CENTRAL BANK OF LESOTHO

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Table of Contents

List of Tables

List of Figures

I. Introduction

During the third quarter of 2009, the global economy displayed strong signs of recovery from the recession which came as a result of the financial crisis. The International Monetary Fund's World Economic Outlook (WEO) argues that the observed recovery is mainly a reflection of strong monetary and fiscal intervention implemented in most developed countries to avert the deepening of the crisis. Thus the important question is whether the observed recovery can be sustained and take the global economy out of the recession. This is particularly important since the developing world business cycle follows that of developed countries with a lag. Notably, economies of the United States (US), Euro Area and South Africa registered positive growths during the quarter. If sustained, the recovery may imply that the domestic manufacturing sector, particularly textile and clothing sub-sector and the diamond mining may fall on the recovery path. As relates to price developments, the developed countries continue to experience falling prices. This has kept interest rates in both the US and the Euro Area markets in their lowest levels.

In Lesotho, economic developments reflected some weak signs of recovery. Data on mining production showed that the output from the mines remain weak despite the observed recovery in the price of rough diamonds. This may be due to some time lags involved before production can respond. However, the prices remain below their pre-crisis levels. On the secondary sector, the signs are still mixed. Indicators of the performance of the manufacturing sub-sector such as electricity consumption slowed down while water consumption declined. It is expected that the recovery in the textiles and clothing industry which is the largest sub-sector in the manufacturing sector will follow the demand in the US. However, the strengthening loti against the US dollar is further squeezing the profitability of the sub-sector.

The labour market conditions in the country showed some improvement. Employment in Lesotho Development Corporation (LNDC) - assisted companies rose by 4.4 per cent in September 2009 mainly due to seasonal factors as firms engage temporary workers to meet the end of the year orders. The level of employment in public sector continued to increase during the quarter under review. However, employment of Basotho in the South African mines continues to decline, though commodity prices such as gold and platinum have remained high over the period.

In line with the global developments, inflationary pressures in Lesotho seem to be abating at a slower pace. Inflation in Lesotho slowed down to 4.7 per cent in September 2009 compared with 8.1 per cent in June 2009. It is worth noting that inflation rate in Lesotho fell below that of South Africa and within the SARB target band of 3 to 6 per cent.

In the financial sector, money supply rose by 15 per cent due to the increase in domestic credit. Domestic credit was driven by the fall in government deposits with the banking system as government purchases of goods and services picked up following the constraint experienced in the previous quarter and some slow down in revenue collections.

Interest rates in Lesotho reflected mixed directions during the quarter. The key rate, the 91 day Treasury bill rate rose slightly while the prime lending and deposit rates continued to fall in line with the regional developments particularly those of South Africa.

Government budgetary operations are estimated to have registered a deficit of 20.0 per cent of quarterly Gross Domestic Product (GDP) during the quarter under review, manly due to the strong recovery in both capital and recurrent expenditures following the overcoming of capacity problems experienced during the initial period of the implementation of Integrated Financial Management Information System (IFMIS). The system replaced the old one called GOLFIS which had serious shortcomings. It is expected that expenditure will be inline with the budget. This demonstrates that expenditures that could not be undertaken in the second quarter were effected in the review period. Indeed, budgetary operations during the two quarter resulted in a combined surplus of M42.3 million.

The stock of public debt fell due to both external and domestic loans. Domestic debt fell mainly due to the maturity of the 10 year Lesotho Bank bond while external debt benefited from the appreciation of the currency. Lesotho continues to meet the Southern African Development Community (SADC) convergence criteria of 60 per cent debt to Gross Domestic Product (GDP) ratio.

The external sector registered an overall deficit of M877.1 million in the quarter under review, reflecting deterioration in the capital and financial account and the impact of the strengthening of the local currency against the major currencies. The outflow in the capital and financial account reflected mainly the government payment into the civil service pension scheme and the repayment of the maturing 10 year bond.

II. International Economic Developments

United States (US)

The US registered the first positive growth in the third quarter of 2009 after a series of contractions in the past four quarters. The real Gross Domestic Product (GDP) rose by 3.5 per cent in the quarter under review, compared with the revised contraction of 3.2 per cent observed in the previous quarter. This could be an indication that the fiscal stimulus package by the Federal Government as well as the monetary and financial policy responses to the crisis are yielding some results. The most encouraging aspect of this growth is the recovery in consumer spending, which rose by 3.4 per cent. The most significant contributor to the increase in consumer spending was spending on new cars and trucks which were, among other things, boosted by purchases under the Consumer Assistance to Recycle and Save Act of 2009 (Cash for Clunkers Program), under which tax credit was provided to encourage consumers to trade in older and less fuel efficient vehicles for new and better ones. Residential fixed investment and government spending also contributed positively to growth during the quarter. The US$8 000.00 tax credit for first time home buyers may have played a significant role in boosting residential fixed investment.

The inflation rate remained below zero during the review quarter. The consumer price index (CPI) decreased by 1.3 per cent in September 2009 compared with a fall of 1.4 per cent in the previous quarter. The decline in inflation is mainly a reflection of the impact of the recession, which has reduced price pressures among a wide range of products and services.

The unemployment rate rose to 9.8 per cent during the quarter, from 9.5 per cent in the previous quarter. The Federal Reserve Bank's Open Market Committee (FOMC) left the benchmark lending rate unchanged at 0.25 per cent during the period ending September 2009.

Table 1: Key World Economic Indicators

	Real GDP Growth		Inflation Rate		Key Interest Rate		Unemployment Rate	
	QII 09	**QIII 09**	**QII 09**	**QIII 09**	**QII 09**	**QIII 09**	**QII 09**	**QIII 09**
China	7.90	8.90	-1.70	-0.80	5.31	5.31	9.20_{2008}	9.20_{2008}
Euro Area	-4.80	1.50	-0.10	-0.30	1.00	1.00	9.40	9.70
India	6.10	N/A	9.30	11.60	4.75	4.75	9.10_{2008}	9.10_{2008}
Japan	-7.20	4.80	-1.80	-2.20	0.10	0.10	5.40	5.30
South Africa	-2.80	0.9	6.90	6.1	7.50	7.00	23.60	24.50
United States	-3.20	3.50	-1.40	-1.30	0.25	0.25	9.50	9.80

Source: Bloomberg, The Economist, STATSSA and SARB

*Real GDP growth rates (measured as the annualised percentage change on previous quarter) are shown for all countries except China and India for which year-on year growth rates are provided because their Governments do not publish the former.

Euro-zone[1]

The Euro-zone economy also recovered during the review quarter with real GDP increasing by 1.5 per cent compared with a contraction of 4.8 per cent in the previous quarter. Germany (Europe's largest economy) grew by 2.9 per cent, while Italy and France expanded by 2.4 and 1.1 per cent respectively. In addition, on a monthly basis, industrial production rose by 0.2 per cent and 0.9 per cent in July and August 2009, respectively, signalling that the Euro-zone economy is recovering from recession.

The harmonised unemployment rate in the Euro-zone increased from 9.4 per cent in June 2009 to 9.7 per cent in September 2009. Deflation continued in the Euro-zone during the review quarter. Inflation, measured by changes in the Harmonised Index of Consumer Prices (HICP), declined by 0.3 per cent at the end of the third quarter compared with a fall of 0.1 per cent in June 2009. The observed deflation during the review quarter was mainly a result of the

[1] Euro-zone: Austria, Belgium, Cyprus, Germany, Greece, Finland, France, Ireland, Italy, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia and Spain. Slovakia became the 16th Euro-zone member country with effect from the 1st of January.

effect of the strengthening Euro (against the US dollar) on US dollar priced imports. The Euro's surge reduced the cost of US dollar priced imports especially in the Euro-zone.

The European Central Bank (ECB) maintained its benchmark lending rate at the third quarter's level of 1.0 per cent. At this low level, interests rates are expected to stimulate economic activity in the region.

South Africa (SA)

The SA economy recovered during the review quarter. Real GDP increased by an annualised rate of 0.9 per cent in the third quarter following a decline of 2.8 per cent in the second quarter mainly as a result of the recovery in the manufacturing industry, general government services, construction industry and personal services, which contributed 1.1 per cent, 0.7 per cent, 0.2 per cent and 0.2 per cent respectively. In addition, manufacturing production increased by a seasonally adjusted quarterly rate of 2.6 per cent in the third quarter compared with a decrease of 3.0 per cent in the previous quarter. This rebound was mainly a result of higher production in iron, steel and non-ferrous metal products. Production of machinery, motor vehicles, parts and accessories also contributed to the observed increase. A much stronger rebound was offset by decreases in furniture, wood and wood products.

Inflation, measured by CPI, declined in September 2009. The CPI increased at a lower rate of 6.1 per cent compared with 6.9 per cent in June. The main factor behind this deceleration was the slowdown in food price increases. In light of the weak economic performance and abating inflation, the South African Reserve Bank's (SARB) Monetary Policy Committee (MPC) reduced the repo rate to 7.0 per cent at the end of the review quarter, from 7.5 per cent at the end of the previous quarter.

Emerging Asian Markets and Japan

China

Preliminary estimates indicate that GDP growth in the world's fourth largest economy, China, accelerated to 8.9 per cent in the third quarter of 2009 compared with 7.9 per cent in the previous quarter. The acceleration was a result of the impact of the fiscal stimulus on investment and the increase in credit availability due to low interest rates.

China's inflation rate fell further by 0.8 per cent in September, compared with a decline of 1.7 per cent in June. Inflation in China has been slowing down since February 2009, mainly on account of the continued deceleration in food prices. The People's Bank of China (PBC) kept the one-year benchmark lending rate at 5.3 per cent during the period ending September 2009.

Japan

Japan's economy grew by 4.8 per cent in the third quarter, supported mainly by a 3.3 per cent increase in domestic demand. In addition, the leading indicator of economic performance in Japan, industrial production, rose by 1.4 per cent in September. Household spending also increased during the same period.

Japan recorded an unemployment rate of 5.3 per cent in September compared with 5.4 per cent in June. The core CPI, which excludes prices of fruits, vegetables and fish, declined by 2.2

per cent in September compared with 1.8 per cent in June 2009. The Bank of Japan (BOJ) left its key interest rate unchanged at 0.1 per cent in the quarter ending September 2009. The key interest rate has been at this level since December 2008.

India

India's major economic indicators signalled that economic growth may have expanded in the third quarter of 2009. Industrial production registered monthly growths of 7.2 per cent and 10.4 per cent in July and August 2009 respectively compared with an increase of 7.8 per cent in June. This was largely driven by both the mining and manufacturing sectors. Manufacturing sector accounts for two-thirds of industrial production. This performance indicates that India's economy is responding positively to stimulus measures such as the reduction in interest rates, tax cuts and the increase in government spending.

The preliminary estimates indicated that India's inflation accelerated to 11.6 per cent in September 2009 from 8.6 per cent in June 2009. The acceleration was largely driven by the rise in prices of manufactured products, fuel and power. The Reserve Bank of India maintained the repo rate at 4.75 per cent in September in order to maintain an accommodative monetary stance until robust signs of recovery emerge.

Implications on Lesotho's Economy

The global economic conditions have improved, indicating that the global economic recovery has started. The recovery seems to reflect the impact of fiscal stimulus packages implemented to ameliorate the adverse direct and second round effects of the financial crisis. The rebound in consumer spending in the US is a welcome development for the textiles and clothing sub-sector in Lesotho, which has been hit very hard by the global recession. Nevertheless, consumer spending should gain more strength, not only in the US but also in SA to have a significant impact on Lesotho's textiles and clothing sub-sector. Retrenchments of workers in the sub-sector are expected to continue in the coming months.

Commodity Prices

Overview

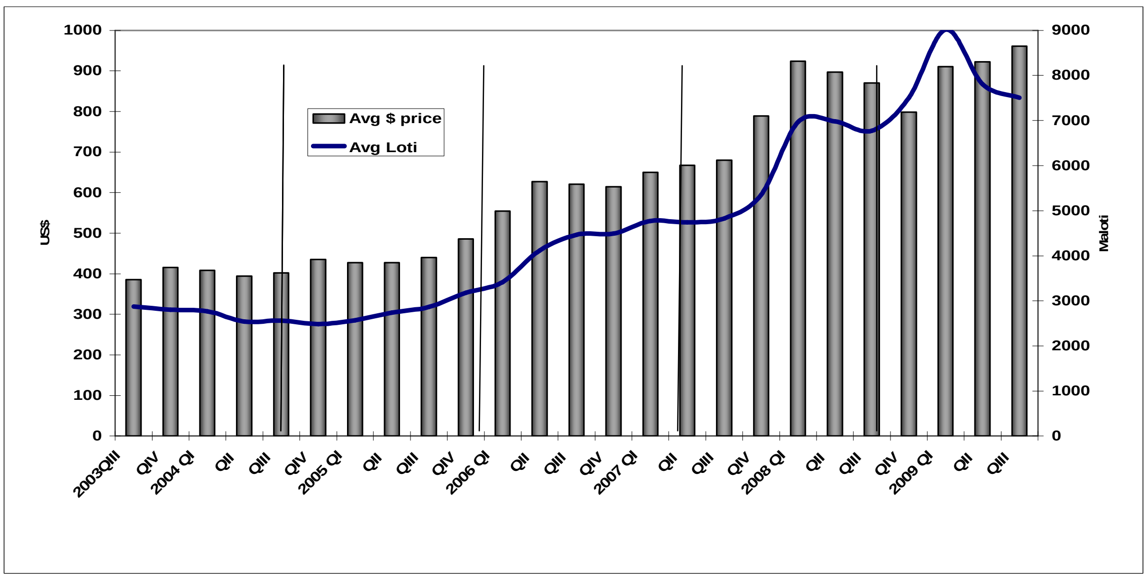
The US dollar prices of gold and platinum continued on an upward trend during the quarter under review as a result of increased financial investment in commodity assets, fuelled by the improvement in investor sentiment as well as the depreciation of the US dollar against other currencies. However, in Rand terms, the prices of these minerals declined on account of the appreciation of the Rand against the US dollar. The international price of oil also rose in response to the rebound in demand in Asian economies, especially China. The price of oil rose in Rand terms as well, indicating that the appreciation of the Rand was not strong enough to counteract the US dollar price increase. With regard to food commodities, prices declined both in US dollar and Rand terms and this is attributable to generally stable weather conditions in food producing countries. Another factor that has affected the price of maize is the fall in demand for production of ethanol on account of the decline in oil prices until the second quarter of 2009. This impact is expected to abate soon as the price of oil has started to rise.

Mineral Products

Gold

The average price of gold grew by 4.2 per cent from US$922.2 per ounce in the second quarter to US$960.88 during the review quarter. This compares with an increase of 13.9 per cent recorded in the previous quarter. However, in Rand terms, the average price of gold continued to fall by 3.9 per cent from R7 808.3 per ounce in the previous quarter to R7 504.5 in review period, following a decline of 13.4 per cent in the previous quarter.

Figure 1: Average Price of Gold

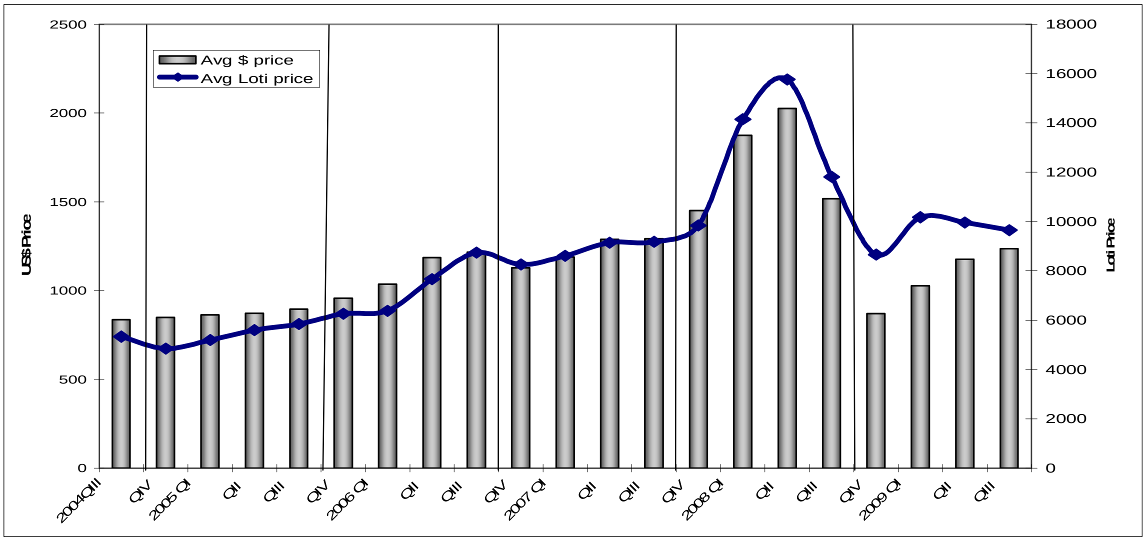


Source: Bloomberg

Platinum

The average price of platinum rose to US$1235.6 per ounce in the review period from US$1176.6 per ounce registered in the previous quarter due to, among other factors, the increase in demand in the Asian market. In Rand terms, the average price of platinum dropped by 3.1 per cent from R9962.4 per ounce in the last quarter to R9650.5 during the review quarter.

Figure 2: Average Price of Platinum



Source: Bloomberg

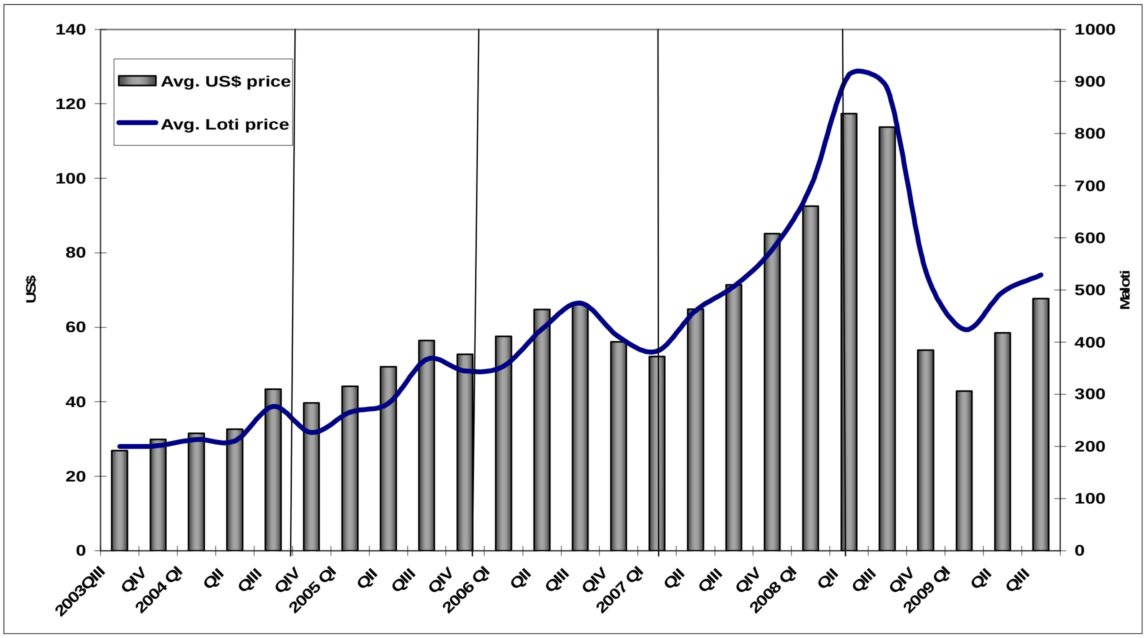
The increase in the international prices of gold and platinum is an encouraging development for the mining sector in SA. However, the appreciation of the SA Rand against the US dollar reduces the benefits of the dollar price increase to mining companies. This could compel SA mining companies to continue with retrenchments, thereby minimising the chances of any significant increase in the number of Basotho migrant mineworkers and hence remittances to Lesotho.

Oil

During the quarter under review, the average price of crude oil maintained an upward movement. The average price of crude oil rose from US$58.6 per barrel in the second quarter to US$67.7 per barrel in the review quarter, representing a quarterly increase of 15.6 per cent. In Maloti terms, the price of crude oil increased from M495.9 per barrel during the third quarter to M528.7 per barrel in the previous quarter.

In line with the increase in crude oil prices, the domestic prices of petroleum products rose during the quarter under review. The pump prices of petrol, diesel and illuminating paraffin closed the review quarter at M7.15, M7.30 and M4.90 respectively. These compare with end of second quarter prices of M6.45, M6.55 and M4.30 for petrol, diesel and illuminating paraffin, respectively.

Figure 3: Average Price of Oil



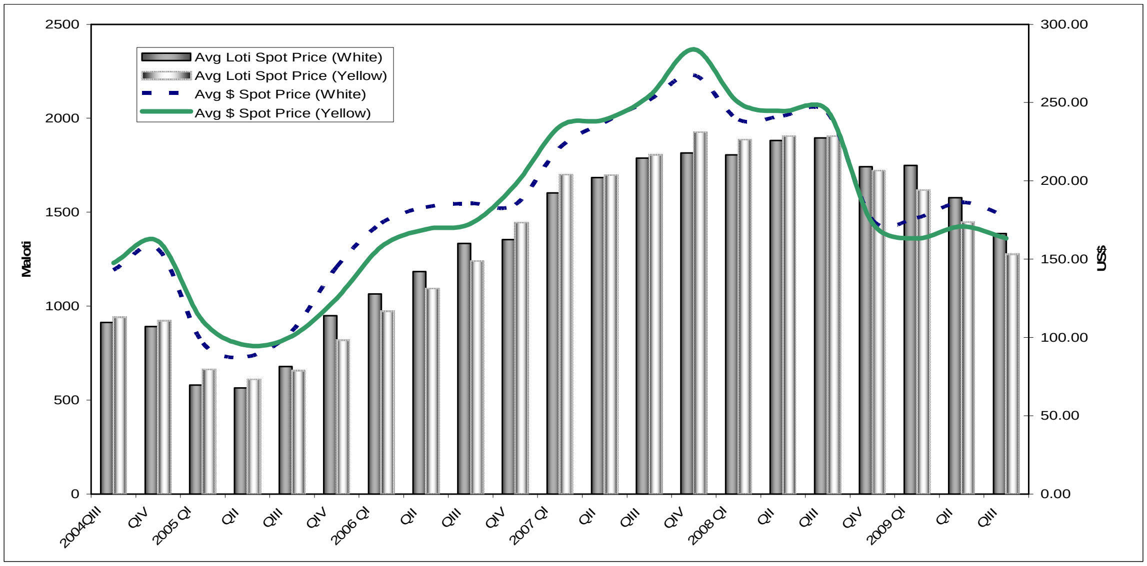
Source: Bloomberg

Agricultural Products

Maize

The average spot prices of white and yellow maize declined by 4.8 per cent and 4.4 per cent respectively during the third quarter. The average spot price of white maize fell from US$186.3 per tonne to US$177.4 per tonne while that of yellow maize declined from S$170.8 per tonne to US$163.3. The prices of both white and yellow maize declined in Maloti terms as well. The average spot price of white maize fell from M1577.3 per tonne in the previous quarter to M1385.2 per tonne in the third quarter and that of yellow maize decreased from M2073.6 per tonne to M1610.5 per tonne.

Figure 4: Average Spot Prices of Maize

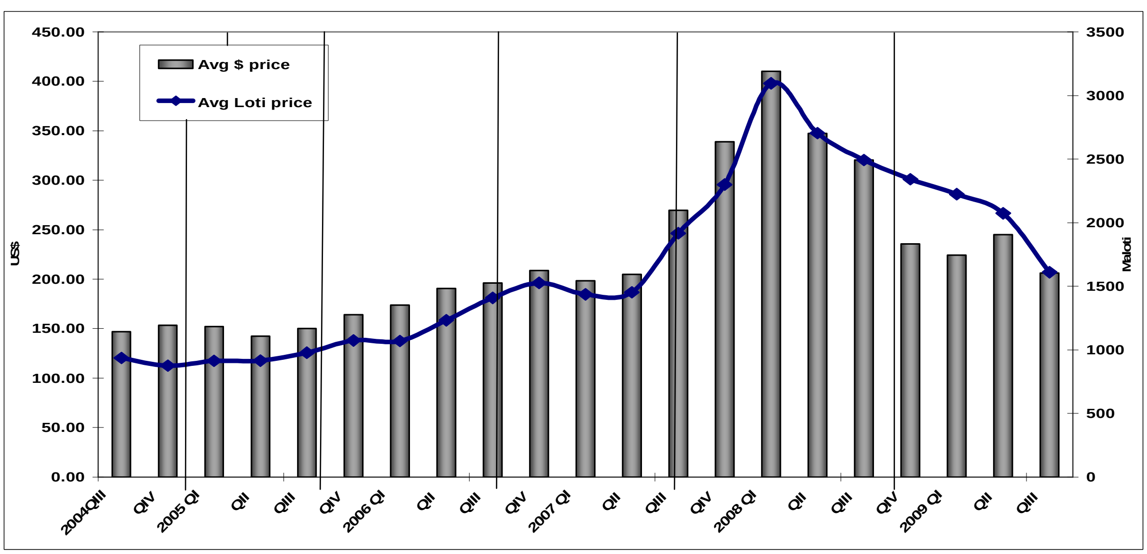


Source: South African Futures Exchange (SAFEX)

Wheat

During the quarter under review, the average spot price of wheat fell by 15.8 per cent to US$206.2 per tonne in contrast with an increase of 9.1 per cent recorded in the previous quarter. In Maloti terms, the average spot price of wheat dropped by 22.3 per cent from M2073.6 per tonne registered in the previous quarter to M1610.5 per tonne in the review period.

Figure 5: Average Spot Prices of Wheat



Source: South African Futures Exchange (SAFEX)

III. Real Sector, Employment and Price Developments

Overview

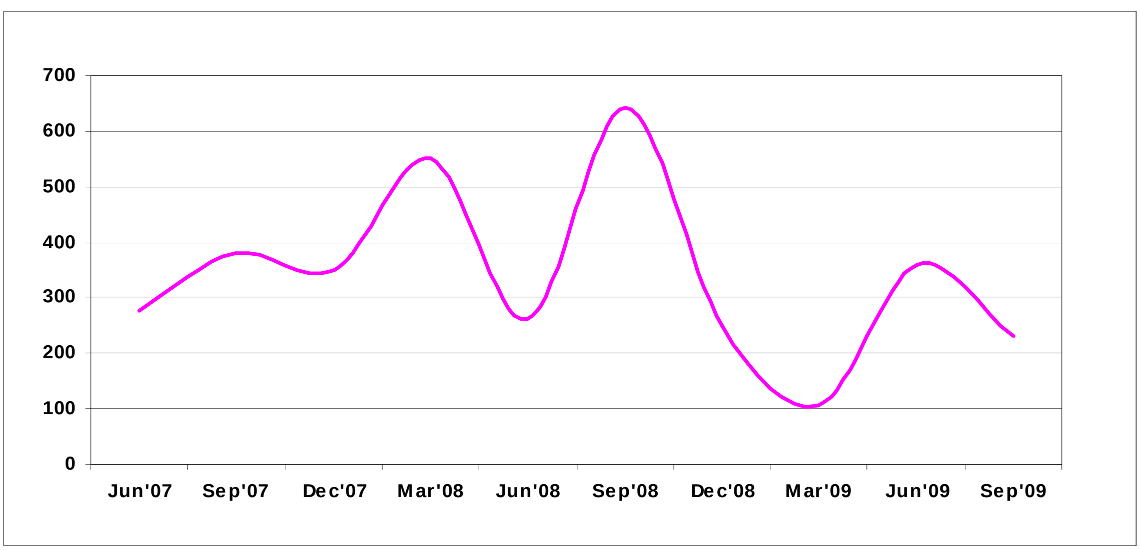
Overall, domestic economic activity showed some mixed signs of developments in the period under review. The primary sector slowed down, especially due to deterioration in the mining sector. The secondary sector, mainly consisting of the utilities' sector showed weakness in the water sector while the electricity sector grew. There were also mixed developments in the tertiary sector with business activity exhibiting a rebound while the telecommunications sector remained under stress.

Primary Sector Developments

The diamond production index declined from 357.7 points during the second quarter to 230.8 points in the period ending in September 2009. The diamond market continued to improve during the quarter, but prices remain below their levels before the financial crisis. The crisis had negatively affected the prices of commodities including the price of rough diamonds, especially in the last quarter of 2008 and early 2009. It is expected that if the recovery in the global economy is sustained the diamond production in Lesotho will follow, particularly the re-opening of the mines that suspended their operations.

Figure 6: Diamond Production Index

(2005: QI=100)



Source: Department of Mines and Geology

Secondary Sector Developments

Electricity Consumption

Electricity consumption increased by 8.9 per cent during the quarter under review compared with 17.0 per cent recorded in the previous quarter. The slowdown in electricity consumption reflects the end of winter months which are mainly in the second quarter. On annual basis, electricity consumption rose by 4.8 per cent. The performance of the sub-sectors reflects some modest performance observed in the manufacturing sectors during the quarter. Significant improvements were observed mainly in 'general purpose' and, 'commercial and industrial' categories. This may be reflective of the rebound in manufacturing sub sector even though it may still be reeling under the impact of the U.S recession.

Table 2: Electricity Consumption
(Million Maloti)

	2008		2009					
	QIV		QI		QII		QIII	
	Kwh	Value	Kwh	Value	Kwh	Value	Kwh	Value
General Purpose	19.50	12.82	20.24	13.70	21.84	15.63	31.67	19.36
Domestic	36.12	21.51	38.49	23.58	45.04	29.20	45.39	31.37
Commercial & Industrial	69.33	31.92	65.60	32.92	78.60	37.53	81.38	38.60
Total	124.96	66.25	124.34	69.19	145.48	82.37	158.44	89.33

Source: Lesotho Electricity Authority and Lesotho Electricity Company

Water Consumption

Overall, water consumption declined by a seasonally adjusted 34.5 per cent in the third quarter of 2009, compared with 11.9 per cent increase observed in the previous quarter. On an annual basis, total water consumption declined by 14.6 per cent. The fall in total water consumption, both on a quarterly basis and annual basis, respectively, is in line with the fall in industrial water consumption. Consumption of water by industrial category is an indicator of activities in the 'wet' industries. The decline in the value of units of water consumed by this sub sector may be reflective of the continued strain in the manufacturing industry as firms are trying to recover from the impact of global economic downturn.

Table 3 : **Water Consumption**

(Units in Million kilo-litres; value in Million Maloti)

		Domestic	Industrial	Other	Total
2008					
III	Units	0.87	1.46	0.55	2.88
	Value	5.67	8.67	3.77	17.53
	Units*		1.39		2.74
IV	Units	0.76	1.23	0.53	2.52
	Value	4.97	8.03	4.22	17.22
	Units*		1.11		2.27
2009					
I	Units	0.92	1.18	0.56	2.66
	Value	3.68	7.55	3.37	14.60
	Units*		1.38		3.11
II	Units	0.87	2.00	0.65	3.52
	Value	3.65	8.75	3.71	16.11
	Units*		2.03		3.57
III	Units	0.88	1.01	0.57	2.46
	Value	3.85	8.04	3.44	15.33
	Units*		0.96		2.34

Source: Water and Sewerage Authority
*denotes seasonally adjusted figures

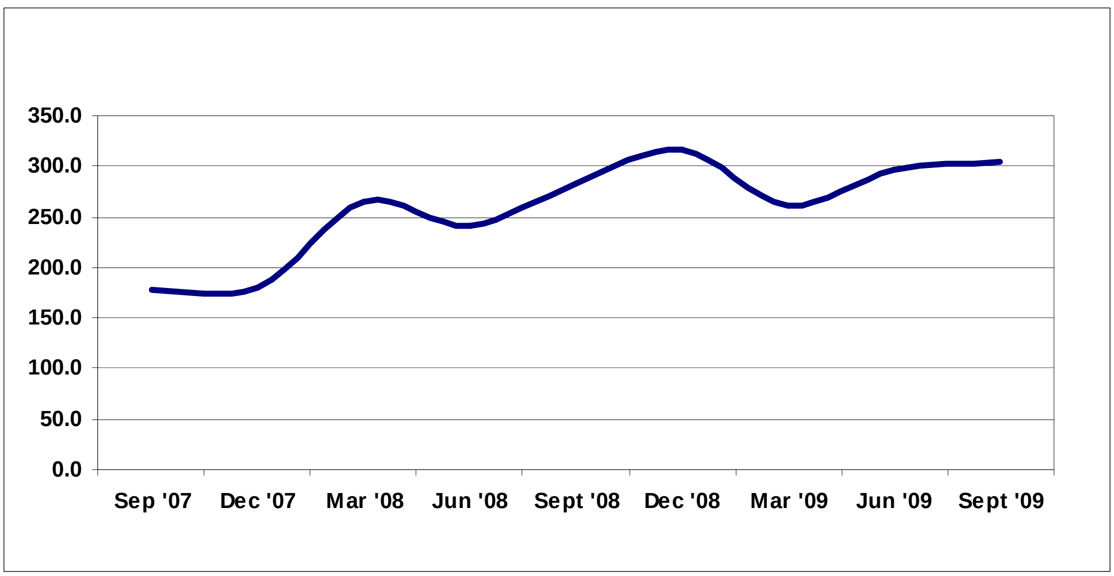
Tertiary Sector Developments

Sales Turnover

The value of sales turnover increased by 2.8 per cent and 7.5 per cent in the third quarter of 2009 on quarterly and annual bases, respectively. The increase of the value of sales turnover, quarter to quarter, is in contrast to a decline of 17.5 per cent in the second quarter of 2009. The sales turnover is an indicator of the business activity in the economy. The increase may be indicative of the improvement in consumer demand in the country.

Figure 7: Value of Sales Turnover

(Million Maloti)



Source: Lesotho Revenue Authority

Telephone Statistics

The total number of telephone calls declined further by 6.1 per cent in the quarter ending in September 2009, from a decline of 9.4 per cent in the previous quarter. The sub-sector continued to reflect the impact of the global recession on Lesotho's economy. The general slowdown in international trade, coupled with the continued job losses, is negatively affecting the telecommunications sub-sector. However, the sector is expected to recover following the positive signs of recovery observed in South Africa

Table 4: Telephone Traffic Statistics

		SA Outgoing Calls	International Calls	Total Calls
2008				
III	No. of calls (millions)	2.58	0.17	2.75
	No. of calls*			2.49
	Total Duration (million minutes)	4.15	0.57	4.72
	Nominal Value (million maloti)	9.54	4.49	14.03
IV	No. of calls (millions)	2.02	0.12	2.14
	No. of calls*			2.16
	Total Duration (million minutes)	3.41	0.39	3.8
	Nominal Value (million maloti)	7.85	2.69	10.54
2009				
I	No. of calls (millions)	2.09	0.12	2.21
	No. of calls*			2.35
	Total Duration (million minutes)	3.51	0.42	3.92
	Nominal Value (million maloti)	8.06	3.13	11.19
II	No. of calls (millions)	1.95	0.11	2.06
	No. of calls*			2.13
	Total Duration (million minutes)	3.39	0.36	3.75
	Nominal Value (million maloti)	7.79	2.57	10.36
III	No. of calls (millions)	2.09	0.11	2.21
	No. of calls*			2.00
	Total Duration (million minutes)	3.67	0.37	4.04
	Nominal Value (million maloti)	8.44	2.58	11.02

Source: Tele-Com Lesotho and Vodacom Lesotho
* Adjusted for seasonality.

Investment Expenditure

Imported Motor Vehicles

During the quarter, the number of imported motor vehicles decreased by a seasonally adjusted 16.3 per cent following an increase of 10.0 per cent in the previous quarter. On annual basis the number of imported motor vehicles declined by 41.0 per cent during the quarter. The decline in the number of imported motor vehicles was mainly driven by the fall in 'Vans', 'Trucks' and 'Buses' categories. These categories rose significantly in the last quarter driven mainly by commencement of a number of construction projects including a new hospital and main south one road.

Table 5 : Motor Vehicle Imports

(Value in Million Maloti)

		Cars	Vans	Trucks	Buses	Tractors	M/ Cycles	Trailers	Total
2008									
III	Value	37.96	138.49	18.34	25.57	1.57	0.11	1.065	223.11
	Units*								1220.46
	Units	455	736	34	75	17	4	20	1341
IV	Value	27.44	56.16	18.92	15.60	0.92	1.44	1.16	243.30
	Units*								816.70
	Units	269	314	32	68	13	16	9	729
2009									
I	Value	36.80	59.16	20.54	10.72	1.37	0.06	2.80	131.45
	Units*								781.71
	Units	385	340	34	46	5	3	18	831

II	Value	28.96	66.18	65.95	12.48	0.15	0.09	2.40	176.21
	Units *								859.81
	Units	317	354	84	42	4	1	11	813
III	Value	29.46	58.05	18.90	4.77	0.53	0.01	0.91	112.62
	Units *								719.90
	Units	374	329	42	20	11	1	14	791

Source: Avis Fleet Services Lesotho and LRA

*denotes seasonally adjusted figures
+Includes imports of second hand cars

Employment Developments

Employment by LNDC-assisted companies increased by 4.4 per cent in the third quarter of 2009 compared with a decline of 5.4 per cent in the previous period. On an annual basis, the number of people employed in the manufacturing sector declined by 4.1 per cent. The quarterly increase may be attributable to seasonal factors as manufacturing companies employ more temporary workers to meet the orders for Christmas.

The employment in the manufacturing sector has been mostly hit by the current global recession due to the strong linkage with the developed countries, particularly the US. It is expected that the employment in LNDC assisted companies would remain under pressure until full economic recovery is attained.

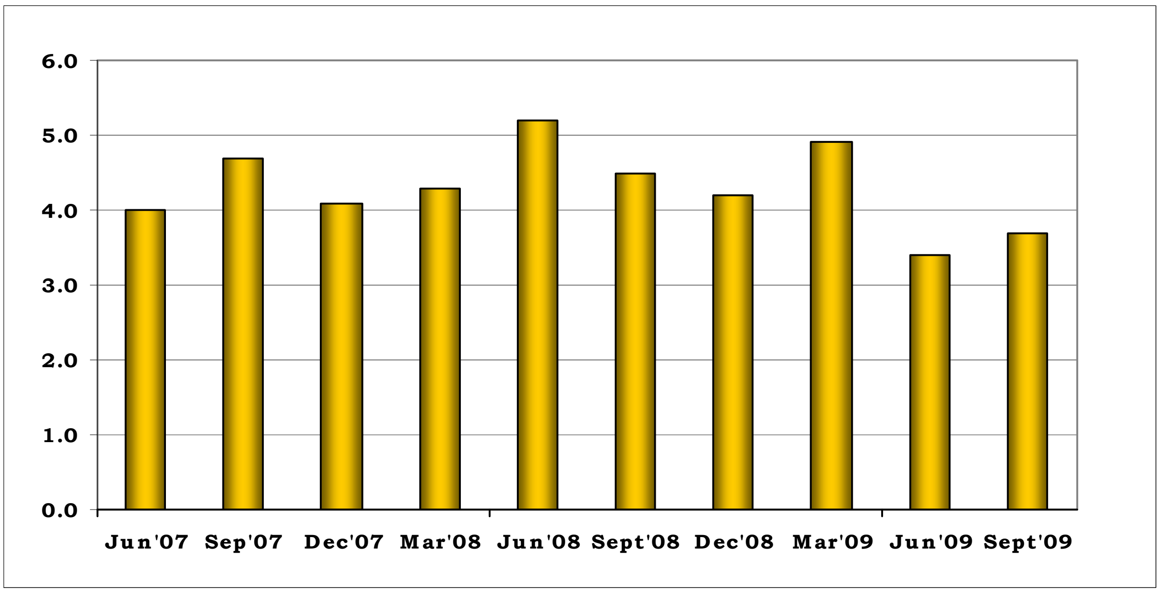
Table 6: Employment Trend of LNDC-Assisted Companies

Period	QI	QII	QIII	QIV
2009	44665	44689	46647	
2008	45650	45549	48621	47204
2007	47731	49392	46772	46633
2006	40459	45140	46189	47462
2005	41985	40111	39597	43131
2004	52532	53525	52922	50607
2003	43525	46960	49862	51187
2002	36906	39255	42011	43773

Source: Lesotho National Development Corporation

Figure 8: **Government Employment**

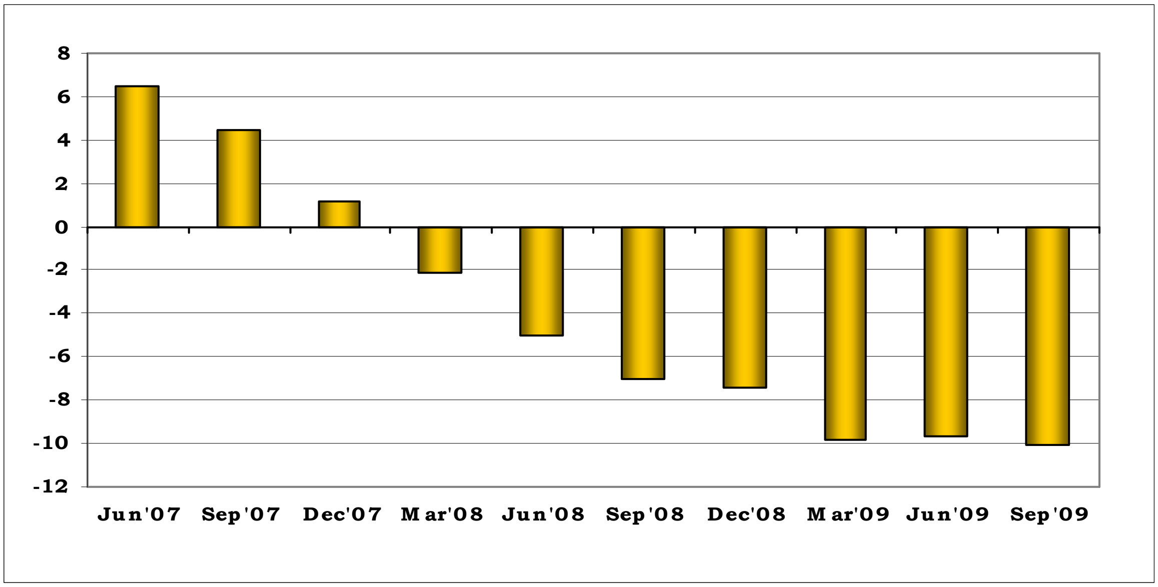
(Annual Percentage Change)



The number of government employees rose modestly by 0.9 per cent during the quarter compared with 0.8 per cent in the second quarter. On annual basis, the number of government employees rose by 3.7 per cent. The continued increase in the number of government employees is mainly due to the number of teachers reflecting the staffing of new schools that were completed at the end of 2008.

Figure 9: **Migrant Mineworkers Employment**

(Annual Percentage Change)



The number of migrant mineworkers declined further by 2.3 per cent in the third quarter of 2009 compared with 2.8 per cent in the previous period. The mining sector in South Africa, the largest employer of Basotho, has been under considerable pressure since the last quarter of 2008. Although the prices of gold and platinum have remained relatively strong in the review period, the long term trend of mineworker's employment has been downward. In Rand terms, the price of gold declined in the third quarter squeezing the companies' profits and revenue and continuing the stress of the labour market. Most mining companies continued to shed jobs, thus presenting a challenge to the employment picture of Lesotho labour market due to close labour market linkages between SA and Lesotho.

Price Developments

The rate of inflation registered 4.7 per cent for the quarter ending September 2009. This is lower than the 8.1 per cent recorded for the quarter ending June 2009. The decrease was driven mainly by the following categories: "food and non-alcoholic beverages' at 4.6 per cent compared with 11.1 per cent recorded in the previous quarter, "housing, electricity, gas and other fuels" at -5.6 per cent compared with 0.1 per cent registered in the previous quarter and "Leisure, entertainment and culture" at 4.7 per cent compared with 7.3 per cent in the previous quarter. Since August 2009, Lesotho's inflation rate was lower than the South African inflation rate which stood at 6.1 per cent in the quarter under review. Lesotho's inflation rate fell within the SA targeted band of 3-6 per cent in the last two months of the third quarter.

Table 7: Inflation Rate

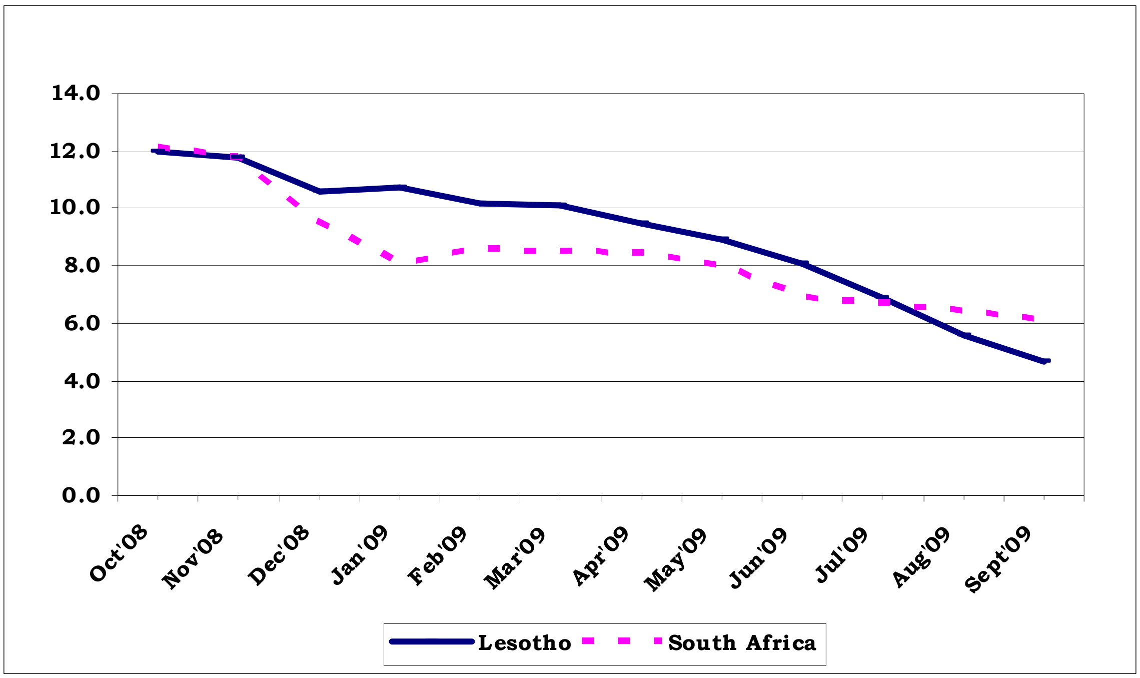
(Annualised Percentage Change: April 1997=100)

	Weight	2009				
		May	Jun	July	Aug	Sept
All items	100.0	8.9	8.1	6.9	5.6	4.7
Food and non-alcoholic beverages	39.8	12.1	11.1	8.9	6.7	4.6
Alcoholic beverages & Tobacco	6.4	6.5	6.1	6.0	6.8	8.8
Clothing & footwear	15.6	6.0	6.1	5.1	5.1	5.4
Housing, electricity gas & other fuels	3.7	3.5	0.1	-2.9	-4.7	-5.6
Furniture, households equipment & routine maintenance of house	17.0	7.4	6.7	6.7	6.1	5.6
Health	1.4	1.5	1.6	1.7	1.5	1.9
Transport	7.8	4.4	3.9	5.3	3.9	4.5
Communication	0.1	0.0	0.0	0.0	0.0	0.0
Leisure, entertainment & Culture	1.2	7.3	7.3	7.8	4.9	4.7
Education	3.2	3.0	3.0	2.9	2.4	2.2
Restaurant & Hotels	0.4	7.6	8.0	9.6	9.0	8.2
Miscellaneous goods & services	3.2	7.2	6.8	6.5	6.6	6.4

Source: Bureau of Statistics, Lesotho

Figure 10: Annual Inflation Rate for Urban Households

(Percent)



IV. Monetary and Financial Developments

Determinants of Money Supply

During the quarter ended September 2009, money supply showed an increase of 15.0 per cent, compared with a decline of 1.0 per cent in the second quarter of 2009. The growth in money supply in September was the largest quarterly increase this year, given that it grew by 12.1 per cent in March. On annual basis, broad money grew by 42.3 per cent in the third quarter of 2009, against an increase of 14.3 percent the preceding quarter.

The expansion in money supply in the review period was mainly driven by a strong increase in total domestic credit. The rise in domestic credit reflected a jump in net claims on government, and to a lesser extent, an increase in private sector credit. Net foreign assets of the banking system grew slightly during the third quarter.

Figure 11: Overview of Recent Monetary Developments

(Million Maloti: End of Period)

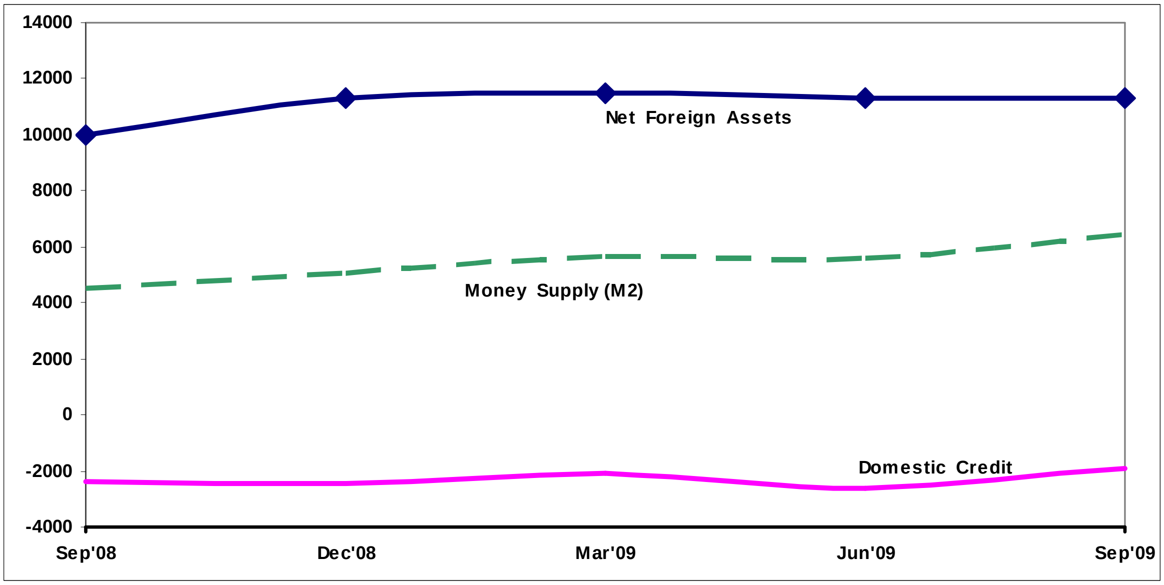


Table 8: Determinants of Money Supply

(Million Maloti: Changes)

Determinants	2008		2009		
	Sep	**Dec**	**Mar**	**Jun**	**Sep**
Net foreign assets	55.0	1296.9	227.1	-218.3	19.6
Domestic credit	-325.5	-65.4	378.4	-581.3	760.9
Net Claims on Govt	-388.0	-38.5	328.0	-693.0	671.7
Statutory bodies	-3.5	-0.4	-3.8	-2.4	-2.2
Private sector	66.0	-26.5	54.6	114.1	91.5
Other items, net	102.6	715.9	-1.5	-745.8	-55.9
Money Supply (M2)	-372.9	515.6	607.0	-54.8	836.4

Components of Money Supply

Table 9 indicates that all components of money supply rose in the third quarter of 2009. Narrow money rose by 14.6 per cent in the review period, following a 1.0 per cent decline the preceding quarter. The increase mainly reflected an 8.3 per cent increase in currency held by the public and a 15.1 per cent jump in demand deposits held by commercial banks. Growth in quasi money was stronger than the increase in narrow money. The former expanded by 16.2 per cent in the quarter to September 2009, compared with an 8.6 per cent rise in the second quarter of 2009. Quasi money generally experienced strong quarterly growth rates this year, with the first quarter growth recorded at 8.0 per cent.

Figure 12 below demonstrates that the increase in quasi-money in the first three quarters of 2009 translated into a gain in its share of total money supply. The share improved from 21.9 per cent in March 2009 to 24.3 per cent in September. The gain was realised at the expense of the share of demand deposits and currency with public, which shrank during the same period.

Table 9: Money Supply

(Million Maloti; End of Period)

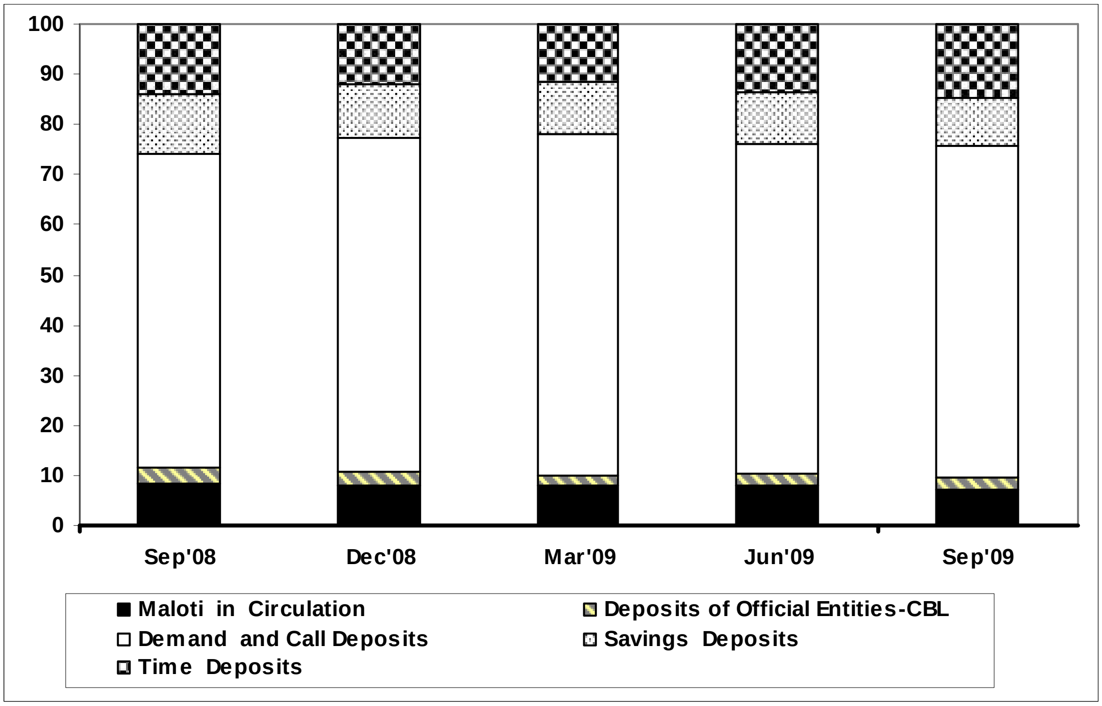
	2008		**2009**		
	Sep	**Dec**	**Mar**	**Jun**	**Sep**
Money Supply (M2)	4506.5	5022.0	5629.1	5574.8	6411.2
Money (M1)	3346.2	3879.4	4394.8	4234.5	4853.6
Maloti with public	378.0	406.6	441.3	434.8	471.0
Demand deposits[1]	28017.9	3346.1	3823.9	3666.8	4221.1
Deposits of official Entities with CBL	150.3	126.7	129.8	133.8	135.7
Quasi-Money	1160.3	1142.7	1234.3	1340.3	1557.6
Savings deposits	540.1	545.4	587.3	593.1	621.1
Time deposits	620.1	597.2	647.0	747.2	936.6

[1] includes call deposits

NB: Totals may not tally due to rounding off

Figure 12: Components of Money Supply

(Percentage shares)



Commercial Banks' Deposits by Holder

Deposits held with domestic commercial banks increased by 16.1 per cent on a quarterly basis in September 2009, against a fall of 1.0 per cent in June. Both deposits of the private sector and statutory bodies grew, with the latter experiencing a rise of 45.0 per cent albeit from a lower base. The deposits of the private sector grew by 15.5 per cent, driven mainly by an increase of 25.3 per cent in time deposits (see Table 10). Savings deposits of the private sector rose by 4.7 per cent in the third quarter of 2009. The share of private sector deposits remained high at over 97 per cent.

Reforms in the treasury bills market undertaken in September 2008 has attracted lower levels of longer-term deposits of the private sector relative to time deposits of commercial banks. The reforms included an increase in the number of tenures and frequency of auctions; reduction of minimum amount of investment; and increase in total amount of securities auctioned. Time deposits increased by M478.9 million between June 2008, before the reforms were implemented, and September 2009. Contrarily, holding of treasury bills by the non-bank sector grew by M25.9 million during the same period. This indicates a need for increased education campaigns to the private sector, as returns are generally higher on treasury bills compared with time deposits.

Table 10: Commercial Banks' Deposits by Holder

(Million Maloti: End of Period)

	2008		2009		
	Sep	Dec	Mar	Jun	Sep
Total Deposits	3665.9	4477.3	5029.3	4977.7	5778.8
Private Sector	3243.4	4133.8	4918.4	4879.9	5637.0
Demand deposits	2220.0	3128.2	3685.6	3541.4	4082.0
Savings deposits	540.0	545.3	587.2	593.0	621.0
Time deposits	583.4	460.3	645.5	745.5	933.9
Statutory Bodies	722.5	343.5	110.9	97.8	141.8

NB: Totals may not tally due to rounding off

Liquidity of Commercial Banks

At the end of September 2009, the liquidity of commercial banks, measured by the ratio of liquid assets (Table 11) to deposit liabilities and placements of other banks, registered 87.2 per cent. This was higher than the 77.9 per cent recorded at the end of the second quarter of 2009. The increase stems from a strong growth in liquid assets which overshadowed a rise in liabilities. Liquid assets jumped by 34.0 per cent in the quarter under review, driven by increases of over 30 per cent each for balances held with banks abroad and in Lesotho. Liabilities grew by a lower 19.5 per cent, which was influenced by a rise in interbank deposits and private sector deposits. At the current level, the liquidity ratio means that banks are more than meeting the required prudential liquidity position since the mandatory liquidity ratio is 25.0 per cent.

Table 11: Components of Commercial Banks' Liquidity

(Million Maloti: End of Period)

COMPONENT	2008		2009		
	Sep	Dec	Mar	Jun	Sep
Maloti Notes and Coins	60.8	74.6	59.8	62.7	70.4
Rand Notes and Coins	37.4	48.7	37.0	38.6	40.8
Balances due from Lesotho Banks	842.2	775.4	994.9	875.1	1400.0
Balances due from Foreign Banks	1784.3	2660.3	3286.1	2954.0	4061.2
Clearing Balances with CBL	278.0	91.4	233.9	196.8	190.4
CBL Bills	0.0	0.0	0.0	0.0	0.0
Lesotho Government Securities	498.4	426.2	480.2	479.7	410.0

The credit deposit ratio deteriorated from the 33.0 per cent registered in June 2009 to 30.7 per cent at the end of the third quarter of 2009. The two-basis point decline in the ratio reflected the increase in deposits of the private sector and statutory bodies, which was stronger than the rise in credit. The former increased by 13.2 per cent in the review period, compared with the latter's increase of 5.3 per cent.

Table 12: Consolidated Balance Sheet of Commercial Banks

(Million Maloti: End of Period)

	2008		2009		
	Sep	Dec	Mar	Jun	Sep
Net foreign assets	2260.0	3034.1	3321.6	3133.1	4023.8
Deposits with CBL	278.0	91.4	233.9	196.8	190.4
Credit:	2057.9	1934.8	2040.4	2172.6	2140.3
Statutory Bodies	44.3	43.8	40.0	37.6	35.4
Private Sector	1466.5	1437.0	1493.2	1605.4	1694.9
Government securities	574.1	476.0	530.2	529.6	410.0
Assets/Liabilities	4490.3	4855.9	5466.4	5502.5	6354.5
Private sector deposits[2]	3665.9	4477.3	5029.3	4977.7	5778.8
Government deposits	167.7	194.1	37.8	33.8	35.3
Capital, reserves & other, net	186.2	320.9	542.3	491.0	540.4

[2] includes statutory bodies' deposits.

Demand for Money

Domestic Credit

Commercial banks provide finance necessary for supporting economic activity through credit extension to the private sector and statutory bodies. Domestic credit maintained a generally steady upward trend observed since the beginning of the year, registering a 5.3 per cent increase at the end of September 2009. The growth was slower than the 7.2 per cent rise at the end of the second quarter. The growth in credit extended to the private sector accounted for this quarter to quarter increase, as credit to statutory bodies fell by 5.9 per cent in the same period. However, domestic credit increased by 14.5 per cent on an annual basis during the review quarter compared with 13.4 per cent recorded at the end of June.

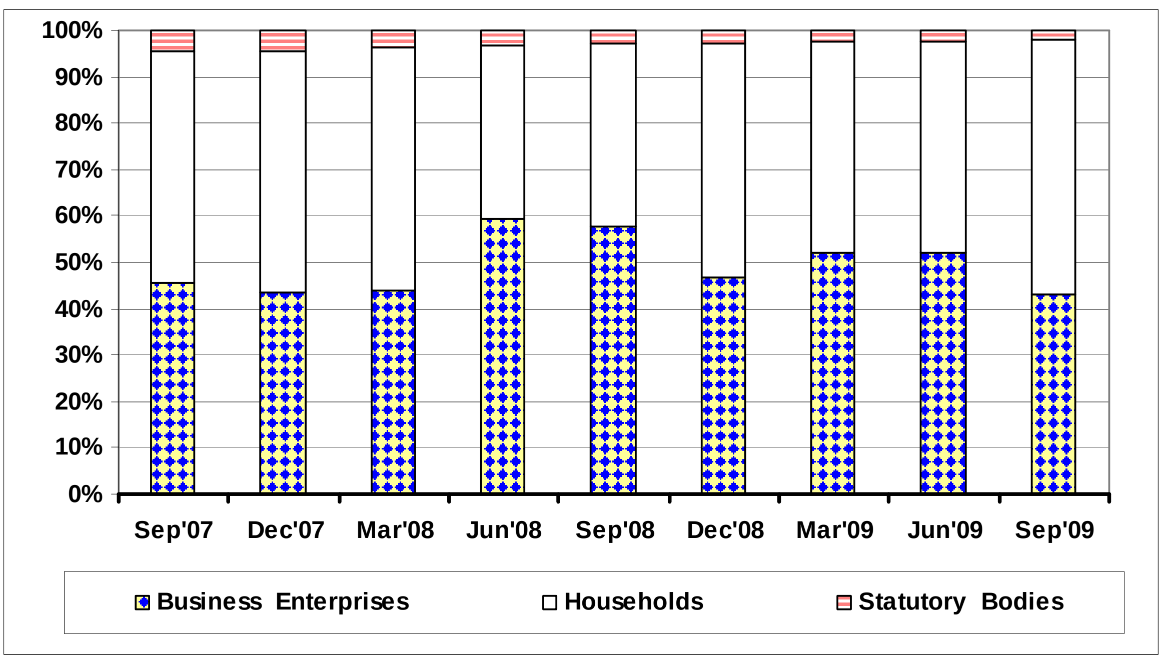
Table 13: Domestic Credit Excluding Net Claims on Government

(Million Maloti: End of Period)

	2008		2009		
	Sep	Dec	Mar	Jun	Sep
Domestic Credit	1510.7	1480.9	1533.2	1643.0	1730.3
Credit to private sector	1466.5	1437.0	1493.2	1605.4	1694.9
Business enterprises	874.5	693.3	797.7	852.2	864.9
Households	592.0	743.8	695.5	753.2	830.0
Credit to statutory bodies	44.2	43.8	40.0	37.6	35.4

Figure 13: Distribution of Credit by Holder

(Percentage shares)



Credit to Private Sector

During the quarter ended September 2009, credit extended to the private sector increased by 5.6 per cent, as a result of an increase in both credit granted to households and businesses. Credit to households grew by 10.2 per cent in the third quarter, compared with 8.3 per cent increase in the quarter to June 2009. Credit to business enterprises increased by 1.5 per cent during the third quarter, slower than the 6.8 per cent growth in the previous quarter. This led to a fall in the share of business credit to total private sector credit from 53.1 per cent in June 2009 to 51.0 per cent in September. On an annual basis, credit to the private sector increased by 15.6 per cent due to a 40.2 per cent improvement in credit to households.

Credit to Statutory Bodies

As mentioned earlier, credit channelled to statutory bodies saw a decline of 5.9 per cent in September 2009, compared with 6.9 per cent fall observed in June. Furthermore, credit to this sub-sector registered a decrease of 19.9 per cent on an annual basis at the end of September, following a decline of 21.2 per cent recorded at the end of June. Figure 13 shows that the share of credit to this sub-sector to total credit also shrank between September 2008 and 2009.

Sectoral Distribution of Credit

Credit extended for business activity, excluding non-performing loans, grew by an overall 2.3 per cent in the review quarter; an improvement compared with the 1.9 per cent growth realised in June. A 22.7 per cent decline in credit to the construction sector led to a reduction of its share to total credit from 26.3 per cent in June to 19.9 per cent in September. Construction's share became identical to that of 'transport, storage and communications' group, whose credit fell by a lower 10.9 per cent during the review period. The 'electricity, gas and water' group experienced a reduction of 49.1 per cent in credit contracted with domestic commercial banks. The group 'non-bank financial institutions and real estate' also saw a decline in credit in the third quarter.

These decreases in credit were overshadowed by increases in other sectors. Wholesale, retail, hotel and restaurant saw an increase of 66.3 per cent in the three months to September 2009, increasing it share to total credit to 11.3 per cent. The mining sector increased its credit to banks by 20.7 per cent, while credit to the agricultural sector rose by 83.2 per cent during the same period.

Table 14: Sectoral Distribution of Credit to Enterprises+

(Million Maloti: End of period)

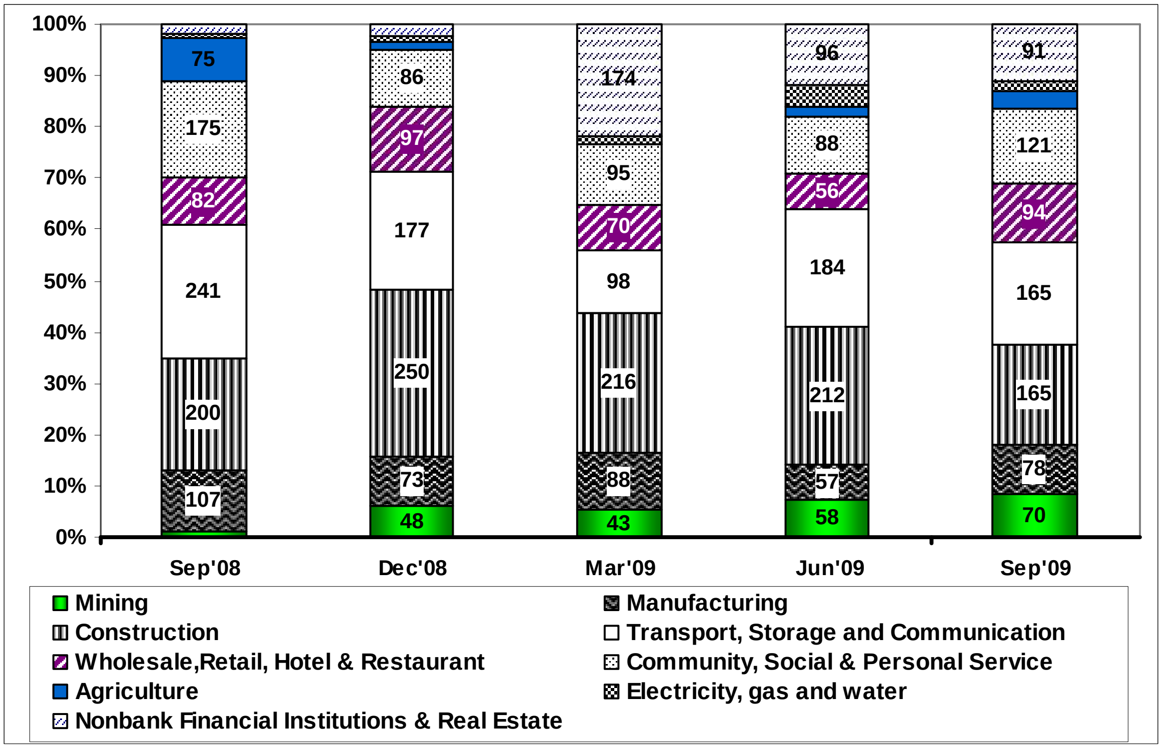
SECTOR	2008	2009

	Sep	Dec	Mar	Jun	Sep
Agriculture	74.8	12.6	2.2	15.5	28.4
Mining	11.3	47.9	43.0	57.8	69.7
Manufacturing	92.2	63.7	80.1	66.4	78.1
Construction	199.3	249.4	215.0	212.9	164.6
Transport, storage and communication	204.3	146.1	72.6	184.0	164.9
Electricity, gas and water	7.6	9.9	10.5	32.9	16.7
Wholesale, retail, hotel and restaurant	67.1	88.3	62.4	56.3	93.7
Non-bank financial institutions and real estate	15.0	16.4	173.7	96.4	91.1
Community, social and personal services.	163.3	86.1	94.5	88.3	121.4
All sectors	834.9	720.4	754.0	810.2	828.6

+excludes non-performing loans.

Figure 14: Commercial Banks' Credit to Business Enterprises

(Percentage shares)



Net Claims on Government

At the end of the quarter ended September 2009, banking system's net claims on government increased by 15.6 per cent following a 19.1 per cent decline registered at the end of June. Net claims on government by the commercial banks, which comprises mostly holdings of treasury bills, fell by 24.4 per cent in the third quarter. The decline was mainly a result of payment of 10-year securities issued to finance the restructuring of the former Lesotho Bank. Deposits of government held with commercial banks and the total amount of treasury bills issued for monetary policy purposes held by banks, increased slightly during the review period.

Net claims on government by the CBL increased by close to M790 million. The large increase was a reflection of 15.6 per cent fall in deposits of government held with the Central Bank. This could be an indication of withdrawals made to finance a large budget deficit caused by the payment of commitments from the previous quarter, which were earlier hindered by technical problems with the new government finance system.

Table 15: Banking System's Net Claims on Government
(Million Maloti: End of Period)

Holder	2008		2009		
	Sep	Dec	Mar	Jun	Sep
Commercial banks	406.3	281.9	492.4	495.7	374.7
Claims on Government	574.1	475.9	530.2	529.6	410.0
o/w MP T Bills[3]	468.2	454.0	461.8	490.5	492.4
Less Government deposits	167.7	194.1	37.8	33.8	35.3
CBL	-4318.5	-4232.6	-4115.0	-4811.4	-4018.7
Claims on Government[4]	316.6	529.9	345.5	292.8	288.3
Less Government deposits	4635.1	4762.5	4460.5	5104.2	4307.1
o/w blocked account	535.0	424.8	475.7	506.1	512.0
Total Net Claims	-3939.2	-3972.7	-3645.7	-4315.7	-3644.0

[3] 'MP T Bills' means monetary policy treasury bills.
[4] IMF loans on-lent to the GOL.

Net Foreign Assets

The net foreign assets of the banking system increased modestly at the end of September contrasted with a decline of 1.9 per cent recorded in June. The increase in the third quarter reflected a 28.4 per cent increase in net foreign assets of commercial banks. Figure 15 below indicates that the increase in net foreign assets of commercial banks led to an improvement in the share of commercial banks holdings of net foreign assets from 27.7 per cent in June 2009 to 35.6 per cent in September. Central Bank's net foreign assets fell by 10.7 per cent during the same period. However, total net foreign assets rose by 13.3 per cent on annual basis in September 2009.

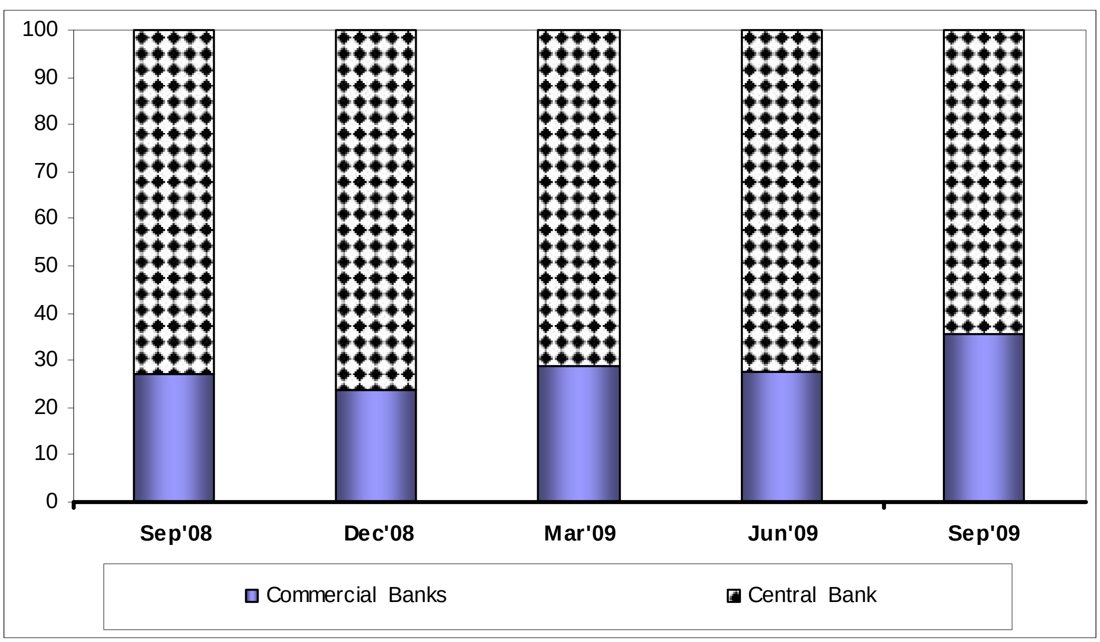
Table 16: Banking System's Foreign Assets and Liabilities

(Million Maloti: End of Period)

Holder	2008		2009		
	Sep	Dec	Mar	Jun	Sep
A. Commercial Banks	2260.0	3034.1	3321.6	3133.1	4023.8
Foreign Assets	2305.5	3126.7	3453.3	3206.2	4075.7
Foreign Liabilities	-45.5	-92.7	-131.7	-73.1	-51.8
B. Central Bank of Lesotho	7728.7	8251.6	8191.2	8160.8	7289.8
Foreign Assets	8430.4	8989.2	8921.9	8852.0	7976.5
Foreign Liabilities	-701.7	-737.7	-730.8	-691.1	-686.7
Net Total	9988.7	11285.6	11512.8	11294.0	11313.6

Figure 15: Net Foreign Assets

(Percentage shares)



Money Market Developments

Overview

The total holding of treasury bills improved by 1.8 per cent during the third quarter of 2009. This increase was reflected in a larger holding of treasury bills by commercial banks, which increased by 3.9 per cent between June and September. Commercial banks continue to gain influence in the securities market since introduction of new reforms, at the expense of the non-financial private sector. The non-bank financial sector increased its holding of treasury bills by 51.4 per cent, though from a low base, while the non-financial private sector saw a decline of 63.4 per cent in treasury bill holdings. This implies that the share of the non-financial sector in the holding of treasury bills fell from 8.3 per cent in the second quarter to 3.0 per cent, while commercial banks' share improved to 86.1 per cent. In order to maintain broad participation in the securities market, public sensitisation campaigns need to be undertaken to promote treasury bills as an alternative form of investment. Reasons for the declining participation of the private sector also need to be investigated, and addressed.

Table 17: Holding of Treasury Bills

(Face Value; Million Maloti)

Type of Holder	2008		2009		
	Sep	Dec	Mar	Jun	Sep
Total	537.7	544.6	561.4	663.2	675.1
Banking System	468.5	485.8	507.4	559.5	581.6
Central Bank	0.3	0.3	0.3	0.3	0.3
Commercial Banks	468.2	485.5	507.1	559.2	581.3
Non-Bank Sector	69.2	58.8	54.0	103.6	93.5
NBFIs	0.3	0.3	7.3	48.4	73.3
Others	68.9	57.9	46.7	55.2	20.2
Memorandum Item					
Average Yield (per cent)	11.91	10.66	9.92	7.05	7.14

Money Market and Short-term Interest Rates

During the third quarter of 2009, major money market rates displayed mixed signals. The domestic lending rate fell from an average of 12.17 per cent in June 2009 to 11.83 per cent in September. This was in response to a 50 basis point reduction in the corresponding rate in South Africa (see Table 18). The fall in the South African prime lending rate was a result of a cut in the South African Reserve Bank's (SARB) repo rate by 50 basis points. At the end of the third quarter, the SARB had cut the repo rate five times since the beginning of the year in a bid to stabilise the economy given abating inflationary pressures.

Contrarily, the 91-days treasury bill rate increased slightly during the review quarter. This was despite the fall in the 91-day treasury bill rate in South Africa during the same period. It led to a reduction in the margin between the two rates from 62 basis points to 4 basis points, with Lesotho's rate remaining lower than South Africa's.

Despite the developments in lending and treasury bill rates in Lesotho within the quarter, many deposit rates remained unchanged. As Table 18 indicates, only the 6-month time deposit rate changed during the quarter, registering a decrease from an average of 2.63 per cent in June to 2.53 per cent at end of the third quarter. This further attests to the insensitiveness of the private sector to rates of return on savings, as time deposits continued to increase despite falling rates, and at the expense of treasury bills which offer higher returns.

Table 18: Major Money Market Interest Rates

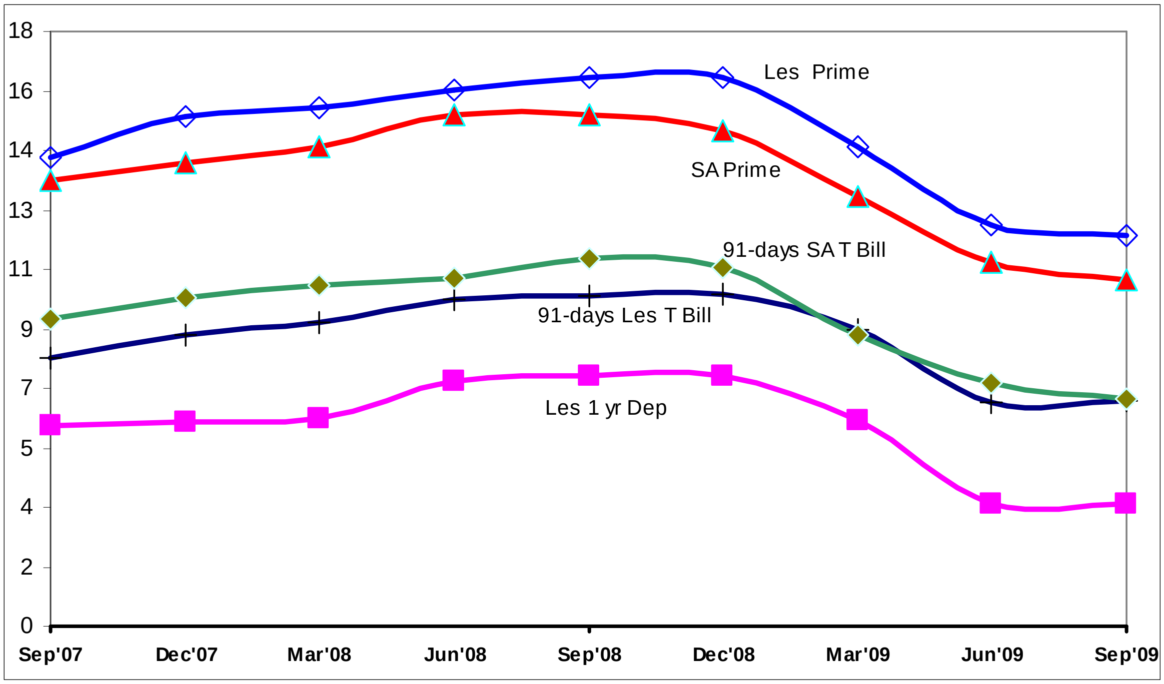
(Percent: End of Period)

Interest Rates by Type	2008		2009		
	Sep	Dec	Mar	Jun	Sep
Central Bank					
T Bill Rate – 91 Days	10.01	10.05	9.00	6.76	6.84
Lombard Rate	14.01	14.05	13.00	10.76	10.84
Commercial Banks[5]					
Call	6.75	6.75	4.75	1.75	1.75
Time:					
31 days	5.54	5.54	3.96	1.65	1.65
88 days	6.22	6.22	4.64	2.20	2.20
6 months	6.60	6.60	5.02	2.63	2.53
1 year	7.57	7.57	6.23	3.69	3.69
Savings	5.04	5.48	3.64	2.11	2.11

Prime	16.58	16.58	14.50	12.17	11.83
South Africa* Repo	12.00	11.50	9.50	7.50	7.00
T Bill Rate – 91 Days	11.11	10.84	8.82	7.38	6.90
Marginal Lending Rate	17.00	16.50	14.50	12.50	12.00
Prime	15.50	15.00	13.00	11.0	10.50

* Figures for South Africa were obtained from the SARB
[5] Average rates by commercial banks

Figure 16: **Short-Term Interest Rates**
(Percent Per Annum)



V. Government Finance

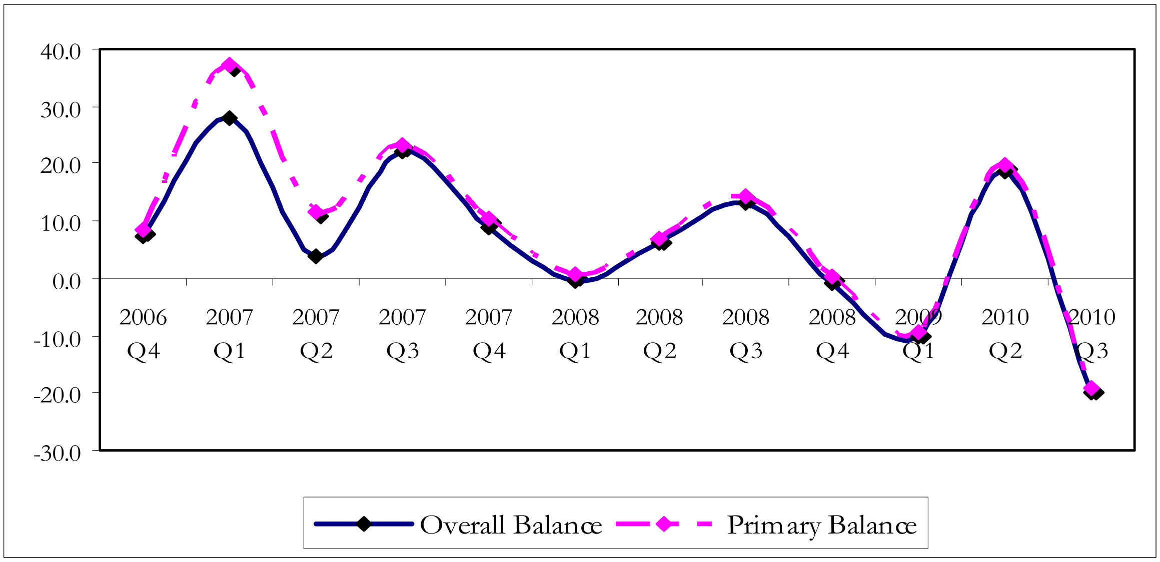
Summary of Budget Outturn

Preliminary estimates on government budgetary operations indicate a fiscal deficit during the third quarter of 2009. As a percentage of GDP, the deficit stood at 20.0 per cent and was mainly attributed to a strong recovery in both recurrent and capital expenditure. The deficit registered in the review quarter followed an 18.8 per cent surplus observed in the previous quarter which was largely reflective of under expenditures due to capacity constraints experienced during the implementation of the government financial management system, Integrated Financial Management Information System (IFMIS). This demonstrates that expenditures that could not be undertaken in the second quarter were effected in the review period. Indeed, budgetary operations during the two quarter resulted in a combined surplus of M42.3 million.

Total revenue and grants were estimated to have shrunk by 3.8 per cent in the quarter to September 2009. As Figure 17 below shows, the primary balance[2] was slightly below the overall balance at 19.1 per cent. Government expenditure and net lending surged by 81.9 per cent over the same period. As a share of total expenditure, recurrent expenditure stood at 68.8 per cent, while capital expenditure constituted 31.2 per cent of total expenditure.

Figure 17: Primary Balance versus Overall Balance

[2] Primary balance is a good indicator of budgetary operations since it excludes interest costs on public debt.



Revenue

Total receipts including grants, dropped by 3.8 per cent during the review period driven by decreases in company tax and value added tax (VAT) and grants. Revenue receipts from the Southern African Customs Union (SACU) remained unchanged, and continued to account for greater proportion of total receipts, at 60.4 per cent. The share of income tax and value added tax (VAT) as a proportion of total receipts was 22.1 per cent and 11.4 per cent, respectively.

Table 19: Government Revenue

(Million Maloti)

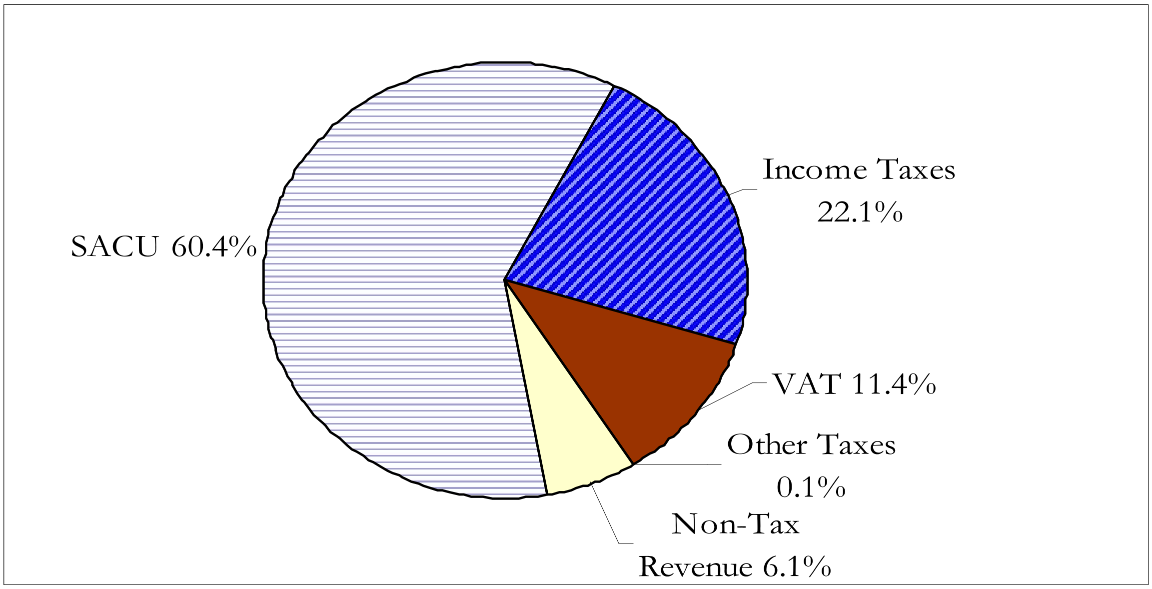
	2008/09			2009/10	
	Jul-Sep	**Oct-Dec**	**Jan-Mar**	**Apr-Jun** Revised	**July-Sep*** Preliminary
Total Revenue and Grants	2223.2	2221.6	2337.6	2114.9	2034.1
Total Revenue	2151.4	2190.8	2306.7	1988.1	2034.1
Tax Revenue	1898.0	1967.4	1925.2	1890.5	1910.8
Customs	1225.2	1225.2	1225.2	1229.5	1229.5
Non-customs	672.7	742.1	700.0	713.8	681.3
Income Taxes	392.6	331.0	429.3	450.4	449.2
Taxes on goods & services	277.2	258.6	247.0	263.3	232.1
Other Taxes	2.9	152.6	23.7	56.6	3.0
Non-Tax Revenue	253.5	223.4	381.5	97.66	123.3
Of which: Water royalties	96.7	81.6	67.9	78.5	90.0
Grants	71.7	30.8	30.8	126.8	252.4

Source: Ministry of Finance and Development Planning (MoFDP)
*Preliminary estimates

VAT revenue fell by 11.8 per cent in the third quarter, following a 6.7 per cent increase in the second quarter. Conversely, income tax revenue rose by 14.1 per cent due to a strong growth in personal income tax in contrast to a 8.3 per cent fall in the previous quarter. The improvement in income tax reflected, amongst others, smooth running of IFMIS following capacity constraints experienced during the implementation stage. Contrary to an increase in the previous quarter, company tax decreased by 23.3 per cent in the review quarter.

The non-tax component rose by 26.3 per cent in the third quarter relative to 74.4 per cent drop in the second quarter. Non-tax revenue comprises water royalties, administrative fees, dividends, interest on loans on-lent to public enterprises. The rise in non-tax revenue was partly driven by a rise in water royalties.

Figure 18: Sources of Government Revenue



Expenditure

Government expenditure and net lending rose by 81.9 per cent in the third quarter following a 42.2 per cent decrease during the previous quarter. The rise was driven by robust growth in both recurrent and capital expenditure. The rise in recurrent expenditure was driven by transfers and subsidies as well as expenditure on goods and services. As earlier indicated, this strong growth was reflective of the smooth functioning of IFMIS following capacity constraints experienced during the initial stages of its implementation. During the early stages of IFMIS implementation, capacity constraints encountered in the use of the system resulted in some payments being delayed or not undertaken at all.

Table 20: Government Expenditure

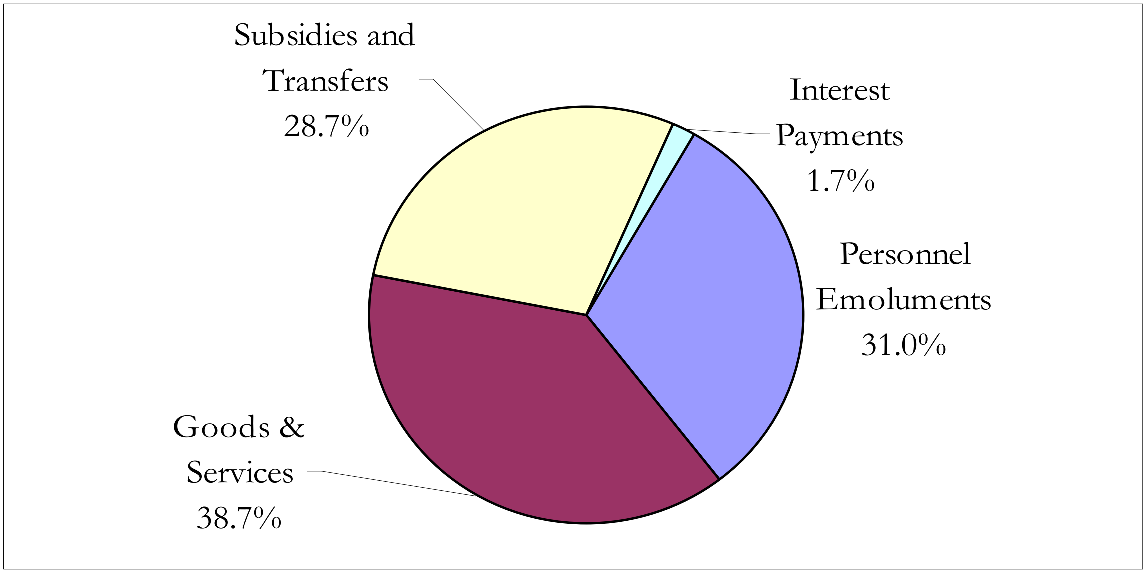
(Million Maloti)

	2008/09			2009/10	
	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun Revised	July-Sep* Preliminary
Total Expenditure & Net Lending	1778.4	2248.2	2670.5	1543.9	2704.2
Recurrent Expenditure	1344.4	1768.1	2201.7	1115.7	1860.1
Personnel Emoluments	482.8	495.4	495.7	576.9	576.3
Interest Payments	35.9	41.5	21.6	31.3	31.0
Foreign	17.7	22.5	11.6	13.5	17.1
Domestic	18.2	19.0	10.0	17.8	13.9
Other Expenditure	825.6	1231.2	1684.4	507.5	1252.8
Capital Expenditure	434.5	480.1	468.8	428.2	1096.5
Net Lending	-0.5	0.0	0.0	0.0	0.0

Source: MoFDP
*Preliminary estimates

Capital expenditure showed strong growth in the third quarter of 2009. It rose by 127.2 per cent following 8.7 per cent drop during the previous period. This strong recovery was a result of several capital projects being undertaken, *inter alia*, construction of the Lesotho Referral Hospital, and construction of urban and rural roads in various districts, expenditures on health sector reforms. Although capital expenditure as a share of total expenditure remained at approximately 30.0 per cent, robust growth in capital expenditure bodes well for a developing economy such as Lesotho.

Figure 19: Recurrent Expenditure by Type



Financing

Government budgetary operations were projected to result in a fiscal deficit during the period under review. The deficit was a result of a drawdown of government deposits with the banking system. The deficit to a great extent reflects some of the expenditures that were not undertaken in the previous quarter due to capacity constraints experienced during implementation of IFMIS.

Table 21: Government Financing

(Million Maloti)

	2008/09			2009/10	
	Jul-Sep	**Oct-Dec**	**Jan-Mar**	**Apr-Jun** Revised	**Jul-Sep*** Preliminary
Financing	-444.8	26.8	332.9	-627.7	670.0
Foreign	-36.1	69.1	2.7	17.9	-19.0
Loan drawings	33.6	142.8	53.2	68.5	39.8
Amortization	-69.7	-73.7	-50.5	-50.6	-58.8
Domestic	-408.7	-42.3	330.2	-645.6	689
Bank Financing	-408.0	-33.5	327.0	-693.0	671.7
Non – Bank	-0.7	-8.8	3.2	47.4	17.3

Source: MoFDP

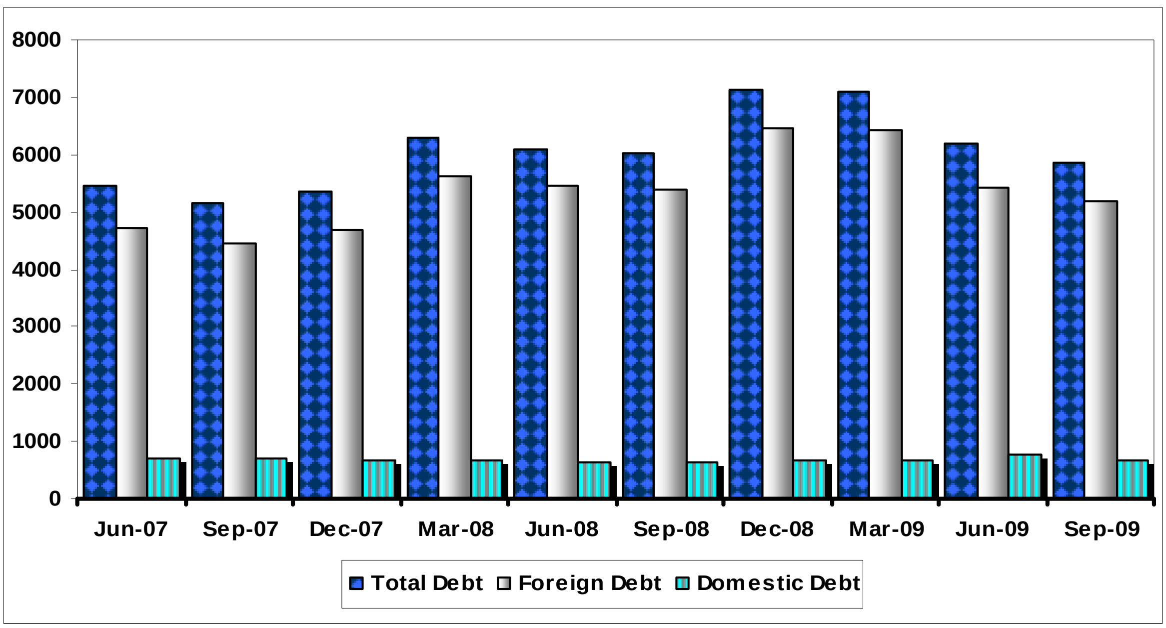
Public Debt

Overview

Government contracts foreign and domestic debt to finance its budgetary operations. Total debt dropped by 5.3 per cent from the level recorded in the second quarter of 2009. As a percentage of GDP, public debt stood at 43.8 per cent, below the 60 per cent threshold set by SADC under the macroeconomic convergence targets. Debt service ratio also remained within the sustainability threshold during the review period, recorded at 2.6 per cent. This is calculated as the ratio of debt service to exports of goods and services and factor income where applicable. External debt continued to constitute a greater percentage of overall debt stock. The ratio of external debt to total debt was 88.5 per cent while the ratio of domestic debt to total debt was 11.5 per cent in the review quarter.

Figure 20: Outstanding Public Debt

(Million Maloti: End of Period)



External debt

External debt dropped by 4.2 per cent in the third quarter of 2009 following a 15.0 per cent drop in the previous quarter. The drop in external debt was on account of the appreciation of the rand vis-à-vis other currencies in which the debt is denominated. In addition, the drop in external debt was driven, largely, by a drop in both bilateral and multilateral loans. Loans from bilateral sources declined by 1.8 per cent in the third quarter following 84.0 percent slump observed in the previous quarter. Credit from financial institutions dropped by 1.6 per cent. Multilateral loans continued to constitute a greater percentage of total external debt.

It was also observed that external debt accounted for 43.8 per cent of GDP compared with 46.2 per cent in the previous quarter. Concessional debt as a percentage of external debt remained unchanged at 94.6. This bodes well for Lesotho as it plays a critical role to ease debt service burden, and also to meet debt sustainability indicators.

Table 22: External Debt

(Million Maloti)

	2008		2009		
	QIII	QIV	QI	QII	QIII
External Debt	5378.3	6457.1	6435.1	5408.1	5181.5
Bilateral Loans	316.7	390.6	426.3	231.5	227.4
Concessional	279.9	348.2	387.6	209.4	204.7
Non-concessional	36.8	42.4	38.7	23.2	22.74
Multilateral Loans	4931.3	5932.6	5874.6	4895.9	4683.0
Concessional	4810.7	5892.0	5833.6	4864.4	4654.8
Non-concessional	120.7	40.6	41.0	31.5	28.2
Financial Institutions	77.1	75.7	75.3	73.1	71.9
Concessional	21.5	21.5	22.4	20.2	19.0
Non-concessional	55.6	54.2	52.9	52.9	52.9
Suppliers' Credit	53.2	58.2	58.9	207.6	199.2

Source: MoFDP

Domestic Debt

Domestic debt is the component of public debt owed to domestic residents. Holding of domestic debt dropped by 13.2 per cent in September 2009, compared with 13.0 per cent growth in the previous quarter. The decline was a result of a drop in holdings of treasury bills by both the Bank and the non-Bank. the drop was largely due to the maturity of the 10-year bond, to the tune of M114.0 million during the quarter. This bond was issued in 1999 to finance the restructuring of the financial sector. As a percentage of GDP, domestic debt decreased from 5.8 per cent to 5.0 percent.

Table 23: Domestic Debt

(Million Maloti)

	2008		2009		
	QIII	QIV	QI	QII	QIII
Domestic Debt	652.5	659.3	676.1	777.5	674.7

Banks	583.2	600.4	622.0	673.9	581.3
Long-term	114.0	114.0	114.0	114.0	0.0
Short-term	468.6	485.8	507.4	559.2	581.3
Non-Banks	69.3	58.8	54.0	103.6	93.5
Short-term	69.3	58.8	54.0	103.6	93.5

VI. Foreign Trade and Payments

Overview

The external sector position deteriorated further in the third quarter of 2009. The overall balance, in seasonally adjusted terms, registered a deficit of M877.1 million during the review quarter compared with a deficit of M72.0 million observed in the previous quarter. This reflected deterioration in the capital and financial account and the impact of the strengthening of the Loti against the major trading currencies, where the CBL's foreign reserves were held. Transaction balance, which represents the overall balance excluding the effects of currency movements, also recorded a deficit of M741.4 million in seasonally adjusted terms in the review quarter in contrast with a surplus of M562.9 million in the previous quarter, on account of the deterioration in capital and financial account.

Current Account

Current account registered a lower surplus during the quarter under review. It narrowed to a surplus equivalent to M297.6 million in the third quarter from a revised M341.8 million in the second quarter of 2009. The narrowing of the current account surplus is attributed to a rise in merchandise imports which overshadowed an improvement in merchandise exports. In addition, deterioration in income and current transfers contributed to the narrowing of current account surplus. As percentage of GDP, current account declined to 11.6 per cent in the review quarter from 13.3 per cent observed in the previous quarter.

Table 24: Current Account Balance

(Million Maloti)

	2008		2009		
	QIII	QIV	QI	QII*	QIII+
I. Current Account	269.04	330.59	322.98	341.82	297.57

(a) Goods	-1724.69	-1705.87	-1779.45	-1566.17	-1541.09
Merchandise exports f.o.b.	2216.05	1675.60	1403.67	1485.46	1782.76
Of which diamonds	784.98	270.40	187.80	355.67	343.92
Of which textiles & clothing	880.96	876.67	846.12	773.09	854.16
Other exports#	550.11	528.53	399.75	356.70	584.68
Merchandise imports f.o.b.	-3940.74	-3381.47	-3183.12	-3051.63	-3323.85
(b) Services	-109.48	-102.42	-80.08	-134.37	-129.14
(c) Income	1020.03	1045.53	979.06	956.81	906.56
(d) Current Transfers	1083.18	1093.35	1203.45	1085.55	1061.24

* Revised estimates
\+ Preliminary estimates
\# All other merchandise exports excluding 'textiles and clothing' and 'diamonds'

Merchandise Exports

Merchandise exports continued to improve for the second consecutive quarter of 2009, reflecting resurgence in the global demand, due to expansionary monetary and fiscal policies in the US and other parts of world. In seasonally adjusted terms, merchandise exports rose by 13.9 per cent during the quarter under review compared with a rise of 6.7 per cent in the previous quarter. The improved merchandise exports emanated largely from manufactured goods such as textiles and clothing and diamond exports. However, the appreciation of local currency counterbalanced an increase in earnings of merchandise exports. On an annual basis, merchandise exports fell by 19.6 per cent. Relative to GDP, merchandise exports increased to 69.2 per cent in the review quarter from 57.7 per cent observed in the previous period.

Merchandise Imports

Merchandise imports, in seasonally adjusted terms, fell by 1.3 per cent in the third quarter of 2009 compared with a decline of 0.2 per cent registered in the previous quarter. In seasonally unadjusted terms, merchandise imports rose by 8.6 per cent during the quarter under review. The increase in merchandise imports may be reflective of the recovery in government purchases of goods following the disruptions experienced during the second quarter of 2009. However, the weak domestic demand coupled with the low level of industrial production continues to affect the growth of imports negatively. On an annual basis, merchandise imports dropped by 15.8 per cent indicating that the economic activity in the country is still sluggish.

Table 25: Value of Exports by Section of the S.I.T.C. #

(Million Maloti)

COMMODITY	2008		2009		
	QIII	QIV	QI	QII*	QIII+
0. Food & Live Animals	123.60	47.30	58.16	52.14	76.83
Cattle	0.01	0.00	0.00	0.0	0.05
Wheat Flour	46.38	17.59	17.53	14.32	23.21
Maize Meal	0.45	1.06	12.14	5.77	23.04
Other	76.76	28.65	28.49	32.05	30.53
1. Beverages & Tobacco	55.08	27.08	36.38	38.53	50.80

Beverages	55.06	27.08	36.38	38.53	50.80
2. Crude Materials	792.14	283.61	193.49	356.99	346.48
Textiles fibres	7.15	13.22	5.69	1.29	2.56
Of which Wool	6.44	12.82	5.69	1.13	0.74
Of which Mohair	0.71	0.39	0.00	0.16	1.82
Crude fertilizers & crude minerals	784.98	270.39	187.80	355.70	343.92
Of which Diamond	784.98	270.39	187.80	355.70	343.92
5. Manufactured Goods	36.26	32.11	49.78	46.35	51.36
Of which textiles yarn and fabric	21.79	17.16	36.04	41.19	25.30
Other manufactured goods	14.47	14.95	13.74	5.16	26.07
6. Machinery & Transport Goods	267.01	354.31	198.03	201.82	317.49
7. Miscellaneous Manufactured Goods	914.71	911.32	853.42	780.48	912.63
Of which clothing accessories	859.17	859.50	810.09	731.91	828.86
Other	55.54	51.82	43.33	48.57	83.77
8. Unclassified Goods	22.18	19.88	14.41	9.15	27.16
TOTAL EXPORTS	2216.00	1675.60	1403.67	1485.46	1782.75

Note: Totals may not tally due to rounding
* Revised estimates
+ Preliminary estimates
# Standard International Trade Classification

Direction of Trade

During the period under review, SACU region continued to be the largest recipient of Lesotho's exports with a share of 41.8 per cent. This is marginally lower than 41.9 per cent recorded in the previous quarter. The US market remained the second largest recipient of Lesotho's exports, particularly textiles and clothing. Its share registered 37.2 per cent in the review period compared with 32.1 per cent observed in the previous quarter. The third largest recipient of Lesotho's exports is the European market, where a large portion of Lesotho's diamond exports is destined for. It registered a share of 19.6 per cent in the quarter ending September 2009 compared with 24.1 per cent in the previous quarter. The Asian market remained insignificant with a share of 0.2 per cent in the quarter under review.

Table 26: Direction of Trade - Exports and Re-Exports, f.o.b.

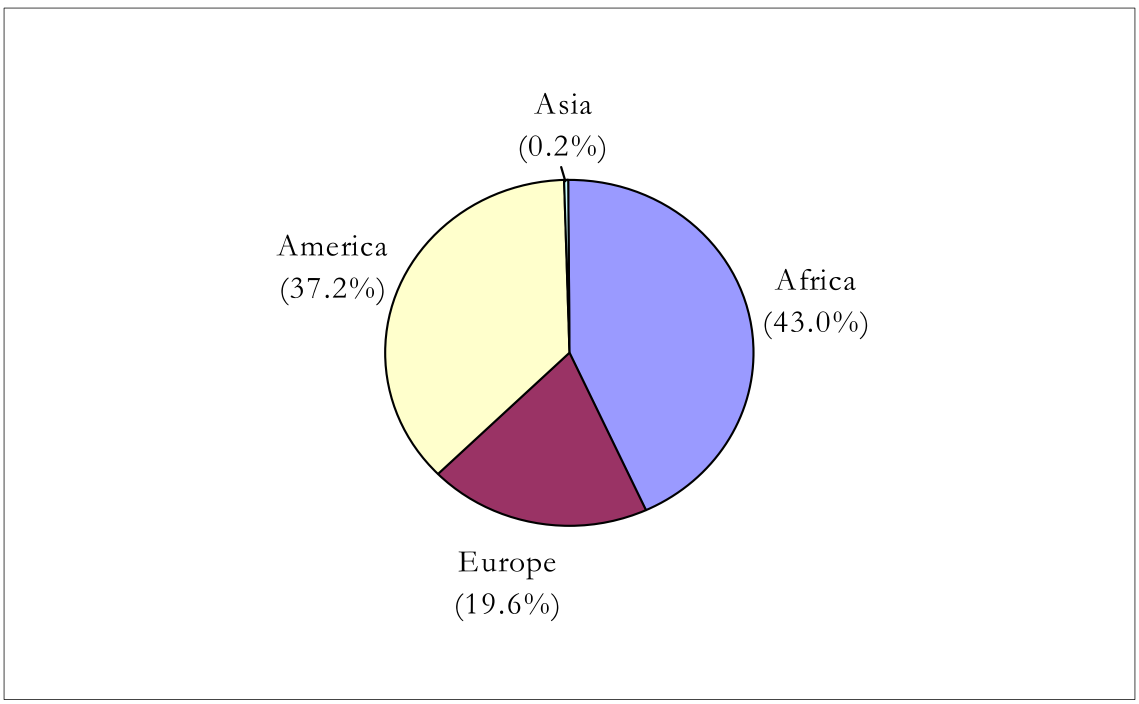
(Million Maloti)

Region	QIII	2008 QIV	QI	2009 QII*	QIII+

World	2216.05	1675.60	1403.67	1485.46	1782.75
Africa	717.26	769.60	601.41	643.74	767.18
SACU	704.23	753.06	585.28	622.54	745.23
SADC	0.03	3.11	3.79	0.52	2.09
Other	13.00	13.43	12.34	20.68	19.86
Europe	783.87	271.48	195.07	358.29	348.90
EC	783.87	271.48	195.07	358.29	348.90
America	709.73	621.29	600.75	477.52	663.49
Asia	5.19	13.22	6.44	5.91	3.19

Note: Total may not tally due to rounding
* Revised estimates
\+ Preliminary estimates

Figure 21: Direction of Merchandise Exports



Services Account

During the quarter under review, net services continued to display an outflows but at the lower rate. It registered an outflow equivalent to M129.1 million in the review quarter compared with a revised outflow of M134.4 million recorded in the previous quarter, largely driven by expenditure by Lesotho's embassies abroad coupled with water royalties which rose by 8.4 per cent.

Travel

International travel services recorded a net inflow of M44.9 million in the quarter ending September 2009 compared with an inflow of M34.9 million in the period ending June 2009, mainly as a result of, among other factors, an increase in personal expenditure by expatriates. The value of travel receipts rose by 16.7 per cent in the review period from a fall of 9.6 per cent in the previous quarter. The value of travel payments also increased by 2.3 per cent in the quarter under review compared with a rise of 1.5 per cent in the previous quarter.

Income

The net income continued to show a fall for the third consecutive quarter in 2009. It registered a decline of 5.3 per cent during the quarter under review following a decline of 2.3 per cent recorded in the previous quarter. The deterioration largely emanated from a fall in labour income coupled with a drop in investment income.

Labour income

During the quarter ending September 2009, labour income, in seasonally unadjusted terms, plummeted by 2.3 per cent, almost the same percentage decline registered in the quarter ending June 2009. Poor performance of labour income is attributed to a drop in miners' remittances, due to a fall in the number of Basotho migrant mineworkers. However, the rising prices of commodities in the international markets suggest that expectations of global economic recovery is becoming more positive, and thus, may curb the negative impact on both SA mining industry and employment of Basotho migrant mineworkers. On an annual basis, labour income plunged by 11.1 per cent.

Investment Income

Net investment income continued to decline for the third consecutive quarter in 2009. It fell by 18.9 per cent to a net inflow of M138.2 million in the review quarter, from a net inflow of M170.5 million in the previous quarter, due to a decline in both inflows and outflows of investments.

Investment income inflows dropped by 20.6 per cent during the review quarter, following a 6.7 per cent decline in the previous quarter, due to declining interest earnings by both CBL and commercial banks. CBL's returns on investment fell by 10.7 per cent while commercial banks' returns on investments declined by 37.7 per cent. The continuing appreciation of the local currency also contributed to the fall in returns on investments. In addition, a decline in interest rate in the CMA region also pulled down returns on investment income inflows.

Current Transfers

During the quarter under review, current transfers, in seasonally adjusted terms, decreased by 2.2 per cent, following a decline of 9.8 per cent observed in the previous quarter. The deterioration is attributed largely to higher payments on subscriptions to international organisations which rose by 32.7 per cent.

Capital and Financial Account

The net capital and financial account registered an outflow in the review quarter. It recorded an outflow equivalent to M501.7 million from an inflow of M607.2 million recorded in the previous quarter. The observed performance is underpinned by a higher commercial banks' foreign assets which registered an outflow of M869.4 million, compared with an inflow of M247.1 million in the previous quarter. It is worth noting that during the quarter, Government further contributed to the civil service pension scheme and redeemed 10 year bond issued during the restructuring of Lesotho Bank.

Table 27: Capital and Financial Account

(Million Maloti)

	2008		2009		
	QIII	QIV	QI	QII*	QIII+
I. Capital and Financial Account	1083.26	-184.20	132.85	607.24	-501.78
Capital Account	47.30	30.80	30.80	6.70	47.30
Financial Account	1035.96	-215.00	102.05	600.54	-549.06
Special Financing – LHWP	22.88	27.49	27.98	45.21	22.88
II. Reserve Assets	-704.65	-558.82	67.28	70.01	875.49

* Revised estimates
+ Preliminary estimates

Reserve Assets

Gross reserves fell to M7.9 billion in the period ending September 2009, from M8.8 billion registered in the previous quarter. The Net International Reserves (NIR) also fell to US$819.3 million in the third quarter of 2009 compared with US$8896.7 million observed in the previous quarter. Measured in months of import cover, gross official reserves dropped to 6.5 months in the quarter under review from 7.3 months recorded in the previous quarter.

Figure 22: Reserve Assets

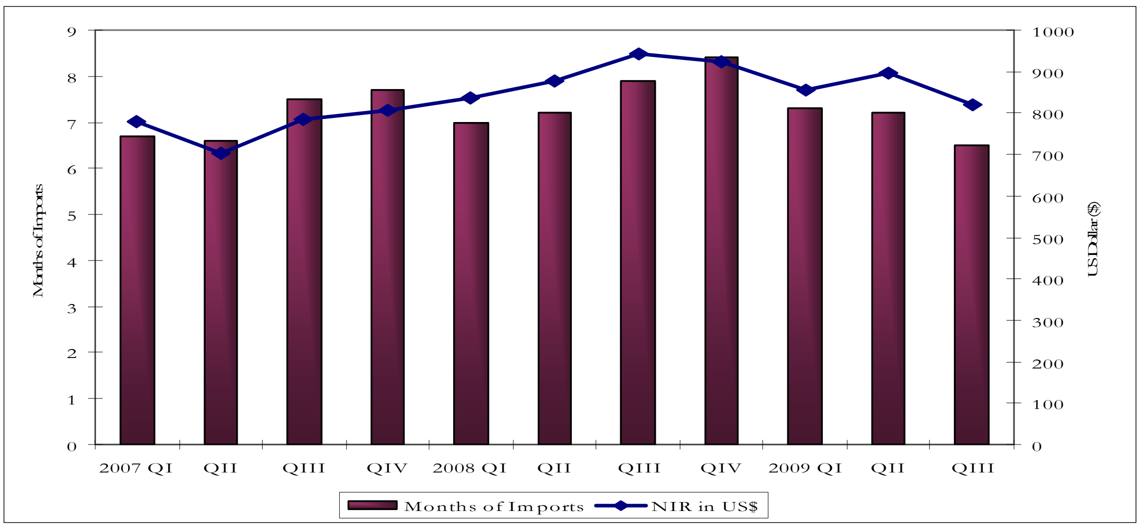
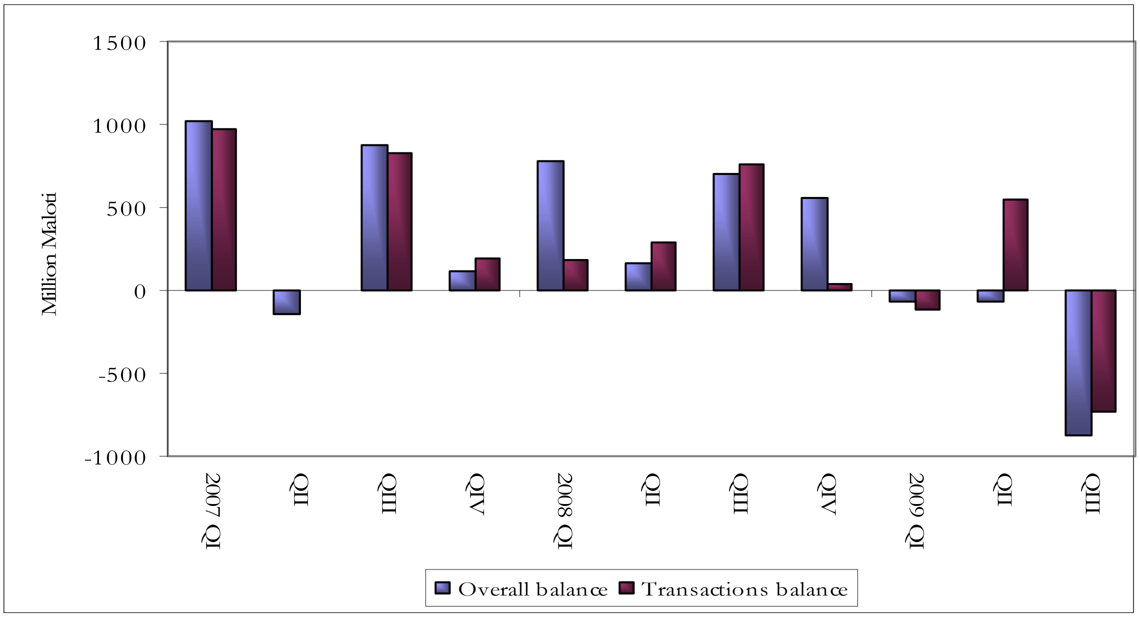


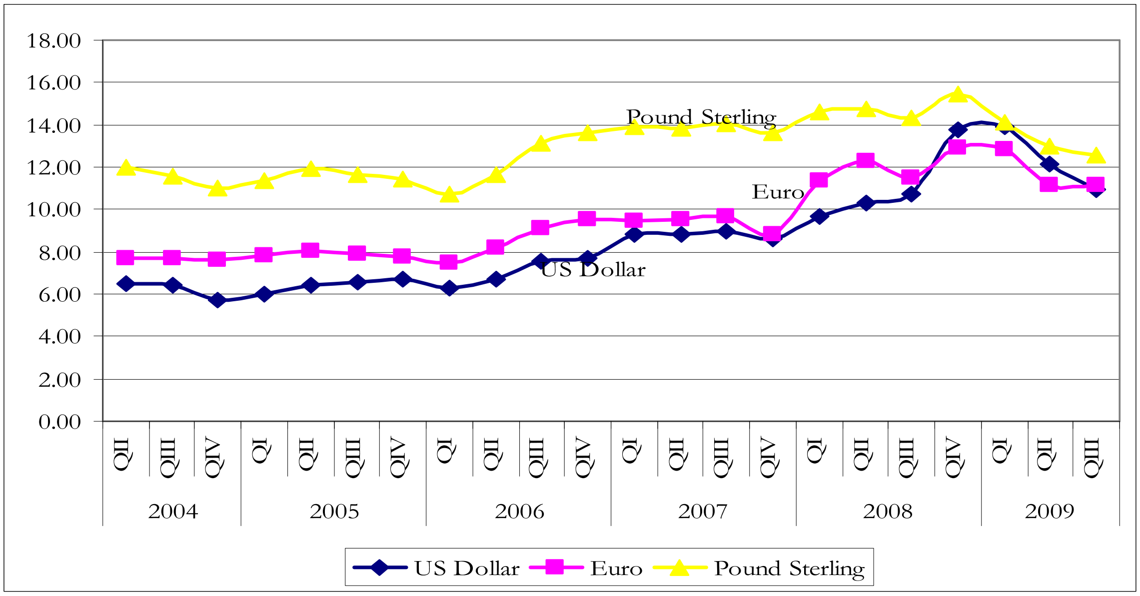
Figure 23: Balance of Payments



Exchange Rates

The Loti, which is at par with the Rand continued to appreciate for the third consecutive quarter in 2009, against the major trading currencies during the period ending September 2009. On average, and in nominal terms, the Loti strengthened by 7.7 per cent against the US Dollar and by 3.2 per cent and 1.9 per cent the Euro and the Pound Sterling, respectively. In real terms, the Loti appreciated by 9.6 per cent against the US Dollar. The Loti also appreciated by 0.5 per cent and 3.0 per cent against the Euro and Pound Sterling in real terms. The continued appreciation of the loti against major currencies is negatively affecting the price competitiveness of Lesotho's exports in the international markets.

Figure 24: Real Exchange Rate of the Loti against Major Currencies



STATEMENT OF MONETARY POLICY COMMITTEE

7 July 2009

1. Introduction

The Monetary Policy Committee (MPC) of the Central Bank of Lesotho (CBL) held its 20th meeting on 07th July 2009 to discuss the recent economic developments and their implications on monetary policy operations. This meeting is held to review and monitor the Bank's prime mandate of price stability. The mandate is pursued by anchoring monetary policy to that of South Africa through the peg of loti to the rand. It allows Lesotho to benefit from the anchor economy's monetary policy regime of inflation targeting became a large proportion of Lesotho's inflation is imported from the neighbouring country. The Committee maintains adequate foreign reserves to underwrite the currency peg. It sets the minimum target level of external reserves and monitors performance of open market operations (auction of treasury bills) in achieving the target.

The Committee noted the ongoing global economic downturn, with SA officially pronounced to be in recession for the first time in more than ten years. The current downturn follows a recession experienced in the developed world in the latter part of 2008, and continued in the first half of 2009. The recession in the developed world impacts negatively on the export sectors in developing countries such as South Africa and Lesotho. Asset prices are dwindling and unemployment is rising in most developed and developing countries. The South African mining industry retrenched a sizable number of employees, the consequences of which will be felt more in Lesotho due to the long standing labour relationship between the two economies. This has potential to affect Government budgetary position and the country's balance of payments.

In spite of this, the Committee expects recovery in the coming months, driven by expansionary policy responses undertaken across the globe. The group of 20 countries (G20) resolved at its meeting in April 2009 to augment efforts to support developing countries weather the crisis. The African Union summit recently completed in Libya identified agriculture as a key alternative for sustainable development. The Committee will continue to monitor the domestic economic developments to ensure stability in these challenging times, and facilitate recovery.

2. Inflation Developments

In contrast to developments in international oil prices, inflation rate maintained a downward trend observed in recent months. It measured 8.9 per cent in May, due mainly to the overall slowdown in food and non-food prices. However, the Committee was cautious about the overall inflation developments in the coming months consequent to episodes of international crude oil price increases. Crude oil was trading at over US$60 per barrel at the time of the meeting compared with US$50 per barrel observed during the previous meeting.

The Committee took note of inflation developments in SA, which continued to be above the target range of 3 to 6 per cent. Inflation, measured by the re-weighted and reconstituted consumer price index for all urban areas, increased to 8.0 per cent in May 2009. Food prices inflation declined from 13.6 per cent to 12.1 per cent during the same period, but remained the main contributor to the inflation outcome. Housing and utilities inflation became the second largest contributor to the outcome, mainly due to a 29.6 per cent increase in electricity prices and a 15.1 per cent rise in the cost of maintenance and repairs. However, deflationary pressures are also present, as evidenced by producer price inflation, which fell by 3.0 per cent in May. In its meeting held on 24th to 25th June 2009, the South African Reserve Bank's Monetary Policy Committee decided to keep its key interest rate, the repo rate, unchanged at 7.5 per cent in line with conditions prevailing in the global and domestic economy.

3. Prospects for the Maintenance of Price Stability

a. Balance of Payments

The exchange rate of the loti fluctuated against the US dollar between the range of about R7.85 and R8.25 since the previous meeting of the MPC. However, the Net International Reserves (NIR) remained adequate to underwrite the fixed exchange rate system due to positive net financial inflows in the balance of payments. NIR was recorded at US$893.19 million at the end of June 2009, compared with the narrow money (M1) worth US$537.73 million. This is equivalent to 1.7 per cent coverage of M1 in circulation.

The global downturn has resulted in a significant decline in Lesotho's exports mainly diamond and textiles in the first quarter of 2009. This has potential to result in a deficit on the current account of the balance of payments. However, external debt service for April and May 2009 was relatively low at US$3.8 million and US$1.8 million, respectively.

The outlook for the global economy could remains under pressure for most of the year before slowly recovering. Therefore, accumulation of foreign reserves is important for monetary policy in Lesotho to underwrite the fixed exchange rate arrangement with SA. This is particularly so with the observed shrinkage in export earnings and the higher Government liabilities on external debt.

b. Fiscal Balance Outlook

Government budgetary operations continued to support favourable macroeconomic environment. Nonetheless, the period realised some hiccups resulting from functional problems related to the newly introduced Integrated Financial Management Information System (IFMIS) of Government. As a result, Government expenditure in the coming quarter could increase once the system is running efficiently.

4. Monetary Policy Stance

While maintaining an import cover of no less than 5 months and observing movements in the exchange rates, the Committee decided to retain the NIR target range of US$ 500 million to US$550 million. At this level, NIR is deemed sufficient to underwrite the fixed exchange rate arrangement between the loti and the South African rand.

M.P. Senaoana (PhD)
GOVERNOR

07 July 2009

STATEMENT OF MONETARY POLICY COMMITTEE

1 September 2009

1. Introduction

At its 21st meeting held on 1st September 2009, the Monetary Policy Committee (MPC) of the Central Bank of Lesotho (CBL) discussed the latest monetary policy operations and inflation-related developments to ensure that the price stability mandate of the Bank is being met.

The Committee observed that the global economic contraction continued in the second quarter of 2009, albeit at a slower rate. Major economies such as the US, Euro area, and in the region, South Africa, shrank by less than half the rates observed in the first quarter of the year. In addition, inflation pressures continued to fall, creating room for interest rate cuts by policy makers. Euro area and South African key interest rates were reduced by 50 and 200 basis points, respectively, between March and June 2009. South Africa reduced its key interest rate further to 7.00 per cent on 14 August 2009. The key interest rate in the US was held constant at 0.25 per cent during the same period.

However, unemployment levels continued to worsen in most countries across the globe. This indicated that the return to full recovery in real global economic activity, which requires a turnaround in incomes and improvement in credit worthiness of households in worsely affected major economies, could take some time.

The domestic economy showed signs of partial improvement in the second quarter of 2009. Diamond mining production increased more than two fold, boosting exports and the current account. It was influenced by a 15 per cent rise in the average price of rough diamonds during the second quarter of 2009. Domestic consumption of electricity also rose by 17 per cent on a quarterly basis, partly as a result of an increase in electricity consumption during the winter season. The number of imported motor vehicles declined slightly. However, textile manufacturing continued to suffer from the fall in incomes in the US. Exports of textile and clothing declined by 8.6 per cent in the second quarter and employment in the manufacturing sector fell by 1.0 per cent. Imports of petroleum products also declined by 30.2 per cent, despite the generally steady trend of domestic fuel prices in the quarter ending June 2009. Employment in the government sector improved moderately while mine workers employment declined by 2.8 per cent to 47,354 workers.

2. Inflation Developments

Inflation continued on a downward trend, registering 8.1 per cent at the end of June 2009 from 8.9 per cent in May. The decline in the inflation rate reflected a broad slowdown in price increases of various items. Both the food and non-food components of inflation declined between May and June. The food component recorded an increase of 11.3 per cent in June from 12.1 per cent in May. Bread and Cereals; fruits and vegetables; as well as milk and eggs categories fell, while the meat component increased. It is worth noting that the slowdown in inflation in the region is sluggish compared with developments in major economies such as the US and Euro area, which are experiencing a decline in the general price level.

The decline in the domestic inflation rate was in line with decreases in inflation rates of other Common Monetary Area (CMA) countries. Namibia's inflation rate fell to 9.1 per cent in June 2009, the highest rate in the region; Swaziland's inflation rate declined in line with Lesotho's to 7.9 cent while South Africa's inflation rate dropped to 6.9 per cent.

3. Prospects for the Maintenance of Price Stability

a. Balance of Payments

The rebound in diamond exports strengthened the balance of payments position, leading to a higher current account surplus and an improvement in the Net International Reserves (NIR) position of the Central Bank. NIR rose to US$976.1 million at the end of July from US$893.2 million in June due mainly to receipt of SACU revenue quarterly payment. These overshadowed the decline in textile and clothing exports on balance of payments.

b. Fiscal Balance Outlook

Preliminary estimates indicated that government budgetary operations realised a large surplus in the second quarter of 2009. The surplus was mainly influenced by expenditure slowdown resulting from capacity constraints in operating the newly introduced Integrated Financial Management Information System (IFMIS) of Government. The Committee expects government expenditure to pick up in the coming quarters when the system is running as expected.

4. Monetary Policy Stance

The Committee was satisfied with the performance of the NIR and decided to retain the NIR target range of US$500 million to US$550 million. At this level, NIR is deemed sufficient to underwrite the fixed exchange rate arrangement between the loti and the South African rand. The Committee noted that the recovery in diamond exports was encouraging, while muted activity in the textile manufacturing sector and pending catch-up in government expenditure could limit further growth in the NIR level.

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GOVERNOR

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Statistical Tables