

Namibia



key figures

• Land area, thousands of km ²	824
• Population, thousands (2006)	2 052
• GDP per capita, \$ PPP valuation (2006)	17 377
• Life expectancy (2006)	46.4
• Illiteracy rate (2006)	15

Namibia



Namibia

NAMIBIA HAS EXPERIENCED SEVERAL YEARS of moderate economic growth, due mainly to strong performance in diamond production and prudent macroeconomic policies. Growth averaged 4.5 per cent a year over the period 2000-05, and is expected to reach 4.8 per cent in 2006 and 2007 and 4.9 per cent in 2008. However, the Namibian economy is poorly diversified, relying heavily on extractive mining for export earnings and fiscal revenue, and is thus exposed to large and unpredictable fluctuations in commodity prices.

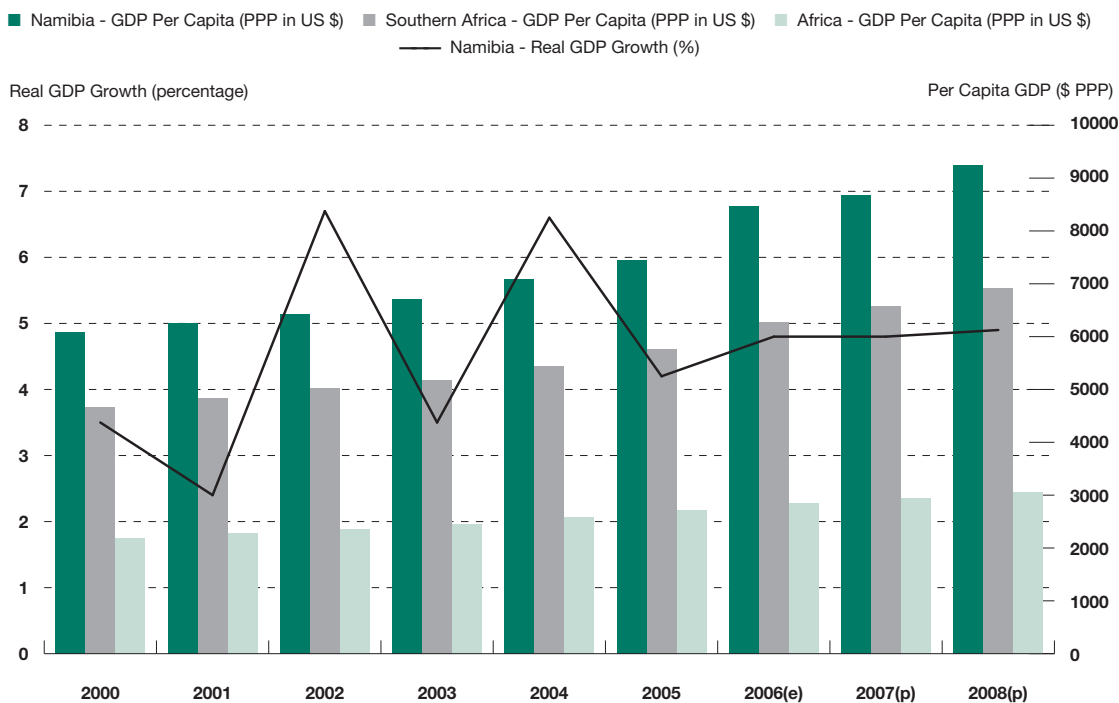
Although Namibia has the continent's fifth-highest per capita income and the eleventh-highest Human Development Index, it faces daunting social challenges, including high rates of rural poverty (of about 42 per cent), large income disparities (the Gini coefficient of 0.6 is among the worst in the world), and a serious

HIV/AIDS epidemic. HIV/AIDS prevalence averages 19.7 per cent (2004) and has contributed to reducing life expectancy at birth from 53.9 years in 1970-75 to 48.6 years in 2000-05.

The most damaging structural impact of apartheid in Namibia was to exclude the majority of the people from the productive economy, and this has stifled entrepreneurship and professional development among the black population. Affirmative action and Black Economic Empowerment (BEE) programmes have been implemented in an attempt to kick-start a process of accelerated transformation by providing previously disadvantaged

Alongside a stable and open political and economic environment exist high rates of rural poverty, large income disparities, and a serious HIV/AIDS epidemic.

Figure 1 - Real GDP Growth and Per Capita GDP
(\$ PPP at current prices)



Source: IMF and Central Bureau of Statistics data; estimates (e) and projections (p) based on authors' calculations.

<http://dx.doi.org/10.1787/741302441458>

groups with the opportunities necessary for them to participate in the country's economic development. Early indications, unfortunately, are disappointing. Also, it has been alleged that most opportunities – for instance in fishing concessions – have benefited only a small number of well-connected people. In the construction industry, where preferential procurement practices could potentially benefit black contractors, the superior competitiveness of Chinese companies is an additional constraint. This situation is exacerbated by skills shortages. Ten per cent of all positions are either occupied by people who lack the right skills or else remain unfilled, while the unemployment rate is 36.7 per cent (in the broad sense, according to the Labour Force Survey 2004). Despite the high share of expenditure on education, the quality of education is low.

The stable and open political environment, sound macroeconomic policies, and favourable growth momentum combine to create a window of opportunity for undertaking the structural reforms necessary to spread the benefits of growth more widely. This will certainly be necessary if recent and forecast short-term GDP growth rates are to be raised in line with the ambitious targets set in Namibia's *Vision 2030*.

Recent Economic Developments

Namibia's economy is small and closely linked to that of South Africa. GDP growth has exhibited considerable fluctuations, having averaged 3.1 per cent over 1998-2001, then accelerating to 5.6 per cent in 2002-04, and slowing to 4.6 per cent in 2005-06. Growth is forecast to average about 4.8 per cent and 4.9 per cent in 2007 and 2008, respectively. The recent acceleration of growth was made possible by increased global demand for minerals, reflected in high international prices for key export commodities such as diamonds, uranium, zinc, copper and gold. The economic structure has remained fairly stable over the past decade, with services contributing some 55 per cent

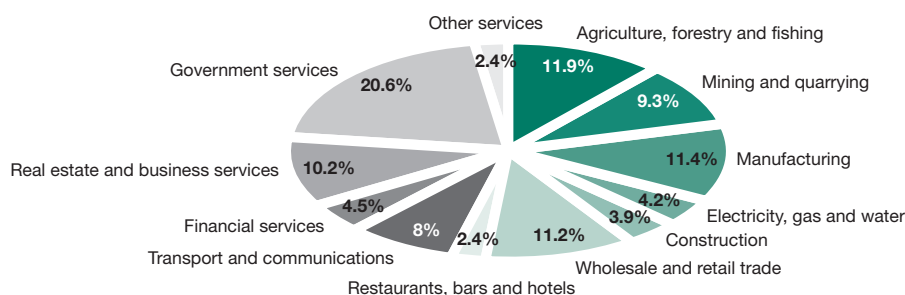
of value added. Business confidence is strong, as shown by the consecutive records reached by the IJG¹ Business Climate Index produced monthly by the Windhoek-based Institute for Public Policy Research (IPPR), which in September 2006 rose by 2.6 points to 139.5 points.

The mining industry accounts for some 9 per cent of GDP, and is dominated by diamond extraction, which accounts for roughly 8 per cent of GDP and has made Namibia the world's seventh-largest producer by value in 2005. Cutting and polishing of diamonds also contribute to economic activity. NamDeb, a 50/50 joint venture between the Government of the Republic of Namibia (GRN) and De Beers, is the largest diamond firm. Various non-diamond operations include: Ongopolo (which re-opened around 2000 under new management); Rosh Pinah; Skorpion (2003/04); and UraMine (2006), which started production recently. Rössing is expected to operate at full capacity in the next couple of years, while Langer Heinrich will start production soon; a third uranium deposit was also launched at the beginning of 2007. Petroleum exploration licenses were issued in August 2005 to BHP Billiton, Hunt Oil and Neptune.

Although the share of mining in GDP has declined from the 1990 high of 20 per cent, it still accounts for 45 per cent of foreign-exchange earnings and roughly a third of fixed capital formation. Expenditures on mineral exploration reached N\$477 million in 2005, its highest level in ten years and 50 per cent higher in real terms than in 1995. Nonetheless, direct employment has halved since independence (to 7 400 people), reflecting the switch from labour-intensive onshore diamond extraction to capital-intensive marine operations, which represented 52 per cent of 2005 production. Tax revenue from mining has been highly variable and difficult to forecast. While tax revenue from diamonds has never fallen below 6 per cent of total tax revenue and averages approximately 8 per cent of total revenue, non-diamond mining has only accounted for an annual average of 1 per cent of tax revenue over

1. IJG (Irwin, Jacobs, Greene) Securities (Pty) Ltd is one of Namibia's financial service providers.

Figure 2 - GDP by Sector in 2005 (percentage)



Source: Authors' estimates based on Central Bureau of Statistics data.

<http://dx.doi.org/10.1787/658621448877>

the past ten years. This mainly reflects a tax formula applied in 1992, whereby the higher the rate of profit, the higher the rate of tax. However, this formula was open to abuse, and it failed to deliver a significant amount of tax revenue to the treasury. Even after the introduction of a new flat tax rate in 2000, the non-diamond sector's contribution to fiscal revenues has remained relatively modest.

Diamond production rose by 50 per cent on a year-on-year basis in the third quarter of 2006, following an expansion of 28.1 per cent in the second quarter of the year. Although receipts for diamond exports declined between the first and second quarter of 2006, they have continued to represent the largest item in total merchandise export earnings, accounting for about 36 per cent. Offshore diamond production in 2006 is estimated to have reached a record one million carats, thanks to the use of advanced marine prospecting and mining technology, whereas the relative share of onshore production is declining. Overall, diamond production expanded to more than two million carats in 2006 for the first time and is forecast to increase further in 2007. NamDeb is promising ten million carats by 2010 and so new production records should be reached in the coming years. In January 2007, De Beers and the Government of Namibia also concluded negotiations started in November 2005 on the renewal of the five-year contract. Namibia succeeded in boosting its local cutting and polishing industry by increasing the share of NamDeb production destined for local sales; however, De Beers will maintain supply control over the so-called "specials", i.e. diamonds of 10.8 carats and bigger.

Manufacturing, which accounts for 11 per cent of GDP, recorded negative growth in 2005/06, owing to the poor performance of fish processing. Over the past few years, the authorities have been trying to develop the manufacturing sector. The opening of the Ramatex apparel factory in Windhoek in 2003 was expected to attract new international investments to the Export Processing Zones (EPZ). Namibia, however, has suffered from the phasing-out of the Multi-Fibre Agreement and the number of new jobs for Namibians in the textile industry has been far below expectations. Other large industrial firms, such as dairies, are also suffering from the high value of the currency and competition from South Africa and China.

The share of agriculture in GDP has fallen continually since independence, and currently hovers around 6.8 per cent. This sector is dominated by meat products such as beef, mutton and goat meat. Thanks to record rainfall experienced in 2005, agriculture grew by 10 per cent. Good rainfall continued in 2006, but nevertheless, a decline in the number of livestock marketed during the year resulted in a contraction of about 6 per cent in the first three-quarters of 2006. Farmers had to postpone the selling of some of their livestock for purposes of restocking after the good rainfall, despite high meat prices.

Despite almost unlimited farmland, the country's geological and climatic conditions make it difficult to generate enough income for the 1.2 million Namibians who rely on farming for their livelihood and who are mostly living in communal areas. Food demand exceeds

supply, with imports of staple food from South Africa and Zambia filling the gap. Poor marketing, the small size of the domestic market, and the inability to add processing value and penetrate foreign markets all act as additional constraints on agricultural development. Meat remains the major export product. Other export-oriented farming products have developed recently in the south, especially grapes, pearl millet/mahangu and horticultural products.

Fishing is also a strong contributor to GDP, accounting for about 5.6 per cent, but it exhibits a

strong cyclical pattern since it is influenced by weather conditions, energy prices, and the exchange rate. After two consecutive years of contraction, the sector recovered gradually in 2005/06, although a four-week closed season for hake was imposed in October 2006 for the first time, and a closed area was also introduced, prohibiting vessels from fishing in depths of less than 200 metres. These actions followed from surveys that revealed mixed results. Most fish caught in Namibia are exported to Spain, although efforts are now under way to find new export markets in Asia, especially for species such as abalone.

Table 1 - Demand Composition (percentage of GDP)

	1998	2005	2006(e)	2007(p)	2008(p)
	Percentage of GDP (current prices)		Percentage changes, volume		
Gross capital formation	25.8	25.6	7.3	5.5	8.7
Public	7.7	7.6	8.0	-5.0	5.0
Private	18.1	18.0	7.0	10.0	10.0
Consumption	87.3	81.1	4.2	0.0	3.1
Public	31.5	29.4	7.0	-1.3	5.0
Private	55.8	51.7	2.7	0.7	2.2
External sector	-13.1	-6.6			
Exports	45.0	35.1	7.5	10.0	6.2
Imports	-58.0	-41.8	7.4	1.8	5.1

Source: Central Bureau of Statistics data; estimates (e) and projections (p) based on authors' calculations.

<http://dx.doi.org/10.1787/488560331871>

Among services, tourism stands out in terms of contribution to export earnings, although the contribution of government services is much higher. Tourism (represented by hotels and restaurants) contributes 3.7 per cent of GDP and 4.7 per cent of total employment, although the indirect contribution (as recorded by the Tourism Satellite Accounts) is estimated to be equivalent to 16 per cent of GDP and 17.7 per cent of total employment. Tourism is estimated to have grown by 21 per cent in the first three-quarters of 2006, with visitor-arrival growth being positively affected by the worldwide publicity generated by the presence in the country of well-known Hollywood stars. The real estate market is also showing moderate growth, which, combined with new infrastructure investment, is providing support to the construction industry.

Growth in Namibia has been driven by exports and private investment in the mineral sector. In 2005, for the third year running, mining investment at N\$477 million outstripped government investment by a wide margin. Over the period 2006-08, other significant investments are expected to boost growth, including: the continuous introduction of new technologies for mining diamonds; the development of new uranium mines; and the development of the Kudu Gas Field and subsequent construction of the gas-fired power plant. In tandem with increased investment, imports of capital goods are expected to grow, although their increase will be more than offset by record diamond and uranium exports. After increasing substantially in 2006, government consumption and investments are expected to contract slightly in 2007, reflecting the tighter budgetary stance adopted in order to compensate

for the anticipated fall in international taxes (Southern African Customs Union revenue – SACU revenue). It is also expected that there will be little growth in private consumption, mainly due to the weak performance of traditional agriculture.

Macroeconomic Policies

Fiscal Policy

Vision 2030 is meant to define the national development strategy, which will then be translated into a series of five-year National Development Plans (NDPs). The Medium-Term Expenditure Framework (MTEF) sets the budgetary priorities for government spending and ought to be in line with the NDP. However, the coherence among these three documents is weak. The *Vision 2030* emphasises industrial development; while the NDP focuses more on pro-poor growth. The MTEF is based on three pillars: *a)* consolidating macroeconomic stability through prudent fiscal policies and maintaining a credible peg to the South African rand; *b)* promoting pro-poor growth by stimulating consumption and promoting industrial diversification; and *c)* further combating poverty by injecting substantial resources into health and education, as well as by grant-based transfers (such as non-contributory social pensions).

On balance, the government has pursued a prudent fiscal policy, reducing the deficit from 7.5 per cent of GDP in 2003/04 and 3.6 per cent of GDP in 2004/05, to 1.1 per cent in 2005/06. This improvement was due to cuts in government recurrent expenditures on goods and services, a drop in capital expenditure and efforts to increase revenue collection and broaden the tax base. In 2006/07, the budget is expected to exhibit a surplus, of 2.2 per cent of GDP, for the first time since independence. Nevertheless, a closer look shows that the improvement was due more to higher revenue than to continued expenditure restraint. An unexpected windfall of SACU receipts, which accounted for 40 per cent of total revenue and grants, offset the growth in the public-sector wage bill which reflects the continuous growth in government personnel. Namibia's growing pool of civil servants makes up 4.3 per cent of the population and their salaries represent more than 40 per cent of total expenditures and account for more than 14 per cent of GDP, which is well above the average of African countries. An additional boost to the government's revenue came from receipts (N\$648 million) from the partial privatisation of the mobile phone company, Mobile Telecommunications (MTC).

The volatility associated with SACU receipts means that the government needs to diversify its sources of revenue and undertake substantial efforts to improve sustainable revenue collection. The government also

Table 2 - Public Finances (percentage of GDP)

	1998	2003	2004	2005	2006(e)	2007(p)	2008(p)
Total revenue and grants^a	36.0	28.2	30.6	30.0	36.4	30.4	29.8
Tax revenue	31.9	25.0	28.0	27.6	32.6	26.7	26.1
Grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total expenditure and net lending^a	40.1	35.7	34.2	31.1	34.2	32.7	32.1
Current expenditure	35.1	30.0	28.9	27.2	29.1	27.9	27.7
<i>Excluding interest</i>	32.5	27.5	26.3	24.5	26.2	24.9	24.7
Wages and salaries	18.4	14.8	14.8	13.5	14.6	14.1	13.9
Interest	2.6	2.5	2.7	2.7	2.9	3.0	3.0
Capital expenditure	4.8	4.5	4.5	3.9	4.1	3.8	3.8
Primary balance	-1.4	-5.0	-0.9	1.6	5.1	0.7	0.6
Overall balance	-4.0	-7.5	-3.6	-1.1	2.2	-2.2	-2.3

a. Only major items are reported

Source: Ministry of Finance data; estimates (e) and projections (p) based on authors' calculations.

<http://dx.doi.org/10.1787/370835576322>

needs to re-orient spending away from wages and subsidies towards priority sectors, namely, health, education and infrastructure. To this end, in the 2006 Article IV consultation the IMF recommended that the authorities enhance tax administration and revise the structure, quality and remuneration of the civil service.

In the MTEF for 2006/07-2008/09, the government has introduced a number of reforms to strengthen tax administration and improve revenue collection, including a system of rewards and penalties for line ministries to encourage them to make greater efforts to collect revenues for the services they deliver. Another important measure includes the clamping-down on tax evaders through targeted forensic audits. On the expenditure side, the authorities have put in place an Integrated Financial Management System which will improve the management of all the transactions between the Ministry of Finance and line ministries.

Regarding sectoral allocations, education will receive about 26 per cent of the total operational budget for the MTEF period, of which personnel expenses account for two-thirds and health will receive 10 per cent (in line with the target set by African Union – AU – Ministers of Health), constituting an increase of 23 per cent compared to the 2006/07 budget. Most of the funds will be channelled to improve antiretroviral treatment for victims of AIDS/HIV and to hire 105 expatriate nurses to work in Namibia in 2007 and 2008. Financial transactions which include transfers, such as social pensions, contributions to Medical Aid Funds and subsidies to loss-making State-Owned Enterprises (SOEs), will remain the second most-important spending category, accounting for 14 per cent of total budget. To reduce the SOEs' drain on the state budget, the government has undertaken to tighten the rules under which subsidies are disbursed. Defence will continue to receive substantial additional resources in the budget, with its overall allocation rising to 9 per cent of total spending, representing the fourth-largest category after education, finance and health.

Despite the government's efforts to improve revenue collection, reduce non-priority spending and contain wage growth, the 2007/08 and 2008/09 budgets are

projected to result in deficits of 2.2 per cent and 2.3 per cent, respectively. This is mainly explained by an expected fall in SACU receipts by more than 6 per cent of GDP.

The reduction of the fiscal deficit over the past few years has led to stabilisation of the public debt at about 33 per cent of GDP. The authorities have fixed an ambitious target of reducing the debt/GDP ratio from 33 per cent to 25 per cent by the end of the decade.

Monetary Policy

Namibia is a member of the Common Monetary Area (CMA), which also includes South Africa, Lesotho and Swaziland. Like other small CMA members, Namibia's monetary policy is determined by the peg to the South African rand. Each CMA member has its own Central Bank and maintains responsibility for foreign exchange transactions within the territories. A bilateral agreement with South Africa requires Namibia to fully back its currency with foreign exchange reserves. This peg also links Namibia to South Africa's inflation-targeting framework, requiring the two inflation rates to converge to the South African Reserve Bank range of 3 to 6 per cent.

Nevertheless, since mid-2005, inflation has been rising. The annual rate for December 2006 was about 6.1 per cent, the highest not only for the year, but since August 2003 (6.7 per cent) compared to a low rate of 0.9 per cent in May 2005. The increase is mainly due to increases in transport prices until the end of the second quarter (reflecting high international crude oil prices), food inflation, strong domestic demand and a weaker exchange rate. Imports account for 80 per cent of the CPI (Consumer Price Index) basket. Mirroring development in the CPIX (Consumer Price Index excluding interest rates on mortgage bonds) of South Africa, which is the major source of Namibia's imports, inflation averaged 5.1 per cent for the year, compared to 2.2 per cent in 2005 and is expected to remain around this level in 2007 and 2008.

To counteract the build-up of inflationary pressures, the Monetary Policy Management Committee of the

Bank of Namibia increased the bank rate by 150 basis points, to 8.5 per cent, from June to October 2006. This tightening was in line with similar action taken by the South African Reserve Bank (SARB). Owing to continued inflationary pressure, the Bank of Namibia increased the Bank rate by another 50 basis points to 9 in December 2006, following an identical rise in the discount rate by the SARB. At this level, the intervention policy rate became the highest since October 2003, when the rate was 8.25 per cent.

As sentiment towards emerging markets deteriorated in May/June 2006, and as concerns mounted over South Africa's large current-account deficit, the currency depreciated by about 20 per cent, reaching a low of N\$7.91 to the US\$ in early October 2006. Softer prices for commodities such as gold and platinum have also helped to push the currency lower. Although a lower exchange rate means higher costs for imports from outside the CMA, it may improve the prospects for non-traditional exports and increase the profits of traditional exports. Towards the end of the year 2006, the currency appreciated again and hovered around N\$7.10 to the US\$ and N\$9.3 to the euro.

Namibia is characterised by a high private-savings rate, mainly reflecting pension contributions from public-sector employees. In fact, the assets of pension funds and insurance companies are equal to GDP. The overwhelming bulk of these funds have been channelled to South Africa's financial market due to the lack of investment opportunities in Namibia. In order to retain more of these funds in Namibia, the government is drafting an amendment to the Namibian Financial

Institutions Supervisory Authority Act which should encourage the development of investment vehicles offering investors the same returns as those expected outside the country.

External Position

About 80 per cent of total imports come from or through South Africa, which absorbs only 30 per cent of exports. The European Union (EU) represents the main export market, in particular the United Kingdom (diamonds) and Spain (as end and transit destinations for fish). Namibia is also actively taking advantage of the African Growth and Opportunity Act (AGOA), with several apparel manufacturers from Asia – actually forming one company with one or two subsidiaries (Ramatex) – which are investing in assembly facilities; at full production, these facilities are expected to generate annual exports of goods valued at over \$100 million. AGOA has created over 6 000 jobs and has led to investment in infrastructure, especially in support of the textile and garment industry. The United States also represents an important source of heavy equipment and machinery imports.

Economic Partnership Agreement (EPA) negotiations with Southern African Development Community (SADC) countries, including Angola, Botswana, Lesotho, Mozambique, Namibia, Swaziland and Tanzania, were opened in July 2004. Botswana was appointed to co-ordinate the overall efforts of the SADC EPA configuration and to prepare negotiating positions, while each SADC EPA member state has been assigned a negotiation issue or issues to co-ordinate.

Table 3 - **Current Account** (percentage of GDP)

	1998	2003	2004	2005	2006(e)	2007(p)	2008(p)
Trade balance	-8.4	-10.3	-5.0	-9.4	-7.3	-5.3	-4.4
Exports of goods (f.o.b.)	35.4	28.0	31.9	27.0	28.5	29.3	29.8
Imports of goods (f.o.b.)	43.8	38.3	36.8	36.4	35.8	34.6	34.2
Services	-4.6	3.8	2.4	2.7	2.3	2.4	2.2
Factor income	3.1	1.3	1.2	1.2	1.0	1.1	1.2
Current transfers	12.8	10.2	11.7	11.2	14.0	12.1	10.1
Current account balance	2.8	5.1	10.2	5.7	10.0	10.3	9.1

Source: IMF and Bank of Namibia data; estimates (e) and projections (p) based on authors' calculations.

<http://dx.doi.org/10.1787/707438272131>

Namibia is in charge of trade facilitation and development co-operation. In March 2006, the SADC EPA group presented this adopted framework document to the European Commission (EC), setting out the principles, objectives and key elements that define their new approach to the EPA negotiations.

The Southern African Customs Union (SACU) has recently engaged in a round of Free Trade Agreement (FTA) negotiations with other countries and regional blocs. Agreements concluded include those with the European Free Trade Association (EFTA) and the Southern Common Market (MERCOSUR); these now await incorporation into the national laws of the individual countries concerned. The SACU-United States FTA, however, has been put on hold due to disagreements over several issues, including “new issues” such as investment, government procurement and competition. This agreement will now be replaced by a less comprehensive version known as the Trade and Investment Co-operation Agreement (TICA). Agreements with India and China are imminent.

Namibia’s transactions with the rest of the world

are characterised by a small deficit in goods and a small surplus in services. Nevertheless, since 2006, booming exports in diamonds, gold, zinc and copper – reflecting higher international prices – have narrowed the trade deficit. In addition, a surge in SACU receipts has resulted in a strong improvement in the current-account surplus. The growth in mineral exports is expected to continue in 2007 and 2008, further improving the trade balance. The current account is also expected to benefit from increased tourism revenue and higher receipts from investment abroad.

Foreign direct investment (FDI) is heavily biased towards the mining sector, which attracted 65 per cent of major projects in the 2003-06 period. In manufacturing, most Asian FDI has been short-lived. Rhino Garments shut down in 2005, while Ramatex has used the threat of doing the same to win new concessions from the trade unions and the government (in particular in the area of environment controls). A revision of the investment legislation is currently under way, in order to define better the role of tax incentives – which, in the case of Ramatex, included

Figure 3 - **Stock of Total External Debt** (percentage of GDP) and **Debt Service** (percentage of exports of goods and services)



Source: IMF.

<http://dx.doi.org/10.1787/178643760831>

a reduced corporate rate and a VAT exemption for equipment purchase – and also to integrate trade, FDI and EPZ promotion. This process is proceeding in tandem with the discussion of the second Investor Roadmap that has identified the major hurdles to FDI in Namibia. The recently established Agricultural Trade Forum should also play a key role in raising awareness and attracting investment towards the production and export of products in which the country has a comparative advantage, such as cotton seed, hides, karakul pelts, raisins, beer, fish, cattle meat and wool.

Namibia's status as a middle-income country does not facilitate access to concessional finance. In fact, donors' support is declining. External grants through the budget dropped from 1.5 per cent of the revenue in 2005/06 to 0.6 per cent in 2006/07. Those funds are exclusively from the EU and are destined for rural water investments and rural roads. The Dutch and British development co-operation agencies ceased their operations in 2006. Interestingly, though, Namibia was deemed eligible for United States Millennium Challenge Account assistance in the 2006 and 2007 selection rounds, under the lower middle-income category. The country is expected to receive about \$450 million over the next five years to finance projects in the following areas: education, livestock, tourism, green scheme, indigenous natural products and roads. There are concerns in the donor community about the effective absorption capacity of such a significant flow of resources, and many fear that Millennium Challenge Account (MCA) aid could crowd out the activity of existing donors.

In December 2005 Fitch Ratings awarded Namibia an investment-grade rating of BBB- for long-term foreign-currency risk, F2 for short-term foreign-currency risk, and BBB for long-term domestic-currency risk, while the overall country rating was set at A-. This reflects an improvement in the perceived creditworthiness of the government, since prices at which government securities were previously traded indicated a far less favourable assessment of risk. Despite the possibilities of tapping international capital markets offered by the favourable sovereign credit rating, the

government will continue issuing bonds on the domestic market to finance its budget.

Structural Issues

Recent Developments

Due to its small population of about 2 million, the legacy of infant-industry protection, and a history of racially-tinted colonialism, the economy of Namibia is characterised by low competition, high regulation, and diffuse rent-seeking. The government has embarked on a process of regulatory reform in order to infuse much-needed competition, but the results achieved so far have been disappointing.

State-owned enterprises (SOEs) play a dominant role in the economy. According to the latest available annual reports covering fiscal years 2003/04 and 2004/05, the ten largest SOEs had a total turnover equal to N\$4 357 million and recorded total profits equal to N\$46 million, compared to GDP of N\$38 400 million in 2005. The list includes eight profit-making SOEs (Telecom Namibia, NamPower, TransNamib, the Roads Contractor Company, NamWater, Namport, Nampost and Namibia Airports Company) and two loss-making ones (Air Namibia and Namibia Wildlife Resorts). The return on assets ratios are very healthy for non-regulated monopolies (such as the telecom and postal services providers), while the two loss-making SOEs have negative net asset values recorded in their books. Only NamPower has an international credit rating.

So far, the government has taken a very cautious approach towards SOE reform. No privatisation has been concluded so far and in fact the term itself has not been used in the Budget speech since 1999. Air Namibia and the state-owned television and publishing enterprises (which includes NamZim, the joint venture with the Government of Zimbabwe which publishes the *Sunday Times*), received sizeable budgetary support in 2006/07 (N\$153 million and N\$78 million, respectively), while NamPower received a N\$250 million transfer to strengthen its balance sheet

in advance of the massive N\$7 billion Kudu gas-to-power project. In order to improve SOE governance, an *ad hoc* Act was finally gazetted in September 2006, although it remains unclear whether operational responsibilities will rest with the newly established Central Governance Agency or an SOE Governance Council which will act as the representative of the state and report to the cabinet committee.

Regulatory reform has also been proceeding very slowly. For public utilities, monopoly provision is still the rule and Namibia does not have independent regulatory agencies, although a number of separate regulatory commissions has been established in line ministries such as Mines and Energy, and Information and Broadcasting. In mobile telephony, Namibia Telecom has been operating the only company, MTC, since 1995, first with Sweden's Telia as a strategic equity partner and most recently with Portugal Telecom. A second mobile telephony license was awarded in 2006 and the new operator, Powercom, a joint venture between NamPower and Telenor of Norway, will start operating the Cell One brand in 2007. In December 2006, Telecom Namibia finally launched a high-speed Internet service, while MTC is expected to launch 3G services in 2007. Namibia does have a competition law and policy (the Competition Act was enacted in 2003), but due to budget and capacity constraints the Competition Commission has not begun operating. However, the Commission is definitely on the budget list for the 2007 financial year, so it is likely that it will start this year.

Partly due to the heavy role of the public sector, investors' perception of the investment climate has deteriorated in recent years, as reflected in Namibia's slipping-down in a number of international competitiveness rankings. Skills shortages, restrictive labour laws, and shallow financial markets are widely mentioned factors. Namibia has a serious deficit in different technical professions, a problem that is aggravated by restrictions on work permits and the haphazard application of existing rules. Moreover, legislation makes labour dismissal very cumbersome and exceedingly long, and this obviously discourages employers from hiring new staff. Labour laws also

include very generous provisions for annual holidays and other special leaves (for medical and compassionate reasons). Cognizant of these problems, government tabled new legislation to Parliament in late 2006 which includes transferring dismissal procedures from courts to tripartite arbitration tribunals.

As in neighbouring South Africa, affirmative action to increase the participation of Historically Disadvantaged Individuals (HDIs) has been introduced since the late 1990s. The policy of Black Economic Empowerment (BEE) places a premium on increasing the participation of HDIs in the equity of Namibian businesses, and thus, on the transfer of assets, although other criteria such as the share of positions filled with HDIs are also included. Black Namibians currently account for 25 per cent of all executive directors, 45 per cent of all senior managers, and 78 per cent of all middle managers. BEE was particularly successful in the fishing industry around 2001-02, although it is questionable whether local partners contributed much in terms of technical support and facilitating access to markets. In 2006, in the single largest BEE deal so far, Old Mutual South Africa transferred part of its shares to its black employees, church groups, and a special trust. The 2006-09 MTEF includes a target for Namibian ownership in the mining sector of up to 33 per cent. While efforts to redress the discriminatory legacy of the past are to be welcomed, this policy carries the risk of stifling entrepreneurship and perpetuating a culture of rent-seeking. A policy mix that improved the terms of financing of small and medium-sized enterprises (SMEs), and assisted micro-finance institutions and accompanied their scaling-up – so ultimately easing the burden of doing business in Namibia – would carry much greater potential in terms of BEE.

Land reform is another policy domain where progress has been slow. Fifty-two per cent of land in Namibia is held under freehold (commercial) title, while the remaining 48 per cent is communally held. At independence, the commercial land area, which represents 74 per cent of the potentially arable land, was owned by less than 4 100 people, mainly white commercial farmers who made up less than 0.2 per cent of the total population. To date, access to agricultural

land in Namibia for formerly disadvantaged citizens has been facilitated by the state, and by market-assisted acquisition schemes based on the willing seller, willing buyer principle. The government initiated a National Resettlement Programme (NRP) whereby people were resettled on state-acquired freehold farms. In addition, the Agricultural Bank of Namibia has put in place an Affirmative Action Loan Scheme to provide financial assistance to communal farmers for the procurement of commercial land.

Between 1990 and 2005, these two programmes redistributed 4.5 million hectares (against a target of 9.5 million hectares) or 12 per cent of freehold land in the country, benefiting some 2 200 families. Since April 2004, state-led acquisition has been supplemented with expropriation in the public interest. As an initial action, some 25 farms were identified. Since then, the negotiations and the legal process have continued, and three farms have been acquired. The objective is to redistribute 15 million hectares by 2020.

The Namibian government is considering ways of improving its land-reform programme, which has not only been slow, but has also had a negative impact on agricultural production. A Permanent Technical Team was created during 2003 in order to review the existing legal and policy framework, and the economic, financial, and environmental sustainability of land reform. According to the analysis of the Team released in 2005, the land reform process lacks transparent and quantifiable indicators, and contains no provision for adequate support services. An assessment on the outcome of the process revealed that emerging commercial farmers received little back-up support to enable them to become economically self-sustainable. Most farmers cannot survive without a supplementary income. This is mainly due to skill shortages, implementing new farming practices, start-up capital and breeding stock, access to operating credit, equipment, and access to information and advice; and also to poorly maintained farm infrastructure.

The team recommended therefore that the government should: improve the screening and selection of beneficiaries; involve civil society in the reform

process; encourage community-driven resettlement; and favour farm workers. In addition, the team identified the support services necessary for emerging commercial farmers, including pre-settlement orientation courses, short courses, and other formal training, as well as a mentoring system to enhance linkages between farmers and service providers.

Access to Drinking Water and Sanitation

Namibia is one of Africa's driest countries, with annual rainfall equal to 360 mm and an annual evaporation of 3 400 mm. The annual amount of water available is equal to 422.5 million m³ per annum, with a geographically uneven distribution of resources. In particular, high-growth agglomerations such as Windhoek and the coastal towns of Swakopmund and Walvis Bay experience severe water shortfalls that require considerable capital investment to increase supply. Groundwater is the single largest natural source of water, accounting for 40 per cent of freshwater. Perennial rivers and ephemeral rivers each provide roughly 30 per cent of freshwater. Reclaimed water provides about 1 per cent of freshwater.

According to the World Health Organization (WHO), about 98 per cent of urban population had access to improved drinking water in 2004, while 50 per cent had access to improved sanitation coverage. In rural areas, about 81 per cent were estimated to have access to improved drinking water. This represented a substantial improvement compared to 1990, where only 42 per cent of people had access. Not much progress has been achieved in sanitation, since still only 13 per cent of the rural population had access to improved sanitation coverage, compared to 8 per cent in 1990. Overall, although progress in sanitation has been moderate, Namibia is ahead of schedule in meeting the MDG on access to drinking water. From a total of 57 per cent of people having access to drinking water in 1990, the percentage increased to 87 per cent in 2004, which is ahead of the target of 78 per cent.

Freshwater supply is provided by four types of agents. Agricultural self-providers are the largest suppliers (45 per cent) and deliverers to end-users (47 per cent).

NamWater was set up in 1997 as a commercialised water corporation under the supervision of the Ministry of Agriculture, Water and Forestry. It accounts for 40 per cent of all abstraction and delivers 22 per cent of all water to municipalities, industries, mines and the Directorate of Rural Water Supply. Lower government bodies, including municipalities and rural authorities, account for 12 per cent of supply and 29 per cent of deliveries. Finally, a small (although increasing) share is provided by mining enterprises.

As is the case in most other countries, households use less than 12 per cent of all water abstracted. Piped water is the source of drinking water for 99 per cent of urban households and 58 per cent of rural households. However, a significant proportion of households in rural areas draw their drinking water from flowing streams/rivers or stagnant sources. Non-revenue water (including administrative, physical infrastructure losses and metering errors) accounts for a low share of NamWater resources, but losses are much higher for most municipalities. Municipalities with non-revenue water of 20 per cent or higher account for 37 per cent of municipal water distribution, while in seven towns, non-revenue water exceeds 60 per cent.

The 2000 National Water Policy White Paper sets the policy and strategy for water resources management and water services. The White Paper addressed the need to separate the roles of water supply, water resources management and regulatory supervision. The water sector is the responsibility of the Ministry of Agriculture, Water and Forestry, whereas the Ministry of Health and Social Services is responsible for the sanitation sector. Enacted in 2004 to replace the outdated Water Act 54 of 1956, the new Water Bill established a national regulatory board, consisting of five members appointed by the Minister of Agriculture, Water and Forestry.

Cost-recovery mechanisms have been introduced gradually since the mid-1990s by NamWater. This has certainly contributed to the improved management of

water demand among urban users, but irrigation, livestock, and mining still enjoy an important subsidy, since depreciation and operating costs are excluded from the tariff formula. According to a 2006 survey, mining also appeared to have switched from paying tariffs that were substantially in excess of cost in 1999, to receiving large subsidies in 2001/02. A process started in 2005 to update NamWater's system of cost allocation according to different schemes: this may result in a better alignment of costs and tariffs, and in a more transparent allocation of subsidies to different classes of users.

An important aspect of water-pricing policy at the municipal level is the effective collection of revenue. Detailed data on the costs and user charges levied by municipalities are not available. In many cases, local authorities are not up to date with the processing of their annual statements. A 2005 survey of a few local authorities determined that payment levels vary from 40 per cent to 85 per cent of the monthly accounts processed. A number of towns are in arrears to NamWater for their bulk water purchases, due to failure to collect payments from local users. In February 2005, the outstanding service accounts of local authorities were estimated to represent debts of well over N\$400 million. To fight the problem of outstanding arrears on user accounts, in 2003 some towns started installing pre-payment water meters. This measure met with widespread criticism by civil-society organisations and was plagued from the beginning by the high incidence of faulty equipment. An alternative mechanism, consisting of communal-level water committees that collect money from different households for the use of shared taps and toilet facilities, has proved more successful, although this mechanism is not yet widely used.

In terms of the affordability of water services, survey data based on water tariffs in 2003/04 and 2004/05 show that low-income families or pensioners with an income of less than N\$600/month cannot afford to use 6 m³/month, which is regarded as baseline water use for an urban family of five with full water services². In

2. In the residential plot of Tsumeb, 64 per cent of the population has an income of N\$400 or less. Note that income distribution in Namibia is very skewed. The per capita income for the 25 per cent households with the lowest income is about N\$1 600, compared to almost N\$150 000 for the 2 per cent households with the highest income.

rural areas, the situation is likely to be worse. The non-payment of accounts leads to a vicious circle, where both NamWater and local authorities need to increase their tariffs to compensate for the non-payment of accounts. This practice makes services more unaffordable to the poor in Namibia.

In both Windhoek and Rehoboth, the intention of the City Council is to subsidise low-income households to make baseline water consumption (40 litres/person/day) available at a lower price. The lower tariff for basic water consumption might be affordable for low- or no-income earners. However, all households pay

monthly basic service fees irrespective of consumption. This service fee is slightly higher than the consumption fees for the minimum of 200 litres per day, and hence doubles the monthly bill. Windhoek currently applies a rising block tariff: each month, the first 6 m³ are provided at a subsidised rate, while in the 6-to-36 m³/month range, the tariff is at cost-recovery levels. For consumption over 36 m³/month, the tariff is set at long-term marginal cost. There is a general consensus within municipalities and at NamWater that the strategy adopted in South Africa of providing free water up to a consumption of 6m³/month is ineffective, as it creates enormous problems for municipalities in covering the

Sustainable water supply in Windhoek

The municipality of Windhoek is served by three dams which are operated by NamWater. 50 boreholes contribute about 4 per cent of total water supply, while the Goreangab Reclamation Plant provides an additional 27 per cent. The plant was built in 1968 and upgraded from 8 000 m³/day to 21 000 m³/day in 2001. Windhoek was one of the first cities in the world to introduce direct recycling of effluent for drinking purposes. Purified effluent is also provided to consumers for landscape gardening. Extensive water-quality monitoring programmes are in place to ensure the required level of water quality after each treatment process, as well as the quality of the water finally supplied to the City of Windhoek.

The City of Windhoek signed a performance-based Private Management Agreement with Windhoek Goreangab Operating Company (WINGOC) in 2002. WINGOC has three shareholders, viz. Veolia Water, Berlinwasser International and WABAG. The water-resource planning year runs from May to April, spanning the rainy season. During May of every year, after the rainy season, the Department of Water Affairs, in conjunction with NamWater, plans the integrated use of the resources. During 2005/06, the Goreangab Reclamation Plant was operated at around 70 per cent of capacity. Due to abundant supplies in the dams, the Department was able to rest the well field and limit abstraction from the boreholes to 1 million m³. The sustainable supply of water to the city remains the top priority of the Department. The Department is also in charge of wastewater collection and treatment, mostly for re-use. The Gammams Water Care Works, where the bulk of the sewage is treated, was first built in the 1960s, and has been upgraded a number of times. Some of the infrastructure components are fairly old, and serious problems are being experienced in dealing with the amount of sludge at the plant.

In an effort to ensure sustainability for water demand in a context of scarcity, the municipality of Windhoek introduced water-demand management in 1994. The strategy concentrates on changing consumer habits by increasing public awareness of the importance of saving water, and on the implementation of a block tariff system that applies a steeply rising water cost with increasing consumption. Some other measures include: the reduction of residential plot sizes; the implementation of legislation to address water conservation in Windhoek; and improved maintenance and technical measures to reduce leaks. In 2006, unaccounted-for water was 10.3 per cent, a very good indicator compared to other municipalities.

costs of supply (240 out of 273 are facing serious financial problems), and it increases water wastages.

The municipality of Windhoek practices integrated water management, and also provides an example of the successful use of unconventional sources of additional water. Technological advancements have allowed the implementation of innovative public-private partnerships in the reclamation of water (see Box).

Political Context and Human Resources Development

Namibia enjoys political stability, and a multi-party system is in place. In the 2004 national elections, the dominance of the South West African People's Organisation (SWAPO), which has been the ruling party since independence in 1990, was confirmed. SWAPO won 76 per cent of the vote, and the new President Hifikepunye Pohamba was elected with 76.4 per cent of the vote. The new administration has made the fight against corruption the cornerstone of its policy. While Namibia ranks relatively well among African countries in Transparency International's annual ranking, a number of recent scandals, including those at Avid Investment and the Offshore Development Company, raised concerns in the business community and civil society that SWAPO's seemingly impregnable position may have turned the government into an instrument at the service of the party. Moreover, while the fragmented opposition does not represent a serious threat to SWAPO, the government party suffers from deep factional divisions.

Namibia is characterised by one of the highest levels of income inequality in the world. The Gini coefficient is 0.6, according to preliminary results from the Namibia Household Income and Expenditure Survey (NHIES) 2003/04. While this represents an improvement from the 0.7 reported in the previous NHIES 1993/1994, Namibia still ranks among the most unequal countries in the world. The 10 per cent of households with the highest income account for nearly half of the total income in the country. The incidence of poverty varies

among functional groups and also according to the economic dualism which characterises the economy; 42.2 per cent of the rural population is estimated to live below the national poverty line, compared to 6.7 per cent for the urban population. In urban areas the per capita income is about three times higher than in rural areas. An example of the differences among functional groups is that the incomes of commercial farmers are eight times higher than those of subsistence farmers.

Despite the large share of expenditure allocated to education – between 20 and 26 per cent of the budget over the past 15 years – the net enrolment rate is only 52 per cent at the secondary level, compared to 95.7 per cent at the primary level, and efficiency is low. Several factors hamper the efficiency of the educational system: as an inheritance of the pre-independence period, the northern regions perform badly, since teachers are not adequately trained, the pupil-teacher ratio is higher compared to the central and southern regions, and the infrastructure is much less developed. This divide applies also to rural and urban areas. In addition, the quality of teaching in scientific subjects is low compared to other subjects, and there is only one technical school in the country.

In order to remedy the inequalities caused by the colonial past, the government has initiated a far-reaching reform of its education and training sector in the context of *Vision 2030*. Apart from free and universal basic education, Vocational Education and Training (VET) has been regarded as key to providing the skilled workers and employees needed for industrialisation. Already in 1994, the Namibian Government introduced the National Vocational Training Act to regulate its VET system. Today, more than ten years later, its ambitious expectations have not been met. Major problems that the Namibian VET system faces include: a mismatch between skills supplied and skills demanded; low intake and output of graduates; high failure rates in national trade tests; high unit costs; and inefficient management.

Due to the lack of efficiency and effectiveness in the education and training sector in general, the government, with the support of the World Bank, has initiated the Education and Training Sector

Improvement Programme (ETSIP), in order to improve the delivery and results of education and training. The ETSIP strategic framework covers the period 2005-20. Major objectives include: improving equality in skills provision, reducing teachers' absences, and raising school enrolment rates. The success of the reform will depend on improved co-ordination between the various education departments (basic, secondary, and higher education), and on a well-functioning evaluation and monitoring mechanism. In addition, one of the major challenges and requirements for successful reform is the increased involvement of the private sector in all aspects of the training system, ranging from the provision of training to management of the VET system. For this, it is crucial to provide incentives for firms to provide on-the-job training.

The first HIV/AIDS cases were reported in Namibia in 1986, and the Ministry of Health and Social Services estimates that 230 000 adults and children were living with HIV/AIDS at the end of 2001. According to the 2004 Sentinel Survey, Namibia exhibits an adult infection rate of 19.7 per cent. In turn, life expectancy at birth declined from 53.9 years in 1970-75 to

48.6 years in 2000-05. Aside from the human aspects, the economic and social costs of the epidemic are enormous. According to a recent IMF study, slippages in counteracting the current spread of the epidemic could reduce real GDP growth by one percentage point in the period 2006-11. In an effort to control the epidemic, plans have been developed consecutively from 1990 onwards. The Third Medium Term Plan (MTP III) for the period 2004-09 benefited from significant support from co-operating partners, and made possible a reduction in drug prices. The MTP III takes a "results-based" management approach to achieving nationally and internationally agreed targets in terms of prevention, access to treatment, care, and support services. The number of beneficiaries of antiretroviral therapies could reach 50 000 by 2009, compared to an initial target of 25 000. The shortage of adequate human resource capacity to manage and implement the national response in a well co-ordinated manner remains a major challenge. In this respect, a National Human Resource Planning Task Force has been created to develop training capacity across the country in order to combat the spread and impact of HIV/AIDS.