



FINANCIAL STABILITY REPORT

MAY | 2026





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MAY 2026
FINANCIAL STABILITY COUNCIL

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ABBREVIATIONS

AI	Artificial Intelligence
AGC	Attorney General's Chamber
AML	Anti-Money Laundering
BETP	Botswana Economic Transformation Programme
BISS	Botswana Interbank Settlement System
BoE	Bank of England
BSEL	Botswana Stock Exchange Limited
CAR	Capital Adequacy Ratio
CDD	Customer Due Diligence
CET 1	Common Equity Tier 1
CF	Credit Facility
CFT	Combating the Financing of Terrorism
CIU	Collective Investment Units
COFC	City of Francistown Council
CorpI	Corporate Bond Index
CPF	Counter Proliferation Financing
CRE	Commercial Real Estate
CSDB	Central Securities Depository of Botswana
DCI	Domestic Company Index
DCTRI	Domestic Company Total Return Index
DISB	Deposit Insurance Scheme of Botswana
DNFBP	Designated Non-Financial Businesses and Profession
D-SIB	Domestic Systemically Important Banks
D-SIFI	Domestic Systemically Important Financial Institution
D-SII	Domestic Systemically Important Insurer
DSTI	Debt-Service-to-Income
DTI	Debt-to-Income
ECB	European Central Bank
EFT	Electronic Funds Transfer
ELA	Emergency Liquidity Assistance
EMDEs	Emerging Market and Developing Economies
EMs	Emerging Markets
EPS	Electronic Payment Services
ESG	Environmental, Social and Governance
ESAAMLG	Eastern and Southern Africa Anti-Money Laundering Group
ETFs	Exchanges Traded Funds
EU	European Union
FATF	Financial Action Task Force
FCI	Foreign Company Index
FIA	Financial Intelligence Agency
Fintech	Financial Technology
FMI	Financial Market Infrastructure
FSAP	Financial Sector Assessment Programme
FSB	Financial Stability Board
FSC	Financial Stability Council
FSDS	Financial Sector Development Strategy
FSR	Financial Stability Report
FSSA	Financial System Stability Assessment
FX	Foreign Exchange
GCC	Gaborone City Council
GDP	Gross Domestic Product

GFSR	Global Financial Stability Report
GovI	Government Bond Index
IMF	International Monetary Fund
LTV	Loan-to-Value
MLGTA	Ministry of Local Government and Traditional Affairs
MMF	Money Market Fund
MoF	Ministry of Finance
MoPR	Monetary Policy Rate
MoU	Memorandum of Understanding
MPC	Monetary Policy Committee
MPR	Monetary Policy Report
MSME	Micro, Small, and Medium Enterprise
NBFI	Non-Bank Financial Institutions
NBFIRA	Non-Bank Financial Institutions Regulatory Authority
NCO	National Coordination Office
NFC	Non-Financial Corporate
NIIP	Net International Investment Position
NMMF	Non-Money Market Fund
NPL	Non-Performing Loan
NWDC	Northwest District Council
OFCs	Other Financial Corporations
PLR	Prime Lending Rate
RCG	Regional Consultative Group
RHS	Right Hand Side
RMCI	Real Monetary Conditions Index
SACU	Southern African Customs Union
SADC	Southern African Development Community
SDR	Special Drawing Rights
STR	Suspicious Transactions Report
SSA	Sub-Saharan Africa
UK	United Kingdom
USA	United States of America
USD	United States Dollar
VASP	Virtual Assets Service Provider
WEO	World Economic Outlook
ZAR	South African Rand

ACKNOWLEDGEMENT

The May 2026 issue of the Financial Stability Report (FSR) was prepared by the Bank of Botswana (the Bank) in collaboration with member institutions of the Financial Stability Council (FSC/Council) viz., Ministry of Finance (MoF), the Non-Bank Financial Institutions Regulatory Authority (NBFIRA), the Financial Intelligence Agency (FIA), the Deposit Insurance Scheme of Botswana (DISB) and the Botswana Stock Exchange Limited (BSEL). The Report was approved for publication by the FSC, a statutory body established by the Bank of Botswana (Amendment) Act, 2022 and with five members, being the Governor of the Bank of Botswana (Chairperson); Permanent Secretary of the Ministry of Finance; Chief Executive Officer, NBFIRA; Director General, FIA; and Director, DISB, while the Chief Executive Officer, BSEL, is an observer member, thus a non-voting member.



PREFACE

Purpose of the Report

The Financial Stability Report (FSR) provides an assessment of the vulnerabilities that could elevate risks to the stability and resilience of the Botswana financial system by the FSC. In turn, the Report includes statements on evaluation of financial stability in Botswana and, as necessary, an outline of any remedial measures to address risks, vulnerabilities and instability. The Report also provides analytical and performance updates for the financial sector, examining its impact on economic activity and welfare. In that regard, it enables information access to support stakeholders' interests and self-reflection on financial risk assessment processes, thus encourage public discourse and engagement on financial stability issues. The FSR is published twice a year following discussion and approval at the FSC meetings.

Macroprudential Policy Framework

The work of the FSC and publication of the FSR relates to implementation of the macroprudential policy framework. The primary objective of the framework is to limit systemic risk and its transmission to the broader economy. This is predicated on the observation and understanding that the financial system is interconnected, which manifests in transmission of risks within and among financial sector entities that can rapidly spill over into the real economy. At the same time, sectoral or broader economic weaknesses could adversely affect the financial system and trigger instability or cause a systemic financial crisis. In turn, this can lead to widespread disruption in the provision of financial services, with serious negative consequences for macroeconomic stability and the real economy.

To limit systemic and spill-over or contagion risks, financial sector regulators pursue a variety of key intermediate objectives, among others: minimising and mitigating excessive credit growth and leverage; mitigating and preventing significant maturity mismatches and market illiquidity; controlling structural vulnerabilities in the financial system that arise through interlinkages; limiting direct and indirect exposure concentrations for domestic systemically important financial institutions (D-SIFIs); reducing the systemic impact of misaligned incentives with a view to moderating moral hazard; monitoring systemic risks from activities outside the banking system implementing appropriate policy responses to contain such risks; as well as strengthening related infrastructure to mitigate aggregate shocks and to enhance resilience of the financial system.

Given the structure of the Botswana economy, the macroprudential policy framework recognises the external sector vulnerabilities of the domestic economy as emanating from trade shocks and capital flows and that these have the greatest potential for elevated financial stability risks. There are also potential risks to the stability of the domestic financial system emanating from economic and trade policy shifts and related disruptions induced by geopolitical tensions and geoeconomic fragmentation, as well as continued exposure to cyber threats due to the increasing integration of technology in finance, and the prevalence of climate-related financial risks. The FSR provides an analysis of these vulnerabilities, highlights where they persist and their interaction, as well as the potential impact and outlines responses to spillovers from regional and global financial stability developments and trends. Macroprudential indicators, complemented by financial soundness and macroeconomic indicators, are used to assess risks to and within the financial system. Relevant and appropriate macroprudential policy instruments and tools are available for intervention to mitigate risks and during periods of financial instability. The instruments and policy tools would be deployed or adjusted accordingly and timeously to mitigate the envisaged threats, and such interventions would be communicated through FSC circulars or by individual member regulators.

Decision-Making Process

The FSC, a multi-agency statutory body, was established under Section 20 (54B) of the Bank of Botswana (Amendment) Act, 2022, to, among others, collaborate and share information on financial sector vulnerabilities and risks, as well as policy and other related issues that strengthen the resilience of the financial system and make it more robust against financial stability risks. The FSC takes prompt action in response to a perceived build-up of systemic risks; ensures a

coordinated response to financial stability issues that may require cross-agency collaboration and information sharing and communicates systemic risk warnings to promote financial stability. The Governor chairs the FSC, and the Bank acts as the secretariat.

The work of the FSC was previously governed by a memorandum of understanding signed in February 2019, which has since been adapted into the FSC Charter.

Announcement of Macroprudential Policy Decisions

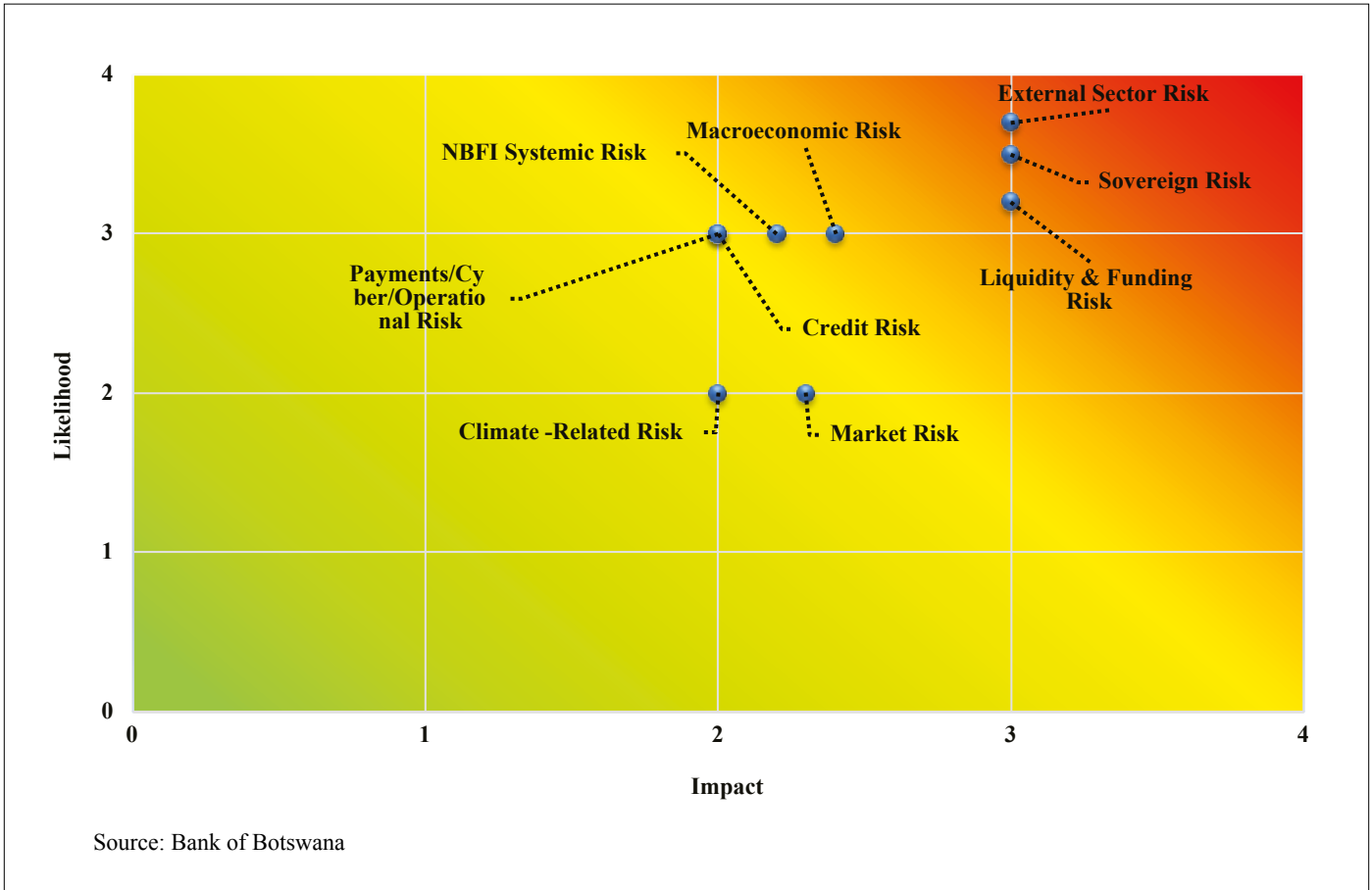
Proceedings of the FSC are communicated through a Press Release, shortly after a Council meeting, to inform the public of the discussions and conclusions on the stability of the domestic financial system. The Press Release further highlights the key risks in the financial system, recommendations and actions to address such vulnerabilities. Policy and regulatory decisions are communicated through a circular to all affected financial institutions. The circular provides a brief description that links the identified risk to the intermediate objective and explains how the measures taken are expected to mitigate the risk.

1. EXECUTIVE SUMMARY

- 1.1 Global financial stability in the first half of 2026 remains fragile** amid stretched asset valuations, rising sovereign debt burdens, and intensifying geopolitical fragmentation. While resilience has gradually been built into the global financial system, the intensity, duration, scale and consequences of the war in Middle East has brought new vulnerabilities, including energy and economic shocks, that could interact with and amplify existing ones. In addition, the growing systemic footprint of non bank financial institutions (NBFIs) continues to amplify liquidity, leverage, and valuation risks. These vulnerabilities heighten the probability of abrupt market corrections and associated asset price volatility as well as disorderly adjustments in global financial conditions. Credible fiscal consolidation, stronger NBFIs oversight, and international cooperation and coordination of financial stability reforms remain essential for safeguarding global financial stability.
- 1.2 Financial stability risks across Sub Saharan Africa (SSA) remain moderate** but increasingly sensitive to global shocks. High public debt burdens, tightening global financing conditions, and declining development finance flows continue to weaken policy buffers across the region. As sovereigns rely more heavily on domestic borrowing, rollover risks and sovereign–bank interlinkages have deepened, increasing liquidity pressures and the vulnerability of regional financial systems to sudden shifts in global risk sentiment.
- 1.3 Botswana’s financial system remains broadly stable**, supported by strong prudential capital and liquidity buffers, profitable institutions, and sound market infrastructures. However, vulnerabilities have risen as weaker external inflows, a prolonged diamond-market downturn, tighter fiscal conditions, and the low foreign-exchange reserves continue to weigh on the macro-financial environment. Liquidity pressures remain elevated and unevenly distributed across banks due to subdued government spending, and softer foreign-exchange inflows. Although interventions by the Bank, such as the reduction of the primary reserve requirement to zero, longer-term repo operations, and adjustments to foreign-exchange trading margins, have eased short-term liquidity pressures, structural weaknesses persist, including concentrated wholesale funding, elevated sovereign financing needs, and increased competition for deposits.
- 1.4 Credit growth has softened due to tighter liquidity** associated with weaker economic activity and more cautious bank risk appetite. Household credit growth slowed to 2.6 percent in December 2025 and remains dominated by unsecured borrowing, while corporate credit growth moderated to 6.6 percent as firms faced high borrowing costs and delayed government payments. Despite this slowdown, the non-performing loans (NPLs) ratio remains stable at 3.4 percent, and the negative credit-to-GDP gap indicates contained systemic credit risk. Sovereign vulnerabilities, however, have intensified and now represent a fundamental financial-stability concern given the central role of the state in domestic economic activity. In a sense, fiscal pressures, declining buffers, and rising reliance on domestic financing, including a USD 216.67 million syndicated bank loan, have deepened the sovereign–bank nexus, elevating rollover and liquidity risks, while recent rating downgrades underscore concerns about fiscal sustainability, subdued mineral revenues, and slow economic diversification efforts.
- 1.5 The Risk Assessment (Figure 1.1) complemented by the financial stability heatmap (Figure 4.1) indicates that systemic risk pressures remain elevated**, largely driven by sovereign vulnerabilities, tight liquidity conditions, external imbalances, and concentrated sectoral exposures. To preserve financial stability, policy priorities include enhancing coordinated macroprudential oversight through the FSC, structural reforms, rebuilding fiscal buffers and improving debt management, and preserving foreign exchange reserves to restore external resilience.
- 1.6 While Botswana’s financial system remains sound**, it is increasingly tested by amplifying external shocks, domestic structural weaknesses, deepening macro financial linkages, subdued domestic growth amid uncertain global outlook, alongside persistent liquidity pressures, structural funding weaknesses, climate-related risks, and sectoral vulnerabilities. Against this background, the FSC, at its meeting of 7 May 2026, noted ongoing measures by its member institutions to ease liquidity pressures, support orderly market functioning and preserve external stability. The measures underscore the need to maintain strong capital and liquidity buffers; enhance liquidity

risk management across financial institutions, including liquidity forecasting; strengthen stress-testing frameworks and building scenarios around the identified shocks; deepen macroprudential surveillance through intensified cross-sector monitoring of sovereign exposures across banks, pension funds and insurers; and reinforce policy coordination among regulatory authorities to maintain durable financial stability.

Figure 1.1: Summary of Risk Assessment



2. GLOBAL FINANCIAL STABILITY

- 2.1 Global financial stability in 2026 rests on a fragile equilibrium, where resilient headline indicators mask deeply interconnected structural vulnerabilities (Box 2.1). This duality is acutely visible in the shifting risk environment confronting central banks, where cyber threats and tariff-induced protectionism have transitioned from peripheral concerns to primary systemic anxieties. As authorities grapple with the dual pressures of rapid technological change and geopolitical fragmentation, resource constraints increasingly limit institutional capacity to respond effectively, transforming operational risks into broader macroeconomic headwinds.
- 2.2 Consequently, the projected global growth rate of approximately 3 percent is structurally uneven and precarious. The conflict in the Middle East serves as a primary transmission channel for this vulnerability, heightening commodity price volatility and tightening global financial conditions. While pockets of disinflation and localised technological gains offer temporary insulation, the narrow foundation of the current economic expansion leaves global output exposed to sudden geopolitical or financial shocks.
- 2.3 This friction at the macroeconomic level is widening global imbalances, which are no longer dictated by traditional economic fundamentals but by policy distortions, trade restrictions, and the deliberate reconfiguration of supply chains. Because these imbalances stem from political imperatives rather than market efficiencies, the traditional mechanisms for economic adjustment have become unstable. The resulting environment elevates the risk of sudden capital reversals and abrupt asset price corrections, exposing vulnerabilities in funding markets that are currently obscured by the backward-looking resilience of banking balance sheets.
- 2.4 These latent vulnerabilities are increasingly concentrated within NBFIs, which now command approximately 80 percent of cross-border debt flows to emerging markets. The structural reliance of NBFIs on short-term funding, paired with high leverage and regulatory opacity, creates a highly reactive environment where localised liquidity stress can instantly scale up. Because the boundaries between traditional banking and non-bank intermediation are deeply porous, any unwinding of leverage within the NBFIs sector threatens to trigger systemic spillovers across the wider financial complex.
- 2.5 The structural catalyst for this vulnerability is an accelerating wave of geo-fragmentation, as major economies systematically prioritise strategic autonomy over global economic efficiency. This deliberate segmentation of trade, investment, and capital flows inherently stokes domestic cost pressures and induces policy divergence among central banks. By fracturing the global safety net, this environment reduces the capacity of the international financial system to smoothly absorb liquidity shocks.
- 2.6 Within these fragmented markets, structural concentration has reached historical extremes, particularly in equity markets where artificial intelligence narratives drive an unprecedented share of total capitalisation. While this concentration reflects expectations for future productivity, it simultaneously narrows the market's support base and increases sensitivity to sentiment shifts. Given the leveraged nature of modern portfolios, a sharp correction in this highly concentrated tech assets could easily catalyse broader cross-border capital flight.
- 2.7 These compounding pressures ultimately converge in sovereign debt markets, where structural stability is facing its most complex test in years. Elevated sovereign borrowing requirements are colliding with a market composition that is increasingly dominated by price-sensitive, private-sector investors, that structurally elevate yield volatility. For emerging and frontier economies, this shift translates into higher refinancing costs and tighter dollar liquidity, leaving them highly exposed to disorderly market adjustments.
- 2.8 Ultimately, the global financial system operates as a highly interdependent network of mutually reinforcing risk variables. Managing this heightened risk profile requires an immediate evolution toward comprehensive macroprudential frameworks, granular data transparency within the non-bank financial sector, and renewed cross-border regulatory coordination to prevent localised volatility from compounding into global systemic disruption.

BOX 2.1

2025 FINANCIAL STABILITY BENCHMARKS

Central Banks Under Pressure in a Converging Risk Environment

Introduction: Central banks are navigating a convergence of significant financial risks. This benchmark report highlights the top emerging threats, their potential impact, and how institutions are responding to strengthen resilience in the year ahead.

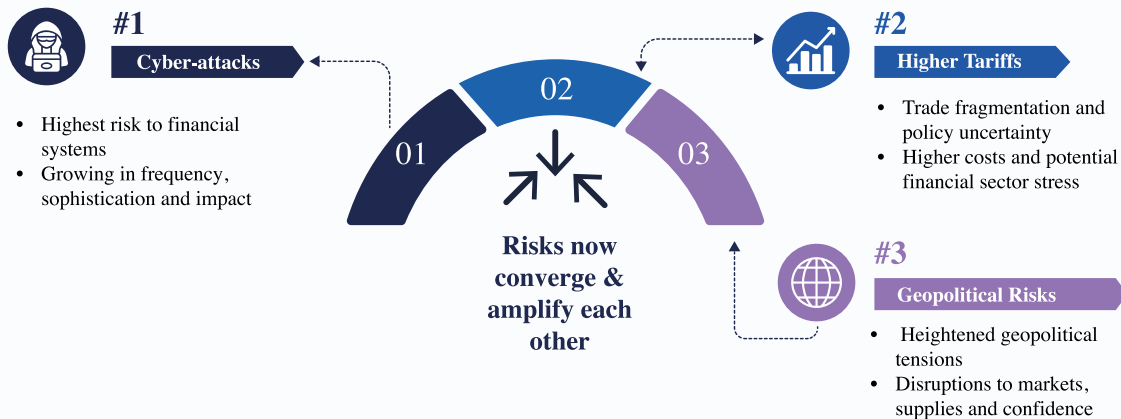
KEY RISK IMPACTS – 2025

These findings show risks are already materialising across jurisdictions.

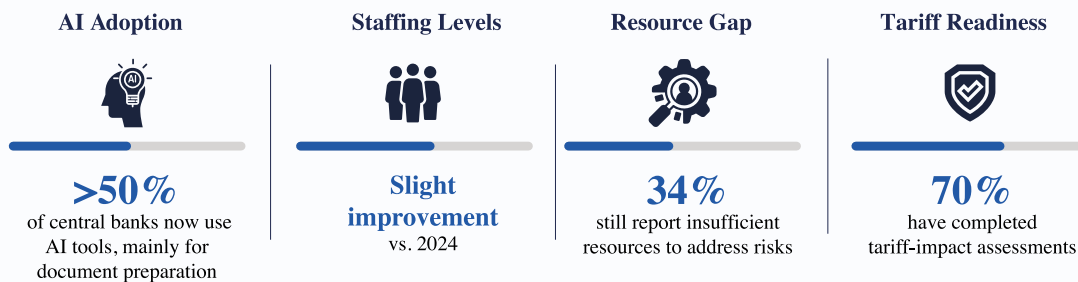


TOP RISKS (NEXT 12 MONTHS)

Ranked by level of concern. These risks are increasingly interconnected and can amplify one another.



HOW CENTRAL BANKS ARE RESPONDING



KEY TAKEAWAY
Financial stability risks are becoming more complex, connected, and immediate. Although central banks are making progress, ongoing capacity constraints highlight the need for stronger resources, better tools, and deeper risk analysis.

Source: Central Banking - Financial Stability Benchmarks 2025

3. REGIONAL FINANCIAL STABILITY

- 3.1 Financial stability risks in SSA are intensifying as structural sovereign debt pressures, restricted access to external capital, and pronounced growth asymmetries interact to form a reinforcing macro-financial cycle that is steadily weakening regional economic resilience. At the centre of this vulnerability lies a persistent sovereign debt challenge, with approximately twenty economies either in, or at high risk of, debt distress. This reflects structurally weak domestic revenue mobilisation, tax revenues averaging 13.8 percent of GDP, while interest payments absorb more than 12 percent of government revenues and exceed 25 percent in the most vulnerable countries. The resulting fiscal constraints limit governments' capacity to sustain investment or deploy countercyclical policy responses, pressures that are further amplified by external financial conditions. As prolonged global monetary tightening and elevated geopolitical risk aversion constrain access to international capital markets, many SSA sovereigns have shifted toward domestic borrowing, shortening debt maturities and raising financing costs.
- 3.2 This growing reliance on domestic financing has tightened the sovereign–bank nexus across the region, as banks expand their holdings of government securities and concentrate exposures on their balance sheets. While this provides near-term support for sovereign financing needs, it simultaneously crowds out private sector credit and weakens monetary policy transmission. More importantly, it creates a direct risk transmission channel, whereby further deterioration in sovereign creditworthiness can quickly weaken bank balance sheets and elevate the risk of financial sector stress. These vulnerabilities are further reinforced by uneven growth dynamics across the region, where a projected aggregate growth rate of 4.3 percent masks significant divergence. Oil-importing economies face rising import costs, exchange rate pressures, and inflation, while oil exporters continue to experience structural constraints in non-oil sectors. In contrast, economies benefiting from stronger prices for gold and agricultural exports have seen relatively improved external and fiscal positions. This divergence underscores the region's continued reliance on a narrow commodity export base, which amplifies the transmission of global shocks into domestic financial conditions.
- 3.3 These pressures are intensifying alongside a sustained contraction in external development financing. Declining official development assistance and reduced concessional funding reflect a structural shift in global financing conditions rather than a temporary adjustment. For many low-income SSA countries, this removes a critical source of stable long-term funding that has historically supported fiscal frameworks and external balances. In response, governments face increasingly constrained policy choices between reducing expenditure and increasing reliance on higher-cost domestic and commercial borrowing. Where borrowing is expanded, this further increases debt service burdens and refinancing risks; where expenditure is reduced, it weakens growth prospects and resilience to shocks. These fiscal pressures can also transmit into the financial system, including through the accumulation of public sector arrears that contribute to rising non-performing loans.
- 3.4 The macro-financial landscape that emerges is one in which sovereign stress, financial sector exposure, and diminishing external buffers have become tightly interconnected, reinforcing one another through the sovereign–bank link and commodity-related channels. Stabilising this environment requires moving beyond incremental adjustments toward a coordinated shift that combines stronger domestic revenue mobilisation with improved debt management and credible multilateral restructuring frameworks. Over time, reducing systemic vulnerability will depend on broadening domestic capital markets, weakening the feedback loop between sovereigns and banks, and diversifying economic structures to lessen dependence on commodity-driven financing cycles.

4. DOMESTIC FINANCIAL STABILITY

The financial system remains broadly resilient

4.1 The heatmap indicates that Botswana’s financial system continues to demonstrate overall resilience, with systemic risk contained at moderate levels (figure 4.1). The banking sector remains stable, supported by strong profitability and contained solvency risks. However, this stability coexists with a clear concentration of risks in specific segments, most notably within NBFIs. The persistent elevation of NBFI contagion and solvency indicators stands out as the dominant feature of current conditions, creating a system that is stable at its core but increasingly exposed to vulnerabilities in key transmission nodes. Systemic risk is therefore not widespread, but more concentrated and structurally embedded, increasing the system’s sensitivity to shocks.

4.2 The elevated risk signals in the NBFI sector should not be interpreted as evidence of financial distress. NBFIs remain profitable, solvent, and operationally sound, with no indication of balance sheet deterioration. Instead, the heatmap reflects their systemic importance and interconnectedness, particularly their role in financial intermediation, capital formation and liquidity provision. The elevated contagion and solvency indicators therefore signal exposure to system-wide transmission risks rather than firm-level fragility. The concern is that, given their scale and linkages, NBFIs are positioned to amplify shocks across the financial system even if they are not themselves the source of stress.

NBFI deposits a key source of systemic liquidity risk

4.3 A central vulnerability arises from the high concentration of wholesale deposits from NBFIs within the banking system. Banks rely significantly on deposits placed by pension funds, insurers, and other institutional investors, creating a funding structure that is stable under normal conditions but inherently sensitive to changes in NBFI behaviour under a stressed liquidity environment. Adjustments in asset allocation or liquidity preferences within NBFIs can result in large and rapid withdrawal of deposits, tightening banking system liquidity and increasing funding costs. This channel is particularly important because it operates even in the absence of stress within NBFIs themselves. Changes in portfolio strategy, rebalancing decisions, or precautionary increases in liquidity buffers can be sufficient to

trigger funding pressures within banks. As such, the systemic concern is rooted less in the health of individual institutions and more in the structure of funding relationships across the financial system. This implies that financial stability risks can emerge from normal portfolio adjustments and liquidity management behaviour, increasing the likelihood that liquidity pressures develop and propagate even without an originating shock in institutional balance sheets.

NBFI dominance heightens exposure to market shocks

4.4 The expanding size of the NBFI sector, reflected in its rising assets-to-GDP ratio, has further increased its systemic importance. As NBFIs account for a larger share of financial system assets, their interactions with banks, financial markets, and the real economy become more consequential. This deepening interconnectedness means that even modest adjustments in NBFI sectoral strategies can have amplified effects across the system, particularly through market-based transmission mechanisms such as asset price movements and changes in liquidity conditions. The heatmap’s elevated contagion indicators are consistent with this increased network complexity, where systemic risk gets shaped by scale and interconnectedness, rather than firm-specific fundamentals.

4.5 Current conditions reflect the interaction between these structural characteristics and a set of ongoing cyclical pressures. Tight domestic liquidity conditions, volatile foreign exchange flows, external financial pressures, and moderate real-sector strain affecting household and corporate cash flows combine to reinforce underlying vulnerabilities. The heatmap captures this through persistent, though not extreme, signals across funding, global, and real-sector indicators, pointing to a system that remains stable but is increasingly sensitive to changing financial conditions.

Entrenched transmission channels amplify spillover risk

4.6 The configuration of risks suggests that the financial system is increasingly exposed to identifiable and active transmission channels. Changes in NBFI behaviour—particularly in deposit placement and

investment allocation—can quickly affect banking sector liquidity and funding costs. These pressures are then transmitted to the real economy through tighter credit conditions, with implications for investment, consumption, and overall economic activity. Specifically, elevated funding costs feed through into higher lending rates, with the resultantly higher borrowing costs weighing on credit growth, particularly for households and non-financial corporates. This effectively links funding-side pressures directly to real-sector outcomes through a credit channel and the persistent elevation in banking funding risk within the heatmap reflects this structural dependence.

- 4.7 A feedback loop may emerge as weaker economic conditions increase credit risk and place further strain on financial institutions. External shocks, including those affecting foreign exchange inflows and global risk premia, can further intensify these dynamics by tightening domestic liquidity and amplifying funding pressures with broader systemic impact.

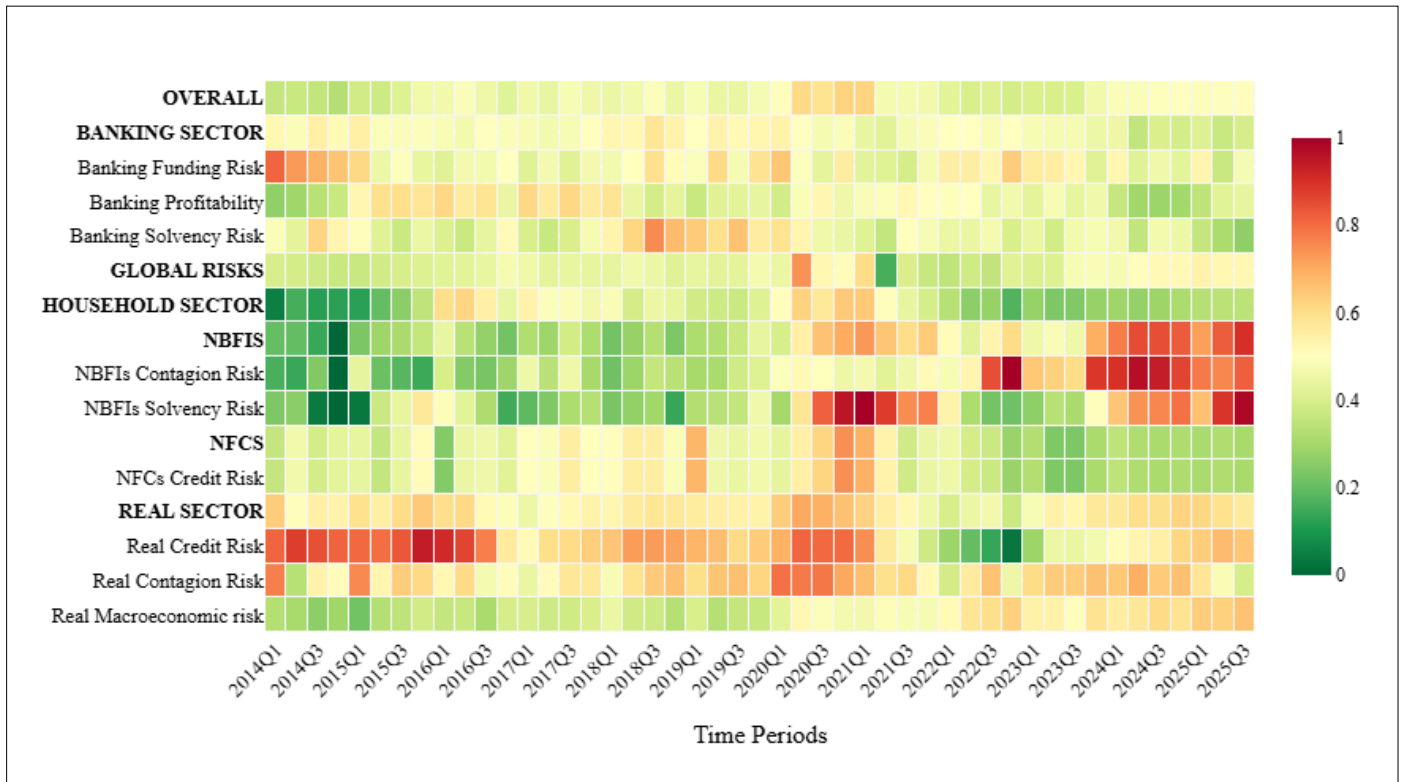
Outlook is stable, but shock sensitivity has risen

- 4.8 Under baseline conditions, the financial system is expected to remain resilient, supported by strong banking buffers and sound NBFIs balance sheets. However, the current configuration suggests that risks are tilted toward transmission, in speed and reach, rather than new sources of stress. Should shocks materialise - whether from external financial tightening, shifts in capital flows, or renewed domestic liquidity pressures - the initial impact is likely to arise through adjustments in NBFIs strategies, particularly in their funding and investment decisions.
- 4.9 Overall, the heatmap indicates that Botswana's financial system remains fundamentally sound, but systemic risk is increasingly shaped by structural characteristics related to the size, concentration, and interconnectedness of NBFIs. The key policy challenge is to ensure that the growing dominance of NBFIs and their role as major liquidity providers do not become channels for amplifying shocks across the system. Maintaining stability will depend on close monitoring of funding concentration, system-wide liquidity conditions, and cross-sector linkages to ensure that localised stresses do not escalate into broader systemic disruption.

Financial integrity risks remain a moderate vulnerability

- 4.10 The National Money Laundering and Terrorist Financing Risk Assessment (NRA) of October 2025 indicates that Botswana's financial system faces moderate but manageable risks to financial integrity, driven primarily by money-laundering threats rather than terrorist financing. These risks originate from activities such as tax crimes, fraud, corruption, environmental offences, and the misuse of corporate vehicles, and are transmitted through key sectors including the banking system, real estate, NBFIs, and selected designated non-financial businesses and professions (DNFBPs). While core financial institutions operate within a relatively robust AML/CFT framework, vulnerabilities persist in areas characterised by cash-intensive activity, complex ownership structures, and uneven supervisory coverage, particularly among DNFBPs.
- 4.11 Although these risks are primarily conduct-and integrity-based rather than prudential in nature, they stay relevant to the prevailing systemic risk environment given the interdependencies between market confidence and operational performance. The increasing use of digital financial products and virtual assets further elevates monitoring challenges. The finalisation of the AML/CFT National Strategy 2025–2030, alongside legislative reforms that have strengthened FATF compliance, represents an important step toward mitigating these risks by enhancing supervisory coordination and reinforcing system-wide integrity.

Figure 4.1: Botswana Financial System Heatmap

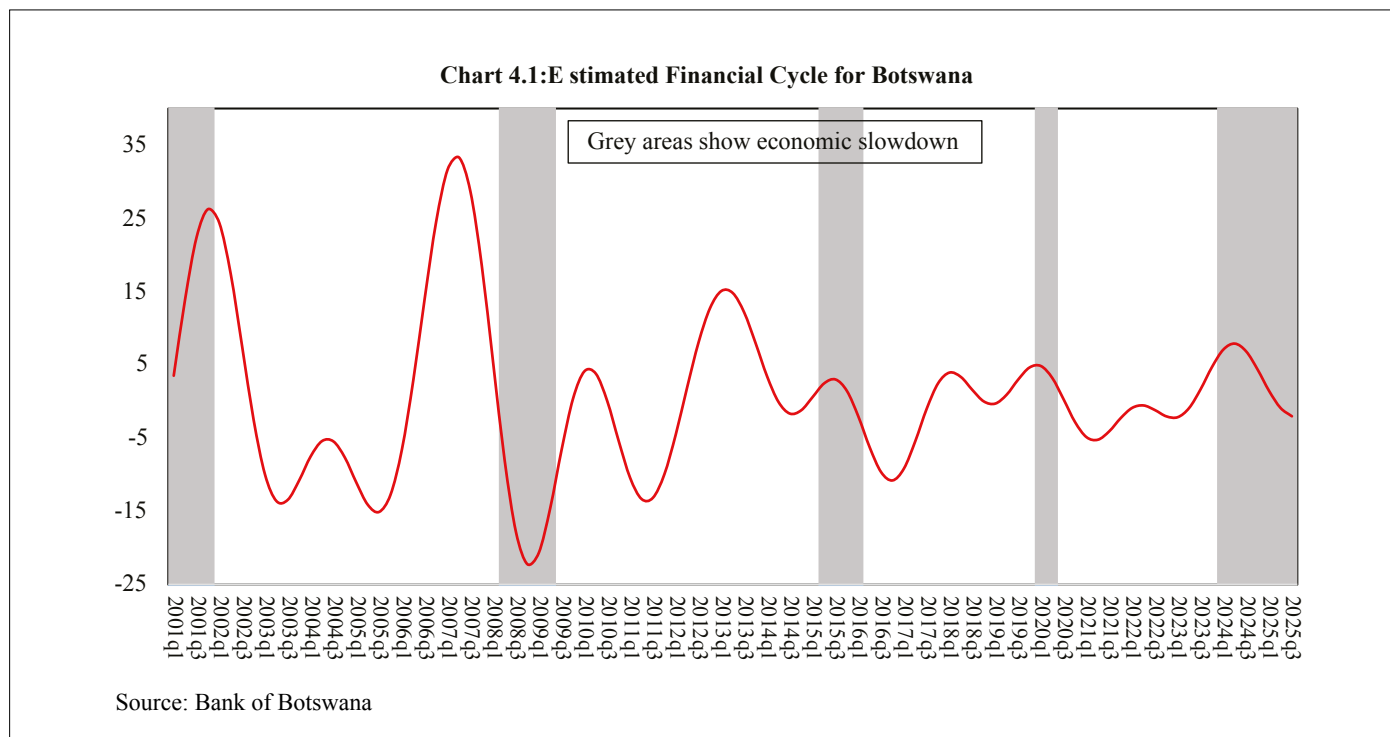


Financial cycle evolution signals systemic deterioration

4.12 The financial cycle is trending downward, reflecting weakening financial conditions amid tightening liquidity, increasingly stringent credit standards, and heightened uncertainty associated with fiscal pressures and subdued economic activity. The downturn signals a decline in risk appetite among banks, which are prioritising balance sheet resilience over credit expansion. These pressures are being amplified by a persistent liquidity squeeze in the banking system, driven by net foreign exchange outflows and reduced government spending, which remains the primary source of systemic liquidity. Continued liquidity shortages, together with ongoing reliance on central bank support, point to heightened fragility in the financial system.

4.13 The softening financial cycle heightens concerns around credit risk, particularly in the context of elevated household indebtedness and weak income growth, which increase the likelihood of rising defaults and pressure on bank profitability. Liquidity constraints are also expected to intensify funding risks, while fiscal consolidation is likely to dampen credit demand. In response, banks are expected to tighten lending standards further, resulting in slower credit growth, potential deterioration in asset quality, and increased short term reliance on emergency liquidity facilities. Against this backdrop, proactive measures, including strengthening macroprudential buffers, enhancing contingency planning, and supporting economic diversification, will be critical to safeguarding financial stability.

Chart 4.1: Estimated Financial Cycle for Botswana



5. SOVEREIGN RISKS

Fiscal pressures remain a potential source of systemic risk

- 5.1 Botswana's sovereign risk position has tightened, prompting increased reliance on domestic borrowing to support near-term budget financing. While these measures have provided temporary relief to fiscal pressures and supported government financing needs, they have also contributed to a rising stock of interest-bearing obligations and increased exposure to refinancing and interest rate risks. In anticipation of further pressures, Government has sought to raise the statutory public debt ceiling from 40 to 60 percent of GDP, with public debt projected to rise to 44.7 percent of GDP by March 2027.
- 5.2 These developments point to a deepening sovereign-bank nexus, as banks' balance sheets become more intricately linked to government financing requirements in an already tight liquidity environment. Increased domestic borrowing, particularly through short-term facilities, has intensified competition for liquidity, raising funding costs and at the risk of crowding out private sector credit. While these measures have helped manage immediate public financing constraints, they do not resolve underlying fiscal imbalances, and continued reliance on them could amplify rollover and liquidity risks over time.
- 5.3 The decline in foreign exchange reserves and government cash balances has further contributed to uneven liquidity conditions, increasing reliance on central bank operations to manage short-term pressures. Should fiscal pressures persist, including through weaker revenues or elevated refinancing needs, spillovers could materialise through tighter liquidity, higher sovereign risk premia, and reduced investor confidence. In this context, sustaining financial stability will require a gradual shift from short-term financing measures towards sustained fiscal consolidation, supported by a credible debt management strategy, to address structural imbalances and mitigate sovereign-related risks.

Downgrade pressures, but creditworthiness remains strong

- 5.4 In March 2026, S&P Global Ratings downgraded Botswana's long-term foreign and local currency sovereign ratings from BBB to BBB-, maintaining a

negative outlook. The downgrade reflects concerns related to prolonged structural and market weakness. In October 2025, Moody's Investors Service affirmed Botswana's Baa1 rating but retained a negative outlook, citing risks associated with weak mineral revenues and constrained fiscal space.

- 5.5 While these developments highlight emerging pressures and a deterioration in the outlook, they do not instantly translate to a fundamental weakening of the country's creditworthiness. Botswana's sovereign rating remains investment grade and comparatively favourable, supported by a track record of prudent macroeconomic management and institutional strength. Nonetheless, the downgrade serves as a forward-looking signal of rising vulnerabilities, reinforcing the need to address underlying fiscal and structural constraints to safeguard credit strength over the medium term.

Coordinated policy action is critical for stability and confidence

- 5.6 The evolving sovereign risk environment underscores the need for coordinated and well sequenced policy action across fiscal, and financial sector domains. Immediate priorities include rebuilding fiscal buffers, anchoring debt on a sustainable path, and strengthening public financial management to enhance spending efficiency and medium-term debt planning. At the same time, advancing structural reforms under NDP 12 and the Botswana Economic Transformation Programme (BETP) will be critical to diversifying the economic base and reducing reliance on volatile mineral revenues.
- 5.7 Effective coordination is also needed to balance investor attraction with the preservation of financial integrity, ensuring that efforts to deepen financial markets and mobilise investment are supported by robust governance, AML/CFT frameworks, and supervisory oversight. Furthermore, maintaining exchange rate stability and adequate reserves, alongside proactive engagement with rating agencies, will further support confidence and safeguard investment grade status. Taken together, these measures highlight that sustained financial stability depends not only on individual policy actions, but on their coherence, consistency, and alignment over the medium term.

BOX 5.1: FISCAL POLICY IMPLICATIONS FOR FINANCIAL STABILITY - A LOOK AT THE 2026 BUDGET SPEECH

a) Introduction

Botswana's 2026 Budget Speech, presented under the theme "A New Era of Economic Transformation and Fiscal Prudence", reflects the government's commitment to structural and fiscal administration reform. The expansionary budget is meant to revive economic activity, however, with potential negative ramifications for the financial sector through increased vulnerabilities. These include widening fiscal deficits and rising public debt amid low foreign exchange reserves, and the Government's recent decision to raise a United States Dollar (USD) syndicated loan from domestic banks. Contemporaneously, linkages between the sovereign, commercial banks, and NBFIs are strengthening, elevating the contagion risk and the potential for rapid transmission of systemic risk. The evolving macro-financial landscape underscores the importance of policy coherence and prudent debt management to protect confidence in the Pula and maintain economic and financial stability.

b) Fiscal Deficit Dynamics and Financial System Liquidity

The fiscal deficit is projected to widen by P4.23 billion to P26.35 billion in 2026/27, accounting for 8.9 percent of GDP and consequently placing greater demand on domestic funding sources. As government financing requirements expand, commercial banks are increasingly absorbing government securities, exposing them to sovereign default risk. The deepening sovereign-bank nexus has the potential to tighten liquidity conditions through the reduction of loanable funds available to the private sector and intensifying competition for domestic deposits as banks channel more resources towards supporting the fiscal budget. In turn, this pressure can influence sovereign yields and heighten the dependence of the fiscal framework on the banking sector's balance sheet.

The introduction of a USD denominated syndicated loan from domestic banks piles additional pressure on banks' liquidity due to hedging requirements. This can reduce the availability of Pula liquidity, accentuate competition for domestic deposits, and intensify the disconnect between the prime lending rate and the monetary policy rate through high funding costs. These dynamics heighten the sensitivity of bank balance sheets to sovereign stress, while also raising the risk that liquidity pressures in the banking system could feed back into the government's borrowing cost and increase the cost of debt.

c) Tax Reforms and Financial Stability

The government's tax reform, including the modernisation of the value added tax (VAT), income tax and customs legislation is designed to strengthen revenue administration, broaden the tax base and enhance the predictability of fiscal revenues. These reforms are complemented by the expected 2.5 percent increase in personal income tax for individuals earning above P400 001 per annum and the 3 percent increase in the corporate income tax rate. In combination with digitalisation measures such as electronic invoicing, domestic revenue mobilisation is expected to be more efficient, and volatility reduced in the medium term, reinforcing efforts towards fiscal consolidation. However, while the revenue outlook is strengthened, tax increases may negatively affect household disposable incomes and corporate cash flows, potentially moderating credit demand and investment appetite, particularly in an environment where liquidity conditions are tight. As such, the reforms provide important medium-term support for fiscal sustainability yet warranting close monitoring to ensure balanced outcomes on credit intermediation and broader macro-financial stability. Over time, a robust revenue base will help strengthen fiscal buffers and reduce the risk of government resorting to increasingly large and potentially disruptive borrowings from banks and pension funds.

d) Public Debt Trajectory and Sovereign Risk Assessment

Botswana's public debt stood at P90.03 billion in 2025, equivalent to 33.0 percent of GDP, and is projected to reach 38.8 percent of GDP by March 2026. Given the expected breach of the statutory debt limit in the 2026/27 fiscal year, Government, through the Stock, Bonds and Treasury Bills (Amendment) Bill, 2026, is seeking to raise the debt ceiling from 40 percent to 60 percent of GDP to create fiscal headroom amid the diamond market downturn. Meanwhile, the cost of servicing the growing stock of debt could become increasingly burdensome in line with the rise in the monetary policy rate. Further, the decision to issue a sizeable USD denominated loan increases the sovereign's exposure to exchange rate risk, as government revenues are increasingly earned in Pula, except in periods where diamond and other mineral revenues recover sufficiently to provide foreign currency buffer. Any depreciation of the currency would therefore, increase debt service costs and exacerbate fiscal pressures. This dynamic intensifies the sovereign-bank nexus, increasing the potential

for two-way transmission of stress and raising broader concerns about the resilience of the financial system should fiscal conditions deteriorate further. These vulnerabilities are compounded by recent sovereign credit rating downgrades by both S&P Global Ratings (March 2026) and Moody's Investor Services (October 2025) that may elevate the government's borrowing costs, while weakening investor confidence.

e) External Buffers and Contagion Channels

Foreign exchange reserves are low relative to historical standards and were around P55.9 billion in March 2026, equivalent to 7.3 months of import cover of goods and services and reflecting sustained pressure on Botswana's external position. In the context and along with tightening global financial conditions, government's expanding financing requirements have increased the likelihood that pension funds will assume a more prominent role in absorbing domestic sovereign issuance, in the process, deepening concentration risk across the financial system. Moreover, pension funds are already interconnected with commercial banks through deposit placements, capital formation and liquidity provisions. Thus, rising sovereign exposure increases the probability that fiscal or exchange rate-induced shocks could propagate simultaneously through banks and non-banks.

With commercial banks holding significant volumes of government securities, reflected in increased uptake of treasury bills and bonds following the 2025 investor roadshow, additional fiscal tightening or pressure on the Pula could lead to correlated valuation losses, increasing system-wide vulnerability. Strengthening buffers, improving debt management and enhancing sectoral surveillance remain critical in limiting contagion risks.

f) Conclusion

The 2026/27 budget portrays ambitious long-term reforms aimed at strengthening economic sustainability, yet significant short-term vulnerabilities remain. The widening fiscal deficit, rising public debt, a weakened external position and increased reliance on foreign currency borrowing contribute to an increasingly complex risk environment. At the same time, the deepening interconnection between the Government, commercial banks and NBFIs amplifies contagion risk and heightens system-wide sensitivity to shocks. In this context, the FSC will continue to play an important coordinating role by enhancing cross-sectoral surveillance, facilitating timely information sharing and ensuring that fiscal, monetary and regulatory actions remain coherent and mutually reinforcing. Maintaining confidence in the Pula, safeguarding institutional balance sheets and preserving financial stability will therefore, require disciplined fiscal management, strengthened revenue administration and effective policy coordination anchored through the FSC.

6. CREDIT AND LEVERAGE RISKS

Commercial Bank Credit

Commercial bank credit growth trends downwards

6.1 Annual growth in commercial bank credit has trended downwards since October 2025, registering a growth of 2.6 percent in February 2026 down from 5.8 percent in the corresponding period in 2025. This is consistent with the subdued economic landscape where firms and households face tighter financing conditions as banks take prudent measures to maintain credit quality amid heightened economic uncertainty. The lower uptake of credit was attributable to a lower uptake of overdraft and revolving credit facilities by businesses, notably parastatals, as well as minimal acquisition of mortgage and motor vehicle loans by households. Meanwhile, credit quality was relatively unchanged, with an NPLs ratio of 3.4 percent in December 2024 and 2025.

Household Borrowing

Household credit growth weakens

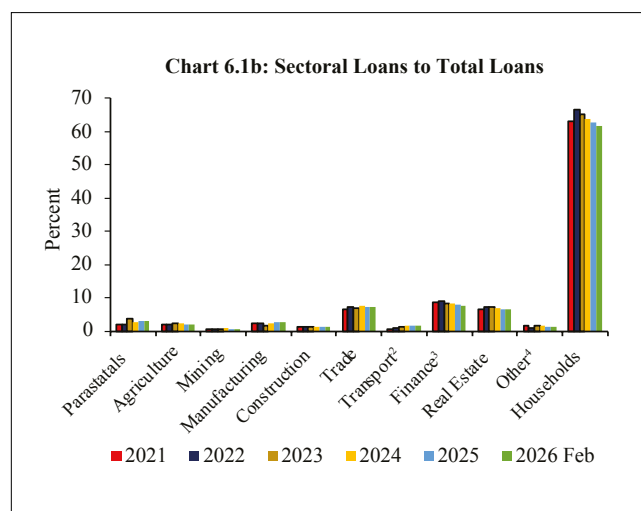
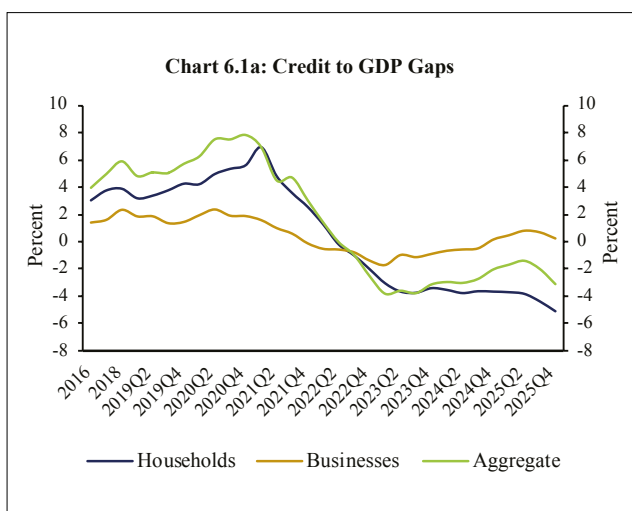
6.2 Consistent with the prevailing macroeconomic landscape and the tighter lending conditions by banks, borrowing by the household sector, a key driver of total credit, has declined significantly since

2022. The growth in household credit ranged between 2 to 6 percent in recent years, from highs of 30 percent in the pre-Covid 19 era. Household credit growth reached 7.7 percent in June 2025, before drastically declining to 0.02 percent in December 2025 (Chart 6.4a). Notably, more expensive unsecured loans continued to dominate household credit at 69.4 percent (Chart 6.4d), while the overall household credit accounted for 62.6 percent of total credit, compared to 36.1 percent for business credit (Chart 6.2b).

6.3 In view of these trends and supported by a negative credit-to-GDP gap, credit developments currently pose limited risks to financial stability. The gap which has widened further from -2 percent in the fourth quarter of 2024 to -3.1 percent in the fourth quarter of 2025, indicates the absence of rapid and excessive credit growth that could cause a credit bubble, but rather suggestive of room for prudent credit extension to sustain economic activity (Chart 6.1a). Similarly, risks to credit are mitigated by deductions from source scheme arrangements for public sector employees, who account for a greater proportion of borrowing by households.

Banking Sector Loans

Proportion of household loans high in commercial banks' loan portfolio



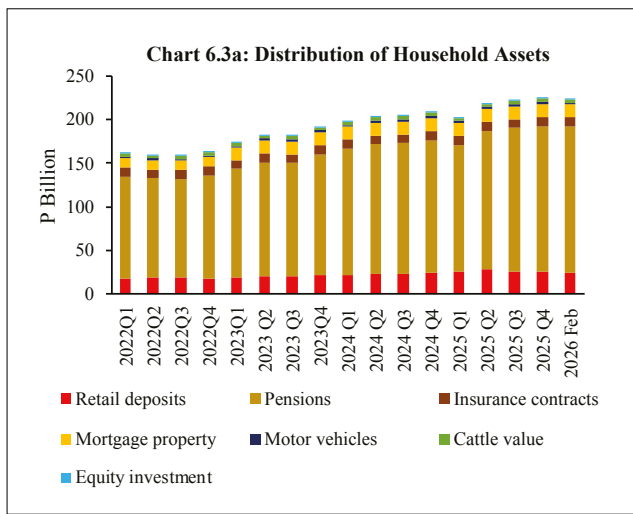
Source: Bank of Botswana

6.4 On the other hand, households are net savers when considering their non-discretionary contractual long-term pension savings and other assets (Chart 6.3a). Pension assets are important for mortgage debt relief under the Retirement Funds Act of 2022 but also improve the long-term financial welfare of households and in general, underpin wealth creation and financial security for retirees. Chart 6.3b

indicates a positive net worth of households, which indicates a healthy financial standing. The estimated net worth of households as a percentage of GDP was 59.6 percent in the fourth quarter of 2025 compared to 55.2 percent in the corresponding period in 2024, reflecting a higher increase in net worth compared to the growth in GDP.

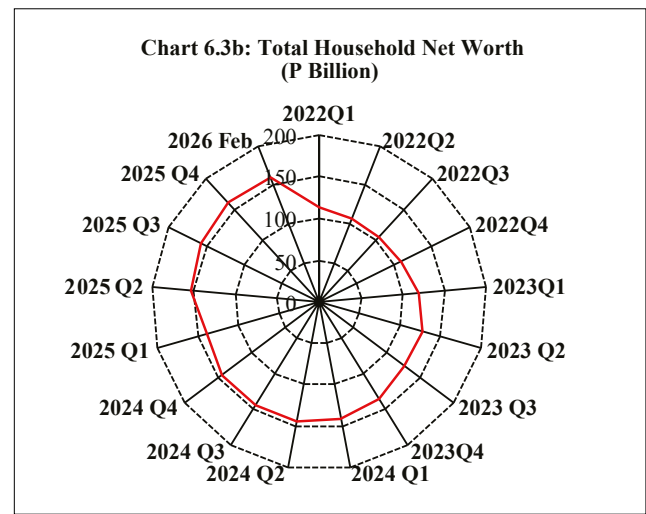
Household Net Worth Estimation

Pension savings dominate household assets



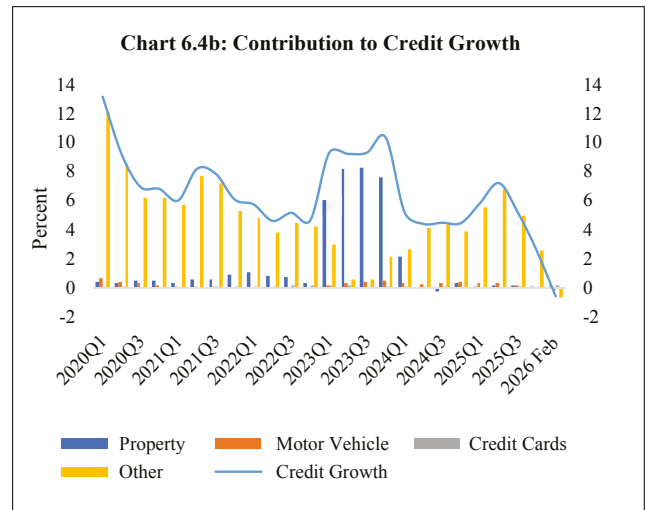
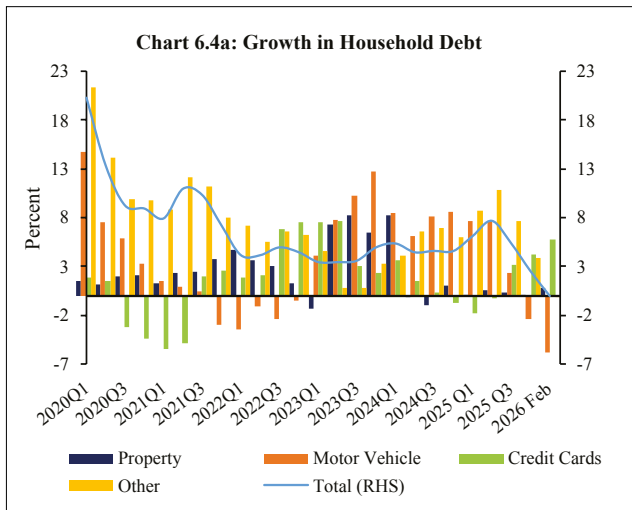
Source: Bank of Botswana

Households' net worth is increasing

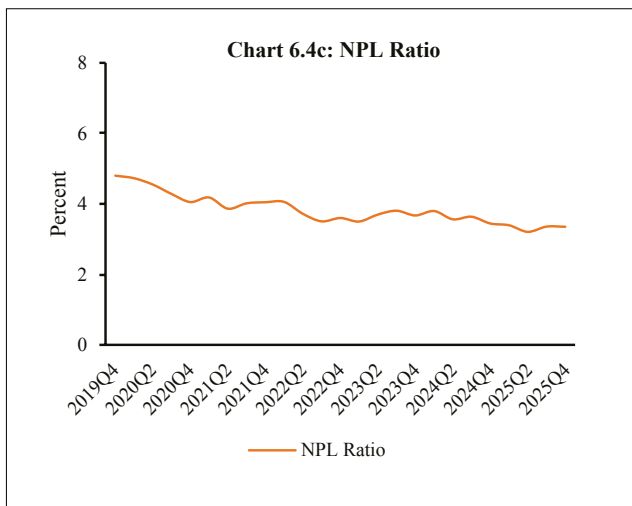


Household Debt Analysis

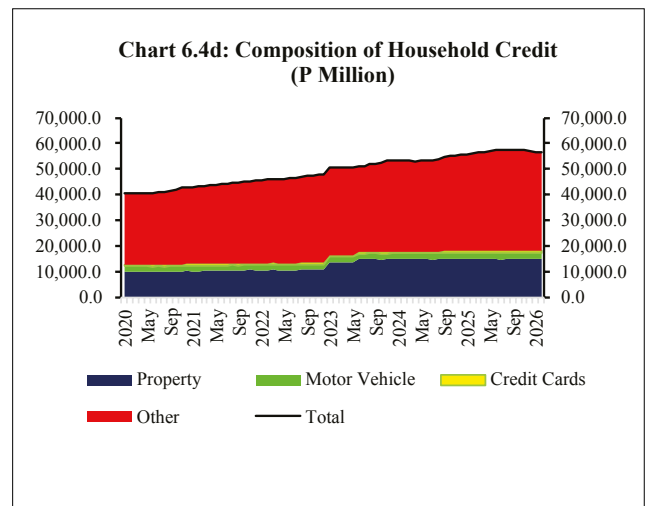
Personal loans (other) are the major driver of household credit growth



Both the debt burden and default rates are decreasing



Personal loans dominate household debt



Source: Bank of Botswana

Non-Financial Corporates Credit

Corporate sector borrowing holds steady

6.5 Corporate loan demand remained strong albeit constrained by high interest rates and delayed payments from the government and state-owned enterprises. Corporate credit grew by 5.8 percent in February 2026, a contraction from 8.4 percent in the corresponding period in 2025. The demand for credit was driven by working capital needs to meet day-to-day expenses across firms of all sizes, as well as inventory financing due to strained cashflows

following cost containment measures by government, such as reduced issuance of purchase orders.

6.6 Proportionally, corporate loans to total commercial bank credit rose marginally from 32.4 percent to 33.4 percent between December 2024 and December 2025. Relative to GDP, bank credit to the corporate sector was 11.1 percent in December 2025 from 10.8 percent in December 2024 and remains low by regional standards. Chart 6.1a shows corporate sector credit dynamics as disconnected from real economic activity, highlighting vulnerabilities that have the

potential to propagate through concentration and leverage rather than broad-based credit expansion. Mining and construction activities are highly volatile thus attract little credit, so shocks in these sectors transmit mainly through external channels such as commodity prices and foreign investment, leading to fiscal stress and liquidity squeeze. In contrast, trade and real estate sectors dominate the corporate loan book, exposing banks to domestic demand shocks. Tighter capital requirements for infrastructure exposures, enhanced liquidity monitoring, limits on concentrated lending, forward-looking provisioning, and the gradual integration of countercyclical buffers supported by improved data infrastructure are all necessary in mitigating any potential vulnerabilities.

Property Market Credit

Secured lending to households decelerates

- 6.7 Household demand for mortgage and residential property facilities was low owing to higher pricing costs and reduced affordability as spreads widened in line with price adjustments commensurate with rising funding and liquidity constraints in the market. Additionally, appetite for secured lending by banks weakened in response to repayment risk from government schemes as government continues to grapple with fiscal constraints.
- 6.8 Residential real estate loans increased marginally from P15.4 billion in February 2025 to P15.6 billion in February 2026, constituting 25.7 percent and 16.4 percent of total household credit and total credit, respectively (Chart 6.5a). These proportions are very low compared to Namibia, where mortgages constituted 66.4² percent of total household loans, which suggests that the level of domestic housing finance is not commensurate with the needed development and growth path to fill the apparent need for housing, as well as the financing gap. At the same time, growth in incomes could be restrained relative to the increase in residential house prices over the years (possibly reflecting limited housing

stock in various categories, or availability of land and affordability of building materials).

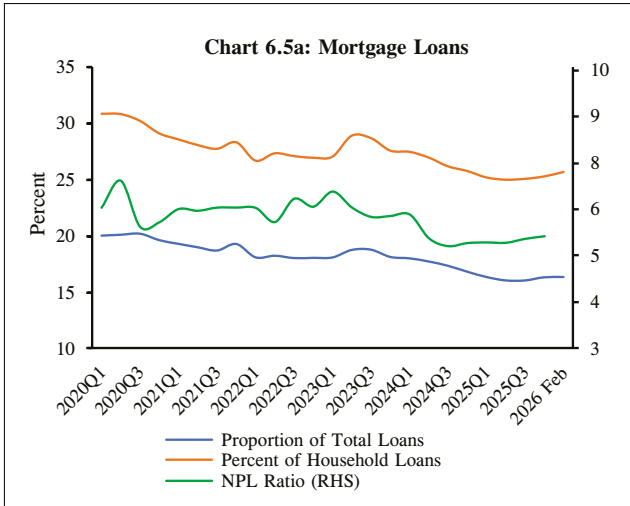
Credit risk from mortgage lending contained

- 6.9 Credit risk in the mortgage sub-sector remains broadly contained, supported by commercial banks maintaining moderate loan-to-value (LTV) ratios, as well as the self-collateralised nature of real estate exposures. In 2025, mortgage lending remained concentrated in low LTV segments, which translated into safer lending practices and minimised potential losses by banks in the event of borrower default (Chart 6.6). Meanwhile, the proportion of impaired mortgage loans to total mortgage loans increased marginally from 5.6 percent in December 2024 to 5.8 percent in December 2025, reflecting, in part, financial pressures arising from the subdued macroeconomic environment.
- 6.10 While these developments are not indicative of systemic stress, the emergence of marginal deterioration in asset quality underscores the need for heightened macroprudential vigilance to mitigate incipient risk build-up. In this context, consideration may be given to the introduction of indicative LTV benchmarks or enhanced supervisory oversight of higher-LTV exposures, as part of a forward-looking and proportionate policy approach aimed at preserving the resilience of the mortgage sub-sector amid a weak economic environment.

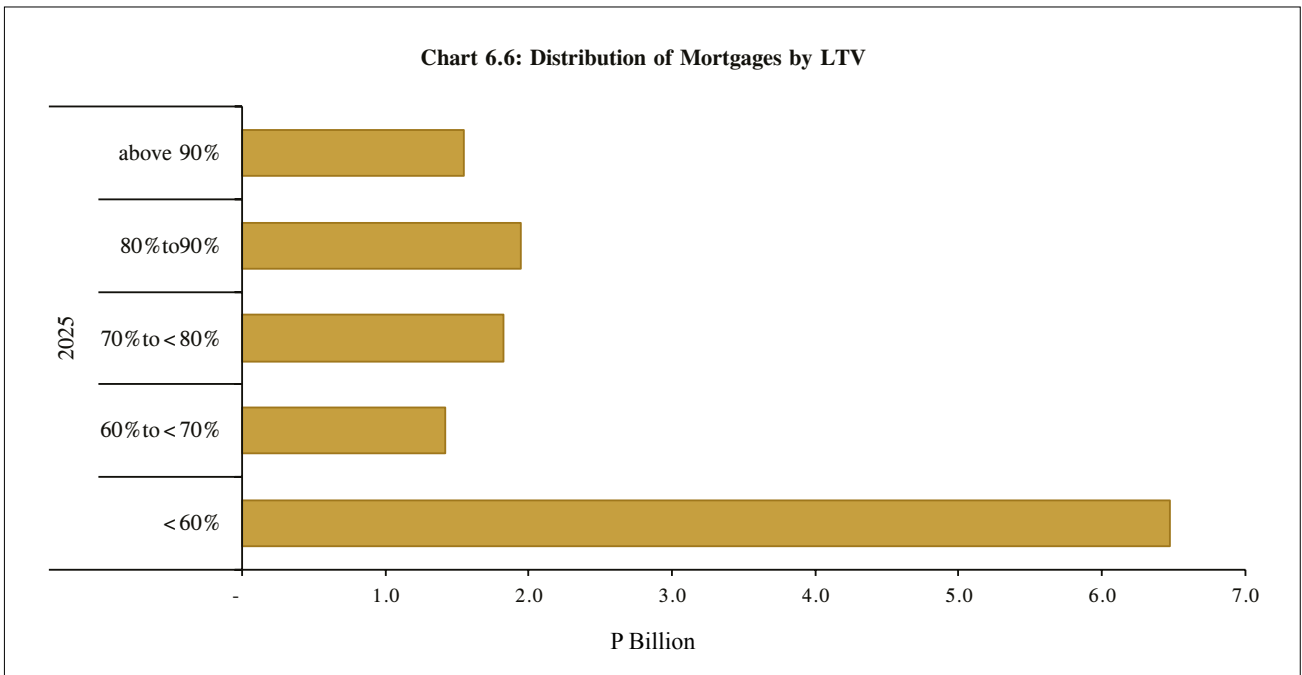
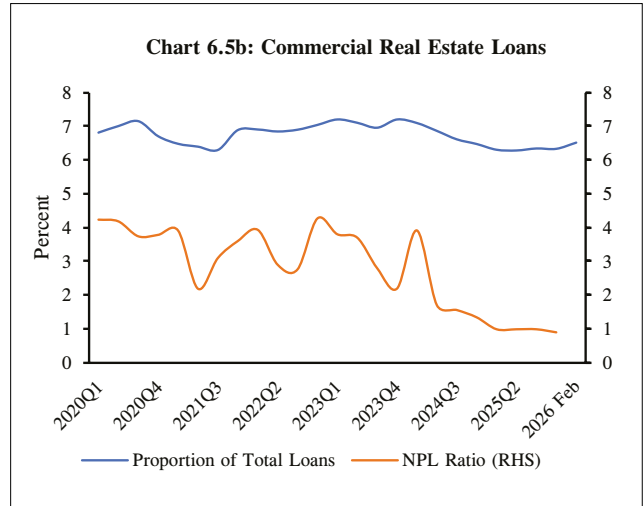
2. Bank of Namibia Financial Stability Report, October 2025

Property Market Developments

Mortgages as a percentage of both total loans and household loans and the NPL ratio are stable



The proportion of CRE loans to total loans is stable and the NPL ratio is modest



Source: Bank of Botswana

7. LIQUIDITY AND FUNDING RISK

Banking Sector Liquidity and Funding

Market liquidity is improving but remains subdued

- 7.1 Average daily market liquidity improved significantly over the twelve months to March 2026, rising from P764 million to P7.5 billion, largely supported by government spending supported by SACU inflows. Despite this improvement, liquidity conditions remain unevenly distributed, and funding costs continue to be elevated, reflecting structural constraints and deposit concentration within the system.
- 7.2 These conditions have contributed to the widening of lending margins above Prime Lending Rates, indicating weakened monetary policy transmission and tighter effective borrowing conditions, with implications for credit growth. While recent monetary policy measures have supported liquidity management, the coexistence of improved liquidity levels and elevated funding costs highlights underlying structural fragilities, particularly the financial system's sensitivity to shifts in funding and liquidity flows, posing risk to financial stability.

Deposit concentration exposes banks to funding risks

- 7.3 The banking sector remains vulnerable to funding risk arising from a concentrated deposit base as reflected in the top 20 deposits³ to total deposits ratio of 39.8 percent in March 2026 from 39.1 percent in March 2025. This increase underscores heightened vulnerability to sudden withdrawal pressures and the potential for increased funding costs, given the inherently volatile and expensive nature of wholesale deposits. Looking ahead, to further mitigate potential financial stability risks while enhancing policy transmission, commercial banks with elevated deposit concentration may be required to hold additional capital. This would align with the regulatory capital standards under Basel III.
- 7.4 That notwithstanding, the banking industry continues to demonstrate healthy levels of credit intermediation, with an intermediation ratio⁴ of 81.5 percent in March

2026 (2025:83.8 percent). The rate of intermediation has remained slightly above the 50 – 80 percent range since December 2024 and is supportive of economic growth.

Interbank Funding

Non-D-SIBs dominate the interbank market

- 7.5 Consistent with the increase in liquidity, the interbank market recorded a sustained decline in trading levels during the twelve months to March 2026. Daily averages mirrored this downward trend, decreasing from P555 million in the second quarter of 2025 to P353 million in the first quarter of 2026. Non-Domestic-Systematically Important Banks (Non-D-SIBs) continued to dominate the interbank market, accounting for 57.5 percent of total interbank borrowing and 84.0 percent of interbank lending. Interbank activity remained higher than historical levels as banks continued to navigate the prevailing liquidity conditions and utilise the Bank's interventions to stabilise short-term liquidity conditions.

Foreign Currency Funding

US dollar vulnerabilities remain limited

- 7.6 Domestic commercial banks' exposure to foreign exchange risk is limited and poses minimal threat to financial stability, as reflected in both the net foreign exchange position and the US dollar net open position. Despite an increment in the absolute overall net open position of banks from P299 million in December 2024 to P590 million in December 2025, the position represented just 3 percent of unimpaired capital and remained significantly below the prudential limit of 30 percent (Chart 7.1a). Conversely, the Pula equivalent absolute net exposure of the domestic banking system to the US dollar decreased to P161 million in December 2025 from P390 million in December 2024, translating to 1 percent of the industry's unimpaired capital, and therefore indicating limited risks from US dollar vulnerabilities.

3. Banks are statutorily required to report their 20 largest depositors as a monitoring tool to track vulnerabilities from wholesale funds.

4. Measured as a ratio of loans to deposits, the financial intermediation ratio measures the extent to which funds (excess) are made available to those who need them.

Exchange rate volatility is falling

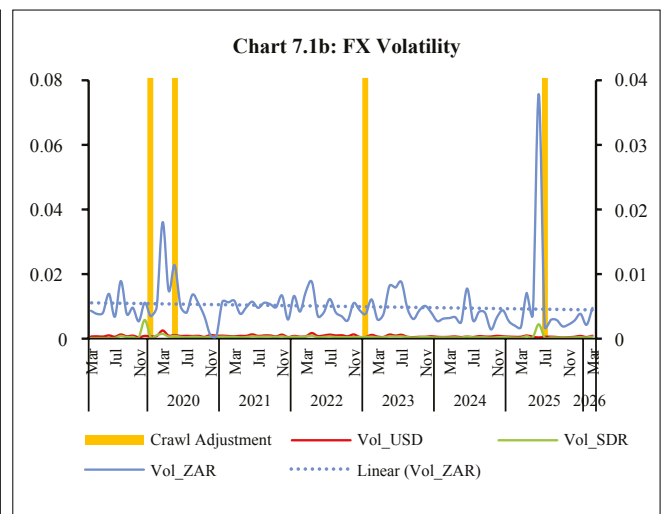
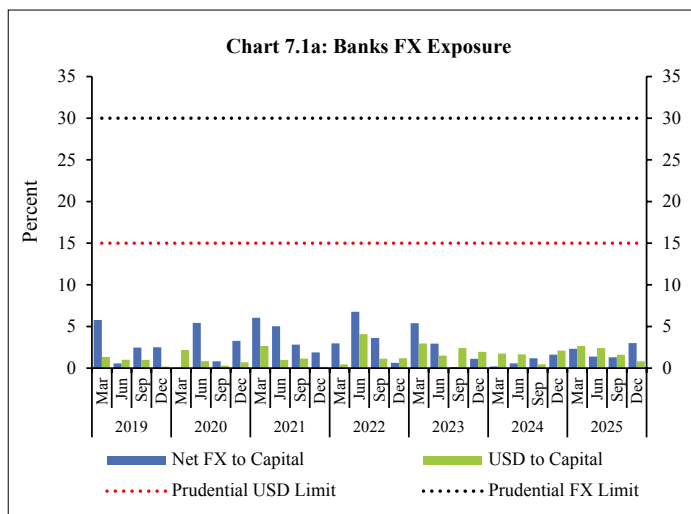
7.7 In the year to March 2026, the nominal Pula exchange rate depreciated by 0.1 percent against the Special Drawing Rights (SDR) and 4.7 percent against the South African rand. The marginal depreciation against the SDR was driven by the Pula’s depreciation against the Euro, the Chinese Renminbi and the British Pound by 3.8 percent, 3 percent and 0.1 percent, respectively, while it appreciated by 8.8 percent and

2.2 percent against the Japanese yen and the US dollar, respectively. Volatility of the Pula against the South African rand continued to subside (Figure 7.1b), indicating growing exchange rate stability and consequent stabilisation of import and export pricing expectations, thereby reinforcing domestic financial system resilience.

Foreign Currency Funding and Exposure

Banks FX exposure is well below the prudential limits

Exchange rate volatility is decreasing but remains elevated



Source: Bank of Botswana

Capital Markets – Equity Funding

Market capitalisation and liquidity improve

7.8 The total equity market capitalisation of domestic listed companies gained 9.7 percent, year on year, to P59.6 billion in February 2026 (2025: P54.3 billion) (Chart 7.2a). The gains largely reflect the increased participation of institutional investors as repatriated pension funds were deployed into domestic assets⁵. In that respect, and coupled with good company fundamentals, some share counters experienced significantly positive valuations, with the top five gainers as follows: Choppies (201.9 percent),

Botswana Telecommunications Corporation Limited (37.7 percent), BBS Bank (29.6 percent), Standard Chartered (24.1 percent), and Sechaba (18.7 percent).

7.9 Turnover in traded equities on the stock exchange increased significantly in the year ended February 2026 (Chart 7.2b), supported by net valuation gains, and this momentum is expected to be sustained in the medium term, thereby enhancing market liquidity (Chart 7.2c). Liquidity conditions were further boosted by the ongoing pension fund transition mandates, as repatriated funds continue to be allocated to long-term domestic assets in pursuit of an

5. Onshore allocations reached 45.3 percent, surpassing the 44 percent regulatory prescribed limit for December 2025.

even split between offshore and onshore investments by December 2027. Coupled with BSEL's market awareness campaigns, this contributed to a surge in the liquidity ratio from 3.0 in February 2025 to 9.8 in February 2026. Improved liquidity levels support efficient price discovery and facilitate easy entry and exit in the stock market without causing material price changes. This would anchor market sentiments and confidence, supporting price stability in the market.

The domestic stock market is profitable but volatile

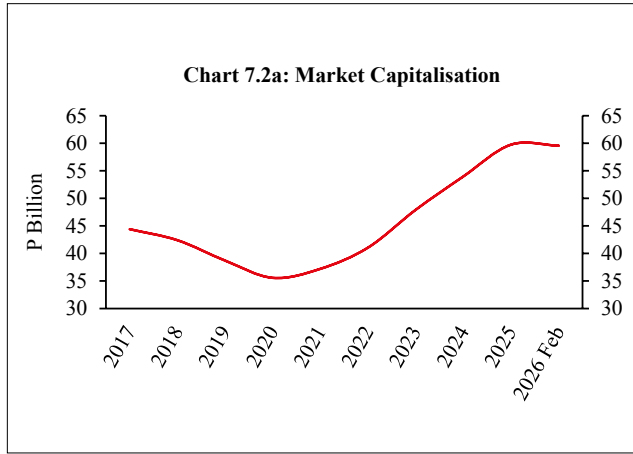
7.10 Profitability in the domestic stock market continues to maintain an upward trajectory as demonstrated by a sustained appreciation in the domestic company total return index (DCTRI) of 15.1 percent in the twelve months ended February 2026 relative to an appreciation of 12.2 percent in the corresponding period in 2025⁶. This was further supported by gains in market capitalisation, which translated into a stronger performance of the domestic company index (DCI) over the same period (Chart 7.2d). On the other hand, stock market volatility⁷ declined in the first three quarters of 2025 for both domestic and foreign listings. However, this moderation reversed in the fourth quarter, with secondary listings experiencing higher volatility relative to primary listings, owing to significant upward revaluations of Anglo-American PLC, CA Sales and Investec. As a result, the foreign company index (FCI) sustained its upward trajectory (Chart 7.2e). Notwithstanding these developments, stock market volatility remains elevated in comparison to historical averages, potentially reflecting the inherently risky nature of equity markets (Chart 7.2f).

6. The DCTRI shows gains (or losses) in equity positions due to market capitalisation appreciation (or depreciation) and dividend returns.

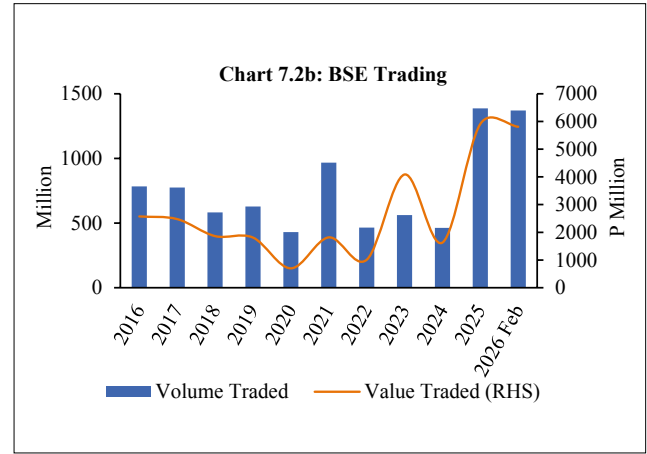
7. Measured as the 12-month standard deviation of the DCI.

Stock Market Developments

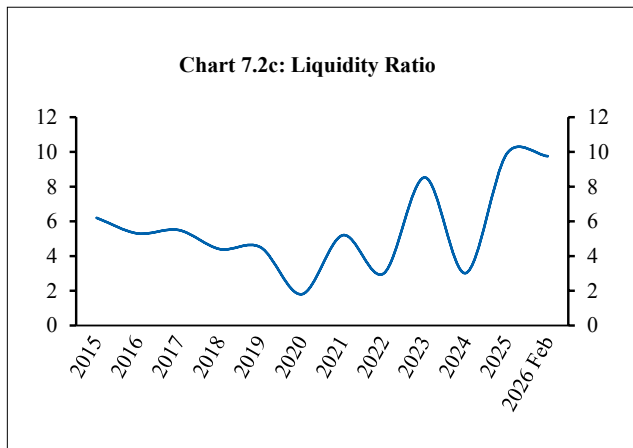
Stock market capitalisation is increasing



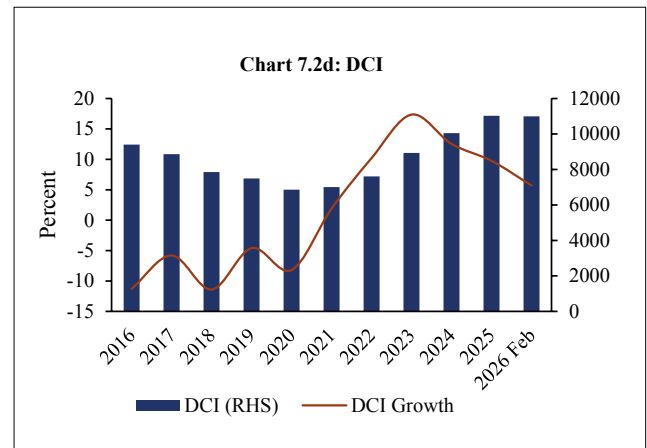
BSE trade by value and volume is increasing



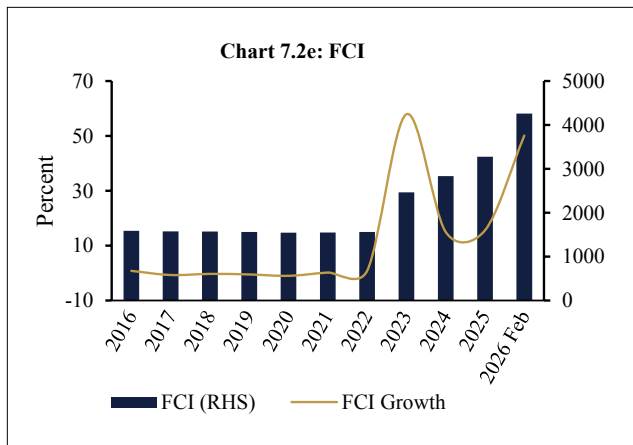
Liquidity in the BSE is increasing



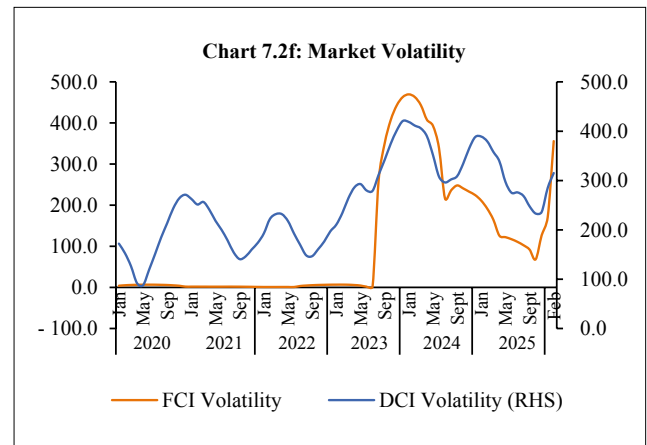
The DCI is improving



The Foreign Company Index is improving



Stock market volatility increasing



Source: Botswana Stock Exchange and Bank of Botswana Calculations

Government bonds drive market capitalisation

7.11 Bond market capitalisation grew by 2.0 percent to P40 billion in the twelve months to February 2026, from P38.3 billion in February 2025. This was driven by the issuance of a new government bond and additional tranches of existing ones amid growing public financing needs (Chart 7.3a). Investor demand reflected in bid-to-offer ratios generally remained robust, albeit with some variations across maturities consistent with evolving macro-financial conditions. The debut of the 25-year benchmark bond demonstrated strong appetite for duration, attracting solid oversubscription at its inaugural auction in October 2025, with subsequent auctions showing sustained demand. The nominal value of government bonds increased by 5.3 percent from P33.8 billion to P35.6 billion. While the local bond market recorded new corporate listings during the period, these were offset by maturing corporate bonds, resulting in an 18.7 percent decline in corporate bond valuations to P4.4 billion.

7.12 Government bonds accounted for 88.8 percent of the nominal value of the fixed income market in February 2026, from 86.0 percent in February 2025, indicative of increased government funding needs and a continued commitment to deepening the domestic capital market. Nevertheless, a sustained dominance of government securities has the potential to crowd out capital funding for the private sector. As domestic capital markets mature, a more balanced composition between government and corporate issuances will be important to support broader market development.

Bonds yield spread tightening

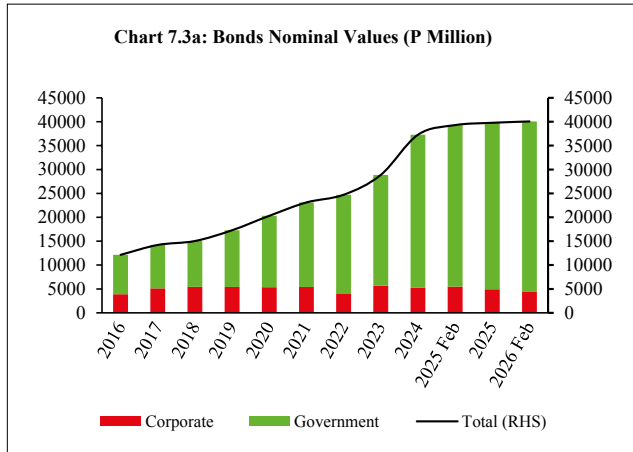
7.13 The spread between average yields on corporate and government bonds decreased from 0.05 percent in February 2025 to -1.22 percent in February 2026 (Chart 7.3e). This indicates a persistent rise in government bond yields relative to corporate yields, reflective of sovereign risk pricing by the market. Furthermore, yields on corporate bonds also increased during the twelve months, albeit at a slower pace, indicative of a growing risk premium required by fixed-income investors (Chart 7.3b).

Bond market volatility is high

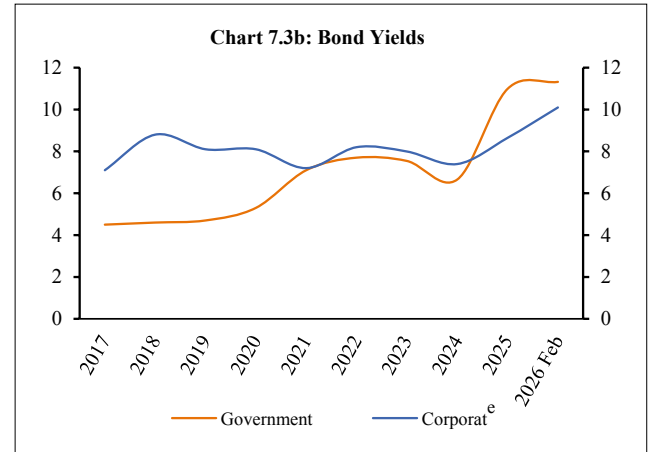
7.14 Although bond market volatility declined in the twelve months ended February 2026, bond risk remains elevated as reflected in the still relatively high volatility of bond indices compared to historical levels (Chart 7.3f). The potential for tightening of funding conditions in the bond market, therefore, remains, especially considering the uncertain macroeconomic environment and deteriorating fiscal position that ultimately translate into weaker corporate fundamentals. However, the generally accommodative domestic financial conditions, as indicated by the real monetary conditions index (RMCI) and the positive returns generated by the bond indices (Chart 7.3d), continue to support funding opportunities in money markets that could augment any shortfall in capital market funding.

Bond Market Developments

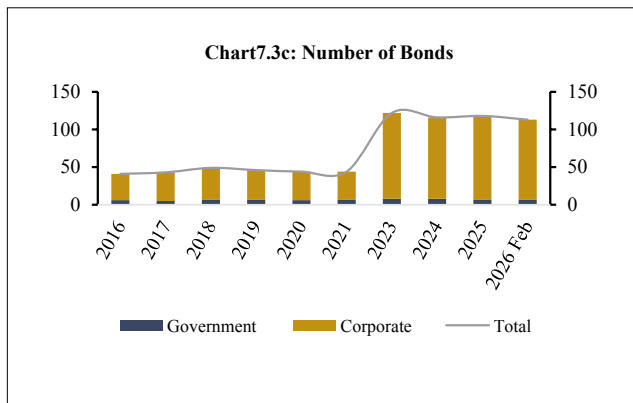
Government bonds dominate the bonds market



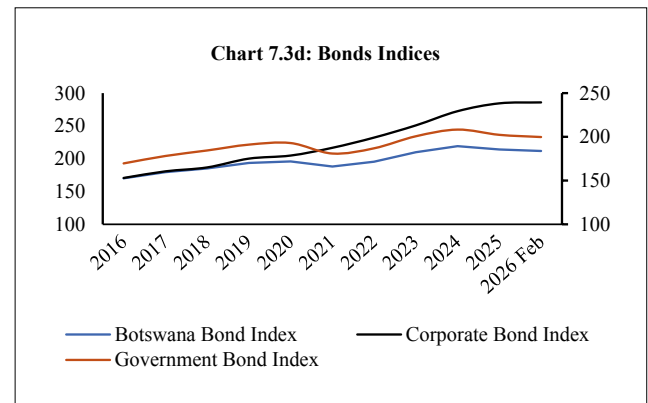
Bonds yields are above pre-COVID-19 levels, indicating higher uncertainty



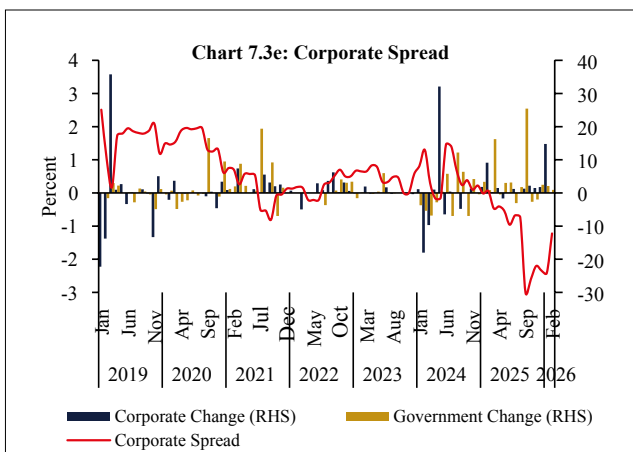
Corporates have many low-value bonds listed on the BSE



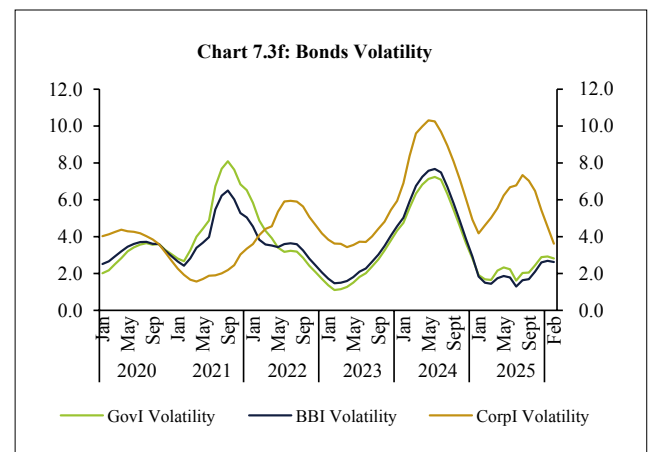
Bond indices are trending upwards



The corporate spread is narrowing



Bond market volatility is declining



Source: Botswana Stock Exchange and Bank of Botswana Calculations

8. CONTAGION RISK

Systemically important institutions are sound

8.1 The Bank has designated First National Bank Botswana and Absa Bank Botswana as the Domestic Systemically Important Banks (D-SIBs) for 2026. In the NBFIs space, NBFIRA has identified three Domestic Systematically Important Insurers (D-SIIs): Botswana Life Insurance Limited (life insurer), Hollard Insurance Company of Botswana (general insurer) and Continental Reinsurance Company (reinsurer). Regulatory authorities continue to intensify their oversight on these institutions with greater focus on their solvency, profitability and operational safety. Given their size and interconnectedness, these institutions have the potential to disrupt the entire financial system when faced with operational challenges or when facing insolvency. To mitigate these vulnerabilities, the Bank is developing regulatory requirements for D-SIBs, while NBFIRA has also strengthened its supervisory framework for D-SIIs. As of December 2025, D-SIBs and D-SIIs were adequately capitalised, liquid and solvent, hence posed limited threat to domestic financial stability.

Significant interlinkages pose a risk of contagion

8.2 Significant interlinkages persist in the financial system, with the banking sector at the centre of the system. The banking sector is highly exposed to households (Figure 8.1) and at the same time, households are highly exposed to NBFIs, with most of their assets (56.2 percent) held abroad. While offshore positions expose NBFIs to external financial and economic shocks, they also provide the needed portfolio diversification benefits. NBFIs are also interlinked with the rest of the financial system through multiple channels, such as deposits held with banks, funding avenues and capital market activities.

8.3 The net lending position of NBFIs to commercial banks (deposits held with banks less loans from banks) decreased by 17 percent to P23 billion, from P28 billion in December 2024. Pension funds and insurance through asset management companies also hold equity positions in other sectors of the economy in pursuit of their investment strategies. These interlinkages present an opportunity for risks that could easily spread across sectors and thus, elevate the risk of contagion in the domestic financial system. In view of the potential risks of cascading shocks due to

interconnectedness, the FSC continues to strengthen regulatory and legislative frameworks to mitigate the potential for propagation of idiosyncratic, sectoral, or institutional shocks to the whole of the financial system.

The insurance sector is concentrated and increasingly interconnected

8.4 The insurance sector remains an important stabilising component of the financial system but is highly concentrated and increasingly interconnected with banks and other financial institutions, particularly through investment and distribution channels. Life insurers dominate the sector, accounting for 81.9 percent of total assets (P21.5 billion), with the largest firms holding over 80 percent of assets. While this concentration supports stability through long-term, liability matched investments, it also raises systemic importance and potential spillover risks given growing interlinkages.

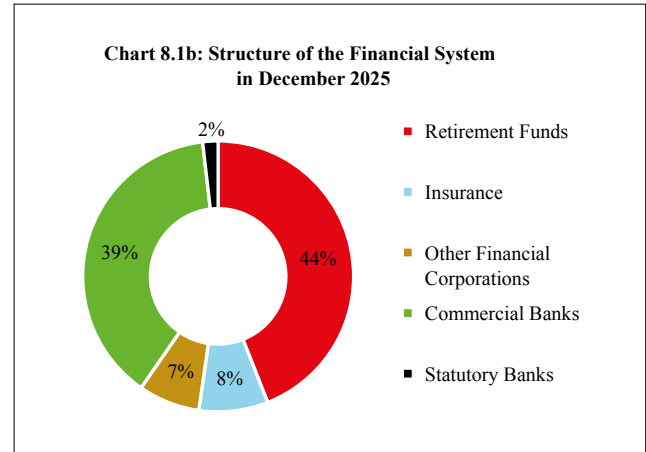
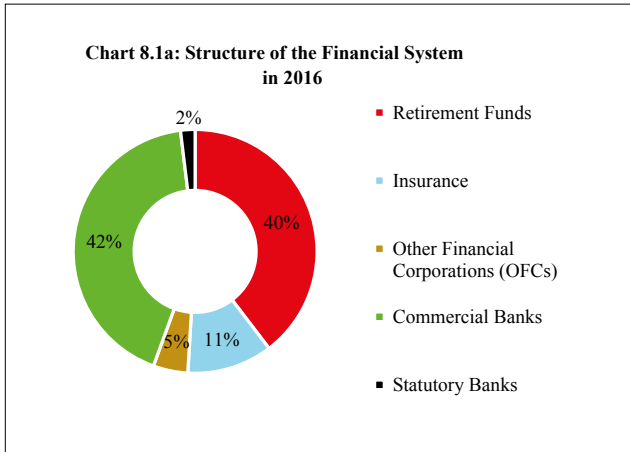
8.5 Across the broader non-bank sector, concentration risks are also evident. Micro-lending is dominated by a few players and heavily exposed to household credit, increasing vulnerability to household income shocks. At the same time, pension funds' significant offshore exposures heighten sensitivity to external market developments. Overall, while risks remain contained, high concentration and interconnectedness increase the potential for cross sector spillovers, underscoring the need for continued vigilant supervision.

Financial sector assets increase

8.6 The total assets of banks and NBFIs increased by 11 percent in 2025, reaching P383 billion from P345 billion in 2024. The surge in NBFIs financial assets, primarily pension funds, continues to be driven by improved global financial market performance and regulatory reforms boosting local investments in public and private equities. The size of the financial system represented approximately 143 percent of GDP in December 2025, compared with 131 percent in December 2024, demonstrating the significant contribution of the financial sector to the economy.

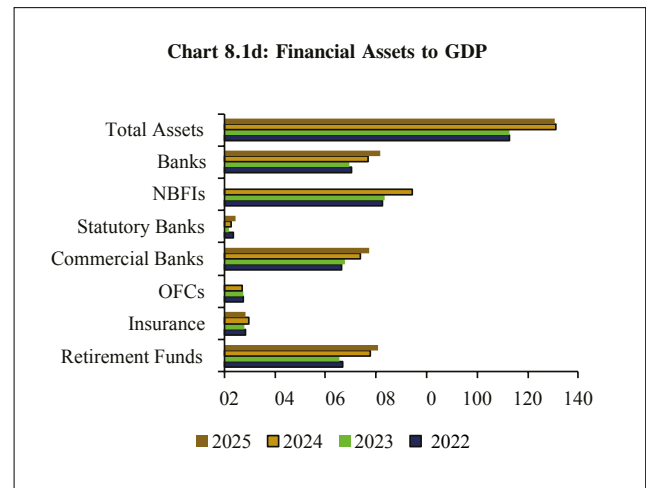
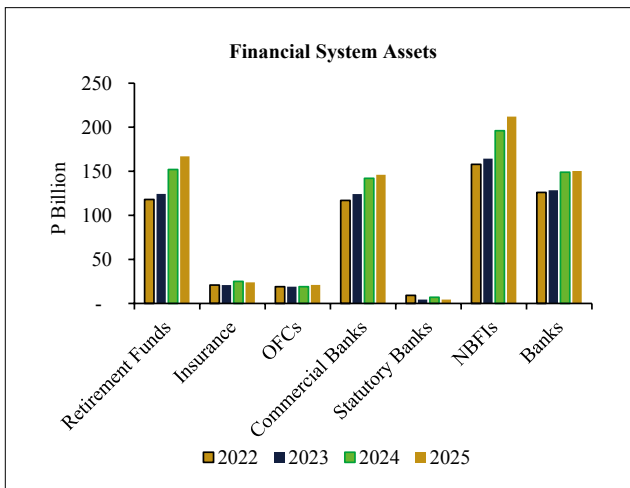
Bond Market Developments

The structure of the financial system has not changed significantly since 2016



Retirement funds and commercial bank assets are relatively high

NBFIs have the largest proportion to GDP owing to the relatively large retirement funds

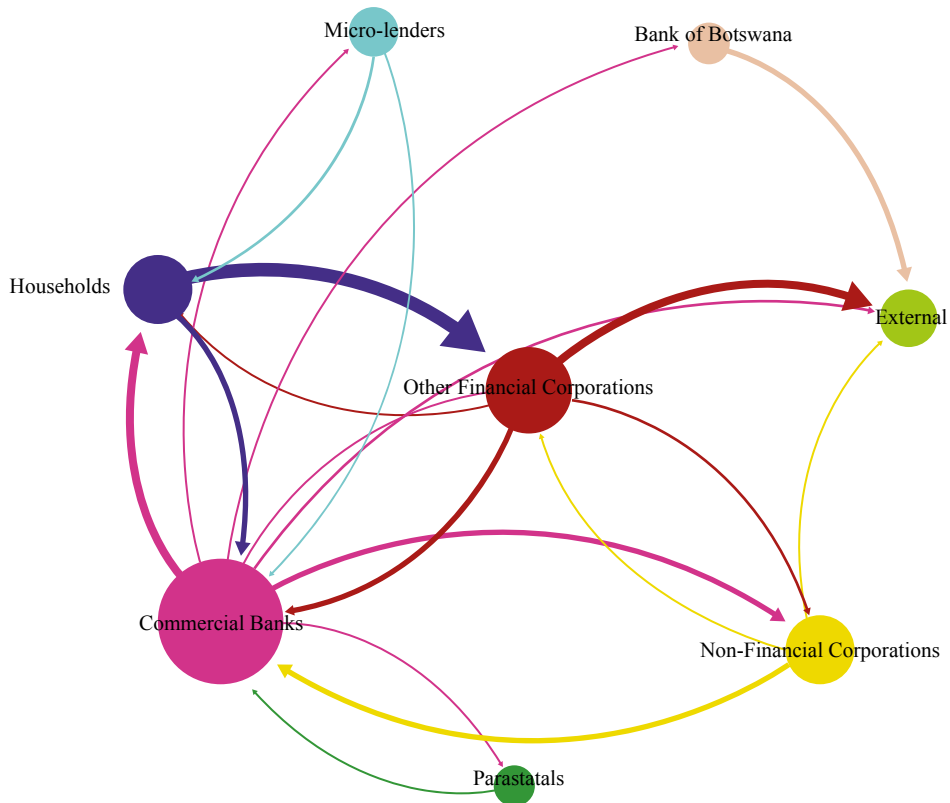


Source: BSEL, NBFIRA, BoB Calculations

Financial Sector Interlinkages

Banks are highly interconnected with the rest of the financial system

Figure 8.1: Macro-Financial Linkages (December 2025)



Notes:

1. A large node indicates a higher degree of interconnectedness across the financial system.
2. Thicker edges show a higher proportion of funds flowing out of the sector relative to the financial system.
3. Balances from the Bank to the external sector represent net foreign assets.
4. Balances from other financial corporations to the external sector are pension fund assets invested offshore.
5. Balances from commercial banks to the external sector are commercial banks' balances due from foreign banks.
6. For Other Financial Corporations, 85 percent are retirement funds assets.

Source: Bank of Botswana

9. BANKING SECTOR ANALYSIS

Asset Quality and Performance

9.1 The Botswana banking sector continues to demonstrate robust financial health and adaptation to the evolving financial and regulatory landscape. Capital adequacy ratios remain above the prescribed minimum threshold of 12.5 percent, indicating a healthy level of capitalisation and buffer to absorb potential losses (chart 9.1a).

Banks have sufficient capital buffers

9.2 Banks demonstrate consistent profitability, with several institutions reporting growth in profit after tax for December 2025. The strong financial performance is driven by a combination of factors, including effective asset and liability management, diversified income streams, and cost optimisation measures. The sector also boasts strong capitalisation levels, with capital adequacy ratios well above the regulatory requirements at 20.3 percent in December 2025 against the prudential limit. This robust capitalisation provides a significant buffer against potential losses and enhances the sector's resilience to economic shocks, contributing to financial stability.

Banking industry concentration remains a concern

9.3 Despite modest balance sheet growth, the banking sector continues to face liquidity and funding vulnerabilities linked to the sector's structural dependence on wholesale deposits from institutional investors, which heightens concentration and rollover risk in a constrained liquidity environment. Nonetheless, NPLs remain contained, although necessitating close monitoring under the uncertain business and economic conditions (Chart 9.1b). This is critical as government employees are the biggest borrowers from banks. In line with the Basel III Pillar 2 framework, the Bank is assessing targeted supervisory measures, including institution-specific capital add-ons for banks with elevated deposit concentration risk, alongside additional actions to strengthen liquidity risk management and reduce reliance on unstable wholesale funding.

Bank post impressive stock performance

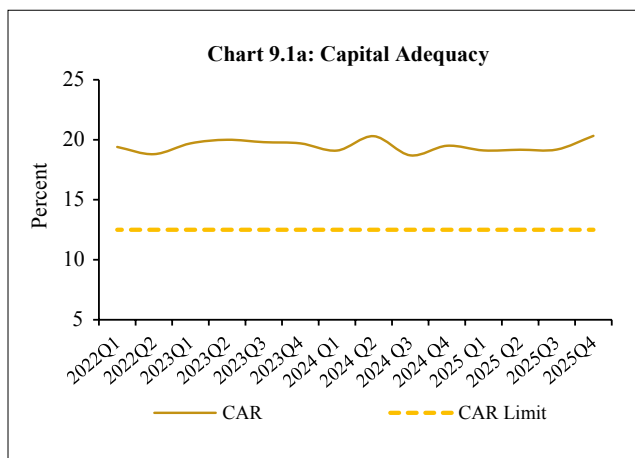
9.4 An analysis of banking sector performance on the stock market indicates strong investor sentiment, reflected by an average equity turnover of 24.1 percent for the period 1 January to 31 March 2026. The two top-performing listed banks recorded a total equity turnover of P23.5 million and P9.1 million while the rest of the listed banks recorded low levels. Overall, these results signal positive investor sentiments and suggest that the banking sector remains profitable (chart 9.1d).

The Deposit Insurance Fund increases

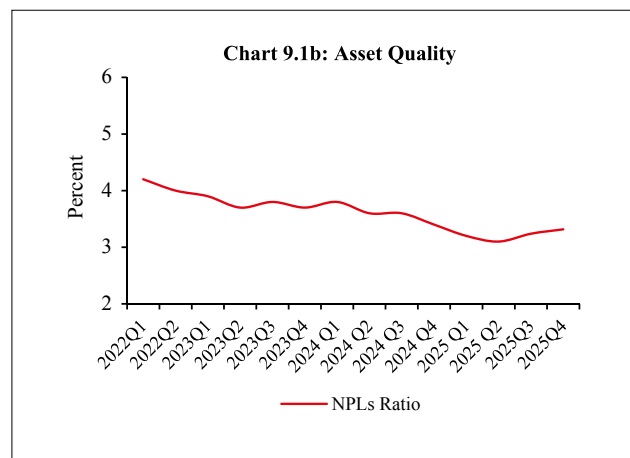
9.5 The Fund reported a balance sheet growth of 131.1 percent, with total assets of P130.1 million in 2025 from P56.3 million, primarily driven by higher premium contributions collected in 2025. However, the target fund ratio, which is a measure of fund balance as a percentage of estimated total insurable deposits, was still very low when compared to the recommended minimum 2 percent. Meanwhile, the average total insurable deposits were estimated at P73.3 billion (December 2024: P72.7 billion) as at December 2025, translating to 61.2 percent of total deposit liabilities of member institutions. In addition, for 2026, the Deposit Insurance Scheme of Botswana (DISB) expects to raise funding in premiums amounting to P73 million, a 0.7 percent increase from premiums collected in 2025.

Banking Sector Financial Soundness Indicators

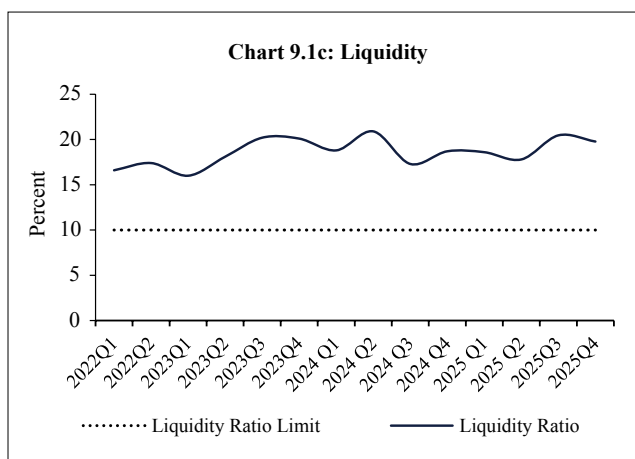
Banks are adequately capitalised



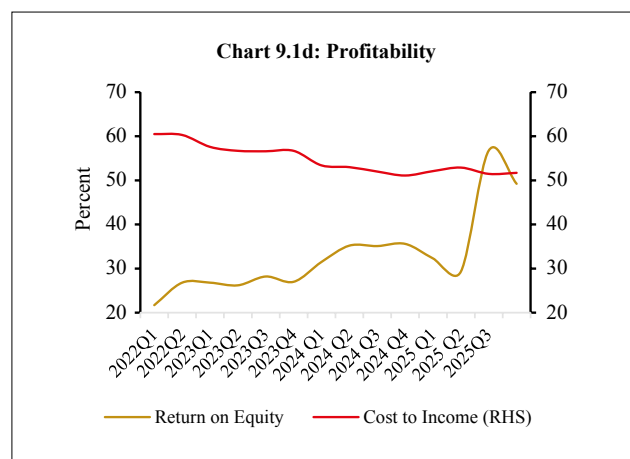
The NPLs ratio is stable



Banks are liquid



Banks are highly profitable, and costs are declining



Source: Bank of Botswana

Stress Test Scenarios

9.6 Stress test scenarios assess the resilience of Botswana's banking sector using December 2025 data, incorporating evolving global, regional and domestic macro-financial conditions. These include tightening global financial conditions, elevated geopolitical uncertainty, uneven recovery in key trading partners, and structural vulnerabilities in the domestic economy. The scenarios aim to identify key risks to banking sector stability, with particular focus on continued weakness in the diamond sector; elevated household indebtedness; intensifying climate-related shocks; and systemic and contagion risks arising from financial interconnectedness and concentration exposures.

Subdued diamond sector performance

- 9.7 Botswana's financial system remains highly exposed to developments in the diamond sector, which continues to underpin export earnings, fiscal revenues and economic activity. The stress test scenario simulates a sustained decline in global diamond demand, in part, due to global economic slowdown, weakened demand of luxury goods in key markets and increased competition from fake diamonds.
- 9.8 Persistence of these circumstances could entail diamond mines scaling down operations, potential job losses in mining and related sectors as well as lower foreign exchange inflows. In turn, household incomes could decline, impacting consumer spending and putting pressure on businesses, particularly those

reliant on domestic demand. This scenario translates into higher NPLs for banks, eroding their profitability and capital buffers. The stress test reveals that while banks can withstand a moderate decline in diamond revenues, a severe and prolonged downturn could push some institutions below regulatory capital requirements.

Impact of potential employment losses

9.9 Current weak domestic economic conditions indicate a heightened risk that employment losses could materialise or intensify in the near term. The stress test therefore incorporates a severe but plausible scenario in which rising unemployment and stagnating real household incomes arise from existing economic pressures. The scenario reflects structural vulnerabilities in the household sector, particularly the high concentration of unsecured borrowing, which increases households' exposure to labour-market shocks and income declines.

9.10 Under this scenario, widespread job losses lead to sharp reductions in household income and a deterioration in debt-servicing capacity. This would lead to higher default rates, resulting in a significant increase in non-performing loans. The resulting deterioration in asset quality erodes bank profitability and adds pressure to funding and liquidity conditions in an already constrained financial system. These dynamics amplify credit risk and weaken overall financial resilience, highlighting the employment channel as an important source of systemic stress under adverse conditions.

Intensifying climate risks could destabilise the financial system

9.11 The climate-related stress scenario assumes the occurrence of severe but plausible climate-related shocks, reflecting Botswana's high exposure to physical climate risks. The scenario captures impact of widespread floods, together with outbreaks of Foot and Mouth Disease. These shocks are assumed to disrupt agricultural production through crop failures, livestock losses, and damage to transport and logistics infrastructure, resulting in lower rural incomes and weaker economic activity.

9.12 The assumed shocks affect the banking sector primarily through higher credit risk. Declines in

agricultural output and income reduce borrowers' repayment capacity, leading to increased loan defaults and deterioration in asset quality, particularly for exposures linked to agriculture and related sectors. Collateral values are assumed to weaken, while limited fiscal space constrains the government's ability to provide economic support or liquidity backstops.

Contagion risk could have negative outcomes for the financial system

9.13 The stress test incorporates contagion risk to reflect the high degree of interconnectedness within the domestic financial system and the potential for shocks to propagate beyond individual institutions. Financial linkages between banks, non-bank financial institutions, and other sectors can transmit stress through multiple channels, including balance-sheet exposures, funding relationships, and confidence effects. Given the concentration of financial activities and common exposures across institutions, the assumption that shocks may spread through the system is considered both relevant and plausible.

9.14 The assessment of contagion is motivated by the presence of domestically systemic banks whose size, interconnectedness, and market significance could amplify stress if they were to experience financial distress. The stress test framework therefore assumes that disruption at a systemically important institution could have broader implications for financial stability, even in the absence of direct exposures.

Stress Test Results

Banks are susceptible to severe credit shocks

9.15 The results of credit shocks indicate that commercial banks are generally resilient to stress, save for severe credit shocks that could result in significant prudential capital breaches. Under the system-wide moderate scenario, where an additional 10 percent of performing loans are assumed to become NPLs, bank capital adequacy levels decline to 10.8 percent, breaching the prudential capital adequacy requirement of 12.5 percent. The industry capital position, however, worsens to 2.0 percent in the severe scenario, where 20 percent of performing loans are assumed to become NPLs. As a result, the asset quality declines, with the ratio of NPLs to total

loans rising from a baseline of 4.1 percent to 12.8 percent and 22.5 percent under moderate and severe scenarios, respectively (Chart 9.2d).

9.16 Regarding sectoral shocks, under the moderate scenario, banks' capital adequacy ratio drops to 8.8 percent, while the NPL ratio rises to 15.2 percent. In the severe scenario, the capital adequacy ratio decreases further to 4.4 percent, and credit quality worsens significantly with an NPL ratio of 20 percent. Concerning credit concentration shocks, banks breach the minimum capital adequacy ratio, with the ratio falling to 10.5 percent under the moderate scenario which assumes the default of each bank's largest single borrower. The ratio declines further to 5.8 percent under the severe scenario, which assumes defaults by the two largest counterparties.

9.17 Under the moderate concentration shock, D-SIBs remain resilient, with a capital adequacy ratio above the prudential limit at 13.8 percent and 11.3 percent for the NPL shock. For the severe concentration and NPL shocks, the capital adequacy ratio falls to 9.3 percent while NPLs worsen to 18.7 percent (Chart 9.2a). In general, credit risk tests show that the NPLs shock has more prominence in the capital and asset quality position of banks than other shocks. Nevertheless, credit stress tests do not consider credit mitigation measures, such as underlying collateral.

Banks are resilient to liquidity shocks

9.18 In the liquidity risk test, banks show resilience to a liability run in the moderate stress scenario, and all banks can withstand liability drawdowns for 14 days. Under severe stress conditions, all banks would be able to withstand drawdowns for 3 days. The results show that dependence on wholesale deposits is prevalent in both bank categories, with a range of 25 to 62 percent of total customer deposits. Therefore, there is a need for banks to diversify their portfolios to mitigate liquidity risks.

9.19 However, the scenarios do not consider the availability of liquidity support provided by the Bank through the Credit Facility, nor liquidity support available from related companies or holding banks. Accordingly, stress test results should not be interpreted to mean that banks would default under these conditions.

Bank profitability to decrease as market rates increase

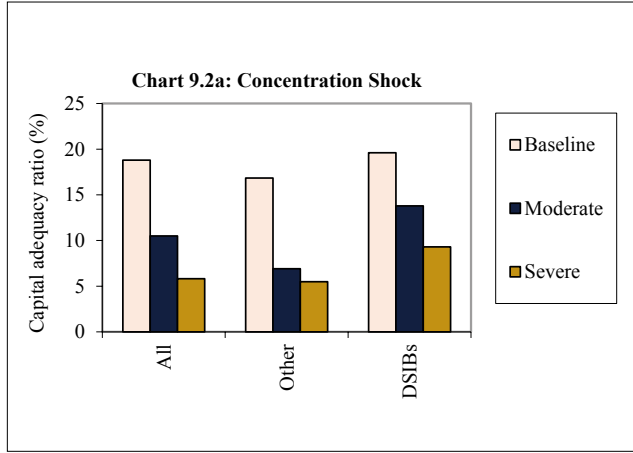
9.20 Results of the moderate interest rate shock indicate that an increase in market rates by 300 basis points would lead to a decrease in interest income by P270 million, with an accompanying potential decrease of P174 million from the repricing of government bonds. Bank's capital adequacy ratio would decrease by 0.2 percentage points. For the severe scenario (500 basis points increase), banks would lose P450 million in interest earnings and P291 million from repricing of bonds leading to a further decline in CAR by 0.3 percentage points. (Chart 9.2f).

9.21 The fall in profit reflects the banking industry's negative cumulative repricing gap over the next 12 months, where interest earning liabilities exceed interest earning assets in the stress horizon. Meanwhile, D-SIBs record a gain in profit as they have a positive cumulative repricing gap where interest earning assets exceed interest earning liabilities, thus sustaining profitability. Therefore, banks incur losses from an increase in funding costs. Overall, while domestic banks are resilient, there is risk stemming from the potential repricing of government bonds.

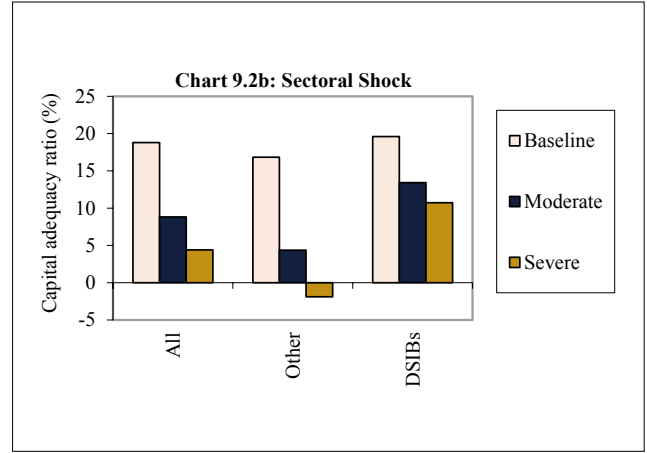
December 2025 Test Results

Credit Shocks

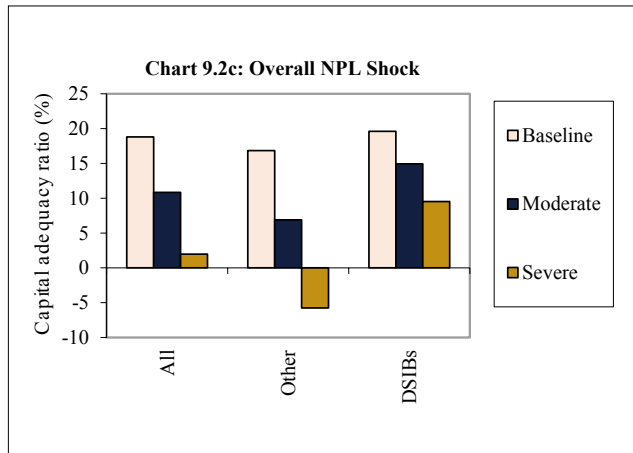
Banks are generally resilient to credit concentration shocks



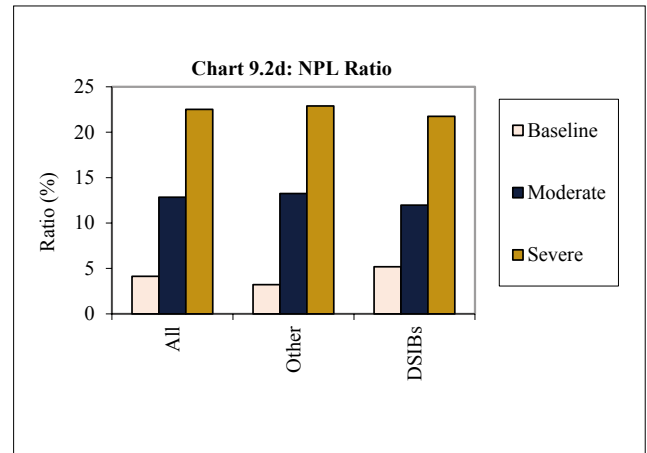
Severe sectoral shocks would lead to a significant breach in CAR



A severe aggregate credit shock would deplete banks' capital

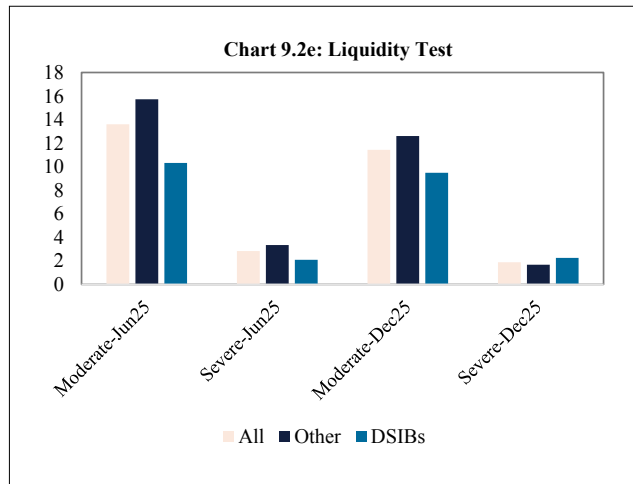


The NPL ratio for the aggregate credit shock increases significantly in the severe scenario

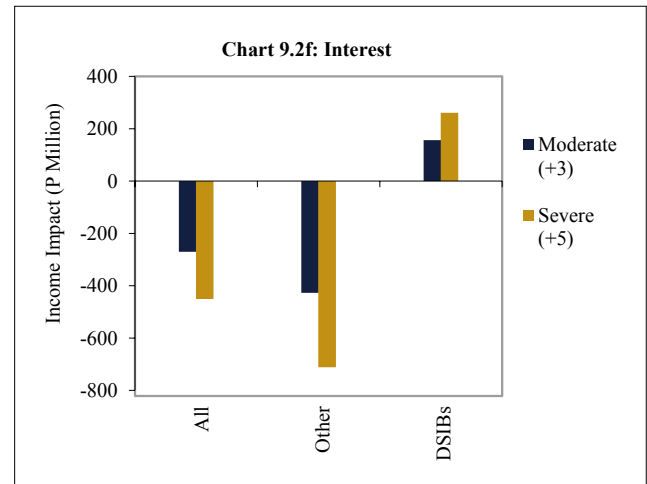


Liquidity and Interest Rate Shocks

Banks have low survival horizon under a severe liquidity shock



Bank profitability to decrease with an increase in market rates



Source: Bank of Botswana

Banks breach prudential limits due to a combination of shocks

9.22 Considering a combination of shocks for scenario analysis, D-SIBs breach the prudential limit with a capital adequacy ratio of 7.8 percent in the moderate scenario, and they are also insolvent in the severe scenario with a capital adequacy ratio of 5.2 percent (Chart 9.3a).

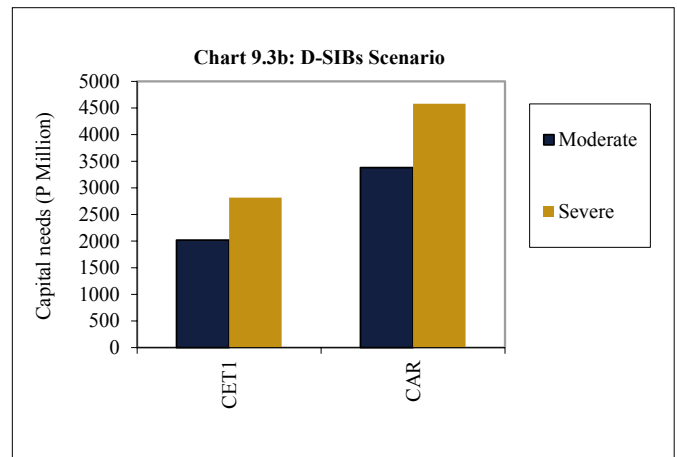
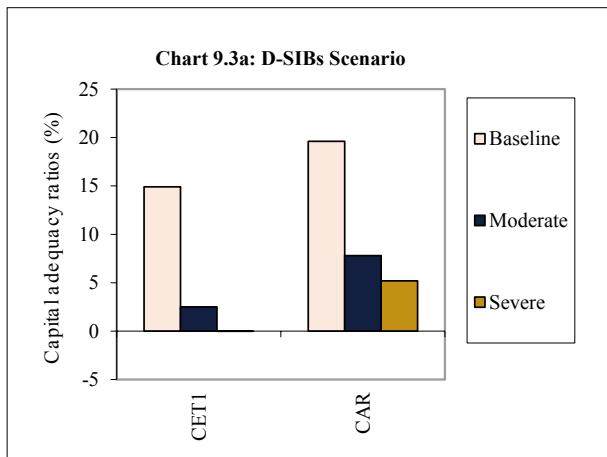
9.23 To capitalise D-SIBs, shareholders would have to inject capital amounting to P3.4 billion in the moderate scenario and P4.6 billion in the severe scenario. Given that credit mitigants are excluded from the stress test scenario, and the loss given default is assumed to be 100 percent, D-SIBs are judged to

be resilient to a combination of shocks, although susceptible to extreme shocks. To link liquidity risk and solvency of the D-SIBs, it is assumed that D-SIBs are closed out of funding markets if the capital adequacy ratio under stress scenario falls below set hurdle rates. Hurdle rates are set at 8 percent for customer deposits, 10 percent for short-term funding, and 4 percent for long-term funding. Under these assumptions, D-SIBs are closed out of short-term funding markets and customer deposits in the moderate scenario and severe scenario, and there is loss of funding amounting to P68 billion and P71 billion, respectively. Consequently, banks would experience severe liquidity shortfall in both the moderate and severe scenarios.

D-SIBs Scenario Analysis

Severe stress scenario completely erodes D-SIBs' capital base

D-SIBs need a significant capital injection to recapitalise under severe stress conditions



Source: Bank of Botswana

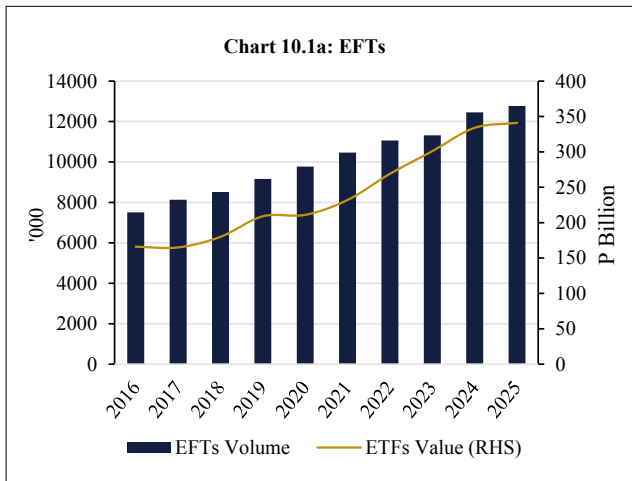
10. PAYMENTS AND SETTLEMENT RISKS

Interconnected digital platforms heighten the risk of contagion

- 10.1 Botswana's digital payments landscape continues to expand, with 23 electronic payment service (EPS) providers and over 1,500 agents as at December 2024. This growth, alongside rising volumes and values of electronic funds transfer (EFT) transactions, reflects increasing public confidence in digital financial services and supports financial inclusion.
- 10.2 Payment and settlement infrastructures are critical to financial stability, given their role in liquidity distribution, contagion transmission, and monetary policy implementation. Real-time gross settlement (RTGS) systems, in particular, ensure immediate and final settlement in central bank money while providing real-time visibility of liquidity conditions.
- 10.3 In line with the Bank's pursuit of its broader macroprudential objective of promoting financial stability, it has developed the Domestic Systemically Important Payment Systems (D-SIP) framework. The D-SIP framework provides a structured approach for identifying and designating payment systems whose disruption could pose significant risks to the stability, efficiency and confidence in the national payment system. Under this framework, the Bank assesses payment systems based on several criteria, including the value and volume of transactions processed, the nature of payments, the size and concentration of financial risks, system interoperability, interdependencies with other financial market infrastructures, the markets in which the systems operate, and the potential for significant credit and liquidity disruptions in the event of system failure. Based on this assessment, the Bank has identified the Domestic Systemically Important Payment Systems (D-SIPs) for 2026 as the Botswana Interbank Settlement System (BISS), the Botswana Automated Clearing House (BACH), and the Central Securities Depository Company of Botswana (CSDB).
- 10.4 While D-SIPs remain stable, divergence in transaction trends, with EFT volumes increasing and BISS activity broadly stable, indicates a shift toward retail and mobile payment platforms, which may reduce oversight over high-frequency, low-value transactions. The concentration of activity among a few EPS providers introduces single-point-of-failure risks, underscoring the importance of robust redundancy arrangements and operational resilience frameworks.
- 10.5 The increasing digitalisation of financial services introduces new systemic vulnerabilities, including cyber threats, operational disruptions, and third-party dependencies. These risks require enhanced cybersecurity frameworks, real-time system monitoring, and coordinated incident response mechanisms. A cyber breach or system failure at a major EPS provider could disrupt payment flows, create liquidity bottlenecks, erode public confidence, and amplify systemic stress. Repeated outages may also reverse gains in financial inclusion. In response, the Bank has enhanced the clearing and settlement framework. Effective 1 February 2026, a revised BISS settlement window was introduced, featuring four daily clearing and settlement cycles, with mandatory crediting after each cycle.
- 10.6 To safeguard financial stability amid rising digitalisation and cyber risks, Botswana should strengthen digital risk governance across the financial sector. This includes establishing a comprehensive National Cyber Resilience Framework for financial institutions, enhancing real-time transaction monitoring and anomaly detection, and promoting interoperability and redundancy across payment platforms to minimise single-point-of-failure risks. Regular sector-wide cyber drills involving financial market infrastructures, payment service providers and regulators are also necessary to test crisis response readiness. In addition, strengthening consumer protection through robust data privacy measures and efficient dispute resolution mechanisms will be critical to maintaining public trust in digital financial services. Collectively, these measures will help limit operational disruptions, contain contagion risks and reinforce systemic resilience as the financial ecosystem becomes increasingly digitised.

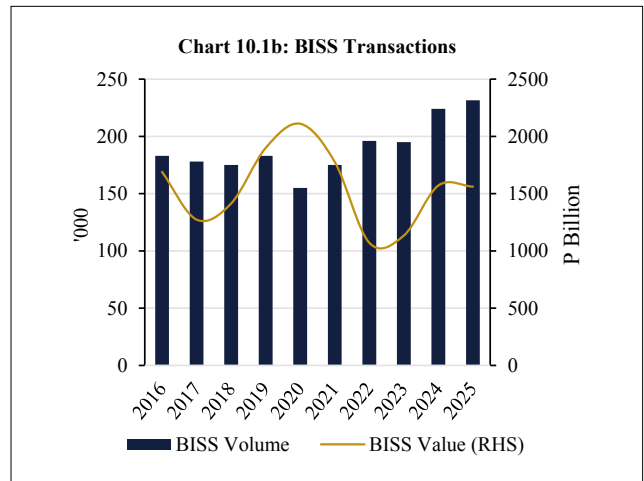
Payments and Settlement Systems Indicators

EFTs volume and value are trending upwards



Source: Bank of Botswana

BISS transactions volume and value are largely stable



Box 10.1: Beyond Payments – The Stability Function of Real-Time Gross Settlement Systems

The resilience of the financial system is anchored not only in sound institutions and prudent policies, but also in the robustness of its core infrastructures. Among these, Real-Time Gross Settlement (RTGS) systems play a pivotal role. By enabling final settlement in central bank money, RTGS systems eliminate settlement risk, support efficient liquidity distribution and intraday liquidity management, facilitate the effective transmission of monetary policy, and provide real-time monitoring of systemic liquidity conditions. Their stabilising function, while often operating in the background, is essential for maintaining confidence and limiting the propagation of financial shocks.

1. Overview

RTGS system is an interbank funds transfer mechanism in which transactions are processed on a gross basis and settled in real time, with finality in central bank money. As the safest settlement asset, central bank money eliminates credit risk in the settlement process. RTGS systems therefore constitute a core component of financial market infrastructures (FMIs), supporting the execution of time-critical, high-value payments.

While RTGS systems are often perceived primarily as payment conduits, their role extends well beyond transaction processing. They underpin the smooth functioning of financial markets, mitigate systemic vulnerabilities associated with deferred net settlement (DNS) arrangements, and serve as a critical platform for the implementation of monetary policy. In this regard, the RTGS system remains a cornerstone of the financial stability architecture.

2. How RTGS Systems Promote Financial Stability

The contribution of RTGS systems to financial stability arises through a set of interrelated mechanisms, each addressing specific vulnerabilities inherent in alternative settlement arrangements. In most jurisdictions, RTGS systems are owned and operated by central banks, placing them at the centre of liquidity management, systemic oversight, and policy implementation.

(a) Risk Mitigation: Eliminating Settlement and Systemic Risks

A primary contribution of RTGS systems is the elimination of settlement risk⁸, which represents a key vulnerability in DNS systems. Under deferred settlement arrangements, payment obligations accumulate over time, creating credit and liquidity exposures among participants. The failure of a single participant to meet its obligations may therefore trigger a cascade of disruptions across the financial system. RTGS systems fundamentally alter this risk profile by settling transactions individually and with immediate finality. Consequently, exposures do not accumulate, and the risk of contagion through settlement failure is significantly reduced.

(b) Intraday Liquidity Management: The Central Bank as System Stabiliser

Although RTGS systems mitigate settlement risk, they increase the demand for intraday liquidity, as each transaction must be funded at the time of processing. This elevates the importance of active liquidity management by both participants and the central bank. In Botswana, the Bank performs a key stabilising function through the Botswana Interbank Settlement System (BISS), supported by a standing facilities framework that provides collateralised intraday credit to address temporary liquidity shortfalls. More broadly, real-time visibility over settlement positions enables the Bank to inject or absorb liquidity as needed, thereby ensuring the orderly flow of payments and limiting the risk of settlement disruptions.

(c) Monetary Policy Transmission: RTGS as a Policy Implementation Platform

RTGS systems serve as the operational platform through which monetary policy decisions are implemented. Settlement accounts held at the central bank are the instruments through which system-wide liquidity is managed, short-term interest rates are influenced, and open market operations are conducted. Adjustments in the policy rate are transmitted through interbank markets via changes in the supply of, and demand for, central bank reserves, as reflected in RTGS settlement flows. Efficient and timely settlement enhances the precision and effectiveness of monetary policy transmission, while delays or frictions in payment systems may weaken policy signals.

8. The risk that one party in a transaction will fail to settle its obligations at the agreed time.

(d) RTGS as Financial Firewall and Early Warning Tool

RTGS systems perform a critical stabilising function during periods of financial stress. By ensuring that payments are settled individually and irrevocably, they prevent the emergence of liquidity gridlock and limit the propagation of contagion arising from counterparty concerns. At the same time, RTGS systems provide real time information on payment flows and liquidity positions, enabling the early identification of emerging stress, including unusual payment patterns or the depletion of settlement balances. This supports timely and targeted policy responses, including the provision of emergency liquidity assistance where necessary.

(e) Operational Resilience and Regional Contingency

RTGS systems contribute to financial stability through strong operational resilience. These systems are designed with robust contingency arrangements, including backup infrastructure, disaster recovery capabilities, and cyber resilience controls, to ensure continuity of operations during disruptions. In the regional context, the SADC RTGS system provides an additional layer of resilience, with the capacity to serve as a contingency mechanism in the event of domestic system disruptions. This underscores the importance of regional cooperation in strengthening the overall resilience of payment systems.

3. Interconnectedness and Contagion Risks

The growing interconnectedness of financial market infrastructures increases the potential for contagion. However, RTGS systems help contain such risks by ensuring settlement finality, enhancing liquidity visibility, and supporting macroprudential surveillance.

4. Conclusion

RTGS systems are a critical pillar of the financial stability framework. By enabling real-time, final settlement in central bank money, they reduce settlement and systemic risks, support effective liquidity distribution, and strengthen monetary policy transmission. Their importance is most evident during periods of financial stress, when uninterrupted settlement, real-time monitoring of payment flows, and access to central bank liquidity facilities are essential to maintaining confidence in the financial system. In this regard, continued strengthening of the domestic RTGS framework, alongside deeper integration with the SADC-RTGS system, will further enhance the resilience and efficiency of Botswana's financial system.

11. REGULATORY AND OTHER DEVELOPMENTS

Deepening the legal foundations of the financial system

- 11.1 Botswana continues to modernise its financial sector regulatory framework to support stability, innovation and market integrity. Progress on the National Payment Services Bill, 2026 advanced in February 2026 with submission of the layperson's draft to the Attorney General's Chambers (AGC), where formal drafting is underway. The Bill will consolidate the legal underpinnings of the payment ecosystem and strengthen the Bank's supervisory reach across clearing, settlement and digital payment platforms.
- 11.2 Work also progressed on the Non-Bank Lenders Bill, 2026, which aims to bring micro-lenders, digital credit platforms and other non-bank lenders under a consistent licensing and oversight regime. Following review by the Cabinet Business Committee in January 2026, the Bill was returned to the AGC on 9 February 2026 for refinement. Once enacted, the Bill will reduce regulatory blind spots, strengthen consumer protection safeguards and enhance the integrity of the broader credit market. Other regulatory reforms implemented, include revisions to the Pension Fund Investment Rule (PFR2), enhancements to the Policyholders Protection Fund framework, and updates to AML/CFT&P supervisory tools. In addition, ongoing legal reforms, such as the Medical Aid Funds Bill, the Health Insurance Bill, the review of the Insurance Industry Act, are expected to modernise NBFI sector oversight and reduce emerging vulnerabilities.

Government advances comprehensive fiscal and revenue reform agenda

- 11.3 In addition, during the 2026 Budget sitting, Government brought a broad reform agenda spanning fiscal governance, revenue administration, customs modernisation, and public sector financing. The Stock, Bonds and Treasury Bills (Amendment) Bill, 2026 introduces a major shift in the sovereign debt framework by raising the statutory ceiling for total public debt and government guaranteed debt to 60 percent of GDP, a structural change designed to expand fiscal headroom and align debt management with evolving financing needs. Complementing this macro fiscal recalibration, both the Customs (Amendment) Bill, 2025 and the Tax Administration Bill, 2025 modernise core elements of the revenue

collection system. The Customs Bill undertakes wide ranging amendments, tightening compliance rules, expanding penalties, addressing valuation gaps, improving the treatment of transit, Special Economic Zone operations, and tariff classification procedures, thereby strengthening trade related revenue governance and closing loopholes that previously hampered enforcement. The Tax Administration Bill consolidates and harmonises all tax administration procedures, introducing uniform rules on taxpayer registration, record keeping, assessments, appeals, enforcement, the establishment of a modern Tax Tribunal, and updated penalties, representing a significant institutional leap forward in Botswana's tax administration architecture.

- 11.4 Alongside these structural reforms, four Bills directly support the Government's funding strategy for the national budget. The Syndication Loan Authorisation Bill, 2026 proposed borrowing of USD 216.67 million from a consortium of three domestic banks. Absa Bank Botswana, First National Bank Botswana, and Stanbic Bank Botswana, embedding a coordinated domestic market financing mechanism into the fiscal toolkit. The Standard Chartered Bank Loan Authorisation Bills (No. 1 and No. 2) complement this strategy by enabling Government to raise P750 million and EUR 400 million, respectively, for budget support.
- 11.5 These combined regulatory developments carry important financial stability considerations. The expanded debt ceiling and the bank financed borrowing strengthen fiscal capacity in the short term. At the same time, the Customs and Tax Administration reforms help mitigate long term vulnerabilities by strengthening compliance, tightening enforcement, improving revenue mobilisation, and reducing leakages, thereby supporting fiscal sustainability and the resilience of public finances. The seven Bills reflect a dual track regulatory agenda: one that expands financing capacity to meet immediate budgetary needs while simultaneously reinforcing the institutional frameworks underpinning revenue administration, customs governance, and fiscal accountability.

Regulation strengthened through improved compliance and supervision

11.6 Apart from legislative development, the regulatory developments during the review period were marked by continued strengthening of Botswana's AML/CFT/CPF framework and enhancements in market conduct oversight. The Bank conducted on-site examinations of banks to assess compliance with AML/CFT/CPF obligations under the Financial Intelligence Act, 2022 (as amended in 2025), identifying deficiencies in customer due diligence, transaction monitoring, and internal escalation processes; however, these gaps did not pose systemic risks and were mitigated through strengthened governance and ongoing supervisory engagement. Botswana's successful re-rating by the Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG), which upgraded six of seven outstanding FATF Recommendations to compliant or largely compliant, further reinforced confidence in the country's regulatory environment and supported the integrity of the financial system. Additional progress was achieved through the completion of the updated 2025 National Risk Assessment (NRA), which clarified major ML/TF threats and informed targeted risk-based supervision. Market-conduct oversight also remained robust, with banks adhering to Monetary Policy Committee guidance on prime lending rates, adjusting deposit pricing transparently, and expanding financial-inclusion products.

11.7 Meanwhile, regulatory action regarding Credit Reference Bureau Africa's exit ensured the protection of credit information integrity and continuity, mitigating the risk of disruptions that could impair lenders' credit-risk assessments and weaken financial stability. At the same time NBFIRA advanced its risk-based supervision agenda through the completion of ML/TF risk-profiling tools for micro-lenders, life insurers and asset managers, and initiated a comprehensive sector-wide ML/TF risk assessment in partnership with international experts.

Catalysing Fintech Innovation: The Launch of Botswana's Regulatory Sandbox

11.8 The Bank established a Regulatory Sandbox in 2025 to provide a controlled and supervised environment in which fintech innovators can test innovative financial products, services, and business models prior to full market entry or licensing. The Regulatory Sandbox

became operational in March 2026, following the publication of the Regulatory Sandbox Guidelines in November 2025. Implemented under the Financial Services and Digitalisation pillar of the BETP, the initiative addresses ongoing regulatory rigidities that had delayed innovation, raised barriers to entry for startups, and constrained fintech development. At the same time, it seeks to foster innovation, support an inclusive digital economy, and safeguard financial stability, market integrity, and consumer protection. The Bank issued its first targeted call for applications on 4 March 2026 under the theme "Unlocking an Inclusive Digital Economy through Digital Banks, Inclusive Payments, and Interoperability Solutions," and the application window closed on 31 March 2026. Applications submitted by innovators are currently under assessment in accordance with the Regulatory Sandbox Framework and Guidelines.

Capital-market reforms reinforce systemic settlement security

11.9 The Botswana Stock Exchange Limited (BSEL) continues to modernise capital-market infrastructure and implement reforms that strengthen market integrity and resilience. The Exchange achieved major technological upgrades, including the rollout of a new Central Securities Depository (CSD) System, a new Automated Trading System (ATS), and integration with the SWIFT network, which enhanced settlement security, operational reliability, and alignment with global best practice. A milestone regulatory development was the commissioning of central-bank settlement of BSE transactions through the Botswana Interbank Settlement System (BISS), significantly reducing settlement risk and reinforcing systemic safeguards. In addition, the domestic investment requirement for NBFIRA-regulated pension funds continued to reshape investor participation, increasing the structural role of local institutional investors in market liquidity and turnover. These developments collectively strengthened the regulatory architecture governing capital-market operations and improved the overall resilience and transparency of the trading, clearing, and settlement framework.

Growing DISB fund enhances system resilience

11.10 The operations of the DISB continued to support domestic financial stability through expanded deposit-insurance coverage, a growing fund

balance, and reinforced public confidence in the banking system. Public awareness efforts, including roadshows in Francistown and Palapye, radio campaigns, and educational publications, further strengthened depositor confidence and reinforced the Scheme's role in promoting financial stability.

Establishment of the Africa Financial Stability Council

11.11 With an increasing interconnectedness across the African continent, with the free flow of capital, cross-border trade, and direct investments across African regions as the main drivers of continental integration and sustainable economic development. In the face of the growing complexity in financial transactions, financial systems, including banks, NBFIs, capital markets, and payment systems, need to be strengthened to ensure safe and efficient intermediation while maintaining confidence among economic agents in financial stability. A robust and resilient financial system that defines and addresses stability issues in a harmonised manner is becoming of paramount importance. Achieving such harmonisation of macroeconomic and financial stability frameworks, as envisaged in the African Association of Central Banks (AACB)'s mandate, would contribute to higher and more inclusive economic growth across member countries, and the continent. Thus, the objectives of the AACB have been reinforced through the establishment of the African Financial Stability Council (Box 11.1).

Box 11.1: The African Financial Stability Committee (AFSC)

Background

The AFSC was established by the Association of African Central Banks (AACB) Governors in September 2024 primarily to enhance cooperation on financial stability issues across the continent and spearhead the first continent wide initiative to produce a comprehensive Financial Stability Report. It also seeks to provide a unified framework for assessing risks and the resilience of African financial systems amid global financial tightening, macroeconomic volatility and domestic vulnerabilities within African financial systems. The AFSC was formally launched at its inaugural meeting in Egypt in December 2024 and the chairmanship of the Committee rotates in line with the chairpersonship of the AACB, while the Central Bank of Egypt (CBE) serves as the Secretariat. The Bank of Central African States (BEAC) is the current chair, succeeding the Bank of Mauritius, which held the inaugural chairmanship.

The AFSC comprises seven voting members and five non-voting observers, serving one-year terms and meets at least annually. Voting members include a chairperson from the central bank holding the AACB chairmanship, a Vice chairperson from the AACB vice-chair country, and five senior financial stability officials representing each of the AACB's sub-regions. The non-voting members consist of financial stability officials from the alternate chair central banks of the sub-regions. The Committee operates through two specialised working groups: the Financial Stability Report (FSR) Working Group (WG), chaired by the CBE, and the Macroprudential Policy Development and Implementation (MPDI) WG, chaired by the Bank of Mauritius. The chairmanship of the working groups is on a permanent basis.

Objectives and Mandate

The AFSC aims to strengthen Africa's financial stability architecture through enhanced macroprudential oversight, coordination and information sharing among member central banks and regulators. Its mandate includes conducting continent-wide risk assessments across banking, NBFIs, capital markets, and payment systems; promoting the harmonisation of supervisory and macroprudential frameworks; and facilitating the exchange of information/data, experiences, and best practices on financial stability monitoring and crisis management. The AFSC also provides comprehensive policy analysis and recommendations on emerging financial vulnerabilities and publishes the annual African Financial Stability Report (AFSR) to support evidence-based decision-making and strengthen regional financial resilience.

Progress to Date

Following its establishment, the AFSC operationalised the FSR WG, which is tasked with assessing key risks to the African financial system and its resilience, evaluating financial stability frameworks across member countries using a common assessment approach developed by the MPDI WG, and drafting the AFSR. The FSR WG held a preparatory session in Cairo, Egypt in September 2025 to finalise data templates, agree on analytical frameworks, and outline the structure of the inaugural report. The first AFSR was subsequently presented and approved for publication at the November 2025 AACB meeting in Cameroon. The 2025 AFSR provides a comprehensive assessment of macro financial developments and systemic risks across Africa, as well as related policy measures to bolster regional resilience and crisis preparedness. At its third meeting in November 2025, the AFSC established the MPDI WG, chaired by the Bank of Mauritius. This technical working group is tasked to strengthen member states' institutional capacity for macroprudential policy formulation and implementation; develop a reference financial stability framework in alignment with international best practice; develop a standardised macroprudential data-sharing platform; design capacity building programmes on systemic risk analysis and financial stress testing; and develop a framework for periodic regional financial stability assessments.

Relevance to Botswana

African economies are increasingly exposed to common and interconnected shocks, including elevated public debt vulnerabilities, commodity price volatility and exchange rate pressures. However, financial stability assessments have historically been conducted in isolation at national level, limiting cross-country comparability and regional coordination. The AFSC addresses this gap by providing a harmonised, system-wide perspective on financial stability risks across the continent.

For Botswana, participation in the AFSC presents a strategic opportunity to contribute and shape Africa's financial stability architecture, including influencing the development of continental standards and policy frameworks. It also provides access to cross-country datasets and peer benchmarking, enhancing technical and analytical depth, policy design and institutional

capacity. Moreover, the AFSC facilitates the development of common metrics such as the Financial Stability Framework Index (FSFI), enabling Botswana to assess its relative performance, identify gaps, and adopt proven policy approaches. Overall, participation strengthens Botswana’s macroprudential policy framework and financial stability governance, supports evidence-based decision-making, and enhances resilience to systemic risks.

Conclusion

The establishment of the AFSC marks a critical milestone in advancing a coordinated and harmonised financial stability framework for Africa. Through enhanced collaboration, data sharing, and joint risk assessment, the AFSC supports the development of more resilient and integrated financial system. For Botswana, engagement in the AFSC provides a valuable platform to strengthen domestic financial stability frameworks through peer learning, improved data quality and consistency, enhanced policy coordination, and alignment with emerging continental standards.

12. CONCLUSION AND OUTLOOK

- 12.1 Botswana's financial system remains sound and resilient, underpinned by strong capital buffers, stable asset quality, improving profitability and well functioning financial market infrastructures. Nevertheless, the balance of risks is increasingly tilted to the upside due to continued macroeconomic, fiscal and external pressures. Weak diamond market conditions, subdued non-mining sector activity, constrained fiscal space and declining external buffers continue to weigh on market liquidity, credit conditions and financial sector confidence.
- 12.2 Sovereign-related vulnerabilities remain a central risk to financial stability. Rising public sector financing needs, increased reliance on domestic borrowing and short-term debt instruments, and recent rating agency downgrades highlight the importance of restoring fiscal sustainability. Elevated sovereign-bank interlinkages may amplify liquidity pressures and pose risks to credit availability, particularly if refinancing costs rise or external conditions tighten further. Fiscal consolidation, revenue mobilisation and improvements in public-financial-management systems will be critical to rebuilding buffers and strengthening resilience.
- 12.3 Liquidity conditions are expected to remain tight in the short term, reflecting ongoing fiscal constraints and uneven cash flow dynamics. While the Bank's liquidity support measures have eased immediate pressures, structural challenges, including concentrated funding bases and limited diversification of bank balance sheets, require continued attention. Strengthening liquidity risk management, expanding stable funding sources and progressing implementation of Basel III standards, including the consideration of additional capital requirements for institutions with high deposit concentration will support stability.
- 12.4 Credit growth is expected to remain moderate as banks balance their risk appetite with the need to preserve strong balance sheet positions. Household credit growth is likely to remain subdued due to tighter affordability and reduced demand for secured lending, while corporate lending may remain constrained by delayed payments, weak cash flows and elevated uncertainty. Nonetheless, the negative credit-to-GDP gap suggests room for prudent credit extension to support economic recovery, provided risks are carefully managed.
- 12.5 NBFIs are a significant component of the financial system. Strengthening surveillance of liquidity transformation, leverage and market valuation risks within this sector will remain a priority. Enhanced coordination among regulators is essential, particularly given rising interconnectedness between NBFIs and banks.
- 12.6 The outlook for financial markets is cautiously optimistic. Equity market liquidity and valuations have improved, supported by pension fund repatriation and structural reforms in the capital market infrastructure. Bond market development is expected to be reinforced by unitisation, centralised settlement and the potential introduction of municipal bonds. However, rising sovereign risk premiums and global yield volatility may place upward pressure on domestic borrowing costs.
- 12.7 Looking ahead, preserving financial stability will require sustained focus on macroprudential vigilance, enhanced scenario analysis and stress testing, and timely deployment of prudential measures to address emerging risks. Continued progress on structural economic reforms, especially through the BTEP and NDP 12, are essential to broadening the productive base, improving resilience and reducing dependency on the diamond sector.
- 12.8 Overall, while the financial system is robust, heightened fiscal, external and structural challenges call for coordinated action across fiscal, monetary, regulatory and macroprudential policy spheres. Successfully addressing these pressures will be key to maintaining investor confidence, safeguarding financial stability and supporting Botswana's long-term growth prospects.

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