

Economic Update

Namibia Foreign Exchange Reserves: Keeping an Eye on a Critical Rule of Thumb

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When it comes to maintaining the one-to-one peg with the South African Rand, the Bank of Namibia ("BoN") is guided by an important international rule of thumb which prescribes that Namibia maintains sufficient foreign exchange reserves to be able to finance at least three (3) months' worth of imports. With foreign exchange earnings from diamonds significantly reduced due to developments in the international diamond market, the question arises whether the redemption of the second US$750 million Eurobond at the end of October will put this rule of thumb under pressure.

After every Monetary Policy Committee ("MPC") meeting, an official statement is issued about the state of the country's foreign exchange reserves and whether their level is such that the exchange rate peg with the South African Rand can be maintained. For example, the last MPC statement in August 2025 stated the following:

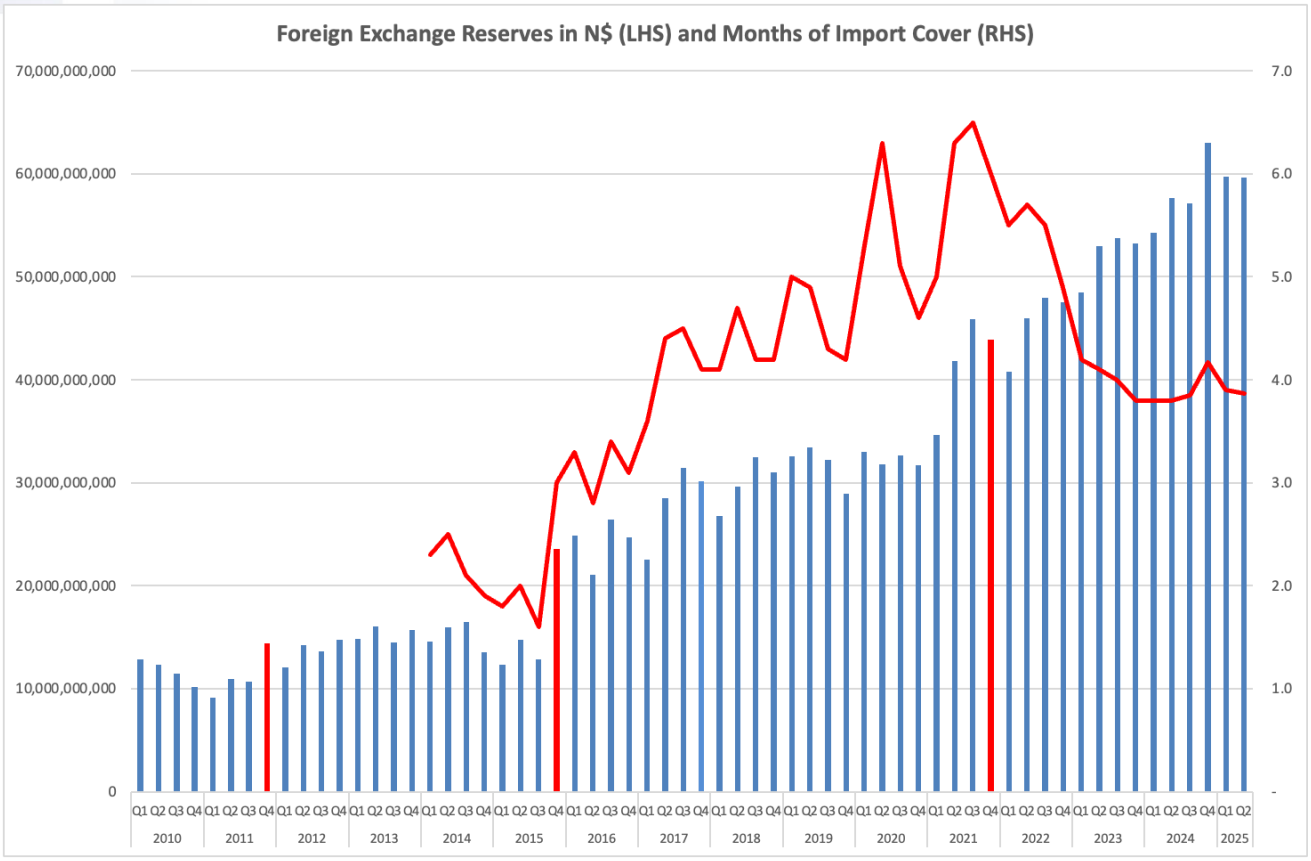
"Against this background, the MPC unanimously decided to maintain the Repo rate unchanged at 6.75 percent. Commercial banks are accordingly expected to keep their prime lending rates at 10.50 percent. This policy stance will continue to safeguard the one-to-one link between the Namibia Dollar and the South African Rand, while supporting domestic economic activity."

Namibia's monetary policy is determined primarily by the commitment to the peg to the Rand. The South African Reserve Bank ("SARB") sets its repo rate (essentially the rate at which it lends to the South African commercial banking sector) in a way that guides expectations of inflation in the wider economy. It will generally raise the repo rate when it sees inflationary pressures mount and reduce the repo rate when it sees inflationary pressures abate. The skill lies in changing the rate at the right time given the leads and lags that exist between interest rates and inflation and for this reason timely and accurate data is essential. The SARB's clear anti-inflationary mandate since the policy of targeting inflation was formally introduced in 2000 has led to lower inflation and lower interest rates in the two decades and a half since. In its own terms the policy has been a great success. The SARB has recently expressed its intention to move from an inflation target band of 3%-6% to a simple target of 3% following examples elsewhere in the world such as the inflation targets of the European Central Bank and the Bank of England, both of which have a target of 2%.

Namibia's main monetary policy objective involves ensuring the one-to-one peg with the Rand is maintained and opportunistic capital flows between the two countries minimised. If Namibia's repo rate is allowed to become significantly higher or lower than South Africa's, this will give rise to arbitrage opportunities given the relatively free flow of capital that is permitted between the two countries. However, Namibia is further constrained in what it can do by the Bilateral Monetary Agreement it has with South Africa based on the fact that the South African currency remains legal tender in Namibia. Under the agreement, Namibia is obliged to back all South African currency in circulation with an equal value of foreign exchange reserves. Over and above this formal agreement, Namibia abides by an internationally accepted rule of thumb to maintain over 3 months' worth of imports in foreign exchange reserves. This cushion means that unexpected outflows of foreign exchange reserves which may occur from time to time will not imperil the currency peg and will allow businesses and households in Namibia access to the foreign currency they require at the pegged exchange rate at any time. Such a cushion would not be as important if Namibia had its own floating exchange rate since the exchange rate would always move to balance supply and demand of foreign exchange.

The BoN expressed this approach in the following words in its Quarterly Bulletin of June 2024:

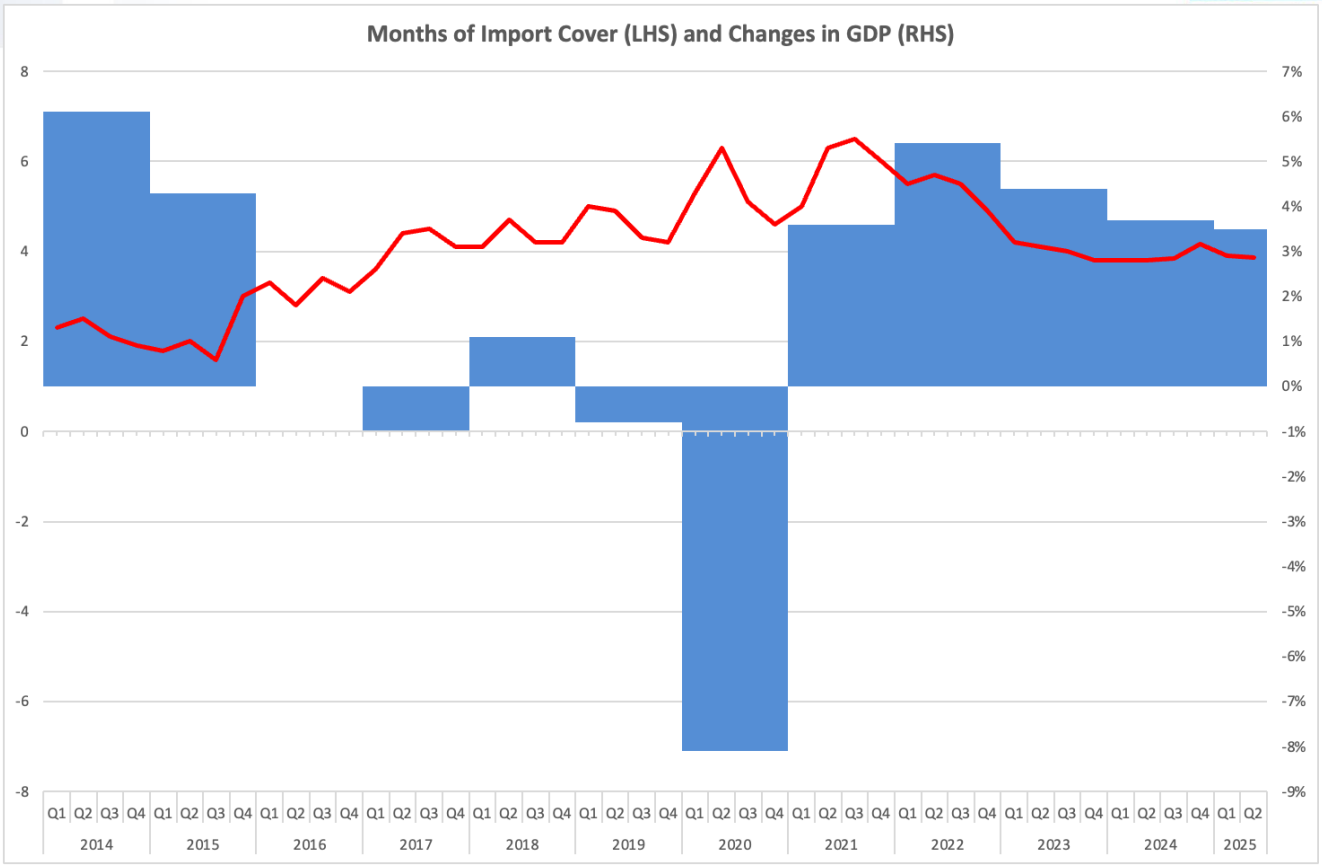
"Maintaining adequate foreign exchange reserves is central to monetary policy implementation in Namibia. According to the bilateral monetary agreement between Namibia and South Africa, Namibia's currency in circulation must be 100% backed by international reserves. However, this is an absolute minimum level and to be able to conduct its policies with confidence, the Bank of Namibia has consistently exceeded the minimum requirement, maintaining official reserve asset levels averaging 11 times the currency in circulation over the year to the end of May 2024 (Figure 1). The robust reserve buffer continues to serve Namibia well, facilitating the smooth conduct of international transactions even in the face of economic headwinds."



Source: BoN

An examination of Namibia's foreign exchange reserves since 2010 leads to a number of conclusions. Foreign exchange reserves have risen significantly in nominal terms from around N$10 billion in 2010 to around N$60 billion in 2025. However, over the same period the Namibia dollar has depreciated significantly against the US dollar which means more Namibia dollars are required to buy the same quantity of imports. At the beginning of 2010 the exchange rate was N$7.3397:1 US$ while at the end of Q2 2025 the exchange rate was N$17.2813:1 US$. At the same time the Namibian economy has also grown thus requiring higher absolute levels of import cover but not months of import cover.

Substantial inflows of foreign exchange were recorded in Q4 2011 and Q4 2015 when Namibia's two Eurobonds of US$500 million and US$750 million were issued on 27 October 2011 and 29 October 2015 respectively. These quarters are highlighted in red in the chart. Import cover was well below the 3-month rule of thumb until the second Eurobond was issued in Q4 2015 (29 October 2015). After that import cover climbed steadily to peak at 6.5 months in Q3 2021. Import cover fell in the quarters following the redemption of the first Eurobond in Q4 2021, which is also marked in red in the chart, and has settled at just under 4 months in the first two quarters of 2025. Since the second Eurobond was issued, foreign exchange reserves have always been maintained at or above the 3 months of import cover rule of thumb on a quarterly basis.



Source: BoN and NSA

A full explanation for the level of import cover would require sophisticated econometric analysis of the type employed in the research papers of the Bank of Namibia. One entitled "Foreign Exchange Reserves and Government Expenditure" employs such techniques to establish the link the between reserves and public spending. Intuitively, however, the main explanation for the level of reserves lies in GDP. Higher economic growth sucks in imports for consumption and investment alike and Namibia's marginal propensity to import is likely to be high although this requires further investigation. The chart above shows the level of reserves in months of import cover (on the left-hand scale) and annual percentage changes in GDP (on the right-hand scale). It can be seen that the level of reserves was low during the end of the six-year period of exceptional growth that followed the Global Financial Crisis in 2008 and 2009. As growth in the economy stalled from 2016, the level of reserves climbed to historically unprecedented levels peaking in 2021 as the impact of the Covid pandemic ebbed. As growth in the economy resumed, the level of reserves steadily declined to a stage where import cover is just under 4 months. It is possible that 3 months' worth of import cover is compatible with steady GDP growth of about 3% a year.

The question is whether this will continue to be the case over the coming months given two factors: a reduction in forex receipts from diamond exports and the redemption of the US$750 million Eurobond II on 29 October 2025.

Namibia's foreign exchange earnings come from three main sources: exports of goods and services, investment income from investments abroad, and the Southern African Customs Union (SACU). Over the coming quarter no major changes are expected in service exports, investment income and SACU receipts so attention focuses on goods exports.

The table shows that Namibia's merchandise exports have held up well over the past quarters even as the value of rough and cut and polished diamond exports has declined significantly. This is primarily down to the strong performance of uranium and gold exports. It appears that the downturn in diamond exports over successive quarters has been more than compensated for by uranium and gold exports whose prices have reached historically high levels in the past year. Namibia is fortunate to have enjoyed such a hedge.

Table 1: Namibia Merchandise Exports

Merchandise Exports (N$m)	2024				2025	
	Q1	Q2	Q3	Q4	Q1	Q2
Rough Diamonds	1,937	4,149	2,979	3,676	1,661	2,925
Uranium	3,224	1,773	6,006	3,495	4,346	7,904
Gold	3,419	3,168	3,758	4,259	4,452	5,071
Other Minerals	811	1,359	1,336	1,330	1,384	937
Food and Live Animals	994	882	926	1,834	662	527
Processed Fish	3,978	3,752	3,468	2,586	3,974	4,038
Polished Diamonds	1,076	1,521	1,262	1,502	1,099	624
Other Manufactured Products	1,037	1,450	1,565	1,857	1,543	1,646
Other Commodities	831	869	707	749	1,002	877
Re-Exports	1,438	1,483	1,592	1,321	1,516	1,117
Total	**18,745**	**20,406**	**23,599**	**22,609**	**21,639**	**25,666**

Source: BoN

All else being equal, a N$14 billion reduction in foreign exchange reserves implied by the repayment of the US$750 million at the current exchange rate would lead to a reduction of reserves to around N$45 billion or 3 months of import cover, exactly the level of the rule of thumb. Fortunately, the exchange rate has strengthened somewhat over the course of this year. Eurobond repayments are unhedged.

The BoN views the next quarter with equanimity stating the following in its latest Quarterly Bulletin from September 2025:

"Looking ahead, Namibia's inward portfolio investment liabilities are expected to decline significantly towards the end of 2025 due to the second Eurobond redemption in October. The repayment of the US$750 million Eurobond (approximately N$14 billion) will result in a substantial outflow of portfolio investment, leading to a marked reduction in foreign liabilities under the portfolio investment category in the financial account, as international investors holding the bond are repaid in full. This transaction will reduce the stock of portfolio investment liabilities in the International Investment Position (IIP), while also leading to a drawdown of foreign reserves. It will also contribute to a notable decline in foreign reserves. As a result, although the stock of both external assets (reserves) and liabilities (Eurobond) will decrease, the overall impact on the net financial account and the net IIP position is expected to be broadly neutral, since the fall in liabilities is matched by a corresponding reduction in assets. Importantly, the redemption will reduce Namibia's external debt, while also underscoring the need for prudent reserve management and effective refinancing strategies to maintain investor confidence and ensure continued access to international capital markets."

Conclusions

Given the relatively high level of import cover enjoyed by Namibia in Q3 2025 and the robust performance of export earnings despite the downturn in the value of diamond exports, rough calculations suggest import cover could be reduced to as low as 3 months by the end of Q4 2025. It can be expected that the redemption of the Eurobond II will not substantially weaken Namibia's ability to maintain the rule of thumb required to protect the peg to the Rand. It is not clear at this stage what Namibian policymakers response will be if reserves drop below 3 months' of import cover but one element of a response is likely to involve raising interest rates or at least leaving them higher for longer. Government has stated it does not intend to issue more Eurobonds. Whatever the case, more research is needed into Namibia's marginal propensity to import.



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