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## **MACROECONOMIC DETERMINANTS OF ECONOMIC DIVERSIFICATION IN BOTSWANA**

### **Abstract:**

Botswana, a sparsely populated middle income developing country in Southern Africa has been dependent on a single resource, diamond. Despite having high growth and high percapita incomes, the rates of unemployment and poverty have been quite high. Hence, the government has put in intense efforts towards diversification of the economy, but the success rate has been dismal. Some limited degree of diversification has occurred in the services sector. Even the latest government budget gives a great deal of importance to the diversification drive. Hence it is imperative to take a look at the factors that drive to the limited diversification observed so far and to see what lessons can be learned from that for taking further steps towards the desired goal.

From the literature and from an understanding of the Botswana economy, the following explanatory variables were picked up to run a multivariate regression model. GDP Growth Rates, Share of Mining Output in GDP, Ratio of Gross Fixed Capital Formation to GDP, Ratio of Public Expenditure to GDP, Share of Tax Revenues in GDP, Annual Rate of Inflation, Share of Total Trade in GDP as a proxy for openness, Ratio of FDI to GDP and Exchange Rate. We took the coefficient of variation of sectoral shares as a proxy for economic diversification. Gross fixed capital formation and public expenditure were dropped as they were found to be highly collinear with some other variables. The estimates are found to be very robust with Adjusted R<sup>2</sup> as high as 0.94. Mining GDP, Share of Taxes, Exchange Rates and GDP Growth are found to be significant at 5% level. Inflation is significant at 10% level. The study shows that still Mining share seems to be the driver of the limited diversification in Botswana. Higher the share of taxes, higher is the degree of diversification. An appreciation in exchange rates seem to be encouraging imports of inputs for various sectors to assist the diversification process. A negative sign for growth rates show that the efforts to diversification becomes effective, when the economy grows slowly and diversification happens to be the only way out. Inflation also affects diversification inversely.

The Policy implication of the study is that the revenues from mining will have to be used prudently to effect diversification in the economy. Appropriate fiscal and monetary policies will have to be put in place to promote the diversification process in the economy.

### **Keywords:**

Botswana, Economic Diversification, Macroeconomic determinants, Multivariate Regression, Policy implications

**JEL Classification:** E27, A10, O11