THIRD QUARTER ECONOMIC BULLETIN-SEPTEMBER 2016

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1.0. Effects of BCL mine closure on the economy

We are still digesting the shocking news which we woke up to on the weekend of the 8th of October; "BCL mine placed under provisional liquidation." The news which we have been dreading to hear all along finally came. We all knew that BCL, just like any other mine have been facing challenges mainly due to the depressed commodity prices on the international market. We never thought it would come to this level. One thing which is certain is that the closure of the mine will send ripple effects not only in the mining town of Selibi Phikwe, Francistown and surrounding areas but the whole economy of Botswana. Francistown will be affected even more as Tati Nickel Mine, a subsidiary of BCL has also been closed. Palapye and surrounding areas will also feel the pinch as the Morupule coal mine will be affected given than BCL was the major consumer of Morupule coal. The placing of BCL under provisional liquidation comes at a time when we are still recovering from the closure of Boseto and African Copper mines throwing many workers into the streets. The negative multiplier effects will be severe and will have long lasting effects on the whole economy at large. It will no longer be business as usual.

Brief history of BCL

BCL formation can be traced back to August 1956 when a meeting, arranged by John Buchanan, Chairman of Minerals Separation Limited, took place between Tshekedi Khama, Regent of the Bangwato Tribe in the Bechuanaland Protectorate (The Republic of Botswana) and Sir Ronald Prain, Chairman of Roan Selection Trust (RST). At the meeeting an agreement was reached between the two men, which was later signed on the 2nd of June 1959 and subsequently ratified by the British House of Lords and led to the formation of Bamangwato Concessions Limited (later to be renamed BCL Limited), to prospect, explore and mine Copper and Nickel ore discovered in the present day township of Selebi Phikwe.

BCL produces two types of finished matte containing nickel, copper, and cobalt and to a smaller extent precious and platinum group metals. It is the second largest private sector employer in the country with a labour force of +/-4200. It consumes just under 20% of total electricity usage in Botswana or 43% of BPC's own power generation.

The aftershock effects

The direct effect is the loss of jobs and income for some +/-4200 workers who were employed by the mine. Companies that were subcontracted will also close further putting more workers on the streets. The indirect jobs that will be lost are even more. Palapye town will be affected as Morupule Coal mine will probably downsize operations as BCL was the biggest user of its coal. The hospitality sector around Selibi Phikwe and Francistown areas will be crippled, if not likely close altogether in the case of Phikwe. The retail sector will face a significant decline in business activity and most will be forced to relocate from Phikwe. This in turn will reduce the business activity of the town ie the transport sector, education sector, food outlets, fuel suppliers, property sectors etc. The property sector will be affected as the decline in occupancy and property demand will have an effect on valuations. The list is endless and the negative multiplier effects will be severe.

Government revenue in the form of taxes will also be constrained due to the reduced business activities that will follow. This will have an impact on the government fiscal balance at a time when diamond prices are not doing very well. Already Lerala Diamond mine is reportedly planning to scale down production and retrench. The country's current account and Balance of Payments positions will also worsen. The mining sector at large contributes over 35% towards government revenue.

Banks not spared either

The banking sector is not spared either. Impairments are likely to spike especially from unsecured facilities extended to the mine directly, mine employees and other related companies exposed to BCL. The list is endless and the negative multiplier effects will be severe. Some of government enterprises will not be spared either. Already Botswana Railways is reportedly facing a P20mn reduction in business revenue from BCL. Water Utilities Corporation will also have to scale down its operations as it has been supplying bulk water to the mine.

Where to from here…

The liquidator report is likely to come up with 2 recommendations.

(1) Complete shutdown of the mine (which is highly unlikely)
(2) Scaling down of the mine operations and closure of some of the shafts which are unprofitable. (This is highly likely, although we cannot rule out some job losses)

Lessons learnt

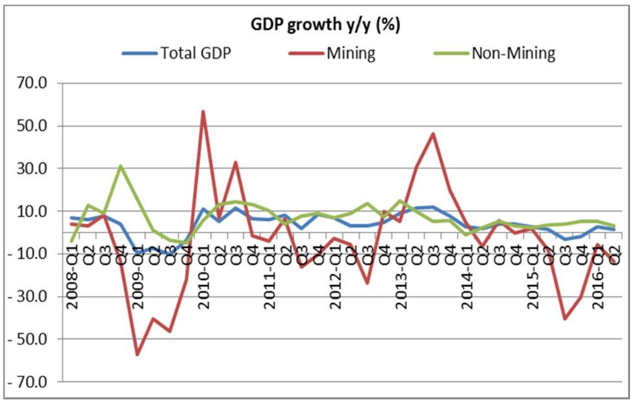
There are many lessons to be derived from the placing of BCL mine under provisional liquidation. Once again this has shown the need to speed up the diversification of the country's economy away from the mining sector. Although there has been some movements in this regard as shown by the growth of the non-mining sector over the years and the decline of the mining sector contribution to the economy from levels around 31% of GDP in 2004 to levels around 13% of GDP as at 31 December 2015. What we can agree is that the speed of the diversification process is not moving at a pace that we want. The pace has been slow.

BCL smelter can be the game changer

BCL has been making losses for some years, but we believe there is still value in the copper/nickel mining company and some of the shafts that are not profitable have to be shut down if the mine is to operate efficiently and profitable. The BCL smelter is one of the project we believe has the potential not only to contribute positively towards the profitability of BCL but also turn Botswana into a hub for the smelting and refining of copper/nickel in the region. With a capacity to treat up to 850 000mt of nickel/copper concentrates per annum, the smelter is large enough to absorb all the smelting requirements of all nickel/copper miners in the region as it is the only copper/nickel smelter in the region. This is because it will be uneconomical for other small mining companies in the region to build their own refineries given the large capital outlay that is required to build one. It is estimated that the current BCL smelter has a replacement value of between US$2bn and US$3bn.

2.0. Agric, Mining and Manufacturing sectors slows the economy during Q2 2016

Botswana's economy limped during Q2 2016 with GDP contracting by -1.3% q/q while growing by a paltry 1.6% y/y from a growth of 2.7% y/y during Q1. The agric, mining, manufacturing and water & electricity sectors all contracted by -2.5% y/y, -13.8% y/y, -0.2% y/y and -449% y/y. What is even more worrying is that the agric and the mining sectors have been contracting since Q2 2015 and the situation appears to be worsening especially in the mining sector. The placing of BCL under provisional liquidation will certainly aggravate the already dire situation in the mining sector. We expect Q4 GDP numbers to fall further led mainly by the contraction of the mining sectors. Other mining houses are also reportedly contemplating on retrenching, citing the depressed commodity prices on the international market and we do not expect any significant increase in commodity prices any time soon. Although the global economy is improving, the recovery is slow and unevenly spread out.



Source: Statistics Botswana

The positive news is that non mining GDP growth has been fairly consistent and is in the positive territory averaging a growth of 3.3% since Q1 2014. This is good as the sustained growth of the non-mining sector will go a long way in the diversification of the country's economy away from the mining sector.

The US economy is picking up with the US Fed widely expected to increase the rate in December due to positive economic numbers. China's economy is also slowly picking, although the growth is still below what we have been accustomed to. China's Q3 GDP grew by 6.7% y/y, in line with forecast and it is the third quarter in a row that the economy grew at that pace. China is the biggest commodity consumer and we hope the sustained growth of China's economy will bond well for the recovery of commodity prices and this will be good news for commodity dependent countries such as ourselves.

3.0. Credit growth on a downward trend

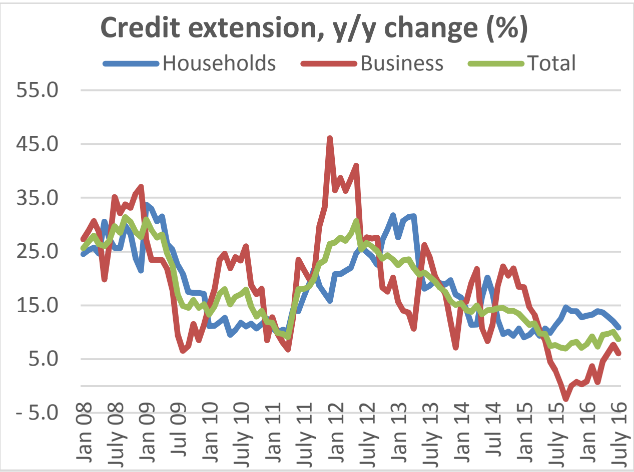
The low interest rate environment seems not to be doing much to boost credit growth by commercial banks in the country. Latest statistics released by the Bank of Botswana for July shows a decline in overall credit growth by commercial banks to 8.7% y/y in July 2016 from a growth of 10.1% y/y the previous year. Since March 2015, credit growth by commercial banks has been growing at a slower pace and below 10% y/y. This is in sharp contrast in preceding years when credit growth used to grow by double digit numbers.

On the 12th of August 2016, the bank of Botswana stunned the markets by reducing the bank rate from 6% to 5.5%. This was almost after a year since the last interest rate cut on the 6th of August 2015 by the

Central Bank. We cannot rule out another interest rate cut by the central bank before the end of the year, although we believe the central bank now has very little room for another downwards adjustment. We are not alone in this interest rate cut as so far this year, a total of 38 central banks have eased their monetary policies, while 18 have tightened.

Why is credit growth failing to pick up?

This is a very interesting and important question as one would have naturally expected credit expansion to grow at a much faster rate given the ultra-low interest rates. We believe the irony of this declining trend could be attributable to the deterioration of borrowers' credit capacity and weak demand prospects, which all have dampened banks appetite to extend more credit and demand for business to take up more credit. The Bank of Botswana March 2016 Business Expectations survey shows that overall business confidence deteriorated from 44% in September 2015 to 36% in March 2016 and this is worrying.



Source: Statistics Botswana

Credit growth to the business sector has declined much faster. Since May 2015 it has registered a single digit growth and in July 2016 stood at a growth of 6.1% y/y. Prior to May 2015, credit growth to the business sector has been averaging 16%. This is not surprising as there has been a significant decline in credit growth to most important and productive sectors of the economy such as agric, mining and manufacturing sectors. Credit growth to the agric sector was at 30.6% y/y in January 2016, but has since fallen to 13.8% y/y in July. Mining sector credit growth is actually in negative territory and this is not surprising given the low commodity prices on the international markets which in turn have seen the closure of some big mines in Botswana such as African Copper, Discovery Metals and most recently the placing of BCL on provisional liquidation.

The household sector has not been spared either from the decline in credit growth as it has fallen to a growth of 10.9% y/y in July 2016 from a growth of 13.1% y/y in January 2016. There are fears that most households will struggle to settle their arrears if interest rates starts to rise in the near future and this will have contagion effects on the banking sector and the economy at large in terms of NPL's. Credit extension to the household sector takes up 59% of total credit extended by commercial banks.

4.0. BSE EQUITY MARKET REVIEW

Q3 was a rough Patch for some…

The 3rd quarter of the year was characterised by a series of double digit losses. Four companies sunk into double digit losses in the quarter alone, while the likes of Letshego managed to stage notable comebacks. The biggest listing in the country by both subscription and value, BTCL traded below the listing price for the first time. The stock opened Q3 trading at P1.09 having dropped gradually from the surge experienced on the first two days were it quickly reached its peak price of P1.35 a share. The share price has been under pressure from a large selloff and profit taking by speculative traders who were initially excited by the IPO. However a reported loss for the period 31st March 2016, saw the newly listed stock experience a new wave of sellers and a drastic drop in price. The stock price fell by 22% to close the quarter at its current price of 85 thebe a share. The loss, which was the result of a huge write off of obsolete technologies, should in theory be a onetime occurrence and the company should bounce back into profitability. The company remains cash rich and managed to declare a final gross divided of 5t a share, relieving in part the capital losses. Expect their end interim results for September no later than New Year 's Eve, for better direction in trading.

In addressing the influx of shares in the market, BTCL was the first to exercise the new provision in regulation from the exchange of engaging a Market Maker to facilitate and improve liquidity. The buyer of the last resort was able to mop up the excess shares in the market to stabilise the price and the stock has been trading at 85t since 18th August.

Furnmart was another major casualty for the period under review. The furniture and appliances retailer, with a footprint that extends into RSA, Namibia and Zambia, also owns the middle to high end Home Corp. However the stock price has been under pressure following a reported loss for the 6 month period end on the January 31st 2016. Growing competition in the sector coupled with regulatory tightening on the Hire-Purchase agreements have impacted both revenue and profitability. Another huge impact on profitability was currency translation differences brought on by a weaker rand for the reporting period as well as the falling Kwacha, in Zambia. Expectations remain bearish on the stock as operating conditions are not expected to change significantly for the year. The stock is currently trading at 85t, down from P1.04, however we believe the 18% price depreciation, could have been worse had our markets been more liquid.

The Choppies slogan of "value for your money" certainly this time around is not targeting investors. The country's fastest growing retailer has not kept up pace when in it comes to profitability. In their recently published year end results, the company reported a huge decline in profitability by 48%, with basic earnings per share reported at 8.48 thebe, with an end of quarter P/E ratio 41 times. In the same period the price has fallen by 12.5% from P4.00 to P3.50 and has fallen further in October currently sitting at P3.05 a share. Worse more the company has not been profitable outside the local boarders and has even moved into recess in Zimbabwe were they have posted positive results before. The company will have to prove to weary investors that their Jwayelani and Kenya acquisition will contribute towards improving the bottom line in their next interim results, or struggle some further depreciation.

First National Bank Botswana continues to struggle through the third quarter on growing pressure from the lowered interest rates in August. This is despite the recently lifted moratorium on banking charges. The banks earnings per share for year ended June 2016 were lower by 15%, although revenue and Non Interest revenue grew for the period. The bank lost 10.3% in share value over the period, to close at P3.05 a share down from P3.40. Still under banking, Stanchart also lost 3.8% from 810 thebe to 779 thebe.

The bank of Botswana announced a further interest 0.5% rate cut in August, squeezing banking margins tighter. Furthermore the recent closure of the BCL and Tati mines will see a lot of banking impairments as former employees failing to meet their obligations.

Letshego Holdings has had a turbulent 3rd quarter. The stock price plummeted to its lowest price in over 5years in August of P1.80 a share. This followed a massive international sell off of the counter which quickly flooded the market. The relentless selloff puzzled many as the company has not been underperforming by any measure. The board and management quickly announced their intention to revive the share buyback of at least 10% of the stocks listed shares. The stock price recovered considerably from there, climbing up to P2.37 a share by the 29th September, having reduced the quarterly deficit to just under 5%, from 25% at the lowest point.

Struggling to keep afloat-Q3 top losers

COUNTER	29 Sep (t)	29 Jun (t)	Change (%)	YTD (%)
BTCL	109	85	-22.00	-15.0
Furnmart	104	85	-18.27	-22.0
Choppies	400	350	-12.50	-30.7
FNBB	340	305	-10.29	-20.4
Letshego	249	237	-4.82	-17.2
Stanchart	810	779	-3.83	-30.4

Source: Motswedi Securities, BSE

The Spring Bloomers

The third quarter marks the end of winter locally and with it flourished some stocks. Engen rose a year to date lose, to 9.9% gains year to date gains over the Q3 alone. The stock price rose from P8.00 to P9.20. The increased demand for the stock follows a series of special dividends, having declared 62.6 thebe this year alone, and a further 15thebe interim dividend which is 25% higher than the previous year's. Cresta's performance, having appreciated by 8.26% in the quarter to P1.31 a share, is only dampened by the recent suspension of both the MD and CFO. This casts a gloomy picture on the stock, which started the year trading at 86t. The only solace coming from this is what seems like good governance structures with the board taking quick action. The true reasons for the suspension have not been made public, but one can speculate given the positions.

Security giant G4S released some positive half year results, with earnings per share 6.4% and a dividend growth of 4.5%. This propelled the stock price higher by 5.77% over the quarter, to P3.85 a share.

Barclays also release some incredible half year results, posting earnings growth of 144% growing by nearly 5% in share price to close the quarter at P4.86, a 52 week high. All this in spite of the challenges facing the banking sector. Lucara Diamonds has been a solid performer for the year, appreciating by 73% year to date, however the stock had a rocky start to the quarter after failing to sell the largest diamond to be discovered in over a century. The stock price was boosted by good half year performance and a special distribution to shareholders. The stock price eventually recovered the losses to close Q3 11% higher at P34.77 a share.

Major Winners– 3rd Quarter 2016

COUNTER	29 Sep (t)	29 Jun (t)	Change (%)	YTD (%)
Engen	920	800	+15.00	+9.9
Lucara	3477	3477	+11.16	+73.0
Cresta	130	131	+8.26	+21.5
G4S	385	364	5.77	+6.4
Barclays	486	463	+4.97	+8.9

Source: Motswedi Securities, BSE

The Domestic Company Index has been under immense pressure for most of the year, having lost 8.4% to date. Q3 was no different, as it depreciated by 3.12% over the period to close at 9,766.95, down from 10,081.31 in June. The losses reflect the impact of the highly capitalised stocks that fell by double digit figures over the period. The Foreign company index benefited from the appreciation of Lucara, and closed 0.43% higher at 1596.

5.0. An Overview of the Botswana Property Market – September 2016

The property market in Botswana has experienced a noticeable decline in the year on year yield or return on investment of all the property asset classes. Projections from the IPD Botswana 2014 Annual Property Consultative Index's report shows a decline in ungeared total returns from 21.5% in 2013 to 11.5%. These numbers are not surprising given the slowdown of the local economy, coupled with the tightening of government budget as well as the oversupply of properties especially in the office and retail space.

Vacancies are steadily rising especially in the office space and in larger shopping malls. The restrictions of the issuance of trade permits under the Trade Act is causing more uncertainty and anxiety in the sector. Already one of the listed property stocks, Primetime has already sounded some warning bells as one of its new shopping centre, Pilane Crossing is likely to be negatively affected as around 30% of the Centre had been let out to South African National Retailers who are struggling to obtain trading licenses. Turnstar and NAP will also be affected as they have significant exposure to the retail sector.

Commercial banks appetite to extend credit to the property sector has also been falling as shown by the latest Bank of Botswana financial statistics. Credit growth to the real estate has dramatically fallen from a growth of around 20% during 2014-15 to a negative growth averaging 19% between March and May 2016. As at July 2016 credit growth to the Real Estate was flat.

Office

There is an oversupply in this space due to the increase in supply especially in the CBD area. Demand has been weak as a result of lack of new market entrants, the slowdown of the local economy and a decrease in govt expenditure. Rentals are softening especially in properties outside the CBD area. Vacancies are also on the rise and its now common to see 'offices for rent signs' around the Kgale Mews area and other outlying areas. We expect rentals to remain under pressure with the possibility of existing tenants even negotiating for lower rentals upon the renewal of their leases.

Retail

The retail sector which has been going through a transformation has now reached a point of saturation in our view. Bigger shopping malls with strong tenancy mix have been expanding as we have seen the expansion of Game City, Rail Park Mall and Airport Junction. The secondary shopping malls, haven't seen any significant expansion. The presence of more Shopping Malls however, is impacting on rental yields as the new developments are simply "recycling" the existing tenants as business is simply shared from the same market, without any significant corresponding increase in new customer base. The good news however, is that vacancy rates in the sector are low and this should sustain some growth in the short to mid-term as existing contractual lease escalations are realised. The restrictions of the issuance of trade permits will likely have an impact on this sector as most of the tenants are from South Africa and they might be forced to close shop upon failure to renew their current trade permits once they expire.

Industrial

Demand for industrial properties is very high boosted by the growth of the logistics and manufacturing industries especially on the smaller starter units of up to $200m^2$ as well as bigger units of over $1,500m^2$. More listed companies are paying closer attention to this sector, with RDCP, Letlole and Primetime increasing their exposure into this sector.

Residential

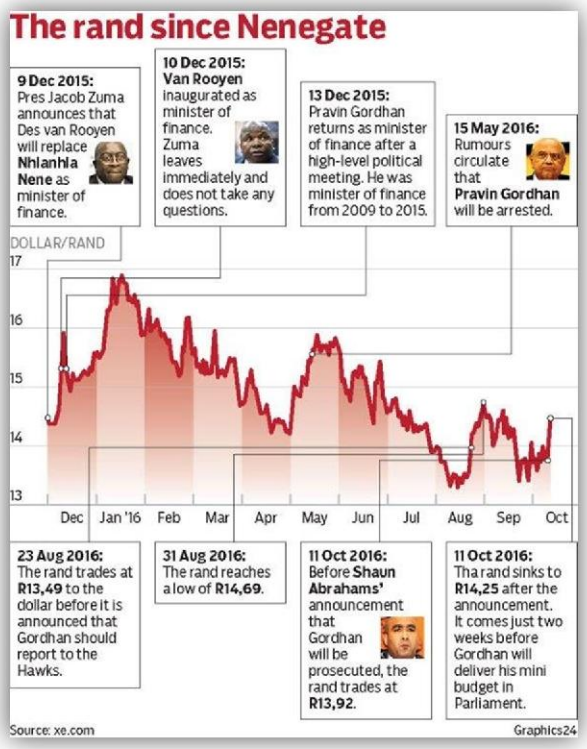
Demand for residential properties especially on the low to mid income levels is very high with the existing supply overweighed by demand. Demand pressures are mainly coming from growth in the population, migration to urban areas especially Gaborone as well as the increase in student and elderly populations. Demand for medium to high cost residential properties is almost at equilibrium and in some cases reaching saturation as there are only a small number of affluent individuals who are able to afford the properties in this space. The few who can afford will rather prefer to get a mortgage than renting. RDCP, one of the listed property firm is however increasing its exposure into this space through the development of the ICC Residential Flats which are aimed at the mid to high income bracket. Demand for secured complex properties is however, stable mostly due to demand from expatriate workers.

6.0. Foreign Exchange Market Developments

The firming of the US dollar continued to wreak havoc on emerging markets currencies as most moved southwards following the rise of the dollar. The US dollar has been on a rebound mostly on growing expectations of a US Fed interest rate hike in December. Positive economic numbers from the US economy such as improving employment statistics, retail sales among others point to an improving US economy, raising more reason for the Fed to hike its bench mark interest rates in December. An increase in US interest rates will see the flow of "hot" money into the US as investors will be seeking to get better returns for their investments and in less risky assets such as bonds and other money market investments.

Meanwhile, the rand has also been on a roller coaster due to a combination of a firmer US dollar and local economic developments. The summoning of the much respected Finance Minister Pravin Gordhan to answer questions related to corruption has spooked investors, resulting in the rand being a punching bag against most currencies. Prosecutors allege that Gordhan and two of his former colleagues from the South African Revenue Service committed fraud when Gordhan granted early retirement to one of the colleagues, then later allowed him to return to work. Gordhan faces a count of fraud and another for the unlawful extension of the former commissioner's contract. The rift between President Jacob Zuma and Gordhan is said to be behind the finance minister's legal trouble.

The infographic below tracks the volatility of the rand since President Jacob Zuma announced that the virtually unknown Des van Rooyen will replace Nhlanhla Nene as minister of finance.



The period saw the inclusion of the Chinese yuan into the SDR by the IMF. In line with this, the Bank of Botswana also announced that it would start publishing the yuan cross rates. The weights of the Pula against the rand and the SDR will remain the same at 50%. The inclusion of the yuan will not have any material effect on the value of the pula. The pula is more prone to rand/$ movements and our calculations shows that a 2% move of the rand against the dollar will have a 1% effect on the BWP/ZAR movements.

Domestic (Pula Exchange rates)*

Currency	29 Sep 2016	30 Jun 2016	Q/Q (%)	YTD (%)
US$/BWP↑	0.0964	0.0914	5.47	8.31
ZAR/BWP↓	1.2951	1.3606	-4.81	-6.36
EURO/BWP↑	0.086	0.0824	4.37	5.65
GBP/BWP↑	0.074	0.0682	8.50	23.33
JPY/BWP↑	9.7	9.38	3.41	-9.51

Source: Bank of Botswana, SARB

***=** *The rates as produced by the Bank of Botswana are for information purposes only and do not represent the rate that may be offered for any foreign exchange transactions.*

For the quarter under review, the pula was firmer against most major currencies with the exception of the rand. The local unit firmed most against the pound, mainly due to the weakening of the pound against the dollar mainly due to negative investor sentiments brought about by the Brexit uncertainty.

7.0. International Commodity Markets- Brent crude oil stable

Brent crude oil prices swigged between $45/ barrel to $53/ barrel on geopolitical tensions and expectations that OPEC member countries would agree on a cut in production. In September Opec announced plans to cut output to boost prices and will meet in Vienna on the 30th of November to iron out how this envisaged production cut will be implemented. The plans for an output cut are already in jeopardy as Iraqi, which is the second largest producer in OPEC has said that it wants to be exempted from this output cut as it needed more money to fight Islamic State militants.

Opec is now comfortable with seeing oil prices trade between $50-$60/ barrel and this can be achieved if the global economy recovery mode gains momentum and Opec members agree on a production cut. It is now evident that the current cycle of falling crude prices is close to an end as market fundamentals are slowly improving.

Gold

Precious Metals were in consolidation mode during the period fluctuating up and down. The weaker dollar gave much needed room with gold trading slightly higher at levels around $1263.95 per ounce. Silver and platinum were however, softer trading down at $17.51/oz and $925.oz respectively.

Base metals on the other hand were hard hit by the slowdown in industrial and manufacturing production from the world's largest consumer. The Chinese GDP grew by a modest 6.7% however the growth was driven retail sales. The demand for base metals is also predicted to go on a decline for the next three years. Nickel and copper where down by over 3.5% trading at $10,165 and $4,633 a tonne, respectively.