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IJG SECURITIES
ECONOMIC OUTLOOK
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Contents

Overview

As the memories of the global recession fade in our minds, so we become complacent, and start to believe that the worst is over, behind us. However, as 2016 starts to grip, it appears that the clouds are once again building, and the frosty headwinds once again gaining force.

China is in turmoil, we all know it and have been aware of its coming for a number of years. A "triple bubble" appears to have started deflating, led by a stock market meltdown, with risks of contagion to the property and credit markets the major concern. Debt levels are too high, growth is too low. The shift from central driven investment lead growth, to large scale consumption lead growth, is proving a bumpy ride, to say the least.

Europe remains troubled, bouncing from one crisis to the next with little real resolution, and as the various cans get booted ever further down the track, the rainclouds build. Grexit, Brexit, debt crises aside, the refugee crisis looks set to derail the "European dream", as vastly different views as to the European response see borders being once again erected, and the popularity of key leaders (notably Ms. Merkel) waning to unprecedented levels.

Snowstorms in the US (literally and figuratively) illustrate an economy that remains fragile, with little real growth in core sectors of the economy (notably manufacturing), and a fragile employment story to tell (low participation rates). The first interest rate hike in almost a decade has not gone down well, as both the stock market and economy appear to be somewhat shaken, and struggling to adjust to the new interest rate (just 0.25% above those of the past 7-odd years).

South Africa continues to teeter on the 3D precipice of high inflation, low growth (recession?) and a credit rating collapse. The causes, while too many to detail, include but are not limited to energy, leadership, commodity prices, labour unrest and capital outflows. With economic deterioration, rating downgrades and an ongoing rand rout, the outlook for our southern neighbour looks increasingly precarious, with many economists seeing "junk" status and recession as inevitable. The SARB is stuck between a rock and a hard place, as its mandate of price-stability stands to push the country into recession, while protecting the value of the rand for those that have some, but making it ever harder for those that do not, to get some.

Namibia too stands in the midst of a storm, where unlike the events of the late noughties, the outlooks for Namibia and South Africa have become notably more correlated. Limited policy space (debt-to-GDP at over 35% for the first time, for example), infrastructure challenges, rating risks, and current account weakness spell doom and gloom for the Namibian economy, but perhaps unlike our southern neighbour, the pain may be short-felt, if handled correctly. With our hand forced on interest rates, and a probable credit rating downgrade, cautious management of the fiscus will be required to ensure that the downturn it temporary. Efforts to keep the spending party going may well spell long term doom for the country, as the deficit will blow out, taking with it the cost of funding, and the debt stock, and making longer term recovery a sizable challenge. On the other hand, fiscal tightening will add fuel to an already slowing economy, making the fiscal tightrope a challenging one to traverse.

Hotspots of growth are to be few and far between, more on account of the exceptionally high base created in the local economy after the five consecutive boom-years from 2010 to 2014, than any great wrongdoing. Drought and commodity price weakness do little to help the cause, however remain largely out of the control of players in the local space.

The downturn will likely leave the pockets of consumers somewhat less padded, and with expected tax increases (solidarity tax and potentially others), and higher debt servicing costs, little growth is expected in the areas of consumer discretionary goods, particularly those considered most luxurious.

The external position is to remain under sizable pressure, both on account of rand weakness and import costs increasing (but volumes decreasing), slow growth in exports and limited FDI inflows. Net outflows are expected to continue in 2016, as was the case in 2015 (if the Eurobond flows are set aside for comparative purpose), leaving the already battered reserve position weaker once again.

The year 2017 should see some respite, all things being equal, as the vast Husab mine ramps up towards full production, adding extensively to mineral output and exports. In addition, our base case scenario sees the end of the current drought in 2016/17, and a slow recovery in agricultural activity, off the low, drought-level, base. Energy and water remain key concerns, however with limited major increases expected in demand for the former, coupled with the relatively small consumption figures for the country and ongoing efforts to expand production, we expect to see energy issues resolved without a major hiccup. Water, however, remains of great concerns, as the security of supply, particularly for the mines at the coast and the central area, remains in the hands and the wills of the gods at present.

The good news for Namibia, however, is that much space still exists to improve the bang-for-buck spending of the national budget, while at the same time, certain state owned enterprises can be wholly or partially privatized, in order to free up some liquid capital for the state. In addition, the funds raised in Namibia's last Eurobond issue remain available to the country to ward off the unwelcome advances of recession, and to protect the external position from further degradation. Moreover, while under pressure, Namibia's key export minerals, namely diamonds, uranium and gold, have been far less badly affected by the recent commodity price rout, and when viewed in Namibia dollar terms, have actually seen price increases. Finally, Namibia remains a net creditor to the rest of the world, with a fairly sizable stock of international investments (the property, let us not forget, of pension fund members).

In all, Namibia is likely to experience a tough year in 2016, but if handled carefully, will likely be fairly short lived. The continued twin deficits situation will hopefully unwind come 2017, all things being equal. While unpleasant, weathering the storm is necessary, and part of the normal economic cycles. All, most certainly, is not lost.

Key risks to the outlook:

Our base case scenario, discussed through this document, does not factor in all of the potential risks at play in the Namibian, regional and global economies. Given the innumerable risks at present, the multitude of scenarios required to capture these risks would ultimately prove to be counterproductive. Nevertheless, some of the key risks are detailed below:

1. Interest rate shocks

Given the recent deprecation of the rand vis-à-vis major currencies, and the inflation implications thereof, there is a possibility, albeit an outside chance, of an interest rate shock in 2016. By our definition, such a shock would take the form of a repo rate increase of more than 350 points through the year. This would have an obvious contractionary impact on the economies of Namibia and South Africa, as well as on the NPLs and impairments of the baking sector in the region.

2. Water

While unlikely in 2016, there exists a risk of serious water shortages across the central area of Namibia in 2017 and thereafter, should rains continue to disappoint. Water shortages of this nature can be expected to have a catastrophic impact on the economy of Namibia, and would likely drive major declines in production and employment, as well as present a raft of other negatives for the local economy.

3. Energy

Energy remains a key issue for Namibia as well as the region. Supply shortages are undoubtedly here to stay within the region, however Namibia has so far managed to avoid any negative fallout. However, should major issues re-develop in South Africa, Namibia may too find itself in hot-water. Similarly, regional issues in Zambia and Zimbabwe, may present supply issues for Namibia. In addition, with continued rand depreciation and extensive new CAPEX required for new supply capacity in Namibia, energy prices may yet introduce a shock to the local economy.

4. FX shock

While the rand has depreciated heavily against major currencies over recent months, it is possible, but unlikely, that further depreciation may be seen. This will put further pressure on the SARB to hike rates, and may precipitate the aforementioned interest rate shock.

5. Policy response

In Namibia, the key risk at present is the fiscal response to the slowing economy and softening revenue collection. It is possible, but unlikely, that the central government will continue to spend aggressively through the downturn, resulting in a blowout of the deficit and debt position of the country. Should this happen, the short term growth outlook will improve, while the long term outlook will collapse.

6. Rating downgrade

There is a fairly high probability that South Africa will receive a rating downgrade, to "junk" status in 2016. Should this happen, the rand will likely blow out, as will bond yields. Namibia will almost undoubtedly be downgraded alongside South Africa. This may precipitate many of the other shocks mentioned above. In addition, it will cause Namibia a great discomfort when it comes to rolling the first Eurobond come 2021. This is a serious concern, which needs to be planned for now.

7. Idiosyncratic ("Zuma risk")

Finally, the region possesses great idiosyncratic risk, which is by nature, impossible to model. 2015 has illustrated the weaknesses and incompetence of key leaders in our southern neighbour, as well as the unpredictability thereof. This presents an unknown risk to the region and the CMA currency. Unfortunately, we simply cannot know what will happen next.

Outturn of 2015

The year 2015 has been one of more negative fortunes than the preceding year. While things have not fallen apart, tears in the fabric of the Namibian economy have emerged, the extent of which will likely play a major role in the years ahead. Much of these tears have been imported from Namibia's ever more fragile neighbour, South Africa. As our largest trading partner South Africa's fortunes have a direct effect on the Namibian economy. Growth in the most industrialised country in Africa has been slowing for a number of years and is estimated to have fallen to 1.4% in 2015, the lowest level since 2009. This is well below global growth which has also been coming down with each update of the IMF's World Economic Outlook, and is now expected to have fallen to 3.1% in 2015. The recovery in the US showed mixed signals and ultimately the country's economy did not perform as well as expected with the first interest rate hike in almost a decade postponed to the last MPC meeting of 2015. Europe managed a fragile recovery to evade a triple dip recession in 2014 registering growth of 0.9%, with growth expected to register 1.5% in 2015.

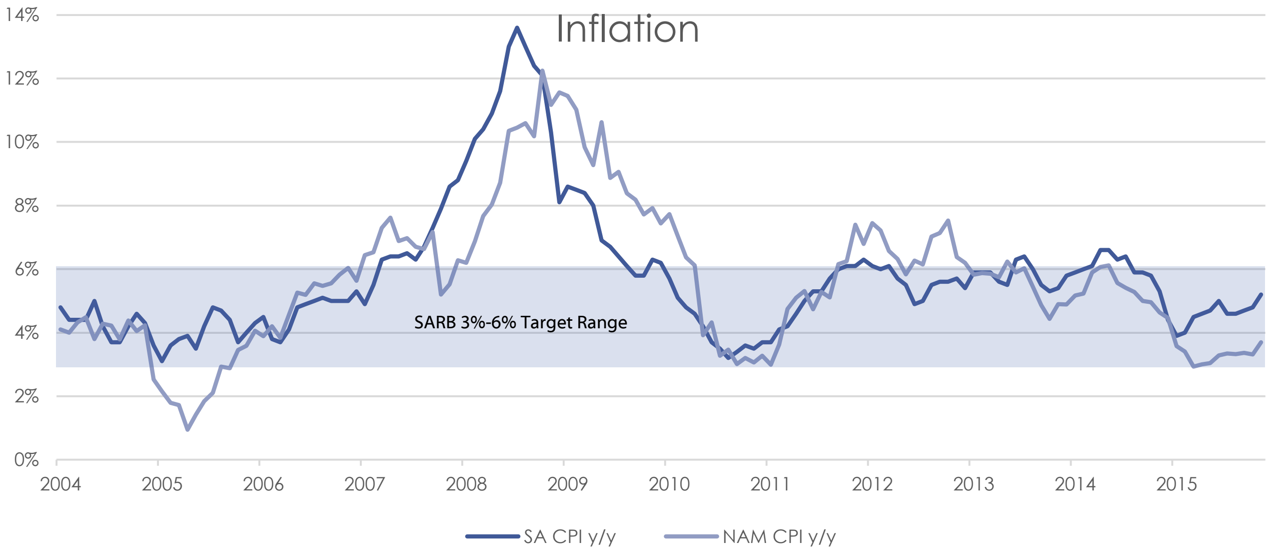
Emerging markets have largely felt the brunt of tighter monetary policy in the US, depressed commodity prices, and a weak global recovery leading to a flow of funds out of these economies. The MSCI emerging market index was down 16.8% for 2015 to its lowest yearly close since 2008. Growth in the index has been stagnant for most of the last five years, as commodity prices peaked and declined. Last year marked the first year of net fund outflows from emerging markets in almost three decades, highlighting extremely low confidence in the group of countries as a whole. For the most part South Africa fared well during the first half of the year, with the Rand depreciating by only 5% against the Dollar, compared to an 8% decline in the Euro versus the Dollar. The second half of the year was however characterised by a steady slide in the value of the Rand as expectations of an interest rate hike in the US ramped up. The decline in the value of the Rand reached a climax in December when President Jacob Zuma removed the respected Minister of Finance from his post and replaced him with a relatively unknown former mayor, resulting in the Rand closing the year down 34%.

Namibia kicked the year off with a new President and a cabinet reshuffle, accompanied by an expansive budget that saw expenditure increase by 7% off of an already elevated base. This marked the continuation of expansionary fiscal policy that was employed after the 2008 financial crisis to minimise the knock on effects of the crisis on the Namibian economy. Policy which started out as counter-cyclical has, as the years went by, turned decidedly pro-cyclical with the result being a large increase in government spending, repeated budget deficits, and a large increase in government debt. Alongside this expansionary fiscal policy, the Bank of Namibia ran expansionary monetary policy with interest rates near historic lows spurring a rapid increase in private debt. Namibian government debt has increased to approximately 35% of GDP at the current exchange rate which brings it up to the prudential limit. This is largely due to a second Eurobond of U$750 million being issued in October of last year as well as a large increase in domestic debt issuance and domestic currency debt issuance in South Africa. Private debt has increased by close to N$10 billion in 2015, much the same as in 2014, although this measure is growing more slowly than before signaling a possible normalisation in the rate of growth going forward. Contrary to our forecasts, and primarily due to the large increase in public debt over the last few years, the Bank of Namibia raised benchmark interest rates by 50 basis points during the year. This mirrored the steps taken by the South African Reserve Bank, not in timing but in size.

Within this backdrop of stimulus Namibia is set to record reasonable growth for 2015, however sees a fairly sizable growth step-down when compared to preceding years. The primary reason for this is a slowdown in many parts of the economy off the extremely high base created in the boom years between 2010 and 2014. Growth for 2015 is expected to register 3.3%, with construction seeing its first contraction in six years, as the high base unwinds.

The expansive budget for the year once again saw above inflation wage settlements for civil servants which has, along with increases in private sector wages and low interest rates, driven consumption growth within the country once again. Thus wholesale and retail trade remained a large contributor to overall GDP in 2015.

Inflation remained low in 2015, averaging 3.4% for the year, driven largely by a decline in oil prices during the end of 2014 and throughout 2015. Anecdotal evidence suggests however that many Namibians have experienced inflation of well above this level.



Source: NSA, Stats SA, IJG Securities

Expected Growth Rates, 2015

Real GDP Growth Rates	Expected Growth, 2015
Industry	**2015**
Agriculture and forestry	-11.0
Livestock farming	-12.0
Crop farming and forestry	-9.5
Fishing and fish processing on board	4.0
Mining and quarrying	2.4
Diamond mining	-6.5
Uranium mining	-18.1
Metal ore mining	78.5
Other mining and quarrying	7.0
Primary industries	**-0.7**
Manufacturing	2.6
Electricity and water	4.0
Construction	-12.0
Secondary industries	**-2.0**
Wholesale and retail trade, repairs	2.0
Hotels and restaurants	8.5
Transport, and communication	10.5
Financial intermediation	6.0
Real estate and business services	6.1
Community, social and personal service activities	1.7
Public administration and defence	8.5
Education	4.0
Health	1.0
Private household with employed persons	2.5
Tertiary industries	**5.3**
All industries at basic prices	**2.8**
GDP at market prices	**3.3**

Source: IJG Securities

IJG forecasts and calls for 2015

Call	HIT/MISS	RAG	Notes
• Brent crude to remain between U$45 and U$50 in H1 2015.	Partial hit		Brent remained supressed, and fell further.
• ZAR to stabilise and retrace to 10.8-11.0 to the US dollar by Q3 2015.	Miss		All currency forecasts were way out
• Namibian inflation to decline to 4.1% in June 2015, before bouncing back to 5.4% by year end.	Partial hit		Inflation declined more than expected.
• Namibian inflation to average 4.7% in 2015, 5.8% in 2016, 6.0% in 2017, 6.1% in 2018 and 6.2% in 2019.	Miss		IJGs forecasts remained amongst, if not the best, in Namibia.
• Euro-Dollar parity to be seen in 2015 or Q1 2016.	Partial hit		We came within 4.6% of parity in March 2015. Not quite what we expected, but very close.
• ECB QE to extend beyond Q3 of 2016, interest rates to remain on hold till end 2016 and beyond.	Hit		On track for a hit
• US interest rates to remain unchanged through first three quarters of 2015.	Hit		Excellent hit on this somewhat bold call.
• South African inflation to fall to below 4% in the first half of the year.	Hit		South African inflation fell to 3.9% in February 2015
• Rand to appreciate to 11:1 to the US dollar and the Euro by year end.	Miss		All currency forecasts were way out
• SARB to cut rates in Q2 or Q3 of 2015.	Miss		Big miss. Weaker than expected exchange rates lead to interest rate increases rather than decreases.
• BON to keep rates on hold through 2015.	Miss		Big miss. SARB and FX calls lead to interest rate increases in SA. Namibia followed.
• Budget expenditure increase of 15.2 percent in 2015/16	Partial hit		Expenditure growth slowed by more than expected, largely due to the change in minister in our view.
• Expenditure growth to be matched by revenue collection growth	Partial hit		Revenue growth is also expected to slow, perhaps by more than expected
• Deficit is to remain unchanged at N$7.6bn.	Partial hit		A sizable deficit remains in place, however may be somewhat larger than expected
• Strong revenue collection from corporate and personal income tax, as well as VAT receipts	Partial hit		Personnel income tax collection is likely to dissapoint. VAT holding up well.
• Major revenue risk from SACU receipts due to weak SA economy	Hit		
• Risk to forecast revenue collection from and mining taxes due to commodity price weakness.	Hit		
• We estimate that the economy grew by 6.8 percent in real terms in 2014, driven by construction.	Hit		
• Growth to remain strong in 2015, at 5.7 percent.	Expected miss		Growth is expected to be low in 2015, given the high base set in 2014.
• Driven by construction, as well as gold production, beverage production, chemical and metallic mineral production	Expected hit		
• Longer term, growth is expected to remain strong at 5.1 percent in 2016, 5.3 in 2017, 5.1 in 2018 and 4.6 in 2019.	Expected miss		We no longer feel this is the most likely outcome. Growth is expected to slow
• Long term growth to remain driven by construction as well as completion and ramping up of mining sector projects.	Expected partial hit		
• The balance of payments is expected to remain under sizable pressure until 2016	Hit		
• The reserve position of the country stands to weaken further both in Namibia Dollar and hard currency terms.	Hit		

Key Themes for 2016

2016, like most years, is likely to be defined by a number of key themes. In our view, some of the most noteworthy for Namibia are listed below.

Fiscal position of Government

In 2010, in order to stave off frosty headwinds emanating from the advanced economies of the northern hemisphere, particularly, Namibia embarked on a programme of fiscal expansion, running some of the largest fiscal deficits in the country's short history. Initially this expansion took the form of an accelerated public works programme, but fast morphed into a general major increase in expenditure, much of which was constituted within the operational budget, and recurrent in nature. As the economy regained its feet following the global recession in 2009, this expansive expenditure moved from counter-cyclical policy, to pro-cyclical policy. This pro-cyclical fiscal policy was coupled with pro-cyclical monetary policy as well as abnormally strong foreign direct investment, which together lead to abnormally high growth rates, and the typical demand-side inflation one expects within an overheating economy.

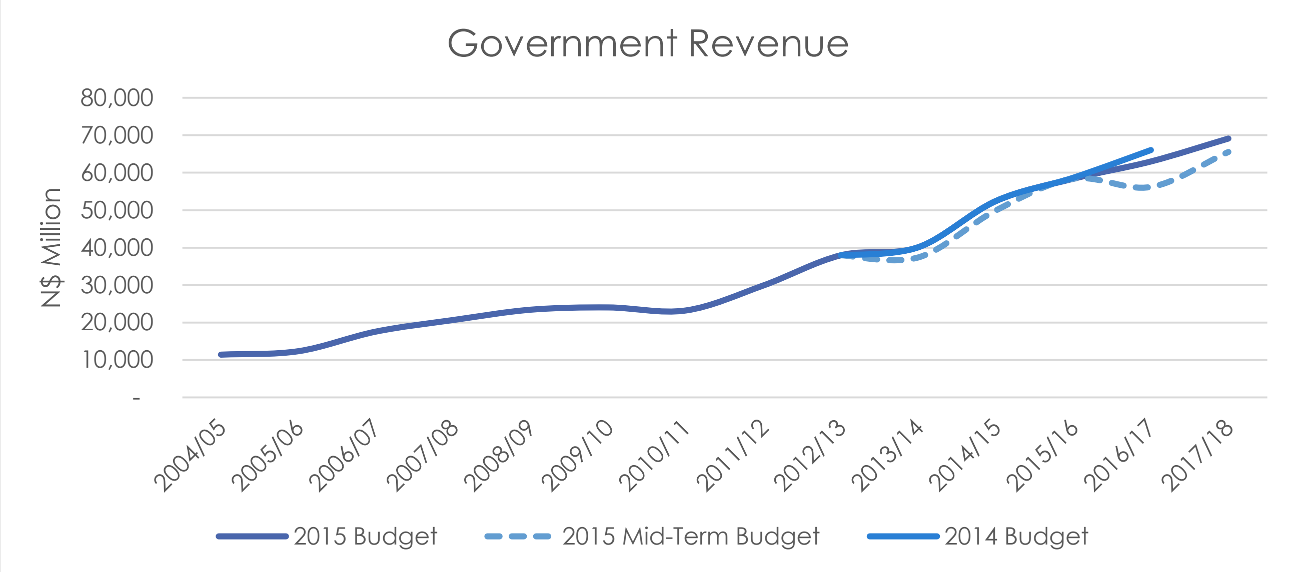
Revenue

Government revenues have shown impressive increases over the past decade, driven by a number of factors. A fast expanding economy from 2010 to 2014 drove major increases in a number of key revenue lines, including VAT collections, personal income tax and corporate tax. In addition, major improvements in tax administration, partially led by the efforts of Sam Shivute, saw increased revenue collection in key areas, particularly personal income tax. These efforts saw a widening of the proverbial tax net, and a reduction in tax evasion.

Over the past 10 years, revenue has grown at an average annual rate of 17.7%, well in excess of nominal GDP growth over the same period, which grew at an average annual rate of 12.8%. As of 2014, the single largest contributor to revenue was "Taxes on International Trade and Transactions", made up of SACU receipts, registering approximately 36% of total revenue collected, according to the latest figures from the Ministry of Finance. Thereafter, VAT and personal income tax made up the second and third largest revenue sources, at 21 and 20% of the total, respectively. Company taxes made up roughly 14% of total collections, with various tax and non-tax revenue sources making up the remainder of the total N$50 billion worth of revenue collected, as per the preliminary figures for the year.

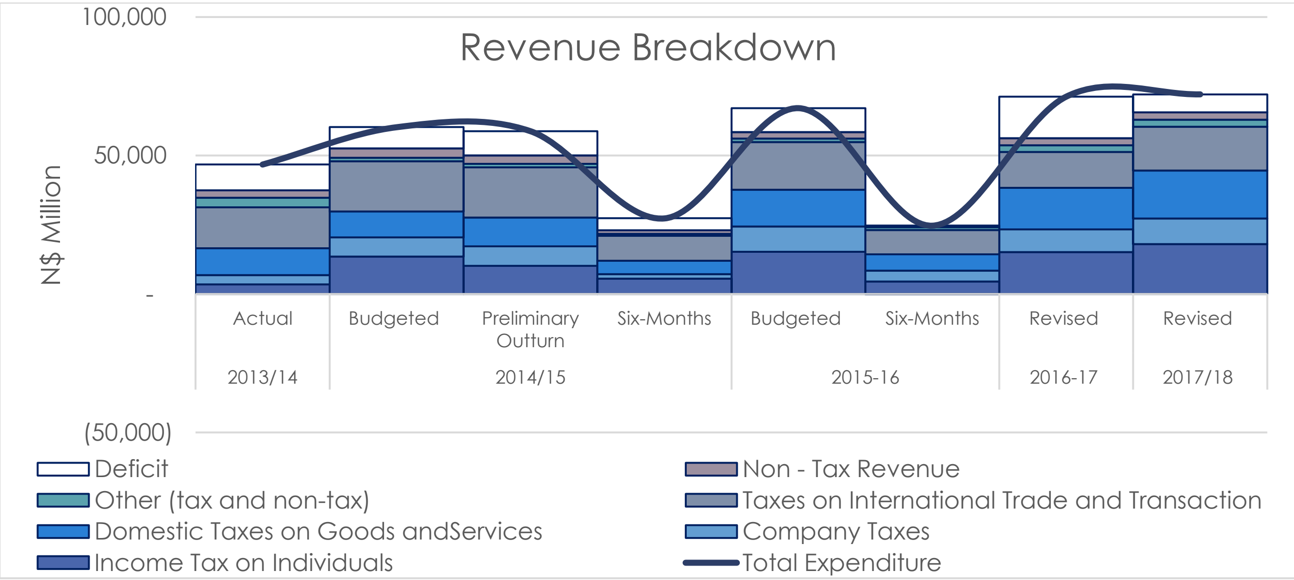
In the recent mid-term budget, a major revision to the revenue outlook has been seen, with revenue expectations (and actuals) for the five years from 2013/14 to 2017/18 all revised down, with the exception of 2015/16. The lack of downward revision in the current financial year is peculiar and ambitious, given macroeconomic conditions in the country, preliminary collection figures and the ambitious growth rates expected in certain revenue lines (personal income tax, for example, expected to expand by 49.3% in 2015/16 when compared to the preliminary outturn for 2014/15).

	2013/14	2014/15	2015/16	2016/17	2017/18
Revision (2015 Mid-Term Budget, from 2015 Budget)	-6.8%	-4.8%	0.0%	-10.8%	-5.2%



Source: Ministry of Finance, IJG Securities

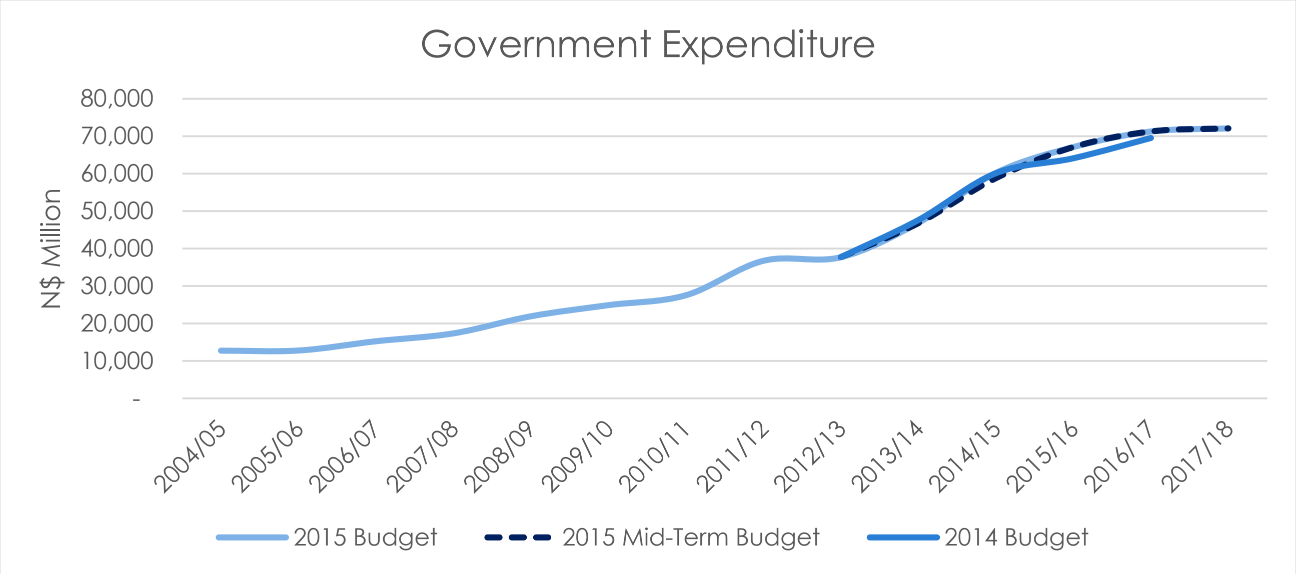
Going forward, we expect to see Government revenue come under notable pressure, for almost all of the primary collection sources. What with the economy slowing off a high base, largely off the back of weakening external factors, commodity price weakness and a winding in of stimuli measures, personal income tax, corporate tax and VAT collections can all be expected to slow. As commodity prices tumble, mining companies' profits are likely to come under pressure, thus reducing profit shares taken by Government (either via mining taxes on profits, and in the case of Namdeb, particularly, dividends). In addition, the volume of production is likely to come under pressure as miners can be expected to wait out low prices, and increase production only once prices recover (this is already seen in the uranium mining industry, and is expected amongst the diamond miners shortly). Reduced production can be expected to reduce turnover, and thus royalties for Government. On the trade side, over-payments by SACU in recent years will put notable pressure on revenue collection by Government, as an effective repayment of approximately N$3 billion is expected in 2016/17 to cover over-payment in 2014/15. This repayment will account for approximately 5% of revenue in 2015/16, and when coupled with the other sources of revenue slowdown or contraction, will put severe pressure on the budget deficit and expenditure envelope if not carefully managed.



Source: Ministry of Finance, IJG Securities

Expenditure

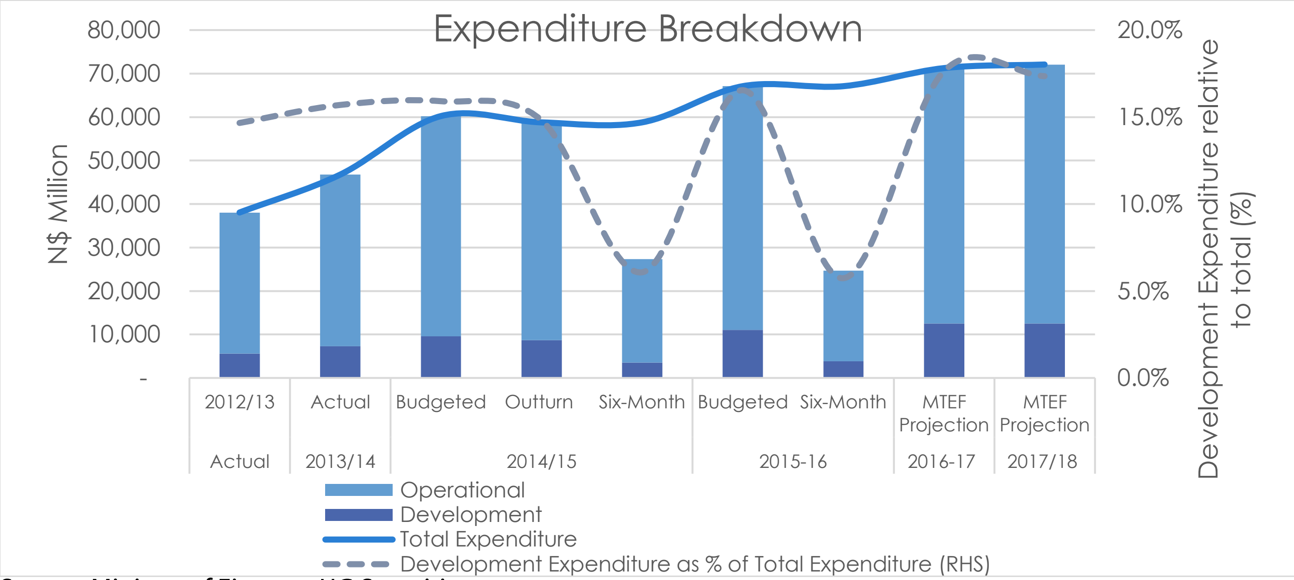
Following a number of years of expansive budgets, the Minister of Finance has emphasised, repeatedly, the need for fiscal consolidation. This is a welcome step, given the size and nature of the deficits run since 2010. However, despite efforts to rein in expenditure, the fund outflows from the Government coffers appears to continue unabated, illustrating the downward-sticky nature of the fiscal envelope. Much of the reason for this is the now sizable recurrent expenditure envelope of Government, which grew extensively through the “good years” when an expansive budget was being pursued. Unlike more conventional counter-cyclical budgets, the budget of Namibia saw major recurrent increases, largely in the form of sizable increases in the civil service wage bill (amongst others), which is now, predictably, proving hard to roll back.



Source: Ministry of Finance, IJG Securities

Over the past ten years, expenditure has grown at an average rate of 18.3%, well above the nominal GDP growth rate over the same period of just 12.8%. This illustrates the fact that Government is becoming an ever larger player in the domestic economy, an unsustainable situation given that most of the funds used to sustain Government are derived from sources external to Government.

With regards to the nature of expenditure, despite efforts to keep development expenditure at approximately 20% of total expenditure, lower execution rates in the capital budget tend to result in lower development budget expenditure than desired. Over the past five years, development expenditure has rarely exceeded 16% of total expenditure. In some ways, this illustrates a story of a bloated civil service being funded off the back of “savings” derived from under spending on capital projects.



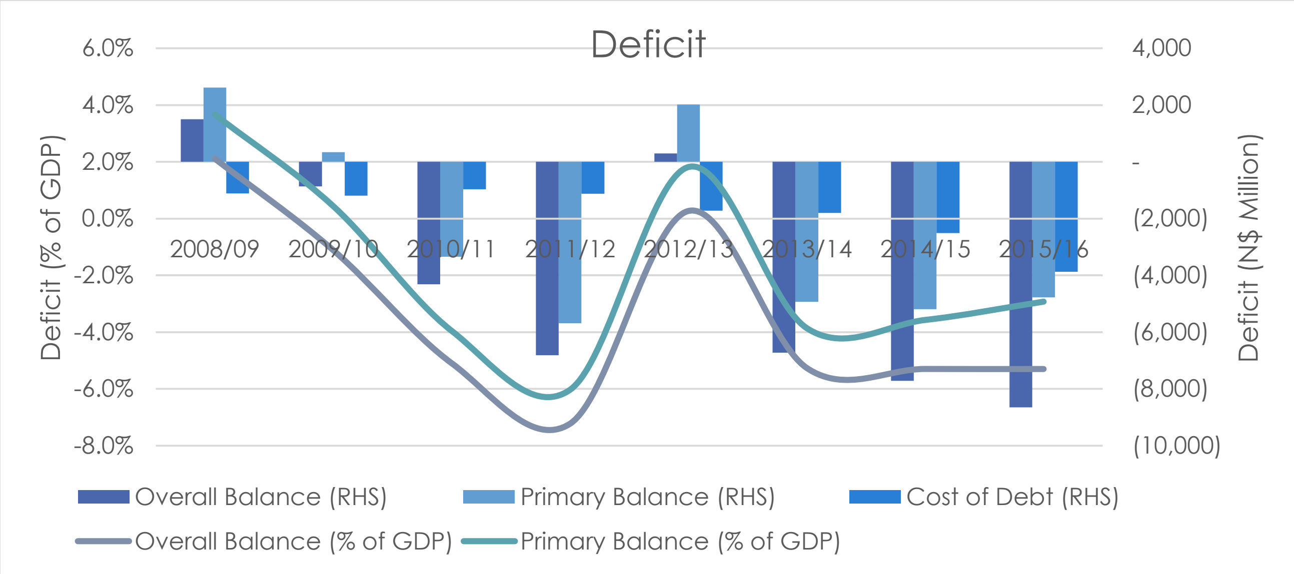
Source: Ministry of Finance, IJG Securities

The nature of the development budget expenditure, is, much like the overall budget, somewhat concerning. Little expenditure, when compared to the total expenditure envelope, goes to development, or capital, projects, and what little does, is rarely spent on critical infrastructure.

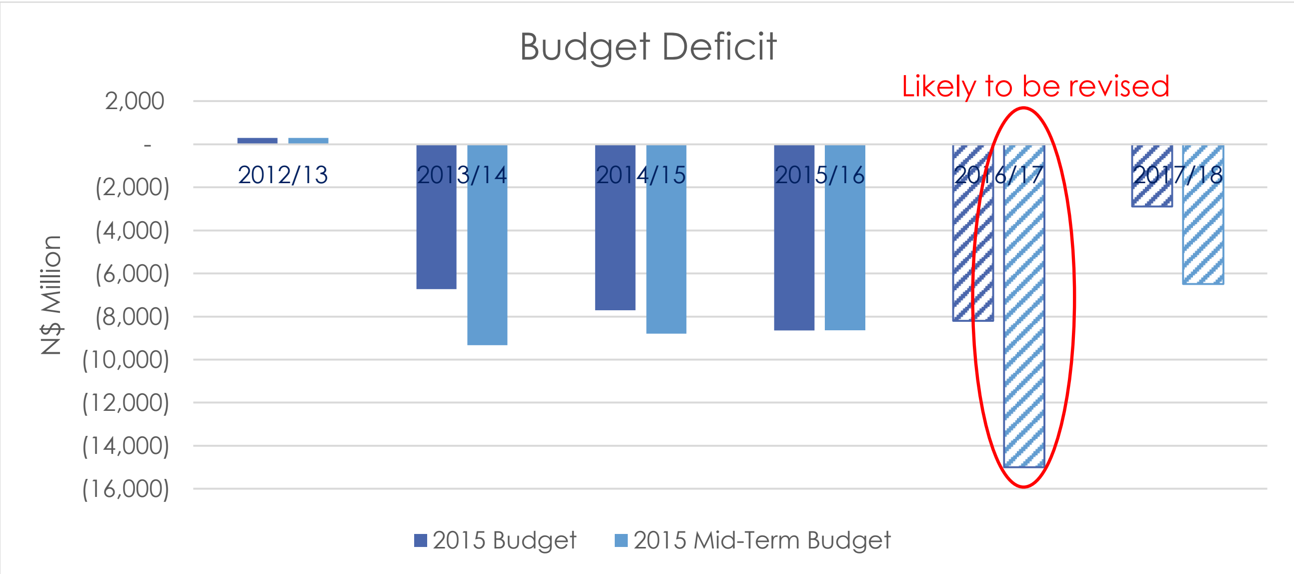
The recent mid-term budget speech talks about notable expenditure cuts in the 2016/17 and 2017/18 financial years, particularly, however, the figures contained within the budget review and policy statement do not show similar declines, unlike the revenue figures. This is somewhat concerning, however the inconsistency is currently thought to be on account of expenditure revisions not yet being finalised, but illustrates the challenges surrounding the reduction of in growth in Government expenditure.

Budget Balance

Over the period between 2010 and the end of 2015, the budget deficit (total) is expected to average 4.7% of GDP, while the primary deficit can be expected to average 3.1% of GDP. While not excessively alarming in and of themselves, the average deficit for the past five years hides three important factors. Firstly, had it not been for major underspending in 2012/13, the average deficit for the period would have been in the region of 5.6% of GDP, and the primary balance in the region of 4.1% of GDP. Secondly, abnormally strong nominal GDP growth has been seen over the period 2010 to 2014, meaning that both the deficit, and the stock of debt of the country have been artificially low when compared to GDP. In addition, much of this growth has been consumption based, led by expansive policy. By nature this is transitory value-added activity, and may well unwind as we see policy tightening; and finally, the deficit figures do not adequately capture the on-going “investment losses” incurred as a result of the devaluation of the hard currency liability to which Government has become exposed (unhedged) via the issuance of Eurobonds in 2011 and 2015.



Source: Ministry of Finance, IJG Securities



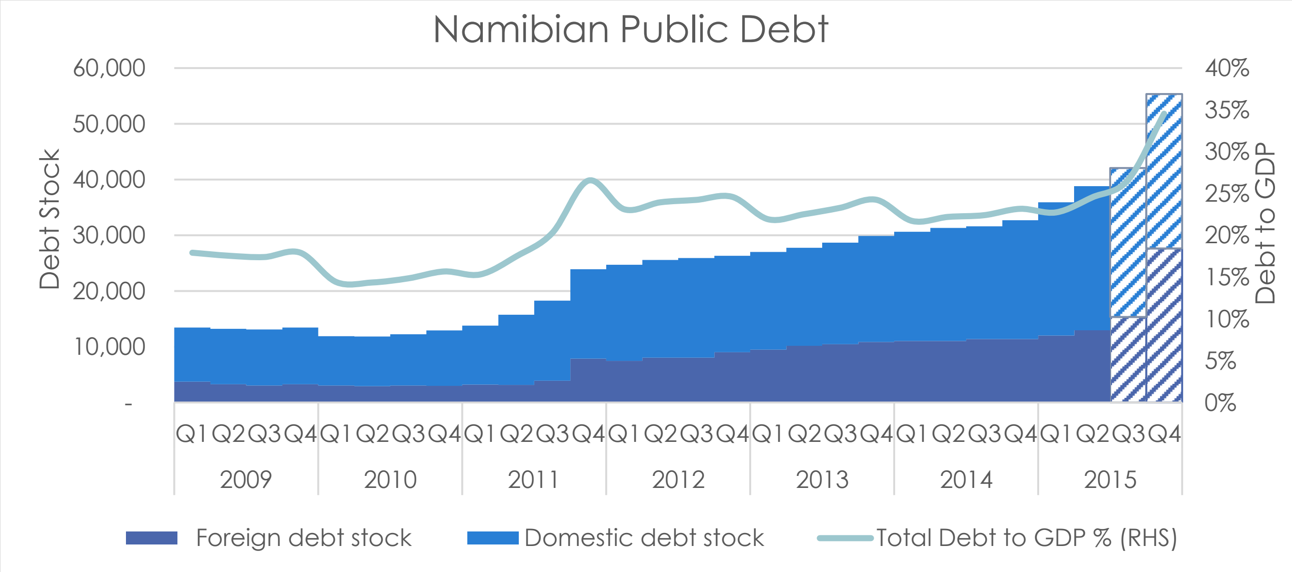
Source: Ministry of Finance, IJG Securities

Debt

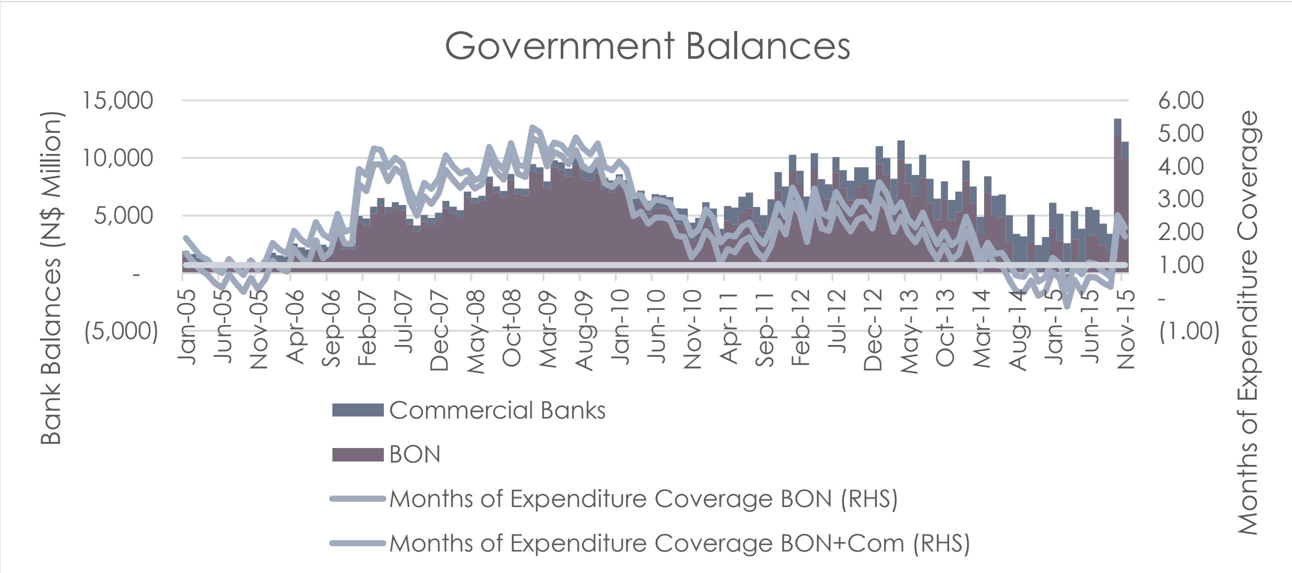
After a number of years of expansive budgets, Namibia's debt to GDP ratio surpassed 35% of GDP for the first time at the end of 2015. This was hugely exacerbated by lower than expected revenue collection, as well as the depreciation of the rand vis-à-vis the US dollar and other major currencies. Rand depreciation caused a major rerating of Namibia's un-hedged hard currency debt. As a result, in the space of just 12 months, it is estimated that public debt has increased by over 65%, and over N$20 billion, to a total of N$55 billion.

It should, however, be note that a large amount of the new debt issued over the past year (approximately half) is made up of the Eurobond issued in October, to the tune of approximately N$10 billion. The Government was forced to issue this hard currency debt in order to protect the crumbling external position of the country, after an extended period of fiscal and monetary stimulus that drove strong growth in consumption activity, and strong demand for imports. As the external position weakened, the risk of a rating downgrade increased to the point that the Ministry of Finance stepped in and borrowed a large chunk of funds on the international market, massively increasing the country's hard currency debt, but thankfully staving off a rating downgrade. While sizable in nature, the funds raised have not been spent (in whole), but are designated to protect the country's external position from the ongoing deterioration seen over recent years. As such, it is assumed that the funds remain in hard currency, thus their value will have appreciated in Namibia Dollar terms.

While the stock of Government debt is still relatively low, the relatively high cost of servicing this debt in Namibia, when compared to many other nations, means that the country's debt servicing cost is now well in excess of many more indebted nations, when compared to GDP.



Source: Ministry of Finance, IJG Securities



Source: Ministry of Finance, IJG Securities

Outlook

Based on the deterioration of the fiscal position, fiscal consolidation is now desperately needed, and the indications from the Ministry of Finance is that this consolidation will now start to take place. The good news, however, is that much meat remains on the bones of the budget, and better "bang-for-buck" expenditure can certainly be found with a simple reprioritisation of expenditure towards key projects. Moreover, the privatisation of some public asset would help to free up some more liquid capital. Finally, allowing more private investment into key revenue generating infrastructure projects will remove much of the infrastructure pressure from the shoulders of the state, and with the new PPP unit in the Ministry of Finance, this appears to be starting to happen.

International ratings

There is no doubt that international ratings agencies will play a larger part in the outlook for South Africa and Namibia in 2016 than they did in 2015, or possibly since independence for that matter. Emerging markets (EM) have been under pressure for a number of reasons. Commodity price declines, a decrease in international liquidity due to the end of quantitative easing in the US, as well as country specific factors such as political instability and infrastructure reliability have led to the first net outflow of funds from EM countries, as a group, in 27 years. South Africa, and Namibia by extension, has experienced a 33.69% drop in the value of the Rand in the space of just one year. RMB South Africa attribute 59% of this drop to the commodity bear market and US Dollar strength. Thus 41% of the year's currency depreciation is captured by South Africa specific factors such a loss of political confidence and diminishing growth forecasts.

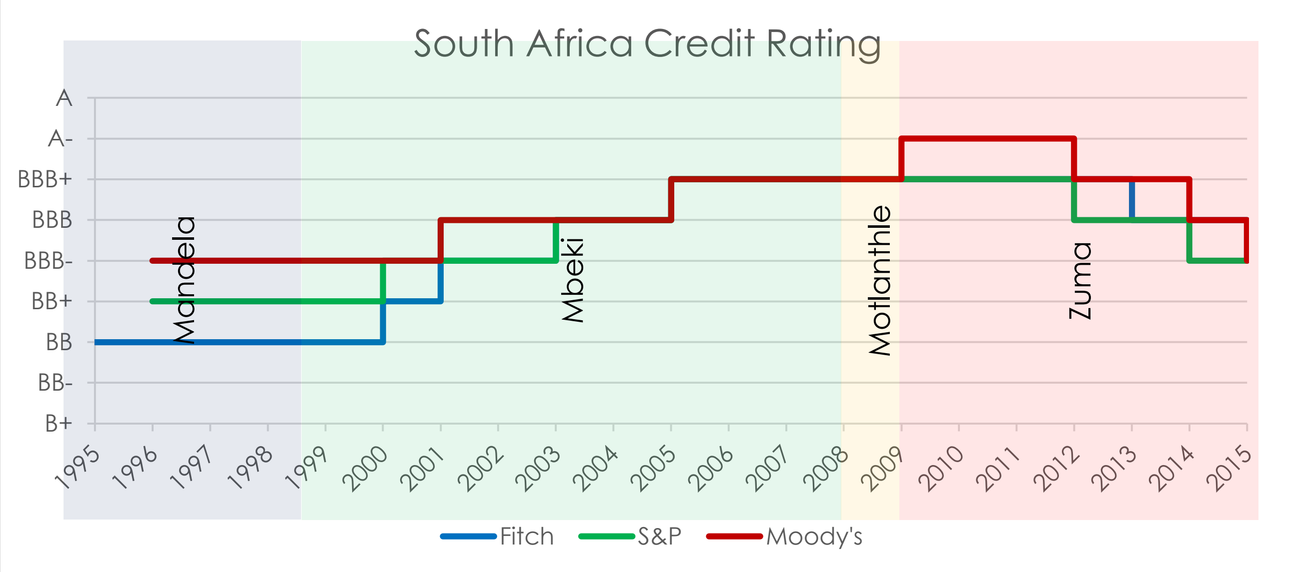
The series of events between the 9th December and 14th December, 2015, regarding the removal of South African Finance Minister Nhlanhla Nene and eventual reinstatement of Pravin Gordhan as the new Finance Minister placed South Africa square within the sights of the international ratings agencies. President Jacob Zuma shocked the world with the removal of respected finance minister Nhlanhla Nene on Wednesday the 9th of December, replacing him with the unknown David "Dez" van Rooyen. The Rand reacted violently to the news, falling 4.5% almost immediately and 9.8% by the Friday following the event. Clearer heads seem to have prevailed when on Sunday the 13th of December President Zuma reinstated former Finance Minister Pravin Gordhan. These events played out within days of Standard and Poor's downgrading South Africa's outlook from stable to negative, and Fitch Ratings downgrading the sovereign credit rating to one notch above "junk". Thus putting the cherry on the cake.

The events of Wednesday the 9th of December led to a sharp decline in various sectors of the stock market, most notably financials. The big four banks lost a combined R127.8 billion in market cap on the JSE over the two following days with First Rand falling 21.9%, Standard Bank and Barclays Group both falling 17.1%, and Nedbank Group falling 15.7%. These four banks were subsequently downgraded by Fitch Ratings on the 13th December. The implications of this are stricter lending standards, higher funding costs for banks, and by implication an increase in interest rates.

The following comments were made by Standard and Poor's ratings when downgrading the South African outlook.

> *"The negative outlook reflects our view that GDP growth might be lower than we currently expect; for instance, due to persistent electricity shortages, continued weak business confidence, or labor disputes escalating again.*
>
> *"The outlook also reflects our view that fiscal flexibility might reduce owing to contingency risks from state-owned entities with weak balance sheets," –Standard and Poor's*

These comments, made before the finance minister debacle, accurately summarised the then prevailing situation in South Africa. The outlook for South Africa has subsequently deteriorated further due to a loss in confidence in the leadership of the country. Indeed, GDP growth is now in danger of going negative, electricity generation challenges remain, and business confidence is at an all-time low while labour unrest remains a probable theme for 2016. Thus further ratings downgrades are probable, or at least more probable than they were before December last year.



Source: IJG Securities

Should South Africa experience a sovereign ratings downgrade to "junk" status this will affect the Country Ceiling of the Common Monetary Area which includes Namibia, Lesotho, and Swaziland. When Fitch Ratings downgraded South Africa's sovereign rating to BBB-, one notch above "junk", it downgraded the Country Ceiling of the Common Monetary Area by two notches to BBB. This is one notch above Namibia's current sovereign rating of BBB-. Thus a further downgrade of South Africa's rating would in all probability drag Namibia's rating down with it. As South Africa is our largest trading partner and the Namibia Dollar is pegged to the Rand we are unlikely to maintain a sovereign credit rating higher than that of South Africa.

The implications of a ratings downgrade to "junk" differ from country to country but in general are characterised by an outflow of funds, a fall in exchange rate, and stock market weakness. Indeed this is precisely what happened in Brazil in December 2015 and in Russia earlier in 2015. As the sovereign rating approaches "junk" status foreign asset managers who are not confined to a specific country, or who do not have "junk" mandates, tend to start unwinding their positions and repatriating their investments. These fund flows out of the downgraded country drive down the value of the currency. The cost of insuring government debt goes up and leads to a sharp rise in interest rates.

A credit ratings downgrade is highly likely considering the arguments above. This provides the basis for our interest rate forecast elsewhere in this Outlook. Six months ago, a ratings downgrade was a speculative possibility that was a worst case scenario projection for most forecasters. Now a downgrade is, for many, the most likely scenario. We feel that there is a possibility of avoiding a downgrade but then there is need for significant improvement in the economy, as well as leadership, in South Africa. Further stagnation, or even if things remain the same, will in all likelihood result in a ratings downgrade which is the last thing a struggling economy needs. The line in the sand will likely come in the form of the February budget, which will likely determine the rating agencies willingness to maintain the country's status as investments grade. However, the ice remains thin, and the challenges, heavy.

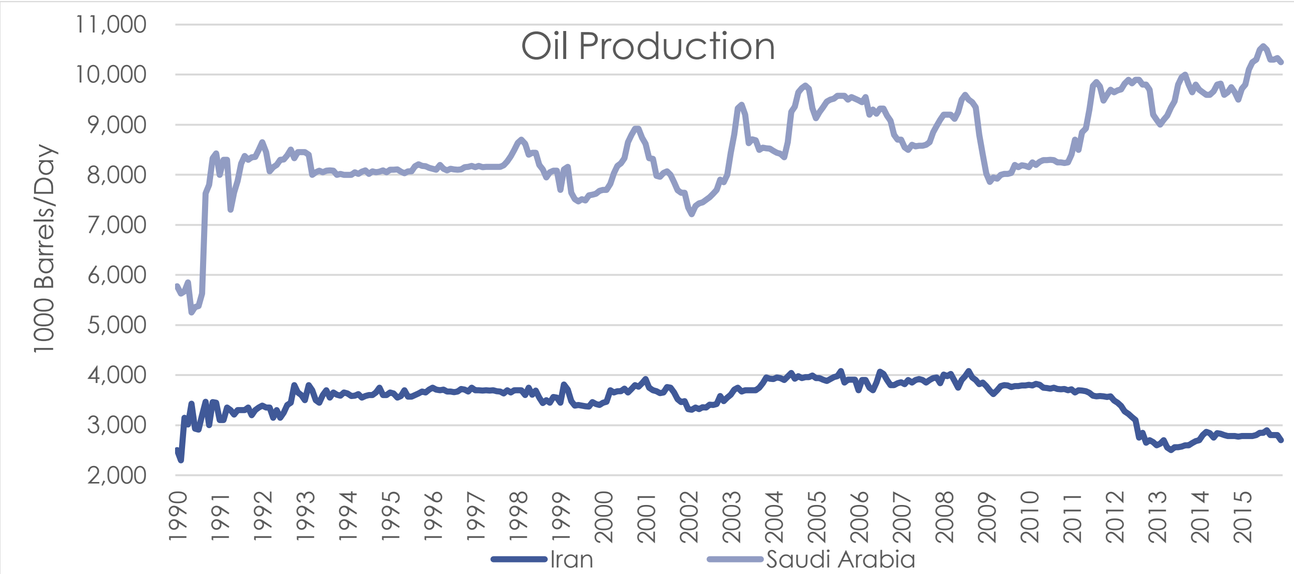
Commodity Prices

Oil

The collapse in the oil price seen over the past 24 months is due to fundamental changes in the oil market, driven by both demand and supply side forces, with supply dynamics being more significant. Increased production from the Middle East and the US, together with a decreased demand from China gives reason to expect oil prices to remain low in 2016.

The Middle East Geopolitics

Oil is used as a weapon within the complex geopolitics of the Middle East, and one being aimed without mercy by Saudi Arabia at its regional rival, Iran. Saudi Arabia was intentionally flooding the market by increasing oil production to constrain Iran prior to economic sanctions being lifted against them. The dynamics driving Saudi Arabia's oil policy is the sectarian rivalry between the Sunni of Saudi Arabia and the largely Shia Iranians. The United Nations announced that Tehran had met its commitments to curtail its nuclear program, a move that prompted the US to revoke sanctions against Iran exporting of oil. Looking forward, as long as Saudi Arabia continues to oversaturate the market together with Iran re-entering the market, oil prices is expected to remain low in 2016.



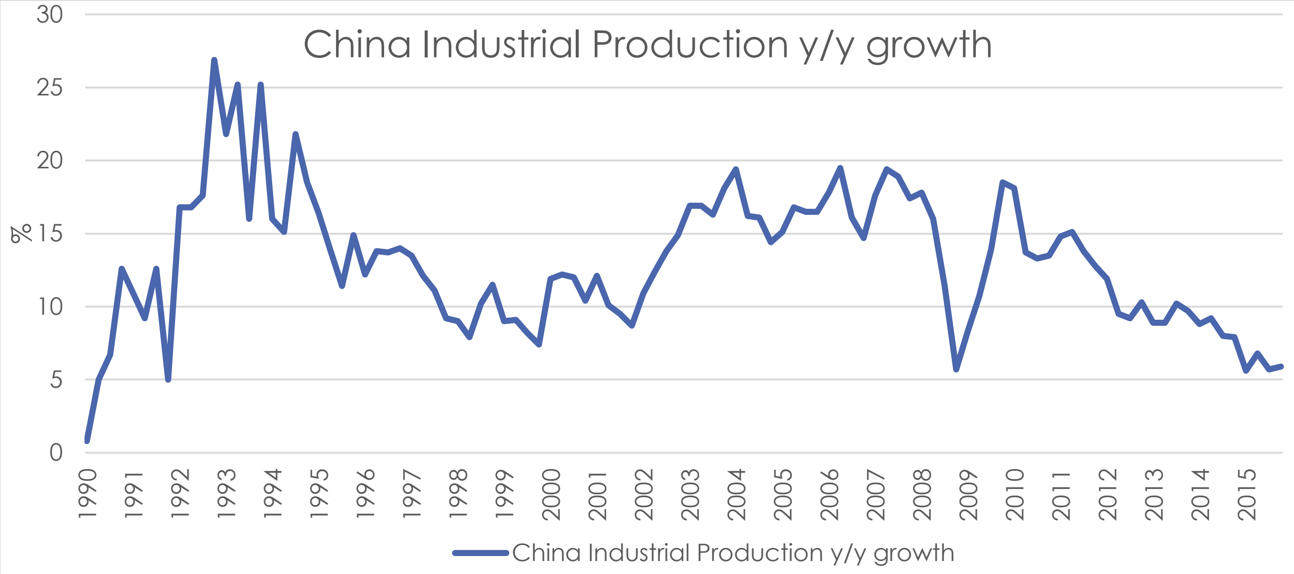
Source: Bloomberg

United States Production

The US has increased production over recent years, taking the country from a major importer to an exporter for the first time in many years. The US government has now lifted the export ban, implemented about 40 years ago, which will also contribute to an oversaturation of the global oil market. However, while the new legislation will increase oil exports, prices are unlikely to lower drastically, as from a global perspective, oil coming out of the US accounts for a very small percentage of the total production and it is small compared to Iran coming back to the market with much larger volumes now that sanctions have been lifted.

China Slowdown

China is one of the world's biggest importers of crude oil, so the Chinese economic slowdown will also have a major effect on global oil prices. China's economy has slowed in part because of a shift from being a manufacturing and exporting nation to a system that is more consumer driven, similar to the US. China's National Bureau of Statistics reported that the country's industrial profits fell significantly during 2015, signaling a continued Chinese economic slowdown in 2016. As a result, China's reliance on crude oil has fallen significantly, which is likely to negatively affect the demand for crude oil and therefore affect oil prices. The Chinese slowdown will absolutely be crucial in 2016 for oil as the country shifts gradually from a manufacturing nation to a consumer based economy.



Source: Bloomberg

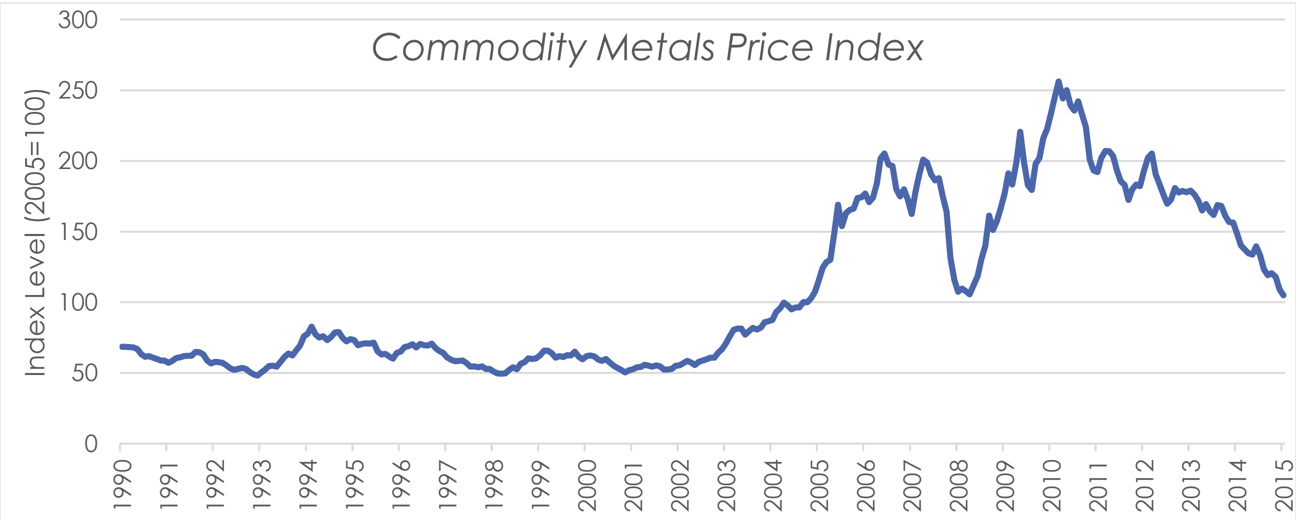
Balance of payment implications

The utility of trade balance data as an economic indicator depends very much on the country itself. The biggest impact is generally seen in nations with limited foreign exchange reserves such as Namibia, where the release of trade data can trigger large swings in their currencies. However, as the Namibian dollar is pegged to the Rand, the country is influenced on what happens in South Africa.

Although the price of oil has fallen significantly, the weakening of the exchange rate has offset the full price advantage that could have been achieved when importing fuel. The exchange rate's ongoing weakness might mean trouble for the fuel price if oil prices begin to recover, which would have a negative impact on the balance of payments as the import value would spike.

Minerals

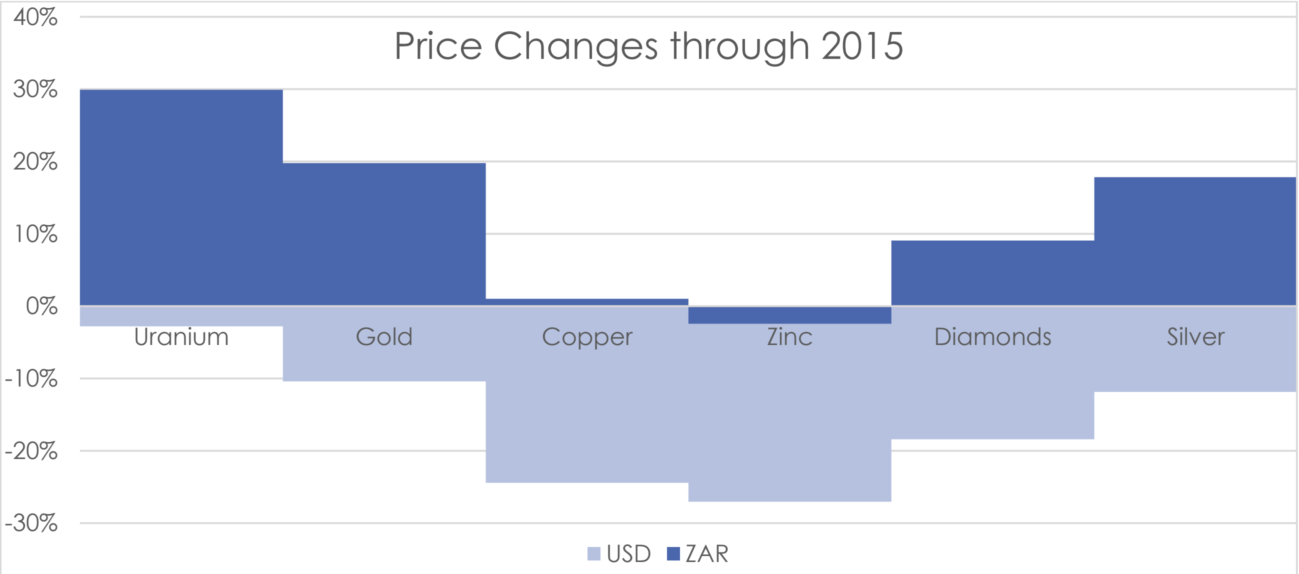
Global commodity prices have fallen significantly since 2011, following large price increases over the previous decade, with growth in global demand, particularly from China, driving up prices. The attractive prices led to a significant expansion of capacity resulting in higher production, including in Namibia. Prices were expected to decline as production increased and demand faded, but the sizes of the declines have been larger than what had been anticipated.



Source: Index mundi

Description: *Commodity Metals Price Index, 2005 = 100, includes Copper, Aluminum, Iron Ore, Tin, Nickel, Zinc, Lead, and Uranium Price Indices*

Namibia as a major exporter of resources, including copper, gold, zinc uranium and diamonds. Therefore, Namibia is directly affected by the demand and prices of these minerals. A slowing growth in China and a generally weak global economy resulted in the demand for commodities to fall, and therefore commodity prices. However, from a commodity price perspective, Namibia was protected to some extent by the rand-dollar exchange rate, as the weak rand softened the impact of low dollar prices. During 2015, the rand depreciated by 34.0% when compared to the US dollar, therefore, the rand based commodity prices for most of Namibia's key commodities remained reasonable throughout the year. Given that the exchange rate is expected to remain weak in 2016, it provides a silver-lining to the mining sector of Namibia



Source: IJG Securities, Bloomberg

Uranium

The uranium price has trended downward since the Fukushima disaster in 2011, and hovered below US$40 throughout 2015. One key element that kept uranium prices suppressed during 2015 was the lack of buying by US utilities. Despite an estimated 15 to 20 percent of uncovered requirements, many utilities refrained from buying uranium due to excess inventories. That said, in the shorter term, it will likely be US utilities that boost uranium prices as contracts are expected to open up after next year and new deals will need to be signed.

Idling reactors in Japan after the Fukushima incident left utility companies with millions of tons of uranium since they still had to honour their existing supply contracts. Japan restarted nuclear reactors at the Sendai power plant a few months ago, and about 40 of Japan's 54 nuclear plants will likely be restarted, but it will still take a while to work through existing inventories, before global demand picks up significantly. At a global level, utilities will need to secure roughly 20% of their uranium needs sometime between 2017 and 2018.

The major catalysts expected to move the uranium price in the coming years are depleting supply from stockpiles paired with existing uranium producers that are likely not able to meet the new demand coming into the market as old reactors are restarted and new ones constructed, particularly in China.

Gold

The gold price has not moved much after the interest rate hike by the US Fed in December, at a time when equity markets experienced their worst start to a year in history, which is typically a catalyst for the safe haven metal. Going forward, the price of gold is expected to remain lackluster as US inflation is expected to remain low. Gold is often thought of as an inflation hedge and as inflation is likely remain low for the time being, given the continuing slump in the oil price having a drag on fuel prices and other items in the consumer basket, the gold price will remain subdued.

The second factor is whether or not the current market correction will unfold in a market crash or if the investor panic underestimates the resilience of the global economy. As was seen in the past, safe-haven rallies are typically short-lived, but gold, which is seen as a store of value in times of stress, soars when markets go into a full crisis. The financial crisis in 2008 directed gold to a three-year bull market reaching an all-time high. At the moment there is no shortage of articles predicting another markets collapse, but there is also enough data proving that investors are merely overreacting to rather small bits of evidence in an environment of high volatility and risk aversion.

Thirdly, should the equity market not collapse, the likelihood of further interest rates hikes is high, enforcing the subdued pattern for gold. If rates rise, it increases the attractiveness of alternative investments which pay income and buoy the dollar, against a gold hedge.

Lastly, once a clearer direction of markets is established and what the Fed decides on interest rates, the market might refocus on demand dynamics to drive prices, but the underlying view is still very unclear. There has been a slight uptick in investors buying gold equity, but this is coming from a very low base following the sell-off in 2015 and purchases of actual gold in the form of jewelry remains low.

Diamonds

During 2015 prices of rough diamond price fell significantly, and major diamond miners have had to move swiftly to react to the weak environment by reducing supply to the market and cutting selling prices.

The current situation in the diamond industry started after the financial crises in 2008, when banks began lending large amounts of money to diamond cutters so that they could buy rough diamonds. While this allowed cutters and polishers to continue business, it ultimately resulted in rough diamond prices being higher than prices for polished diamonds. In other words, cutters were borrowing money to buy rough diamonds, but once they had polished the gems they were unable to sell them profitably.

According to a report released by De Beers, which compares global diamond demand in 2008 to what is expected in 2016, the US share in global diamond demand is expected to decrease from 40 percent to 35 percent. China’s share of global diamond demand will double from 8 percent to 16 percent, while India’s is expected to grow from 7 percent to 11 percent and Italy is expected to decline from 4 percent of global diamond demand to 2 percent. The Gulf region’s diamond demand will grow slightly from 8 percent to 9 percent, while Japan’s market share will continue to decline from 11 percent in 2008 to 9 percent in 2016. Market share is however of less relevant than actual market growth. Despite predictions of rough diamond supply shortages and possible declines in mining production, long-term prices depend on market growth.

Zink and Copper

During 2015, many zinc and copper mines closed down as the prices of these minerals fell. Along with those outright shutdowns, key players in these markets have been cutting production in 2015. Unfortunately, even these sizeable reductions in supply did not buoy the price of copper and zinc for long as high inventories and concerns about Chinese demand resulted in the prices remaining low.

Balance of payments implications

The increase in mining capacity in Namibia was triggered by attractive commodity prices, which has led to strong growth in the volume of mineral exports over the past 20 years. The subsequent price declines have so far had little impact on export volumes because most Namibian mines remained profitable, which was supported by the weak local currency. Exports of commodities like gold are expected to continue to grow over the next couple of years as additional capacity comes on line with the expansion of the B2Gold mine and as demand for the save haven commodity picks up.

Namibia’s imports increased significantly when commodity prices were still favorable, in line with the pick-up in demand for mining equipment during the construction of mines. As commodity prices have collapsed and the three major mines under construction are now complete or close to complete, we expect to see a pickup in exports.

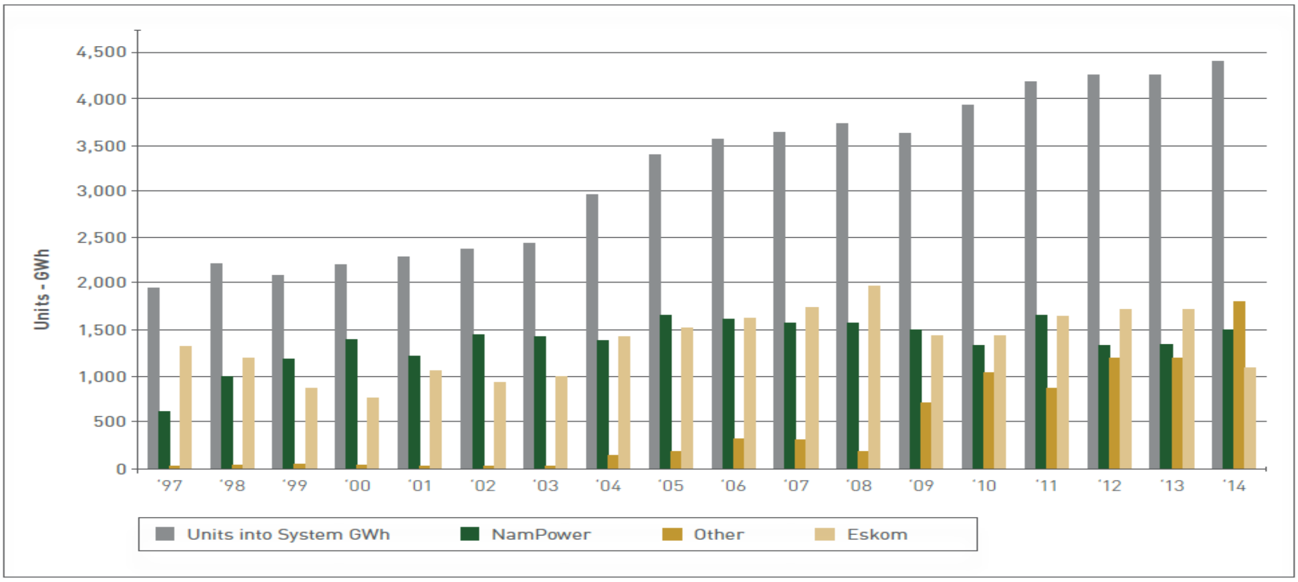
Energy

Current situation

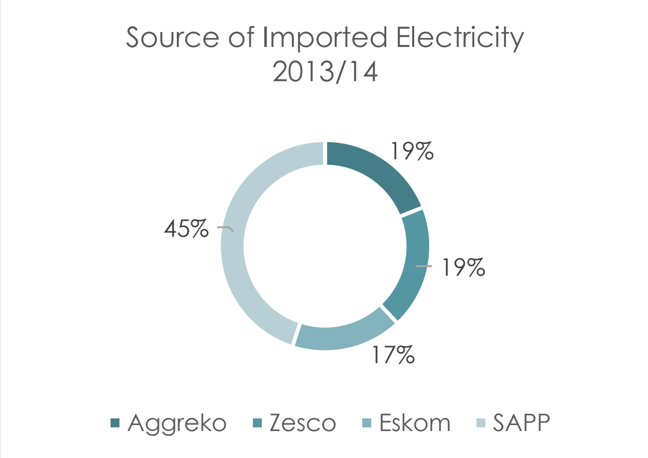
The Southern African region as a whole is currently in the midst of a power crises, with the region estimated to have a power generation deficit of approximately 4GW at peak demand. This has resulted in several countries within the Southern African Power Pool (SAPP) experiencing load shedding during 2015. The major cause of this is that the addition of electricity generation capacity has not being able to keep up with the rate at which demand has grown. Approximately 37% of people living in Southern Africa have access to electricity (World Bank, 2012), and thus there is substantial room for demand to grow as countries develop.

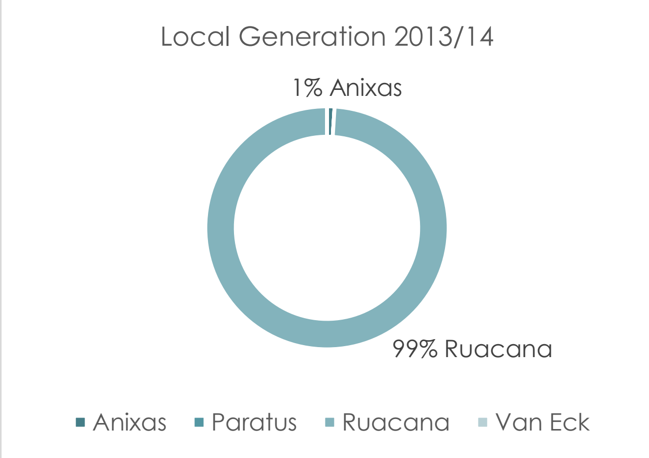
Zambia has been particularly hard hit by load shedding as the country generates much of its power through hydro plants, particularly on Lake Kariba, which generation capacity has been severely affected by drought. Current estimates suggest that Lake Kariba's water supply will only be sufficient to generate electricity until February 2016 unless exceptional rainfall is recorded. Current power generation is already being restricted to a fraction of total generation capacity due to the low water level. As the Lake is shared between Zambia and Zimbabwe for power generation purposes, it is unsurprising that Zimbabwe is suffering much the same fate. Both nations have been experiencing load shedding leading directly to economic strain within the countries. South Africa suffered widely documented load shedding during the first half of 2015 due to delays in infrastructure deployment. Botswana relies on electricity imports for roughly half of its usage as does Namibia. Thus there is an energy generation deficit within the region which has affected many of our neighbouring countries negatively.

It is worth noting that to date Namibia is yet to be plagued by load shedding or blackouts due in large part to the power purchase agreements (PPAs) in place with countries such as South Africa, Zimbabwe, Zambia, and Mozambique that allow us to import electricity from the region when necessary. At present Namibia generates roughly 40% of electricity usage locally and imports close to 60%, although these figures may vary from year to year depending largely on river flows through the Ruacana plant. Thus, we are heavily reliant on our distressed neighbours for electricity, although the relatively low peak demand in Namibia simplifies the task of negotiating PPAs as we need little power in relation to other countries within the SAPP. Current peak demand of around 525MW is a drop in the ocean within the greater power pool and has to a large extent been our saving grace as we are able to agree to PPAs of 50MW or 100MW which does not greatly affect the exporting country but serves as a substantial energy supply to Namibia.



Source: NamPower Annual Statements 2014





Source: NamPower Annual Statements 2014

Local generation capacity is dominated by Ruacana which has a peak output of 347MW. The Van Eck thermal plant in Windhoek has a reduced generation capacity of 90MW, although once the currently behind schedule refurbishment of the plant is complete, generation capacity will be restored to 120MW. The Anixas and Paratus plants add a combined capacity of 35MW but are classified as emergency stand by generators and thus only run on occasion, and at high cost. Adding to this generation capacity is the 4.5MW Omburu solar plant run by InnoSun. This plant is the first of its kind in the country and can be seen as a major step forward as it is the first time an independent power producer has supplied electricity to the Namibian grid. A second solar plant has recently been installed by HopSol, adding a further 5MW to the grid since mid-November 2015.

The decision to allow Independent Power Producers (IPPs) to contribute to the grid is a big step in terms of alleviating Namibia's reliance on neighbouring countries for electricity. A major benefit of allowing the private sector to contribute to solving the energy problem is that the private sector participants, or independent power producers (IPPs), finance the projects. Thus the financial burden is removed from government's shoulders while increasing electricity supply.

Outlook, 2016 and beyond

Namibia will continue to rely heavily on energy imports in 2016. Namibia is not in a position to provide for peak demand from local sources and is unlikely to be in such a position in the near future. While some of the local energy used at peak times is generated by Ruacana and supplemented by Van Eck, much still comes from the Southern African Power Pool (SAPP) through negotiated bilateral PPAs or from the pool directly. Various PPAs that supply our country with electricity have been successfully renegotiated by NamPower recently. These include agreements with ZPC and ZESCO in Zimbabwe and Zambia respectively. How reliable these agreements are will be determined by the ability of these countries to generate electricity from Lake Kariba, to a large extent. Should the present drought continue or the dam wall suffer further damage (a real possibility) it may limit the ability of these two countries to uphold the PPAs with Namibia. This may see Namibia become more reliant on the agreements with Eskom in South Africa as well as EDM in Mozambique.

The current duel PPAs with Eskom are likely to be ongoing although one of the agreements will terminate in March this year. The terminated agreement is expected to be renegotiated and rolled into the remaining agreement resulting in one longer term agreement. This may see Namibia draw up to 200MW of electricity from Eskom under the combined agreement. The current agreement does contain a clause that allows Eskom to limit the amount of power imported by Namibia should Eskom come under pressure for whatever reason. Whether the new agreement will contain a similar clause is unknown, but it remains likely.

NamPower is currently investigating the use of container generators to add up to 120MW of capacity to the grid by August this year. These generators are convenient as they are modular and quick to set up, but they are expensive as there are rental costs involved which accrue even when the generator is not in use. Additionally these diesel generators run on more expensive fuel than other sources of power. NamPower sees these generators as a short term solution only, bolstering the generation capacity of the country until such a time that longer term solutions are in place.

One such longer term solution that has been taken off the table for the time being is the Kudu Gas-to-Power project. The estimated cost of the Kudu plant is huge and would necessitate a large investment from government who are cash strapped as it is, with the expected economic downturn reducing the feasibility of the project. This has however left scope for a smaller medium term project to be undertaken.

One such project that has recently regained traction and may fill this space is the Xaris Energy project which proposes to install a 250MW gas powered plant near Walvis Bay. The initial tender process, completed in late 2014, was marred by controversy surrounding the manner in which the tender was awarded to Xaris. This seems to have passed with the project gaining support from the government in December 2015. The company released a press statement in January 2016 indicating that negotiations with NamPower regarding the project will resume and that implementation of the project will go forward. A substantial amount of work has already gone in to the project with costs amounting to US$30 million as explained below:

"While awaiting a signed PPA, we have progressed the development of the Project as far as possible towards financial close. We have largely completed the due diligence, GE has manufactured gas turbines for the Project and Excelerate Energy remains committed as our FSRU provider with its proven and innovative capabilities and supply solutions," – Hennie Steyn, MD Xaris Energy

The Xaris power plant should be cost effective enough to provide Namibia with electricity at cheaper rates than those paid for importing power from the SAPP. Additionally it should be able to provide a reliable base load, greatly reducing Namibia's reliance on electricity imports. While this is not the only medium term power solution currently being investigated by NamPower, it may be the first to be approved and implemented.

Additionally it seems that the Baynes hydropower joint venture between Namibia and Angola will be pursued in the future. This is a more long term undertaking with an estimated project timeline of close to nine years. The project will generate up to 600MW which will be evenly shared by the two countries. Feasibility studies and environmental impact assessments seem positive although a greater challenge may be to coordinate the project between the two countries as political interference will likely delay the process. At present this is not a bankable project then.

This year will see a myriad of different independent power producers enter the electricity generation space. Various solar offerings are planned as well as a wind farm near Lüderitz. The Diaz wind farm will generate 44MW of renewable energy if it is able to gain traction. The project has lost some steam due to a lack of agreement on purchase assurances from the Namibian government, although there is some evidence to the fact that it will go ahead in 2017. Additionally, approximately 65MW of solar power may be added in during the year from 14 licenses of 5MW each which are expected to be approved by the end of the first quarter in 2017. These licenses will be supplemented with one 5MW license to generate wind power. Various other tenders are in the process of gaining traction or have been delayed and as such will be revisited at a later stage.

One issue that NamPower has to contend with is how the addition of supply from renewables, such as those mentioned above, will affect baseload generation demand. Essentially, these renewables contribute electricity during the day and provide little supply during evening peak times and at night. Thus, there is a large step-up in demand which needs to be matched by supply which drops off before dark. The challenge is to seamlessly add supply from other sources of electricity as this happens. Generally these sources of power are difficult to switch on or switch off as needed with little or no moderation in-between. This is a major reason why each renewable source of electricity needs to be evaluated in terms of the whole and what it brings to the table.

Another negative effect of supplementing the grid with renewables is that the average cost of electricity produced by NamPower will go up as it needs to spread the cost of running baseload power stations over a reduced number of units of electricity sold. This will effectively reduce NamPower's income while not affecting the costs of production putting financial pressure on the organization. This could in turn lead to more expensive electricity for the consumer.

That said, 2016 should be an interesting year on the energy generation front and it remains highly unlikely that Namibia will experience loadshedding or blackouts of a serious nature. Thus we will see the same stable electricity supply that has been enjoyed in the past which should underpin business confidence in this regard.

Exchange Rates

The South African Rand is projected to remain subdued in 2016 given the combination of a strengthening US dollar, a decline in South Africa's investor confidence and the potential of a downgrade by ratings agencies. Given that the Namibian Dollar is pegged to the South African Rand, the Namibia Dollar will follow suit.

Although the Rand had been weakening steadily in 2015 due to increasingly negative economic fundamentals, the currency collapsed after President Zuma dismissed the country's finance minister Nhlanlah Nene, following news that the South Africa's credit rating was cut. Nhlanlah Nene had been widely respected as a hand of moderation in the ANC administration, and the sudden dismissal of the minister was seen as opening the potential of irresponsible spending in a government already seen as corrupt. Nene was replaced by David Van Rooyen, which made matters worse as he was unknown with little experience in finance and the Rand continued to weaken. It was not until Van Rooyen was fired after only 4-days in office and replaced by former finance minister Pravin Gordhan that the currency stabilized slightly.

One of the main reasons of the increasingly bearish stance on the South African Rand is the US Federal Reserve Bank which is turning less accommodative and entered an interest rate hiking cycle in December 2015. We expect the US Dollar to experience broad-based strength because the US Fed is tightening its monetary policy which has led to capital which had been invested in emerging markets, now rapidly being repatriated. Carry trades of high-yielding currencies like the South African Rand will therefore become less attractive to fund in US dollar.

Secondly, investors are shifting away from risk assets and moving to safe haven assets. A move to bonds, gold and hard currencies such as the US dollar and British pound has seen investors dropping riskier assets such as South African debt and equity.

Thirdly, the Rand weakness can be ascribed to the economic slowdown in China and due to South Africa's exposure to commodities. China has been the world's largest consumer of raw materials and commodities and although the financial sector is the biggest contributor to the South African economy, South Africa is still heavily reliant on commodity exports to maintain a stable balance of payments, and with commodity prices that have been falling due to the slowdown in China, South African exports have dropped.

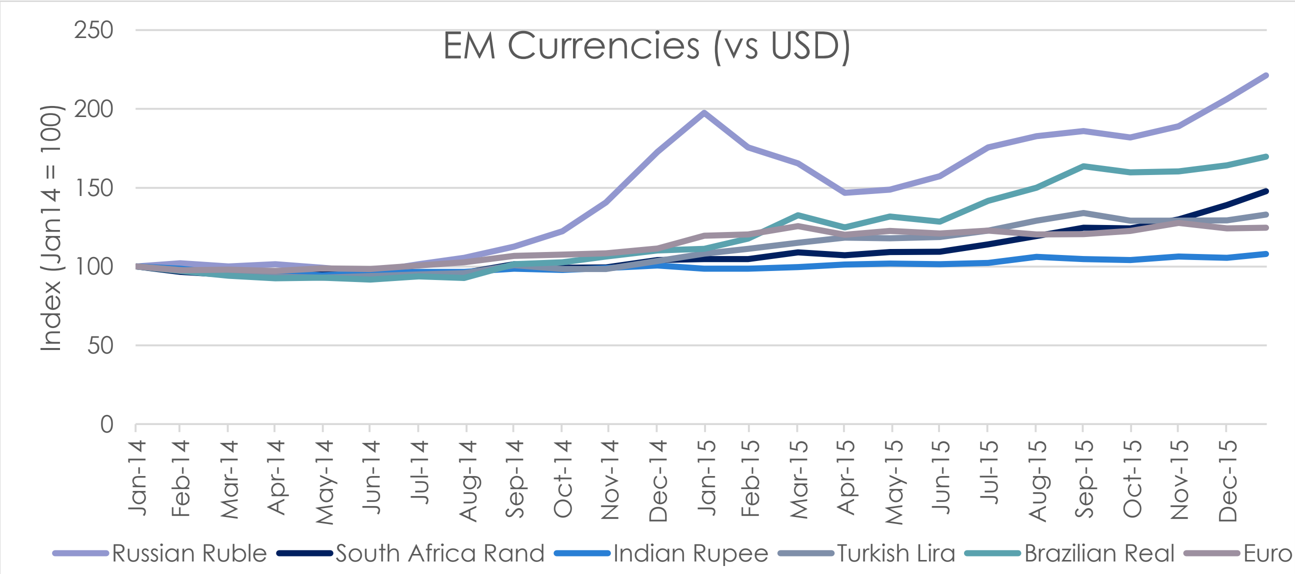
Lastly, South Africa's local problems are contributing to further rand weakness. Although negative sentiment surrounding emerging markets is a global theme, sentiment towards South Africa is particularly poor as extremely high levels of unemployment, with over a third of young people not working, increasing levels of fraud and constant conflict between government, corporates and labour unions, are all factors weighing on a grim outlook for South Africa.

The main immediate risk and source of volatility for the Rand going forward is what the SARB decide to do at their next few meetings. The bank raised interest rates by 25 basis points to 6.25% in November 2015 amidst fears the Rand would devalue as a result of a Fed rate hike. Now that it has devalued, and devalued more than expected due to the December finance minister crisis, there is a bigger probability that the SARB decide to raise rates even further, in an attempt to defend the currency. The weak currency results in inflationary pressure, but raising rates to defend the currency dampens growth as borrowing costs increases, in a time when economic growth is already very low. Therefore, one of the major themes for the Rand in 2016 will be how the country's central bank balances the need of economic growth with inflation and the exchange rate.

One of the major implications of the rand weakness is that the cost of imported goods in South Africa and also Namibia are expected to spike, this is not only luxury goods, but includes basic consumer staples. The impact is expected to be a steep rise in Inflation, resulting in higher prices of goods on the shelf. Inflation is the key mandate of the South African Reserve Bank, and is critical to the decision on interest rate levels. The current position South Africa finds itself in, with rising inflation, translates to higher interest rates, with the current economic growth levels, this situation could push South Africa into a recession as the weak currency together with higher interest rates decreases the disposable income of South Africa consumers and result in a slow-down in almost all sectors.

Compounded to this is the petrol price which has both the rand and oil price as significant components. While South Africa and Namibia enjoyed a dip in crude oil prices, the weaker rand largely offset these potential gains, and pump prices fell little.

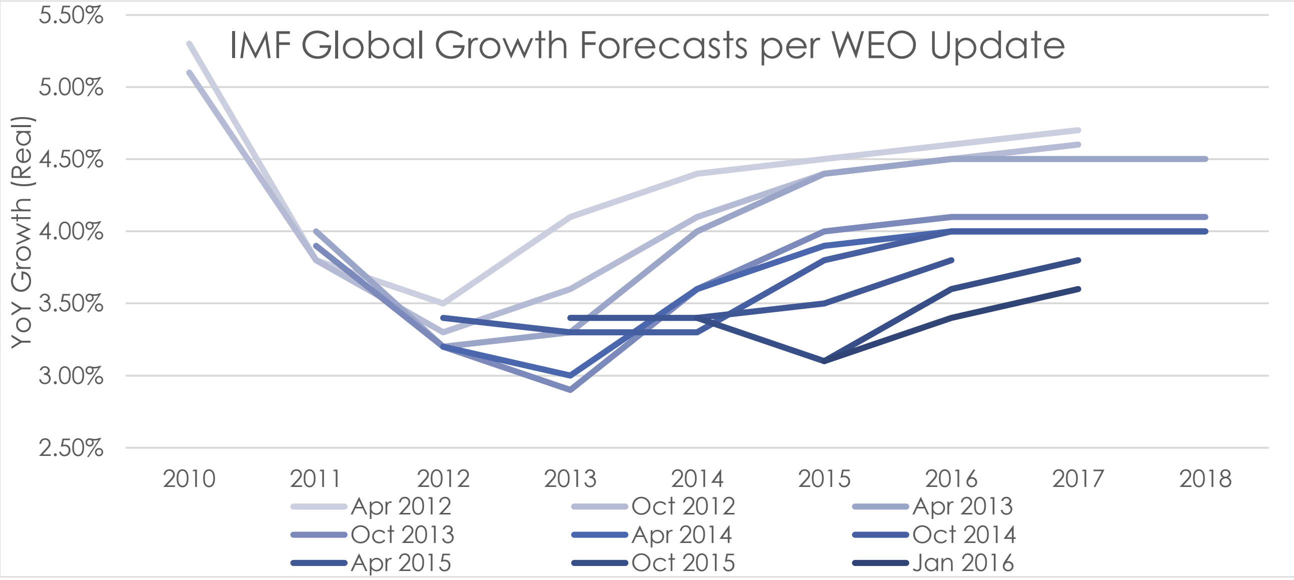
Lastly, the National Treasury of South Africa and Namibia borrows large tranches of Dollar debt from international markets, this debt must be repaid and serviced in US dollars and given the recent movements the rand, this now means higher debt servicing costs. The Rand meltdown also increases the probability of a ratings downgrade of South African debt, which means if downgraded further, it will be regarded as sub-investment grade. The reality is that the fundamentals, which were already under pressure, have now been exacerbated by the dramatic weakening of the exchange rate since December, due to irresponsible political action.



Source: IJG Securities, Bloomberg

Global economy

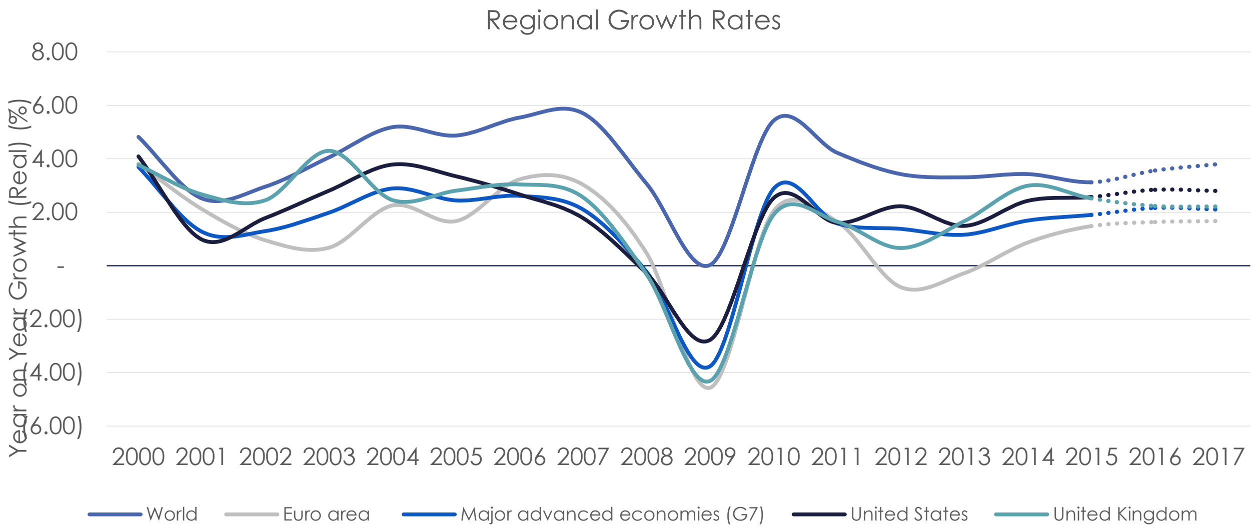
Global growth for 2015 was projected at 3.5% in January 2015 by the International Monetary Fund (IMF) in its World Economic Outlook update. This year the January update estimated that global growth will come in at a more sedate 3.1% in 2015. Projections for 2016 global growth have also been revised down to 3.4% from 3.7% last year and the latest IMF World Economic Outlook update projects 2017 growth picking up to 3.6%. The trend for the last few years has thus been for global growth estimates to come in below the forecasted figures with growth accelerating in the future. As the graph below indicates, expected increases in the rate of growth have not materialized over the last few years and growth expectations have been revised down with each new update. The darker lines indicate that global growth is expected to remain low for the next year or two at least.



Source: IMF, IJG Securities

Developed Markets

The IMF expects a modest and uneven recovery in developed markets in 2016 which builds on our 2015 outlook where we saw divergence as a major theme. The US was expected to outpace Europe and lead the world economic recovery during the year. This played out to some extent with US posting reasonable, if not quite as projected, GDP growth during 2015. GDP growth for 2015 is now expected to come in well below last year's forecast of 3.1%. This illustrates a slower than expected recovery from the US with unemployment rates falling below the Fed targets but labour participation not improving as expected. Inflation has remained below the target range buoyed no doubt by tightening monetary policy in the form of the end of quantitative easing as well as the recent interest rate hike, the first in almost a decade. Recent stock market weakness in the US indicates a more negative impact on the market than was expected after the first rate hike which could see further rate hikes being delayed in order to gauge the real impact on the economy. Thus the recovery in the US has seen mixed results although showing relative strength when compared to its European peers.



Source: IMF, IJG Securities

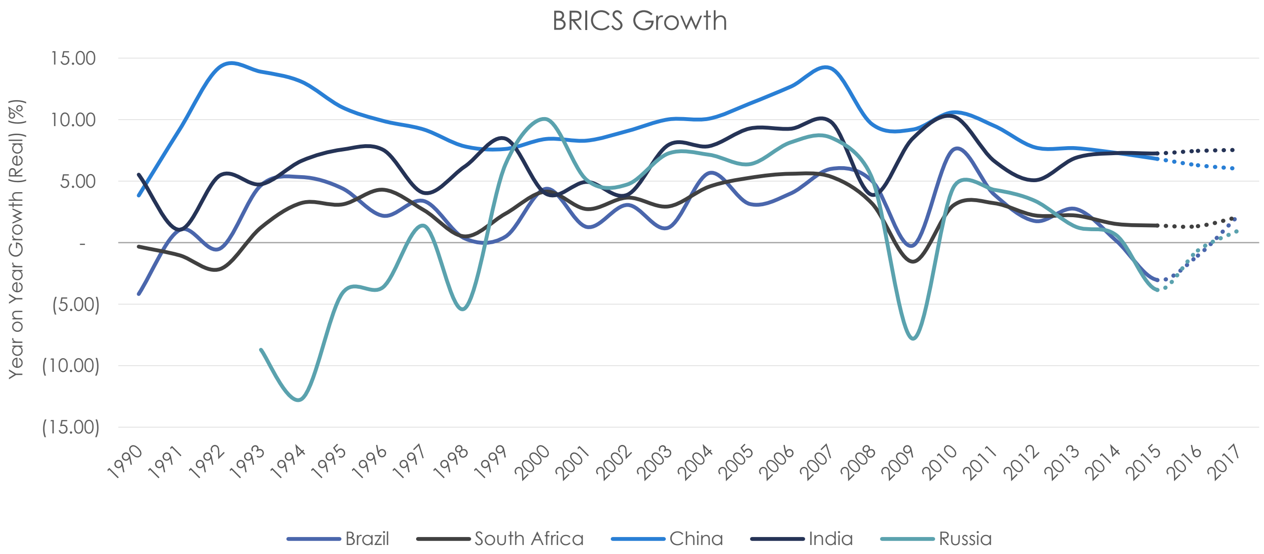
European growth, despite quantitative easing measures implemented late in 2014, has been muted at best. While Mario Draghi continues to laud the results that the EU's QE program is producing, there is little doubt that the system is "still broken". Unemployment rates, although steadily improving, remain elevated, especially among the youth. Interest rates within the Euro Area are at historically low levels with the European Central Bank's (ECB) current benchmark rate of 0.05% the lowest on record. Thus, extensive monetary easing within the Eurozone has been slow to promote growth with the figure above showing a very fragile recovery is taking place. The initial duration for EU quantitative easing would see bond buying come to an end in September 2016. This is unlikely to happen and it is widely expected that the ECB will introduce an extension to the program of bond buying. Worth noting is that low oil prices are a net benefit to the EU and the US and should continue to provide relief throughout the year.

The United Kingdom has proven to be more resilient than mainland Europe over the recent period although this divergence seems likely to mean revert with the UK's downward revisions coming in more aggressively. The UK economy showed some resilience in 2015 and expectations of normalising monetary policy and economic outperformance relative to peers was widely expected. Unemployment rates have largely normalised to pre-crisis levels and growth has persisted above 2% for an extended period of time thus indicating a relatively robust economy, if not growing at quite the rate expected early in 2015.

Japanese growth is expected to recover from the contraction seen in 2014 with IMF projections of growth of 0.6% for 2015 and 1.0% for 2016. This is largely as a result of expansive monetary policy and quantitative easing driving equity prices and real wage growth.

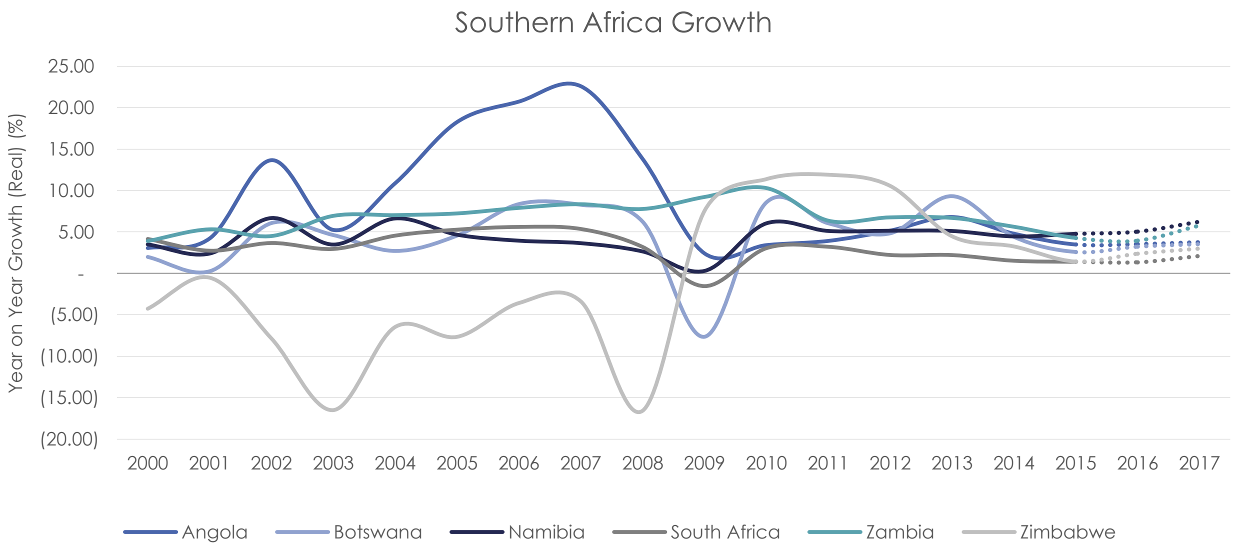
Developing Countries

Growth in developing countries in general has been slowing for the last few years, largely driven by a slump in commodity prices due to China transitioning from infrastructure driven economic expansion to a consumption driven economy. China's growth forecasts have been steadily coming down since the onset of the economic crisis in 2008, with 2015 growth coming in at 6.9%. The world's second largest economy is thus still growing at a rapid rate although below the much talked about 7%. The way in which the Chinese economy is growing has changed and this has driven the slump in commodity prices, the elevated levels of which were caused by Chinese infrastructure growth to a large extent in the first place. While growth in China is expected to slow further it is unlikely that the country will experience a hard landing although risks do remain to the downside. A triple bubble has formed within China consisting of what is estimated to be the biggest credit bubble of all time, a large investment bubble, as well as a real estate bubble, each of which bursting could set off the others. The repercussions of this would be felt worldwide, especially in emerging markets.



Source: IMF, IJG Securities

China's slowdown and the subsequent commodity price slump has affected most emerging market economies negatively, hampering economic growth and foreign investment into the area. As many, if not most, emerging market economies are heavily reliant on commodity production, the boom in Chinese infrastructure spend drove growth in these economies. These countries are now coming under pressure as revenues derived from commodity exports have tapered off. Commodity prices are to remain depressed going into 2016, and probably thereafter, thus featuring as a major cause of reduced growth expectations from emerging markets for the foreseeable future. The above figure shows that of the BRICS countries India and China are expected to grow at reasonable rates while those countries that saw growth driven directly and indirectly by commodity price increases are expected to record weak growth. Brazil and Russia have been hard hit by the ongoing oil glut and rating downgrades, while commodity prices in general are likely to have a negative impact on South African growth.



Source: IMF, IJG Securities

The rest of the Southern African countries have also been negatively affected by the slump in commodity prices with growth in the region slowing considerably. South Africa, the most industrialised country in Africa is expected to record the lowest growth of the countries within the region in 2015 and indeed over the next few years. These growth estimates are largely based on recent trends with risks very much to the downside. A large and currently expanding power deficit as well as an El Nino caused drought will add to the woes experienced by the region, negatively affecting growth further. There is a large probability that some countries within the region will experience a contraction in growth, most notably Angola and Zambia. Angola has enjoyed an abundance of oil which has driven growth to a large extent, but the current global glut has led to the government having to slice their budget in half. The Zambian economy has experienced similar trials with low copper prices affecting mining revenues negatively, and the current drought leading to some of the lowest water levels ever seen in Lake Kariba, the country's primary source of electricity generation.

The Namibian outlook is intertwined in that of South Africa to a large extent. Rising inflation and the expectation of interest rate hikes will dampen growth in Namibia to some extent. Tighter monetary policy from the SARB will force the BoN to follow suit, although this may actually be a positive for Namibia in the longer term as public and private debt levels have risen substantially and rate hikes may contain this to some degree. Namibia is positioned more favourably to deal with the aforementioned measures as real GDP growth is higher than that of South Africa. Risks to the downside remain, with drought in the region affecting the availability of power as well as driving up food prices in general. Another major downside risk is that of a credit ratings downgrade in South Africa as well as the common monetary area which will lead to increased borrowing costs making it more difficult, and costly, for government to fund a budget deficit.

Supply side growth

Namibia's growth is expected to slow markedly in 2016, off the back of a high base set in previous years, and an unwinding of expansive fiscal and monetary policy, influenced by external pressures, particularly on export earnings. Details of our growth expectations are given in the following section.

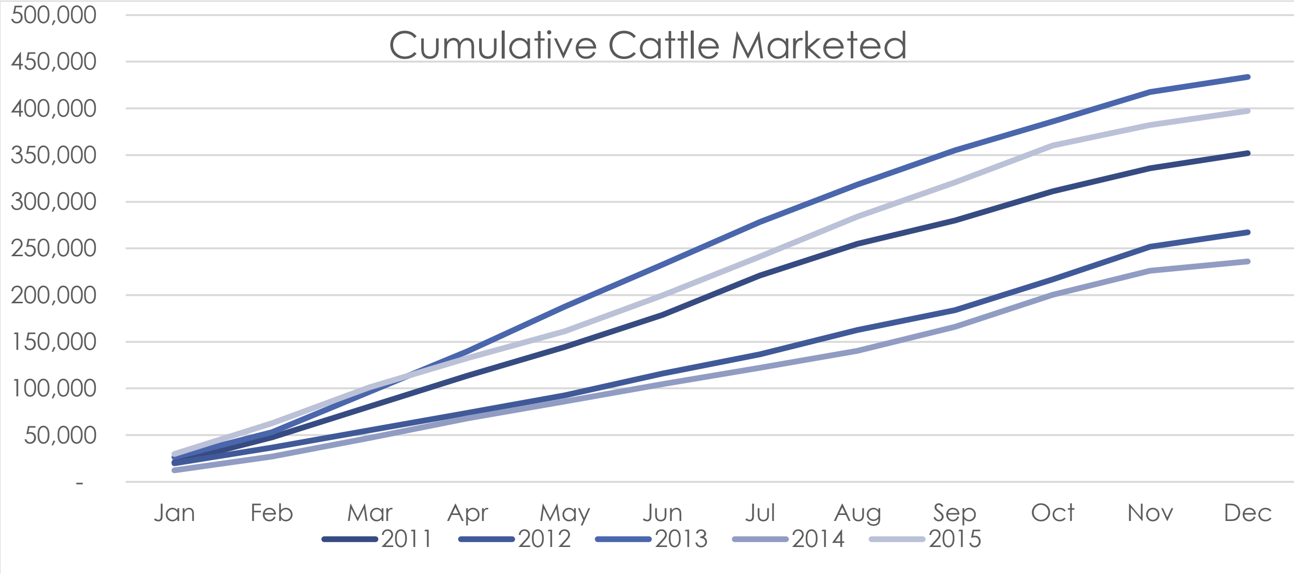
Real GDP Growth Rates

	Actual			Nowcast	Forecast				
Industry	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**
Agriculture and forestry	8.1	-19.3	9.6	-11.0	5.6	9.9	1.5	3.4	3.4
Livestock farming	6.0	-25.5	13.0	-12.0	8.3	8.7	-0.9	2.2	2.2
Crop farming and forestry	11.6	-9.6	5.3	-9.5	2.0	11.6	5.0	5.0	5.0
Fishing and fish processing on board	-7.6	3.0	-2.5	4.0	-7.3	0.0	0.0	0.0	2.0
Mining and quarrying	25.1	2.6	-6.3	2.4	-6.1	21.9	13.2	0.6	3.2
Diamond mining	13.0	10.0	6.2	-6.5	-7.0	9.1	0.0	0.0	5.6
Uranium mining	27.1	-7.0	-9.8	-18.1	0.0	122.1	53.8	0.0	0.0
Metal ore mining	32.4	-25.7	0.6	78.5	-16.3	4.5	1.5	-1.3	-1.2
Other mining and quarrying	62.6	11.0	-39.7	7.0	6.0	6.0	6.0	6.0	7.0
Primary industries	**14.4**	**-3.2**	**-2.2**	**-0.7**	**-3.6**	**15.5**	**8.7**	**1.1**	**3.1**
Manufacturing	-6.8	4.2	-2.2	5.8	3.6	3.0	4.0	3.8	4.1
Meat processing	-1.1	30.2	-17.4	15.1	4.2	4.2	-1.1	-1.1	-1.1
Grain Mill products	-1.5	8.0	2.8	8.0	16.4	-1.5	2.8	2.8	2.8
Other food products	-16.8	3.4	11.4	10.1	6.7	6.7	6.7	6.7	6.7
Beverages	15.0	13.5	-18.1	3.0	3.0	3.0	3.0	3.0	3.0
Textile and wearing apparel	6.1	4.8	-30.2	3.4	3.7	3.7	3.7	3.7	3.7
Leather and related products	10.9	-7.8	2.1	2.5	2.5	2.5	2.5	2.5	2.5
Wood and Wood product	-4.9	3.1	1.9	2.0	1.0	1.0	1.0	1.0	1.0
Publishing and Printing	-12.2	6.3	9.5	5.3	5.3	5.3	5.3	5.3	5.3
Chemical and related products	4.2	4.4	6.5	6.0	7.0	5.0	5.0	5.0	5.0
Rubber and Plastics products	-7.7	5.7	7.1	2.0	2.0	2.0	2.0	2.0	2.0
Non-metallic minerals products	0.5	3.8	5.6	6.1	3.8	3.8	3.8	3.8	3.8
Basic non-ferrous metals	-23.0	-4.0	-3.2	5.0	0.0	0.0	7.0	5.0	3.0
Fabricated Metals	7.0	5.7	3.9	3.5	3.5	3.5	5.7	5.7	5.7
Diamond processing	-6.7	-7.4	8.1	5.4	-7.0	5.4	-6.7	-7.4	8.1
Other manufacturing	3.9	8.4	14.2	4.8	2.8	4.6	4.3	6.1	6.5
Electricity and water	15.5	-1.5	4.8	4.0	2.1	6.0	6.0	3.0	0.0
Construction	7.5	28.2	40.6	-12.0	8.3	-15.0	-8.0	7.0	7.0
Secondary industries	**-1.8**	**8.6**	**9.4**	**-0.2**	**4.8**	**-2.0**	**1.2**	**4.4**	**4.3**
Wholesale and retail trade, repairs	4.3	14.4	15.2	2.0	0.5	2.0	3.0	4.0	4.5
Hotels and restaurants	8.1	9.2	5.3	8.5	8.5	6.0	4.5	4.5	0.0
Transport, and communication	8.0	6.4	6.6	10.5	4.3	5.1	5.5	6.0	6.7
Transport	10.0	12.8	4.9	12.7	7.0	7.3	7.9	8.7	9.7
Storage	7.6	3.8	6.8	14.1	2.0	5.8	6.2	6.5	6.8
Post and telecommunications	6.1	0.8	8.5	6.4	2.0	2.0	2.0	2.0	2.0
Financial intermediation	6.8	17.9	9.9	6.0	5.0	5.0	5.0	5.0	6.0
Real estate and business services	4.7	4.6	3.2	6.1	4.8	4.2	4.9	4.3	4.7
Real estate activities	6.7	4.9	3.1	4.9	4.3	4.1	4.4	4.3	4.3
Other business services	-0.7	4.0	3.5	9.6	6.3	4.5	6.3	4.5	5.7
Community, social and personal service activities	-16.6	-9.9	2.8	1.7	1.7	1.7	1.7	1.7	2.7
Public administration and defence	2.7	3.6	-0.7	8.5	0.0	3.2	3.2	3.2	3.2
Education	4.4	3.3	11.1	4.0	3.1	3.1	3.1	3.1	4.1
Health	5.6	9.0	7.9	1.0	1.0	1.0	1.0	1.0	2.0
Private household with employed persons	8.5	-6.7	5.5	2.5	2.5	2.5	2.5	2.5	3.5
Tertiary industries	**3.9**	**7.2**	**7.4**	**5.3**	**2.6**	**3.4**	**3.7**	**3.9**	**4.3**
Less: Financial intermediation services indirectly measured	4.5	18.8	7.1	7.1	7.1	7.1	7.1	7.1	7.1
All industries at basic prices	**4.8**	**5.2**	**6.0**	**3.2**	**1.9**	**4.2**	**4.1**	**3.4**	**4.0**
Taxes less subsidies on products	8.9	11.6	10.9	9.2	9.2	9.2	9.2	9.2	9.2
GDP at market prices	**5.1**	**5.7**	**6.4**	**3.7**	**2.5**	**4.7**	**4.6**	**4.0**	**4.6**

Real GDP (N$ Million)		Actual				Forecast			
Industry	**2012**	**2013**	**2014**	2015	2016	2017	2018	2019	2020
Agriculture and forestry	4,603	3,714	4,072	3,626	3,830	4,208	4,273	4,420	4,571
Livestock farming	2,806	2,090	2,362	2,078	2,252	2,447	2,424	2,477	2,531
Crop farming and forestry	1,797	1,624	1,710	1,548	1,579	1,762	1,850	1,942	2,039
Fishing and fish processing on board	2,525	2,602	2,536	2,637	2,446	2,446	2,446	2,446	2,495
Mining and quarrying	10,170	10,438	9,781	10,016	9,409	11,468	12,981	13,059	13,481
Diamond mining	5,176	5,695	6,047	5,654	5,257	5,735	5,735	5,735	6,054
Uranium	1,697	1,579	1,424	1,167	1,167	2,592	3,987	3,987	3,987
Metal Ores	1,352	1,004	1,010	1,803	1,509	1,577	1,601	1,579	1,560
Other mining and quarrying	1,945	2,159	1,301	1,392	1,476	1,564	1,658	1,757	1,880
Primary industries	**17,299**	**16,753**	**16,389**	16,279	15,685	18,122	19,700	19,925	20,547
Manufacturing	10,147	10,572	10,344	10,940	11,332	11,676	12,147	12,605	13,128
Meat processing	354	461	381	439	457	476	471	466	460
Grain Mill products	598	646	664	717	835	822	845	869	893
Other food products	1,141	1,180	1,314	1,447	1,544	1,647	1,758	1,876	2,002
Beverages	1,561	1,771	1,450	1,494	1,538	1,584	1,632	1,681	1,731
Textile and wearing apparel	502	526	367	379	393	408	423	438	454
Leather and related products	102	94	96	98	101	103	106	109	111
Wood and wood products	255	263	268	273	276	279	282	284	287
Publishing and Printing	158	168	184	194	204	215	226	238	251
Chemical and related products	896	935	996	1,056	1,130	1,186	1,245	1,308	1,373
Rubber and Plastics products	265	280	300	306	312	318	325	331	338
Non-metallic minerals products	399	414	437	464	481	499	518	537	558
Basic non-ferrous metals	2,431	2,333	2,258	2,371	2,371	2,371	2,537	2,664	2,744
Fabricated Metals	459	485	504	522	540	559	591	624	660
Diamond processing	623	577	624	657	611	644	601	556	602
Other manufacturing	404	438	500	524	539	563	588	624	664
Electricity and water	1,807	1,779	1,865	1,940	1,980	2,098	2,224	2,291	2,291
Construction	3,261	4,180	5,875	5,170	5,599	4,759	4,379	4,685	5,013
Secondary industries	**15,215**	**16,531**	**18,085**	18,050	18,911	18,534	18,750	19,581	20,432
Wholesale and retail trade, repairs	10,245	11,719	13,503	13,773	13,842	14,119	14,542	15,124	15,805
Hotels and restaurants	1,681	1,835	1,932	2,096	2,274	2,411	2,519	2,633	2,633
Transport, and communication	4,800	5,109	5,447	6,017	6,273	6,592	6,956	7,376	7,866
Transport	2,039	2,301	2,413	2,719	2,910	3,122	3,369	3,663	4,018
Storage	823	854	912	1,041	1,061	1,122	1,192	1,270	1,357
Post and telecommunications	1,938	1,954	2,121	2,257	2,302	2,348	2,395	2,443	2,492
Financial intermediation	5,194	6,123	6,730	7,134	7,490	7,865	8,258	8,671	9,191
Real estate and business services	7,882	8,248	8,514	9,033	9,469	9,866	10,352	10,802	11,305
Real estate activities	5,852	6,138	6,329	6,638	6,923	7,207	7,526	7,847	8,182
Other business services	2,030	2,111	2,185	2,395	2,545	2,660	2,827	2,955	3,123
Community, social and personal service activities	2,076	1,870	1,922	1,955	1,988	2,022	2,056	2,091	2,147
Public administration and defence	9,838	10,188	10,112	10,972	10,972	11,323	11,685	12,059	12,445
Education	7,200	7,440	8,264	8,595	8,860	9,134	9,417	9,708	10,105
Health	2,825	3,080	3,324	3,357	3,391	3,425	3,459	3,494	3,563
Private household with employed persons	1,005	938	990	1,015	1,040	1,067	1,094	1,121	1,161
Tertiary industries	**52,748**	**56,551**	**60,737**	63,945	65,599	67,823	70,338	73,078	76,221
Less: Financial intermediation services	1,169	1,389	1,487	1,592	1,704	1,824	1,953	2,091	2,239
All industries at basic prices	**84,093**	**88,446**	**93,723**	96,683	98,491	102,655	106,835	110,493	114,962
Taxes less subsidies on products	7,108	7,934	8,799	9,606	10,486	11,447	12,496	13,642	14,892
GDP at market prices	**91,200**	**96,381**	**102,522**	106,288	108,977	114,102	119,331	124,134	129,854

Agriculture and forestry

The poor rainfall over the last three years had a major impact on the entire agriculture industry. The country received favourable rainfall in 2014, however while livestock farmers started rebuilding herds after poor veld conditions and high feeding costs as a result of the drought in 2013, crop farmers were hesitant to plant in 2014 after poor or no harvests were made the previous year. The 2015 rainfall season started off promisingly, however, scattered and poor rainfall further along the season resulted in below average harvests, and livestock farmers had to reduce animal numbers as veld conditions deteriorated.

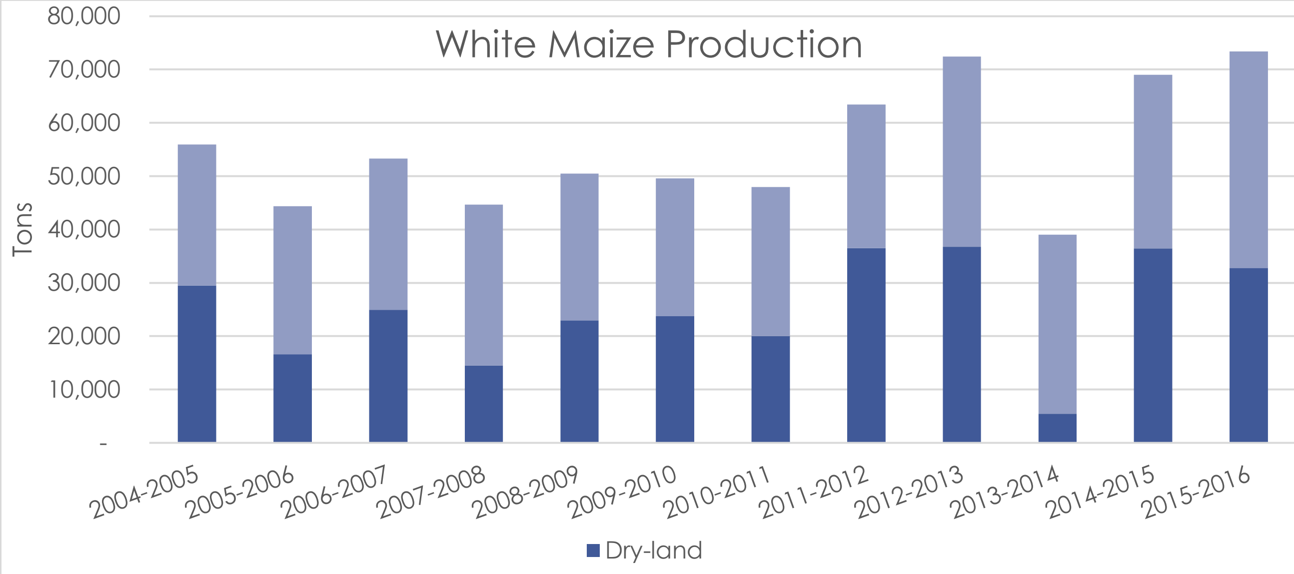


Source: Meat Board of Namibia

Looking forward, we expect the livestock sector to perform in 2016 in a similar manner to 2014, from a gross value addition perspective. Therefore, we should see a rebound in 2016 from the contraction in 2015. The reason for this is that as a consequences of the number of cattle that were exported in 2015, it will take the industry a couple of years before the national cattle herd has recovered, thus inventory rebuilding can be expected in 2016.

The outcome regarding export regulations with regards to livestock to South Africa will also be a determining factor for the industry in 2016. As a background, during an Animal Health Consultative meeting on 11 December 2013, the Namibian meat industry was informed of new veterinary requirements to be imposed by the South African Veterinary authority for the exporting of livestock to South Africa. These new requirements were made known to the Namibian delegation during a bilateral meeting between the Namibian Veterinary authority and their South African counterpart in early December 2013. Initially these requirements were to be implemented by January 2014, but the implementation date was postponed to 01 May 2014. Stakeholders in the livestock industries of Namibia and South Africa objected to these revised import requirements. The Director General of the South African Department of Agriculture, Water and Fisheries then suspended these import requirements with immediate effect on 26 August 2015 due to insufficient inclusive consultation.

The next meeting is in March 2016 and whether or not these regulations will actually be implemented remains uncertain. However, the proposed revised import requirements will have detrimental impact on Namibian livestock producers as the stringency of these proposed measures would make it virtually impossible to export livestock to South Africa, and Namibia will lose a market for about 180,000 weaners, 90,000 sheep and 250,000 goats per year.



Source: Agronomic Board of Namibia

White maize is a staple grain in Namibia and is grown primarily for human consumption. On average, dry-land harvests almost equal those grown under irrigation, and sometimes exceed it during good rainfall seasons, as was the case in 2011, 2012 and 2014. However, in the case of a drought, dry-land harvests collapse, as was witnessed in 2013. The 2015 rainfall season was one known as a wet-dry season, with favourable rain initially, but follow up rain was poor, which meant low harvest were achieved in 2015.

The harvest of maize grown under irrigation for 2015 was in line with previous years, but it is estimated that hectares planted so far in 2016 have declined as some farmers moved away from wheat and planted more luscern, which is less labour intensive and more suitable for the Namibian climate. Farmers have also waited on confirmation of rain, but can still plant up to the 27th February.

The outcome of the application by Grain SA for an upwards adjustment of maize reference price will be a determining factor for the grain industry in this year. The current applicable reference price was last reviewed in 1999, to date, it is still US$110/ton. From 1999 to 2014, US maize prices have increased by 120%, from an average of US$93/ton in 1999 to US$205/ton in 2014. At the same time the domestic (Safex) yellow maize price have increased by 187%, from an average annual price of R970/ton in 1999 to R2273/ton in 2014. Safex white maize prices increased by 185%, from an average of R794/ton in 1999 to R2268/ton in 2014. Hence, the application for the reference price to be revised upwards. Grain SA requested that the new domestic reference price for maize be calculated by using the same methodology as applicable in the determination of the wheat tariff. Therefore, the new domestic reference price will be US$233/ton. The US$233/ton is determined by calculating the recent five year value of US No 2 yellow corn price and the FoB Gulf of Mexico price from 1 June 2010 to 1 June 2015.

The Motivation for the increased grain tariff is that low international grain prices, caused by tariffs and subsidies in developed countries, have been blamed for causing financial difficulty for South African grain producers. This could be one of the reasons why the area of grain planted over the past decade has decreased, as grain production was seen as being uncompetitive at the low international wheat price rates.

The application by Grain SA for an upwards adjustment of the reference price level from US$110/ton to US$233.39/ton means that should the world reference price (US No 2 yellow corn price, FoB Gulf of Mexico) trade below US$233.39/ton, the tariff will start to take effect. (Below is the world reference price from June to November 2015.) It means that should the application be approved and the world reference price stay around these levels, a tariff will be applicable immediately – and this dollar specific tariff is then converted to Rand according to the prevailing Rand/US Dollar exchange rate.

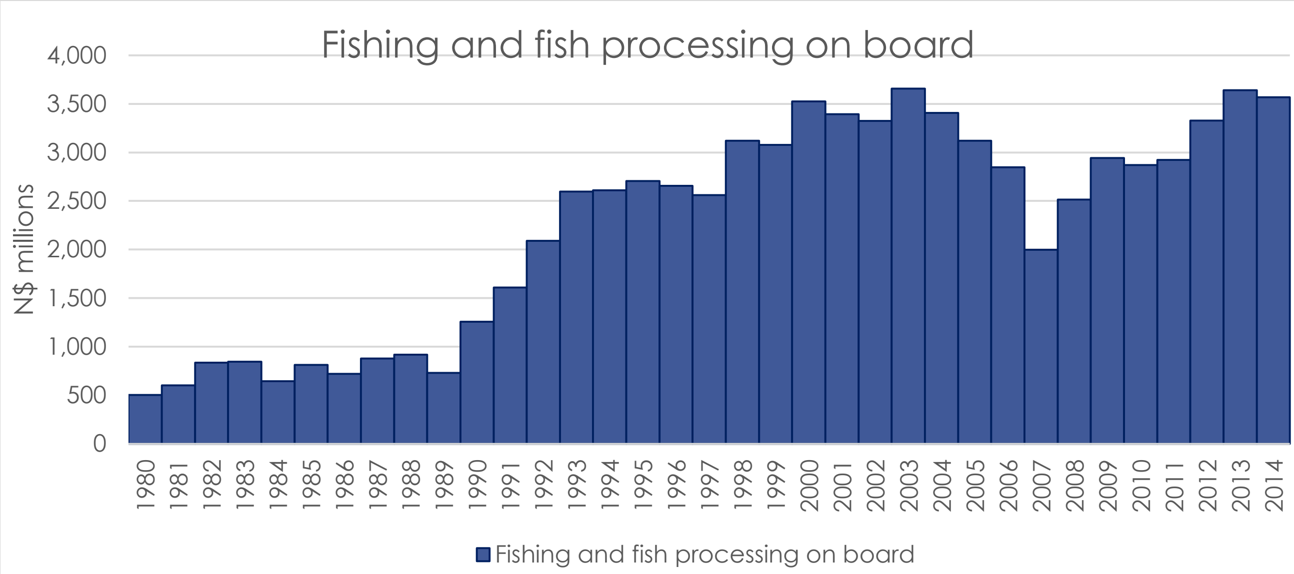
Month	Price	% Change
Jun 2015	166.72	-
Jul 2015	179.60	7.73 %
Aug 2015	162.74	-9.39 %
Sep 2015	166.01	2.01 %
Oct 2015	171.39	3.24 %
Nov 2015	166.03	-3.13 %

Source:NAU

This application was meant to protect the South African industry, as well as the other SADC countries, however, given the drought situation where South Africa is compelled to import maize, like most of the countries in the region, this change in the reference price will have severe implications for South Africa and Namibia with the current Rand/US dollar exchange rate. Looking forward, a good year for crops is expected in 2016, should the rain be favourable. The Horticulture outlook is positive, while good wheat and maize harvests are also expected during 2016. From a growth perspective, we expect agriculture as a whole to rebound, growing by 5.6 percent in 2016, driven by 2.0 percent growth in crop farming and by 8.3 percent growth in livestock farming.

Fishing and Fish Processing on Board

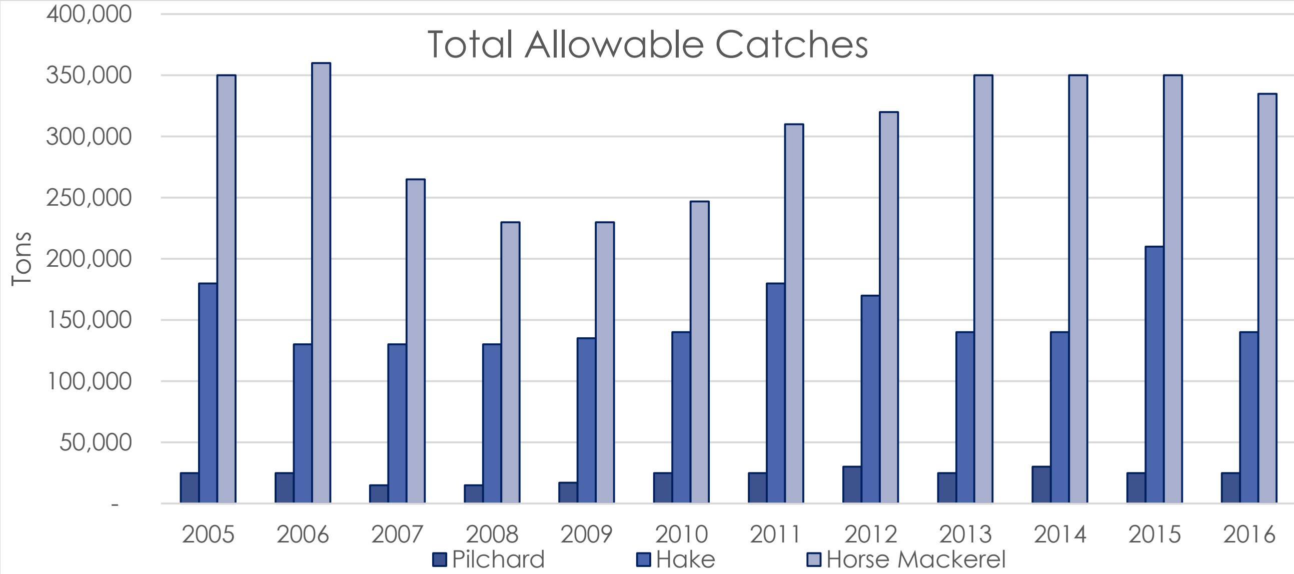
During 2014, the Namibian fishing industry recorded a contraction in real terms, down 2.0 percent as landings were down slightly, in particular that of pilchard. 2015 is expected to deliver good results as Total Allowable Catches (TAC) for hake was increased significantly and the industry reported good landings of horse mackerel due to the healthy state of the fish resource.



Source: NSA

The fishing sector's main products are hake and horse mackerel as well as canned pilchards. The TAC for hake was set at 140,000 tons for both the 2013 and 2014 fishing seasons, but increased to 210 000 tons for 2015, as the season was extended to an 18-month period. However, the 2016 hake TAC was set at 140,000 tons, with the fishing season running from 1 November to 30 September, stalling fishing activities during the spawning period in October. Local fishing companies noted that horse mackerel landings showed good results, however the TAC for horse mackerel was reduced to 335,000 tons for 2016 by the Ministry, from 350,000 tons for the last three years.

Prospects for pilchard are not positive as pilchard stocks remain of much concern to the industry. The pilchard population was seriously reduced due to negative environmental conditions, known as the Benguela Nino, in 1993 and 1995 and due to massive over-fishing in the period prior to Namibia's independence. This resource has never recovered from this over-fishing, and as such only very minor quota's, just to keep the fishery open and industry players active, are assigned each year. However, the Ministry of Fisheries and Marine Resources, with the approval of Cabinet lifted the ban imposed on pilchard fishing, which was under moratorium since 2005 due to dwindling stock levels that threatened the extinction of this valuable fish species in Namibian waters. Biomass assessments in 2014 showed an increase in pilchard numbers and plankton levels, which is a food source for pilchard. Based on that, the Marine Advisory Council recommended a TAC of 25 000 tons for 2016.



Source: Ministry of Fisheries and Marine Resources

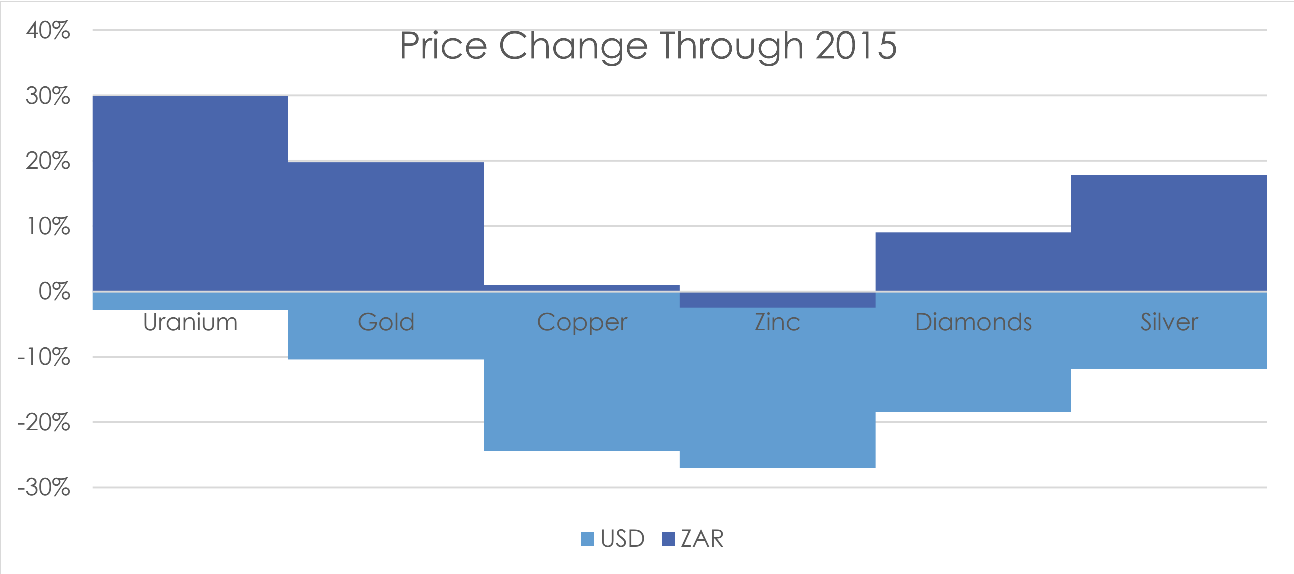
The Namibian fishing industry is currently performing well, with catch rates and fish quality high across most of the marine species. The regulation of October as a no-fishing month in some of the key industries appears to have served the sector well, with a notable improvement in catches following its implementation. Broadly, it appears that the Ministry of Fisheries and Marine Resources has managed the fish stocks well, allocating annual quotas at, or below, the sustainable off take levels.

However, weak European demand for luxury fish, and import restrictions on fish imports to Nigeria continue to dampen prices for hake and horse mackerel. That said, the weaker local currency remains the silver lining for many fishing companies, coupled with the collapse in oil prices, as fuel is one of the largest cost contributors to the industry.

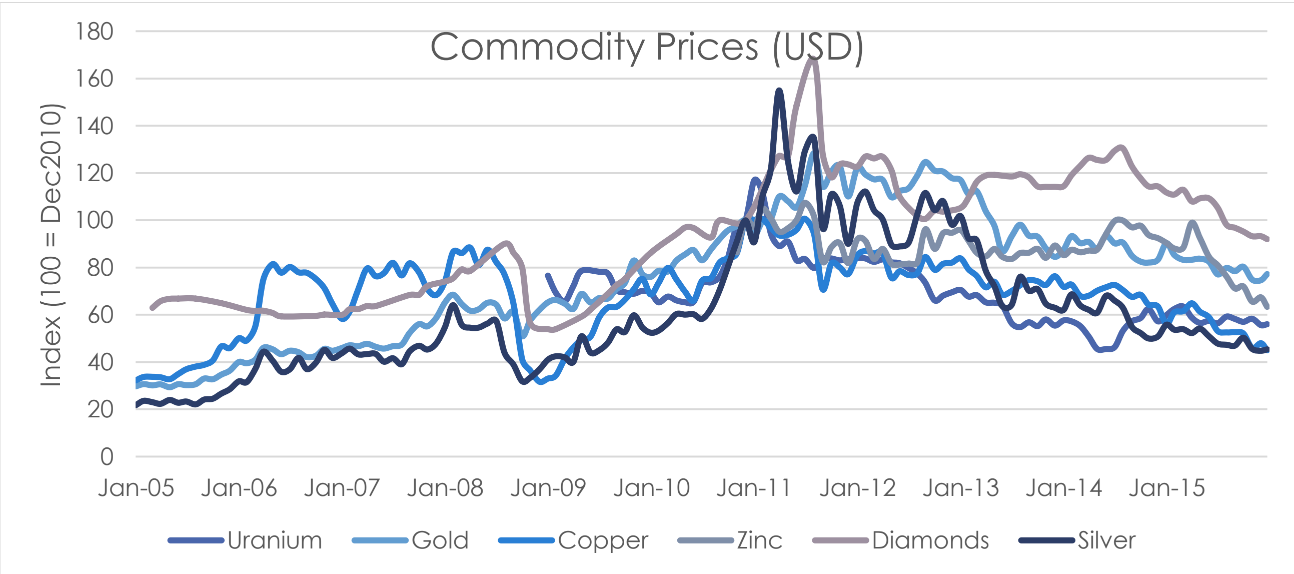
The greatest challenges currently faced by the industry are the changes in regulation and reduction in certainty surrounding quota allocation, as well as the proposed marine phosphate mining projects off the country's coast. While neither of these is likely to be catastrophic in nature, both pose a certain threat to the economic growth of the industry, should they be enacted without care.

Mining and quarrying

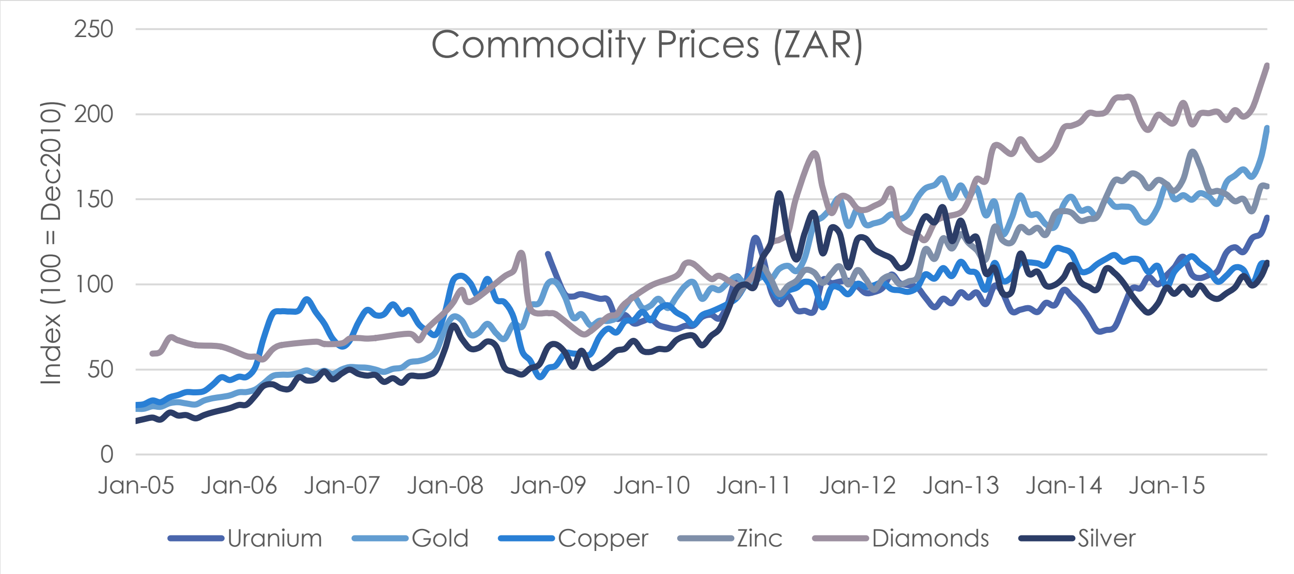
For miners, recent years will not be remembered as favourable, as an ever more prolonged period of weakness in global demand for commodities has led to a sizable price rout. In a move away from earlier expectations, it appears less and less likely that a major price rebound will be seen any time soon, meaning that producers will be required to endure current low prices for the foreseeable future. Namibian miners, like those across the world, have come under pressure as a result of lower prices and thus revenues, particularly in hard currency terms. This price weakness has been, however, largely off-set by currency weakness, and the rand price of most of the key commodities for Namibia have actually been fairly stable or increased over the past few years. Nevertheless, pressure remains, and with mounting costs, both in hard and local currency terms, the current environment remains a challenging one.



Source: IJG Securities, Bloomberg



Source: IJG Securities, Bloomberg



Source: IJG Securities, Bloomberg

Diamonds

Diamond production has been Namibia's key export earner for a number of years, however as the economy of the globe slows, it is likely that we will see a decline in demand for diamonds. As such, we expect to see a slowdown, albeit minor, in production volumes in 2016, when compared to the previous years. However, we expect this to be short lived, and expect production to recover once again in 2017 and 2018.

Uranium

Following recapitalization in 2014, both uranium mines continue to operate, with Rossing running on a fairly thin production profile, on the back of weak uranium prices. In 2014, both miners came under severe pressure, with Rossing forced to cut production and thus jobs, as the uranium price fell to U$28/lb for the first time in almost a decade. Langer Heinrich fared little better and was forced to sell a minority (25%) stake to a subsidiary of the China National Nuclear Corporation, for a sum of just under N$2 billion, in order to refinance the project's finance facility. The uranium outlook, while uncertain suggests that some increases in price can be expected over coming years, partially due to increased nuclear power demand by china, and also the restarting of the Japanese nuclear power station fleet.

The main story surrounding uranium, however, continues to be the construction and now imminent start of production at the new Husab mine, which is scheduled to take place in 2016. While slightly behind schedule, the mine is expected to increase domestic uranium production significantly in 2017, and will provide the country with much needed export earnings and growth. When in full production in 2018, the mine will result in a three-to-fourfold increase in Namibia's uranium output, and become the second largest uranium mine in the world. Moreover, it will rocket Namibia from the globes fifth largest uranium producer, to second largest. While the nature of the value chain of uranium makes further capture on the downstream side unlikely, the economies of scale created by the N$20 billion capital project and its forecasted expenditure and export earnings, suggest that major upstream benefits could be seen. In addition, major growth multipliers can be expected off this expenditure, as well as off the sizable cash-wages expected to be paid by the mine to her employees.

Gold

The Otjikoto gold mine was a key performer in 2015, as it ramped up towards full production for the year, and is likely to prove the saving grace of the country's external position in 2015 and into 2016. The mine, once at full production will deliver between 160,000 to 170,000 ounces of gold a year, worth over N$3 billion. Cash operating costs are forecast to be approximately $400 to $440 per ounce, significantly lower (by approximately 18%) than the Company's 2015 cost guidance of $500 to $525 per ounce, as a result of higher throughput, lower projected fuel costs and a weaker Namibian dollar (relative to the US dollar). With the gold price remaining fairly strong in US dollar terms, and reaching record highs in rand terms, the mine is likely to perform admirably over coming years.

Copper

The new Tschudi mine reached nameplate capacity in December 2015, and 2016 will thus be its first year at operating at full production for the whole year. The mine produced an estimated 10,600 tons of copper cathode in 2015, which is expected to increase notably, to 17,000 tons in 2016. Due to the nature of the mine and mineral extraction process (open-pit mine extracting oxidised copper ore to be treated through heap-leach, solvent extraction and electro-winning) Tschudi should remain in a position to operate despite the major fall in copper prices seen over the past few years. The same, however, cannot be said for the other copper mines in the country, which went into care and maintenance during the year following the collapse of the commodity price. Nevertheless, the Tschudi mine will not only offset the loss in copper production from the concentrate mines, but will actually increase total production of copper in the country, despite their closure.

While 2015 was a challenging year for Namibian miners, the outlook remains broadly positive as the mines recently built and under construction ramp up to full production. The uranium price is likely to stabilise or recover through the year; gold prices are likely to remain supported by deflation fear and volatile global markets; and diamond prices are expected to remain manageable. Copper prices, however are somewhat concerning. Additional challenges, however, remain for the sector. Shortages of power and water supply are fast becoming prohibitive to the sectors' further development, while prices are ever-increasing. In addition, while low commodity prices should be manageable, particularly given the weak rand, exploration and new mining activities are expected to remain limited for the foreseeable future.

Growth in 2016 is expected to be driven by gold production, while major growth is expected in 2017, from the Husab mine.

Mineral Production:

		2008	2009	2010	2011	2012	2013	2014	2015
Cu Cathode	t	-	-	-	-	-	-	-	10,527
Cu Concentrate	t	32,722	-	-	-	21,083	21,347	22,004	19,717
Cu Metal Contained	t	7,471	-	-	-	4,886	5,145	5,248	3,351
Gold Bullion	kg	2,125	2,057	2,190	2,112	2,289	1,968	2,377	6,213
Lead Concentrate	t	26,722	20,262	18,365	15,514	17,557	21,409	22,317	21,464
Lead Metal Contained	t	14,062	8,385	-	-	9,530	11,224	11,746	10,746
Manganese	t	86,874	51,471	126,448	41,876	188,863	133,473	104,527	36,386
Zinc Concentrate	t	82,224	93,953	93,829	89,488	94,421	113,778	104,046	99,756
Zinc Metal Contained	t	38,319	33,746	-	-	50,143	60,111	54,953	51,711
Zinc Refined	t	145,396	153,815	151,748	145,639	144,508	128,291	118,665	59,018
Diamonds	Carrats	2,224,897	939,916	1,475,610	1,344,932	1,665,684	1,776,290	1,897,872	1,774,509
Uranium	lbs	-	10,751,733	11,619,052	8,748,205	10,316,833	10,352,606	8,326,257	7,668,691

Source: Ministry of Mines and Energy

Manufacturing

The 2014 final National Accounts saw manufacturing registering growth of -2.2%. This compared negatively to the preliminary figure which projected growth of 0.5%. Both these figures were below our estimate of 4.4% growth for the period. The meat processing subsector saw a decline of 17.4% which was largely foreseen due to higher than normal slaughtering during the 2013/14 period due to drought, and the subsequent heard rebuilding in 2014. Beverage production experienced an unforeseen decline of 18.1% compared to our forecast of 7.3% growth. This can largely be attributed to the migration of beer volumes by Namibia Breweries to the Sedibeng brewery in South Africa. Various other subsectors experienced higher or lower growth than projected although with arguably less influence on the manufacturing sector as a whole. These can be seen in the figure below.

	2008	2009	2010	2011	2012	2013	2014
Manufacturing	**4.9**	**2.0**	**7.5**	**5.7**	**-6.8**	**4.2**	**-2.2**
Meat processing	-6.3	4.1	5.6	-2.7	-1.1	30.4	-17.4
Grain Mill products	14.9	16.3	8.4	6.5	-1.6	8.1	2.7
Other food products	8.5	6.7	17.2	-10.3	-16.8	3.4	11.4
Beverages	3.2	15.2	1.9	0.4	15.0	13.5	-18.1
Textile and wearing apparel	3.0	-1.1	3.6	4.7	6.1	4.7	-30.3
Leather and related products	6.9	-35.9	11.6	12.7	11.3	-7.3	1.5
Wood and wood products	14.7	-3.8	-10.0	-1.0	-4.5	3.1	1.8
Publishing and Printing	8.2	-7.4	-7.7	10.9	-12.6	6.8	9.5
Chemical and related products	0.2	5.9	7.3	12.0	4.1	4.3	6.6
Rubber and Plastics products	-3.9	-0.2	7.9	4.6	-7.6	5.6	7.0
Non-metallic minerals products	6.4	-2.1	1.2	72.3	0.6	3.8	5.5
Basic non-ferrous metals	-11.2	11.7	13.0	15.5	-23.0	-4.0	-3.2
Fabricated Metals	17.0	-10.9	9.1	-7.1	7.0	5.6	4.0
Diamond processing	55.6	-44.2	23.4	5.5	-6.8	-7.3	8.2
Other manufacturing	18.3	19.2	-22.4	-8.1	3.8	8.4	14.1

Source: National Accounts

As is evident from the above data above, the manufacturing sector in Namibia has experienced rather erratic growth over the period following the economic crisis. However a trend has developed over the last four years or so- one of low growth. Within the subsectors, growth has been erratic with various industries exhibiting almost no trend growth but rather isolated patches of growth or decline. This makes forecasting expected overall manufacturing performance a difficult task.

The current drought is expected to play a big part in the economy in 2016 and thereafter, should it persist. If prolonged, this will be one of the main challenges for the manufacturing sector over coming years. Water is a major input in various subsectors of manufacturing and the current water crisis will no doubt negatively impact output growth. The drought has already resulted in reduced crop yields in 2015 and is likely to result in the need to import more grains and grain products and a contraction of the grain mill products subsector. However, the drought has led to increases in the number of animals being slaughtered, which is positive for meat processing, but considering that herds have not recovered in number from the excess slaughtering in 2013, this increase in meat processing is likely to be modest at best and of lower quality than usual. Beverage production experienced a large decline during the last fiscal year which has substantially lowered the base off of which 2015/16 production will be calculated. However drought conditions may lead to further volumes being migrated to South Africa by Namibia Breweries leading to a further, albeit smaller decline, in beverage production (this may only be visible in the 2016 National Accounts though). A further thorn in the side of various manufacturers may be a decline in construction growth. Construction has boomed in recent years but could see a slowdown in 2016 due to water issues.

The fishing sector which is also a large input contributor to the manufacturing sector has recently been plagued by strikes. This delayed the going to sea of some fishing boats involved in the primary fishing industry. The knock on effect of this is that landed catches have also been delayed somewhat. While this is an inconvenience it may have a positive spinoff as the current currency weakness will benefit revenue of exported manufactured products produced by the industry. Total allowable catches have been reduced by the Ministry of Fisheries and Marine Resources, which will see the industry contract somewhat, mitigating to some extent of the benefit of the currency weakness.

Exporting manufacturers will be greatly assisted by the weak currency in 2016, to the extent that inputs to the manufacturing process are derived locally. Manufacturers that rely heavily on imported materials may find that margins will diminish due to higher input costs. Manufacturers serving the local market will have to contend with drought and slowing growth from primary industry which may negatively affect consumer spending habits and thus demand side growth. The outlook for the manufacturing sector is thus challenging and low growth should be expected, if any. The factors highlighted above could very well lead to manufacturing output falling once again.

Electricity and water

Water

Water supply has been an issue in the past and will continue to be one of Namibia's biggest challenges as a semi-arid, developing country. Currently the dams that supply the central region with water hold only about 13% of their combined capacity (January 2016), the lowest level since 1996/7. In that year, we received good rainfall and dam levels improved after the drought, and have subsequently not been drawn down to such low levels until now. Whether we will be saved by the rainy season this year is hard to tell as the central area receives most of its rain during the period from February to April. Thus far, the current rainy season has not resulted in major inflows into the Von Bach, Swakoppoort, and Omataku dams that supply the capital.

The north of Namibia has also experienced lower than anticipated rainfall leading to crop failures and excess slaughtering of animals, particularly during 2013. During drought years the carrying capacity of the land is severely affected leading to necessary culling of livestock. Subsequent years see less slaughtering due to livestock numbers being restored, but in Namibia these numbers never reach pre drought levels as some farms fail and farmers leave the sector, destock or shift across to wildlife and tourism as a preferred land use. Thus even multiple good rainy seasons leave the country with less meat production than before the preceding drought.

The south of the country has been affected similarly by the drought, although the regions to the south are generally more arid and thus sustain fewer people and less farming. Ironically some of the largest dams in the country are found there. Thus, the supply of water is not really as big an issue as in the central and northern areas of Namibia. The south may gain importance in terms of economic development due to the currently under construction Neckartal Dam, a peculiar priority for finite government funds, as well as the underutilised Naute Dam and Hardap Dams. The outlook for the south of the country is thus not as dire as that of the rest of Namibia, with this outlook reinforced by recent rains.

The current water crisis being experienced in Windhoek is much more severe by comparison. As the densest populated and one of the most industrialised cities in Namibia, the implications of drought are far reaching, affecting the economy and social stability of the country. As of the end of January there is a high likelihood that the City of Windhoek will put a moratorium on the issuance of new building plans, due to the water shortage, for the foreseeable future. This will have negative knock on effects in the construction industry, a major source of economic growth and employment over the last decade. Even if the approval of building plans continue it is likely that construction activity will face a downturn due to water restrictions, thus reducing the sector's contribution to growth. Manufacturing activities such as the brewing of beer and the processing of meat and fish are heavily reliant on water as well, and may go much the same way as the construction sector should good rainfall not be received. These are but a few examples to highlight the seriousness of the issues caused by a drought, and inadequate planning for water supply to the capital over the past two decades.

Major emphasis is currently being put on finding solutions to the water crisis experienced by the capital and surrounding areas. It is estimated that water demand has surpassed the sustainable yield available from the current water sources some years ago. The current drought is simply highlighting this. An underinvestment in infrastructure and rapid growth have contributed to the current situation. The issue with generating solutions to the water crisis is that solutions, like building new dams or pumping water from the north of the country or desalinated water from the coast, are expensive to implement and take time to put in place. Solutions which address the long term sustainability of water as a resources require long term planning and thus leadership that is forward looking and willing to make decisions that account for future sustainability. This issue will not be solved through trying to manage the present.

That said there are some steps that are more immediately implementable. There is rampant water wastage at various large consumers which could be curbed. This wastage takes the form of leakage due to poor maintenance as well as misuse of the water infrastructure. Various large consumers such as the two breweries could be relocated to areas with sufficient water and incentives could be used to ensure that new industries are developed in areas where water is plentiful. Indeed the fact that SAB was allowed to build a new brewery in Okahandja, drawing on the same water source as Windhoek, is peculiar to say the least.

Electricity

The current energy crisis within the region serves as a reminder that Namibia has an electricity generation capacity deficit as do many of the countries that supply us with electricity. Thus, Namibia cannot rely on its neighbours indefinitely for electricity. As highlighted earlier in this outlook, countries like South Africa, Zambia and Zimbabwe are experiencing major electricity issue although still supplying Namibia with power, at present. However this is due to Namibia's relatively small demand relative to the region. Approximately 48% of the country has access to electricity and the demand from large industries is limited as they are few in number.

Electricity, and water for that matter, are required for economic growth and to attract investment. Thus electricity is part of a key mix of ingredients which promote foreign investment as well as local development. Currently Namibia imports close to 60% of domestic electricity usage during the typical year and generates the remaining 40% from local plants, mainly Ruacana. The Van Eck thermal plant is undergoing refurbishment which should boost generation capacity and ensure sustainable power generation in the future. The refurbishment is running behind schedule at present but should be complete within the year. While this may help to alleviate the power deficit within Namibia it will by no means solve it. We will continue to rely on power purchase agreements with our neighbouring countries to supply us with electricity over the medium term. Thankfully the renegotiation of PPAs with Eskom, ZESA, ZPC and EDM have thus far been successful.

Unlike with water, government has recently been more proactive in developing solutions for the energy deficit we face as a country. A major step forward in this regard has been opening up the energy generation space to the private sector, although only to a very limited extent. The major benefits of involving the private sector is that the costs of setting up infrastructure are privately financed removing this burden from government's shoulders, and through competitive tendering, the best price should be achieved for the consumer. In addition, the pace at which private sector companies are able to implement projects has and will be a major advantage. Already we have seen two solar parks erected in Otjiwarongo and Omaruru which have added 10MW to the grid. The fact that the private power plants being erected and in the pipeline all generate renewable energy can also be seen as benefit and is certainly investor friendly. However it places pressure on NamPower to supply a stable baseload as renewables tend to creates spikes in supply during certain times of the day and provide no electricity during others.

A baseload solution is thus required and has been a primary focus of the government for a number of years. The Kudu Gas-to-Power project seems to be off the table for the time being which will hopefully open up space for a more immediate solution to be implemented. A tender was put out towards the end of 2014 for a 250MW open cycle gas turbine power plant which was awarded to Xaris Energy. The tender process was handled in a questionable manner and thus saw delays in the development of the plant. It does appear as though the project has the support of the president and that it will go forward. As yet the cost of electricity produced by this plant, to be built near Walvis Bay, is unknown. The Xaris plant, if implemented will address some of Namibia's electricity deficit but will likely not eliminate it. It will however buy time so as to develop further electricity generation sources. At present alternative mid-sized plants (in relation to demand) are being investigated and may be considered for the medium to long term. However there appears to be, as with the water supply issues, a lack of direction in determining which solutions will be implemented.

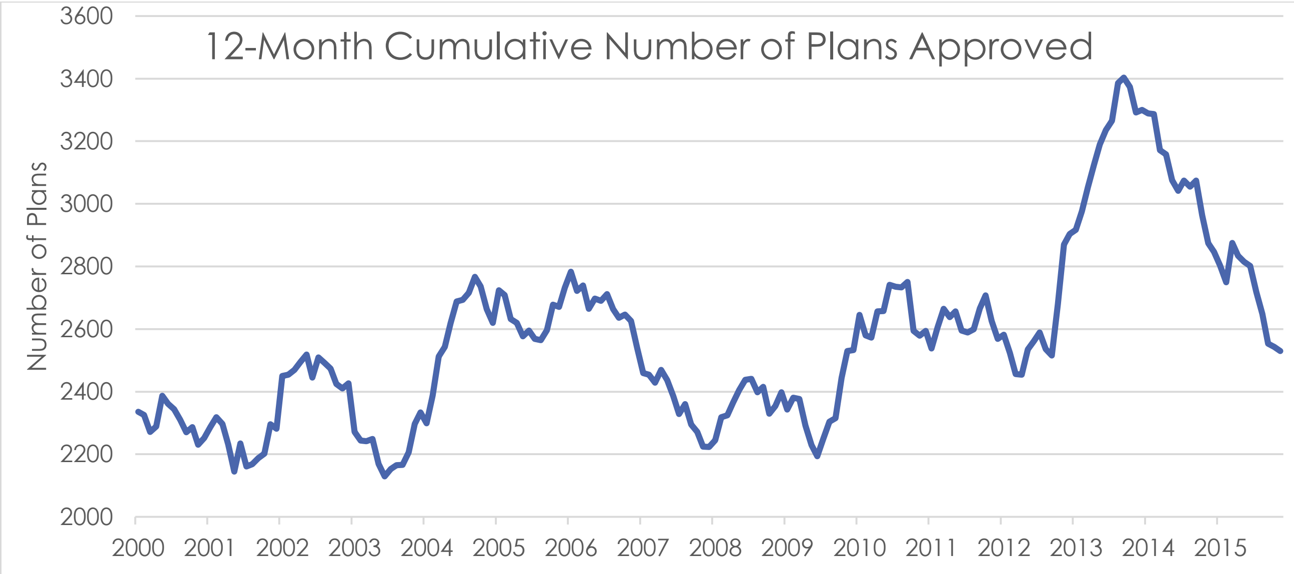
Supply side growth in electricity generation in 2016 will likely be driven by the independent power producers installing renewable power plants. The various solar projects already awarded as well as a wind farm will add much needed generation capacity and promise to do so at a reasonable price. However this generation capacity does not provide for much needed base load electricity generation. 2016 may be the year that we see tangible steps taken to construct a baseload power plant, weaning Namibia off its current reliance on neighbouring countries. For the time being we are highly unlikely to experience load shedding or major electricity shortages due to the ongoing PPA's with these countries, as well as very limited demand increases expected due to the slowing economy.

Construction

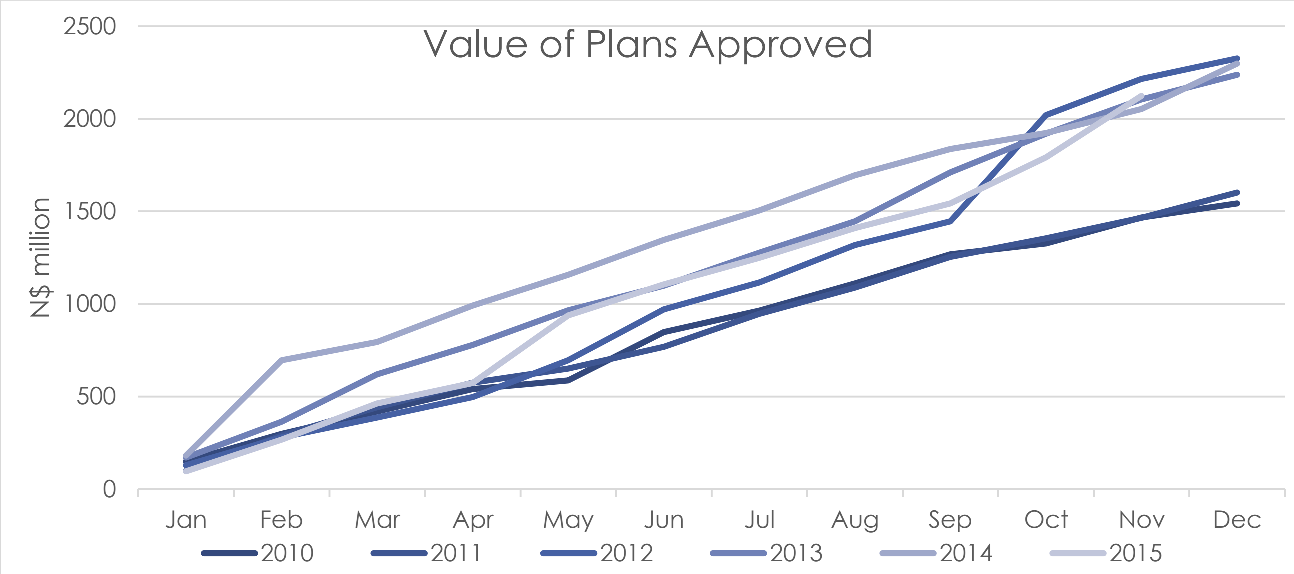
The Namibian economy was largely driven by the construction sector over the past five years. The exceptional growth in the construction sector stemmed from the construction of three major mines across the country and also both private sector and government investing aggressively in infrastructure development.

Construction at the B2Gold mine and the Tschudi copper mine has been completed during 2015, while construction of the Husab mine is nearly completed and production is planned to start by the end of the year. Therefore, growth contribution from the construction sector is expected to decline, but be compensated for by major growth in uranium output. Although the activities in the mining sector had a significant impact on construction growth, other big projects such as, the Neckertal Dam Project, the new container terminal and expansion of the harbour in Walvis Bay, the construction of the new Dunes Mall in Walvis Bay, and the Grove Mall too contributed to the overall growth figures.

Looking at construction activity within the capital, the 12-month average number of building plans approved by the City of Windhoek has continued on a downward trend to 2,530 plans approved in November 2015, after peaking in September 2013 at 3,403. However, from a value perspective, the value of plans approved reflect a different picture. As at the end of November, year to date value of plans approved totalled N$2.124 billion, 3.4% higher than for the same period in 2014 and 1.0% higher than for the same period in 2013.



Source: City of Windhoek



Source: City of Windhoek

Government continues to allocate sizable funding for infrastructure construction, renovation, and improvements for the 2015/2016 period ending in March this year. This budget was estimated at N$5.856 billion, up from N$4.549 billion during the previous financial year. The estimated amount for the 2016/2017 financial year is N$7.437 billion, ramping up to N$8.295 billion in the following period. Given the magnitude of these amounts, government remains significant in context of recent construction spending.

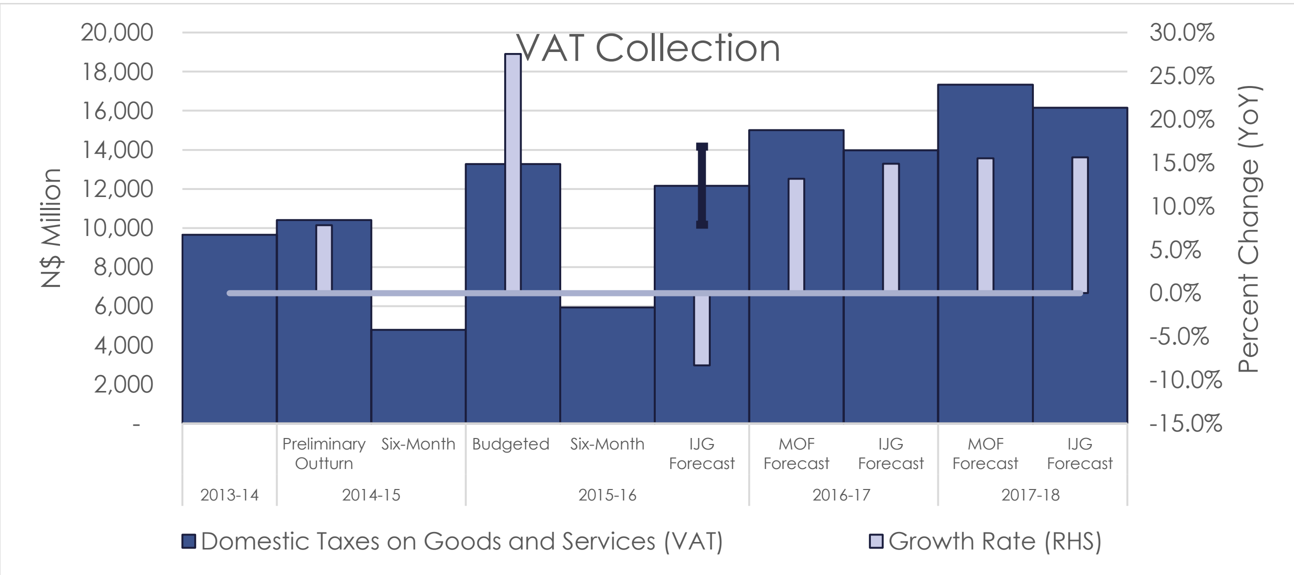
Water shortages and restrictions in Windhoek will directly affect economic activity in Namibia, impacting water dependent industries, such as construction. If water restrictions are implemented in Namibia, it would have a severe impact on the construction industry as they are heavily reliant on water supply.

With the high base created in 2014, we expect the construction sector to have contracted in 2015, but for it to recover slightly in 2016. Thereafter, the unwinding of construction at Husab will see the sector contract once again, despite upcoming energy, water and housing projects (amongst others).

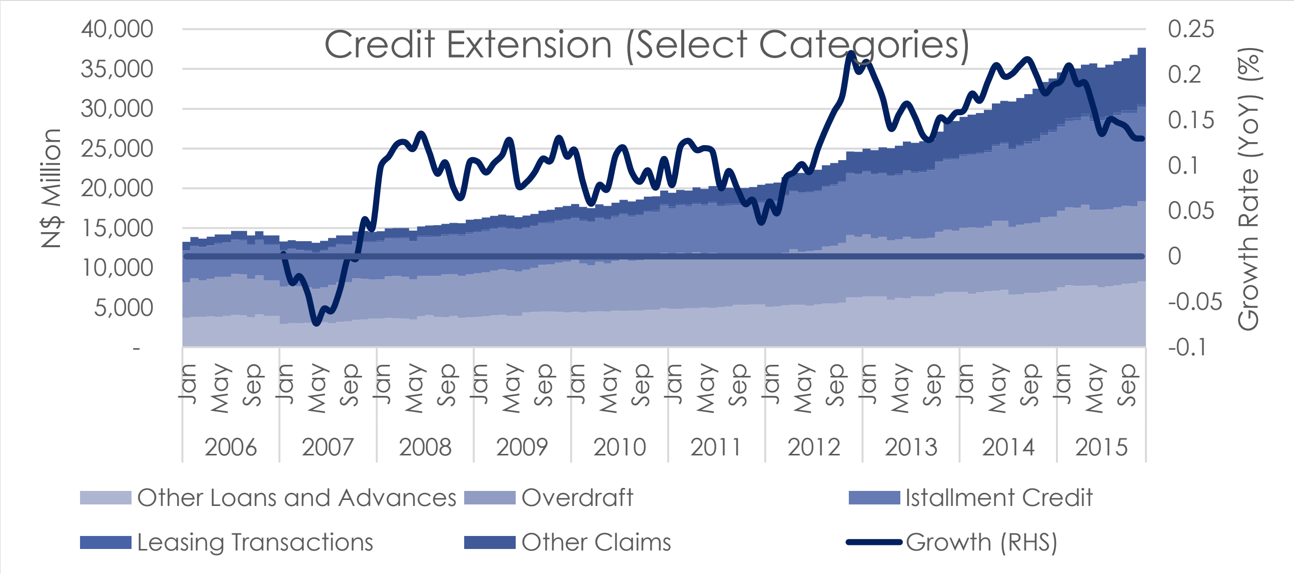
Wholesale and retail trade

The wholesale and retail sector of the economy has been a key driver of growth over recent years, largely on account of unusually high levels of government spending, personal income tax cuts and unusually low interest rates in the country. However going forward, there appears to be a very high likelihood that growth in this segment of the economy will slow of the exceptionally high, and unsustainable, base created over recent years. Various high-frequency indicators are already illustrating a slowdown, particularly on a real basis. Therefore, we expect to see growth of around 2% in the sector in 2015, followed by very low growth of half a percent in 2016, before returning to around 2% in 2017, thereafter normalization towards and average real growth rate of around 3 to 3.5%. Real growth is expected to be severely dampened by an extremely weak exchange rate at the moment, which is likely to force down demand for consumables as the price of such consumables increases, at the same time as the local economy slowing and reductions in disposable incomes are becoming more likely. This is likely to be further exacerbated by increasing interest rates, which will put further pressure on consumers, further reducing the growth in demand for consumables, thus driving down growth in this sector. In addition, a major slowdown in the economy of Angola has resulted in a notable decline in retail tourism from our northern neighbour, a situation that is expected to continue for the foreseeable future.

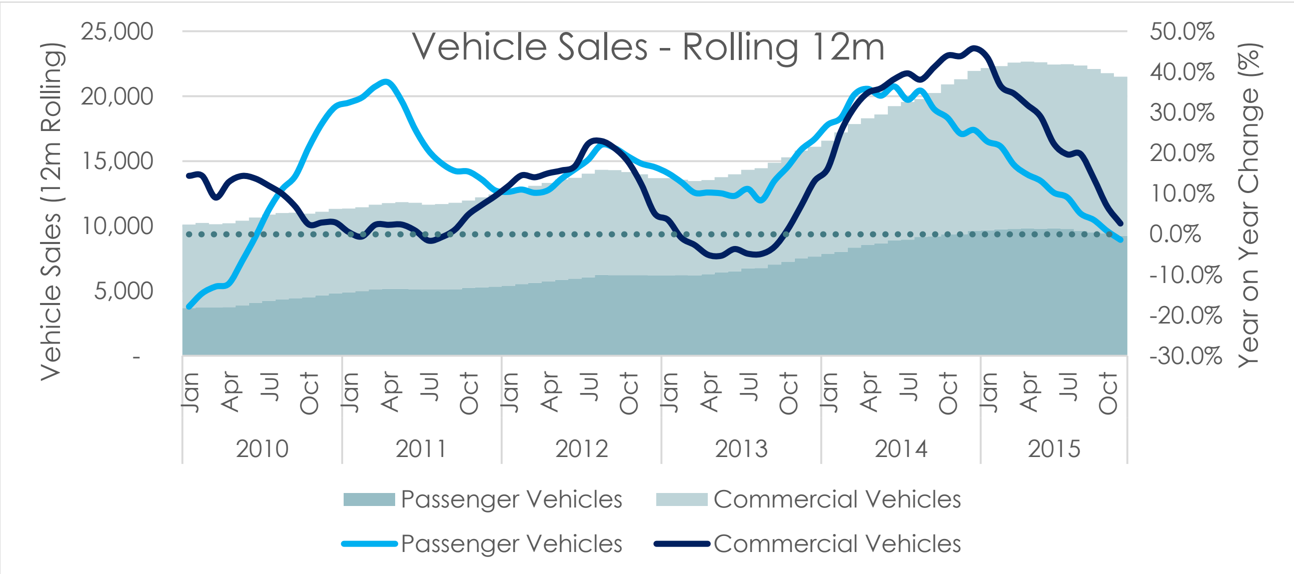
The general outlook for the sector remains overcast, particularly given the high base created over recent years, and given the expected constraints on disposable income and disposable income growth in the country, a contraction, in real terms, is not out of the question. This will become even more likely should we see a major tightening in the fiscal space, either via lower government expenditure or a surprise increase in taxation.



Source: Ministry of Finance, IJG Securities



Source: Bank of Namibia, IJG Securities



Source: IJG Securities

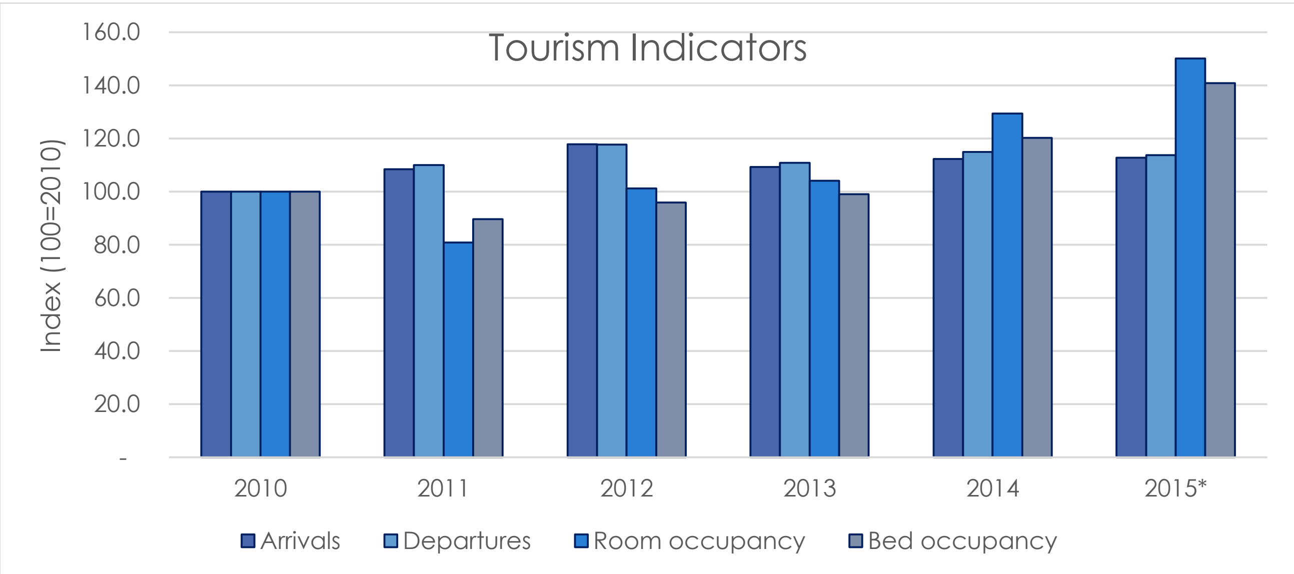
Tourism

Tourism has been a key component of the local economy for a number of years, and a key source of growth in recent years. It is a particularly valuable sector, as it creates jobs and therefore wealth, in rural parts of the country. In addition, it remains one of the key service exports of the country therefore earning the country much-needed hard-currency. Due to the fact that most tourists that come to Namibia do so from Europe, the exchange rate between the rand and the euro is of critical importance to the sector. Recent currency movements, with regards to the rand weakening vis-à-vis major currencies such as the euro, US dollar and the pound, has certainly helped the industry making the industry relatively more competitive. This depreciation of the exchange rate means that for those earning hard-currency, Namibian becomes an increasingly cheap destination to visit.

As a result of the current weak euro-rand exchange rate, we expect to see high levels of current and forward bookings in the tourism industry, as visitors can effectively lock in the current exchange rate by booking now, and visiting later. In addition, the exchange rate means that not only do more tourists visit, but the average spend in Namibia Dollar terms also increases, which is very positive for the industry and its service providers.

In addition to overseas tourists, we expect to see a pickup in regional tourism, particularly from South Africa, as the increased costs of going abroad see South African's substituting their overseas travel for more regional holidays. This can be expected to be partially offset by a decline in tourism from Angola, as the collapse in oil price has placed disposable incomes under severe pressure in the country.

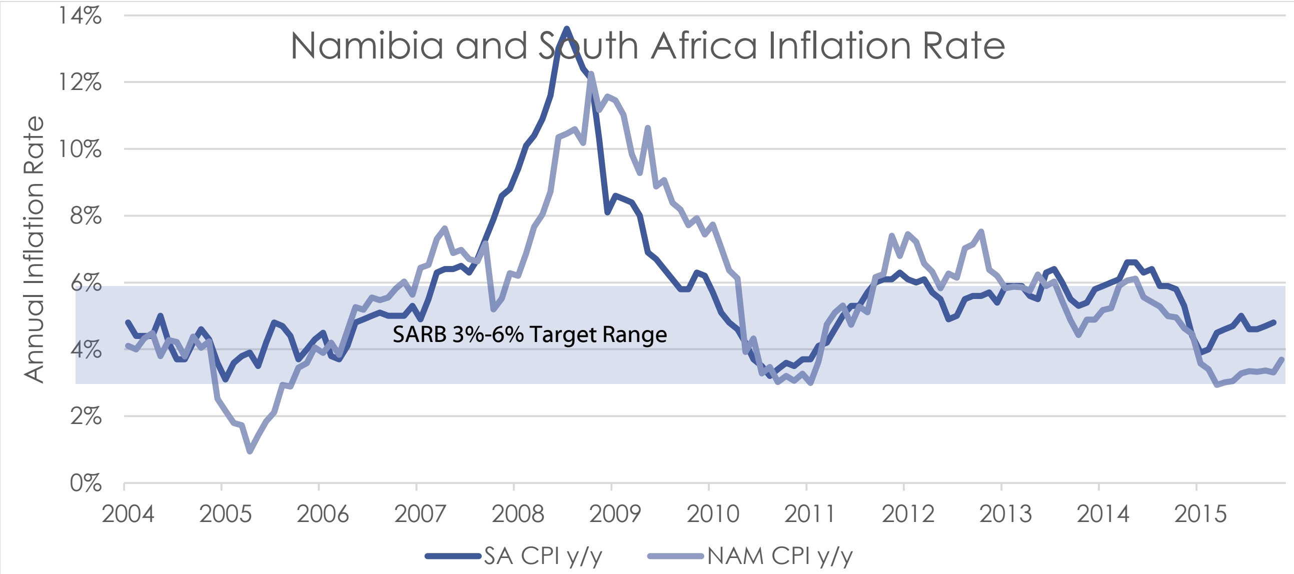
Going forward, our expectation is that tourism to remain one of the key drivers of growth in 2016 and 2017. This comes at a time when many other sectors are languishing and the economy as a whole is slowing. We expect real growth of 8.5% to have been recorded in 2015, and similar to be seen in 2016, before growth slows to 6.0% in 2017.



Source: Namibia Statistics Agency, IJG Securities

Inflation

Inflation in Namibia was low during 2015, largely due to a drop in the price of oil over the past year, and the knock on effects this has on prices of many heavy weighted basket items such as transport, food and non-alcoholic beverages and housing utilities, which experienced prolonged inflation below the basket average. With the effects of the drop in oil prices and the spillover effects thereof starting to work through the basket, coupled with a severe drought in the region together with the weakening of the exchange rate, we expect the Namibian inflation rate to pick up notably in 2016.



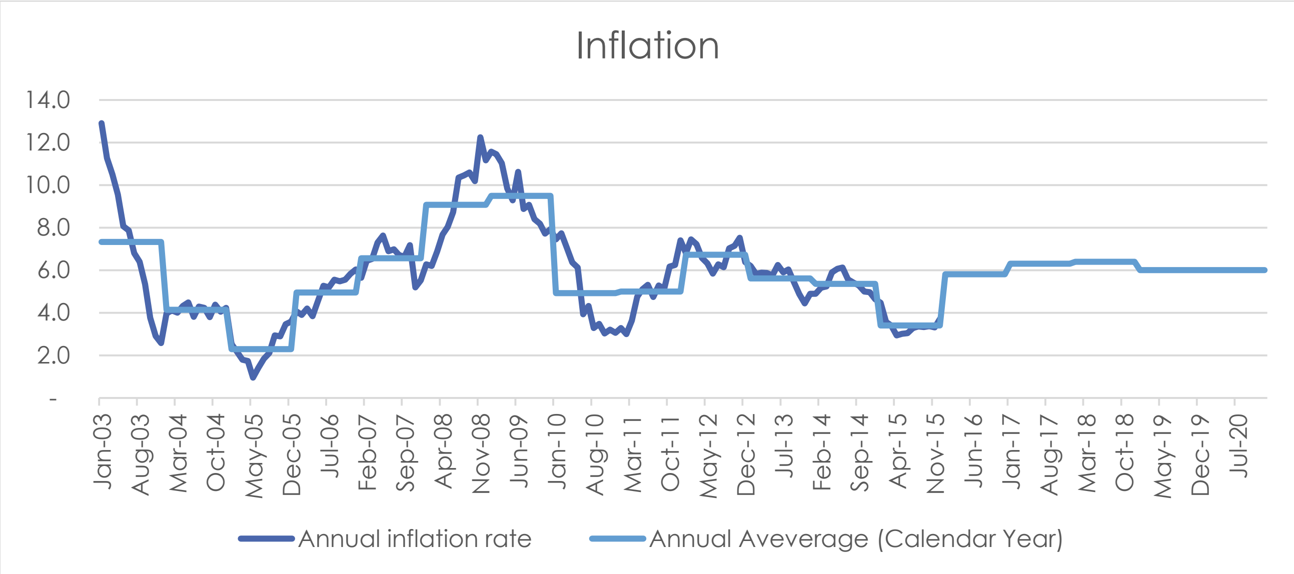
Source: Namibia Statistics Agency, Stats SA

After the major collapse in oil prices last year, the transport category of the inflation basket experienced year on year price contractions for 11 months in 2015, as it directly influenced fuel pump prices. However, the transport deflation started slowing down towards the end of the year. The transport basket category contributed positively to on overall inflation, exhibiting a 12-month average inflation of -2.1% by the end of 2015. The deflation experienced by this basket category is largely due to the operation of personal transportation equipment becoming less expensive. Prolonged lower fuel prices due to the oil rout have provided consumers with some relief worldwide and to a large extent in Namibia as well. While there has been a significant fall in oil price, fuel pump prices have not followed to the same extent, as the rand depreciated significantly over the last year, offsetting the fall in oil prices to a large degree.

Transport is the third largest basket category by weighting and as such has a large impact on overall inflation as the effects of cheap transportation flow through to many other basket categories, contributing to lower overall inflation.

When looking at the 12-month average inflation rate, accelerating price increases in the food and non-alcoholic beverages basket category was largely driven by meat prices rising relatively more quickly than in 2014, followed by milk, cheese & eggs as well as coffee, tea and cocoa price inflation accelerating. The food price increases could largely be ascribed to the drought currently experienced in Namibia and South Africa. Going forward we expect the drought to continue to have a major impact on food prices as there is already a shortage in food produced such as maize and wheat within the region. The drought, together with the depreciating Namibian dollar will have a significant impact on input costs of farmers and producers, which would flow through to the consumer.

We expect inflation to remain low for the first half of 2016 as oil prices have fallen further during January. However, we expect inflation to pick up drastically during the second part of the year as the full benefit of cheap oil is worked through the system, and the weak rand causes import prices to rise. Looming drought conditions as well as increasing utilities costs should see a further inflation pick up in basket categories such as food and non-alcoholic beverages, and alcoholic beverages and tobacco.



Source: Namibia Statistics Agency

Inflation forecasts:

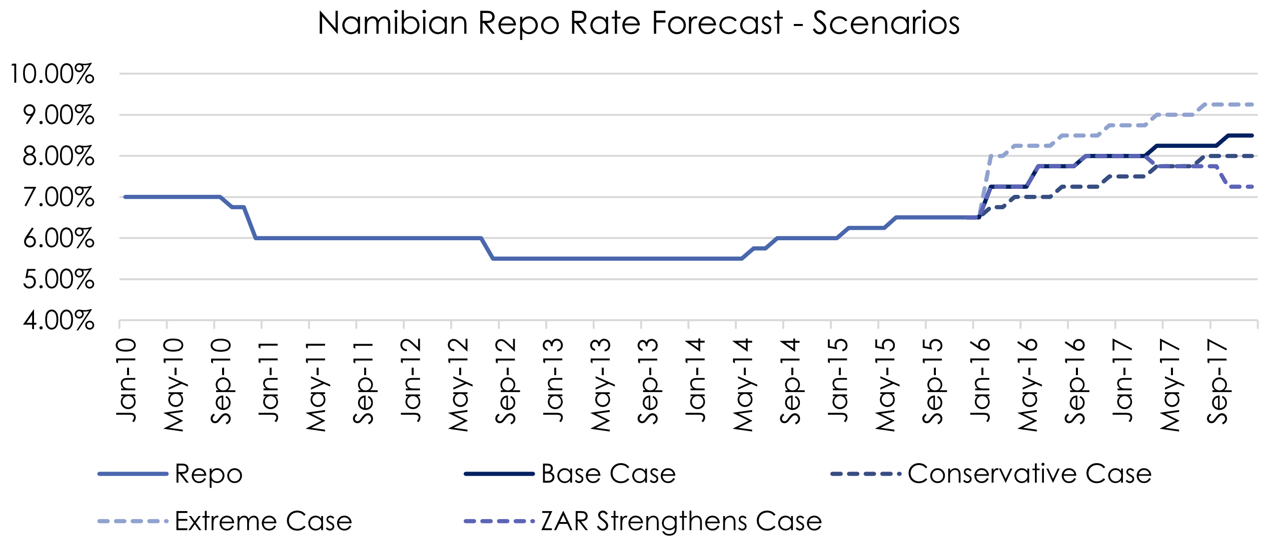
Actual						Forecast				
2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
4.9	5.0	6.7	5.6	5.4	3.4	5.8	6.3	6.4	6.0	6.0

Source: Namibia Statistics Agency, IJG Securities

Interest rates

Interest rates in South Africa and Namibia have been at or near historically low levels since the global financial crisis. Rates bottomed out in 2012 with the Namibia repo rate dropping to 5.5% during the year. Since then, the Bank of Namibia has administered four rate hikes of 25 basis points each. Thus monetary policy has been highly accommodative for a substantial period of time. As expected both private and public debt has increased greatly in both countries and government spending has over time gone from counter-cyclical, in an effort to promote growth, to pro-cyclical.

The recent outlook downgrade and credit ratings downgrade by Standard and Poor's and Fitch Ratings respectively as well as some ill-timed political maneuvers by the South African president, have sent the Rand, as well as bond yields, through the roof. Namibian and South African bond yields are approximately 100 basis points higher than they were at the start of December, and one year T-Bills are up by 75 basis points, while the Rand weakened by 34% against the US Dollar during 2015. Due to these movements there is little doubt that the SARB will be under pressure to hike interest rates at the January MPC meeting, and no doubt that we will see interest rate hikes during the year in order to protect the Rand. The SARB will be forced to sacrifice much needed monetary relief by hiking rates, but we feel that this is the most likely course of action as illustrated in the below scenarios figure. These scenarios are based off of our assumption that Namibia will replicate the steps taken by the SARB.



Source: Bank of Namibia, IJG Securities

Our base case scenario follows a gradual course of 200 basis points hikes over the next 2 years. At first rate hikes are large to counter the expected increase in inflation and stabilise the Rand. The magnitude of hikes decreases gradually over the timeframe to a point where the Namibian repo rate reaches 8.5% and stability within the SA economy allows for rates to remain at these levels for an extended period of time. The conservative case sees rates rise by 1.5% over the period via six individual 25 basis point hikes. The extreme case scenario sees a 150 basis point hike at the SARBs first MPC meeting with further hikes moderating somewhat. This scenario is driven by the Reserve Bank Governor's decision to stabilise the Rand by any means necessary. A final scenario sees the SARB hike rates aggressively at first and then gradually cutting rates to near current levels in order to support economic growth once the Rand trades back to pre-December 2015 levels.

The above scenarios assume that South Africa will be downgraded to a "junk" rating during 2016. Standard and Poor's is likely to be the first ratings agency to issue a sub-investment grade rating, possibly in March 2016. Standard and Poor's and Fitch Ratings' decisions to downgrade their respective outlooks and ratings in December effectively opened both agencies up to a ratings downgrade should the South African outlook change. Shortly after this the president removed the country's finance minister. This is exactly the type of action that could trigger the ratings agencies to react. Furthermore, the economic outlook has been under pressure due to the ongoing drought, social unrest, commodity price pressure and labour market tensions. This forms the basis for our view that we will see a credit ratings downgrade.

Historic Interest Rate Moves, SARB

	Largest Hikes			Largest Cuts	
	Repo After Hike	**Point Move**		**Repo After Cut**	**Point Move**
Sep-02	13.50%	1.00%	May-09	7.50%	-2.00%
Jun-02	12.50%	1.00%	Oct-03	8.50%	-1.50%
Mar-02	11.50%	1.00%	Jun-03	12.00%	-1.50%
Jan-02	10.50%	1.00%	Sep-01	9.50%	-1.50%
Jan-14	5.50%	0.50%	Mar-09	9.50%	-1.00%
Jun-08	12.00%	0.50%	Feb-09	10.50%	-1.00%
Apr-08	11.50%	0.50%	Sep-03	10.00%	-1.00%
Dec-07	11.00%	0.50%	Aug-03	11.00%	-1.00%
Oct-07	10.50%	0.50%	Jun-01	11.00%	-1.00%
Aug-07	10.00%	0.50%	Jul-12	5.00%	-0.50%
Jun-07	9.50%	0.50%	Nov-10	5.50%	-0.50%
Dec-06	9.00%	0.50%	Sep-10	6.00%	-0.50%
Oct-06	8.50%	0.50%	Mar-10	6.50%	-0.50%
Aug-06	8.00%	0.50%	Aug-09	7.00%	-0.50%
Jun-06	7.50%	0.50%	Dec-08	11.50%	-0.50%
Nov-15	6.25%	0.25%	Apr-05	7.00%	-0.50%
Jul-15	6.00%	0.25%	Aug-04	7.50%	-0.50%
Jul-14	5.75%	0.25%	Dec-03	8.00%	-0.50%
Oct-00	12.00%	0.25%	Jan-00	11.75%	-0.25%

Private Sector Credit:

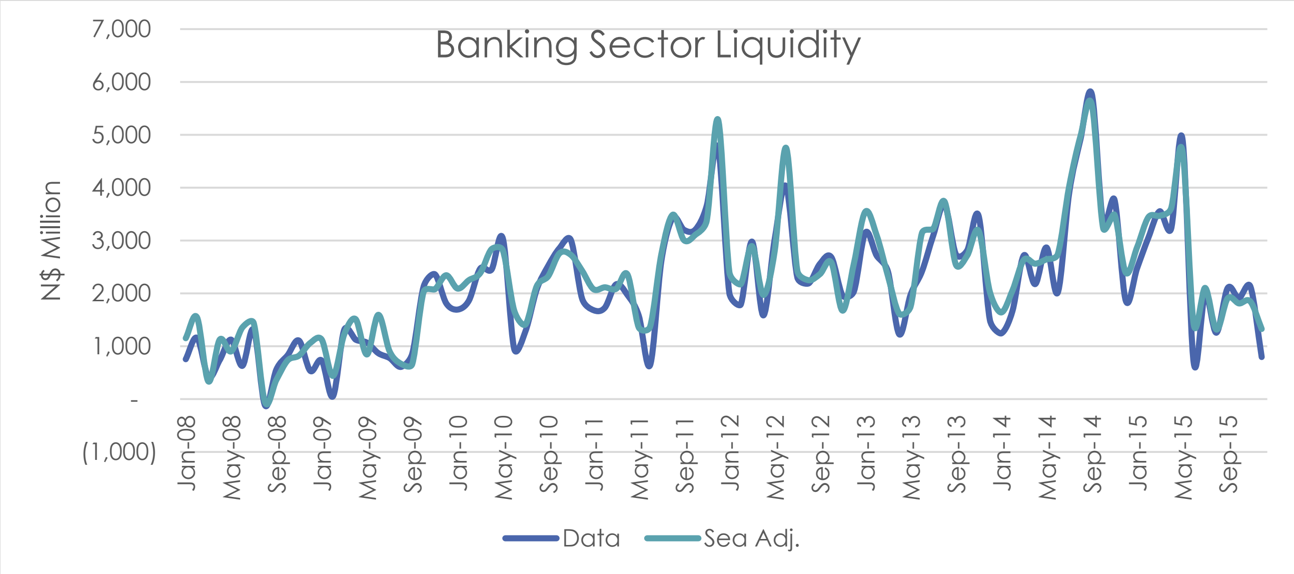
As we move through an interest rate hiking cycle, private sector credit extension, one of the key drivers of growth in the Namibian economy over recent years, is likely to come under ever increasing pressure. Strong growth in credit extension through the trough of the cycle has left many consumers highly indebted, and many corporates with heavily leveraged balance sheets.

After an extended period of extremely low interest rates, an additional challenge is looming in the Namibian banking sector, namely low liquidity. What we've seen over recent months is that the liquidity situation in the country has deteriorated markedly due to a number of factors. On the one hand, sustained long periods of low interest rates mean that the borrowing has been incentivised, while saving has been disincentivized. This has put the loan to funding ratios of the commercial banks under a fair amount of pressure. In addition to this, Government, previously a key provider of liquidity in market has come under severe financial pressure and simply does not have the funds that they used to have to deposit with the commercial banks (often via local authorities or state owned enterprises) and as well as this is becoming relatively slow when it comes to paying contractors, particularly for civil works, which of course means few deposits from such individuals and entities into commercial banks. Private sector credit extension growth for 2015, however, remained fairly strong at 14.5% (to November) driven by mortgage loans.

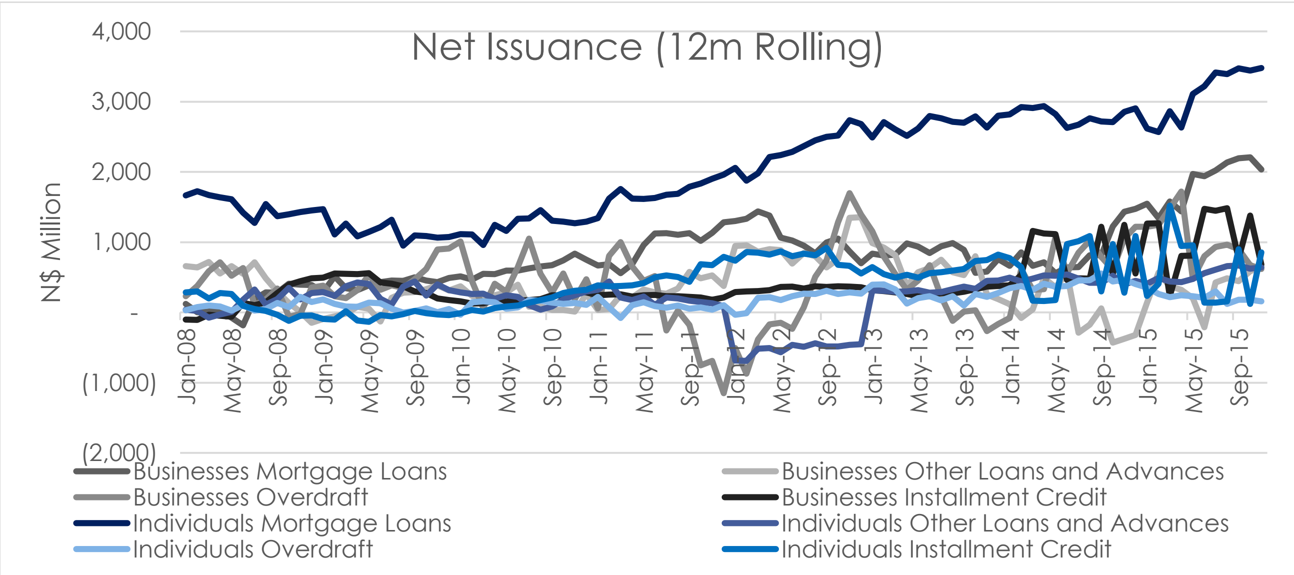
Going forward, the question remains that of whether the liquidity situation in the country will allow for further strong growth in credit extension, while increasing rates will also raise questions about the ability of banks to continue to growth their balance sheets without jeopardizing loan quality.

As such, private sector credit extension is expected to slow quite significantly over coming years, which is expected to not only have a negative impact on growth, but also on the earnings of the commercial banks and potentially, the property market in the country. With regards to the latter, constraints on disposable income, coupled with a rising interest rate environment is likely to contain price increases, which may be further added to by low liquidity and a reluctance to lend by commercial banks.

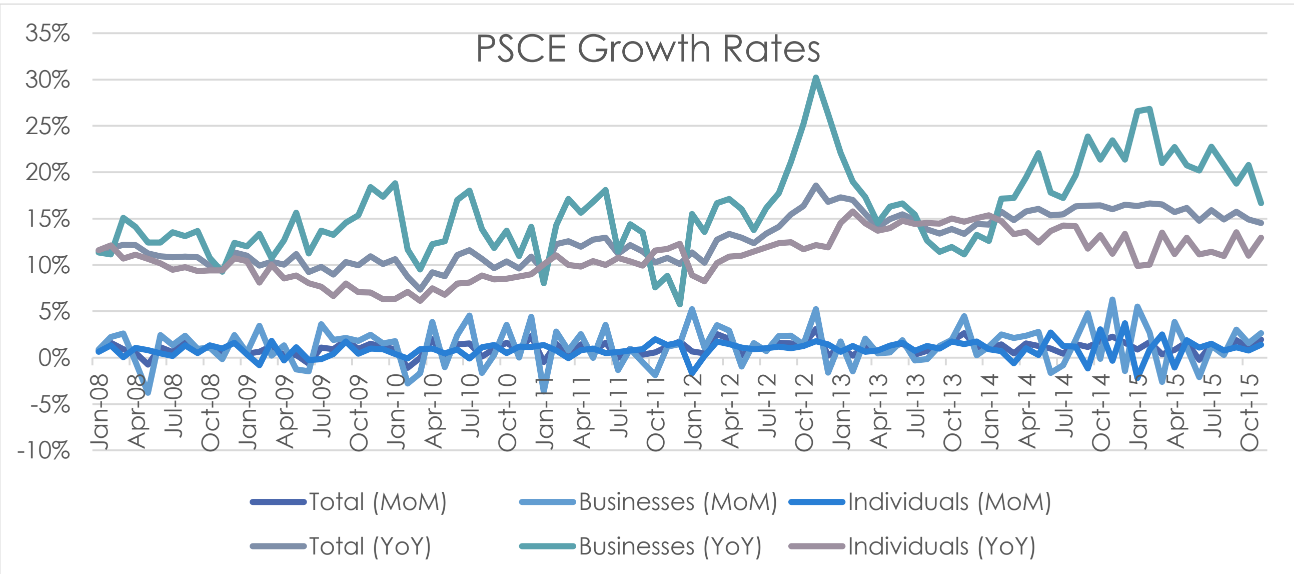
The rate at which interest rates stand to increase remains fairly unclear. Major rand weakness has turned the inflation outlook in South Africa for the worse, and may see the SARB hiking aggressively in an effort to protect the currency’s value, and maintain credibility. Should this happen, Namibia will be forced to follow suit, which will of course, incentivise saving over borrowing. Nevertheless the bottom line is that credit extension is expected to slow and our forecasts suggest that we will see private sector credit extension slow to 11.6% in 2016 and further to 9.8% in 2017. We expect remaining growth to be driven by mortgage loans particularly, as property supply constrains ensure that house prices remain elevated, despite consumer income waning. Further, we believe that commercial banks will continue to favour corporate lending over household lending, given the high level of household indebtedness in the country and the aforementioned disposable income squeeze.



Source: Bank of Namibia



Source: Bank of Namibia, IJG Securities



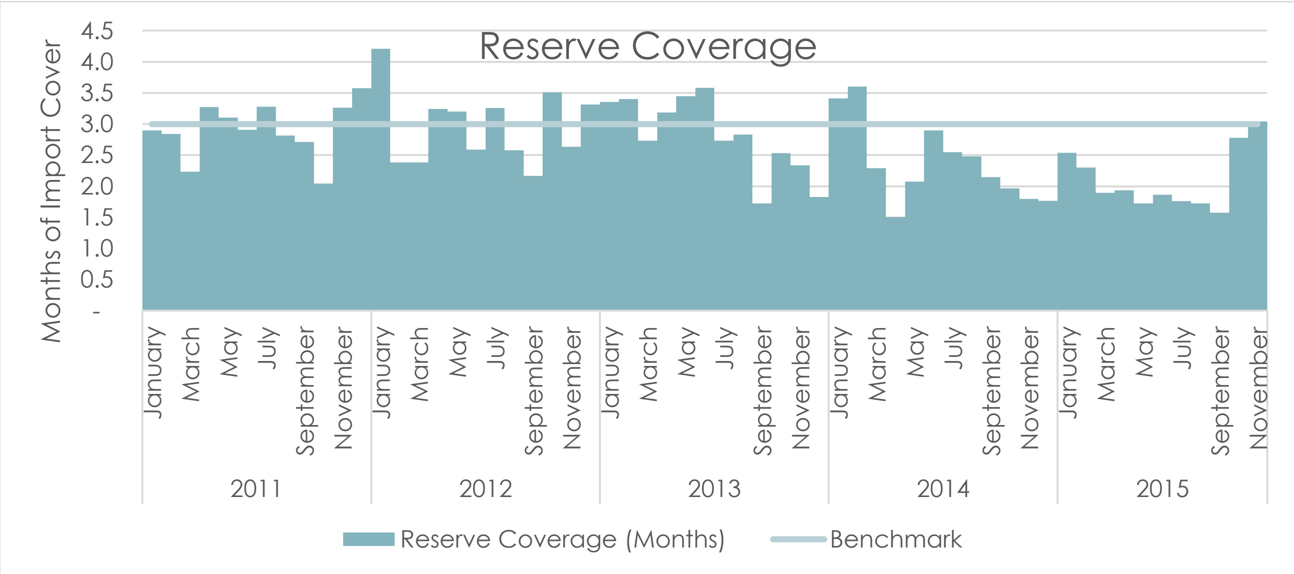
Source: Bank of Namibia, IJG Securities

BOP

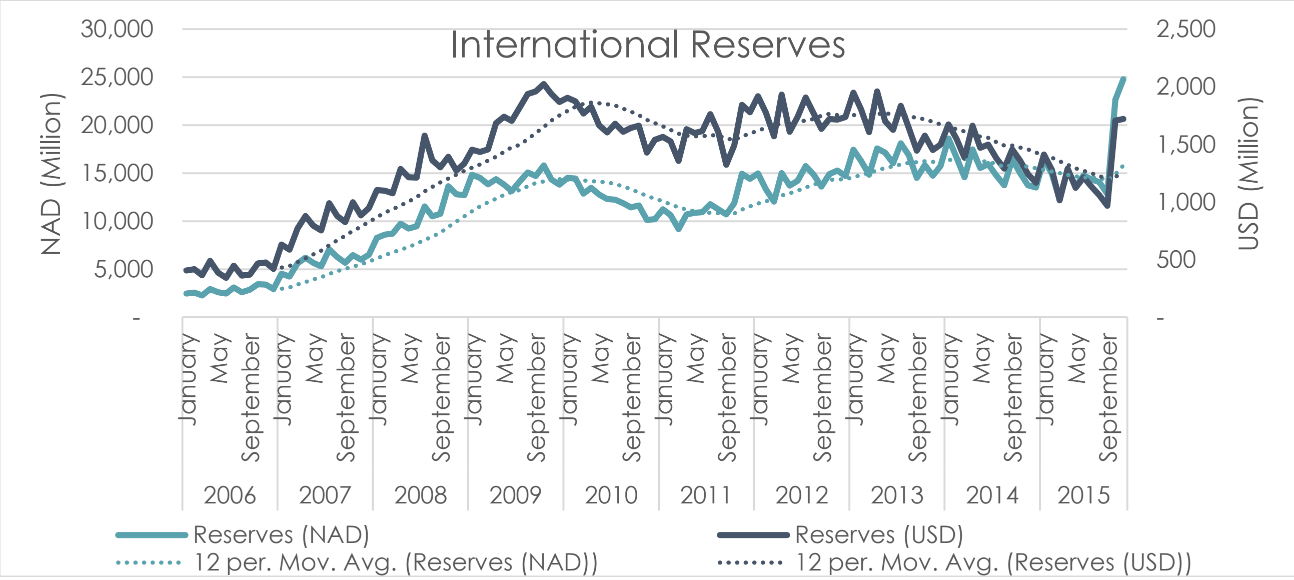
The balance of payments for Namibia has remained under pressure for a number of years, driven particularly by exceptional import volumes when compared to the historical norms of the country. In part, this is due to the abnormally high levels of construction activity that took place between 2012 and 2015, led by the construction of three mines, major public works programmes and retail floor space development. In addition to this, however, major fiscal and monetary expansion has also spurred private purchases of imported goods, as low interest rates, high government spending, wage settlements above inflation, and income tax cuts, buoyed the disposable income of local consumers.

While the growth in imports has run rampant over recent years, export growth has been largely stagnant over the same period, and as a result, the current account has experienced large deficits and is expected to register a deficit of 8.6% of GDP in 2015.

While the capital and financial account has been positive, on an annual basis, every year since 2008, the magnitude of the inflow has not been adequate to offset the net outflows on the current account, and as such the overall balance of payments was negative in 2014, and would have been highly negative in 2015 had it not been for external debt issuance by the Government. As a result of the major deterioration in the external position through 2015, the Ministry of Finance was forced to issue hard currency debt in order to protect the country's external position, as months of important cover fell well below the three-month prudential limit, to a low of 1.6 months in September 2015, presenting a very real rating downgrade risk to the country. As such, a sizable component of the external funds raised are to be ring-fenced to protect the external position.



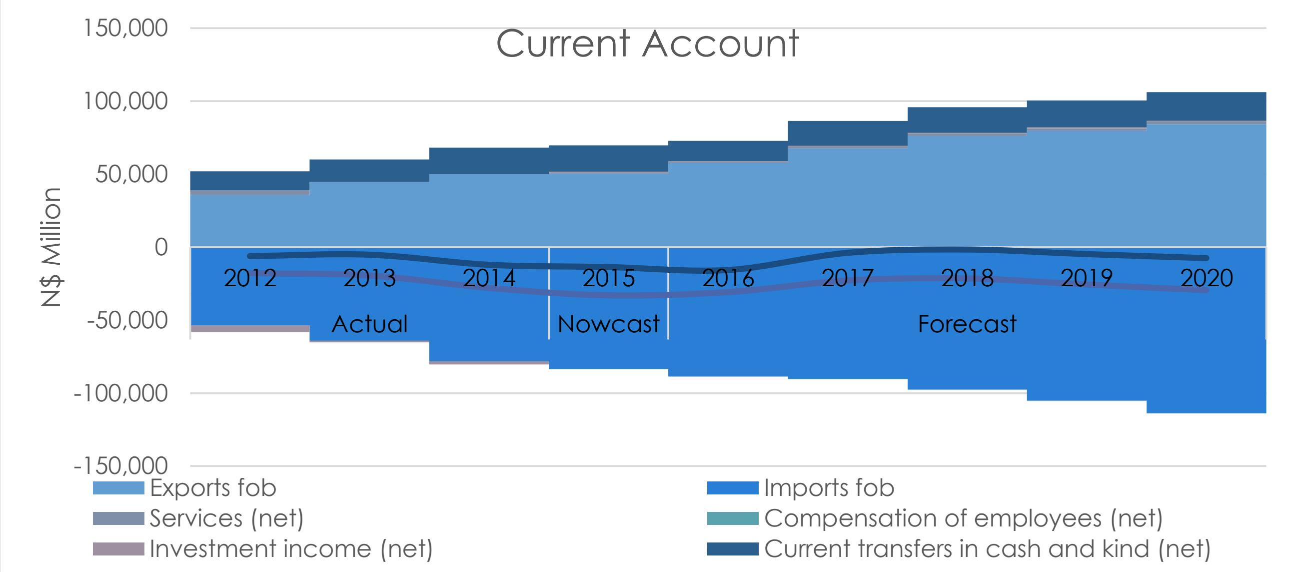
Source: Bank of Namibia, IJG Securities



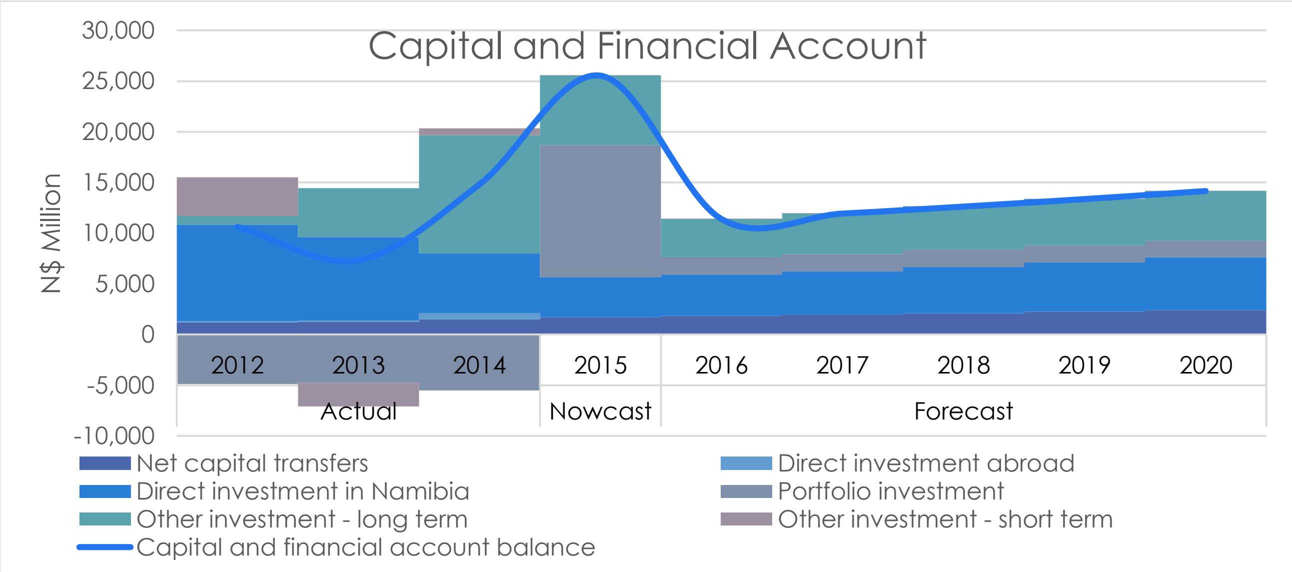
Source: Bank of Namibia, IJG Securities

Going forward we expect the balance of payments to remain under severe pressure in 2016 largely due to three factors. Firstly, while imports are expected to decline somewhat, due to the fact that much of the construction activity in the country is now coming to an end or winding down, the rand moves seen recently will result in a major dampening in this decline, as the price of other imports increase on the back of rand weakness. Secondly, while exports are expected to grow in a fairly healthy manner, largely as a result of increases in mineral exports, specifically gold from the new Otjikoto mine and copper from the new Tschudi mine, this increase is not significant enough to close the gap on imports generated over recent years. Finally, SACU receipts, also recorded on the current account, are expected to decline fairly sizably this year, largely due to the fact that the country was overpaid by SACU in 2014 and now repayment of N$3 billion is expected to be made to SACU in the coming fiscal year of Government. This repayment will simply take the form of lower receipts received from the customs union, rather than an actual repayment, but will be seen as a lower-than-normal flow on the current account. As such the current account is likely to remain under severe pressure in 2016 and we expected us to see a current account deficit of approximately $15 billion representing 8.5% of GDP. From 2017 onwards, we expect to see major improvement in the current account, driven particularly by exports from the new uranium mine, which will be ramping up to full production through 2017. Nevertheless, we still expect the current account to remain negative but not as negative as was the case in 2015 and 2016. On the capital and financial account side we expect to receive continued net inflows meaning that the account will be positive in 2016 as is usually the case. However, the extent of the inflows will once again not offset the outflows on the current account in 2016, but will do so once again from 2017, all things being equal. As such, in 2017 and possibly thereafter, we should see the balance of payments turn positive. A key development on the capital and financial accounts side of the balance of payments in 2016, will be the reduction in foreign direct investment into Namibian following a number of years of extremely strong foreign investment into the country, particularly for the development of the three new mines.

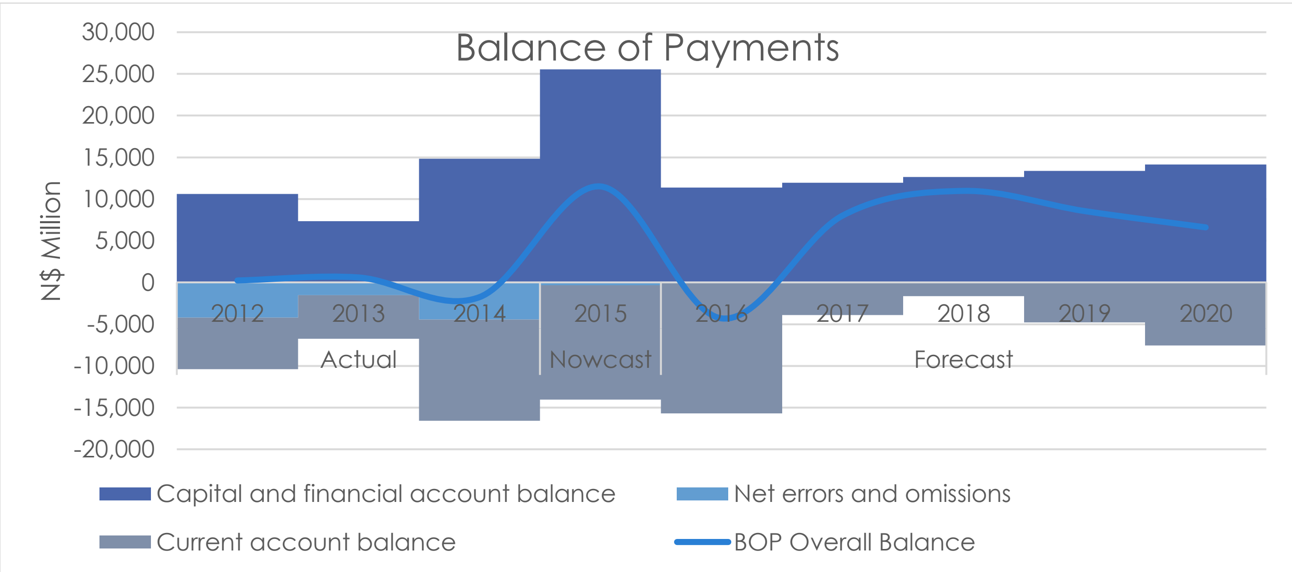
One additional noteworthy development on the capital and financial account side of the balance of payments is the ever increasing noise with regards to amendments to the Regulation 28 which stipulates the local asset requirements of pension funds and life insurance companies. At a number of events and in a number of speeches, the Minister of Finance has mentioned his intention of increasing the local asset requirements from their current 35% level, which would result in major inflows into the country from the common monetary area, primarily, as asset managers managing the funds of pensioners and life insurance companies will be forced to bring funds back into Namibia in order to meet the local asset requirements. This will of course register as a positive flow on the capital and financial account, however as little detail currently exists as to the nature and timing of these regulation changes, we have not taken these flows into account in our forecast, and will only do so once more information becomes available.



Source: Bank of Namibia, IJG Securities



Source: Bank of Namibia, IJG Securities



Source: Bank of Namibia, IJG Securities

	Actual			Nowcast	Forecast				
Million	2012	2013	2014	2015	2016	2017	2018	2019	2020
Current Account									
1. Merchandise trade balance	(17,753)	(19,281)	(27,865)	(32,955)	(26,171)	(17,434)	(17,015)	(21,707)	(25,305)
2. Exports fob	35,835	44,724	50,055	50,473	62,263	72,769	80,404	83,505	88,324
Diamonds	8,250	11,698	14,005	14,352	12,541	13,955	14,234	14,519	15,632
Other mineral products	6,975	7,421	7,284	8,657	18,701	25,030	29,782	29,641	32,071
Food and live animals	3,672	4,386	4,131	4,473	4,725	5,191	5,272	5,452	5,638
Manufactured products	6,564	7,379	9,638	8,615	11,057	12,439	13,993	15,743	15,744
Other commodities & Re-exports	10,373	13,841	14,997	14,377	15,239	16,154	17,123	18,150	19,239
3. Imports fob	(53,588)	(64,005)	(77,920)	(83,428)	(88,434)	(90,203)	(97,419)	(105,212)	(113,629)
4. Services (net)	3,114	105	(950)	505	533	1,487	1,583	1,684	1,793
5. Compensation of employees (net)	(56)	(57)	(32)	(56)	(60)	(65)	(70)	(76)	(82)
6. Investment income (net)	(4,445)	(1,173)	(1,462)	794	618	607	592	571	546
7. Goods, services and income balance (2 to 6)	(19,140)	(20,405)	(30,309)	(31,712)	(25,082)	(15,405)	(14,911)	(19,528)	(23,049)
8. Current transfers in cash and kind (net)	12,973	15,212	18,165	18,007	13,920	16,779	17,558	18,534	19,570
Gov't - current transfers	12,837	15,050	18,027	17,880	13,887	16,743	17,519	18,493	19,526
- from SACU	12,131	14,494	17,269	17,374	12,859	15,842	16,634	17,632	18,690
Private - current transfers	137	162	138	127	34	36	39	41	44
9. Total current account balance (7+8)	(6,167)	(5,193)	(12,145)	(13,705)	(11,161)	1,374	2,647	(993)	(3,479)
Capital and Financial Account									
1.Net capital transfers	1,218	1,246	1,495	1,718	1,837	1,964	2,100	2,245	2,401
2.Direct investment abroad	92	127	626	(21)	(21)	(21)	(21)	(21)	(21)
3.Direct investment in Namibia	9,527	8,234	5,893	3,935	4,092	4,266	4,565	4,884	5,226
4.Portfolio investment	(4,880)	(4,751)	(5,520)	13,011	1,727	1,705	1,683	1,658	1,632
Equity	(1,800)	(2,001)	(3,176)	1,605	30	30	30	30	30
Debt	(3,080)	(2,749)	(2,344)	11,406	1,696	1,675	1,652	1,628	1,602
5.Other investment - long term	858	4,823	11,629	6,878	3,741	4,001	4,280	4,577	4,896
General Government	(64)	(14)	(74)	601	(418)	(418)	(418)	(418)	(418)
Monetary authorities	99	336	125	499	499	499	499	499	499
Banks	(2)	(53)	(66)	(57)	(57)	(57)	(57)	(57)	(57)
Other sectors	826	4,555	11,644	5,834	3,716	3,976	4,254	4,552	4,871
6.Other investment - short term	3,809	(2,350)	695	16	17	18	19	20	22
Banks	3,714	(1,550)	407	(424)	(453)	(485)	(519)	(555)	(594)
Other sectors	95	(801)	288	439	470	503	538	576	616
7. Capital and financial account balance	10,624	7,330	14,819	25,537	11,393	11,934	12,625	13,365	14,156
8.Net errors and omissions	(4,227)	(1,539)	(4,442)	(318)	-	-	-	-	-
BOP Overall Balance	231	598	(1,768)	11,514	232	13,308	15,272	12,371	10,677
Reserve Balance	14,729	15,736	13,968	25,482	25,713	39,021	54,293	66,664	77,341
Δ Reserves	323	1,007	(1,768)	11,514	232	13,308	15,272	12,371	10,677

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