IJG SECURITIES

# ECONOMIC OUTLOOK 2019

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# Contents

# Executive Summary

The year 2018 was another lost year for the Namibian economy. The latest quarterly GDP release shows that after the first three quarters of the year the Namibian economy had contracted by a further 0.4% on a year-to-date basis. This follows a contraction of 0.9% in 2017 and brings the consecutive quarterly contraction count to ten. Although negative growth has been seen for 10 consecutive quarters, some upward revision is likely in 2018 mining output as diamond and uranium production has exceeded expectations. Our full year "nowcast" for 2018 shows very subdued, but positive, growth of 0.2% for the year, down from the 0.9% we expect in our 2018 Outlook.

| Real GDP Growth Rates | Actual | | | Nowcast | | Forecast | | |
|---|---|---|---|---|---|---|---|---|
| Industry | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
| Primary industries | -1.6 | -5.2 | -1.5 | 11.1 | 8.3 | -6.9 | 6.7 | 2.0 |
| Secondary industries | 10.9 | 6.8 | -6.4 | -6.7 | 0.9 | 3.4 | 3.9 | 3.0 |
| Tertiary industries | 7.7 | 7.9 | 3.2 | -1.4 | -1.6 | 2.4 | 2.4 | 3.7 |
| GDP at market prices | 6.4 | 6.1 | 0.6 | -0.9 | 0.2 | 0.9 | 3.4 | 3.4 |

*Source: NSA, IJG Securities*

A rough GDP per capita calculation shows that, by this measure, the Namibian economy has been in a deeper contraction for a longer period of time. The standard of living of the average Namibian has been deteriorating for three years as real output growth has lagged population growth, and there is little chance of a reversal of this trend in 2019. Our forecast is for the economic growth of 0.9% in 2019, with most of the growth expected in the latter part of the year. Population growth of 2.2% means that GDP per capita will decay further still. Adding to the falling living standards is our view that unemployment continued to rise in 2018.

We started 2018 cautiously optimistic for a modest economic recovery. In the outturn section of this report we unpack why this optimism was misplaced. We expected to see growth of 0.9% in 2018, led by primary industry expansion, primarily stemming from diamond and uranium output growth. These expectations were exceeded as data from the Chamber of Mines shows diamond production rose by 15.2% versus our forecast of 12.6%, and uranium output rose by 68.7% versus 60.8% forecast. While mining output exceeded forecasts, agriculture and fishing underperformed our expectations. Our "nowcast" indicates that both industries contracted by more than expected in 2018. We previously forecast overall growth of 10.6% for primary industries in 2018, which we have now revised down to 8.3%.

Our expectations for growth in secondary industries in 2018 is unchanged from 0.9% last year. How we get to that number has, however, changed. We forecast a rebound in manufacturing output, driven by a modest recovery in consumer confidence, as well as mining and exploration activities having a positive impact on the industry. At the same time, we expected to see a further contraction in construction activity. We now expect to see a contraction of 2.8% in manufacturing activity in 2018, and growth of 5.9% in construction. The contraction in manufacturing can be attributed to, amongst others, a decrease in copper cathode and sulphuric acid production, a decrease in demand for beverages and meat, and less grain processing, by our estimates. The growth in construction activity was largely as a result of delays in completing various public projects in prior years which drew to a close in 2018. The electricity and water industries have also outperformed our expectations.

We forecast a contraction of 1.6% in tertiary industries in 2018, slightly down from a contraction of 1.4% expected previously. Tertiary industries make up the bulk of the Namibian economy and are heavily affected by consumer demand and confidence. Consumer confidence remained depressed in Namibia as retrenchments continued, weighing on tertiary industries such as wholesale and retail trade, financial intermediation, and other business services. It comes as no surprise that these industries have been struggling after numerous difficult years experienced by high multiplier industries such as construction and manufacturing. Government's fiscal consolidation drive was the cherry on the cake, reducing the growth in funds injected into the economy by the fiscus, and contributing to the drag on growth in tertiary industries.

For 2019 we expect only a very modest recovery in economic activity as the structural issues which have resulted in the protracted nature of the recession, remain for the most part. Government is unable to provide meaningful stimulus to the economy due to persistent large budget deficits and slow revenue growth. Monetary stimulus is largely out of the question although interest rates remain accommodative by historical standards. And finally, the policy overhang which has done so much damage to investor and business confidence continues to be a source of uncertainty. With these factors weighing on the economy we expect real GDP growth of 0.9% for 2019, which will see per capita GDP decline further, indicating a tough year ahead for many Namibians.

We expect primary industries to contract by around 6.9% in 2019, driven by contractions in agriculture as well as mining and quarrying. Agriculture is highly dependent on the rainfall and the very slow start to the 2018/19 rainy season is already putting pressure on the industry. Poor rainfall threatens maize and mahangu production as well as grazing conditions. Given these considerations our forecast of a contraction of only 2.3% in agriculture may seem optimistic, but this is largely due to base effects from the expected contraction in 2018. Fishing is expected to post growth in 2019, albeit from a low base.

We forecast a contraction of 11.0% in the mining industry in 2019, driven by decreased output from uranium and diamond mining. The Langer Heinrich mine went into care and maintenance in August 2018, removing a large amount of uranium production. The Husab mine will continue ramping up to full production, but this is taking longer than expected and the increase in output expected from Husab in 2019 only partially offsets the decrease attributable to Langer Heinrich's exit. Uranium prices remain low and have weighed on the sustainability of the Namibian mines. Diamond mining output will be similarly impacted by the closure of the Elizabeth Bay mine, as well as routine maintenance of vessels. Both uranium and diamond mining output are expected to rebound in 2020 as operations normalise.

We expect reasonable growth from secondary industries in 2019 with construction expected to gain some momentum, development of water and electricity infrastructure to continue, as well as a rebound in copper cathode production. Construction activity is coming off a low base after large contractions in 2016 and 2017. While government has not meaningfully increased infrastructure expenditure for the 2019/20 budget year, funds from the African Development Bank (AfDB) and other development institutions have been allocated to infrastructure projects, aiding growth. Government's budget for the year is likely to see revisions in March, and as it is an election year there may be an incentive to increase expenditure, possibly leading to the resurrection of projects put on hold in prior years due to the fiscal consolidation drive.

Manufacturing in Namibia is forecast to grow at 1.4% in 2019. We expect copper cathode production to improve this year after water ingress at the Tschudi mine resulted in decreased output in 2018. Beverage production is also likely to post growth after multiple years of contraction. This is more due to base effects than anything else, but we do expect an increase in beverage sales due to election related events. The decrease in diamond production expected this year will lead to some drag on manufacturing output due to a reduction in cutting and polishing. The conditions for manufacturing in Namibia remain challenging as local manufacturers compete with foreign companies which benefit from scale advantages amongst other things.

Tertiary industries have contracted for two consecutive years, reflecting subdued consumer and business confidence. Unemployment has increased greatly since the economy started cooling in the latter half of 2015, taking its tole on sectors such as wholesale and retail trade and services industries. We forecast a modest recovery in these industries due to expected increases in government and state-owned enterprise wage bills, some improvement in consumer confidence due to unemployment bottoming out as businesses find a balance between supply and demand, as well as a low base due to prior year contractions.

The forecast contraction in primary industries is expected to be offset by growth in secondary and tertiary industries in 2019. This muted growth should be supported by stable interest rates in South Africa and Namibia by extension. Should rates remain at the currently accommodative levels, we would expect to see some improvement in credit extension, first from consumers and towards the latter part of the year from businesses. Downside risks to the interest rate outlook (higher rates) are plentiful however with a myriad of potential external shocks looming which may impact the South African currency and inflation outlook. South African elections are widely expected to result in President Cyril Ramaphosa and the ANC remaining in power and the Ramaphosa faction of the ANC gaining a stronger grip on policy direction. There has been much talk from the president regarding strategies for improving economic growth in South African, but as yet there has been little to show for it. We expect to see Ramaphosa and the ANC remain in power, but what comes thereafter will indicate whether talk is cheap or whether the president has more up his sleeve in the form of structural reforms to government, SOEs and policy.

The trade war between the US and China is a geopolitical threat to global trade which poses a risk to the fragile Namibian economy. The impact on China's demand for commodities is likely to have knock-on effects on commodity producing countries such as Namibia and South Africa. A substantial fall in commodity prices is a possibility and would lead to rand depreciation. This in turn may drive inflation, although the impact is likely to be partially offset by lower oil prices in such a scenario. Should the trade war lead to a drop in commodity prices and cause inflation to rise in South Africa, it is likely that interest rates will be hiked. Interest rate hikes in South Africa would be replicated by the BoN and thus put pressure on Namibia's recovery.

A more direct threat to Namibian industries may be Brexit and the outcome of negotiations surrounding the trade agreement that would replace the Economic Partnership Agreement (EPA) between SACU and the EU. Currently Namibian exports to the UK are governed by the EPA but Brexit will see an end to this agreement regarding trade with the UK. SACU is negotiating for a replication of the EPA with the UK which would effectively ensure that trade with the UK will continue as before. All indications are that these negotiations are progressing well as at the time of writing, but should they not be concluded before the 29 March Brexit deadline, Namibian trade with the UK would revert to World Trade Organisation (WTO) rules, impacting Namibian exports negatively. Of particular concern is the impact that such a scenario may have on beef exports. It is however not our base case expectation that the trade agreement between SACU and the UK will not be concluded in time for the deadline.

In summary, 2019 is unlikely to bring widespread relief to the Namibian economy. While interest rates remain accommodative and government spending is likely to be increased slightly this year, large twin deficits continue to erode the fiscal position and policy uncertainty weighs on investor confidence. Government debt is likely to increase more than the finance ministry forecast in last year's mid-term budget, leading to a larger interest burden in future years. In order to fund this year's spending increase and future deficits, government will be forced to increase taxes. Proposals for such tax amendments were already made in March 2018. Given the stagnant growth environment, an increase in taxes will add to the drag on growth rather than enable fiscal stimulus in our view.

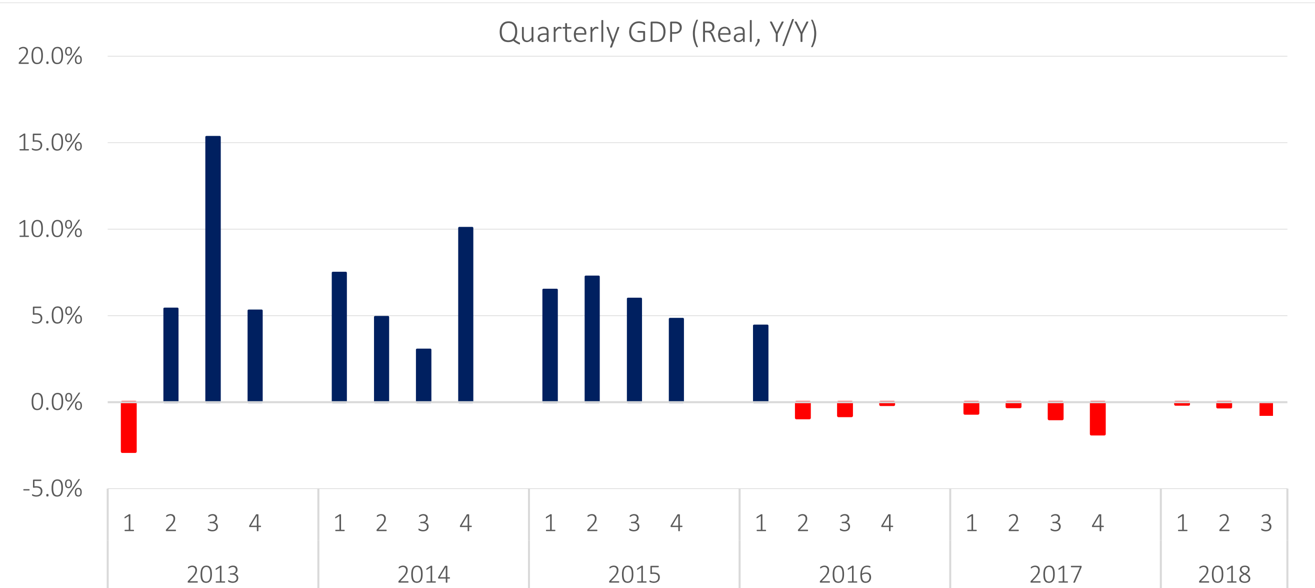
It is not all doom and gloom however, as simple fixes are available. The most obvious being policy clarity. Certainty regarding the investment promotion act and empowerment legislation (NEEEF) will in itself generate some confidence in the business climate. Should these pieces of legislation prove to be investor friendly and be enacted early in 2019 we believe that there is much latent investment potential, from both foreign and local sources, which could be deployed relatively quickly. Clarifying the policy environment is thus key to resuscitating the Namibian economy in our view. Removing the proposal to increase taxes will also be positive for business and investment alike. These are the tools available to government at present and, wielded correctly, can have a positive impact on the Namibian economy.

# Outturn of 2018

Contrary to our expectations for subdued - but positive - growth for 2018, the Namibian economy continued its search for a bottom to what has become a long-winded recession. We expected primary industries, primarily mining, to drive growth in 2018, supported by marginal growth in secondary industries, and only a modest contraction in tertiary industries. Global growth forecasts pointed to a favourable macro-environment with developing economies leading the growth charge despite monetary tightening in the US (although offset by fiscal easing). This favourable environment and a growth surprise in China in 2017 led to an optimistic outlook for commodity prices and the impact on commodity producing countries such as Namibia. As well as this an increase in diamond and uranium output was expected.

Our muted optimism was short lived as commodity prices broke their upward trend on the back of deleveraging in China, as well as US-China trade tensions. The second half of the year saw the trade war between China and the US in full swing after months of threats and inconsequential action, resulting in further market uncertainty and drops in commodity prices. A depreciating domestic currency helped to alleviate some of the pressure on Namibian commodity producers and Q3 GDP data (latest at time of writing) confirmed that mining output grew as anticipated at over 10% y/y. Dampening the positive performance from the mining sector are expectations for relatively flat performance from agricultural and a contraction in fishing output.

Despite the growth in mining output in 2018, much of the multiplier benefits from the increase in mining capacity on the services and construction sectors were reaped in prior years during the construction phases of the Tschudi, Husab, and Otjikoto mines. Increased output did however bolster exports, supporting the reserve position to some extent. The completion of the construction of the three aforementioned mines in earlier years created a high base of activity with strong multiplier effects which was always going to be challenging to maintain. Large scale government works projects such as the Neckartal Dam, fuel storage facility, and various road upgrades contributed further to this base. The contraction in high multiplier activities such as construction was largely responsible for the contraction experienced in tertiary industries in 2017 and 2018.




*Source: NSA*

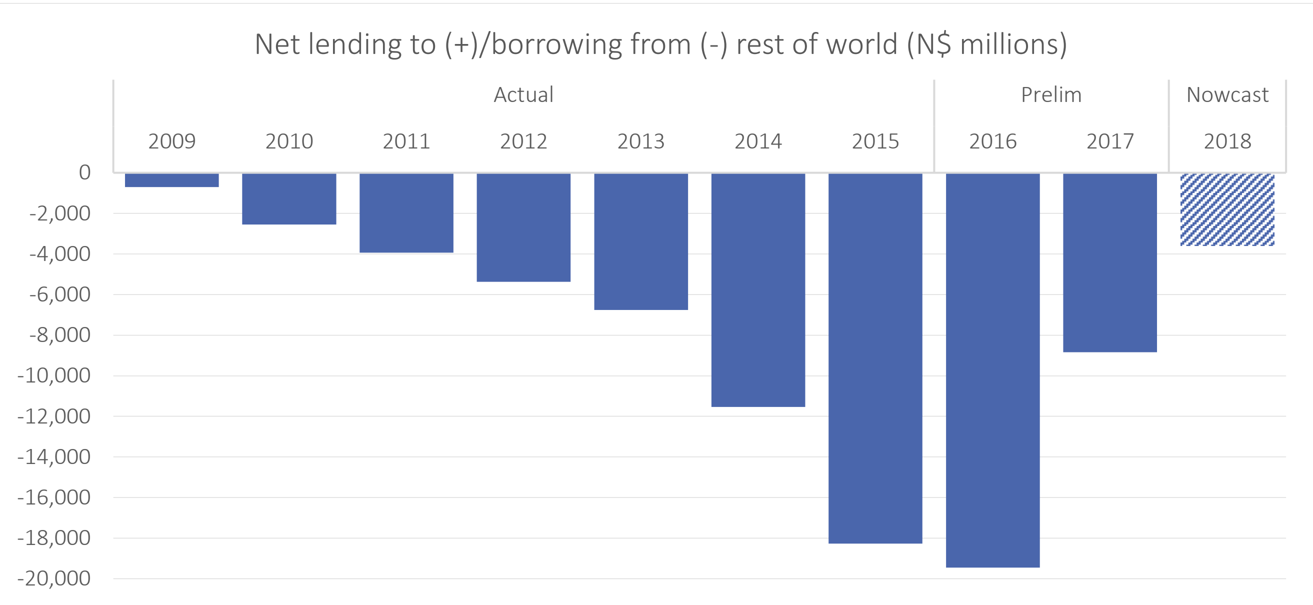
Q3 2018 GDP statistics point to a year-to-date contraction in real GDP of 0.4%, well below our expectations of 0.9% growth (from our February 2018 Outlook document where we were notably among the most pessimistic forecasters). With Q4 and full year GDP releases still some way out we see it as unlikely that 2018 will record positive real GDP growth when the full year data is released later this year. The Bank of Namibia's latest expectations are for a contraction of 0.2% in 2018 as a whole.

Quarterly GDP has recorded 10 consecutive quarters of negative annual growth, making the current recession abnormally prolonged. The deep trough is the result of procyclical fiscal and monetary policy contributing to the overheating of the economy in 2015. Various factors contributed to the onset of the current recession (commodity price decline, drought, etc), but the magnitude and length of recession is largely the result of the unwinding of a debt fuelled overheating of the economy. Private sector debt grew at a CAGR of 15.3% between 2012 and the end of 2015, almost doubling over the period. The increase in government debt was even more rapid, rising by a CAGR of 33.9% between April 2011 and March 2016.

These high rates of credit uptake supported the abnormally high growth rates over the period between 2011 and 2015. Credit alone was not responsible for the strong real growth, but rather served to amplify the cycle.

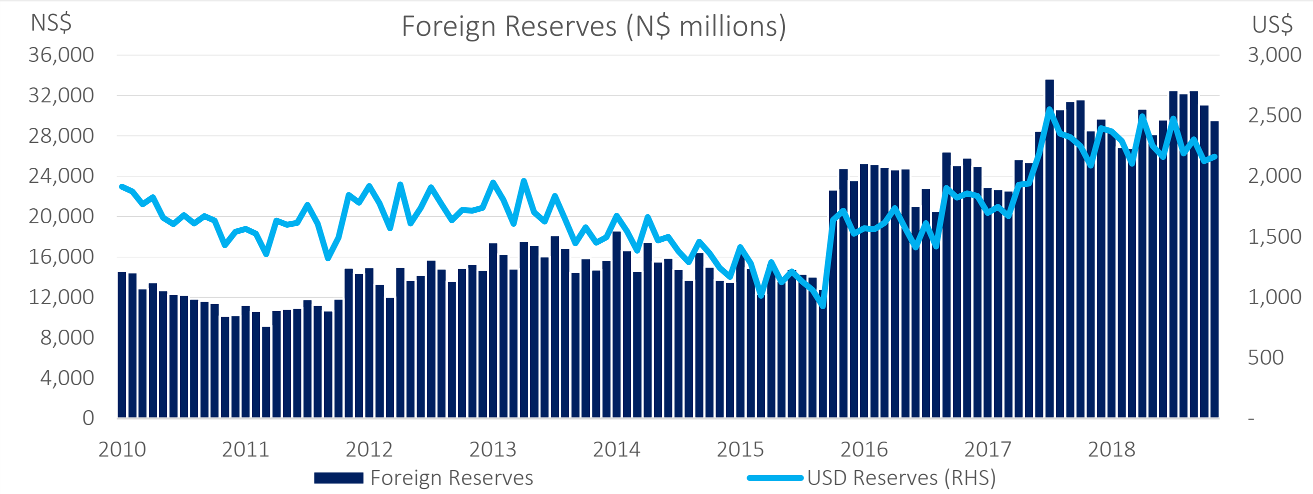
Monetary policy remained accommodative during 2018 with interest rates remaining unchanged for the year. The Bank of Namibia chose not to follow the SARB's rate cut in March, nor did it hike rates following the SARB's November hike. Namibian repo and prime rates are currently only 1.25% above the historic lows of 2013 and 2014, yet there has been a marked slowdown in credit extension. The annual rate of private sector credit extension (PSCE) fell as low as 5.0% y/y in January 2018, a far cry from the 15+% y/y growth rates of 2014 and 2015. PSCE growth rebounded somewhat from the lows as the year drew on, with the November growth rate coming in at 8.0% y/y. The quality of the 2018 growth in private sector credit is however questionable, with much of the acceleration attributable to shorter term loans and overdrafts. Mortgage credit extended to individuals is recording some of the lowest growth rates in over a decade and the subdued uptake of productive credit by corporations is a clear indication that business confidence is depressed. It must also be said that banks have not lent as freely as in the past in an effort to contain risk, which, although prudent, has impacted the availability of credit and thus contributed to the slowdown in economic activity.

The slowdown in credit extension and decrease in foreign direct investment (FDI) flows into Namibia since 2016, coupled with increased mine output, has resulted in a reduction of the trade deficit to below 2013 levels. Q3 2018 data shows that the current account deficit also narrowed, to N$757 million, versus N$2.7 billion in the corresponding quarter of 2017 which was less than half that of Q3 2016. The reduction in the trade deficit is the main reason for the improved current account deficit. While a reduced deficit is an improvement and relieves much pressure off of the central bank and finance ministry, the improvement is attributed largely to a drop in demand for imports rather than a major increase in exports. Mining output has improved, but not sufficiently so to offset the growth in demand for imports, and the trade deficit thus remains large. As a result, Namibia has continued to borrow from the rest of the world, although at much reduced levels when compared to 2016 and 2017.




*Source: Bank of Namibia*

Namibia's international reserve position held up reasonably well in the current environment as might be expected with a decrease in consumer demand. The stock of international reserves stood at N$29.5 billion at November 2018, up around N$1 billion over the previous year. While the Namibia dollar fluctuated between 11.7 and 14.7 to the US dollar over this period, it ended pretty much where it began with little change in the US dollar value of reserves as a result.

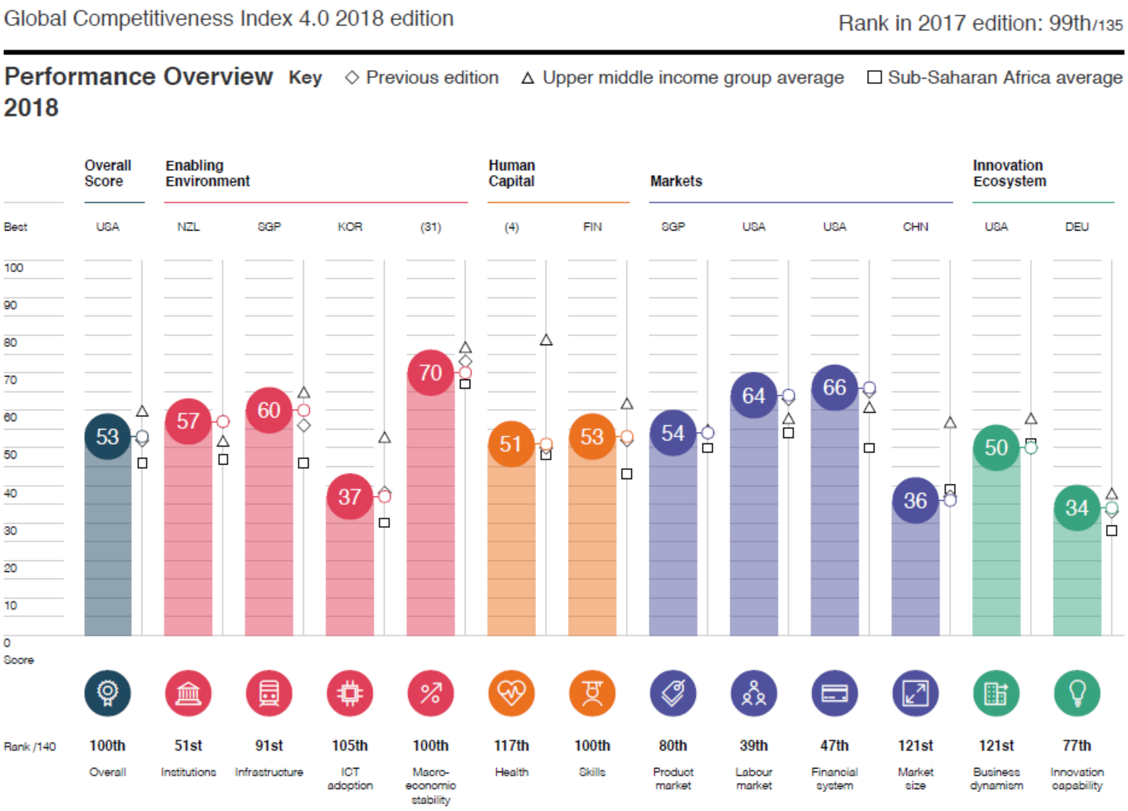



*Source: Bank of Namibia, IJG*

Government continued 2018 with its “pro-growth fiscal consolidation” efforts of the last few years. This involved capping public expenditure while continuing to run a large deficit in an effort to avoid creating a further drag on economic activity. This process has not seen the containment of recurrent consumptive expenditure but rather seen a reallocation of funds from the development budget to the operational budget, while keeping within the overall budget ceiling. Such a reallocation was once again prioritised in the mid-term budget tabled in November which saw N$1.77bn moved from the development budget to the operational budget. This shortfall on the development budget is to be filled through loans from the African Development Bank, but these are once-off (two tranches of N$2bn), and the operational expenditure is likely to be recurrent. Overall the process of pro-growth fiscal consolidation has not brought about enough structural change to the public expenditure profile to increase productive capacity and the fact that government has been running large deficits has also resulted in a rapid increase in government debt over the last four years.

A positive to come from the forced fiscal consolidation is the hiring freeze in the civil service which has been ongoing since the 2016/17 fiscal year. Government started a process of identifying redundant positions in 2017 which has resulted in internal transfers to fill vacancies, helping to stem the ballooning of the civil service. Another positive is the improved accuracy of budget forecasts which have contained more reasonable revenue and expenditure growth assumptions than prior to 2017. As such funding shortfalls are less likely, and should they occur, will be easier to resolve. The finance ministry has also been open to private sector engagement and the minister has managed to keep expenditure forecasts in check leading up to an election year which is encouraging.

Namibia slipped one place in the World Economic Forum’s (WEF) Global Competitiveness Index (GCI) in 2018, placing 100th out of 140 countries. Ironically Namibia, the second most sparsely populated country, placed one point below Mongolia, the most sparsely populated country. Various index components show that Namibia has the potential to move up the rankings in a meaningful way should a few key weaknesses be addressed. Components in which Namibia ranked highly include institutions (51$^{st}$), labour market (39$^{th}$), and financial system (47$^{th}$). The figure below unfortunately highlights the many components of the GCI where Namibia is lagging both peers and the rest of the world. Government refers to the GCI rankings in various development documents (Harambee Prosperity Plan, NDP5, etc) yet Namibia is slipping in the rankings. Some areas which are notably holding Namibia back in terms of competitiveness are the homicide rate (128$^{th}$), quality of land administration (110$^{th}$), electrification rate (116$^{th}$), exposure to unsafe drinking water (103$^{rd}$), life expectancy (116$^{th}$), skills (100$^{th}$), ease of hiring foreign labour (136$^{th}$), time to start a business (135$^{th}$), and quality of research institutions (111$^{th}$). The World Bank’s Ease of Doing Business rankings show a similarly stagnant picture with Namibia ranking 107$^{th}$ out of 190 countries. These indices/rankings play a role in investor decision making and are often the first point of reference for foreign investors when assessing opportunities. This data thus plays an important role in the investment decision making process over and above providing a benchmark for policymakers with which to measure relative progress.




*Source: World Economic Forum, Global Competitiveness Report (2018)*

Namibia is suffering from a lack of business and consumer confidence. Part of the reason for the continuation for this lack of confidence is the own goals scored by government on the policy front. Investor unfriendly policies such as NEEEF and the Namibian Investment Promotion Act (NIPA) remain an overhang to the investment environment. The fact that these policies, amongst others, remain on the table makes for increased uncertainty regarding the safety of investing into Namibia. Investors do not like uncertainty as it raises the cost of investment and often deters some investments completely, as has been the case with the current policy environment in Namibia. At the start of 2018 we hoped to gain clarity regarding the implementation of these policies, but this has not happened, causing needless uncertainty. Similarly, the tax reforms proposed in the March budget are investor negative as they aim to extract more tax from the population in order to fund a consumptive government. The investment climate for local and foreign direct investment thus remains murky at best, hampering economic recovery. Policy will thus be a major factor in whether or not the Namibian economy continues to stagnate in 2019.

# Key Themes for 2019

Each year we explore a few key themes which are likely to affect the outlook for the year on both a global and national scale. International developments such as the escalating trade war between the US and China affect commodity prices and as such have an impact on commodity currencies such as the rand and the Namibia dollar. Brexit is another factor which will have an impact on trade and demand and we unpack what the risks are and how they may impact Namibia and her trading partners. Developed market (DM) monetary tightening and the impact of this on global liquidity is likely to impact emerging market asset prices. Finally, local and regional developments such as Namibian and South African elections will impact policy, and by extension investor confidence going forward.

## Trade Wars

2018 saw US president, Donald Trump, acting on his 2016 presidential campaign promise to renegotiate trade agreements he deemed to be unfair to the US in an attempt to reduce the nation's trade deficit. His strategy has thus far been to impose tariffs on several specific goods traded (and strangely not traded) with some of the US' biggest trading partners and to renegotiate trade deals with them. As expected, many of the US' trading partners have since imposed retaliatory tariffs, escalating the dispute into a full-blown trade war.

### China

One of Trump's main targets from the start has been China. Since his campaign Trump has promised to address China's "long time abuse of the broken international system and unfair practices". Trump isn't wrong in accusing China of unfair trade practices. Even though China joined the World Trade Organisation in 2001, the country has done little to ensure that trade with its partners is fair. Some of these unfair practices include currency manipulation, dumping, providing uncompetitive export subsidies, and forcing US companies to create joint ventures with Chinese companies if they wish to build plants in China and then forcing them to share their intellectual property.

Chinese Vice Premier Liu He, US trade representative Robert Lighthizer, and US Treasury Secretary Steven Mnuchin are expected to meet at the end of January in an attempt to settle the ongoing trade dispute. The presidents of the two countries agreed in December to temporarily suspend any additional tariffs until 28 February 2019. If no agreement is reached before then, current tariffs on US$200 billion worth of Chinese goods will increase to 25% from 10% at present. Whether the US and China will come to an agreement remains to be seen, as the US Commerce Secretary Wilbur Ross has recently said that the US is "miles and miles" from a trade deal with China, thus raising the probability of further escalations in trade tensions before a final agreement is reached. The US might, however, postpone the tariff hike if it believes that China has made significant progress in addressing some of its prior practices.

The US has thus far imposed tariffs on US$250 billion worth of Chinese goods, including solar panels, washing machines, steel, aluminium, printed circuit boards, and various automotive parts. China has retaliated by imposing tariffs on US$110 billion worth of US goods. China imports US$130 billion worth of goods from the US annually, compared to over US$500 billion worth of exports. Further retaliatory measures from China would likely include increases in existing tariffs or other non-tariff barriers. The IMF has warned that if tensions persist China's economic growth would drop below 5% in 2019, compared to the current forecast of 6.2%.

### Europe

Trump has also taken on the European Union (EU) after criticising the bloc for having a trade surplus of US$150 billion with the US, and for having a 10% tax on imports of US vehicles, compared to the 2.5% rate charged by the US. Trump hit the EU with 10% tariffs on steel and 25% on aluminium in June last year.

The EU quickly retaliated with tariffs on US$3.2 billion worth of iconic US goods such as Harley-Davidson motorcycles, bourbon whiskey and Levi Strauss jeans. Trump and European Commission President Jean-Claude Juncker however soon afterwards agreed to a truce not to levy any new tariffs on one another while negotiations are underway. The US wants to negotiate a deal to expand European imports of US liquefied natural gas and soybeans and to lower industrial levies.

The threat however remains that Trump will impose tariffs of up to 25% on EU manufactured vehicles and automotive parts this year should he feel that the bloc is not importing enough US goods to narrow the trade surplus the EU has with the US. Such a move would significantly escalate trade tensions as the value of EU vehicle exports to the US is about 10 times greater than that of the EU's steel and aluminium exports combined.

These tariffs will mostly affect Germany, the EU's largest economy, and Europe's top car exporter. The EU is however prepared to hit back with tariffs on US$22.7 billion worth of US goods. According to analysis by the European Commission, a 25% tariff would add about €10,000 on average to the purchase price on EU built cars sold in the US. Such a tariff would cut US imports of European vehicles and automotive parts in half, according to a forecast by the commission.

The long-term trading relationship between the US and EU thus remains fragile, as the US is unpredictable and is a strong believer of using tariffs as leverage.

## Mexico and Canada

In 2018 Trump also acted on his campaign promise to repeal the North American Free Trade Agreement (Nafta). On 30 November, the leaders of the three countries signed the US-Mexico-Canada Agreement (USMCA) to replace Nafta, which Trump hailed as the "worst deal ever made". The USMCA maintains duty-free access for agricultural goods between the three countries and eliminates other non-tariff barriers.

Under Nafta, Canada had restrictions on the quantities of milk and other dairy products that could be imported from the US. The USMCA opens up Canada's dairy market to US farmers by setting higher quotas for the US which will increase market access for US dairy producers. Canada also agreed to remove a policy that made it cheaper for Canadian producers to buy domestic ultra-filtered milk, used to produce yogurt and cheese. Canadian farmers see this as a way for US dairy farmers to dump their surplus product in Canada. At face value, this amendment should however be positive for consumers as it will lead to cheaper dairy products.

The new agreement also requires that about 45% of automotive parts be made by workers earning at least US$16 an hour. The goal is to stop manufacturers moving their operations to Mexico where workers earn much less than their US counterparts, thus making it cheaper for manufacturers to produce their vehicles there. The agreement also requires 75% of a vehicle's parts be made in North America, an increase from the current 62.5% requirement. These two changes are negative in our view as they are likely to lead to an increase in production costs and subsequently, more expensive vehicles which could lead to fewer vehicles produced in Mexico and job losses for the industry in that country.

The new trade agreement will come up for review every six years, which will give the US leverage to make sure that it still is to its liking. The new agreement is expected to take effect on 1 January 2020, after all three governments give it their approval.

### *The Impact of Trump's Protectionism*

Trump's protectionist policies are likely to have a negative effect on the world economy, with China's economy already experiencing a slowdown as a result of the tariffs imposed to date. The slowdown in China will have knock-on effects on other countries, particularly commodity exporters, as demand for these commodities from China will fall, weighing on earnings and output. The tariffs will cause prices of various products such as appliances, machinery and vehicles to rise as manufacturers will have to pass along higher input costs to consumers.

Should the tariffs cause inflation to accelerate at a faster than expected rate, the Federal Reserve will have to step up its interest rate hiking cycle which will ultimately lead to the depreciation of the rand relative to the US dollar. A weaker rand will further increase the cost of imports which will filter through to the Namibian economy as Namibia imports most of its inflation from South Africa through the currency peg.

A further threat to South Africa is the US's position on the African Growth and Opportunity Act (AGOA) which gives Sub-Saharan beneficiary countries duty-free access to the US. Trump's import duties on aluminium and steel last year did not exempt South Africa, increasing the risk that the country's AGOA duty-free privileges will be suspended at some point in the future, or that the US will decide not to renew the act when it expires in 2025.

Tariffs add friction to trade which leads to a decrease in total trade volumes. This means that less of certain products are consumed. Less products consumed, all else equal, means that living standards are decreasing and less people are being employed. These impacts are often experienced in countries or regions not directly targeted by the tariffs such as Namibia. As a small open economy with a trade deficit Namibia is particularly prone to impacts such as declines in commodity prices. A weak fiscal position means that external shocks such as a decline in commodity prices are likely to add severe pressure to an already ailing economy, with little that can be done by government to alleviate the situation. It is for this reason that the threat of further tariff action poses a major downside risk to the fragile Namibian economy and the outlook for 2019.

## Brexit

With the 29 March 2019 deadline approaching fast, much uncertainty still hangs in the air regarding the path the UK will take to leave the EU. With the EU and the UK struggling to reach a consensus on a number of issues, and UK Members of Parliament (MP's) divided, Brexit negotiations have been extraordinarily difficult.

## Possible Scenarios

1. UK manages to sign deal with the EU

Even though Teresa May's Withdrawal Agreement was voted down by the UK parliament last month, we still see this scenario as the most likely outcome. If it eventually passes, it will mean that the UK will enter a transitionary period whereby current EU rules and tariffs will apply to it as if the UK were still a member of the EU, in order for the two parties to finalise the details of their new post-Brexit relationship. UK MPs however have a problem with the current agreement's "backstop" solution to avoid a hard border between Ireland and Northern Ireland. This backstop will come into force if the EU and the UK fail to reach a long-term agreement on a free trade deal that would make trade frictionless during the transition period. The backstop will keep the UK in a "single customs territory" with the EU, but will leave Northern Ireland in the EU's single market. UK MPs have criticised the backstop arguing that it will lead to different regulations for Northern Ireland compared to the rest of the UK and that the UK would not be able to leave the backstop without the approval from the EU. May returned to Brussels in an attempt to renegotiate some of the terms of the Withdrawal Agreement, but it remains to be seen whether the EU will allow any changes to the agreement, as it has already indicated that it is not willing to renegotiate it.

2. No-deal Brexit

A 'no-deal Brexit' would not be an intentional choice but rather an accidental outcome of a government unable to obtain a majority vote for an alternative solution. Avoiding this scenario seems to be the only thing British MPs are currently united on, since it would likely have dire consequences for businesses and the wider economy. Without a formal bilateral trade agreement in place, Britain would need to adhere to World Trade Organisation rules without a transition period, introducing customs checks and tariffs. The IMF has warned that this would "bring about output losses of around 5 to 8 percent compared to a no-Brexit scenario in the long run."

3. EEA Membership (The Norway Option)

Under a Norway-style Brexit, Britain will leave the EU, join the European Free Trade Association (EFTA) and then become the 31st full member of the European Economic Area (EEA). This will allow the UK to continue having full access to the single market, but it will have less say in the rules that it has to adhere to. According to the government's own Brexit impact assessment, this option would be least damaging in terms of economic harm. This would however mean that the UK has to continue making contributions to the EU budget.

4. Second Referendum

We see the probability of a second referendum taking place as unlikely. It would firstly be a time-consuming process for parliament to pass a bill for the second referendum (the 2016 referendum took seven months to pass), let alone the time required to organise campaigns and to hold the vote itself. This will not be possible to do before 29 March 2019. Secondly, there would be a lot of debate on what the actual question of a second referendum should be. This scenario will likely cause even more uncertainty, division and disruption.

5. No Brexit

Although not entirely impossible, we see it as a highly unlikely scenario that the UK government will ignore the referendum result and backtrack all progress made so far.

## Implications for SACU and Namibia

Irrespective of which Brexit route the UK decides to take, trade between SACU member countries and the UK should be little affected. The UK has been in discussions with SACU countries since 2017 to reaffirm its commitment to the current trade agreement in order to provide clarity and prevent disruption.

The focus of the talks has been for the UK to enter into a new deal with SACU which essentially replicates the existing terms of the SADC Economic Partnership Agreement (EPA), rather than to renegotiate terms.

Should the UK and EU manage to reach a deal, the UK will continue to abide by the EU's rules and trade agreements for a transitional period until December 2020. During this period the existing trade agreement that SACU has with the EU (including Britain) will stay in place until the UK fully leaves the EU. After this transitional period a new trade agreement between SACU and the UK will kick in should one be reached.

Such an agreement, or lack thereof would, however, start immediately in a no-deal Brexit scenario, should the UK and EU fail to reach consensus. With the end of March deadline fast approaching it is worth noting that SACU (including Mozambique) still does not have a new trade agreement with the UK. While all accounts point to such an agreement progressing well, it is not finalised, posing a risk for Namibia. Should SACU be forced to revert to the WTO trade rules it is likely affect Namibian exports to the UK negatively, increasing the trade deficit and placing further pressure on the reserve position. As such Brexit remains a possible source for a negative external shock to the fragile Namibian economy.

## South African Election

South Africa's political landscape will remain a key focus point in 2019 due to it being an election year. Investors and ratings agencies will be keeping a close eye on the result of the general election as it will signal which reform policies will be implemented and how lacklustre economic growth will be revived. Most analysts expect improved economic growth to stem from these reforms should Ramaphosa win convincingly, strengthening the president's mandate.

The Independent Electoral Commission (IEC) of South Africa has announced that 285 political parties are currently registered, and that it is busy processing 37 more applications. It is however unlikely that all of these parties will contest in the upcoming election as high registration fees need to be paid in order for the parties to appear on the ballot paper.

### Early Polls

With the election to take place in May, the Institute for Race Relations (IRR) has conducted quarterly opinion polls to determine voters' voting intention should a national election take place on that day. The summarised results from the IRR's latest (early December 2018) poll are as follows:

| | Turnout Scenario | | | | |
|---|---|---|---|---|---|
| Political Party | 69% | 71% | 75% | 78% | 100% |
| ANC | 59% | 60% | 58% | 60% | 56% |
| DA | 22% | 20% | 21% | 20% | 18% |
| EFF | 10% | 11% | 11% | 11% | 11% |

*Source: Institute for Race Relations*

*The table above shows the percentage of the vote each party is expected to receive given five different voter turnout scenarios.*

According to the IRR's poll, the ANC will likely win the upcoming election with roughly 60% of the vote, depending on the number of voters turning up on election day. Trust in the ANC at the end of the Zuma years was relatively low, but support for the party appears to have started to pick up again after Ramaphosa became president early in 2018. We expect the ANC to resort to populistic statements and policies leading up to the election in a desperate attempt to win back votes (from the EFF in particular) should it fear that support for the party will wane further. In such a case the ANC will essentially try to beat the EFF at its own game.

The DA, meanwhile, seems to have reached a support ceiling, according to the poll, with the party unlikely to secure more than 22% of the vote. 2018 has been a particularly difficult year for the party, which not only struggled to remove Cape Town mayor Patricia de Lille for what seemed like most of the year, but also lost control of Nelson Mandela Bay's mayoral office when Athol Trollip was ousted during a no confidence vote by opposition parties. Another blow to the party was the recent resignation of its head of policy, Gwen Ngwenya, who stated that the DA's leadership is falling apart and that the party does not take policy seriously. These and other own goals are likely to hurt the DA at the polls.

The EFF could almost double its support in the upcoming election, according to the poll. The party has less to lose than the ANC and DA, and will thus continue to resort to voicing their controversial and populistic views. The EFF's strong support of economic nationalism (especially when it comes to land) is not investor friendly, and a stronger than expected result for the party would make investors cautious.

Voter turnout will play a key role in the upcoming election, as it will determine how much of a lead the ANC will have over the opposition parties and, ultimately, how much influence opposition parties will have on policy decisions. The 2014 general election saw 74% of registered voters turn up to vote and although this percentage seems high, it represents just 57% of all eligible voters. Should voters feel that the ANC remains tainted by corruption and that not enough was done by the party to 'self-correct', it is more likely that these voters will decide to not turn up on election day rather than to vote for opposition parties, as was the case with the 2016 municipal elections. Many ANC voters, however, continue to tolerate the party's involvement in corruption.

A key downside risk that remains is that if the ANC loses a significant amount of votes in the upcoming election the party could recall Ramaphosa and deputy president David Mabuza might be promoted to president. This will please the Zuma faction and would lead to the reversal of the cautious optimism that has built around the Ramaphosa campaign.

## Cyril Ramaphosa and the ANC

Cyril Ramaphosa's appointment in February 2018 brought a moment of 'Ramaphoria' as he promised from the start that he plans on reviving economic growth and to eradicate widespread corruption throughout the state. 2019 will thus be another definitive year for president Ramaphosa as voters and investors want to see how much progress has been made ahead of the election.

'Ramaphoria' was however short lived as the economy entered a surprise recession in the first half of 2018 and the rand weakened steadily. Consumer confidence also fell sharply in the third quarter, which put additional pressure on an already struggling economy.

Some small victories were seen in the fight against corruption and the president removed former SARS commissioner, Tom Moyane, and the head of the NPA Shaun Abrahams. Although these are steps in the right direction to root out corruption in the state, they were soft targets and little more was done to bring those involved in graft to justice. The real test for Ramaphosa will be to act against the party members implicated in the Zondo Commission of inquiry into state capture as several of those implicated form part of the Zuma faction.

The ANC is arguably a more divided party a year after Ramaphosa took office. A point which is proven by the party's conflicting views on the Reserve Bank. At the launch of the party's election manifesto in January, the ANC announced that the Reserve Bank "must pursue a flexible monetary policy regime, aligned with the objectives of the second phase of transition". This is consistent with the party's announcement at its national conference at Nasrec in December 2017 that "South Africa requires a flexible monetary policy regime, aligned with the objectives of the second phase of the transition" of the National Democratic Revolution (NDR), a theory which the ANC's tripartite alliance partners (SACP and COSATU) classify as the "most direct route to socialism". Ramaphosa and finance minister Tito Mboweni responded swiftly by reassuring that the independence of the reserve bank is "sacrosanct", to which the deputy president responded by reaffirming the ANC's intention to nationalise the Reserve Bank.

A similar challenge for Ramaphosa is to calm investors and give clarity on the ANC's decision to expropriate land without compensation. The president has tried to give reassurance that the reform will be handled carefully to avoid harm to the economy or agricultural output, but the threat remains that this will not be the case. The uncertainty regarding property rights is again investor unfriendly and may lead to some businesses and investors reconsidering investing in South Africa.

Another risk that is worrisome is the ANC's plan to prescribe assets on financial institutions whereby asset managers will be forced to invest a portion of their funds in state-owned enterprises or "socially productive investments". This could make it difficult for asset managers to protect the investments of their clients against permanent losses of capital and is very likely to lead to a drag on performance.

## Impact on Namibia

We identify the South African election as a key theme for 2019 due to the close economic ties between South Africa and Namibia. South Africa is Namibia's largest trading partner and is a key source of revenue and stability for the country. Southern African Customs Union (SACU) revenues make up about 31% of total government income, making Namibia very dependent on the receipts of this pool. As South Africa is by far the largest contributor to this revenue pool, the performance of the South African economy has a direct impact on Namibian government revenue. Due to the abnormally large role government plays in the Namibian economy, any negative impact on government revenues affects the rest of the economy as well.

The currency peg, which tethers the Namibia dollar to the rand, remains a source of price stability for Namibia despite the rand's exaggerated fluctuations at times. This benefit of the peg was reiterated by Bank of Namibia (BoN) in December 2018 when the deputy governor announced that the BoN was not looking to do away with the peg. The peg does, however, transfer South African currency risk on to Namibia at times when South Africa faces challenges. Thus, a South African election result that is investor unfriendly and results in rand depreciation will negatively impact producer and consumer buying power in Namibia. Given the current state of the Namibian economy, a further drag resulting from a large depreciation in the currency would be detrimental to living standards in general.

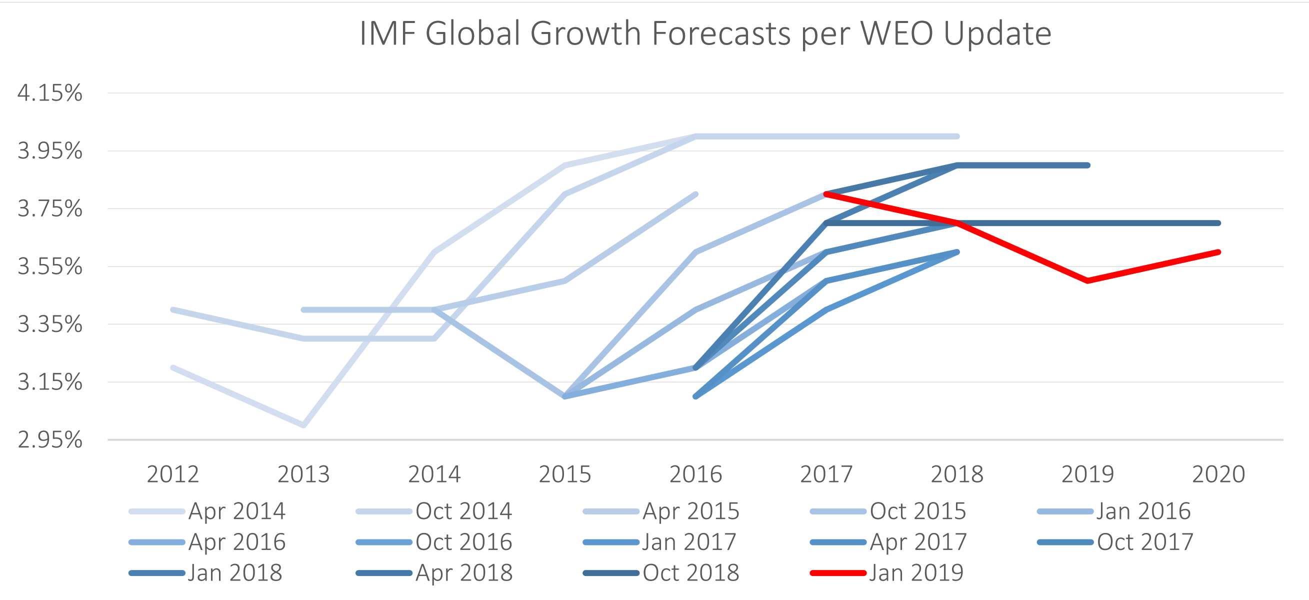
The result of the SA election is likely to give an indication on whether investor friendly policies will be implemented, and consequently what direction the South African economy (and due to the above-mentioned reasons, the Namibian economy) will be heading in 2019 and beyond. We do not expect a negative result when South Africa goes to the polling booths in May, but believe that the possibility of such a result remains and should not be ignored as it could have a meaningful impact on the Namibian economy.

# Global Economy

The harmonized global acceleration in economic expansion that started mid 2016 has begun to lose steam. The International Monetary Fund (IMF) recently released its January 2019 World Economic Outlook (WEO) update. In it the IMF estimates that global growth rose by 3.7% in 2018, an unchanged forecast from the IMF's October 2018 WEO but 0.2 percentage points lower than its April 2018 forecast. Global growth has remained resilient in 2018 despite subdued growth from economies in Europe and Asia.

Furthermore, the IMF estimates that the global economy will expand by 3.5% in 2019 and 3.6% in 2020. Both projections are downward revisions from the IMF's October 2018 WEO report. The IMF attributes these downward revisions to the impact of the already enacted tariff increases in the US and China and slowing momentum during the second half of 2018. The drag on growth during 2H18, the IMF says, stems from Germany's adoption of fuel emission standards, Italy's sovereign and financial risks, Turkish contagion, and the US government shutdown, which have weakened financial market sentiment.

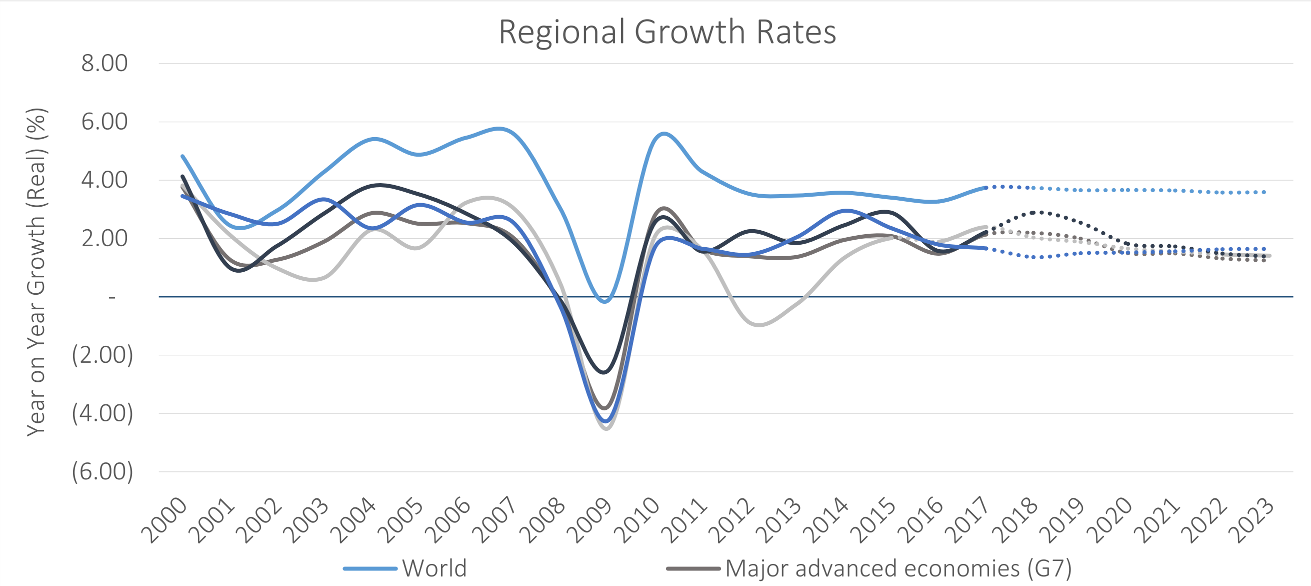
Several key developments carry further downside risks to global growth. The 90-day US and China tariff ceasefire is scheduled to end on the 1st of March and fears of trade tensions escalating further is a factor that could weigh on global growth in 2019. The volatility in crude oil prices has been exacerbated by the US imposing sanctions on Iranian exports at a time of supply uncertainty. Britain's unresolved exodus from the EU, with the 29th of March looming ever closer, is another factor weighing on global growth prospects. Apart from uncertainty emanating from the trade war with the US, the magnitude of China's economic slowdown will also have an impact on global growth in 2019.




*Source: IMF, IJG Securities*

## Developed Markets

Developed Markets (DM's) have maintained steady growth since 2016, posting growth of 1.7% in that year, followed by 2.3% in 2017. The IMF further estimates that DM's collectively grew by 2.4% in 2018. True to what has been the theme for the past few years, the IMF's 2018 growth projections for developed markets are a 0.1 percentage point downward revision stemming from lower revisions of EU economies. Growth in developed markets in 2019 and 2020 is expected to slow from 2018 estimates to 2.0% and 1.7% respectively.




*Source: IMF, IJG Securities*

## United States of America

The US economy has been expanding since 2010, and 2018 was a year supported by fiscal stimulus while at the same time the Fed continued on its path of policy normalization. The IMF estimates that the US economy expanded by 2.8% in 2018, an improvement from growth of 2.6% recorded in 2017. Tighter financial conditions and the tapering of fiscal stimulus will slow growth in the US to an estimated 2.5% in 2019 followed by yet slower growth of 1.8% in 2020 according to the January WEO. These forecasts are in line with the IMF's projections from its October 2018 WEO. Consumer spending will remain a key driver of economic growth in the US. Consumer spending is expected to be buoyed by low unemployment and accelerating wage growth that is likely to spur spending. The US does face risks to this outlook. With the 90-day tariffs ceasefire set to end on the 1st of March, the outlook on US-China trade negotiations remains uncertain. Protracted negotiations and or retaliations in tariffs will have far reaching effects that will weigh heavily on global trade, investment and output.

## Eurozone

The outlook for Europe has deteriorated with growth in the bloc estimated to have slowed to 1.8% in 2018 from 2.4% in 2017 according to the IMF January 2019 WEO update. The IMF forecasts that growth will moderate to 1.6% in 2019 (a 0.3 percentage point downward revision from October) before growing at a marginally quicker pace of 1.7% in 2020. Expectations for lacklustre economic growth in the region stem from downward revisions in many EU economies, with the most notable revision being that of Germany (the bloc's largest economy). Slower private consumption and meek industrial production on the back of auto emission standards revisions have been a drag on the German economy. Further risks to the Euro Area emanate from Italy, currently enduring subdued domestic demand as well as facing the risks associated with a spike in bond yields, combined with the adverse economic impact of the yellow vest protests in France.

## United Kingdom

The year 2019 will be a defining year for the British economy with the country's exit from the European Union currently set for the 29th of March. Prime Minister Theresa May continues to face parliamentary rejection of her Brexit proposals. This not only increases the likelihood of a "no deal" Brexit but the widely observed anti-Brexit sentiment provides for more uncertainty of any likely outcome, leading to heightened volatility. As such the UK is projected to grow by 1.5% in 2019 and in 2020, which is marginally better than the 1.4% growth measured in 2018. This follows on from the 2.2% growth the UK experienced for the three years between 2015 and 2017.

## Japan

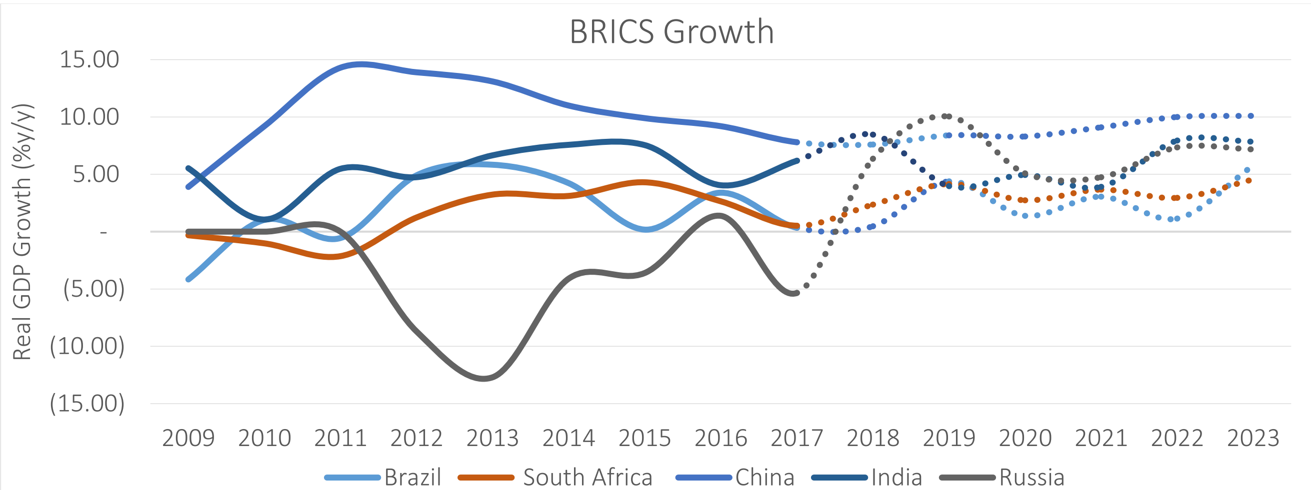
The IMF estimates that the Japanese economy grew by 0.9% in 2018 and expects marginal growth of 1.1% in 2019. Both of these estimates constitute a 0.2 percentage point upward revision from the IMF's October 2018 WEO. The 2019 revision stems largely from the planned fiscal stimulus, in additions to measures aimed at mitigating the effects of the planned consumption tax rate increase in October 2019. Growth in 2020 is expected to slow down to 0.5% due to the lagging effect from the consumption tax (VAT) increase. Monetary policy in Japan still remains very much accommodative with interest rates still in negative territory.

## Developing Countries

Overall the prospects for growth in emerging markets (EM) in 2019 have been revised downward. EM economic growth, as a whole, is estimated to slow by 0.1 percentage points every year from 4.7% recorded in 2017 to 4.6% in 2018, before slowing further to 4.5% in 2019. The IMF then projects EM growth will accelerate to 4.9% in 2020. Economic performance across the EM landscape remains mixed.

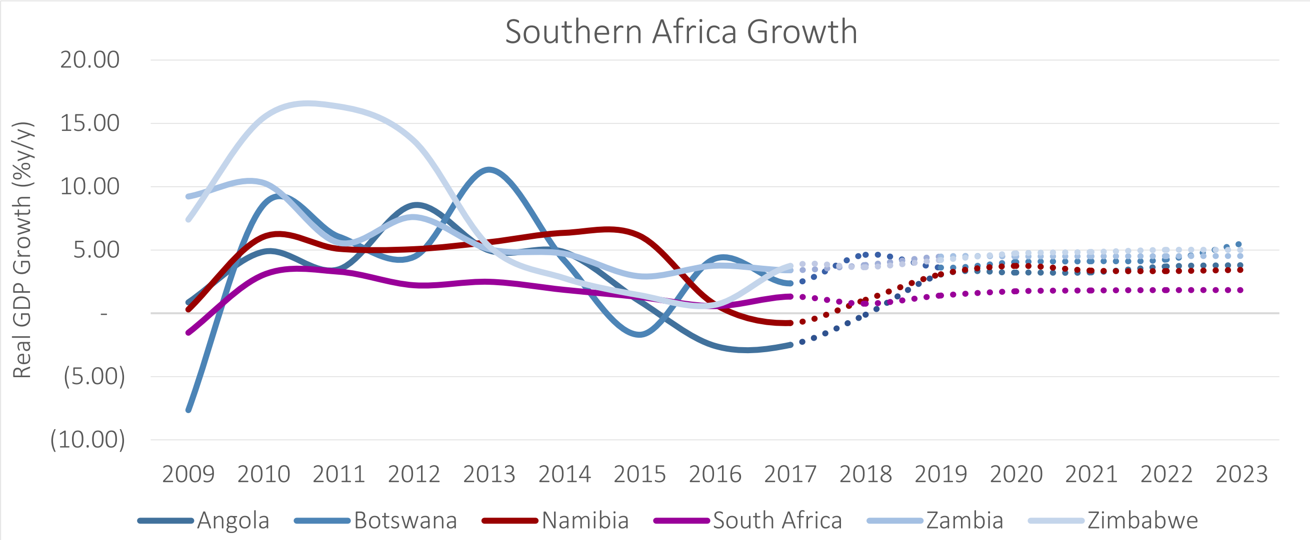
Monetary policy across EM's have taken on a tighter stance since 2Q2018 and this has restricted financial conditions to a large extent. The impact, earlier in 2018, of escalating oil prices on inflation, coupled with widespread currency depreciation, resulted in EM central banks tightening monetary policy. Over the same period risk-off sentiment weighed on EM equities and bonds, leading to large sell-offs. EM economies experienced net capital outflows in the third quarter of 2018 as a result.

Chinese economic growth has been slowing since 2010 from elevated levels. Economic growth in the world's second largest market is expected to slow to 6.6% in 2018 from 6.9% in 2017 and is expected to taper to 6.2% in both 2019 and 2020. The 2018 slowdown is attributed to deleveraging in the first quarter of 2018 and trade disputes with the United States. A slowing China does not bode well for its trading partners and global commodity prices in general. Chinese policymakers will now turn to easing monetary policy in response to the slowdown. The IMF has warned that Chinese economic activity may expand less than expected, citing uncertainty in trade tensions as a reason for concern.




*Source: IMF*

The IMF is forecasting that growth will accelerate to 3.5% in Sub-Saharan Africa in 2019, a marked improvement from growth of 2.9% recorded in 2018. Growth is set to pick up to 3.6% in 2020. Both the 2019 and 2020 forecasts are 0.3 percentage points lower than the IMF projected in its October WEO. Oil producing nations such as Angola and Nigeria have received downward revisions to their 2019 and 2020 outlooks, on the back of expectations for lower oil prices going forward.




*Source: IMF*

Growth in South Africa is expected to have slowed to 0.8% in 2018, from an estimated 1.3% in 2017. The IMF expects the SA economy to grow by 1.4% in 2019 followed by a 1.7% increase in real GDP in 2020. This forecast is unchanged from the IMF's October WEO. 2019 is an election year for South Africa and President Ramaphosa's ascendancy to the helm has been positively received. A landslide ANC victory may boost business and investor confidence on the back of Ramaphosa securing a strengthened mandate, which may enable him to effect structural reforms. Should we see a drive to unite the ANC behind positive structural reforms and a clamping down on corruption, it is likely that the impact on business and investor confidence will lead to accelerating growth in our southern neighbour's economy.

An immediate risk to the SA outlook lies in the impending announcement of Moody's credit review of SA. Moody's is the only ratings agency to still rate SA one notch above junk. However, the country has exited a technical recession in Q3 and looks set to have remained fiscally prudent enough for Moody's to at most change only its outlook for SA. Monetary policy will remain relatively accommodative in 2019 with the SARBS's inflation outlook estimated a peak at 5.6% in 2020 only.

# Supply Side Growth

The final Namibian national accounts for 2018 will not be released for at least six months. We expect that slightly positive real GDP growth will be recorded for the calendar year after all revisions have been passed. Contractions in agriculture and fishing, as well as manufacturing and a large proportion of tertiary industries are expected to largely offset growth in mining and quarrying. Uranium and diamond mining output rose significantly, contributing enough to counteract the decrease in consumer and business activity recorded in tertiary industries. Q3 national accounts data points to a year-to-date contraction in real GDP of 0.4%. We believe that revisions to the data (specifically from the mining sector) will see Namibia escaping a second annual contraction by the slightest of margins. As a result, we expect real GDP growth of 0.2% in 2018. The possibility of downward revisions remains but is not our base case expectation.

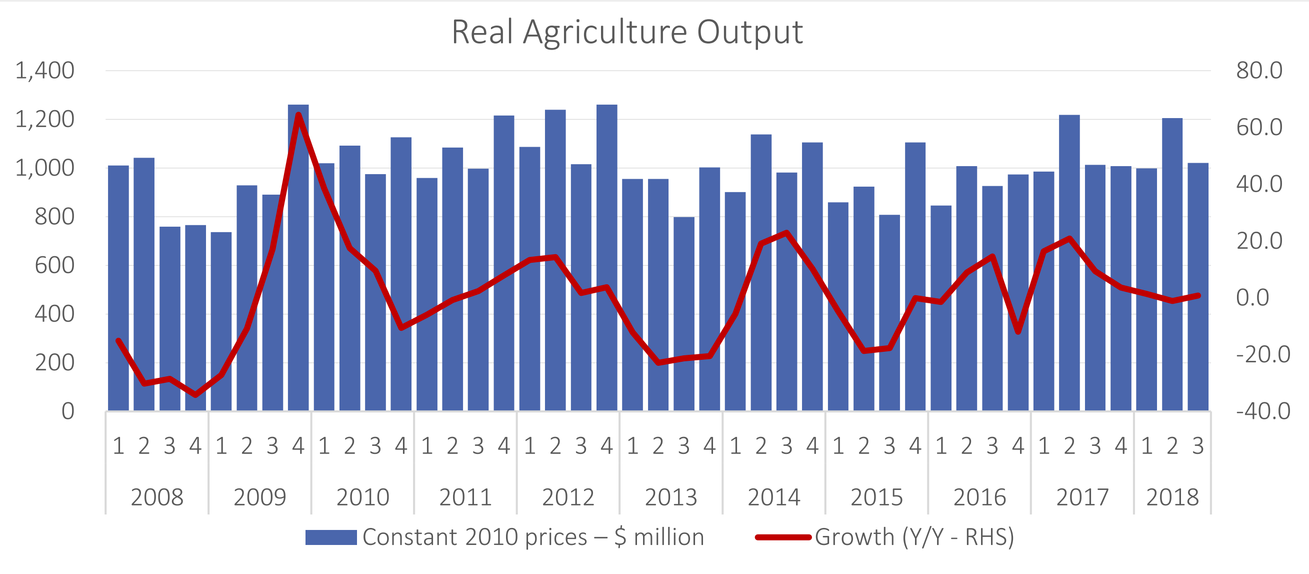
| Real GDP Growth Rates | Actual | | | Nowcast | | Forecast | | |
|---|---|---|---|---|---|---|---|---|
| **Industry** | **2014** | **2015** | **2016** | **2017** | **2018** | **2019** | **2020** | **2021** |
| Agriculture and forestry | 11.1 | -10.4 | 1.5 | 12.6 | -2.8 | -2.3 | 3.2 | 1.3 |
| Livestock farming | 13.9 | -13.3 | 4.2 | 13.7 | -1.5 | -2.5 | 2.0 | 2.0 |
| Crop farming and forestry | 7.6 | -6.6 | -1.8 | 11.0 | -4.5 | -2.0 | 5.0 | 0.4 |
| Fishing and fish processing on board | -2.5 | 2.3 | 9.1 | 1.3 | -9.8 | 4.5 | 4.7 | 4.7 |
| Mining and quarrying | -6.0 | -4.9 | -5.8 | 13.7 | 18.3 | -11.0 | 8.5 | 1.6 |
| Diamond mining | 4.9 | -4.1 | -9.6 | 14.6 | 15.2 | -13.9 | 8.0 | -1.0 |
| Uranium mining | -9.9 | -18.1 | 13.6 | 18.8 | 68.7 | -15.4 | 16.4 | 8.4 |
| Metal ore mining | 0.6 | 60.0 | 0.1 | 9.9 | -9.7 | 3.5 | 1.4 | 0.0 |
| Other mining and quarrying | -36.4 | -44.1 | -19.8 | 4.3 | -0.5 | 3.0 | 3.0 | 3.0 |
| **Primary industries** | **-1.6** | **-5.2** | **-1.5** | **11.1** | **8.3** | **-6.9** | **6.7** | **2.0** |
| Manufacturing | -0.1 | -4.3 | 5.6 | 1.3 | -2.8 | 1.4 | 3.3 | 2.7 |
| Meat processing | -17.2 | -3.0 | -2.1 | -14.4 | -8.0 | 14.6 | 8.4 | 0.4 |
| Grain Mill products | 13.7 | 13.0 | 8.1 | 15.5 | -5.0 | 0.0 | 5.0 | 4.0 |
| Other food products | 11.7 | -12.3 | 4.8 | -4.6 | -6.5 | 1.0 | 4.5 | 2.5 |
| Beverages | -16.5 | -2.1 | -1.6 | -0.8 | -3.0 | 2.5 | 2.5 | 2.5 |
| Textile and wearing apparel | -2.9 | -8.9 | 3.7 | -3.2 | -2.0 | 2.0 | 2.0 | 2.0 |
| Leather and related products | 10.7 | -1.8 | -6.2 | 2.3 | 2.0 | -0.3 | -0.3 | -0.3 |
| Wood and Wood product | 1.7 | -2.6 | 3.5 | 1.6 | -5.0 | 4.5 | -1.7 | -1.7 |
| Publishing and Printing | 10.6 | 6.3 | -1.9 | -2.4 | -1.3 | 0.7 | 0.7 | 0.7 |
| Chemical and related products | 1.2 | -3.3 | -2.6 | -5.7 | -4.0 | 3.6 | 2.5 | 2.5 |
| Rubber and Plastics products | 5.4 | 26.9 | 2.6 | -9.1 | 2.0 | 3.3 | 0.0 | 0.0 |
| Non-metallic minerals products | 5.6 | 8.1 | 5.8 | 0.8 | -2.0 | 4.0 | 2.6 | 2.6 |
| Basic non-ferrous metals | -3.2 | -8.3 | 1.0 | 4.8 | -5.7 | 7.0 | 2.5 | 6.5 |
| Fabricated Metals | 3.7 | -6.4 | -1.3 | -6.5 | -5.0 | 0.0 | 0.0 | 0.0 |
| Diamond processing | 24.4 | -19.0 | 86.0 | 14.6 | 9.1 | -13.9 | 8.0 | -1.0 |
| Other manufacturing | -2.9 | -8.1 | -12.5 | -2.4 | -2.9 | 3.1 | 2.5 | 2.5 |
| Electricity and water | 1.5 | 13.6 | 6.8 | 1.8 | 10.2 | 5.0 | 5.0 | 5.0 |
| Construction | 42.6 | 24.3 | -26.3 | -25.6 | 5.9 | 7.3 | 4.6 | 2.5 |
| **Secondary industries** | **10.9** | **6.8** | **-6.4** | **-6.7** | **0.9** | **3.4** | **3.9** | **3.0** |
| Wholesale and retail trade, repairs | 13.9 | 7.4 | 3.1 | -7.5 | -4.0 | 3.3 | 2.0 | 4.5 |
| Hotels and restaurants | 10.8 | 5.6 | 3.5 | -1.1 | -2.3 | 2.1 | 4.4 | 3.8 |
| Transport, and communication | 5.7 | 6.9 | 7.0 | 0.8 | 2.6 | 3.4 | 4.2 | 4.2 |
| Transport | 3.3 | 7.9 | 6.9 | 1.4 | 2.5 | 3.9 | 4.0 | 4.2 |
| Storage | 5.7 | -0.6 | 2.0 | -4.7 | 3.0 | 2.7 | 2.4 | 1.9 |
| Post and telecommunications | 8.6 | 8.9 | 8.9 | 2.1 | 2.5 | 3.0 | 5.0 | 5.0 |
| Financial intermediation | 10.9 | 5.0 | 2.8 | 2.8 | -1.0 | 2.5 | 4.5 | 5.0 |
| Real estate and business services | 2.8 | 4.7 | 0.7 | 0.8 | 0.2 | 0.2 | 2.6 | 3.0 |
| Real estate activities | 3.0 | 3.6 | 2.6 | 2.7 | -0.2 | 0.0 | 2.5 | 2.5 |
| Other business services | 2.4 | 6.6 | -3.8 | -4.6 | 1.5 | 1.0 | 3.1 | 4.6 |
| Community, social and personal service activities | 3.0 | 11.9 | -0.3 | -0.1 | 1.5 | 1.5 | 1.5 | 1.5 |
| Public administration and defence | 1.4 | 14.0 | 3.3 | 0.3 | -2.0 | 3.0 | -1.0 | 3.0 |
| Education | 10.3 | 4.1 | 2.8 | -1.2 | -1.5 | 1.5 | 3.5 | 3.5 |
| Health | 10.2 | 17.5 | 7.2 | -1.3 | -5.2 | 2.8 | 2.5 | 3.5 |
| Private household with employed persons | 5.5 | 1.7 | 1.4 | 1.0 | -2.0 | 2.5 | 4.3 | 2.5 |
| **Tertiary industries** | **7.7** | **7.9** | **3.2** | **-1.4** | **-1.6** | **2.4** | **2.4** | **3.7** |
| Less: Financial intermediation services indirectly measured | 5.3 | 0.1 | 2.1 | -0.2 | -1.5 | 2.0 | 2.5 | 2.5 |
| **All industries at basic prices** | **6.6** | **5.6** | **0.6** | **-0.4** | **0.5** | **0.8** | **3.4** | **3.3** |
| Taxes less subsidies on products | 4.1 | 12.5 | 0.9 | -5.5 | -3.2 | 1.2 | 4.5 | 4.5 |
| **GDP at market prices** | **6.4** | **6.1** | **0.6** | **-0.9** | **0.2** | **0.9** | **3.4** | **3.4** |

*Source: IJG Securities*

We expect real GDP growth of 0.9% in 2019, driven by a marginal rebound in tertiary sector activity as government ups operational expenditure (including salaries and wages) and consumers starts to recover. We expect a contraction in primary industries as diamond and uranium mining output are likely to decline this year, largely as a result of the closure of the Langer Heinrich uranium mine and the Elizabeth Bay diamond mine. Below we take a brief look at some of the larger sectors of the economy and how they performed in 2018, breaking down our expectations for these sectors for the year ahead.

## Agriculture

Agriculture output has remained steady in real terms in 2018 with year-to-date growth of 0.3% in Q3 versus Q3 2017. Agriculture posted strong growth of 12.6% in 2017, setting a high base for future performance, and partly informing our prior expectation for a contraction of 1.6% in 2018. Decent rainfall, although late, lead to improved conditions which supported both agronomic and livestock farming in general. After strong agricultural growth posted in 2017, maintaining constant output in 2018 is highly encouraging, especially when seen in the context of lower rainfall.



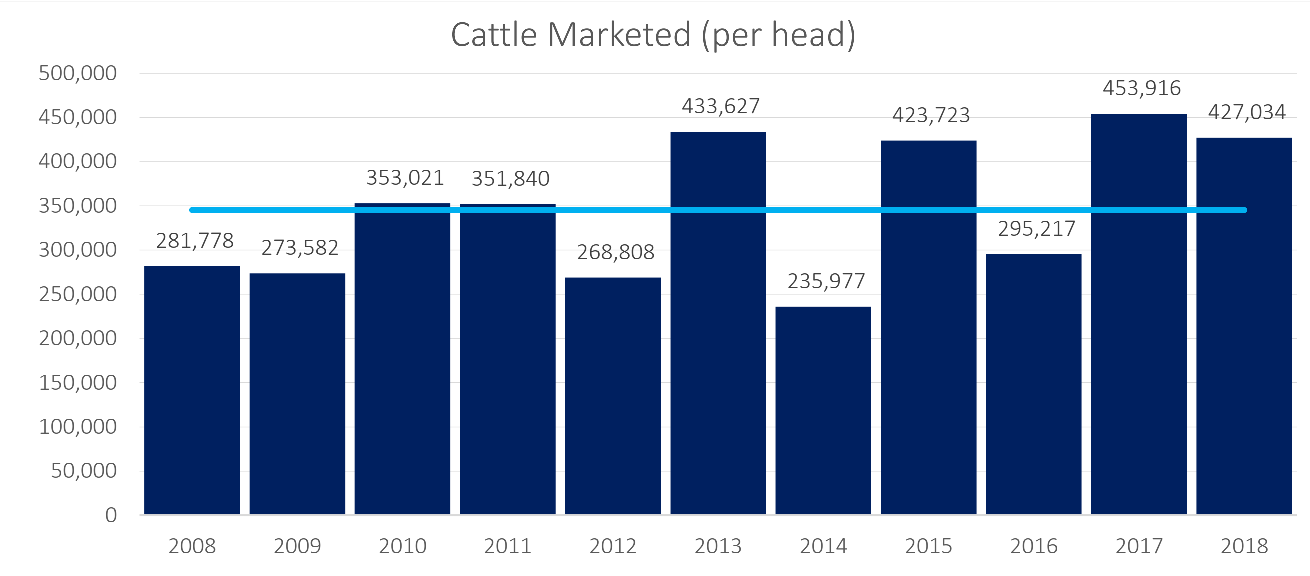

*Source: NSA*

2019 is shaping up to be a trying year for the farming community due to expectations for a below average to average rainfall year. The Oceanic Niño Index (ONI) is currently pointing to mild El Niño conditions in Southern Africa which, on average, coincide with periods of lower rainfall. The index is however not a perfect predictor of rainfall and there have been periods in Namibia's history where the country has received good rainfall despite these conditions, as well as periods of drought when conditions were favourable according to the ONI. That said, various weather services and commentators have urged farmers to prepare for a below average rainfall year in 2019. January proved to be a disappointing month for rainfall and the probability for average rainfall for the year is likely to be well below 50% now.

While rainfall in Namibia is the most important factor for agricultural production and output, regional rainfall has a large impact on farmers and output in the livestock sector as well. During periods of domestic drought cattle and sheep farmers import feeds, mainly from South Africa, which adds to the cost of production but enables sustainable production in most years. Regional droughts decrease South African feed crop production and therefore increase the cost of animal feeds which squeezes the sustainability of Namibian farms. Thus, regional droughts put additional pressure on livestock farmers and the sustainability of their operations and often lead to a decrease in the size of the national herd in Namibia.

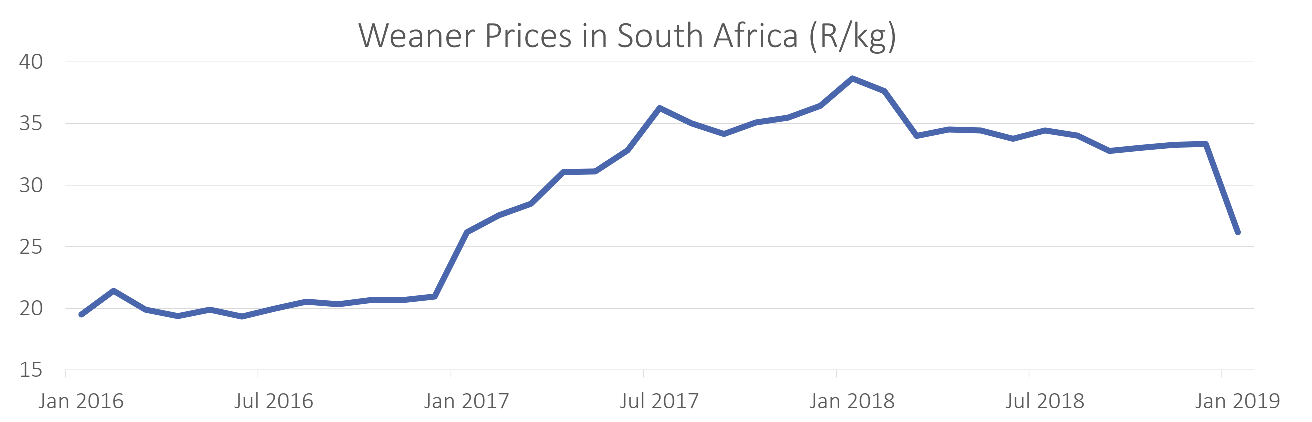
Poor rainfall in South Africa in December is expected to lead to reduced yellow maize and other animal feed crops. Imports are likely to be necessary to supplement this shortfall and this has led to a rapid increase in prices for these crops. This suggests that the scenario described above has started to materialise and may intensify going forward as El Niño conditions develop. While it is still too early to tell how severe the impact on Namibian livestock farmers will be, a significant number of signs are currently pointing to a disappointing year.

## Beef



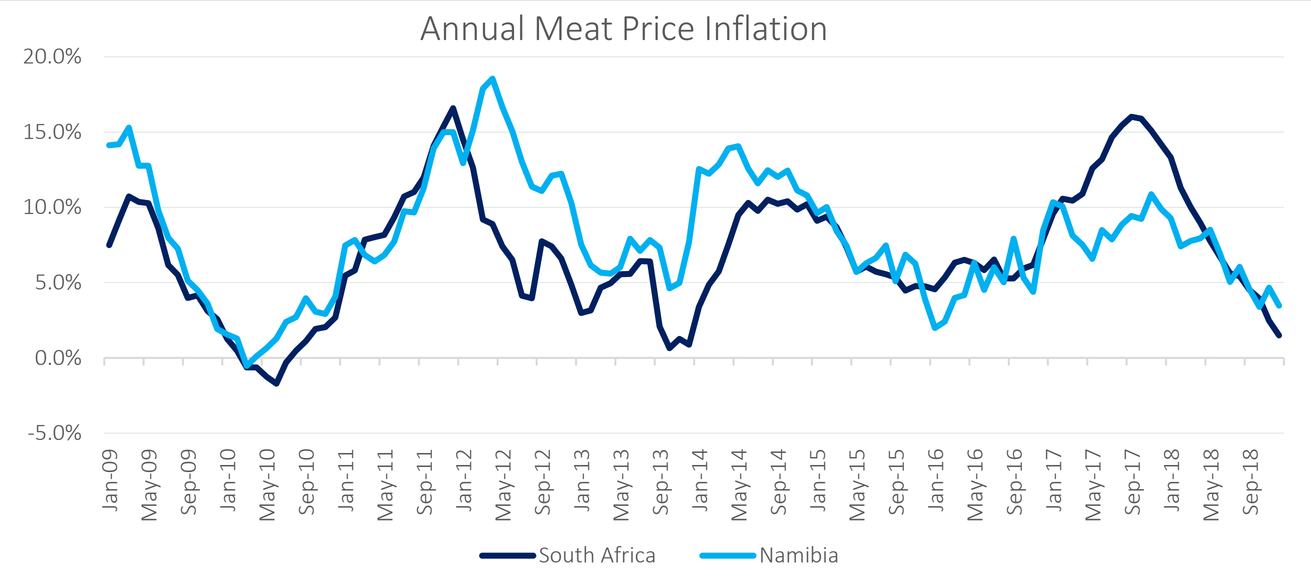

*Source: Namibia Meat Board*

In our 2018 Outlook document we noted that we expected output from the beef industry to decrease due largely to a high base set in 2017. Beef production for 2018 dropped 5.9% y/y in terms of the total number of cattle marketed, but still recorded well above average figures when compared to the last decade. The base set in 2017 was supported by an almost doubling of the number of weaners exported to South Africa when compared to 2016. The weaner export market has become a vital source of sustainability for Namibian cattle farmers in recent years due to difficult local market conditions. Strong feed crop production over the last two years (2017 and much of 2018) in South Africa resulted in low feed prices, a major input cost in South African feedlots. As a result of the lower feed prices demand for weaners at feedlots went up due to higher margins which in turn benefitted Namibian weaner exporters.



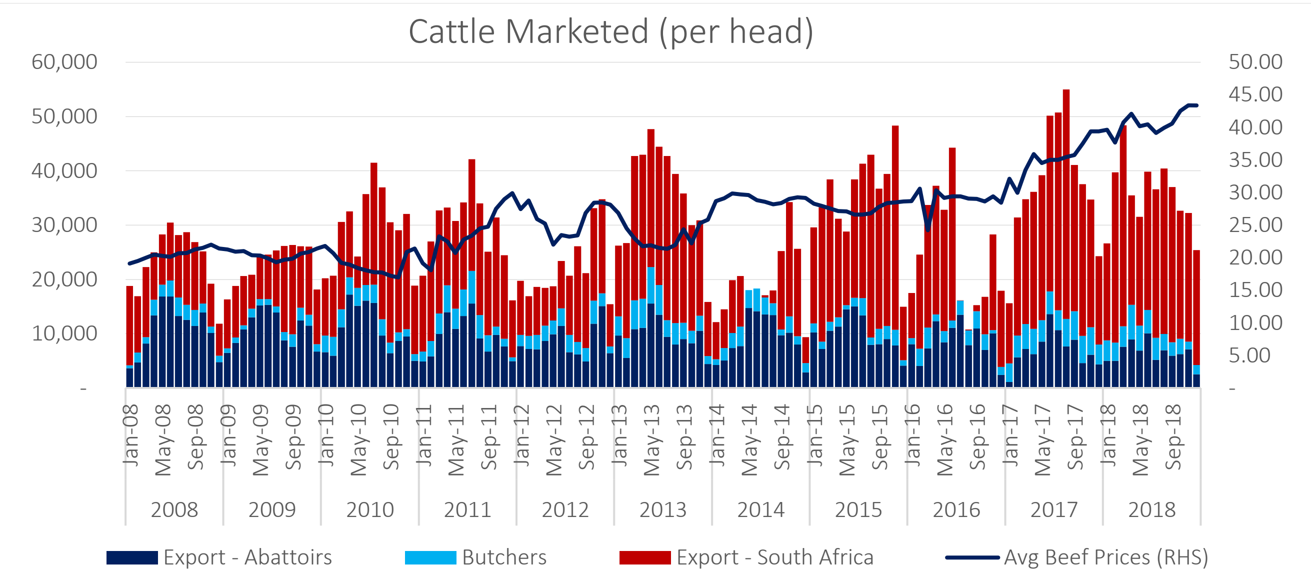

*Source: Red Meat Producers Organisation*

Feed crop prices have been rising rapidly in South Africa due to poor rainfall early in the 2018/19 season. Our Southern neighbour, the largest feed producer in the region, is likely to need to import yellow maize and other feeds in 2019 which has driven prices closer to import parity. Higher feed costs make it more expensive for feedlots to finish animals (a period where an energy-dense diet is used to round off an animal's development), and these costs are difficult to pass on to consumers without impacting demand negatively, especially in the South African market where real per capita incomes have been stagnant for a decade now. As these costs are difficult to pass on to consumers this results in feedlots pushing producer prices down in order to remain viable. As a result, prices received by Namibian weaner producers from South African feedlots have come off and may drop further. The recent Foot and Mouth Disease outbreak has exacerbated this situation further.




*Source: Stats SA, NSA*

Over the short term, the Foot and Mouth Disease (FMD) outbreak in South Africa has and will put pressure on producer prices. The outbreak has already resulted in a ban on imports of South African meat and meat products by most trading partners. This has flooded the South African market with supply and probably accounts for much of the producer price pressure experienced in January. Only time will tell how rapidly the FMD outbreak is resolved and until such a time both Namibian and South African farmers are likely to remain under pressure due to depressed prices offered at abattoirs and feedlots. This does not necessarily mean that a corresponding drop in meat prices will be seen in the supermarket. Namibian supermarkets have been under pressure due to depressed sales volumes and squeezed margins and are unlikely to drop meat prices significantly, as are wholesalers.




*Source: Namibia Meat Board*

## *Outlook for Beef*

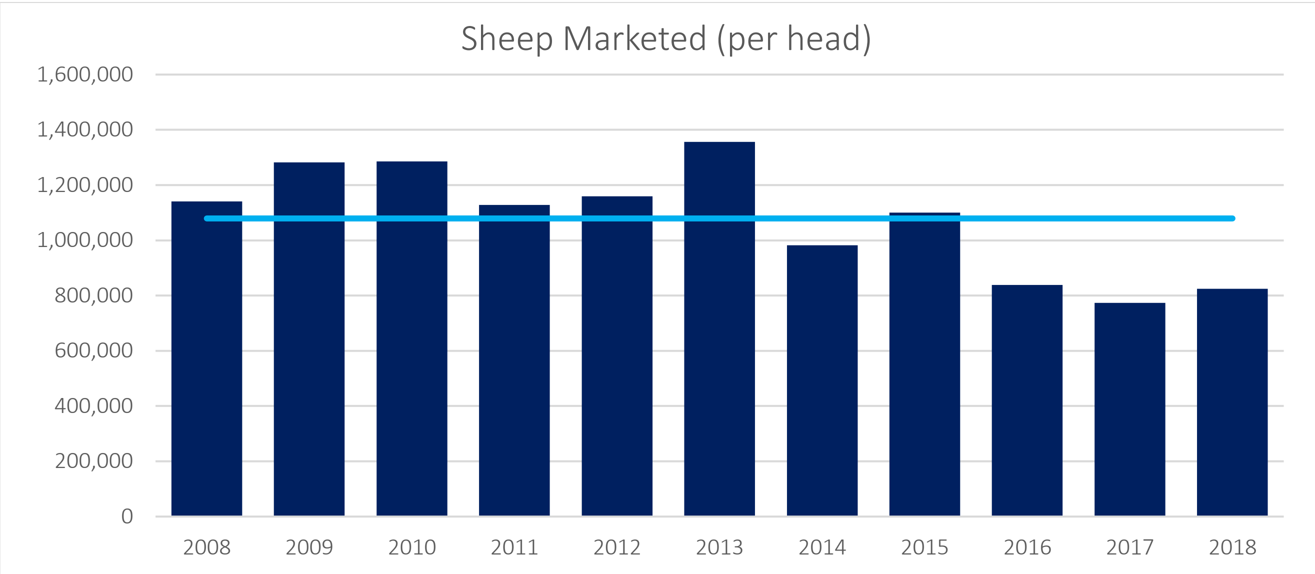
The outlook for the beef/cattle industry is leaning toward another negative performance in 2019. A below average rainfall year will lead to reduced carrying capacities on farms in general. The increase in feed prices means that the use of feeds to sustain herds will be expensive and the increase in input costs could result in some farms running losses. The current FMD outbreak in South Africa adds to the challenges faced due to excess supply within the country putting pressure on producer prices. The loss of FMD free status in South Africa in 2011 was only regained in 2014, indicating the length of time that such an outbreak may affect the industry, although such a lengthy process is less likely this time around due to the relatively contained area of the current outbreak.

A further factor which is not explored in detail here is the effects of *Brexit* on Namibian beef exports. Beef exports to the UK are currently regulated by the Economic Partnership Agreement (EPA) with the EU and a disorderly *Brexit* could thus affect exports to the UK. The way in which the UK leaves the EU will determine the future of trade between SACU and the UK and could potentially become a stumbling block over the short to medium term. Thus far SACU negotiations with the UK and EU are progressing well and it is hoped that SACU (+Mozambique) will be able to replicate the current EPA with the UK. This will allow beef exports to continue as before. However should a no-deal *Brexit* take place then trade will revert to World Trade Organisation (WTO) rules which will have a meaningful impact on Namibian beef exports as it will increase the landed price of Namibia beef in the UK. There is a strong possibility that should this happen Namibian beef prices will be uncompetitive and Namibian beef exporters will suffer the loss of a lucrative market.

Due to the current headwinds facing the beef industry we expect to see reduced output for 2019 when compared to 2018. Potential upsides to this scenario are good late rainfall, a speedy resolution to the FMD outbreak in South Africa, and reduced yellow maize and feed import prices. As always during years of below average rainfall, there is an increased risk of marginal farms running losses and farmers leaving the industry.

## Sheep, Goats and Pigs

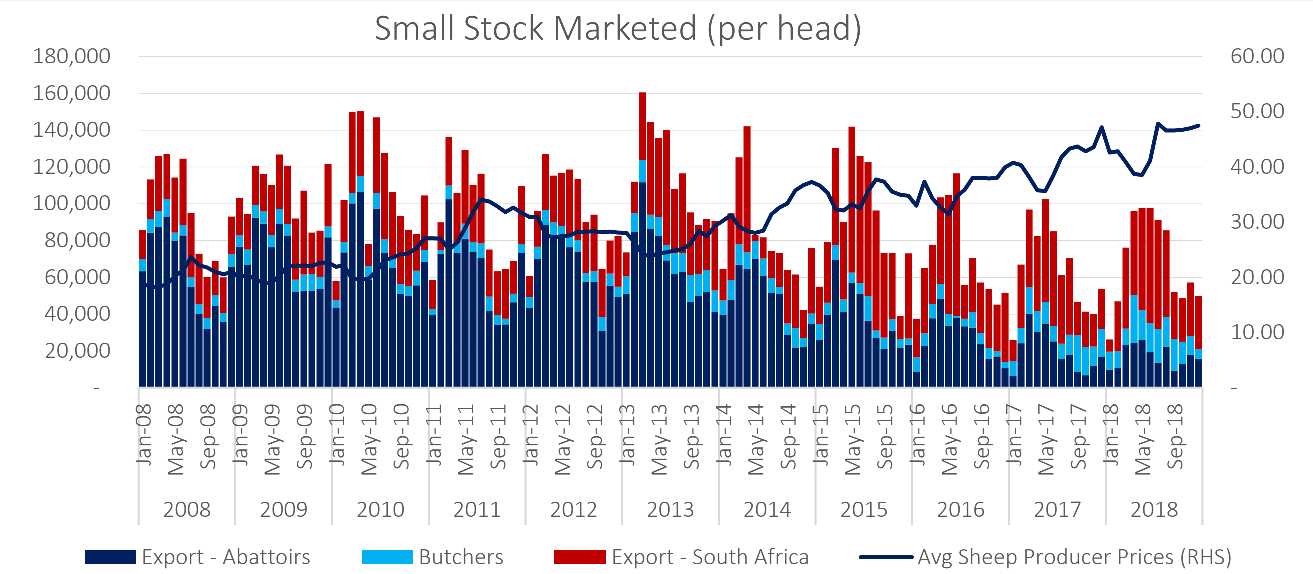
The cumulative number of sheep marketed in 2018 rose 6.6% when compared to 2017. 2017 saw a 7.8% decrease in the cumulative number of sheep marketed, setting a low base, and meaning that cumulative sheep production in 2018 was below 2016 levels, and well below average levels over the last decade (as illustrated below). Export abattoirs processed 13.9% less sheep than in 2017, causing a drag on the overall production figure. By contrast butchers processed 15.8% more sheep in 2018 than in 2017, and 15.7% more sheep were exported to South Africa on the hoof during 2018.




*Source: Meat Board of Namibia*

The cumulative number of goats and pigs marketed during 2018 rose by 2.8% y/y and 1.2% y/y, respectively. The vast majority of goats marketed are exported on the hoof to South Africa while pigs are slaughtered and processed domestically. Together goat and pig production make up around a fifth of small livestock production in Namibia.

As with most agricultural production in Namibia, the production of sheep, goats and pigs is highly dependent on weather conditions and rainfall and thus the outlook for rainfall hangs like a dark cloud over these industries. Poor rainfall is not a given but the ever-increasing likelihood of a poor rainfall year sees the likelihood of a contraction in small livestock production increase too. Adding to this challenge is the FMD outbreak in South Africa which has resulted in that market being flooded with meat previously destined for export. While much of the meat currently flooding the system is beef, this meat competes with other protein sources such as lamb and mutton, putting pressure on prices. This is driving down producer prices in Namibia's main export destination for sheep and goats, adding to the pressure already experienced by local farmers. A further negative impact due to the FMD outbreak is restrictions on imports of certain feeds which are particularly important in dry years. This raises costs for farmers and squeezes margins. The Livestock Producers Organisation (LPO) has described the situation as a "national crisis".




*Source: Namibia Meat Board*

### *Outlook for Small Livestock Production*

We expect to see a contraction in small livestock production during 2019, especially from sheep farming. The industry is under pressure which is likely to remain should the current dry conditions persist and depending on how long it takes for South Africa to regain its FMD free status. Restrictions on the importation of feeds due to FMD will make for a trying year for the sheep and goat farming communities and relief is likely to be necessary. Local maize farmers may provide some of this relief by switching from maize to Lucerne production, but this is unlikely to be sufficient and exports will still be necessary, significantly raising the cost of maintaining herds.

## White Maize

The 2017 white maize harvest set an all-time record high of around 76,000 tonnes according to the Namibia Agronomic Board (NAB). Last year saw a harvest of around 57,000 tonnes, a decrease of 25% from the prior year. This decrease was larger than we expected. Despite the decrease, the total production figure remained above the average over the last decade. Late rainfall undoubtedly played a role in the decreased production although other factors such as further Fall Army Worm infestations in certain areas also affected production negatively again. The drop in production in 2018 means that Namibia was once again below 50% self sufficient with regards to white maize production.

The predictability of rainfall in Namibia continues to hamper production and irrigation is the key to self-sustainability according to the NAB. Currently around 60% of Namibia's maize crop is produced under irrigation with the remainder contingent on rainfall. Thus, poor rainfall, in general, or in certain crop producing regions, leads to large fluctuations in output. The variability and even the periods between good showers leads to a large amount of uncertainty with regards to when to plant crops. This uncertainty means that farmers may invest into the season only to be struck by drought and plants dying early in the season.

### *Outlook for Maize*

Expectations for average to below average rainfall in much of Namibia affects the outlook for white maize production for 2019 negatively. A further factor expected to play a negative role is the heat currently experienced in some of the maize production zones in Namibia. The above normal soil temperatures affect the water retention ability of the soil, leading to dryer soils. The heat may also physically damage seedlings leading to reduced yields, especially so in those areas where rainfall is relied on. We expect a trying year for the dry land (rainfall dependent) maize producers leading to a contraction in white maize production.

## Horticulture

Horticulture production increased by 26.8% in terms of the total number of tonnes of the various products produced in 2017/18. In value terms production increased by 9.4% versus the prior year. Horticulture production volumes have benefitted from the Market Share Promotion scheme which currently requires retailers to source 47% of certain products locally before import permits are issued. This percentage was increased from 44% to 47% effective 1 December 2018 and as such the current year's production is expected to benefit further from this initiative.

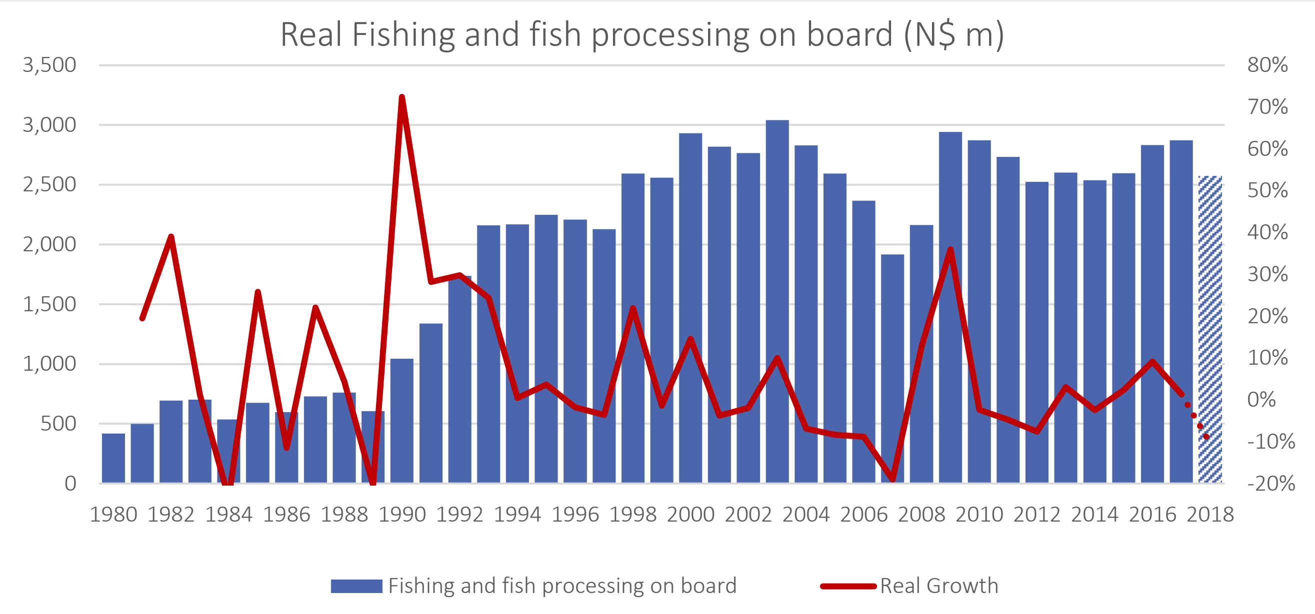
The outlook for this sector of agricultural production is less uncertain as irrigation is widely used and thus horticulture is less affected by dry spells. Heat is a factor which may impact production though, and given the expectations for hot conditions during the month of February this poses a downside risk in a sub-sector of agriculture which is otherwise expected to perform relatively well compared to maize and livestock production.

## Outlook for Agriculture

Real growth in agriculture in 2019 is unlikely in our view. The FMD outbreak in South Africa has already started impacting the livestock sector negatively, weighing on producer prices and restricting feed imports. The ever-increasing likelihood of a poor rainy season means that carrying capacities on farms are likely to be somewhat reduced when compared to 2018. The rainfall outlook is also likely to hurt maize and mahangu production. Added to the dry conditions are the expectations for a hot February which in itself may lead to crop losses through damage to seedlings. Much rests on rainfall over the months of February to April as such, and an upside surprise to the expected below average season could possibly see decent agricultural production. However, such a scenario is becoming less likely in our view and thus we expect a contraction in agricultural output for 2019.

## Fishing

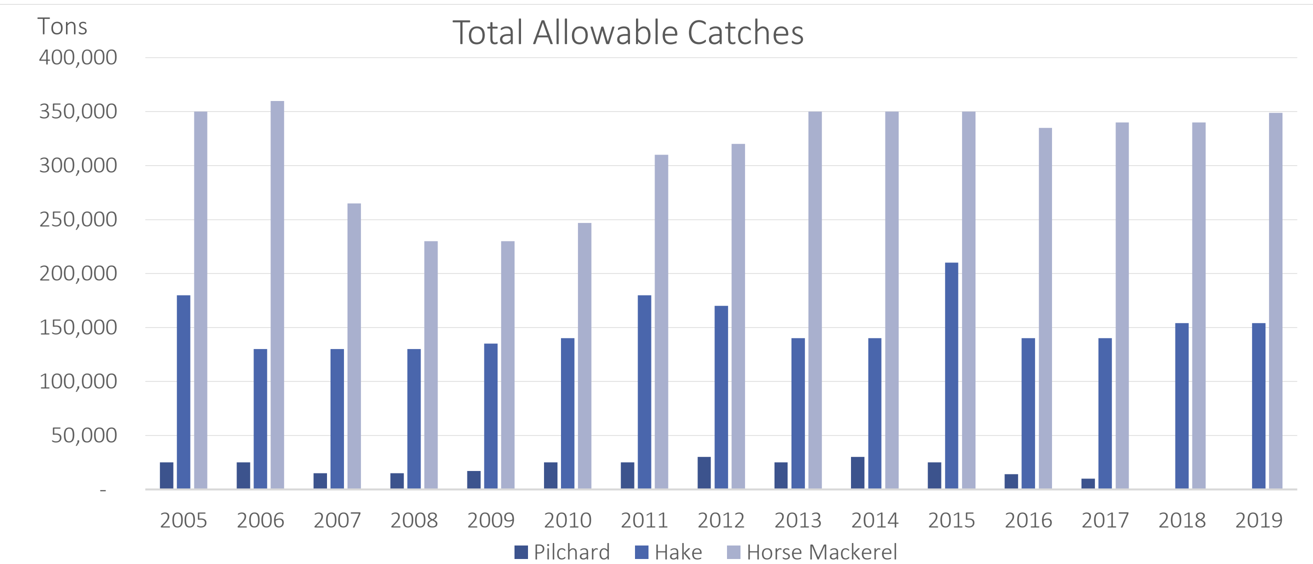
The latest available GDP figures show that fishing and fish processing on board recorded slow growth of 1.3% y/y in 2017, and that our expectations for modest growth of 1.2% in 2018 were ambitious. Third quarter 2018 GDP data released by the NSA points to a year-to-date contraction of 10.4% in fishing and fish processing on board. While this data is subject to change, Q4 data shows seasonally weaker output than in other quarters and is unlikely to result in much improvement to the year-to-date growth seen in Q3.




*Source: NSA*

In 2017 Namibia exported N$9.2bn worth of fish and fish products (processed and preserved), making it a key export industry and foreign exchange earner. Only mining related exports contribute more to Namibia's trade balance than the fishing industry. The NSA's Q3 trade statistics reveal that N$2.5 billion worth of fish and fish products were exported by Namibia in Q3 of 2018 alone, surpassed only by diamond exports during the quarter.

Horse mackerel and hake continue to make up the bulk of total allowable catches (TAC) in Namibian waters. For 2018 the horse mackerel TAC was kept steady at 340,000 tonnes while hake TAC's were increased to 154,000 tonnes from 140,000 tonnes in 2017. The ministry of fisheries did however note that the impact of the moratorium on pilchard fishing, in addition to slight decreases in other fish quotas, resulted in a 3% drop in TACs when compared to the prior season. The contraction in the year-to-date figures noted above point to a larger than 3% decline in output from the industry, although these figures may still be revised. Accounts from fishing industry role-players seem to point towards a reasonable year with a contraction of less than 10% expected.




*Source: Ministry of Fisheries and Marine Resources*

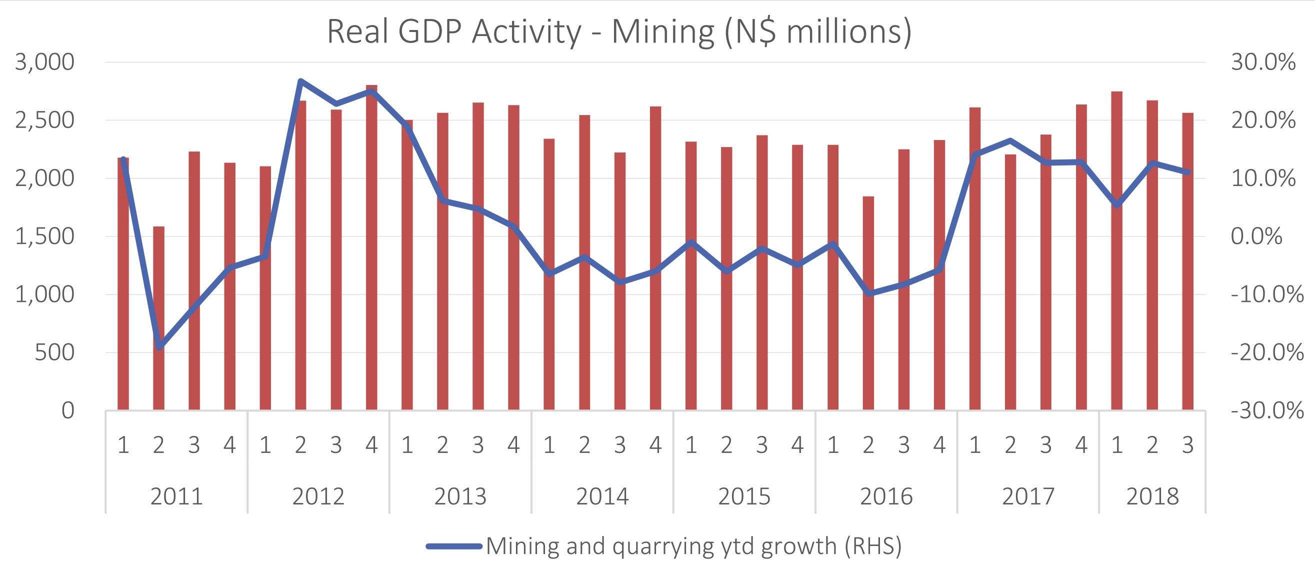
For 2019 horse mackerel TACs have been increased by 2.6% to 349,000 tonnes. Hake TACs remain unchanged however at 154,000 tonnes for the period running from 1 November 2018 to 30 September 2019. The industry remains optimistic regarding the health of the resource with both horse mackerel and hake abundant according to sources within the industry. The pilchard resource is still under severe pressure, however, and the moratorium on pilchard fishing will remain in place for the next two seasons. Rock lobster TACs for 2019 have been decreased from 230 tonnes to 200 tonnes.

The fishing industry is going through a period of disruption at present. Various long-term fishing rights expired in 2018 leading to 5,176 applications for the 120 rights on offer. There is no guarantee that companies who previously held fishing rights will be awarded new rights which means that some established companies with operational boats will most likely need to acquire rights from new rights holders or partner with them in order to remain sustainable businesses. This is disruptive to say the least.

Amendments to the Marine Resources act in 2015 allowed the minister greater powers in allocating quotas under the unclear conditions of to "advance any social, economic, cultural or other government objective in the public interest". This was followed by a government notice in 2018 which prohibited any listed company from obtaining fishing rights in Namibia. This is once again disruptive and could be destructive, leading to company closures and job losses in a worst-case scenario. Political interference has already led to the exit of Namsov (Bidvest Namibia) from the industry while destroying much value for Namibian pensioners holding Bidvest Namibia stock in the process. While the playing field does not seem to be level, the fishing industry has adapted to the murky environment and the uncertainty surrounding rights is not likely to lead to a major contraction in the industry. If anything the slight increase in quotas and high probability of a contraction in 2018 could see a modest expansion in fishing industry output in 2019.

## Mining and Quarrying

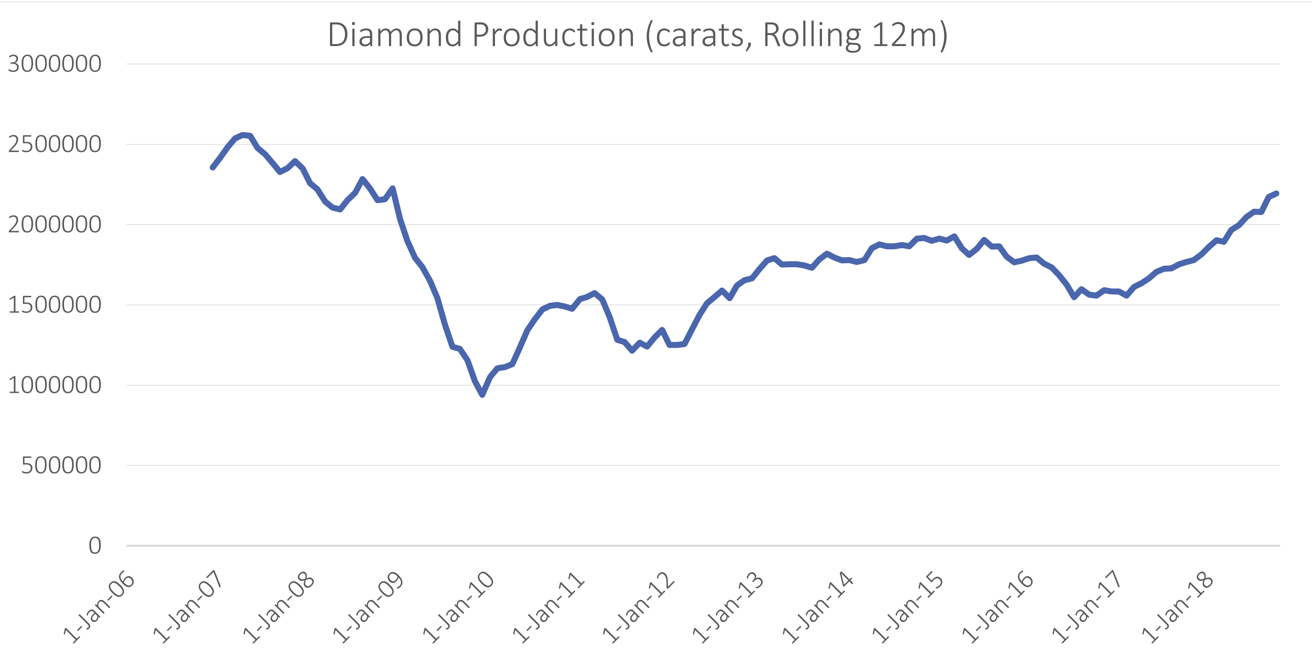
After a strong year in 2017, mining and quarrying is on track for another round of decent performance in 2018 if the latest production figures available are anything to go by. Q3 2018 GDP statistics indicate an 11.0% expansion in the industry on a year-to-date basis. This follows an expansion of 12.8% in 2017 (NSA data), largely driven by diamond and uranium production increases. As mining is Namibia's largest export industry and foreign exchange earner the recovery in output in 2017 and 2018 has contributed to a decrease in the trade deficit, and provided some stability for the international reserve position. It is for this reason that mining remains a key industry in Namibia.




*Source: NSA*

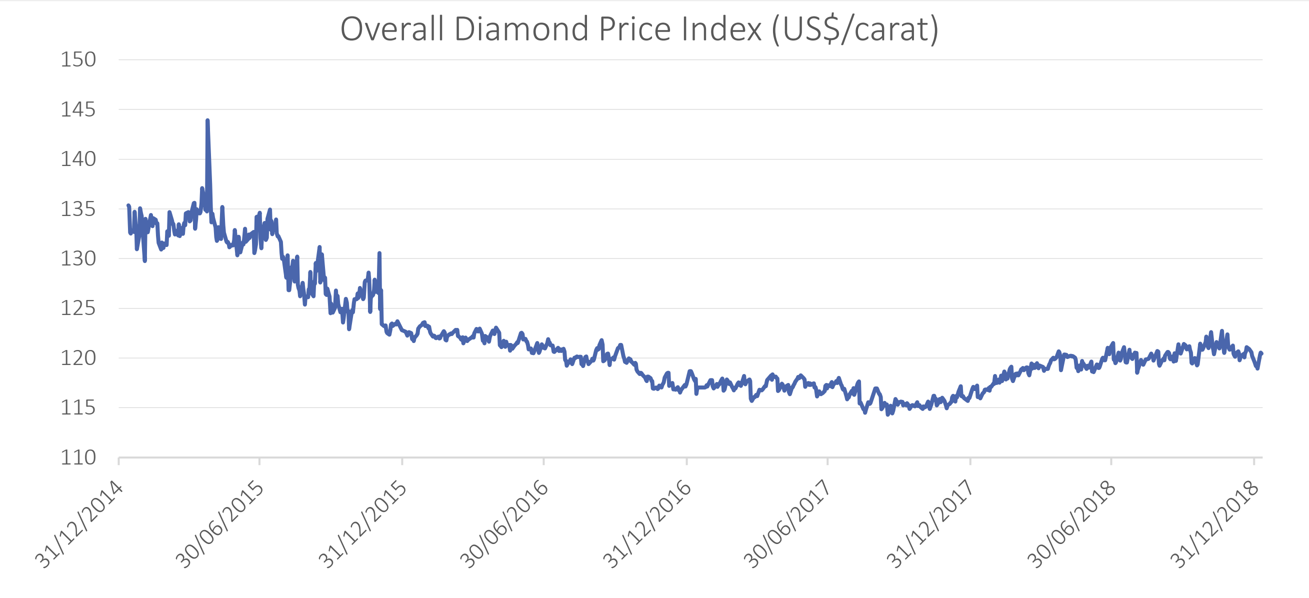
### Diamond Mining

The latest commodities statistics received from the Namibian Chamber of Mines indicate that diamond mining production increased by 14.6% in 2017 and 15.2% in 2018. As growth increased so did royalties to government which further benefitted from an increase in the average price per carat sold. This growth in royalties from the diamond mining industry boosted government revenues at a time when it was most necessary, once again illustrating the value of the partnership for government. Diamond mining activity is a key component to Namibia's economy for this reason.




*Source: Chamber of Mines, IJG*

Due to the elevated base set in 2018 and the phasing out of the land-based diamond mining operations we do not expect to see further growth in diamond production in 2019. The Elizabeth Bay mine situated south of Lüderitz remains up for sale with activity reduced to a minimum. This mine produced in the region of 200,000 carats of rough diamonds in 2017 and, we assume, slightly more in 2018. Removing this production alone should lead to a drop of close to 10% on overall production.

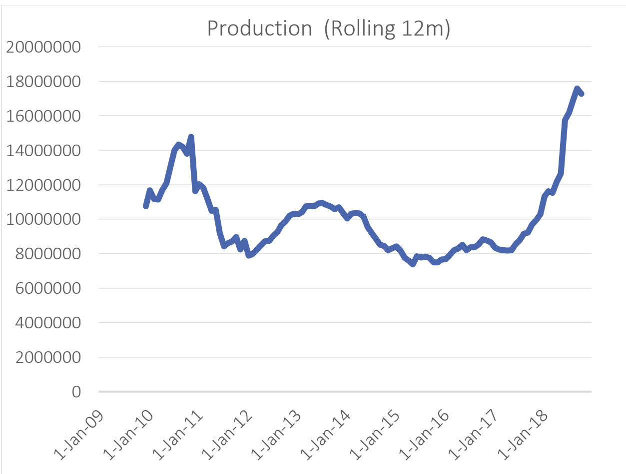


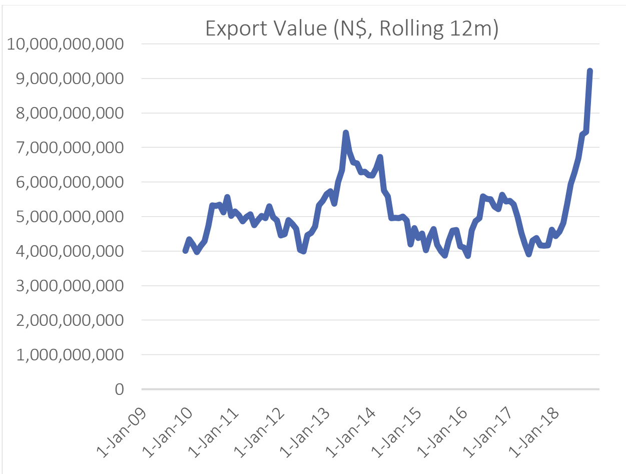

*Source: Polishedprices.com, Bloomberg*

Further adding to the expected decrease in production in 2019 is the scheduled maintenance of vessels by Debmarine. The maintenance schedules run on three-year intervals and a drop in marine diamond production is expected at these times. The combined impact of the decreases in land based and marine mining is likely to see diamond production drop by between 10% and 15% in 2019, after which some recovery can be expected in 2020. The impact of reduced production will be a decrease in taxes and royalties to government, although such a decrease will be anticipated by the ministry of finance and planned for accordingly. An increase in diamond prices as well as a depreciating currency may provide something of a buffer to royalty and tax income.

## Uranium Mining

Uranium production grew by 68.8% in 2018 as per the Chamber of Mines. This is a positive growth surprise versus our expectations for growth of just over 60% in uranium production in 2018. The Husab mine was expected to be the driver of most of this growth in uranium output, as we expected production to more or less double from what was produced in 2017. It seems as though the Husab mine did not quite produce as much as we expected and that the Rössing and Langer Heinrich mines churned out more uranium than we forecast. This is despite the Langer Heinrich mine going into care and maintenance in August.

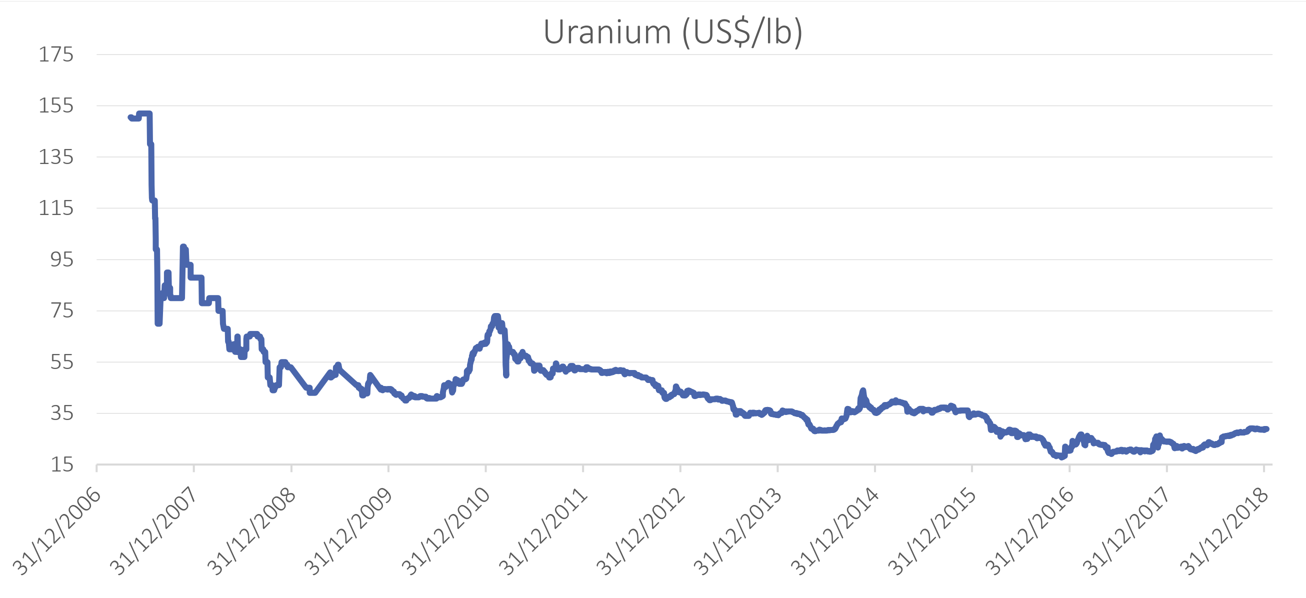



*Source: Chamber of Mines*

Uranium prices remain under pressure despite being up over 20% for 2018. Spot prices remain under US$30/lb, a far cry from the US$45/lb most of Namibia's mines need to operate sustainably and profitably. Significant developments in terms of production cuts from some of the world's largest producers have seen a consistent rise in prices, but not sufficiently so as to aid Langer Heinrich. It is unlikely that Langer Heinrich will start up again in 2019 as we do not expect to see such a rapid increase in prices during the year.

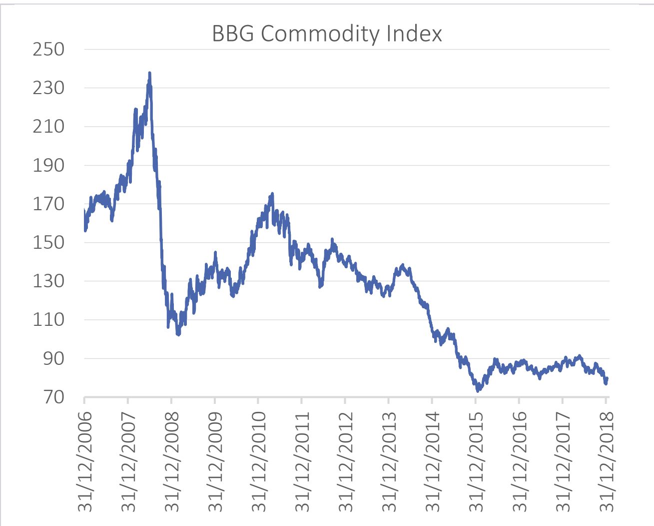
For 2019 we expect a further ramp up of production at the Husab mine to around 75% of nameplate production capacity. This would be an increase of over 10% on the expected production volumes for 2018. This increase is thus unlikely to make up for the drop in production from the Langer Heinrich mine which leads us to believe that uranium output as a whole is likely to contract in 2019, albeit from a high base.

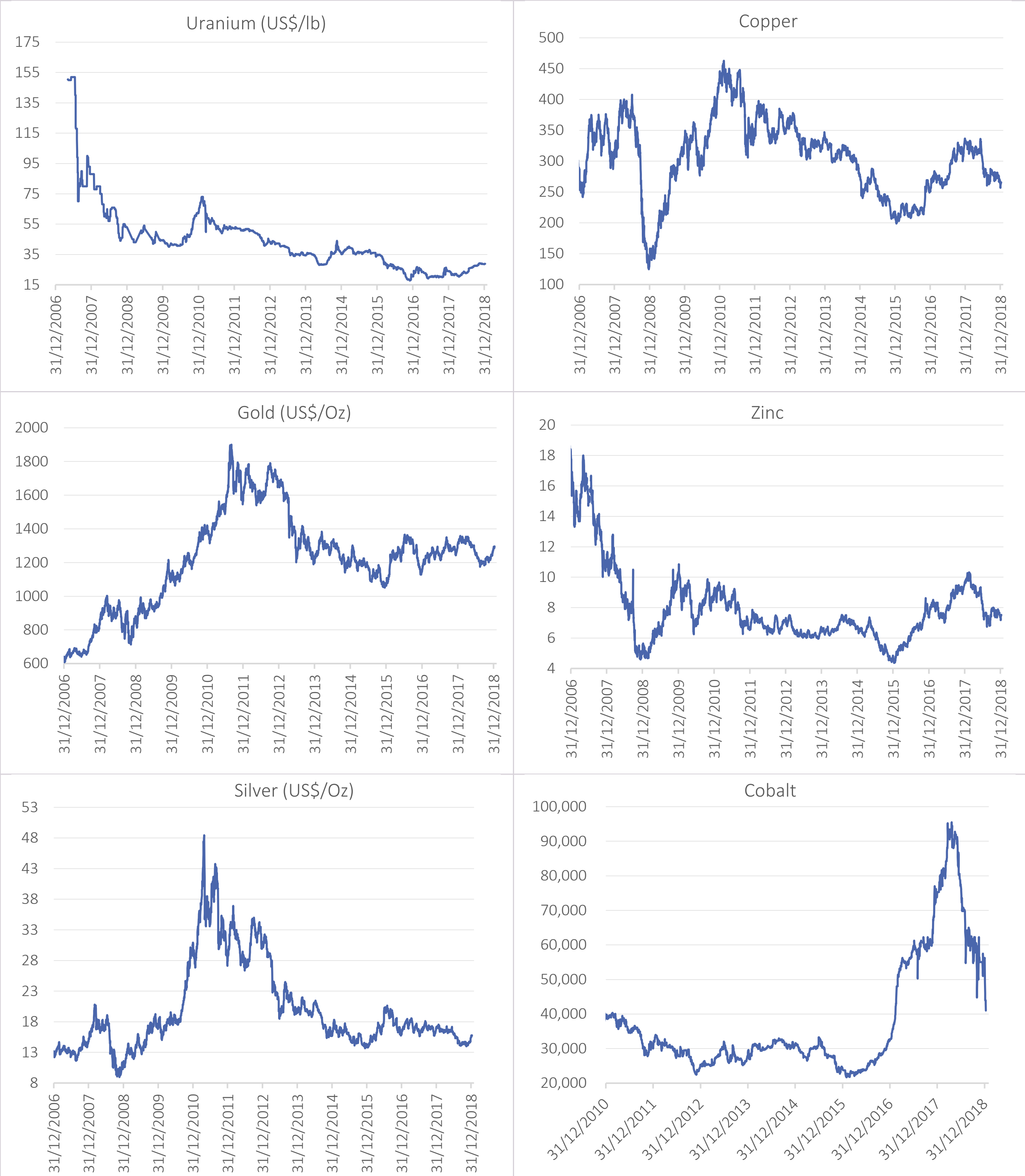



*Source: Bloomberg*

## Other Mining Activities

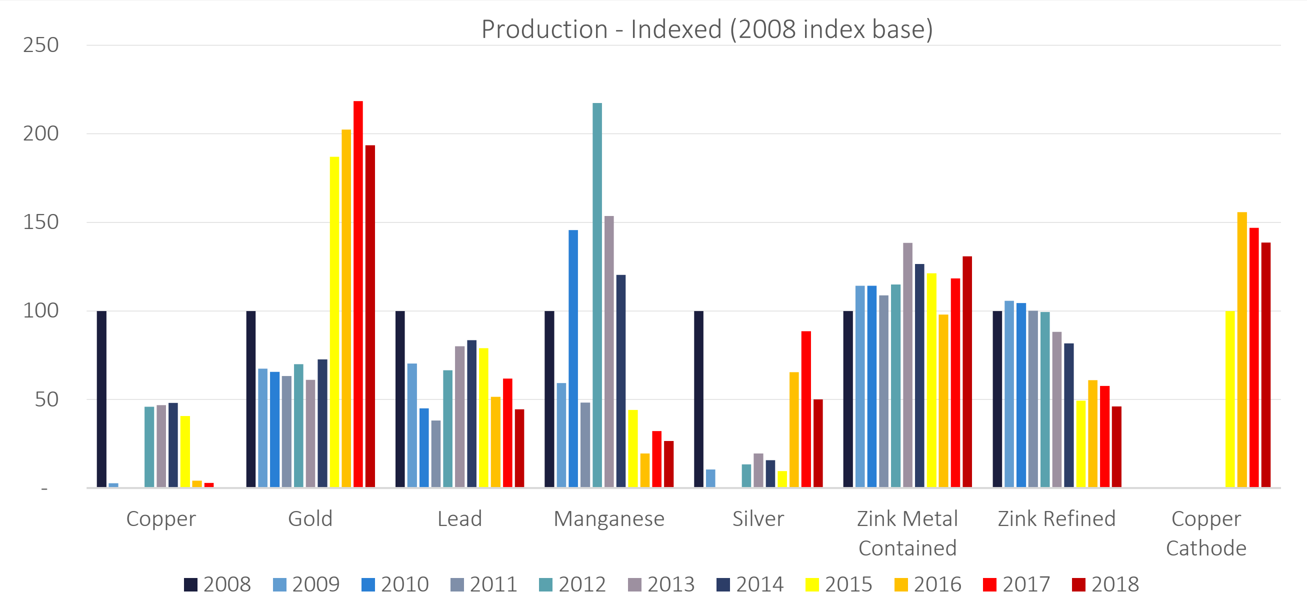
In last year's outlook we were optimistic regarding the trends in commodity prices being seen early in the year. Prices for a wide range of commodities were pushing higher and a flood of exploration activity was sweeping through the country as a result. This optimistic trend turned by April, or a few months later for commodities such as cobalt, with prices retracing across a range of commodities as illustrated by the Bloomberg Commodity Index and other figures below. Currency depreciation absorbed some of the impact of the price decline however, meaning that Namibian miners were less hard hit in Namibia dollar terms.




*Source: Bloomberg*

While output for the mining sector as a whole should post growth in the region of 18% in 2018, most of this growth was driven by uranium and diamond production increases. The figure below shows the output of various metals and elements over the last 10 years, indexed to show relative output (we used 2008 as a base year). For the most part volumes produced have declined in 2018, albeit from high bases in some commodities such as gold and copper cathodes (which value add is classified as manufacturing activity). We explore some of the more important (in terms of economic contribution) commodities below.




*Source: Chamber of Mines*

## *Gold*

Gold production decreased by 11.4% in 2018, albeit from an elevated base. While the B2Gold mine continued to exceed expectations, the Navachab mine has been struggling. Mining of the main ore body at Navachab has not recommenced as it remains inaccessible. Efforts to raise funding to access the main ore body have not materialised and mining of peripheral (or satellite) pits has not produced enough funds to enable access to the main ore body. These satellite pits were expected to produce the required cashflow to strip material in order to access the main ore body, but yields have not been supportive of this. That said, Navachab is the smaller of the two mines and even with very little output from this mine Namibian gold production remains elevated versus the period prior to 2014 due to the B2Gold mine's solid performance. The B2Gold mine has been a consistent outperformer and should produce at or around current levels for the foreseeable future. Should the Navachab mine manage to secure funding to allow access to the main ore body we would expect to see growth in gold output in 2019. We however do not expect this to materialise and have not worked such a scenario into our forecasts for 2019.

## *Copper*

Production of copper cathodes fell by 5.7% in 2018, a drop in output for the second year in a row. While base effects are present in the decrease in output, water troubles at the Tschudi mine have made mining conditions more difficult than anticipated. In July it was announced that significant water ingress was making it difficult to access the ore, and that funds were mobilised to expand pumping capacity at the mine. At that time it was expected that production would recover by December 2018. Production figures show a drop in copper cathode production mid-2018 but some recovery in the last part of the year. Little more information has been circulated to the market regarding the progress made and whether the measures put in place were sufficient to allow mining to ramp up to full capacity. Weatherly International, the owner of the Tschudi mine, remains under administration and the shares have ceased trading, increasing the overall uncertainty regarding the future of the mine. We expect production to continue but have tempered our expected output due to the uncertainty regarding the parent company's future.

## *Zinc*

Zinc production was a mixed bag in 2018 as zinc production from the Rosh Pinah mine increased by 5.1% while refined zinc production from Skorpion declined by 19.9%. The Skorpion product is the higher value of the two and the mine's output is substantially higher than that of Rosh Pinah. As a result, Namibian zinc production as a whole decreased during the year. The Skorpion mine's life of mine was extended to 2020 in 2017 and the figure above (refined zinc specifically) shows that yields have been decreasing as time has passed. The drop in output is attributed to lower ore grades as well as maintenance shutdowns. Key to the mine's survival rests on the conversion of the smelter to refine zinc sulphide concentrate from the Gamsberg mine being developed in South Africa. It is likely that refined zinc from the Skorpion mine itself will underperform guidance, given the reduced ore quality. This does not necessarily mean that production will drop from the low base created in 2018. We expect to see some increase in refined zinc production from the 67,000 produced in 2018 given that guidance suggests 130,000 tonnes is possible.

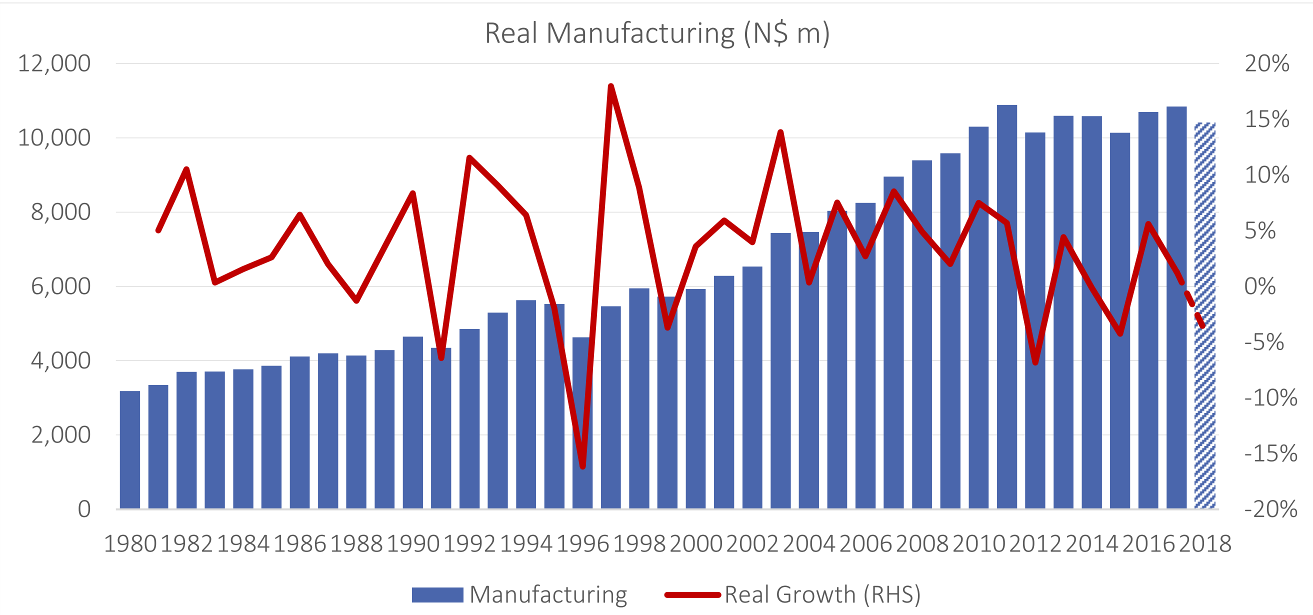
While zinc production at Rosh Pinah grew in 2018, Vancouver based Trevali Mining Corp, the owner of the mine since its purchase from Glencore in 2017, has released guidance that it too is expecting lower ore grades, and for that to lead to a reduction in output at the mine in 2019. Rosh Pinah benefits from a longer life of mine than Skorpion, with the latest estimate for production up to 2025. As the mine has been operational for 50 years this year it may be expected that the ore grade may not be what it once was, although this would be presumptuous as output has only been higher than in 2018 once in the last ten years. It is therefore not inconceivable that the life of mine may be extended beyond 2025 as various technological improvements in the mining process may enable such extension.

Overall we expect zinc production to remain relatively stable as Skorpion could post higher production in 2019 while Rosh Pinah is expected to produce less zinc. We anticipate these fluctuations in zinc production to have a limited impact on GDP growth in 2019 after which we expect to see a decline in zinc production as the Skorpion mine reaches the end of its life of mine.

## Manufacturing

Manufacturing in Namibia peaked in 2011 in real terms, after which it has remained relatively constant. The sector has not shown growth but remains critical to the economy due to the high multiplier effects associated with manufacturing activity. In 2017 manufacturing encompassed around 10% of the Namibian economy, down from 12.5% in 2011 and 13.2% in 1994. This comparison illustrates the difficulties associated with manufacturing in Namibia, with a sparse population and limited resources such as water and electricity. Achieving economies of scale in order to compete with imported products will always be a challenge in Namibia. Namibia has few competitive advantages when it comes to manufacturing and this is reflected in the stagnation of the industry despite tax incentives.

The March 2018 budget speech saw a host of proposed tax including the proposal to repeal the Export Processing Zones (EPZ) Act which provided certain manufacturers in Namibian with preferential tax treatment, amongst other things. Pressure from the EU regarding the preferential treatment of manufacturers seems to have been the main reason for the finance ministry's decision to relook at this legislation. The EPZ has not, as illustrated in the manufacturing GDP figures, led to a meaningful increase in manufacturing activities in Namibia over the last decade, with many previous EPZ companies rather opting to operate as normal companies in order to service the local market. For now, manufacturing status and the EPZ have been put on hold but not replaced by the proposed Special Economic Zones (SEZ) legislation.




*Source: NSA*

The Growth at Home strategy and Retail Charter remain as aspiring industrialisation strategies but are still not receiving the support needed to lead to meaningful growth in Namibian manufacturing activity. There has been much talk surrounding these documents but a lack of focus in execution thereof. Anyone interested in reading the Growth at Home document will be forced to turn off their antivirus protection just in order to access the Ministry of Trade and Industry's website, illustrating this point.

Noteworthy manufacturing projects on the horizon are the Otavi Steel Manufacturing facility and the Peugeot Assembly Plant in Walvis Bay. The Otavi plant will be constructed over the next two years or so with the aim of manufacturing simple steel products such as rebar from scrap metals. The Peugeot facility was launched in December 2018 and will assemble imported vehicle kits for the Namibian and Southern African markets. The Peugeot factory and Otavi steel plant are expected to add to manufacturing output in 2019 and 2021 respectively.

Q3 2018 GDP data showed a year-to-date decline in manufacturing activity of 5.1%, after expanding by 1.3% y/y in 2017. We suspect that the decrease in copper cathode production played a major role in the 2018 slowdown and that manufacturing is likely to record a full year contraction of around 2.8%. This is well below our 2018 Outlook expectation for growth of 2.6% and indicates how sensitive manufacturing activity is to a few key sectors such as copper cathode production. We expect a rebound in manufacturing activity in 2019 due to increased output in copper cathodes, a rebound in beverage production, as well as vehicle assembly.

## Electricity

The Namibian economy is dependent on the stable, uninterrupted supply of affordable electricity for economic growth to occur. As the country's three power stations do not have the capacity to generate enough electricity to meet domestic demand, most of the country's electricity supply is still imported.

NamPower's three power stations have a combined installed capacity of 489.5 MW, of which the Ruacana Power Station is the largest with an installed capacity of 347 MW. The output of the power station varies depending on the flow of the Kunene River. According to NamPower, the average river flow in the last year was significantly lower than average, due to lower rainfall in the catchment region than the year before. In its 2018 Annual Report, the power utility stated that the total energy generated by the power station in the 2017/18 financial year amounted to 1,144 GWh, which is below the annual average of 1,500 GWh. As a result of the low river flows recorded last year, and the subsequent lower power generation, Namibia's dependence on regional trading partners to meet domestic energy demand increased. Imports from neighbouring countries increased from 63% in 2017 to 73% for the period ended 30 June 2018. Independent Power Producers (IPPs) contributed 3% of the total energy generated during the year according to the 2018 Annual Report.

NamPower's South African counterpart, Eskom, is struggling to service its R419 billion debt while maintaining ageing infrastructure. As Namibia sources the majority of the power it imports from Eskom this poses some risk to the power outlook locally. Namibia currently has a contract with Eskom to import 200 MW until March 2022, with an option to renew. Should Eskom's woes result in a larger than expected load shedding exercise it will affect Namibia proportionally due to this contract. The risk that the contract is forfeited completely is minor in our view as Namibia is a paying customer with strong political ties that may be damaged by a breach of contract. Of larger concern is the possibility for a tariff hike of 17.4% by Eskom (if approved by the National Energy Regulator of South Africa), which would definitely mean more expensive electricity for Namibians as well. Security of supply is however not a major threat due to excess generation capacity within the Southern African Power Pool (SAPP) and the small amounts (relative) that Namibia consumes should be easily acquired on the day ahead market (DAM), albeit at a cost.

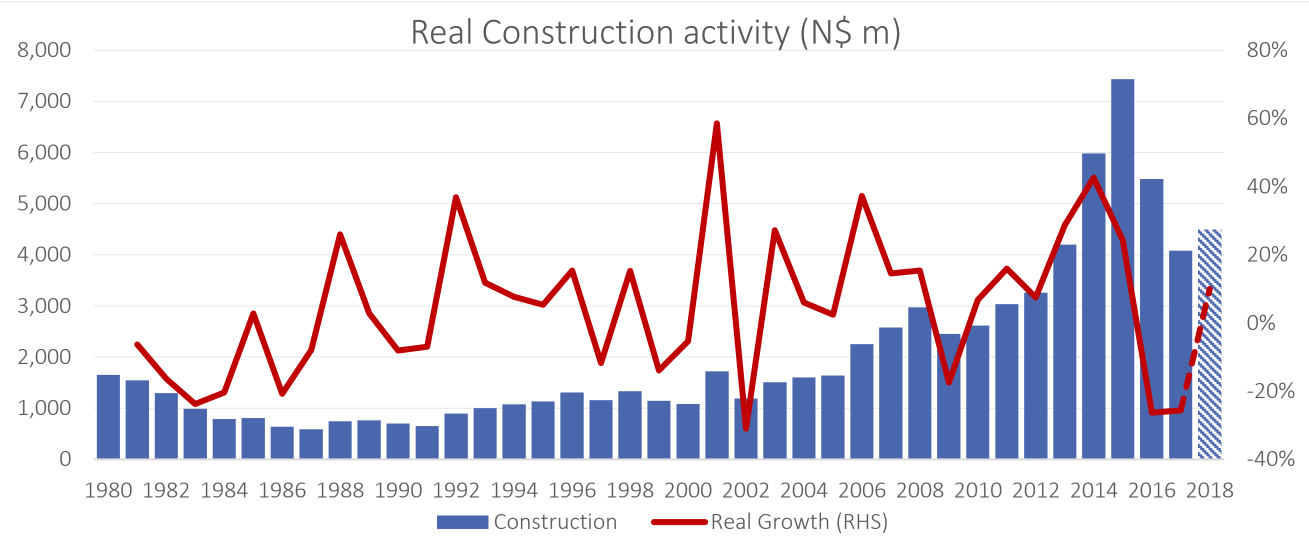
The 120 MW, coal-fired Van Eck Power Station in Windhoek is still being refurbished and work on it should be completed fairly soon according to NamPower. The power station remains a relatively expensive source of electricity, and as such will not be used to supply the country with electricity full time, as other energy sources are currently cheaper. The power station will however remain a safety net during periods of high electricity use. The Anixas Power Station in Walvis Bay, which runs on diesel and heavy fuel oil, continues to be on stand-by in the case of an emergency. The plant has an installed capacity of 22.5 MW.

It remains highly unlikely that anything will come from the Kudu Gas project, as it has seen numerous delays in the last 25 years. NamPower announced in April that the project will be resized down to 442.5 MW from the initially planned 850 MW after power purchase agreements with Eskom and Zambia's Copperbelt Energy Corporation failed to materialise. Towards the end of the year, Mines and Energy Minister Tom Alweendo however aired his scepticism on whether the project will ever start, stating that he is not convinced that it is viable. Finance minister Calle Schlettwein also stated during the year that the financial risk is too big for an already constrained government, and continuation of the project would mean that government "will have to close the door on other potential alternative sources of energy".

The Ministry of Mines and Energy last year announced that 220 MW of additional power will be added to the grid over the next three years. The 220 MW allocation will be subdivided with 150 MW allocated to NamPower and 70 MW allocated to IPPs by means of a competitive bidding process. Of the 70 MW, 20 MW will be allocated to solar power and 50 MW to wind power. These projects are likely to be positive from a cost point of view, as the offtake agreements will be more competitively priced than the REFIT programme was. The objective is to minimise cost escalation going forward while increasing in-country generation. Electricity is already expensive in Namibia and energy solutions need to be cost effective in order to improve competitiveness in this regard. Overall, Namibia is unlikely to see load shedding during the medium term due to the regional surplus as well as the favourable PPA with Eskom. The low probability of being without power is supportive of economic activity, and it is encouraging to see the electricity sector not acting as a major drag on activity in Namibia as it is likely to be this year in South Africa.

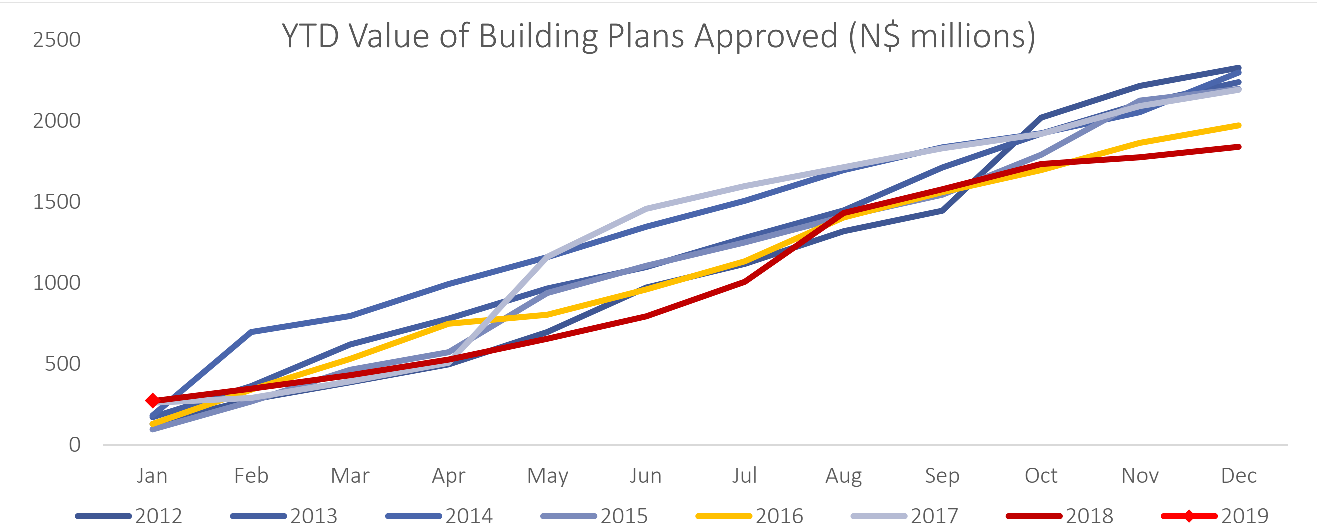
## Construction

The construction sector has taken the brunt of the economic slowdown in Namibia, contracting by 26.3% in 2016 and 25.6% in 2017. Construction output in 2017 was below that of 2013, indicating the extent of the slowdown. Q3 GDP data for 2018 indicates somewhat of a recovery in the industry with year-to-date growth of 13.5%, although building plans for the capital show a continued slowdown in activity.



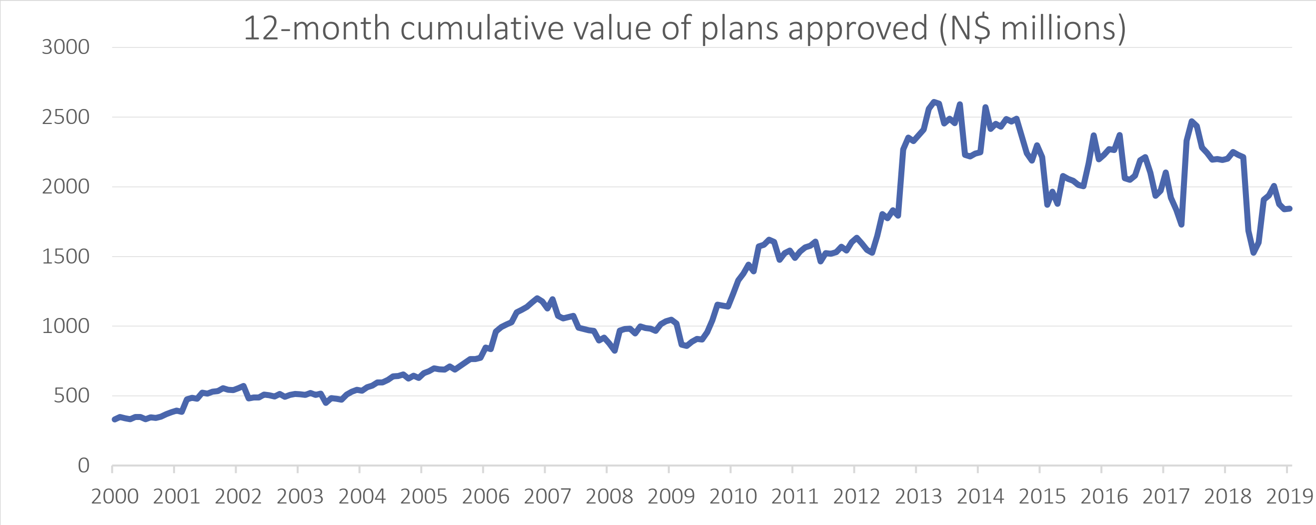

*Source: NSA*

During 2018 the Neckartal dam project was completed with construction ending in the final quarter of the year. This project cost approximately N$5.7 billion and employed around 2,000 people. Construction is transitory, and the completion of a large project such as Neckartal leads to a decrease in construction activity and output. Job losses are expected as the current state of the industry and the lack of infrastructure projects means that there are few jobs available for those workers who were employed at the Neckartal project to go to. The completion of another large-scale project, the Walvis Bay fuel storage terminal, was also achieved in 2018 and will further add to the decrease in output from the industry and increase in unemployed construction workers.




*Source: City of Windhoek*

Risk appetite and investor confidence remains low in Namibia. The overhang of an uncertain policy environment has resulted in a weary approach to applying capital. Banks are similarly cautious when it comes to lending, especially with regards to construction projects. Thus, despite interest rates being accommodative, mortgage lending grew by only 6.6% in 2018, barely above inflation. Cumulative mortgage loans to corporates, which may be viewed as productive mortgage loans, grew by only 2.6% y/y in December 2018. Business confidence is thus still severely depressed, and even more so in the construction industry where businesses are still closing their doors and professional engineers and architects among the rising number of unemployed.




*Source: City of Windhoek (not adjusted for inflation, data for Windhoek only)*

While we may see some growth in construction in 2018 due to base effects, it is likely to be well below the Q3 year-to-date figure of 13.5% due to the completion of Neckartal dam. Commercial projects have been few and far between and leading indicators such as the value of plans approved (above figure) point to a continuation of the subdued activity of the previous three years. Government's commitment to infrastructure projects remains constrained by poor revenue growth and a rapidly growing debt burden. 2019 is however an election year which may bring some relief to the industry as government may be tempted to increase spending. Such spending is more likely to contribute to the operational budget than the development budget but will result in an increase in money in the pockets of Namibians which could drive some demand.

Of more importance will be the deployment of various loans and grants into infrastructure projects such as road and rail network expansions, amongst others. A summary table of the projects approved for financing by the African Development Bank loan is included below. The projects to be financed are not new projects, but rather existing development budget projects for which the funding source has changed. The approval of AfDB funding for these projects last year allowed the ministry of finance to reallocate the funds it had planned for these projects to the operational budget. Furthermore, funding from German development bank, KfW, and the Chinese Exim bank into road projects through the RFA add to the funds flowing into infrastructure.

| *AfDB Loan Utilisation* | 2019/20 | 2020/21 | 2021/22 |
|---|---|---|---|
| *AfDB Loan Mechanisation program (Agriculture)* | 225 | 170 | 171 |
| *AfDB Loan Transport (Rail ZAR1,350)* | 386 | 514 | 514 |
| *AfDB Loan Transport (Road)* | 259 | 330 | 330 |
| *AfDB Loan Basic Education (School Renovation)* | 198 | 395 | 396 |
| ***Total*** | 1,068 | 1,409 | 1,411 |

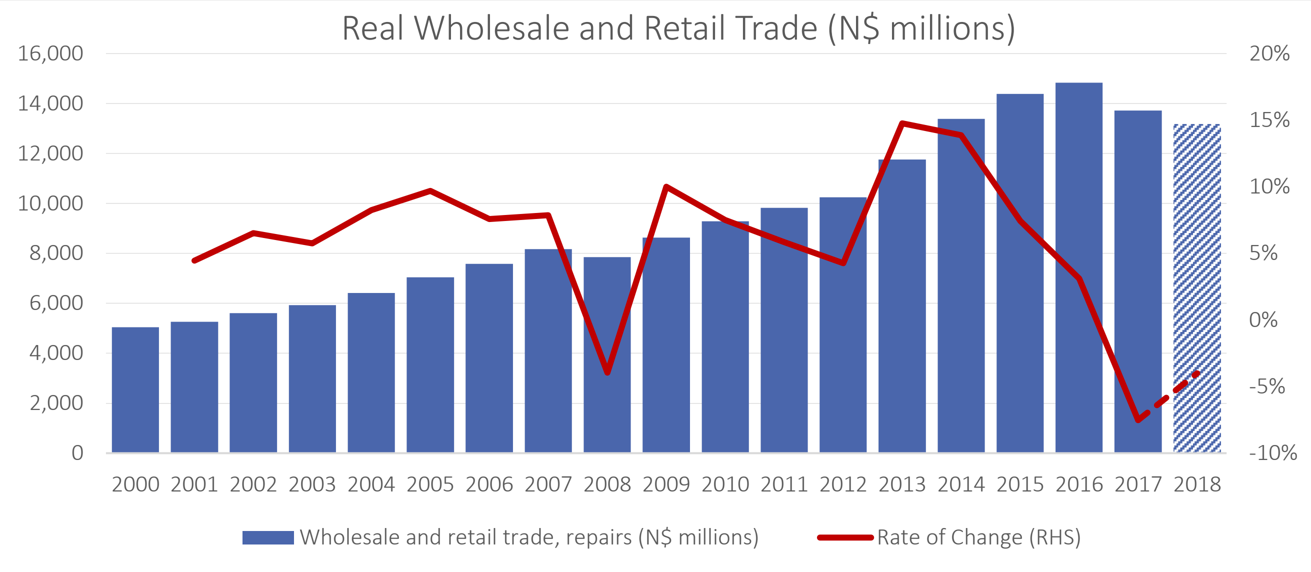
*Source: MoF*

The flow of funds into infrastructure in 2019 allows for a continuation of activity rather than a large-scale expansion of activity. The development portion of government's budget has been shrinking in relation to total expenditure for a number of years now, meaning that government infrastructure spend cannot, at present levels, lead to a significant uptick in GDP growth. Government and SOE infrastructure spend provides a base for construction activity, but is unlikely to return to levels seen between 2011 and 2015 due to structural hurdles in government's expenditure profile. Nevertheless even the limited increase in activity we expect is likely to drive some growth in the construction sector due to the low base created in 2016 and 2017.

Private sector investment is depressed at present and is taking longer to recover due to policy overhangs and the uncertainty this creates. Should we see policy clarity during the year there may be some upside for the construction sector as businesses that have held off on investment deploy funds. We expect overall performance in the construction sector to remain depressed when compared to 2015 levels, but that base effects allow for modest growth.

## Wholesale and Retail Trade

Wholesale and retail trade activity is set to record another contraction in 2018, with Q3 2018 year-to-date figures indicating a contraction of 5.0%. This follows a real contraction of 7.5% seen in 2017. As the single largest line-item in the National Accounts and one of the best indicators of consumer activity, this contraction perhaps best reflects the "feeling" of the average Namibian. High frequency indicators such as credit extension and vehicle sales corroborate the contraction shown in the National Accounts figures. An increase in unemployment as well as more difficult wage negotiations during the last two years has contributed to the contraction in activity in this industry and the depressed consumer confidence experienced at present.




*Source: NSA*

Perhaps the most concerning conclusion to be drawn by the further contraction in wholesale and retail trade activity in 2018 is that consumer confidence in general remains depressed. Business confidence is largely reliant on consumer confidence. Businesses do not invest in their operations when demand is low. Thus the fact that consumer confidence has not recovered sufficiently to drive an increase in demand after a protracted period does not bode well for the business climate in 2019 either. The completion of large-scale construction activities such as Neckartal Dam and the fuel storage facility in Walvis Bay, and the Langer Heinrich uranium mine being put on care and maintenance have resulted in further increases in unemployment in 2018. Consumer confidence is slow to return whilst unemployment is still growing.

The outlook for wholesale and retail trade thus seems bleak for 2019, but we do expect one source of relief: government spending. With Namibian presidential and government elections set to take place in November this year there is an increased likelihood of above inflation wage settlements within government and SOEs, as well as social grant expenditure. As a large proportion of the population derive some benefit from such expenditure we expect to see this have an impact on wholesale and retail trade in 2019. The extent of this impact will be limited by government's ability to raise debt and as such we now expect the budget deficit for 2019/20 to be larger than that proposed in the latest medium-term expenditure framework (MTEF).

## Tourism

Annual GDP data for 2017 indicates that the hotels and restaurants industry recorded a contraction of 1.1%. The latest figures released with the Q3 2018 GDP data indicate that 2018 is likely to be another contractionary year for the industry. While the hotels and restaurants industry statistics do not capture the entire impact of tourism on the economy, it does account for most of it. Accommodation and occupancy data from the Hospitality Association of Namibia (HAN) also suggests that the tourism industry has seen a decline in tourist numbers for a second consecutive year. According to the HAN statistics the national accommodation occupancy rate fell from 56.9% in 2017 to 53.0% in 2018. While these statistics are contributed by industry role-players, all role-players do not contribute, meaning that the data is incomplete. However, the correlation with the annual GDP figures leads us to believe that this data is not necessarily inaccurate.

The increasingly popular trend of people listing their backyard flats and unused holiday homes on Airbnb may account for some of the decline in occupancy rates noted above (as these are unlikely to be captured in either dataset), although not nearly to the extent that may be thought. A quick count on the Airbnb website indicates around 300 sites are advertised in Namibia at present. Self-drives may be another reason for the decrease in occupancy levels, although good data on the increased use (anecdotal) of this form of tourism is also lacking.

Namibia frequently appears in top travel destination lists, online as well as in print, which is positive news as it is good publicity for the country and places it on the radar. Service and quality of experience is necessary to keep Namibia in these lists and as such infrastructure such as airports, immigration facilities and roads between destinations is of importance, especially if a greater number of tourists are to be attracted to Namibia.

A big concern in this regard is the Hosea Kutako International Airport which has exceeded its capacity limit in terms of passengers it is capable of handling. The airport was constructed to handle 250,000 passengers per year, but currently sees about 1 million people pass through each year. This affects security measures at the airport, as security staff and immigration officials have to not only deal with more people, but at a faster pace as well to avoid bottlenecks. Although the International Civil Aviation Organisation cleared the airport of significant security concerns at the end of last year, uncertainty surrounding the international status of the airport, and continued media reports of a possible downgrade, had a negative effect on the tourism industry with the Namibia Airports Company reporting that it had seen an increase in the cancellation of scheduled bookings to Namibia last year. Government has however approved a N$245 million upgrade to the airport which, according to the Namibia Airports Company, will be completed before the end of 2019.

While tourism seems to have taken a step or two backwards over the last two years, it remains in healthy shape when compared to most other industries in the country. It is likely that Namibia is fluctuating at, or near, capacity when it comes to the number of tourists that it can accommodate. Infrastructure such as borders, airports, and roads all show signs that they are running at close to full capacity, at least during the peak tourist season, and as such do constrain expansion of the industry. While some of these issues are relatively easy to address, others will require significant funding, which is in short supply at present. Hence we do not expect to see much growth in tourism in 2019, rather stable performance, supporting, rather than driving the economy.

## Interest Rates

In general, global monetary policy was less accommodative in 2018. The year 2019 looks set to be characterised by the continued adaptation to global monetary policy normalisation. The US economy has been expanding steadily and looks set to carry much of that same momentum forward through the first half of 2019. The Federal Open Markets Committee (Fed) had its first meeting of 2019 in January with the chair Jerome Powell delivering a profoundly dovish statement. The Fed is now effectively signalling a slower pace of interest rate increases during 2019 that will be very data dependent. Market sentiment got an additional boost by the possibility of an earlier than expected end to the Fed's balance sheet normalisation regime.

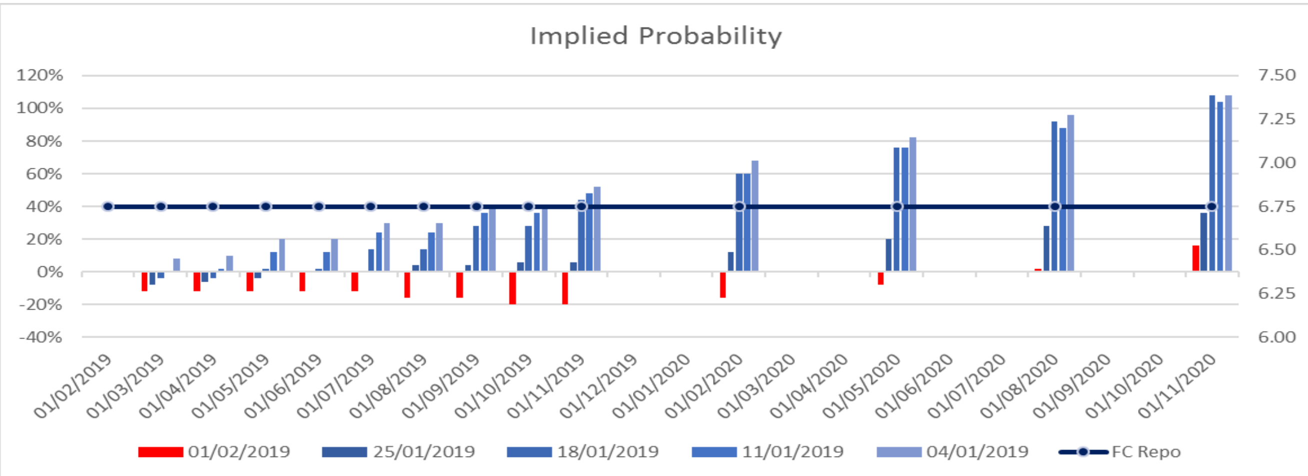
With rates still in negative territory and the European Central Bank's (ECB) quantitative easing (QE) programme having come to an end in December 2018, expectations are now for monetary policy tightening over the next two years, with at least one rate hike pencilled in for 2019. The policy path embarked on by the US and the EU is likely to set the tone for global monetary policy in 2019.

The UK economy had registered its best economic growth in almost two years with Q3 GDP expanding 0.6% q/q. Although GDP data was positive and accompanied by a relatively hawkish November inflation reading, the Bank of England's (BoE) decision on whether to hike rates or not will hinge solely on the outcome of Brexit negotiations. Should the British leave the European Union on a "no-deal" basis, the BoE would need to re-evaluate its policy stance in terms of restricting the impending rise in inflation which would result from this.

Expectations for higher rates and the subsequent tightening of monetary policy in the US was the cause of the broad-based EM sell-off in 2018. The Fed's dovish announcement in January has brought some reprieve for EM countries, which may be a catalyst for EM risk-on sentiment. Internationally, markets will also closely monitor developments regarding the trade war between the US and China with less than a month left before the ceasefire expires on 1 March.

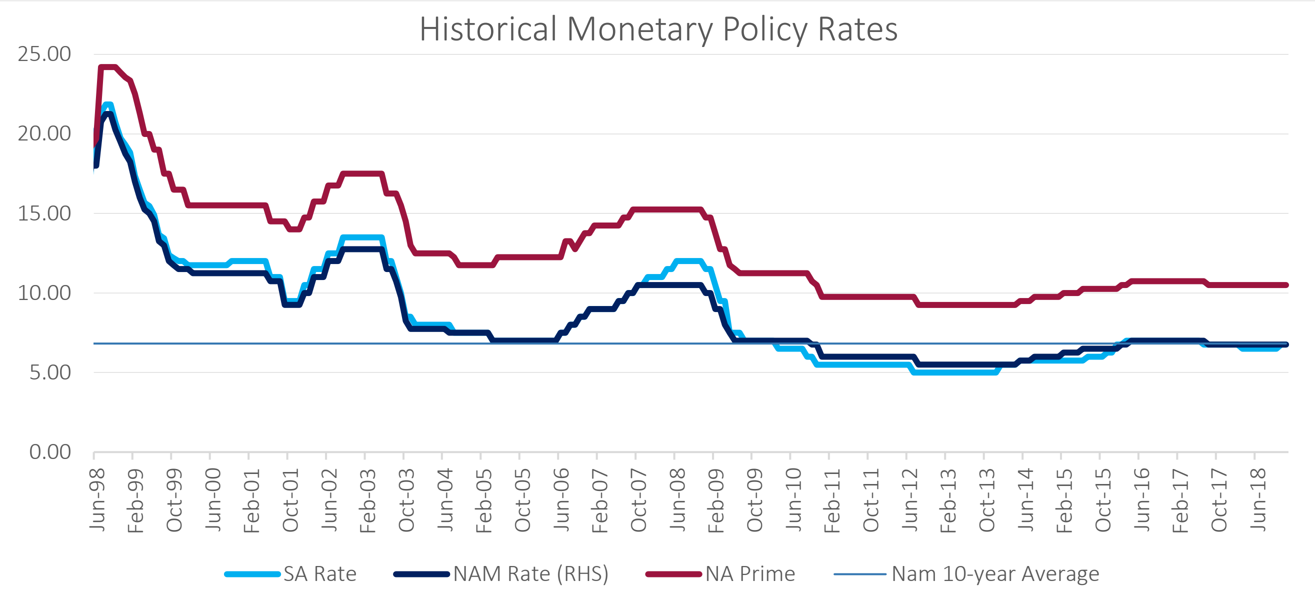
Closer to home, the South African interest rate outlook seems likely to be more accommodative going forward after the 25bps rate hike enacted in November last year. The South African Reserve Bank's (SARB) inflation expectations at that point prompted an early response to inflation possibly breaching target levels. However, falling oil prices and a stronger currency led to a decline in transport inflation which does beg the question whether the November hike was too soon. Looking ahead, SA-specific risks that will impact the rand (and domestic debt markets), and therefore inflation, do remain. One of these risks being the possibility of Moody's releasing a negative ratings assessment of SA's sovereign debt a month after the February 2019 budget statement. Moody's delayed its October released forewarning that a deterioration of SA's fiscal metrics and SOE reform (Eskom) could be credit negative. The repercussions of a Moody's downgrade of SA sovereign debt to sub-investment grade include SA falling out of the Citi World Bond Index, which will lead to a significant capital exodus and a blowout of the rand.

The SARB's forecasts are for inflation to slow to approximately 4.4% in the first quarter of 2019, comfortably close to its mid-range target of 4.5%. The second half of the year, however, could see inflation rising quicker owing to a possible double-digit electricity tariff increase. The risks to the inflation outlook do remain skewed to the upside and the SARB will be mindful of this heading into its March MPC meeting, having kept rates unchanged (widely expected) in January. Furthermore, the FRA curve (measure of market participants expectation of future policy moves) indicates that the market is currently not pricing in any rate hikes in 2019.



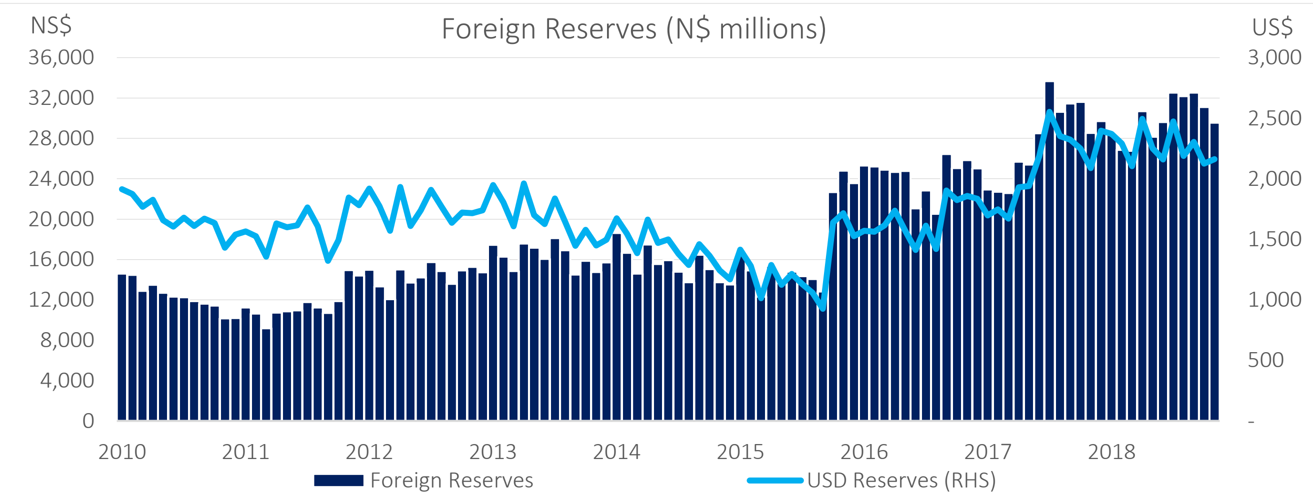

*Source: Bloomberg, IJG Securities*

Locally, interest rates have remained relatively accommodative towards the Namibian consumer and supportive of spurring economic growth. The Bank of Namibia (BoN) ended its hiking cycle in August 2017 and has kept rates unchanged since. While accommodative monetary policy was decidedly pro-cyclical between 2011 and 2015 leading to the overheating of the Namibian economy in 2015, current policy is countercyclical and supportive of the fragile economy. Current monetary policy is more prudent than during the previously mentioned period and less likely to lead to adverse economic conditions as a result.




*Source: Bloomberg, BoN, IJG Securities*

The BoN's approach to monetary policy is governed by its mandate to maintain the one-to-one currency peg with the rand by ensuring the country maintains sufficient foreign reserves. Foreign reserve levels have been volatile since peaking in June 2017. The disbursement of loans to Namibia by the African Development Bank (AfDB) has aided in keeping a sufficient level of foreign reserves to maintain the currency peg. BoN's December money and banking statistics release indicated that an increase in reserves to N$30.9 billion stemmed from the disbursement of the second tranche of N$3.0 billion of AfDB funding.




*Source: Bank of Namibia, IJG*

Namibia's fragile economy and weak fiscal position mean that the country is more exposed to external factors than would be the case had monetary and fiscal policy been applied more prudently between 2011 and 2015. As such the SARB's interest rate trajectory will have significant bearing on BoN's MPC decisions in 2019. Having kept a 25bps buffer above the SARB's interest rates for eight months, BoN was able to afford itself room to leave rates unchanged when the SARB hiked rates in November. With rates once again on par, BoN will be wary of the SARB's interest rate decisions, bearing in mind how the impending political and credit assessment scenarios are likely to play out. Needless to say, BoN cannot find itself in a position where its rates are lower than that of SA. Such a scenario could very well lead to an exodus of capital, which directly puts in jeopardy the foreign reserve position.

Below we have formulated 3 scenarios showing how we believe interest rates are likely to unfold during 2019, based on our assessment of the international monetary environment as well as South African political and economic outlook.

Base Case: BoN hikes by 25bps

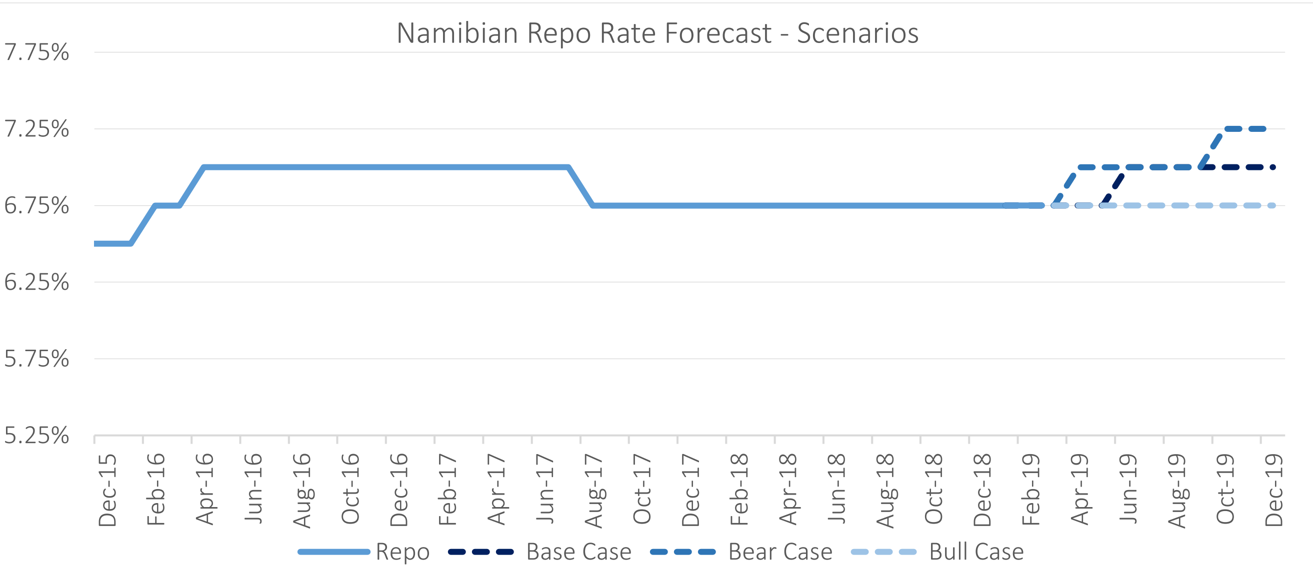
- Our base case is built around the pace of monetary tightening of 1st world central banks such as the US and ECB slowing as per current guidance.
- The US and China amicably resolve trade disputes.
- SA fundamentals prove sufficient to avert a Moody's downgrade.
- SARB hikes by 25bps on back of long-term inflation forecasts skewed to the upside.
- BoN adjust accordingly to keep pace and avoid capital outflows.

Bear Case: BoN hikes twice

- Our bear case is based on the Fed tightening more than expected in 2019.
- The possibility of higher oil prices resulting in higher inflation.
- Moody's downgrades SA to below investment grade resulting in a fallout from the Citi World Bond Index.
- SARB hikes rates to protect a deteriorating currency, and to curb the effects passing through to inflation.
- The BoN adjusts accordingly to preserve foreign reserves levels.

Bull Case: BoN keeps rates flat

- US economy slows faster than anticipated.
- Inflation pressures recede on the back of easing oil prices.
- SA economic growth remains depressed.
- SARB cuts by 25bp on the basis of downward revisions to inflation forecasts.
- BoN keeps rates unchanged once again affording itself a 25bp buffer over South African rates, thus holding onto capital and maintaining sufficient reserves.




*Source: IJG Securities*

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