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MEDIA RELEASE

In terms of the provisions of the Bank of Namibia Act, 1997, the Bank of Namibia is required to finalise its Annual Report before the end of March of each year. The same Act requires the Bank to prepare the Bank's annual accounts certified by the auditors, a report of the Bank's operations and affairs during the year, and a report on the state of the economy. As customary, although not a statutory requirement, the Bank also includes a chapter dealing with banking supervision.

Accordingly, the Bank of Namibia has prepared its Annual Report for the year ended 31st December 2005. Part A of the Report, dealing with the state of the economy, covers monetary and financial developments, as well as economic activities on the real, fiscal and external sectors. This year's Annual Report theme chapter focuses on the viability of second tier banks[1] in Namibia.

Theme Chapter

The objective of the theme chapter is to assess whether or not second tier banks could be viable in Namibia. The approach was to consider the critical success factors which are necessary for the establishment of second tier banks (STBs) to succeed, such as macro-economic and political stability, population size and density, availability of investment opportunities, culture of entrepreneurship as well as infrastructure development.

The conclusion from the assessment was that STBs would not be a viable proposition warranting implementation in Namibia and were unlikely to be so in the near future without substantial state intervention and support. The study, however, recommended that since the existing banks have indicated their willingness to open more branches in rural areas and to provide more banking services to poor communities which lacked banking facilities, the Bank of Namibia and other relevant authorities should provide guidelines regarding the expected content and outcomes to be derived from the

[1] Second tier banks are defined as banks that are subjected to lower initial entry and supervisory requirements compared to first tier banks. These smaller banks traditionally cater for the financial needs of the SMEs and low income customers a niche market which is inadequately served by the first tier banks.

banking/financial charter which is being developed by the banking and financial sector. The banking/financial charter aims at developing mechanisms for the improvement of access to financial services and the empowerment of the formerly disadvantaged communities.

Global Economic Developments

Global output growth was expected to decline to 4.3 percent in 2005, from 5.1 percent during 2004. The effects of the increasing oil prices on the global economy were expected to be partly offset by the worldwide environment of relatively lower interest rates, therefore ensuring the positive growth.The US and China remained the main drivers of global economic growth. Despite the US deterioration of current account and fiscal deficits, the US Dollar had, contrary to expectations, been strengthening during 2005. This was due to China, which had been experiencing surplus savings and was channeling these excess funds to the US in a bid to keep interest rates low as well as benefiting from the good returns offered in the US. This situation, the global imbalance, was of great concern because it reflected substantial gaps in growth performance between the regions of the world and implied movements in capital that were not sustainable.

Sub Saharan Africa

During 2006, growth in Sub Saharan Africa was expected to accelerate and record the strongest growth of 5.9 percent, since the early 1970s. The overall growth was largely dependent on the specific development of countries which were more responsible for the improvement. In particular, the new oil production facilities in Angola and Mauritania were expected to boost growth in these countries substantially in 2006, while oil production was also expected to increase in Nigeria.

The Domestic Economy

Following the expected slowdown in the global economy during 2005, the Namibian economy grew also at a slower pace. The slow growth could mainly be explained by the decline in the value added of the primary industry, particularly due to the poor performance of the mining and fishing sectors, as well as a slight deceleration in the value added of the tertiary industries.

The sluggish performance of the mining activities in 2005 had been the result of the slowdown in the activities of diamond mining due to the non-operation of some mining vessels, as well as the scaling down from the high production base in 2004, which had been deliberately made to offset the effects of a strong domestic currency. The poor performance of the fishing sector in 2005 was attributed to several factors such as rising operation costs, the unfavourable market conditions and low fish landings for most of the major species.

The deceleration in the value added of the tertiary industries is primarily reflected in the slowdown of sectors such as transport and communication, financial intermediation and producers of Government Services. The transport and communication sector was curtailed by the high increases in fuel prices during 2005.

During the year 2005, Namibia experienced the lowest inflation since independence in 1990. An average of 2.3 percent was registered in 2005, much lower than the 4.2 percent recorded in the previous year. The low inflation was reflected in almost all the price indices of the major group items, with the major driving categories being alcoholic beverages and tobacco, and housing, water, electricity, gas and other fuels, whose inflation rates fell during the review period. Although, fuel prices increased substantially during the period under review, their impact on the overall inflation was moderated by the inflation of those other categories whose inflation fell.

The year 2005 saw an environment of lower interest rates. Commercial banks held the short-term nominal interest rates constant, in line with the Bank Rate which remained unchanged at 7.00 percent since April 2005. Then too, the cost of borrowing was held constant by the maintenance of the prime lending rate at the same level of 11.75 percent since the change in April 2005. This monetary policy stance resulted in an increase in the net domestic claims of the depository corporations during the year.

The budget of the Central Government for the 2004/05 financial year, realized a lower budget deficit relative to the year 2003/04. The deficit during 2004/05 was, however, higher than the figure estimated in the main budget. Despite the fact that Government spending had been contained during this period, the higher deficit was the result of a shortfall in the realized revenue during 2004/05, which was lower than the estimate. By end of December 2005, the Government's outstanding total debt had increased from the level reached in December 2004. Total loan guarantees for the Central Government, on the other hand, had contracted moderately during 2005, mainly due to the decreased stock of guarantees on domestic loans.

To improve investor confidence, the Government of Namibia invited FitchRatings to conduct an assessment of Namibia's credit rating. During 2005, FitchRatings assigned Namibia a favourable sovereign rating of BBB- on its long-term foreign currency. This followed the joint initiatives of the Ministry of Finance and the Bank of Namibia to obtain a credit rating for the country, which was important to determine the creditworthiness of the Government. The outcome for the rating augured well for the economy of the country, in terms of bond and equity market development and an increasing inflow from foreign direct investments.

On the front of the balance of payments (BoP), the current account surplus is estimated to have declined during 2005. The deficit in the merchandise trade narrowed while the net inflows from investment income, current transfers and services, declined. The deficit in the capital and financial account was, on the other hand, estimated to have improved during 2005. A significant decrease in the net outflow of other long-term investments was responsible for the narrowing deficit in this account.

It is worth to note that as communicated in the Bank's December 2005 Quarterly Bulletin, a survey on Asset Management Companies was conducted to obtain data on the Namibian pension, life insurance and unit trust funds. The actual data obtained through the conducted survey has necessitated the revision of the old published BoP estimates for the period 2000 to 2004 and the International Investment Position (IIP) for 2000 to 2003 as will be seen in both the Annual Report and Quarterly Bulletin. The affected items under those two statements (BoP and IIP) have been clearly indicated in the Revision Notices in both the reports.

Responding to the developments on the global front in 2005, the Namibia Dollar had experienced an appreciation, year-on-year, against the major currencies of the world, such as the British Pound, Euro, and the US dollar. The appreciation of the Namibia Dollar against the United States Dollar reflected the weakening of the US Dollar on international foreign exchange markets and the strong commodity prices and capital inflows to South Africa to which the Namibia Dollar is pegged.

Outlook for 2006

The year 2006 indicated good prospects for the Namibian economy, as the economy was projected to grow at a higher rate than in 2005. The growth in 2006 would be supported by the primary sector, mainly through an increased production in the mining sector. The secondary sector was also expected to contribute positively to the growth in 2006, especially with regard to activities such as the refining of zinc and copper.

Banking Supervision Issues

In line with its responsibility as the regulator and supervisor of banking institutions, the Bank, through the Banking Supervision Department, undertook a number of regulatory and supervisory activities during the year under review. The activities were aimed at providing the supervisory oversight on banking institutions in order to strengthen the stability and soundness of the banking system. The supervisory oversight strives to ensure that players in the Namibian banking system are employing internationally recognized best practices and are in compliance with the provisions of the Banking Institutions Act of 1998, (Act No. 2 of 1998) and the Bank of Namibia Act of 1997 (Act No. 15 of 1997).

The supervisory activities carried out during the year, were in the form of the normal on-site examinations and off-site surveillance of banking institutions. Through the examinations, the Bank was able to establish that the banking institutions had maintained adequate internal control systems, had complied with prudential standards and had adhered to internal policies and procedures. The analysis performed on the financial data for the period ended 31 December 2005 had revealed a healthy and sound banking sector.

Policy Focus and Operations

The mandate of the Bank of Namibia as prescribed by Section 3 of the Bank of Namibia Act and the economic conditions described in Part A of this Report has shaped the strategic focus and other activities of the Bank of Namibia during the year under review.

The Bank of Namibia has continued to participate in various forums and projects co-ordinated under the auspices of the Common Monetary Area (CMA). During the past year, the Bank of Namibia participated in various consultative meetings aimed at enhancing the co-ordination of monetary policy within the CMA, as provided for in the CMA bilateral and multilateral agreements. The exchange of economic information at these forums has assisted with the formulation of monetary policies in the respective four CMA countries. A key milestone of the forum of the CMA central bank Governors for this year was the finalization of a study on the desirability and feasibility of establishing a common central bank for the CMA. The study concluded that a common central bank was feasible in the CMA. The findings of this study were shared with the respective Ministers responsible for finance within the CMA.

The Bank of Namibia also participated actively in the activities and programmes of the Committee of Central Bank Governors in SADC (CCBG), a body which had been established in 1995 by the SADC Ministers for Finance, to spearhead the regional agenda of economic integration in the financial and monetary area in SADC. Good progress has been made with projects related to the harmonization and standardization of the processes and systems in the recent past. During the period under review, the activities of the CCBG were characterized by a deeper focus on the achievement of the basic building blocks for a regionally integrated SADC, while securing an alignment with the continental programmes for the establishment of a monetary union. Substantial progress was made in the compilation of the monetary and financial statistics database, the information bank on policies and structure of the SADC central banks and the payment, clearing and settlement systems. Progress made in the payment, clearing and settlement systems for the SADC countries included the implementation of a real-time gross settlement (RTGS) system for most of the SADC countries.

During the year under review, Namibia was elected to chair the CCBG subcommittee on exchange controls. The main purpose of the committee was to harmonise and co-ordinate the terms and conditions of exchange controls in the SADC region, with the purpose of gradually removing all the controls between member states.

March 2006 Quarterly Bulletin

As has become customary, the March 2006 Quarterly Bulletin is also released today. The Quarterly Bulletin contains the usual quarterly analysis of key economic developments.

Conclusion

From the above, it is clear that the key indicators in the economy signify a healthy state of the economy and the stability of the financial sector. This is also reflected in a favourable sovereign rating assigned to the country. The prospect of the economy is geared towards a higher growth in 2006 under the envisaged environment of stable exchange rate and low inflation.

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