Analysis of Namibia's latest sovereign ratings
Presented at the NPC Multi-stakeholder Forum

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Role of rating agencies

- Three major rating agencies – Standard & Poor, Moody, Fitch
- Namibia engaged Moody and Fitch
- Assess country and company risks to inform potential investors
- Assessment usually based on country visits and extensive stakeholder consultations (Government, Private Sector, Research institutions)
- Companies can't be better rated than a country
- Rating influences cost of borrowing
- Rating agencies follow the same scale, but Moody's uses different scores than S&P and Fitch

Rating scales

Grade	Moody's	S&P	Fitch
Prime	Aaa	AAA	AAA
High grade	Aa1	AA+	AA+
	Aa2	AA	AA
	Aa3	AA-	AA-
Upper medium grade	A1	A+	A+
	A2	A	A
	A3	A-	A-
Lower medium grade	Baa1	BBB+	BBB+
	Baa2	BBB	BBB
	Baa3	BBB-	BBB-
Non-investment grade speculative	Ba1	BB+	BB+
	Ba2	BB	BB
	Ba3	BB-	BB-
Highly speculative	B1	B+	B+
	B2	B	B
	B3	B-	B-
Substantial risks	Caa1	CCC+	CCC+
	Caa2	CCC	CCC
	Caa3	CCC-	CCC-

Moody's assessment

11 August 2017 downgrade from Baa3 to Ba1 (non-investment grade) with negative outlook

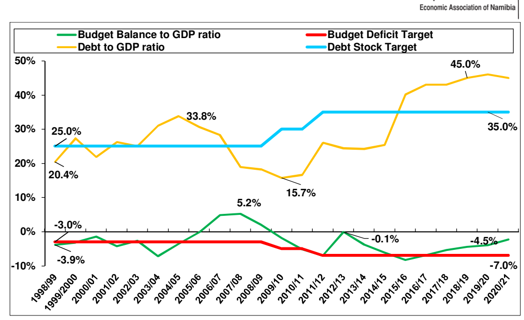
- Assessment based on desk top research; no country visit
- Three main factors:
  - Erosion of Namibia's fiscal strength due to fiscal imbalances and rising public debts (incl. potential deterioration of SACU revenue)
  - Limited institutional capacity to manage shocks and address long-term structural fiscal rigidities
  - Risk of renewed government liquidity pressure in coming years

Fitch assessment

20 November 2017 – downgrade from BBB- to BB+ (non-investment grade) with stable outlook

- Based on country visit and extensive stakeholder consultations
- Main reasons included:
  - Government missed own fiscal targets (deficits, debt)
  - Previously unreported arrears of NAD2.7 billion highlight shortcomings in management of public finances
  - Rising wage bill might not be addressed owing to upcoming elections
  - Lower than expected economic growth in 2017 and hence lower revenue
  - Exchange rate risks for hard currencies loans
  - Loss making Public Enterprises
  - Current account deficit
  - Policy uncertainties (NIPA, NEEEF) expected to ease after SWAPO Party Congress

Budget deficit and public debts

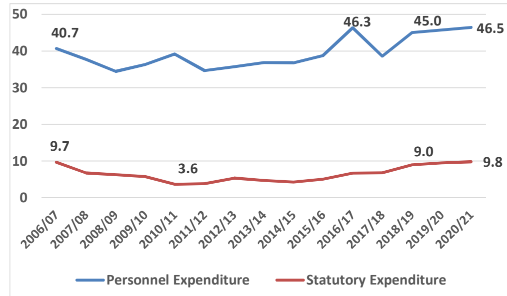


Budget deficit and public debts cont.

- Deficit within current fiscal target (7.0%), but outside the previous more ambitious target of 3.0% and of SADC Convergence Criteria
- Public debt exceeds target of 35% and is expected to rise, despite declining deficit.
- Domestic debt stock accounts for 65% of total public debt; foreign for 35%
- Debt ratio remains within SADC Convergence Criteria (60% of GDP), but is reportedly at upper end of peers of upper middle-income countries
- Debt ratio benefited recently from currency appreciation, but suffers from economic contraction / low growth (GDP is the denominator)

➢ Reducing debt ratio will take more time than previously expected, while currency risk remains.

Selected expenditure items



Selected expenditure items cont.

- Personnel expenditure absorb 45.0% of total budget and is increasing (46.5% in 2020/21)
- Statutory expenditure (interest payments) account for 9.0% of total expenditure and is expected to increase to 9.8%, which is close to Namibia's own fiscal target of 10.0%

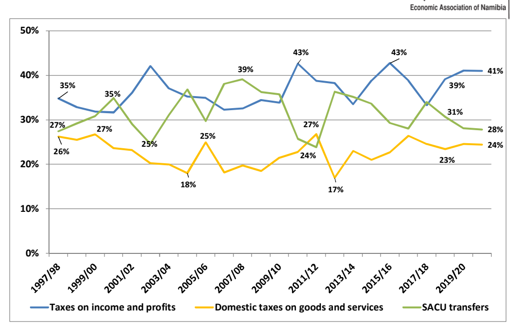
➢ Comprehensive strategy needed to address high wage bill – review of public sector structure required (ministries, directorates etc.)

➢ Identify overlapping functions of ministries etc.

➢ Resignations, retirements etc. neither sufficient to address high wage bill nor targeted

➢ Medium to long-term strategy needed for developing a lean, efficient and effective public sector

Revenue sources



Revenue sources cont.

- Taxes on income and profits expected to increase from NAD19.2bn (2017/18) to NAD22.2bn (2018/19) and NAD25.1bn (2020/21) despite subdued economic growth.
- Domestic taxes on goods and services (VAT, fuel levy, fishing quota levy, environmental tax) expected to decline from NAD14.2bn (2017/18) to NAD13.3bn (2018/19) before increasing to NAD15.0bn (2020/21)
- Taxes on international trade (SACU transfers) expected to decline from NAD19.6bn to NAD17.4bn (2018/19) and NAD16.2bn (2019/20) before recovering slightly.
  - Low growth in RSA (0.9% for 2018 and 2019) and stronger currency impacts on imports and SACU revenue
  - However, improved political environment could attract more investment and stimulate growth

➢ SACU transfers strongly influenced by economic performance of RSA

➢ Declining share of SACU transfers not due to diversification of revenue sources, but caused by actual decrease of SACU transfers

➢ New taxes expected to contribute about NAD0.5bn

Other concerns raised

- Public Enterprises – Strengthen governance structure, without increasing shareholder's interference in PE operations
- Current account deficit - trade deficit during first three quarters of 2017 higher than in 2016 although completion of major infrastructure projects would have suggested otherwise.
- Foreign exchange reserves – improvement owing to AfDB loan, 'repatriation' of investment abroad due to changes in Regulation 28 etc., but not due to improving trade balance (increasing exports and declining imports)

Potential consequences of the downgrade

- Could affect investment decisions (incl. into PPPs), but assessment of sovereign rating agencies one of the factors potential investors take into account
- Could increase borrowing costs in the medium term for government, Public Enterprises and private sector companies due to perceived higher risk

Recommendations

- Create conducive environment for domestic and foreign direct investment in order to diversify the economy, increase value of exports and substitute imports, create employment and raise revenue
- Develop strategy to address high wage bill
- Enforce accountability at O/M/As and PEs
- Ensure value for money for capital projects (external evaluators for tender documents and bids)
- Establish forum for regular, structured, high-level consultations with private sector
- There remains room to improve the effectiveness of the budget (PSEMAS subsidy – NAD2.1 billion, VAT exemptions, lack of stock controls, payroll etc.)

Thank you for your attention

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