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MARKET INSIGHTS

Botswana Fixed Income and Macroeconomics

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MARKET INSIGHTS: BOTSWANA FIXED INCOME AND MACROECONOMICS

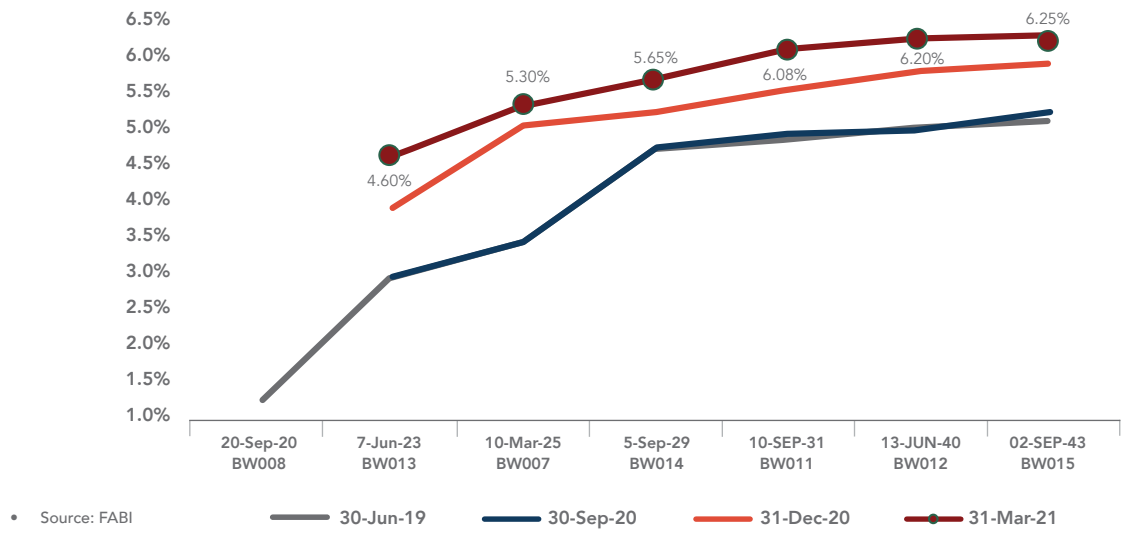
- **Government bonds have continued to come under pressure due to increased supply as the Botswana Government looks for funding for its Economic Recovery and Transformation Plan (ERTP).**
- **We have revised our 2021 growth expectation upwards to 7.2% from 6.3% previously with risks balanced.**
- **We expect inflation to accelerate in the next few months. This will be driven by Transport inflation where we expect further pump price increments as global oil prices continue to rebound on the back of optimism regarding the global economic recovery from the pandemic.**

The first quarter of 2021 continued with unprecedented challenges emanating from the 2020 outbreak of COVID-19. In Botswana, we continue to see the economy reel from the effect and impact of the pandemic. In today's article and insights, we take an in-depth look at how the economy and market performed in the first quarter of 2021.

MARKET REVIEW

The FABI generated a negative quarterly return, with the index declining by 0.3% for the quarter. Government bonds were the main reason for the decline, registering a return of -0.4% for the quarter. Corporate bonds generated positive returns of 0.9% for the quarter. Government bonds have continued to come under pressure due to increased supply as the Botswana Government looks for funding for its Economic Recovery and Transformation Plan (ERTP). Yields rose by at least 30bps across the yield curve with the yield of the BW013 (2-Year), BW007 (4-Year), BW014 (8-Year), BW011 (10-Year), BW012 (19-Year) and BW015 (22-Year) rising by 70bps, 30bps, 45bps, 58bps, 42bps and 39bps respectively.

CHART 1: GOVERNMENT BOND YIELD CURVE CHANGES



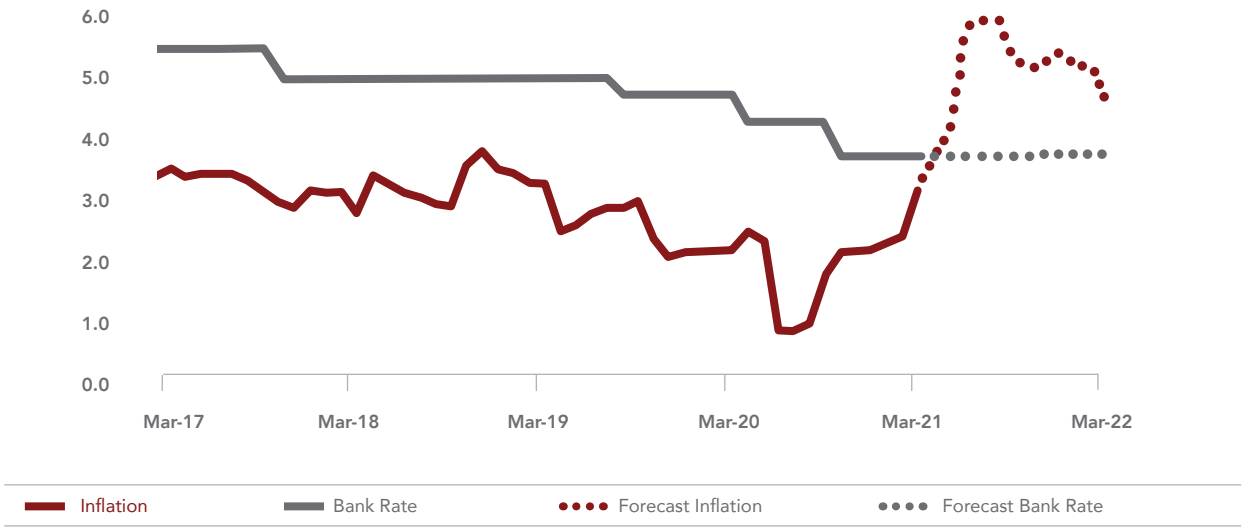
- Source: FABI

There were three auctions held during the quarter where P8.6bn of bonds and T-Bills were offered. There was decent demand with P10.8bn of bids received, however, in a similar manner to Q4 2020's auctions, all auctions were under-allotted with an allotment ratio (allotment divided by securities on offer) of 59.0%. The low allotment was likely due to bids received considered too rich. The key question remains how the Government plans to fund its projected deficits. Even with the possibility of securing bilateral funding, there is an increased likelihood that projects under its ERTP may be delayed.

Inflation breached the lower bound of the Bank of Botswana's (BoB) objective range, ending the quarter at 3.2% in March 2021. The main driver of inflation was Transport inflation which moved out of deflation territory as a result of the ~6.9% (~54t) increase in pump prices effected in March 2021. We expect inflation to accelerate further and briefly touch the 6% upper bound of the BoB's objective range in late Q2 2021/Q3 2021 before decelerating. Our expectation is premised on continued supply-push inflation and base effects arising from the Transport basket.

The main upside risks to our outlook remains higher than expected Food and Transport inflation while the main downside risk remains lacklustre domestic demand.

CHART 2: BOTSWANA CPI (Y/Y %)



- Source: Statistics Botswana, Kgori Capital Analysis

The BoB Monetary Policy Committee (MPC) met once during the quarter on 25 February 2021 and maintained the Bank Rate at 3.75% despite expecting inflation to move closer to the 6% upper bound of its objective range

The MPC views the expected increase in inflation as transitory (due to factors such as increase in VAT, sugar tax and fuel levy) and hence maintained its accommodative position.

A trade surplus of P1.4bn was recorded for the month of January 2021, breaking the trend of monthly trade deficits recorded since February 2020. The main driver of this was the normalisation in diamond trade which registered a surplus of P4.7bn in January 2021. On a Last Twelve Months (LTM) basis, the trade deficit stood at P25.0bn. The main driver of the trade deficit was the reduction in diamond activity brought about by COVID-19 and the restrictions implemented locally and globally to combat its spread which has resulted in diamond trade surplus declining 35.4% y/y to P20.3bn LTM.

Economic growth continued to recover in Q4 2020, registering growth of 3.7% q/q growth from a growth of 24.1% in Q3 2020. Moreover, growth was varied across sectors with noted positive contributions from Wholesale and Retail Trading (+10.6% q/q) and Finance & Business Services (+4.2% q/q). Notable negative contributions were Mining (-6.7% q/q), Water & Electricity (-23.1% q/q) and General Government (-0.3% q/q). On an annual basis, the Botswana economy contracted 7.9% driven by Mining (-26.2% y/y), Wholesale and Retail Trading (-14.8% y/y), Finance & Business Services (-1.2% y/y). The only positive contributors were Agriculture (+2.3% y/y), Water and Electricity (+5.1% y/y) and General Government (+2.8% y/y).

BoB released its 2021 Monetary Policy Statement where it highlighted that in the medium term, it expects below potential local economic performance. This, supported by low and predictable inflation and a continuation of its accommodative monetary policy stance is consistent with inflation being within its 3%-6% objective range. The BoB also assessed the current levels of credit growth to be sustainable. Additionally, the BoB highlighted that it had maintained the downward rate of crawl at 2.87% for the Pula as barring any significant inflationary pressures (in the context of weak economic activity), the BoB believes that the economy could benefit from a measured depreciation in the Pula against trading partners in order to ease real monetary conditions and support domestic industry competitiveness.

January 2021 credit growth decelerated 0.5% to 3.9% y/y from 4.4% y/y in December 2020. The deceleration was driven by falls in both household and business credit growth. Business credit growth fell into negative territory registering a decline of 2.5% to -1.7% y/y. Furthermore, household credit growth decelerated 0.6% to 6.7% y/y.

The Minister of Finance and Economic Development (MFED) presented the 2021 Budget Speech against an unprecedented backdrop of a rapid deterioration in revenues and an equally rapid uptick in necessary expenditure. The Minister highlighted that the 2021/22 budget will be geared towards steering the economy through the uncertainty caused by the COVID-19 pandemic and fast tracking Government initiatives expected to have the biggest impact on the economy. The Minister also highlighted that P14.5bn will be spent under ERTP in the 2021/22 and 2022/23 financial years. The 2021/22 budget is expected to run a deficit of P6.0bn (2.9% of GDP). Weak performance from traditional revenue earners will be countered by increased levies and taxes such as the increase in VAT by 2% to 14.0%. Government will also embark on a cost rationalisation exercise which will see the elimination of some central Government vacancies as well as cuts in subsidies granted to parastatals.

MARKET OUTLOOK

GDP

We have increased our GDP growth estimate for 2021 following the release of better-than-expected Q4 2021 economic data which indicated that the economy contracted 7.9% versus our expectation of an 8.5% contraction.

We have revised our 2021 growth expectation upwards to 7.2% from 6.3% previously with risks balanced. Whilst there have been no hard lockdowns yet in 2021, curfews have been implemented since January 2021 and alcohol sales were banned between January 2021 and February 2021. Current restrictions are less constricting than the lockdowns imposed in 2020 but they will nonetheless constrain business activity in 2021. Forecasts will remain fluid as we get more information on the status of the local and global vaccine rollout as well as the implementation of Government's ERTP.

INTEREST RATES

We expect the BoB to maintain interest rates at current levels in the medium term in order to support economic growth.

INFLATION

We expect inflation to accelerate in the next few months. This will be driven by Transport inflation where we expect further pump price increments as global oil prices continue to rebound on the back of optimism regarding the global economic recovery from the pandemic.

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