EXPLAINING AFRICAN GROWTH PERFORMANCE
THE BOTSWANA CASE STUDY **

by

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1.0 INTRODUCTION AND OVERVIEW

1.1 Background

The main objective of this paper is to explain Botswana's economic growth performance for cross-country comparison. The growth record of independent Botswana has been impressive. From being one of the poorest countries in the wold at independence in 1966 and dependent on foreign aid for all of its development spending and most of its recurrent budget, Botswana has enjoyed rapid economic growth with decreasing dependence on foreign aid and is now classified by the World Bank as an upper middle income country with a per capita GDP of more than US $6000. In a region where the average country has been either poorer than at independence or/and in socio-economic crisis, Botswana stands out as one of the few countries in Africa with both an impressive sustainable development and political stability records. The country is also the region's longest democracy with good governance/state management record. Looking at Botswana's economic accomplishment over the last thirty five years' period or so, the country has sustained the world's highest real GDP growth rate and GDP per capita growth rates (Leith 2001).

The successful growth of the economy is mainly driven by mineral revenue from diamonds – a resource, which the state has used strategically to develop socio-economic infrastructure and human resource that has been rated among the highest levels in Africa in the UNDP Human Resource Development index since 1992. The role of the state in Botswana is, in many respects, similar with the development success story of the "East Asian miracle" experience where the state has been strategically interventionist rather than crisis driven under capitalist market economic development formula. But the institutional context of rapid growth in Botswana – that is a multi-party democratic system of government – offers a sharp and refreshing contrast to authoritative/undemocratic regimes elsewhere in China and the East Asian miracle which do not have a history of democratic systems/settings of government in the first place until quite recently.

However, it is also important to note that Botswana's strong economic growth and deserved praises for relative efficient institutions have not translated into significant structural economic diversification and poverty alleviation. Like many other African countries, Botswana is still basically a mono-economy, heavily dependent on one mineral, diamonds and it is riddled with high levels of poverty. With unemployment level estimated at nearly twenty percent and with about 47 per cent of Batswana living below the poverty line (BIDPA, 2000) – close to the African average of fifty percent – it is clear that the benefits of spectacular economic growth have not been well distributed, and Botswana exemplifies the huge income differentials elsewhere on the continent. The education system, considered one of the best in Africa, appears to have not yet sufficiently empowered citizens to either access jobs in a highly competitive labour market or and to innovatively take up/create business opportunities despite excess liquidity in the market and public sector business incentives. Although there has been a relatively good health system that provides free primary health care, the country suffers from one of the highest rates of HIV/AIDS infections in the world, a problem that has already began to undermine successes in human resources development with adverse implications for overall socio-economic development. Further, it has been recognized that the development strategy of state-led development that Botswana has followed over the years has reached its limits; and although the government is deservedly praised for being largely non-corrupt, the bureaucracy has out-grown its capacity for effective policy implementation ( ).

Recognition of the above limits together with the experience of rapid growth with limited structural economic transformation have necessitated the need for energizing the role of private sector and the need for economic diversification. These concerns are high on the national agenda, as evidenced by the themes of the current national development plan (NDP8), Nation Vision 216, and annual budgets – all of which emphasise the need for sustainable broad-based growth – premised on private sector led development and scaling down the sheer size of government through privatisation. Thus, although economic growth has been very rapid so far, there are grounds to think that it was not probably as rapid and diversified as it could have been and long-term self-sustaining growth may be questioned in view of a few but crucial negative dimensions/constraints indicated above; and the rate of real growth has slowed down during the last decade or rather in recent years. Nevertheless, Botswana's economic growth record remains exceptional. Since such success stories are rare (at least in Africa) the Botswana case provides an opportunity to examine what can go right in explaining African economic growth performance.

1.2 Objectives and Main Observations of the Study

Primarily drawing on growth accounting decompositions and cross-country endogenous growth literature, the main purpose of this paper is to explain Botswana's economic growth performance and general social development from 1960s to the end of 1990s and start of the new millennium. This is done by highlighting the salient features of the growth process and by showing which and how different factors contributed to this process. The analysis is explored in comparison with cross-country norms following Beno Ndulu and Steve O' Connel (1999) for macro-economic growth data and Macartan Humphreys (2000) for social and political development data. The analysis has also been complemented by the review of some relevant political economy readings, such as Bates and Krueger (1993) provided as background information on economic growth for this project and some cited literature on Botswana. We have not been able to complete filling in all data gaps - posing a major problem for implementing the regression-based growth decomposition. But the thrust of the basic issues and arguments, derived from other sources, are reasonably clear within a common framework, making it possible to compare and contrast the cases and draw inferences from them.

Following our interpretation/review of the evidence, Botswana stands out without doubt, as one of the few countries in Africa with an impressive economic growth record, and our explanation endorses a general consensus among the country's development analysts that Botswana has achieved rapid economic growth because it managed to adopt good policies and also to manage the economy and the country effectively. It is the acknowledgement of the country's long track record of good economic policies, prudent economic management and good governance given the supportive institutional framework over the years. Batswana are deeply suspicious of praise singers – preferring (in line with the country's democratic tradition), engaging in a debate on the challenges confronting the nation and the region rather than on being showered with praises/epitaphs. Thus the paper is also critical and ends with challenges. In the context of this study, Botswana's performance illustratively deviates positively well above the African average or the mean in the cross-country norms, which have been designed for the AERC Collaborative Research Project Coordinators to compare economic and political performance. The average rate of growth over the country's post-independence period of three and half decades and the institutional context of a stable and largely less corrupt democratic multi-party system of government over the same period are outstanding in cross-country comparative analysis of all the African countries covered by the project with any other country in Africa. The fundamental question is: Why and how?

Pursuing the route of policy influence in explaining differences in cross-country growth performance, our main hypothesis, is that the qualities of both the policy environment and governance, under pinned by the quality of leadership relative effectiveness of the inherited and newly established institutions, combined to positively influence dynamics of rapid economic growth and development. Given the few but crucial dimensions/constraints noted above, the thrust of the paper suggests that although growth has been very rapid so far, it was not probably as rapid as it would have been in the absence of the noted constraints which are subsequently elaborated upon in the text. Thus, the economic policies and established economic and political institutional context modified over time - interacted to induce and sustain the quality of policies the leadership adopted and sustained to generate the development evidence we now observe in retrospect. Fundamental aspects of democratic culture, state and public good and private property ownership with relatively effective property rights and the role of the state in administering public goods are relatively well established/entranched in Botswana's history and culture (See Schapera 1967:43-64; Parsons 1984:16-22 as quoted in Robison et.al 2001 – brief political history 2001:9-15).

The paper is divided into four main sections. The first section discusses macro-economic and sectoral performance of the economy and this is subdivided into three broad periods for telling the growth story. Section two focuses on macro-economic factors of the growth story and section three discusses the role of agents in savings and investment. Part four ties the factors of growth together followed by why and how sectors reconciled political economy conflicts.

2. MACRO AND SECTORAL ANALYSIS OF GROWTH PERFORMANCE

This section provides a general overview of the process of economic growth. After a brief reflection on macro-economic and sectoral performance, the growth analysis illuminates the role of policies, main agents, markets and interests under political economy issues.

2.1 **General Macro-economic Analysis of Structure and Growth**

The overview of Botswana's development record is captured in one sentence. Initially based on agriculture and heavily dependent on foreign aid, the rapid economic growth and general development in Botswana have been driven by the mining sector, particularly the diamond industry, and have been strategically led/influenced and managed by the state and decreasingly complemented by foreign aid within the overall institutional context of a liberal market economy and multi-party democratic system of government. Table 2.1 shows GDP annual growth rates and sectoral share of GDP economic activities and how each of these sectors grew annually. This broad review is complemented by graphs 2.2) on foreign aid and 2.3 showing the savings and investment patterns for macro-economic analysis over the same period as shown under section 3. Taking the whole period of this study's review – from 1960 to 1997, real GDP average growth has been almost 10 percent while real GDP per capita growth of 7.04 percent is far above the sub-Saharan Africa average – registering a

Table 2:1 Sectoral Percentage Share of GDP & Annual Growth Rates (Constant 1993/94 Pries

	1966	1975/76	1977/78	1979/80	1982/83	1985/86	1987/88	1989/90	1991/92	1993/94	2000
Agriculture	39	25.4	21.3	13.1	8.9	5.5	7.2	4.8	4.4	4.4	4.2
	-	(1.3)	(-0.5)	(2.0)	(-12.5)	(10.8)	(65.5)	(3.6)	(2.0)	(-0.9)	-
Mining	0	12.5	15.2	31.2	32.0	47.2	45.5	51.2	37.7	35.7	33.7
	-	(64.5)	(86.1)	(41.8)	(46.3)	(3.1)	(2.8)	(-3.3)	(-0.5)	(5.4)	-
Manufacturing	8	6.9	5.8	3.7	6.7	5.2	5.1	5.0	5.0	4.6	6.0
	-	(28.2)	(-6.4)	(-35.1)	(-8.1)	(30.1)	(29.9)	(4.8)	(6.4)	(-0.6)	-
Water and	2.8	3.8	2.5	2.0	2.6	2.4	2.9	2.0	2.0	2.2	2.2
Electricity	-	(51.1)	(9.9)	(-3.8)	(-1.3)	(33.6)	(14.4)	(2.2)	(5.7)	(14.9)	-
Construction	5	8.9	9.8	7.6	5.1	4.0	4.9	5.5	7.8	6.5	6.4
	-	(1.1)	(36.3)	(11.6)	(-18.4)	(-11.2)	(18.1)	(25.1)	(4.6)	(3.7)	-
Trade, Hotels &	5	8.0	8.1	8.2	6.8	6.9	5.7	5.2	5.6	8.3	9.7
Restraurants	-	(15.8)	(-1.5)	(9.3)	(-33.4)	(44.4)	(20.2)	(18.0)	(-8.7)	(65.1)	-
Transport	2	4.0	3.6	1.7	3.0	2.5	2.9	2.6	3.4	3.7	3.8
	-	(20.6)	(11.1)	(57.6)	(11.3)	(29.5)	(52.3)	(7.7)	(13.9)	(1.3)	-
Finance, Real	2	6.4	6.9	7.7	6.3	6.0	5.1	6.1	7.8	10.1	10.8
Estate & Bus. Serv	-	(8.3)	(-3.1)	(46.4)	(5.4)	(21.8)	(6.9)	(27.9)	(3.9)	(8.1)	-
General Govt	12.3	14.1	15.3	13.0	16.4	13.0	13.4	11.5	14.6	15.6	15.5
Services	-	(22.8)	(1.9)	(3.4)	(9.6)	(7.9)	(21.8)	(2.1)	(16.8)	(3.4)	-
Social & Personal	3.2	4.4	3.7	2.7	3.3	2.8	2.7	3.1	4.1	4.3	4.4
Services	-	(32.7)	(1.6)	(0.0)	(19.9)	(13.8)	(30.6)	(16.3)	(5.4)	(1.8)	-
+ Adjustments:-		0.9	-1.7	-1.9	-2.1	-2.0	-2.0	-2.2	-2.2	-2.7	-2.8
Dummy sector	-	(50.0)	(-2.5)	(32.1)	(17.1)	(48.0)	(16.2)	(2.7)	(3.2)	(18.0)	-
Custom Duties	-	6.6	9.5	11.1	11.1	6.5	6.6	5.4	9.9	7.3	6.1
		(5.8)	(26.9)	(28.3)	(8.2)	(-9.2)	(12.4)	(8.5)	(32.6)	(-25.5)	-
Total GDP											-
(aggregate)	-	**(18.4)**	**(19.5)**	**(14.4)**	**(16.0)**	**(7.5)**	**(14.7)**	**(5.5)**	**(6.3)**	**(4.2)**	-
GDP excluding											
Mining	-	**(12.2)**	**(6.3)**	**(6.2)**	**(-3.2)**	**(11.7)**	**(25.1)**	**(11.5)**	**(10.3)**	**(3.5)**	-

Source: National Accounts Statistics of Botswana – 1974/75 to 1994/95 (Central Statistics Office, Gaborone, March 2000). **NB:** Annual growth rates are in brackets.

deviation of 4.82 from the mean sample. It is noteworthy that Botswana's real GDP per capita growth has been the world fastest over the years (Harvey 1992; Leith 2001). Looking at value added as a percentage of GDP, we note that agriculture's share in GDP has shrunk significantly from over 40 percent in 1960s to about 4 percent almost swapping with mining whose share rose sharply from almost zero to nearly 50 percent for some years before sliding but still maintaining a dominant position as the lead sector. The share of manufacturing has remained almost constant, seemingly playing a marginal role of 4 percent GDP share. Like other sectors that have maintained their share of GDP, manufacturing has been growing in absolute terms during the country's period of rapid overall growth as can be seen from table 2.1, but relative terms, which are crucial for structural transformation, shares have not positively changed except for the government and quite recently the service sector.

As elaborated upon under the periodised broad growth section below, Botswana is still at the factor driven stage of economic development, highly dependent on vulnerable primary products for growth. The shrinkage of agriculture in favour of mining – not manufacturng – is not regarded as sustainable development path in development literature (Stern 1989; Weiss 1988; Roemer and Lindauer 19..) The development of a mineral "staple" such as diamond export in Botswana, has been thought of as a potential spring board for structural transformation – not via expansion of the mineral factor itself but via its linkages to the rest of the economy (including fiscal linkages). Fortunately, Botswana policy makers seem to be fully aware of this as reflected in the development strategies and some key facets of macro-economic policy. Reserve accumulation during good or boom periods and rapid response to adverse terms of trade shocks are two crucial facets of Botswana's supper-prudent macro-economic policy ingredients that treats diamond price increases as temporary and declines as permanent. The strategy of state-led development was underlined by using diamonds for developing other sectors and so has been the new strategy of private sector led development. Given this perspective, it is therefore imperative to shift attention towards the contribution of the diamond sector to growth of the non-mineral, non-agricultural sectors (such as tourism, financial services etc.), which are regarded as the ultimate destinations of structural transformation.

PERIODISATION OF GROWTH PERFORMANCE

Using the annual and half-decadal data, which have already been provided by the project coordinators, we have identified and corroborated three broad periods for the case study, during which the main drivers of economic growth and development appear to have differed or to have behaved differently. The first phase is from 1960 through independence in 1966 up to 1974, described as a period of initial base creating or foundation making. This phase is characterized by transitional rapid growth with significant flow of foreign capital - aid and private investment; the capital accumulation stage, recognized by massive expenditures on physical and human capital. The second phase, starting from 1975 up to the end of 1989 is denoted as a period of rapid economic transformation, marked by fastest economic growth with limited structural diversification. The period is underlined by transitional and fundamental sectoral transformation with agriculture and mining switching their lead positions and also changes regarding the trends in domestic savings and investment over time with the ratio of savings to GDP subsequently exceeding investment, leading to moderate growth or reaching (what some analysts described as) the limit of state-led development model. The third period, though overlapping to some degree with the end of 1980s, covers the whole of 1990s and the new millennium, characterized by moderate economic growth rates with domestic savings consistently exceeding domestic investment. The period is, in term of policy choices, marked by major re-orientation in economic development strategy and re-alignment of particular interests and is marked by complex policy choices and efforts towards privatisation and to enhance private sector led development and also consolidation of democratic governance and economic management.

Fortunately for us, the rate of growth and pattern of general development appear to have fitted relatively well within the three broad growth periods. The very lumpy nature of some big investments caused growth to be far from even. Periods of very rapid growth were followed by periods of relative stagnation, during which GDP was sustained at or near its new higher level by government spending of the revenue generated by the previous boom. While recognizing that Botswana's development record reflects "good luck" to some degree, the pattern of development has led many analysts acknowledge the reputation that has been established "for good management/governance" on the part of government - emphasizing the importance of stable democratic system of government and growth promoting policies which Botswana has pursued. The analysis of how evolution and sustainability of growth promoting policies has been shaped by leadership, interest and institutions is broken up into three broad phases in what follows below and all factors are tied together and reviewed under section 3.

GROWTH PERFORMANCE: THE STORY FOR THE FIRST PERIOD – 1960S TO 1974

The first phase of growth pattern covers a period a few years before and almost a decade after independence in 1966 up to 1974. The data during this period is incomplete mainly because some key economic data were controlled by South Africa and Botswana did not start submitting its own data until 1975. But available evidence shows that it is a period of laying the foundation for economic growth and the country's political system. The main causes of moderate to rapid rate of GDP growth were a combination of some "good luck" factors and most importantly good management issues/policies, and elaborated upon under section three. The main argument, under this growth period, is that the growth inducing factors, especially quality of policies adopted, were first and foremost due to good leadership including use of technocrats/advisers, and relatively good inherited and newly developed institutions within which various economic interests – foreign capital and the ruling elite – have been relatively well accommodated. The Botswana political leadership – itself rather unique in some respects – managed to modify and build on the pre-colonial Tswana state culture to create what Maundeni (2002) refers to as "an indigenous developmental state" (above other social institutions and marginalize them). The new, but basically modified state was premised on basic values of modern democracy with relatively strong executive state power regarding appointments of state personnel, training and promotion, commend and discipline. This institutional context of "good luck" and qualitative dimension of policies adopted will be elaborated upon to explain why Botswana leadership adopted such policies.

Development Policies and Strategy

Like many other development analysts before us, the country's rapid economic growth is attributed to the effective state management – the long track record of goods policies, good governance and prudent economic management. It is therefore imperative to briefly reflect on some of these policies during this phase of the country's development. On political front Botswana adopted a multi-party democratic system of government, to manage political competition. This policy choice confomed relatively well with the first wind of democratic transformation cutting across new independent African states in the 1960s, but this does not explain why the system survived and continued allegience to mass participation and multi-party policies when one-party and military regimes swept the region. There is no documented evidence identifying key points at which decisions were made and/or confirmed. Much of this comes down to the quality and interests of "the ruling class" especially within the ruling Botswana Democratic Party leadership and Sir Khama himself, and also democracy tied well with the consensus-seeking approach that had deep roots on the Tswana culture as elaborated upon later. During this period two main political parties participated in the two general Parliamentary and Local Government elections - the Botswana Democratic Party (BDP), known as the liberal/conservative party, and the Botswana Congress Party - subsequently replaced by the Botswana National Front (BNF), known as radical left or socialist/communist oriented. The BDP led by Khama who was earmarked to become chief of one of the prominent tribes, was put in power in 1966 and re-elected in 1972 with an overwhelming and largely rural-based majority, while the opposition increasingly became an urban-based party. Analysing public policy from institutional perspective, it was inconceivable for Batswana ruling elite, drawn disproportionately from the upper socio-economic strata of society to break the system that was operating in their interest in favour of the radical ideology of the opposition to maintain stability and avoid "revolution"

Another important policy choice to note was the approach to national development, underlined by development planning and progmatism – not "ideological dogma" – for economic policies and the overall strategy of state-led development. Approach to national development. Significance of state strategic intervention, especially the idea of formulating and implementing a national development plan, a fore-runner of development planning as an instrument for resource mobilization and management that runs up to-date in what was basically a market economy. Each of the country's development plans has since then sought to promote four national principles of democracy, development, self-reliance and unity - leading to four overall national development objectives of rapid economic growth, social justice, economic independence and sustain development.

Botswana's economic development strategy was and continued to exploit the country's mineral worth and invest the proceeds from mining in improving social and economic conditions and create new economic opportunities, while at the same time encouraging the role of foreign aid and private (foreign) investment. This strategy of transforming the mineral endowment into an endowment of physical and human endowment has the potential to achieve self-sustaining growth because physical and human capital is renewable, whereas the mineral endowment is not (Bank of Botswana, 1995: 5). State management capacity was enhanced by some early government policies such as land policies and their management to Land Boards; vesting mineral rights (from local authorities) into central government and negotiated shares as approved to nationalization of mines; and the policy of gradual localization by relying on foreign experts. These policies averted land and mineral right disputes which are the main source of tribal or regional conflicts in some countries, and equally important private foreign investment had not been threatened and reliance on foreign operational experts enhanced technical and management competency.

During this early period of factor driven economic development, the main direct causes of rapid growth of GDP were many and only the crucial ones have been identified (Harvey & Lewis 1990: 30). The most important ones are the discovery and successful exploitation of copper, nickel and diamonds; increasing flows of aid from an increasing wide range of donors, initially financing the whole development budget and about half of its recurrent expenditure. The gaining of access to the EEC for beef exports, at prices above world market was very important for the agriculture sector. The other factor was the ending of the major drought of the mid-1960s in the context of positive agriculture policies had noticeable impact. So was membership of the (Southern African) Rand Monetary Area, thereby limiting the country's discretion over monetary policy at a time of implied temptation for deficit financing given limited financial and manpower resources was crucial during this period. The pragmatic sense of the government was also demonstrated by the decision to remain within the Southern African Customs Union of 1910 and renegotiation of the revenue distribution formula in 1968, which ensured a stream flow of revenue for needed development projects.

Growth Performance and Basic Structure

All the above policy-related factors combined to induce rapid rate of growth. The country's growth progressed from moderate rates before independence to high average growth of 7 percent between 1965 and 1969 and reached an average peak of about 10 percent between 1970 and 1974. Fits and residuals derived from Pooled Conditional model are equally illustrative of Botswana's exceptional growth performance. It shows the actual average growth of about 16 percent between 1970 and 1974 - with a deviation of 14 percent from the sample mean. It is also important to note that the growth rate was high partly due to small GDP base and mainly because the aggregate growth of the economy was dominated by two mining projects - the copper-nickel mine at Selebi-Phikwe and the Orapa diamond mine. The former, the largest of the two projects, was 1.5 times GDP and its large infrastructure, know as the Shashe Project, was financed through public spending, made possible largely by foreign aid, while the diamond mining company, De Beers built the "closed town" of Orapa as part of the security area (Harvey and Lewis 1990). A parallel development took place in sectoral shares of GDP. The share of industry, mainly mining rose sharply from near zero to 39, and manufacturing only managed to grow in absolute terms to keep its relative share unchanged at 4 percent while that of agriculture declined from 40 percent to about 21 percent. Other sectors maintained their share of GDP, responding to the growth of public services and the stimulus provided by mining.

It is also noteworthy at this stage that behind the statistics of growth pattern lay two remarkable paradoxes or puzzles – namely that the rate of growth was exceptionally high and yet there was extreme shortage of skilled/educated manpower in Zambia and "Dutch disease" or adverse consequences of the "mineral-led economy syndrome" was avoided. Manpower constraint did not seriously affect economic growth because of the policy of foreign operational experts and gradual localization, and relatedly the government had taken care not to spend more than the economy could absorb and to avoid the boom and bust cycle common to mineral-led economies as elaborated upon in the next phase of review.

Institutional context of Growth

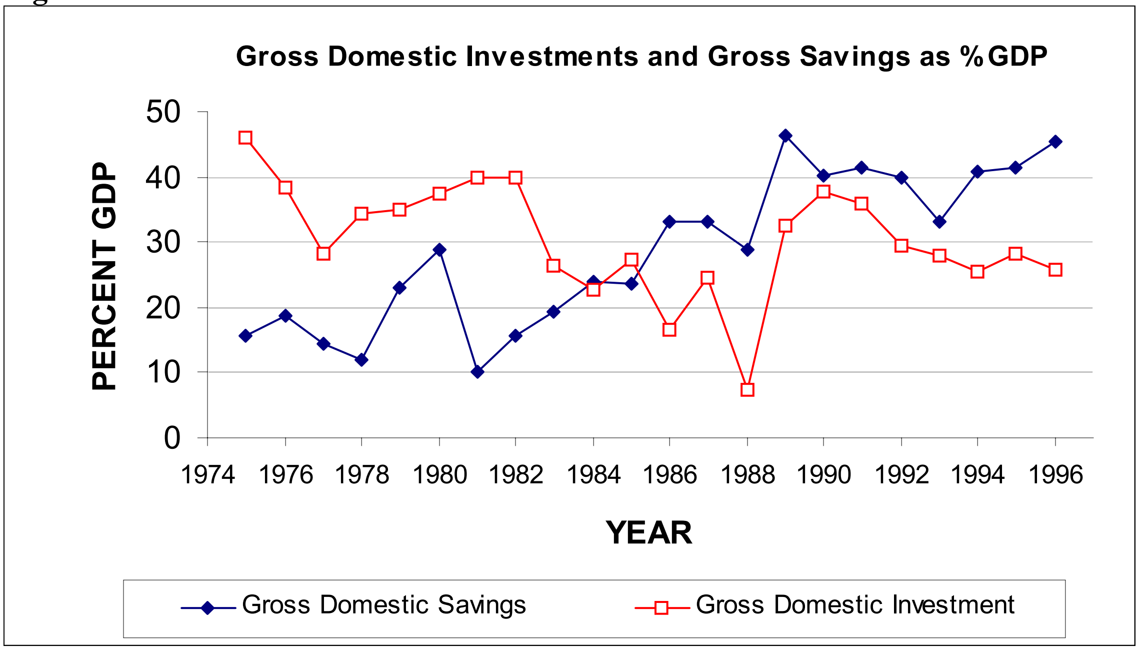
The institutional context of rapid growth and early sectoral transformation is crucial for explaining the forces behind these changes. The quality of democracy/governance was important in influencing policy choices and reconciling various interests. The country's performance in all the five political variables for cross-country comparison - democracy, strikes, demonstrations, coups and guerrilla wars - was outstanding (Macartan Humpreys 2000). By 1974 Botswana had two competitive general parliamentary and local government elections won by the Botswana Democratic Party BDP, in power with overwhelming and largely rural-based majority. The two main political parties had different ideological orientations and the main opposition party was regarded as "a radical left" with socialist/Communist ideals. But the interests of the Batswana elite were largely homogeneous, based on cattle. This made it relatively easier to reach consensus on policies. The leadership in the ruling party had considerable interest in promoting their own version of good government. But knowing that it must stand for election every five years - seeking "profit" in the form of "political income" - the ruling party pursued policies it believed will gain it the political support necessary to defeat its opponents. Priorities of the key rural development programmes, initiated during this period, and attention given to the cattle industry have not been biased against rural areas as elaborated upon subsequently. Thus, neglect of rural interests, a widespread problem in sub-Saharan Africa (Bates), was largely avoided in Botswana because of representative government, which was elected by the rural majority and the ruling elite had interests in rural development policies/programmes.

Foreign aid is power and has interest. The government worked to attract aid from a number of donors and built donor's confidence through ensuring proper allocation and efficient management of aid-supported projects and the government budget. Being the only liberal democracy surrounded by racist and minority ruled southern African states, Botswana attracted sympathy from the Western donor agencies. Thus, in addition to using foreign aid effectively, aid agencies were also motivated by the country's democratic attributes in the troubled southern African region. In fact, international aid was a crucial resource that the government initially used strategically to develop physical and social infrastructure and diversify its economy. To reconcile the interests of foreign capital, the government had a relatively open economic policy. Private foreign capital was attracted by political stability, a relatively open liberal economic policy, and maintenance of enabling environment, especially macro-economic stability for foreign and private investment.

Growth Rates, Investment & Savings

The links between savings, investment and growth are well established in economic theory and need not be elaborated upon here. The objective is to establish, without the benefit of an econometric analysis for empirical test, correlation that might exist between savings, investment and growth in Botswana. The analysis may be seen as a reflection of the growth model with which the classical economists argued that the rate of economic growth depended on the proportion of an economy's activities that were productive and the rate of surplus (savings) for reinvestment. Figure 2.1 shows trends in gross domestic investment and gross domestic savings as a percentage of GDP. The savings available to the nation can come from domestic and foreign sources, and the rate at which capital stock accumulates contributes to determine the rate at which productive capacity is created.

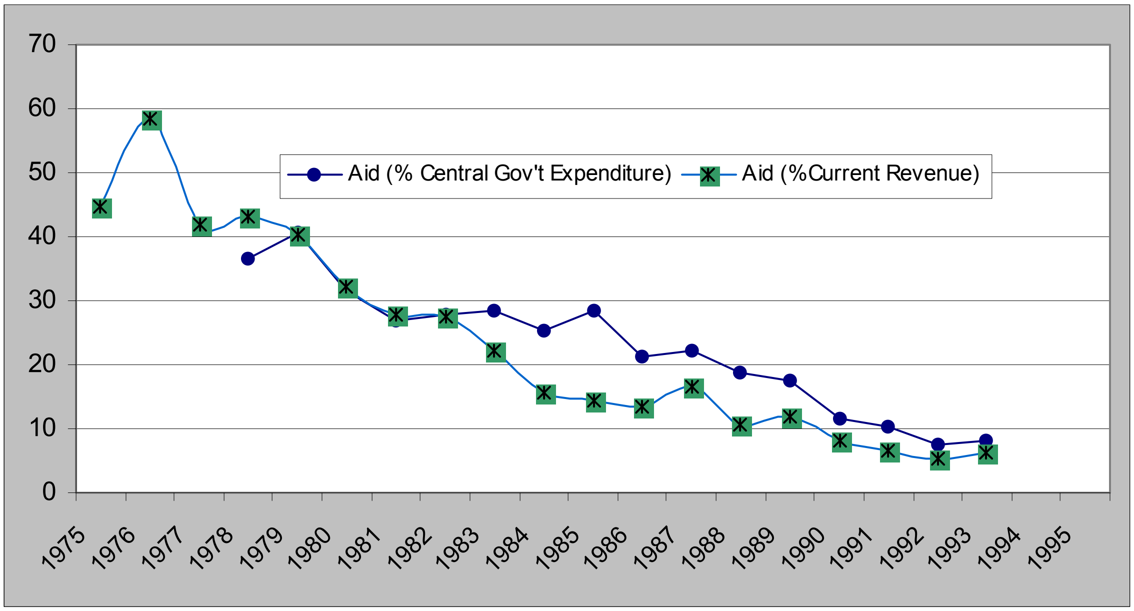
Figure 2.1



Source: Calaculated from Botswana "DAC data" 1998

Taking into account the main observations made above and the trends of saving, and investments depicted in figure 2.1, a number of points related to economic impact of aid can be raised. To start with, the economic role of foreign capital including aid -- especially its contribution to growth, investment and savings -- has changed over time. In early years, aid was essential in relaxing macro-economic constraints -- particularly the foreign exchange constraint and financing development budget, and thus financed priority government projects. It may be seen from the figure that investment exceeded domestic savings before 1986, and the shortfall of domestic savings over investment was financed by foreign savings. During this period, Botswana was a net recipient of capital flows. Thus, Botswana's rapid rate of economic growth, at least during the first two decades of independence depended to a considerable degree on capital from abroad. The period of sustained and exceptionally high economic growth rates annually from 1966 to 1989 -- also coincided with sustained jerks or step-like increases in aid to Botswana (tables 2.2). How can we have a rough idea of the contribution of aid to investment financed by foreign savings?

Chart 2.2



Source: Calculated from Botswana "DAC data" 1998

<u>Aid's contribution to Investment and Savings</u> is roughly shown in figure 2.2. In simple economic growth model, the rate of growth is directly proportional to the savings ratio divided by the incremental capital-output ration -- ICOR -- ( ). Statistical analyses tend to show a close correlation between investment in physical capital and economic growth and also a correlation between shortage of foreign exchange (needed to import machinery, equipment and inputs) and negative growth or and capacity under-utilisation (Barro & Sala-Martin 1995). On the basis or backdrop of this relatively simple economic growth theory, aid could be said to have made significant contribution to the early growth, although private investment increasingly played a greater role (figure 2.1 above seen together with figure 2.2). Perhaps most importantly, aid helped finance much of the original public investment in infrastructure and mining -- facilitating private capital inflows especially for the mining sector (Maipose et al 1996:). A well-functioning infrastructure is regarded (with empirical evidence) as a precondition for economic

development and sustained growth (Abramo Vits 1993; Maddison 1996). On the basis of this argument it can be concluded that, Botswana's development strategy of prioritising infrastructure and the donor's response to support infrastructural development during the early period of independence were in the right direction.

GROWTH PERFORMANCE: THE SECOND PERIOD 1976 - 1989

The Second Phase of the growth Period - starting from 1975 to 1989 - is described here as the period of fastest growth and structural transformation. It is during this period that the mining sector clearly emerged and consolidated itself as the engine of growth, putting the strategic and positive role of the Botswana state in clear perspective as an instrument of society and consolidating its pragmatic approach to development management. During this period, growth was sustained by some important policy related factors and these are reflected upon below:

Continuation of some key positive policy stances from the first phase, such as retention of the multi-party democratic system of government at a time when many sub-Saharan African countries abandoned the system and became one-party or regimes. The other was membership of the SACU, which effectively meant that Botswana was not free to set up its own import tariffs to protect domestic producers including import-substituting industries as was the case in many developing (African) countries. The gaining of access to the EEC market, at prices above world prices under the special provisions of the Lome Convention negotiated for by government and signed in 1975. This boosted the principal capital assert of economic inheritance, cattle. Control over monetary and exchange rate and policies following a decision to move out of the monetary union in 1975; and the creation of the country's currency, the Pula in 1996.

Much of the growth during this period was factor driven closely associated with the expansion of Orapa diamond mine; the development of another mine at Letlhakane and the third and larger mine at Jwaneng by 1981 leading to significant growth in GDP. The steady built-up of government spending, made possible by the customs union revenue and the mining sector, with the state emerging as one of the main growth promoting sectors/agents. Foreign Exchange Policy issues, firmly in place by the time Botswana withdrew from the Rand Monetary Area in 1976, initially focused on exchange controls and exchange rates and subsequently the management of the foreign exchange reserves. Before they were completely liberalised in mid-1990s, all foreign exchange payments were initially subject to control formalities and a fixed exchange rate was operational over many years. However, these instruments were not designed to directly ration foreign exchange. They were deliberately designed to occasionally deal with capital account disturbances and mainly to maintain stability, competitive position and to avoid the well-known "Dutch Disease" effect of a strong currency crowding out all but the most robust export activities.

Fiscal revenue and expenditure trends reflected a coherent view of development and priorities in government policy throughout this period. All the three main sources of income - customs union, minerals and aid grew rapidly and the peak in aid inflows was attained before it declined in relative terms and replaced by earnings from foreign exchange reserves. On expenditure side, the government has been rather cautious despite its enormous revenue base, resulting in budget and trade surpluses throughout this period. Although afraid of - turning rapid growth into an inflationary spiral, the government did relatively well in building socio-economic infrastructure and developing human resource without which little growth would be achieved and sustained.

Growth Performance and Basic Structure

Three issues are worth noting about growth performance during this period. First, growth rates, though high, fluctuated significantly and flattened out towards the end of the 1980s - influenced by expansion or opening up of new mines. Second, the sectoral variables show tremendous expansion of the mining sector's claim of a GDP share of over 50 per cent. More or less the same happened to services which had an average of 14 percent GDP share while agriculture continued to decline significantly from 15 to 5 percent during the same period. Furthermore, the ratio of government expenditure to GDP grew significantly and became one of the highest in Africa (Leith, 2001:45) and total government revenue had the average of 50 percent of GDP – the highest in the region. There are a number of reasons to account for these changes. Third, there were significant changes in both government revenue and in the aggregate ratios of investment and savings to GDP. While domestic savings as a share of GDP was negative in mid-1960s and inflows of foreign aid and foreign investment into the country increased, the contribution of domestic savings to investment rose significantly during this period (Matsheka, 1997). Actually, it was during this period that domestic savings began to exceed domestic investment. Domestic savings financed almost all of Gross Fixed Capital Formation for the first time in 1984, even though capital inflow remained positive.

Institutional Context of Growth

Finally, another point worth noting in comparison with cross-country norms is that the ratios of both government revenue and expenditure to GDP are among the few highest in Africa and substantially in excess of the average of the countries covered by the project. So is the magnitude and ratio of the military expenditure, which subsequently became the highest in Africa. However, it is equally important to note that the high extractive capacity (taxing burden) does not directly fall on the ordinary voters because all the three main sources of income are denominated in foreign exchange, while high state expenditure tended to maximize social/collective benefits without deficit financing and therefore not inflationary - a pattern of development which was both economically and politically (in terms of interests and institutional relationship) tolerable. But the high ratio of government expenditure and revenue to GDP are clear indicators of the overall size of government – a matter of concern, seemingly clouding out the role of the private sector and thus the challenge to scale-back the relative size of the government. Despite the Botswana government's strong private sector thrust, it retained a strong presence in the economy – hence the need to privatize for efficient resource allocation and effective policy implementation. This leads us to discuss growth performance under the third phase of our development process review.

GROWTH PERFORMANCE: THE THIRD PERIOD

The third and the last growth phase is a period roughly starting from 1990 up to 2000 or rather to-date, marked by moderate economic growth and a major shift in the thrust of the growth promoting policy from state led development to market led development. This re-orientation, bluntly put as privatisation drive, is complemented by concerted state effort aimed at empowering the Batswana - the citizens – without frustrating foreign investment, a clear reflection of the fact that interests are no longer homogeneous as they fight for the spoils of the system. Thus, while one can still discern a significant degree of continuity of some policy measures in place, growth has been sustained by the following additional policy issues or re-orientation.

New Development Policies and Strategy

The new economic development strategy of the Botswana government is to promote economic growth through the private sector, develop an efficient financial system, and provide a stable macroeconomic environment (Budget Speech, 1997). The aim is to reverse the structural bias against the non mineral sector and achieve a more balanced and diversified economy. The Bank of Botswana (1993) summarises the strategy as follows:

> The basic strategy in our National Development Plans has been to transform the mineral endowment into an endowment of physical and human endowment. This has the potential to achieve self-sustaining growth as physical and human capital are renewable, whereas the mineral endowment is not. But it depends, crucially, on achieving the transformation of the mineral endowment into productive physical and human capital (p.5).

This policy position marks a shift from economic independence to economic diversification and the provision of an enabling environment for the development of the private sector. The commitment to the promotion of the private sector is not new (Harvey and Lewis, 1990). The choice of the strategy was dictated by the narrowness of the domestic market; the opportunities presented by membership of the Southern African Customs Union Agreement (SACU), and skills shortages.

There are two related issues with implications for the financial system, and more broadly economic diversification. Firstly, the nature of the development strategy, and the acceptance that diamonds are not forever, requires the development of the financial system to lessen dependence on minerals to ensure sustainable economic growth. This requires the financial system to perform the intermediation function more efficiently. This is important because according to the Bank of Botswana (1993) a significant amount of capital or mineral rents has been spent on non productive and consumption goods rather than on investment activities thereby hampering the efforts to achieve economic diversification.

Secondly, in order to achieve economic diversification the government initiated a number of financial assistance programs and offered credit to the private sector through organisations such as the Botswana Development Corporation. There were other policy initiatives. For example, the Financial Assistance Policy (FAP) the thrust of which was, among other things, to encourage labour intensive operations through wage subsidy for unskilled labour; the Selibe-Phikwe Incentive Package (SIP), and Infant Industry Licenses. Assessments of the various packages have generally found them to have achieved their set objectives (World Bank, 1993; IMF, 1995).

This position has changed. The government's dominant role in the financial system is deliberately reduced to remove the non market allocation of capital, especially, but not exclusively, to parastatal organisations. The large volume of capital allocated by the government to parastatal organisations has constrained the development of domestic capital markets (Bank of Botswana, 1986, 1994). There is a recognised need to give the financial system a greater role in the allocation of financial resources. Otherwise to the extent that a large volume of financial resources is channelled outside the domestic financial system the role of financial intermediation in Botswana is limited(World Bank, 1991). The argument is that the financial system would not be able to support the economic diversification program and help achieve a higher rate of economic growth.

Financial reform to support economic diversification is intended to address four main problems (Bank of Botswana, 1996). Firstly, the fact that major financial flows take place outside the private financial system. This requires the reduction of the role of government in the financial sector. Secondly, the lack of competition in financial market which results in the provision of a poor quality of service. Thirdly, the lack of established and developed money and capital markets which are necessary to improve the range of financial instruments offered in the market. This will also address the lack of funding for long term projects which has also resulted in the greater participation of the government in the domestic financial system. Fourthly, to promote the effectiveness and efficiency of development finance institutions.

Economic Growth and the Structure of Output

The rate of economic growth during the period 1965 to 1989 averaged 12 percent per annum, consistently much higher growth rates of economic growth compared to most sub-Saharan African countries.[1] However, economic growth has remained single digit in the 1990's. Recent estimates put the rate of economic growth at 6.9 percent in 1997. Although the growth rate of gross domestic product has been impressive, the structure of output has seen the continued dependence on a single product. The manufacturing sector is beset with problems of productivity and competitiveness, whilst the employment potential of the service sector remains untested (IMF, 1995). Recent estimates of productivity in the manufacturing sector indicate that it has declined between the 1989-1992 period, but has since 1992 been on the increase. The fall in productivity, in the period 1989-1992, is partly attributed to the incentive schemes of the Financial Assistance Policy (FAP) that encourage the employment of unskilled labour which has tended to neglect skill development and training (Jefferis, 1997). The share of the agricultural sector, as a proportion of Gross Domestic Product, declined from 23 percent in 1974 to 3.4 percent in 1997. The mining contribution of the mining sector increased from 12 percent in 1974 to 50 percent in 1989. The sector's contribution has fallen to 33 percent in 1997.

The growth and expansion of the mining sector was not, however, replicated in other sectors of the economy. The manufacturing sector, like the agricultural sector, has

[1] For a detailed account of Botswana's growth experience see (Harvey, 1992; Harvey and Lewis, 1990; World Bank, 1989; Salkin. et.al, 1997).

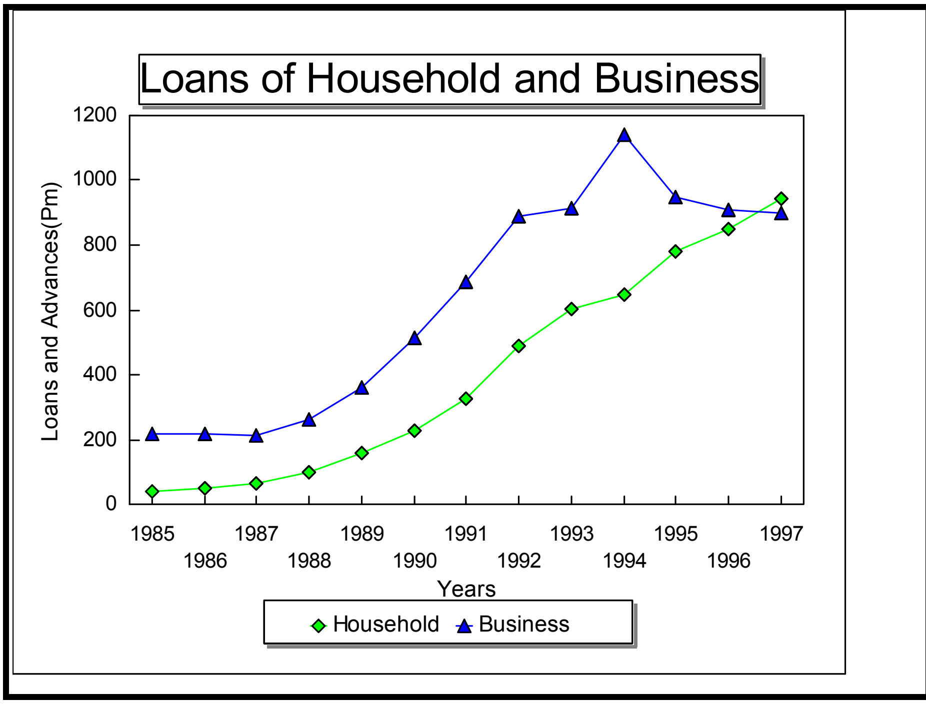
recorded modest growth since independence. The sector accounts for 5.5 percent of total GDP in 1997. The minor contribution of the manufacturing sector to total GDP is attributable to, among other things: the size of the domestic market; the lack of skilled labour and infrastructure; free trade within SACU, and high utility costs, mainly electricity and water rates.

The argument that the size of the domestic market is an explanatory factor for the slow rate of industrialisation is rejected because Botswana by being a member of the Southern Africa Customs Union, has access to a potentially larger market for exports (Mayo, 1983). Instead the problems is identified to be the dominance of South Africa in the Customs Union Agreement. The strength of South Africa in the Union is thought to be detrimental to the establishment of industry in the member states because member countries have access to a wide range of inexpensive and indirectly subsidised South African products, especially food imports that have harmed local industry and agricultural production. Mayo attributes the poor performance of the industrial sector to the failure to use the accumulated financial resources to build productive capacity to a point where vulnerability to diamonds still persists. Moreover, Botswana has healthy foreign exchange reserves, and the banking and monetary system has excess liquidity.

International Monetary Fund (1995) estimates indicate that "power and telecommunications costs are twice as high as those in Zimbabwe and South Africa, while water rates are roughly 10 times those in Zimbabwe, and more than twice those of South Africa"(p.15). However, it is considered that increased competitiveness in the economy, and the manufacturing sector in particular, depends on the ability to restrain wage costs, sustained improvements in productivity, and the ability of the financial system to serve potential investors.

This could partially explain why the manufacturing sector has not provided the expected impetus to the economy despite the various investment packages provided by the government. The policy of government to attract foreign investment is increasingly limited to the provision of an appropriate legal framework, infrastructure and macroeconomic stability.

The promising sector, in terms of potential contribution to gross domestic product, is the trade, hotels and restaurants sector, which contributes 17 percent in 1997;



this makes it the third largest sector after mining and general government. The services sector benefits directly from the growing tourism industry. How growth has been enhanced by service sector is illustrated by what follows below.

Financial Sector Development and Economic Growth

The developments in the mining sector were funded by inflows of foreign capital. In the period between 1985 and the economy has accumulated surplus of saving over investment. As a result "resource availability could not have been a constraint to investment " in this period (Bank of Botswana, 1997, p.88). The fall in investment as indicated in the figure above is explained by the possible lack of profitable investment projects and the *inefficient intermediation of the financial system*(ibid). The end result of this failure to engage effectively in risk and maturity transformation by the Botswana financial system is that internal funding of investment assumes greater importance in the economy. In a sense the financial institution is still dominated by self-financing behaviour; prior saving is made necessary for investment by the lack of efficient intermediation.

Figure 3: Loans and Advances of the Household and Business Sectors

Source: Bank of Botswana, 1997.

The growth in commercial bank credit was stagnant until 1979 when it expanded to grow at an annual rate of 19.8 percent between 1979 and 1981. Then it declined in the following year due to the imposition of credit ceilings and interest rate increases of 1981. It also declined due to the completion of the construction of the Jwaneng mine, which reduced demand for imports associated with the project (Bell, 1987). Credit expansion continued after the removal of restrictive measures, to grow at 25 percent per annum in the 1983-1997 period.

An evaluation of the sectoral distribution of credit shows a pattern of demand dominated by two sectors, the household and trade sectors.

The proportion of total credit to the household sector increased from 7 percent in 1976 to 49 percent in 1997. This was followed by the trade and business sector at 13 percent each in the same period. The share of credit allocated to the agricultural sector accounted for 19 percent in 1976, but declined to 2 percent in 1997. Whilst the decline in credit to the agricultural sector is explained by occasional drought spells, the sector also obtains credit from other financial institutions, especially those created by the government, like the National Development Bank. On the other hand, parastatal organisations account for about 3 percent of total private sector credit in 1997.

The share of credit to the manufacturing sector was low over the same period. The sector accounted for 6 percent of credit in 1976, but later increased to 8 percent in 1997. The share of credit allocated to the private sector, excluding the household sector, was 66 percent in 1976 but declined to 61 percent of total credit in 1994 and has since declined further to 47 percent in 1997.

The share of credit allocated to the private sector declined whereas credit to the household sector has continued to increase. But credit allocated to the private sector was larger than credit channelled to the household sector until 1997(See Figure 3 above).

However, this refers to credit allocated by the commercial banking sector only. It excludes credit allocated by parastatal organisations.

The increase in the growth of credit to the household sector is due to the increase in incomes (paid employment and government transfer payments), which afford the opportunity to pledge security.

The greater proportion of commercial bank borrowing has also tended to meet the short end of the market, a large part of which is the household sector. The structure of commercial bank lending is biased to the provision of short-term loans and advances. The single largest form of lending is through overdrafts. Lending by overdrafts averages 30 percent of total loans and advances over the period 1986-1995. This is more than twice the share of credit allocated for loans with a maturity period of 3-5 years (12.5%) over the same period.

This pattern of lending becomes even clearer when we consider the ratio of credit with a maturity of less than 3 years. This accounts for an average ratio of 69 percent of total loans and advances per annum. This is against an average ratio of 18 percent per annum for loans and advances with a maturity of 5 years and above. It is clear, therefore, that the commercial banking system alone cannot provide for the needs of long term investors in the market.

The response of policy to deal with the results of the analysis of the sources and uses of funds in the financial system has been to recommend that the household sector to save for investment. What is important is to actually have an idea of the motives to save by the household sector, motives which may not coincide with macroeconomic goals of raising national savings.

The above section has attempted to link financial development, particularly saving mobilisation with economic growth of the non-mining sector (economic diversification). It shows that the economy of Botswana developed as a result of large inflows of capital into the mining sector. This allowed for the accumulation of savings that are comparable to the saving rates evident in the fast growing East Asian economies (Bank of Botswana, 1997). The Botswana banking system has since the 1980's experienced excess liquidity because of the lack of profitable investment opportunities, and most importantly entrepreneurial expertise.

The domestic investment ratio has declined consistently during the last ten years at least because of the limited absorptive capacity. On the other hand the saving ratio has increased. It is concluded that because investment is dependent on investment decisions and the policy of saving mobilisation will have no effect on such investment behaviour. Moreover, resource availability is not a constraint on the growth rate of the economy. What could be done to promote economic diversification is carry on the reforms to the financial system and develop further instruments to tap the accumulated savings in the economy (Motsomi, 1997). This is the portfolio effects or second round effects of economic growth on saving that are discussed in McKinnon(1973). No amount of forced saving will increase investment in the economy (Reinske, 1997). It is only attempts at improving opportunities for lending to small-scale investor who are excluded by the domestic banking industry that will support economic diversification.

Recent Institutional Context of Growth

Changes made to some fundamental aspects of the democratic governance/multi-party system, such as reducing the voting age, establishing an independent electoral commission, limiting the tenure of the executive president, removing various forms of discrimination, especially against women in order to meet new challenges and defuse grievances over electoral/constitutional flaws articulated by the opposition and some civil society organisations. Various forms of the new institutions, such as the Ombudsman, the Anti-corruption Commission, etc, have complemented existing instruments of public accountability. Two general parliamentary (and by implications presidential) and local government elections have taken place in 1994 and 1999 - all won by the ruling party. The elections illuminated some issues related to shifts in political support and changes in interests. Until 1994, the ruling Botswana Democratic Party (BDP) had won each parliamentary election with an overwhelming majority and strong rural support. 1994 looked like a turning point with the opposition winning one-third of the seats in Parliament and almost all the local government elections in major towns. Although the trend was reversed in the 1999 election (with a divided opposition winning only seven

Parliamentary seats and lost ground in some major towns), the period has gone down into the country's history as one of land marks. It is a period of tremendous growth for the resilient independent press and civil society. Issues of poverty, unemployment and inequality were articulated and widely talked about. Sharp differences in interests among the ruling elite emerged and the government started for the first time bailing out a wide range of batswana business interests, rural and urban based.

The government planning process and national development plan implementation has continued to play pivotal role in development policy and the management of aid resources. In contrast to the socialist model, the plans serve to guide public expenditure and investment, not control the economy. Donor confidence in government administration helped maintain aid level and reduced/defused donor demands for costly parallel management structures (Maipose et. al 1996). The most significant policy shift has been the change in the overall development strategy from state-led to private sector led development through, among other instruments, the various forms of privatisation and cost recovery measures; and enhancing productivity on the public sector by instituting various forms of performance management systems (PMS) in the public sector. It should be recognized the role of the key institutions, e.g. Ministry of finance and Development Planning and the Central bank. These have been very pivotal in ensuring continuity in policy implementation.

The government adopted the policy of enhancing sustainable economic performance and sustainable government budgeting adopted during the period of relative stagnation in early 1990s. The base case scenario included good prospects for the diamond sector whose output was planned to double at some existing mines (Orapa and Jwaneng), economic diversification and sustainable fiscal situation through cost recovery measures and broadening tax base and increasing use of VAT. The same period led to adopt new policies or to intensify the measures for economic diversification and enhancing savings and investments. Measures included further liberalisation of exchange rate and interest rates, and concessional tax reforms - all in order to increase domestic output of tradable especially non-traditional exports and mobilise domestic savings and investment.

Review have been undertaken for some broad-based growth promoting projects, such as the Rural Development Policy; implemented in 1973; the Tribal Grazing Lands Projects, (TGLP) launched in 1975; and the Financial Assistance Policy (FAP); General policy of government leading to public enterprises; and investment of budget surpluses and foreign exchange reserves, etc. Some of the policies were long due for review - making one of Bate's questions relevant: why should reasonable "men" adopt let alone sustain persist with inappropriate or ineffective policies? The answer lies in people or interest groups with tangible vested interests in maintaining those policies.

3.0 GROWTH, INSTITUTIONAL AND INTEREST ISSUES

Explaining the process of economic development through the institutionalist thrust and its linkages to interests is not new. Many empirical studies, some of them cross-sectional, have shown that institutional quality is important for growth, and the relationship with growth is a complex matter with many different channels of influence (Bates and Krueger, 1993; Aaron 2000). Using the five political variables presented by Macartan Humphreys (2000) for comparative cross-country analysis for explaining African growth, Botswana's actual performance has been positively above African average and standard deviation. Actually, it has emerged well off in all marginal and conditional distribution of five political variables - the executive measuring democracy, strikes, demonstrations, coups and guerrilla wars.

The analysis of evidence on significance of institutional issues highlights the following four inter-related factors. The first is the institutionalization of a stable and largely less corrupt democratic system of government with good (exemplary) leadership and how this has enhanced public accountability and transparency. Second, the established system of national development planning and its integration with annual budgetary process. Third, good state financing/extractive capacity and how together with diamond/aid fortunes have loosened financial and to some extent manpower constraints on development. Fourth, prudent macro-economic management and its implications for managing “national fortune” ensuring macro-economic stability, while at the same time distributing and redistributing benefits of growth to the economy and wider society in a manner that avoids budgetary crisis and minimizes adverse consequences of the “mineral led economy” syndrome. Other elements of good governance/management need not be elaborated upon at this stage, but how growth and democracy and interests have interacted deserves illustration.

It is important to note that is that the strategy of "state-led" development and national economic planning, which Botswana implemented successfully, is not a strategy unique to Botswana. Many African countries adopted more or less the same strategy. But the strategy has worked very well in Botswana and the country has prospered under a democratic system of government. The same strategy is associated with, and it is now blamed for, the general economic crisis in many African countries most of which have been under authoritative/one party regimes. However, following the dominance of "neoliberalism dogma" and the collapse of many centrally planned economies, the emphasis on the role of the state in development has currently shifted towards attacking the development theories of the 1950s and 1960s as well as introducing, in a new style, the argument of "government failure" and the need for a minimalist role for the state to leave sufficient space for “market-based” socio-economic development (Stern, 1989; Huntington, 1994; World Bank, 1992; Hope & Kayira 1997). The current wave of political and economic liberation has cut across African countries. Partly in line with the new school of thought on development policies, and mainly out of the internal review of the old development strategy, Botswana, too, has followed the new thinking about the role of the state in socio-economic development by re-orienting the overall strategy from state-led to private sector-led development. The crucial question is: what are the factors, which accounted for Botswana as a successful developmental state so far, and what are the common challenges and lessons for the region?

4.0 LINKING FACTORS OF BOTSWANA’S DEVELOPMENT SUCCESS

The explanation for Botswana's "success story" and the outlook for the country's future prosperity tend to oscillate between emphasis on the "good luck" factors, on the one hand, and the "good management", on the other hand (Harvey & Lewis 1990:6-7;

Tordoff 1993:282). The current President (when he was the Vice President) reasserted this observation in his address to the International Conference on Southern Africa and East Asia in Gaborone, January 1991. He observed that:

> Indeed, while it is recognised that Botswana's development record reflects "good luck" to a substantial degree, we are also proud of the reputation that has been established for "good management" on part of the government ... Although the national diamond endowment has for the past 15 years or so been the main element in the "good luck" factor, it is nevertheless recognised by those who are well acquainted with our country that we have striven with good effect to minimise adverse consequences of the 'mineral led economy' syndrome (Somolekae 1998:29).

It must be added that the two factors -- "good luck" and "good management" -- are inter-related, but independently constituted.

To start with, the achievements owed something to "good fortune", but more to careful or "good management" (Tordoff, 1993:282). Some other countries which enjoyed a windfall of resources immediately after independence (such as Zambia and its copper, and Nigeria and its oil) did not perform nearly as well as Botswana did (Harvey & Lewis 1990; Maipose et al 1996:440-441). Indeed, the reader does not need to be reminded that in some African countries such as Zaire (Democratic Republic of Congo) and Angola natural "fortunes" were either transformed into personal riches and externalised into personal foreign bank accounts or/and mismanaged and dissipated into regional/civil wars. Some argue that Botswana is so special, that little can be drawn as general lessons applicable to other countries. But this can be said about most countries. Botswana represents an odd case, at least in Africa, of rapid economic growth with market economy formula and good democratic governance. The important lessons and challenges for the region seem to be less about the "good fortune" factor than the elements of "good management" and these are analysed in the next paragraphs.

4.1 The Elements in Good Luck Factors

The elements in the good luck factor are basically four, though a detailed survey could reveal some other complementary issues. These are the national mineral endowment, particularly diamonds; the production and marketing of diamonds within the most durable and successful producer/marketing cartel run by De Beers, the Central Selling Organisation (CSO); inflow/impact of foreign aid; and small and basically homogenous population. The "good fortune" element in terms of the natural mineral endowment or exploitation of mineral worth, such as copper, oil, gold and also diamonds, applies also to many African countries. However, the diamonds marketing cartel under the control by De Beers (unlike for copper and oil under their respective producer organisations) has now been in a continuous operation for over six decades; and it is one of the most successful commodity buffer stock arrangements in the world and it is also the most durable producer cartel (Jefferis 1998:306-308). Botswana has not suffered an extended period of depressed demand and low prices of diamonds and has enjoyed political stability since independence. This aspect goes a long way in explaining why "diamonds are forever" in Botswana, at least so far. However, it would be rather naive, certainly not realistic, to compare Botswana's diamond-led boom with copper-led and oil-led booms in Zambia and Nigeria respectively. In these countries poor economic performance has been partly attributed to a variety of adverse external shocks and more particularly depressed export earnings for decades or, at least, many years. This may be qualified as "bad luck" for those countries. In fact, Botswana has had "bad luck" too – serious profitability problems with regard to the BCL copper-nickel and soda ash mining, which commenced operation in 1973 and 1991 respectively. These projects have been a drain on government revenue during many years of their operation (Gaolathe 1997:409).

With regard to foreign aid Botswana, like all Sub-Saharan African countries, has been a long term recipient of foreign development assistance. As an aspect of "good luck", the country has had the highest per capita aid in the region, and aid in the form of grants continued to flow long after Botswana attained middle-income status (Maipose et. al 1996). But unlike the situation in most African countries, which have become increasingly dependent on aid with disappointing impact, Botswana has managed its aid resources effectively and sustained economic growth with decreasing dependence on aid (Steven 1981; Carlsson et. al 1996; Maipose et. al 1999). The main point is that the experience in other African countries with diamond endowment and aid inflow but have governance problems, such as the war torn Angola and Sierra Leone, has been quite different. Many ordinary citizens do not know who benefit from the "diamonds fortune" in those countries and few benefits from foreign aid. In terms of country size, Botswana is a large country - mainly arid and drought is a regular occurrence with scarce arable land - conditions that make communication difficult and agriculture a precarious undertaking. But the country's population is quite small and although there are different tribes (seemingly dominated by tswana speaking) the population looks largely homogeneous at least in the sense that 'tribalism' and 'sectionalism' are not sharply used to explain electoral behaviour and leadership competition in Botswana. With these observations one can appreciate, to some degree, advantages of "small country" effect in key macro-economic indicators, and managing of people relatively easier than is the case in large but ethnically divided population in many other African countries. This background partly explains factors behind high GDP per capita, frustrations regarding broad/agricultural-based poverty reduction strategies, while multi-party political system and good macro-economic management contained various interests - thereby managing not just the country's wealth but also the diversity of its people. Thus, the context of the "good natural fortune" is crucial.

Additional elements in the "good luck" factor relate to the fact that Botswana virtually has no public debt burden and some analysts point their fingers at the benefits derived from the country's close economic ties with South Africa. Botswana has no debt burden because of two main reasons. First, and foremost, this is due to diamond "windfalls" and how this has been managed. Second, because it was classified as very poor country at independence and the implication of this on the country's debt profile. Nearly all Botswana's foreign aid was in the form of grants complemented with very concessional loans, while the country's membership in Southern African Customs Union (SACU) and the Rand Monetary Area restricted its discretion in monetary policies. Thus, following the country's graduation to the middle income status, Botswana has had a very low external debt burden and the profile of that external debt is basically that of a poor country. Fortunately, debt management – servicing or choices to repay – takes place when Botswana is a prosperous middle-income country. Given this situation, debt service costs has not impaired the ability of the Botswana government to operate normally and the country can even choose whether or not it makes economic sense to repay off its external debt. This again may be contrasted with Zambia, which was a middle income country in 1960s and 70s. She could not qualify for concessional loans, and borrowed from the commercial windows including preferred creditors (such as the World Bank and the IMF) who until quite recently never rescheduled/cancelled their debt. Much of the acquired debt was short-term in addition to increasing internal debt – all in the hope of copper prices recovering soon. As an aspect of "bad luck", copper prices remained depressed for long time. Unfortunately, Zambia has a debt profile of a middle income country and has to service or repay its external debt when the country, ironically, has been reclassified among the poor countries of the world. The point is that debt-service costs can impair the ability of the borrower to operate normally.

Some observers have argued that Botswana benefited from its long close “economic ties” with South Africa and the embargo/sanctions on South Africa - benefits which may be construed as aspects of good “luck/fortune” factor. This is a debatable issue - raising some circumstantial benefits exploited to national advantage by good policy choices and also potential benefits which were not taken advantage of due to structural/in-built constraints. It is well documented that a multi-party Botswana state, surrounded by racially dominated white minority regimes in 1960s and 1970s and as part of the politically troubled Southern African region and aspirations of the then Southern African Development Co-ordination Conference (SADCC) to reduce dependence on South Africa, received generous international support and sympathy in the form of aid which proved critical for development. Furthermore, from independence up to 1976 the determination of the monetary and part of fiscal policies remained under the command of the South African government with important implications for the young nation given its serious financial and manpower constraints at that time. One of the crucial advantages was that the arrangement restrained the Botswana government from financing budget deficit by money creation in early period when the country was desperately in need of cash (Harvey 1997). When Botswana chose to leave the Rand Monetary Area and introduced the Pula in 1976, the government never resorted to borrowing from the

Central Bank because the transition coincided with rapid growth in government revenue, complemented by prudent macro-economic policies for which the country leadership gradually prepared itself for.

The extent to which the country's rapid growth and general development benefited from international sanctions on South Africa is rather controversial. Benefits where expected in regional infrastructural aid and diversion of private (multinational) investment, seizing opportunities in the peripheral states (Becker 1987:147). As a member of SADCC, Botswana benefited from infrastructural foreign aid targeted at helping South Africa's neighbours to reduce their dependence on South Africa. However, there is overwhelming evidence to show that Botswana was not able to attract significant foreign investment following the embargo on South Africa because of the fundamental constraints arising from the country's membership in SACU, dominated by South Africa and partly due to small domestic market and internal policy/institutional constraints (Mpabanga 1997; Ndzinge 1998; Siwawa-Ndai 1997). The level of SACU common external tariff and also the use of excise taxes and other non-tariff trade barriers reflected interest of South African producers and market - problems which have not been resolved yet. Botswana market was too small to attract foreign investors which could not take advantage of the regional market because Botswana was and is still sceptical of joining the oldest regional common market - COMMESA, while SADC which Botswana joined was not and has not yet become a fully fledged common regional market. In addition to constraints associated with well-documented industrial polarisation and trade-distorting effects within South African dominated SACU, it is important to note that South Africa has tended to frustrate new industrial development in the region (Mayo, 1986). The evidence is enormous including the recent frustration and subsequent closure of the Hyundai motor vehicle assembly plant in Botswana, which contributed significantly to the value of the country's non-traditional exports - destined for South Africa auto market. The industry was closed and re-located to South Africa as a result of what looked like a combination of trade war or South Africa's sabotage and unethical business deals by foreign investors taking advantage of the country's generous government financial investment support. South Africa's relationship with the region - for a long time in SACU and now in SADC - has been described as “a selfish regional hegemon,” underpinned by calculated efforts/measures to obstruct industrial development, especially the development of the manufacturing sector in other countries in the region, except investment in the *extractive* mining sector (McGowan and Ahwireng-Obeng 1998).

The arguments above give some rough indication of the relative importance of the "good luck" factor elements and the extent to which Botswana exploited them to national advantage - illuminating significance of policy choices and context of “good fortune”. Many of these "good luck" elements constitute the context or experiences, which may be or may not be applicable to other countries. How Botswana has taken advantage of the favourable events and other aspects, which constitute "good management" or importance of policy choices factor is the primary concern of what follows.

The Elements in Good management Factor

The elements in the Good Management factor are many and basically different, though inter-related. These are the experiences of Botswana which offer many practical lessons and pose challenges for the region. It is one thing to have "good fortune" or receive windfall foreign aid resources, and it is another thing to put one's fortune to good use. Indeed, many of the favourable events -- the "good luck" elements discussed above -- could not, on their own, have transformed Botswana at all. They had to be exploited to national advantages. Experience elsewhere and analysis of Botswana's development policies makes one point clear, which is the main lesson and challenge for the region. *The quality of domestic economic policies* that a government pursues and political stability (made possible by good governance) have an inordinately greater influence on a country's economic and social progress than any form of "good fortune" or external assistance. Good luck, like foreign aid, can have an important catalystic and supportive effect, but ultimately, the quality of domestic policies and general stability are what count most (Brautigam, 1996). What follows is in the nutshell an account of "managing good fortune" in Botswana and this is regarded by many analysts as the most important factor in explaining the country's success story. It brings to the surface the key lessons and challenges drawn from Botswana’s experience. What are the elements of good management?

National Development Planning and its integration with the annual budgetary process has been the foundation of Botswana's development management machinery, and the basis for managing its windfall gains -- mineral rent and foreign aid (Stevens 1981; Raphaeli et al 1984; Maipose et al 1996). The country relies on a six-year planning cycle, with mid-term reviews to update the plans in response to changes in the economic and political context. National Development Plans, are essentially plans for public spending and human resource use, and the Ministry of Finance and Development Planning (MFDP) plays a central role. On the basis of the projections underlying the Botswana macro-economic model (which includes forecasts for economic output and growth, employment, foreign trade, government revenue etc.), MFDP derives three main ceilings for the public sector. These are the skilled labour ceilings; the recurrent expenditure ceiling (which in recent years must be financed out of recurrent non-mineral revenue) and the development expenditure ceiling (Jefferis 1998). The National Development Plans are constructed around the programmes and a "shopping list" of projects for which finance is derived from own current income, mainly mineral rent or sought from donors. For effective aid management and co-ordination, the donors are asked to support (and have flexibility to choose) projects that are already identified as national priorities in the plan. This increases national project ownership and avoids problems elsewhere in Africa where donors have allegedly "imposed" or taken over design of key policies/programmes (Van de Walle & Johnston 1996). In Botswana the plan and how it is enforced ensures that programme and projects address government priorities.

We do not have to go into details about how the system works. However, it is a common view among donors and development analysts that the planning system has worked relatively well in Botswana as opposed to many instances of failure in many developing countries (World Bank 1984; Harvey & Lewis 1990; Maipose et al 1996). A review of literature on the nature of development planning and its institutional, operational and procedural relations with budgeting, suggests that a government's budget is a key instrument in converting a development plan into a programme for action (Herman 1962:319; Waterston, 1979:201). In Botswana, this is structurally enforced by putting overall economic, financial/budgetary and planning responsibilities for the government under a powerful Ministry of Finance and Development Planning with a considerable degree of career continuity for largely merit-based staff. In this way, planning in Botswana is not an academic exercise of little operational value and it is a means of enforcing accountability. It also explains why the government has done relatively well to redistribute mineral revenue to the wider society and economy especially with regard to investment in physical and human capital and targeted subsidies without adverse consequences of the mineral led economy syndrome. Although conventional national development planning has fallen out of favour in policy circles, the idea of integrating planning and budgeting under one ministry seem to be a relevant lesson for other countries, as elaborated upon later.

Good governance record, underlined by the nature of Botswana's political system and the quality of its political leadership, is another important factor which explains good management. The development of a stable and relatively non-corrupt multi-party democratic system of government, coupled with good leadership quality, entailed putting in place administrative system that provided an enabling environment for development. It also reinforced national vision in government plans and helped ensure accountability. Compared to rapid growth under authoritative regimes in china and the Asian Tigers and new fragile/emerging democracies in many African countries, multi-party democracy in Botswana seem to have been institutionalised. The ruling party, in power since independence, has had unimpeachable electoral legitimacy, the product of fair and honest regular elections. This, in our view, seems to be “a continuing vote of confidence” in the ruling party, its leadership and policies. Some critical political observers, such as Ken Good (1997; 2000), have interpreted continuation of one-party in power as one of the main limitations of Botswana’s democracy which has not been seriously tested. This critique is probably applicable to all liberal democracies where governments did not change for a long time such as Japan, and this is probably one of the main reasons for explaining sustainability of political stability and good economic management in Botswana.

Given the nature of political context in Botswana we are inclined to argue that the "national fortune" has not been mismanaged and the strategy of state-led development has worked well partly because politics have been relatively free of corruption and patronage, common in many African countries. Botswana is often cited as the foremost example of a stable multi-party democracy in Africa, which maintains freedom of speech, press and association and most importantly property rights and rule-based governance. Judiciary is independent of both the legislature and executive branches, and Botswana has one of the best human rights records in Africa. A participatory and transparent political system has combined with the good and disciplined political leadership to moderate/limit corruption and most importantly enhance public accountability.

The question is: Why have these factors evolved and worked in Botswana? The country has a strong tradition of participation and consultation at all levels of public life from the village to central government, and this has strong roots from *Tswana* custom of holding "town meetings" known as the *kgotla* which still exists and is part of the local consultative network (Lekorwe 1989:217). Many analysts and Batswana themselves acknowledge the exemplary ethical leadership and general foundation made by the country's first President, Sir Seretse Khama. He firmly established a precedent for high ethnical standards, a strong and relatively independent but accountable civil service, and a developmental orientation of government. These attributes have been carried on and built upon by his successors (Tordoff 1993:281). Although there are cases of corruption and probably increasing (Good 1994), there are also cases of suicides (for fear of obvious consequences), resignations or dismissals (on matters of principle/accountability) and imprisonment involving politicians and government officers. The point is that state action remains largely predictable for ensuring public accountability.

Thus, the "checks" in place appear to have worked relatively well so far in Botswana. It must be added that the country has been probably luck to have produced honest and committed leaders so far. Hence, the general trust in government or the leadership to spearhead development and handle "national fortune." This emphasises the importance of good governance and leadership quality as some of the key lessons for many countries in the region. But it also raises a challenge for Botswana future leadership to rely/hold on exemplary leadership or/and decide to empower Batswana economically through privatisation to reduce over-dependence on government and enhance the new strategy of private-sector led development as a sustainable route. There is a strong feeling among the Batswana that the country is rich and they acknowledgingly rate it among a few richest countries in Africa, but they are also quick to qualify that the country's wealth/money is in the hands of the government and to some extent foreigners, and not the Batswana. They point to absence of indigenous business people outside the cattle industry, disappointing high level of unemployment and noticeable poverty among the people as evidence.

The country's evidence on governance is illustrative within the region. The general poor quality of governance and budgeting in many African countries led Hyden (1983) and the World Bank (1992) to note that in African countries, which are characterised by weak policy and institutional performance (weak administration) and a culture of personal and ethnic loyalties, government failure has proved to be a bigger problem than market failure. African development analysts have also increasingly acknowledged poor governance as the main problem facing the region (Lipumba 1994:3; Elbadawi 1996). Although one cannot prove that the development of a stable and largely non-corrupt democratic system of government in Botswana has contributed to good economic performance, the available evidence suggests that the two are more likely to be complementary than competing. This is a lesson that has implication for the region and in many parts of the Third World. On the positive development, many African countries have now put in place multi-party democratic systems and good governance is being enforced as one of the key conditions for getting foreign aid. On a cautious note, democracy and good governance have yet to be institutionalised – not imposed from elsewhere and the region has had reversals in countries such as Nigeria, Sierra Leone, Luanda and Angola.

<u>Prudent macro-economic management</u> including emphasis on openness, macro-economic stability and recurrent funding, for which Botswana has acquired a good reputation, is regarded by many analysts to have played a key role in the country's success (Harvey & Lewis 1990; Hill and Knight 1999). We can just highlight a few

dimensions of sound economic management. First, Botswana's main economic development strategy has been to exploit the country's mineral wealth, and invest the proceeds in improving social and economic conditions and creating new economic opportunities. Strikingly, the country has been able to maximise the domestic benefits of its mining development, increase its domestic savings and investment, and diversify (rather than suppress) the non-mining economy, while at the same time mitigating the potentially adverse effects of mineral-led development syndrome. Second, the government has had a relatively good sense of priorities and a conscious policy of reviewing key policies and programmes in light of set targets to appreciate limits and opportunities consistent with expected revenue and absorptive capacity of the economy. For example, when Botswana's economic and fiscal prospects were expected to improve dramatically, the government established in the first year of budgetary independence the Public Debt Service Fund (PDSF) and the Revenue Stabilisation Fund (RSF). These funds were conceived as mechanisms that would, respectively, enable the country to service its debt obligations, and cope with temporary revenue shortfalls that might arise from fluctuations in international mineral markets, drought and other contingencies. These funds turned out to be good vehicles for prudent management -- simultaneously working as a device for siphoning government surpluses away from the recurrent budget and as a source of funding for the capital formations and public debt management. (Faber 1997).

Third, management of inflation and current account has been good over the years, consistent with a broad counter-cyclical policy of managing booms and slumps. Although the Botswana economy has, to some degree, experienced booms and slumps, the latter have not been dramatic and the government has been relatively successful in avoiding extreme episodes of government led inflation which actually has been relatively low (Hill and Knight 1999). A conscious and deliberate policy in this regard, illustratively included bold decisions not to award salary/wages increases for public servants during the sensitive election years in 1992 and 1999 because of projected deficits, and yet they could have easily done so and increase the deficit which could be financed through past savings. The government's self-imposed adoption of orthodox stabilisation and adjustment policies is viewed as illustrative of strategic state intervention, and this is in sharp contract to "forced adjustment reforms" in some other African countries.

Lastly, the government appears to have managed well its budget surpluses, and foreign exchange reserves -- investing and using them in ways that have increasingly proved beneficial for the country. For example, Public Debt Service Fund (PDSF) became the largest source of loan funds in Botswana -- lending primarily to public organs such as state owned enterprises and local authorities. The fund has grown to comprise assets far greater than total public debt and thus could actually redeem the entire government debt if it were advantageous to do so (Faber 1997:323). As international reserves began to accumulate rapidly in the 1980s, it was decided, among other options for reserve management, to invest the reserves in excess of the levels required for the primary purpose of facilitating the timely meeting of payment obligations. The idea of saving mineral rent and transforming them into financial asserts has paid off handsomely -- yielding investment income which since 1993 account for the second or third largest source of government revenue (Mohohlo, 1997). Since minerals are a non-renewable resource, the government also adopted a policy of "sustainable budgeting", using mineral revenue to finance only investment not recurrent expenditure (GoB 1994).

Obviously, prudent economic management is an element of "good management factor" which needs to be taken seriously for the region. Consequently a <u>virtuous</u> cycle emerged. ‘In contrast, macro-economic instability has engendered a vicious cycle in all too many African states’ (Van de Walle & Johnston 1996:89). Zimbabwe case is currently illustrative of how poor economic management on the part of the government can reverse growth pattern of what used to be a strong regional economy and lead to economic crisis. Another aspect about country’s development, which is important to note, is the way the Botswana state has performed in extracting resource from the economy. This deserves some explanation as a separate issue.

STATE EXTRACTIVE AND SAVING CAPACITIES

<u>The degree of state extractive and saving capacities</u>, which the Botswana state has displayed, has been incredible. In fact the level of performance is far beyond what many countries have been able to do and this applies even when one compares Botswana with

the countries in developed and developing world (Bank of Botswana 1998: World Bank 1999). The concept of state extractive capacity, as used here, and some crucial indicators of measuring it follows the conceptual framework by Brautigam (1996), complemented with some ideas by Vito Tanzi(1990) on fiscal vulnerability and Jose Cheibub (1998) on factors that affect extractive/tax capacity. State extractive capacity, as defined by Brautigam (1996:83) 'is a measure of the ability of a government to raise the revenue it needs to pay for the expenses of implementing its policies and goals', and it is analytically seen as one of the four dimensions of state capacity - regulatory, administrative/managerial and technical. Some development analysts regard this as the most important elements of the state capacity mainly because financing capacity can be used to increase other forms of state capacity (Skocpol 1998:17). Furthermore, Prest (1975) argued that the critical gap between load and capacity in developing countries can be explained by constraints of taxable capacity and tax effort.

Applying Brautigam's ideas, the main indicators of extractive capacity are: 'the ratio of revenues to Gross Domestic Product (GDP), ... the relative weight of different categories of revenues, and the ratio of fiscal self-reliance - aid receipts compared with total domestic revenue' (Brautigam 1996:84). The simplest measure of state extractive/taxable capacity is the ratio of revenue to GDP as presented in table 3.1 by way of comparison, and this method is widely used, especially in public finance literature. Other indicators may be used to assess degree of diversification and stability. Some analysts include the degree of vulnerability or exposure to external shocks. Fiscal vulnerability measures the proportion foreign sector income in total revenue and proportion of foreign debt that is public or and debt service ratio, the ratio of foreign trade taxes in total tax revenue and the level of foreign exchange reserves (Prest 1975:26-27; Tanzi 1990:25-27). The basic message that comes out of these indicators is to appreciate the fact that many fiscal accounts of developing countries are exposed to many environmental/external shocks, such as changes in export earnings, foreign trade levels for custom's revenue, access to and cost of foreign borrowing, degree of debt crisis and flow of foreign aid, etc. - emphasising the link between national budgets and foreign sector in these countries. Attempting to compare extractive capacities of governments under different political regimes, Cheibub (1998) used factors which affect the magnitude of revenue government collects, such as level and sources of income, transaction costs, government's overall fiscal situation, government's bargaining power and the rate at which the government discounts the future. Interestingly, the conclusion confirmed contradictory arguments about taxation/extractive capacity under different types of political regimes, showing that a regime type - classified as democracy or dictatorship - 'has no casual impact on the extractive capacity of a government, as measured by the level of taxes it collects' (Cheibub 1998:350).

Against the above background, a number of observations can be made about Botswana. First table 3.1 below shows that overall extractive capacity has been quite impressive by regional and probably international standard. During the period 1980 to 1996 government revenue (excluding grants) as a percentage of GDP, has averaged over 50 percent - reaching the peak of 64% in 1988 and the lowest flows of 44% in 1993 (World Bank, 1995; 1999). Second, unlike most other African countries, aid represents a small portion of Botswana's national budget and is hardly significant in other key macro-economic variables (Carlsson et al, 1997:14; World Bank 1999). Financial aid as a percentage of public capital expenditure has come down from near 100 percent in 1960s (Stevens 1981) to 15 percent in 1992, and represents about 5% of total government revenue in the recent statistics (Maipose et al, 1996; 1999). Moreover, foreign debt remains almost insignificant and the debt service ratio is about 3% of export earning . The recent development on the flow of aid is, to a significant degree, a reflection of Botswana as a "phase-out country" for the key donors who have scaled down their programmes or closed their missions with a sense of completed task, and the country is now listed among the new donors for the International Development Association (IDA 2000:13).

Table 1: Government Revenue: Percentage in GDP

	1980	1984	1987	1989	1991	1993	1995	1996
Botswana	34.2	54.0	60.7	49.2	56.7	43.7	46	50.0

Kenya	21.9	20.2	21.0	21.8	24.7	21.8	23	27.9
Mauritius	20.8	22.6	22.1	23.7	23.7	22.4	18.5	18.8
South Africa	23.9	24.7	26.3	31.3	32.8	16.4	31.5	31.8
Swaziland	32.8	28.9	27.7	31.2	32.8	29.2	31.8	32.2
Zambia	25.0	22.1	21.6	11.9	18.6	16.4	20.0	19.1
Zimbabwe	24.1	31.8	33.0	32.4	29.2	30.9	24.8	26.9

Source: African Development Indicators 1994-95 and 1998 (World Bank - Washington 1995 and 1999.

Botswana is also rather unique in terms of state capacity to save and its financial asserts to finance development efforts. Unlike nearly all the recipient of aid in Africa, Botswana, in relative terms, has had a substantial net inflow of foreign exchange in the form of mineral rents, complemented by development aid. Much of these inflows have accrued to the government, and a significant proportion of public revenue in the form of annual budget surpluses and the foreign exchange reserves have been saved - constituting off-shore capital investment or savings abroad (Jefferis 1998:38). This situation has made Botswana unusual in four inter-related respects. First, the economy has excess liquidity vis-a-vis absorptive capacity of the economy and the government has been a net saver - not borrower as is the case in many countries, while households have been net borrowers from the banking system (Motsomi 1997). This is a moot feature. Some people may argue that this is not a "conventional" practice and therefore not sustainable. Some other people can see this as a good attribute for a developmental state - leading saving and investment in the initial stage. In many developed economies, the household sector is the main or net saving sector that releases resources for business and public sectors (Reinke 1997). To encourage private sector savings, especially the household sector, the government has broadened coverage of the Bank of Botswana certificates to attract small savers and a new funded (contribution) pension scheme for public service was effected in April 2001 to afford public officers the opportunity to manage their own pension benefits (GoB, Budget 2001:3).

The second unusual fiscal aspect is that all the main sources of government revenue - minerals, customs union, foreign exchange reserves, and aid - are somewhat denominated in foreign exchange and the tax burden/incidence does not directly fall on Batswana. This is a clear case of “windfall gain” - partly explaining the vulnerability of the whole fiscal situation and why the Botswana government can afford low income tax rates to stimulate growth with long-term fiscal pay off. The third unique aspect about Botswana is the advantage of holding one of the highest levels of international reserves in the world, equivalent to approximately 40 months of imports of goods and services as at the end of December 2001 (GoB, Budget Speech 2002:7). Income from its offshore investment/savings, as already noted, now constitute the second or third major source of government income - a development which effectively makes Botswana an exporter of capital. Forth, the Botswana government has no internal debt and most importantly foreign borrowing and debt crisis have been avoided with foreign debt constituting about only 14% of the GNP and debt service ratio is about 3% of exports.

The underlying fiscal problems, which are interrelated, are the vulnerability of the budget to the external shocks and the over-dependence of the government revenue on mineral rent. The other main concern is the government’s overwhelming dependence on diamond revenue and the extent to which the dominance of diamond-related revenue sources may have retarded the development of other sources of income. This observation led some analysts, such as Wright (1997), to wonder whether or not Botswana suffers from a particular kind of “fiscal Dutch disease.” In the 1995/96 budget, for example, mineral revenue contributed 47% of the total. Together with the revenues from the Bank of Botswana (earnings from offshore cash investment) and the Southern African Customs Union (SACU) the contribution was 82%. In contrast, non-mineral income tax and the sales tax accounted for 6% and 4% of the total revenue, respectively. In fact, one can observe more or less the same trend from 1989 to 2001 budgets. ‘Such a tendency,’ argues Wright (1997:168), ‘can be characterised usefully in the same terms as the socalled Dutch disease problem of exchange rates.' This argument is persuasive, but it needs to be qualified.

The well-known "Dutch disease" effect arises where the rapid development of one sector, in this case the export mineral sector with its substantial revenue to government, crowds out all except the most robust activities, thereby serving to hamper/obstruct new industrial/export development elsewhere, possibly on a permanent basis. In examining this possibility, it must be repeated again that many policy analysts believe that Botswana has avoided Dutch disease with demonstrable efforts to diversify the non-mining economy (Harvey 1992; 1998). Economic diversification policies, if successful, entail broadening up of tax base in the medium to long term. Botswana's exchange rate policy seeks to maintain a real effective exchange rate that is supportive of, and does not disadvantage, macro-economic stability and productive activities in the economy. This is in line with the goals of sustainable economic diversification and employment creations and, therefore, sustainable sources of public income. It should also be acknowledged, as Wright (1997) implies to some extent, that the government in Botswana has not ignored the development of other alternative revenue sources and this is demonstrated by the gradual extension of the scope of the sales tax since its introduction in 1982 and the recent decision to introduce broad-based value added tax (VAT) to replace sales tax (GoB Budget, 1997 & 2001). To encourage savings and stimulate investment and growth in the economy, the government in 1994 and 1996 reviewed the structure of income taxation. It reduced the top marginal rate of personal income taxation from 40% to 25% and the rate for businesses, which qualify for the status of manufacturing operations, is only 15%. While this entailed losing some taxable income in the short-run, low tax rates are known to induce people to declare their taxable income and to encourage savings and investment, and this would eventually widen the tax base and increase revenue. The tax reforms have also given Botswana a clear advantage within the Southern African region in having the potential for establishing itself as a low tax jurisdiction, building on the country's long track record of political stability and prudent economic management.

The arguments advanced above to qualify the assertion of a “fiscal Dutch disease” do not contradict the overwhelming concern for Botswana to diversify sources of government revenue to reduce its overwhelming dependence on one source - diamond. It must be mentioned and emphasised that the foundation of Botswana's extraordinary extractive and financing capacity is, paradoxically, the main cause for some crucial issues of concern and it does not seem to offer clear lessons for the region. First, the government’s high extractive capacity has been mainly due to" windfall gains" without high tax effort. Using the four categories under which Prest (1975:21) divided developing countries, Botswana would fall under the “high capacity and low effort” group, and yet the share or level of revenues government collects is large relative to the economy as a whole. There are some reasons why extractive capacity is high without hard toil. All the main sources of revenue - mineral rent, foreign exchange reserves, customs union and development aid - have been accruing directly to the government with little collecting effort. The government is the main shareholder for the key companies in mining and the crucial public enterprises. Customs revenue, know to be easy to collect, comes directly in “a lump sum” every two years from the SACU headquarters in South Africa, collected on the country’s behalf with very little Botswana effort. Taxes and dividend from profitable big export companies (such as diamond mining in Botswana) require less effort to collect than broad-based income or value added/sales taxes from the agricultural and informal sectors, which now account for a significant share in the GDP of many other African countries (Brautigam 1996:84; Cheibub 1999; Prest 1975).

The most important and related issue of concern is that, over 80 percent or above of the total government revenue in Botswana is exposed to a variety of environment shocks - directly related to the foreign sector in the form of mineral rent, foreign reserves earnings, customs revenue, and foreign aid, while beef exports are prone to draughts. The point is that revenue base for the government is potentially vulnerable to external shocks. Thus, one of the major fiscal challenges for the Botswana government is to diversify sources of government revenue, minimise its income vulnerability, boost collection of non-mineral taxes in line with the proclaimed policy of sustainable sources of public revenue. Evidence of revenue diversification were lacking in the past, but they now include adoption of VAT, the innovative method of earning money from budget surpluses/trade reserves and the related policy of making Botswana an International Financial Centre.

5.0 ISSUES OF CONCERN AND CHALLENGES FACING BOTSWANA

In conventional/traditional usage, good governance, in concept and practice, means a state with an established liberal democracy, underlined by social legitimacy of the state, rule of law (including property rights) and the basics of the market economy or good (liberal) economic management (Dahl 1970; Hyden 1983). Assessed in this context of governance, the evidence above clearly puts Botswana as an example of African good governance/management case that has sustained itself over time, a position which compares well with or may only be contested by Mauritius (Barbara and Terrance Carroll 1989). The country's performance would also deviate positively well above the African average if a cross-country comparison were made applying the four criteria used by Brautigam (1996:83-84) to evaluate state capacity - regulatory, administrative, technical, and extractive.

The idea of good governance has taken new dimensions following the dominance of "neo-liberalism dogma" and the collapse of the centrally planned economies. The concept now clearly denotes a change in the meaning of governance with several contending meanings - referring, for example, to the minimal state, corporate governance, entrepreneurial management and the new public management with enhanced role of the civil society to increase participation by non-governmental agencies (Huntington 1994; Kooiman 1993:1; Rhodes 1997). Good governance under the current thrust retains the overall liberal democratic and economic settings with an emphasis on minimal but strong and competent state that provides a visionary leadership and a "market-centred" state management role, without itself getting involved in the nuts and bolts of production (Hague 2000). In many respects, this is the kind of role that the Botswana government has been playing since independence though, as picked up among issues of concern below, there are fundamental challenges including a debate on the size and extent of government involvement in the economy, and some dimensions of social exclusion/inequity manifested in relatively high poverty/unemployment levels. Thus, analysed from the new ideas and perceptions about good governance and public management, the country has a number of challenges in order to consolidate its established reputation and continue to be a lead example in Africa. There are challenges of loosening some limits of the form of liberal democracy in place; rationalising the role and size of the public sector; diversifying the economy and sources of public revenue; containing the spread of HIV/AIDS which threatens to reverse achievements in human resource development; and transforming the country's wealth into jobs and socio-economic activities that will have the effect of alleviating poverty. It is necessary to amplify some of the issues involved.

On political dimensions and within a liberal democratic framework, close examination of Botswana's democracy reveals some contentious flaws or issues of participatory/representative substance, posing challenges to enhance representation or and countervail centralisation executive/extrabureaucratic powers. Challenges in this respect led a critical political scientist (Good 1997) to describe the system as "authoritarian liberalism," while a sociologist, (Molutsi 1998) characterised the system as a "paternalistic democracy." A number of observations are note-worthy. To start with, Botswana can be described as a "one-party dominant democracy", characterised by a weak opposition, weak parliament and weak civil society (Holm 1988; Molutsi 1998). Although this situation was looked upon favourably during the reign of one-party and military regimes across the continent, the quality of democracy in Botswana is contestingly questioned since the rise of some "infant" but broad-based democracies, such as Namibia and South Africa (Good 1997; 2000; Molomo 2000). However, the situation of one-party dominance in Botswana is not by design but actual outcomes of electoral process of a relatively fair/neutral ground, and one can argue that the new democracies have yet to be institutionalised given the rate of reversals (as happened in Nigeria and recently in Senegal) and constitutional changes to suit individual rulers (as has been the case in Namibia and the current debates in Malawi and Zambia). The ruling Botswana Democratic Party (BDP) – in power since independence in 1966 – has won each parliamentary election with an overwhelming majority and strong rural support. Although 1994 looked like a turning point with the opposition winning one-third of the forty seats in parliament and almost all the local government elections in major towns, the trend was reversed in the 1999 elections. A divided opposition won only seven seats and lost ground in some major towns and the opposition continues to be weak – a deficiency which leads some analysts to describe parliament and local government councils as weak (Molutsi 1984; 1998). For the same reason, there has been no change of government since independence and what would happen is largely speculative, though we should recognise significance of smooth transitions of leadership/presidential change within the ruling party and inevitably at the national level. Clearly, no credible/strong official opposition has existed and the level of popular participation has been questioned (Molutsi 1998; Molomo 2000). The dominance and unbroken rule by one party (BDP) has been critically analysed as not good enough for democracy (Good, 2000), and this experience contrasts sharply with Mauritius where democracy has been tested by changes in governments and coalition/power sharing (Barbara and Terrace Carroll 1989). However, the same evidence can be interpreted, as we have done above, as a continuing vote of confidence in the ruling party and its policies.

Like is the case in many other African countries, centralisation of power and dominance of the executive/president over other organs of government is well entrenched in the constitution. But unlike many new/fragile democracies in the region that may look to Botswana, the president in whose hands all executive powers and co-legislative powers with the National Assembly are vested, is not directly elected by the people and, unlike the prime ministers/presidents in many parliamentary systems, he is not required to hold an elected parliamentary seat (Good, 1997: 3; 2000:21; Molomo 2000; 95). The point being made is that centralisation of powers (including veto powers over the legislature) in the executive president exists and yet the president is not popularly elected. It should be added that the formal provisions of presidential powers has been hardly less substantial in Botswana than in many other African states like Kenya, Zambia, Malawi etc. which were authoritative/one party regimes. However, the main difference, which must be acknowledged immediately and illustrates a case for good governance in this respect, is that there has been no evidence of excessive power abuse in Botswana mainly because property rights and rule-based governance are relatively well institutionalised, and the judiciary has gained a good reputation as an independent legal system and the watchdog of citizens' rights. Moreover, major policy decisions are not made single-headedly. Policy decisions tend to be reached in consultation with cabinet colleagues or through other participatory mechanisms, such as commissions, or the *kgotla* because of the country's well-established consensus-seeking/consultation culture that is deeply rooted in *tswana* custom/heritage. In many other African countries, Presidents have used constitutional powers to detain opponents at will and frustrate the opposition/civil society efforts and private sector (Rosberg and Jackson 1982; Good 2000).

The country's high growth rate record and availability of considerable financial resources have helped Botswana benefit from a state-led "virtuous cycle" – making some difficult choices less painful and facilitating prudent management of the development process. In other words, high rates of economic growth and state extractive capacity enabled the government redistribute mineral revenues to the economy and the wider society – financing high levels of investment in both physical and human capital, while at the same time accumulating budget surpluses and foreign exchange reserves. Clearly, performance legitimacy has been tangible so far – shown in the ability to produce desired results. But in terms of economic resilience and structure, Botswana, like many other African countries, faces three challenges. There is a debate on the size and extent of government involvement in the economy, and the proclaimed need to reduce this role in order to make more space for the private sector. The country faces the challenge of diversifying what is basically a mono economy, heavily dependent on one primary commodity, in this case diamonds. Unfortunately and despite the country's wealth and impressive economic growth rates since independence, Botswana exemplifies high unemployment level of about 20 per cent and high income differentials with gine-coefficient estimated at 0.56 and about half (47 per cent) of Batswana live below the poverty line (BIDPA 1997) - quite close to the African average of fifty per cent. The crucial point is that development policies so far have not sufficiently tackled the problems of high unemployment rate and poverty alleviation, and yet the country's population - currently estimated at 1.4 million - is very small relative to its wealth and geographical size. The situation has hardly changed today regarding income poverty (Mayo 1983; Hope 1996; Good 1999), but there has been tremendous improvement in provision of and access to crucial social services, such as education, health and water.

The country's inability to reduce the current high rate of unemployment and poverty is partly explained by the fact that the mining industry, which is the engine of growth, is highly automated/capital intensive, while agriculture has been a precarious undertaking for environmental reasons and the percentage share of manufacturing in GDP - currently at 4.5 per cent - is still far below the average in Sub-Saharan Africa. This has happened despite the concerted drive to support agriculture and manufacturing including small-scale enterprises development. These indications seem to suggest that the country's success has come to a stage where it must confront a new set of more complex development challenges if its strong development record is to continue. High rates of unemployment and poverty, especially if they outpace economic growth, could become some of the ingredients for social unrest and ultimately lead to political instability.

Socially, the country has to contain threats posed by the spread and incidence of HIV/AIDS - already seen as a major setback in terms of people health and survival, the economy and the country's human resource base. Botswana is presently said to have the highest rate of HIV/AIDS in Africa (Botswana UNDP 1998). Furthermore, the study of the macro-economic impact rate of HIV/AIDS, recently done by BIDPA (2000), predict that growth in GDP will slow by 1.5 per cent per annum as a result of this pandemic, leading to the economy shrinking by 31 per cent in 25 years time and average life expectancy has already declined from 70 to 45 years. While unemployment is expected to decline among unskilled workers, but the report shows that HIV/AIDS will exacerbate the shortage of skilled workers at a time when they are most needed to help effect structural changes in the economy and public revenue will be under drastic pressure due to higher health expenditure and greater demands for poverty relief. Various reports have acknowledged government effort to contain the problem. Government has already taken control measure regarding public awareness, drugs for pregnant mothers and insurance covers for HIV/AIDS related illnesses, but not much can be done apart from prevention in the absence of a cure. Comparatively, Botswana may not have the highest rates of HIV/AIDS and its impact in Africa because these problems seem to be equally spread within the Southern African region (Hope 1999; UNDP 2000). The point is that Botswana, like other countries in the region, is sitting on a volcano whose eruption has already started and whose consequences we can hardly begin to know on the economy and human capital. Hence, the urgency to contain the spread of HIV/AIDS.

Development planning and the strategy of state-led development - regarded as the foundation of Botswana's development management - face two inter-related challenges. First, although economic and per capita growth rates are likely to remain reasonably high for some years to come, the limits of the current state-led development strategy may have been reached (Hermans 1995). According to the Bank of Botswana (Annual report 1993:3) 'the economic slow-down is symptomatic of another and more fundamental concern that current policies are no longer generating as much real growth as before.' Economic growth has picked up significantly since this observation was made, averaging 5 per cent per year with noticeable increase in non-traditional exports and some degree of structural economic diversification (Harvey 1998; MFDP 2000). Structural diversification seem to be promising for the tourism and financial sectors which have doubled their GDP share to 12 percent and 11 percent respectively from 1986/87 to 1998/99. The mining GDP share has declined from 49.3 per cent to its present level of 32.5 per cent for the same period, and prospects for manufacturing sector, whose GDP share remained more or less the same since independence, cannot be ruled out yet. A related issue of concern is that the present scale and scope of the government appear to be unsustainable from the financial point of view; and the sheer size of government has outgrown its capacity for effective policy implementation and monitoring of development projects/programmes (MFDP 2000; BIDPA 2000).

The Botswana government has acknowledged these problems and has embarked on public sector reform process aimed at changing the development strategy from state-led to private sector-led through various forms of privatisation, complemented by a more extensive use of Performance-based (contract) Management Systems (PMS). But practical evidence or some notable examples of privatisation have yet to be demonstrated, while implementation of PMS - partially in force throughout the public sector - has already posed some concerns/challenges regarding the overall reform agenda and how to ensure public accountability (Maipose and Lekorwe 2000). For instance, measurable indicators for "result-oriented" performance in the public service have yet to be developed and agreed upon without overlooking the procedural question of "how" such achievements are made. Debate is also live over the policy to replace the tenured heads of government departments with contract-based appointments and implication of this for the seemingly politically neutral, impartial and merit-based civil service that appear to have served the country relatively well so far. Similarly, implementation of many cost-recovery/sharing measures have been delayed because of a growing public concern over how to ascertain citizens' entitlements and guarantee equality/justice for services, such as education and health, which in the minds of many people Botswana's democratic government (given budget and trade surpluses) can afford and are at the heart of the role of government and its existence. There are questions about how to contain increasing allegations, in the words of a prominent ruling party figure, that 'winners of public tenders for services/goods delivered through extensive use of management contracts are decided at Bull and Bush, and the Golf Club, calculated for rubber-stamping by the Tender Board' (Kedikilwe, P.H.K. in Mmegi, The Reporter 23 March 2001).

The usefulness of development planning - currently viewed with much greater skepticism than before the end of Cold War period and collapse of many centrally planned economies - may be questioned (Stern 1989; Gwartney 1996; Mbaku 1998), though 'one must be careful not to be too sweeping'(Stern 1989:669). Some observers think that the ability of governments to plan comprehensively and effectively tends to be more effective in the early stages of development and that the instrument tends to be less appropriate for a middle income country which, in Botswana's situation, must have lasting economic diversification for sustainable economic development. Indeed, "a diversified industrial structure... is seen by many as a prerequisite of a self-sustaining programme for long run growth" (Weiss, 1988:9), and it makes the economy less vulnerable to environmental shocks. This is very crucial and it has long been recognized in Botswana because both the engine of economic growth (the mining sector) and, as already noted, all the three main sources of government revenue are vulnerable to a variety of external/environmental shocks. Having reached middle-income status, the Botswana economy is relatively grown/matured and complex, but it is not sufficiently diversified. Moreover, the rise in income, the GDP per capita for the current middle-income status, has not been accompanied by a "normal" degree of diversification or a rise in the share of manufactured exports in total exports and decline in poverty/unemployment levels observable in many other middle income countries, such as Mauritius with which Botswana shares similar spectacular development record in Africa, let alone the "Asian Tigers" (Siwawa-Ndai 1997:342-347).

The critical question, against the above background, is whether or not development planning can stimulate sustainable economic diversification and attain other aspirations (in the country's *Vision 2016*) at a reasonable rate/pace of growth to climb to the second wrung!! There has been no critical review of development planning or, at a minimum, internal debate over it. The usefulness of the planning instrument has not been questioned domestically, and it continues to be highly regarded even within the current development strategy, which places greater emphasis on market/private sector-led development relative to the role of the state. That leaves the obvious question: What will be the engine of growth and will the required transition be induced by development planning or the market? The crisis of governance to which many fundamental Africa's development problems are linked has been avoided in Botswana. The country's new development strategy - "governance for market-based economic performance" - entails "right-sizing" the public sector 'through selling of shares or asserts... and by a more extensive use of performance-based management contracts' (MFDP 1997:86). The strategy does not necessarily imply weakening the role of the state in development or abandoning development planning. The new strategy, to borrow the expression by Hague (2000:602), may be described as a 'shift in the role of governance toward facilitating economic performance through a more extensive leading role of the private sector.'

Two inter-related reasons may be advanced to explains why the planning instrument has not been critically reviewed internally. First, in Botswana the government has never tried to plan comprehensively. According to authoritative sources, commitment to planning is intended to put public resources to their most effective use and is not intended to stifle private initiatives but to create favourable conditions in which the private sector has ample scope to contribute to national development (MFDP, 1985:54; 1997:85; 2000:1). This statement has remained more or less the same in all development plans since independence; and so has been the practice. This contrasts significantly with experiences in many other countries, which either attempted comprehensive planning or had mixed economies but with poor economic management - models in which markets/prices played a minimal role. In Botswana development planning represents public sector medium term planning, using annual budgets as instruments for translating plans into action within what has consistently been a capitalist/market economy with concerted support for the private sector development. Second, it is widely acknowledged that development planning, though currently out of favour in policy circles elsewhere, has worked relatively well in Botswana so far. The instrument has enabled the government to manage public expenditure targets - keeping a mineral led economy on a steady growth path and avoiding the well-known Dutch Disease (Hill and Knight 1999; Harvey 1998), and planning has been a crucial instrument for ensuring public accountability. Seen together with other favourable attributes (such as the country's long track record of good democratic governance and investment friendly policies, a well articulated and managed development planning process continued to make Botswana an attractive destination for many donors agencies as well as foreign investment.

Having made these observations it is also important to note, as one of the critical points/challenges, that rapid growth and good performance has not always equated competitiveness and increased productivity (Leith 1998). This observation is supported by the facts that "new dimensions of growth" tend to be associated with "new expansions" and Botswana exporters have operated in one cartel or another such as diamonds in the De Beers Cartel and beef in the EU Market under the Lome Convention, and some nontraditional exports within the SACU. All or some of these "cartels" may not hold for long, given the current waves towards world trade liberalisation. There is also a strong feeling that within a good environment for growth, development of indigenous business class, like income poverty reduction, has been modest, at best. To put it differently, there is a strong feeling among the country's elite that indigenous business people have not participated fully enough in Botswana's "economic miracle", leading to the debates on "citizen empowerment" and the need for "growth with income poverty reduction." Local business fears that apart from marginalising Botswana in global terms, globalisation will make affirmative action for local business more difficult. It is against this background that a generous Financial Assistance Policy (FAP) has continued in place with increasing trend for government "bail-outs," especially for indigenous Batswana businesses, despite extensive abuses by foreign and domestic local investors. It is the same concern which also explains the increasing attention being paid to Small and Medium Enterprises (SMEs). This sector is crucial in Botswana and globally. The sector in Africa has the major advantage of being predominantly owned by indigenous people, creating jobs and empowering women (World Bank 1993a). According to BIDPA (1998) SME's in Botswana account for 50 per cent of private sector employment and 15 to 20 per cent of GDP. But 80 per cent cease trading within five years of operation due to the myriad of problems that face this sector, and many of these problems in Botswana, according to the same BIDPA source, are not financial or collateral requirements, but non-economic such as regulatory environment, and skills/managerial inadequacies.

Thus, the extent to which development planning and state-led development might have frustrated private investment and diversification, including development of manufacturing and small scale enterprises, is debatable - probably by overlooking collateral requirements or "throwing" too much money at the problem, leading to poor business choices. The evidence above - macro-economic and political environment and specific instruments - have been supportive/conducive for private 'initiatives'. What can be appreciated and the government has already taken the initiative in this direction is the need for privatisation and this is potentially an important means of boosting the indigenous private sector to some extent. Despite the Botswana government's strong private sector thrust, it still retains a strong presence in the economy. While there are good reasons for retaining government involvement in areas such as diamond mining - the country's key assert - there are areas where it may now make sense to step back. Unlike other African countries, Botswana has not been under the same financial stress or and pressures of mismanagement associated with public enterprises to make this move, and the number of state-owned enterprises and the size of the sector did not grow excessively in Botswana - accounting for about 6 per cent of GDP (Jefferis 1996). But the government, usually good at anticipating opportunities and problems, has been wise to make sensible economic move before one is forced to do so. A privatisation policy, designed to avoid flawed mass privatisation elsewhere, is now in place and government companies such as Air Botswana and some utilities have featured in this plan (GoB 2000; 2001). An important means both of increasing transparency and facilitating local participation in privatisation is partly through performance management contracts and the development of capital markets. This has been complemented by both promising start made by the Botswana Stock Exchange, one of the best performing emerging markets, and the development of a Financial Services Centre that has been recently launched - building on the country's tradition of political stability, a strong regional currency, enormous reserves and prudent management.

The underlying problems or issues of concern, which are interrelated, are the vulnerability of the main sources of public income and therefore the budget to the external shocks; the over-dependence of the government revenue on mineral rent; and the extent to which the dominance of diamond-related revenue sources may have retarded the development of other sources of income as already noted. To overcome these problems, the objective of diversification requires the generalisation of new "engines of growth" in the economy, and given the small size of Botswana's domestic market, the required form of diversification will have to be export-led. These concerns have been compounded by the fact that the country's impressive growth record has had little impact on unemployment/poverty reduction and HIV/AIDS pandemic threatens to reverse

CONCLUSION

Our interpretation/review of the evidence, Botswana stands out without doubt, as one of the few countries in Africa with an impressive economic growth record, and our explanation endorses a general consensus among the country's development analysts that Botswana has achieved rapid economic growth because it managed to adopt good policies and also to manage the economy and the country effectively. It is the acknowledgement of the country's long track record of good economic policies, prudent economic management and good governance given the supportive institutional framework over the years. The paper is also critical and ends with challenges. The fundamental question is: Why and how?

Pursuing the route of policy influence in explaining differences in cross-country growth performance, our main hypothesis, is that the qualities of both the policy environment and governance, under pinned by the quality of leadership relative effectiveness of the inherited and newly established institutions, combined to positively influence dynamics of rapid economic growth and development. But it has been suggested that although economic growth has been very rapid so far, there are grounds to think that it was not probably as rapid and diversified as it could have been and long-term self-sustaining growth may be questioned in view of a few but crucial negative dimensions/constraints indicated above; and the rate of real growth has slowed down during the last decade or rather in recent years. Major macro-economic puzzles are few but significant. Negatively a growth rate of that magnitude, sustained for a long period, has had limited impact on structural economic transformation/diversification diamonds industrial sub-sector continues to be the main engine of the country growth and foreign exchange earnings while manufacturing remains insignificant. Second, Botswana’s population, currently estimated at 1.7 million, is quite small relative to its geographical size and real GDP growth rate but failure to reduce unemployment level and inequality in income – hence poverty is disappointingly a startling phenomenal. A positive and a remarkable puzzle of international credibility is that Botswana has avoided suffering from Dutch disease; and rapid growth has been sustained and yet skilled and educated manpower over the period was both in extreme shortage and relative scarcity.

APPENDIX A

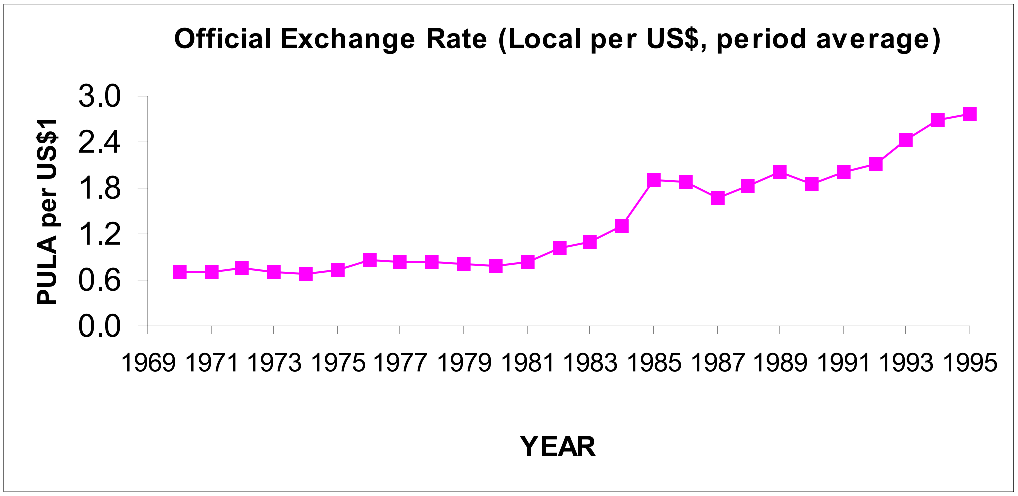
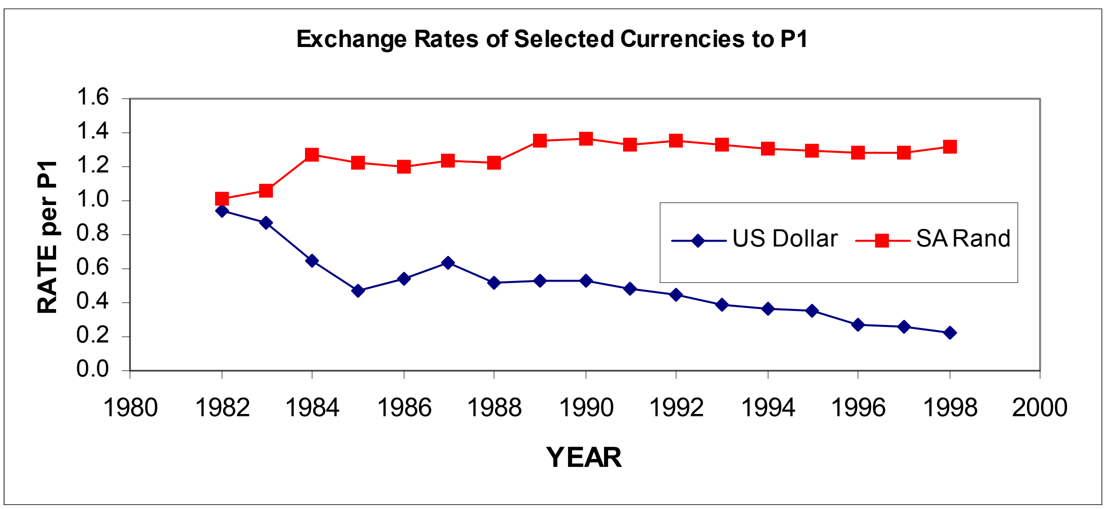
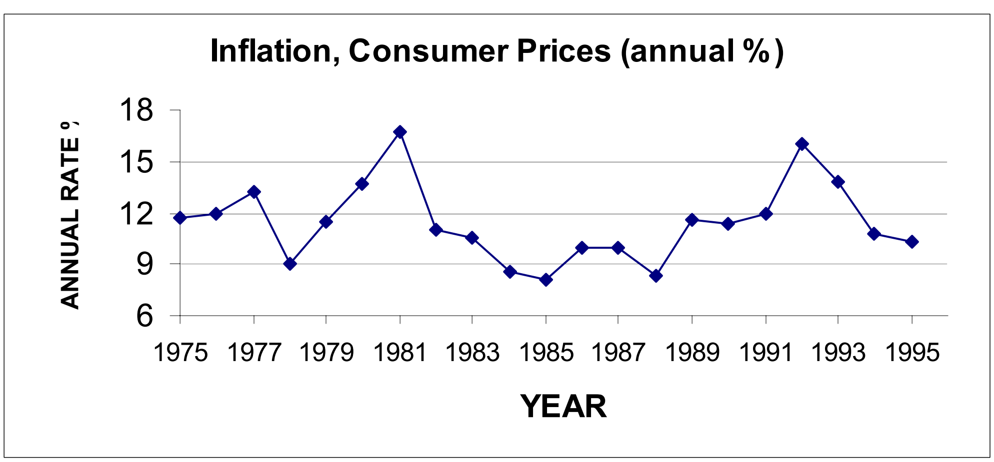


Figure 4.4





Source: Central Statistics Office: Various Bulletins from 1981 to 1996

APPENDIX B (To be reworked and integrated later)

Agriculture & Rural Development

Inspite of major investment by government and donors in the 1970s and 1980s, commercialization and modernization of agriculture has not occurred on any significant scale. Except for a few commercial farms, increases in agricultural productivity and output have not been commensurate with the magnitude of public investment in the sector. The government probably spends more each year on agricultural services, broadly defined, than the volume of the annual output of the entire rural sector. Poor soil and climatic conditions are a major factor in low returns on agricultural investments. Many donors have withdrawn from agriculture projects and the government has increasingly emphasised food security and rural income policy over attempting to increase agricultural output. Rural development, seen in term of social and economic infrastructure, has progressed relatively well and these are the areas in which the government has recently concentrated their support. Specific examples are projects for capacity building for District Councils, rural health centres and water supply. Batswana today are in close proximity with water, health and education facilities. The problems of agricultural development are closely related to the impact on poverty alleviation and issues of equity.

Employment, Poverty and Equity Aspects

Poverty alleviation is an explicit objective of foreign aid and in case of Botswana, it is one of the main planning objectives, explicitly enunciated in National Development Plans and policy statements – the concern for social justice. While Botswana has made wide-ranging development strides and the country is cited as a success story where aid has been effective, there are still too many Batswana who have been left behind without productive employment opportunities and without adequate levels of income. Rapid economic growth and high per capita income is underlined by a significant degree of unemployment, poverty and inequality. It has long been recognized that Botswana has unequal distribution of income whether incomes are measured on a household or individual basis. The unequal distribution of income in Botswana is probably not unusual. But the concern has been on the self-evident continued existence of extreme poverty given the country's impressive record of sustained growth in national and per capita income. There are a number of reasons.

Poverty in Botswana is due primarily to the capital-intensive nature of the economy, the poor productivity of agriculture and recurrent drought, and inequalities in rural land holdings (Keith Jefferis 1997). Government policies and projects were designed and appraised under the assumption that growth would "trickle down" to the poor. Since the mid-1980s, much counter-evidence has appeared suggesting that steady growth in Botswana has not brought significant declines in poverty incidence or severity, but wide disparity in incomes instead (Bank of Botswana 1987; Good, 1992; Jefferis 1997). Indeed, an environment of rapid increase in workforce and skill-intensive and capital-intensive foreign-funded projects (as has been the case with mining) can interact harmfully with government projects that "go for growth". Recovery in the formal sector employment remains weak -- registering marginal growth after a period of rapid growth before the recession started in 1990s. Unemployment remains one of the major problems facing the country. According to the recent data, the rate of unemployment worsened between 1991 and 1994 -- rising from the rate of 14% to 21 % (GoB, Budget Speech 1996.6) and the problem has not been significantly reversed (GoB, Budget Speech 1999).

<u>On employment creation</u>, the mineral industry, the engine of growths has performed rather poorly, to say the least. As can be seen from table 2.5 (Appendix D), the mining industry has not clearly been an effective means for large scale job creation for selected years over the period 1972 to 1995. This is mainly because major mineral projects have been characterised by capital intensity and automation. For example, the Orapa expansion project, which was estimated to cost nearly P1.5 billion to increase production by 100% and the largest project to have taken place in Botswana, provided only 300 additional permanent jobs.

On poverty alleviation, the most recent investigation by the BIDPA Poverty study team (1996) -- using "an inability to meet basic needs, as a working definition of poverty -- showed that the percentage of the Botswana households who had income below the relevant poverty line declined from 49% in 1985/86 to 38% in 193/94. The percentage for individuals fell from 59% to 47%. Although those percentages may still be considered to be rather high, the positive side is that poverty has declined to some extent within a decade. Despite the drop nearly half of Botswana were still below the poverty line. The unsatisfactory performance in alleviating poverty can partly be attributed to the failure of the programmes for agriculture and rural development largely due to environmental factors -- not deliberate lack of concern by the authorities. Botswana has had rural development programmes, such as the Tribal Grazing Land Policy (TGLP) and Arable Land Development Policy (ALDEP) with the support from donors. But the impact has not been encouraging. Further, many aid-supported government projects or schemes ostensibly directed at alleviating poverty were for infrastructure and government capacity building. At the same time it should be noted that basic social indicators have improved considerably in Botswana compared to other African countries. The social infrastructure available in rural areas is clearly superior to that of most countries in the regions (UNDP, 1997).

Thus although income and distribution remain major concerns, the quality of life seems to have improved for the majority of rural people. In its latest attempts to alleviate poverty, the government has introduced an old age pension of P100 per month -- a form of social security for everybody who is over 65 years old; and this commitment is in addition to destitute allowance already given to people who qualify as destitute. This is well-intentioned entitlement programme, but it may be costly to sustain unless economic growth is sustained because it is budgeted under the public spending programmes (uncontrollables), which are politically difficult to reverse. Furthermore, some development analysts think that the degree of poverty is not as acute as is usually presented especially if income poverty is complemented with the capability dimensions of poverty -- viewed as factors, which prevent or constrain the poor from climbing out of poverty. This perspective is persuasive. Many donors-supported projects and public spending (financed by mineral revenue) have sustained high levels of expenditure on services like education, health care, water supplies and so on. While these have no immediate impact on incomes, and therefore do not show up in the poverty conventional measures, they do have a major impact on the quality of live and on people's longer term ability to raise their income and the widespread availability of these public services sharply distinguishes the position of an income-poor person in Botswana as compared with a similarly income poor person in many other African countries (UNDP Human Resource Development Report 1997). To promote poverty alleviation a two-pronged approach needs to be intensified. Creating productive and sustainable employment opportunities in a rapidly growing economy remains the most effective way to reduce poverty and achieve a more socially just and harmonious society. Second, new government initiative need to be targeting activities that promote poverty alleviation and evaluated not only with respect to their benefit to Botswana, but also with respect to their distributional impact.

The Creation and strategic role of Special Funds is also an important aspect of Botswana's overall development strategy and needs to be noted. Like many other open economies relying on one or two primary exports, Botswana's revenue can be volatile, and tended to grow in a series of discrete steps. Government has tried to minimize such disruptions and to avoid a "boom, and bust" cycle in the government budget by taking a long-term view of revenue trends and attempting to stabilize expenditure around a sustainable growth rate. A number of measures were taken to achieve this and these measures are still useful and instrumental for enhancing sustainable development with less aid dependence.

First, in an effort to anticipate problems and opportunities, three funds were established to provide for stabilization reserves, public debt service, and local development opportunities. These measures were taken after the first year of budgetary independence in 1973 anticipating that having achieved domestic responsibility for spending, it was important to develop vehicles for prudent management. The Domestic Development Fund (DDF) is the key domestic source of funding for development projects. Money intended for capital expenditure together with finance from external funding agencies, is first paid into the Development Fund and then paid out of it to meet approved project expenditures. The Development Fund helps the government to avoid costly delays in project implementation by, for example, allowing donors' funded projects to go ahead on a reimbursement basis. The Revenue Stabilization Fund (RSF) helps to even out fluctuations in revenue trends and accumulates from budget surplus. The Public Debt Service Fund (PDSF) is earmarked for debt servicing and the high level of foreign exchange reserves is a result of a deliberate policy to accumulate as much as possible for unexpected changes regarding the balance of payments.

Second all these special funds (which could be seen as budget surplus funds) including foreign exchange surplus are invested to generate more financial resources. The significant increase in the non-mineral revenue, especially since 1989, is primarily due to investment revenue. Bank of Botswana profits (mainly profits from off-shore investments) are now the second or third largest source of government revenue. Effective economic management was also reflected in progressive adjustments of the exchange rate to encourage other sources of foreign exchange earning. The government explicitly pursued a counter-cyclical policy in the management of foreign exchange reserves and government cash balances, basing year-to-year spending decisions on the intermediate-term forecasts of export earnings and government revenue, and on a realistic view of spending capacity. The other useful device was the creation of bridging finance to enable any donor-funded project to begin should there be delay in donor notification of finance release. This was made possible by money from the Domestic Development Fund (DDF). Seen as a package, these measures enabled Botswana to moderate the inflationary pressure that would have followed massive government spending, and to avoid Dutch disease, fluctuations in revenue trends, incomplete or understaffed projects, and disproportionately large debt servicing obligations. Despite considerable political pressure, the temptation to spend reserves was avoided. However, the underlying concern is that a large share of GDP is really not production but sales of asserts and the country will remain vulnerable so long it remains highly dependent on mineral rent.

Regardless, the decision to adopt the principle of sustainable government budgeting demonstrates effort to anticipate problems and opportunities and proceed to take measures to deal with the situation rather than wait to be "forced" by donors or economic crisis. Thus, it follows that if increasing amounts of mineral revenue (a non-replenishable resource) and aid are used to finance non-investment related recurrent expenditure, the government is seen as pursuing an expenditure pattern that is not viable in the long run. Using this formula, government is expected to monitor budget position carefully and, if conditions warrant, it is expected to further restrict the growth of government expenditures and/or raise the growth of non-mineral revenue. The amount of mineral revenue over and above the required development expenditure is expected to be saved -- leading to accumulation of budget and trade surpluses for investment to generate more financial resources and contingent fund which can be used to minimize the impact of aid reduction. However, it should be noted that this strategy or the approach underlying sustainable budget index -- some times labeled as "super-cautious" -- has been criticized by some people (Auty 1996). They argue that reserving all such revenues for investment is neither necessary to ensure that consumption remains on a sustainable path, nor desirable in the context of structural transformation of the economy that may temporarily increase the need for spending for social purposes. This is a controversial point. But the logic of the reservation principle may be appreciated as a further extension of the risk reservation which is one of the characteristics of economic policy in Botswana. This is crucial for sustainable development without or with reduced aid..0% at its peak tended to squeeze out the shares of other sectors. What needs to be checked is the growth rate of the public sector - a continued reflection of the dominant role of the state in the economy (GoB, Budget Speech 1999).

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