

AFRICA RISK CONSULTING

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Botswana Summary 15 May 2017

The World Bank advises Botswana to improve transparency and accountability in the mining sector by making details of mining contracts publicly available. This comes as the World Bank's Mining Investment and Governance Review (MinGov) ranks the country low in the accountability and inclusiveness category. Global rating agency Standard and Poor's maintains its -/A-2 rating for Botswana, reaffirming its negative outlook for the economy. Russia-based mining group Norilsk Nickel will sue the government over its default on a deal to sell state-owned nickel mining company BCL. Botswana introduces a tourism levy for all non-Southern African Development Community (SADC) tourists in order to raise funds to develop the tourism sector.

World Bank recommends transparency in mining contracts

The **World Bank** advised Botswana on 4 May to make details of its large mining contracts publicly available in order to promote transparency.¹ The World Bank's recommendations challenge the popular belief that Botswana's public institutions are inclusive and transparent.² World Bank consultant **Nils Handler** criticised the government's secretive conduct in contract negotiation processes, especially for large-scale diamond mining, sales and marketing, in a report titled "*Botswana Mining Investment and Governance Review*" (*MinGov*).³ Handler recommended that the government implement a more open process in which contracts are made public, which will improve transparency and accountability.⁴

*"Although it is well-known for having a 'vibrant' democratic political system, Botswana's public institutions, especially those responsible for managing the mineral sector are anything but transparent or accountable to the public. For example, there are several instances where the government has granted licences for diamond mining in protected areas, such as the **Central Kalahari Reserve**, without publicly disclosing the contract details. This has often led to the forced removal of rural communities, especially the **Basarwa** indigenous people."⁵*

The government has never publicly revealed details of its largest diamond sales contract, signed with **De Beers** in 2011, in which the company transferred its sorting and marketing operations from **London (United Kingdom)** to **Gaborone**.⁶ The decision resulted from the government's ongoing drive to diversify the economy through allied economic sectors and

¹ EWN, 4 May 2017.

² EWN, 4 May 2017.

³ EWN, 4 May 2017.

⁴ Mmegi, 9 May 2017.

⁵Source, analyst, Botswana

⁶ Mmegi, 9 May 2017.

non-diamond related industries.⁷ Although the government's deal with De Beers became one of the most successful examples of beneficiation in the **African** minerals sector, Handler notes that it came at the expense of transparency and inclusiveness.⁸ He also noted that the country ranks "low" in the MinGov report's rankings on accountability and inclusiveness, which reflects concerns that civil society organisations, industry members and some ministries expressed.⁹ The MinGov report also indicated that the government marginalises rural communities from earning mining revenue, despite their experience of negative effects from mining operations, which mostly take place in rural areas.¹⁰ Botswana earns 89% of its foreign income and 30% of national revenues from mining, especially diamonds.¹¹

The MinGov report highlights the negative consequences of president **Ian Khama's** (2008-present) authoritarian governance style, which is pronounced in the minerals sector. The Botswana government will need to revamp its domestic regulatory framework, and ratify global instruments for transparency and good governance in the extractives industry, such as the **Extractives Industry Transparency Initiative (EITI)**.

S&P maintains negative outlook for Botswana

Global credit rating agency **Standard and Poor's** maintained its -/A-2 rating for Botswana on 28 April and reaffirmed its negative outlook for the country's economy.¹² The negative rating is linked to the country's dependence on the diamond sector, which is currently underperforming globally.¹³ The agency wrote,

"The negative outlook reflects our view that economic growth performance and fiscal outcomes could be weaker than we now expect over the next 12 months, barring a structural improvement in international diamond prices to support higher production levels...the ratings are constrained by the country's narrow economic base, which relies heavily on the diamond sector and is vulnerable to external shocks, despite efforts to diversify. Under our current assumptions, we expect Botswana's economy may be able to maintain economic growth rate of three per cent in real terms in 2016, similar to 2016...We estimate the 10-year weighted real GDP per capita growth at 1.5 per cent over 2010-2010. We also expect wealth levels, measured by GDP per capita, will remain above \$6000, over the medium term."¹⁴

S&P also said that Botswana had an improved fiscal fourth quarter that ended 31 March, when its 50:50 joint venture with De Beers, **Debswana Diamond Co**, sold off inventory in response to growing demand for rough diamonds.¹⁵ This lowered the country's deficit for the fiscal year.¹⁶ However, Debswana's diamond production dropped from 23 million carats in 2014, to 20.5 million in 2016, negatively affecting the country's overall economic growth.¹⁷ Average diamond prices also fell by 15%, from \$178 per carat in 2015, to \$152 per carat in

⁷ Rapaport, 30 Apr 2017.

⁸ Mmegi, 9 May 2017.

⁹ Mmegi, 9 May 2017.

¹⁰ Mmegi, 9 May 2017.

¹¹ EWN, 4 May 2017.

¹² IDEX Online, 29 Apr 2017.

¹³ IDEX Online, 29 Apr 2017.

¹⁴ S&P Statement in Botswana, 28 Apr 2017.

¹⁵ IDEX Online, 29 Apr 2017.

¹⁶ Rapaport, 30 Apr 2017.

¹⁷ Rapaport, 30 Apr 2017.

2016.¹⁸ However, Botswana's economy is likely to grow by 3% in 2017, because of an anticipated boom in the service and construction sectors.¹⁹ Botswana is the second largest diamond producer in the world, after **Russia**.²⁰ De Beers obtains more than two thirds of its global diamond supply from Botswana through Debswana.²¹ Diamond exports account for approximately 80% of Botswana's total exports, and roughly one third of its gross domestic product (GDP).²²

S&P's negative outlook reflects Botswana's extensive dependence on diamonds. The government's current efforts at economic diversification have not yet taken off. The cornerstone of its initiatives is the **Economic Stimulus Plan (ESP)**, which Khama launched in October 2015.²³ The anticipated economic boom in construction and services sectors, which is also partly funded by the ESP, will facilitate the shift from dependence on diamond revenue to alternative income streams for the economy.

Russian mining group sues Botswana government

Russia-based mining company **Norilsk Nickel** sued the Botswana government on 27 April over an alleged breach of contract in 2014.²⁴ Investors will watch the case closely, since its outcome will reflect the extent of the country's rule of law, business risk and safety of investments.²⁵ The lawsuit follows a 2016 deal in which Norilsk agreed to sell its operations, including a 50% stake in **South Africa**-based **Nkomati** mine to the state-owned **BCL Group**, for \$271m.²⁶ However, BCL filed for liquidation in October 2016 before the completion of the transaction, citing its inability to pay the purchase price.²⁷ The government also reportedly owes Norilsk \$6.4m from the sale of the **Tati** mine in Botswana.²⁸ BCL has always depended on government subsidies, and the government also reportedly acted as guarantor to BCL during negotiations of the sale of Norilsk's assets.²⁹ However, it allegedly neglected to inform Norilsk of the decision to liquidate BCL, despite the ongoing transaction, which only learned of it through the media.³⁰ Norilsk CEO **Michael Marriott** accused the government of recklessness by entering into the deal while it was unsure of its ability to afford it.³¹

*"The government displayed a complete disregard for the fair, frank and reasonable dealing with outsiders that BCL's insolvent circumstances demanded...Botswana has a reputation as one of the safest and best places to invest in the whole of Africa, and it has earned the strongest credit rating on the continent on that basis. The way that the government of Botswana has acted over BCL brings the validity of that reputation into question."*³²

¹⁸ Idex Online, 29 Apr 2017.

¹⁹ Rapaport, 30 Apr 2017.

²⁰ Rapport, 30 Apr 2017.

²¹ Rapaport, 30 Apr 2017.

²² Rapaport, 30 Apr 2017.

²³ Sunday Standard, 14 Oct 2015.

²⁴ Financial Times, 28 Apr 2017.

²⁵ Financial Times, 28 Apr 2017.

²⁶ Financial Times, 28 Apr 2017.

²⁷ Financial Times 28 Apr 2017.

²⁸ Mining Review, 28 Apr 2017.

²⁹ Mining Review, 28 Apr 2017.

³⁰ Mining Review, 28 Apr 2017.

³¹ Financial Times, 28 Apr 2017.

³² Norilsk Nickel Africa CEO, Michael Marriott quoted in Business Day, 2 May 2017.

The government had indicated in February that it was on the verge of securing new investment from unnamed investors in the **Middle East**, although it is yet to confirm if it has secured new financing.³³ However, Norilsk indicated that it will block any agreement that the government tries to enter into before it compensates the company for the failed deal.³⁴

The lawsuit will challenge Botswana's reputation as a safe investment destination. The **Canada-based Fraser Institute** ranked Botswana as the best mining investment destination in Africa, and ranked second to **Australia** on regulatory certainty worldwide.³⁵ The case also shows the extent to which the non-disclosure and public audit of mining contracts may result in disputes that emanate from administrative or legal missteps.

Tourism ministry introduces new tax

The tourism ministry announced that it will introduce a new \$30 **Tourism Development Levy (TDL)** on visitors to Botswana, according to media reports on 3 May.³⁶ This will apply to tourists who are not resident of the **Southern African Development Community (SADC)** member states.³⁷ The government will charge the tax at all airports and border crossings, and indicated that it will use the funds to carry out conservation and national tourism development initiatives, which will support the growth of the industry and broaden the country's tourism base.³⁸ Each TDL stamp will be valid for a month, and tourists can use it for multiple entries within the 30-day period.³⁹ **Botswana Tourism Organisation (BTO)** spokesperson **Tafa Tafa** indicated that the government has begun installing payment points at all the country's points of entry, which will enable tourists to pay before entering the immigration ports.⁴⁰ Tourism minister **Tshekedi Khama** said his ministry imposed the tax after failing to secure funding from the central government through the **National Development Plan II (NDPII)**.⁴¹

*"Marketing Botswana to the international community was an expensive exercise, and the local events that the BTO supported grew from four when [I] took over, to 16... We had hoped to get more money through NDPII ... but when we realized that the budget was not going to get any better we had to pursue this route ...Maun Airport is one of our biggest embarrassments, looking at the quality of the tourists who are transiting through it to the **Okavango Delta**."⁴²*

Khama said Botswana had joined other countries in imposing a tourism levy.⁴³ He also said that the ministry decided to charge the levy on tourists to ensure the ministry received the money directly.⁴⁴ Botswana's tourism industry has been a key economic sector since independence, and its global reputation for political stability and good governance makes it an attractive destination for many tourists, especially from countries in **North America** and

³³ Business Day, 2 May 2017.

³⁴ Business Day, 2 May 2017.

³⁵ Financial Times, 28 Apr 2017.

³⁶ Deutsche Welle, 3 May 2017.

³⁷ Deutsche Welle, 3 May 2017.

³⁸ Deutsche Welle, 3 May 2017.

³⁹ Deutsche Welle, 3 May 2017.

⁴⁰ Daily News, 2 May 2017.

⁴¹ Daily News, 2 May 2017.

⁴² Minister Khama quoted in Daily news, 2 May 2017.

⁴³ Daily News, 2 May 2017.

⁴⁴ Daily News, 2 May 2017.

Europe.⁴⁵

The move to impose a tourist tax is unlikely to reduce the number of tourists because of the relatively small amount. However, it will earn the ministry substantial funds, given the increasing popularity of Botswana as a tourist destination.⁴⁶

About Africa Risk Consulting:

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⁴⁵ Daily News, 2 May 2017.

⁴⁶ Daily News, 2 May 2017.