KPMG

Economic Snapshot H2, 2016

Namibia

Inflation – Inflation trended broadly higher in 2016 H1, rising from 5.3% y-o-y in January to 6.7% y-o-y in June, mainly ascribed to a rise in transport costs and higher food prices. The headline figure rose further to 7% y-o-y in July. The recent strength of the Namibia dollar (pegged to the South African rand) could provide some reprieve moving forward, but the currency remains at the mercy of uncertain global developments pertaining to emerging market sentiment and possible moves by the US Federal Reserve. Regardless, food price pressures will likely keep inflation elevated in the coming months. We forecast inflation will average 6.7% in 2016.

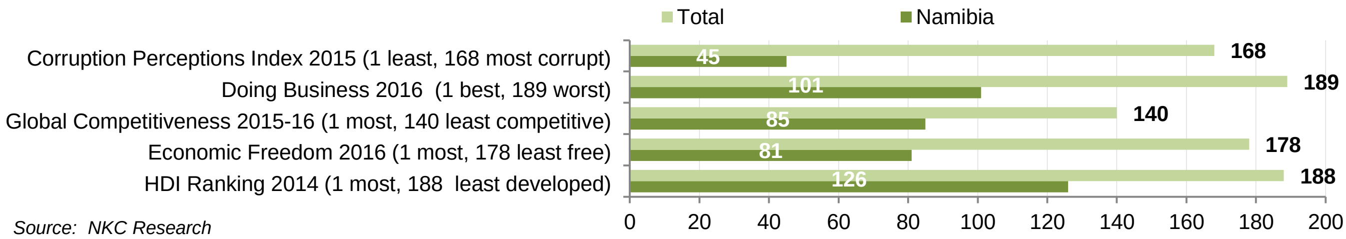
Growth – The Namibia Statistics Agency (NSA) released its final 2015 national accounts data on August 11, with real GDP growth in 2015 revised down from 5.7% to 5.3%. The Namibian economy looks set to face stronger headwinds this year, with the services sector in particular forecast to post slower growth as consumer demand buckles under higher inflation and interest rates. Industry should perform better with a number of new mines expected to ramp up production. We nonetheless forecast real GDP growth will decline to 4.7% in 2016.

National development plan – The National Development Plan (NDP4) was launched in 2012 with the intention of refocusing the government's efforts towards achieving three main objectives. These objectives included: 1) faster and sustainable economic growth; 2) the creation of employment opportunities; and 3) enhanced income equality. NDP4 aims to achieve fast economic growth in order to bring down the country's unemployment rate to 20% by 2017. The NSA measured an average unemployment rate of 28.4% during 2012-14, which suggests that the goal of 20% in three years is unlikely to be met.

OPPORTUNITIES	STRENGTHS
The majority of food and consumer goods purchased in the country are imported from South Africa, signalling import-substitution opportunities.	Low political risk with stable trend lines suggests that the country should continue on this footing over the medium to long term.
A five-year, N$223bn infrastructure development plan kicked off in early 2015 to boost Namibia's status as a regional transport hub.	Small size and low growth rate of population, high literacy rates, and GDP per capita relatively high among developing countries.
The real estate sector is experiencing a boom in prices and development, but the IMF has raised concern of a potential housing bubble.	Links with South Africa's economy are supported by a closely aligned legal environment, good quality economic data, and linguistic features.
Hydrocarbon exploration continues along the coast, though results have so far not been inspiring.	Financial sector is small but well developed and regulated. The capital market (used to help finance the fiscal deficit) is deep by African standards.

VULNERABILITIES	WHAT IS BEING DONE?
Dependent on mineral exports for foreign revenues and state income. This makes the country susceptible to international developments affecting demand for copper, uranium and diamonds.	Government is promoting tourism, transport & storage facilities, agriculture and manufacturing as alternative investment opportunities in order to diversify foreign revenue streams and investment interest.
The desert economy's reputation as a business-friendly country has deteriorated in recent years, based on international surveys.	NDP4 again strives to improve the investment climate in Namibia – though progress has been slow.
Faces significant climate change risks over next few decades. Groundwater recharge could fall by 30% - 70% in some areas.	Authorities have identified the steps required to mitigate the negative effects, including water management and infrastructural adaption.
More than two decades after independence, Namibian society is still beset by unacceptable levels of inequality along the lines of gender, race, religion, ethnicity and class, according to the United Nations.	The New Equitable Economic Empowerment Framework (NEEEF) Bill, currently still in the consultation phase, strives to address inequality issues, but in its current form, it may hold adverse consequences for investment.

MEGA TRENDS	
Population	2,212,307 (July 2015 est.); Age 15 - 64: 64.56%
Population growth rate (%)	0.59% (2015 est.)
Life expectancy at birth	Total population: 51.62 years; male: 52.05 years; female: 51.18 years (2015 est.)
HIV/AIDS	Adult prevalence rate: 13.3%; People living with HIV/AIDS: 210,000 (2015 est.)
Adult literacy rate (age 15 and over can read and write)	Total population: 81.9%; male: 79.2%; female: 84.5% (2015 est.)
Urbanisation	Urban population: 46.7% of total population (2015); Urban population growth: 4.2% (2015)
Population below national poverty line	28.7% (2010 est.)
Unemployment rate	28.1% (2014 est.)
Employment (% of total)	Agriculture: 29.5%; Industry: 14.7%; Services: 55.8% (2014 est.)
Labour participation rate (% of total population ages 15+)	69.1% (2014 est.)
Business languages	English, Afrikaans, German
Telephone & Internet users	Main lines in use: 182,507; Mobile cellular: 2.44 million; Internet users: 493,566 (2015)
Sources: CIA World Factbook, World Bank, ITU, UNAIDS, Namibia Statistics Agency (NSA) & NKC Research	



Source: NKC Research

Risk environment / Risk outlook

Sovereign Risk Ratings		
S&P Global Ratings	**Fitch**	**Moody's**
N/R	BBB-/Stable	Baa3/Stable

Fitch Ratings reported on September 2 that it has decided to reaffirm its credit rating for the Namibian sovereign at an investment-grade "BBB-". The country's ratings are supported by *"a track record of political stability, slightly stronger governance indicators than rated peers, a net external creditor position, financing flexibility enhanced by access to South Africa's deep capital markets and a liquid banking system. However, it has a fairly low level of GDP per capita and economic development, high unemployment and inequality, and is vulnerable to shocks to commodity prices."* Fitch placed the "BBB-" rating on a negative outlook due to concern about a sharp widening in the fiscal deficit during 2015/16, a decline in revenues from the Southern African Customs Union (SACU), and an expected continued rise in government debt. Future developments that could result in a downgrade include a failure to narrow the fiscal deficit (leading to continued rise in government debt) and deterioration in economic growth.

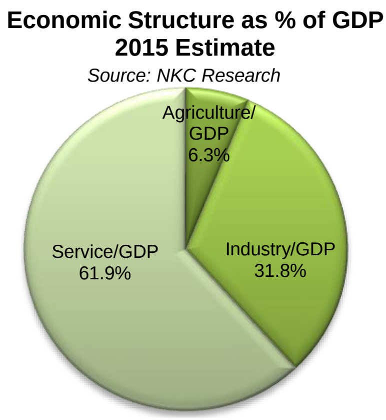
Moody's Investors Service rates Namibia "Baa3" with a stable outlook. Moody's said in a publication released on February 29 that *"high levels of unemployment, poverty and inequality threaten to undermine Namibia's implementation of a plan to reduce the public sector wage bill as part of a wider fiscal consolidation drive over the next three years"*. Nevertheless, the rating agency noted that the government's fiscal consolidation approach would be a 'credit positive' if successfully implemented, given that Namibia's public sector wage bill is *"among the highest in sub-Saharan Africa"*. On the economic front, Moody's noted that prolonged depressed commodity prices and subdued growth in South Africa are set to weigh on Namibia's economic expansion prospects this year. The rating agency again emphasised the aforementioned factors as key downside risks to the growth outlook in an announcement on May 19. Moody's further highlighted some concern about Namibia's external vulnerabilities, *"in particular the widening current account deficit that is financed increasingly by debt-creating flows combined with relatively low foreign exchange reserves under a pegged exchange rate regime."*

Infrastructure	Diversity of the Economy	Banking Sector	Continuity of Economic Policy	GDP Growth	Key Balances	Foreign Investment	Socio-economic Develop-ment	Forex Reserves
Limited due to low population density, but of good quality	Fairly diverse in African context	Small but developed & well regulated	Stable	Moderate to strong	Twin deficits	Strong	Moderate	Low, but still adequate to maintain peg

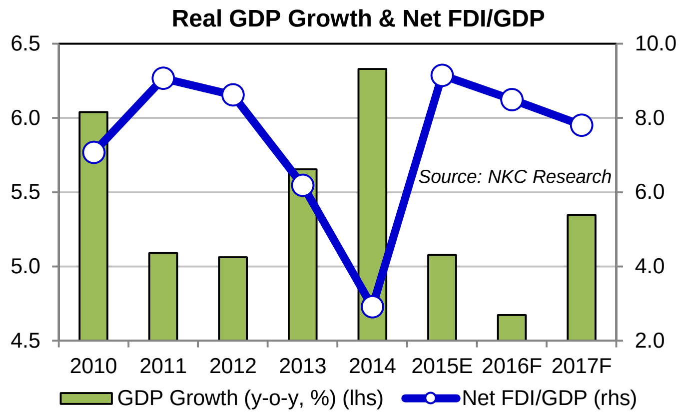
Stock Market	Listed Companies	Liquidity	Market Cap	Dominant Sector	Daily Trading Volume
Namibia Stock Exchange (NSX)	33 main board listings; 6 development board	Reasonable	N$1.64trn (main board, 22 July 2016)	Financials	1,225,919 shares (22 July 2016)
Capital Market	**Development**	**Liquidity**	**Maturity Range**	**Municipal Bonds**	**Corporate Bonds**
Yes	Developed in an African context	Reasonable	91 to 364 days (T-bills), 1 to 30 years (T-bonds)	N/a	Limited

Macro-economic overview

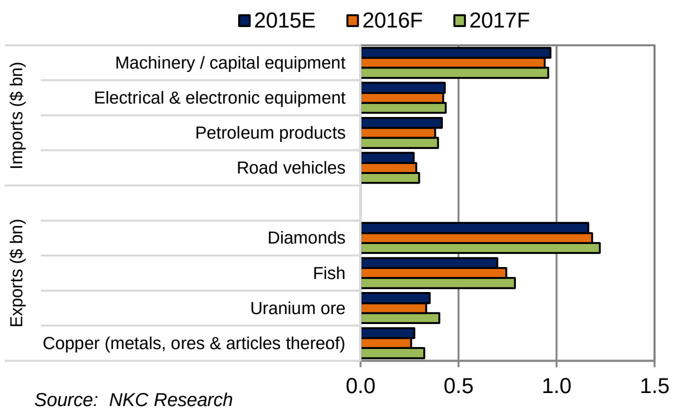
The Namibia Statistics Agency (NSA) released its final 2015 national accounts data on August 11. The NSA lowered its 2015 real GDP growth estimate from 5.7% to 5.3%. The Namibian economy looks set to face stronger headwinds this year, with the services sector in particular forecast to post slower growth in 2016. Higher inflation and tighter monetary policy will pressure disposable income levels, with adverse consequences for the demand side of the economy. Negative spill overs from the desert economy's neighbours may also play a role here. The South African economy finds itself facing ever stronger headwinds, while to the north, the Angolan economy is buckling under oil price pressures, with Namibian retailers already seeing a decline in turnover as less Angolans cross the border to buy Namibian goods. The industrial sector will also have to contend with challenges pertaining to higher input costs, water shortages and low-trending commodity prices (uranium in particular). Uncertainties regarding the New Equitable Economic Empowerment Framework (NEEEF) Bill may also adversely affect capital investment. That said, we expect industry to perform relatively well under these challenging circumstances, with mining activity set to rebound as production from the new gold and copper mines is ramped up. The Husab uranium mine was also formally opened in Q2, with production set to increase gradually before reaching capacity in 2018. The agricultural sector is also faced with various challenges. Besides the impact of the drought, livestock farmers have also had to contend with new export regulations imposed by South Africa. Taking all of the above into account, we forecast real GDP growth will slow to 4.7% in 2016, before rebounding to 5.3% next year.



The Bank of Namibia (BoN, the central bank) highlights that net foreign direct investment (FDI) increased significantly last year. More specifically, net FDI rose from N$4.7bn in 2014 to N$13.8bn in 2015. The sharp rise in foreign investment inflows is ascribed to *"debt/equity swaps by some companies in the mining sector."* In this regard, *"equity capital increased to N$11.4bn during 2015, compared to N$230m during 2014."* Reinvested earnings however declined by N$576m to N$463m last year, as operating profits of foreign-owned companies operating in Namibia were lower last year compared to the case back in 2014. Although commodity prices are forecast to rebound over the medium term, the recovery looks set to be a gradual process. As such, profit margins in the minerals industry will not rise sharply overnight, and companies that are not cost-effective may still need foreign capital to fund operations and/or expansion plans. As a result, we expect net FDI to remain relatively elevated this year, trending marginally lower to $0.96bn in 2016, down from $1.13bn in 2015.

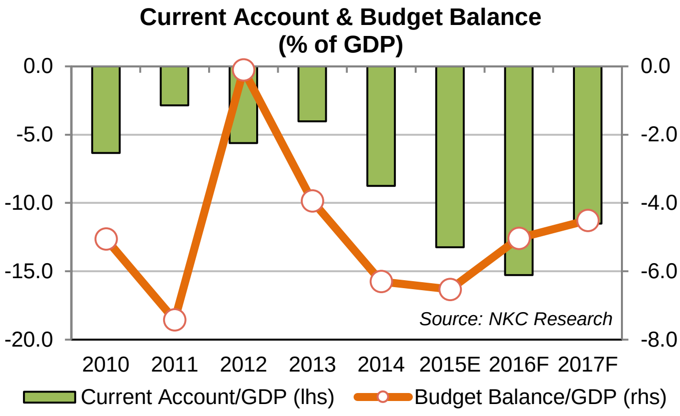


According to the NSA, the country's trade deficit narrowed during the first quarter of the year. Total exports in 2016 Q1 amounted to N$17.9bn, representing an increase of 31.2% compared to the value of exports recorded in the same quarter a year earlier. Imports amounted to N$22bn during 2016 Q1, up by 12.8% y-o-y from the N$19.5bn worth of imports recorded a year earlier. Namibia's trade deficit amounted to N$7.4bn in 2016 Q2, wider than the previous quarter but 37% narrower than a year earlier. Total exports in 2016 Q2 amounted to N$16.5bn, representing an increase of 3.5% y-o-y, driven by a significant rise in copper ore exports. Meanwhile, total imports in 2016 Q2 amounted to N$23.8bn, representing a decrease of 13.6% y-o-y. This decline is ascribed to a decrease in fuel and vehicle imports. When expressed in Namibia dollar terms, the country's trade figures may be slightly misleading due to the volatile exchange rate. When converted to US dollars, the figures indicate that Namibia's trade deficit narrowed during 2016 H1, due to a decline in imports outstripping the fall in exports.

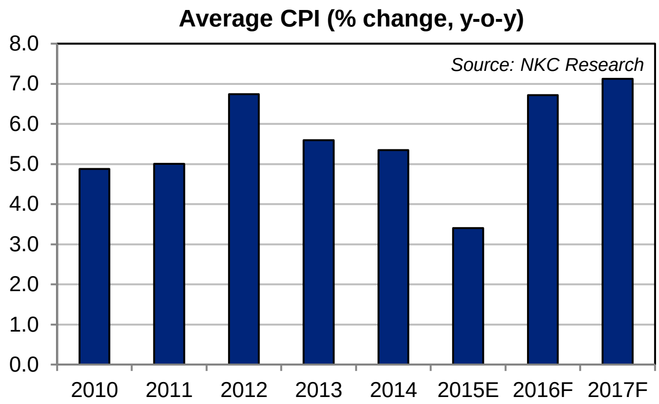


Main Imports: % share of total	2015E	2016F	2017F
Machinery / capital equipment	14.03	13.85	13.55
Electrical & electronic equipment	6.22	6.21	6.14
Petroleum products	6.02	5.61	5.59
Road vehicles	3.92	4.19	4.22
Main Exports: % share of total	**2015E**	**2016F**	**2017F**
Diamonds	28.93	28.86	27.28
Fish	17.37	18.16	17.60
Uranium ore	8.79	8.18	8.99
Copper (metals, ores & articles thereof)	6.82	6.31	7.25

We predict total exports will increase marginally to $4.1bn this year, supported by production being ramped up at the new gold, copper and uranium mines. The fact that exports declined in H1 (when expressed in US dollar terms) is somewhat concerning, but the effect of increased output from the new mines will likely be more pronounced in H2. We predict imports will decline from $6.9bn in 2015 to $6.8bn in 2016, as demand for foreign goods starts to wane in line with a weaker exchange rate and a tighter domestic monetary environment. As a result of the above, we see the trade deficit narrowing this year. That said, the anticipated fall in Southern African Customs Union (SACU) revenues will weigh on the transfers surplus – SACU customs and excise income has been an important source of foreign exchange earnings in recent years, but is expected to fall this year due to slower growth in South Africa and possible amendments to the revenue sharing formula. As such, we project a significantly smaller surplus on the combined invisible accounts. This will more than offset the narrower deficit on the trade account, translating into our forecast for the current account deficit to widen to 15.3% of GDP in 2016. The current account shortfall should however narrow to 11.5% of GDP next year as SACU revenues rebound and exports get a boost from a recovery in commodity prices and an increase in uranium production from the Husab mine.



Finance Minister Calle Schlettwein delivered his second budget speech on February 26. Overall, the latest budget projects an 8.3% decrease in revenue compared to the original projection under the Medium-Term Expenditure Framework (MTEF), reflecting a forecast reduction in SACU receipts. Total revenue and grants are budgeted at N$57.8bn for the 2016/17 fiscal year. In line with the government's consolidation efforts, authorities have reduced the expenditure envelope by 7.3% compared to the MTEF projection. The expenditure envelope for the 2016/17 fiscal year, budgeted at N$66bn, is also 1.6% lower than estimated actual expenditure in the previous financial year. As such, the government estimates that Namibia's fiscal deficit in the 2016/17 fiscal year will lie around 4.3% of GDP, narrower than the 4.6% of GDP deficit projected under the MTEF. Namibia is set to record its eighth straight annual fiscal deficit during the 2016/17 financial year. Our own projections are relatively in line with those provided by the finance ministry, although weighed to the more pessimistic side – it is worth noting that authorities have consistently missed fiscal deficit targets in recent years. More specifically, Namibia's fiscal deficit is forecast to narrow to 5% of GDP in the 2016/17 fiscal year.



Inflation trended broadly higher in 2016 H1, rising from 5.3% y-o-y in January to 6.7% y-o-y in June, mainly ascribed to a rise in transport costs and higher food prices. In response to mounting inflationary pressures, the BoN raised the repo interest rate by a cumulative 50 bps in H1. However, despite inflation rising to 7% y-o-y in July, the apex bank opted to keep all policy instruments on hold following the most recent Monetary Policy Committee (MPC) meeting concluded in August. According to the BoN, this decision was necessary to support the country's economic growth, particularly in light of the *"slow and fragile recovery in the economies of Namibia's trading partners."* The decision by the central bank to hold off on further tightening was largely expected given the recent strength exhibited by the Namibia dollar (pegged to the South African rand) and the associated impact thereof on the inflation outlook. That said, the BoN's monetary policy statement was more dovish than originally anticipated, with the regulator placing significantly more emphasis on the slowdown in economic activity on the domestic front. Regardless, we maintain our view that the balance of probability is still leaning towards further tightening later this year. Upside risks to the inflation outlook include a weaker exchange rate in Q4 (dependent on emerging market sentiment and moves by the US Federal Reserve), elevated food prices on account of the drought and/or a rebound in crude oil prices. Tightening by the South African Reserve Bank (SARB) may also prompt the BoN to take action in defence of the currency peg. We forecast inflation will average 6.7% in 2016, up from 3.4% in 2015.

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