

LESOTHO

Table 1 **2015**

Population, million	2.1
GDP, current US\$ billion	2.0
GDP per capita, current US\$	926
Poverty rate (\$1.9/day 2011PPP terms) ^a	59.6
Poverty rate (\$3.1/day 2011PPP terms) ^a	77.3
Gini Coefficient ^a	54.2
School enrollment, primary (% gross) ^b	111.0
Life Expectancy at birth, years ^b	48.8

Sources: World Bank WDI and Macro Poverty Outlook.

Notes:

(a) Most recent value (2010)

(b) Most recent WDI value (2014)

The easing of GDP growth since 2013 is expected to continue through 2016 due to persistent drought effects and weak regional conditions, leading to a decline in SACU revenues and associated fiscal pressures. The drought will likely translate into only a moderate decline of 1.36 percentage points in the poverty rate (\$1.9 PPP a day) to 55.4 percent by 2018.

Recent developments

Following average growth of 4.7 percent in 2012 and 2013, the advance in real GDP softened to 3.6 percent in 2014 and slackened further to 1.7 percent in 2015. The main drivers of growth deceleration include shrinking agricultural production due to El-Nino, a slowdown in industrial output due to uncertainty of AGOA extension, and slippage in mining production. Services remain a brighter spot, growing at 2.6 percent in 2015.

Net exports declined due to supply reductions and weak demand from trade partners. Investment growth was modest due to the shortfall in the government's capital budget, uncertainty over AGOA and the completion of the Metelong Dam. Although government consumption remained high as the wage bill increased to 21.8 percent of GDP, government investment was limited due to under-execution of the capital budget (65 percent).

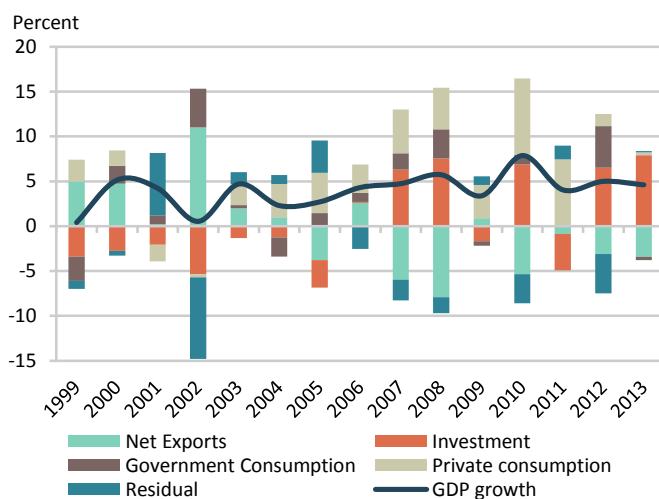
Fiscal balances are likely to deteriorate over the next years due to lower SACU revenues—which amounted to 30 percent of GDP in 2014/15. The overall fiscal balance registered a modest surplus of 0.6 percent of GDP in 2015, while the non-SACU fiscal deficit is estimated to stand at 24 percent of GDP in 2015/16, improving from 28.6 in FY2014/15. The current account deficit widened to 9.4 percent of GDP; while Lesotho's public debt increased to 59.5 percent of GDP in 2015 due to depreciation of the local currency.

Due to the severe drought, year-on-year inflation increased to 7.5 percent in June 2016, tied in large measure to increasing food prices. Food prices surged by 14 percent in June 2016 contrasted with levels for the same period a year earlier. CPI inflation registered 6 percent in 2015 and is likely to rise to 8.5 percent in 2016. International reserves were the equivalent of 6.1 months of imports in 2015, similar to year earlier ratios.

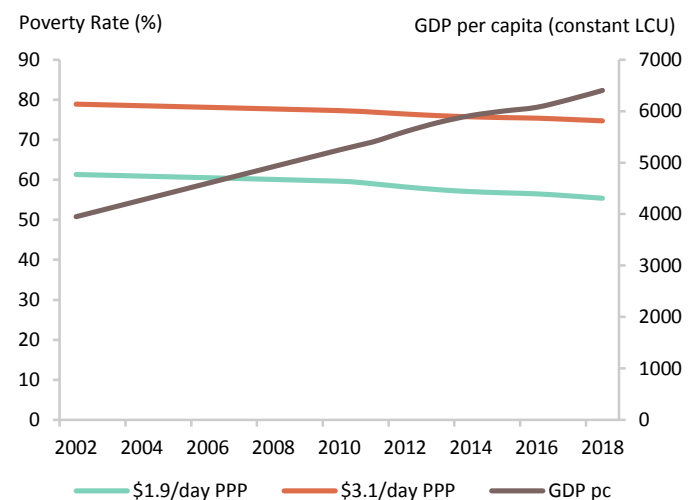
Between 2002 and 2010 Lesotho made little progress in reducing extreme poverty. The headcount poverty rate was 57.1 percent in 2010 (national poverty line), accompanied by high inequality, measured at 53.8 percent by the Gini coefficient—such inequality itself an obstacle to poverty reduction. Lesotho's economic structure and poorly targeted social protection policies are at the heart of high and stagnant poverty and inequality. Low-productivity agriculture remains the main source of income for over 1 in 3 households. The benefits of a well-paid public sector mainly flow to the most affluent households. Most social protection transfers do not target the poor.

Outlook

Growth is expected to increase slightly to 2.4 percent in 2016-- a downward revision from the last forecast (2.6 percent). Weaker growth prospects in South Africa, and uncertainty due to the sustainability of the exchange rate peg are key factors in the markdown to growth. Over the medium

FIGURE 1 Lesotho / Contributions to annual GDP growth


Source: Lesotho Bureau of Statistics.

FIGURE 2 Lesotho / Actual and projected poverty rates and GDP per capita (constant LCU)


Source: World Bank (see notes to table 2).

term growth is expected to pick up gradually to 3.7 percent in 2017/18 driven by the commencement of operations at the Lihobong mine in the 4th quarter of 2016, and accelerate further to 4 percent by 2018/19 supported by construction activity tied to the Second Phase of the Highlands Water project.

Fiscal balances will come under increasing pressure over the next years due to lower SACU revenues. Such revenues are projected to fall to 15.9 percent of GDP in FY2016/17—almost halving from earlier levels—driven by a slowdown in the South African economy, and are expected to remain low into the medium term. Still, the fiscal shortfall is anticipated to ease from 9.4 percent of GDP in 2016 to 3.2 percent by 2018. Lesotho is expected to finance this deficit by drawing down reserves. Limited commercial bank interest in government bonds and potential additional spending needs arising from a mid-term budget review have the potential to exacerbate the fiscal stance. And significant deterioration in the current account deficit is expected (to 19 percent of GDP in 2016) due to the sharp falloff in SACU revenues.

Inflation is anticipated to bounce back to 6 percent over the medium term, while private consumption should advance only modestly in 2016 due to lower wage

increases. Investment has dropped considerably following completion of the Metelong Dam and increased uncertainty regarding AGOA. Capital outlays should grow once more in 2016 due to commencement of mine operations, and remain strong in 2017 and 2018 due to the second phase of the Lesotho Highlands Water Project.

Tied to persistent effects of drought, the poverty rate (\$1.9 PPP a day) is projected to fall only moderately by 1.36 percentage points from 56.7 to 55.4 percent between FY2016 and FY2018. This is attributable to the sectoral composition of growth. Adverse weather conditions led to lower agricultural production during FY 2015 with persisting effects through FY 2016. The decline in production and corresponding increases in food prices will carry a more negative impact among the poor, deriving most of their income from agriculture. Though mining will grow quickly, the sector will not generate many jobs due to its capital intensity.

Risks and challenges

Risks to the outlook are several, and include: decline in SACU revenues, political instability, slow global recovery, lower

growth in South Africa, fiscal sustainability and competition due to the potential coming on-stream of the Trans-Pacific Partnership. In the medium term commitment to fiscal adjustment is crucial for macroeconomic stability. The current level of spending places strong pressure on the sustainability of public debt and the exchange rate peg. The government has shown some commitment to fiscal consolidation by keeping wage increases in line with inflation during 2016, but proposed measures in the budget fall short of the necessary adjustment. Though government spends a large portion of its budget on social sectors, outcomes to date have not been encouraging. Increasing efficiency and effectiveness of government spending is important to sustaining growth and promoting shared prosperity. Along with fiscal adjustment, ambitious structural reforms are needed to raise potential output. Improvements in human capital through lower HIV/AIDS prevalence and better educational outcomes, in investment climate constraints, and in key infrastructure are necessary to boost private sector development and job creation.

TABLE 2 Lesotho / Macro poverty outlook indicators

(annual percent change unless indicated otherwise)

	2013	2014	2015	2016 f	2017 f	2018 f
Real GDP growth, at constant market prices	4.5	3.6	1.7	2.4	3.7	4.0
Private Consumption	0.2	7.0	2.0	3.0	3.0	3.0
Government Consumption	-0.9	3.5	6.7	7.8	-3.3	6.2
Gross Fixed Capital Investment	17.4	-1.7	3.8	2.0	23.3	14.0
Exports, Goods and Services	-5.2	13.1	0.8	3.0	6.0	7.0
Imports, Goods and Services	1.4	7.0	3.5	4.6	7.6	8.2
Real GDP growth, at constant factor prices	4.4	3.1	1.9	2.5	3.0	3.5
Agriculture	13.2	4.8	-4.8	-4.0	2.0	2.0
Industry	-1.5	0.6	2.3	3.1	3.7	3.7
Services	6.8	4.2	2.6	2.9	2.7	3.5
Inflation (Consumer Price Index)	4.9	5.3	6.0	8.5	6.0	5.0
Current Account Balance (% of GDP)	-11.0	-6.3	-9.4	-18.4	-17.6	-17.1
Financial and Capital Account (% of GDP)	9.0	11.2	2.4	14.3	8.3	5.9
Net Foreign Direct Investment (% of GDP)	1.2	1.2	1.2	1.1	1.1	1.1
Fiscal Balance (% of GDP)	-2.3	0.6	0.1	-9.5	-4.9	-3.2
Debt (% of GDP)	44.2	49.5	59.5	59.9	57.3	54.5
Primary Balance (% of GDP)	-1.4	1.6	1.3	-8.5	-3.9	-2.5
Poverty rate (\$1.9/day PPP terms)^{a,b,c}	58.5	57.3	57.1	56.7	56.1	55.4
Poverty rate (\$3.1/day PPP terms)^{a,b,c}	76.6	75.9	75.8	75.5	75.2	74.7

Sources: World Bank. Macroeconomics and Fiscal Management Global Practice, and Poverty Global Practice.

Notes: e = estimate, f = forecast.

(a) Calculations based on 2010-CM SHBS.

(b) Projection using annualized elasticity at regional level with pass-through = 0.5 based on private consumption per capita in constant LCU.

(c) Projections are from 2013 to 2018.