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BOTSWANA: LAND OF PARADOXES

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Cover photo: Susan Anderson – Walking along the Main Mall in Gaborone, Botswana.
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BOTSWANA: LAND OF PARADOXES

SUSAN ANDERSON

EXECUTIVE SUMMARY

Botswana's successful use of natural resource wealth has made it a land of seeming paradoxes. It has a high level of government spending, yet a competitive business climate and a low tax burden. It is classified by the World Bank as an upper-middle income country, yet almost half of its population lives below the poverty line. These outwardly contradictory characteristics are in fact logical results of high levels of government involvement dependent on government-owned resources rather than taxes.

Estimates of falling diamond revenues in the near future mean that the paradoxes of Botswana are unsustainable in the long run. The government must align its spending more closely with tax revenues in order to reduce resource dependency and make the transition to a mature and more diverse economy.

Public sector reforms to date have focused on improving efficiency, not on reducing government size and scope. Privatization and economic diversification are recognized as important policy objectives, but very little has been accomplished in either area. We view the following implications as top priorities for Botswana's long term success:

- Government spending should be reduced to a level sustainable both economically and politically, through tax revenue. This step is crucial to ending resource dependency;
- Problems of poverty, unemployment, better health care, etc. are facilitated in the long run through the development of a growing economy that is not resource dependent; and,
- Diversification cannot be accomplished through government action. Re-focusing on privatization is an obvious and viable starting point in reforming the public sector.

In short, the current level of government involvement is unsustainable with diamond output expected to begin falling within the next 30-50 years, and thus public sector reform needs to be re-emphasized if Botswana is to continue to be economically successful.

BOTSWANA: LAND OF PARADOXES

INTRODUCTION

Botswana has enjoyed record levels of economic growth, and acclaim in the development world since its independence almost 40 years ago. The speed of economic development was made possible by the discovery of diamonds. Unlike other resource-rich countries, this discovery was accompanied by the development of good institutions and the goal of using the mining revenues to benefit all citizens of Botswana. This goal has been accomplished to a large degree, especially when compared with other African countries: education and health care are available to most of the population, clean water and electricity can be found throughout the country, and Botswana's income per capita is above that of most of its African neighbors.

However, because the government owns and controls many crucial assets – including all the diamond mines – it has attained a huge presence in the economy. This situation has created several seeming paradoxes within Botswana's economy. Government spending is extremely high – it accounts for almost half of Botswana's Gross Domestic Product (GDP), and yet taxes are very low. The level of national income ranks Botswana among upper-middle income countries, yet the country still suffers from many characteristically low-income country problems such

as high levels of poverty and unemployment. These paradoxes, allowed because of mining-funded government spending, are detrimental and untenable. The high level of government expenditure inhibits future economic development by perpetuating resource dependency. Now that diamond revenues have stabilized and are expected to decline within the next three to five decades, the current size and scope of the public sector is not only unsustainable, but also undesirable if Botswana is to make the switch to a more balanced and modern economy. Public-sector reform has taken a back seat to major issues such as the HIV/AIDS crisis, income inequality, and economic diversification, but needs to be re-emphasized if Botswana is to continue to be economically successful. The main points covered in this Country Brief are:

- Botswana's early success is largely attributable to an institutional structure created through National Development Plans (NDPs);
- Continued government involvement in the economy and high levels of spending have not burdened the population through taxation, but have perpetuated resource dependency; and,
- Diamond output is estimated to begin falling within the next fifty years and therefore the current situation is neither sustainable nor desirable.

ORGANIZATION OF THE COUNTRY BRIEF

This Country Brief presents an overview of the Botswana economy, assesses its strengths and weaknesses, and suggests directions for future reform. **Section 1** provides background on Botswana and a brief discussion of how good institutions led to a profitable partnership between the government and De Beers. **Section 2** discusses the issue of HIV/AIDS and its impact on policy and the economy. **Sections 3 and 4** focus on the large government presence in the economy, and the seeming paradoxes arising from high public spending and resource dependency. **Section 5** addresses the issue of economic diversification, which is seen by many as the answer to the problem of resource dependency. The conclusion revisits Botswana's paradoxes and suggests priorities for policy action.

1. BACKGROUND

BOTSWANA AS THE “GEM OF AFRICA”

As Botswana nears forty years of independence, there is much to reflect on and be proud of. The country has achieved remarkable development in a short time. Responsible handling of diamond revenues allowed Botswana to sustain the highest

growth rates in the world from 1966 - 1991, averaging 6.1% per annum and pushing per capita income from US\$660 to over US\$4,000 in 2003¹. In spite of persistent poverty in rural areas, the quality of life for almost everyone has improved: clean water, education, and access to health care are now available to over 90% of the population. Literacy rates have climbed from under 50% in the early 1970s to over 80% today.

Talking with Batswana (citizens of Botswana) who have seen the country's development first-hand, the anecdote most often told to illustrate the changes that have taken place is about the roads.² There were only six kilometers of tarred road in Botswana at its independence in 1966. Today there are over 6,000 kilometers of paved roads – over 50% of the total road network. Having driven on both paved and unpaved roads during field work in Botswana in June and July 2004, it was obvious why this story is so often told. The unpaved roads are often composed of soft sand, full of large rocks, and deeply rutted. Traveling on unpaved roads takes much longer and is a stressful experience. The anecdote captures well the idea of how much the quality of everyday life has improved for Batswana over the last forty years.

¹ World Bank, *World Development Indicators* 2004. All statistics in constant 1995 USD.

² All personal anecdotes are from two months of field work in Botswana in June-July 2004, sponsored by the Mercatus Center's Global Prosperity Initiative. We conducted 32 formal interviews with academics, current and former government officials, and business leaders; and over a dozen informal interviews around the country. One of the benefits of doing research in Botswana was being able to talk with people who were a part of Botswana's development from the very beginning. In many cases, the people we interviewed worked in the Protectorate Administration and were present at the Independence Ceremony.

GOOD INSTITUTIONS BEFORE DIAMOND DISCOVERIES

Botswana was a protectorate of the British empire until 1966. When it was granted independence, the first item on the agenda of the new government was to lay out a plan for development. The country's leaders had very little to work with. The country was so poor that the British Government Economic Survey Mission of 1960 portrayed Botswana as a country "close to being the world's poorest," having "dismal economic prospects based on vague hopes of agriculture, salt and coal." The government could not even meet its meager recurrent budget, and the country's future appeared to hinge on foreign aid. It was against this background that the government was structured and plans for development were formed.

National Development Plans (NDPs) are six year plans which project expected revenues and priorities for expenditure of those revenues. The planning process itself is kept in check by fiscal controls which strictly allow funding only for projects within the plan. NDPs were in place before independence was officially declared, because of the need for multi-year financial assistance from the British government. The transparency and success of these plans was reinforced as these qualities attracted foreign aid from other donors from around the world. When diamonds were discovered in 1967, revenues freed the government from reliance on foreign aid, but NDPs continued to limit and direct government spending.

National planning was a big part of development

economics in the 1960s and 70s, and many African countries had development plans in place at their independence. Botswana's National Development Plans are unique in that they were used to *constrain* government as much as to enable it. This contradiction of planning explains a large part of the success of the country in using natural resources to aid development. Initially these plans prevented the otherwise likely corruption and predation, and provided some institutional certainty for foreign investors and donors. However, as we will see later, while National Development Plans helped prevent the government from making bad decisions in the early stages of development, they did not place overall limits on government spending or involvement. As a result, escalating diamond revenues led to expanding government involvement even as development projects became less urgent. Over-involvement by the government in the economy has put Botswana in a precarious position.

DIAMONDS FOR DEVELOPMENT

Other institutions which served to restrain predation by the government were formed by the need for foreign investment to successfully mine the diamonds. In Botswana diamonds are extracted from kimberlite pipes, and this requires expensive equipment and technical expertise, which meant the diamonds could not be mined successfully without foreign investment. Initially investors like De Beers faced considerable risk by counting on the fact that the host government would adhere to consistent policies over time, not changing taxes, regulations or nationalizing operations.



Currently all diamonds are mined and marketed through Debswana, an equal partnership between De Beers and the government of Botswana.

In 1967 Botswana had a brand new government, and no substantial mineral operation or infrastructure. In order to persuade De Beers to invest, Botswana's political leadership had to make a credible commitment in the form of good political institutions and mineral policy. The government of Botswana faced a trade-off between claiming a significant portion of the revenues and providing incentives for private investment. The result was a profit-sharing arrangement³ which gave both parties a stake in the continuing success of mining operations.

The arrangement has proved extremely profitable for both parties. The last and biggest mine became operational in 1982 at Jwaneng, and rev-

enues from diamond mining are just now beginning to level off. These revenues, in addition to royalties and taxes from the diamond industry, have remained the largest contributor to the economy. Minerals currently account for about 35% of GDP, and roughly 55% of annual government revenue. Figure 1 (below) shows the sources of government revenue in 2001-02, of which mineral revenues account for 55.06% directly and another 5 – 6% indirectly through export duties, fees and interest on foreign exchange reserves.

LAND OF PARADOXES

Sustained high levels of economic growth and a stable partnership between the government and a foreign investor is an unusual story for a develop-

³ Currently all diamonds are mined and marketed through this partnership, called Debswana. Originally ownership of profits was split 15% to the Botswana government and 85% to De Beers. This was renegotiated to an equal partnership after the second diamond discovery.

ing country rich in natural resources. Typically countries with large resource deposits are characterized by economic stagnation and political turmoil. This phenomenon is so common it has been labeled the “natural resource curse” – countries rich in natural resources such as gold, diamonds, or oil tend to experience growth rates far below nations lacking natural resources.⁴

Recent studies of the natural resource curse have also focused on the fact that countries with natural resource wealth are not forced to develop strong institutions such as the rule of law, because wealth can be generated without their presence.⁵ Botswana is a contradiction to all of these curses, boasting both a wealth of natural resources and a high level of economic growth, a stable government, and a solid institutional framework.

Because resource-rich countries rarely get past the first step of successfully exploiting the resource, it is easy to overlook the long run significance of resource-funded government spending. Government expenditure based on collection of natural resource revenues is akin to government spending based on foreign aid, only on a much

larger scale.⁶ Botswana is more like a country dependent on foreign aid than a “normal” economy. Although the national income and scale of government spending puts Botswana in a category with other middle-income countries, its economy is still dependent on diamond revenues.

This is the most significant paradox of Botswana: high spending and low taxes.⁷ The economic, political and social dynamic of the country ultimately revolves around this incongruity where Botswana get government largess without paying for it. The level of spending is not sustainable, and the long-run will largely depend on the way this paradox evolves and is addressed in public policy.

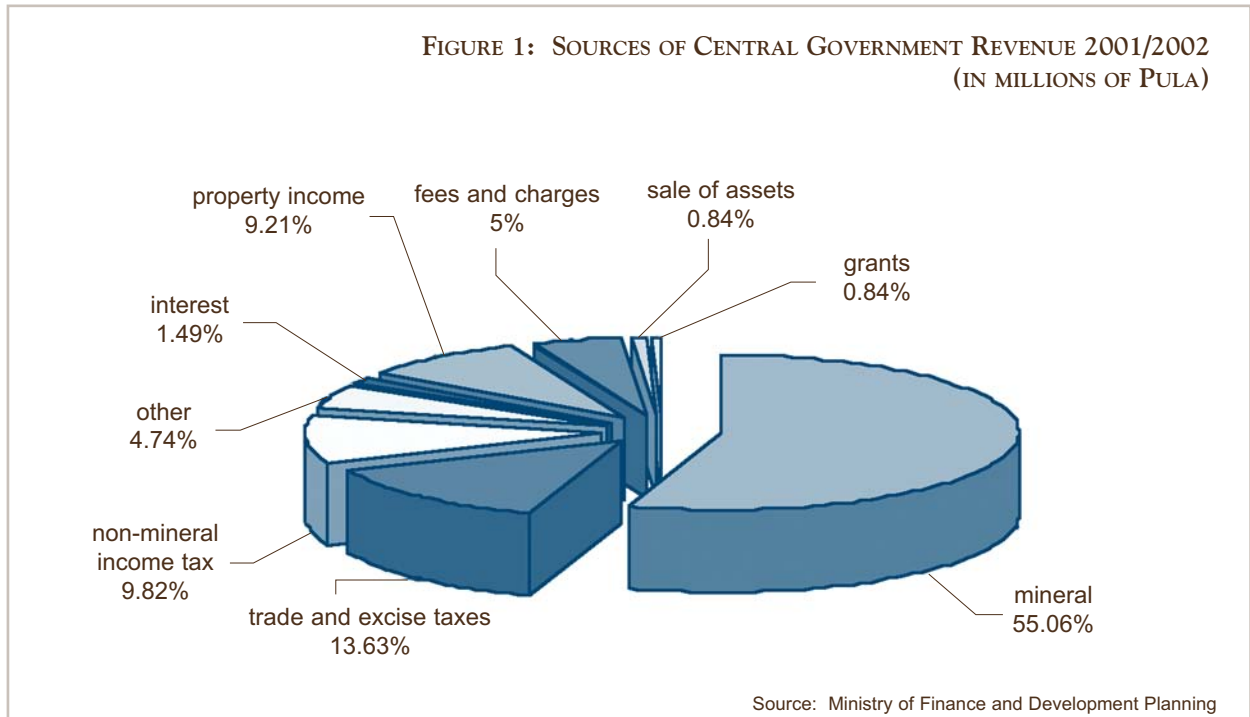
The only way to resolve this paradox in the long run is by reducing the size and scope of the government to what can be supported by non-mining revenues. Making public sector reforms will not be easy, in part because of the effect this economic paradox has undoubtedly had on Botswana’s politics. Botswana’s history does not include the political strife and civil unrest that characterized surrounding sub-Saharan countries, and the most

⁴ The first and foremost paper on the natural resource curse is Sachs, J. D., and A.M. Warner, 1995, “Natural Resource Abundance and Economic Growth,” *Development Discussion Paper No. 517a*, Harvard Institute for International Development, Cambridge, MA.

⁵ See Daron Acemoglu, Simon Johnson and James Robinson “The Colonial Origins of Comparative Development: An Empirical Investigation,” *American Economic Review*, December 2001, volume 91, pp. 1369-1401, and (same authors) “An African Success Story: Botswana” in *In Search of Prosperity: Analytical Narrative on Economic Growth*, edited by Dani Rodrik, Princeton University Press. 2003.

⁶ Revenue for the 2002/03 budget was P14.42 billion (US\$2.85 billion), 46% coming from minerals.

⁷ Income, sales and property taxes accounted for 17.34% of government revenue in 2001-2002. To contrast, US personal income taxes alone made up almost half of government revenue.



recent elections in October 2004 continued to reinforce the political stability of the country.

The Botswana Democratic Party (BDP) has kept the majority position since independence, and under this party's leadership have come improvements in education, health care, infrastructure, and other government services at little or no cost to taxpayers. In July 2004, three months before the elections, we interviewed a candidate of the Botswana Congressional Party (BCP) running for office in Gaborone. His objections to the leadership of the BDP were typical of opposition parties, based on criticism of government programs for not doing enough.

Cutting government spending will not be easy politically - it is hard enough to get elected as a member of an opposition party, why campaign on

reduction of government benefits when there are no constituents being taxed to pay for them?

Given the background of Botswana's development, the following sections focus on examining current and future challenges. HIV/AIDS, as the most visible and urgent problem, is considered first.

2. HIV/AIDS AND IMPLICATIONS FOR ECONOMIC DEVELOPMENT

Botswana is full of volunteers from all over the world who have come to help in AIDS clinics. Many international HIV/AIDS conferences are held in Gaborone, and representatives from private foreign donors, like Merck & Co., Inc. and the Bill and Melinda Gates Foundation, maintain a presence. Living in Gaborone, reminders of the

problem are everywhere – billboards advertising condoms or preaching abstinence and faithfulness, advertisements and posters proclaiming HIV/AIDS support group meetings, and free condom dispensers in almost every government building. Even in more remote areas, billboards proclaim the ABCs of AIDS prevention.⁸

Until 1998, 13 years after the first case of HIV and AIDS was reported in Botswana, there was no coherent national response to the AIDS epidemic. Other than a few early corporate programs, most notably Debswana's, the response was centered on overall health and had limited impact. The United Nations Development Program (UNDP) became involved in 1998, and in 1999 the National AIDS Coordinating Agency (NACA) was created. Where National Development Plan 7 basically ignored AIDS, National Development Plan 8 labeled it a national emergency. Domestic spending on AIDS has increased at an average rate of 162% each year to more than US\$80 million in 2003/2004.

INCONSISTENCIES SURROUND THE BOTSWANA AIDS CRISIS

The United Nations AIDS project prevalence rates for Botswana are the world's highest, which explains the urgency and huge amounts being spent by the government. Life expectancy has

been reduced drastically over the last two decades, from 67 to 38 years,⁹ and estimates of HIV prevalence range as high as 38.5% for the 15 - 49 age group. Yet despite the amount of attention and money being spent on AIDS education and treatment in Botswana, prevalence rates have not dropped (see figure 2). Neither have the expected economic effects of the epidemic surfaced.

In 2001 the IMF released a study entitled *The Macroeconomic Impact of HIV/AIDS in Botswana*,¹⁰ which details the expected economic consequences of the AIDS epidemic. The study projects that by 2010 the economy will be a third smaller than it would have been without the AIDS epidemic. Other effects include an increase in the number of households living below the poverty line, rising deficits, and increasing wages. Yet indicators such as GDP, wages, and poverty levels have remained constant. If life expectancy truly has dropped below 40 years, we should see significant drops in population as well as shifts in macroeconomic indicators.

In addition, there has been no evidence of changes in behavior. This is not consistent with a 30 year reduction in life expectancy. Education programs appear to be having little impact on estimates, but there is no way to tell which programs are working and which are not.

⁸ The ABCs of AIDS prevention – Abstinence, Be faithful, Condomize – was one of the first efforts to educate the public about the disease.

⁹ World Development Indicators 2004.

¹⁰ Available from: <<http://imf.org/external/pubs/cat/longres.cfm?sk=15138.0>>.



Advertisements like this one are a common sight in the cities of Botswana. Education has been one of the key strategies of the government in fighting the HIV/AIDS problem (photo by Phyllis Puffer).

WHY AREN'T THE NUMBERS ADDING UP?

Sustained high prevalence rates have had no observable effect on the overall economy, despite dire predictions. This may be the case because:

- Economic indicators are incorrect (or incapable of capturing the effects of the epidemic); and/or,
- Prevalence rates are incorrect.

The IMF (2001) report draws on a growing literature of predictions on the economic impact of HIV/AIDS, ranging from drops in GDP growth and labor productivity, to rising budget deficits. But there may be good reasons why the economic impact of the disease is not more evident. The impact of AIDS on Botswana's *overall* economic performance is not expected to be large because labor intensive sectors of the economy such as agriculture and industry do not make up a large percentage of GDP. Mining, which comprises about 70% of GDP, employs only 3% of the work-

force (roughly 6,000 people).

Another reason the impact of AIDS may be missed in Botswana is the small and largely rural population. With only 1.7 million people - a quarter of whom are unemployed, and government income that is not dependent on a tax base, it is possible that the overall economy would not be affected by a declining population. Similarly, the large budget deficits that are predicted may not occur. The level of health spending could be countered by the reduction in social spending on a smaller population.

Reasons why infection rates may be overestimated might include:

- Problems with testing and estimation techniques; and,
- Problems of incentives.

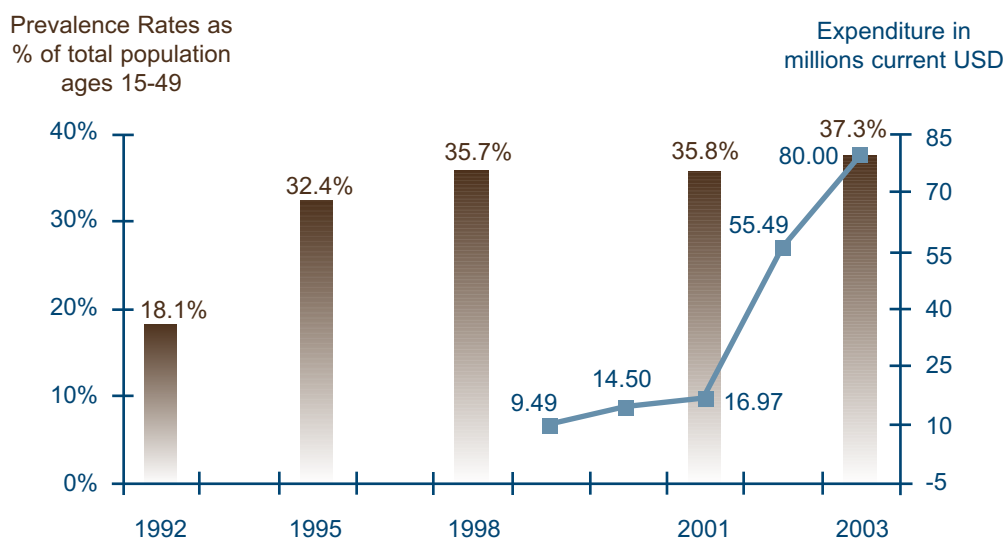
Although Botswana is pouring more money into

the AIDS battle, and has a more coherent national response than any other African country, there is still a problem both in gathering accurate results, and in diagnosing and administering treatment. Estimations of infection and prevalence rates in Botswana are generated through sentinel surveys – surveys which use anonymous testing of samples of pregnant women attending prenatal clinics. Prevalence and infection rates are estimated by combining the data above with information from household surveys and information on AIDS transmission in order to come up with rates for the entire population.

Quality of estimation techniques is continually being improved, and it is interesting to note that access to better data and better estimation software have consistently led to a lowering of current and previous rates.¹¹ In December 2004, results from the latest household survey of 14,000 people reported a much lower HIV prevalence rate than earlier surveys. Results from the 2004 Botswana AIDS Impact Survey II (BAIS II), conducted by the National AIDS Coordination Agency (NACA), showed an infection rate of 17.3%.¹²

This result has not been widely publicized or

FIGURE 2: HIV PREVALENCE RATES AND EXPENDITURE ON HIV/AIDS PROGRAMS



Source: UNAIDS 2004. IMF 2003

¹¹ <<http://www.unaids.org/Unaid/EN/Resources/Epidemiology/How+do+UNAIDS+WHO+arrive+at+estimates/>>.

¹² Daily News Online, December 24, 2004. "AIDS survey results differ with others":

<http://www.gov.bw/cgi-bin/news.cgi?d=20041224&i=AIDS_survey_results_differ_with_others>.

accepted. UNAIDS stated that national surveys such as the BAIS II are not necessarily a better measurement of HIV prevalence than the sentinel surveys of pregnant women currently being used.¹³ Whether or not these survey results are an accurate picture of reality will be revealed through the program of routine HIV testing which was instituted in all health clinics by the end of 2004. Before those who asked to be tested would; now everyone is tested (though individuals are allowed to opt out). If substantiated, the significantly lower prevalence rate indicated by the NACA survey may be the explanation for the paradox of high prevalence rates and few economic effects.

As in any situation where large amounts of public money are involved, the incentives can lead to problems of exaggeration. The Copenhagen Consensus¹⁴ recently named the fight against HIV/AIDS as the world's number one priority, urging that the necessary spending (US\$27 billion) would yield even higher value in human life. Botswana has been able to attract a large amount of foreign aid both because of its high prevalence rates, and the government's commitment to action. The current amount of foreign aid spent on HIV/AIDS in Botswana is estimated to be \$96 million,¹⁵ and it is not unreasonable to

suggest that those measuring will either get more money or prestige the higher the figures.

Overall, the difficulties in accurately measuring the real threat, the incentives to exaggerate prevalence rates, and the failure of economic indicators to capture the effects of AIDS may all be reasons we have not yet seen the predicted economic consequences of AIDS in Botswana. More accurate measurements are imperative for gauging the true impact of this disease, and learning the best ways to fight it.

Because AIDS is a national and international priority, we expect major improvements to continue. Steps have been taken to improve organization and communication between programs, and in 2004 routine testing for HIV was implemented. The main issue should be to focus on continuing to improve the quality of information, both in terms of actual rates and the success of specific programs. With this information, money can be directed in the most effective ways to battle the disease.

3. BIG GOVERNMENT PRESENCE

HAS BOTSWANA ESCAPED THE RESOURCE CURSE?

Whether or not Botswana could have grown as

¹³ Norway's Afrol News, December 20, 2004. "Botswana HIV rate at 17, not 40 percent": <http://www.afrol.com/articles/15067>.

¹⁴ Some of the world's greatest economists gathered to prioritizing action on some of the biggest challenges in the world. See <http://www.copenhagenconsensus.com>.

¹⁵ More information on how the HIV/AIDS programs are being financed, along with helpful tables and graphs, can be found in *A Comparative Analysis of the Financing of HIV AIDS Programmes in Botswana, Lesotho, Mozambique, South Africa, Swaziland and Zimbabwe* (from the Research Programme on the Social Aspects of HIV/AIDS and Health) which can be downloaded for free at: <http://www.hsrbpublishers.co.za/index.html?finance.html~content>.

ECONOMIC FREEDOM INDICES

Botswana's overall ranking is 18th in the Cato and Fraser Institute's *Economic Freedom of the World* 2004, and 37th in the Heritage Foundation/Wall Street Journal *Index of Economic Freedom* 2005. The score in both indices has risen over the years.

This is remarkable because over those same years, government presence in Botswana has grown. Botswana scores high overall because strong numbers in many areas, such as business regulation and taxes, override low numbers in the areas that specifically measure government size and scope.

The freedom rankings in each area represent a static observation, not a trend. As a result, the indices correctly capture Botswana's stability and friendly business climate, as well as the large government presence. But they do not take into account the inconsistency of big government - low taxes over time, and therefore may underestimate future problems.

The freedom indices are extremely useful, but like other aggregate indicators, they are a snapshot of the situation, and should not take the place of deeper analysis.

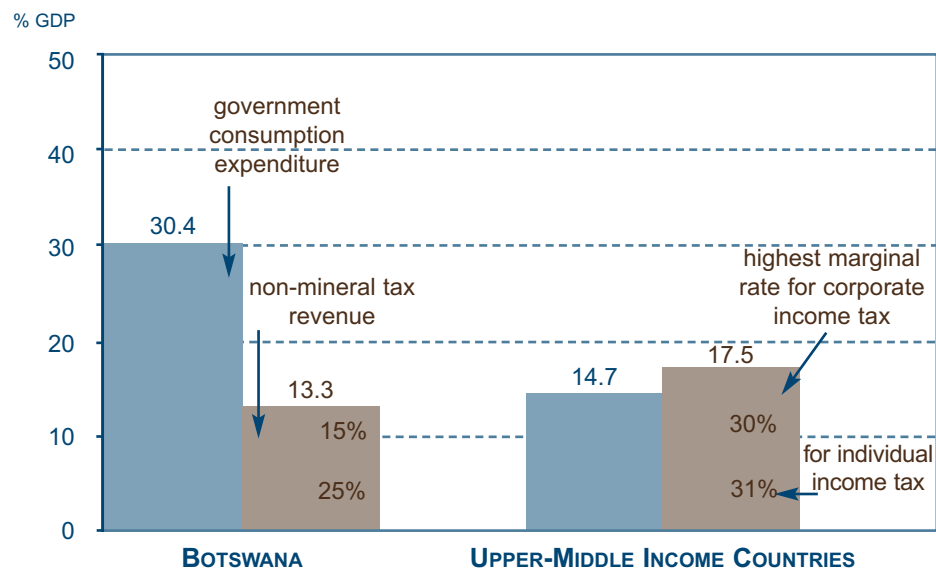
rapidly as it did with less government involvement is unknown. But an unintended consequence of the rapid development is that Botswana today is weighted with a huge and pervasive government. Macroeconomic data indicate a significant dependence upon government spending. Government expenditure accounts for over half of GDP, and over 65% of the total national revenue collected for that expenditure comes from state-owned enterprises and government ownership of property. An estimated 43% of the labor force works in the public sector. This number includes those working for central or local government, or for parastatals,¹⁶ and this is

only the number *directly* employed. Government spending on construction, maintenance and government activities provides work for many private sector employees. Local businessmen in the capital of Gaborone told us that doing business means doing business with government. Even small businesses depend on government contracts: cleaning services clean government buildings; mechanics work on government cars; newspapers run government ads, etc.

Concern about government domination of the economy is not a new issue. There have been several reports in recent years that mentioned the

¹⁶ As defined by USAID, a parastatal is a business owned and controlled by government.

FIGURE 3: GOVERNMENT CONSUMPTION SPENDING AND TAX REVENUE (% OF GDP), 2000



Source: World Development Indicators, 2003

dubious sustainability of the size and structure of the public sector in Botswana. The 1997 World Bank World Development Report and a 2000 report by the Royal Norwegian Ministry of Foreign Affairs¹⁷ (with the Botswana Institute for Development and Policy Analysis – BIDPA) both examined the problem of government size. It was found in these reports that government agencies were fulfilling roles that could easily, and in many cases more effectively, be performed by the private sector.

Strong government involvement in economic

activities was perceived as necessary for development in the early years, but the situation of the economy is presently very different from what it was 35 years ago. There is no economic justification, for example, for continued government involvement in the provision of goods and services such as urban housing, cleaning services, or food services. The financial sector has also developed, reducing the need for government lending.

These concerns are also well known to the government. National Development Plan 8 declared that the “current size and structure of the public sector

¹⁷ “Making Government Smaller and More Efficient: The Botswana Case”.

are not sustainable and measures will be put in place to ‘right-size’ and rationalize the public sector,” and the government has included within its national strategy the need for privatization and decentralization. Efforts to divest the parastatals have been a relative achievement, but privatization has been uncoordinated and unsuccessful. A recent BIDPA study¹⁸ showed that despite lip service to public sector reform, the size and scope of government activities have remain unchanged. In practice, most reform has centered on making the public sector more efficient, and not necessarily reducing government presence.

What has not been emphasized as a motivation for shrinking the public sector is the paradox of large government presence and low taxes. As mentioned above, there is a sense that many government services provided are free, because the revenue does not come from taxation: for most Botswana, services are provided by third party payment. A decline in diamond revenues will mean the government will have to either drastically cut the amount of services provided, run large deficits, or increase taxes.

If the tax base – the private sector – does not grow, this will be a serious economic and political problem. Figure 3 shows the difference between tax revenue and government consumption spending in Botswana compared with the average for all upper-middle income countries.

¹⁸ BIDPA Briefing. “Public Sector Reforms” July 2004.

VISION 2016

A good illustration of the fact that the role of government is far from being reduced is the pursuit of Vision 2016. In 1996 a government task force assessed the development accomplishments of the past and constructed a vision for Botswana at its 50th birthday.

The Vision 2016 project is a comprehensive “national manifesto” encompassing political, economic and social goals. The Vision includes rather utopian goals like, “an educated and informed nation,” where “income will be distributed equitably,” and “violent crime will have been eliminated.” The Vision also includes even less policy prescriptive aims such as, “Botswana will be a hard working and disciplined people with a diversified economy,” and “Botswana will be a moral and tolerant nation.”

Evidence of Vision 2016 is all around Gaborone. Calendars, posters, and thick booklets can be found in most government and parastatal offices. The official goals of the program – to be a moral and tolerant nation; to be a safe and secure nation; to be an educated and informed nation; a prosperous, productive, innovative nation; a caring and compassionate nation – are admirable, but the underlying message calls for increasing public sector involvement. It is no wonder that efforts to reduce government involvement have been lackluster, if at the same time public sector



The town of Gweta

agencies are encouraged to play their part in working towards an “ideal nation”.

POVERTY REDUCTION

Most criticisms of Botswana’s development focus on income inequality. While incomes have increased for a large part of the population, many still live in poverty. According to the UNDP, 47% of the population is below the national poverty line,¹⁹ and the standard measure of income inequality is one of the highest in the world.²⁰ The majority of those living below the poverty line are in rural areas, and recent rising levels of migration to cities and towns have prompted policy makers to take action.

Basic services like health care and education have been made available to a majority of the population. Nevertheless, Botswana is under pressure to reduce the income inequality, and raise the standard of living of the rural poor, despite the fact that extending infrastructure and services becomes more expensive the more remote the area. The main initiative currently being implemented in Botswana as part of National Development Plan 9 is the National Strategy for Poverty Reduction (NSPR). The strategy includes bringing more services to remote areas, by subsidizing farming, digging bore holes for water, and increasing availability of telecommunications.

¹⁹ The poverty line is not an objective standard, but is set by the government according to six classes: food, clothing, personal items, household goods, shelter and miscellaneous items. National estimates are based on population-weighted subgroup estimates from household surveys: 50% of median income-50% of the median adjusted household disposable income.

²⁰ The Gini coefficient in Botswana is 0.6. However, there are many issues with the Gini coefficient as a true measure of inequality, as it is a relative measure.

According to the World Bank, 97% of the 47% of the population living below the poverty line lives in rural areas. Traveling through the vast emptiness between towns in Botswana, we wondered at the cost of getting any services at all to these rural areas. The immense cost of bringing equal quality of life to citizens in rural areas is enormous, and would penalize those who choose to live in more concentrated areas. When funding for programs like this has to come from taxpayers, the real cost will become more apparent, and programs may be short-lived.

The problem of poverty is a long standing one in Africa. The fact that poverty in rural areas has persisted while the overall economy has grown significantly is another illustration of Botswana's

resource dependency, and simply expanding the amount of government services available will not bring people above the poverty line. In mature economies, wealth creation is a private matter, while redistribution is a public concern.

Inequality in Botswana is mainly a function of the cost of *distribution* of diamond revenues. Bringing services to areas farther away and less dense in population has a higher cost, and benefits fewer people. The best way to alleviate poverty in the long run is to concentrate on the growth of the private sector, and develop a solid and sustainable economy. Poverty alleviation programs should not be eliminated, but serious consideration needs to be given to their true costs, benefits, and sustainability.

DIAMONDS AREN'T FOREVER...

Diamond revenues have leveled off, and are estimated to remain at current levels until at least 2030. Economic diversification efforts have been increasing in importance with this deadline in mind.

DeBeers has kept the world diamond market relatively stable, and by keeping a large amount in foreign reserves, Botswana has been able to ride out slumps in world demand.

But things might be changing. Competition in the diamond market, and the prospect of higher quality synthetic diamonds could have a dramatic impact on world demand. Although the government renewed its Jwaneng contract with DeBeers after extended negotiations, there are signs that the cartel's hold might be weakening.

The official stance of Botswana, as related by the head of public relations, is not to worry about it. But the growing uncertainty associated with the diamond market is another reason for the government to hasten movement away from dependence on diamond revenues.

4. THE GOVERNMENT INVOLVEMENT IN DAILY LIFE

Beyond the issue of GDP growth rates and public sector efficiency are more ominous problems associated with a large government presence. A public sector so intertwined with daily life can have more than just economic effects. With government revenues based on diamond revenues instead of taxes, along with the initial absence of any private enterprise, capital or infrastructure, the government of Botswana has filled a role in

nearly every social and economic activity at one time or another.

Today the government provides social security, free education,²¹ and subsidized water, electricity, and health care. The government owns the country's telecommunications provider, the national airline, and half of the largest contributor to the economy – Debswana. The government heavily subsidizes agriculture, tourism, and “citizen entrepreneurship”. Figure 4 (below) illustrates that government spending on social services has continued to grow.

**FIGURE 4: GOVERNMENT EXPENDITURE FOR NDP8,
MINISTRIES PROVIDING SOCIAL SERVICES**

(Pula millions, 1997/98 prices)	98/99	99/00	00/01	01/02	02/03
EDUCATION	1,273	1,351	1,433	1,520	1,613
LOCAL GOVERNMENT, LANDS & HOUSING	1,042	1,105	1,171	1,241	1,316
WORKS, TRANSPORT & COMMUNICATIONS	484	509	535	563	592
HEALTH	333	359	388	419	452
AGRICULTURE	251	253	254	255	256
LABOUR & HOME AFFAIRS	126	133	139	146	154
MINERAL RESOURCES & WATER AFFAIRS	111	117	123	130	137
Source: Ministry of Finance and Development Planning					

²¹ Dr. Patricia Makepe, a professor at the University of Botswana, explained the education system to us. Higher levels of education continue to be free for those who are able to pass to the next level. Dr. Makepe attended the University of Botswana and her doctorate from the Michigan State University was also paid for by the government in exchange for returning to teach at the University of Botswana. Education is generally seen as a way of returning diamond revenues to the people of Botswana.

WATER

Rural water rates are determined by the central government and implemented by district councils. They are uniform throughout the country, despite the variation of supply costs in different places. Urban water tariffs are generally higher than rural rates regardless of the lower supply costs in order to cross-subsidize rural use, and are determined by the Water Utilities Corporation subject to approval by the central government. Even in urban areas, the current subsidies keep the price of water at an artificially low level.

LAND

A related issue is the government control of land allocation. In traditional tribal life in Botswana, chiefs were in charge of dispersing land within their jurisdictions, typically with each male head of household entitled to three plots of land. In 1968, The Tribal Land Act assigned these powers to Land Boards, and since 1992 this has been administered under the Department of Lands.

The Department develops a land allocation policy and administers allocation of state land. This not only creates the attitude that land ownership is a right bestowed by the government, but provides opportunities for corruption. While we were living in Gaborone, newspapers featured stories on an ongoing land scandal. We spoke with an employee at the University of Botswana who had been waiting for 2 years to receive his plot of land, and spoke bitterly of richer, better connected people receiving their plots.

Currently about 23% of land is still owned by the state. The manner in which it is distributed, and the property rights conferred vary by case according to the Department of Lands regulations.

NEGATIVE BARRIERS TO (CITIZEN) ENTREPRENEURSHIP

The government, in its effort to reduce unemployment and diversify the economy, has gone to amazing lengths to encourage local business and entrepreneurship. The Financial Assistance Policy, which gave subsidized loans to businesses for the first 2 - 5 years in order to encourage new investment and entrepreneurship, was ended in 2001, when it was discovered that companies would come in, and then leave once the subsidy was over.

CEDA (the Citizen Entrepreneurial Development Agency) replaced the FAP, but it too already appears to be suffering from a lack of quality clients and unpaid loans. Speaking with the branch manager of the CEDA office in Selebi-Phikwe (Botswana's third largest city), we found that the busiest area of the office was collections. This is an indication that the government finances businesses which shouldn't be in business.

XENOPHOBIA

Botswana does not have an official policy on immigration, but lately has been tightening restrictions, the most obvious sign of which is a new 500 km electric fence on the Zimbabwean border. The government has also beefed up



CEDA loans make small businesses possible, like this private pay phone.

exclusion measures and strengthened punishments for illegal immigrants. Critics worry that this type of policy is encouraging attitudes hostile towards non-citizens.

This attitude is a relatively recent phenomenon – in fact Botswana’s history is one of the few in sub-Saharan Africa that does not include a period of violent nationalism. Yet a 2001 Southern African Migration Project (SAMP)/University of Botswana survey showed that more than 20% of respondents were in favor of deporting all immigrants from Botswana, and 71% would deport all immigrants “not contributing to the economy.” These attitudes are normal in a country with a high level of social services and a new influx of immigrants. Especially considering circumstances in Zimbabwe, immigration is expected to increase, and if a coherent and less protectionist policy is not made official, xenophobic attitudes will increase even further.

Recognition of this problem is especially important in light of the AIDS crisis as Botswana offers a higher level of care (including free Anti Retro Viral (ARV) treatment) to AIDS victims than any of the surrounding African countries. Immigration and xenophobia can also have an effect on the attractiveness of the country to foreign investors. A growing population would encourage investment by offering a greater supply of labor and a larger domestic market. Increasing xenophobia and restrictions on property ownership and employment will only drive away foreign investors.

EFFECT ON CULTURE

Alec Campbell, former member of the Protectorate government and Khama and Masire administrations, National Museum curator, and co-author of *History of Botswana*, has seen the development of Botswana take place during his lifetime. He talked with us about the gap between

the older generation, who remember life before diamond revenues, saving up to survive droughts, and extreme hardship; and the younger generation of Botswana, who live with less responsibility, and do not remember what it is like to live without schools, cars, or shopping malls. In particular there is a concern about the younger generation turning to government, rather than themselves, for a solution to problems.

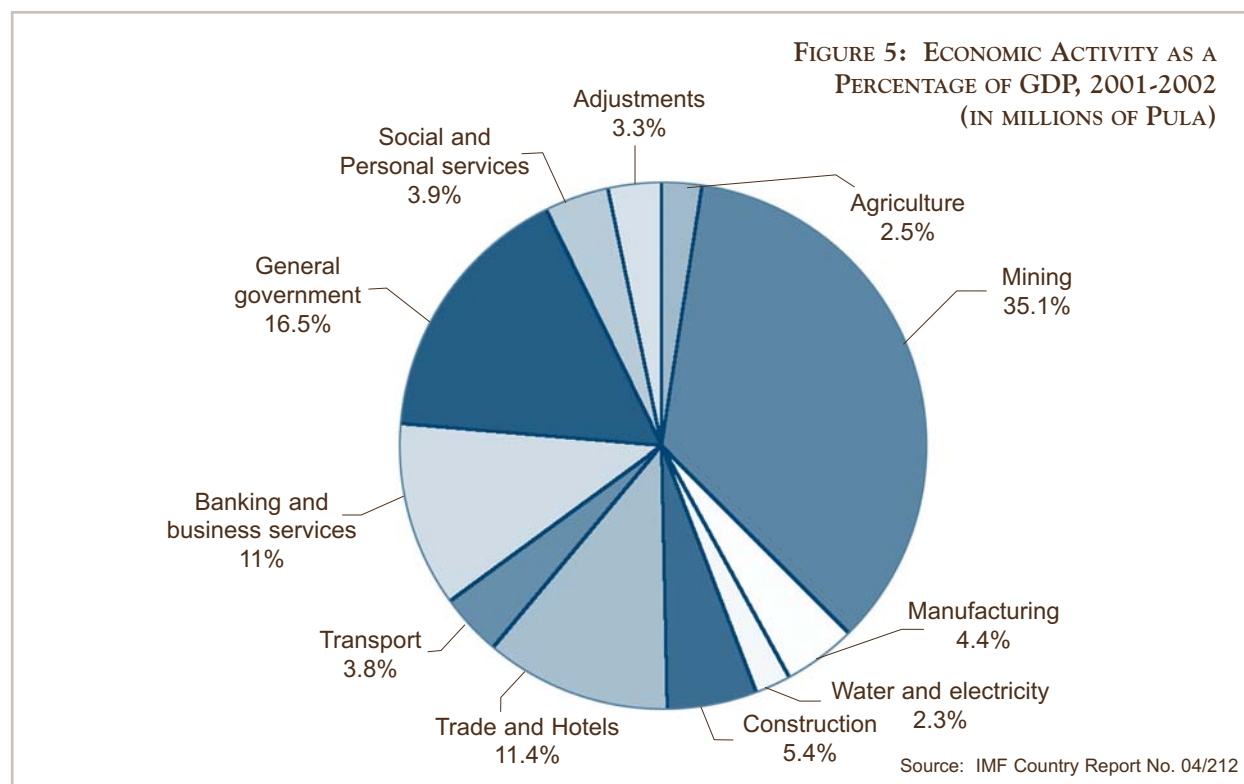
5. ECONOMIC DIVERSIFICATION

From bank officials to government ministers to businessmen to people on the street, when asked what needs to be done to ensure Botswana's continued success, "economic diversification" is the phrase on everyone's lips. It is not a new idea. It has always been accepted that diamond revenues

would not last forever, and efforts have been made to encourage non-mining industry and foreign direct investment for many years.

Subsidies for manufacturing, citizen entrepreneurship programs, and exchange rate policy are examples of efforts to diversify the economy. These have met with mixed success.

Private investment and business *have* increased enough to equal the growth of mining over the years. An interview with Keith Jefferies, deputy governor of the Bank of Botswana explained that, "Clearly the economy hasn't diversified in the last 10 years, [but] mineral sector growth over the last decade has averaged about 6% a year, and the fact that relative shares have not changed means that the other shares of the economy have also been



growing at 6%, and that is quite good.” He went on to say that this may not be as good as it sounds because much of the non-mining sector is dependent on government spending, or the spending of government employees.

Figure 5 depicts an economy that is not completely resource dependent, but which has 40% of its labor force employed in the public sector.

Although official policy emphasizes encouraging the private sector, not much has been accomplished. Parastatals have been made more independent, but still rely heavily on government funding. Both Air Botswana and the Botswana Telecommunications Corporation (BTC) were up for privatization at different times but this has been put off. President Festus Mogae has publicly endorsed the idea to privatize water utilities as “the only way to provide adequate water to all” but no concrete plans have been introduced.

Botswana does have certain unalterable features that will slow diversification efforts down – it is a land-locked country, dependent on imports, and offers a small domestic market. The country also has many institutional strengths – low corruption, strong rule of law, and political stability. The government has made a significant effort to make the country an attractive place to do business with low corporate taxes. The major issue here is that “diversification” should be seen as a measure of success and not an end in itself.

The current emphasis on diversification has led the government to help finance a manufacturing industry, and to consider expanding the domestic diamond industry (into cutting, polishing, etc). The emphasis on balancing the source of revenue should not hide the real problem, which is a high level of government spending reliant on an unsustainable revenue source.

What is needed to sustain Botswana’s impressive growth rates is privatization and reduced government involvement in the economy. If this happens, diversification will follow. There needs to be less emphasis on encouraging diversification through government action (i.e. providing subsidies and tax incentives), and more emphasis on private investment. There have been efforts made to encourage privatization, but these have taken a back seat to the priorities of AIDS and other programs. Getting government out of the economy needs to be recognized as at least an equally important priority – as it is crucial for building up the tax base that will be necessary for continuing to fund social spending as diamond revenues diminish.

CONCLUSION

The Republic of Botswana turned a natural resource curse into a blessing by creating institutions to ensure responsible spending, and pursuing policies that encouraged growth and investment. Almost 40 years later, the carefully man-

aged revenues from that natural resource have allowed much of the population to enjoy an improved standard of living.

However, government involvement in the economy has been allowed to expand to an unsustainable level because its main source of revenue comes out of diamond mines instead of from taxpayers. It should be emphasized that:

- Botswana's early success can be largely attributed to institutional structure created through National Development Plans (NDPs);
- Continued government involvement and high levels of spending have not burdened the population through taxation, but have perpetuated resource dependency; and,
- Diamond output is estimated to begin falling within the next thirty years and therefore the current situation is neither sustainable nor desirable.

Botswana has not had to make the difficult political decisions of other upper-middle income countries. The expectation that output in diamond mines will begin to fall in the next thirty years, along with the growing insecurity of the diamond industry, gives Botswana a short time in which to make changes. With shrinking resource revenues, the government will have to begin to finance spending in other ways, and Botswana will be hit hard by these political difficulties if they are not anticipated.

In order to move ahead, Government leaders must now take on the hardest project yet: reducing the government's involvement in the economy. This will be difficult, particularly in the face of the AIDS crisis, international pressure over poverty and income inequality, and a tradition of government involvement. It will be difficult, but long term success depends on upon it.

Botswana is a unique country. It is not a typical middle-income nation with a mature economy, nor is it a typical resource dependent economy. Good economic, political and legal institutions have been developed. We traveled to Botswana to investigate its economic success. We came away impressed by the history and culture, the emphasis on education, and the drive for continuous improvement. We also came away shocked at both the size and scope of government.

The political leadership, though not taking diamond revenues for granted, has done little to resolve the paradox of high spending and low taxes. We have hope that Botswana can continue to develop and succeed, but the government must confront the paradoxical problems of the economy if the country is to move beyond resource dependency. We view the following implications as the most important for policy in Botswana:

- Government spending should be reduced to a level sustainable, both economically and politically, through tax revenue. This step is crucial to ending resource dependency;

- Poverty, unemployment, xenophobia, better health care, etc. are better facilitated in the long run through the development of a real, growing economy rather than through the unsustainable government spending; and,
- Diversification cannot be accomplished through government action. Re-focusing on privatization is an obvious and viable starting point in reforming the public sector.

Botswana's history offers shining examples to both resource-rich and all developing countries. It now has the opportunity to go one step further by turning resource dependency into a mature economy. Implementation of the policies suggested above will be economically and politically difficult, but reforming the public sector should be a top priority to ensure continued and sustainable economic growth for the years to come and after diamond revenues are gone.



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