LESOTHO

Government of Lesotho

Industrialisation Master Plan

2007-2010

Ministry of Trade & Industry, Cooperatives and Marketing

Draft

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PREAMBLE

This paper outlines the Government of Lesotho (GoL) industrialisation strategy - the Lesotho Industrialisation Master Plan (IMP) for the period 2007-10. It is intended that the plan and the programme of activities it comprehends should be continuously reviewed throughout the 3-year period and renewed as appropriate at the end of the period by the machinery provided herein. The plan sets out development objectives and corresponding action plans.

It is worth noting that the GoL has always supported and continues to support industrial development. However, the programmes and interventions to this effect have been fragmented and have tended to be developed in response to immediate needs in an *ad hoc* manner. The GoL now intends to organise its interventions within a clearly articulated and coherent policy framework.

In order to ensure that the strategy presented is relevant and appropriate, it has been necessary to take a backward-looking perspective and evaluate the context from which the need for the IMP arises and within which its objectives are formulated and the activities to realise those objectives are implemented. The paper begins, therefore, with a brief review of the industrial sector in terms of its evolution to its current state as well as the perceived threats and opportunities that lie ahead, as a basis for the formulation of future strategy.

The second section of the IMP deals with industrial development policy objectives. This section spells out in general terms the parameters within which the industrialisation action plan is formulated and arises from the analysis of the sector undertaken in section 1. This both acknowledges and defines the role the GoL should play in developing the industrial sector and its relationship to other stakeholders in the industrialisation process.

Section 3 considers the measures that have been adopted by the Government to support and develop industrial activity. Each one of these activities is analyzed with respect to its impact on the industrial development policy objectives of section two. The fourth section is a forward-looking outline of additional activities required for the attainment of the industrial development policy objectives.

The IMP concludes with an implementation plan derived from the activities identified and organised according to defined priorities. This sets out the ministries or other agencies that will be primarily responsible for each intervention under the continuing direction of the coordinating body established for this purpose, the indicators of success and the assumptions made by the government both as to their importance relative to the achievement of plan objectives and the expectations as to the likelihood of its successful implementation.

EXECUTIVE SUMMARY

INDUSTRIALISATION MASTER PLAN AND ITS PURPOSE

The Industrialisation Master Plan (IMP) is a programme of government interventions over a three-year period, 2007-10, intended to ensure the Manufacturing Sub-Sector of the Lesotho economy (the Industrial Sector) continues to contribute to the realisation of the government's overall economic objectives as set out in its paper **Vision 2020**. In particular it is expected that the continued expansion of manufacturing activity will result in further employment creation and thus address directly the issue of national poverty. The economic analysis on which the plan is based shows how in recent years the Industrial Sector has become the major source of employment in the economy outside subsistence agriculture.

THE PRIVATE SECTOR AND THE GOVERNMENT IN THE INDUSTRIALISATION PROCESS

The IMP is based on the assumption that the industrialisation process will continue to be market-driven and that the Private Sector will be the main engine of growth. The role of the government will be to facilitate the process by creating an enabling environment which will sustain industrial activity and encourage further investment in industrial enterprises.

INFRASTRUCTURAL DEVELOPMENT – A TEMPORARY EXCEPTION TO THE PRINCIPLE OF MARKET-DRIVEN INDUSTRIAL DEVELOPMENT

The most significant departure from the principle of market-driven industrial activity will lie in the continuing need for government provision of an infrastructure of industrial locations fully serviced with electric power, water and liquid-waste disposal facilities and equipped with shell factory units for leasing to entrepreneurs. This is necessitated by the market imperfection arising from the present system of land-tenure enshrined in the Land Act which has the effect of strongly discouraging such infrastructural development by private capital.

However, the plan recognises that this effect of the Land Act is a grave weakness and that the difficulty experienced by the government in providing an adequate supply of locations is probably discouraging potential industrial investors from locating in Lesotho. To address the problem of infrastructural under-supply the plan envisages that ways will be explored of enabling private capital to participate in infrastructural projects in the context of the Land Act in its present form with a view to speeding up the development of existing sites to adequate standards, particularly that at Ha Tikoe on the eastern outskirts of Maseru.

However, in the longer term the government will seek changes in the Land Act which will allow private investors to acquire leasehold and freehold titles in land designated for industrial use. This will encourage private provision of industrial locations. It will also make possible the use of land holdings as collateral for business loans which is expected to go some way to addressing the problem of under-representation of Basotho enterprises in the industrialisation process which is in large measure a factor of their difficulty in raising credit from commercial banks.

The supply of power, water and waste services on a national basis will continue to be the responsibility of the state-owned Lesotho Electricity Corporation (LEC) and the Water and Sanitation Authority (WASA). The provision of these utilities will be expanded during the plan period by the Minimum Infrastructural Platform (MIP) programme which will also expand the telecommunications network and improve customs services at all main points of entry into the country.

INDUSTRY TO CONTINUE TO BE EXPORT-ORIENTED

It is envisaged that activity in the Industrial Sector will continue to demonstrate an overwhelming export-orientation. This is an inevitable consequence of two factors:

1. The small size of the domestic market which makes it impossible for it to support enterprises which enjoy economies of scale sufficient for them to be internationally competitive; and of

2. The impossibility of protecting domestic producers against international competition given the country's commitment to reciprocal free trade arrangements, which limit the government's ability to impose high tariffs or non-tariff barriers on imported goods.

The USA will continue to be the major overseas destination for Lesotho exports, in particular as an outlet for Lesotho garment suppliers. However, the government will seek to develop trade with EU markets. It will also make greater efforts to promote Lesotho as a manufacturing location for the supply of regional markets.

THE PATTERN OF SUB-SECTORAL DEVELOPMENT

The Industrial Sector is presently dominated by enterprises which concentrate on the production of garments for export to the USA intended mainly for the high-volume/low-value end of the market. Because of its importance as an employer of labour the government will continue to encourage this activity and defend the interests of those engaged in it to the best of its ability. However, it recognises that the US market for clothing is likely to become even more intensely competitive during the plan period while the value of the preferences which give Lesotho-based suppliers an advantage will decline. Therefore promoting the diversification of industrial activity will constitute an important element in the programme of interventions in the plan.

Lesotho's relative comparative advantages as a supplier of industrial products relate most importantly to the textile and garment sub-sectors and it is in these areas that diversification will chiefly be pursued. To this end the government will seek to revive exports to EU markets by using the on-going EU/SADC Economic Partnership Arrangement (EPA) negotiations to mitigate the effects of the Cotonou Convention Rules of Origin that destroyed Lesotho's once-significant trade with Europe in these products in the mid-1990s.

However, the government recognises that, even if it were to be successful in this endeavour, the market for bulk garment items in the EU is likely to become more difficult for the same reasons of increased competition and preference erosion as will apply in the case of the country's trade with the USA. Diversification will, therefore, be sought into the production of higher-value items, in particular knitwear, although it is recognised that here too the US and EU markets will become increasingly difficult to operate in during plan period.

To address this problem the government will seek to revive Lesotho as a significant supplier of regional markets, particularly in the Republic of South Africa (RSA). Here it will promote investment in the production of high-value clothing (both woven and knitwear) which is required in relatively low volumes with very short delivery periods thus making it difficult for it to be supplied by producers in East and South Asia. The possibility of producing the high-quality fabrics needed for the manufacture such items, possibly on the basis of imported grey cloth will also be considered.

In addition to the textile and garment sub-sectors the government will also promote investment in non-textile projects. Areas where Lesotho appears to have the greatest relative comparative advantage include operations requiring labour-intensive assembly of imported components, such as electronic and electrical goods for regional markets and the processing of local agricultural and mineral raw materials to add-value in-country prior to export. A number of such projects have been developed in recent years. Consideration will also be given to the development of import-substitution activities such as the provision of 'findings' (buttons, zips, garment components) for the textile and garment industries and the manufacture of generic medicines.

It is expected that the main outlets for non-textile exports will be found in regional markets in southern Africa.

As already intimated, the pattern of development within the Industrial Sector will be determined by private sector initiatives on the basis of market signals. The government will not participate in this process and it will certainly not take private equity holdings to encourage particular developments deemed to be in the National Interest which have not attracted private investment. However, as intimated above, this will not preclude the government from promoting particular sub-sectoral developments by supporting feasibility studies to determine the commercial viability of specific investment projects and by undertaking other promotional activities to this end.

MOST INVESTMENT TO COME FROM FOREIGN SOURCES

It is recognised that most investment in industrial activity will continue to come from external sources. This reflects both the shortage of domestic capital and the reluctance of Basotho to invest in industrial projects, a reluctance which reflects low levels of available technical and business expertise and the difficulty of potential local entrepreneurs in raising credit from commercial sources.

The government will not differentiate between local and international investors in the operation of its investment incentive regime except in the most clearly-defined circumstances. However, it does recognise that efficiency and equity both require greater participation by Basotho in the industrialisation process. It is also recognised that the SMME sector is important as a major generator of non-agricultural employment and has thus a major role to play in achieving the government's overall economic objectives.

The IMP will, therefore, continue to pursue policies designed to encourage investment in industrial projects by Lesotho nationals.

SCOPE OF INDUSTRIALISATION MASTER PLAN (IMP)

The IMP is a programme of activities intended to address obstacles to industrial development. It envisages that there will be 29 specific interventions over the plan period in the following main areas:

- The development of a centralised structure for formulating industrialisation policy and monitoring its implementation thus addressing the lack administrative coherence and failures in coordination which have reduced the effectiveness of government activity in this area ;
- Improvements in the investment incentive regime;
- The diversification of the present pattern of industrial activity;
- Securing access to export markets through improvements in trade negotiating capacity;
- Industrial infrastructure development;
- Improving the business environment – i.e. addressing bureaucratic obstacles to industrial development and inadequacies of business intelligence sources;
- Indigenous investors' access to credit from commercial banks;
- Low levels of labour productivity; and
- The development of the Micro, Medium and Small Enterprise (SMME) sector.

The various activities are prioritised on the basis of their perceived importance to the achievement of plan objectives and the expectation of a successful outcome within the plan period. Where activities are considered critical or highly important to the achievement of plan objectives, but for various reasons there is a low expectation of the immediate objectives of an intervention being achieved in the plan period consideration will be given to whether or not donor-funded technical assistance should be sought.

The timing of the various interventions will be determined primarily on the basis of the priority assessment discussed above. However, other factors will be taken into account to bring forward the initiation of activities if:

- They already on-going at the start of the plan period;
- If this is considered necessary to the achievement of plan objectives; and
- If this is considered necessary to enable the government or its agencies to respond adequately to external events over whose timing it has no control.

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1. ECONOMIC AND INDUSTRIAL CONTEXT

1.1. INTRODUCTION

The GoL is committed to the fight against poverty and has identified employment creation as a sustainable way of reducing poverty. The development of the Industrial Sector of the economy driven by Private Sector initiatives within an enabling environment created by government action offers the realistic potential of creating jobs in numbers that will make an impact alleviating poverty. The **Industrialisation Master Plan (IMP)** with which this paper is concerned is aimed at unlocking this potential by setting out in detail the measures by which the GoL will facilitate and encourage private sector growth.

The guidelines within which national short–term to medium–term development plans are formulated are provided in the Government of Lesotho (GoL) paper known as **Lesotho Vision 2020**. A principal objective of the Vision is that by the year 2020 Lesotho should have a stable and strong economy. The **Poverty Reduction Strategy (PRS)** together with the **Millennium Development Goals (MDGs)** are the operational tools formulated within the context of the Vision for realising this objective. The PRS outlines the national priorities and strategies to reduce poverty and promote equitable economic growth. The priorities have been identified as among others: employment creation; infrastructure development; promotion of good governance; and improving public service delivery.

1.2. THE ECONOMY

1.2.1. Overview

The Lesotho economy, during the period 1980/81–1986/87 grew at an average rate of 2.8 percent per annum. During the high-LHWP period, 1987/88–1996/97, the economy grew at an average growth rate of 6 percent per annum. However, towards the end of 1990s the growth rate fell to an average of about 3 percent annually. This was mainly due to a decline in capital expenditures associated with LHWP which had accounted for a significant part of domestic investment in the earlier years. Furthermore, the political instability that characterised 1998 caused the economy to register a negative growth rate of -4.6 percent in that year. However, it quickly recovered from this experience and in the three years to 2001 averaged the growth rate of 1.5 percent while in the subsequent four years to the end of 2005 it grew at an annual rate of 3.1 percent.

1.2.2. Sectoral analysis

The Lesotho economy is divided into to three major sectors – **Primary** (principally Agriculture and Mining and Quarrying), **Secondary** (Manufacturing – i.e. the area covered by IMP – Electricity and Water, and Building and Construction and **Tertiary** (Government and Services). Table 1 below shows the contribution of each sector to economic activity.

It can be observed that over the eight years to end of 2005 the tertiary sector was the leading contributor to Gross Domestic Product (GDP) with an average of 42 percent followed closely by the secondary sector with the average contribution of 40 percent. The primary sector was responsible for the remaining 18 percent.

Within the primary sector, the agricultural sub-sector was stable over time. However, the majority of the population are dependent on this sector, albeit at a subsistence level. It is reported that about 80 percent of the Lesotho population reside in the rural areas and of those 55 percent depend on subsistence farming for livelihoods. From a poverty reduction point of view, the agricultural sector merits attention.[1] The extractive sector made a negligible contribution until 2004 when it rose to a recognizable 2.3 percent before nearly doubling to 5.2 percent in 2005. The establishment of the Lets'eng Diamond Mine in 2004 was the main factor underlying this development.

Looking at the secondary sector, manufacturing and construction have been the major drivers. Five years prior to 1998 the average contribution of the construction sector to GDP was 19.1 percent. This was due to the LHWP as noted earlier. The apparent decline that is observed post-1998 is a result of the completion of the Phase 1 of the project. However, the mantle was then passed on to the manufacturing, with the garment and textile sub-sector playing a prominent role in the subsequent surge.

However, despite the relatively stable performance at a macroeconomic level, poverty remained very high in Lesotho. This was primarily due to the drastic cut-backs in remittances by migrant labourers which had been the principal main-stay of the economy in earlier years.

[1] Among the PRS priorities, food security is predicated on this sector. The Agricultural Development Policy addresses relevant strategies towards the attainment of food security.

Table 1: Structure of the Lesotho Economy

SECTOR	SUB-SECTOR	1998	1999	2000	2001	2002	2003	2004	2005
Primary	Agriculture	17	16.7	17.9	17	16.5	17.1	17.1	16.5
	Mining and quarrying	0.1	0.1	0.1	0.2	0.2	0.2	2.3	5.2
		17.1	**16.8**	**18**	**17.2**	**16.7**	**17.3**	**19.4**	**21.7**
Secondary	Manufacturing: of which	17.7	16.5	17	17.9	20.8	20.1	18.5	15.9
	• Food products and beverages	*7.4*	*6.8*	*6.6*	*6.2*	*6.7*	*5.9*	*5.6*	*5.1*
	• Textiles, clothing, footwear	*7.2*	*6.4*	*7*	*8.1*	*10.4*	*10.7*	*9.2*	*7.1*
	Construction	16.3	18.5	18.4	18	16.4	15.7	14.7	14.4
		39.1	**41.5**	**41.3**	**42.1**	**42.5**	**40.7**	**38.1**	**37.1**
Tertiary		**43.8**	**41.8**	**40.7**	**40.7**	**40.9**	**42**	**42.5**	**41.3**

Source: Bureau of Statistics

1.2.3. Retrenchment of RSA mining activity

Remittances by Basotho workers employed in mining in the Republic of South Africa (RSA) had formed an important part of household income and their decline as a result of retrenchment in mining activity in that country in turn suppressed domestic consumption in Lesotho. In the early 1980s remittances were estimated at around 90 percent of GDP, but by the beginning of the 1990s this proportion had fallen to less than 50 percent. By 2001 it had fallen still further to around 23 percent and it continues to fall.

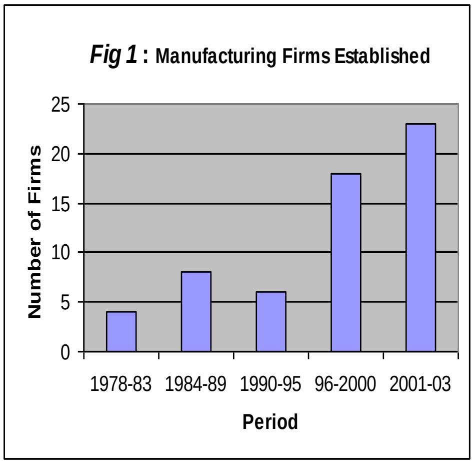
In terms of numbers of jobs, Basotho employment by the RSA mining industry fell from 127,000 in 1990 to 65,000 in 2000 and subsequently to fewer than 50,000 at present. This cut-back severely depressed the incomes of a large number of households, thereby removing resources for agriculture, including for purchase of inputs and implements. This external shock directly translated into a rising incidence of poverty, as a result of the inability of the domestic productive sector to absorb returning miners and compensate for attendant losses of income.

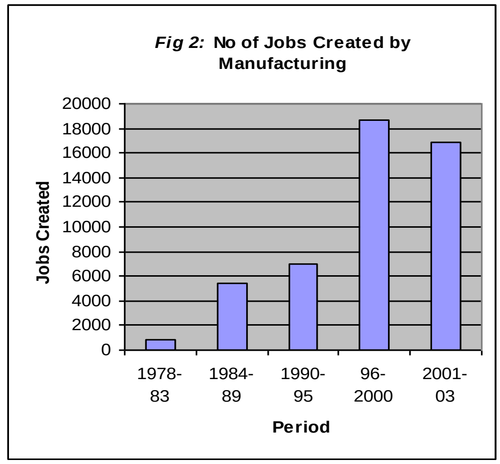
As noted above to deal with the current state of extreme poverty large numbers of alternative employment opportunities had to be created. The principal response to this charge was from the Private Sector which in 2000 for the first time surpassed the public service in terms of numbers employed. The manufacturing sub-sector was largely responsible for this development. The industrialisation, therefore, warrants specific attention within the overall PRS programme by its demonstrated potential for employment creation.

1.3. THE INDUSTRIAL SECTOR

1.3.1. Evolution

The Lesotho formal Industrial Sector emerged in the early 1980s when RSA-based clothing manufacturers took a decision to relocate to Lesotho in order to avoid the United States of America (USA) sanctions that were imposed on the Apartheid Regime. Statistics relating to Lesotho National Development Corporation (LNDC)-assisted firms show that in the period 1978-2003 59 manufacturing firms were established in Lesotho creating 48,707 jobs. Figures 1 and 2 below show breakdown of these numbers (firms and jobs) per blocks of five years. Figure 1 shows the evolution of the manufacturing sector in terms of the number of firms established within the period 1978-2003. Figure 2 shows the corresponding number of jobs created as a result of the establishments depicted in figure 1.





The five years to 1983 saw the establishment of four firms creating 814 jobs followed by the establishment of eight more employing 5,384 people in the next block of five years. The most notable development is that the three (as opposed to five) years spanning 2001 through 2003 saw the greatest number of firms established. During that time twenty-three (23) establishments employing 16,847 people opened for business. This was a direct result of Lesotho's qualification as a beneficiary under the Africa Growth Opportunity Act (AGOA) in April 2001.

AGOA is the US Government's non-reciprocal preferential trade arrangement which extended to Sub-Saharan Africa (SSA) suppliers duty-free/quota-free access to the US market under the US GSP regime for virtually all product-lines. This had a dramatic impact on the Lesotho manufacturing sector making it economic leader in terms of growth and employment creation.

However, the benign consequences of the AGOA in terms of industrial projects established were qualified by the fact that development was almost completely confined to the clothing sub-sector. This was only in part a result of AGOA qualifying textiles and garments for preferential access to the US market under the American GSP regime for the first time. More significantly, in the case of defined Less-Developed Beneficiaries in SSA such as Lesotho, AGOA granted preferential access for goods manufactured from fabrics sourced in Third Countries under the so-called Special Provision (SP). The AGOA SP was an act of US generosity to its SSA trading partners only previously paralleled by the EC decision to allow Lesotho and other ACP suppliers a derogation from its own highly restrictive Rule of origin under the Cotonou Agreement. This had also brought about a substantial upturn in shipments to EU markets, but the EC ended the concession in 1996 as a result of which Lesotho's garment shipments to EU markets fell to insignificant levels in a very short period.

AGOA caused an upsurge in investment in Lesotho by Asian manufacturers supplementing those who had migrated from the RSA in the 1980s. There is no doubt that the AGOA Special Provision was the main attraction for these new investors. However, the availability of incentives aimed at promoting FDI which had been put in place under the World Bank-sponsored Agro-Industrial Project (1991-96) was also an important factor in ensuring that Lesotho became a major SSA beneficiary of the AGOA.

1.3.2. Current State of the Industrial Sector

As of August 2006, again based on LNDC statistics, there were forty-four (44) manufacturers in Lesotho employing 47,466 people. Projections at the time were that the sector would have fifty-four (54) firms employing 54,347 people by January 2007, but this has yet to be verified. Table 2 below profiles the manufacturing sector by product line in broad terms with corresponding employment levels.

Table 2: Manufacturers by Products and Corresponding Employment, August 2006

Product	Number of Firms	%	Employment	%
Other Manufacturing *(electronics, auto parts, cartons, pharmaceuticals, etc)*	14	31.8	1027	2.2
Shoes	4	9.1	1090	2.3
Garments *(T-Shirts, Jeans, Childrenswear, etc)*	26	59.1	45,349	95.5
Total	**44**	**100**	**47,466**	**100**

Source: Derived from LNDC Manufacturing Portfolio

An assortment of product-lines is aggregated under ‘other manufacturing’ and a total of fourteen (14) firms were engaged under that head in August 2006 employing 1,027 people. This amounted to no more than 2.2 percent of the total employment in manufacturing sector as a whole at that time. Twenty-six (26) of the forty-four (44) firms were garment producers who employed 95.5 of the total manufacturing labour force. This clearly shows the significant role that the garment sub-sector producing largely for the US market has played in creating jobs in Lesotho.

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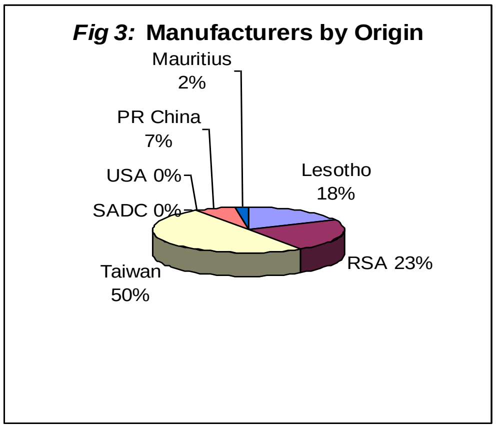
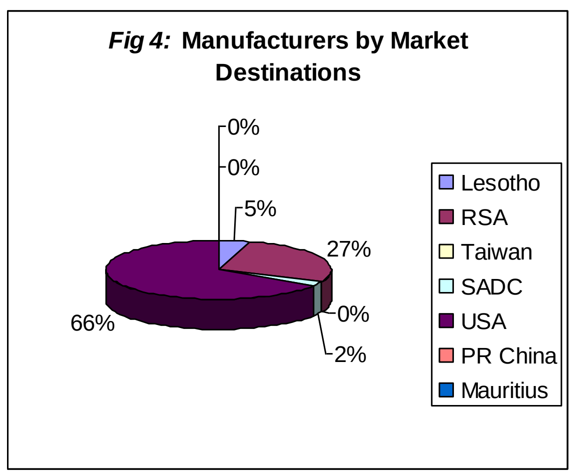


Most of the firms operating in Lesotho are of foreign origin. Figure 3 shows that only 18 percent of the manufacturers (8) were of **domestic** origin. Of the 44 firms in total, 22 (50 per cent) were from **Taiwan** and most of these were established post 2001. The **RSA** presence in Lesotho declined during the later 1990s, but in 2006 it still accounted for 23 percent of the total firms in the Industrial Sector. All of which underlines the fact that this sector is driven by the foreign direct investment (FDI).

The figure illustrates that the capacity of the domestic private sector terms of investing in large projects is limited. This clearly highlights the central and primary role of FDI in the development of the Industrial Sector and justifies the emphasis placed on this in Lesotho Industrial Policy. However, it also indicates the need to develop the domestic Private Sector (via facilitation and support through incentives). It has been and remains a primary goal of the GoL that this sector too should grow and contribute significantly to employment creation.

In terms of market destinations only five (5) percent of the total firms in the sector produce for the domestic market. The other ninety-five (95) firms service the export market. The USA is the market destination for most of the manufacturers (66%) followed by the RSA being serviced by 27 percent of the firms in the sector.

This reflects the reality of Lesotho's situation as a nation with a population of only about 2.2 million which cannot, therefore, provide a market for any significant part of what it produces. Export promotion is vital for Lesotho's industrialization strategy. Securing access to its overseas outlets has to be a prime object of government policy and the preparation of favourable positions for use in trade negotiations by taking full advantage of the benefits accruing to the country as an LDC is a matter of constant concern.



1.4. EXPORTS

1.4.1. Direction of Trade

Given that export-oriented FDI is an important element of Lesotho's industrialization process, export markets are also equally important. Manufacturing data (the limitations of which were noted at the outset) show only two major markets – the USA and the RSA. However the total exports data show that there are other markets besides these two. Notable other markets are the SACU (in which RSA is by far the most important outlet) and the European Union (EU). (In the 1980s and early 1990s SACU was the major outlet for Lesotho exports, but this declined after the end of the Apartheid era as firms which had come to Lesotho to escape the troubles in the RSA closed down or returned that country). Exports to the South African Development Community (SADC) countries and other parts of the world have been negligible in terms of the total exports. Table 3 shows exports to various parts of the world per blocks of five years to end of 2004 and the subsequent two years to 2006.

The last row of table 3 shows the relative importance of the North American and European markets combined. In the years 1990-94 around 50 percent of all exports were to these markets. In the following block of five years from 1995-99 only 37 percent of total exports went to these markets largely as a result of the decline in exports to EU destinations following the ending of the textile Rule of Origin derogation in 1996 noted above. During that period exports to North America increased while those to Europe fell sharply from over 18 percent to only 1.6 percent. The recovery that followed, firstly to 4 percent in 2000-04 and later to 15 in the last two yeas 2005-06, could as well be a result of the Everything-But-Arms agreement effected in 2001 that allowed duty-free access into the EU. However, the textile Rule of Origin regime continues to limit Lesotho's exports to EU markets. The AGOA is responsible for the surge in exports to North America with the USA being the primary destination. Over the years 2000-04 and 2005-06 the Lesotho exports to the North America and Europe were 75.7 percent and 76.8 percent of total exports respectively.

Table 3: Direction of Total Exports

	90-94		95-99		00-04		2005/06	
Total	***1598.85***	***100***	***3880.28***	***100***	***15724.75***	***100***	***8988.81***	***100***
Africa	**792.4**	**49.6**	**2441.63**	**62.9**	**3798.73**	**24.2**	**2057.40**	**22.9**
SACU	*780.64*	*48.8*	*2436.78*	*62.8*	*3754.3*	*23.9*	*1858.89*	*20.7*
SADC	*10.39*	*0.6*	*4.37*	*0.1*	*2.58*	*0.0*	*18.12*	*0.2*
Other	*1.37*	*0.2*	*0*	*0.0*	*41.57*	*0.3*	*180.40*	*2.0*
Europe	**294.89**	**18.5**	**61**	**1.6**	**629.39**	**4.0**	**1345.22**	**15.0**
EU	*282.55*	*17.7*	*60.29*	*1.6*	*626.05*	*4.0*	*1345.16*	*15.0*
Other	*12.34*	*0.8*	*0.71*	*0.0*	*3.34*	*0.0*	*0.06*	*0.0*
N. America	**503.63**	**31.5**	**1372.8**	**35.4**	**11273.02**	**71.7**	**5554.07**	**61.8**
Asia	**6.03**	**0.4**	**2.81**	**0.1**	**23.5**	**0.1**	**32.08**	**0.4**
Oceania	**1.9**	**0.1**	**1.34**	**0.0**	**0.1**	**0.0**	**0.03**	**0.0**
Non US & EU	*800.33*	*50.1*	*2445.78*	*63.0*	*3822.33*	*24.3*	*2089.52*	*23.2*

Source: Derived from Central Bank of Lesotho

1.4.2. The Domestic Private Sector

The domestic private sector is made up of formal and informal sectors. It is dominated by micro, small and medium enterprises (SMMEs).In the Lesotho context,[2]

- A micro-enterprise is defined as an organisation that employs fewer than 3 people;
- A small enterprise as one that employs 3 to 9 people; and
- A medium enterprise as one that employs 10 to 49 people

As of 2005, there were more than 100,000 SMMEs employing nearly 200,000 people having grown from 59,650 SMMEs that employed 82,567 people in 1990.[3] This sector is

[2] White Paper on the Development and Promotion of Small Business, 2002

[3] Lesotho Growth and Employment Options Study, 2005 and the Gemini Survey, 1990.

thus a means of livelihood for the majority of the population not accommodated in the formal employment or engaged in subsistence farming.

The development and promotion of this sector is high on the government developmental agenda. The generic problems of small businesses include:

- Lack of understanding of international trade practices and policies;
- Low product quality and inferior production technology;
- Ineffective marketing
- Limited access to credit and finance;
- Poor supply chain management; and
- Poor labour skills

The government, as articulated in the Private Sector Development Strategy, is committed to creating an enabling regulatory and institutional environment that allows local entrepreneurs to strengthen their productive capacities and competitiveness. This is also crucial for the industrialization process of the economy.

1.4.3. The textile sub-sector

The development of the Lesotho textile sub-sector in recent years is indicated in Table 4 below. This clearly shows the effects of the market down-turn in 2005 and the partial nature of the recovery of 2006. It also indicates that the sub-sector is largely focussed on garment production – mainly top-weight knitted fabric products (T-shirts above all) and bottom-weight trousers/slacks (especially jeans).

However, the table also addresses the criticism often made of the present concentration on the production of garments for exports in that it creates no backward/forward linkages to other sectors of the economy. As a direct result of the expansion of demand from the garment industry caused by the AGOA the CGM Group was encouraged to invest in the Formosa Denim Mill which was commissioned in 2004 to supply jeans (and other denim product) manufacturers. In addition, there are 4 companies supplying services to the garment industry such as embroidery, screen-print and home-textile production.

Although this is not indicated in the table, there is also a plant dedicated to the production of packaging for the garment industry. In addition, the very existence of the industry creates a demand for formal services in such areas as freight[4], finance, retailing and

[4] However, the World Bank Investment Climate survey for 2005 found that most of the international freightage on which the Lesotho garment industry depends to carry its raw materials from and its export shipments to Durban or Port Elizabeth is supplied by South African companies as Lesotho suppliers cannot meet the heavy insurance standards required to operate in the RSA.

accommodation of all sorts. Much of the expansion of the informal sector in recent years (about which too little is known) is likely to have come about as a result of the development of the demand for services of various kinds encouraged by the expansion of garment production.

1.5. BARRIERS TO INDUSTRIALIZATION

1.5.1. Eroding Trade Preferences

1.5.1.1. The USA Market under AGOA

Lesotho products in the US market are wholly dependent on the AGOA preferential trade arrangement (PTA) and, more particularly, the Special Provision relating to Third Country fabrics. In 2004, 98 percent (99.5 percent in both 2005 & 2006) of all Lesotho textile exports to USA were under AGOA.

AGOA is a non-reciprocal arrangement – i.e. it is offered by the USA, but creates no obligations on the beneficiaries– and has a life span that ends in 2015. However, its most significant provision from the point of view of industrial development in Lesotho, the SP, expires in 2012. Furthermore, as from September, 2007, the advantages of the SP may be balanced by the “Abundant Supplies” provision of the fourth amendment to the AGOA tacked on to the bill by the US legislature.

The “Abundant Supplies” provision could effectively nullify the operation of the Special Provision if the US Trade Representative (USTR) determines that there is sufficiency of any fabric being produced in the AGOA beneficiary states to meet regional demand. The USTR may interpret this to mean that, because Lesotho and other SSA states (notably the RSA) produce denim fabric, garment producers in SSA beneficiary states should, therefore, obtain their requirements of this material either from those sources or the USA and consequently cannot claim the AGOA preference if they use materials from Third Country sources. This would be to ignore the fact that, despite the addition of the fabric produced by the Formosa mill to SSA supplies, the region does not produce denim fabric in a sufficient quantity for its needs and certainly not all the different categories of the material required by its garment industry.

Table 4: Profile of Lesotho textile industry

Industry sub-sector	July 2004		July 2005		July 2006	
	Workers	**Establishments**	**Workers**	**Establishments**	**Workers**	**Establishments**
Garments	**47,384**	**45**	**38,951**	**38**	**44,324**	**42**
- Trousers (woven fabric)	15, 167	8	16,204	8	17,136	10
- Tops (knitted fabric)	32,217	37	22,927	30	27,188	32
Fabric (denim) and yarn	0	0	1,045	1	1,155	1
Embroidery, screen-print, home textile	703	4	188	3	410	4
	53,087	**49**	**40,364**	**42**	**45,889**	**47**

Source: Derived from "Economic Situational Analysis", ComMark Trust: February, 2007

The consequence of the ‘Abundant Supply’ clause is that the Lesotho industry could lose some of the benefits of the Special Provision as early as the end of 2007 and, thus, a significant comparative advantage in the US market relative to its international competitors. Furthermore, even if this does not take place and the SP is unaffected until 2012, the advantages Lesotho producers enjoy in the US market as a result of this provision will be reduced as a result of expected reductions in US MFN tariffs under the WTO NAMA programme which may begin as early as 2008.

This progressive diminution of the benefits of AGOA has serious implications for Lesotho. Statistics show that the 66 percent of the manufacturing firms that rely on the USA market employ 93 percent of the total labour employed in the Industrial sector, which is currently the leading employer. It is against this background that the Government is committed to finding solutions that reduce the country’s reliance on a single sub-sector (garments) and a single market even though this approach has so far been highly effective in terms of achieving economic goals. Several studies have been carried out to identify potential areas for diversification of industrial activity.

1.5.1.2. Expiry of the MFA

The termination of the Multi-Fibre Arrangement (MFA) of the General Agreement on Tariffs & Trade (GATT) at the end of 2004 was expected to adversely affect Lesotho’s garment export sales and this expectation was justified insofar as the measure did remove the quantitative restrictions (quotas) previously imposed on Asian garment and textile exporters in the US market – particularly those on the People’s Republic of China (PRC). Other countries such as Lesotho affected by this development included Bangladesh and Cambodia. On the other hand, Lesotho continued to enjoy a significant comparative advantage over these competitors insofar as, under the AGOA, it escaped the US MFN duties on garments averaging around 17 per cent to which these countries were still liable.

In fact the impact of the expiry of the MFA was less severe than had been expected. For instance, exports from Bangladesh and Cambodia declined tremendously while Lesotho did experience some decline but not as acute as had been expected. To some extent this was a consequence of China’s accession to the WTO in 2002 which had the effect of reducing substantially the quotas previously placed on its exports to the USA as a non-member thus reducing the effect of the formal expiry of the MFA two years later. (This was, in any case, mitigated, as the USA continued to impose quotas on China as it is allowed to do under China’s WTO accession agreement until 2008). In the case of Lesotho it is difficult to distinguish the effects of the removal of the MFA quotas in the US market from that of the strengthening of the Rand against the US dollar which created significant problems for its garment suppliers who are obliged to operate in an international market which is denominated in terms of dollars.

Nevertheless, the consequences were serious enough for Lesotho. Its garment exports declined by 13 percent from 2004 to 2005 and 8,000 jobs were lost as a result of six (6) firms closing down. From 2005 to 2006 there was a slight recovery of 2.2 percent in textile exports to the USA.

1.5.1.3. Textile and Clothing Industrial Development Programme (TCIDP)

An important element of the competitiveness of the Lesotho industry in the US market was the availability of the TCIDP incentive which is estimated to be equivalent to a net benefit of14 per cent of producer's export selling price. It is likely that this scheme alone prevented a far greater number of Lesotho producers from closing their doors during the down-turn in export activity in 2005-6. Even in the present slightly improved state of the US market the TCIDP is still considered critical to the survival of the garment industry in its present form.

However, the scheme appears to be non-WTO compliant and it is likely that it will be abolished as from April, 2007, by SACU members. As an LDC, Lesotho is the only SACU member-state which could be exempted from the WTO ruling. However, it will follow its fellow members if they decide to abolish the scheme. Alternatively, given the importance of the TCIDP to the export competitiveness of the Lesotho garment industry, a similar, but WTO-compliant programme may be adopted. This would terminate on 31 March, 2014.

1.5.1.4. Global Outlook

As already indicated, at a multilateral level the on-going Non-Agricultural Market Access (NAMA) negotiations are also leading to preference erosion in a sense that they are likely to drive down the global tariffs. In particular, Lesotho will lose the duty-break averaging around 17 per cent on its garment exports in the US market which presently gives it a significant advantage against its Asian competitors. How far its suppliers will be able to compete in the US market when this is removed and the remaining quotas on Chinese suppliers are also dismantled is problematical. It also casts a cloud over their chances of developing and holding onto market outlets in the EU which is another major objective of the IMP.

The WTO is committed to adopt specific measures that would facilitate the fuller integration of small, vulnerable economies into the multilateral trading system. For instance, the principle of "Special & Differential (S&D) treatment" for LDCs such as Lesotho will in theory allow it to reduce its tariffs at a lower rate than its more developed trading partners. However, in the case of Lesotho, this concession will inevitably be qualified by its membership of the SACU which imposes a Common External Tariff on all its members (the CET) which takes no account of the disparity between the economic development of the RSA and the BNLS group including Lesotho. There is provision in the SACU agreement for the BNLS countries imposing higher tariffs than the RSA, but this mechanism is untried and, in any case, the practical difficulties inherent in the implementation of such a provision in the SACU context are formidable.

In any case the "S&D" principle affords little prospect of being of assistance to Lesotho when that country's interest is that major trading partners should maintain existing MFN tariffs against Third Countries thus sustaining the relative comparative advantage it presently derives from its preferential access to their markets. This paradox highlights the need to seek changes in the current network of Non-Tariff Barriers (NTBs) to Lesotho's advantage – a point discussed in more detail in section 5 below.

1.5.1.5. The 2005 experience seen as a warning

The government views the decline in garment exports in 2005 with only a limited recovery in 2006 as a warning of the dangers in its present industry structure which relies on one industry producing one category of product for one market. While every effort will be made to maintain (and, if possible, expand) garment sales to the US market because of the importance of this activity in present employment patterns, it is recognised that this can be no more than a temporary expedient: it is necessary that the other markets are found and developed and that the present industrial structure diversified. This will be a major objective of industrial policy.

1.5.2. Infrastructure Constraints

Studies and surveys carried out reveal some sort of a consensus when they make allusions to the infrastructural capacity. The consensus is that there are serious infrastructure constraints that stifle the efficiency (and growth) of the industrial sector. The following constraints have been identified:

1.5.2.1. Lack of pre-built factory shells

Present restrictions on the ability of private sector enterprises to acquire titles to the land they occupy means that there is little incentive for investors to develop manufacturing premises and the provision of such facilities by the Government has, accordingly, been an essential element in its ability to attract investment projects to Lesotho. However, currently unoccupied factory shells exist only in Mohale's Hoek while those in other designated industrial estates such as Thetsane, Nyenye, Maputsoe, etc. are fully occupied. Unless this is addressed as a matter of urgency, efforts to attract the additional investment which is regarded as essential will be of little consequence.

1.5.2.2. Lack of serviced industrial land

Another priority is the identification and designation of industrial estates. Currently there is a designated industrial location, at Ha Tikoe on the outskirts of Maseru beyond Thetsane. There is an urgent need for more such locations to be identified **and developed** given the importance of the growth of the Industrial Sector for the achievement of national development objectives.

1.5.2.3. Inadequate water supply & Lack of waste water treatment facilities

The Lesotho industrial sector is dominated by the garment sub-sector which is regarded as a 'wet' industry due to the amount of water it uses in its operations. According to the World Bank's "Investment Climate Assessment" (ICA) report, manufacturing enterprises suffered inadequate water supplies for about 10 days in 2004. This is a matter of concern and a number of manufacturers are currently using boreholes to supplement the public water supply. Paradoxically the problem is to large extent a consequence of the very low cost of water in Lesotho. Tariffs are so low that the revenue yield is inadequate to finance the construction of an adequate public supply or even to properly maintain the existing supply infrastructure. (In 2004 it was reckoned that some 40 percent of the total supply was lost as a result of leakages).

The problem is exacerbated by the fact that industrial estates in Lesotho suffer from inadequate water-treatment and sewerage facilities. As a result not only is it not possible to recycle used water, but also untreated water is discharged into the environment laying up problems for the future.

1.5.2.4. Electricity

The cost of electricity is low in Lesotho compared to many countries in the region and even by international standards. However, it is higher than in the RSA which is significant given that the government hopes to attract investment from that country.

In any case the main problem with the electricity supply for Lesotho industrialists is not its costs, but its inadequacy which brings about outages which slow down operations and result in loss of production. Again their experience in this respect is worse than that of their counterparts in the RSA with an average of 12 outages lasting 3 hours being reported during 2004 according to the ICA report[5]. However, power outages in Lesotho are less common than in many other countries in SSA.

1.5.3. Access to credit

The difficulty of accessing credit is a significant constraint on investment. However, this largely affects indigenous rather than foreign investors who seem largely to rely on banks in their home-countries or on their parent companies for their credit needs.

To some extent the problems experienced by indigenous investors reflects the difficulties in arranging adequate collateral given the restrictions of the land law. However, there seems to be wide-spread disillusionment with the operation of the system of justice on grounds of its slow pace and the uncertainty of outcome and this is an additional factor underlying the reluctance of the commercial banks to extend credit to potential local entrepreneurs. In short, the banks are not confident that the courts will support them in their efforts to foreclose on property advanced as collateral even where this is available. The government will address this issue.

1.5.4. Labour – Related Factors

1.5.4.1. The HIV/AIDS Pandemic

The current HIV/AIDS prevalence has severely reduced life expectancy. From the GoL's point of view, labour intensive projects are desirable. The impact of HIV/AIDS on labour productivity (most notably through absenteeism) is a constraint that is likely to frustrate efforts to attract labour intensive projects.

1.5.4.2. Low Labour Productivity

The documented low labour productivity in Lesotho against comparator countries in terms of wage competitiveness may turn out to be a constraint in persuading investors to view Lesotho as a destination of choice for their operations. The ICA report already cited above observes that value-added per worker in 2002 averaged US$2799 in Lesotho across all manufacturing sectors. This was higher than in Mozambique (US$500) and

[5] ICA - Invest Climate Assessment Report (World Bank)

Tanzania (US$2650), but lower than Kenya (US$3200), Senegal (US$6000), China (US$4500) and India (US$3800) (2001 figure). In South Africa is the comparable figure was about US$14000 per worker.

Overall unit labour costs – i.e. wages and salaries as a percentage of value added – is generally considered a superior indicator of international competitiveness than added value per worker as it allows for such factors as currency fluctuations and quality of labour. By this measure labour productivity in Lesotho is worryingly low being equal to about 50 per cent of value added across all industries. This was higher than in any of the comparator countries and is particularly problematic in the light of the impending erosion of trade preference after Lesotho producers' ability to compete internationally will depend on lower manufacturing costs in all areas.

1.5.4.3. Absence of Local Supervisors

The absence of Basotho in supervisory and managerial positions in the industrial firms is a notable reality. The skill and knowledge transfer that is necessary to empower Basotho to operate industries is as a result lacking. This explains the nearly non-existent participation of local firms in the industry.

The ICA report established that only 25 percent of workers in the Lesotho manufacturing sector have 10 years or more of education as opposed to nearly 50 per cent of workers in India and over half the workers in South Africa has the same years of schooling. Literacy rates are high (about 72 percent for adults over 15 years). However, this is perhaps not a good indicator as there is a high drop-out rate between primary and secondary school averaging about 80 percent. This has a disproportionate effect on girls who form a very high proportion of the textile industry workforce and goes some way to explain why Basotho have not been promoted in that industry.

1.5.5. <u>The business environment</u>

Central to the attainment of the IMP objectives (outlined in section 2 below) is the existence of a business-friendly environment that imposes as few obstacles as possible on the conduct of legitimate business activity and facilitates the process of realizing investment projects. Lesotho does not compare well internationally in these terms – i.e. in overcoming what is referred to as 'hassle factor'.

According to the World Bank "Doing Business" report, 2006[6], out of **175** countries Lesotho had an overall rank of 114 having moved up two places from 116 in 2005. Specific areas where improvements were found to have taken place were those relating to 'starting a business' and 'paying taxes' which moved up 8 and 12 positions to 113 and 44 respectively. On the negative side the country's ranking under the heading 'trading across borders' moved down 5 positions to 121. This is of particular concern because most of industrial activity in Lesotho is highly export-oriented and the efficiency of border

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[6] Ranking from http://www.doingbusiness.org

controls is, therefore, crucial. 'Investor protection' and 'contract enforcement' were the other main areas where the country's rating declined in the period to 142 and 130 respectively. There was no change to its rating of 117 in respect of 'getting credit' although, as has been noted, this is a major area of concern by indigenous businessmen.

A closer look at a number of these indicators reveals that the problem in Lesotho is efficiency and perhaps not bureaucracy. For instance, there are 8 procedures (bureaucracy indicator) in starting a business compared to an average of 11 in SSA. However, to go through these procedures takes 73 days in Lesotho compared to only 62 days in SSA (efficiency indicator). Table 5 below summarizes the report findings.

Table 5: Ease of Doing Business in Lesotho-Bureaucracy vs. Inefficiency

	Lesotho	**RSA**	**SSA**	**OECD**
Starting a Business				
Number of Procedures	*8*	9	11.1	6.2
Number of Days	*73*	35	61.8	16.6
Dealing with Licenses				
Number of Procedures	*14*	17	17.7	14
Number of Days	*265*	174	230.2	149.5
Paying Taxes				
Number of Payments per year	*21*	23	41	15.3
Number of Hours in a year	*352*	350	336.4	202.9
Trading across Borders				
Import Documents (Number)	*9*	9	12.2	5.9
Import Time (Days)	*51*	34	51.5	12.2
Export Documents (Number)	*6*	5	8.2	4.8
Export Time (Days)	*46*	31	40	10.5

Source: http://www.doingbusiness.org

On average the neighboring RSA and the SSA region as a whole are more heavily regulated than Lesotho. However, the relative efficiency with which the bureaucratic procedures are dealt with in terms of time spent on them make these places better places to do business than Lesotho. The achievement of greater efficiency merits priority in the government's efforts to improve the business environment.

1.6. RATIONALE FOR INDUSTRIALIZATION

The contextual outline above has shown that, within the context of the national **Vision 2020** and the resulting PRS, employment generation leading to poverty reduction is a policy priority. The Industrial Sector through the garment sub-sector has so far served this purpose with distinction, indicating that the industrial activity offers the realistic potential of creating jobs in the numbers required to make some impact on poverty. Policy guidelines for capitalising on this potential are set out in the following sector.

The manufacturing sector through the garment sub-sector has so far served this purpose with distinction, indicating that the Industrial Sector offers the realistic potential of creating jobs in the numbers required to make some impact on poverty. Against this background the government acknowledges the need to have a clear policy position with which to work towards preserving and prolonging the current manufacturing sector, which is currently the country's number one employer. Within that area of focus, two broad lines of activity emerge. The first activity line is to diversify within from basic jeans and t-shirts to other high value commodities within the garment product line. This *within-diversification* will dilute the current over-specialization and bring with in it an expansion of the export base targeted at already existing markets. The second activity line is *between-diversification*, which is essentially diversifying into other products besides textiles and garments.

Not withstanding the impressive achievements of the manufacturing sector based on garment exports, there are challenges ahead. The success of the manufacturing sector was based not only on one product line, but also on one market, the USA under AGOA PTA. Access to the EU was adversely affected by the rules of origin clause of the Cotonou agreement. (As already noted, the withdrawal by the EC in 1996 of the derogation from the rules of origin regime that it had earlier granted Lesotho as an LDC largely destroyed the significant garment trade with European markets that the country had enjoyed in the early 1990s). However, erosion of trade preferences does not make the industrial sector any less promising as a major source of additional employment opportunities.

As a result, the government is committed towards creating an enabling (business-friendly) investment environment that will attract further FDI and encourage domestic private sector participation. In particular the government undertakes to:

- Intensify efforts in the pursuit of export-led growth by encouraging and facilitating both product diversification (which essentially is identifying other products besides garments) and market diversification (facilitation of market outlet repositioning through negotiating market access and other trade arrangements). With respect to product diversification, several studies have been carried out to this effect and recommendations made on sectors and products with that potential.

- Promote and support the domestic private sector to be involved at a scale commensurate with the national aspirations of employment generation and ultimately poverty reduction.

2. LESOTHO INDUSTRIAL[7] DEVELOPMENT POLICY

2.1. INTRODUCTION

This section sets out the policy principles and guidelines that will inform the analysis of the effectiveness of the government's current industrialisation activities in section 3, the consideration of additional activities that need to be undertaken in section 4 and the IMP programme of activities set out in section 5. The policy outline has been developed in the light of the historic review of the development of the Industrial Sector carried out in section 1.

2.2. OBJECTIVES OF INDUSTRIALISATION POLICY

2.2.1. General Objective

As demonstrated in section 1, the expansion of the industrial sector of the economy has in the past made effective contribution to the achievement of national economic goals. The general objective of the Government of Lesotho industrial policy is, therefore, to promote further industrial activity in Lesotho's economy with a view to ensuring that the sector plays its part in achieving the Vision 2020 goals.

Achieving the **Vision 2020** goals requires:

- Increasing domestic employment opportunities and thus reducing poverty;
- Increasing foreign exchange earnings to compensate for loss of remittances from Basotho working abroad, especially in the RSA and the downturn in earnings from garment exports; and
- Augmenting government revenue sources to compensate for reductions in yield from the SACU revenue pool consequent on the opening of the SACU market to increased foreign competition as a result of preferential trade arrangements;
- Encouraging greater indigenous participation in economic activity.

[7] For the purpose of the IMP the Industrial Sector of the economy is considered as being that sub-sector of the Secondary Sector defined as "Manufacturing" in official statistics. (See also Table 1 above). It is, therefore, differentiated from Agriculture, Mining and Quarrying, Construction, Government activity and Services.

2.2.2. <u>Specific Objective</u>

Given this general objective and the present situation of the Industrial Sector, the specific objective of the IMP will be to maintain present levels of garment exports to the US market despite the depressing effect of the present weakness of the US dollar against the South African rand and the likely erosion of the value of the trade preferences in the US market enjoyed by Lesotho on which the expansion of trade with that country has been built.

In adopting this as a principal objective of industrial policy, the government recognises that garment exports to the USA support an industry that sustains large numbers of jobs which will not easily be replaced. Everything that can be done to prevent a downturn in this trade will therefore be done. However, given the disadvantages inherent in the present over-reliance of the economy on the garment sub-sector and the likelihood that Lesotho's trade with the USA will come under increasing pressure as a result of developments in the world market beyond the control of the government, the IMP will place equal emphasis on the need to diversify the activity of the industrial sector.

The IMP identifies the **textile sector** as a promising area for diversification of existing activity, particularly the following:

1. The revival of Lesotho's former garment export sales to EU markets as a result of improved access negotiated under the Economic Partnership Agreement (EPA). However, the government is aware that even if less restrictive Rules of Origin can be secured in the EPA negotiations, Lesotho will face an erosion of the value of its preferences in Europe as in the USA. Any increases in the volumes exported to European destinations as a result of successes in this area are likely to be limited and tend to diminish over time. Nevertheless, this objective is considered worth pursuing as an interim measure while other opportunities are developed;

2. The development of knitwear production units aimed at the US and EU markets to diversify away from the present concentration on bulk commodity products (jeans and tops);

3. The revival of Lesotho as an industrial location for the manufacture of garments for the SACU/SADC markets, in particular the RSA. Here the government considers that there is an opportunity to develop Lesotho as a location for manufacturing higher value garments which are required in relatively small volumes with short delivery periods. This sort of demand cannot be easily serviced by East/South Asian suppliers which tend to concentrate more on high-volume commodity products and Lesotho enjoys the advantage of proximity.

4. The promotion of further investment in fabric (knitted and woven) and yarn production to supply the SACU/SADC regional market. As noted in section 1, Lesotho has already succeeded in attracting investment in a major project in the area of woven fabric (denim) production. Success in this area will contribute towards the creation of further backward linkages for the existing garment

industry, the absence of which has been a significant (if over-stated) defect of the present structure of the textile sub-sector

However, under the IMP the government will also seek to promote investment in sub-sectors **other than textiles and garments**. It is envisaged that the most promising areas for such development will include:

1. Adding value to Lesotho's output of agricultural and mineral materials by processing this in-country prior to export. Such operations will be those which can be justified by strict commercial criteria: the mere fact that materials are produced in Lesotho will not be considered a sufficient argument for processing them here when economic logic suggests they be exported with only minimal refining. The regional market will probably be the main outlet for such operations;

2. The establishment of assembly operations in such areas as electrical appliances and electronics where the existence of relatively low-cost labour already accustomed to industrial disciplines will give Lesotho a comparative advantage as a manufacturing location if drawbacks arising from low labour productivity can be overcome. Again such operations are most likely to be oriented to regional markets; In addition, the government will

3. Review possible import-substitution activities to identify areas where it might be feasible for Lesotho to produce, for the SACU market, goods currently imported into the region.

In pursuit of the above, the IMP will actively promote the development of **indigenous private sector** industrial activity. This will include encouraging Lesotho entrepreneurs to invest in projects oriented to the export market. However, equal emphasis will be placed on the need to develop the activities of the SMME sector which, at least in the early stages of their development, will probably concentrate on servicing the local market. This will require a concerted programme to develop skills and inculcate knowledge of business principles while facilitating access to credit all of which are presently identified as constraints. As was demonstrated in section 1.4.2, this sector already makes a major contribution to employment creation and IMP will seek to develop it as a major contribution towards the realisation of policy objectives.

2.3. GUIDING PRINCIPLES OF INDUSTRIAL POLICY

2.3.1. Role of Government

The role of the government in the development of the industrial sector will continue to be based on open market principles. This takes into account the limited scope for state intervention given that:

- The economy is exposed to external influences beyond the control of the government; while

- The effect of the international preferential trade agreements to which Lesotho is a party makes it impossible for the government even to attempt to protect industry from these influences in the domestic market by use of tariffs or NTBs. The main obstacle to the pursuit of an autarchic economic policy is membership of the SACU which allows for the imposition of duties above the union's Common External Tariff (CET) to protect 'infant industries', but which renders this difficult to achieve in practice.

In practical terms a free market approach means that the government will **facilitate** the process of industrial development and will not intervene directly to **bring about** such development.

Its main tools in this respect will be the macro-management of the economy to encourage an environment favourable to the growth of export-oriented industrial activity. In this respect, its main areas of activity will be:

- The continuation of a **tax-regime** as far as possible favourable to investment;
- The transparent administration of a regime of **investment incentives** that does not discriminate between
  - FDI and domestic investment; or between
  - Investment projects in different sub-sectors;
- The maintenance of a transparent **regulatory framework** for industrial activity, which is non-discriminatory as between different categories of investor and which minimises the scope for administrative discretion in the levying of fees and the issue of licenses and impinges as little as possible on the cost of doing business;
- The pursuit of a foreign trade policy designed to maximise the **access** to foreign markets enjoyed by suppliers of Lesotho goods and services. In this respect the government attaches as much weight to the need to secure non-restrictive Rules of Origin for its trade as to reduced tariffs;
- The provision of timely and accurate **intelligence** as a basis for sound decision-making by both the Public and the Private sectors. This includes:
  - Up-to-date economic statistical series regularly published;
  - Details of investment opportunities;
  - Information on major external markets.
- The provision of **general educational facilities** of a high standard and **appropriate support for technical education**;

- The maintenance of public order and support for the judiciary, appropriate definition of private and public property and an equitable Law of Contract;

- The development and maintenance of the physical and communications infrastructure required for the successful operation of the industrial sector. Present restrictions on land ownership make it necessary for the government to play a major role in the provision of serviced manufacturing locations and factory shells for leasing to investors. The government will vigorously engage in this area while continuing to seek modifications to the present Land Act to bring about an environment more conducive to industrial development.

Industrial policy will largely consist in ensuring that the above functions are carried out as far as possible in a manner favourable to industrial development and likely to enhance the environment for all business in Lesotho. This requires a dedicated institutional framework capable of monitoring the whole range of government activity and of assessing the impact on the industrialisation process of the specific activities of government agencies and ensuring that these are carried out in full awareness of that impact. See section 2.4.

The government will not attempt to micro-manage the development of the industrial sector. This means in particular it will not seek to identify specific developments to which it will give material support. Investment incentives will be made available to investors in any sub-sector on a non-discriminatory basis on the fulfilment of defined (and well-publicised) criteria. Above all, the Government will not act as a venture-capitalist in respect of particular projects.

However, this commitment not to intervene at a sub-sectoral level to bring about specific outcomes will not preclude government from giving focussed support to particular development promotion activities. For the time-being this will include facilitating access to finance for indigenous investors in projects which meet strict commercial criteria as a means of encouraging local entrepreneurship although this facility will only be used to finance contracts already secured and will not be available for capital investment.

2.3.2. Role of Private Sector

The Private Sector is the main engine of industrial growth and policy is formulated and implemented on this understanding. Only projects for which private risk-capital is forthcoming will be approved as recipients of available investment incentives from public sources and these incentives will not be used in a discriminatory way to distort the market in order to favour developments in any particular industrial sub-sector. An exception will be made here in the case of preferential finance for indigenous investors in particular circumstances as referred to in the previous section.

As will be noted in section 2.3.3.6 – for the foreseeable future most investment is likely to come from foreign sources. However, as indicated in section 2.3.4, the present significance and potential of indigenous entrepreneurial activity requires that it should be brought into the IMP process.

Other non-government agencies, including the Trade Unions, concerned NGOs and Academe also have a legitimate interest in the success of the IMP and will be meaningfully involved both in its development and implementation and be in real sense part-owners of the policy that the plan encapsulates. This is a necessary condition of its success.

The institutional structure discussed in section 2.4 considers the basic mechanisms by which the participation of these various non-government actors in the IMP process will be more effectively secured.

2.3.3. <u>Emphasis on development of export-oriented industry</u>

2.3.3.1. General considerations

The IMP will continue established policy by giving priority to the development of export-oriented activity. This reflects the realities of Lesotho's economy. To be internationally competitive, production units must enjoy economies of scale in their operations which require that they must serve large markets. However, the small size of the national population and the low level of *per capita* income make it difficult to justify such units on commercial grounds when they are oriented towards the Lesotho domestic market. Furthermore, the international trade arrangements to which Lesotho is a party – in particular its membership to SACU – largely precludes the possibility of protecting its domestic producers from low-cost import competition by means of high tariff and non-tariff barriers.

However, the IMP will also seek to mitigate the less desirable consequences of the necessary reliance on export-oriented production. The present emphasis of industrial activity on exports of garments to the USA and the failure to attract significant investment in other industrial sub-sectors despite nearly forty years of preferential access to EU markets under the Lomé and Cotonou arrangements and the unparalleled generosity with which the country is treated under the US AGOA regime underlines the need for this. The downside for Lesotho of the present over-heavy reliance on the garment sub-sector is considered in some more detail in the following section.

2.3.3.2. The garment sub-sector

As a massive creator of employment, export-oriented garment production is a major force for the alleviation of poverty and thus addresses very well one of the main objectives of government economic policy. It is also important in that it encourages the emergence in Lesotho of work-force accustomed to the disciplines of industrial employment – in effect developing a national working class. The existence of such a work-force will be a major attraction for investors in other industrial sub-sectors.

However, the industry's dependence on Third Country fabric sources and its subordination to overseas associates for most material purchasing and product marketing activity means that the Lesotho garment industry is to some extent insulated from the rest of the industrial sector and the Lesotho economy as a whole. It is able to play, at most, a limited role only in promoting sympathetic development in other industrial sub-sectors.

The government acknowledges that it is probably not possible to change this situation although, under the IMP, active consideration will be given to ways in which it could make greater use of local services – see Table 8, intervention, No. 27 (Business Linkages project).

Furthermore as an exporter outside the SACU region, the industry is largely excused payment of company income tax. As will be argued below, the benefits of this situation are judged to outweigh the costs and, indeed, there are sound arguments for extending this tax-break to exports within SACU as well. However, it does mean that the industry's main contribution to the public revenues comes from the VAT paid by its workforce on purchases of consumer goods – although the importance of this as a developing source of tax income should not be denied.

2.3.3.3. Revenue impact of reliance on export-oriented industrial activity

The impact on revenue-yield of an industrialisation policy that relies on a tax-break on export earnings for attracting investment is not, of course, unique to the garment sub-sector: the same problem arises in the case of any sub-sector where this concession is a necessary condition of attracting investment – as it certainly is in the case of Lesotho. In these circumstances, governments have the option of deciding to forgo revenue in order to bring about the desirable benefits of industrialisation (including employment creation). They can, on the other hand, seek to maximise revenue by taxing export earnings. However, the latter approach will probably deter investment and thus limit any increase in tax-yield while having a devastating impact on employment-generation. The government will continue to pursue the former course.

2.3.3.4. Main markets

The main markets in which Lesotho will seek outlets for its industrial products are the USA and the EU. This reflects the sheer size of these markets and their insatiable demand for imports – albeit in the case of Lesotho these have been largely confined to garments. Under the IMP the government will not ignore opportunities to promote investment in other sub-sectors oriented to these markets. However, as already suggested above, the most likely scope for diversification of existing trade lies in attracting projects in other areas of the textile sub-sector – notably knitwear and clothing based on the use of knitted fabric. In the meantime the government will seek to maintain for as long as possible the existing trade in garments in the case of the USA and to revive it in the case of the EU.

However, acknowledging the historic reluctance of non-garment investors oriented to the USA and the EU to locate in Lesotho, the IMP will seek also to expand and diversify its trade with other outlets. To this end its African neighbours seem to offer the greatest opportunities. Under the IMP investment will be sought in projects aimed at the SACU market – particularly the RSA as by far the largest partner in this grouping – and at the wider SADC region. There are opportunities for investment in textile and non-textile projects.

Despite the priority that should be accorded to export-oriented activity in the formulation and implementation of government policy the government will take measures under the IMP to promote the growth of SMEs engaged in industrial production, which will normally be oriented to the domestic market or the market for artisan products. The reasons for this are discussed more appropriately in section 2.3.4.

2.3.3.5. Emphasis on labour intensive operations

Industrial policy recognises that Lesotho's chief comparative advantage as a location for industrial activity is the relatively low cost of its labour, even though this advantage is presently off-set by low levels of labour productivity. Nevertheless investment will most probably be attracted to labour intensive sub-sectors[8]. This understanding will inform decisions concerning specific investment promotion activity undertaken under the IMP. However, the IMP will actively promote investment in projects based on the use of Lesotho's agricultural materials and its mineral base, where such projects are judged to meet strict commercial criteria. The commercial feasibility of selected import-substitution activities will also be considered.

2.3.3.6. The importance of FDI

The IMP acknowledges that FDI will be the main source of finance for export-oriented industrial development projects. This reflects both the inadequacy of domestic sources of finance available for investment in industrial enterprises and the presently limited availability of local technical expertise. However, the government will actively explore ways of encouraging greater readiness by local capitalists to invest in industrial projects.

2.3.4. Role of local entrepreneurs

Despite what has been said in the previous section, industrial policy will also acknowledge that local entrepreneurs in the form of SMMEs operating in both the formal and informal sectors of the economy, do play a significant role in the creation of economic activity and employment opportunities. They thus constitute a significant factor in poverty reduction, although they could probably make a greater contribution in this respect. Another consideration in this regard is that the growth of the formal SMME sector should also, in the longer term, promote the development of indigenous capital resources and technical expertise. These are good and sufficient reasons why the IMP will actively promote indigenous SMME activity.

To this end under the plan the government will:

- Continue and expand present programmes for the training in technical and business skills for potential entrepreneurs; it will also seek to

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[8] In making this prediction the GoL has regard to the recent (2004) commissioning of a denim mill which is generally regarded as a capital-intensive investment.

- Promote the local sourcing of goods and services by the larger, internationally-oriented companies where this offers a commercially viable alternative to existing arrangements; in addition, as already indicated

- Make available credit guarantees to indigenous investors whose projects are judged to be commercially viable to ease the problems of accessing credit;

- Continue the policy of giving a 15 per cent preference to local suppliers in government procurement contracts; and

- Consider ways of increasing confidence in the certain and impartial delivery of justice in commercial cases insofar as this is seen as a constraint on the availability of credit.

2.4. POLICY FORMULATION AND IMPLEMENTATION – THE INSTITUTIONAL FRAMEWORK

The institutional structure required to manage the implementation of the IMP will have the following characteristics:

- It will represent all the stakeholder interests in an effective manner and impart to each of them a sense of ownership and control of the IMP;

- It will provide for a single agency mandated to exercise an ongoing overview of all aspects of government activity by all agencies so that policy is both formulated and implemented at every level with a proper understanding of its impact on the IMP; and

- It will be represented at a sufficiently high political level as to ensure that necessary actions and adjustments to further the IMP can be undertaken expeditiously and effectively.

These considerations suggest that the Core group on Industrialisation Matters established by the MTICM to develop the IMP, and committees (Industrialisation Technical Committee and Inter-Ministerial Task Team (IMTT)) will be a useful basis for the more permanent institutional arrangements that will be required to implement the plan. The mandate of the core group will be appropriately extended and its membership reinforced to make it an even more effective instrument by which the stakeholders can influence the formulation and implementation of industrial policy within the framework of the IMP.

However, attention will also be given to the need to ensure that adequate arrangements are in place for monitoring and coordinating activities of other ministries and other agencies whose functions impinge on industrial policy to ensure that they operate in full understanding of the needs of the IMP. The government intends that this unit will be located within the Industry Department, MTICM, and will act as the secretariat for the core group.

2.5. IMP PRIORITIES

The IMP will consist of a programme of activities within an overall framework intended to achieve the objectives of the plan. Such activities were for the most part identified within the Ministry of Trade and Industry, Co-operatives and Marketing framework document[9]. The effective realisation of the objectives of industrial policy requires that specific activities be prioritised in the IMP.

The criteria that will determine priorities for action under the plan are as follows:

- Whether planned activities:

  (i) are attuned to the achievement of the specific objectives of industrial policy as set out in section 2.2.2;

  (ii) Are realistic insofar as they reflect what is feasible given Lesotho's economic circumstances; and

  (iii) require government action to bring them about; in the case of individual activities under the IMP priorities will be determined by

- The extent to which their successful execution is likely to be critical to that of other proposed actions or to the IMP programme overall;

- The need to address the issue of the adequate provision of serviced industrial sites which is critical to industrial development given the present restrictions on private ownership of industrial land;

- The need to address the availability of credit, particularly for indigenous investors;

- Whether the timing is constrained by factors not susceptible to control by the government - as in the case of on-going trade negotiations;

- Whether the government has the capacity to implement them. Where technical assistance is required account will be taken in determining the priority of an activity of the lengthy delays usually associated with the launching of donor-funded service contracts;

- Whether or not legislation is required and the contentiousness of the activity under consideration. Thus early attention will be given to the improvement of administrative procedures that presently tend to discourage investors.

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[9] 'Framework for developing Industrialisation Master Plan for Lesotho': Ministry of Trade & Industry and Co-operatives and Marketing, revised September, 2004.

3. POLICY IMPLEMENTATION - INVENTORY OF CURRENT MEASURES TO PROMOTE INDUSTRIALISATION

3.1. INTRODUCTION

In support of industrialization, the government has coordinated a wide range of activities. This section compiles an inventory of current (implemented and planned) activities aimed at promoting industry and the private sector at large.

The inventory in Table 6 below groups the government interventions into broad categories: institutional structures; promotion initiatives; infrastructure constraints; access to credit; the business environment; and labour productivity issues. Each activity or intervention is scored on the basis of its **perceived** effectiveness in promoting industrialization or private sector development. The score is a point scale from 1 = least effective to 5 = very effective. A number of interventions herein are in the planning stages. All such are scored as ineffective simply because there is no track record against which to review their effectiveness. Good intentions are not taken into account in determining the appropriate scoring

Table 6: Measures currently undertaken under industrial policy

Intervention	Description of Intervention	Institution	Effectiveness Score (1 – 5)	Score Narrative
Investment Promotion Initiatives				
Investment Promotion Structures / Institutions				
Lesotho National Development Corporation (LNDC)	A statutory corporate body established by the government with a mandate to promote investment – both foreign and domestic. Also provides the after-care service to foreign investors in matters such as industrial relations, counselling, compliance, and other forms of assistance. Infrastructure-wise, LNDC is charged with developing industrial estates and in addition to that provides factory space to the manufacturing industry.	LNDC	3	▪ Succeeded in promoting and facilitating foreign investment. ▪ No success on the domestic front.
Basotho Enterprise Development Corporation (BEDCO)	A statutory corporate body established by the government with a mandate to promote Basotho entrepreneurs. Present services offered are industrial work space and facilities, business counselling, training, and preparation of business plans. Initially it was involved in loan financing for projects costing M250, 000 or less. Projects costing more than that were referred to the LNDC. The fund dried up due to poor recovery and hence the loan financing aspect was discontinued.	BEDCO	2	▪ Perhaps through no fault of its own, was perceived to be ineffective hence creation of SMME network and LNDC taking some of the responsibilities upon itself.
Private Sector Development Section	A Section within the Private Sector Development and Financial Affairs Department of the Ministry of Finance and Development Planning. Main	MFDP	1	▪ Still very new, no track record. ▪ Intent is fine.

Intervention	Description of Intervention	Institution	Effectiveness Score (1 – 5)	Score Narrative
	functions are to coordinate all private sector development activities (by virtue of MFDP being the central ministry) working closely with all other ministries and agencies involved. Ensuring that the government discontinues the activities that can be done by the private sector. (e.g. supply of stationery by the Government Printing.)			
SMME Network	Established to drive the development of the SMME sector. In place there is a White Paper and a Strategic Plan of the network.	MTICM	1	▪ Never got off the ground.
Inter-Ministerial Task Team (IMTT) on Attracting and Maintaining FDI	The IMTT was formed by the Right Hon. Prime Minister and the task team was composed of the following ministers: Employment & Labour, MHAPS, MFDP, Local Government, Natural Resources, MoPWT and MTICM. The composition is reflectively of the wide-ranging issues that the IMTT was tasked to address that have some bearing on industrial development. Private sector (industrialists and labour organisations) were also represented in the task team.	Represented ministries	4	▪ Effectively carried out its mandate.
Investment Incentive Regime				
Fiscal and Related Incentives				
Tax Incentives	▪ 0% tax on income generated from exporting manufacturing goods outside SACU. ▪ Permanent corporate tax rate of 10% for all manufacturing activity.	LRA	2	▪ Most FDI came in before the introduction of this regime.
	▪ No withholding tax on dividends		3	Value of these incentives lies in two areas: Cash

Intervention	Description of Intervention	Institution	Effectiveness Score (1 – 5)	Score Narrative
	distributed by manufacturing firms to local or foreign shareholders. ▪ Duty-free import of industrial materials and components ▪ 125% allowance against training expenses. ▪ 50% of wages of trainees allowed against tax in the first six months ▪ Flexible VAT payment plans to ease cash flows. ▪ Free repatriation of profits. ▪ Uncontrolled foreign exchange access.			flows and Convenience. These are important for the industrialist, but the effectiveness of the measures in attracting investment and causing it to stay is still unclear. However, in different forms most of these incentives have been available since the early 1990s.
Financial Incentives:				
The Export Finance and Insurance Scheme	▪ Credit guarantees to the commercial banks on behalf of the financed exporters. Only 50% of the extended loan is guaranteed by the scheme while the exporter provides collateral for the remainder of the credit extended. The scheme is only for working capital requirements. ▪ In its present form, the primary objective is to assist local exporters because 60% of the entire scheme is set aside specially for them.	Central Bank of Lesotho (CBL)	4	▪ In its previous form – the 1998 version – the scheme was used extensively by large exporters and was considered the best of its type in Africa. ▪ Currently – the 2001 version – there has been no utilization as the conditions are seldom met by the target group (local exporters). ▪ To be reviewed.
Textile and Clothing Industrial Development Programme (TCIDP) formerly known as the DCCS	Lesotho textile and apparel manufacturers can earn Duty Credit Certificates (DCC). These are tradable instruments for which a secondary market exists, and can be used to offset the duty on fabric and garment imports.	MTICM via Baffoe & Associates	4	▪ These are important to the existing investors as their annual value is reportedly around the same as the industry's annual wage bill.

Intervention	Description of Intervention	Institution	Effectiveness Score (1 – 5)	Score Narrative
Development Debt Finance	LNDC provides loan finance to projects that demonstrate long term viability. This is applied for by the project promoter.	LNDC	2	▪ Currently not active.
Equity Participation	Projects that prove to be in the 'national interest' (strategic industries) for which no local investments are found may be considered for this scheme.	LNDC	1	Involves direct government in intervention in industrial development at a sub-sectoral level specifically targeting projects which have failed to attract commercial interest. This has a record of failure in almost every country where it has been tried.
Identification and Promotion of Investment Opportunities				
dentification Commissioned studies on Diversification Options	Identification of activities to aggressively promote in order to diversify away from the textile and garments which is nearly the sole export line. Among the activities identified were the following: Local resource-based projects (e.g. Sand Stone Mining, Water Bottling) Agro-processing, Horticulture, Electronics, Leather Accessories & Footwear.	MTICM	3	▪ The glaring need to diversify acknowledged and acted upon.

Intervention		Description of Intervention	Institution	Effectiveness Score (1 – 5)	Score Narrative
Promotion	Identifying, Lobbying and Negotiating with investors.	▪ The GoL opened and operates a peach cannery. ▪ Mushroom farming & processing: Training of trainers has taken place and interested farmers have been identified.	GoL	2	▪ GoL investment not in line with goals of PS development in general. ▪ Training and identification of farmers is a facilitation process and much in line with industrial development.
Securing Access to Main Markets					
Market Access Arrangements					
Intra-SACU Trade		Duty-free access to the market of over 50 million customers with RSA being the largest market of all the SACU countries.	SACU member states	3	▪ Not fully exploited. Much can be done in servicing this market.
Qualified for AGOA		A USA decision to relax the Rule of Origin requirement for least-developed countries such as Lesotho, where such countries were granted duty-free access for goods produced from Third Country fabrics. This third country fabric provision will to expire in 2012. AGOA will expire in 2015.	USA	4	▪ The most effectively used market access to date. ▪ Only one product line (garments) was exploited. More can be exploited.
Being party to the Cotonou Agreement. (Commissioned a Rules of Origin [RoO] study for the		Lesotho is a signatory to the Cotonou Agreement which offers concessionary access to the EU market (of over 400 million customers) of a wide-range of manufactured goods from ACP	EU and ACP countries	1	▪ Restrictive RoO have rendered this access virtually valueless.

Intervention	Description of Intervention	Institution	Effectiveness Score (1 – 5)	Score Narrative
on-going EPA negotiations)	countries.			
SADC Trade Protocol	Imminent implementation of the SADC Trade Protocol offers improved access to the regional market beyond SACU.	SADC (non-SACU) member states	1	▪ Has restrictive Rules of Origin hence unlikely to be of any value.
Infrastructure Constraints				
Cabinet Sub-Committee on Industrialization	A committee composed of ministers of Finance and Development Planning, Public Works and Transport, Labour and Employment, Natural Resources, Local Government and Trade and Industry, Cooperatives and Marketing as the chairperson.	Represented ministries	4	▪ Effectively carried out mandate as numerous infrastructural bottlenecks were dealt with.
Technical Committee on Industrialization	A sub-committee of the above charged with the responsibility of addressing infrastructural problems. Composition is officials from the above-mentioned ministries plus LNDC, LEC, Telecom Lesotho, Maseru City Council, Water and Sewerage Authority, Lands, Survey and Physical Planning and National Environmental Secretariat.	Represented ministries, agencies and corporations.		

Intervention	Description of Intervention	Institution	Effectiveness Score (1 – 5)	Score Narrative
Land Reform Bill	The barriers to industrialization that the current land tenure system presents are well documented. A review was undertaken and among the recommendations was that foreigners be allowed to own land in freehold in designated areas for industrial development and for approved industrial purposes, high rise buildings for residential and commercial use and for special projects.	Ministry of Local Government	1	▪ The Bill has been in parliament for more than four years and there is no sign that its recommendations will be implemented. This may be because the bill also covers agricultural land where sensitivities are more pronounced.
Business Environment				
Legislative Review	Several legislations e.g. the Companies Act and the Immigration Acts are being reviewed in order to make them less restrictive and facilitate smooth business operations.	Relevant Ministries	3	The process is on-going with a number of reviews having been done and forwarded to parliament.
Inception of the Trade and Investment Facilitation Centre (TIFC)	Envisaged as a service point from which investors will get all the services they need from Visas, banking and licensing. The primary objective is to reduce the bureaucratic procedures that are time consuming. This is to be implemented in five phases. Currently only phase one	Currently MTICM and LRA. Other ministries and agencies to follow with implementatio	3	Though not yet fully implemented, at its current state the TIFC has gone a long way to reducing the burden of regulation that hampered the doing of business in Lesotho.

Intervention	Description of Intervention	Institution	Effectiveness Score (1 – 5)	Score Narrative
	is operational with the bringing together of the MTICM foreign trade officials and LRA Customs officials working under one roof.	n of other phases.		
Access to Credit				
Credit Risk Guarantee Scheme	LNDC, under the Private Sector Competitiveness Project, acts as a guarantor to unlock the commercial banks reluctance to lend towards the private sector. LNDC assets are used to provide the collateral for loans which private bodies are unable to supply	LNDC	1	The effectiveness of the measure will depend on how far commercial banks believe that LNDC assets will be put at risk in the event of debtor non-performance.
Repositioning the Commercial Court	Plans are underway to take the non-functioning commercial court out of the judiciary system and grant it the standing similar to that of the labour court.	MFDP		This assumes that the system of justice is at fault for failing to adjudicate rapidly in cases involving bad debt when it is more likely that lack of clarity in the laws governing transfers of property are chiefly to blame.
Establishing a Credit Bureau	So that it is possible to have the applicant's credit record, the current absence of which is exacerbating the credit access constraint.	CBL		This is an elementary tool for establishing the credit-worthiness of those seeking credit.
Labour Productivity Issues				
Technical & Vocational Education Training (TVET)	The TVET policy proposes the establishment of the Lesotho Skills			Good intent.

Intervention	Description of Intervention	Institution	Effectiveness Score (1 – 5)	Score Narrative
Policy	Agency, a National Training Fund, a TVET Learning Framework, and a TVET Quality Management System	MOET	1	
ComMark Trust/LNDC Partnership	ComMark Trust is co-financing a training institute for the garment and textiles sector.	ComMark Trust	3	Addressing the problem where it matters most – the current workforce that surveys have revealed to be less productive than in comparator countries.
Capacity Building for Textile Industry Employees	Championed by the Private Sector Development Unit under the Private Sector Competitiveness Project. Two centres – one in Maseru and the other in Maputsoe are expected to be established. Training will be co-financed by the government and the industrialists under that project.	MFDP	2	Good intent, based on the model that has worked for a country not different from Lesotho.
BEDCO/NSIC Institute	Envisaged training institute to empower indigenous entrepreneurs and capacitate the further in areas that BEDCO is currently working and perhaps beyond.	BEDCO	1	Good intent.
The ALAFA Programme	The Apparel Lesotho Alliance to Fight Aids (ALAFA) programme is aimed at mitigating the impact of HIV and AIDS on the Lesotho apparel industry.	ComMark Trust	2	Relatively new. Will mitigate the HIV/AIDS induced productivity constraints.

3.2. CONCLUSIONS

Two main conclusions may be derived from the above review of industrial policy measures:

1) The government correctly identified the main obstacles to the development of the Industrial Sector and developed a series of measures to address them. This is to the credit of the institutional structure developed for that purpose; equally it may be concluded that;

2) The institutional structure has failed to secure the implementation of these policy measures by the various government agencies concerned in a coherent and coordinated manner. This has been particularly noticeable in that area of policy concerned with increasing the participation of Basotho in the process of industrial investment and, especially, the development of the SMME sector. Here there has been uncertainty as to the functions and responsibilities of LNDC and BEDCO which brought about the failed attempt to establish an SMME network within MTICM and the more recent establishment of the Private Sector Development section within the MFDP to oversee yet another programme in this area.

This suggests that:

- The policy formulation structure centred on the IMTT should be reinforced and made more representative of all stakeholder interests;

- A special unit should be established with a mandate to monitor policy implementation across the board and supply the information and analysis the IMTT requires if it is to direct and coordinate that process.

The GoL believes that the above measures are essential if the ends of industrial policy are to be achieved.

4. POLICY IMPLEMENTATION – ADDITIONAL MEASURES IN INDUSTRIAL POLICY

Table 7 below indicates additional measures required to achieve the objectives of its Industrial Policy within the policy framework indicated in section 2 and its assessment of the effectiveness of the measures analysed in section 3. The additional measures are organised according to the categories of obstacles to the industrialisation process identified in section 1 of this paper: the particular constraint addressed is indicated together with the corresponding intervention. The table also indicates the assumptions the government has made regarding the importance of each intervention to the achievement of plan and its assessment of the likelihood of the intervention succeeding within the period of the IMP – i.e. 2007-2010. These additional measures will be included in the programme of activities of the Industrialisation Master Plan in section 5.

Table 7: Additional activities required to achieve objectives of Industrial Policy

Constraint	Intervention	Assumptions	
		Importance to achievement of plan objectives	**Likelihood of success in plan period**
INVESTMENT PROMOTION STRUCTURES/INSTITUTIONS			
Need to reinforce authority of body responsible for industry policymaking and make it more representative of all stakeholder interests.	Reinforce authority of IMTT by: 1. Extending its mandate to include responsibility for overseeing implementation of IMP 2. Strengthen membership by: • Making Ministers of Finance and Development Planning and Trade and Industry, Cooperatives and Marketing joint-chairmen; • Strengthen representation of all stakeholders in industrialisation process	**5**	**5**
Lack of an adequate mechanism to monitor implementation of industrial policy by agencies of the GoL on a coordinated basis	• Establish IMP Secretariat in Department of Industry, MTICM, to monitor plan implementation • Strengthen capacity of secretariat officers to carry out functions	**5**	**2**
Need to define responsibilities as regards industrialisation process of LNDC and BEDCO in particular as regards the involvement of the Basotho Private Sector.	Review roles of LNDC and BEDCO with respect to the industrialisation process.	**4**	**4**
INVESTMENT INCENTIVE REGIME			
Lack of clarity in investment regime	**Redraft Investment Bill to:** ▪ Define powers of Minister ▪ Put foreign and domestic investors on equal footing and define where they are not to be treated equally ▪ Require gazetting of investment incentives and the criteria for qualification	**4**	**5**

Table 7 cont'd

DIVERSIFICATION OF INDUSTRIAL SECTOR STRUCTURE			
Undesirable dependence on production of bulk garment categories for the US market where the relative comparative advantages enjoyed by Lesotho producers are likely to erode in the IMP period.	Identification of projects and support for investment promotion programmes leading to: ▪ Diversification of textile sub-sector ▪ Development of non-textile sub-sectors concentrating on areas of comparative advantage	**5**	**3**
SECURING ACCESS TO EXPORT MARKETS			
Inability of Trade Department, MTICM, to keep up with demand for policy analysis and represent Lesotho's interests adequately in international negotiations	**Strengthening capacity of Trade Department, MTICM**	**5**	**2**
Lesotho's interests not adequately reflected in common SACU negotiating positions	**Seek closer consultations with BNLS partners in developing common SACU negotiating positions**	**4**	**3**
Anticipating possible effects of 'Abundant Supply' provision of AGOA IV	**Anticipate any US attempt to restrict use of Third Country fabrics under AGOA SP using this provision by undertaking a review of the availability of denim in AGOA-beneficiary states and acceptability of this material to US garment buyers.**	**4**	**3**
INFRASTRUCTURAL CONSTRAINTS TO INDUSTRIAL DEVELOPMENT			
Inadequate supply of industrial sites with access to adequate electricity, water and waste water treatment facilities	**1. In short term consider ways of involving private capital in development of industrial locations without changing Land Act**	**5**	**3**
	2. In longer term seek change in Land Act to allow private ownership of industrial land	**5**	**1**

Table 7 cont'd

Inadequacies in supply of electricity and water to industrial sites	**Proceed with Metolong Dam project and associated water reticulation project and electrification programme**		
	Involve LEC and WASA at earlier stage in planning of industrial locations	**3**	**4**
BUREAUCRATIC OBSTACLES TO INDUSTRIAL DEVELOPMENT			
Lack of adequate business intelligence	▪ Continue on-going project to establish Policy & Regulatory Unit within MTICM ▪ Improve data-collection procedures in Customs, LRA, Bureau of Statistics	**4**	**2**
LABOUR PRODUCTIVITY ISSUES			
Low level of general technical and clerical education	**Establish Technical Education Task Force to consider various schemes and formulate single policy. This should make positive efforts to end the bias against girls in the delivery of general education which is both economically damaging and socially unjust.**	**4**	**3**
DEVELOPMENT OF SMME SECTOR			
Lack of information about structure of sector	**Detailed survey of sector along lines of that carried out under Gemini Programme in 1990**	**4**	**4**
Inability of indigenous suppliers to compete with companies based in RSA in bidding for government procurement contracts	**Giving 15 per cent preference for local suppliers in Government procurement contracts**	**2**	**3**
Lack of information which discourages building of links between large industrial enterprises and SMME suppliers of goods and services	**Initiation of Business Linkages Project to promote contracts between large industrial producers and local suppliers of goods and services**	**3**	**3**
SMMEs lack of understanding of business procedures and how to prepare Business Plans	**Improvement of business advisory service**	**4**	**3**

Table 7 cont'd

5. INDUSTRIALISATION MASTER PLAN –PLANNED INTERVENTIONS BY THE GOVERNMENT

5.1. INTRODUCTION

Table 8 below sets out the programme of activities to be undertaken under the Industrialisation Master Plan in the period 2007-10. Detailed consideration of each intervention is undertaken in Annex I below.

The activities are grouped according to the category of barrier to industrialisation into which it falls as defined in section 1.5 above and are considered under the following headings:

- The specific constraints (to the achievement of industrial policy goals) addressed;
- The intervention by the government planned;
- The ministry or other agency of the government responsible for the activity;
- Verifiable indicators for determining the success of the intervention;
- The government's assumptions as to the importance of the measure in achieving plan objectives and its expectations as to its likelihood of being successfully accomplished with in the plan period. These are based on the criteria for determining plan priorities as set out in section 2.5 above.

Table 8: Programme of Activities Planned Under Industrialisation Master Plan, 2007-10

Constraint	Intervention	Responsible agency of the government	Verifiable Indicators of Success	Assumptions	
				Importance to achievement of project objectives	Likelihood of success in plan period
INVESTMENT PROMOTION STRUCTURES/INSTITUTIONS					
Need to reinforce authority of body responsible for industry policy making and make it more representative of all stakeholder interests.	**1** Reinforce authority of IMTT by: 1. Extending its mandate to include responsibility for overseeing implementation of IMP 2. Strengthen membership by: • Making Ministers of Finance and Development Planning and Trade and Industry, Cooperatives and Marketing joint-chairmen; • Strengthen representation of all stakeholders in industrialisation process	MFDP/MTICM	• Reinforcement of the IMTT along the lines indicated; • Regular meetings of IMTT	**5**	**5**

*Explanation of assumption ratings:
Importance to achievement of IMP objectives: 1 = Moderately important only; 2 = Necessary, but not sufficient; 3 = Important; 4 = Very important; 5 = Critical
Likelihood of successful outcome in IMP period: 1 = Not likely to be achieved; 2 = Could be achieved, but difficulties expected; 3 = Could be achieved; 4 = Likely to be achieved; 5 = Expected to be achieved.

Table 8 cont'd

Lack of an adequate mechanism to monitor implementation of industrial policy by agencies of the government on a coordinated basis	**2**	• Establish IMP Secretariat in Department of Industry, MTICM, to monitor plan implementation and report regularly to IMTT • Strengthen capacity of secretariat officers to carry out functions	MTICM	Establishment of secretariat able to carry out its functions	**5**	**2**
Uncertainty as to responsibility for promotion of indigenous enterprises	**3**	Establish task force to review roles of LNDC and BEDCO in respect of the development of the Basotho Private Sector in the context of the Private Sector Competitiveness project.	MTICM/MFDP	Submission of task force report with recommendations	**4**	**4**
INVESTMENT INCENTIVE REGIME						
Lack of clarity in investment regime	**4**	**Redraft bill on Foreign Direct Investment to:** ▪ Define powers of Minister ▪ Put foreign and domestic investors on equal footing and define where they are not to be treated equally ▪ Require gazetting of investment incentives and the criteria for qualification	**MTICM**	**Enactment of Investment Law with amendments indicated**	**4**	**5**
Uncertainty as to efficacy of investment incentives	**5**	**On-going review of incentives leading to reforms**	**MFDP/MTICM**	**More effective incentives**	**4**	**4**
	6	**Consideration of zero-rating income tax on earnings from export to SACU to bring these into line with those to rest of world**	**MFDP**	**Publication of policy review**	**4**	**4**

Table 8 cont'd

DIVERSIFICATION OF INDUSTRIAL SECTOR STRUCTURE						
Undesirable dependence on production of bulk garment categories for the US market where the relative comparative advantages enjoyed by Lesotho producers are likely to erode in the IMP period.	**7**	Identification of projects and support for investment promotion programmes leading to: ▪ Diversification of textile sub-sector ▪ Development of non-textile sub-sectors concentrating on areas of comparative advantage	**MTICM**	**Development of investment projects in textile and non-textile sub-sectors**	**5**	**3**
SECURING ACCESS TO EXPORT MARKETS						
Inability of Trade Department, MTICM, to keep up with demand for policy analysis and represent Lesotho's adequately in international negotiations	**8**	**Strengthening capacity of Trade Department, MTICM**	**MTICM**	**Improved capacity of Trade Department to carry out functions**	**5**	**2**
Lesotho's interests not adequately reflected in common SACU negotiating positions	**9**	**Seek closer consultations with BNLS partners in developing common SACU negotiating positions**	**MTICM**	**Improved representation of Lesotho interests in development of common SACU negotiating positions**	**4**	**3**
Erosion of preferences in EU and US markets	**10**	**Seek relaxation of EC common preferential Rules of Origin and other S&D treatment in EU/SADC EPA negotiations.**	**MTICM**	**Significant improvements in access to EU markets**	**4**	**3**

Table 8 cont'd

Reduced competitiveness in overseas markets as a result of termination of TCIDP (DCCS)	**11**	**Persuade SACU partners to:** • Allow Lesotho to continue to issue Duty Credit Discount Certificates; and • Replace the TCIDP programme with a WTO-compatible conferring comparable benefits	**MTICM**	▪ Agreement with SACU partners to allow phasing out of TCIDP over period ▪ Replacement of programme by WTO-compatible programme	**5**	**2**
Anticipating possible effects of 'Abundant Supply' provision of AGOA IV	**12**	**Anticipate any US attempt to restrict use of Third Country fabrics under AGOA SP using this provision by undertaking a review of the availability of denim in AGOA-beneficiary states and acceptability of this material to US garment buyers.**	**MTICM**	**Review undertaken**	**4**	**3**
INFRASTRUCTURE CONSTRAINTS ON INDUSTRIAL DEVELOPMENT						
Inadequate supply of industrial premises on serviced locations	**13**	**1. In short term consider ways of involving private capital in development of industrial locations, in particular the Ha Tikoe estate, without changing Land Act**	**LNDC**	▪ Completion of Ha Tikoe estate to acceptable standards ▪ Identification of other areas for industrial development	**5**	**3**
	14	**2. In longer term seek change in Land Act to allow private development of industrial zones**	**Ministries of Law & Constitutional Affairs/Local government & Chieftainship/MFDP/MTICM**	**Private development of industrial locations in response to market.**	**5**	**1**

Table 8 cont'd

Inadequacies in supply of electricity and water to industrial sites and lack of waste water treatment facilities	**15**	**Proceed with construction of Metolong Dam and water reticulation component of that project, industrial waste water programme and expansion of electricity supply**	**WASA/LEC**	**These elements of MIP programme proceed on schedule.**	**5**	**3**
	16	**Discussions with LEC and WASA aimed at (i) securing adequate access to electricity. water and sewerage at Ha Tikoe estate; and (ii) improving supply at all locations**	**LNDC**	▪ **Reduced incidence of power outages** ▪ **Reduced dependence on borehole water** ▪ **Improved planning procedures**	**5**	**3**
BUREAUCRATIC OBSTACLES TO INDUSTRIAL DEVELOPMENT						
Unnecessary regulation and bureaucratic inefficiencies	**17**	**Continue on-going review of present legislation and its implementation**	**Concerned ministries**	**Improved ratings for Lesotho in World Bank "Doing Business" surveys**	**4**	**4**
Lack of adequate business intelligence	**18**	▪ Continue on-going project to establish Policy & Regulatory Unit within MTICM ▪ Improve data-collection procedures in Customs, LRA, Bureau of Statistics	**MTICM ; MFDP**	**Establishment of PRU and its regular use as business tool**	**3**	**3**
INDIGENOUS INVESTORS' ACCESS TO CREDIT						

Table 8 cont'd

Reluctance of banks to advance credit to Basotho investors	**19**	**Develop use of Credit Guarantee Facility backed by LNDC assets**	**LNDC**	▪ **Increased willingness of banks to lend to indigenous businesses** ▪ **Good performance record in servicing guaranteed loans**	**4**	**2**
Lack of information on creditworthiness	**20**	**Establish Credit Bureau**	**CBL**	**Establishment of credit bureau; regular reference to it**	**3**	**4**
Banks' lack of faith in legal process	**21**	▪ **Review operation of all laws affecting ability of commercial banks to foreclose on property advanced as collateral in the event of non-performance of loan terms** ▪ **High Court to issue guidelines to lower courts on trying commercial cases.**	**Ministries of Law & Constitutional Affairs and Local government & Chieftainship**	**Greater willingness of commercial banks to advance credit to indigenous businessmen**	**3**	**2**
Difficulty in using land as collateral	**22**	**Changes in Land Act to allow commercial and industrial land to be privately owned**	**Ministries of Law & Constitutional Affairs and Local government & Chieftainship**	**Private citizens able to use land as collateral for commercial credit**	**5**	**1**

Table 8 cont'd

LABOUR PRODUCTIVITY ISSUES						
Inflexibility of textile industry workforce	**23**	**Establishment of industry training facilities based on Cambodian model at Maseru and Maputsoe under Private Sector Competitiveness Project**	**MFDP**	Improved productivity of textile sub-sector workforce	**4**	**2**
Low level of general technical and clerical education	**24**	**Establish Technical Education Task Force to consider various schemes and formulate single policy**	**MTICM/MOET /BEDCO**	**Establishment of programme for general technical and clerical education**	**4**	**4**
High incidence of HIV/AIDs infection in working age population	**25**	**Continuation of textile industry ALAFA programme**	**ComMark Trust**	**Lower incidence of infection among textile industry workers**	**4**	**3**
DEVELOPMENT OF SMME SECTOR						
Lack of information about structure of sector	**26**	**Detailed survey of sector along lines of that carried out under Gemini Programme in 1990**	**MTICM**	**Execution of programme**	**4**	**4**
Inability of indigenous suppliers to compete with companies based in RSA in bidding for government procurement contracts	**27**	**Continuation of 15 per cent preference for local suppliers in government procurement contracts**	**MFDP**	**Increase in number of local suppliers succeeding in bids for procurement contracts**	**3**	**3**

Table 8 cont'd

Lack of information which discourages building of links between large industrial enterprises and SMME suppliers of goods and services	**28**	**Continuation of Business Linkages Project to promote contracts between large industrial producers and local suppliers of goods and services**	**MTICM**	▪ Meetings between the large industrial enterprises and small suppliers of goods and services to exchange information; ▪ Identification by large industrial enterprises of goods and services they might purchase locally; ▪ Changes in sourcing of goods and services by large industrial enterprises from foreign to domestic suppliers.	**3**	**3**
Lack of understanding of business procedures and how to prepare Business Plans	**29**	**Improvement of business advisory service**	**MTICM**	Increased participation by SMMEs in formal sector	**4**	**3**

5.2. PRIORITISING IMP ACTIVITIES

Table 9 overleaf lists the various activities in the IMP programme according to the priority in implementing the plan. This takes account of the importance the government attaches to each activity in achieving the policy objectives of the plan balanced by its assessment of the likelihood of a successful outcome within the plan period.

The object of combining these factors is to ensure that priority is given to activities that are not only important, but which government considers to have a reasonable expectation of a successful outcome within the plan period. However, this sometimes means that a number of activities judged very important in terms of plan objectives are given a relatively low rating because of the limited expectations of a successful outcome. It is not always desirable that such activities should be given low priority.

Where this relates to lack of capacity on the part of the government, the need to seek donor-funded technical assistance and the form this might take will be considered. This will be the subject of systematic assessment by the IMTT; the establishment of which in a strengthened form is seen as the most important activity of the plan programme. However, it seems likely that, by this criterion, technical assistance will be required in the case of activities numbers 2 (establishing the IMP Secretariat) and 7 (strengthening the negotiating capacity of the Trade Department, MTICM). Both these activities are considered critical to the achievement of plan objectives in that they are a necessary condition for the successful execution of other activities.

Table 9: IMP activities in order of priority

Intervention		Importance to IMP	Likelihood of success	Priority weighting (1-10)	Timing of intervention after start-up/Duration of activity
1	Establishing strengthened IMTT	5	5	10	Immediate/two months
4	Redrafting FDI Bill	4	5	9*	On-going/18 months
3	Roles of LNDC and BEDCO in promoting Basotho participation in industrial process	4	4	4	Immediate/3 months
5	Review of fiscal and financial incentives	4	4	8	Immediate/Plan period
6	Consideration of zero-rating earnings from SACU exports	4	4	8	Immediate/9 months. (It is intended that the outcome of the review will be announced in the Budget Statement for fiscal year 2008-9
17	Review of legislation and administrative procedures	4	4	8	On-going/Two years
24	Formulate policy on general technical education	4	4	8*	Sixth month/2 years
23	Textile industry training institutions (establishment)	4	4	8*	On-going/NA
7	Identification of investment projects	5	3	8*	Sixth month/six months

13	Innovative ways of financing infrastructure investment (especially at Ha Tikoe location)	5	3	8	Second month/2 months
15	MIP programme	5	3	8	This activity is independent of the IMP
16	Discuss provision of electricity, water and waste disposal facilities with LEC and WASA with particular reference to the Ha Tikoe industrial zone	5	3	8	Second month/2 months
26	Survey of SMME sector	4	3	8*	Twelfth month/6 months
3	Establishment of IMP Secretariat able to carry out its mandated functions	5	2	7*	Immediate/Plan Period
8	Strengthen trade negotiating capacity of MTICM	5	2	7*	Sixth month/Plan Period
11	Response to threat to end TCIDP	5	2	7	On-going/1 year
20	Establish credit bureau at CBL	3	4	7	Immediate/6 months
9	Seek closer consultations with BNLS partners in negotiating common SACU positions	4	3	7*	On-going/Plan Period
10	Seek S&D treatment in EU/SADC EPA negotiation	4	3	7*	Immediate/six months
12	AGOA ‘Abundant Supply’ provision (review of denim availability)	4	3	7*	Sixth month/3 months
25	Textile sector ALAFA programme	4	3	7	On-going/NA
29	Improve provision of Business Advisory Service for SMMEs	4	3	7	Sixth month/one year

18	Business intelligence provision	3	3	6*	On-going/1 year
28	Establish linkages between major industrial enterprises and local suppliers of goods and services	3	3	6*	On-going/1 year
27	15% preference for indigenous bids on government procurement contracts	3	3	6	On-going/NA
19	Introduce LNDC Credit Guarantee facility	4	2	6	Fiscal 2007/8 /NA
14	Implement Land Act Commission proposals in respect of land designated for industrial use	5	1	6	Immediate/2 years
22	Change Land Act to facilitate use of land as collateral	5	1	6	Immediate/2 years
21	Review laws affecting commercial contracts	3	2	5	Immediate/2 years

Source: Based on Table 8.

ANNEX I – DETAIL OF PROPOSED INTERVENTIONS

A. INVESTMENT PROMOTION STRUCTURES/INSTITUTIONS

Constraint(s) addressed

The establishment of the Interministerial Task Team on FDI together with the Cabinet Sub-Committee on Industrialisation and Industrialisation Technical Committee has gone some way towards resolving the problems of **policy formulation** in the area of industrial development and securing a degree of representation for non-government stakeholders in this process. These structures require to be strengthened to reflect the importance of industrial policy in the achievement of national economic objectives and their specific responsibility for overseeing the implementation of the IMP have to be defined.

However, there is lacking an adequate mechanism for coordinating the **implementation of policy** affecting the development of the Industrial Sector by the many ministries and other agencies of the government whose activities impinge on this in a coherent manner. This is judged to be a major factor in the apparent loss of momentum in industrial policy in recent years.

Intervention(s) planned

1. **Development of IMTT**

The government will reinforce the present structure of the IMTT structure by the following measures:

- Making the Minister of Finance and Economic Planning co-chairman of the committee together with the Minister of Trade and Industry, Cooperatives and Marketing thus bringing together the two ministries whose activities chiefly affect the development of the industrial sector. These ministers will take the chair on an alternating basis;
- Facilitating liaison between the IMTT and the Cabinet sub-committee by making the Principal Secretary, Trade, MTICM, secretary of both bodies;
- Requiring all other ministries and agencies of the government whose activities impinge on industrial development to nominate members of the IMTT. These will be at departmental director level or have particular expertise/experience of areas of policy that impinge on the industrialisation process. It is intended that the members of the present Technical Committee will become members of the IMTT. Attendance by nominated members at meetings will be obligatory save in exceptional circumstances;

- Inviting Private Sector representative bodies to nominate their CEOs as members of IMTT and urging their regular attendance at meetings;

- Inviting other non-government actors from, for instance, Academe and the NGO community to nominate high-level representatives.

The mandate of the IMTT will be extended specifically to include responsibility for: overseeing the implementation of the plan; and for preparing programmes of further activities to be undertaken after the end of the present IMP period.

The Cabinet sub-Committee on Industrialisation will be retained as a channel of communication between the strengthened IMTT and the highest level of government. The present functions of the Technical Committee will be absorbed by the IMTT.

2.1 Coordinating Secretariat to be established in Department of Industry, MTICM

A coordinating unit for the above institutions will be established in the Department of Industry, MTICM, to be known as the IMP Secretariat. The Director of Industry, MTICM, will the head of the unit and shall also nominate an officer as deputy.

The IMP Secretariat's mandate will be as follows:

- To prepare agenda as instructed by the secretary and issue invitations to meetings;

- To handle all organisational matters relating to the meetings of the committees;

- To prepare quarterly reports for the IMTT on progress with implementing the activities set out in this section within the policy guidelines as set out in section 2; further to this

- To keep minutes of meetings;

- To maintain regular contacts with all stakeholders represented on the IMTT; and

- To prepare papers on specific policy issues on an *ad hoc* basis with recommendations for consideration by IMTT. Such papers shall be prepared in on the instructions of the secretary.

2.2 Building capacity of IMP Secretariat

The capacity of the Department of Industry will be reinforced in order for it to be enabled to carry out its secretariat functions, particularly in the area of policy analysis. An economist with suitable experience will be appointed on a one-year contract to the department specifically to advise the Director on IMP matters. Training of existing officers in the Department of Industry will be carried out both on-the-job and by means of formal programmes. This process has already begun with the development of a Policy & Regulatory Analysis Unit (PRAU) within MTICM which will be a key part of the process of ensuring that the IMP Secretariat has the capacity to carry out its functions. (See also note under Intervention 18 on page 82).

Responsible ministry/other agency of the government

The change in the composition and functions of the IMTT and its relations with the Cabinet-level Industry Sub-Committee will be determined by Cabinet. The IMP Secretariat will be established and organised by MTICM.

It is envisaged that Technical Assistance will be required both to develop secretariat procedures and to identify training needs and formulate appropriate programmes.

Verifiable indicators of success of intervention

The success of the intervention will be indicated by:

- Reinforcement of the IMTT along the lines indicated;
- The establishment of the IMP Secretariat;
- The preparation of regular reports by the Secretariat on progress with planned activities for the consideration of the IMTT thus empowering the IMTT to carry out its policy coordination function;
- The institution of regular meetings of the IMTT under the alternating chairmanship of the two ministers to consider the above reports by the secretariat;
- Systematic implementation of the plan on a coordinated and coherent basis.

Assumptions

The government considers that the interventions under this head are critical to the success of the IMP insofar as little is likely to be achieved unless they are undertaken.

Likelihood of a successful outcome in the IMP period

The government expects the formal institutional changes outlined above to be achieved within the plan period.

Given the importance of the coordination to be supplied by the IMP Secretariat, much will depend on whether or not the capacity of the officers of this unit can be developed as to enable them to carry out its functions in an effective manner. The government considers that the difficulty in finding officers of appropriate qualifications and experience will make it difficult for this to be achieved within the IMP period. Even were officers of appropriate capabilities to be identified the need to secure funding will still remain.

The availability of Technical Assistance along the lines indicated would modify this latter expectation.

3. Clarifying institutional arrangements for promoting indigenous private sector

Constraints addressed

The efforts pursued since the Agro-Industrial Project of 1991 to encourage Basotho participation in the industrialisation process have constituted the most significant failure of the government's industrial policy. As noted in the contextual analysis undertaken in section 1, LNDC has had little success in promoting indigenous investment in the formal sector of the economy and, insofar as SMMEs in the informal sector do create many thousands of jobs and, thus, make a major contribution to poverty alleviation, this outcome is largely unrelated to government policy.

The inherent characteristics of Basotho SMMEs as a group – see section 1.4.2 above – indicate why attempts to involve them in the formal sector have been largely nugatory. However, government policy measures have failed to adequately address these weaknesses. The lack of clearly defined responsibility as between the LNDC and BEDCO in respect of the provision of specific measures is considered a factor in this failure. The lack of any discernible progress in the context of the MTICM's SMME Network project made it inevitable that another actor would become involved in this area in the form of the MFDP's Private Sector Development and Financial Affairs Department as administrator of the World Bank sponsored Private Sector Competitiveness project. However, it may also result in confusion worse confounded unless specific responsibilities and chains of command are clearly defined.

Intervention(s) planned

A commission will be established to examine all aspects of the roles of LNDC and BEDCO in respect of the industrialisation process as this affects efforts to promote the involvement of Basotho-owned enterprises and to make recommendations as to their future responsibilities in this regard and to which authority they should be answerable especially in the context of the Private Sector Competitiveness project.

Responsible ministry/other agency of the government

MTICM/MFDP

Verifiable indicators of success of intervention

Submission of commission report with recommendations.

Assumptions

Importance to achievement of plan objectives

This intervention is considered highly important to the success of the plan.

Likelihood of success in plan period

It is considered that the intervention objectives will be achieved in the plan period.

B INVESTMENT INCENTIVE REGIME

4. Definition of Investment Law

Constraint(s) addressed

The bill currently under consideration by MTICM is considered inadequate in that it is: (i) concerned with foreign direct investment only; (ii) it does not sufficiently define the duties of the Minister, Trade and Industry and Cooperatives and Marketing, in respect of the approval of investment projects for purposes of qualifying for available fiscal and financial incentives; (iii) does not indicate the functions of other bodies concerned with the administration of investment incentives; and (iv) it does not list the incentives that are available or the criteria by which they are given.

Intervention(s) planned

The current bill will be redrafted to:

- Define the powers of the Minister to approve investment projects;
- Set out the criteria by which he shall determine whether or not to approve projects;
- Indicate the manner in which he shall exercise his power to approve projects;
- Make it clear that in most areas national and foreign investors are treated on an equal footing; in industrial sub-sectors reserved for domestic investment only the bill will
- Define what these sub-sectors are; and, insofar as the Minister is given additional discretion to determine whether or not the right to invest in a project shall be reserved for citizens of Lesotho
- Indicate the criteria by which he shall exercise this power;
- Define the responsibilities of MTICM, LNDC and BEDCO in promoting investment to avoid all confusion of functions.

In addition, the bill will oblige the Minister to publish in the Official Gazette:

- A list of available fiscal and financial investment incentives;
- The criteria by which enterprises qualify for these incentives;
- The bodies responsible for their administration;

Details of all amendments to the list of incentives as these are determined.

Responsible ministry/other agency of the government

MTICM.

Verifiable indicators of success of intervention

The success of this intervention will be determined by the Parliamentary enactment of a bill along the lines indicated above.

Assumptions

Importance to achievement of plan objectives

This intervention is regarded as being important to the achievement of plan objectives.

Likelihood of success in plan period

It is considered likely that an amended bill will be considered by Parliament during the plan period.

5. Assessment of the effectiveness of investment incentives

Constraint(s) addressed

As indicated in section 1 above, the effectiveness of some of the present fiscal and financial investment incentives in serving the purposes for which they were introduced and, indeed, the validity of those purposes is unclear.

Intervention(s) planned

The government will continue to review on an on-going basis the effectiveness of all investment incentives according to the following criteria:

- The extent to which their availability is essential to the object of sustaining the present industrial structure and its development into a more diverse form as discussed in section 2.2.2;

- The revenue impact of the specific measures as compared to their effectiveness in generating economic activity and thus addressing the broad objectives of the industrialisation process.

Incentives that are not justified in the light of these criteria will be modified or wholly abandoned.

Greater efforts will also be made to publicise the existence of these benefits and the terms on which they are made available.

Responsible ministry/other government agency

MFDP possibly also the Macro Economic Working Group

Verifiable indicators of success

The verifiable indicators of success will be:

- Abandonment of ineffective incentives;
- Increased usage of those presently under-utilised.

Assumptions

Importance to achievement of plan objectives

This intervention is judged important in that it will facilitate the promotion of industrial investment. It is therefore, a necessary but not a sufficient condition for the achievement of plan objectives.

Likelihood of success within plan period

It is considered likely that the expected effects of this intervention will manifest themselves within the plan period.

6. Consideration of the Zero-rating of Company Income tax on earnings from exports within SACU region

Constraint(s) addressed

The imposition of a 10 per cent tax on company earnings derived from exports within the SACU region whereas exports to the Rest of the World are zero-rated creates a differential which could have the following undesirable effects:

- It acts as a disincentive to trade with the SACU region whereas industrial policy seeks to promote such trade as a useful means of encouraging the diversification of the present Industrial Sector – see section 2.3.3.4 above;
- It encourages exporters to falsify the destinations indicated on their export declarations which is a cause of revenue loss and reduces the value of Lesotho trade statistics as an analytical tool and creates the need for costly and intrusive countermeasures to prevent such practices.

Intervention planned

The government will consider whether the benefits of zero-rating company earnings from exports to the SACU region in terms of increased economic activity is likely to outweigh the impact of such a measure in terms of reduced revenue yield. If this proves to be desirable the tax will be reduced to zero to bring it into line with that on earnings from exports to the Rest of the World.

Responsible ministry/other government agency

MFDP.

Verifiable indicators of success

The success of this intervention will be indicated by the publication of a government policy document setting out the results of the MFDP study of this issue and its decision on whether or not to institute the proposed reform.

Assumptions

Importance to achievement of plan objectives

This intervention is considered important to the achievement of plan objectives in that it will either:

- Facilitate the process of developing export outlets in the SACU region and reduce the perceived adverse consequences of the present differential in the tax-levels imposed on exports to this region and the Rest of the World; or

- Demonstrate that such a measure is unnecessary or even undesirable.

Likelihood of success within plan period

It is expected that this exercise will be undertaken and successfully concluded within the plan period.

Timing of intervention

The decision on whether or not to introduce this measure will be announced in the Budget Statement for fiscal year 2007/8.

C THE NEED TO DIVERSIFY THE PRESENT STRUCTURE OF THE INDUSTRIAL SECTOR

Constraint(s) addressed

A grave weakness of the present structure of the Manufacturing sub-sector of the Lesotho economy (in this paper commonly referred to as the Industrial Sector) is its reliance on sales of two broad product categories (top-weight and bottom-weight bulk clothing items) to one market (the USA)..

<u>Intervention(s) planned</u>

General considerations

The review of government Industrial Policy (section 2) suggests that diversification of the Industrial Sector will be most readily achieved by developing the present **textile sub-sector**. The comparative advantage enjoyed by Lesotho by virtue of its relatively low-wage labour force, the nature of the international market for textile products (although, as discussed elsewhere, this is rapidly changing) and its established reputation as a location for textile product manufacture combine to support this assumption.

However, diversification will also be actively pursued in **non-textile** areas of manufacturing activity. There has already been some success in attracting investment in such projects.

7. Measures

Textile sub-sector diversification

Interventions to this end will include consideration of the commercial feasibility of investment projects in the following area to determine whether government should support their promotion:

- A knitwear mill for the production of knit-to-shape garment items. It is envisaged that this would be oriented to the US market and would make possible an extension of the range of products presently shipped to that country. It would also be oriented to the EU market. (Because this category of mill produces garments from yarn-forward a change it would not need to rely on the operation of the AGOA Special Provision for its output to gain preference in the US market. Similarly, it would not need the present EC Cotonou Rules of Origin to be changed for that output to gain preferential access to the EU markets). Such a mill could also produce for the regional market, but it is more likely that this would require a separate facility dedicated to SSA outlets because those investors acquainted with the US and EU markets are not acquainted with the RSA and other regional markets and *vice versa*;

- A knitted fabric mill to produce fabrics for the manufacture of higher value garments. It is envisaged that this mill would be oriented to national and regional garment producers servicing the regional market. However, it could also service the demand for knitted fabrics for the production of top-weight items for the US and EU markets. Clothing manufactured from its output would meet the present AGOA and Cotonou Rules of Origin;

- A finishing mill for the processing of short runs of higher value woven fabrics from imported grey cloth required with very short delivery periods. It is envisaged that this would be oriented to regional producers of higher value garments for regional markets;

- Mills for the production of higher value clothing for regional markets required in short runs with short delivery times. Regional demand for such clothing cannot easily be supplied by East or South Asian suppliers because of the lengthy delivery periods necessitated by their geographic remoteness from the market.

MTICM will discuss the commercial feasibility of projects falling into these categories with industry sources and ComMark. Where appropriate it will then assist in the identification of possible investors and part-finance the development of promotional activities.

Investment projects other than in the textile sub-sector

The most promising areas for government interventions to this end are considered to be the promotion of the following categories of projects:

- Labour-intensive operations involving the assembly of imported component items which take advantage of the relatively low levels of wages in Lesotho. (Particular opportunities appear to exist in the area of electrical/ electronic goods where, in fact, projects have already materialised);

- Increasing the export value of local agricultural and mineral raw materials by processing them in-country prior to shipment. (The development of block production based on the use of local sandstone affords a number of examples of projects successfully developed in this general area). Areas that will be considered under this head might include the bottling of water, and the tanning and further processing of leather where feasibility studies as to commercial viability have already been carried out under MTICM auspices. However, as indicated in the discussion of Industrial Policy in section 2, the decision to give government support to the promotion of such projects will be based upon a strict assessment of their commercial viability. The mere fact that materials are produced in Lesotho will not be considered a sufficient reason for promoting projects to beneficiate those materials in-country.

- In addition to projects in the above areas consideration will be given to the feasibility of producing generic medicines and ‘findings’ for the textile and garment industries (i.e. buttons, zips etc.)

As in the case of the textile sub-sector projects presented above consideration will be given to whether the use of public funds to promote developments in these areas can be justified by commercial criteria and the form such promotion might take.

In line with overall industrial policy as set out in section 2, in no circumstances will the government countenance the use of public funds to purchase equity-holdings in particular projects.

Responsible ministry/other agency of the government

MTICM and LNDC

Verifiable indicators of effectiveness of intervention(s)

These will include:

- Identification of possible projects for promotion on the basis of feasibility studies;
- Identification of possible investors;
- Development of appropriate promotion projects;
- Expressions of interest by potential investors;
- Applications for licensing/registration of new investment projects.

Assumptions

Importance to achievement of IMP objectives

Diversification of the present structure of the Industrial Sector is considered very important (if not critical) to the achievement of IMP objectives. Therefore, it is considered generally very important that the government should encourage reviews of the feasibility of manufacturing projects outside those areas where they are presently concentrated (i.e. the manufacture of bulk garment items for the US market) and facilitate their promotion in those instances where they are judged to be commercial.

Likelihood of successful outcome in project period

Assessments of the likelihood of successful outcomes to the above effort in the plan period are as follows:

- Knitwear mill: It is considered unlikely that such a mill will be established in the IMP period because of uncertainties about the main markets for its output in the USA and the EU and because of constraints imposed by the shortage of sites with adequate water supplies and waste water treatment facilities. A mill oriented to the South African and other regional markets might be more successful in attracting investment. However, here again, infrastructural constraints are likely to discourage the development of such a facility.

- Knitted fabric mill: The assumptions governing the government intervention in this area are the same as those pertaining to the knitwear mill;

- Woven fabric finishing mill: It is considered unlikely that such a project will be identified as feasible given that these mills are highly capital-intensive and demand a level of sophistication and willingness to adopt flexible working practices in the workforce unlikely to be achieved in Lesotho within the plan period. Again, infrastructural constraints are considered likely to discourage interest;

- High value garment production facilities: The establishment of at least one such unit during the project period is considered not impossible because of the interest already shown by South African investors. However, as in the case of the other textile projects considered, shortage of suitable infrastructure may discourage investment interest;

Investment projects in other than textile sub-sectors: It is anticipated that such projects are most likely to be oriented to the South African and other regional markets. Investors are also most likely to be found in the RSA and be motivated by their desire to benefit from Lesotho's relatively low-cost labour and generous incentive regime.

The government is sanguine that additional projects in this area will be identified in the plan period, but most likely in the two main areas where Lesotho enjoys a relative comparative advantage – i.e. labour-intensive assembly operations and in-country processing of agricultural and mineral projects. However, as in the case of the textile projects, infrastructure may be a constraining factor.

D SECURING ACCESS TO EXPORT MARKETS

8. Inadequate capacity of Department of Trade, MTICM

Constraint(s) addressed

A major constraint in securing adequate access to export markets for suppliers of Lesotho products is the inadequate capacity of the Department of Trade, MTICM, to carry out policy analysis, make recommendations on negotiating positions and represent the views of the government in international negotiations.

Intervention planned

The capacity of the Department of Trade will be strengthened by the recruitment of additional officers with experience in the area of economics and trade law. A programme of training for the officers will be formulated and instituted. It is envisaged that much of the training will be delivered 'on-the-job' reflecting the pressures placed upon the department by the plethora of negotiating processes in which it is engaged and the consequent difficulty of releasing officers for programmes of formal instruction. However, the organisation of some short courses in special subjects is likely to prove necessary and will be provided for.

The government envisages that Technical Assistance will be required to assist the department in recruiting suitable new officers and in developing training programmes including the organisation of 'on-the-job' training.

Responsible ministry/other agency of government

MTICM.

Assumptions

Importance to achievement of IMP objectives

This intervention is considered highly important to the achievement of IMP objectives.

Likelihood of success in period 2007-10

The likelihood of any significant improvement in the capacity of the Trade Department being achieved in the plan period is assessed as no higher than possible. This reflects largely the expected difficulties in recruiting additional policy analysts of a suitable quality given the demand for such persons not only in the Lesotho Private Sector, but also in the RSA. Even were suitable candidates to be recruited, much will depend on whether Technical Assistance in training the department's officers is forthcoming.

9. Difficulty in securing proper representation of Lesotho interests in negotiations carried out jointly with SACU partners

Constraint(s) addressed

In negotiating international trade agreements Lesotho normally acts together with its SACU partners (as in the EU/SADC Economic Partnership Arrangement) requiring the development of common SACU negotiating positions on policy issues. It is usually difficult for the government to ensure that the particular interests of Lesotho are adequately represented in this process and the development of SACU positions. This reflects for the most part the overwhelming economic strength of the RSA vis-à-vis its BNLS partners, although the inadequate negotiating capacity of the Trade Department discussed in relation to Intervention No. 8 on page 82 above is also a contributory factor.

Intervention planned

The government will seek to formalise procedures for consulting with its BNLS partners prior to the discussion of common SACU positions on the issues under negotiation with the RSA. On each occasion the government will:

- Circulate its own position papers to its BNLS partners; and
- Seek meetings in good time to develop a common position prior to the discussion of common SACU positions.

It will also encourage its BNLS partners to proceed in similar fashion in respect of their own position papers.

Responsible ministry/other agency of government

MTICM.

Verifiable indicators of success

The success of this intervention will be judged by the extent to which SACU negotiating positions adequately reflect BNLS interests.

Assumptions

Importance to achievement of plan objectives

This intervention is deemed important to the achievement of plan objectives.

Likelihood of success in plan period

This intervention could succeed if Technical Assistance to meet the cost BNLS meetings is forthcoming.

10. Erosion of preferences enjoyed by Lesotho in its main markets

Constraint(s) addressed

The removal from 2008 onwards of quantitative restrictions on imports of textile products from PR China and the reduction of MFN tariffs on all imports from Most-Favoured Nation (MFN) sources by the European Commission and the government of the USA will erode appreciably the value of Lesotho's present preferential access to the EU and US markets. These developments will not only affect its present shipments of clothing to the USA, but make it less likely that it will be able to revive sales of such items in the EU. More generally it will become increasingly difficult for Lesotho suppliers of any industrial goods to or find outlets for the higher-value products of projected investment projects in the area of knitwear and clothing produced from knitted fabric see section **Error! Reference source not found.**).

Intervention planned

The government will address this constraint by seeking Special & Differential treatment in the negotiation of preferential trade arrangements which may be granted LDC partners under the WTO non-agricultural market access programme.

In particular to this end it will continue its present efforts to secure relaxation of the EU common preferential rules of origin in the EU/SADC EPA negotiations, especially for textile products. However, it recognises that the value to Lesotho exporters of any concession by the EC in this area will depreciate as the EU reduces its MFN tariffs from 2008 onwards. Therefore, the government will also use the EPA negotiations to seek Trade-Related Assistance (TRA) from the EC in developing meaningful programmes for promoting investment in Lesotho by European entrepreneurs and for marketing Lesotho products in the EU as enjoined on advanced industrial economies entering into PTAs with LDCs by the WTO.

It is recognised that very little can be done to address the erosion of preferences in the US market which poses an even more significant threat to the present industrial structure than that likely to occur in the EU market given the overwhelming importance of export sales to the USA in sustaining manufacturing activity in Lesotho. This reflects the failure to progress the SACU/US FTA negotiation which is expected to remain moribund during the lifetime of the AGOA SP – i.e. until after 2012. However, as indicated below, the government will seek to mitigate threats to Lesotho's position in the US market, specifically by resisting the termination of the TCIDP by its SACU partners and possible restrictions on the use of the AGOA SP by the government of the USA.

Responsible ministry/other agency of government

MTICM.

Verifiable indicators of success

The securing of Special & Differential treatment for Lesotho in the EU/SADC EPA negotiations which leads to a meaningful improvement in its position as a supplier of EU markets.

Assumptions

Importance to achievement of plan objectives

Success in this area is considered moderately important to the achievement of plan objectives.

Likelihood of success in plan period

It is possible that some progress will be made under this head during the plan period in respect of programmes to assist Lesotho's development as a supplier of industrial products to EU markets. However, it is considered unlikely that the EC will agree to any meaningful relaxation of its textile rules of origin.

11. Countering the effects of the termination of the Textile and Clothing Industrial Development Programme (TCIDP)

Constraints to be addressed

The expected decision by the SACU partners to end the TCIDP (formerly the DCCS) threatens fatally to undermine Lesotho garment suppliers' ability to compete in international markets.

Intervention

The government will seek to persuade its SACU partners to allow it to continue to issue duty credits under the TCIDP and to permit the sale of these credits to regional clothing distributors until the programme can be replaced by a WTO-compatible programme offering comparable benefits. To this end it will consider the proposals put forward in the Justin Barnes Report[10] and whether these might be adopted as government policy.

Responsible ministry/or other government agency

MTICM.

Verifiable indicators of success

Indicators of success will be the willingness of the SACU partners to:

- Prolong the life of the TCIDP for a reasonable period to enable Lesotho suppliers to adjust to its termination;
- Agree the replacement of the programme by one judged WTO-compatible and offering comparable benefits to Lesotho textile product exporters.

Assumptions

Importance to achievement of IMP objectives

This intervention is judged to be highly important to the achievement of plan objectives.

Likelihood of success in plan period

The opposition of South African textile producers to the continuation of the TCIDP is considered likely to make it very difficult for the government to succeed in this intervention.

12. Possible restrictions on preferential access under AGOA for goods manufactured using Third Country denim

Constraint addressed

Restrictions imposed under the 'Abundant Supply' provision of AGOA IV (2006) could prevent or severely limit the use of denim from Third Country sources in the manufacture of goods that presently enjoy preferential access to the US market under the act. This would pose a significant threat to the present structure of the Lesotho Industrial Sector given its reliance on the production of denim goods for the US market and the importance attaching to its ability to use fabric from Third Country sources in the manufacture of goods that qualify for the AGOA preference.

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[10] See: "Replacing the Southern African Customs Union's Duty Credit Certificate Scheme with a WTO-compliant Development Programme for the Region's Clothing and Textile Industries": Prepared for the: Botswana Exporters' Association; Clothing Trade Council of South Africa; Clothing Export Council of South Africa; Lesotho Textile Exporters Association, Textile Federation of South Africa; South African Textile Industry Export Council; and Swaziland Textile Exporters' Association by Dr. Justin Barnes, Benchmarking & Manufacturing Analysts: February, 2007.

Intervention(s) planned

The government will review the likely availability of denim from Sub-Saharan African (SSA) sources in the plan period and also the readiness of US garment buyers to accept garments made from material sourced in that region. Should the US government consider the imposition of restrictions the government will lobby against it in concert with its BNLS partners using the findings of the study to support its representations.

Responsible ministry/or other government agency

MTICM.

Verifiable indicators of success

Verifiable indicators of success will include:

- The successful execution of a study along the lines indicated; Should the US government seek to impose restrictions

- A successful lobby against such restrictions should these be sought by the USTR undertaken in concert with BNLS partners.

Assumptions

Importance to achievement of IMP objectives

The intervention is considered important in the achievement of plan objectives.

Likelihood of success in planned period

It is expected that a study along the lines indicated will be undertaken. However, should the US government seek to impose restrictions on the use of Third Country denim fabric under the AGOA SP, it is uncertain whether it will be dissuaded by BNLS representations because such restrictions are regarded as being in their interest by regional denim fabric producers. This will almost certainly undermine the effect of official BNLS representations against such measures.

E INFRASTRUCTURE CONSTRAINTS

13-14. Development of locations for siting industrial development projects

Constraint(s) addressed

As it is virtually impossible for private sector investors to develop land for industrial usage industrial development in Lesotho has been predicated on the ability of the government to provide industrial locations with adequate access to utilities and, usually, factory shells. (The nature of the textile industry which supports the great bulk of the country's manufacturing activity means that it is more than usually important that the industrial locations provided should have effective waste water treatment facilities, in addition to access to water and electricity, but the provision for this is rarely adequate and has been largely neglected at the industrial estate presently under development at Ha Tikoe). It is highly likely that the recent failures of the government to provide an adequate supply of industrial locations have deterred potential investors from coming to Lesotho.

Intervention(s) planned

The inadequate supply of serviced locations is attributed by the LNDC (the agency responsible for this function of the government) to financial constraints. Consideration will therefore be given to innovative ways by the Ha Tikoe development might be financed – in particular by exploring ways in which private capital might be used for this purpose without contravening the present restrictions on private ownership of land. Other possible obstacles to the more rapid provision of serviced industrial sites will also be reviewed.

The government considers that the best resolution to this problem will be a change in the Land Act to make it possible for land designated for industrial usage to be sold into private ownership either on a freehold or long leasehold basis with incontrovertible titles passing to the owner. This would make it possible to attract private capital (including FDI) into the development of industrial locations. Ways in which this might be done without affecting the present system of agricultural land tenure will be considered as part of the review of the proposals of the Commission on the Land Act to be undertaken with a view to facilitating the use of land as collateral for credit .

Responsible ministry/other agency of the government

LNDC.

Verifiable indicators of success of intervention

The success of the intervention will be indicated by the completion of the Ha Tikoe estate with adequate power, water and sewerage access and factory shells and the rapid identification and development of industrial sites at other locations.

Longer term success of the intervention will be indicated by the adoption of proposals of the Land Act Commission which would make it possible for private capital – including FDI – to provide industrial premises in response to market requirements.

Assumptions

Importance to achievement of plan objectives

The provision of properly serviced locations for industrial investment projects is critical to the achievement of plan objectives.

Likelihood of success in plan period

It is considered possible to ensure that the Ha Tikoe estate can be completed during the plan period. However, a longer-term resolution of the problem of ensuring an adequate supply of industrial locations will require a change in the Land Act which is not expected to occur during this time.

15-16. Availability of electric power, water and waste water treatment

Constraint(s) addressed

The inadequacies in the supply of electricity and water discussed in section**Error! Reference source not found.** above undermine Lesotho's attractions as a location for industrial investment.

Intervention(s) proposed

Minimum Infrastructure Programme (MIP)

Inadequacies in the supply of water, waste water treatment and electricity will be addressed by the Minimum Infrastructure Programme (MIP) which will during the plan period, *inter alia*:

- Begin the construction of the Metolong Dam and the associated water reticulation component;
- Initiate a Waste Water project to deal with liquid waste from industry;
- Expand the supply of electricity.

Short term solutions

LNDC will discuss with the LEC and the WASA to consider ways in which adequate supplies of electricity, water and waste water treatment facilities the existing industrial zones and the Ha Tikoe development can be provided as a matter of urgency. LNDC will seek to involve LEC and WASA more fully in the detailed planning of new industrial zones to ensure that adequate provision for access to utilities is built in to the development process.

Responsible ministry/other agency of the government

LEC/WASA/LNDC

Verifiable indicators of success of intervention

The government is aware that the benefits of the MIP will not be fully realised during the plan period. The measure of success of this intervention will, therefore, be whether the programme proceeds according to schedule.

The success of the intervention will also be judged by:

- Reductions in the incidence of power outages in existing industrial zones;
- Reduced dependence on borehole water as a result of improvements in the public supply;
- Changes in planning procedures to take more thorough account of the likely demand for utilities in the development of new estates.

Assumptions

Importance to achievement of plan objectives

The MIP programme and finding short term solutions to the problems of inadequate supply of utilities at existing industrial locations are both is considered critical to the achievement of plan objectives.

Likelihood of success in plan period

Improvements in the supply of utilities to industrial users are expected within the plan period. Should this be necessary the government will authorise a strategic decision to down-grade the rate of provision of services to residential and commercial areas in favour of speeding up the supply to existing industrial zones and the Ha Tikoe development in particular.

The MIP programme is expected to proceed on schedule, during the plan period.

F BUSINESS ENVIRONMENT ISSUES

17. Business regulation

Constraint(s) addressed

Even in the SSA context Lesotho is in too many areas considered as a place in which it is difficult to do business not only because of the plethora of regulatory measures that affect this, but also because of the inefficiency with which the regime is administered. This particularly affects the development of local business as the cumbersome regulations effectively become barriers to entry.

Intervention(s) planned

The government will continue the review of legislation affecting investment which is already on-going with a view to identifying and removing unnecessary bureaucratic obstacles to investment. Of particular concern will be Companies Act, the Investment Bill (see also the discussion under Intervention No. 4 on page 66 above) and the Immigration Acts. In addition, it will continue to seek improvements in the efficiency with which necessary regulations are administered. As part of this effort it will continue the process of bringing together all agencies administering regulations that impinge on the investment process together under one roof by completing all four phases of the TIFC.

Responsible ministry/other agency of the government

All concerned ministries.

Verifiable indicators of success of intervention

The verifiable indicator of success in this intervention will be:

- The completion of all phases of the TIFC project;
- Improvements in border crossing Customs and Immigration facilities;
- A marked improvement in Lesotho's ratings in the World Bank sponsored 'Doing Business' surveys.

Assumptions

Importance to achievement of plan objectives

This intervention is considered important to the achievement of plan objectives. It is recognised that ease of doing business is not a critical factor in investment decision making, but can be significant in the absence of marked comparative advantages in other areas.

Likelihood of success in plan period

It is considered that some improvement in Lesotho's international rating in this respect can be achieved in the plan period.

18. Availability of business intelligence

Constraint(s) addressed

The process of industrialisation is hampered by the inadequacy of statistical and other information and the poor quality of much of the data that is collected on a regular basis. This situation affects both potential investors and those responsible for formulating and implementing government policy.

Intervention(s) planned

The government will continue the process of establishing a Policy & Regulatory Analysis Unit within MTICM for which Technical Assistance has been made available by DFID under the Priority Support Programme (PSP). It is intended that not only will this project bring information together in one place, thus facilitating its access and analysis, but that it will also make possible improvements in the quality of official data.

Responsible ministry/other agency of the government

MTICM.

Verifiable indicators of success of intervention

The establishment of a functioning Policy & Regulatory Analysis Unit (PRAU) within MTICM accessible to businessmen and policy analysts concerned with the industrialisation process.

Assumptions

Importance to achievement of plan objectives

This intervention is judged important to the achievement of plan objectives.

Likelihood of success in plan period

It is expected that the PRAU will be established within the plan period. However, its effectiveness as a source of intelligence for policy analysis and taking business decision will depend upon effective reformation in ways in which economic data are collected, collated and processed by agencies with primary responsibility for this process – in particular Customs, the LRA and the Bureau of Statistics. Some improvement is anticipated in this area, but the process is not expected to be completed within the plan period.

G ACCESS TO CREDIT

19. Credit Risk Guarantee Scheme

Constraint(s) addressed

The difficulties experienced by indigenous investors in accessing credit is a major obstacle to the achievement of greater Basotho participation in the process of industrialisation The government considers such participation desirable on grounds both of efficiency and equity.

Intervention(s) planned

Easier access to credit by Basotho entrepreneurs will be sought by use of the Credit Risk Guarantee Scheme under the World Bank-funded Private Sector Competitiveness Project. Under the scheme the LNDC will offer the banks guarantees backed by corporation assets to underwrite loans made to businesses unable to supply adequate collateral of their own for that purpose. The operation of the scheme will be confined to the provision of working capital to established businesses to finance business that has been already secured and will not be used to guarantee loans to fund new investment.

Responsible ministry/other agency of the government

LNDC

Verifiable indicators of success of intervention

The success of the intervention will be indicated by:

- Greater willingness by the commercial banks to advance credit to indigenous businessmen who cannot borrow on normal commercial terms because of lack of collateral; and

- A good performance record for the servicing of loans guaranteed under the scheme.

Assumptions

Importance to achievement of plan objectives

The government considers that this intervention is very important to the achievement of plan objectives.

Likelihood of success in plan period

The guarantee facility will be introduced during the plan period. However, the success of the measure will depend on acceptance by the commercial banks that LNDC will honour the guarantees that it gives even where this involves loss of corporation assets.

20. Establishment of Credit Bureau

Constraint(s) addressed

The government understands that the lack of reliable information on the credit records of those seeking loans may be one factor in the reluctance of banks to advance credit to indigenous businessmen.

Intervention(s) planned

The CBL will proceed with its plan to establish a credit bureau in concert with the commercial banks.

Responsible ministry/other agency of the government

CBL.

Verifiable indicators of success of intervention

The verifiable indicator of the success of this intervention will be the establishment of the credit bureau and systematic reference to it by the commercial banks as one means by which they determine whether or not to advance credit to Basotho entrepreneurs.

Assumptions

Importance to achievement of plan objectives

This intervention is considered of moderate importance in facilitating the rationalisation of bank lending policies and, therefore, their readiness to give more sympathetic consideration to requests for credit by Basotho. It will also be of service to the LNDC in determining whether or not to use the credit risk guarantee scheme to underwrite loans made by commercial banks.

Likelihood of success in the plan period

The government expects the bureau to be established within the plan period.

21. Improvements in the administration of justice in commercial cases

Constraint(s) addressed

The government is aware that a major factor in the reluctance of the commercial banks to advance credit to indigenous investors even where collateral is available is their uncertainty as to the ability or willingness of the justice system to enforce contractual obligations when debtors fail to service their loans. This appears to be based on a history of the courts failing to adjudicate in such cases in a timely manner.

This failure is understood in large measure to reflect lack of clarity in the laws which affect the banks' ability to foreclose on property advanced as collateral in cases where loans are not serviced. This situation has encouraged suspicions of judicial impartiality which, whether or not it is justified, fuels the unwillingness of the banks to advance loans to indigenous businessmen. The decision to establish what amounts to a commercial court by instructing one judge to hear only commercial cases appears not to have affected this situation. Since the judge in question was given this responsibility his court is understood to have heard no cases.

Intervention(s) planned

The government will review the operation of all laws affecting the ability of commercial banks to foreclose on property advanced as collateral in the event that loans are not serviced and make necessary changes. The judge assigned to hear commercial cases will be given greater powers to set guidelines for the operation of lower courts in such cases.

The possibility of establishing a stand-alone Commercial Court on the pattern of the Labour Court will be further considered.

Responsible ministry/other agency of the government

Ministries of Law & Constitutional Affairs/Local government & Chieftainship/CBL

Verifiable indicators of success of intervention

The success of this intervention will be measured against evidence of increased willingness of the banks to advance credit to indigenous businessmen indicating greater confidence in the justice system.

Assumptions

Importance to achievement of plan objectives

Reforms in the laws which affect the ability of the commercial banks to foreclose on debtors' property in the event that loans are not serviced are considered desirable and will be pursued. However, this will not in itself address the present reluctance of the commercial banks to advance loans to Basotho entrepreneurs which arise chiefly from the difficulties the latter experience in using real estate as collateral for loans which is a direct effect of the present Land Act.

Likelihood of success in plan period

Given the complexity of the issues involved it is not expected that significant improvements will be achieved in the plan period.

22. Modification of the Land Act

Constraint(s) addressed

The government considers that the provisions of the Land Act which render highly uncertain the process of transferring landed property between individuals is the main reason why Basotho businessmen experience such difficulty in accessing credit from the commercial banks. Their situation would be radically transformed were it possible for them to offer houses or commercial premises as collateral for loans – although, as noted in the previous section, it would still be important for the banks to have confidence that the courts would enforce judgements in their favour in the event of the loans not being serviced.

Intervention(s) planned

The government will consider again recommendations of the Commission on the Land Act to see what scope there is for modifications in the present law to allow private citizens to secure good titles in land used for housing or commercial/industrial development which they can then use as collateral for loans. As concerns about the status of land used for agricultural purposes seem to be the main political obstacle to a general change in the Land Act as recommended by the commission, as far as possible this will be excluded from the effects of any change.

Responsible ministry/other agency of the government

Ministries of Law and Constitutional Affairs/Local government & Chieftainship.

Verifiable indicators of success of intervention

The success of this intervention will be indicated by a change in the law which makes it possible for private citizens to use land in their effective occupation as collateral for commercial loans.

Assumptions

Importance to achievement of plan objectives

This intervention is considered very important to the achievement of plan objectives. Not only will its success facilitate Basotho access to credit, but it will open up the possibility of the use of private capital (including that supplied by foreign investors) for the development of industrial infrastructure.

Likelihood of success in plan period

It is considered possible that reforms along the lines indicated will be secured within the plan period, but the government is well aware of the extent of public concern in this matter and will not seek to advance more rapidly than the country as a whole is prepared to accept.

H LABOUR PRODUCTIVITY ISSUES

23. Textile Industry training

Constraint(s) addressed

The ability of the textile sub-sector to diversify its operations away from its present over-reliance on the production of bulk commodity-type clothing for the US market towards the servicing of higher value areas of the clothing market is presently constrained by the inflexibility of its work force. Workers are for the most part trained to undertake a limited number of operations within the manufacturing process. This is appropriate to the needs of the present limited product range, but means that their productivity tends to drop when they are called upon to provide the different inputs as becomes inevitable when production is oriented towards the upper ends of the market where the product changes frequently, production runs are short and delivery schedules very tight.

In addition the industry has largely failed to train Basotho to work at supervisor or junior management levels even though it is generally recognised that this is more economic than using foreigners in these positions as well as being more socially acceptable.

Intervention(s) planned

Under the World Bank-funded Private Sector Competitiveness Project the government will co-finance with the textile industry the establishment of a training institute for the industry on the Cambodian model with facilities at Maseru and Maputsoe. The institute will offer technical training designed to produce a more productive and flexible workforce able to take a wider variety of tasks and also courses for supervisors and junior management to address the present lack of Basotho able to undertake these roles. The training offered will be largely determined by industry needs.

Responsible ministry/other agency of the government

MFDP

Verifiable indicators of success of intervention

Verifiable indicators of success will include:

- The establishment of the planned facilities;
- The development of an appropriate training curriculum;
- The delivery of training to a significant proportion of the industry workforce;
- The appointment of Basotho personnel to supervisor and junior management positions in significant numbers;
- Improvements in workforce productivity, especially where this is required to make possible the development of a significantly more varied product range.

Assumptions

Importance to achievement of plan objectives

This intervention is judged very important to the achievement of plan objectives.

Likelihood of success in plan period

It is judged that the benefits of the measure are likely to begin to appear within the plan period.

24. General technical education

Constraint(s) addressed

The development of industrial activity outside the textile sub-sector is generally hampered by the lack of a work force with basic technical and clerical skills or indeed any exposure to the necessary disciplines of industrial production. Various schemes have been mooted for addressing this deficiency such as MOET's Technical & Vocational Education Training Policy and the BEDCO proposals that would deal with different aspects of the same problem. There is need for a coherent national policy in this area, properly funded and coordinated by a single agency.

Intervention(s) planned

The government will establish a Technical Education Task Force to consider the following matters:

- National needs in the area of education in technical and clerical skills;
- How such education is to be provided throughout the country;
- How it is to be funded;
- Whether participation is to be compulsory or voluntary; and
- How it will best be organised and coordinated and by which body;
- The need for Technical Assistance.

Given the importance of women in the workforce – particularly in the textile and garment industries – the present disparity between girls and boys revealed by the figures for drop-outs after primary school is not only socially unjust, but is also economically damaging. Any scheme will produced by the Task Force will seek to address this disparity and its consequences.

The Task Force will be required as far as possible to base their proposals on existing schemes and institutions.

Responsible ministry/other agency of government

MTICM, MOET and BEDCO.

Verifiable indicators of success of intervention

The success of the intervention will be indicated by the establishment of institutions for education in appropriate technical and clerical skills at a national level.

Assumptions

Importance to achievement of plan objectives

The intervention is considered very important to the achievement of the objectives of the plan although government appreciates that the economic benefits of the measure will only be secured over a longer time-frame.

Likelihood of success in plan period

The government considers that while it may be possible to develop proposals along the lines indicated within the plan period other demands on government financial resources and scarcity of trained personnel are likely to make it difficult to achieve success in the plan period.

25. HIV/AIDS

Constraint(s) addressed

The high incidence of HIV/AIDS infections poses a major threat to Lesotho as a viable location for industrial investment especially as the part of the population most at risk is that from which the industrial workforce is recruited.

Intervention(s) planned

Although this poses wider problems of public health which will be addressed by the Know Your Status (KYS) programme and the provision of retro-viral drugs, the government considers that this crisis cannot be ignored in the context of industrialization policy. It will, therefore, continue to support the Apparel Lesotho Alliance to Fight Aids (ALAFA) programme as a useful means of addressing the problem within the textile industry (which presently employs by far the greatest proportion of the industrial workforce) and any lessons to be learned will be considered for more general application within the Industrial Sector.

Responsible ministry/other agency of the government

ComMark Trust.

Verifiable indicators of success

The success of the intervention will be indicated by a lowering of the incidence of infection among textile industry employees.

Assumptions

Importance to achievement of plan objectives

The intervention is considered important to the achievement of plan objectives.

Likelihood of success within the plan period

Improvements in the incidence of infection among textile industry employees are possible within the period of the plan.

I DEVELOPMENT OF SMME SECTOR

General

Some of the constraints that presently hold back the development of the SMME sector will be addressed by other measures indicated in this plan such as those relating to indigenous investors' access to credit and programmes for technical and clerical skills training. Furthermore, the matter is addressed comprehensively in the context of the government's White paper on SMMEs. However, a number of measures are planned specifically concerned to encourage greater participation by SMMEs in the industrialisation process either by undertaking manufacturing activities on their own account or by expanding the services that such enterprises currently supply the large manufacturing enterprises.

The government's policy with regard to the SMME sector is set out in the 'SME White Paper'. The interventions proposed below are intended to complement the implementation of the measures proposed in that document.

26. Review of SMME sector

Constraint(s) addressed

The development of coherent government policies for the promotion of industrial activity by SMMEs is hampered by lack of information on the composition of the sector and the activities in which it engages. Although it is known that the numbers employed by formal and informal enterprises increased significantly in recent years the last comprehensive review of the sector was that undertaken under the Gemini Programme as long ago as 1990.

Intervention(s) planned

The government will commission a review of the SMME sector to determine numbers of enterprises involved, areas of activity, numbers employed, levels of remuneration and business level constraints. This will build on the information gathered through the national census and be modelled on the review carried out under the Gemini Programme in 1990.

Responsible ministry/other agency of the government

MTICM, BEDCO

Verifiable indicators of success of intervention

The success of the intervention will be determined by the completion of the review.

Assumptions

Importance to achievement of plan objectives

The government regards the intervention as very important to the achievement of plan objectives.

Likelihood of success in plan period

It is considered likely that the review can be carried out within the plan period.

<u>27. Preference for SSME suppliers in government procurement tendering</u>

Constraint(s) addressed

It is usually not possible for local suppliers of goods to compete with South African-based suppliers in terms of price in bidding for government supply contracts because of the difficulty in securing economies of scale in their operations.

Intervention(s) proposed

The government will continue to give a 15 per cent price preference to local companies in tendering for supplies of goods and services. This is considered a useful way of promoting the development of SMME suppliers.

Responsible ministry/other agency of government

MFDP.

Verifiable indicators of success of intervention

Maintenance of present numbers of local suppliers within totals of successful bidders for government supply contracts.

Assumptions

Importance to achievement of plan objectives

This intervention is judged a necessary measure in the achievement of plan objectives

Likelihood of success in plan period

The intervention is likely to be successful within the plan period.

<u>28. Development of business linkages between large industrial enterprises and SMMEs</u>

Constraint(s) addressed

Although there are more backward and forward linkages between large industrial enterprises and SMMEs than is generally thought, the development of such links are constrained by ignorance on the part of the large producers of the various supporting activities they might economically access within Lesotho and, on the part of the SMMEs, of the needs of the large producers and how to promote themselves as suppliers of these needs.

Intervention(s) planned

The government will develop a Business Linkages project in partnership with the private sector. This programme is entirely voluntary and no pressure will be brought to bear to compel industrial enterprises to switch to local suppliers of goods and services which would be in direct contravention of overall industrial policy that the government will not intervene in sectoral decision making processes to achieve specific outcomes.

Responsible ministry/other agency of the government

BEDCO.

Verifiable indicators of success of intervention

Verifiable indicators of the success of the intervention will include:

- Meetings between the large industrial enterprises and small suppliers of goods and services to exchange information;
- Identification by large industrial enterprises of goods and services they might purchase locally;
- Changes in sourcing of goods and services by large industrial enterprises from foreign to domestic suppliers.

Assumptions

Importance to achievement of plan objectives

This intervention is considered important to the achievement of plan objectives.

Likelihood of success in plan period

A degree of success is expected within the plan period.

<u>29. Small business advisory service</u>

Constraint(s) addressed

The development of SMMEs and, consequently, their absorption into the formal economy is hindered by entrepreneurs' lack of business skills and their inability to prepare the business plans necessary for them to access credit.

Intervention(s)

The government will implement the proposals in the SME White Paper for the provision of Private Sector-led business advisory services. The role of BEDCO in this process will be considered in the course of the enquiry indicated into the role of that body in Intervention 3.

Responsible ministry/other agency of government

MTICM.

Verifiable indicators of success of intervention

Increased licensing/registration of viable SMME operations supplying goods and services.

Assumptions

Importance to achievement of plan objectives

Improvements in this service are considered very important to the achievement of plan objectives.

Likelihood of success in the plan period

It is likely that shortages of qualified personnel will adversely affect the effort to expand this service during the plan period. However, increases in the numbers of SMMEs entering the formal sector of the economy are expected within the plan period.

ANNEX II - LIST OF ACRONYMS

Acronym	**Definition**
AGOA	African Growth and Opportunity Act, 2000
ALAFA	Apparel Lesotho Alliance to Fight Aids
BEDCO	Basotho Enterprises Development Corporation
BNLS	Botswana, Namibia, Lesotho and Swaziland
CET	Common External Tariff
DCCS	Duty Credit Certificate Scheme
EC	European Commission
EPA	Economic Partnership Arrangement
EU	European Union
GoL	Government of Lesotho
ICA	Investment Climate Assessment.
IMP	Industrialisation Master Plan
LDC	Least Developed Country
LEC	Lesotho Electricity Corporation
LNDC	Lesotho National Development Corporation
MFA	Multi-Fibre Arrangement
MFDP	Ministry of Finance and Development Planning
MFN	Most-Favoured Nation
MTICM	Ministry of Trade and Industry, Cooperatives and Marketing
PRAU	Policy & Regulatory Analysis Unit
PTA	Preferential Trade Arrangement
PRC	People’s Republic of China
RSA	Republic of South Africa
SACU	Southern African Customs Union
SADC	Southern African Development Community
SP	Special Provision
SSA	Sub-Saharan Africa
TCIDP	Textile and Clothing Industry Development Programme
TIFC	Trade and Investment Facilitation Centre
USA	United States of America
USTR	United States Trade Representative
WASA	Water and Sewerage Authority
WTO	World Trade Organisation