Rating Action: Moody's Ratings changes Botswana's outlook to negative from stable; affirms A3 ratings

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London, April 04, 2025 -- Moody's Ratings (Moody's) has today changed the outlook on the Government of Botswana to negative from stable and affirmed the local and foreign currency long-term issuer ratings at A3.

The outlook change to negative reflects increasing risks to Botswana's credit profile due to a prolonged downturn in the diamond industry, a key pillar of the economy. This downturn will affect government revenue and deplete fiscal buffers, leading to a rapid increase in government debt and a weakening of debt affordability. In response, we expect the government to implement fiscal consolidation measures and improve its access to borrowing by better leveraging the large pool of domestic savings in Botswana. However, past attempts by the authorities to diversify the economy and revenue base have yielded mixed results. Any delay in their policy response risks continuous debt increases in the years to come.

The affirmation of the A3 ratings is supported by Botswana's still moderate debt burden and strong debt affordability, as well as low susceptibility to event risks. Domestic political and geopolitical risks are very low, as demonstrated by the peaceful power transition following the 2024 election, the first transition in Botswana's history. High domestic savings provide the government with sufficient financing options to limit the deterioration in debt affordability even as the debt rises, subject to the authorities' ability to foster the rapid development of the untapped domestic investor base and a robust government debt market.

Botswana's local currency (LC) and foreign currency (FC) country ceilings remain unchanged at Aa3 and A1, respectively. The three-notch LC ceiling gap to the sovereign rating reflects predictable institutions and government actions, low political risk and external imbalances against the government's significant footprint in the economy and reliance on a single revenue source. The one-notch gap between the FC ceiling and the LC ceiling reflects moderate policy effectiveness and low external indebtedness that point to limited transfer and convertibility risks.

RATINGS RATIONALE

RATIONALE FOR THE NEGATIVE OUTLOOK

The prolonged downturn in the diamond sector is exerting pressure on Botswana's economic growth prospects, exports and government revenues. Demand for polished diamonds remains subdued due to slowing global demand and changing consumer preferences, while structural shifts, including the growing popularity of lab-grown diamonds, are likely to continue to erode the industry's long-term profitability and its contribution to the economy and government finances.

Despite Botswana's history of managing diamond sector volatility, the government has nearly depleted its fiscal reserves, making the credit profile more vulnerable to ongoing weakness in the diamond sector. We expect large fiscal deficits to persist due to the decline in mineral revenue, mainly from diamonds. The fiscal deficit widened to an estimated 9.0% of GDP in the fiscal year ending March 31, 2025 (fiscal 2024/2025), from 4.3% of GDP in the prior year. The deterioration in the fiscal deficit was driven by a decline in mineral revenue to 3.2% of GDP, compared to 9.3% of GDP in the prior year. We expect ongoing weakness in the diamond sector, and subdued mineral revenue, will keep the deficit around 9% of GDP in 2025/26, before narrowing as the government implements a fiscal consolidation plan. As a result, we forecast the government debt burden to increase to 40% of GDP at the end of 2025/26 from 27% at the end of 2024.

In the absence of a fiscal buffer, the government intends to rely on a combination of domestic and external financing sources to meet its gross financing needs, which we estimate at 13.4% of GDP in 2025/26. However, the government's limited track record in mobilizing large-scale financing from domestic or external sources increases risks to the government's liquidity and debt affordability. We also see risks to the timely and adequate disbursement of concessional external financing for general budget purposes, as this financing often involves long timelines before disbursement and restrictions on how funds can be used. Any shortfalls in external concessional financing, along with potential constraints in scaling up domestic financing, would likely increase the government's reliance on external commercial borrowing. This shift in financing would contribute to a more rapid deterioration in Botswana's debt affordability than currently envisioned. We expect the interest-to-revenue ratio to increase to 4.2% in 2025/26, up from just 2.2% in 2022/23 and 4.0% in 2024/2025.

RATIONALE FOR AFFIRMING THE A3 RATING

The affirmation of the A3 rating is supported by Botswana's credit strengths, including its still moderate debt burden and its track record of managing economic and fiscal shocks. At 27% of GDP at the end of 2024, Botswana's debt burden remains lower than most other A3-rated peers.

The peaceful transition of power following the October 2024 election reinforces our confidence in the country's governance and political institutions. The current government has the mandate and political capital to implement fiscal consolidation measures, including a reduction in development spending as well as controlling growth in the wage bill and rationalizing transfers to state-owned enterprises. The government also has space to increase tax revenues to levels closer to regional peers. These measures could support a stronger-than-expected fiscal consolidation and help stabilize Botswana's debt burden. Furthermore, the administration has committed to implement economic reforms to reduce reliance on the volatile diamond sector and support private sector-led growth, raising the possibility of lower deficits and stronger long-term growth potential than we currently expect.

Botswana's credit profile also benefits from low susceptibility to event risks. Geopolitical risks are very low relative to A3-rated peers and foreign exchange reserves, while declining, remain sufficient to meet the government's very low external debt service obligations and support the foreign exchange regime. Botswana's sizeable positive net international investment position reflects high domestic savings, which have been invested abroad, mitigating external vulnerability risk.

GDP per capita (PPP basis, US$): 19,391 (2023) (also known as Per Capita Income)

Real GDP growth (% change): 3.2% (2023) (also known as GDP Growth)

Inflation Rate (CPI, % change Dec/Dec): 3.5% (2023)

Gen. Gov. Financial Balance/GDP: -4.7% (2023) (also known as Fiscal Balance)

Current Account Balance/GDP: -0.6% (2023) (also known as External Balance)

External debt/GDP: 10.3% (2023)

Economic resiliency: baa2

Default history: No default events (on bonds or loans) have been recorded since 1983.

On 01 April 2025, a rating committee was called to discuss the rating of the Botswana, Government of. The main points raised during the discussion were: The issuer's economic fundamentals, including its economic strength, have materially decreased. The issuer's institutions and governance strength, have not materially changed. The issuer's fiscal or financial strength, including its debt profile, has materially decreased. The issuer has become more susceptible to event risks.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE CONSIDERATIONS

Botswana's ESG Credit Impact Score of CIS-3 indicates that ESG considerations have a limited adverse impact on the current credit rating with potential for greater negative impact over time. This reflects high exposure to social risks combined with high resilience, reflecting relatively strong governance profile, moderate wealth levels, and strong fiscal metrics that provide fiscal space to respond to E and S risks.

Botswana's credit profile is moderately exposed to environmental risks as reflected in its E-3 issuer profile score. Botswana is affected by water scarcity and is vulnerable to recurrent droughts, despite relatively low economic reliance on agriculture compared to other sub-Saharan African sovereigns. A high reliance on coal-fired power generation also increases carbon transition risks.

Exposure to social risks is high (S-4 issuer profile score), as progress in reducing high unemployment, in particular among the youth, and high-income inequality lags compared to Botswana's relatively strong economic performance and sound institutions, in part reflecting dependence on the mining sector, limited private sector job creation, and labor market distortions. Outcomes in terms of health, and to a lesser extent education, are not commensurate to the level of income and social spending.

Botswana has a G-2 issuer profile score. The country performs strongly on the Worldwide Governance Indicators, particularly in the category of control of corruption, and ranks 6th out of 54 African countries according to the 2024 Ibrahim Index of African Governance. Botswana has been characterized by sound management of the natural resources income, which it has invested to expand the country's social and physical infrastructure, its education sector and the government's institutional capacity. Nevertheless, efficiency of spending remains low and a sluggish fiscal adjustment to declining mineral revenues or declining debt affordability despite adequate domestic savings would weigh on our assessment of governance strength.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

An upgrade is unlikely given the negative outlook. The outlook could return to stable if the government debt burden and debt affordability were likely to weaken materially less than currently projected and fiscal buffers were to increase. This would most likely require the adoption and implementation of significant fiscal consolidation measures or a lasting rebound in the diamond sector.

A downgrade of Botswana's rating would be likely if the government's policy response were insufficient to arrest the deterioration in its debt burden and debt affordability. Evidence of financing constraints, such as a greater reliance on more expensive funding sources that weakens debt affordability more than currently envisioned, would be credit negative. A structurally weaker growth outlook or a material deterioration of the external position due to a more prolonged downturn in the diamond sector could also lead to a downgrade.

The principal methodology used in these ratings was Sovereigns published in November 2022 and available at https://ratings.moodys.com/rmc-documents/395819 .

Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

The weighting of all rating factors is described in the methodology used in this credit rating action, if applicable.

The net effect of any adjustments applied to rating factor scores or scorecard outputs under the primary methodology(ies), if any, was not material to the ratings addressed in this announcement.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions .

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