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**AN
ASSESSMENT OF THE CONSTRUCTION INDUSTRY IN
BOTSWANA**

A report from

BOCCIM

The Botswana Confederation of Commerce, Industry and Manpower



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EXECUTIVE SUMMARY

The postponement and cancellation of contracts by the Botswana Housing Corporation in 1992 led to a 300 million pula decline in the gross output of Botswana's construction sector. Of the work that was completed last year, approximately 410 million pula went to foreign contractors. In addition, approximately 521 million pula was spent on foreign sourced materials and supplies. In the aggregate, the direct and indirect effects on Botswana is that the country loss between 561 million and 708 million pula of potential GDP and a potential loss of between 12,369 and 13,452 of local employment.

Had Botswana's building materials manufacturers been fully utilised last year, the country would have saved between 109 million pula and 135 million pula. The country is self sufficient with respect to face bricks, cement bricks, paint, timber trusses, window and door frames, yet government continues to specify foreign products. Government's impact on the construction industry is not insignificant. Nearly 90 percent of all the construction work in Botswana emanates from the government and its parastatals. Of that amount, nearly 60 percent is being undertaken by foreign based companies.

To address these concerns, BOCCIM recommends, among other things, that (1) a minimum percentage of all government work be "set-aside" for the local construction industry, (2) government implement a Botswana Procurement Policy, (3) laws, regulations and procedures be applied equally to foreign and local companies, (4) the Local Preference Scheme and the Financial Assistance Programme be strengthened to ensure Botswana's competitiveness, (5) a bureau of standards, a Code of Conduct and some form of professional registration be introduced, (6) the Central Tender Board be strengthened by specifying local products, and (7) government develops a national policy on Botswana business utilisation.

At a time when the country faces an appreciable decline in revenues due to the reduction in diamond sales, it cannot continue to permit the massive outflow of capital to be paid to foreign companies for services and products which are readily available through local contractors and manufacturers. BOCCIM urges government to seriously consider these recommendations.

SUMMARY OF FINDINGS AND CONCLUSIONS

1. Over the past decade, the construction industry has been a major contributor to the growth of Botswana's GDP providing approximately 20 percent per annum to the economy.
2. Within the private sector, over the last decade, the construction industry has been the second largest formal employer both in raw numbers and percentage distribution with the percentage of employment being fairly consistent at approximately 12.7 percent.
3. The local building industry manufacturing sector is generally uncompetitive compared to the equivalent sector in South Africa. It is approximately five percent the size of its South African counterpart.
4. It is estimated that between 272 million pula and 334 million pula was spent in 1992 on importing building materials and components, most of which came from South Africa.
5. Were Botswana to have fully utilised existing local industry to provide such materials and components, the country could have saved between 109 and 135 million pula of that amount.
6. Based on a consideration of installed capacity of local manufacturers, Botswana could be self-sufficient with regard to face-bricks, cement bricks, paint, timber trusses, and window and door frames. Existing capacity is underutilised mainly due to imports from South Africa.
7. Government does specify local manufacturers of window and door frames in contracts and similarly local sub-contractors are also specified for solar water heating systems. However no other local products are specified.
8. Government continues to specify foreign products even where local alternatives are available due to ignorance of what is available locally and perceived problems with quality and product range.
9. Although numerous allegations have been made about dumping by South African firms, there is no conclusive evidence of such unfair practices.
10. Government and the various parastatal agencies account for more than 87 percent of Botswana's on-going construction work.

11. The arrival of foreign contractors in early 1990 in conjunction with an over-traded construction industry, contributed to a reduction in tender prices by 30 percent during 1991-1992.
12. Approximately 570 million pula of building contracts are currently postponed, 80 percent of which is attributed to the BHC.
13. Approximately 140 million pula of BHC contracts scheduled for 1992 were cancelled.
14. Contract curtailments created nearly a 190 million pula decline in expected GDP for 1992.
15. The value of active contracts above 10 million pula in 1992 is estimated to have been 560 million pula of which almost 56.6 percent is being undertaken by foreign based companies.
16. Based on Central Tender Board classifications, most local contractors do not qualify to undertake work over 4 million pula.
17. Local contractors are only able to tender for 18 percent of all work currently ongoing and have had to rely on subcontractor work to survive in 1992.
18. Since 1988, 60 companies have been awarded Local Preference Scheme certificates of which only 11 are directly connected with the building industry.
19. Based on the study and its underlying survey, three basic assumptions can be made about Botswana's construction sector for 1992:
 - ▶ an estimated decline in gross output of over 300 million pula will result from contract postponements and cancellations by BHC;
 - ▶ approximately 521 million pula will have been spent on foreign sourced materials and supplies by contractors doing work in Botswana; and
 - ▶ foreign contractors in Botswana will have captured approximately 410 million pula of the total amount of contract work done by contractors for the year.
20. The direct and indirect aggregate effects of these three factors on Botswana's economy results in an estimated "Total Unrealised GDP" which includes:
 - ▶ an estimated loss of between 651 and 708 million pula of potential GDP, and
 - ▶ the potential loss of between 12,369 and 13,452 of local employment. Nearly half of this loss would be borne by the construction sector.

SUMMARY OF RECOMMENDATIONS

1. Government should develop a National Policy on Botswana Business Utilisation. [pg.21]
2. Government should consider implementing a Botswana Procurement Policy Strategy. [pg.21]
3. A minimum percentage of all government and parastatal construction expenditure should be "set aside" and used to develop and stabilise local industry. [pg.22]
4. Large government contracts should be sub-divided into more modest units and reserved for smaller companies. [pg.23]
5. Local Preference Scheme should be extended to cover contractors, professionals, wholesalers/retailers, complimentary and downstream manufacturers. [pg.23]
6. Under the Local Preference Scheme, government should consider a mechanism that would permit direct payments to sub-contractors. [pg.23]
7. A sales tax subsidy on machinery and raw materials should be included in the Financial Assistance Programme as well as a subsidy on factory costs to ensure price competitiveness against South African firms. [pg.24]
8. The Financial Assistance Programme as modified, should be extended over ten years. [pg.24]
9. The tendering procedures of the Central Tender Board need to be strengthened by specifying nominated suppliers in contracts. [pg.26]
10. A Ministry of Commerce representative should be involved with the assessment of tenders above certain amounts and certify the consideration of Local Preference Scheme certificates in awarding tenders. [pg.26]
11. A joint industry -- government task force should be formed and tasked with the assignment of establishing an industry wide Code of Conduct [pg.27]
12. It is imperative that some form of professional registration to regulate the construction industry. [pg.26]
13. Government needs to establish an industry-wide bureau of standards. [pg.21]
14. Government enforce and equal apply the laws and regulations governing the construction industry to the foreign as well as domestic construction industry. [pg.22]

1 INTRODUCTION¹

- 1.1 Within the past 12 months, the construction industry² in Botswana has suffered a precipitous decline in turnover and earnings which has necessitated a significant reduction in employment. The prolonged contraction in the industry may have caused irreparable and permanent damage to many local firms³ which have made major and sustained contributions to the country's overall productivity and prosperity.
- 1.2 In a special report issued in July, 1992, BOCCIM expressed grave concern over the difficulties confronting producers of manufactured/fabricated components for the industry and made several recommendations to the Ministry of Finance.⁴ At the same time, and with respect to the industry more generally, BOCCIM commissioned the Botswana Technology Centre ("BTC") to undertake a comprehensive study to determine more precisely the impact and implications of the contractions in the construction industry. The purpose of the BTC study was to permit BOCCIM to formulate recommendations on specific policy initiatives for government consideration which might afford the construction industry a measure of short-term relief and over time strengthen the sector so that it may continue to be a source of substantial employment and profitability.

¹ This report is based in part on materials and data presented in the BOCCIM Special Study of 8th July 1992 and a BOCCIM commissioned study conducted by the Botswana Technology Center dated October 1992.

² For purposes of this report, the construction industry is defined as encompassing contractors, professionals, manufacturers and wholesalers and retailers.

³ For purposes of this study, BTC defined a company as "local" if (1) it is majority Botswana owned or (2) is locally registered with a locally functioning office, has been in Botswana at least five years, has had an active localisation policy and is investing in the local economy (i.e. training, etc.).

⁴ See BOCCIM's Special Study: *"Manufactured/Fabricated Components for the Construction Industry"* which was presented to the Permanent Secretary for the Ministry of Finance and Development Planning on 8th July 1992.

- 1.3 While the purpose of the study was to assist BOCCIM in developing policy recommendations, the study's fundamental objective was to assess the feasibility and desirability of specifying local manufacturers of building materials for construction contracts and thereby developing a viable locally based construction sector. This objective is critical to BOCCIM because as noted by the BTC study:

In the light of the explicitly stated objectives of The National Development Plan 7 (NDP7) i.e. the diversification of the economy and the move away from the over dependence of the country on diamonds, self sufficiency in key sectors is critical. Indeed one such sector is the building industry which accounts for millions in lost revenues to the country due to the considerable importation of building materials and services from abroad.⁵

- 1.4 The primary impetus for the study came from two concerns expressed by industry representatives in Botswana: that local construction companies and building material manufacturers were suffering contraction of business volume and financial losses due to the effects of foreign competition, and that local building material manufacturers were encountering resistance in their efforts to penetrate local markets both in the public and private sector. In the terms of reference prepared for BTC, BOCCIM expressly requested a study "documenting the extent of overcapacity in the Botswana construction industry, the root causes of the problem, and the costs and benefits of requiring increased usage of local construction firms and locally manufactured building materials in projects constructed under government and other contracts."
- 1.5 Of principle concern to BOCCIM is (1) the extent of excess capacity among Botswana construction firms and building material manufacturers, (2) the underlying causes of the lack of competitiveness of local firms when compared to foreign companies, (3) the extent local firms received preferences in tendering for government contracts, and (4) and evidence of unfair competition or discrimination, if any, against local firms in government funded construction.

⁵ BTC Construction Industry Study ("Study"), pg. 17.

2 ***APPROACH AND METHODOLOGY:***

- 2.1 To address the terms of reference, BTC devised a structured questionnaire designed to solicit information as to how the industry had developed over the period 1988 to 1992. The questionnaire objectively sought data regarding turnovers and staffing levels, and subjectively sought views about the current state of the industry and future prospects. The survey was developed in consultation with BOCCIM to cover a sample size which was representative and practical within the strict time schedule of the study.
- 2.2 The original sample set was based on contacts with 144 companies and government departments and agencies with 95 responses being received. The selection of companies was based on BTC's database which was compiled from Central Statistics Office information. This was further supplemented in consultation with BOCCIM and the Botswana Development Corporation. The sample set from which the selection was made was based on companies involved only in the building sector. This comprised 66 companies in manufacturing, 101 in contracting, and 32 in wholesaling and retailing.
- 2.3 The final survey yielded a total of 81 responses in the four broad categories of contractors, professionals, manufacturers and wholesalers/retailers. The study's findings were based on this representative sample and augmented by interviews with government officials and independent research and analysis.

3 MAJOR FINDINGS

3.1 In October 1992 the BTC submitted a 130 page study supported by 13 annexes of approximately another 100 pages. To the extent possible, the study applied the same approach to each sector of the industry independently and then collated those results collectively. The result was a study which gave specific details on the construction industry in general and particular information on the four broad sub-sectors of contractors, manufacturers, wholesalers and retailers and professionals. Because each sub-sector has different interests and characterizations, the findings in each category reflected those differences.

3.2 With respect to the four key issues the study addressed, the major findings were the following:

3.2.1 Extent of Excess Capacity:

Based on a consideration of installed capacity of local manufacturers, Botswana could be self-sufficient with regard to face-bricks, cement bricks, paint, timber trusses, and window and door frames. Existing capacity is underutilised mainly due to imports from South Africa.⁶

There is more than a 50% overcapacity in the cement brick industry based on the formal sector production.⁷

Future growth possibilities exist in the roof cladding sector as there is undercapacity in both concrete roof tiles and galvanised roof sheeting.⁸

⁶ Study, pg 2.

⁷ Study, pg 2.

⁸ Study, pg 2.

3.2.2 Competitiveness of Industry:

The local building industry manufacturing sector is generally uncompetitive compared to the equivalent sector in South Africa. The prime reasons for this being the economies of scale which the South African companies enjoy.⁹

The creation of economies of scale through revised Government purchasing policy and export incentives, coupled with the appropriate choice of technologies based on readily available raw materials can play a significant role in developing and sustaining an industrial sector in Botswana.¹⁰

3.2.3 Implementation of Local Preference Scheme ("LPS"):

It appears that while the Government through Central Tender Board does try to ensure that local preference is applied, this works only where there is a direct purchasing agreement with Government. In the case of building contracts where the manufacturers rely on other clients for business, Local Preference Scheme has not been applied.¹¹

3.2.4 Contract Discrimination:

Far from discriminating against local products, Government does in fact specify local manufacturers of window and door frames in contracts. Similarly local sub-contractors are also specified for solar water heating systems. However no other local products are specified. This is despite the fact that local manufacturers/fabricators have the capacity to supply bricks (clay/masonry), trusses, glazing materials, paint, roof tiles and sheets. It appears that Government continues to specify foreign products even where local alternatives are available due to ignorance of what is available locally and perceived problems with quality and product range.¹²

⁹ Study, pg 2.

¹⁰ Study, pg 2.

¹¹ Study, pg 2.

¹² Study, pp 2.

Among the parastatals, the Botswana Housing Corporation ("BHC") also specifies locally produced frames and solar water heating systems. In addition, locally manufactured sanitaryware is also specified. BHC is currently actively looking at ways of extending the local content in its contracts and this is likely to have an impact in 1993.¹³

The survey confirmed that a large number of professionals did not actively source, select or give preference to local manufacturers and building materials due to quality and product range issues.¹⁴

¹³ Study, pg 2.

¹⁴ Study, pg 2.

4 **OTHER FINDINGS AND CONCLUSIONS**

4.1 Construction Industry Overview:

The Construction Industry in Botswana is approximately five percent the size of its South African counterpart. It services an extremely small domestic market, has virtually no export capacity and relies largely on imported raw materials for production.¹⁵ Given the economies of scale, the Botswana construction industry is generally uncompetitive compared to the equivalent sector in South Africa. Nonetheless, over the past decade, the construction industry has been a major contributor to the growth of Botswana's Gross Domestic Product providing approximately 20 percent per annum to the economy. With respect to real growth rates in constant 1991-1992 prices – excluding mining – the construction industry's contribution to GDP over the period 1980 to 1997 is as follows:

PERIOD	GDP ANNUAL % GROWTH	CONSTR. SECTOR ANNUAL % GROWTH	CONSTR. SECTOR % OF GDP ¹⁶
80-85	5.1	15.3	15.4
85-88	18.7	20.9	21.6
89-91	11.8	12.4	25.2
92-97	6.6	-7.7	6.9

The industry has also been critical in the area of job creation. Within the private sector, over the period 1981 - 1991, the construction industry has been the second largest formal employer both in raw numbers and percentage distribution with the percentage of employment being fairly consistent at approximately 12.7 percent. However, during the peak period of September 1990 to March 1991, more than 15 percent of Botswana's total private sector and parastatal workforce (i.e. 33,800 of a total of 225,000) was employed by the construction industry.

While no official figures are available on the level of retrenchments in the industry as a whole, the representative survey revealed that for 1992 contractors and manufacturers have had the largest number and percentage of retrenchments with

¹⁵ South Africa by far is the principal source of finished products, raw materials, equipment and information and technology.

¹⁶ Study, Table 8.6, pg 125.

contractors laying off 1,787 employees or 27.9 percent of their workforce while manufacturers have reduced their staff by 620 people or 18.7 percent.

4.1.1 Construction Sector Activity:

In Botswana, the largest client for the construction industry are government and the various parastatal agencies. Together they account for more than 87 percent of Botswana's on-going construction work.¹⁷ Consequently, more than any other single factor, government -- its policies, programs, regulations and initiatives -- has inordinate influence over the shape, direction and ultimate fate of Botswana's construction industry. Indeed, however prudent, government's decision not to embark on any major construction projects during the early stages of NDP6¹⁸ artificially stunted the growth of the industry during that time-frame and resulted in a shortage of firms able to meet the backlog of construction demand when government spending increased and the Accelerated Land Servicing Programme ("ALSP") was introduced.¹⁹

With respect to construction activity for 1992, as of late July, early August, survey submissions of architects, engineers and contractors, indicated that 700 million pula worth of work in the building sector was in the design stage. Assuming 15 percent of this work materialised, then the volume of work for 1992 was approximately 100 million pula.²⁰ Approximately 570 million pula of building contracts were postponed, 80 percent of which were attributed to the BHC controversy. Moreover, approximately 140 million pula of BHC contracts scheduled for 1992 were cancelled. The curtailment of contract work initiated by the breakdown in procurement policies and procedures at BHC created nearly a 190 million pula decline in expected GDP for 1992.²¹

¹⁷ Study, pg 70.

¹⁸ National Development Plan Six (4/85 - 3/91).

¹⁹ Following the introduction of the ALSP, a total of 200 million pula was spent on civil works between January 1989 and March 1991. Much of the work was undertaken by major resident and foreign civil engineering firms. Study, pg 100.

²⁰ Study, pg 101.

²¹ Based on these findings, it is estimated that at least 300 million pula worth of BHC contracts which should have been undertaken in 1992 have not materialised, resulting in a temporary downturn of a recessionary magnitude. Study, pgs 101 and 116.

Based on NDP7 projections, it is estimated that almost 3500 million pula (at current prices) worth of projects will be undertaken in building construction work between 1993 and 1997. An additional 1700 million pula civil and infrastructure work is also scheduled.²²

4.2 Foreign Competition:

The sharp increase in construction activity due to the introduction of the Accelerated Land Servicing Programme and the need to overcome the backlog of earlier years resulted in spiralling prices in 1989 and 1990 as the local construction sector was not geared up to cope with the demand of work.²³

Too few firms pursuing too many tenders resulted in skyrocketing contract prices which spurred government to open the construction sector to foreign companies primarily from South Africa and China as a means of increasing price competitiveness. The policy worked only too well. The arrival of foreign contractors in early 1990 and in particular the Chinese, together with the subsequent involvement of South African contractors in major contracts reduced tender prices by 30 percent during 1991-1992. By late 1991 and early 1992 foreign contractors had become the dominant force in the Botswana construction market. One of the principal reasons this occurred was that the government's deliberate decision to increase foreign competition in the sector coincided with a deep recession in South Africa which was already forcing South African contractors and manufacturers to aggressively seek new markets in Botswana and elsewhere.²⁴ Consequently, in 1992, foreign firms were carrying out nearly 60 percent of Botswana's construction contracts that were valued at 10 million pula or greater.²⁵ While government seemingly solved the problem of price competitiveness, it inadvertently created other problems by undermining its fledgling construction industry and exacerbating the country's growing unemployment difficulties. Thus the current downturn in Botswana's construction industry is attributable to two interrelated government decisions:

- ▶ the backlog of construction demand following the vigorous growth of the industry during the period;

²² Study, pg 102.

²³ Study, pg 100.

²⁴ Study, pg 100.

²⁵ Study, pg 101.

- ▶ the exposure of the local construction industry to foreign competition.

An additional policy of government also negatively affected the local construction industry and that was the decision to award extremely large contracts. Approximately 47 percent of all contracts (active, design and postponed) are of a value greater than 30 million pula and 82 percent are of a value greater than 10 million pula.²⁶ The value of active contracts above 10 million pula in 1992 is estimated to be 560 million pula of which almost 56.6 percent is being undertaken by foreign based companies.²⁷ The size of contracts awarded in the industry preclude the majority of local contractors the opportunity to work in the sector. Indeed, based on Central Tender Board classifications, most local contractors do not qualify to undertake work over 4 million pula.²⁸ While this pertains to the mostly smaller companies, with a few significant exceptions the majority of local contractors of any size are unable to take on contracts greater than 10 million pula.²⁹ Consequently, local contractors are only able to tender for 18 percent of all work currently ongoing and have had to rely on subcontractor work to survive in 1992.³⁰

Finally the lack of professional registration for contractors, architects and consulting engineers has fostered a situation which permits foreign contractors to enter the Botswana market without making the kind of investments in staff, training, housing and machinery that local contractors have made. Without the burden and additional overhead expense borne by local contractors, foreign competitors are better positioned to tender lower bids for Botswana's public and private contracts.

4.3 Building Materials and Components:

The BTC study assumed that if 15 percent of the work in the design or pre-implementation stage materialised in 1992, the volume of work for the year would have been 1000 million pula.³¹ Of that amount, between 450 million pula and 550 million pula would have gone to the building materials sector based on the assumption

²⁶ Study, pg 101.

²⁷ Study, pg 101.

²⁸ Study, pg 80.

²⁹ Study, pg 101.

³⁰ Study, pg 101.

³¹ See footnote 15 and accompanying text.

that between 45 percent and 55 percent of contract value goes toward the purchase of building materials and components.³² Of this amount, it is estimated that between 272 million pula and 334 million pula was spent in 1992 on importing building materials and components, most of which came from South Africa.³³ Were Botswana to have fully utilised local industry to provide such materials and components, the country could have saved between 109 and 135 million pula of that amount.³⁴

Based on estimates of installed local capacity, Botswana's construction manufacturing sector could be self-sufficient in supply of face bricks, cement bricks, paint, timber trusses, and window and door frames.³⁵ Notable exceptions to self sufficiency exist in supply of ceramic tiles and cement.

That the market for construction materials in Botswana is not functioning efficiently is clearly evidenced by a number of examples highlighted in the BTC study. For instance, annual market size for claybricks in Botswana is estimated at 26 million units valued at over 16 million pula. As of August 1992, Botswana was importing 95 percent of its claybricks³⁶ while the country's largest clay brick factory was working at 50 percent of its 24 million brick capacity. As a consequence, the company was able to sell only a third (4 million bricks) of its actual output leading to stockpiles in excess of 3 million bricks.³⁷ Similarly, the annual market for masonry bricks and blocks in Botswana is estimated at 63 million units valued at 16 million pula. BTC estimates overcapacity in this sector at 50 percent with the largest local manufacturer currently operates at 15 percent of capacity. Annual market size of the concrete roof tile industry is estimated at 10.8 million units. While local concrete tile producers have a capacity to produce up to 7.2 million tiles per year, local sales in this sector are 2.8 million tiles. The value of the annual market for galvanised roofsheets is

³² Study, pg 102.

³³ Study, pg 80.

³⁴ Study, Tables 7.21(a) and 7.21(b) pgs 104, 105.

³⁵ Study, pg 79.

³⁶ Study, Annex 7.4.

³⁷ The explanation for the apparent discrepancy between what was sold (approximately 4 million bricks) and what was stockpiled (only 3 million instead of 8 million) is that in the latter part of 1992 the company shut down operations and sold off much of the existing stockpile rather than to continue production.

estimated at between 38 million pula and 46 million pula. BTC estimates that local manufacturers are operating at approximately 10 percent of capacity.

The inescapable conclusion that must be drawn from these examples is that despite available capacity, local manufacturers of building supplies and materials are failing in their efforts to capture and retain market share against imported products. BTC's analysis of responses to its survey questions by the users of building and construction materials in Botswana indicated a clear preference for imported products. The most important reasons cited for preference of imported over local manufactured products were: price, reliability of supply, product quality and product range.³⁸

Although numerous allegations have been made about dumping by South African firms, the BTC study was unable to provide conclusive evidence of such unfair practices. However, circumstantial evidence suggests that due to the recession in South Africa, there is an over capacity in all sectors of their building industry. As a result, South African firms are willing to sell at cost to move stock whenever possible. This has impacted in a negative way in Botswana as the local manufacturing capacity with their higher operating costs are unable to compete with South Africa's cost recovery prices.

4.4 Government Assistance Programmes:

Essentially there are two programmes that government offers which provide assistance to the construction industry, and they are the Local Preference Scheme and the Financial Assistance Programme ("FAP"). Neither programme has been a substantial factor in expanding the market for indigenous firms in the construction industry. Since 1988, 60 companies have been awarded Local Preference Scheme certificates of which only 11 are directly connected with the building industry.³⁹ Of the 11 companies, 10 have LPS certificates which are currently active.⁴⁰ In the case of building contracts where the manufacturers rely on other clients for business, local preference scheme has not been applied.

Although the perception is that government has been unwilling to specify local products, the fact of the matter is that with respect to window and door frames government does specify local manufacturers. Similarly local sub-contractors are also specified for solar water heating systems. However, no other local products are

³⁸ Study, pg 81.

³⁹ Study, pg 64.

⁴⁰ Study, pg 64.

specified. In other areas government continues to specify foreign products even where local alternatives are available.⁴¹

While the Foreign Assistance Policy is more likely to provide greater employment opportunities than existing unregulated economic factors, its comparably small size in relation to the industry and its needs makes FAP a less potent tool for development of the construction industry. Nearly a fourth of the BTC survey respondents emphasized the need for greater monitoring of FAP to ensure that government's interests are protected. Other respondents felt that the program needed to be modified to benefit only citizen owned companies. Finally, the study notes that there seems to be limited strategic thinking behind the disbursement of FAP funds.

4.5 Impact on GDP:

Based on the study and its underlying survey, three basic assumptions can be made about Botswana's construction sector for 1992:

- ▶ an estimated decline in gross output of over 300 million pula will result from contract postponements and cancellations by BHC;⁴²
- ▶ approximately 521 million pula will have been spent on foreign sourced materials and supplies by contractors doing work in Botswana;⁴³ and
- ▶ foreign contractors in Botswana will have captured approximately 410 million pula of the total amount of contract work done by contractors for the year.⁴⁴

⁴¹ Study, pg 80.

⁴² The direct impact of this loss is estimated to cause a decline between 66 and P151 million pula in the projected level of 1992 GDP. A further decline in GDP of 66 million million through the operation of the indirect process of the expenditure multiplier effect will occur. In the workings of this multiplier effect, the ultimate expected outcome is the total effect on GDP of a projected 186 million pula decline in total expenditures. Study, pg 118.

⁴³ In the National Income Accounts, imports expenditures are subtracted from total expenditures for purposes of estimating Gross Domestic Product. Therefore, a expenditure level of 521 million pula, viewed as import expenditures, translates into a direct loss of potential GDP, estimated to be between 143 and 204 million pula. Adding to this amount the indirect multiplier effect, provides a projected loss to potential GDP of P268. Study, pg 118.

⁴⁴ If this amount is reclassified as an imported item, then a direct projected loss of potential GDP is estimated to be between 120 million pula and 177 million pula. The total effect on GDP, in terms of potential level, is projected to be approximately 226 million pula. Study,

According to BTC, the direct and indirect aggregate effects of these three factors on Botswana's economy results in an estimated "Total Unrealised GDP" which includes:

- ▶ an estimated loss of between 651 and 708 million pula of potential GDP,⁴⁵ and
- ▶ the potential loss of between 12,369 and 13,452 of local employment. Nearly half of this loss would be borne by the construction sector.⁴⁶

The Study's estimation of potential GDP is based on the total sourcing of all materials and supplies locally and the undertaking of all construction contracts by local firms. The difference between the Study's estimate of potential GDP and that of the Ministry of Finance and Development Planning's MEMBOT projected GDP is described as a "GDP GAP."⁴⁷ Obviously, both the sourcing of construction sector materials and supplies as well as the market share of foreign based firms will never be reduced to zero, but the GDP GAP represents this hypothetical condition. The more Botswana moves towards localizing its construction industry, the greater the reduction in GAP will be. While GAP can never be completely closed it does serve as a point of reference or target for policy planning purposes. In that regard it is worth noting that the GDP GAP of NDP7 is estimated to be 494 million pula in 1992 and projected to reach 629 million pula by 1997.⁴⁸

pg 118.

⁴⁵ Study, pg 118.

⁴⁶ Study, pg 118.

⁴⁷ MEMBOT is the Macro-Economic Model of Botswana which was developed in the 1970s and is presently managed within the Macro Unit of the Ministry of Finance and Development Planning. The National Development Plan's economic projections on the current and future status of Botswana's economy are derived for the most part from MEMBOT. Study, pg 126.

⁴⁸ Study, Table 8.10, pg 130.

5 RECOMMENDATIONS

- 5.1 As mentioned at the beginning of this report, BOCCIM seeks to (1) encourage policies which will address the immediate short term needs of the construction industry and (2) create a foundation for a viable and sustainable local construction industry which will be a source of employment and profitability.
- 5.2 One of the more significant findings of the BTC study is the overwhelming presence and vital role of government in shaping and directing the fortunes of Botswana's construction industry. Accounting for more than 87 percent of all on-going construction activity, government and its parastatals are the largest single purchaser of construction goods and services. Government is therefore uniquely placed to utilise its enormous purchasing power to positively influence the growth of a vibrant, indigenous construction industry. It is therefore critical that government appreciate its responsibility in this regard and undertake measures designed to strengthen and foster such development. In that regard, the following recommendations are made:
- 5.2.1 In a preliminary draft of its study, BTC suggested that government develop a National Policy on Botswana Business Utilisation under which all government ministries, agencies, parastatals and local governing bodies proactively target procurement opportunities in favour of the Botswana business community. This suggestion deserves serious consideration.
- 5.2.2 In implementing such a policy it is necessary that a comprehensive review of public policy towards land acquisition and the rules, regulations and procedures governing the construction industry be undertaken so that a coordinated government procurement process be established that explicitly addresses the vital issue of private sector development within the context of national planning.
- 5.2.3 As a major component in such a policy BTC proposed a Botswana Procurement Policy Strategy, as an implicit business development program aimed at improving local based firms quality and management standards. The net effect of such an effort should be strong, locally based firms able to compete on a regional basis.
- 5.2.4 Two additional proposals merit consideration;
- ▶ The establishment of a bureau of standards, and

- ▶ The enforcement and equal application of laws and regulations governing the construction industry.

Currently the contents and quality of building materials is largely unregulated. A bureau of standards is necessary to monitor and ensure industry-wide conformity and to establish a basis for objective appraisal of both local and foreign products used in public and private sector construction.

To overcome the problem of "Briefcase Businessmen" and "fly-by night" companies who operate without holding the necessary licenses, government needs to clearly enunciate and enforce its policies pertaining to the construction industry. Such an approach would ensure that foreign competition comply with licensing requirements and conform to local labour laws and regulations.

5.2.5 Further recommendations were proposed by BOCCIM in its Special Study which was presented to the Ministry of Finance and Development Planning in July of 1992. Among the most important of those recommendations were the following:

1. Establish a government sponsored "assistance" or "set-aside" programme;
2. Enforce a "visible" Local Preference Scheme or Assistance Policy;
3. Allow concurrent utilization of the Financial Assistance Programme and the Local Preference Scheme;
4. Complement the current contractual "inflation clause" with a "deflation clause";
5. Allow direct contractor/supplier payment by the client;
6. Establish an administrative Central purchasing scheme for construction materials and supplies.

5.2.5.1 Set Aside Programme

Given the enormous purchasing power of government, a major opportunity exists to utilise government spending to finance private sector growth. BOCCIM recommends that a minimum percentage of all government and parastatal construction expenditure should be "set aside" and used to develop and stabilise local industry. Architects, consultants and contractors should be made to comply with such a program. At present, there is no regulation to ensure that at least a minimum amount of government construction spending is reserved for local content. BOCCIM strongly recommends that local products should be specified in all contracts.

On the basis of work prepared by BTC,⁴⁹ a 25 percent set-aside program based upon the 1992 projected figure of 1000 million pula for the construction industry would have:

- A. A direct effect of 452 million pula increase in locally based enterprises gross production levels;
- B. An increase in potential GDP of 199 million pula;
- C. A resultant employment effect of between 1000 and 1200 new jobs overall and between 222 and 264 new construction sector jobs for citizen employment.

According to BTC, if a 30 percent set-aside program were initiated based on the 1992 figure the impact would be the following:

- A. A direct effect of 638 million pula increase in locally based enterprises gross production levels;
- B. An increase in potential GDP of 238 million pula;
- C. A resultant employment effect of between 1699 and 1810 new jobs overall and between 252 and 272 new construction sector jobs for citizen employment.

If a formal set-aside program cannot be established, then the alternative which BOCCIM recommends is that large contracts be broken into more modest units and reserved for smaller companies. The Central Tender Board has in the past split contracts to increase the number of local contractors who are eligible for work. This policy needs to be extended and strengthened. The Botswana Government's policy of investing in large scale projects has precluded even the largest local contractors from bidding on prime contracts while at the same time providing little or no sub-contracting opportunities for local businesses.

5.2.5.2 Local Preference Scheme

Introduced in 1978 and modified a decade later, the Local Preference Scheme ("LPS") administered by the Ministry of Commerce is designed to direct a substantial share of government purchases toward local manufacturers. The

⁴⁹ Preliminary Draft, pg 71.

scheme accords a 40 percent advantage based on local value added to registered resident manufacturers over foreign competition. It is agreed by both government and the construction industry that the scheme is not as widely applied as it should be. Part of the difficulty may well be that when manufacturers bid and supply through main contractors they are not eligible to utilise their local preference scheme percentage, putting them at a disadvantage when bidding against a "cost recovery" competing quotation.

While the construction industry has not benefitted from the Local Preference Scheme, measures which might be taken to strengthen the programme include examining the tendering procedures more closely and defining the scheme more clearly to ensure that Government, Parastatals and councils adhere to its provisions. Moreover, the scheme should be extended to cover contractors, professionals, wholesalers/retailers, complimentary and downstream manufacturers. Whether this suggestion is accepted or not, greater monitoring of the programme is essential.

Finally, with respect to sub-contractors, which is the position of the vast majority of Botswana's contractors, government should consider a mechanism that would permit direct payment to the sub-contractor once it has been demonstrated that such supplies or services have been delivered or rendered to the main contractor or the government entity or parastatal. Moreover, sub-contracting to smaller, local firms should be made a condition of awarding contracts to (larger) expatriate firms.

5.2.5.3 Financial Assistance Programme

While there is general consensus that the Financial Assistance Programme ("FAP") has been a major inducement to the development of the construction industry, BOCCIM takes the position that the policy should be revisited and consolidated as the present package is not suitable for local industry when compared to other countries. To strengthen the policy, BOCCIM recommends that sales tax subsidy for machinery and raw materials should be included as well as a subsidy for factory costs to ensure price competitiveness against the South African industry. In addition, the policy should be extended over ten years to ensure setting-up of a profitable enterprise. In that regard, and where appropriate, recipients of FAP should be assured of a certain level of government contractual work. BOCCIM therefore recommends the concurrent utilisation of the Financial Assistance Programme and the Local Preference Scheme. Finally, there is a need to improve the procedures of obtaining FAP and its overall implementation through more regional offices and simplification of application forms.

5.2.5.4 Complementary "inflation-deflation" clauses:

Currently, and in normal circumstances, if a contractor can prove extraordinary "proven costs" escalation in the cost of construction such excesses can be claimed from the client. However, any savings similarly obtained by the contractor can be pocketed as excess profit rather than be used to offset true inflationary influences. To strike a balance and to ensure "best bid" prices on tendering documents BOCCIM recommends that the equation needs to be balanced to include both a "rise and fall" in prices clause.

5.2.5.5 Central Purchasing Scheme:

Both the BOCCIM Special Study and the BTC Study recommend an "administrative central purchasing scheme," or a "direct domestic basic building materials sourcing policy program". As BOCCIM noted earlier, to ensure that government, DHC and other parastatals are receiving the best "value for money" and to eliminate the common "post tender" price cutting negotiations, a scheme could be established which provides for supplying materials for all government and other parastatal construction. BTC elaborates by stressing that government can regulate building material quality and domestic sourcing of these products. It would also address the problem of market size which hampers meaningful business start-ups in Botswana. BOCCIM pointed out that by tendering for larger quantities over longer periods of time, by eliminating overheads associated with multiple tendering, and by effectively utilizing FAP and LPS, suppliers will be able to significantly lower unit costs of production, compete with South African firms, and provide the client with corresponding benefits. The BTC study notes that such a program would require a substantial startup cost, but has the potential of providing a sheltered environment for the development and foundation of a crucial industry as part of the total scheme for economic diversification. The ultimate output and employment effects, if such a program had existed for 1992 would have been a 119 million pula increase in potential GDP and an increase in over 700 new jobs overall.⁶⁰

- 5.2.6 Beyond the recommendations BOCCIM made in its Special Study, the BTC study suggested numerous other areas that government policy should address. Among these are:

⁶⁰ Preliminary Draft, pg 71.

5.2.6.1 Central Tender Board:

There is an urgent need to strengthen the Central Tender Board ("CTB") and the tendering procedures especially with respect to having the ability to successfully implement both the BOCCIM and BTC recommendations. The CTB has the authority to insist on local preference when reviewing tenders. In the case of the building industry this can be strengthened if nominated suppliers are specified in contracts. The precedent for this is already in place for window and door frames and solar water heating systems. The tendering process should assess the full impact of what each tender offer contributes, both as to the specific scope of work and the macro-economic implications. The multiplier effects of sourcing local against foreign products and services could far outweigh pula savings in the tender amount.

To allay concerns over the tendering process, BOCCIM recommends that a representative from the Department of Industrial Affairs in the Ministry of Commerce and Industry be involved with the assessment of tenders above certain amounts and certify the consideration of LPS certificates in awarding of tenders. Reasons for not awarding of local manufacturers in preference to imported items should be reported back.

Finally, a consequence of the contraction in the industry is that it is not unusual for more than 30 companies to bid per contract. This situation has extended in the last few months even to very small contracts. Moreover, it appears that large contractors, both local and foreign, are currently bidding on small and very small contracts in areas peripheral to their major contract interests. BOCCIM would recommend that there be strict adherence to bidding within contract classification and that as a general rule, large foreign concerns should not be allowed to tender on medium, small, or very small tenders. BOCCIM would also recommend that government review its lowest cost tender price policy and ascertain that decisions are made on the basis of Botswana's long-term economic interests and not solely on that of price.

5.2.6.2 Professional Registration:

In addition to the recommendation that a bureau of standards be established,⁵¹ there is an immediate need for the creation of an industry wide Code of Conduct and some form of professional registration to regulate the industry given that there are currently almost no restrictions on setting up a

⁵¹ See paragraph 5.2.4 above.

construction business in Botswana. With respect to the Code of Conduct, a joint industry - government task force should be formed to determine and draft the criteria for such a Code. Professional registration on the other hand would ensure a more equal playing field for all firms involved in the building sector. At the moment, the Chinese contractors are allowed to bring in foreign labour which constitutes an unfair advantage due to the poor productivity of local labour. In addition, locally based companies are involved in training as well as general staff development which are not always required of foreign firms. Foreign companies which have established themselves in Botswana for a period greater than five years and have invested in both capital and staff training should be given a favourable status as compared to new start up companies. This will encourage companies to take a long term view about setting up and investing in the economy. Moreover, a newly registered company should be scrutinised in greater detail. This should include determining whether or not local participation is legitimate and actually operates the company. Finally, there is a need to provide a contract registration service that facilitates easy access to information on tenders and contract start-ups.

6 CONCLUSIONS

- 6.1 The one inescapable conclusion which flows from this report is that government has failed to appreciate the broader implications of its purchasing power on specifically the construction industry and more generally the economy as a whole. With nearly 90 percent of the construction work in Botswana emanating from government or its parastatals, it is imperative that policy-makers focus on ways and means of channelling the country's construction expenditures into stimulating and strengthening the local construction industry. Over the past several years, government has been primarily concerned with the more narrow issue of reducing tender prices on public sector construction projects. As the BTC study points out, government has apparently not considered the rippling effect of its decision to purchase foreign building materials and components and to award the bulk of its contract work to non-local companies.
- 6.2 This study points out that for 1992 alone, the direct and indirect aggregate effect of government's policy has been an estimated loss to the economy of between 651 million and 708 million pula and the potential loss of between 12,369 and 13,452 jobs, nearly half of this in the construction sector.
- 6.3 The recommendations which are made in this report, if accepted by government, would substantially reverse the outflow of capital from the country and have a positive impact on strengthening Botswana's construction industry.
- 6.4 With the possible exception of the modification of the Financial Assistance Programme, ~~none~~ of the recommendations made herein are compatible with the rationale and thrust of NDP7. In many instances the recommendations are but modification of existing policy which could have an immediate and beneficial effect on the local construction industry. Other recommendations, namely the "set-aside" programme, the adoption of a national policy on Botswana Business Utilisation and the implementation of a national procurement policy, reflect notions that ideally should be an integral part of any long-term strategy on Botswana's economic future.
- 6.5 The realization that Botswana is virtually self-sufficient in a variety of building materials but government continues to specify foreign products is an issue that must be addressed. In addition, the fact that Botswana imports 100 percent of its concrete and ceramic tiles suggest that a profitable industry can be created in these two product lines. While the Botswana Development Corporation is looking into the possibility of a concrete factory, there are serious questions as to whether the project is the appropriate scale for the market.

- 6.6 Finally, despite the anticipated downturn in the market as a result of diminishing diamond sales, Botswana can alleviate some of its budgetary shortfalls by directing more of its construction expenditures to local contractors and manufacturers. The BTC study suggests that if this were done, the savings to the country would be substantial.

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