THE ECONOMIC DEVELOPMENT OF BOTSWANA SINCE 1980 WITH SPECIAL REFERENCE TO THE ROLE OF FOREIGN AID

by

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DECLARATION

I, TAKALANI ARCHIBALD MARAGA declare that:

THE ECONOMIC DEVELOPMENT OF BOTSWANA SINCE 1980 WITH SPECIAL REFERENCE TO THE ROLE OF FOREIGN AID, is my own work, that all the sources used or quoted have been indicated and acknowledged by means of complete references, and that this dissertation has not previously been submitted by me for a degree at another university.

T.A. MARAGA

DATE: 1993/06/30

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AIM OF THE STUDY AND METHOD OF RESEARCH

A. AIM OF THE STUDY

1. SUBJECT

The subject of the field of research is the role and effect of foreign aid in the form of grants, loans and direct investment in the economies of third world countries.

2. TITLE OF RESEARCH

THE ECONOMIC DEVELOPMENT OF BOTSWANA SINCE 1980 WITH SPECIAL REFERENCE TO THE ROLE OF FOREIGN AID

3. REASONS FOR THE RESEARCH

The purpose or reason for this research is to determine the effect foreign aid in the form of grants, loans and direct investment has had on the economy of Botswana since 1980, and also identify specific sectors within the economy that received foreign aid in the form of grants, loans, direct investments and how they compare with those sectors which did not receive the same. On the whole the research will endeavour to determine which of foreign aid: grants, loans or direct investment is most suitable with maximum benefit for the economic development of third world countries.

4. SCOPE OF RESEARCH

It is envisaged that the dissertation/research will be spread over five chapters.

CHAPTER ONE - INTRODUCTION

This chapter will introduce the field of research by introducing the concept of foreign aid in the form of grants, loans and direct investment in a great level of depth. It will also provide for the methodology to be used in the ensuing chapters and also examine arguments for and against foreign aid in the form of grants, loans and direct investment in the economies of third world countries.

CHAPTER TWO - STATE OF THE ECONOMY

This chapter will examine the economic backdrop of Botswana since 1980. It will examine basic indicators such as GNP, GDP, level of industrialisation etc., since 1980.

CHAPTER THREE - FOREIGN LOANS AND GRANTS

This chapter will determine who (countries, banks, agencies) provided the foreign loans and grants, when, for what purpose it was required, to which sector of the economy it was to be utilised, repayment terms and problems encountered in the repayment of the loans (if any). It will conclude with an evaluation of what foreign aid in the form of grants and loans has had on those sectors of the economy where it was provided and also its contribution to the economy in general.

CHAPTER FOUR - DIRECT INVESTMENT

This chapter will determine where the direct investment came from (countries or multinationals), when, for how long (i.e. determine whether it was continuous or just one-off direct investment) and which sector benefited from the direct investment. It will conclude with an evaluation of what impact (both negative and positive) direct investment has had on the economy of Botswana since 1980.

CHAPTER FIVE - CONCLUSION

This chapter will determine and evaluate the effect foreign aid in the form of grants, loans and direct investment has had cumulatively on the economy of Botswana since 1980 and which of the three had a greater impact on the economy of Botswana as a whole.

B. METHOD OF RESEARCH

The following methodology will be used in the ensuing chapters.

1. DESK RESEARCH

This will be from the following sources:

- Books on Aid, with particular reference to books on Aid in Africa.

- Periodicals and journals of the following organisations:
  * IMF
  * United Nations
  * Bank of Botswana
  * Barclays Bank of Botswana
  * Botswana National Development Corporation
  * The Economist Intelligence Unit
  * World Bank
  * Interdevelopment Bank of America
  * Financial Mail
  * The Times, and also newspapers such as the Business section of the Star.

2. IN-COUNTRY RESEARCH

This will be done in Botswana through interviews with representatives of the various bodies involved in Commerce. These bodies will comprise of the following:

- Bank of Botswana
- Botswana National Development Corporation
- Department of Trade & Industry (Botswana)
- Standard Chartered Bank of Botswana
- Various Multinational Corporations operating in Botswana.

CHAPTER ONE

GENERAL ORIENTATION

1.1 INTRODUCTION

In this chapter we are going to look first at the definition of foreign aid, the different components comprising the concept of foreign aid, as well as how foreign aid has been applied. This chapter will also endeavour to show why donors are willing to give foreign aid and also why the less developed countries accept foreign aid.

The chapter will proceed with a discussion of what foreign aid is meant to do or achieve, as well as addressing the question of how much foreign aid are donor countries prepared to give as well as how much foreign aid the less developed countries expect.

This chapter will also give an indication on the forms which foreign aid can take, the sources of foreign aid, as well as the principle forms of foreign aid. These being grants, loans and foreign direct investment.

This chapter will also introduce arguments in support of and against private foreign investment and will end up with a discussion on the meaning of development as well as a discussion on the objectives of development.

1.2 TOWARDS A DEFINITION OF FOREIGN AID

Aid is an ambiguous word and there is no common agreement on its definition and hence its measurement.[1]

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1 HEALEY, J.M, THE ECONOMICS OF AID, ROUTLEDGE & KEAGAN PAUL LTD, LONDON, 1971, P1

Different organisations and different countries include or exclude a variety of items. The Development Assistance Committee of the Organisation for Economic Cooperation and Development defines aid as consisting of grants, loans of whatever terms or duration, contributions in kind, reparations payments, and consolidation credits.[2] Under the more inclusive heading of "flow of financial resources", it includes private direct investment, purchase of World Bank bonds, and government guaranteed private export credits. On the other hand, it excludes trade under preferential arrangements; tariff rebates under preferential systems; and payment of prices above market levels for imports.

This definition of aid does not make much sense because it lumps together incommensurate transactions. Normally, we would think of aid as a transaction that would be entered into if only the direct economic rewards were considered. One suggestion for reducing these heterogeneous categories to a common measure is to define aid as the real cost or sacrifice to the countries providing the nominal flows of resources.[3] This would then give aid an economic meaning. The real cost or "grant element" in a loan would be measured by the difference between its nominal value and the future interest payments and amortization discounted at a rate which reflects the return on the funds alternatively open to the country supplying them. In the case of a grant the cost would obviously be identical with its nominal value.[4]

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2 PINCUS, J, <u>TRADE, AID AND DEVELOPMENT: THE RICH AND THE POOR NATIONS,</u> MCGRAW-HILL BOOK COMPANY, NEW YORK, 1967, P308

3 HEALEY, J.M, <u>OP CIT</u>, P1

4 IBID, P2

Thus, a grant would usually be considered as aid, the exception would be if it were really a disguised transaction, such as a form of air base rental.[5] From the donor's point of view, a foreign loan is not regarded as aid if its terms and conditions approximate those of the domestic capital market, although the recipient may still look on it as aid because his alternative borrowing rates are higher. The aid element in a loan can therefore be computed for donors, as the difference between the face value of the loan, and the present value of future interest and amortization discounted at the lender's alternative lending rate.[6] From the above, it is obvious that the lower the interest rate and the longer the term of the loan, the greater the aid element for the donor. If the loan is made under stiffer conditions or terms than those that prevail in the domestic market, then its aid value is negative from the viewpoint of the donor's cost.

For the aid recipient, this definition is changed in three respects. First, the appropriate discount rate to use is that prevailing in the country receiving the aid. Second, to the extent that foreign exchange is at a premium in the receiving country, the value of aid is higher than it would be if payments were in equilibrium. Third, financial aid tied to procurement in the donor country is worth less to the recipient than it would be if the funds could be used for procurement worldwide.[7] The value of aid to the recipient in this form should be discounted by an amount equal to the differences between prices paid for the goods and services and their world prices.

5 PINCUS, J, <u>OP CIT</u>, PP308-309

6 IBID, P309

7 IBID, P309

The above definitions concentrate on the real cost of aid to the donor and the real benefit to the recipient. They are an attempt to express formally and to quantify some obvious points about real levels of aid.

In principle, all real resources transfers from one country to another (mostly from developed to less developed nations but increasingly from OPEC to other Third World Countries) should be included in the definition of foreign aid. However, even this simple definition raises a number of problems.

Firstly, many resources can take disguised forms such as the granting of preferential tariffs by developed countries to Third World exports of manufactured goods. This permits LDC's to sell their industrial products in developed-country markets at higher prices than without such tariff reductions. There is consequently a net gain for LDC's and a net loss for developed countries which amount to a real resource transfer to LDC's. Such implicit capital transfers of "disguised flows" should be counted in quantifying foreign aid flows. Normally, however, they are not.[8]

On the other hand, we should not include all transfers of capital to LDC's, particularly the capital flows of private foreign investors.[9] For a number of years aid was calculated as the sum of official and private capital flows, although now these items are listed separately i.e. official capital flows are not distinguished from private capital flows. Private flows represent normal commercial transaction, are

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8 TODARO, M.P, <u>ECONOMIC DEVELOPMENT IN THE THIRD WORLD,</u> LONGMAN, NEW YORK, 1977, P332

9 IBID, P332

prompted by commercial considerations of profits and rates of return and, therefore, should not be viewed as aid any more than LDC exports to developed countries should be viewed as aid to the LDC's. Commercial flows of private capital are not a form of foreign assistance, even though they may benefit the developing country in which they take place.[10]

Economists have defined foreign aid, therefore, as any flow of capital to LDC's which meets two criteria: Firstly, its objective should be non-commercial from the point of view of the donor; and secondly, it should be characterised by "concessional" terms i.e. the interest rate and repayment period for borrowed capital should be "softer" than commercial terms. However, even this definition can sometimes be inappropriate since it could include military aid which is both non-commercial and concessional. Normally, however, military aid is excluded from international measurements of foreign aid and flows.

The concept of foreign aid, therefore, which is now widely used and accepted is one which encompasses all official grants and concessional loans, in currency or in kind, which are broadly aimed at transferring resources from developed to less developed nations (and, more recently, from the OPEC to other Third World Countries) on developmental and/or income distributional grounds.[11] Unfortunately, there is often a thin line separating purely "developmental" grants and loans from those ultimately motivated by security and/or commercial interests.

However, from the point of view of the recipient country, foreign economic aid occurs when:

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10 IBID, P333

11 IBID, P333

a) The country receives additional resources in foreign currency, or its equivalent in goods, over the capacity to import generated exports or financed from accumulated reserves, without the need of immediate repayment and at a cost lower than the prevailing rates of commercial loans.

b) These additional resources are used in order to improve the recipient country's economic performance above the level otherwise attainable, that is either the country achieves a higher rate of growth without reducing the anticipated consumption of working people or it implements the anticipated rate of growth, managing to increase the volume of popular consumption over the anticipated level.[12]

A combination of the two situations described above is, of course, possible.

We assume that this higher rate of growth implies changes in the structure of the economy although in the short run structural rigidities or imbalances which give rise to scarcities in supplies of determined commodities and services can only be relieved by additional imports.

The country's economic performance is not improved however, when additional resources are used to increase the consumption of "luxuries", i.e. to permit the implementation of the anticipated rate of growth with an unchanged level of popular consumption and a lower volume of internal savings. Hence we cannot equate all the inflows of foreign capital with foreign aid.

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12 KALECKI, M, ESSAYS ON DEVELOPING ECONOMIES, THE HARVESTER PRESS LIMITED, ENGLAND, 1976, P65

Whether it should be considered as "aid" or not depends on the one hand, on the comparative cost of such capital and, on the other, on the use made of it by the recipient country, which may not always have a free hand to act without taking into consideration the suggestions of the donor.[13] Thus a certain measure of arbitrariness cannot be entirely dissociated from evaluations of foreign aid received.

Turning now to the definition of aid from the point of view of the donor country, a clear distinction must be made between two positions.

a) The donor country has no free productive capacity. This usually happens in socialist countries.

b) The donor country does not fully use its productive capacity because of lack of effective demand, a situation frequent in developed capitalist countries.

In the former case, giving foreign aid, embodied in an export surplus, means a sacrifice because the aggregate internal expenditure will be less than the income generated, which cannot be stepped up above the maximum level warranted by the productive capacity.[14] Were there no export surplus, the aggregate internal expenditure would be equal to the income generated at the maximum level.

In the latter case, the picture changes entirely. The export surplus, similar to investment, has a "multiplier" effect so that the aggregate domestic expenditure after deduction of the export surplus from the income thus generated is higher than the income which would be generated without the export surplus. From the above it can be said therefore that, by giving

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13 IBID, P65

14 IBID, P66

economic aid to other countries, a developed country with free productive capacity assists its own economy in obtaining a higher level of economic activity. Foreign aid, far from being a burden on it, can perform a very useful role in achieving full employment while it serves a better purpose than encouraging the armaments race provided it does not compete with public expenditures, other than armaments, which are of considerable importance for the country in question.[15]

The value of "official development assistance" which includes bilateral grants, loans and technical assistance as well as multilateral flows has grown from about an annual rate of $6 billion in 1962 to approximately $10.5 billion in the mid 1970's. However, in terms of the percentage of developed country GNP's allocated to official development assistance, there has been a steady decline from 0.52 per cent in the early 1960's to slightly less than 0.30 per cent in the mid 1970's.[16] The United States is still the major supplier of public aid to Third World nations, but its proportion of total development assistance has declined from 59 per cent in 1960 to approximately 35 per cent in the mid 1970's.

However, just as there are conceptual problems associated with the definition of foreign aid, so too there are measurement and conceptual problems in the calculation of actual development assistance flows. In particular, three major problems arise in measuring aid:-

First, one cannot simply add together the dollar values of grants and loans since each has a different

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15 IBID, P66

16 TODARO, M.P, OP CIT, PP333-334

significance to both aid-giving and aid-receiving countries. Loans must be repaid and therefore "cost" the donor and "benefit" the recipients less than the "nominal" value of the loan itself. Conceptually, therefore, one should deflate or discount the dollar value of interest-bearing loans before adding them to the value of outright grants.[17]

Secondly, aid can be "tied" either by source or by project. When loans or grants are "tied" by source, the loans or grants have to be spent on the purchase of donor country goods and services. When loans and/or grants are "tied" by project, the funds cannot be spent on raw materials and intermediate products. In either case, the "real value" of the aid is reduced because the specified "source" is likely to be an expensive supplier, otherwise there would be no need to "tie" the aid, or the project itself may require purchase of new machinery and equipment from monopolistic suppliers while existing productive equipment in the same industry is being operated at very low levels of capacity.

Finally, we need to distinguish between the "nominal" and "real" value of foreign assistance, especially during periods of rapid inflation. Aid flows are usually calculated at nominal levels and tend to show a steady rise over time. However, when deflated for rising prices, the actual volume of aid from most donor countries, especially the United States, has declined substantially during the last decade.[18]

Quoting statistics on the volume, direction and trends in the development assistance however, is of little

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17 IBID, P335

18 IBID, P336

relevance without an understanding of the ultimate objectives of foreign aid and its role and/or limitations in promoting economic and social development. However, this presents difficulties for the actual definition of aid and the meaning and motives attached to it may vary from donor country to donor country and from one multilateral development assistance agency to another. Moreover, there are likely to be fundamental differences in attitudes and motivations between donor and recipient countries. Aid is thus a complex and confusing term, especially when it is used to cover a variety of resource transfers from one country to another. Many of these may be military and/or political in nature and have nothing to do with assisting economic development. This is especially true if we look at Communist aid to Third World Countries. The case of Cuban aid to Angola represents a very good example.

Because foreign aid is seen differently by donor and recipient countries, we have to analyse the giving and receiving process from these two often contradictory viewpoints. One of the major criticisms of the literature of foreign aid is that it has concentrated almost exclusively on the motives and objectives of donor countries while devoting little attention to why LDC's accept aid and what they perceive it will accomplish.[19]

2. FOREIGN AID: WHY DONORS GIVE AID

Official net flows of financial resources have been transferred from rich to poor countries on a large and growing scale in the last fifteen years. This is very

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19 IBID, P336

much a post-war phenomenon and it raises the question of why it has occurred.[20] Governments usually state that they provide assistance to other countries to assist their economic development. An interest in development per se, of course, implies a purely humanitarian motive but governments are also motivated by national self interest.

Donor countries give aid primarily because it is in their political, strategic and/or economic self-interest to do so. While some development assistance may be motivated by moral and humanitarian reasons to assist the less fortunate, for example, emergency relief programmes, there is no historical evidence to suggest that over longer periods of time donor countries assist others without expecting some corresponding benefits (political, economic, military etc.) in return.[21] Therefore we can characterize the foreign aid motivations of donor countries into two broad, but often inter-related categories: political and economic.

2.1 POLITICAL MOTIVATIONS

The offer of finance to "keep friends and influence people" is a long-standing international practise and the desire to preserve friendly links and historical ties by offers of assistance partly accounts for the concentration of U.K. assistance on Commonwealth countries.[22] Aid becomes merely an instrument of foreign policy when its intent is to buy support for the policies of the assisting country in the U.N. and other international forums. Aid which is used to "buy

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20 HEALEY, J.M, OP CIT, P2

21 TODARO, M.P, OP CIT, P337

22 HEALEY, J.M, OP CIT, P4

a base" for the air or naval operations of the aiding country is basically a payment for a service.

This has been by far the primary motivation of aid-granting nations, especially by the major donor country, the United States. Foreign aid has been viewed from its very beginnings in the late 1940's under the Marshall Plan, when the United States set out to reconstruct the war-torn economies of Western Europe as a means of containing the international spread of Communism. When the balance of "cold war" interests shifted from Europe to the Third World in the mid 1950's, the policy of containment embodied in the U.S. aid programme dictated a shift in emphasis towards political, economic and military support for "friendly" less developed nations, especially those considered geographically strategic.[23] Most aid programs to developing countries were, therefore, orientated more towards purchasing their security and propping up their sometimes shaky regimes than promoting long-term social and economic development. The successive shifts in emphasis from South Asia, to South East Asia, to Latin America, the Middle East and back to South East Asia during the 1950's and 1960's reflects the changes in U.S. strategic and political interests more than changing evaluations of economic need.[24] The relative neglect of Africa throughout the period supports the validity of this proposition.

Even the Alliance for Progress, which was inaugurated in the early 1960's with such fanfare and noble rhetoric about promoting Latin American economic development, was in reality formulated primarily as a direct response to the rise of Fidel Castro in Cuba and

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23 TODARO, M.P, <u>OP CIT</u>, P337

24 IBID, P337

the perceived threat of Communist takeovers in other Latin American countries. As soon as the security issue lost its urgency, however, and other more pressing problems came to the fore, such as the war in Vietnam, the growing dollar crisis, the rise in U.S. domestic violence etc., the Alliance for Progress stagnated and began to fizzle out. The point illustrated above is that where aid is seen primarily as furthering donor-country interests, the flow of funds tends to vary in accordance with the donor's political assessment of changing international situations and not the relative need of different political recipients.

The experience of other major donor countries like Great Britain and France has been similar to that of the United States. Although obvious exceptions such as Sweden and Norway can be cited, it remains widely agreed that donor countries have utilised foreign aid largely as a political weapon or lever to prop-up or underpin "friendly" political regimes in Third World Countries; Regimes whose continued existence was perceived to be in the "national security" interests of Western nations. Most "Socialist Aid", especially that of the Soviet Union, grew out of essentially the same political and strategic motivations, although the form and content of that aid may have been different.

2.2 ECONOMIC OR COMMERCIAL MOTIVATIONS

Within the broad context of political and strategic priorities, foreign aid programmes of the developed nations have had a strong economic rationale. In fact, while political motivation may have been of paramount importance, the economic rationale was at least given greater lip-service as the overriding motivation for assistance.

The principle economic arguments which have been advanced in support of foreign aid are as follows:-

2.2.1 FOREIGN EXCHANGE CONSTRAINTS

External finance from both loans and grants can play a critical role in supplementing domestic resources in order to relieve savings or more important foreign exchange bottlenecks. This is the familiar "two-gap" analysis of foreign assistance. The basic argument of the model or the two-gap model is that most developing countries are faced either with a shortage of domestic savings to match investment opportunities or a shortage of foreign exchange to finance needed imports of capital and intermediate goods. Most two-gap models assume that the savings and foreign exchange gaps are unequal in magnitude and that they are mutually independent; that is, there is no substitutability between savings and foreign exchange. This assumption is obviously unreal but it greatly facilitates the mathematical analysis.

These assumptions imply that one of the two gaps will be "binding" or dominant for any LDC at a given point in time. For example, if the savings gap is dominant this would imply that the country is operating at full employment and is not using all of its foreign exchange earnings. It may have enough foreign exchange to purchase additional capital goods from abroad but there is not enough excess domestic labour or other productive resources to carry out additional investment projects. The importation of such capital goods would only direct domestic resources from other activities and probably lead to inflation. As a result, "excess" foreign exchange, including foreign aid, might be spent on the importation of luxury consumption goods.[25] Such a country is said to have a shortage of

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25 IBID, P338

"productive resources" which, from a different perspective, can be regarded as a shortage in savings. An outstanding example of "savings gap" nations would be the Arab oil states.

Most developing countries, however, are assumed to fall, into the second category where the foreign exchange gap is binding. These countries have excess productive resources, mostly labour, and all the available foreign exchange is being used for imports. The existence of complementary domestic resources would permit them to undertake new investment projects if they had the external finance to import new capital goods and associated technical assistance. Foreign aid, therefore, can play a critical role in overcoming the foreign exchange constraint and raising the real rate of economic growth.

2.2.2 GROWTH AND SAVINGS

External assistance is also assumed to facilitate and accelerate the process of development by generating additional domestic savings as a result of the higher growth rates which it is presumed to induce. Eventually it is hoped that the need for concessional aid will disappear as local resources become sufficient to give the development process a self-sustaining character.

2.2.3 TECHNICAL ASSISTANCE

Financial assistance needs to be supplemented by "technical assistance" in the form of high level manpower transfers to assure that aid funds are most efficiently utilised to generate economic growth. The manpower gap filling is thus analogous to the financial gap filling process.

2.2.4 ABSORPTIVE CAPACITY

Finally, the amount of aid should be determined by the recipient country's "absorptive capacity"; a euphemism for its ability to use aid funds wisely and productively. Very often it is the way donors want them to be used. Typically it is the donor countries which decide which LDC's are to receive aid, how much, in what form (i.e. loans or grants, financial and/or technical assistance) for what purposes and under what conditions on the basis of their assessment of LDC absorptive capacities. But the total amount of aid rarely has anything to do with Third World absorptive capacities; typically it is a residual and low priority element in donor country expenditure. In most instances the recipient countries often have had little say in the matter.

2.3 ECONOMIC MOTIVATIONS AND SELF-INTEREST

The above arguments on behalf of foreign aid as a crucial ingredient for the LDC development should not mask the fact that even at the strictly economic level, definite benefits accrue to donor countries as a result of the aid programmes. The increasing tendency towards providing loans instead of outright grants and towards "tying" aid to exports of donor countries has saddled many LDC's with substantial debt repayment burdens.[26] It has also increased their import costs often by as much as 20 to 40 percent. These extra import costs arise because aid which is tied to donor country exports limits the receiving nation's freedom to shop around for low cost and suitable capital and intermediate goods. Tied aid in this sense is a second best option to untied aid even though it may still be

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26 IBID, P340

desirable from a LDC's economic point of view. In fact, one former U.S. aid official candidly put it as follows: "The biggest single misconception about the foreign aid programme is that we send money abroad. We don't. Foreign aid consists of American equipment, raw materials, expert services and food - all provided for specific development projects which we ourselves review and approve .... Ninety-three percent of Aid funds are spent directly in the United States to pay for these things. Just last year some 4,000 American firms in 50 states received $1,3 billion in Aid funds for products supplied as part of the foreign aid programme".[27]

Similarly, a former British Minister of Overseas Development, Mr Earl Grinstead, once noted that "About two-thirds of our aid is spent on goods and services from Britain .... trade follows aid. We equip a factory overseas and later on we get orders for spare parts and replacements .... aid is in our long-term interest".[28]

3. FOREIGN AID: WHY LDC RECIPIENTS ACCEPT AID

The reasons why Third World nations, at least until recently, have been very eager to accept aid even in its most stringent and restrictive forms have been given much less attention than why donors provide aid. This is especially puzzling in view of the many instances where both parties may have conflicting rather than congruent motives and interests.

Basically, however, one can identify three reasons - one major and two minor - why LDC's have sought foreign

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27 IBID, P340

28 IBID, P340

aid. The major reason is clearly economic in concept and in practice. Third World countries have often tended to accept uncritically the proposition, typically advanced by developed country economists, taught in all university "development" courses, and supported by reference to "success" cases like Taiwan, Israel and South Korea to the exclusion of many more "failures", that aid is a crucial and essential ingredient in the development process.[29] It supplements scarce domestic resources; it helps to transform the economy structurally; and it contributes to the achievement of LDC "trade-offs" into self-sustaining economic growth. Thus the economic rationale for aid in LDC's is largely based on their acceptance of the donor's perceptions of what they, the poor countries, require to promote their economic development.[30]

The basic area of conflict arises, therefore, not out of any disagreement about the role of aid but about its amount and conditions. LDC's, naturally, would like to have more aid in the form of outright grants or longer term low cost loans with a minimum of strings attached. This means the abolition of tying aid to donor exports and the granting of greater latitude to recipient countries to decide for themselves what is in their best long-run development interests. The two minor, though still important motivations for LDC's to seek aid are political and moral. In some countries aid is seen by both donor and recipient as providing greater political leverage to the existing leadership to suppress opposition and maintain itself in power. In such instances "assistance" takes the form not only of financial resource transfers but military and internal

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29 IBID, P341

30 IBID, P341

security reinforcement as well. While South Vietnam represents the most dramatic illustration of this "aid" phenomenon in the 1960's, a number of other Third World nations have this political motivation.[31] The problem is that once aid is accepted, the ability of recipient governments to extricate themselves from implied political and/or economic obligations to donors and to prevent donor governments from interfering in their internal affairs can be greatly diminished.

Finally, we come to the moral motivation. Whether on grounds of basic humanitarian responsibilities of the rich towards the welfare of the poor or because of a belief that the rich nations owe the poor "conscience money" for past exploitation, many proponents of foreign aid in both developed and developing countries believe that rich nations have an obligation to support the economic and social development of the Third World. They then go on to link this moral obligation with the need for greater LDC autonomy with respect to the allocation and use of aid funds.

4. WHAT IS AID MEANT TO DO?

4.1 THE CASE FOR AID

The aim of promoting development overlaps with that of alleviating poverty. There is, however, some conflict between the essentially moral case for giving the most aid to those who are poorest, and the desire to maximise the returns from aid by directing it to where it will be used most effectively. This dilemma arises with respect to the allocation of aid between countries and allocation to groups and institutions within

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31 IBID, P341

countries. Most donors have a very deep-rooted belief that aid should lay the foundations for "self-sustaining" growth that will make future aid unnecessary and that if it does not do so, it is in some sense wasted. Implicitly, they work on a very crude mixture of welfare and growth theory, which might be summarised: "aid produces incomes; incomes produce welfare but, for any individual, do so with diminishing marginal efficiency; aid should be allocated in such a way as to maximise welfare.[32] The objectives still carry the implication that aid is good for the recipient. However, one would expect this to be the case if aid truly is a transfer of real resources from the donor to the recipient, and if it does not lead to offsetting reverse flows. This does not tell us how much aid is needed, or how much good it is. The earliest analysis of the effect of aid, accepted capital accumulation as the basis for development, often using a "Harrod-Domar" type of model.[33]

It is evident that one of the main features of underdevelopment is a lack of capital investment and if one asks why there is this lack, the answer given is either that domestic savings are too low to pay for investment, or that there is too little foreign exchange. Such perceptions led to the so-called "two-gap" models of resource needs discussed earlier. One gap being that between savings and investment, and the other that between exports and imports. Some countries were diagnosed as savings-constrained, others as foreign exchange constrained. Courageous attempts were made to estimate the need for foreign capital flows by choosing a desirable growth rate, estimating the two

32 JONES, D, AID AND DEVELOPMENT IN SOUTHERN AFRICA, CROOM HELM, LONDON, 1977, P46

33 IBID, P47

gaps, and taking the larger as the ruling constraint and accepting it as an estimate of foreign capital requirements. The paradoxical thing about this approach is that the two gaps are, and always must be, identical. In fact, if a model shows a savings/investment gap which is different from the export/import gap, it is either incorrect or incomplete.[34]

Developing countries, however, are prone to diagnose their problems as foreign exchange shortage, because of the illusion that they can cover any savings shortfall by recourse to the banking system. It is interesting, however, that BLS countries never diagnosed their problems in this way, because they had no control over currency issue and no independent monetary policy. They therefore saw their constraint as a savings gap, or simply as an inability to raise enough government revenue to cover governmental expenditure.

In some cases, however, there may be some point in saying that the foreign exchange constraint is more important than the savings constraint. This is when the willingness to save, though it exists, is frustrated by the inability to acquire through trade the imports which are required to produce investment goods. If the country is incapable of producing the investment goods it requires, increased savings only helps to the extent that it permits locally produced goods to be diverted to exports, and decreased demands for imported consumption goods, thus alleviating existing foreign exchange earnings to be diverted to imports. If the demand for the country's exports is highly inelastic, higher savings may even have a perverse effect on the capacity to import.

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34 IBID, P47

The capital-based model is, of course, naive. Capital investment is not the only determinant of development, and can be entirely useless if not accompanied by markets, skilled labour, managerial skills, intermediate inputs and ancillary industries and services. To make the capital accumulation approach generally applicable, one needs to broaden the definition of capital to cover many items that would conventionally be classified as consumption: health, education, government services, high-level skills.

However, some of these items are difficult to buy, particularly skilled manpower. Technical assistance can therefore break a development bottleneck by providing resources that are not readily available for import. Other development bottlenecks which can be solved with aid may be structural or the result of inflexible procedures and perceptions, but none the less are real for that. One example is the shortage of recurrent funds experienced by the BLS countries, or the foreign exchange controls may let in trivial imports and keep out vital ones unless they are aid-financed, or donors may perceive the existence of bottlenecks more clearly than recipients. Aid can achieve most if it provides specific resources that could not, or would not, have been obtained without aid, rather than simply providing general resources; and the scope of breaking development bottlenecks is likely to be greater, the more backward and inflexible is the economy concerned.

4.2 THE CASE AGAINST AID

The case against aid is substantial and rests on a number of propositions, the most important of which are the following:

i) Aid permits recipient governments to postpone unpleasant decisions and reforms which are necessary for real development;

ii) Aid distorts economic development by encouraging the recipient to adopt inappropriate technology, inappropriate organisational structures, and inappropriate values;

iii) the negative flows resulting from aid reduce the transfer of resources, and may produce a net negative transfer;

iv) donors use aid to create a situation of economic dependence;

v) donors use aid to keep compliant governments in power;

vi) politicians in recipient countries use aid to further their own ends;

vii) donors interfere with the choice of development strategy.

These objectives all deserve to be taken seriously, though some apply more to direct commercial investment rather than to aid. Point (i) has probably received the most attention because of the debate on whether aid depresses savings rates in developing countries. "This argument rests on implied belief that savings are substantially determined by government policy, and that a government's savings will be less vigorous if greater foreign resources are available."[35] This has an intuitive plausibility about it, more savings mean less consumption, which is seldom good for politicians. The statistical evidence is, however, weak and contradictory.

Savings data are often the residuals from poor national accounts, and hence doubly untrustworthy; the functions

35 IBID, P49

tested were not always well specified; there are non-casual reasons for expecting a negative relationship between savings and capital inflows; e.g. wars and natural disasters lead to low savings and abnormally high aid; some aid is given for purposes like training or technical assistance salaries and is liable to turn up in the national accounts as consumption; though its main purpose is to increase productive capacity. "There is not enough evidence to lead to any firm conclusion on whether aid is a disincentive to saving, let alone on the extent of the disincentive."[36]

However, even if there is a disincentive, this alone would not nullify the benefits of aid. Even the most pessimistic studies generally agree that aid leads to some net increase in investment as conventionally defined. If the definition was widened to cover those "consumption" goods necessary for development, the increase would, of course, be greater. If this produces extra income, it may actually lead to higher total domestic savings, despite lower savings rates. And if marginal propensities to save are below average propensities, the average savings propensity may be raised, even if the marginal propensity is lowered.

Similar negative arguments are advanced about the effect of aid on exports, and on agricultural production. As far as exports are concerned, it may be argued that aid permits over-valuation of the currency if it is not all used for extra imports and, if it is, there may still be an undervaluation of imported capital goods and an incentive to use inappropriate technology. Aid, and particularly food aid, can affect agricultural pricing and be a disincentive to government effort. On the other side, however, the

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36 IBID, P49

existence of aid may actually make it easier to take unpopular decisions, by softening their impact.

On point (ii) - distortion - aid can have all the negative effects mentioned; it need have none of them. The onus is on the donor and recipient to avoid distortions. Strict aid-tying increases the dangers of distortion, since it limits the use of aid to offshore purchase. The tying of aid to specific projects can work either way. It can force distortions on the recipient; it can also force the recipient not to distort and if there is "shunting", it may have no effect either way.

On point (iii), there are negative flows particularly from aid on loan terms. Even if these come to outweigh positive flows, they do not necessarily nullify the benefits of aid, provided they have created productive capacity. However, one cannot reach any general conclusions. "Of BLS, only Swaziland has very substantial negative flows, but these come from investments that have produced substantial increases in the country's productive capacity. Moreover, there is far more cause for concern over foreign direct investment that, in principle, provides perpetual profit outflows, than over 20-25 year aid loans."[37]
Point (iv) has some validity. Donors create some economic dependence simply by tying aid; they may deliberately set out to create more elaborate forms of dependence by, for example, directing aid towards production of raw materials which they require. Recipient countries know this and try to avoid dependency by spreading their aid net. In the case of the BLS countries, one of the aims of U.K. aid as seen by the U.K. and the recipient countries, is to reduce

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37 IBID, P50

economic dependence on the Republic. As for point (v), bilateral donors almost invariably give disproportionate amounts of aid to "friendly" recipients, but they are often sadly disappointed, partly because there is competition among donors. It is arguable that donors more often give way to the political pressures of recipients than vice-versa. So far as point (vi) is concerned, corruption may be part of the process of keeping a friendly recipient friendly, and is equally subject to failure. However, most donors take fairly elaborate steps to avoid simple misappropriation. Other forms of diversion are more subtle: building a road that benefits a Minister's constituency, or which assists his own profit making enterprises, for example. This sort of diversion may well contribute to development, though probably less so than a completely objective choice of projects. Lastly, there is the objection that donors try to impose their own ideas. This, however, cannot be denied, although it is questionable whether it is undesirable. Donors generally pay lip-service to the principle of not interfering in the domestic policies of aid recipients. This suggests various alternative aid strategies. It is, for example, recommended by some that aid be apportioned on a priori basis, and handed out with no strings attached. The problem with this approach is that aid may be used for completely undesirable purposes. It may for example end up in Minister's bank accounts or simply ill-conceived projects. To avoid such dangers, it is sometimes suggested that aid should be given only to those countries whose policies the donor approves of. The snag here is that this involves penalizing populations for the faults of governments. Moreover, this approach still puts pressure on recipient governments to alter their policies. Another superficially non-interfering approach is to work on a strict project-by-project basis. This in practice, leads to bizarre intercountry allocations.

4.3 LEVERAGE AND SHUNTING

This raises the question of how donors influence recipient country policy. "There is always a bargaining process, though it may work in many different ways, and may relate to other altruistic or self interested objectives."[38] The donors offer aid on condition that the recipients do something. There is no limit to what the donors may ask. The price of changing a policy depends on the recipient's degree of attachment to his present policy. If he was going to change it anyway, he can, perhaps, get something for nothing. But though there are no rules, there are implicit protocols and conventions. "One is that it is acceptable for a donor to set conditions on the use of the aid he provides, but that attempts to set conditions on wider political or economic issues constitute unjustifiable interference."[39] For example, if Britain gives aid for primary schools, it may impose conditions on building standards without affecting other aspects of education policy, but if she starts to impose conditions on the curriculum, the age of entry or selection procedure, these make sense only if they are applicable to the whole of the recipient's education policy.

The bargaining process can be opened. On one occasion for example, Lesotho was told that it could have aid only if it accepted a number of specific conditions. However, this oversteps the rule that donors must restrict "leverage" to the use of the aid, and it can cause grave offence. Diplomacy usually demands more subtle methods. The donor has to make his conditions

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38 IBID, P51

39 IBID, P51

clear without making them explicit. Hence, the need for some rather esoteric signalling conventions. Aid negotiations provide a stage for this. Experienced negotiators know the significance of apparently innocent questions about difficulties being experienced in such and such a sector, or a spontaneous offer of technical assistance. Unfortunately, poor negotiators often came away with entirely the wrong message. High-level expatriates play a particularly important role as go-betweens because they can talk freely with both sides.

Outside negotiations, the most common means of leverage is control over the nominal end-use of aid. The extent of specification can vary widely. Britain's programme aid to India, for example, may be restricted to solely British procurement. By contract, development aid to BLS countries is less strictly tied to British goods, but is tightly tied to projects. In either case there are opportunities to shunt aid, and this releases funds to cover expenditures that the donor would not have financed. In other words, shunting is likely to occur when a donor finances a project that is of high priority to the recipient. It is ruled out only when the donor finances something that the recipient would not, or could not have financed without the aid. Thus aid given for primary education may, without any fraudulent diversion of funds really finance a presidential palace if in its absence, the presidential palace would have been forgone. In this case, the control exercised over the end-use of aid may be completely illusory.

It may be argued that political priority projects of the sort that donors refuse to finance have first call on scarce resources even if there is no aid, and therefore that shunting of the aid recipients own funds is unlikely to be a problem, but this is clearly not always true. Primary education may well take precedence over a presidential palace. The only control over shunting of this sort is a wider implicit bargaining process: the knowledge that donors are likely to give less aid if they believe recipients are wasting their domestic resources. It seems unlikely, however, that pure shunting is very prevalent, because donors seldom finance exactly the projects that the recipients would undertake without aid. Donor requirements change the nature of projects and do not affect policies. "In some cases the results are good; in others they are lamentable. Some donors for example, insist on quite inappropriate building standards, and most require some procurement-tying - yet often there is a potential for improving projects and policies".[40] Probably the most important way donors exercise policy influences is through technical assistance, for it is very difficult to refuse an offer of technical assistance from a donor in a sector where the donor is contributing substantial aid. Thus, although project-tying does not necessarily lead to higher expenditure in the sectors that nominally receive the aid, it does lead to considerable donor influence within those sectors.

Shunting also occurs between donors. It is common for several donors to compete for particularly attractive projects. The donor who lands the project will, again, be financing something which would have been financed in his absence. In doing this, he may force another potential donor to use his funds on a less attractive project, which is fine so far as the recipient is concerned, or to spend his funds in another country, which is a net loss to the potential recipient and perhaps to the Third World. The ideal donor is the one who finances the good projects that would not otherwise receive backing.

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40 IBID, P53

A rather obvious point should also be made about the fact that shunting is avoided only when the projects are at the bottom of a recipient's project list. This does not necessarily mean that projects of this sort are of low priority. One of the most important ways in which a donor can exercise a beneficial effect on recipient projects is that, being free of local political constraints, it can sometimes be more far seeing than the recipient and pick up neglected sectors. This can be of considerable assistance to progressive elements in the recipient country.

5. HOW MUCH AID?

The flow of aid from the developed countries to the developing countries forms part of an interrelated system of world trade and investment. At any time capital is flowing to and from countries as the counterpart of the flow of goods and services that are moving across national boundaries. Economic aid, as defined above in terms of goods and services made available on terms other than those which could normally apply, forms part of these flows. It does not make up the major part of world capital flows, although for individual countries it may be particularly significant. For particular countries the question as to how much aid is likely to be available, compared with how much they can usefully use, is a very pertinent question. It becomes more important as countries learn more about the theory and practice of planning their development. For those countries with a central development plan the question as to how much aid they could use and how it should be used becomes a central part of their planning exercise.[41]

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41 HAWKINS, E.K, THE PRINCIPLES OF DEVELOPMENT AID,

"For the donor countries and for the international agencies concerned with the disposal of loan and grant funds, the question arises from the other side. Given the fact that aid funds are always going to be smaller in amount than the sum which can be used effectively throughout the world, how should these funds be allocated? For some donor countries, the question is often answered in non-economic terms."[42] Political considerations, or the existence of old links between countries arising from linguistic, political or historical circumstances, very largely determine the allocation of their available aid. "For the international agencies, however, there does arise the problem as to how limited funds should be allocated amongst the competing claims of member countries. Such a question can only be answered largely in economic terms where political considerations are explicitly ruled out, as for example, in the case of the Articles of Agreement of the World Bank Group.[43]

This leads to the question how much aid can a country take? "On a purely theoretical plane, any amount of economic aid can be swallowed, as an inflow of foreign capital will always increase the volume of aggregate domestic expenditure and, whenever properly used in accordance with a plan, will materialise also in a higher rate of growth of the national income. But the higher this rate, the higher will have to be the relative share of imports in the increment of the national income, because of the lack of free productive capacities, including the skilled labour force, which we consider for the moment to be an importable item.[44]

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[41] Cont. PENGUIN BOOKS LTD, ENGLAND, 1970, P67

[42] IBID, P67

[43] IBID, P68

[44] KALECKI, M, OP CIT, P72

However, two other factors are likely to set a ceiling to the absorptive capacity of the recipient country. On the other hand, there is the problem of financial capacity to service the debt. The better the terms of credit, the less will be the burden on servicing a given volume of credits. But unless new outlets for exports are created, servicing of the debt is likely to become a problem if the country indulges in taking credit for some years. An increasing share of foreign currency earned through exports will be devoted to this aim and the net capacity to import will, in consequence, decrease, unless new credits are taken. "This will start a snowball process, which only shows that even sustained foreign assistance will not solve the problems of the developing countries as long as the stalemate in foreign trade persists. We must never lose sight of the fact that credits are but a form of postponing the payment for a delivery of goods; ultimately this payment will have normally to take the form of an export."[45] On the other hand, the capacity to absorb foreign aid depends to a great extent on the country's availability of skilled manpower of different grades and types. The assumption that skilled labour could always be imported from abroad is unrealistic. At best a developing country can rely for some time on highly qualified foreign technicians, but already the medium grades required in great numbers cannot be brought from abroad due to both difficulties in recruitment and the political complications that are likely to arise. "That is why technical assistance and the so-called 'investment in human resources' should be considered as the complement of economic and foreign aid in the form of credits for the purchase of goods. The volume and forms of such assistance must be

45 IBID, P72

carefully harmonized with the economic development plan. Normally, contracts for the supply of complete industrial plants should contain clauses about technical assistance. But the problem is, of course, broader."[46]

6. THE FORM OF AID

"All aid donors, however, whether national or international financial institutions, have to bear in mind that there are basically only two routes by which capital can be made available to a country to assist its economic development. In the first place, capital can be made available to help finance a particular item of expenditure, and it can be earmarked for this purpose. Those in control of the flow of aid may then lay down that they will help the development of a particular firm, or of a particular sector, or a particular item of expenditure which they believe will have an impact upon the development situation. These items of expenditures have become known as 'projects' and this way of proceedings is known as the 'project approach'. The alternative way, however, is not to bother with the detailed uses for which the resources are required, but to look instead at the overall needs of the economy and to identify the total financial requirements for the development for all purposes. It is then possible to see what the total needs for capital are and to provide an external contribution without designating that it be used for particular items of expenditure. This is the opposite of the project approach and is known as the 'programme' method of finance, because such assistance can be related to a programme of activities over a period of time".[47]

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46 IBID, P73

47 HAWKINS, E.K, OP CIT, P85

6.1 THE PROJECT APPROACH

The project approach follows through all the detailed application of the transfer of resources that has been discussed above. It seeks to define the final items of expenditure for which the resources required from abroad will be used. A good deal depends in practice, of course, on the level of detail involved. In an economy where there are a large number of small economic units, each concerned with expenditure decisions, it is neither practical nor desirable that each of these expenditure decisions be followed through by an aid-giving body from overseas. "The project approach naturally began with those schemes which were relatively large and works best in such circumstances. It is least satisfactory in those sectors where projects are not large in relation to the whole pattern of development expenditures, and this may be the case for most of the field of industry."[48] The basic attractiveness of the projects approach, however, is undoubtedly that it enables an account to be kept of what the money obtained from abroad has been used for; it relates means to ultimate ends. It also receives powerful support from the argument that even where sums of money are made available for aid purposes and employed on a programme basis it is ultimately final expenditures that matter, even if it is difficult or impossible to tally them all up. In principle, therefore, the project method does indicate the final purposes for which resources are being transferred from other parts of the world. The programme approach, which deals only in aggregates, must necessarily tell only part of the story.

48 IBID, P86

6.2 THE DEFINITION OF A PROJECT

Before considering in more detail the advantages and disadvantages of the project approach it is useful to say a few words about the definition of a project. "The broadest definition of such a word is 'proposal of something to be done, a scheme of action'. In looking at the field of foreign aid, however, one is struck at the wide variety of 'schemes of action' which can be covered by the name 'project'. Project is, indeed, a work of art and not of science. In the present discussion, however, a project can be defined as a plan of action involving the use of resources in order to achieve objectives which will result in a permanent change in the environment".[49] Such a plan of action normally involves expenditures which are the counterpart of combining factors of production in new forms. Something new must be created; it is not sufficient for a project to consist of an alternative way of doing something which is already being done with the present means available to the economy. For example, a project would not consist of expenditure in goods and services which are required as raw materials for the ongoing productive process. It would cover an extension of such a process in order to increase output, involving the creation of new productive capacity; it would more often, however, deal with the situation where different goods and services were produced as a result of the activities encompassed by the project. "The essential point is the self-contained nature of the enterprise. It must be a set of activities which can be considered in isolation without the necessity of exploring in detail all the ramifications that may exist between the project and the rest of the world. In other words, a project is

49 IBID, P87

essentially a micro phenomenon and not a macro phenomenon."[50] It is the self-contained nature of a project which distinguishes it from programmes, sector studies and general plans for the whole of the economy. Such activity can normally only be carried on in terms which do not permit or require a detailed examination of the individual economic units involved. A project is essentially the reverse of this situation. It is possible to go into considerable detail and to see the way in which the various elements of the situation fit together and relate to one another.

6.3 THE GENERAL FEATURES OF A PROJECT

A project as a plan of activities, has a number of general features. "There must be a specific aim which can be agreed upon and it must be possible to specify how that aim can be reached. It is this feature, as has already been stressed above, which makes the project approach so attractive in the foreign-aid field since the use of foreign resources can be ultimately linked to the final objectives of the project."[51] In addition, the manner in which the foreign assistance relates to the other resources available can also be demonstrated. It is also possible to set out in detail the technical nature of the project, thus exposing it to a critical evaluation by the appropriate experts. A project will include details such as to the manner in which the objectives are to be reached. In other words, what kind of management will be necessary? How will the additional resources be administered in the most effective manner? "Finally, a project will set out the proposed relationship between the new objectives now sought and past activities and also

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50 IBID, P87

51 IBID, P88

indicate the way in which the plans for the future will link with other possible developments in the same or neighbouring fields."[52] It may be asked why a potential lender or provider of foreign funds should be at all interested in these details.

"The narrowest basis of interests is that involving the capacity of the borrower to repay and service the loan, where lending is involved. This is the long-standing traditional interest of the banker in the activities of his borrowers. It can vary enormously in practice; it may be a general assessment of the overall credit-worthiness of the institution carrying out the project, an assessment which will not involve the detailed plans to make use of the borrowed resources. At the other extreme it may be manifested in a desire to make sure that every step involved in the new enterprise is soundly based."[53] There may also be additional reasons peculiar to particular suppliers of funds; international agencies, for example, have their own reasons, which are not necessarily connected in any way with the nature of particular projects, for insisting on a fairly detailed plan of action. These reasons may be purely institutional in origin.
"The main reason for wishing to relate ends and means in a particular project is to be able to see whether proper use is made of the resources involved.[54]

The yield must clearly be such as to cover the cost of the resources used up in the process of producing it, including whatever is necessary to recompense those who provided the resources and, if necessary, to repay the owners of borrowed funds. This is the aspect which

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52 IBID, P88

53 IBID, P89

54 IBID, P89

concerns any owner of assets which are used in the process of production. However, although many projects are of a commercial nature, there are others where the products are not sold and where it is necessary to think of this question of yields in a much wider context, perhaps even totally distinct from the issue of repayment. At this level one is concerned with the wider principle of the right use of resources. There may be no normal requirement to repay or to recover a return for those setting up the project. There would still, however, be an interest in ensuring that the overall yield to this use of resources is satisfactory compared with the alternatives involved." At bottom, therefore, an interest in the planning and execution of the project is really based upon an application of the principle of opportunity-cost. Is it an adequate use of the resources in the light of all the other alternative uses to which they could be applied?[55] The attractiveness of the project approach to suppliers of aid from overseas lies principally in the accountability aspects. It is possible to consider in detail the manner in which the resources will be used, and it is also possible to follow the progress made by the project. This possibility follows ultimately from the self-contained nature of the activity, which has already been mentioned above. "However, this same feature is also the basis for the main criticism of the project approach, which is that too strict an adherence to the method may discount and ignore the links that exist between projects. In concentrating on specific details of the economy the project designer may be led into thinking that this is the optimum use of the resources available. In practice, of course, a narrow consideration of a project in isolation may not permit the planners to know whether this is the highest yielding use for the resources at hand."[56]

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55 IBID, P89

6.4 THE PROGRAMME APPROACH

"The programme approach, which makes foreign resources available for the purpose of broader objectives than that of an individual project, has emerged in the post-war picture rather slowly. In many respects it marks a reversion to former methods of financial support from abroad."[57] The movement of foreign capital which took place in the last two decades of the nineteenth century and the first decade of this century through the private markets of the Western world to the then developing countries were essentially programme loans. They provided capital either to governments or institutions who did not spell out in detail what they proposed to do with it. The project approach, as developed by the international agencies, and especially by the World Bank Group, was designed to correct the faults of this earlier type of programme lending. Nevertheless, programme lending and grants have always continued to exist. The immediate post-war flows of aid to Europe moved by this route, and even the more developed versions, as practised in the later stages of the Marshall Plan, still remained programme assistance, rather than project assistance. The technique as applied to developing countries was developed by the United States in the period when aid flows were at their peak in the early 1960s. The United States experience is possibly unique, both in scope and in the manner in which a serious attempt was made to relate the aid flows to broad development objectives.

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56 IBID, P90

57 IBID, P91

6.5 THE BASIS OF THE PROGRAMME APPROACH

The programme approach rests fundamentally on two arguments. "Firstly, that it is more easily related to the benefits of overall planning for development purposes; it starts from the idea developed earlier that the problem of development shows up as a lack of resources. The second reason is an awareness of the difficulties and problems that can arise with the application of the project approach."[58] It is limitations of the project approach which encourage people to advocate the use of programme assistance as a more effective way to deal with the development problem." The programme approach arises rather naturally out of the macro-economic framework to which most economists have subscribed since the work of J.M. Keynes. From this is derived both a viewpoint and a form of analysis."[59] The former ascribed the development problem to the kind of gaps discussed above, either gaps in terms of the ability of the community to save, or gaps in terms of an insufficient supply of foreign exchange to permit the economy to move forward as it should." The analysis provides the arguments by which such gaps can be quantified and therefore supports the idea that the most direct route to development lies through the filling in of this gap by supplying the missing resource, by supplementing savings from outside and at the same time providing additional foreign exchange."[60]

6.6 ADVANTAGES OF THE PROGRAMME APPROACH

This method is necessarily limited to the consideration of very broad objectives, often measured in terms of

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58 IBID, P92

59 IBID, P92

60 IBID, P92

target rates of growth of national income or in per capita incomes. Apart from its attractiveness to the more sophisticated planners it also offers a considerable advantage in terms of economy in time and talents. Of course, certain skills are needed to provide the quantitative analysis and make use of it to demonstrate the need. Obviously, however, the skills required are small compared with the quantity and variety of resources that are needed to plan and appraise a large number of projects. A large programme loan or grant may be the equivalent of many different projects and there are economies in scarce manpower in programme aid which cannot be achieved in the project approach. "A second attractive advantage of programme aid is the ease with which it may be related to general policy issues. In many ways the kind of discussion leading up to the calculation of gaps automatically involves the question of policy issues.[61] If one is forecasting a need it is necessary to specify the kind of policies that one has in mind, since the gaps are not unique under changing policy formulations. It is an easy step from that to go to the position whereby the provision of programme assistance is negotiated or contingent upon the adoption of certain policies as quid pro quos for the provision of capital." It is not surprising, therefore, that parallel with the use of programme assistance there has grown up a technique of policy agreements between the donor or lender and the recipient government. These policy agreements may often be complicated, taking into account many aspects of the country's social and economic life."[62]

"Project lending is very unsuitable for this kind of policy linkage. It is possible and quite common to

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61 IBID, P93

62 IBID, P93

link project lending to agreements concerning the policies or attitudes of the institutions receiving the funds. It is difficult to attach general conditions to such project loans if those general conditions are in no way related to the purpose for which the money is being made available".[63] The advantages, therefore, sum up as being of three different kinds. The first is the ease with which the amount of money involved which can be related to the overall growth prospects of the country. This, it must be recognised, depends fundamentally on the correctness of the Keynesian type of analysis and its proper application to the conditions of the country concerned. The second advantage is the economy of time and manpower that comes from making programme loans compared with project assistance. This cost in time offers a considerable saving over the project approach. It may take many months to examine, develop, appraise and approve a project loan since the essence of the approach is attention to detail and there are so many different factors which can hold up the smooth process of providing project aid. By contrast, the programme approach can be swift and it is very economical of the kind of manpower which is often scarcer in developing countries. Speed, of course, may be essential if the funds are to avert short-term crises. In principle, however, it is the main function of the IMF to make such programme assistance available as the need arises; the IMF 'drawing' may well be the most important form of short-term programme lending available to developing countries. "The macro-economic approach which forms the basic justification for programme lending is open to the objection that it conceals the mechanism of development. It illustrates very clearly the overall trends and possibilities for the nation-state. In this

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63 IBID, P93

respect it rather resembles the illustration often used in economics of the distinction between looking at the face of the clock to see the passage of time as indicated by the hands; a proper understanding of the mechanism of the economy can only be gained, as with a clock, if the manner in which the mechanism works is fully understood."[64] An ignorance or a neglect of the detailed workings of the economy can be justified if the smooth running of the machine can be taken for granted. If funds are made available to a country by means of programme assistance, it can only be on the basis of the assumption that their employment will result in an increase in incomes and output through the normal operations of the economy. The chain between cause and effect is not only well established and effective but also fairly well understood. This situation is most likely to be true of a more developed country, however, it is no accident that the most widespread use of programme assistance has been for transfers between the developed countries, as in the massive aid made available from the United States to Western Europe in the early post-war years. Similarly programme loans have been used to transfer resources from the developed countries to the more advanced developing countries on the same basis of belief that there were at least large sections of the economy operating at an acceptable level of efficiency and able to absorb the resources productively. "For other developing countries, however, this cannot be assumed. Either the structure of the economy is primitive or incomplete, or the actual mechanism of operation is seriously deficient. It is somewhat ironic that for these developing countries it appears to be more appropriate to use a project approach although it has been argued above that programmed assistance is the

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64 IBID, P94

more economical of the two forms as far as both time and talent is concerned."[65] A developing country which is short of skilled manpower for administrative and other organisational purposes can find it difficult to provide this talent necessary to develop projects to the point at which they can be financed by overseas aid.

7. THE SOURCES OF AID

"Ever since postwar foreign aid began, there has been a question of whether it should be a national task or a multilateral one. The question has never been resolved. The proof-of-the-pudding principle indicates a movement away from strict, or "beggar my neighbour," bilateral aid and toward coordinate bilateralism, regional multilateralism, and United Nations agencies".[66]

The first large-scale postwar efforts were almost entirely U.S.-financed: UNRRA, the U.S. bilateral loan to Great Britain, and the Marshall Plan. The first and third were administered through international organizations. UNRRA appeared initially to be a convenient device for promoting the fledgling world organization. Unfortunately, from the U.S. viewpoint, decisions were based on the one-country, one-vote principle, so it was soon rejected as inadequate.

The Organization for European Economic Cooperation passed on to Europe the touchy task of allocating a fixed Marshall aid total, and also furnished a basis for the U.S. goal of creating a unified West that could

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65 IBID, P95

66 PINCUS, J, <u>OP CIT</u>, P338

effectively resist soviet pressures.[67] The World Bank, part of the United Nations system, and nominally multilateral (both because of its voting system and because of its loan authority has multinational backing), was de facto as device for channeling U.S. funds to the war-damaged countries. Only in the 1950's did it start to evolve into a lending agency for the South, and large-scale Bank borrowing in Europe is a more recent phenomenon. As the Bank has become increasingly a multilateral agency, it has spawned offshoots: the soft-loan affiliate International Development Association (IDA), and the private industry promotional agency International Finance Corporation.[68] The United Nations itself has not developed successfully as a large-scale lender, despite the steady expansion of its technical assistance work and the surveys and studies of the United Nations Special Fund. However, the South lost the battle to make the United Nations a large-scale aid agency in the mid-1950's. Since then, in the United Nations and at UNCTAD, poor countries have nevertheless repeatedly sponsored and voted resolutions aimed at creating a U.N. capital fund. The North, led by the United States, invariably refuses, unimpressed by the one-nation, one-vote principle as a means of distributing funds supplied by the minority.[69] The evidence demonstrates a steady recent trend towards multilateralism. Between 1960 and 1964, multilateral agency loan and grant disbursements to LDC's rose from $500 million annually to more than $1 billion. In 1964, multilateral disbursements accounted for about 18 per cent of the Northern aid flow, compared with about 10 per cent in the mid-1950's.[70]

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67 IBID, P338

68 IBID, P339

69 IBID, P339

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Probably of more importance in practice than the steady trend to use of international agencies is the increasing use of new forms of international cooperation in the bilateral aid. The most notable example is the Development Assistance Committee of the OECD. It serves a number of purposes. The DAC annual aid reviews offer a form to examine a member's performance by tacit burden-sharing criteria. It also acts with the IBRD as an organizing decide for international aid consortia, which are devices for coordinating large-scale bilateral aid to individual developing countries. The consortium technique has been applied to India, Pakistan, Turkey, and Columbia, among others. It offers a potentially useful method of programming aid by country, very similar in effect to the intent of the World Bank supplementary finance proposal, on a coordinated bilateral basis.[71]

From the U.S. viewpoint, DAC has been only a modest success in the effort to push Europe into carrying some of the Northern aid total. However, it has been useful as an arena for steady pressure to relax lending terms; both the United Kingdom and Germany have succumbed. Meanwhile, ironically, U.S. lending terms have become stiffer, thanks to Congressional refusal to allow AID to lend on IDA terms. These efforts at coordinating bilateral aid have been supplemented by regional forms of multilateral aid on both donor and recipient sides. The Inter-American Development Bank (IDB) is the vehicle for official financial aid under the Alliance for Progress. It is primarily a device for channeling U.S. funds, but it has the advantage in recipients' eyes of being subject to a degree of genuine multilateral control over allocation of funds. IDB

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71 IBID, P339

loans under multilateral control average about $200 million annually.[72]

The EEC Development Fund is the only multilateral agency that gives capital grants. These go primarily to Africa, with commitment levels now averaging about $150 million annually. In a sense, the EEC fund is a Europe-Africa analog of the IDB. To extend the analogy, the IDB combines aspects of both the World Bank and the IDA. Part of the IDB funds are essentially grants of American aid administered by IDB, under the appealing title of the Social Progress Trust Fund. The EEC fund, on the other hand, gives out its aid straight, without the creation of banking and trust fund superstructures. However, EEC has created a European Investment Bank which makes the most of its investments in Europe with less-developed regions of the EEC as frequent beneficiaries.[73]

The political appeal of regional development aid funds is apparently strong. UNCTAD approved two resolutions on regional development funds. The United States has successfully negotiated the creation of an Asian Development Bank (ADB). This organization, with an initial capital of $1 billion, will be open both to countries in the region as donors and recipients, and to those outside the region as donors only. The ten-nation board of directors will have seven regional representatives and three extra-regional ones. The initial capital is to be used for lending on self-liquidating terms, much in the manner of the World Bank. It is hoped that the Bank will receive trust funds to administer on concessional terms in the manner of IDA and the Social Progress Trust Fund. The ADB has

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72 IBID, P340

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also been envisioned by both the United States and Japan as a channel for increasing Japanese aid levels and political commitment to the development of Southeast Asia.[74]

Africa, too, has sought additional trappings of regionalism and attained them in part through an African Development Bank, with headquarters in Abidjan, and aspirations expressed, at least verbally, throughout the continent.[75]

There is something inconsistent about regional development banks organized on the basis of self-liquidating loans. The World Bank repeatedly stated that its supply of funds for self-liquidating projects in the South exceeds the effective demand. On purely economic grounds, therefore, there is some mystery involved in the creation of new organizations aimed at the same purpose.

The motives are obviously, political, fortified by the recipient's aspiration that they will encourage two tendencies: (1) increased flow of funds to the region in question; (2) creation of a magnet to attract funds to be channeled through these banks on concessional terms.[76]

In addition, the voting arrangements for the regional banks give stronger weight to the South than does the World Bank voting system. The donors' interest are still well protected, but the voting system is nonetheless more congenial to the LDC members.[77]

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75 IBID, P341

76 IBID, P341

77 IBID, P341

The proliferation of international aid efforts also reflects certain motives on the donors' part, beyond a desire to satisfy Southern aspirations for control of aid funds. First, there is the belief, fostered by the successful record of the World Bank, that international aid-giving may be more effective than bilateral aid; specifically, more directed for developmental goals and less subject to political pressures. This feeling is reinforced by the demonstrated difficulties of using aid as a political weapon. Generally the political and institutional weight of large-scale bilateral commitments (for example, U.S. aid to India; French aid to Africa) is so great that the donors' freedom to maneuver is limited. If bilateral aid combines political and administrative disadvantages with constant reduction of freedom to maneuver, it is no wonder that the quest for multilateral alternatives is increasing.[78]

On the other hand, despite the flurry of multilateral devices, certain donors and recipients have strong incentives to insist on predominantly bilateral assistance. Some donors feel that they do get substantial political advantage from bilateral aid, despite the difficulties. The United States has used aid as a lever in such countries as Brazil, Turkey, Columbia, Indonesia, occasionally with considerable political effectiveness. Second, some recipients, such as India, Pakistan and the former French African States, are major beneficiaries of the present bilateral system. They have little interest in a switch to multilateralism.[79]

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The forms of multilateral aid and coordinated bilateral aid and their effects on different parties' interests are now so various that simple generalizations have lost whatever value they may once have had. Most LDC's seek more multilateral aid, if it means no net aid loss, providing there is more Southern control over allocation. Similarly, the North generally would prefer multilateral aid, even with diminished control, if it meant no increase in total aid, and if the political gains of the switch outweighed the losses.[80]

Considering the importance that all major donors and recipients place on flexibility for themselves, the trend to multilateral activity will probably continue to be expressed largely through the various hybrid aid resources discussed earlier. The World Bank system, while still in a growth phase, cannot accommodate the parties' search for room to maneuver.[81]

The source of finance for concessional aid is always the same. Whether the paymaster is a government, a regional institution, a United Nations agency, or an international consortium, the grant element is always a transfer of resources whose real cost is paid for by the individuals in the North. There may well be tactical advantages in obscuring the point, but the significance is clear. The North controls the decision as to aid sources. Its control is modified by Southern pressure, and by intra-Northern differences. But the present and future distribution of aid sources should be a relatively accurate reflection of Northern interests in the matter. Multilateralism will become the wave of the future only if these interests are served.[82]

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8. PRINCIPLE FORMS OF ECONOMIC AID

Before discussing principle forms of economic aid in detail, mention should be made on the two general aspects of all such types of aid.

a) Their relationship with the public and the private sectors both in the donor and in the recipient countries.

b) The pros and cons of bi-and multi-lateral arrangements.

As far as the first issue is concerned, the developing countries have good reasons to prefer aid coming from public funds and put at the disposal of the recipient country's government. Such aid eliminates, or at least reduces, possible pressures on the part of powerful private corporations of the donor countries, operating in the recipient countries. At the other end, it makes easier proper utilisation of available foreign assistance in harmony with the economic plan objectives. The least we can say is that it is always possible for the authorities of the recipient country to make use of the foreign aid received in such a way as to strengthen the private sector, if it chooses to do so, while the contrary is not true.[83] It is difficult to imagine that a private concern in the recipient country will avail itself of foreign loans put at its disposal for any other purpose than that of expanding its own productive capacity, however low might be the social priority attached to such a project. The individual interests of firms cannot, of course, be taken as identical with the social priorities established in the plan, unless we believe that the market mechanism allocates investment in the

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83 KALECKI, M, <u>OP CIT</u>, P73

best way. The whole experience of the developing countries belies such a belief; were we to go by market indications alone, we should have a completely lop-sided development, with a hypertrophy of the sector turning out luxuries.

At any rate, planning would have to be considered as perfectly redundant. Actually, making foreign loans available to specified private firms amounts in some cases to influencing the pattern of investment in the recipient country by the donor institution.[84]

Besides, several developing countries are interested in expanding their public sector, as an objective of their economic and social policies, aimed at strengthening their independence and speeding up the necessary structural transformations. While asking for an increased stream of aid coming from public funds and going to the public sector, many economists and politicians at the same time advance unexceptionable arguments in favour of multi-lateral aid, channelled through the United Nations and their specialised agencies, rather than offered through bi-lateral government-to-government contracts.[85] Such a shift towards a system of multi-lateral international aid distribution would, in their opinion, reduce to a minimum the political aspects of aid giving.

Bi-lateral assistance has, however, something to recommend it: it does not require very heavy machinery, it can adjust itself to new and elastic forms and it can be more easily coordinated and harmonised with trade relations, at least between countries adopting some measure of long term planning.[86]

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8.1 GRANTS (GIFTS)

From the strictly economic point of view, a free grant is, of course, the best form of foreign aid. Aggregate internal expenditure exceeds the income generated by the total of the grant and no repayment is involved, either at the moment or in the future. But economic aid has been too much of an instrument of policy, not to have some strings or second thoughts attached in many actual cases of free grants.[87] This is why grants cannot be judged just on their face economic value. But neither can any precise measure be given of the political price attached to them.

8.2 LOANS (CREDITS)

Loans given on terms better than the currently prevailing ones in standard commercial transactions, usually tied to specific investment projects and associated with some form of technical assistance, constitute the bulk of what is termed 'foreign economic aid' given to the developing countries. The borderline between the 'commercial' loans and 'long term' loans is, of course, rather arbitrary and, rigorously speaking, aid should be computed as the difference between the actual cost of credit borne by the recipient country and the cost-to-be of a standard commercial credit.[88] Such an approach would lead, however, to endless complications of a purely technical nature, and make quantitative estimates of foreign aid still more shaky. The more so, because the terms of credits granted to developing countries have recently

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86 IBID, P74

87 IBID, P74

88 IBID, P75

been changing quite substantially, not to speak of the differences attached to the kind of supplies which are offered on deferred payment basis, so that it would be quite difficult to define for reference the 'standard commercial loan'.[89] The recent downward trend in the cost of foreign credits can to a great extent, be ascribed to the action of the Soviet Union and other socialist countries which not only broke the Western monopoly for the supply of industrial equipment to the former colonial and dependent countries, but introduced and generalized the practice of loans, repayable in 10 to 20 years and bearing low rates of interest of no more than 2.5 per cent. Even if the conditions offered by the socialist countries are from time to time overbidden now, we should not forget that before the emergence of the socialist countries on the world market for industrial equipment, the developing countries had to content themselves with much less favourable conditions of deferred payment.

Credits should, therefore, be classified by ranging them from expensive commercial loans to 'soft' credits repayable in local currency over such a length of time that they approach asymptotically the category of grants. Apart from the distinction, already discussed in general terms, between public and private loans, we can classify the different types of credits available to developing countries according to the cost of servicing (including the repayment of the principal) and the modalities of such repayment. The cost of servicing depends on three elements: the grace period, the length of the credit and the rate of interest. The average yearly burden decreases with the length both of the grace period and of the credit itself and increases with the level of the rate of interest. It is more

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sensitive to the first two elements than to the third one.[90] The less the cost of servicing the loan the better the loan is, from the point of view of the recipient country, subject to the note of caution already expressed about grants: the more 'commercial a loan the less likely it is to have political strings attached. In the evaluation of a loan the stipulations about the method of its repayment are just as important as its 'cost'. Broadly speaking, three methods can be distinguished.

a) Repayment in hard (convertible) currency;

b) Repayment in local, unconvertible currency of the recipient country (soft loans);

c) Repayment in goods.

In the first case, the recipient country increases its income from exports in order to earn the necessary hard currency to service the debt, or be prepared to reduce its potential imports to the same amount. Otherwise, it will have to seek new loans to consolidate its foreign debt.[91] However, a loan does not solve the problems of foreign trade, but merely postpones them. Without a lasting solution in the sphere of foreign trade, the only economically - but by no means politically - viable alternative is that of a continuous inflow of grants.

In the second case, the recipient country's situation is somewhat better because the creditor country becomes interested in finding in the recipient country new exportable goods, to be purchased with the local currency received in repayment of the credit. But two dangers always loom: that of financing from these funds part of 'normal' imports, which otherwise would have

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90 IBID, P76

91 IBID, P76

been paid for in hard currency, or that of accumulating a huge sum in local currency, which either will finally have to be converted or may be used as an instrument of interference in the economic life of the recipient country.[92] The soundest from the point of view of the recipient country is the third modality, especially if repayment in goods is negotiated in addition to the 'normal' volume of trade between the countries concerned, or, at least, constitutes part of the foreseen increment in trade relations between the two partners. If equipment for a plant is being furnished on a deferred payment basis and the credit is going to be cancelled out by shipments of part of the output of the new plant, we are in the presence of a truly 'self-liquidating' and mutually advantageous credit. Different variations of the pattern described above have been suggested, from the Indonesian 'production sharing' formula to the industrial branch agreements which combine elements of loans and of long term trade arrangements. These arrangements do not necessarily involve payments in terms of products of a given plant, but may be based on equivalent future exports of other goods. In this regard, relatively cheap loans repayable in goods are the most viable form of aid to developing countries. For they combine, to the mutual interest of the recipient and donor countries, elements of assistance and trade and contribute to a lasting solution of the problem of insufficient export outlets at present affecting so many developing countries. The current practice in this respect, already existing between some socialist and developing countries, should be considerably expanded and equally extended to the sphere of economic relations between the developing and the capitalist developed countries.

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8.3 GRAIN LOANS AND FARMS SURPLUS DONATIONS

A substantial part of American aid to the developing countries takes the form of supplies of grain under the provision of Public Law 480. This is a highly complex form, combining elements of trade loan and grant.[93]

From the point of view of the donor country, i.e. USA, the whole operation consists of shipping abroad a part of the agricultural surpluses, which are anyhow purchased by the Commodity Credit Corporation as part of the policies of support to agricultural incomes. That is why, strictly speaking, no cost whatever is involved on the side of the donor country. PL 480 established four titles under which grain surpluses are delivered to foreign countries, as well as some general conditions, such as the obligation of transporting at least 50 per cent of the grain by ships under the American flag, the necessity of making some additional cash purchases of American agricultural products, the acceptance of the clause forbidding competition with American agricultural goods in third markets, etc. The most important is Title I which is dealt with below in more detail. Title II and III relate to operations of relief, charity and barter transactions. Title IV relates to long-term loans, repayable in dollars, with an additional clause giving the USA some control over the use of the proceeds of the sale of grain in local currency by the government of the recipient country.[94] Title I - as mentioned above, by far the most important - technically deals with cash sales of grain against local unconvertible currency, which are credited to a special account of the donor country, thus creating the so-called 'counterpart funds' but at

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93 IBID, P77

94 IBID, P78

the same time established directly, or by supplementary bi-lateral agreements an elaborate mechanism for the utilisation of the counterpart funds. Part of these funds serves to finance the expenditure of American agencies in the recipient country. Another share is earmarked for loans granted to American private companies operating in the recipient country or local enterprises affiliated to them. These are the so-called "Cooley loans". The rest of the counterpart funds is usually lent or granted by the USA to the government of the recipient country for projects mutually agreed upon. In other words, to the extent to which the counterpart funds finance American activities, this is tantamount to a transfer of funds, which otherwise would have taken the form of transfers of dollars. Similarly, the Cooley loans take the place of an inflow of foreign capital to a particular section of the private sector.[95] To the extent of this utilisation of counterpart funds, PL 480 amounts to replacing certain dollar flows from the donor to the recipient countries by shipment of grain and, therefore, no foreign aid whatever is involved. Roughly speaking one-third of the value of shipments of grain to the developing countries from 1954 till the end of 1964 should be deducted to allow for these transfers (including the Cooley loans).

The grain supplies, which in fact are nothing but grants, have the same double effect as imports of capital in general. On the one hand, they supply the deficient necessities and thus permit the country concerned to develop at a higher rate without inflationary pressures, or counteract existing inflation.

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95 IBID, P78

On the other hand, they ease the problem of financing investment, because the proceeds from the sales of grain provide a source of financing.[96]

As to the release of the counterpart funds for loans and grants for development (excluding the Cooley loans), this has, like all loans in local currency, an effect fully equivalent to deficit financing. Thus, such releases do not constitute any real assistance in financing government investment and must not affect its total volume, determined by the considerations of full utilisation of resources without creating inflationary pressures. If, however, the donor country is reluctant to permit the blockage of counterpart funds and insists on playing the game of releasing them for projects mutually agreed upon, and further supplies of grain, depending on the 'utilisation' of the counterpart funds, this creates a channel for the donor country's influence upon public investment in the recipient country. This effect will grow in importance very quickly unless shipments of grain under Title IV become the dominant form of exports of American agricultural surpluses.[97]

The imponderabilia attached to this situation might be of such a nature as to make it preferable to the developing countries to avail themselves of Title IV rather than of Title I, even though the imponderabilia will not be entirely eliminated in this way and the necessity of servicing the debt in hard currency will have to be faced.[98]

A still better solution would consist in convincing the American government that an accumulation of counterpart

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96 IBID, P79

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funds should not be considered as an obstacle to further supplies of grain under PL 480. Such accumulation could be viewed as a transfer of funds to finance the future activities of American agencies in the recipient country after the deliveries of grain under PL 480 come to an end.[99]

The above is not meant as denying the positive effect of the supplies of grain, apart from the handling of the counterpart funds. However, even with regard to the positive impact of grain deliveries, care should be taken to avoid two negative side effects: a mood of complacency towards the problem of agricultural backwardness on the part of the ruling classes in the recipient country and the temptation to sell the available additional grain supplies at low prices, in order to gain popularity among the urban population, with no regard to the fact that such a policy may discourage local agricultural producers and compel them to reduce the area under food crops. Recent experience of several developing countries shows that both dangers are real.[100]

8.4 FOREIGN DIRECT INVESTMENT

The international flow of financial resources takes two main forms: private foreign investment, mostly by large multinational corporations with headquarters in the developed nations, and public development assistance (foreign aid), both from individual national governments and multinational donor agencies. In this section I will deal with foreign direct investment in the following manner:

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99 IBID, P80

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8.4.1 THE THEORY OF DIRECT INVESTMENTS

Direct investments have played an increasingly important role in the world economy since the Second World War. The United States is by far the most important country engaging in direct investment. Together with Great Britain, the United States accounted for two-thirds of the total book value of foreign direct investments at the beginning of the 1970s. The active agents making direct investments are developed, industrial economies. The large industrial countries are the primary investors; but even smaller, industrially advanced nations like the Netherlands, Switzerland and Sweden are home countries for important multinational firms (M.N.C's) making large direct investments. The country whose direct investments have increased most during the last two decades is Japan.[101]

The largest share of direct investments is carried out in the developed countries. By far the largest single recipient of U.S. direct investment is Canada. Since about 1958, Western Europe, and the E.E.C. countries in particular, has become an increasingly important

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101 SÖDERSTEN, BO, <u>INTERNATIONAL ECONOMIES</u>, MACMILLAN PUBLISHERS LTD, LONDON, 1980, P292

receiver of direct investments from the United States. The multinational corporations also play a major role in some less developed countries.

Roughly two-thirds of all direct investments are made in developed countries and one-third in less developed countries. It is usually the latter which arouses the greatest controversy, since the M.N.C's of the rich countries are often viewed as exploiters of the weaker, less developed economies.[102] The alternative form of investment, portfolio investments, were governed by a wish to maximize the rate of return and to spread risks so as to obtain an optimal portfolio mix of investments which were essentially passive; someone else made the real investments which were financed by the portfolio investments. At the heart of direct investments is control. The investor wants to retain the control over his direct investment himself. The most frequent emissary of a direct investment is the multinational corporation.[103]

Direct investment occurs essentially because a firm has some superior technology or some type of comparative advantage over which it wants to retain control. The best way to retain this control and to improve the firm's standing and profits is through direct investments. A firm or corporation, say in the United States, working under monopolistic or oligopolistic market conditions has developed some new product or new production technique. It wants to generalize the use of its innovation and to increase its possibilities of making a profit from its superior technology. Therefore, it wants to enter foreign markets. The natural way to do this and to enjoy the benefits of its

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superior technology is by direct investment.[104] To understand the determinants of direct investments, it could be useful to set out the following production function:

$$Q=f(L,C,M)$$

Where Q denotes the output produced, L and C are labor and capital, and M managerial skills or organizational technique.

Speaking in terms of factor endowments, we could say that the United States has a large amount of M compared with other countries. This leads to the marginal product of managerial skills, aQ/aM, being lower in the United States than in other countries. The United States, therefore, ought to export products which are intensive in the use of managerial skills. We live in a world where factors of production are at least partially mobile. Some factors, however, are more mobile than others.

The least mobile factor is labor. For legal, institutional and sociological reasons such small parts of the labor force are mobile that we can presume labor to be, for all practical purposes, immobile. Capital is more mobile than labor, but the conditions of supply of capital are not so different between countries as to make capital movements all that important. Furthermore, capital is a joint factor of production, often paired with management. The most mobile factor of production is management.[105]

Executives, or members of the technostructure, as Galbraith calls them, can fairly easily move between countries. The sociological milieu of executives in

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developed industrial countries is not all that different; to be a director of an oil company or a computer corporation in New York, Paris, London or Frankfurt does involve certain differences in the way of life, but the resemblance in general cultural outlook, family life, and above all, in general working conditions is also great. It might even be argued that making an executive career in an international corporation today implies a willingness to spend one's life in different parts of the world. This is also true, though to a somewhat lesser degree, for the interchange between industrial and the less developed countries of a capitalistic type.[106] An important reason for making direct investments is hence a willingness to increase profits by taking advantage of some technological superiority or some superior organizational form. A number of studies have produced empirical evidence of the relationship between knowledge and organizational techniques and the growth of overseas manufacturing investment. Gruber et al. found that U.S. overseas manufacturing investments and manufacturing exports were concentrated in research-intensive industries. A similar relationship has also been established by the U.S. Tariff Commission.[107] In a somewhat analogous manner, the international firm can be thought of as a perfector of markets. One can view the firm as a 'privately owned market' instead of, as is standard, seeing the market as a public coordinating function open to anyone who wants to enter it as an economic agent. The big international firm can be regarded as an international market for inputs and information.

It might be more efficient, it is argued, to have market conditions equalized throughout the world with

106 IBID, P294

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the help of big international firms in various branches of industry, than to have the same equalization process obtained by way of international trade in goods.[108] Before elaborating on the causes of direct investment, it should be observed that the term 'direct investment' is somewhat inadequate. It is not so much a movement capital that is involved in a direct investment as an international movement of techniques or organizations. This improved technique or organization, is often embedded in capital, but the main thing to keep in mind is that capital, most of the time, is only the complementary factor of production in a direct investment.[109] The agent of direct investments is typically the large multinational corporation. Foreign investment is seldom undertaken by a firm until it has gained a strong position in the domestic market. The foreign firm is always at a disadvantage compared with the local producer who knows the language, the customs and the local markets.

Direct investment is typically industry-specific. The significance of this is that it is not so much the transfer of investment between nations as the transfer from one industry in one country to the same industry in another country. Industry-specific investments take two important forms: horizontal and vertical integration. Large corporations wish to integrate horizontally by opening new subsidiaries in various parts of the world. This is often done in a predatory way: one or several existing, competing firms in the host country are simply bought up by a large international rival. In the process competition is often reduced and markets are divided in an oligopolistic fashion.[110]

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108 IBID, P295

109 IBID, P295

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Vertical integration is also a strong motive for direct investments. For instance, there are only a few companies that refine and fabricate copper. It is not astonishing that they also try to achieve control over copper mines by vertically integrating backwards in the production process. One obvious reason for vertical integration is a desire to reduce risk. From the point of view of the international firm, both horizontal and vertical integration can have perfectly rational grounds. They might lead to better control over markets and/or more efficient ways of organizing production. This is, however, not the same as saying that they also are beneficial for governments and consumers in the host countries.[111]

About 90 per cent of all direct investments emanate from the O.E.C.D. countries. The United States is the largest direct investor but it is not the only country making such investments. Direct investments are often a two-sided affair. Most industrial countries are both foreign investors and host countries. The balance varies, with the United States being primarily an investing country while Canada, Belgium and Italy belong more to the second category. In an intermediate position are countries such as Great Britain and the Netherlands, where in 1970 flows of direct investment were approximately the same in both directions.[112]

It is true that, generally speaking, the United States has the most developed technology. But the technological level within any one country varies between sectors. Some sectors are the leading ones, whereas others are relatively backward. This is true

[111] IBID, P295

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in varying degrees for all countries. Therefore, some parts of German industry or of Swedish industry are technologically more sophisticated than the corresponding parts of American industry. This being so, there is a prima facie case for German or Swedish direct investments in the United States. Empirical facts also show that, between industrial countries, direct investments flow in both directions. U.S. direct investments in Europe are much more important than European direct investments in the United States, but there are still flows going in both directions. No such correspondence principle holds, however, for the relations between developed and less developed countries. Here it is a one-sided relationship whereby the developed countries make direct investments in the less developed countries without any offsetting direct investments being made by the less developed countries in the industrial countries. The capital flows from less developed to developed countries are exclusively of a portfolio type.[113]

The essence of direct investments is that it brings one of the three factors of production, managerial skills, or organizational efficiency (M), to work with the other two. Hence the marginal productivity of labor and capital increases in the country where the investment is made. This will lead to an increase in wages for the workers and to an increase in the return to capital because of the foreign investment. However, explanations of direct investment that are based upon these factors are often integrated with theories of industrial organization, particularly those of oligopolistic behaviour. Under free competition there is no room for product differentiation, brand names, etc. and the scope for technical improvement is

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limited. The representative firm is small; it cannot differentiate its product, and it has few resources to devote to research and development.[114]

On the other hand, the conditions of oligopoly, which prevent, for example in the automobile and petroleum industries, a substantial proportion of direct investment abroad, take the form of horizontal expansion into the same or similar lines of production. The firm that successfully produces a differentiated product controls knowledge about serving the market that can be transferred to other national markets at little additional cost. However, it should be noted that although transfer costs are low, the relatively high fixed costs of securing the knowledge act as a barrier to the participation of smaller companies, who may instead prefer a licensing arrangement. At the same time, the alternative of licensing a foreign producer is limited to those cases where the information can be transferred independently of the entrepreneurial manpower or the organizational framework, such as in the case of a 'one-off' technical innovation.[115]

In his work on the evolution of the firm - the so-called 'product-cycle' theory - Vernon has emphasized that a firm tends to become multinational at a certain stage in its growth. In the early stages of the product cycle, initial expansion into overseas market is by means of exports. Because countries are at different stages of economic development, separated by a 'technology gap', new markets are available to receive new products through the demonstration effect of richer countries. Prior to the standardization of

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the production process, the firm requires close contacts with both its product market and its suppliers. However, once the product has evolved in a standard form and competing products have been developed, the firm may decide to look overseas for the lower cost locations and new markets. It is not only that factor inputs may be less expensive abroad but that considerable scale economics from longer production runs may be obtained through the allocation of component production and assembly to different plants.

On the demand side, new markets can be established by price reductions, or more typically by the firm operating in an oligopolistic market situation by means of product differentiation.[116] The product-cycle concept offers a useful point of departure for a study of the causes of international investment but it is important to remember, as Hufbauer has emphasized, that 'the story of international oligopoly is not a story of aggressive expansion by giant multinational companies in a predatory effort to crowd out small local firms' but rather 'a preference for the status quo.' Empirical work has shown that growth has not in fact been an increasing function of size. In an uncertain world, security and counter-strategy take on an increased importance. It is in this light that one should view the phenomenon of vertical integration. In order to secure their lines of supply, multinational corporations integrate 'backwards' by means of foreign investment in the production of a raw material or input. Besides the avoidance of risk, the control of input sources by a form or a small group of firms raises substantial barriers to the entry of new competitors.[117]

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Direct investments are a very complex affair. It is only natural that, in outlining the basic theory, we seek to focus attention on some simple explanations that can take us a long way toward an understanding of the subject. However, several other factors are important. One is protectionist policies, another is closeness to the market, The effect of protectionist policies is quite obvious. Many countries are averse to imports of industrial products. Governments with a protectionist slant often think that such products could, or should, equally well be produced by national firms. They then seek to foster domestic industries by using tariffs and other protectionist means. What such policies cannot do, however, is to deprive the foreigner of his technological or managerial advantage. Such policies, therefore, often induce foreign corporations to undertake direct investments and go directly into the protected market to which they earlier, instead, exported their products.[118]

It is not difficult to find examples of direct investments that have been undertaken for such reasons. Countries such as Argentina and Brazil offered examples of protectionist policies that stimulated direct investments in the late 1940s and early 1950s. Some of the upsurge in direct investments which took place in the E.E.C. countries during the latter part of the 1950s could be explained along similar lines.

Protectionist policies were not the only reasons for the steady increase in direct investments, especially from the United States, which took place in Western Europe from the mid-1950s onward. Western Europe had experienced an unpredicted economic growth. This made

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the European market attractive to many American corporations. Western Europe, especially the E.E.C. countries, had emerged as politically stable industrial countries with mass markets for consumer goods. Currency restrictions were removed and full currency convertibility for non-residents was established for most European currencies at the end of 1958. All this naturally encouraged American direct investments.[119]

Another factor worthy of note concerns size - the fact that most leading American corporations are much larger than their foreign counterparts. Not only is it true that in most fields the American firm represents the most advanced technology, it also typically commands much larger personal and financial resources. In many industries, the petroleum, electronic, and computer industries, for instance, American corporations could take over some very promising and prosperous European firms for defensive reasons - to make sure that there could be no unnecessary competition from foreign firms.[120]

8.4.2 PRIVATE FOREIGN INVESTMENT AND THE MULTINATIONAL CORPORATION

Few developments have played as critical a role in the extraordinary growth of international trade and capital flows during the past two decades as the rise of the multinational corporation (MNC). These huge business firms with their far-flung networks of subsidiaries all marching to the drum of decentralized global profit-maximizing decisions of parent companies located in North America, Europe and Japan present a unique opportunity and a host of critical problems for the

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many developing countries in which they conduct their business.[121] The growth of private foreign investment in the Third World has been extremely rapid. It has risen from an annual rate of $2.4 billion in 1962 to almost $9 billion by the mid-1970s.[122] Direct foreign investment involves much more than the simple transfer of capital or the establishment of a local factory in a developing nation. MNC's carry with them technologies of production, tastes and styles of living, managerial services and diverse business practices including cooperative arrangements, marketing restrictions, advertising and the phenomenon of "transfer pricing". Unlike certain types of foreign aid, the purpose of MNC activities is far from charitable. In many instances, these activities have little to do with the development aspirations of the countries in which they operate. But before analyzing some of the arguments for and against private foreign investment in general and multinational corporations in particular, we outline the character of these enterprises.[123]

8.4.3 MULTINATIONAL CORPORATIONS: SIZE, PATTERNS AND TRENDS

Two central characteristics of multinational corporations are their large size and the fact that their world-wide operations and activities tend to be centrally controlled by parent companies. Many MNCs have annual sales volumes in excess of the entire GNPs of the developing nations in which they operate. Typically, annual sales run into hundreds of millions of dollars. The five largest MNCs now have annual sales volumes of $10 billion or more, while more than

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200 others have annual sales in excess of $1 billion.[124] Such enormous size confers great economic power on MNCs vis-a-vis the countries in which they operate. This power is greatly strengthened by their predominantly 'oligopolistic' market positions, that is, they tend to operate in product markets dominated by a few sellers and buyers.[125] They thus have the ability to manipulate prices and profits, to collude with other firms in determining areas of control, and in general to restrict the entry of potential competition through their dominating influences over new technologies, special skills and consumer tastes through product differentiation and advertising.[126] The largest MNCs have many foreign branches and overseas affiliates. Nearly 200 have subsidiaries in twenty or more countries. Eight of the ten largest are based in the United States, while US firms exercise control over about 30 per cent of all foreign affiliates. Britain, Germany and France together with the United States control over 75 per cent of all MNC affiliates. Estimates put the book value of their total foreign investment in excess of $175 billion with over 80 per cent of that total owned by MNCs in these four countries. Of this total, approximately one-third is located in developing countries. But, given their small size, the LDCs feel the presence of multinational corporations more acutely than do the developed countries.[127] Historically, multinational corporations, especially those operating in developing nations, focused on extractive industries, mainly mineral and raw material production.

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A few 'agribusiness' MNCs became involved in export-oriented plantation agriculture and local food processing. Recently, however, manufacturing interests have occupied a greater share of their activities. At present, manufacturing accounts for almost 28 per cent of the estimated stock of foreign direct investment in LDCs while petroleum and mining represent 40 per cent and 9 per cent respectively. But the overall importance of MNCs in the economies of Third World nations, especially in the manufacturing and service sectors, is rapidly growing. In the 1960s, MNC private direct investments represented about one-fifth of the total flow of resources to LDCs. Moreover, this flow increased at an annual average rate of 9 per cent. Thus, the stock of foreign private investment increased faster than the GNPs of most poor countries during the past decade.[128]

8.4.4 PRIVATE FOREIGN INVESTMENT: ARGUMENTS IN SUPPORT OF AND AGAINST PRIVATE INVESTMENT

Few areas in the economics of development arouse so much controversy and are subject to such varying degrees of interpretation as the question of the benefits and costs of private foreign investment. If, however, we look closely at the essence of this controversy, we will find not so much a disagreement about the influence of MNCs on traditional economic aggregates such as GNP, investment, savings and manufacturing growth rates, as about the fundamental economic and social 'meaning' of development as it relates to the diverse activities of MNCs. In other words, the controversy over the role of and impact of foreign private investment in Third World economies often has as its underlying, though usually unstated,

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basis a fundamental disagreement about the nature, style and character of a desirable development process. The basic arguments for and against the developmental impact of private foreign investment in the context to the type of development it tends to foster can be summarized as follows:[129]

8.4.4.1 ARGUMENTS IN SUPPORT OF PRIVATE INVESTMENT

The pro-foreign investment arguments grow largely out of the traditional neo-classical analysis of the determinants of economic growth. Foreign private investment is typically seen as a way of filling in 'gaps' between the domestically available supplies of savings, foreign exchange, government revenue and skills and the planned level of these resources necessary to achieve development targets.[130]

Therefore, the first and most often cited contribution of private foreign investment to national development is its role in filling the resource 'gap' between targeted or desired investment and locally mobilized savings. A second contribution, analogous to the first, is its contribution to filling the gap between targeted foreign exchange requirements and those derived from the net export earnings plus net public foreign aid. This is the so-called foreign exchange or trade 'gap'.[131]

An inflow of private foreign capital can not only alleviate part or all of the deficit on the balance-of-payments 'current account' but it can also function to remove that deficit over time if the foreign-owned

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enterprise can generate a net positive flow of export earnings. Unfortunately, in the case of import substitution, the overall effect of permitting MNCs to establish subsidiaries behind protective tariff and quota walls is often a net worsening of both the current and capital account balance. Such deficits usually result both from the importation of capital equipment and intermediate products and the outflow of foreign exchange in the form of repatriated profits, management fees, royalty payments and interest on private loans.[132] The third gap said to be filled by foreign investment is the gap between targeted governmental tax revenues and locally raised taxes. By taxing MNC profits and participating financially in their local operations, LDC governments are thought to be better able to mobilize public financial resources for development projects.[133] Fourth and finally there is the gap in management, entrepreneurship, technology and skill which is presumed to be partially or wholly filled by the local operations of private foreign firms. MNCs not only provide financial resources and new factories to poor countries: they also are believed to supply a 'package' of needed resources including management experience, entrepreneurial abilities and technological skills which can then be transferred to their local counterparts by means of training programs and the process of 'learning-by-doing'. Moreover, according to this argument, MNCs can educate local managers about how to establish contacts with overseas banks, locate alternative sources of supply, diversify market outlets and, in general, become better acquainted with international marketing practices. MNCs bring with them the most sophisticated technological knowledge about production processes

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while transferring modern machinery and equipment to capita-poor Third World countries. Such transfers of knowledge, skills and technology are assumed to be both desirable and productive to the recipient nations.[134]

8.4.4.2 ARGUMENTS AGAINST PRIVATE FOREIGN INVESTMENT

There are two basic arguments against private foreign investment in general and the activities of MNCs in particular - the strictly economic and the more philosophical or ideological. On the economic side, the four 'gap filling' pro-private foreign investment positions outlined above are countered by the following arguments. Although MNCs provide capital they may lower domestic savings and investment rates by stifling competition, failing to reinvest much of their profits, generating domestic incomes for those groups with lower savings propensities, inhibiting the expansion of indigenous firms who might otherwise supply them with intermediate products by their practice of importing these goods from overseas affiliates and imposing high interest costs on capital borrowed by host governments.[135]

Although the initial impact of MNC investment is to improve the foreign exchange position of the recipient nation, its long-run impact may be to reduce foreign exchange earnings on both current and capital accounts. The current account may deteriorate as a result of substantial importation of intermediate products and capital goods while the capital account may worsen because of the overseas repatriation of profits, interest, royalties, management fees, etc.[136]

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While MNCs do contribute to public revenue in the form of corporate taxes, they can also diminish that revenue as a result of liberal tax concessions, excessive investment allowances, disguised public subsidies and tariff protection provided by the host government. The management, entrepreneurial skills, technology and overseas contacts provided by MNCs may have little impact on developing local sources of these scarce skills and resources and may in fact inhibit their development by stifling the growth of indigenous entrepreneurship as a result of the MNCs dominance of local markets.[137]

But the really significant criticism of MNCs is usually conducted on more fundamental levels than those briefly outlined above. In particular, Third World countries have commonly raised the following objections:

- Their impact on development is very uneven and in many situations MNC activities reinforce dualistic economic structures and exacerbate income inequalities. They tend to promote the interest of the small number of well-paid modern sector workers against the interests of the rest by widening wage differentials. They divert resources away from needed food production to the manufacture of sophisticated products catering primarily for the demand of local elites and they tend to worsen the imbalance between rural and urban economic opportunities by locating primarily in urban areas and contributing to the accelerated flow of rural-urban migration.

- MNCs typically produce inappropriate products, stimulate inappropriate consumption patterns

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through advertising and their monopolistic market power, and do this all with inappropriate technologies of production. This is perhaps the major area of criticism of MNCs.

- As a result of the above, local resources tend to be allocated towards socially undesirable projects. This in turn tends to aggravate the already sizable inequality between rich and poor and the serious imbalance between urban and rural economic opportunities.

- MNCs use their economic power to influence government policies in directions unfavourable to development. They are able to extract sizable economic and political concessions from competing LDC governments in the form of excessive protection, tax rebates, investment allowances and the cheap provision of factory sites and essential social services. As a result, the private profits of MNCs may exceed social benefits. In some cases, these social returns to host countries may even be negative! Alternatively, a MNC can avoid much local taxation by artificially inflating the price which it pays for intermediate products purchased from overseas affiliates so as to lower its stated local profits. This phenomenon, known as 'transfer pricing', is a major practice of MNCs and one over which host governments can exert little control so long as corporate tax rates differ from one country to the next.[138]

- MNCs may damage host economies by suppressing domestic entrepreneurship and using their superior knowledge, worldwide contacts, advertising skills

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and range of essential support services to drive out local competitors and inhibit the emergence of smaller scale local enterprises.[139]

- At the political level, the fear is often expressed that powerful multinational corporations have the ability to gain control over local assets and jobs. They can then exert considerable influence on political decisions at all levels. In extreme cases, they may even, either directly by payoffs to corrupt public officials at the highest levels or indirectly by contributions to 'friendly' political parties, subvert the very political process of host nations.[140]

Foreign ownership of important parts of a country's industry can stifle scientific research and development work in the host country. The main determinant of direct investments is superior technology or managerial skills. Direct investments, especially U.S. direct investments in Europe, tend to be made in technologically advanced industries whose importance for economic development is great. The research for further development of these key industries tends, however, to be located in the investing country, i.e. primarily in the United States. Thereby the host countries are deprived of the important stimulus given by research in these industries. It is this concern which motivated the demands for a Code of Conduct for the transfer of technology at the fourth conference of UNCTAD.[141]

Thus research tends to be concentrated in the home country. The home country started with a comparative

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advantage in the production of goods which are intensive in research and innovating capacity. By the cumulative effects related to direct investments, this comparative advantage tends to become even more pronounced, and the host countries tend to sink into a position of second rate economic powers.[142]

Another important point in this connection concerns external effects. It is widely believed that expenditures on research and development have important external effects. In the process of developing a certain product or improving production techniques, scientists and technicians are stimulated; new applications valuable outside the immediate project will be discovered; encouragement for, and incentives to, research in universities and other organizations outside the industry will be provided; and so on. A rational attitude geared towards experimenting will be fostered, competent scientists will be trained, etc., and all this will have positive effects on the whole intellectual climate of the country.[143]

If foreign firms via direct investments take over control of important parts of a country's industry, they will tend to shift research to their home country. This could be entirely rational from the point of view of the international firm, which is simply taking advantage of the economies of scale connected with the research activity. It can even be argued that this behaviour is rational from the world's standpoint, because it maximizes world income. It still can have very detrimental effects on the host country, which is deprived of research activities that are perhaps comparatively inefficient but which, to the country

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itself, can be of great importance. How this question is viewed is largely a matter of values.[144]

It depends, in technical language, largely on the kind of preference function used, whether international, for the home country, or for the host country. The tendency, inherent in direct investments, to lead to a reallocation of research activities could also induce scientists and technicians to leave their home countries - to what has popularly been called the 'brain drain'. According to this argument, the United States will induce a 'brain drain' from Canada and Europe; Britain and France, too, will tend to siphon off scientific and technical talent from their formerly dependent areas.[145]

It should be pointed out that such movements of educated and skilled people from the periphery to the center can be explained in rational economic terms. Education is a time-consuming activity, and teaching is a labour-intensive activity. It could therefore be expected that human capital should be produced in low-cost locations, as presumably the less developed or semi-developed countries are, being rich in labour. This is probably to some extent what happens. Several less developed and semi-developed countries have probably in relative terms, quite a large supply of certain types of educated people who might have difficulty finding adequate work in their home countries. As wages are higher in the developed, industrial countries, the educated people will naturally move away from their home countries to more developed countries, i.e. a 'brain drain' will take place. This type of migration is also encouraged by

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laws and institutional factors, as most countries tend to favour immigration of educated persons rather than those with less training. To this should also be added the important fact that these skilled immigrants will be provided with more material capital to work with as the ratio of material to human capital is often much higher in the rich countries. Hence an English scientist will often be more efficient in the United States, and an Indian doctor will be more highly productive in England. The migrating scientist can often truthfully argue that what attracts him to move, to take part in the 'brain drain', is not the increased salary but the opportunity to work with better equipment and more assistance in more congenial surroundings.[146]

How one views the effect on scientific activity induced by direct investments and the consequent 'brain drain' is largely a matter of values. From the world's standpoint, it can be argued that both of these effects are beneficial, as they tend to increase world income. But world income is a fairly abstract concept. There is also little reason why anybody should want to maximise world income irrespective of the effects on the world income distribution. Measures that only make the rich richer and the poor poorer can certainly be questioned.[147]

How we view these problems, therefore, primarily depends on what type of welfare function we use. From the investing country's point of view the secondary effects on research and migration could be all to the good. From the host country's point of view it could be quite another matter. The host country could

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welcome the immediate effects of a direct investment but be highly reluctant toward the secondary effects on research activity and the 'brain drain' that could be induced. If it means, for instance, that a highly promising computer program is abandoned because a domestic firm is being bought up and some very able scientists are induced to move abroad, the negative effects are obvious. Then the country could, instead, choose to engage in a scientifically oriented infant-industry protection in the hope that, after a certain amount of development aid, the firm will become competitive on a world scale.[148]

8.4.5 RECONCILING THE PROS AND CONS

While the above lists provide a range of conflicting arguments, the real debate ultimately centres on different ideological and value judgements about the nature and meaning of economic development and the principal sources from which it springs. The advocates of private foreign investment tend to be 'free-market', private enterprise, laissez faire' proponents who firmly believe in the efficacy and beneficence of the 'free market' mechanism, where this is usually defined as a 'hands-off' policy by host governments. However, the actual operations of MNCs tend to be monopolistic and oligopolistic in practice. Price setting is achieved more as a result of international bargaining and collusion than as a natural outgrowth of free market supply and demand.[149]

Those who argue against the activities of MNCs are often motivated more by a sense of the importance of national control over domestic economic activities and

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the minimization of dominance/dependence relationships between powerful MNCs and Third World governments. They see these giant corporations not as needed agents of economic change but more as vehicles of 'anti-development'. MNCs, they argue, reinforce dualistic economic structures and exacerbate domestic inequalities with their wrong products and inappropriate technologies.[150]

Some opponents, therefore, call for the outright confiscation or the nationalization of foreign-owned enterprises. Other advocate a more stringent regulation of foreign investments, a tougher bargaining stance on the part of host governments, a willingness on the part of LDSs to 'shop around' for better deals and finally, a greater coordination of LDC strategies with respect to terms and conditions of foreign investment.[151] One example of such coordinated strategies was the 1971 decision by the Andean Group in Latin America to require foreign investors to reduce their ownership in local enterprises to minority shares over a 15 year period. Tanzania adopted a similar policy of securing a controlling share of foreign enterprises in line with its "Arusha Declaration" of 1967 on socialism and self-reliance. As might be expected, however, the annual flow of private foreign investment declined as a result of these more stringent conditions.[152]

In view of the strong anti-MNC sentiment being aired in the capitals of many Third World nations and the 'demonstration effect' of the power of OPEC nations to gain increasing control over foreign oil companies, it

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appears that the phenomenal growth of MNC influence in less developed countries in the 1950s and 1960s will not be matched in the 1970s and 1980s. The arguments both for and against private foreign investment have a certain empirical validity while reflecting important differences in value judgements. Perhaps the only really valid conclusion is that private foreign investment can be an important stimulus to economic and social development so long as the interests of both MNC and host country governments coincide.[153]

As long as MNCs see their role in terms of global output or profit maximization with little interest in the long-run domestic impact of their activities, the accusations of the anti-private investment school of thought will gain increasing Third World acceptance. Perhaps there can be no real congruence of interest between the objectives of MNCs and the priorities of LDC governments. On the other hand, a strengthening of the relative bargaining powers of host-country governments through their coordinated activities, while probably reducing the overall magnitude and growth of private foreign investment, may make that investment better fit the real long-run development needs and priorities of poor nations. The net social benefit of this trade-off between quantity and relevance is likely to have a positive impact on national development.[154]

8.4.6 DIRECT INVESTMENTS AND EXPLOITATION

Direct investments have in the Marxian tradition played a double role, and in both roles they have had important political implications. In the first variant, direct investments are necessary to postpone

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the collapse of the capitalist system, and in the second and milder variant they are merely one of many forms of capitalist oppression.[155]

The first line of thought was started by J.A. Hobson and taken up and developed by Lenin. The essence of the argument is that capitalism needs new markets to survive. The inner forces of capitalism, primarily the relentless pursuit and application of new innovations, make it expand to the new territories to find new markets and new consumers to postpone the collapse that history, according to Marx, has in store for it. The drive to technical progress also makes capitalists look for cheaper sources of raw materials in distant countries. Imperialism, according to Hobson and Lenin, is simply the logical consequences of the economic forces inherent in the capitalist system of production.[156]

Marxists of later vintage have some difficulties in explaining this theory in its strict Leninist formulation. The Marxian theories of impending collapse of the capitalist system, impoverishment of the workers, etc., are not easy to uphold in the light of the development of the capitalist system. The strong version of the Marxian theory of direct investments, which argues the necessity to these investments for the survival of the capitalist system, can hardly be sustained. That capitalist countries derive profits from their direct investments abroad is one thing; it is quite another thing to argue that the industrial, capitalist nations are so dependent on the territories they in some sense dominate via direct investments that their economies would break down

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without them. It is hardly correct to argue that the United States, Britain, France etc. are so dependent on their investments or their trade with third countries in general for that matter that their economic systems could not be sustained without them. A certain lowering of U.S. economic welfare would follow if, to take a drastic example, all U.S. foreign investments were nationalized overnight by the countries in question and no compensation paid. But there is no doubt that the effect of such an action would imply marginal changes in the American economy rather than a collapse of its capitalist system.[157]

The strong version of the first line of thought which argues that direct investments are necessary for the survival of the capitalist system is not easy to uphold. Capitalism's power of survival should not be underestimated. However, this does not imply that part of international politics cannot be explained in economic terms, even in fairly crude terms like 'search for profits'. The second tenet of Marxist theory which relates to the need for raw materials has to a certain extent been vindicated in recent years.[158]

This is not primarily due to the strength of Marxist methodology. However, the assumptions underlying the Marxist analysis, with its emphasis on conflict between various factors of production, on the importance of power relationships and of the natural interest on the part of the producers to try to limit competition and control markets, would seem to be more realistic than the often simple-minded, harmony-geared assumptions of neo-classical economics.[159]

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It is not difficult to find examples of varying degrees of economic exploitation. If one country has a strong economic influence over another, and couples that with an allegiance with certain ruling forces of the host country and maintains a close military cooperation with those ruling forces, the host country could be in a difficult position. Then it can certainly be maintained that both political and economic exploitation can occur. Nevertheless, the multinational corporation remains a topic of considerable controversy. There is no doubt that the large multinational firm, through its dominance of local markets and research and development and its ability to shift taxable income, can have substantial negative effects on the host country.[160]

8.5 OTHER FORMS OF AID

8.5.1 COMPENSATORY FINANCE

Fluctuations in export earnings are not themselves of great moment to developing countries although excessive price fluctuations may in the long run reduce export markets. Such devices as the IMF short-term lending facility for countries whose export earnings fall as a result of factors beyond their control are adequate because the problem is minor. The real difficulty lies not with short-term fluctuations around an export earnings trend but with the persistent balance-of-payments problems that plague underdeveloped countries when they try to speed up their economic growth. The two issues cannot always be separated in practice, because a rise or fall in earnings or prices may be temporary or persistent, and there is no way to be sure

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until after the fact. However, it seems clear that the umbrella expression "compensatory finance" lends the mantle of a just claim to the underlying demand - more foreign aid.[161] Proposals for maintaining Southern exchange receipts at an agreed and "fair" level have been circulating since the early 1950's. They have included: (1) schemes for payments from rich to poor countries when the latters' terms of trade decline below some agreed level; (2) payments aimed at assuring stability of export prices; (3) payments for persistent shortfalls in export receipts, either through a sort of international social insurance fund, or through IDA loans.[162] The proposals for compensating a country that experiences deteriorating terms of trade usually involve some form of grant aid automatic or discretionary, if an LDC's terms of trade fall by more than a fixed percentage from some reference point. The payment would be some fraction of the difference between purchasing power of sales at the current terms of trade and their value at the reference point. In some versions, the source of the funds is countries whose terms of trade have improved; in others, it is rich countries in general.[163]

The terms-of-trade approach to compensatory finance has the advantage of being subject to automatic measurement, so that some of the controversy involved in discretionary decision making about how much aid to give to whom can be avoided. The disadvantages are well-known: (1) terms-of-trade is not necessarily a good index of welfare, or of a country's balance-of-payments situation; (2) the reference point chosen may soon become outdated by changes in economic structure;

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161 PINCUS, J, <u>OP CIT</u>, P328

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(3) if the gainers compensate the losers, the result could be transfers among LDC's, instead of from North to South; (4) if the rich compensate the poor, with the objective of easing foreign exchange and capital shortages, why go through the indirect and often inaccurate indicator offered by the terms of trade?[164] The second method of compensatory finance is price stabilization, it is inherent in effective commodity price-fixing schemes, and may either stabilize or destabilize earnings in the long run, depending on demand and supply conditions.[165] The third technique of compensatory finance often called supplementary finance compares actual export receipts and those that would be expected under "normal" circumstances, and would attempt to guarantee a certain level of foreign exchange avenues, offering aid to supplement inadequate export levels, when necessary. The UNCTAD Final Act reached virtual unanimity in supporting a proposal of this kind, advanced by the U.K. delegation. In enacting the resolution entitled "Supplementary Financial Measures," the conference requested the World Bank to study and report on a scheme aimed at dealing with:

" ... problems arising from adverse movements in export proceeds (defined in the resolution as "shortfalls from reasonable expectations") which prove to be of a nature or duration which cannot adequately be dealt with by short-term balance-of-payments support. Its purpose should be to provide longer term assistance to developing countries which would help them to avoid disruption of their development program".[166]

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The World Bank report calls for aid designed to compensate for such shortfalls in export earnings. In the words of the report, the purpose of the scheme is:

"To help assure that the achievement of these (growth) objectives will not be frustrated because foreign exchange earnings from exports do not materialize in the amounts envisaged at the time the investment and aid decision were made".[167]

The report calls for the following system:

(1) LDC's will review their development programs and their payments prospects with the administering agency.

(2) The agency and the country will agree on a "policy package" designed to meet realistic plan targets that would commit the country to economic policies designed to achieve targets.

(3) If the country held to the policies and were still faced with a shortfall in export proceeds over the plan period (4-6 years), due to factors beyond its control, then the agency would advance aid on flexible terms. Financing would be on the basis of net shortfalls during the plan period, after prior year earnings in excess of anticipations were deducted.[168]

The anticipated aid level as estimated on the basis of past experience would be $300-$400 million annually. This system of compensation would be financed by contributions from "all participants" (an internationalese term meaning rich countries), with benefits going only to the South. The transfers would be administered by IDA or a similar agency, and would

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167 IBID, P330

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be distributed on the basis of export shortfalls below "reasonable expectations", and in light of the needs engendered by national development programs.[169]

Schemes of this kind offer flexibility to the donors. If they want to give small amounts, they have only to set "reasonable expectations" low. If they want to munificient, the expectations have only to be inflated. In the IDA-IBRD version, "reasonable expectations" appear to be defined as a blend of objective forecast and calculated aspirations. That is, the target would not be based simply on extrapolation of trends, or even of a more sophisticated balancing of supply and demand forecasts. It would combine the latter with the assumption that the approved candidate for compensatory financing could meet at least some of its aspirations for export growth. The result would be to increase each candidate's chance of receiving compensatory repayments.[170]

Judging the merits of such a scheme is a complex enterprise. From the donor's viewpoint, it offers the advantage of setting up performance criteria for aid that (at least in theory) could be applied to all forms of aid. The compensatory funds would act as a lever to assure that performance criteria are met on all scores. The disadvantage of compensatory aid is that it also sets up an obligation to provide more aid on concessional terms, unless the obligation can be offset by reducing other forms of aid. In the IBRD version, the funds would be supplementary finance, in addition to existing aid; but the Bank's aspirations don't bind member governments.[171]

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169 IBID, P331

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For the recipient, the situation is reversed. He loses freedom of action by making performance commitments, and gains from the increase in aid. If, as the World Bank report anticipates, the aid is an increase over previous levels, then the benefit is clear. No LDC is made worse off, and those whose exports lag are better off. In fact, this is simply another way of stating the objective of the scheme, in its proponents' eyes.[172]

If, on the other hand, this form of compensatory finance simply switches aid among recipients without increasing its volume, then countries whose exports prosper are worse off and those whose exports lag are better off than they would be otherwise. It seems obvious that the unanimous LDC support for compensatory finance was based on the tacit, but questionable, assumption that it would be an automatic supplement to existing aid.[173]

Compensatory finance may or may not offer net benefits to the South as a whole, but it obviously does provide incentives to import substituting industry in the South. When minimum foreign exchange revenues are in effect guaranteed, the guarantee means that a country is penalized if it increases exports above the compensatory finance support level. Therefore, the country is likely to be better off if it uses resources to substitute for imports instead of producing export goods. When import-substituting industry is as profitable as exports, the country is obviously better off. But even when it is less profitable than exports, the recipient may be better off by subsidizing import-

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substituting industry in preference to exports. The subsidy allows it to retain aid that would not be available if export revenues were higher. Naturally, it is possible to incorporate devices that diminish these incentives for export avoidance. The one usually proposed is partial compensation, for example, to give the country suffering a shortfall only half of the gap between actual receipts and expectations. However, no method appears foolproof; there is an inherent contradiction between simultaneous efforts to compensate for export shortfalls and to prevent countries that experience them from benefiting.[174]

Compensatory finance also offers another incentive, regardless of whether there are aggregate benefits to the South - the incentive to cheat. If payments are based on failure of exports to meet specific targets, then the easiest way to gain benefits is by manipulating trade statistics. To a certain extent this effort can be contained by making sure that the total of recorded imports from country X is equal to X's export record. However, this is far from a perfect check in practice for a variety of reasons - imperfections in data, lags in time periods covered, problems created by unwillingness or inability of some importers to furnish the required detail, and so on.[175]

One way of getting around some of the perverse incentives offered by compensatory finance was proposed by the Indian delegation at UNCTAD. Instead of paying a country directly on the basis of export shortfalls, it would require all Northern importers to commit themselves to a minimum level of imports from all LDC's combined. The importer would pay to a central fund an

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amount determined by its shortfall. The money would be paid out to LDC's experiencing export shortfalls. This system gives the North an incentive to import rather than pay cash to the fund, and is therefore consistent with the "trade not aid" approach inherent in encouragement of LDC exports. However, the scheme appears to suffer from one signal deficiency. If the import targets are low enough, or the importers zealous enough in meeting their targets, no money will be paid into the fund and there will be no compensation available for the unfortunate LDC that fails to share in the general trade bonanza. In the absence of additional sources of largesse, the prospective recipient is likely to find himself in a "no trade, no aid" position. Even if money is paid into the fund the fact that it would be distributed according to export shortfalls reintroduces negative incentives.[176]

The best argument for compensatory finance as a technique of aid provides the benefits aimed at by commodity price-fixing schemes without introducing the complex control apparatus that these schemes require. However, there is no objective reason why simpler forms of foreign aid could not be used for the same purpose. The decisive issues remain as stated above: do North and South stand to gain more from an automatic aid system (for countries that meet certain initial standards) than they do from the present one? For the North, the answer depends on changes in the leverage it could exert as a result. For the South, it depends on the balance between constraints imposed and additional resources gained (or increased certainty of receipts from year to year). Clearly for some Southern countries, the bargain described by the IBRD could be a bad one. In order to get access to a modest, but

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[176] IBID, P333

uncertain, aid increment the recipient has to allow international review of its domestic policies. This may be a pretty high price to pay for uncertain benefits. On the other hand, it may provide Southern government international support or pressure for measures it would like to take anyway, but feels hesitant about in the face of domestic opposition. In that event, of course, the "interference" by the outside agency is a welcome safety valve.[177]

8.5.2 INTEREST SUBSIDIES

Another UNCTAD resolution called in effect for Northern subsidy of World Bank or IDA lending rates. The IBRD would borrow at normal terms from private investors; the loans would be supported by member government guarantees. The proceeds would be relent by IDA at concessional terms (30 years, one per cent), and the North would subsidize the difference by contributing to an "interest equalization" fund. The scheme, originally proposed by D.Horowitz, head of Israel's delegation to UNCTAD, was also studied and reported on by the World Bank.[178]

The Bank report expressed doubts about carrying out the proposal on the large scale originally proposed at UNCTAD (annual borrowings and relendings of $2 billion a year) or even on the more restricted scale (of $600 million annually) later proposed by Horowitz. The report found that the private capital markets of Europe and America were not likely to make willing purchases of an additional $600 million of Bank bonds annually at going interest rates. The estimate was that, in the absence of payments constraints, the U.S. market might

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177 IBID, P333

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take $200-$300 million annually, if the bonds were appropriately guaranteed, whereas Europe would take far less. However, there are payments constraints, and some European countries whose payment are in surplus are unwilling to allow increased Bank borrowing for other reasons. The creation of an interest equalization fund for thirty year loans also requires substantial long-term commitments of funds. Therefore, the report was very dubious about Horowitz' proposal. In the light of all this, the report suggested that the donors might be better off if they used other techniques (higher IDA subscriptions, soft loans to IDA) to the same end.[179]

This appraisal may well be realistic, but it is difficult to accept solely on the basis of the report. A major advantage of IBRD, in many donors' eyes, is that its loans are not financed from government budgets. A disadvantage of IDA is that its lending terms are too soft to be self-financed. Yet, IDA terms are increasingly attractive to donors, because the debt service is fast becoming politically difficult. It seems likely that this combination of leverage from appropriated funds and avoidance of anticipated political embarrassments may be more enticing than the World Bank report allows. Of course, this begs the question of restrictions created by payments problems and by the desire of governments and capitalists in many countries to reserve the domestic capital market for domestic borrowers. Since the Bank researchers apparently talked mostly to finance ministries and money men, it is perhaps not surprising that they reached rather negative conclusions. The politics of money, however, is not the exclusive province of the financial community, so that we may not have heard the end of interest subsidy proposals.[180]

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179 IBID, P334

8.5.3 TAX CREDITS

Foreign aid is generally a nuisance to donor governments. There has been considerable political dissatisfaction with aid in the United States and France. It seems clear that most other nations' aid efforts are strongly affected by what the United States and, to a lesser degree, France choose to do.[181] In both countries, the objectives are similar - "What do we get out of it?" and "Why couldn't we keep it at home?" One way to find out how much political support aid has is to make it voluntary but costless. Each government can set up a non-profit corporation to administer foreign aid, financed wholly from private contributions. All contributions would be credited against income taxes up to the full amount of the taxpayer's liability. Thus, a $1,000 contribution, given to the Foreign Aid Foundation, would reduce the tax liability by the same amount. If the tax liability were equal to or less than that amount, then there would be no tax due.[182]

This device would have the effect of more or less definitively answering the question of the appropriate level of aid, from the donor's side. The amounts given would represent what people want to give for foreign aid. It also offers an interesting experiment in public finance. If the government pledges to abstain from foreign aid appropriations, and reduce its budget by that amount, then we would have some idea of whether people really believe what they tell the public opinion polls - that the present level of aid is about right.

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180 IBID, P335

181 IBID, P335

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It would also take aid out of the realm of domestic controversy.[183]

A simpler scheme with the same effect would be to hold a referendum, in which people in donor countries were asked to indicate their ranking of various specified alternative levels of aid. The aid level receiving the highest weighted preference ranking would be adopted by the donor country. Both systems, while gravid with merit, are far removed from most countries' political traditions, at least in foreign policy. Furthermore, if adopted, they would offer developing countries some incentive to plow back the proceeds into campaigns to influence future voting in donor countries. This activity would introduce a neat economic calculus regarding marginal costs and benefits of public relations efforts.[184]

8.5.4 FINANCING EXPORT SUBSIDIES

Export subsidies are a more logical way of financing LDC manufactured exports than preferences. It has been suggested that the local currency of PL.480 sales could be earmarked for industrial subsidies. This has several disadvantages. Once the commodities are sold, the resource transfer is done. There isn't any way to eat the same food twice, normally. Therefore, PL.480 proceeds are not needed. Any government that wants to print money can do so anyway. Second, the system would link the ability to subsidize to PL.480 receipts. In other words, only food-deficit LDC's could subsidize. On the other hand, once we forget the tie-in to food aid, whether for home consumption or export, subsidy has its own merits and is theoretically superior to

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[183] IBID, P336

[184] IBID, P336

protection because it doesn't use restriction as an income vehicle.[185]

8.5.5 TURNOVER TAXES

It has often been suggested that the costs of multilateral programs be supported by taxes on international economic activity, such as international travel, petroleum products, international waterways, or the value of international trade. These proposals have a certain appeal, because they involve international payment for the use of internationally "owned" facilities - the sea and the air. More important, the value of all these activities is high and fast-growing, so that low rates of taxation would have a high payoff. World trade, for example, is increasing at the rate of about eight per cent a year. A one per cent tax on the value of world imports in 1964 would have yielded $1.7 billion. By 1975, the sum would double if trade growth rates stayed the same. The Coffee Council tax on exports, proposed in 1966, is an embryonic application of the principle of trade taxation for economic development use.[186]

8.5.6 TRADE TARGETS

One of the UNCTAD resolutions called for industrial countries to set import targets for trade with underdeveloped countries. This is reminiscent of the European trade liberalization targets of the 1950's, by which Marshall Plan recipients progressively removed quantitative restrictions on trade. It seems unlikely that the North could operate a system of import targets with equal success. How can a fixed level of imports

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be guaranteed without a state-trading system? The only sure way is to set import targets low enough to assure that they will be met by the normal course of business. But in that case, the target is a token.[187]

The trouble with all these devices, except the impractical suggestion of voluntary aid, is that they offer no appeal to Northern self-interest. Food aid or an equivalent for dumping the surplus manufactures of countries with excess industrial capacity are the only obvious techniques. Unfortunately, this runs into two stumbling blocks (1) it interferes with commercial trade; (2) Northern excess capacity is frequently not in lines that allow LDC's to increase their imports easily; the South has its own industries to protect.[188]

8.5.7 OPEC AND DEVELOPMENT ASSISTANCE

Instead of looking only at the traditional aid relationships between the developed 'North' and the underdeveloped 'South', we should also take into account the vast new potential for intra-Third World development assistance growing out of the enormous surplus oil revenues currently being generated by the thirteen members of the Organization of Petroleum Exporting Nations (OPEC). In 1974 alone, a total of $54 billion of surplus oil revenues was available for 'recycling' to the non-oil exporting nations.[189]

While by far the greatest proportion of the 1974 surplus 'petrodollars' were recycled back to the developed industrial nations, a total of $9.5 billion was earmarked for loans and investments in Third World

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187 IBID, P338

188 IBID, P338

189 TODARO, M.P, OP CIT, P342

nations with almost $7.2 billion going into direct bilateral assistance. It is to be hoped than an even greater proportion of future surplus oil revenues will actually find its way back to the non-oil-exporting developing nations whose economies were hit the hardest by the dramatic increase in international oil prices.[190]

There are a number of possible ways in which the major oil exporters can play a significant new role in assisting less fortunate Third World countries. To a large degree they are already initiating such a role. For example, the principal Arab members of OPEC, notably Saudi Arabia and Iran, have been extending sizable grants and credits to neighbouring Arab states like Egypt and Syria. Although much of this assistance is in the form of military and political support, a good deal of it is for genuine economic development. Additionally, Arab oil producers have created an Arab Fund for Economic and Social Development with an initial capital endowment for $300 million as well as a Fund for African Development with an initial outlay of $250 million. A few of the Persian Gulf oil states which have close religious and technical ties with Pakistan are stepping up their development assistance to that country. Outside the Middle East, Venezuela has embarked on an ambitious aid programme to assist needy Latin American nations, while Nigeria has recently initiated an $80 million Special African Aid Fund to be administered by the African Development Bank and to provide long-term, low interest loans to the neediest of African nations.[191]

Of much greater potential significance, however, were two major OPEC initiatives to assist other developing

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countries to increase their agricultural potential and to overcome short-run balance of payments difficulties. First, OPEC, led by Saudi Arabia, initiated and contributed $600 million towards the establishment in 1976 of a new $1.2 billion International Fund for Agricultural Development. The other $600 million was contributed by the developed nations. The fund doubled the external resources being given or loaned at low interest for long-term agricultural development in Asia, Africa and Latin America and will thus help to alleviate the problem of chronic world hunger. Its financial resources are to be replenished each year with Saudi Arabia being the largest single contributor. The voting power within the new fund is divided one-third for OPEC countries, one-third for the developing nations and one-third for the developed world. Thus, for the first time in history there now exists a major international financial institution which is controlled by the Third World. This, indeed, is a remarkable breakthrough in a global economic system which has in the past been totally dominated by the rich nations. It is hoped that it will provide a precedent for future aid relationships in which economically more fortunate developing nations begin to assume increased responsibility for the welfare of their less fortunate colleagues.[192] The second major OPEC initiative, sponsored jointly by Iran and Venezuela, was the decision taken in January 1976 to set aside an annual fund of $800 million to assist those Third World countries whose economics were hurt most severely by the fivefold increases in oil prices. This new fund, which represents an equivalent price reduction of approximately eight cents per barrel of oil (at 1975 prices), provides long-term, interest-free loans to aid other developing nations to meet short-term balance of

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payments deficits and to finance needed development projects and programs. Although initially financed for one year only, the fund if proven successful, will continue to be operated until such time as this form of development assistance is no longer necessary.[193]

8.5.8 OTHER POSSIBILITIES

Among the other possible aid strategies which the now wealthy oil exporting nations might pursue are the following:

8.5.8.1 BILATERAL AID

Expanded bilateral assistance programs ranging from outright grants to low-interest, long term concessional loans would obviously be one of the most important mechanisms for recycling surplus petrodollars to needy developing nations. Moreover, direct private or public investment projects in fertilizer and energy production in the poorest countries would assist these nations to meet their current and future food requirements.[194]

8.5.8.2 EXPANDED FINANCIAL SUPPORT FOR INTERNATIONAL ASSISTANCE AGENCIES

An alternative to direct intra-Third World bilateral assistance would be the channelling of more surplus oil revenues into the major international and regional financial institutions such as the World Bank, the International Monetary Fund, and the Asian, African, and Inter-American Development Banks. Such indirect assistance would have the advantage of all multilateral over bilateral assistance: the minimization of political and/or ideological 'strings'.[195]

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194 IBID, P344

8.5.8.3 CONCESSIONAL OIL SALES

A third possibility would be for OPEC to establish a 'two-tier' or dual price system for their oil sales - a much higher 'market' price for rich industrial nations and a considerably lower 'subsidized' price for Third World oil importers. The problem here as with all dual price systems, is the likelihood of 'black market' operations. In the case of oil, this would probably take the form of the diversion (i.e. re-export) of cheap oil from some Third World nations to the developed nations. An easier and much more feasible possibility, therefore, would be for OPEC nations to sell their oil at a common world price but allow poor Third World Nations to purchase oil at concessional terms - e.g. payment over a 40 to 50 years period at say 3 per cent interest. In effect, at currently high international interest rates, the 'grant' component of such long-term credits would be in excess of 50 per cent (i.e. the 'real' cost to Third World importers would be less than half of the actual market price had they been required to borrow funds to purchase the oil at higher world market interest rates and with considerably shorter repayment periods of 10 to 20 years).[196]

Despite the economic hardships which the quadrupling of international oil prices has had on most less developed nations the oil-exporting countries are nevertheless riding a crest of popularity among their Third World colleagues. They are experiencing this strong sense of identification largely because they have shown that it is possible for small countries, acting together, to

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bring the big industrial giants to their economic knees. But such 'good-will' and peer group identification will quickly vanish if wealthy OPEC nations do not rapidly seize the opportunity to step into the foreign aid vacuum and assume their important new role of economic leadership within the Third World.[197]

9. THE MEANING OF DEVELOPMENT

Before concluding this chapter, it will be useful to define the meaning of development.

9.1 TRADITIONAL ECONOMIC MEASURES

In strictly economic terms, "development" has traditionally meant the capacity of a national economy, whose initial economic condition has been more or less static for a long time, to generate and sustain an annual increase in its gross national product at rates of perhaps 5-7% or more. An alternative common economic index of development has been the use of rates of growth of per capita GNP to take into account the ability of a nation to expand its output at a rate faster than the growth rate of its population. Levels and rates of growth of "real" per capita GNP are normally used to measure in a broad sense the overall economic well-being of a population - that is, how much of real goods and services is available for consumption and investment for the average citizen.[198]

Economic development in the past has also been typically seen in terms of the planned alteration of

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[197] IBID, P346

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the structure of production and employment so that agriculture's share of both declines, whereas that of the manufacturing and service industries increases. This, of course, is the essence of theories of structural change. Development strategies, therefore, have usually focused on rapid industrialization, often at the expense of agriculture and rural development. Finally, these principal economic measures of development have often been supplemented by casual reference to noneconomic social indicators; gains in literacy, schooling, health conditions and services, and provision of housing for instance.[199]

But on the whole, development in the 1960s and 1970s was nearly always seen as an economic phenomenon, in which rapid overall and per capita GNP growth would either "trickle down" to the masses in the form of jobs and other economic opportunities or create the necessary conditions for the wider distribution of the economic and special benefits of growth. Problems of poverty, unemployment, and income distribution were of secondary importance to 'getting the growth job done".[200]

9.2 THE NEW ECONOMIC VIEW OF DEVELOPMENT

The experience of the 1950s and 1960s, when a large number of Third World nations did achieve the overall UN growth targets but the levels of living of the masses of people remained for the most part unchanged, signaled that something was very wrong with the narrow definition of development. An increasing number of economists and policy makers now clamored for the "dethronement of GNP" and the elevation of direct

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199 IBID, P84

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attacks on widespread absolute poverty, increasingly inequitable income distributions, and rising unemployment. In short, during the 1970s economic development came to be redefined in terms of the reduction or elimination of poverty, inequality, and unemployment within the context of a growing economy. "Redistribution from Growth" became a common slogan. Professor Dudley Seers posed the basic question about the meaning of development succinctly when he asserted:

"The questions to ask about a country's development are therefore: What has been happening to poverty? What has been happening to unemployment? What has been happening to inequality? If all three of these have declined from high levels then beyond doubt this has been a period of development for the country concerned. If one or two of these central problems have been growing worse, especially if all three have, it would be strange to call the result "development" even if per capita income doubled".[201]

The above assertion is not idle speculation nor the description of a hypothetical situation. There were a number of developing countries that experienced relatively high rates of growth of per capita income during the 1960s and 1970s but that showed little or no improvement or even an actual decline in employment, equality, and the real incomes of the bottom 40% of their populations. By the earlier "growth" definition, these countries were "developing". By the more recent poverty, equality and employment criteria, they were not. The situation in the early 1980s worsened further as GNP growth rates turned negative for many LDCs and governments were forced to cut back on their already limited social and economic programs.[202] But the

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[201] IBID, P84

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phenomenon of development or the existence of a chronic state of underdevelopment is not only a question of economics or even of quantitive measurement of incomes, employment and inequality.

Underdevelopment is a real fact of life for over 2 billion people in the world - a state of mind as much as a state of national poverty. As Denis Goulet has so forcefully portrayed it:

"Underdevelopment is shocking: the squalor, disease, unnecessary deaths, and hopelessness of it all! No man understands if underdevelopment remains for him a mere statistic reflecting low income, poor housing, premature mortality or underdevelopment. The most empathetic observer can speak objectively about underdevelopment only after undergoing personally or vicariously, the "shock of underdevelopment". This unique culture shock comes to one as he is initiated to the emotions which prevail in the "culture of poverty". The reverse shock is felt by those living in destitution when a new self-understanding reveals to them that their life is neither human nor inevitable......... The prevalent emotion of underdevelopment is a sense of personal and societal impotence in the face of disease and death, of confusion and ignorance as one gropes to understand change, of servility toward men whose decisions govern the course of events, of hopelessness before hunger and natural catastrophe. Chronic poverty is a cruel kind of hell, and one cannot understand how cruel that hell is merely by gazing upon poverty as an object".[203]

The condition of underdevelopment in its totality is thus a consciously experienced state of deprivation

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203 IBID, P85

rendered especially intolerable as more and more people acquire information about the development of other societies and realize that technical and institutional means for abolishing poverty, misery, and disease do indeed exist.[204] Development must, therefore, be conceived as a multidimensional process involving major changes in social structures, popular attitudes, and national institutions, as well as the acceleration of economic growth, the reduction of inequality, and the eradication of absolute poverty. Development, in its essence, must represent the whole gamut of change by which an entire social system, tuned to the diverse basic needs and desires of individuals and social groups within that system, moves away from a condition of life widely perceived as unsatisfactory and toward a situation or condition of life regarded as materially and spiritually "better".[205]

9.3 THREE CORE VALUES OF DEVELOPMENT

9.3.1 LIFE-SUSTENANCE: THE ABILITY TO PROVIDE BASIC NEEDS

All people have certain basic needs without which life would be impossible. These "life-sustaining" basic human needs include food, shelter, health, and protection. When any of these is absent or in critically short supply, we may state without reservation that a condition of "absolute underdevelopment" exists. A basic function of all economic activity, therefore, is to provide as many people as possible with the means of overcoming the helplessness and misery arising from a lack of food, shelter, health and protection. To this extent, we may

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[204] IBID, P85

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claim that economic development is a necessary condition for the improvement in the "quality of life" which is "development". Without sustained and continuous economic progress at the individual as well as the societal level, the realization of the human potential would not be possible. One clearly has to "have enough in order to be more". Rising per capita incomes, the elimination of absolute poverty, greater employment opportunities, and lessing income inequalities, therefore, constitute the necessary but not the sufficient conditions for development.[206]

9.3.2 SELF-ESTEEM: TO BE A PERSON

A second universal component of the good life is self-esteem - a sense of worth and self-respect, of not being used as a tool by others for their own ends. All peoples and societies seek some basic form of self-esteem, although they may call it authenticity, identity, dignity, respect, honor or recognition. The nature and form of this self-esteem may vary from society to society and from one culture to another. However, with the proliferation of the "modernizing values" of developed nations, many societies in Third World countries that previously may have possessed a profound sense of their own worth suffer from serious cultural confusion when they come in contact with economically and technologically advanced societies because national prosperity has become an almost universal measure of worth. Because of the significance attached to material values in developed nations, worthiness and esteem are nowadays increasingly conferred only on those countries who possess economic wealth and technological power - those that have "developed." Again, we may quote Professor Goulet:

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206 IBID, P86

"The relevant point is that underdevelopment is the lot of the majority of the world's population. As long as esteem or respect was dispensed on grounds other than material achievement, it was possible to resign oneself to poverty without feeling disdained.

Conversely, once the prevailing image of the better life includes material welfare as one of its essential ingredients it becomes difficult for the materially "underdeveloped" to feel respected or esteemed ... nowadays the Third World seeks development in order to gain the esteem which is denied to societies living in a state of disgraceful "underdevelopment"... Development is legitimized as a goal because it is an important, perhaps even an indispensable, way of gaining esteem".[207]

9.3.3 FREEDOM FROM SERVITUDE: TO BE ABLE TO CHOOSE

A third and final universal value that we suggest should constitute the meaning of development is the concept of freedom. Freedom here is not to be understood in the political or ideological sense (e.g., the free world), but in the more fundamental sense of freedom or emancipation from alienating material conditions of life and from social servitude to nature, ignorance, other people, misery, institutions, and dogmatic beliefs. Freedom involves the expanded range of choices for societies and their members together with the minimization of external constraints in the pursuit of some social goal we call development. W. Arthur Lewis stressed the relationship between

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[207] IBID, P87

economic growth and freedom from servitude when he concluded that "the advantage of economic growth is not that wealth increases happiness, but that it increases the range of human choice." Wealth can enable a person to gain greater control over nature and his physical environment (e.g. through the production of food, clothing, and shelter) than he would have if he remained poor. It also gives him the freedom to choose greater leisure, to have more goods and service, or to deny the importance of these material wants and live a life of spiritual contemplation.[208]

9.4 THE THREE OBJECTIVES OF DEVELOPMENT

We may conclude that development is both a physical reality and a state of mind in which society has, through some combination of social, economic, and institutional process, secured the means for obtaining a better life. Whatever the specific components of this better life, development in all societies must have at least the following three objectives.

1. To increase the availability and widen the distribution of basic life-sustaining goods such as food, shelter, health, and protection.
2. To raise levels of standard of living including, in addition to higher incomes, the provision of more jobs, better education, and greater attention to cultural and humanistic values, all of which will serve not only to enhance material well-being but also to generate greater individual and national self-esteem.
3. To expand the range of economic and social choices available to individuals and nations by freeing them from servitude and dependence not only in

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relation to other people and nation-states but also to the forces of ignorance and human misery.[209]

We may therefore reformulate and broaden Professor Seer's questions about the meaning of development as follows:

1. Have general levels of living within a nation risen to the point that there has been a lessening of absolute poverty (i.e., deprivation of life-sustaining goods) and of inequality in income distribution, as well as improvements in the level of employment and the nature and quality of educational, health, and other social and cultural services?
2. Has economic progress enhanced individual and group esteem both internally vis-a-vis one another and externally vis-a-vis other nations and regions?
3. Finally, has economic progress expanded the range of human choice and freed people from external dependence and internal servitude to other men and institutions, rather than merely substituting one form of dependence (e.g., economic) for another (e.g., cultural?)[210]

If for a given nation the answer to each of the above three questions is yes, then clearly that nation has undergone development. If the first question (which is equivalent to Seers' three questions) can be answered affirmatively but the other two remain negative, then the country may properly be designated as "economically more developed" yet it remains underdeveloped in a more fundamental sense. In this context, it is more appropriate to refer to the rich nations of the world

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209 IBID, P87

210 IBID, P88

as economically developed and reserve judgement as to whether or not they are actually developed in a more thoroughgoing social, political, and cultural analysis. To paraphrase Seers, if the second and third of these central questions evoke negative responses (i.e., if people feel less self-esteem, respect, or dignity and/or if their freedom to choose has been constrained), then even if the provision of life-sustaining goods and improvements in levels of living are occurring, it would be misleading to call the result development.[211]

10. CONCLUDING REMARKS

Somehow, in the welter of gapmanship, of Southern pressure and of strident voices calling for more aid in the name of almost anything, we may forget some of the simple points about aid. Aid may be small in terms of the North's ability to pay, but it is big to many Southern nations. For such countries as Turkey, Brazil, Chile, India, and some of the French-speaking African states, capital flows from the North are vital elements of the existing politico-economic structure. Foreign capital flows to LDC's from all sources were probably about $10 billion in nominal value in 1964. This amounts in aggregates to about 5 per cent of Southern GNP, or by a more valid analogy, to about one-third of the annual value of Southern gross capital formation in that year. For some countries the capital inflows were larger than domestic savings.[212] Second, this means that no matter how one believes aid should be handled, it necessarily implies a substantial possibility for Northern influence over Southern

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[211] IBID, P88

[212] PINCUS, J, OP CIT, P345

behavior. Naturally, the room for maneuver is greatly reduced by a number of factors, principally: competition among donors; the political inertia of existing commitments; the political dangers of the obvious attempt to use aid as a lever, even if there were no alternative aid sources for the recipient; ignorance about the relationship between specific policies and donors' long-term goals.[213]

If we look on the aid process in economic terms, the effort to exert influence should be viewed as a joint effort by donor and recipient to meet agreed goals. It should be possible to reward performance by increasing aid and to penalize inefficiency by reducing it. In view of the limiting factors described above, such economic targets can be only the justification for marginal aid changes - variations of perhaps the order of 25 per cent maximum, above or below existing aid levels. The presence of conflicting goals make blanket threats and promises entirely incredible, except if there is a prior political motive for large changes. In that case, recipients' development policies are largely irrelevant.[214]

Aid strategy is a rather fine instrument in respect of economic goals, one that has perhaps been used improperly. The reason is simple, but reflects no great credit on donors' perceptiveness. Because political considerations are paramount, proponents of all-or-nothing approach to aid policy invariably lose. Even the suggestion for smaller changes tends to be discussed in donor governments as a predominantly political issue. The opportunities for economic influence are lost, often in the name of political

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213 IBID, P346

214 IBID, P346

goals that would not be genuinely affected by small changes in aid.[215]

Aid strategy has another face. To use influence effectively, you also have to know what you are doing - in this case, the economic effects of policy changes. Unfortunately, there is not much evidence that the use of influence and the knowledge of how to use it are effectively combined. This is the standard complaint of the structuralist economists against IMF policies. Whatever its merits in that case, the effectiveness of donor-induced policy shifts is far from universally endorsed, in North or South. This uncertainty is no surprise. People in LDC's clearly respond to economic incentives, but the structural economic relations, and those that link politics and economics, are not the same as in the North. Hence Northern advice is worth less abroad than at home. Furthermore, the costs of following bad advice are greater in the South because it is poorer.[216]

This leads to an important corollary for aid strategy. If a donor wants to induce someone to change his policies, he should be prepared to underwrite the costs. This is clearly an appropriate policy for economic motives where a subsidy is desirable anyway. But it is equally appropriate in cases where there are no specifically economic grounds for subsidizing change. It is essentially a form of incentive pay for uncertainty. As an illustration, suppose the donor wants Peru to use new hatrack-producing techniques in order to stimulate greater efficiency in the Peruvian hatrack industry and more purchase of donor's hatrack-turning lathes. Peru may be reluctant to do so because

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it believes the new method will raise costs, not lower them. The donor should be prepared to underwrite at least part of the risk. This kind of consideration is particularly important for agricultural changes where the producer may fear that change will bring irreparable loss, and for tinkering with foreign exchange rates and controls, where the LDC is likely to view in advance any change as a change for the worse, destined to bankrupt it internationally.[217]

The search for coincidence of interest should be the guiding principle. Prebisch claims that the transfer of aid is costless to the North in a certain sense, because the South spends all its reserves in the North anyway. This is fine as a sort of second-best solution for unemployment, but with Europe and North America both producing at close to full capacity, the argument doesn't stand up - the North is paying the real cost of aid. It is hard to find much coincidence of material interest in concessional aid. Food aid is one example; support of genuine self-help measures another. A third is as yet largely prospective, and likely to become important only if Northern defense requirements fall. If aid funds can be presented as a major customer for Northern industrial capacity, as military budgets are today, it will naturally tend to build up and sustain its own lobby. A strong Northern producer interest is the South's best friend in court. However, current trends are all in the opposite direction. The North has generally full employment, rising defense budgets, and declining proportions of combined GNP devoted to aid.[218]

The conclusions, provisionally, seem straightforward. There is not much short-run prospect for large

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[217] IBID, P347

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increases in nominal aid levels, unless there should be major reductions in donors' military budgets, because in Northern eyes the current price seems right for the diverse collection of benefits received. This reinforces the argument cited above for using effectively whatever influence can be wisely brought to bear for economic advantage. Development resources will be tight on both sides, for different reasons. It is important to use them as catalystic agents, particularly if the reaction favors all parties. If the search for mutual benefits from aid fails, then it is appropriate to seek other approaches, where mutual benefits are clearer.

However, for donors, aid possesses the advantage of flexibility, for which there is no ready substitute. Therefore, there is no prospect that aid will be abandoned, despite the sentiments of frustration it induces in North and South alike.[219]

11. SUMMARY

In this chapter, an attempt was made to define the concept of foreign aid and its different components. An attempt was also made to show why donors give aid. The reasons why donors give aid were discussed under the following sub-headings:

- Political motivations
- Economic or commercial motivations
- Foreign exchange constraints
- Growth and savings
- Technical assistance
- Absorptive capacity

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- Economic motivation and self-interest.

The issue of why less developed countries accept aid was also discussed and also what aid is meant to do. This was discussed under the following sub-headings:

- The case for aid
- The case against aid
- Leverage and shunting

In this chapter a discussion was also made on the form of aid. Here the project approach as well as the programme approach to foreign aid were discussed. The advantages and disadvantages of both approaches were also highlighted.

The chapter proceeded with a discussion on the various sources of aid, as well as the principle forms of foreign aid. These being grants, loans and direct investment. Other forms of foreign aid ranging from tax credits to concessional oil sales were also highlighted. The multinational corporation, its size, patterns and trends as well as arguments for and against private foreign investment were also discussed.

The chapter ended with a discussion of the meaning of development and covered the following:

- Traditional economic measures
- The new economic view of development
- Three core values of development, these being life sustenance, self-esteem and freedom from servitude.

CHAPTER TWO

BOTSWANA - STATE OF THE ECONOMY

1.1 INTRODUCTION

In chapter 1 we looked at the definition of foreign aid, the different components comprising the concept of foreign aid, as well as how foreign aid has been applied. Chapter 1 also discussed why donors are willing to give foreign aid and also why the less developed countries accept foreign aid.

Chapter 1 also discussed what foreign aid in its various forms is meant to do or achieve as well as addressing the question of how much foreign aid donor countries are prepared to give as well as how much foreign aid the less developed countries expect. All these were general, not specific to any particular country.

However, as we proceed, we are going to look at how foreign aid helped the development of Botswana economically since 1980. In other words, we are going to look in a certain amount of depth at the role and effect of foreign aid in the form of foreign loans, foreign grants and direct investment in the economy of Botswana since 1980.

But first, Chapter 2 will look at the state of the economy of Botswana since 1980. In this chapter we are going to examine Botswana's geographical location. From here we will also examine Botswana's population composition, as well as the ethnic composition.

The chapter will also discuss the availability of natural resources and also indicate which minerals played a dominant role in the economic development of

Botswana since 1980. The chapter will also explore the development of party politics in Botswana as well as the challenge of the unilateral declaration of independence (UDI) in 1965 by what was then known as Rhodesia. The chapter will also look at internal developments as well as external relations in Botswana since 1980.

In the economic sphere, the chapter will also discuss the role played by agriculture, minerals and mining and the manufacturing industry since 1980. The chapter will also discuss energy and water management, foreign trade and balance of payments, government finance, employment and wages, industrial development, tourism and education.

1.2 GEOGRAPHICAL LOCATION

Botswana is a landlocked country located in southern africa and occupies an area of 557,570 sq km, extending 1,115 km NNE to SSW and 951 km ESE to WNW.

Botswana shares its total international boundary of 4,052 km with South Africa (1,778 km); Namibia, or Southwest Africa, (1,461 km); and (Zimbabwe) Rhodesia (813 km). Botswana touches Zambia at the confluence of the Zambezi and Chobe Rivers in the extreme north. This part of the border is a source of controversy with South Africa.[220]

The capital is Gaborone with a 1981 population of 59,657. Gaborone is a comparatively new city and until 1975 had a much smaller population than Serowe (23,661) or Francistown (31,065). Other population centres are

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220 KURIAN, G.T, ENCYCLOPEDIA OF THE THIRD WORLD, VOLUME I, 3RD EDITION, FACTS ON FILE, INC., NEW YORK, 1987, P227

Lobatse (19,034), Selebi-Phikwe (29 469), Kanye (20,215 including seasonal migrants), Maun (14,925), Molepolole (20,565), Ramotswa (13,009) and Mochudi (18,386).[221] The population growth rate is currently estimated at 3,4 percent per annum, and the 1991 population was projected at 1,35 million, of whom 341,149 (25,3 percent) resided in towns.

Botswana is a vast tableland at a mean altitude of 1,000 meters (3,300ft). A gently undulating plateau running from the South African border near Lobatse to a point west of Kanye and from there northward to Bulawayo on the Rhodesian (Zimbabwe) border forms the watershed between the two main natural divisions of Botswana. The fertile land to the south of this plateau is hilly bush country and grassland, or veld. To the west of the plateau, stretching over the border into Namibia, is the Kalahari (also known as Kgalagadi) Desert. The Kalahari is more accurately a semi-desert, or sandy tract, covered with thorn bush and grass. In the extreme northwest lies the area known as Ngamiland dominated by the Okavango Swamps, a great inland delta of some 16,835 sq km (6 500 sq mi), and the Makgadikgadi Salt Pans. Around the swamps and along the northeastern border from Kasane to Francistown there is forest and dense bush.

Most of Botswana is without surface drainage, and apart from Limpopo and Chobe Rivers the country's rivers never reach the sea. The major interior river system is the Okavango, which flows into Botswana from the Angolan Highlands in the northwest to form the Okavango Swamps, a delta covering about 3% of the total land area of the country. About half of this area is perennially flooded and the rest is seasonally flooded.

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From this marsh there is a seasonal flow of water into the ephemeral Lake Ngami and, along the Botletle River, to Lake Dow and the Makgadikgadi Salt Pans. Much of the water is, however, lost through evaporation. The Chobe River in the north flows into the Zambezi after marking the border of the Caprivi Strip for part of its course.[222]

1.3 POPULATION COMPOSITION

The population of Botswana was estimated at 1,068,000 in 1985 based on the last official census held in 1981 when the population was 936,600. The annual growth rate is estimated at 4.8% based on an annual birthrate of 50.5 per 1,000. The population is expected to reach 1,429,000 by the year 2000.[223]

Over 80% of the population is concentrated in the region to the east of the central plateau. Overall population density is 2 persons per sq km (5 persons per sq mi) and the density in agricultural areas is not much higher at 0.48 per hectare.

Although there is considerable mobility (as young people leave their villages each year to seek work in South Africa), there is little urbanization. Only 19.18% of the population is urbanized; there are only 11 towns with over 10,000 inhabitants. However, the pace of urban growth is 8.0%. Urbanization is heaviest along the railway line that runs across the country.

The median age is falling, reflecting a rising birth-rate. Persons below 14 years of age constitute 49.7% of the population, while those between 15 and 64

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222 IBID, P228

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constitute 48.3% and those over 65 2.0%. The male/female ratio is high at 91.3 males for every 100 females because at any given time at least 35,000 males are temporarily absent from the country working in Zimbabwe and South Africa. Three out of every four male Tswana (as citizens of Botswana are called) have worked in South Africa at some point in their lives.[224]

Women hold approximately 24% of paid employment positions. An estimated 41% of central government employees are women, many of them in high-level positions. While there is little overt discrimination, statistics suggest that social custom elevates the rights and privileges of men above those of women. Some 40% of rural households (83% of the total population is rural) are headed by women, and generally their economic situation - access to capital, seeds, labour, and draft animals - is significantly worse than that of households headed by men. Women about to marry may choose civil marriage, in which all property is held in common, or customary marriage, which recognises individual property brought to a marriage. Most women are not aware, however, of the implications of these alternatives. Often a married woman is unable to obtain a bank loan without the signature of her husband, or an unmarried woman without the signature of her father. The government has participated in the preparation of a handbook outlining women's rights in Botswana and established preference points for women who seek government-sponsored development loans.[225]

The political rights of women and minority groups generally are observed. There are two female members of Parliament, one of whom is also Minister of External

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Affairs. The other works as Executive Secretary of the majority political party.

The government has included accelerated family planning programmes in its 1973-78 Development Plan. The target of the Plan is a population growth not exceeding 2.5%. Financial assistance for these programmes is provided by the U.N. Fund for Population Activities, U.S. AID, the Danish International Development Agency and the International Planned Parenthood Federation, which established a subsidiary in Botswana in 1971.[226]

In its National Development Plan 1973-1978, the government indicated that at Botswana's stage of development, economic growth is in no way assisted by the rapidly rising population and that a conscious and planned effort must therefore be made to stabilize the growth of the population.

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DEMOGRAPHIC INDICATORS (1984)	
Population, total (in 1,000)	1,068
Population, males (in 1,000)	515
Population, females (in 1,000)	564
Population ages (% of total)	
0 - 14	49.7
15 - 64	48.3
65 +	2.0
Women ages 15 - 49 (000)	250
Dependency ratio	107.0
Child-woman ratio	869
Sex ratio (per 100 females)	91.3
Median age (years)	15.2
Proportion of urban (%)	19.8
Population density (per sq.km)	2
Rates of growth (%)	3.46
Natural increase rate (per 1,000)	37.3
Crude birth rate (per 1,000)	50.0
Crude death rate (per 1,000)	12.7
Gross reproduction rate	3.20
Net reproduction rate	2.52
Total fertility rate (per 1,000)	6.50
General fertility rate (per 1,000)	215
Life expectancy, male (years)	52.8
Life expectancy, female (years	56.2
Life expectancy, total (years)	54.5
Population Doubling Time in Years at Current Rate	18.6

SOURCE: Kurian, G.T., Encyclopedia of Third World Countries, P.228

1.4 ETHNIC COMPOSITION

According to legend the Tswana are the descendants of the sons of Chief Malope who gave their names to eight communities of the country:

TSWANA TRIBES	%
Bakgatla	5.1
Bakwena	11.5
Bamalete	2.2
Bamangwato	31.7
Bangwaketsi	11.3
Batawana	6.7
Batalokwa	0.6
Barolong	1.7

All tribes except Bamalete belong to the Hurutshe stock. The Bamalete are not Tswana at all but Transvaal Ndebele who have assimilated Sotho culture. In each tribal area there are subordinate tribes. These include Kuba, Mpukusha, Subia, Tswapong, Kalaka, Seleka, Phaleng, Birwa, Pedi, Najwa, Talaote, Kaa, Maherero and Rotse.[227]

There are also small Kalanga, Herero and Bushman (also known as Sarwa) minorities who together number around 30,000. They are generally unrepresented in government or the legislature. The Sarwa belong to the Naron, Auen, and Kung, and Herkum groups. There are over 11,000 nomads in the Kalahari Desert who are sometimes not included in the census. Territoriality is implicit in ethnic descent and each tribe has absolute rights to its own region of dominance.[228]

Botswana has always had a substantial non-African population which plays an active political and economic role. The largest non-African groups are 1,400 Britons, 3,400 South Africans, 2,700 Zimbabweans, and some Asians. In 1976 there were 560 U.S. citizens in the country, of whom 400 were private citizens.

In terms of ethnic and linguistic homogeneity, Botswana ranks 53rd in the world with 49% homogeneity (on an ascending scale in which North and South Korea are ranked 135th with 100% homogeneity and Tanzania is ranked 1st with 7% homogeneity).[229]

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1.5 NATURAL RESOURCES

Shortage of water, resulting from low annual rainfall (average 450 mm) aggravated by considerable fluctuations in the monthly distribution and total seasonal rainfall, is the biggest hindrance to the development of Botswana's natural resources, although a number of projects improved water supply to the main centres of economic activity in the 1970s. Limitations imposed by rainfall make much of the country more suitable for the rearing of livestock, especially cattle, but arable agriculture will have to make much more progress if the industry is to meet employment targets and the country is to become self-sufficient in food. It is estimated that in eastern Botswana 4.45m. ha are suitable for cultivation, of which only about 10% is actually cultivated. Although in the east the irrigation potential is limited, the Okavango-Chobe swamps offer substantial possibilities for irrigation, tentatively estimated at 600,000ha. The much wider range of crops which could be grown under irrigation would greatly add to the country's agricultural production.[230]

In recent years Botswana's economic base has been considerably widened. Substantial deposits of diamonds, copper, nickel, coal, manganese, asbestos, common salt, potash, soda ash and sodium sulphate have been proved (some are already being mined) and the search for further minerals, notably uranium, is continuing. In particular, the major developments of diamond mining at Orapa, Letlhakane and Jwaneng, and copper-nickel mining focused on Selebi-Phikwe, with their attendant infrastructural improvements, are helping to diversify the predominantly agricultural

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230 <u>AFRICA SOUTH OF THE SAHARA</u>, EUROPA PUBLICATIONS LIMITED, 19TH EDITION, ENGLAND, 1990, P268

economy of Botswana and broaden the industrial base. A central generating station on the coalfield at Morupule, which came into operation in May 1987, will greatly lessen Botswana's growing dependence on imported electricity from South Africa. Coal may also become a major export. Large coal reserves have been proved at Serowe and Mmabula, and their exploitation would justify the construction of a trans-Kalahari railway westwards through Namibia to the port of Walvis Bay, a development which is favoured by the government, although confirmation of the project is unlikely in the immediate future. Exploitation of gold reserves at Map Nora, near Francistown, was to begin in 1989. The exceptional variety of wild game in northern Botswana and in the Kalahari Desert offers considerable scope for the expansion of tourism.[231]

1.6 DEVELOPMENT OF PARTY POLITICS

The 1961 elections preceded the formation of Botswana's present-day political parties. The first political party was established in 1959, but this Bechuanaland Protectorate Federal Party proved to be short-lived. In the following year, the Bechuanaland People's Party (BPP) was founded by one of the protectorate's few university graduates, K.T. Motsete. Its secretary-general, Motsamai Mpho, had been a member of the African National Congress of South Africa (ANC) and maintained close links with that organization. A relatively rapid spread of political consciousness, and certainly of factionalism, was stimulated by an influx of politically experienced refugees from South Africa. Within a short time, the BPP split into two factions, one of which, led by Mpho, is now the small Botswana Independence Party (BIP). The rival faction

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subsequently became the more important Botswana People's Party (BPP).[232]

Partly in reaction to the militant stance of the original BPP, Seretse Khama formed the more moderate Bechuanaland Democratic Party (BDP) in January 1962. In 1961 Khama gained a seat on the legislative council and was appointed to the executive council. Khama recruited 10 of the 12 African members of the legislative council to his party. This, at one stroke, made the BDP a major force. Alarmed by the militancy of the rival BPP, a number of whites gave support to Khama's BDP as the lesser of available evils, and the British administration unofficially prepared him to assume office as the first prime-minister. This he duly became in March 1965, when the BDP won the territory's first direct election, gaining 28 of the 31 seats in a new legislative assembly, chosen on the basis of universal adult suffrage in accordance with the provisions of a pre-independence constitution which granted internal self-government. Independence was achieved on 30 September 1966, when Bechuanaland became the Republic of Botswana with Sir Seretse Khama as president.[233]

The immediate post-independence period, marred by years of severe drought and lack of finance, saw four significant party political development. The first was the firm establishment of the BDP (restyled the Botswana Democratic Party) as a national party and the acceptance of Sir Seretse Khama as Botswana's leader. The second was the fading into relative insignificance of the BIP. The third was the apparently increased support in the 'urban' centres from the October 1969

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general elections onwards for Philip Matante's BPP. Following victories in both parliamentary seats in the northern commercial centre of Francistown, the BPP went on to gain majorities in local council elections for Francistown and the neighbouring north-western district council. In both cases Khama's government countered Matante's gains by increasing the number of nominated, as opposed to elected, members of the councils. In response, Matante denounced the BDP as undemocratic and 'neo-colonialist'. Moreover, the BPP and the other two opposition parties were critical of the terms on which the government granted exploitation rights to the country's newly discovered mineral wealth.[234]

The fourth significant party-political development was the emergence of a new organization, the Marxist-orientated Botswana National Front (BNF). It gained in reputation when Chief Bathoen II relinquished his hereditary headship of the Bangwaketse tribe, and, in the 1969 elections, took all three parliamentary seats in the Bangwaketse Reserve for the BNF, unseating the vice-president, Quett Masire, in the process. If an alliance were ever formed between the opposition parties, and in particular between the BNF and the BPP, then the BDP could face a more serious challenge. The elections in October 1974, which left the party situation virtually unchanged, suggested that this would be unlikely. In June 1978 conflict arose when international passports were withdrawn from 17 members of the BNF preparing to leave for a world youth festival in Havana, Cuba. This led to accusations that the BDP sought to undermine all opposition, and to deny it an adequate platform. However, the BDP (which has, in turn, sought to brand the BNF as a subversive force, prepared to seize power through violent means) emerged

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from the October 1979 elections stronger than ever, winning 29 of the 32 seats at stake, increasing its majority by two. The leaders of the three opposition parties all lost their seats to the BDP in a poll of over 50% of registered voters (compared with only 33% in 1974). The BNF, with two seats, remained the official opposition party.[235]

While still unable to dispense wholly with the support of the chieftainship, Khama's government nevertheless significantly reduced the chief's powers, including the crucial one of land allocation (land being held communally), and control of mineral concessions. The opposition parties remained divided and largely ineffectual. There were, however, several potential storm-centres. One was increasing discontent with what was viewed as inadequate rural development. Another was the continued existence of slums in Francistown.[236]

In the early stages of development in the Selebi-Phikwe mining complex, racial tension between expatriate whites and Batswana was reported. Soon afterwards, Sir Seretse announced the creation of a parliamentary standing committee to keep this situation under review and to ensure that the penal code's sanctions against racial insult were enforced. Further tension within the mining areas arose at the diamond fields at Orapa in April 1972, when 400 miners went on strike in protest against a policy, on the part of white managers, which the miners regarded as favouring the employment of blacks from South Africa. The Khama government implemented a policy to control mine wages to avoid major disparity between the income of Botswana miners and the rural population. The government also

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moved to resolve friction in the civil service, introducing a policy of indigenizing senior posts in the police as expatriate officers completed their contracts.

1.7 THE CHALLENGE OF UDI

The unilateral declaration of independence (UDI) by Rhodesia (now Zimbabwe) in 1965 presented the Botswana government with its first challenge in international relations. The railway on which Botswana itself depends, and which is still the main link between South Africa and Zimbabwe, was owned and operated by Rhodesia Railways (and subsequently by National Railways of Zimbabwe, until 1989, when the entire length of track within Botswana was transferred to Botswana Railways). For clear reasons of economic survival, Botswana was in no position strictly to enforce economic sanctions against Rhodesia, and it decided against following Mozambique's example when the latter closed its border with Rhodesia in March 1976. Nevertheless, President Khama denounced the rebel Rhodesian regime, apartheid and the sale of arms to South Africa, with whose economy Botswana continued to be closely linked.[237]

While maintaining the delicate diplomatic balance which history, geography and economics has forced on Botswana, Khama gave increasing support to African nationalist movements in neighbouring white-ruled countries following the independence of the former Portuguese territories and the emergence of a new balance of power in the sub-continent. In 1976 he joined the presidents of Angola, Mozambique, Tanzania and Zambia in bringing a united approach to the issue of Rhodesia and Namibia: ' `e condemning the Turnhalle

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talks on the future of Namibia, they accepted Ian Smith's announcement, in September, of his government's agreement, in principle, to the introduction of majority rule within two years. However, following the failure of lengthy international negotiations Khama joined the other presidents of the 'front-line' states in declaring support for the Patriotic Front (PF), a loose alliance between Joshua Nkomo and Robert Mugabe. Although Botswana denied the nationalist guerrillas the use of military bases, sanctuary was given to guerrilla fighters seeking refuge and to those passing to and from training camps in Zambia. The resultant tensions with the Rhodesian regime prompted President Khama, under pressure from opposition parties, to expand the parliamentary police and to increase the number of border patrols. A permanent defence force was formed in 1977.

The achievement of internationally-recognised independence by Zimbabwe in April 1980 had immediate and profoundly important political repercussions of general benefit to Botswana. Large numbers of Zimbabwean exiles (then estimated at up to 25,000) in Botswana returned to Zimbabwe in the early part of 1980. However, the problem of unrepatriated refugees has continued to bedevil relations between the two countries (see below). The settlement of the Rhodesian conflict permitted the release of substantial Botswana resources for development purposes, and also reopened the alternative trade route through Zimbabwe to Beira in Mozambique, so that Botswana's transport and communications were no longer so dependent upon South Africa. It also made available to Botswana a new source of supply for a whole range of both manufactured goods and raw materials. Finally it ensured an auspicious beginning for a new regional economic and political grouping, the Southern African Development Co-ordination Conference (SADCC).[238]

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The SADCC really came into being at a meeting of the five then 'front-line' presidents, held in Botswana in 1979, when they examined what might develop in the area as a result of Zimbabwean independence. From the outset the emphasis was upon concrete projects of a nature that would be mutually beneficial to all members of the group (which was later expanded to include Lesotho, Malawi, Swaziland and Zimbabwe). In July 1979 the SADCC met at Arusha in Tanzania, where the members formulated their strategy: they agreed that top priority had to be accorded to the co-ordination of transport and communications in the area. On 1 April 1980 the nine southern African countries met in Lusaka. A statement of aims was issued, and different tasks assigned to the members. Botswana undertook responsibility for a regional foot-and-mouth disease control programme as well as a research programme on crop production. The SADCC now maintains its permanent secretariat in Gaborone.[239]

1.8 BOTSWANA SINCE 1980

1.8.1 INTERNAL DEVELOPMENTS

Sir Seretse Khama died in July 1980. Elections to the national assembly in October 1979 had again returned the BDP with an overwhelming majority and demonstrated that Khama had no effective rival in the esteem of the people. He was succeeded by Dr Quett Masire, a founder of the BDP and hitherto the vice-president, who was elected by secret ballot in the national assembly on 18 July 1980 and then unanimously endorsed as president by the legislature on 21 July.[240]

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Masire, a long-serving minister of finance and development planning, had played a pivotal role in the country's economic development. He suffers from having only a narrow political base: he comes from the minority Bangwaketse tribe where he has considerable opposition from more conservative elements. Masire's presidency was renewed in September 1984, when, in a general election to the national assembly, the BDP again won a decisive victory, originally gaining 29 of the 34 elective seats (the number of elective seats having been increased since the previous general election). The 1984 election was contested by the six registered parties, and 78% of the electorate voted. The BNF originally won four of the elective seats; the party's leader, Kenneth Koma, initially failed to gain a seat, losing to the vice-president, Peter Mmusi, by a narrow margin. However, this result was challenged by the BNF, and was subsequently ruled null and void by the high court in October, following the discovery of an unopened ballot box. Mmusi had to relinquish the vice-presidency, but retained his other post as minister of finance and development planning. None the less, his position in the cabinet appeared to be in jeopardy after he was defeated by Koma in a re-contest, held in December. However, following the resignation of an MP in December, Mmusi was appointed to the vacant seat and was subsequently reinstated as vice-president.[241]

Although the BDP's success in the parliamentary elections consolidated its position, some discontent among the population at the country's high level of unemployment was reflected in the outcome of the local government elections (held on the same day as the

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parliamentary elections), in which the BDP lost control of all the town councils except that of Selebi-Phikwe. The BDP's strength was also undermined by the defection, in November 1985, of two prominent party members to the opposition BNF.[242]

Tension between the BDP and the BNF continued to grow in early 1987. In March reports that a five-year-old girl had been abducted in Gaborone, by a female witch-doctor (or sangoma) who was reputedly a supporter of the BDP, led to serious rioting, which some observers interpreted as a reflection of popular discontent over worsening unemployment. The BNF was subsequently accused of provoking the unrest, the sangoma was absolved, a 16-year-old girl was charged with the kidnapping, and two men were charged with disseminating the accusations against the sangoma. In May some members of the BDP alleged that youthful elements within the BNF were being trained in insurgency techniques by Libya and the USSR. The government, however, dissociated itself from these allegations. In September 1987 a referendum was held on constitutional amendments concerning the electoral system; a large majority reportedly voted in favour of endorsing the reforms, although the BNF boycotted the referendum. Parliamentary and presidential elections were due to be held in Botswana in September 1989.[243]

1.8.2 EXTERNAL RELATIONS

In recent years, relations with South Africa have remained strained. Revelations in mid-1980 that the South African armed forces had been recruiting Botswana citizens to serve in Namibia against guerrillas of the

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South West Africa People's Organisation of Namibia (SWAPO) caused concern to the government. The people whom the South Africans recruited were the Basarwa (Bushmen), to act as trackers in the bush war. The Basarwa are amongst the least advanced groups in the country, with little understanding, perhaps, of the implications of their decision. None the less, the revelations caused alarm and President Masire promised an investigation.[244]

During 1981 a contretemps developed with South Africa over the supply of Soviet arms to the Botswana Defence Force (BDF). The South African newspaper, Beeld, described Botswana as 'our own Cuba'. President Masire defended the purchases on financial grounds and reiterated Botswana's adherence to its policy of non-alignment. He described the South African comments as deliberate destabilization tactics, and stated that the instructors who accompanied the arms had all left the country. (Advisors from India subsequently took responsibility for the maintenance of the weaponry). By expanding the capabilities of the BDF, Botswana sought to achieve a more extensive and effective surveillance of its long borders thereby preventing insurgents from crossing into South Africa, and so removing any South African excuse for making punitive raids into Botswana. At the same time, it has remained Botswana policy to accommodate South African refugees, although they are not allowed to use the country as a base for attacks on South Africa.[245]

Botswana has not been immune to South Africa's general destabilizing pressures on its black-ruled neighbours. Several incidents, including, in April 1982, an

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exchange of fire over the border between Botswana and South African troops, have kept the two countries' relationship uneasy. In May 1984 Masire accused South Africa of attempting to coerce Botswana into signing a non-aggression pact similar to that negotiated by the Pretoria government with Lesotho. The president said that South Africa had hinted that, if Botswana refused to sign, it might position troops along the frontier between the two countries and cause disruptions of cross-border traffic. In February 1985 relations were further strained when Botswana asserted that South Africa and one of the 'independent Homelands', Bophuthatswana, had threatened to invade Botswana's territory, under the pretext of mounting 'hot-pursuit' operations against guerrillas of the ANC who were allegedly infiltrating into South African territory from Botswana. Towards the end of February, relations with South Africa appeared to have improved slightly, following a meeting between the two countries at which South Africa reportedly abandoned its insistence that Botswana sign a formal joint security pact. However, relations deteriorated once again in June, following a raid on alleged ANC bases in Gaborone by South African forces, in which at least 15 people were killed. Representatives of the two countries met in September 1985 to discuss demands by Botswana for compensation from South Africa for the June raid. Although Botswana's demands were endorsed by the UN, South Africa was reluctant to pay compensation.[246]

In January and February 1986 there were renewed threats of an attack by South Africa, following armed incidents near the Botswana border. Promises of military aid by Britain and the USA against South African attacks and terrorist infiltration were not sufficient to protect

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Botswana against pressure from South Africa; in February Botswana reiterated its undertaking that it was not to be used as a base for attacks by terrorists, and in March the government expelled ANC representatives. The improvement in relations was short-lived, for in May 1986, in conjunction with attacks on Zambia and Zimbabwe, units of the South African defence force launched land and air attacks on a complex of buildings at Mogaditsane, near Gaborone, causing one death. South Africa once again claimed that its action was aimed at ANC bases. The attacks on all three countries received international condemnation. Although Botswana sympathized with the subsequent upsurge in international opposition to apartheid, the vulnerability of the country's position, both geographically and economically, prevented Botswana from committing itself to the imposition of economic sanctions against South Africa, which was recommended by the SADCC in August.[247]

In early 1987, with the approach of the South African general election in May, tension increased as South Africa warned Botswana and other 'front-line' states that it would launch attacks against them in order to pre-empt disruption of the election by the ANC. In April, within hours of one such warning, four people were killed in a bomb explosion in Gaborone. South African involvement was strongly suspected, despite claims by Pretoria that the bombing was part of an unsuccessful ANC operation directed against South Africa. Later in 1987 there was speculation that South Africa was again attempting to coerce the Botswana government into signing a security accord. Following repeated accusations that Botswana was failing to prevent an alleged mass infiltration of ANC members

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into South Africa via its territory, South Africa implemented stricter security controls at its border with Botswana.[248]

In March 1988 South Africa openly admitted responsibility for a commando raid on a house in Gaborone, in which four alleged members of the ANC were killed. South Africa sought to justify the attack as a counter-insurgency measure, but many observers believed that the raid, conducted on the eve of a South African parliamentary by-election, was a political manoeuvre aimed at securing conservative white support for the ruling National Party in South Africa. In June President Masire announced the capture of two members of a South African defence force which had allegedly opened fire on Botswana security forces in a town south of Gaborone while attempting to conduct a commando raid. South Africa claimed that the unit had been on a mission only to gather information, and that the members of the unit had been fired on by the Botswanans before opening fire themselves. The president also blamed South Africa for a car-bomb attack in Gaborone, several hours after the gun battle, although no link was established between the two incidents. An attempt to rescue the two South African commandos from jail failed in September, and in December they were each sentenced to 10 years' imprisonment for inflicting grievous bodily harm. In early August five alleged members of the ANC were killed by South African police just inside South Africa, near the South Africa-Botswana border: later in that month, the South African army announced plans to construct an electrified fence along a section of South Africa's border with Botswana, to thwart a perceived threat of ANC guerrilla infiltration from Botswana. In mid-December two people

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died in a raid, allegedly by South African commandos, on a Botswana border village. Another alleged South African intrusion occurred towards the end of that month, when a bomb exploded in Gaborone, killing one person. In late March 1989 nine South Africans were expelled from Botswana for 'security reasons'. The Botswana government maintained its strong denials of South African allegations that Botswana permitted ANC guerrillas to use Botswana as an infiltration route into South Africa.[249]

Plans to complete the transfer of control of the railways in Botswana from National Railways of Zimbabwe to Botswana Railways, were delayed in early 1987, amid growing tension between the authorities of the South African 'Homeland' of Bophuthatswana and the Botswana government, which was being pressurized to recognise the 'Homeland' as independent. In late 1986 Bophuthatswana announced that all Botswana train crews would be required to obtain visas to travel through its territory. Major disruption to the rail service was, however, avoided by the introduction of South African train crews to operate the section of rail lines crossing Bophuthatswana. In February 1987 Botswana began construction of a railway line which will bypass Bophuthatswana boundaries. The dispute between Botswana and Bophuthatswana was relaxed in April, when the 'Homeland' agreed to abandon the new visa requirements.[250]

Relations between Botswana and Zimbabwe (whose ideologies are far apart) have been correct rather than friendly. Although Masire made an official visit to Harare in October 1982, tension subsequently increased

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as a large number of former ZAPU guerrillas, supporters of Joshua Nkomo (viewed as insurgents by the Zimbabwe government), crossed the border and entered refugee camps. A sharp deterioration in Botswana-Zimbabwe relations occurred in March 1983, when, with serious unrest in Zimbabwe's Matabeleland province, Nkomo fled to Botswana. Zimbabwe had already claimed that Botswana was providing a base for pro-Nkomo guerrillas, and that these were being sent to South Africa for training. It was, therefore, a considerable relief to the Botswana government when Nkomo left for London after only a few days in the country.[251]

The issue of Zimbabwean refugees in Botswana has continued to beset relations between the two countries. In February and March 1983 the increasing difficulties that had been caused by the presence of growing numbers of refugees from Zimbabwe (there were estimated to be 3,000-4,000 at the Dukwe camp in April) led the Botswana government to agree to impose stricter controls on the refugees. It was reported in May that about 200 refugees, most of whom were believed to be Zimbabwean dissidents, had been expelled from Botswana. In the same month, Botswana and Zimbabwe established diplomatic relations at ambassadorial level. In August the Zimbabwe prime minister, Robert Mugabe, visited Botswana for talks, and it was announced that a joint trade agreement was being drafted. However, the recurrence of incidents on the Botswana-Zimbabwe border between members of the BDF and armed men wearing Zimbabwean military uniforms created further tension, and led to security talks between the two countries in late 1983. In July 1984, however, Zimbabwe claimed that Botswana had repatriated more than 1,200 Zimbabwean refugees, including more than 300 alleged

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guerillas, and relations between the two countries appeared to improve later that year. The first meeting of the Botswana-Zimbabwe joint commission for co-operation was held in October 1984. Following the July 1985 general elections in Zimbabwe, a new influx of refugees threatened to disrupt relations, and in November a Zimbabwe delegation criticized Botswana for its unwillingness to impose a test on potential dissidents. However, at a meeting of the joint commission of defence and security in February 1986, satisfaction was expressed at the successes achieved in combating South African-sponsored attacks along the Zimbabwe-Botswana border. In May 1988 President Masire expressed confidence that the remaining Zimbabwean exiles would return to their country voluntarily as a result of an apparent improvement in the political climate in Zimbabwe, following the signing of a unity agreement between the country's two main political parties in December 1987. However, in April 1989 there were still some 600 Zimbabweans at the Dukwe camp. At the end of that month the Botswana government announced that refugee status for Zimbabwean nationals in the country was to be revoked. Zimbabwean émigrés were advised to seek immediate repatriation.[252]

Botswana is a member of the OAU, the UN and the Commonwealth. It is also a non-aligned nation and its principled stands over issues such as apartheid, coupled with general moderation of approach, have given Botswana an effective voice in many international deliberations.[253]

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1.9 THE ECONOMY SINCE 1980

At independence in 1966, Botswana was one of the 20 poorest countries in the world, with minimal infrastructural development and a predominantly subsistence economy. Government revenues were critically dependent on foreign aid and the remittances of the Botswana males employed in South Africa. Moreover, there were no obvious prospects for economic development outside the beef sector. Dominated by a few large-scale, predominantly expatriate, farmers, the commercial livestock sector was the largest contributor to gross domestic product (GDP) and export earnings. By the early 1980s, however, Botswana's economic performance was exceeding that of all other non-petroleum producing countries in Africa. Real GDP rose by an annual average of over 11% in the 21 years to 1987/88. Measured at constant 1979/80 prices, GDP was estimated at P1,584m in 1986/87, compared with P129m in the year of independence. GDP per head increased from P689 in 1977/78 to more than P2,000 in 1986/87, despite an acceleration in the population growth rate during the period from 3.1% to 3.7% per year. This exceptional record was partly due to the rapid expansion of the beef industry, but the predominant cause was the discovery of valuable mineral resources, especially diamonds. Apart from transforming Botswana's export base, the development of the mineral sector has also helped to stimulate and finance the development of the infrastructure, the manufacturing sector and the social services.[254]

The rise in the mineral sector is reflected in the alteration of economic structure since 1966. The contribution of agriculture to GDP has fallen

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dramatically, exacerbated by the return of drought in 1981/82, from almost 40% of the total at independence to 3% in 1986/87. The contribution of mining increased from 0% to 51% during the same period, and growth in manufacturing, transport and communications, financial and social services sectors was also impressive, if less dramatic. A similar situation has prevailed in exports, with beef sales falling from over 90% of merchandise earnings in 1966 to 4% in 1987. Visible export earnings from diamonds rose from 0% to more than 79% of the total during the same period. When combined with exports of copper-nickel matte, minerals have accounted for 66%-82% of total export earnings since the mid-1970s.[255]

Growth-based on such narrow foundations is vulnerable, as shown in 1981/82, when, owing largely to a depression in the mining sector, GDP growth registered only 4.1%, the lowest growth rate since independence. Long-term growth is also hard to sustain. The sixth National Development Plan (1985-91) has been predicated on a substantial diminution in growth rates to an average 4.8% a year through the levelling out of diamond and beef output and the lack of obvious alternative means to sustain high growth levels, particularly in the minerals sector. However, higher than anticipated diamond production and price levels have meant that the projections for the first four years of the Plan have proved too pessimistic, with real average annual growth rates of about 14% in both 1985/86 and 1986/87. In 1987/88 and 1988/89, growth in GDP slowed to an average annual rate of about 8.7%, but remained substantially higher than the population increase rate. The trend towards slower growth in GDP indicates that the next decade will be a major

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challenge, if job creation is to keep pace with growth in the labour force, and if high income differentials, particularly between the formal and traditional sectors, are to be reduced.[256]

1.9.1 AGRICULTURE

Despite recent rapid urbanization, an estimated 65.2% of the formal-sector labour force was engaged in agriculture in 1987, while many other Botswana were subsistence farmers. Composed partly of semi-desert and partly of a savannah area with highly erratic rainfall and relatively poor soils, Botswana is more suited to grazing than to arable production. There have been some recent attempts to compensate for this through development of the country's irrigation potential, but agriculture remains dominated by the livestock sector generally, and the cattle industry in particular, which contributes over 80% of agricultural GDP.[257]

The national herd increased dramatically after independence, from 1.4m head in 1965 to a peak of almost 3m in 1981, stimulated by improved beef export prices, the expansion of available grazing through drilling of new boreholes, and the establishment of effective disease control, based on a system of cordon fences and vaccination, which has kept the country free of foot-and-mouth disease since 1981. The cordon system has opened up the lucrative European market, which offers preferential terms to Lome Convention signatories able to satisfy the stringent disease-control criteria, but it has also involved the government in international controversy over the impact

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on wildlife. The criticism has been intensified by the fact that the economic benefit of beef exports has largely accrued to the 5% of households who are estimated to own more than one-half of the national herd, with about 20% of the total held by the country's 360 large-scale commercial farms. Approximately 50% of rural households neither own nor have any access to cattle, and many others rely on the mafisa system of managing animals for livestock-owners to gain access to draught power, milk and the occasional calf.[258]

The reocurrence of drought from 1981 until 1986/87 has had a severe impact on cattle numbers. Average mortality rates rose from 13.8% in 1980 to 25% in 1986/87, when the national herd was estimated to have fallen by almost 25%, to 2.3m. The ending of the drought in the 1987/88 rainy season has enabled some rebuilding of stocks, but at the end of 1988 the size of Botswana's herds was still only four-fifths of that in 1981, and it will require at least three years of good rainfall for cattle numbers to recover properly. For the beef industry, the draught caused a decline in both cattle weight and numbers slaughtered. Animals passing through abattoirs of the Botswana Meat Commission (BMC) declined from 239,000 head in 1984 to 220,000 in 1985, and to 196,000 in 1986. The number of slaughtered cattle declined further, to 146,000 head in 1987, and reached its lowest level for 20 years, at fewer than 110,000 head, in 1988, as farmers retained stock for the rebuilding of herds. As a result, the BMC has been able to fulfil, at best only 70% of its EEC quota of 19,100 metric tons since 1985. Nevertheless, Europe remains its single most important market, taking more than 50% of total exports, thereby helping to sustain both export and BMC revenues. In

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spite of depleted cattle numbers, the government has forecast annual growth in the beef industry of about 5% to 1991, owing mainly to the impact of planned further expansion of the cordon system and a number of programmes aimed at improving the herds of small-scale farmers. It is also proceeding with a project, costing P45m, to construct a new abattoir in Francistown, which will complement existing BMC facilities at Lobatse and Maun. Construction, largely funded by the European Development Fund (EDF) and the African Development Bank (ADB), commenced in early 1988, and was due to be completed by mid-1989.[259]

In contrast to cattle, sheep and goat numbers appear to have withstood the drought reasonably well. After an initial decline from an estimated 628,000 head in 1978 to 621,000 in 1981, they were estimated to total more than 1.2m head in 1987. They remain predominantly a subsistence sector resource, and the main commercial development outside beef has been in the poultry sector. By 1980 domestically produced eggs accounted for 80% of urban demand and poultry meat for 20%, and by 1983 imports of both products accounted for only 5% of urban requirements. It is hoped during the 1985-91 Development Plan to improve the availability of eggs and chickens in rural areas, and also to improve local production of milk and fish. At present over 70% of domestic milk requirements have to be imported in the form of milk powder, and it is estimated that fish production is only 15% of the optimal annual catch.[260]

In the arable sector, as in the beef sector, commercial farmers account for a disproportionate amount of output: government figures show that just 100

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commercial farmers produce some 37% of total sorghum, maize, millet, beans and pulses. Of the 85% of small-scale farms producing crops, almost one-third are less than 3 ha, and only 6.8% over the 10 ha minimum necessary for household self-sufficiency, even in years of reasonable rains. As a result, two-thirds of rural households are reported to depend for up to 40% of their income on members employed in the formal, predominantly commercial, agricultural sector.[261]

The level of national self-sufficiency is little better, with domestic grain needs satisfied in only two years since 1975. In recent years only 10%-20% of national demand has been met by domestic production. Total cereal requirements rose from 100,000 tons in 1979 to 190,000 tons in 1985, and are expected to exceed 200,000 tons by 1991. This extremely low level of self-sufficiency reflects the fact that only 5% of Botswana has adequate rainfall for rain-fed farming. Combined with poor soils, yields are therefore low, at under 300 kg per ha on the majority of traditional farms. The six years of drought, which began in 1981, exacerbated the situation. Traditional farm yields averaged under 100 kg per ha in 1983, while total grain production fell from 60,000 tons in 1981 to 9,700 tons in 1984. There was some improvement in 1985 to 17,820 tons, but in spite of improved rainfall in 1986, locust swarms reduced output in that year to only 21,000 tons. In 1987 rains were again inadequate, but government incentives led to a 25% rise in the planted area, to 306,000 ha, enabling output to be increased to 25,000 tons. Output improved further in 1988, with the end of the drought, although excessively heavy rains near the end of the growing season destroyed many crops. The outlook for 1989 was good, as weather conditions were

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favourable during the growing season. The shortfall in requirements has been met by a combination of commercial purchases and food aid, and in 1984 a national drought-relief strategy was introduced to co-ordinate food distribution to those who required additional assistance, then estimated to be some 60% of the population. By 1987 the proportion in need had reached nearly 80%, and in November the government appealed for P7m in aid to supplement its own allocation of P8m.[262]

Despite the return of rains in the 1987/88 and 1988/89 crop seasons, cereal self-sufficiency remains no better than a remote prospect. Even so, the arable sector is the focus of agricultural development under the 1985-91 Development Plan, with the immediate aim of minimizing the detrimental effects of drought on the traditional sector and the longer-term target of raising both household and national food sufficiency levels. The strategy for the former involves the continuation of the relief measures instituted after 1981, notably borehole drilling and distribution of drought-resistant seed varieties. That for the longer-term focuses on expanding the availability of credit, inputs and equipment, including draught power. It also aims to assist small scale producers to extend their farms, on the one hand, and to increase the area under irrigation on the other.[263]

In the mid-1980s land under irrigation totalled only 1,000 ha, the majority consisting of privately owned developments growing primarily cotton, citrus fruits and tobacco. Botswana is considered to have substantial irrigated potential, however, particularly

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in the Okavango Delta and Chobe areas. Given the unique and fragile nature of the Okavango, especially, there are also significant possible environmental risks in realising this potential, which have been the subject of considerable study in recent years. Some pilot plots utilising melapo, or flood recession irrigation, have been started at the Molapo development project on the eastern fringe of the Okavango. Pending the final outcome of environmental studies on the project, it is planned to proceed during the ensuing years with a scheme, costing P180m, to develop 5,000-10,000 ha of high-yielding crops by improving water- and crop-management systems. A study on a similar project on the southern edge of the Okavango, also focusing on possible environmental implications, was completed in 1988, although the results had not been disclosed by June 1989. With a view to expanding irrigation and satisfying rapidly increasing urban demand for water, the government has instigated an 'accelerated water resource development programme'. Studies for irrigation dams on the Lotsame, Mahalapyswe and Motloudse rivers commenced in early 1989, and were due to be completed in early 1990.[264]

1.9.2 MINERALS AND MINING

Mining was practised on a small scale in Botswana from about 1900, but as recently as 1965 a British survey found no indication of profitable large-scale mineral reserves. Following independence, however, the country was discovered to have abundant reserves of diamonds, coal, copper-nickel, soda ash, potash and sodium sulphate. Although substantial deposits of salt and plutonium, as well as smaller reserves of gold, silver and a variety of industrial minerals, have also been

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identified, Botswana's full mineral potential remains unknown. The geology of the eastern area of the country, where most discoveries have been made, is well-mapped. Nevertheless, much works still needs to be done on the geology of western Botswana, where the overlying Kalahari sands make geological exploration very difficult. Mapping of this area is under way with external assistance, and is a priority under the 1985-91 Development Plan. In particular, aeromagnetic surveys in the mid-1970s indicated potential oil- and gas-bearing structures in the Nossop, Ncojane and Passarge sedimentary basins in the west and north-west. A more detailed geophysical survey of the western Kalahari, funded by Canadian aid, was completed in late 1988, and was reported to have had encouraging results. Government approval for the drilling of a test well in the area was expected during 1989, and it was hoped that this would yield results by early 1990.[265]

Large-scale mineral exploitation began in 1971, when the Orapa diamond mine came on stream, and Botswana now has a relatively diverse mining sector, with three major diamond mines, coal and copper-nickel mines, as well as small-scale mining of gold, industrial minerals and semi-precious stones. The diamond mines are owned by Debswana, a joint-venture equally owned by the Botswana government and De Beers Consolidated Mines of South Africa. De Beers began diamond exploration in 1955, but it was not until 1967 that the 112-ha Orapa kimberlite pipe was discovered. This is the world's second largest, after the Williamson pipe in Tanzania. Mining at Orapa was quickly followed by the inauguration of production at the adjacent Letlhakane pipe. Over the years 1971-81, the annual output of diamonds increased by 16%, to 4.96m carats. The main

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expansion of production came in 1982, with the development of the Jwaneng mine, 125 km west of Gaborone. In 1983, its first full year of production, Jwaneng produced 5.85m carats, compared with 4.4m at Orapa and 540,000 at Letlhakane. Annual production increased by 166% during 1981-87, to 13.2m carats, making Botswana the world's third largest producer in volume terms, after Australia and Zaire. Botswana mines a high proportion of gem stones, while Australia and Zaire produce mostly industrial diamonds. The majority of gem stones come from Jwaneng, where output has expanded more rapidly than was initially anticipated, reaching more than 7.2m carats in 1985, compared with an earlier target of 6m carats. Initial estimates of ore reserves at the mine were found to be too conservative, and production was retargeted at a minimum of 7.2m carats annually to 1990. Reserve estimates at Letlhakane have also been revised upwards, while production at Orapa has stabilised at about 4.5m-4.9m carats per year. A total annual production target of about 13m carats, sufficient to maintain Botswana as a leading diamond producer into the 21st century, was set in 1987, based on known reserves. Although continuing exploration has revealed no new deposits, annual production reached a record 15.2m carats in 1988, as the result of a decision to take advantage of favourable world market conditions by mining more high-grade diamonds, especially from Jwaneng. The increased exploitation of high-grade reserves was to continue in 1989, again as a result of high world prices, but was due to return to the previously planned level in 1990. The annual production target of 15m carats will be retained: the shortfall of 2m carats is to be met from a scheme to sift tailings for stones at Jwaneng; work on the construction of a P200m reprocessing plant began in 1989, and it is due to come into operation by mid-1990, producing mainly small diamonds.[266]

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The expansion of production, and the government's right to some 70% of Debswana's profits under its agreement with De Beers, largely protected Botswana against the low level of international diamond prices during the early 1980s. With the recovery of prices after mid-1985, the industry further strengthened its role as the mainstay of Botswana's strong economic position. In 1986 export earnings from diamonds, which amounted to P1,103m (compared with P956m in 1985), contributed substantially to the P566m overall surplus on the balance of payments, and to the P502m trade surplus for the year, and underpinned the 14% growth in GDP. In 1987 earnings from the export of diamonds more than doubled, to P2,253m, helping to increase the balance-of-payments surplus to a record P950m, and GDP growth to an estimated 14.7%. The surge in earnings was mainly attributable to a 10% increase in the diamond price in October, and to the sale by Debswana of its stockpile to De Beers in July. The sale, valued at some $600m, formed part of an agreement giving Debswana a 5.27% shareholding in De Beers. For the government, this meant an effective 2.6% stake, entitling it to appoint two directors both to the main De Beers board and to that of its London-based Diamond Trading Co subsidiary. The directors, who were to be the first black members of the De Beers board, were appointed in October 1988. De Beers' unprecedented agreement to allow an external shareholder to participate was mainly a reflection of Botswana's increasing importance in production by the group. In 1987 Debswana accounted for 58% of total output by the De Beers group, compared with 55% in 1986. For the government, the agreement was not only a long-term investment in a company with net profits of R1,501m in 1987, but also a means of gaining access to decision-making on the diamond market. In 1988 export earnings from diamonds amounted to P1,963m, less than in 1987. However, if the distorting effect of the sale of the Debswana stockpile in 1987 is removed, earnings from the export of diamonds increased by 47% in 1988.[267]

Production of copper-nickel matte at Selebi-Phikwe began in 1974, and output has steadily risen, reaching a peak of 50,171 metric tons in 1983/84. However, the value of sales of matte per ton declined consistently, from P1,859 in 1979 to P1,394 in 1984, owing to depressed international prices for nickel and copper. This created profound financial problems for the operating company, BCL, and the shareholders in its parent group, Botswana Roan Selection Trust (Botrest), in which the Botswana Government holds 15%, with Anglo American Corporation of South Africa and Amax Corporation of the USA holding the remainder. To offset these problems, BCL's finances were restructured four times between 1979 and mid-1985. Although BCL returned to operational profitability in 1984, when a surplus of P424,000 was achieved, accumulated losses continued to rise. These losses increased from P604m in 1984 to P992m in 1985, when operating profits totalled P45.7m (mainly as a result of a renegotiation of BCL's sales agreements). In 1986, when operating profits declined to P18.2m (owing to adverse currency movements), accumulated losses exceeded P1,100m, and it was decided to seek a further restructuring of BCL's finances. However, the resurgence of prices for base metals after mid-1987 led to a considerable improvement in BCL's financial position. In 1988 earnings from exports of copper-nickel matte increased by almost 230% to P421m, while profits advanced to P250m from P20m in 1987. As a result, BCL was able to repay P180m in debts and P60m in emergency funding to major creditors, and the proposed fifth restructuring of the company's finances was deferred. BCL was expected to reduce its

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debts further in 1989, as continuing high metal prices were envisaged. The improvement in BCL's condition has been advantageous to the economy as a whole: the company is the country's largest private-sector employer, with a work-force of 4,000, and an important source of foreign exchange, accounting for about 10% of Botswana's total export earnings. The improvement in prices also enabled two new copper-nickel mines to be brought into production. In July 1988 BCL announced plans to bring the high-grade Selebi North mine into production, to replace deteriorating ore bodies at its other two mines. Work on the project started in early 1989, and production was expected to begin by the end of the year. The mine was expected to reach full capacity of about 1,500 tons of ore per day by mid-1990. The other copper-nickel mine (at Selkirk, east of Francistown) was brought into production at the end of 1988 by a consortium of Swiss and British investors. At full capacity, output is expected to reach 60,000 tons of high grade ore per year; BCL is to undertake refining of the output on a toll basis. There are plans to develop the adjacent, and larger, Phoenix deposit.

Plans to exploit Botswana's coal reserves have been restricted by the low level of international prices. Some 17,000m tons of steam coal suitable for power-plant use have been identified in the east, and production for domestic use at the Moropule mine averaged 385,000 tons per year during 1979-84. Output increased to 499,400 tons in 1986, to satisfy increased demand from Botswana Power Corporation, but major exploitation of the reserves depends on the development of export markets. There were hopes of achieving this in the late 1970s, and in 1982 a preliminary agreement was signed with Shell Coal for developing a mine at Kgaswe, near Serowe. Studies showed the project to be technically feasible, but economically unviable because of the fall in world prices during the period, and

Shell withdrew from the project in early 1985. Other companies have considered export development, but the outlook for world prices suggests that any exploitation would be unlikely until after 1990. Another long-term possibility is the production of oil from coal, but the government wants first to complete the present studies into Botswana's potential for producing petroleum and natural gas. In the mean time, with donor support, it is concentrating on expanding domestic coal use.[268]

The exploitation of brine deposits at Sua Pan, in central Botswana, has also proved difficult. Of the numerous attempts to set up a soda ash/salt plant since independence, the BP subsidiary Soda Ash Botswana had, by 1984, made most progress: a pilot project had proved the technical feasibility of a $75m scheme to build a plant at Makgadikgadi, to produce 30,000 tons per year of soda ash for export to glass-, paper- and steel-making industries in the region, and especially in South Africa. The pilot studies, however, also showed that, in view of the potential for the 'dumping' of soda ash (particularly by US exporters), the scheme would be economically viable only if South Africa would agree to some protection under the Southern African Customs Union (SACU) arrangements. When negotiations began in 1984, however, South Africa linked agreement on SACU protection to a non-aggression pact, a demand which was unacceptable to the Botswana government, and the project was apparently suspended until 1986, when the prospect of US sanctions appeared to make the South African government more amenable. In December 1986 African Explosives and Chemicals Industries (AECI) of South Africa began talks with BP to acquire its interest in Soda Ash Botswana, with the government taking a 48% share in the project, which was now

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envisaged on a much larger scale, with annual output of some 300,000 tons of soda ash and 650,000 tons of salt. Costs had increased proportionately, and were estimated at 920m South African rand in November 1988, when AECI and the government signed an agreement to undertake the project. AECI, with a 26.5% holding in Soda Ash Botswana, is the leading member of a consortium that will take a 52% share of the operating company; the other members of the consortium, Anglo American Corporation of South Africa (which owns 38% of AECI) and De Beers, will have a joint 25.5% stake. The Commonwealth Development Corporation (CDC), the International Finance Corporation and Zimbabwean interests from both the private and public sectors were expected to be represented in the Botswana government's 48% share of Soda Ash Botswana. Work on the project commenced at the end of 1988, and was scheduled to be completed by March 1991.[269]

Botswana's dependence on South African support to implement the soda ash project has raised domestic and regional concern that the government is increasing the country's vulnerability to political pressure, particularly with regard to the breaking of economic sanctions. Similar concerns have surrounded exploration work on plutonium deposits being carried out in the south by two South African firms, Gold Fields of South Africa (GFSA) and Southern Prospecting. GFSA holds three prospecting licences, through its Gold Fields of Botswana subsidiary, for a 3,000 sq km concession north of the Molopo river and adjacent to its new concession in South Africa's Bushveld igneous complex, which contains 75% of the world's known platinum and 80% of known chrome reserves. Although Botswana's reserves are thought to be of lower grade

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and far less substantial, GFSA was reported, in early 1987, to be considering construction of a refinery in the country for processing of output for export, from its local as well as South African concessions. Southern Prospecting has two licences for a 1,900 sq km concession, and has formed a new locally-incorporated subsidiary.[270]

In 1987 a joint venture, Shashe Mines was formed between the government, a Canadian company and a US company, to conduct exploration work on gold deposits at Map Nora, near Francistown, and exploitation of the mineral, with a projected value of P13m in the first year of production, was due to begin in 1989.[271]

1.9.3 MANUFACTURING

Although manufacturing contributes only about 7% of GDP, it has emerged since the late 1970s as one of Botswana's most dynamic economic sectors, despite the constraints of a small domestic market, limited export outlets, weak infrastructure, import dependence and shortage of skilled manpower. The number of companies in the manufacturing sector rose from 88 in 1979 to 276 in 1984, representing an investment of over P115.3m. Manufacturing employment grew from 4,625 to just under 11,000, or, at an annual average rate of 18.7%, more than twice the target rate for the period. By the end of 1987 it had exceeded 13,000. This expansion did much to reduce the parastatal BMC's domination of the sector, with its share of industrial employment declining from 36% to 18% over the period 1979-84. It also represented a considerable diversification of Botswana's manufacturing base, with textiles,

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beverages, chemicals, paper, metal, plastics and electrical products showing the largest rates of expansion. The sector's strong performance was due to a number of government policies, based on a financial assistance programme (FAP), inaugurated in 1982, which provides a wide range of subsidies to potential entrepreneurs, particularly in the small-scale sector, and a highly attractive foreign investment code.[272]

The parastatal Botswana Development Corporation (BDC) has been a major promoter of industrial development, identifying projects and potential joint-venture partners, and establishing industrial sites for smaller firms to rent. The value of BDC's investment holdings grew from P11m in 1979 to almost P25m at the end of 1984, with its interests including brewing, sugar packaging, furniture and clothing manufacturing, tourism, milling and concrete products. In 1984 BDC established the Setshaba Investment Trust Co as a vehicle for offering shares in its subsidiaries to the public. The revenue from the sale of shares has been used to promote further industrial and commercial ventures. The BDC investment portfolio had risen to almost P49m by mid-1987, and increased by a further P33m in 1988/89. By 1991 it is targeted to reach P110m., with projects including a new international hotel in Gaborone, improved reservation and maintenance facilities for Air Botswana, and development of a financial market system centred on the Setshaba Investment Trust and Tswelelo, a joint venture between BDC and the National Development Bank to provide financial and management services to small businesses. The government is projecting that the sector will expand by around 8.3% per year up to 1990, with BMC expanding at just below this rate, and the balance of

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the manufacturing sector growing by 10%. This growth will be based on an intensification of policies aimed at encouraging local entrepreneurs as well as foreign investment, reinforced by further infrastructural development. A crucial element has been the development of new industrial interests in Gaborone, Francistown and Selebi-Phikwe. Since 1986, Botswana's strong foreign exchange position has proved an increasing attraction for foreign companies, notably those from Zimbabwe and South Africa. The increasing interest of South Africa, which already dominates foreign investment, has created some concern because of the political implications. This situation is, however, being alleviated, to some extent, by the country's greater success in attracting other international investment interest. The UK's Lonrho and Metal Box, and Heinz and Colgate Palmolive of the USA, have made investments since the beginning of 1988.[273]

1.9.4 ENERGY AND WATER DEVELOPMENT

Rapid economic and population growth, particularly over the past decade, has been paralleled by a rapid expansion in demand for energy and water. Energy demand rose by 68% between 1978/79 and 1984/85, and although the period saw major investment in electricity capacity, some 50% of energy demand is still met by fuelwood, posing potentially serious environmental problems. Domestic electricity supply capacity rose from under 30GWh in the early 1970s to over 550 GWh in 1984/85, while sales increased from 173 GWh to 612 GWh; the difference was provided by purchases from South Africa. The principal consumers of energy are urban areas, including industrial consumers, and the mines; since the late 1970s the main aim of investment by

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Botswana Power Corporation (BPC) has been to fulfil their requirements. The largest scheme, and one of the largest projects ever undertaken in Botswana, has been the Moropule power station. Using coal mined at Moropule, the station is the focus of a new national grid system linking the existing northern and southern networks based on Selebi-Phikwe and Gaborone power stations. The first P250m phase of the power station, comprising three 30 MW units, was commissioned at the beginning of May 1987, and work on a fourth 30 MW unit was completed in 1989. Units five and six are planned for the early 1990s, and up to 14 units could be operational by the year 2000, if demand grows as predicted. Work at Moropule has been paralleled by smaller-scale upgrading work at Gaborone and Selebi-Phikwe, and by incorporation of 15 of the largest villages into the new grid system, enabling a number of diesel power stations to be closed. BPC now estimates that supplies are sufficient to satisfy demand until the early 1990s, permitting Botswana to dispense with the 30 MW per year that it has been importing from South Africa. Up to 10 MW per year will continue to be imported, however, to cover demand surges and to ensure alternative sources in the event of problems at Moropule. In accordance with this objective, work is nearing completion on a project to link northern Botswana, at Kasane, into the Zambian grid. Another project began in late 1987 to link Selebi-Phikwe into the Zimbabwean-Zambian grids at Bulawayo. Apart from the further work at Moropule, the main short-term focus of the electricity programme will be the extension of the rural catchment area of the national grid, with the aim of conserving fuelwood and reducing oil demand. Although oil imports have not caused such a burden on foreign exchange as in many other African countries, their share of total import costs has risen from just under 9% in 1979 to almost 15%, owing partly to the expansion of the mining industry, which is the major consumer. The government has maintained a high retail price policy for petroleum products with the aim of encouraging efficient use, and has also begun to build up a three month strategic stockpile in recognition of the vulnerability of its supply route through South Africa.[274]

Botswana's enormous coal reserves and the substantial surplus power generated in neighbouring countries has made it relatively easy to satisfy the rising energy demand, when compared with the problem of the increasing domestic requirements for water. The country has minimal surface water supplies outside the remote Okavango and Chobe areas, and 80% of national demand is currently being met from ground-water sources, with livestock the largest single user, consuming 35.6%, followed by mining (12.6%), urban areas (11.6%) and rural areas and villages (5.1%). Although not fully assessed, groundwater supplies are not expected to exceed 4,000m.cu m per year, and already real competition for water is emerging in the main urban-mining areas in the east, leading to the postponement of plans for the development of industrial sites, particularly in Gaborone. The situation was exacerbated by the drought, which forced not only a doubling of funding for water supply development after 1981, but also a reassessment of priorities. Expansion of supplies to the Gaborone-Lobatse area was a major priority, with the third water project, to raise the Gaborone dam by 8m, brought forward by two years to meet an escalation in demand of 23% per year. The project was completed in 1984, giving Gaborone access in theory to 30,000 cu m of water per day. However, the newly expanded dam did not fill until the return of rains in 1987, necessitating the development of additional borehole supplies at the adjacent Ramotswa

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well field. By early 1991 it is planned to raise the supplies of water to the Gaborone dam by 50%, to some 42,000 cu m per day, through construction of a dam at Bokaa, on the Metsemotlahaba river, and a 34-km transfer tunnel between the two dams. Work on the P50m project began in early 1989; the additional capacity is being financed by the EDF, the CDC, the ADB and Gaborone's Water Utilities Corporation (WUC). The WUC has also partly funded a P10m project to bring water from the Molatedi dam on the Mareko tributary of the Limpopo river, in the South African 'homeland' of Bophuthatswana. Botswana has rights to a proportion of the water obtained from Molatedi. The project, due for completion in early 1990, will provide about 6.3m cu m per year, and is aimed at meeting an anticipated shortfall in the capital's water supplies before the Bokaa scheme is completed. However, the two projects are expected to satisfy Gaborone's requirements only until 1995, and, with urban and agricultural demand expanding rapidly in the south-east of the country, the government has instigated an accelerated water development programme. Studies on four potential dam sites in the north and east are to be completed by early 1990, and the results will be incorporated into a national master plan for water development, which was due to start in 1989. Of the four proposed dams, the Lower Shashe would be the next major urban water resource for the south-east, while the Motloudse dam, provisionally located near Selebi-Phikwe, would be primarily an irrigation source which could additionally be incorporated into regional plans for urban water development.[275]

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1.9.5 FOREIGN TRADE AND BALANCE OF PAYMENTS

Diamonds have been Botswana's principal export (accounting for up to 80% of total earnings) since the mid-1970s, when they replaced beef, which, from being the country's sole export at independence, normally accounts for about 10% of export earnings. Other exports are copper-nickel matte and textiles, at around 7.5% and 3% respectively of total earnings. In contrast to the shift in export composition, the structure of imports has remained relatively constant, covering almost the entire range of consumer and capital goods. Food and beverages are the most important category, at almost 17% of the total, followed by machinery and electrical equipment, with more than 16%, and vehicles and transport equipment with around 16%. Botswana's principal trading partners have also remained unchanged, with Europe providing the largest export market, and South Africa the main source of imports, each with about 80% of the total. The high levels of imports of capital inputs and finished goods, combined with a deterioration in Botswana's overall terms of trade, made a deficit on the merchandise trade account a persistent feature until recently. Taking 1977=100, the terms of trade index declined from 90.3 in 1978 to 62.5 in 1985. The visible deficit reached a record P239m in 1981, but thereafter the situation began to change, particularly as a result of the rapid expansion of diamond exports after 1982. Botswana's first merchandise trade surplus of P27m, was recorded in 1983. With the recovery of world diamond prices in 1985, the surplus rapidly escalated, reaching P459m in 1986. In 1987 it surged by almost 170%, to P1,230.5m, reflecting the effect of the sale of Debswana's diamond stockpile to De Beers in July. In 1988 the surplus declined to P1,088m, but, with the distorting effect of the stockpile sale removed, the trend is still one of steady improvement.[276]

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Botswana operates an open economy, with combined import and export values exceeding GDP, making both the domestic economy and external account vulnerable to fluctuations in the terms of trade and exchange rates. The latter, particularly the movement between Botswana's key trading currencies, the US dollar for exports and South African rand for imports, have proved extremely volatile since 1979. To counter this, the government has operated a flexible, trade-orientated exchange rate policy since the pula was established in 1976 as the national currency. It was initially tied to the US dollar exchange rates, but the appreciation of the South African rand against the dollar forced several revaluations in the following four years, in order to contain import costs and domestic inflation. In June 1980 the pula was linked to a trade-weighted 'basket' of currencies, in order to minimise such disruptions. However, after 1982 the relationship between the US dollar and the South African rand began to reverse; this trend gained strength as the political situation in South Africa deteriorated. The pula also began to strengthen against the rand as domestic inflation fell from 12.7% in 1982 to 5.5%, well below the South African rate, at the end of 1984. The result was a series of trade-orientated devaluations, with a 10% cut in 1982 followed by a 5.07% devaluation in 1984, and two devaluations in 1985, one of 15% in January and another of 3% in August. Domestic inflation rose to 10% in 1985, and according to official figures, has since steadily increased, reaching 12% at the end of February 1989; however, unofficial estimates indicated that it had exceeded 30%.[277]

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Apart from maintaining trade competitiveness, the exchange rate adjustments have also ameliorated the effect on the balance of payments of the steady deterioration in the country's terms of trade. Since 1976 Botswana has generally enjoyed a secure balance-of-payments position, with the current account in surplus for seven of the 10 years since 1979 and these surpluses advancing steadily in every year but 1981. Net transfers, including SACU revenue, and capital inflows, including both private investment and foreign aid, more than offset the continuing deficit on both the invisible and overall trade account after 1982. In 1981 there was a massive deterioration in the visible trade deficit from P45m in 1980 to P239m, through a fall in revenue from diamonds and a substantial increase in import costs and volume, financed by heavy commercial bank borrowings by traders. The government responded in 1982 with a deflationary budget, a 'freeze' on wages, a rise in interest rates, a 'squeeze' on commercial bank lending to curtail domestic demand, and a currency devaluation to reduce the burden of imports on the external account. These measures proved effective, with the overall account subsequently returning to a P57m surplus, and the visible deficit almost halved to P122m. Since then, a healthy balance of payments position has been assured by the expansion of export earnings, particularly from diamonds, which, apart from pushing the trade account into surplus, has underpinned a rapid growth in the overall surplus. This reached P501m in 1985 and P566m in 1986. In 1987 the surplus increased to P942m, a record caused by the sale of the Debswana stockpile. The surplus fell to P692m in 1988.[278]

The most obvious effect of Botswana's strong balance-of-payments position has been the growth of foreign

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exchange reserves. These were sufficient to cover 5.5 months of imports in 1980 and to cover 9.2 months of imports in mid-1985. By mid-1986 they totalled P1,644.9m, sufficient for 17.3 months' cover, and had exceeded 31 months' cover at the end of 1988, at almost P4,000m. The government views the high reserve level as essential to sustain Botswana's future economic development as diamond earnings level out, with no single source of export revenue to replace them. The rapid escalation in reserves after 1985 was paralleled, however, by growing criticism of the Botswana government's concern with long-term financial security. According to the critics, the government's conservative fiscal policies were depressing productive investment, particularly by the private sector, and were subsequently hindering job-creation. Of particular concern was the government's insistence on maintaining relatively high interest rates, and the resulting massive surplus liquidity in the banking sector. Credit demand for capital projects was so low by 1986 that commercial banks began to refuse large deposits, forcing the central bank to act as a deposit-taker of last resort. In response to growing pressure, the central bank was permitted to reduce its prime lending rate to 10% in September 1986, and again, to 8.5% in January 1988. In addition, with the growing demand for more active encouragement of investment following the unexpected earnings caused by the De Beers sale, a greater liberalization of exchange controls was announced in early 1988. Apart from relaxing controls on the remittance of company and individual funds, the changes also allowed the insurance and corporate sectors to invest overseas, on condition that the investment resulted in the creation of new employment at home, or in the expansion of Botswana's export market. These changes, supported by the recent boom in mining and increased government capital expenditure, have helped to alleviate the problem of too much money chasing too little investment. Surplus liquidity in the banking sector declined from nearly P160m at the end of 1987 to P93m at the end of 1988. Bank lending rose by nearly 30% during 1988.[279]

Botswana's balance-of-payments situation has also been helped by its low debt burden. The external public debt, which stood at P329m in mid-1986, has been projected to reach P392m in 1991. Debt-servicing costs totalled just 5% of export earnings in 1985, and had declined to less than 3% of export earnings by early 1989, reflecting the recent surpluses on the trade account.[280]

1.9.6 GOVERNMENT FINANCE

At independence about one-half of Botswana's public expenditure was financed directly by the government of the United Kingdom. This extreme level of reliance on external support was altered by Botswana's accession to SACU in 1969 and the country had become financially independent of the UK by 1972/73. From 1977/78 until 1982/83 customs revenue constituted the principle component of government income, but since then this source has been overtaken by mineral revenue, which now accounts for about 58% of the total, compared with 17% for customs revenue. Since the unexpected fall in diamond revenues in 1981/82 (which forced a heavily deflationary budget in the following year), the government has adopted a cautious approach to expenditure, which has been reflected in a steady rise in the budget surplus. This increased from P68.5m in 1983/84 to P413m in 1986/87. In 1987/88 when expenditure was projected to expand by 9%, in real terms, to P1,081m, the surplus was initially expected

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to fall to P347.1m. The actual out-turn, however, was a surplus of about P377m as a result of the higher-than-expected mineral earnings, which boosted budget revenue by 18% over projections, to P1,649m. The extra money generated by the sale of the Debswana stockpile finally led the government, in December 1987, to respond to pressure for a more positively expansionary approach, based on greater public spending. Additional recurrent expenditure of P109m was approved for the budget year, and development spending was to increase by P650m for the last three years of the development plan, ending in 1991. As a result, total expenditure for 1987/88 reached P1,317m. Nevertheless, the government opted for a cautious budget for 1988/89, warning that a stabilization of revenues from the diamond industry would quickly lead to the return of an overall deficit. Once again, however, revenues exceeded expectations, as a result of high diamond earnings and the buoyant market for base metals. Actual revenue, at P2,223m, was 25% ahead of the budget projection of P1,777m. Expenditure, at P1,922m, was also ahead of the projected P1,497m, leaving a budgetary surplus of P301m. The proposed 1989/90 budget was again conservative, the government justifying potentially unpopular measures on the grounds that export earnings were unlikely to show any further dramatic or unexpected increases. Revenue, at P2,237m, and total expenditure, at P1,955m, were projected to be only slightly higher than the 1988/89 actual figures, producing a surplus of P282m. Planned recurrent spending, however, has been allowed to rise by 20% over 1988/89 actual figures, to P1,033m, attributable largely to a 10% rise in public-sector wages from April 1989. To compensate, development spending has been reduced to P838m, from P933m in 1988/89.[281]

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1.9.7 EMPLOYMENT AND WAGES

Botswana's population growth rate has accelerated significantly since 1981, from 3.1% per year to 3.7% in 1986/87. As a result, the total population increased from 941,027 at the census of August 1981 to an estimated 1,211,816 at mid-1988. Current projections indicate a total of 1,600,200 in 1996. As a result of the high growth rate, the net addition to the labour force of people aged 15-64 years has been in the region of 20,000 per year, many of them joining the 53% of the working-age population who were estimated in 1985/86 to be unemployed or in school. Only around 20% of the labour force are employed in the formal sector, with another 9.1% self-employed. The strong economic growth rates since 1979 have led to a significant expansion in job creation, with formal-sector employment rising from 65,500 in 1978 to 100,600 in 1983, and to 150,000 in 1988, amounting to an annual average growth rate of more than 10%. The main sectors in which employment has increased are manufacturing, finance and business services, transport and communications and social services. Until the beginning of 1988, government employment grew relatively slowly, but subsequently it expanded significantly. Construction employment, which performed weakly until 1983, has since grown impressively, as a result of increased government expenditure and a recent rapid rise in commercial and residential building developments. Despite the rate of economic growth exceeding that of population growth, formal-sector employment in terms of absolute numbers has not been able to absorb the increase in the labour force. This situation has been exacerbated by a decline in the number of Batswana working abroad from 20,800 in 1978 to 18,800 in 1983, or from 8.3% to 6.6% of the working-age population.[282]

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With almost half the population aged under 15 years, job creation has become a major political issue and the main priority in government planning with the 1985-91 Development Plan focusing principally on the expansion of employment opportunities in manufacturing, agriculture and trade. The aim is to increase the percentage of the labour force with job opportunities to 36.1% in 1990/91 from 32.5% in 1985/86. The number of working-age people still in education is expected to rise from 7.5% to 9.6% during the period, but even so, the absolute number of people without job or educational opportunities is expected to rise from 303,600 on 1985/86 to 338,000 in 1990/91. The projected rise of those still in education reflects the government's parallel priority to increase the country's pool of trained labour. A prices and incomes policy, aimed at ensuring that basic local wage and salary levels in the private sector do not exceed those received by comparable grades of government employees, is enforced by a National Employment, Manpower and Incomes Commission.[283]

1.9.8 INDUSTRIAL DEVELOPMENT

The Government of Botswana enunciated the following objectives for industrial development during the NDP VI period:

- the encouragement of a healthy private sector and free enterprise system by creating a favourable business environment;

- the diversification of the economy through accelerated growth in manufacture and trade;

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the stimulation of export activities and the encouragement of increased processing and value-added in import substitutions;

the provision of more productive job opportunities for citizens, particularly in rural areas;

the encouragement and support of opportunities for citizens in the management and ownership of business;

the protection of the interests of consumers and workers.[284]

The government is committed to the aggressive creation of new job opportunities for its ever increasing labour force. This will be achieved through the encouragement of labour-intensive, import-substitution and export-orientated industries.

Examples of import-substitution industries are processed foods, soft drinks and beer, clothing and textiles, building materials and fabrications. Duty-free access to the larger southern African market provides attractive opportunities for local and foreign investors manufacturing items such as candles, pharmaceuticals, chemical and toilet products (for example, soap), plastic goods and clothing.

There are many opportunities arising from the raw materials that are available in Botswana. The most obvious is the manufacture of leather and related products, including boots and shoes. A further opportunity for industrial expansion based on local

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products is the game-skins, trophies, and curio industry. The timber resources of the indigenous forests and, more especially the products of the mill at Kasane, are open for development.[285]

Good long-term possibilities for industrial development include the production of ceramics and facing bricks from local clays, the processing of fish and manufacture of fish-meal from the Okavango area, and the production of paper products. Finally, with the development of the mining sector of Botswana it is possible that many related industries could be successfully established.[286]

Botswana can offer considerable advantages to the industrialist. The country has an ample supply of unskilled labour. As a signatory to the Lome Convention, Botswana has duty-free access to the European Economic Community (EEC) and, as one of the independent Black African states, ready access to the rest of Africa, and particularly to the eight other countries of the Southern African Development Co-ordination Conference.[287]

Botswana, together with Lesotho, South Africa and Swaziland, is a member of the Southern African Customs Union, which provides for a free and virtually unimpeded exchange of goods between the member states. Membership of the customs union has, however, hampered industrial development because of Botswana's openness to South African exports. Other factors restricting industrial progress are the small size of the local domestic market, the shortage of manpower with the

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required managerial and technical skills, and the limited availability and high cost of water and electricity. Serviced urban land is also expensive.[288]

In many ways industrial development is still in its infancy, but there has been remarkable growth over the last eight years.

Most industries are located in the four major towns of Francistown, Gaborone, Lobatse and Selebi-Phikwe. Francistown has two light industrial estates and a third is under consideration. An advanced industrial area, some 65 hectares in extent, has been established at Gaborone West. Primary infrastructure has been installed. Rail siding facilities are to be available and a goods marshalling yard designed to handle containers will be incorporated in the area. There are a small number of industries at Lobatse, where it is intended to establish an industrial estate; while Selebi-Phikwe has one area devoted to industry.[289]

To create economic opportunities for Batswana and to encourage citizen participation in commercial, manufacturing, construction and service activities, the government has reserved certain activities for citizens and wholly-citizen-owned firms. No new applications from non-citizens or by firms with no citizen involvement will be considered. Existing businesses will, however, be permitted to continue operations.[290]

New licences for the following commercial and industrial activities are reserved for citizens and wholly-citizen-owned firms:

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commercial activities	hawking and vending butcheries and fresh produce dealers dairies small general traders petrol filling stations bottle stores bars (other than hotel establishments) taxi services security guard services chibuku bars village-type restaurants/takeaways general traders (excluding chain store and franchise operations) simple speciality operations e.g. clothing boutiques
industrial activities	school furniture manufacturers manufacturers of uniforms overalls, dust coats ordinary cement and baked brick producers sorghum millers bakers of ordinary bread burglar bar manufacturers

The Ministry of Commerce and Industry, together with the local licensing authorities must apply their administrative judgement in the promotion of joint ventures. Non-citizen participation in chain store and franchising operations will be permitted on a case-by-case basis.[291]

The Reserved Activities Regulations also apply to the undermentioned roads and railways maintenance contracts:

fencing
road maintenance
drainage

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culvert construction
transport and plant hire
clearing and scrubbing bush
stock piling of materials
carting gravel and chippings
bridge painting
road markings, fog spraying and
re-surfacing bitumen roads

The Reserved Activities Programme is to be regularly reviewed and new proposals for reserving further activities will be referred to the ad hoc committee from time to time.[292]

The Ministry of Commerce and Industry has established a Trade and Investment Promotion Agency (TIPA) whose objectives are:

to simplify procedures for the establishment and operation of business in Botswana;

to actively encourage the localisation of jobs to ensure that Batswana become more involved in industry and commerce;

to promote the growth of employment opportunities by encouraging labour-intensive production methods;

to ensure the maximum diversity of commercial and industrial enterprises from the point of view of product and geographical location;

to aggressively promote Botswana and its products.

These objectives will be achieved by the TIPA providing the following facilities:

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advisory, consultancy and liaison services;

a trade and industrial information service, organising trade fairs and exhibitions such as the annual Gaborone International Fair, and assisting trade and investment promotion missions;

public relations exercises - for example, the production of the quarterly publication Botswana Business News, and the wide range of other specialist trade and investment literature issued by the ministry.

The overall objective of the TIPA, then, is to co-ordinate the promotional activities of the Ministry of Commerce and Industry in the stimulation and development of commercial and industrial activities throughout Botswana.[293]

The promotion of industrial development is also undertaken by two other agencies, Botswana Development Corporation Limited (BDC) and Integrated Field Services. The Ministry of Commerce and Industry also assists in matters relating to industrial development. BDC is the primary development and investment agency with a wide range of activities covering agro-industry, commerce and industry, property management and development, financial services, hotels, tourism and transport.[294]

In its promotion campaigns BDC stresses that membership of the customs union not only offers duty free access to the wider southern African market, but also the possibility of protection for infant industries,

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through the raising of special tariffs on all imports of a particular product. Further, in the case of an industry established in Botswana and capable of supplying 60 per cent of the entire requirements of the customs union area, such an industry can be granted "specified" status - i.e. special duties against imports into the whole of the customs union area can be arranged to provide the industry with protection against imports from overseas. The trade agreement between Botswana, Malawi and Zimbabwe provides for the transfer of goods locally grown or manufactured free of duty and without restriction between the three countries. Zimbabwe currently requires an open general import licence.[295]

Botswana Development Corporation was established in 1970 for the purpose of identifying business opportunities, undertaking any related feasibility studies and interesting potential investors in specific projects. The corporation participates in promising new ventures in partnership with local as well as foreign capital. Such participation may take the form of any or a combination of the following:

financing with share capital
loan finance
loan guarantees
provision of industrial buildings.

The BDC group consisted of 31 subsidiaries and 17 associated companies as at 30th June, 1986. Assistance in the way of loans was provided to another 19 companies. A further nine companies and organisations received grants totalling P122 303,00 under the BDC's subcommercial fund for activities having an economic

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295 IBID, P66

benefit to the country. Total capital employed increased from P72,0 million to P87,0 million in 1986, an increase of 21 per cent over the previous year, while turnover was up to 33 per cent from P90,5 million to P120,3 million. Before profit tax increased from P5,4 million to P108,0 million and after tax profits were P79,0 million as against P36,0 million in 1985.[296]

The corporation operates the following divisions:

agricultural	irrigation schemes, dairying and livestock (beef)
commercial and industrial	retail, manufacturing and wholesale services
financial services	hire purchase, leasing, insurance broking and underwriting
property management and development	industrial, commercial and residential property
tourism, hotels and transport	hotels, game lodges, car hire, air passenger and freight transport services

The corporation is giving top priority to the establishment of new ventures in the commercial and industrial fields.[297]

The corporation normally finances projects where its total investment is at least P100 000. Its maximum involvement is generally P6 million in share capital or P10 million in total in any one project. In the case of share capital BDC prefers to have a minority shareholding but in excess of 15 per cent. In considering project financing the corporation would not normally finance more than 50 per cent of the total costs;

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297 IBID, P66

though in respect of projects where the costs are less than P500 000 consideration would be given to financing up to 75 per cent thereof. In all cases the corporation would like management to finance at least 25 per cent of total project cost.[298]

The Botswana Enterprises Development Programme aims at providing technical assistance for the development of enterprises owned and managed by local entrepreneurs, to enable citizens to play a greater part in commercial and industrial development. The practical implications of this programme are worked out by the Botswana Enterprises Development Unit now known as Integrated Field Services (IFS), which has already assisted in the development of indigenous enterprises, mainly in construction, furniture and textile manufacturing and metal work, in urban areas.[299]

IFS has promoted a wide range of small scale industries, including metal and wood working, garments, leather goods, pottery and construction.

IFS has now undertaken a major shift in its overall policy away from the concept of industrial estates in favour of rural industrialisation. This involves the promotion of cottage industries and liaison with rural industrial officers of the Ministry of Commerce and Industry. Extension services are being established throughout the country and selected entrepreneurs are being given basic training in the urban estates. These trainees will then be located in rural areas as soon as the necessary facilities become available. Active encouragement is being given to the development of rural infrastructure.[300]

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298 IBID, P66

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The Ministry of Commerce and Industry also assists private entrepreneurs in identifying suitable and professional projects in the industrial sector. It helps with specialised investigations such as market and sectoral surveys and renders general assistance in setting up an industry in Botswana.[301]

1.9.8.1 INVESTMENT INCENTIVES

The Government of Botswana is very conscious of the constraints placed upon industrial development and foreign investment. These constraints may be grouped as follows:

small local market;
high cost of services;
taxation;
land and housing expenses;
shortage of skilled manpower.

The situation is further complicated by the competition provided by the Republic of South Africa and its homelands. Moreover, independent Zimbabwe now provides an alternative base from which to conduct business operations geared for exporting to the rest of Africa and even South Africa.[302]

The government's commitment to the creation of productive employment was given further practical form with the launching of a package of financial incentives in May, 1982. Known as the Financial Assistance Policy (FAP), the package is designed to use the country's abundant labour resource for the expansion of economic

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301 IBID, P66

302 IBID, P67

activities. This will be achieved through the provision of financial assistance to productive businesses i.e. business activities which produce or process goods for export or import substitution. The cattle industry and its products together with large scale mining are excluded. This effectively limits the activities eligible for assistance to manufacturing, small and medium scale mining and agriculture other than cattle.[303]

One other type of industry is eligible for assistance. This is termed a "linking" industry which refers to those industries which provide a marketing or collecting function for the productive sectors. Repair and maintenance facilities would also qualify under this section. Service industries (e.g. internal transport, retailers, construction, banking, tourism and entertainment) do not qualify, neither do brewing and distilling.

New ventures and existing productive businesses which qualify for assistance have been categorised into three groups. These are:

1. small scale projects - a fixed capital investment of less than P20 000.

2. medium scale projects - a fixed capital investment of between P20 000 and P900 000.

3. large scale projects - a fixed capital investment in excess of P900 000.

Group 1 is restricted to citizens only. Depending on the nature of the project, applications for assistance

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in Group 2 are handled by the Ministries of Agriculture, Mineral Resources and Water Affairs, and Commerce and Industry. Large scale projects should be referred to the Ministry of Finance and Development Planning. Applicants can only make one application every twelve months.[304]

Two packages of financial assistance are offered for medium scale projects:

the Automatic Financial Assistance (AFA) scheme is awarded only to new manufacturing ventures.

the Case-by-Case Financial Assistance (CFA) scheme applies to expansions of existing productive activities and also to new ventures.[305]

The following automatic grants are available to eligible manufacturing industries under the AFA scheme:

1. Five year tax holiday allowing for reimbursement to a business of its income tax liability on the following basis:

   100% business tax reimbursement for years 1 and 2;
   75% business tax reimbursement for year 3;
   50% business tax reimbursement for year 4;
   25% business tax reimbursement for year 5.

   (More advantageous concessions are available for business located in rural areas, and Selebi-Phikwe which has been designated "rural" for the purpose of the FAP only).

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2. Unskilled citizen labour grant in respect of citizens earning less than P7,40 per day may be claimed on the following basis:

   80% reimbursement on wage bill in years 1 and 2;
   60% reimbursement on wage bill in year 3;
   40% reimbursement on wage bill in year 4;
   20% reimbursement on wage bill in year 5.

3. Training grants of 50 percent of citizens off-the-job training costs will be paid during the first five years of the project. These grants cover, inter alia, tuition, board and lodging, travel, materials and wages.[306]

It should be noted that AFA grants are in the form of reimbursements and no funds whatsoever are provided to assist with initial project investment.[307]

Under the CFA scheme, the project must yield an economic rate of return of at least 6 percent for consideration. The undermentioned grants are available:

1. Capital grants of P1 000 per job created. The following maximum limits apply:

   - 40 percent of total fixed investment in peri-urban areas (Francistown, Gaborone and Lobatse).

   - 50 percent of total fixed investment in peri-urban areas (Mogoditshane and Tlokweng).

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- 55 percent of total fixed investment in non-urban primary centres (Mahalapye, Maun, Mochudi, Molepolole, Kanye and Serowe).

- 65 percent of total fixed investment in rural area east including Selebi Phikwe.

- 85 percent of total fixed investment in rural area west.

2. Sales augmentation grants are made to a maximum of:

   - 8% of sales revenue in each of the first two years;
   - 6% of sales revenue in year 3;
   - 4% of sales revenue in year 4;
   - 2% of sales revenue in year 5.

3. Unskilled labour grant as in AFA scheme.

4. Training grant as in AFA scheme.[308]

There are certain limits to the assistance provided under the CFA scheme. These limits are determined as follows:

The total volume of sales augmentation, unskilled labour and training grants summed over the five year period should not be more than:

a) 50% of the domestic value added accruing in Botswana over the five year period. Value added is defined here as sales revenue minus inputs minus transfers to foreigners;[309]

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or

b) a percentage of unskilled wages plus training costs over the same period of time. The percentage varies by location and is determined by the scheme below:

Gaborone	80%
Other urban and peri-urban areas	100%
Non-urban primary centres	110%
Rural Area East	120%
Rural Area West	135%

The maximum assistance is the lower of a) and b).

(These grants are awarded on an individual case-by-case merit basis).

Similar grants under either the AFA or CFA schemes are made available to large scale project operators. There is some flexibility in the application of these package deals relative to the complexity of many of the large scale projects.[310]

Medium-scale citizen applicants have experienced difficulty in preparaing the documentation required for FAP assistance. The Government has, therefore, introduced a financial counsellors' scheme through which the government meet the cost of approved private sector consultants up to P500 for fine-tuning FAP applications by citizens. Citizen projects with a fixed investment magnitude of more than P100 000 do not qualify for this benefit.[311]

Applications for assistance may be obtained from the Ministries of Commerce and Indusrty, Mineral Resources

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and Water Affairs, Agriculture, and Finance and Development Planning. Forms are also available from Botswana Development Corporation, Commercial Banks, the National Development Bank, consulting firms, Botswana's missions overseas and other such bodies.[312]

1.9.8.2 INDUSTRIAL LAND AND BUILDINGS

Government-owned land may be made available to prospective industrialists by way of fixed period state grants with a normal period of 50 years. Land prices as established by the government vary between P7,00 for ordinary industrial areas and P9,00 per square metre for industrial areas with rail services (Gaborone).[313]

The following is the approximate tendered building cost per square metre:

a)	warehouse	P 300,00
b)	warehouse with offices	P 450,00
c)	retail store - single storey	P 350,00
d)	retail store - supermarket	P 400,00
e)	office building - two storey	P 750,00
f)	office building - multi-storey	P1 000,00

These figures reflect the position as at the end of 1986. A reasonable allowance for escalation during 1987 would be one and a half percent per month.[314]

1.9.8.3 INVESTMENT POLICY

There are a number of factors which should encourage businessmen and industrialists to invest in Botswana:

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- the government believes in free enterprise and fosters foreign investment;
- the registration of companies is relatively simple;
- minimal controls are exercised on business operations;
- no expropriation or nationalisation;
- no difficulty in obtaining foreign exchange;
- exchange control regulations are interpreted as liberally as possible;
- little difficulty in repatriating capital;
- labour is reasonably cheap and there is little union agitation;
- there are good transport links with major trading partners;
- electricity is readily available;
- country is financially stable;
- access to world markets through SACU, Lome Convention and SADCC;
- investment incentives, especially financial assistance policy, generous;
- there is an established expatriate community;
- adequate educational and medical facilities;

- sporting facilities are excellent;
- little pollution;
- the country is socially and politically stable.[315]

On the debt side, the potential investor should note:

- there is on-going pressure to localise jobs;
- under-employment and unemployment;
- productivity is low compared with Western standards;
- English medium schools have few vacancies;
- housing and land are expensive;
- infrastructure is costly and services may be restricted in the less populous areas;
- competition from neighbouring states, especially the Republic of South Africa and its black homelands, which also offer attractive investment incentives;
- the small size of the local market.[316]

Most expatriates state that it is pleasant to live and work in Botswana. There are few tensions and the people are friendly.

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The Government of Botswana has prepared the following Code of Conduct to publicise its attitude to foreign investors.

1. Foreign investors should regard themselves as full participants in Botswana's economic life and should take a long term view of their contribution to Botswana. As a consequence of taking a long view, foreign investors should take steps to ensure that their operations in Botswana become as independent as feasible with respect to performing their own technical services, adaptive research, purchasing of inputs, etc. In return, foreign investors can expect to be treated fairly and equitably in regard to such policies as taxation and exchange control, since government recognises the requirement for investors to earn a reasonable return on well managed, economically viable investments.[317]

2. Foreign investors should recognise the need to actively train Batswana for positions at all levels of technical expertise and should reduce the share of non-citizens in their work-force over time. In this effort they must be co-operative with the Commissioner of Labour in preparing an agreed training and localisation programme. Government has various financial incentives to assist companies with their training programmes and government welcomes suggestions and other contributions from foreign investors on how the public sector can best assist with training and the promotion of opportunities for citizens to advance. Foreign companies who are maintaining appropriate levels of training activities and who

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are moving expeditiously to promote citizens will receive co-operation from the Commissioner of Labour in meeting their remaining requirements for work permits for non-citizens.[318]

3. Foreign investors are expected not only to be law-abiding, but also to identify with the development aspirations of Botswana and its national planning objectives, to assist in the implementation of national development plans and actively to share Botswana's commitment, to maintenance of a democratic, open, non-racial society.[319]

4. Foreign investors are encouraged to offer shareholdings in their ventures to citizens. In some sectors, government will expect to be a direct shareholder; in others Botswana Development Corporation will take an equity interest. In most sectors, individual citizens should be sought as investment partners, even if on a modest scale. Government believes that the long-run stability of the economic system will be greater if citizens share ownership of economic ventures in all sectors of the economy. In addition, foreign investors should, if they wish to sell their enterprises, give citizens a fair opportunity to purchase.[320]

1.9.8.4 LAND TENURE

There are three legally recognised categories of land tenure in Botswana: state land (23 percent), tribal land (71 percent) and freehold land (6 percent).

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State Land falls under the direct control of the central government and any applications for leases must be referred to the Ministry of Local Government and Lands.[321]

Tribal Land is allocated by Tribal Land Boards in terms of the Tribal Land Act 1968. This act aims at developing the process of land allocation in accordance with Botswana's democratic principles, providing a legal framework for land allocation in tribal areas and encouraging agrarian land reform.[322]

Freehold Land. While there is no formal policy to buy back land owned by non-citizens, the government intends to encourage increased citizen ownership. The Land Control Act, 1975, lays down that all land for sale must be advertised in Botswana and ministerial authority has to be obtained for all agricultural land transactions involving non-citizens. This authority will only be given if there is no citizen desirous of and able to acquire the property. Furthermore, a higher rate of transfer duty, at present 30 percent, is levied on transactions involving non-citizens. The transfer duty for citizens is five percent.[323]

Freehold land is concentrated in the Francistown, Gaborone, Ghanzi, Lobatse, Molopo, North East District and the Tuli Block areas. Here large ranches are located and modern skilled agricultural practices employed. An increasing number of Batswana farmers are purchasing land in these areas.[324]

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321 IBID, P62

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There is a Deeds Registry in Gaborone. It falls under the control of the Department of the Attorney-General. It should be noted that stamp duty on all documents has been abolished.[325]

A Presidential Commission on Land Tenure was set up in 1982 to look into the whole area of land tenure. Its findings were published early in 1984. One important recommendation, the easing of restrictions involving the mortgage of tribal land, was accepted. Financial institutions may now take bonds over tribal land.[326]

1.9.8.5 TENDERING

The Botswana Government has a Central Tender Board which is located in, and controlled by the Ministry of Finance and Development Planning in Gaborone. In practice the Board is autonomous and is composed of senior officials from various ministries such as Commerce and Industry, Finance, Works and Communications, and Mineral Resources and Water Affairs. The rules and regulations concerning tender procedures are contained in Financial Instructions and Procedures which are issued pursuant to Section 44 of the Finance and Audit Act of the Laws of Botswana.[327]

Tenders for contract values in excess of P50 000 are classed as public tenders and as such are advertised in the Government Gazette, the local press, in Southern Africa and often on an international basis. Tenders received by the Secretary of the Central Tender Board are confidential and are secured unopened in a double

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locked container until the appointed tender closing time, when the sealed envelopes or packages are opened in the presence of the public and details read out.[328]

The board normally meets once a week to open and record tenders in the presence of the public, after which work continues in private. Contract values below P50 000 are awarded by the board following an informal tender procedure.[329]

TYPES OF CONTRACTS

Supplies are obtained on an individual purchase basis or by period contracts over one year or more with allowance for proven cost escalation. Tenderers for supply items are usually requested to price in their national currencies, and payment made on any subsequent contract would be in the national currency of the successful tenderer.[330]

Works and service contracts, eg. major road projects, buildings and supervision of such works by consultants, are governed by internationally accepted contract conditions.[331]

EVALUATION AND AWARD OF CONTRACTS

Tenders are evaluated by the ministry or department concerned, which makes a recommendation to the board after assessing all factors such as price, quality or known performance, delivery or completion date, and

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local preference for goods manufactured in Botswana. The board adjudicates the tender as a whole, seeking expert advice where necessary, and authorises the award of the contract to the firm whose tender is found most satisfactory.[332]

LOCAL PREFERENCE

Manufacturers resident in Botswana are allowed a local preference of 12,5 percent when tendering for government supply contracts in competition with foreign manufacturers. Citizen-owned firms in the building industry are given assistance with their cash flow at the beginning of a government contract by being allowed reduced sureties for the due performance of the work.[333]

1.9.8.6 HOUSING

The urban areas of Botswana suffer from acute housing problems and the cost of accommodation has risen considerably. It is estimated that country-wide there are some 24 000 families on the waiting list for all types of housing. The critical situation has been aggravated by the problem of urban drift which is a feature of development in most third-world countries. The squatter camps which have grown up around most of the towns are, however, being upgraded by the provision of infrastructural services and controlled re-organisation is being undertaken.[334]

The Botswana Housing Corporation is a statutory body whose major functions are to ascertain the demand,

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332 IBID, P62

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334 IBID, P53

rather than the need for housing, to plan to meet this demand, to provide housing of all types throughout the country for sale or rental on an economic basis and to manage the government housing pool.[335]

The corporation is responsible for the design, construction, management and maintenance of housing, principally within the urban areas of Francistown, Gaborone, Jwaneng, Lobatse and Selebi-Phikwe. It has been particularly successful in supplying housing in the medium to high bracket range. No attention is being given to the supply of high density medium cost housing and core units for enlarging by purchasers.

The need to provide low-cost housing still constitutes a major problem area. In the capital alone, some families have been on the waiting list for renting low-cost houses since 1978. There is an urgent need for the setting aside of serviced sites for such housing. The corporation continues to stress the urgency of the situation.[336]

As at 31 March 1986 the corporation owned 7 256 housing units. Industrial housing projects have been entirely the responsibility of the private sector. Individuals and companies are now purchasing plots but on a relatively small scale. Most individuals settle in the capital, where housing is at a premium.[337]

Government "pool" houses are allocated in accordance with Government regulations by committees in Francistown, Gaborone, Jwaneng, Lobatse and Selebi-Phikwe. It is largely "situational" housing related

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335 IBID, P53

336 IBID, P53

337 IBID, P54

for example to the building of schools which generally necessitates the provision of teacher accommodation.[338]

In terms of the Government Guaranteed Purchase Scheme, the Botswana Building Society entered into an agreement with the government to assist citizens to purchase or build houses for owner-occupation, with maximum assistance if the house does not cost more than P100 000. The normal maximum loan is 75 percent, but under the agreement, this can be increased to 95 percent. The maximum period of repayment is 25 years. Special conditions exist for loans in excess of P100 000. The interest rate on such loans is 12 percent up to P50 000 and 13 percent for accounts above this amount. There has been some dissatisfaction with the scheme, which is at present under review.[339]

The average price to build a low cost house is R300 per M^2 with an additional P4 000 to cover cost of land in extent $450M^2$. A medium cost house would be priced at P400 per M^2 with land priced at P7 500 for $600\text{-}900M^2$. In respect of a high cost dwelling, the price would be P450 per M^2 on a stand $900\text{-}1000M^2$ in extent costing in the region of P11 000. These prices apply to Gaborone and are for land purchased direct from thee Government. Prices of land purchased on the private market are substantially greater. Prices outside of the capital are higher.[340]

Building plans must be submitted to the local authority and the Town and Regional Planning Division of the Ministry of Local Government and Lands. The architect is usually responsible for this. The Deeds Office is in Gaborone.[341]

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Increased attention is being given to housing in the rural areas, where until recently houses were generally company or institutional dwellings. In these areas some 80 percent of units are traditional dwellings of thatched roofs supported by wooden poles with mud brick surrounds.[342]

1.9.9 TOURISM

Tourism is increasingly recognised as an important sector under the Government's diversification policy, with the potential to create additional employment and foreign exchange earnings. The country has been made more accessible to tourists by improved air services and a new tourism policy due to be approved by Parliament in 1990. This reaffirms the government's commitment to promoting low volume, high cost tourism and will establish a licensing system for tour operators.[343]

The number of visitors remains modest. There were 242 000 business, tourist and other visitors (excluding returning residents, day trippers and visitors in transit) in 1988, down from 275 000 in 1987. Business visitors continued to outnumber tourists and of the total most came from South Africa and Namibia. There are three national parks and five game reserves; the principle attractions are the unique Okavango Delta region, a vast maze of waterways, islands and lakes in

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341 IBID, P55

342 IBID, P55

343 THE ECONOMIC INTELLIGENCE UNIT, BOTSWANA, LESOTHO, SWAZILAND, 1990-91 COUNTRY PROFILE, ANNUAL SURVEY OF POLITICAL AND ECONOMIC BACKGROUND, WORLD MICROFILMS PUBLICATIONS LTD., LONDON, 1990. P24

the north west, and the wildlife of the Chobe reserve in the north east. A conference centre has been added to the 158 room Gaborone Sun, and capacity at the President Hotel has been increased to 100 rooms while a 200 room Sheraton Hotel was opened in August 1990.[344]

In recent years, greater efforts have gone into marketing Botswana overseas, through participation in the London and Berlin tourist fairs. The tarring of Maun airport and the introduction of regular flights from Gaborone has made the north west more accessible, while Namibia's independence has opened up the prospect of marketing Botswana's tourist attractions alongside those of Namibia, as well as Zimbabwe, through joint packages with tour operators.[345]

1.10 EDUCATION

The following are the government's enunciated objectives for education:

- to prepare Batswana for useful and productive lives with emphasis on training to meet the manpower requirements of the economy;

- to increase educational opportunities for all age groups and reduce inequalities of educational opportunity;

- to co-ordinate educational facilities to provide continuous access from primary to post-primary education and training using both the formal and informal systems;

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344 IBID, P25

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- to strengthen the co-operation between the school and the community by encouraging joint participation in the management of schools.[346]

The government plans to intensify vocational and technical training by expanding existing centres and introducing additional courses at the university.[347]

The budget speech 1987 contained a major statement on education when the Minister of Finance and Development Planning informed the National Assembly of the government's intention to abolish secondary school fees as from 1988. Primary school fees were done away with in 1980 and as a direct result enrolment rose from 72 000 to 200 000.[348]

While there has been a remarkable expansion of educational opportunities during the last decade with an estimated 83 percent of the primary school age population at school, the objective of universal access to primary education has not been achieved. The government introduced in 1986, a nine-year basic education programme, the first phase of which will be seven years of primary and two years of junior secondary education. These years will be amended to six and three years respectively at phase two. It is planned that by the middle of the 1990's universal access to this nine-year programme will be available to all Batswana children.[349]

In 1986 there were 231 397 children attending primary school. Minimum entry age is seven years and tuition

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346 BARCLAYS BUSINESS GUIDE TO BOTSWANA, 1987, P55

347 IBID, P55

348 IBID, P55

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is free. In 1986 there were 68 secondary schools with an enrolment of 39 584. The momentum of secondary school expansion characteristic of the last five years is to be maintained so that by 1991 some 70 percent of standard seven leavers will gain access to secondary education.[350]

Setswana is the medium of instruction for the first four years of schooling, thereafter instruction is given in English. At present, the seven-year primary course culminates in a public examination: the primary school leaving certificate. The majority of the secondary schools are located in the eastern part of the country and most have boarding facilities. Pupils write the Cambridge examinations, after the successful completion of a further five years study. At the end of the third year of secondary school, pupils may write a public examination which qualifies them for further training in the civil service, nursing and teaching professions.[351]

There are nine fee-paying English medium primary schools. These are located at Francistown (two), Gaborone (three), Lobatse, Orapa, Mogoditshane and Selebi-Phikwe. At Lobatse fees are levied for boarders only. These schools provide a good standard of education. There is a limited availability of places.[352]

There are four primary teacher training colleges in Botswana. These are situated in Francistown, Lobatse, Serowe and Tlokweng. Further such colleges are planned. Junior secondary school teachers are trained

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351 IBID, P55

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at Molepolole, where the college facilities are designed to cater for 600 students. Teacher training for secondary school is also offered at the university. In-service training is to be aggressively encouraged by the establishment of more education centres for two-week non-residential courses with the emphasis on the curriculum for the nine-year basic education programme.[353]

Tertiary education is provided at the University of Botswana which was established in 1982 following the dissolution of the University of Botswana and Swaziland. The University offers degree courses in agriculture, commerce, economics, law, social studies and the natural sciences. New departments of geology and pre-entry science have been established. The latter is an attempt to raise the standard of a reasonable "O" level student to that of university entrance.[354]

Degree programmes in business administration and commerce, and diploma courses in librarianship, adult education and primary education have been introduced. A Bachelor of Education (Science) programme is under implementation, while a certificate in Mathematics/Science (Education) has been started. In 1986 there were 1 543 students, 95 percent of whom were Batswana. Academic staff for the year number some 200. It is envisaged that there will be 3 374 students by 1991.[355]

Vocational training is undertaken in one guise or another in approximately seventy different centres

353 IBID, P56

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throughout the country. These centres provide training opportunities in varying degrees and forms for 8 000 - 9 000 Batswana.[356]

In conjunction with employers and employees in industry, the government has set up a tripartite committee known as the National Industrial Training and Technical Education Committee (NITTEC) to ensure that the many government departments and organisations involved in education are progressing efficiently and effectively. The terms of reference of the committee are:

- to co-ordinate technical and vocational education and industrial training;

- to ensure progress on achieving national standards for technical education and trades testing, and assessing the comparability of foreign qualifications;

- to be responsible for technical and professional matters related to vocational and technical training;

- to advise government and industry on training priorities and training for localisation.[357]

The Technical Education Committee, formerly the Technical Training Committee is charged with the integration of education and training with the industrial sector. It will report directly to the NITTEC.[358]

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356 IBID, P56

357 IBID, P57

358 IBID, P57

Four vocational training centres are to be opened at Jwaneng, Maun, Palapye and Selebi-Phikwe. The sites have been identified and the outline designs are in hand. These centres will be able to accommodate 1 400 students at any one time and will play an important role in regional development.[359]

The Botswana Polytechnic in Gaborone offers craft and technician courses in a wide range of subjects such as bricklaying, telecommunications, printing and refrigeration. Diploma courses are provided in civil, electrical and mechanical engineering. The Botswana Institute of Administration and Commerce caters for secretarial, public service and accountancy training. Certificate and diploma courses in agriculture and animal health are available from the Botswana Agricultural College. Plans are in hand for these three educational institutions to provide degrees in their particular technical fields. The degree courses would be monitored by the University of Botswana, and controlled and assessed by foreign universities of international repute. These programmes would avoid the duplication of facilities at the university.[360]

The Automotive Trades Training School opened in 1982 and offers three-year courses for auto-electricians and mechanics, with plans for the introduction of a course for heavy duty plant mechanics. All courses follow the City and Guilds of London curricula and certification, with local adaptations as and when necessary. Successful candidates are, therefore, in the possession of an internationally accepted qualification.[361]

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359 IBID, P57

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In 1983 the government published a policy paper on the Brigades, training and production units, offering vocational training orientated to the needs of the local community with the emphasis on rural development. Trainees should have a minimum of seven years primary education. There were 839 trainees in 1985. Courses last three years. The brigades are private enterprises which receive a government training allowance of P1 300 per trainee. With only 55 percent of primary school leavers proceeding to secondary school, the importance of the brigades in accepting some of the remainder should not be under-estimated.[362]

A community service, known as Tirelo Setshaba, a national study-service scheme for Botswana citizens commenced in 1980. Through it "O" level school leavers undertake a year of study service in remote rural areas before proceeding to further education or employment. Completion of a Tirelo Setshaba year in addition to normal academic qualifications is now required for entry to many further education courses. The scheme is to be expanded to include all "O" level school leavers. At present, however, it can only absorb half the citizens who apply. In 1986/87 there were 850 participants and staff numbered 52.[363]

The main objectives of the scheme are:

- to give an educating, broadening, maturing experience to all "O" level school leavers before they begin further education or employment;

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362 IBID, P57

363 IBID, P57

- to provide educated manpower to help carry out development programmes in rural areas, particularly in remote areas;

- to encourage greater understanding of each other among people from different parts of the country.

An important incentive toward the formation of Tirelo Setshaba was the increasing gap between the educated urbanised minority and the less educated rural majority.[364]

Participants in the Tirelo Setshaba scheme will be able to assist with the National Literacy Programme, which is designed to promote literacy especially in remote areas where there are no schools. The Department of Non-Formal Education will co-operate with the National Library Service in the establishment of reading rooms at village level.[365]

The National Library Service is the centralised authority responsible for the development of government, departmental, special libraries, school/college libraries and public libraries in Botswana. The primary objectives of the service are "to make library services accessible to all members of the community for the purposes of education, recreation, research and information, and to provide professional advisory services to government, private organisations, the education sector and other interested institutions in the development of library and information services". The service has 21 branches and service points which include a mobile library. The annual budget for books is P160 000. The current total

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364 IBID, P57

365 IBID, P57

book stock is 254 987 volumes, while the registered membership stands at 65 794.[366]

The Government of Botswana is aware that "one of the prerequisites of sustained economic growth is the availability of skilled and productive manpower; and, especially in Botswana, there is an increasing need for skilled manpower in all sectors of the economy". It is anticipated that by the year 2001 the difference between the needs of industry and the number of available skilled workers will be 28 000. This projection is based on an anticipated industrial growth rate of 7 percent and the government is making every effort to narrow this gap.[367]

1.11 CONCLUDING REMARKS

For a country to be endowed with a resource that is valued highly in world markets can be a benefit. However, it is not sufficient for strong growth performance. If badly managed, both unstable growth and external debt crises can result. Recent experiences of oil-exporting, middle-income, developing countries demonstrate this. Botswana has avoided many of the problems that other developing countries have been unable to avoid.[368]

Macro-economic policies can help offset any undesirable effects of temporary commodity price booms. One lesson that can be learned from Botswana's experience is that in the face of variability in and uncertainty about the

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366 IBID, P57

367 IBID, P57

368 R. BHEENICK <u>ET AL</u>, <u>SUCCESSFUL DEVELOPMENT IN AFRICA</u>, ECONOMIC DEVELOPMENT INSTITUTE OF THE WORLD BANK, WASHINGTON D.C. 1989, P204

value of a major export sector, erring on the cautious side and assuming that any increase is temporary and any decline permanent is better. Most pressures in the economy, particularly on the government, will be to reach the exact opposite conclusion: that increases are permanent and declines temporary. The cost of assuming a boom to be permanent when it is not may include balance of payments crises and unstable growth. However, the costs of assuming the boom to be temporary when in fact it is permanent will be increased savings at the expense of increased expenditures.[369]

Another lesson is that adjusting to shocks quickly rather than postponing adjustment can have benefits. The necessary changes are smaller, which can reduce the short term costs of adjustment. The package of adjustment policies adopted in Botswana in response to the bust in the diamond market in the early 1980s is a good example. Another example is Botswana's frequent but relatively small adjustments in the pula exchange rate over the last decade.[370]

Anticipating and planning for future shocks can also help prevent crisis situations from arising and result in better economic performance. In Botswana, not only were reserves accumulated in expectations of future declines in diamond export growth rates, but the government thought through the effects of different adjustment policies that could be used if needed. As a result, when the bust occurred in the early 1980s, adjustment was easier than it would have been otherwise.[371]

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369 IBID, P204

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Although some of the reasons why Botswana was able to manage commodity booms and busts successfully are not applicable to other countries, these lessons are relevant for other countries They apply not only to other countries trying to manage variable export earnings, but also to countries subject to other types of external shocks as well.[372]

1.12 SUMMARY

In this chapter we discussed the geographical location of Botswana and found it to be a landlocked country, sharing its borders with South Africa, Namibia, Zimbabwe and Zambia. Its population was estimated at 1,068,000 in 1985, based on the last official census held in 1981 when the population was 936,000 and was composed of mainly eight tribes, which are the Bakgatla, Bakwena, Bamalete, Bamangwato, Bangwaketsi, Batawana, Batalokwa and Barolong.

On the side of the natural resources, we mentioned that shortage of water, resulting from low annual rainfall, aggravated by considerable fluctuations in the monthly rainfall distribution and the total seasonal rainfall, is the biggest hindrance to the development of Botswana's natural resources.

Focus was also placed on the development of party politics and here we learned that Botswana has three main political parties. These being the Botswana Democratic Party(BDP), Botswana National Front (BNF) and Botswana People's Party (BPP). The challenge faced by the government of Botswana with the unilateral declaration of independence by Rhodesia (now Zimbabwe) in 1965 was discussed, as well as internal and external relations.

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The chapter also looked in a certain amount of detail at the economy of Botswana since 1980. Particular attention was focussed on the role played by the following in the economic development of Botswana:

- Agriculture
- Minerals and Mining
- Manufacturing
- Energy and Water Management.

The chapter also looked, in a fair amount of detail, at the following:

- Foreign trade and balance of payments
- Government finance
- Employment and wages
- Industrial development
- Tourism and
- Education.

1.13 TABLES

1.13.1 DISTRIBUTION OF VOTES AND PARLIAMENTARY SEATS

	1979 Seats (no)	Votes %	1984 Seats (no)	Votes %	1989 Seats (no)	Votes %
Elected Seats						
Botswana Democratic Party (BDP)	29	75	29	68	31	75
Botswana National Front (BNF)	2	13	4	20	3	15
Botswana People's Party (BPP)	1	7	1	7	-	5
Other	-	5	-	5	-	5
Nominated Seats						
Botswana Democratic Party	-	-	4	-	4	-
TOTAL	32	100	38	100	38	100

SOURCE : Central Statistics Office (CSO)

1.13.2 POPULATION BY TOWN AND DISTRICT

	1971	1981	% change	Estimates 1989
Town				
Gaborone	17 718	59 657	237	120 239
Francistown	18 613	31 065	67	52 725
Selebi-Phikwe	4 940	29 469	497	49 542
Lobatse	11 936	19 034	59	26 841
Palapye	5 218	9 594	-	16 959
Jwaneng	-	5 567	84	13 895
Total Urban including others	63 540	166 268	162	300 855
District				
Central[a]	210 840	313 735	49	373 667
Ngwaketse	70 558	104 182	48	127 180
Kwengeng	65 251	117 127	80	154 733
Other (8 districts)	163 905	239 715	46	299 314
Total Rural	510 554	774 759	52	954 894
Grand Total	574 094	941 027	64	1 255 749

[a] Excluding Palapye

SOURCE : Central Statistics Office (CSO)

1.13.3 EXCHANGE RATE (pula per $; annual average)

1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
0,777	0,833	1,022	1,096	1,284	1,888	1,868	1,678	1,816	2,012

SOURCE : IMF, International Financial Statistics

1.13.4 TREND OF GROSS DOMESTIC PRODUCT AT MARKET PRICES[a]

	1981/82	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88	1988/89
Total (Pmn)								
At current prices	793	1 050	1 302	1 661	2 235	2 648	3 398	4 988
At constant (1979/80) prices	754	934	1 121	1 212	1 308	1 441	1 570	1 783
Real Change %	-2,4	23,9	20,0	8,1	8,0	10,2	9,0	13,5
Per Head (P)								
At current Prices	844	1 071	1 289	1 582	2 050	2 343	2 904	4 122
At constant (1979/80) prices	802	953	1 110	1 154	1 200	1 276	1 342	1 474
Real change %	-	18,9	3,6	4,0	4,0	6,3	5,2	9,8

[a] Years ending June 30

SOURCE : CSO, Statistical Bulletin, IMF, International Financial Statistics

1.13.5 INDUSTRIAL ORIGIN OF GDP AT CURRENT MARKET PRICES[a]

	1981/82 P mn	%	1983/84 P mn	%	1986/87[b] P mn	%	1988/89 P mn	%
Agriculture, forestry & fishing	88	11,1	76	5,8	87	3,2	149	3,0
Mining & Quarrying	130	16,4	406	31,2	1 211	44,1	2 542	51,0
Manufacturing	71	9,0	82	6,3	169	6,2	209	4,2
Construction	48	6,1	71	5,4	79	2,9	166	3,3
Electricity & Water	22	2,8	32	2,5	71	2,6	93	1,9
Transport & Communications	20	2,5	33	2,5	59	2,1	82	1,6
Trade, Hotels & Restaurants	182	23,0	277	21,2	460	16,7	818	16,4
Financial Services	62	7,8	87	6,7	164	6,0	263	5,3
Government	156	19,7	225	17,3	394	14,3	638	12,8
Social & Personal Services	33	4,2	44	3,4	72	2,6	118	2,4
GDP at Market Price[b]	**793**	**100,0**	**1 302**	**100,0**	**2 747**	**100,0**	**4 988**	**100,0**

[a] Years ending June 30. [b] Including imputed bank service charges which are negative

SOURCE : CSO

1.13.6 EXPENDITURE ON GROSS DOMESTIC PRODUCT[a] (current market prices)

	1980/81 P mn	%	1981/82 P mn	%	1985/86 P mn	%	1986/87 P mn	%
Private Consumption	410	51,9	488	61,5	817	37,2	969	37,2
Public Consumption	203	25,7	243	30,6	527	24,0	625	24,0
Gross fixed capital formation	307	38,8	305	38,5	512	23,3	607	23,3
Change in Stocks	38	4,8	46	5,8	-6	-0,3	-8	-0,3
Exports of goods & services	398	50,4	350	44,1	1 472	67,1	1 748	67,1
Imports of goods & services	-566	-71,6	-639	-80,6	-1 128	-51,4	-1 339	-51,4
GDP at market prices	**790**	**100,0**	**793**	**100,0**	**2 194**	**100,0**	**2 605[b]**	**100,0**

[a] Years ending June 30. [b] Total does not add due to rounding.

SOURCE: CSO, Statistical Bulletin

1.13.7 SECTORAL GROWTH OF GDP[a]
(%)

	1981/82	1982/83	1983/84	1984/85	1985/86	1986/87
Agriculture	-4.3	-16.3	-15.3	-8.1	-16.7	-10.6
Mining	-14.8	77.1	35.6	4.9	19.3	22.1
Manufacturing	23.8	-7.4	3.8	-18.6	22.1	11.0
Construction	16.3	-29.6	47.7	-8.0	9.3	16.7
Electricity & water	3.9	-1.3	24.2	20.5	35.3	4.1
Transport	22.3	31.5	-2.9	23.8	25.9	-0.3
Trade and hotels	-7.9	7.5	12.4	12.9	0.4	12.7
Finance	11.8	5.9	10.7	26.1	22.9	3.5
Government	8.8	7.9	11.1	14.6	5.7	10.4
Services	14.1	19.9	0.3	22.9	11.2	2.9
GDP at market prices	-2.4	23.9	20.2	8.1	14.0	14.7

[a] At constant 1979/80 prices

SOURCE: Central Statistics Office

1.13.8 STRUCTURE OF EMPLOYMENT[a]
('000)

	1981	1982	1983	1984	1985	1986	1987	1988	% of total
Private & parastatal	64.8	65.8	63.3	70.4	71.5	79.4	97.4	111.8	66.3
of which:									
agriculture, forestry & fishing	4.8	4.2	4.5	5.4	4.0	4.9	5.6	6.5	3.9
mining & quarrying	7.3	7.1	7.2	7.5	7.3	7.5	7.0	7.5	4.5
manufacturing	6.4	7.2	9.8	9.5	10.1	12.2	14.7	16.4	9.7
electricity & water	1.6	2.2	1.9	2.0	1.9	2.0	2.2	2.3	1.4
building & construction	15.2	13.6	9.6	11.1	11.6	13.7	16.9	22.3	13.2
trade, restaurants & hotels	15.3	16.6	15.3	18.1	18.3	20.9	25.7	28.8	17.1
transport, storage & communications	3.9	3.7	3.9	5.5	5.7	5.1	6.7	7.9	4.7
financial services	4.9	5.7	6.0	6.2	6.8	7.4	9.8	11.2	6.6
community & social services	3.8	3.9	3.5	3.5	3.9	4.0	6.6	6.7	4.0
education	1.6	1.6	1.6	1.6	1.9	1.7	2.1	2.3	1.4
Central government[b]	26.3	27.6	30.1	32.1	36.8	41.3	42.5	46.2	27.4
of which:									
education	6.8	7.7	8.3	8.8	10.2	11.1	11.2	12.3	7.3
Local government	6.3	6.7	7.2	7.5	8.8	9.4	10.3	10.5	6.2
TOTAL	97.4	100.1	100.6	110.0	117.1	130.1	150.2	168.5	100.0

[a] Excludes working proprietors and unpaid family workers. Data are as of August for 1981-84, and thereafter as of September. [b] Excludes both Botswana Defence Force (BDF) and central government casual and temporary employees, except for 1985-87 which include the latter.

SOURCE : CSO, Statistical Bulletin.

1.13.9 CONSUMER PRICE INDICES

(annual averages)

	1984	1985	1986	1987	1988	1989
National Index (Aug 1980 = 100)	152.7	165.0	181.6	199.4	216.0	241.0
% change	8.6	8.1	10.1	9.8	8.3	11.6
Urban Index (Sep 1985 = 100)	...	100.6	107.9	119.4	131.2	147.7
% change	...	...	7.3	10.7	9.9	12.6

SOURCE: CSO, Statistical Bulletin

1.13.10 LIVESTOCK NUMBERS

('000)

	1984	1985	1986	1987	1988	1989
Cattle	2,685	2,459	2,332	2,264	2,390	2,509
Goats	889	1,138	1,332	1,470	1,664	1,850
Sheep	167	200	229	240	269	290

SOURCE: CSO, Statistical Bulletin

1.13.11 CATTLE SLAUGHTERINGS AND SALES

	1984	1985[a]	1985/86[b]	1986/87[b]	1987/88[b]	1988/89[b]
Slaughterings ('000)	239	190	196	146	112	135
Average weight/head[c] (kg)	188	193	190	200	208	219
Sales of beef[d] ('000 tons)	26.4	17.0	24.6	18.4	16.1	19.0
Sales value[e] (P mn)	119	95	154	145	115	171
Total paid to producers (P mn)	59	58	62	56	55	91

[a] January-September only; the BMC changed its accounting period from a calendar year to an October-September basis in 1985. [b] Year ending September 30. [c] Average cold dressed weight (cdw). [d] Frozen and chilled boneless beef. [e] All products.

SOURCE: Botswana Meat Commission, Statistical Bulletin.

1.13.12 PRODUCTION OF PRINCIPLE CROPS[a]

('000 tons)

	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88[b]
Sorghum	5.2	5.7	15.0	16.0	18.0	96.0
Maize	8.5	0.5	1.5	3.6	3.3	8.5
Millet	0.5	0.7	1.8	1.3	0.4	3.0
Total incl others	15.8	8.6	20.0	21.9	22.0	116.0

[a] Crop years July-June. [b] Preliminary estimates.

SOURCE: Ministry of Agriculture.

1.13.13 MINERAL PRODUCTION

	1984	1985	1986	1987	1988	1989
Diamonds (mn carats)	12.9	12.6	13.1	13.2	15.2	15.3
Copper-nickel matte ('000 tons)	51.8	51.5	47.9	43.2	57.5	49.8
Gold (kg)	17.9	12.7	25.2	31.7	21.0	67.0
Semi-precious stones (tons)	37	14	5	40	38	146
Mineral production index(1984=100)	100.0	98.0	101.1	101.6	117.8	...

SOURCE: Department of Mines, Annual Report

1.13.14 SELECTED ENERGY STATISTICS

	1982	1983	1984	1985	1986	1987
Coal						
Production ('000 tons)	414.8	395.1	392.9	437.4	499.4	579.4
Value (P mn)	4.7	5.4	5.5	6.2	8.4	10.3
Electricity[a] (gwh)						
Production	432.0	432.2	426.1	438.5	426.4	551.1
Imports[b]	27.1	101.0	176.2	182.7	252.2	185.1
Consumption[c]	414.4	484.6	548.8	565.1	617.2	659.1
of which:						
mining	215.8	263.1	418.5	419.6	460.2	482.2
Liquid fuels						
Imports (P mn)	90.2	88.9	78.6	109.7	83.7	...

[a] Years to March 31. [b] All from Escom, South Africa. [c] Excludes station usage'distribution.

SOURCES: Statistical Bulletin; Botswana Power Corporation; IMF, International Financial Statistics.

1.13.15 TRANSPORT STATISTICS

	1983	1984	1985	1986	1987	1988
Vehicle registration & renewals	38.1	42.4	45.7	50.1	52.8	58.4
Railways:						
passengers	490	511	564	508	440	442
freight ('000 ton-km)	1,432	1,315	1,325	1,237	1,141	773
of which:						
transit	1,159	1,042	1,078	1,001	874	505
Airways: passengers	127	122	135	168	221	185

SOURCE: CSO

1.13.16 CENTRAL GOVERNMENT REVENUE AND EXPENDITURE

(P mn)

	Outturn 1986/87	1987/88	1988/89	1989/90	Budget 1990/91
Revenue					
Mineral taxes and royalties	845	1,034	1,508	1,551	2,057
Customs and excise	192	234	293	374	480
International aid grants	8	106	110	61	55
Non-tax revenues[a]	303	296	457	409	543
Total incl other	1,548	1,825	2,556	2,666	3,318
Expenditure					
Recurrent	582	696	907	1,129	1,290
Development[b]	427	616	880	1,209	1,609
Total	1,009	1,312	1,787	2,338	2,899
Overall balance	539	513	769	328	419

[a] Mainly the government's share in central bank surpluses.
[b] Total capital outlays, including net lending and deficit grants.

SOURCES: Ministry of Finance & Development Planning; budget statements

1.13.17 INTEREST RATES

(%; end year)

	1982	1983	1984	1985	1986	1987	1988	1989
Bank rate	12.0	10.5	9.0	9.0	8.5	8.5	6.5	6.5
Prime rate	14.5	13.0	11.5	11.5	10.0	10.0	7.5	8.0
Mortgage loans	14.5	13.0	13.0	13.0	12.0	12.0	10.0	10.0-11.5
Savings accounts	11.0	9.5	8.0	8.0	7.5	7.5	5.0	6.0
12 months fixed	13.5	12.0	10.0	10.0	8.5	8.5	6.5	6.5

SOURCE: Bank of Botswana, Annual Report.

1.13.18 MONEY SUPPLY

(P mn; end year)

	1982	1983	1984	1985	1986	1987	1988	1989
Currency in circulation	29.0	30.2	35.2	43.4	58.5	68.6	95.8	117.5
Demand deposits	97.2	165.5	134.9	317.6	386.7	771.6	881.2	1,385.0
M1	126.2	195.7	170.1	361.0	445.2	840.2	977.0	1,502.5
Savings deposits	36.8	43.9	51.2	59.4	74.1	91.6	123.6	158.0
M2	163.0	239.6	221.3	420.4	519.2	931.8	1,100.6	1,660.5
Notice & time deposits	74.0	71.5	132.3	101.0	67.3	56.2	90.2	95.1
M3	237.0	311.1	353.5	521.4	586.5	988.0	1,190.8	1,755.6

SOURCE: Bank of Botswana, Annual Report.

1.13.19 ASSETS AND LIABILITIES OF THE COMMERCIAL BANKING SECTOR

(P mn; end year)

	1982	1983	1984	1985	1986[a]	1987	1988	1989
LIABILITIES								
Deposits	201.6	225.9	321.4	330.7	367.7	481.0	672.9	863.4
Capital & reserves	20.9	24.8	29.5	40.3	41.3	55.8	62.7	99.4
Other[b]	39.3	37.7	47.9	94.8	60.3	64.3	93.4	119.0
Total	261.8	288.4	398.8	465.9	469.3	601.1	828.9	1,081.9
ASSETS								
Balances at central bank	58.2	68.3	75.7	106.6	90.9	183.9	290.7	347.5
Balances due from other banks	11.9	8.8	33.8	38.5	46.2	52.2	71.7	46.5
Bills of exchange	6.0	7.8	16.0	17.0	21.4	20.7	21.0	38.8
Cash	10.4	12.0	13.2	12.5	14.0	16.0	27.4	32.8
Loans, advances & leasing	142.6	169.4	222.7	239.9	252.0	264.7	347.8	490.9
Other[c]	32.7	22.0	37.4	51.3	44.6	63.6	70.3	125.4
Total	261.8	288.4	398.8	465.9	469.1	601.1	828.9	1,081.9

[a] Assets and liabilities do not balance in source. [b] Includes balances due to other banks and government deposits. [c] Includes fixed assets and domestic investments.

SOURCE: Bank of Botswana, Annual Report.

1.13.20 TREND OF TRADE

(P mn)

	1984	1985	1986	1987	1988	1989[a]
Exports fob	880	1,384	1,602	2,672	2,686	3,661
Imports cif	-895	-1,096	-1,331	-1,572	-2,129	-2,557
Balance	- 15	288	271	1,100	557	1,104

[a] Preliminary

SOURCES: Bank of Botswana, Annual Report; Department of Customs and Excise

1.13.21 EXPORTS BY MAJOR COMMODITY

(P mn)

	1984	1985	1986	1987	1988	1989[a]
Diamonds	616	1,048	1,226	2,251	1,963	2,838
Copper-nickel[b]	78	120	99	129	421	432
Meat products	95	102	125	101	97	147
Other[c]	91	114	152	191	205	244
Total	880	1,384	1,602	2,672	2,686	3,661

[a] Preliminary. [b] Metal in matte. [c] Includes re-exports

SOURCES: Bank of Botswana; Department of Customs and Excise

1.13.22 IMPORTS BY COMMODITY GROUP

(P mn; cif, duty inclusive)

	1983	1984	1985	1986	1987	1988[a]
Food, beverages & tobacco	153.9	165.0	191.7	221.9	253.4	307.9
Machinery & electrical goods	103.2	147.4	185.1	219.0	260.4	254.1
Vehicles & transport equipment	93.2	115.1	150.1	222.5	242.8	289.4
Fuel	102.1	92.2	126.5	111.9	113.6	135.1
Metal & metal products	79.2	81.7	100.9	122.4	148.5	172.9
Chemical & rubber products	67.2	75.9	88.8	124.6	153.4	181.7
Other	207.1	215.6	251.9	308.8	400.3	509.9
Total	805.9	892.9	1,095.1	1,331.1	1,572.5	1,851.0

[a] Preliminary (BANK OF BOTSWANA); CONVERTED FROM SACU UNITS OF ACCOUNT (RAND) at year average exchange rate

SOURCES: SCO, Statistical Bulletin; Bank of Botswana, Annual Report

1.13.23 MAIN TRADING PARTNERS

(% of total)

EXPORTS TO:	1982	1987	IMPORTS FROM:	1982	1987
Other Europe	51	90	Sacu	87	79
Sacu	11	4	Other Africa	6	8
Other Africa	13	4	Other Europe	2	7
UK	12	1	USA	2	2
USA	12	-	UK	2	2

SOURCE: CSO, Statistical Bulletin

1.13.24 BALANCE OF PAYMENTS

(P mn)

	1984	1985	1986	1987	1988[a]	1989b
Merchandise exports fob	879.4	1,384.4	1,601.9	2,663.8	2,686.1	3,660.8
Merchandise imports fob	-757.5	-939.5	-1,143.3	-1,349.7	-1,804.7	-2,147.6
Trade balance	**122.4**	**444.9**	**458.6**	**1,314.1**	**881.4**	**1,513.2**
Exports of services	253.3	306.6	407.0	484.5	561.9	720.3
Imports of services	-494.5	-671.0	-753.4	-989.9	-1,430.6	-1,786.4
Net private transfers	-9.5	-6.0	-4.9	11.4	-29.4	-31.5
Net official transfers	141.5	176.4	215.1	272.8	325.4	388.5
Current account balance	**13.1**	**250.9**	**322.4**	**1,029.9**	**308.7**	**804.1**
Private long term capital	129.3	199.8	187.2	-141.5	237.3	258.6
Private short term capital	13.3	-0.3	47.7	-26.3	24.9	29.0
Government capital	22.8	-13.5	17.0	26.9	13.1	14.9
Banking sector capital	-21.4	52.6	-45.0	-2.0	-10.6	11.6
Capital account balance	**144.0**	**238.6**	**206.9**	**-142.9**	**264.7**	**314.1**
Net errors & omissions	7.5	11.1	36.6	-8.0	124.0	45.5
Valuation adjustments	-	-	-9.9	9.1	518.6	-284.1
Change in reserves (- indicates increase)	**-164.6**	**-500.5**	**-556.0**	**-951.1**	**-1,216.0**	**-879.5**

[a] Revised. [b] Preliminary

SOURCE: Bank of Botswana, Annual Report.

1.13.25 INTERNATIONAL LIQUIDITY

($ mn)

	1982	1983	1984	1985	1986	1987	1988	1989
Foreign exchange	276.05	376.23	453.83	758.35	1,161.48	2,012.95	2,217.14	2,791.00
SDRs	6.83	7.60	8.36	10.65	17.14	21.82	22.59	24.85
IMF reserve position	10.09	11.84	12.10	14.20	19.06	22.32	18.36	25.26
Total reserves excl gold	**292.97**	**395.67**	**474.29**	**783.21**	**1,197.67**	**2,057.08**	**2,258.09**	**2,841.11**

SOURCE: IMF, International Financial Statistics.

CHAPTER THREE

FOREIGN AID - LOANS AND GRANTS

1.1 INTRODUCTION

This chapter investigates the role played by foreign aid in the form of grants and loans in the economic development of Botswana since 1980. The chapter will also investigate how much foreign aid (in the form of loans and grants) was available at the time of independence in Botswana.

The chapter will proceed by analysing the build-up of development assistance in Botswana. More specifically, the chapter will look at where the development assistance came from (countries and organisations), what it was meant for, how it was managed and how it was paid back as well as conditions attached to the development assistance.

The chapter will also look, in a fair amount of depth, on the question of donor preferences as well as focussing on the question of donor management. In this chapter focus will also be placed on what actually attracted aid donors to Botswana.

The issue of donor influence, especially as it relates to donor influence on the selection of projects, will also be looked into. In addition, the chapter will look into the impact of technical assistance in the economic development of Botswana.

This chapter will also focus on Botswana's external payment and debt, and will conclude by looking at how this debt was actually serviced.

1.2 DEVELOPMENT ASSISTANCE AFTER INDEPENDENCE

Independence brought immediate and profound political change, but in the economic sphere Botswana faced critical problems in the mid-1960s, and the prospects for rapid progress appeared to be slight. With a per capita income of about P60 per year (then equivalent to about US $80), Botswana was one of the poorest countries in the world. Widespread absolute poverty had become entrenched as a result of five years of serious drought. By 1966, one third of the national herd of cattle had died, and in the same year one fifth of the population were receiving famine relief.[373]

During the years immediately prior to independence a number of economic-survey missions had visited the protectorate to assess aid requirements and development prospects. Each of them concluded that the likelihood of achieving a rapid growth of domestic income was negligible - so much so that the Government would be unable to raise sufficient revenue from local sources to cover even its recurrent expenditures within the foreseeable future. By implication, aid would have to be sought to finance not merely the future investment programme, but also to help cover the basic consumption needs of the society. If this aid was not forthcoming, it seemed that the Government would have to remain a skeletal institution along colonial lines, with a continued emphasis upon regulatory rather than developmental functions.[374]

From the point of view of the new Government, the most important of these survey missions was that of the

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373 COLCLOUGH C & MCCARTHY S, <u>THE POLITICAL ECONOMY OF BOTSWANA</u>, 1ST EDITION, OXFORD UNIVERSITY PRESS, LONDON, 1980, P54

374 IBID, P54

British Ministry of Overseas Development, which completed its report in November 1965. In that year, almost half of the total recurrent and development expenditure of the protectorate was financed directly by the United Kingdom, and it seemed certain that Botswana would continue to seek the major part of its aid requirements from the same source. Not surprisingly then, the British survey team was mainly concerned with the problem of how to achieve development in a way which would not significantly increase the budget deficit. Mineral deposits of copper, soda-ash, and coal were known to exist. But the survey team believed that the exploitation of these resources could affect economic growth and government revenues only in the long run. It was clear that the Government had insufficient resources to engage in any direct physical investment for mining development, but the report did not seriously consider how the Government might stimulate or benefit from private initiatives in the minerals sector. It was thought that economic growth would have to be based upon agricultural development, and the strategy envisaged by the British team concentrated upon measures to rebuild the national herd of cattle and regulate offtake from it, together with stronger measures in support of arable production. There was a firm emphasis in the report upon the need for stringent economic and financial management, reflecting a pessimistic view of the prospects for economic growth. As a result, its budgetary projections painted a depressing picture. The mere maintenance of public services at pre-independence levels would involve only a small narrowing of the recurrent deficit over a ten year period - from P4.7 million in 1966/67 to P3,8 million in 1975/6, in constant prices. The addition of even a modest development programme was expected to increase the recurrent deficit to P6 million by 1970/1.[375]

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375 IBID, P55

Fortunately this view was not shared by the government. A Transitional Plan covering the first two years of independence was quickly put together, to be followed by a succession of five-year National Development Plans, the first covering the period 1968-73. In these documents the government laid out the basic priorities.[376]

One basic priority was to create a sound administrative basis for development. Also fundamental was the need to generate enough domestic revenue to finance the government's recurrent budget in its entirety, and to contribute to development spending. However, there was a paradox. In order to end budgetary support, grant-in-aid had first to be increased, since long overdue investment in administrative, social and physical infrastructure appeared to be an essential precondition of financial self-sufficiency. The Transitional Plan put it as follows:

> However, even on the most optimistic projections and assuming that funds for development are forthcoming as requested, it does not appear possible for Botswana's dependence on grants-in-aid for recurrent expenditure to be ended for a long time to come unless the pace of development is much accelerated.

Financial self-sufficiency was in fact achieved in 1972-3; it was several years earlier than forecast, partly as a result of the renegotiated customs union agreement and mining developments.[377]

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376 HARVEY, C (ED), PAPERS ON THE ECONOMY OF BOTSWANA, 1ST EDITION, HEINEMANN EDUCATIONAL BOOKS INC, LONDON, 1981, P160

377 IBID, P160

At first there was one principle donor, the United Kingdom. In addition to budgetary support, the UK provided the bulk of the capital funds available to the government, in the form of Colonial Development and Welfare Act monies, Intercolonial Loans and Exchequer Loans. These funds were limited and had to cover many needs, ranging from agricultural and educational schemes whose development value was self-evident, to equally needed investments in administration and other government infrastructure. In the first five years of independence, 57 per cent of total development spending was financed from the United Kingdom.[378]

Other development finance consisted of an IDA (International Development Association) credit, worth P2.6 million, negotiated in 1964, and used for a nationwide programme of road and bridge improvements, an early Swedish grant for teacher training in Francistown, and a series of smaller grants from voluntary agencies such as Oxfam and the UK Freedom from Hunger Campaign, mainly for self-help projects in the rural areas. In addition, the government was able to negotiate a series of modest commercial loans from Barclays and Standard, the two international banks with branch networks in Botswana.[379]

2. THE BUILD-UP OF DEVELOPMENT ASSISTANCE

In the first four years after 1966 the general level of development spending was low. Then in the early 1970s, development spending rose dramatically.

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378 IBID, P160

379 IBID, P161

There were two reasons for the rise in development spending. First after years of prospecting, negotiation and design, construction of the large copper-nickel complex at Selebi-Phikwe got under way. The project was a joint venture between the government and an international consortium headed by Roan Selection Trust. The latter was responsible for the construction and operation of the mine, and the government undertook to build the infrastructure, the main elements of which were the mining township, a power station and a dam and pipeline to take water from the Shashe river. To meet the government's share of the project, finance was raised from the World Bank (US $32 million), the Canadian government (Can $30 million), and the United States government (US $6.5 million). These substantial sums of money were far beyond existing levels of project finance. Taken with the mining components of the project, they involved complex multiple financing and interlocking legal responsibilities between the investors, the lenders and the government. Both the size of the project and the complexity of its financing imposed a strain on the slender administrative resources of the government, particularly of high level managers. The government had to put a major effort into the project, including the creation of a special Shashe Project management unit within the administration. The ability of the government to borrow such a disproportionately large amount was partly because the government's debts were guaranteed by the mining companies involved, and partly because of a general belief, shared also by the donors, that Selebi-Phikwe would provide the desired breakthrough to budgetary self-sufficiency. As events transpired, these aspirations were met, but not in the way expected. The costs of the project severely escalated, particularly the mining components. Furthermore, technological troubles delayed start-up and the attainment of full production. Coupled with falling metal prices, this dashed hopes for a profitable return on investment. Although this led to losses and additional capital expenditure for the investors, the project had benefits for the government. First, it added substantially to customs receipts from the Southern Africa Customs Union pool, both during construction and in subsequent operation, leading directly to the attainment of budgetary self-sufficiency. Secondly, it exposed the aid agencies, to an extent that had not happened before, to Botswana and its development prospects, and particularly to the fact that the country had the ability to co-ordinate a project of this complexity and magnitude.[380]

Apart from the Shashe Project itself, the government's additional efforts to diversify aid sources were beginning to be successful. After the United Kingdom, the first major bilateral donor to commit itself to support a programme of projects was Sweden. In 1971, following visits to Stockholm by the Vice-President and senior officials, a major mission comprising members of the Swedish Ministry of Foreign Affairs and the Swedish aid agency, SIDA, arrived in Botswana to establish that Botswana met the criteria for Swedish assistance. This led shortly afterwards to the establishment of a regular annual aid programme. Spending from Swedish aid rose to over P9 million in 1977-8, having started with spending of P0.05 million in 1968-9. Two years later similar arrangements were concluded with the Norwegian government, represented by its aid agency, NORAD.[381]

Although all three aid agencies provided finance for a programme of development projects, chosen in the first instance by the Botswana government, Swedish and

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380 IBID, P162

381 IBID, P162

Norwegian aid differed operationally from United Kingdom aid. First the ground rules on spending the money were different. Because the UK Treasury limited spending authority to the year in which funds were voted, the Ministry of Overseas Development could not normally permit a carry-forward of unspent project finance from one year to the next. For an aid recipient, this meant projects that for one reason or another were not completed under one year's funding, lost their unspent allocation and competed with new projects for money in the following year. In other words, aid unspent in one financial year was lost to the recipient, since it could not be added to the following year's allocation. To avoid systematic underspending, since projects are habitually delayed, the British government allowed Botswana to overcommit by up to 40 per cent the total value of projects submitted for approval during the year. This concession was given on the understanding that should it appear in the closing months of the financial year that expenditures were likely to exceed the amount available, projects would be deliberately slowed down, or the excess met with other funds.[382]

Swedish and Norwegian procedures were simpler. Whilst no over-commitment was permitted, funds unspent in one year could be carried forward into the next year. This lessened somewhat the pressure to spend, and in turn pointed Scandinavian assistance towards projects in the rural areas where implementation slippage was traditionally greatest and the rate of project expenditure was harder to predict.[383]

Botswana's official aid receipts remained relatively static during the early 1980s, but the value of

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382 IBID, P162

383 IBID, P162

disbursements began increasing in 1986. This was mainly due to a rise in bilateral disbursements which, from a low point of $65 mn in 1985, had increased to $133 mn by 1987, declining slightly in the following year. This reflected an increase in aid from Sweden, now the country's largest bilateral aid donor, with Japan, Norway, the USA, and West Germany the other major sources. In 1988, grant aid comprised 82 per cent of total disbursements.[384]

Ironically in view of its recent wealth, but perhaps not surprisingly given its huge reserves and ability to import from these same bilateral donors, the country now receives more aid per head of population than any other country in the world apart from Israel - $128 per head in 1988, according to the World Bank's World Development Report.[385]

TABLE I

<u>GROSS OFFICIAL DEVELOPMENT ASSISTANCE</u> [a]
($ mn)

	1983	1984	1985	1986	1987	1988
Bilateral	84.5	77.0	65.3	84.9	132.4	131.8
of which:						
Sweden	11.6	11.0	7.3	16.3	14.2	21.1
Japan	0.1	0.1	-	1.2	0.1	20.5
Norway	8.0	7.8	11.1	11.7	17.0	18.0
USA	13.0	13.0	11.0	11.0	21.0	17.0
UK	15.1	12.6	7.9	9.9	12.5	14.7
West Germany	20.1	13.0	13.2	12.5	21.3	14.3
Multilateral						
of which:						
EC	2.1	6.8	2.8	7.3	5.2	8.9
WFP	9.9	10.3	22.1	9.3	9.0	6.3
UNDP	1.7	2.2	2.4	2.1	3.0	5.2
Total	105.5	105.4	101.1	108.9	167.4	159.1
of which:						
grants	92.0	87.8	90.6	105.1	149.0	129.7

384 THE ECONOMIC INTELLIGENCE UNIT, <u>BOTSWANA, LESOTHO, SWAZILAND</u>, 1990-91 COUNTRY PROFILE, ANNUAL SURVEY OF POLITICAL AND ECONOMIC BACKGROUND, WORLD MICROFILMS PUBLICATIONS LTD, LONDON 1990. P34

385 IBID, P34

[a] Disbursements. Official development assistance is defined as grants and loans with at least a 25 per cent grant element, provided by OECD and Opec member countries and multilateral agencies, and administered with the aim of promoting development and welfare in the recipient country. IMF loans, other than Trust Fund facilities, are excluded, as is aid from the Eastern bloc.

Source: OECD Development Assistance Committee, Geographical Distribution of Financial Flows to Developing Countries.

3. DONOR PREFERENCES

As Botswana diversified its sources of aid, it became apparent that the new donors had strong preferences about the categories of projects they were prepared to finance. How donor preferences affect the composition of development spending can be difficult initially to tie down. Most donors, for example, stress that the recipient selects the projects and provided there is reasonable economic justification, implementation has been thought through, and the project can be shown to fit the current development strategy, aid money will be forthcoming. Yet behind the apparent willingness to consider all projects, most donors have clear preferences. In the case of Norway and Sweden, there was a strong leaning towards rural projects and projects which were expected to benefit the lower income groups in the population. Fortunately, it was relatively easy for Botswana to assemble programmes that met these criteria. Furthermore, the flexibility with which the aid was administered made these donors the natural funding source for the projects that they were given.[386]

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386 HARVEY, C, OP CIT, P163.

All developing countries suffer from a shortage of administrative capacity in one form or another, and one of the surest ways of wasting precious management talent is to allocate priority projects to the wrong donors. SIDA's and NORAD's procedures were sufficiently flexible for this not to be a problem. But as Botswana's aid sources were further diversified, they were joined by other donors whose procedures were less flexible. Matching donors with suitable projects became critically important if the development programme was not to become bogged down. In most cases, the correct decisions were made, although the procedural difficulties of dealing with one particular donor were underestimated so that several priority projects were delayed.[387]

The interest shown in Botswana by the new donors coincided with the peaking of expenditures on the Shashe Project. Within the country there was concern that the capacity to implement demonstrated by the government should not be lost, but applied in some way to the rest of the development programme. There appeared to be an analogy with the early 1960s, when project implementation capacity had shown a similar sharp rise with the construction of the new capital at Gaborone, only to fall away again in succeeding years through lack of finance and follow-up. In 1973 the situation was different. Not only were new sources of aid becoming available, but substantial surpluses were being projected for the recurrent budget. Buoyant revenues were double edged. Whilst they could finance the recurrent costs arising from capital spending, there was a strong risk that if not applied to development they would find their way into unproductive consumption expenditure. As the construction stage of

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the Shashe Project wound down, a major effort was mounted to increase implementation capacity for all developmental projects. Agencies that provided expatriate technical assistance were asked to increase their ceilings, and did so. The project management unit concept, used so successfully to co-ordinate the Shashe Project, was applied to some other large projects. Most important of all, a number of existing and planned development projects in the rural areas were brought together in 1973 to form the Accelerated Rural Development Programme (ARDP). When it was wound up three years later, the ARDP's achievements included the construction of 78 miles of tarred road through major villages, 489 primary school classrooms, 425 teachers' houses, 596 latrines, 21 clinics, 43 health posts and 30 nurses' houses - the majority in nearly all cases being in smaller villages.[388]

The ARDP was important not only for giving concrete expression to the government's rural development policies but also for the implications it had on aid programming. Although the heavy concentration on rural projects resulted in delays elsewhere in the development programme (which affected in particular the UK programme), the ARDP was particularly good for the Swedish programme, its major external source of funding. There was also a useful demonstration effect on other donors whose programmes were just beginning. The ARDP showed that a capacity existed for the design and execution of rural projects, not only at central government level, but also in the district councils. Just as in earlier years the country had shown a capacity to make full use of the annual British allocation, and so gain additional sums, so successive years of full expenditure of Swedish monies resulted in a steady raising by SIDA of the country ceiling.[389]

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388 IBID, P164

Other donors, too, were showing increased interest in the country. Botswana's first loan from the African Development Bank, for telecommunications, was negotiated in 1972, to be followed by lending for road, health and airport development. Botswana's association with the World Bank group dated back to before Independence, but apart from two road credits, the bank's assistance had been concentrated in the Shashe Project. Following an economic survey mission in 1973, the bank reclassified Botswana as a country eligible for IRBD type loans to replace the IDA credits hitherto available. This meant harder lending terms, but it did hold out promise of a greater volume of resources. In 1974 a five-year rolling programme of projects was agreed between the bank and the government. This implied roughly one project a year, with a cumulative total of $50 million in loan finance over the period. At the same time there was much concern that the country was being promoted directly to hard loan status without enjoying the intermediate status of a combination of soft and hard lending. But the new arrangements did mean both an increased volume of lending and the convenience of being able to plan the preparation of bank projects several years in advance, with reasonable certainty that the requisite finance would be available at the time of implementation.[390]

Another major donor that was keen to expand its assistance was the United States. USAID financing had first been made available for Shashe Project water supplies. The next major project was the construction of Botswana-Zambia Highway, a project rated highly by the government for its strategic value, but which

389 IBID, P164

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suffered from delays and cost escalation. This ensured that it absorbed a large amount of US funds; after its completion in 1976, expenditure of AID funds fell back. There were several reasons for this. First, veterinary and other technical reasons caused the indefinite postponement of its successor project, the Northern Abattoir, to the consternation of the United States. Secondly, the strict rules governing where materials purchased under a USAID loan could be obtained limited the projects that were suitable. Thus for several years the bulk of American assistance took the form of technical assistance projects. More recently, USAID has been able to apply more flexible procedures, and the volume of disbursements is increasing.[391]

Another major Western country that has a substantial aid programme is the Federal Republic of Germany. A total of DM22 million (P9.5 million) was available in 1978-9, and the prospects for further assistance are encouraging. However, the large volume of German assistance is of recent origin. The first major project was the construction of the Francistown-Serule section of the north-south road, but this was slow in getting under way, and it was a long time before co-operation was expanded from a single project to a programme basis, so that only P3.0 million was actually spent in 1977-8.[392]

The final major Western donor was Canada, which had contributed at a critical time in the financing of the Shashe project by providing a low interest loan (later converted into a grant) for the power station, and had broadened its assistance subsequently in the support of the mining sector, the government transport

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391 IBID, P164

392 IBID, P165

organization, urban development and the university. Initially, the expansion of Canada's role was limited by the requirement that 75 per cent of expenditures had to be on Canadian goods and services, but these requirements were subsequently eased somewhat.[393]

The first efforts of the Botswana government to obtain from Arab sources were made in 1974, in the aftermath of the Arab-Israeli war. Approaches were made to several Arab agencies, but despite the solidarity between African and Arab countries at that time, the initiative was premature, and nothing came of it, with the exception of an allocation from the Oil Price Alleviation Fund in 1975 of $4.5 million. More recent approaches are beginning to show results, and in 1978 the first BADEA (Arab Bank for Economic Development in Africa) was approved for local vaccine production.[394]

The Lomé Convention between the African, Caribbean and Pacific (ACP) states (including Botswana) and the EEC was signed in February 1975, and within two weeks Botswana had submitted a portfolio of project outlines. Despite this promptness, there was a delay of over a year before the Commission was able to field a programming mission to announce the country ceiling (22 million units of account or US $28.9 million) and agree on as list of projects for financing. These covered a broad range of sectors, but the delay in establishing the programme was an augury of worse to come, for by the beginning of negotiations for the successor to the Lomé Convention in 1978, only 14 per cent of the funds available had been disbursed.[395]

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393 IBID, P165

394 IBID, P165

395 IBID, P165

4. DONOR MANAGEMENT

By the middle of the 1970s the diversification of Botswana's sources of external assistance was thus well under way. The additional finance, when added to growing local resources, made possible a rapid increase in the level of public sector development spending. It also brought with it a greater complexity to the management of the Development Budget.[396]

In the early days aid administration was simple. With only one major donor, all the implementing departments knew the rules and how to get the most out of them. Two things were important. First, to ensure that the total amount of capital aid available in the year was spent (otherwise it would be lost). Secondly, to follow the rules laid down on procurement. The first gave an immediacy to project implementation. Departments knew that their performance in carrying out their projects on time was the critical factor in deciding whether they would have an increased share of next year's funds, or more immediately, any supplementary finance that might be allocated to Botswana in the last quarter of the financial year. It has been argued that this emphasis on expenditure created bad habits and was at the expense of more carefully thought-out projects, and, worst of all, skewed expenditure in favour of the fast spenders. These tendencies undoubtedly existed but were more than offset by the positive incentives it gave to implementation performance and the focusing of attention on development. Botswana's ability in later years, when aid flows increased, to handle the greater flow of projects is primarily due to the habits

396 IBID, P165

learned, and the system of project monitoring developed, in the early days of British aid.[397]

In the early days, procurement rules were quickly learned. Any materials purchased with British aid had to originate either in Botswana or the United Kingdom. There were, however, important exceptions. In the first place, with few building materials produced locally, essentials such as cement, window and door frames, conduit piping, electrical fittings and corrugated roofing sheets had to be imported. It was clearly impractical to ship these supplies from the United Kingdom. Not only would this add to the cost, but delays would occur so that administration of contracts would have become almost impossible. The United Kingdom authorities quickly accepted this point, and a standing waiver for the purchase of general building supplies from South Africa was approved for all projects. Waivers were also granted for certain categories of vehicles that were assembled in South Africa from UK manufactured components, and for equipment items that were substantially more expensive to obtain from the UK, or on which for technical reasons the government had already standardized on a third country source. Aid officials of the Ministry of Overseas Development were under constant pressure, on the one side from the UK Department of Trade to increase the British content of aid spending, and on the other from Botswana to widen the scope of existing waivers. Yet despite these conflicting pressures, the aid programme was operated with commendable flexibility.[398]

As sources were diversified, matters became more complicated. Both Norway and Sweden readily accepted

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397 IBID, P166

398 IBID, P166

the need to buy essential supplies from South Africa, and were themselves under less balance of payments pressure to maximize domestic procurement. Their aid was therefore completely untied. Other donors, either through a failure to perceive the special position of the BLS countries, or, more frequently, because of restrictions imposed on the aid agency by other arms of government, were not able to take such a pragmatic line, and the usefulness of their aid was thereby diminished. USAID had an elaborate system of codes that listed the third countries eligible for procurement. In practice the ones that could supply were no more accessible than America, and little use could be made of them. Canada for a long while required 75 per cent Canadian procurement which ruled out most projects except consultancy services. The European Development Fund, while appearing in the text of the Lomé Convention to have a flexible approach, ended up applying one of the most impractical waiver systems of all.[399]

The different characteristics of donors clearly influenced the selection of projects and how they were implemented. The policy adopted by the government was to match projects with donors in a way that minimized implementation difficulties, while at the same time trying to retain priorities and to maximize the availability of external resources. How successfully this was done, and some of the unforeseen side effects is discussed below. In the meantime it is worth setting out the main reasons why the international community was so keen to increase aid flows to Botswana.[400]

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399 IBID, P166

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5. THE ATTRACTIONS OF BOTSWANA TO AID DONORS

There were a number of reasons why Botswana in the 1970s was an attractive place for the aid agencies. At the beginning of the period Botswana was unquestionably a poor country, with a per capita income level that qualified the country as one of the least developed. Yet unlike other low income countries once the mineral possibilities were perceived, Botswana offered the prospects of rapid growth. This provided two stimuli: first, the opportunity to participate in the government component of the Shashe Project, seen as critical to that project's success; second, an opportunity to help Botswana with the social, physical and administrative infrastructure that would become even more necessary as mineral-led growth accelerated. The growth potential also meant that Botswana seemed very likely to have the recurrent revenues necessary to maintain the schools, roads, clinics and other schemes that the donor money made possible.[401]

Next, Botswana was quick to establish a routine of planning that led to the production of clear and straightforward development plans in which it was easy to identify the policies of the government and the projects that needed financing. At independence Botswana issued the Transitional Plan for Social and Economic Development, covering the period 1966-8. This was followed by the National Development Plan 1968-73, the first of a series of five year plans, prepared on a rolling basis every two to three years. These plans, moreover, were not prepared in a separate planning commission, detached from the rest of government, but jointly by the planners and the executing departments.

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Consequently, the resulting sectoral programmes had an operational reality that the donor agencies appreciated.[402]

The ability to prepare effective development plans was matched by a capacity to implement that was unusual at such an early state of development. This advantage was probably more important in the eyes of the donors than the expertise in planning, although both stemmed from the importance given to development by the political leadership. In the clamour for a greater flow of resources from the rich countries to the poor, the point is generally overlooked that poor countries can be inefficient utilizers of the existing flows, inefficient, that is, in the eyes of donor agencies. Aid agencies, irrespective of whether their funds are grudgingly supplied by a government more concerned about domestic priorities, or are striving to disburse a target proportion of a rising GDP, are embarrassed by a failure of developing country governments to spend funds that have been approved. Consequently Botswana's ability not only to spend fully the amounts available under the UK aid programme in the early years, but to absorb at short notice supplementary allocations, resulted in additional aid, an effect that has not been fully appreciated. So not only was Botswana a country that met the normal criteria for aid worthiness, it also appeared able to spend the additional funds agencies provided. This it was able to do in an atmosphere that was remarkably free from corruption and dud projects.[403]

Political factors, too, were important. First, the political philosophy of the country's leadership

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translated into a real commitment to democratic freedoms and the rule of law that few other developing countries could match. This in turn led to policies for development that were broad based, and (at least in intent) refreshingly free from the modern sector biases found in many comparable countries. Next, the geopolitical position of Botswana, although it added a dimension of vulnerability to the county's future, gave an extra reason for assisting Botswana. If it was not possible for Western countries to alter the apartheid policies of South Africa, then contributing to an independent multiracial democratic state at its borders was a partly compensating alternative. For some donors this interest in Botswana in a wider setting did influence how they viewed domestic policies, and this is discussed in a later section.[404]

Finally, there was an intangible factor which although perhaps not apparent to new donors, did affect the aid relationship as it matured. This was the ability of Botswana government officials to establish excellent working relationships with those in the agencies that were responsible for determining policies towards Botswana. The result of this was that Botswana became a special case and rules that otherwise would have remained inviolable were bent in Botswana's favour. Some of the best examples come from the early days of the United Kingdom capital assistance. When supplementary loans were made available for spending in the last quarter of the financial year, short cuts were taken in both the preparation and approval of project memoranda based largely on the understanding between the officials of the two sides involved. The same also applied to waiver requests. In part this was due to the long association of the former colonial power and

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the continuity of individual contact. But it was also due to a genuine identification of agency staff with the development aspirations of the country, shared by other institutions like the World Bank, the Canadian aid agency (CIDA) and the Scandinavian agencies.[405]

6. DONOR INFLUENCE

The diversification of aid sources and the increase in the total amount available did place a burden on the administrative machinery of the government. At Independence a separate Ministry of Development had been formed, but in 1970 this was fused with the Ministry of Finance to create a powerful Ministry of Finance and Development Planning with the then Vice-President, Dr Masire, as its Minister. For most of the period aid co-ordination was the responsibility of the Division of Economic Affairs (corresponding to the former Ministry of Development), which was also responsible for plan preparation, project preparation and evaluation. Latterly the aid co-ordination role was shared with the budget section of the joint ministry. Aid relations took up a major portion of the time of officials in the division, and it may be asked whether a preoccupation with aid donors was not at the expense of longer term planning and policy activities.[406]

Several answers may be given to this point. First, for much of the period external finance was essential if the development programme was to go ahead, and, as explained below, the co-ordination of donors critically affects the rate of plan implementation. Secondly,

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there is little evidence to substantiate the claim that long term planning was adversely affected. Inevitably, progress on such policies as equitable income distribution, and industrial development has been less than one might hope. But the lack of progress in these areas is common to almost all developing countries, and it is questionable whether a less heavy aid co-ordination role would have made much difference.[407]

One of the reasons why Botswana throughout the period was able to achieve such a good record of aid utilization was the establishment from the outset of a sound monitoring system. When the United Kingdom was the sole source of programme aid, and the chance of supplementary allocations depended on spending performance, a simple but effective monitoring system was established. At regular intervals throughout the year, increasing to monthly in the final quarter, meetings would be held under the chairmanship of the Vice-President to review the implementation performance of development projects. Ministers accompanied by their officials would be called upon to report progress, and to undertake remedial action if bottlenecks were identified. As the aid programme became diversified and the number of projects both grew and became more complex, it proved impossible to handle the entire development budget in a single plenary session: the review meetings were then handled on an individual ministry basis in more detail, but with longer intervals between reviews.[408]

Such a high inflow of external resources clearly had a major effect on the rate of development in Botswana. Without the amounts made available in the years before

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and after Independence, the attainment of budgetary self sufficiency would have long been delayed; and if the build-up of aid resources had not continued after the end of grant-in-aid, domestic resources would have been woefully inadequate for the high levels of social and physical infrastructure investment that Botswana's circumstances required.[409]

What needs to be examined in greater detail is how the diversity of donors, each with their different philosophies of assistance with different rules and procedures, affected the shape and outcome of the development programme. What was the impact of this massive mobilization of external resources on domestic policy? To what extent did the terms of the aid affect the choice of projects, and how much leverage was applied?[410]

It is easiest to eliminate those aspects of the aid relationship that had little effect on the choice of projects and the outcome of the development programme. Aid funds were offered to Botswana under a range of different financial terms, but all loans had total repayment periods (that is, including the grace periods) of more than twenty-five years. A large proportion of the outstanding external debt consisted of IBRD borrowings (44 per cent in March 1979) which had long repayment periods but commercial rates of interest, and were mostly denominated in the currencies of the surplus countries. Other borrowings, though nominally on concessionary terms, required repayment in hard currencies like the Deutschmark. To what extent did the terms of borrowing affect either the willingness of the government to accept the loans or the uses to which the funds were put?[411]

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The short answer is: surprisingly little. With all donor financing on concessional terms, debt service was not normally a significant consideration. Furthermore, as part of a global effort to ease the burden of debt servicing, a number of Western donors retrospectively converted past loans into grants. This was welcomed in Botswana, but with a debt service ratio of about 4 per cent, and debt servicing never more than about 8 per cent of the recurrent budget, it was not a critical problem. Interestingly, as Botswana's per capita income rose, the terms of external financing if anything became softer, partly for compositional reasons and partly because of a worldwide trend towards increasing the concessional element in aid. In the early years the emphasis was on increasing the volume of external assistance, and the terms of new aid (seldom onerous) was never a serious factor. And with such a favourable time profile for its borrowings, throughout the period Botswana could afford to take a macro view on its borrowings.[412]

In the future, however, Botswana may have to rely more on near-commercial borrowings such as official export credits, and on fully commercial credit, for example from the eurocurrency markets. The country's first ever large-scale commercial loan, for $45 million from a consortium of banks, was negotiated in 1978, although it had not been drawn on by the end of 1979. The private sector, notably the copper-nickel mining company, has large external debts on commercial terms; although these do not affect the government directly, they do affect it indirectly by postponing the taxation of profits.[413]

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A potentially greater influence on poorer countries' development strategies is the aid philosophies of donors and their preference for projects to support. Most agencies stress that their assistance is guided by the development priorities of the recipient country. The Lomé Convention, for example, talks about the indicative programme being drawn up by 'mutual agreement', with a formal exchange of views between the European Economic Community and the ACP state to 'enable the ACP state to set out its development policy and priorities'. The Scandinavian agencies follow this approach as well, and international institutions like the World Bank are at pains to explain that they exist to respond to, not set, the priorities of the poorer nations. Yet on the other side the agencies themselves have development preferences, which tend to follow the current fashion in development thinking. In the 1950s, when development aid was seen as creating the take-off conditions for sustained growth, agencies liked large infrastructure and industrial projects. There was also a time when investment in education was seen as the key to unleashing the development process; and in the 1960s Botswana found it impossible to gain the interest of one major donor except with regional proposals. In the present decade the emphasis has been on rural development, income distribution and the share of benefits to the poor, with the World Bank in particular being concerned with the plight of the poor both in the rural areas and in the rapidly expanding cities of the Third World.

To workers in the field, with daily contact with these problems, it would be excusable if the successive highlighting of different aspects of underdevelopment by the agencies were greeted with some cynicism. The agencies, of course, have another constituency, the parliaments and taxpayers in the developed countries; and opponents of aid have been quick to criticize the failures of past policies. Nor have developing country governments necessarily followed enlightened policies themselves; for example, they have pressed hard for the financing of wasteful prestige projects.[414]

Yet it must be asked whether donor pressure is productive in the long run. For a start it is questionable whether the approach works, and when it does there can be some harmful side effects. It works something like this. The representatives of a new donor come into town and announce that they would like to assist the development of the country with an annual aid programme of X million dollars. 'Give us your highest priority projects' they say, and the ritual of selling the projects begins. Overlooked are the considerations that, first, while most governments have a general view on what is most urgent, there is no systematic ranking of projects. Theoretically this could be done by calculating internal rates of return, but no developing country government could or should afford the time for such an exercise. The project evaluation techniques of the textbooks are employed mainly to satisfy donor requirements for individual projects (that are probably going to be financed anyway). Secondly, to the extent that they have been identified, the highest priority projects are in the pipeline for an earlier donor. Finally, even if the highest priority projects were identified and available, it might be better for reasons of procedures and fungibility to finance them with non-donor funds if these are available.[415]

The fungibility argument runs as follows. A donor who wishes to influence the composition of the development

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programme should not rush for the priority projects. Whether he or someone else does it, they will be financed anyway. Donor finance then simply releases funds for other projects - of which the donor might, or might not, approve. Instead the donor should concentrate on the marginal projects where his influence on what he does or does not go ahead might be more effective.[416]

Looking back, then, on Botswana's experience with a multiplicity of donors, the answer is that probably the preferences of individual donors had relatively little effect overall on the composition of the development programme. There were certainly times when a deliberate effort was made to give a donor the type of project he wanted, particularly when the aid relationship was a new one, and the government was keen to build up the programme. But as long as there were other donors who were prepared to accept a different blend of projects, and as long as there were domestic resources available to finance the important but unappealing schemes (such as government infrastructure), the overall composition of the development programme was not really affected. It may, of course, be necessary to exert this sort of leverage in a country that is seriously neglecting important development areas, but in a country that prided itself on having a balanced development programme (on which the donors agreed), the result of such activities is likely to be a waste of many people's time on both sides.[417]

The project preferences of donors are likely, however, to affect the outcome of the development programme in a

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way that is not generally seen. From the point of view of the people co-ordinating the development programme within the government, the easiest type of money to handle is the one that carries the fewest strings. So the best kind of finance is domestic funds. Approval of the project is an internal process, far faster than the donor's clearance, and there are no restrictions other than the established rules of financial control governing the use of the funds. Donor finance comes with a baggage of procurement, tendering, disbursement, accounting and reporting requirements that can become quite burdensome in a developing country where shortage of administrative skills is one of the greatest bottlenecks. Some of the more advanced donors have realized this and their procedures are commendably simple and adapted to local conditions. British and Scandinavian aid has always been clear on this matter. Most other agencies have made progress with simplifying their procedures and adapting them to better local conditions.[418]

Yet the very priority areas that the donors have been stressing, rural development and the poor, are ones where it is more difficult to design delivery mechanisms and implementation success is less certain. A major highway is designed and supervised by international consultants who can handle most of the special procedures with relatively little administrative cost to the recipient. A village water supply scheme dealing in small units and dependent on local initiatives is a fragile affair by comparison and a lighter touch by the aid agency is essential. Some recognize this but many are still bound by the rigidity of their procedures (sometimes externally imposed); in other cases there is a lack of understanding of

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conditions on the ground. By insisting on projects which are in any case the most difficult to identify and implement, the donors may, therefore, actually slow down development spending in precisely those areas which both they and the government would like to emphasize.[419]

In some well known cases there was a pronounced cost to using donor money. The implementation of Broadhurst II, a project on which the next stage of Gaborone's expansion depended, became critically delayed by unforeseen evaluation, tendering and procurement delays on the part of the European Development Fund which had agreed to finance the water supply. Two similar village water supply schemes proceeded at different rates because one donor insisted on inspecting each village plant before its installation. The other was content with an annual evaluation after installation was completed.[420]

Yet on balance, Botswana has been remarkably free from this sort of difficulty. There were several reasons for this. First, the largest programme donor during this time, Sweden, arrived quite early on the scene, had incorporated into its programme some large rural development projects, and proved to be the most flexible of all external sources. Secondly, as the programme expanded a policy was evolved in the Ministry of Finance and Development Planning of giving the donors not necessarily the projects that they wanted but the projects that their procedures allowed them best to finance. This is not to suggest that the allocation of projects was tightly controlled and planned; it was a looser arrangement with give and take

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between the executing departments (who wanted finance for their projects but were not always aware how difficult their life might become if the wrong choice was made), the Ministry of Finance and Development Planning and the aid agencies. Because of the close working relationship, already mentioned, that grew up over the years between government officials and the local representatives of the agencies, much of this was done by mutual agreement.[421]

7. THE IMPACT OF TECHNICAL ASSISTANCE

Virtually all of the bilateral donors, and the United Nations Development Programme (UNDP), provided Botswana with large amounts of technical assistance, in the form of consultants, advisers and executive personnel holding established posts at the technical or administrative level. Some programmes were fully funded. Others like the United Kingdom's OSAS (Overseas Service Aid Scheme) programme supplemented the salaries of expatriate staff on government of Botswana contracts. In addition there were a large number of third country nationals occupying mainly middle level positions, directly recruited by the government. One donor, with unusual flexibility, even provided funds to finance key people in the latter category. Just as capital aid was being diversified the same process was happening with technical assistance personnel, although the numbers provided by the United Kingdom were so much in excess of other nationalities that the relative shift was much less. The need for such large numbers of foreign personnel was clear. Because of the lack of investment in education in colonial times, at Independence Botswana

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was in critical need of the skills to manage development. And as the pace of change accelerated, the manpower gap grew. Although manpower projections showed that investments in education and training would close the gap in the 1980s, Botswana in the first decade of Independence had no alternative but to expand considerably the numbers of expatriate staff in the public sector.[422]

There was, of course, an implicit trade-off between the pace at which the government could tackle the challenges of development and the rate at which localization could be achieved. In 1966 there was no doubt in the minds of ministers that to tackle the agenda that the government plan set forth required an expansion for a period in the numbers of expatriate personnel. The long-run plan for localization laid down in the first National Development Plan was self-sufficiency in higher level manpower for the whole economy by 1990, and the localization of all posts of a non-specialized administrative nature by 1972, with full localization for the public sector by the early 1980s. Such was the determination to break out of the stagnancy of the colonial period that considerations of localization were secondary. For the latter to be achieved, there needed to be substantial investment in education, and in other sectors to generate the revenues that would pay for the teachers and extension workers that were the front rank of the government's development strategy. No other route existed. In the early days a trade-off between alternative rates of growth and localization was never seriously debated: the key objective was to get the growth process started.[423]

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However, in 1973, when the country broke free from grant-in-aid and faced the prospects of larger surpluses in the future, a clear choice faced policy makers. Implementation capacity rather than finance was the new bottleneck. There was a risk that with the running down of construction activity on the Shashe project, the overall level of development spending would fall, resulting in a partially completed third National Development Plan and the temptation to use the new domestic revenues for public sector consumption, not investment. Accordingly, approaches were made to the agencies that provided technical assistance to raise the ceilings on their technical assistance, a request that was generally met.[424]

Thus a further growth in the numbers of technical assistance personnel took place, so that by 1978 there were more expatriate personnel serving in the public sector than at any time previously. At the same time, of course, the public sector was both growing very rapidly and making solid progress with localization, although it was increasingly clear that the targets of the first National Development Plan were unachievable.[425]

For most of this period there was little doubt in the mind of the government that the course that was followed was the right one. Outside commentators have generally failed to grasp the depth of feeling Botswana policy makers had about the lack of progress during the colonial period. Given, then, that Botswana's strategy for development did result in a large number of expatriates in the public sector, what were the

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particular consequences on the pattern of development that followed? The obvious one is that the expatriates brought with them technical and managerial skills that made the devising of key policies and the implementation of the government's development programme possible. The government could not have launched the Tribal Grazing Land Programme in the form it took without substantial additional expatriates in land-use planning and other planning capacities, and the same will be true for the new initiatives in dryland farming. The launching of the currency and the operation of the central bank would have been delayed, and it is hard to see how district planning and the channelling of funds for council projects could have been set up without the key role played by the volunteer agencies. Perhaps most important of all, the government would not have been able to play such a calculated hand in its dealings with the mining companies, and the level of revenues would have been less.[426]

But there were costs associated with such a large inflow of foreign personnel, with different living standards and many without experience of developing countries. Undoubtedly there was a powerful demonstration effect that showed through in wage demands and other areas. There were also costs in accommodating expatriates: houses had to be built and places found in English language primary schools. Some of the capital costs were met through aid funds, but a large part devolved on domestic revenues. However, the latter were costs that the growing revenues could accommodate.[427]

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More difficult to assess is the effect the expatriates had on the style of the government. Such an assessment has a high degree of subjectivity, but the following conclusions can be fairly drawn. First, although the personnel provided by the agencies were on the whole well qualified and able, the short period many of them served limited their contribution and made the job of training and localization more difficult. There was less time to find the best possible mode of operation and understand the wider setting into which their activities fitted. In turn this led to a second effect. In any job people tend to bring to it the standards and methods learned in their previous employment. In the early days the bulk of expatriates could show a continuity of service within the country, or in a similar territory where resources were limited and means had to be found for building roads, housing teachers and training farmers within a very tight budget. By later plan periods this continuity had been lost. At the same time projects and policies had become more complex, requiring longer time and more resources to carry them out. They also imposed a greater load on the largely local managerial cadre.[428]

In part this was a natural consequence of Botswana's economic growth, and the increased range of government involvement. Early plans were comprised of the simple and obvious projects that departmental heads had considered for years, in the absence of financial resources to put them into effect. Once the first generation of programmes was completed, the next rank was harder. Most of the key government policies, for example, grazing policy, dryland farming, mineral policy, employment, etc., were mentioned as objectives in the early plans, but it was left to the later period

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for comprehensive policies to be worked out. Yet while the technical expertise the donors provided made these new approaches possible, there is no doubt that the loss of continuity meant that in many cases technical and administrative approaches were devised that were fundamentally out of scale with the supply of indigenous technical and administrative resources.[429]

One example is the consultant who recommends a solution that can only be implemented if further consultants are employed. The history of regulations provides further examples. It will never be possible to more than guess at the cost of this phenomenon. As the economy has grown, it has also become more complex, which in turn has been reflected in the complexity of regulations emanating from the public sector. This process must have been worsened by the use of technical assistance personnel, although the impact cannot be quantified.[430]

8. EXTERNAL PAYMENTS AND DEBT

Mainly in consequence of export earnings rising more rapidly than imports, the overall balance of payments remained strongly in surplus throughout the 1980s, apart from 1981 when a small deficit was recorded. The diamond stockpile sale in 1987 produced a record current account surplus of P1.1 bn ($651 mn) and an overall surplus of P951 bn, almost double that of the preceding year. The current account surplus has subsequently fallen, but was still a healthy P804 mn in 1989, mainly due to an increase in the deficit on the services account, which reached P1.1 bn, according to preliminary figures. The increased net outflow on the

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services account is mainly attributable to a higher level of profit and dividend remittances, especially by Debswana, as well as interest payments on public and private sector external debt. Dividend outflows are estimated to have risen by some 56 per cent in 1989, with the main inflow comprising interest from investment of the country's foreign exchange reserves.[431]

BALANCE OF PAYMENTS
(P mn)

	1984	1985	1986	1987	1988[a]	1989[b]
Merchandise exports fob	879.9	1,384.4	1,601.9	2,663.8	2,686.1	3,660.8
Merchandise imports fob	-757.5	-939.5	-1,143.3	-1,349.7	-1,804.7	-2,147.6
Trade balance	**122.4**	**444.9**	**458.6**	**1,314.1**	**881.4**	**1,513.2**
Exports of services	253.3	306.6	407.0	484.5	561.9	720.3
Imports of services	-494.5	-671.0	-753.4	-989.9	-1,430.6	-1,786.4
Net private transfers	-9.5	-6.0	-4.9	11.4	-29.4	-31.5
Net official transfers	141.5	176.4	215.1	272.8	325.4	388.5
Current account balance	**13.1**	**250.9**	**322.4**	**1,092.9**	**308.7**	**804.1**
Private long term capital	129.3	199.8	187.2	-141.5	237.3	258.6
Private short term capital	13.3	-0.3	47.7	-26.3	24.9	29.0
Government capital	22.8	-13.5	17.0	26.9	13.1	14.9
Banking sector capital	-21.4	52.6	-45.0	-2.0	-10.6	11.6
Capital account balance	**144.0**	**238.6**	**206.9**	**-142.9**	**264.7**	**314.1**
Net errors and omissions	7.5	11.1	36.6	-8.0	124.0	45.5
Valuation adjustments	-	-	-9.9	9.1	518.6	-284.1
Change in reserves (- indicates increase)	**-164.6**	**-500.5**	**-556.0**	**-951.1**	**-1,216.0**	**-879.5**

[a] Revised. [b] Preliminary.

Source: Bank of Botswana, Annual Report.

The capital account has normally offset any weakness on the current account, remaining in surplus apart from 1987. In 1988-89 there were strong inflows of private long term capital, mainly in connection with the Sua Pan project and industrial investments. The overall balance of payments surplus peaked in 1988 at P1.2 bn, although valuation adjustments accounted for a large proportion of the final outcome, as in 1989 when the overall balance remained strongly in surplus. The positive evolution of the payments situation has

431 THE ECONOMIC INTELLIGENCE UNIT, BOTSWANA, LESOTHO, SWAZILAND, 1990-91 COUNTRY PROFILE, ANNUAL SURVEY OF POLITICAL AND ECONOMIC BACKGROUND, WORLD MICROFILMS PUBLICATIONS LTD, LONDON 1990, P32

enabled the foreign exchange regime to be progressively liberalised and there are now virtually no restrictions on current international transactions.[432]

Botswana's international reserves strengthened significantly in 1985-87, with foreign exchange holdings almost trebling to $2 bn. In 1988 and 1989 there were less spectacular increases, to $2.2 bn and $2.8 bn respectively. Bank of Botswana data show foreign exchange reserves to have reached a record P5.5 bn by the end of 1989, equivalent to 31 months' import cover. With the substantial increase in reserves, the bank adopted a set of guidelines in 1986 for managing these assets so as to maintain a diversified portfolio and maximise returns from high yield securities. Balances at foreign banks increased to 51 per cent of total reserves by December 1987, reflecting a move in the portfolio away from bonds and securities towards term deposits, but these had declined to 41 per cent of total reserves by December 1989.[433]

INTERNATIONAL LIQUIDITY
($ mn)

	1984	1985	1986	1987	1988	1989
Foreign exchange	453.83	758.35	1,161.48	2,012.95	2,217.14	2,791.00
SDRs	8.36	10.65	17.14	21.82	22.59	24.85
IMF reserve position	12.10	14.20	19.06	22.32	18.36	25.26
Total reserves excl. gold	474.29	783.21	1,197.67	2,057.08	2,258.09	2,841.11

Source: IMF, International Financial Statistics.

9. FOREIGN DEBT

Botswana continues to enjoy a very low level of foreign debt, and debt service in 1989 at $77 mn was only 3.8

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per cent of exports of goods and services. The bulk of Botswana's existing debt is to official multilateral creditors, which accounted for $336 mn of the total disbursed long term debt of $512 mn at the end of 1989. There was no recourse to foreign borrowing for payments support until mid-1982 when a eurodollar loan of $30 mn was drawn down, the only time Botswana has used this method of financing its external payments. However, the level of debt service has been gradually increasing and the 1989 repayment obligation was more than double the level of five years earlier. Payments on existing debt will reach a peak of $86.3 mn in 1993, based on commitments as at the end of 1988, but this would only place a strain on the country's finances if there were a significant deterioration in its trading position.[434]

EXTERNAL DEBT
($ mn unless otherwise indicated)

	1984	1985	1986	1987	1988	1989[a]
Total external debt	268	343	390	511	499	515
of which:						
long term debt [b]	263	341	387	507	494	512
short term debt	5	2	3	3	5	3
Public disbursed debt [b]	263	341	387	507	494	512
of which:						
official creditors	233	320	363	475	466	483
multilateral	146	216	258	339	324	336
bilateral	87	104	104	136	142	147
private creditors	30	21	25	33	28	29
Debt service	32	50	45	69	74	77
of which:						
principal	16	29	18	38	39	42
interest	16	21	27	32	35	36
Total external debt/GNP (%)	26.3	38.6	38.2	40.5	38.3	...
Debt service ratio (%)	3.6	5.6	4.3	3.6	4.1	3.8
Short term debt/total external debt(%)	1.9	0.6	0.8	0.6	1.1	0.6
Concessional loans [b]/total external debt (%)	40.4	36.0	31.9	28.2	30.9	31.6
Variable interest rate loans [b]/total external debt (%)	11.9	11.1	13.1	12.9	13.4	13.6
Interest arrears on long term debt	-	-	-	-	2	2

[a] Estimates. [b] Maturity over one year.

Source: World Bank, World Debt Tables.

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10. CONCLUDING REMARKS

There can be little questioning that the overall impact of foreign assistance in Botswana has been a beneficial one. Initially, the role played by British aid from the early 1960s until 1972-3, with both capital, recurrent and technical assistance support, when little other assistance was available, was vitally important, since it enabled Botswana to lay the foundations for future development. Many of the features that attracted later donors are directly traceable to this period. Secondly, the financing of the copper-nickel complex at Selebi-Phikwe by a consortium of donors under the co-ordination of the World Bank was also crucial. Although the profitability of the mine itself has proved a disappointment, its scale both in terms of construction and operation had major indirect effects on government revenues and economic activity as a whole. It established the ability of the government to co-ordinate such a large project, and in turn a determination to apply those management skills in other sectors.[435]

The subsequent diversification to many donors has made management of the development programme more complex, but that complexity has proved in some real sense to be manageable; meanwhile there are other (mainly strategic) advantages to diversity, so that the flow of development finance is now more secure than it was when there was only one donor.[436]

From the above, it is clear that both foreign loans and grants played a major role in the economic development of Botswana. Without official development assistance

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the economic development of Botswana would not have been possible to the level that we know today.

Official development assistance is defined as grants and loans with at least a 25 percent grant element, provided by OECD and OPEC member countries and multilateral agencies, and administered with the aim of promoting development and welfare in the recipient country. IMF loans, other than Trust Fund facilities, are excluded, as is aid from the Eastern Bloc. The value of official development assistance, which includes both loans and grant is well indicated in Table 1.

Important to note, is the role played by the provision of technical assistance in the economic development of Botswana. Virtually all of the bilateral donors as well as the United Nations Development Programme (UNDP) provided Botswana with large amounts of technical assistance in the form of consultants, advisors and executive personnel holding established posts at the technical or administrative level. Some programmes were fully funded. Others, like the United Kingdom's OSAS (Overseas Service Aid Scheme) programme supplemented the salaries of expatriate staff on Government of Botswana contracts. In addition, there was a large number of third country nationals occupying mainly middle level positions, directly recruited by the government.

11. SUMMARY

This chapter investigated the role played by foreign aid in the form of loans and grants in the economic development of Botswana since 1980.

During the years immediately prior to independence a number of economic survey missions had visited the protectorate to assess aid requirements and development prospects. Each of the concluded that the likelihood of achieving a rapid growth of domestic income was negligible, so much so that the Government would be unable to raise sufficient revenue from local sources to cover even its recurrent expenditures within the foreseeable future. By implication, aid would have to be sought to finance not merely the future investment programme, but also to help cover the basic consumption needs of the society. If this aid was not forthcoming, it seemed the Government would have to remain a skeletal institution along colonial lines, with a continued emphasis upon regulatory rather than development functions.

However, in the first four years after 1966 the general level of developmental spending was low. Then in the early 1970s development spending rose dramatically. This was partly because of the construction of the large copper-nickel complex at Selebi-Phikwe and also the Shashe project.

Apart from the Shashe project itself, the government's additional efforts to diversify aid sources were beginning to be successful. Foreign aid came from Sweden, Japan, Norway, USA, UK and West Germany, as well as from multilateral donors.

The chapter also showed that certain donors had their preferences. Most donors, for example, stressed that the recipient selects the projects and, provided there was reasonable justification, implementation has been thought through, and the project can be shown to fit current development strategy, aid money will be forthcoming. However, certain donors, such as Norway and Sweden, had a strong leaning towards rural projects and projects which were expected to benefit the lower income groups in the population.

Also in this chapter, an attempt was made to indicate the attractions of Botswana to aid donors. Once the mineral possibilities were perceived, Botswana offered the prospects of rapid growth. This provided two stimuli: first, the opportunity to participate in the government component of the Shashe project. Second, an opportunity to help with the social, physical and administrative infrastructure that would become even more necessary as mineral-led growth accelerated.

Also covered in this chapter is the question of donor influence. A potentially greater influence on poorer countries' development strategies is the aid philosophies of donors and their preference for projects to support. The impact of technical assistance on the economic development of Botswana was also discussed, as well as the question of external payments and debt.

CHAPTER THREE

FOREIGN AID - LOANS AND GRANTS

1.1 INTRODUCTION

This chapter investigates the role played by foreign aid in the form of grants and loans in the economic development of Botswana since 1980. The chapter will also investigate how much foreign aid (in the form of loans and grants) was available at the time of independence in Botswana.

The chapter will proceed by analysing the build-up of development assistance in Botswana. More specifically, the chapter will look at where the development assistance came from (countries and organisations), what it was meant for, how it was managed and how it was paid back as well as conditions attached to the development assistance.

The chapter will also look, in a fair amount of depth, on the question of donor preferences as well as focussing on the question of donor management. In this chapter focus will also be placed on what actually attracted aid donors to Botswana.

The issue of donor influence, especially as it relates to donor influence on the selection of projects, will also be looked into. In addition, the chapter will look into the impact of technical assistance in the economic development of Botswana.

This chapter will also focus on Botswana's external payment and debt, and will conclude by looking at how this debt was actually serviced.

1.2 DEVELOPMENT ASSISTANCE AFTER INDEPENDENCE

Independence brought immediate and profound political change, but in the economic sphere Botswana faced critical problems in the mid-1960s, and the prospects for rapid progress appeared to be slight. With a per capita income of about P60 per year (then equivalent to about US $80), Botswana was one of the poorest countries in the world. Widespread absolute poverty had become entrenched as a result of five years of serious drought. By 1966, one third of the national herd of cattle had died, and in the same year one fifth of the population were receiving famine relief.[373]

During the years immediately prior to independence a number of economic-survey missions had visited the protectorate to assess aid requirements and development prospects. Each of them concluded that the likelihood of achieving a rapid growth of domestic income was negligible - so much so that the Government would be unable to raise sufficient revenue from local sources to cover even its recurrent expenditures within the foreseeable future. By implication, aid would have to be sought to finance not merely the future investment programme, but also to help cover the basic consumption needs of the society. If this aid was not forthcoming, it seemed that the Government would have to remain a skeletal institution along colonial lines, with a continued emphasis upon regulatory rather than developmental functions.[374]

From the point of view of the new Government, the most important of these survey missions was that of the

373 COLCLOUGH C & MCCARTHY S, THE POLITICAL ECONOMY OF BOTSWANA, 1ST EDITION, OXFORD UNIVERSITY PRESS, LONDON, 1980, P54

374 IBID, P54

British Ministry of Overseas Development, which completed its report in November 1965. In that year, almost half of the total recurrent and development expenditure of the protectorate was financed directly by the United Kingdom, and it seemed certain that Botswana would continue to seek the major part of its aid requirements from the same source. Not surprisingly then, the British survey team was mainly concerned with the problem of how to achieve development in a way which would not significantly increase the budget deficit. Mineral deposits of copper, soda-ash, and coal were known to exist. But the survey team believed that the exploitation of these resources could affect economic growth and government revenues only in the long run. It was clear that the Government had insufficient resources to engage in any direct physical investment for mining development, but the report did not seriously consider how the Government might stimulate or benefit from private initiatives in the minerals sector. It was thought that economic growth would have to be based upon agricultural development, and the strategy envisaged by the British team concentrated upon measures to rebuild the national herd of cattle and regulate offtake from it, together with stronger measures in support of arable production. There was a firm emphasis in the report upon the need for stringent economic and financial management, reflecting a pessimistic view of the prospects for economic growth. As a result, its budgetary projections painted a depressing picture. The mere maintenance of public services at pre-independence levels would involve only a small narrowing of the recurrent deficit over a ten year period - from P4.7 million in 1966/67 to P3,8 million in 1975/6, in constant prices. The addition of even a modest development programme was expected to increase the recurrent deficit to P6 million by 1970/1.[375]

375 IBID, P55

Fortunately this view was not shared by the government. A Transitional Plan covering the first two years of independence was quickly put together, to be followed by a succession of five-year National Development Plans, the first covering the period 1968-73. In these documents the government laid out the basic priorities.[376]

One basic priority was to create a sound administrative basis for development. Also fundamental was the need to generate enough domestic revenue to finance the government's recurrent budget in its entirety, and to contribute to development spending. However, there was a paradox. In order to end budgetary support, grant-in-aid had first to be increased, since long overdue investment in administrative, social and physical infrastructure appeared to be an essential precondition of financial self-sufficiency. The Transitional Plan put it as follows:

> However, even on the most optimistic projections and assuming that funds for development are forthcoming as requested, it does not appear possible for Botswana's dependence on grants-in-aid for recurrent expenditure to be ended for a long time to come unless the pace of development is much accelerated.

Financial self-sufficiency was in fact achieved in 1972-3; it was several years earlier than forecast, partly as a result of the renegotiated customs union agreement and mining developments.[377]

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376 HARVEY, C (ED), <u>PAPERS ON THE ECONOMY OF BOTSWANA</u>, 1ST EDITION, HEINEMANN EDUCATIONAL BOOKS INC, LONDON, 1981, P160

377 IBID, P160

At first there was one principle donor, the United Kingdom. In addition to budgetary support, the UK provided the bulk of the capital funds available to the government, in the form of Colonial Development and Welfare Act monies, Intercolonial Loans and Exchequer Loans. These funds were limited and had to cover many needs, ranging from agricultural and educational schemes whose development value was self-evident, to equally needed investments in administration and other government infrastructure. In the first five years of independence, 57 per cent of total development spending was financed from the United Kingdom.[378]

Other development finance consisted of an IDA (International Development Association) credit, worth P2.6 million, negotiated in 1964, and used for a nationwide programme of road and bridge improvements, an early Swedish grant for teacher training in Francistown, and a series of smaller grants from voluntary agencies such as Oxfam and the UK Freedom from Hunger Campaign, mainly for self-help projects in the rural areas. In addition, the government was able to negotiate a series of modest commercial loans from Barclays and Standard, the two international banks with branch networks in Botswana.[379]

2. THE BUILD-UP OF DEVELOPMENT ASSISTANCE

In the first four years after 1966 the general level of development spending was low. Then in the early 1970s, development spending rose dramatically.

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[378] IBID, P160

[379] IBID, P161

There were two reasons for the rise in development spending. First after years of prospecting, negotiation and design, construction of the large copper-nickel complex at Selebi-Phikwe got under way. The project was a joint venture between the government and an international consortium headed by Roan Selection Trust. The latter was responsible for the construction and operation of the mine, and the government undertook to build the infrastructure, the main elements of which were the mining township, a power station and a dam and pipeline to take water from the Shashe river. To meet the government's share of the project, finance was raised from the World Bank (US $32 million), the Canadian government (Can $30 million), and the United States government (US $6.5 million). These substantial sums of money were far beyond existing levels of project finance. Taken with the mining components of the project, they involved complex multiple financing and interlocking legal responsibilities between the investors, the lenders and the government. Both the size of the project and the complexity of its financing imposed a strain on the slender administrative resources of the government, particularly of high level managers. The government had to put a major effort into the project, including the creation of a special Shashe Project management unit within the administration. The ability of the government to borrow such a disproportionately large amount was partly because the government's debts were guaranteed by the mining companies involved, and partly because of a general belief, shared also by the donors, that Selebi-Phikwe would provide the desired breakthrough to budgetary self-sufficiency. As events transpired, these aspirations were met, but not in the way expected. The costs of the project severely escalated, particularly the mining components. Furthermore, technological troubles delayed start-up and the attainment of full production. Coupled with falling metal prices, this dashed hopes for a profitable return on investment. Although this led to losses and additional capital expenditure for the investors, the project had benefits for the government. First, it added substantially to customs receipts from the Southern Africa Customs Union pool, both during construction and in subsequent operation, leading directly to the attainment of budgetary self-sufficiency. Secondly, it exposed the aid agencies, to an extent that had not happened before, to Botswana and its development prospects, and particularly to the fact that the country had the ability to co-ordinate a project of this complexity and magnitude.[380]

Apart from the Shashe Project itself, the government's additional efforts to diversify aid sources were beginning to be successful. After the United Kingdom, the first major bilateral donor to commit itself to support a programme of projects was Sweden. In 1971, following visits to Stockholm by the Vice-President and senior officials, a major mission comprising members of the Swedish Ministry of Foreign Affairs and the Swedish aid agency, SIDA, arrived in Botswana to establish that Botswana met the criteria for Swedish assistance. This led shortly afterwards to the establishment of a regular annual aid programme. Spending from Swedish aid rose to over P9 million in 1977-8, having started with spending of P0.05 million in 1968-9. Two years later similar arrangements were concluded with the Norwegian government, represented by its aid agency, NORAD.[381]

Although all three aid agencies provided finance for a programme of development projects, chosen in the first instance by the Botswana government, Swedish and

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380 IBID, P162

381 IBID, P162

Norwegian aid differed operationally from United Kingdom aid. First the ground rules on spending the money were different. Because the UK Treasury limited spending authority to the year in which funds were voted, the Ministry of Overseas Development could not normally permit a carry-forward of unspent project finance from one year to the next. For an aid recipient, this meant projects that for one reason or another were not completed under one year's funding, lost their unspent allocation and competed with new projects for money in the following year. In other words, aid unspent in one financial year was lost to the recipient, since it could not be added to the following year's allocation. To avoid systematic underspending, since projects are habitually delayed, the British government allowed Botswana to overcommit by up to 40 per cent the total value of projects submitted for approval during the year. This concession was given on the understanding that should it appear in the closing months of the financial year that expenditures were likely to exceed the amount available, projects would be deliberately slowed down, or the excess met with other funds.[382]

Swedish and Norwegian procedures were simpler. Whilst no over-commitment was permitted, funds unspent in one year could be carried forward into the next year. This lessened somewhat the pressure to spend, and in turn pointed Scandinavian assistance towards projects in the rural areas where implementation slippage was traditionally greatest and the rate of project expenditure was harder to predict.[383]

Botswana's official aid receipts remained relatively static during the early 1980s, but the value of

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disbursements began increasing in 1986. This was mainly due to a rise in bilateral disbursements which, from a low point of $65 mn in 1985, had increased to $133 mn by 1987, declining slightly in the following year. This reflected an increase in aid from Sweden, now the country's largest bilateral aid donor, with Japan, Norway, the USA, and West Germany the other major sources. In 1988, grant aid comprised 82 per cent of total disbursements.[384]

Ironically in view of its recent wealth, but perhaps not surprisingly given its huge reserves and ability to import from these same bilateral donors, the country now receives more aid per head of population than any other country in the world apart from Israel - $128 per head in 1988, according to the World Bank's World Development Report.[385]

TABLE I

GROSS OFFICIAL DEVELOPMENT ASSISTANCE [a]
($ mn)

	1983	1984	1985	1986	1987	1988
Bilateral	84.5	77.0	65.3	84.9	132.4	131.8
of which:						
Sweden	11.6	11.0	7.3	16.3	14.2	21.1
Japan	0.1	0.1	-	1.2	0.1	20.5
Norway	8.0	7.8	11.1	11.7	17.0	18.0
USA	13.0	13.0	11.0	11.0	21.0	17.0
UK	15.1	12.6	7.9	9.9	12.5	14.7
West Germany	20.1	13.0	13.2	12.5	21.3	14.3
Multilateral						
of which:						
EC	2.1	6.8	2.8	7.3	5.2	8.9
WFP	9.9	10.3	22.1	9.3	9.0	6.3
UNDP	1.7	2.2	2.4	2.1	3.0	5.2
Total	105.5	105.4	101.1	108.9	167.4	159.1
of which:						
grants	92.0	87.8	90.6	105.1	149.0	129.7

384 THE ECONOMIC INTELLIGENCE UNIT, BOTSWANA, LESOTHO, SWAZILAND, 1990-91 COUNTRY PROFILE, ANNUAL SURVEY OF POLITICAL AND ECONOMIC BACKGROUND, WORLD MICROFILMS PUBLICATIONS LTD, LONDON 1990. P34

385 IBID, P34

[a] Disbursements. Official development assistance is defined as grants and loans with at least a 25 per cent grant element, provided by OECD and Opec member countries and multilateral agencies, and administered with the aim of promoting development and welfare in the recipient country. IMF loans, other than Trust Fund facilities, are excluded, as is aid from the Eastern bloc.

Source: OECD Development Assistance Committee, Geographical Distribution of Financial Flows to Developing Countries.

3. DONOR PREFERENCES

As Botswana diversified its sources of aid, it became apparent that the new donors had strong preferences about the categories of projects they were prepared to finance. How donor preferences affect the composition of development spending can be difficult initially to tie down. Most donors, for example, stress that the recipient selects the projects and provided there is reasonable economic justification, implementation has been thought through, and the project can be shown to fit the current development strategy, aid money will be forthcoming. Yet behind the apparent willingness to consider all projects, most donors have clear preferences. In the case of Norway and Sweden, there was a strong leaning towards rural projects and projects which were expected to benefit the lower income groups in the population. Fortunately, it was relatively easy for Botswana to assemble programmes that met these criteria. Furthermore, the flexibility with which the aid was administered made these donors the natural funding source for the projects that they were given.[386]

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386 HARVEY, C, OP CIT, P163.

All developing countries suffer from a shortage of administrative capacity in one form or another, and one of the surest ways of wasting precious management talent is to allocate priority projects to the wrong donors. SIDA's and NORAD's procedures were sufficiently flexible for this not to be a problem. But as Botswana's aid sources were further diversified, they were joined by other donors whose procedures were less flexible. Matching donors with suitable projects became critically important if the development programme was not to become bogged down. In most cases, the correct decisions were made, although the procedural difficulties of dealing with one particular donor were underestimated so that several priority projects were delayed.[387]

The interest shown in Botswana by the new donors coincided with the peaking of expenditures on the Shashe Project. Within the country there was concern that the capacity to implement demonstrated by the government should not be lost, but applied in some way to the rest of the development programme. There appeared to be an analogy with the early 1960s, when project implementation capacity had shown a similar sharp rise with the construction of the new capital at Gaborone, only to fall away again in succeeding years through lack of finance and follow-up. In 1973 the situation was different. Not only were new sources of aid becoming available, but substantial surpluses were being projected for the recurrent budget. Buoyant revenues were double edged. Whilst they could finance the recurrent costs arising from capital spending, there was a strong risk that if not applied to development they would find their way into unproductive consumption expenditure. As the construction stage of

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the Shashe Project wound down, a major effort was mounted to increase implementation capacity for all developmental projects. Agencies that provided expatriate technical assistance were asked to increase their ceilings, and did so. The project management unit concept, used so successfully to co-ordinate the Shashe Project, was applied to some other large projects. Most important of all, a number of existing and planned development projects in the rural areas were brought together in 1973 to form the Accelerated Rural Development Programme (ARDP). When it was wound up three years later, the ARDP's achievements included the construction of 78 miles of tarred road through major villages, 489 primary school classrooms, 425 teachers' houses, 596 latrines, 21 clinics, 43 health posts and 30 nurses' houses - the majority in nearly all cases being in smaller villages.[388]

The ARDP was important not only for giving concrete expression to the government's rural development policies but also for the implications it had on aid programming. Although the heavy concentration on rural projects resulted in delays elsewhere in the development programme (which affected in particular the UK programme), the ARDP was particularly good for the Swedish programme, its major external source of funding. There was also a useful demonstration effect on other donors whose programmes were just beginning. The ARDP showed that a capacity existed for the design and execution of rural projects, not only at central government level, but also in the district councils. Just as in earlier years the country had shown a capacity to make full use of the annual British allocation, and so gain additional sums, so successive years of full expenditure of Swedish monies resulted in a steady raising by SIDA of the country ceiling.[389]

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Other donors, too, were showing increased interest in the country. Botswana's first loan from the African Development Bank, for telecommunications, was negotiated in 1972, to be followed by lending for road, health and airport development. Botswana's association with the World Bank group dated back to before Independence, but apart from two road credits, the bank's assistance had been concentrated in the Shashe Project. Following an economic survey mission in 1973, the bank reclassified Botswana as a country eligible for IRBD type loans to replace the IDA credits hitherto available. This meant harder lending terms, but it did hold out promise of a greater volume of resources. In 1974 a five-year rolling programme of projects was agreed between the bank and the government. This implied roughly one project a year, with a cumulative total of $50 million in loan finance over the period. At the same time there was much concern that the country was being promoted directly to hard loan status without enjoying the intermediate status of a combination of soft and hard lending. But the new arrangements did mean both an increased volume of lending and the convenience of being able to plan the preparation of bank projects several years in advance, with reasonable certainty that the requisite finance would be available at the time of implementation.[390]

Another major donor that was keen to expand its assistance was the United States. USAID financing had first been made available for Shashe Project water supplies. The next major project was the construction of Botswana-Zambia Highway, a project rated highly by the government for its strategic value, but which

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suffered from delays and cost escalation. This ensured that it absorbed a large amount of US funds; after its completion in 1976, expenditure of AID funds fell back. There were several reasons for this. First, veterinary and other technical reasons caused the indefinite postponement of its successor project, the Northern Abattoir, to the consternation of the United States. Secondly, the strict rules governing where materials purchased under a USAID loan could be obtained limited the projects that were suitable. Thus for several years the bulk of American assistance took the form of technical assistance projects. More recently, USAID has been able to apply more flexible procedures, and the volume of disbursements is increasing.[391]

Another major Western country that has a substantial aid programme is the Federal Republic of Germany. A total of DM22 million (P9.5 million) was available in 1978-9, and the prospects for further assistance are encouraging. However, the large volume of German assistance is of recent origin. The first major project was the construction of the Francistown-Serule section of the north-south road, but this was slow in getting under way, and it was a long time before co-operation was expanded from a single project to a programme basis, so that only P3.0 million was actually spent in 1977-8.[392]

The final major Western donor was Canada, which had contributed at a critical time in the financing of the Shashe project by providing a low interest loan (later converted into a grant) for the power station, and had broadened its assistance subsequently in the support of the mining sector, the government transport

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391 IBID, P164

392 IBID, P165

organization, urban development and the university. Initially, the expansion of Canada's role was limited by the requirement that 75 per cent of expenditures had to be on Canadian goods and services, but these requirements were subsequently eased somewhat.[393]

The first efforts of the Botswana government to obtain from Arab sources were made in 1974, in the aftermath of the Arab-Israeli war. Approaches were made to several Arab agencies, but despite the solidarity between African and Arab countries at that time, the initiative was premature, and nothing came of it, with the exception of an allocation from the Oil Price Alleviation Fund in 1975 of $4.5 million. More recent approaches are beginning to show results, and in 1978 the first BADEA (Arab Bank for Economic Development in Africa) was approved for local vaccine production.[394]

The Lomé Convention between the African, Caribbean and Pacific (ACP) states (including Botswana) and the EEC was signed in February 1975, and within two weeks Botswana had submitted a portfolio of project outlines. Despite this promptness, there was a delay of over a year before the Commission was able to field a programming mission to announce the country ceiling (22 million units of account or US $28.9 million) and agree on as list of projects for financing. These covered a broad range of sectors, but the delay in establishing the programme was an augury of worse to come, for by the beginning of negotiations for the successor to the Lomé Convention in 1978, only 14 per cent of the funds available had been disbursed.[395]

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393 IBID, P165

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395 IBID, P165

4. DONOR MANAGEMENT

By the middle of the 1970s the diversification of Botswana's sources of external assistance was thus well under way. The additional finance, when added to growing local resources, made possible a rapid increase in the level of public sector development spending. It also brought with it a greater complexity to the management of the Development Budget.[396]

In the early days aid administration was simple. With only one major donor, all the implementing departments knew the rules and how to get the most out of them. Two things were important. First, to ensure that the total amount of capital aid available in the year was spent (otherwise it would be lost). Secondly, to follow the rules laid down on procurement. The first gave an immediacy to project implementation. Departments knew that their performance in carrying out their projects on time was the critical factor in deciding whether they would have an increased share of next year's funds, or more immediately, any supplementary finance that might be allocated to Botswana in the last quarter of the financial year. It has been argued that this emphasis on expenditure created bad habits and was at the expense of more carefully thought-out projects, and, worst of all, skewed expenditure in favour of the fast spenders. These tendencies undoubtedly existed but were more than offset by the positive incentives it gave to implementation performance and the focusing of attention on development. Botswana's ability in later years, when aid flows increased, to handle the greater flow of projects is primarily due to the habits

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learned, and the system of project monitoring developed, in the early days of British aid.[397]

In the early days, procurement rules were quickly learned. Any materials purchased with British aid had to originate either in Botswana or the United Kingdom. There were, however, important exceptions. In the first place, with few building materials produced locally, essentials such as cement, window and door frames, conduit piping, electrical fittings and corrugated roofing sheets had to be imported. It was clearly impractical to ship these supplies from the United Kingdom. Not only would this add to the cost, but delays would occur so that administration of contracts would have become almost impossible. The United Kingdom authorities quickly accepted this point, and a standing waiver for the purchase of general building supplies from South Africa was approved for all projects. Waivers were also granted for certain categories of vehicles that were assembled in South Africa from UK manufactured components, and for equipment items that were substantially more expensive to obtain from the UK, or on which for technical reasons the government had already standardized on a third country source. Aid officials of the Ministry of Overseas Development were under constant pressure, on the one side from the UK Department of Trade to increase the British content of aid spending, and on the other from Botswana to widen the scope of existing waivers. Yet despite these conflicting pressures, the aid programme was operated with commendable flexibility.[398]

As sources were diversified, matters became more complicated. Both Norway and Sweden readily accepted

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397 IBID, P166

398 IBID, P166

the need to buy essential supplies from South Africa, and were themselves under less balance of payments pressure to maximize domestic procurement. Their aid was therefore completely untied. Other donors, either through a failure to perceive the special position of the BLS countries, or, more frequently, because of restrictions imposed on the aid agency by other arms of government, were not able to take such a pragmatic line, and the usefulness of their aid was thereby diminished. USAID had an elaborate system of codes that listed the third countries eligible for procurement. In practice the ones that could supply were no more accessible than America, and little use could be made of them. Canada for a long while required 75 per cent Canadian procurement which ruled out most projects except consultancy services. The European Development Fund, while appearing in the text of the Lomé Convention to have a flexible approach, ended up applying one of the most impractical waiver systems of all.[399]

The different characteristics of donors clearly influenced the selection of projects and how they were implemented. The policy adopted by the government was to match projects with donors in a way that minimized implementation difficulties, while at the same time trying to retain priorities and to maximize the availability of external resources. How successfully this was done, and some of the unforeseen side effects is discussed below. In the meantime it is worth setting out the main reasons why the international community was so keen to increase aid flows to Botswana.[400]

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5. THE ATTRACTIONS OF BOTSWANA TO AID DONORS

There were a number of reasons why Botswana in the 1970s was an attractive place for the aid agencies. At the beginning of the period Botswana was unquestionably a poor country, with a per capita income level that qualified the country as one of the least developed. Yet unlike other low income countries once the mineral possibilities were perceived, Botswana offered the prospects of rapid growth. This provided two stimuli: first, the opportunity to participate in the government component of the Shashe Project, seen as critical to that project's success; second, an opportunity to help Botswana with the social, physical and administrative infrastructure that would become even more necessary as mineral-led growth accelerated. The growth potential also meant that Botswana seemed very likely to have the recurrent revenues necessary to maintain the schools, roads, clinics and other schemes that the donor money made possible.[401]

Next, Botswana was quick to establish a routine of planning that led to the production of clear and straightforward development plans in which it was easy to identify the policies of the government and the projects that needed financing. At independence Botswana issued the Transitional Plan for Social and Economic Development, covering the period 1966-8. This was followed by the National Development Plan 1968-73, the first of a series of five year plans, prepared on a rolling basis every two to three years. These plans, moreover, were not prepared in a separate planning commission, detached from the rest of government, but jointly by the planners and the executing departments.

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Consequently, the resulting sectoral programmes had an operational reality that the donor agencies appreciated.[402]

The ability to prepare effective development plans was matched by a capacity to implement that was unusual at such an early state of development. This advantage was probably more important in the eyes of the donors than the expertise in planning, although both stemmed from the importance given to development by the political leadership. In the clamour for a greater flow of resources from the rich countries to the poor, the point is generally overlooked that poor countries can be inefficient utilizers of the existing flows, inefficient, that is, in the eyes of donor agencies. Aid agencies, irrespective of whether their funds are grudgingly supplied by a government more concerned about domestic priorities, or are striving to disburse a target proportion of a rising GDP, are embarrassed by a failure of developing country governments to spend funds that have been approved. Consequently Botswana's ability not only to spend fully the amounts available under the UK aid programme in the early years, but to absorb at short notice supplementary allocations, resulted in additional aid, an effect that has not been fully appreciated. So not only was Botswana a country that met the normal criteria for aid worthiness, it also appeared able to spend the additional funds agencies provided. This it was able to do in an atmosphere that was remarkably free from corruption and dud projects.[403]

Political factors, too, were important. First, the political philosophy of the country's leadership

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402 IBID, P167

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translated into a real commitment to democratic freedoms and the rule of law that few other developing countries could match. This in turn led to policies for development that were broad based, and (at least in intent) refreshingly free from the modern sector biases found in many comparable countries. Next, the geopolitical position of Botswana, although it added a dimension of vulnerability to the county's future, gave an extra reason for assisting Botswana. If it was not possible for Western countries to alter the apartheid policies of South Africa, then contributing to an independent multiracial democratic state at its borders was a partly compensating alternative. For some donors this interest in Botswana in a wider setting did influence how they viewed domestic policies, and this is discussed in a later section.[404]

Finally, there was an intangible factor which although perhaps not apparent to new donors, did affect the aid relationship as it matured. This was the ability of Botswana government officials to establish excellent working relationships with those in the agencies that were responsible for determining policies towards Botswana. The result of this was that Botswana became a special case and rules that otherwise would have remained inviolable were bent in Botswana's favour. Some of the best examples come from the early days of the United Kingdom capital assistance. When supplementary loans were made available for spending in the last quarter of the financial year, short cuts were taken in both the preparation and approval of project memoranda based largely on the understanding between the officials of the two sides involved. The same also applied to waiver requests. In part this was due to the long association of the former colonial power and

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the continuity of individual contact. But it was also due to a genuine identification of agency staff with the development aspirations of the country, shared by other institutions like the World Bank, the Canadian aid agency (CIDA) and the Scandinavian agencies.[405]

6. DONOR INFLUENCE

The diversification of aid sources and the increase in the total amount available did place a burden on the administrative machinery of the government. At Independence a separate Ministry of Development had been formed, but in 1970 this was fused with the Ministry of Finance to create a powerful Ministry of Finance and Development Planning with the then Vice-President, Dr Masire, as its Minister. For most of the period aid co-ordination was the responsibility of the Division of Economic Affairs (corresponding to the former Ministry of Development), which was also responsible for plan preparation, project preparation and evaluation. Latterly the aid co-ordination role was shared with the budget section of the joint ministry. Aid relations took up a major portion of the time of officials in the division, and it may be asked whether a preoccupation with aid donors was not at the expense of longer term planning and policy activities.[406]

Several answers may be given to this point. First, for much of the period external finance was essential if the development programme was to go ahead, and, as explained below, the co-ordination of donors critically affects the rate of plan implementation. Secondly,

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there is little evidence to substantiate the claim that long term planning was adversely affected. Inevitably, progress on such policies as equitable income distribution, and industrial development has been less than one might hope. But the lack of progress in these areas is common to almost all developing countries, and it is questionable whether a less heavy aid co-ordination role would have made much difference.[407]

One of the reasons why Botswana throughout the period was able to achieve such a good record of aid utilization was the establishment from the outset of a sound monitoring system. When the United Kingdom was the sole source of programme aid, and the chance of supplementary allocations depended on spending performance, a simple but effective monitoring system was established. At regular intervals throughout the year, increasing to monthly in the final quarter, meetings would be held under the chairmanship of the Vice-President to review the implementation performance of development projects. Ministers accompanied by their officials would be called upon to report progress, and to undertake remedial action if bottlenecks were identified. As the aid programme became diversified and the number of projects both grew and became more complex, it proved impossible to handle the entire development budget in a single plenary session: the review meetings were then handled on an individual ministry basis in more detail, but with longer intervals between reviews.[408]

Such a high inflow of external resources clearly had a major effect on the rate of development in Botswana. Without the amounts made available in the years before

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and after Independence, the attainment of budgetary self sufficiency would have long been delayed; and if the build-up of aid resources had not continued after the end of grant-in-aid, domestic resources would have been woefully inadequate for the high levels of social and physical infrastructure investment that Botswana's circumstances required.[409]

What needs to be examined in greater detail is how the diversity of donors, each with their different philosophies of assistance with different rules and procedures, affected the shape and outcome of the development programme. What was the impact of this massive mobilization of external resources on domestic policy? To what extent did the terms of the aid affect the choice of projects, and how much leverage was applied?[410]

It is easiest to eliminate those aspects of the aid relationship that had little effect on the choice of projects and the outcome of the development programme. Aid funds were offered to Botswana under a range of different financial terms, but all loans had total repayment periods (that is, including the grace periods) of more than twenty-five years. A large proportion of the outstanding external debt consisted of IBRD borrowings (44 per cent in March 1979) which had long repayment periods but commercial rates of interest, and were mostly denominated in the currencies of the surplus countries. Other borrowings, though nominally on concessionary terms, required repayment in hard currencies like the Deutschmark. To what extent did the terms of borrowing affect either the willingness of the government to accept the loans or the uses to which the funds were put?[411]

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The short answer is: surprisingly little. With all donor financing on concessional terms, debt service was not normally a significant consideration. Furthermore, as part of a global effort to ease the burden of debt servicing, a number of Western donors retrospectively converted past loans into grants. This was welcomed in Botswana, but with a debt service ratio of about 4 per cent, and debt servicing never more than about 8 per cent of the recurrent budget, it was not a critical problem. Interestingly, as Botswana's per capita income rose, the terms of external financing if anything became softer, partly for compositional reasons and partly because of a worldwide trend towards increasing the concessional element in aid. In the early years the emphasis was on increasing the volume of external assistance, and the terms of new aid (seldom onerous) was never a serious factor. And with such a favourable time profile for its borrowings, throughout the period Botswana could afford to take a macro view on its borrowings.[412]

In the future, however, Botswana may have to rely more on near-commercial borrowings such as official export credits, and on fully commercial credit, for example from the eurocurrency markets. The country's first ever large-scale commercial loan, for $45 million from a consortium of banks, was negotiated in 1978, although it had not been drawn on by the end of 1979. The private sector, notably the copper-nickel mining company, has large external debts on commercial terms; although these do not affect the government directly, they do affect it indirectly by postponing the taxation of profits.[413]

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A potentially greater influence on poorer countries' development strategies is the aid philosophies of donors and their preference for projects to support. Most agencies stress that their assistance is guided by the development priorities of the recipient country. The Lomé Convention, for example, talks about the indicative programme being drawn up by 'mutual agreement', with a formal exchange of views between the European Economic Community and the ACP state to 'enable the ACP state to set out its development policy and priorities'. The Scandinavian agencies follow this approach as well, and international institutions like the World Bank are at pains to explain that they exist to respond to, not set, the priorities of the poorer nations. Yet on the other side the agencies themselves have development preferences, which tend to follow the current fashion in development thinking. In the 1950s, when development aid was seen as creating the take-off conditions for sustained growth, agencies liked large infrastructure and industrial projects. There was also a time when investment in education was seen as the key to unleashing the development process; and in the 1960s Botswana found it impossible to gain the interest of one major donor except with regional proposals. In the present decade the emphasis has been on rural development, income distribution and the share of benefits to the poor, with the World Bank in particular being concerned with the plight of the poor both in the rural areas and in the rapidly expanding cities of the Third World.

To workers in the field, with daily contact with these problems, it would be excusable if the successive highlighting of different aspects of underdevelopment by the agencies were greeted with some cynicism. The agencies, of course, have another constituency, the parliaments and taxpayers in the developed countries; and opponents of aid have been quick to criticize the failures of past policies. Nor have developing country governments necessarily followed enlightened policies themselves; for example, they have pressed hard for the financing of wasteful prestige projects.[414]

Yet it must be asked whether donor pressure is productive in the long run. For a start it is questionable whether the approach works, and when it does there can be some harmful side effects. It works something like this. The representatives of a new donor come into town and announce that they would like to assist the development of the country with an annual aid programme of X million dollars. 'Give us your highest priority projects' they say, and the ritual of selling the projects begins. Overlooked are the considerations that, first, while most governments have a general view on what is most urgent, there is no systematic ranking of projects. Theoretically this could be done by calculating internal rates of return, but no developing country government could or should afford the time for such an exercise. The project evaluation techniques of the textbooks are employed mainly to satisfy donor requirements for individual projects (that are probably going to be financed anyway). Secondly, to the extent that they have been identified, the highest priority projects are in the pipeline for an earlier donor. Finally, even if the highest priority projects were identified and available, it might be better for reasons of procedures and fungibility to finance them with non-donor funds if these are available.[415]

The fungibility argument runs as follows. A donor who wishes to influence the composition of the development

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programme should not rush for the priority projects. Whether he or someone else does it, they will be financed anyway. Donor finance then simply releases funds for other projects - of which the donor might, or might not, approve. Instead the donor should concentrate on the marginal projects where his influence on what he does or does not go ahead might be more effective.[416]

Looking back, then, on Botswana's experience with a multiplicity of donors, the answer is that probably the preferences of individual donors had relatively little effect overall on the composition of the development programme. There were certainly times when a deliberate effort was made to give a donor the type of project he wanted, particularly when the aid relationship was a new one, and the government was keen to build up the programme. But as long as there were other donors who were prepared to accept a different blend of projects, and as long as there were domestic resources available to finance the important but unappealing schemes (such as government infrastructure), the overall composition of the development programme was not really affected. It may, of course, be necessary to exert this sort of leverage in a country that is seriously neglecting important development areas, but in a country that prided itself on having a balanced development programme (on which the donors agreed), the result of such activities is likely to be a waste of many people's time on both sides.[417]

The project preferences of donors are likely, however, to affect the outcome of the development programme in a

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way that is not generally seen. From the point of view of the people co-ordinating the development programme within the government, the easiest type of money to handle is the one that carries the fewest strings. So the best kind of finance is domestic funds. Approval of the project is an internal process, far faster than the donor's clearance, and there are no restrictions other than the established rules of financial control governing the use of the funds. Donor finance comes with a baggage of procurement, tendering, disbursement, accounting and reporting requirements that can become quite burdensome in a developing country where shortage of administrative skills is one of the greatest bottlenecks. Some of the more advanced donors have realized this and their procedures are commendably simple and adapted to local conditions. British and Scandinavian aid has always been clear on this matter. Most other agencies have made progress with simplifying their procedures and adapting them to better local conditions.[418]

Yet the very priority areas that the donors have been stressing, rural development and the poor, are ones where it is more difficult to design delivery mechanisms and implementation success is less certain. A major highway is designed and supervised by international consultants who can handle most of the special procedures with relatively little administrative cost to the recipient. A village water supply scheme dealing in small units and dependent on local initiatives is a fragile affair by comparison and a lighter touch by the aid agency is essential. Some recognize this but many are still bound by the rigidity of their procedures (sometimes externally imposed); in other cases there is a lack of understanding of

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conditions on the ground. By insisting on projects which are in any case the most difficult to identify and implement, the donors may, therefore, actually slow down development spending in precisely those areas which both they and the government would like to emphasize.[419]

In some well known cases there was a pronounced cost to using donor money. The implementation of Broadhurst II, a project on which the next stage of Gaborone's expansion depended, became critically delayed by unforeseen evaluation, tendering and procurement delays on the part of the European Development Fund which had agreed to finance the water supply. Two similar village water supply schemes proceeded at different rates because one donor insisted on inspecting each village plant before its installation. The other was content with an annual evaluation after installation was completed.[420]

Yet on balance, Botswana has been remarkably free from this sort of difficulty. There were several reasons for this. First, the largest programme donor during this time, Sweden, arrived quite early on the scene, had incorporated into its programme some large rural development projects, and proved to be the most flexible of all external sources. Secondly, as the programme expanded a policy was evolved in the Ministry of Finance and Development Planning of giving the donors not necessarily the projects that they wanted but the projects that their procedures allowed them best to finance. This is not to suggest that the allocation of projects was tightly controlled and planned; it was a looser arrangement with give and take

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between the executing departments (who wanted finance for their projects but were not always aware how difficult their life might become if the wrong choice was made), the Ministry of Finance and Development Planning and the aid agencies. Because of the close working relationship, already mentioned, that grew up over the years between government officials and the local representatives of the agencies, much of this was done by mutual agreement.[421]

7. THE IMPACT OF TECHNICAL ASSISTANCE

Virtually all of the bilateral donors, and the United Nations Development Programme (UNDP), provided Botswana with large amounts of technical assistance, in the form of consultants, advisers and executive personnel holding established posts at the technical or administrative level. Some programmes were fully funded. Others like the United Kingdom's OSAS (Overseas Service Aid Scheme) programme supplemented the salaries of expatriate staff on government of Botswana contracts. In addition there were a large number of third country nationals occupying mainly middle level positions, directly recruited by the government. One donor, with unusual flexibility, even provided funds to finance key people in the latter category. Just as capital aid was being diversified the same process was happening with technical assistance personnel, although the numbers provided by the United Kingdom were so much in excess of other nationalities that the relative shift was much less. The need for such large numbers of foreign personnel was clear. Because of the lack of investment in education in colonial times, at Independence Botswana

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was in critical need of the skills to manage development. And as the pace of change accelerated, the manpower gap grew. Although manpower projections showed that investments in education and training would close the gap in the 1980s, Botswana in the first decade of Independence had no alternative but to expand considerably the numbers of expatriate staff in the public sector.[422]

There was, of course, an implicit trade-off between the pace at which the government could tackle the challenges of development and the rate at which localization could be achieved. In 1966 there was no doubt in the minds of ministers that to tackle the agenda that the government plan set forth required an expansion for a period in the numbers of expatriate personnel. The long-run plan for localization laid down in the first National Development Plan was self-sufficiency in higher level manpower for the whole economy by 1990, and the localization of all posts of a non-specialized administrative nature by 1972, with full localization for the public sector by the early 1980s. Such was the determination to break out of the stagnancy of the colonial period that considerations of localization were secondary. For the latter to be achieved, there needed to be substantial investment in education, and in other sectors to generate the revenues that would pay for the teachers and extension workers that were the front rank of the government's development strategy. No other route existed. In the early days a trade-off between alternative rates of growth and localization was never seriously debated: the key objective was to get the growth process started.[423]

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However, in 1973, when the country broke free from grant-in-aid and faced the prospects of larger surpluses in the future, a clear choice faced policy makers. Implementation capacity rather than finance was the new bottleneck. There was a risk that with the running down of construction activity on the Shashe project, the overall level of development spending would fall, resulting in a partially completed third National Development Plan and the temptation to use the new domestic revenues for public sector consumption, not investment. Accordingly, approaches were made to the agencies that provided technical assistance to raise the ceilings on their technical assistance, a request that was generally met.[424]

Thus a further growth in the numbers of technical assistance personnel took place, so that by 1978 there were more expatriate personnel serving in the public sector than at any time previously. At the same time, of course, the public sector was both growing very rapidly and making solid progress with localization, although it was increasingly clear that the targets of the first National Development Plan were unachievable.[425]

For most of this period there was little doubt in the mind of the government that the course that was followed was the right one. Outside commentators have generally failed to grasp the depth of feeling Botswana policy makers had about the lack of progress during the colonial period. Given, then, that Botswana's strategy for development did result in a large number of expatriates in the public sector, what were the

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particular consequences on the pattern of development that followed? The obvious one is that the expatriates brought with them technical and managerial skills that made the devising of key policies and the implementation of the government's development programme possible. The government could not have launched the Tribal Grazing Land Programme in the form it took without substantial additional expatriates in land-use planning and other planning capacities, and the same will be true for the new initiatives in dryland farming. The launching of the currency and the operation of the central bank would have been delayed, and it is hard to see how district planning and the channelling of funds for council projects could have been set up without the key role played by the volunteer agencies. Perhaps most important of all, the government would not have been able to play such a calculated hand in its dealings with the mining companies, and the level of revenues would have been less.[426]

But there were costs associated with such a large inflow of foreign personnel, with different living standards and many without experience of developing countries. Undoubtedly there was a powerful demonstration effect that showed through in wage demands and other areas. There were also costs in accommodating expatriates: houses had to be built and places found in English language primary schools. Some of the capital costs were met through aid funds, but a large part devolved on domestic revenues. However, the latter were costs that the growing revenues could accommodate.[427]

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More difficult to assess is the effect the expatriates had on the style of the government. Such an assessment has a high degree of subjectivity, but the following conclusions can be fairly drawn. First, although the personnel provided by the agencies were on the whole well qualified and able, the short period many of them served limited their contribution and made the job of training and localization more difficult. There was less time to find the best possible mode of operation and understand the wider setting into which their activities fitted. In turn this led to a second effect. In any job people tend to bring to it the standards and methods learned in their previous employment. In the early days the bulk of expatriates could show a continuity of service within the country, or in a similar territory where resources were limited and means had to be found for building roads, housing teachers and training farmers within a very tight budget. By later plan periods this continuity had been lost. At the same time projects and policies had become more complex, requiring longer time and more resources to carry them out. They also imposed a greater load on the largely local managerial cadre.[428]

In part this was a natural consequence of Botswana's economic growth, and the increased range of government involvement. Early plans were comprised of the simple and obvious projects that departmental heads had considered for years, in the absence of financial resources to put them into effect. Once the first generation of programmes was completed, the next rank was harder. Most of the key government policies, for example, grazing policy, dryland farming, mineral policy, employment, etc., were mentioned as objectives in the early plans, but it was left to the later period

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for comprehensive policies to be worked out. Yet while the technical expertise the donors provided made these new approaches possible, there is no doubt that the loss of continuity meant that in many cases technical and administrative approaches were devised that were fundamentally out of scale with the supply of indigenous technical and administrative resources.[429]

One example is the consultant who recommends a solution that can only be implemented if further consultants are employed. The history of regulations provides further examples. It will never be possible to more than guess at the cost of this phenomenon. As the economy has grown, it has also become more complex, which in turn has been reflected in the complexity of regulations emanating from the public sector. This process must have been worsened by the use of technical assistance personnel, although the impact cannot be quantified.[430]

8. EXTERNAL PAYMENTS AND DEBT

Mainly in consequence of export earnings rising more rapidly than imports, the overall balance of payments remained strongly in surplus throughout the 1980s, apart from 1981 when a small deficit was recorded. The diamond stockpile sale in 1987 produced a record current account surplus of P1.1 bn ($651 mn) and an overall surplus of P951 bn, almost double that of the preceding year. The current account surplus has subsequently fallen, but was still a healthy P804 mn in 1989, mainly due to an increase in the deficit on the services account, which reached P1.1 bn, according to preliminary figures. The increased net outflow on the

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services account is mainly attributable to a higher level of profit and dividend remittances, especially by Debswana, as well as interest payments on public and private sector external debt. Dividend outflows are estimated to have risen by some 56 per cent in 1989, with the main inflow comprising interest from investment of the country's foreign exchange reserves.[431]

BALANCE OF PAYMENTS
(P mn)

	1984	1985	1986	1987	1988[a]	1989[b]
Merchandise exports fob	879.9	1,384.4	1,601.9	2,663.8	2,686.1	3,660.8
Merchandise imports fob	-757.5	-939.5	-1,143.3	-1,349.7	-1,804.7	-2,147.6
Trade balance	**122.4**	**444.9**	**458.6**	**1,314.1**	**881.4**	**1,513.2**
Exports of services	253.3	306.6	407.0	484.5	561.9	720.3
Imports of services	-494.5	-671.0	-753.4	-989.9	-1,430.6	-1,786.4
Net private transfers	-9.5	-6.0	-4.9	11.4	-29.4	-31.5
Net official transfers	141.5	176.4	215.1	272.8	325.4	388.5
Current account balance	**13.1**	**250.9**	**322.4**	**1,092.9**	**308.7**	**804.1**
Private long term capital	129.3	199.8	187.2	-141.5	237.3	258.6
Private short term capital	13.3	-0.3	47.7	-26.3	24.9	29.0
Government capital	22.8	-13.5	17.0	26.9	13.1	14.9
Banking sector capital	-21.4	52.6	-45.0	-2.0	-10.6	11.6
Capital account balance	**144.0**	**238.6**	**206.9**	**-142.9**	**264.7**	**314.1**
Net errors and omissions	7.5	11.1	36.6	-8.0	124.0	45.5
Valuation adjustments	-	-	-9.9	9.1	518.6	-284.1
Change in reserves (- indicates increase)	-164.6	-500.5	-556.0	-951.1	-1,216.0	-879.5

[a] Revised. [b] Preliminary.

Source: Bank of Botswana, Annual Report.

The capital account has normally offset any weakness on the current account, remaining in surplus apart from 1987. In 1988-89 there were strong inflows of private long term capital, mainly in connection with the Sua Pan project and industrial investments. The overall balance of payments surplus peaked in 1988 at P1.2 bn, although valuation adjustments accounted for a large proportion of the final outcome, as in 1989 when the overall balance remained strongly in surplus. The positive evolution of the payments situation has

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431 THE ECONOMIC INTELLIGENCE UNIT, BOTSWANA, LESOTHO, SWAZILAND, 1990-91 COUNTRY PROFILE, ANNUAL SURVEY OF POLITICAL AND ECONOMIC BACKGROUND, WORLD MICROFILMS PUBLICATIONS LTD, LONDON 1990, P32

enabled the foreign exchange regime to be progressively liberalised and there are now virtually no restrictions on current international transactions.[432]

Botswana's international reserves strengthened significantly in 1985-87, with foreign exchange holdings almost trebling to $2 bn. In 1988 and 1989 there were less spectacular increases, to $2.2 bn and $2.8 bn respectively. Bank of Botswana data show foreign exchange reserves to have reached a record P5.5 bn by the end of 1989, equivalent to 31 months' import cover. With the substantial increase in reserves, the bank adopted a set of guidelines in 1986 for managing these assets so as to maintain a diversified portfolio and maximise returns from high yield securities. Balances at foreign banks increased to 51 per cent of total reserves by December 1987, reflecting a move in the portfolio away from bonds and securities towards term deposits, but these had declined to 41 per cent of total reserves by December 1989.[433]

INTERNATIONAL LIQUIDITY
($ mn)

	1984	1985	1986	1987	1988	1989
Foreign exchange	453.83	758.35	1,161.48	2,012.95	2,217.14	2,791.00
SDRs	8.36	10.65	17.14	21.82	22.59	24.85
IMF reserve position	12.10	14.20	19.06	22.32	18.36	25.26
Total reserves excl. gold	474.29	783.21	1,197.67	2,057.08	2,258.09	2,841.11

Source: IMF, International Financial Statistics.

9. FOREIGN DEBT

Botswana continues to enjoy a very low level of foreign debt, and debt service in 1989 at $77 mn was only 3.8

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per cent of exports of goods and services. The bulk of Botswana's existing debt is to official multilateral creditors, which accounted for $336 mn of the total disbursed long term debt of $512 mn at the end of 1989. There was no recourse to foreign borrowing for payments support until mid-1982 when a eurodollar loan of $30 mn was drawn down, the only time Botswana has used this method of financing its external payments. However, the level of debt service has been gradually increasing and the 1989 repayment obligation was more than double the level of five years earlier. Payments on existing debt will reach a peak of $86.3 mn in 1993, based on commitments as at the end of 1988, but this would only place a strain on the country's finances if there were a significant deterioration in its trading position.[434]

EXTERNAL DEBT
($ mn unless otherwise indicated)

	1984	1985	1986	1987	1988	1989[a]
Total external debt	268	343	390	511	499	515
of which:						
long term debt [b]	263	341	387	507	494	512
short term debt	5	2	3	3	5	3
Public disbursed debt [b]	263	341	387	507	494	512
of which:						
official creditors	233	320	363	475	466	483
multilateral	146	216	258	339	324	336
bilateral	87	104	104	136	142	147
private creditors	30	21	25	33	28	29
Debt service	32	50	45	69	74	77
of which:						
principal	16	29	18	38	39	42
interest	16	21	27	32	35	36
Total external debt/GNP (%)	26.3	38.6	38.2	40.5	38.3	...
Debt service ratio (%)	3.6	5.6	4.3	3.6	4.1	3.8
Short term debt/total external debt(%)	1.9	0.6	0.8	0.6	1.1	0.6
Concessional loans [b]/total external debt (%)	40.4	36.0	31.9	28.2	30.9	31.6
Variable interest rate loans [b]/total external debt (%)	11.9	11.1	13.1	12.9	13.4	13.6
Interest arrears on long term debt	-	-	-	-	2	2

[a] Estimates. [b] Maturity over one year.

Source: World Bank, World Debt Tables.

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10. CONCLUDING REMARKS

There can be little questioning that the overall impact of foreign assistance in Botswana has been a beneficial one. Initially, the role played by British aid from the early 1960s until 1972-3, with both capital, recurrent and technical assistance support, when little other assistance was available, was vitally important, since it enabled Botswana to lay the foundations for future development. Many of the features that attracted later donors are directly traceable to this period. Secondly, the financing of the copper-nickel complex at Selebi-Phikwe by a consortium of donors under the co-ordination of the World Bank was also crucial. Although the profitability of the mine itself has proved a disappointment, its scale both in terms of construction and operation had major indirect effects on government revenues and economic activity as a whole. It established the ability of the government to co-ordinate such a large project, and in turn a determination to apply those management skills in other sectors.[435]

The subsequent diversification to many donors has made management of the development programme more complex, but that complexity has proved in some real sense to be manageable; meanwhile there are other (mainly strategic) advantages to diversity, so that the flow of development finance is now more secure than it was when there was only one donor.[436]

From the above, it is clear that both foreign loans and grants played a major role in the economic development of Botswana. Without official development assistance

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the economic development of Botswana would not have been possible to the level that we know today.

Official development assistance is defined as grants and loans with at least a 25 percent grant element, provided by OECD and OPEC member countries and multilateral agencies, and administered with the aim of promoting development and welfare in the recipient country. IMF loans, other than Trust Fund facilities, are excluded, as is aid from the Eastern Bloc. The value of official development assistance, which includes both loans and grant is well indicated in Table 1.

Important to note, is the role played by the provision of technical assistance in the economic development of Botswana. Virtually all of the bilateral donors as well as the United Nations Development Programme (UNDP) provided Botswana with large amounts of technical assistance in the form of consultants, advisors and executive personnel holding established posts at the technical or administrative level. Some programmes were fully funded. Others, like the United Kingdom's OSAS (Overseas Service Aid Scheme) programme supplemented the salaries of expatriate staff on Government of Botswana contracts. In addition, there was a large number of third country nationals occupying mainly middle level positions, directly recruited by the government.

11. SUMMARY

This chapter investigated the role played by foreign aid in the form of loans and grants in the economic development of Botswana since 1980.

During the years immediately prior to independence a number of economic survey missions had visited the protectorate to assess aid requirements and development prospects. Each of the concluded that the likelihood of achieving a rapid growth of domestic income was negligible, so much so that the Government would be unable to raise sufficient revenue from local sources to cover even its recurrent expenditures within the foreseeable future. By implication, aid would have to be sought to finance not merely the future investment programme, but also to help cover the basic consumption needs of the society. If this aid was not forthcoming, it seemed the Government would have to remain a skeletal institution along colonial lines, with a continued emphasis upon regulatory rather than development functions.

However, in the first four years after 1966 the general level of developmental spending was low. Then in the early 1970s development spending rose dramatically. This was partly because of the construction of the large copper-nickel complex at Selebi-Phikwe and also the Shashe project.

Apart from the Shashe project itself, the government's additional efforts to diversify aid sources were beginning to be successful. Foreign aid came from Sweden, Japan, Norway, USA, UK and West Germany, as well as from multilateral donors.

The chapter also showed that certain donors had their preferences. Most donors, for example, stressed that the recipient selects the projects and, provided there was reasonable justification, implementation has been thought through, and the project can be shown to fit current development strategy, aid money will be forthcoming. However, certain donors, such as Norway and Sweden, had a strong leaning towards rural projects and projects which were expected to benefit the lower income groups in the population.

Also in this chapter, an attempt was made to indicate the attractions of Botswana to aid donors. Once the mineral possibilities were perceived, Botswana offered the prospects of rapid growth. This provided two stimuli: first, the opportunity to participate in the government component of the Shashe project. Second, an opportunity to help with the social, physical and administrative infrastructure that would become even more necessary as mineral-led growth accelerated.

Also covered in this chapter is the question of donor influence. A potentially greater influence on poorer countries' development strategies is the aid philosophies of donors and their preference for projects to support. The impact of technical assistance on the economic development of Botswana was also discussed, as well as the question of external payments and debt.

CHAPTER FOUR:

FOREIGN DIRECT INVESTMENT

1.1 INTRODUCTION

This chapter will examine the role played by foreign direct investment in the economic development of Botswana since 1980. However, before going into detail, we will start by examining the relevance of the theory of direct investment. This will be followed by an analysis of the characteristics of the manufacturing sector in Botswana.

This chapter will also examine the role played by government, policy and incentives in encouraging foreign direct investment in Botswana, as well as the attitude of the government towards the private sector. The chapter will also look into the main objectives of the government's industrial policy and actions taken by the government in creating a favourable environment for foreign investment.

In addition, the chapter will look into the role played by trade agreements, macro-economic policy, trade policy and protection, as well as other policies which were formulated to promote the manufacturing sector. The chapter will also focus on local preferences, financial incentives, Botswana's tax system, licensing arrangements as well as the provision of positive encouragement and advice by the government of Botswana. The question of tariffs as well as the extent of the government's involvement will also be dealt with.

This chapter will also examine the structure and growth of the manufacturing sector and the role played by foreign investment. The chapter will also examine the profile of the manufacturing sector as well as an analysis of the financial assistance programme and its results. The availability and cost of inputs for manufacturing will also be looked into as well as raw materials, packaging, land, labour and services.

The results of the government's policy and prospects for industrialisation will also be looked into, as well as the size of the local market and government tenders. The chapter will also investigate some episodes or cases of manufacturing growth and will end with an analysis of prospects for future foreign manufacturers as well as future trade and international relations.

1.2 INVESTMENT DECISIONS: THE RELEVANCE OF THEORY

In the hope of attracting investment from abroad, with its accompanying technology and management, the governments of African countries, in common with the governments of most developing countries, have offered at various times all sorts of investment incentives. The details vary, but they frequently include tax holidays, accelerated depreciation of fixed assets, the provision of low-cost industrial sites and other measures aimed at reducing costs.[437]

There is a theory behind such cost-reducing incentives, even though the civil servants and politicians involved may not perceive the matter in those terms. The theory in this case is an attractively simple one, namely that if a profitable investment opportunity exists then someone will take advantage of it.[438]

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437 HARVEY, C, (ED) PAPERS ON THE ECONOMY OF BOTSWANA, 1ST EDITION, HEINEMANN EDUCATIONAL BOOKS LTD, LONDON, 1981, P209.

438 IBID, P209

In countries with an adequate local supply of savings, financial intermediaries, technology and skilled manpower (including managers) the theory is quite likely to hold true. African governments are obviously aware that these conditions do not apply to their own economies - indeed, if they did, then the problem of underdevelopment would scarcely exist. So investment incentives are aimed at foreign companies, as the only likely source of investment in a large range of modern manufacturing industry. But it is a serious mistake to assume that the same theory applies to foreign investors, that is, to companies already established in another (almost certainly developed) economy and considering setting up a subsidiary manufacturing plant in a developing country.[439]

All investors are interested in making a profit; but there is a big difference between companies operating entirely within a country, and companies operating across national borders. The latter have a choice as to where they make profits and will normally try and do so where taxes are lowest, where risks are thought to be least and where there is as little danger as possible of not being able to transfer profits - to shareholders or for investment, wherever the world it seems most profitable. If, therefore, foreign companies can make profits by exporting to African countries, they will normally prefer to do so. That way they will continue to make a profit out of selling to an African country without having to invest in what appears to them to be a remote, risky, difficult environment.

Normally, a manufacturer who is already supplying a foreign market will only consider investing in

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439 IBID, P209

manufacturing capacity (as opposed to distribution facilities) if he is threatened with a loss of that market. Such a threat comes either from rival manufacturers or from governments. A rival manufacturer can threaten a competitor's market in any given country by offering to manufacture locally behind tariff protection provided by the government. In that way, one exporter can attempt to capture a larger share of the market by excluding his rivals. Alternatively, a government interested in forcing its import suppliers into manufacturing locally, can itself take the initiative by threatening to exclude those suppliers who continue to supply the market from factories abroad.[440]

There are, of course, other reasons why foreigners may be reluctant to invest in African countries. Wages, although low, may reflect low levels of skill, experience and therefore productivity. Governments, from a distance, appear unstable. Skilled labour is scarce and expensive. There are also the risks of nationalization and exchange controls on the remission of profits. Meanwhile, for most African countries, markets are small, so that the economies of large-scale production are not usually available and the foreign investor may have to change his production methods from those with which he is most familiar.

However, it seems that the desire to supply the market from abroad, for as long as conceivably possible, is the dominant factor. This is neatly illustrated by Kilby's work on Nigeria, because it related mainly to the colonial period when political risks were minimal, and because Nigeria has by African standards an exceptionally large market, with a population some hundred times larger than that of Botswana.[441]

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440 IBID, P210

Kilby has shown that, for a whole range of products, the local market had grown large enough to make local manufacture profitable, while the market continued to be supplied from abroad. This situation continued for many years - in some cases for more than 50 years. Then within a very short period, several manufacturers set up in Nigeria, each protecting his share of the market from the others - hence Kilby's name 'market-protector' for this type of investment.[442]

From the point of view of the foreign investor, this pattern of market-protecting investment is wholly rational. In most cases, that is, where the export market is fairly small, production facilities in the investor's home country will have adequate capacity to supply the export market, in which case building additional capacity abroad is completely unnecessary and indeed will reduce the profitability of existing factories. Where additional production capacity is needed, the risks and problems of investing abroad are unlikely to seem worthwhile, even when such costs as unskilled wages may appear lower. So the manufacturer will prefer to expand his production capacity at home, for continued export.[443]

Furthermore, even when investment abroad becomes necessary in order to protect a company's market share, or desirable in order to try and capture a larger market share, the foreign investor will normally build only last-stage assembly and packaging facilities.

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441 IBID, P210

442 KILBY, P, INDUSTRIALISATION IN AN OPEN ECONOMY: NIGERIA 1945-66, CAMBRIDGE, CAMBRIDGE UNIVERSITY PRESS, 1969, 1ST EDITION, P54

443 HARVEY, C, OP CIT, P210

There are two reasons for this: first, it minimizes the investment and therefore the risk; secondly, it maximises the sale of intermediate inputs by the parent company. At its best (from the investor's point of view) or its worst (from the host country's point of view) a company can protect or increase its share of the market, behind tariff barriers and at a higher selling price, with a minimal investment in bottling, packaging, assembling and labelling, while continuing to supply the greater part of value added from abroad.[444]

Examples of this type of investment are very numerous, although so far, not in Botswana, where the brewery was the first manufacturing investment to be given protection. In Zambia, the Italian Fiat Motor Company set up an assembly plant to put together complete kits imported from Italy, refusing at first to buy even those components which were already being manufactured in Zambia, such as batteries and tyres. Machinery for the factory was also, of course, imported. Another, almost comical example in Zambia was a factory which imported machinery, bottles, labels, and essence of whisky, gin and brandy in order to assemble them and add the only local component - water. There was even talk at one stage of importing Scottish water in order to improve the taste of the whisky, although this was never done.[445]

It is also worth noting that if a company supplies inputs to a local assembly and packaging operation, where it used previously to supply finished products, then it is in a very strong position to supply those inputs at a higher price than if it were selling to a

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444 IBID, P211

445 IBID, P211

third party. This higher price can then be passed on in higher prices, made possible by protection and (very often) the monopoly position given to new industries by governments. Although 'transfer pricing' is a problem wherever associated companies trade across national frontiers, it is obviously a much greater risk in the sort of manufacturing investment, in last stage assembly, being described here.[446]

It remains to be asked what motive an investor can have for investing (in manufacturing) if he is not already exporting to a market, and is not therefore protecting or expanding an existing market. Why, in other words, would a foreign company launch itself in an unknown country, of which it has no previous knowledge, and with (usually) a small market? The answer in most cases has been in order to make a profit out of selling its own, or other people's machines. This strategy requires, however, that the profit or commission realized from the sale of machines is greater than the investor's share of the investment. So the investor seeks some form of partnership with government, or with a government owned development corporation, or he seeks to be financed out of money borrowed from local banks - since otherwise the investor would also have to make a profit out of production in order to recover his money. Thus 'the actual investments made by these firms (machinery merchants) has been very small - typically 10 per cent of the equity, which represents 3-4 per cent of the combined equity - debenture capital commitment'. Clearly it is possible to recover 3-4 per cent of the total capital cost of a project out of the profit margin on machinery sales, and make a large return on the investment as well, especially if capital costs are inflated 'by 100 per cent or more'. This

446 IBID, P211

sort of investment tends to be very unsuccessful from the host country's point of view, since the primary objective of the foreign 'investor' is to make a profit on the sale of machinery rather than from successful production. Alternatively, a management contract based on sales (rather than profits) can be used as a supplement to profits on the sale of machinery, while relieving the investor of responsibility for making a success of the investment.[447]

There are many other types of investment, each with its own rationale. For example, mining investment needs to be analysed quite differently, since it usually involves a large fixed investment and depends, apart from the obvious requirement of identifying something to mine, mainly on estimates of future mineral prices and the need to secure sources of supply.[448]

The main point in the present context is to ask the question, why should any manufacturing company think of investing in a small, remote country in Africa, of which it has no previous experience, if it is not threatened with the loss of a market? The answer is, of course, in order to make a profit. But the crucial subsidiary question is then whether its profit is expected from selling machinery, from selling intermediate inputs, or from the local manufacturing process. Only if the host country can be fairly sure of the answer to these questions will there be a proper understanding of the investor's motives, and therefore reasonable chance of successful negotiation. While it is difficult to make a success of a factory set up by a machinery salesman or machinery merchant, there can be considerable advantages to be derived by host countries

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447 IBID, P211

448 IBID, P212

from market-protecting investments. Those advantages have to be actively sought, though, by monitoring of transfer pricing, by insistence on the use of local inputs where they exist and by many other means. The danger lies in assuming that the building of a factory will automatically result in a positive net flow of benefits.[449]

The negotiating position of a government is quite considerable. Although the foreign firm has control of know-how and management, the host government has in its power the right to give protection and exclusive licence - in other words the local market. Both lose negotiating power once the factory is built: the investor has, if the bargain is a fair one, committed some resources and begun to transfer some of its know-how; the government has granted the market and is usually most unwilling to throw people out of work by closing an unsuccessful factory.[450]

2. BOTSWANA: CHARACTERISTICS OF THE MANUFACTURING SECTOR

At Independence, manufacturing in Botswana was dominated (perhaps 95 per cent of manufacturing value) by the Botswana Meat Commission (BMC) in Lobatse, which is an abattoir producing chilled and frozen de-boned beef for the high-quality international market. As late as 1984/85 the BMC's meat and meat products operations still accounted for 28 per cent of value added and 36 per cent of output from the manufacturing sector, but less than 20 per cent of manufacturing employment. Over the 20 years after Independence a variety of other activities has been developed in

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449 IBID, P212

450 IBID, P212

response to different stimulae. The second largest single establishment (after the BMC) is the Kqalakgadi Brewery in Gaborone, which was established in the mid-1970s. Operations have been established in textiles, food products such as grain milling and bakeries, building supplies (concrete products, metal-working for door and window frames and galvanised iron products, etc.). Traditional village industries, such as beer brewing, have declined in relative importance, while the workshops associated with the mining industry have added a variety of miscellaneous metal working and chemical activities. There are no petroleum refining, cement making, or large metal-working activities. Apart from the BMC, the larger establishments tend to be those which are foreign owned or in partnership with local firms, particularly the Botswana Development Corporation (BDC).[451]

By 1985 the manufacturing sector provided 12.6 per cent of total wage employment in the private and parastatal sector, up from 7.4 per cent in 1975. Manufacturing activities are highly concentrated geographically, with over 60 per cent of all manufacturing jobs in Gaborone and Lobatse in both 1975 and 1985, while half of all manufacturing jobs created in that decade were located in Gaborone.[452]

As mentioned at the outset, one of the things which makes Botswana's manufacturing record of some potential interest is the fact that the real rate of growth of manufacturing value added of 10.8 per cent a year over the 20 years ending in 1985 is among the highest in the world. Figures available for the period 1972-85 show

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451 LEWIS, STEPHEN R. JNR., AND SHARPLEY JENNIFER, 1988, BOTSWANA INDUSTRIALISATION, DISCUSSION PAPER 245, INSTITUTE OF DEVELOPMENT STUDIES, SUSSEX, P7.

452 IBID, P8

that the average annual growth rate of employment in manufacturing was over 11 per cent per year. Botswana's extremely rapid growth of overall GDP meant that, despite the high growth rate of manufacturing, that sector's share of total GDP declined, as shown by national accounts. However, as overall GDP growth was dominated by mining, it is useful to examine manufacturing relative to both the non-mining and agricultural sectors. Since the early 1970s manufacturing has risen from around 8 per cent to over 11 per cent of non-mining GDP and from less than 20 per cent of agricultural GDP to over 150 per cent of agricultural GDP (a calculation affected in part by the drought of the early 1980s). The explanation of the rapid growth rate of manufacturing in absolute terms and a fairly substantial rate of structural change within the non-mining sectors of the economy, would appear to be of some interest.[453]

3. GOVERNMENT POLICY AND INCENTIVES

3.1 ATTITUDES TOWARDS THE PRIVATE SECTOR

Since Independence, the government has always regarded the development of the enterprise sectors of the economy as an activity primarily for the private sector. The government viewed its own role as one of providing infrastructure and services, including basic education and training for the labour force. A basic statement of policy, first given in the <u>Transitional Plan for Social and Economic Development</u> published at Independence in 1966, and repeated with minor changes in all six National Development Plans, read in part:

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453 IBID, P8

> A rationally planned and guided economy is the objective of government policy. However, a balance must be struck where private initiative has ample scope within the general confines laid down by government. It is government's duty to set forth its objectives and priorities, to frame its policies accordingly, and to assist the private sector in every way consistent with the attainment of these goals.
>
> ... Private enterprise will only be interested in investing in Botswana if there is a profit to be made ...... The government's policy will be, in the case of every proposal [for added incentives], to examine the balance of advantages to Botswana; the costs and benefits will be studied, and decisions made on that basis alone.[454]

In 1970 the government established the Botswana Development Corporation to be its operational arm in promoting industrial and commercial development, either in partnership with the private sector or, where private initiative was not forthcoming, on its own. The BDC was established to be a commercial enterprise and to operate on strict commercial lines though with a bias toward projects which would lead to further development within Botswana.[455]

The lack of basic physical and social infrastructure at Independence, as well as the initial dependence on foreign grants to balance the recurrent budget (which caused decisions about government spending to be made in London rather than in Gaborone), meant that the government's efforts in the first decade of

454 IBID, P16

455 IBID, P19

independence were focused primarily on the growth of the public sector. It concentrated on the development of water, roads, communications, basic health services, and, in general, a public sector that could deliver services to the population, especially in the rural areas, where the majority of citizens, and voters resided. In the mid-1970s, attention began to shift within the government toward more active measures to promote the diversification of the economy away from beef and the newly found minerals exports, and to encourage the creation of employment opportunities in manufacturing and other sectors. An extremely comprehensive study of employment policies and a series of policy initiatives in the next few years [Financial Assistance Policy 1982; National Policy on Economic Opportunities 1982] showed the increased attention which government was paying to the development of the manufacturing sector in particular. The protection of local industry clause in the Southern African Customs Union Agreement was first used in 1976; a Local Preference Scheme was introduced in government purchasing and tendering arrangements in 1976; and a variety of additional measures were introduced in the early 1980s to promote particular industries and to provide (with price and quality guarantees) protection from imports for specified industries.[456]

3.2 OBJECTIVES

The main objectives of the government's industrial policy, as described in the Fifth National Development Plan 1979-85, (NDP V) were to: increase the number of worthwhile job opportunities; increase economic independence; diversify the economy; and protect the interests of consumers and workers.[457]

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456 IBID, P19

457 WHITESIDE, A.W.; (ED), INDUSTRIALIZATION AND INVESTMENT

The most recent plan, National Development Plan VI, 1985-90, has more specific policies regarding foreign-owned business. It states:

> During NDP 6 employment creation, rural development, increased citizen participation and national economic independence will continue to guide overall activities in the industry and trade sectors.
>
> Government believes that a free enterprise, market oriented system is more efficient in producing goods and services and is more economical in the use of scarce administrative capacity. The principle means of ownership will continue to be the private sector.
>
> There will be a continuing need for foreign investment especially in those areas where the necessary skills and technologies are not available locally. Therefore government places a great deal of emphasis on maintaining a favourable climate for the investment of private capital.
>
> Botswana's economy is both open and trade oriented. It can be sustained only by a dynamic private sector. Government will continue to encourage foreign investment and skills to strengthen the private sector and stimulate its increased participation in external trade on a global basis.
>
> Trade policy considerations often influence industrial development in Botswana, especially in

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[457] Cont. <u>INCENTIVES IN SOUTHERN AFRICA,</u> UNIVERSITY OF NATAL PRESS, PIETERMARITZBURG, 1ST EDITION, 1989, P45

> the light of its open import regime, and membership of the Southern Africa Custom Union...
>
> Government will adopt a selective approach to promotion of citizen participation in order to ensure a smooth transition to localisation. Joint Ventures between expatriates and citizens will be encouraged in selected commercial activities...
>
> Government will in principle charge industrial users a price which covers the full cost of the infrastructure and services. A policy of general [but time limited] subsidies in the form of FAP will be preferred to the subsidising costs of land, electricity, water etc... Government will participate in projects which are large and of a sensitive or strategic nature.[458]

Government participation is through BDC or other parastatals in certain areas, such as where monopolistic powers could lead to abuses by private companies or where the national or social benefits are not matched by the profit potential.[459]

It is evident that the government aims to encourage private sector development. It recognizes the need for foreign investment, especially in larger, specialized industries for which the necessary capital and technical resources are not available locally. At the same time government has a direct role to play, particularly in areas that are less attractive to private investors. Here foreign investment may occur in the form of participation by foreign aid organizations, or loans from international banks.[460]

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458 BOTSWANA, MINISTRY OF FINANCE AND DEVELOPMENT PLANNING, 1985. SIXTH NATIONAL DEVELOPMENT PLAN, 1985-91, GABERONE, PP242-244

459 WHITESIDE, A.W. OP CIT, P47

The government believes it can assist in the development of manufacturing industry at three levels: by creating a favourable environment - providing essential infrastructure, negotiating advantageous international trade agreements, operating favourable fiscal and monetary policies and licensing arrangements; by positive encouragement and advice - preparing and publishing industry feasibility studies, providing general advice to entrepreneurs, financial aid packages; and by more direct government involvement - such as is provided by the parastatals, Botswana Enterprises Development Unit (BEDU), and Botswana Development Corporation (BDC), and wholly owned enterprises such as Botswana Meat Commission (BMC).[461]

3.3 CREATION OF A FAVOURABLE ENVIRONMENT

The government believes a stable investment climate is more attractive to foreign investors than a range of specific financial incentives. Botswana has an international reputation for being politically stable and of having good financial management, yet at the same time providing liberal allowances for the repatriation of profits by foreign-owned firms. The government has never forcibly taken over a foreign-owned company and accepts that the bulk of the manufacturing industry will be more efficiently run by private enterprise.[462]

Recently a number of manufacturing activities have been reserved for citizen ownership. These are instances

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460 IBID, P47

461 IBID, P48

462 IBID, P48

where there has been local productive capacity and where, consequently, it was less attractive to potential foreign investors. (Foreign manufacturers already participating in these sectors are allowed to continue). Foreign investors are encouraged to form joint venture businesses with Batswana partners, but this is not obligatory.[463]

A number of factors have been identified as being within the government ambit as far as the creation of a favourable environment is concerned.

3.4 TRADE AGREEMENTS

With a population of 1,2 million (1988) many of whom are barely in the money economy, the size of the internal market is a severely limiting factor for manufacturers. For this reason external trade agreements are of crucial importance in attracting manufacturers.

By far the most important of the trade agreements is the Southern African Customs Union (SACU), comprising Botswana, Lesotho, Swaziland and South Africa, which allows virtually unimpeded and free interchange of goods between member states. In addition there are trade agreements with Zimbabwe and Malawi in which it is stated that a given percentage of the cost of an item traded must pertain to local inputs. The percentage for Malawi is 25 per cent, but that for Zimbabwe has recently been reduced from 25 per cent to 20 per cent. More than half of all regional trade with Africa (excluding South Africa) is with Zimbabwe.[464]

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463 IBID, P48

464 IBID, P48

Botswana has observer status with the Preferential Trade Area for Eastern and Southern Africa, but has not committed herself to joining.

Botswana's goods enjoy preferential access to the European Community (EC) through the Lomé Convention. These concessions on the import tariffs of the EC have been very important in facilitating sales of beef, but also apply to a range of other foodstuffs and manufactured products. Botswana competes for this market with a number of developing countries, and has to find products it can produce efficiently and which can bear transport costs.[465]

Generally, to qualify for a certificate of Botswana origin, the manufacturer must show that: at least 25 per cent of the production costs of the goods is represented by materials produced, and labour performed, in Botswana (for Zimbabwe, 20 per cent); and the last process in the production or manufacture of the goods must have taken place in Botswana.

In the calculation of production costs, the following items may be included: the cost to the manufacturer of all materials; manufacturing wages and salaries; direct manufacturing expenses; the cost of inside containers (the immediate wrappings in which the goods are necessarily contained); other expenses incidental to the manufacturing operation at the discretion of the Director of Customs and Excise; and overhead factory expenses.[466]

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465 IBID, P49

466 IBID, P49

3.5 MACROECONOMIC POLICY

Under macroeconomic policies we include budgetary or fiscal policy (including counter-cyclical policy), monetary policy (including money, credit and interest rates), exchange rate policy and wages/income policy.

At the time of Independence, Botswana had no opportunity to exercise any kind of independent macroeconomic policy. It was still in a monetary area using South Africa's currency, and it had no independent budgetary policy, since government expenditure plans had to be approved by the British government as a condition of receiving annual grant-in-aid. After Independence Botswana gave high priority to developing its own revenue base and achieving 'financial independence'. Through the successful renegotiation of the terms of revenue sharing in the Southern African Customs Union and through revenue from the new mining projects, particularly diamonds, Botswana achieved a position where recurrent costs were fully covered from its own revenue sources in the financial year 1972-73. A significant indication of the government's overall financial policy is that in the same year two special funds were created: the Revenue Stabilisation Fund and the Public Debt Service Fund. The RSF was to provide a vehicle for balancing year-to-year fluctuations in revenue with long term growth in public expenditure and the PDSF was to be invested in domestic projects which would yield a flow of interest and principal repayments to match Botswana's debt service obligations abroad. Financial prudence and a long term view of the budget were early parts of the macro-management system.[467]

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467 LEWIS, STEPHEN R. JNR., AND SHARPLEY JENNIFER, OP CIT, P20

The overall financing requirements of the government budget have always been considerably below the gap between domestic investment and domestic saving. Indeed, after the opening of the Jwaneng diamond mine in 1982 the government budget went into overall surplus (though the Development Plan makes it clear that this surplus would be temporary). Maintaining a growth rate of total government expenditure that could be financed on a long-term basis has been a part of the overall fiscal strategy, and the lower increase in the share of total expenditure than in the share of total revenue in GDP reflects that approach. The large negative figure for net imports of goods and services shown for most years is the result of the substantial role of foreign private financing of mining projects and of many manufacturing ventures which added to the capital inflow provided by foreign loans and grants to the government. However, as compared with many developing countries, Botswana's fiscal policy was not one which added substantially to domestic aggregate demand and created an unsustainable level of imports. The large excesses of imports over exports in some years were a reflection of project financings in the public, private and parastatal sectors, not the result of increased domestic demand brought about by excessive borrowing from the banking sector to hold up general government or private spending.[468]

The story of Botswana's counter-cyclical macroeconomic and budgetary policy is an interesting and extended one.

What Botswana managed to achieve in its overall budgetary stabilisation policy was a rate of growth of government expenditure that fluctuated much less than

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468 IBID, P23

the rate of growth of government revenue, with the consequence that the level of government cash balances at the Central Bank (and, to some extent as a counter-part, the level of foreign exchange reserves) were used as a buffer to absorb differentials in the growth of government revenue and planned spending. Even in its only major balance payments 'crisis' of 1982, Botswana was able to avoid the need to depress domestic demand excessively in order to meet balance of payments constraints. Further, in 1981, the government began a process of making annual wage adjustments in the government sector after consultation with the tripartate consultative National Employment Manpower and Incomes Commission, on which government, trade unions, and employers were represented. Government sector wage rate decisions then became more closely integrated into general budgetary policy, though ad hoc approaches through public service salary commissions were reintroduced in 1985/86.[469]

It is in exchange rate policy that Botswana has been most active in managing its macroeconomic affairs. In 1975 Botswana made a decision to establish its own currency and central bank, and in 1976 the Pula was introduced. From that time on, Botswana had its own independent monetary and exchange rate system and policies. When the Pula was introduced, the government made clear that it intended to use general macroeconomic policies rather than exchange controls or import controls to manage its external balance of payments. Only nine months after introducing the new currency the government made the first of what became a number of adjustments in the exchange rate as a tool of influencing general economic conditions and of macroeconomic policy.[470]

469 IBID, P23

470 IBID, P23

The authorities have tried to maintain a balance in exchange rate policy between using the exchange rate as a tool for influencing the general rate of domestic inflation (given that inflation in southern Africa has been above world levels for most of the last decade) and the need to maintain competitiveness for domestic sectors producing tradeable goods and services (other than mining and beef, both of which would be competitive at a wide range of exchange rates). The fact that, in Botswana, the share of imports in the consumption basket of the poorest groups is higher than that of the richest, has meant that exchange rate policy has important distributional implications as well. Finally, the authorities have considered wage policy and exchange rate policy together, recognising the importance of the need to maintain competitiveness in new economic activities, particularly in manufacturing, both for potential import substituting industries as well as for potential export industries.[471]

Through a variety of measures (discretionary changes in the exchange rate, the adoption and adjustment of the mix of a 'basket' of currencies to which the Pula has been pegged at various times, and combinations of the two devices), Botswana has followed a very active exchange rate management policy. Determining a sensible policy is complicated by the fact that the vast majority of exports are priced in and sold for US dollars (85 per cent in 1985), while the vast majority of imports are priced in and sold for either South African Rand (75 per cent in 1985) or Zimbabwe dollars (about 8 per cent in 1985). Thus, movements in cross exchange rates, over which Botswana has no control and

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471 IBID, P24

which have been very large, complicate the exchange rate management issue considerably.[472]

Botswana has managed to maintain a real effective exchange rate between the Pula and other major trading currencies which has not eroded Botswana's competitive position (indeed, its competitive position has improved in SDR and Zimbabwe markets), and at the same time has been able to maintain a rate of inflation that is substantially less than that of other countries in the region (though above that of the industrial countries).

Botswana's manufacturing sector has been able to operate in a situation of relatively stable competitiveness with respect to the South African Rand, the currency of the principal markets of local competition in the Southern African Customs Union Area.[473]

But competitiveness of manufacturing depends not only on general price/exchange rate movements but also on the levels of wages relative to those in competing countries. Even before it had achieved budgetary independence, and well before it had its own currency , the government recognised that the structure of wages could have an effect not only on the distribution of income but on the rate of growth of employment and the competitiveness of various industries. Following a major consultant's report in 1972, the government adopted a National Policy on Incomes, Employment, Prices and Profits. Two of the principal objectives of this Policy were to limit competitive bidding for scarce skilled citizen manpower at the top of the income distribution by restricting the private and

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472 IBID, P24

473 IBID, P24

parastatal sectors to wage and salary levels set by government, and to hold the levels of unskilled wages to the productivity of labour in traditional agriculture. While there have been important exceptions to this policy at various times, particularly the fact that the level of unskilled wages in government has on several occasions increased substantially relative to those in agriculture, the general outline of the incomes policy remained intact through the mid-1980s.

Most of the increase took place before 1980, and some of it was due to increased localisation of higher-paid positions previously held by expatriates.[474]

Price and profit controls have not been a major policy instrument in Botswana, though undertakings on prices were a major part of the agreement to provide protection for the brewery, the wheat-flour mill, and the soap factory that were established in the second decade of Independence. It appears that these controls were not an adverse factor in the profitability of two of the three enterprises, and they were an essential part of providing protection to the enterprises without increasing prices to consumers. There has never been any attempt to use price controls as a general macroeconomic policy tool.[475]

In terms of domestic money and credit policy, Botswana was relatively inactive between the introduction of the Pula in 1976 and the balance of payments crisis caused by a downturn of the diamond market in 1981-82. In 1981-82, however, the government began a relatively active interest rate management policy, pushing

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474 IBID, P28

475 IBID, P28

interest rates to positive levels in real terms and taking cognisance of the rates available to finance foreign trade transactions in neighbouring countries.

Botswana also introduced restrictions on the growth of credit in 1982, though those were quickly reduced as the corrective measures took effect and the balance of payments position improved in late 1982 and early 1983. Overall, Botswana continued to maintain commercial bank borrowing rates that were positive in real terms.[476]

Botswana's monetary policy was relatively favourable to foreign capital as compared with some other countries. Foreign investors could borrow locally up to P100,000 without matching foreign funds, and could borrow P1 over that amount for every P1 of foreign capital, debt or equity, which the investor brought in. Perhaps most significant because of its absence, Botswana did not use selective credit controls by sector in its dealings with commercial banks.[477]

3.6 TRADE POLICY AND PROTECTION

The three most important elements of foreign trade policy in Botswana are the preferential trading arrangements that Botswana has through its membership of the Southern African Customs Union, the free trade agreement with Zimbabwe, and its preferential trading arrangements with the EEC/ACP countries under the Lome Conventions. Each of these affects major sectors in manufacturing as well as the aggregate economy.[478]

Botswana, Lesotho and Swaziland were joined with South Africa in a Customs Union at the time of the

476 IBID, P28

477 IBID, P28

478 IBID, P30

establishment of the Union of South Africa in 1910. The arrangements provided for duty free movement of goods among the four member countries with the responsibility to set external tariffs resting with the government of South Africa. The three smaller countries received a fixed share of the customs revenue pool each year.[479]

Following their Independence in the 1960s, the three smaller countries renegotiated the arrangements for the Customs Union with South Africa, culminating in an agreement in 1969 which provided both for a new basis for revenue sharing and for a variety of measures designed to make it possible for the smaller countries to both share in the growth of the regional economy and to protect new local industries from competition from other producers within the Customs Union (principally South Africa). There were also a variety of provisions dealing with marketing arrangements for agricultural commodities which permit quantitative restrictions to ensure orderly marketing, but which prohibit the use of such restrictions to protect one country's producers at the expense of another.[480]

The Customs Union arrangements have been significant for Botswana in several respects, not least of which has been the source of revenue provided by the Revenue sharing formula. The Customs Union revenue was a major source of government income in the early 1970s as Botswana's imports rose rapidly during the construction periods of the Orapa diamond mine and the Selebi-Phikwe copper-nickel project. The revenue from the Customs Union was still 15 per cent of government recurrent revenue even in 1985/86, despite the very rapid increase in revenues from diamond mining.[481]

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479 IBID, P30

480 IBID, P30

In addition to the revenue benefits from the Customs Union (these being off-set by the fact that Botswana has to pay protected prices for South African goods) Botswana enjoys a reciprocal advantage on its exports to South Africa. The largest single export item that benefits from this fact is beef from the BMC and by-products of cattle slaughter, but there are increasing numbers of other manufactured goods exported to South Africa. In addition, the Customs Union also provides by way of international agreement, free rights of transit for Botswana traffic destined to and from world markets via South African routes. In view of the transit difficulties which have been experienced by other countries in the region, notably Zambia and Zimbabwe, this benefit is of considerable importance to Botswana.[482]

Under the provisions of the Customs Union Agreement, any of the BLS countries can provide for 'additional duties' to be levied on imports from any source, including South Africa, into their territory to provide an additional price advantage for a period of up to seven years. The revenue collected by the additional duty is paid into a common customs pool, rather than to the treasury of the government imposing the duty. This provision places a serious penalty on the protection of any industry which would provide only a small share of the consumption in the local market, since higher payments by consumers would go to the common customs pool rather than representing a transfer within the economy of the imposing country, as would be the case in a normal protective tariff situation.[483]

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481 IBID, P30

482 IBID, P31

483 IBID, P31

One significant difficulty with the Customs Union arrangements is that the South African market itself is highly regulated, with protected import substituting industries subject to 'rationalisation' by the authorities, meaning that a limited number of producers may be given permission to supply the protected domestic market. On several occasions producers in the BLS countries have been blocked from exporting to South Africa on the basis of these 'rationalisation' arrangements.[484]

Finally, the Customs Union arrangements provide a framework under which Botswana can discuss matters of trade and commercial policy with its most important trading partner. Regular meetings at the technical level provide an opportunity to work out arrangements to overcome practical difficulties which arise in a variety of commercial transactions, and these regular meetings have also provided opportunities for Botswana to take some of the initiatives in providing modest additional protection for Botswana's domestic industries.[485]

Trade with Zimbabwe has fluctuated over the years, but in the mid-1980s it constituted approximately eight per cent of Botswana's imports and four per cent of Botswana's exports. The free trade arrangements with Zimbabwe predate Independence in both countries, and therefore also predate the renegotiation of the Southern African Customs Union Agreement in 1969. As a result, Zimbabwe's exports to Botswana are duty free (though they have been subject to temporary import surcharges imposed by South Africa from time to time).

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484 IBID, P31

485 IBID, P31

This means that Zimbabwe has access to a portion of the Southern African Customs Union market and is able to sell its exports in Botswana at prices that are protected by the Customs Union's external tariff. At the same time, Botswana is able to accrue revenue from the Customs Union revenue sharing formula on those imports.[486]

Following the Independence of Zimbabwe in 1980, there were several developments which began to inhibit the flow of trade between the two countries. A number of manufacturing investors moved from Zimbabwe to Botswana, some apparently, to take advantage of differentials in the rules of origin for determining duty free importation of goods into Botswana from Zimbabwe and into Zimbabwe from the common customs area. In addition, as Zimbabwe moved into somewhat severe balance of payments difficulties, the authorities in Zimbabwe began to impose import quotas against Botswana's exports. Zimbabwe also began to 'dump' a number of products, including steel door and window frames, on the Botswana market, using South African steel which was being sold in Zimbabwe (a non-Customs Union country) at lower prices than the same steel was being sold in Botswana (a Customs Union country).[487]

While at the time of Zimbabwe's Independence it had been hoped that there could be a large increase in trade between Botswana and Zimbabwe, a number of difficulties have interfered with this trade. After a substantial increase of exports from Botswana to Zimbabwe in 1981 and 1982 (reaching a high of 13 per cent of total exports), there was a large drop

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486 IBID, P32

487 IBID, P32

following the imposition of controls by Zimbabwe on imports from Botswana, particularly in the textile industries.

Zimbabwe has been attempting to raise the local content requirements that qualify for duty free importation into Zimbabwe, and this would reduce the volume of Botswana's exports that could enter Zimbabwe's markets.[488]

The third important set of trading arrangements which affect Botswana's exports are the privileged access Botswana has to the European Community markets through the Lome arrangements. The most important single benefit comes from the fact that Botswana's beef exports to the European Community enjoy a 90 per cent abatement of the variable import levy on beef for 17,000 tons of beef each calendar year. Because of the price support nature of the Common Agricultural Policy, European prices are considerably above world market prices in most years, and this abatement of 90 per cent of the variable import levy has been of considerable importance to Botswana's beef exports, in some years adding as much as 15-20 per cent to the value of exports and an even higher percentage to cattle producers (since BMC operates as a non-profit organisation and distributes surplus revenues to its suppliers). Further, the relatively high prices for quality beef in the European market have encouraged the Botswana Meat Commission to increase the degree of processing that is done domestically and, thereby, the value added.[489]

Botswana also receives duty concessions on other exports to the European Community. There are some

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488 IBID, P32

489 IBID, P33

manufactured exports, principally textiles, which have benefited from concessions under the EEC/Lome arrangements, but these have been relatively small to date.[490]

The framework of international agreements, particularly the Customs Union agreement and the free trade agreement with Zimbabwe, have placed general constraints on Botswana's trade policy with regard to protecting local industries through tariffs or quantitative restrictions. Especially in the case of the Customs Union, there are provisions for the application of protective duties and in practice quantitative restrictions of various kinds have been used as well. Nonetheless, the agreements do provide a constraint on the use of such protective devices.[491]

In addition to the constraints provided by the agreements, however, there has generally been an aversion to the use of restrictive trade policies by the Botswana Government. After the renegotiation of the Customs Union agreement in 1969, internal procedures were developed for the evaluation of proposals for protection (few of which have ever been received). The approach taken to the analysis was in line with the statement of policy quoted earlier that 'the costs and benefits will be studied, and decisions made on that basis alone'. Perhaps because farmers and consumers are well represented in Parliament and the Cabinet, there has never been a rush to subsidise manufacturing jobs through raising prices to consumers, though there have frequently been questions raised as to whether the relative lack of restrictive trade policies has been the wisest course of action. Cases

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490 IBID, P33

491 IBID, P33

of both tariff protection and use of quantitative restrictions on imports to provide protection to local producers have always provided for undertakings by the producers to maintain their selling prices at the same level that would prevail for imports from normal sources of supply without payment of any duties. The same principle governed the development of two other policies to promote local manufacturing activity: the Local Preference Scheme and the Financial Assistance Policy.[492]

3.7 OTHER POLICIES TO PROMOTE MANUFACTURING

3.7.1 Local Preferences

Tenders for government contracts are handled by the Central Tender Board, which comes under the Ministry of Finance and Development Planning. Tenders for contracts in excess of P50 000 are classed as public tenders and are advertised in the Government Gazette, the local press, in Southern Africa, and often on an international basis. Contract values below P50 000 are awarded by the board following and informal tender procedure. Manufacturers resident in Botswana are allowed a local preference of 12,5 per cent when tendering for government supply contracts in competition with foreign manufacturers.[493]

3.7.2 Financial Incentives: Financial Assistance Policy

In 1982 the government introduced a new approach, the Financial Assistance Policy, which provides for a system of grants to new and/or expanded business. FAP is provided on a capital grant only basis to citizens

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492 IBID, P33

493 WHITESIDE A.W.,(ED), OP CIT, P52

for small scale projects. For medium scale investments, the investor has two options. 'Automatic' FAP receives a tax holiday for up to five years on a declining share of its profits over five years; a reimbursement of documented wage costs for unskilled and semi-skilled citizen labour, also on a decreasing basis over five years; and a grant for documented off-the-job training costs. This automatic package is available only to new ventures in manufacturing.[494]

The other opportunity for medium scale projects is available on a case-by-case basis for an initial capital grant based on the number of jobs that are expected to be created for citizens, reimbursement of a declining fraction of the wages of unskilled and semi-skilled citizens, grants to reimburse portions of off-the-job training costs, and grants, which decline over time, related to the value of sales from the project regardless of whether they are in export markets or in the domestic market.[495]

Large scale profits (those with investments of P1 m or more) may apply for FAP but may be refused if it appears that the project is already sufficiently profitable without the additional financial assistance.[496]

Applications for financial assistance are analysed according to a set of well publicised criteria, principally that the projects should show a minimum six per cent real rate of return when evaluated at social costs, including a discount for unskilled labour costs and an enhancement for the value of tradeable output

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494 IBID, P34

495 IBID, P34

496 IBID, P34

produced and an enhanced deduction from benefits for the value of tradeable inputs used.[497]

FAP was designed to do a number of things: provide additional cash flow at earlier years of projects, subsidise the use of unskilled and semi-skilled citizen labour, particularly in the first five years of a project, and provide a modest cash subsidy on the basis of total sales, regardless of whether the projects are import substituting or export creating. Since FAP assistance is limited to manufacturing and to non-cattle agriculture, and since the parameters involved in analysing projects provide a premium for import substitution and exporting, FAP is to some degree a substitute for protection via tariffs or quantitative restrictions. In the government paper which introduced the Financial Assistance Policy in 1982, it was stated that 'the same criteria for analysis would be applied to applications for protection under the Customs Union'. Thus, the Financial Assistance Policy was intended not only to be a specific instrument but also to establish the general rules by which costs and benefits would be weighted in judging other forms of protection or subsidy to local ventures.[498]

A variety of other policies and actions of the government have affected the incentives facing the manufacturing sector, some positively and others negatively. Some have clear counterparts in other countries, and others may be unique to Botswana. With significant exceptions, Botswana has not pursued a policy of negotiating arrangements with individual foreign (or domestic) investors on the terms under which they would undertake projects. The Working Group

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497 IBID, P34

498 IBID, P35

which recommended the introduction of FAP rejected proposals for subsidising water and power (which are priced at full economic cost including replacement cost of capital in urban areas) as well as other specific subsidies that had been proposed from time to time. Thus, the overall system of incentives facing the manufacturing sector is relatively even among different types of sectors (e.g. any new project is eligible for assistance from FAP).[499]

3.7.3 The Tax System

The income tax system inherited at Independence was revised in 1972 and has had a number of modest changes since then. The individual income tax is of the usual type found in English-speaking countries, with a basic exemption for single or married taxpayers (no exemptions for children) and a rising marginal tax rate structure which moved fairly quickly through the middle and upper-middle income ranges. In the late 1970s and early 1980s, individuals in management or professional positions in the private sector were likely to be in brackets with a marginal rate in excess of 50 per cent.[500]

In the late 1970s a tax free housing allowance for civil servants was abolished, and the economic value of free or subsidised housing was made subject to tax for all individuals. For expatriate employees, who constitute a large share of the management and technical personnel in the private sector in Botswana, the increase in tax was very large. Most companies, who recruit on an opportunity cost basis with other countries in the region, 'grossed up' the incomes of

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499 IBID, P35

500 IBID, P35

their employees to cover the cost of the tax (as well as the tax on the gross-up). As a result, unit costs of senior expatriate personnel rose dramatically. The view of the private sector was that they would prefer to have a higher rate of corporate tax than the combination of high marginal rates in the individual tax and the taxation of housing benefits. How much investment, if any, was actually lost through this disincentive is unknown, but the issue had an effect on the 'climate' for investment in Botswana from the late 1970s through the mid-1980s.[501]

The company tax is relatively straightforward in Botswana and the rate (initially 30 per cent and raised in the late 1970s to 35 per cent) is low compared with other countries in the region. From the modification of the Income Tax in 1973 through the adoption of the Financial Assistance Policy in 1982, investment allowances permitted accelerated depreciation of capital in manufacturing. During the discussion of FAP the government concluded that accelerated depreciation was encouraging capital intensity of production unnecessarily, and it was dropped from the law. Provisions under FAP relate capital grants to numbers of jobs created and provide grants in the first five years of production related both to employment and to sales, and provide a partial tax holiday under 'automatic' FAP. The law allows 'Development Approval Orders' which can provide special tax treatment for particular enterprises or classes of expenditure, but little use has been made of the possibility. The only other significant factor in income tax that might affect manufacturing is that 200 per cent of training expenditures can be deducted from taxable income, thus providing (at the 35 per cent rate) a 70 per cent effective subsidy from government for such spending.[502]

501 IBID, P36

A number of other elements of the 'investment climate' in Botswana involve government procedures or regulations. The private sector had complained for some years of the unfavourable 'climate' for investors, which included everything from the relatively high charges for power and water to the difficulties in finding housing for employees and the obstruction of various licensing procedures. While the physical scarcity of land and housing appear to be of some importance in limiting the rate of manufacturing growth, there is no hard evidence that the other elements in the 'investment climate' have had a measurable effect on the growth of the sector.[503]

3.7.4 Licensing Arrangements

All manufacturers who propose employing ten or more people, or use machinery of 18kva, must first obtain a manufacturer's licence from the Ministry of Commerce and Industry. The purpose of this licensing is to identify all but small and informal manufacturers for subsequent gathering of statistical data; to enable the Ministry to advise on potential business operations, the level of production in Botswana or neighbouring countries, or to refuse or restrict a new venture where the production may be at a level where an additional manufacturer will cause more harm than good; and to enable other producers, or even the general public, to lodge complaints, since the application must be placed in the Government Gazette.[504]

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502 IBID, P37

503 IBID, P38

504 WHITESIDE, A.W,(ED) OP CIT, P50

3.7.5 Positive Encouragement and Advice

The government recognises that as well as providing a good investment and business climate, positive assistance and encouragement will also do much to promote the manufacturing sector and foreign investment. It has created a wide range of institutions and programmes to promote and assist the development of industry. Some are specifically to help Botswana with small scale businesses (Business Advisory Services, 'Tswelelo', and 'PFP' - Partnership for Productivity; also 'BEDU' - Botswana Enterprises Development Unit, although the last named has now introduced a scheme for joint ventures with foreign entrepreneurs). Some are also for rural areas (the Rural Industrial Officer cadre, 'Rural Industries Promotions' and the 'Botswana Technology Centre').[505]

Positive encouragement for the foreign investor comes from a package of financial incentives, the Financial Assistance Policy, which can actually provide monetary assistance. In addition, the government encourages manufacturers by providing for local preference on tenders and has the ability to provide tariff protection. The Ministry of Commerce and Industry has sponsored feasibility studies for a range of manufactured items. These have included the production of: coal briquettes, egg boxes, toilet rolls, wooden pallets, injection-moulded plastic products, floor tiles, refined tallow for the textile industry, milk, manhole covers, spiced venison, railway brake shoes, biltong, buttons made from horn, recycled oil, red clay bricks, hydrated lime, refined salt, potash and canned tripe. The list is continually being added to.[506]

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505 IBID, P50

506 IBID, P51

Several of the studies have shown that the manufacture of these products is unlikely to be successful in Botswana. This is usually because of the expense of raw materials, (including packaging, for bottled or canned goods), the high cost per unit of production with a small plant for the local market (e.g. glass bottle production), or the difficulty of exporting profitably in the case of a larger plant. The Botswana Development Corporation has carried out its own studies, and often come to the same conclusions.[507]

Finally and most important is the Trade and Investment Promotion Agency (TIPA), which was established in 1985 in the Ministry of Commerce and Industry. Its function is to promote investment possibilities in the country, and to provide a one-stop service to assist prospective entrepreneurs in the setting up of their businesses. The scope is intentionally vague. Although the staff make no promises at having to hand all the information, their help is a welcome change from the normal bureaucratic delays that beset prospective entrepreneurs. TIPA also organizes trade fairs and exhibitions, so is able to help promote local products. It probably has most success in promoting speciality products such as handcrafts and garments which can be promoted as unique to Botswana.[508]

3.7.6 Tariffs: The Infant Industry

The Southern African Customs Union was designed to give protection to developing industries within its borders, but except for industries where the BLS countries (Botswana, Lesotho and Swaziland) have comparative

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508 IBID, P51

advantages, they are at a disadvantage compared to South Africa and its highly developed industrial areas and infrastructure. To help redress the balance the BLS countries are allowed to put a tariff on the import of a product when local production can be shown to supply at least 75 per cent of the market, and when it has the facilities to reach all areas of Botswana. This tariff can remain for a maximum of eight years. The Infant Industry Clause is not widely used, and previously there has been a policy to only allow a manufacturer this protection to the exclusion of other forms of incentives, although this may change.[509]

3.7.7 Government Involvement:
The Botswana Development Corporation

The Botswana Development Corporation (BDC) was established in 1970 for the purposes of identifying business opportunities, undertaking any related feasibility studies and interesting potential investors in specific projects. The corporation participates in promising new ventures in partnership with local as well as foreign capital. Such participation may take the form of any one or a combination of the following: financing with share capital; loan finance; loan guarantees; and provision of industrial buildings.[510]

The corporation normally finances projects where its total investment is at least P100 000. Its maximum involvement in a project is generally P3 million in share capital of P6 million. In the case of share capital BDC prefers to have a minority shareholding, but in excess of 15 per cent. In considering project financing the corporation would not normally finance

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509 IBID, P53

510 IBID, P53

more than 50 per cent of the total costs; though, in respect of projects where costs are less than P500 000, consideration would be given to financing up to 75 per cent. In all cases the corporation likes to hold at least 25 per cent of the share capital.[511]

The BDC group consisted of 31 subsidiaries and 17 associate companies as of 30 June 1986. The BDC also had given loans to 16 associated companies and financed 9 companies directly by way of grants. Total capital employed increased to P87 million, with before tax profits increasing to P10,8 million in spite of the down-turn in the economy. The corporation operates the following divisions: agricultural, commercial and industrial, financial services (hire purchasing, leasing, insurance broking and underwriting), property management and development, and tourism, hotels and transport.[512]

4. STRUCTURE AND GROWTH OF MANUFACTURING AND THE ROLE OF FOREIGN INVESTMENT

Manufacturing formed only 6 per cent of GDP (current prices) or 3,4 per cent (constant 1985-86 prices) in 1983-4 and its share of GDP has not grown in the last ten years despite an increase from P25,3 million to P129,4 million in current prices during this period (see Table 1). Gross capital formation within the manufacturing sector (Table 2) has been erratic over the last eight years, a reflection of the effect of the construction of a few relatively large factories within a small enclave.[513]

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511 IBID, P53

512 IBID, P53

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Investment in manufacturing in 1984 reached a value of P115 321 000, an overall average of P550 871 per firm. The greatest investment per firm was in the meat and meat products, and beverage sectors. The former is dominated by the Botswana Meat Corporation (BMC), the latter by Kgalagadi Breweries. This is shown in Table 3. Since the compilation of

TABLE I Gross domestic product (million pula at current prices

SECTOR	1977/78	1979/80	1981/82	1983/84	1985/86
Agriculture	71,7	83,3	87,8	76,1	84,0
Mining and quarrying	55,8	210,7	129,5	405,3	1 005,3
Manufacturing	24,4	29,2	71,2	82,1	129,4
Electricity and water	10,0	15,0	21,8	32,3	40,0
Construction	17,1	36,4	47,6	70,5	61,3
Wholesale and retail	71,9	157,0	182,4	276,9	377,0
Transport and communications	15,0	13,6	19,8	32,7	42,5
Financial institutions	29,9	70,5	87,6	86,5	109,5
General government	58,6	92,6	144,1	202,0	284,8
Household, social services	15,2	20,9	32,7	43,5	49,1
Dummy sector	-9,3	-27,7	-45,3	-28,9	-38,0
Total (Current prices)	360,3	701,5	779,2	1 279,0	2 144,9
(Constant prices)	549,4	701,5	742,5	1 106,0	1 315,6

Sources: Botswana Central Statistics Office, 1987
Whiteside,AW,(ED), Industrialization and Investment Incentives in Southern Africa, P54

TABLE 2 Gross capital formation in manufacturing (million pula)

	1976,77	1978/79	1980/81	1981/82	1982/83	1983/84	1984/85
Current	7,3	7,7	20,5	18,8	12,7	16,9	25,5
Constant	18,7	9,3	16,8	15,3	8,3	10,8	15,8

Sources: Botswana Central Statistics Office, 1987
Whiteside,AW,(ED), Industrialization and Investment Incentives in Southern Africa, P54

this table, licenses have been granted to manufacturers with plans to invest approximately P35 million in addition to the amount in the table, but there are no published figures on how many of these new investments have been committed. Many firms obtain licenses but do not follow through. At the same time a number of firms have stopped production. These are mainly within the textile and electrical goods and subsectors, where difficulties arose in the exporting of goods to Zimbabwe and South Africa.[514]

514 IBID, P54

From the above it is clear that ownership of most manufacturing companies is dominated by foreigners. Reference can be made to Tables 4 and 5. Out of a total of 209 manufacturing concerns 122 are foreign owned as compared to only 32 which are owned by Botswana citizens. The balance of 55 is made up of joint venture companies. Although most manufacturing companies are foreign owned, the number of locals employed accounted for 96 percent of the total.

The Botswana Development Corporation (BNDC) is the main investor, in partnership with foreign companies and local entrepreneurs. In 1987-90 major projects financed included a maize meal joint venture with a Namibian company at Francistown, an iron foundry at Palapye, factory shells, an asphalt mixing plant and the Boiposo exhibition centre outside the capital.

Several multinational companies have invested in industry, including Colgate Palmolive (soaps and cosmetics), and Lonrho (textiles). Lonrho began an expansion of its textile subsidiaries in Selebi-Phikwe and Gaborone and several other firms are setting up in Selebi-Phikwe to take advantage of the regional development programme for the area launched in 1988, designed to encourage export-oriented, non-mining activities. Botswana's sound financial position and liberal foreign exchange regulations have made it attractive as a regional base, as an alternative to South Africa, although the high cost of housing and land, shortage of skilled manpower, and the small domestic market remain disadvantages.

4.1 PROFILE OF THE MANUFACTURING SECTOR 1984

The majority of firms are owned by foreigners. As Tables 4 and 5 show, the trend has been for the percentage of foreign-owned firms to increase.

Most of the manufacturing industries were located in the urban areas (177 out of 209). Although the ownership is dominated by foreigners, the number of locals employed accounted for 96 per cent of the total. Wholly owned foreign firms tend to be of medium size, Batswana mostly own the smaller firms and the larger firms tend to be of joint ownership.[515]

TABLE 3 Investment in manufacturing in Botswana 1984

SUBSECTOR	NUMBER OF COMPANIES	INVESTMENT (P'000)	INVESTMENT COMPANY (P'000)
Meat and meat products	2	19 151	9 576
Agro-based products	8	7 327	916
Beverages	13	16 357	1 258
Bakery products	13	2 104	162
Textiles	48	21 541	449
Tanning and leather products	7	3 793	542
Chemical and rubber products	16	15 702	981
Wood and wood products	12	1 934	161
Paper and paper products	6	2 022	337
Building materials	26	6 808	262
Plastic products	8	4 623	578
Electrical products	10	2 444	244
Handicrafts	3	399	133

Sources: Whiteside, AW, (ED), Industrialization and Investment Incentives in Southern Africa, P55

TABLE 4 Ownership of firms by sector

SUBSECTOR	OWNERSHIP			LABOUR FORCE	
	BOTSWANA	MIXED	FOREIGN	LOCAL	FOREIGN
Meat and meat products		1	1	1 956	41
Dairy and agro-based	1	4	3	46	9
Beverages	1	7	5	579	27
Bakery products	3	3	7	377	20
Textiles	8	8	32	2 432	87
Tanning and leather products		4	3	419	23
Chemical and rubber products		2	14	393	32
Wood and wooden products	1	6	5	448	22
Paper and paper products		2	4	238	22
Metal products	9	7	21	1 490	79
Building materials	7	4	15	1 063	38
Plastics	1	3	4	262	16
Electrical	1	3	6	318	33
Handicrafts		1	2	52	4
TOTAL	32	55	122	10 073	453

Sources: Whiteside, AW, (ED), Industrialization and Investment Incentives in Southern Africa, P55

515 IBID, P56

TABLE 5 Ownership trends in manufacturing: 1979 and 1984

	1979 NUMBER OF FIRMS	%	1984 NUMBER OF FIRMS	%
Botswana	15	17.0	32	15,3
Joint Venture	26	29,5	55	26,3
Foreign	47	53,4	122	58,4
TOTAL	88		209	

Sources: Whiteside,AW,(ED), Industrialization and Investment Incentives in Southern Africa, P56

4.2 THE FINANCIAL ASSISTANCE PROGRAMME AND ITS RESULTS

The importance and degree of success of the incentives will be discussed later but it is appropriate to provide a summary of the results of this policy (see Table 6).

By December 1985 a total of 182 medium-and four large scale projects had been approved, 151 of which were of the CFA type and 31 of the AFA type. There was no up-to-date information on how many of these projects were under way, as both the licensing and FAP are necessarily approved before the commencement of operations. It is clear, however, that not only are many firms licensed to produce but fail to begin operations, but that the same applies, if to a somewhat lesser extent, to firms that have also received approval for FAP funding. Foreign-owned firms tended to operate without the benefit of FAP in contrast to locally-owned firms, but that is mainly a reflection of the predominance of capital-intensive sectors they favour.[516]

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516 IBID, P57

TABLE 6 FAP summary results: medium-scale industrial projects May 1982-November 1984

	NUMBER OF PROJECTS			PROJECT EMPLOYMENT		
	RURAL	URBAN	TOTAL	RURAL	URBAN	TOTAL
Textiles	4	13	17	42	788	820
Concrete products	5	2	7	121	53	174
Mechanical projects	1	7	8	10	157	167
Woodwork projects	3	5	8	92	157	249
Sorghum milling	8	1	9	53	8	61
Bakery projects	5	2	7	178	37	215
Leather and leather goods	1	4	5	27	293	320
Meat products		1	1		17	17
Paper products	2	4	6	115	144	259
Chemical projects	1	2	3	8	34	42
Food processing	3	3	6	145	90	235
Other	7	11	18	352	305	657
TOTAL	40	55	95	1143	2083	3216

Sources: Whiteside,AW,(ED), Industrialization and Investment Incentives in Southern Africa, P56
Barclays Business Guide to Botswana, 1987, P37

4.3 AVAILABILITY AND COST OF INPUTS FOR MANUFACTURING

In order to attract an industry a number of factors are important. The government regards the business climate and government support as being crucial, but has introduced the incentive package in the hope of attracting industry and influencing the capital: labour mix and location. Nonetheless other factors are significant and they are examined below.

4.4 RAW MATERIALS AND PACKAGING

Botswana has certain raw materials in abundance. With the notable exception of diamonds and cattle, which are well exploited, the drawback is normally that the scale of operation needed for economic exploitation would require a huge investment and the market is not sufficiently attractive to justify the development at present. Coal and soda ash are the two best examples. Importing countries are presently served from regions with lower transport costs and/or lower unit costs of production. Smaller supplies of other materials are present, but here the market is weak. Other resources such as wildlife and timber are partially exploited. The game population was affected by drought. There is little furniture made from local hardwoods, as the cheaper, if lower quality, maranti wood from Malaysia is preferred, (the BDC joint venture in furniture manufacture is however leading a promotion of furniture made from the main local hardwood).[517]

Botswana is poor in agricultural resources other than livestock, and cannot compete with South African food processors. It has no sizeable iron ore reserves, but buys all its structural steel from the Republic of Zimbabwe. It also imports all organic chemicals including synthetic fibres.[518]

It is difficult for Botswana manufacturers to compete with South African producers when the raw materials are imported from South Africa and the scale of purchasing is much higher there. In some instances raw materials can be imported from outside Southern Africa with little or no duty payable, and then manufactured into goods which are sold to countries which have a high tariff barrier to the raw material but allow such imports on the basis of value added in Botswana. An important example is polyester yarn which is dyed and made into fabric in Botswana and can be sold to Zimbabwe or South Africa at competitive prices. This largely explains the impressive growth of Botswana's textile industry.[519]

In the past five years paper, box and plastics packaging firms have increased their output and range so they can supply most of the demand at prices comparable to those of South Africa. The exceptions are for specialized requirements, such as cellophane,

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517 IBID, P57

518 IBID. P57

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which is used in cigarette packaging. Can add bottle manufacturers are at a disadvantage because of the scale of production and technology required. These items are imported.[520]

4.5 LAND

Land in Botswana falls into three categories: tribal, freehold and state. Tribal land accounts for 70 per cent of the area and is allocated by the local Land Board under customary law, except where it is used for commercial purposes. Then it is let under common law, and is liable for a rental charge, though demand is reduced by the frequent and lengthy delays in allocation.[521]

Freehold land occupies about 5 per cent of the land area, mostly away from the centres of population. The towns occupy land that was formerly freehold or tribal land but is now being progressively bought out as state land. State land is bought and sold as freehold, but on leases of 50 or 99 years. The remainder of the country is also state land and comprises game parks, reserves, and forest reserves, or else is simply awaiting future allocation.[522]

There have at times in the last ten years been acute shortages of serviced industrial land. Currently all the towns (and most of the villages) have available serviced plots for lease, including plots with factory shells from BDC.[523]

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4.6 LABOUR

In the 1981 census the de jure population was found to be 967 000, increasing at the rapid rate of 3,5 per cent. Botswana also has one of the highest rates of urbanization in the world (from a very low base of course), and in 1985 it was estimated that 196 000 people were living in the five main towns and that the capital, Gaborone, grew at a rate of 9,9 per cent from 1981-6. At the other extreme 41 per cent of the population live in settlements of less than 500. The rural areas are not depopulating: rather, some of the increase is moving to the large villages and towns.[524]

If the population labour force is regarded as all the population between the ages of 16 and 64 years, this yields a figure of about 447 000 people in 1981. Formal employment in 1984 was calculated as 110 000 jobs, or about a quarter of the number potentially available. Whilst this overstates the labour supply, it demonstrates the reserve of labour available. Of this the vast majority are unskilled. People with academic qualifications of secondary school and above have been at a premium, and not unnaturally have ambitions for high standards of living. Technically qualified staff are also scarce, although the number of training institutes is now growing rapidly. Unskilled labour is paid much less than in Western countries although manufacturers doubt how cost effective this labour is.

Employment of labour is controlled by a number of acts, which include regulations on minimum wages. For the manufacturing industry this is currently P0,64 an hour.[525]

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4.7 SERVICES

Water is a scarce resource. The north has the largest reserves but the lowest population. In the south, Gaborone and Lobatse are supplied from a dam at Gaborone with a back-up from a wellfield some 30km to the south. The situation here is likely to remain one of limited water supplies. The region is short of rain and the generally flat topography does not provide good dam sites. This is reflected in the pricing structure for water which effectively prohibits medium-and large-scale users. The north-east zone has a more secure supply, having a number of sand rivers, one of which has been dammed to give a much larger reservoir than supplies Gaborone, while others have useful amounts of water that can be extracted. However, the price of the water remains very high.[526]

Electricity is supplied by the Botswana Power Corporation. This is run as a commercial operation and has had to charge high prices for electricity generated from small coal-fired power stations and even smaller diesel-engined ones. The new thermal power station at Morupule, adjacent to the existing coal-mine, was completed in 1986. It reduces the need for importing electricity from South Africa and provides reserves of electrical power for future industrial expansion. Repayment of the capital investment will prevent the electricity from being sold any more cheaply than at present, but the real cost should fall.[527]

The postal service is generally efficient, at least in the towns. The telephone service has suffered from

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using outdated and undersized exchanges, plus a distribution network of lines that are prone to breakdown. The exchanges are now being updated and micro-wave links installed between the towns and main villages. There is also a ground station link with telecommunications satellites. Telex is widely used by businesses.[528]

Transport links include a gazetted roads network extending over approximately 8 026 km of which some 1 762 km is bituminized. Transport companies serve all of these centres, especially for goods moving north/south and in or out of the country. The railway system consists of a single line from the border with South Africa ('Bophuthatswana') in the south to the border with Zimbabwe in the north-east, a distance of 640 km. The line was owned by the National Railways of Zimbabwe but has been taken over by Botswana. The poor condition of the track and inefficient operation of the line have resulted in poor service. Rail transport has been losing out to road haulers despite the latter's much higher charges. The present upgrading of the track and take-over may enable the railways to win back some of their custom. The Seretse Khama International Airport outside Gaborone, completed in late 1984, is capable of handling intercontinental jets. There are connecting services with the intercontinental flights from Harare, Johannesburg or Lusaka, and one airline flys to Europe from Botswana.[529]

Banking services are provided by three commercial banks. They follow normal banking procedures with regard to financing industry. The government established the National Development Bank in 1963.

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This was particularly active in lending for agricultural developments, but is increasingly lending for industrial projects. It is also responsible for the disbursement of funds under the FAP. The Financial Services Company of Botswana (Pty) Ltd. was formed in 1974 by the BDC, the National Development Bank and two commercial banks. The company deals in hire-purchase financing, industrial leasing and medium-term lending.[530]

5. THE RESULTS OF GOVERNMENT POLICY AND PROSPECTS FOR INDUSTRIALIZATION

During the past decade the government has taken on the responsibility for promoting industrialization. In assessing the success of government policies, the FAP must be seen as most important.

5.1 THE FINANCIAL ASSISTANCE POLICY

Foreign manufacturers are eligible for FAP incentives and are not discriminated against. They tend to receive less assistance as they pay larger sums to non-citizens and these are excluded from the calculation of the assistance. It has also been suggested that medium-and large-scale FAP actually favours foreign business as, with their access to capital elsewhere, they are more able to make use of a policy which emphasizes grants on running costs rather than capital. Isaksen came to the conclusion that the AFA scheme was unnecessarily generous in helping manufacturers, especially foreign-owned companies, to make profits (with a tax holiday) in situations where they would have in any case found the investment opportunity

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sufficiently attractive. How FAP had affected the growth of the manufacturing sector in Botswana was difficult to determine because of the upturn in the economy and the influence of the situation in Zimbabwe. Isaksen concluded that FAP had probably speeded up investments that might have taken place anyway, and that the multiplier effects should not be forgotten.[531]

FAP attempts to persuade businesses to locate in rural areas by offering them a much higher maximum grant. This incentive was increased following a recommendation from Isaksen as he had found no evidence that FAP had caused investors to relocate in more rural areas. There is still little evidence to suggest relocation is happening; foreign manufacturers are rarely located in rural areas in comparison with citizen-owned firms, but this is more a reflection of the types of business favoured by expatriates.[532]

Included in the FAP was the intention that manufacturers should turn to labour-intensive methods, as these could employ more Batswana and were felt to be more appropriate to the needs and aims of the country. Isaksen found that only one manufacturer interviewed had redesigned his business with more labour-intensive methods, and he apparently was planning to cut back on employment as the labour subsidy would be reduced over subsequent years. Whilst there is still no evidence that FAP has promoted labour-intensive methods it happens that many of the foreign-owned businesses have chosen sectors which are naturally labour-intensive, such as garment making and assembly of electronic goods. This lack of influence from FAP may disappoint planners who had hoped for imaginative schemes to

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restructure businesses with high labour requirements, but it may be more helpful to Botswana in the long run (as long as present economic parameters persist) to have businesses that run profitably with or without FAP labour subsidization grants. Foreign manufacturers have contributed significantly to employment within the manufacturing sector; indeed it is the larger joint ventures, such as the breweries, milling and packaging companies (and of course diamond mining), where, with the full approval of the Batswana partners, the most capital-intensive examples are to be found.[533]

Training subsidies are rarely taken advantage of, for reasons that are not clear. It may be that training courses of suitable length and location are still hard to find, although training institutions are now available for a wide range of courses. Employers may also be wary of sending promising people on courses, since on completion those people become attractive to other employers and are frequently poached.[534]

Many manufacturers have talked of frustrating delays in the processing of FAP applications, and some have simply gone on without waiting, a criticism of the speed of processing rather than of the investment opportunities, as such.[535]

It would seem therefore that the government's incentives are assisting in encouraging the development of the industrial sector, but neither as much as hoped for nor in the ways intended.[536]

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5.2 THE LOCAL MARKET AND GOVERNMENT TENDERS

A disincentive that the government is aware of but is either unable or unwilling to remove at this stage is the strong hold that South African-owned retail outlets and wholesalers have on the Botswana market. Retailers, notably in furniture and household goods, have close connections with the South African manufacturers, who are able to supply cheaply produced goods and give long credit terms. It is very difficult for local furniture manufacturers to break into this market, and with the exception of school furniture (now reserved for local manufacturers) neither have they been able to succeed with government offers to tender. This is partly because only one local (joint ownership) company has sufficient investment to manufacture veneer furniture as is produced for the mass market in South Africa.[537]

Local manufacturers and processors of foodstuffs and household items typically sold in general stores and supermarkets find a similar difficulty in breaking into the local market. The largest supermarket has its wholesaling depot in South Africa and so finds it inconvenient to have to purchase locally produced goods separately in Botswana, especially since they would rarely be any cheaper. The largest wholesalers similarly are South African-based companies which have long-term agreements with South African producers, and whilst their policy is not openly against purchasing from local producers, they stock practically nothing which is locally manufactured.[538]

These difficulties make it more important for firms to obtain tenders to supply government orders. Many

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manufacturers, both citizen-owned as well as foreign-owned, have complained of difficulties in tendering for government orders. At times this is because the department has British or South African standards, so goods can only be bought from a British manufacturer (e.g. electrical fittings), or a South African manufacturer who is able to get the South African Bureau of Standards' stamp (e.g. treated poles for transmission lines). The 12,5 per cent preference clause is crucial to some local manufacturers, (e.g. of foam mattresses), since with their smaller scale of production they buy the raw materials at higher prices than the large scale units in South Africa. Even with selling to other customers, it has been tendering to government that has enabled them to survive.[539]

5.3 TARIFF PROTECTION

Although FAP may be helpful, especially, to small scale local producers short of capital and large scale labour-intensive units (such as garment makers) who are exporting, the difficulty of breaking into a local market already well supplied (usually from South Africa), has meant manufacturers have realized the advantages of tariff protection over FAP. The condition to supply at least 75 per cent of the market is usually easy to meet in the manufacturing sector. The problem arises in being able to reach all parts of Botswana with the product. Parts of the country, namely the north-west (Ghanzi) and the extreme north (Kasane) are logically supplied from Namibia and Zimbabwe/Zambia. Manufacturers who can supply the bulk of the market have obtained tariff protection, and have by and large benefited from it. The most recent example is soap packaging (all imported soap now

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attracts a 100 per cent surcharge). It has been government policy that a manufacturer can only receive one type of incentive (FAP being counted as one). The situation may be changed with both tariff protection and FAP available to appropriate manufacturers.[540]

5.4 LICENSING

Foreign entrepreneurs have only rarely complained of not being able to obtain a licence to manufacture a product. More frequently licences are given too freely, and any chance of protecting manufacturers from competitors within a small market is lost. This fear may have some justification as machinery for certain products is not made for low output. Whilst this may have resulted in some lost investment, it has also resulted in some remarkably aggressive marketing. Plastic bag manufacturers, with a capacity well in excess of the local market, have developed export markets in Zimbabwe, South Africa and Zambia; wire nails are sold to South Africa as far away as Durban; prefabricated roof trusses to Bophuthatswana; and garments (fashion clothes) to England. At the same time electronics manufacturers have had markets closed to them in South Africa for what they regard as vindictive formalities to protect South African manufacturers, and exports to Zimbabwe are sometimes frustrated simply by the tight restrictions on paperwork formalities and foreign currency.[541]

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6. SOME EPISODES OR CASES OF MANUFACTURING GROWTH

In this short section we consider a few examples from the major manufacturing sectors, and focus on the extent to which government policy affected them and the nature of their interaction with the international economy.

The BMC, a statutory corporation which slaughters cattle and markets meat and by-products, has been the dominant enterprise in the manufacturing sector since before independence. The BMC distributes to the cattle owners all revenues in excess of its operating costs plus some appropriations to reserve accounts. Cattle prices are determined by the price BMC can get for Botswana beef and by-products in international markets. The BMC has resisted pressures to sell by-products to local industries at lower than export market prices. The European market has been important to the BMC for many years. High transport costs led to the decision to increase the de-boning of beef prior to shipment in order to increase the net returns to Botswana. A canning line was added to process low-quality cuts of beef, and a tannery was built to process hides and skins through to the wet-blue stage. Both processing projects were completed in the late 1970s.[542]

The BMC might have expanded its operations more rapidly but for the fact that sales in its two principal and highest-priced markets (the European Communities and South Africa) are limited by quota. Marginal sales are made in lower-priced world markets. Increased sales would reduce the BMC's average price, which would reduce average prices paid to producers, even though total producer incomes would rise. The BMC's

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542 LEWIS, STEPHEN R. JR., AND SHARPLEY JENNIFER, OP CIT, P39

management and board resisted pressures for additional abattoir capacity in the northern parts of Botswana, despite the fact that capacity there would have saved transport costs (beef being cheaper to transport than live cattle) and would have provided insurance for both drought and veterinary emergencies. Had the BMC moved more quickly (a small abattoir was built in Maun in the early 1980s, and a second larger abattoir is being planned for Francistown), the growth of manufacturing in the meat and meat products subsector would have been more rapid.[543]

The meat and meat products sub-sectors of Botswana's manufacturing does receive 'protection', in European and South African markets, but not at the expense of other sectors within Botswana. However, if the protection were to be removed, the pricing arrangements for cattle are such that the decrease in revenue would accrue to cattle producers, not to value added or employment in the meat manufacturing sectors.[544]

The second largest source of employment and output in manufacturing is the Kgalakgadi Breweries, established in 1975 as a joint venture with a German group (which brought in its own brands) and the BDC. Protection was provided under the Customs Union arrangements by the imposition of a 100 per cent 'Additional Duty' on all imports of beer into Botswana (which principally affected imports from South Africa). The arrangement with the brewery provided for beer to be priced in Botswana at the same levels as prevailed in South Africa, so that consumers who bought domestic beer would not pay the tariff-protected price. However, the quality of the local beer proved to be so poor, and

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brand loyalties to the traditional brands so strong that after some initial successes in establishing the local brands in 1976, beer imports flooded in, local sales fell, and there were substantial outflows of payments of Additional Customs revenues to the customs revenue pool. By 1979 the brewery was reorganised with a new technical partner, and there was a switch back to the traditionally popular brands now locally produced, which then again became available at cross-border prices.

This episode illustrates that fully competitive import substitution can and did take place, but that the right mix of incentives and the choice of management was necessary to achieve that result. The government and the BDC placed constraints on the brewery management, and ultimately limited the losses to Botswana by insisting on pricing guarantees and by changing the management rather than simply restricting imports in order to ensure the profitability of the local industry. Indeed, since the brewery was a major consumer of Botswana's scarcest resource, water, it was of more than passing importance that the industry should be an efficient producer.[545]

The textile sector is the third largest identifiable manufacturing group in Botswana. Located mainly in Francistown, much of the industry processes for the export market, principally to Zimbabwe. In some of the largest firms, goods are processed at different stages in both Botswana and Zimbabwe, taking advantage of the free trade arrangements. There are advantages to Botswana producers at some manufacturing stages, since they can import intermediate goods from South Africa duty free, while Zimbabwe producers would have to pay

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import duties on the same goods. Provided there is 25 per cent value added in Botswana, the processed goods can then enter Zimbabwe on a duty-free basis. There was fairly rapid growth in textiles in the 1970s, and a major increase in investment occurred immediately after Zimbabwe's independence in 1980, and exports from Botswana to Zimbabwe increased substantially. However, restrictions imposed on Zimbabwe's imports in 1983 and 1984 led to a sharp reduction in textile exports and there was a consequent drop in output and employment in the Botswana textile sectors. Textiles have been exported to other markets as well, including Europe, but the vulnerability of manufacturing to a single large regional market has been considerable. It is of some importance that on several occasions textile producers came to the government for financial subsidies or some form of protection with the explicit threat that failure to provide assistance would result in job losses. The government consistently refused such proposals, making it clear that private enterprises were expected to stand on their own. In the mid-1980s the BDC did provide some financing to the textile sector during the period of export cut-backs, but the financing was on a commercial basis.[546]

The metal products industries, linked largely to construction activity, also had difficulties in the 1980s as Zimbabwean firms dumped goods in the Botswana market, and also because Zimbabwe manufacturers were able to purchase steel more cheaply from South Africa than could Botswana producers (due to Customs Union pricing practices). The Botswana government responded by developing rules under which the Local Preference Scheme for government contracts could be extended to local manufacturing sub-contractors covered by Local

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Preference. The arrangements provided some price preference to local producers on government-related contracts.[547]

Another BDC joint venture of some interest and success was a wheat flour mill, established on Tribal land in Ramotswa, about 20 miles from Gaborone. The choice of site was dictated in part by the scarcity of land in the existing industrial estates in urban areas. The technical partners and foreign investors were from Zimbabwe, a firm with considerable regional expertise. They undertook to produce according to price and quality standards which would fully compete with imports, and in return were provided with exclusive access to the Botswana market. The project resulted in nearly 100 per cent import replacement (based entirely on imported wheat, since Botswana produces no wheat) and at no measurable welfare losses to Botswana consumers, since both price and quality guarantees were fully met.[548]

One protected sector on which the jury was still out (in late 1987) is a soap factory (Kgalakgadi Soap Industries) established in Gaborone in the early 1980s without BDC partnership. This project obtained protection under the Customs Union agreement, with pricing guarantees that they would exceed import parity by only a small percentage. As with the first brewery project, the brands were new, not traditional. The first two years of operation resulted in an experience better than that of the brewery, though imports continued to occupy a substantial share of the market despite the price premium. It remains to be seen whether the management can meet the necessary quality

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standards, capture a sufficiently large share of the market to be financially viable, and replace enough imports so that payments into the customs pool become negligible.[549]

This brief listing of projects does not include a number of the ventures that arose without any government intervention.

What was happening in these industries was a 'normal' development of the domestic market in response to the increased market size and changing competitive position of potential local firms. Government interventions took place, but they did not involve 'protection' of one kind or another that imposed a drain on the other sectors of the economy or on the government budget in order to support the manufacturing sector.[550]

7. CONCLUDING REMARKS

7.1 PROSPECTS FOR FUTURE FOREIGN MANUFACTURERS

Effects of government policy will continue to be central to the growth of manufacturing. Barring dramatic changes in the trading relations of Botswana and the political situation within the country and region, there is every reason to believe that there will be a continuation of the open policy towards foreign manufacturers as emphasized in NDP V1.[551]

There are, however, already certain trends in evidence which qualify this statement. Firstly, it is likely

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that the number of reserved sub-sectors from which new foreign manufacturers will be excluded will increase, although these may continue to be activities where few foreign businessmen show interest anyway. Secondly, while welcoming foreign manufacturers themselves, there may be increased pressure on the expatriate to localize the middle management and technical positions within his company quicker than he thinks possible, and leaving aside the question of who is right, the result could be to frighten away new entrepreneurs. Joint ownership can be seen as a form of localization and is naturally a very attractive proposition to the government as it seems to hold all the advantages of foreign ownership, plus most of the advantages that can accrue to citizen ownership, including retention of more of the profits within the country.[552]

The Sixth Plan acknowledges that the labour pool will increase faster than formal employment. This is bound to put pressure on the government to think of new ways of finding employment. It is stated that most people will have to continue as self-employed farmers, yet with unchecked urban migration, people will continue to flock to the towns and larger villages in the hope of employment. In the long run this seems likely to force changes in policy which will affect manufacturers.[553]

It is entirely possible that the BDC may be called on to play a more important role in meeting the employment and development challenge. BDC participation will be considered in the following categories: when it is in the national interest that an economic rent be transferred to government as a share of returns to equity instead of being charged as a simple royalty;

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where there is a foreseeable possibility of passing control to citizen shareholders in a relatively short period of three to five years; and where the project appears profitable and economically beneficial but despite active promotion, has not been undertaken by the private sector, or would not be initiated without government intervention.[554]

Further, in considering parastatal participation, the following aims will be kept in mind: their main role is in creation of new economic opportunities and not merely gaining control over existing ones; they should avoid competing with Batswana entrepreneurs; and they should positively assist citizen entrepreneurs to start or participate in viable businesses and should, wherever possible, sell off suitable ventures to Batswana owner-managers. This effectively gives BDC a very wide mandate where, with broad interpretation, almost any enterprise could be embarked upon, especially if it did not harm citizen entrepreneurs.[555]

The government will have to monitor the manufacturing sector carefully and may wish to reconsider the role of the FAP in bringing about industrialization. Nonetheless, it is clear that its main effort may be through the BDC, although it will have to reconcile the need for the corporation to be profitable and the desire to use it to solve problems that free enterprise chooses not to tackle.[556]

7.2 FUTURE TRADE AND INTERNATIONAL RELATIONS

This is perhaps the most crucial issue with regard to development within Botswana. The region is dominated

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by South Africa, which will have a direct and indirect effect on development. On the question of whether it would be better to leave SACU or not, Miller and Decaux decided that, on balance, Botswana stood to gain more by remaining within the Union (Miller and Decaux, 1980).[557]

Two considerations may cause the government to review the situation. One is the political aspect. While other front-line states would like to see South Africa isolated, Botswana has so far resisted this pressure for practical considerations. Another aspect is, however, that as of late 1984 the customs pool has been considerably reduced. This will affect the revenue derived from this by the BLS countries (there is a time lag of up to 18 months before this will show). The balance is now likely to be much less in favour of remaining in SACU.[558]

However much leaving SACU could leave trading relations unaffected (Zimbabwe's main trading partner is still South Africa), it would make industrial development more difficult since the added incentives to encourage manufacturers could be offset by increasing delays in obtaining plant and spares as the customs would have to deal with revenue collection as well as the present paperwork. Within SADCC there have been no effects on the direction of trade as a result. Perhaps it has been realistic to concentrate on improving communications links as a first step. Improvements in trade within the region can be welcomed, although in the long run it may be acknowledged that South Africa contains by far the largest concentration of industry, with the consequent implications for Botswana.[559]

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The easing of tensions with South Africa, as a result of the adoption of a political reform programme and the ending of the policy of destabilisation of neighbouring states by President FW de Klerk in 1989 and Namibia's independence in March 1990, have opened up new prospects for Botswana during the 1990s. Close bilateral relations have quickly been established with Namibia, following reciprocal visits by Presidents Masire and Nujoma during the latter part of 1990. This could enable Botswana to lessen its dependence on South Africa by new export outlets to the Namibian coast and the sourcing of some imports via Namibia. Since 1990 relations with South Africa have been stable and Botswana would, along with Namibia, undoubtedly have a key role in the expected entry of South Africa into regional organisations such as SADCC following the establishment of a non-racial government in Pretoria.

8. SUMMARY

In this chapter we examined the relevance of the theory of direct investment. This was followed by an analysis of the characteristics of the manufacturing sector in Botswana. Here we found that at independence manufacturing in Botswana was dominated by the Botswana Meat Commission in Lobatse. However, over the 20 years after independence a variety of other activities have been developed in response to different stimulae.

This chapter also examined government policy and incentives. Here we found that since independence, the government has always regarded the development of the enterprise sectors of the economy as an activity primarily of the private sector. We also found that the main objectives of the government's industrial policy were to increase the number of worthwhile job opportunities; increase economic independence;

diversify the economy; and protect the interests of consumers and workers. The government also believes that a stable investment climate is more attractive to foreign investors than a range of specific financial incentives.

Botswana also has a number of trade agreements with various countries. The most important of the trade agreements is the Southern African Customs Union (SACU), comprising of Botswana, Lesotho, Swaziland and South Africa. Botswana's macroeconomic policy was also examined as well as its trade policy and protection.

Under other policies to promote manufacturing the following were examined:

- local preferences
- Financial incentives: Financial Assistance Policy
- The tax system
- Licensing arrangements
- Positive encouragement and advice
- Tariffs
- Government involvement.

The structure and growth of manufacturing and the role of foreign investment were also examined. Here we found that as at 1984, 122 manufacturing companies were foreign owned, representing 58.4 percent. 55 companies were of a joint venture nature. This represented 26.3 percent. Only 15.3 percent, i.e. 32 companies, were actually owned by Botswana citizens.

The chapter also investigated the following:

- The financial assistance programme and its results;
- Availability and cost of inputs for manufacturing;
- Raw materials and packaging;
- Land availability;
- Labour;
- Services.

The results of government policy and prospects for industrialisation were also examined under the following:

- The financial assistance policy;
- The local market and government tenders;
- Tariff protection;
- Licensing.

The chapter also highlighted some episodes or cases of manufacturing growth as well as looking into prospects for future trade and international relations.

CHAPTER FIVE:

CONCLUDING REMARKS

1. INTRODUCTION

The economic history of the Republic of Botswana provides an almost classic example of how a developing country with determined and devoted leadership can help itself. When independence was gained, the generally accepted assessment of Botswana's prospects emphasized the apparent weaknesses and ignored some very basic strengths. These forecasts missed the mark entirely. Observers noted the lack of infrastructure and the problems of a landlocked country. Perhaps because it was then an unknown quantity, they gave no weight at all to leadership - to the dogged determination and devotion with which the new leaders intended to pursue their goals. Observers focused on the country's modest resources - its tiny and untrained population, its limited known mineral endowment, its arid climate. The leadership was untested, but it has made all the difference in the world.[560]

A propitious world economic environment aided Botswana's economic development, but the new leaders took advantage of every opportunity. They urged everyone - potential investors, South African officials, Common Market officials, United Nations officials - to participate. They mobilized their own resources, they prepared their positions with care, and they coordinated their own efforts to ensure that they were all working for the same ends. If genius is

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560 HARTLAND-THUNBERG, P., BOTSWANA: AN AFRICAN GROWTH ECONOMY, 1ST EDITION, WESTVIEW PRESS, INC, COLORADO, 1978, P79

defined in terms of diligence, these men and women were certainly of genius calibre.[561]

The lesson is clear. A "bootstrap" economic development program can succeed. Foreign aid in the form of financial and technical resources from public and private sources, is readily available for projects and programs when they seem to be economically feasible and when the developing country is willing to contribute substantial amounts of its own limited resources. The cost of providing the extended road and rail network and the power and water supplies for the projects at Selebi-Phikwe and Orapa was high for Botswana. It was high because of the number of skilled personnel required to plan and implement the schemes and because of the amount of public credit committed to their financial support. The fact that the country was willing to commit its own scarce resources to the projects encouraged foreigners to do so.[562]

In this chapter we are going to look at important factors in the economic development of Botswana since 1980. These will be examined as follows:

- willingness to seek foreign expertise
- the success of government policies
- Botswana's success at managing booms and busts

Under the availability of aid we will examine the following:

- foreign loans and grants
- foreign direct investment

561 IBID, P80

562 IBID, P80

2. IMPORTANT FACTORS IN THE ECONOMIC DEVELOPMENT OF BOTSWANA

2.1 WILLINGNESS TO SEEK FOREIGN EXPERTISE

An important factor in the economic achievements of the first decade was Botswana's willingness to seek foreign expertise to supplement its own meagre supply of trained professional and technical talent in staffing the ranks of the senior civil service. Equally important was the reception accorded them. They were made to feel welcome - so much so that many of the top expatriate civil servants have been in their jobs for most of a decade. This is evidence of a large degree of trust and mutual respect between the Batswana in cabinet-level positions and the (mostly European) expatriate civil servants. The trust would not exist if the cabinet members had any doubt about the loyalties of the expatriates or if the expatriates themselves felt at all harassed, socially or professionally, because of their race. This is not to deny the strength of the pressures for "localization" or the dissatisfaction over progress achieved so far. The pressures are strong. They are, however, managed in a mature, pragmatic manner in order to maximize economic growth.[563]

Not every developing country is as fortunate as Botswana, which has escaped an inheritance of resentment toward citizens of a former colonial power. The practical advantages of suppressing such bitterness are clearly documented by the major role that talented European expatriates have played and are playing in Botswana's self-help exercise. The country could not have accomplished what it has without their skills. To

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563 IBID, P81

have forced their own people into top-level policy positions before they were qualified would have meant plans less carefully developed, projects less completely studied, and proposals less thoroughly documented. The risks of failure would have been greatly enhanced. Botswana's experience illustrates that even with this expertise, the risks are substantial.[564]

It is fashionable to encourage self-help in the developing countries. Self-help, however, is an alternative or supplement to foreign help only if it is soundly based on feasible plans and well managed and directed. Self-help depends on talented and devoted leaders in the developing country. Without these qualities of leadership, foreign help will be wasted.[565]

2.2 THE SUCCESS OF GOVERNMENT POLICIES

The government's overall macro-economic policy has been consistent with avoiding balance of payments crises and with encouraging diversification. As already discussed, the government has managed international reserve accumulation, government expenditure, the exchange rate, and wages with these goals in mind.[566]

The government has avoided balance of payments crises. The required adjustment in 1982 was the result of an unexpectedly large decline in diamond earnings and was less severe than would have been necessary if the

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564 IBID, P81

565 IBID, P81

566 ECONOMIC DEVELOPMENT INSTITUTE OF THE WORLD BANK, 1989, <u>SUCCESSFUL DEVELOPMENT IN AFRICA</u>, WASHINGTON, D.C. THE WORLD BANK, P201

government had not previously accumulated reserves. In 1986, international reserves equalled over 20 months of imports. This should certainly help Botswana avoid balance of payments problems in the near future.[567]

- GDP growth has been high and less variable than income from mining. The government has stabilized the growth of its expenditures, thereby contributing to this stability, and has avoided declines in GDP as a result of severe balance of payments crises. Real GDP growth per annum averaged 13 percent between 1979/80 and 1984/85, while non-mineral GDP increased an average of 5-1/2 percent per year.[568]

In general, the evidence suggests that diversification is progressing. Non-traditional exports have grown as rapidly as other exports maintaining their share of total exports at around 12 percent. Manufacturing had the fastest rate of employment growth from 1979/80 to 1984/85, almost twice as fast as projected in the fifth plan. For the sixth plan, the government used lower import coefficients of private consumption to reflect increased production in Botswana of consumer goods and services.[569]

2.3 BOTSWANA'S SUCCESS AT MANAGING BOOMS AND BUSTS

Many countries do not handle temporary booms in export earnings well. Windfall gains in export earnings often lead to increased spending and increased imports. Saving does not increase in the form of either foreign assets or domestic investment by an appropriate amount given the temporary nature of the windfalls. Instead,

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567 IBID, P201

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public spending increases and governments borrow against expected future export receipts that often do not materialize when the boom subsides. As a result, many countries that experienced windfalls in the 1970s have since run into serious debt servicing difficulties.[570]

Why do countries find it so difficult to respond to windfall gains? Part of the explanation is that commodity prices are difficult to forecast, and determining the appropriate macro-economic policy is more difficult under uncertain conditions. Second, most governments are under heavy pressure to spend. In a developing country, the government may find accumulating large stocks of foreign assets very difficult politically when demand for both current consumption and investment expenditure is high. In many countries these political pressures make optimal saving during boom periods impossible. When governments do not know for certain that prices will fall in the future, they will be under strong pressures to err on the side of optimism about future price trends.[571]

There is some debate about whether adopting appropriate policies is easier or harder if the government receives the windfall gain rather than the private sector. If the boom accrues to the private sector, the government can either tax it away to raise savings or devise policies to encourage the private sector to save it in an appropriate way. If the private sector is not allowed to accumulate foreign assets, the resulting increase in international reserves will lead to an increase in the monetary base. The government must

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sterilize this effect if it wants to avoid inflationary pressures and real exchange rate appreciation. Sterilization, however, can be difficult. If the government receives the windfall gain, the appropriate macro-economic response may be less complicated in theory. However, many governments that have received windfall gains have managed their booms disastrously. Several explanations for this exist. Governments find avoiding increased expenditures during booms difficult. The expenditures can take many forms, including increased parastatal deficits and overpriced government contracts with the private sector.[572]

Another possible negative effect of the government receiving the windfall is that when the boom ends, the government can more easily postpone adjustment by borrowing from the central bank or abroad, which ultimately may make adjustment more costly. In addition, when the government finally cuts back on its expenditures, the cuts may take debilitating forms, such as neglecting maintenance and cutting everything except salaries. As a result, the country ends up in worse shape with the boom than it would have been without it.[573]

Botswana has avoided many of the negative economic effects of a booming export sector that other countries have been unable to avoid. One reason may be Botswana's overall vulnerability. The country is landlocked, and therefore depends on transportation routes through other countries. Among the major risks facing Botswana cited in the sixth plan was "the possibility of supply decreases or inability to obtain access to markets due to unfavourable development in

572 IBID, P202

573 IBID, P202

other countries ... risks of this nature are very real in Botswana's circumstances, and it is precisely because of such risks that Botswana needs to maintain a reasonable level of contingency reserves.[574]

In addition, another major export earner, copper-nickel matte, has also proved vulnerable to external events. With reduced world demand, world prices have fallen. Nickel prices fell 22 percent in 1986, while copper prices fell 3 percent. As a result exports fell from P120 million (US$65 million) in 1985 to P99 million (US$53 million) in 1986. Meat and meat products - Botswana's third largest export commodity - is vulnerable to both drought and foot and mouth disease. Also, customs union revenue is not perfectly predictable. All these sources of uncertainty make following a cautious policy on international reserve accumulation politically easier.[575]

Another explanation of why Botswana has been able to accumulate foreign assets is that real GDP, real government recurrent expenditure, and real development expenditure have all been growing at very high rates. The mineral sector has generated so much foreign exchange and government revenue that government expenditure could grow very fast and still not use up all the additional reserves. Accumulating savings must be easier when real income and spending are increasing rather than when more obvious sacrifices in current expenditures are required. Nonetheless, the government has experienced pressure to expand its expenditures even faster and could have tried to undertake additional projects or activities, perhaps projects and activities with very low rates of return.[576]

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574 IBID, P203

575 IBID, P203

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Several other factors may have contributed to Botswana's successful management of its diamond export booms. First it has had the advantage of experiencing booms later than many other developing countries and has seen the effects of mismanagement. This may have contributed to Botswana's success, but is not in itself a sufficient explanation. Many other countries mismanaged commodity booms in the late 1970s and 1980s that had either watched other countries mismanage booms earlier or had mismanaged booms within their own countries.[577]

The second factor concerns the timing of Botswana's first bust. In the early 1980s, with the Jwaneng mine, forecast as one of the most profitable diamond mines in the whole world, coming on line, the government experienced considerable pressure to increase its spending even faster than planned. Some people cautioned against too fast an increase on the grounds that the opening of Jwaneng would increase foreign exchange earnings and government revenues to a higher level than before, but thereafter those revenues would increase in real terms only to the extent that diamond prices rose faster than the price of imports. Given the uncertainty in diamond prices, this would not be a reasonable assumption. So faster growth rates of government spending would not be sustainable in the long run. In the end, the opening of Jwaneng coincided with a bust in the diamond market. If it had coincided with a boom, the pressure for faster expansion of government expenditures would have been very difficult to resist. The lesson that diamond markets are volatile came very quickly, so that the country did not have time to make any major mistakes.[578]

577 IBID, P203

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The third factor is Botswana's political stability and quality of leadership. Countries with unstable governments may find saying no to pressures from special interest groups to increase spending more difficult. Increased spending in response to political pressures may have short-run political benefits that outweigh any negative effects on the economy later on. Botswana also has had the advantage of having an ex-minister of finance as president.[579]

Given the political commitment to follow appropriate economic policies, setting up a system within the government whereby key officials have access to sound economic advice on macro-economic policy can contribute to success.[580]

3. AVAILABILITY OF AID

3.1 FOREIGN LOANS AND GRANTS

Botswana's official aid receipts remained relatively static during the early 1980s, but the value of disbursements began increasing in 1986. This was mainly attributable to a rise in bilateral disbursements which, from a low point of $65 million in 1985, had increased to $132 million in 1987, declining slightly in each of the following years. This reflected an increase in aid from Sweden and Norway, now the country's largest bilateral aid donors, with Japan, the USA and West Germany the other major sources. In contrast to the stagnation in bilateral aid during 1988-1989, multilateral aid rose to a record

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579 IBID, P203

580 IBID, P204

$45 million in 1989. In that year grant aid amounted to $132 million or 79 percent of the total, and Botswana has remained eligible for concessionary aid funding despite its achievement of middle-income status.

Ironically in view of its recent wealth, but perhaps not surprisingly given its large reserves and ability to import from these same bilateral donors, the country now receives more aid per head of population than any other country in the world, apart from Israel - $133 million per head in 1989 according to the World Bank's World Development Report. The aid flow into Botswana is depicted in Table 1 in chapter 3, which defines official development assistance as grants and loans with at least a 25 percent grant element, provided by OECD and OPEC member countries and multilateral agencies, and administered with the aim of promoting development and welfare in the recipient country. IMF loans, other than Trust Fund facilities, are excluded, as is aid from the Eastern Bloc.

From the above, it is clear that aid in the form of loans and grants played a very important role in the economic development of Botswana since 1980. Initially, the role played by British aid from the early 1960s until 1972-73, with both capital, recurrent and technical assistance support, when little other assistance was available, was vitally important since it enabled Botswana to lay the foundations for future development. Many of the features that attracted later donors are directly traceable to this period. The financing of the copper-nickel complex at Selebi-Phikwe by a consortium of donors under the co-ordination of the World Bank was also crucial.

Also important is the fact that virtually all of the bilateral donors and the United Nations Development Programme (UNDP), provided Botswana with large amounts of technical assistance in the form of consultants, advisors and executive personnel holding established posts at the technical or administrative level. Some programmes were fully funded. Others, like the United Kingdom's OSAS (Overseas Service Aid Scheme) programme supplemented the salaries of expatriate staff on government of Botswana contracts. In addition there was a large number of third country nationals occupying mainly middle level positions, directly recruited by the government.

3.2 FOREIGN DIRECT INVESTMENT

Just as the provision of foreign aid in the form of grants and loans was important in the economic development of Botswana, so too was the role played by foreign direct investment.

At independence, manufacturing in Botswana was dominated by the Botswana Meat Commission (BMC) in Lobatse, which is an abattoir producing chilled and frozen de-boned beef for the high quality international market. As late as 1984/85 the BMC's meat and meat products operations still accounted for 28 percent of value added and 36 percent of output from the manufacturing sector, but less than 20 percent of manufacturing employment.

Over the twenty years after independence, a variety of other activities have been developed in response to different stimulae. The second largest single establishment (after the BMC) is the Kgalakgadi Brewery in Gaborone, which was established in the mid-1970s. Operations have been established in textiles, food products such as grain milling and bakeries, building suppliers, etc. However, apart from the BMC, the larger establishments tend to be those which are foreign owned or in partnership with local firms, particularly the Botswana Development Corporation

(BDC). Out of a total of 209 manufacturing companies in 1984, 122 of these were foreign owned as compared to only 32 which are owned by Botswana citizens. The balance of 55 manufacturing companies is made up of joint venture companies. Several multinational companies have invested in industry, including Colgate Palmolive (soaps and cosmetics). Lonrho began an expansion of its textile subsidiaries in Selebi-Phikwe and Gaborone and several other firms are setting up in Selebi-Phikwe to take advantage of the regional development programme for the area launched in 1988, designed to encourage export-oriented, non-mining activities. Although most manufacturing companies are foreign owned, the number of locals employed accounted for 96 percent of the total.

Botswana's experience - so different from some other countries that enjoyed a primary product boom, such as Nigeria between 1973 and 1982, highlights the importance of pragmatic, even conservative management of bountiful foreign exchange inflows.[581] It's government did almost everything correctly:

- it maintained an open economy, dismantling exchange control;

- it ploughed diamond revenues back into infrastructure - roads, houses and schools;

- it wooed foreign investment;

- it allowed multi-party democracy to develop, with an efficient and incorrupt administration, leaning more heavily than elsewhere on expatriate skills;

581 OPTIMA, VOLUME 38, NUMBER ONE, 1991, ANGLO AMERICAN CORPORATION AND DE BEERS GROUP OF COMPANIES, CREDA PRESS, CAPE TOWN, P.28

- it is working hard to establish a strong, diverse financial sector, encouraging new banks and financial institutions to open up in the country.[582]

Botswana provides a classic case of an administration which correctly summed up its strengths and weaknesses and acted accordingly. But its success should not be allowed to obscure its forthcoming problems.

The economy has not been diversified. In 1990, half the GDP emanated from mining; manufacturing's share has actually halved since 1966, while agriculture's languishes at only 3%.[583]

There is a massive task of diversification ahead which must succeed if an unemployment crisis is to be avoided.

Even if Botswana can sustain the sound policies that served it so well in the 1980s, continued success is far from certain.

The underlying challenge is that of creating sufficient jobs for a fast growing - if small - population in a country with such a narrow resource base.

If the diamond boom does indeed run out of steam, Botswana will be lucky to maintain economic growth of 4% or 5% a year.[584]

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4. SUMMARY

In this chapter we looked at important factors in the economic development of Botswana since 1980. An important factor in the economic achievements of the first decade was Botswana's willingness to seek foreign expertise to supplement its own meagre supply of trained professional and technical talent in staffing the ranks of the senior civil service. Equally important was the reception accorded them.

Under the success of government policies we found that the government's overall macro-economic policy has been consistent with avoiding balance of payments crises and with encouraging diversification. The government has managed international reserve accumulation, government expenditure, the exchange rate, and wages with these goals in mind. It is these and various other factors that enabled Botswana to have access to foreign aid in the form of both grants and loans, and also be able to attract foreign direct investment.

APPENDIX 1

SUMMARY

1. TITLE

   The economic development of Botswana since 1980 with special reference to the role of foreign aid.

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   JOINT SUPERVISOR: DOCTOR E.T. BASSON

6. SUMMARY

The primary object of the study was to determine the effect foreign aid in the form of grants, loans and direct investment has had on the economy of Botswana since 1980, and also to identify specific sectors within the economy that received foreign aid in the form of grants, loans and direct investment and how they compare with those sectors which did not receive the same.

It has been the conclusion of this study that foreign aid in the form of grants, loans and direct investment played a very important role in the economic development of Botswana since 1980. Initially the role played by British aid from the early 1960s until 1972-73, with capital, recurrent and technical assistance support, when little other assistance was available, was vitally important since it enabled Botswana to lay the foundations for future development. Many of the features that attracted later donors are directly traceable to this period. The financing of the

copper-nickel complex at Selebi-Phikwe by a consortium of donors under the co-ordination of the World Bank was also crucial.

It must, however, be pointed out that the economy has not been diversified. In 1990, half the GDP emanated from mining; manufacturing's share has actually halved since 1966, while agriculture's languishes at only 3%. There is a massive task of diversification ahead which must succeed if an unemployment crisis is to be avoided. Even if Botswana can sustain the sound policies that served it so well in the 1980s, continued success is far from certain.

APPENDIX 2

OPSOMMING

1. TITEL

Die ekonomiese ontwikkeling van Botswana sedert 1980 met spesiale verwysing na die rol van buitelandse hulp.

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5. LEIER : PROFESSOR G.L. DE WET
MEDE-LEIER : DR E.T. BASSON

6. OPSOMMING

Die primêre doel van die studie was om te bepaal watter uitwerking buitelandse hulp in die vorm van skenkings, lenings en direkte beleggings sedert 1980 op die ekonomie van Botswana gehad het; om spesifieke sektore binne die ekonomie te identifiseer wat buitelandse hulp in die vorm van skenkings, lenings en direkte beleggings ontvang het en hoe hulle met daardie sektore vergelyk wat dit nie ontvang het nie.

Daar is in hierdie studie tot die gevolgtrekking gekom dat buitelandse hulp in die vorm van skenkings, lenings en direkte beleggings 'n baie belangrike rol in die ontwikkeling van Botswana sedert 1980 gespeel het. Aanvanklik was die rol wat Britse hulp vanaf die vroeë sestigerjare tot 1972-73 gespeel het, in die vorm van kapitaal, herhalende en tegniese bystandsverlening toe daar min ander bystand beskikbaar was, van uiterste belang aangesien dit Botswana in staat gestel het om die grondslag

vir toekomstige ontwikkeling te lê. Baie van die kenmerke wat latere donateurs gelok het, kan regstreeks teruggevoer word tot hierdie tydperk. Die finansiering van die koper-nikkelkompleks by Selebi-Phikwe deur 'n konsortium van donateurs wat deur die Wêreldbank gekoördineer is, was ook deurslaggewend.

Daar moet egter ook daarop gewys word dat die ekonomie nie gediversifiseer is nie. In 1990 was die helfte van die BBP uit die mynbou afkomstig; die vervaardigingsektor se aandeel het inderwaarheid sedert 1966 met die helfte verminder, terwyl die landbou s'n wegkwyn teen slegs 3%. Daar lê 'n massiewe taak van diversifisering voor wat sal moet slaag indien 'n werkloosheidskrisis verhoed wil word. Selfs al kan Botswana die gesonde beleidsrigtings handhaaf wat hom in die tagtigerjare so goed te staan gekom het, is voortgesette sukses nog lank nie verseker nie.

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