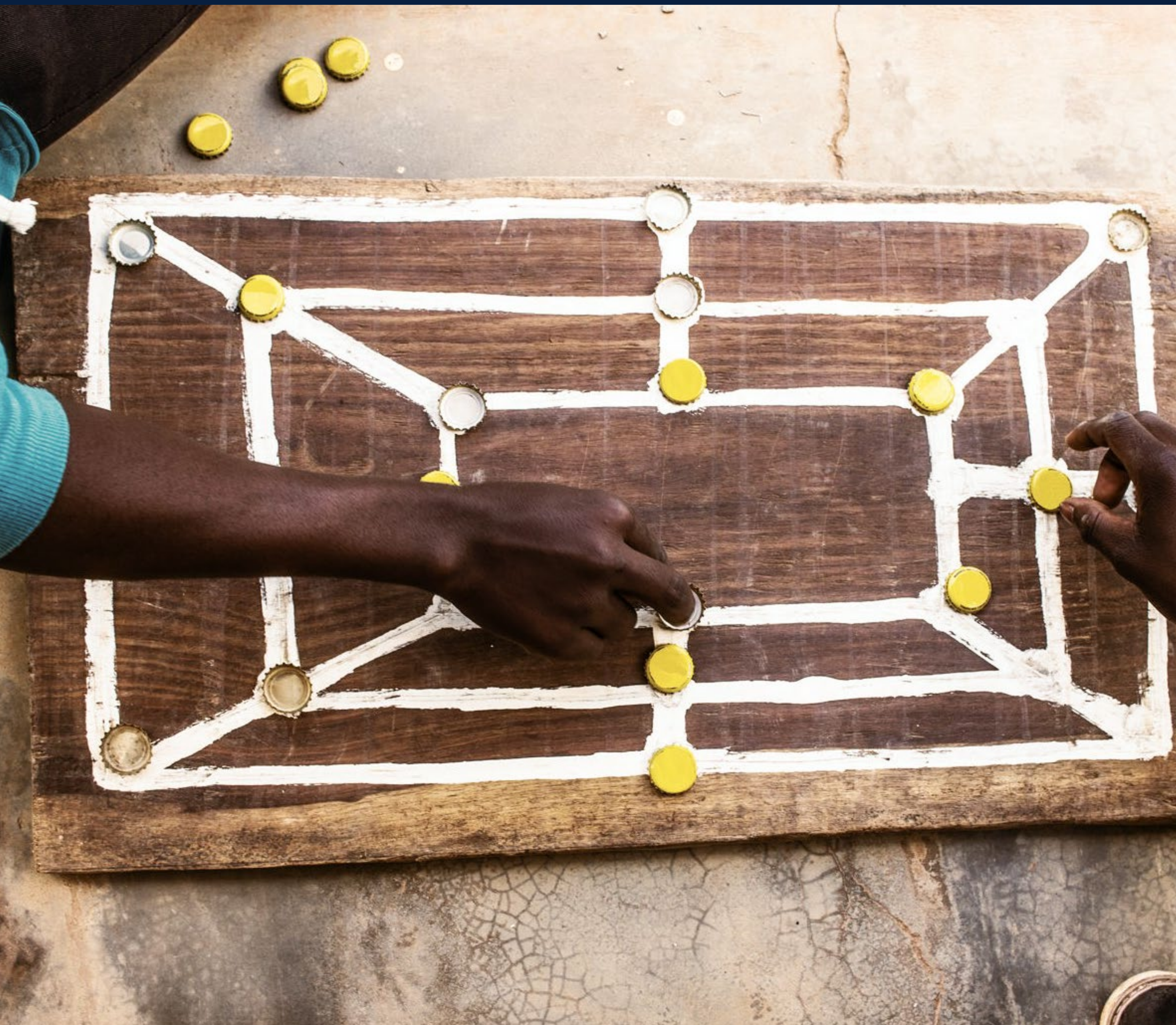
MONETARY POLICY REPORT

APRIL | 2024



STRATEGIC INTENT STATEMENTS

VISION

The Bank aspires to be a world-class central bank with the highest standards of corporate governance and professional excellence.

MISSION

The mission of the Bank is to contribute to the sound economic and financial well-being of the country. The Bank seeks to promote and maintain:

- monetary stability;
- a safe, sound and stable financial system;
- an efficient payments mechanism;
- public confidence in the national currency;
- sound international financial relations; and to provide:
    - efficient banking services to its various clients; and
    - sound economic and financial advice to Government

Monetary Policy Report
April 2024

17938, Khama Crescent, Gaborone, Botswana
Tel: 360 6000 | Website: www.bankofbotswana.bw

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1. PREFACE

1.1 Purpose of the report

The Monetary Policy Report (MPR) is the main medium through which the Bank of Botswana (the Bank) informs the public about the conduct of monetary policy on a regular basis. It serves to meet the public's expectation of a transparent and accountable central bank in fulfilling the monetary policy mandate set out in the Bank of Botswana (Amendment) Act, 2022.

The MPR presents the Bank's review of economic and inflation trends as well as policy performance. The report also provides an assessment of economic and financial developments that are likely to influence the inflation path in the medium term and, in turn, the Bank's future policy choices. In this respect, the MPR promotes an understanding of the conduct of monetary policy to anchor public expectations of a low, predictable and sustainable level of inflation.

1.2 Monetary policy framework

The primary objective of the Bank's monetary policy is to achieve price stability. For Botswana, price stability is defined as a sustainable level of annual inflation, as measured by the consumer price index (CPI), that is within the medium-term objective range of 3 – 6 percent. Consequently, as of April 2022, the Bank uses the Monetary Policy Rate (MoPR) to influence short-term market interest rates to steer the economy through business cycles, thus contributing to sustainable economic growth. The policy is also formulated with a view to safeguarding the stability of the financial system. The monetary policy framework is anchored on the crawling band exchange rate mechanism, which seeks to maintain a stable real effective exchange rate (REER), conducive for macroeconomic stability and the international competitiveness of domestic producers' tradeable goods and services. The Ministry of Finance (MoF), in consultation with the Bank, makes a recommendation on the parameters of the exchange rate mechanism (weights of currencies that comprise the Pula Basket and the rate of crawl) that determine the value of the Pula for approval by His Excellency, the President.

In evaluating policy options, the Bank implements a forward-looking monetary policy framework with a central role for a medium-term inflation forecast. The Bank sets the policy to direct projected movements of inflation towards the medium-term objective range, while considering the prevailing rate of crawl of the exchange rate mechanism, prospects for economic growth and developments relating to the stability of the financial system. The policy horizon is up to 3 years, and evaluated on a rolling basis, because monetary policy affects price developments with an estimated lag of up to four quarters. A proactive approach to setting policy necessitates a continuous review of the inflation outlook.

The monetary policy stance is signalled by the MoPR. To support this signal, the Bank uses open market operations, which entail, primarily, auctioning of the Bank of Botswana Certificates (BoBCs) using fixed rate full allotment system, engaging in repo/reverse repo transactions with commercial banks (primary dealers), and a one-month BoBC paper to help address some of thestructural liquidity positions and support the construction of the short-end of the yield curve (see Box 1 in page 22 for more details on monetary policy implementation and operations framework).

1.3 Decision-making process

Monetary policy is implemented in line with the decisions of the Monetary Policy Committee (MPC). Effective 14 February 2023, and as required by the Bank of Botswana (Amendment) Act, 2022, the MPC comprises nine members, four of whom are external members appointed by the Minister of Finance. All external members have been appointed. The five internal members are the Governor, two Deputy Governors, head of department responsible for economic research and head of department responsible for treasury operations (See Box 3 on page 27 for further details). The MPC holds six pre-scheduled meetings or more per year, as necessary, during which the monetary policy stance is determined. The dates for the MPC meetings for the ensuing year are pre-announced.

1.4 Announcement of the monetary policy decision

The monetary policy decision is announced by the Governor, shortly after each MPC meeting, at a Press Briefing. The Press Briefing allows for interaction with members of the media and to promote understanding of the Bank's economic analysis and policy stance. Afterwards, a Press Release, informing the public of the Committee's decision regarding the MoPR and the reasons for the policy choice is released.

The first MPC meeting of the year, held in February, is accompanied by the issuance of the Monetary Policy Statement, through which the Bank reports on inflation trends, policy performance and the likely policy posture for the ensuing year. Subsequently, the MPR is produced for the April, August and October meetings. The MPR is published on the Bank website (www.bankofbotswana.bw) within a week of the announcement of a policy decision.

BANK OF BOTSWANA'S MONETARY POLICY COMMITTEE

Mr. Cornelius Dekop
Governor (Chairman)

Dr. Kealeboga Masalila
(Deputy Governor)

Dr. Tshokologo Kganetsano
(Deputy Governor)

Mr. Innocent Molalapata
Director, Research and Financial Stability

Mr. Lesego Moseki
Director, Financial Markets

Professor Patricia Makepe
External Member

Dr. Pinkie Kebakile
External Member

Dr. Onkokame Mothobi
External Member

Dr. Taufila Nyamadzabo
External Member

2. EXECUTIVE SUMMARY

In 2024, monetary policy is being implemented in the context of projections for lower inflation in the short-to-medium term, due to base effects associated with upward adjustments in domestic fuel prices and the reversion of value added tax (VAT) from 12 percent to 14 percent in 2023, impact of the reduction in domestic fuel prices on 21 December 2023; the projected appreciation of the Pula against the South African rand; and anticipated lower international food prices and trading partner countries' inflation. The MPC projected the domestic economy to operate below full capacity in the short term and, therefore, not generate demand-driven inflationary pressures. Although inflation is expected to remain below the lower bound (3 percent) temporarily, it will be within the objective range in the medium term and closer to the upper bound in 2025. Thus, the Bank maintained the MoPR at 2.4 percent at the April 2024 MPC meeting, following a 25-basis points policy rate decrease in December 2023.

The Bank's formulation and implementation of monetary policy focuses on entrenching expectations of low, sustainable and predictable level of inflation through a timely response to price developments. The Bank remains committed to responding appropriately to preserving price stability without undermining economic activity.

In 2023, world economic performance and sentiment were negatively affected mostly by the ripple effects of the Russia-Ukraine war, global monetary policy tightening and the lingering effects of the COVID-19 pandemic, particularly zero-COVID policies and lockdowns in China. In addition to the adverse impact on global economic activity, the war resulted in significantly elevated commodity prices and, therefore, inflationary pressures. In response, there was generalised increase in policy interest rates and, hence, tightening of financial conditions.

The global economic outlook for 2024 was revised slightly upwards in the International Monetary Fund (IMF)'s April 2024 World Economic Outlook (WEO), due to stronger-than-earlier forecast performance for the United States (US) and some large emerging market economies. However, global output growth remains below the historical (2000 – 2019) annual average of 3.8 percent, on account of restrictive monetary policies and withdrawal of fiscal support measures introduced during COVID-19 pandemic, increasing geoeconomic fragmentation, extreme weather conditions, as well as low underlying productivity growth. Thus, prospects for growth in both advanced and emerging market economies remain broadly restrained. Growth is forecast to increase modestly from 1.6 percent in 2023 to 1.7 percent in 2024 for advanced economies, while it is expected to decrease marginally from 4.3 percent to 4.2 percent for emerging market economies, in the same period. Overall, global economic growth is forecast to remain unchanged at 3.2 percent between 2023 and 2024.

Global inflationary pressures are generally moderating in both advanced and emerging market economies, due to relatively lower food and fuel prices, as well as high borrowing costs associated with tight monetary policy implemented in 2023 and squeezing of household budgets. Global inflation is estimated to have eased to 6.8 percent in 2023 from 8.7 percent in 2022 and forecast to decline further to 5.9 percent in 2024. International oil prices decreased, averaging below USD90 per barrel in the first quarter of 2024, mainly due to lower demand amid weak global economic activity, the increase in oil supply particularly from the United States and Brazil, as well as weak industrial demand for oil in China. Similarly, the United Nations' Food and Agriculture Organization (FAO) food price index decreased in the first quarter of 2024, mainly due to weak demand resulting from the global economic slowdown, as well as increased seasonal food production in leading producer countries across the globe.

Domestically, headline inflation averaged 3.6 percent in the first quarter of 2024, down from 9.4 percent in the first quarter of 2023, mostly accounted for by the dissipating impact of the increase in domestic fuel prices in 2023, the reduction in domestic fuel prices effected on 21 December 2023, and the restrained growth in the prices of food and non-alcoholic beverages. However, inflation is forecast to temporarily breach the lower bound of the objective range in the second quarter of 2024 and revert to within the objective range on a sustained basis from the third quarter of 2024. The April 2024 inflation forecast has been revised downwards in the short term compared to the February 2024 forecast.

Botswana's real gross domestic product (GDP) increased by 2.7 percent in 2023, compared to a higher growth rate of 5.5 percent in 2022. The slowdown in growth was mainly attributable to the deteriorating global economic conditions, and geopolitical events, including the conflict in Ukraine, which have negatively impacted demand for diamond jewellery and rough diamonds. Effective implementation of the economic transformation reforms and stimulative government expenditure indicated in the 2024/25 Budget, alongside the April 2023 – March 2025 Transitional National Development Plan (TNDP), would be supportive of economic activity through facilitating expansion of productive capacity, accelerating economic transformation and enhancing economic resilience in the medium term. Consequently, the domestic economy is forecast to grow by 4.2 percent and 5.4 percent in 2024 and 2025, respectively.

As at the end of January 2024, the foreign exchange reserves were estimated at P64.6 billion, an increase of 6.8 percent from P60.5 billion in January 2023, which translated into 8.7 months of import cover. The current account of the balance of payments (BoP) is estimated to have recorded a deficit of P10.1 billion in the fourth quarter of 2023, compared to a revised deficit of P3.3 billion in the corresponding period in 2022.

In the year to February 2024, commercial bank credit growth accelerated to 8 percent, from 6 percent in February 2023, driven by higher growth in lending to both the business and household sectors due to increased overdraft credit utilisation and revolving credit facilities, as well as some new loan acquisitions. Meanwhile, money supply (M2) increased annually by 9.2 percent in the year to December 2023, compared to 6.8 percent in December 2022.

An annual downward rate of crawl of 1.51 percent was implemented effective 1 January 2024, with a view to enhancing domestic industry competitiveness. Consequently, the nominal effective exchange rate (NEER) of the Pula depreciated by 1.5 percent in the twelve months to March 2024. Against the Pula basket currencies, the Pula appreciated by 0.8 percent against the South African rand and depreciated by 3.4 percent against the Special Drawing Rights (SDR) in the twelve months to March 2024. In the year to March 2024, the REER depreciated by 2.4 percent, due to the depreciation of the NEER (rate of crawl) and lower inflation in Botswana than in trading partner countries, suggesting a marginal gain in Botswana's export competitiveness.

3. RECENT ECONOMIC DEVELOPMENTS

3.1 Recent global economic developments

Global growth subdued

According to the April 2024 WEO, the global economy is estimated to have grown by 3.2 percent in 2023, compared to an expansion of 3.5 percent in 2022 (Table 3.1). The lower growth for 2023 was partly due to the impact of central banks' policy rate hikes to combat inflation and associated tighter financial conditions across the globe, the negative spill over effects from the Russia-Ukraine war, withdrawal of fiscal support measures introduced during COVID-19 pandemic, extreme weather events, weaker growth in some advanced economies, particularly the euro area, as well as subdued growth in China amid a property sector crisis.

Meanwhile, growth outturn for the second half of 2023 was stronger than expected, particularly in several major emerging market economies, mainly in India.

The US economic growth slowed

The US real output expanded by an annualised 3.4 percent (third estimate) in the fourth quarter of 2023, below the 4.9 percent expansion in the third quarter of 2023. The lower output growth for the fourth quarter mainly reflected a negative contribution of private inventories, which subtracted 0.27 percentage points from growth.

Euro area growth stagnates

In the euro area, GDP growth was flat in the fourth quarter of 2023, following a 0.1 percent contraction in the third quarter of 2023, as persistently high inflation and borrowing costs, as well as weak external demand continued to exert downward pressure on growth. Among the bloc's largest economies, output in Germany contracted by 0.3 percent, while it grew by 0.6 percent, 0.2 percent and 0.1 percent in Spain, Italy and France, respectively, in the same period.

United Kingdom (UK) entered a technical recession

GDP in the UK contracted for the second consecutive quarter, registering a 0.3 percent contraction in the fourth quarter of 2023, following a 0.1 percent contraction in the third quarter, and worse than the market expectation of a 0.1 percent decline. The economy entered a technical recession amid a broad-based decline in output, particularly in services, industrial production (mostly manufacturing of machinery and equipment) and construction sectors. In expenditure terms, there was a fall in the volume of net trade, household spending and government spending.

Emerging markets' growth improved

Output growth in emerging markets improved in the second half of 2023, primarily due to stronger-than-expected growth in India, the reopening of China, as well as lower global commodity prices, particularly food and fuel. The improvement in growth for the economic group also indicates the removal of COVID-19 restrictions and governments' efforts to stimulate economic activity.

The Indian economy grew, year on year, by 8.4 percent in the fourth quarter of 2023, compared to an upwardly revised expansion of 8.1 percent in the third quarter of 2023, and was above the market expectation of 6.6 percent. Growth in the fourth quarter of 2023 was driven by stellar performances in services, finance and real estate.

China's economy expanded annually by 5.3 percent in the first quarter of 2024, slightly higher than the 5.2 percent in the fourth quarter of 2023, and exceeded the market expectation of 5 percent growth. Growth in the first quarter of 2024 was supported by the stimulus package from Beijing[1] and spending related to the Lunar New Year Festival. This was the largest yearly expansion since the second quarter of 2023. However, industrial output and retail sales experienced weaker-than-expected growth in March 2024, underscoring the impact of persistently weak consumption and a prolonged property sector crisis.

South African economy remains subdued

Regionally, output growth in South Africa remained subdued but increased, quarter on quarter, by 0.1 percent in the fourth quarter of 2023, from a contraction of 0.2 percent in the third quarter of 2023. However, output growth for the quarter was below market expectation of an expansion of 0.3 percent. The restrained growth was mainly attributed to persistent rotational load shedding, logistical constraints, as well as the challenging global environment. Output growth in the fourth quarter of 2023 was driven by the transport, storage and communication sector (2.9 percent) and the finance industry (2.8 percent), which contributed 0.2 percentage points and 0.1 percentage points to GDP growth, respectively.

1 The Chinese government issued a net 3.96 trillion Yuan in special bonds in 2023, exceeding the annual quota of 3.8 trillion Yuan to finance government spending aimed at supporting economic recovery post COVID-19.

Table 3.1: Growth Estimates and Projections

	Estimate		Projection	
	2022	2023	2024	2025
Global	**3.5**	**3.2**	**3.2**	**3.2**
Advanced economies	**2.6**	**1.6**	**1.7**	**1.8**
USA	1.9	2.5	2.7	1.9
Euro area	3.4	0.4	0.8	1.5
UK	4.3	0.1	0.5	1.5
Japan	1.0	1.9	0.9	1.0
EMDEs	**4.1**	**4.3**	**4.2**	**4.2**
China	3.0	5.2	4.6	4.1
Brazil	3.0	2.9	2.2	2.1
India	7.0	7.8	6.8	6.5
Russia	-1.2	3.6	3.2	1.8
South Africa	1.9	0.6	0.9	1.2
Botswana	**5.5**	**2.7**	**3.6 (4.2)**	**4.6 (5.4)**

Source: IMF WEO April 2024 and MoF for Botswana.
Note: EMDEs stands for emerging market and developing economies, while figures in parentheses are forecasts by the MoF.

Global commodity prices

Rough Diamond prices decreased in the first quarter of 2024

The global rough diamond price index decreased by 2.5 percent from 153.3 points in the fourth quarter of 2023 to 149.5 points in the first quarter of 2024, mainly due to a decline in demand, amid high inflation, rising interest rates and a shift towards spending on travel. Moreover, the decrease in demand for diamonds was due to increased competition from lab grown diamonds as a substitute product.

Polished diamond prices decreased in the fourth quarter of 2023

The global polished diamond price index also decreased by 10.3 percent from 121.6 points in the third quarter of 2023 to 109 points in the fourth quarter of 2023, amid a rise in inventory levels due to weaker demand and global economic outlook. The global polished diamond price index averaged 110 points in January 2024.

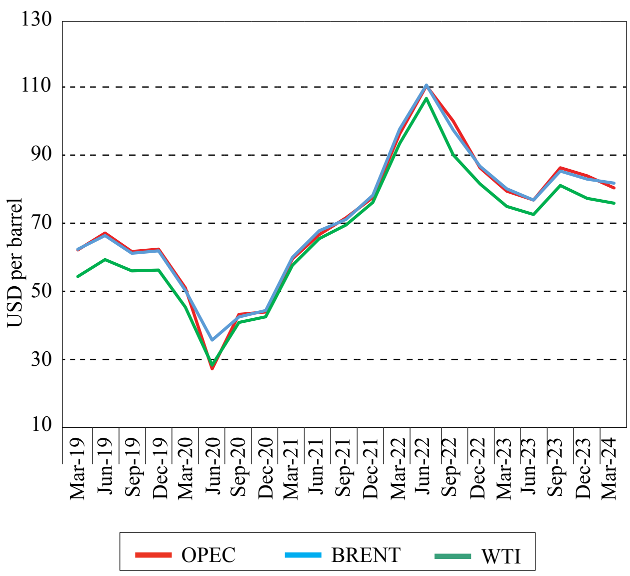
Oil prices decreased in the first quarter of 2024

International oil prices decreased in the first quarter of 2024 compared to the fourth quarter of 2023 but remained above the pre-pandemic levels (Chart 3.1). The price of the Organization of the Petroleum Exporting Countries (OPEC) reference crude oil basket, Brent crude and West Texas Intermediate (WTI) decreased by 4.4 percent, 2 percent and 1.5 percent, from an average of USD85.43 per barrel, USD78.60 per barrel and USD84.33 per barrel in the fourth quarter of 2023 to an average of USD81.70 per barrel, USD77.01 per barrel and USD83.06 per barrel, respectively, in the first quarter of 2024.

The decrease in oil prices was, in part, due to lower demand concerns amid weak global economic activity, the increase in oil supply, particularly from the US and Brazil, as well as weakening industrial demand for oil in China.

Meanwhile, international oil prices increased marginally, month on month, in March 2024. The increase in oil prices was mainly driven by the increase in commercial shipping vessels attacks by the Houthis rebels on the Red Sea, as a result of the escalation of the Israel-Hamas war. This resulted in heightened supply concerns with major oil companies, such as BP suspending transportation of oil via the Red Sea. Moreover, OPEC and its allies' agreement to cut production, as well as Saudi Arabia and Russia's decision to voluntarily increase their production cuts and continued draw down in US crude oil inventories, contributed to the increase in oil prices.

Chart 3.1: International Oil Prices

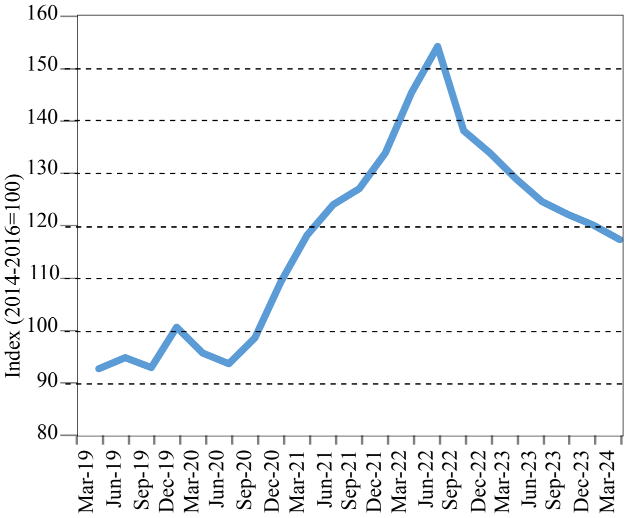


Source: Bloomberg

Food prices decreased in the first quarter of 2024

According to FAO, the global food price index decreased by 2.2 percent from an average of 120.3 points in the fourth quarter of 2023 to an average of 117.6 points in the first quarter of 2024 but remained above pre-pandemic levels (Chart 3.2). The decrease was attributable to increased seasonal supply from some major commodity exporting countries, such as maize from Brazil and the US; vegetable oil in the US and South Asia, sugar in Thailand and Brazil and meat in Australia; as well as modest demand resulting from the global economic slowdown.

Chart 3.2: Food Price Index

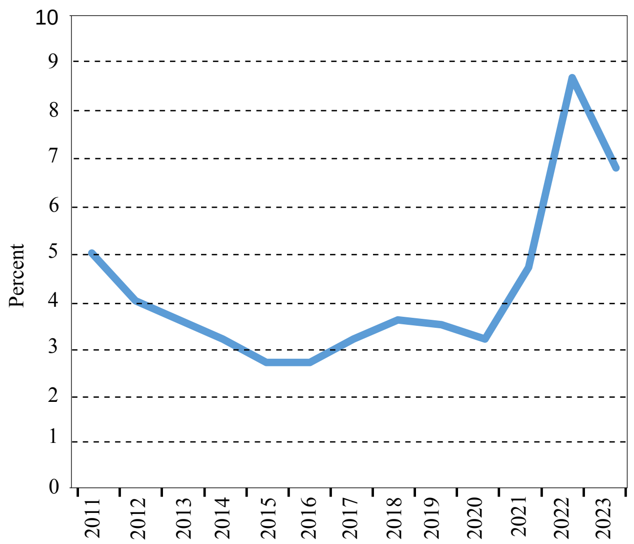


Source: FAO

Global inflation eased in the first quarter of 2024

Globally, inflationary pressures eased in the first quarter of 2024[2], due to relatively lower food and fuel prices, tight monetary policy and squeezing of household budgets. Inflation for advanced economies decreased from 4.5 percent in the fourth quarter of 2023 to 4.3 percent in the first quarter of 2024. However, inflation for emerging market economies increased significantly from 2.8 percent to 7.9 percent in the same period, due to increase in costs of production in the manufacturing and service sectors amid rising worldwide transport costs due to disruptions to shipping in the Red Sea. Global inflation is estimated to have decreased from 8.7 percent in 2022 to 6.8 percent in 2023 (Chart 3.3).

Chart 3.3: Global Inflation

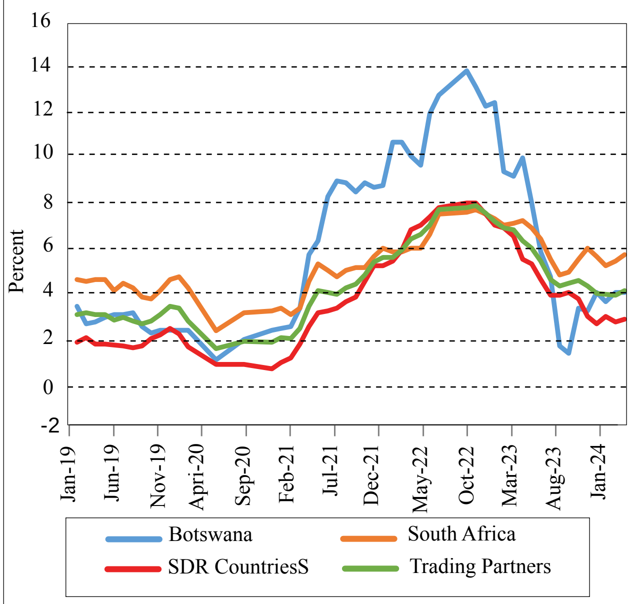


Source: IMF April 2024 WEO

In South Africa, headline inflation decreased slightly from 5.5 percent in the fourth quarter of 2023 to 5.4 percent in the first quarter of 2024, remaining within the South African Reserve Bank (SARB)'s target range of 3 – 6 percent.

The average trade-weighted inflation for Botswana's trading partners decreased from 4.3 percent in the third quarter of 2023 to 4 percent in the fourth quarter of 2023 (Chart 3.4). Meanwhile, trade-weighted inflation for Botswana's trading partners increased from 3.8 percent in January 2024 to 4 percent in February.

Chart 3.4: Botswana Inflation and International Inflation



Source: Statistics Botswana, Bank of Botswana, Statistics South Africa and Bloomberg

Monetary policy divergence across the globe

In the most recent policy review, there was divergence in monetary policy decisions (Table 3.2). The European Central Bank (ECB) maintained the deposit rate, refinancing rate and lending at 4.5 percent, 4.75 percent and 4 percent, respectively, in April 2024, following a series of ten consecutive rate increases since July 2022, which elevated the refinancing operations rate to a 22-year high. The Governing council reaffirmed its determination to ensure that inflation returns to its 2 percent target over the medium term, saying it will maintain interest rates at these high levels for a sufficiently extended period until it achieves that objective despite the decline in inflationary pressures.

In March 2024, the US Federal Open Market Committee (FOMC) maintained the target policy rate at 5.25 – 5.50 percent, for a fifth consecutive time, reflecting policymakers' dual focus on returning inflation to the 2 percent target, while avoiding excessive monetary tightening. The Fed has maintained its projection for a 75-basis points rate cut in 2024, but generally noted that they did not expect it would be appropriate to reduce it until they had gained greater confidence that inflation was moving sustainably towards the 2 percent target objective. In assessing the appropriate stance of monetary policy, the

2 The quarterly inflation estimates are sourced from Bloomberg.

FOMC reinforced that the future path of the policy rate would depend on incoming data, the evolving outlook, and the balance of risks. In addition, the FOMC will continue reducing its holdings of Treasury securities, agency debt and agency mortgage-backed securities.

The Bank of England (BoE) maintained its Bank Rate at 5.25 percent in March 2024, for the fifth consecutive time in nearly two years. The Committee acknowledged that headline inflation had continued to fall sharply. However, the restrictive stance of monetary policy was weighing on activity in the real economy, leading to a looser labour market and containing inflationary pressures. Nonetheless, key indicators of inflation persistence remained elevated. The BoE emphasised that monetary policy would need to remain restrictive for sufficiently long to return inflation to the 2 percent target sustainably in the medium term.

The Bank of Japan (BoJ) increased the key short-term interest rate by 10 basis points from -0.1 percent to 0 – 0.10 percent in March 2024, ending its eight years of negative interest rates, as inflation had exceeded the central bank's 2 percent objective in over a year, while some companies have agreed to raise salaries by 5.28 percent, the biggest wage hike in three decades. Moreover, the BoJ terminated yield curve control for 10-year government bonds and discontinued the purchases of Japanese exchange-traded funds (ETFs) and Japan real estate investment trusts (J-REITs). The BoJ provided forward guidance that it would slowly reduce the pace of corporate bond buying before fully stopping it in about a year.

In emerging market economies, the Central Bank of Brazil cut the policy rate by 50 basis points to 10.75 percent for the sixth consecutive meeting in March 2024, against the backdrop of anticipated economic slowdown and disinflationary pressures. Moreover, the Committee stated that the total magnitude of the easing cycle over time will depend on the evolution of inflationary dynamics, inflation expectations, particularly longer-term ones, their projections of inflation, the output gap and the balance of risks. The Committee stated that the decision is in line with the strategy of anchoring inflation around the target over a relevant horizon, while anticipating further cuts of the same magnitude in the next meetings.

Conversely, the Central Bank of Russia (CBoR) maintained the key policy rate at 16 percent at the March 2024 meeting, following a cumulative 850 basis points increase in 2023, and signalled that it will leave borrowing costs at a restrictive level for a long period to achieve its inflation target. The CBoR indicated that the risk to the inflation outlook had improved since the last meeting, although demand continues to outstrip the country's capacity for producing goods and services, limiting investor's hopes for looser monetary conditions.

In March 2024, the People's Bank of China (PBoC) maintained the one-year and five-year Loan Prime Rates (LPR) unchanged at 3.45 percent and 3.95 percent, respectively, as commercial banks face the pressure of rising operational costs, and the economic recovery gains momentum.

The SARB maintained the repo rate at 8.25 percent in March 2024, to anchor inflation expectations more firmly around the mid-point of the 3 – 6 percent target range. The SARB judged the policy rate to be restrictive, consistent with elevated inflation expectations and the inflation outlook. The SARB considered risks to the inflation outlook to be on the upside and expected headline inflation to average 5.1 percent (revised upwards from 5 percent in the previous forecast) in 2024. The SARB emphasised that its future policy decisions will be data dependent and sensitive to the balance of risks to the outlook.

In April 2024, the Reserve Bank of India (RBI) maintained the policy rate at 6.5 percent for the seventh consecutive meeting. The RBI projected that headline inflation would average 4.5 percent in 2024, compared to a forecast of 5.4 percent at the previous meeting. Additionally, the RBI remains focused on withdrawal of accommodative policy stance to ensure that inflation progressively reaches the midpoint of the 2 – 6 percent inflation target, while supporting growth.

Table 3.2: Monetary Policy Decisions

Central Bank	Latest Meeting	Current Policy Rate (Percent)	Change from Previous Meeting	Likely Policy Decision at the Next Meeting
Bank of Botswana	April 2024	2.4	No change	No indication of the direction of policy
SARB	March 2024	8.25	No change	With the latest inflation projection (March 2024) showing that inflation is expected to remain within target, the policy rate is likely to remain unchanged. However, the SARB is expected to respond to new data and risks.
US Federal Reserve	March 2024	5.25-5.50	No change	The Federal Reserve has maintained its projection for 75 basis points rate cut in 2024, but generally noted that they did not expect it would be appropriate to reduce it until they had gained greater confidence that inflation was moving sustainably towards the 2 percent target objective.
BoE	March 2024	5.25	No change	The Committee emphasised that monetary policy would need to remain restrictive for sufficiently long to return inflation to the 2 percent target sustainably in the medium term. However, Governor Bailey expressed optimism about Britain's economic trajectory, suggesting that conditions were favourable for the central bank to begin reducing interest rates, but stressed the necessity for greater certainty regarding the economy's control over price pressures.
ECB	April 2024	4.50	No change	Monitoring current market tensions closely and ready to respond as necessary to preserve price stability and maintain financial stability in the region. Likely to maintain policy stance. Currently, there is a probability of a policy hike in June 2024 with a cumulative 130 basis points policy rate cut expected by December 2024.
BoJ	March 2024	0-0.10	No change	Noted that the virtuous cycle between wages and prices will intensify and inflation has increased to 2 percent in over a year, and some companies having agreed on salary hikes. Thus, the BoJ is likely to increase the key interest rate at the next meetings.
PBoC	March 2024	3.45	No change	The PBOC is committed to keeping liquidity adequate at a reasonable level, keep credit growing reasonably at a stable pace, and ensure that the growth of money supply and the aggregate financing to the real economy are generally in line with the nominal GDP growth. Given this commitment, the PoBC is likely to keep the LPR low until the economy has recovered.
Brazil	March 2024	10.75	Decreased by 50 basis points	The inflation profile gives confidence to gradually ease monetary policy and the total magnitude of the easing cycle over time will depend on the evolution of inflationary dynamics, inflation expectations, particularly longer-term ones, their projections of inflation, the output gap and the balance of risks.
India	April 2024	6.50	No change	RBI remains focused on withdrawal of accommodation to ensure that inflation remains within the target going forward, while supporting growth.
Russia	March 2024	16.00	No change	Noted that inflationary outlook had improved since the previous meeting, although risks were judged to still be on the upside. Signalled that it will leave borrowing costs at a restrictive level for a long period to achieve its inflation target.

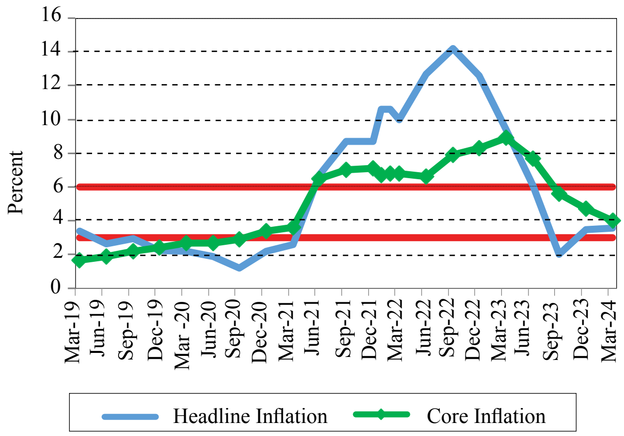
Source: Various central banks' websites.

3.2 Domestic inflation environment

Headline inflation decreased in the first quarter of 2024

Headline inflation averaged 3.6 percent in the first quarter of 2024, compared to 9.4 percent in the first quarter of 2023 (Chart 3.5 and Table 3.3). The decrease in inflation in the first quarter of 2024 was mostly accounted for by the dissipating impact of the increase in domestic fuel prices in 2023, the reduction in domestic fuel prices effected on 21 December 2023[3] and the slower growth in the prices of food and non-alcoholic beverages.

Chart 3.5: Botswana Headline and Core Inflation

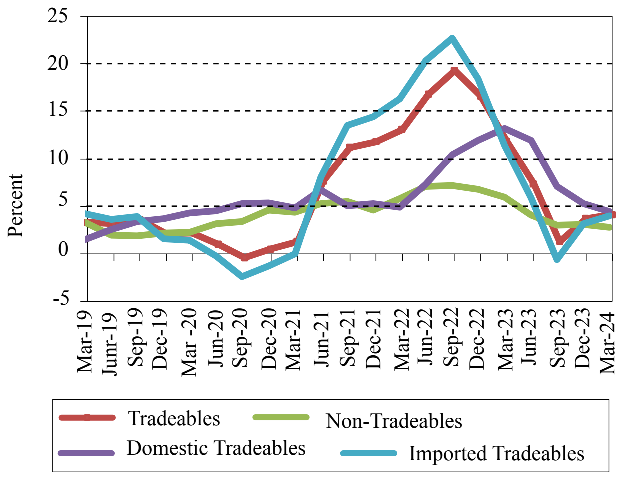


Source: Statistics Botswana and Bank of Botswana
Note: Core Inflation is headline inflation excluding administered prices.

Prices for domestic tradeables and imported tradeables decreased in the first quarter of 2024

Inflation for domestic tradeables decreased from an average of 13.2 percent in the first quarter of 2023 to an average of 4.5 percent in the first quarter of 2024 (Chart 3.6), due to the broad-based decrease in food prices as well as price of cement. Imported tradeables inflation decreased from an average of 11.4 percent to an average of 4 percent in the same period, due to the decrease in domestic fuel prices and dissipating impact of the increase in domestic fuel prices in 2023, deceleration in vehicle prices mainly on account of dealership discounts, as well as broad-based decrease in prices of imported goods. As a result, all tradeables inflation decreased from an average of 11.8 percent in the first quarter of 2023 to an average of 4.1 percent in the first quarter of 2024. Inflation for non tradeables also decreased from an average of 6 percent to 2.8 percent in the same period, due to deceleration in price of private rentals, as well as consultation fees for health specialists.

Chart 3.6: Inflation for Tradeables and Non-Tradeables



Source: Statistics Botswana

Generally, there has been a downward trend in non-tradeables inflation since June 2022 and domestic tradeables inflation from March 2023. The reduction in non tradeables inflation was mainly due to the base effects associated with the upward adjustment in administered prices in 2022, while for domestic tradeables, the reduction was attributable to restrained growth in food prices. The decrease in food prices was partly a result of the decrease in oil prices, an input in food production.

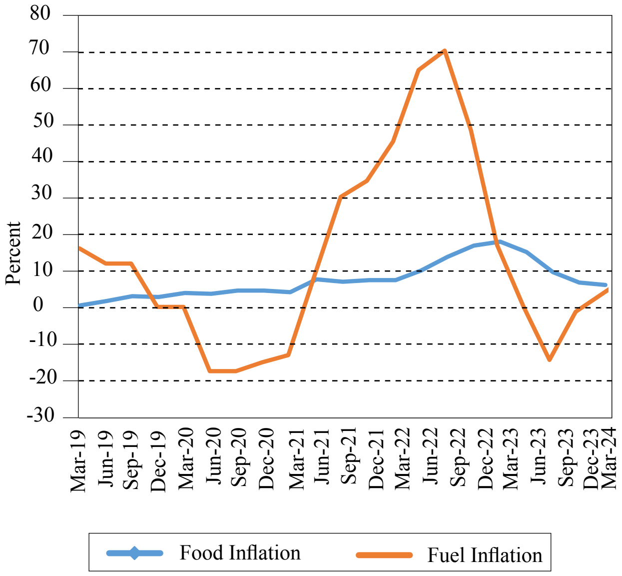
Core inflation measures decreased in the first quarter of 2024

The trimmed mean inflation (CPITM) decreased to 3.3 percent in the first quarter of 2024, from 8.6 percent in the first quarter of 2023, while inflation excluding administered prices (CPIXA) averaged 4 percent from 8.9 percent (Table 3.3) due to the decline in prices of food and non alcoholic beverages, deceleration in prices of vehicles, cement and other building materials, as well as consultations fees for health specialists. Similarly, inflation excluding food and fuel[4] (CPIXFF) averaged 3.8 percent in the first quarter of 2024, lower than the 6.4 percent recorded in the corresponding quarter in 2023, due to the decrease in vehicle prices mainly on account of dealership discounts in the same period.

3 The cut-off for price collection surveys by Statistics Botswana is the 20th of every month. Therefore, the decrease implemented on 21 December 2024 fell outside the period used for the calculation of inflation. Hence, the impact was realised in January 2024.

4 Food inflation decreased from an average of 6.4 percent in the fourth quarter of 2023 to an average of 5.6 percent in the first quarter of 2024, while fuel inflation increased from an average of -1.2 percent to an average of 3.3 percent in the same period (Chart 4.3).

Chart 3.7: Food and Fuel Inflation



Source: Statistics Botswana and Bank of Botswana

Table 3.3: Annual Price Changes for Categories of Goods and Services (Percent)

Category of commodities	Basket Weights	March 2024	Q1 2024	Q1 2023
Food and non-alcoholic beverages	13.6	5.0	5.6	17.4
Alcoholic beverages and tobacco	4.3	5.3	5.8	2.8
Clothing and footwear	6.0	4.3	4.8	5.7
Housing, water, electricity, gas and other fuels	17.5	1.3	1.3	4.6
Furnishing, h/h equipment and routine maintenance	4.9	4.5	4.8	6.6
Health	3.4	1.8	1.7	3.3
Transport	23.4	0.7	2.5	15.6
Communications	6.9	0.5	0.6	2.6
Recreation and culture	2.8	3.1	3.0	3.3
Education	4.6	1.5	1.4	5.4
Restaurants and hotels	3.7	5.6	5.7	6.1
Miscellaneous goods and services	9.0	8.5	8.6	8.6
Annual Inflation (All items)	**100.0**	**2.9**	**3.6**	**9.4**
CPITM		2.6	3.3	8.6
CPIXA		3.7	4.0	8.9
CPIXFF		3.1	3.8	6.4

Source: Statistics Botswana and Bank of Botswana calculations

3.3 Recent domestic economic developments

GDP growth decelerated in 2023

Real GDP grew by 2.7 percent in 2023, compared to a higher growth of 5.5 percent in 2022 (Chart 3.8). The slowdown in growth was mainly attributable to the deteriorating global economic conditions, and geopolitical events, including the conflict in Ukraine, which have negatively impacted demand for diamond jewellery and rough diamonds. Mining sector GDP grew by 3.1 percent in 2023, a notable deceleration from the 7.6 percent recorded in 2022. This was due to a slower growth in output of most sub-sectors, led by diamond mining, which decelerated to 3.2 percent, compared to the higher growth of 7 percent in the previous year. The slower growth in the sector reflects deteriorating global economic conditions, and geopolitical events, including the conflict in Ukraine, which have negatively impacted demand for diamond jewellery and rough diamonds. Furthermore, copper production decelerated to 35.2 percent in 2023, from a significant growth of 207.8 percent, due to base effects of the resumption of copper production in the third quarter of 2021.

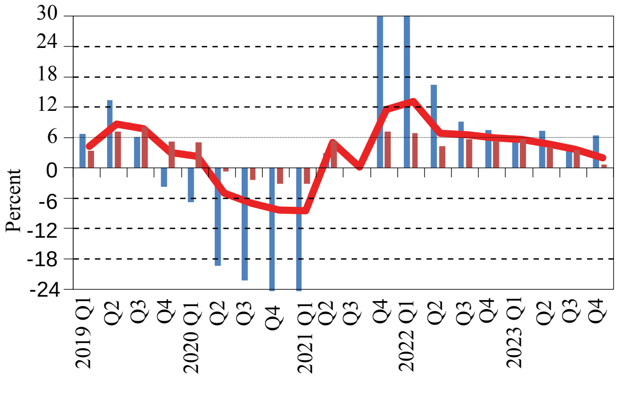
Meanwhile, output of other mining sub-sectors, such as mining of gold and other metal ores, mining of soda ash and salt, as well as mining of coal decreased in 2023. The contraction in the output of gold is due to resource depletion as the lifespan of the Mupane Mine approaches the end, while plant care and maintenance at the Sowa Pan Mine that took place in the second quarter of 2023, decreased mining of soda ash and salt output.

Non-mining GDP grew by 2.6 percent in 2023, compared to a growth of 4.9 percent in 2022. The decrease was due to contraction in the output of the Diamond Traders sector, reflecting deteriorating global economic conditions and geopolitical events. The contraction in Water and Electricity sector, attributable to operational challenges realised at Morupule B Power Station since the second quarter of 2023, also contributed to the deceleration in non-mining output. Furthermore, the slowdown in output growth for some sectors, namely, Manufacturing, Information and Communication Technology, Wholesale and Retail, Transport and Storage, Accommodation and Food Services, and Human Health and Social Work also contributed to the overall deceleration in the non-mining sector output growth.

Meanwhile, Statistics Botswana reported a 1.9 percent increase in real GDP in the fourth quarter of 2023[5], compared to an increase of 5.5 percent in the fourth quarter of 2022.

5 Calculated as the current quarter over the corresponding quarter in the previous year.

Chart 3.8: GDP Growth Rates



Source: Statistics Botswana

Note: Growth rates are reported on a rolling 12-month basis.

In terms of GDP by expenditure, growth in Government Final Consumption was 4 percent in 2023, compared to a growth of 2.5 percent in 2022. The increase was largely due to a faster growth in the output of individual consumption and collective consumption[6], which accelerated to 8.8 percent from 3.5 percent, and 2.7 percent from 2.3 percent, respectively, in the review period.

Household Final Consumption grew by 5.6 percent in 2023, compared to a growth of 3.1 percent recorded in 2022. The expansion in Household Final Consumption was due to an increase in both the Non-profit Institutions Serving Households (NPISH) and Household Consumption Expenditure.

Gross Fixed Capital Formation (GFCF) increased by 4.2 percent in 2023, compared to a decrease of 0.2 percent in the previous year. The increase in GFCF was due to the expansion in investment in transport equipment; plant, machinery and equipment; and mineral prospecting subsectors

Table 3.4: Real GDP Growth by Sector and Expenditure (Percent)

	2022 Q4	2023 Q3	2023 Q4
Total GDP	**5.5**	**3.6**	**2.7**
By Sector:			
Mining and Quarrying	7.6	3.9	3.1
Non-Mining	4.9	3.5	2.6
Agriculture, Forestry & Fishing	1.2	1.1	1.3
Manufacturing	8.2	3.1	1.9
Water and Electricity	48.9	0.7	-16.9
Construction	3.2	3.4	3.3
Wholesale & Retail	5.8	4.6	4.5
Diamond Traders	15.0	-7.0	-29.4
Transport and Storage	4.1	4.5	3.8
Accommodation & Food Services	4.3	4.6	4.7
Information & Communication Technology	5.6	4.4	3.9
Finance, Insurance & Pension Funding	1.9	4.5 (3.7)	5.6
Real Estate Activities	3.6	4.9	5.4
Professional, Scientific & Technical Activities	3.0	4.2	4.9
Administrative & Support Activities	3.7	4.4	4.6
Public Administration & Defence	4.5	4.2 (4.4)	5.1
Human Health & Social Work	4.0	3.8	3.7
Education	4.6	5.3	5.2
Other services	2.4	3.3	3.5
By Type of Expenditure:			
Government Final Consumption	2.5	2.4 (1.7)	4.0
Household Final Consumption	3.1	5.0	5.6
Gross Fixed Capital Formation	-0.2	2.4	4.2
Exports of Goods and Services	-5.3	-17.8	-16.2
Imports of Goods and Services	-11.7	-22.1	-9.9

Source: Statistics Botswana and Bank of Botswana Calculations.

Note: Figures in brackets are earlier estimates which have now been revised.

6 Collective consumption expenditure comprises the expenditures made by general government on services that benefit households, collectively while individual consumption expenditure includes expenditure whose real consumer is identifiable and the ultimate benefit falls to households e.g., education and healthcare.

Diamond production decreased in the first quarter of 2024

Debswana Diamond Company produced 5 million carats of diamonds in the first quarter of 2024, 27.7 percent lower than the 6.9 million carats produced in the corresponding period in 2023. The lower production in the first quarter of 2024 was in response to the deteriorating global economic conditions, and geopolitical events, including the conflict in Ukraine. Meanwhile, Debswana's production target for 2024 has been revised downwards to 20.7 million carats from 23.7 million carats in 2023 and initial target for 2024 at the beginning of the year. Similarly, production guidance for the larger De Beers Group has also been revised down to 26 – 29 million carats from 29 – 32 million carats, subject to trading conditions.

Production at Lucara Diamond Corporation (Karowe Mine) increased by 13.3 percent to 98 177 carats in the fourth quarter of 2023, from 86 655 carats produced in the corresponding period in 2022. The increase was mainly attributable to the increased number of special stones (greater than 100 carats in weight).

Budget surplus recorded in the first quarter of the 2023/24 fiscal year

Government budget was in a surplus of P5.2 billion in the first quarter of the 2023/24 fiscal year (Table 3.5). The surplus was mainly due to good revenue performance, driven by larger-than-expected mineral receipts, reflecting supply constraints stemming from the United States and European sanctions on the import of Russian diamonds. Regarding other major revenue streams, the Southern African Customs Union (SACU) revenues and Bank of Botswana revenues were generally in line with the 2023/24 budget. Total government expenditure and net lending was P19.2 billion, lower than the P21.8 billion anticipated in the budget.

For the 2023/2024 fiscal year, it is expected that the deficit will be P7.1 billion (2.6 percent of GDP). Recurrent spending also included the 5 percent salary increment for public service employees effected in April 2023. Specific to development spending, the budget was used to fill infrastructure gaps (implementation of delayed projects from the previous financial year) in order to unlock economic growth. Consequently, the projection for expenditure and net lending has been revised upwards by 1.6 percent to P88.8 billion, which is equivalent to 31.8 percent of GDP (thus slightly above the fiscal rule limiting total expenditure to 30 percent of GDP). The increase in expenditure and net lending is lower than the change in the consumer price index, hence not inflationary.

Table 3.5: Quarterly Budget Outturns (P Million)

	Total Revenues and Grants	Total Expenditure and Net Lending	Budget Surplus/ Deficit
2022/23 Q1	20 438	19 793	645
2022/23 Q2	17 264	18 287	-1 023
2022/23 Q3	17 670	16 386	1 283
2022/23 Q4	18 727	19 623	-896
2023/24 Q1	24 389	19 215	5 173

Source: Cash Flow Unit, Ministry of Finance

Labour Force and Wage Developments Trends[7]

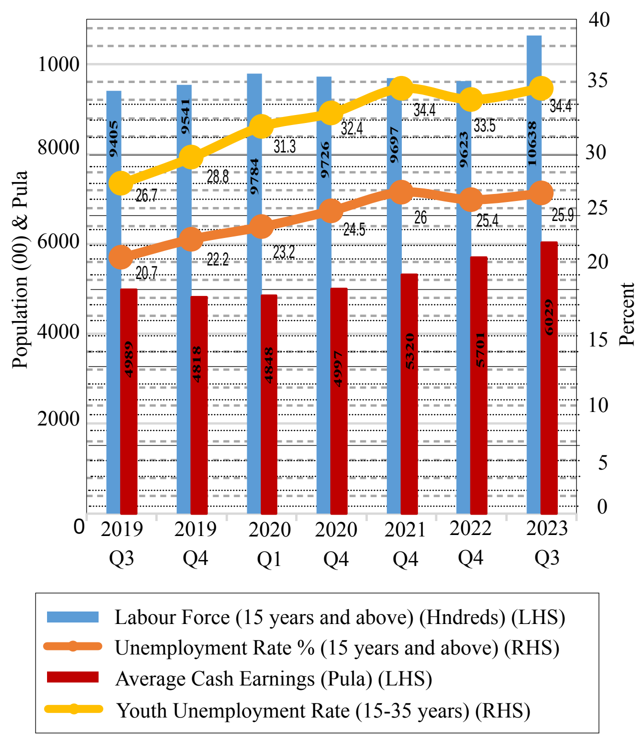
According to Statistics Botswana's Quarterly Multi-Topic Survey (QMTS) report for the fourth quarter of 2023, the unemployment rate was 25.9 percent in the third quarter of 2024, compared to 25.4 percent in the fourth quarter of 2022[8] (youth unemployment rate rose to 34.4 percent from 33.5 percent). The survey also indicates that formal sector employment increased by 0.9 percent to 490 625, from 486 376 in the review period.

Regarding other indicators, the survey indicates that Government continued to be the single largest employer, with employment in public administration constituting 18.3 percent of total formal sector employment. In this regard, personal emoluments constitute the largest share (above 50 percent) of the government recurrent budget, and about 13 percent of GDP. Meanwhile, the formal sector average earnings per month were estimated at P7 396 for citizens, P15 863 for noncitizens and P7 692 for all employees in the third quarter of 2023. The average monthly earnings for all employees are estimated to have increased by 13.1 percent or P889 from P6 803 estimated for the fourth quarter of 2022, therefore, higher than the change in the consumer price index (general prices) and the inflation objective. A longer-term trend analysis of the QMTS data since the third quarter of 2019 indicates that the total labour force (15 years and above) increased by 13.1 percent to 1 063 776 persons in the third quarter of 2023, from 940 546 persons in the third quarter of 2019. Over the same period, the employed labour force increased by 5.8 percent. The overall unemployment rate was estimated at 25.9 percent in the third quarter of 2023, compared to 20.7 percent recorded in the third quarter of 2019. Youth labour force (15–35 years) increased by 8.1 percent, to 520 582 persons in the third quarter of 2023 from 481 441 persons in the third quarter of 2019. The youth unemployment rate, which continues to be a national concern, increased to 34.4 percent in the third quarter of 2023, compared to 26.7 percent in the third quarter of 2019. Meanwhile, average earnings for all employees increased by P1 040, from the P4 989 estimated for the third quarter of 2019.

7 The QMTS is conducted by Statistics Botswana. Since its inception in the third quarter of 2019, Statistics Botswana published the first QMTS (July-September 2019) Report in January 2020. This was followed by reports for the fourth quarter of 2019, first and fourth quarters of 2020, the fourth quarter of 2021, and the fourth quarter of 2022. However, the conduct of the rest of the quarterly surveys for 2020, 2021 and 2022 was hampered by the outbreak of COVID-19 and, subsequent movement restrictions to contain the pandemic, and financial constraints to conduct surveys resulting in data gaps.

8 Statistics Botswana did not conduct any Labour Force Survey in the fourth quarter of 2023.

Chart 3.9:Trends in selected Labour Force Indicators



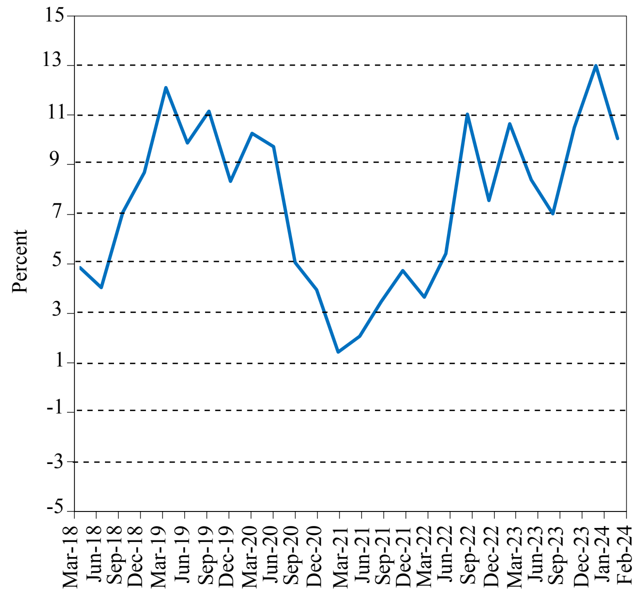
Source: Statistics Botswana

3.4 Monetary developments

Banking sector assets growth accelerated in February 2024

Annual banking sector assets' growth increased from 9.5 percent in February 2023 to 10.1 percent in February 2024 (Chart 3.10). The increase was mainly driven by gross loans and advances, BoBCs, balances at Bank of Botswana, fixed assets, as well as other assets. Loans and advances, which accounted for the largest proportion of commercial banks' assets (60.9 percent) in February 2024, increased by 8 percent, higher than the 6 percent increase in February 2023. Overall, growth in banking sector assets was mainly funded through customer deposits, which rose annually by 14.7 percent in the same period, associated with the repatriation of investment funds from offshore markets by pension funds.

Chart 3.10: Year-on-Year Commercial Banks' Growth in Total Assets

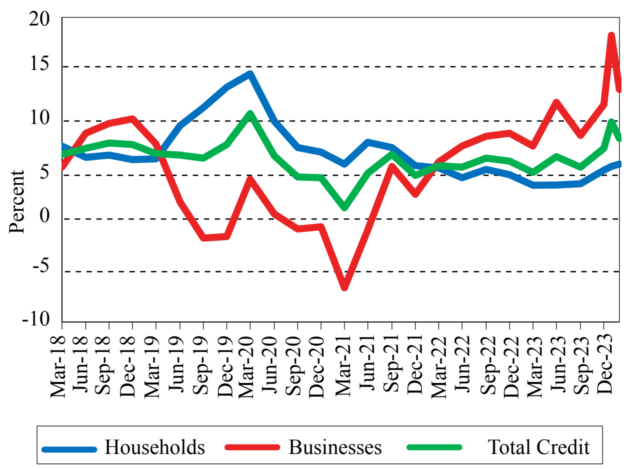


Source: Bank of Botswana

Credit growth accelerated in the year to February 2024

Commercial bank annual credit growth accelerated from 6 percent in February 2023 to 8 percent in February 2024 (Chart 3.11), associated with higher rate of expansion for lending to both the business and household sectors due to increased overdraft credit utilisation and revolving credit facilities, as well as acquisition of new loans.

Chart 3.11: Year-on-Year Commercial Banks' Growth in Total Credit



Source: Bank of Botswana

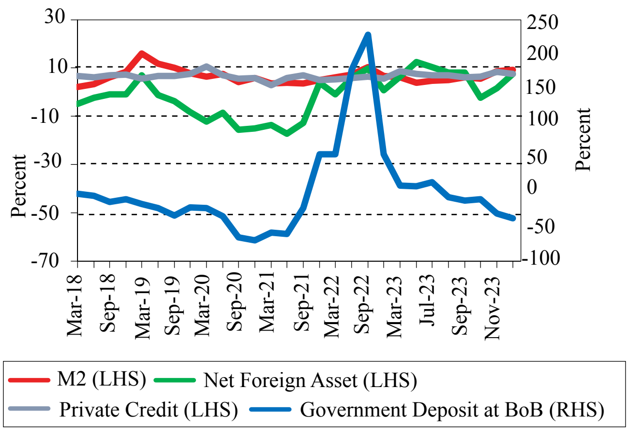
Lending to the business sector increased by 12.9 percent in the year to February 2024, higher than the 10.8 percent expansion in the corresponding period in 2023, reflecting an increased overdraft utilisation of credit facilities by some businesses. Credit to businesses excluding parastatals increased by 9.5 percent in the year to February 2024, lower than the 10.6 percent expansion in the corresponding period in 2023, mainly due to acquisition of new loans and increased usage of overdraft and revolving credit facilities by some companies in mining, transport and communications, construction, business services, as well as real estate. Meanwhile, credit to parastatals increased by 64.6 percent in the year to February 2024, compared to the 14.1 percent increase in the twelve months to February 2023, due to the utilisation of overdraft facilities.

On the other hand, year-on-year growth in household loans increased from 3.6 percent in February 2023 to 5.5 percent in February 2024. The higher growth in household credit was mainly attributable to the increase in lending for acquisition of property (contributing 2.3 percentage points) and motor vehicles (contributing 0.4 percentage points) during the period under review. Meanwhile, there was a decrease in the growth of unsecured personal loans and credit card-based loans during the period under review, a possible reflection of the effects of the policy tightening in 2022 by the Bank of Botswana, which had a dampening effect on demand for these products, which are generally pricey. Banks also likely restricted credit supply to guard against an increase in default rates as the cost of credit became expensive. The share of the household sector in total lending by commercial banks decreased from 66 percent in February 2023 to 64.5 percent in February 2024.

Money supply growth accelerated in December 2023

Money supply (M2) grew by an annual rate of 9.2 percent in December 2023, higher than the 6.8 percent in the corresponding period in 2022 (Chart 3.12). The acceleration in money supply expansion was mainly due to the increase in credit to the private and parastatals sectors to fund growth enhancing opportunities post COVID-19 restrictions. Moreover, there was a decrease in public sector deposits at the Bank of Botswana, which also had an expansionary effect on M2. Meanwhile, there was an offsetting impact from the increase in net foreign assets.

Chart 3.12: Year-on-Year Growth in Money Supply



Source: Bank of Botswana

The nominal BoBC yields decreased in the first quarter of 2024

The 7-day nominal BoBC yield (MoPR) decreased from an average of 2.65 percent in the first quarter of 2023 to an average of 2.40 percent in the first quarter of 2024, due to the 25-basis policy rate cut by the MPC in December 2023. In contrast, the real rate of interest for the 7-day paper increased from -6.20 percent to -1.12 percent in the same period, reflecting the significant decline in the inflation rate.

The stop-out yield on the 1-month BoBC, which was introduced in June 2022 to address some of the structural liquidity positions and support the construction of the short-end of the yield curve, averaged 2.60 percent in the first quarter of 2024, a decrease from an average of 2.94 percent in the corresponding period in 2023. However, the real rate of interest for the 1-month paper increased form an average of -5.93 percent to an average of -0.93 percent in the same period, reflecting the significant decline in the inflation rate.

S&P Global Ratings and Moody's affirm Botswana's sovereign credit rating and maintain a stable outlook

On 15 March 2024, S&P Global Ratings (S&P) affirmed Botswana's credit rating and maintained the stable economic outlook. S&P affirmed Botswana's sovereign credit rating for long-term foreign and domestic currency bonds at "BBB+", and "A-2" for short-term foreign and domestic currency bonds. The rating agency indicated that the affirmation of the ratings was underpinned by Botswana's strong institutional frameworks (compared with that of regional peers), continued prudent management of the domestic natural resource wealth, strong external balance sheet and low government debt burden, as well as a strong monetary policy framework. Meanwhile, a stable economic outlook was maintained on account of the expectation that the demand for Botswana's diamonds and economic growth will remain relatively resilient, thus supporting export receipts and fiscal revenue.

On 27 October 2023, Moody's Investors Service affirmed the Government of Botswana's long-term local and foreign currency issuer ratings at "A3" for 2023 and maintained a stable outlook. The ratings are underpinned by the country's very low debt levels, and its robust institutional frameworks and governance strength, balancing economic concentration in mining and related activities, as well as very low susceptibility to political, liquidity and banking-related event risks. The stable outlook owes to balanced risks premised on expectation that the demand for Botswana's diamond will remain strong despite a softened global outlook for diamond prices.

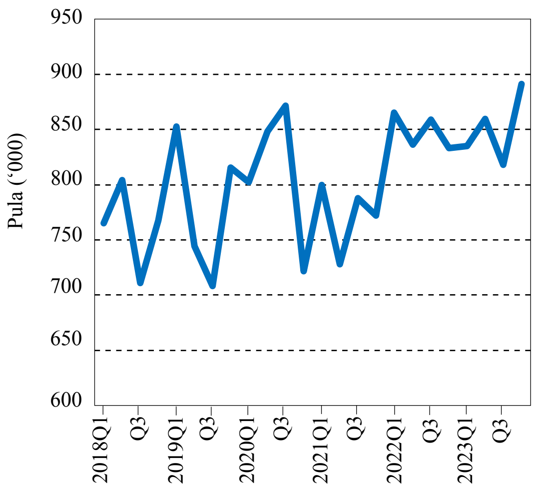
3.5 Asset market prices

Property market improved in the fourth quarter of 2023

According to the latest (2023Q4) Riberry Report[9], the residential rental market showed signs of improvement in the fourth quarter of 2023, compared to the third quarter, driven by good demand for rental and purchases of houses in prime locations, while their supply was limited. Conversely, middle-end houses to let experienced increased supply and weaker demand. Nonetheless, the rental market for low-end properties continued to have reasonable demand.

Meanwhile, there is an oversupply of upper-end properties, leading to a possible decrease in the rental prices of these houses. The average price for residential properties sold in the fourth quarter of 2023 was P891 184, a 9 percent increase, compared to the previous quarter (Chart 3.13), attributable to the increase in the number of high-valued properties traded in the quarter under review.

Chart 3.13: Riberry Average Prices



The demand for office space remains reasonable and improved slightly as Government took up some vacant properties. Even though slower, there has been continued reasonable office enquiries and/or uptake in the Central Business District, Showgrounds and Government Enclave. However, the merging of some parastatals is likely to curtail the growth in demand for office space by Government. In addition, there is limited construction of office space, which will most likely lead to excess demand for the same.

Similar to the previous quarter, the demand for retail space remained fair across all market segments, while the supply is expected to increase, as two malls are proposed for Mogoditshane. In addition, other centres with good demand for retail space are Jwaneng, Selibe-Phikwe, Maun (Mall of Maun under construction), Ramotswa, Molepolole and Mahalapye. Most of these locations have a few retail schemes, to be anchored by reputable supermarkets, at planning and/or construction stage.

Regarding industrial property, the supply of unoccupied big warehouse space has decreased, while the demand has improved.[10] Meanwhile, the demand for industrial space in prime locations is expected to improve going forward.

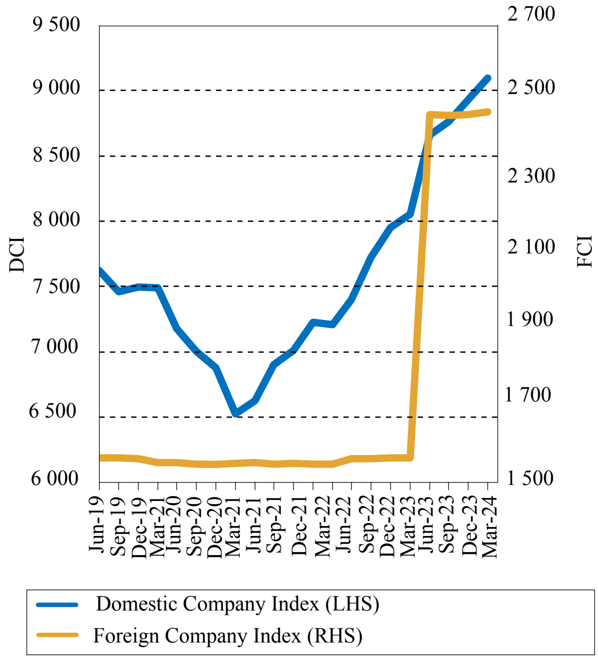
Stock market indices increased

The Domestic Companies Index (DCI) increased by 14.4 percent in the twelve months to March 2024, compared to an increase of 10.1 percent in the year to March 2023 (Chart 3.14). The increase was mainly due to the higher share prices for First National Bank of Botswana, Standard Chartered Bank and Chobe, which increased by 31.4 percent, 69 percent and 64.7 percent, respectively, in the same period. The higher share prices were because of increased trading activity and a significant increase in average daily turnover during March 2024, (led by FNBB, possibly reflecting the announcement of the increase in overall profit for 2023), with the institutional investors being the biggest contributors to equity turnover.

The Foreign Companies Index (FCI) increased by 58.1 percent in the year to March 2024, compared to an increase of 1 percent in the corresponding period in 2023 (Chart 3.14). The increase was largely due to the year-on-year increase in the share prices for New Gold Issuer (RF) Limited (14.4 percent) and CA Sales Holdings Limited (34.1 percent) because of increased trading activity (since August 2023) and a significant increase in average daily turnover during March 2024.

Of note, on 23 August 2023, the Botswana Stock Exchange recorded the highest turnover (P235.7 million) in a single day of trading during 2023, adding to a series of significant trade milestones in the recent past years.

Chart 3.14: Stock Market Indices



Source: Bank of Botswana

9 This is a quarterly report produced by independent valuers, Riberry Botswana (Pty) Ltd.

10 Investors prefer bigger warehouses, but available warehouse space is limited.

Box 1: Monetary Policy Implementation and Operations Framework

Open Market Operations remain the main liquidity management tool in the domestic market, as well as implementing decisions of the MPC. This entails the issuance of BoBCs to mop-up excess liquidity in order to maintain interest rates that are consistent with the monetary policy stance. Moreover, the Bank continuously evaluates its monetary policy implementation framework, aimed at strengthening the monetary policy transmission mechanism where necessary. In this respect, the Bank introduced reforms to the monetary policy operations in April 2022. These included, in the main, the discontinuation of the Bank Rate as the main anchor policy rate and the transition to the MoPR, which is an instrument-based policy rate (7-day BoBCs yield) for effective monetary policy transmission.

The transition also marked the introduction of an interest rate corridor with a 200-basis points width, comprising the Standing Deposit Facility (SDF) at 100 basis points below the MoPR and the Standing Credit Facility (SCF) at 100 basis points above the MoPR. The SDF and SCF serve as the floor and ceiling of the interest rate corridor, respectively, and commercial banks use both facilities at their own discretion for their daily liquidity management. The interest rate corridor helps to ensure that money market interest rates move within a reasonably close range around the MoPR, culminating into a symbiotic relationship between the policy rate and market interest rate, thus providing the fundamental basis for effective monetary policy transmission.

The monetary operations reforms are now embedded in the Bank's monetary policy operations. There has been some noticeable improvement in policy transmission, while the interest rate structure is operating as expected. The adoption of the MoPR as a reference rate has had an immediate impact on the shorter end of the yield curve i.e., overnight interbank rates, as was expected. The interest rate corridor plays a critical role of affording commercial banks an opportunity to manage their liquidity in between BoBC auctions. However, transmission or impact on the longer end is expected to be rather slower as there are other factors that come into play that may counter the expected impact of reforms, such as inflation expectations.

The reforms also allow for the conduct of fine-tuning operations (repos and reverse repos) which are done at the discretion of the Bank upon evaluation of the general market liquidity. If offered, the fine-tuning operations are conducted at the MoPR. Furthermore, a 1-month BoBC is issued for structural liquidity management and price discovery purposes, while the Prime Lending Rate (PLR) is determined by the individual commercial banks (effective 1 April 2023).

3.6 Balance of payments

Current account in deficit during the fourth quarter of 2023

The current account is estimated to have recorded a deficit of P10.1 billion in the fourth quarter of 2023, compared to a revised deficit of P3.3 billion in the corresponding period in 2022 (Chart 3.15). The larger deficit was mainly on account of merchandise trade deficit. Exports of goods declined by 43.8 percent, from P20.8 billion to P11.7 billion while imports of goods increased by 10.3 percent, from P21.4 billion to P23.6 billion, resulting in a trade deficit of P11.9 billion. The decrease in exports was primarily due to the poor diamond trade performance. The secondary income account, supported by SACU revenues, increased from P3.2 billion to P5.7 billion, helping to offset what would have otherwise been a larger current account deficit. SACU revenues increased from P3.4 billion in the fourth quarter of 2022 to P6 billion in the corresponding period in 2023 as a result of forecast error adjustments related to the 2021/22 financial year.[11]

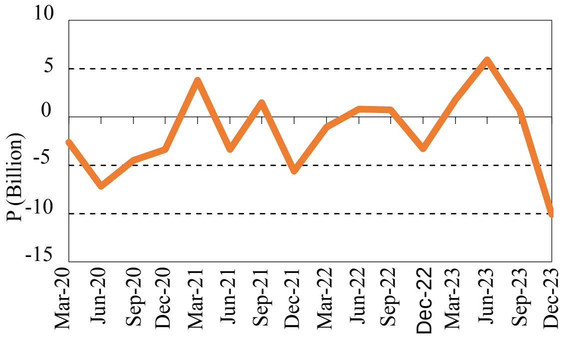
Diamond exports, which accounted for 62.4 percent of total exports of goods in the fourth quarter of 2023 (82.1 percent in the fourth quarter of 2022), decreased from P17.1 billion to P7.3 billion in the fourth quarter of 2022. During the same period, diamond imports increased from P4.3 billion to P4.7 billion. The decrease in diamond exports resulted from weakened global demand for rough diamonds induced by large inventories and plunging prices of polished diamond during the second half of 2023.

The other commodities that contributed to a decline in exports include live cattle (85.4 percent), vehicle and transport equipment (23.9 percent), coal (34.7 percent) and other goods (21.3 percent). However, other export commodities increased; copper (68.6 percent), meat and meat products (205.7 percent), iron and steel products (85.5 percent), salt and soda ash (8.9 percent) and machinery and electrical equipment (8.8 percent).

The increase in imports was driven by increases across most commodities: diamonds (8.3 percent), fuel (7.7 percent), food, beverages and tobacco (22.7 percent), chemicals and rubber products (10.6 percent), vehicles and transport (18.6 percent), machinery and electrical equipment (2.8 percent), textiles and footwear (10.4 percent), metals and metal products (15.5 percent), salt ores and related products (21.3 percent), furniture (8.6 percent) and wood and paper products (5.3 percent).

11 The 2002 SACU Agreement provides that adjustments in respect of the differences between the forecast and actual revenue collected in time (t) to be made in years (t+2) to adjust for forecast errors with a two-year lag. As a result, the projected 2023/24 SACU payments include the forecast error adjustment for 2021/22. The substantial increase in the payments resulted from higher-than-expected customs and excise tax collections during the financial year 2021/22.

Chart 3.15: Quarterly Current Account Balance



Source: Bank of Botswana

The current account deficit is estimated to have narrowed to P1.7 billion in 2023 from a revised P3 billion recorded in 2022 and this was on account of higher SACU receipts and reduced investment income payouts.

The financial account recorded a net inflow in the fourth quarter of 2023

The financial account is estimated to have recorded a net inflow of P682 million during the fourth quarter of 2023, compared to a net outflow of P2.5 billion recorded in the fourth quarter of 2022. The net inflow was attributable to an increase in foreign direct investment inflows during the last quarter of the year.

In 2023, the financial account recorded a net inflow of P4.1 billion mainly reflecting an increase in foreign direct investment inflows and withdrawal of deposits held in offshore banks by residents.

The BoP was in deficit in the fourth quarter of 2023

The overall BoP deficit worsened from P925 million recorded in the fourth quarter of 2022 to P3.4 billion during the same quarter in 2023. The deficit was attributable to the current account deficit.

The overall balance of payments was in a surplus of P1.7 billion in 2023, a decline from a surplus of P4.5 billion recorded in 2022.

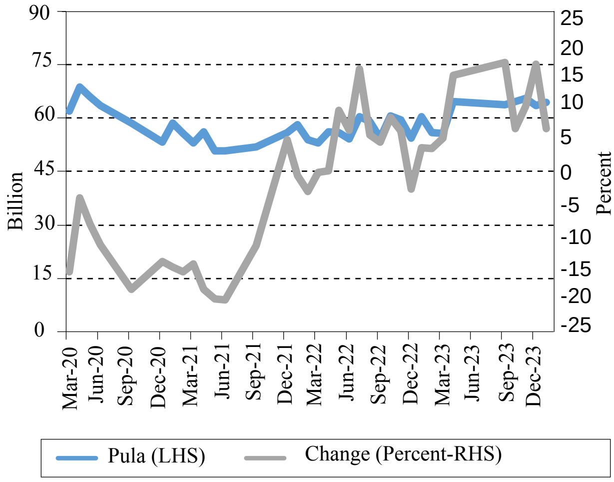
Foreign exchange reserves increased

As at the end of December 2023, foreign exchange reserves amounted to P63.7 billion, an increase of 16.9 percent from P54.5 billion in December 2022 (Chart 3.16).

In foreign currency terms, the level of foreign exchange reserves increased by 11.6 percent from USD4.3 billion in December 2022 to USD4.8 billion in December 2023 (Chart 3.17) and increased by 9.4 percent from SDR3.2 billion to SDR3.5 billion, during the same period. The estimated level of foreign exchange reserves in December 2023 was equivalent to 8.6 months of import cover of goods and services.

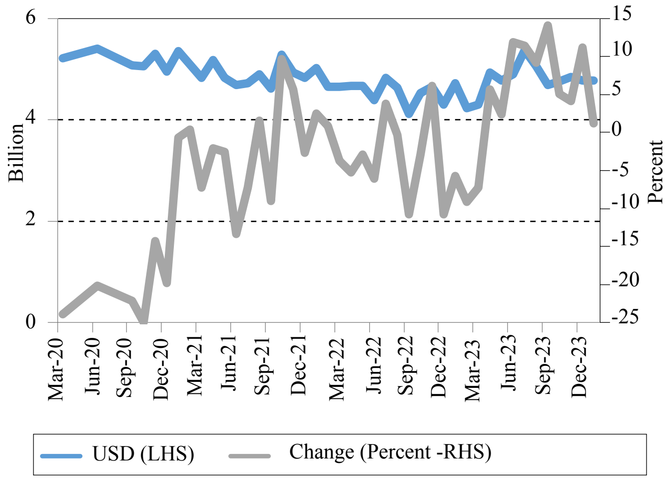
The foreign exchange reserves were estimated at P64.6 billion at the end of January 2024, an increase of 6.8 percent from P60.5 billion in January 2023. In foreign currency terms, the reserves are estimated to have increased by 2.1 percent from USD4.7 billion to USD4.8 billion and by 2.9 percent from SDR3.5 billion to SDR3.6 billion. The estimated level of reserves as at the end of January 2024 was equivalent to 8.7 months of import cover.

Chart 3.16: Foreign Exchange Reserves in Pula and Annual Percentage Change



Source: Bank of Botswana

Chart 3.17: Foreign Exchange Reserves in US Dollars and Annual Percentage Change



Source: Bank of Botswana

3.7 Exchange rate developments

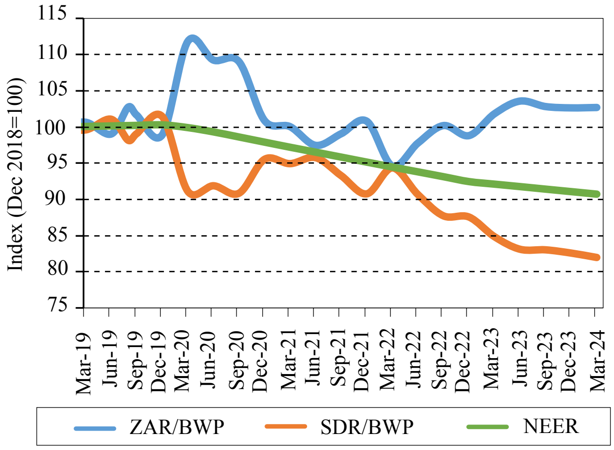
For 2024, the Bank's implementation of the exchange rate policy entails an annual downward rate of crawl of 1.51 percent. This downward rate of crawl was implemented effective 1 January 2024, with a view to enhancing domestic industry competitiveness. During the same period, the Pula basket weights were maintained at 45 percent for the South African rand and 55 percent for the SDR, guided by Botswana's trade pattern and international transactions. Box 2 explains the current exchange rate policy framework and the Pula exchange rate parameters for 2024, which were announced in December 2023.

In the twelve months to March 2024, the Pula appreciated by 0.8 percent against the South African rand and depreciated by 3.4 percent against the SDR (Chart 3.18). With respect to the SDR constituent currencies, the Pula depreciated by 6.8 percent against the British pound, 4.9 percent against the US dollar and 4.3 percent against the euro, while it appreciated by 8.3 percent against the Japanese yen and 0.4 percent against the Chinese renminbi.

The movement of the Pula against the SDR constituent currencies largely reflects the performance of the South African rand against the SDR constituent currencies. Therefore, in the same review period, the South African rand depreciated by 4.2 percent against the SDR. With respect to the SDR constituent currencies, the South African rand depreciated by 7.6 percent against the British pound, 5.7 percent against the US dollar, 5.1 percent against the euro and 0.5 percent against the Chinese renminbi, while it appreciated by 7.4 percent against the Japanese yen.

The South African rand continued to weaken as both the 2024 State of the Nation Address (SONA) and budget speech failed to convince investors that the country was on track to turn around its subdued growth prospects. During the SONA, the President failed to announce a clear plan that will address the country's major challenges, such as inconsistent electricity supply and congestion at the seaports, which continue to delay the delivery of significant inputs of production. Moreover, the Finance Minister announced that the Government will draw down 150 billion rands ($7.8 billion) from the gold and foreign exchange contingency reserve account at the central bank over the next three years to limit rising debt. He, however, did not provide details on the wider macroeconomic structural reforms to address problems, such as high unemployment and stagnant economic growth. Meanwhile, the political risk, ahead of South Africa's upcoming election in May 2024, is keeping investors cautious, thus weighing on the demand for the South African rand.

Chart 3.18: Nominal Exchange Rate Indices

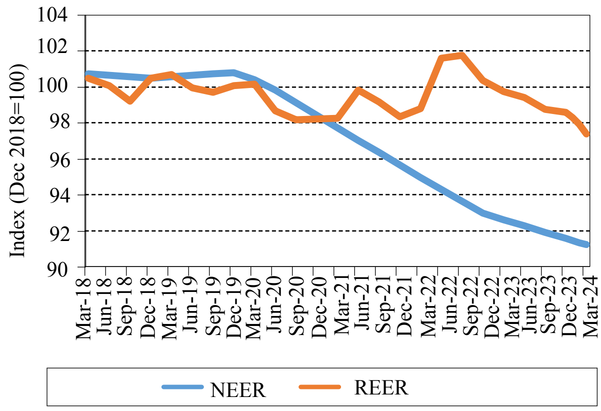


Source: Bank of Botswana

NEER depreciated in March 2024

The NEER of the Pula depreciated by 1.5 percent in the twelve months to March 2024 (Chart 3.19), consistent an annual downward rate of crawl of 1.51 percent implemented effective January 2024.

Chart 3.19: Nominal and Real Effective Exchange rates



Source: Bank of Botswana

REER depreciated in March 2024

The REER depreciated by 2.4 percent in the twelve months to March 2024 (Chart 3.19), due to depreciation of the NEER (rate of crawl) and lower inflation in Botswana than in trading partner countries, suggesting a marginal gain in Botswana's export competitiveness.

With respect to bilateral movements against the Pula basket currencies, the real Pula exchange rate (using headline inflation) depreciated by 3.1 percent and 1.4 percent against the SDR and the South African rand, respectively. It depreciated by 7 percent against the British pound, 5.4 percent against the US dollar and 3.8 percent against the euro, while it appreciated by 8.5 percent against the Japanese yen and 3.2 percent against the Chinese renminbi.

Box 2: The Pula Exchange Rate Framework Explained

Definition of Exchange Rate

The exchange rate of a currency is how much one currency can be bought for each unit of another currency or, put differently, the rate at which domestic currency can be converted into a foreign currency or vice versa.

Exchange Rate Policy Frameworks

The exchange rate policy framework refers to the way a country manages its own currency in relation to foreign currencies and the foreign exchange market.

Exchange rate policy frameworks range from flexible to fixed, with variations in between. In a flexible exchange rate framework, the exchange rate is freely determined by the market on the basis of demand and sentiments about the economy. In a fixed exchange rate regime, the domestic currency is linked to another currency or a basket (combination) of other currencies. In between flexible and fixed exchange rates, there is a range of, usually managed exchange rate frameworks, such as a crawling band or peg.

Botswana's Exchange Rate Policy Framework

Since 2005, Botswana adopted and implemented a crawling peg exchange rate policy framework that has three key attributes.

First, the Pula is fixed to a basket of foreign currencies, namely the SDR and the South African rand. The SDR comprises the US dollar, British pound, euro, Japanese yen and Chinese renminbi.

Second, is the weight of these currencies in the Pula basket (proportions that each of these currencies contribute to the value of the Pula). Currently, the Pula exchange rate is constituted by 55 percent SDR and 45 percent South African rand.

Third, is the annual rate of crawl, which is the amount (rate) by which the exchange rate is allowed to gradually depreciate or appreciate. This amount reflects the projected inflation differential between Botswana and its trading partner countries. For example, the 1.51 percent downward rate of crawl for 2023 was as a result of a determination that inflation in Botswana would be, on average, 1.51 percentage points higher than in the trading partner countries.

Botswana's Exchange Rate Policy Objective

The policy objective is to maintain price competitiveness of local producers for similar products, in both the domestic and international markets by equalising the exchange rate-adjusted prices. In general, this is done through adjusting the nominal Pula exchange rate by an amount that is equal to the differences in projected inflation between Botswana and the trading partner countries. That is, **the rate of crawl**.

For example, if a bag of potatoes is currently P100 in Botswana and R130 in South Africa, at an exchange rate of P1 = R1.30, and assuming transport costs are not embedded in the pricing, Botswana's producers face similar market price as South African producers and, therefore, competitive. If, however, inflation in Botswana rises to be 5 percentage points higher than in South Africa, Botswana producers will be disadvantaged as it would be cheaper to purchase the same bag of potatoes in South Africa, holding all other things constant. Therefore, the Pula exchange rate needs to adjust downward by 5 percent **(rate of crawl)** to maintain competitiveness of producers in Botswana; technically, maintenance of a stable REER.

The exchange rate and competitiveness also have to relate to countries that Botswana trades with, in terms of goods and services, but also the flow of investments. It has been determined that these are mostly South Africa and the SDR countries (the USA, UK, euro area, China and Japan). This explains the fixing of the Pula to currencies of these countries. The 45 percent South African rand and 55 percent SDR proportions are based on observed historical trade pattern and are also subject to semi-annual review. In addition, the fixing to a basket rather than a single currency helps to moderate volatility of the Pula against any single currency. This explains why during the times when the South African rand and other currencies are volatile, the Pula remains relatively stable.

2024 Pula Exchange Rate Parameters

In the context of Botswana's crawling band exchange rate arrangement for the Pula, the Ministry of Finance in conjunction with the Bank of Botswana, reviews the parameters for the Pula exchange rate twice in a year; being the currencies in the Pula basket and their weights, as well as the rate of crawl. This is done to assess alignment of

Source: Bank of Botswana

the Pula exchange rate with the policy objective of maintaining a stable and competitive REER of the Pula; that is, retaining competitiveness of Botswana producers against imports and exports in international markets.

For 2024, it was determined that inflation in Botswana would be on average higher than in the trading partner countries, suggesting maintenance of an annual downward rate of crawl of 1.51 percent, which would be implemented through small daily adjustments that would equal 1.51 percent over twelve months. This annual downward rate of crawl was implemented effective 1 January 2024, with a view to enhancing domestic industry competitiveness. It was also determined that the trade patterns remain largely unchanged and, therefore, the Pula Basket weights were also maintained at 55 percent SDR and 45 percent South African rand.

The Benefits of the Crawling Band Framework for Botswana

The benefits of the current crawling band framework are therefore as follows:

(a) it affords flexibility for adjustments to address deterioration in international price competitiveness of the domestic industry;
(b) any adjustment is gradual and, therefore, not disruptive nor destabilising;
(c) the rate of adjustment is preannounced and, therefore, enables planning for economic decisions;
(d) the framework is broadly in alignment with the price stability objective (inflation objective inherent in the monetary policy framework; and
(e) and the basket composition moderates fluctuations of the Pula exchange rate against any individual currency.

In contrast, alternative arrangements could have disadvantages as follows:

(a) with a small undiversified economy such as Botswana with irregular and lumpy foreign exchange flows, a floating exchange rate regime would imply large exchange rate fluctuations that could be debilitating to price determination and economic activity. In addition, there could be sustained movement of the exchange rate, especially appreciation, that can undermine competitiveness of the non-mining sector and, therefore, diversification efforts;
(b) as demonstrated in the past, a fixed hard peg would often require adjustments that are large and discrete with a destabilising disruptive impact. For example, a large devaluation with significant inflationary impact; and
(c) a peg to a single currency would imply the Pula being subject to fluctuations and shocks to the currency to which it is pegged and, in turn, policy responses that may be inimical or inconsistent with the needs of the domestic economy at the time.

Limits of Exchange Rate Adjustments on Industry Competitiveness

While there are short-term benefits of deliberate exchange rate adjustments to maintain price competitiveness, for it to have the desired long-term impact, there should be adequate production capacity and productivity improvements by the domestic industry. In addition, for government institutions, there should be effective implementation of plans and programmes. Overall, therefore, there is need for generalised entrenchment and traction of structural transformation and policy reforms as being fundamental to industrialisation and productivity improvements that would enhance competitiveness of domestic producers in a low inflation environment.

It is recognised that, in the main, sustained (need for) downward adjustment of the currency is a reflection of weak production capacity and productivity of the economy; and is also inflationary (ultimately affecting price competitiveness).

Transparency and Market Information

The announcements of the Pula exchange rate parameters and any adjustments are intended to enhance transparency and integrity of the framework. In this regard, knowledge of the Pula basket weights, and rate of crawl enable the market and the general public to plan for investments and transactions on the basis of publicly available information that can be used as an input to any economic decisions.

Box 3: Bank of Botswana (Amendment) Act, 2022

In July 2022, Parliament passed the Bank of Botswana (Amendment) Act, 2022 (the Act), which introduces new provisions to enhance the Bank's powers to achieve the price and financial stability mandates. The Act commenced on 14 February 2023. The new changes are discussed below.

Dual Mandate for the Bank of Botswana

Section 4 (2) of the Act incorporates a financial stability mandate for the Bank in addition to the primary mandate of maintaining price stability. Under the new legislation, the primary objective of the Bank shall be to achieve and maintain domestic price stability. Subject to attaining its primary mandate, the Bank shall contribute to the stability of the financial system and foster and maintain a stable, sound and competitive market-based financial system. In addition to making explicit the twin-mandates of the Bank, the provision further endows the Bank with operational independence in pursuit of its primary objectives, and in the performance of its functions under the Act.

Revised Composition of the Monetary Policy Committee

One of the major changes in the Act is the establishment of a statutory Monetary Policy Committee (MPC) under Section 19 A of the Act. The MPC shall be composed of 9 members, being the Bank of Botswana Governor, deputy Governors, head of department responsible for economic research and head of department responsible for treasury operations and 4 external members, with relevant skills and knowledge on the functions of the MPC, appointed by the Minister of Finance. Two external members were appointed on April 1, 2023, and the third on August 1, 2023, while the fourth was appointed on September 1, 2023.

Establishment of a Statutory Financial Stability Council

Section 54 B of the amended Act establishes Financial Stability Council (FSC), which shall be responsible for preserving the stability of the financial system; ensuring cooperation between members with respect to the assessment of the build-up of economic and financial sector systemic risks in Botswana; developing coordinated policy responses to risks including crisis management; and making recommendations, issuing warnings or opinions addressed to regulatory bodies regarding financial institutions. The FSC shall comprise the Governor, who shall be the Chairman, the Permanent secretary in the Ministry responsible for Finance, Chief Executive Officer of the Non-Bank Financial Institutions Regulatory Authority, Director of the newly established Deposit Insurance Scheme for Botswana, and the Director General of the Financial Intelligence Agency. The FSC was previously established through a memorandum of understanding between participating institutions.

Provision for the Establishment of a Deposit Insurance Scheme

Section 43 A of the amended Act provides for the establishment of a Deposit Insurance Scheme to provide insurance against loss of part or all insured customer deposits in a bank. The Deposit Insurance Scheme shall be established and operate in a manner that will contribute to the stability of the financial system in Botswana and minimise exposure to loss for customers.

4. THE ECONOMIC AND POLICY OUTLOOK

4.1 Global economic prospects

The global economic outlook remains broadly restrained, although the 2024 growth forecast is revised slightly upwards in the April 2024 WEO compared to the January 2024 projection. The upward revision was largely due to stronger-than-earlier forecast performance for the US and some large emerging market economies. Nonetheless, the restrained outlook is on account of lower consumer demand associated with higher borrowing costs resulting from monetary policy tightening implemented in 2023, withdrawal of fiscal support amid high debt, the geopolitical tensions, low underlying productivity growth and extreme weather conditions. Regionally, in South Africa, growth prospects remain restrained on account of tight credit conditions and structural bottlenecks in the economy. With regard to price developments, global inflation is projected to moderate further, due to anticipated decrease in food prices, the impact of monetary policy tightening in 2023, as well as squeezing of household budgets.

Global economic growth to remain restrained

According to the April 2024 WEO, global output growth is forecast at 3.2 percent for both 2024 and 2025, the same as in 2023. The growth forecast for 2024 was revised slightly upwards by 0.1 percentage points, compared to the January 2024 projection. Meanwhile, the 2024-2025 forecasts are lower than the historical (2000-2019) annual average of 3.8 percent. The anticipated restrained growth is on account of higher borrowing costs resulting from monetary policy tightening in 2023, withdrawal of fiscal support amid high debt, geopolitical tensions, extreme weather conditions, as well as low underlying productivity growth.

For advanced economies, output growth is projected to rise slightly from 1.6 percent in 2023 to 1.7 percent in 2024, and to accelerate further to 1.8 percent in 2025. The 2024 growth forecast is 0.2 percentage points higher than the January 2024 projections, reflecting mainly the upward revision in growth for the US.

Risks to the global economic outlook are assessed to be broadly balanced. Upside risks include possibility of stronger than expected global growth that could arise from lower inflation, slower than assumed withdrawal of fiscal support, stronger structural reform momentum and faster economic recovery in China. On the downside, new commodity price spikes from geopolitical shocks including those from the Russia-Ukraine war and the conflict in Gaza and Israel, as well as supply disruptions or more persistent underlying inflation could prolong tight monetary conditions. Moreover, the possibility of systemic debt distress in emerging market countries due to a combination of higher borrowing costs and weaker growth could result in lower growth. A divergence in disinflation speeds among major economies could also cause currency movements that put financial sectors under pressure.

UK economic growth to remain subdued

The UK economy is forecast to grow by 0.5 percent in 2024, from an estimated expansion of 0.1 percent in 2023, against the backdrop of easing inflationary pressures as the lagged negative effects of high energy prices wane and anticipated lower interest rates. Growth projection remains restrained, and the 2024 projection is 0.1 percentage points lower than in the January 2024 WEO Update.

Output growth for US to increase

For the US, output is forecast to grow by 2.7 percent in 2024, higher than an estimated expansion of 2.5 percent in 2023. The 2024 projection is 0.6 percentage points higher compared to the January 2024 forecast, on account of stronger than earlier anticipated growth in the fourth quarter of 2023, which is expected to persist into 2024. Meanwhile, output growth is forecast to moderate to 1.9 percent in 2025 as gradual fiscal tightening and softening labour markets slow aggregate demand.

Growth for the euro area to increase

In the euro area, economic growth is projected to increase to 0.8 percent in 2024 (0.1 percentage points lower compared to the January 2024 forecast), from an expansion of 0.4 percent in 2023, resulting from improved domestic demand as consumers start to recover purchasing power amid lower commodity prices, as the effect of the Russia-Ukraine war to energy prices subside and the fall in inflation supports growth of real income. Meanwhile, GDP growth for the region is expected to improve to 1.5 percent in 2025 (0.2 percentage points lower than the forecast made in January 2024).

Emerging markets GDP growth to decrease

Growth in economic activity in emerging market and developing economies is projected to expand by 4.2 percent in 2024 and 2025, slightly lower than an estimated expansion of 4.3 percent in 2023, due to subdued performance in China amid persistent property market crisis. However, the forecast for 2024 was revised slightly upwards by 0.1 percentage points due to an upgrade of growth for India resulting from resilience in domestic demand.

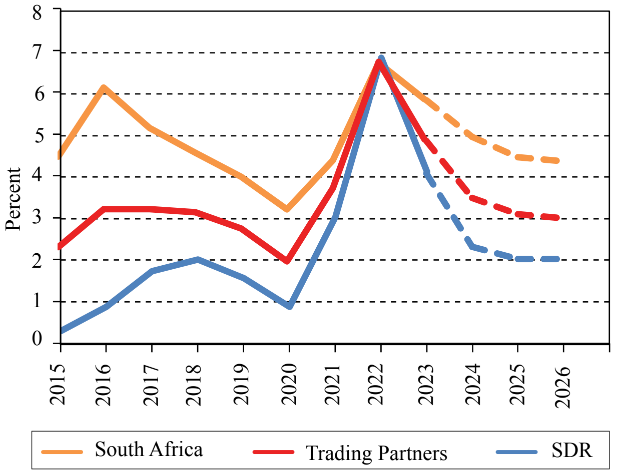
In India, growth is expected to expand by 6.8 percent and 6.5 percent in 2024 and 2025, respectively, compared to 7.8 percent in 2023. The growth forecast for 2024 is an upward revision of 0.3 percentage points from the January 2024 forecast, reflecting stronger-than-expected growth in the second half of 2023, as a result of stronger domestic consumption and investment. Meanwhile, output for China is forecast to grow by 4.6 percent and 4.1 percent in 2024 and 2025, respectively, lower than the estimated expansion of 5.2 percent in 2023, as weaker private investment and property market crisis continue to negatively affect the economy. The growth forecasts for 2024 and 2025 are unrevised from the January 2024 projections.

Growth prospects for the South African economy remain weak

Regionally, growth prospects in South Africa are expected to remain restrained on account of carryover effects of tight monetary policy conditions to control inflationary pressures in 2023, restrained fiscal support, ports and rail logistical constraints, power outages, as well as the grey listing of the economy by the Financial Action Task Force in February 2023. Thus, South African output growth is forecast to remain subdued at 0.9 percent in 2024, from 0.6 percent in 2023, and to increase to 1.2 percent in 2025. Meanwhile, projections for 2024 and 2025 are both 0.1 percentage points lower than in the January 2024 WEO Update.

Meanwhile, in March 2024, the SARB maintained the forecast for GDP growth for 2024 at 1.2 percent but revised slightly upwards the projection for 2025, from 1.3 percent to 1.4 percent. The subdued growth prospects are mostly due to energy and logistical constraints, which continue to weigh on South African economic activity.

Chart 4.1: South Africa and SDR Headline Inflation



Source: SARB and Bloomberg

Global inflation to moderate

Globally, inflation is expected to moderate further in 2024, supported by lagged effects of monetary policy tightening in 2023 on consumption and investment, squeezing of household budgets, softening labour markets, as well as anticipated lower food prices. Thus, inflation for advanced economies is forecast to ease from 4.6 percent in 2023 to 2.6 percent in 2024, while for emerging market economies, it is forecast to remain unchanged at 8.3 percent in the same period. Overall, global inflation is expected to ease from 6.8 percent in 2023 to 5.9 percent in 2024, and further moderate to 4.5 percent in 2025.

Meanwhile, the SARB forecasts South African inflation to average 5.1 percent and 4.6 percent in 2024 and 2025, respectively. The forecast for 2024 is 0.1 percentage points higher than the January projection, while it is unchanged at 4.6 percent for 2025. Overall, headline inflation reverted to within the SARB's 3 – 6 percent target range in June 2023 and is expected to remain within the target range, albeit higher than the mid-point, before sustainably reverting to the mid-point of the target range in 2025 (Chart 4.1).

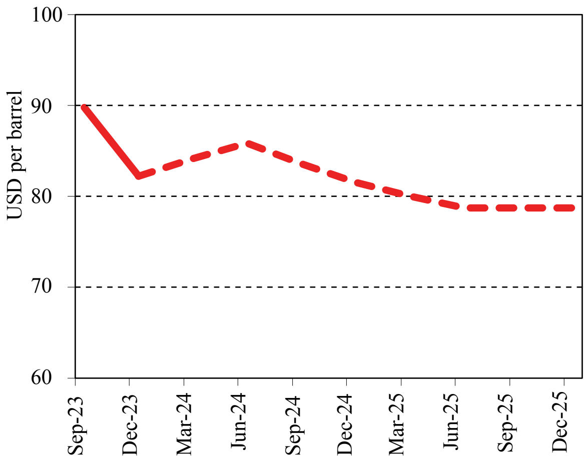
Diamond prices to trend downwards

Diamond prices are expected to continue trending downwards in the short term due to the anticipated slowdown in economic activity in major consuming countries, particularly China and India, as well as decreased demand for the commodity, amid uncertainty in major consuming markets underpinned by tight monetary policy, which has squeezed consumer budgets.

International oil prices to increase modestly in the second quarter and decline thereafter

International oil prices are projected to increase modestly in the second quarter of 2024 and to decrease thereafter (Chart 4.2). The projected increase in oil prices in the first quarter is on account of OPEC and its allies' agreement to cut production by around 2 million barrels per day until mid-2024, as well as Saudi Arabia and Russia's decision to voluntarily increase their production cuts by an extra 1.471 million barrels per day effective April 2024. Moreover, fears of supply and logistical challenges emanating from the attacks on commercial oil shipping vessels by the Houthi rebels in the Red Sea as a result of the escalation of the Israel-Hamas war is expected to exert upward pressure on international oil prices in the short term. However, weak global economic activity, the increase in oil supply, particularly in the US and Brazil, as well as weak industrial demand for oil in China are expected to weigh on oil prices, thus leading to the decrease in oil prices in the third quarter of 2024 going forward.

Chart 4.2: International Oil Prices



Source: Bloomberg

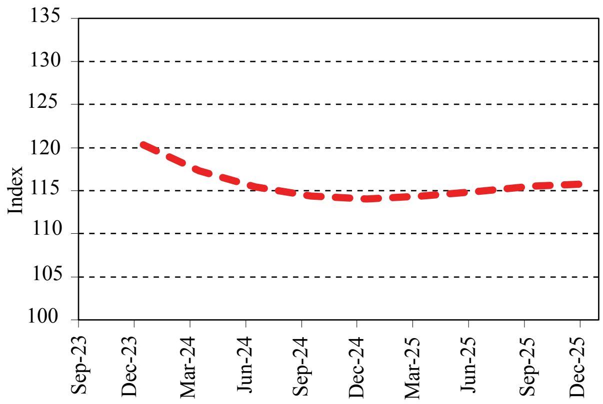
Overall, there is potential marginal upward pressure from international oil prices on domestic inflation in the short term, but thereafter, the forecast implies downward pressure on domestic oil prices.

International food prices to decrease

Global food prices are expected to trend downwards in the short term (Chart 4.3). The anticipated decrease in international food prices is driven by larger-than-expected seasonal harvests from leading food producers, such as Brazil, the US and Argentina. However, this may be partially offset by the termination of the Black Sea Grain Initiative and the ongoing strikes on Black Sea ports.

Chart 4.3: International Food Prices

FAO Index



Source: Bloomberg
Note: Approximated using forecasts for international

In Southern Africa, food prices are expected to remain elevated in the short term, compared to pre-pandemic levels, due to low rainfall experienced at the start of the 2023/24 ploughing season. Furthermore, the El Nino condition could result in another drought year, thus exerting an upward pressure on food prices. Most countries in the region are experiencing long dry spells, with Zambia having declared a national emergency due to drought. Botswana is also experiencing a severe drought. Overall, there is potential marginal downward pressure from international food prices on domestic inflation in the short term.

4.2 Outlook for domestic economic activity

According to the Ministry of Finance, GDP is expected to grow by 4.2 percent in 2024, from 2.7 percent in 2023. This growth will be supported by the prevailing accommodative monetary conditions; improvements in some non-mining sectors, such as water and electricity and finance, insurance and pension funds; reforms to further improve the business environment; and the expansionary fiscal policy, among others. However, output in the non-mining sector is anticipated to be below its potential in the short term.

Output growth to increase in 2024

The Ministry of Finance forecasts GDP to grow by 4.2 percent in 2024, from an expansion of 2.7 percent in 2023. Growth in 2024 is attributable to the anticipated improvement of the non-mining sectors, underpinned by, among others, improvements in electricity and water supply, as well as finance, insurance and pension funds sectors. It is also anticipated that effective implementation of the economic transformation reforms [12] and stimulative government expenditure indicated in the 2024/25 Budget, alongside the April 2023 – March 2025 Transitional National Development Plan (TNDP) would be supportive of economic activity, through facilitating expansion of productive capacity, accelerating economic transformation and enhancing economic resilience. Monetary policy also remains largely accommodative, given the projections for inflation remaining within the objective, therefore, conducive for financing of economic activity facilitated by economic transformation and policy reforms. However, given the downside risks to global economic activity, including weaker global demand and adverse impact of the Russia-Ukraine war, the growth trajectory remains uncertain.

The Bank's March 2024 Business Expectations Survey (BES) indicates that firms were less optimistic about business conditions in the first quarter of 2024, compared to the fourth quarter of 2023. The reduced level of optimism in the first quarter is reflected by the anticipated deceleration in exports and imports of goods and services; production; inventories; profitability; and investment in buildings, as well as plant and machinery, mainly due to the weaker global demand and adverse impact of the Russia-Ukraine and Israel-Hamas wars. Firms expect GDP to expand by 3.2 percent and 3.4 percent in the first and second quarters of 2024. Meanwhile, the below trend output in the short term is consistent with the high unemployment rate (25.9 percent as at the third quarter of 2023) and restrained growth in real wages.

12 These include, among others, tax reforms, such as implementation of Electronic Invoicing (E-Billing) for efficient VAT collection by Botswana Unified Revenue Service.

4.3 Monetary Policy and Inflation Outlook

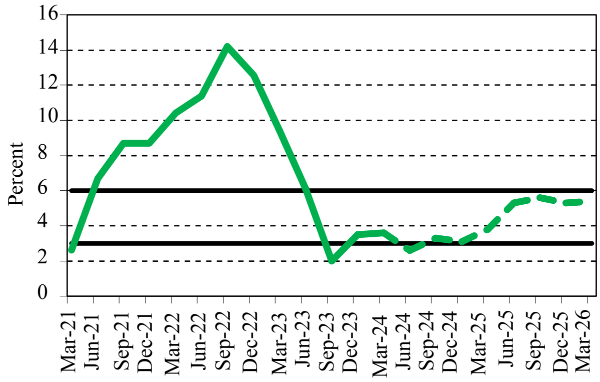
Inflation is forecast to temporarily breach the lower bound of the 3 – 6 percent objective range in the second quarter of 2024, but to revert to within the objective range on a sustained basis from the third quarter of 2024. The inflation forecast has been revised downwards in the short term compared to the February 2024 forecast.

Inflation is projected to breach the lower bound of the objective range temporarily in the second quarter of 2024

Inflation is expected to temporarily breach the lower bound of the objective range in the second quarter of 2024. The temporary breach is mainly due to the base effects associated with the reversal of VAT to 14 percent from 12 percent in April 2023 and the restrained growth in the domestic prices of most categories of goods and services. Nonetheless, inflation is expected to revert to within the objective range on a sustained basis from the third quarter of 2024 (Chart 4.4).

The projection takes into account the anticipated increase in domestic fuel prices based on the slate receivable from Botswana Energy Regulatory Authority (BERA), which recorded overall under recoveries in March 2024, as well as the possible increase in electricity tariffs by Botswana Power Cooperation, both expected to occur in the second quarter of 2024.

Chart 4.4: Botswana Headline Inflation Forecast

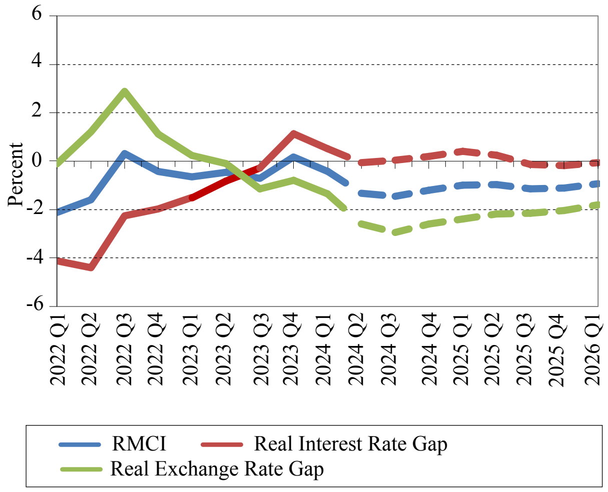


Source: Bank of Botswana

The projection also considers the anticipated growth in domestic output in response to the generally prevailing accommodative monetary conditions (Chart 4.5) and the implementation of an expansionary government budget for the 2024/25 fiscal year; the expected appreciation of the Pula against the South African rand; the developments in international commodity prices; and the base effects associated with adjustments in administered prices in 2023.

Meanwhile, the April 2024 inflation projection for 2024 (3.2 percent) is lower than expectations in the March 2024 BES, where the business community expect inflation (on average) to be 4.9 percent.

Chart 4.5: Real Monetary Conditions

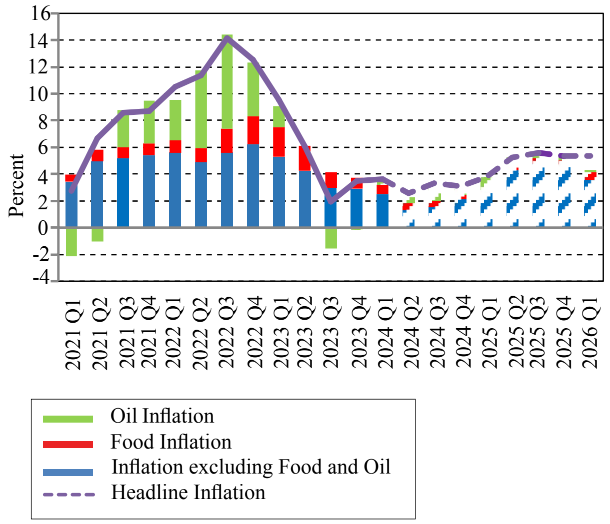


Source: Bank of Botswana

Core inflation to increase in the medium term

Inflation, excluding food and fuel prices, is forecast to increase in the medium term, on account of the expected second-round effects from the potential increase in domestic fuel prices and expected improvement in non-mining economic activity (Chart 4.6).

Chart 4.6: Headline Inflation and its Components



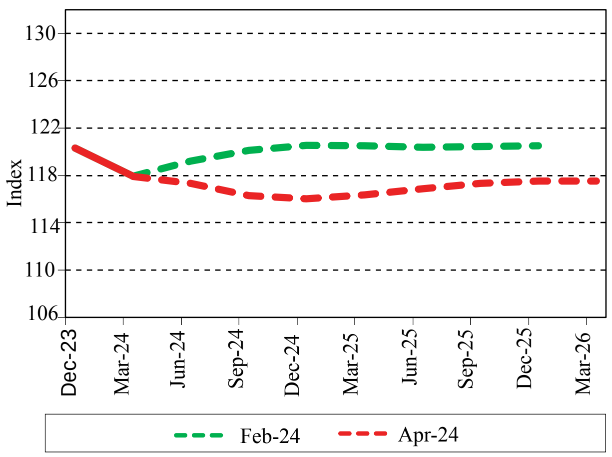
Source: Bank of Botswana

Forecasts for international food prices revised downwards

Compared to the February 2024 forecast, forecasts for international food prices have been revised downwards (Chart 4.7). The downward revision is mainly due to the larger-than-expected seasonal harvests from leading food producers, such as Brazil, the US and Argentina, as well as the notable increase in global cereal production from 2023 to date.

In Southern Africa, food prices are expected to increase due to anticipated decline in food production during the 2023/24 ploughing season in part due to El Niño weather phenomenon, which has resulted in below-average rainfall and drought conditions in the region.

Chart 4.7: International Food Prices
FAO Index



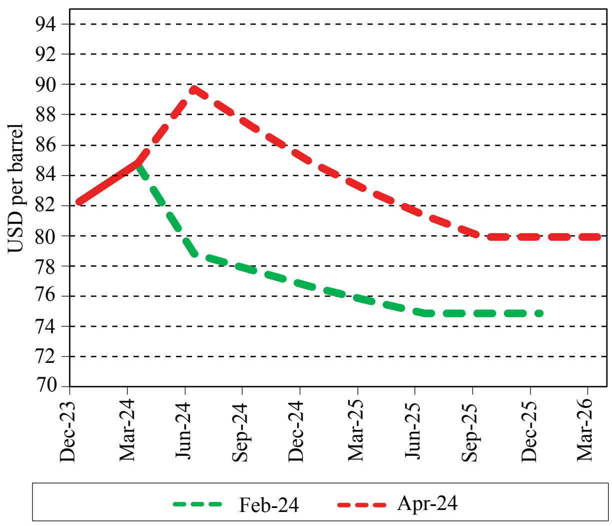
Source: Bloomberg

Forecasts for international oil prices revised upwards

Relative to the February 2024 projection, forecasts for international oil prices have been revised upwards (Chart 4.8), mainly due to the decision by OPEC and its allies to cut production, with Saudi Arabia and Russia volunteering for additional production cuts; the escalating war between Russia and Ukraine, which threatens supply and potential declines in worldwide oil stockpiles in 2024; and the concern regarding supply and logistical challenges arising from the Houthi rebels' attacks on commercial oil shipping vessels in the Red Sea due to the escalation of the Israel-Hamas war.

Although forecast to rise in the short term, international oil prices are expected to trend downwards from the third quarter of 2024 due to a weak global demand outlook emanating from efforts to combat heightened inflation through tight monetary policies and weak industrial demand for oil in China.

Chart 4.8: International Oil Prices



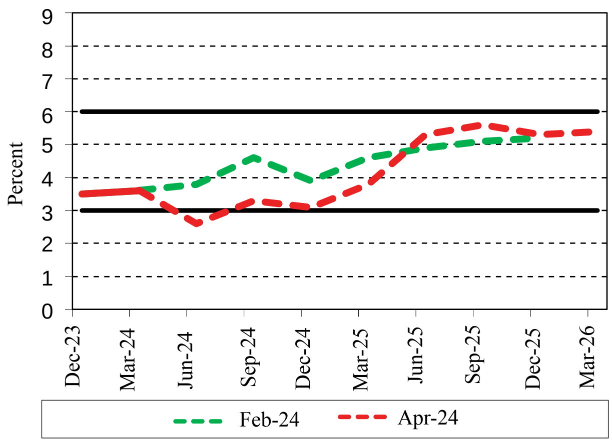
Source: Bloomberg

Overall, developments with respect to international food prices imply downward pressures on domestic inflation into the medium term, while international oil prices imply upward pressure on domestic inflation in the short term.

Inflation forecast revised downwards in the short term

Compared to the February 2024 forecast, the domestic inflation projection has been revised downwards in the short term and upwards in the medium term (Chart 4.9). The downward revision is mainly due to base effects associated with reversion of VAT from 12 percent to 14 percent in April 2023, the restrained growth in the domestic prices of most categories of goods and services compared to the recent past and the downward revision in forecasts for international food prices into the medium. The anticipated upward adjustments in domestic fuel prices in April 2024 and the possible increase in electricity tariffs in May 2024 are expected to partially offset the fall in inflation and are estimated to add approximately 0.48 percentage points and 0.14 percentage points, respectively to inflation in the second quarter of 2024. Meanwhile, the higher inflation in the medium term is mainly attributable to base effects and the expected improvement in non-mining output.

Chart 4.9: Botswana Headline Inflation - Revision



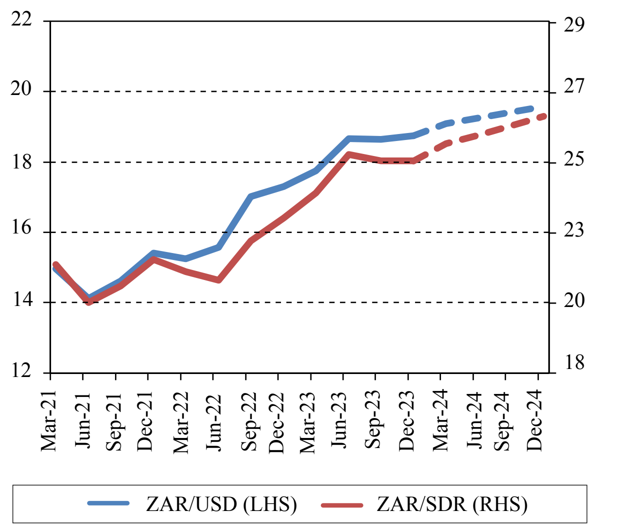
Source: Bank of Botswana

Exchange rate movements

The Pula exchange rate is determined by the performance of the Pula basket currencies and the rate of crawl. Once the basket composition and the rate of crawl (based on inflation differentials) have been determined, the daily changes in the value of the Pula against other currencies are a result of movements in the cross rates of the South African rand and the SDR constituent currencies against each other, and their relative weights in the composite currency basket.

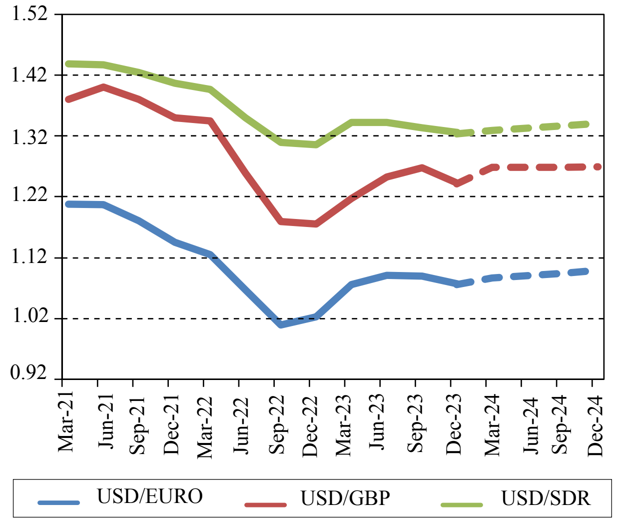
The South African rand is expected to depreciate against the US dollar and the SDR into the medium term (Chart 4.10). The general elections due in May 2024 are among key risks facing the South African economy as suggestions indicate that the ruling African National Congress could lose its absolute majority for the first time since coming into power, which has resulted in uncertainty in the outlook of the South African rand and is expected to weigh heavily on investor sentiments. In addition, South Africa faces idiosyncratic risks, including the electricity crisis – the country has been subjected to power outages and logistics bottlenecks stemming from problems at its seaports and railway lines, as well as the poorly performing highly indebted state-owned enterprises (SOEs), despite the announced possible tax increases and cuts in public expenditure through SOE mergers.

Chart 4.10: ZAR against USD and SDR



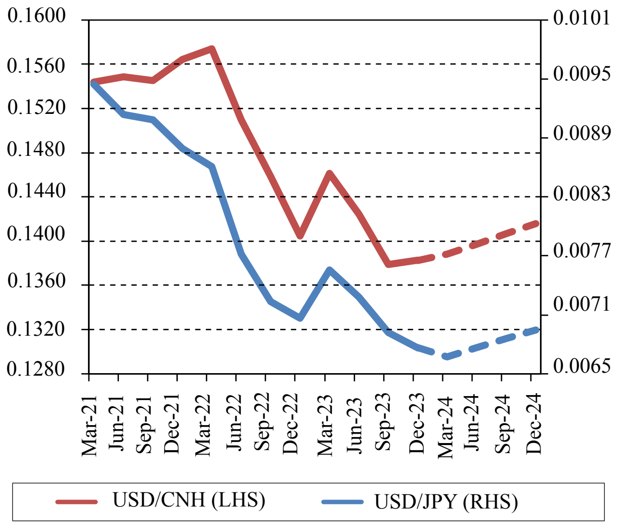
Source: Bloomberg

Chart 4.11A: Exchange Rates against USD



Source: Bloomberg

Chart 4.11B: Exchange Rates against the USD



Source: Bloomberg

The US dollar is expected to slightly depreciate against most major international currencies in the medium term (Chart 4.11A and Chart 4.11B) due to the generally easing US inflation, which raised expectations that the Federal Reserve (the Fed) may start interest rate cuts this year. However, the Fed's first interest rate cut may get delayed to the second half of this year, which is likely to influence investors to hold the safe-haven currency, the US dollar, thus affecting this forecast.

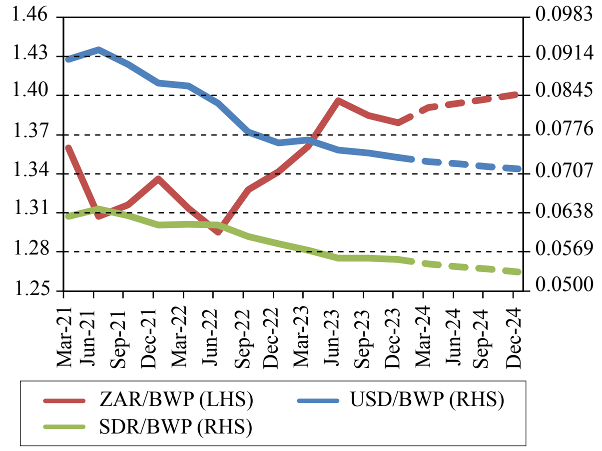
The British pound is expected to appreciate marginally against the US dollar (Chart 4.11A) due to expectations that the Bank of England will delay its first rate cut until August. In addition, UK economic growth is also forecast to exceed earlier expectations following announcement of permanent tax cuts by UK Finance Minister Hunt, aimed at fostering economic growth. The Minister in his spring budget speech revealed that the latest forecasts anticipate a quicker decline in inflation and stronger GDP growth for both 2024 and 2025. On the other hand, Fed Chair Powell hinted that the Fed was nearing sufficient confidence in the inflation trajectory to consider interest rate cuts, prompting investors to anticipate policy easing starting in June. Meanwhile, the euro is anticipated to slightly appreciate against the US dollar as Europe avoids a recession, fostering risk appetite. The recovery of the European economy from the energy shock is expected to align with market expectations, supporting the currency's resurgence. Furthermore, euro's rise could be supported by the weakening US Dollar and declining US Treasury yields. However, the persistent decrease in Eurozone bond yields could hinder the euro's prolonged gains, but a further decline in US bond yields could alleviate this effect.

The Japanese yen is expected to appreciate against the US dollar in the medium term, as speculations grew that the Bank of Japan might start shifting away from its ultraaccommodative monetary policy, a move that is expected to boost the demand for the Japanese yen. The bank raised short-term interest rates from negative levels for the first time in decades at its March 2024 meeting due to rising wages, high inflation and a robust economy. The Bank also ended yield curve control. As a result, the Japanese yen is expected to appreciate as domestic investors repatriate money that has been invested abroad.

The Chinese renminbi is expected to slightly appreciate against the US dollar in the forecast horizon (Chart 4.11B), as the cumulative effects of the stimulus measures that have been announced, including the recent ones around the property sector, should start to reflect in better economic data in the first half of 2024.

Overall, forecast movements of other SDR constituent currencies imply a marginal appreciation of the SDR against the US dollar (Chart 4.11A). The anticipated depreciation of the South African rand against major international currencies is expected to exert downward pressure on the Pula against the SDR constituent currencies in the forecast horizon (Chart 4.12). However, the Pula is expected to appreciate against the South African rand into the medium term.[13] The projected appreciation of the Pula against the South African rand is expected to exert marginal downward pressure on domestic inflation.

Chart 4.12: BWP Exchange Rates against ZAR, USD and SDR



Source: Bloomberg and BoB calculations

Risks to the inflation outlook

Overall, risks to the inflation outlook are assessed to be slightly skewed to the upside. Inflation could be higher than projected if international commodity prices increase beyond current forecasts, supply and logistical constraints persist and the reversal of global economic integration (geoeconomic fragmentation) escalates. Furthermore, inflation may be heightened by possible upward adjustment in administered prices that are not factored in the current projection, possible increase in domestic fuel prices following the increase in the National Petroleum Fund (NPF) levy effective 1 April 2024, and any increase in domestic food prices due to the prevailing El Niño conditions in Southern Africa. However, inflation could be lower than currently anticipated because of the possibility of weaker domestic and global economic activity, as well as any decrease in international commodity prices.

13 Given its singular higher weight relative to any other single currency in the Pula currency basket mechanism, the Pula tends to closely follow the performance of the South African rand. However, the depreciation of the Pula is moderated by the effect of the SDR currencies in the basket.

5. APRIL 2024 MONETARY POLICY COMMITTEE DECISION

At the meeting held on 26 April 2024, the Monetary Policy Committee (MPC) of the Bank of Botswana maintained the Monetary Policy Rate (MoPR) at 2.4 percent.

Inflation

Headline inflation decreased from 3.9 percent in February to 2.9 percent in March 2024, breaching the lower bound of the medium-term objective range of 3 – 6 percent. The decrease in inflation was mainly due to the diminishing impact of the increase in domestic fuel prices in the corresponding period in 2023 (base effects). Inflation is forecast at 2.3 percent for April 2024 and the MPC projects that inflation will remain below the lower bound of the objective range temporarily and revert to within the objective range from the third quarter of 2024 into the medium term, averaging 3.2 percent in 2024 and 5 percent in 2025. The projected low inflation is due to, among others, base effects related to the reversal of value added tax from 12 percent to 14 percent in 2023, subdued domestic demand and the downward revision in recent forecasts of international food prices.

The risks to this inflation profile/trajectory were assessed to be slightly skewed to the upside. The MPC observes that inflation could be higher than projected if international commodity prices increase beyond current forecasts, supply and logistical constraints persist and the reversal of global economic integration (geoeconomic fragmentation). Furthermore, inflation may be heightened by possible upward adjustment in prices controlled by government (administered prices) that is not factored in the current projection and any increase in domestic food prices due to the prevailing El Niño induced drought conditions in Southern Africa. However, these upside risks are partly offset by the possibility of weaker domestic and global economic activity, as well as any decrease in international commodity prices.

Economic Performance

Real gross domestic product (GDP) grew by 2.7 percent in 2023, compared to 5.5 percent in 2022. The slowdown was mainly attributable to subdued mining activity.

According to the April 2024 World Economic Outlook, global output growth is forecast at 3.2 percent for both 2024 and 2025, the same as in 2023. For Botswana, the Ministry of Finance projects growth to accelerate to 4.2 percent and 5.4 percent in 2024 and 2025, respectively.

The MPC notes the potential growth-enhancing economic transformation reforms and supportive macroeconomic policies as underpinned by mindset change. These include the stimulus budget announced on 5 February 2024, by the Honourable Minister of Finance; supportive monetary and fiscal policies; improvement in water and electricity supply; continuation of the Economic Reform and Transformation Plan and Transitional National Development Plan; and infrastructure projects and initiatives announced in the 2024 Budget Speech; as well as various new legislation and changes.

Decision

The MPC recognises that the economy is expected to operate below full capacity in the short term and, therefore, not generate demand-driven inflationary pressures. Although inflation is expected to remain below the lower bound (3 percent) temporarily, it will be within the objective range in the medium term and closer to the upper bound in 2025. Similarly, businesses (as reflected in the latest Business Expectations Survey) expect inflation to be within the medium-term objective range but closer to the upper bound in 2025. Hence, the MPC decided to maintain the MoPR at 2.4 percent.

Accordingly,

(a) the 7-day Bank of Botswana Certificates auctions, repos and reverse repos will be conducted at the MoPR of 2.4 percent;

(b) the Standing Deposit Facility (SDF) Rate is maintained at 1.4 percent, 100 basis points below the MoPR; and

(c) the Standing Credit Facility (SCF) Rate remains at 3.4 percent, 100 basis points above the MoPR.

Meetings of the MPC

The next MPC meetings for 2024 are scheduled as follows:
13 June 2024
22 August 2024
31 October 2024
5 December 2024

Annex: Inflation Forecast Summary for April 2024 MPC Meeting

	Actual					Forecast									
	2023				2024	2024				2025					2026
	Q2	Q3	Q4	Annual Average	Q1	Q2	Q3	Q4	Annual Average	Q1	Q2	Q3	Q4	Annual Average	Q1
Inflation	6.1	2.0	3.5	**5.2**	3.6	2.6 (3.8)	3.3 (4.6)	3.1 (3.9)	**3.2 (4.0)**	3.8 (4.6)	5.3 (4.9)	5.6 (5.1)	5.3 (5.2)	**5.0 (5.0)**	5.4 (5.3)

Note: Figures in parentheses represent the previous MPC forecast (February 2024)

Factors contributing to the downward revision of the forecast in the short term include the following:

Domestically

1. Base effects related to the reversal of value added tax from 12 percent to 14 percent in 2023.
2. Restrained growth in the domestic prices of most categories of goods and services.

Externally

1. Downward revision in forecasts for international food prices.

NOTE

Website: www.bankofbotswana.bw | **Email:** info@bob.bw | **Tel:** 360 6000

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