REPUBLIC OF BOTSWANA

2018/2019

BUDGET STRATEGY PAPER

MINISTRY OF FINANCE AND ECONOMIC DEVELOPMENT

August 2017

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I. INTRODUCTION

1. The Ministry of Finance and Economic Development has consistently produced the Budget Strategy Paper (BSP) every year, for the past seven (7) years, as part of the national budgeting process. The draft BSP, which is discussed extensively at various budget consultation forums, aims at giving a synopsis of the available resource envelope vis-à-vis the required government expenditure for the year, as well as the medium term budget projections based on the prevailing economic conditions. These extensive budget consultation forums provide an opportunity for key stakeholders to review the: proposed national policies; priority areas; implementation strategies; as well as proposed programmes, projects and budget allocations for the year. Following these consultations, the revised BSP will then be used to inform the Budget Speech for the next financial year. Hence, for the 2018/2019 BSP, Ministries have also been requested to provide a review in the implementation of their programmes and projects during 2017/2018 financial year, in terms of challenges encountered as well as strategies going forward into 2018/2019.

2. In preparing the 2018 BSP, it is worth noting that, the 2018/2019 is the second year of implementation of National Development Plan (NDP) 11 and Vision 2036. The theme for NDP 11 is "*Inclusive Growth for the realisation of Sustainable Employment and Poverty Eradication*" while emphasis for Vision 2036 is on, "*Achieving Prosperity for All*". Hence, the strategic thrust for 2018/2019 should continue being on sustainable job creation that delivers on poverty eradication through creation of sustainable job opportunities and contributing towards making all Batswana better off.

3. Such a strategic thrust will be pursued within the backdrop of a mild recession in 2015 in the domestic economy. Future growth in the domestic economy, will however be supported by the prospects of strong positive global growth in 2017 and 2018, particularly in emerging markets and developing economies, as well as Sub-Saharan Africa. Domestic inflation has remained within the Bank of Botswana's objective range in the first half of 2017. The monetary policy mechanism has also continued to be supportive of investment initiatives by maintaining the bank rate at its all-time low level of 5.5 percent. To this end, the domestic economy is expected to register positive growth rates in 2017 and 2018. However, the country remains vulnerable to external shocks, especially volatile exchange rate movements, which also affect global demand for our major export, the diamonds.

4. This document consists of six (6) sections, including this introduction. Section II reviews the global and domestic economic performance and outlook, while the 2016/2017 budget outturn is reviewed in Section III. An overview of the NDP 11 national priority areas, as well as strategies envisaged for implementation in the 2018/2019 financial year are discussed in Section IV. Section V contains the budget projections for 2018/2019 and 2019/2020, while Section VI provides the summary conclusion.

II. MACROECONOMIC DEVELOPMENTS

Global Economic Review and Outlook

5. The global economy is anticipated to gain momentum in 2017 and 2018, following a weak outturn in 2016 According to the World Economic Outlook (WEO) update released by the International Monetary Fund in July 2017, global economic growth is projected to increase from estimated growth rate of 3.2 percent in 2016 to reach 3.5 percent and 3.6 percent in 2017 and 2018, respectively (Table 1). The positive outlook is attributed to an anticipated improvement in the performance of the financial markets and a recovery in manufacturing industries.

Table 1: World Economic Outlook Projections (%)

		April 2017 Projections		July 2017 Projections Update	
	2016	2017	2018	2017	2018
World Output	3.2	3.5	3.6	3.5	3.6
Advanced Economies	1.7	2.0	2.0	2.0	1.9
Emerging Market Economies	4.3	4.5	4.8	4.6	4.8
Sub-Saharan Africa	1.3	2.6	3.5	2.7	3.6

Source: WEO Update, July 2017.

6. A summary analysis of the growth prospects for the main regions in 2017 indicates that advanced economies remained unchanged at 2.0 percent in July 2017, as was projected in April 2017. However, the projected growth rate of this group of countries is expected to trend downwards to 1.9 percent in 2018. Many advanced economies are expected to face excess capacity, as well as headwinds to potential growth from aging populations, weak investment and low productivity. The projected decline in growth for 2018 is largely attributed to the assumption that fiscal policy will be less expansionary in the United States, due to the uncertainty surrounding the timing and nature of US policy changes, as well as policy and supply side reforms in China. Emerging markets and developing economies at the same time are projected to grow by 4.6 percent and 4.8 percent in 2017 and 2018, respectively. Such higher growth rates are mainly driven by commodity importing countries such as China and India, but also reflect to a large extent, improving conditions in the large commodity exporting countries.

7. However, there are some downside risks to this positive global economic outlook, which include structural problems such as low productivity growth and high income inequality. These risks pose a threat to a strong recovery as well as to global economic integration, particularly in emerging markets and developing economies.

8. As for the Sub-Saharan Africa region, a modest recovery is anticipated in 2017, with growth projected to reach 2.7 percent, compared to 1.3 percent registered in 2016. This positive growth momentum is expected to continue in 2018, during which the region is projected to grow by 3.6 percent. The medium term positive outlook in the Sub-Saharan Africa is generally attributed to the recovery in commodity prices and easing of drought conditions in the region. Expected positive global and regional economic outlook for 2017 bodes well for the domestic economy, which is an open economy dependent on trade. In particular, the recovery of commodity prices and improved global demand will boost diamond exports, thereby increasing growth prospects in the domestic economy. Hence, policies for promotion of export-led growth are needed.

Domestic Economic Review and Outlook

9. After recording a decline of 1.7 percent in 2015, the domestic economy recovered strongly to register a positive growth of 4.3 percent in 2016 (Table 2). The positive rebound in the domestic economy was largely due to the improvement in the Trade, Hotels & Restaurants and Transport & Communications sectors, which recorded positive growth rates of 13.5 percent and 5.6 percent, respectively. Growth in the Trade, Hotels and Restaurants sector was mainly driven by downstream diamonds industries, which contributed significantly to the wholesale sub-sector. This is a positive result of the decision that was taken to relocate the Diamond Trading Company International from the United Kingdom to Botswana in 2012.

Table 2: Real GDP Growth Rates by Sector (2006 constant prices): 2015-2019

	Actual		*Projections*		
	2015	**2016**	**2017**	**2018**	**2019**
1. Agriculture	0.3	-1.0	1.0	1.1	1.2
2. Mining	-19.6	-3.7	0.5	9.3	2.6
3. Manufacturing	3.2	0.8	1.8	1.9	1.5
4. Water & Electricity	7.0	123.0	39.2	10.9	4.0
5. Construction	4.0	4.2	4.5	4.4	4.3
6. Trade, Hotels & Restaurants	-3.9	13.5	9.1	7.3	10.0
7. Transport & Communications	4.5	5.6	6.7	6.2	6.2
8.Finance & Business Service	4.5	3.8	3.6	4.0	4.0
9. General Government	3.3	2.0	2.6	2.6	2.6
10. Social & Personal Services	3.6	3.5	3.6	3.7	3.7
Adjustment items	1.1	0.0	4.7	5.3	5.0
Total GDP	**-1.7**	**4.3**	**4.7**	**5.3**	**5.0**
Non-Mining	**1.7**	**5.5**	**5.3**	**4.8**	**5.4**

Source: Statistics Botswana Actuals & MFED Projections.

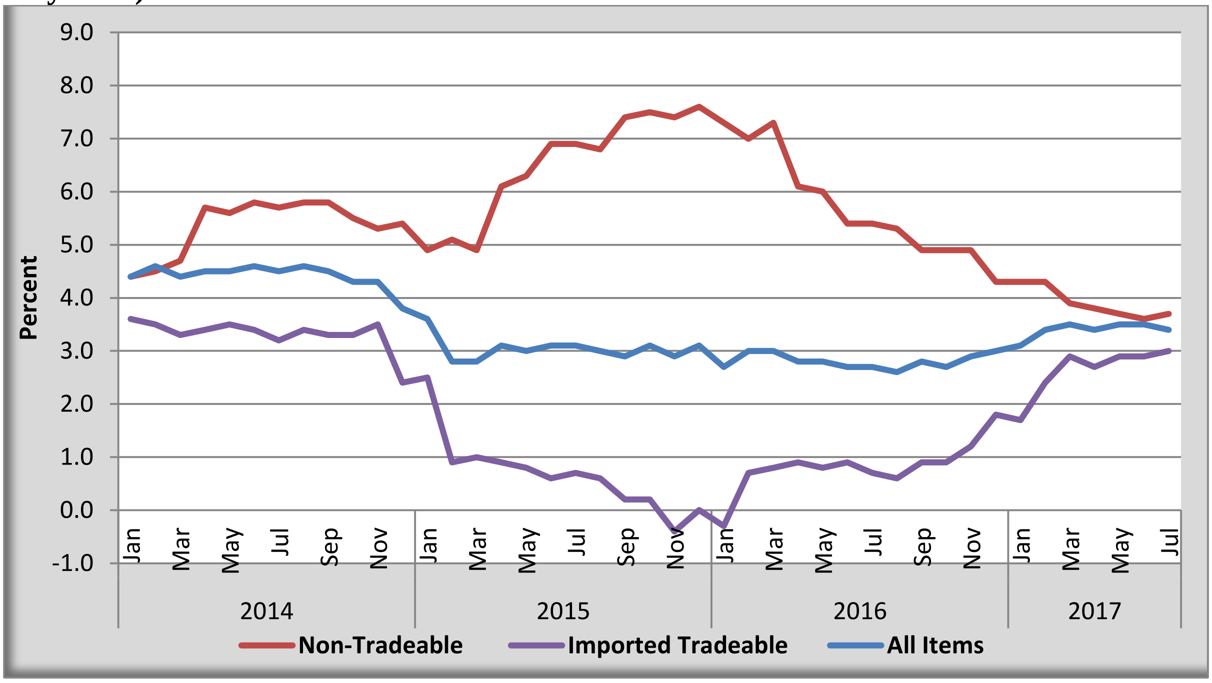
10. Water & Electricity sector which supports other sectors, registered a higher growth of 123.0 percent in 2016, however, its contribution to GDP is insignificant. In addition, other sectors which recorded positive growth rates during 2016 were Construction (4.2 percent), and Finance and Banking Services (3.8 percent). Meanwhile, the agriculture and mining sectors recorded negative growth rates in 2016; the latter mainly due to a decline in copper production as well as the provisional liquidation of BCL mine in October 2016.

11. In terms of the domestic economic outlook, real gross domestic product (GDP) is projected to grow by 4.7 percent, 5.3 percent and 5.0 percent in 2017, 2018 and 2019, respectively (Table 2). The positive outlook is attributed to projected improvements in the sectors of: Mining; Trade, Hotels & Restaurants; Transport & Communication, and Water & Electricity. The Mining sector is expected to recover in line with the positive global economic prospects, while the other sectors will continue to benefit from the implementation of the Economic Stimulus Programme adopted by Government to boost growth, and create employment opportunities.

Inflation and Monetary Policy

12. Domestic inflation remained low during 2016, with average inflation reaching a recent all-time low rate of 2.8 percent; well below the lower band of the Bank of Botswana's objective range of 3-6 percent (Figure 1). Low domestic demand pressures and global fuel prices contributed to the positive price developments in the country during the period. This favourable inflationary environment provided a scope for easing monetary policy to support economic activity. Hence, monetary authorities adjusted the policy rate or bank rate from 6.0 percent in August 2015 to 5.5 percent in August 2016. This rate has been maintained thus far, on account of the positive medium-term inflation outlook. An accommodative monetary policy stance is at this point considered appropriate to support economic activity, mobilisation of resources and financial sector development.

Figure 1: All Items, Non-Tradeable and Imported Tradeable Inflation, (January 2014 to July 2017)



Source: Statistics Botswana, July 2017

13. Meanwhile, the low inflationary environment observed in 2016 has continued in the first half of 2017, with monthly inflation rates reaching as low as 2.7 percent in January 2017, and 2.9 percent in June 2017, hence remaining at the lower bound of Bank of Botswana's objective range of 3-6 percent. With low domestic demand pressures and subdued trading partners' inflation, hence low imported inflation, the outlook for price stability remains positive in the short to medium-term. A low and predictable inflation coupled with a conducive financial environment therefore eases savings mobilisation, productive investment and increases competitiveness of domestic producers. This is necessary for attaining a sustainable economic growth and creation of employment opportunities particularly during the period where growth is still below trend.

14. However, downside risks to inflation outlook in the short term include the impact of adjustments to administrative prices such as electricity and water tariffs effected from April 2017, as well as possible recovery in international oil prices.

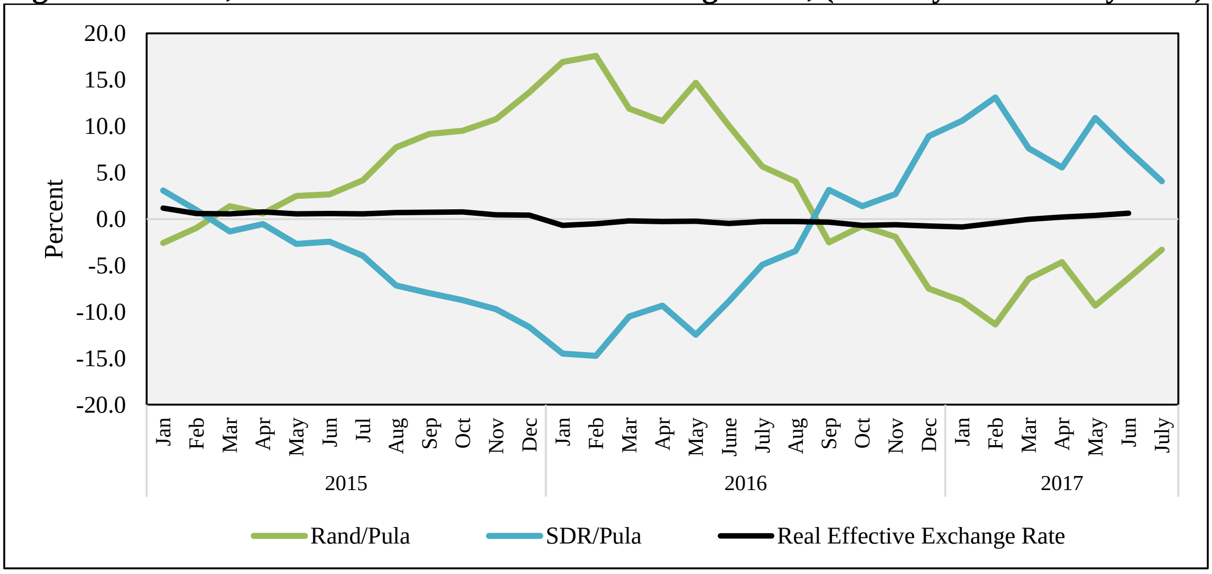
Exchange Rate Developments

15. The management of the country's exchange rate policy is aimed at achieving and maintaining competitiveness of domestic enterprises in the international and domestic markets. Achieving this strategic objective requires a stable real effective exchange rate (REER), maintained through regular adjustments of the currency basket weights to reflect the country's trade patterns, and the rate of crawl based on the projected inflation differentials between Botswana and its trading partners.

16. Pursuant to this objective, adjustments were made to both the currency basket weights and rate of crawl in January 2017; with the weight of the South African rand in the basket reduced from 50 percent to 45 percent, while that of the International Monetary Fund's Special Drawing Rights (SDR) currency increased from 50 percent to 55 percent. At the same time, an upward rate of crawl of 0.26 percent per annum was adopted for 2017, down from 0.38 percent in 2016, reflecting the expected narrowing of inflation differential between Botswana and its trading partners during the current year.

17. As a result of the marginal inflation differential between Botswana and trading partner countries; the REER remained broadly stable (Figure 2), appreciating marginally by 0.6 percent from 100.0 in June 2016 to 100.6 in 2017, reflecting a positive inflation differential between the country and its trading partners.

Figure 2: REER, Rand/Pula and SDR/Pula Exchange rates, (January 2015 to July 2017)



Source: Bank of Botswana & MFED

18. In terms of bilateral exchange rate movements, the domestic currency unit appreciated against the SDR by 4.1 percent, while it depreciated against the rand by 3.3 percent, over the twelve months to July 2017 (Figure 2). Against the composite currencies of the SDR, the Pula appreciated by 12.4 percent against the Japanese yen; 5.7 percent against British pound; 5.2 percent against the US dollar, while it depreciated by 0.6 percent against the euro. The appreciation of the Pula against the British pound reflected, in part, the continued uncertainty over the economic effects of Britain's decision to exit from the European Union.

Balance of Payments

19. The external balance of payments recorded a surplus of P2.8 billion in 2016, compared to a deficit of P57 million recorded in 2015. The surplus was attributable to the improvement in the trade balance as exports of rough diamonds increased in 2016. Exports of goods and services increased by 9.1 percent, sustained by a significant increase of 13.9 percent in exports of rough and polished diamonds, which was supported by higher demand in global markets. The relocation of the De Beers aggregation and sales to Botswana thus continues to benefit the local diamond cutting and polishing businesses, as well as the economy as a whole.

20. Total imports of goods and services on the other hand were valued at P66.1 billion in 2016, representing a decline of 9.2 percent from the revised P72.8 billion in 2015.The decline in imports was largely attributed to the contraction of diamond imports, textiles and footwear, vehicles and transport equipment and fuel, owing to the generally weak domestic demand.

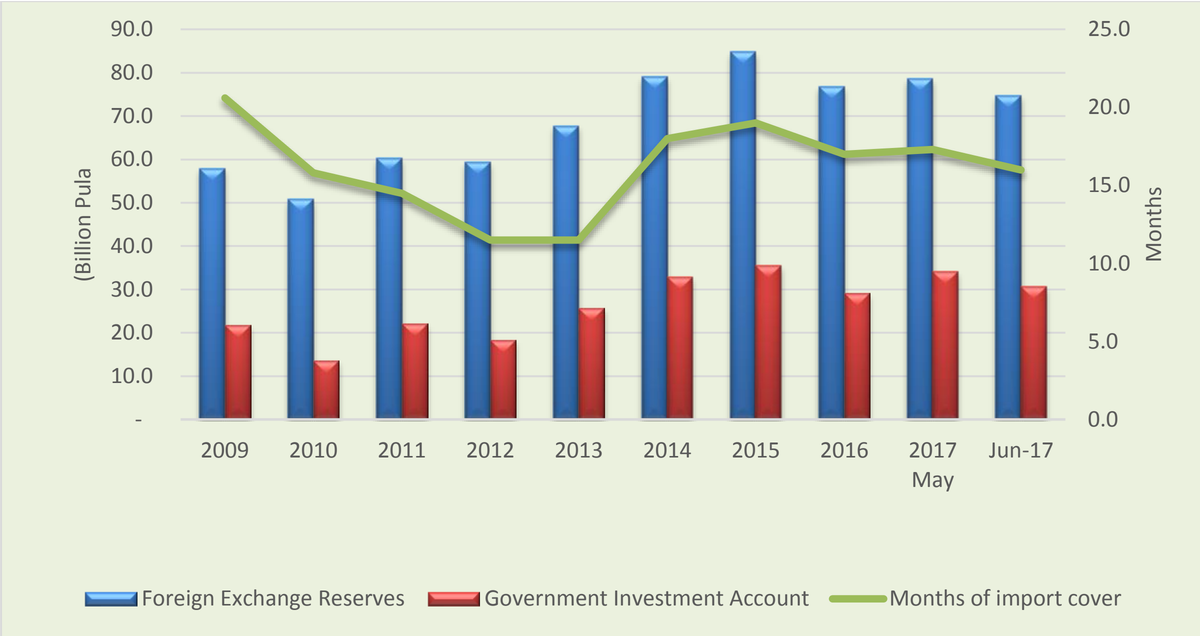
21. Overall, the current account registered a surplus of P19.9 billion for the period under review mainly due to an increase in mineral exports. The surplus was also sustained by inflows from the Southern African Customs Union (SACU), however lower in 2016 than 2015. SACU receipts have been declining as share of GDP since 2012, owing to the appreciation of the Pula against the rand, and the deceleration in South Africa's GDP growth, which in turn lowered imports growth. SACU receipts are projected to fall further in the medium term reflecting a further reduction in South Africa's growth. However, the current account will continue to be supported by the growth in mineral exports emanating from the anticipated robust global demand particularly in major diamond markets. With the narrow export base and dependency on external sources of which the economy has little control over, the economy remains susceptible to economic shocks which undermine the external balance outcome.

Foreign Exchange Reserves

As at December 2016, foreign exchange reserves amounted to P76.8 billion, representing a decline of 9.5 percent from P84.9 billion registered in December 2015. Measured in terms of import cover, the foreign exchange reserves in December 2016 were equivalent to 17 months of import cover of goods and services, compared to 19 months in December 2015. The fall in the country's level of foreign exchange reserves was mainly due to an increase in demand for foreign exchange to pay for imported electricity. Of the total reserves as at the end of December 2016, the Government Investment Account (GIA) amounted to P29.1 billion, a decline from P35.5 billion in December 2015. Although the stock of foreign exchange reserves remains comfortably high, the country's volatile and uncertain foreign exchange receipts requires monitoring of the reserve adequacy and implementing policies that make prudent use of revenues from non-mineral resources.

22. As at June 2017, the level of foreign exchange reserves has slightly declined to P74.7 billion, or US$7.3 billion, from P78.6 billion recorded the previous month. Of this total reserves, the Government Investment Account (GIA) accounted for P30.6 billion (Figure 3). The decline in GIA has negative implications in terms of the ability to absorb major external shocks in the economy and guard against depletion of savings for future generations.

Figure 3: Foreign Exchange Reserves and Government Investment Account: 2009-June 2017



Source: Bank of Botswana, August 2017.

III. BUDGET OUTTURN FOR 2016/2017

23. The budget outturn for the 2016/2017 financial year was better than anticipated in the revised budget estimates, mainly due to improved revenue situation underpinned by a significant performance of the BoB revenue. As a result, a budget deficit of P0.53 billion or 0.3 percent of GDP was realised, compared to the P1.10 billion or 0.6 percent of GDP projected in the revised budget estimates.

Total Revenues and Grants

24. The budget outturn for the financial year 2016/2017 indicates that total revenue and grants amounted to P56.8 billion, which represents 102 percent over the target of P55.9 billion estimated in the revised budget. Of this amount, 39.6 percent was Mineral revenue; 20.8 percent customs & excise; 16.8 percent non-mineral income tax; 11.6 percent VAT; and 5.0 percent BoB revenue. Except for Mineral, customs & excise and BoB revenue items, the performance of most revenue items in the budget outturn was below their targets, as indicated in the revised budget. Mineral revenue outperformed its target in the revised budget by 8.0 percent, due to increased mineral tax received during the financial year following the sale of diamond inventory. On the other hand, the increase on the BoB revenue over the figure in the revised budget was due to the unanticipated performance of the Government investment portfolio, as well as some effects of currency movements on the portfolio.

Total Expenditure and Net Lending

25. Total expenditure and net lending during 2016/2017 amounted to P57.4 billion, of which; recurrent expenditure amounted to P41.6 billion, or 72.5 percent, while the development budget amounted to P15.1 billion or 26.3 percent of total expenditure. The overall expenditure performance was satisfactory; with the development budget recording 93.0 percent over the revised budget, while the recurrent budget recorded 103 percent. The former included equity injection into state owned enterprises amounting to P100 million, and P1.05 billion lending from the Public Debt Service Fund towards state-owned enterprises.

26. The overall budget balance was a small deficit of P535 million or -0.3 percent of GDP. This was almost a balanced budget, which is consistent with the fiscal policy of maintaining balanced budgets in the medium term. In order to achieve economic growth and development, Government's fiscal policy objective is to maintain a balanced budget and only run modest deficits under exceptional circumstances. This is because deficits have the potential to erode our foreign exchange reserves as well as impact negatively on the country's sovereign credit ratings. While reserves are critical in maintaining economic stability during hard times, positive sovereign ratings are key in attracting foreign direct investment.

Table 3: Budget Outturn for 2015/16 and 2016/17 (P million)

	Actual Budget	**Revised Budget**	**Budget Outturn**	**% of**
	2015/16	**2016/17**	**2016/17**	**Revised Budget**
Total Revenues & Grants	**47,420.3**	**55,925.6**	**56,828.3**	**102**
Mineral Revenue of which:	14,437.64	20,854.00	22,495.88	**108**
Mineral Tax	4,455.96	4,273.25	7,212.51	**169**
Mineral Royalties & Dividends	9,981.68	16,580.75	15,283.37	**92**
Customs & Excise	15,817.58	11,515.56	11,773.34	**102**
Non Mineral Income Taxes	8,690.63	11,468.05	9,572.20	**83**
VAT	5,547.59	7,528.56	6,642.69	**88**
BOB Revenue	1,133.03	848.00	2,841.95	**335**
Other Revenue	1,648.20	3,488.40	3,346.09	**96**
Grants	**145.65**	**223.03**	**156.17**	**70**
Total Exp. & Net Lending	**54,411.16**	**57,031.27**	**57,363.80**	**99**
Recurrent Expenditure	40,413.36	39,662.90	41,633.19	**103**
Development Expenditure	12,772.93	16,276.91	15,137.70	**93**
Government Equity	545.00	100.00	100.00	**100**
PDSF/DF Loans	755.00	1,317.46	1,052.30	**80**
Repayment of DF/PDSF loans	-75.13	-326.00	-559.39	**172**
Overall Surplus/Deficit(-)	**-6,990.84**	**-1,105.67**	**-535.48**	29
% of GDP	**-4.7**	**-0.7**	**-0.3**	

Source: MFED, August 2017

IV. NATIONAL PRIORITY AREAS AND BUDGET STRATEGIES FOR 2018/2019

27. The country's medium term national priorities were established as part of the NDP 11 approved in December 2016. These are: *Developing Diversified Sources of Economic Growth; Human Capital Development; Social Development; Sustainable Use of Natural Resources; and Consolidation of Good Governance and Strengthening of National Security.* Annual national budgets therefore, provide an opportunity for Government to implement specific strategies and allocate appropriate resources to the relevant sectors of the economy in order to realise these national priorities. 2018/2019 financial year will be the second in the implementation of NDP 11, and therefore, the proposed policies and strategies for implementation during the year, as well as the resource allocations, should be aligned to the national priorities, as indicated in the medium term plan.

Developing Diversified Sources of Economic Growth

28. The main objective under this national priority area is to diversify the economy in terms of the sources of growth, government revenues and composition of exports. In this regard, various initiatives will be implemented during the 2018/19 financial year towards the achievement of this objective. These will include the implementation of on-going initiatives in the areas of *mineral beneficiation, cluster development, special economic zones, and economic diversification drive.* Specific programmes under the initiatives planned for the 2018/19 financial year will be presented by the relevant Ministries and Departments during the preparation of the annual budget.

29. In addition, Government will continue to implement several infrastructural projects, as part of the efforts to diversify the economy during the 2018/2019 financial year. These infrastructural projects will be implemented across the board to include: water and energy connection networks; transport and communications; and, development of border facilities to facilitate trade, to mention but a few. Specific programmes and projects planned for the 2018/2019 financial year under these broad areas will also be presented by the relevant Ministries and Departments at the appropriate stage in the budgeting process. Suffice to note that the importance of *Developing Diversified Sources of Economic Growth*, as a national priority area, is reflected in the largest amount of the development budget proposed for allocation to the area. This is in recognition of the central role of economic growth to development in general, or even achieving the other national priorities.

Human Capital Development

30. Under the national priority area of human capital development, efforts will continue during the 2018/2019 financial year to identify areas for reforms, with a view to improving on the delivery of education and training in the country. One of the initiatives planned under the basic education is the finalisation of the Out of School Children Policy and curriculum, whose aim is to break the cycle of inter-generational poverty by ensuring that: (i) children who would otherwise not start school do so at the right age; (ii) children who are struggling with school achievement and attendance return to school; and, (iii) children and youth who are unable to be in school are given a second chance of gaining basic education through an alternative route and are supported to move into technical and vocational opportunities. Likewise, more initiatives will be presented by the relevant Ministries and Departments during the budget preparation process.

31. Achieving some of the objectives envisaged under this national priority area will however require continued investment in the social infrastructure such as education and health facilities.

Construction and maintenance of health facilities such as hospitals and clinics and the education and training facilities including schools and vocational training centres will continue to be a priority, as evidenced in previous annual budget allocations. With Government's commitment to the development of human capital, it is expected that programmes for improving social facilities will continue to be allocated substantial portion of the annual budget during the 2018/2019 financial year, as it has been the case in previous years.

Social Development

32. Social development is yet another area identified as a national priority in NDP 11. Under this national priority area, Government is committed to: *promote access to basic services such as shelter and sanitation; provide social safety nets by ensuring their better alignment with other interventions for the best results; implement initiatives aimed at eradicating absolute poverty; and strength health prevention interventions to ensure healthy living during NDP 11*. Hence, as part of the preparation of the 2018/2019 budget, relevant Ministries will be proposing various initiatives for implementation to achieve the goals envisaged under the *Social Development* national priority area. As in the past years, Government will endeavour to provide adequate budget provision during the 2018/2019 financial year, subject to the resource envelope, to ensure smooth implementation of the envisaged initiatives by Ministries in order to realise the country's goals under this priority area.

Sustainable Use of Natural Resources

33. A sustainable and resilient development path rests on the harmony between the country's environment, the economy and the people. In this respect, several initiatives and programmes are planned for implementation under this national priority area during NDP 11; some of which will form part of the budget for the 2018/2019 financial year. Specific initiatives planned for the 2018/2019 financial year will be presented by the Ministry of Environment, Natural Resources Conservation and Tourism, which is the main Ministry responsible for this national priority area, later during the budgeting process. Suffice to note that the strategies for achieving the goals for this priority area, as indicated in NDP 11, are: *sustainable management of natural and cultural resources; climate change adaptation and mitigation; integration of sustainable human settlements; and, a healthy environment for healthy population*. It is therefore, expected that the Ministry will be presenting some initiatives and programmes towards the implementation of these strategic objectives during the 2018/2019 financial year, with a view to contributing to the goals for this sustainable use of natural resources priority area.

Good Governance and Strengthening of National Security

34. In recognition of their importance to development, good governance and strengthening of national security were adopted as one of the national priorities in NDP 11. Among the key elements of good governance are: *the promotion of participatory democracy; transparency and accountability of government; and, observance of the rule of law*. Various strategies are envisaged for implementation during the Plan period to achieve these goals. Regarding the strengthening of national security, Government through NDP 11, committed to implement strategies to safeguard territorial integrity and sovereignty and ensure public safety and protection. Using the budget for the 2018/2019 financial year as a vehicle to implement some of these strategies, relevant Ministries will be presenting some of specific initiatives planned for implementation later on in the budgeting process.

35. The nature of operations of the safety and security agencies makes it inevitable to invest in infrastructure development in order to realise the goals envisaged under this national priority area. Consequently, in addition to the implementation of various initiatives, the safety and security cluster will continue to be allocated adequate funds in the 2018/2019 financial year, subject to the resource envelope, in order to construct offices and housing accommodation for police, prisons and BDF personnel, as well as upgrade equipment for the army to enhance security capabilities.

V. BUDGET PROJECTIONS FOR 2018/2019

Fiscal Policy Objectives

36. The design and implementation of fiscal policy must be executed to ensure optimum allocation of resources and equitable distribution of income and wealth. In this way, efficiency in the use of public finances has a special role to play in creating fiscal sustainability in the government budget. To this end, preceding budgets have been characterised by deficits, due to low domestic economic growth as a result of the slow recovery in the global economy, coupled with increasing expenditure pressures aimed at stimulating economic growth. However, going forward, it will be important to reign in on the expenditure so that the country returns to a sustainable fiscal position in the medium to long-term.

37. Furthermore, Government will continue to promote the development of the private sector, as a potential source of growth and revenues. A significant growth in the private sector contributes to the expansion of the domestic revenue base, which cushions the country against volatile mineral revenues. In the medium term, the fiscal objective is to promote fiscal stability by ensuring that the country's expenditure path remains broadly in line with revenue growth trajectory. In this regard, one of the measures is to curtail undesirable and unproductive expenditure patterns, which do not contribute to growth, but increases pressure on the budget. This calls for strict enforcement of the fiscal discipline throughout the public sector to remove wastage and ensure that government limited resources are deployed to provide the necessary economic infrastructure needed for growth, and the basic social services for the citizens, if the country is to achieve prosperity for all.

Medium Term Fiscal Framework (MTFF)

38. Table 4 presents the budget projections for financial year 2018/2019 in the Medium Term Fiscal Framework (MTFF). The MTFF takes into account: the prevailing macroeconomic environment as detailed in section II; information on current Government policies; as well as new policy initiatives that may have significant impact on Government revenues and expenditures.

Table 4: Government Budget (P' million), 2016/2017 to 2019/2020[1]

	2016/2017	2017/2018	2018/2019	2019/2020
		Revised	Projections	
Total Revenue and Grants	**56,828.32**	**57,187.11**	**58,810.83**	**66,897.84**
Mineral Revenue	22,495.88	16,334.25	19,670.50	25,687.00

[1] Please note that this figures are likely to change as, and when new data becomes available.

Customs & excise	11,773.34	17,059.79	14,002.26	13,964.78
Non-mineral income tax	9,572.20	12,348.20	13,357.67	14,503.89
VAT	6,642.69	8,106.36	8,106.36	8,801.97
BoB revenue	2,841.95	708.00	1,000.00	1,000.00
Other revenue & grants	3,502.26	2,630.51	2,674.04	2,940.20
Total Expenditure and Net Lending	**57,363.80**	**62,425.42**	**66,872.53**	**67,447.48**
Recurrent Expenditure	**41,633.19**	**45,811.99**	**48,976.69**	**50,976.59**
Personal emoluments & pensions	19,224.22	22,898.90	23,730.05	24,591.37
Other charges	9,707.79	8,241.60	10,103.38	10,515.10
Grants & subventions	11,823.35	13,768.85	14,275.17	14,809.42
Interest payments	877.83	902.64	868.09	1,060.71
Development Expenditure	**15,137.70**	**16,660.89**	**17,971.84**	**16,546.89**
Net Lending	**592.91**	**-47.46**	**-76.00**	**-76.00**
Overall surplus/ deficit (-)	**-535.48**	**-6,559.98**	**-8,061.70**	**-549.64**
% of GDP	*-0.31*	-3.52%	-4.00%	-0.25%

Source: MFED, August 2017

Projected Total Revenues and Grants

39. The 2018/2019 financial year budget points to a constrained fiscal space, which continues to characterise the domestic economy. This is mainly a result of slow growth in revenues, coupled with continued expenditure pressures, due to additional budgetary requirements by various Ministries. Total revenues and grants for the 2018/2019 financial year are estimated at P58.81 billion, with the largest amount of P19.67 billion, or 33.4 percent of the total revenues expected to be accounted for by mineral revenue. Customs and excise is projected to account for the second largest share of total revenue at P14.00 billion, or 23.8 percent during the 2018/2019 financial year. This will be followed by non-mineral income tax at P13.36 billion, or 22.7 percent and Value Added Tax at P8.11 billion, or 13.8 percent of the total. The remaining 6.3 percent of the total revenues expected in the 2018/2019 financial year will come from the Bank of Botswana, as expected earnings on government investment account of the foreign exchange reserves, and "other revenues", which is mainly property income taxes, fees and grants from donors and development partners.

Proposed Total Expenditure and Net Lending

40. The proposed 2018/2019 expenditure budget allocations amount to P66.87 billion, representing an increase of 7.1 percent from the current year's revised budget of P62.42 billion. Of the proposed total expenditure; P48.98 billion, or 73.2 percent of the total is proposed for Recurrent Expenditure, mainly to cover personal emoluments and pensions and gratuities (P23.73 billion) and subventions to state-owned enterprises, Local Authorities in the form of revenue support grants, and post-secondary schools' bursaries (P14.27 billion). The remaining balance of P17.97 billion, or 26.9 percent of the total is proposed for the Development Expenditure in the financial year 2018/2019. The amount proposed under the development vote will cover, first and foremost, on-going projects and programmes and the balance can be used for new projects as set out in the NDP 11.

Expected Overall Balance

41. With estimated total revenues and grants of P58.81 billion and proposed total expenditure and net lending of P66.87 billion for 2018/2019, the overall budget balance points to a deficit of P8.06 billion, or minus 4.0 percent of GDP. It is important to note that, the projected budget deficit has to be viewed against the recent trend, where Government continues to run budget deficits, contrary to its commitment in NDP 11 to reign in budget deficits.

42. To finance the expected budget deficits, Government will be guided by the Medium Term Debt Management Strategy (2017/18 – 2019/2020), which clearly outlines the options available in the event of government budget deficits. However, in the short term, the options revolve around borrowing, either domestic or external, subject to the country's borrowing limits, and drawing down on government cash balance held as part of the foreign exchange reserves. Each of these options has its own pros and cons. For instance, the option of drawing down on government cash balances has the potential to jeopardise our sovereign credit, as the Economist Intelligence Unit observed in its August 2017 publication; "*Botswana's sovereign risk rating remains at A, underpinned by a sizeable stock of foreign reserves that can be used for debt repayments and a narrowing budget deficit. However, the past relaxation of fiscal rules on the size of deficit and a concomitant risk of a spending overshoot could put the rating under pressure".*

43. The decline in Government's net worth, as a result of the drawdown of cash balances to finance budget deficits will also have negative implications on the ability of the country to absorb major external shocks and cushion the domestic economy in case of financial crisis. Therefore, in the event of the need to finance budget deficits by drawing down on government cash balances, there will be strict enforcement of current fiscal rules of withdrawals from the foreign exchange reserves to ensure the use of such funds are restricted to funding productive Government spending priorities that benefit the country's economic and social development in the long-term.

VI. SUMMARY CONCLUSION

44. While the global and domestic economic outlook underpinning the preparation of the 2018/2019 budget is generally positive, the country is still expected to run a budget deficit, due to continued slow growth in revenues and increased expenditure pressures. With the projected moderate growth in the domestic economy in the coming financial year, it is important that Government continues to focus attention on the implementation of initiatives to support strategies aimed at realising the goals set out for the NDP 11 national priority areas. Achieving the goals envisioned under the national priority areas will promote growth and employment creation.

45. Furthermore, there will be need for continued focus on prudent expenditure management, given the projected budget deficit in the next financial year. In this regard, Government will be closely monitoring expenditure during the financial year to ensure *value-for-money*. In particular, there will be strict application of the financial rules and regulations to avoid wastages in government expenditures such as cost overruns, change of project scopes and awarding of tenders without budget provision, among others.

46. In spite of the recent budget deficits, Government remains committed to fiscal sustainability in the medium to long term. Hence, the fiscal goal of maintaining a balanced budget in the medium term as indicated in NDP 11. In the short term, Government will be considering the following options to deal with expected budget deficit for the 2018/2019 financial year: re-prioritise the approved programmes and projects included in NDP 11; adopt measures to increase domestic revenue base; or a combination of the two measures to avoid the country falling into a fiscal unsustainable path. The preferred option would be to reign in on the country's expenditures in the medium term; failing which consideration will be given to enhanced measures to raise domestic revenues through measures such as adjustments in various tax rates, fees and licences, as well as review of subsidies across government. Additionally, Government will be intensifying its implementation of the cost recovery policy. These measures are necessary to avoid the country falling into a fiscal unsustainable path, thus, risking a negative rating from the sovereign rating agencies.