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July 23, 1984

To: Members of the Executive Board

From: The Acting Secretary

Subject: Lesotho - Staff Report for the 1984 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1984 Article IV consultation with Lesotho. A draft decision appears on page 22.

This subject will be brought to the agenda for discussion on a date to be announced.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Edo (ext. (5)8750).

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INTERNATIONAL MONETARY FUND

LESOTHO

# Staff Report for the 1984 Article IV Consultation

Prepared by the Staff Representatives for the
1984 Article IV Consultation with Lesotho

Reviewed by the Committee on Article IV Consultations

Approved by Oumar B. Makalou and Eduard H. Brau

July 19, 1984

## I. Introduction

The 1984 Article IV consultation discussions with Lesotho were held in Maseru May 17-June 1, 1984. The representatives for Lesotho included the Hon. Mr. Rakhetla, Minister of Finance; the Hon. Mr. Makhele, Minister of Rural Development and Cooperatives and Minister to the Prime Minister; Mr. Waddington, Permanent Secretary of Finance; and Mr. Schoenberg, Governor of the Central Bank. The staff representatives were Messrs. Williams (head-AFR), Reichardt (AFR), Khatchadourian (BUR), Mansoor (EUR), and Ms. Eugenio (secretary-FAD). Mr. Alexander (RES) joined the mission for about one week for discussions with the authorities concerning a possible CF drawing.

## II. Background

Lesotho is a small, landlocked country of 1.4 million inhabitants, located within the geographical frontiers of the Republic of South Africa (RSA), with which it is closely linked through its membership in the Rand Monetary Area (RMA) 1/ and South African Customs Union (SACU) 2/. More than one half of the male Basotho labor force is employed in the RSA, mainly in mining, and their remittances account for over 50 percent of GNP. About two thirds of the Government's revenues come from payments from SACU.

Agriculture accounts for roughly 20 percent of GDP, though, because of the country's rugged terrain and widespread soil erosion, only about 13 percent of the total land area is suitable for crop farming. The supply of known mineral resources is also very limited. Diamonds used to be an

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1/ Comprising South Africa and Swaziland, as well as Lesotho. For background information, see Collings, F. d'A., The Rand Monetary Area, DM/83/16, February 17, 1983.

2/ Comprising Botswana, South Africa, and Swaziland, as well as Lesotho.

important export from around 1977, but declining supplies and a slump in international prices forced the closure of the major diamond mine in late 1982. The manufacturing sector accounts for only 7 percent of GDP, while services (dominated by distribution and government services) make up more than 50 percent of GDP. Less than one tenth of the resident labor force of 420,000 is employed in the modern sector, and about one half of them work for the Central Government.

During the 1970s both GDP and GNP grew at a rate of 8 percent per annum in real terms. The rapid growth reflected the impact of the expansion of miners' remittances and SACU receipts on the construction and services sectors, as well as the sharp increase in diamond production between 1977 and 1979. The termination of the construction boom, the closure of the major diamond mine, and a steep decline in agricultural production precipitated a fall in real GDP in both 1981/82 (April/March) and 1982/83 (Table 1).

The stagnation in SACU receipts led to the deceleration in the growth of government revenues in 1980/81 and 1981/82. As this was not matched by a corresponding slowdown in expenditure growth, the Government's budgetary operations shifted from a surplus, equivalent to 1.4 percent of GDP, in 1979/80 to a deficit of around 17 percent of GDP in 1981/82. Over the same period the current account of the balance of payments swung from a small surplus to a deficit of 14 percent of GDP. To aid in the financing of the growing fiscal and external deficits, the Government contracted some short-term external loans, some of which were channeled through the banking system.

In 1982/83 the Government initiated efforts to reduce the large financial imbalances. In the fiscal area, domestic revenues were increased through the introduction of a sales tax, and total expenditures were held virtually unchanged in nominal terms through a freeze on recruitment in the civil service and reduced capital outlays. With the aid of these measures, the overall fiscal deficit was reduced to 11 percent of GDP (Table 2). Credit developments in 1982/83 also reflected the restrictive policy stance, as net bank claims on the Government increased by 19 percent, compared with a rise of 147 percent in 1981/82, and credit to the private sector (including statutory boards) showed no increase after a rise of 29 percent in 1981/82 (Table 3). With regard to the balance of payments, the rate of import growth slackened somewhat, while miners' remittances increased sharply. Accordingly, the current account deficit was almost halved, to the equivalent of 7 percent of GDP, and the overall balance of payments deficit of 1981/82 was reversed (Table 4).

Lesotho's external debt outstanding rose by 45 percent in 1982/83, following drawdowns of concessionary loans of M 34 million. Debt servicing, largely related to nonconcessional loans contracted over the previous two years, represented 18 percent of total government revenues in 1982/83 or 5 percent of exports of goods and services (Table 5).

Table 1. Lesotho: Selected Economic Indicators, 1980/81-1983/84

(Percent change)

| | 1980/81 | 1981/82 | 1982/83 | 1983/84 |
|---|---|---|---|---|
| Nominal GDP | 21 | 10 | 8 | 12 |
| Nominal GNP | 19 | 19 | 23 | 16 |
| Real GDP | | | | |
| Of which: agriculture | -16 | -2 | -4 | -20 |
| manufacturing | 11 | 11 | 5 | -- |
| Real GNP | 7 | 8 | 10 | 1 |
| Domestic prices | 17 | 10 | 13 | 15 |
| Import prices | 13 | 13 | 17 | 14 |
| Employment in RSA mines 1/ | -4 | 3 | -5 | -2 |
| Miners' remittances | 17 | 33 | 42 | 18 |

Sources: Data provided by the Lesotho authorities; and staff estimates.
1/ Calendar years.

Table 2. Lesotho: Summary of Government Budgetary Operations, 1980/81-1984/85

(In millions of maloti)

| al Year 1-March) | Actuals 1980/81 | 1981/82 | 1982/83 | Est. actuals 1983/84 | Budget 1984/85 | Staff proj. 1984/85 |
|---|---|---|---|---|---|---|
| nue and grants | 125.5 | 124.8 | 144.2 | 177.4 | 276.5 | 236.6 |
| venue | 104.3 | 111.1 | 134.8 | 169.9 | 229.7 | 221.6 |
| Customs | (71.4) | (70.8) | (76.7) | (109.9) | (151.5) | (151.5) |
| Other | (32.9) | (40.3) | (58.1) | (60.0) | (78.2) | (70.1) |
| ants 1/ 2/ | 21.2 | 13.7 | 9.4 | 7.5 | 46.8 | 15.0 |
| nditure and net lending | 166.0 | 183.7 | 185.0 | 199.3 | 271.9 | 241.5 |
| current expenditure | 103.8 | 117.1 | 121.9 | 141.5 | 151.7 | 161.5 |
| Salaries | (54.9) | (60.5) | (63.5) | (66.4) | (72.0) | (72.0) |
| Interest payments | (4.2) | (8.0) | (16.1) | (19.6) | (22.0) | (22.5) |
| Other | (44.7) | (48.6) | (42.3) | (55.5) | (57.7) | (67.0) |
| pital expenditure and net lending 2/ | 62.2 | 66.6 | 63.1 | 57.8 | 120.2 | 80.0 |
| all surplus/deficit (-) | -40.5 | -58.9 | -40.8 | -21.9 | 4.9 | -4.9 |
| l financing | 40.5 | 58.9 | 40.8 | 21.9 | -4.9 | 4.9 |
| reign financing 2/ 3/ | 10.5 | 8.8 | 23.5 | 29.5 | ... | -- |
| mestic financing | 30.0 | 50.1 | 17.3 | -7.6 | ... | 4.9 |
| Bank financing 3/ | (24.4) | (37.1) | (10.5) | (-9.6) | ... | (--) |
| Other (residual) | (5.6) | (13.0) | (6.8) | (2.0) | ... | (--) |
| | | | | (As a percent of GDP) | | |
| nue and grants | 39 | 35 | 38 | 41 | 55 | 47 |
| which revenue | 32 | 31 | 35 | 39 | 46 | 44 |
| l expenditure | 51 | 52 | 48 | 46 | 55 | 48 |
| all surplus/deficit (-) | -12 | -17 | -11 | -5 | 1 | -1 |

urces: Budget estimates; and data provided by the Lesotho authorities.
Excludes grants received in kind.
Data exclude transactions financed by direct donor contributions.
Foreign financing excludes borrowing from South African banks channeled through Central Bank of Lesotho and the Lesotho Bank, which is shown as a part of domestic bank ncing. Because of differences in coverage there are discrepancies between these estimates et foreign financing and data shown in balance of payments and external public debt.

Table 3. Lesotho: Factors Affecting Changes in Money Supply, 1981-83 and 1981/82-1983/84

| | Calendar years | | | Fiscal years 1/ | | |
|---|---|---|---|---|---|---|
| | 1981 | 1982 | 1983 | 1981/82 | 1982/83 | 1983/84 |
| | | | (In millions of maloti) | | | |
| Money and quasi-money ($M_2$) 2/ | 27.8 | 40.5 | 33.8 | 34.2 | 41.5 | 25.6 |
| Money | 10.1 | 18.5 | 9.2 | 14.4 | 17.8 | 5.5 |
| Quasi-money | 17.6 | 22.0 | 24.6 | 19.8 | 23.7 | 20.1 |
| Time deposits | (9.9) | (15.5) | (9.0) | (10.6) | (16.4) | (5.5) |
| Savings deposits | (7.7) | (6.5) | (15.6) | (9.2) | (7.3) | (14.6) |
| Foreign assets (net) | -17.1 | 24.7 | 37.2 | -20.9 | 45.0 | 38.8 |
| Central Bank/LMA | -18.4 | 5.8 | 39.5 | -33.4 | 15.1 | 36.4 |
| Commercial banks | 1.0 | 21.4 | -2.6 | 13.2 | 30.1 | 2.1 |
| Rand with banks | 0.3 | -2.5 | 0.4 | -0.7 | -0.2 | 0.3 |
| Domestic credit | 45.2 | 24.6 | 1.9 | 52.1 | 12.3 | 3.5 |
| Claims on Government (net) | 28.3 | 14.3 | 2.5 | 37.1 | 9.3 | -9.6 |
| Claims on other sectors | 16.9 | 10.3 | -0.6 | 15.0 | 3.0 | 13.1 |
| | | | (In percent of opening $M_2$ level) | | | |
| Claims on Government (net) | 23.2 | 9.9 | 1.4 | 29.7 | 5.8 | -4.8 |
| Claims on other sectors | 14.4 | 7.1 | -0.3 | 12.0 | 1.9 | 6.5 |
| | | | (Percentage change) | | | |
| Deposits (nongovernment) | 21.9 | 24.9 | 15.7 | 25.1 | 22.8 | 11.8 |
| Claims on other sectors | 68.0 | 23.5 | -1.1 | 38.6 | 0.6 | 26.2 |

Source: Central Bank of Lesotho.

1/ April-March.

2/ Exclusive of rand in circulation, the amount of which is not known. Since monetary base is understated, growth rates are overstated.

Table 4. Lesotho: Balance of Payments Summary, 1980/81-1984/85

(In millions of maloti)

| | 1980/81 | 1981/82 | 1982/83 | 1983/84 Prelim. | 1984/85 Proj. |
|---|---|---|---|---|---|
| Merchandise trade | -292.3 | -387.2 | -460.6 | -543.3 | -621 |
| Exports, f.o.b. | 48.5 | 39.2 | 36.9 | 26.4 | 29 |
| Imports, f.o.b. 1/ | -340.8 | -427.0 | -497.5 | -569.7 | -650 |
| Net services | -18.9 | -22.7 | -27.1 | -30.5 | -34 |
| Factor income (net) | 217.5 | 287.7 | 407.4 | 483.5 | 532 |
| Unrequited transfers | 87.5 | 72.2 | 54.1 | 83.4 | 110 |
| Of which: official (net) | 85.8 | 70.2 | 51.6 | 80.7 | 107 |
| Current account deficit | -6.2 | -50.6 | -26.2 | -6.9 | -13 |
| Long-term capital | 29.0 | 32.0 | 32.8 | 32.6 | 37 |
| Of which: official (net) 2/ | 25.3 | 27.8 | 28.8 | 30.1 | 34 |
| Short-term capital (incl. errors and omissions) | 17.4 | 10.2 | 6.9 | -4.3 | -8 |
| Of which: official (net) 3/ | -- | 20.0 | 7.0 | -3.0 | -8 |
| Official reserves (increase -) | -40.2 | 8.4 | -13.5 | -21.4 | -16 |
| | | | (In percent of GDP) | | |
| Current account deficit | 1.9 | 14.2 | 6.8 | 1.6 | 2.6 |

Sources: Data provided by the Lesotho authorities; and staff estimates.
1/ Recorded imports adjusted for imputed customs duties.
2/ Because of differences in coverage, these estimates are not consistent with data shown in the fiscal and external debt tables.
3/ Includes government external borrowing channeled through the banking system.

Table 5. Lesotho: Outstanding Disbursed Public External Debt, 1980/81-1984/85

(In millions of maloti)

| | 1980/81 | 1981/82 | 1982/83 | 1983/84 | 1984/85 Proj. |
|---|---|---|---|---|---|
| Concessional | 33.6 | 54.3 | 93.5 | 131.0 | 151.5 |
| Bilateral sources | (1.8) | (3.1) | (3.8) | (6.6) | (16.5) |
| Multilateral sources | (31.8) | (51.2) | (89.7) | (124.4) | (135.0) |
| Export credits | 0.6 | 2.0 | 5.3 | 3.4 | 2.2 |
| Nonconcessional 1/ | 12.4 | 19.3 | 17.7 | 25.3 | 6.8 |
| Total outstanding 1/ | 46.6 | 75.6 | 116.5 | 159.7 | 160.5 |
| Debt service | 3.1 | 10.3 | 25.9 | 29.1 | 33.3 |
| Memorandum items: | | | | | |
| Debt as percent of GNP | 9 | 12 | 15 | 17 | 16 |
| Concessional | 6 | 8 | 12 | 14 | 15 |
| Nonconcessional | 3 | 4 | 3 | 3 | 1 |
| Debt service as percent of exports of goods and services | 1 | 3 | 5 | 5 | 6 |
| Debt service as percent of government revenue and grants | 2 | 8 | 18 | 16 | 14 |

Sources: Central Bank of Lesotho.

1/ Excluding external bank loans to Government that were channeled through the banking system.

The Government's attempts to stimulate growth in the agricultural sector from the mid-1970s met with little success, as production of all major crops declined steadily. This performance was related to many factors, the most important of which were the poor soil quality and the high level of mine-labor income, which made lower-paying farm work undesirable. In 1980 the Government adopted a new approach to stimulating agricultural growth with the launching of the Food for Self-Sufficiency Program (FSSP), which aimed at transforming the system of subsistence agriculture by demonstrating to farmers how the application of modern capital-intensive methods could significantly increase yields of food grains (maize, wheat, and sorghum). In essence, the FSSP offered mechanized field service to farmers in return for one half of their harvest. In the first three years, 1980/81-1982/83, the project succeeded in more than doubling yields, but too rapid expansion resulted in inefficiency of operation that greatly increased cost (almost entirely met from local resources). With tightening fiscal constraints, a review of the program was initiated in 1983/84.

Modest attempts at industrial expansion have been stymied since 1980, as many small enterprises, lured by more generous investment incentives, have closed down in Lesotho to relocate in the "homelands," which also attracted skilled Basotho with higher wages. In 1982/83 a few medium-size enterprises started production, among which was the Malothi Brewery, a M 10 million investment producing both for the domestic market and for exports.

## III. Developments in 1983/84

According to preliminary staff estimates, real GDP declined in 1983/84 by about 1.5 percent, raising the cumulative decline in the last three years to over 5 percent (Table 1). Last year's fall reflected the effects of a severe drought on agricultural output and the full-year impact of the closure of the diamond mine. The growth of real GNP slackened to about 1 percent as a result of slower growth in miners' remittances. The 1983/84 maize crop is estimated at 23,700 tons, less than one third the 1982/83 level; there was a similar decline for wheat and a much smaller one for sorghum. The sharp decline in cereal production has prompted an increase in food imports, financed in part by external food aid 1/. The rate of inflation, as measured by the average annual increase in the retail price index, rose to 15 percent in 1983/84, up from 12.5 percent in 1982/83, reflecting the higher cost of domestic agricultural commodities and the impact of the 5 percent sales tax.

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1/ The European Community (EC) has contributed M 2 million to a drought relief scheme.

Based on the preliminary data the overall government deficit for 1983/84 was reduced by nearly one half to M 22 million, equivalent to 5 percent of GDP (Table 2). Government expenditures rose by only 8 percent, about one half the rate of inflation, while revenue rose by 23 percent. Almost the entire growth in revenue came from the increase in customs duties. Current spending rose by 16 percent as a result of higher expenditures related to national security, defense, and education. Capital outlays were about 8 percent lower than in 1982/83, partly due to delays in receipts of external grants and partly reflecting the scaling down of certain projects (e.g., the government office complex). Expenditure on the FSSP was M 10 million (double the previous year's allocation), while expenditure on the construction of the new international airport was M 15 million.

During 1983/84 there was a sizable increase in disbursements of foreign concessional loans, much of which represented reimbursements for capital expenditures made in previous years. Furthermore, the Government contracted a two-year external bridging loan of M 12 million to finance expenditures related to the construction of the airport pending the receipt of the proceeds of a long-term loan from the African Development Bank. Domestic bank claims on Government fell by M 10 million reflecting repayment of a M 15 million loan from a South African bank that was channeled through the Central Bank of Lesotho and net credit expansion from the commercial banks amounting to M 5 million.

Net foreign assets rose sharply in 1983/84, but sluggish credit growth and a decline in real interest rates held the increase in the money supply to 13 percent, one half the previous year's rate. Reflecting the decline in bank claims on Government, total domestic credit increased by about 3 percent in 1983/84, about one half the rate of the previous year. Credit to the private sector increased by 26 percent, with about two thirds of this increase occurring in the first quarter of 1984.

Interest rates in Lesotho declined sharply in the first quarter of 1983, following similar movements in rates prevailing in the RSA. 1/ With the upturn in interest rates in the RSA, interest rates in Lesotho also began to rise as from the second quarter. However, through moral suasion, the Central Bank made the increase in domestic rates lag behind the corresponding increases in the RSA. By March 1984 the maximum time deposit rate and the prime lending rate in Lesotho were 4 and 4.5 percentage points lower than the corresponding rates in the RSA, compared with differentials of 3 and 2 percentage points prevailing at the end of 1982. Domestic deposit rates were also slightly below prevailing rates of inflation.

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1/ The central bank call rate declined by 4.5 percentage points (from 12.0 percent to 7.5 percent), while the maximum time deposit rate fell by 5 percentage points, the minimum lending rate by 3 percentage points, and the savings deposit rate by 1 percentage point.

Based on the partial estimates available, the merchandise trade deficit increased sharply in 1983/84, as exports continued to decline and imports rose by about 15 percent. However, this deterioration was more than offset by the growth in miners' remittances and in official transfers, with the result that the current account deficit was reduced by over two thirds to the equivalent of 2 percent of GDP. The improvement facilitated the achievement of an overall surplus of M 21 million (Table 4).

Lesotho's external public debt rose by 37 percent in 1983/84 to M 160 million, the equivalent of 17 percent of GNP. Almost all the increase in external debt represented drawdowns of concessional loans (mainly from the IDA and the African Development Bank). Debt servicing in 1983/84 was equivalent to 16 percent of total government revenues and 5 percent of exports of goods and services (Table 5).

## IV. Report on the Discussions

### 1. Development strategy

The Lesotho representatives acknowledged that despite the many and varied efforts of the last few years, progress toward economic diversification has been disappointing. They also noted that the reduction in employment opportunities for Basotho in the RSA mines and the need to reduce the import bill had given new urgency to the need for expansion in agricultural output and manufacturing. With regard to the agricultural sector, they explained that, following a comprehensive review of the sector, conducted with the assistance of the Food and Agriculture Organization, (FAO), the Government had decided to introduce changes in the major programs.

In the case of the FSSP, the strategy will now emphasize the idea that farmers must assume the primary role in the process of agricultural development. This represents a departure from the previous arrangements whereby the farmer merely offered his land, and the responsibility for production rested with the government agency, the Technical Operations Unit (TOU). Also, steps will be taken to get other government institutions concerned with agricultural credit, marketing, and extension services more involved in the program. In the modified program--which will concentrate on maize production--land preparation, weed control, and harvesting activities will be the responsibility of the farmer, who can purchase services from the FSSP Machinery Hire Unit or from private contractors. The TOU would be responsible for extension services and for the provision of a basic input package consisting of fixed quantities per acre of improved seed, fertilizer, and insect control chemicals, at subsidized prices. For the time being these packages will be imported by Co-op Lesotho (a state corporation), which will also continue to be responsible for marketing. Steps are, however, being taken to open up the marketing function to private traders. The Lesotho Agriculture Development Bank (LADE) will provide credit for assisting farmers in the purchase of planting packages and for purchase of TOU's technical services. In order to be in a better position to service the agricultural sector, LADB is in the process of opening up several branches in the rural areas. Steps are being taken to implement the provisions of the Land Tenure Act so that existing land allocations could be converted into leaseholds and used for collateral for loans from the LADB as well as from commercial banks.

The Lesotho representatives expected that the new program would be less of a drain on the budget than previously. Expenditure on the FSSP was budgeted to be M 10 million in 1984/85, about M 2 million of which represented obligations incurred in 1983/84 when the program was severely affected by the drought. The cost of the program is expected to decline to under M 5 million in 1985/86. Attempts are being made to secure donor financing of the project.

The authorities have started to give renewed emphasis to the production of fruit and vegetables, an area that is labor-intensive and has a potential for providing larger incomes than the cultivation of food grains. The main constraint is the shortage of water, recently rendered more severe by the drought. The Government has begun to rehabilitate irrigation schemes covering some 980 acres and has started building small irrigation systems to service a further 1,000 acres.

Agricultural diversification is also being pursued through the development of the livestock subsector, which now generates the larger part of cash income of the agricultural sector. At present the number of livestock in Lesotho exceeds the carrying capacity of the land, a fact that has given rise to overgrazing and erosion problems. Policy is being directed toward reducing the older stock, introducing improved varieties, and increasing wool and mohair yields. With effect from April 1984, a levy has been imposed on imports of cattle, sheep, and goats, except high quality animals for breeding purposes. Various measures, including charges for access to grazing pasture, have been introduced to encourage farmers to reduce the size of their herds, but the long tradition of pastoralism has hampered the Government's efforts so far. A program has been started to demonstrate new range management techniques suitable to the achievement of higher wool and mohair yields.

In 1980 the manufacturing sector employed 4,000 persons, or about 10 percent of wage employment in the modern sector. During the first three years of the Third Development Plan (1980/81-1984/85) between 4,000 and 4,500 jobs were created, and partial information indicates that another 1,500 manufacturing jobs were created in 1983/84. The rate of job creation falls somewhat below expectations and considerably below levels required to absorb annual increases in the labor force. The Lesotho representatives stated that the major constraints to the expansion of the manufacturing sector were the limited resource base, the shortage of technical and managerial skills, and, most important, the generous financial incentives offered by South Africa for investment in the "homelands." At present, to encourage manufacturing industry, the Lesotho National Development Corra-tion (LNDC) provides subsidized factory space, and enterprises are offered an income tax holiday of up to six years. However, investors in the "homelands" receive, in addition to the tax holidays, wage subsidies of up to 95 percent of the wage bill. Within recent times LNDC has been shifting to a more selective promotion strategy that emphasizes Lesotho's access to the European Common Market and is also working to improve the system of incentives, including extending the tax holiday from six to ten years.

2. Prices, employment, and wages policy

There is no official intervention in setting consumer prices except in the case of a few social services, such as education and health and electricity and transportation rates. The Lesotho representatives explained that during 1983 the Government had delayed adjusting electricity charges in line with increases in costs (electricity is imported from South Africa), thus creating a subsidy. A 15 percent rate increase was introduced, as from March 1, 1984, eliminating this subsidy. A small subsidy on public transportation was also eliminated in 1983/84.

The Lesotho representatives expressed concern at the economy's inability to generate sufficient jobs to absorb the 12,000-15,000 persons added to the labor force annually. The situation was being further complicated by declining employment opportunities for Basotho in the RSA mines and the Government's inability to expand employment in the public sector because of budgetary constraints. The shortage of employment opportunities had caused a marked exodus of school-leavers to the South African "homelands." It was hoped that a faster expansion of agriculture and manufacturing would significantly increase job opportunities in the medium term. In the meantime, the Government was seeking to increase the flow of external grants from donor countries in order to expand the recently established Labor Construction Unit (LCU), which provides about 1,000 jobs. The LCU is now primarily engaged in road construction, but plans are for broadening the scope of operations to include conservation projects and the construction of irrigation systems. The LCU is also planning to initiate training programs for new entrants to the labor force in skills that are still in short supply in Lesotho.

In discussing incomes policy, the representatives stated that the public sector wages were increased by 50 percent in 1980 to compensate for the rapid rate of inflation that had taken place since the previous adjustment in 1977 and to bring them closer in line with wage levels in the private sector. Since 1980, however, there had been no wage increases in the public sector (except annual increments that averaged 3.5 percent) and minimal increases in the private sector. The significant fall in real wages that had taken place over the last three years, coupled with the increase in wages of Basotho employed in the RSA mines, had now created serious pressures for wage adjustments in both the public and private sectors. In April 1984 a tripartite commission was established to make recommendations for adjustments in the system of minimum wages. The interim recommendations of this commission are now being studied by the Government. The Lesotho representatives said that in the public sector, in addition to the absolute level of wages, there was the problem of declining wage differentials between the general body of civil servants and the skilled technical and managerial grades and the excessive disparities in salaries and benefits between the staff of the parastatal organizations and the civil service. The Government has decided to tackle both issues jointly and is in the process of appointing a special commission to review the level and structure of public sector wages and make recommendations by August 1984. The Government's final decision on wage adjustments, which would be incorporated in the 1985/86 budget, would take into account the present budgetary constraints and the need to set the stage for wage restraint in the private sector. Meanwhile, the Government is considering a shift away from the present system of large awards every four or five years to one of small annual or biannual wage adjustments.

## 3. Fiscal policy

Fiscal policy for 1984/85 aims at consolidating the recent improvement in public finances. The budget, as approved by the Parliament in March 1984, introduced measures to boost domestic revenues by means of (i) an increase in the general sales tax from 5 to 6 percent, (ii) higher liquor taxes, and (iii) the introduction of user charges for technical services provided by the Government to farmers. SACU receipts were expected to rise sharply, but, in line with recommendations of an earlier Fund mission, most of the increase was to be allocated to the retirement (including prepayments) of outstanding short-term external debt. The budget provided for no wage increase in 1984/85 and no expansion in civil service personnel except for a modest expansion in the number of teachers. Capital expenditures were budgeted to increase substantially, compared to 1983/84, primarily because of decisions to accelerate the completion of the airport, resume construction work on the government office complex, and undertake a major expansion of the road program that was being largely financed by international aid agencies.

Since the budget was approved, the Government has made changes in its agricultural strategy (as described earlier) that will affect revenues from user charges and has reduced capital spending allocations. Staff projections, which were discussed with the authorities, indicate that both revenues and expenditures were projected to increase by one third, resulting in an overall deficit of about M 5 million, or 1 percent of GDP.

This compares with a budgeted surplus of M 5 million (Table 2). After making allowance for projected capital inflows and the repayment of foreign debt (including the retirement of short-term external debt anticipated in the budget), there remains a financing requirement of M 5 million to be covered by domestic financing. 1/

The Lesotho representatives noted that, following two years of very strong growth, SACU receipts were expected to fall in 1985/86 because of lower import levels in 1983 and 1984 and the abolition of the import surcharge in the RSA in February 1984. They also mentioned that the Government of South Africa had requested a renegotiation of the terms of the SACU agreement because of the increasing financial burden created by the present arrangements. In these circumstances, the Government of Lesotho was actively examining ways to increase domestic revenue and control expenditures so as to avoid renewed recourse to nonconcessional foreign borrowing. In this context, consideration is being given to increasing the sales tax on luxury items, especially motor vehicles and tobacco products, and discussions with the RSA authorities on the feasibility of imposing a tax on miners' incomes are continuing. The Lesotho representatives acknowleged that the recent extension of the South African income tax to the Basotho miners was somewhat of a setback, but thought that the low rate of tax applicable (about M 18 a year, on average) still left room for an additional levy by the Government of Lesotho. It was also pointed out that the present level of miners' earnings could accommodate such a levy without imposing a heavy burden on the miners. 2/ Steps were also being taken to increase collection of income tax arrears and to improve tax administration. To this end, the Government has decided to merge the three tax collection departments (the Commissioners of Income Tax, Sales Tax, and Inland Revenue) so as to make a more efficient use of available resources for the collection of taxes and fees.

The Lesotho representatives stressed that the control of government expenditures was the key to any sustained improvement in the public finances. Over the next few years they expected some reduction in interest payments, following the scheduled elimination of short-term external indebtedness, but wage increases and operating costs related to earlier projects, like the airport, that were not self-financing were likely to exert upward pressures on current spending. In an effort to restrain expenditure growth, the Government has begun to implement measures to eliminate subventions to certain parastatals (particularly the Hilton Hotel and the Lesotho Bus Company) and is examining ways of reducing

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1/ M 13 million, after allowance for repayment of M 8 million of foreign loans channeled through the banking system.

2/ Average mine wages are currently about M 3,500 (about US$2,850) a year and are to be increased by 14 percent as from July 1, 1984. This compares with a per capita GDP of M 310 in 1983/84.

subsidies to education and health. As for capital expenditure, the Lesotho representatives stated that, too often in the past, capital projects were initiated without sufficient consideration being given to their economic feasibility, their domestic resource requirements, and the operating costs involved. By the end of 1984/85 two major projects, the airport and the government complex, would have been completed, and the expenditure requirements of the FSSP should have declined markedly. In these circumstances, the Government intended to be extremely cautious about starting any major new programs that were not fully financed by foreign concessionary assistance. The staff noted the reference, contained in the budget, to the possible establishment of a National Television Service and urged that detailed consideration be given to its financial aspects before a decision on implementation is made.

The Lesotho representatives pointed to improvements that are being made or contemplated in the parastatal sector. Co-op Lesotho was being streamlined with a view to making it profitable, after two years of cumulative losses amounting to M 0.5 million. In February 1984 3 of its 56 outlets were closed down, and there are plans to close 9 more by September 1984. In early 1984 the Liquor Commission, a state-owned distribution outlet, was abolished, and its functions were transferred to the privately owned Maloti Mountain Brewery. Following a change in management and some staff rationalization, the Lesotho National Bus Company (LNBC) no longer requires operating subsidies, though, for the time being, debt servicing is still being met by the Central Government. In the case of the Hilton Hotel, the Government is negotiating a new agreement with potential investors with a view to eliminating the annual subsidy, which now stands at about M 1 million.

## 4. Monetary policy

The Lesotho representatives stated that the main concern in the monetary area, at present, was the lack of private sector credit demand, as a result of which much of the savings mobilized by commercial banks are held as surplus deposits in the Central Bank of Lesotho. 1/ They argued that, while these deposits were interest bearing, the lack of opportunities for the employment of funds was inhibiting bank competition for deposits. They hoped that the slack in credit demand will be short-lived and expected that improvements in the investment climate will lead to an increase in credit demand for productive purposes. In the meantime, the LNDC and Basotho Enterprise Development Corporation (BEDCO) are working, along with commercial banks, to identify some projects suitable for joint financing. Consideration is also being given to the introduction of rediscounting arrangements at the Central Bank for selected export activities.

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1/ The statutory local assets ratio of 85 percent of deposit liabilities constrains the ability of commercial banks to invest these resources abroad.

Lesotho's membership in the RMA severely limits its ability to pursue independent monetary and credit policies. Past experience has shown that the structure of interest rates in Lesotho could be 2-3 percentage points below that prevailing in the RSA without inducing sizable capital flows. Lately, however, in an effort to stimulate domestic credit demand, the Central Bank has encouraged commercial banks to hold down lending rates, at a time when corresponding rates were increasing sharply in South Africa. At present, the differential between the prime lending rate in Lesotho and the RSA is 4.5 percentage points. The mission urged the authorities to take action to trim this differential so as to reduce the incentive for capital outflows.

In late May 1984 the authorities took steps to broaden the domestic money market by increasing the stock of Treasury bills and improving their liquidity through the provision of rediscounting arrangements at the Central Bank. The Lesotho representatives stated that consideration was being given to the issue of longer-term financial assets more suited to the portfolio of institutions such as pension funds and insurance companies.

## 5. Medium-term balance of payments outlook

The Lesotho representatives expected the current account deficit of the balance of payments to increase in 1984/85, to about 2.6 percent of GDP, because of higher cereal import requirements as well as an increase in imports of capital goods related to the completion of the airport. The higher current account deficit, combined with the sizable amortization payments on short-term external debt, would reduce the overall balance of payments surplus below the 1983/84 level. Balance of payments projections to 1988/89, which were prepared by the staff and discussed with the Lesotho representatives, are presented in Table 6. The projections indicate that Lesotho's balance of payments is viable over the medium term, provided that there are no major external shocks such as a sizable reduction in the number of Basotho miners in the RSA or a revision in the SACU formula that significantly reduces Lesotho's receipts from this source. To ensure this viability, however, policies will need to be directed toward increasing domestic savings and dampening import demand, and efforts to increase the flow of concessionary assistance will need to be intensified.

In Table 6 a steady increase in merchandise exports is projected from 1984/85, bringing export value in 1988/89 close to the level attained in 1980/81. The export growth is expected to come from new enterprises that have indicated an interest in starting operations in Lesotho to exploit the country's access to the EC, as well as from ongoing efforts to expand livestock exports. Merchandise imports are projected to increase by about 11 percent a year, compared to 14 percent over the last two years. The import projection implies a small annual growth in import volume, as the annual increase in import prices (largely reflecting the price level in the RSA) is expected to decelerate from 12 percent in 1984/85 to 9 percent thereafter. Even at this restricted rate of import growth, the trade deficit would increase by about one third from 1984/85 to 1988/89.

Table 6. Lesotho: Balance of Payments Projections, 1984/85-1988/89

(In millions of maloti)

| | 1984/85 | 1985/86 | 1986/87 | 1987/88 | 1988/89 |
|---|---|---|---|---|---|
| Exports, f.o.b. | 29 | 32 | 36 | 40 | 44 |
| Imports, f.o.b. | -650 | -723 | -804 | -894 | -994 |
| Trade balance | -621 | -691 | -768 | -854 | -950 |
| Net services | -34 | -36 | -38 | -41 | -44 |
| Factor income | 532 | 600 | 671 | 751 | 839 |
| Unrequited transfers | 110 | 90 | 95 | 102 | 109 |
| Current account | -13 | -37 | -40 | -42 | -46 |
| Net capital inflow 1/ | 29 | 38 | 45 | 45 | 45 |
| Official reserves (increase -) | -16 | -1 | -5 | -3 | 1 |
| Memorandum item: | | | | | |
| Current account deficit as a proportion of GDP | 3 | 6 | 6 | 6 | 6 |

Source: Staff estimates.

1/ Includes errors and omissions.

The number of Basotho working in the RSA mines is assumed to remain constant as from 1984/85, but mine wages are projected to increase by 1 percent a year in real terms, i.e., by 12 percent in nominal terms (the average annual increase over the last four years was 3 percent in real terms). Thus miners' remittances are projected to rise at an annual rate of 12 percent. Official transfers (whose largest component, SACU grants, are assumed to remain constant) are projected to show only a modest increase from 1985/86 to 1988/89. Under these assumptions the current account deficit is projected to rise to M 46 million, or 6 percent of GDP.

Gross inflows of concessional loans from 1985/86 are projected to be somewhat lower than in 1984/85. However, net capital inflows will be sufficient to finance the current account deficits because amortization payments fall from M 25 million in 1984/85 to M 12 million in 1985/86 and M 9 million a year thereafter. The debt service projections consistent with this balance of payments scenario indicate that the debt service ratio will fall to 2 percent by 1988/89, compared with 6 percent in 1984/85 (Table 7).

Regarding exchange rate practices, the Lesotho representatives stated that the pegging of the maloti to the South African rand with full rand backing for the currency has been helpful in providing monetary discipline. This, combined with the country's liberal trade and exchange system, helps to provide a favorable climate for foreign direct investment.

Lesotho is a member of the Southern African Development Coordination Conference (SADCC), a grouping of nine regional states seeking to promote mutual cooperation and reduce the weight of the RSA in their economic relationships. Due to Lesotho's geographic location, its membership appeared, from the Lesotho representatives' viewpoint, to have only limited economic significance for the country. They welcome regional development projects and would benefit from some donor initiatives in this regard but are obliged to regard them as supplements to, rather than substitutes for, existing arrangements. Lesotho has no bilateral payments agreements.

Table 7. Lesotho: Projected Debt Service, 1984/85-1988/89

(In millions of maloti) 1/

| | 1984/85 | 1985/86 | 1986/87 | 1987/88 | 1988/89 |
|---|---|---|---|---|---|
| Currently contracted debt | | | | | |
| Amortization | 24.6 | 12.2 | 8.5 | 8.7 | 8.8 |
| Interest | 8.7 | 5.5 | 4.9 | 4.8 | 4.6 |
| Total debt service | 33.3 | 17.7 | 13.4 | 13.4 | 13.3 |
| New debt | | | | | |
| Amortization | -- | -- | -- | -- | -- |
| Interest | -- | 2.0 | 4.0 | 5.0 | 6.0 |
| Total debt service | -- | 2.0 | 4.0 | 5.0 | 6.0 |
| Total debt | | | | | |
| Amortization | 24.6 | 12.2 | 8.5 | 8.7 | 8.8 |
| Interest | 8.7 | 7.5 | 8.9 | 9.8 | 10.6 |
| Total debt service | 33.3 | 19.7 | 17.4 | 18.4 | 19.3 |
| Memorandum item: | | | | | |
| Debt service as % of exports of goods and services | 5.5 | 2.9 | 2.3 | 2.2 | 2.0 |

Source: Staff estimates.

1/ Totals may not add up due to rounding.

## V. Staff Appraisal

Lesotho has made considerable progress in reducing financial imbalances in the past few years. The overall fiscal deficit has been reduced from the equivalent of 17 percent of GDP in 1981/82 to 5 percent of GDP in 1983/84. The main factor behind this improvement was the large increase in customs revenues under the SACU formula. However, domestic revenues also increased by 50 percent from 1981/82 to 1983/84 (though they still account for only about one third of tax revenues), and government expenditure fell from the equivalent of 52 percent of GDP in 1981/82 to 46 percent of GDP in 1983/84. With regard to the balance of payments, the external current account has fallen from the equivalent of 14 percent of GDP in 1981/82 to 2 percent of GDP in 1983/84, mainly on account of the significant growth in workers' remittances and external grants. In 1984/85 a further reduction in the fiscal deficit is forecast, but the external current account deficit is expected to widen somewhat, partly because of higher food import requirements occasioned by the drought.

Developments in the real economy have not been as favorable. Real GDP has declined by 5 percent over the three years to 1983/84, and another sizable decline is expected in 1984/85. Also, the Government's efforts to promote expansion of agriculture and manufacturing, so as to provide needed employment opportunities and increase domestic incomes, have shown only limited results to date. The rate of inflation, which is heavily influenced by price trends in the RSA, rose to 15 percent in 1983/84 from an average of 11 percent in the previous two years.

Lesotho's membership in the RMA and SACU constrains its ability to pursue independent monetary and credit policies within narrow limits. In the last two years monetary developments have been generally favorable and have contributed to the reduction in financial imbalances. Since the start of 1984, however, large differentials between interest rates in Lesotho and those prevailing in the RSA have developed. In order to minimize the incentive for capital outflows, action should be taken to increase domestic interest rates to bring them more in line with rates in the RSA.

On wage policy, the Government has decided to review public sector wages in order to stem the decline in real incomes since 1980, and to correct anomalies in the civil service and between the civil service and the parastatals. The staff urges moderation in the granting of wage increases in the light of the budgetary constraint. Adjustments in the system of minimum wages are also earmarked to take effect by April 1985, at the latest. These adjustments should take into consideration the need to maintain export competitiveness so as not to jeopardize ongoing efforts at attracting investment in manufacturing.

Despite the reductions in the budgetary deficit since 1981/82, further fiscal adjustment will be required in the next few years. In 1985/86 customs revenues are expected to decline, and the Government will have to face demands for increased wages in the public sector. To contain the overall fiscal deficit, the authorities plan to increase domestic revenues through various measures, including the extension of the income tax to miners' incomes. Efforts should also be made to limit capital outlays to economically viable projects with significant foreign concessional financing.

The medium-term balance of payments outlook is viable, provided that there are no major external shocks such as a significant reduction in the number of Basotho miners in the RSA or a cut in SACU receipts and that measures are taken to control the growth of imports. Staff projections indicate that, because of the slower-than-expected growth in miners' remittances, the current account deficit is likely to increase to around 6 percent of GDP from 1985/86. Lesotho should be able to finance these deficits without recourse to foreign commercial borrowing.

Lesotho continues to maintain an exchange and trade system that is free of restrictions.

It is recommended that the next Article IV consultation with Lesotho be held on the standard 12-month cycle.

## VI. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board:

1. The Fund takes this decision in concluding the 1984 Article XIV consultation with Lesotho, in the light of the 1984 Article IV consultation with Lesotho conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. The Fund notes with satisfaction that Lesotho continues to maintain an exchange system that is free of restrictions on payments and transfers for current international transactions.

# LESOTHO - Basic Data

## Area, population, and income

| | |
|---|---|
| Area | 30,444 square kilometers |
| Population: | |
| Total (mid-1984 estimate) | 1.4 million |
| Annual growth rate | 2.3 percent |
| GDP per capita | SDR 254 |
| GNP per capita | SDR 538 |

| | 1980/81 | 1981/82 | 1982/83 | 1983/84 | 1984/85 Proj. |
|---|---|---|---|---|---|
| **National income** | (In millions of maloti) | | | | |
| GDP at current prices | 324.5 | 356.0 | 383.8 | 431.6 | 498.6 |
| GNP at current prices | 542.0 | 643.7 | 791.3 | 915.1 | 1,030.6 |
| | (Percentage change) | | | | |
| GDP at current prices | 21 | 10 | 8 | 12 | 16 |
| GNP at current prices | 19 | 19 | 23 | 16 | 13 |
| Final consumption | 20 | 24 | 18 | 18 | 15 |
| Gross domestic investment | 12 | 7 | 3 | 3 | 11 |
| GNP at 1982/83 prices | 7 | 8 | 10 | 1 | -2 |

| | 1980 | 1981 | 1982 | 1983 | 1984 Proj. |
|---|---|---|---|---|---|
| **Prices** | (Percentage change) | | | | |
| Consumer prices | 16.5 | 10.2 | 12.6 | 14.9 | 15.0 |

| | 1980/81 | 1981/82 | 1982/83 | 1983/84 | 1984/85 | 1984/85 |
|---|---|---|---|---|---|---|
| | Actuals | | | Est. actual | Budget | Staff projections |
| **Central government finances** (Fiscal year April-March) | (In millions of maloti) | | | | | |
| Revenue and grants | 125.5 | 124.8 | 144.2 | 177.4 | 276.5 | 236.6 |
| Current revenue | 104.3 | 111.1 | 134.8 | 169.9 | 229.7 | 221.6 |
| External grants | 21.2 | 13.7 | 9.4 | 7.5 | 46.8 | 15.0 |
| Total expenditure | 166.0 | 183.7 | 185.0 | 199.3 | 271.9 | 241.5 |
| Current expenditure | 103.8 | 117.1 | 121.9 | 141.5 | 151.7 | 161.5 |
| Capital expenditure and net lending | 62.2 | 66.6 | 63.1 | 57.8 | 120.2 | 80.0 |
| Overall surplus/deficit (-) | -40.5 | -58.9 | -40.8 | -21.9 | 4.9 | -4.9 |
| Overall deficit/surplus as percent of GDP | -12.5 | -16.5 | -10.6 | -5.1 | 1.0 | -1.0 |
| Overall deficit/surplus as percent of GDP before grants | -19.0 | -20.4 | -13.1 | -6.8 | 8.4 | -4.0 |

| Money and credit | 1980/81 | 1981/82 | 1982/83 | 1983/84 |
|---|---|---|---|---|
| | (In millions of maloti) | | | |
| Domestic credit | 63.58 | 111.87 | 124.21 | 127.72 |
| Government (net) | 25.22 | 62.30 | 74.34 | 64.79 |
| Private sector | 38.36 | 49.57 | 49.87 | 62.93 |
| Money and quasi-money 1/ | 124.80 | 158.97 | 200.49 | 226.12 |

| Balance of payments | 1980/81 | 1981/82 | 1982/83 | 1983/84 |
|---|---|---|---|---|
| | (In millions of SDRs) | | | |
| Exports, f.o.b. | 49.2 | 36.6 | 30.5 | 21.7 |
| Imports, f.o.b. | -345.4 | -398.3 | -410.8 | -468.9 |
| Trade balance | -296.2 | -361.7 | -380.3 | -447.2 |
| Labor income | 220.4 | 268.9 | 337.3 | 396.6 |
| Other service and income receipts | 29.9 | 32.4 | 32.5 | 37.6 |
| Service and income payments | -49.1 | -54.1 | -55.8 | -61.3 |
| Unrequited transfers | 88.7 | 67.3 | 44.7 | 68.6 |
| Current account deficit | -6.3 | -47.2 | -21.6 | -5.7 |
| Long-term capital | 29.4 | 29.8 | 27.1 | 26.8 |
| Basic balance | 23.1 | -17.4 | 5.5 | 21.1 |
| Short-term capital | 27.5 | 7.0 | -19.0 | -4.4 |
| Errors and omissions (net) | -9.8 | 2.5 | 24.7 | 0.9 |
| Overall balance | 40.8 | -7.9 | 11.2 | 17.6 |
| Current account deficit as a percentage of GD | 1.9 | 14.2 | 6.8 | 1.6 |

| External public debt | 1980/81 | 1981/82 | 1982/83 | 1983/84 | 1984/85 Projection |
|---|---|---|---|---|---|
| | (In millions of SDRs) | | | | |
| Disbursed and outstanding (end of period) | 48 | 65 | 99 | 121 | 122 |
| Debt service as percent of exports of goods and services Including the Fund | 1.0 | 2.8 | 5.3 | 5.3 | 5.5 |
| Excluding the Fund | 1.0 | 2.8 | 5.3 | 5.3 | 5.5 |

1/ Exclusive of rand in circulation, the amount of which is not known.

## Lesotho - Fund Relations
(As of end of June 1984)

(Amounts in millions of SDRs)

I. Membership status

| | | |
|---|---|---|
| (a) | Date of membership | July 25, 1968 |
| (b) | Status | Article XIV |

### (A) Financial Relations

II. General department (General Resources Account)

| | | |
|---|---|---|
| (a) | Quota | SDR 15.1 |
| (b) | Total Fund holdings of member's currency | SDR 13.9<br>91.8 percent of quota |
| (c) | Fund credit | None |
| (d) | Reserve tranche position | SDR 1.2 |
| (e) | Current operational budget | -- |
| (f) | Lending to the Fund | None |

III. Current stand-by or extended arrangement and special facilities

| | | |
|---|---|---|
| (a) | Current stand-by or extended arrangement | None |
| (b) | Previous stand-by and extended arrangements during the last 10 years | None |
| (c) | Special facilities | None |

IV. SDR Department

| | | |
|---|---|---|
| (a) | Net cumulative allocation | SDR 3.7 |
| (b) | Holdings | SDR 0.9 or 23.2 percent of net cumulative allocation |
| (c) | Current Designation Plan: | -- |

V. Administered accounts

| | | |
|---|---|---|
| (a) | Trust Fund loans | |
| | (i) Disbursed | SDR 4.9 |
| | (ii) Outstanding | SDR 4.5 |
| (b) | SFF Subsidy Account | -- |

VI. Overdue obligations to the Fund: None

VII. Lesotho has not used Fund resources to date. Preliminary discussions on use of Fund resources were held during the period November 3-18, 1983. In January 1984 the authorities notified the Fund that, in view of the difficulty in implementing certain policy measures, the Cabinet had decided not to request a stand-by arrangement in 1984/85.

On June 20, 1977 the Fund as Trustee approved Lesotho's request for a loan equivalent to SDR 4.9 million under the Trust Fund.

## (B) Nonfinancial Relations

VIII. Exchange rate arrangement: The currency of Lesotho is the maloti, which is pegged at par to South African rand.
M 1 = R 1 = US$0.7794

IX. The last Article IV consultation was held during the period April 23-May 6, 1983; Board discussion of the staff report (SM/83/155) took place on August 24, 1983, and the following decision was adopted:

1. The Fund takes this decision in concluding the 1983 Article XIV consultation with Lesotho, in the light of the 1983 Article IV consultation with Lesotho conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. The Fund notes with satisfaction that Lesotho continues to maintain an exchange system which is free of restrictions on payments and transfers for current international transactions.

Lesotho is on a 12-month consultation cycle.

X. Technical assistance

(a) From April 1982 to December 1983 the CBD has provided an advisor to the Research Department of the Central Bank. Furthermore, an advisor has been sent to Lesotho in May 1984 to assist in improving the bank inspection.

(b) FAD: none

(c) The Bureau of Statistics provided short-term technical assistance in the field of government finance statistics and in money and banking, both in 1983.

XI. Resident Representative/Advisor - None

Lesotho - Relations with the World Bank Group

As of the end of May 1984 IDA had approved 13 credits for a total of US$86.0 million, of which US$51.07 million were disbursed (by end of March 1984). These credits were provided for agricultural, educational, road, and urban development; rural water supply projects; and the financing of the Lesotho National Development Corporation.

Currently IDA has included in its lending program five additional projects totaling about US$50 million, of which three--in the fields of education, population, and health--are in an advanced stage of preparation.

IFC provided a loan and obtained equity, totaling US$0.33 million, for a quarry project.

The World Bank is participating in the Highland Water Scheme and has currently allocated US$6 million for an engineering component in 1985/86. This is a project to divert water into the Vaal Valley, South Africa's industrial heartland. At present, the first stage of a feasibility study has been completed, financed by the European Development Fund and UNDP. The total cost of the project is estimated to be about US$2.5 billion, for which financing is mainly expected from South Africa.