



WORLD BANK GROUP

AFRICA REGION, PRIVATE SECTOR UNIT

Summary of Botswana Investment Climate Assessment

Botswana has a reputation for excellent macroeconomic management, modest inflation, and extremely rapid growth. Other aspects of the Investment Climate also appear favorable. Firms complain little about many areas of the investment climate, such as regulation and infrastructure, and objective indicators usually confirm that Botswana compares favorably with other middle income economies in these respects. Although firms have concerns in other areas such as corruption, taxation, and macroeconomic instability, Botswana often compares favorably with other SACU economies and high performing middle income economies in these areas as well.

Despite having a relatively attractive investment climate, firms in Botswana are not highly competitive. Both labor productivity and total factor productivity are low compared to the best performing middle-income economies, few firms export, and domestic firms sell a large share of their output to the Government. Given that with a few exceptions—most notable worker skills and education—the investment climate appears favorable, this suggests that structural problems (e.g., the small size and remoteness of the economy and the macroeconomic effects of mining on the rest of the economy) probably play an important role in affecting the firm competitiveness.

The Botswana Investment Climate Assessment evaluates the investment climate in Botswana in all its operational dimensions to promote policies which will strengthen the private sector. The ICA uses two firm-level surveys covering small, medium, and large enterprises with 5 or more employees and microenterprises with fewer than 5 employees in the same sectors. Improving worker skills and education, improving tax administration, business licensing, and land allocation could help resolve Botswana's problems regarding evasion and informality.

Macroeconomic Framework

Despite being one of the poorest countries in the world at its independence in 1966, Botswana has grown very quickly since this. Although this is partly due to abundant natural resources (especially diamonds), good policies and strong institutions have played an important role. Most growth, however, has been heavily concentrated in the mining sector while manufacturing's share of GDP has declined modestly despite the government's concerted efforts to promote economic diversification.

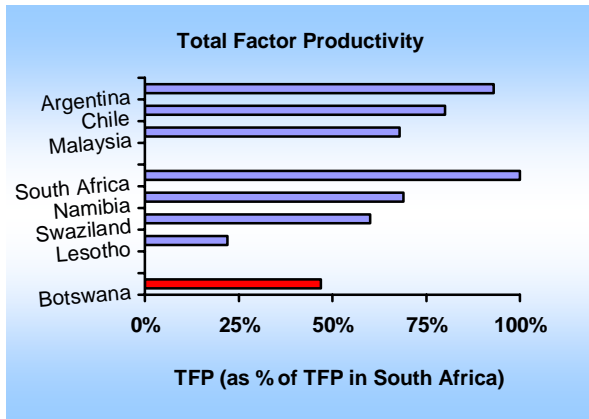
Firm Performance & Competitiveness

Productivity

Compared to other sub-Saharan countries, Botswana's firms are relatively

productive. Botswana's total factor productivity (TFP), which takes into account both labor and capital use, is higher than in all but three countries in sub-Saharan Africa – although it is considerably lower than in the best performing middle-income economies (e.g., Chile, Malaysia, and South Africa).





Unit labor costs (labor costs as a percent of value-added) are relatively low in Botswana. Because wages and productivity are both lower than in most of the middle-income comparator countries, firms could potentially remain competitive despite low labor productivity.

Exports

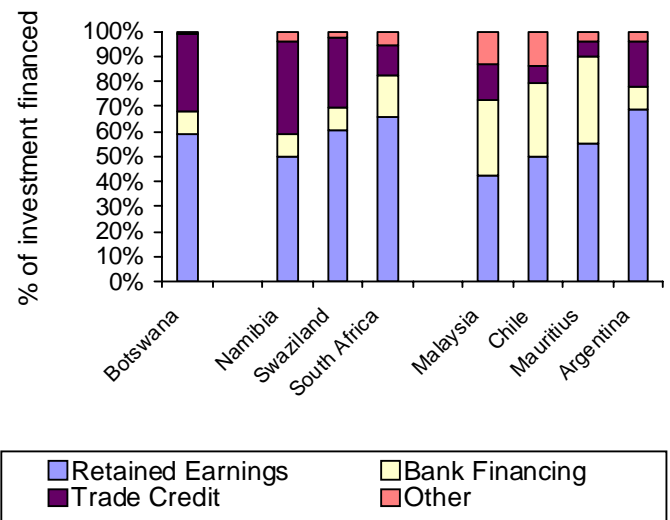
Because uncompetitive firms are often able to compete in domestic markets due to natural barriers (e.g., remoteness) and policy barriers (e.g., tariffs and quotas) to trade, the ability to compete on international markets is an important indicator of competitiveness. In this respect, enterprises in Botswana perform less well. Less than a quarter of manufacturing enterprises in Botswana export and, on average, exports account for only about 10 percent of output. This is lower than in any of the comparator countries.

Sales to the government, government agencies and state-owned enterprises are more important in Botswana than in other countries, and are, on average, more important to domestic firms than exports. Together these provide strong evidence that despite a favorable investment climate, firms do not appear to be highly competitive.

Key Investment Climate Constraints

Access to Finance

Across the board, irrespective of size or sector, enterprises cited access to finance as the most serious obstacle. Firms in Botswana finance about 10 percent of working capital through bank financing. Although this is similar to other countries in the region, it is lower than in Chile, Malaysia, and Mauritius which finance between 30 and 35 percent. Another aspect more specific to Botswana is the degree of government intervention in the sector. Firms are far more likely to have loans from the government than in any of the other SACU economies.



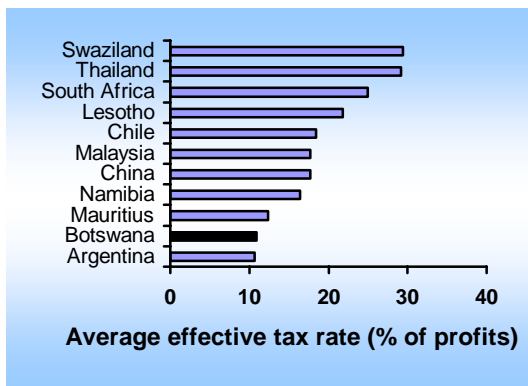
Macroeconomic Instability

Macroeconomic instability is perceived as the second most restrictive factor to the investment climate, despite Botswana's reputation for excellent macroeconomic management, modest inflation, and extremely rapid growth. The timing of the survey probably impacted the results, due to a burst of inflation at the time of the survey due to the devaluation of the pula.

Taxes

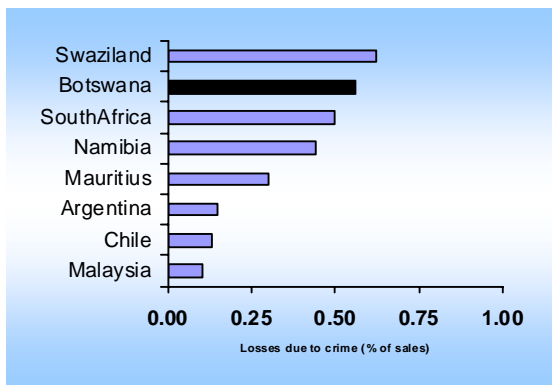
Tax rates typically rank among enterprises' greatest concerns in investment climate assessments. Botswana, however, is known for its favorable tax environment. The total company tax rates are lower than in most of the comparator countries, and broader measures of tax rates also suggest that the burden of taxation is low.

Complaints may thus stem from the fact that manufacturing firms receive preferential tax treatment, resulting in the perception that service enterprises carry an unfair burden. Despite low tax rates, non-compliance is a problem in Botswana relative to other middle-income economies.



Crime

Firms in Botswana rated crime, theft and disorder as the fourth most serious constraint. The direct costs of theft and



security are relatively high. The median firm reports that the combined cost of crime and security is about \$112 per worker per year or 0.6 percent of sales. The cost in US dollars is lower than in Namibia or South Africa, but is higher than in most of the middle income comparator countries.

Access to Land

Although the government of Botswana supported land market development and efficient use of land since independence, access to land is still a major impediment to private investment. Fewer firms own their own land in Botswana than in most of the middle-income comparator countries and firms were more likely to say that attempted purchases had failed.

Labor Skills

Manufacturing firms tend to be more concerned about skills shortages than firms in retail trade or other service sectors. To the extent that the government would like to diversify the economy towards manufacturing, workers skills and education might be a serious concern. One way that firms can deal with a skills shortage is to provide firm-based training; however, only 38% of manufacturing firms in Botswana provide training. This is fewer than in most of the comparator countries.

HIV/AIDS

HIV/AIDS has the potential to be a severe burden on the private sector in Botswana. Botswana has one of the highest rates of HIV infection in the world.

Both firms and the Government appear to have responded vigorously to the crisis. Botswana has the highest percentage of firms issuing HIV

prevention messages (65%), the highest providing anonymous HIV tests (20%), and the second highest distributing free condoms (38%). Moreover, according to data from UNAIDS, the Botswana government spends more on HIV/AIDS per worker than in any other surveyed African country.

Botswana’s low rate of absenteeism is therefore surprising, but this may reflect the strength of the national health sector in comparison to its neighbors, who tend to report higher worker absenteeism.

Informality

Many firms in Botswana are concerned about competition from the informal sector. Despite this, the evidence from the microenterprise survey suggests that informality is not particularly high in Botswana; almost all (97%) of the microenterprises reported being registered with at least one government agency, compared to only about 75% in other Sub-Saharan African countries. Because firms are likely to over-report their registration status, this might underestimate informality. However, this is also true in the comparator countries and so still suggests that informality is probably quite low.

One possible explanation is that tax

evasion appears to be relatively higher in Botswana than in other middle-income economies. That is, the concern might not be about informality as much as tax evasion by registered firms. Although registration does not seem to be the only issue, the Doing Business report suggests that registration procedures are quite burdensome. Reducing them might further reduce informality

Conclusions

- Competitiveness is an issue: few firms export, domestic firms rely heavily upon sales to the government, and productivity is low compared to other middle-income economies. As well as reflecting structural problems, this might also reflect problems with worker skills and education.
- The government has been active in promoting diversification, but domestic firms are heavily dependent upon the government for many services.
- Suggested areas for improvement include improving tax administration to reduce evasion, improving business licensing to reduce informality, and improving land allocation.

