MID-YEAR BUDGET REVIEW 2019/20

2019/20 - 2021/22

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Key Points from Budget Speech

May be edited for context by IJG analysts

- The (budget) review framework has three distinct policy actions:-

  (i) First, it frees up a resource envelope for re-allocation to alternative priority programmes within the appropriated expenditure ceiling. This is to enable optimal provision of services in areas where shortfalls are anticipated and to achieve enhanced development outcomes,

  (ii) Second, it ring-fences expenditure allocations to capital and development programmes as a way of enhancing growth consistent with sustainable fiscal policy, and

  (iii) Third, it unveils an integrated economic recovery and growth stimulus intervention measures to support short-run economic recovery and sustainable economic growth in the medium and the long-term.

2018/19

- Revenue outturn for 2018/19 amounted to N$55.9bn, 1.4% less than the budgeted N$56.7bn. This reflects shortfalls in non-mining company tax and Value Added Tax due to weak domestic economic activity.
- Total expenditure, including interest payments amounted to N$65.1bn, relative to the N$65.0bn budget.
- The budget deficit was 4.8% of GDP, compared to the budgeted 4.5% due to lower revenue outturn.
- Interest rate payments consumed approximately 11.3% of revenue reflecting the increasing burden of high public debt stock.
- Total debt stood at N$87.5bn, equivalent to 45.2% of GDP.

2018/19

- The preliminary revenue outturn of N$29.4bn, which is 50% of the budgeted revenue and about 2% better than the average half-year collection rate.
- The half-year expenditure execution was N$30.6bn, 46% of the budget.
- The half-year non-interest operational budget expenditure execution, including expenditure commitments was 52%, while the development budget implementation rate at the end of September 2019 was 37%.
- Total debt is expected to remain at the budgeted level of 48.9% of GDP.
- Revenue for FY2019/20 is estimated to remain unchanged at the budgeted N$58.4bn.
- Over the next MTEF, total revenue is projected to increase on average by 3.1%.
- Aggregate expenditure over the next MTEF is projected to increase at an average growth rate of 1.5%.

- At this level of expenditure, the budget deficit will reduce from an estimated 4.1% of GDP in FY2019/20 to about 3.5% in FY2020/21 and reach about 2.5% of GDP by FY2022/23.
- In this framework, total debt as a proportion of GDP is expected to increase to 51.0% in FY2020/21 and stabilize at about 53.1% by FY 2022/23.

Tax Policy and Tax Administration Reforms

- Amendments to the Income Tax Act, Value Added Tax Act and Export Levy Act are proposed to implement the proposals completed during the consultation process. These entail, among others:
    - The taxation of trusts and certain commercial entities.
    - Eliminating base eroding tax holidays and preferential tax rates accorded only to some manufacturers and exporters of manufactured goods for a more uniform treatment of taxpayers through the establishment of the Special Economic Zone.
    - Eliminating certain base eroding exemptions and VAT zero-rating of certain goods.
- Necessary research and investigation will be made on the possibility of introducing a lower tax regime for small businesses as a means of encouraging entrepreneurship and business growth.
- Residents will be required to pay a 10% tax on dividends to enhance the fairness of the tax system and dividend income will be taxed the same as other streams of passive income such as interest income.
- Eliminate the loophole that lead to conduit (flow through) principle, through harmonisation of the taxation of trading trusts in line with regional economies.

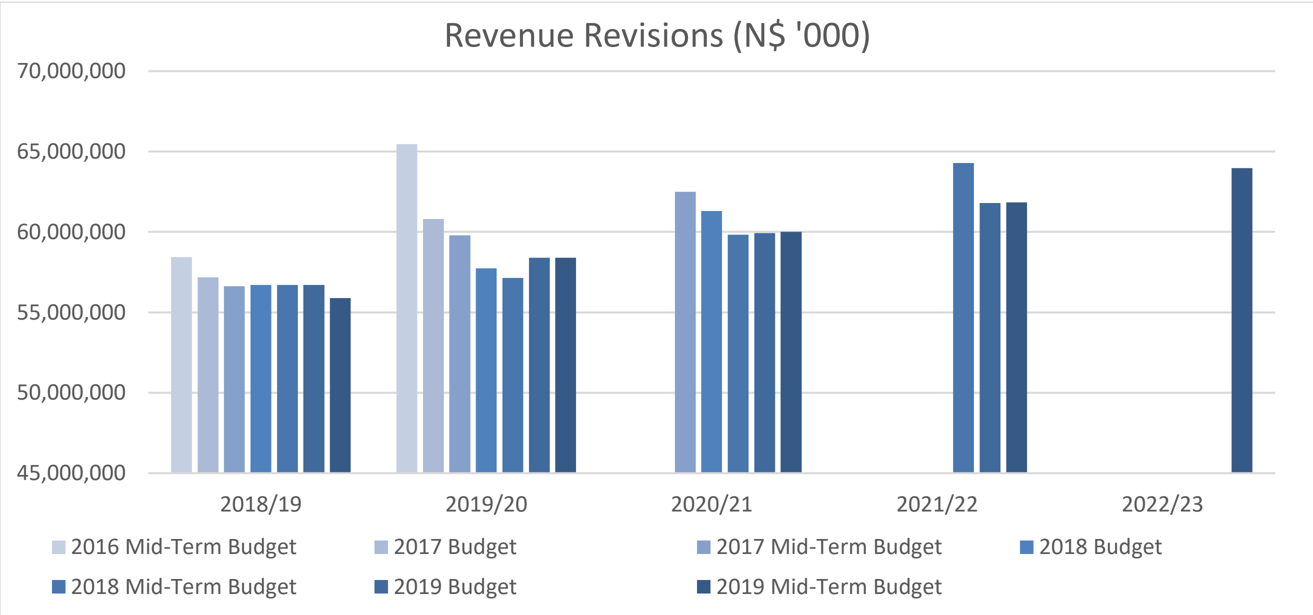
The FY2019/20 Appropriation Amendment Bill

- In regard to the FY2019/20 Appropriation Amendment Bill, a total of N$1.18bn was freed up through expenditure cuts during the Mid-Year Budget Review process. This amount comprises of N$176.32m realized from the Operational budget on personnel emoluments and N$999.59m from the Development Budget.
- The proposed reallocation is to meet essential needs for the smooth conduct of elections with further budgetary support to the Electoral Commission of Namibia and the Ministry of Safety and Security, needs in the Basic Education Sector, Health and Social Services in respect of procurement of pharmaceuticals, supporting funding needs of the Namibian Broadcasting Corporation, Drought Relief and Social Grants needs.

Revenue

2018/19 Outturn

The revised revenue collection for 2018/19 came in at N$55.88bn, 1.4% below the revised March figure. The N$822m shortfall stems mostly from shortfalls in non-mining company tax, value-added tax, coupled with lower than expected SACU revenue. In the March budget the ministry noted that it does not expect any shortfalls, but pointed out that collection pressures remain for these tax categories. This should not come as a complete surprise as domestic economic growth has been stagnant since 2016 and has put both businesses and consumers under severe pressure.

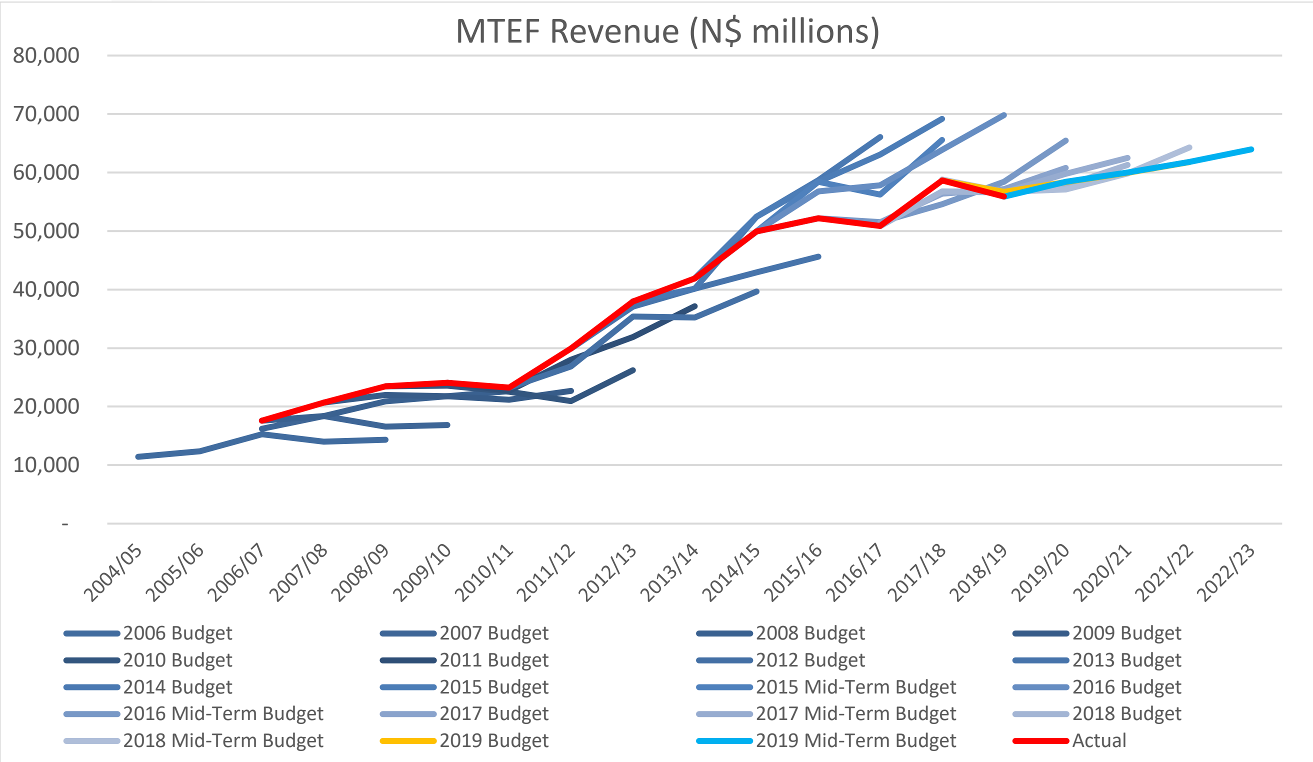


Source: MoF, IJG Securities

Revenue collection for 2018/19 was 4.7% lower than that of 2017/18. Value-added tax revenue fell 4.9% to N$11.46bn, while non-mining company tax decreased by 6.8% compared to 2017/18. SACU receipts came in 10.1% lower than the prior year.

Total revenue to GDP amounted to 28.8% in 2018/19, which is lower than the 30.2% forecasted in the March budget. This is also a decrease from the 32.0% total revenue to GDP figure of 2017/18 as nominal GDP increased and revenue decreased.

2019/20 Budget Review

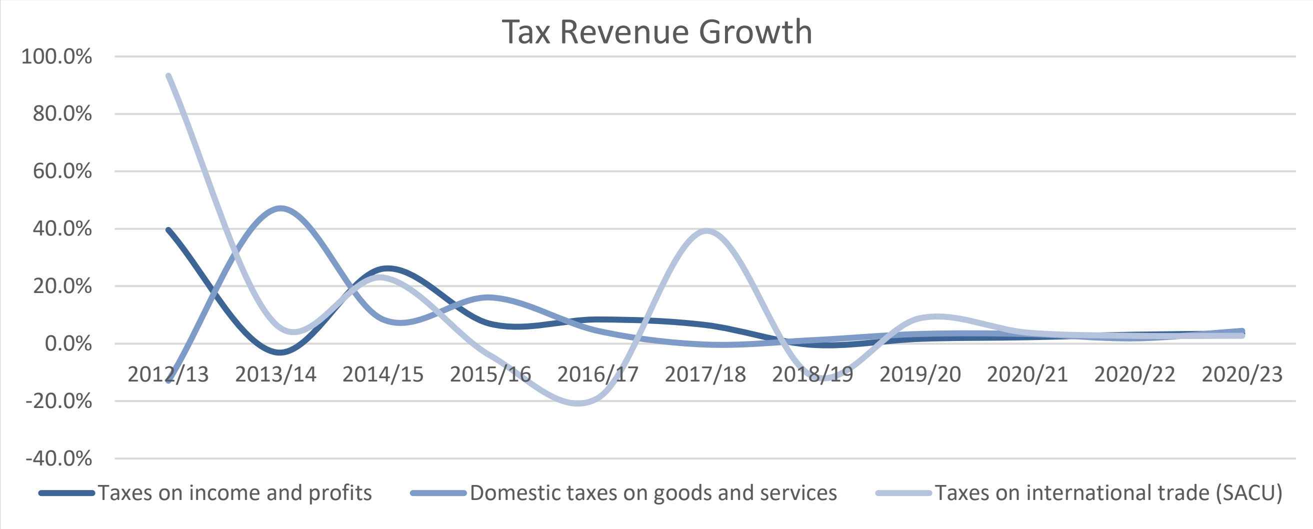


Source: MoF, IJG Securities

According to the Ministry of Finance, the mid-year revenue outturn amounted to N$29.4bn, which is 50.3% of the budget revenue for the current year. The minister noted that this rate is 2.4% better than the revenue collected at the same period last year. Total revenue for 2019/20 is expected to fall short of the March estimate by N$138m at N$58.54bn. This is however still N$2.52bn (or 4.5%) more than the revenue collection in 2018/19.

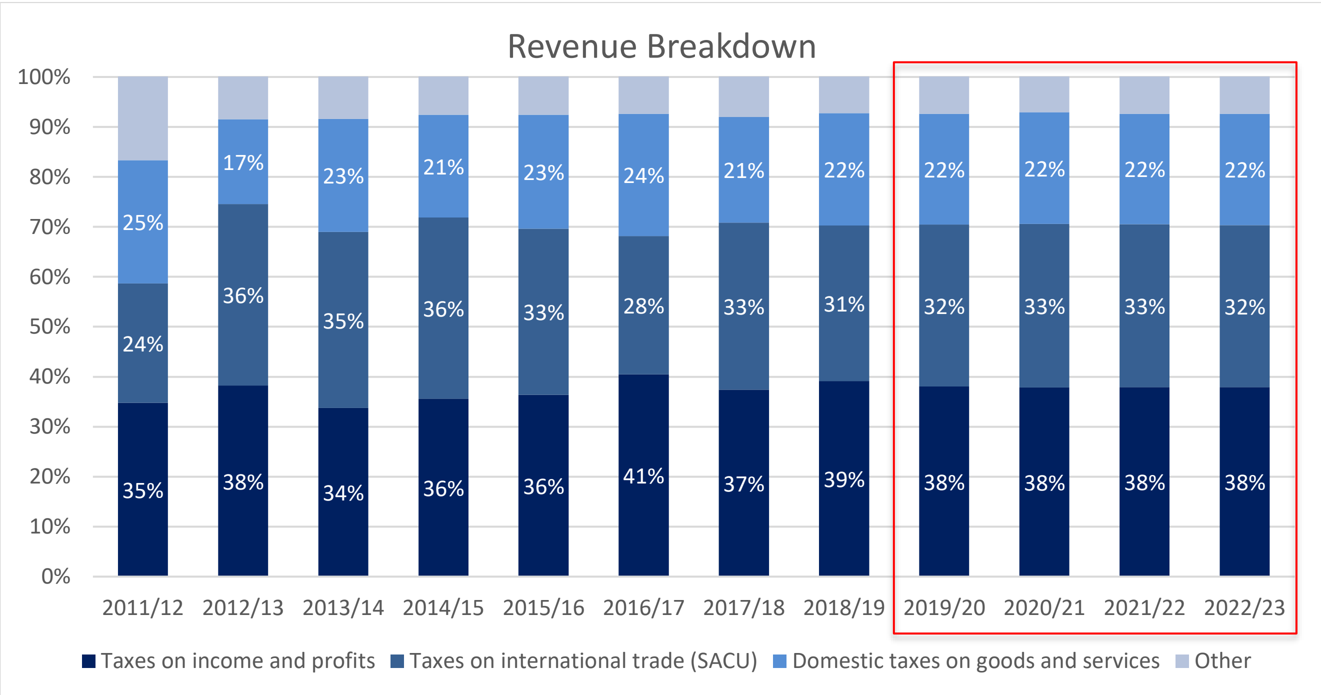
The ministry expects income taxes on companies and individuals to be more or less in line with the March budget, as it anticipates that economic activity will remain subdued. It is in light of this that the ministry expects value-added tax revenue to be N$500m lower than forecasted, but that this decline will be somewhat offset by an upward revision of N$350m in fuel levies. The ministry further anticipates that dividends and profit share from state-owned enterprises in 2019/20 will be about halve the N$711m expected in March.

The expected growth in income and company tax revenues is concerning from a budgeting perspective given the downward revisions to GDP growth in the budget documents themselves. It is possible that nominal growth may be seen despite real contractions in economic activity, but from a planning perspective it seems ambitious to plan for the expected or positive outcome rather than the worst case scenario.



Source: MoF, IJG Securities

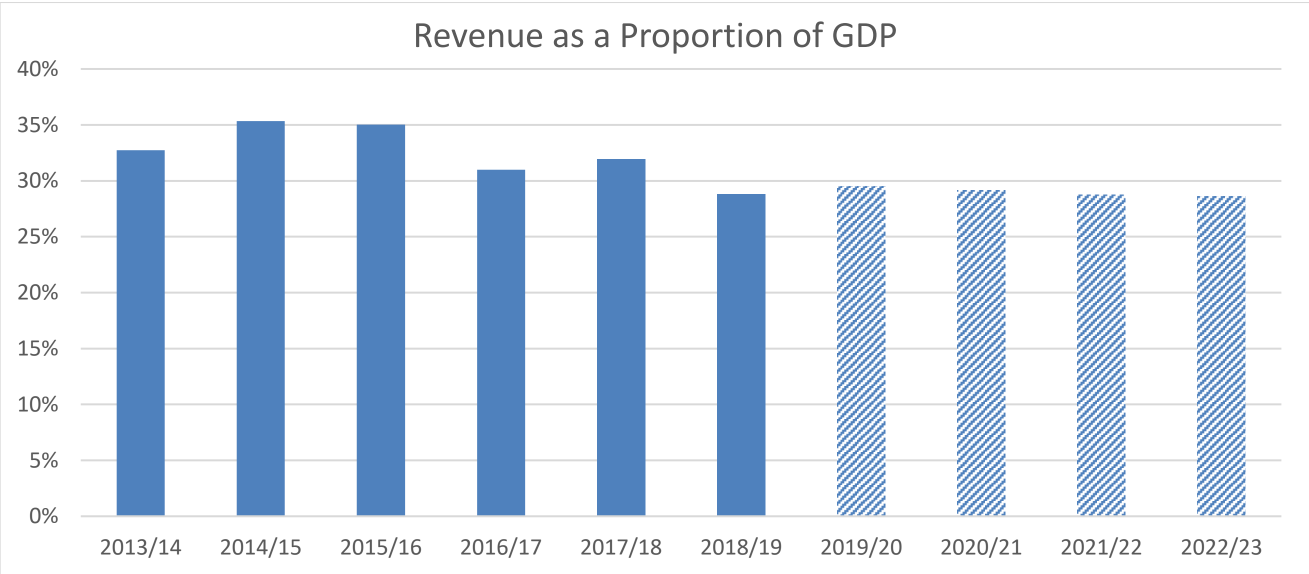
SACU revenues for the coming fiscal year are expected to be in-line with the March forecast of N$18.92bn, increasing by 8.9% from the N$17.38bn received in 2018/19. According to the ministry, SACU receipts have rebounded, and are expected to increase at an average growth rate of about 4.5% over the MTEF. Namibia has to repay N$2.51bn over 2019/20 against its nominal share of N$21.43bn, as the Common Revenue Pool was overpaid by N$9.31bn in an earlier year. However, this has been budgeted for already and thus does not constitute a surprise shock to revenues. SACU revenues make up about 32% of government revenue. An over reliance on this revenue stream is however unwise as it tends to fluctuate and is dependent on the economic performance of the SACU members, making it more difficult to forecast future revenue. Given that Namibia, Botswana and South Africa are not posting strong growth at present, there is a likelihood that SACU revenue projections may be unreliable.



Source: MoF, IJG Securities

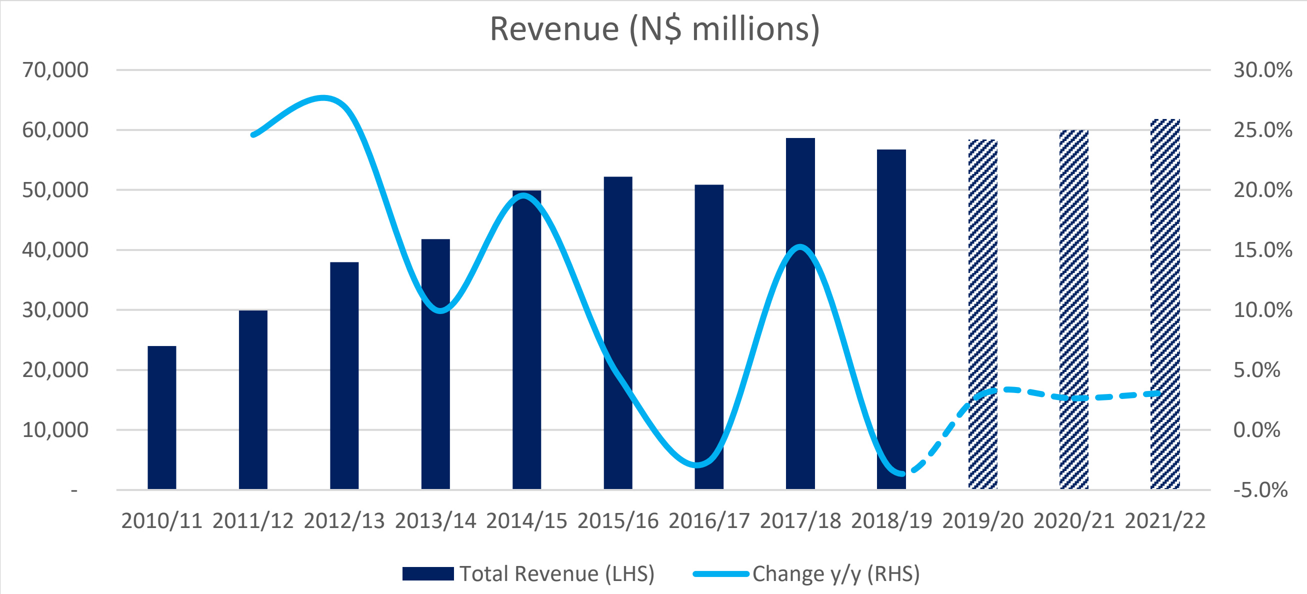
Taxes on income and profits make up 38.0% of the total estimate revenue and is expected to increase by a mere 1.7% in 2019/20 to N$22.22bn. This estimate represents a small upward revision from the forecast of N$21.8bn at March. Most of this increase will come from withholding taxes which has been revised up by N$260m. This will come from the planned implementation of withholding taxes on dividends declared. Income tax on individuals has also been revised up slightly from the March estimate of N$13.57bn to N$13.62bn. The ministry expects income tax on individuals to grow at a decelerating pace during 2019/20 and 2020/21 as a result of “sticky wages and limited job growth” in the struggling economy.

Forecasts for domestic taxes on goods and services (largely VAT collections) have been left unchanged from the figures in the March budget. Despite a downward revision of N$500m (or 4.0%) in VAT, the ministry anticipates the decrease to be offset by an increase in fuel levies of N$350m and the introduction of the plastic levy contributing N$140m.



Source: MoF, IJG Securities

Revenue as a proportion of GDP is set to increase from 28.9% in 2018/19 to 29.5% in 2019/20, but thereafter decline to 29.2% in 2020/21 and 28.8% as revenue growth is estimated to remain muted, whereas nominal GDP is expected to grow at a faster rate. The ministry estimates SACU revenue to hover around 9.4% of nominal GDP over the MTEF.



Source: MoF, IJG Securities

MTEF Revenue Estimates

The outlook for revenue growth remains rather poor. Revenue collection is expected to grow by an average of 3.1% over the 2020/21 to 2022/23 period. Total revenue is predicted to increase from N$58.41bn in 2019/20 to N$60.00bn in 2020/21 and 61.82bn in 2021/22.

SACU revenues are expected to be relatively flat over the MTEF, albeit still on average 26.2% higher than the actual N$17.4bn received in 2018/19. Most of the growth in revenue is estimated to come from taxes on income and profits, which will mostly stem from increased revenue from income tax on individuals and company taxes, especially in the outer years of the MTEF. The ministry correctly admits that the main risks to the revenue outlook comes from domestic macroeconomic risks, possible shocks in SACU revenue and external shocks from the global economy.

Tax Policy and Tax Administration Reforms

According to the Minister's speech: "it is not the policy intention for general tax rate increases. Such relief would encourage economic agents to produce and invest." Although the general tax rates will remain unchanged, it is unclear exactly where the relief part lies. A number of tax policy amendments were announced in the March budget will be tabled in the 2019/20 financial year. The budget did not bring any surprises as most of these proposals have been previously announced, which included:

- A 10% resident dividend withholding tax;
- The elimination of the conduit principle for trusts;
- The phasing out of Export Processing Zones and its replacement with Special Economic Zones;
- The taxing of commercial activities by charitable, religious, educational and other types of institutions under Section 16 of the Income Tax Act;
- Introduction of VAT on asset managers;
- Removal of zero-rating of sugar;
- Export levies coverage will be expanded to include agricultural, forestry and game products and mining products that are currently not covered;
- Conducting a study to identify the revenue potential of a 37% profit tax on betting and gaming entities; and
- Increase in the tax deductibility of retirement fund contributions from N$40,000 per annum to 27.5% of income with a maximum of N$100,000.

Save for the changes in retirement fund contributions deductibility, most of these changes aim to raise new taxes or broaden the net for tax collections. The minister previously pointed out that these changes should generate roughly N$400m in increased revenue. We have discussed most of these changes in our 2019 Budget Review. A new development was the mention of investigating a lower tax regime for small businesses, although no further details were provided but this could be a very positive development.

From the tax administration side, the implementation of the new Integrated Tax Administration System (ITAS), has largely been a success, despite a few teething problems. The implementation and promotion of e-filling system will continue. Additionally, the establishment of the autonomous revenue agency has been postposed again, this time for implementation on the 1st of April 2020.

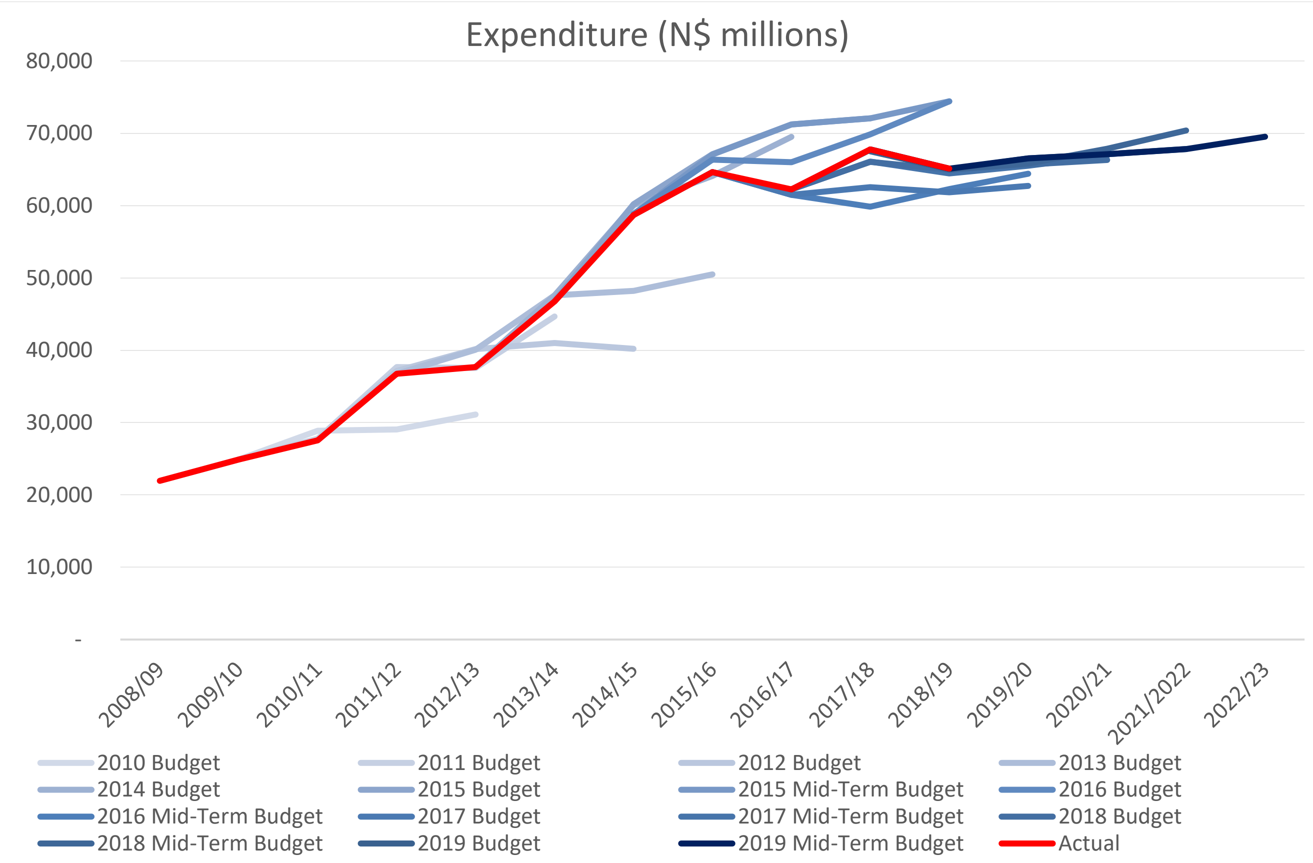
Expenditure

2018/19 Outturn

Expenditure for 2018/19 came in at N$65.11bn, in-line with the March budget figure of N$65.02bn. Fiscal expenditure as a percentage of GDP was 33.6%, down from 42.8% in 2015/16. While this is a marked improvement we still believe that government plays too large of a role in the economy even at these reduced levels. Government expenditure-to-GDP is still among the highest in the world and outcomes do not reflect this in our view. The operational budget implementation rate for 2018/19 was 99.5% according to the ministry of finance statement, while the development budget execution rate stood at 94.8%.

The ministry of finance says that personnel expenditure was the main driver behind the expenditure increase during the budget year and that personnel expenditure made up 45.3% of total expenditure. Development expenditure accounted for only 7.8% of total expenditure in 2018/19. The high public sector wage bill has plagued government since the start of the fiscal consolidation exercise and remains the most difficult expenditure line to bring under control.

2019/20 Budget Review and Mid-Year Outturn



Source: MoF, IJG

Mid-year expenditure amounted to 46.0% of total budgeted expenditure for 2019/20, reflecting a lower execution rate than in the 2018/19 budget year. It seems as though development expenditure made up only 6.8% of what was spent during the first half of the 2019/20 year despite the additional allocations to the development budget announced in the April budget statement. This is however not very clear in the budget documents.

MTEF Expenditure Growth	
2019/20	2.2%
2020/21	0.9%
2021/22	1.0%
2022/23	2.5%

The expenditure ceiling for 2019/20 of N$66.55bn remains in place in this mid-term update. This is a 2.2% increase from 2018/19 and 1.8% down from 2017/18. Over the outer years of the MTEF expenditure is set to grow very modestly as indicated in the adjacent table.

The ministry of finance recognizes that fiscal stimulus is necessary but that expenditure increases at time when revenue growth is subdued are not sustainable. The ministry states that its focus is on the "implementation of growth-enhancing public spending stimulus to support economic recovery and job creation within the fiscal consolidation program". The challenge with this is that close to 50% of expenditure is related to civil service wages which are unlike to be adjusted down or reduced through job cuts. Add to this the 10% of expenditure tied up in growing interest costs and it leaves very little room within which to stimulate growth as the funds need to come from other allocated areas of the budget. Thus, without growing the expenditure ceiling stimulus will be extremely limited as funds can only be reallocated within the determined ceilings.

In this regard the ministry has announced reallocations in this mid-term review. Despite the mid-term review being a course correction tool and not one in which additional expenditure is allocated, government offices, ministries and associations (OMAs) applied for N$8.08bn in additional expenditure for 2019/20, of which around N$400m seem to be requests for vehicles. The largest of these requests were as follows:

Vote	N$
Transport	1,431,301,409
Education, Arts and Culture	1,400,196,054
Health & Social Services	1,010,209,594
Defence	830,779,000
Agriculture, Water and Forestry	595,423,463
Finance	380,471,129
Poverty Eradication and Social Welfare	359,220,402
Veterans Affairs	307,609,693

Despite the mid-term budget not intended to be used to increase expenditure allocations, an amount of N$1.18bn was made available to "cater for critical expenditure items that experience budget shortfalls", significantly less than requested. These funds were however sourced from within the budget ceiling, thus constituting a reallocation rather than an increase in expenditure. The ministry notes that funds would be sourced from savings in operational expenditure as well as from development budget projects effectively deemed to be less urgent.

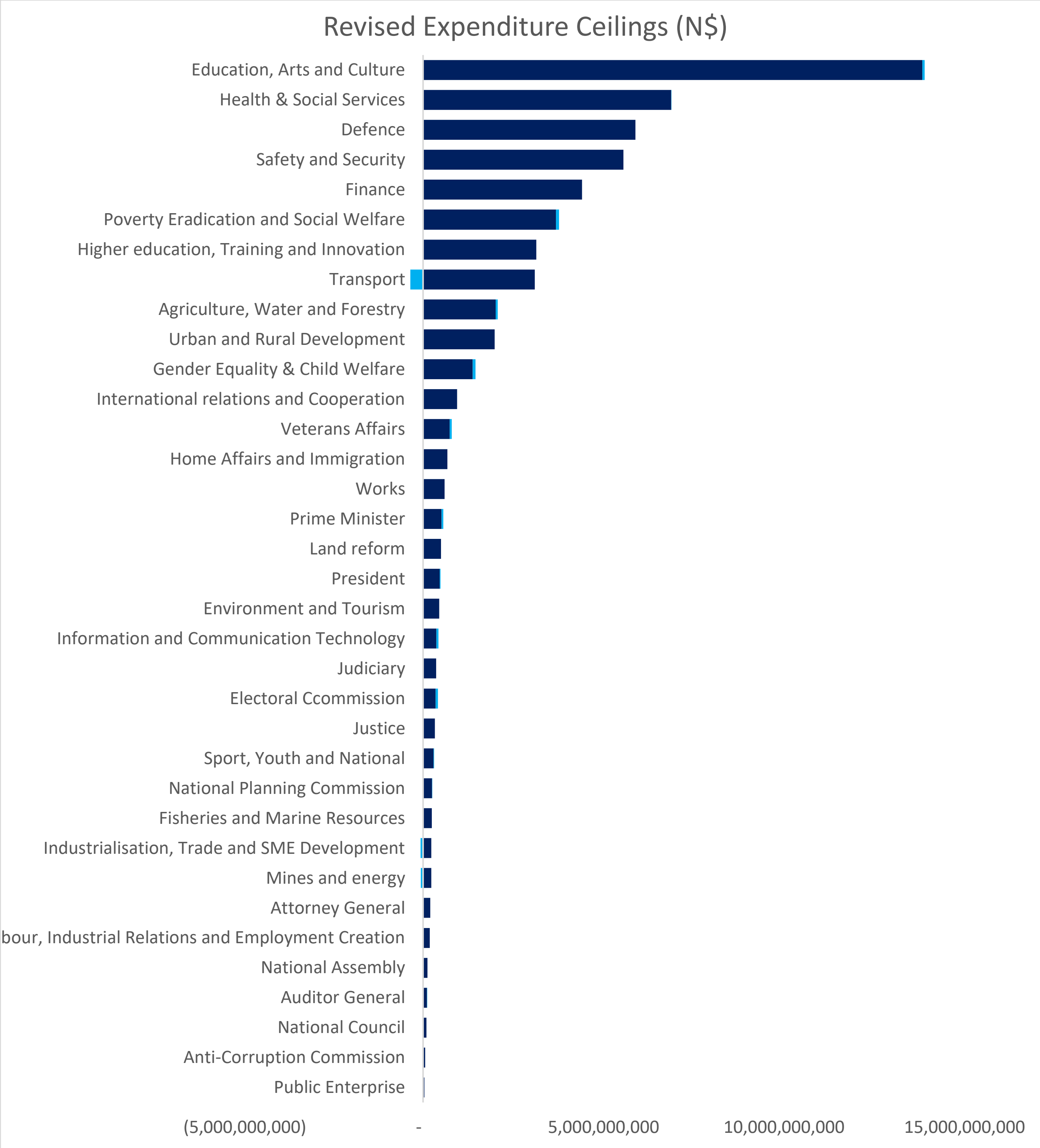
Of the N$1.18bn reallocation a total of N$176.7m was sourced from operational budget savings resulting from non-filling of vacancies. We view this as a very positive first stem in slowing the growth in the wage bill. The remaining N$1.0bn to be reallocated was sourced from the development budget. The funds were sourced from projects which have yet to start or where execution has been poor to date. Transport loses N$347.6m, health and social services loses N$206.2m, and education, arts and culture loses N$122.1m from their respective development budgets. A complete list of changes to allocations follows on the next page.

Vote	*Original Appropriation*	*Revised Ceilings*	*Change*
Poverty Eradication and Social Welfare	3,592,653,000	3,679,149,000	86,496,000
Gender Equality & Child Welfare	1,296,314,000	1,375,933,000	79,619,000
Education, Arts and Culture	13,767,697,000	13,829,663,000	61,966,000
Electoral Commission	288,358,000	350,161,000	61,803,000
Agriculture, Water and Forestry	1,959,307,000	2,014,517,000	55,210,000
Veterans Affairs	685,060,000	739,142,000	54,082,000
Information and Communication Technology	321,148,000	372,554,000	51,406,000
Prime Minister	459,391,000	508,799,000	49,408,000
President	435,369,000	458,859,000	23,490,000
Sport, Youth and National	285,999,000	294,091,000	8,092,000
National Planning Commission	241,584,000	248,084,000	6,500,000
Health & Social Services	6,868,271,000	6,872,753,000	4,482,000
Auditor General	109,265,000	109,582,000	317,000
Safety and Security	5,550,941,000	5,550,941,000	-
International relations and Cooperation	941,274,000	941,274,000	-
Urban and Rural Development	1,982,234,000	1,982,234,000	-
Land reform	496,792,000	496,792,000	-
Higher education, Training and Innovation	3,137,381,000	3,137,381,000	-
Home Affairs and Immigration	677,129,000	676,494,000	(635,000)
Justice	326,952,000	325,998,000	(954,000)
Public Enterprise	40,022,000	38,985,000	(1,037,000)
Attorney General	204,031,000	202,851,000	(1,180,000)
Anti-Corruption Commission	61,610,000	60,320,000	(1,290,000)
Defence	5,884,817,000	5,883,184,000	(1,633,000)
Labour, Industrial Relations and Employment Creation	189,924,000	188,188,000	(1,736,000)
National Council	94,763,000	92,481,000	(2,282,000)
National Assembly	126,848,000	123,516,000	(3,332,000)
Finance	4,409,320,000	4,401,667,000	(7,653,000)
Judiciary	368,444,000	360,191,000	(8,253,000)
Works	606,060,000	597,196,000	(8,864,000)
Fisheries and Marine Resources	250,214,000	239,992,000	(10,222,000)
Environment and Tourism	461,731,000	447,155,000	(14,576,000)
Mines and energy	286,165,000	225,164,000	(61,001,000)
Industrialisation, Trade and SME Development	295,026,000	226,681,000	(68,345,000)
Transport	3,443,437,000	3,093,541,000	(349,896,000)

Source: MoF

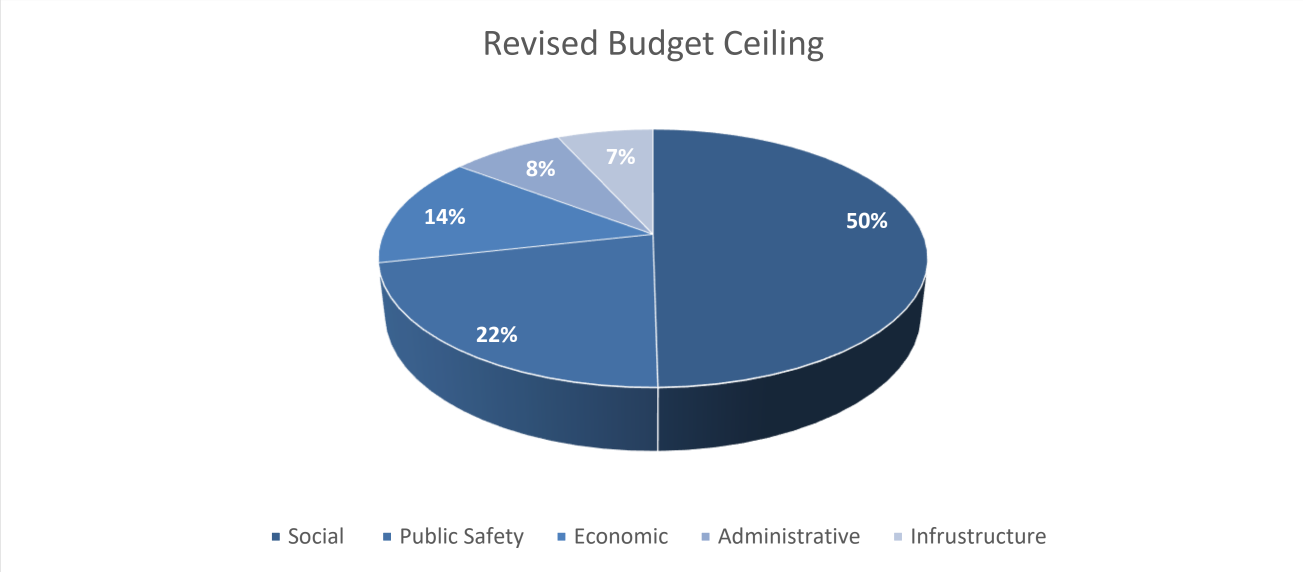
The fact that the changes mentioned in the previous paragraph to the development budgets of votes such as education, arts and culture are not visible in the above table tells us that funds have effectively been shifted to the operational budgets of some votes. This is concerning from a high-level perspective as development budget expenditure has higher multiplier effects in the economy in general. Some reallocations are easily justifiable such as those to support Namibians in need of food aid due to drought or other support systems for the poor. But much of the funds will flow to inefficient operational expenditure. The electoral commission, office of the president, office of the prime minister, and veteran's affairs all see reasonably large increases in allocations which seem to be election related. These funds are flowing into subsistence and travel allowances, transport (vehicles) and subnational bodies (regional and local government). Many of these reallocations are also poorly classified onto "other" categories.

It is concerning to note that despite the stated focus on channeling expenditure toward growth inducing activities, without neglecting social services, reallocations seem to, at least partially, contradict this explicit goal.



Source: MoF, IJG

Expenditure is still heavily skewed towards the social sectors as is appropriate in a country with high unemployment, low skills, little access to healthcare, and low per capita incomes. Reallocations are toward the social sector and administrative sector and away from infrastructure with transport the biggest loses in allocation in 2019/20.



Source: MoF, IJG

MTEF Expenditure Estimates

The ministry of finance has kept the 2020/21 expenditure ceiling unchanged from the April budget at N$67.13bn, down from N$67.85bn budgeted in last year's mid-tear review. Expenditure is set to grow to N$67.83bn in 2021/22 and N$69.52bn in 2022/23. This is in stark contrast to the 2016/17 forecast to exceed N$74bn by 2018/19 and serves as a reminder of how much the budgeting process has improved over the last three years. The current mid-year review projections are very reasonable in comparison to those of 2016/17 and before.

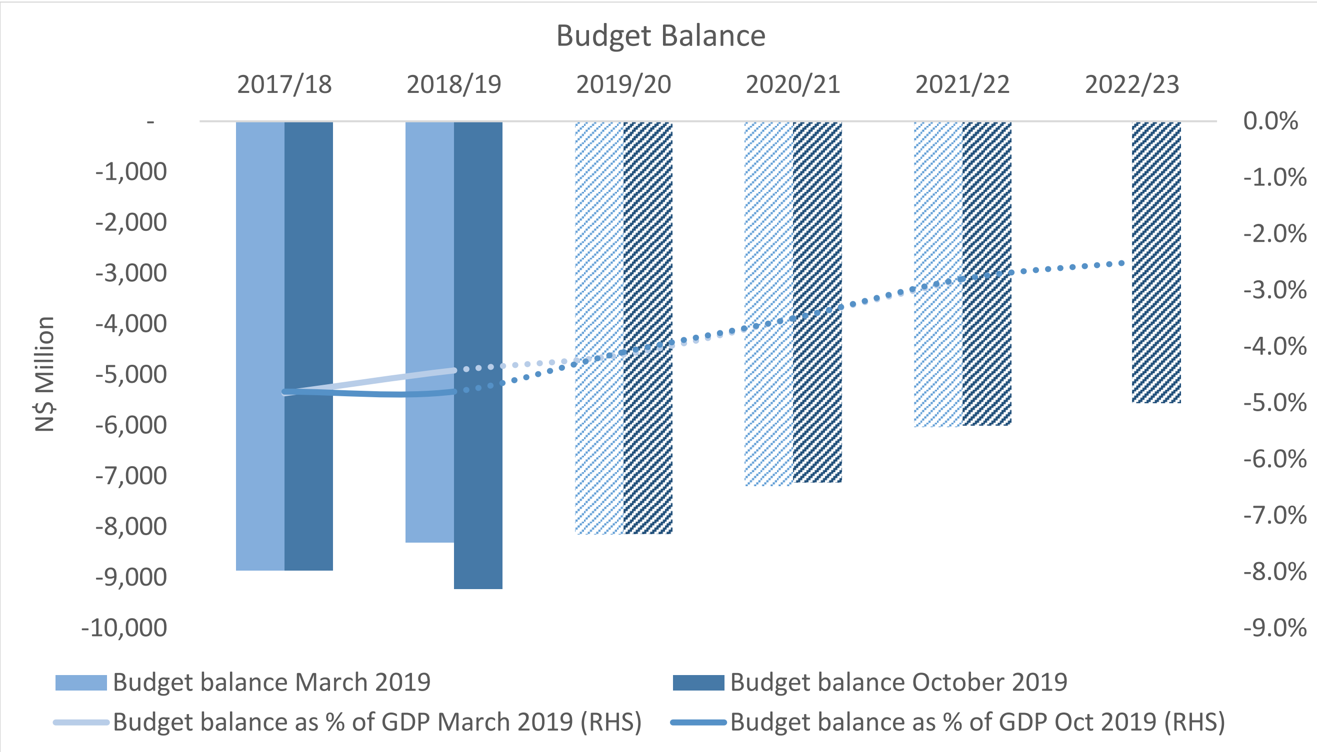
We anticipate difficulty in maintaining low growth in expenditure ceilings over the MTEF period due to the difficulty in reigning in the public sector wage bill and growth in finance costs. Inflationary increases to half the budgeted expenditure, the expenditure on the wage bill, will already exceed the overall growth projections noted in the budget statement and above paragraph. To this needs to be added an upward adjustment to interest costs which are projected to benefit from decreasing interest rates. Just these two adjustments alone would make it necessary to borrow more from the development budget or save more from the operational budget in order to not exceed the stated expenditure ceilings.

Budget Balance and Financing

2018/19 Outturn

Since the start of fiscal consolidation introduced in 2016/17 some headway has been made in reigning in the budget deficit. Since its implementation the budget deficit as a percentage of GDP declined from 6.7% in 2016/17 to 4.8% in 2017/18, but this decline slowed in 2018/19 as the recession in Namibia continued to drag on.

Total revenue for 2018/19 stood at N$55.88bn, a decrease of 1.4% or N$822m from the revised figure of N$56.7bn in 2017/18. The decrease in tax revenue is attributed to a decline in SACU receipts, company taxes and a large decrease in VAT. This was while total expenditure for 2018/19 amounted to N$65.11bn, about N$90m more than the revised figure. As a result, the 2018/19 budget balance amounted to N$9.23bn and was roughly N$912m larger than initially budgeted for. This represented an increase in the budget deficit from an initial expectation of 4.4% to 4.8% as a proportion of GDP. This also meant that the budget deficit was unchanged as a proportion of GDP from 2017/18. The 2018/19 deficit was funded mainly through the issuance of domestic debt stock which increased by N$6.7bn over the year.



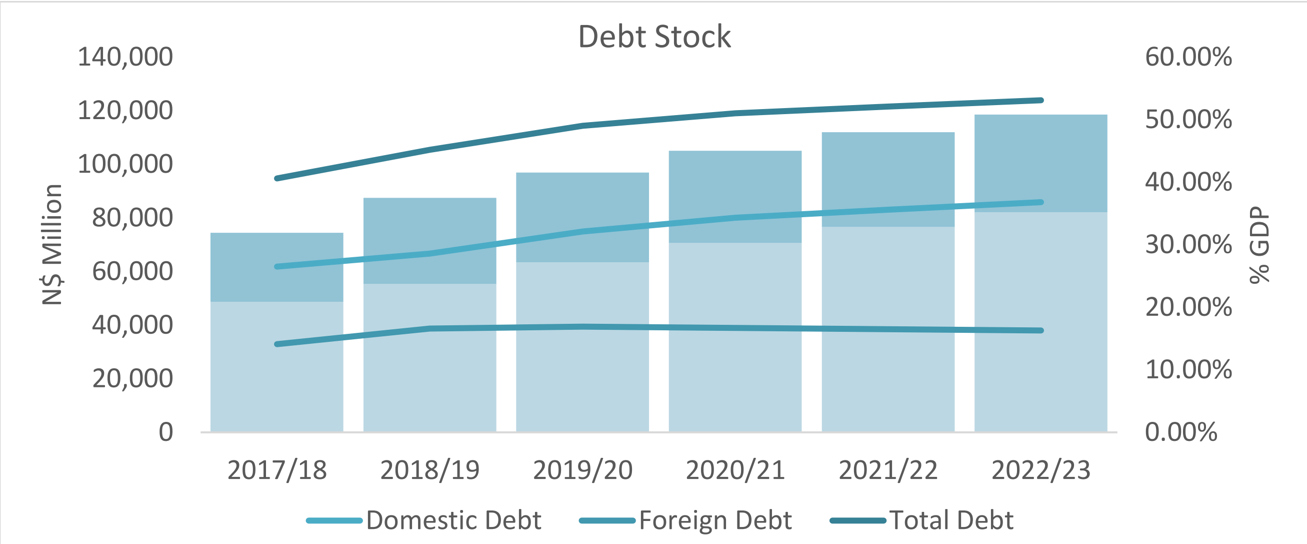
Source: MoF, IJG

2019/20 Budget Review and Mid-Year Outturn

The revisions to the total amount of revenue and expenditure over the MTEF to the budget presented in March were almost negligible, and as a result the trajectory of the deficit is expected to remain largely unchanged. That is for deficits to decline in the future. This is very much in line with the goal of fiscal consolidation, which aims to stabilise the ballooning stock of government debt. The budget deficit is forecast to contract over the following four years to N$8.1bn in 2019/20, N$7.1bn in 2020/21, N$6.0bn in 2021/22 and N$5.6bn in 2022/23. This is a steady decline from the current 4.8% budget deficit to 2.5% over the course of the next four years.

Despite the fact that the budget deficit is expected to contract, the annual additions to the debt stock remain sizeable. Most of the deficit funding will be raised in the domestic market as the medium term borrowing strategy aims to rebalance the split of domestic to foreign debt to 70:30, from the current split of 63:37. Local debt issuance is expected to amount to N$8.1bn in 2019/20, N$7.1bn in 2020/21 N$6.0bn in 2021/22 and N$5.6bn in 2022/23.

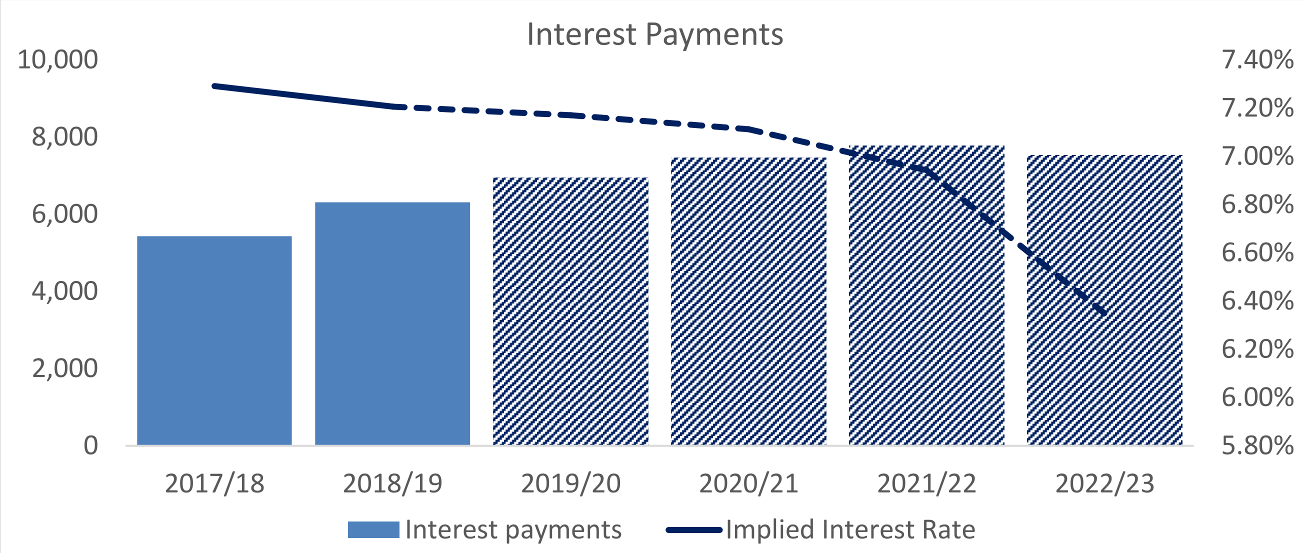
Raising this amount of debt in the local market will be difficult, but has been done before. A large amount of the demand in the last year was driven by changes in domestic asset requirements of Regulation 13 requiring 45% of regulated assets such as pension funds to be invested domestically. This persistent demand will likely not continue indefinitely, seeing as most portfolios should now be at or close to this allocation to domestic assets and options in terms of local assets should increase over the next year. We have already witnessed slightly lower demand for government bonds in recent auctions. To compound this funding problem, it has been proposed to increase the threshold for unlisted investments in phases up to 10%.



Source: MoF, IJG

The budget documents have indicated that large infrastructure development will be funded largely by concessional loans with reasonable terms and conditions from external lenders. targeted project financing will be increased by about N$2.5bn to finance water infrastructure projects. Additionally, an amount of N$2.2bn have been earmarked for projects over the next three financial years, which include road and rail infrastructure and Agriculture Mechanization, this will be funded mainly through the African Development Bank facility.

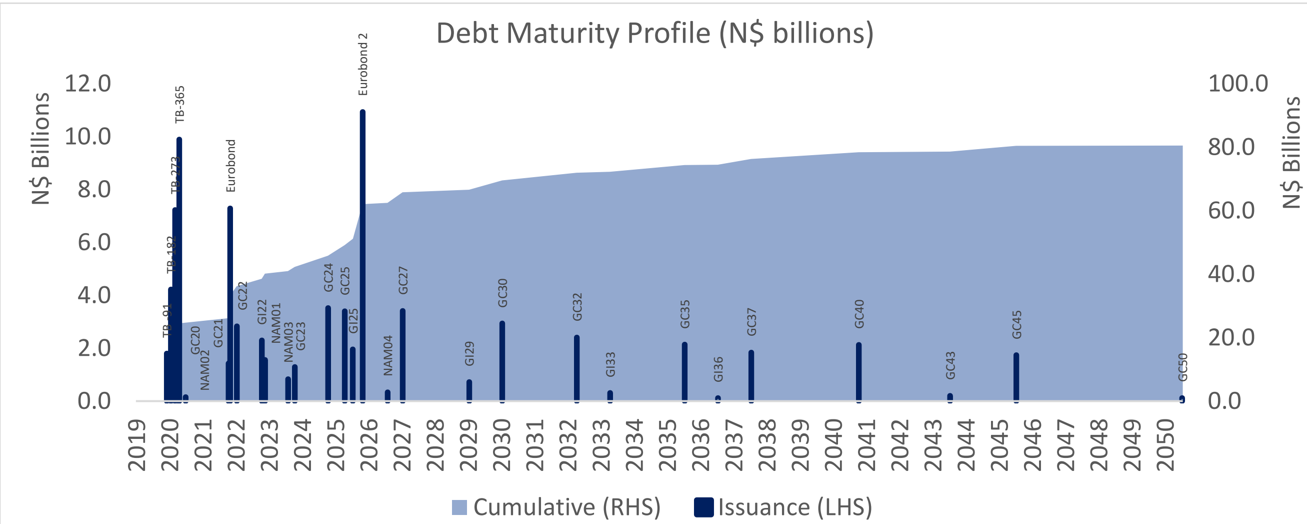
Interest payments are set to increase to N$7.0bn in 2019/20, or 11.3% of total revenue. These costs are expected to rise steadily to N$7.8bn or 12.6% of total revenue by 2021/22. This is well above the benchmark of 10%. Oddly, despite Namibia being downgraded and our debt to GDP ratio steadily declining, our implied interest costs (interest rates) are somehow expected to decrease over the next four years, which is largely to thank for the declining trend in the forecast interest payment to revenue ratio and budget deficits.



Source: MoF, IJG

Given the low levels of nominal GDP growth combined expected over the next three four years with a continued uptake of debt, debt-to-GDP is set to increase to 49.0% in 2019/20 and surpass the 50% mark in 2020/21, climbing steadily to 53.1% in 2022/23.

On a positive note, there are no expected increases in the amount of expected government guarantees, which are projected to decline to 5.0% of GDP from 5.6% currently. This is specifically due to a moratorium placed on government guarantees to state owned enterprises. These contingent liabilities can place a large amount of stress on a sovereign should they ever be called upon. According to the budget documents: “new issuance of guarantee(s) are only expected on the ground (of) economic and commercial related projects under the PPP arrangement.”



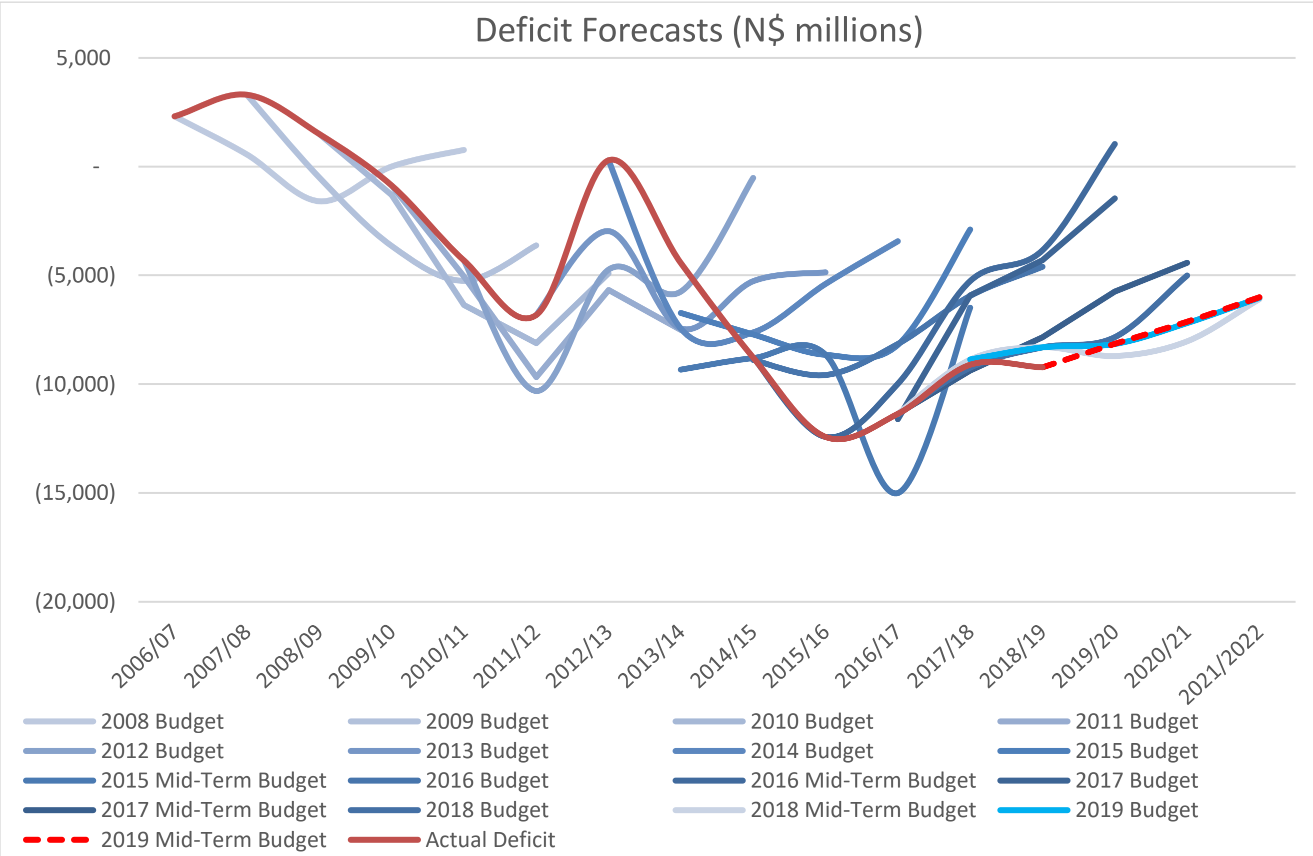
Source: BoN, IJG

The debt maturity profile remains worryingly steep. About 32.5% of all outstanding debt is redeemable in the next 12 months, while 49.8% matures in the next three years. As mentioned previously, the second Eurobond remains the largest single roll over risk. On the other hand, the switch auctions for the GC20 have been reasonably well subscribed and the GC21 switches will start in the second half of the financial year. These auctions have systematically been spreading the maturity profile more evenly over the maturity horizon reducing concentration risk, albeit a relatively slow process.

IJG Wrap and Outlook

Since the budget presented in March, Bank of Namibia have vised their outlook for 2019 to a 1.7% contraction in GDP and growth of only 0.8% in 2020. We also expect a continued slowdown in SACU activity and contractions in VAT and corporate income tax as both the regional and domestic economy shows little signs of growth in the medium term.

Given the fact that the macroeconomic outlook has deteriorated significantly, while company and personal income taxes have been revised up, we believe that there is a good chance that revenue may underperform expectations, as was the case in the 2018/19 fiscal year. We are concerned that expenditure is not aligned to realistic revenue forecasts. As a result, we will likely see slower than expected contractions in the budget deficit and a quicker deterioration in fiscal metrics such as debt-to-GDP and debt servicing costs relative to revenue.



Source: MoF, IJG

As the above figure indicates, the projected outer year deficits seldom come to pass. The actual deficit is historically almost always higher than projected by the ministry of finance. We believe that the accuracy of the budgeting process is vastly improved from periods prior to 2015 but the reasons noted above lead us to believe that deficits are unlikely to fall much below 4.0% to GDP in the medium term.

Revenue may or may not underperform as we suspect it will, but debt service costs will be larger than projected in the mid-year budget review tabled yesterday as interest rates on debt are not likely to drop as far as implied. In addition, growth in the wage bill and social safety nets are likely to exceed projected growth in the overall expenditure ceiling which will mean further reallocation of funds away from the development budget, constraining growth and the rollout of public infrastructure. These arguments form the basis of our view that deficit forecasts are likely underestimated which will lead to further fiscal deterioration over the medium term all else equal.

Of further concern is the deterioration in the global outlook with a projected global growth slowdown, ongoing trade tensions and growing fears of recession in the US and Europe. The risks of external shocks are mounting and could exacerbate the current troubles experienced in the Namibian economy. A global recession is likely to lead to more rapid fiscal deterioration domestically, leading to deeper recessions to come. Further fiscal deterioration will inhibit government's already constrained ability to drive economic growth further. This is not an unlikely scenario in our view and should form the basis for fiscal and policy planning.

It is clear that government spending is unable to provide the stimulus needed in order to reignite the Namibian economy at the present moment. Government may be able to maintain the current fiscal stability in the absence of external shocks, but returning to growth is likely to come from investment rather than government spending. We have been of the view for a number of years that a more investor friendly policy space needs to be created, or returned to, in order to attract the investment needed to stimulate growth. Indeed policy certainty has previously been a relative advantage that benefitted Namibia in the past.

In this regard we have seen signs of potential progress and the mid-term budget review has reiterated government's commitment to tabling the empowerment policy that has eroded much investor confidence over the last four years. This may be what is needed to bolster investor confidence. Further developments such as the possibility of lower taxes on small companies would add greatly to building domestic investor confidence. Improved governance of SOE's and possible creation of public private partnerships to run these entities are further positive signs that government is actively working on alternative means to stimulate economic growth and right size government's role in the economy.

We believe that this recognition of alternative means to improve facets of government and economic performance is a step in the right direction. Implementation is the next step and will be crucial if the Namibian economy is to be revived. Thus amidst a relatively gloomy outlook there are still levers that can be pulled in order to right the ship. They just require focused effort and cooperation between public and private sector to be successful.

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