

Utilities Tariffs are Revised Upwards

The water and electricity utility companies announced increases in their tariffs in April...

Background

It is now normal for utility companies in Lesotho to review their tariffs in April. This is partly to ensure that tariffs in the country remain commercially viable. The significance of April month is because it is the beginning of the financial year. The recent increases in water and electricity tariffs are occurring at the time when the region is undergoing through an inflationary episode driven mainly by the continued increase in the price of Brent crude oil. Hence it is important to understand their implications on economic growth and poverty reduction.

As discussed below the electricity distribution in the country is regulated by the Lesotho Electricity Authority (LEA) from which operators in the sector are required to apply for any changes in the pricing structure. During the month, LEA has approved increases of Lesotho Electricity Corporation (LEC) electricity charges for 2008/2009. Table 1 below shows the increases in LEC energy charges. The tariff for street lights registered the highest increase of 18.9

per cent followed by domestic with 15.8 per cent.

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The charges for both Industrial and commercial heavy voltage (HV) customer categories increased by 14.6 per cent while those for low voltage rose by 14.0 per cent. The tariffs for the general purpose category which includes churches, schools and health centres was not increased. The increases in the oil prices in international markets appears to have a feed through effect onto the operations and maintenance costs of the Corporation.

As relates to water tariffs, the Water and Sewage Authority (WASA) announced an average tariff increase of 6.3 per cent for domestic customers and 19.5 per cent for non-domestic customers. Non-domestic consumers include industries, businesses, government and schools. Standing charge rose by more than seven-fold and forty-seven fold for domestic and non-domestic customers, respectively. The higher increase in standing charges is attributable to, among others, high costs incurred by WASA in modernising billing systems including the introduction of the pre-paid metering. Furthermore, WASA has increased its fleet in order to ensure

proper maintenance. Therefore, the maintenance costs associated with the operations have increased. In addition, WASA has also expanded its operation to include, *inter alia*, Maseru peri-urban water supply (phase I and Phase II). These phases comprise of storage reservoirs, pumping stations, main transmissions, reticulation pipes and house connections. The projects are financed or sponsored by external sources such as the Arab Bank for Economic Development of Africa (BADEA) and Organisation for Petroleum Exporting Countries (OPEC) and the Government of Lesotho.

Table 1: Approved LEC Energy Charges for 2008/09 Fiscal Year

	Previous energy charge (M/kwh)	Approved energy charge (M/kwh)	% changes
Industrial HV	0.074	0.0848	14.6
Industrial LV	0.0819	0.0934	14
Commercial HV	0.074	0.0848	14.6
Commercial LV	0.0819	0.0934	14
General Purpose	0.68	0.68	0
Domestic	0.49	0.5675	15.8
Street lighting	0.269	0.32	18.9

Source: Lesotho Electricity Authority (LEA)

These tariff increases should be compared with the annual average inflation rate of 7.9 per cent registered in 2007. Over the previous years, water and electricity prices have always been increased by almost the rate of inflation.

However, operational and maintenance cost emanating from the high international oil prices seemed to have been the major reason that led to the premium above inflation.

Table 2: Increases in Water Tariffs

	Previous rates (Maloti/1000 litres)	New rates (Maloti/1000 litres)	% change
Domestic Customers			
Standing Charge	3.13	22.41	615.9
<i>Band</i>			
A. 0 to 5 kilolitres	2.07	2.19	5.8
B. 5 to 10 kilolitres	3.46	3.71	7.2
C. 10 to 15 kilolitres	6.14	6.52	6.2
D. Above 15 kilolitres	8.48	8.99	6.0
Non Domestic Customers			
Standing Charge (per month)	3.13	149.26	4668.6
Industries, business, government	4.94	5.93	20.0
Schools, churches	4.94	5.88	19.0

Source: WASA (April 2008)

Structure of Utilities Sector in Lesotho

Electricity and water sub-sector play a significant role for economic growth in Lesotho. The sub-sector accounted for an average 6.0 per cent of real Gross Domestic Product (GDP) during the period 2002 - 2006. It registered an average growth rate of 6.4 per cent during the same period. This is above the average overall GDP growth rate of 4.0 per cent registered during the same period.

It is important to evaluate the market structure of this sub-sector when addressing the question of pricing. This is partly because of the capital requirement that water and electricity utilities are monopolistic. As relates to the electricity distribution, a number of reforms have been effected in an effort to improve the efficiency of the sub-sector. A management contract was effected during 2001 to 2006 to turn around LEC which is the only operator in the electricity distribution. In addition, a regulatory authority, LEA was

established in 2004 to regulate the electricity sub-sector.

In the water sub-sector, WASA is the only operator in the distribution and is regulated by the Commissioner of Water Affairs. There are efforts to further reform the market structure in the sub-sector by establishing the regulatory authority to regulate water. The proposal is to house both water and electricity regulation together.

Implications of the Recent Increase

The recent increases in water and electricity tariffs are likely to have negative effects on the manufacturing sub-sector. The sub-sector is dominated by 'wet' industries' due to their high usage water. There is evidence that following wages, the cost of water and electricity is the major cost driver in the manufacturing of textiles. In addition, these increases are occurring at the time when the sub-sector faces stiff

external competition from low cost producers such as China and India coupled with the general global economic slowdown.

The households are also likely to be affected by the increase in basic utilities. With inflation rate at 9.5 per cent in April, households' budgets are likely to be constrained. Under these conditions,

it is expected that in the next round of wage negotiations, the trade unions are likely to bargain for higher wage adjustments. This would worsen the high costs already faced by the domestic production units. However, it is important that LEC and WASA remain commercially viable.

2. Continuous Increases in Fuel Prices Impact on Road Transportation Fares

Background

During the month of April, the Lesotho Road Transport Board announced new fares for public transport throughout the country. On average, public transport fares rose by 22 per cent. The main input in the transportation sub-sector is liquid oil based fuel.

Table 4 shows the prices of petrol, diesel and illuminating paraffin for the first four months of 2008. The prices

have risen every month since the beginning of the year. This has been mainly because international prices of crude oil has increased significantly over the last five years and it breached a US\$100 level in January 2008. The domestic prices of petroleum products although controlled, also followed the trend in international oil prices.

Table 3: Road Transport Board Fares-Maseru Urban Area (Maloti)

Mode of Transport	Old Fare	New Fare	% change
4 + 1	3.2	4	25
9 – 18 Seats (Mini-Buses)	3	3.5	16.7
19 – 90 Seats (Buses)	2	2.5	25

Source: Road Transport Board (April 2008)

**Table 4: Lesotho Fuel Price Changes for January to April 2008 in the Lowlands
(Units: Maloti per Litre)**

Date	Petrol (Leaded/unleaded)	Diesel	Illuminating Paraffin
18 January 2008	7.20	8.10	5.70
15 February 2008	7.40	8.20	5.80
14 March 2008	8.05	9.00	6.45
11 April 2008	8.65	10.30	7.60

Source: Lesotho Petroleum Fund Board (Various Reports)

Public road transport in Lesotho is regulated by the Road Transport Board. The Board, *inter alia*, determines the pricing structure, approval of road transport licenses for taxi/bus owners and allocation of routes.

Increases in petroleum prices have adversely affected the profitability of the

taxi/bus industry on the one hand. On the other hand, the standard of living of the majority of low and middle income earners has also lowered significantly as they rely heavily on public transport to commute to their respective work-stations within the country.

3. Lesotho Road Fund Revised Toll Gate Tariffs Upwards

Background

The Road Fund (RF) commercialises the road construction and maintenance by shifting the responsibility from the Government to beneficiaries (road users) on a fee-for-service basis. The RF collects revenue from road maintenance levy charged on petrol prices and diesel, and road toll gate fees. Fines on overloaded Toll gate fees are the second largest source of revenue collected by the RF. Other sources of revenue include licence fees on motor vehicles .

Prior to April 2008, revenue collected from toll gate tariffs accounted for 37 per

cent of the total road fund revenue. The toll gate fee tariffs have been increased effective from the 1st April 2008. The adjustments are meant to mitigate the impact of the escalating road maintenance costs. The increases in toll gate tariffs are expected to raise toll gate revenue collection to 60 per cent of total road fund revenue.

Toll gate revenue collection was introduced in Lesotho in 1976. Table 5 depicts price increases in toll gate tariffs from 1976 until 2001 while table 6 compares the newly introduced 2008 rates to those of 2001.

Table 5: Increases in Toll Gate Tariffs (1976 – 2001)

	1976	1988	2001
Light Motor Vehicles	M0.2	M2.00	M5.00
Medium, Heavy and extra heavy vehicles	M1.00	M6.00	M15.00

Source: Lesotho Road Fund (April 2008)

Table 6: Increases in Toll Gate Fee Tariffs

	Previous rate - 2001 (Maloti)	New Rate - 2008 (Maloti)	% change
Light Vehicles (motor cycles, cars, vans & combis)	5.00	20.00	300.00
Medium Vehicles (Land Rovers, Q7, X5, Land Cruisers, Medium Buses and Half Trucks: 4 – 6 wheels)	15.00	40.00	166.67
Heavy Vehicles (Large Buses and Goods Vehicles: 6 – 10 wheels, 20 and 3 Axle)	25.00	60.00	140.00
Extra Heavy and Super Link Vehicles (Large Goods Vehicles and Large Buses with Trailers: 10+ wheels, 4 Axle)	25.00	140.00	460.00

Source: Lesotho Road Fund (April 2008)

Table 6 depicts that the toll gate fee tariffs at the border gates have increased tremendously in 2008 to cover the years from 2001. The toll gate fee tariff has increased six-fold for extra heavy and super link vehicles. The tariff for light motor vehicles has also increased significantly. However, regional comparisons show that the current rates are still low given the fact that in countries such as Swaziland and

Botswana, light motor vehicles are charged E50.00 and P60.00 at the border gates, respectively as at 31st March 2008. In South Africa on N1 highway from Lesotho to Johannesburg, there are two toll gates and light motor vehicles are charged R10.00 (Kroonvaal toll gate) and R32.00 (at Grasmere toll gate). Hence the total value that a light motor vehicle pays en-route to Johannesburg is R42.00.

4. Monetary Policy Operations for April 2008

The Central Bank's objective of maintaining price stability is attained through the maintenance of an adequate level of foreign reserves and fighting domestically generated inflation. As such, the Bank has adopted reserve money as its operating target, interest

rates of treasury bill as intermediate target and net foreign assets as its ultimate target. Against the background of net increase in overall liquidity during the period under review, efforts continued to focus on absorbing the excess liquidity in the economy.

Table 7: Treasury Bill Auctions

Type of Security	Auction Date	Maturity Date	Auction Amount (million)	Amount Issued (million)	Discount Rate	RSA Disc. Rate
91-day TBs	02-Jan-08	04-Apr-08	M150.0	M150.0	9.10%	10.52%
182-day TBs	09-Jan-08	11-Jun-08	M30	M24.8	10.45%	10.47%
91-day TBs	30-Jan-08	02-May-08	M150.0	M150.0	9.17%	10.37%
91-day TBs	05-Mar-08	06-Jun-08	M150.0	M150.0	9.21%	10.26%
182-day TBs	12-Mar-08	12-Sep-08	M20.0	M20.0	10.45%	10.41%
91-day TBs	02-Apr-08	02-Jul-08	M150.0	M150.0	9.71%	10.04%

Success of the CBL in achieving its monetary policy objectives could be assessed by monitoring the movement of the intermediate target (treasury bill rate) against trends in the region. A successful policy would result in a treasury bill rate that moves in line with comparable rates in the region, given the free movement of funds within the CMA region, to avoid undesirable capital flight or costly accumulation of foreign funds.

As Figure 1 shows, 91-day treasury bill rates in Lesotho and South Africa have generally been at a steady upward trend

in the recent months, with the Lesotho rate lower than South Africa's by less than two percentage points. However, the South African rate declined for the third consecutive month in April while the rate in Lesotho showed a steep increase. This resulted in a narrow margin of 33 basis points from 105 after the March auction. In the period covered by the graph, the margin reached a peak of 161 basis points after the November 2007 auction. The graph indicates that Lesotho's rate has been moving in line with rates in the region, and its level remains competitive.

Figure 1: Measuring the Success of Monetary Policy Objectives

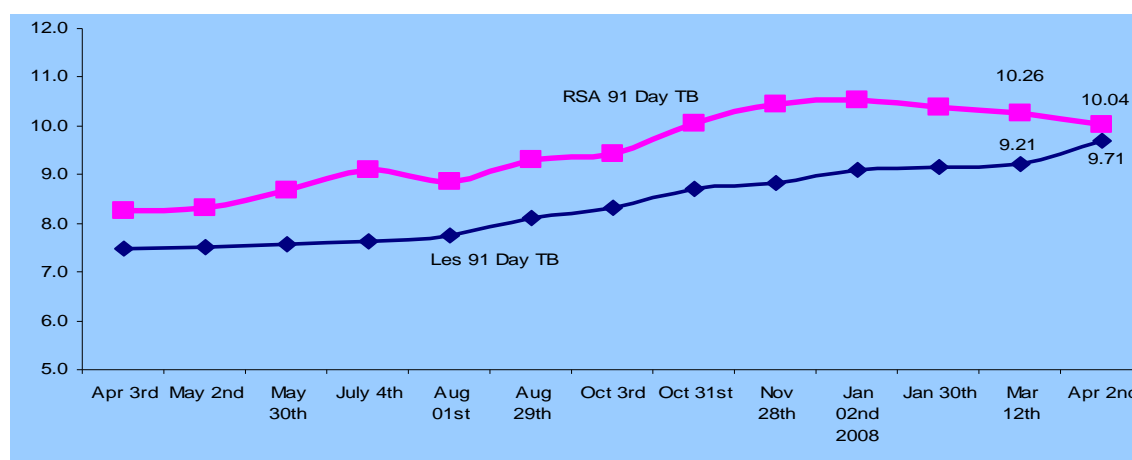


Table 8: Selected Monetary and Financial Indicators

	2008		
	Feb	March	April
1. Interest rates (Percent Per Annum)			
1.1 Prime Lending rate	15.42	15.67	15.92
1.2 Prime Lending rate in RSA	14.50	14.50	14.50
1.3 Savings Deposit Rate	4.57	4.57	4.57
1.4 Interest rate Margin(1.1 – 1.3)	10.85	11.10	11.35
1.5 Treasury Bill Yield (91-day)	9.17	9.21	9.08
2. Monetary Indicators (Million Maloti)			
2.1 Broad Money (M2)	4285.60	4176.62	4591.71
2.2 Net Claims on Government by the Banking System	-3646.22-	-3273.76	-4049.23
2.3 Net Foreign Assets – Banking System	9165.58	9258.58	10151.90
2.4 CBL Net Foreign Assets	7521.07	7560.44	8048.03
2.5 Domestic Credit	-2305.81	-1933.78	-2689.44
2.6 Reserve Money	457.01	427.35	489.40
3. Spot Loti/US\$ Exchange Rate (Monthly Average)	7.6707	7.9741	7.7769
4. Inflation Rate (Annual Percentage Changes)	10.6	10.7	9.5
5. External Sector (Million Maloti)	2007		2008
	QIII	QIV	QI
5.1 Current Account Balance	440.15	328.39	517.63
5.2 Capital and Financial Account Balance	248.60	-83.21	310.40
5.3 Reserves Assets	-870.86	-116.19	-774.19

+ These indicators refer to the end of period. Prime and deposit (savings) rates are averages of all commercial banks' rates operating in Lesotho. The Statutory Liquidity Ratio in Lesotho is 25 percent of commercial banks' short-term liabilities

Table 9: Selected Economic Indicators

	2004	2005	2006	2007+
1. Output Growth(Percent)				
1.1 Gross Domestic Product – GDP	4.2	2.9	7.2	5.1
1.2 Gross National Product – GNI	7.9	5.5	3.1	4.9
1.3 Per capita –GNI	7.9	5.5	3.1	4.0
2. Sectoral Growth Rates				
2.1 Agriculture	-1.9	-1.7	1.7	-39.3
2.2 Manufacturing	2.1	-8.6	10.5	11.0
2.3 Construction	-4.4	-3.4	0.6	3.5
2.4 Services	2.1	4.1	6.6	6.3
3. External Sector – Percent of GNI				
3.1 Imports of Goods	86.3	83.1	80.1	86.5
3.2 Current Account	-4.7	-5.7	3.5	9.5
3.3 Capital and Financial Account	5.8	3.6	0.7	8.2
3.4 Official Reserves (Months of Imports)	5.2	5.5	6.7	7.6
4. Government Budget Balance (Percent of GDP)	5.7	4.8	11.8	5.3

* Preliminary estimates

+CBL Projections