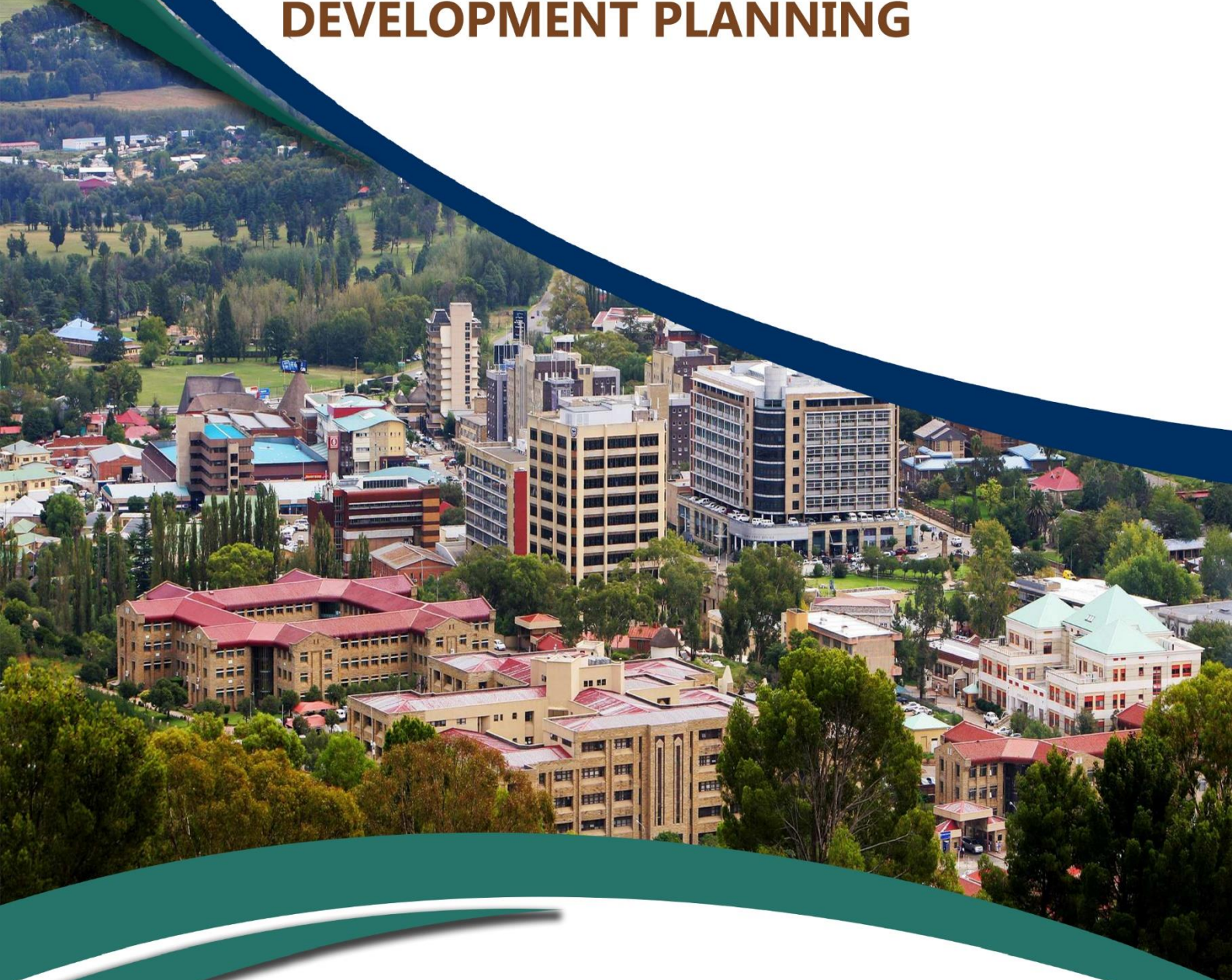




THE KINGDOM OF LESOTHO

MINISTRY OF FINANCE AND DEVELOPMENT PLANNING



2023/2024

BUDGET STRATEGY PAPER

November 2022

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LIST OF ABBREVIATIONS AND ACRONYMS

1. ART – Antiretroviral Therapy
2. BEDCO – Basotho Enterprises Development Corporation
3. BSP – Budget Strategy Paper
4. COVID-19 – Corona Virus Disease 2019
5. CSOs – Civil Society Organisations
6. DFA – Development Finance Assessment
7. DSA – Debt Sustainability Analysis
8. DSSI – Debt Service Suspension Initiative
9. FY – Financial Year
10. GCI – Global Competitiveness Index
11. GDP – Gross Domestic Product
12. GoL – Government of Lesotho
13. HIV/AIDS – Human Immunodeficiency Virus and Acquired Immune Deficiency Syndrome
14. HDI – Human Development Index
15. IATI – International Aid Transparency Initiative
16. INFF – Integrated National Financing Framework
17. KPAs – Key Priority Areas
18. LEC – Lesotho Electricity Company
19. LHWP – Lesotho Highlands Water Project
20. LNDC – Lesotho National Development Corporation
21. LSL – Lesotho Loti
22. MAP – Making Access Possible
23. MDAs – Ministries, Departments and Agencies
24. MFDPP – Ministry of Finance and Development Planning
25. MPM – Macroeconomic Policy and Management
26. MSMEs – Micro, Small and Medium Enterprises
27. MTDS – Medium Term Debt Strategy
28. MTEF – Medium-Term Expenditure Framework
29. MTFF – Medium-Term Fiscal Framework
30. MTR – Mid Term Review
31. NSDP II – National Strategic Development Plan II
32. PSID – Public Sector Investment Database
33. SA – South Africa
34. SACU – Southern African Customs Union
35. SADC – South African Development Community
36. SADP – Small-holder Agriculture Development Project
37. SOEs – State Owned Enterprises
38. SWAP – Sector Wide Approach
39. TB – Tuberculosis
40. UN – United Nations
41. UNDP – United Nations Development Programme
42. USD – United States Dollar
43. WASCO – Water and Sewage Company
44. ZAR – South African Rand

FORWARD

Budget Strategy Paper is instrumental to Government of Lesotho's strategic priorities and medium-term objectives. Public Finance Management and Accountability Act 2011 (PFMA Act, 2011) requires presentation of a Medium-Term Budget Strategy Paper for consideration and approval of the Cabinet. The Medium-Term Budget Strategy Paper for 2023/24 to 2025/26 has been formulated with a focus on economic recovery, increasing revenue, resolving high fuel prices, and protecting vulnerable segments of society.

The Paper provides a two-branched budget strategy. On the one hand, it encompasses optimal mobilization of revenue through broadening and deepening of tax base and increase in the tax net, removal of irrational exemptions, transformation of procedures, and augmentation of the capacity of revenue administration. On the other hand, it is based on reduction in non-development expenditure without compromising social and development priorities of the government.

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I. INTRODUCTION

1. **Under the Medium-Term Budget Framework, the BSP is a strategic policy document that outlines the upcoming proposed budget priorities after taking into account the macroeconomic conditions in the country.** The policy paper is reviewed annually to facilitate informed policy discussions and decisions for the preparation of the upcoming budget year, and to further evaluate the effectiveness of the Government's existing policies with the intention of bridging the gap between the public expectations and what is fiscally attainable.
2. **The 2023/24 BSP is meant to improve transparency in the preparation of the national budget and form the basis for a detailed budget preparation process** that will culminate in the presentation and approval of the 2023/24 budget by Parliament later on in the year. The BSP has incorporated public, stakeholders and parliamentary consultations and engagements on the policy priorities of the 2023/24 national budget in order to respond to difficult and uncertain global and domestic economic environment.
3. **The objective of the BSP is to present strategic policy priorities of the government** while enhancing the understanding amongst stakeholders of the broader macro-fiscal issues that guide both the budgeting process and the prioritisation of budget allocation. The policy priorities are in line with the national strategic documents as well as the Medium-Term Fiscal Framework.
4. **In preparation for the 2023/24 BSP, the Ministry of Finance and Development Planning (MFDP) has conducted the 2023/24 Pre-Budget Consultations in all administrative districts of the country.** The aim of the consultations was to increase awareness and public participation in the budget process at the local government level and provide an opportunity for input in policy direction for the preparation of the 2023/24 national budget.
5. **The 2023/24 BSP is designed to foster the recovery from the adverse effects of COVID-19, the Russia-Ukraine war and ensure resilience to future shocks.** The pandemic has highlighted many longstanding pre-existing vulnerabilities in the economy, such as high public expenditure, low domestic revenue mobilization, low investment, low productive capacity, and high-income inequality, as well as a limited capacity to attract foreign investment. On the other hand, the Russia-Ukraine war has escalated and worsened the uncertainty and upheaval to the supply and demand of goods and services. The situation has led to an immense impact on the global supply chain, impeding the flow of goods, fuelling dramatic cost increases and product shortages, and creating catastrophic food shortages around the world.
6. **While the country is unable to depend solely on the traditional suppliers, it is therefore necessary to diversify and consider other alternative sources for evitable supply chain transformation.** Lesotho should continuously implement measures to help reconstruct the economy in the wake of the COVID-19 pandemic and implement long overdue reforms to shift the economy to a stronger growth path. This will be achieved by reviewing and redefining Lesotho's sustainable development and growth path in the short to medium term to facilitate the post pandemic recovery.

7. **At a time of limited fiscal resources, the strategic thrust for 2023/24 -2025/26 national budget should be to two-fold;** on the one hand, it should encompass optimal mobilisation of revenue through broadening and deepening of tax base and increase in the tax net, removal of irrational exemptions, simplification of procedures, and augmentation of the capacity of revenue administration. On the other hand, it should be based on reduction in non-development expenditure without compromising social and development priorities of the government. Whilst the BSP provides a snapshot of proposed key issues for consideration during a given fiscal year, the subsequent annual Budget Statement and Estimates will provide more elaborate details of these issues, taking into account inputs from all stakeholders.

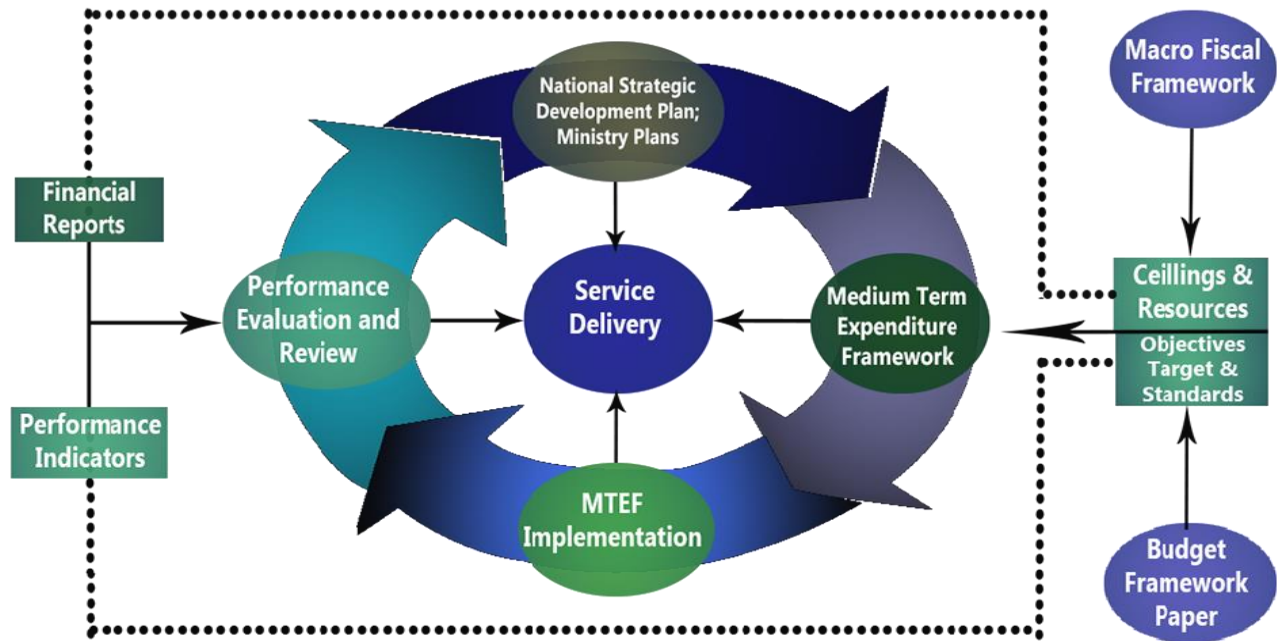
WORKING TOGETHER FOR BETTER FUTURE

8. **The Government will implement sector budgeting approach which is defined in the NSDP II and it is anticipated to achieve improved service delivery.** Government of Lesotho has overtime invested significantly in public finance reforms, especially in the formulation of the budget but has failed to link the budget allocations to planning. In ensuring improved alignment, the main goal is to start by making key priority areas of NSDP II as the broad functions of government activities in relation to specific government objectives. While intermediate outcomes will be considered as sub functions of the government objectives. This will enable government to better align its priorities and spending plans, as well as to improve value for money, enhance decision-making and service delivery through proper coordination of all government programmes both at national and local government levels.
9. **In the 2023/24 fiscal year, the MFDP will harmonise the sectors used in budget preparation and in the NSDP II to ensure appropriate allocation of resources and proper alignment of national priorities and budget through full implementation of Medium-Term Expenditure Framework (MTEF).** This will be realised through establishment of Sector Working Groups (SWGs) that are intended to plan and decide on the allocations together. The same exercise will be done to align Parliamentary Portfolio Committees to that of the NSDP II to make reporting easier for executive and spending units and thereby enhancing accountability.

BUDGET CYCLE

10. **To provide for responsible government, budgeting is geared to a cycle. The cycle allows the system to absorb and respond to new information and, therefore, allows government to be held accountable for its actions.** Although existing budget systems may be less than perfect in guaranteeing adherence to this principle of responsibility, the argument stands that periodicity contributes to achieving and maintaining a constitutional government. The budget cycle consists of four phases: (1) strategic planning, (2) MTEF preparation, submission and approvals, (3) MTEF execution, and (4) evaluations, audit and oversight.

Figure 1 Budget Cycle



BUDGETARY PRINCIPLES

11. **In response to consistent shortfall in cash and foreign reserves as well as the volatile SACU revenues;** the depreciation of South African Rand (ZAR) against major world currencies and its negative impact on the external debt stock and strong recurrent expenditure growth which have put pressure on budget deficit, the Government will continue to adopt the following principles which will underpin and guide the 2023/24 budget:
 - i. Adopt a budget that is affordable, sustainable, and yet responsive to the needs of the country over the medium-term.
 - ii. Adopt austerity measures to control and curb expenditure waste:
 - a. Over the medium-term, bring the overall fiscal deficit to below 3 percent of GDP consistent with long-term GDP growth.
 - b. The Government's expenditure on wage bill should not grow as a share of GDP and must be reduced over the medium term alongside measures to streamline the civil service.
 - c. Consistently constraining the Government's recurrent expenditure not to grow more than the development expenditure as a percent of GDP.
 - iii. Improve monitoring, evaluation, transparency, and accountability mechanisms to ensure expenditure efficiency.
 - iv. Prioritise the elimination and curtailment of accumulation of arrears.
 - v. Expand domestic revenue mobilisation to reduce reliance on volatile and shrinking transfers from the Southern African Customs Union (SACU).
 - a. Introduce reforms, as needed, to broaden the tax base, boost taxpayer compliance, and improve revenue administration.
 - b. A realistic degree of predictability with respect to the level of tax rates and tax bases shall be maintained, considering any future tax reforms.

- vi. Over the medium-term, the Government's borrowings shall be used only for the purpose of financing development expenditure and not for recurrent expenditure.
- vii. Expand the sources of public debt financing to enable the Government to restructure its public debt portfolio and to better facilitate the financing of deficit; and
- viii. Achieve consistency of the Medium-Term Fiscal Framework (MTFF) and Medium-Term Expenditure Framework (MTEF) to the national priorities, efficiency, effectiveness, and value for money in public expenditure.

II. DEVELOPMENT CONTEXT

BACKGROUND

12. **The current developments in the global economy that arose at the back of the advent of COVID-19 have had severe negative impact on Lesotho's economic growth which was already on a downward spiral.** The effects of the pandemic have caused the unprecedented socioeconomic chaos that transcend the interventions outlined in the current five-year national development plan. For economic recovery, Lesotho will need to make policy decisions and trade-offs that promote domestic economic resuscitation, macroeconomic stability and fiscal sustainability. This will require a review of the national strategy to be responsive to the emerging socio-economic challenges in the short term, as well as envision development agenda in the medium term. The NSDP II will be revised and reprioritized to make it to be more focused and bring the plan to the context. The plan will continue to guide development and resource allocation in the medium term.

13. **The developmental challenges that have haunted Lesotho for a long time still persist and are further exacerbated by the unfavorable and uncertain external economic environment facing global economies.** Lesotho is faced with increasing poverty, endemic corruption, political instability, high prevalence of HIV/AIDS and weak government capacity to implement strategies aimed at improving the poor socio-economic plight faced by the majority of Basotho. If Lesotho is to realize its economic development goals, strong linkages between resource allocation and national priorities need to be forged, robust monitoring and evaluation should be established, and accountability measures (rewards and sanctions) need to be instigated upon the implementing ministries, departments and agencies. The 2023/24 BSP is developed against a difficult financial and socio-economic environment which will require strict prioritization of budget allocations and implementation.

PERSISTENT POVERTY AND INEQUALITY

14. **Lesotho has one of the highest poverty rates in the Southern African Development Community (SADC) region.** The level of poverty in Lesotho dropped from 56.6 percent in 2002 to 49.7 percent in 2017. This decrease was largely attributed to a more equitable distribution of consumption in that period. However, it is worth noting that poverty levels in rural areas are higher than in urban areas. Poverty fell in four out of six regions. The Rural Mountains and Rural Senqu River Valley experienced poverty increase. For instance, 67.8 percent of Basotho living in Rural Mountains were poor in 2017, an increase of 10.9 percentage points from 56.9 percent recorded in 2002. This enlarges the already large rural urban divide and indicates that poverty will continue to be a rural phenomenon if development initiatives are still focused only in urban areas. Furthermore, a profile of Lesotho's poor shows that poverty levels are highest among female-headed households, who are less educated, unemployed and caretakers of large families and

children. This implies acute vulnerability and increased risk of food insecurity in female-headed households.

15. **Food insecurity is forecasted to increase in the medium-term in Lesotho.** The most recent national food security assessment report indicates that 22 percent of Basotho living in the rural areas will face severe food insecurity between October 2022 and March 2023. This indicates the worsening situation of food insecurity in Lesotho as only 15 percent was deemed food insecure for the period between July and September 2022. It is estimated that 320,000 people in rural areas and 201,000 people in urban areas will require food assistance towards the end of 2023 and early 2024. The foreseen increase of acute food insecurity levels is primarily due to the reduced harvest, high food prices in basic food and non-food commodities and a slow recovery of households' income reflecting a downturn economic growth. This has compromised the purchasing power of very poor and poor households, resulting into some households engaging in negative livelihood coping strategies.
16. **Inequality measured by Gini coefficient has declined to 44.6 percent in 2017/18 fiscal year from 51.9 percent in 2002/03 fiscal year.** The improvement is due to expansion of the social protection programs and an increase in wage incomes among the poor. Lesotho spends 4.5 percent of Gross Domestic Product (GDP) on social protection programs, against the below 2 percent in other African countries or lower middle-income countries. Despite this improvement, Lesotho remains to be one of the 20 percent most unequal countries in the world.

RISING UNEMPLOYMENT

17. **Unemployment is high at 22.5 percent (males 22.6 and females 22.2)¹ and even higher among the Youth at 29.1 percent (males 27.4 and females 31.1).** The unemployment challenge is exacerbated by a small private sector whose competitiveness has been limited by skills mismatches and lack of entrepreneurship programs for growth-oriented businesses. Furthermore, manufacturing sector which has always been the main driver of private sector employment continues to be negatively affected by the aftermath of COVID-19 epidemic.

INTERNATIONAL COMPETITIVENESS

18. **Lesotho ranks 131 out of 140 countries in the Global Competitiveness Index (GCI) and 122 out of 190 countries with a score of 59.4 on the Ease of Doing Business in 2019.** Lesotho's international competitiveness ranking is low in comparison to other SACU countries in both Global Competitiveness and Ease of Doing Business Rankings. This is as a result of inadequate enabling policy and regulatory frameworks, poor functioning business development services, a paucity of domestic capital markets investing in local economy in a way that promotes sustainable and equitable growth, and weak private sector. In addition, high integration of Lesotho's economy with that of South Africa implies increased exposure to external shocks. To reduce this vulnerability, Lesotho must diversify into new economic activities and remain competitive in the region and beyond.

¹ BOS Labour Force Survey 2019

Table 1: International Competitiveness of SACU Countries, 2019

| Country | Global Competitiveness Ranking | Ease of Doing Business |
|----------------|--------------------------------|------------------------|
| South Africa | 60 | 84 |
| Botswana | 91 | 87 |
| Namibia | 94 | 104 |
| Eswatini | 121 | 121 |
| Lesotho | 131 | 122 |

Source: 2020 Global Competitiveness Report and World Bank Ease of Doing Business Report

HUMAN DEVELOPMENT

19. **Lesotho continues to experience low levels of human development as compared to other developing countries in the region.** The country falls in the low human development category with a score of 0.527 and ranks 165 out of 189 countries on the 2019 UN Human Development Index (HDI). There is high level of communicable and non-communicable diseases including HIV/AIDS epidemic, worsened by the COVID-19 pandemic which has had a devastating impact on the country's human development, its economy, social structure and capacity of families to care for themselves.

Table 2: Human Development Index of SACU Countries, 2019

| Country | HDI Rank | HDI Value | Life Expectancy | GNI Per Capita |
|----------------|------------|--------------|-----------------|----------------|
| Botswana | 94 | 0.728 | 69.3 | 15,951 |
| South Africa | 113 | 0.705 | 63.9 | 11,756 |
| Namibia | 130 | 0.645 | 63.4 | 9,683 |
| Eswatini | 138 | 0.608 | 59.4 | 9,359 |
| Lesotho | 164 | 0.518 | 53.7 | 3,244 |

Source: 2020 UN Human Development Report

NATURAL DISASTERS

20. **In recent years, Lesotho has been experiencing some recurrent and extreme natural disasters that are predominantly weather related and are as a result of a change in climatic conditions.** The most common natural disasters Lesotho is prone to are droughts, floods and storms. Since most of the rural population depends on agriculture for livelihood, these natural disasters impede food production and exacerbate poverty among Basotho rural population. Lesotho should strengthen its efforts to implement the climate change adaptation and mitigation strategies in order to mitigate the effects of the climate change.

CLIMATE CHANGE

21. **Climate change and environmental degradation present a great threat to poverty reduction and to achieve achievement of development objectives.** In the past ten years, Lesotho has experienced successive climate shocks such as recurrent droughts, dry spells and floods which have negatively affected communities and households' livelihoods, with serious consequences for people's food security. The convergence of multiple vulnerabilities in Lesotho has created a complex risk profile, in which poor households and communities are continually exposed to a wide range of economic, health, environmental, income and climate risks and shocks. This exacerbates vulnerability among the poor and rural communities who tend to have lower coping capacities.
22. **Increased use of natural resources for farming, grazing, and fuel has resulted in high environmental degradation, presenting both economic and governance challenges.** Access to grazing land fuels communal conflicts, particularly during periods of drought. Arable land suitable

for agriculture is below 9 percent (279,773 hectares) of total land area (3 million hectares). Annual depletion of natural resources is estimated at 4.6 percent of gross national income and the country loses at least 2 percent of its topsoil annually due to erosion. About 66 percent of households live on degraded land which represents a direct challenge to agricultural production and food security.

INCREASING DEMAND FOR SOCIAL PROTECTION

23. **Lesotho is experiencing increasing demand for social safety nets from the poor and vulnerable groups such as orphans and people with disabilities, particularly for those leaving in rural areas.** With increased poverty, food insecurity, negative effect of climate change and COVID-19, many people will continue to need and demand social protection services and empowerment. It is therefore important to have a sustainable financing of social safety nets as a means of income for the vulnerable groups in the country. There is increasing evidence that social protection not only reduces poverty among direct beneficiaries and their households, but it also improves wealth distribution and economic growth within local communities. This makes comprehensive social protection an attractive policy instrument for both social protection and economic point of view. It also enhances human dignity, social cohesion and political stability.

DECLINING DONOR SUPPORT

24. **There is a decline in support from development partners which hampers support for development and social programs.** The development finance landscape for Lesotho has gone through a significant shift due to multifaceted factors. These include changing international priorities such as climate change, increasing incidences of natural disasters such as EL-NINO-induced drought and heavy rains, conflicts and COVID-19 pandemic. These risks erode traditional sources of aid and increase the competition for these scarce resources. A greater global need for aid (due to a larger number of humanitarian emergencies, predominantly natural disasters and conflict) has increased competition for aid globally, resulting in aid flows being more thinly spread. This has encouraged developing countries to seek alternative options (Public Private Partnerships, domestic resources mobilization just to mention a few) to finance their development priorities as it may no longer be possible to depend solely on traditional sources of finance for their development agendas, which require significant annual contributions.
25. **Mobilization of resources, and their allocation and management, in order to implement development projects remains a challenge.** As the Government of Lesotho seeks to reduce dependency on development assistance, it also recognizes the important role that it will continue to play in the country over the short and medium term. Therefore, to improve on resource mobilization, the government has finalized and launched the Development Finance Assessment which provided the snapshot of development finance in the country and its recommendations will in turn shape the roadmap that will foster the Integrated National Financing Framework. The development of the Integrated Financing Strategy is underway, and the strategy will help the government to identify possible mechanisms for mobilizing resources for achievement of development agenda with particular attention given to strengthening the domestic resource mobilization.

III. LESOTHO'S PROGRESS OF THE SUSTAINABLE DEVELOPMENT GOALS (SDGs) OF THE UNITED NATIONS AGENDA 2030

26. **Lesotho's development agenda is anchored on the NSDP II, which aims to transform Lesotho from a consumer-based economy to a producer and export-driven economy.** The plan underscores the Government of Lesotho's multisectoral approach of directly engaging citizens, empowering individuals and encouraging participation in the development process. NSDP II is the nucleus of all development plans in the country, including the United Nations Agenda 2030. The Agenda 2030 for Sustainable Development and its 17 Sustainable Development Goals (SDGs), adopted by all Member States of the United Nations in September 2015, provide a visionary roadmap for all countries and stakeholders to strive for a world of sustainable prosperity, social inclusion and equality while at the same time preserving our planet and leaving no one behind. It is through this global Agenda that countries made a commitment to embark on a journey to improve their countries' development status and improve the standard of living of their citizens. By no means is this an easy mission and in the recent years, it has been further compounded with the COVID-19 pandemic. Many hard-achieved gains are threatened as means of implementation are diverted to combat impact of the pandemic on health and socio-economic areas.
27. **Effective follow-up and review of the Agenda 2030 through peer learning is essential for renewed action and progress in achieving the ambitious and interlinked SDGs in these challenging times.** At the heart of this process are Voluntary National Reviews (VNRs), which have become a critical component of the review and implementation of the Agenda 2030 and the SDGs and will continue to show the way forward and provide essential source of lessons learned and experience sharing. The VNR is one of the ways that the country uses to monitor and report on the implementation of SDGs and achievement of the respective targets. Lesotho prepared its first VNR in 2019 and the second one in 2022. The 2022 VNR took an in-depth assessment of five goals selected by the UN under the theme "Building back better from COVID-19 while advancing the full implementation of the 2030 Agenda for Sustainable Development". The selected Goals were SDG 1 – No Poverty; SDG 4 – Quality Education; SDG 5 – Gender Equality; SDG 15 – Life on Land; and SDG 17 – Partnerships.

SDG 1 – NO POVERTY

28. **The GoL has successfully reduced absolute poverty in the past two decades.** Between 2002/2003 and 2017/2018, Lesotho's overall national poverty and extreme poverty headcount ratios declined from 56.6 percent to 49.7 percent and from 34.1 percent to 24.1 percent. The level of inequalities, measured as Gini index, also declined from 51.9 percent in 2002/2003 to 44.6 percent in 2017/2018. However, these gains were eroded by the effects of COVID-19 pandemic, pushing additional 2 percent of the population into poverty and rendering more than 25 percent food insecure.

SDG 4 – QUALITY EDUCATION

29. **Between 2016 and 2018, the Net Enrolment Rate (NER) at Early Childhood Care and Development (ECCD) centres increased,** partly due to Government of Lesotho's decision to provide reception classes in several primary schools to prepare young children for the primary curriculum. Enrolments by location indicate low levels of NER in rural districts. Regarding primary schooling, the country is close to achieving universal primary education (UPE). The NERs increased from 60.2 percent before FPE in 1999 to 85.8 percent in 2019. The review also noted

high repetition rates, especially among boys. The net effects of COVID-19 on the education sector shook the sector to its core, yet with private sector collaborations and innovation, a swift online mode of learning birthed a new means to learning, a trend likely to impact the sector positively post COVID-19.

30. **Secondary education has shown the least progress, with NER for both boys and girls low but much more adverse in the case of boys** and STEM subjects reflect a low uptake in the girl student population. It is further noted that Net Enrolments in the upper secondary was significantly lower than in lower secondary education, estimated at 11.1 percent and 21.0 percent for males and females, respectively.
31. **The Gross Enrolment Rate (GRE) in Higher Education Institutions (HEI) has shown limited overall growth in recent years with undergraduate programmes having the largest share of students.** The most significant growth has been in the private cross-border institutions while the least growth has been in the denominational providers all offering undergraduate health education. The highest enrolment remains at sub-degree level diploma enrolments constituting the majority (52 percent). The review also revealed that girls are generally ahead of boys in both access and the quality of learning outcomes, apart from mathematics at school-leaving examinations level.
32. **People with disability are under-represented in both ECCD and Tertiary levels.** With the sector facing all these challenges and opportunities to venture into online and other sustainable means of learning, resource mobilization and education funding model relevant to the current state is thus vey key.

SDG 5 – GENDER EQUALITY

33. **The Government of Lesotho has made progress with regard to de jure equality or equality in the eyes of the law**, where law reform has seen the removal of various discriminatory laws and the enactment of laws that foster an enabling environment for the advancement of women and the achievement of gender equality. Notable is the ongoing amendment of the Inheritance Act in 2022, which brings together the customary and the Roman-Dutch law allowing both sexes equal access to an inheritance of property. However, progress is limited with regard to de facto equality, where there is no full and effective enforcement of laws, policies and strategies. Regarding violence against women and girls, there are reports indicating an increase in cases of Gender-Based Violence (GBV) since the beginning of the mandated lockdown due to COVID-19.
34. **While the Government of Lesotho has made efforts to end child marriage, data reveals that between 2006 and 2016 there was an increase in the proportion of women who were married before the age of 18.** Lesotho, due to its patriarchal system, women still perform most of the domestic responsibilities, but qualitative data suggest that the inequalities in unpaid care may be declining. Lastly, the review noted that the women’s representation in parliament has generally been low throughout, but information from BoS reveals that representation of women in decision-making bodies has increased and even overtaken that of men in the civil service.

SDG 15 – LIFE ON LAND

35. **There has been notable progress in the proportion of forest area to the total land area between 2015 and 2020.** Much of this progress is due to community education programmes on the importance of growing of trees. Livestock agricultural projects such as WAMP empowered

beneficiaries on wetlands management for the sustainability of wool and mohair harvesting. While the data revealed that the area under formal protection has not changed since 2016, several areas (such as Letseng-La-Letsie Nature Reserve (LLLNR) and Tsetse) are either informally designated or proposed for protection in various parts of the country. And there has not been encroachment on the area covered under protected areas by other land-use activities. Regarding land degradation, the review noted that about 66 percent of households live on degraded land, and the country loses 2 percent of its topsoil annually due to soil erosion.

36. **The review also revealed that in 2016 the country had only one animal species listed in the IUCN Red List index, the Lesotho Meadow Katydid.** But the country now has additional three species. These include a bird species, bearded vulture (*Gypaetus barbatus*), aquatic (fish species) Maloti minnow (*Pseudobarbus quathlambae*) and a plant species, Spiral Aloe (*Aloe polyphylla*).

SDG 17 – PARTNERSHIPS FOR THE GOALS

37. **The review indicates that the country managed to enhance domestic resource mobilisation, despite the challenges brought by the COVID-19 pandemic.** The country introduced tax reforms to improve domestic resource mobilisation by bringing about collaboration between all institutions to effectively enable compliance. Government has adopted the roadmap on the Integrated National Financing Framework to enhance mobilization and management of development finance flows and to facilitate development of a financing strategy for development. Moreover, the Government of Lesotho adopted several initiatives such as the Public-Private Partnership (PPP) Policy, the Investment Policy and the Diaspora Strategy Engagement for Trade and Investment and strengthened the One-Stop Business Facilitation Centre (OBFC) to enable investors to register companies easily; get tax registration, industrial and trading licenses; get immigration, residence, and labour permits, as well as export and import permits and rebates.
38. **The government managed to develop its telecommunications infrastructure and extend access to mobile communication services in remote areas.** For instance, the GoL has constructed 22 towers that facilitated the migration from analogue to digital. On the policy front, the country further undertook to fortify the mobile communication industry by introducing the Communication (Subscriber Identify module registration) Regulations of 2021. The country also managed to develop the National Strategy for Development of Statistics (NSDS) II (2022/23-2026/27) to strengthen the collection, analysis and dissemination of development data and enhance institutional and technical capacities for monitoring and evaluation of development programmes.

IV. VISION 2020 EVALUATION

39. **Lesotho Vision 2020 provided a long-term vision for national development and outlined a number of broad long-term objectives to be achieved by 2020.** The Vision was implemented through the medium-term plans of Poverty Reduction Strategy Paper (PRSP), National Strategic Development Plan (NSDP) (I and II). The Vision was inspired by the themes: “By the year 2020 Lesotho shall be a stable democracy, a united and prosperous nation at peace with itself and its neighbors. It shall have a healthy and well-developed human resource base. Its economy will be strong; its environment well managed and its technology well established”.

40. **The Vision came to an end in 2020 and its implementation is currently being evaluated with the purpose of providing the Government of Lesotho with reliable information** that would assist in formulating a much more coherent and responsive long term development framework based on the latest information and data as well as lessons learnt from its implementation. The preliminary evaluation findings indicate that the Vision 2020 implementation frameworks have been coherent with the tenants of the Vision. However, the achievements made across different sectors have not influenced significant changes particularly at service delivery level and upliftment of Basotho people from abject poverty in particular those in the rural areas and the vulnerable people namely women, young girls, the disabled, the elderly and youth. As thus, the Vision is still relevant but requires major revisions to accommodate emerging issues as the overall priorities and needs of Basotho remain the same.

V. TRANSPARENCY, PARTICIPATION AND OVERSIGHT STRATEGY

41. **In fiscal policy, public participation is established throughout different stages of the annual budget cycle and should strengthen and complement existing systems of transparency and accountability.**



Different public participation mechanisms can cover a range of topics: from new policy, plans or revisions of policies in managing revenues, expenditures, sources of financing, assets, and liabilities, and extrabudgetary funds of government. It goes from national and sectoral planning to the preparation, assessment, and selection of projects, monitoring performance, audit, and review.

42. **The executive and oversight institutions should actively use public participation to address distinctive goals and challenges.** The way this is normally done is by creating formal responsibilities regarding fiscal issues, as well as the broader governmental structures in which they are embedded. For example, legislation might formally require the executive to engage with other actors before and after the budget is formally tabled in the legislature for approval. There are also different purposes for public participation across the stages of the fiscal policy cycle, with distinct tools that can be used to design, plan, and implement appropriate participation mechanisms.

VI. MACROECONOMIC TRENDS AND OUTLOOK

CURRENT SITUATION

43. **In its latest outlook, the International Monetary Fund (IMF) revised downwards its projection for global economy to 3.2 percent in 2022 after recording a strong growth of 6.0 percent in 2021 before slowing further to 2.7 percent in 2023.** The downward revision in growth outlook was attached to protracted war in Ukraine, escalation of sanctions on Russian Federation, the possibility of more lockdowns as part of the strict zero-COVID-19 strategy in China, as well as uncertainties related to the emergence and spread of new strains of the virus. Subsequently, world trade growth, which accelerated by 10.1 percent in 2021, is also expected to decelerate to 4.3 percent and 2.5 percent in 2022 and 2023.

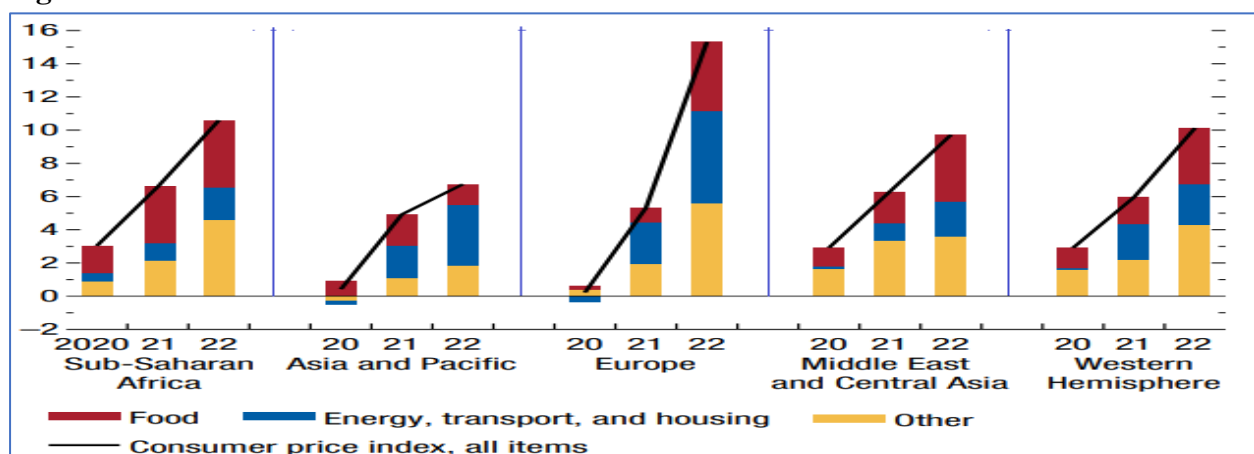
Table 3: World Economic Outlook Projections

| | Actual | Projections | |
|---|-------------|-------------|------------|
| | 2021 | 2022 | 2023 |
| World Output | 6 | 3.2 | 2.7 |
| Advanced Economies | 5.2 | 2.4 | 1.1 |
| Emerging Markets & Developing Economies | 6.6 | 3.7 | 3.7 |
| South Africa | 4.9 | 2.1 | 1.1 |
| World Trade Volumes | 10.1 | 4.3 | 2.5 |
| Commodity Prices (USD) | | | |
| <i>Oil</i> | 65.9 | 41.4 | -12.9 |
| World Consumer Prices | 4.7 | 8.8 | 6.5 |
| Advanced Economies | 3.1 | 7.2 | 4.4 |
| Emerging Markets & Developing Economies | 5.9 | 9.9 | 8.1 |

Source: IMF WEO October 2022

44. **The IMF also projects global crude oil prices to remain high at an average of USD107 per barrel in 2022 exacerbated by the geopolitical tensions in Ukraine.** Inflation on the other hand will be driven by high commodity and food prices and is projected at 7.2 percent in advanced economies and 9.9 percent in Emerging Markets and Developing Economies. Inflation forecast for 2023 is expected to ease to 6.5 percent from 8.8 percent in 2022 and is projected to slow to 4.4 percent in advanced economies and 8.1 percent in emerging markets and developing economies. In 2022, inflation in advanced economies has reached its highest rate. Although inflation is affecting most economies across the world, it has the most severe impact on lower income developing economies. In these economies, the larger part of household consumption expenditures is on food commodities, which means that inflation can have serious ramification on living standards. Regardless of a slight decline in the global consumer price index in July and August 2022, food price inflation in South Africa has been revised upwards to 8.1 percent from 7.4 percent the previous year and is forecasted to slow to 5.6 percent and 4.2 percent in 2023 and 2024.

Figure 2: Food and Fuel Driven Inflation



Sources: IMF WEO, Consumer Price Index database

STATE OF ECONOMY AND GROWTH PROSPECTS FOR 2023/24 -2024/25

45. **After experiencing significant supply and demand shocks caused by the pandemic in 2020, economic activity improved in 2021/22 with GDP growth recovering to 1.8 percent (-3.9 percent in 2020/21), mainly buttressed by a turnaround in private sector spending following less restrictions, better adjustments to the new norm, improved compliance to the standard operating procedures and rapid vaccination progress.**

Table 4: Real Sector 2019/20 – 2022/23

| Fiscal year | 2019/20 | 2020/21 | 2021/22 | 2022/23 | 2023/24 | 2024/25 | 2025/26 |
|---|--------------|--------------|------------|------------|------------|------------|------------|
| Percentage change | | | | | | | |
| | | Actual | | Estimate | Forecast | | |
| GDP at constant market prices, % growth | -2.0 | -3.9 | 1.8 | 2.3 | 2.7 | 3.9 | 4.0 |
| Agriculture, forestry and fishing | 2.4 | 2.1 | 2.3 | 1.5 | 1.3 | 2.0 | 2.5 |
| <i>Growing of crops; market gardening; horticulture</i> | <i>-13.5</i> | <i>18.6</i> | <i>1.5</i> | <i>1.7</i> | <i>2.9</i> | <i>3.1</i> | <i>3.1</i> |
| Mining and quarrying | -11.2 | -7.8 | 2.4 | 2.9 | 3.3 | 3.6 | 4.8 |
| Manufacturing | -2.8 | -5.2 | 8.1 | 1.3 | 1.2 | 1.3 | 1.3 |
| <i>Food products and beverages</i> | <i>-21.5</i> | <i>-11.5</i> | <i>6.5</i> | <i>2.5</i> | <i>3.0</i> | <i>3.5</i> | <i>4.0</i> |
| <i>Textiles, clothing, footwear and leather</i> | <i>0.0</i> | <i>-2.5</i> | <i>8.5</i> | <i>0.8</i> | <i>0.6</i> | <i>0.6</i> | <i>0.7</i> |
| <i>Other manufacturing</i> | <i>-6.6</i> | <i>-23.9</i> | <i>5.4</i> | <i>6.5</i> | <i>5.1</i> | <i>6.4</i> | <i>5.0</i> |
| Construction | -24.2 | -30.9 | 11.8 | 12.3 | 20.9 | 21.9 | 19.7 |
| Wholesale and retail trade; repair of motorvehicles | -19.7 | -21.3 | 1.3 | 1.5 | 2.3 | 3.1 | 3.1 |
| Accommodation and food service activities | -26.3 | -34.2 | 0.8 | 1.1 | 1.5 | 1.9 | 2.3 |
| Information and communication | 2.1 | -0.6 | 5.4 | 4.5 | 5.0 | 6.0 | 2.8 |
| Financial and insurance activities | 36.3 | 3.8 | -1.1 | 5.0 | 4.7 | 4.8 | 5.6 |
| Government sector | 1.4 | 4.8 | 0.3 | -6.5 | -0.5 | 2.8 | 4.4 |

Source: MFDP

46. **The gradual improvement in income and labor market conditions during the year had provided support to household spending.** Meanwhile, investment activity benefitted from continued capital spending especially in the Lesotho Highlands Water Project II, Queen Elizabeth II hospital and Ramarothole Solar Power generation station, alongside other government financed capital spending. In addition, improvement in global rough diamond prices have supported diamond export in 2021/22. External demand also provided additional support to Lesotho’s textiles exports in 2021/22.
47. **Economic recovery continued in the first half of 2022. Growth in the first quarter expanded by 1.5 percent, supported by strong growth of 53.1 percent in mining and quarrying sector and construction which expanded by 17.3 percent.** However, growth slowed in the second

quarter to 0.1 percent. The performance in quarter two was driven by weak performance in manufacturing sector which contracted by 17.7 percent.

Figure 3: Real Domestic Product

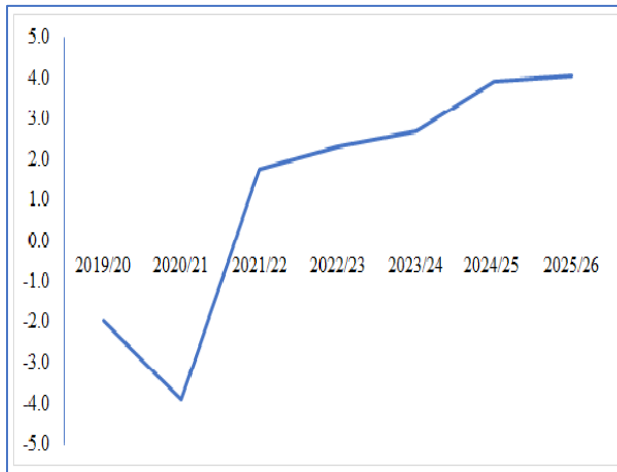
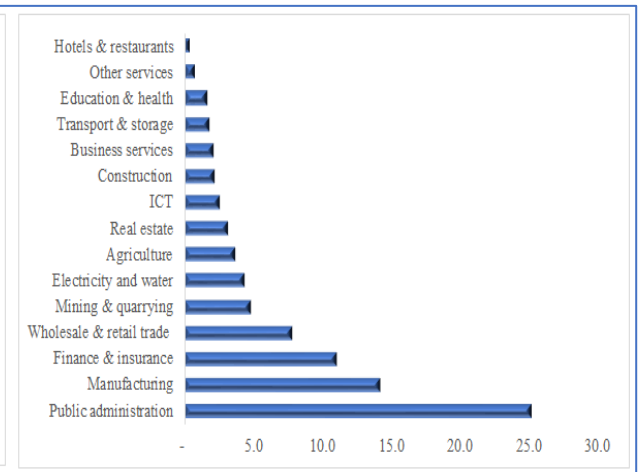


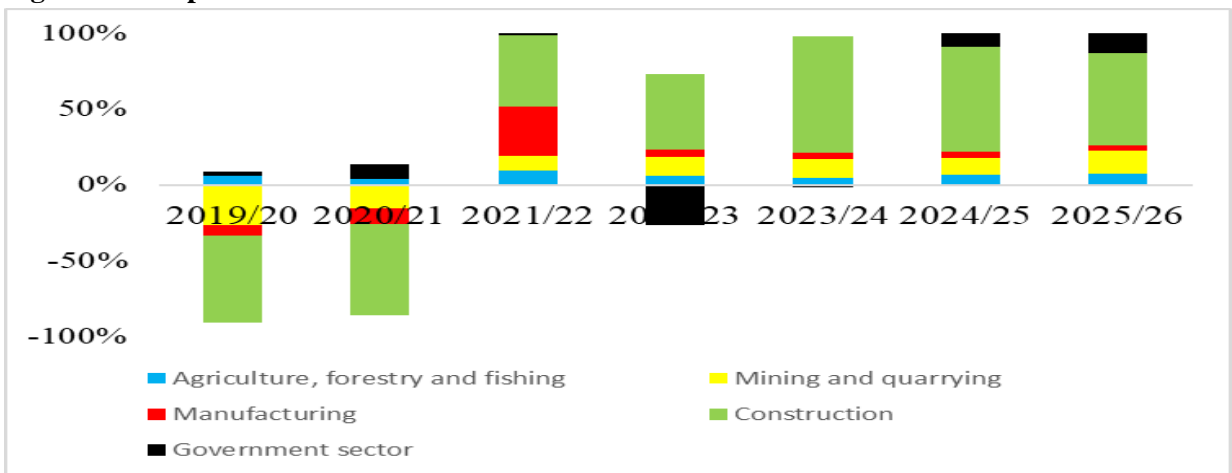
Figure 4: Sectoral Contribution to GDP Growth



Source: MFDP, BoS

48. **The high integration of Lesotho's economy with South Africa implies increased exposure to external shocks and recovery in the remaining half of 2022/23 will depend on economic developments in South Africa which is directly affected by global economic developments.** Protracted war in Ukraine, for instance, have caused economic pressures on multiple fronts, most notably an increase in global inflation as commodity prices continue to rise. Also, the risk of tighter global financial conditions, labor shortages and rising cost of living may pose a challenge to the South African economic recovery efforts and consequently spill over to Lesotho's effort to recover. However, growth is projected to average 2.3 percent by the end of 2022/23 and expand further to 2.7 percent in 2023/24 before averaging 4.0 percent between 2024/25 and 2025/26. The positive outlook is supported by continued activities of LHWP II dam construction together with huge investment in climate smart agriculture by Millennium Challenge Corporation (MCC) and Small Agriculture Development Project (SADP II).

Figure 4: Composition of GDP Over the Medium-Term



Source: MFDP

FITCH RATING

49. **Fitch Ratings has revised Lesotho’s outlook on Long Term Foreign Currency Issuer Default Rating (IDR) to stable from negative and affirmed the IDR at ‘B’.** The revision of the outlook to stable from negative reflects better than expected performance in public finances, resistance in domestic financing and continued support from multilateral and bilateral lenders that have combined to ease concerns regarding financing pressures and risks to the exchange rate peg. However, the ‘B’ rating is constrained by high external indebtedness and weak medium-term growth prospects. The current growth profile will be dampened by soaring commodity prices, lower SACU revenue sluggish regional growth and climate change.

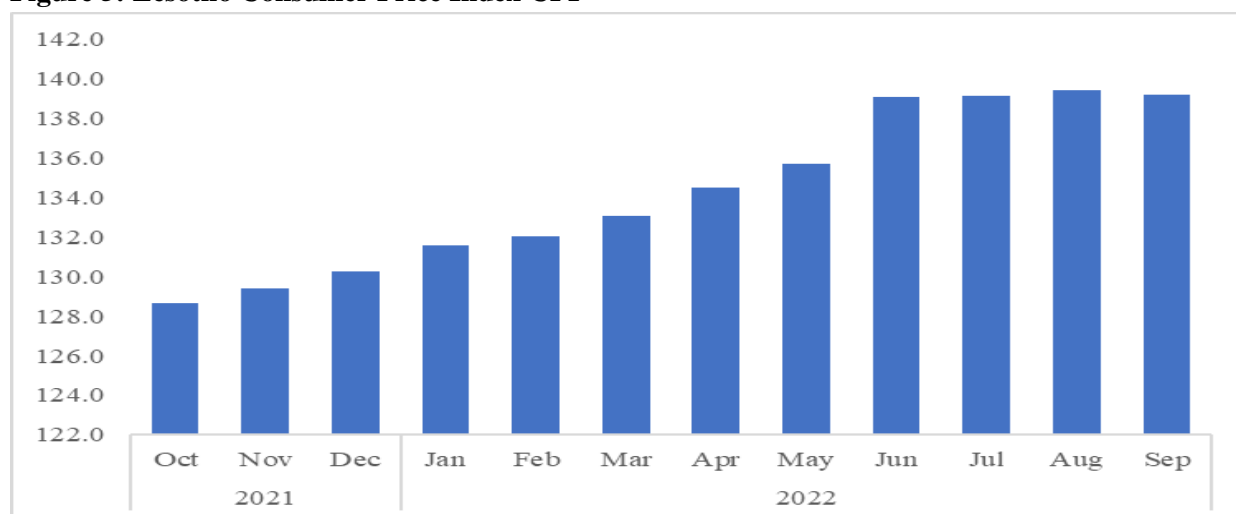
FISCAL STRATEGY

50. **The government is committed to putting in place a transparent medium-term expenditure framework (MTEF) which seeks to contain expenditure and limits wasteful capital spending by identifying and reducing stalled projects, while improving investment appraisal and execution.** Furthermore, the government aims to lessen the amount of domestic arrears and fiscal rule will be explored and adopted which will manage growth of such arrears.

INFLATION

51. **Elevated imported plus domestic food inflation (10.2 percent) and high fuel prices (14.5 percent) are key sources of inflationary pressure observed in September 2022.** Annual headline inflation accelerated to 9.2 percent in September from 5.4 percent observed in the same month of 2021. These price developments have broadly increased the cost of living of most households.

Figure 5: Lesotho Consumer Price Index CPI



Source: BoS – Statistical Report No.29:2022

52. **Central Bank of Lesotho’s response in curbing inflation has been through monetary tightening as seen by the increase in the CBL Rate from 5.5 percent per annum to 6.25.** The bank also revised upwards the current Net International Reserve floor from USD720 million to USD730 million in order to maintain the one-to-one exchange rate peg between Loti and ZAR. Over the medium term, price developments in Lesotho will continue to mimic those in South Africa.

53. **Nevertheless, the Government will continue to monitor the various economic risks and effectively manage any external shocks that may affect the wellbeing of Basotho and their businesses.** The Government's medium-term priority is to implement structural reforms by, among others, increasing inclusive and sustainable economic growth and private sector job creation; strengthening human capital development as well as enhancing transparency and accountability of public institutions; promoting regional collaboration to ensure resilient infrastructure development and energy provision. These measures will further improve policy certainty and investors' confidence, thus strengthening the country's economic resilience for Lesotho to continue becoming an attractive investment destination.

Box 1: Performance of Agriculture Sector in the First Half of 2022

Considering the adverse impact of climate change, agricultural sector contracted 11.9 percent and 6.5 percent in both quarter one and two of 2022. This was worsened by sharp increase in agricultural inputs during the first half of the year. Fertilizer prices have increased nearly 30 percent since the start of 2022, following last year's 80 percent surge. Spiralling prices are driven by a confluence of factors, including surging input costs, supply disruptions caused by sanctions on Belarus and Russia amid war in Ukraine, and export restrictions on China.

Fertilizer prices rose in response to the war in Ukraine, reflecting the impact of economic sanctions and disruptions in Black Sea trading routes. Russia accounts for about 16 percent of global urea exports and 12 percent of DAP and MAP exports, while Russia and Belarus together make up two-fifths of global MOP exports. Adding to supply concerns, China suspended exports of fertilizers until June 2022 to ensure domestic availability.

Domestic price trends for selected fertilizers

From January 2021 to September 2022, domestic fertilizer price for Potassium Chloride (KCL), Urea and Mono-Ammonium Phosphate (MAP) increased by 179.1 percent from M6 856 per ton to M19 136 per ton, 139.4 percent from M7 880 per ton to M18 862 per ton and 101.8 percent from M11 753 per ton to M23 718 per ton, respectively. The fluctuation of the domestic prices of fertilizers is subjected to price volatility in the global market as Lesotho is a net importer of fertilizers. Since the beginning of 2022 international fertilizer prices have been rising steeply in response to lower global supply. Export restrictions by China and Russia of fertilizers and the high international price of gas are aggravating the local fertilizer price hikes. For net importing countries, macroeconomic factors such as the exchange rate also play a crucial role in this regard.

FISCAL OUTLOOK

54. **The 2021/22 budget was drawn alongside a projected fiscal deficit of 13.1 percentage points of GDP in the wake of poor SACU revenues shares coupled with spending which increased alongside better SACU revenue shares in 2020/21.** However, the end year outcome turned out better than expected. Overall fiscal deficit was recorded at M1.6 billion, an equivalent of 4.3 percentage points of GDP. Although SACU revenue for 2021/22 was lower by M2.9 billion relative to 2020/21, the issuance of quarterly spending warrants to line ministries well served the

purpose of muting fast-growing expenses. Government was therefore forced to allow recurrent spending to average only M13.6 billion against budget estimate of M16.3 billion.

55. **Consistent with projected GDP growth of 2.3 percent in 2022/23, the overall fiscal operations are expected to remain muted at 4.3 percentage points of GDP (M1.7 billion) despite reduced SACU revenue shares which dwindled by M608.5 million against M6.01 billion received in 2021/22.** However, the 2022/23 budget had projected a deficit of 7.7 percentage points of GDP (M3.3 billion) at the back of projected 14.3 percent increase in recurrent spending relative to 2021/22. The government wage bill is projected to decrease by M1.2 billion against the budget estimate of M7.9 billion. Also, M20.6 million will be saved in use of goods and services, while debt service will remain the same as budget at M765.7 million. It is expected that by end of 2022/23 fiscal year, tax revenue will be short of its budget target by M531.26 million, while other revenue will miss the target by M531.3 million. the expected shortfall in the tax revenue will draw from poor performance of income tax collection which is expected to be short of M318.7 million compared with budget estimate. Out of the projected M586.4 million alcohol and tobacco levy, nil amount will be collected after the levy failed to take effect.

Table 2: Medium Term Fiscal Framework 2020/21 – 2024/25 (Million LSL)

| | 18/19 | 19/20 | 20/21 | 21/22 | 22/23 | 23/24 | 24/25 | 25/26 |
|--|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| | | Actual | | | Est. | Projection | | |
| Revenue | 16,013.7 | 16,257.6 | 18,632.8 | 17,569.4 | 18,666.7 | 19,060.6 | 21,706.5 | 23,469.8 |
| Revenue without SACU | 10,471.4 | 10,031.4 | 9,652.2 | 11,561.4 | 13,267.2 | 13,893.0 | 15,252.7 | 16,884.2 |
| Taxes | 7,616.8 | 7,346.5 | 6,778.6 | 7,756.5 | 8,976.0 | 9,876.2 | 10,987.7 | 12,190.0 |
| Taxes on income, profits and capital gains | 4,313.1 | 4,052.1 | 3,722.1 | 4,087.9 | 4,537.0 | 4,986.1 | 5,536.9 | 6,169.8 |
| Payable by individuals | 2,170.3 | 2,195.7 | 2,532.8 | 2,320.3 | 2,489.4 | 2,775.6 | 3,082.9 | 3,448.9 |
| Payable by corporations and other enterprises | 1,203.9 | 1,004.4 | 447.0 | 925.4 | 1,060.7 | 1,221.0 | 1,355.2 | 1,480.7 |
| Other taxes on income, profits and capital gains | 938.9 | 851.9 | 742.4 | 842.2 | 986.9 | 989.4 | 1,098.8 | 1,240.2 |
| Taxes on goods and services | 3,299.6 | 3,294.4 | 3,056.4 | 3,668.5 | 4,439.0 | 4,889.3 | 5,448.1 | 6,020.2 |
| Value added taxes | 2,899.8 | 2,906.6 | 2,607.7 | 3,051.2 | 3,815.8 | 4,193.5 | 4,656.7 | 5,189.0 |
| Excise taxes | 393.2 | 372.6 | 420.1 | 596.7 | 608.7 | 676.0 | 770.3 | 809.9 |
| Grants | 1,076.8 | 1,255.9 | 1,049.0 | 1,756.6 | 2,262.7 | 1,850.5 | 1,984.6 | 2,127.6 |
| Other revenue | 1,777.8 | 1,429.0 | 1,824.7 | 2,048.3 | 2,028.4 | 2,166.3 | 2,280.5 | 2,566.5 |
| SACU | 5,542.2 | 6,226.2 | 8,980.5 | 6,008.0 | 5,399.5 | 5,167.6 | 6,453.8 | 6,585.7 |
| Expenditure | 17,629.2 | 18,935.1 | 16,749.7 | 19,171.5 | 20,419.5 | 21,281.7 | 22,718.0 | 23,738.1 |
| Expense | 13,102.7 | 13,521.0 | 12,835.7 | 13,583.8 | 15,584.9 | 15,638.7 | 16,723.2 | 17,523.0 |
| Compensation of employees | 5,994.7 | 5,890.6 | 6,029.7 | 6,130.2 | 6,679.0 | 7,148.7 | 7,666.9 | 8,219.5 |
| Wages and salaries | 5,469.0 | 5,425.2 | 5,501.6 | 5,584.3 | 6,036.3 | 6,457.3 | 6,925.3 | 7,424.4 |
| Social contributions | 525.6 | 465.4 | 528.1 | 545.9 | 642.7 | 691.5 | 741.6 | 795.0 |
| Use of goods and services | 3,112.5 | 3,161.1 | 2,330.5 | 2,152.5 | 2,754.1 | 2,963.0 | 3,177.7 | 3,406.7 |
| Interest | 482.6 | 479.5 | 544.1 | 441.8 | 765.7 | 792.3 | 819.6 | 848.8 |
| TRANSACTIONS IN NONFINANCIAL ASSETS | 4,526.4 | 5,414.1 | 3,914.0 | 5,587.7 | 4,834.6 | 5,643.0 | 5,994.8 | 6,215.2 |
| NET LENDING/BORROWING | -1,615.5 | -2,677.4 | 1,883.0 | -1,602.1 | -1,752.8 | -2,221.1 | -1,011.5 | -268.3 |

Memorandum Items: Items

| | | | | | | | | |
|--|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Nominal GDP | 34,171.1 | 35,111.6 | 34,911.0 | 37,216.0 | 41,080.6 | 45,154.8 | 50,164.8 | 55,845.0 |
| GDP growth | -1.3 | -2.0 | -3.9 | 1.8 | 2.3 | 2.7 | 3.9 | 4.0 |
| As % of GDP | | | | | | | | |
| Taxes | 22.3 | 20.9 | 19.4 | 20.8 | 21.8 | 21.9 | 21.9 | 21.8 |
| Other revenue | 5.2 | 4.1 | 5.2 | 5.5 | 4.9 | 4.8 | 4.5 | 4.6 |
| SACU | 16.2 | 17.7 | 25.7 | 16.1 | 13.1 | 11.4 | 12.9 | 11.8 |
| Expense | 38.3 | 38.5 | 36.8 | 36.5 | 37.9 | 34.6 | 33.3 | 31.4 |
| Compensation of employees | 17.5 | 16.8 | 17.3 | 16.5 | 16.3 | 15.8 | 15.3 | 14.7 |
| Use of goods and services | 9.1 | 9.0 | 6.7 | 5.8 | 6.7 | 6.6 | 6.3 | 6.1 |
| Interest | 1.4 | 1.4 | 1.6 | 1.2 | 1.9 | 1.8 | 1.6 | 1.5 |
| TRANSACTIONS IN NONFINANCIAL ASSETS | 13.2 | 15.4 | 11.2 | 15.0 | 11.8 | 12.5 | 12.0 | 11.1 |
| NET LENDING/BORROWING | -4.7 | -7.6 | 5.4 | -4.3 | -4.3 | -4.9 | -2.0 | -0.5 |

Source: MFDPA

56. **The fiscal deficit for 2023/24 is projected to remain moderate at 5.9 percentage points of GDP and average 2.0 percentage points of GDP over the medium term.** The fiscal deficit in 2023/24 will result from expected further decline in SACU revenues. SACU revenue is expected at M5.1 billion before recovering to M6.5 billion in 2024/25. Total revenues are projected to expand to M9.8 billion in 2023/24 and average M11.5 billion over the medium term. Meanwhile, total government expenditure will grow only by 4.2 percent and average M21.3 billion in 2023/24, at the back of continued payroll audit and other Public Finance Management reforms. Recurrent spending is expected to remain muted in 2023/24 through the medium term, while investment spending is projected to increase by 16.7 percent relative to 2022/23. These reforms include restraining the wage bill, pay roll audit and other.

FINANCING AND DEBT MANAGEMENT

57. **Total public and publicly guaranteed debt stock (excl. monetary policy T-Bills) at the end of 2021/22 fiscal year was recorded at M18,938.4 million, an increase of M1,496.7 million year on year.** External debt increased by M371.5 million to a total of M15,220.3 million at the end of March 2022. At the same period domestic debt was recorded at M3,718.1 million, an increase of M1,125.2 million from the previous year. The stock of debt at current at BSP period was recorded at M19,589.1 million, an increase of M2,430.2 million year on year from the previous BSP period. The increase was shared almost equally between domestic and external debt obligations.
58. **External debt has widened by a net of M371.5 million in 2021/22 driven mainly by borrowing, disbursements and major currency exchange rates.** Gross borrowing for the year was M1,542.9 million across all currencies in the portfolio. There was an overall appreciation of M527.4 million of Rand/Loti against all those currencies except Chinese Yuan (CNY) which gained M60.1 million. The exchange rate gains combined with principal redemptions assisted to offset debt increase by M1,171.5 million. Between current and previous BSP period external debt increased by M1,256.7 million to M15,632.2 million, attributable mostly to new borrowing and currency valuation.
59. **The stock of Domestic debt at the end of March 2022 was recorded at M3.7 billion, it includes short term debt of M584.8 million and medium to long term debt of M3.1 billion.** Domestic debt increased by M1.1 billion year on year to finance budget gap. There has been a gradual increase of medium to long-term debt since 2018/19. However, observed fluctuations in the stock is typically a reflection of short-term debt movements year on year. At end of 2020/21 fiscal year all outstanding stock of short-term debt had been retired, that resulted in relatively large increase of debt year on year when T-bills were issued for 2021/22 fiscal year. In the BSP observation period domestic debt has increased by M1,173.6 million to M3.956.5 million after issuances of both short-term and long-term instruments.
60. **The confidence of the government to finance budget deficits is growing as more and more participants enter the market, which prompts a cautious approach of issuing mostly long tenured bonds.** The 2022/23 auction calendar is biased towards long term instruments, short term instruments are included to ease liquidity needs. The first bond auction of the 2022/23 has been oversubscribed and raised all the offered amount of M200 million. The assessment results of the newly conducted Debt Sustainability Analysis suggest that Lesotho's public debt is assessed to be

at moderate risk of debt distress with some space to absorb shocks. This rating implies that only a sizable shock would take the country's debt portfolio towards high risk of debt distress.

| Year | 2019/20 | 2020/21 | 2021/22 |
|--|-----------------|-----------------|-----------------|
| TOTAL DISBURSED OUTSTANDING DEBT | 18 464.2 | 17 448.6 | 18 938.4 |
| EXTERNAL DEBT | 15 651.6 | 14 848.8 | 15 220.3 |
| Bilateral | 12 23.4 | 989.2 | 956.7 |
| Export Credit (China and India) | 1 176.7 | 1 574.4 | 2 121.8 |
| Multilateral | 13 251.5 | 12 285.2 | 12 141.8 |
| DOMESTIC DEBT | 2 812.6 | 2 599.8 | 3 718.1 |
| Commercial Banks | 1 410.0 | 1 117.3 | 1 805.3 |
| Non-Bank Financial Institution & Insurance | 1 210.8 | 1 168.5 | 1 465.0 |
| Private (Individuals, Organisations and Societies) | 191.8 | 314.0 | 447.8 |
| T-Bills (Monetary Policy) | 876.8 | 875.7 | 876.6 |
| In Percentage of GDP | | | |
| Total Debt | 51.3% | 46.5% | 48.7 % |
| External Debt | 43.5% | 39.5% | 39.1 % |
| Domestic Debt | 7.8% | 6.9% | 9.6 % |
| In Percentage of Total Debt | | | |
| External Debt | 84.8% | 85.1% | 80.4% |
| Domestic Debt | 15.2% | 14.9% | 19.6% |

61. **The Medium-Term Debt Strategy remains to develop the domestic market and attain a share of 70 percent external debt to 30 percent domestic debt in the long term.** As at end March 2022, the share of external debt to domestic was recorded at 80.4 percent to 19.6 percent, a slight deterioration from the previous year after appreciation of exchange rates. The bulk of external debt stock is concessional but the level of concessionality is expected to decline in the long run, while remaining significant as Lesotho grows and graduates from some concessional borrowing openings and the domestic debt stock grow.

| | 2020/21 BSP | 2021/22 BSP | Jul 2022/23 |
|--------------------------|------------------|------------------|------------------|
| Total Public Debt | 18 244.80 | 17 158.80 | 19 589.07 |
| External Debt | 15 432.2 | 14 375.5 | 15 632.2 |
| Bilateral | 1 173.7 | 915.3 | 984.3 |
| Export Credit | 1 168.3 | 1 525.0 | 2 235.4 |
| Multilateral | 13 090.2 | 11 935.2 | 12 412.5 |
| <i>Concessional</i> | <i>82.2%</i> | <i>81.3%</i> | <i>81.4%</i> |
| <i>Non-concessional</i> | <i>17.8%</i> | <i>18.7%</i> | <i>18.6%</i> |
| Domestic Debt | 2 812.6 | 2 783.3 | 3 956.9 |
| Long term | 2 382.6 | 2 783.3 | 3 333.3 |
| Short term (T-Bills) | 430.0 | 0.0 | 623.6 |
| <i>Monetary</i> | <i>881.3</i> | <i>882.5</i> | <i>870.2</i> |

VII. RISKS TO THE ECONOMIC AND FISCAL OUTLOOK

62. **Medium term growth outlook remains resilient but dependent on fiscal saving, structural reforms, donor support, and external developments.** Growth is heavily dependent on investments from LHWP-II construction. Constant growth over the medium and long term will have to hinge on strong private sector development and successful execution of structural reforms to improve governance.
63. **Growing domestic payment arrears can cause increased costs to government:** government suppliers may adjust prices to compensate for late payments or delayed supply of inputs which may affect service delivery. A large volume of arrears may indicate several different problems, such as inadequate commitment controls, cash rationing, inadequate budgeting for contracts, under-budgeting of specific items, and lack of information.
64. **Managing fiscal revenue volatility is a serious policy challenge for Lesotho.** Over the past decade, Lesotho has faced significant revenue volatility, largely owing to highly unstable SACU receipts. A reduction in receipts typically leads to a fiscal adjustment and contraction in domestic absorption, weakening short-term economic growth, worsening fiscal and external balances while increasing government debt, and lowering international reserves.
65. **Following 2020 pandemic induced economic crisis, SACU revenues for 2023/24 are expected to significantly decline,** then followed by a sharp recovery in 2022/25 resulting from recovery in 2021 as a result of reopening of the global economy. During the 2008-09 financial crisis, SACU earnings fell significantly, and Lesotho faced significant balance of payment needs and called for IMF financial assistance under the Extended Credit Facility (ECF). *This experience highlight the importance of securing fiscal and external buffers - accumulation of international reserves or other type of precautionary savings-*, to help ensure fiscal sustainability, reduce the prospects of boom-bust cycles and support sustainable growth.

Box 2: Risks to the Baseline Macroeconomic Framework

| Time Horizon | Source of Risk | Relative - Likelihood | Impact if Realized | Implication for Fiscal Management |
|----------------------|--|-----------------------|--|---|
| Short to Medium Term | Volatile SACU Revenues | High | High The past SACU windfalls have fed higher public wages and other recurrent expenditures, which could not be brought | The fiscal outlook remains challenging and upfront consolidation is needed to sustain the external position while hurting growth and |
| Short to Medium Term | Growing Domestic Payment Arrears | High | High Efforts to restrain expenditure have also been undermined by growing domestic payments arrears and | Cost of domestic and external financing and debt servicing could increase substantially |
| Short to Medium Term | a) Rise in global interest rates and risk aversion affecting external funding costs: and (b) Inflationary pressures and Currency depreciation arising from conditions in the monetary union, possibly resulting in a policy reaction involving higher real and nominal domestic interest rates. | High | High Higher cost of domestic borrowing arising from higher interest rates. | Increase in the domestic interest payments as investors charge high interest rates to compensate for higher inflation. High external debt service costs arising from a depreciating exchange rate |

Source: MFDP

VIII. STRATEGIC PRIORITIES FOR 2023/24 – 2025/26 BUDGET

66. **By modernising the major economic sectors, social sectors, infrastructure sectors and governance sectors and by providing capacities to labour force, Lesotho will experience high economic growth that will create jobs for its citizens in a diverse range of industries.** It is, therefore, the purpose of this framework of NSDPII to set out a roadmap for achieving the rapid economic growth through adherence to the following key priority areas of sustainable development.

- Growth Progression
- Social Transformation
- Infrastructure Development
- Good Governance and Accountability

GROWTH PROGRESSION

67. **The goal of this Key Priority Areas (KPAs) is to achieve inclusive, sustainable and equitable growth and create private sector - led employment for Basotho.** The aim is to aspire to change to a knowledge-based economy. This is hoped to be achieved through structural transformation of the following productive sectors. Agriculture, Manufacturing, Mining and Tourism.

SOCIAL TRANSFORMATION

68. **The aim of this KPA is to build capable and healthy human resources.** Quality human capital is crucial to optimizing productivity and associated socioeconomic benefits to the people. Lesotho's population is undergoing a demographic transition where the age structure is changing from dominantly children to one dominated by working age population. Thus provide an opportunity for demographic dividend. Lesotho should choose to accelerate demographic transition through investment in youth, education, and health.

INFRASTRUCTURE DEVELOPMENT

69. The aim of this KPA *is to build new and expand the existing infrastructure that will help productive sectors* to achieve their goal. Strong infrastructure enables economic growth and is the bedrock for better living conditions. Energy, water, Transport, ICT and build environment are the vital forces that supports economic transformation. Sustainable investment in infrastructure needs to be prioritized and sequenced to support economic development.

GOOD GOVERNANCE AND ACCOUNTABILITY

70. The goal of this KPA is to promote good governance through effective institutions. **Good governance and responsive institutions and an engaged citizens are the fundamental principles of democracy and sustainable development.** Lesotho's economic, social, political, and environmental future rests on its ability to put people at the centre of decision making. Lesotho wants to continue to safe, peaceful and upholding the rule of law, secure, transparent and accountable and to improve the service delivery while also being at peace with other countries.

IMPLEMENTATION, MONITORING AND EVALUATION

71. **The Government of Lesotho is committed to effective service delivery to its people.** To accomplish this, the government had already adopted the prudent and accountable methodology that is result driven and performance-oriented for the benefit of all Basotho. In this regard, Big Fast Results Methodology (BFR) which has sufficient intermediate indicators that deliver quick feedback on results that can continually be improved through decision making and learning has been adopted by the government. Frequent monitoring and evaluation need to be undertaken while frequent reporting should also be done to track the progress through usage of dashboards.

IX. TRANSLATING POLICIES INTO RESOURCE ALLOCATION

72. **This BSP will be realised by introducing initiatives that will encourage the establishment and implementation of priority projects that will stimulate the economy as articulated by the NSDP II priorities.** There is an ongoing initiative on the enhancement of capacity of Ministries, Departments and Agencies (MDAs) on appraisal tools and techniques among others for better appraisal of development projects to ensure that the Public Sector Investment Programme (PSIP) contains bankable projects. There is also a concerted effort to improve the absorptive capacity of capital projects whereby the frequency of site visits coupled with progress reporting will be increased to enable taking corrective measures on time. The Government has introduced a project "Advanced Infrastructure Development for Economic Growth and Job Creation" which is meant to provide the necessary impetus for private sector-led economic growth. In addition, institutional capacity will be improved though resuscitation of sector working groups. The prerequisite studies will be done prior to implementation of development projects.

73. Currently there are 92 ongoing projects which include among others; **Wool and Mohair Promotion Project (WAMPP, M571, 824, 000)** addressing increased production and improved value chain of wool and mohair, **Small Holder Agriculture Development Project II(SADP II, M997, 920, 000)** that aims to increase productivity, improve quality and increase marketed output among programme beneficiaries in Lesotho's smallholder agriculture sector. These projects seem to be performing very well in changing lives of Basotho. The government also invested in **Private Sector Competitiveness and Economic Diversification Project (PSCEDP) – Phase II (M 397,600,000)** which aims to build on reforms initiated under the PSCEDP Phase I as well as reforms in new areas to support government priorities that would lead to greater private sector development. This will be achieved through improved business environment, greater access to finance, supporting investment promotion activities in new sectors and enhancing linkages to domestic SMEs and improved economic diversification in the economy through targeted support to new growth sectors such as horticulture and tourism that have tremendous potential to create sustainable jobs and improve livelihoods.
74. There are also 15 infrastructural projects which are on the pipeline including among others; **Construction of School of Engineering(M378, 521, 384), LCE Infrastructure Development project (Maseru and Thaba-Tseka campuses (M232, 684, 135) and Infrastructure Development at Centre for Accounting Studies (M436, 965, 518)** which are believed to have potential in job creation, **Mpilo Upgrade (M448, 982, 076)**, the construction on this projects will reduce carnage significantly and relieve traffic jams in a tremendous manner. **Mofoka to Sehlabathebe 132kV Overhead Line and Sub Station Project (M1,516,270,346)** which is meant to benefit the residents of the Kingdom of Lesotho along the project area as well as businesses and industries connected to the grid. The living and working conditions will improve as a result of access to more stable and better-quality power supply, bringing better network stability, allowing future development of the Southern region and reducing power cut events. **Upgrading of Moshoeshe 1 International Airport (M1,172,160, 000)** that will offer more job opportunities for Basotho as there will be more operations at the airport. Moreover, airlines will be attracted to use MIA resulting in more revenue for Government. This will also improve agricultural export.

FINANCIAL SECTOR DEVELOPMENT AND FINANCIAL INCLUSION TO PROMOTE PRIVATE SECTOR DEVELOPMENT AND HELP THE RECOVERY

75. **Financial sector development and access to a broad range of quality financial services for the private sector particularly the MSMEs is vital for employment and inclusive growth.** Specifically, NSDP II identified increasing financial inclusion and access to credit as priorities meant to kick start the productive sectors in the economy. A liquid, stable, competitive, and efficient inclusive finance sector is a necessary precondition for expanding agricultural production, eliminating financial constraints faced by several micro and small enterprise operators in manufacturing, tourism, and other growth sectors. Further, the provision of financial services, particularly to the excluded, would increase income in the wider economy by mobilizing savings and providing loans, which can be used to support the creation and expansion of small business in urban and rural areas.
76. **For the current BSP, the Government plans to undertake the FinScope MSMEs so as to have fresh data relating to the status of the MSMEs sector** to inform responsive policy interventions towards this sector, especially those relating to access to financing instruments. The Ministry further intends to link private sector with investment opportunities in their locality in view in

thriving the domestic real economy. Finally, Government plans to develop a financial education strategy with a clear financing model to ensure sustainability in the delivery of national financial education especially that leverage of the use of technology for the MSMEs.

ROLE OF STATE-OWNED ENTITIES

The State-owned Entities (SOEs) will continue to play pivotal role in the socio-economic development of the Lesotho's economy and need to be managed effectively and efficiently.

SOEs are required to enhance competitiveness of the economy, invest in economic infrastructure, stimulate growth, and fulfil a range of industrial policy goals. In fulfilling these key roles, there is an acknowledgement of the need to improve SOE performance through ensuring financial sustainability in operations, private competition, and **clarity over SOE mandates**. Weak governance and financial oversight monitoring may place very significant fiscal risk on the Government.

77. In the recent years a critical role of this sector has come clearly evident in the wake of the Government reforms to improve service delivery and attract new investment opportunities for growth and prosperity in pursuit of its national development Plans and strategies. This oblige the government to increase its investment in the sector and strengthen **oversight monitoring on transparency and accountability of resources allocated**.
78. **Most of the SOE special 100 percent owned by Government are subsidized from the national budget for their operations and social mandate.** The current forms and mechanisms are used to finance the SOE's operations and infrastructure depend partly on the economic and fiscal environment, as well as the rationale for state ownership (whether 100 percent or more than 50 percent direct or indirect through government entities or minority stake interest). For instance, where an entity is owned for strategic reasons and has limited non-commercial mandates it operate using its own revenues and private debt financing. By contrast, where developmental mandates form a significant part of an entity's operations it is likely that significant, recurrent transfers will be required for its operations. The current funding models for social and economic development mandates of SOEs are blurred and confusing, leading in some instances to undercapitalisation, which impedes the SOE's ability to contribute to meeting national challenges such as job creation and revenues enhancement. The model also is not transparent in terms of resources allocation as it is subject to political will than developmental needs. Based on the above the Government will continue on the SOE reforms to review its current legal frameworks to enhance SOE's support and clearly provide recommendation on SOE financing models that would be suitable for the sector to enable monitoring and transparency and also address the governance issues that also weigh heavily on SOE's performance.

SOE REFORMS CONTINUES

79. **The fragmented and incomplete understanding of the SOE sector; its value to the economy and the country; poor reporting performance; and current weak oversight and management is exacerbated by the lack of a clear SOE policy.** There is now an ideal opportunity to take stock and introduce an SOE policy that reflects GoL's needs. Government is aware of the need for a sensitive balance between the desired level of autonomy and commercial independence of SOEs on the one hand, and the need for a reasonable level of conformity and effective performance

monitoring by government on behalf of the public, as well as Parliament in its oversight role, on the other. The policy will strengthen government ownership and control to attain its socio-economic development goals.

80. **The Ministry of Finance in persuade of its mandate and the overall responsibility for the finance portfolio management that include investment portfolio**, and in particular responsible for the for fiscal and macroeconomic management policy advice and process, and review of government programs has produced the State-Owned Entity policy draft to be endorsed by Cabinet that will eventually pave the way for the development of law and regulations that will govern the sector.

The policy is premised on two key objectives to be able to address the challenges that have been alluded to above:

- to centralised *ownership* function vested in the position of Minister of Finance and all SOEs shall report to the position and
- also be a centralised *oversight* function within the Ministry of Finance.

81. **This shall ensure the separation of ownership and regulatory control**; the improvement of governance; reduction of political interference/influence; and professionalising the oversight and performance monitoring of the GoL's investments in enterprises/entities.

X. SUMMARY CONCLUSION

82. A strong economic recovery and innovative change is well underway, despite the new emerging shocks. The proposed policy actions identified in this document seek to accelerate and deepen this transformation “in pursuit of economic and institutional transformation for private sector led jobs and inclusive growth”.
83. The macro-economic and fiscal forecasts and targets included in this Budget Strategy Paper remain indicative, and hence, subject to review, taking into account developments and proposals that may arise during the 2023/24 Budget formulation process. Furthermore, the above proposals are by no means exhaustive and Ministry of Finance and Development Planning welcomes further relevant inputs from stakeholders in order to ensure an inclusive and people centered Budget.



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