Institute for Public Policy Research

14 Nachtigal Street PO Box 6566 Ausspannplatz Windhoek Namibia Tel: +264 61 240514 Fax: +264 61 240516 info@ippr.org.na www.ippr.org.na

# IPPR Economic Outlook, March 2008

## A Rocky Ride Ahead:
## Power Shortages, High Interest Rates and Increased Fuel Costs

***A slowdown in the world's major economies combined with power shortages, record fuel prices, high interest rates and a less favourable inflation outlook will continue to shape the domestic economic environment for the remainder of 2008. The recently tabled budget offers little help as it focuses on correcting past imbalances in expenditure rather than acting as a stimulus for economic growth. However, a pick up in mining production combined with a weaker exchange rate should place the economy on a moderate growth path.***

**What's Inside?**



**International Growth Outlook**

Estimates from the Organisation for Economic Cooperation and Development (OECD) indicate that most major world economies are set to experience a downturn this year, with a combined projected growth rate of 2.3 percent, down from 2.7 percent in 2007 for the OECD group of countries. However, much of the attention will be on the imminent recession in the United States where falling property prices and a financial crisis have created a gloomy picture. Attempts by the Federal Reserve Bank to ease the crisis by lowering short-term interest rates may have limited impact as this has the potential of weakening the currency and thus putting more pressure on both the domestic and global economies. Overall, it is expected that the events in the US will continue to influence the global market.

**South African Economic Outlook**

A recent hike in electricity prices and current high fuel costs should see inflation increasing further, thereby inducing tighter monetary policy resulting in a slowdown in consumer spending and the consequent low economic growth. This view is generally supported by a consensus poll of economists carried out by Reuters (see table 1 below) in February this year where the targeted inflation rate (CPI-X) is expected to remain above the upper-targeted range of 6 percent for the rest of the year before slowing to 5.6 percent in 2009. The poll also show that GDP growth is forecast to slow down to 3.8 percent (marginally lower than the Treasury's forecast of 4.1 percent), down from the actual revised figure of 4.7 percent achieved in 2007. However, an expected repeat of electricity blackouts experienced in January, which led to mine shutdowns, could see growth prospects sliding further due to cuts in productivity levels.

On a positive note, the economy is expected to find support through record-breaking commodity prices (platinum and gold) and an expected depreciation of the rand against the US dollar and other major currencies. Nevertheless, the impact of the latter should be interpreted with caution in view of its impact on imports, oil in particular, which have been the major cause of the high inflationary environment.

**Table 1 Consensus of Independent Economic Forecasts for South Africa 2008-2009**

| | 2008 Q1 (f) | 2008 Q2 (f) | 2008 Q3 (f) | 2008 Q4 (f) | 2008 (f) | 2009 (f) |
|---|---|---|---|---|---|---|
| Real GDP growth | 3.0 percent | 3.4 percent | 3.7 percent | 3.8 percent | 3.8 percent | 4.3 percent |
| Inflation (average CPI-X) | 9.1 percent | 8.3 percent | 7.8 percent | 7.0 percent | 8.1 percent | 5.6 percent |
| Repo rate (year end) | 11.00 percent | 11.00 percent | 10.93 percent | 10.75 percent | 10.77 percent | 9.33 percent |
| Prime interest rate (year end) | 14.50 percent | 14.50 percent | 14.43 percent | 14.25 percent | 14.27 percent | 12.83 percent |
| Exchange rate R/US$ (year end) | 7.58 | 7.66 | 7.66 | 7.73 | 7.71 | 8.06 |

*Notes: (f) Latest consensus forecasts*
*Source: http://www.ber.sun.ac.za/downloads/2008/consensus/reuters/reuters_feb08.asp*

## Growth Outlook for the Namibian Economy

### Agriculture

The drought experienced last year and the subsequent late rains during the current rain season are likely to put a damper on the growth prospects of the grain-producing sub-sector. The floods will place limitations on the number of livestock being marketed in the northern regions, where there has been significant growth in livestock marketing (cattle mainly) in the past few years. On the positive side, a last minute signing of the preliminary Economic Partnership Agreement, thus allowing Namibian products, and beef in particular, to be exported to the European Union (EU) should provide relief to the sector. Help should also be expected from a weaker exchange rate. Overall, low to negative growth should be expected for the year.

**Table 2 Real production and annual growth in agriculture**

| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Commercial (N$m) | 602 | 519 | 489 | 495 | 648 | 589 | 723 | 755 | 681 | 738 | 746 |
| Percent Growth | 16.3 | -13.8 | -5.8 | 1.1 | 31.1 | -9.2 | 22.7 | 4.5 | -9.9 | 8.5 | 1.0 |
| Subsistence (N$m) | 403 | 407 | 420 | 514 | 408 | 310 | 252 | 255 | 338 | 391 | 450 |
| Percent Growth | 13.6 | 1.1 | 3.2 | 22.4 | -20.7 | -24.0 | -18.6 | 0.9 | 32.7 | 15.8 | 9.8 |

*Source: National Accounts 1996-2006, CBS*

### Fishing

The key factors that have blocked the progress of the sector over the past four years have not disappeared completely. However, a weaker Namibia dollar against the US dollar and a rise in fish prices should improve growth prospects for the ailing sector. Unfortunately, these will have to be balanced against very high fuel prices as well as a reduction in total allowable catches in some of the prime species (see table 3 below). Thus, a moderate loss is expected for the sector.

**Table 3 Total Allowable Catches**

| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 |
|---|---|---|---|---|---|---|---|---|
| Pilchard | 25,000 | 10,000 | 0 | 20,000 | 25,000 | 25,000 | 25,000 | 15,000 |
| Hake | 194,000 | 200,000 | 195,000 | 180,000 | 195,000 | 180,000 | 130,000 | 130,000 |
| Horse Mackerel | 410,000 | 410,000 | 350,000 | 350,000 | 350,000 | 350,000 | 360,000 | 230,000 |
| Crab | 2,000 | 2,100 | 2,200 | 2,000 | 2,200 | 2,300 | 2,400 | 2,500 |
| Rock Lobster | 35 | 400 | 400 | 400 | 420 | 420 | 420 | 350 |
| Orange Roughy | 2,400 | 1,875 | 2,400 | 2,650 | 2,600 | 2,050 | 1,100 | 900 |
| Monk | N/A | 13,000 | 12,000 | 12,500 | 12,000 | 11,500 | 9,500 | 9,500 |

*Source: Ministry of Fisheries and Marine Resources and Cabinet Media Briefing (GRN 2007)*

**Table 4 Real production and annual growth in fishing**

| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Fishing (N$m) | 482 | 456 | 567 | 559 | 641 | 631 | 703 | 732 | 666 | 643 | 612 |
| Percent Growth | -1.8 | -3.6 | 21.9 | -1.4 | 14.5 | -1.5 | 11.4 | 4.2 | -9.1 | -3.4 | -4.8 |

*Source: National Accounts 1996-2006, CBS*

### Mining

Increased investment in the uranium sub-sector (owing to an improved demand leading to higher prices) should usher in hope of a much-improved performance from the mining sector in the face of several hostile factors. Key among these is the imminent power crisis, which, coupled with high fuel prices, will result in lower production. In addition, the expected recession in the US is likely to reduce demand for diamonds as the sub-sector tries to improve on last year's poor performance. Consecutive months of decline in zinc and copper prices towards the end of 2007 should also be of concern to the metals sub-sector. The benefit of a relatively weaker exchange rate should be limited, as this also has to be seen in terms of its impact on key import items such as oil and equipment. Overall, growth prospects for the sector remain strong but with a significant downward risk owing to the imminent power shortage.

**Table 5 Real production and annual growth in mining**

| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Diamond Mining (N$m) | 783 | 782 | 793 | 908 | 847 | 803 | 942 | 909 | 1,260 | 1,217 | 1524 |
| Percent Growth | 2.6 | -0.1 | 1.3 | 14.5 | -6.7 | -5.1 | 17.3 | -3.5 | 38.6 | -3.4 | 25.2 |
| Other Mining (N$m) | 317 | 363 | 324 | 303 | 343 | 314 | 355 | 328 | 426 | 448 | 398 |
| Percent Growth | 7.5 | 14.4 | -10.8 | -6.5 | 13.3 | -8.5 | -12.9 | -7.5 | 30.6 | 4.5 | -11.2 |

*Source: National Accounts 1996-2006, CBS*

### Manufacturing

The impending power crisis poses a considerable threat to the sector, as stoppages are expected with a resultant loss of production leading to a loss in earnings across the board. The sector will still have to contend with a declining contribution from the fish and meat-processing sub-sectors, with the former being plagued by lower stocks, as well as high-energy costs. Not much should be expected from the meat-processing sub-sector as the late rains could convince farmers to re-stock and therefore result in reduced processing. Moreover, the situation cannot have been helped by the recent closure of the Ramatex garment factory, which will see further decline in the sector. Altogether, the growth outlook for the sector should be seen in the negative.

**Table 6 Real production and annual growth in manufacturing**

| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Meat Processing (N$m) | 128 | 92 | 99 | 111 | 101 | 107 | 109 | 97 | 88 | 95 | 84 |
| Percent Growth | 3.6 | -28.3 | 8.0 | 12.6 | -9.7 | 6.4 | 2.1 | -11.6 | -8.6 | 7.7 | -11.2 |
| Fish Processing (N$m) | 139 | 262 | 356 | 281 | 241 | 204 | 183 | 277 | 269 | 256 | 159 |
| Percent Growth | -64.4 | 88.8 | 35.7 | -21.1 | -14.2 | -15.3 | -10.1 | 51.1 | -3.0 | -4.7 | -38.0 |
| Other Food (N$m) | 586 | 654 | 725 | 759 | 774 | 808 | 875 | 872 | 885 | 929 | 980 |
| Percent Growth | 8.7 | 11.5 | 10.9 | 4.7 | 1.9 | 4.4 | 8.3 | -0.3 | 1.4 | 5.0 | 5.6 |
| Other (N$m) | 372 | 438 | 394 | 364 | 455 | 538 | 648 | 665 | 726 | 728 | 618 |
| Percent Growth | -9.0 | 17.6 | -10.0 | -7.5 | 24.9 | 18.3 | 20.5 | 2.6 | 9.2 | 0.3 | -15.2 |

*Source: National Accounts 1996-2006, CBS*

### Water and electricity

The late rains experienced in the country as well as reduced imports of electricity due to expected power cuts should see an increase in the local production of electricity from both the coal-powered Van Eck and the hydro-powered Ruacana stations, with a combined capacity of 360 Mega Watts (MW) when fully operational. Demand for electricity will further be boosted by the expansion in the mining sector. However, this positive outlook could potentially be affected by the non-perennial nature of the water flow and price of coal, which makes using Van Eck an expensive exercise. Similarly, the water sub-sector should also see growth with demand coming from the mining sector, combined with the effects of the good rains on dam levels. Overall, higher growth is forecast for the sector.

**Table 7 Real production and annual growth in electricity and water**

| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Electricity and water (N$m) | 238 | 214 | 223 | 268 | 299 | 228 | 230 | 266 | 278 | 315 | 299 |
| Percent Growth | -8.3 | -10.1 | 4.3 | 20.2 | 11.5 | -23.8 | 1.1 | 15.6 | 4.4 | 12.9 | -4.9 |

*Source: National Accounts 1996-2006, CBS*

### Construction

Current steel shortages and high interest rates mean the construction sector will remain under pressure during the year. Much of this should come through a decline in demand for residential property development as individuals shy away from costly mortgages. Nevertheless, an expected increase in mining activity, in the uranium sub-sector in particular, and the anticipated construction of a desalination plant in the Erongo region, as well as some reconstruction and rehabilitation of roads and buildings in flood-affected regions, should see the sector remain in positive territory with medium growth foreseen.

**Table 8 Real production and annual growth in construction**

| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Construction (N$m) | 416 | 367 | 423 | 364 | 344 | 527 | 459 | 564 | 570 | 586 | 777 |
| Percent Growth | 15.4 | -11.8 | 15.3 | -43.9 | -5.4 | 53.1 | -13.1 | 22.9 | 1.2 | 4.4 | 32.5 |

*Source: National Accounts 1996-2006, CBS*

### Wholesale and retail trade

A combination of high fuel costs, inflation and interest rates means the sector's traditional resilience will be heavily tested during the year. However, the expected poor harvest in the northern regions, due to floods, could potentially push up demand for food items. Unfortunately, the same cannot be said about durable and semi-durable items (vehicle sales as well as furniture), where interest rates could negatively influence consumers. Altogether, this points to rather moderate growth prospects for the sector.

**Table 9 Real production and annual growth in wholesale and retail trade**

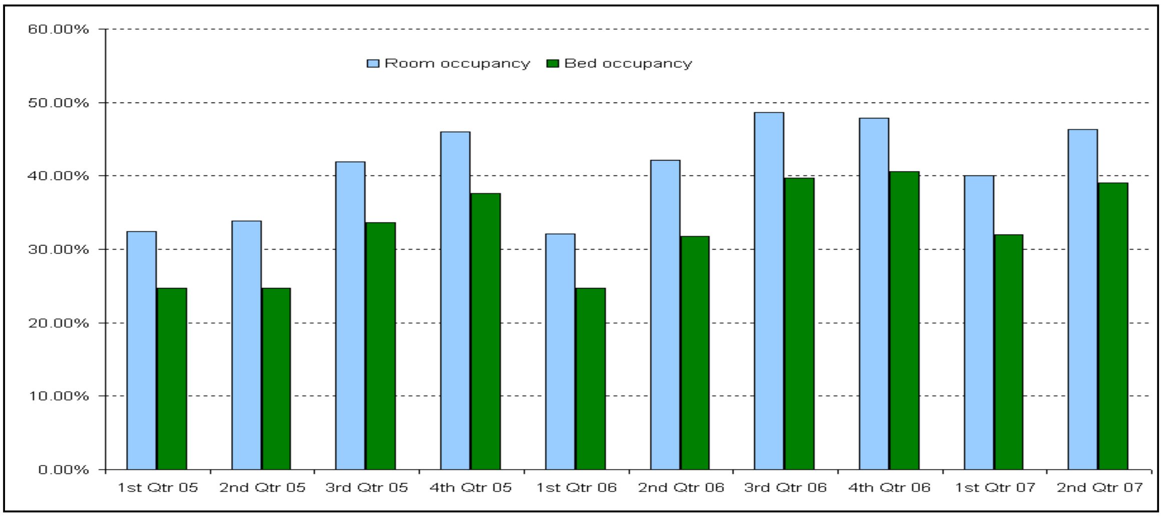
| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Retail and Trade (N$m) | 1,179 | 1,248 | 1,336 | 1,380 | 1,455 | 1,496 | 1,607 | 1,674 | 1,801 | 1,915 | 2,117 |
| Percent Growth | 9.5 | 5.9 | 7.1 | 3.3 | 5.4 | 2.8 | 7.4 | 4.1 | 7.6 | 6.4 | 10.5 |

*Source: National Accounts 1996-2006, CBS*

### Hotels and restaurants

As *Figure 1* below shows, the past few years have seen a steady growth in room and bed occupancy among Hospitality Association of Namibia members throughout the country. However, a possible slowdown in the local and global market poses a threat to the hotel and restaurant sector in the current year. Similarly, the current high fuel prices mean tourists will have to contend with relatively higher air ticket prices. Nevertheless, the favourable exchange rate and the constant search for new markets through marketing campaigns by the Namibia Tourism Board should result in moderate growth for the sector.

**Figure 1 Quarterly average room and bed occupancy at HAN members (2005 - 2nd quarter of 2007)**




*Source: Hospitality Association of Namibia*

### Transport and communication

The recent announcement that the Mobile Telecommunications Company (MTC) has reached 800,000 subscribers (about 40 percent of the country's population) demonstrates the unparalleled growth prospects for the telecommunications sub-sector. The onset of competition through the launch of a second mobile telecommunication company (CellOne) as well as a new satellite television network (GTV) should see the sub-sector growing further in the year as consumers will not only be exposed to diverse but also competitively-priced products. However, the Ministry Finance's decision to do away with VAT exemption on prepaid services could prove costly, as the majority of subscribers are likely to be found into this category. Recent research (Stork, 2008) has since pointed out that the move is likely to place Namibia among the countries with the costliest telecommunication services in Africa.
The transportation sub-sector will continue to be under pressure from high fuel costs, though some relief could come from the expansion in the mining sector and therefore moderate growth is expected.

**Table 10 Real production and annual growth in transport and storage and post and telecommunications**

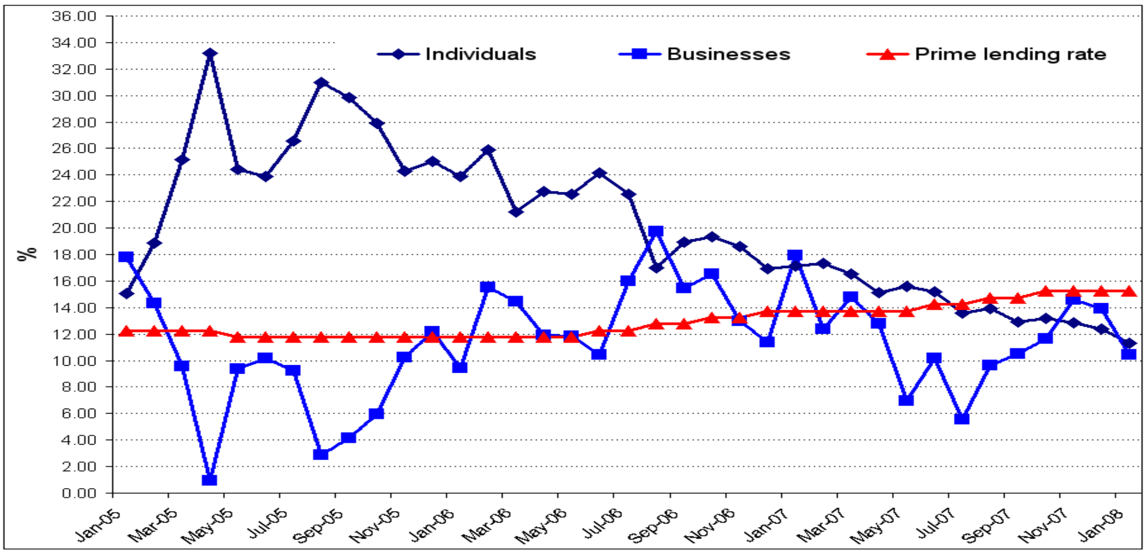
| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 03 | 04 | 05 | 06 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Transport and Storage (N$m) | 655 | 673 | 533 | 631 | 671 | 725 | 837 | 753 | 816 | 863 | 964 |
| Percent Growth | 3.1 | 2.8 | -20.8 | 18.4 | 6.3 | 8.1 | 15.5 | -10.0 | 8.4 | 5.7 | 11.7 |
| Post and Telecommunications | 239 | 289 | 329 | 337 | 379 | 471 | 494 | 619 | 741 | 852 | 1050 |
| Percent Growth | 10.7 | 20.8 | 14.0 | 2.3 | 12.4 | 24.3 | 5.0 | 25.2 | 19.7 | 28.4 | 10.3 |

*Source: National Accounts 1996-2006, CBS*

## Financial intermediation

*Figure 2* below shows that growth in total credit extension remained fairly robust during the preceding year, averaging13 percent, despite high interest rates. However, it can also be observed that the growth rate shows a declining trend, particularly in the individual category. Expected decline in disposable income due to higher inflation and high interest rates should see this trend continue through the year as borrowers struggle to keep up with the servicing of already existing debts. Similarly, the expected slowdown in economic activity could potentially lead to businesses shying away from debt and thus adding pressure on the sector. The same should also apply to the equity markets where stock prices are expected to fall initially, with a late pick up expected towards year-end as investors could be enticed by relatively cheaper shares. The insurance industry is also expected to come under pressure as they attempt to comply with Regulation 28 of the Pension Funds Act of 1956, which is expected to come into force this year. In addition, the insurance industry will face increased claims due to flooding in the northern regions. Overall, moderate growth is expected for the sector 2008.

**Figure 2 Year-on-year growth rates in credit extension of Namibian commercial banks versus the prime-lending rate for the period Feb 2005 – Jan 2008.**




*Source: Bank of Namibia (2007)*

**Table 11 Real production and annual growth in financial intermediation**

| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Intermediation (N$m) | 380 | 423 | 450 | 461 | 489 | 498 | 514 | 564 | 646 | 768 | 788 |
| Percent Growth | 16.9 | 11.4 | 6.5 | 2.4 | 6.2 | 1.7 | 3.3 | 9.6 | 14.6 | 18.9 | 2.6 |

*Source: National Accounts 1996-2006, CBS*

## Producers of government services

The recently presented government budget for the 2008/09 financial year shows that expenditure will rise from N$17.8 billion to N$22.5 billion, representing a 26 percent increase. The major shift has been made through yet another windfall from the Southern African Customs Union (SACU) revenue pool, an expected increase in individual and company tax collections, as well as VAT returns. Expenditure items indicate that the major beneficiaries of the budget will be the Police, Defence, Education and Health sectors, all of which can hardly be classified as productive sectors, although education could qualify in the long term. An increase in social pensions, new grants for war veterans, possible salary adjustments, and an increase in contingency funds due to the floods in the populous northern regions were some of the other main features. While an increase in

SACU receipts is expected, it remains to be seen whether government will collect the anticipated local tax revenue given the expected slowdown in the domestic economy.

**Table 12 Real production and annual growth in government services**

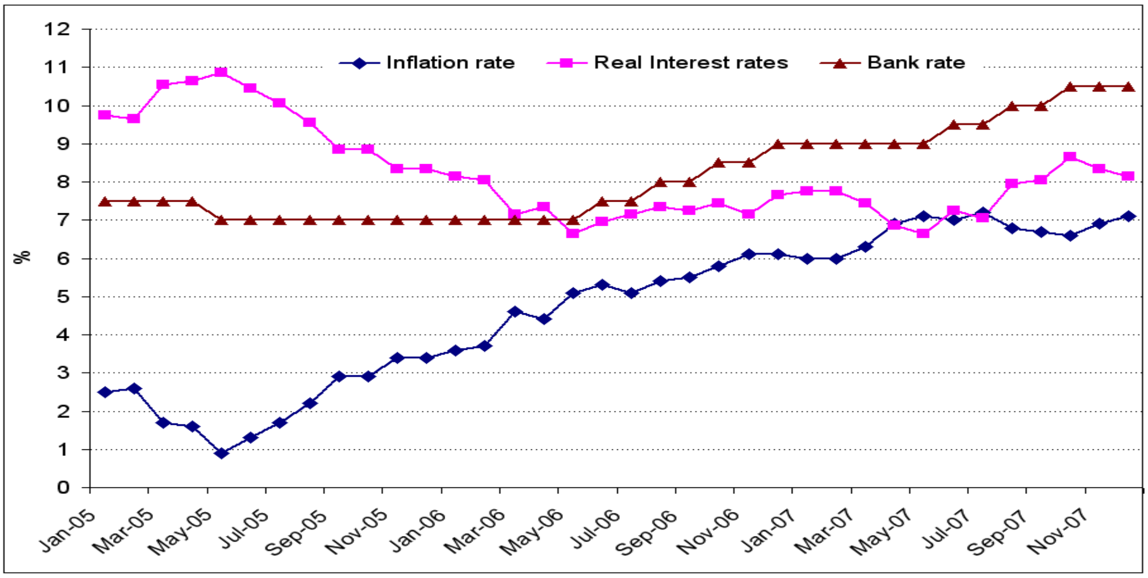
| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Government (N$m) | 2,876 | 2,980 | 3,060 | 3,162 | 3,236 | 3,281 | 3,408 | 3,475 | 3,650 | 3,811 | 3,769 |
| Percent Growth | 3.5 | 3.6 | 2.7 | 3.4 | 2.3 | 1.4 | 3.9 | 2.0 | 5.0 | 4.4 | -1.1 |

*Source: National Accounts 1996-2006, CBS*

**Price developments**

The dramatic peak in international Brent crude oil prices in the last quarter of 2007 points to an upward risk for the inflation outlook. This, in turn, means the tight monetary stance could linger for much longer with real interest rates (the nominal lending rate minus the inflation rate) coming under pressure. This will be necessitated by the fact that monetary authorities will be mindful of the slowing domestic economy and thus may be less inclined towards raising rates.

**Figure 3: Developments in inflation and interest rates (Jan 2005 to Dec 2007)**




*Source: Bank of Namibia (2007)*

**Overall GDP growth**

The power crisis, high interest rates, high-energy costs and flooding in the northern regions will set the scene for the local economy. The expected slowdown in the major economies should also limit the growth of the export sector. Unfortunately, the expansionary fiscal policy stance in the recently tabled budget for 2008/09, though welcomed, will not be sufficient to provide impetus to the domestic economy. This is partly because of the sluggish nature of fiscal policy, which unlike monetary policy, takes a long time to be fully implemented. Also, a glance at the main expenditure items shows that the budget is focused on correcting past imbalances in expenditure rather than focusing on productive sectors and stimulating aggregate consumption in light of the tight monetary policy. Altogether, the IPPR expects a moderate growth rate of 3.5 percent for the domestic economy in 2008.

**Note on methodology:**
At the beginning of each year, the Institute for Public Policy Research (IPPR) produces an economic outlook for Namibia. The title 'economic outlook' has been chosen in preference over anything more "scientific" such as 'forecast' since the idea is to survey the economic landscape in a general way rather than come up with detailed estimates of economic variables that later prove wide of the mark. Making forecasts with any precision is a difficult task, especially in small open economies like Namibia. The IPPR Economic Outlook includes an estimate of Gross Domestic Product (GDP) growth based on an assessment of the likely performance of the sectors of the economy. For the latest edition, a mini-survey was carried out seeking the views of industry leaders regarding the local economy. The power crisis, fuel costs and high interest rates were singled out by most respondents as the major threats to the local economy.

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