Local Government, Lands and Housing. Alternatively, the Government could examine existing committees dealing with land issues and, if appropriate, modify one of these to deal with the issues outlined herein. The committee would be in charge of determining the long term demand for industrial land. The committee should be comprised of high level representatives from MFDP, DTRP, Department of Surveys, the Department of Local Government and Development (MLGLH), and the Department of Industrial Affairs (MCI). The land should be available on a long term lease of at least 50 years and the transfer of the lease would be automatic if it is to another user for industrial purposes. Local taxes and land fees should also be levied at a much higher rate on undeveloped industrial land so as to encourage development for industrial purposes rather than having it remain idle for purely speculative purposes.

6.31 The Government could also attach higher priorities within the Accelerated Land Service Program to the development of industrial land. The situation seems more acute in Gaborone where industrial land is in great shortage. Some of problems may be solved by encouraging the development of industrial parks in neighboring towns. To avoid competition from commercial users, industrial zones should be located more distant from the town center.

E. UTILITY PRICING POLICY

6.32 As noted in chapters 4 and 5, the *cost of utilities* (water, power, telecommunications and transportation) is very high in Botswana. All services are provided by parastatals with the exception of trucking. High costs are a result of a policy of full cost recovery, and cross-subsidization built into the rates to cover for low income consumers. These high prices are also affected by a number of other factors including: the efficiency of the production and distribution of the services (capital and operating costs), the rate of depreciation of capital equipment, and the "appropriate" rate of return established for the utility.

6.33 In addition, prices are affected by policy toward the importation of these services from neighboring countries. If Botswana developed a more pragmatic approach toward the use of low cost infrastructure services available from RSA and other neighboring countries it could enhance the competitiveness of all user sectors. By locking into electricity grids and water supplies from neighboring countries, rather than developing additional, high cost domestic facilities, it may be possible to keep some utility costs from rising faster than they otherwise would. There is, for example, a growing move within the SADC region to lock into neighboring countries electricity grids to take advantage of lower cost, and sometimes, more reliable sources of power.[7]

F. PROMOTING FOREIGN INVESTMENT

6.34 The decision of a foreign investor to invest in a certain country is mainly affected by strategic considerations and perceptions of risk and return. The main strategic considerations include access to markets, competitively priced natural resources, and the existence of a low cost production base for export. Access to markets includes the domestic market, regional markets, and markets with which the host country has preferential trade agreements. Perception of risk involves an assessment of the political risk in the country of location and risk in the destination market. Political risk can create push and pull effects which induce investors to move away from one country as a result of an uncertain future -- because of, for example, political unrest and economic sanctions -- to countries from which export markets can be more securely served.

6.35 Botswana's small domestic market offers limited opportunities to foreign investors and existing possibilities are likely to be gradually exploited, in the near future, probably by local interests with foreign technical partners or investors. In such cases, only minimal foreign investment promotion efforts will be required since projects will be small, due to small market size. Although some foreign investment promotion will be needed to help realize these opportunities, most of this will be project oriented and will be undertaken by the development finance institutions, and by the SME development institutions.

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[7] For example, between Zambia and Zimbabwe, between Zaire and neighboring countries, between South Africa and Lesotho, Mozambique and Swaziland. SADC is also undertaking a power interconnection study to investigate further how generated electricity in the region can be better utilized by the region as a whole.

6.36 The area for major foreign investment promotion effort is export oriented foreign direct investment -- including to the most important export destination, RSA. Research[8] has shown that promotion efforts can have an effect on foreign direct investment, particularly export-oriented investments. These findings can be explained by imperfect information and the influence of non rational elements -- such as perceptions and biases -- in the investment decision process. An analysis of foreign direct investment trends in developing countries that have conducted promotion has revealed a statistically significant relationship between promotion and the inflow of foreign investment. Promotion is a significant variable explaining such investment trends.

6.37 An investment promotion program has three main elements:

(a) a strategy -- the sectors, countries and investors to target and the investment promotion techniques that will be used;

(b) an institutional structure -- the structure and functions of the organization that will develop and carry out the strategy, and the place of the organization within the larger structure of Government;

(c) management -- the philosophy that motivates the investment promotion staff and measures their effectiveness.

6.38 Experience shows that the most successful investment promotion programs rigorously target the sectors and countries where they seek foreign investors. Sector targets, of course, have to be based on an analysis of sectors where the country has attractive investment opportunities as a result of its resource base, markets, location and other factors. Sector targets also have to take into account the propensities of foreign investors and capabilities of local investors. There are some sectors in which foreign investment is relatively rare. These and other sectors may be reserved for local investors. Sectoral targets for foreign investors, on the other hand, do not necessarily exclude foreign investment in other sectors.

6.39 Country targets will be linked to sector targets. The countries to be targeted should be those where there are investors interested in the targeted sectors -- investors looking for alternative investment sites or additional sources of supply. Country targets also may take into account special factors, such as trade agreements with the promoting country and historical or political ties. All of these factors can influence the propensity of investors to respond to promotional efforts.

6.40 Investment promotion generally must be targeted at specific countries because of limited resources. Botswana's promotion effort will have neither the budget nor the manpower to be active in investment generating efforts globally. Choosing appropriate country targets will be as important as selecting proper industry targets. Countries must be chosen where there is a strong chance of finding potential investors. To evaluate the group of investors that are the potential market for investment promotion efforts one must identify the potential export markets and the origin of the investors that would be attracted to Botswana to serve these markets. The major potential markets for export promotion efforts are identified as -- South Africa, Europe

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[8] *Marketing a Country*, Louis T. Wells Jr. and Alvin G. Wint, FIAS, IFC and MIGA. 1990.

(under Lomé) and the United States (under the GSP agreement). The major sources of investors are South Africa, the newly industrializing countries of Asia, Europe and the United States.

6.41 The interest of foreign investors in Botswana is affected by the political situation in RSA and the relationship between the two countries. In periods of instability in RSA there is growing interest in Botswana by RSA investors, and less interest by other investors -- except NIC investors who seem less affected by political circumstances.

6.42 *South Africa* is the dominant market in the region. With a high GDP, a well developed industrial sector, and political uncertainty, it is likely to provide an important pool of potential investors for Botswana. This should be Botswana's primary target market for foreign investment promotion. For most South African investors, Botswana is merely an extension of the larger RSA market. Their alternatives for production to serve the SACU market are RSA and the other members of the BLNS countries. South African investors are attracted to Botswana by its political stability, its less militant labor force, its more relaxed foreign exchange regime, and its preferential access to major world markets.

6.43 The concerns of the *Newly Industrialized Country* (NIC) investors must be evaluated in a different context. As production costs within Hong Kong, Taiwan and South Korea rise, their manufacturing communities are aggressively seeking lower-cost production sites and countries with trade preference agreements with their main world markets (the US and Europe). A need to maintain competitiveness is the major driving force in the appearance of NIC investors in the BLNS countries. Their production strategies center around clothing and footwear. In these products there are two distinct groups, high-end and low-end markets. The high-end products demand fine quality and quick turn-around and the share of labor costs in the product value is low. Thus, the European and US producers maintain domestic production for these products. However, for the lower-end products the US and European producers or marketers (under general label or private label) continue to establish direct sourcing arrangements in lower-cost areas throughout the world. NIC producers, who have long established relations with them, will continue to search for lower-cost production sites[9] to serve them. This trend does not necessarily cover only clothing and footwear but also other labor intensive products such as toys, giftware, some hand tools, some electronic products, and so on.

6.44 The last group of investing countries includes *Europe, the US and Japan*. Their prime motivation for locating in the BLNS is the South African market. Some are still operating in RSA, despite the difficult political and economic conditions, but they may consider moving to the BLNS countries to overcome the difficulties arising from the reduced protection of the RSA market and to reduce the risk of the expected difficult political transition period. For other investors, political change and the lifting of sanctions, may prompt a renewed interest in locating in the entire SACU region. However, this group will be difficult to approach as they are likely to adopt a "wait and see" policy until the situation is clear in RSA.

6.45 Investment promotion involves three types of activities. These include:

(a) programs to improve a country's image, within the investment community, as a favorable location for investment (image building activities);

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[9] And also countries with unused import quotas in the importing countries.

(b) efforts to directly generate investment (investment generating activities); and

(c) programs to provide services such as information, and assistance in obtaining permits, to prospective and current investors (investor services).

6.46 Experience shows that the provision of services is the most cost effective promotion activity. It involves mostly local costs and can generate immediate results from investors coming to the country whether independently or as the result of other promotion efforts. Image building, on the other hand, is extremely important for small countries that investors either do not know or which are located in a region of conflict. Image building, however, can require large amounts of money and it requires a long term commitment. Image building is useful only if there is a good story to tell -- there is no point in trying to build a favorable image if the policy environment is not right. Likewise, image building and investment generating activities make no sense if a country has not developed the capacity to provide services to investors. These efforts will be defeated by the reality of frustrated investors trying to implement their projects.

6.47 The central issue that governments face in structuring investment promotion efforts revolve around the appropriate mix of private and public involvement in such efforts. There are various reasons why the private sector has difficulties in establishing and funding such operations. First, investment promotion cannot be a profit making activity -- it requires long term efforts and the benefits arising from these efforts are also long term because of the lengthy investment decision and implementation period. Second, to provide effective investor services there is a need for close interaction with government institutions that provide permits and incentives -- an organization that is considered part of the system will probably be more effective in obtaining these approvals. Third, investors do not feel comfortable revealing their project details to people with business interests because of fear of competition or disclosure -- they sometimes prefer to deal with government officials that are expected to be objective, or are monitored, and who are without business interests. On the other hand, the skills and level of expertise needed to perform the investment promotion function are usually found in the private sector. Promoters and good marketing people are scarce in developing countries and are hard to retain on Government pay scales.

6.48 Indeed, neither the wholly public nor the wholly private approach to the management of investment promotion is ideal. Regardless of the approach that is chosen, there will be management issues with respect to how the inherent disadvantages of either approach are to be overcome. In an attempt to overcome these disadvantages, governments may search for organizational approaches that combine most effectively the skills and resources of both the public and the private sectors.

6.49 Many governments avoid extreme approaches and, instead, choose an intermediate approach by conducting investment promotion through a quasi-governmental organization. These organizations, while reporting to the government, are not enmeshed within the conventional government and civil-service structure. This separation from the conventional apparatus of government gives these organizations more flexibility than governments normally enjoy in carrying out the investment promotion function. At the same time these quasi-governmental organizations have an advantage over private organizations in conducting the tasks of investment promotion that require close contact with the government since they are, in fact, an autonomous part of the government.

6.50 *Trade and Investment Promotion Agency (TIPA).* The Trade and Investment Promotion Agency (TIPA), formally known as the Department of Trade and Investment Promotion, has neither the resources nor the mandate to undertake its functions properly. TIPA operates as a small department of the Ministry of Commerce and Industry (MCI) with a recurrent budget of P1.9 million in 1992, about five per cent of the Ministry's total. The 1984 Industrial Development Policy called for the establishment of TIPA, which it charged with the following tasks:

(a) Provision of a "one-stop" service to local and foreign investors to speed up the establishment of productive activities;

(b) Provision of information on investment opportunities;

(c) Provision of trade information;

(d) Maintaining an "Industrial Land Register".

TIPA, were it to function as intended, would serve as a one-stop-shop where investors could obtain all necessary information and approvals. An investor would be able to apply to TIPA for visas and work permits, land, manufacturing licenses, and even to rely on TIPA's help in obtaining financing for a project. While TIPA itself would not be empowered to grant all necessary approvals, it would deal directly with the departments, ministries, and other authorities involved to obtain the necessary approvals. TIPA could act as the principal or sole intermediary between an investor and Government. SPRDP, in fact, provides most of these functions for investors in Selebi-Phikwe, providing initial information, coordinating site visits, securing land or factory shells, guiding an investor through all the steps required for a project to be implemented and, most important, acting as the investor's advocate in negotiations with other Government, parastatal and private sector bodies. TIPA, however, has not been able to perform this function. The real difficulties for investors (decisions on immigration, work permits, land allocations and licensing) remain with other departments, ministries and local authorities and must all be negotiated separately. Hence, although TIPA genuinely tries to assist and support investors, it cannot deliver what it promises. In addition, being subject to civil service pay scales it has less freedom to offer higher salaries and thereby attract the best people. The hierarchy within Government ministries not only prevents TIPA's director from taking decisions and acting independently, but also prevents the kind of flexibility that would enable TIPA personnel to deal directly and informally with the personnel in other departments and ministries whose cooperation is essential for investment decisions to be expedited.

6.51 TIPA could become a more effective trade and investment promotion facility, providing the kind of one-stop services that investors require, if it were given significantly more independence and resources. Ideally, TIPA would become an independent parastatal under the tutelage of MCI, with a board of directors chaired by the Permanent Secretary of MCI and comprising other Permanent Secretaries and representatives of the private sector and, possibly, donor agencies. This would give TIPA control over its own funds and the freedom to set and carry out its own strategic plans. At the same time, the composition of its board of directors would ensure Government oversight, as well as facilitating the kind of inter-ministerial cooperation that is so important if TIPA is to succeed as a one-stop-shop. The Mauritius Export Development and Investment Authority (MEDIA), and Hong Kong's Trade Development Council (TDC) are just two examples of successful and independent trade and investment promotion

agencies which, nonetheless, are subject to some Government oversight. Malawi has recently established an investment promotion agency (MIPA) as an independent agency under the Office of the President, with a mixed Government-private sector board of directors.

6.52 There is legitimate concern that an independent parastatal that is entirely dependent on general Government revenues for its budget would be an anomaly and might violate general standards for accountability. It should be possible, however, to obtain some donor funding to cover a portion of TIPA's expenses and to provide ample technical assistance, especially if it is given the independence and the mandate to undertake its job effectively. USAID is supporting, or has supported, trade and investment promotion agencies in The Gambia, Egypt, Ghana, and the Caribbean with both technical assistance and direct financial aid. The Foreign Investment Advisory Service (FIAS) of the World Bank/IFC is currently supporting technical assistance to the Malawi Investment Promotion Agency and has supported similar agencies in other countries. World Bank support for SPRDP, although it is a regional, rather than a national promotion facility, indicates that similar support might be available to support TIPA. Although it may not be practical from the outset, at some point TIPA may be able to generate revenues of its own by charging fees for services or even by a small levy on exports. Hong Kong's TDC is entirely supported by an 0.25 percent levy on exports, which companies are willing to pay because of the value of TDC's services. There is no evidence that this has functioned as an export disincentive.

6.53 If Government is unwilling to separate TIPA from the Ministry of Commerce and Industry, then it should, at the very least, be prepared to give it substantially greater autonomy within the confines of MCI. This would involve a larger budgetary allocation with which to perform its promotional functions, greater independence in developing strategic plans, and enhanced capacity to recruit sufficient numbers of well-trained staff to undertake serious promotional activities. Even with some reformulation within MCI, TIPA could operate better as an industrial promotion agency. Nonetheless, its chances of success are likely to be substantially increased if it is made an independent institution under the sponsorship, but not the exclusive control, of MCI.

6.54 Overseas investment promotion activities involving a long-term presence should be under the direct control of TIPA and devoted exclusively to the trade and investment promotion function. As the review of SPRDP points out, "there have recently been problems in the operation of the Investment Promotion office [in Hong Kong]. Botswana's presence in Hong Kong has been upgraded to diplomatic representation with consular status, under the Department of External Affairs. Although trade and investment promotion work remain part of the brief, this is now receiving much lower priority and it appears that much of the momentum built up under the [investment promotion] consultancies has been lost."[10] Trade and investment promotion on the one hand, and diplomatic responsibilities on the other, require different kinds of training, orientation, personality, and priorities. Except in those countries where limited trade and investment prospects may not justify the expense of maintaining a separate trade and investment promotion presence, the two functions should be kept separate.

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[10] *ibid.*, par. 4.16.

G. A NEW ROLE FOR THE MINISTRY OF COMMERCE AND INDUSTRY

6.55 As the functions of the Ministry of Commerce and Industry move away from issuing licenses and monitoring their use, it will have to prepare itself to take on new roles. In general, these will be more policy oriented and related to issues which affect the structure and viability of the general industrial system. Issues will include new areas such as trade policy, policies towards service industries, and intellectual property. It should also prepare itself to enter more positively into the debates on those policies which affect the whole environment within which the business community operates. These include taxation policy, employment law and regulations, educational training, public utilities pricing, immigration regulations and land policies. It will have to continue to consult widely with the private sector and to monitor the performance of industry. To facilitate this function, it should develop and maintain a more extensive and coherent data base on the performance characteristics of industrial sub-sectors.

6.56 It will continue to devote considerable resources to existing policy areas such as consumer protection and product standards. These are both key areas for the business environment. Given the small market in Botswana, some consideration may have to be given to competition policy and how this might best be achieved in the Botswana context. In general, the Ministry should prepare itself to develop policies and legislation, and engage in the debates on policies and legislation of other Ministries -- that determine the framework within which the private sector will operate.

6.57 The Ministry will continue to have some program administration functions, especially in the small business and regional development sectors. It will also have to administer legislation on standards and intellectual property, and will also have some general responsibilities for investment and trade promotion. The Ministry, in other words, will have a very full agenda -- but with a new priority on policy issues.

H. THE INDUSTRIAL DEVELOPMENT STRATEGY

6.58 The industrial sector is expected[11] to achieve accelerated growth and contribute to the attainment of national goals through: the creation of productive jobs for citizens, training of citizens, increasing the value added accruing to Batswana, diversifying the productive sectors, and dispersing industrial activities to rural areas. Industrial policy is affected by choices concerning the degree and type of Government intervention, market and product emphasis, emphasis in assistance between foreign and local, rural and urban, formal and informal and large and small. The Government only influences and assists industry with general incentives and services rather than detailed directives or controls -- direct assistance only being used in its efforts to promote the rural, informal and SME sectors.

6.59 The inward orientation of past strategies, however, needs to be further curtailed. This inward orientation, and the associated concern over Botswana's particular constraints, led strategists to assign the public sector the leading -- and sometimes, only -- role in development. Such policies included the use of subsidized capital for development; income tax incentives that result in a very low effective income tax environment; the use of protective measures such as

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[11] *Industrial Development Policy*, Government paper No. 2 of 1984, October 1984.

industrial licensing and import regulation; immigration and labor control measures to limit the presence of foreign entrepreneurs, professionals and managers; and land ownership and use control measures against foreigners.

6.60 A new industrial policy will need to be based on the recognition of the evolving regional and global environment and the need to promote competition, limit the effects of protection and promote foreign investment flows. It will also be necessary to recognize the growing sophistication of Botswana labor and its entrepreneurial base and its ability to play a major role in the diversification process within the manufacturing and service sectors. Last, macroeconomic policy will need to become even more supportive of the establishment of export oriented activities through the removal of policy constraints rather than through the granting of subsidies.

6.61 Past perceptions of constraints needs to be replaced by recognition of the current and future strengths of the Botswana economy. Its closeness to major production and consumption areas in RSA; its large investment in human resources that will increasingly provide skilled workers at competitive prices; its foreign exchange policy that ensures regional and international competitiveness and full convertability; its trade policy that will continue to provide for free entry to the SACU market and to other regional and international markets as the future direction of SACU changes; an export promotion policy that provides exporters with internationally priced inputs and with export insurance and finance; an income tax policy that provides for a low income tax for the manufacturing sector without administered tax incentives; a policy to provide competitively priced infrastructure services by opening these sectors further to low cost imports (including energy, land transport, air transport, telecommunications and construction); and its emerging competitive local capital market that is increasingly open to the private sector for long term finance.

6.62 A new policy must acknowledge the need to assist the development of the local entrepreneurial class. This assistance should take the form of education, training, provision of technical and market information and financial assistance. Under the program of promotion recommended in this report (see chapter 5), smaller scale Batswana entrepreneurs would be the only category of entrepreneurs eligible for FAP assistance. The development of the informal sector is also important and the Government and local authorities should give careful consideration to ways in which they could assist the further development of this sector. Foreign investment should be promoted by the creation of a streamlined entry environment, by ready access to industrial land, and by the provision of information and facilitation services.

6.63 *General incentives for the SME sector* should continue to include a series of general industrial incentives including FAP and the Local Preference Scheme (LPS) -- to provide important assistance to the development of Batswana entrepreneurs. This sector should also continue to be supported by extension services provided by Integrated Field Services (IFS) in rural areas. Financial assistance should be made available through Tswelelo, FAP and to a lesser extent -- until it has been restructured -- the National Development Bank. Training should continue through the services of BEDU and other private and public institutions.

6.64 *Incentives for the larger scale and foreign investors* should be available through the Trade and Investment Promotion Agency (TIPA) and its provision of a "one stop" service to potential investors. TIPA should provide information on trade, investment opportunities, the availability of industrial land, wages and employment information, and industrial licensing

regulations. Manpower training assistance should continue to be provided through the FAP training grant to large, medium and small scale enterprises. Export promotion and participation should initially focus on the active use of existing trade agreements, adapting to new arrangements as they develop. Utility prices should continue to be based upon full cost recovery, with every effort made to increase the efficiency of the utility parastatals and enhance their access to regional sources of supply -- where feasible. Land development policies should fully recognize the pressing needs of industry and meet them to the full. Last, there is the need to coordinate all of these with other policies.

6.65 The evolving policy environment and the need to develop a more neutral, yet transparent, industrial promotion policy will necessitate the modifications in FAP recommended in chapter 5. The introduction of a more flexible wage system, and continued Government focus on skills development and training, will help reduce the need to compensate for high labor costs with labor subsidies. The introduction of competition and cost reduction policies in infrastructure services and construction will reduce the need for protection and sales augmentation subsidies. A new income tax policy of low tax rates and elimination of case by case tax holidays and special treatment of certain groups of investors will create a competitive income tax environment within the region and eliminate the need for tax rebates. FAP will then become solely a system for promoting SMEs.

6.66 The Industrial Development Act, 1988 was enacted to *supervise* industrial development. This supervision was needed to protect certain classes of investors against competition -- indigenous SME investors against all other investors, local investors against foreign investors, and existing investors against new investors. In practice, except for the manufacturing activities reserved for Botswana citizens[12], protection is for existing investors against new investors. The over-riding criteria for refusal of a license can be the presence of *over capacity* in a product or in a certain location. The notion of the ability of the Government to *supervise* development by measuring demand and licensing production capacity to avoid *over capacity* and *waste* of investment, is an archaic concept that by 1988 was fading in most developing countries. Experience in other countries shows that it only leads to the creation of monopolies, inefficiencies, and a high cost environment -- while promoting *rent seekers* rather than efficient and competitive investors. In most cases it does not protect local investors against foreign investors but powerful existing investors against weak new investors as, in most cases, protection is given to existing foreign investors. The recent changes in the industrial licensing procedures will do much to deregulate this market and allow for unfettered competition based upon each private individual's own investment decisions.

I. CONCLUSIONS AND RECOMMENDATIONS

6.67 It is highly recommended that the Government's management of industrial development in Botswana should be based upon "management by exception" procedures. This would permit the Government to concentrate its efforts in sensitive areas while liberalizing in other areas. This method streamlines Government involvement by using the concept of the "negative list" -- which would limit the number of exceptions, permitting all other activities to

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[12] The production of school uniforms, school furniture, burglar bars, protective clothing, cement and baked bricks, milling of sorghum and baking of bread.

proceed unimpaired. This procedure could be used in the area of industrial licensing, regulation of the employment of foreign workers, and in the provision of land for industrial development.

6.68 Future macroeconomic policies will need to ensure, and in fact intensify, the provision of an enabling environment for industrial development. Specifically the Government will need to intensify efforts to promote productivity and efficiency, ensure that deposit and lending rates move to and remain at positive real levels, and improve fiscal policy specifically as it applies to wages and taxes.

6.69 Specifically, tax policy should be overhauled to eliminate the large number of tax exemptions, holidays and allowances which have been granted. Corporate tax levels should be reduced to a lower level and, as much as possible, all exemptions removed. Given current high levels of nominal taxation, combined with a very low effective tax rate, it should be possible to implement this program in such a manner that it actually increases tax receipts while providing a powerful incentive to foreign investors to enter the Botswana market. The fiscal impact of any tax incentives introduced to promote industrial development, will need to be carefully weighed against the changing fiscal environment envisaged during the NDP 7 plan period -- with a projected transition from a budget surplus to a budget deficit situation.

6.70 Rather than fixing minimum wages at a level which makes Botswana uncompetitive in terms of labor costs and productivity, and then providing a subsidy through FAP to help reduce this distortion, a preferable policy would be to eliminate the minimum wage. Allowing wages to be determined by market forces may well lead to higher overall levels of employment. Current minimum wages merely protect the living standards of the currently employed against the currently unemployed. Depending upon unemployment levels and the trade-off between work and leisure time, wages may be sticky downwards. Nonetheless, the continued existence of unemployed unskilled job seekers, and the existence of below minimum wages in work categories currently exempt from minimum wages legislation, argues for some potential for downward flexibility in wage levels. If such action is not possible for political reasons, then the authorities should investigate alternative methods of reducing real wage levels in the industrial sector. Such alternatives include the collapse of the minimum wage structure down to the minimum wage established for night watchmen; exempting manufacturing industry from minimum wage requirements as rural and domestic workers are currently exempted; and, passing on less than the full cost of living increase to minimum wage earners to ensure the erosion of the real level of salaries.

6.71 As increased productivity is also important in Botswana, it is recommended that the authorities should put in place policies which facilitate the greater utilization of piece rate systems. Piece rates can be an effective tool for more appropriately aligning wage levels with overall levels of productivity. However, in the Botswana context, existing policy needs to be changed, so that workers who do not perform to "average" levels of productivity, can be paid below the existing minimum wage.

6.72 Work and residence permits for expatriates continue to be an impediment to foreign investors. It is recommended that the Government move toward a more targeted immigrant labor control system, similar to schemes used in more developed countries. Under such schemes, positive occupation lists are used, and entry for individuals with qualifications identified on that list, is reasonably free. Typically these are occupations which are in short supply and high demand in the local economy.

6.73 Industrial land should be dealt with in a completely separate manner from other types of land in Botswana and there is an urgent need for planners to plan for industrial land development well beyond the current 20 year planning horizon. Large industrial zones should be demarcated in urban areas and access to this land should be extended to all investors, both local and foreign. It should be available to investors on the basis of, at least, a 50 year lease and should be transferable for alternative industrial uses. Taxes on industrial land should be designed in such a way that they encourage the development of the land for industrial purposes rather than having it remain idle for purely speculative reasons. Under the existing ALSP, the Government should also give higher priority to the development of industrial land -- specifically in Gaborone. To oversee land distribution and to assist in the planning process, it is further recommended that a Land for Industry Committee be established (or created from existing committees) in the Department of Town and Regional Planning in the MLGL with broad, high level representation from relevant Government ministries.

6.74 In addition to encouraging greater efficiency in the utility parastatals, it is recommended that Botswana should develop a more pragmatic approach toward the use of low cost utility and infrastructure services available from South Africa and other neighboring countries -- wherever possible. Although this may not be possible for some utility services, it is certainly possible with respect to transport facilities, power and telecommunications.

6.75 Attempts should not be made to subsidize utility costs to make them comparable to levels in neighboring Southern African countries. In some cases, the prices in the neighboring countries are themselves subsidized and unsustainable and will ultimately have to be "freed" with adverse implications for industrial development in those countries. In addition, subsidizing utility costs in Botswana may well distort the pattern of industrial development towards a pattern of production which is undesirable (i.e. high water utilization industrial production).

6.76 Investment promotion in Botswana will need to have a strategy, an institutional structure, and good management. It should target sectors in which it wishes to actively promote foreign investment and also regional markets from which it intends to draw foreign investment. With respect to targeting of regional markets, it is recommended that South Africa, and possibly other neighboring countries such as Zimbabwe, should be targeted for investment in Botswana. Thereafter the newly industrializing countries of Asia should be a secondary target, followed by investors from Europe, the US and Japan. Investment promotion should build Botswana's image, directly attempt to generate more investment, and provide crucial investor services.

6.77 To assist in export promotion, the Trade and Investment Promotion Agency (TIPA) should be removed from the Ministry of Commerce and Industry and reformulated as an independent parastatal. It should be allowed to develop as a true "one-stop" services center such as the Mauritius Export Development and Investment Authority (MEDIA) and Hong Kong's Trade Development Council (TDC). If this recommendation was unacceptable to Government then it should, at the very least, be provided with substantially greater autonomy within the confines of the MCI.

6.78 Last, there is an important need for the Ministry of Commerce and Industry to reexamine its future role with respect to industrial development. Whereas, in the past, the Ministry has had responsibility for the two potentially conflicting objectives of licensing and regulating industry and promoting and encouraging industry, in a new substantially deregulated

environment for industrial development, it should be the latter, rather than the former role which assumes prominence within the "new" MCI.

CHAPTER 7

OPPORTUNITIES FOR INVESTMENT IN BOTSWANA

A. THE CURRENT INVESTMENT ENVIRONMENT

7.1 Few developing countries have been as fortunate as Botswana enjoying over 25 years of political stability and democratic rule. Botswana's political system, which incorporates both the traditional kgotla tribal gathering and a modern democratic state, ensures that Government responds to the people to a degree found in few other countries, thereby reducing the risk that opposition groups will resort to extra-parliamentary means to advance their causes. Regular parliamentary elections have kept the Botswana Democratic Party in power since Independence. However, other parties participate freely in these elections and are represented in national and municipal governments. Botswana enjoys freedom of the press, and experiences lively debate on a wide range of issues. Although there has been concern in recent years about growing corruption, there is evidence that corruption is still considered an aberration that will not be tolerated.

7.2 Since Independence Botswana has lived in an uneasy accommodation with South Africa. While deploring its system of apartheid, Botswana's leaders have recognized that for economic, logistical and security reasons they must maintain peaceful coexistence. Even during the period of greatest tension between South Africa and the frontline states, the Southern African Customs Union was preserved and serious military confrontation was avoided. During that period transport and telecommunication links, electricity and water connections, and other essential areas remained undisturbed -- even though, at times, they may have been at risk. In the foreseeable future Botswana's location, across the border from RSA, may again be seen as a comparative advantage over most other African countries.

7.3 Botswana has one of the world's fastest-growing economies. The Government has used its diamond revenues well, building essential infrastructure and creating an open economy -- while mainly being successful in resisting pressures to increase its spending. While the public sector continues to grow rapidly, and Government remains the largest employer, its spending has nonetheless grown more slowly than the economy as a whole. The strength of the pula has permitted Botswana to remove most foreign exchange restrictions -- and further liberalization is in prospect. This is a major competitive strength and a key element of Botswana's potential to become a regional financial center.

7.4 Botswana has significant advantages in access to regional and world markets. Membership in SACU has given Botswana free access to a wide range of consumer and capital goods produced in South Africa while providing Botswana manufacturers duty-free and quota-free access to the South African market, the richest in Africa, with over 35 million consumers. Zimbabwe has been another major outlet for Botswana manufacturers. Although current trade disputes and a fall in the value of the Zimbabwe dollar have reduced the ability of Botswana companies to compete in this market, over the long term, Zimbabwe is likely to once again become an important trading partner. Botswana also enjoys preferential access to markets in Europe and North America -- as a member of the Lomé Convention and under the Generalized System of Preferences. While these agreements are unlikely to change, closer ties between the EC and countries in Eastern and Central Europe on the one hand, and between the United States, Canada and Mexico, on the other, will increase competition for Botswana manufactures in those markets.

B. DEVELOPMENT OF MANUFACTURING INDUSTRY

7.5 As the discussion of the political and economic environment indicates, Botswana, while continuing to enjoy a number of advantages, will also find competition more difficult in many markets, especially with respect to exports of manufactured goods. Botswana's strengths that give it a competitive advantage include: (a) an open, liberal economy; (b) political stability; (c) commitment to private sector driven development; (d) few exchange restrictions and a realistic exchange rate; (e) good infrastructure and reliable telecommunications; (f) close links with the RSA economy; (g) unique wildlife and natural attractions; (h) one of the highest literacy rates in sub-Saharan Africa; (i) rising levels of computer literacy; (j) specialized agricultural potential (cotton); (k) diversified financial services, by regional standards; and (l) a high savings rate[1] -- which at 37 percent of GDP, is one of the highest in the world.

7.6 Its weaknesses include: (a) remoteness from major markets other than RSA; (b) high cost of transport; (c) high cost of land, utilities, and construction; (d) high cost and low productivity of labor; (e) shortage of skilled personnel and lack of vocational training: (f) lack of large-scale agricultural potential; (g) lack of commercial/entrepreneurial orientation among the local population; and (h) a persistence of regulatory disincentives to investment.

7.7 Botswana's industrial development strategies have tended to focus on the labor-intensive manufacturing industries that every developing country has tried to encourage. It is understandable that the Government would seek to develop such industries. Other countries, including Singapore, Taiwan, Korea and, closer to home, Mauritius, have successfully pursued similar strategies.

7.8 As indicated in numerous policy statements and on-going development plans, a major aim of Botswana's drive for industrial development is to generate employment for a pool of unskilled individuals entering the labor market. Although it is unclear the extent to which unemployment is currently a pressing problem, there will necessarily be an on-going need for the creation of unskilled employment opportunities. The development of labor intensive manufacturing industry appears to offer the best hope of creating large numbers of employment opportunities for unskilled personnel within the economy. As a result, the continued promotion of such industries will remain an important imperative. Botswana's success over the 1980s in generating rapidly growing employment opportunities in the manufacturing sector, albeit from a low base, is evidence of the fact that it can have important employment generating effects.

7.9 It will be important, however, that any such industries which are developed, be sustainable over the longer term. The criticism in this report of the FAP scheme, is that it may well be developing unsustainable manufacturing industries -- which after the five year period of the scheme, will have not *grown up*, and consequently will come back to Government requesting further support, with the implicit threat that, without such support, they will lay off many employed workers. Examples of structural adjustment problems, caused by the creation of inefficient industries, are in evidence all around the world -- in both developed as well as developing countries. Botswana should take care to avoid future pain and realignment by supporting infant industries which never grow up. This report seeks to put forward recommendations to ensure that this will not take place.

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[1] Mainly public sector savings.

7.10 The industries that Botswana has targeted most intensively, such as garments, are highly sensitive to cost. Differences in manufacturing or transport cost of a few percent can mean the difference between a profitable venture and one that fails. As these are industries in which labor represents a large portion of total cost, it is important that Botswana tackle the issues of wages and productivity addressed in chapter 6. A streamlining of the incentive system to a country wide, low tax system, in which special additional benefits are only granted to small scale Batswana entrepreneurs, is considered preferable to the current system. This would need to be supported by the introduction of other recommendations made in this report -- including the introduction of management by exception with respect to work permits and residence permits, freeing up land markets, developing a more independent investment promotion agency -- if the program is to be successful.

7.11 However, the diversification of Botswana's industrial sector into labor-intensive manufacturing is but one of several options that offer opportunities within a generally enabling environment for economic growth. Capital-intensive investment in the mining sector has been a key factor in the country's growth during the last three decades. The infrastructure also exists to support capital intensive projects in manufacturing. Botswana has a comparative advantage in such investment over most Sub-Saharan and other labor-rich developing countries, and there is evidence that such investment is already happening -- in the textile industry, for example.

7.12 As they have not been publicized, the opportunities for capital intensive manufacturing in Botswana will need to be actively promoted both in the region and further afield. There is also no need for special incentive programs for investors (such as FAP for labor intensive operations) as there are no local constraints requiring compensation, although, institutional problems that affect all forms of investment (access to land, work permits, and so on) need to be resolved as much as they do for other types of investment. Botswana has the foreign exchange resources, the local financing capacity and both local and expatriate experience in managing and executing projects involving large inputs of plant and technologically advanced machinery. It is important for industrial development policy to not neglect particular sectors, whatever the proposed mix of factors of production, but to keep the door open for all legitimate investment. The decision as to what is sustainable and what is not can be left to individual investors.

7.13 Botswana should also encourage the development of industries that build on its potential advantages in finance, tourism, and other services. The tendency has been to think of these as mainly domestic industries. Other developing countries, however, have demonstrated the export potential of a wide range of services, some of which have significant potential for development in Botswana. As indicated in chapter 2, whereas the impetus for growth throughout the 1980s came from a surge in domestic demand, NDP 7 foresees a possible halving in the growth of domestic demand over the plan period. If these projections prove to be correct, employment creation in labor intensive manufacturing industries may not be as rapid during the 1990s as it was in the 1980s. This makes it all the more necessary to diversify industry and to encourage an even-handed approach to all investment, whether in manufacturing, services or in the primary sectors -- and whether labor intensive or capital intensive.

C. OPPORTUNITIES FOR DEVELOPMENT OF SERVICE INDUSTRIES

7.14 *On-line Transactions*. The relatively large number of computer-literate and English-speaking people available in Botswana provides a potential for the development of on-line transactions -- such as airline reservations -- at a competitive cost. Botswana's reliable telecommunications infrastructure should make it possible to develop this industry, as several Caribbean countries and Mauritius have done. Although the combination of good telecommunications, computer literacy, English language and moderate wages is not unique, it does appear to be an area in which Botswana is potentially competitive. Botswana could become an on-line center for the UK.[2] This would probably require the installation of dedicated satellite communication lines and fault-tolerant computer systems, at a significant cost, but over time the cost of paying Botswana wages rather than European wages should make this an economically viable industry.

7.15 *Postal Re-expediting*. Botswana, which has international postage rates a fraction of those in Europe or North America, could become a center for bulk mailings, following similar developments in Denmark and the Netherlands. Companies sending out large numbers of promotional mailings or bills could obtain significant savings by transporting the materials in bulk, via air freight, to Botswana, where they would then be sorted and the appropriate postage affixed. Such operations are relatively labor intensive. While Botswana's cost advantage could be partially eroded the next time international postage rates are negotiated, it is unlikely to disappear altogether. Starting from simple sorting and franking this industry could soon move to higher value added operations, such as generating and printing bills or other statements of account.

7.16 *Computer Programming*. Compared to its low level of skill and productivity in manufacturing, Botswana's capabilities in computer operations are fairly well-developed. This advantage can be increased by placing greater emphasis on computer training at the University, the Polytechnic, and in secondary schools. Computer and software companies in Europe and North America, which require millions of lines of computer code to be generated in developing or refining computer applications, could use Botswana workers to perform much of this work, at a much lower cost than in their home countries. Other countries, such as India and Ireland, have had considerable success in developing this industry. Given its superior business environment, Botswana should be able to do likewise.

7.17 *Medical Services*. With the opening of a state-of-the-art hospital in 1992, Botswana will be diversifying into another area of invisible exports -- that of medical services. This hospital is one of the most advanced in the region and is staffed by extremely good doctors. While it may take time to attract large numbers of patients from the region, the regional demand for good quality medical services is very large among the more affluent social groups and expatriate communities in Sub-Saharan Africa. With the right kind of marketing, it should be possible to attract affluent patients, or those requiring specialty treatment, to come to Botswana from neighboring countries.[3] The demonstration effect of the new hospital is important and would make it easier to interest international medical insurance groups in

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[2] In such cases, the actual response to people in, say, Britain, who call up British Airways to make a reservation, is by someone in Botswana. This has been done quite successfully by some of the United States airlines -- in Barbados.

[3] Such schemes operate between other countries, even in the developed world, where patients with a particular ailment may go to a hospital in a nearby country because of either the reputation of that hospital in a particular type of treatment, or simply because the home country does not offer treatment in a particular area of healing or surgery.

further expansion in this sector. If there is to be any encouragement of medical research activities there may also be a need for patent registration facilities in Botswana.

7.18 The availability of land and of immigration permits for expatriate staff are key factors in the development of this sector. Mauritius provides a tax incentive for the operation of clinics by levying income tax at 15 percent instead of the standard rate of 35 percent. Botswana might consider similar incentives, which only benefit profitable entities, and which would be less of a financial burden than FAP.

7.19 *Financial Services*: Botswana's open financial system, the strength of its currency, the relative lack of exchange controls, as well as its political and economic stability and reliable telecommunications, give it the potential to become a financial center, providing services both to other countries in the region and to clients worldwide. For Botswana to become a recognized offshore financial center would require further liberalization of financial regulations -- at least for exclusively off-shore oriented business. Specifically, it would require:

(a) removal of personal and corporate exchange controls
(b) allowing individuals and corporations to hold, and banks to provide, foreign-currency account facilities
(c) removing all restrictions on offshore investment for off-shore annuity and other long-term risk insurance business
(d) removing restrictions on foreign purchases of Botswana shares and unit trusts
(e) removing withholding tax on dividends paid offshore
(f) drafting regulations to prevent abuse of the banking system
(g) appointing an off-shore banking supervisor
(h) liberalizing work and residence regulations affecting essential expatriates working in the off-shore sector.

7.20 Botswana has significant potential to become an insurance and reinsurance center for Africa. The establishment in Botswana of the Information Trust Company credit rating service (formerly a subsidiary of Dun & Bradstreet) will facilitate the availability of export credit insurance, and will also give Botswana greater credibility in international markets. Since reinsurance rates are determined on world markets, with complete foreign exchange liberalization, Botswana reinsurers will be able to compete internationally. As this market is developed, foreign insurers and reinsurers will begin to set up operations in Botswana. The technology and skills base available locally will undergo constant improvement, which will, in turn, increase Botswana's competitive advantage. This has happened, for example, in Bermuda, where over 1,300 insurance operations are now domiciled.

7.21 As a banking center, Botswana can become the financial capital of Southern Africa and a conduit for the increased flow of investment into South Africa that has already begun as apartheid is dismantled. Since there is little likelihood that South Africa itself will lift exchange controls in the foreseeable future, Botswana is ideally placed to become the banker to future development there, as well as in the rest of the region as South African firms, now able to trade freely with and invest in other African states, seek financing for expansion. With a freer financial and tax regime, companies investing in South Africa may choose Botswana as their domicile, just as in Europe, many companies have incorporated in Luxembourg. As its importance as a regional financial center grows, Botswana may ultimately become a fully international financial center, similar to Luxembourg or the Channel Islands.

Alternatively, should conditions in South Africa remain unsettled or become more unsettled, Botswana may become a conduit (or a parking place) for the outflow of capital from South Africa.

7.22 Either way, the potential benefits to Botswana are great. In Jersey, for example, for every job created in the banking industry, a further eight jobs were created in other areas. Banking expansion has important multiplier effects on employment in construction, communications, trade and other commercial services.

7.23 Other finance-related services in which Botswana has potential include bank back-office operations, such as cheque-clearing. Both South African and European banks may find the cost of processing bank transactions significantly lower in Botswana. With regular direct flights from London and Paris, Botswana could prove a low-cost location for this service which Caribbean islands, such as Barbados and Jamaica, provide for the American banking market.

7.24 ***Off-Shore Banking***. Location, the availability of capital and foreign exchange and other aspects of the investment environment favor the development of services which generate invisible export earnings. Prominent among these activities as a potential growth sector in Botswana is offshore banking.[4] The main business of offshore banks, whatever their location, is to borrow money from non-residents, the loan instrument being denominated in a foreign currency, for re-lending to other non-residents, at a profit. There are prerequisites for a country that proposes to become an offshore banking center, based on the experience of countries which have done so or failed to do so. It is essential that offshore banking operations be free of foreign exchange controls and of withholding tax on bank earnings from offshore business. There should be low, or no, reserve ratios on offshore liabilities. There must be a good telecommunications network, skilled banking staff, and political stability. It also appears that countries which operate effective banking controls and supervision stand a better chance to develop as offshore financial centers than those which favor a free-for-all. Since control and supervision bodies of the world's newer financial growth centers favor banks with a pedigree, it is the old, established banks that have been the moving force behind the overall growth in offshore banking. Mauritius is the only African country to have made real attempts to provide the institutional framework for such activities. However, in Mauritius the Government's control of offshore banking units (OBUs) includes the regulation of liquidity ratios by the central bank, which is unusually restrictive. As a consequence, there has not been much growth in the OBU sector after the initial registration of a handful of entities, mainly banks already operating there. It is likely, however, that these controls will be relaxed.

7.25 Once the appropriate regulatory and fiscal environment for offshore banking operations is in place there is scope for development of a number of other international financial and management services including custody services, portfolio investment, insurance and holding company operations. With Botswana's central location in the region, political stability and agreeable living conditions, it could attract a host of other invisible export activities related to regional corporate headquarters, countertrade, entrepot, distribution and sales companies, such as US Foreign Sales Corporations. As RSA opens up to foreign investment, and there is a real prospect for the regeneration of Angola and Mozambique, the time may well be right for Botswana to take this opportunity to establish itself as a secure base from which to operate regional financial and management services.

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[4] Also mentioned in a report for MCI: *Trade and Investment Promotion Consultancy*, by L. James Eaton, March 1988.

7.26 Setting the scene for development of offshore banking and other services will require certain important regulatory and legislative measures to be taken after an in-depth review of all the issues. Access to office space and housing will be an important factor, as will a fundamental change in the attitude toward temporary immigration of expatriate staff. Operating an offshore banking sector would need a further relaxation in exchange controls or legislative provisions to allow offshore banks and other offshore businesses to operate through *exempt* entities, not subject to exchange restrictions. There is no tax on foreign sourced income, which is an important advantage for offshore operations with funds coming in from abroad. However, the kind of turntable operations performed by offshore financial institutions would require a matching removal of withholding tax on dividends, interest and royalties paid out to non-residents. The tax treatment of offshore banks would have to include the introduction of license fees instead of corporation tax. This provides a reliable and potentially important source of revenue for the Government. A framework for offshore finance regulation and supervision would have to be established. Technical assistance for such institutional changes would be available through the Offshore Group of Banking Supervisors, formed by the world's 15 leading offshore finance centers, or the Bank for International Settlements. Two decades of offshore business expansion around the world coincided with two decades of legislative and regulatory trial and error. A new entrant, such as Botswana, can now pick and choose from control systems elsewhere, the elements of which are most suitable to its particular operating environment.

7.27 ***Grain Storage.*** With its central location in the southern African region there is a case to be made for the construction of storage facilities for a Strategic Regional Grain Reserve in Botswana. The 1992 drought and consequent grain shortages in Zimbabwe, for example, illustrate the need for such a facility established out of reach of local political pressures. The construction of storage facilities could be financed by Botswana, while the aid community and participating Governments would finance the stocks. Botswana would earn storage and management fees and would be responsible for the release of supplies and transport arrangements, as needed.

7.28 Such a project would require land for construction (derelict mining property could be considered for adaptation -- provided that access was adequate). There would be a need for technical assistance in establishing management and control systems which were clearly independent from all Governments, possibly by granting some form of diplomatic status. The operational methods adopted by different buffer stock management schemes, including EC strategic oil supplies and farm surpluses administration, could offer elements that could be adapted for this project.

7.29 ***Skills and Training for the Development of the Service Sector.*** With respect to the development of service industries, concerns have been raised about the education system's ability to produce the skills required for the industries which could develop in Botswana during the 1990s and beyond. Government policy during NDP 6 was to use scholarships to address areas of critical manpower shortage. With the abolition of secondary school fees in 1989, scholarship awards became restricted to higher education, mainly for University of Botswana students and students training abroad. Allocation is based on the country's perceived manpower requirements, not on students' individual financial needs. Government scholarships to students in local tertiary institutions increased to almost 98 percent of the total number of students by 1990/91. Scholarship beneficiaries sign agreements to complete their specific courses and to contribute 5 per cent of initial salaries for the same number of years as the courses taken.

7.30 Among the industrial development opportunities for Botswana suggested in this report are

a range of business and financial services. Such industries rely on the availability of low and medium-level data-processing and other computer-based skills. These are currently in short supply and therefore command premium pay rates. Both the public and private sectors are now engaged in a program of education and training which will relieve some of the worst bottlenecks.

7.31 Beginning in the early 1980s microcomputers found their way into secondary schools and higher education institutions in Botswana. There was no national policy on computer education and whatever took place was a result of the efforts of enthusiastic individuals. The University of Botswana and the Polytechnic were the first institutions to establish computer laboratories and to run some formalized courses. At the university, computer courses were gradually introduced as part of degree courses; in Science, mainly programming; in Commerce and Education, the use of appropriate application software. The Polytechnic commenced with basic computer awareness programs for students in the Telecommunications course and later moved into computer-aided design and other more advanced applications.

7.32 At secondary school level, students are exposed to computers through computer clubs. There are no recent figures on the number of computers in secondary schools, but it is known that in 1989 -- 19 out of the 23 secondary schools had access to at least one computer, usually donated by local businesses or obtained through parent/teacher fund raising. The result is a wide range of hardware and software in schools with a consequent lack of coordination.

7.33 A few teachers have used computers as an aid in science and mathematics lessons. One senior secondary school, Lotsane, introduced computer studies as an O-level subject in 1986; a private secondary school, Maru-a-Pula, has been offering a non-examinable course for all students since 1984, focusing initially on Logo, but more recently on word-processing. Under an ADB-financed project all 23 secondary schools were given 5 computers each in 1992, plus printers and software as part of a Form 5 computer awareness program. In-service training is to be provided for 2 teachers per school. Students will be issued with certificates to indicate which modules they covered.

7.34 There is also a whole range of, mainly private, organizations offering short courses on software applications. In some cases diploma courses are offered, but of varying standards. The task of Government will be to ensure uniformity and acceptable standards.

7.35 A Government Computer Bureau (GCB) has been set up, initially to address the public sector's skills requirements in the face of an overall shortage and a continued drift of trained people from the public to the private sector. It is now concerned both with training trainers and with training for the country's needs as a whole. The GCB introduced its computer training program in conjunction with the National Computing Center of the UK. The numbers of students leaving with a standard diploma from GCB and associated programs will be about 40 a year from 1992/93. The numbers leaving with higher diplomas should reach 15-20 a year starting in 1993/94. In addition, the Botswana Institute of Administration and Commerce runs a one-year computer studies course with an output of 20 or so successful candidates per annum. The university started its 4-year computer science degree course in 1992 and also offers a 2-year diploma course. The combined education efforts of the private and public sectors are expected to achieve a better-balanced skills market within the next 5 to 10 years.

7.36 A computer education turning point was reached in 1991. Parliament passed a resolution fully supporting the introduction of computer education in schools and the Ministry of Finance and

Development Planning took the initiative to speed up computer education and training nationally, at all levels.[5] A National Committee on Computer Education and Training with representation from relevant training institutions, the Ministry of Education and the Ministry of Finance and Development Planning, was established to advise Government on pre-and in-service needs in the field of computer education and training. The specific terms of reference for this committee are to:

(a) Identify national computer training needs by carrying out research on both present and planned computer applications and, from there, establish and monitor manpower requirements.

(b) Draw up and oversee the implementation of a cohesive national training plan for both pre-service and in-service computer education. Ensure that course content meets national training needs.

(c) Advise on resources required for computer education and training.

7.37 The Committee's main responsibility will be to oversee work that will lead to the identification of Botswana's needs in terms of computing abilities, and to translate these needs into a national training plan. It will report to the Government Computer Steering Committee, an umbrella organization, which has been dealing with the country's overall computerization program.

7.38 Continued Government and private sector support for training and skills development programs will be important for the foreseeable future. Although the Government will have an important lead role to play in this regard, it will also be necessary to harness the support of the private sector. Hence, the continuation of expanded training grants under the FAP program, as recommended in chapter 5, is considered important, to encourage the private sector to be more actively involved in training programs. The further development of private sector based technical education and training facilities should also be encouraged.

D. DEVELOPMENT OF DOWNSTREAM PROCESSING INDUSTRIES

7.39 One answer to the lack of a competitive cost structure in manufacturing has historically been to place greater emphasis on using raw materials available in Botswana. Every attempt should be made to further develop such activities, where such action proves viable. The industries generally considered for further downstream processing, and the products that can be produced from them, include:

(a) Hides and skins, leading to production of leather and leather goods, including footwear;
(b) Salt and soda ash, leading to production of glass, detergents, table salt, and chemicals;
(c) Uncut diamonds, leading to production of cut diamonds and jewellery;
(d) Semi-precious stones, leading to polishing and jewellery production;
(e) Timber, leading to production of veneers, parquet flooring, and hardwood doors;
(f) Raw silk, leading to production of fabrics and clothing;
(g) Game, leading to production of meat, leather and leather goods;

[5] Data for this section was provided by Ms. Marianne Nganunu, Ministry of Education, Botswana.

(h) Cattle bone leading to production of buttons;
(i) Tallow, leading to production of soap and candles;
(j) Indigenous fruits and veld products, leading to production of dried flowers, jams, medicinal plants;
(k) Handicrafts, with potential for export of beads, carvings and baskets;
(l) Cotton.

7.40 *The leather industry*, which Government, BMC and BDC have for years tried to develop, has faced several problems including the low quality of Botswana hides, low-cost competition from Argentina and Brazil, and a market structure that can keep the export price of Botswana wet-blue hides higher than further processed crust or finished leather.

7.41 *Game Skins and Meat Products*. Limits on shooting of local game, together with an overabundance in Europe of game meat products from Eastern Europe, mean that game skins and meat products will never be more than an attractive niche industry. A 1989 study concluded that an abattoir devoted to game meat processing could never be viable. BGI Tanning in Francistown already employs some 130 citizens in game-skin tanning, and is considering an expansion into tanning locally-produced crocodile skins. Apart from this, there appears to be little prospect for further expansion.

7.42 *Timber* supplies in Chobe Forest Reserves may be far lower than previously thought. There is little prospect for expansion of the industry beyond the two companies currently operating. Depending on the results of a timber census, currently in process, even the activities of these companies may have to be curtailed.

7.43 *Diamond Cutting and Jewellery Manufacturing*. Two companies, with projected future employment of 700, have recently begun diamond-cutting operations in Botswana, with the possibility of further expansion into jewellery-manufacturing. Together with the Oro-Bot jewellery manufacturing Company -- scheduled to begin operations in Selebi-Phikwe in late 1992 and expected to employ 1,500 people -- these projects could be the start of the development of a jewellery industry which, as some people trained in these projects start their own small companies, could grow significantly. It is questionable, however, whether any further large-scale investments can be expected. While diamonds are produced in Botswana, and gold in South Africa, prices for both commodities are set in world markets, with no local cost advantage. Given the high value of the finished product, however, and the relatively low proportion of final value represented by direct labor, Botswana may be able to develop a competitive advantage in jewellery production, provided that local workers can be trained in a reasonable time to reach required quality standards.

7.44 *Soap*. The availability of locally-produced tallow in Botswana gives local soap manufacturers a slight cost advantage, although the quality of Botswana tallow is inferior to that of imported tallow. Namibian tallow, moreover, is even cheaper than Botswana's. Any cost advantage is, in any case, negated by the high cost of transport to markets in South Africa and Zimbabwe; the low cost of Zimbabwean exports into Botswana due to the decline in the Zimbabwe dollar; smuggling of soap into Botswana because of the 100 percent tariff protection; and the 20 percent tariff imposed by the PTA.

7.45 *Veld products* and other *horticultural products* show some potential. There is a small,

but attractive market in South Africa, Europe, and even North America, for such products as jams and dried fruits produced from marotse melon or morula, as well as for herbal medicines from indigenous plants. The cost of transport, as well as the cost of setting up production facilities that meet US and EC health regulations, may, however, price Botswana products out of these markets. Nonetheless, with the availability of regular direct flights from Botswana to Europe, it may become possible to cultivate and export horticultural products such as cactus plants, cut flowers or certain high-priced vegetables. Developing this market may require more frequent air connections than are currently available, and may also require flights to cities that are not currently served (e.g., to Amsterdam for house plants and cut flowers). Nonetheless, these possibilities are worth further investigation.

7.46 *Cotton* is a crop that could be grown in commercial quantities in Botswana, at a competitive cost. Lonrho is currently negotiating with BDC to take over management of Talana Farm in the Tuli Block, to increase cotton yields. This in turn could give Botswana a cost advantage in the production of textiles and, possibly, garments. If this project is successful, it could give Botswana a base from which to promote further development of the textile and garment industry. Given the cost of transport, however, the main potential market may be South Africa rather than Europe and North America.

7.47 Lonrho is also investigating a potential project in which it would grow sugar cane under irrigation in the Caprivi Strip for consumption by Namibia and Botswana. A sugar refinery would be established adjacent to the sugar estates in the Caprivi. If this scheme was acceptable to Botswana, the estate would be extended to include the cultivation, under irrigation, of cotton on the Botswana side of the border. This cotton would be ginned in Kasane and would make Botswana self-sufficient in cotton. In addition, cattle feed would be available as a by-product.

7.48 As this discussion indicates, there may well be some limited potential in the development of down stream processing industries in Botswana. As the experience in diamond-cutting and jewellery-manufacturing shows, companies may find attractive opportunities, even where local availability of raw materials does not necessarily translate into a cost advantage for local manufacture. Hence, Botswana should continue to promote these, and other, opportunities by creating an enabling environment for investment in manufacturing and service industries generally.

E. DEVELOPMENT OF TOURISM

7.49 Tourism has been identified as an industry with potential to contribute to rural development and employment creation. Nearly 70 percent of employees in this industry are located in rural areas, and 40 percent of all formal sector jobs in the north-west of Botswana are linked to tourism. As shown in table 7.1, employment in tourism and related activities increased by about 78 percent from 1984 to 1988 -- 15.5 percent per annum.

7.50 The development of tourism has been largely through the initiative of the private sector and non-government organizations, with the Government playing a supportive role -- which it intends to strengthen in the immediate future. A new Tourism Policy was approved by Parliament in 1990 and a new *Tourism Development Act* was passed in August 1992. These measures are designed to improve earnings from tourism resources and to ensure that the development of the industry meets international standards for quality -- while using the resources on an environmentally sustainable basis. The following

steps are being taken to achieve these objectives:

(a) *Emphasizing up-market tourism.* The mix of tourists is being shifted away from casual campers toward occupiers of permanent accommodation.

(b) *Benefitting local people.* The share of financial returns from tourism that accrue to Batswana will be increased -- especially to those living in the local communities where wildlife resides.

(c) *Sustainability.* Measures are being taken to ensure that tourist activity is carried out in ecologically sustainable ways.

Table 7.1: Employment in Tourism and Related Activities
1984 and 1988

Category of Employment	1984	1988
Tourism Development Unit	13	21
Accommodation	2,200	3,242
Air Transport	250	519
Vehicle Hire	55	64
Travel Companies	48	863
Safari Companies	240	478
Crafts and Trophies	200	159
TOTAL	3,006	5,352

Source: NDP 7 and Tourist Statistics, CSO.

(d) *Regulation.* The Tourism Development Act provides for systems of licensing and grading of tourist operators which will ensure that standards are established and maintained.

(e) *Tourist Concessions.* The terms of new concessions are being designed to provide greater security of tenure to encourage investment and better management; to provide for increased Batswana participation in tourist activities; and to improve revenues accruing to the Government and local authorities.

(f) *Taxation.* The new Companies Act will ensure that companies operating in Botswana

comply fully with the taxation and accounting requirements of Botswana.

(g) *Localization*. The Government wishes to increase Batswana participation in the tourism industry as employees, investors, and operators. Licensing will establish localization objectives for operators, and financial assistance will be made available for training in tourism skills. Consideration is being given to the provision of a FAP type program for Batswana embarking on tourism ventures.

7.51 ***Institutional Framework***. In few other countries is there a greater risk that the development of the country's tourism potential will destroy the main tourist attractions, than in Botswana. The desert, the wildlife, and the Okavango are ecologically vulnerable. The experience in Botswana is that nature is severely impaired if tourist density increases. As Government has identified, the challenge is to increase the money spent by tourists without increasing their numbers.[6]

7.52 The new Tourism Policy proposes several measures that can increase tourist income, while preserving the natural resources on which the industry depends. These include:

(a) increasing the length of concession leases and ensuring their transferability
(b) ending the ban on permanent structures
(c) awarding concessions through public bid, with bidders submitting development plans with their bids
(d) establishing a system of licensing and grading of hotels, lodges and safari operations to conform with the World Tourism Organization (WTO) standards for Africa.

7.53 By ending the ban on permanent structures and increasing the length and transferability of concessions, tourism companies will have a greater incentive to invest in facilities, knowing that they will have the right to operate them long enough to earn a return and recover on their investment. Awarding concessions through public bid will result in higher revenues paid to Government and a tendency to move up-market in developing tourist facilities, since high-quality and high-cost operations will be able to afford higher lease rates.

7.54 By upgrading the Tourism Department from a unit to a fully-fledged Department in the Ministry of Commerce, Government has sought to make it a more effective promotor of tourism. The Tourism Department's responsibilities under the new policy will include marketing, collection of statistics, licensing and inspection, training, and management services. The department's main problems are similar to those faced by TIPA. As a part of Government, staffed by members of the civil service, it cannot become an effective promotion unit, especially since it also has regulatory responsibilities. While the Tourism Department can, and should, continue to collect statistics and play a role in licensing of tourist operations, the marketing and promotion function should be separate from the regulatory function, a situation which already exists in practice.

7.55 The Hotel and Tourism Association of Botswana (HATAB) has become an effective organization for promoting tourism with its annual Kgotla event in Gaborone and participation in overseas

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[6] It is interesting to note, however, that in Kenya, which also has a fragile eco-system, large volumes of tourists visit each year making tourism a major foreign exchange earner for the economy.

tourism fairs. Since HATAB already consults with the Tourism Department, there is unlikely to be excessive tension between them if HATAB takes over tourist marketing and promotion. Funds currently allocated by Government for tourism promotion could be given to HATAB, as the executing agent. HATAB, with the support of BOCCIM, is planning to open its own training center, which will have support from Government and some technical cooperation with Namibian tourist organizations. One of HATAB's functions is to lobby Government on behalf of the industry for changes in tourism policy. Closer coordination between HATAB, BOCCIM and the Tourism Department should ensure that this continues.

7.56 Annex 4 includes a short "think-piece" on the relationship between nature tourism and the new Tourism Policy in Botswana.

F. CONCLUSIONS AND RECOMMENDATIONS

7.57 Botswana's current investment environment has much to recommend it to potential foreign investors. Political stability and democracy are rare in Africa and yet Botswana offers both of these attractions. It also has experienced continuous rapid growth, it has a high level of per capita national income and it is situated next door to one of the largest markets on the African continent, also with a high level of per capita national income. It is also a member of several important trading agreements including SACU and bilateral agreements with other neighbors -- and has preferential access to European and North American markets under Lomé and GSP.

7.58 Current industrial development strategy has tended to focus on labor intensive manufacturing industry. It is the contention of this report that, although this will remain an important focus of attention for generating employment opportunities for large numbers of unskilled laborers, that this focus should now be somewhat broadened. In addition, the pressing need to generate large numbers of unskilled job opportunities to reduce unemployment levels is now less evident. Consequently, in addition to promoting labor intensive manufacturing industries, efforts should also be made to promote capital intensive manufacturing industries, service industries, niche markets, downstream processing industries and any other industrial activities that will help to diversify and broaden the nation's economic base.

7.59 Within the service sector, potential areas for development could include:-

(a) On line transactions, postal re-expediting, computer programming, medical services and grain storage.

(b) Financial services to the region, including banking services, insurance and re-insurance services, and back office operations such as cheque clearing.

(c) Off-shore banking and the development of other international financial management services including custody services, portfolio investment, insurance and holding company operations.

7.60 To support the development of the service sector in Botswana it will be necessary for education and training policies to focus on particular skills, notably computing skills, which may currently

not be available in adequate supply to meet the needs of this sector. Nonetheless, computer skills training in Botswana has progressed relatively rapidly over the past decade.

7.61 Although the potential for the development of downstream processing activities may be limited, all possibilities should be encouraged and pursued. Downstream processing activities for Botswana include: (a) leather, (b) game skins and meat products, (c) timber products, (d) diamond cutting and jewellery manufacturing, (e) soap manufacturing, (f) veld products and horticultural products, and (g) cotton. Within this group, diamond cutting/jewellery manufacturing, veld products and horticultural products, and cotton, appear to have the best chances of making a substantial contribution to the industrial development process.

7.62 The development of tourism -- another service industry -- is an activity which should also be encouraged. Tourism development confers special advantages, including the employment of people in remote rural areas where other forms of employment are unlikely. To become an effective industry, however, it will be necessary for the Department of Tourism to operate with a modicum of independence from the Ministry of Commerce and Industry, so that it can effectively promote this sector. Close coordination between HATAB, BOCCIM and the Tourism Department will also be important to ensure that tourism development is to the benefit of all parties concerned.

CHAPTER 8

CONCLUSIONS, PRIORITIES AND TRANSITION STRATEGIES

8.1 The main conclusion of this study is that industrial development in Botswana has been very rapid -- and that it has been particularly successful in meeting the Government's twin objectives of generating employment opportunities and diversifying the economic base. While many African countries experienced a decline in manufacturing output, and low capacity utilization, Botswana enjoyed rapid growth and high capacity utilization. This was in response to rapidly growing incomes, strong domestic demand, the availability of foreign exchange to purchase imported raw materials, and a favorable political setting. A wide range of manufacturing firms have been able to operate at high capacity -- with the major constraint on further development being a shortage of serviced factory space.

8.2 In the 1990s, however, several important developments are taking place which will impact upon future growth. The first of these is a lower rate of growth in the domestic market anticipated over the NDP 7 plan period -- including a transition from a surplus Government budget to a deficit budget situation. The second is potentially dramatic changes in the external environment. The future of the long established customs union agreement with South Africa is unknown, and the future political and economic direction of countries in the region is in a state of flux. In the broader international sphere, rapid increases in manufacturing productivity are combining with new trading arrangements, and new sources of supply from Asia and Eastern Europe, to create highly competitive markets.

8.3 With a small internal market, many firms in Botswana are rapidly reaching the stage where they need to access international markets if they are to continue to grow. The required standards of competitiveness are therefore those of the regional and international markets and not those of the relatively easy and affluent domestic market. The pressure to increase productivity and competitiveness will consequently increase substantially.

8.4 The next stage of industrial growth will probably, therefore, be more difficult. The first stage of industrial expansion, carried by a wave of high income from the resource industries, responded primarily to domestic demand and to domestic requirements to absorb large numbers of unskilled workers at relatively high wage rates. The next stage will require industry with higher productivity, lower labor intensity, and higher skilled employees -- if it is to meet the competitive pressures in domestic and international markets. The challenge therefore, is to define a pattern of development -- and corresponding policies -- that will respond to both the need for competitiveness and the need to employ a large and increasingly skilled labor force.

8.5 In addition, the need to skew industrial incentives solely to the development of labor-intensive manufacturing industry is less clear than it was in the past. Available information on unemployment presents a relatively healthy position -- despite the recent adverse consequences occasioned by the international recession. Although it will remain important for Botswana to continue encouraging such industries for the benefits of employment generation and skills acquisition which they provide to large numbers of unskilled laborers entering the work force as a result of natural population growth and continuing rural-urban migration, there is increasingly a need to encourage alternative types of industrial development. In addition, within the context of an enclave, natural resource driven economy which has catapulted Botswana from the ranks of the least developed nations to a middle income developing country -- one of the richest in per

capita national income terms in Sub-Saharan Africa -- exclusively pursuing labor intensive manufacturing industry may, in fact, be working against Botswana's comparative advantages.

8.6 Consequently, in addition to providing continued incentives for the development of labor-intensive manufacturing, serious consideration should be given to encouraging alternative types of industrial development. Increasingly, Botswana should focus its attention on increasing the quality and the value added of the output from the industrial sector -- to better reflect its position as a middle income developing country. This implies a concentration of effort on improving the quality and the productivity of the country's human capital base so that it can better operate in higher-level industrial activities -- including service industries, down-stream processing of goods produced in Botswana, and even non-labor intensive manufacturing activities. Important strides have already been made in improving the human capital base, and are expected to continue at a rapid pace over the NDP 7 plan period.

8.7 The recommendations of this report are therefore based upon two important premises. The first, is that Botswana no longer has a strong rationale for skewing industrial incentives in the direction of labor intensive manufacturing industry -- although opportunities in this area will continue to remain important for the foreseeable future. This implies that incentives should be provided on a broader basis to all types of industrial activity. Encouragement should be given to all industrial activities in which Botswana might be expected to compete on a sustainable basis. The second, is that the delivery mechanisms for industrial incentives should increasingly move away from a case-by-case approach -- to a more transparent and uniform system. This has the advantages of establishing well known, and advantageous, ground rules for all players, while helping to remove some of the rent seeking activities and potential scope for bribery, which is possible within the current system.

8.8 The following three sections outline the report's specific recommendations with respect to the trade environment, the enabling environment, and the new incentive structure. There is a short concluding note on the transition strategy which discusses priorities and sequencing for industrial sector reform.

A. THE TRADE ENVIRONMENT

8.9 Botswana is likely to face a major change in its existing trading relationships -- which have been well established and relatively stable under the terms of the Southern African Customs Union Agreement for a long period of time. With imminent political change in South Africa the future direction of SACU can only be the subject of speculation. Nonetheless, it is recommended that Botswana must:

(a) make a concerted effort to exercise an effective voice in the formulation of new rules for regional trading relationships, and

(b) develop a better understanding of the industrial development problems and policies of other countries in the region, and anticipate opportunities for more productive economic interactions.

8.10 The policy agenda within Botswana should be oriented towards the establishment of greater clarity regarding Botswana's national interest with respect to:

(a) future institutional arrangements governing international trade and foreign investment;

(b) the economic relationships to be developed with the other countries comprising the Southern Africa region; and,

(c) the domestic economic policy framework required to guide progress towards the country's industrial development objectives.

B. THE ENABLING ENVIRONMENT

8.11 Future macroeconomic policies will need to ensure and, in fact, intensify the provision of an appropriate enabling environment for industrial development. Specifically the Government will need to intensify efforts to build on Botswana's existing advantages; promote a better balance between wages and productivity; provide adequate land for industrial purposes; ensure that industrial finance is available; foster the development of capital markets; ensure that interest rates are positive in real terms; appropriately determine the value of the exchange rate; loosen the constraints which have been imposed by the regulatory environment; to the extent possible, lessen the constraints to industrial development through, for example, changes in policy with respect to the utility parastatals; and redefine the role of the Ministry of Commerce and Industry.

8.12 To assist in this process, it is recommended that the Government's management of industrial development should be based upon "management by exception" procedures. This would permit the Government to concentrate its efforts in sensitive areas while liberalizing in other areas. This method streamlines Government involvement by using the concept of the "negative list". This procedure could be used in the area of industrial licensing, regulation of the employment of foreign workers, and in the provision of land for industrial development.

Building on Existing Advantages

8.13 Botswana should clearly recognize its existing advantages and build upon them further. The current investment environment has much to recommend it to potential foreign investors. Political stability and democracy are rare in Africa and yet Botswana offers both of these attractions. It also has experienced continuous rapid growth, it has a high level of per capita national income and it is situated next door to one of the largest markets on the African continent, also with a high level of per capita national income. It is also a member of several important trading agreements including SACU and bilateral agreements with other neighbors -- and has preferential access to European and North American markets under Lomé and GSP.

Wages and Productivity

8.14 As an important determinant of foreign investment, it is necessary to ensure that real wages are brought into a better alignment with productivity. As a major wage setter within the economy, the Government should ensure that salary increases for civil servants are not above the level of price inflation -- and preferably at a lower level to take account of normal creep within the salary structure.

8.15 In addition, rather than fixing minimum wages at a level which makes Botswana uncompetitive in terms of labor costs and productivity, and then providing subsidies through FAP to help reduce this distortion, a preferable policy would be to eliminate the minimum wage. Allowing wages to be determined by market forces may lead to higher overall levels of employment and eliminate the cost and inefficiency associated with the extension of FAP grants to medium and large scale firms. Current minimum wages merely protect the living standards of the currently employed against the currently unemployed. Abolishing minimum wages would not affect existing wage agreements, but could encourage employers to introduce productivity-related wage incentive schemes.

8.16 If such action is not possible, for social and political reasons, the authorities should investigate alternative methods of reducing minimum wage levels in the industrial sector. Such alternatives could include:

(a) collapsing the minimum wage structure to one single minimum wage at the lowest rate (established for night watchmen);

(b) exempting manufacturing industry from minimum wage requirements -- as rural and domestic workers are currently exempted;

(c) passing on less than full cost of living increases to minimum wage earners to ensure the gradual erosion of the real level of salaries.

8.17 At the same time, it will be important to increase productivity levels within the economy. This will partly be made possible by the on-going effort to enhance the skills of the labor force -- through educational and private and public vocational training programs -- as well as continued on-the-job training. As many Batswana are first generation workers in the formal sector, increases in productivity will require time and good management supervision. Nonetheless, every effort should be made to improve productivity by the introduction of schemes such as piece rate systems which reward workers based upon their effort -- and changes should be made to existing legislation to ensure that these can be utilized as fully and effectively as possible.

8.18 Last, the National Productivity Center will have an important role to play in measuring productivity, providing comparisons with countries in the region and more widely throughout the world, and helping to make recommendations on training and other actions which can be implemented to increase the efficiency and effectiveness of Batswana workers.

Land for Industrial Development

8.19 The availability of land and housing is a major constraint which will continue to be an impediment to industrial development despite the implementation of the Accelerated Land Servicing Program. It is imperative, therefore, that the Government should continue to ensure that serviced land is made available for residential, commercial and industrial purposes. This process could, in part, be accelerated through the greater involvement of private sector developers in these markets. The Botswana Housing Corporation should also gradually move out of the housing rental business and redefine its role within the context of a deregulated market in which the Government is no longer a major landlord.

8.20 If the problem of industrial land is to be adequately addressed, then it should be dealt with in a completely separate manner from other types of land in Botswana. There is an urgent need for planners to plan for industrial land development well beyond the current 20 year planning horizon. Large industrial zones should be demarcated in urban areas and access to this land should be extended to all investors, both local and foreign. It should be made available to investors on the basis of, at least, a 50 year lease and should be transferable for alternative industrial uses. Taxes on industrial land should be designed in such a way that they encourage the development of the land for industrial purposes rather than having it remain idle for purely speculative reasons. Under the existing ALSP, the Government should also give higher priority to the development of industrial land -- specifically in Gaborone. Last, a Land for Industry Committee should be established (or created from existing committees) in the Department of Town and Regional Planning within the Ministry of Local Government, Lands and Housing, to assist the planning process for industrial land. This committee should be comprised of high level representatives from the relevant ministries and should be charged with determining the long term demand for industrial land.

Finance for Industrial Development

8.21 As the Government budget moves into deficit during the NDP 7 plan period, domestically generated, private sector financial resources will become an increasingly important source of financing for the economy. Hence, the banking system must be encouraged to mobilize more resources from the household sector. As the ability of the banks to perform this role is crucially linked to the rate of return on financial sector savings, deposit interest rates must be increased to positive real levels relatively quickly.

8.22 The current excess demand for long term finance in Botswana is partly a consequence of negative real rates on lending. To move the demand for long term funds into better balance, interest rates on lending should increase to positive real levels. This will more appropriately measure the real effective demand for long term finance, and provide the authorities with a better picture of the extent to which this demand is not being met by the existing financial system -- rather than measuring the artificially high demand generated by a negative cost of capital.

8.23 Once positive real lending rates have been achieved, the Government can monitor the true demand for long term financial resources against the availability of long term credit in the economy. Should the availability of long term capital continue to be a problem, even after attaining positive real rates of interest, then consideration should be given to developing appropriate mechanisms for channelling long term Government resources to the economy, on a fully commercial basis. The Government is currently reviewing possible options in this area in conjunction with the World Bank.

8.24 The recent development of the stock market is an important step in the deepening of the financial markets, and recent moves to encourage companies to go public should be continued. It will also be important for the Government to move to positive real PDSF/RSF interest rates to encourage the further development of additional debt and equity instruments -- and related secondary market trading.

The Regulatory Environment

8.25 Despite positive developments over the recent past, the regulatory framework requires further improvement. The bureaucracy surrounding work and residence permits for expatriates continues to be slow; the waiver system is still not operating adequately; the priority processing of work and residence permits for "critical occupations" is not yet operational; and, there is a lack of efficiency in the departments responsible for the allocation of land. These issues must be urgently addressed. In addition, there is a need to monitor the industrial and commercial licensing system, which has recently been substantially streamlined, and ensure that the redrafted Employment Act meets the needs of a pro-active industrialization policy.

8.26 With respect to work and residence permits for expatriates, it is recommended that the Government move toward a more targeted immigrant labor control system, similar to schemes used in the more developed countries. Under such schemes, positive occupation lists are used, and entry for individuals with qualifications identified on that list, is reasonably free.

The Legislative Environment

8.27 The amended Employment Act (1982), Trade Disputes Act (1982) and Trade Union's and Employers' Organizations Act (1983), which has been approved by Parliament, should be brought into effect as quickly as possible -- to provide an adequate collective bargaining machinery for employees and employers. The plan to establish an industrial court to arbitrate on labor related grievances and disputes should also be carried through quickly, and guidelines for the court should be agreed.

Utilities and Utility Pricing

8.28 Utility prices in Botswana are high compared to neighboring countries. This is partly due to price subsidization in those countries, but also due to the high cost of production and the low economies of scale which can be achieved in the production of such services in Botswana.

8.29 Part of the industrial policy debate has focussed on whether utility prices should be subsidized to help reduce this constraint. This report has argued that attempts should not be made to subsidize utility costs to make them comparable to levels in neighboring Southern African countries. Alternatively, the Government should emphasize efficiency in the operation of the utility parastatals to ensure that costs are kept as low as possible within the relatively high cost environment in which they operate -- possibly by the establishment of a parastatal monitoring unit within the Ministry of Finance and Development Planning.

8.30 In addition, wherever possible, the utility companies should examine the feasibility of meeting future increases in demand by importing low cost utility services from neighboring countries. Although this will not be possible for all utility services, it is certainly possible for some. For example, the Southern African region is a relatively low cost producer of electricity and several neighbors have the capacity to export to Botswana. The importation of lower cost sources of electricity would make it possible to bring Botswana's electricity costs more in line with electricity costs and prices in the region.

Role of the Ministry of Commerce and Industry

8.31 In the 1990s, the role of the Ministry of Commerce and Industry will have to change in fundamental ways. Whereas it has had responsibility for the two potentially conflicting objectives of licensing and regulating industry and promoting and encouraging industry, in a new industrial environment it should be the latter role which assumes prominence within the "new" MCI. Careful consideration should be given to ways in which it can most effectively carry out this new role.

8.32 One useful contribution it could make to the industrial development process is to assist the Government in taking a more pro-active stance in ensuring an on-going dialogue between the public and private sectors. Specifically, it should be at the forefront of analyzing any outstanding recommendations made at the Francistown seminars and implementing those that Government considers appropriate.

C. THE NEW INCENTIVE STRUCTURE

8.33 As indicated, the new incentive structure should be based, as much as possible, on two important principles. The first, is that industrial incentive packages should not attempt to bias industrial development in a particular direction or location. Every effort should be made to encourage all activities. Whereas past policy has emphasized labor-intensive manufacturing industry, the rationale for this particular bias, is now less obvious. Although such activities are likely to remain important for the foreseeable future for their impact on creating employment opportunities for unskilled workers -- this should not be at the expense of other types of industrial development. The second is that the incentive mechanisms should move away from the current system of case-by-case incentives which encourages an environment of rent-seekers. Incentives should be transparent and automatic and should apply uniformly to all industrial sector participants.

The Financial Assistance Policy

8.34 In line with the principles enunciated above, it is recommended that FAP should be eliminated for medium and large scale enterprises. These schemes permit potential abuse and fraud, do not necessarily lead to increases in labor productivity within the scheme's time frame, and may well lead to the development of uncompetitive companies after the expiration of the benefits package. It is also questionable whether FAP should be trying to promote medium and large scale investments in rural areas, and whether FAP should have a labor intensive bias. The encouragement of industries in the most economically attractive locations, uninfluenced by the distortions that subsidies may produce, as well as the removal of the temporary subsidy for labor utilization, will ultimately lead to a more efficient industrial sector with a greater potential for long term viability.

8.35 The FAP training grant should be retained, but substantially modified. Given the obvious need to improve skill levels in Botswana, it is recommended that the grant should be extended to all enterprises (including services) and should cover up to 75 percent of allowable training costs. Given the importance of management supervision in increasing labor productivity, the training grants should be extended to cover the training of citizen supervisory and management personnel. As much as possible, training grants should be provided on an automatic

basis and, where possible, should also be extended to cover defined on-site training activities. However, as training subsidies can also be wasteful, it will be important for the Government to carefully monitor these to ensure that they are cost effective in terms of increased worker productivity.

8.36 FAP should only remain in its current form, for small scale, citizen owned enterprises. This is discussed more fully below.

The Selebi-Phikwe Regional Development Program

8.37 The removal of FAP for medium and large scale enterprises will also remove many of the existing attractions of the Selebi-Phikwe program of incentives. It is further recommended that the unique attractions of the Selebi-Phikwe program should be removed, and more general incentives provided to the entire Botswana economy to provide a "national investment promotion strategy". These benefits should apply country-wide and without time limits. In as much as Selebi-Phikwe retains any special advantages, these may be in the form of providing "Export Processing Zone" status. However, a decision to confer such status should only take place after due consideration of its full implications, combined with an examination of the success of EPZ's in other countries.

The Taxation Environment

8.38 In place of the FAP benefits, and in conjunction with the above recommendations on wages, a low tax on corporate profits should be established for all corporations operating in Botswana.

8.39 At the same time, tax policy should be overhauled to eliminate the large number of tax exemptions, holidays and allowances which have been granted. Only the mining sector should continue to be taxed differently from other sectors in the economy -- due to its unique profitability and importance in the economy. Corporate tax levels should be reduced to a lower level in combination with the removal of all exemptions. Given current high levels of effective taxation, combined with low collections, it should be possible to implement this program in such a manner that it actually increases tax receipts while providing a powerful incentive to foreign investors to enter the Botswana market. In any case, at the current time, there is a less pressing need to collect income taxes for fiscal reasons.

8.40 If it were not possible to reduce tax levels to a level which was sufficiently low to attract potential investors, then the Government may wish to consider (either alternatively, or in addition to a generally lower tax rate) the introduction of special tax incentives for specialized sectors -- such as manufacturing or non-traditional exports. However, as this would go against the guiding principle of uniform incentives, it is considered a less desirable outcome.

8.41 Given the impact of tax policy on all sectors of the economy, its importance for fiscal policy, and the fact that the entire tax system has not been subject to external review for some time[1], it is highly recommended that the authorities should give serious consideration to the establishment of a Taxation Commission to review tax policy in a holistic context.

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[1] The last time the entire tax system was reviewed was by an external Fiscal Review Team in 1970.

The Small Scale Sector

8.42 Given the economic, social and political importance of the small scale sector, it is highly desirable that the Government should continue to support the activities of small scale citizen investors. This support should not come from restricting markets and the activities of foreign investors, but rather through intensified programs to help develop entrepreneurial, technical and business skills and the preparation of projects for financing.

8.43 In this regard, it is recommended that FAP benefits should remain for small scale enterprises -- and should be broadened to include service industries. In addition, the definition of the small scale sector should be adjusted upward, to take into account the impact of inflation since the upper size limit was last determined. In addition, as FAP assistance would no longer be available to the medium scale sector, it may be desirable to increase the upper limit further to include some of the smaller of the medium scale enterprises which were previously eligible for FAP assistance. A limit of P100,000 (total fixed investments), which is periodically revised in light of inflationary trends, may be appropriate, but would be subject to internal review within Botswana. Establishing an appropriate upper limit could form part of the terms of reference of the FAP review which is scheduled for 1993.

8.44 Given the high failure rate of small scale FAP projects, evaluation, monitoring and follow up work would need to be substantially enhanced within the Government -- possibly by diverting personnel previously involved on medium- and large-scale FAP projects. Continued assistance through the provision of small scale factory shells may also be appropriate.

8.45 Availability of finance may continue to act as a constraint on the development of this sector. During the current difficult period at the National Development Bank, Tswelelo should be developed as the chief source of financing for the small and medium scale enterprise sector. Tswelelo's past track record has improved considerably and further efforts should be made to bolster its strengthened position. It is important to note that financial support for SMEs in Botswana has been reasonably good within a wider African context.

Investment Promotion Activities

8.46 The Trade and Investment Promotion Agency (TIPA) should be removed from the Ministry of Commerce and Industry and reformulated as an independent parastatal. It should be allowed to develop as a true "one-stop" services center such as the Mauritius Export Development and Investment Authority (MEDIA) and Hong Kong's Trade Development Council (TDC). Ideally an independent institution should be supported by independent sources of funding and aid donors may be amenable to providing some initial support -- as they have done in other developing countries. Nonetheless, it is recognized that TIPA is likely to remain largely dependent upon Government sources of funding for some time to come. This less than ideal situation should be altered over time to have TIPA's functions funded on a fee basis.

8.47 If it were not possible to establish TIPA as an independent parastatal agency, it could still be made to operate more effectively, if it were given substantially more autonomy within the Ministry of Commerce and Industry and access to additional financial resources to carry out its promotional functions. However, this is considered less desirable, and likely to be less effective, than providing the type of autonomy outlined above.

8.48 In addition, investment promotion in Botswana will need to have a strategy, an institutional structure, and good management. It should target sectors in which it wishes actively to promote foreign investment and also the regional markets from which it intends to draw foreign investment. With respect to targeting of regional markets, it is recommended that South Africa, and possibly other countries in the region such as Zimbabwe, should be major targets for investment in Botswana. Thereafter the newly industrializing countries could be a secondary target, followed by investors from Europe, the United States and Japan. Investment promotion should build Botswana's image, directly attempt to generate more investment, and provide crucial investor services.

The Botswana Development Corporation

8.49 With respect to the Botswana Development Corporation, it is recommended that it should: (a) accelerate the spin-off of its companies either into the Sechaba Investment Trust, through direct sales of shares by Stockbrokers Botswana, or by public issues; (b) it should pursue its strategic plan goal of equity and loan investments in the order of 35 to 65 percent; equity investments in new projects should be limited to 49 percent and reduced as quickly as possible thereafter; (c) explore ways of improving flexibility in reducing equity contribution and collateral requirements, given the basic requirements of project viability and significant sponsor involvement.

Bonded Warehousing Facilities

8.50 Given the advantages that they confer on exporters, and the potential for attracting additional investors, a bonded warehouse scheme should be permitted for any company which may request such services. Under such an arrangement, duty would only be payable on those inputs which are placed in bond and subsequently used in the production of goods sold in the local (SACU) market. Duties would become payable at the time of shipment of the finished good.

D. THE TRANSITION STRATEGY

8.51 Movement to a new system of industrial incentives will require the development of a transition strategy. For example, current FAP recipients, and investors operating at Selebi-Phikwe must continue to receive the benefits which have been promised. It will also be necessary to establish some date in the future, after which no further new benefits will be provided under these two arrangements -- to allow for business people who have been planning on the basis of receiving FAP and/or developing at Selebi-Phikwe to follow through on their plans. It should not be necessary to make this transition period longer than twelve months. This would imply that FAP recipients would remain in the system for a six year period (a one year transition plus the five years of FAP benefits), after the decision to move to an alternative incentive structure.

8.52 During such a transition period, priority should be given to addressing the "enabling environment" issues discussed above. Most importantly, the Government should give priority to pursuing actions that will enhance the productivity of labor -- such as introducing piece rate systems on a wider basis, addressing the industrial land issue as a matter of urgency, and moving forward on the various regulatory constraints which adversely impact upon industrial

development. At the same time, the Government will need to be diligent in pursuing a policy which seeks to bring minimum wages more into line with productivity.

8.53 Over the twelve month transition period the Government should also devote its attention to designing the details of the most appropriate incentive structure -- reviewing the extent to which it can reduce the corporate tax rate, within the confines of fiscal policy. As indicated, it may also need to give consideration to special incentives to encourage particular activities -- such as the manufacturing sector and non-traditional exports -- if overall tax rates could not be brought down to a level which would be sufficient to attract additional investment in the sector.

ANNEXES

Table 1: GDP by Type of Economic Activity
(current prices)

	1980/81	1981/82	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88 (Prov)	1988/89 (Prov)	1989/90 (F/est)	1990/91 (F/est)
GDP (pula million)											
1. Agriculture	109.1	113.0	101.7	103.5	118.8	132.4	143.9	268.0	300.8	334.5	361.3
2. Mining	241.3	201.6	366.6	466.4	753.1	1133.9	1229.8	1652.3	2832.3	2762.5	2873.0
3. Manufacturing	47.3	69.9	77.4	80.6	86.6	124.2	167.9	177.8	221.3	247.9	276.9
4. Water & Electricity	19.3	21.8	29.7	32.3	42.9	57.7	72.2	106.9	122.3	136.6	160.9
5. Construction	69.0	53.0	58.0	94.8	97.4	96.0	132.3	185.2	259.3	337.1	393.4
6. Trade, Hotels, Restaurants	168.3	182.1	205.0	245.3	268.7	319.9	384.1	464.4	568.4	774.3	983.0
7. Transport	21.8	25.0	37.6	41.4	49.7	66.5	59.1	97.9	117.1	137.0	175.6
8. Financial Institutions	53.8	63.4	72.0	87.4	112.0	145.2	167.4	201.1	255.0	288.6	354.3
9. General Government	135.0	156.3	191.5	224.6	274.7	325.7	428.3	562.9	685.1	998.4	1284.2
10. Soc. & Per. Services	27.2	32.7	37.5	43.5	55.3	66.7	81.5	102.8	118.4	137.2	166.0
Dummy Sector (2)	-17.6	-18.9	-23.9	-28.9	-30.6	-47.6	-56.7	-74.2	-94.3	-106.8	-117.5
GDP at Current Market Prices	875.5	899.9	1153.1	1390.9	1828.6	2420.6	2809.8	3745.1	5385.7	6047.3	6911.1
GDP (excluding mining)	634.2	698.3	786.5	924.5	1075.5	1286.7	1580.0	2092.8	2553.4	3284.8	4038.1
Percentage of Total											
1. Agriculture	12.5	12.6	8.8	7.4	6.5	5.5	5.1	7.2	5.6	5.5	5.2
2. Mining	27.6	22.4	31.8	33.5	41.2	46.8	43.8	44.1	52.6	45.7	41.6
3. Manufacturing	5.5	7.8	6.7	5.8	4.7	5.1	6.0	4.7	4.1	4.1	4.0
4. Water & Electricity	2.2	2.4	2.6	2.3	2.3	2.4	2.6	2.9	2.3	2.3	2.3
5. Construction	7.9	5.9	5.0	6.8	5.3	4.0	4.7	4.9	4.8	5.6	5.7
6. Trade, Hotels, Restaurants	19.2	20.2	17.8	17.6	14.7	13.2	13.7	12.4	10.6	12.8	14.2
7. Transport	2.5	2.8	3.3	3.0	2.7	2.7	2.1	2.6	2.2	2.3	2.5
8. Financial Institutions	6.1	7.0	6.2	6.3	6.1	6.0	6.0	5.4	4.7	4.8	5.1
9. General Government	15.4	17.4	16.6	16.1	15.0	13.5	15.2	15.0	12.7	16.5	18.6
10. Soc. & Per. Services	3.1	3.6	3.3	3.1	3.0	2.8	2.9	2.7	2.2	2.3	2.4
Dummy Sector (2)	-2.0	-2.1	-2.1	-2.1	-1.7	-2.0	-2.0	-2.0	-1.8	-1.8	-1.7
GDP at Current Market Prices	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
GDP (excluding mining)	72.4	77.6	68.2	66.5	58.8	53.2	56.2	55.9	47.4	54.3	58.4
Annual Percentage Change											
1. Agriculture	8.8	3.6	-10.0	1.8	14.8	11.4	8.7	86.2	12.2	11.2	8.0
2. Mining	0.7	-16.5	81.8	27.2	61.5	50.6	8.5	34.4	71.4	-2.5	4.0
3. Manufacturing	70.7	44.7	10.7	4.1	7.4	43.4	35.2	5.9	24.5	12.0	11.7
4. Water & Electricity	28.7	13.0	36.2	8.8	32.8	34.5	25.1	48.1	14.4	11.7	17.8
5. Construction	18.8	-23.2	9.4	63.4	2.7	-1.4	37.8	40.0	40.0	30.0	16.7
6. Trade, Hotels, Restaurants	13.9	8.2	12.6	19.7	9.5	19.1	20.1	20.9	22.4	36.2	27.0
7. Transport	27.5	14.7	50.4	10.1	20.0	33.8	-11.1	65.7	19.6	17.0	28.2
8. Financial Institutions	-8.3	17.8	13.6	21.4	28.1	29.6	15.3	20.1	26.8	13.2	22.8
9. General Government	34.2	15.8	22.5	17.3	22.3	18.6	31.5	31.4	21.7	45.7	28.6
10. Soc. & Per. Services	30.1	20.2	14.7	16.0	27.1	20.6	22.2	26.1	15.2	15.9	21.0
Dummy Sector (2)	18.9	7.4	26.5	20.9	5.9	55.6	19.1	30.9	27.1	13.3	10.0
GDP at Constant 1985/96 prices	13.5	2.8	28.1	20.6	31.5	32.4	16.1	33.3	43.8	12.3	14.3
GDP (excluding mining)	19.2	10.1	12.6	17.5	16.3	19.6	22.8	32.5	22.0	28.6	22.9

Source: Central Statistical Office, *Statistical Bulletin*, Volume. 16 No.'s 1 & 2 and *Bank of Botswana Bulletin*, Vol.10. No. 1.

Table 2: GDP by Type of Economic Activity
(constant 1985/86 prices)

	1980/81	1981/82	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88 (Prov)	1988/89 (Prov)	1989/90 (F/est)	1990/91 (F/est)
GDP (pula million)											
1. Agriculture	158.3	161.4	141.3	122.4	119.5	132.4	122.8	203.2	202.5	209.9	215.5
2. Mining	530.3	628.5	919.7	1,065.6	1,099.7	1,133.9	1,225.6	1,269.7	1,485.4	1,436.5	1,533.0
3. Manufacturing	100.6	125.6	115.4	119.9	95.5	124.2	146.4	168.8	177.9	186.4	198.7
4. Water & Electricity	28.1	29.2	28.9	35.8	43.2	57.7	63.9	73.1	82.3	84.2	91.3
5. Construction	116.4	83.7	68.3	105.1	108.1	96.0	111.4	131.6	171.4	188.2	201.9
6. Trade, Hotels, Restaurants	265.8	251.6	233.4	239.9	287.7	319.9	340.8	381.3	438.5	496.4	539.2
7. Transport	28.3	30.8	34.5	39.9	50.9	66.5	65.7	103.4	110.3	117.9	136.2
8. Financial Institutions	72.6	81.1	85.5	93.9	119.2	145.2	145.7	168.9	187.1	209.9	227.5
9. General Government	199.8	216.6	238.1	263.3	301.7	325.7	353.9	416.8	457.2	552.9	642.0
10. Soc. & Per. Services	35.0	39.9	47.8	47.7	58.6	66.7	74.2	86.1	89.9	91.7	98.1
Dummy Sector (2)	-24.1	-24.5	-28.7	-32.3	-32.2	-47.6	-52.5	-61.0	-70.0	-71.8	-69.8
GDP at Current Market Prices	1,511.1	1,623.8	1,884.1	2,101.2	2,251.9	2,420.6	2,597.8	2,942.0	3,332.6	3,502.2	3,813.6
GDP (excluding mining)	980.9	995.3	964.4	1,035.7	1,152.2	1,286.7	1,372.2	1,672.3	1,847.2	2,065.6	2,280.6
Percentage of Total											
1. Agriculture	10.5	9.9	7.5	5.8	5.3	5.5	4.7	6.9	6.1	6.0	5.7
2. Mining	35.1	38.7	48.8	50.7	48.8	46.8	47.2	43.2	44.6	41.0	40.2
3. Manufacturing	6.7	7.7	6.1	5.7	4.2	5.1	5.6	5.7	5.3	5.3	5.2
4. Water & Electricity	1.9	1.8	1.5	1.7	1.9	2.4	2.5	2.5	2.5	2.4	2.4
5. Construction	7.7	5.2	3.6	5.0	4.8	4.0	4.3	4.5	5.1	5.4	5.3
6. Trade, Hotels, Restaurants	17.6	15.5	12.4	11.4	12.8	13.2	13.1	13.0	13.2	14.2	14.1
7. Transport	1.9	1.9	1.8	1.9	2.3	2.7	2.5	3.5	3.3	3.4	3.6
8. Financial Institutions	4.8	5.0	4.5	4.5	5.3	6.0	5.6	5.7	5.6	6.0	6.0
9. General Government	13.2	13.3	12.6	12.5	13.4	13.5	13.6	14.2	13.7	15.8	16.8
10. Soc. & Per. Services	2.3	2.5	2.5	2.3	2.6	2.8	2.9	2.9	2.7	2.6	2.6
Dummy Sector (2)	-1.6	-1.5	-1.5	-1.5	-1.4	-2.0	-2.0	-2.1	-2.1	-2.1	-1.8
GDP at Current Market Prices	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
GDP (excluding mining)	64.9	61.3	51.2	49.3	51.2	53.2	52.8	56.8	55.4	59.0	59.8
Annual Percentage Change											
1. Agriculture	-9.8	2.0	-12.5	-13.4	-2.4	10.8	-7.3	65.5	-0.3	3.6	2.7
2. Mining	34.1	18.5	46.3	15.9	3.2	3.1	8.1	3.6	17.0	-3.3	6.7
3. Manufacturing	25.1	24.9	-8.1	3.9	-20.4	30.1	17.8	15.3	5.4	4.8	6.6
4. Water & Electricity	2.0	3.9	-1.3	24.2	20.5	33.6	10.8	14.4	12.6	2.2	8.5
5. Construction	-0.9	-28.1	-18.4	53.8	2.9	-11.2	16.0	18.1	30.3	9.8	7.3
6. Trade, Hotels, Restaurants	-6.2	-5.3	-7.2	2.8	19.9	11.2	6.5	11.9	15.0	13.2	8.6
7. Transport	2.9	8.5	12.0	15.9	27.4	30.7	-1.2	57.4	6.7	6.9	15.6
8. Financial Institutions	-18.7	11.7	5.4	9.8	26.9	21.8	0.3	16.0	10.7	12.2	8.4
9. General Government	13.5	8.4	9.9	10.6	14.6	7.9	8.6	17.8	9.7	20.9	16.1
10. Soc. & Per. Services	22.5	14.1	19.9	-0.3	22.9	13.8	11.3	16.0	4.4	2.0	7.0
Dummy Sector (2)	12.8	1.8	17.1	12.6	-0.4	48.0	10.3	16.2	14.7	2.7	-2.8
GDP at Constant 1985/96 prices	9.5	7.5	16.0	11.5	7.2	7.5	7.3	13.2	13.3	5.1	8.9
GDP (excluding mining)	-0.4	1.5	-3.1	7.4	11.5	11.7	6.6	21.3	10.5	12.2	10.0

Source: Central Statistical Office, *Statistical Bulletin*, Volume. 16 No.'s 1 & 2 and *Bank of Botswana Bulletin*, Vol.10. No. 1.

Table 3: Gross Domestic Product at Current Prices
(percentage)

	1980/81	1981/82	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88 (Prov)	1988/89 (Prov)	1989/90 (F/est)
I. GDP BY TYPE OF ACTIVITY										
Agriculture	12.5	12.6	8.8	7.4	6.5	5.5	5.1	7.2	5.6	5.5
Mining & Quarrying	27.6	22.4	31.8	33.5	41.2	46.8	43.8	44.1	52.6	45.7
Manufacturing	5.5	7.8	6.7	5.8	4.7	5.1	6.0	4.7	4.1	4.1
Electricity & Water	2.2	2.4	2.6	2.3	2.3	2.4	2.5	2.9	2.3	2.3
Construction	7.9	5.9	5.0	6.8	5.3	4.0	4.7	4.9	4.8	5.6
Wholesale & Retail Trade	19.2	20.2	17.8	17.6	14.7	13.2	13.7	12.4	10.6	12.8
Transport & Communications	2.5	2.8	3.3	3.0	2.7	2.7	2.1	2.6	2.2	2.3
Financial Institutions	6.1	7.0	6.2	6.3	6.1	6.0	6.0	5.4	4.7	4.8
General Government	15.4	17.4	18.8	18.1	15.0	13.5	15.2	15.0	12.7	16.5
Soc. & Per. Services	3.1	3.6	3.3	3.1	3.0	2.8	2.9	2.7	2.2	2.3
Dummy Sector (2)	-2.0	-2.1	-2.1	-2.1	-1.7	-2.0	-2.0	-2.0	-1.8	-1.6
TOTAL GDP (Output)	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
II. GDP BY EXPENDITURE										
Public Consumption	23.2	27.0	26.2	26.1	24.2	22.0	25.7			
Private Consumption (3)	52.6	57.0	48.8	44.2	42.9	37.3	35.1			
Increase in Stocks	5.6	9.8	2.3	2.1	3.9	-2.7	0.8			
Gross Fixed K Formation	35.0	33.8	27.8	24.3	26.5	18.9	23.8			
Export of Goods	53.1	47.6	61.7	63.6	58.8	71.8	65.4			
Imports of Goods & Services	-69.5	-75.2	-66.8	-60.3	-56.3	-47.3	-50.8			
TOTAL GDP (Expenditure)	100.0	100.0	100.0	100.0	100.0	100.0	100.0			
III. GDP BY INCOME										
Compensation of Employees	35.9	39.9	37.3	36.4	32.7	28.8	30.0			
Operating Surplus	34.6	28.4	32.5	34.1	43.1	50.0	46.4			
Consumption of Fixed Capital	15.4	17.7	18.5	17.5	15.1	14.4	15.3			
Total GDP (Income) at Factor Cost	86.0	85.9	88.3	88.0	91.0	93.1	91.6			
Indirect Taxes (Net)	14.0	14.1	11.7	12.0	9.0	6.9	8.4			
TOTAL GDP (Income)	100.0	100.0	100.0	100.0	100.0	100.0	100.0			

Source: Central Statistical Office, *Statistical Bulletin*, June 1991, Table 2.1B.

Table 4: Direction of Trade: Exports
(pula thousand)

Year	Common Customs Area	Other Africa	United Kingdom	Other Europe	U.S.A.	All Other	TOTAL EXPORTS
1980	25,899	32,947	8,242	239,506	81,805	2,037	390,437
1981	55,066	35,039	22,146	138,257	80,631	1,115	332,254
1982	52,951	61,694	53,891	239,655	55,775	3,581	467,546
1983	57,703	64,049	30,528	489,567	51,870	3,015	696,732
1984	75,768	34,109	17,862	650,248	70,021	10,626	858,635
1985	77,702	54,705	53,225	1,121,606	73,401	5,655	1,386,294
1986	91,066	97,047	59,632	1,361,671	3,688	8,409	1,621,512
1987	110,658	128,286	30,560	2,384,109	4,371	8,336	2,666,319
1988	144,766	215,553	30,578	2,274,674	7,134	8,522	2,681,228
1989	112,323	224,130	11,521	3,354,809	4,898	4,468	3,712,149
1984 Q1	17,579	10,594	1,156	113,190	16,418	1,126	160,063
Q2	22,102	9,003	7,893	213,753	18,409	1,933	273,092
Q3	19,469	10,868	6,791	156,034	18,118	1,367	212,647
Q4	16,619	3,644	2,022	167,272	17,077	6,200	212,832
1985 Q1	16,273	7,355	7,172	182,070	26,001	1,369	240,239
Q2	17,339	8,041	14,096	237,124	27,404	1,220	305,223
Q3	19,776	14,627	20,554	276,207	19 365	1,716	352,244
Q4	24,315	24,682	11,404	426,205	631	1,349	488,587
1986 Q1	19,018	22,409	5,157	251,192	513	1,297	299,587
Q2	24,629	23,038	30,838	376,630	729	1,954	457,819
Q3	23,724	27,012	16,816	336,021	787	2,830	407,190
Q4	23,695	24,587	6,821	397,827	1,658	2,328	456,916
1987 Q1	22,167	27,781	6,036	309,537	489	1,800	367,809
Q2	27,451	31,858	10,704	395,238	1,022	1,466	467,739
Q3	31,858	33,217	11,052	1,211,899	1,375	2,541	1,291,942
Q4	29,182	35,430	2,768	467,434	1,485	2,529	538,828
1988 Q1	31,653	40,278	2,847	342,621	1,214	1,926	420,540
Q2	35,085	58,153	10,755	632,788	2,151	2,596	741,529
Q3	39,817	49,472	8,456	571,426	1,998	2,397	673,566
Q4	38,211	67,650	8,519	727,839	1,771	1,603	845,593
1989 Q1	31,194	50,055	2,096	755,175	1,773	1,290	841,583
Q2	29,630	71,313	4,143	1,061,476	279	1,130	1,168,570

Source: Central Statistical Office, *Statistical Bulletin*, June 1991.

Table 5: Direction of Trade: Imports
(pula thousand, c.i.f. incl of duty)

Year	Common Customs Area	Other Africa	United Kingdom	Other Europe	U.S.A.	All Other	TOTAL IMPORTS
1980	466,585	36,061	7,299	5,822	16,266	4,327	536,359
1981	581,330	42,046	7,515	11,398	14,836	6,796	663,921
1982	608,838	44,751	16,000	12,273	11,550	10,440	703,852
1983	669,876	59,305	10,129	42,038	8,547	16,049	805,944
1984	698,116	78,200	27,637	58,521	16,540	13,919	892,933
1985	814,280	81,720	53,120	81,958	30,639	33,347	1,095,064
1986	1,021,532	101,161	32,836	82,147	37,805	55,798	1,331,279
1987	1,250,954	121,674	36,248	106,182	29,703	27,696	1,572,457
1988	1,681,488	152,418	132,991	90,145	49,827	65,336	2,172,206
1989	2,335,502	208,862	175,808	125,814	72,657	93.062	3,011,705
1984 Q1	156,648	16,080	2,850	9,954	3,524	3,235	192,291
1985 Q1	178,135	19,072	12,344	37,045	12,536	8,793	267,925
Q2	206,847	19,389	22,430	17,591	4,629	6,680	277,566
Q3	211,963	23,426	8,124	14,069	6,421	2,016	266,019
Q4	217,336	19,833	10,222	13,252	7,053	15,858	283,554
1986 Q1	215,652	20,441	12,421	18,374	10,473	4,849	282,210
Q2	254,942	21,767	5,945	19,665	4,514	8,050	314,883
Q3	268,485	27,547	8,393	21,824	19,828	8,001	354,077
Q4	282,453	31,406	6,078	22,284	2,990	34,898	380,109
1987 Q1	258,231	27,527	8,196	17,247	7,175	6,604	324,981
Q2	307,752	29,301	10,178	30,366	7,646	6,673	391,916
Q3	345,859	31,599	8,187	35,447	8,555	8,570	438,217
Q4	339,112	33,247	9,687	23,122	6,326	5,849	417,343
1988 Q1	365,308	28,414	9,780	19,839	15,853	24,336	463,530
Q2	386,961	32,069	19,455	19,697	15,962	11,013	485,157
Q3	424,706	41,934	72,957	32,674	8,316	9,201	589,788
Q4	504,513	50,001	30,799	17,935	9,696	20,786	633,731
1989 Q1	435,058	34,666	56,837	33,975	4,780	10,538	575,855
Q2	624,193	54,965	22,186	54,581	3,071	8,675	767,671

Source: Central Statistical Office, *Statistical Bulletin*, June 1991.

Table 6A: Imports by Principal Commodities
(pula thousand, c.i.f., inclusive of duty)

Year	Food Beverages & Tobacco	Fuel	Chemicals & Rubber Products	Wood & Paper Products	Textiles & Footwear	Metals & Metal Products	Machinery & Elect. Equipment	Vehicles & Transp. Equipment	Other Goods	TOTAL IMPORTS
1980	84,543	70,196	41,762	17,149	45,250	58,991	88,192	63,526	68,197	537,808
1981	94,344	84,068	51,639	20,795	61,123	76,557	108,818	82,484	84,093	663,921
1982	116,047	99,028	57,821	27,765	68,587	65,493	97,036	82,461	89,614	703,852
1983	153,879	102,079	67,197	28,044	75,120	79,213	103,192	93,214	104,007	805,944
1984	164,964	92,189	75,905	29,861	81,710	81,713	147,445	115,099	106,375	895,260
1985	191,664	126,463	88,764	35,310	88,648	100,941	185,060	150,051	128,282	1,095,184
1986	221,949	111,937	124,644	51,026	104,468	122,425	219,007	222,507	153,455	1,331,418
1987	262,493	113,608	153,345	72,819	137,829	148,542	260,218	242,905	180,696	1,572,455
1988	310,882	132,446	184,585	96,620	180,663	201,429	394,183	419,622	251,761	2,172,191
1989	301,078	141,212	252,445	127,303	233,006	420,369	698,324	467,681	378,193	3,019,612
1990	-	-	-	-	-	-	-	-	-	3,659,553(P)
1991										3,976,148(P)
1992										3,856,292(P)

Table 6B: Exports by Principal Commodities
(pula thousand, f.o.b.)

Year	Meat & Meat Products	Live Animals	Hides & Skins	Diamonds	Copper Nickel Matte	Textiles	Soda Ash	Other Goods	TOTAL EXPORTS	Meat Diamonds & Copper
1980	28,166	126	3,031	235,733	80,768	15,641	-	25,554	390,437	344,667
1981	60,461	124	4,552	136,499	79,703	16,020	-	36,631	332,254	276,663
1982	79,499	228	7,098	246,433	64,514	27,368	-	45,584	467,546	390,446
1983	79,059	222	5,653	459,244	65,805	32,989	-	49,080	696,732	604,109
1984	62,403	138	11,179	615,896	68,271	41,274	-	57,916	857,076	746,570
1985	97,548	317	11,686	1,048,116	119,870	28,934	-	77,813	1,384,284	1,265,534
1986	120,091	319	10,176	1,202,414	121,052	43,177	-	122,037	1,619,265	1,443,556
1987	83,908	828	7,019	2,251,408	118,214	59,216	-	144,078	2,664,671	2,453,530
1988	112,167	500	11,672	1,979,163	371,190	60,261	-	143,306	2,678,258	2,462,521
1989	133,240	659	15,623	2,860,866	471,902	79,752	-	180,559	3,742,602	3,466,008
1990	121,887	-	-	2,613,618	271,025	-	-	335,115	3,341,646(P)	3,006,531
1991	140,633	-	-	2,941,456	296,351	-	13,808	350,962	3,743,210(P)	3,378,440
1992	160,789	-	-	2,898,922	260,731	-	46,247	345,737	3,712,426(P)	3,320,442

Source: Central Statistical Office, *Statistical Bulletin*, June 1991, Tables 3.1A and 3.2A.

Table 7: Formal Employment by Sector and Economic Activity (1984 - 1991)

	1984 Aug	1985 Sep	1986 Sep	1987 Mar	1987 Sep	1988 Sep	1989 Mar	1989 Sep	1990 Mar	1990 Sep	1991 Mar	1991 Sep
Private & Parastatal	70,500	71,200	79,400	88,400	97,400	111,900	115,500	129,600	135,500	143,700	154,100	157,500
Agriculture	5,400	4,000	4,900	5,100	5,600	6,500	6,600	6,000	6,500	6,400	6,700	6,700
Mining	7,500	7,300	7,500	7,200	7,000	7,500	7,600	76,000	7,800	8,100	7,800	7,700
Manufacturing	9,500	9,900	12,200	12,900	14,700	16,400	18,100	22,200	23,300	34,300	26,000	26,300
Water & Electricity	2,000	1,900	2,000	2,100	2,200	2,300	2,200	2,100	2,100	2,100	2,500	2,500
Construction	11,100	11,500	13,700	14,600	16,900	22,200	23,900	27,200	29,300	31,000	33,800	34,000
Commerce	18,100	18,300	20,900	24,500	25,700	28,800	28,600	34,500	35,700	38,300	41,000	42,000
Transport	5,500	5,700	5,100	6,400	6,700	7,900	7,400	7,300	8,100	8,500	9,100	9,800
Finance	6,200	6,800	7,400	8,800	9,800	11,200	11,600	13,100	13,200	14,700	16,100	17,100
C&P Services*	3,500	3,900	4,000	4,900	6,600	6,700	7,400	7,500	7,300	8,200	8,600	8,900
Education	1,600	1,900	1,700	1,800	2,100	2,300	2,300	2,000	2,200	2,100	2,500	2,500
Sub-Totals - Private	n.a.	63,600	71,600	80,300	88,700	101,000	104,900	118,700	124,200	132,500	142,500	144,600
- Parastatal	n.a.	7,600	7,800	8,100	8,700	10,800	10,600	10,900	11,300	11,300	11,800	12,900
Central Government	32,100	36,800	41,300	41,900	42,500	47,200	48,900	49,300	51,700	52,500	55,500	57,500
Local Government	7,500	8,800	9,400	9,900	10,300	10,500	11,000	10,600	11,300	12,600	13,000	13,900
All Sectors	110,000	116,800	130,100	140,200	150,200	169,500	175,500	189,500	198,500	209,000	222,800	228,900

Note: Excludes working proprietors and unpaid family workers. All figures are rounded.

* C&P Services = Community and Personal Services

Table 8: Employment: Minimum Hourly Wage Rates
(thebe per hour)

Private and Parastatals	1980 Aug	1982 Aug	1983 Jul	1984 Jul	1985 Jun	1986 May	1987 May	1988 May	1989 May	1990 May	1991 May
Building, Construction Exploration and Quarrying	36	44	48	53	56	64	70	75	83	92	103
Manufacturing, Service & Repair Trades	36	44	48	53	56	64	70	75	83	92	103
Wholesale Distributive Trades	36	40	43	47	50	58	65	70	77	86	97
Retail Distributive Trades	36	40	43	46	49	56	62	66	73	81	91
Hotel, Catering & Entertainment Trades	36	44	48	53	56	64	70	75	83	92	103
Garage, Motor Trades & Road Transport	36	44	48	53	56	64	70	75	83	92	103
Retail & Wholesale Night Watchmen	26	30	32	35	37	50	55	59	65	72	81
Night Watchmen (excl Retail & W/sale)	26	34	37	41	43	50	55	59	65	72	81

(1) Correction for 1988.

Table 9: Gross Domestic Product by Sector/Formal Sector Employment Ratios
(1980/81 - 1990/91)

	1980/81	1981/82	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88 (Prov)	1988/89 (Prov)	1989/90 (F/est)	1990/91 (F/est)
ECONOMIC ACTIVITY - GDP BY SECTOR (pula mill., 1985/86 prices)											
1. Agriculture	158.3	161.4	141.3	122.4	119.5	132.4	122.8	203.2	202.5	209.9	215.5
2. Mining	530.3	628.5	919.7	1,065.6	1,099.7	1,133.9	1,225.6	1,269.7	1,485.4	1,436.5	1,533.0
3. Manufacturing	100.6	125.6	115.4	119.9	95.5	124.2	146.4	168.8	177.9	186.4	198.7
4. Water & Electricity	28.1	29.2	28.9	35.8	43.2	57.7	63.9	73.1	82.3	84.2	91.3
5. Construction	116.4	83.7	68.3	105.1	108.1	96.0	111.4	131.6	171.4	188.2	201.9
6. Trade, Hotels & Rest.	265.8	251.6	233.4	239.9	287.7	319.9	340.8	381.3	438.5	496.4	539.2
7. Transport	28.5	30.8	34.5	39.9	50.9	66.5	65.7	103.4	110.3	117.9	136.2
8. Finance & Buss. Serv.	48.5	56.6	56.0	61.6	87.0	97.6	93.2	107.9	117.1	138.1	157.7
9. General Government	199.8	216.6	238.1	263.3	301.7	325.7	353.9	416.8	457.2	559.6	642.0
10. Soc. & Per. Services	35.0	39.9	47.8	47.7	58.6	66.7	74.2	86.1	89.9	91.7	98.1
GDP AT MARKET PRICES	1,511.1	1,623.9	1,884.2	2,101.2	2,251.9	2,420.6	2,597.9	2,941.9	3,332.5	3,508.9	3,813.6
FORMAL SECTOR EMPLOYMENT											
1. Agriculture	4,800	4,200	4,500	5,400	4,000	3,500	5,100	6,600	6,600	6,500	6,700
2. Mining	7,300	7,100	7,200	7,500	7,300	7,500	7,200	7,300	7,600	7,800	7,800
3. Manufacturing	6,400	7,200	9,800	9,500	9,900	10,600	12,900	15,300	18,100	23,300	26,000
4. Water & Electricity	1,600	2,200	1,900	2,000	1,900	2,000	2,100	2,200	2,200	2,100	2,500
5. Construction	15,200	13,600	9,600	11,100	11,500	12,000	14,600	20,700	23,900	29,300	33,800
6. Trade, Hotels & Rest.	15,300	16,600	15,300	18,100	18,300	20,400	24,500	26,300	28,600	35,700	41,000
7. Transport	3,900	3,700	3,900	5,500	5,700	5,700	6,400	7,100	7,400	8,100	9,100
8. Finance & Buss. Serv.	4,900	5,700	6,000	6,200	6,800	7,300	8,800	10,100	11,600	13,200	16,200
9. General Government	32,600	34,400	37,300	39,600	45,600	49,000	51,800	56,500	60,700	63,000	68,500
10. Soc. & Per. Services	5,400	5,500	5,100	5,100	5,800	5,500	6,700	8,700	9,700	9,500	11,100
TOTAL EXCLUDING BDF	97,400	100,200	100,600	110,000	116,800	123,500	140,100	160,800	176,400	198,500	222,700
GDP/EMPLOYMENT (pula million per employee)											
1. Agriculture	0.0330	0.0384	0.0314	0.0227	0.0299	0.0378	0.0241	0.0308	0.0307	0.0323	0.0322
2. Mining	0.0726	0.0885	0.1277	0.1421	0.1506	0.1512	0.1720	0.1739	0.1954	0.1842	0.1965
3. Manufacturing	0.0157	0.0174	0.0118	0.0126	0.0096	0.0117	0.0113	0.0110	0.0098	0.0080	0.0076
4. Water & Electricity	0.0176	0.0133	0.0152	0.0179	0.0227	0.0289	0.0304	0.0332	0.0374	0.0401	0.0365
5. Construction	0.0077	0.0062	0.0071	0.0095	0.0094	0.0080	0.0076	0.0064	0.0072	0.0064	0.0060
6. Trade, Hotels & Rest.	0.0174	0.0152	0.0153	0.0133	0.0157	0.0157	0.0139	0.0145	0.0153	0.0139	0.0132
7. Transport	0.0073	0.0083	0.0088	0.0073	0.0089	0.0117	0.0103	0.0146	0.0149	0.0146	0.0150
8. Finance & Buss. Serv.	0.0099	0.0099	0.0095	0.0099	0.0128	0.0134	0.0106	0.0107	0.0101	0.0105	0.0097
9. General Government	0.0061	0.0063	0.0064	0.0066	0.0066	0.0066	0.0068	0.0074	0.0075	0.0089	0.0094
10. Soc. & Per. Services	0.0065	0.0073	0.0094	0.0094	0.0101	0.0121	0.0111	0.0099	0.0093	0.0097	0.0088
TOTAL	0.0155	0.0162	0.0094	0.0191	0.0193	0.0196	0.0185	0.0183	0.0189	0.0177	0.0171

Table 10: Employee Estimated Monthly Cash Earnings by Sector, Economic Activity and Citizenship

	1980 Aug	1982 Aug	1984 Aug	1985 Aug	1986 Mar	1986 Sep	1987 Mar	1988 Mar	1989 Mar	1990 Mar	1991 Mar	1980-91 127 mo.s	1980-86 67 mo.'s	1986-91 60 mo.'s
A. CITIZENS - PRIVATE AND PARASTATAL	140	167	216	244	248	279	285	307	350	396	463	12.0	10.8	13.3
Agriculture	48	45	66	64	70	88	92	88	117	138	212	15.0	7.0	24.7
Mining	186	249	315	350	396	465	488	523	504	688	765	14.3	14.5	14.1
Manufacturing	138	160	213	264	248	282	284	286	325	343	427	11.2	11.0	11.5
Water & Electricity	227	224	348	353	346	431	437	424	788	680	823	12.9	7.8	18.9
Construction	120	145	198	200	178	214	214	245	251	309	387	11.7	7.3	16.8
Commerce	106	128	169	186	207	200	215	237	282	313	353	12.0	12.7	11.3
Transport	202	199	243	274	239	315	318	409	568	588	689	12.3	3.1	23.5
Finance	211	244	318	369	382	457	454	476	535	654	740	12.6	11.3	14.1
C&P Services*	159	191	230	245	253	313	313	355	382	415	436	10.0	8.7	11.5
Education	199	340	295	338	368	446	490	552	618	816	724	13.0	11.6	14.5
Local Government	200	203	356	270	249	278	297	339	411	465	581	10.6	4.0	18.4
Sub-Total	146	170	230	247	248	279	286	310	356	402	473	11.8	10.0	13.8
Central Government	n.a.	n.a.	n.a.	298	358	388	364	426	526	575	701	n.a.	n.a.	14.4
TOTAL CITIZEN	n.a.	n.a.	n.a.	263	285	298	310	343	404	448	531	n.a.	n.a.	13.3
B. NON-CITIZENS														
Private & Parastatal	1,104	1,309	1,699	1,742	1,892	1,964	2,255	2,183	2,603	2,759	2,783	9.1	10.1	8.0
Local Government	803	879	1,072	1,099	1,137	1,193	1,025	1,371	1,387	1,765	2,130	9.7	6.4	13.4
Sub-Total	1,100	1,304	1,690	1,733	1,881	2,020	2,241	2,173	2,586	2,748	2,775	9.1	10.1	8.1
Central Government	n.a.	n.a.	n.a.	1,046	1,129	1,215	1,229	1,525	1,410	1,743	2,118	n.a.	n.a.	13.4
Total Non-Citizens	n.a.	n.a.	n.a.	1,593	1,731	1,817	2,046	2,037	22,334	2,564	2,655	n.a.	n.a.	8.9
C. ALL CITIZENS														
Grand Total	196	226	299	319	345	360	379	413	482	543	639	11.8	10.6	13.1

Notes: (1) Reclassifications and coverage changes have affected some of these comparisons over time.
(2) Seasonal influences have been identified in this first March survey compared to September surveys.
(3) 1980 - 1985 excludes Central Government.
* C&P Services = Community and Personal Services

Table 11: Prices - Cost of Living Index
(September 1985 = 100)

	Food	Drink and Tobacco	Clothing and Footwear	Housing Lighting & Fuels	Household Goods & Operation	Medical Care	Transport etc.	Other Goods	All Items Index	Annual Rate of Inflation	Urban Index	Rural Index
Weights	36.7	3.4	10.8	13.1	13.7	1.3	10.5	10.5	100.0	(%)	57.8	42.2
1985: Dec	100.4	100.0	101.5	100.1	101.4	100.2	101.8	100.5	100.7	10.4	100.7	100.8
1986: Dec	110.9	106.6	113.0	100.3	120.8	102.6	111.9	111.0	111.6	10.8	111.2	110.1
1987: Mar	113.3	107.8	115.6	100.4	122.9	104.4	113.9	113.8	113.6	9.9	114.5	112.4
Jun	116.6	113.3	121.7	106.0	126.8	108.3	115.4	115.8	117.6	9.4	119.4	115.1
Sep	118.9	113.8	125.9	108.2	128.9	108.4	117.1	117.0	119.6	9.8	121.9	116.4
Dec	120.0	116.3	129.6	109.2	127.6	109.3	118.9	118.5	120.6	8.1	122.6	117.8
1988: Mar	123.3	116.6	137.6	109.8	136.8	114.4	125.3	95.2	122.7	8.0	125.9	118.3
Jun	125.2	125.4	143.8	114.1	141.6	115.8	127.2	99.2	126.3	7.4	130.9	120.1
Sep	128.1	127.8	149.9	116.2	151.4	116.3	131.3	99.0	130.5	9.1	134.6	125.0
Dec	132.0	128.9	153.5	119.0	151.9	121.7	134.3	100.8	133.1	10.4	137.8	126.6
1989: Mar	133.5	141.6	158.8	123.6	158.3	129.5	141.5	105.3	137.4	12.0	142.8	130.0
Jun	137.5	149.8	165.8	129.8	163.4	132.6	142.2	107.8	142.1	12.5	148.2	133.7
Sep	141.1	151.3	165.5	132.4	166.2	134.7	148.8	109.4	145.1	11.2	150.8	137.2
Dec	144.8	151.7	170.4	132.6	174.4	132.2	149.9	110.2	148.2	11.3	154.3	139.8
1990: Mar	148.7	153.3	178.9	136.6	185.2	144.3	149.6	114.0	153.2	11.5	160.2	143.7
Jun	152.9	162.0	181.8	142.7	190.5	147.4	150.9	117.3	157.2	10.6	164.4	147.4
Sep	157.6	164.7	188.1	143.8	193.8	150.0	152.4	119.1	160.9	10.9	167.7	151.6
Dec	162.9	165.0	192.0	157.3	194.5	149.8	168.4	121.3	166.0	12.0	172.8	156.6
1991: Jan	165.4	166.3	193.3	156.6	197.2	150.8	166.1	126.9	168.2	12.0	175.4	158.4
Feb	165.7	167.3	194.9	157.1	198.5	151.5	167.2	128.5	168.9	11.3	176.4	158.7
Mar	166.1	174.0	185.7	157.9	201.0	152.7	170.6	129.1	170.5	11.3	178.4	159.8
Apr	167.3	180.1	199.0	163.3	201.9	152.8	164.0	131.1	172.3	10.7	181.3	160.0
May	168.8	182.8	201.2	163.3	202.5	153.2	164.6	131.6	173.4	10.8	182.4	161.1
Jun	170.0	187.2	202.0	163.1	205.1	154.0	164.9	132.9	174.7	11.1	183.4	162.8
Jul	171.4	187.3	203.7	163.3	205.8	154.5	172.6	132.9	177.0	12.0	186.4	164.2
Aug	173.9	188.0	206.4	163.3	208.2	155.4	174.3	133.3	178.7	11.9	187.8	166.2
Sep	176.8	187.5	210.6	163.7	211.0	155.8	175.2	133.8	181.0	12.5	190.3	168.3
Oct	178.7	193.6	213.1	163.9	212.2	157.2	177.6	135.0	182.7	12.6	192.5	169.1
Nov	181.8	196.6	216.1	164.0	215.5	157.0	179.0	135.3	185.0	12.3	194.3	172.2
Dec												

Petrol is included under "Transport".

Table 12: Weights in the Cost of Living Index
(1985 and 1991)

Sub-Groups	September 1985 = 100	November 1991 = 100
Food	36.9	27.0
(Drink and Tobacco	3.9	12.4
Total Food, Drink and Tobacco)	(40.8)	(39.4)
Clothing and Footwear	10.8	5.6
Housing	9.2	11.0
Lighting and Fuel	3.5	2.5
Furniture and Appliances	10.0	9.4
Household Operations	4.1	4.4
Health and Medical Care	3.8	4.5
Transport, etc.	10.5	13.1
Other Goods, etc.	7.3	10.1
ALL ITEMS	100.0	100.0

Table 13: Profile of the Formal Manufacturing Sector (1985 - 1991)

Product Group	Citizen Owned	Projected Employment	Joint Ventures	Projected Employment	Foreign Owned	Projected Employment
1. Meat and Meat Products	4	218	0	0	2	85
2. Dairy & Agro Based Products	42	1,046	27	845	37	1,552
3. Beverages	0	0	5	591	3	216
4. Textiles	19	602	32	885	44	2,436
5. Tanning and Leather Products	2	218	3	100	5	440
6. Chemical and Rubber Products	4	139	23	721	33	1,134
7. Wood & Wooden Products	12	647	9	238	17	508
8. Paper & Paper Products	9	222	6	63	13	323
9. Metal Products	43	1,151	21	801	40	1,482
10. Building Materials	50	2,358	14	576	15	850
11. Plastic Products	6	178	16	933	8	480
12. Electrical Products	6	282	9	512	11	1,096
13. Handicrafts	1	234	3	28	3	1,047
TOTAL	198	7,295	168	6,293	231	11,649

Source: Department of Industrial Affairs, Ministry of Commerce and Industry.

Table 14: Total Number of Manufacturing Licenses Issued (1985 - 1991)

Product Group	1985	1986	1987	1988	1989	1990	1991	TOTAL	Expected Employment
1. Meat and Meat Products	1	2	0	0	1	1	1	6	2,162
2. Dairy & Agro Based Products	10	15	16	17	14	3	16	91	3,288
3. Beverages	0	2	2	2	2	0	0	8	1,000
4. Textiles	4	13	22	24	6	7	19	95	7,277
5. Tanning and Leather Products	0	3	1	2	1	2	1	10	631
6. Chemical and Rubber Products	4	3	11	13	10	5	14	60	2,606
7. Wood & Wooden Products	4	4	7	6	4	6	7	38	1,593
8. Paper & Paper Products	3	6	1	5	3	3	7	28	1,158
9. Metal Products	7	20	17	15	17	13	19	108	4,720
10. Building Materials	4	10	7	14	12	11	27	85	4,410
11. Plastic Products	4	6	5	7	4	6	3	35	1,581
12. Electrical Products	2	5	4	4	3	4	4	26	1,055
13. Handicrafts	1	1	0	0	1	0	4	7	1,312
TOTAL	44	90	93	109	78	61	122	597	32,793

Source: Department of Industrial Affairs, Ministry of Commerce and Industry.

Table 15: Manufacturing Companies by Location (1985 - 1991)

Product Group	Gaborone	Lobatse	Selebi-Phikwe	Francistown	Others*	TOTAL
1. Meat and Meat Products	1	1	2	1	1	6
2. Dairy & Agro Based Products	23	7	8	11	42	91
3. Beverages	1	0	4	1	2	8
4. Textiles	39	9	5	16	26	95
5. Tanning and Leather Products	2	0	0	3	5	10
6. Chemical and Rubber Products	24	2	4	10	20	60
7. Wood & Wooden Products	8	0	5	9	16	38
8. Paper & Paper Products	11	4	1	6	6	28
9. Metal Products	24	1	14	12	57	108
10. Building Materials	18	8	1	8	50	85
11. Plastic Products	12	2	2	9	10	35
12. Electrical Products	13	0	1	6	6	26
13. Handicrafts	0	0	2	3	2	7
TOTAL	176	34	49	95	243	597

* Companies in rural and peri-urban areas.

Source: Department of Industrial Affairs, Ministry of Commerce and Industry.

Table 16: Export/Import Licenses Issued, by Location and Year (1985 - 1991)

LOCATION	1987	1988	1989	1990	1991	TOTAL
Gaborone	9	13	21	27	38	108
Francistown	1	1	5	3	4	14
Selebi-Phikwe	1	0	0	0	1	2
Lobatse	1	1	1	1	2	6
Tlokweng	0	0	1	0	3	4
Mochudi	0	0	0	1	1	2
Mogoditshane	0	0	0	0	1	1
Maun	0	0	0	0	1	1
Ramotswa	1	0	0	0	0	1
Jwaneng	0	0	0	0	1	1
Pilane	0	0	0	0	1	1
Palapye	0	0	0	0	1	1
Mahalapye	0	0	0	1	0	1
Molepolole	0	0	1	0	0	1
Pitsane	0	0	0	0	1	1
TOTAL	13	15	20	33	35	145

Source: National Licensing Authority, Gaborone.

Table 17: Export/Import Licenses Issued, by Location and Ownership (1987 - 1991)

LOCATION	Local	Joint	Foreign	TOTAL
Gaborone	30	43	35	108
Francistown	4	3	7	14
Selebi-Phikwe	0	1	1	2
Lobatse	3	2	1	6
Tlokweng	0	3	0	3
Mochudi	0	2	0	2
Mogoditshane	0	0	2	2
Maun	0	1	0	1
Ramotswa	0	1	0	1
Jwaneng	0	1	0	1
Pilane	1	0	0	1
Palapye	1	0	0	1
Mahalapye	1	0	0	1
Molepolole	0	1	0	1
Pitsane	0	1	0	1
TOTAL	40	59	46	145

Source: National Licensing Authority, Gaborone.

Table 18: Export/Import Licenses (Renewed and Operating), by Location and Year (1987 - 1991)

LOCATION	1987	1988	1989	1990	1991
Gaborone	9	22	42	65	90
Francistown	1	2	7	10	13
Selebi-Phikwe	1	1	1	0	1
Lobatse	1	2	3	4	6
Tlokweng	0	0	1	1	4
Mochudi	0	0	0	1	2
Mogoditshane	0	0	0	0	1
Maun	0	0	0	0	1
Ramotswa	1	1	1	1	1
Jwaneng	0	0	0	0	1
Pilane	0	0	0	0	1
Palapye	0	0	0	0	1
Mahalapye	0	0	0	1	0
Molepolole	0	0	1	1	1
Pitsane	0	0	0	0	1
TOTAL	13	28	56	84	124

Source: National Licensing Authority, Gaborone.

Table 19: Exporter/Importer Licenses (Renewed and Operating), by Ownership (as at December, 1991)

LOCATION	Local	Joint	Foreign	TOTAL
Gaborone	24	35	31	90
Francistown	4	3	6	13
Selebi-Phikwe	0	1	0	1
Lobatse	3	2	1	6
Tlokweng	1	3	0	4
Mochudi	0	2	0	2
Mogoditshane	0	0	1	1
Maun	0	1	0	1
Ramotswa	0	1	0	1
Jwaneng	0	1	0	1
Pilane	1	0	0	1
Palapye	1	0	0	1
Mahalapye	0	0	0	0
Molepolole	0	1	0	1
Pitsane	0	1	0	1
TOTAL	34	51	39	124

Source: National Licensing Authority, Gaborone.

CURRENT INDUSTRIAL INCENTIVE PROGRAMS IN BOTSWANA

A. FINANCIAL ASSISTANCE POLICY

1. Botswana enacted its Financial Assistance Policy (FAP) in 1982 in recognition of the need to generate employment opportunities and to diversify the economic base away from its reliance on diamonds and cattle. Specific objectives of FAP were to:

(a) create sustainable employment for unskilled workers;
(b) produce goods for export or to substitute for imports;
(c) diversify the economy to lessen dependence on large scale mining, beef exports, and growth of the public sector;
(d) improve citizen skill levels through training.

2. Given the emphasis on employment generation, FAP incentives were structured so as to encourage maximum employment of unskilled and semi-skilled workers. The FAP Capital Grant, for example, is based on the number of actual or projected employees, and the FAP Labor Grant on wages paid to unskilled and semi-skilled workers. FAP also seeks to achieve geographical diversification of industry by offering greater incentives to those companies locating in rural areas or in the Selebi-Phikwe region.

B. SMALL-SCALE FAP

3. The overall FAP program includes two distinct programs, one of which is targeted exclusively at small-scale, citizen-owned businesses, with a total fixed investment of P25,000 or less.

4. By the end of 1990, an estimated 1270 projects, 85 per cent of them in rural areas, had received FAP small-scale assistance. The cumulative total investment in these projects was about P9 million, of which some P3.6 million consisted of FAP grants. FAP small-scale assistance during 1982 to 1990 supported the creation of some 3800 jobs. Projects were concentrated in knitting and sewing, carpentry, bakeries, brick-making, and metal working.

5. It is difficult to say how many of these projects ultimately survived. The 1988 evaluation of small-scale FAP, conducted by the Ministry of Finance and Development Planning (MFDP), reported that, of a total of 747 small-scale FAP projects approved from 1982 to 1986, 142 failed or were cancelled. That report cautioned, however, and anecdotal evidence suggests, that the actual failure rate is likely to be much higher, and that some 50 percent of small scale enterprises fail. Although this may appear high, a 50 percent success rate among entrepreneurs with little or no prior business experience and a work force with minimal wage-earning experience is impressive. While small-scale FAP clearly will not provide the sole solution to Botswana's unemployment problems, it is providing necessary assistance to entrepreneurs and workers who otherwise would have few opportunities in the formal sector. When combined with the technical assistance provided by Integrated Field Services to small-scale enterprises, small-scale FAP appears to make a useful contribution to future industrial development.

C. MEDIUM AND LARGE-SCALE FAP

6. FAP assistance to medium-scale (total investment between P25,000 and P900,000) and

large-scale (total investment greater than P900,000) enterprises provides a wider range of grants and tax holidays, spread over the first five years of a project's operation, than is the case with small-scale FAP. It is intended to assist entrepreneurs who are assumed to have greater resources of capital and greater technical and managerial ability than those receiving small-scale FAP. Open to citizens and non-citizens alike, medium and large-scale FAP is, at least in part, an incentive to foreign businesses to invest in Botswana rather than in other countries. As such, it must be evaluated in comparison to other countries offering a combination of financial and tax incentives and economic and business conditions that compete directly with those Botswana has to offer. Like the small-scale program, medium and large-scale FAP offers greater incentives to projects in rural areas and the Selebi-Phikwe region, and calculates grants based on total employment and wages paid to unskilled and semi-skilled workers. Unlike small-scale FAP, it does not discriminate on the basis of sex.

7. In the first five years of FAP, to March 1987, 193 projects employing 3135 people had received medium and large-scale FAP assistance, with total disbursements of P9 million. Based on projections submitted with their FAP applications and approved by the FAP Committee, these projects would ultimately employ 7776 people, and would receive more than P30 million in FAP grants. Grants paid at the time of this evaluation had amounted to P2,870 per job created; this would increase, however, according to the projections, to P3,850.

8. By the end of 1990, 391 projects had received medium-scale FAP assistance and 5 had received large-scale FAP. A total of about P55 million in medium- and large-scale FAP grants had been disbursed, and another P40 million committed but not yet disbursed. Total employment in medium- and large-scale FAP projects was an estimated 16 000 as of June 1990. Total medium- and large-scale FAP commitments therefore have amounted to some P6,000 per job created. According to the 1992 Budget Speech, FAP-approved projects created some 3500 jobs in 1990, and were expected to create 5900 jobs in 1991.

D. FINANCIAL ASSISTANCE PROGRAM CAPITAL GRANT

9. Under Case-by-Case FAP Assistance (CFA), a grant of P1,000 per job created is paid to foreign-owned or joint venture companies, and P1,500 to 100 percent citizen-owned companies. This grant, which is based on projections submitted by the company to the FAP Committee, is paid before the project commences, and is intended to supplement borrowed funds and share capital invested by the project promoters. The capital grant is not paid to the firm in cash, but is used for the purchase of capital equipment, and is paid directly by the National Development Bank (NDB) to the equipment suppliers.

10. Perhaps no other element of the FAP program is so readily subject to fraud and misrepresentation. Since in most cases the suppliers of capital equipment are located outside Botswana, the potential for over-invoicing, shipment of machinery of lesser value than that indicated on the invoice, and other abuses is enormous, potentially involving collusion between the company in Botswana and the overseas equipment suppliers.

E. FINANCIAL ASSISTANCE PROGRAM LABOR GRANT

11. Under both Automatic FAP (AFA) and CFA, a company is reimbursed a percentage of the wages it pays to unskilled and semi-skilled workers, starting at 80 percent in the first two years and

descending to 60 percent in Year 3, 40 percent in Year 4, and 20 percent in Year 5, the final year. This component of FAP was intended to compensate for the low productivity of Botswana workers, the expectation being that by the time the grants expired the workers would have received enough training and experience to become competitive with workers in other countries. Experience, however, does not support this.

F. FINANCIAL ASSISTANCE POLICY SALES AUGMENTATION GRANT

12. CFA provides a sales augmentation grant of 8 percent of a company's total sales in Years 1 and 2, 6 percent in Year 3, 4 percent in year 4, and 2 percent in Year 5. The Sales Augmentation Grant is often justified as a compensation for the high cost of utilities, land, construction and transport in Botswana, since it increases with sales volume just as most direct costs and overheads do. It also is represented as a sort of export incentive, compensating exporters for the high cost of inland transport to South African ports and for the exceptionally high wharfage charges assessed.

G. TRAINING GRANT

13. The FAP Training Grant provides for reimbursement of 50 percent of off-site training expenses incurred during the first five years of operation. In a country as short of skills as Botswana, a grant of this kind has substantial merit. There have been suggestions that the training grant be expanded to include on-site training as well, or that 100 percent of the cost be reimbursed by Government. However, it is difficult to differentiate between on-site training and normal technical supervision, since in any manufacturing environment, technicians and managers constantly train and transfer skills to workers If on-site training is covered by the FAP training grant, then all technicians' and managers' salaries could potentially be eligible for reimbursement, leading to employment of unnecessary personnel and a virtual absence of controls on the cost of the program.

14. Similarly, if FAP were to cover 100 percent of off-site training costs, then companies would not be subject to any cost discipline of their own and might send too many workers to training courses of questionable value. By continuing to bear a substantial portion of the cost of training, FAP recipients will be encouraged to select the most cost-effective forms of training and to send only those workers most likely to benefit.

H. TAX HOLIDAYS

15. Companies receiving AFA, while ineligible for the FAP Capital Grant, qualify for tax holidays that are not available to CFA recipients. Although it is called a tax holiday, it is, in fact, a reimbursement of taxes paid on a company's profits. In urban and peri-urban areas the reimbursement is 100 percent in years 1 and 2, 75 percent in Year 3, 50 percent in year 4, and 25 percent in Year 5. In rural areas it is 100 percent in Years 1-3, 75 percent in Year 4, and 50 percent in Year 5.

I. SELEBI-PHIKWE REGIONAL DEVELOPMENT PROGRAM

16. As early as 1983 the Government began to consider policy measures, strategies and plans for diversifying the economy of Selebi-Phikwe and its surrounding area away from dependence on the copper-nickel mines. This culminated in 1986 with the drafting of terms of reference for the Selebi-Phikwe Regional Development Project (SPRDP), which began operation in March 1988. In January 1990

a Special Incentive Package for Selebi-Phikwe was instituted. Based on the existing case by case (CFA) FAP incentives, it provided additional benefits for 100 percent export manufacturing companies locating in Selebi-Phikwe. In order to receive the special incentive package, a firm was required to:

(a) establish a factory in Selebi-Phikwe;
(b) export 100 percent of its output outside the SACU or SADCC region;
(c) employ at least 400 Botswana citizens within two years of start-up;
(d) have been in operation elsewhere for at least 10 years;
(e) contribute at least 25 percent of the total project cost, including working capital, as equity.

17. For companies meeting these criteria, the special incentive package offered consists of:

(a) normal CFA FAP grants over five years of up to the lesser of 120 percent of unskilled labor and training costs in the same period or 50 percent of the project's value added in the same period;
(b) a 15 percent corporate tax on profits for the first 20 years of the project's life;
(c) a ten-year exemption from the withholding tax on dividends paid to non-residents.

18. In its first four years of operation, the SPRDP has had considerable success. Eight new projects went into production, two of which subsequently failed. As of February 1992, the six remaining projects employed 1472 citizens, and were projected to employ 1886 at full production. An additional six projects were considered "Category A" pipeline projects, which had already applied for manufacturing licenses, FAP, and/or factory building sites, and were considered highly likely to go into production. Projected employment in these Category A projects was 2060. 56 companies in all had made site visits to Selebi-Phikwe, and promotional efforts continued in Southern Africa, East Asia, and Europe, where discussions continue with a large number of interested potential investors.

J. TRADE AND INVESTMENT PROMOTION AGENCY (TIPA)

19. When Government, in 1990, upgraded TIPA from the status of a unit within the Ministry of Commerce and Industry (MCI) to that of a fully-fledged Department (formally known as the Department of Trade and Investment Promotion, but still popularly referred to by its former name, TIPA), it signalled the increased emphasis it intended to place on promoting foreign direct investment into Botswana and on active promotion of Botswana's exports. Sadly, TIPA did not receive increased resources and authority commensurate with its enhanced status and increased responsibilities.

20. The 1984 Industrial Development Policy called for the establishment of TIPA, which it charged with the following tasks:

(a) 'Provision of a "one-stop" service to local and foreign investors to speed up the establishment of productive activities (channeling of application forms, etc.),
(b) 'Provision of information on investment opportunities,
(c) 'Provision of trade information,
(d) 'Maintaining an "Industrial Land Register".

21. TIPA, by the admission of its own Director, has not succeeded in carrying out these

functions. While the Commercial Attachés at Botswana's Embassies and High Commissions overseas, who nominally report to TIPA, have generated some trade and investment enquiries, TIPA overall has not become a "one-stop-shop" for investors, and is unable to provide the kind of assistance in obtaining licenses, land, housing, visas and work permits, financing, and Government incentives that many of its counterpart agencies in other countries do. TIPA's performance is here reviewed by function:

22. **Trade and Investment Promotion.** TIPA's promotional activities consist of three parts: 1) overseas promotion carried out on a regular basis by commercial attachés; 2) overseas trade and investment missions or delegations; and, 3) organizing trade fairs within Botswana (Gaborone International Fair and Botswana International Trade Exhibition). No real effort has ever been made to assess the effectiveness of TIPA's performance of these functions, in generating either trade and investment enquiries or consummated trade and investment transactions. In the cases of one-off missions or delegations on the one hand, and trade fairs on the other hand, clear measures of effectiveness are hard to devise.

23. It should be possible, however, to develop clear measures of the effectiveness of promotional activities undertaken by the commercial attachés. While neither TIPA nor the embassies and high commissions compile statistics on such activities, all evidence suggests that they are, at most, marginally effective. Few, if any, of the commercial attachés have devised and carried out any concerted promotional campaigns, tending instead only to respond to enquiries. There are several reasons for this failure: 1) the commercial attachés function without much strategic guidance or support from TIPA, so that they have little notion what industries, sectors, regions or specific companies should be targeted; 2) the commercial attachés lack the resources needed to conduct extensive promotion campaigns; 3) the commercial attachés have diplomatic duties that detract from the time they have to devote to trade and investment promotion; 4) as civil servants, commercial attachés are recruited and rewarded according to criteria that may have little to do with their effectiveness in trade and investment promotion; 5) commercial attachés are placed in countries and cities where Botswana has a diplomatic presence, with little or no consideration of the location's trade and investment potential; 6) even in locations, such as Brussels, where a promotional presence is warranted, commercial attachés may spend most of their time in bilateral or multilateral trade negotiations rather than on promotion.

24. **Provision of "One-Stop" Service to Investors.** TIPA, were it to function as intended, would serve as a one-stop-shop where investors could obtain all necessary information and approvals. An investor should be able to apply to TIPA for visas and work permits, land, manufacturing licenses, and even to rely on TIPA's help in obtaining financing for a project. SPRDP, in fact, provides most of these functions for investors in Selebi-Phikwe, providing initial information, coordinating site visits, securing land or factory shells, guiding an investor through all the steps required for a project to be implemented and, most important, acting as the investor's advocate in negotiations with other Government, parastatal and private sector bodies.

K. LOCAL PREFERENCE SCHEME

25. Many countries give preference to local companies in awarding Government procurement contracts. Botswana's Local Preference Scheme (LPS) seeks to do this by applying a preference formula to bid prices that is meant to give companies a cost advantage based on the percentage of local content in the product being procured. While this is unobjectionable, the formula in use appears excessively complicated. It is unclear whether Government has the capacity to develop an accurate measure of local

content, particularly where a company has purchased intermediate goods from another Botswana company, which would entail calculating that company's local content percentage. Also, it is not clear why purchases from a Botswana company which is majority foreign-owned but which operates in Botswana with Botswana workers should not count as local content.

FINANCIAL ASSISTANCE POLICY TABLES

Table 1: Financial Assistance Policy Summary - All Projects

Category	Number of Projects	Projected Employment	Actual Employment	Grants Committed
Small Scale				
Industrial	1,708	6,536	n/a	13,937,912
Agricultural	1,172	2,602	n/a	7,888,863
Medium Scale				
CAF-Industrial	267	11,378	4,696	145,642,175
AFA-Automatic	147	6,507	3,682	n/a
CFA-Agricultural	119	4,910	2,295	16,784,713
Large-Scale	19	3,640	1,958	54,472,894
TOTAL	3,432	35,573	12,631	238,726,557

NOTE: Actual employment for small scale projects not available because of insufficient monitoring. Therefore, the figure for actual employment should be higher than the figure shown above.

Table 2: Financial Assistance Policy
Grants Committed by Year and Location Medium Scale Case-by-Case Industrial Projects
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Gaborone	76,700	560,144	256,602	1,227,307	4,174,357	7,873,276	7,617,252	62,283,096	6,269,141	10,646,481	100,984,356
Francistown	0	82,450	303,473	0	1,433,768	2,156,448	410,033	382,972	2,180,794	3,356,138	10,308,076
Lobatse	0	240,505	0	0	0	687,015	901,820	1,698,699	1,309,156	1,309,156	6,146,351
Tuli Block	550,520	0	0	87,552	0	0	0	0	0	0	638,072
Northern	62,517	31,788	44,056	495,800	191,026	0	0	0	0	0	825,187
Central	20,884	292,248	914,850	0	654,880	144,050	690,465	98,644	0	654,419	3,470,440
Kgatleng	0	0	188,253	0	0	65,382	626,200	0	0	964,167	1,844,002
Ngamiland	0	143,076	0	0	37,584	0	0	394,484	338,562	0	913,706
Jwaneng	0	33,461	0	0	201,850	0	0	326,156	301,725	121,677	984,869
Kweneng	0	26,816	108,226	542,318	0	204,828	0	1,132,036	0	145,376	2,159,600
Selebi-Phikwe	0	326,369	1,022,743	264,016	206,014	395,912	469,684	0	317,148	2,312,394	5,314,280
Pandamatenge	0	367,452	0	0	2,243,646	486,570	0	0	0	0	3,097,668
Southeast	0	178,750	397,479	0	263,001	626,167	2,653,585	374,480	193,340	0	4,686,802
Southern	382,230	138,960	247,653	131,119	1,622,249	532,837	511,471	434,900	173,182	96,165	4,270,766
TOTAL	1,092,851	2,422,019	3,483,335	2,616,993	11,028,375	13,172,485	13,880,510	67,125,467	11,083,048	19,605,973	145,642,175

Table 3: Financial Assistance Policy
Number of Projects Approved by Year and Location
Medium Scale Case-by-Case Industrial Projects
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Gaborone	1	11	13	8	13	25	17	9	8	13	118
Francistown	0	2	1	0	5	5	3	1	5	7	29
Lobatse	0	2	0	0	0	3	3	3	2	0	13
Tuli Block	1	0	0	1	0	0	0	0	0	0	2
Northern	1	1	1	1	1	0	0	0	0	0	5
Central	1	3	1	0	2	2	3	1	0	5	18
Southern	2	1	2	2	2	2	1	2	1	1	16
Kgatleng	0	0	1	0	0	1	1	0	0	4	7
Kweneng	0	1	2	2	0	2	0	3	0	1	11
Selebi-Phikwe	0	1	4	1	1	1	2	0	1	4	15
Ngamiland	0	1	0	0	1	0	0	1	1	0	4
Jwaneng	0	1	0	0	1	0	0	2	1	1	6
Southeast	0	1	6	0	2	4	4	1	1	0	19
Pandamatenge	0	1	0	0	2	1	0	0	0	0	4
TOTAL	6	26	31	15	30	46	34	23	20	36	267

Table 4: Financial Assistance Policy
Projected Employ..ent by Year and Location
Medium Scale Case-by-Case Industrial Projects
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Gaborone	52	389	439	220	545	1,134	813	445	541	463	5,041
Francistown	0	52	67	0	218	358	107	104	269	513	1,688
Lobatse	0	57	0	0	26	166	117	194	16	0	576
Jwaneng	0	8	0	0	29	0	0	30	38	13	118
Selebi-Phikwe	0	62	138	45	50	60	56	0	435	184	1,030
Southern	82	18	39	28	27	65	62	31	36	0	388
Kweneng	0	8	39	58	0	22	0	82	0	90	299
Chobe	65	31	0	0	154	77	0	60	21	0	408
Kgatleng	0	0	28	0	0	10	80	0	0	73	191
Southeast	0	30	96	0	43	90	326	458	13	0	1,056
Central	100	46	170	18	91	23	76	12	0	47	583
TOTAL	299	701	1,016	369	1,183	2,005	1,637	1,416	1,369	1,383	11,378

Table 5: Financial Assistance Policy
Actual Employment by Year and Location
Medium Scale Case-by-Case Industrial Projects
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Gaborone	107	281	403	120	413	337	436	494	219	277	3,087
Francistown	83	87	41	0	147	47	0	4	16	76	501
Lobatse	0	87	0	0	0	148	30	0	64	0	329
Jwaneng	0	7	0	0	0	0	0	13	0	0	20
Selebi-Phikwe	0	19	47	0	0	0	0	0	0	10	76
Southern	91	0	8	0	68	0	0	0	0	0	167
Kweneng	0	0	43	0	0	0	0	89	0	13	145
Chobe	0	0	0	0	31	0	0	0	59	0	90
Kgatleng	0	0	50	0	0	0	0	0	0	10	60
Southeast	0	0	40	0	0	0	57	52	0	0	149
Central	72	0	0	0	0	0	0	0	0	0	72
TOTAL	353	481	632	120	659	532	523	652	358	386	4,696

NOTE: Some projects are either withdrawn or cancelled and others have not started operating.

Table 6: Financial Assistance Policy
Grants Committed by Year and Location
Medium Scale Case-by-Case Agricultural Projects
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Gaborone	0	9,369	18,480	33,282	45,578	154,911	239,228	1,475,841	62,766	347,684	2,387,139
Francistown	0	0	0	0	201,985	0	118,586	117,016	144,638	880,920	1,463,145
Lobatse	0	0	125,768	0	0	34,928	645,013	0	696,679	0	1,502,388
Tuli Block	378,632	67,812	305,158	368,390	122,856	0	0	0	0	0	1,242,848
Northern	0	252,518	0	115,313	0	0	0	0	0	0	367,831
Central	0	0	34,823	53,270	0	114,500	158,351	104,686	0	214,545	680,175
Southern	0	0	30,392	0	0	0	40,004	0	0	322,418	392,814
Ngamiland	148,193	0	0	87,012	159,484	70,028	0	0	152,836	0	617,553
Kgatleng	72,980	0	2,500	0	292,382	22,361	243,688	0	101,746	65,855	801,512
Kweneng	8,920	0	0	0	0	116,174	0	0	0	155,573	280,667
Maun	0	268,640	0	0	0	0	0	0	0	0	268,640
Selebi-Phikwe	0	0	0	0	0	0	244,320	0	208,780	0	453,100
Ghanzi	0	0	0	0	0	0	0	160,420	0	0	160,420
Pandamatenge	0	0	0	657,267	3,700,502	659,239	691,300	458,173	0	0	6,166,481
TOTAL	608,725	598,339	517,121	1,314,534	4,522,787	1,172,141	2,380,490	2,316,136	1,367,445	1,986,995	16,784,713

Table 7: Financial Assistance Policy
Number of Projects approved by Year and Location
Medium Scale Case-by-Case Agricultural Projects
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Gaborone	0	1	1	2	1	7	1	1	2	2	18
Francistown	0	0	1	0	2	1	0	1	2	3	10
Southern	0	1	0	0	0	0	1	0	0	2	4
Lobatse	0	0	4	2	0	0	5	0	3	0	14
Tuli Block	0	3	2	2	0	2	0	0	0	0	9
Northern	1	1	0	1	0	0	0	0	1	0	4
Central	0	0	3	2	1	3	0	0	1	3	13
Southeast	0	0	3	0	0	0	1	0	3	0	7
Kgatleng	0	0	0	0	1	1	2	0	0	1	5
Ngamiland	1	1	3	0	1	0	0	0	2	0	8
Jwaneng	0	0	0	0	0	0	0	0	0	0	0
Kweneng	0	0	0	0	0	1	0	0	0	1	2
Selebi-Phikwe	0	1	0	0	0	0	1	1	0	0	3
Pandamatenge	0	0	0	4	9	6	1	1	0	1	22
TOTAL	2	8	17	13	16	21	12	4	14	13	119

Table 8: Financial Assistance Policy
Projected Employment by Year and Location
Medium Scale Case-by-Case Agricultural Projects
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Gaborone	0	2	8	0	11	28	5	161	7	7	229
Francistown	0	0	0	0	16	0	22	12	13	59	122
Lobatse	0	0	47	0	0	0	138	0	55	0	240
Tuli Block	126	37	84	114	35	0	0	0	0	0	396
Northern	0	110	0	30	0	0	0	0	0	0	140
Central	0	0	0	0	0	25	40	5	0	16	86
Southern	0	0	4	0	0	0	13	0	0	21	38
Ngamiland	237	0	0	0	32	34	0	0	20	0	323
Kgatleng	0	0	13	0	75	4	52	0	14	5	163
Kweneng	2	0	0	0	0	10	0	0	0	10	22
Maun	0	65	0	0	0	0	0	0	0	0	65
Selebi-Phikwe	0	8	0	0	0	0	50	0	25	0	83
Ghanzi	0	0	0	0	0	0	0	0	0	0	0
Pandamatenge	0	0	0	183	2,290	207	209	114	0	0	3,003
TOTAL	365	222	156	327	2,459	308	529	292	134	118	4,910

Table 9: Financial Assistance Policy
Actual Employment by Year and L/ ation
Medium Scale Case-by-Case Agricult/ al Projects
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Gaborone	0	0	0	0	10	46	19	50	0	30	155
Francistown	0	0	0	0	62	0	15	42	2	0	121
Lobatse	0	0	43	14	0	0	80	0	19	0	156
Tuli Block	44	10	41	9	5	0	0	0	0	0	109
Northern	0	184	0	26	0	0	34	0	0	0	244
Central	0	0	0	0	0	28	0	0	0	0	28
Southern	0	0	8	0	0	0	0	0	0	0	8
Ngamiland	195	0	0	0	55	14	0	0	16	0	280
Kgatleng	21	0	0	5	12	3	10	0	13	0	64
Kweneng	0	0	0	0	0	5	0	0	0	0	5
Maun	0	21	0	0	0	0	0	0	0	0	21
Selebi-Phikwe	0	14	0	0	0	0	23	0	0	0	37
Ghanzi	0	0	0	0	0	0	0	13	0	0	13
Pandamatenge	0	0	0	47	645	145	160	57	0	0	1,054
TOTAL	260	229	92	101	789	241	341	162	50	30	2,295

Table 10: Financial Assistance Policy
Number of Projects Approved by Year and Location
Medium Scale Automatic Projects (AFA)
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Gaborone	3	9	5	2	8	10	9	16	9	12	83
Francistown	0	3	5	3	3	3	3	3	6	2	31
Lobatse	0	2	1	0	0	0	0	1	0	1	5
Central	0	0	0	0	0	0	0	1	0	0	1
Southern	0	0	0	0	0	0	0	1	0	0	1
Kgatleng	0	0	0	0	0	0	0	1	0	0	1
Selebi-Phikwe	1	1	0	1	0	6	2	3	2	2	18
Ngamiland	0	0	0	0	0	0	0	1	1	1	3
Jwaneng	0	0	0	0	1	1	0	0	0	0	2
Southeast	0	0	0	0	1	0	1	0	0	0	2
TOTAL	4	15	11	6	13	20	15	27	18	18	147

Table 11: Financial Assistance Policy
Projected Employment by Year and Location
Medium Scale Automatic Projects (AFA)
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Gaborone	164	162	145	11	456	471	219	580	0	265	2,473
Francistown	0	52	83	0	191	371	0	0	388	32	1,117
Lobatse	0	39	58	22	38	151	55	47	163	22	595
Selebi-Phikwe	0	96	178	79	50	325	56	28	35	48	895
Southern	82	25	39	28	27	39	0	0	28	0	268
Southeast	0	30	124	0	44	77	15	0	31	0	321
Kweneng	2	8	22	75	71	0	0	0	0	0	178
Kgatleng	25	0	44	0	115	21	0	0	23	0	228
Central	4	75	170	0	83	86	0	0	0	14	432
TOTAL	277	487	863	215	1,075	1,541	345	655	668	381	6,507

Table 12: Financial Assistance Policy
Actual Employment by Year and Location
Medium Scale Automatic Projects (AFA)
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Gaborone	238	181	114	8	103	215	260	607	38	0	1,764
Francistown	293	24	34	230	0	47	0	72	74	175	949
Lobatse	42	0	0	0	0	0	0	0	90	0	132
Selebi-Phikwe	29	7	64	0	0	143	0	234	0	0	477
Southern	0	0	0	0	0	0	0	0	35	0	35
Southeast	0	0	0	0	0	0	0	0	0	0	0
Kweneng	0	0	0	0	37	0	0	0	0	0	37
Kgatleng	0	0	0	0	0	0	0	127	0	0	127
Central	12	0	0	0	0	0	0	149	0	0	161
TOTAL	614	212	212	238	140	405	260	1,189	237	175	3,682

NOTE: Some projects are either withdrawn, cancelled or some have not started operating. There are 8 citizen, 113 non-citizen and 26 joint venture projects.

Table 13: Financial Assistance Policy
Number of Loans Approved
Large Scale Projects
(1989 to 1991)

	1989	1990	1991	TOTAL
Gaborone	4	2	3	9
Francistown	0	0	1	1
Selebi-Phikwe	0	1	3	4
Southern	0	0	1	1
Kgatleng	1	1	0	2
Southeast	0	0	1	1
Central	1	0	0	1
Pandamatenga	0	0	0	0
TOTAL	6	4	9	19

Actual Employment
(1989 to 1991)

	1989	1990	1991	TOTAL
Gaborone	458	49	0	507
Francistown	0	0	216	216
Selebi-Phikwe	0	206	707	913
Southern	0	35	0	35
Kgatleng	74	78	0	152
Southeast	0	0	0	0
Central	135	0	0	135
Pandamatenga	0	0	0	0
TOTAL	667	368	923	1,958

Projected Employment
(1989 to 1991)

	1989	1990	1991	TOTAL
Gaborone	362	295	207	864
Francistown	0	0	207	207
Selebi-Phikwe	0	240	2,000	2,240
Southern	0	0	38	38
Kgatleng	100	80	0	180
Southeast	0	0	0	0
Central	111	0	0	111
Pandamatenga	0	0	0	0
TOTAL	573	615	2,452	3,640

Grants Committed
(1989 to 1991)

	1989	1990	1991	TOTAL
Gaborone	6,178,825	5,305,692	2,445,320	13,929,837
Francistown	0	0	3,302,880	3,302,880
Selebi-Phikwe	0	2,820,601	27,370,824	30,191,425
Southern	0	0	1,019,364	1,019,364
Kgatleng	664,448	1,118,714	0	1,783,162
Southeast	0	0	1,915,986	1,915,986
Central	2,330,240	0	0	2,330,240
Pandamatenga	0	0	0	0
TOTAL	9,173,513	9,245,007	36,054,374	54,472,894

NOTE: From 1982 to 1988 some projects are withdrawn, cancelled and others have not started operating.
There are 5 citizen projects, 8 non-citizen and 6 joint venture projects.

Table 14: Financial Assistance Policy
Grants Committed by Year and Location
Small Scale Industrial Projects
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Selebi-Phikwe	24,447	0	0	8,996	505,734	26,027	13,610	123,846	23,934	111,716	838,310
Chobe	2,892	492	3,455	1,469	26,307	8,103	2,610	32,224	180,285	111,087	368,924
Central	83,925	4,201	29,533	14,720	37,149	38,626	41,102	238,795	161,087	640,126	1,289,264
Tutume	11,240	1,828	28,551	8,267	7,458	8,460	0	0	10,688	248,844	325,336
Francistown	20,097	14,075	53,928	25,902	1,394	31,628	11,361	61,000	287,474	115,200	622,059
Gaborone	32,404	16,404	17,937	12,100	27,059	43,543	44,623	71,898	16,836	128,749	411,553
Ghanzi	0	37,239	13,043	20,742	91,530	11,077	35,291	78,234	118,368	64,184	469,708
Northeast	30,449	662	20,952	10,367	11,962	1,456	23,715	28,258	246,283	230,517	604,621
Ngamiland	25,620	62,813	1,641,612	622,812	35,194	65,739	33,862	186,346	193,531	97,279	2,964,808
Jwaneng	645	0	0	0	0	4,000	0	0	0	0	4,645
Kgalagadi	41,650	0	11,060	3,878	4,363	0	4,410	0	323,144	295,546	684,051
Kgatleng	53,867	45,600	15,729	132,836	39,088	54,376	90,973	345,568	400,818	556,975	1,735,830
Kweneng	105,894	41,601	29,677	120,800	61,739	50,368	63,406	228,716	508,728	437,705	1,648,634
Lobatse	0	0	4,237	25,435	11,607	37,875	27,419	29,781	18,026	62,703	217,083
Southeast	14,960	0	4,059	22,108	21,582	1,006	16,478	192,749	264,594	274,806	812,342
Southern	22,770	52,537	29,022	49,299	45,851	67,078	50,481	110,910	193,570	319,226	940,744
TOTAL	470,860	277,452	1,902,795	1,079,731	928,017	449,362	459,341	1,728,325	2,947,366	3,694,663	13,937,912

Table 15: Financial Assistance Policy
Number of Projects Approved by Year and Location
Small Scale Industrial Projects
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Selebi-Phikwe	12	1	0	1	5	6	6	10	5	8	25
Chobe	7	2	1	2	5	3	4	6	11	7	48
Central	46	2	13	6	20	19	12	46	64	50	278
Tutume	12	4	5	4	1	2	0	0	3	17	48
Francistown	15	3	2	5	1	7	3	13	20	7	76
Gaborone	14	11	19	6	7	10	9	11	2	8	97
Ghanzi	0	8	3	6	25	4	10	25	22	10	113
Jwaneng	1	0	0	0	0	1	0	0	0	0	2
Kgalagadi	10	0	8	2	4	0	1	0	30	30	85
Kgatleng	16	15	7	4	5	7	11	27	27	24	143
Kweneng	9	11	20	23	10	18	22	26	35	35	209
Lobatse	0	0	1	7	2	4	3	4	2	3	26
Northeast	23	1	8	3	4	1	7	4	19	17	87
Ngamiland	9	17	6	18	27	18	9	25	23	14	166
Southeast	8	0	3	6	9	2	5	14	18	16	81
Southern	8	28	15	16	20	22	18	21	24	23	195
TOTAL	190	103	111	109	145	124	120	232	305	269	1,708

Table 16: Financial Assistance Policy
Projected Employment by year and Location
Small Scale Industrial Projects
(1982 to 1991)

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	TOTAL
Selebi-Phikwe	57	3	0	10	21	17	8	56	30	45	247
Chobe	11	2	3	4	18	7	4	18	57	26	150
Central	129	3	52	19	63	43	38	142	268	200	957
Tutume	19	6	16	10	7	7	0	0	10	100	175
Francistown	51	12	17	21	1	23	15	67	125	53	385
Gaborone	44	25	38	18	18	30	28	36	20	36	293
Ghanzi	0	27	8	14	66	10	41	87	71	32	356
Jwaneng	1	0	0	0	0	2	0	0	0	0	3
Kgalagadi	36	0	16	3	14	0	6	0	97	98	270
Kgatleng	77	60	22	11	27	32	58	123	155	89	654
Kweneng	41	36	55	90	35	63	78	130	216	183	927
Lobatse	0	0	11	26	3	9	14	12	10	18	103
Northeast	56	2	44	13	14	1	30	25	75	66	326
Ngamiland	37	100	45	44	46	55	50	106	81	72	636
Southeast	20	0	8	18	22	5	21	84	107	108	393
Southern	20	80	38	48	62	55	63	72	118	105	661
TOTAL	599	356	373	349	417	359	454	958	1,440	1,231	6,536

NOTE: No actual employment data because of insufficient monitoring. Some projects are either withdrawn, cancelled or have not started operating.

Table 17: Financial Assistance Policy
Number of Projects, Projected Employment and Grants Committed
Small Scale Agricultural Projects

	Number of Approvals	Projected Employment	Grants Committed
Bobonong	27	75	289,918
Chobe	96	79	53,808
Mahalapye	61	147	539,409
Serowe	118	252	640,215
Tutume	82	211	763,383
Francistown	15	63	59,663
Kgatleng	22	50	174,727
Kweneng	63	149	462,056
Northeast	69	227	587,763
Ngamiland	300	472	667,798
Southern	193	595	2,452,695
Kgalagadi	67	121	546,733
Gaborone	7	20	37,650
Southeast	52	141	613,045
TOTAL	1,172	2,602	7,888,863

NOTE: It is not possible to give data by years as the Ministry of Agriculture does not keep its records by years.

Table 18: Financial Assistance Policy
Amount Disbursed
(1982 to 1991)

	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88	1988/89	1989/90	1990/91	TOTAL
Small Scale Capital Grant	149,122	448,405	371,058	528,004	710,198	917,525	911,768	2,188,705	5,398,884	11,623,669
Medium Scale Capital Grant	215,132	683,337	663,172	841,809	2,589,576	1,252,866	1,420,703	1,192,904	990,874	9,850,373
Large Scale Capital Grant	0	0	0	0	0	0	0	986,722	1,882,960	2,869,682
Labor Case by Case	0	208,364	816,477	1,537,160	2,317,446	3,559,610	3,635,581	4,681,833	6,631,813	23,388,284
Labor Automatic	0	106,933	387,481	831,575	1,127,857	1,028,159	1,568,524	2,400,879	1,113,963	8,565,371
Sales Augmentation	0	85,178	276,908	561,984	733,557	1,436,099	1,266,383	1,256,067	2,853,003	8,469,179
Tax Holiday	0	0	141,071	266,868	490,154	1,076,649	394,482	684,873	1,332,238	4,386,335
Training	0	0	75,824	77,036	1,591	33,105	14,866	8,718	64,381	275,521
Counsellor Scheme	0	1,070	11,940	29,320	22,800	20,420	15,650	16,126	4,980	122,306
TOTAL	364,254	1,533,287	2,743,931	4,673,756	7,993,179	9,324,433	9,227,957	13,416,827	20,273,096	69,550,720

ANNEX 4

NATURE TOURISM AND THE NEW TOURISM POLICY

1. Nature tourism could also be developed based on Botswana's large tracts of undeveloped land set aside as national parks, game reserves and wildlife management areas. With 70 per cent of tourism-related jobs in rural areas, the tourism industry generally is a vital element in achieving a countrywide growth of employment opportunities. Available facilities consist mainly of lodges, camps and mobile safari operations in the Okavango swamps and the Chobe area. There is little information on nature tourist movements, numbers, length of stay or spending patterns. Lack of such knowledge is a serious defect of the regulation orientated tourism policy statement of 1990. The principal objective of the statement is to increase foreign exchange earnings by boosting the numbers of high spending visitors whilst actively discouraging low spending campers who come in by road from neighboring countries. Other policy objectives are to increase taxation and licensing of tourist services and to raise citizen participation in the industry as employees, operators and investors. The special characteristics of nature tourism demand are not addressed, nor is there an analysis of the type of services required, or of the tradeoffs between encouraging one type of tourist at the expense of another.

2. Despite the unique attraction of the Okavango delta ecosystem Botswana is not an important single country destination in the international nature tourism market. The majority of eco-tourists come to Botswana as part of the Southern African nature tourism circuit, combined with travel to Zimbabwe, Zambia and South Africa. Tourists can make immediate comparisons between countries, not only with respect to costs and the quality of services or facilities, but also with respect to attitude to tourists among those coming into contact with them, from immigration officials onwards. Botswana still has some relative advantages over competing nature tourism facilities in Zimbabwe and Zambia. For example, there are no import constraints due to foreign exchange shortages, which means that appropriate equipment, food and beverages required by tourists are readily available. Transport and communications are also better than in Zambia. However, costs are already higher in Botswana compared with nature tourism options in Zambia and Zimbabwe, as well as those offered by South Africa, Swaziland and Lesotho. The imposition of sales tax could further reduce Botswana's competitive position. As for proposed increases in profits taxation, experience elsewhere has shown that the most efficient way of taxing informal nature tourism enterprises is to charge an annual operating fee. The fee is related to capacity and to the length of annual opening, as an optional alternative to incorporation and company profits tax liability, with its demanding bookkeeping requirements.

3. The tourism policy objective of encouraging arrivals of high spending visitors whilst discouraging low spending campers requires reconsideration. There is no evidence of campers crowding out high spending visitors in nature tourism facilities, so a reduction in the number of low spending visitors is most likely to result in a fall in the total number of visitors, and a decline in total tourism receipts. Evidence from other countries with important camping tourism sectors shows that today's campers are often tomorrow's formal tourists. It is therefore important for Botswana to build up consumer loyalty in this niche market as short-stay tourists from neighboring countries are likely to make an important year-round contribution to tourism earnings in the foreseeable future. In this respect it is also recommended that all visitors should pay the same camping fees to avoid one group (foreign visitors) subsidizing another group (local visitors) in consuming a good (camping space) that is in limited supply. Preferential rates for citizens and residents would continue for park entrance fees.

4. Citizen participation in the nature tourism sector is more a question of time and experience than of legislative or regulatory measures. There are at present no barriers to new investment

by citizens, but there is still a lack of skills. Small scale nature tourism enterprises worldwide are heavily dependent on links with individual international tour operators as, by definition, they do not have marketing resources. This relationship is difficult to break into unless there are big local tour operators who have their own international connections and are prepared to work with the small local nature tourism enterprises. As for employment in the nature tourism facilities themselves, they require people capable of improvisation and adaptability above all else. These are skills which are acquired on the job and it can be expected that Batswana owner-managers will emerge during the NDP 7 period, with a decade of nature tourism expansion to build on. There is also a need for graduate naturalist guides, preferably with language skills. Currently, most available guides are expatriates. Since Botswana still suffers from a chronic shortage of graduate skills it would seem preferable, for the time being, to rely on relatively cheap temporary immigrant skills than to impose restrictions on expatriates at a time when Batswana graduates are more usefully employed in other areas of the economy. Meanwhile further resources are required for the Botswana Wildlife Training Institute in Maun, as proposed in NDP 7, to increase the supply of skilled workers needed in the nature tourism sector and other wildlife-related activities.

MAP SECTION

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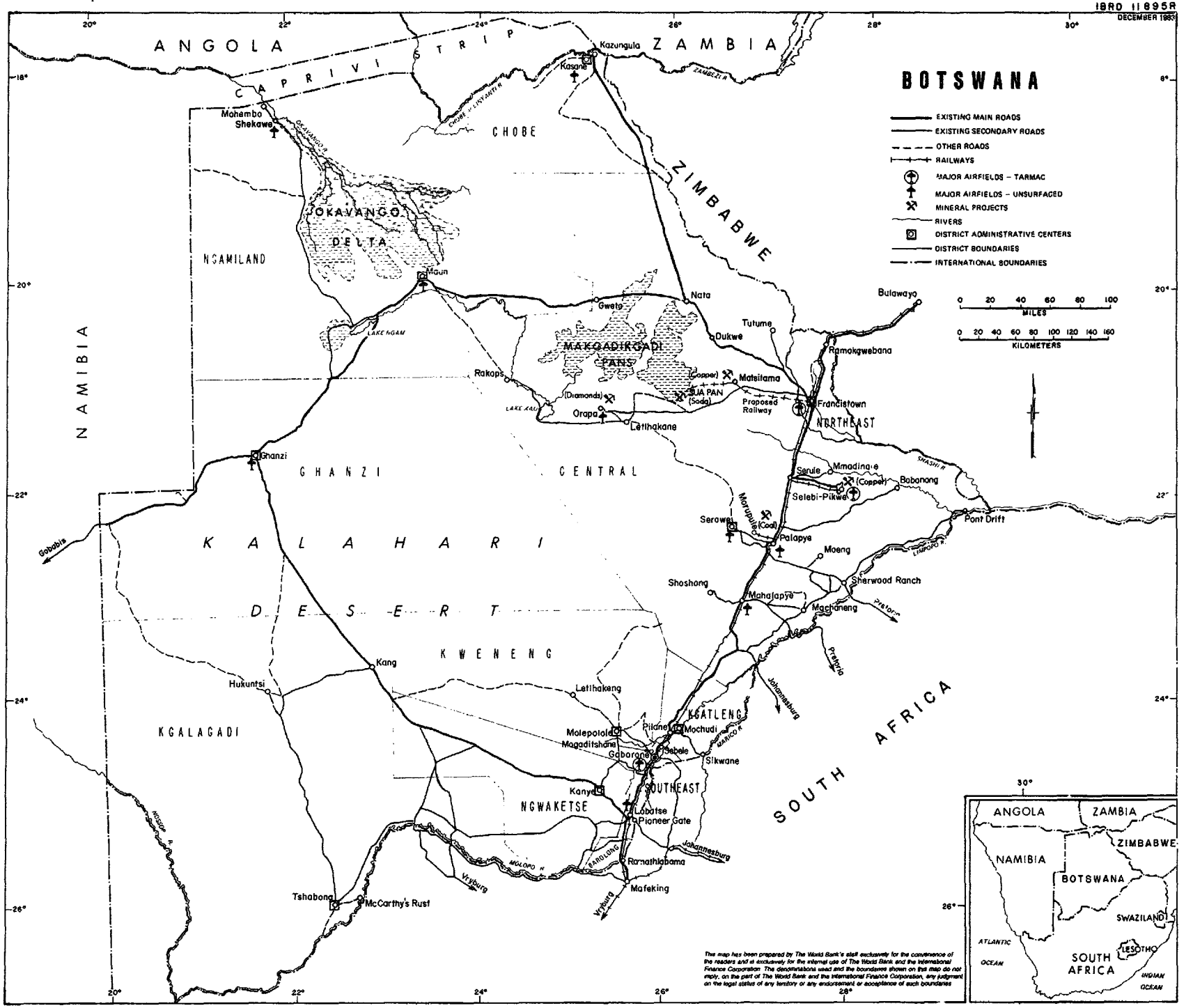

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